Banc Ceannais na hÉireann
Central Bank of Ireland

Eurosystem

Central Bank of Ireland
Financial Stability Review 2024:I

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Notes

1. Unless otherwise stated, this document refers to data available on 24th May 2024.

2. Unless otherwise stated, the aggregate banking data refer to all credit institutions operating in the Republic of Ireland.

   The term "domestic banks" refers to the three banks offering retail banking services within the Irish State: Allied Irish Banks plc, The Governor and Company of the Bank of Ireland and Permanent TSB, unless stated otherwise.

3. The following symbols are used:

e	estimate	H	half-year
f	forecast	rhs	right-hand scale
Q	quarter	lhs	left-hand scale

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Preface

The Central Bank is responsible for maintaining monetary and financial stability and ensuring the financial system works in the interests of the community.

The *Financial Stability Review* evaluates the main risks facing the financial system and assesses the resilience of the financial system to those risks. A resilient financial system is one that is able to provide services to Irish households and businesses, both in good times and in bad. The Central Bank's policy actions seek to ensure that the financial system functions in this manner.

The structure of this publication mirrors the overall approach the Central Bank takes in reaching a judgement around its macroprudential policy stance.

- The first section outlines the Central Bank's assessment of the main risks facing the Irish financial system over the short to medium term.
- The second section outlines the Central Bank's assessment of the resilience of the domestic-facing financial system to adverse shocks and its ability to absorb, rather than amplify, shocks of this nature.
- The third section explains the Central Bank's policy actions to safeguard financial stability and ensure that the resilience of the financial system is proportionate to the risks it faces.

Ireland is host to a large and diverse financial sector. A large part of that financial sector serves international clients, with limited direct implications for the domestic economy. This publication focuses on the segments of the financial sector that provide services to Irish households and businesses.

The Central Bank is committed to transparency over its judgements around financial stability and uses the *Financial Stability Review* as a key vehicle to explain the policy actions taken, within its mandate, to safeguard financial stability. The publication reflects, and is informed by, the deliberations of the Central Bank's Financial Stability Committee. It focuses on adverse outcomes that may materialise, and their potential implications for domestic financial stability in the event of materialisation, rather than on presenting economic forecasts.

Réamhrá

Tá an Banc Ceannais freagrach as cobhsaíocht airgeadaíochta agus airgeadais a choimeád ar bun agus as a chinntiú go bhfeidhmeoidh an córas airgeadais ar mhaithe le leas an phobail.

San *Athbhreithniú ar Chobhsaíocht Airgeadais*, déanaimid measúnú ar na príomhrioscaí atá ann don chóras airgeadais agus ar athléimneacht an chórais airgeadais i leith na rioscaí sin. Is ionann córas airgeadais athléimneach agus córas atá in ann seirbhísí a chur ar fáil do theaghlaigh agus do ghnóthaí Éireannacha le linn tréimhsí maithe agus drochthréimhsí araon. Le gníomhaíochtaí beartais an Bhainc Ceannais, féachtar lena chinntiú go bhfuil an córas airgeadais in ann turraingí dochracha a iompar seachas a mhéadú.

Tá struchtúr an fhoilseacháin seo ag teacht leis an gcur chuige foriomlán atá ag an mBanc Ceannais chun teacht ar bhreithniú maidir lena sheasamh beartais macrastuamachta.

- Sa chéad mhír, déantar cur síos ar mheasúnú an Bhainc Ceannais ar na príomhrioscaí atá roimh chóras airgeadais na hÉireann sa ghearrthéarma agus sa mheántéarma.
- Sa dara mír, leagtar amach measúnú an Bhainc Ceannais ar athléimneacht an chórais airgeadais intíre i leith turraingí dochracha agus ar a chumas rioscaí den sórt sin a iompar seachas a mhéadú.
- Sa tríú mír, déantar cur síos ar ghníomhaíochtaí beartais an Bhainc Ceannais chun cobhsaíocht airgeadais a chosaint agus chun a chinntiú go bhfuil athléimneacht an chórais airgeadais comhréireach leis na rioscaí atá roimhe.

Tá earnáil mhór ilchineálach airgeadais in Éirinn. Tá fás ag teacht ar an gcuid sin de sheirbhísí earnála airgeadais a fhreastalaíonn ar chliaint idirnáisiúnta, agus tá impleachtaí díreacha teoranta ann don gheilleagar intíre. Dírítear san fhoilseachán seo ar na codanna sin den earnáil airgeadais a chuireann seirbhísí ar fáil do theaghlaigh agus do ghnóthaí Éireannacha.

San *Athbhreithniú*, léirítear breithnithe ón gCoiste um Chobhsaíocht Airgeadais de chuid an Bhainc Ceannais agus tá na breithnithe sin mar bhonn eolais don *Athbhreithniú*. Ní hé is aidhm don *Athbhreithniú* réamhaisnéis eacnamaíoch a chur ar fáil, ina ionad sin díríonn sé ar thorthaí díobhálacha a d’fhéadfadh teacht chun cinn agus ar na himpleachtaí a d’fhéadfadh a bheith acu don chobhsaíocht airgeadais intíre. Tá an Banc Ceannais tiomanta do thrédhearcacht a chuid breithnithe maidir le cobhsaíocht airgeadais agus tá sé beartaithe aige an foilseachán seo a úsáid mar bhealach tábhachtach chun míniú a thabhairt ar na gníomhaíochtaí beartais a ghlactar laistigh dá shainordú chun cobhsaíocht airgeadais a chosaint.

Overview

The global economy continues to surprise in its resilience to higher interest rates, with short-term, acute macro-financial risks receding somewhat since the last *Review*. Rising geopolitical tensions bring with them the possibility of further negative shocks, posing particular concern in open, globalised economies such as Ireland. Sustained falls in inflation are opening the prospect of falling interest rates in Europe this year, although markets may be under-pricing risks around the "last mile" of the monetary policy response. In the US, inflation is proving more stubborn, with higher interest rates now likely to last for longer than previously expected. A prolonged period of higher rates could expose risks in the global financial system related to optimistic pricing in equity and bond markets. These risks could be exacerbated by high levels of public and private debt and vulnerabilities in the non-bank financial sector, increasing the imperative for policy action to mitigate systemic risks posed by the sector.

Ireland has experienced sustained economic growth, albeit at a slower pace recently, with the labour market close to full employment. Households and businesses remain resilient to the ongoing adjustment to higher interest rates, with only modest increases in arrears and insolvencies up to now. The domestic CRE market is in the midst of a sharp downturn, which will have implications for borrowers and lenders, but the Central Bank's judgement is that the domestic banking sector is well placed to absorb – rather than amplify – this shock. Irish banks posted strong profits last year, supporting their financial resilience as well as their capacity to build operational resilience. Against this backdrop, the Central Bank is maintaining the CCyB at 1.5 per cent, strengthening banks' resilience to macro-financial risks, and continues to develop the macroprudential framework for non-banks.

Inflation has continued to fall globally, but geopolitical tensions bring with them the risk of further shocks. Inflation increased sharply in 2021 and 2022 driven by supply shocks from the pandemic and Russia's invasion of Ukraine, but it has gradually declined towards central bank target levels. However, the risk of delays in reaching central bank inflation targets along the "last mile" remains, as evidenced by market repricing in the US since the last *Review*. Inflationary risks from geopolitical tensions also remain. Further escalation in the Middle East, for example, could hamper global supply chains, which are particularly relevant for global inflation through commodity and food markets, and shipping of manufactured goods more broadly.

The global economy has proven resilient so far, but risks from higher interest rates remain. Since the last *Review*, a combination of falling inflation and continued economic growth has supported the global outlook, although growth is expected to be more subdued in Europe compared with the US. There are significant downside risks and uncertainty around this outlook, particularly from the ongoing lagged impact of higher interest rates, which affect households and businesses as they refinance loans issued under lower rates. Medium-term vulnerabilities have also been building, particularly related to levels of private and public debt. Strength in the US economy brings with it a likely longer period of higher US interest rates, with implications for the global financial system.

A longer period of high interest rates could expose vulnerabilities in the global financial system. Financial market volatility has been low in some sectors, with equity prices rising and risk premia

in credit markets compressing. Markets may be "priced for perfection", since expectations last year were firmly for monetary policy easing on both sides of the Atlantic. Given its primacy in the global financial system, elevated US interest rates may force downward adjustments in a range of global asset prices, adding to the recent volatility in interest-rate markets.

Vulnerabilities in the non-bank sector could amplify market adjustments. Two potential sources of vulnerabilities for non-banks are liquidity mismatch and leverage. These vulnerabilities can increase the fragility of pockets of the sector under stressed conditions, causing them to amplify shocks, and potentially transmit them to other segments of the wider financial system and economy. A prominent recent example is the gilt market turbulence of September 2022 in the UK, where high leverage and concentrated positions among some funds led to the amplification of the shock.

Global and Irish CRE markets are firmly in a downturn, although there are significant sectoral differences. Global CRE markets, particularly in office and retail, are exposed to the twin shocks of pandemic-related demand changes and the sharp rise in interest rates since 2022. The Irish CRE market is no different, with capital values in the office and retail sectors down an estimated 29 and 38 per cent, respectively, since their peak. The Dublin office market has been among the most acute increases in vacancy rates and falls in take-up rates in Europe. Rents may not have fully adjusted to the severity of the shock, risking further falls in office capital values. The residential and industrial markets, by contrast, have had a more benign outcome since the pandemic, and are offsetting the shocks to the office and retail markets to some extent.

Despite the magnitude of the CRE shock, the adjustment in the domestic financial system has, so far, been orderly. A more diversified investor base in Irish CRE, in terms of its geographic origin, investor entity type and financing source, mitigates domestic macro-financial risks through greater risk sharing. Irish banks are at the core of domestic financial intermediation, and their balance sheets are less exposed to CRE risks than in the past, both due to a smaller loan book as well as credit risks being mitigated by more prudent underwriting practices and a gradual refinancing profile. The Central Bank's judgement is that the domestic banking system is sufficiently resilient to absorb – rather than amplify – this CRE downturn. Bridging data gaps on potential new macro-financial interlinkages in this evolving market remains a priority to support risk assessments. The Central Bank today publishes a detailed assessment in the accompanying *FSR Special Feature*.

Irish household finances have been supported by a gradual and uneven pass-through of higher interest rates, underpinned by a strong labour market. Despite the level of increase in the ECB policy rate since 2022, most mortgage borrowers have seen manageable changes in their monthly repayments, owing to a large share of fixed-rate lending, proactive switching behaviour, and the slow pass-through of monetary policy rates to lending rates. Irish household solvency is being supported by a strong labour market driving nominal income growth, coupled with healthy liquid savings and low debt levels relative to income, gradually bolstered by the Central Bank's mortgage measures for close to a decade.

SME profit margins have held up despite significant cost inflation. Irish businesses have experienced a large shock to their cost base since 2021. Despite this, and certain sector-specific

challenges, businesses have been broadly able to maintain or increase their profit margins, clearly demonstrating the underlying strength of demand in the real economy. Insolvencies are rising, but only to levels seen in the pre-pandemic period of strong growth.

Domestic bank profitability has increased significantly in the higher interest-rate environment, but is expected to moderate this year. Irish banks had extremely strong profitability growth last year, driven by increases in margins on loans, particularly tracker mortgages, and the direct impact of monetary policy on their earnings on reserves. Any lowering of monetary policy rates would directly reduce profitability through these channels, while lagged effects of higher interest rates may yet emerge through deposit competition increasing funding costs, as well as increases in impairment charges and a moderation of loan volume growth.

Irish government finances are strong, but reliance on multinationals poses risks in an uncertain geopolitical context. The Irish government's debt levels have fallen relative to the economy over the past decade. Higher interest rates are having only a gradual and modest impact on interest burdens due to the maturity profile of outstanding debt. However, this headline position could prove to be fragile. Recent surpluses are heavily reliant on the receipts of a small number of large multinational tax payers in a narrow set of sectors. This concentration risk is particularly salient when set against rising geopolitical tensions and the potential for increased trade protectionism and sector-specific shocks.

The CCyB rate of 1.5 per cent is now in effect, and continues to support the resilience of the banking sector to shocks. The Central Bank's strategy for the CCyB involves maintaining the buffer at 1.5 per cent when cyclical risks are neither subdued nor elevated. The nature of the buffer provides scope for the Central Bank to release the buffer should systemic risks crystallise, supporting banks' ability to lend during a downturn. The Central Bank judges that the 1.5 per cent rate remains appropriate given the current macro-financial risk environment.

Mortgage lending to First Time Buyers has continued to grow, but lending standards are being supported by the macroprudential mortgage measures. The refreshed mortgage measures framework has now been in place since January 2023. Consistent with the Central Bank's aim of mitigating some of the costs of the measures, without unduly compromising the benefits of strengthened resilience, more FTB lending is being facilitated at or close to the new LTI limit of 4. The Central Bank continues to judge that the measures are fostering sustainable lending standards, limiting the feedback loop between the mortgage and housing markets.

The Central Bank continues to develop the macroprudential framework for non-banks and has two macroprudential measures relating to cohorts of investment funds in place. New macroprudential policy measures for Irish-authorised GBP-denominated liability driven investment (LDI) funds were announced in April 2024, and aim to make this cohort of funds more resilient to shocks to UK interest rates. After the phased implementation of macroprudential measures for property funds, these are the second measures under the third pillar of the Central Bank's macroprudential framework in relation to non-banks. The Central Bank welcomes the feedback received to the Discussion Paper on an approach to macroprudential policy for investment funds, and has continued engagement with stakeholders on this topic by hosting an international conference in May 2024.

Forbhreathnú

Tá an geilleagar domhanda fós ina ábhar iontais maidir lena athléimneacht in aghaidh rátaí úis níos airde, agus tá rioscaí géara macra-airgeadais gearrthéarmacha ag cúlú beagán ó rinneadh an t*Athbhreithniú* deireanach. Mar gheall ar an teannas geopholaitiúil atá ag dul i méid, d'fhéadfadh suaití diúltacha breise a bheith i gceist, a d'fhéadfadh a bheith ina ábhar imní ar leith i ngeilleagair oscailte dhomhandaithe amhail Éire. Le titim leanúnach sa bhoilsciú, tá seans ann go dtiocfaidh laghdú ar rátaí úis san Eoraip i mbliana, cé go bhféadfadh rioscaí praghsála faoi bhun an 'mhíle deiridh' den fhreagairt beartais airgeadaíochta a bheith sna margaí. Sna Stáit Aontaithe, tá boilsciú ag éirí níos déine, agus is dócha anois go mairfidh rátaí úis níos airde níos faide ná mar a bhíothas ag súil leis roimhe seo. D'fhéadfadh tréimhse fhada de rátaí níos airde rioscaí a nochtadh sa chóras airgeadais domhanda a bhaineann le praghsáil dhóchasach i margaí cothromais agus bannaí. D'fhéadfadh na rioscaí sin a bheith níos measa mar gheall ar leibhéil arda fiachais phoiblí agus phríobháidigh agus leochaileachtaí san earnáil airgeadais neamhbhainc, a mhéadaíonn an gá atá le gníomhaíocht bheartais chun rioscaí sistéamacha a bhaineann leis an earnáil a mhaolú.

Tá fás eacnamaíoch marthanach tagtha ar Éirinn, cé go bhfuil an fás sin ag luas níos moille le déanaí, agus is gearr go mbeidh lánfhostaíocht i margadh an tsaothair. Tá teaghlaigh agus gnólachtaí fós athléimneach maidir leis an gcoigeartú leanúnach ar rátaí úis níos airde, gan ach méaduithe beaga ag teacht ar riaráistí agus ar dhócmhainneachtaí go dtí seo. Tá margadh intíre eastáit réadaigh tráchtála (ERT) i lár géarchoir chun donais, rud a mbeidh impleachtaí aige d'iasachtaithe agus d'iasachtóirí, ach is é breithiúnas an Bhainc Ceannais go bhfuil an earnáil baincéireachta intíre in ann an suaitheadh sin a mhaolú – seachas a mhéadú. Bhreac bainc na hÉireann brabúis láidre anuraidh, ag tacú lena n-athléimneacht airgeadais chomh maith lena gcumas athléimneacht oibríochtúil a fhorbairt. I bhfianaise an mhéid sin, tá caipiteal maolánach fritimthriallach (CCyB) á choinneáil ag an mBanc Ceannais ag 1.5 faoin gcéad, rud a neartaíonn athléimneacht na mbanc i leith rioscaí macra-airgeadais, agus leanann sé den chreat macrastuamachta a fhorbairt do neamhbhainc.

Tá titim leanúnach ag teacht ar an mboilsciú ar fud an domhain, ach tá baol ann go mbeidh tuilleadh suaití ann mar thoradh ar theannas geopholaitiúil. Tháinig méadú mór ar an mboilsciú in 2021 agus 2022 mar gheall ar shuaití soláthair de bharr na paindéime agus de bharr ionradh na Rúise ar an Úcráin, ach tá laghdú tagtha air de réir a chéile i dtreo spriocleibhéil bainc ceannais. Mar sin féin, tá an riosca fós ann go mbeidh moill i gceist le spriocanna boilscithe banc ceannais a bhaint amach feadh an 'mhíle deiridh', mar is léir ón athphraghsáil ar an margadh sna Stáit Aontaithe atá tarlaithe ó bhí an t*Athbhreithniú* deireanach ann. Tá rioscaí boilscithe ó theannas geopholaitiúil fós i gceist freisin. D'fhéadfadh géarú breise sa Mheánoirthear, mar shampla, bac a chur ar shlabhraí soláthair domhanda, atá ábhartha go háirithe don bhoilsciú domhanda trí mhargaí tráchtearraí agus bia, agus loingseoireacht earraí monaraithe ar bhonn níos leithne.

Tá sé cruthaithe go bhfuil an geilleagar domhanda athléimneach go dtí seo, ach tá rioscaí fós i gceist ó rátaí úis níos airde. Ó rinneadh an t*Athbhreithniú* deireanach, thacaigh meascán de bhoilsciú atá ag titim agus fás eacnamaíoch leanúnach leis an ionchas domhanda, cé go meastar go mbeidh an fás níos ísle san Eoraip i gcomparáid leis na Stáit Aontaithe. Tá rioscaí suntasacha agus

éiginnteacht shuntasach ar an taobh thíos i gceist leis an ionchas sin, go háirithe mar gheall ar an tionchar diúltach leanúnach atá ag rátaí úis níos airde, rud a imríonn tionchar ar theaghlaigh agus ar ghnólachtaí agus iasachtaí a eisítear faoi rátaí níos ísle á n-athmhaoiniú acu. Tá leochaileachtaí meántéarmacha ag teacht chun cinn freisin, go háirithe maidir le leibhéil an fhiachais phríobháidigh agus phoiblí. D'fhéadfadh tréimhse níos faide de rátaí úis níos airde a bheith sna Stáit Aontaithe mar thoradh ar an neart i ngeilleagar na Stát Aontaithe, a mbeidh impleachtaí don chóras airgeadais domhanda i gceist leis.

D'fhéadfadh tréimhse níos faide de rátaí arda úis leochaileachtaí a nochtadh sa chóras airgeadais domhanda. Bhí luaineacht an mhargaidh airgeadais íseal i roinnt earnálacha, agus praghsanna cothromais ag ardú agus préimheanna riosca ag comhbhrú sna margaí creidmheasa. D'fhéadfadh sé go mbeadh margaí "praghsáilte go foirfe", ós rud é gur bhain ionchais na bliana seo caite go láidir le héascú beartais airgeadaíochta ar dhá thaobh an Atlantaigh. I bhfianaise a thosaíochta sa chóras airgeadais domhanda, d'fhéadfadh rátaí úis arda sna Stáit Aontaithe coigeartuithe anuas a chur i bhfeidhm i raon praghsanna sócmhainní domhanda, rud a chuirfeadh leis an luaineacht a bhí ann le déanaí i margaí rátaí úis.

