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PRESS RELEASE

Financial Stability Report 2018: "**A sound and robust Belgian financial sector, but some formidable challenges**"

The Belgian banking and insurance sector is sound and robust thanks to restructuring and changes in the regulatory and supervisory framework. But a number of sizeable challenges still require special attention: that is what the National Bank concludes in its Financial Stability Report 2018.

The National Bank of Belgium is publishing its Financial Stability Report for the 17th consecutive year. The publication comprises three main sections: the Macroprudential Report on the Bank's responsibilities and its policy on macroprudential supervision, the Overview which describes the main determinants of the stability of the financial system in Belgium, and four articles on specific macrofinancial and macroprudential themes (recent property market developments, the use of derivatives, the potential impact of climate policy on the financial sector, and sectoral credit cycles).

The Macroprudential Report published today is the fourth report produced by the Bank in its capacity as the macroprudential authority. The first part of the Report deals with the main risk factors identified during the year under review and their effect on the financial sector. The second part details the macroprudential measures adopted by the Bank.

Risk factors

Ten years after the crisis, Belgian financial institutions are in a sound and robust financial position. That situation, already highlighted by the IMF in its FSAP (Financial Stability Assessment Programme), is attributable both to the sector's restructuring and to changes made to the regulatory and supervisory framework. However, financial institutions face some sizeable challenges. Some of those challenges concern the persistent low interest rate environment, the possibility of risk repricing, and developments on the real estate and mortgage markets. In addition, structural challenges are increasingly emerging, as a consequence of a change in the financial sector's operating environment.

Up to now, interest rates have remained at a low level, weakening the profitability of financial institutions – primarily the banks. Even though it is most likely that interest rates will rise gradually in the years ahead, the scenario of a sudden increase in long-term interest rates cannot be ruled out. Such a scenario could be detrimental for banks if they were inadequately hedged, and could have an adverse effect on the solvency of the life insurance sector. However, stress tests conducted by the IMF during the FSAP showed that the sector had a sufficient shock absorption capacity.

The real estate market, which has been highly dynamic in recent years, remains a point for attention. Belgian banks' mortgage lending to Belgian households remains vigorous, with loans often granted under lax credit conditions, leading to a steadily increasing debt level (and vulnerability) of Belgian households. In addition, the low level of interest rates has prompted some investors (particularly institutional investors) to refocus their strategy on the property sector, while at the same time the borrowing rates charged for both residential and non-residential projects reached record low levels. In those circumstances the Bank maintained a very close watch on developments on the Belgian housing and commercial property market, and in May 2018 introduced a new macroprudential measure for the residential property market in view of the continuing accumulation of vulnerabilities in that sector and the level of exposures on bank balance sheets. With this new and more targeted macroprudential measure the Bank aims primarily to strengthen the resilience of the Belgian banks in order to ensure sustainable lending level in the longer term. This measure also gives a signal to the sector, encouraging a cautious and well thought-out lending policy.

In general, credit cycle developments are still being closely monitored, especially as regards lending to the non-financial private sector. However, as in other European countries, the recent acceleration of the cycle in Belgium was not considered excessive by the Bank and therefore did not lead to activation of the countercyclical capital buffer. The Bank will continue to maintain a close watch on developments in the financial cycle. It issues quarterly communications on those developments and on its policy concerning determination of the countercyclical buffer.

Structural change in the operating environment

Apart from these primarily cyclical risks, more structural or permanent points for attention also require macroprudential policy monitoring. Domestic systemically important banks, whose failure could have a significant impact on the financial system or on the real economy, are thus subject to capital surcharges. The structural change in the environment in which financial institutions operate also requires close monitoring. **The digital transformation** creates **increased cyber risks**. It also represents a source of other risks, particularly in terms of future profitability, if institutions are inadequately prepared for it. **The development of the shadow banking sector** could also pose a number of risks which need to be identified, monitored and limited. Finally, **considerations relating to climate change** and, at least as important, the **transition to a low carbon economy** play an ever larger role in economic developments and/or policy, and may therefore present potential risks for the financial sector. Of course, these various aspects of the changing financial environment also offer opportunities. It should become possible to reduce operating costs by boosting efficiency and to expand the range of financial products, tailoring them ever more closely to the needs of the real economy.

These various aspects, both cyclical and more structural, are closely monitored by the Bank in its capacity as the macroprudential authority for Belgium.

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