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## Financial stability

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# Revised format for financial stability assessment

- Publication on new Bank of Finland Bulletin site
- Comprises an editorial, a summary and a number of thematic articles
- Topical articles and other material published on the site throughout the year
- [www.bofbulletin.fi/en/financial-stability](http://www.bofbulletin.fi/en/financial-stability)



## Lessons learnt from previous crises – unforeseen risks pose new threats

- Broadly based strengthening of financial regulation and supervision
- Macroprudential instruments created to prevent financial crises and enhance loss-absorbing capacity of financial institutions
- However, new unpredictable risks may emerge in current exceptional operating environment



# World economy and global financial markets in uncharted waters

- Abundant liquidity in international financial system largely channelled into financial investments
- Prolonged period of low interest rates encourages a search for yield and increased risk-taking
- Strong increases and decreases in international asset prices also spill over to Finland



# Finnish banking sector structurally vulnerable

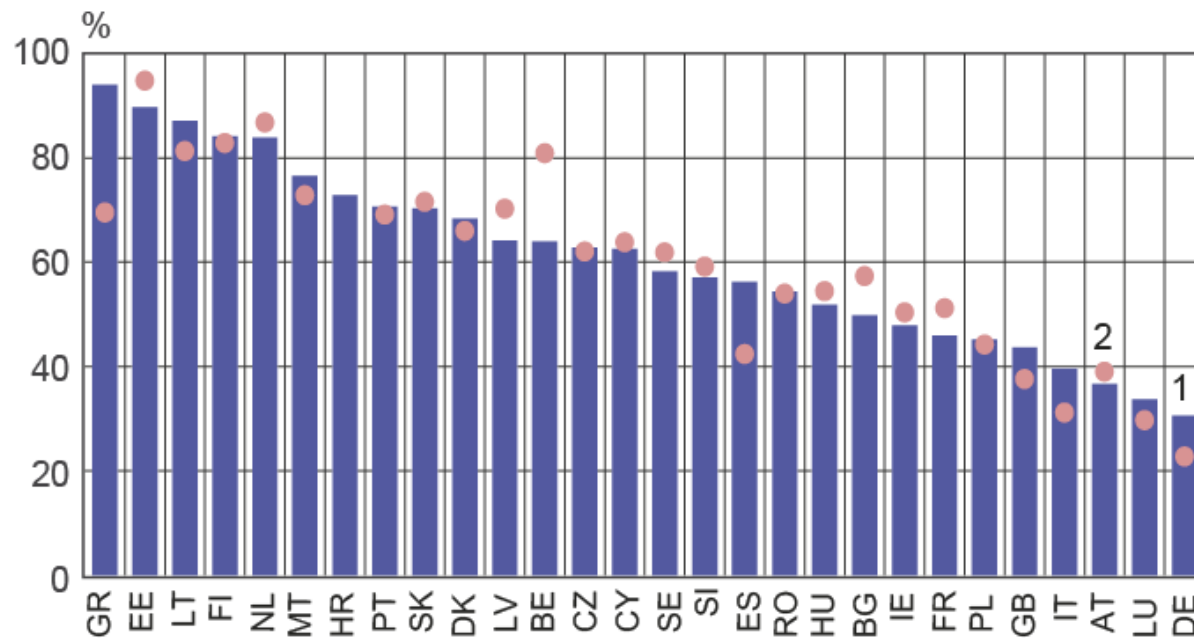
- Profitability and capital adequacy have remained strong in a difficult operating environment
- The Finnish banking sector is
  - among the most concentrated in the euro area
  - dependent on funding raised from international financial markets
  - strongly linked across borders
  - focused on lending for house purchase
- A concentrated banking system amplifies the severity of crises