D'fhéadfadh leochaileachtaí san earnáil neamhbhainc coigeartuithe margaidh a mhéadú. Is dhá fhoinse leochaileachtaí a d'fhéadfadh a bheith i gceist do neamhbhainc iad neamhréir leachtachta agus giaráil. Is féidir leis na leochaileachtaí sin leochaileacht phócaí na hearnála a mhéadú faoi dhálaí anáis, rud a fhágann go méadaíonn siad suaití, agus go bhféadfaí iad a tharchur chuig codanna eile den chóras airgeadais agus den gheilleagar i gcoitinne. Sampla suntasach le déanaí is ea suaiteacht an mhargaidh sárurrúis i mí Mheán Fómhair 2022 sa Ríocht Aontaithe, áit a raibh méadú ar an suaitheadh mar thoradh ar shuíomhanna ardghiarála agus comhchruinnithe i measc cistí áirithe.

Tá margaí eastáit réadaigh tráchtála domhanda agus na hÉireann ag dul chun donais go mór, cé go bhfuil difríochtaí suntasacha earnála i gceist. Tá margaí eastáit réadaigh tráchtála domhanda, go háirithe i ndáil le hoifigí agus miondíol, neamhchosanta ar dhá shuaitheadh na n-athruithe ar an éileamh a bhaineann leis an bpaindéim agus ar an méadú géar ar rátaí úis ó 2022 i leith. Níl aon difríocht idir iad agus margadh eastáit réadaigh tráchtála na hÉireann, le luachanna caipitil sna hearnálacha oifige agus miondíola síos thart ar 29 agus 38 faoin gcéad, faoi seach, óna mbuaic. Tá an t-ardú ar rátaí folúntais agus an titim ar rátaí glactha i margadh oifigí Bhaile Átha Cliath i measc na rátaí is géire san Eoraip. D'fhéadfadh sé nach mbeadh cíosanna coigeartaithe go hiomlán do dhéine an tsuaite, rud a d'fhéadfadh titim bhreise i luachanna caipitil oifige a chur i mbaol. Os a choinne sin, bhí toradh níos neamhurchóidí ar na margaí cónaithe agus tionsclaíocha ó bhí an phaindéim ann, agus tá na suaití sna margaí oifigí agus miondíola á bhfritháireamh acu go pointe áirithe.

D'ainneoin mhéid an tsuaite san eastát réadach tráchtála, bhí an coigeartú sa chóras airgeadais intíre ordúil go dtí seo. Le bonn infheisteoirí níos éagsúlaithe in eastát réadach tráchtála na hÉireann, i dtéarmaí a thionscnaimh gheografaigh, a chineáil eintitis infheisteora agus a fhoinse maoiniúcháin, maolaítear rioscaí macra-airgeadais intíre trí chomhroinnt riosca níos mó. Tá bainc na hÉireann i gcroílár na hidirghabhála airgeadais intíre, agus níl a gcláir chomhardaithe níos neamhchosanta ar rioscaí san eastát réadach tráchtála ná mar a bhí san am a chuaigh thart, mar gheall ar leabhar iasachtaí níos lú chomh maith le rioscaí creidmheasa a bheith á maolú le

cleachtais frithghealllta níos stuama agus próifíl athmhaoinithe de réir a chéile. Is é breithiúnas an Bhainc Ceannais go bhfuil an córas baincéireachta intíre sách athléimneach chun an cor chun donais seo san eastát réadach tráchtála a mhaolú – seachas é a mhéadú. Is tosaíocht i gcónaí é bearnaí sonraí a líonadh maidir le hidirnaisc nua mhacra-airgeadais a d'fhéadfadh a bheith i gceist sa mhargadh athraitheach sin chun tacú le measúnuithe riosca. Foilsíonn an Banc Ceannais measúnú mionsonraithe sa lá atá inniu ann sa *Ghné Speisialta ACA* a ghabhann leis.

Tacaíodh le cúrsaí airgid teaghlaigh na hÉireann trí rátaí úis níos airde a chur ar aghaidh de réir a chéile agus go míchothrom, agus margadh saothair láidir mar bhonn taca leis sin. D'ainneoin leibhéal an ardaithe ar ráta beartais BCE ó 2022, tá athruithe soláimhsithe tagtha ar a n-aisíocaíochtaí míosúla i bhformhór na n-iasachtaithe morgáiste, mar gheall ar sciar mór d'iasachtú ar ráta seasta, iompar malartaithe réamhghníomhach, agus rátaí beartais airgeadaíochta a chur ar aghaidh go mall chuig rátaí iasachta. Tá tacaíocht á tabhairt do shócmhainneacht teaghlaigh na hÉireann ag margadh saothair láidir lena spreagtar fás ioncaim ainmniúil, mar aon le coigilteas leachtach sláintiúil agus leibhéil ísle fiachais i gcoibhneas le hioncam, arna neartú de réir a chéile ag bearta morgáiste an Bhainc Ceannais le beagnach deich mbliana anuas.

Tá corrlaigh bhrabúis FBManna fós láidir d'ainneoin boilsciú suntasach costais. Tá suaitheadh mór bainte as bonn costais ghnólachtaí na hÉireann ó 2021 i leith. Ina ainneoin sin, agus dúshláin áirithe a bhaineann go sonrach le hearnáil faoi leith, bhí gnólachtaí in ann a gcorrlaigh bhrabúis a choinneáil nó a mhéadú den chuid is mó, rud a léiríonn go soiléir bun-neart an éilimh san fhíorgheilleagar. Tá dócmhainneachtaí ag ardú, ach go dtí na leibhéil a chonacthas sa tréimhse roimh an bpaindéim lenar bhain fás láidir.

Tá méadú suntasach tagtha ar bhrabúsacht na mbanc intíre i dtimpeallacht an ráta úis níos airde, ach meastar go maolóidh sé i mbliana. Bhí fás brabúsachta an-láidir ag bainc na hÉireann anuraidh, rud a spreag méaduithe ar chorrlaigh ar iasachtaí, go háirithe morgáistí rianaithe, agus tionchar díreach an bheartais airgeadaíochta ar a dtuilleamh ar chúlchistí. Dá n-ísleofaí rátaí beartais airgeadaíochta, laghdófaí brabúsacht go díreach trí na bealaí sin, agus d'fhéadfadh éifeachtaí diúltacha rátaí úis níos airde teacht chun cinn fós trí iomaíocht taisce lena méadófaí costais chistiúcháin, chomh maith le méaduithe ar mhuirir lagaithe agus maolú ar fhás mhéid na n-iasachtaí.

Tá cúrsaí airgid rialtas na hÉireann láidir, ach tá rioscaí ag baint le bheith ag brath ar chuideachtaí ilnáisiúnta i gcomhthéacs geopholaitiúil éiginnte. Tá leibhéil fiachais rialtas na hÉireann tar éis titim le hais an gheilleagair le deich mbliana anuas. Níl ach tionchar beag de réir a chéile ag rátaí úis níos airde ar ualaí úis mar gheall ar phróifíl aibíochta an fhiachais gan íoc. Mar sin féin, d'fhéadfadh an príomhsheasamh sin a bheith leochaileach. Tá an barrachas a bhí i gceist le déanaí ag brath go mór ar fháltais líon beag cáiníocóirí ilnáisiúnta móra i sraith chúng earnálacha. Tá an riosca comhchruinnithe sin thar a bheith suntasach nuair a chuirtear é i gcoinne an teannais gheopholaitiúil atá ag dul i méid agus i gcoinne na caomhnaitheachta trádála méadaithe agus na suaití a bhaineann go sonrach le hearnáil a d'fhéadfadh a bheith i gceist.

Tá ráta an chaipitil mhaolánaigh fhritimthriallaigh 1.5 faoin gcéad i bhfeidhm anois, agus leanann sé ag tacú le hathléimneacht na hearnála baincéireachta i leith suaití. Is éard atá i gceist le straitéis an Bhainc Ceannais maidir leis an gcaipiteal maolánach fritimthriallach an maolán a choinneáil ag

1.5 faoin gcéad nuair nach mbíonn rioscaí timthriallacha faoi smacht ná ardaithe. Le cineál an mhaoláin, tugtar deis don Bhanc Ceannais an maolán a scaoileadh i gcás ina dtiocfadh laghdú ar rioscaí sistéamacha, rud a thacaíonn le cumas na mbanc iasachtaí a thabhairt le linn cor chun donais. Measann an Banc Ceannais go bhfuil an ráta 1.5 faoin gcéad fós iomchuí i bhfianaise na timpeallachta rioscaí macra-airgeadais atá ann faoi láthair.

Tá iasachtaí morgáiste do Cheannaitheoirí Céaduaire ag dul i méid i gcónaí, ach tá na bearta macrastuamachta morgáiste ag tacú le caighdeáin iasachta. Tá creat na mbeart morgáiste athnuaite i bhfeidhm anois ó mhí Eanáir 2023. I gcomhréir le haidhm an Bhainc Ceannais cuid de chostais na mbeart a mhaolú, gan cur isteach go míchuí ar na tairbhí a bhaineann le hathléimneacht níos láidre, tá níos mó iasachtaithe ar Ceannaitheoirí Céaduaire iad á éascú ag teorainn LTI nua 4 nó gar di. Measann an Banc Ceannais fós go bhfuil caighdeáin iasachtaithe inbhuanaithe á gcothú ag na bearta, rud a chuireann teorainn leis an lúb aischothaithe idir na margaí morgáiste agus tithíochta.

Leanann an Banc Ceannais ag forbairt an chreata macrastuamachta do neamhbhainc agus tá dhá bheart macrastuamachta i bhfeidhm ag an mbanc a bhaineann le cohóirt cistí infheistíochta. Fógraíodh bearta beartais macrastuamachta nua le haghaidh cistí infheistíochta faoi thionchar dliteanais (LDI) ainmnithe in GBP atá údaraithe in Éirinn i mí Aibreáin 2024, agus is é is aidhm dóibh an cohórt cistí sin a dhéanamh níos athléimní in aghaidh suaití ar rátaí úis na Ríochta Aontaithe. Tar éis chur chun feidhme céimnithe na mbeart macrastuamachta le haghaidh cistí maoine, is iad sin an dara beart faoin tríú colún de chreat macrastuamachta an Bhainc Ceannais i ndáil le neamhbhainc. Is díol sásaimh don Bhanc Ceannais an t-aiseolas a fuarthas ar an bPlépháipéar maidir le cur chuige i leith beartas macrastuamachta le haghaidh cistí infheistíochta, agus lean sé de bheith i dteagmháil le páirtithe leasmhara ar an ábhar seo trí chomhdháil idirnáisiúnta a óstáil mí na Bealtaine 2024.

Risk assessment

Global risk assessment

Inflation has fallen significantly but challenges remain in the "last mile" for central banks. Heightened geopolitical risk could generate further shocks that undermine the disinflation process. Interest rate uncertainty is heightened, with diminishing market expectations for interest rate cuts in the US due to a robust domestic economy. Higher for longer interest rates could expose vulnerabilities in the global financial system and strain public finances, while households and firms remain vulnerable as loans refinance onto sharply higher borrowing costs. CRE risks have intensified, with uncertainty around the ultimate impact on banks' balance sheets globally. Over-optimism and under-pricing of risk in financial markets, reflected in low volatility and compressed risk premia, could give rise to sharp asset price declines, with potential amplification from the non-bank sector.

Inflation has continued to fall globally but challenges remain along the "last mile" for central banks. Significant progress has been made in the global fight against inflation (Chart 1). However, challenges remain along "the last mile" to reaching target levels of inflation, particularly in relation to stickier core inflation. In the US, headline inflation increased unexpectedly in March while core inflation levels continue to suggest challenges may lie ahead. In the euro area, headline inflation also rose higher than expected in May, as strong domestic demand led to increases in services price inflation from 3.7 per cent to 4.1 per cent.[1]

Heightened geopolitical instability leaves open the prospect of further unexpected shocks. As a small, open economy, receiving investment and trade flows from a wide range of countries, global developments are particularly relevant for Ireland. The geopolitical environment has become more unstable in recent years, both through direct conflict and the wider fragmentation of the global system into competing blocs. Since the last *Review*, heightened tensions between Israel and Iran, and increased uncertainty over the next phase of the conflict in Ukraine, increase the likelihood of an unexpected geopolitical shock that could impact the domestic economy.

Geopolitical, cyber and climate risks could all compromise the global fight against inflation via supply chains or commodity markets. Russia's war against Ukraine and the conflict in the Middle East are examples of geopolitical risk that could undermine the global disinflation process through supply chain, commodity or food market channels (Chart 2). This may delay central bank easing of monetary policy. Countries with heightened exposure to geopolitical tensions are also at an increased risk of experiencing cyber incidents which could disrupt financial and economic activity. Furthermore, extreme weather events linked to climate change continue to become more frequent and more intense, and could generate shocks that are inflationary in nature, for example through the production of food or commodities, or supply chains more broadly.

Increasingly restrictive trade policies have consequences for global trade and investment. The rise in geopolitical tensions between major economies in recent years could accelerate the weakening

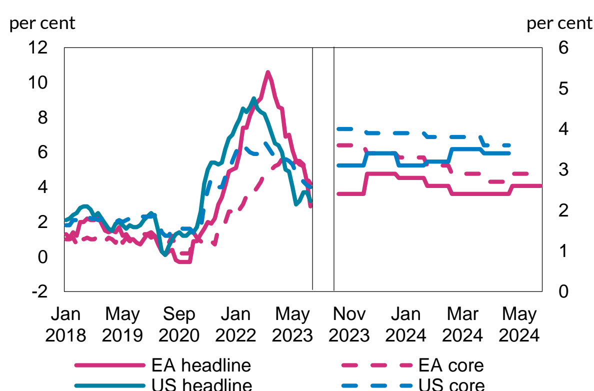
[1] The ECB has also warned that domestic price pressures remain strong as wage growth is elevated, noting inflation is likely to stay above target well into next year. See Christine Lagarde's speech for details.

of global trade links and generate more restrictions on trade and cross-border movements of capital, technology and workers. The number of restrictive trade policies globally has increased significantly between 2019 and 2023.[2] Amid an export-led growth strategy in China, there is a growing risk of further trade barriers from the rest of the world, particularly the US, as global economies struggle to absorb China's excess capacity.[3,4] As a small, open economy that relies heavily on exports, Ireland is particularly vulnerable to weakening global trade (see *Resilience: Non-financial corporations*).

Further geo-economic fragmentation will increase uncertainty, with financial stability implications. The continued fragmentation of the world economy into blocs could lead to higher macro-financial volatility. Reduced cross-border capital flows shrink international risk-sharing opportunities and increase the cost of funding for borrowers, including financial institutions. In this context, the record number of elections across the world in 2024 is likely to add to uncertainty around global economic policies and could weigh further on an already weak global trade outlook.

Chart 1: Inflation in the US and euro area is falling but remains vulnerable to upside surprises

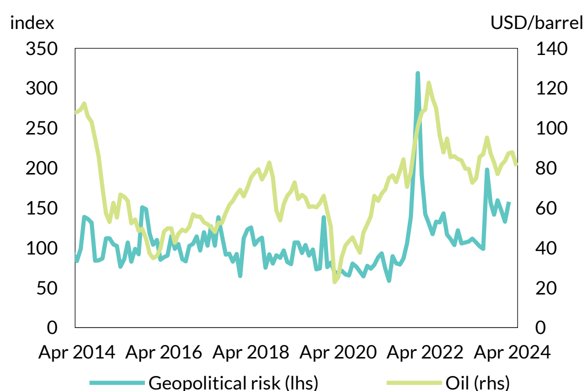
Euro area and US inflation



Source: Statistical Office of the European Communities and Bureau of Labor Statistics via Haver Analytics.
Notes: Left panel uses the left hand side axis and shows long term data up to October 2023. Right panel uses the right hand side axis and shows the last 6 months. Last observation is May 2024 for euro area and April 2024 for the US.

Chart 2: Recent geopolitical tension raise fears of increases in oil prices

Geopolitical risk index and Brent crude oil prices



Source: Bloomberg and Caldara, D. and Iacoviello, M. (2022).
Notes: The geopolitical risk index is a measure of adverse geopolitical events based on news articles covering geopolitical tensions. Last observation for geopolitical risk is 1st April 2024. Last observation for Brent crude oil price is 24th May 2024.

Despite geopolitical tensions and restrictive monetary policy, the global macro-financial outlook has improved in recent months, driven by the US economy. Despite higher interest rates - necessary to tackle the sharp rise in inflation since 2021 - global economic activity has been surprisingly resilient (Chart 3). Global growth is forecast to maintain its momentum in 2024 and 2025, growing 3.2 per cent in each year, supported by the strength of the US economy, where 2024 growth forecasts have been upgraded significantly in recent months. However, growth has been notably subdued among European economies.[5]

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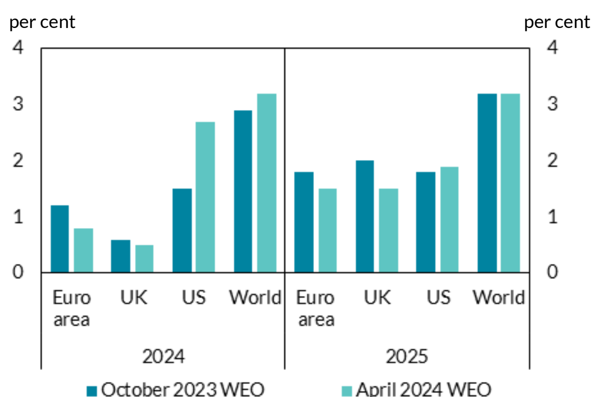
[2] For details, see ECB Financial Stability Review, May 2024.
[3] US President Biden recently called on US Trade Representatives to triple the existing tariffs on Chinese steel and aluminium due to China's overcapacity and China's non-market investments in the sector. For more, see the White House's statement.
[4] For details, see Institut Montaigne's 'Searching for Growth Engines Via Innovation'.
[5] See IMF World Economic Outlook, April 2024.

Continued uncertainty around the outlook for inflation and the required central bank response is increasing the risk of financial volatility. As a result of an upward tick in inflation in the US in March, market participants have lowered rate cut expectations for the US. The rate cut expectations for the euro area have also lowered (Chart 4). The volatility in forward curves reflects the very high levels of uncertainty in financial markets' assessment of the path of policy rates, which remain acutely sensitive to information from data releases, such as economic growth and inflation data, as well as communication by policymakers from the ECB and the Fed.

Chart 3: Economic growth has proven resilient, although there is a divergence in trends between the US and Europe

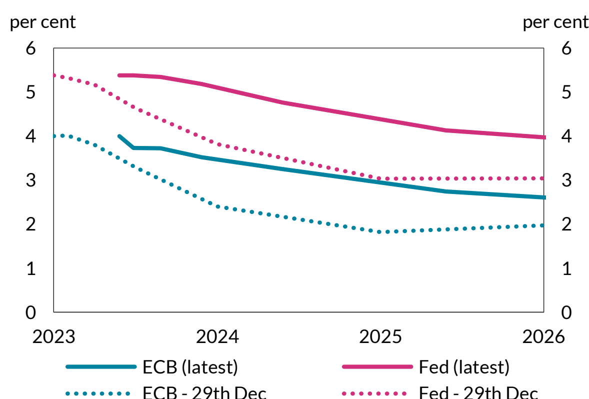
Evolution of global GDP growth outlook for 2024 and 2025



Source: IMF World Economic Outlook, October 2023 and April 2024.
Note: WEO refers to the IMF's World Economic Outlook. Last observation April 2024.

Chart 4: Interest rates are set to remain higher for longer than previously expected

Market implied policy rates for the ECB and Fed



Source: Bloomberg and Central Bank calculations.
Notes: The ECB rate refers to the deposit facility rate. Latest data show market expectations of policy rates as at 24th May 2024.

Public finances could also be strained by higher rates, limiting the fiscal space to respond to crises and posing risks to financial stability. Globally, government debt rose sharply during the pandemic, facilitated by low interest rates. For example, euro area sovereign debt is at around 90 per cent of GDP at 2023Q3, up from just above 80 per cent in the first quarter of 2021. Higher interest rates for longer will increase risks to fiscal sustainability in many countries. Decreased fiscal space may limit governments' abilities to combat future shocks.

