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Statement of opinion with regard to Nordea Bank AB's application for permission to implement merger plans

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Summary

A relocation of Nordea's corporate residence to Finland will not affect the bank's operations or customers in Sweden to any great degree. Nordea will remain one of the most important banks in Sweden. A relocation may nevertheless have significant consequences for the Swedish financial system and for Swedish financial stability. A condition for a relocation not to lead to increased risks that may threaten financial stability is that Nordea's capital and liquidity requirements do not become lower.

A direct consequence of a relocation is that the main responsibility for supervision, regulation, crisis management, resolution, deposit insurance and liquidity support moves from Sweden to different authorities within the banking union, in this case European authorities (the European Central Bank, ECB, and the Single Resolution Board, SRB) and Finnish authorities (Bank of Finland, the Finnish supervisory authority, and the Finnish Financial Stability Authority, RVV). Thus, related costs will no longer be incurred by Sweden. In a formal sense, therefore, this reduces Sweden's financial commitments. At the same time, however, Swedish influence over, and insight into, Nordea's operations also diminishes.

In the long term, once the European banking union is fully developed, the risks to Sweden could decrease as a result of the Nordea relocation. Centralised European supervision could enable more intensive supervision of Nordea with greater resources, less person-dependence and less "home bias". A European responsibility for crisis management also enables greater risk diversification and risk distribution for an individual country. A fully developed, efficient banking union, with effective risk sharing among participating countries, could therefore lead to lower risks for Sweden as well. This presupposes, however, that the banking union is completed.

In the short term, the risk outlook is more complex. Until the banking union is complete, much of the ultimate risk still has to be borne by the home country – Finland in Nordea's case. In a completed banking union, the costs of managing a troubled major bank are supposed to be covered by shareholders and creditors, and a single resolution fund and deposit guarantee. However, the currently limited risk sharing within the banking union and thereby Finland's increased responsibility may affect the scope for effectively dealing

with a crisis, as the Finnish economy is smaller than the Swedish economy. Confidence in crisis measures may also be negatively affected as the Finnish deposit guarantee system has a lower coverage ratio than its Swedish equivalent. This applies even though there is scope to write down private debt in the event of a crisis.

Against this background, it is of utmost importance that the requirements imposed on Nordea are not lowered. For several years, Swedish authorities have set stricter requirements for Swedish banks than what is stipulated as European minimum levels in order to safeguard financial stability. The reasons for this, among other things, are that the Swedish banking system is concentrated and has a large amount of foreign wholesale funding. The stricter requirements for Nordea include capital requirements, liquidity requirements and requirements regarding eligible liabilities. As Nordea's risks will not be affected by the relocation, it is the Riksbank's opinion that these requirements should not be lowered. It is also unfortunate as a matter of principle if a bank can lower its requirements by changing its corporate residence, as this creates the wrong incentive for banks.

To ensure that the risks in Nordea's operations are limited and financial stability is maintained, it is also important to continue to intensify the cooperation between Swedish authorities and the authorities that will take over the responsibility for Nordea. Natural forums for this cooperation are the supervisory and resolution colleges as well as central bank cooperation. Furthermore, it is important that such cooperation considers national knowledge and national conditions, especially as the share of Nordea's operations that will be within the banking union is relatively small – approximately 75 per cent of Nordea's operations will instead be in countries outside the banking union. Deeper cooperation includes everything from risk assessments to preparations for measures in the event of a crisis. It also includes questions regarding how to transfer and recognise the macroprudential policy measures of different countries in order to safeguard financial stability, offset imbalances and allow banks in the same country to operate under similar conditions to prevent unfair competition.

The Riksbank's overall assessment is that the risks to financial stability will increase slightly in the short term, which is why the Riksbank considers it to be a precondition for the relocation that Nordea's capital and liquidity requirements are not reduced. The Riksbank also considers it important that all banks in Sweden, including Nordea, continue to have liquidity requirements in all significant currencies, in order to counteract short-term liquidity risks. The Riksbank further notes that a relocation means that the responsibility for supplying liquidity in a crisis will move to the Bank of Finland, which will be expected to deal with any application for emergency liquidity assistance from Nordea. This responsibility includes the bank's foreign branches and also applies to any possible liquidity in Swedish kronor. Finally, the Riksbank notes that Nordea is a key player within the Swedish financial infrastructure, including RIX, but that there is no reason to believe that a relocation will in itself change Nordea's role within the financial infrastructure in Sweden.

1. Background

In September 2017, the Board of Directors of Nordea Bank AB (Nordea) made the decision to move the parent company to Finland and thereby to the European Union's (EU's) banking union. The decision to move the parent company was preceded by a

decision to convert Nordea's subsidiaries in Finland, Denmark and Norway into branches of Swedish Nordea. This transformation into a branch structure entered into force on 1 January 2017.¹ Nordea's annual general meeting in March 2018 consequently approved the relocation plans. The move is planned as a reverse cross-border merger, in which the parent company is incorporated with a newly established Finnish subsidiary. Nordea plans to carry out the relocation on 1 October this year, assuming that the ECB approves the application for a bank licence for the newly-established Finnish subsidiary and that Finansinspektionen (FI) approves the merger application. The license application was submitted to the ECB in December last year and a decision is expected in June this year. The merger application was submitted to FI on 22 March this year and a decision is expected during the third quarter of 2018.