# Finnish banking sector concentration among highest in euro area

**Proportion of total banking sector assets held by five largest banks, by country**

1. ■ 31 Dec 2013      2. ● 31 Dec 2008



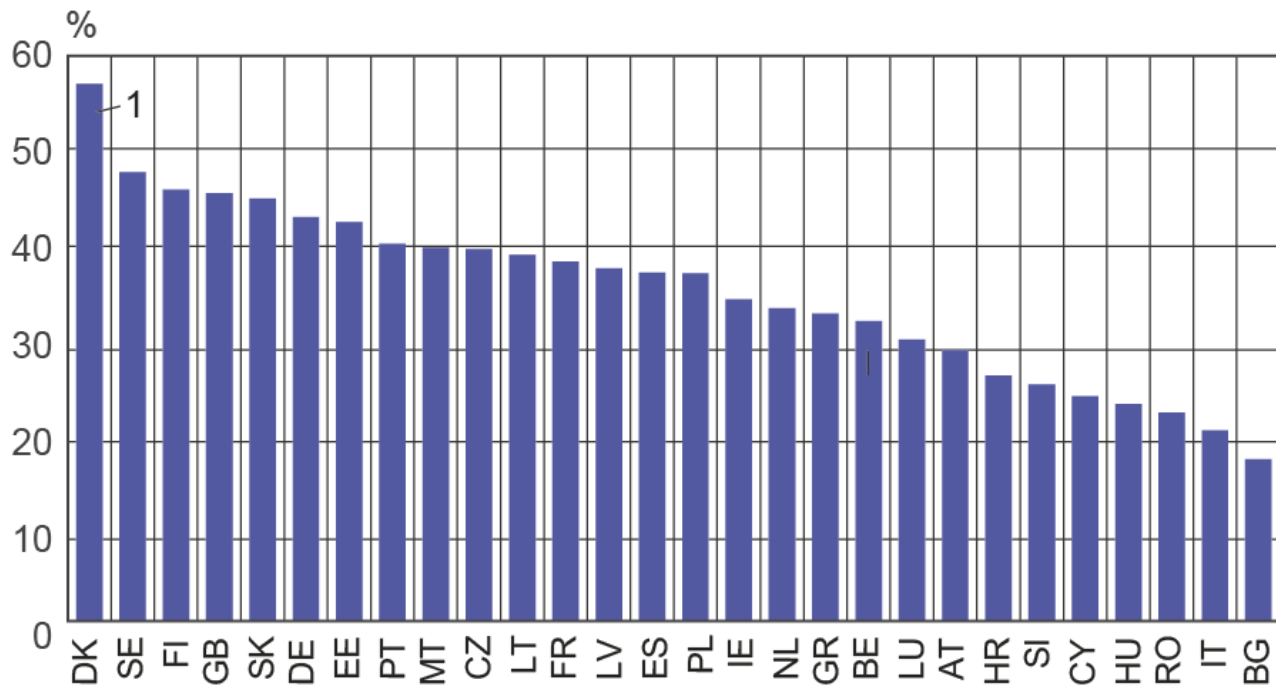
Source: European Central Bank.



# Lending for housing purchase a key activity for banks

Housing loans as a proportion of bank lending

1. ■ 31 Dec 2014



Source: European Central Bank.



## Well-functioning corporate finance provides base for economic growth

- Financing for SMEs mainly provided by banks, dependence further increased
- Widening margins on corporate loans signalling reduced bank competition?
- Diversified corporate finance beneficial to economic growth



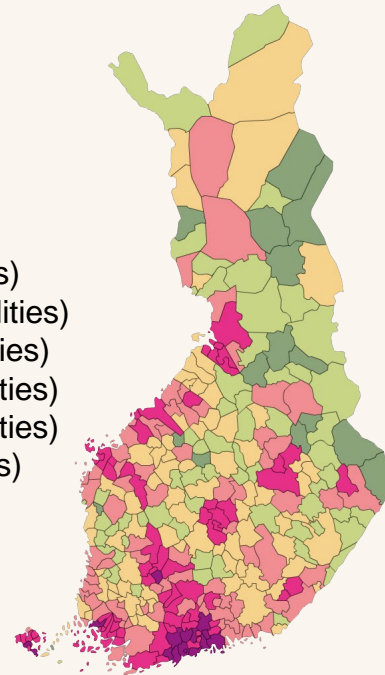
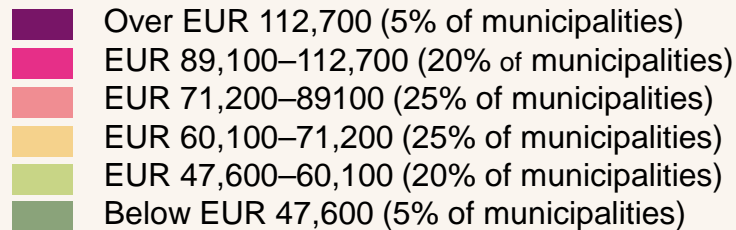


## Housing debt piles up – indebted households vulnerable to changes in economic conditions and interest rates

- Amount of household loans relative to GDP doubled since turn of millennium
- Housing debt burden and related risks concentrated on just a small group of debtors
- Regional divergence in housing markets and debt in Finland