Higher for longer interest rates could expose vulnerabilities in the global financial system. If interest rates stay higher for longer than markets are currently expecting, it could expose vulnerabilities among borrowers in the real economy. Significant volumes of corporate debt are due to be refinanced in the coming years at higher interest rates. Furthermore, many households have been sheltered from recent monetary policy tightening due to fixed-rate mortgages. However, in some countries, many such mortgages have short fixation periods, exposing them to sharp increases in borrowing costs when fixed rate periods expire.

Even if official rates decline, the lagged effect of higher inflation and interest rates could still expose built-up vulnerabilities. Households and businesses across the global economy will continue to be affected by higher interest rates, with new borrowing rates likely to be substantially higher than pre-2022 levels even as headline policy rates begin to ease (see *Resilience* for assessment of the capacity of Irish households and businesses to absorb the shock). According to the latest ECB's SAFE survey, euro area firms have seen a deterioration in profitability,

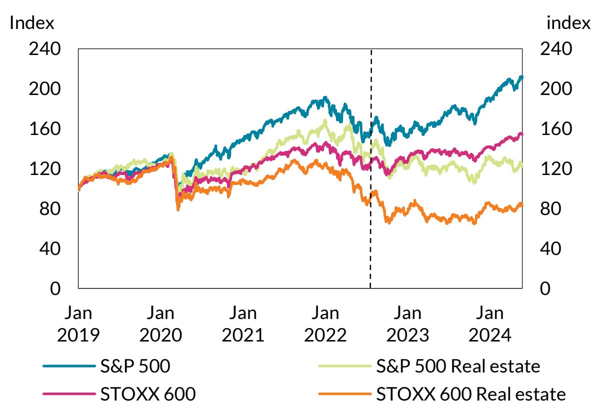
reflecting increases in labour and other costs relating to materials and energy, as well as increased interest expenses.[6] Weaker-than-expected growth and rising costs could erode corporate debt repayment capacity, which is of particular concern for highly indebted corporates that have to refinance their debt in the higher interest rate environment. Tighter financing conditions, in the euro area in particular, could weigh against investment and growth prospects.

Global CRE markets have been adjusting, as higher borrowing costs and weak demand trigger further price declines. Globally, CRE prices have declined sharply, driven by both higher global interest rates and post-pandemic structural changes to real estate demand (see the accompanying *FSR Special Feature* for a detailed assessment of the global CRE shock and its implications for Ireland). Sustained higher interest rates could pose further risks, driving yields from owning CRE towards or below the cost of financing CRE purchases with debt, resulting in further downward price pressure.[7] CRE borrowers are vulnerable and could face difficulties refinancing existing loans.[8] The shock has resulted in a strong negative drift in real estate firms' credit ratings, and a sharp fall in the valuations of European listed real estate companies, compared to the wider stock market (Chart 5).

Uncertainty remains over the ultimate impact of the CRE shock on certain global banks' balance sheets. While euro area banks have thus far experienced only contained losses on CRE exposures, banks globally have experienced asset quality deterioration on their CRE exposures, particularly among smaller regional US banks. Further deteriorations in prices, or the crystallisation of recent stresses through borrower defaults, could lead to greater investor uncertainty, with a particular focus on credit institutions with large exposures to CRE.[9]

Chart 5: Real estate equities have sharply under-performed since 2022

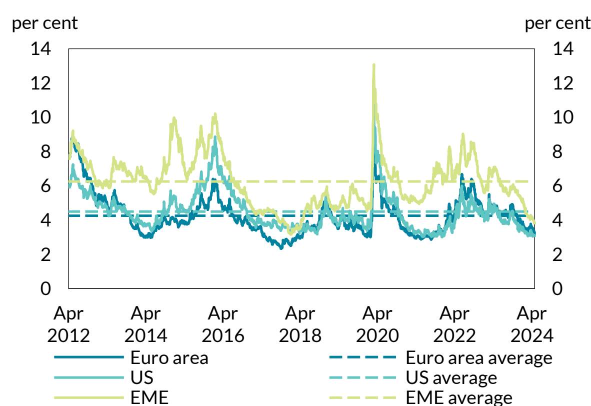
Valuation of stock market indices and real estate sub-categories in Europe and the US



Source: Bloomberg and Central Bank calculations.
Notes: Data indexed to January 2019. Broken line reflects 27th July 2022 when the ECB first raised interest rates. Last observation 24th May 2024.

Chart 6: Credit spreads are falling, exposing markets to risks from higher interest rates

High-yield corporate bond spreads



Source: ICE Data Indices via Federal Reserve Bank of St Louis.
Notes: ICE BofA Option-Adjusted Spreads on below investment grade corporate bonds. Dashed lines indicate historical averages since April 2012. Last observation 23rd May 2024.

[6] For more, see the latest ECB Survey on the Access to Finance of Enterprises.
[7] For more, see IMF Global Financial Stability Review, April 2024.
[8] In Europe, an estimated €110 billion of outstanding corporate bonds is due to mature up to 2026. For more, see ESMA Real estate markets – risk exposures in EU non-bank financial markets.
[9] Stock prices of some banks in Germany and the US declined sharply following the announcement of losses or provisions on their US CRE portfolios.

Equity market volatility and bond credit spreads may not be reflecting the extent of underlying risks whereas high volatility persists in interest rate markets. In recent months, volatility within equity and corporate debt markets has shown a further decrease, with credit spreads continuing to compress (Chart 6). Conversely, the interest rate markets continue to experience heightened levels of volatility, despite recent declines both in the US and the EU. These divergent trends point to the complexity of the current financial landscape. Interest rate markets remain sensitive to new information regarding the path for inflation, economic growth and monetary policy, and could be prone to swift repricing. While equities in general do not appear overvalued compared to historical standards, a question remains as to whether uncertainty has been priced appropriately given current prices, volatility, and risk premia (Chart 7).

In pockets of the non-bank financial intermediation (NBFI) sector, existing vulnerabilities could amplify market shocks. The global NBFI sector has grown rapidly since the GFC, largely driven by an increase in assets under management in the investment funds sector (Chart 8).[10] Liquidity mismatches, leverage and interconnectedness are key potential sources of vulnerability in non-bank financial intermediaries.[11] Shocks could be amplified by these existing vulnerabilities and cause disruptions and spillovers across markets. Such dynamics could potentially lead to broader financial stability concerns, which can come from unexpected sources at rapid speed, as evidenced by the gilt market turbulence of September 2022.[12]

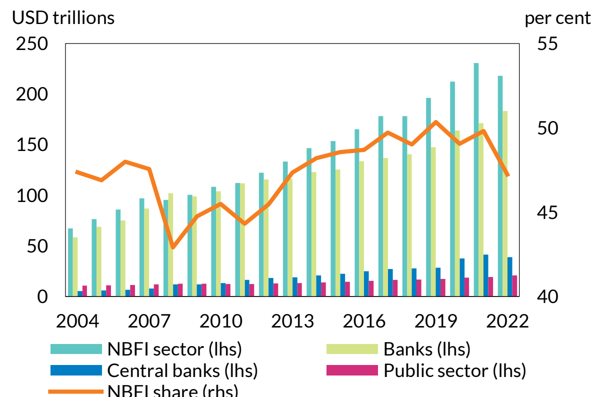
Chart 7: Risk premia are compressed in equity markets, raising the risk of reversals

Implied equity risk premium, S&P 500

Source: Aswath Damodaran, NY Stern.
Notes: Trailing 12 month cash yield implied equity risk premium for S&P 500. Last observation May 2024.

Chart 8: The size of the NBFI sector has increased significantly since the GFC

NBFI as a share of total global financial assets



Source: Financial Stability Board.
Notes: Methodological details available in the FSB's Global monitoring report on non-bank financial intermediation 2023. Last observation 2022.

[10] Investment funds as share of the financial system fell in 2022, but started recovering in the first half of 2023.
[11] Central Bank of Ireland Discussion Paper 11: An approach to macroprudential policy for investment funds provides more details on the materialisation of systemic risk arising from a shock, the interplay between leverage and liquidity mismatch, and the interconnectedness of the fund cohorts.
[12] The Central Bank has introduced macroprudential measures to Irish-authorised GBP-denominated liability driven investment (LDI) funds by codifying, and in certain cases augmenting, the yield buffer to safeguard the resilience of these funds such that they do not amplify stress in the gilt market as they did over September-October 2022.

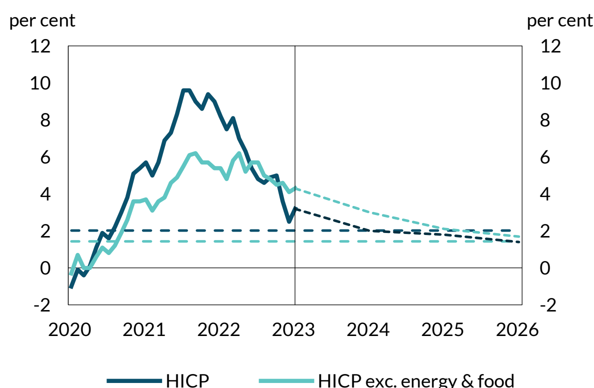
Domestic risk assessment

The domestic economy continues to grow at a moderate pace, and inflation has further declined and is expected to converge towards its long-run average in the coming years. Borrowers, credit flows, and asset prices appear to have broadly weathered the impact of the rapid rise in ECB interest rates since mid-2022, although risks remain from the ongoing refinancing of loans issued under lower interest rates. Reflecting developments in many global markets, the Irish CRE market is suffering from tighter financial conditions and a structural slump in the office market in particular. Geopolitical tensions are the most prominent source of potential further negative shocks for Ireland's open, FDI-reliant economy, in particular relating to the concentration of corporate tax receipts on a small number of MNEs.

The outlook for the domestic economy is broadly unchanged since the publication of the last *Review*. The domestic economy is expected to grow at a rate of 2.2 per cent in 2024 and by 2 per cent in each of 2025 and 2026. Unemployment remains at close to historically low levels, with the Central Bank forecasting unemployment rates to remain at about 4.5 per cent over the forecast horizon. While there are risks to the inflation outlook from capacity constraints, domestic inflation is expected to settle around its long-run average (Chart 9).

Chart 9: Inflation has continued to fall and is projected to settle close to its long-run average

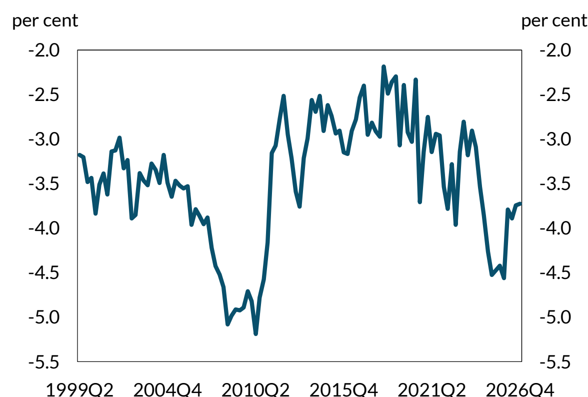
Actual and projected Irish inflation rate



Source: CSO and Central Bank calculations.
Note: Projected inflation rates are the Central Bank's latest forecast and are denoted by dashed lines. Dashed horizontal lines represent long-run averages.

Chart 10: Measured 'tail risk' for the Irish economy is neither subdued, nor elevated

GNI* growth rate at risk



Source: Central Bank of Ireland.
Notes: The T+12Q ahead output (GNI*) at risk. Risk is defined as the fifth percentile of the forecast distribution. For more on Growth at Risk see Box 3 from FSR 2020: 1.

Tail risks to the Irish economy remain in light of the geopolitical backdrop. Forward-looking estimates of tail risk in Irish economic growth point to a risk environment that is neither elevated nor subdued (Chart 10).[13] These estimates are based on a range of measures of the macro-financial environment. Nevertheless, the geopolitical backdrop (see *Risks: Global)* poses risks to this outlook. New shocks to energy prices could reverse the disinflationary process and undermine growth. A resurgence of inflation in such a scenario could also pose financial stability risks, as the debt service capacity of lower-income households and firms in energy-intensive sectors could come

[13] The reduction in risk primarily stems from a tapering off of the high level of GNI* growth volatility that accompanied the pandemic and post-pandemic period. In contrast, the credit cycle appears settled at historically benign levels.

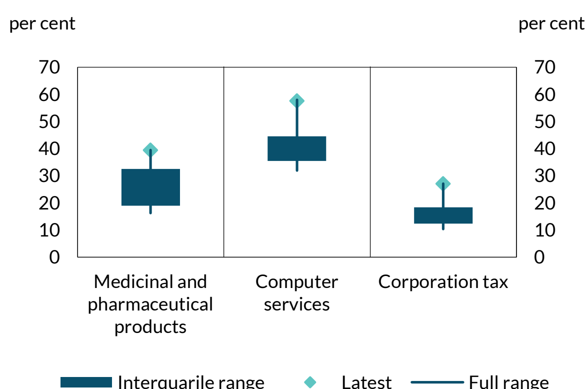
under strain if monetary policy rates remained higher for a prolonged period. Finally, the ongoing reliance of the Irish economy on fossil fuels leaves it vulnerable to transition risks related to climate change.[14]

As a small, open economy, Ireland is particularly exposed to developments in international trade and investment. Following a period of exceptional growth Irish exports contracted by 4.8 per cent in 2023 primarily driven by pharmaceuticals and contract manufacturing. The Central Bank currently forecasts that export growth will resume in 2024 bolstered by the recovery in the pharmaceutical sector, as well as continued growth in ICT services. However, increasingly restrictive international trade policies could impact this outlook (see *Risks: Global).*

Concentration of FDI in pharmaceutical and ICT firms increases the potential impact of unexpected sector-specific shocks (Chart 11).[15] While it has been an important source of revenue for the Irish State, corporation tax is particularly concentrated, with 10 firms accounting for more than half of all corporation tax receipts in 2022.[16] The potential for further geo-economic fragmentation poses particular risks to open, globalised economies such as Ireland. Though MNEs comprise a relatively small share of the number of firms operating in Ireland, they account for a disproportionately large share of employment and taxes (Chart 12) (For more see *Resilience: Sovereign*).

Chart 11: The Irish economy's pharma and ICT sector export shares remain at historically high levels

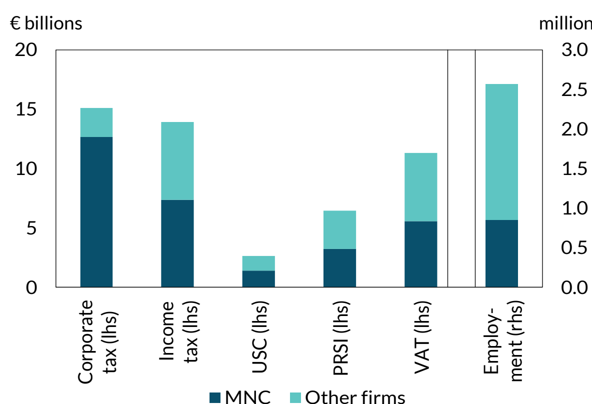
Percentage share of goods and service exports, and corporation tax receipts



Source: CSO, Revenue Commissioners and Central Bank calculations.
Notes: Left pane shows the share of total exported goods accounted for by medicinal and pharmaceutical products. Centre pane shows the share of total services exports accounted for by computer services. Right pane shows the share of taxation revenue generated from corporation tax receipts. Data are annual for the period 2003-2023 except for service exports where the last observation is 2022.

Chart 12: MNEs play an important role in the Irish economy, particularly for tax receipts

Contribution of MNEs to Ireland's economy



Source: Revenue Commissioners.
Notes: Central Bank calculations relating to data presented via Revenue Commissioners Corporation Tax analysis for 2022 (latest data available). Refer to Table 20 for more details.

Despite higher interest rates, the pace of credit growth has increased. The growth in outstanding credit owed to banks has increased from 0.8 per cent in September 2023 to 1.6 per cent in March 2024 (Chart 13). Loans to households, in particular mortgage credit, are the main contributors. In

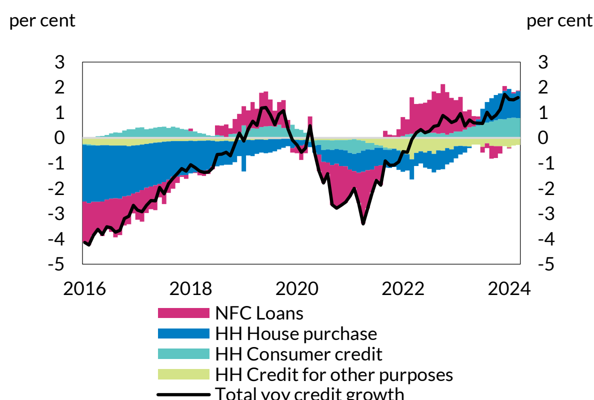
[14] See Department of the Environment, Climate and Communications (2023) "Energy Security in Ireland to 2030".
[15] For more on the outlook for these sectors see Central Bank Quarterly Bulletin, QB1/March 2024.
[16] Between 2019 and 2022 corporation tax receipts more than doubled.

contrast, credit to NFC has been broadly stable over the past year. Nevertheless, shorter-term trends suggest that lending to larger corporates is also starting to pick up. The latter may reflect both a lowering in interest rates for large firms and some increased demand across large enterprises.

Irish borrowers are likely to face higher interest rates over the medium term. Since the start of the monetary policy tightening cycle in mid-2022, Irish banks have not passed on the full increase in policy rates to borrowing rates (Chart 14). While the future path for official interest rates remains uncertain, the cost of financing for the private sector is likely to remain high when compared with the previous decade. The latest BLS survey also indicates that Irish banks expect to tighten lending standards on mortgage and SME lending in the short term. Overall, while lagged higher interest rates will continue to exert a drag on the domestic economy, their impact on aggregate household and business resilience remains moderate so far. Within that aggregate, though, some more vulnerable cohorts of borrowers have been more adversely affected (see *Resilience: Household* and *Resilience: Non-financial corporations*).

Chart 13: Credit growth has accelerated, primarily driven by households

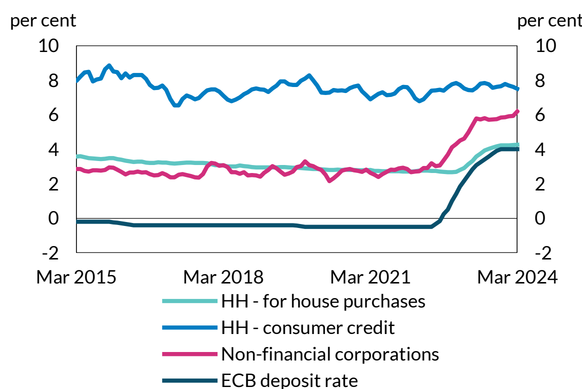
Contribution by loan type to annual growth of total credit



Source: Central Bank of Ireland Credit and Banking statistics.
Notes: Calculations based on data from Tables A.1 and A.6. As of January 2022 Table A.6 has been discontinued following an updated ECB regulation on the treatment of securitised loans. Credit considers only loans from banks to Irish residents. HH – households. Last observation March 2024.

Chart 14: Retail interest rates have increased by significantly less than key ECB rates

Interest rates on new lending by loan type



Source: Central Bank of Ireland Credit and Banking statistics and ECB.
Notes: The chart shows 3-month rolling averages. Last observation March 2024.

Capacity constraints remain in the domestic economy. If the downside risks outlined above did not materialise, capacity constrains in the economy could contribute to the emergence of overheating dynamics in the medium term. The labour market remains tight with unemployment remaining at historically low levels. Ambitious housing-related and capital infrastructure projects will test capacity constraints even further and could fuel wage demands in related sectors, threatening inflation targets. A loosening in financing conditions could also add to current pressures.

