MEMORANDUM

The Danish FSA
31 August 2018

Statement on inspection at Sydbank A/S (loans to finance purchases of owner-occupied dwellings in growth areas)

Introduction

In February and March 2018 the Danish FSA conducted an inspection of Sydbank's approvals of new loans to retail customers to purchase owner-occupied dwellings in growth areas. The inspection formed part of a thematic review of six large banks' approvals in Q2 and Q3 2017.

Competition for home buyers has been intense in recent years, which has manifested itself in for instance increased risk-willingness among banks. This is reflected by the fact that in a number of cases banks have approved loans to customers with a low disposable amount, high debt-to-income ratio or negative assets.

The main objective was to assess the bank's risk appetite in connection with lending to customers' purchases of owner-occupied dwellings in growth areas. For that purpose the Danish FSA reviewed whether the bank's approvals were in compliance with the guidance on prudence in the credit evaluation as regards housing loans in growth areas etc (growth guidance) issued in January 2016. Moreover the Danish FSA assessed the bank's own controls and reporting as to whether the approvals were in compliance with the growth guidance.

The growth areas had been defined as Copenhagen and its suburban municipalities as well as the municipality of Aarhus.

Summary and risk assessment

The Danish FSA's assessment as to whether the approvals were in compliance with the growth guidance was based on a random sampling review of 14 approvals which had been established during the review period and a data analysis of all the bank's approvals of loans to purchase owner-occupied dwellings in growth areas during the review period. In addition the Danish FSA reviewed the result of the bank's own controls in relation to the growth guidance.

According to the guidance banks must take extra care to ensure that customers purchasing homes in growth areas have sound finances.

More than 4% of the approvals to purchase owner-occupied dwellings during the review period did not live up to the growth guidance. The primary deviation was that customers had a high debt-to-income ratio without having sufficiently large assets. Consequently the finances of these customers were not sufficiently sound. The share of cases with deviations was somewhat lower than those of the other banks inspected.

According to the bank's approval structure, approvals that do not live up to the principal rules of the growth guidance can only be approved by the credit department. The Danish FSA assesses that this is an important reason why the share of cases deviating from the growth guidance is lower than that of the other banks inspected.

The credit department did not check compliance with the growth guidance until autumn 2017. The control was inadequate.

The bank's independent credit control function had not performed controls in relation to compliance with the growth guidance.

The bank was ordered to ensure that credit controls of compliance with the growth guidance will be performed and that the findings thereof will be part of management reporting.