FINANCIAL STABILITY ASSESSMENT

Global upheaval – Financial stability at risk from power politics

Financial stability | 19.06.2025

Finland's financial system is stable. However, aggressive power politics and erosion of the international rules-based system could undermine this stability. A slow recovery in the Finnish economy would prolong the downturn in the housing and real estate markets and increase the risks for banks and investors. Given the challenging global circumstances, the banking sector's resilience should be maintained and reinforced further by improving the capacity of macroprudential policy to react to crises in the financial system. The EU financial system should be strengthened and diversified by implementing the plans for a Savings and Investment Union.

The Finnish economy started to grow slowly during 2024 but is still struggling to recover from the recession. Labour market conditions continued to weaken in spring 2025, housing prices continued to decline compared to a year ago, and housing construction and property investment were experiencing difficulties. Corporate bankruptcies increased, albeit more slowly than before. However, lending rates have declined and are likely to continue doing so along with short-term market rates. The consequent reduction in interest payments has already eased the debt servicing of households and businesses. It is anticipated that the lower interest rates will lead to a pick-up in borrowing, supporting a gradual recovery in the real estate market.

Shifts in the foreign and trade policies of the superpowers are darkening the outlook for the global and Finnish economies. Political uncertainty and a deterioration in the economic outlook have caused volatility particularly in share prices. Uncertainty in financial markets is high, and financing conditions have tightened in international financial markets. The possibility of a serious disruption in the financial markets cannot be ruled out if geopolitical tensions escalate further and the economy's downside risks materialise.

Although Finland's financial system has remained stable in the uncertain operating environment, risks have increased. The downturn in the credit and real estate markets may be prolonged if the recovery in Finland's economy is significantly slower than forecast. A weak recovery would increase banks' credit risks, prolong the difficulties of real estate investors and increase the risks of forced sales of housing properties.

The resilience of the banking sector has been strengthened in Finland through the use of discretionary additional capital requirements, or macroprudential buffers, imposed by the Financial Supervisory Authority (FIN-FSA). The resilience of households against risks has also been strengthened with restrictions and recommendations on mortgage borrowing and housing company loans, and through macroprudential policy measures. The Bank of Finland's key policy recommendations for maintaining and reinforcing financial stability are summarised in Table 1.

The tightening of US trade policy in spring 2025 is part of a broader shift in power politics in which the economy, security and technology are more closely intertwined. This requires governments, businesses and public authorities to engage in more active risk management and to prepare for complex threats related to economic and financial affairs, financial stability and security.

In an uncertain operating environment, it is essential that the financial sector and the authorities have preparations in place for severe operational disruptions and financial crises. Consolidation of the public finances in Finland is also essential for ensuring financial stability, but at the same time an increase in defence spending is justified in the current geopolitical landscape.

The strong resilience of Finland's banking sector must be ensured by having sufficiently large macroprudential buffers. Borrowers' resilience and the good lending practices of banks must be maintained by means of requirements and recommendations on lending. The way in which countercyclical capital buffer (CCyB) requirements are imposed on banks should be amended to allow the requirement to be increased even before the credit cycle threatens to overheat. This would enable the authorities to lower the capital requirements for banks, if necessary, during any sudden disruptions in the economy, thus supporting banks' lending capacity.

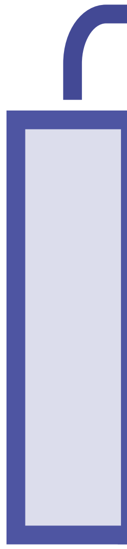
Erosion of the international rules-based system could undermine financial stability in the long term if international cooperation is weakened in areas such as financial regulation and combating climate change. A race to loosen financial regulation would increase the likelihood of financial crises, and there is no reason to embark on such a path.

In an environment that is geopolitically and economically challenging, bold and swift reforms are required from Europe. Europe must improve its competitiveness, accelerate growth and invest in the green and digital transitions and defence. For financial stability, the main concern is to make progress with developing the capital markets and finalising the banking union in accordance with the strategy for the new Savings and Investment Union. The development of the capital markets cannot be left solely to the EU as it also requires national measures. Indeed, in its mid-term policy review, the Finnish Government decided on a number of measures to develop the capital markets in Finland.

