FJÁRMÁLAEFTIRLITIÐ
THE FINANCIAL SUPERVISORY AUTHORITY, ICELAND

Reykjavík, 15 May 2018.

Financial Supervisory Authority's decision on raising the countercyclical capital buffer

On 1 November 2016, the Financial Supervisory Authority decided to impose a 1.25% countercyclical capital buffer in accordance with Article 86(d) of Act No 161/2002 on Financial Undertakings.[1] The financial undertakings subject to the buffer have therefore maintained the 1.25% countercyclical capital buffer since 1 November 2017. The capital buffer has been maintained on a consolidated basis and it covers all domestic exposures.

The Financial Stability Council is tasked with reviewing the countercyclical buffer rate every quarter in accordance with Article 86(d)(1) of Act No 161/2002 on Financial Undertakings. On 13 April 2018, the Council submitted a recommendation to the Authority that the countercyclical capital buffer be raised to 1.75%.

On 15 May 2018, the Authority decided to raise the countercyclical capital buffer in accordance with the recommendations of the Council.

The Authority has today announced its decision to the undertakings concerned and is hereby making the announcement public in accordance with Article 86(d)(1) of the Act on Financial Undertakings.

Decision on raising the countercyclical capital buffer

Among other things, the recommendations of the Council state that the primary purpose of the countercyclical capital buffer is to increase the resilience of the financial system against potential losses due to the accumulation of cyclical systemic risk. They further state that during a financial downturn, releasing the buffer provides financial undertakings with the margin to maintain a sustainable supply of credit. The countercyclical capital buffer should therefore be changed in reflection of developments in cyclical systemic risk.

As provided for in Article 136(2) of Directive 2013/36/EU of the European Parliament and of the Council, the Financial Stability Council considers the deviation of the ratio of liabilities to GDP from its long-term trend and the standard buffer guide of the Basel Committee for Banking Supervision in its recommendations.

[1] See the recommendations of the Financial Stability Council from 30 September 2016.

The Council also considers several other indicators to obtain a clear overview of cyclical systemic risk. The financial cycle has already entered an expansion phase and the development of cyclical systemic risk warrants continued build-up of the countercyclical capital buffer. The continuous growth in household and corporate debt for the past year is an indicator of increased cyclical systemic risk. At the same time, housing prices have deviated from fundamentals, which further supports raising the buffer. Risk has also increased in confined sectors where no targeted policy responses are available at present. Of particular note are the sharp uptick in the bank funding cycle and the interaction between commercial property lending, real estate development projects and high commercial property prices. It is furthermore noted that, at least for the present, supervisory bodies are facing difficulties in assessing the need for applying targeted policy instruments in the housing market and the impact of their application. If using specific measures in response to the abovementioned risk factors becomes an option in subsequent quarters, the Authority will review whether they are called for and what impact their application will have on the rate of the countercyclical capital buffer. Such a review may be conducted before the entry into force of the present decision.

Considering the foregoing and the recommendation of the Financial Stability Council, the Authority imposes a countercyclical capital buffer of 1.75% on domestic exposures of all financial undertakings, both individually and on a consolidated basis, unless they are specifically excluded from the buffer according to Article 86(d)(4) of the Act on Financial Undertakings. The calculation of the own funds requirements shall reflect the weighted average of the countercyclical capital buffer rates that apply domestically and in other EEA-States, in accordance with each country's share of the exposure, pursuant to Article 86(d)(3) of the same Act.[2]

[2] The Financial Supervisory Authority will introduce rules implementing the regulatory technical standards in Commission Delegated Regulation (EU) No 1152/2014 that further prescribes the calculations, cf. Consultation Paper No 4/2016 available on the Authority's website. In addition, the Financial Supervisory Authority has laid down Rules No 506/2017 implementing the regulatory technical standards in Commission Delegated Regulation (EU) 2015/1555.