



BANK ĊENTRALI TA' MALTA
EUROSISTEMA
CENTRAL BANK OF MALTA

CENTRAL BANK OF MALTA

DIRECTIVE NO XX

in terms of the

**CENTRAL BANK OF MALTA ACT
(CAP. 204)**

REGULATION OF BORROWER-BASED MEASURES

Ref: CBM/xx

Introduction

1. In terms of Article 17A of the Central Bank of Malta Act (Cap. 204) (hereinafter referred to as ‘the Act’), the Central Bank of Malta (hereinafter referred to as ‘the Bank’) is empowered to issue directives in order to develop macroprudential tools and implement macroprudential policy;

Objective of the Directive

2. In accordance with Directive 11, the objective of macroprudential policy shall be to contribute to the safeguard of the stability of the financial system as a whole, primarily by strengthening the resilience of the financial system and decreasing the build-up of systemic risk, thereby ensuring a sustainable contribution of the financial sector to economic growth;
3. The objective of the Directive is to strengthen the resilience of banks and borrowers against the potential build-up of vulnerabilities which could result in financial losses to both banks and borrowers stemming from potential unfavourable economic developments;

Scope and Application

4. The Directive shall apply to all credit institutions authorised under the Banking Act 1994 (Cap. 371 of the Laws of Malta) on a solo basis;
5. The Directive shall target both resident and non-resident borrowers entering into new residential real estate (RRE) loans secured by RRE;

Definitions

6. The following definitions shall apply for the purposes of this Directive:
 - a) **‘Annual Repayment’** – includes the combined interest and principal repayments on a borrower’s total debt over one year;
 - b) **‘Bank’** – means the Central Bank of Malta established by Article 3 of the Act;
 - c) **‘Borrower’** – means the signatory, or cosignatory, of a RRE loan contract and receiving financing from the lender;
 - d) **‘Buy-to-Let (BTL) Housing’** – means any RRE directly owned by a private natural and legal persons primarily for letting to tenants;
 - e) **‘Buy-to-Let (BTL) Loan’** – means the sum of all loans or loan tranches secured by the borrower on the BTL housing at the moment of loan origination;
 - f) **‘Category I Borrowers’** – comprises first-time buyers (FTBs) and non-FTBs purchasing their primary residence;

- g) **‘Category II Borrowers’** – any other loan to purchase an RRE excluding Category I Borrowers. This category comprises borrowers purchasing their second or additional RRE and natural and legal persons borrowing for BTL purposes;
- h) **‘Credit Institution’** – has the same meaning assigned to it by Article 2 of the Act;
- i) **‘Commercial Real Estate (CRE)’** – means any income-producing real estate, either existing or under development, and excludes (i) social housing; (ii) property owned by end-users; and (iii) BTL housing;
- j) **‘Debt Service to Income Ratio at Origination’ (DSTI-O)** – means the annual total debt service relative to the borrower’s total annual gross income at the moment of loan origination;
- k) **‘First-time Buyer’** – means a borrower who acquired his/her first immovable RRE property;
- l) **‘Gross Income’** – means the total monetary income received by the household over a specified income reference period, before deduction of income tax, regular taxes on wealth, employees’ or self-employed social security contribution and any recurrent sources of income. For joint loan accounts, income should include the joint gross income, unless the bank decides otherwise at loan evaluation stage. For BTL loans, rental income derived from the mortgage-backed property shall not be considered as gross income for the purpose of this Directive;
- m) **‘Loan’** – means the total amount made available to the borrower by means of a contract for the purchase, improvement and/or finishing of an RRE which is backed by the said RRE;
- n) **‘Loan-to-Value Ratio at Origination (LTV-O)’** – the sum of all loans or loan tranches secured by the borrower on the immovable property at the moment of loan origination relative to the market value of the property at the moment of loan origination;
- o) **‘Market Value of the Property’** – has the same meaning as assigned to it in point (76) of Article 3 of the Capital Requirements Regulation (Regulation (EU) No 575/2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012);
- p) **‘Maturity at Origination’** – the duration of the RRE loan contract expressed in years at the moment of loan origination;
- q) **‘Non-First Time Buyers purchasing their Primary Residence’** – means a borrower who already owns or owned a primary residence and intends to sell or sold his/her primary residence;
- r) **‘Primary Residence’** – means the RRE in which an individual habitually resides in or intends to habitually reside in as his/her principle place of abode;
- s) **‘Residential Real Estate Loan’** – means a loan to a private individual secured by RRE collateral;

- t) **‘Residential Real Estate’** – means any immovable property located in the domestic territory, available for RRE purposes, acquired, built or renovated by a private individual and that is not qualified as a CRE property;
- u) **‘Second Residential Real Estate’** – means property classified as residence other than primary residence and includes summer residence, vacant property, or BTL property;
- v) **‘Speed Limit’** – restricts the share of new RRE lending at LTV-O over the thresholds stipulated in this Directive;

