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## **Financial stability – timely measures to curb household indebtedness necessary**

Bank of Finland Bulletin 2/2019 press briefing





## Bank of Finland's financial stability assessment

- Annual assessment of the stability of the Finnish financial system and related risks and vulnerabilities
  
- Editorial, financial stability assessment, summary and various feature articles
  - Heavily indebted persons reduce their consumption in response to slowing economic growth
  - A cap on debt-to-income ratio would complement the housing loan cap
  - New tools necessary to curb consumer credit
  - Credit risk of a company dependent on economic cycle and business sector
  - Finnish and foreign commercial real estate markets increasingly interconnected
  - Effects of digitalisation on the profitability of banks
  
- Bank of Finland Bulletin website <https://www.bofbulletin.fi/en/financial-stability/>



## Main topics

- Uncertainties surrounding the global economy are weakening the outlook for the Finnish economy.
- Finland needs to introduce further tools to prevent excessive accumulation of household debt and related risks to the economy.
- The Finnish commercial real estate market is more closely interconnected with the international real estate market.
- The euro area financial architecture must be further reinforced by completing the Banking Union with a common Deposit Insurance Scheme and promoting the Capital Markets Union.

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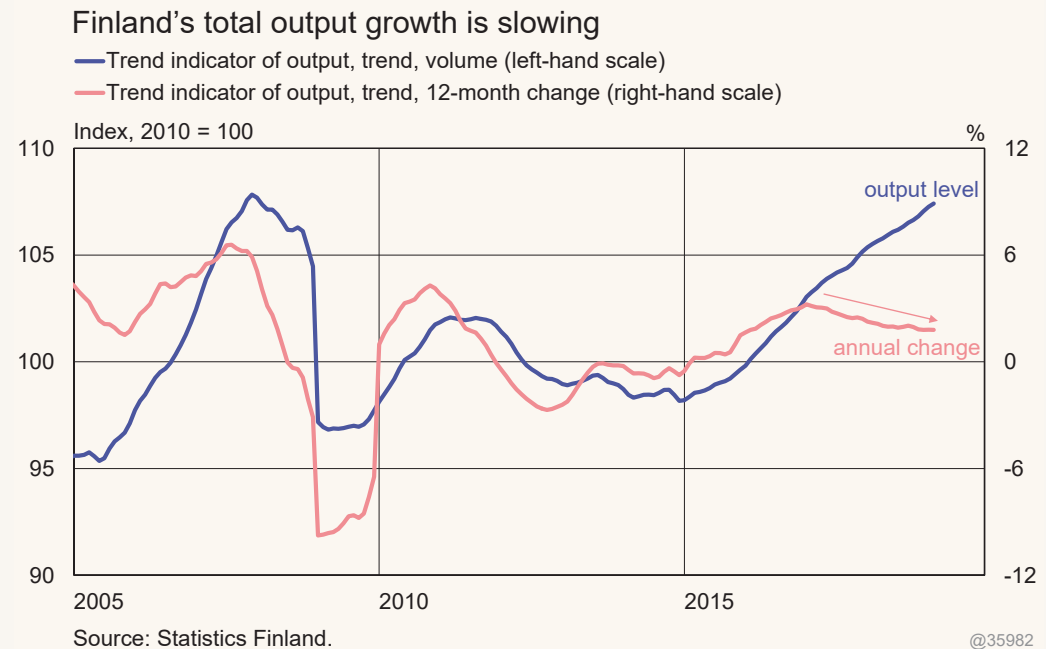
## Uncertainties surrounding the global economy weakening the outlook for the Finnish economy





