



OESTERREICHISCHE NATIONALBANK
EUROSYSTEM

Developments in financial and housing markets – which ways are there to address the challenges in real estate?

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XIXth European Congress of the EFBS in Prague, “Housing finance: addressing regulation, low interest rates, and digitisation”, session 1 “Have we reached a turning point in financial and housing markets?”

Opinions expressed by the authors do not necessarily reflect the official viewpoint of the Oesterreichische Nationalbank or of the Eurosystem.

The author wants to thank the colleagues of the Financial Stability and Macprudential Supervision Division and Claudia Kwapil from the Economic Analysis Division.

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- Prices and lending
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- Profitability of Austrian banks in CESEE

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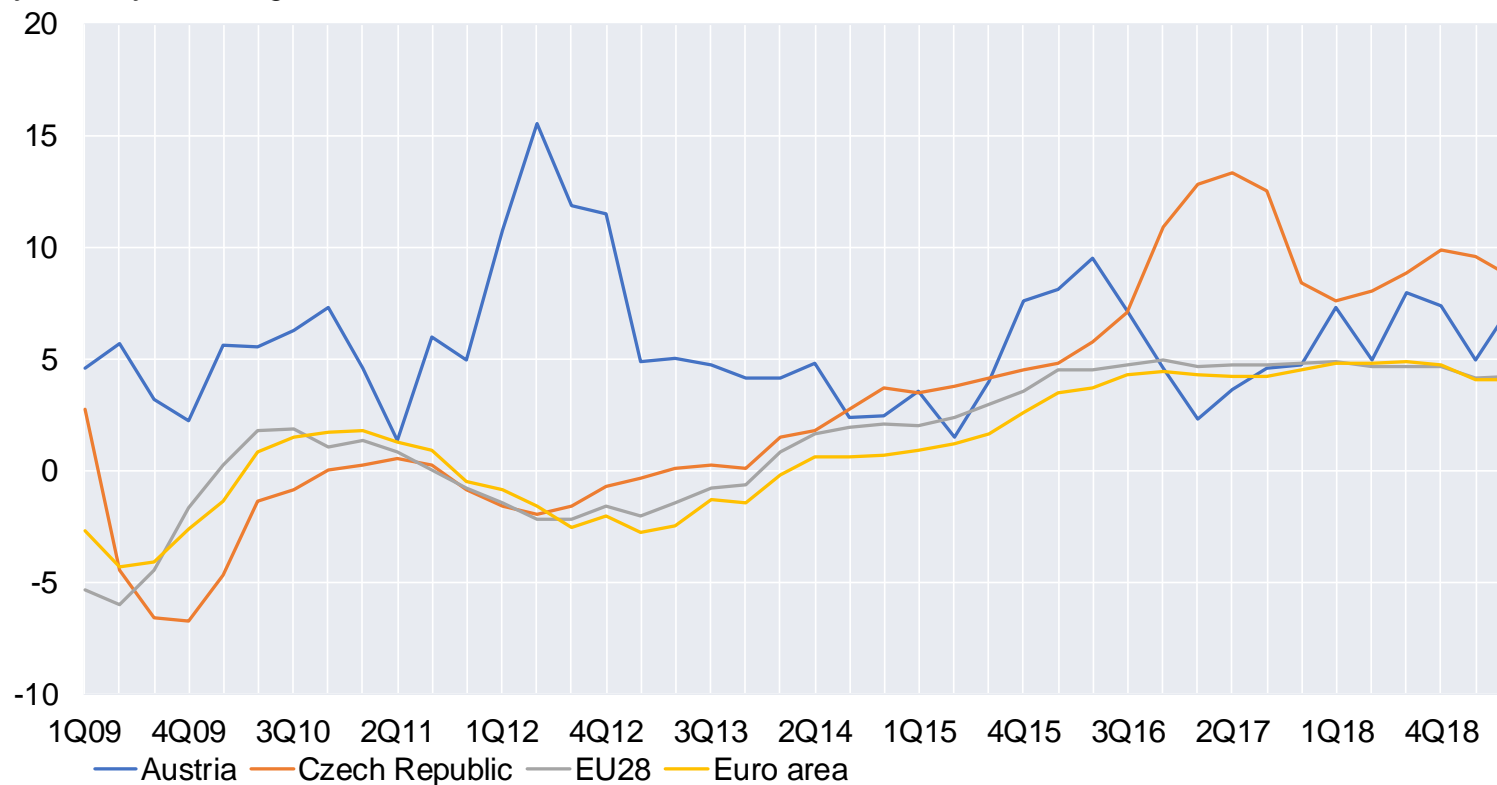
I. Overview on developments in financial and real estate markets

- **Prices and lending**
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Divergence in house price growth rates across Europe

Development of residential property prices¹

year-on-year change, in %



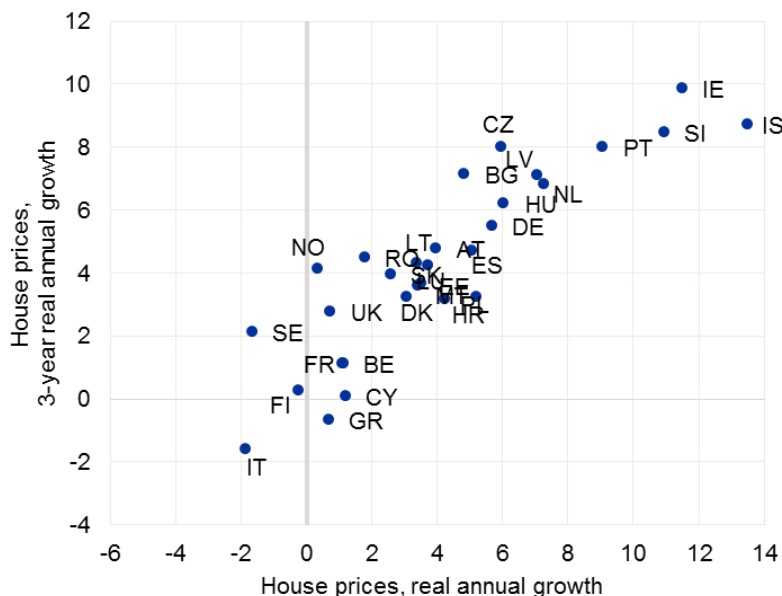
Source: ECB.

¹Whole country, All dwelling types, existing.

