
CNB press conference on the outcome of the autumn meeting on financial stability issues

Financial Stability Report – Autumn 2022

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30 November 2022



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- 1. Aggregate assessment of risks and overview of CNB's main measures**
2. Assessment of selected risks



Aggregate assessment of risks

- The global and domestic economies are facing increased risks to economic activity and price and financial stability:
 - Economic outlooks are being revised downwards.
 - Global inflation pressures, linked mainly with rising energy and food prices, persist.
- High commodity prices and tightening financial conditions are affecting the non-financial sector:
 - The debt servicing costs of non-financial corporations and households are increasing...
 - ...and, together with growth in corporations' input prices and households' living costs, are generating pressure on the financial soundness of these sectors.
- Government deficits and rising government debt are causing the sovereign exposures of domestic banks to rise and have the potential to increase systemic risk.
- Geopolitical and macroeconomic uncertainties are creating room for sudden and strong materialisation of previously accepted risks.

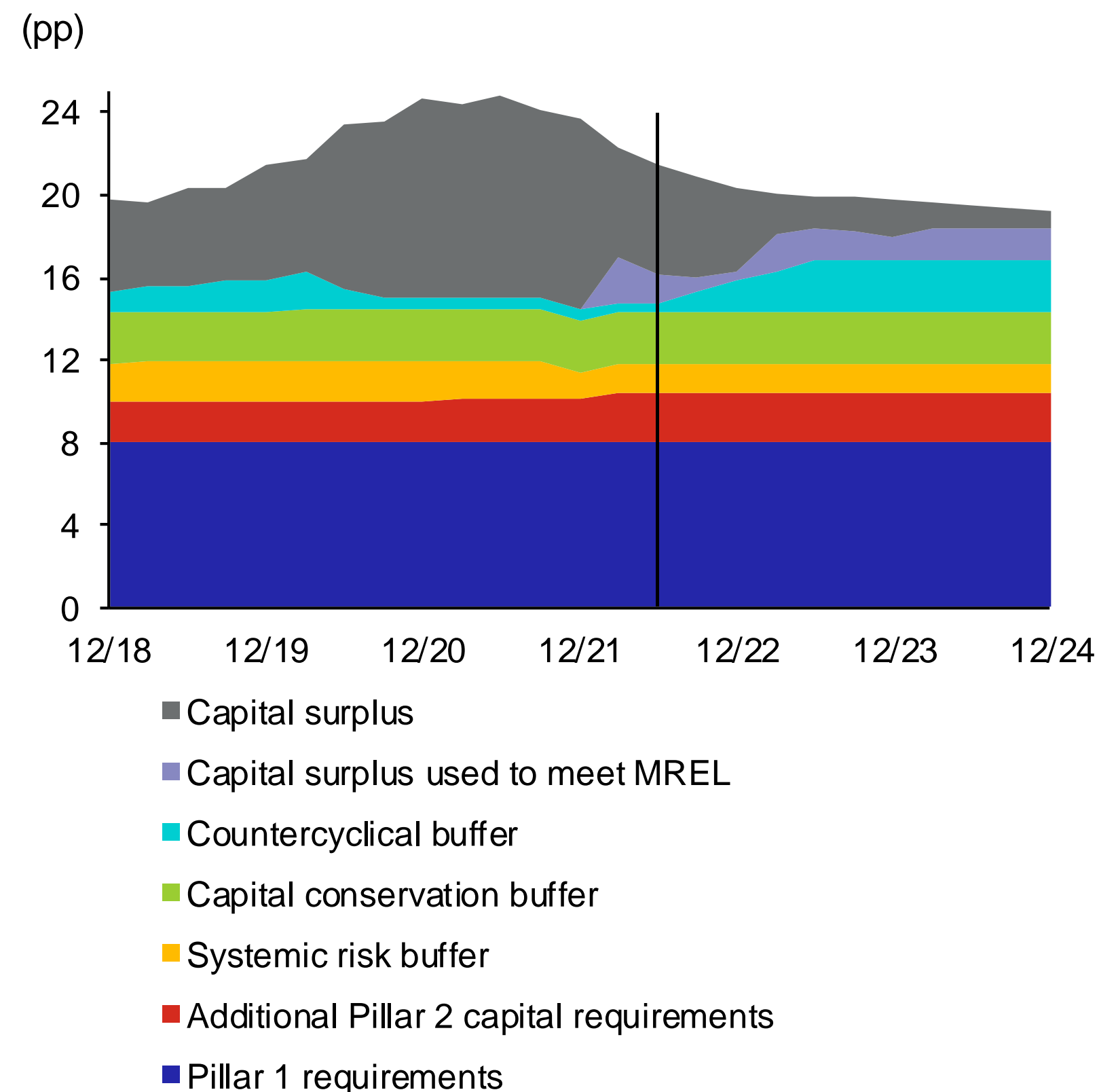
Financial stability in November 2022 (1)

- The Czech financial sector developed favourably in 2022, with most segments recording growth in assets and profitability.
 - Their resilience to shocks is based on a strong capital and liquidity position.
- The elevated risks to economic activity pose a threat of sizeable credit losses in the banking sector:
 - Government stabilisation and support measures are helping to reduce this potential threat...
 - ...as is the CNB's long-standing active policy in the area of capital buffers and credit ratio limits:
 - Capital buffers are strengthening banks' ability to cover credit losses.
 - The LTV, DSTI and DTI limits are reducing the accumulation of risks in banks' mortgage portfolios and enhancing households' ability to service their debt.

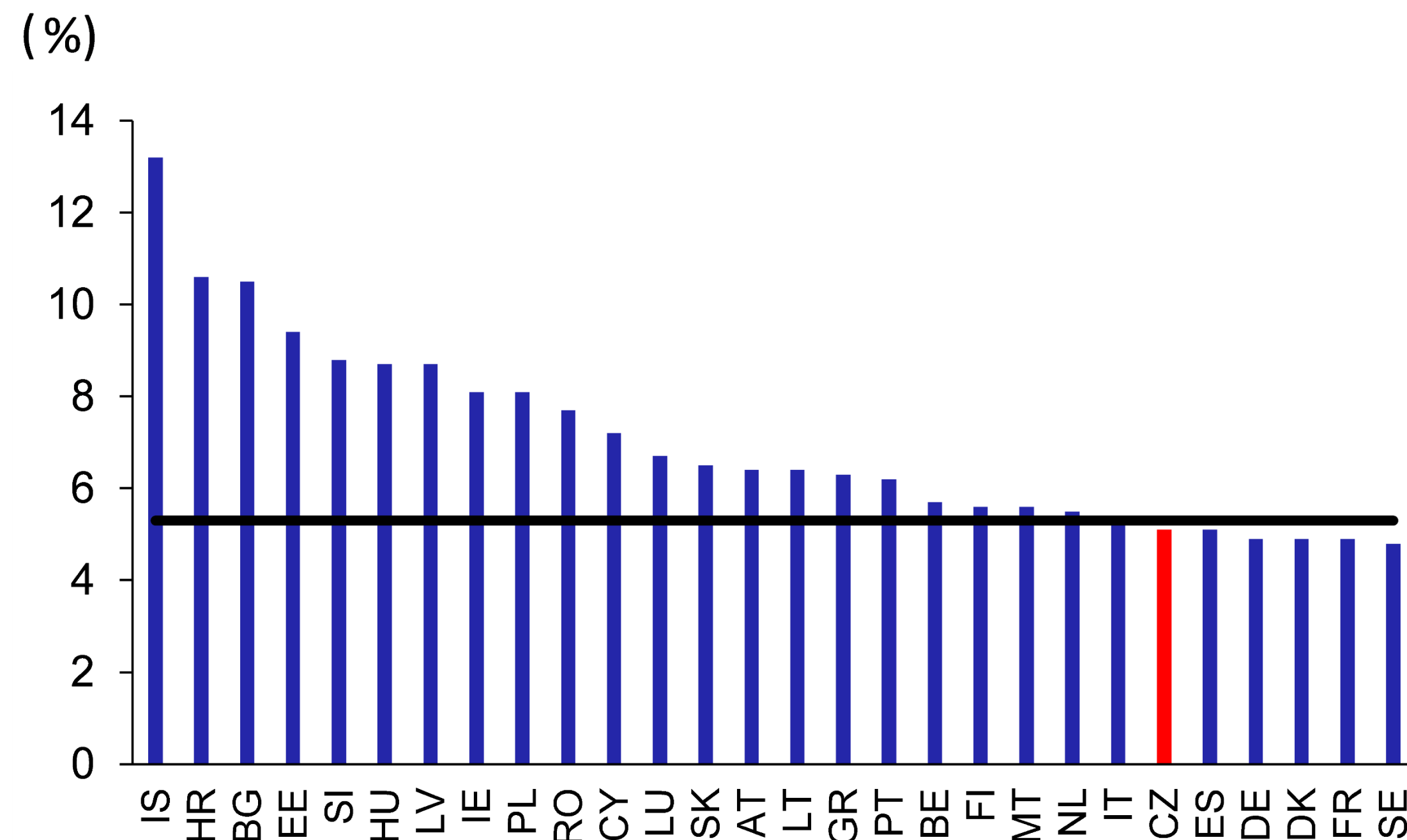
Financial stability in November 2022 (2)

- The **crucial banking sector** is highly resilient to adverse shocks.
 - Capitalisation remains very robust thanks to capital buffers and capital surpluses in excess of the regulatory requirements.

Structure of capital requirements in the domestic banking sector



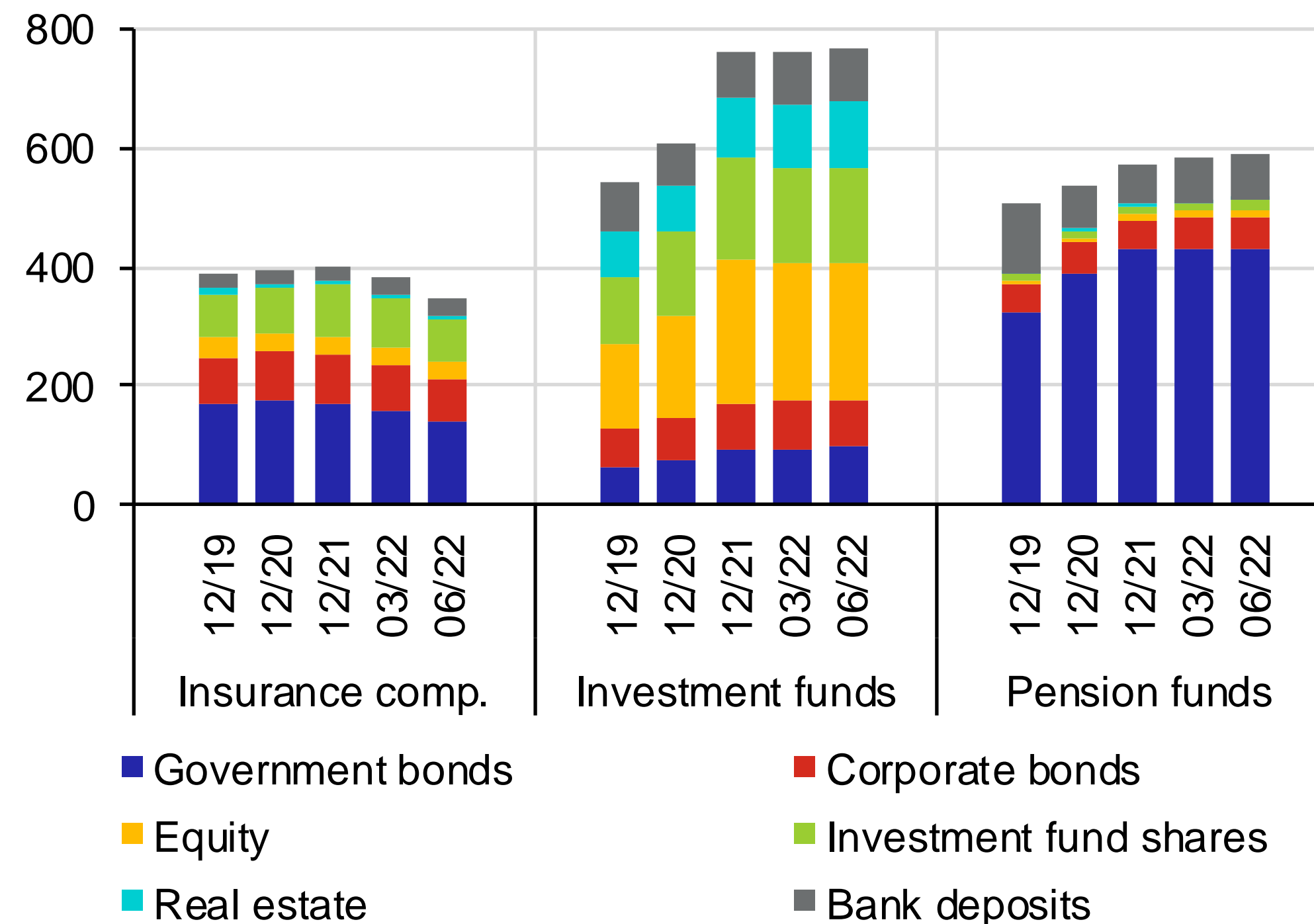
Leverage ratio (as of 2022 Q2)



Financial stability in November 2022 (3)

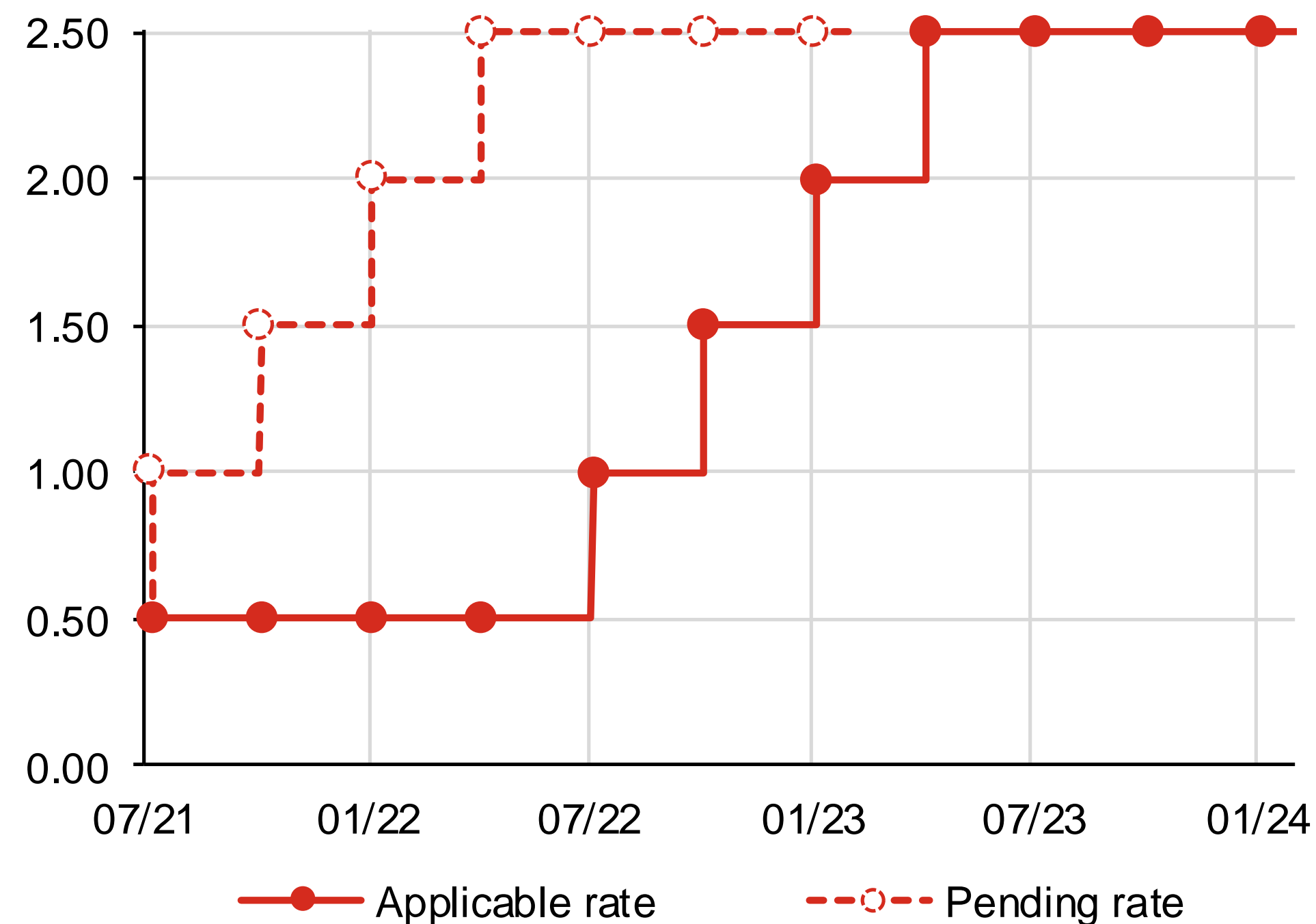
- The domestic **non-bank financial sector** is stable and resilient.
 - Persisting uncertainty on global financial markets and a potential decline/increased volatility of financial asset prices are the main **risks**.

