EBA/Op/2025/06

28 May 2025

Opinion of the European Banking Authority on measures in accordance with Article 458 of Regulation (EU) No 575/2013 regarding certain corporate exposures secured by immovable property in Sweden

Introduction and legal basis

1. On 30 April 2025, the European Banking Authority (EBA) received a notification from the European Systemic Risk Board (ESRB) on the intention of the Swedish Financial Supervisory Authority (Finansinspektionen), thereafter the 'Swedish FSA', to apply Article 458(9) of Regulation (EU) No 575/2013 of the European Parliament and of the Council (Capital Requirements Regulation, CRR)[1].

2. The notification concerns the extension of a measure originally introduced by the Swedish FSA on 30 September 2023 for a period of application of two years. The measure to be extended applies to all credit institutions using the Internal Ratings Based (IRB) approach to calculate regulatory capital requirements and it sets an exposure-weighted average risk weight floor of 35% for certain corporate exposures secured by commercial properties, and a risk weight floor of 25% for certain corporate exposures secured by residential properties.

3. The EBA's authority to deliver an Opinion in based on the second subparagraph of Article 458(4) in conjunction with Article 458(9) of Regulation (EU) 575/2013.

4. In accordance with the second sub-paragraph of Article 458(4) of the CRR, within one month of receiving the notification, the EBA is required to provide its opinion on the points referred to in Article 458(2) of the CRR to the Council, the European Commission and the Member State concerned.

[1] Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and amending Regulation (EU) No 648/2012 (OJ L 176, 27.6.2013, p. 1).

5. In accordance with Article 14(2) of the Rules of Procedure of the Board of Supervisors, the Board of Supervisors has adopted this Opinion.[2]

Background of the measure to be extended

6. The proposed measure under Article 458 of Regulation (EU) No 575/2013 concerns the extension of a measure applicable as of 30 September 2023 for a two-year window. The measure applies for institutions using the Internal Ratings Based approach (IRB) and introduced two exposure-weighted floors on average risk weights for corporate exposures secured by immovable property physically located in Sweden, which are owned to generate income through rental to tenants (CRE). The floors are calibrated as follows:

- 35% for corporate exposures secured by commercial properties;

- 25% for corporate exposures secured by residential properties.

7. The following type of properties are outside the scope of the measure: i) agricultural properties, ii) properties owned directly by municipalities, states and regions, iii) properties where more than 50% of the property is used for own business (not rental), iv) multi-dwelling properties where the purpose of the property is not commercial (for example housing associations that are owned by the residents and that are not profit making) or where the number of dwellings is less than four. According to the Swedish FSA, these exemptions target types of real estate associated with a different level of risk compared to other CRE firms because of their ownership or income characteristics.

8. The exposures under scope are largely held by IRB institutions. If the measure is recognised by Member States, the measure will also apply to branches and Swedish exposures of foreign IRB institutions.

9. The measure complements the existing measure under Article 458 of the CRR on retail exposures originally implemented in December 2018 and extended on three occasions, which increases the risk weight for mortgages.

10. The Swedish FSA calibrated the measure building from analyses conducted by the Swedish FSA[3]. The additional capital requirement is set to ensure that the banks have enough capital to cover the risks in their lending, with a differentiation by the type of underlying collateral, whereby corporate exposures secured by residential real estate receive a calibration of 25%, in line with the national measure according to Article 458 regarding retail exposures on mortgages. This calibration is underpinned by the more stable cashflows presumed by

[2] Decision of the EBA concerning the Rules of Procedure of the Board of Supervisors of 22 January 2020 (EBA/DC/2020/307).

[3] See Commercial Real Estate Market and Financial Stability, May 2019, FI, Stability in the Financial System, May 2019, FI, and Stability in the Financial System November 2019, FI

residential properties as opposed to commercial properties. On the other hand, corporate exposures secured by commercial real estate are assigned a higher floor, at 35%.

11. It is recalled that the measure intended to replace an associated capital add-on in Pillar 2 through the comprehensive Supervisory Review and Evaluation Process (SREP). This was set out in 2020 by the Swedish FSA for IRB banks to address an identified underestimation of risk in the models used for corporate exposures secured by commercial real estate, which are owned to generate income through rental to tenants. Against the background of the gradual implementation of bank's reviewed internal models, the Swedish FSA considers it appropriate to make use of Article 458 instead of Pillar 2 for operational reasons, coupled with the simplicity for reciprocity, as the identified risks also affect foreign institutions. This is of particular importance in the highly integrated financial system of the Nordic-Baltic region. In particular, the two largest foreign branches have exposures under the scope of the measure to be applied.

12. According to the Swedish FSA, the measure intended to be extended affects mostly the three largest Swedish institutions. The impact on capital requirements for the three largest Swedish institutions is set to be:

    a. An increase in total capital requirements of 3.7% or SEK 18.9bns (link).

    b. An increase in the average risk weight:

        i. From 15% to 35% when secured by commercial property

        ii. From 13% to 25% when secured by residential property

13. The Swedish FSA intends to request reciprocity by other EU member states. Reciprocity will make sure that the measure also applies to foreign branches and direct foreign exposures. If the measure is reciprocated, the impact on affected banks from other jurisdictions is set to be small as their current risk weights are higher or close to the proposed floors, according to the Swedish FSA.