Increasing house price growth in Europe

House price growth

(in %)

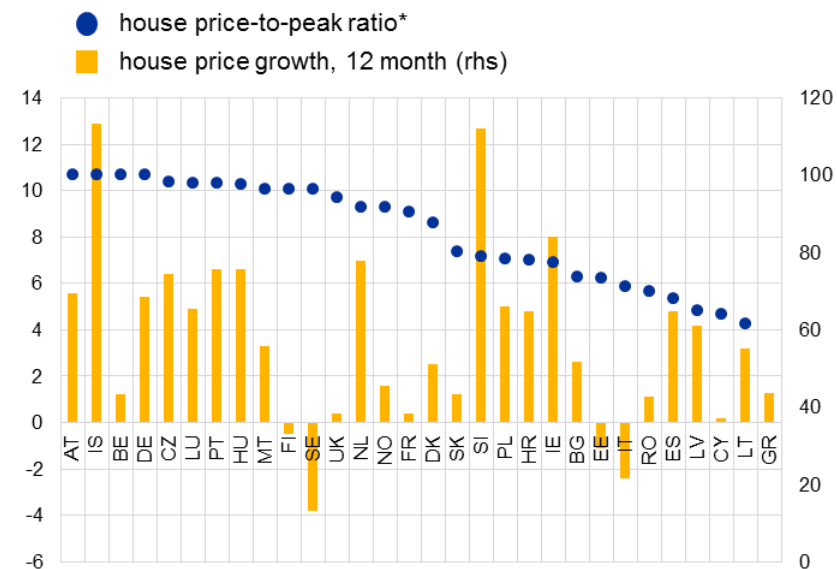


Source: ECB, ESRB.

Notes: Data for three-year growth are from Q3 2018, except for EE, IS, SE (Q4 2018), CY, FI (Q2 2018) and BE (Q1 2018). Data for annual growth (average over four quarters) are from Q3 2018, except for DE, EE, GR, IS, LV, NL, SE, SK, UK (Q4 2018).

House price-to-peak ratio and house price growth

(in %)



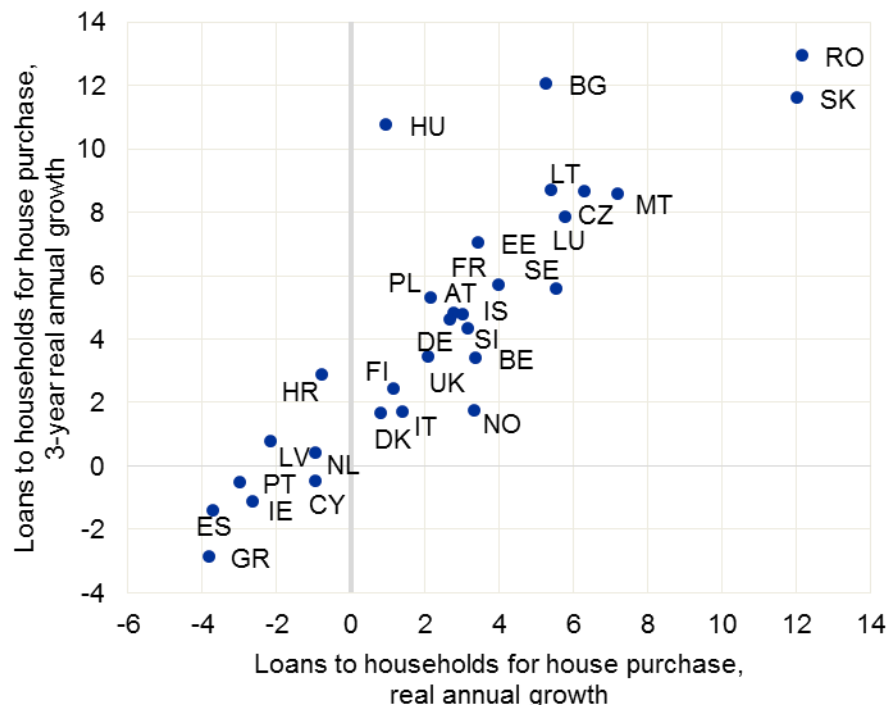
Source: ECB, ESRB.

Note: Data are for 2018Q3. Data for DE, EE, IS, UK, GR, NL and SE are from 2018Q4, for NO from 2019Q1. *The house price-to-peak ratio was computed as the ratio between the current value of the house price index and the maximum registered over the period 2000 to last data point.

Lending developments

Growth in lending for house purchases

(in %)

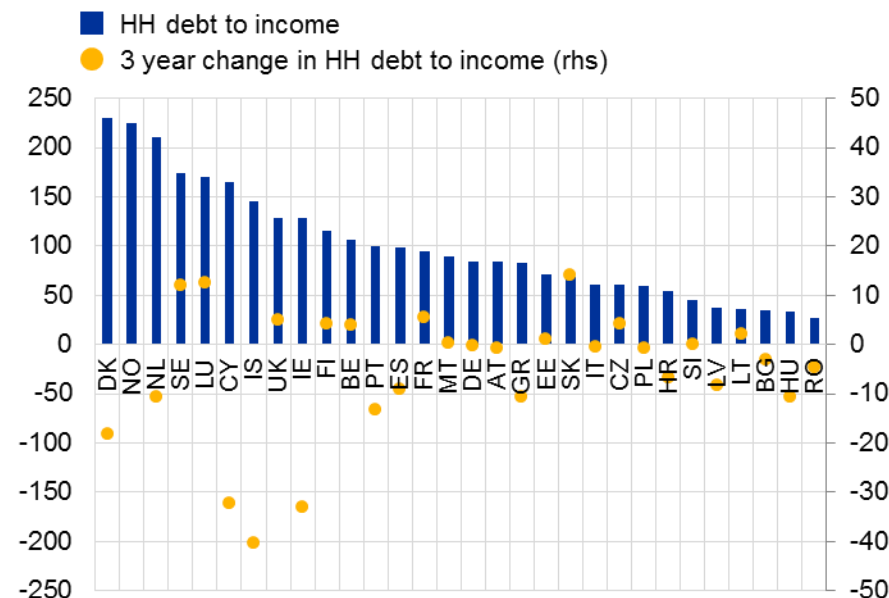


Source: ECB, ESRB.

Note: Data are from 2018Q4. Data for IS and NO are from 2018Q3. Loans are adjusted for sales and securitizations. For BG, DK, GB, HR, HU, PL, RO, SE data on adjusted loans are not available so time series on growth of non-adjusted loans were used.

Household indebtedness and its dynamics

(in % on lhs axis and percentage points on rhs axis)



Sources: ECB and ESRB calculations on basis of information collected by NAs.

Note: Data on household debt to income are from 2018Q3. Data for BG, CY, EE, HU, LT, LU, LV, SK are from 2017Q4 and for HR from 2016Q4.