On 2 May 2018, the Riksbank received Nordea's merger application from FI for comments. Specifically, FI asked for the Riksbank's views on the following three questions:

- 1) *In view of the Riksbank's mandate, are there any crucial objections to granting Nordea's application based on the so called public interest as well as creditor interest perspectives that Finansinspektionen is to take into consideration when assessing the application?*
- 2) *To what extent can the Riksbank offer different forms of extraordinary liquidity support measures to Nordea if the merger is realised in line with the application?*
- 3) *What is the Riksbank's view as regards to whether, and if so how, the public interest will be affected by Nordea's relocation in light of Nordea's various roles in Swedish financial market infrastructures and payment systems?*

Section 2 aims to explain the effect of a relocation of Nordea to Finland on the Swedish banking system and the allocation of responsibility between authorities and the Riksbank's areas of responsibility. Section 2 then forms the basis for Section 3, in which the Riksbank responds to FI's specific questions. In Section 4, the Riksbank's main conclusions are presented.

2. Implications of a relocation of Nordea to Finland for the Swedish banking system, allocation of responsibility between authorities and the Riksbank's role as liquidity provider

A relocation of Nordea to Finland may have significant consequences for the Swedish financial system and for Swedish financial stability. The part of the Swedish banking system under Swedish responsibility will be significantly reduced. Not only Sweden's formal commitments and responsibilities towards, but also its oversight and control of, the Nordea group, including the new Swedish branch, will decrease significantly as a result of a relocation. The main rule for supervision, resolution and deposit guarantee is home country responsibility, which means that ECB/the Single Supervisory Mechanism (SSM) and SRB will take over the main responsibility for Nordea as a result of the move.

¹ See the Riksbank's statement of opinion to Finansinspektionen from 12 April 2016 regarding Nordea's application for permission to transform its operations from a subsidiary structure to a branch structure, http://archive.riksbank.se/Documents/Remisser/2016/remiss_FI_160413_eng.pdf.

A relocation of Nordea to Finland will also have consequences for the Riksbank due to Nordea's role as RIX participant and monetary policy counterparty, and for the Riksbank's liquidity support.

At the same time, however, Nordea's actual operations will remain in Sweden, as will the risks associated with concentration and interconnectedness in the Swedish banking system.

Concentration and interconnectedness in the Swedish banking system will remain

The Swedish banking system's total assets currently correspond to around 400 per cent of GDP.² The banking system is concentrated, with the four major banks responsible for about 80 per cent of lending to households and companies. It is also interconnected, partly as a result of the major banks' significant holdings of each other's securities. This concentration and interconnectedness exposes vulnerabilities, as problems in one bank can quickly spread to the other banks. All four major banks also have significant operations outside the Swedish home market. A relocation of Nordea to Finland would reduce the assets in the Swedish banking system to around 300 per cent of Sweden's GDP. The Swedish banking system would thus remain large in relation to Sweden's economy. At the same time, Finland's banking system will increase in size, from around 200 per cent to about 400 per cent of Finland's GDP.³

Nordea is currently one of the largest players in Sweden. Around 35 per cent of Nordea's total lending is to households and companies in Sweden.⁴ Nordea's share of the Swedish banking system's total assets amounts to around 30 per cent, relatively evenly distributed between lending to companies and households. After a relocation, Nordea will continue to conduct operations in Sweden in the form of a newly opened branch, as well as through its five existing subsidiaries.⁵ After a move, Nordea's share of the Swedish banking system's assets is expected to decrease to less than 10 per cent. Nordea's de facto operations in Sweden will, however, remain largely the same as they are today, which means that the risks related to concentration and interconnectedness will also remain.

The vulnerabilities posed by interconnectedness are particularly obvious in the case of Nordea as the bank has major exposures over the entire Nordic region. This is illustrated in Figure 1, which shows that, after a relocation, about three-quarters of Nordea's assets would still be outside the banking union, in Sweden, Denmark and Norway. The banking union will thereby also have a dominant role in the banking systems of several host countries outside the banking union itself.

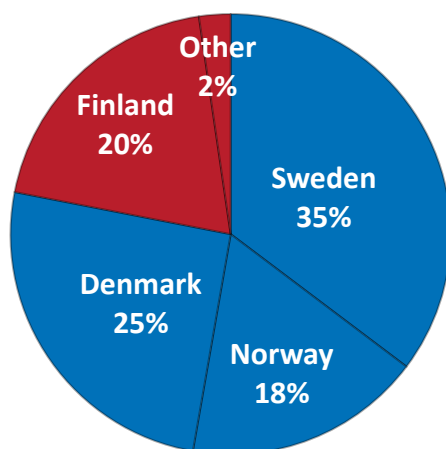
² The term 'the Swedish banking system' refers to monetary financial institutions (MFIs) according to Statistics Sweden's definition and corresponds to total bank assets in Sweden, including both bank branches and subsidiaries under foreign management that are active in Sweden, as well as Swedish banks' branches abroad.

³ The figure of 200 per cent includes Nordea's current Finnish branch and the figure of 400 per cent includes the entire Nordea group, i.e. including foreign subsidiaries.

⁴ That is, lending booked in Sweden.

