Reciprocity of the macroprudential measure imposed by the National Bank of Belgium

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Taking into consideration the regulatory framework in force, on 21 January 2016, the National Bank of Belgium (NBB) notified the European Systemic Risk Board (ESRB) of its intention to extend the application of the macroprudential measure imposed in 2014, under Article 458 of the CRR, which materialized in an increase of the minimum capital requirements associated with mortgage credit[1] whose collateral is located in Belgium. This measure was only addressed to the institutions using the Internal Ratings Based (IRB) model for the calculation of the minimum capital requirements. Simultaneously, taking into consideration the entry into force of Recommendation ESRB/2015/2, the NBB asked the ESRB to issue a recommendation so that the other European Union (EU) Member States may reciprocate this measure. This recommendation was included in ESRB/2015/2 (Recommendation C of Section 1 and Annex) following the amendment introduced by Recommendation ESRB/2016/3.

Article 458 of the CRR provides for the adoption of a set of more stringent requirements to address systemic risk in one Member State. These requirements include inter alia the possibility of imposing a capital add-on on risk weights applied to exposures secured by mortgages on (residential or commercial) immovable property in order to prevent speculative bubbles in this sector.

Making use of this possibility, the NBB, the Belgian macroprudential authority, decided in March 2014 to impose a capital add-on on institutions using the IRB Approach for the calculation of minimum capital requirements.[2] The imposition of this measure was justified by the Belgian authority taking into account the following aspects:

- The fact that mortgage credit granted by Belgian financial institutions showed an increasing trend during the last 15 years, both in terms of stock and average amount of loan per agreement, as well as an increase in the average duration of loan agreements. This growth trend was only momentarily interrupted at the onset of the 2007 crisis;
- A sustained rise in the price of the immovable property collateralising this type of loan and concomitantly a reduction in households' ability ('affordability') to buy their own house as the annual average rise in house prices was higher than the average growth of Belgium's nominal GDP (particularly in the period between the second half of 2010 and the end of 2011);
- The exposure to the real estate sector represents approximately 15% of the Belgian institutions' portfolio, suggesting that price correction in the real estate sector, increasing unemployment, changes to the tax regime or the contagion resulting from changes in the economic environment elsewhere could give rise to losses in the Belgian banking sector;
- The existence, given the rising trend in real estate prices and hence their valuation, of reduced risk weights in Belgian institutions that use the IRB model (based on historical PD and LGD and therefore highly procyclical) compared to their European peers; and
- Insufficient capital buffers for potential losses in the real estate sector.

In light of the above, in the NBB's view, this measure would dampen growth of housing credit (and the rise in the price of real estate assets), resulting in risk weights of around 14.5%, in line with the European average.

After two years, the period set out in Article 458 (4) of the CRR to reassess the measure, the Belgian authority decided to extend its imposition, considering that the macroprudential or systemic risk had not materially decreased.[3]

The indicators presented below were calculated to assess the materiality of the Portuguese financial system's exposures to the risk identified by Belgium.

Indicators - Description	*Standard*+IRB	IRB
Mortgage credit granted directly or through branches to Belgium/Total assets of the Portuguese banking system	0,016 %	0,006 %
Mortgage Credit granted directly or through branches to Belgium/Total mortgage credit granted in Belgium	0,051 %	0,019 %

Source: FINREP – December 2015

The table shows that exposures to Belgium, in terms of the mortgage sector, are of low materiality compared with the Portuguese banking system's total assets. Materiality remains low conidering total mortgage credit granted in Belgium.

For Portuguese banking institutions as a whole, mortgage credit granted to Belgium reached 0.02% of total assets, dropping to 0.01%, when only taking into account the institutions that are authorised to use the IRB Approach for the calculation of minimum capital requirements.

Regarding mortgage credit granted in Belgium, exposures of Portuguese institutions reach 0.05%. This percentage falls to 0.019%, when only taking into account the institutions authorised to use the IRB Approach for the calculation of minimum capital requirements.

Note that there is no information available on credit granted to entities having their head office in Portugal whose collateral is located in Belgium.

Despite the low materiality of the financial services provided by the Portuguese banking system in Belgium, Banco de Portugal decided to reciprocate the measure as a matter of principle, as provided for in point 15 of Recommendation ESRB/2015/2.

This decision will remain in force as long as the measure applied by the NBB is in force, including any extensions under Article 458 (9) of CRR.

Considering that the measure imposed by the Belgian macroprudential authority is envisaged in the CRR (Article 458), reciprocation will be made through the same measure, i.e. by imposing an increase in minimum capital requirements associated with mortgage credit, for institutions that use the IRB model for the calculation of these requirements, with regard to credit granted, either through branches, or directly to Belgian entities, specifically credit whose collateral is located in Belgium.

Notes

[1] Add-on of 5 percentage points on risk weights resulting from the IRB model.

[2] This add-on had already been introduced through national legislation (in 2013), repealed with the entry into force of the CRR.

[3] This fact was also taken into consideration in the decision of the European Commission on its non-opposition to the extension requested by the Belgian authority.