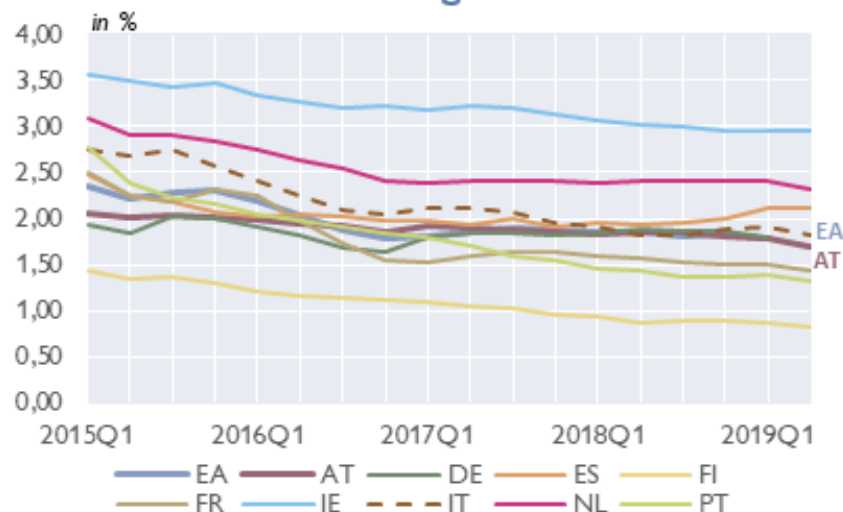
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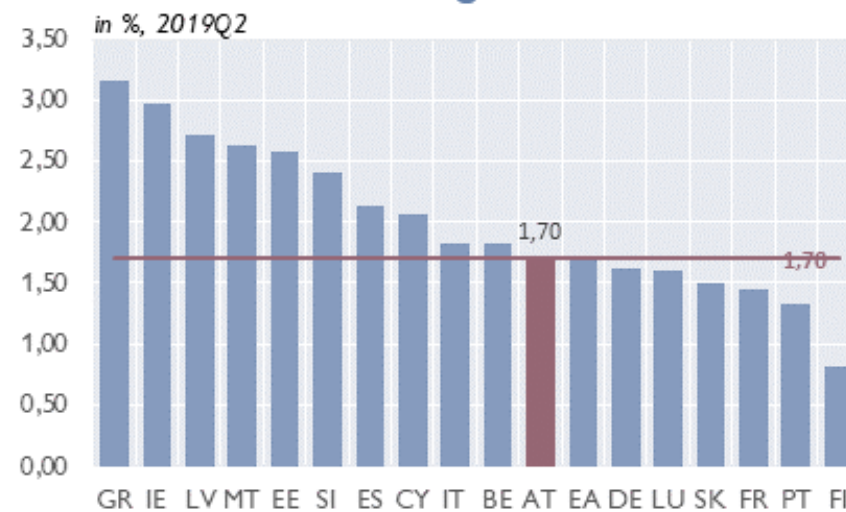
- Prices and lending
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Historically low interest rates

Interest rate for housing loans



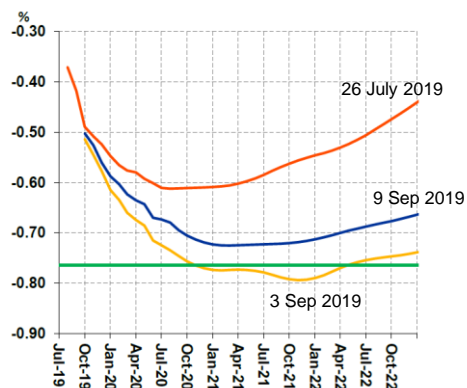
Interest rate for housing loans



Interest rates are expected to stay low for longer

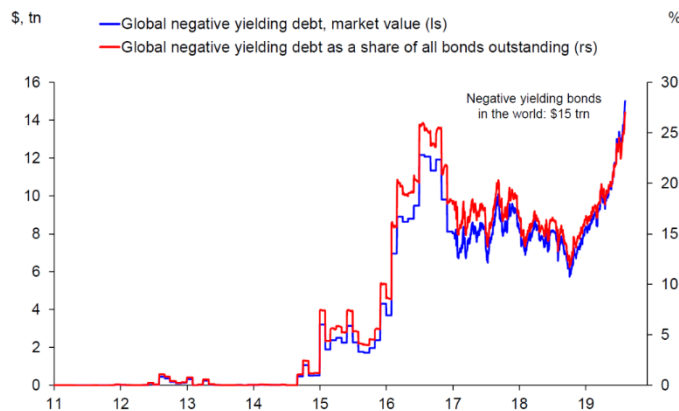
Following major central banks' forward guidance, market participants expect the **low interest rate environment to last longer**. Currently, 27% of global debt is trading at negative rates.

Forward 1-month OIS curve
(in %)



Source: Bloomberg, ESRB.

Negative yielding debt globally
(market value and share)

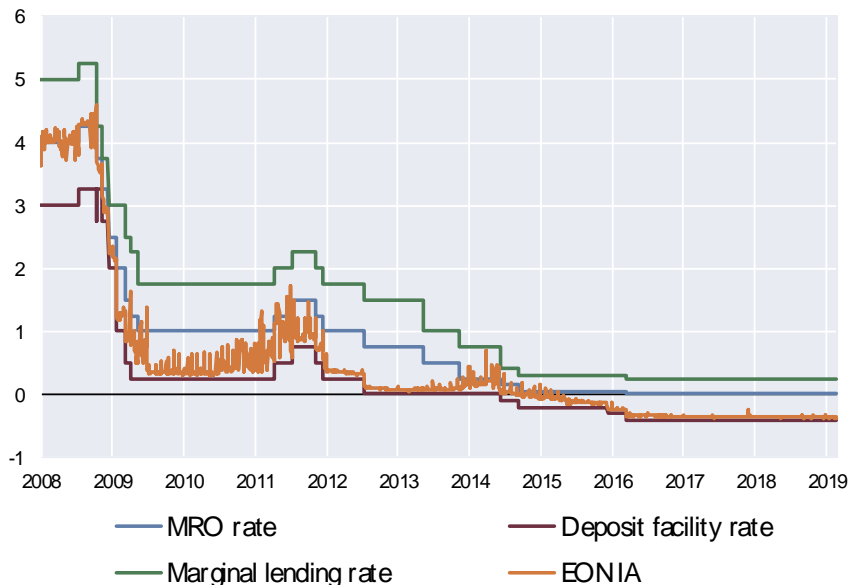


Source: Deutsche Bank Research, ESRB.

Historically low monetary policy rates in the euro area...

ECB key interest rates and money market rates

in %



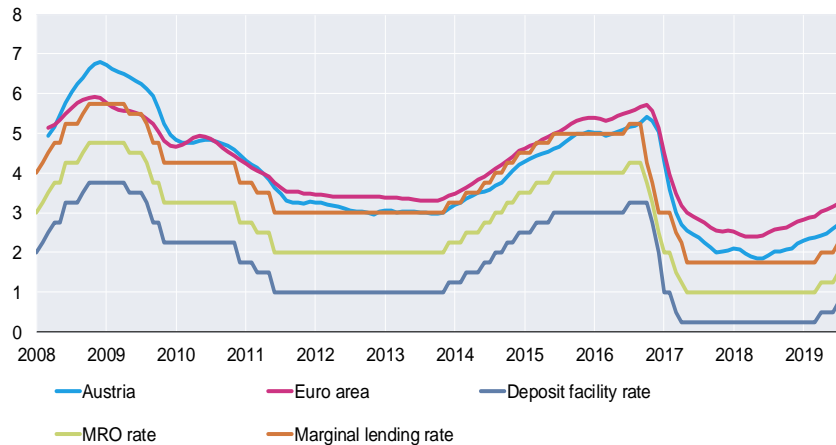
Source: ECB, Macrobond.

- Between 2008 and 2016, the ECB Governing Council decreased the interest rate of the main refinancing operation (policy rate) by 425 bps.
- Targeted longer-term refinancing operations (TLTROs): The outstanding TLTROs II have a term until 2020/2021. Banks in the eurozone still have 715 billion euros in these transactions. The average interest rate is -0.3650%.
- Full allocation in all tender transactions (with terms of 1 week or 3 months) until March 2021.
- Asset Purchase Program (APP): Between March 2015 and December 2018, the Eurosystem invested just under EUR 2,600 billion.

