



FINANCIAL STABILITY COUNCIL

Ministry of Finance and Economic Affairs, Arnarhvoli, 150 Reykjavik

Tel: (+354) 545 9200

[www.ministryoffinance.is/financialstability](http://www.ministryoffinance.is/financialstability)

Reykjavik, 26 September 2019

### **Recommendation on countercyclical capital buffer**

On a quarterly basis, the Financial Stability Council shall submit recommendations to the Financial Supervisory Authority concerning the value of the countercyclical capital buffer pursuant to Article 86(d), Paragraph 1 of the Act on Financial Undertakings, no. 161/2002. In particular, the Council bases its recommendations on recommendations and analysis from the Systemic Risk Committee in determining the value of the countercyclical capital buffer; cf. the Act on a Financial Stability Council, no. 66/2014.

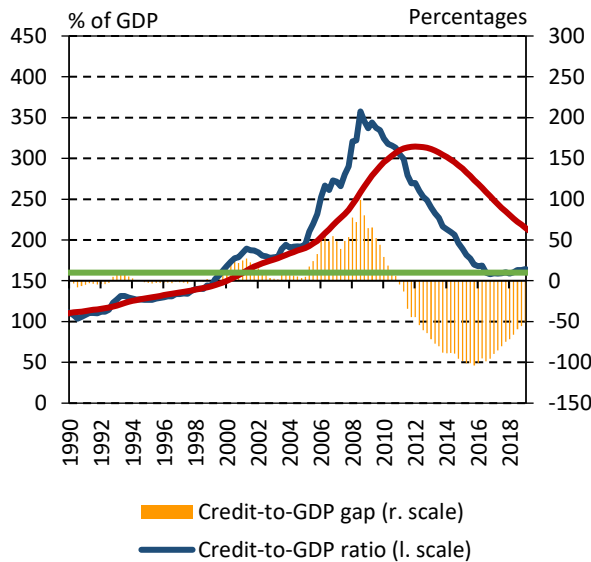
The main purpose of the countercyclical capital buffer is to enhance financial system resilience against potential losses following excessive debt accumulation and build-up of cyclical systemic risk. The buffer may be built up when a comprehensive assessment indicates that imbalances in the financial system are accumulating. The buffer requirement is reduced or lifted during a concurrent downward financial and business cycle so as to enhance financial institutions' ability to maintain a sustainable supply of credit.

With reference to the analysis conducted by the Systemic Risk Committee, the Financial Stability Council recommends to the Financial Supervisory Authority that the countercyclical capital buffer be held unchanged. Household and corporate debt growth has been in excess of economic growth over the recent term. Although the economy is now slowing down, debt impairment is still low. There is uncertainty about future developments. Forthcoming recommendations on the countercyclical capital buffer will take note of developments in cyclical systemic risk.

## Appendix to recommendation concerning countercyclical capital buffer

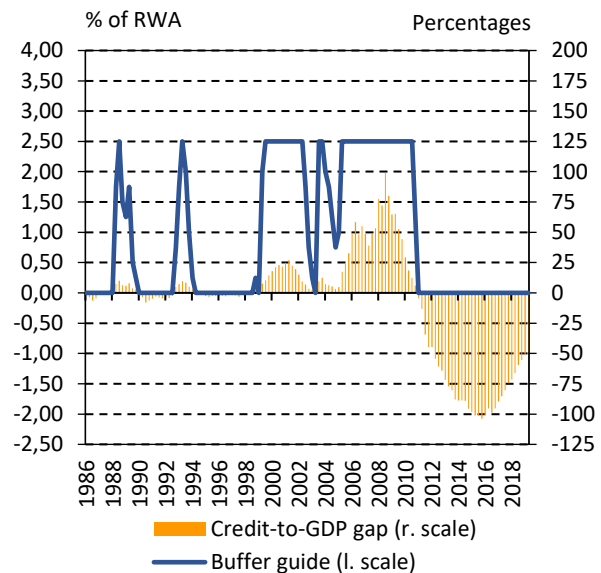
This recommendation is based on the Financial Stability Council's general guidelines of the application of the countercyclical capital buffer. In accordance with official financial stability policy, the Financial Stability Council shall regularly disclose which indicators it takes into particular consideration in analysing systemic risk. Below are the indicators considered most important in the assessment of the countercyclical capital buffer at the Financial Stability Council meeting of 26 September 2019.

