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Biggest threats to financial stability are from outside Finland

21 May 2025 – Simply Short – Financial stability

Finland's financial system has remained stable despite the increase in global risks that are hard to predict. The trade tariffs imposed around the world by the United States are shaking the global economy and investment markets, and Russia's war in Ukraine is undermining security in Europe. To guard against unforeseeable crises, the authorities in Finland should be allowed to ensure that Finnish banks accumulate buffers against such situations in a new way. Lending to households must continue to be on a sound basis. Finland and Europe must also ensure that businesses have access to a broader range of options for financing their investments.

Risks to financial stability are growing due to global power politics Releasable capital buffers needed for banks' resilience against unforeseeable crises
Europe must focus on attracting investments and growth-oriented businesses

Increase in global risks that are hard to predict

Finland's banking sector and entire financial system have remained stable despite the recent unpredictability of the global environment. Households and businesses have, for the most part, successfully coped with the regular payments of their loans, but are cautious about taking on any new loans. Nevertheless, the lowering of interest rates is easing debt repayment, and this may encourage further borrowing. This would gradually revive housing sales and professional real estate investment.

The risks in the global economy grew considerably in the early part of 2025. In particular, geopolitical risks and the rapid shifts in trade and foreign policy are casting gloom over the near-term outlook and adding to uncertainty in the economy. The threat of an expansive trade war is overshadowing the global economy, and Russia's war in Ukraine is undermining security in Europe. If confidence, consumption, investment and exports suffer, this will slow the Finnish economy's revival.

The trade tariffs imposed by the United States on its imports of goods and raw materials generated considerable turbulence in global financial markets in early April. Investors took the view that the tariffs will harm the global economy and increase the risk of a recession. Although the US has postponed some of the tariffs, the exceptional uncertainty is affecting the economic outlook and raising the question of whether international cooperation can be relied on.

The growth in risks that are hard to assess has been evident in investment markets, for example in the form of unusually high volatility in the demand for shares and in share prices. Major investors have transferred some of their assets to investments that can be quickly converted to cash, such as low-risk government bonds. The financial markets have remained sound, but a detrimental spiral could emerge if investors avoid risk-taking and there is a shortage of good collateral.

If global economic growth falters and concern remains high in financial markets, the scenarios for Finland would also grow dimmer. The risks to the economy and for banks and investors could grow. They could materialise if, for example, the revival in the housing and real estate market slows, the construction sector recovery is further delayed, a significant worsening occurs in the situation of manufacturers exporting goods to the United States, or unemployment continues to rise.

Chart 1.

Releasable capital buffers needed for banks' resilience against crises

Although the world is churning, Finnish banks have stayed in good shape. A contributory factor in this is that the regulation and supervision of banks has worked well. The Finnish Financial Supervisory Authority (FIN-FSA) has strengthened the ability of Finnish banks to withstand losses by ensuring that they have at least a certain minimum level of their own funds, or equity, in relation to the risks associated with their activities.

The FIN-FSA has calibrated these requirements for banks' additional capital on the basis of the Finnish financial system's long-term vulnerabilities that are independent of cyclical fluctuations. Among these vulnerabilities are the current situation in which the entire banking sector and individual major banks play a very important role in the national economy and in financial and payment services.

The increase in global risks must also be taken into account in the regulation of the banking sector. In Finland, the capital requirements applying to banks are not as diverse in all respects as in many other European countries. In contrast to Finland, in many European countries the countercyclical capital buffer (CCyB) requirement can be imposed on banks even during 'fair weather', before there are signs of an increase in risks.

An advantage of this proactive use of the CCyB requirement is that the authorities can correspondingly reduce this requirement during a downturn or crisis. In this case the banks would quickly have these funds available in a situation where losses could deplete their equity. This would maintain the ability of banks to grant loans to households and businesses, which could alleviate the crisis and ease the subsequent recovery.

In Finland, the FIN-FSA can impose on banks a CCyB requirement only if bank lending is at risk of first overheating, and the requirement can be released later as necessary. The proactive use of this requirement in normal cyclical conditions is permitted in many

European countries and should be allowed in Finland too. This would enable such a capital buffer to be accumulated and used more flexibly than at present. It would therefore improve preparedness for unexpected economic and financial shocks originating from outside the Finnish banking sector.

Authorities and legislators must ensure that sound practices are maintained for lending by banks and other lenders and for debt accumulation by households. Finland has made determined and sustained efforts towards this by curbing particularly high-risk borrowing. The Government's intended loosening of the statutory restrictions concerning mortgages and housing company loans, announced in April, would be a step backwards in this important work.

Capital market growth in Finland and Europe would support investment

Capital markets are markets in which governments, banks, businesses and others can obtain long-term financing from different investors. Trading in, for instance, shares and debt securities also takes place in capital markets. Finland's capital markets are, overall, more developed than in the EU countries on average. The greatest need for further development in Finland's capital markets concerns the access to finance from private equity investors by businesses looking to invest or grow.

There is an abundance of risk financing from private equity investors in Finland for small businesses starting up who may find it difficult to borrow from banks. However, larger and more established businesses that are seeking rapid growth and international expansion have a need for a broader range of financing options. These businesses need equity investment and other forms of equity financing, in particular.

The operation of the capital markets must be furthered by concrete efforts throughout Europe, as we are lagging behind in this by comparison with economies such as the United States. In March, the European Commission published its plans for a Savings and Investments Union (SIU). The aim is to improve the way savings are channelled to productive investments, fostering growth in the economy. These plans are now even more important in the current difficult global environment where economic challenges are being posed by tensions between major economies and by climate change and technological advances, which require substantial investment in Europe.

Growth in the capital markets would improve Europe's competitiveness and its strategic autonomy from other economies such as China and the United States. Europe's financial markets need more securities that are popular with investors, which means low-risk securities that are attractive and safe. Defence spending will increase in the next few years, which may boost the supply of safe government bonds in Europe as governments seek to expand their borrowing. At the same time, it will be important for governments to ensure that their debt expansion does not grow to an unsustainable level that would diminish creditworthiness.

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