Minutes of the meeting of the Council for Cooperation on Macroprudential Policy held on 24 February 2012

Finansinspektionen and the Riksbank have held their first meeting within the framework of the Council for Cooperation on Macroprudential Policy. The two authorities discussed the current situation and noted that the unease on the financial markets has subsided somewhat and that the resilience of the Swedish banks is still strong. They also discussed Finansinspektionen's work on the introduction of a Liquidity Coverage Ratio and the ongoing work to evaluate the loan-to-value mortgage cap. Finansinspektionen also gave an account of its ongoing inquiry into risk weights for Swedish mortgages. Finansinspektionen's ambition is to present a proposal on this issue by this summer. The two authorities also noted that there is a risk that the maximum harmonisation of the future capital adequacy regulations within the EU will constitute a significant obstacle to effective macroprudential policy.

Resilience of Swedish banks still strong

Late last year, Finansinspektionen and the Riksbank assessed that the resilience of the Swedish banks was strong and that they were thereby well equipped to cope with weaker economic development in Sweden and abroad. The Swedish banks had, in addition, good access to market funding.

At that time, the authorities pointed out that the greatest risk of a disruption to the Swedish financial system lay in the concern about public finances in the euro area and the unease this had led to on the financial markets.

The authorities noted during the meeting that the unease on the financial markets has abated since these assessments were published. There are a number of reasons for this, for example the impact of the political efforts that have been made. In addition, the three-year loans offered to the European banks by the ECB have eased the strained funding situation in the short term. Many banks have also raised new capital on their own. However, although unease in Europe has declined the crisis has not been resolved. This means that the public-finance problems in Europe and the unease concerning European banks continue to pose the greatest risks of a disruption to the Swedish financial system. However, the resilience of the Swedish banks is still strong and they continue to have good access to market funding.

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Other macroprudential policy issues

The recommendation of the European Systemic Risk Board (ESRB) concerning the European banks' dependence on US dollar funding
The authorities in the Council discussed the recommendation published by the European Systemic Risk Board (ESRB) on 16 January 2012 which aims to prevent the risk of the European banks' dependence on US dollar funding leading to a crisis situation. The ESRB recommends that the national supervisory authorities should, as a preventive measure, monitor imbalances in maturities between assets and liabilities in US dollars and ensure that the banks have sustainable contingency plans for their funding in US dollars.

The authorities believe that the ESRB's recommendation is highly relevant for Sweden as there is a significant liquidity risk in foreign currency, and particularly in US dollars, in the Swedish financial system.

Finansinspektionen gave an account of its work on the implementation of the recommendation. During the course of 2012, Finansinspektionen will ensure that the banks report and have contingency plans in line with the recommendation. Another important component of the effort to limit the liquidity risk in US dollars is to introduce requirements for a Liquidity Coverage Ratio (LCR) for this currency, too, see below.

The European Systemic Risk Board's (ESRB) recommendation on lending in foreign currency
At the Council meeting, the authorities discussed the recommendation on lending in foreign currency that the ESRB issued on 11 October 2011 with the aim of reducing the risks associated with lending in foreign currency. The ESRB's recommendation primarily applies to new loans in foreign currency and means, among other things, that the authorities concerned should ensure that the banks inform borrowers about risks (for example exchange-rate risks) and that the banks should have sufficient equity to be able to manage the risks that lending in foreign currency entails.

The Council participants believe that the ESRB's recommendation in this area is important. Previous Swedish experience – partly from the Swedish crisis of the 1990s, and partly from the crisis in the Baltic countries – has clearly demonstrated the risk that lending in foreign currency constitutes to the stability of the financial system. The authorities noted that this mainly relates to the Swedish banks' operations in the Baltic countries and Poland. It will therefore be appropriate to raise this issue in Nordic-Baltic forums and the supervisory colleges concerned during the spring. The authorities will then return to this issue at a future meeting of the Council.

Introduction of a Liquidity Coverage Ratio (LCR)
As a part of the Basel III Accord, the Basel Committee has proposed a Liquidity Coverage Ratio (LCR) that aims to strengthen the banks' resilience to short-term liquidity stress. In brief, this requirement means that the banks should maintain adequate liquidity reserves to be able to handle short-term outflows in stressed situations.

Both Finansinspektionen and the Riksbank have previously stated that as far as Sweden is concerned the LCR should apply from January 2013. This means that Sweden will introduce this regulation before 1 January 2015, the date by which it should be introduced under the Basel III Accord, and before the regulation begins to apply in the EU. Both Finansinspektionen and the Riksbank believe that this regulation is of such importance to increasing the resilience of the Swedish financial system that Sweden should introduce it earlier.

