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Experiences from the 1990s financial crisis in Nordic countries

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The views expressed are my own and do not necessarily represent the position of the Bank of Finland

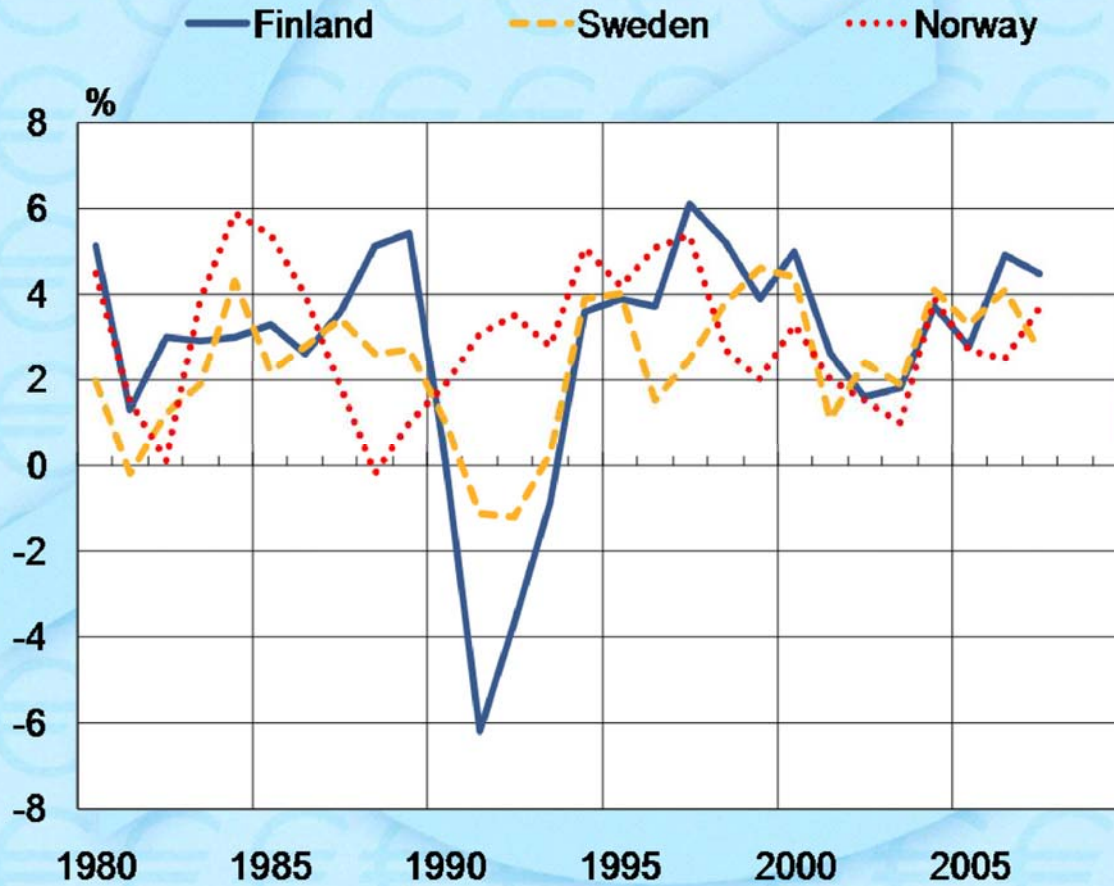
1. Introduction

- ◆ 19 crises in advanced countries since WWII (before the current crisis)
- ◆ 1990's crises in Finland, Norway and Sweden are among the "big five"
- ◆ Crises in Finland, Norway, and Sweden became systemic
 - Crisis remained non-systemic in Denmark

