

Statement of the Financial Stability Committee 29 September 2021

The economic recovery of the past few months, coupled with an accommodative monetary and macroprudential stance, has supported households and businesses. On the other hand, asset prices – equity securities and real estate prices in particular – have risen markedly.

The three large banks are strong, their capital and liquidity are well above regulatory minima, and they have ready access to liquidity in both krónur and foreign currencies. As a result, they are highly resilient.

In recent months, the rapid rise in house prices has gone hand-in-hand with increased household debt. Therefore, with the aim of containing long-term systemic risk, the Financial Stability Committee (FSN) has decided to adopt rules on maximum debt service-to-income (DSTI) ratios, as is provided for in Article 27 of the Act on Mortgage Lending to Consumers, no. 118/2016. In general, the maximum DSTI ratio shall be 40% for first-time buyers and 35% for all other borrowers. The ratio shall be calculated based on a specified maximum loan maturity. Lenders are granted an exemption from the rules for up to 5% of the total amount of new mortgage loans issued each quarter.

Uncertainty about financial institutions' position has receded, and loan quality has improved. As a result, financial institutions are resilient enough to lend to households and businesses. In the FSN's opinion, the scope it had granted to financial institutions after the pandemic reached Iceland, in the form of a reduction in the countercyclical capital buffer (CCyB), is no longer needed. The FSN is of the view that the combination of rapidly rising asset prices and increased household debt has already raised cyclical systemic risk to at least the pre-pandemic level. As a consequence, in view of the build-up of cyclical systemic risk, the FSN has decided to increase the CCyB from 0% to 2%. This decision will take effect twelve months from now, in accordance with the rules that apply to the countercyclical capital buffer. The CCyB proved its worth during the pandemic, and the Committee has given consideration to what a neutral buffer value should be in the future.

The FSN has concluded its annual review of the capital buffer for systemic importance (O-SII buffer) and has decided to hold it unchanged at 2% for all exposures at the parent company and the group level. The review of systemically important financial institutions, carried out in accordance with European Banking Authority methodology, confirmed the systemic importance of Arion Bank hf., Íslandsbanki hf., and Landsbankinn hf.

In view of recent cyberattacks and operational disruptions in payment intermediation, the FSN urges operating entities to examine the security

of their systems and take steps to ensure business continuity. The Committee is of the view that, alongside payment cards, Iceland needs to have in place a domestic electronic retail payment solution that is independent of international financial infrastructure. This will bring increased operational security and efficacy. The Central Bank is preparing for the implementation of such a solution.

The Financial Stability Committee will continue to use every tool at its disposal to safeguard financial stability in Iceland.