Main components of domestic institutional investors' investment assets
(CZK billions)



Decision on countercyclical capital buffer rate (1)

Applicable and pending CCyB rate in the Czech Republic
(% of total risk exposure)



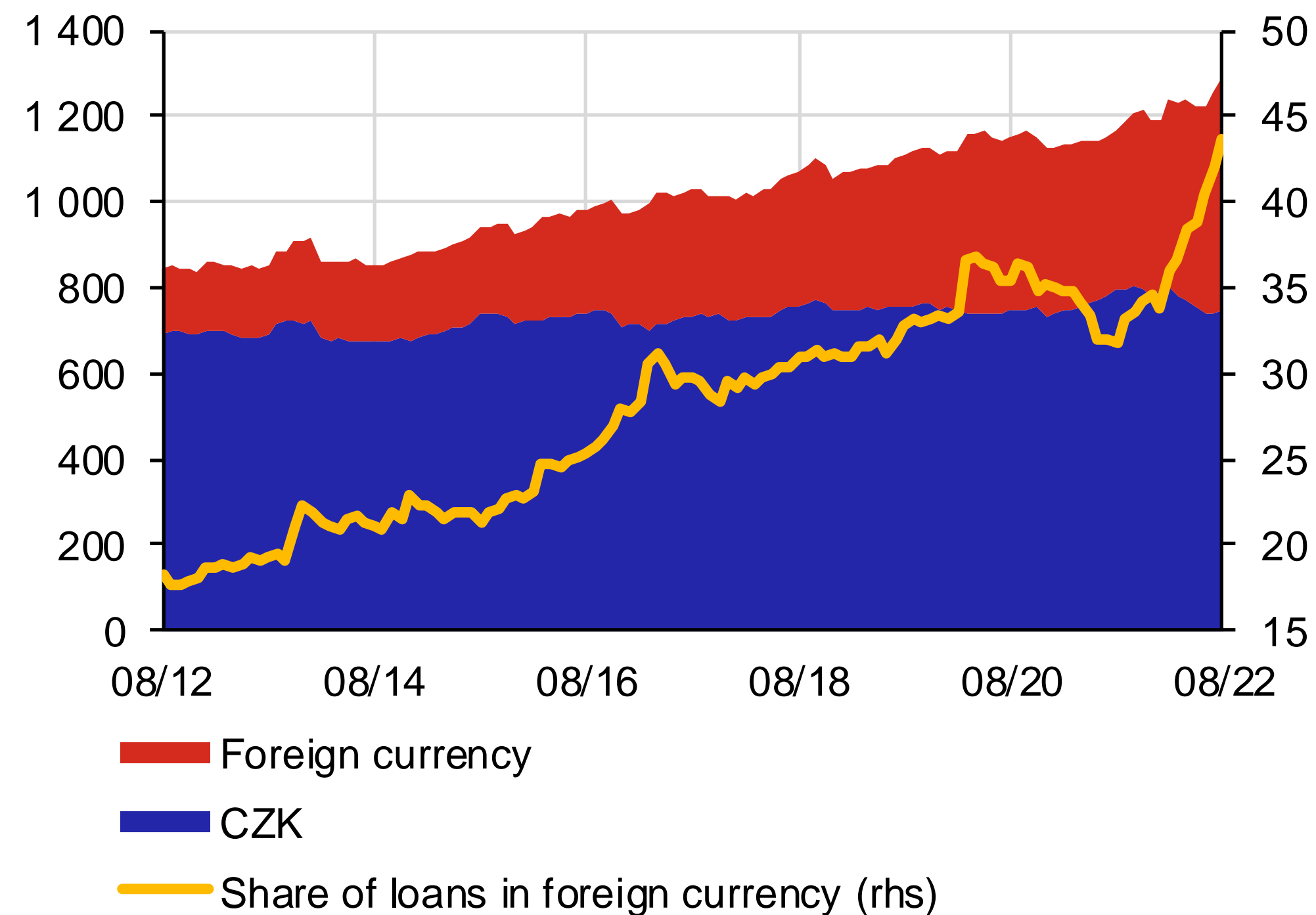
- **The Bank Board decided today to leave the countercyclical capital buffer (CCyB) rate unchanged at 2.5% with effect from 1 April 2023.**
 - Until then, the CCyB rate will rise gradually from the current level of 1.5%.
 - Should the economic situation worsen and significant credit losses form in the domestic banking sector, the CNB is ready to lower the CCyB rate or release the buffer fully in order to cover the losses and support banks' ability to provide credit to the real economy without interruption.

Decision on countercyclical capital buffer rate (2)

- The decision to leave the CCyB rate at 2.5% is a reaction to the high volume of previously accepted cyclical risks in the banking sector's balance sheet.
 - Additional risks are entering banks' balance sheets through growth in credit to non-financial corporations, especially foreign currency loans.

Loans to NFCs

(CZK billions, right axis: % of total loans to NFCs)

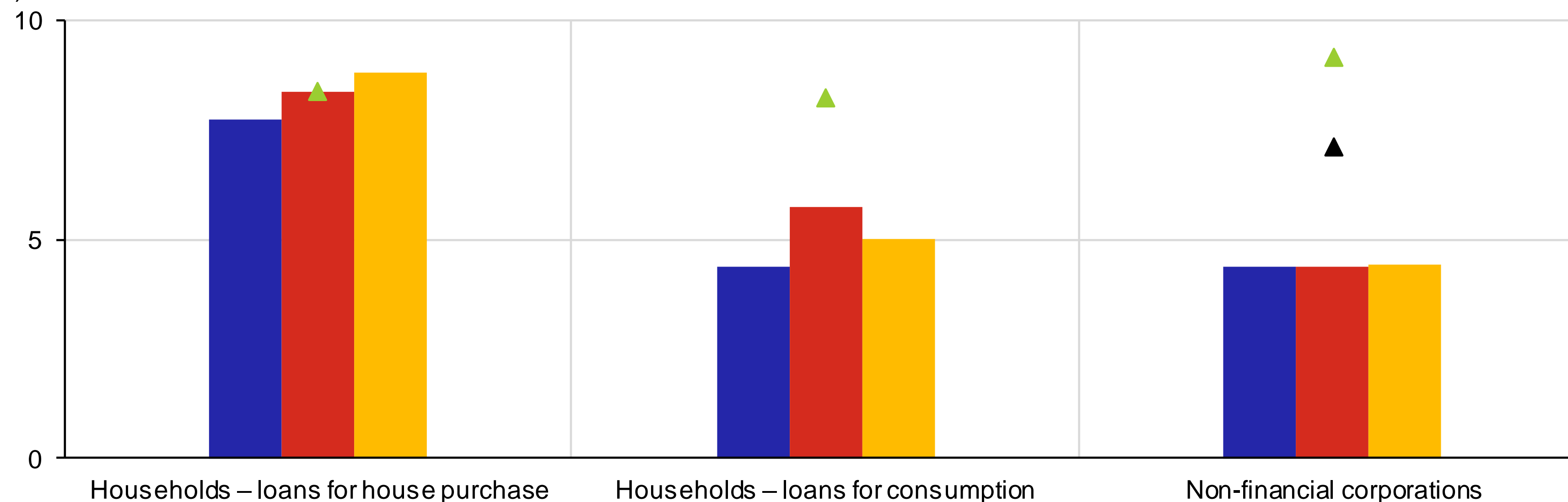


Decision on countercyclical capital buffer rate (3)

- Year-on-year growth in loans was still high at the end of September 2022.
- The Bank Board also took into account the current geopolitical and macroeconomic uncertainties, which create room for sudden and strong materialisation of previously accepted risks.

Average and current growth in bank loans to the private non-financial sector

(%)



■ Growth in loans – 10Y average

■ Growth in loans – 3Y average

▲ Year-on-year growth in 09/2022 (without 4 utility companies)

■ Growth in loans – 5Y average

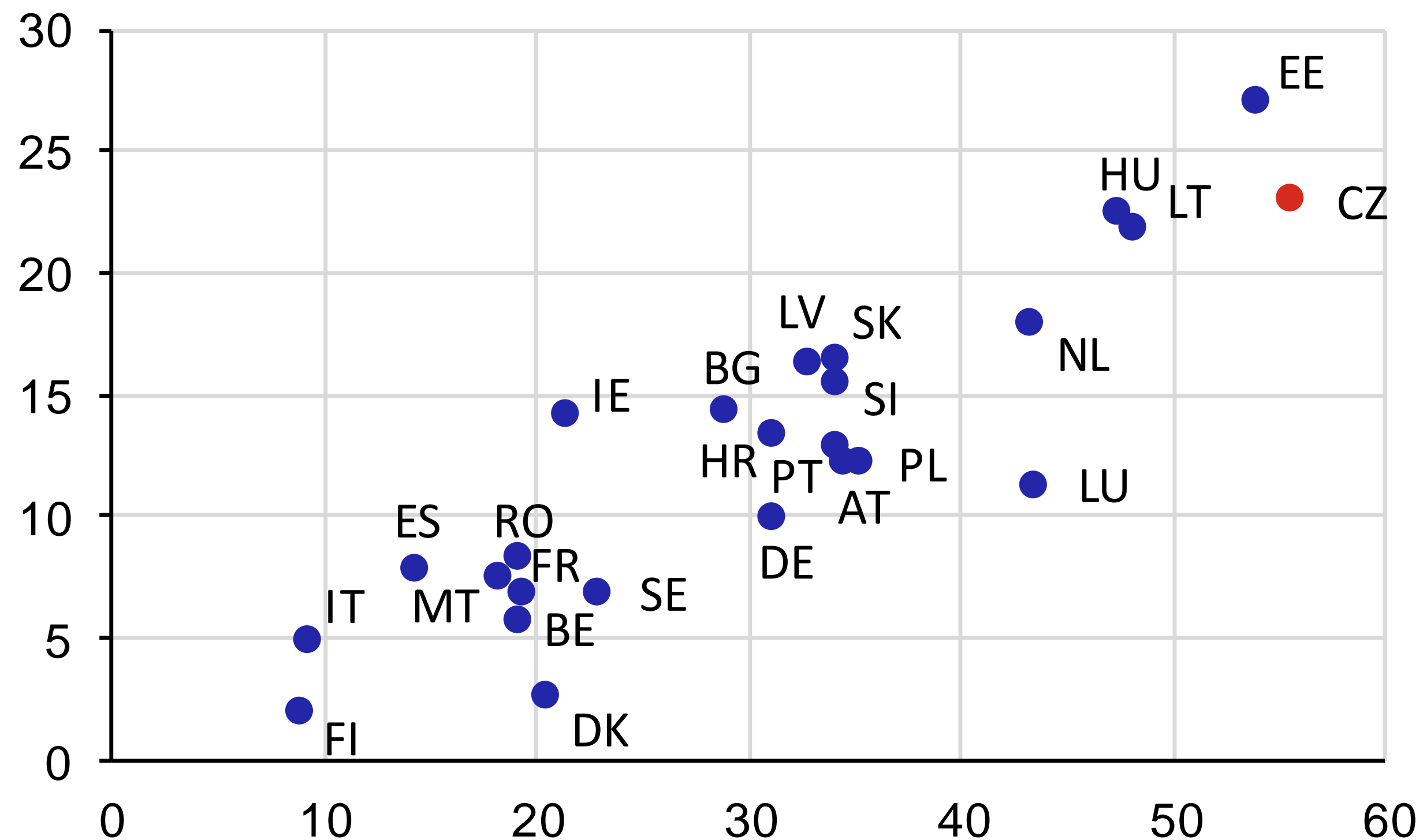
▲ Year-on-year growth in 09/2022

Property market and mortgage lending (1)

- House prices increased in all European countries in previous years.
 - The almost 60% three-year growth rate in the Czech Republic was the highest.

Residential property price growth in selected EU countries

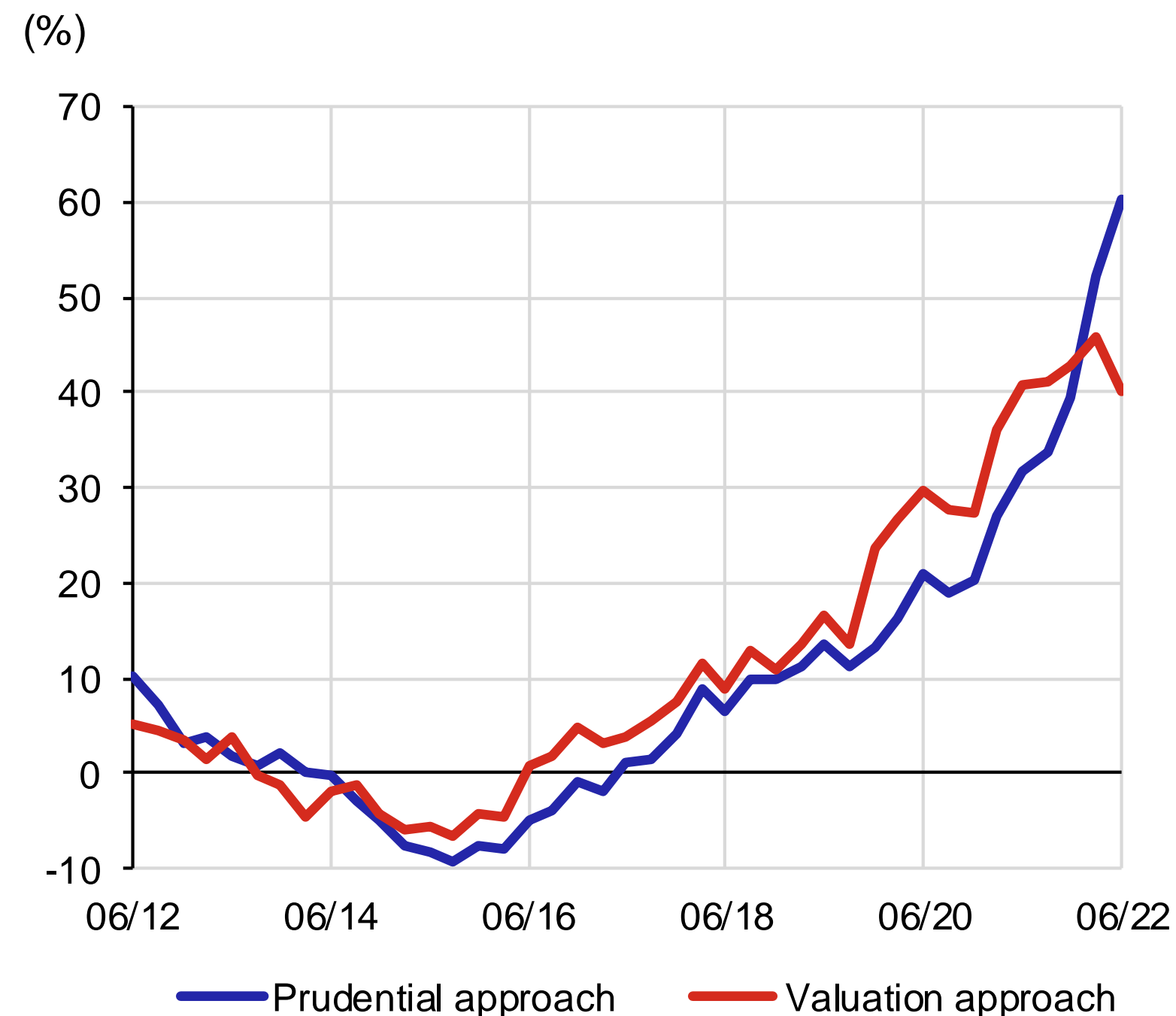
(%; x-axis: three-year growth; y-axis: one-year growth)