## Finnish economic growth has slowed and outlook weakened faster than expected

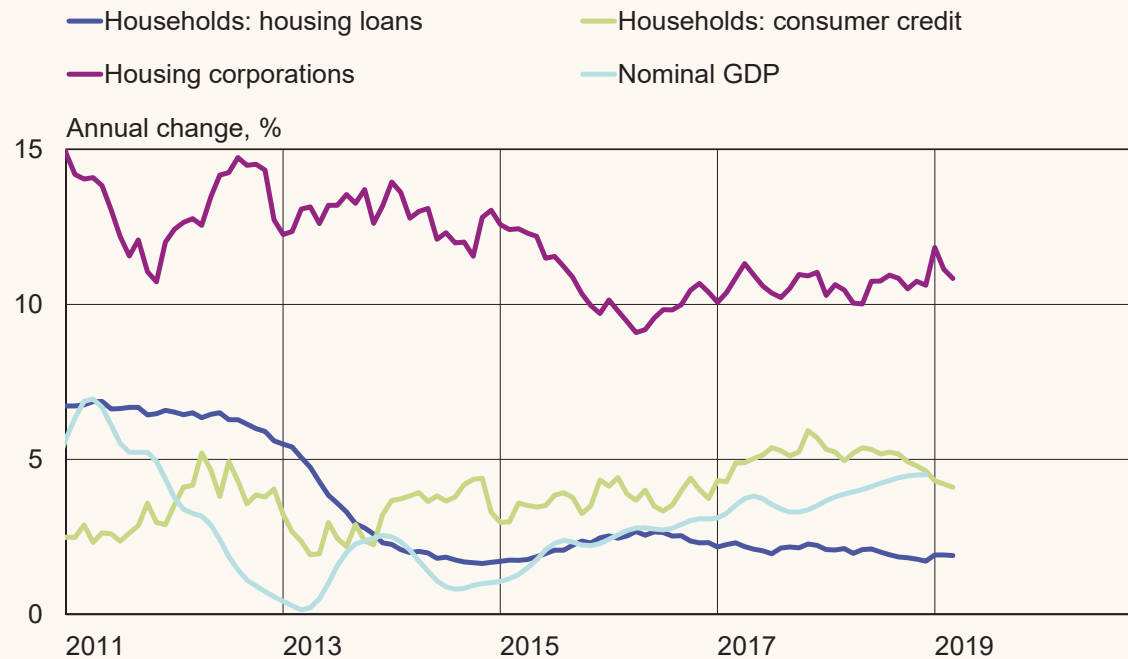
- Uncertainty in the global economy has increased in early 2019.
- Escalation of the trade dispute between the United States and China as well as Brexit pose the biggest risks to the economy in the short term.
- Faster-than-expected weakening of the euro area economic outlook is the biggest downside risk to the Finnish economy.
- Finnish economic growth is increasingly dependent on domestic demand.





## Loans to housing corporations and consumer credits have increased rapidly, driven by construction and consumption

Credit institutions' loan stock and GDP



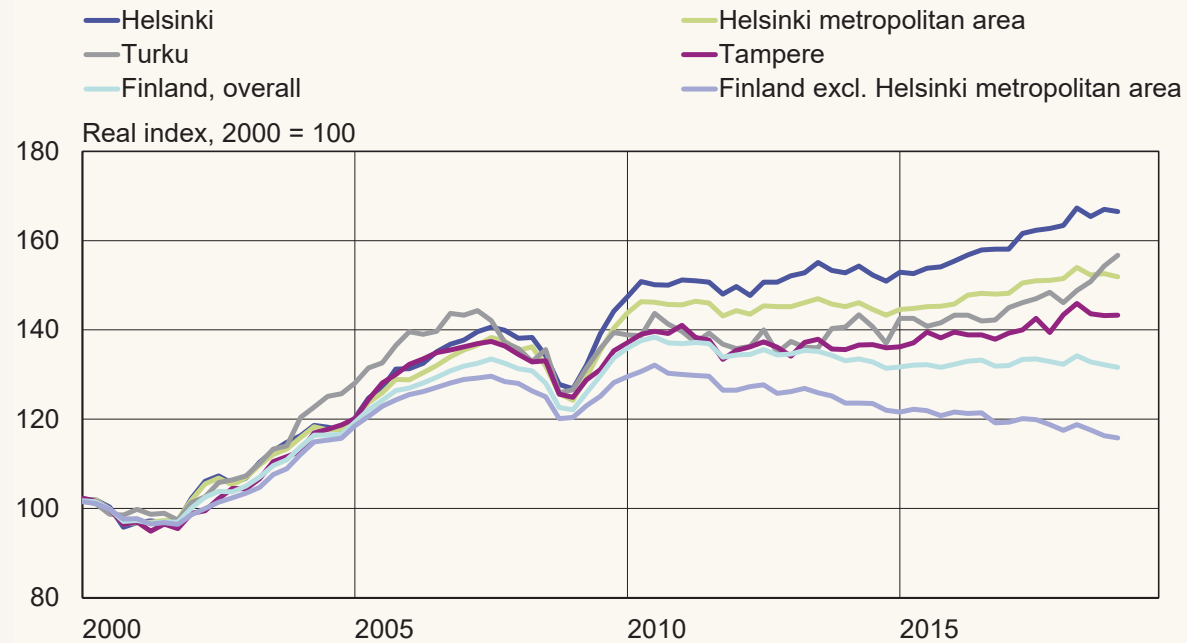
Sources: Statistics Finland and Bank of Finland.