The domestic CRE market is in the midst of a sharp downturn, driven by structural and cyclical factors. CRE capital values have declined by over 25 per cent since 2019Q3.[17] The decrease has been driven by a combination of pandemic-induced structural shocks to demand, most acutely

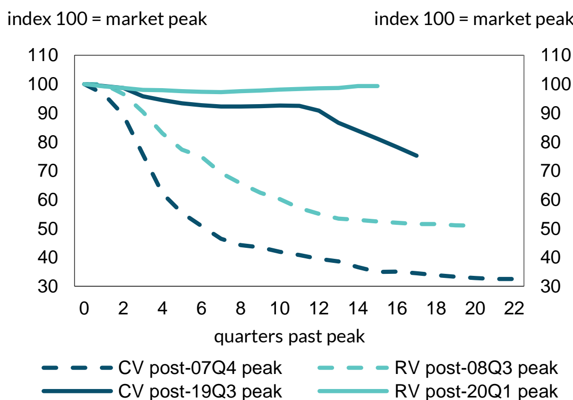
[17] According to the latest data from MSCI, year-on-year CRE prices have declined by 12.7 per cent in 2024Q1.

affecting the office and retail sectors, as well as the global monetary policy tightening since 2022. Investment expenditure on Irish commercial property, over 60 per cent of which came from foreign sources, declined sharply to around €2 billion in 2023, standing at 45 per cent of the annual average spend between 2014 and 2023. The trend has continued in the first quarter of the year with CRE investment almost 80 per cent below the ten-year average. While the scale of the decline in Irish CRE prices and investment activity since the pandemic has been significant, it has occurred in a relatively orderly manner to date, with substantially smaller falls than those experienced in the GFC period (Chart 15).

Headline commercial property rents have been broadly stable since the last *Review*.[18] A strong labour market and robust domestic economic growth combined with lengthy rental agreements, many of which pre-date the pandemic, have so far led to only gradual adjustment in market rents. Landlords have also in some cases increased inducements to tenants, rather than negotiate headline rents downward. As the volume of expiring leases increases over time however, and uncertainty surrounding the post-pandemic "steady state" demand for office space persists, further downward adjustments in CRE rents are possible.

Chart 15: Declines in CRE values have been large but remain well below the experience of the GFC

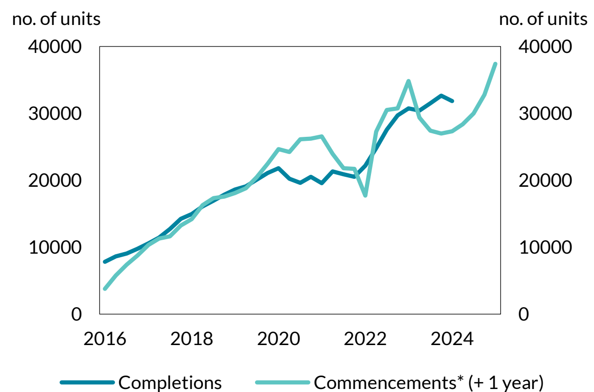
Irish commercial property capital value and rent indices in the aftermath of the 2007/08 and 2019/20 peaks



Source: MSCI and Central Bank calculations.
Notes: CV post-07Q4 peak = post-2007Q4 peak index of capital values, RV post-08Q3 peak = post-2008Q3 peak index of rental values, CV post-19Q3 peak = post-2019Q3 peak index of capital values, RV post-20Q1 peak = post-2020Q1 peak index of rental values.

Chart 16: Housing supply is expected to increase

Housing completions vs. (+ 1 year) commencements



Source: CSO, Department of Housing, Local Government & Heritage and Central Bank calculations.
Notes: Last observation 2024Q1.

The Central Bank's judgement is that the domestic banking system is sufficiently resilient to absorb – rather than amplify – this CRE downturn. Increased vacancy rates and an overhang of existing and new CRE supply coupled with reduced demand for office space post-pandemic could aggravate the ongoing CRE price and rent adjustments. Credit risks from CRE borrowers would directly have an impact on Irish lenders, while pro-cyclical disorderly falls in CRE prices could trigger forced sales by leveraged investors, undermining confidence, and having broader economic spill-overs. However, the Central Bank's assessment, published in the accompanying FSR Special Feature, is that the domestic banking system is sufficiently resilient to be able to absorb a

[18] According to MSCI, Irish commercial property rents grew 0.9 per cent annually in 2024Q1, and have been growing at a very similar level for the past 2 years.

commercial property shock. Banks' CRE exposures are a considerably smaller share of total lending compared to the pre-GFC period and banks have larger buffers of loss-absorbing capital. The *FSR Special Feature* also highlights the importance of new sources of global CRE funding, which have increased international risk-sharing thus diversifying risks to the core domestic financial system during this downturn.

Residential property prices are growing despite higher interest rates. Housing markets are critical for broader financial stability, given that mortgage-related lending represents the largest exposure of Irish banks while housing accounts for 70 per cent of household sector net wealth. Residential real estate price growth has accelerated in recent months, despite the impact of higher interest rates. According to CSO data, annual residential property price growth increased to 7.3 per cent in March 2024, the highest level in since December 2022, and well above recent expectations in market forecasts and various surveys from late-2023 and early-2024.[19]

There is mounting evidence of a build-up of momentum in housing supply. As well as an expansion in house building activity, the latest BNP Paribas PMI is reporting a fifth consecutive monthly increase in construction sector employment and high levels of optimism around output and activity amongst Ireland's building firms.[20] Meanwhile, residential completions reached 32,700 units last year while forward-looking indicators of housing output are pointing to the likelihood of further increases for this year (Chart 16). An easing in the overall cost of construction and building materials in early 2024, in addition to the recent extension of the Government's temporary waiver on development levies, is also likely to have a positive impact on housing output.[21, 22]

Residential transactions have been steady since the last *Review*, underpinned by the growth in new housing supply and the purchasing activity of non-household entities. Non-household buyers have been particularly active in the new homes market recently. While there has been no recent CSO breakdown of these figures between public and private entities, anecdotal evidence suggests that publicly-funded entities such as local authorities and approved housing bodies accounted for the majority of these purchases. Looser monetary policy globally would likely stimulate additional non-household investment from institutional investors, whilst also improving affordability for households, further bolstering residential housing demand. The positive outlook for disposable incomes, government fiscal supports of prospective FTBs, and favourable demographic trends are likely to also sustain high levels of housing demand from the household sector.

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[19] For instance in the 2023Q4 edition of the Central Bank of Ireland / SCSI Property Survey, the median expectation was for a 2 per cent increase in national house prices over 2024. Similarly, according to a Daft.ie survey contained in its 2024Q1 House Price Report, expectations for price growth over the next 12 months remain low at 1.1 per cent.
[20] See BNP Paribas Real Estate Ireland Construction PMI April 2024.
[21] The CSO's Wholesale Price Index (ex. VAT) for Building and Construction Materials fell 1.4 per cent year-on-year in April 2024.
[22] At the end of April, the Government approved an extension for the waiving of local authority "section 48" development contributions to the end of 2024, and the refunding of Uisce Éireann water and waste water connection charges to the beginning of October 2024.

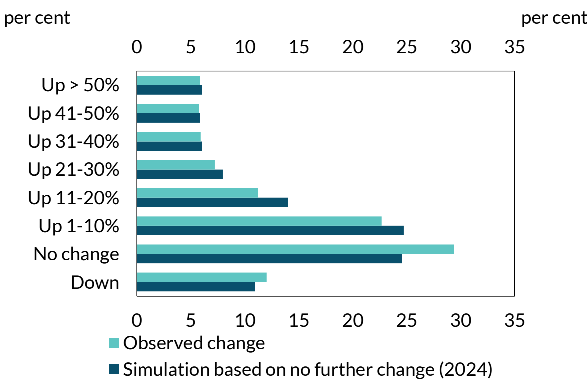
Resilience

Households

Households are, in aggregate, weathering the cost-of-living and interest rate shocks. The impact of monetary policy tightening has been manageable for most mortgage borrowers due to a high share of fixed-rate contracts and the incomplete pass-through of policy decisions to lending rates. Nonetheless, almost all bank mortgage borrowers will be exposed to interest rate repricing by 2028. A robust labour market and healthy balance sheets are key to the resilience of household finances to date. Measures of consumer loan performance remain strong and do not signal growing financial distress, while new flows into early mortgage arrears appear contained among borrowers that have experienced the largest increases in interest rates and those with a history of repayment difficulties, even among the most affected tracker-loan borrowers.

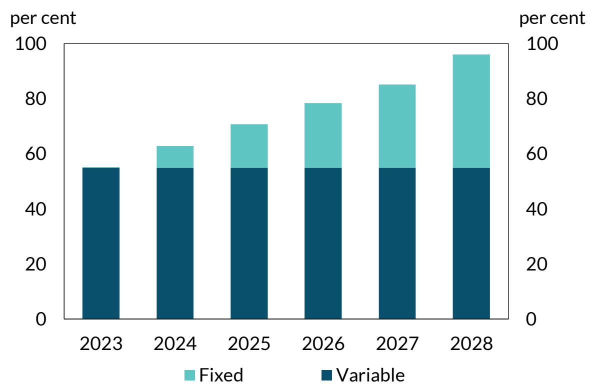
The impact of monetary policy tightening has been manageable thus far for most mortgage borrowers (Chart 17). 29 per cent of borrowers saw no change in their scheduled repayment between mid-2022 and December 2023. This is explained by the high share of borrowers with fixed rate contracts. A further 23 per cent of borrowers saw their repayment rise by less than 10 per cent in the same period, while 11 per cent saw an increase of between 10 and 20 per cent. A quarter of borrowers experienced increases above 20 per cent. 12 per cent of borrowers experienced decreases in their repayment amount, explained in part by switching activity in the early phase of monetary tightening (Scott and Singh, 2024). While the impact of higher interest rates on borrowers has clearly been uneven, repayment changes have been manageable for most borrowers. In a hypothetical scenario under which retail mortgage rates remain unchanged in 2024, repayment increases for borrowers with expiring fixed rate contracts are mostly below 20 per cent.

Chart 17: The impact of monetary policy tightening has been manageable for most mortgage borrowers
The distribution of mortgage repayment changes between June 2022 and December 2023



Source: Central Bank of Ireland and Central Credit Register.
Notes: The share of household mortgage borrowers by repayment change in the period June 2022 to December 2023 and a simulation of outcomes in 2024 if retail interest rates were to remain unchanged.

Chart 18: Almost all bank mortgage borrowers will be exposed to interest rate repricing by 2028
The share of bank residential mortgage loans that will be exposed to interest rate repricing by year



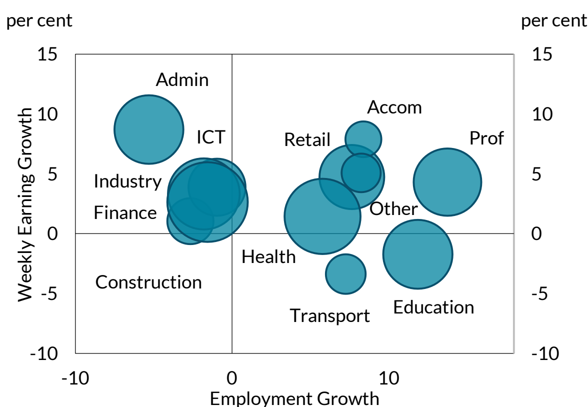
Source: Central Bank of Ireland.
Note: Shares are reported as a percentage of all outstanding loans at the five retail banks at end-December 2022.

Almost all mortgage borrowers will be exposed to interest rate repricing by 2028, but this is unlikely to have a significant impact on monthly repayments (Chart 18). The ECB began raising interest rates in July 2022 and mortgage holders on a variable rate or a tracker rate (45 per cent of loans at end-2022) were exposed to higher interest rates in subsequent months. Those on fixed rates are gradually being exposed to higher payments over time, and by the end of 2028, almost all borrowers are scheduled to roll off their existing fixed rate. With inflationary pressures easing across European countries, financial markets are widely expecting a fall in interest rates. But even if retail interest rates do not decline in 2024, the impact on monthly repayments of borrowers will be contained and the proportion who pay significantly more will not change materially.

Labour markets have been performing strongly and have provided the first line of defence for borrowers' resilience (Chart 19). Since the start of monetary tightening in 2022, the Irish labour market has performed robustly (see *Risks: Domestic*), with incomes also supported by fiscal support to cushion the impact of rising energy costs. Although there was a small decline in employment across some mortgage-concentrated sectors like ICT and Admin, these still maintained robust income growth. Similarly, while Transportation and Education experienced moderate declines in income growth, employment in these sectors grew strongly. Looking ahead, the labour market is likely to remain relatively tight, supporting employment and earnings growth, albeit at a slowing rate (Quarterly Bulletin, 2024 Q1).

Chart 19: Employment and income growth continue to support mortgage borrower resilience

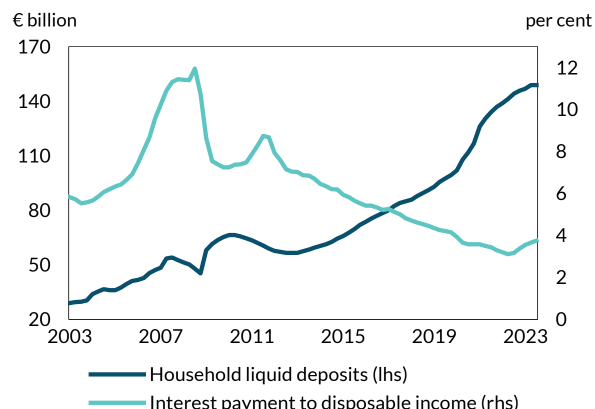
Mortgage book exposure, earnings growth, and total employment growth between 2022Q4 and 2023Q4



Source: CSO, Labour Force Survey and Household Finance and Consumption Survey.
Notes: Bubble size represents the share of mortgage loans for each sector where borrower's income is earned. The share is constructed based on Household Finance and Consumption Survey in 2020.

Chart 20: Household balance sheets have been repaired since the GFC and can weather future shocks

Household sector interest payment to disposable income ratio and liquid savings stock



Source: Central Bank of Ireland and CSO.
Notes: Household liquid deposits are the sum of overnight deposits and redeemable at notice. Interest rate calculated as a weighted average of interest rates on all household debt types. Last observation 2023Q4.

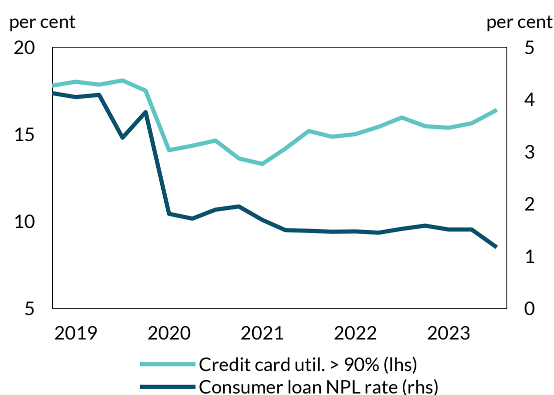
Households' balance sheets are healthy in aggregate (Chart 20). The Irish household sector has been deleveraging since the GFC, and since 2012 interest payments have declined steadily relative to incomes. The increase in the ratio from higher interest rates since 2022 has been reduced by strong income growth. Besides a reduction in debt, household liquid savings have been growing strongly. Savings growth, which accelerated during the pandemic due to public health measures imposed by the government, has moderated recently. The accumulated liquid saving stock

provides borrowers with a cushion against changes in interest payments, even if it is unevenly distributed across households.

Consumer loan performance remains strong (Chart 21). Households' income and accumulated savings have broadly been sufficient to dampen the impact of the cost of living shock so far, with little change in the share of non-performance among consumer loans or in the share of mortgage borrowers with high credit card utilisation rates. As of December 2023, the share of borrowers with credit card utilisation rates above 90 per cent, a leading indicator of financial distress, had not increased.[23] This share reduced during the pandemic in 2020, due to restricted spending opportunities, and has returned to just below the pre-pandemic level at around 16 per cent. Similarly, the share of non-performing consumer credit loan balances remains below 2 per cent, despite the increase in the cost of living and debt-servicing burden (Gaffney and Lyons, 2024).

Chart 21: Consumer loan performance remains strong

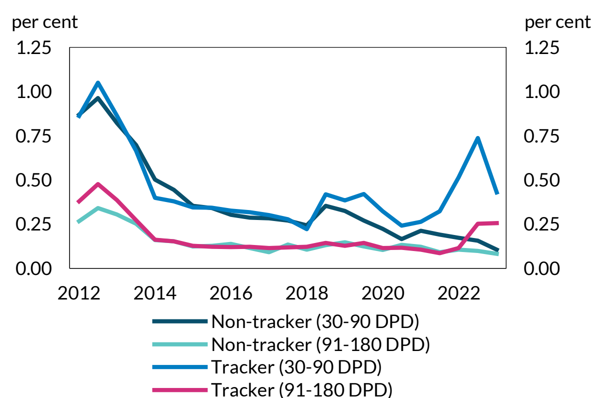
NPL rate in consumer loans and share of mortgage borrowers with a credit card utilisation beyond 90 per cent



Source: Central Bank of Ireland and Central Credit Register.
Notes: Credit card utilisation is based on data from all CCR lenders and it is the ratio of outstanding balance to credit limit, adjusting for the impact of annual stamp duty charges. NPL rate is the share of domestic bank outstanding consumer credit balances that are non-performing.

Chart 22: Tracker rate loans account for the rise in new mortgage arrears cases among bank borrowers

Share of domestic bank mortgage loans entering arrears by interest rate type



Source: Central Bank of Ireland.
Notes: The share of domestic bank Irish primary dwelling house mortgage loans moving from zero days past due to 30-90 days past due and from zero days past due to 91-180 days past due in the following six months, by interest rate type.

The impact of higher interest rates on mortgage arrears appears broadly contained. The share of mortgage loan accounts in arrears of over 90 days was stable in 2023 at 4.1 per cent.[24] Pockets of vulnerability are evident, however, particularly for borrowers that have experienced relatively large increases in their interest rates and those with a history of repayment difficulties (Shaikh et al., 2023). Tracker rate loans account for the rise in new mortgage arrears cases among bank borrowers (Chart 22). 0.26 per cent of domestic bank tracker loans entered arrears of greater than 90 days in 2023, a similar rate to that observed in 2022. Among non-tracker loans, the same transition rate was flat at 0.1 per cent. Some uncertainty remains, given that higher interest rates may only affect arrears with a lag, due to households first utilising liquid assets to meet repayments before eventually entering arrears and default.

[23] Stavins (2023) shows that credit utilisation is high among delinquent accounts, particular for low income households.
[24] See the Central Bank of Ireland's Mortgage Arrears statistics.

Non-financial corporations

Trading conditions for Irish businesses have remained robust since the onset of higher inflation and the tightening of monetary policy. Despite input cost and interest rate headwinds, SME profit margins were broadly stable in 2023. SMEs are mostly insulated from direct debt service shocks, either because they have no financial debts, fixed rate loans, or moderate leverage ratios. One cohort that are more exposed are export-orientated SMEs, who are more likely to have financial debts and whose leverage generally rises with export intensity. Leverage is high for some large corporates, though finance costs are generally modest relative to current operating profits. CRE borrowers are showing more acute signs of financial vulnerability than other NFCs. Insolvencies continue to rise from a low base, driven mainly by firms in the Accommodation & Food and Other Services sectors.

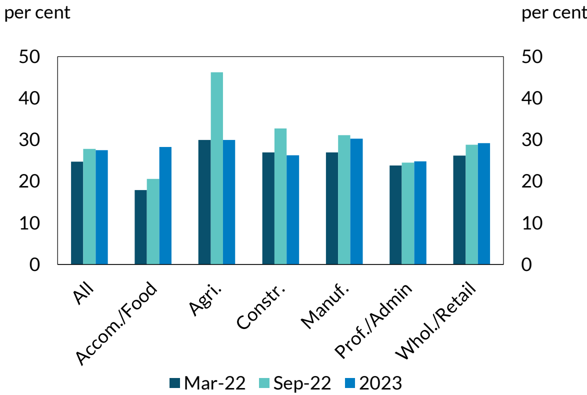
Trading conditions of Irish businesses have remained robust since the onset of higher inflation and the tightening of monetary policy. Retail sales volumes remained strong throughout 2023 and into the 2024 Q1.[25] Similarly, measures of household consumption pointed to continued growth throughout 2023 and the early months of 2024.[26] Further, the domestic economy is expected to experience modest growth in 2024, with unemployment projected to remain at low levels.[27]

SME profit margins remained stable in 2023 (Chart 23). This is despite input cost pressures – particularly wage growth – and the higher interest rate environment. The average gross profit margin across all firms was steady relative to 2022 at approximately 27 per cent. Accommodation & Food firms continued their strong performance in the post-pandemic era, with an average margin of 28 per cent up from 18 per cent in the six months to March 2022. The average margin for Construction firms declined somewhat from 33 per cent in the six months to September 2022 to 26 per cent in the full-year 2023. The share of SMEs reporting losses was also stable in 2023, with nine per cent of SMEs reporting a negative profit margin.