II. Main Developments

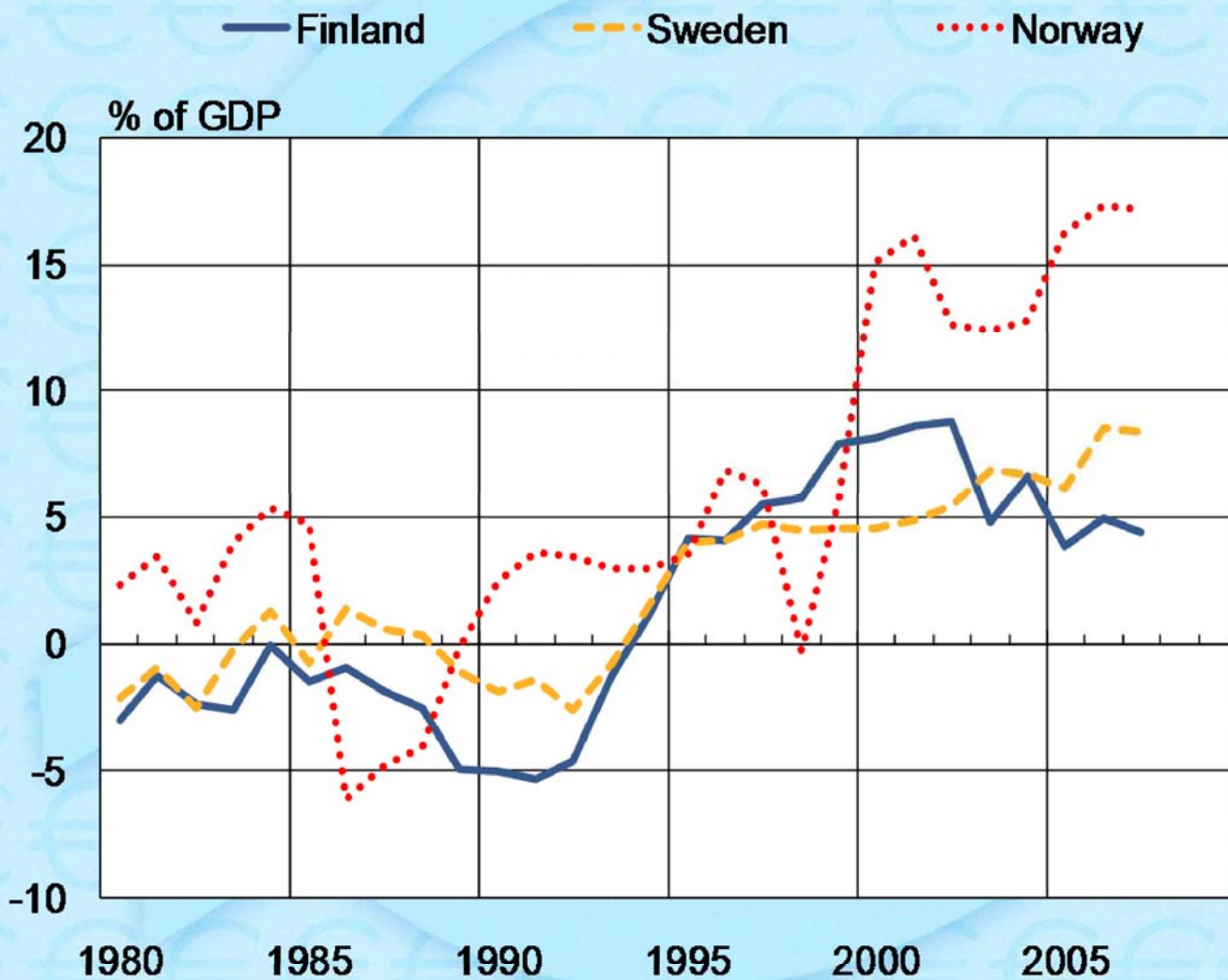
II.1 The Real Economies

Figure 1. Real GDP growth



Sources: Eurostat and IMF.