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## Growth in house prices mostly moderate, while regional price divergence continues to widen

Regional disparities in prices of old dwellings have increased in the 2010s



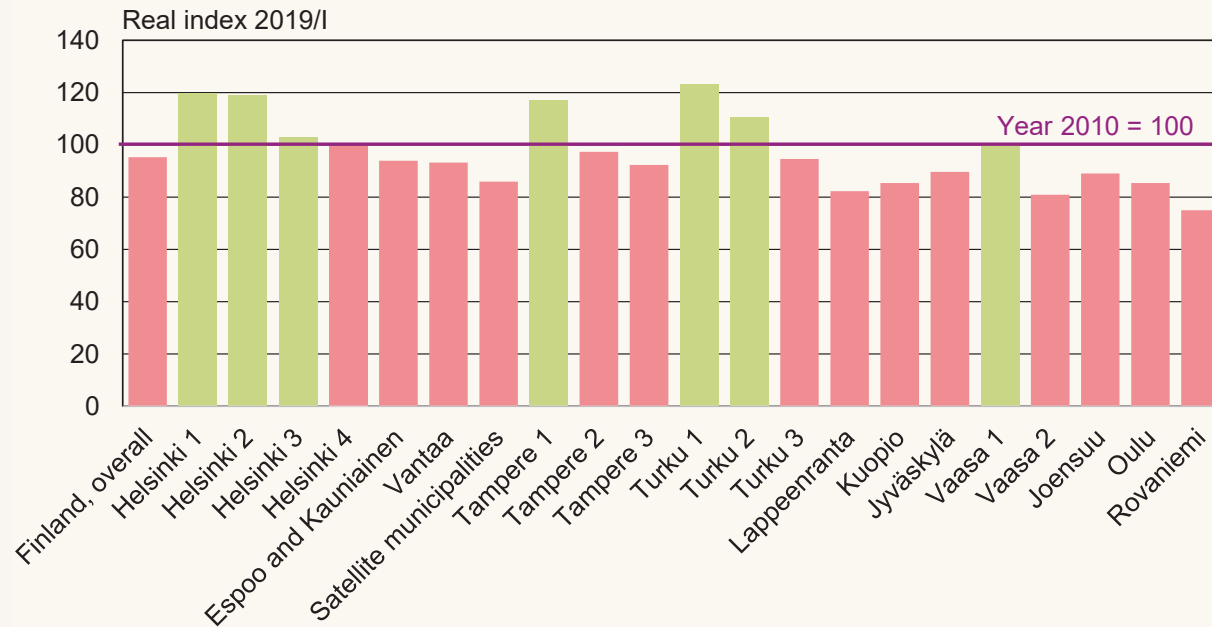
Source: Statistics Finland.

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## Real house prices have increased only in a few city centres

Prices of old dwellings in housing companies relative to the situation in 2010 in selected cities



Sources: Statistics Finland.

