Macroprudential strategy of the Board of the Financial Supervisory Authority

Macroprudential policy refers to measures directed at preventing and limiting systemic risks and their effects that threaten the stability of the financial system. The macroprudential strategy of the Board of the Financial Supervisory Authority (FIN-FSA) combines macroprudential policy objectives, indicators and instruments into a coherent whole. It describes how the various policy objectives are linked to systemic risks that jeopardise the attainment of the primary goal and how the instruments can be used to achieve the objectives. The strategy serves the work of the Board in its role as the national macroprudential policy decision-maker.

Macroprudential policy is forward-looking and predictable. In addition to decisions on macroprudential instruments, the macroprudential toolkit includes recommendations and raising issues for public discussion.

The FIN-FSA Board evaluates annually the success of the policy it practises, the effectiveness of the available tools, and whether the macroprudential strategy is up to date. Regular updates to the strategy ensure its effectiveness in a changing operating environment.

The primary goal of macroprudential policy is to reduce the probability and adverse effects of financial crises and other severe disruptions to the financial system on the real economy and thereby promote long-term economic growth by:

- preventing and limiting the build-up of systemic risks and vulnerabilities,
- strengthening the risk resilience of the financial system for system risks, and
- supporting financial intermediation in the event of disruptions to the economy or the financial system.

The primary goal of macroprudential policy is divided into intermediate objectives and operational policy objectives.

The FIN-FSA Board has specified ***four intermediate objectives for macroprudential policy***:

1. Preventing excessive growth of credit granted to households, non-financial corporations and the entire private sector and mitigating the consequent risks as well as preventing excessive indebtedness of households and thereby maintaining households' risk resilience.
2. Maintaining adequate risk resilience of credit institutions taking into account cyclical systemic risks, structural vulnerabilities of the financial system and the systemic significance of individual credit institutions.
3. Improving the risk resilience of the financial system as a whole by also taking into account the risks to financial activity other than traditional credit institution activity.
4. Supporting the lending capacity of the financial system if threatened as a result of severe distress in the economy or the financial system.

Macroprudential analysis identifies systemic risks, which, if materialised, could jeopardise the achievement of the primary or intermediate objectives, and evaluates different policy options. Systemic risks can be broken down into cyclical and structural systemic risks. Cyclical systemic risks are typically linked to strong fluctuations in lending and asset prices. Structural systemic risks, in turn, are associated with long-term and slow-moving characteristics of the economy and the financial system. Such structural vulnerabilities are, for example, high private-sector debt and a large and concentrated banking system. On the other hand, severe disruptions to the economy and to the financial system, such as those stemming from external shocks, for example, can also jeopardise financial intermediation in the economy. In such cases, macroprudential policy can contribute to strengthening the supply of credit in the financial system. When strengthening credit supply, the estimated duration and severity of the disruption should be taken into account. Macroprudential stability assessments should also take into account new types of global risks, such as cyber risks, climate risks and geopolitical risks.

Macroprudential policy also has its limitations: macroprudential instruments alone cannot sufficiently prevent the build-up of economic imbalances or support financial intermediation. When assessing the success of macroprudential policy, the combined effect of other policy segments and regulation should also be taken into account.

Communication allows macroprudential authorities to explain the rationale behind macroprudential policy and its objectives to the general public. Forward guidance on forthcoming macroprudential measures contributes to reducing market uncertainty. It can steer expectations of forthcoming macroprudential policy and thereby influence the behaviour of economic agents. Communication also ensures and strengthens the transparency and openness of decision-making to the public, stakeholders and relevant parties.

The FIN-FSA Board pursues its four intermediate macroprudential objectives through the following four ***operational policy objectives***:

- The growth rate of loans to the household sector for house purchase and the growth rate of total household sector debt remain moderate. The achievement of the objective is assessed primarily on the basis of whether these growth rates exceed the growth rate of annual household disposable income over the medium term. In addition, the achievement of the objective is assessed by means of risk indicators (e.g. debt-to-income and debt-servicing-to-income ratios) describing households' adequate debt servicing capacity (intermediate objective 1).
- Systemic risks relating to credit granted to the private sector remain moderate in light of the risk indicators for setting the CCyB requirement. The achievement of the objective is assessed primarily on the basis of whether the growth rate of loans to the private sector exceeds the growth rate of nominal GDP over the medium term (intermediate objective 1).
- The capital adequacy of the entire credit institution sector is sufficiently strong to cover potential losses in the economy and the financial system in the event of exceptionally severe crises (intermediate objective 2).