Many SMEs are insulated from direct debt servicing shocks, either because they have no debts or they have moderate leverage ratios, but export-oriented firms tend to be more leveraged (Chart 24). Approximately half of SMEs have no financial debts and, among indebted firms, the average leverage ratio is 0.46. Overall, 15 per cent of indebted firms have leverage ratios in excess of 0.8. Export-orientated firms are more indebted, which may reflect their investment needs and growth prospects, and are more exposed to developments in the global economy (see *Risks: Global*). They are more likely to have debts, have higher leverage ratios on average, and their propensity to have debts as well as their average leverage ratios rise with export intensity. Among the quarter of exporters with the highest share of their turnover made up of exports, 75 per cent have financial debts and their average leverage ratio is 0.6.

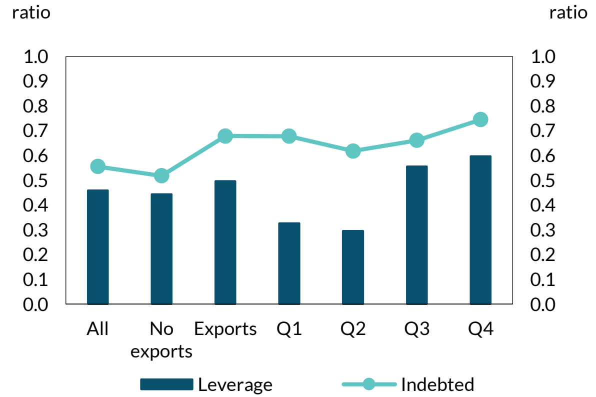
[25] See the CSO Retail Sales Index.
[26] See the Central Bank of Ireland's Card Payment Statistics.
[27] See the Central Bank of Ireland's 2024Q1 Quarterly Bulletin.

Chart 23: SME profit margins remained stable in 2023 despite sharp increases in costs
Average gross profit margin by sector and survey wave



Source: SME Credit Demand Survey.
Notes: The average gross profit margin of SMEs by sector. 'Mar-22' refers to the six months to March 2022, 'Sep-22' to the six months to September 2022, and '2023' to the full year 2023. Excludes financial & other business services and real estate activities sectors.

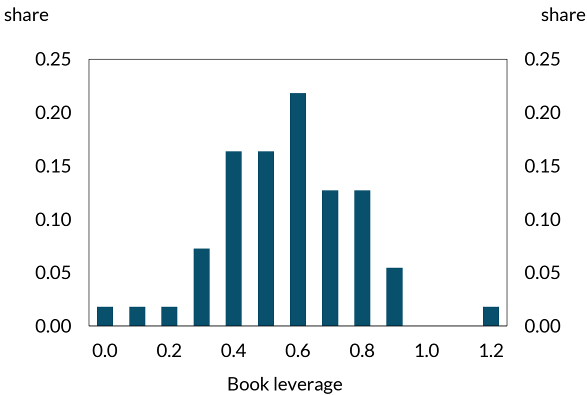
Chart 24: Half of SMEs have no financial debts, though export-orientated firms are more indebted
Share of SMEs with debt and average leverage of indebted SMEs by export status and export intensity



Source: SME Credit Demand Survey.
Notes: 'Indebted' refers to the share of firms with financial debts. 'Leverage' refers to the average leverage ratio (financial debts over assets) of indebted firms. 'q1' (or quartile 1) refers to the 25 per cent of exporting SMEs with the lowest ratio of exports over turnover, while 'q4' refers to the 25 per cent of exporters with the highest ratio of exports to turnover. Excludes financial & other business services and real estate activities sectors.

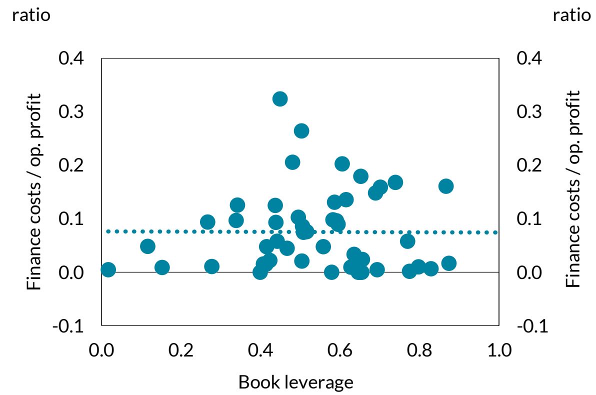
Leverage remains high for some large corporates (Chart 25). The median book leverage ratio was broadly stable between 2021 and 2023 among larger firms at 0.58, with assets values and liabilities growing at similar rates. However, approximately one-in-ten large corporates have book leverage ratios in excess of 0.8. These firms have limited capacity to absorb a shock to their asset values and their balance sheets may be tested in a macroeconomic downturn.

Chart 25: Leverage remains high for some large corporates
Book leverage for large corporates



Source: Companies Registration Office.
Notes: Book liabilities-to-assets ratio for large corporates.

Chart 26: Finance costs for large corporates are generally modest relative to operating profits
Leverage and debt service burdens of large corporates



Source: Companies Registration Office.
Note: Book liabilities-to-assets ratio versus net finance costs over annual operating profit. The dotted line refers to the average finance cost to operating profit ratio.

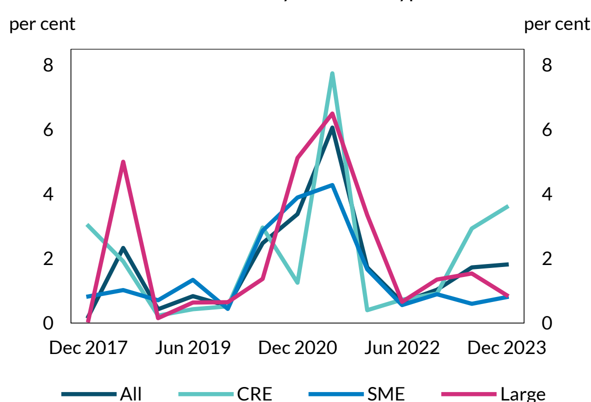
Finance costs for large corporates are generally modest relative to operating profits (Chart 26). Net finance costs were equivalent to 8 per cent of yearly operating profits on average in 2023 and this ratio was below 10 per cent for more than two thirds of firms. Even among high book leverage firms, finance costs are generally modest relative to current operating profits. The picture is a

more mixed when considering cash holdings, with finance costs exceeding cash holdings for approximately a third of high leverage firms.

CRE borrowers are showing more acute signs of financial vulnerability than other NFCs (Chart 27). CRE firms are particularly vulnerable given the nature of the shock being experienced globally and locally.[28] They have seen an increase in performing loans transitioning into forbearance at a rate larger than pre-pandemic norms. Similarly, between December 2022 and December 2023 there was a 2.1 percentage point increase in the transition rate into non-performing status – although the transition rate of performing CRE loans into arrears decreased in the last six months of 2023 (back to 2018 levels). This contrasts with both SMEs and large corporates, which have typically seen their financial distress metrics decrease and return to pre-pandemic norms (the only exception is the non-performing loan transition rate for SMEs, which has seen a modest increase). Overall, both SMEs and large corporates appear more resilient to the higher interest rate environment than CRE firms.

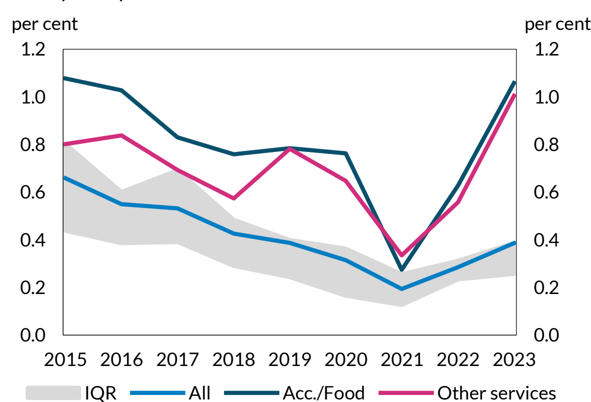
Insolvencies have risen significantly among Accommodation & Food and Other Services companies (Chart 28). Overall, each industrial sector has seen an uptick in insolvencies – albeit from historically low levels. For example, at 0.45per cent (and a 0.28 annual percentage point increase) the manufacturing insolvency rate is still below its June 2018 value (and for the three years prior to that). While most sectors have seen a gradual rise in insolvencies, two notable exceptions are the Accommodation & Food and Other Services[29] sectors – both of which have seen sharp increases back to their 2015 insolvency levels, although these sectors have typically seen higher insolvency rates throughout the economic cycle.

Chart 27: CRE borrowers are showing more acute signs of financial vulnerability than other NFCs
Share of performing NFC bank loan balances becoming forborne in each six months by borrower type



Source: Central Bank of Ireland.
Notes: Share of performing Irish NFC loans by outstanding balance transitioning from no forbearance to forbearance by borrower cohort. The CRE cohort refers to borrowers in the construction or real estate sectors. The SME and Large Corporate cohorts exclude CRE borrowers.

Chart 28: Insolvencies have risen significantly among Accommodation & Food and Other Services firms
Share of active Irish companies entering insolvent liquidation each year by sector



Source: Companies Registration Office, CRIF Vision-Net and CSO.
Note: The share of active Irish companies entering insolvent liquidation each year by sector, 2015 to 2023. 'IQR' refers to the interquartile range of sectoral insolvency rates. Active public and private limited company counts by sector are sourced from the CSO's Business Demography statistical release.

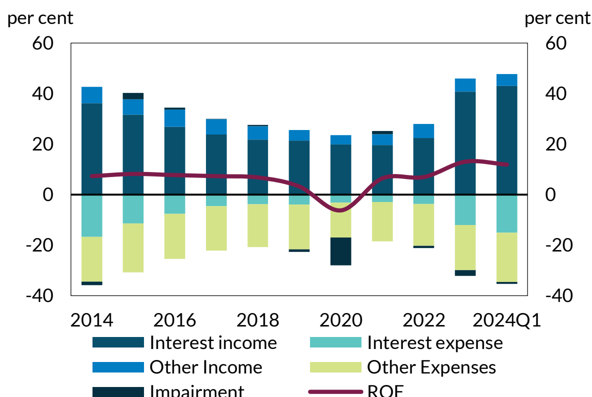
[28] See the FSR Special Feature for a detailed assessment. See also Shaikh (2024) and Lambert et al. (2024) for further detail on the CRE market in Ireland.
[29] Companies in the Other Services sector include a variety of service-orientated enterprises, including hairdressing, beauty treatment, and physical fitness facilities.

Domestic banks

Domestic bank profitability rose significantly in 2023, underpinned by strong net interest income growth. Net interest margins are expected to moderate in 2024 in the context of market expectations of interest rate decreases, higher deposit funding costs, and the potential materialisation of credit losses. Banks' overall asset quality remains robust, but is subject to risks from the ongoing impact of higher interest rates, particularly among CRE and SME borrowers. While down after a period of market consolidation, domestic bank capital ratios continue to provide loss absorbing capacity. The aggregate CET1 ratio for the sector stood at 15 per cent at end-2023, allowing for capital depletion under certain adverse scenarios such as those in recent EBA stress test exercises.

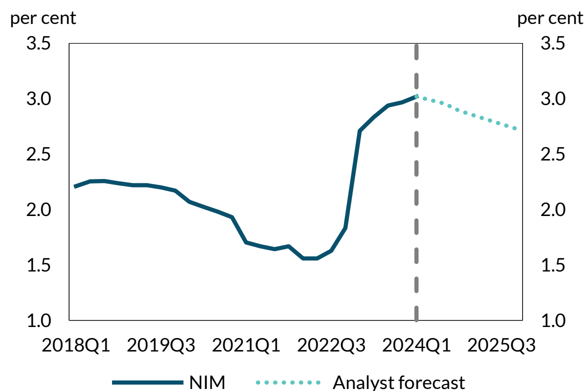
Domestic bank profitability rose significantly in 2023 (Chart 29). The aggregate return on equity (RoE) for the sector rose from 7 per cent in 2022 to 13.1 per cent in 2023. The main factor boosting profitability was a 63 per cent increase in net interest income associated with monetary policy tightening and the pass-through of higher interest rates to retail lending rates. RoE declined modestly to 12 per cent in 2024Q1, in part due to rising interest expense.

Chart 29: Domestic bank profitability rose significantly in 2023
Domestic bank RoE and RoE decomposition



Source: Central Bank of Ireland.
Notes: Domestic bank return on equity (RoE) and the percentage contribution of its components. 'NFCI' refers to Net Fee and Commission Income.

Chart 30: Net interest margins are expected to moderate
Aggregate net interest margin and analyst projections



Source: Bloomberg and Central Bank of Ireland.
Notes: Net interest margin of the three main domestic banks. 'Analyst Forecast' refers to Bloomberg Professional Forecasters series.

Net interest margins are expected to moderate in 2024 (Chart 30). Market expectations of interest rate decreases, rising deposit funding costs, a potential slowdown in loan growth, and weaker asset quality may all contribute to lower levels of profitability. Analyst forecasts point to a peak in NIMs in 2024 and a gradual decline to 2.7 per cent by end-2025. However, there is downside risk associated with these projections. For example, a plausible rise in interest rate pass-through on deposits or the materialisation of greater than expected credit losses have the potential to weigh further on NIMs going forward.

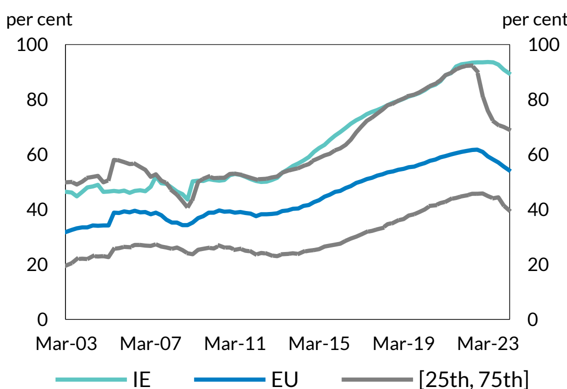
Irish households have been slow to move their savings to higher yielding term deposit accounts (Chart 31). The share of household bank deposits in Ireland held in overnight accounts is unusually high relative to other EU countries and relative to historical experience in Ireland. 90 per cent of

deposits were held in overnight accounts in March 2024, down modestly from 94 per cent in June 2023. The equivalent share for EU household deposits fell more markedly, declining from 62 per cent in June 2022 to 54 per cent in March 2024. The range across EU countries also tightened significantly, with half of countries having an overnight share between 40 and 69 per cent in March 2024.

Deposit funding costs could rise significantly if a greater share of households in Ireland shifted their savings to term deposit accounts. Irish banks have passed through some of the rise in interest rates to term deposit rates, with the weighted-average interest rate paid by banks on new term deposits from households in Ireland was 2.51 per cent in March 2024. The equivalent rate for EU household term deposits was 3.16 per cent, demonstrating a greater level of pass-through than in Ireland (Byrne and Foster, 2023). A large movement of households from overnight to term deposit accounts has the potential to push up bank funding costs significantly.

Chart 31: Irish households have been slow to move to higher yielding term deposit accounts

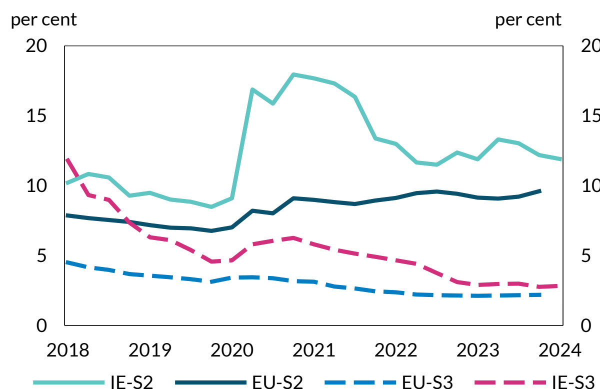
Overnight share of household deposits



Source: ECB.
Note: The share of overnight deposits is calculated by dividing the volume of overnight deposits by the sum of overnight, term and notice deposits. [25th, 75th] represents the 25th and 75th percentile shares respectively of a select number of countries where data is available for all time periods.

Chart 32: Credit risk has increased since origination for a sizeable share of loan exposures

IFRS 9 Stage 2 and Stage 3 ratios of domestic Irish and EU banks



Source: Central Bank of Ireland and EBA.
Notes: IE (EU)-S2 is the ratio of IFRS 9 Stage 2 exposures to all loans and advances subject to impairment and IE (EU)–S3 is the ratio of IFRS Stage 3 exposures to all loans and advances subject to impairment. IE data is available up to Q1 2024 while EU data is available to Q4 2023.

Banks' asset quality positions are robust, but pockets of vulnerabilities remain (Chart 32). The IFRS 9 Stage 3 ratio, similar to the Non-Performing Loan (NPL) ratio, fell further in 2023 and was under 3 per cent at March 2024. The improvement is explained both by loan portfolio sales and the resilience to date of borrowers to the higher interest rate environment. Nonetheless, the IFRS9 Stage 2 ratio – the share of loan exposures that have experienced a significant increase in credit risk since origination – remains elevated. This is particularly the case for CRE and SME loans. While there is uncertainty around the adequacy of provision cover to future losses, particularly in an environment of falling property valuations, any under-provisioning would result in a negative shock to bank capital.

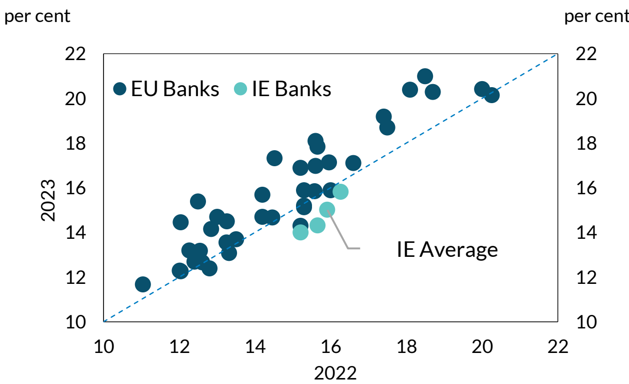
The exposure of banks to CRE lending represents a salient near-term risk for banks. CRE lending, at 11 per cent of total loans and advances of Irish banks represents a smaller proportion of their total lending than at the time of the GFC. There is also more diversification across CRE segments such as office, retail, industrial and residential. The accompanying *FSR Special Feature* provides a

detailed assessment of the resilience of domestic bank to the CRE shock. Although the assessment concludes that the banking sector is well positioned to absorb losses that might materialise via their CRE exposures, the potential for further CRE related distress - amid the post-pandemic structural changes in the demand for office in particular and higher refinancing costs - represents a salient near-term risk for banks that requires ongoing monitoring and management.

Domestic banks continue to have adequate capital headroom. The aggregate domestic bank fully loaded CET1 ratio stood at 15 per cent at end December 2023, compared with 15.9 per cent at end December 2022. This allows for loss absorbing capacity under certain adverse scenarios such as those from recent EBA stress tests.[30] The decline over the year is linked to recent market consolidation, whereby the remaining banks acquired portfolios from two exiting banks. The decline in the aggregate CET1 ratio stood in contrast to European peers where 83 per cent of banks increased their CET1 capital ratios in 2023 relative to 2022 (Chart 33). Following record profits in 2023, Irish banks, where permitted, announced increased distributions to shareholders in the form of cash dividends and share buybacks. In total, distributions amount to a combined €2.9 billion from after tax profits of €3.7 billion or a payout ratio of 77 per cent (Chart 34).