Monetary policy works: interest rate changes are passed on to customer interest rates

ECB key interest rate and retail lending rates for bank loans to NFC

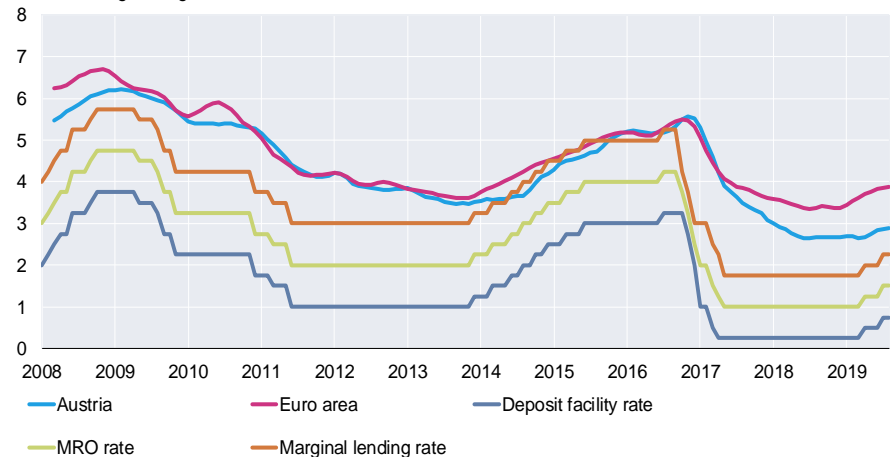
in %, moving average over 3 months



Source: ECB.

ECB key interest rates and retail rates for housing loans

in %, moving average over 3 months

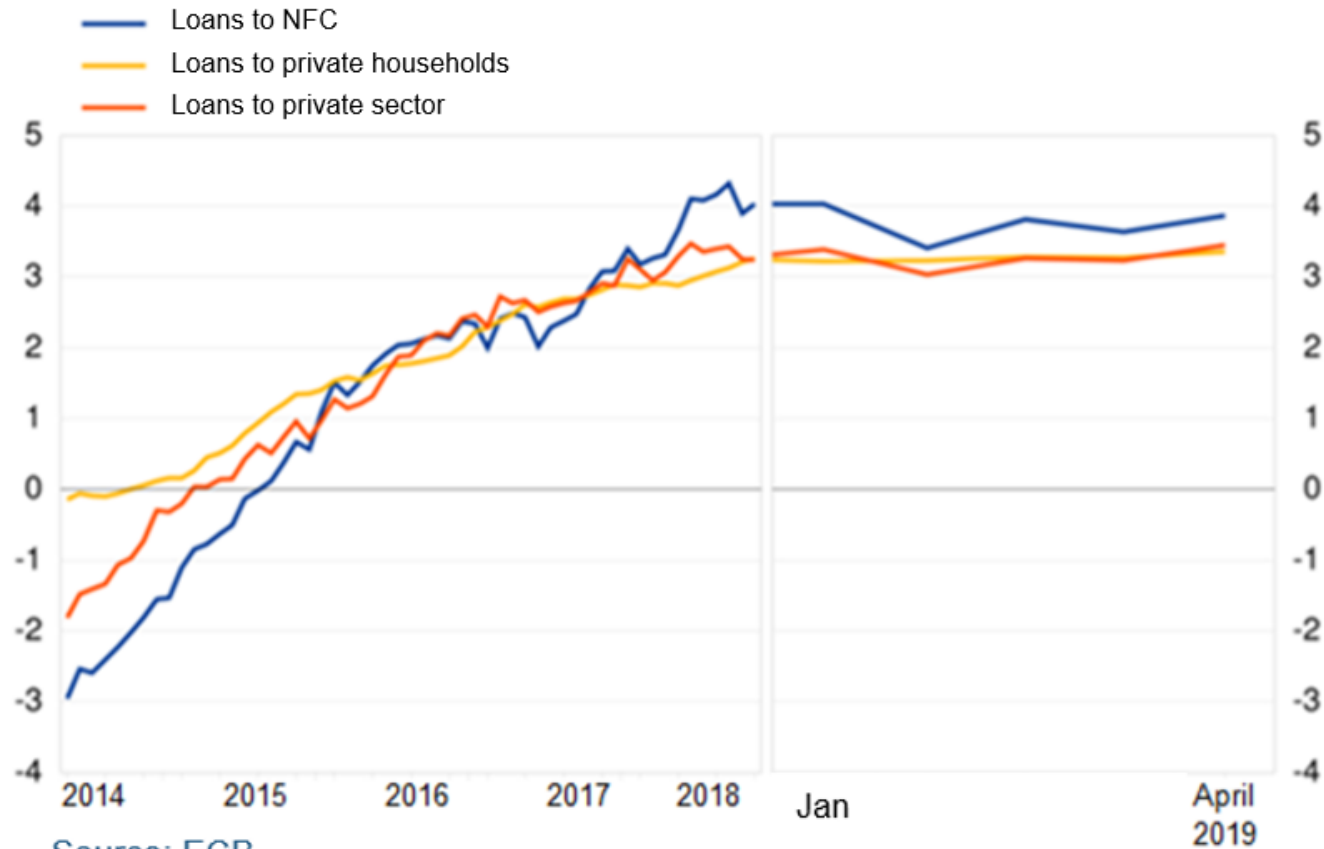


Source: ECB.