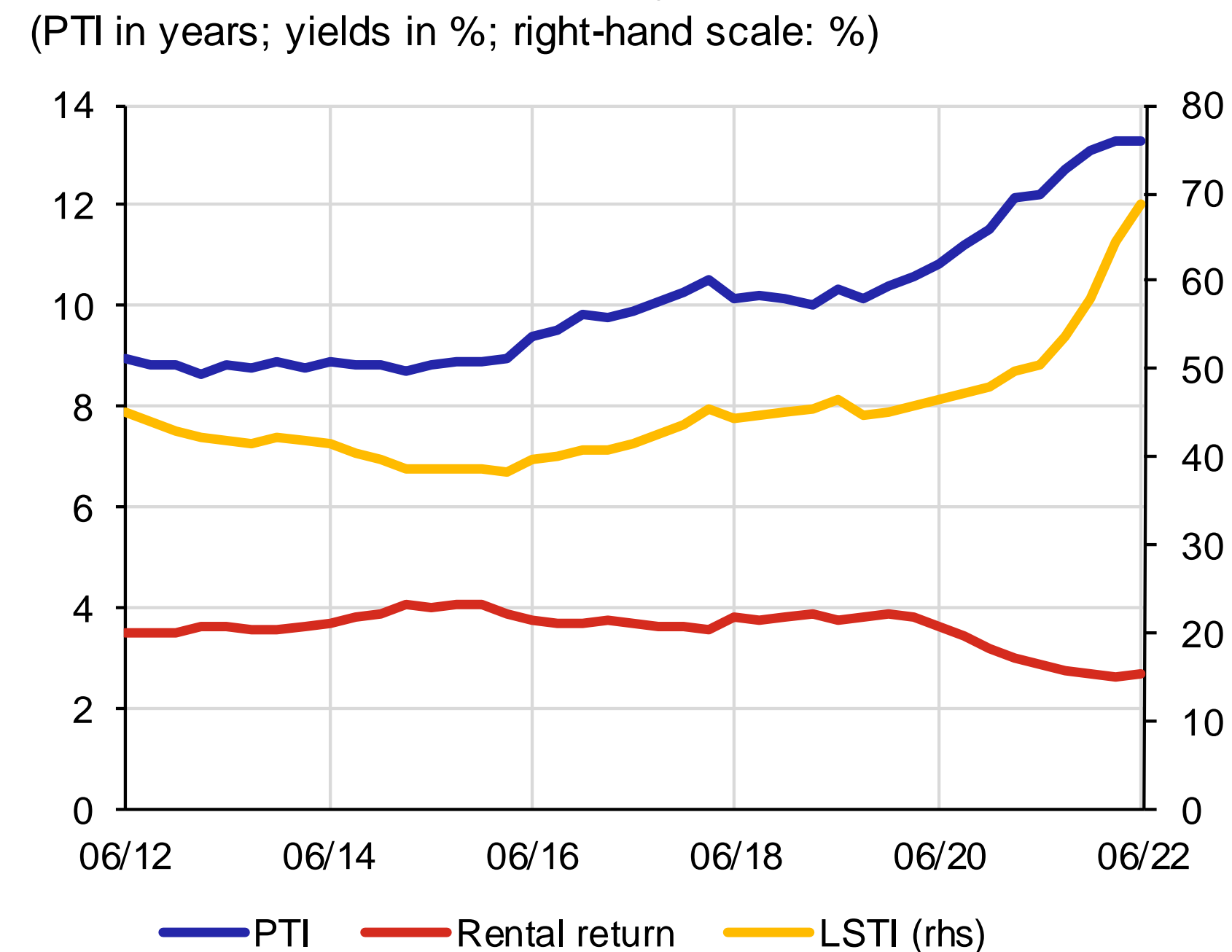
Property market and mortgage lending (2)

- The CNB estimates that apartments in the Czech Republic are overvalued by about 60% (20 pp more than at the end of 2021) for median-income households and by 40% for investors.
 - The share of households whose income allows them to safely debt-finance an average apartment at the given level of interest rates dropped below 10%.

Estimated overvaluation of apartment prices



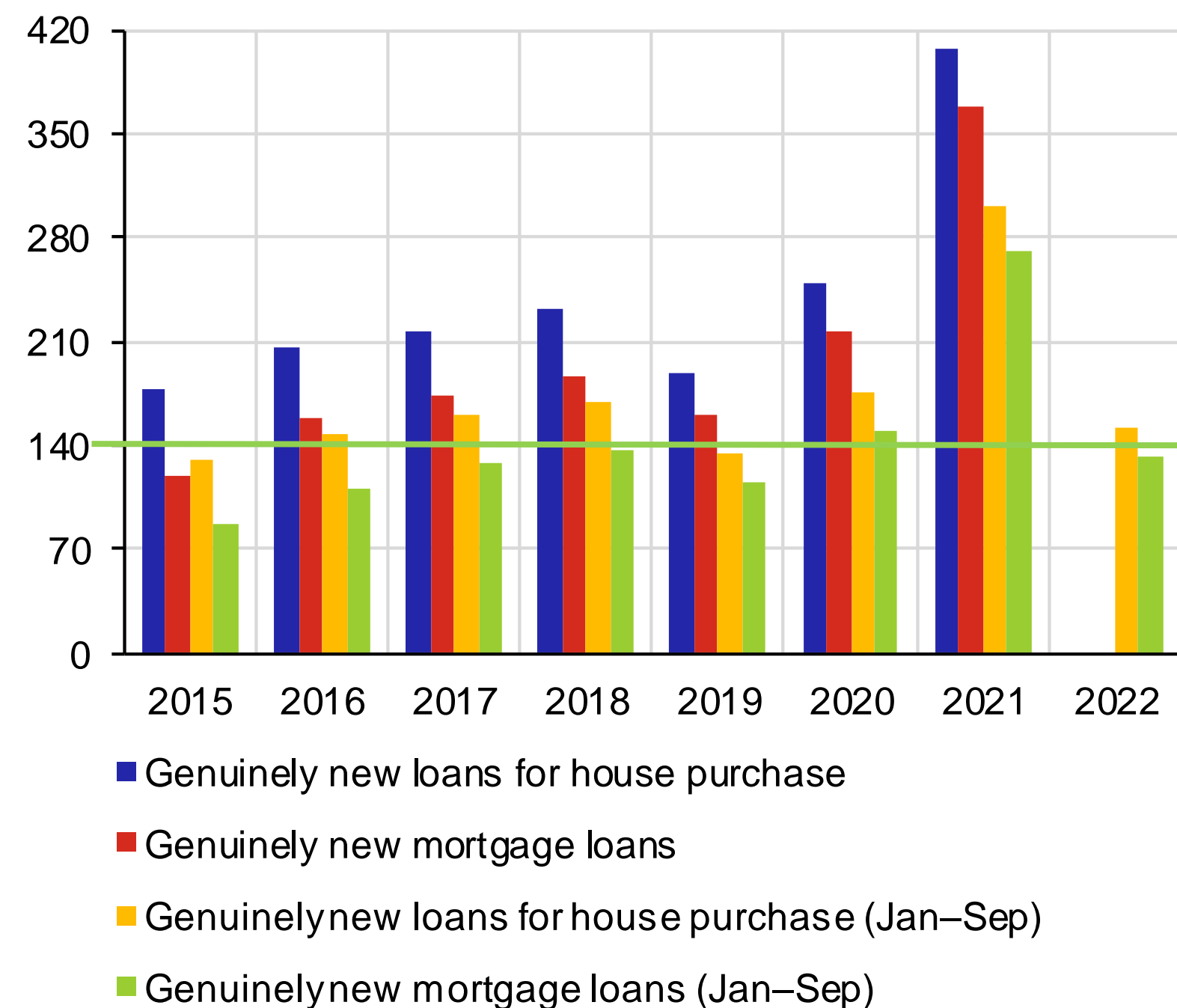
Selected apartment affordability indicators



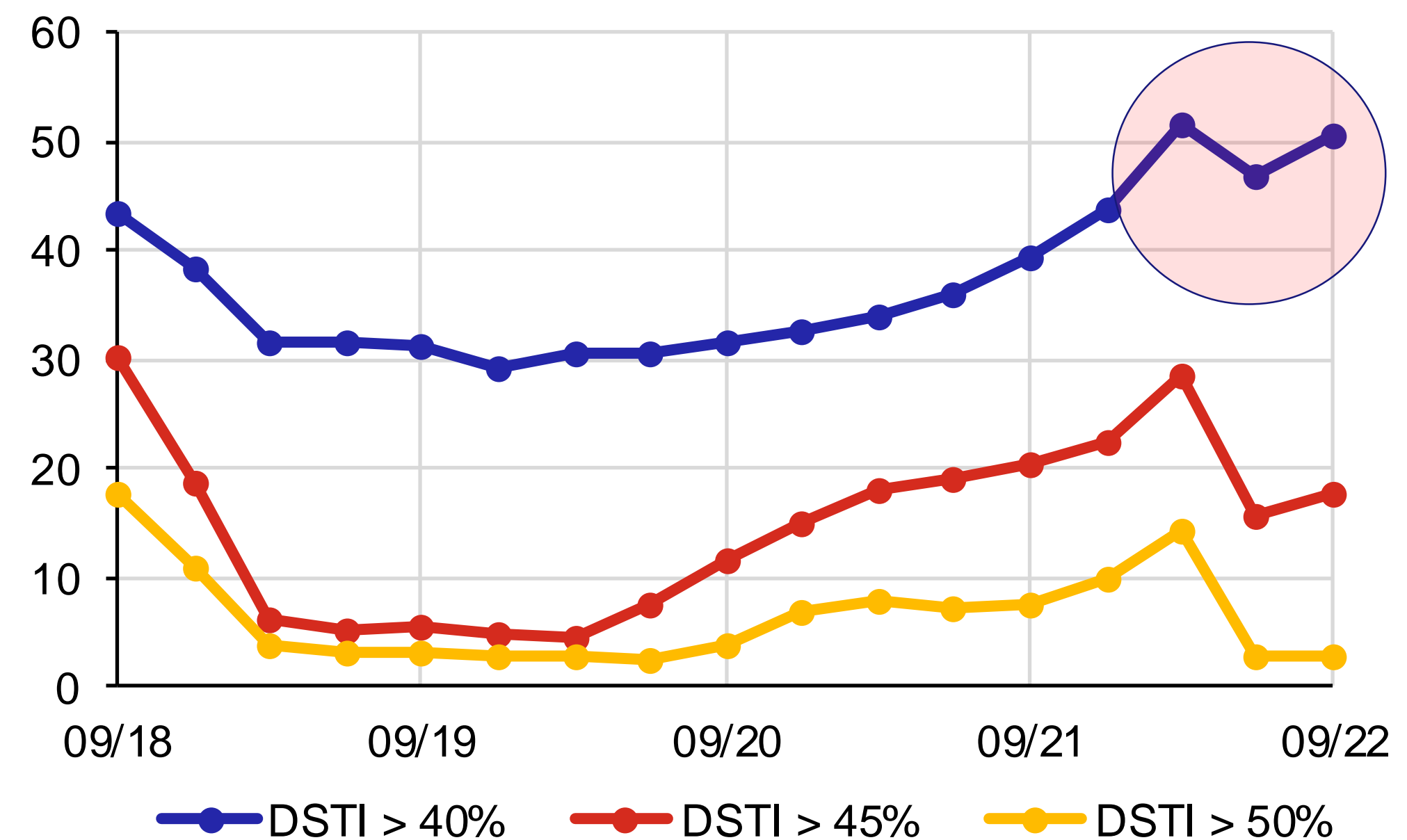
Property market and mortgage lending (3)

- The volume of genuinely new mortgage loans fell sharply from an all-time high in 2021 to slightly below the long-term average in January–September 2022:
 - Interest rates and the applicable credit ratios dampened lending activity.
 - Banks were mostly compliant with the LTV, DSTI and DTI limits effective since April.
 - However, the share of mortgage loans with a risky DSTI level above 40% remains high.

Bank loans for house purchase and mortgage loans (CZK billions)



Loans with DSTIs in selected bands (share of loans in volume provided in %)



Limits on mortgage loan ratios (1)

- The Bank Board decided to **keep the credit ratio limits** effective since 1 April 2022 **unchanged**.

DTI

Ratio of applicant's total debt to net annual income.

8.5



9.5

DSTI

Ratio of sum of applicant's monthly repayments to net monthly income.

45%



50%

LTV

Ratio of value of loan to value of collateral.

80%



90%

For applicants under 36 years if the loan is for the purchase of owner-occupied housing.

Lenders may in the current calendar quarter apply an exemption from compliance with the limits of up to 5% of the total volume of loans provided in the previous quarter.

Limits on mortgage loan ratios (2)

- The Bank Board still considers the **systemic risks** associated with mortgage lending to be **elevated**:
 - The overvaluation of apartment prices rose further in 2022.
 - The proportion of new loans with a DSTI ratio above the risky level of 40% remains elevated.
 - Significant economic and geopolitical uncertainties persist, amid slowing economic activity and rising living costs of households.
- Some mortgage-lending conditions continue to be set using the **Recommendation**, the wording of which remains unchanged.
- The CNB will publish its next analysis of the residential property market and mortgage loans in June 2023 in **Financial Stability Report – Spring 2023**.

Contents

1. Aggregate assessment of risks and overview of CNB's main measures

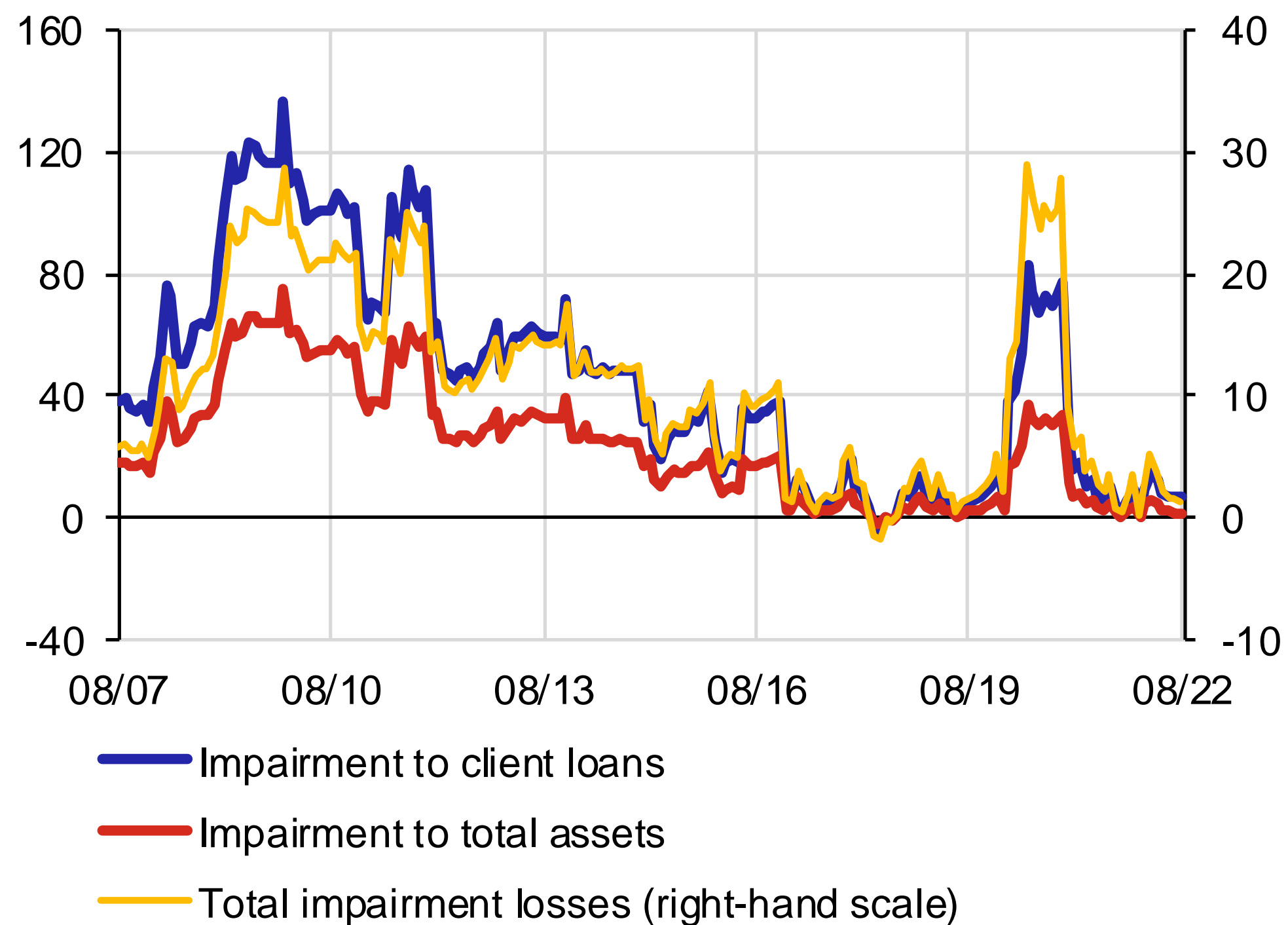
2. Assessment of selected risks



Initial level of banks' credit risk (1)