Chart 33: CET1 capital ratios across Europe have remained resilient in 2023, albeit Irish CET1 ratios declined.

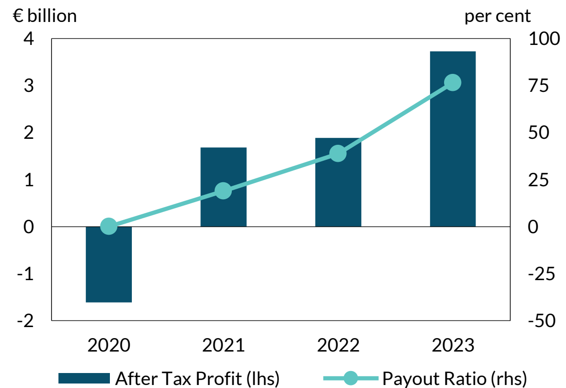
CET1 ratios of Irish and European banks in 2022 and 2023



Source: BankFocus and Central Bank of Ireland.
Notes: Fully-loaded CET1 ratios of Irish and EU banks at end-2022 and end-2023. The IE Banks data point with the "IE Average" label represents the weighted average CET1 ratios for the three IE banks.

Chart 34: Domestic banks are distributing most of their increased profits

Post-tax profits and payout ratio



Source: Banks' annual reports.
Notes: After-tax profit is the yearly sum of after-tax profits of the domestic banks. The payout ratio is the sum of all dividends and share buybacks in a given year divided by total after-tax profit.

[30] For Irish banks that took part in the last three EBA stress tests, their aggregate fully loaded CET1 ratio fell from an average starting point of 15.4 per cent to 9.9 per cent.

Non-bank financial sector

Investment funds and non-bank lenders

The resilience of domestically-orientated non-bank financial entities is being tested by tighter financial conditions and continued weakness in the CRE market. CRE price declines are likely pushing up leverage for certain Irish property funds, particularly those exposed to the office and retail sectors. Net inflows remained positive in 2022, particularly for residential funds and aggregate data indicate tentatively that flows into the sector continued in 2023. A new property funds data collection exercise is boosting transparency in the sector. Non-bank lending to Irish SMEs stabilised in 2023, following a decline in credit volumes and market share in 2022. Measures of borrower distress among non-bank lenders to SMEs remain modest.

Improved data collection indicates Irish property funds hold €29 billion of property assets either directly or indirectly, €4 billion higher than previous estimates. New data is allowing a more accurate estimate of the total market footprint of the sector, as well as leverage. This data (see Box 1) shows that on aggregate Irish property funds hold c. €22.5 billion in direct property holdings and €6.5 billion in indirect property holdings (such as investments in subsidiaries or related entities). This new data also allows for an improved measure of leverage. Combining Irish property funds direct and indirect holdings indicates that funds with holdings representing 42 per cent of total assets of Irish property funds had leverage exceeding 60 per cent (see *Policy: Non-banks* for discussion of the macroprudential measures in this area).[31]

Falling CRE prices are likely pushing up leverage among Irish property funds. Irish property funds investing in the office and retail sectors are likely to be most affected by the ongoing CRE downturn (see *Risks: Global*, *Risks: Domestic*, *FSR Special Feature*).[32] Assuming that their holdings' valuations move with the relevant underlying index, and no actions to pro-actively manage leverage are taken (e.g. additional equity injections etc.), leverage in the Irish property funds sector is projected to increase from 53 per cent in 2022 to 59 per cent in 2023.[33] The projected increase in leverage is particularly significant for funds primarily exposed to retail and office properties (Chart 35). Higher leverage can increase vulnerability to shocks and increase the likelihood that collectively these funds may amplify rather than absorb the shock.[34] This underpins the importance of managing leverage-related risks carefully, for example through additional equity injections from investors.[35]

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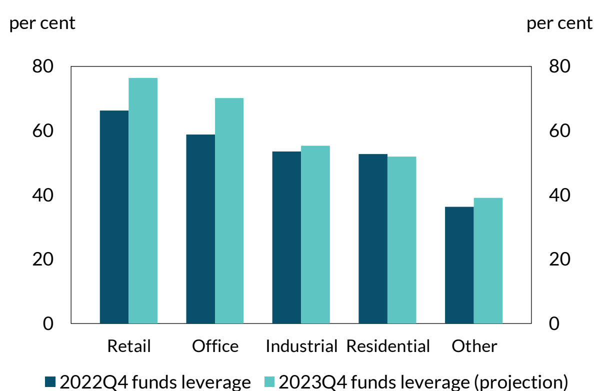
[31] Indirect holdings includes holdings not taken on directly by the funds but employed via their related or controlled entities.
[32] CSO RPPI rose 4 per cent in 2023. MSCI Ireland Quarterly Property Indexes indicate industrial properties valuations remained flat, while retail and office property values declined by 9 and 17 per cent, respectively.
[33] The projection of leverage is computed by applying the percentage change in market valuations in 2023 to 2022 funds' holdings data. Debt is assumed to remain constant at 2022 levels. Funds are categorised in Office, Retail, Industrial, Residential and Other based on the category in which they have more than 50 per cent of exposures. Other includes funds that have more than 50 per cent of exposures in Other assets and funds which don't have more than 50 per cent of exposures concentrated in a single category.
[34] See Daly et al. (2021) and Central Bank of Ireland Discussion Paper (2023).
[35] See the Central Bank's Macroprudential Measures for Property Funds.

Net investment inflows remained positive in 2022 and are higher for residential than for non-residential funds. Net inflows into residential property funds have increased in the last years, whereas for non-residential property funds net inflows have remained positive but have moderated since 2020 (Chart 36). More recent – albeit less complete – data on aggregate flows into the property fund sector suggest that net inflows remain positive in 2023. Market intelligence suggests that some of these flows may relate to additional equity injections by investors to manage leverage.

Chart 35: Falls in CRE markets in 2023 are projected to increase leverage in retail and office funds

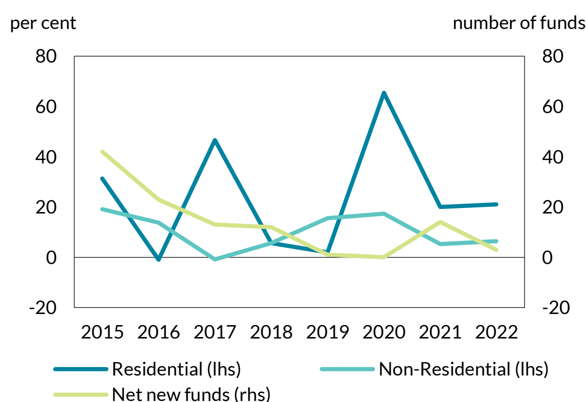
Leverage levels of Irish property funds by category of assets



Source: Irish Property Funds Return and Central Bank calculations.
Note: Leverage is calculated as total non-equity liabilities over total assets using consolidated reporting. Related parties leverage is leverage used by subsidiaries or related parties to the fund, such as limited partnerships. Funds are categorised in Office, Retail, Industrial, Residential and Other based on the category in which they have more than 50 per cent of exposures. Other includes funds that have more than 50 per cent of exposures in Other assets and funds which don't have more than 50 per cent of exposures concentrated in a single category. The projections reflect a revaluation of property assets consistent with the price movements of the MSCI Ireland Quarterly Property Indexes (Retail, Industrial, Office and Other) and of the CSO RPPI (Residential). Liabilities are assumed to stay constant. Last observation 2022Q4.

Chart 36: While moderating, net inflows remained positive up to the end of 2022

Growth in the number of new property funds and net inflows as percentage of NAV into Irish property funds by property type



Source: MMIF returns and Central Bank calculations.
Notes: The growth in the number of new property funds is calculated as the number of property funds in year t less the number of property funds in year t-1. Net inflows are calculated as total subscriptions less total redemptions as percentage of NAV. Property funds are defined as investment funds with at least 50 per cent of holdings invested in Irish property assets. Last observation 2022Q4.

Non-bank lending to SME borrowers has recovered from a decline in 2022, with lending to real estate SME borrowers reaching 50 per cent of total lending at Q3 2023. Non-bank lenders are loan-originating entities that are not banks, credit unions or government entities. To quantify non-bank lending, loan-by-loan data recorded in the Central Credit Register (CCR) is used to produce experimental statistics. [36] The share of new lending to SMEs by non-banks has stabilised at 34 per cent over 2023Q2 and Q3, following a decline in 2022 (Chart 37). Breaking the share of lending down by non-bank lender category (identified in Moloney et al., 2023), *Specialist Property Lenders* (SPLs) account for a large share of non-bank lending and their lending shows more variation than other lender categories. SPLs lend nearly exclusively to real estate companies, which means they are subject to greater concentration risk. The share of new lending to real estate SMEs by non-

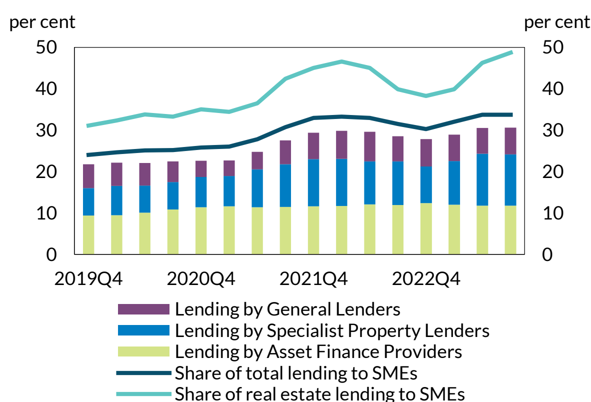
[36] Data on non-bank lending is an experimental statistical series as the Central Credit Register's (CCR) primary function is to serve as a credit register. As a consequence certain fields in the CCR are enriched with external data and with rules based on the data. This enrichment process can lead to changes in series if the external data change or if there are improvements in rules. Changes in the time series of the non-bank share of SME lending arise from delayed reporting by non-banks to the CCR and improvements in rules enriching the data. In recognition of delayed reporting, a 9-month lag is used when reporting new lending for non-banks.

banks has exceeded its pre-2022 level, reaching nearly 50 per cent in 2023Q3. This reflects above average nominal non-bank lending and below average nominal bank lending to real estate SMEs. The recovery of non-bank lending in 2023 suggests that financial institutions funding non-bank lenders still have appetite for exposure to non-bank lending, despite the higher interest rate environment increasing the risk of default and the cost of finance.

Indicators of distress for non-bank loans to SMEs are at a low level. The CCR includes two experimental indicators of whether a borrower is unable to repay their loan. The first indicates whether the conditions of a loan have been altered (e.g. term extension, interest only period, etc.) so that the borrower can continue to pay. The second indicates whether a loan is at an advanced stage of distress.[37] Both indicators appear to be at a low level – only 0.9 per cent of loans at the end 2023 were restructured, and 0.4 per cent had a status indicating they were in distress – although the absence of historical data for non-bank lenders hinders long-run comparison (Chart 38). While not directly comparable, these figures are still well below historical default rates for bank loans to SMEs observed in Ireland over periods of economic distress. This suggests that non-bank lenders are not seeing significant rates of repayment difficulties amongst borrowers (in line with bank borrowers and rates of corporate insolvency more generally – see *Resilience: Non-financial corporations*), which in turn may help explain why lending volumes have remained resilient.

Chart 37: The non-bank share of new SME lending has continued to stabilise in 2023

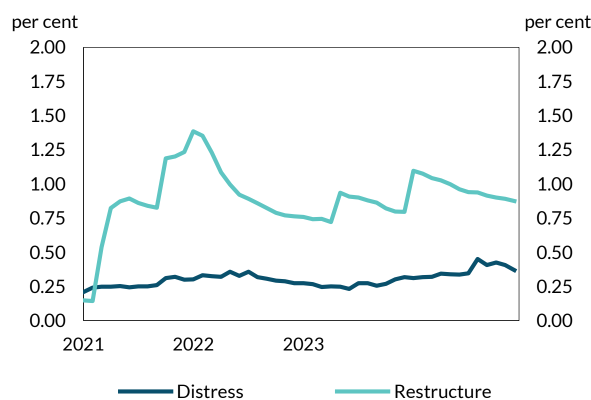
Share of lending to SMEs by non-banks, with breakdown by lender and borrower category



Source: CCR and Credit and Banking Statistics.
Notes: All series are four-quarter moving averages. The share of total lending to SMEs is the share of new loan agreements from non-bank lenders relative to the sum of gross non-bank loan agreements and bank gross new lending. Real estate SMEs include SMEs in real estate activity and construction. Lending by General Lenders, Specialist Property Lenders and Asset Finance Providers all refer to the share of total new lending to SMEs accounted for by each lender category. These are experimental series. Last observation 2023Q3.

Chart 38: Non-bank loans to SMEs show low rates of distress

Share of non-bank loans currently restructured or in distress



Source: CCR.
Notes: Series measure count of loans classified as distressed or restructured in a month as count of all non-bank loans in that month. Loans are counted as distressed if they have a contract status of 'write off', 'voluntary surrender', 'legal proceedings', 'settlement', 'irregular payment missed' or 'repossession'. These are experimental series. Latest observation 2023Q4.

[37] These include: voluntary surrender, repossession, settlement, legal proceedings, write-off, and irregular payment missed.

Box 1: New insights on Irish Property Funds

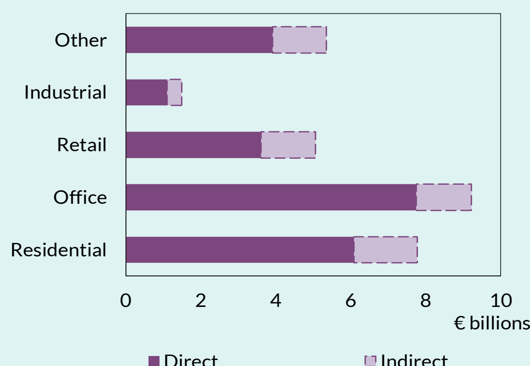
By Frederik Ledoux (International Finance Division)

In 2023, the Central Bank developed a new annual data return for Irish property funds to support the effective implementation of the macroprudential measures.[1] The measures – a leverage limit of 60 per cent and liquidity guidance to ensure a twelve month liquidity timeframe – were introduced as Irish property funds have become a key participant in the investable CRE market in Ireland, while also having excessive leverage and, to a lesser extent, liquidity mismatches. The return reduces existing data gaps and is used to assess the phased implementation of the macroprudential measures.

The new return fills important data gaps on indirect exposures to Irish CRE and the additional leverage that property funds can obtain through these exposures. Indirect exposures were outlined in the Central Bank's macroprudential policy framework for Irish property funds as a way for property funds to gain exposure to Irish CRE, in addition to their on-balance sheet holdings of property assets. Irish property funds can invest in other property funds or use subsidiaries or related parties, such as limited partnerships, to invest in Irish property. They are primarily invested in office and residential property, with a sizable share held indirectly (Chart A). Investment in Irish property is more concentrated in some CRE sub-sectors than previously estimated with different sources of data. The indirect exposures data also provide first insights on leverage that property funds employ indirectly through related parties, thus providing a more detailed picture of the risk to financial stability posed by excessive leverage.

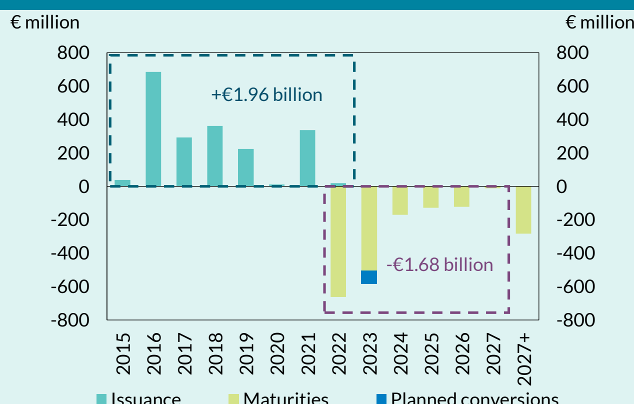
The conversion and maturity of shareholder loans will likely reduce the leverage of Irish property funds. Around 86 per cent of the shareholder loans outstanding as of end-2022 will either mature or be converted to equity by end 2027 (Chart B).[1] Industry engagement suggests the majority of the maturing shareholder loans are expected to be converted to equity. This would reduce leverage, improving Irish property fund resilience. Outstanding shareholder loans account for nearly €2 billion in debt, with most of this issued between 2016 and 2019.

Chart A: Indirect exposures make up a sizable portion of the total CRE exposure of Irish property funds



Source: Irish Property Funds Return.
Notes: Aggregated figures do not represent the sum of exposures of each fund, but take into account subsidiary investments of investments so as to not double-count assets. Observation is for end-2022.

Chart B: Shareholder loans are set to largely mature before the end of 2027



Source: Irish Property Funds Return.
Notes: Around 86 per cent of the outstanding shareholder loans as of end-2022 will either be converted to equity or mature before the end of the leverage limit's implementation period at the end of 2027.

[1] The term Irish property funds is used to describe funds in scope of the macroprudential measures announced in November 2022.

Insurance firms

The aggregate solvency position of the Irish insurance sector remains stable. Aggregate capital buffers are well in excess of regulatory requirements, with a slight reduction in the buffers for the life insurance sector offset by increases in the non-life and reinsurance sectors. The investment profile of the sector remains stable, with investments concentrated in relatively low risk asset classes. A high level of investment in bonds exposes the sector to widening credit spreads, however the potential impact is mitigated by the credit quality of the bonds held. Direct exposure to real estate investments is low. Inflationary factors driving non-life claims are being monitored, with the risk of pressures being reignited by geopolitical issues, while there may also be delays in the transmission of general economic inflation into insurance claim awards. Irish home insurance premiums are showing a disinflationary trend, while motor insurance premiums are increasing following a sustained period of reductions.

The aggregate solvency position of the Irish insurance sector remained stable and well in excess of regulatory requirements through 2023. High inflation and higher interest rates have not eroded the sector's capital buffer, with (re)insurers' aggregate solvency remaining at 187 per cent of regulatory requirements at 2023Q4, and the median solvency coverage ratio[38] at 194 per cent. Over 99 per cent of the sector's liabilities are held by (re)insurers with SCR coverage of 120 per cent or more. There was a reduction in the aggregate SCR coverage for the life insurance sector to 167 per cent in 2023Q4, partially due to the payment of dividends.

Insurers and reinsurers are exposed to market risk through their investment holdings, with individual firms' exposures depending on their investment mix. At an aggregate level, Irish insurers continue to hold a high proportion of their non-linked assets in relatively low-risk investment categories. Over 50 per cent of non-linked investments are held in fixed-interest securities, with an average credit rating broadly equating to a Standard & Poor's AA-/A+ rating at 2023Q4. Insurers are exposed to a widening of credit spreads which could negatively impact bond valuations without any offsetting reduction in liabilities. Such a deterioration in credit conditions could occur as the full impact of higher interest rates transmits to the real economy, though the relatively high quality of the bonds held reduces the likely impact.

The direct exposure of Irish insurers to real estate related investments is very low and a correction to CRE valuations would not pose a direct threat to Irish insurers' solvency. Property related investments[39] represent less than 3 per cent of the aggregate non-linked or unit-linked investments of the Irish insurance sector and even a significant write-down in valuations would not directly threaten the solvency of individual (re)insurers. A number of Irish insurers continue to apply deferral periods on withdrawals from property-related unit-linked funds[40] due to low levels

[38] Solvency coverage is measured as a firm's available capital (known as "own funds" under Solvency II) as a percentage of its Solvency Capital Requirement (SCR).
[39] Property related investments include directly owned property, investments in real estate funds, equity of real estate related corporations, mortgages, real estate based collateralised securities, and structured notes based on real estate risk. Analysis based on data submitted in Solvency II QRTs (template S.06.02) at 2023Q4.
[40] As at 2023Q4 the value of direct investments in Irish property by unit-linked funds was approximately €2.5 billion which was small in comparison to Irish investment funds. At 2022Q4 the investment by unit-linked funds in Irish property was equal to approximately 10 per cent of the total value of Irish property held by Irish investment funds.