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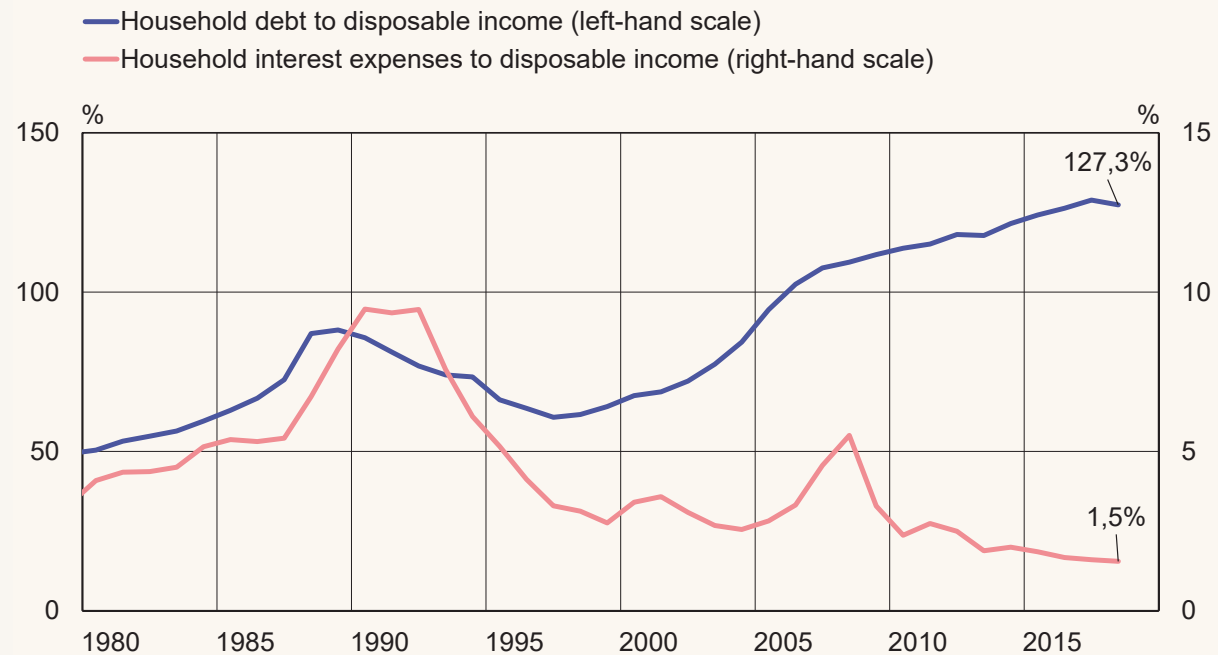
## **Finland needs to introduce further tools to prevent excessive accumulation of household debt and related risks to the economy**





# Excessive household indebtedness must not be allowed to jeopardise stable economic growth

Household indebtedness in Finland



Sources: Statistics Finland and calculations by the Bank of Finland.

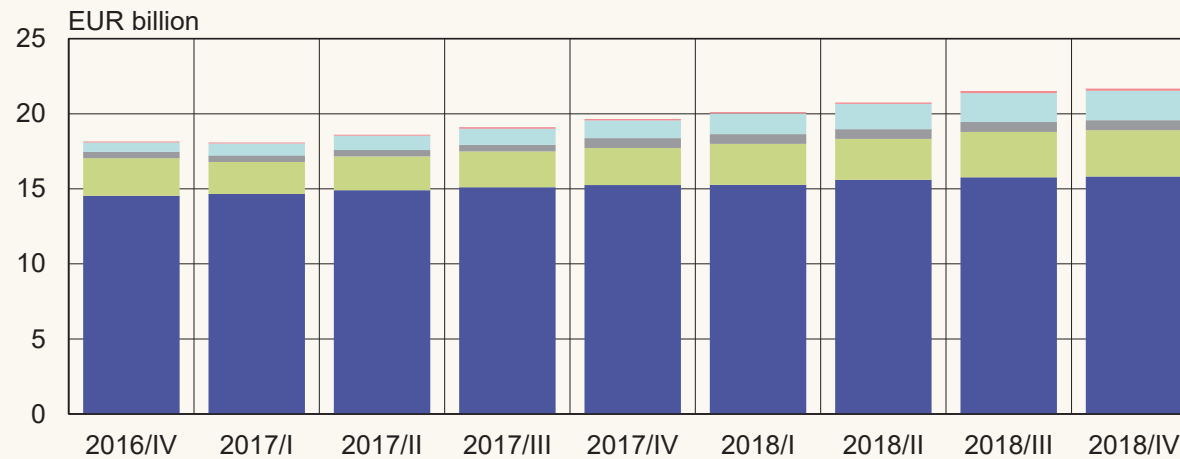
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## Consumer credit lending outside the banking sector is growing

Households' consumer credit stock estimated at almost EUR 22 bn

- Peer-to-peer lending
- Foreign credit institutions lending cross-border
- Small-loan companies
- Other financial institutions excl. small-loan companies
- Credit institutions



Sources: Bank of Finland, Statistics Finland, Ministry of Finance, Sweden's Riksbank, financial statements and consumer credit lenders' published data. @35982



## Indebted households prone to reduce consumption, which may aggravate problems in economy as a whole



Source: Bank of Finland.

