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EUROPEAN
COMMISSION

Brussels, 11.7.2023
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COMMISSION DECISION

of 11.7.2023

not to propose an implementing act to reject the draft national measure concerning risk weights for targeting asset bubbles in the residential property and commercial immovable property sector notified on 12 May 2023 by Sweden under Article 458(4) of Regulation (EU) No 575/2013 of the European Parliament and of the Council

(Text with EEA relevance)

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THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union,

Having regard to Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and amending Regulation (EU) No 648/2012[1], and in particular Article 458 thereof,

Having regard to the opinions of the European Systemic Risk Board[2] and of the European Banking Authority[3],

Whereas:

(1) On 12 May 2023, Finansinspektionen, the Swedish Financial Supervisory Authority (the 'FSA'), which is the national designated authority in charge of the application in Sweden of Article 458 of Regulation (EU) No 575/2013, notified the Commission and the European Systemic Risk Board (the 'ESRB'), in accordance with Article 458(2) of that Regulation, of its intention to implement a draft national measure concerning risk weights for targeting asset bubbles in the residential property and commercial immovable property sector (the 'Notification'). More in particular, the draft national measure consists of the imposition of an exposure-weighted average risk weight floor of 35% for corporate exposures secured by commercial properties physically located in Sweden that generate a rental income, and of an exposure-weighted average risk weight floor of 25% for corporate exposures secured by residential properties physically located in Sweden that generate a rental income (jointly referred to as 'CRE exposures'). The draft national measure would be applicable to all credit institutions authorised in Sweden using the Internal Ratings Based (IRB) approach for calculating regulatory capital requirements. The draft national measure is planned to enter into force on 30 September 2023 and would be applicable for 2 years.

(2) Pursuant to Article 458(4), second subparagraph, of Regulation (EU) No 575/2013, the ESRB and the European Banking Authority (the 'EBA') are to provide the Council, the Commission and the Member State concerned, within 1 month of receiving a

1 OJ L 176, 27.6.2013, p.1.

2 Opinion of the European Systemic Risk Board of 9 June 2023 regarding Swedish notification of a stricter national measure based on Article 458 of Regulation (EU) No 575/2013 of the European Parliament and of the Council on prudential requirements for credit institutions (ESRB/2023/3).

3 Opinion of the European Banking Authority on measures in accordance with Article 458 Regulation (EU) No 575/2013 of 12 June 2023 (EBA/Op/2023/06).

notification as referred to in paragraph 2 of that Article, with their opinion on draft national measures. On 9 June 2023, the ESRB adopted its opinion on the draft national measure (the 'ESRB opinion'). The EBA adopted its opinion on 12 June 2023 (the 'EBA opinion').

(3) Article 458(2) of Regulation (EU) No 575/2013 requires that a national authority that wishes to apply a national measure as referred to in Article 458(2), point (d), of that Regulation submits to the Commission and the ESRB relevant quantitative and qualitative evidence showing that the criteria set out in paragraph 2 of that Article are fulfilled. Under Article 458(4), third subparagraph, of Regulation (EU) No 575/2013, the Commission has to consider that evidence before proposing to the Council an implementing act to reject the draft national measure concerned. The Commission has thereby to assess whether there is sufficient evidence of a continued heightened systemic risk and whether such risk poses a threat to the financial system and the real economy of the Member State concerned. The Commission has also to assess the suitability, effectiveness, and proportionality of the draft national measure, and the availability of alternative measures and macroprudential instruments. Pursuant to that same provision, the Commission may propose to the Council an implementing act to reject the draft national measure where, taking utmost account of the opinion of the ESRB and the EBA, there is robust, strong, and detailed evidence that the draft national measure will have a negative impact on the internal market that outweighs the financial stability benefits resulting in a reduction of the macroprudential or systemic risk identified.

(4) The FSA identified an elevated and increasing systemic risk that originates from the Swedish commercial real estate ('CRE') sector, namely from corporate exposures secured by commercial or residential real estate properties that generate rental income. Over the recent years, the FSA has noted a significant increase in CRE property prices in Sweden, in parallel with high and further increasing indebtedness of CRE firms. A tightening in financing conditions in future or a worsened macroeconomic situation may impair the ability of CRE firms to service their debts. According to the FSA, the CRE sector is closely connected with the financial system, as lending to the CRE sector constitutes about 50 % of total credit institutions' lending to non-financial corporations in Sweden. Potential losses for credit institutions can therefore be high. The FSA also notes that the CRE sector played a significant role in past major financial crises, including in Sweden.

(5) In January 2023, the ESRB acknowledged in its report titled "Vulnerabilities in the EEA commercial real estate" the importance of the CRE sector for financial stability. The ESRB also issued Recommendation ESRB/2022/9, in which authorities in charge of financial stability were recommended to closely monitor vulnerabilities stemming from the CRE market and, where necessary, to address those vulnerabilities, by activating capital-based macroprudential measures to increase the resilience of credit institutions. The ESRB determined that risk weight measures would be suitable in a scenario of varying or continuously declining risk weights for CRE loans.