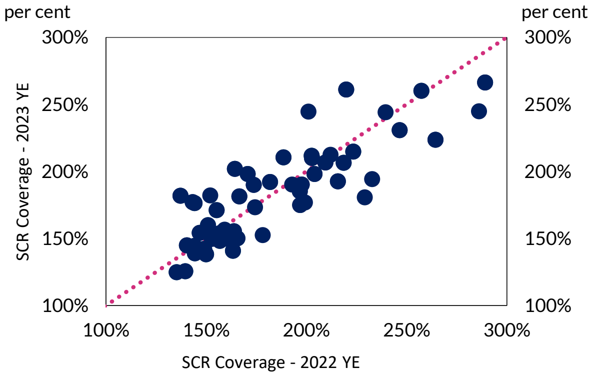
of liquidity in the funds. These restrictions allow for the orderly disposal of property assets to meet redemption requests.

The impact of higher inflation on non-life insurance claim costs is being monitored. While general economic inflation has reduced significantly, the reversion of inflation to target levels could be delayed particularly if further geopolitical risks materialise. Certain claim types have already been impacted by higher inflation, however the domestic non-life market has remained profitable. The full transmission of higher inflation into claim costs may take time due to delays in the processing of claims through the legal system and for compensation award guidelines to be updated.

The latest CSO data show the costs of home and motor insurance in the Irish market are both increasing broadly in line with general inflation. However, home insurance costs are showing a disinflationary trend, while motor insurance inflation is trending upwards. Home insurance inflation increased very significantly in 2022H2, but is now showing a disinflationary trend indicating a moderation in increases to sums insured and premium rates. Motor insurance costs decreased consistently between 2018 and mid-2023 due to reductions in claim costs[41] and competitive pressures in a profitable market. However, motor insurance rates have begun to increase and are trending upwards driven by the increased cost of motor damage repairs.

Chart 39: Solvency coverage movements over 2023 were widely dispersed

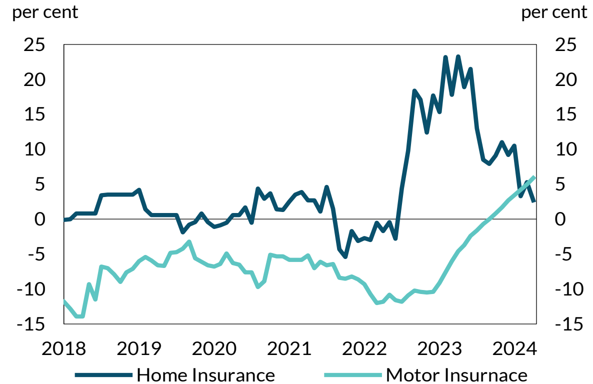
Plot of solvency coverage of insurers and reinsurers 2022YE and 2023YE



Source: Central Bank of Ireland.
Notes: The scatter chart shows the solvency coverage of individual firms at 2022YE (x-axis) versus their coverage at 2023YE (y-axis). A position below the diagonal line means a fall in coverage over the period. Only firms with PRISM impact rating of Medium Low and above are shown. Firms with SCR coverage of greater than 300 per cent are not shown.

Chart 40: Disinflationary trend in home insurance costs, while motor insurance inflation trending upwards

Plot of annual percentage change in consumer price sub-indices for home and motor insurance.



Source: CSO, CPI.
Note: The chart shows monthly data for the percentage change over the previous 12 months for selected CPI sub-indices.

Climate change continues to represent a significant risk for the insurance sector. The transition to a low carbon economy will impact the valuation of specific investments, change demand for insurance, and require (re)insurers to adjust business models. The increased frequency of severe weather events will impact the cost and availability of property insurance and reinsurance, with the potential for certain regions or events to become uninsurable. The level and sophistication of climate-related litigation is increasing which may lead to increased insurance liability claims for failing to manage climate risk, enabling greenwashing, or enabling carbon intensive industries.

[41] See the National Claims Information Database: Private Motor Insurance Report 5.

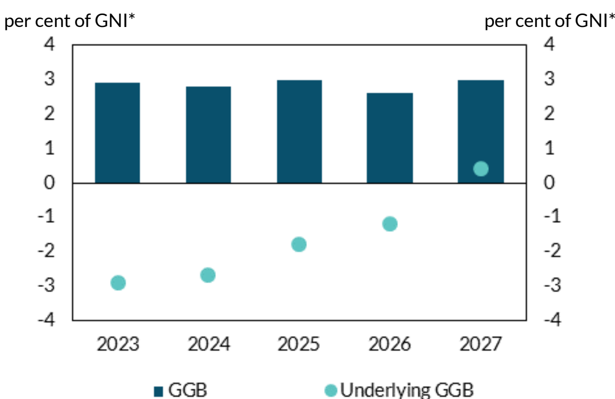
Sovereign

While the fiscal outlook remains favourable, the public finances face a number of risks and challenges. These include long-standing risks related to corporation tax receipts and persistent breaches of the national spending rule. Challenges include maintaining an appropriate fiscal stance when the economy is at full employment, ensuring the economy has the capacity to absorb the necessary investment in infrastructure to address the challenges of housing and climate change, and having sufficient resources available to meet future ageing costs.

The Government is running large fiscal surpluses due to excess corporation tax (CT) receipts. The Government's latest projections – published in the 2024 Stability Programme Update (SPU) - forecast a budget surplus of 2.8 per cent of GNI* in 2024, increasing to 3.0 per cent by 2027. When estimates of excess CT are excluded, however, the general government balance would remain in deficit until 2027, when a modest surplus is anticipated (Chart 41). Excess CT receipts cannot be explained by developments in the underlying economy and, as a result, could be subject to a sudden reversal. Public debt dynamics remain favourable, despite the upward trend in government borrowing costs that has occurred since end 2021. The Government has forecast that the public debt ratio will continue its downward trend in the coming years, falling to 66 per cent of GNI* in 2027 (Chart 42). This reflects large budgetary surpluses and, to a lesser extent, a favourable economic growth rate relative to interest.

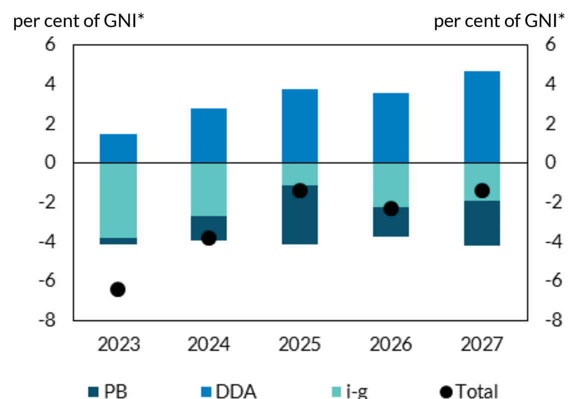
While baseline fiscal projections remain favourable the public finances face a number of challenges in the coming years. Aside from risks related to excess CT receipts, concerns remain about spending pressures over both the medium and longer term. Net core government spending is projected to exceed the national expenditure rule again in 2024, and the Government is no longer assuming a withdrawal of non-core spending in the SPU. In the longer term, ageing and climate costs will require significant resources. A key challenge for Government will be maintaining an appropriate fiscal stance while the economy is at full employment, particularly given the investment needed to address the challenges of housing and climate change.

Chart 41: Excluding 'excess' CT receipts the budget would remain in deficit until 2027
Government's GG balance forecast



Source: Stability Programme Update 2024.
Notes: Underlying GGB excludes estimates of excess CT.

Chart 42: Debt dynamics are expected to remain favourable in to the medium term
Factors driving change in Government's GG debt forecast



Source: Stability Programme Update 2024.
Note: PB = Primary Balance; i-g = Interest Growth Differential; DDA = Deficit Debt Adjustment; Total = total change in debt ratio.

Macroprudential policy

The Central Bank's macroprudential policies aim to promote resilience, proportionate to the risks faced by the financial system. The Central Bank undertakes regular monitoring and assessment of each of its macroprudential policies to ensure its policy stance remains appropriate for the prevailing systemic risk environment. This chapter presents an update on the Central Bank's current macroprudential policies (summarised in Table 1) across the three broad pillars of its macroprudential policy framework: macroprudential capital buffers for banks, the mortgage measures, and policies relating to non-banks, in particular investment funds.

Table 1 | Summary of macroprudential policies

	Instrument	Policy stance	Additional information
Macroprudential capital buffers for banks	• **O-SII buffer** – aims to safeguard resilience of systemically important institutions.	• 6 O-SIIs identified • Institution specific buffer rates range between 0.5% - 1.5%	• 5 O-SIIs have buffer rate already in place • 2023 review identified 1 new O-SII where buffer rate will apply from Jan 2025
	• **CCyB** – aims to safeguard resilience of the banking sector as a whole, with a view to facilitating a sustainable flow of credit to the economy through the financial cycle.	• 1.5%	
Mortgage measures	Aims to ensure sustainable lending standards in the mortgage market. • **LTV** - provides a buffer against the risk of house price falls, which could leave borrowers in negative equity. • **LTI** – provides a long-term link between developments in the housing market and the real economy.	• LTV: 90% for PDH loans, 70% for BTL loans • LTI: 3.5 times for SSB loans; 4 times for FTB lending • 15% of new FTB & SSB lending segment is allowed above the limits. 10% in the case of BTL lending	
Policies relating to non-banks	**Irish property funds** – aims to safeguard resilience of the sector, reducing the risk that financial vulnerabilities might amplify adverse shocks in future periods of stress. • **Leverage limit** • **Liquidity guidance**	• Leverage limit: 60% total debt to total assets ratio • Liquidity guidance: generally, property funds should provide for a liquidity timeframe of at least 12 months	• Applies to funds domiciled in Ireland, authorised under domestic legislation, and investing over 50% of their portfolio in either directly or indirectly held Irish property assets. • Measures have applied to newly authorised funds since Nov 2022. An implementation period is provided for funds authorised prior to this date whereby leverage limits become effective from November 2027 and liquidity guidance from May 2024.
	Irish authorised GBP-denominated LDI funds – aims to safeguard resilience of these funds to sudden increase in yields.	• 300 bps minimum yield buffer	• Measures have applied to newly authorised GBP LDI funds in Ireland since 29 April 2024. • Existing GBP LDI funds have a three-month implementation period from the announcement of the measures, i.e. until 29 July 2024.

Macroprudential capital buffers

Countercyclical capital buffer

The Central Bank is maintaining the CCyB rate at 1.5 per cent, judging the rate to remain appropriate given the prevailing macro-financial risk environment. Under the Central Bank's strategy for the CCyB, 1.5 per cent is the rate it expects to maintain when risk conditions are deemed to be neither elevated nor subdued. The 1.5 per cent CCyB rate on Irish exposures supports the resilience of the domestic banking sector by providing releasable capital (of over €1 billion) to support a sustainable flow of credit to the economy through the cycle. Future CCyB rate decisions will be based on macro-financial conditions in a manner consistent with the Central Bank's strategy for the CCyB.

The CCyB rate on Irish exposures is being maintained at 1.5 per cent. In line with its framework for the CCyB (Chart 43), the Central Bank considers that the 1.5 per cent rate remains appropriate given the prevailing macro-financial risk environment.[42] Based on its latest quarterly review, the Central Bank judges that cyclical conditions have not evolved in a manner that would warrant either an increase or decrease in the CCyB rate. Domestically, the economy has continued to perform solidly (see *Risks: Domestic*), while key financial factors such as residential real estate prices and household credit so far have proved robust to the increase in interest rates. At the same time, certain risks have been crystallising, most notably in the CRE market (see *FSR Special Feature* for an in-depth assessment). To date, the downturn has been orderly, and the increase in CRE-related provisions has been absorbed, with the banking system remaining profitable. In addition, as a small, open economy, Ireland is particularly exposed to developments in international trade and investment. Rising geopolitical tensions bring with them the possibility of further negative shocks (See *Risks: Global*). Balancing these considerations, the Central Bank is maintaining its existing CCyB policy stance.

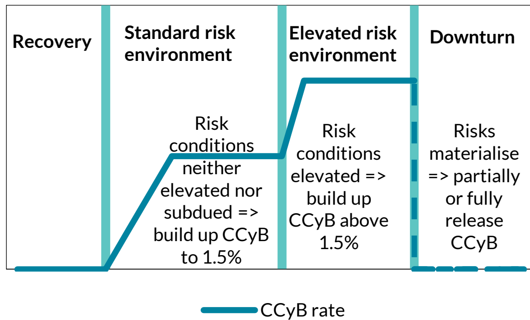
Future CCyB rate decisions will be based on macro-financial conditions in a manner consistent with the Central Bank's strategy for the instrument. The primary objective for the CCyB is to promote resilience in the banking sector – proportionate to the risk environment – with a view to facilitating a sustainable flow of credit to the economy through the macro-financial cycle. The 1.5 per cent CCyB rate on Irish exposures, which is the rate the Central Bank has outlined as being appropriate when risks are neither elevated nor subdued, is now in effect, having initially been announced in June 2023.[43] In aggregate, this provides approximately €1.3 billion in releasable capital across the domestic banks. Having the CCyB in place (Chart 44), supports the instrument's objective by providing scope for its release, should it be warranted due to the materialisation of cyclical systemic risk or where a downturn is identified, to support the banking system to absorb losses and maintain the supply of lending to the economy. The CCyB rate could be increased above 1.5 per cent if cyclical risks were deemed to have become, or risk becoming, elevated.

[42] See the Central Bank's Framework for Macroprudential Capital and the Central Bank's framework for macroprudential capital: CCyB addendum.

[43] The 1.5 per cent CCyB rate on Irish exposures became effective on 7 June 2024 having been announced a year previously. CCyB rate increases generally become applicable 12 months after they are announced.

Chart 43: The calibration of the CCyB at 1.5 per cent reflects the Central Bank's strategy for the buffer

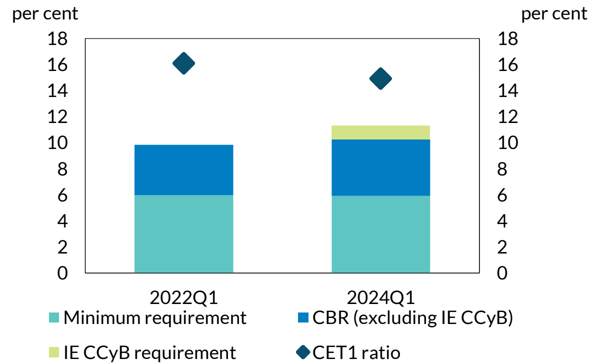
The Central Bank's high-level strategy for the CCyB



Source: A framework for macroprudential capital.
Note: Stylised representation, does not refer to specific figures.

Chart 44: The 1.5 per cent CCyB rate supports resilience, providing macroprudential space to respond to shocks with a buffer release if required

CET1 capital requirement and ratio of domestic banks – 2022 & 2024



Source: Central Bank of Ireland.
Note: Aggregate position of domestic banks. Minimum requirement includes Pillar 1 and Pillar 2 requirement. CBR stands for Combined Buffer Requirement and includes the capital conservation buffer, O-SII buffer and CCyB rates. In 2022Q1 the CCyB rate on Irish exposures was 0 per cent. 2024Q1 position reflects the impact of announced macroprudential capital buffer requirements.

Macroprudential mortgage measures

Mortgage measures

The mortgage measures are a permanent feature of the housing and mortgage markets and aim to ensure sustainable lending standards in the mortgage market. The first year of operation of the refreshed framework, following the 2022 review, broadly indicates that the measures are operating as intended. The recalibration of the headline limits sought to relieve some of the economic costs of the measures, without unduly reducing their benefits and aimed to reduce the importance of the proportionate allowances in overall credit allocation. FTB lending continued to grow in 2023, while lending was more subdued in other market segments. There has been a shift in the share of lending bunched at the previous limits towards the increased FTB LTI and SSB LTV limits. At the same time, the use of allowances above the limits has been reduced. Overall, the measures continue to guard against lending at very high levels of indebtedness.

The Central Bank considers the mortgage measures to be permanent in nature and their calibration to be largely driven by slower-moving forces.[44] The Central Bank is committed to undertaking monitoring, analysis, engagement and communication around the measures on an ongoing basis. Data on new mortgage lending for 2023, the first full year of the implementation of the refreshed framework, is now available – with initial insights on the operation of the framework provided below.[45] Alongside this continual monitoring, the Central Bank will undertake periodic reviews of the strategy around the measures.

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[44] For example, structural forces which play a role in determining, for example, the magnitude of risks to affordability or the sustainable level of house prices relative to incomes.
[45] Over the course of 2021/22, the Central Bank conducted a comprehensive review of the overall mortgage measures framework. The purpose of this overarching review was to ensure the measures remained fit for purpose, in light of changes to the financial system and economy since they were first introduced in 2015. The Central Bank has set out the conclusion of its review in its framework for the macroprudential mortgage measures.

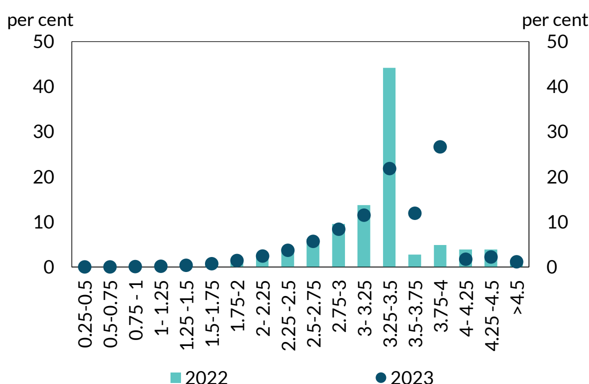
Insights on new mortgage lending in 2023

During 2023, the mortgage market has adjusted to the refreshed calibration of the mortgage measures broadly in line with previous expectations. The recalibration of the headline limits introduced in 2023 sought to relieve some of the economic costs of the measures, without unduly reducing their benefits. The recalibration also sought to reduce the importance of the proportionate allowances in overall credit allocation. In 2023, as had been expected at the time of the review, there was a shift in lending that was bunched at the previous limits towards the new limits. At the same time, the use of the proportionate allowances decreased.[46]

In the FTB market, lending has shifted towards the new LTI limit of 4x, whereas the LTV distribution has remained broadly unchanged. In 2023, 39 per cent of FTB lending had an LTI between 3.5 and 4, compared with 8 per cent in 2022 (Chart 45). On the other hand the share of lending close to the previous limit halved, from 44 per cent in 2022 to 22 per cent in 2023. Overall, the median FTB LTI remained broadly unchanged between 2022 and 2023, but, consistent with the increase in the headline limits, more loans are now originating at higher LTI multiples. Taking a longer time horizon, and pointing to the continued safeguarding role of the measures, the share of FTB loans being issued at higher LTIs is substantially below that seen during the mid-2000s (Chart 46). The distribution of lending in terms of FTB LTV, where no changes were made under the framework review, were broadly similar in 2023 and 2022.

Chart 45: Loans that would have clustered at the 3.5 LTI limit have originated closer to the new limit of 4

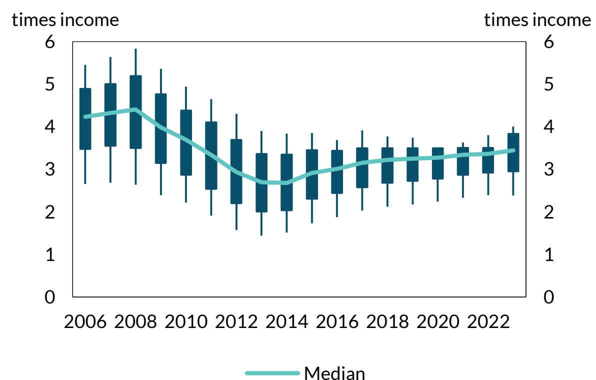
LTI distribution for FTBs in 2023 vs 2022



Source: Central Bank of Ireland Monitoring Templates Data.
Notes: Share of value. FTB in-scope new property purchase and self-build loans only.