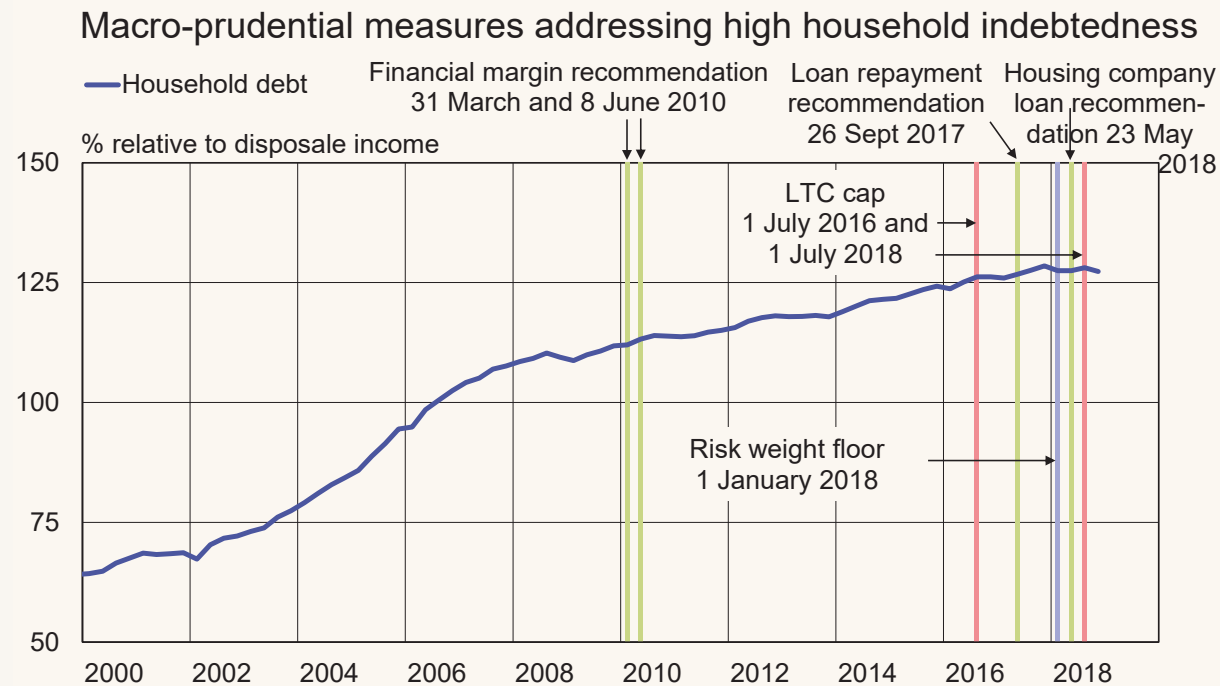


## Macroprudential policy supports long-term economic growth

- The objective is to reduce the probability of financial crises and their adverse effects on the real economy.
- Financial stability improves the conditions for economic growth in the long term.
- Macroprudential instruments particularly aim to mitigate excessive credit growth and debt accumulation and related risks to the economy.