- The capital adequacy of systemically important credit institutions is strong relative to their importance for the stability of the whole financial system, measured by statutory criteria (intermediate objective 2).
- The capital adequacy, leverage and funding structure of the entire credit institution sector are strong relative to identified systemic risks and vulnerabilities (intermediate objective 2).
- The effectiveness of macroprudential policy is ensured and circumvention of policy measures prevented by imposing, if necessary, macroprudential requirements permitted by legislation also on financial service providers other than credit institutions (intermediate objective 3).
- Macroprudential policy space is enhanced for example with releasable capital buffers and the policy space is used swiftly and in a temporary manner in the event of severe economic and financial market disruptions (intermediate objective 4).

The FIN-FSA Board's macroprudential policy is forward-looking. Macroprudential policy that is proactive and strengthens the resilience of the financial system ensures adequate policy space in good time in the event of severe economic and financial market disruptions. The aspect of proactivity is emphasised especially when preventing cyclical risks. Proactive prevention of the build-up of risks also entails lower costs than addressing risks that have already materialised.

The Board's decision-making in managing risks and vulnerabilities is supported by *ex-ante* analysis of the effects of the various alternative policies and instruments. The analysis assesses the suitability of the different policy options for mitigating vulnerabilities and the cost and benefit of the different options. As a rule, the identified macroprudential risks or vulnerability should always be addressed with instruments that target risks most effectively and most directly. On the other hand, each systemic risk or vulnerability should principally be addressed by only one instrument.

After its policy decisions, the Board assesses the effects of the measures undertaken through *ex-post* evaluations. The purpose of these evaluations is to ascertain whether the measures undertaken had desired effects and whether they were calibrated correctly in relation to the identified vulnerability and to the state of the economy.

Instruments for achieving the intermediate objectives

The decision-maker should have at least one instrument available for each intermediate objective of macroprudential policy.

For ***intermediate objective 1***, the primary instruments available are the countercyclical capital buffer (CCyB) requirement, the maximum loan-to-collateral (LTC) ratio and recommendations on household indebtedness and debt-service burdens.

Other instruments available are structural additional capital requirements and risk weight requirements. In addition, the maximum repayment period and the maximum interest-only period for housing company loans are likely to limit the risks associated with housing finance. Key instruments whose binding application is not permitted under Finnish legislation are the maximum debt-to-income (DTI) ratio, the maximum debt service-to-income (DSTI) ratio and amortisation requirements for mortgage loans.

For ***intermediate objective 2***, the primary instruments available are the countercyclical capital buffer (CCyB) requirement, the capital buffer requirements for structural systemic risks and vulnerabilities of the entire credit institution sector (SyRB), and the OSII and G-SII/B capital buffer requirements imposed on global and other systemically important credit institutions.

Other available instruments in addition to the capital conservation buffer (CCoB) requirement include measures made possible under Articles 458, 124 and 164 of the EU Capital Requirements Regulation (CRR).

For intermediate objective 3, in particular, instruments will be used to improve the risk resilience of the financial system outside the credit institutions sector. Instruments which may also have potential macroprudential effects in the event of systemic risks are a leverage limit for alternative investment fund managers (AIFMs), instruments based on Solvency II and other instruments applicable to insurance institutions, and exceptional measures targeted at pension providers. In the case of investment funds, no instruments complying with the macroprudential instrument definition are available, but the supervisory authority is entitled, under specified conditions, to suspend the redemptions of an individual investment fund, in addition to which the Real Estate Funds Act imposes a permanent limitation on the borrowing of funds.

In the absence of binding measures, the FIN-FSA issues, where appropriate, recommendations and warnings to financial market participants with respect to financial stability risks potentially emerging or building up outside the credit institutions sector. The FIN-FSA will separately assess the possible impact on its macroprudential strategy of the regulatory changes coming into force in early 2027 in the non-life and life insurance sector and of regulations concerning the exceptional circumstances of the employee pension sector.

For ***intermediate objective 4***, the instruments available are the countercyclical capital buffer (CCyB) requirement, the systemic risk buffer (SyRB) requirement and other additional capital requirements. The lending capacity of the financial system in the event of severe economic or financial market disruptions is primarily supported by lowering buffer requirements intended to be released in times of crises, such as the CCyB. The possibility to set a positive neutral CCyB rate, i.e. a buffer rate that is above zero in the normal "neutral" phase of the credit cycle, would help achievement of the intermediate objective but would require a legislative change. The aim is to restore the lowered buffer requirements when the disruption and threats to the lending capacity of the financial system have been mitigated, the possible negative effects of the increase on the supply of credit are assessed to be moderate and the formal conditions for the imposition of the requirements are in place.

In the context of a possible temporary reduction in requirements, the FIN-FSA may also issue recommendations, where appropriate, to limit the distribution of profits in the financial sector to ensure that the released capital is channelled to lending, loss-covering and preparedness for future losses.

