Decision by the Board of the Financial Supervisory Authority regarding the use of macroprudential instruments

By virtue of section 10, subsection 1, paragraph 6 of the Act on the Financial Supervisory Authority (878/2008), the Board of the Financial Supervisory Authority (FIN-FSA) decided at its meeting on 16 March 2015 not to impose a countercyclical capital buffer requirement as referred to in chapter 10, section 4 of the Credit Institutions Act (610/2014).

In addition, at the aforementioned meeting, the Board of the Financial Supervisory Authority also decided not to adopt other macroprudential instruments, i.e. capital requirements for lending secured by residential and commercial immovable property, as referred to in Articles 124 and 164 of Regulation (EU) No 575/2013 of the European Parliament and of the Council on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 *(Capital Requirements Regulation)*, that are higher than the minimum defined in the Regulation, and further decided not to apply Article 458 of the said Regulation.[1]

The decision of the Board was made as proposed by the Director General of the Financial Supervisory Authority. The decision was based on an assessment, jointly prepared by the experts of the Financial Supervisory Authority, the Bank of Finland and the Ministry of Finance, of the need for using macroprudential instruments. Opinions from the Bank of Finland, the Ministry of Finance and the Ministry of Social Affairs and Health supported the decision made today.

Background and main contents of the decision

Cyclical systemic risks

The credit-to-GDP ratio has exceeded its long-term trend. Based on a mere mechanistic interpretation of this indicator, the countercyclical capital buffer requirement for banks should be activated at the level of 0.75%, but the other most important indicators for the setting of this additional requirement – e.g. developments in housing prices, lending and the external balance of the economy – do not signal growth in systemic risks. The trend deviation of the credit-to-GDP ratio is also forecast to decrease in the course of this and next year.

With protracted weak economic activity, credit growth has subsided significantly. Subdued economic trends have reduced risk appetite on the part of both borrowers and banks. In the context of an overall weakness of economic activity, growth in household debt accumulation has slowed,

[1] The said section of the Act also includes the loan-to-value ratio (LTV) as a macroprudential instrument, but it is not due to enter into force until 1 July 2016.

even though the level of indebtedness is considerable. The current low level of interest rates reduces the debt-servicing burden of debtors.

Activity in lending for house purchase and on the housing market has declined from previous years. Real housing prices have been on a moderate downward path in Finland as a whole, but are historically still high. However, based on risk measures, potential over-valuation of housing prices is not significant, Bof.fi > Statistics > Chart gallery > Macroprudential analysis indicators. In addition, on the basis of available indicators, there are no grounds for setting higher capital requirements on lending secured by residential and commercial immovable property than the minimum criteria set out in the Capital Requirements Regulation.

Structural systemic risks

In the Finnish banking sector, there are structural features that could reinforce the systemic effects of risks if these were to materialise. These include, above all, a high degree of concentration, strong Nordic links and high dependence on market-based funding. Even so, banks' risk-weighted capital position clearly exceeds official requirements, and the overall capital adequacy of the banking sector is currently strong.

Capital requirements for banks will tighten significantly this year even in the absence of discretionary decisions on macroprudential instruments. The capital conservation buffer requirement (2.5%, comprised of common equity Tier 1 capital) entered into force in Finland at the beginning of this year. In addition, starting on 1 January 2016, a capital buffer for other systemically important banks will be applied.