# Household indebtedness at historically high level



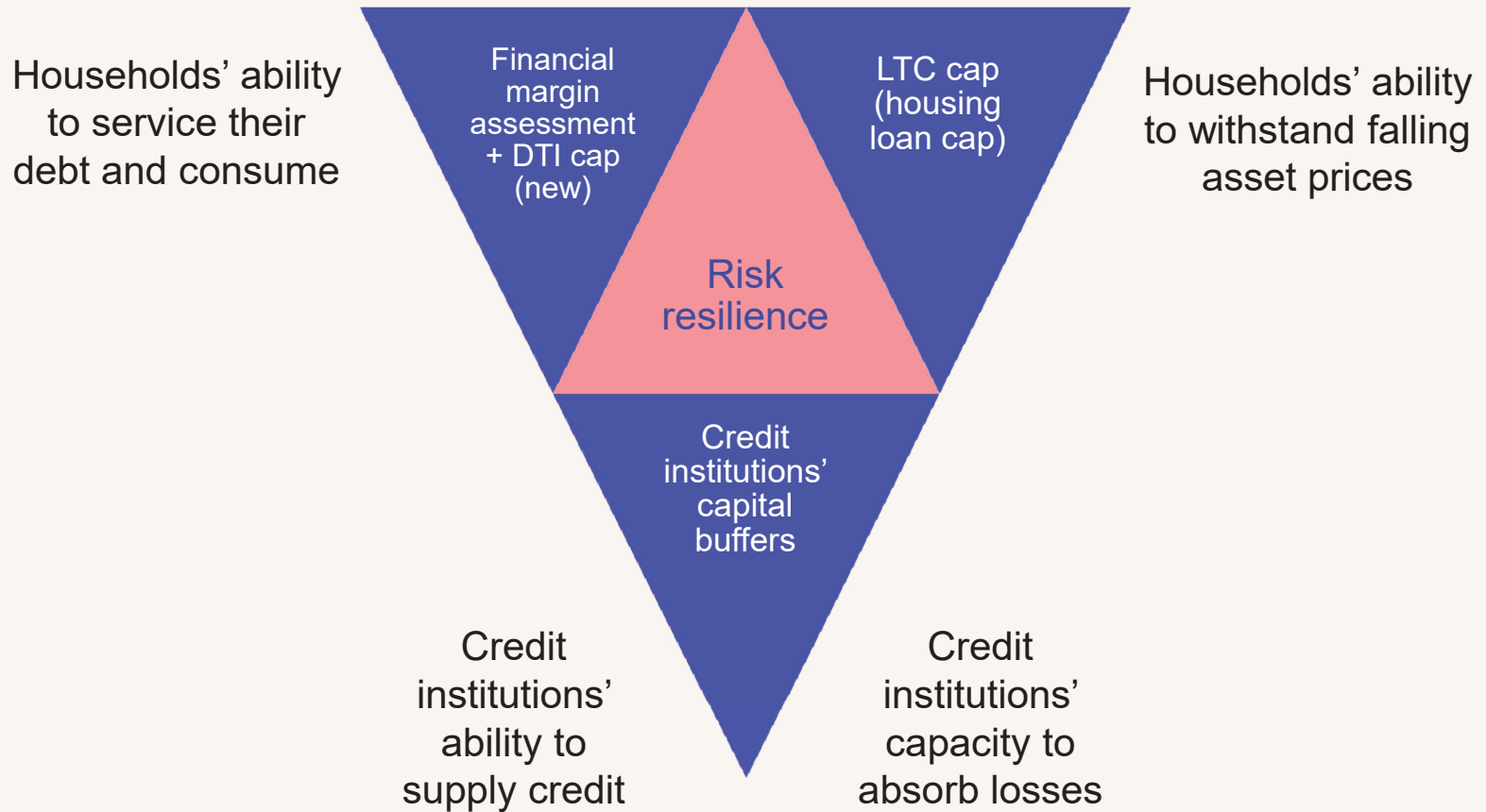
Vertical lines: Effective date of the macroprudential measure in question.

Sources: Statistics Finland and Bank of Finland.

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## Macroprudential policy needs complementary measures





## Macroprudential tools should also be extended outside the credit institutions sector

- Debt-to-income cap: limits the ratio of total debt to income
- Maximum maturity of housing loans and housing company loans
- Maximum share of housing company loan in loans for the purchase of new-build dwelling, and loan amortisation requirement
- Amortisation requirement for consumer credit and more extensive supervision



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## The Finnish commercial real estate market more closely interconnected with the international real estate market