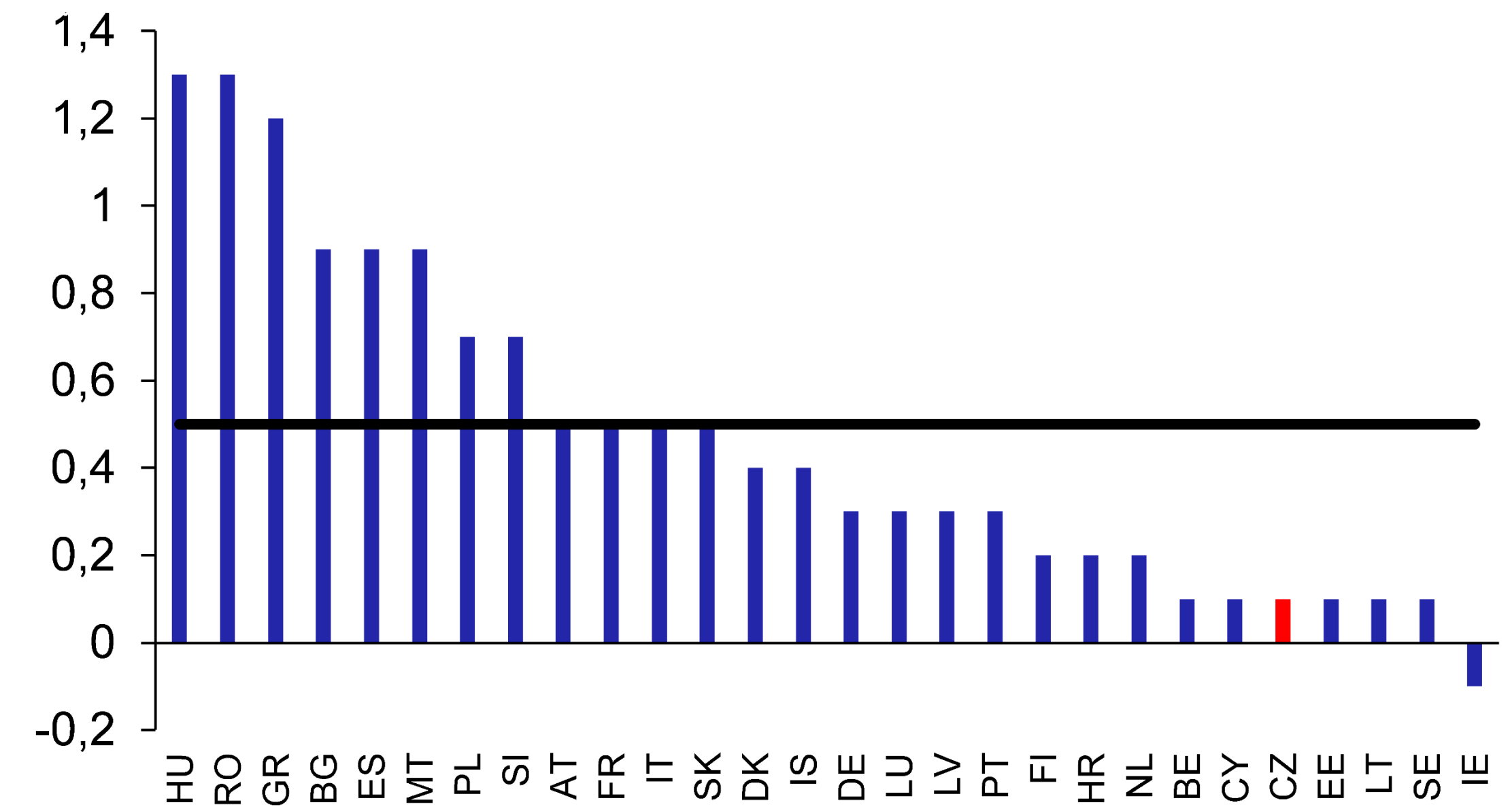
Asset impairment losses

(impairment/total assets in bp; total impairment losses in CZK billions)



Cost of risk (as of 2022 Q2)

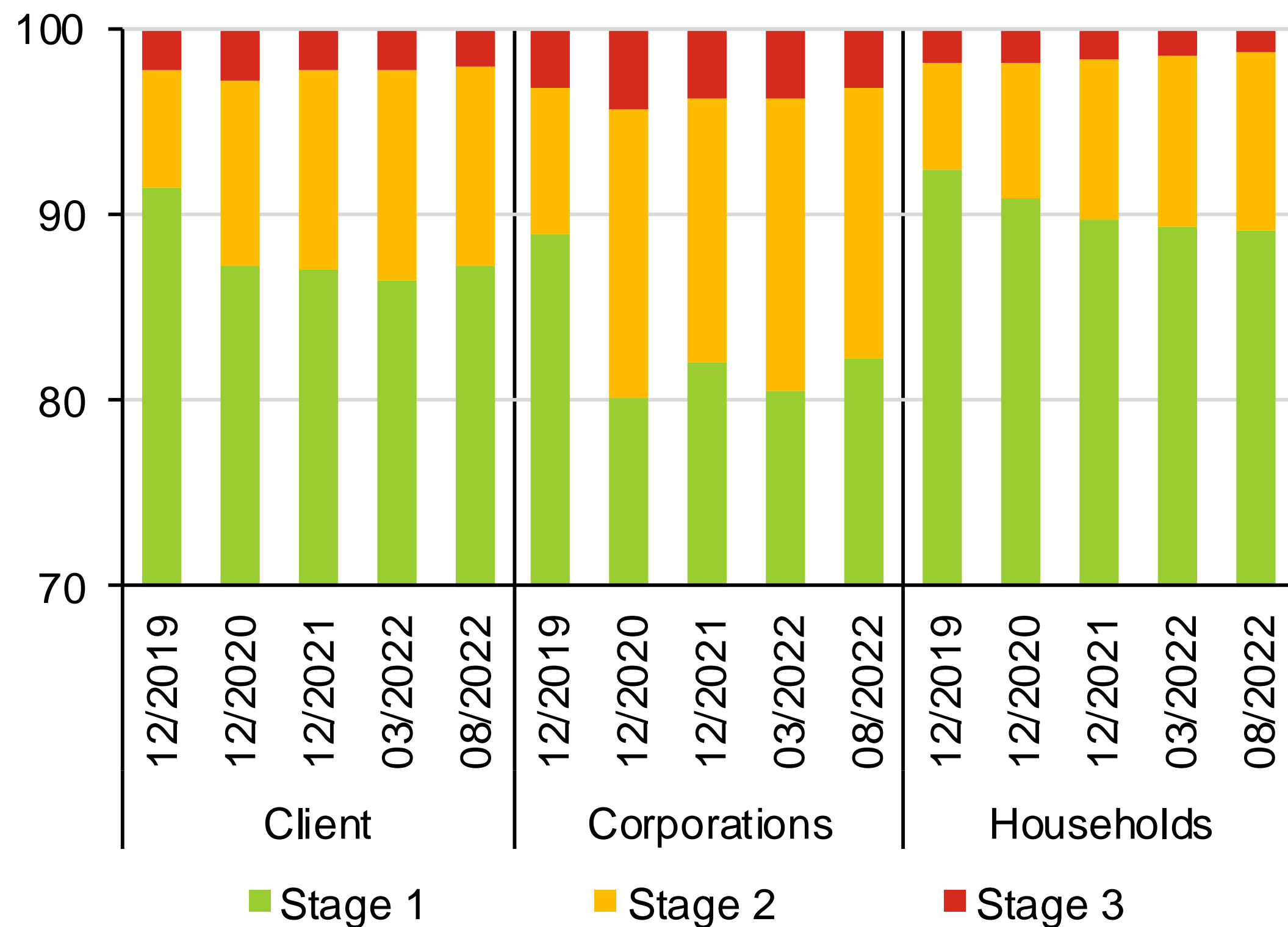
(%)



Initial level of banks' credit risk (2)

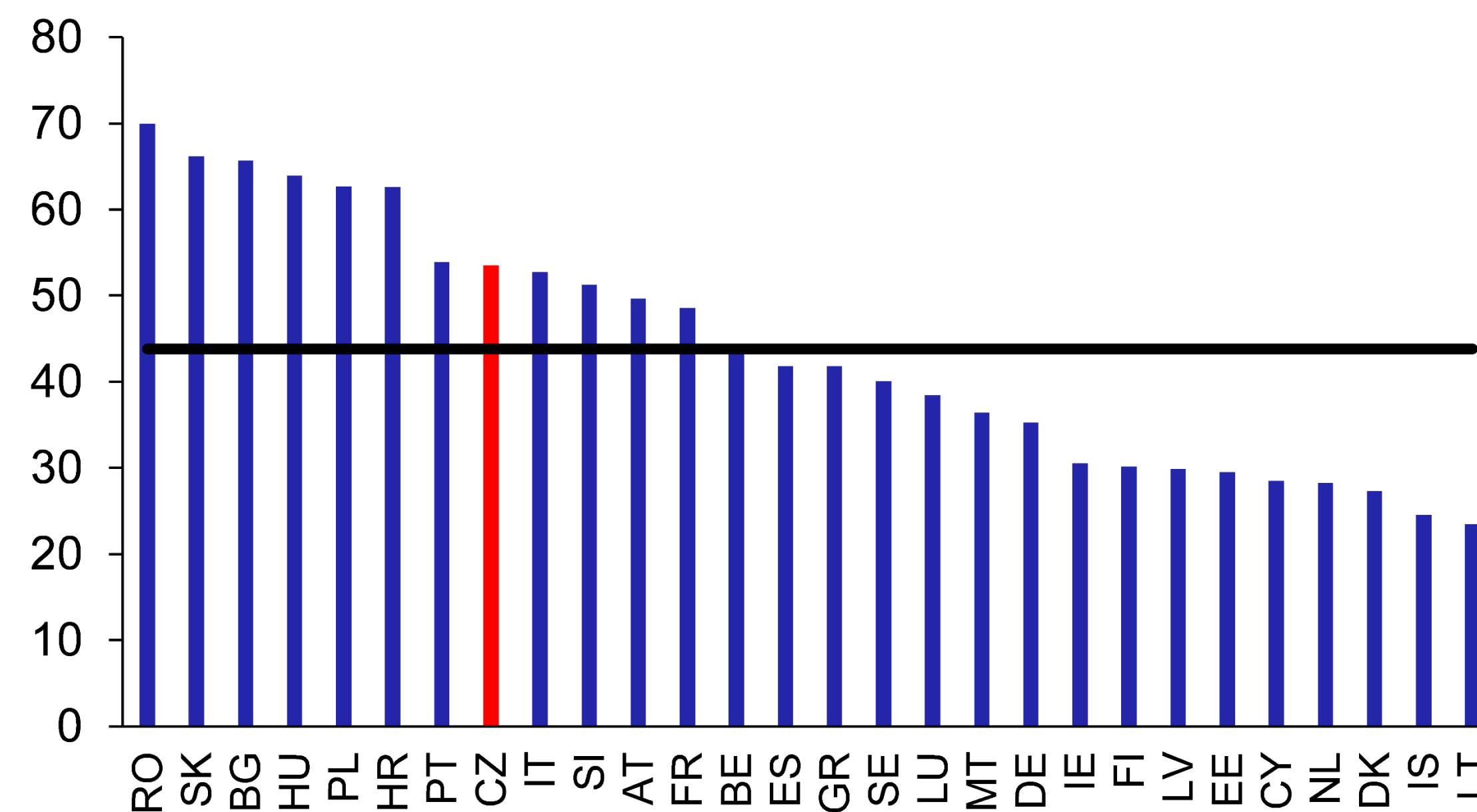
Loan structure by portfolio

(%)



