

# DANMARKS NATIONALBANK

29 NOVEMBER 2017 — No. 11

Record-high profits increase banks' risk appetite

## Several banks are stepping on the accelerator



**Optimism and large lending capacity make banks more willing to take risks.**



**Rising house prices have increased home equity, and this may lead to strong growth in lending by banks and mortgage banks.**

The largest banks and mortgage banks came out of the 1st half of 2017 with record-high profits, which has boosted optimism in the financial sector and is increasing the institutions' risk appetite. Several banks are stepping on the accelerator by easing credit standards and granting loans to more vulnerable customers. This may lead to more losses.

That is Danmarks Nationalbank's conclusion in its Financial Stability analysis, which also notes that growth in the banks' profits is to a large extent attributable to extraordinarily high value adjustments and very low loan impairment charges.

### Indications of higher risk in bank lending

While growth in lending to households remains modest, lending to corporate customers is rising, especially to firms that are sensitive to fluctuations in the economy in general.

"Loan impairment charges and losses on these industries cannot be expected to remain at the present low level when the economy reverses," the analysis concludes, also pointing out that many banks have the capacity to increase lending. This intensifies competition for customers as well as the pressure on the banks' credit standards.

According to Danmarks Nationalbank's quarterly lending survey, medium-sized and large banks alike have tended to ease credit standards in recent years. Both groups state that increased competition from other banks is the main reason for adjusting credit standards.

The aggregate trend in bank lending in combination with other factors indicates that risks are building up in the financial system. Low interest rate, rising house and equity prices, and the economic upswing are all drivers of an increasing

### ABOUT NEWS



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risk appetite. Against this background, Danmarks Nationalbank assesses that the conditions for activating the countercyclical capital buffer are in place. The banks and mortgage banks should build up this buffer and strengthen their capitalisation in good times. When the financial system becomes stressed, the buffer is to be released. In that way, the institutions have capital at their disposal which they can use to keep up their lending capacity.

#### Lack of limitation of interest-only loan

Higher house prices have increased home equity for many owners, so credit growth may take off suddenly if households increasingly begin to raise new loans against home equity as collateral. A rising share of homeowners have high debt-to-income, DTI, ratios, Danmarks Nationalbank notes.

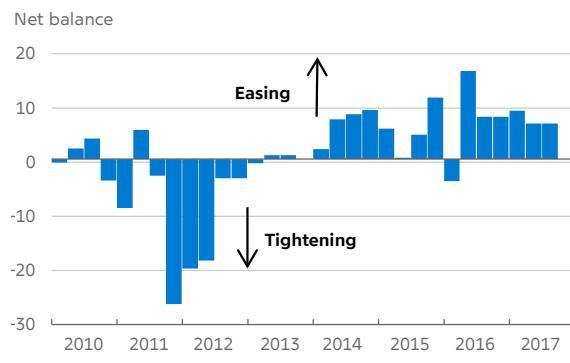
The Danish Financial Supervisory Authority's proposal to amend the rules for good business practice for mortgage lending will contribute to limiting the range of loan types available to homeowners with high DTI ratios. The nationwide scope of the proposal is positive. On the other hand, it is inexpedient that people with high debt ratios can still obtain loans with deferred amortisation when buying a home.

Ensuring the stability of the financial system is one of Danmarks Nationalbank's overall objectives, so especially the largest banks are subject to monitoring as it may have negative implications for the financial sector and for the economy as a whole if the banks encounter difficulties.

See the full Financial Stability analysis at  
Danmarks Nationalbank's website ([link](#)).

#### Banks are easing credit standards for corporate customers

Chart 1

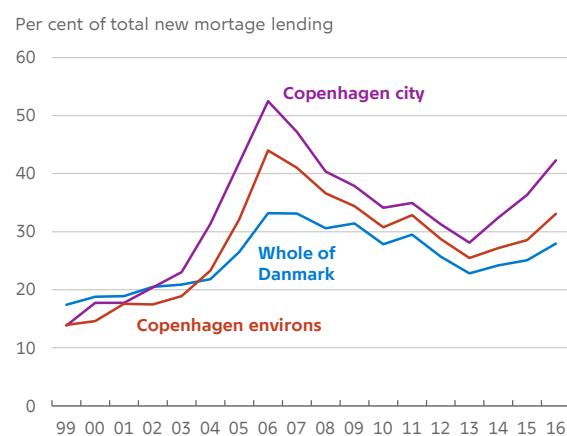


Note: Since the 2nd quarter of 2013 credit standards have been eased in all quarters, except one.

Source: Danmarks Nationalbank.

#### Larger share of households with high debt

Chart 2



Note: Share of new mortgage loans among households with loan to income greater than 4.

Source: Statistics Denmark, Danish mortgage banks and own calculations.