FINANSSIVALVONTA
FINANSINSPEKTIONEN
FINANCIAL SUPERVISORY AUTHORITY

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Basel Committee on Banking Supervision

Countercyclical capital buffer proposal

Response of the Finnish Financial Supervisory Authority to the consultation document of July 2010

The Finnish Financial Supervisory Authority very much welcomes the proposed introduction of the counter cyclical buffers, and generally supports the proposals laid down by the Committee. We recognize that a counter cyclical capital buffer requirement can be a useful macro-prudential tool for protecting the banking system against the systemic risks originated from excessive credit growth.

We generally support the idea of significant discretionary powers of supervisory authorities in setting up the buffer requirements, as they are difficult to be based on exact formulas and single macro-economic indicators. The strong international cooperation and "peer group" comparisons will, however, be needed to support harmonized application of the requirements.

We propose that the Committee could consider the following aspects of the proposal.

- A shorter than 12-month implementation period for the buffer requirement, e.g. 6 months, could be more efficient, still giving banks enough time to meet the higher capital requirements. The capital requirement should control the build-up of excessive leverage in the economy as timely as possible.

- The method of defining the size of the counter cyclical capital buffer should also take into account sector specific growth rates of credits (i.e. corporate and household sectors). This feature would have many advantages in environments e.g. with specialized banks operating in particular credit segments. Taking into account sectoral developments would result in a more effective setting up of the buffer than basing it only on universal credit developments. It can be that there is excessive credit growth only in a single sector, causing relatively minor growth in total lending. E.g. currently corporate credit is growing sluggishly in Finland and in Europe generally, while there are concerns related to the growth of housing loans in certain countries.

- We believe that more consideration is needed on supervisory cooperation and level-playing field issues regarding cross-border lending. The effectiveness of the new capital requirements to curb excessive credit growth in individual countries rests on the effectiveness of the international supervisory cooperation in the case of cross-border banks - especially operating

through branches in host countries. In countries where the banking sector has significant branches of cross-border banks, but where the significance of the branches for their parent banks' entire balance sheets is small, the effect of the country specific buffer might be very limited. Hence, the buffer requirement for such cross-border banks could be only a fraction of the buffer required from local banks resident in that host country, and the buffer requirement could be ineffective in curbing the credit granting of the branches of cross-border banks. And, there would be level playing field issues compared to local institutions. We would support further thinking of this issue; also whether some other tools should be made available for the host supervisor to make sure that the credit growth restrictions would apply effectively also to cross-border banks operating in their jurisdiction.

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