Monetary policy works: credit growth in the euro area has picked up

Adjusted loans to private sector

year-on-year change, in %

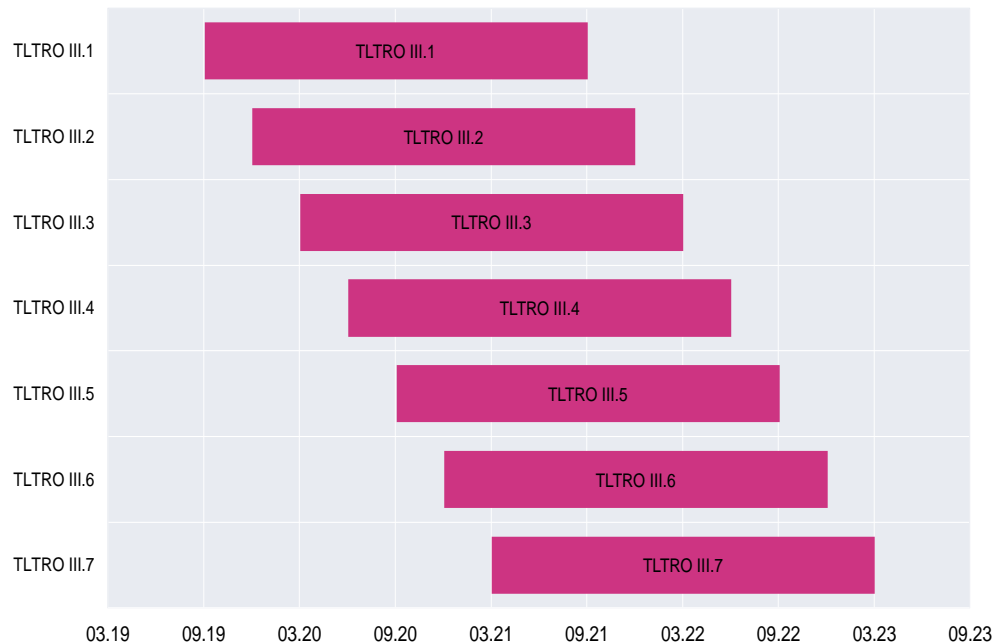


Monetary Policy Decisions of 12 September 2019

- **Lowering the deposit facility rate** by 10 basis points to -0.50%.
The MRO rate and the marginal lending rate remain unchanged at 0.00% and 0.25%, respectively.
- **Forward Guidance:** ECB key rates will remain at their current or lower levels until the inflation outlook over the projection horizon approaches a level that is sufficiently close, but below 2%.
- **Restart of asset purchase program (APP):** Net purchases will start at € 20 billion per month on 1 November.
- **Reinvestment:** The repayment amounts of the securities acquired under the APP will be fully reinvested for a longer period.
- Modification of the modalities of the new series of targeted longer-term refinancing operations - TLTROs: see next slide
- **Establishment of a two-tier system** for reserve remuneration, which exempts parts of banks' holdings of excess liquidity from the negative deposit facility.

The third generation of targeted longer-term refinancing operations (TLTROs III)

Timing of TLTROs III



Source: OeNB.

- From September 2019 to March 2021, each quarter a new targeted longer-term refinancing operation (TLTRO III) with a term of 3 years will be offered.
- Counterparties may receive up to 30% of eligible loans in the TLTRO III (less loans in the TLTRO II)
- The interest rate is based on the maturity of the individual transactions at the key policy rates (indexation):
Maximum: Interest rate in HRG
Minimum: Interest rate in the ELF (depending on the lending of each bank)
- Early repayments are possible after 2 years.

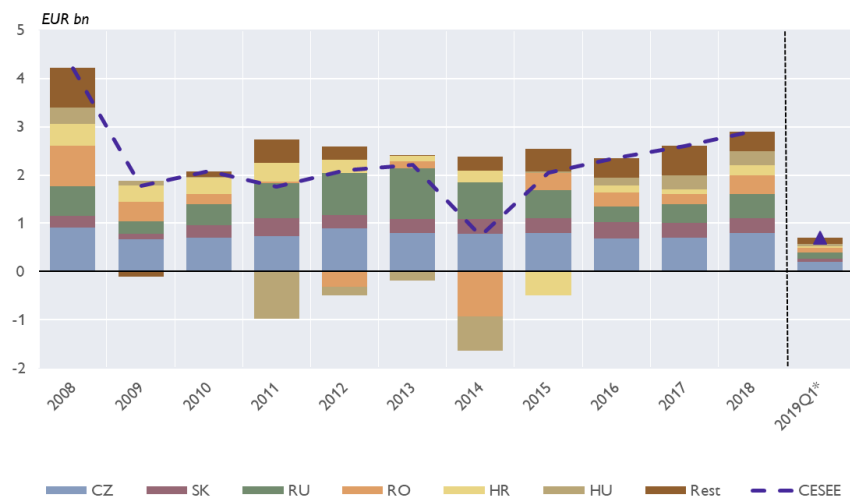
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- **Profitability of Austrian banks in CESEE**

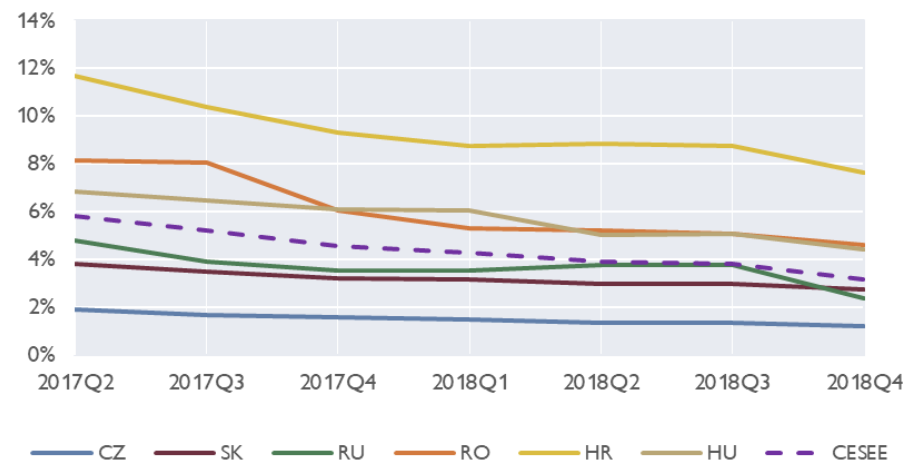
Profitability and credit quality of Austrian banks' subsidiaries in CESEE

Net result of Austrian subsidiaries in CESEE



Source: OeNB. * not comparable with year-end data.
From 2016 onwards figures do not include subsidiaries of UniCredit Bank Austria.

NPL ratios of Austrian subsidiaries in selected CESEE countries

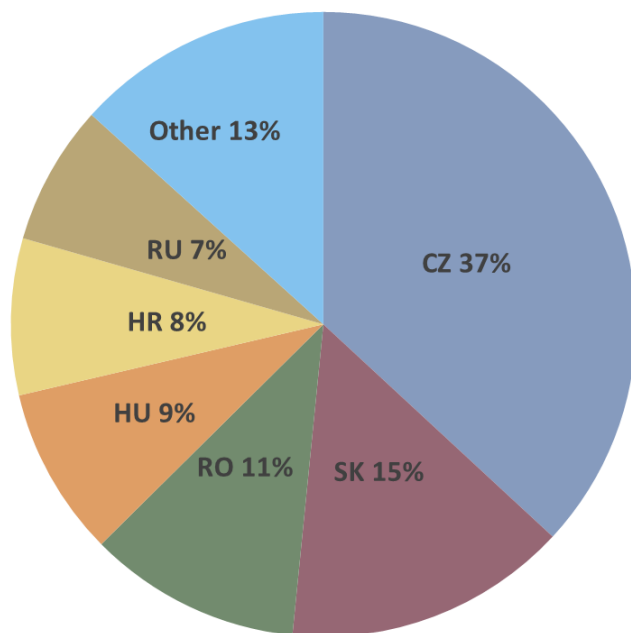


Source: OeNB.

