FIN-FSA principles for tightening the maximum loan-to-value ratio and restricting the collateral used in calculating the loan-to-value ratio

Pursuant to chapter 15, section 11 of the Credit Institutions Act (610/2014), the loan-to-value ratio means the loan amount granted in relation to the current value of the collateral security lodged as security for the loan at the time of granting the loan. A personal guarantee is not taken into account as security.

According to said legal provision, a credit institution may grant consumer credit secured by shares in a corporation conferring the right of possession to a residential apartment, or by residential property or the right of using such property, up to the maximum amount according to the loan-to-value ratio, if such credit is intended for i) purchase of shares in a corporation conferring the right of possession to a residential apartment, or residential property or such a residential building as is located on a site possessed by virtue of the right of using the property or ii) refurbishment of a residential apartment, residential property or residential building.

The loan amount referred to above may be *90% at most of the current value of collateral posted at loan approval.*

By way of derogation from the foregoing, the amount of a loan taken out for a first home purchase may be *95% at most of the current value of collateral posted at loan approval.*

> **In order to limit any exceptional increase in risks to financial stability**, the Financial Supervisory Authority (FIN-FSA) may *decide to reduce the above maximum loan amounts by not more than 10 percentage points.* In addition, the FIN-FSA may also *restrict the taking into account of any other collateral security except real security in calculating the loan-to-value ratio if this is necessary in order to manage said risks.* The decision is taken by the Board of the FIN-FSA.

According to Government Bill 39/2014, the tightening of the maximum loan-to-value ratio or the restriction of collateral would need to be applied in situations where the housing market threatens to overheat in a manner that jeopardises the stability of the financial markets and macroeconomic stability. A key indicator for market overheating would be a rise in house prices relative to overall earnings developments. Other justifications to be taken into account would include, in particular, significant growth in residential mortgages relative to disposable household income and significant threats to macroeconomic performance that affect the housing market.

The right to restrict the amount of eligible collateral applies to guarantees and insurance granted by firms or public entities providing credit insurance or guarantees, and comparable collateral. The FIN-FSA is required to make a quarterly decision on amending or extending the validity of an earlier decision made in this respect. *The FIN-FSA must publish on its website the principles it complies with when assessing the conditions for tightening the maximum loan-to-value ratio and restricting collateral.*

Principles for tightening the maximum loan-to-value ratio and restricting the collateral used in calculating the loan-to-value ratio

An assessment whether to tighten the maximum loan-to-value ratio or restrict the collateral used in calculating the loan-to-value ratio is prepared in cooperation with the Bank of Finland and the

Ministry of Finance, based on a comprehensive analysis assessing growth in risks to financial stability, including the exceptional nature of such growth.

The level of the maximum loan-to-value ratio may be lowered if the analysis undertaken discloses factors endangering the stability of the financial system and relating to

- growth in the stock of residential mortgages granted to households (taking also into account other household debt)
- a threat of overheating on the housing market or
- other developments pertaining to the macro economy that may have an impact on residential mortgage or housing markets.

In assessing household indebtedness, household debt will be aligned in relation to disposable household income and macroeconomic developments. Attention will be focused on the significance of residential mortgage lending in household indebtedness, the current and expected interest rate level, as well as loan repayment periods and other lending practices.

In evaluating housing market overheating, account will be taken of, in particular, house price developments relative to the earnings level and macroeconomic performance. The evaluation will consider the most significant regional differences in house price developments.

Tightening of the maximum loan-to-value ratio may be warranted, for example, in a situation where residential mortgage lending and house prices begin to rise strongly in connection with a cyclical upswing in the economy. In such a scenario, lending and price developments could reinforce each other, leading to an overheating on housing and residential mortgage markets. The aim of tightening the maximum loan-to-value ratio is, in this case, to dampen growth in the size of new residential mortgages and help reduce the number of households taking out residential mortgages that are large in terms of the loan-to-value ratio and possibly defaulting or strongly reducing their consumption at the same time as the economy weakens and house prices fall.

An assessment of a potential tightening of the maximum loan-to-value ratio and restriction of the collateral used in calculating the loan-to-value ratio is supported by statistical data on credit developments, broken down by loan-to-value ratio.

The above analysis makes use of the following indicators:

i) developments in residential mortgages and other loans granted by monetary financial institutions to households, developments in repayment periods agreed for new residential mortgages, interest rate margins and interest rate linkages
ii) changes in the ratio of the stock of residential mortgages and other household loans to disposable annual income
iii) changes in the ratio of the stock of residential mortgages and other household loans to GDP
iv) factors impacting households' debt-servicing ability, such as developments in unemployment and the interest rate level (and the relevant forecasts)
v) nominal and real house price developments in the country as a whole and particularly in regions of high house prices, changes in the ratio of house prices to wage and salary earnings, and
vi) developments in loan-to-value ratios for new residential mortgages, and indicators for the distribution of such ratios.

In changing the upper limits for the maximum loan-to-value ratio, a change to the permitted maximum amount of a loan taken out for a first home purchase may, for justified reasons, deviate from changes to the permitted maximum amounts of other loans.

The taking into account of any other collateral security except real security in calculating the loan-to-value ratio may be restricted if it is necessary in order to ward off factors jeopardising the stability of the financial system, as disclosed by the analysis, or if the use of collateral other than real security is so extensive that it endangers the effectiveness of the maximum loan-to-value ratio for the mitigation of risks to the financial system.

Decision-making process

Prior to making decisions as referred to above, the FIN-FSA must request an opinion from the sector concerned.

A decision to lower the maximum loan-to-value ratio or to restrict the use of collateral enters into force at the earliest after three months from the date of the decision or a later date as determined by the FIN-FSA.

A decision on alleviating these requirements may take immediate effect. In the event of any alleviation, use will be made of the same indicators.

On 27 September 2023, the FIN-FSA Board has extended these principles to also apply, as from 1 January 2024, to institutions defined in section 1 of the Act on the Registration of Certain Credit Providers and Credit Intermediaries.