⁵ Nordea's Swedish subsidiaries include Nordea Hypotek AB, Nordea Finans Sverige AB, Nordea Investment Management AB, Nordea Asset Management Holding AB and Nordea Livförsäkring Sverige AB (part of Nordea Life Holding). None of these subsidiaries are funded through deposits.

Figure 1: Nordea's total lending, December 2017



Note. Refers to where the loans are booked.
Source: Nordea

The main rule for supervision, resolution and deposit guarantee is home country responsibility

The Swedish authorities – FI and the Swedish National Debt Office – will have the status of host authority for Nordea instead of home authority and hence a significantly more limited role in various supervisory and resolution decisions. As Nordea to all intents and purposes will come under ECB/SSM supervision, capital and liquidity requirements will be based on the enforcement of regulations applicable in the banking union. The issue of reciprocity will be an important factor in FI's ability to conduct effective macroprudential policy. The responsibility for resolution planning for the Nordea group will be transferred from the Swedish National Debt Office to the SRB in the event of a relocation. The Finnish authorities will assume responsibility for the deposit guarantee system as there is still no joint deposit insurance scheme on the banking union level.

The ECB will assume responsibility for microprudential supervision

At present, FI has the main responsibility for the Nordea group's microprudential supervision, including chairmanship of Nordea's supervisory college.⁶ The ECB and the Finnish financial supervisory authority are members of the college, as they currently exercise supervision of Nordea's Finnish branch and Finnish subsidiaries, respectively.

Following a relocation of Nordea's head office to Finland, the ECB will assume responsibility for Nordea's microprudential supervision, including for the new Swedish branch, given its supervisory responsibility for the banking union's significant banking groups (about 118 banking groups at present).⁷ Within the SSM, joint supervisory groups are responsible for the day-to-day supervision of all significant banks. These supervisory groups are made up of staff from the ECB and national supervisory authorities that are members of SSM. The aim is

⁶ For banks with operations both within and outside of the banking union, supervision is conducted via 'supervisory colleges' made up of the supervisory authorities in the countries in which the banking group has operations.

⁷ The criteria for significant banks are reported in Council Regulation (EU) 1024/2013, as well as in ECB Regulation 468/2014.

over time to develop a uniform supervisory culture, with consensus regarding the assessment of risks, methods and processes.

FI will continue to be the supervisory authority for and take decisions regarding the Swedish subsidiaries, including Nordea Hypotek AB. A relocation of Nordea's headquarter will not affect the supervisory college other than that there will be a redistribution of roles, where ECB will assume the chairmanship while FI, due to being supervisor for the Swedish subsidiaries, will be a member. As supervisory authority for the Swedish subsidiaries, FI will be involved in and make decisions regarding, for example, capital and liquidity, for the entire group. If the supervisory authorities are not in agreement, however, decisions applicable to the group will be made by the ECB.

Finland will assume responsibility for macroprudential supervision

If Nordea relocates to Finland, the Finnish supervisory authority will become responsible for the bank's macroprudential policy, including for Nordea's branch in Sweden. This means that several of the macroprudential policy measures introduced by the Finnish supervisory authority will also apply to Nordea's branch in Sweden. The Governing Council of the ECB can also set higher macroprudential policy requirements ("topping-up") than national authorities do.

Macroprudential measures founded on consumer protection, such as the loan-to-value limit and amortisation requirements, will also apply to Nordea's branch in Sweden in the future as they are based on national legislation. On the other hand, other macroprudential measures adopted in Sweden to safeguard Sweden's financial stability, such as FI's risk-weight floor for mortgages, will not automatically apply to Nordea's branch in Sweden. For this to be the case, reciprocity is required from the Finnish supervisory authority. It is therefore important to ensure good cooperation among different national authorities on macroprudential policy issues.

Capital requirements

Nordea is currently subject to Swedish capital requirement regulations and the bank's Common Equity Tier 1 (CET1) requirement amounts to 17.5 per cent of risk-weighted assets. It is only the minimum requirement and the capital conservation buffer (corresponding to a total of 7 per cent of risk-weighted assets) that constitute internationally agreed requirements, Nordea's other CET1 requirements are Swedish special requirements (Table 1). Since 2012, when the framework for global systemically important banks (G-SIBs) was introduced, Nordea has been classified as a G-SIB, which entails a supplementary CET1 requirement. However, this is currently incorporated into the systemic risk buffer.⁸

FI also makes use of special requirements to manage macroprudential risks. The ECB and the Finnish supervisory authority, on the other hand, currently use special requirements mainly as microprudential policy measures. It is therefore unclear whether it is possible to achieve reciprocity for macroprudential policy measures that currently constitute Swedish special requirements.

⁸ As a G-SIB, Nordea is also subject to extended reporting and coordination requirements, and stricter requirements regarding eligible liabilities.

