

Statement of the Financial Stability Committee 18 March 2020

The Financial Stability Committee of the Central Bank of Iceland has decided to reduce the countercyclical capital buffer on financial institutions from 2% to 0%. Rules to this effect have been approved and will take effect upon publication in the *Law and Ministerial Gazette (Stjórnartíðindi)*. The Committee will not increase the countercyclical capital buffer in the next twelve months; therefore, according to the applicable rules, it will remain unchanged for at least two years, until Q1/2022.

The spread of COVID-19 has had a profound impact on communities, dampening economic activity and eroding financial conditions worldwide. It is uncertain how strong this impact will be and how long it will last, but it is clear that the economic outlook for Iceland has deteriorated markedly, at least for the short term.

The Icelandic banks' capital position is strong, and well above current Central Bank requirements. The banking system is well equipped to respond to shocks. It is important, however, to mitigate the negative impact of increased arrears and impairment on the intermediation of credit. Lifting the countercyclical capital buffer requirement will make it easier for the banking system to support households and businesses by increasing flexibility for new lending in an amount ranging up to 350 b.kr., or 12.5% of the current loan portfolio, all else being equal.

The main objectives of the countercyclical capital buffer are to strengthen financial institutions' resilience to cyclical risk and strengthen credit intermediation during contractionary episodes, thereby mitigating the impact of the financial cycle on the real economy. In recent years, the buffer has been built up in order to mitigate cyclical risk.

The Financial Stability Committee urges financial institutions to take into consideration the currently high level of economic uncertainty when they take decisions on dividend payments and stock buybacks in the coming term. The Committee expects the scope created with the reduction in the countercyclical capital buffer to be used to support households and businesses. The banking system's response, the position of households and businesses, and the financial conditions offered to them will be closely monitored in the coming term. The Committee is prepared to use the tools at its disposal to safeguard financial stability in Iceland.