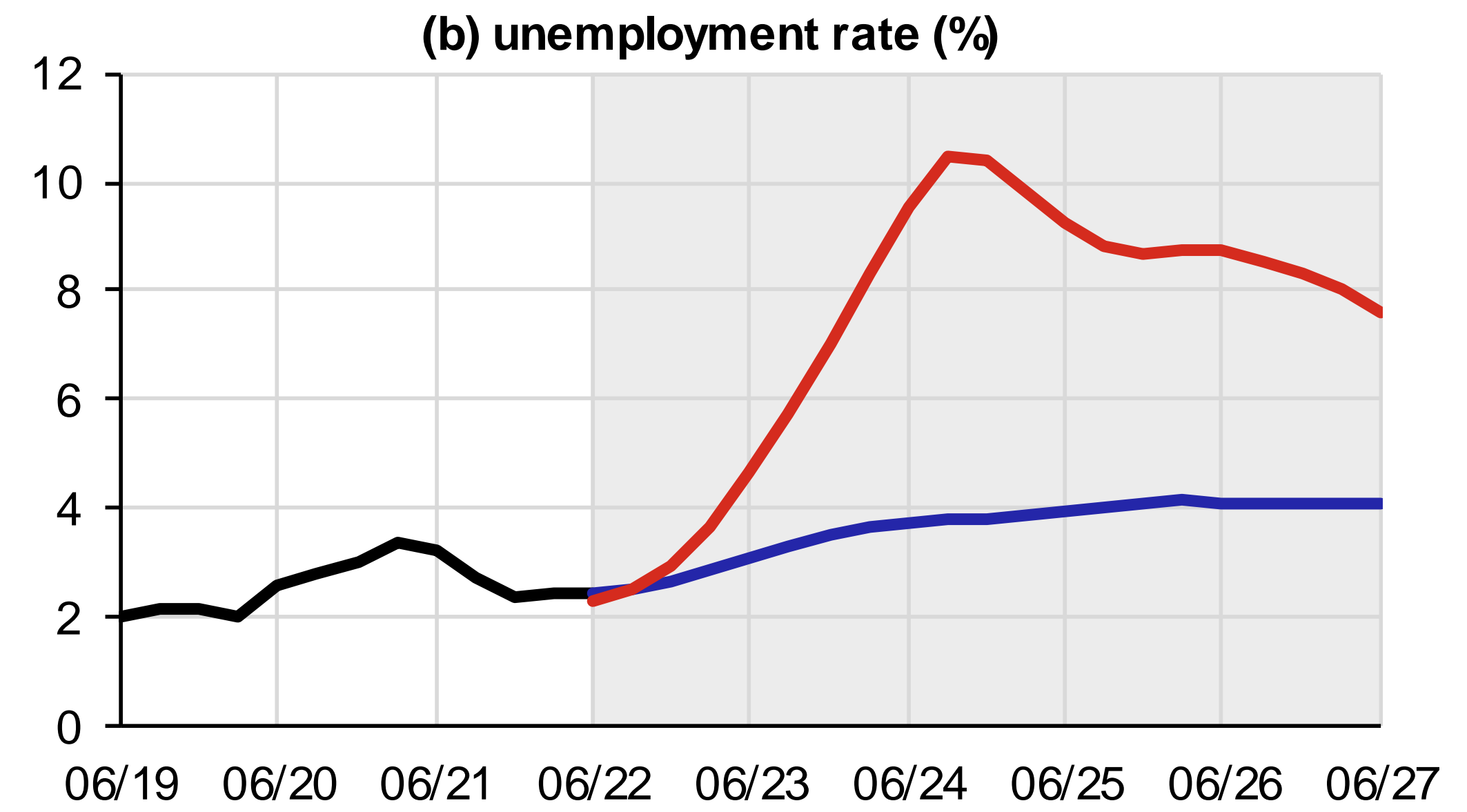
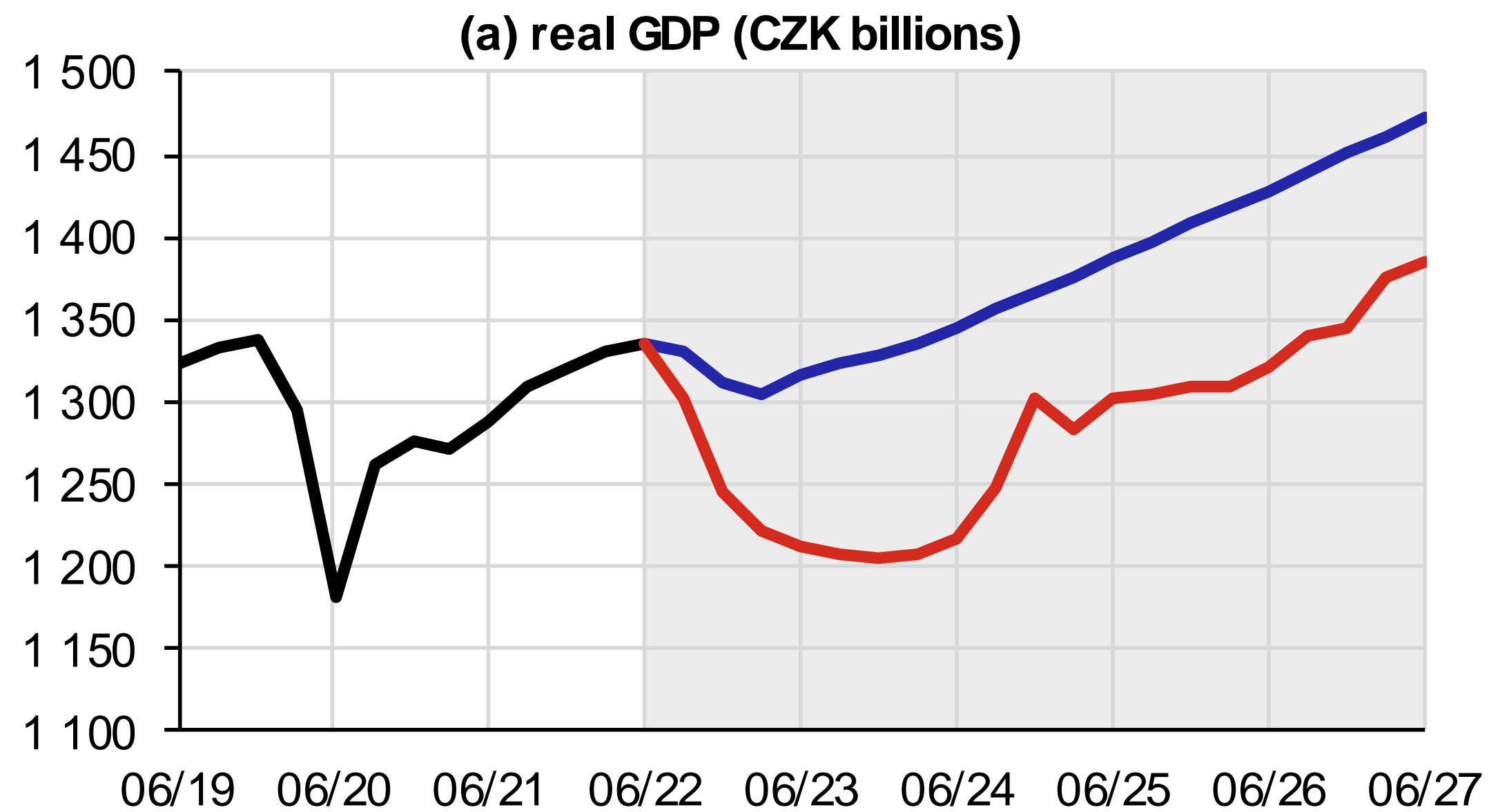
Coverage of non-performing loans (as of 2022 Q2)

(%)



Main characteristics of stress test scenarios

Alternative scenarios



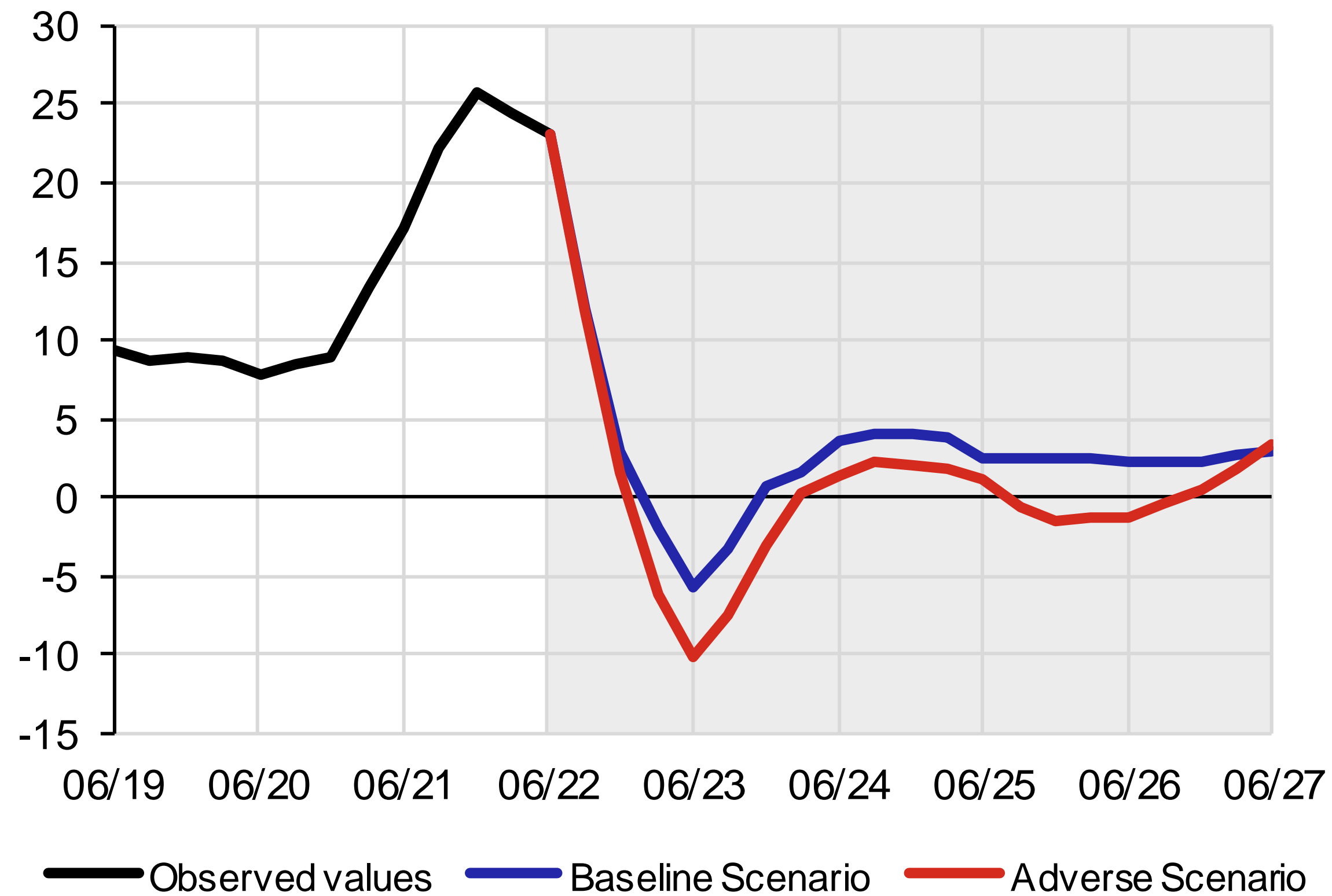
— Observed values

— Baseline Scenario

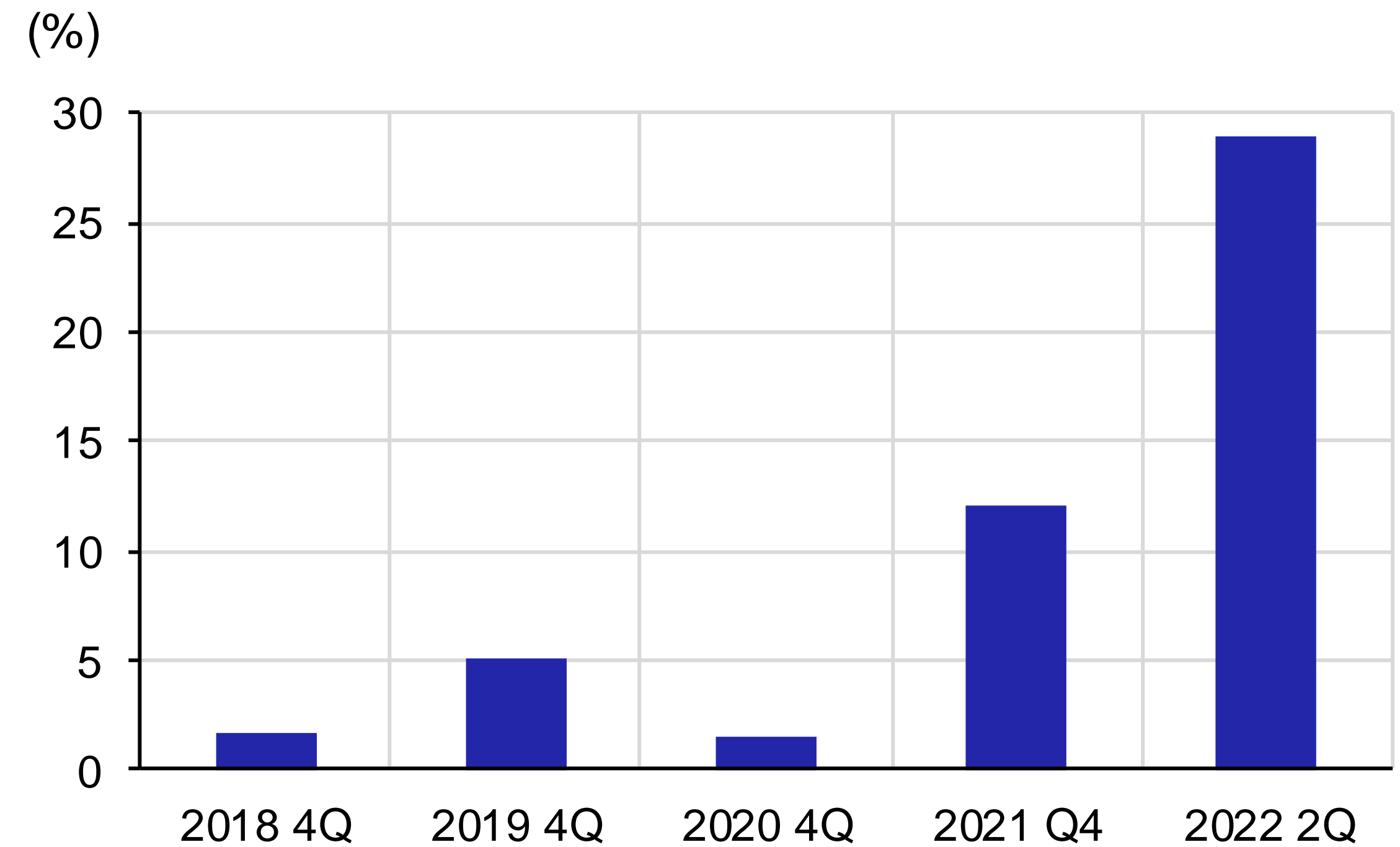
— Adverse Scenario

Residential property price scenarios

Property price projections
(year-on-year growth in %)

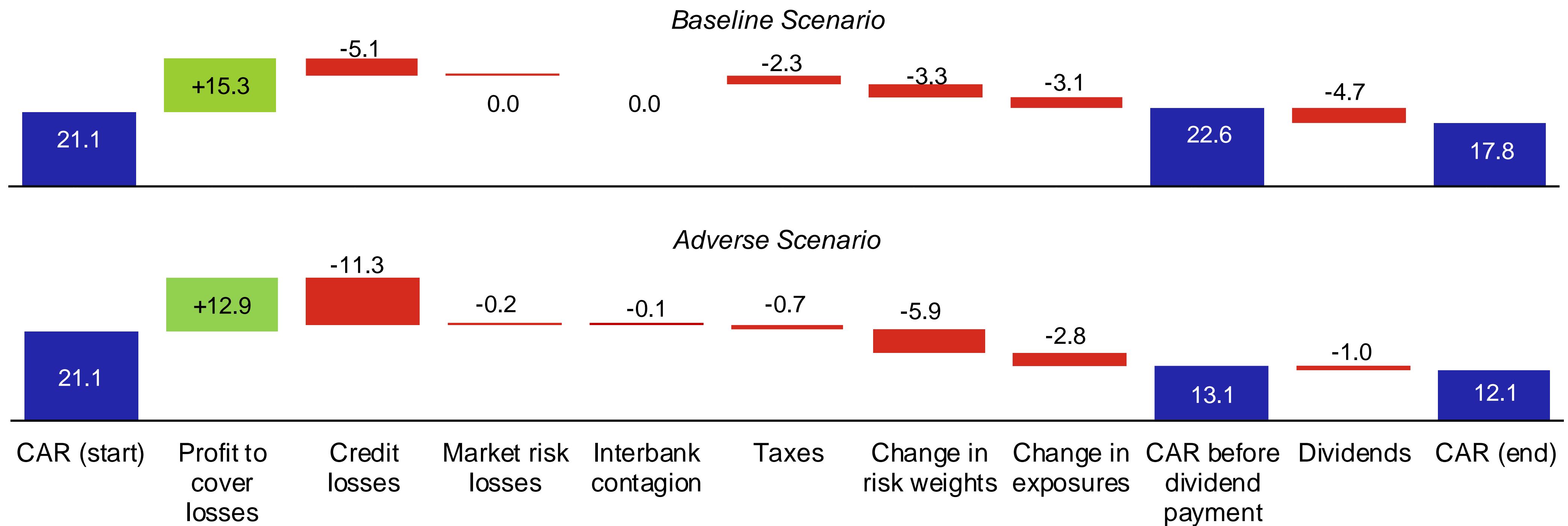


Probability of average apartment prices falling by more than 10%



Bank stress test results (1)

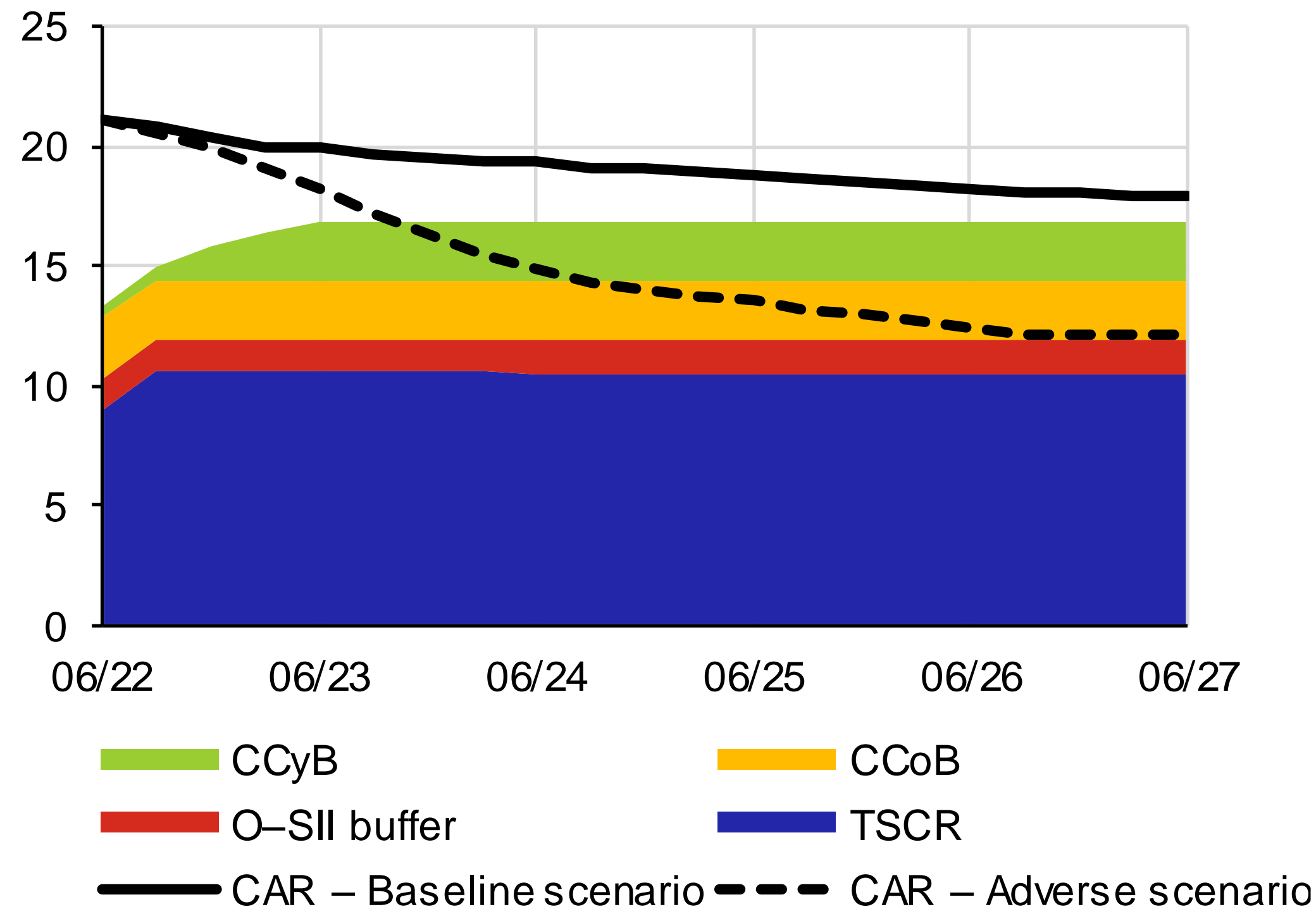
Decomposition of the change in the total capital ratio of the banking sector in the *alternative* scenarios (pp)