### The credit-to-GDP gap



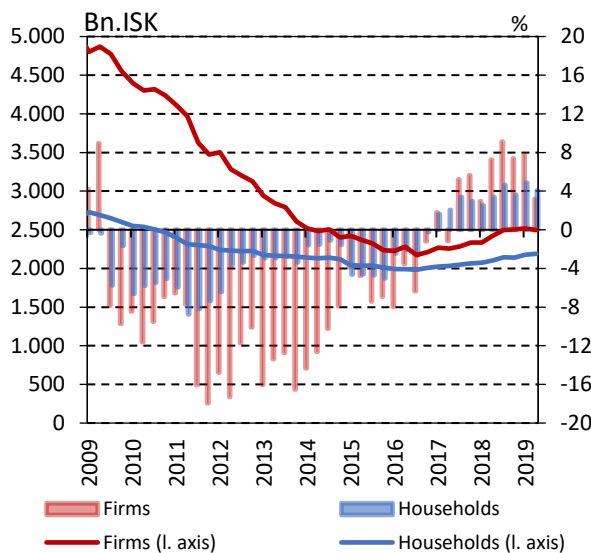
Total credit to households and firms in relation to GDP. The trend component obtained with a one-sided HP-filter with  $\lambda=400.000$ . The 9% threshold value comes from Laina, Nyholm & Sarlin (2015).  
Sources: Statistics Iceland, Central Bank of Iceland.

### The buffer guide



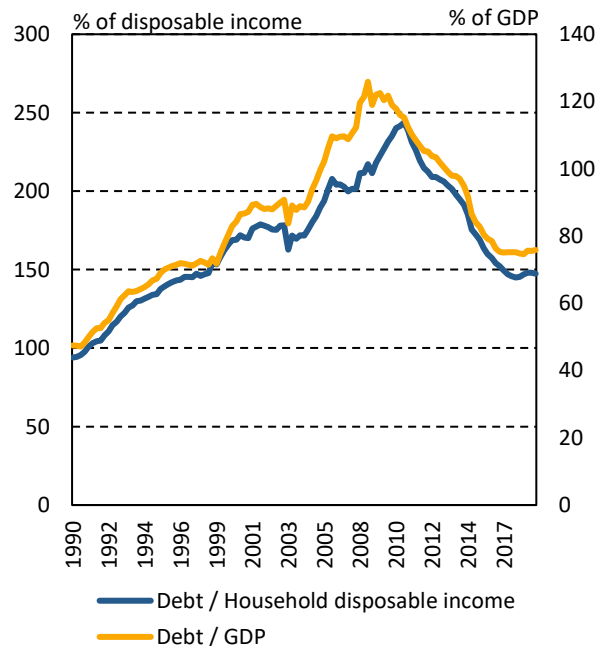
The buffer guide is a simple function of the credit-to-GDP gap, which is the deviation of the credit-to-GDP ratio from its long term trend.  
Sources: Statistics Iceland, Central Bank of Iceland.

### Real growth in credit to households and firms



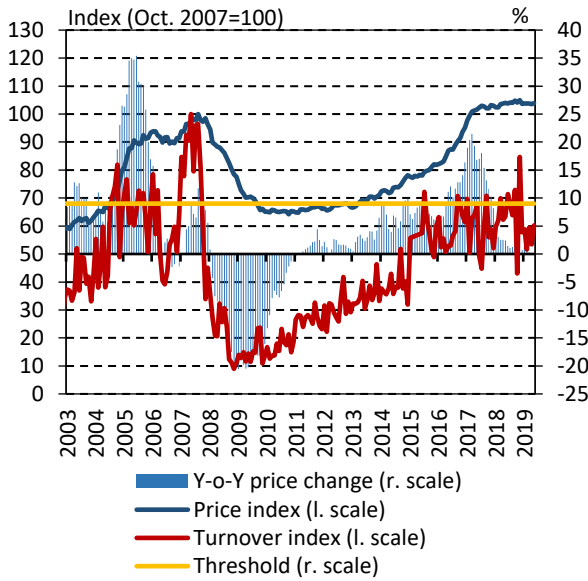
Total credit to households and firms, excluding holding companies. Deflated the consumer price index. Year-on-year growth.  
Sources: Statistics Iceland, Central Bank of Iceland.