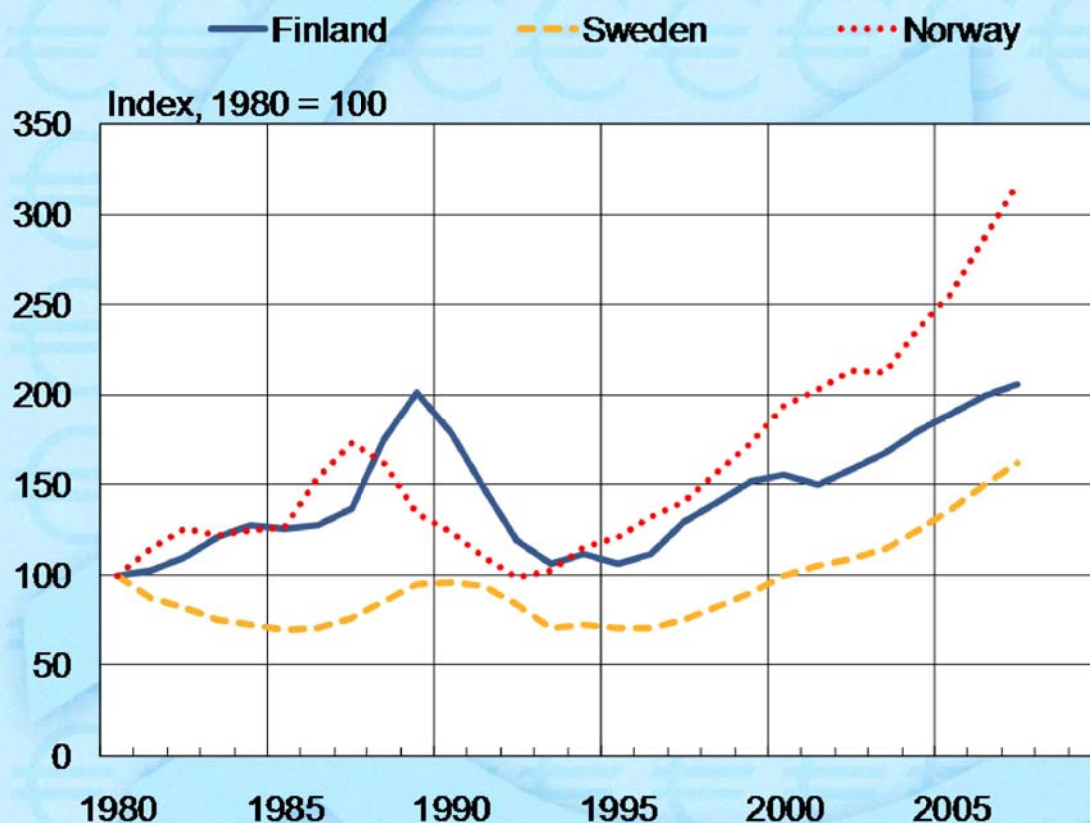
Figure 2. Current account



Source: European Commission.