(6) The ESRB and the EBA, in their opinions, concurred with the assessment of the FSA that the Swedish CRE sector is a source of systemic risk to the Swedish financial system and its national economy.

(7) The Commission has carefully considered the evidence provided by the FSA and has taken utmost account of the views of the ESRB and the EBA in their respective opinion. The Commission considers that there is sufficient evidence as regards the

required change in the intensity of macroprudential or systemic risk, which could pose a threat to the financial system in Sweden and its national economy, which is one of the conditions laid down in Article 458(2), points (a) and (b), of Regulation (EU) No 575/2013 for the application of that provision. The intensity of that risk is such that it justifies the implementation of a capital-based macroprudential measure, which should increase the resilience of Swedish credit institutions.

(8) With the implementation of the draft national measure, the FSA aims to increase resilience in the Swedish financial system in relation to the systemic risk that is connected to the Swedish CRE sector. The FSA notes that for credit institutions that use the IRB approach, the average (exposure-weighted) risk weight is around 17 % for corporate exposures secured by commercial real estate, and 13 % for corporate exposures secured by residential real estate, which may not be adequate and sufficient in light of the that systemic risk. The FSA is therefore of the view that the systemic risk can be best addressed by a risk weight floor that ensures appropriate loss absorbency of Swedish credit institutions for the CRE exposures concerned.

(9) The FSA views the draft national measure as suitable in terms of ensuring that credit institutions hold enough capital to withstand any potential disruptions in the CRE sector that could otherwise affect credit institutions’ financial position and the real economy in general. According to the Notification, the draft national measure is proportionate and effective, as it targets the CRE exposures of credit institutions that apply the IRB approach where such exposures may create systemic risk. The FSA is of the view that the draft national measure increases resilience without imposing an excessive burden, and that it is designed and calibrated to be sufficiently precise in targeting exposures to the CRE sector by credit institutions that apply the IRB approach. Furthermore, to ensure proportionality, the draft national measure exempts properties where more than 50 % of the surface is not used for producing rental income, agricultural properties, properties owned by the government or by housing associations, and multi-dwelling properties that have less than four dwellings. For the same reason, the FSA proposes a differentiation of the risk weight floor between exposures secured by commercial and residential properties, with a lower risk weight floor for exposures secured by residential properties which, according to the FSA, are less risky.

(10) The Commission has considered the suitability, effectiveness, and proportionality of the draft national measure. The Commission considers that the draft national measure is proportionate, in so far as its design does not go beyond what is necessary to address the identified systemic risk. In terms of its effectiveness and suitability, the Commission considers that draft national measure is suitable and effective as it will address the risk and vulnerabilities stemming from the exposures to risks from the CRE sector of credit institutions that apply the IRB approach and will strengthen credit institutions' resilience to a potential economic downturn or disruptions in the real estate sector.

(11) Article 458(2), point (c), of Regulation (EU) No 575/2013 requires the national competent authority to justify why the macroprudential tools set out in Articles 124 and 164 of that Regulation and Articles 133 and 136 of Directive 2013/36/EU of the

European Parliament and of the Council[4] are less suitable and effective to deal with the macroprudential or systemic risk identified.

(12) Article 124 of Regulation (EU) No 575/2013 allows the competent authorities to set higher risk weights for exposures secured by mortgages on immovable property where the standardised approach is used for calculating the own funds requirements for credit risk. The draft national measure, however, addresses risk emanating in credit institutions that use the IRB approach, which means that that provision is not applicable to such risks. Swedish credit institutions applying the standardised approach must assign a minimum risk weight of 50 % to their exposures secured by commercial real estate in Sweden, and a minimum risk weight of 35% to their exposures secured by residential real estate, which is well above the proposed floor levels for credit institutions that apply the IRB approach. Under Article 164 of Regulation (EU) No 575/2013, competent authorities may set higher minimum values of exposure weighted average loss given default (LGD) for retail exposures secured by immovable property in their territory. Article 164 is, however, not applicable to corporate exposures of credit institutions that use the IRB approach.

(13) As regards the countercyclical capital buffer (CCyB) set out in Article 136 of Directive 2013/36/EU, the FSA considers that the CCyB is not an appropriate tool to address sectoral systemic risk, as it would apply to all exposures in Sweden and not only to Swedish CRE exposures. This would result in penalising also exposures which are not the source of the systemic risk. Thus, increasing the CCyB would not adequately address the identified risk in an effective and proportionate way.

(14) Article 133 of Directive 2013/36/EU allows Member States to introduce a systemic risk buffer (SyRB) to prevent and mitigate systemic or macroprudential risks not covered by either Regulation (EU) No 575/2013 or Articles 130 and 131 of Directive 2013/36/EU. Like the CCyB, a SyRB applied on all exposures of the credit institution or all its exposures in Sweden would have a disproportionate impact beyond the risk identified in the CRE sector. While the SyRB can also be targeted to a subset of exposures, to have the same impact as the draft national measure in absolute terms, the SyRB buffer rate would have to vary across credit institutions between 20 – 40 % for exposures secured by commercial real estate and between 10 – 25 % for residential real estate and also vary over time. According to the FSA, such a SyRB would be cumbersome to calibrate and monitor. Alternatively, a single SyRB rate applicable to all credit institutions applying the IRB approach would impact most heavily those credit institutions that have the highest risk weights, which is not desirable as the draft national measure intends to address risk in credit institutions with low risk weights. The ESRB is also of the view that a SyRB would not be efficient in preventing a further decline in risk weights, compared to the risk weight floor proposed in the draft national measure.