Table 1: Nordea's capital requirements Q4 2017

Capital requirements	Per cent of risk-weighted assets	Per cent of total assets
<u>Pillar 1 requirements:</u>	10.7 %	2.5 %
- Minimum requirement	4.5 %	1.1 %
- Capital conservation buffer	2.5 %	0.6 %
- Systemic risk buffer	3.0 %	0.7 %
- Countercyclical capital buffer	0.7 %	0.1 %
<u>Pillar 2 requirements:</u>	6.8 %	1.7 %
- Systemic risk	2.0 %	0.5 %
- Risk-weight floor, Swedish mortgages	1.2 %	0.3 %
- Capital requirement, Norwegian mortgages	0.4 %	0.1 %
- Other Pillar 2 requirements	3.3 %	0.8 %
<u>Total requirement</u>	<u>17.50 %</u>	<u>4.1 %</u>
Actual CET1 capital ratio	19.50 %	4.5 %

Note. Only the minimum requirement and the capital conservation buffer constitute internationally agreed requirements. Nordea is also subject to a CET1 capital requirement as a global systemically important bank, which is included in the systemic risk buffer. The countercyclical capital buffer corresponds to 2 per cent of risk-weighted assets but only applies to Nordea's Swedish exposures. If a bank contravenes Pillar 1 requirements, it may lead to restrictions on share dividends (buffer requirements) or licence revocation (minimum requirement). Pillar 2 requirements are not currently formal requirements.

Source: Finansinspektionen and the Riksbank

If the Finnish supervisory authority were unable to recognise the special requirements currently imposed by FI on Nordea, the capital requirement for the Nordea branch in Sweden would risk being lower than for Swedish banks. As regards the risk-weight floor for mortgages of 25 per cent, FI can choose to make use of Article 458 in the CRR⁹ (Pillar 1) and request reciprocity from the Finnish supervisory authority for Nordea's exposures in the Swedish branch.¹⁰ The Riksbank has previously taken a positive attitude towards Article 458, as it entails a Pillar 1 solution.¹¹

⁹ European Capital Regulations Requirements.

¹⁰ Article 458 in the CRR enables time-limited national flexibility with respect to macroprudential policy measures and requires opinions from the European Systemic Risk Board (ESRB) and the European Banking Authority (EBA) and approval by the European Commission. The drawback with Article 458 is that the measures are not permanent but, after an initial two-year period, must be renewed annually.

¹¹ FI has recently proposed the replacement of the risk-weight floor for Swedish mortgages in Pillar 2 with an equivalent capital requirement in Pillar 1. The purpose of this change, which is proposed to enter into force on 31 December this year, is to safeguard the current level of capital requirements for mortgage exposures in Sweden in the event of a relocation of Nordea to Finland. The Riksbank supports this proposal, see further the Riksbank's consultation response from 18 April 2018: <https://www.riksbank.se/globalassets/media/remisser/riksbankens-remissvar/svenska/2018/remissyttrande-om-forslag-till-forandrad-metod-for-tillampn-av-riskviktsgolvet-for-svenska-bolan.pdf>.

The Finnish supervisory authority can utilise the scope for national discretion that exists in the banking union to impose additional capital requirements. A new Finnish law from 1 January 2018 allows the Finnish supervisory authority to set a systemic risk buffer of between 1 and 5 per cent. However, it would require the approval of the European Commission, in consultation with the ESRB and EBA, if the systemic risk buffer were to be set above 3 per cent.

In sum, the shape of Nordea's future capital requirements is therefore currently unclear.

The ECB will set liquidity requirements

As from 2018, all banks in the EU are subject to common regulations regarding how much liquid assets they must retain overall. According to the Commission Delegated Regulation with regard to liquidity coverage requirements, individual supervisory authorities may also adopt currency-specific liquidity requirements. In accordance with this, FI has elected to set Pillar 2 special requirements on liquid assets in EUR and USD – in addition to overall liquidity requirements – to strengthen the resilience of Swedish banks. With Nordea's relocation to the banking union, responsibility for setting liquidity requirements will be transferred to the ECB. The ECB adopts requirements in specific currencies on a case-by-case basis, within the framework for its supervisory process (SREP).¹²

A common deposit guarantee system not yet in place

The deposit guarantee system reimburses depositors in financial institutions in the event of an institution going bankrupt. The deposit guarantee is funded through fees from the affiliated institutions which are invested in a fund. Current EU regulations require the national deposit guarantee funds to amount to at least 0.8 per cent of guaranteed deposits by 2024 at the latest.

The Swedish deposit guarantee system is administered by the Swedish National Debt Office. At year-end 2017, the Swedish deposit guarantee fund amounted to about SEK 40 billion. This corresponds to 2.4 per cent of guaranteed deposits, almost three times more than what is required by the EU directive.¹³

A common deposit insurance scheme, with a single deposit guarantee fund, is intended to constitute the banking union's third pillar, together with joint supervision and resolution cooperation. The European Commission's proposal for a common deposit insurance scheme would represent the clearest example of risk-sharing within the banking union. However, it is uncertain at present when the banking union's deposit insurance scheme will be in place and how it will be designed, including the size of the single deposit guarantee fund.

¹² European Supervisory Review and Evaluation Process.

¹³ The value of guaranteed deposits is from the end of 2016 as data on guaranteed deposits for 2017 have not yet been published. This means that guaranteed deposits reflect the situation prior to Nordea transforming its Nordic operations into branches on 1 January 2017, which made the Swedish deposit guarantee fund responsible for deposits in Sweden, Denmark, Finland and Norway. The Swedish deposit guarantee fund as a proportion of guaranteed deposits is thus currently smaller; the EU's minimum requirement is, however, still fulfilled by some considerable distance.