II.2 Financial developments

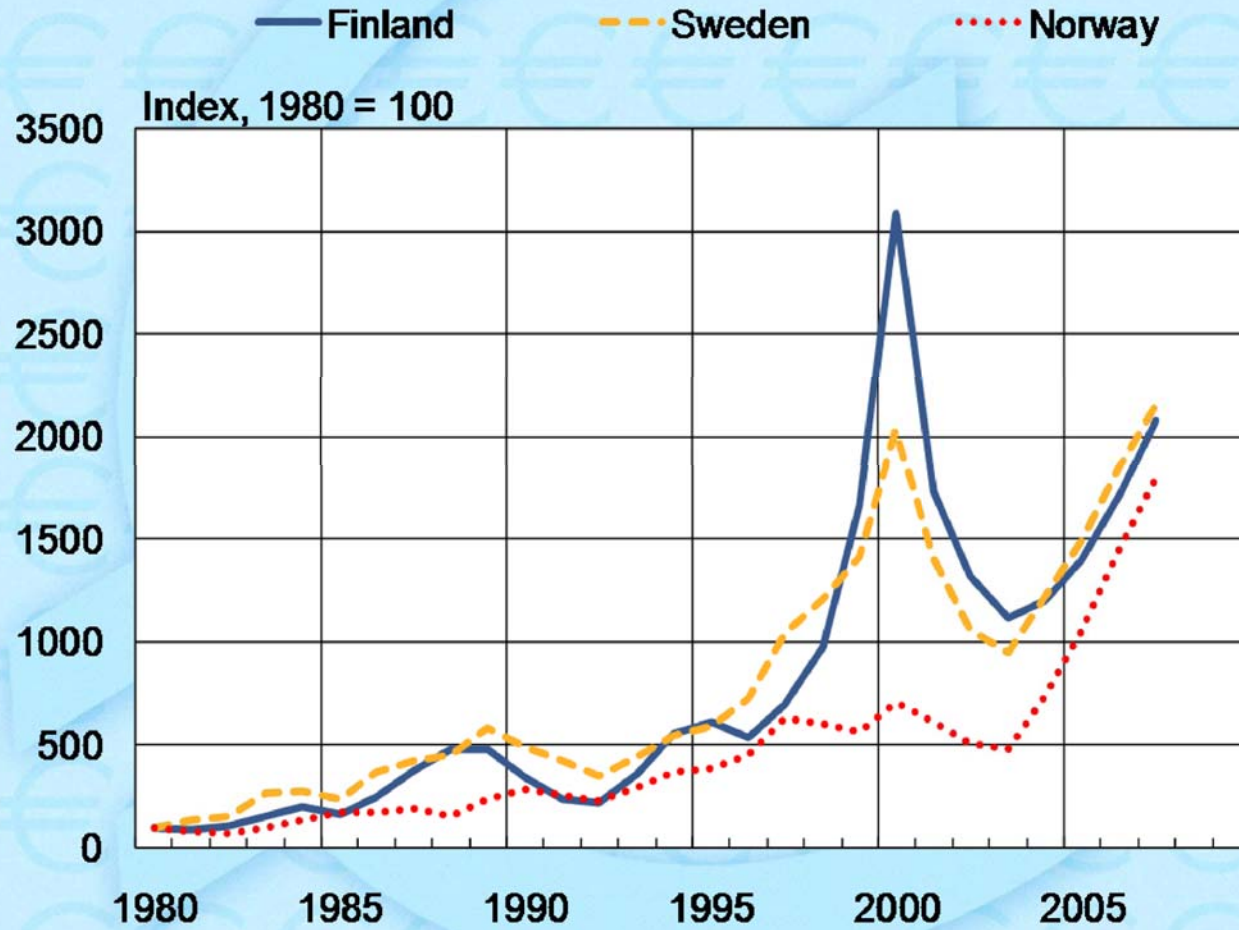
Figure 4. Real house prices



Nominal house prices deflated using the consumer price index.

Sources: Statistics Finland, Statistics Sweden, Norges Bank and Bank of Finland.

