Box 8. Calibration of the measure to set the maximum level of indebtedness

The default risk for loans to the private sector is assessed to be high in the medium run, for households in particular. A major concern remains the asymmetry of the level of indebtedness by income, as the DSTI for borrowers earning minimum to average wage economy-wide is well above that for higher earners. Under the circumstances, a potential unfavourable change in the economic and financial conditions could push indebtedness above the sustainable level in the case of these debtors.

In this context, in October 2018, the NBR adopted Regulation No. 6/2018 amending and supplementing NBR Regulation No. 17/2012 on certain lending conditions, as subsequently amended and supplemented, which entered into force on 1 January 2019. The new measure sets a limit of 40 percent on total level of indebtedness, of which at most half can stem from forex exposures. Total level of indebtedness is measured as a ratio of total monthly debt service to the monthly net income (DSTI)[1]. The regulation applies to both banks and non-bank financial institutions, which allows for a uniform treatment in the credit market and limits the potential regulatory arbitrage opportunities of financial institutions.

An analysis of the impact this measure has on non-performing housing loans shows that if the measure had been previously applied, the probability of default would have been 27 percent lower than the current level. Moreover, the impact would have been stronger for below-average income earners, for whom the probability of default would have decreased by 41 percent.

This measure was introduced, on the one hand, to ensure debtors' enhanced capacity to withstand adverse conditions and, on the other hand, to lower the negative impact on households' access to financing. Specifically, the new measure sets forth a number of facilities ensuring credit institutions higher flexibility when implementing it. First, the maximum level of indebtedness is raised by 5 percentage points on first-time home buyer loans. Second, credit institutions are allowed not to apply the requirement for the maximum level of indebtedness for debtors with low default risk[2]. However, this exception may not exceed 15 percent of the quarterly volume of new loans and the maximum value of such a new loan can be no higher than EUR 250,000.

Loans granted for the sole purpose of repaying the loans already taken are exempt from being applied an indebtedness ceiling. This exception aims to ensure households' unrestricted access to loan refinancing. Furthermore, in order to ensure higher transparency of this measure in the creditor-loan applicant relationship, as well as uniform implementation across the banking sector, the obligation to deduct subsistence expenses from eligible income was eliminated from the Regulation.

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1 If applicable, in order to calculate the level of indebtedness, income will be adjusted by coefficients based on income certainty and permanence.

2 Their income is equal to or above the average net wage economy-wide, thus creating conditions for the adequate management of default risk.