14. The proposed measure is not expected to affect banks' interest margins or the supply of credit to CRE firms because it refers to the intended extension of a measure in place.

Opinion on the extension

Economic rationale for the measure

15. The Swedish FSA notes that the measure is set to ensure that banks hold sufficient capital and continue financing the real economy in the event of potential shocks from the indebted CRE sector, which is particularly vulnerable to deterioration in the macro-economic conditions. Further, banks exposures to CRE is large (number) and increases in non-bank borrowing from

CRE amplifies interconnected with financial sector. This message aligns with reports from Risksbank, the ESRB and IMF describing commercial real estate as one the more prominent vulnerabilities for financial stability in Sweden. In particular, the IMF recommended in 2023 that higher capital requirements towards CRE should be considered in Sweden[4].

16. Regarding recent developments in the commercial real estate sector, the Swedish FSA notes that since 2024 prices have stabilised and even increased, with lower ability from CRE firms to increase rents due to lower inflation, and increasing vacancy rates given the economic situation. Structural changes related to slower population growth rise of online shopping and teleworking, are set to put upward pressure on vacancy rates going forward.

Rationale for not using alternative measures

17. Regulation (EU) No 575/2013 requires the designated authority to explain why other possible measures (i.e., under Articles 124 and 164 of that Regulation and under Articles 133 and 136 of Directive 2013/36/EU) would be less suitable and effective in dealing with the macroprudential or systemic risk identified than measures in accordance with Article 458(2)(d) of that Regulation.

- Article 124 of the CRR applies to the standardised approach of credit risk, while most exposures under scope of the notification are held under the IRB approach. Hence it is deemed any measure under 124 is not adequate to meet the risks for corporate exposures secured by real estate.

- Article 164 of the CRR applies to retail exposures, while the intended extension of the measure applies to corporate exposures.

- The Swedish FSA has already set a 3% Systemic Risk Buffer (SyRB) to the three largest banks, in accordance with Article 133 of Directive 2013/36/EU (the CRD). Applying a sectoral SyRB targeting CRE exposures is deemed less efficient than the floor as the ongoing review of internal models would prompt recalibration of the sectoral SyRB. Further, the sectoral SyRB is deemed to disproportionately affect institutions with higher risk weights for he targeted exposures, while the intention is to address institutions with lower risk weights.

- The Countercyclical Capital Buffer (CCyB) rate in Sweden under Article 136 of the CRD has been set at 2% since 22 June 2023. As the scope of the measure is not tailored for CRE, any increase of the CCyB to address CRE market risks is set to unduly penalise other type of exposures.

[4] Sweden: Financial System Stability Assessment, IMF, 2023

Assessment and conclusions

18. Based on the evidence provided by the Swedish FSA, the EBA takes note of the concerns of the Swedish FSA regarding the systemic of risk related to CRE and the persistence of macroprudential vulnerabilities in the Swedish financial system. The EBA does not object to the extension of the current measure for 2 years or a shorter period if risks at stake cease to exist sooner.

19. The measure has been in place in one form or another since 2020, originally introduced through Pillar 2 and then replaced in 2023 by the current Article 458 measure. The EBA notes that the calibration of the measure has not changed since. According to the Swedish FSA, the risk weight floor continues to be adequate despite changes in the CRE market, the macroeconomic environment and further macroprudential measures implemented since the application of the original measure.

20. The calibration is set so that the average risk weight floor covers future losses in a stressed scenario assessed as severe but plausible. Therefore, the EBA stresses the need to avoid overlaps with other requirements, in particular with the Pillar 2 Guidance (Article 104b Directive 2013/36/EU), which is set based on the outcome of stress tests.

21. The measure is set to address issues related to banks' repair of IRB models, which are still under review in Sweden, with an implementation timeline longer than originally expected despite being a priority for the Swedish FSA. IRB models continue to generate risk weights for CRE exposures that are relatively low, with concerns about unjustified variability between banks. A review of IRB models, which has been ongoing for several years, is expected to lead to some adjustments. The EBA understands that micro-prudential measures have been taken in Sweden to ensure that conservative PD and LGD projections underpin banks' IRB risk-weight calculations, including the use of the margin of conservatism to be applied to risk parameters.

22. Hence, the EBA stresses the need to avoid any overlaps with other micro-prudential requirements and in particular requirements for the estimation of IRB models (Article 179 Regulation (EU) 575/2023 and EBA's RTS and Guidelines on the review of the IRB approach, notably Commission Delegated Regulation (EU) 2022/439 on the IRB assessment methodology and EBA/GL/2017/16 on the PD and LGD estimation), Pillar 2 Requirements and Pillar 2 Guidance (Articles 104a and 104b Directive 2013/36/EU) which could be used to tackle and cover similar risks.

23. Lastly, the introduction of relevant changes to the CRR will affect the risk weights for IRB banks, in particular the output floor under Article 92 of Regulation (EU) 575/2013, which will become fully applicable by January 2033. The EBA therefore invites the Swedish FSA to undertake a comprehensive assessment on the appropriateness of the notified measure taking into account the outcome of the internal model review and the impact of relevant changes to the CRR.

This Opinion will be published on the EBA's website.

Done at Paris, 28 May 2025

[signed]

Jose Manuel Campa

Chairperson

For the Board of Supervisors