Bank stress test results (2)

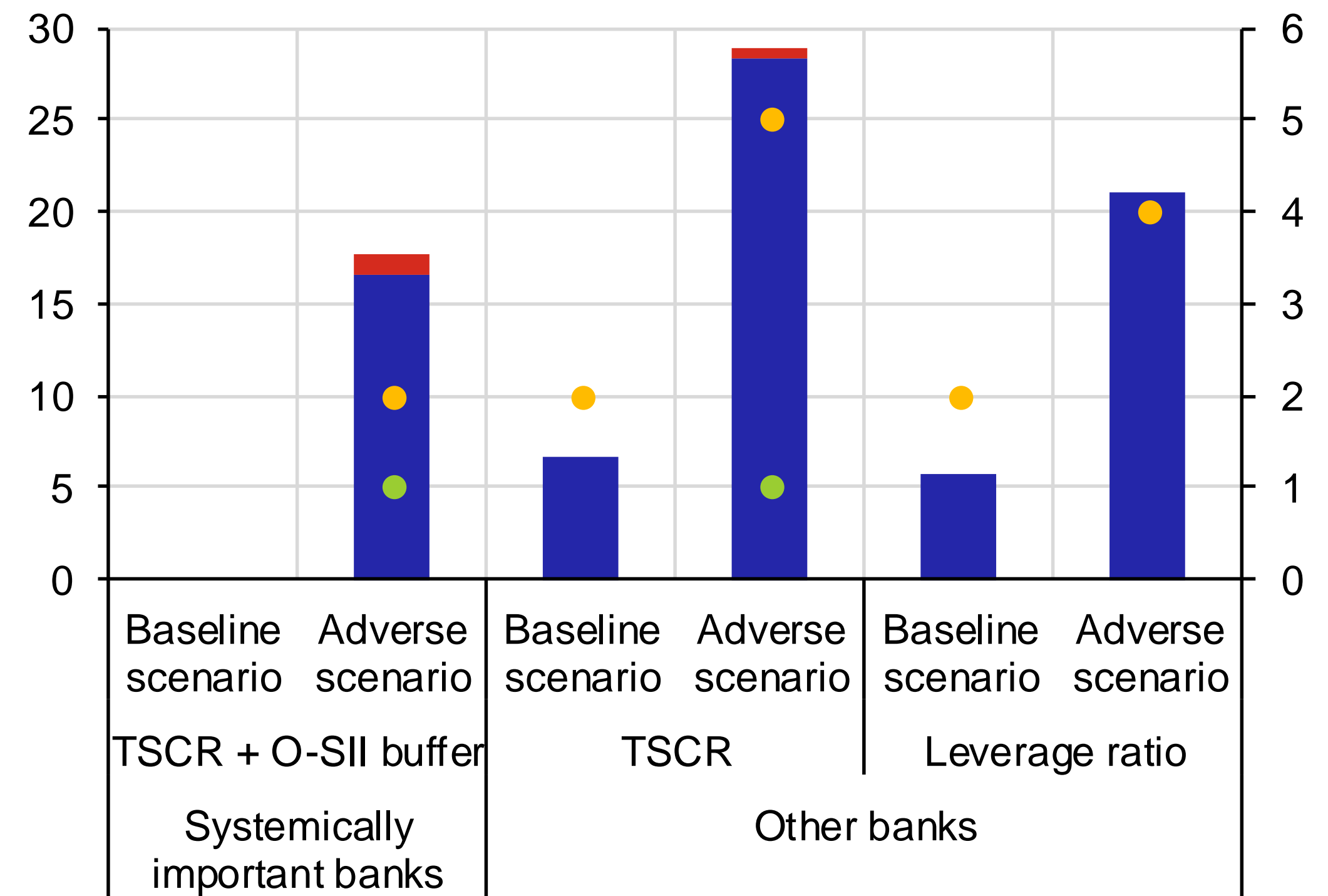
Compliance with selected regulatory requirements by the banking sector in the *alternative scenarios*

(% of TREA)



Need and method for replenishing own funds at different capital requirement levels

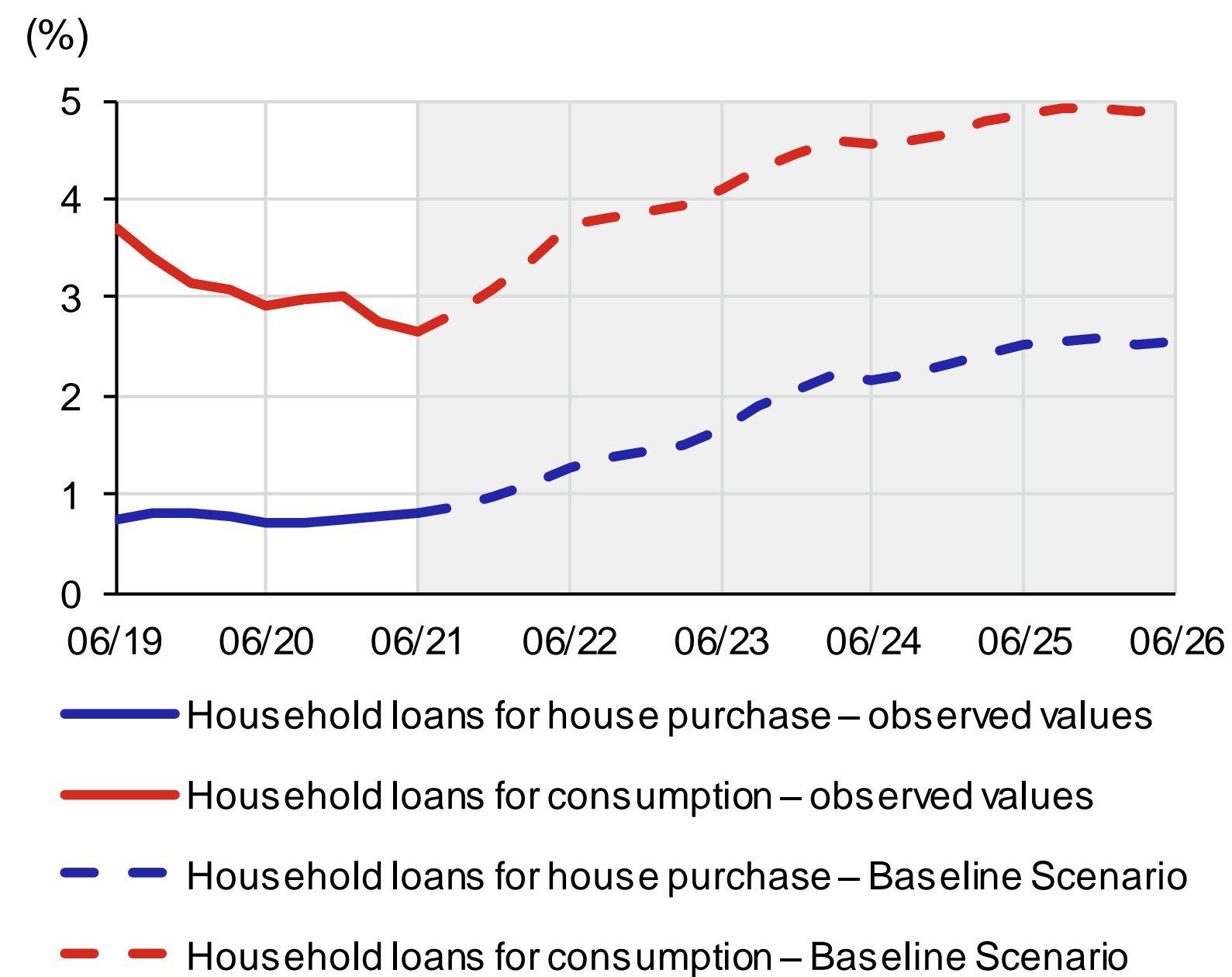
(CZK billions; right-hand scale: number of banks)



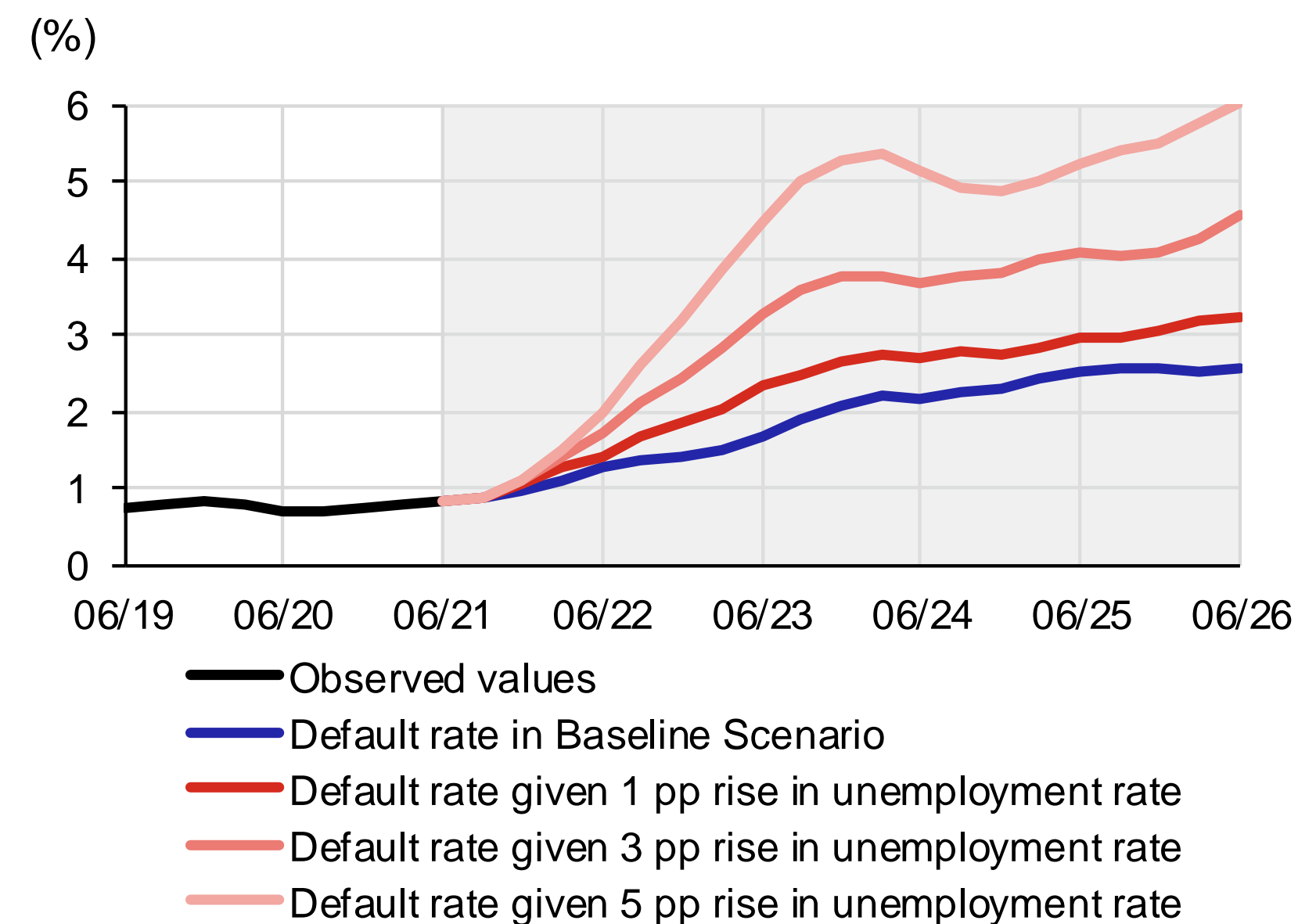
■ Conversion (CZK billions) ■ Capital injections (CZK billions)
 ● Capital injections (No. of banks) ● Conversion (No. of banks)

Results of stress test of households (1)

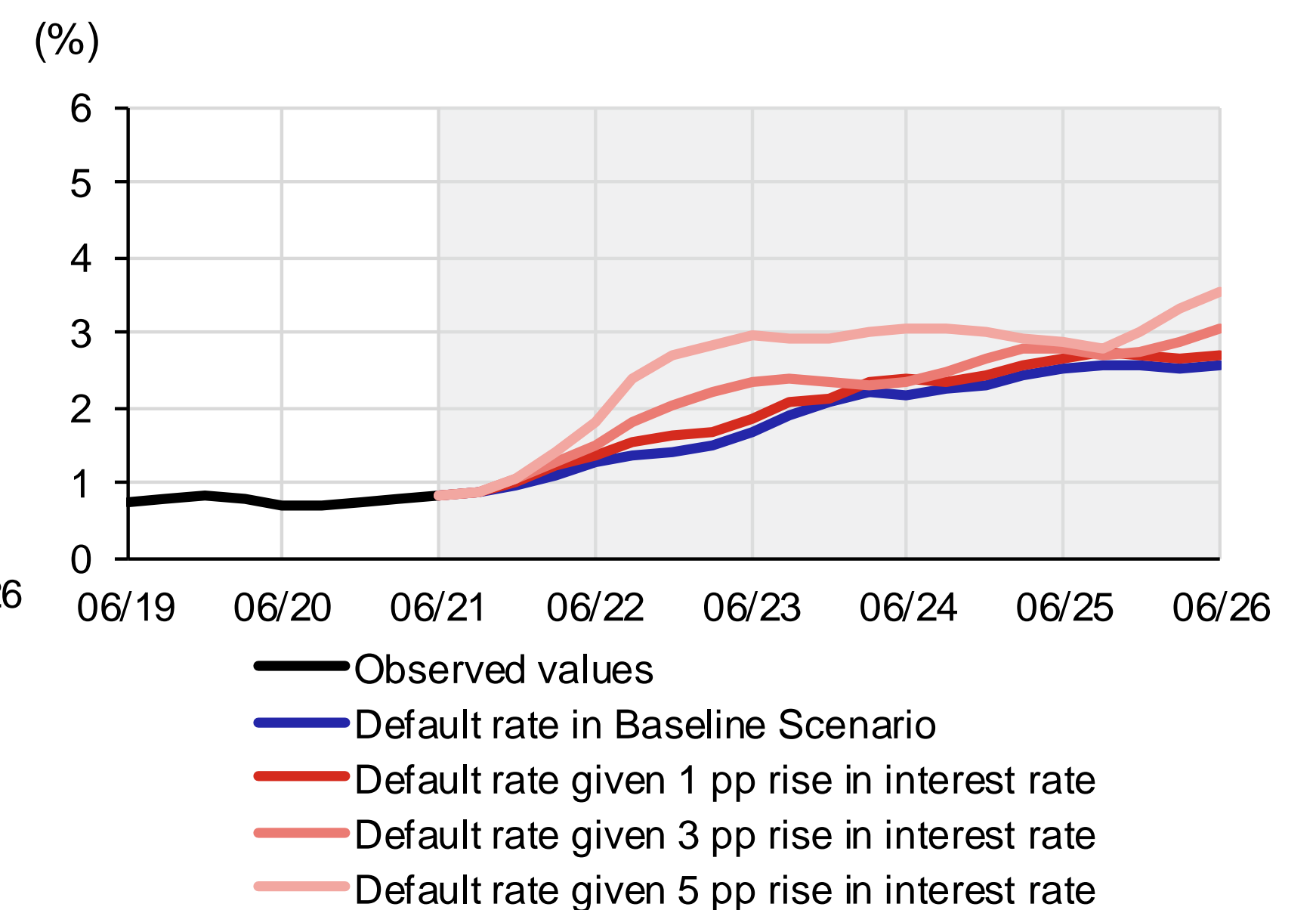
12M default rate on loans to households in the *Baseline Scenario*