### Household debt



Sources: Statistics Iceland, Central Bank of Iceland

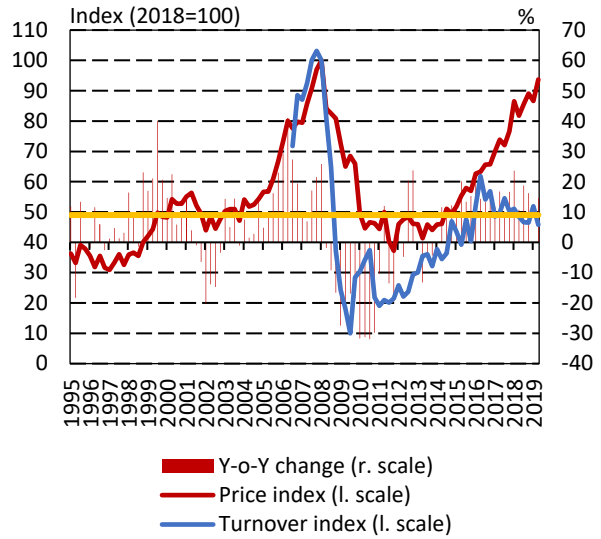
### Real RRE prices and turnover in the capital area



Price indices at constant prices according to CPI. The 9% threshold is from Laina, Nyholm & Sarlin (2015).

Sources: Statistics Iceland, Registers Iceland, Central Bank of Iceland.

### Real CRE prices and turnover in the capital area

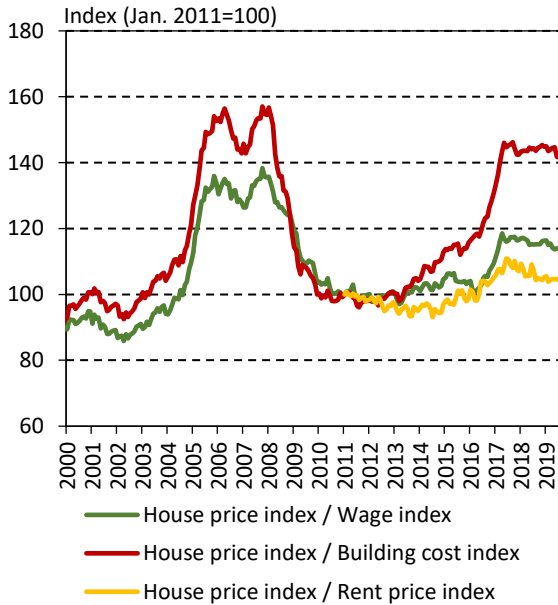


Price index at constant prices according to CPI. Commercial property index is a weighted average of industrial, retail and office housing.

Turnover index based on running average of last four quarters.

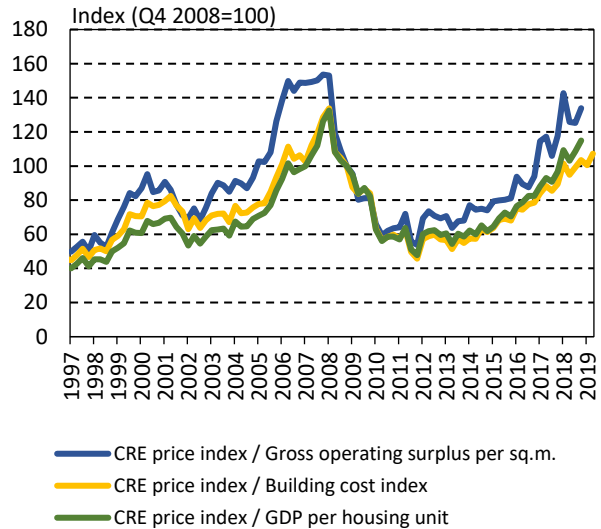
Sources: Statistics Iceland, Registers Iceland, Central Bank of Iceland..

### Capital area real house prices and determining factors



Sources: Statistics Iceland, Registers Iceland, Central Bank of Iceland.

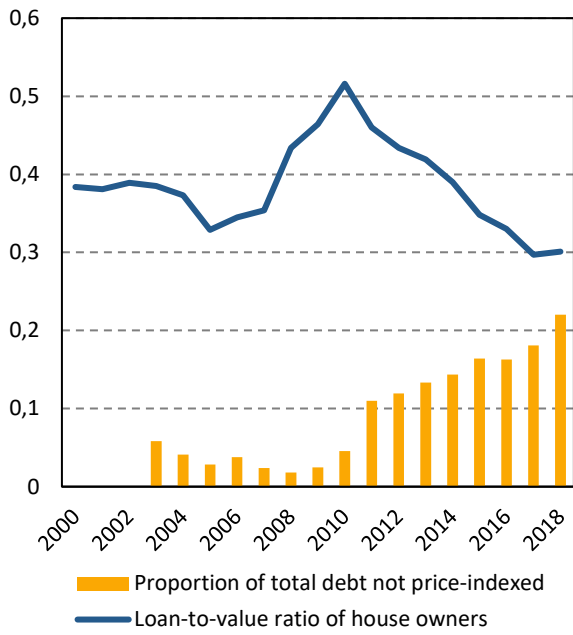
### Commercial real estate prices and other economic variables



All variables set to 100 at Q4 2008, before calculating a ratio. Annual data for gross operating surplus and the housing stock are non-linearly interpolated.