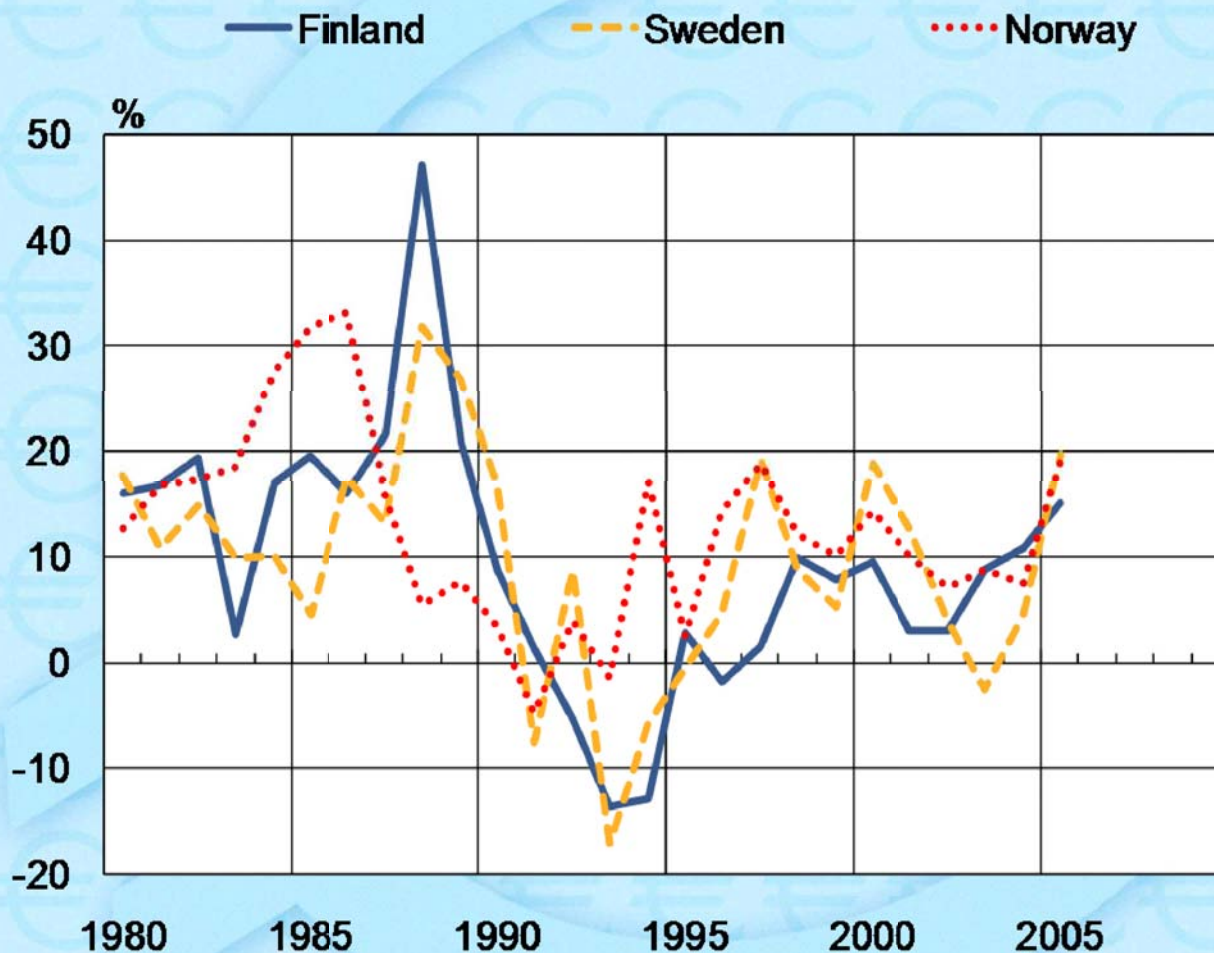
Figure 5. Real share prices



Nominal share prices deflated using the consumer price index.

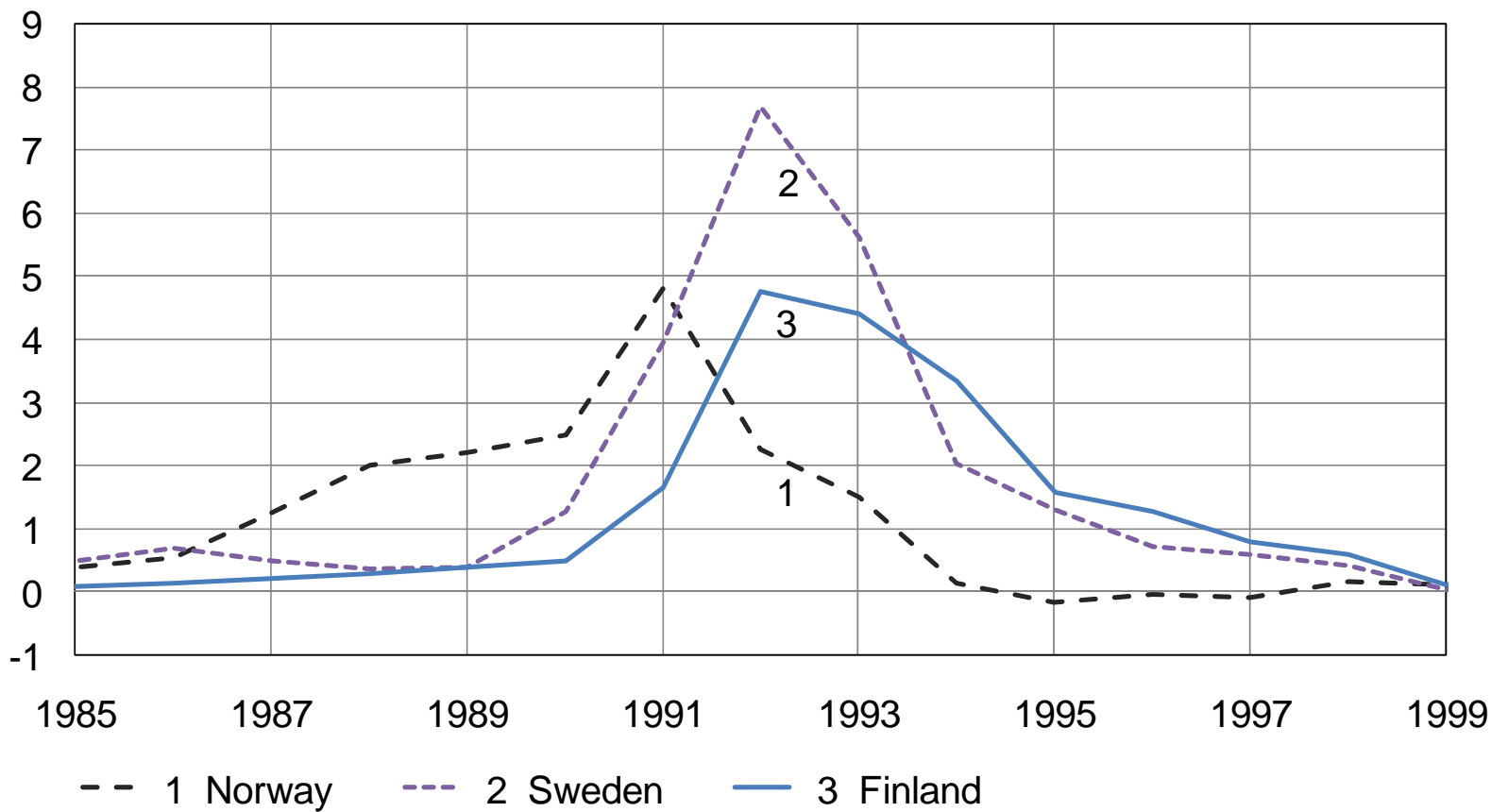
Source: IMF.