12M default rate on mortgage loans to households given additional growth in unemployment rate beyond the *Baseline Scenario*



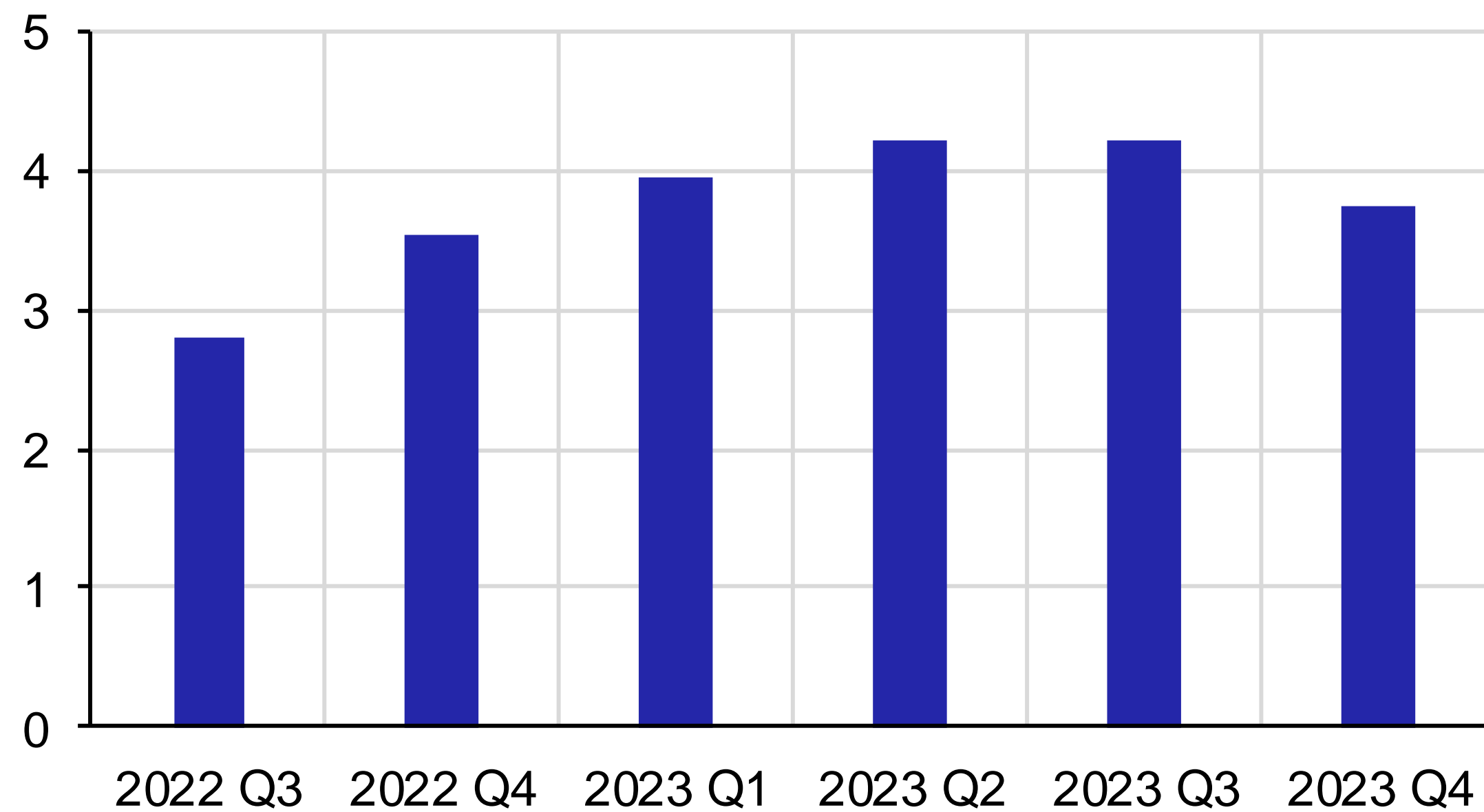
12M default rate on mortgage loans to households given additional growth in interest rate beyond the *Baseline Scenario*



Results of stress test of households (2)

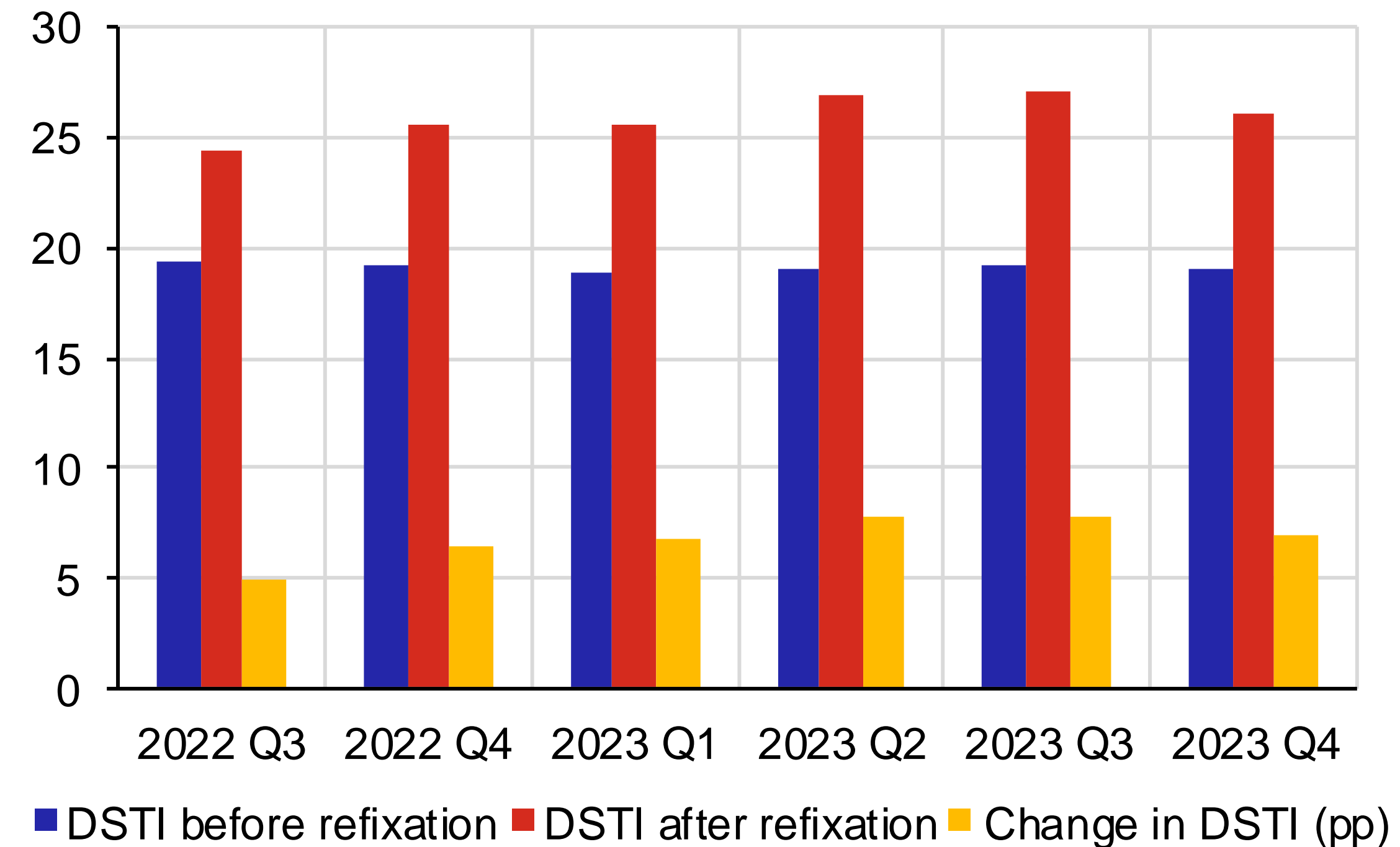
Estimate of the change in mortgage interest rates at the time of refixation

(pp)



Estimate of the DSTI value for refixed loans

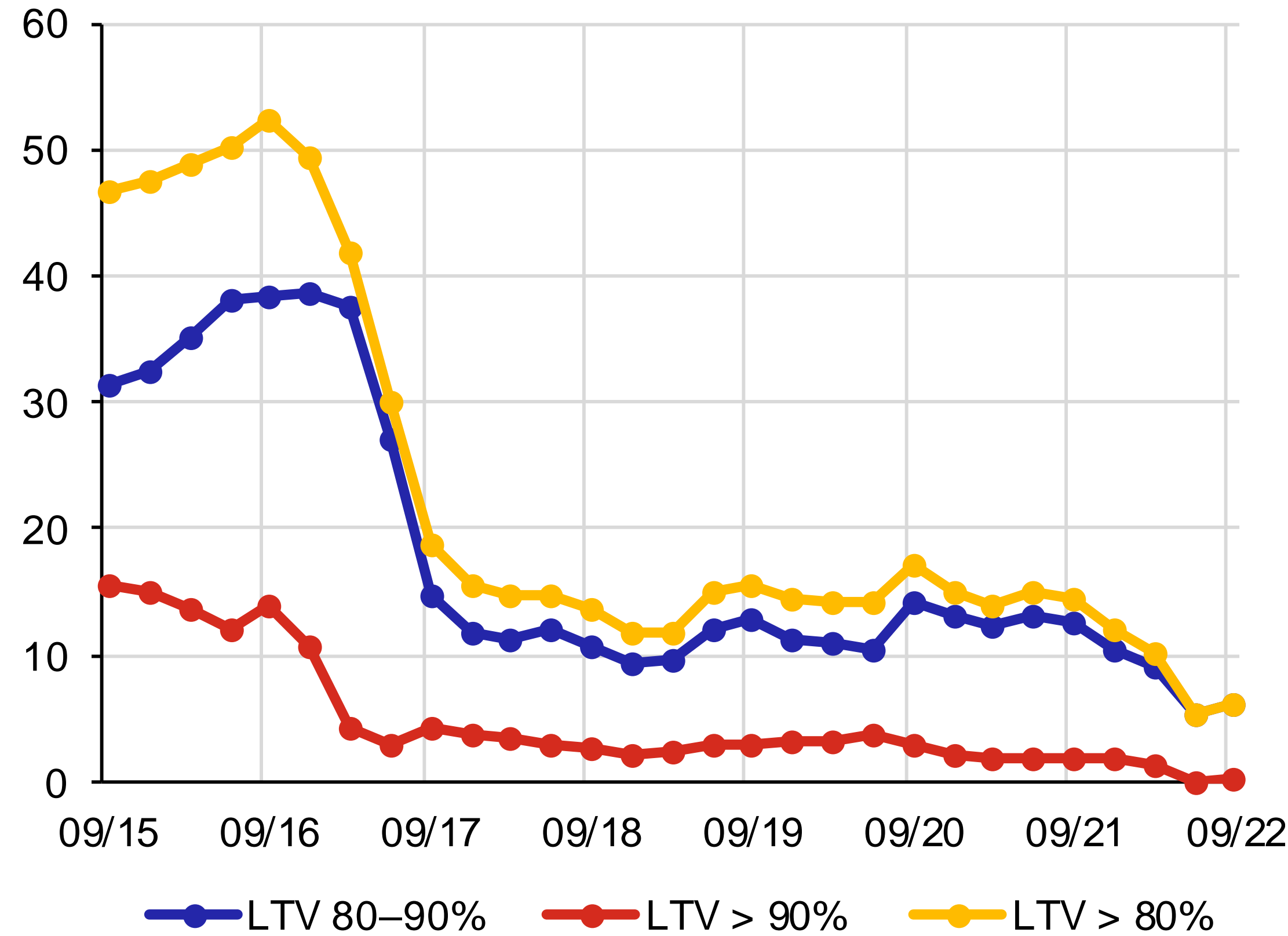
(%)



Compliance with LTV limit

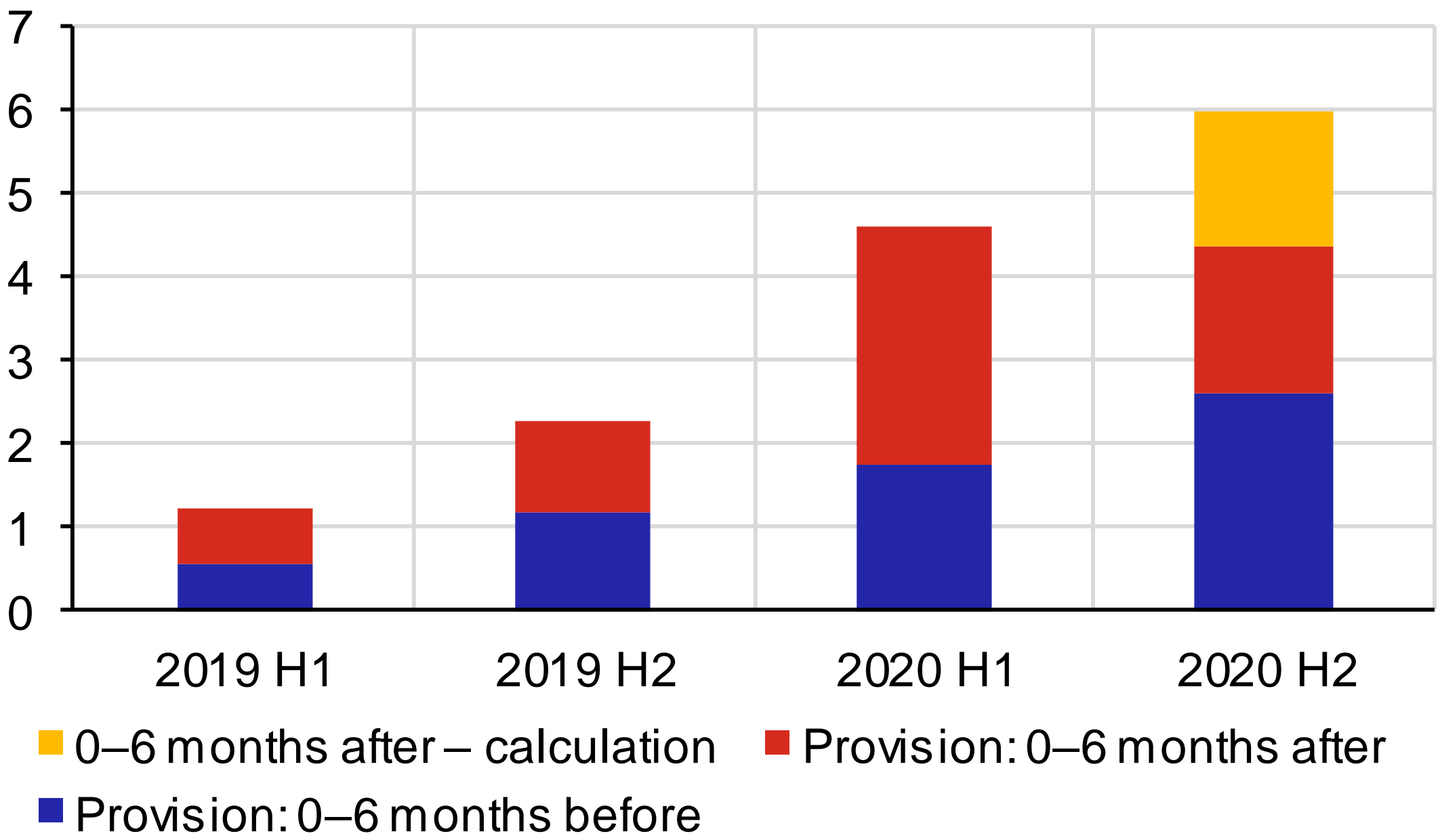
Loans with LTVs in selected bands

(share of loans in quarterly volume provided in %)