If a joint deposit insurance scheme were to materialise within the banking union, it would significantly strengthen the deposit guarantee with regard to Finnish banks, including Nordea, after relocation. In the present situation, however, deposits in Nordea by the general public (up to EUR 100,000, just over SEK 1,000,000) will be protected by the Finnish deposit guarantee in the event of a relocation of Nordea to Finland.¹⁴

As mentioned earlier, after the move the Finnish banking system will roughly double in size, which in turn will lead to a substantial increase in the commitments of the Finnish deposit guarantee system. According to the Finnish RVV, in an interview with Svenska Dagbladet, the Finnish deposit insurance system's commitment is estimated to increase by about EUR 80 billion of guaranteed deposits, or almost 150 per cent, in the event of Nordea moving its corporate residence to Finland.¹⁵ The Finnish deposit guarantee fund, which amounted to EUR 1.1 billion at the end of 2016, is expected to amount to around 0.8 per cent of guaranteed deposits after a relocation of Nordea, in line with the target level of the deposit guarantee directive. The Swedish deposit guarantee system's coverage ratio would, at the same time, be significantly strengthened as a result of the reduced commitment.

It can be noted that if Nordea fails, the bank would, in all likelihood, be put into resolution (see further below). During a resolution process, parts or all of the institution are kept open so that depositors and other customers have access to their accounts and other services. This means that the deposit guarantee system would not have to reimburse depositors directly. However, a strong deposit guarantee system is generally considered important in order to ensure that the banking system is stable in times of uncertainty. In the event of resolution, the idea is that some of the eligible liabilities would be either written down so that the value will be lower, or converted into equity. To ensure an orderly resolution in a crisis, it is therefore important for Nordea to have sufficiently large amounts of liabilities that actually can be written down. The so-called TLAC/MREL requirements should therefore not decrease.¹⁶ In addition to a write-down or conversion of these liabilities, there is a resolution fund to be utilised to co-finance a possible resolution procedure.

Resolution fund under development

Resolution implies that the central government assumes control over a failing bank to allow reconstruction or winding down of operations in an orderly manner. To finance resolution measures, a resolution fund can be built up using fees from banks, so that the bank's owners and creditors – and not the taxpayers – are the main funders of the procedure.

Currently, the Swedish National Debt Office has the responsibility for a possible resolution of Nordea. There is no resolution fund in the Swedish resolution system. Instead there is a resolution reserve, a special account into which banks' resolution fees are paid. However, the money is not placed in a fund, but is available to cover the central government's expenditure. So far, a total of about SEK 30 billion has been paid in, corresponding to 1.7 per

¹⁴ Fees paid by Nordea over the last year will be transferred to the Finnish deposit guarantee fund in the event of a relocation.

¹⁵ Svenska Dagbladet 12 November 2017.

¹⁶ Total Loss Absorbing Capacity/Minimum Requirement for Own Funds and Eligible Liabilities.

cent of guaranteed deposits.¹⁷ The target level of the Swedish resolution reserve is 3 per cent of guaranteed deposits.¹⁸

If Nordea carries out its relocation as planned, responsibility for the resolution of Nordea's parent company will be transferred to the banking union and the SRB.¹⁹ The SRB is responsible for both systemically important banks and cross-border banking groups, criteria that the new parent company, Nordea Bank Abp, will fulfil.

Within the banking union, there is a joint fund, the Single Resolution Fund (SRF), which can contribute with funding during a resolution procedure. However, this fund is still being set up and is not expected to be fully developed until 2024 at the earliest. The target level is 1 per cent of guaranteed deposits, which corresponds to EUR 55 billion. In 2017, the fund amounted to about EUR 17 billion, about 0.3 per cent of guaranteed deposits, which is significantly lower than the coverage ratio of the Swedish resolution reserve. Within the banking union, a financial backstop to the SRF has yet to be adopted.

Until the SRF is completed, it is divided into national departments based on each country's deposits. Each country is allowed to take a successively smaller proportion from its own national department and an increasingly large proportion from the common funds until finally, in 2024, all funding is to come from the SRF. Until then, Finland would thus have to bear a greater economic responsibility for a possible resolution of Nordea. The Finnish national department currently amounts to about 2 per cent of the funds collected by the SRF.

The Riksbank's areas of responsibility: payment systems, monetary policy, liquidity supply

Nordea is currently a participant in RIX, a primary monetary policy counterparty and a counterparty in foreign exchange transactions in relation to the Riksbank. The Riksbank has assumed that Nordea will continue in the same counterparty roles as it has today. If the reversed merger is approved, Nordea's participation in the RIX system will then be transferred to Nordea Bank Abp. Nordea Bank Abp and its Swedish branch will be expected to fulfil the fundamental requirements for RIX participants (as a credit institution be subject to adequate supervision), a primary monetary policy counterparty (have branches in Sweden and have, on its own or together with another company in the same group, a share of the money and bond market that the Riksbank considers large enough), and a foreign exchange counterparty (have, on its own or together with another company in the same group, a share of the foreign exchange market that the Riksbank considers large enough).

As a RIX participant, Nordea Bank Abp's Swedish branch will have access to the Riksbank's intraday credit line and, as a monetary policy counterparty, it will have access to so-called standing facilities, i.e. overnight lending and deposits in Swedish kronor. These two are the Riksbank's normal liquidity facilities.

¹⁷Guaranteed deposit figures are from 31 December 2016.