Summary of the assessment of Finland’s financial stability	
Short-term risks	

Summary of the assessment of Finland’s financial stability

Aggressive global power politics would add to the risk of liquidity crises and operational disruptions in the financial markets.



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Summary of the assessment of Finland’s financial stability

Banks’ liquidity offers them protection against temporary funding constraints. Back-up systems have been put into place as a contingency measure for operational disruptions.

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Policy recommendations for strengthening financial stability

The financial sector and the authorities must continue to prepare for operational disruptions and financial crises	**The resilience of financial market participants must be maintained through macroprudential policy**	**The EU must harmonise and diversify Europe’s financial system**

The financial sector and the authorities must be prepared to deal with complex economic, financial stability and security threats that are difficult to predict. Finland's public finances must be consolidated and financial stability consequently secured.	Banks need sufficient capital buffers as a counterbalance to their structural vulnerabilities. The requirements on mortgages and housing company loans must not be diluted. The responsiveness of macroprudential policy should be improved by allowing for more flexible use of countercyclical capital buffers.	Finland must actively advance the Savings and Investment Union to speed up competitiveness, investment and growth and to increase harmonisation within Europe's financial system. International and domestic financial regulation should be reassessed and simplified, but deregulation should be approached with caution.

International investors seek safe havens from geopolitical uncertainty

Geopolitical tensions escalated in spring 2025, adding to concerns in the global economy, the financial markets and political circles.[1] Russia's war in Ukraine, which it started in 2022, is undermining security in Europe. In the United States, the administration of President Trump, who was inaugurated in January 2025, has created turmoil in many areas of domestic and foreign policy and undermined confidence in international cooperation.[2]

Unpredictable US policies have increased volatility in international financial markets. In early April, President Trump's announcements of new tariffs[3] caused investors to transfer some of their assets to lower risk securities. Concerns over the direction of US foreign and security policy and the aggressive attitude towards its allies have also contributed to investor unease.

Investors have taken the view that the tariffs increase the likelihood of a recession, which is why share prices and raw material prices fell abruptly and risk premia widened in early spring 2025. At the start of April, the United States postponed by 90 days the entry into force of its previously announced tariffs. The financial markets calmed down when expectations regarding the outcome of trade negotiations improved.

In the spring, the VIX and VSTOXX indices, which are a measure of the uncertainty in financial markets, rose to their highest level since the pandemic (Chart 1). However, in contrast to the time of the pandemic, the markets remained functional without the need for government and central bank intervention (see Large market fluctuations include risk of liquidity spiral).

Chart 1.