As part of the annual evaluation of the macroprudential strategy, the FIN-FSA Board evaluates the instruments available and any related changes that may be required together with the experts of the FIN-FSA, the Bank of Finland, the Ministry of Finance and the Financial Stability Authority who participate in the preparation of the Board's macroprudential decisions.

Macroprudential policy objectives and instruments in Finland

<table>
<tr><th>Primary goal</th><th>Intermediate objectives</th><th>Operational policy objective</th><th>Instruments</th></tr>
<tr><td rowspan="3">Reducing the probability and adverse effects of financial crises and other severe disruptions to the financial system on the real economy, thereby promoting long-term economic growth by:
- preventing and limiting the build-up of systemic risks and vulnerabilities,
- strengthening the risk resilience of the financial system for system risks, and
- supporting financial intermediation in the event of disruptions to the economy or the financial system.</td><td rowspan="2">Preventing excessive growth of credit granted to households, non-financial corporations and the entire private sector and mitigating the consequent risks as well as preventing excessive indebtedness of households and thereby maintaining households' risk resilience.</td><td>The growth rate of loans to the household sector for house purchase and the growth rate of total household sector debt remain moderate. The achievement of the objective is assessed primarily on the basis of whether these growth rates exceed the growth rate of annual household disposable income over the medium term. In addition, the achievement of the objective is assessed by means of risk indicators (e.g. debt-to-income and debt-servicing-to-income ratios) describing households' adequate debt servicing capacity.</td><td>Primary instruments
Countercyclical capital buffer (CCyB) requirement
Maximum loan-to-collateral ratio
Recommendations on household indebtedness and debt-service burdens

Other instruments
Other additional capital requirements and risk weight requirements
Maximum repayment period
Limitations to housing company loans in new housing construction

Additional instruments requiring regulatory changes
Maximum DTI ratio or maximum DSTI ratio
Amortisation requirement</td></tr>
<tr><td>Systemic risks relating to credit granted to the private sector remain moderate in light of the risk indicators for setting the CCyB requirement. The achievement of the objective is assessed primarily on the basis of whether the growth rate of loans to the private sector exceeds the growth rate of nominal GDP over the medium term.</td><td>Primary instruments
Countercyclical capital buffer (CCyB) requirement

Other instruments
Maximum loan-to-collateral ratio
Other additional capital requirements

Additional instruments requiring regulatory changes
Positive neutral CCyB rate</td></tr>
<tr><td>Maintaining adequate risk resilience of credit institutions taking into account cyclical systemic risks, structural vulnerabilities of the financial system and systemic significance of individual credit institutions</td><td>The capital adequacy of the entire credit institution sector is sufficiently strong to cover potential losses in the economy and the financial system in the event of exceptionally severe crises.</td><td>Primary instruments
Countercyclical capital buffer (CCyB) requirement
Systemic risk buffer (SyRB) requirement
CRR Article 458 (risk weights)

Other instruments
Capital conservation buffer (CCoB) requirement</td></tr>
</table>

			CRR Articles 124 and 164 (risk weight, LGD)
		The capital adequacy of systemically important credit institutions is strong relative to their importance to the stability of the whole financial system, measured by statutory criteria.	Primary instruments*O-SII and G-SII/B buffers (individual credit institutions)*
		The capital adequacy, leverage and funding structure of the entire credit institution sector are strong relative to identified systemic risks and vulnerabilities.	Primary instruments *CRR Article 458 (capital and liquidity requirements)* *CRR Articles 412 and 413 (liquidity requirements)* *CRR Article 429 (leverage ratio)*
	Improving the risk resilience of the financial system as a whole by also taking into account the risks to financial activity other than traditional credit institution activity.	The effectiveness of macroprudential policy is ensured and circumvention of policy measures prevented by imposing, if necessary, macroprudential requirements permitted by legislation also on financial service providers other than credit institutions.	Instruments also with potential macroprudential effects *Leverage limit for AIFMs* *Instruments based on Solvency II and other instruments applicable to insurance institutions* *Exceptional measures targeted at pension providers (incl. regulatory measures)* *Maximum repayment period (other creditors and credit intermediaries)* *Recommendations and warnings*
	Supporting the lending capacity of the financial system if threatened as a result of severe distress in the economy or the financial system.	Macroprudential policy space is enhanced for example with releasable capital buffers and the policy space is used swiftly and in a temporary manner in the event of severe economic and financial market disruptions.	Primary instruments *Countercyclical capital buffer (CCyB) requirement* Other instruments *Systemic risk buffer (SyRB) requirement* *Other additional capital requirements* Additional instruments requiring regulatory changes *Positive neutral CCyB rate*