Figure 6. Lending growth



Sources: OECD and Bank of Finland.

Loan losses/lending in the Nordic countries' banking sector 1985-1999, %



Source: Central banks.

III. Management of banking crisis

◆ Finland

- 1st measure: Bank of Finland took control of Skopbank in September 1991
- Public support: preferred capital certificates to banks, with strict requirements
- Support to be converted into shares if not repaid
- Government set up the crisis management agency to restructure the banking system
- Policy-makers made promises to guarantee banks' obligations, also further public support

◆ Finland (continued)

- Banks became profitable again in 1996
 - Improved efficiency (staff halved, etc.)
 - Major restructuring of banking system:
 - savings banks largely disappeared,
 - one big commercial bank was merged to another
 - remaining comm. bank merged with Nordbanken
 - Nowadays about 60 percent of banks owned by foreigners
- => Biggest part of the crisis was in Savings Banks

◆ Sweden

- Crisis erupted in autumn 1991 with Första Sparbanken; government gave a loan and FS merged with other savings banks
- Nordbanken (3rd largest comm. bank) was 71% govt owned and had to be recapitalized
- Many banks made heavy credit losses
- In autumn 1992 blanket creditor guarantee by government
- Crisis resolution agency set up, public support with strict criteria in risk reduction and efficiency

- ◆ Sweden (continued)
 - Some banks did not need public support
 - ⇒ In the end nearly all support went into two banks, Gotabanken and Nordbanken.
 - ⇒ Nordbanken became a pan-Nordic bank "Nordea".

◆ Norway

- Crisis erupted in autumn 1988
- Initially private guarantee funds provided support and bank mergers took place
- In late 1990 private funds were exhausted, so government guarantee fund set up in early 1991
- Support had to be converted into solvency support
- In autumn 1991 capital support needed
- In Spring 1992 several banks, incl. three biggest commercial banks were nationalized

◆ Norway (continued):

- no blanket guarantee by government, but specific announcements about securing depositors and creditors
- Banks' situation started to improve in 1993
- One of the nationalized banks was sold in 1995 and two other banks were sold later
- Government still owns 34 percent of one bank

=> In the end the Norwegian tax payer made money out of the crisis. The table shows gross and net fiscal costs.

Fiscal costs

	Gross cost	Net cost
Finland	9.0 (% of 1997 GDP)	5.3 (% of 1997 GDP)
Norway	2.0 (% of 1997 GDP), 3.4 (present value, % of 2001 GDP)	-0.4 (present value, % of 2001 GDP)
Sweden	3.6 (% of 1997 GDP)	0.2 (% of 1997 GDP)

IV. Some lessons for crisis management

IV.1 Prevention of a major crisis

- ◆ This is the first priority
=> stability-oriented macro policies
- ◆ How to diagnose an overheating situation?
 - rapid credit expansion
 - strong increase in leverage
 - big external deficits in open economies
- ◆ **Political-economy reasons** can be an obstacle in crisis prevention.

IV.2 Crisis management

- ◆ Maintaining confidence in the banking system is crucial
 - Broad political support and speedy action were important
 - Political guarantees to banks' obligations in Finland and Sweden but not in Norway
- ◆ The role of central banks: liquidity provision, emergency loans
 - Liquidity support in Norway and Sweden
 - Bank of Finland had to take over a problem bank

- ◆ Restructuring of the banking system
 - **Crisis resolution agencies** were used all Nordic countries
 - Capital injections to banks
 - treatment of "old shareholders" was mixed
 - Guidance of restructuring of the banking system
 - Administrative separation from central bank and ministry of finance

- ◆ Asset management companies ("bad banks") to deal with non-performing assets
 - Norway: banks had their own bad banks
 - Finland and Sweden had public agencies
 - A private good bank / bad bank scheme used by Finnish cooperative banks



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Thank you