



NORGES BANK

Ministry of Finance
P.O. Box 8008 Dep
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Advice on the countercyclical capital buffer 2018 Q2

Norges Bank's Executive Board has decided to advise the Ministry of Finance to keep the buffer rate unchanged at 2 percent.

Norges Bank is responsible for preparing a decision basis and advising the Ministry of Finance on the level of the countercyclical capital buffer for banks four times a year. The decision basis for Norges Bank's advice in 2018 Q2 is presented in the June 2018 *Monetary Policy Report*.

Banks should build up and hold a buffer when financial imbalances are building up or have built up. Financial imbalances increase the risk of an abrupt decline in demand and bank loan losses. The buffer rate may be reduced in the event of an economic downturn and large bank losses, with a view to mitigating the procyclical effects of tighter bank lending.

Norges Bank's assessment of financial imbalances is based on developments in credit and property prices and banks' wholesale funding ratios. The buffer rate is not an instrument for fine-tuning the economy and should not be reduced automatically even if there are signs that financial imbalances are receding. Advice to reduce the rate will be based on factors such as information about market turbulence, and prospects for substantial bank losses and significant credit supply tightening.

Large Norwegian banks are posting solid profits and low losses, and meet the total Common Equity Tier 1 (CET1) capital requirement. At the end of 2018 Q1, capital ratios were in line with banks' long-term targets. Banks have ample access to wholesale funding, and wholesale funding ratios have been stable for a long period.

Household debt has long risen faster than income. In recent months, household debt growth has edged down. The requirements in the mortgage lending regulation may limit the rise in debt among highly indebted households. The Ministry of Finance has recently decided to retain the regulation on requirements for new residential mortgage loans. In Norges Bank's Survey of Bank Lending for 2018 Q1, banks reported that no changes in credit standards for households and enterprises were expected in 2018 Q2.



Corporate credit growth picked up through 2017, in line with an upswing in investment. Corporate credit growth has held up so far in 2018, but is not particularly high compared with previous periods. The rise in corporate credit is broadly based and has picked up from both banks and the bond market.

After declining in 2017, house prices have risen again in 2018. House price inflation has been high over the past two months. In the commercial real estate market, the rise in selling prices for prime office space in Oslo continued, following a pronounced rise over several years. In other segments of the Oslo office market, selling prices also increased at a faster rate in 2017.

The countercyclical capital buffer rate is currently set at 2 percent. This rate reflects the build-up of financial imbalances resulting from a persistent rise in household debt ratios and high property price inflation over a long period.

The upswing in the Norwegian economy and continued low interest rates entail a risk of high house price inflation ahead. This may lead to a renewed rise in household sector debt growth and vulnerabilities. On the other hand, an increase in the interest rate level will help curb debt growth. The pronounced rise in commercial real estate prices in recent years has increased the risk of marked value declines further out. A continued rise in residential and commercial property prices that leads to an increase in financial imbalances may indicate a need to raise the countercyclical capital buffer rate.

On the basis of an overall assessment, Norges Bank's Executive Board has decided to advise the Ministry of Finance to keep the buffer rate unchanged at 2 percent. The decision was unanimous.

In preparing its advice on the countercyclical capital buffer, Norges Bank has exchanged information and assessments with Finanstilsynet (Financial Supervisory Authority of Norway).

Sincerely,

Øystein Olsen

Torbjørn Hægeland

Copy: Finanstilsynet