Austrian banks' CESEE activities are concentrated on EU member states

Total assets of Austrian banking subsidiaries in CESEE (as of Q1 2019)

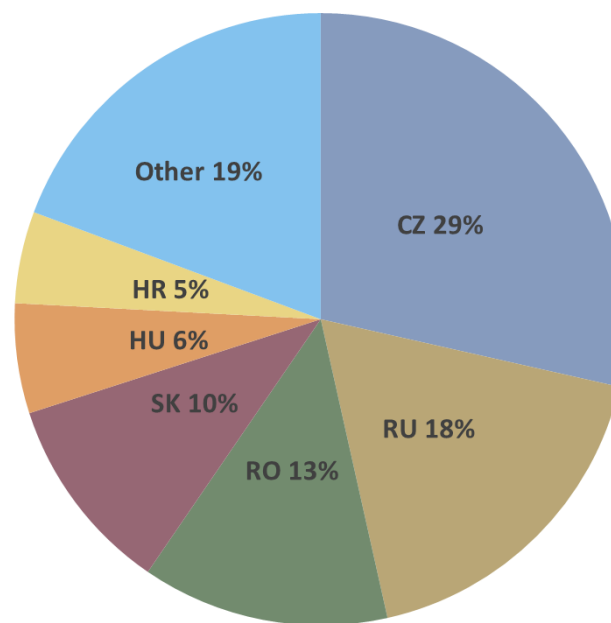
Total = EUR 211 bn



Source: OeNB.

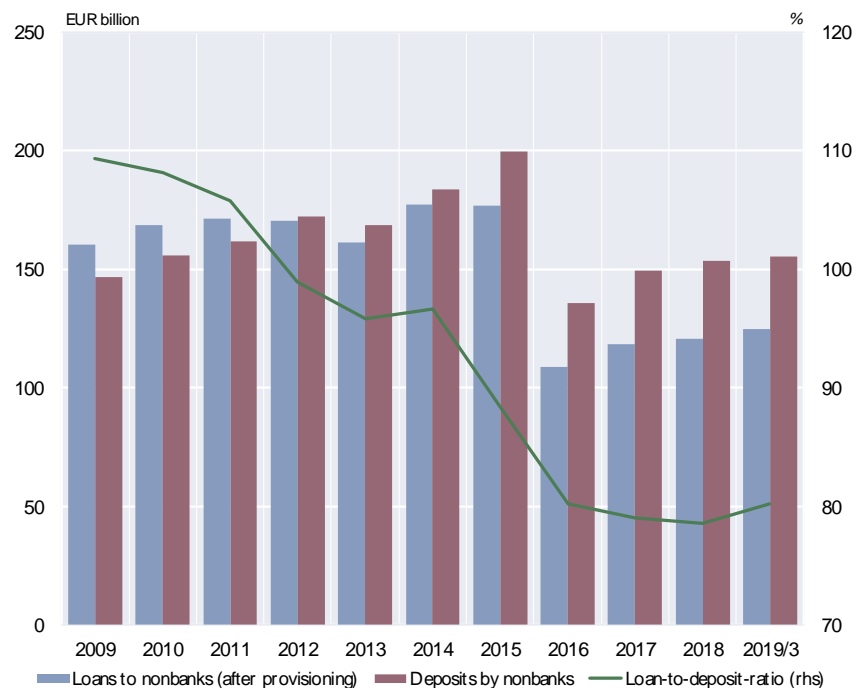
Profits of Austrian banking subsidiaries in CESEE (as of Q1 2019)

Total = EUR 0.7 bn



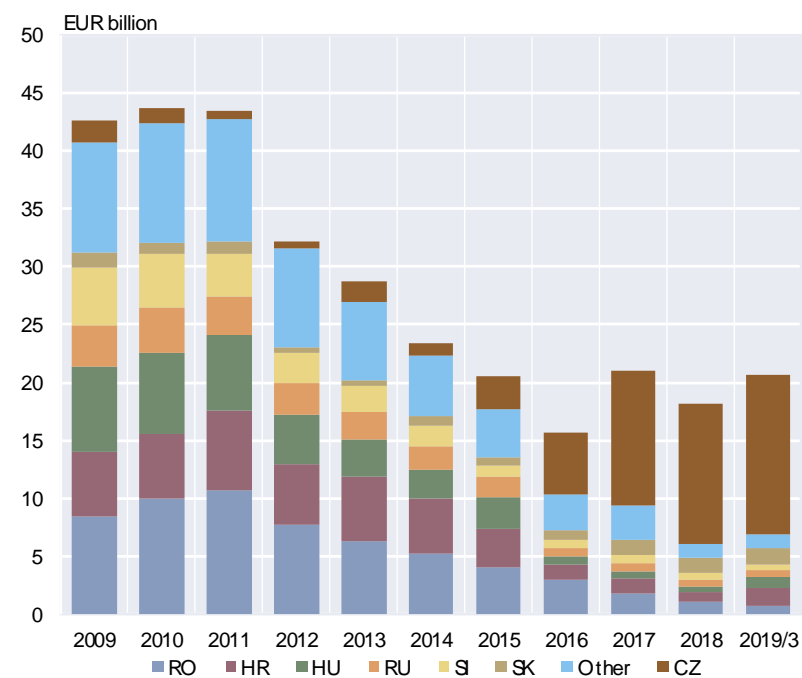
Local funding situation of Austrian subsidiaries in CESEE improved significantly

Local funding situation of Austrian subsidiaries in CESEE



Source: OeNB, variable bank sample (e.g. without Unicredit BA subsidiaries since 2016).

Intra-group liquidity transfers to CESEE credit institutions



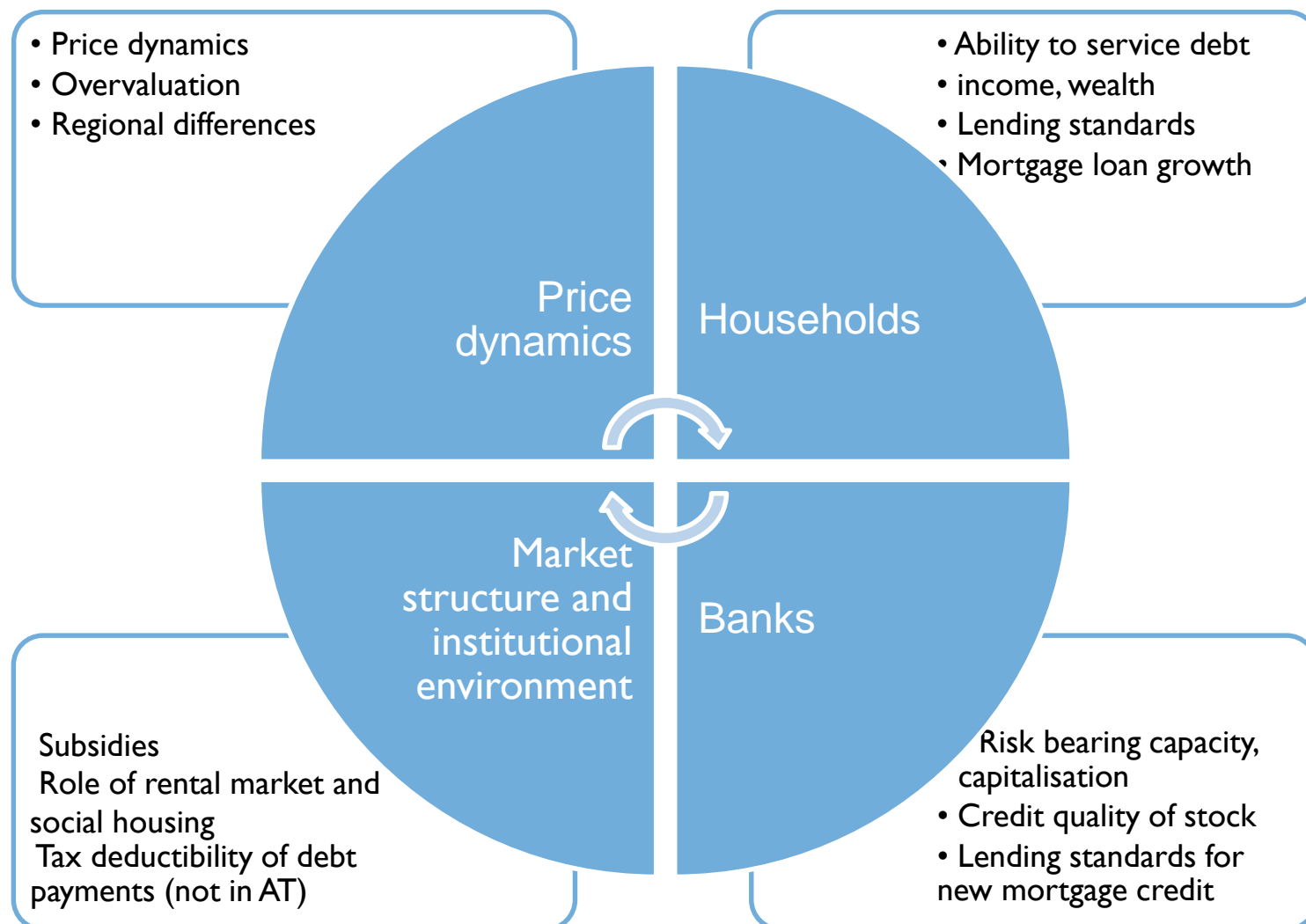
Source: OeNB.

