



Decision

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DEPARTMENT: Asset Management Department/Financial Stability Department
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■ Change in the rules regarding limitations for collateral in the form of covered bonds issued by the counterparty or by an institution with close links to the counterparty for credit in the RIX payment system

Background

The Riksbank decided on 13 December 2007 to accept covered bonds issued by the counterparty, or by an institution with close links to the counterparty¹, as collateral for credit in RIX or monetary policy instruments. As it was assessed that these covered bonds contained a higher risk than covered bonds issued by an institution independent of the counterparty, it was decided that an extra haircut would be made on these bonds.

At the same time, the Riksbank decided on a concentration limit, which meant that a maximum of 25 per cent of a counterparty's total collateral value could be comprised of securities issued by the same counterparty or by a group of closely-related issuers. Today this limitation only applies to covered bonds issued by the counterparty or by an institution with close links to the counterparty and to other securities issued by a Swedish bank or foreign credit institution. However, the opinion was that this limitation might later be applied more generally, after a consultation process.

On 18 September 2008 the Swedish National Debt Office, after consultation with the Riksbank, decided on measures to ease the functioning of the Swedish money and bond markets. The market for treasury bills had been subjected to strong demand pressures; this was linked to the developments in the US market. The Swedish National Debt Office decided on an additional issue programme for treasury bills. The liquid funds from these issues would be used for reverse covered mortgage bond repos. This would also ease tensions on that market.

Given these events, the Riksbank has found reason to consider taking measures to further facilitate the functioning of the money and bond markets. Taking into account the deliberations made in connection with the decision taken in December 2007, there is reason for the Riksbank to examine whether covered bonds issued by the counterparty or by an institution with close links to the counterparty can be accepted to a greater extent.

¹ Covered bonds in this context refer to debt instruments issued in accordance with the Swedish Covered Bonds Act (2003:1223).

Considerations

There is no equivalent to the Riksbank's rules regarding extra haircuts and limitations to the volume of covered bonds issued by the counterparty or by an institution with close links to the counterparty in the central banks in the Eurosystem, in Denmark or in Norway.

The Riksbank's assessment when making the decision in December 2007 was that it was appropriate, from a risk point of view, to aim at diversification in the collateral volume pledged to the Riksbank by its counterparties. One means of achieving this aim is to limit the share of the counterparty's collateral that is issued by the same counterparty or by a group of closely-related issuers. The Riksbank noted at that time that there was no evident optimum level for such a limit, but reached the conclusion that 25 per cent was a reasonable level. At present, however, the limitation only applies to (i) covered bonds issued by the counterparty or by an institution with close links to the counterparty and (ii) to other securities issued by a Swedish bank or foreign credit institution.

The Riksbank based its decision in December 2007 on the conclusion that covered bonds, because of their construction, are securities of such good quality that they should be accepted as collateral by the Riksbank even if they are issued by the counterparty or by an institution with close links to the counterparty. However, accepting such securities issued by the counterparty itself entails a greater risk that accepting the same securities issued by another party. The Riksbank therefore decided on an extra haircut in these cases.

The Riksbank now makes the assessment that covered bonds can be accepted to a greater degree than is currently the case without significantly increasing the Riksbank's credit risk. Such a change increases the opportunities for credit in RIX and benefits the functioning of the Swedish money and bond markets. However, the Riksbank still considers it important to strive to achieve a diversification of the collateral volume pledged to the Riksbank by its counterparties. Given this, the limitation should not be entirely withdrawn. The increase in the permitted share that should be made is therefore limited to an increase from 25 per cent to 75 per cent of the total value of the collateral pledged by the counterparty.

The increase in the limitation ought reasonably to refer only to covered bonds issued by the counterparty itself or an institution with close links to the counterparty. This means that for other securities issued by a Swedish bank or a foreign credit institution a maximum share of 25 per cent of the total collateral should continue to apply, as the limitation in this case cannot be assumed to have a negative effect on the functioning of the Swedish money and bond markets.

The change in the limitation should apply until further notice, but the Riksbank will review the rules regarding collateral during autumn 2008 and in this context also examine what rules should apply to this type of concentration in the long term. It is appropriate to carry out a review now given, for instance, the changes regarding collateral implemented or planned by other central banks.

According to the current Rules and Regulations for RIX and monetary policy instruments, the Riksbank must normally submit proposals for changes in the Rules and Regulations to the RIX participants, with a period for consideration of 30 days. The Riksbank must also inform the RIX participants of any changes no later than 15 days before they enter into force. However, the Riksbank may disregard these requirements if special circumstances apply. As this change can only benefit the RIX participants and

taking into account the purpose of the change, such circumstances must be considered to apply. The change should come into effect immediately.

There has been consultation on this matter with the Financial Stability Department, the Monetary Policy Department and the General Secretariat and information on the proposed change has been given to the Executive Board of the Riksbank.

Decision

Given the above it is decided that:

- section 3.1.3 in the Riksbank's guidelines for collateral management will be changed in accordance with Appendix 1,
- the change will enter into force on 22 September 2008, and
- section 3.1.3 in Appendix H4 to the Conditions for RIX and monetary policy instruments be changed in the same way and that this change will come into force at the same time as the Conditions for RIX and monetary policy instruments comes into force.

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