Policy

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RESPONSIBLE DEPARTMENT:	Financial Stability Department
ADMINISTRATIVE	Head of the Financial Stability Department
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Policy for pricing of Emergency Liquidity Assistance

If the Riksbank provides Emergency Liquidity Assistance (ELA), the interest rate charged will include a mark-up, the size of which is determined by the specific circumstances in each case.[1] The following principles shall apply when calculating the interest rate mark-up:

I. The interest rate shall be high enough to ensure that the institution receiving ELA does not gain an advantage from it in relation to other institutions. The interest rate shall hence be higher than the rate at which other comparable institutions can borrow on the market.[2]

II. The interest rate shall compensate the Riksbank for the credit risk associated with the lending. The credit risk is determined based partly on the counterparty risk, i.e. the risk of the counterparty not being able to repay its debts and the risk of changes in the value of the collateral received by the Riksbank.

III. The interest rate shall also reflect the type of event that has given rise to the ELA. In particular, the Riksbank shall consider how the risks in the institution's operations – for example credit risk, market and liquidity risk, as well as operational risk – have created the need for liquidity assistance. These risks then form the basis of the assessment of the Riksbank's credit risk in conjunction with the liquidity assistance. Liquidity risks are of particular importance in this context. If the institution has historically had an insufficient Liquidity Coverage Ratio (LCR) in any significant currency or mismanaged its liquidity risks in some other way,

[1] In addition to the interest rate, the haircuts applied to the collateral received by the Riksbank can be changed.
[2] "Institution" refers here to a banking institution in accordance with Chapter 6, Article 1, first paragraph of the Sveriges Riksbank Act and to a Swedish company under the supervision of Finansinspektionen, see Chapter 6, Article 8 of the Sveriges Riksbank Act.

the interest rate shall be set higher.[3] Insufficient liquidity coverage means an LCR level that has historically been below 100 per cent. This level is compatible with the minimum level according to the Basel Accord and the European regulatory framework.[4]

Background

Liquidity problems in the banking sector can cause financial instability and disrupt the monetary policy transmission mechanism, resulting in negative effects on the economy. To combat these problems, the Riksbank may, under Chapter 6, Article 8 of the Sveriges Riksbank Act, provide ELA on special terms and conditions to banks and certain other institutions under the supervision of Finansinspektionen. This also implies that the risk-taking of banks and other institutions can affect the Riksbank's balance sheet and its credit risk in that they are or may become counterparties to the Riksbank.

This policy aims to clarify in advance the principles to be employed when the Riksbank prices such ELA. Institutions being granted ELA must not gain an advantage over other institutions as a result, which means that the interest rate shall be higher than the level at which comparable institutions can borrow on the market. The pricing policy can thereby reduce the potentially distorting effects of ELA on competition.

How banks and other institutions manage liquidity risks under normal circumstances affects the likelihood of them having problems and hence requiring ELA. With a clear policy for ELA, the Riksbank can reduce the incentives of banks and other institutions to take large liquidity risks. Ultimately, the policy can thereby reduce the Riksbank's credit risk in its role as Lender of Last Resort.

[3] A significant currency is a currency that comprises more than five per cent of a bank's total liabilities, according to the Basel Accord and European Commission Delegated Regulation (EU) 2015/61 on LCR. The proportion of funding in a specific currency can vary over time as can therefore the currencies classified as significant in accordance with this definition.

[4] See "Basel III. The Liquidity Coverage Ratio and liquidity risk monitoring tools", Basel Committee on Banking Supervision, January 2013 and "Commission Delegated Regulation 2015/61", October 2014.