Chart 46: FTB lending at higher LTI multiples remains well below pre-crisis levels, while the median is broadly stable relative to 2022

FTB LTI percentiles over time



Source: Central Bank of Ireland.
Note: Chart shows the distribution of LTI, based on the number of loans, across the 90th, 75th, 50th, 25th and 10th percentiles, respectively. Data for 2006-2014 are for all mortgage agreements originated by retail banks - excluding split mortgages. Data for subsequent years relates to loans in-scope of the mortgage measures captured through the Central Bank's Monitoring Templates Data. Last observation 2023.

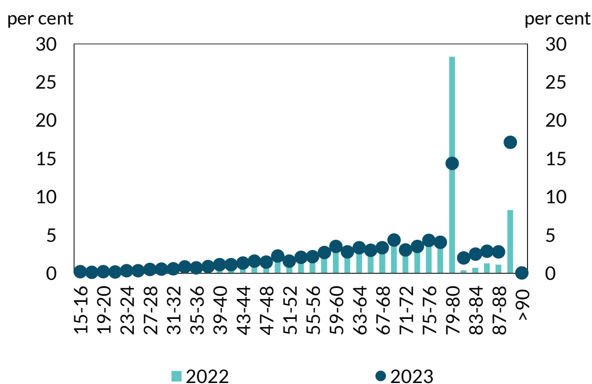
In the SSB market, the LTV distribution also shifted toward the new limit of 90 per cent in 2023, whereas the LTI distribution remained broadly unchanged. The share of SSB lending with an LTV of 89-90 per cent increased to 17 per cent in 2023 (Chart 47), reflecting the increase in the LTV

[46] The analysis in this section is based on loans originated by the five institutions that submitted mortgage measures monitoring template data to the Central Bank for 2023. For the purposes of monitoring the mortgage measures, any lender that originates €50 million or more in new lending in a given 6 month period (Jan-June; July-Dec) is required to submit corresponding loan level data to the Central Bank. A detailed overview of new lending under the mortgage measures is published twice yearly by the Central Bank on its website – See New Mortgage Lending Data.

limit from 80 per cent to 90 per cent. This has seen an increase in the 90th percentile LTV from 80 per cent to 90 per cent, albeit the distribution below this remained stable (e.g. the median SSB LTV was unchanged at 68 per cent).[47] The distribution of lending in terms of SSB LTI, where no changes were made under the framework review, were broadly similar in 2023 and 2022.

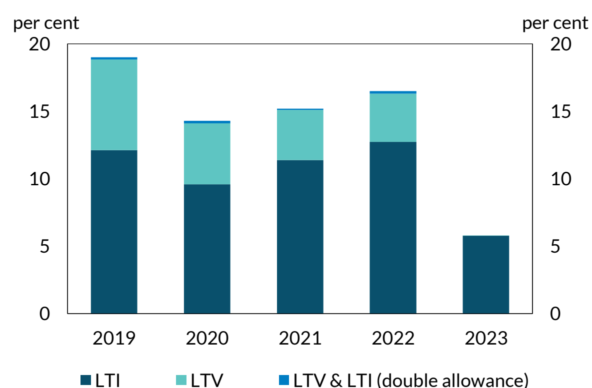
The share of lending with an allowance declined in 2023, and the distribution of FTB lending above the LTI limit shifted to lower levels of indebtedness. Overall, 6 per cent of total PDH in-scope lending, by value, had an allowance in 2023 (Chart 48). This represents a significant decline on the share of lending with an allowance under the previous framework, and is consistent with the Central Bank's aims when increasing the headline LTI and LTV limits. The profile of lending with allowances suggests a limited appetite among lenders to originate mortgages at very high multiples. The LTV and LTI applying to allowance loans are at the discretion of institutions, in line with their own lending standards and policies. In 2023, essentially no new mortgage lending took place at LTVs greater than 90 per cent – something which is reflective of mortgage lenders own risk appetite in this regard. In terms of LTI, approximately 5 per cent of FTB lending had an LTI in excess of 4. The corresponding share in 2022 was almost 10 per cent. The share of SSB lending above 3.5 LTI in 2023 was in line with that observed in 2022.

Chart 47: Higher shares of SSB lending originated at LTVs above 80 per cent in 2023, compared to 2022
LTV distribution for SSBs in 2023 vs 2022



Source: Central Bank of Ireland Monitoring Templates Data.
Notes: Share of value. SSB in-scope new property purchase and self-build loans only.

Chart 48: The use of allowances declined in 2023, consistent with expectations
Share of PDH in-scope lending with an allowance



Source: Central Bank of Ireland Monitoring Templates Data.
Note: Share of value. In-scope PDH loans only.

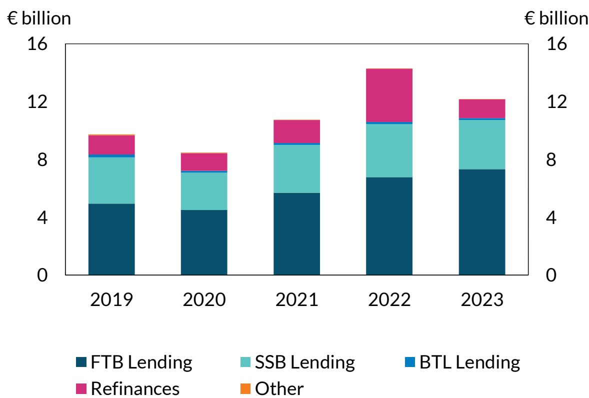
Taking a broader perspective on new mortgage lending in 2023, overall FTB lending remained strong while other segments saw a decline. Lending to FTBs increased by 8 per cent, from €6.8 billion in 2022 to €7.3 billion in 2023 (Chart 49). A total of €12.2 billion of new mortgage lending was originated during 2023 by institutions submitting monitoring templates data to the Central Bank, a 15 per cent decrease on the value of lending observed in 2022. This decrease in lending was largely driven by a decline in lending originated for a refinance, which does not relate to house purchases, and fell by 65 per cent compared with 2022.[48] Lending to SSBs and lending for a Buy-to-Let (BTL) also decreased.[49]

Average FTB loan sizes, property values and incomes continue to increase and the pass-through of interest rates in 2023 is also evident. For FTBs, average loan sizes and property values increased

[47] More detail on the distributions can be found in New Mortgage Lending Data for 2023.
[48] Refinances category includes loans both in and out of scope of the mortgage measures.
[49] These findings are consistent with data from the BPFI.

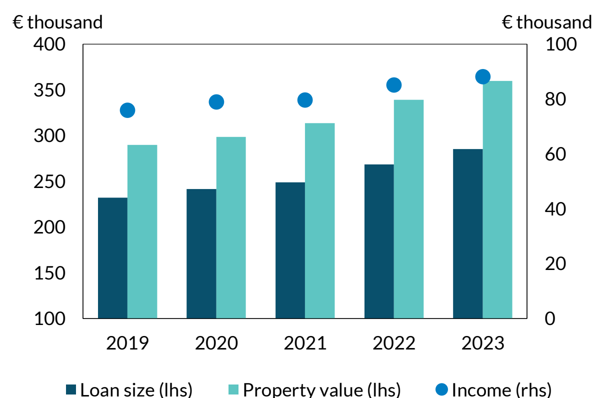
by 6 per cent and average incomes increased by 4 per cent compared with 2022 (Chart 50). This represents a continuation of the trend observed over the last number of years. Average interest rates on new lending for both borrower types increased from 2.6 per cent in 2022 to approximately 3.8 per cent in 2023. Fixed rate loans account for the majority of new loans in 2023 (see *Resilience: Households*) at 90 per cent for FTBs and 82 per cent for SSBs, a small decrease on the share of fixed loans observed in 2022 (94 per cent and 87 per cent respectively). The profile of borrowers originating new PDH lending is consistent with that observed in recent years.

Chart 49: While overall the mortgage market slowed down during 2023, FTB lending remained strong
Breakdown of new lending volumes by type



Source: Central Bank of Ireland Monitoring Templates Data.
Notes: Includes all new loans. Refinances category includes loans both in and out-scope of the mortgage measures. 'Other' refers to out-scope negative equity, title transfer and restructured loans.

Chart 50: Average FTB loan size, property value and income have continued to grow in line with trends
Average characteristics of FTB lending



Source: Central Bank of Ireland Monitoring Templates Data.
Notes: FTB in-scope new property purchase and self-build loans only. Income refers to total gross income of all borrowers in each year. All figures are nominal.

Macroprudential policy for non-banks

Reflecting the scale of the sector in Ireland and the growing connections to the domestic economy, developing a macroprudential framework for non-banks remains a key priority for the Central Bank. The focus for the Central Bank in recent years when developing and operationalising macroprudential policy for non-banks has been on the investment fund sector. This reflects the size of the investment fund sector resident in Ireland, its significant growth over the last decade and its interconnectedness to the wider financial system and in some cases the real economy.

The Central Bank has announced two macroprudential measures relating to cohorts of investment funds, which cover property funds and GBP-denominated liability driven investment (LDI) funds. In November 2022, the Central Bank announced the phased implementation of macroprudential limits on leverage of 60 per cent and Guidance on liquidity timeframes to address financial stability concerns with Irish property funds. The Central Bank is currently focused on ensuring appropriate progress is being made throughout the implementation period. New macroprudential policy measures for Irish-authorised GBP-denominated LDI funds were announced in April 2024, and are the second measures under the third pillar of the Central Bank's macroprudential framework in relation to non-banks. The policy measures aim to make this cohort of funds more resilient to shocks to UK interest rates, by codifying and, in certain cases, augmenting the existing yield buffer measure.

The Central Bank continues to advocate progressing the development of an overarching macroprudential framework for investment funds. The Central Bank published a Discussion Paper

on an approach to macroprudential policy for investment funds in July 2023, setting out what the Central Bank considered to be important elements in the development of a comprehensive macroprudential framework for the wider funds sector. The Discussion Paper did not propose specific policy measures, but was designed to engage stakeholders, domestically and internationally, to further advance the discussion on developing an approach to macroprudential policy for investment funds. The Central Bank welcomes the feedback received to the Discussion Paper, and continues to engage with stakeholders on a macroprudential framework for the investment fund sector, including with a related international conference held on 20 May 2024. A Central Bank Feedback Statement to the Discussion Paper will be published in the coming months.

The Central Bank continues to engage actively in international work that seeks to strengthen the macroprudential lens of the regulatory framework for investment funds. The Central Bank plays an active role in several international and European fora in relation to macroprudential policy development for the investment fund sector. This is consistent with one of the key principles set out in the Discussion Paper, emphasising the importance of international coordination. The Financial Stability Board (FSB) published a set of revised policy recommendations on liquidity risk management in open-ended funds (OEFs) in December 2023, with IOSCO concurrently publishing final guidance on liquidity management tools (LMTs). These revised recommendations and guidance seek to address vulnerabilities that arise from liquidity mismatch and to strengthen the effectiveness of liquidity management practices within funds. The recommendations for greater inclusion of LMTs in constitutional documents and their greater use in both normal and stressed conditions is supported by comprehensive guidance on their design and use as part of the liquidity risk management of their OEFs.

The Central Bank supports these recommendations and it is important that the focus now shifts to their implementation as well as engaging in other discrete pieces of work to take forward the development of a macroprudential framework for the funds sector. In order to support the aforementioned work on liquidity risk management in OEFs, the Central Bank is undertaking work domestically to understand better how price-based LMTs are used by Irish-domiciled funds, as well as exploring in more depth some of the key implementation challenges to inform operational discussions internationally on this issue. This includes work on issues such as incorporating the market impact of asset sales into swing factors; inconsistencies in the use of these tools; and their use in normal as well as stressed conditions.

Macroprudential measures for Irish property funds

The Central Bank is focused on monitoring the phased implementation of the macroprudential measures for Irish property funds. Property funds authorised prior to the announcement of the macroprudential measures have until 24 November 2027 to comply with the limits on leverage of 60 per cent, while appropriate action in response to the Guidance on liquidity mismatch was expected by 24 May 2024, for which the Central Bank has issued further clarifications in recent months. Additional data collected as part of the implementation of the measures have provided additional transparency on the sector and enable the Central Bank to monitor closely how property funds are managing leverage-related risks in the context of deteriorating CRE market conditions.

Irish property funds remain a key participant in the Irish CRE market, holding approximately €29 billion in Irish property holdings, including €6.5 billion in indirect property investments. As part of the phased implementation of the macroprudential measures, the Central Bank introduced a new annual data collection to assist with the monitoring of the measures by providing additional information on in-scope property funds. The data allows the Central Bank to identify indirect holdings of Irish CRE by property funds, such as through investments in subsidiaries or related entities, and the additional leverage obtained through these exposures (see also Box 1). Central Bank analysis shows that 42 per cent of Irish property funds maintained leverage in excess of 60 per cent as at end-2022, when the measures were initially announced.[50] The leverage limit is calculated as total debt (i.e. total non-equity liabilities) to total assets. These funds must comply with the limits on leverage by 24 November 2027.

Given the ongoing adjustment in the CRE market, the Central Bank is monitoring closely how funds are managing leverage-related vulnerabilities. Central Bank analysis outlined in *Resilience: Investment funds and non-bank lenders* illustrates that – absent mitigating actions - developments in CRE valuations over 2023 are expected to lead to higher levels of leverage, especially for property funds specialised in the office and retail sectors. In light of the current environment, the Central Bank is actively monitoring how funds are managing leverage-related risks. The Central Bank's annual monitoring assessment of the new measures enables an evaluation on the progress made by property funds towards meeting the requirements of the macroprudential measures, and the broader operation of the measures.

Following the annual monitoring cycle, the Central Bank issued further clarification on its expectations on the Guidance on redemption terms to limit liquidity mismatch for property funds. Last year's annual monitoring assessment in relation to the phased implementation of the Central Bank Guidance on redemption terms highlighted some areas where additional clarity was needed on the Guidance. The Central Bank engaged with fund managers to issue additional clarification around the Guidance.

[50] 42 per cent refers to the percentage of total assets in the sector.

Macroprudential measures for Irish GBP liability driven investment funds

On 29 April 2024, the Central Bank announced the introduction of macroprudential measures for Irish-authorised GBP-denominated liability driven investment (LDI) funds. The measures codify, and in certain cases augment, the existing yield buffer measure in order to safeguard the resilience of LDI funds such that they do not amplify stress in the gilt market as they did over September-October 2022.

The yield buffer is codified in conjunction with the Commission de Surveillance du Secteur Financier (CSSF), with whom the Central Bank undertook an aligned public consultation, given the cross-border nature of this cohort of funds. Irish authorised GBP-denominated LDI funds have until 29 July 2024 to comply with the yield buffer requirement, while the measures apply immediately for any GBP denominated LDI funds in scope authorised on or after 29 April 2024.

The 2022 gilt (UK government bond) market crisis highlighted vulnerabilities amongst GBP-denominated liability driven investment (LDI) strategies that posed a risk to financial stability. Irish-authorised GBP-denominated LDI funds played a significant role in the gilt market crisis in 2022, accounting for approximately 30 per cent (£11 billion) of total net gilt sales, while Irish-resident GBP-denominated LDI funds constitute at least 20 per cent of the UK LDI industry, and a greater share of LDI funds. Gilt sales by Irish-authorised GBP LDI funds were notably concentrated amongst less resilient LDI funds, i.e. those with a lower yield buffer. In November 2022, the Central Bank and CSSF set out a 300-400 bps yield buffer as a minimum safeguard to maintain the operational and financial resilience of GBP-denominated Irish-resident LDI funds in an industry letter.

Building on the November 2022 supervisory expectations, and the recent public consultation process, the Central Bank codified leverage limits for Irish authorised GBP-denominated LDI funds in April 2024. The macroprudential measures for Irish GBP-denominated LDI funds require that Irish authorised GBP-denominated LDI funds maintain resilience to a minimum of 300 bps increase in UK yields. The yield buffer places an upper limit on the amount of leverage that an LDI fund can employ, given the duration of the portfolio. The Macroprudential policy framework for Irish-authorised GBP LDI funds also outlines the main elements of the final framework including its scope, buffer usability feature, and targeted guidance on liquidity.[51] The Central Bank's objective in codifying the yield buffer is to safeguard the resilience of GBP-denominated LDI funds such that they do not amplify stress in the UK gilt market as they did over September-October 2022. Published with the final measures framework was a feedback statement to the related consultation paper (CP157), along with the individual feedback responses received.

The macroprudential measures for Irish GBP-denominated LDI funds are the second measures to be introduced under the third pillar of the Central Bank's macroprudential policy framework in relation to non-banks. The codification of the yield buffer is imposed using Article 25 of the Alternative Investment Fund Managers Directive (AIFMD). Unlike the leverage limit applied to property funds, the yield buffer is codified as an 'other restriction' under Article 25 of the AIFMD, rather than as a single leverage limit. Given the business models and activities of LDI funds, imposing a single leverage limit could lead funds whose portfolios were highly sensitive to interest

[51] For further details, please see the Central Bank's macroprudential policy framework for Irish domiciled GBP-denominated LDI funds.

rates to be able to take on a level of leverage that would see their NAV turn negative in the event of a less than 300 bps increase in yields. Consistent with other regulatory requirements, the yield buffer will be subject to regular monitoring by the Central Bank, and the effectiveness of the measures will be monitored via an updated data template pertaining to these LDI funds.

Given the cross-border nature of GBP-denominated LDI funds, the Central Bank has sought to ensure international coordination and consistency in order to safeguard the effectiveness of the measures. GBP-denominated LDI funds are domiciled in various jurisdictions in the EU, and a cohort of GBP-denominated LDI funds are managed on a cross-border basis. In line with the November 2022 industry letter and the recent consultation process undertaken in parallel with the CSSF, a fully aligned macroprudential framework was also introduced by the CSSF for Luxembourg managed GBP-denominated LDI funds. As part of the Article 25 process, ESMA provided advice to both the Central Bank and the CSSF. They assessed the set of measures as appropriate and concluded that it should contribute to improving the resilience of EU GBP LDI funds.[52] The international cooperation between the Central Bank and CSSF, with the involvement of ESMA, UK authorities and the ESRB, have made this framework the first example of macroprudential measures introduced on a cross-border basis.[53] This approach also reflects the Central Bank's views outlined in DP11, which recognises the importance of international coordination in operationalising a macroprudential framework for investment funds more generally.

[52] See ESMA's advice on the measures proposed by the Central Bank here.
[53] See https://www.cssf.lu/en/Document/macroprudential-measures-for-gbp-liability-driven-investment-funds/.

Abbreviations

Country and currency abbreviations follow the European Union standards.

AIB	Allied Irish Bank
BLS	Bank lending survey
BOI	Bank of Ireland
BTL	But-to-let
CCR	Central Credit Register
CCyB	Countercyclical capital buffer
CET1	Common equity tier 1
CPI	Consumer price index
CRE	Commercial real estate
CSO	Central Statistics Office
EBA	European Banking Authority
ECB	European Central Bank
ESMA	European Securities and Markets Authority
ESRB	European Systemic Risk Board
EU	European Union
FDI	Foreign direct investment
FSR	Financial Stability Review
FTB	First-Time Buyer
GDP	Gross domestic product
GFC	Global Financial Crisis
GNI	Gross national income
HH	Households
ICT	Information and communications technology
IFRS	International financial reporting standards
IMF	International Monetary Fund
IOSCO	International Organisation of Securities Commissions
IPF	Irish property funds
LDI	Liability driven investment
LMT	Liquidity management tools
LTI	Loan to income ratio
LTV	Loan to value ratio
MSCI	Morgan Stanley Capital International
NAV	Net asset value
NBFI	Non-bank financial intermediation
NFC	Non-financial corporation
NPL	Non-performing loan
OEF	Open ended funds
O-SII	Other Systemically Important Institutions
PDH	Primary dwelling house
PMI	Purchasing managers' index
PTSB	Permanent PTSB
RoE	Return on equity
RPPI	Residential property price index
SAFE	Survey on access to finance of enterprises
SCR	Solvency capital requirement
SCSI	Society of Chartered Surveyors of Ireland
SME	Small and medium enterprise
SSB	Second and subsequent buyer
WTO	World Trade Organisation

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