



ESRB

European Systemic Risk Board

European System of Financial Supervision

Press release

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ESRB issues a recommendation on vulnerabilities in the commercial real estate sector in the European Economic Area

The European Systemic Risk Board (ESRB) has today published a [recommendation](#) on vulnerabilities in the commercial real estate sector in the European Economic Area (EEA).

The ESRB recommends that EU and national authorities improve the monitoring of systemic risks stemming from the commercial real estate sector. Monitoring vulnerabilities related to this sector is key to identifying potential risks to financial stability and to assessing possible responses. The nature of the vulnerabilities varies across EEA countries. Based on the findings from monitoring, EU and national authorities should ensure that financing practices in the sector are sound and financial institutions are resilient. Furthermore, the European Commission should assess the current macroprudential framework and ensure that consistent rules for addressing risks related to commercial real estate exposures are applied across all financial institutions when they perform the same activities, taking into account their specificities.

The recommendation is based on an assessment of vulnerabilities identified in the commercial real estate sector that could be a source of risk to financial stability. The findings show that the sector is currently vulnerable to cyclical risks related to heightened inflation, a tightening of financial conditions limiting the scope for refinancing existing debt and taking new loans, and the pronounced deterioration in the growth outlook following Russia's invasion of Ukraine. Vulnerabilities related to structural changes include the impact of climate-related economic policies, such as stricter building standards, and the shift towards e-commerce. In addition, the coronavirus (COVID-19) pandemic has accelerated the demand for flexibility in leasable office space as remote and hybrid working models have become more widespread.

Furthermore, the ESRB's analysis shows that adverse developments in the commercial real estate sector can have a systemic impact on the financial system and the real economy. Such vulnerabilities can be amplified by spillovers across countries and through interlinkages between financial institutions. Credit institutions such as banks are particularly exposed to this sector via credit risk on loans. Available data suggest that bank lending to the sector is occurring at high loan-to-value ratios in several EEA countries. If the value of the loan collateral decreases, the loan-to-value ratio goes up, increasing banks' loss-given-default ratios and potentially leading to higher provision and capital requirements. Eventually, this could limit banks' ability to maintain credit supply. One of the

vulnerabilities for the non-banking sector is related to liquidity mismatches in open-ended real estate investment funds. Risks related to pension funds and insurance undertakings in commercial real estate markets differ across jurisdictions, reflecting different business models and practices, as well as different market structures. A materialisation of risks in the commercial real estate market would also negatively affect the credit rating of securitisations used to pool sector loans, which are held by credit institutions or other market participants.

Further details of the ESRB's assessment are included in the ESRB report entitled "[Vulnerabilities in the EEA commercial real estate sector](#)", which has also been published today. The assessment of vulnerabilities is based on available data and mostly covers developments up to mid-2022. It includes all EU Member States and also Iceland, Liechtenstein and Norway.

With the publication of the recommendation and the report, the ESRB concludes its third regular assessment of vulnerabilities in the commercial real estate sector. The ESRB has undertaken this monitoring on a continuing basis because of the sector's importance for financial and macroeconomic stability. In [2016](#), the ESRB issued a recommendation on closing real estate data gaps (amended in [2019](#)). In [2015](#) and [2018](#), the ESRB also conducted assessments of CRE vulnerabilities in the European Union.

The assessment of vulnerabilities in the commercial real estate sector is without prejudice to the overriding importance of other sources of systemic risk, as described in the [ESRB warning of September 2022](#). Going forward, the ESRB will continue exercising its mandate of macroprudential oversight of the financial system in the EU Member States, Iceland, Liechtenstein and Norway, including identifying financial stability vulnerabilities related to real estate. The ESRB will continue to issue warnings if a significant systemic risk to financial stability is identified and, where appropriate, will issue recommendations for remedial action.

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