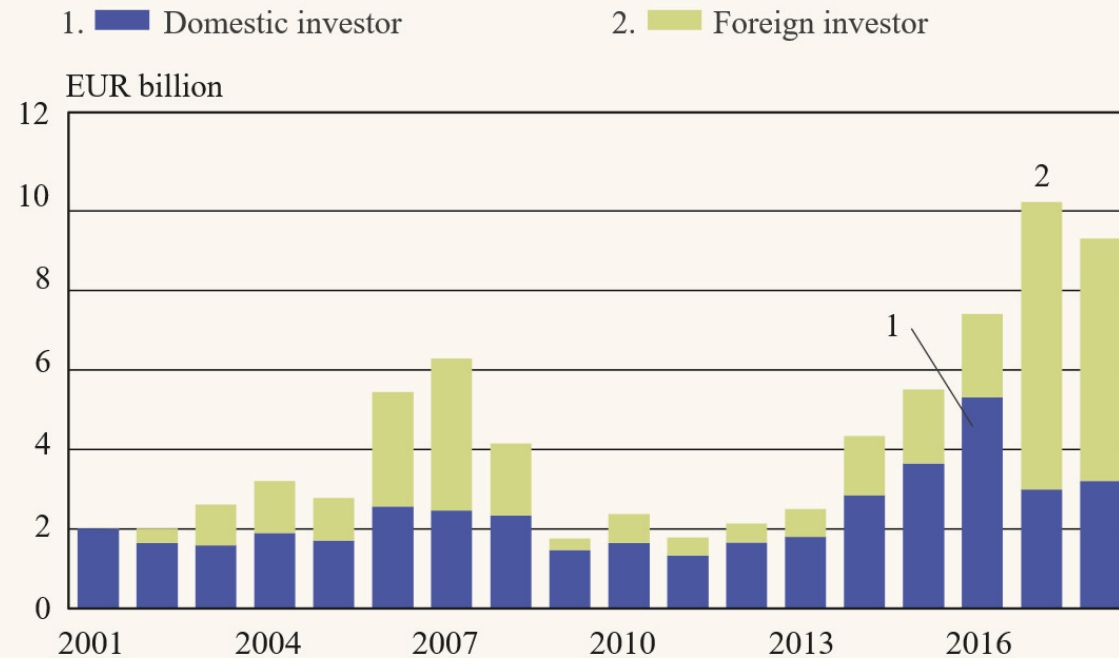
## Finnish real estate market increasingly vulnerable to international risks

- Prices up, total volume of transactions higher and international investors more active on the Finnish real estate market
- Because of foreign investors, the Finnish real estate investment market is more exposed to cyclical fluctuations in the European real estate market.
- Weakening of the international market or business cycle could also strengthen the volatility of real estate prices in Finland.



# Foreign investors participate more often in large real estate transactions in Finland

Volume of major real estate transactions in Finland



Source: KTI Property Information Ltd.



## Structural changes in Finland's commercial real estate market

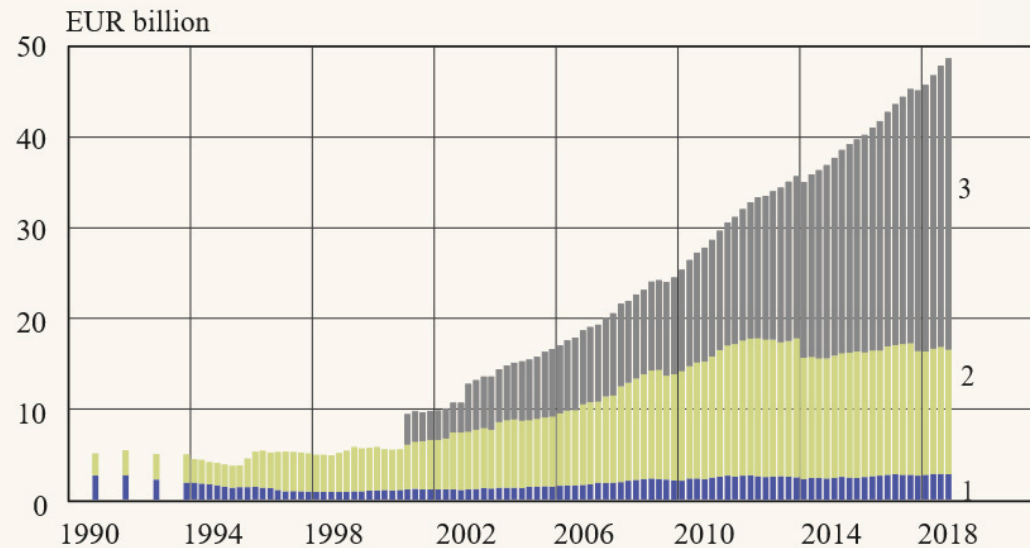
- Urbanisation and the favourable economic situation have boosted the construction of commercial and office properties in growth centres.
- Investors have also increased their holdings of rental housing.
- Urbanisation and digitalisation decrease particularly the demand for commercial and office properties located outside city centres.
- The growth in e-commerce and changes in consumer behaviour present a challenge to shopping centres.