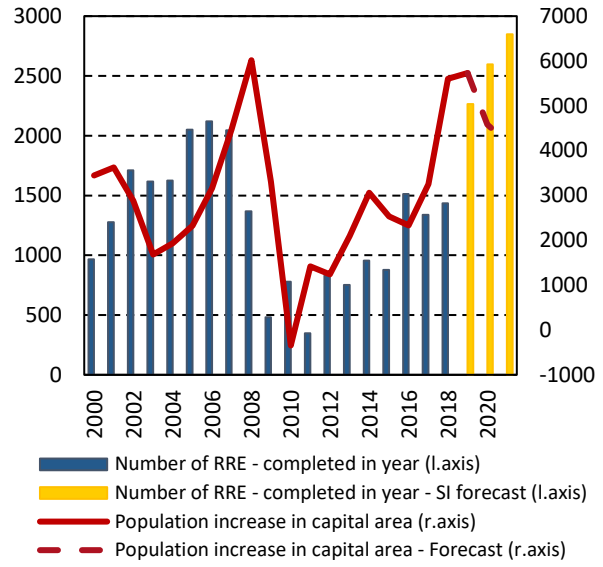
Sources: Statistics Iceland, Registers Iceland, Central Bank of Iceland.

Household resilience



Sources: Statistics Iceland, Central Bank of Iceland

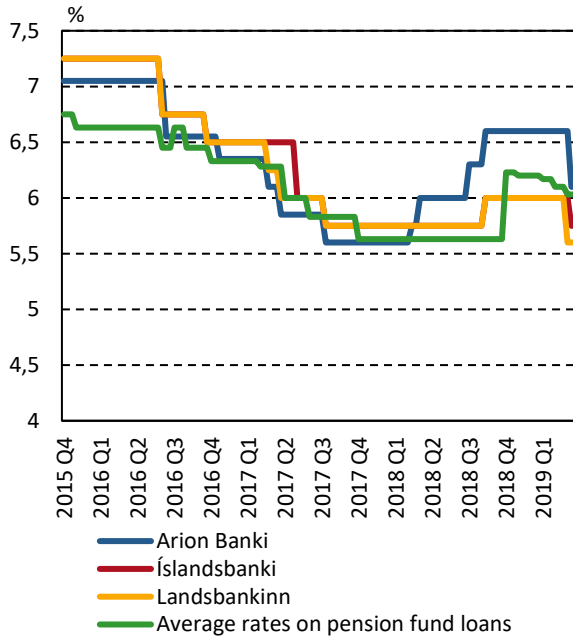
Newly constructed RRE and population growth in the capital area



1. Forecast on population increase past 2018 is based on Statistics Iceland population forecast.

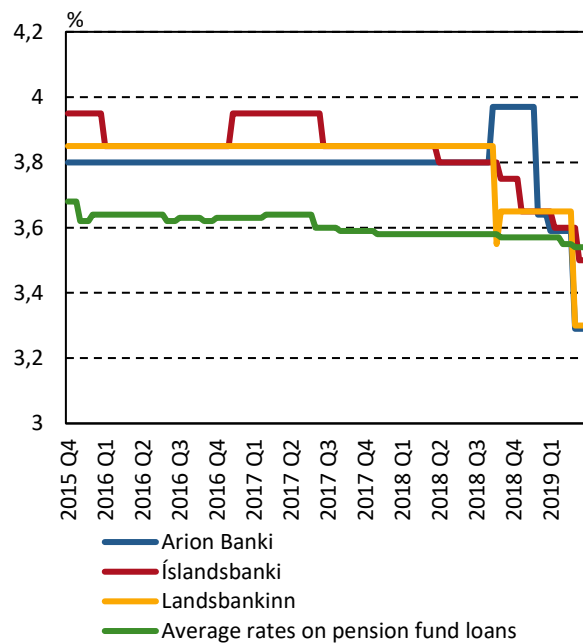
Sources: Statistics Iceland and SI - The Federation of Icelandic Industries

Interest rates on non-indexed RRE loans



Source: Central Bank of Iceland.

Interest rates on indexed RRE loans



Source: Central Bank of Iceland.