¹⁸ At present, the Swedish National Debt Office's resolution reserve has a borrowing limit of SEK 100 billion and a guarantee limit of SEK 200 billion.

¹⁹ After the relocation, it will still be possible for Nordea's Swedish subsidiary to be wound up or entered into bankruptcy or resolution in accordance with Swedish law.

The Riksbank can also provide extraordinary liquidity facilities in a crisis situation, which would also be available to foreign branches if they are monetary policy counterparties. Such operations could involve loans with longer maturities, in either Swedish kronor or foreign currencies, and against other collateral than what the Riksbank usually accepts.

A Memorandum of Understanding (MoU) between the Nordic and Baltic central banks from December 2016 discusses in more detail how responsibilities shall be allocated in practice as regards extraordinary liquidity support.²⁰ Under this MoU, the home country central bank is expected to deal with any request for emergency liquidity assistance. This means that the Bank of Finland is expected to deal with any request for emergency liquidity assistance from Nordea after its relocation. This includes emergency liquidity assistance to foreign branches and also applies to requests for emergency liquidity assistance in Swedish kronor. At the same time, the host country central bank of a foreign branch is expected to strive to assist.

In exceptional cases, the Riksbank can provide emergency liquidity assistance to an individual bank, including branches. Different conditions can be attached to such assistance based on the Riksbank's assessment of which purpose would best benefit financial stability in Sweden.

3. The Riksbank's answers to Finansinspektionen's specific questions

- 1) In view of the Riksbank's mandate, are there any crucial objections to granting Nordea's application based on the so called public interest as well as creditor interest perspectives that Finansinspektionen is to take into consideration when assessing the application?*

Under the Riksbank Act, the Riksbank's tasks are to maintain price stability and to promote a safe and efficient payment system.²¹ Financial stability is a precondition for both price stability, i.e. low and stable inflation, and a safe and efficient payment system. The Riksbank has therefore analysed Nordea's planned relocation from a financial stability perspective.

An important starting point for the analysis is to note that Nordea's relocation does not seem to involve any significant changes regarding Nordea's banking operations in Sweden and that the challenges associated with a highly interconnected and concentrated Swedish banking system will therefore remain. On the other hand, the formal commitment for the Swedish taxpayer decreases, as the responsibility for crisis management, including costs for resolution and the deposit guarantee as well as the provision of liquidity support, will be transferred to authorities within the banking union. As far as Nordea is concerned, the SRB will have the responsibility for resolution and use of the single resolution fund, the Finnish state will have the responsibility for the deposit guarantee and the Bank of Finland will be responsible for liquidity support.

Another important aspect is to distinguish between the short- and long-term effects. In the long run, a relocation of Nordea to Finland could lead to reduced risks for financial stability in Sweden and for Swedish taxpayers. Fully developed, the banking union

²⁰ See *Memorandum of Understanding on Cooperation regarding Banks with Cross-Border Establishments between the Central Banks of Denmark, Estonia, Finland, Iceland, Latvia, Lithuania, Norway, and Sweden*, December 2016, http://archive.riksbank.se/Documents/Rapporter/%c3%96vrigt/NB_MoU_161215.pdf.

²¹Sveriges Riksbank Act (1988:1385).

should be able to contribute to a more robust European banking system with more intensive supervision without a national “home bias” and with significant risk sharing among the participating member states in the form of a joint deposit insurance scheme and a single resolution fund.

Much of the banking union is also already in place. For example, the main framework of the supervisory function, the SSM, has already been established. In a short period of time, the ECB has built up significant supervisory resources and cooperation with national authorities, which seems to be working relatively well. There is also reason to believe that the intensity of supervision will increase with respect to Nordea, which in itself indicates a reduced risk for financial instability in Sweden.²² At the same time, it should be noted that effective supervision requires good knowledge of local conditions. In Nordea’s case, about 75 per cent of its operations will be outside the banking union. It is therefore important for the supervisory colleges to have sufficient local knowledge regarding host countries outside the banking union. It is reasonable to assume overall, however, that the prerequisites for supervision will be improved even in the relatively short term.

However, the fact that the banking union is not yet fully developed means that much of the responsibility in a crisis falls back on the individual member state. Remaining uncertainties can, in the short term, lead to negative overall effects of a relocation from a stability perspective, as there is still political disagreement on the elements of the banking union most clearly aimed at sharing the risks among participating member states. For example there is still no final guarantor for the joint resolution fund, which could lead to problems in the event of large pay-outs. From a risk-sharing perspective, it can also be noted that a relatively small part of the resolution fund is available for joint financing. Neither has it been possible to reach agreement on a common European deposit insurance scheme, which means that depositors are still dependent on their own member state’s ability to guarantee their deposits. Hence, the banking union is not fully developed and a substantial part of the responsibility for managing banking problems within the banking union still lies with the individual member state, in this case Finland.

The size of the home country affected is an important aspect to consider in this perspective, as a smaller country generally has less resources than a larger country to manage a troubled bank. The fact that the Finnish economy is about half the size of the Swedish economy (with a significantly lower coverage ratio in the deposit guarantee) may prove to be important in this perspective, as market confidence in banks is affected by a country’s ability to manage its banking sector. If Nordea were to encounter problems, there is hence a risk of concerns regarding Finland’s crisis management capacity allowing problems to spill over more easily to neighbouring countries. It is therefore reasonable to assume that the financial stability risks seen in total will increase slightly for Sweden in the event of a relocation.