Concurrent provision of unsecured and mortgage loans

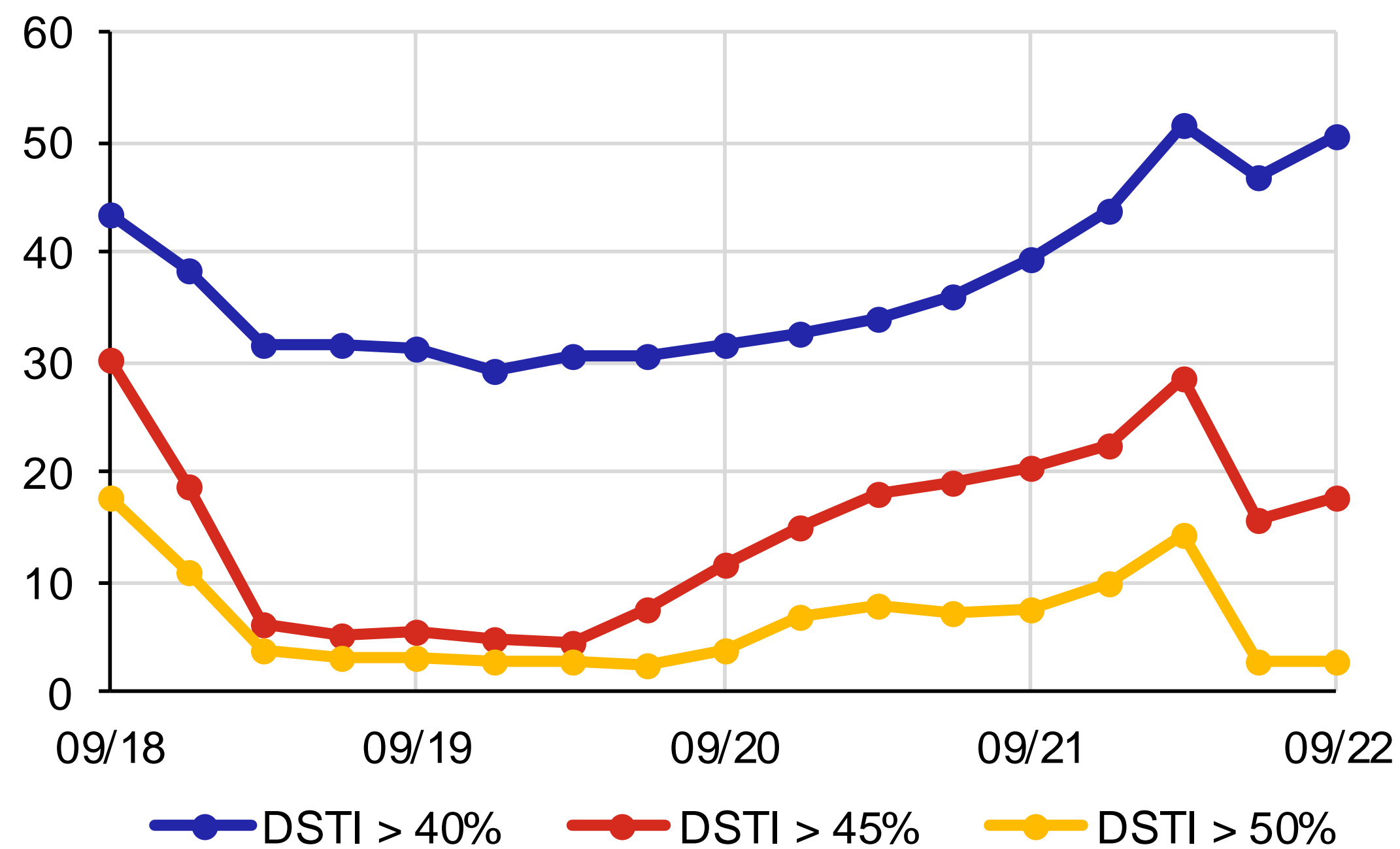
(unsecured loans in CZK billions; x-axis: half-year in which mortgage loan was provided)



Compliance with DSTI and DTI limits

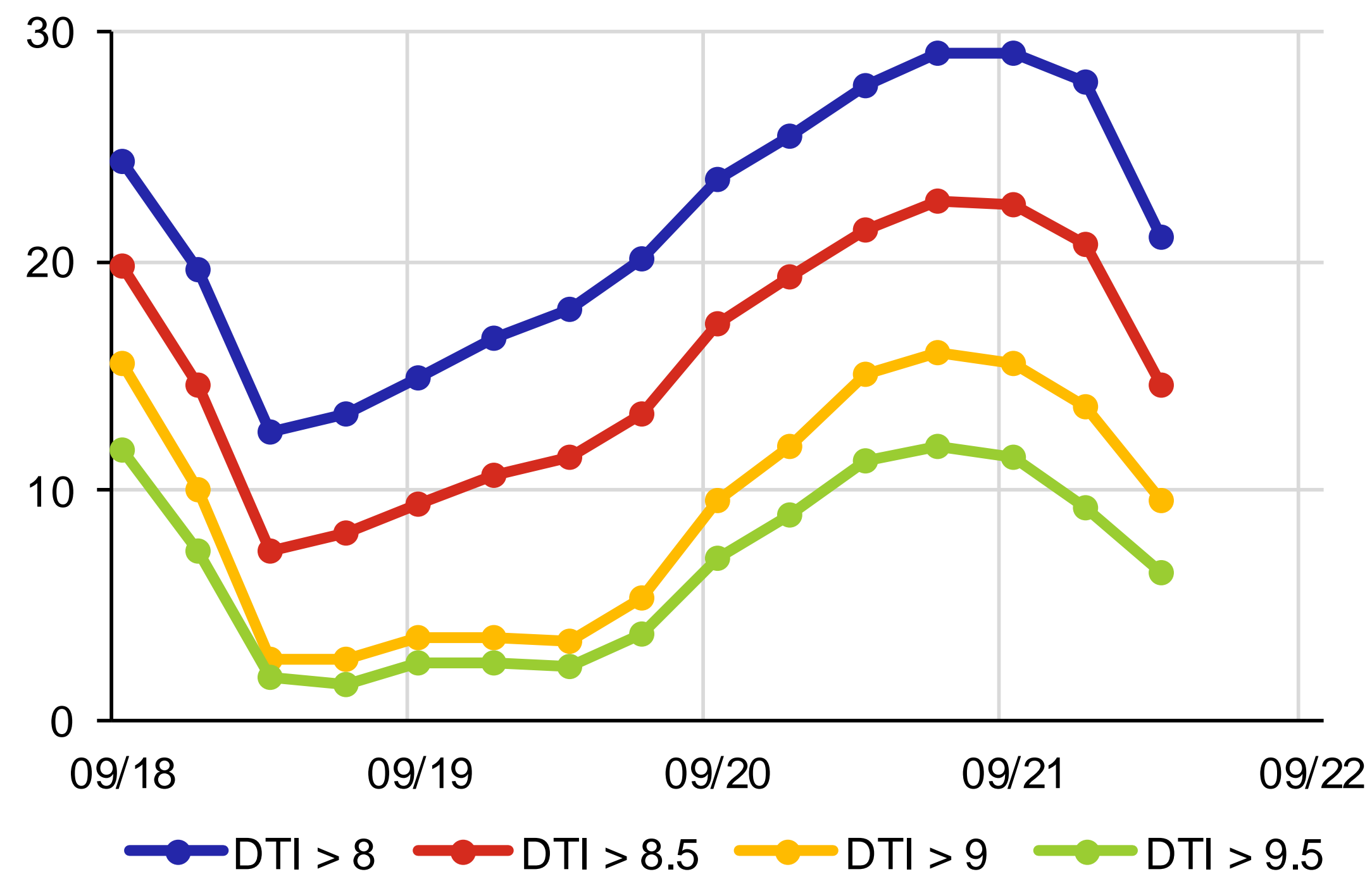
Loans with DSTIs in selected bands

(share of loans in quarterly volume provided in %)



Loans with DTIs in selected bands

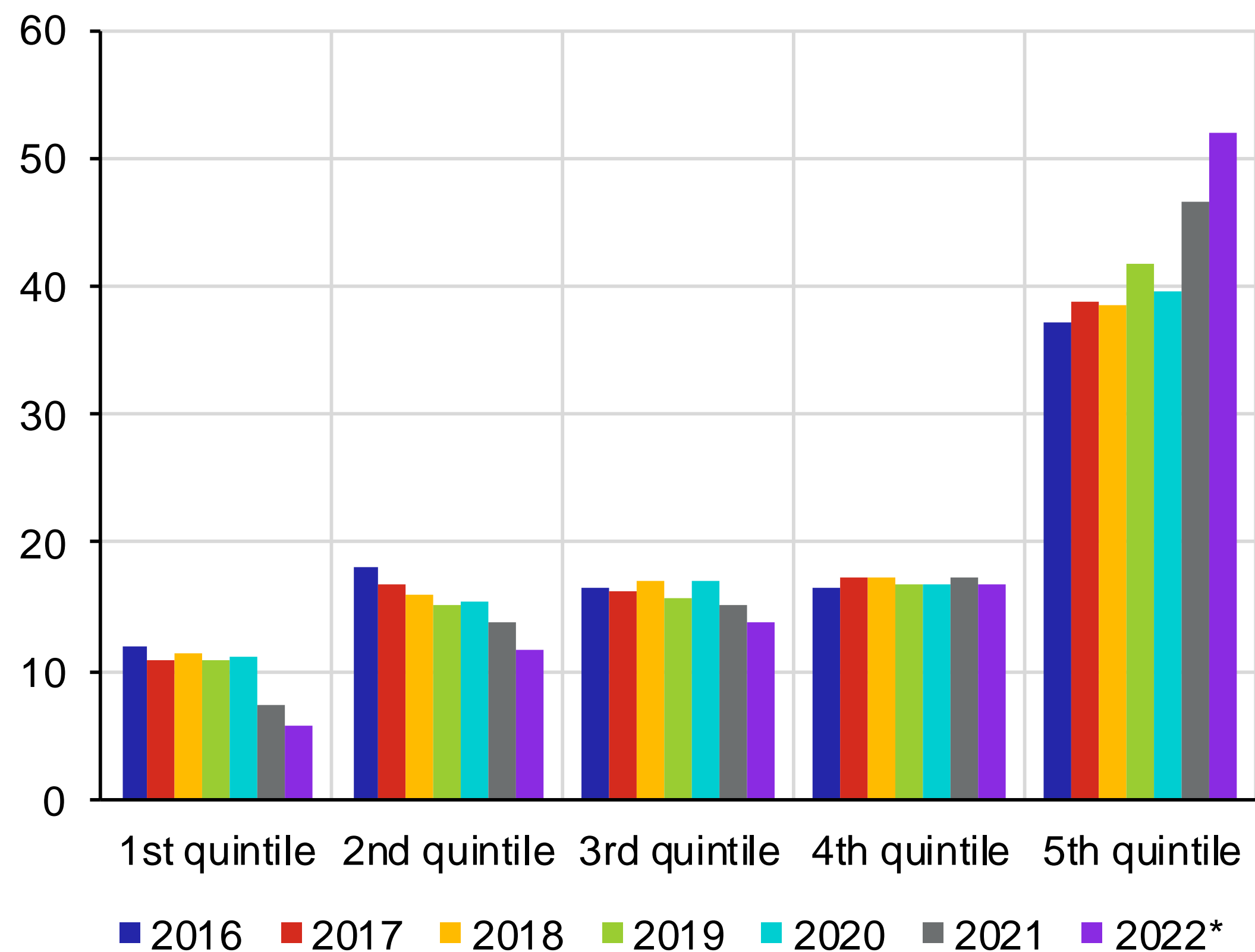
(share of loans in quarterly volume provided in %)



Structure of mortgage loans

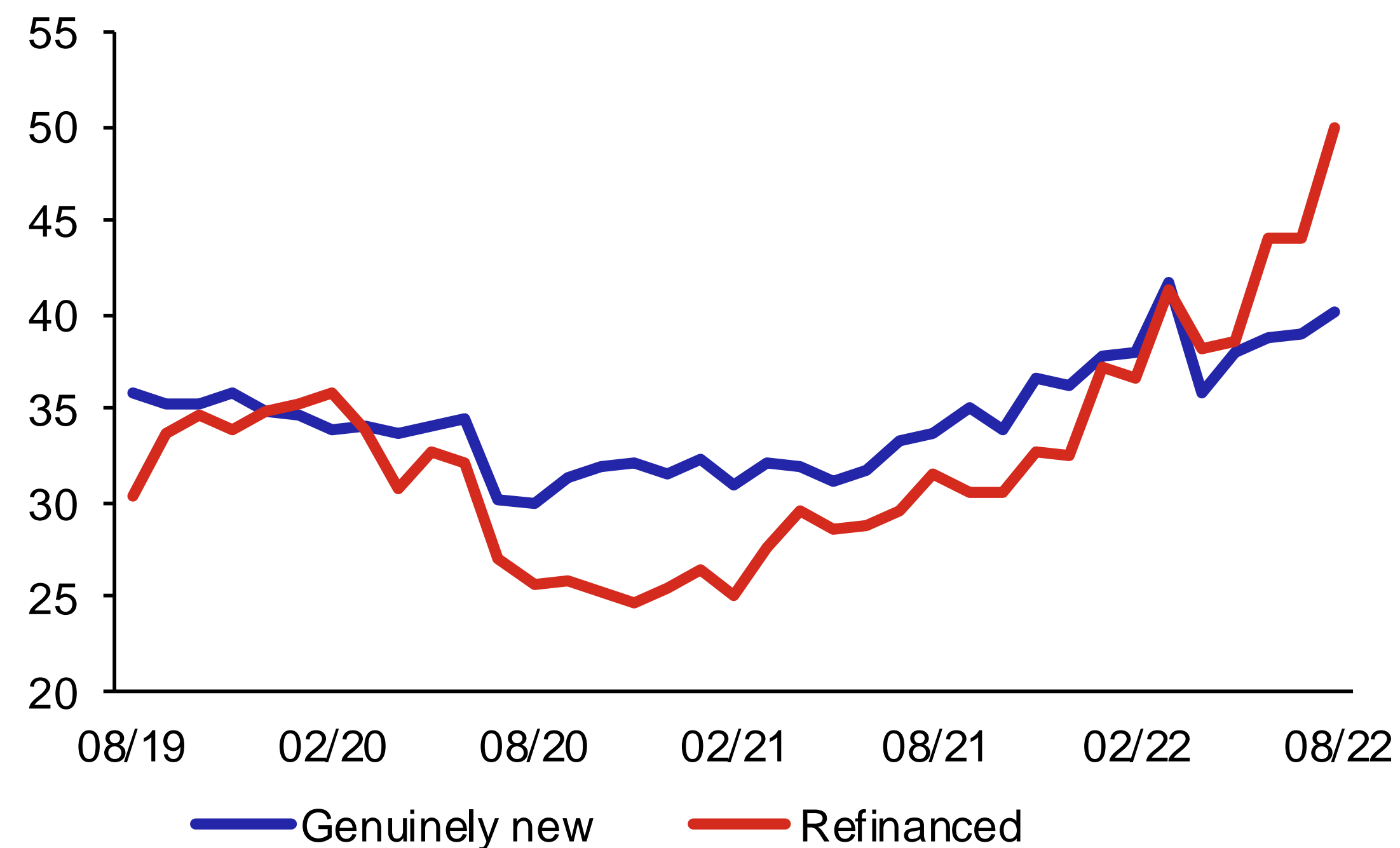
Share of mortgage loans provided by income quintile of households

(% of total volume of mortgage loans)



Share of second and subsequent mortgage loans

(% of monthly volume)



Thank you for your attention

The following will be published on the CNB website on **1 December 2022**:

- Provision of a general nature on setting the countercyclical capital buffer rate No. IV/2022

The following will be published on the CNB website on **16 December 2022**:

- Financial Stability Report – Autumn 2022
- The minutes of the Bank Board meeting on financial stability issues complete with attributed arguments of individual CNB Bank Board members, as in the case of monetary policy meetings