At its 561st meeting of 30 August 2016, the Governing Board of the Bank of Slovenia adopted the following

MACROPRUDENTIAL RECOMMENDATION

for housing loans

I. Content and purpose of the recommendation

(1) The Bank of Slovenia is issuing the macroprudential recommendation pursuant to Article 19 of the Macroprudential Supervision of the Financial System Act.[1]

(2) This recommendation is addressed to banks, savings banks, branches of Member State banks and branches of third-country banks in Slovenia (hereinafter: banks).

(3) By virtue of the Guidelines for macroprudential policy of 6 January 2016[2] (hereinafter: the guidelines) and on the basis of Recommendation ESRB/2013/1,[3] the Bank of Slovenia has put in place an operational framework for macroprudential policy and the macroprudential supervision of the banking system. In response to systemic risks identified at a given moment, the Bank of Slovenia may select the appropriate instrument from a toolkit of possible measures and instruments aimed at limiting or preventing the further build-up of systemic risk. The toolkit of (potential) instruments is adjusted to the selected intermediate objectives that the Bank of Slovenia pursues in the implementation of macroprudential policy. In order to pursue the intermediate objective of macroprudential policy of "mitigating and preventing excessive credit growth and excessive leverage", the Bank of Slovenia may introduce instruments for the area of real estate.

(4) The macroprudential instruments used to achieve the intermediate objective of mitigating and preventing excessive credit growth and excessive leverage in the area of real estate cited by the ESRB recommendation and the guidelines are the LTV (loan-to-value) ratio, the LTI (loan-to-income) ratio and the DSTI (debt service-to-income) ratio. The purpose of limiting the LTV and LTI/DSTI ratios is to mitigate the credit cycle and to increase the resilience of financial institutions. A stricter LTV ratio reduces the amplitude of the credit cycle and improves the resilience of the banking system, as the potential loss given default is lower. Lower LTI and DSTI ratios reduce the probability of default. Other macroprudential instruments may also be used, having regard for their effectiveness in meeting intermediate objectives.

(5) This recommendation applies to new housing loans, and sets the maximum acceptable level of:
  (a) the loan-to-value ratio when the loan agreement is concluded (hereinafter: the LTV ratio), and
  (b) the debt service-to-income ratio when the loan agreement is concluded (hereinafter: the DSTI ratio).

(6) Banks' credit standards for new housing loans and the situation on the real estate market currently do not present any direct systemic risk to financial stability. This could change rapidly due to the sustained period of low interest rates and the relatively low level of household indebtedness. Housing loans represent a segment of lending activity that could face relatively high exposure to systemic risks at the start of a new financial cycle. The purpose of the recommendation is to ensure that existing credit standards do not become excessively loose, to improve existing risk management systems at banks and to harmonise the monitoring of credit standards among banks

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[1] Official Gazette of the Republic of Slovenia, No. 100/13.
[2] http://www.bsi.si/financna-stabilnost.asp?MapaId=1739.
[3] Recommendation of the European Systemic Risk Board of 4 April 2013 on intermediate objectives and instruments of macroprudential policy (ESRB/2013/1), Official Journal of the EU 2013/C 170/01.

with regard to the LTV and DSTI ratios.

(7) The recommendation is issued as a preventive measure. The toolkit of instruments and the parameters thereof are defined so that they do not encroach significantly on current housing lending activity at the level of the banking system. The recommendation does not prevent banks from granting loans with a higher LTV or DSTI ratio in justified cases, i.e. when other relevant indicators suggest loan repayment.

(8) The recommendation does not encroach on rules governing the responsibilities of banks in the assessment and take-up of risks. Banks shall continue to define their own internal business policies in the assessment and take-up of risks with regard to the value of real estate collateral and the creditworthiness of borrowers.

(9) In the context of changing circumstances and increasing systemic risks to financial stability, the Bank of Slovenia may tighten the parameters of instruments or issue a binding macroprudential supervisory measure or instrument.

II. Definition of terms

(1) The following definitions shall apply for the purposes of this recommendation:

(a) **'borrower'** means the signatory or co-signatory of a loan agreement for the purchase of residential real estate (without guarantors or lienees who establish a lien as collateral for the debt of another party, or persons acceding to debt);
(b) **'lender'** means a bank, savings bank, branch of a Member State bank or a branch of a third-country bank in Slovenia;
(c) **'loan agreement'** means an agreement between a borrower and lender under which the lender grants or promises to grant the borrower a loan in the form of a deferred payment, or a loan or similar financial agreement, the repayment of which is secured by a mortgage or other comparable right in rem on real estate, or the purpose of which is to acquire or maintain ownership rights over existing or planned real estate;
(d) **'housing loan'** means a loan granted for the purchase, construction or renovation of residential real estate;
(e) **'housing loan secured by real estate'** means a loan granted for the purchase, construction or renovation of residential real estate for which real estate has been pledged as collateral;
(f) **'residential real estate'** means immovable property intended for residential use that is located in the territory of Slovenia and is the subject of purchase, construction or renovation by a consumer;
(g) **'consumer'** means a natural person who is acting for purposes outside their profession or gainful activity;
(h) **'LTV (loan-to-value) ratio'** means the ratio of the amount of a housing loan to the value of the real estate pledged as loan collateral;
(i) **'amount of a housing loan'** includes all housing loans or tranches (instalments) of a housing loan secured by the borrower's real estate when the loan agreement is concluded. The aforementioned amount is based on previously paid-out loans and does not include undrawn loans. In the case of real estate under construction, the amount of the housing loan is the sum of all paid-out loan tranches (instalments). It does not include loans not secured by real estate, unless the lender believes that an unsecured loan is intended for the purchase of the same residential real estate as is a secured loan. In this case the unsecured loan is included in the amount of the housing loan;
(j) **'real estate value'** means the lower of the transaction value of the real estate in question (i.e. as stated in a notarial record) and the market value of the real estate as appraised by independent external or internal real estate appraisers when the loan agreement is concluded. It does not include the value of planned renovations or construction works. In the case of real estate under construction, it refers to the value of real estate until the payment of loan tranches (including increases in value due to completed construction works). It is adjusted by

the value of outstanding housing loans, drawn or undrawn, that are secured by a lien on the real estate in question. When there are several older liens, the entire amount of debt already secured by a mortgage on that real estate must be deducted. A proportional adjustment must be made if the liens in question are of the same seniority. It is not defined as the “long-term value”, but as value of the real estate when the loan agreement is concluded. For the purpose of this recommendation, the real estate value does not take account of internal adjustments or the methods for calculating the real estate value used by banks for risk management purposes;

(k) **‘DSTI (debt service-to-income) ratio’** means the ratio of the annual debt servicing costs to the borrower’s annual income when the loan agreement is concluded;

(l) **‘debt servicing costs’** include interest and the repayment of the principal of the borrower’s total debt in a given period;

(m) **‘borrower’s debt’** refers to a borrower’s total debt when the loan agreement is concluded, irrespective of whether it is secured by real estate, including all other outstanding financial loans granted to the borrower by the lender who will grant the housing loan or by other lenders; and

(n) **‘borrower’s income’** means the annual income of a borrower when the loan agreement is concluded. A bank may take into account the following types of income when defining the ‘borrower’s income’: annual earnings from all income sources (employment income, income from self-employment, pensions, earnings from unemployment and social transfers, private transfers such as maintenance payments, earnings from the letting of real estate, financial investments and other sources), minus taxes and contributions (e.g. contributions for health insurance, pension insurance and social security), and excluding expenses.

III. Recommendations

Recommendation A:
Limitations on the LTV ratio when the loan agreement is concluded for new housing loans

1) It is recommended that the LTV (loan-to-value) ratio does not exceed 80% when the loan agreement is concluded for new housing loans secured by residential real estate.

Recommendation B:
Limitations on the DSTI ratio when the loan agreement is concluded for new housing loans

1) It is recommended that the DSTI (debt service-to-income) ratio does not exceed the following values when the loan agreement is concluded for new housing loans:
   a) for borrowers with monthly income of EUR 1,700 or less: 50%; and
   b) for borrowers with monthly income of more than EUR 1,700: 50% for that portion of income up to EUR 1,700 inclusive, and 67% for that portion of income exceeding EUR 1,700. In the case of multiple borrowers, this provision applies to each borrower separately.

2) In the loan approval process (when assessing creditworthiness) it is recommended that banks apply, *mutatis mutandis*, the limitations on the attachment of a debtor’s financial assets set out in the Enforcement and Securing of Claims Act (ZIZ)[4] and the Tax Procedure Act (ZDavP-2),[5] i.e. earnings that are exempt from attachment and limitations on the attachment of a debtor’s financial earnings.

IV. Assessment of compliance with the recommendation

(1) The Bank of Slovenia shall regularly assess compliance with recommendations A and B via annual questionnaires on the structure of new housing loans, or during ordinary inspections of banking

[4] Official Gazette of the Republic of Slovenia, Nos. 3/07 (official consolidated version), 93/07, 37/08 (ZST-1), 45/08 (ZArbit), 28/09, 51/10, 26/11, 17/13 (constitutional court ruling), 45/14 (constitutional court ruling), 53/14, 58/14 (constitutional court ruling), 54/15 and 76/15 (constitutional court ruling).

[5] Official Gazette of the Republic of Slovenia, Nos. 13/11 (official consolidated version), 32/12, 94/12, 101/13 (ZDavNepr), 25/14 (ZFU), 40/14 (ZIN-B), 90/14 and 91/15.

operations.

(2) Compliance with the recommendation shall be assessed for the first time in 2017. When assessing compliance with recommendations A and B, the Bank of Slovenia shall take into account the time required by individual banks to adapt their information system and risk management system.

V. Final provision

(1) This recommendation was formulated on the basis of an assessment of systemic risks to financial stability up to 30 August 2016.

(2) This recommendation shall enter into force when published on the Bank of Slovenia’s website.

Ljubljana, 30 August 2016

Boštjan Jazbec
President,
Governing Board of the Bank of Slovenia