During the meeting, Finansinspektionen gave an account of its work to implement the LCR. Requirements will be stipulated jointly for all currencies and separately for the euro and the US dollar. A consultation on the proposed regulations is planned for the summer. Finansinspektionen's assessment at the meeting was that it should be possible to implement the LCR by 1 January 2013.

The implementation of Basel III at the EU level and stricter requirements for Swedish banks
In the Basel III Accord, the Basel Committee has proposed reforms that entail increasing the capital adequacy requirements for the banks in comparison with previous regulations, as well as stricter regulations on what may be included in the capital and how it should be calculated. The Basel III Accord is not formally binding for Swedish banks. To become binding, the Accord must be implemented into national law through EU laws or Swedish legislation.

Work is underway to implement the Basel III Accord at the EU level. The current proposal for a regulatory framework for the EU contains a requirement for maximum harmonisation; that is, a restriction on the possibility of individual Member States to impose stricter requirements on banks (capital adequacy requirements, etc.) through legislation or regulations than those stipulated in the EU regulation. If the current proposal is accepted, it will be more difficult to impose capital adequacy requirements on Swedish banks that exceed the requirements in the EU regulation as planned. The Ministry of Finance, Finansinspektionen and the Riksbank advocated on 25 November 2011 that the capital adequacy requirements for the four major Swedish banking groups Handelsbanken, Nordea, SEB and Swedbank should be at least 10 per cent of their CET 1 capital from 1 January 2013, and 12 per cent from 1 January 2015.[1]

The authorities in the Council believe that maximum harmonisation constitutes a significant obstacle to effective macroprudential policy. It is probable that systemic risks vary between the Member States as there are major differences within the EU; there are, for example, major structural differences between the various financial systems. The Member States must be able to safeguard their national financial stability as each Member State has the ultimate responsibility for the commitments of its national banking system. It is therefore vital that the Member States have the possibility to set stricter capital requirements than in the Basel III Accord if this is justified on the basis of the national structures and risks in the national financial systems.

Creating the preconditions for a stable and efficient financial system is in the interests of the EU as a whole. Setting insufficiently stringent requirements for financial institutions in one Member State may lead to financial unease in the rest of the EU. Finansinspektionen and the Riksbank therefore believe that the regulatory framework should be designed so that it permits Member States to introduce stricter regulations than those presented in the EU regulation. The Member States should be given the possibility to deal with national imbalances, for example by setting stricter requirements for systemically-important institutions, higher risk weights for mortgages or stricter requirements for liquidity buffers. It should be possible to incorporate such requirements in national legislation and statutes and not simply rely on supervision under Pillar 2.

[1] See press release from Finansinspektionen at www.fi.se/Press/Press releases/2011 "New capital requirements for Swedish banks"/ and press release from the Riksbank at www.riksbank.se/en/Press and published/Press/Press release/2011/"New capital requirements for Swedish banks"/.

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Mortgage survey and Finansinspektionen's inquiry on increasing the capital requirement for mortgages
Finansinspektionen will soon present a report based on the mortgage survey conducted during the autumn which, among other things, analyses the effects of the loan-to-value mortgage cap. Finansinspektionen briefed the participants on how the mortgage survey was conducted, the current progress of the report and the preliminary conclusions that have been drawn.

The authorities then discussed the risk weights for Swedish mortgages in the Swedish banks' internal models for the calculation of capital requirements. The models stipulated in the international capital adequacy regulations, which the major Swedish banks use to calculate the risks in their mortgages, can result in too low capital requirements for the mortgage portfolios of the Swedish banks. This is the case even after the introduction of the higher capital requirements for systemically-important Swedish banks. Finansinspektionen is therefore investigating various ways of increasing the capital requirement for mortgages, thereby increasing the Swedish banks' resilience to financial crises, as well as market confidence in the capital strength of the banks. During the meeting, Finansinspektionen described the progress of this inquiry. Finansinspektionen's ambition is to publish a proposal by the summer of 2012.

In mid-February, the European Commission published an Alert Mechanism Report in which the competitiveness as well as internal and external imbalances of the EU countries are analysed. For a large number of EU countries (including Sweden), the EU points out that further analyses of a range of issues are required. In Sweden's case this relates, for example, to the need for a deeper analysis of household indebtedness and changes in housing prices. The authorities in the Council believe that it is important to carefully analyse these issues and to continue to focus on them. The mortgage survey is a part of this work. The authorities also noted that the issues discussed during the meeting, such as stricter capital adequacy requirements for systemically-important banks, risk weights for mortgages and the introduction of LCR will increase the resilience of the financial system.

The Council also discussed the need for greater transparency at the banks with regard, for example, to their costs for mortgages. The authorities believed that it should be possible for the banks to publicly and more clearly present their costs for mortgages, and thus the development of mortgage rates, to the consumers.