## Domestic banks' real estate-related loan stock grown rapidly in past 20 years

The stock of loans exposed to real-estate risk has grown rapidly in recent decades

- 1. Construction, loans
- 2. Real estate sector, loans
- 3. Housing corporation loans



Sources: Bank of Finland and Statistic Finland.

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**The euro area financial architecture must be further reinforced by completing the Banking Union and promoting the Capital Markets Union**





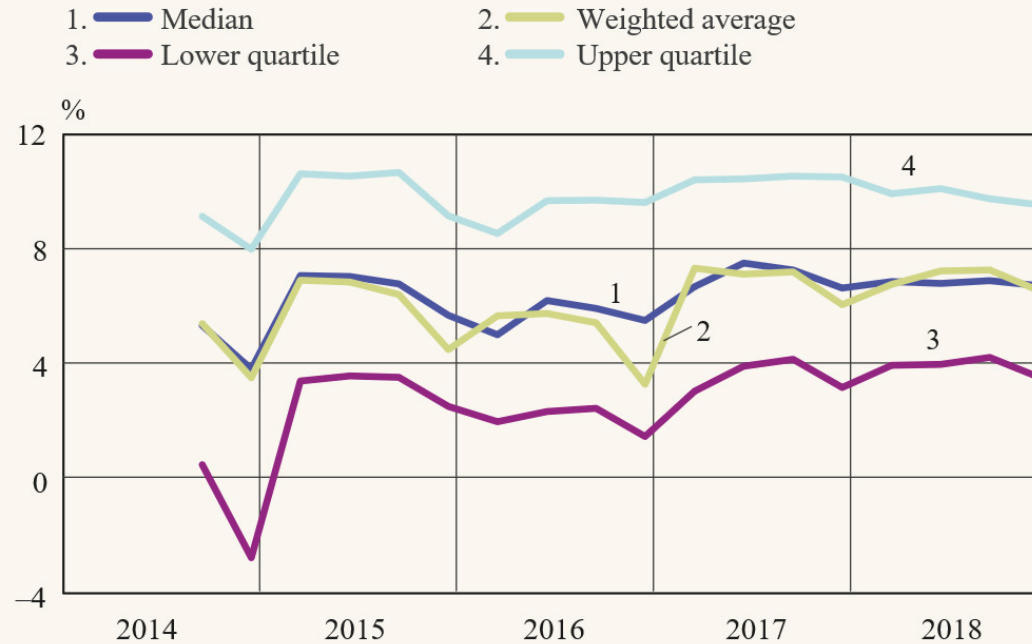
## Nordea's redomiciliation increased interconnectedness between Finnish and other Nordic banking sectors

- The banking sector's size, degree of concentration and interconnectedness increased as Nordea transferred its domicile to Finland.
- The banking system's strong capital and liquidity position ensure the sector's loss-absorbing capacity and lending capacity under all circumstances.
- The Nordic and Baltic authorities conducted in January 2019 a joint banking crisis simulation exercise.



## Subdued outlook for profitability in European banking sector

Major European banks' return on equity (ROE) has improved only slightly in recent years



Source: European Banking Authority (EBA).





## The resilience of the euro area's financial system must be reinforced further

- Banks' exposures to national sovereigns should be reduced further.
- Banking Union should be completed with a common Deposit Insurance Scheme.
- More determined action should be taken to dismantle the barriers to integration of the capital markets, and the EU's Capital Markets Union initiatives should be promoted.



**Thank you!**