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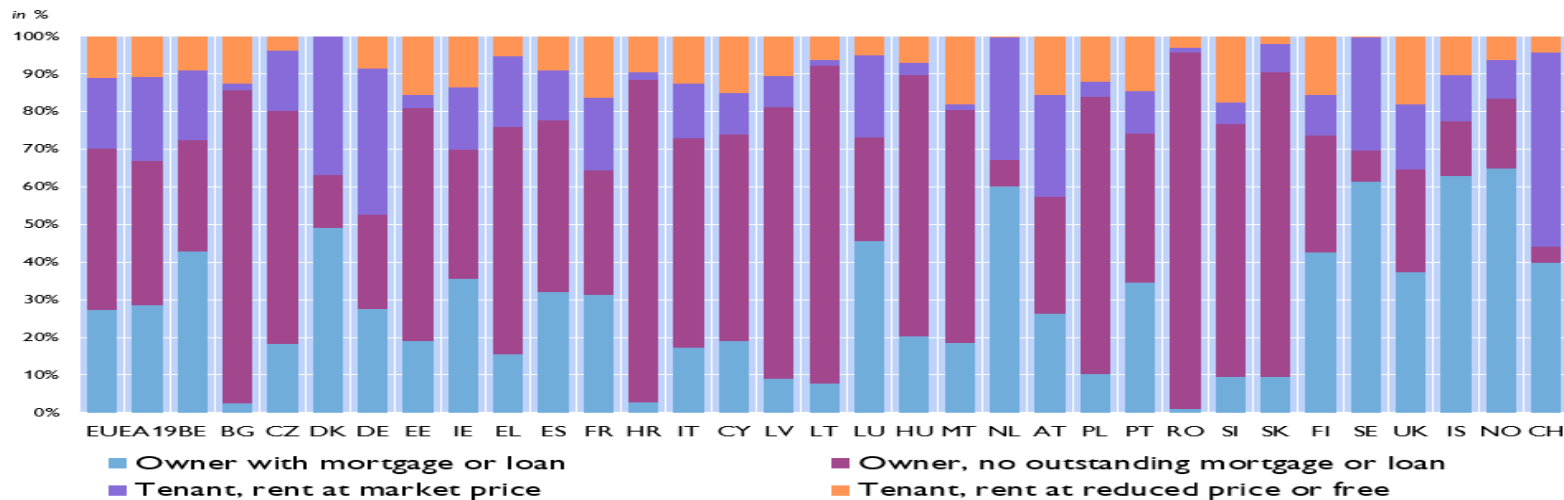
II. Systemic risk analysis in real estate

- **Four areas to analyze: price dynamics, market structure, households, banks**
 => Take out two of them:
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 The ESRB and its warnings

Dimensions of systemic risk analysis in real estate



Rental markets market shares vary in Europe a lot



Source: Eurostat.

=> Let's take a closer look on two areas:

- Borrower-based measures (LTV, DTI, DSTI)**

LTVs and DTIs effective in reducing loan-growth and improving debt-servicing performances of borrowers, but not always in curbing house price growth.

(f.e. Jacome and Mitra (2015). LTV and DTI Limits – Going Granular, IMF Working Paper WP/15/154)

- Regulation (incl. taxation) on the owner-occupied and the rental market**

Studies show that a high share of rental market stabilize house price fluctuations

(f.e., A. Czerniak, M. Rubaszek (2018). The Size of the Rental Market and Housing Market Fluctuations, Open Economies Review, April 2018,

Volume 29, Issue 2, pp 261–281.

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How market structure and institutional features influence property markets

The Austrian rental market

2017: 3.8 million households in Austria

- about **40% live in rented homes** (plus about 4% in sublet and other accommodation); thereof:
 - * ~ 20% in municipal apartments
 - * ~ 40% in apartments provided by limited-profit housing associations
 - * ~ 40% in apartments rented out privately
- Austrian legislation governing residential tenancy is **very complex** as different regulations apply depending on the time a building was erected, the type of subsidies granted, or the time the lease was signed.

How market structure and institutional features influence property markets

market policy instruments – the Austrian housing model

The Austrian housing model rests on **five pillars**:

1. The system of housing subsidies

Although about 80% of new housing units are currently being subsidized, these subsidies amount to only **1% of GDP**, which is comparatively low by Western European standards.

2. The legal framework consisting of private law, building regulations and property development regulations

3. The limited-profit housing associations

manage almost a quarter of the total Austrian housing stock, account for ~30% of residential building completions, for ~50% of rented and owner-occupied dwellings of multi-family houses

4. Building and loan associations

Government bonus system to ensure continued stream of savings; Over 4.4 million savers in 2 Q2019 (population: 8.8 million), penetration of ~ 50%; mortgage finance for family homes and multi-story residential buildings; long-term financing (up to 30 years); guaranteed capital and interest (minimum or fixed interest) after 6 years

and home loan banks issue long-term bonds that are exempt from investment income tax (up to 4% p.a.); funds are passed on as low-interest credit to the Austrian construction industry