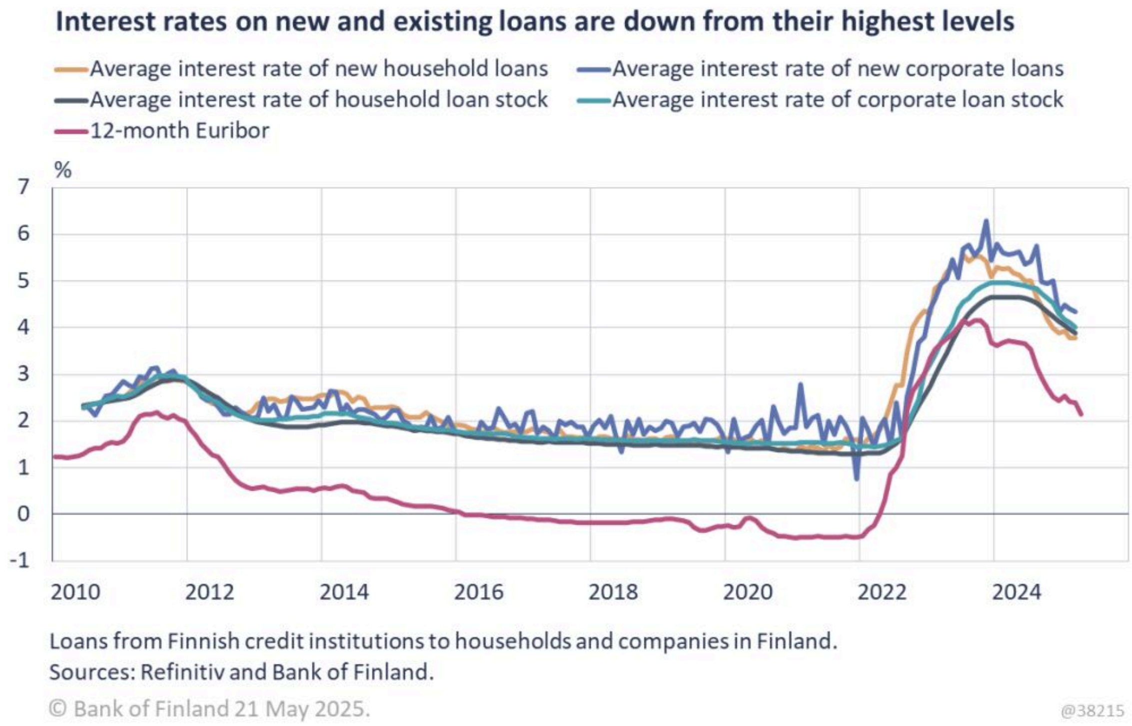
Delta Risk Reversal describes the price of hedging against developments in the EUR/USD exchange rate. A positive (negative) figure means that the price of hedging against appreciation (depreciation) is higher.
Source: Bloomberg.

The highly protectionist measures by the United States and the unpredictability of trade policy are currently the greatest threats to global economic growth.[4] Growth strengthened in 2024, but in the first half of 2025 there were already signs of a slowdown. Purchasing managers' indices have been sluggish, and consumer confidence has deteriorated in many of the world's main economies. In the financial markets,the increased uncertainty raises the cost of finance and can make it more difficult to obtain finance.

Global economic slowdown, a trade war and a weakening security situation in Europe could dampen growth in the Finnish economy if they were to lead to a reduction in consumption and investment. In its March interim forecast, the Bank of Finland projected that Finland's economy would gradually strengthen in 2025 and 2026.[5]

During 2024, the Finnish economy was starting to grow slowly, but private domestic demand was still subdued at the end of the year and labour market conditions were gloomy. On the other hand, lower interest rates (Chart 2) are supporting economic recovery and the purchasing power of borrowers. The markets expect interest rates to continue declining during 2025.

Chart 2.



ⓘ Large market fluctuations include risk of liquidity spiral

Major economic shocks usually lead to a rapid repricing of risks in the securities markets and to increased demand for safer and more liquid assets. Investors are generally able to estimate the impact of the shock on the future outlook for companies and other debtors and can rapidly set a new price for the risk. If a shock causes substantial uncertainty, the price formation process can be difficult. In such cases, trading will be low and prices will fluctuate wildly with the small trading volumes.

The responses of international financial market participants to a shock could even lead to forced sales of securities and a self-perpetuating liquidity spiral (Chart 3). This happened during the pandemic, for example. Initial signs of something similar were also seen in early April 2025.

A liquidity spiral is created when investors have a sudden escalating need for liquidity that triggers a chain reaction leading to a growing liquidity shortage. The spiral is caused by an initial shock, which gives rise to a substantial increase in market volatility as a result of a decrease in the prices of assets such as equities and bonds. The sudden increase in market volatility raises the collateral requirements placed on investors. These requirements are imposed by securities brokers and central counterparties on market participants to mitigate counterparty and credit risks. They are obliged to impose these requirements to ensure the stability of their balance sheets amid growing market risks.

The increased collateral requirements are typically met with deposits, which increases investors' liquidity needs. Investors in need of liquidity start selling assets to meet their obligations, adding to downward pressure on prices and further raising volatility. Investors may also need to liquidate assets from different funds, for example, in order to meet collateral requirements elsewhere. This increases liquidity risks in the entire system.