Exemptions

- 7. Loans of Category I Borrowers with a collateral market value below EUR175,000 (*excluding haircuts*) are exempted from the LTV-O and DSTI-O limits specified in this Directive. Credit institutions shall still apply prudent lending policies in terms of the MFSA Notice on the Management of Credit Risk by Credit Institutions authorised under the Banking Act 1994 (BN/01/2002) in relation to loans of Category I Borrowers with collateral market value falling below EUR175,000 (*excluding haircuts*);

Borrower-Based Measures

Compliance with LTV-O Limits for New Residential Real Estate Loans

- 8. A credit institution shall ensure that the LTV-O for Category I Borrowers shall not exceed the 90 per cent LTV-O;
- 9. A credit institution shall ensure that the LTV-O ratio of an RRE loan for Category II Borrowers shall not exceed 85 per cent in the first year of the coming into force of this Directive and 75 percent in the years thereafter;
- 10. A credit institution shall ensure that the total volume of RRE loans provided to Category I Borrowers with an LTV-O beyond the 90 per cent threshold does not exceed 10 per cent of the total volume of RRE loans provided to Category I Borrowers in a given quarter;
- 11. A credit institution shall ensure that the total volume of RRE loans advanced for Category II Borrowers with an LTV-O beyond that set in paragraph 9 shall not exceed 20 per cent of the total volume of RRE loans provided in a given quarter;
- 12. Credit institutions shall follow established prudent credit risk management practices when exercising the speed limits;
- 13. For the purposes of calculating the LTV-O, credit institutions shall determine the collateral value in a prudent and conservative manner in accordance with paragraphs 11-14 of the MFSA Banking Rule on the Measures addressing credit risks arising from the assessment of the quality of asset portfolios of credit institutions authorised under the Banking Act 1994 (BR/09/2016);

14. No additional collateral (financial and non-financial) besides that backing the RRE loan should be taken into account when calculating the LTV-O, except when exercising the speed limit;

Compliance with DSTI-O Limits for New Residential Real-Estate Loans

15. A credit institution shall assess the borrowers' ability to service the RRE loan by applying a stressed DSTI-O of 40% limit, subject to an interest rate shock of 150 basis points for both Category I and Category II Borrowers. The stressed DSTI-O shall be calculated as follows:

$$DSTI-O_{\text{stressed}} = \frac{\text{Annual Repayment}|\Delta r_{\text{stressed}}}{\text{Gross Income}}$$

$$\Delta r_{\text{stressed}} = +150 \text{ bp}$$

16. A credit institution shall identify the total amount of the borrower's debt servicing when applying the affordability test specified in para 15 of this Directive;

Compliance with Maturity Limits for All New Residential Real-Estate Loans

17. The maturity term at origination of an RRE loan provided for Category I Borrowers shall not exceed the horizon of 40 years or the official retirement age, whichever occurs first;
18. The maturity term of an RRE loan provided for Category II Borrowers shall not exceed the horizon of 20 years or the official retirement age, whichever occurs first;
19. The official retirement age referred to in paragraphs 17 and 18 of this Directive is based on the statutory pension age as follows:
- a. In the case of a person born during the years 1952 to 1955: the pension age shall be 62 years;
 - b. In the case of a person born during the years 1956 to 1958: the pension age shall be 63 years;
 - c. In the case of a person born during the years 1959 to 1961: the pension age shall be 64 years;
 - d. In the case of a person born after 1961 the pension age shall be 65 years;

Summary of Borrower-Based Measures as specified in Articles 8-19

	LTV-O	DSTI-O	Maturity
<u>Category I Borrowers</u>	90% LTV-O cap with a ' <i>speed limit</i> ' of 10% on the volume of loans, for loans with a market value in excess of EUR175,000	A stressed DSTI-O of 40% for loans with a market value in excess of EUR175,000 with a shock to interest rates of 150 bps	A maturity term of 40 years or the official retirement age – whichever occurs first: 1952 – 1955: 62 years 1956 – 1958: 63 years 1959 – 1961: 64 years Born after 1961: 65 years
<u>Category II Borrowers</u>	<u>Gradual Phase-in:</u> <u>1st year:</u> 85% LTV-O cap with a ' <i>speed limit</i> ' of 20% on the volume of loans <u>2nd year:</u> 75% LTV-O cap with a ' <i>speed limit</i> ' of 20% on the volume of loans	A stressed DSTI-O of 40% with a shock to interest rates of 150 bps	A maturity term of 20 years or the official retirement age – whichever occurs first: 1952 – 1955: 62 years 1956 – 1958: 63 years 1959 – 1961: 64 years Born after 1961: 65 years

Assessment of Compliance with the Regulations

20. Credit institutions shall be required to assess their compliance with the Directive through an annual external audited self-assessment on the adherence to these measures. This without prejudice to on-site and off-site supervision by the MFSA. The audited self-assessment is to be forwarded to the Bank;
21. Non-compliance with the requirements set out in this Directive shall be subject to administrative penalties imposed by the Bank in terms of Article 56 of the Act;

Final Provisions

22. This Regulation shall enter into force upon publication.