(15) The draft national measure is intended to replace a similar measure that was introduced in 2020 as a Pillar 2 requirement. Taking into consideration the increasing systemic relevance of CRE exposures which is not allowed to be addressed by Pillar 2 measures, and the variation in risk weights between individual credit institutions that

[4] Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC (OJ L 176, 27.6.2013, p. 338).

are expected to persist until the FSA completes its review of of the IRB models used by the credit institutions, the FSA considers that a macroprudential measure is more appropriate to address the vulnerabilities identified. Furthermore, the FSA notes that Pillar 2 requirements are set only annually, which limits their possibility to reflect actual evolution of risk weights in a timely manner and that competent authorities in other Member States cannot apply those measures to their credit institutions that are exposed to risks in Sweden.

(16) After having examined the arguments and evidence put forward by the FSA, and having taken utmost account of the opinions of the ESRB and of the EBA, the Commission considers that the measures referred to in Articles 124 and 164 of Regulation (EU) No 575/2013, as well as the tools referred to in Articles 133 and 136 of Directive (EU) 2013/36, appear less suitable than the draft national measure in addressing the identified specific systemic risk in a suitable, effective and proportionate manner. That assessment is shared by the ESRB and the EBA.

(17) Article 458(2), point (f), of Regulation (EU) No 575/2013 requires that the national authority assesses the likely impact of a draft measure on the internal market. According to the FSA, the impact would be positive as sustained resilience of Swedish credit institutions would allow those credit institutions to continue lending to the real economy also in other Member States where those institutions are active, if the risks to the Swedish CRE sector were to materialise. The FSA also notes a limited impact on overall capital requirements of Swedish credit institutions that would be subject to the draft national measure, because that measure is replacing a Pillar 2 measure with a broadly similar impact on capital requirements. The FSA observes that the risk weights of credit institutions that are located in other Member States which have exposures to the Swedish CRE sector are generally above the risk weight floors proposed in the draft national measure.

(18) Neither the ESRB nor the EBA identify in their opinions a possibility of a negative impact on the internal market. The Commission concurs with that assessment and notes that reciprocity of the draft national measure by authorities in other Member States would, besides ensuring sufficient resilience of credit institutions in those Member States that have exposures to the Swedish CRE sector, also ensure a level playing field for credit institutions in the Union.

(19) According to the ESRB opinion, the draft national measure may help to maintain resilience in Swedish credit institutions that apply the IRB approach, and thus mitigate a possible materialisation of systemic risk in the Swedish CRE sector. Based on the evidence provided by the FSA and acknowledging that CRE activity levels in the Swedish economy have increased substantially in the last years, which increases the risks for financial stability, the EBA considers that the draft national measure could help Swedish credit institutions that apply the IRB approach to weather the challenges that might stem from the CRE sector. As such, neither the ESRB, nor the EBA object to the implementation of the draft national measure. The EBA opinion acknowledges that the FSA decided to replace a Pillar 2 measure with a macroprudential one, the Pillar 2 measure being a credit institution-specific capital requirement tailored to a credit institution's risk profile, while the macroprudential measure is not specific to a credit institution's risk profile. The EBA notes the need to distinguish between institution specific risk, including from internal model deficiencies, and financial stability risks. The Commission concurs with that view. To that extent, while the Commission notes that macroprudential measures should not, in principle, substitute

microprudential action, it acknowledges the systemic risks identified by the FSA and the macroprudential objectives of the draft national measure in this particular case.

(20) The Commission, after having examined the arguments and evidence put forward by the FSA and after having taken utmost account of the opinions of the ESRB and the EBA, concludes, on the basis of its assessment, that there is no robust, strong and detailed evidence that the draft national measure proposed by the FSA will have a negative impact on the internal market that outweighs the financial stability benefits resulting from a reduction of the macroprudential or systemic risk identified. The Commission nevertheless stresses the importance of closely monitoring the evolution of systemic risks related to the Swedish CRE sector and of the IRB risk weights proposed in the draft national measure, and points to the need for a periodic evaluation by the FSA of the necessity, effectiveness, suitability and proportionality of the draft national measure and its calibration,

HAS DECIDED AS FOLLOWS:

Sole Article

The Commission does not propose to the Council an implementing act to reject the draft national measure notified by Sweden on 12 May 2023 in accordance with Article 458(4) of Regulation (EU) No 575/2013, to be applicable from 30 September 2023 until 29 September 2025.

Done at Brussels, 11.7.2023

For the Commission
Mairead McGUINNESS
Member of the Commission