The dramatic increase in the size of the Finnish banking sector, and hence the commitment of Finnish public finances, in the event of a move, also means that the risks to Sweden’s public finances in the short term may not decline fully until the banking

²² According to the IMF, FI has significantly fewer resources to allocate to supervision of major banks compared with the SSM. See Sweden, *Financial Sector Assessment Program*, Technical Note on Banking Supervision and Regulation, October 2017. International Monetary Fund (IMF).

union is fully developed and the responsibility for resolution costs and deposit guarantee is shared by all the member states in the banking union.

Against this backdrop, and as the risks of concentration and interconnectedness in the Swedish banking system are expected to remain, it is the Riksbank's view that a prerequisite for the relocation is to ensure that Nordea's capital and liquidity requirements are not lowered so as not to jeopardise financial stability in Sweden. It is the Riksbank's view that the current Swedish liquidity requirements in US dollars and euro have strengthened banks' resilience. The Riksbank has also previously highlighted the importance of all banks in Sweden, including Nordea, having liquidity requirements in all significant currencies, in order to counteract short-term liquidity risks. Apart from weaker resilience, lower requirements may also lead to competitive advantages for Nordea in relation to Swedish and Nordic banks, which could lead to increased risk-taking by both Nordea and other players in the Swedish banking system. Lower requirements for Nordea may also lead to pressure from other banks to also lower their requirements. As a principle, it is also unfortunate if banks try to minimise the regulations by playing different countries off against each other. This risks creating a negative spiral of ever-lower requirements. As a failing bank creates major externalities for the economy, there is a need for public regulation to limit the risks. These externalities are often difficult to estimate and different countries can make different assessments. But in an internationalised world in which the risks of contagion are considerable, it is important to counteract tendencies for banks to choose residence with the main aim of reducing the regulatory burden.

Nordea's planned move highlights the problems surrounding the authority of home countries and host countries with respect to foreign bank branches and the importance of host country authorities having sufficient insight into the supervision and resolution plans for the entire banking group. This will be particularly important for a major, systemically important branch such as Nordea's future Swedish branch. For Sweden, the relocation implies a substantial reduction in not only the responsibility for a systemically important financial player in Sweden, but also the control and insight as regards supervision, deposit insurance and resolution for the entire group. This, in turn, may lead to reduced scope for safeguarding Swedish interests, which may increase stability risks in Sweden in a crisis situation. Increased cooperation and the exchange of information between the Nordic countries in terms of supervision and liquidity supply will continue to be very important.

2) *To what extent can the Riksbank offer different forms of extraordinary liquidity support measures to Nordea if the merger is realised in line with the application?*

As the Riksbank has previously pointed out, Swedish banks are exposed to both short-term and structural liquidity risks.²³ Periodically, some of the major banks have very low liquidity coverage ratios. This applies, in particular, to Swedish kronor but also to other significant currencies, for which FI has no specific requirements. As the Riksbank has emphasised many times, it is important for banks to, first and foremost, have their own self-insurance by holding adequate liquidity reserves. It will be even more important for Nordea to have sufficient liquidity reserves in Swedish kronor after a move as the

²³ The Riksbank Financial Stability Report 2018:1, 23 May 2018, https://www.riksbank.se/globalassets/media/rapporter/fsr/engelska/2018/fsr-180523/financial-stability-report-2018_1.pdf.

responsibility for dealing with an application for emergency liquidity assistance will be transferred to the Bank of Finland.

Next, if the bank's self-insurance is insufficient and, despite everything, a situation arises whereby Nordea needs to be supplied with liquidity, the responsibility lies with the Bank of Finland, which will be expected to deal with a request for emergency liquidity assistance from Nordea under the Nordic-Baltic central bank MoU from December 2016. Such a responsibility for the Bank of Finland also applies to emergency liquidity assistance to foreign branches, and for liquidity in Swedish kronor. In such a situation, the Riksbank can assist the Bank of Finland.

Even if the responsibility lies with the Bank of Finland, there is still legal scope for the Riksbank to also assist as a last resort with extraordinary liquidity facilities in a crisis situation.

- 3) *What is the Riksbank's view as regards to whether, and if so how, the public interest will be affected by Nordea's relocation in light of Nordea's various roles in Swedish financial market infrastructures and payment systems?*