# Housing debt concentrated in growth centres

## Size of housing debt by municipality, per household with housing debt



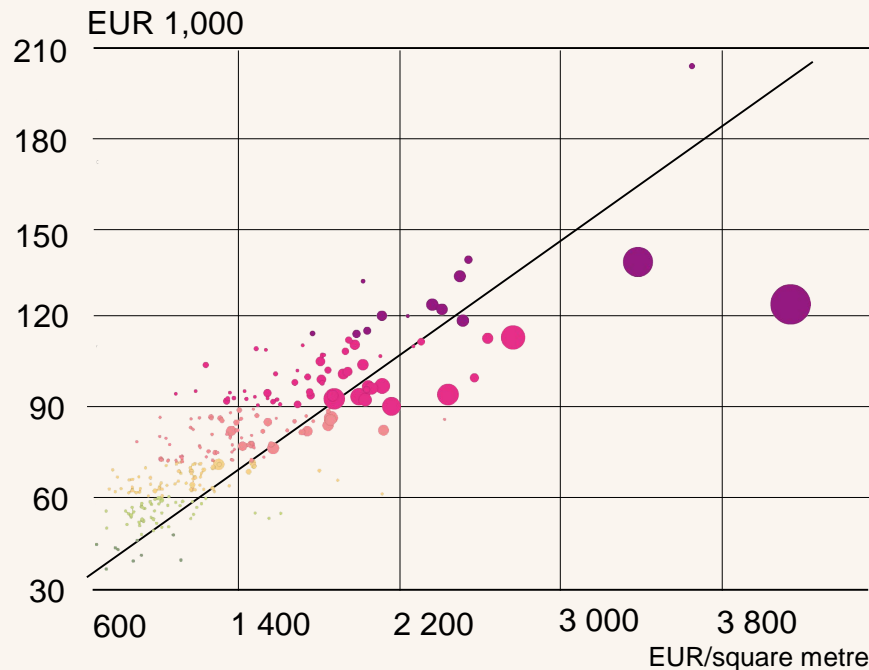
Housing loan debt categories are composed on the basis of the 5th percentile, lower quartile, median, upper quartile and 95th percentile of the distribution. The data refer to 2013.

Sources: Statistics Finland and Bank of Finland calculations.



# As with debt, strong divergence in prices

## Housing debt and house prices by municipality



The vertical axis indicates the average amount of housing loan per household with housing debt (EUR 1,000); the horizontal axis indicates the average selling price of an apartment in a housing company (EUR/square metre) in 2013. The diameter of a circle denotes the aggregate amount of housing debt in a municipality.

Sources: Statistics Finland and Bank of Finland calculations.



## Low interest rates and slow economic growth weigh on insurance sector

- Finnish insurance sector's profitability and solvency are strong.
- Slow economic growth and low interest rates cut insurance companies' investment income and increase their liabilities.
- More attention should be paid to potential systemic risks posed by possible extensive sales of insurance companies' investments.



## Increased risks to financial market infrastructure

- Financial sector digitalisation improves the supply and availability of financial services, increasing the efficiency of operations and promoting competition.
- The threat of a cyber attack against an increasingly digitalised financial sector has grown.
- Internationalisation of the Finnish payment system and securities services has made Finland dependent on foreign service providers.

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## Conclusions





## Tools must be available to curb debt accumulation and mortgage lending

- The increase in debt levels makes households vulnerable.
  
- A housing loan must not be too large relative to a household's debt-servicing capacity.
  
- Postponing debt repayment with interest-only periods is not a 'free lunch'
  - Increases the household sector's debt burden and vulnerability
  - Flexibility is justifiable, case-by-case
  - No reason to launch non-amortising housing loans in Finland, as experiences from other countries have been negative



## Competition must be fostered in provision of financial services

- Banks' good cost-efficiency facilitates provision of competitive services.
- We need diverse service providers and sources of finance.
- The European Commission's plan for Capital Markets Union will improve conditions for corporate finance and economic growth.
- Growing popularity of non-bank finance means we must prepare for related risks.





## Strong capital adequacy in Finnish financial sector must be ensured

- MFIs must maintain their strong capital positions to ensure their loss-absorbing and lending capacity in all circumstances.
- Authorities must have internationally harmonised tools to ensure this.
- The regulatory differences between the Nordic countries are harmful.
- The principle of proportionality must be observed: there must be discretion for applying regulations less stringently to smaller entities.

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**Thank you!**





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