

Seppo Honkapohja: Brief remarks of Finnish financial history

Welcome remarks by Mr Seppo Honkapohja, Deputy Governor of the Bank of Finland, at the dinner for the SUERF Conference, Helsinki, 14 September 2017.

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Speakers, organizers and participants of the 33rd SUERF Colloquium,

It is my pleasure to welcome you to the dinner. Shadow Banking, the theme of the conference is of course highly topical and is also a central concern for financial regulation. I will not try to comment on the conference theme but instead thought to tell you a little bit of Finnish financial history in my short welcoming remarks.

Finland has not experienced any major problems in banking or financial markets during the recent global financial crisis. Finland did, however, go through a major financial crisis in the early 1990's. In fact, the Finnish crisis was one of the Big Five in the table of 18 financial crises in advanced economies in the period from WWI to 2007 (i.e. before the current global crisis) developed by Ken Rogoff and Carmen Reinhard in 2008.¹ Incidentally, both Norway and Sweden are also among Big Five.

The Finnish crisis was a boom-bust cycle, which was to large extent caused by problems in the deregulation of the financial system in the 1980s. Before the deregulation, the Finnish financial system was tightly controlled with interest rates mostly set by the central bank and controls of external capital movements.

Financial deregulation led to a huge credit expansion and large inflows of capital. The growth rate in bank lending reached to about 45 % at the end of 1980's². The boom period came to an end in 1990 when a rapid decent in real activity ensued. This development led to a major banking crisis which started in September 1991.

Large amounts of public funds and some other forms of support had to be employed to counter the crisis. Major restructuring of the banking system was carried out to improve the efficiency of the banking system. The banking crisis came to its end in 1996–7 when the banks began to show positive profits, though structural changes in the banking system continued much longer.

This is in brief the story of the Finnish financial crisis in the 1990's. I should note that shadow banks did not have any major role in the Finnish financial system in 1980s and in the financial crisis. However, we saw a little bit of the shadow bank phenomenon in what was called “grey economy” and “grey financial activity”, where notary departments of banks mediated loans with flexible interest rates outside the official system. The “grey economy” was an indication of the pressures created by tight rationing of the Finnish financial system in the 1980's.

References:

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Princeton University Press, Princeton.

¹ See Reinhard and Rogoff (2008, 2009).

² The Finnish crisis and those of Norway and Sweden are well discussed in the literature. For example, see Honkapohja (2014 a, b) and the references there in.