5. The financial industry including property investment funds

How market structure and institutional features influence property markets

The (quite complex) Austrian residential tenancy act

- Austrian residential tenancy act distinguishes between **full and partial applicability** as well as **full exceptions**. Differences in full and partial applicability concern in particular **legal protection against the early termination of the lease** and the option for close relatives (who are already resident in the respective apartment and who can prove a need for own use) to enter into existing rental agreements.
- **Fully applicable to:** *buildings* with a building permit dated June 30, 1953, or earlier; *owner-occupied dwellings* with a building permit dated May 9, 1945, or earlier; buildings subsidized under the Austrian housing subsidy act of 1968; system of reference rents with various surcharges and deductions.
- **Partially applicable to:** non-subsidized buildings with a building permit dated after June 30, 1953; owner-occupied dwellings with a building permit dated *after* May 9, 1945; certain attic conversions since the adoption of the 2001 and 2006 amendments to housing legislation

How market structure and institutional features influence property markets

The effect of regulation on housing costs

| Housing Cost Burden (in % of household net income) | | | | |
|-----------------------------------------------------------|-------------------------------|--------|---------------------------|--------|
| | Not Subsidized Tenants | | Subsidized Tenants | |
| | Mean | Median | Mean | Median |
| 1st quartile | 53.0 | 42.7 | 48.0 | 40.1 |
| 2nd quartile | 34.1 | 33.0 | 30.7 | 29.2 |
| 3rd quartile | 28.3 | 26.7 | 24.8 | 25.0 |
| 4th quartile | 21.0 | 20.4 | 18.1 | 16.5 |
| Total | 35.7 | 30.7 | 32.0 | 29.1 |

Source: OeNB Housing Cost Survey 2012. Beer and Wagner (2012).

C.Beer und K.Wagner (2012), Housing Cost Burden of Austrian Households: Results of a Recent Survey

Monetary Policy and the Economy Q4/12, http://www.oenb.at/en/img/mop_2012_q4_analyses4_tcm16-253970.pdf

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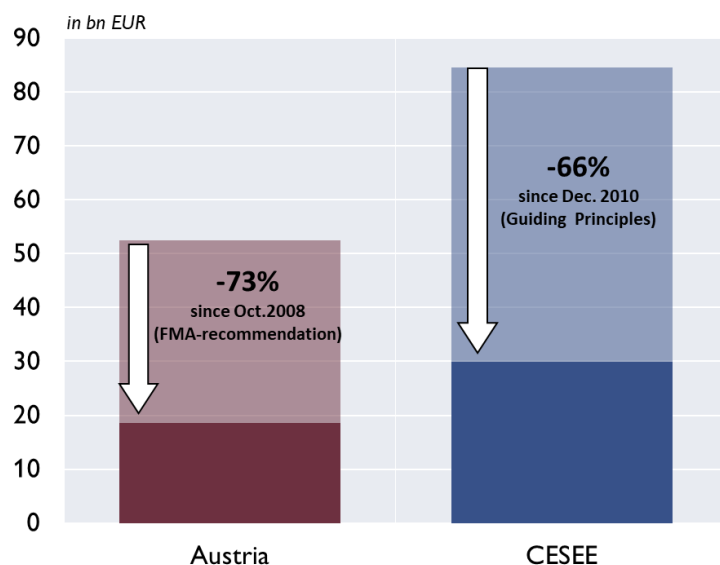
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How macroprudential authorities influence property markets

Foreign currency loans in Austria and CESEE continue to decline

Foreign currency loans of Austrian banks in Austria and CESEE*



Source: OeNB.

* loans to households and nonfinancial corporations

Note: Percentage values are FX-adjusted changes since the launch of macroprudential measures in Austria from October 2008 (FMA recommendation) to December 2018, in CESEE from December 2010 (Guiding Principles) to June 2018.

Austria

- FMA Minimum Standards for the Risk Management and Granting of FX and RPV Loans (2013), revision in 2017
- FMA recommendation to AT banks to refrain from any FX lending to unhedged borrowers (2008)
- Bilateral negotiations between banks and borrowers over measures to enable sustainable, tailor-made solutions and to reduce the risks stemming from FX loans.

CESEE

- Guiding Principles (2010): Commitment of AT banks to refrain from the riskiest forms of FX lending in CESEE
- Banks will not grant new loans in currencies other than the domestic currency or the Euro to unhedged private households and SMEs.
- Unilateral FX conversion measures in various countries increase business conduct risk for Austrian banks
 - Croatia, Hungary, Romania, Montenegro

How macroprudential authorities influence property markets

Austria: macroprudential policy actions since 2016

- Communications of FMA, OeNB and the Financial Market Stability Board (FMSG) on sustainable lending standards in the course of the year 2018: requirement for a 20% down payment, requirements on loan affordability (DSTI limit of between 30% and 40%), and maximum maturities (35 years).
- §22b Austrian Banking Act: Austrian authorities were given powers over legally binding instruments in 2017. These powers cover a wide range of tools (LTV, DSTI and DTI limits, and amortization criteria), they may be exercised should emerging vulnerabilities accelerate.
- Austrian authorities have positive experiences with effectiveness of non-binding measures/recommendations in the past (e.g. recommendations on FX loans, sustainability package).

=> The measures taken are currently considered sufficient by the ESRB to address residential property-induced systemic risk. Their effectiveness is constantly evaluated by FMA and OeNB; if the effectiveness proves to be low and systemic risks become significant, the FMSG had already announced that measures will be tightened.

How macroprudential authorities influence property markets

European Systemic Risk Board (ESRB) issued warnings on medium-term residential real estate vulnerabilities

- November 2016 country-specific warning to 8 countries:
AT, BE, DK, FI, LU, NL, SE and UK
- September 2019 warnings to 5 countries with measures considered inadequate:
CZ, DE, FR, IS, NO

recommendations to all countries that received a warning in 2016 and for which the capitalized measures are considered inadequate:
BE, DK, FI, LU, NL, UK, SE

<https://www.esrb.europa.eu/news/pr/date/2019/html/esrb.pr190923~75f4b1856d.en.html> (accessed on 10 Oct 2019)

How macroprudential authorities influence property markets

ESRB warning for CZ

The ESRB sees a risk in

- Overvaluation and continued credit growth
- Doubts about the sustainability of the procurement standards in CZ

It justified the warning mainly with the missing legal framework in CZ. Although the Czech central bank has actively taken measures and has regularly tightened these measures, *“the current borrower-based measures have been introduced on the basis of a recommendation from CNB which is not legally binding, and there is no legal framework in place to activate these measures through legally binding acts”*.

https://www.esrb.europa.eu/pub/pdf/warnings/esrb.warning190923_cz_warning~bd479e5cb1.en.pdf
(accessed on 10 Oct 2019)

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III. Conclusions

Conclusions

Macroeconomic relevance

- Real estate is the most important asset of households. The share of real estate ownership in total household wealth is 50-70% on average in Europe.
- Housing prices influence private household consumption and investment decisions through wealth effects.
- Housing expenses are a relevant part of total household expenditure → Housing prices affect purchasing power.
- Construction industry plays an important role in the economy; Real estate booms can distort aggregate production structure (e.g. Spain)

Real estate markets and prices are closely linked to the financial system and stability

- Buying property often (at least partially) credit-financed → Impact on debt situation and credit sustainability of households.
- Mortgage loans play an important role in banks' balance sheets.
- Real estate bubbles and crashes pose a threat to financial market stability.

As shown central banks/financial market authorities and economic policy institutions can influence price and lending developments in the housing and financial markets