

**ABI comments on the EBA  
Consultation Paper on Draft Regulatory  
Technical Standards  
specifying the types of factors to be  
considered for the assessment of  
appropriateness of risk weights under  
Article 124 (4) of Regulation 575/2013 and  
the conditions to be taken into account for  
the assessment of appropriateness of  
minimum LGD values under Article 164 (8)  
of Regulation 575/2013**

July 2021

## Preliminary remarks

The Italian Banking Association (ABI) is pleased to provide herewith its views on the EBA consultation paper on "Draft Regulatory Technical Standards specifying the types of factors to be considered for the assessment of appropriateness of risk weights (RW) under Article 124 (4) of Regulation 575/2013 (CRR) and the conditions to be taken into account for the assessment of appropriateness of minimum LGD values under Article 164 (8) of Regulation 575/2013" (further referred to as "EBA CP").

ABI would highlight that the EBA regulations might result, along with the National Supervisory Authorities' actions, in a possible increase of banks' capitalisation on exposures collateralised by real estate, with the possible impact of financing the purchasing or renovation of commercial and/or residential property.

EBA itself in the CP indirectly seems to be concerned about the impact of a possible increase of RW or minimum LGD values in the Real estate market when it recommends to avoid "double counting" effects or underlines that *"When considering any changes to risk weights or minimum LGD values, the relevant authority should also be aware of the direct linkages to other parts of the regulation, including the impact of such changes on the calculation of large exposure values, liquidity and capital ratios, reporting requirements and other macroprudential measures"*.

Furthermore, we would highlight that every specific action on a specific national real estate credit market could undermine the level playing field among different EU Member States. Indeed, the scope of regulation should avoid any possible action to increase competitive gaps in the European banking sector.

The section below "Answers to the questions in the consultation paper" includes ABI responses to the questions posed in the Consultation Paper.

## Answers to the questions in the consultation paper

### **1. What is the respondents' view on the types of factors to be considered during the determination of the loss expectation for the appropriateness assessment of risk weights under the SA?**

In general, in order to catch all the elements to assess all the possible implications by the decisions proposed in EBA CP, ABI recommends National Competent Authorities **to adopt appropriate consultation processes and impact studies before deciding to set higher RW or imposing stricter criteria than those set out in Article 125 (2) and 126 (2) CRR or setting other minimum average exposure.**

Furthermore, we do not completely support the EBA CP position according to which the length of the forward-looking horizon over than 3 years "*may increase the degree of inaccuracy of the loss expectation.*" We think instead **that a longer period** could avoid/overcome any possible conjunctural economic effect which can affect the forward-looking assessment of loss expectation. In light of this, we suggest that the National Competent Authorities decide annually the length of this period, even over than 3 years.

In a more technical view, considering that in SA risk weights on exposures collect all credit risk factors of that specific exposure (on the borrower's and collateral's side), we suggest that Competent Authorities take in account the general level of **borrower's indebtedness** on real estate market, too. Indeed, the general level of indebtedness could represent an important element to assess the borrower's capability to sustain the mortgage loans.

In the end, EBA CP considers the "price" as a "base of value" to evaluate the property collateral. Actually, CRR provides that the properties which secure the mortgage exposure have been evaluated using as "base of value" the "Market value" (MV) or the "Mortgage lending value" (MLV). This base of value is recognised and defined by International and European Valuation Standard Association/Council (RICS, TEGOVA, IVSC). Furthermore, in many Member states, public and private databases collect information only on MV and MLV. In this regard, we propose that EBA CP takes in account the concepts of **"Market Value" and "Mortgage Lending value" instead of "price"** to assess/monitor the value of real estate.

***2. What is the respondents' view of the option of considering climate related risks in the determination of the loss expectation where the relevant authority was in a position to perform an appropriateness assessment to one or more parts of the territory of the Member State? What would for the respondent be the benefits and the challenges (costs) of such option?***

ABI is aware with the possible relevance of risks related to "climate change" - as the "transition risks" and "physical risks" - and their potential impact on the level of credit risk on the portfolios of banks.

Anyway, we are in an early stage to consider climate related risk in the determination of loss expectation: there is a general lack of data on those types of risks and the international/national climate related policies are still uncertain. Same considerations/views are also highlighted by recent EBA Report "Mapping climate risk: Main findings from the EU-wide pilot exercise" issued on May 21<sup>st</sup>, 2021.

For this reason, we propose to put off the possibility to consider climate related risks in the determination of the loss expectation when we will have more certainty and data on this issue.

***3. What is the respondents' view on the conditions when assessing the appropriateness of minimum LGD values (cf paragraph 1 of Article 2)?***

***4. What is the respondents' view on the considerations to be taken into account when assessing the appropriateness of minimum LGD values (cf paragraph 2 of Article 2)?***

LGD values in IRB banks are approved and supervised by Competent/Relevant Authority. For this reason, it is even more important that Competent Authorities adopt appropriate consultation processes and impact studies before deciding to set higher minimum LGD threshold.

Also in this case, as we mentioned in answering to Question 1, we propose that EBA CP takes in account the concepts of **"Market Value" and "Mortgage Lending value" instead of "price"** to assess/monitor the value of real estate.