ESRB
European Systemic Risk Board
European System of Financial Supervision

Press release

7 December 2023

The General Board of the European Systemic Risk Board held its 52nd regular meeting on 30 November 2023

At its meeting on 30 November 2023, the General Board of the European Systemic Risk Board (ESRB) concluded that financial stability risks in the EU remain elevated. Looking forward, the General Board cautioned that several factors continue to weigh on the financial stability outlook. Uncertainty and downside risks to the growth outlook have increased in recent months, not least on the back of rising geopolitical tensions. In particular, the challenging macroeconomic environment could create balance sheet stress for households and non-financial corporations, as the capacity of fiscal policy to support these sectors is more limited than in the past. The General Board acknowledged the high volatility in bond markets and the potential of a disorderly adjustment in financial markets, which could be amplified by high credit risk and liquidity risk in the non-bank financial intermediation sector.

Moreover, the General Board discussed recent strains in the commercial real estate (CRE) sector in several European Economic Area (EEA) countries and stressed the importance of its January 2023 recommendation [LINK] on CRE exposures across the financial sector. The recommendation called for medium-term actions by supervisory authorities to improve their monitoring of CRE-related risks, ensure sound financing practices and increase the resilience of financial institutions. It highlighted that the CRE sector is particularly vulnerable to the tightening of financial conditions, and noted its modest growth outlook in the light of structural changes such as the shift towards e-commerce, remote working developments and stricter building standards as a result of climate policies. Finally, the recommendation also called for the development of activity-based supervisory tools for CRE exposures in the EU, to be applied consistently across all financial institutions.

The banking sector is still benefiting from strong profitability and robust funding liquidity, but uncertainty is also weighing on its outlook. First, the weak macroeconomic environment may affect

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asset quality, particularly for banks with high exposures to consumer loans and the CRE sector. Second, banks' funding costs are expected to weigh on net interest income. Third, reduced credit demand and subdued growth prospects are likely to curtail lending volumes to households and non-financial corporations.

Against this background, the General Board considered it crucial for micro- and macroprudential authorities to continue monitoring the impact of the changing macro-financial environment on financial stability, with a view to adjusting policy responses as appropriate.

Furthermore, the General Board held its regular discussion on financial stability issues stemming from residential real estate (RRE) markets.[1] Overall, housing markets have decelerated in many EEA countries, with some undergoing an orderly correction in house prices and mortgage lending. However, the level of accumulated vulnerabilities – such as high household indebtedness and the overvaluation of house prices – remains high or medium in most EEA countries. Therefore, the ESRB's current assessment of vulnerabilities in the RRE sector is largely unchanged compared to its 2021 assessment [LINK]. The full analysis will be published at the beginning of 2024.

Moreover, the General Board finalised the adverse scenarios for the one-off climate risk scenario analysis in line with the Fit for 55 package, after an initial methodological discussion at its September meeting [LINK PR]. The European Central Bank (ECB) and the European Supervisory Authorities will conduct the scenario analysis using these adverse scenarios. The detailed scenarios will be included in their final report to the European Commission on the results of the exercise.

Finally, the ESRB concluded its exploratory work on measuring and modelling the systemic dimension of climate risks, and on possible macroprudential policy options. The General Board discussed three aspects of this work, which was conducted jointly with the ECB. First, it took stock of ways in which climate risk could trigger systemic risk, noting that EU banks should properly assess climate-related financial risks of lending portfolios that are clearly tilted towards higher emitting parts of the economy. Second, the Board discussed the macroprudential policy toolbox and the possibility of applying instruments provided for by current legislation in order to address risks to banks, borrowers and non-bank financial intermediaries. Third, the Board had an initial exchange of views about the risks of nature degradation, which could exacerbate the effects of climate change, with repercussions for financial stability. These findings are summarised in the final joint ESRB/ECB report, which is due to be published in mid-December.

[1] The ESRB conducted systematic, forward-looking assessments of vulnerabilities in the residential real estate sector in the European Economic Area in 2016 [LINK], 2019 [LINK] and 2021 [LINK].

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The ESRB today released the 46th issue of its risk dashboard**.** The risk dashboard is a set of quantitative and qualitative indicators measuring systemic risk in the EU financial system.

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