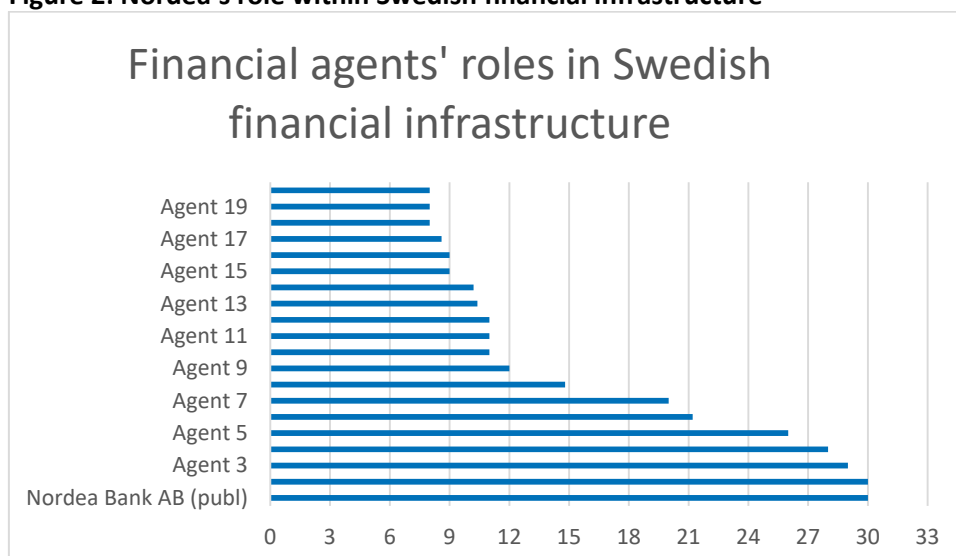
Nordea is a member of all systemically important Swedish financial market infrastructures (FMIs), i.e. RIX, Euroclear Sweden, Nasdaq Clearing and Bankgirot. Apart from being a participant in an FMI, a bank may have several roles that are important for an FMI to function safely and efficiently. Examples include: acting as an agent for indirect participants, providing lines of credit to a central counterparty (CCP), or being a settlement bank.

Figure 2 shows the number of roles a bank has within Swedish financial infrastructure, i.e. in RIX, Euroclear Sweden, Nasdaq Clearing, Bankgirot, the Swedish National Debt Office, EuroCCP and CLS. In total, there are 33 possible roles, which are specific to each system. A bank can, for example, be a normal participant, a settlement bank or a monetary policy counterparty. Each role counts as an observation regardless of the bank's significance in this role. Figure 2 shows the sum of all roles and is a simplified illustration of the significance of a bank for the financial infrastructure. Still, the figure indicates that Nordea is one of the most important players in the Swedish financial infrastructure, measured in terms of the number of roles.

A relocation may lead to certain operational problems but these are deemed manageable. As the company's legal residence will move to Finland, certain agreements will have to be rewritten. This is, however, a formality and is predictable. For certain roles, such as monetary counterparty or RIX participant, a Swedish branch or registered office in Sweden is required. This is not deemed to be a problem either, as Nordea will have a branch in Sweden in the future.

The Riksbank considers Nordea to be a central player within Swedish financial infrastructure. There is, however, no reason to believe that a move in itself will change Nordea's role in the financial infrastructure in Sweden. The Riksbank also considers the operational risks associated with the move to be small.

Figure 2: Nordea's role within Swedish financial infrastructure



Note. The figure shows the total number of roles a bank has in RIX, Euroclear Sweden, Nasdaq Clearing, Bankgirot, the Swedish National Debt Office, EuroCCP and CLS. In total, there are 33 possible roles, which are specific to each system. Each role counts as one observation regardless of the bank's significance in this role.

Source: The Riksbank, Euroclear Sweden, Nasdaq Clearing, Bankgirot, the Swedish National Debt Office, EuroCCP and CLS

Neither will a relocation of Nordea to Finland have any specific impact on its role as a RIX participant, apart from operations continuing under a different name, as a branch with its own corporate identity number. This only involves a name change in the RIX system and the change in participation will therefore not affect the payment system or the other RIX participants. After the move, Nordea's RIX participation will be monitored by the Riksbank in the same way as before.

Lastly, it is the Riksbank's assessment that Nordea and other major Swedish banks are also critical players regarding cash provisioning in Sweden.

4. Conclusions

- The Riksbank is of the view that a prerequisite for a relocation not to lead to increased risks to financial stability is that Nordea's capital and liquidity requirements do not become lower.
- The Riksbank's view is also that it is important that all banks in Sweden, including Nordea, have liquidity requirements in all significant currencies, in order to counteract short-term liquidity risks. It will be even more important for Nordea to have sufficient liquidity reserves in Swedish kronor after a relocation.
- In addition to retained capital and liquidity requirements, increased cooperation and the exchange of information between the Nordic countries regarding supervision and liquidity provision will continue to be very important.
- Within the SSM, it will be important for the supervisory colleges to have sufficient local knowledge about host countries outside the banking union. This will be particularly important in light of Nordea having about 75 per cent of its operations outside the banking union.

- As the Riksbank has emphasised many times, it is important for banks to, first and foremost, have their own self-insurance by holding adequate liquidity reserves.
- If a situation arises in which Nordea needs to be supplied with liquidity, the responsibility will lie with the Bank of Finland, which will be expected to deal with a request for emergency liquidity assistance from Nordea, including its foreign branches, even regarding liquidity in Swedish kronor.
- The Riksbank considers Nordea a central party within Swedish financial infrastructure. There is, however, no reason to believe that a move in itself will change Nordea's role within the financial infrastructure in Sweden.
- Neither will a relocation of Nordea to Finland have any specific impact on its role as a RIX participant, apart from operations continuing under a different name, but as a branch.

On behalf of the Executive Board:

Stefan Ingves

Sophie Brauner

Taking part in the decision: Stefan Ingves (chair), Kerstin af Jochnick, Per Jansson, Martin Flodén, Henry Ohlsson and Cecilia Skingsley.

The reporting staff was Ann-Margret Westin.