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ECB ESTIMATION OF SENSITIVITY TO HOUSE-PRICE AND INTEREST RATE SHOCKS

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The global financial crisis has brought about adverse consequences for households. Across the euro area, households experienced financial pressures regarding their wealth, income and consumption. To measure the potential financial fragility of households in response to external shocks, the ECB used euro area household micro data collected by the Household Finance and Consumption Survey and applied various alternative shock specifications.[1]

This report summarizes the main findings of the ECB's sensitivity analysis of house prices and interest rate shocks, with a focus on Maltese households.[2]

The relatively resilient situation in Malta is corroborated by the estimated effect of a negative shock to house prices, specifically the impact of a 20% decline in property prices on the households' debt-to-asset ratio. As a result, the median debt-to-asset ratio generally increases in all countries. The change varies across countries and ranges from 1% to 6.5%. Malta is the second most resilient country, with just a 1% increase in the median ratio (see Chart 1).

Particularly vulnerable households, with a debt-to-asset ratio above 100%, and therefore with negative equity, are also analysed against the drop in house prices. In this respect, Malta emerges as the country with the least share of households that experience a negative equity position in the euro area. This share stands at only 2.4% in Malta, while it is as high as 18% in the Netherlands and in Finland, and 16% in Germany (see Chart 2).

Chart 1
THE EFFECT OF A HOUSE PRICE SHOCK ON THE MEDIAN DEBT-TO-ASSETS RATIO
(2010, percentages, median of indebted households)

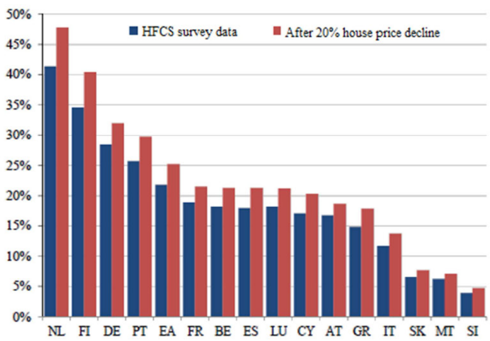
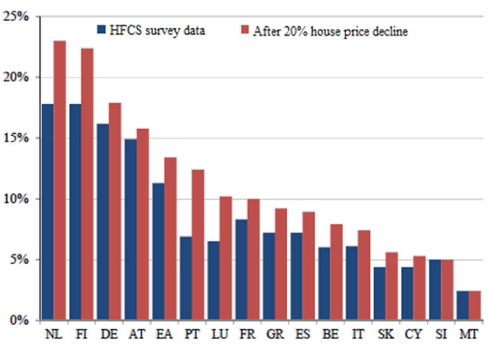


Chart 2
THE EFFECT OF A HOUSE PRICE SHOCK ON THE PROPORTION OF HOUSEHOLDS WITH A DEBT-TO-ASSETS RATIO ABOVE 100%
(2010, percentages of indebted households)



Source: Financial Stability Review, ECB, November 2013.

[1] Published in April 2013, the Eurosystem's Household Finance and Consumption Survey dataset contains information on the wealth, income and consumption patterns of more than 62,000 euro area households. The results serve as the baseline for the ECB's assessment of the sensitivity to shocks.

[2] This report draws on the ECB *Financial Stability Review*, November 2013, pages 32—35, which also provides information on data sources, a summary of the findings for other euro area countries and for references on the specification.

For such households, sensitivity to a decrease in house prices is also uneven across the euro area. In Malta the house-price shock would have no effect on the debt-to-asset ratio, while in almost all other euro area countries, it would show an increase particularly in the Netherlands and in Finland, where the share of households with negative equity would increase to 23% (see Chart 2). On the basis of these results Maltese households demonstrate strong resilience to external shocks in terms of mortgage solvency.

Separately, the estimation of the impact of a positive interest rate shock assesses the capacity of households to repay their debts without drawing on their assets. An increase of 300 basis points in the interest rate results in a moderate but varying rise of the median debt service-to-net income ratio in all countries. The ratio increases by 2.3% on average for the euro area, from 18.7% to 21%. Maltese households once again demonstrate a high degree of resilience to this shock, with an increase in the ratio equivalent to the euro area average, and just slightly above that registered by households in France or Germany.