Leveraged investment can exacerbate the situation. When asset prices fall, their collateral value decreases. Loan issuers can raise their collateral requirements or apply higher valuation haircuts to existing collateral, which demands additional collateral from investors. The spiral continues when a price decline causes further losses that need to be covered again with new additional collateral.

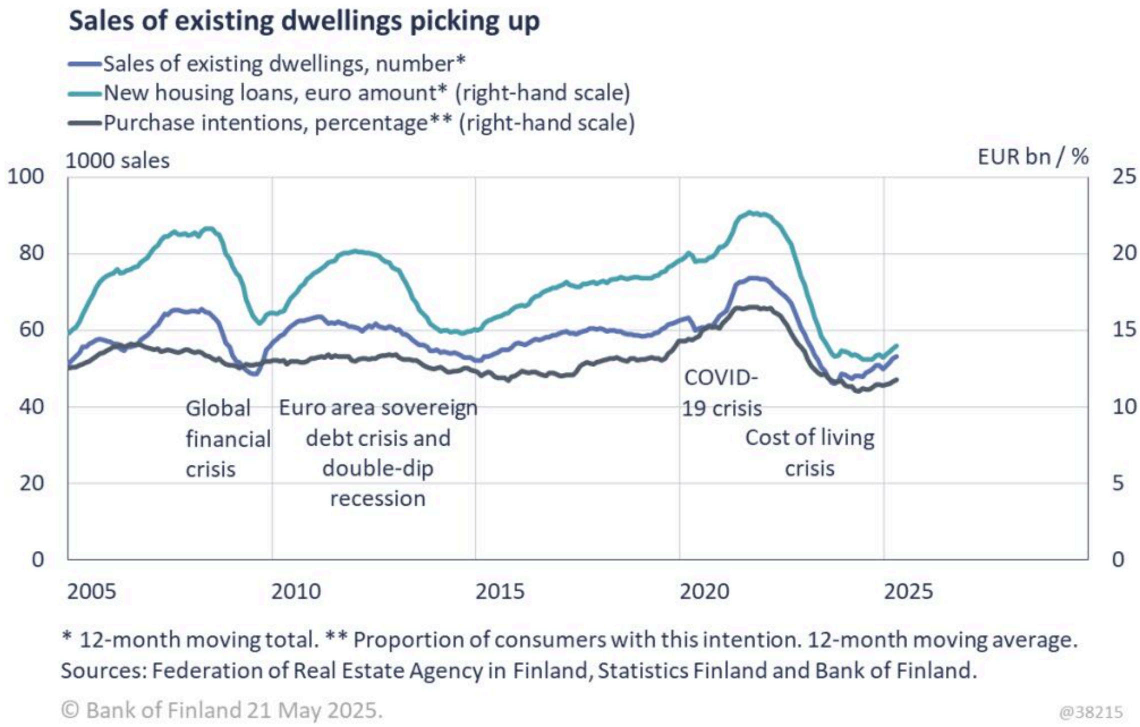
The spiral is dangerous and can undermine both financial institutions and the functioning of the markets. In order to break the liquidity spiral following the pandemic shock, robust measures to support liquidity were required from central banks, which helped stability to return to international financial markets.[6]

Chart 3.

Loss of momentum in the economy would put recovery of real estate market at risk

The downturn in the Finnish housing market is moving on from its lowest point (Chart 4). Residential property sales started to pick up in the second half of 2024 on the back of the decrease in interest rates, although the prices of dwellings[7] have continued to decline and housing construction remains low. In early 2025, sales of existing dwellings were notably higher than in the two previous years. However, sales of new dwellings remain very low and fewer dwellings have been completed and are under construction than before.

Chart 4.



The downturn is also expected to ease gradually in the professional real estate investment market.[8] The overall return from real estate began to be positive again in 2024 (Chart 5), although for offices it remained negative. The decline in market values of properties eased during 2024 and net rental income increased.

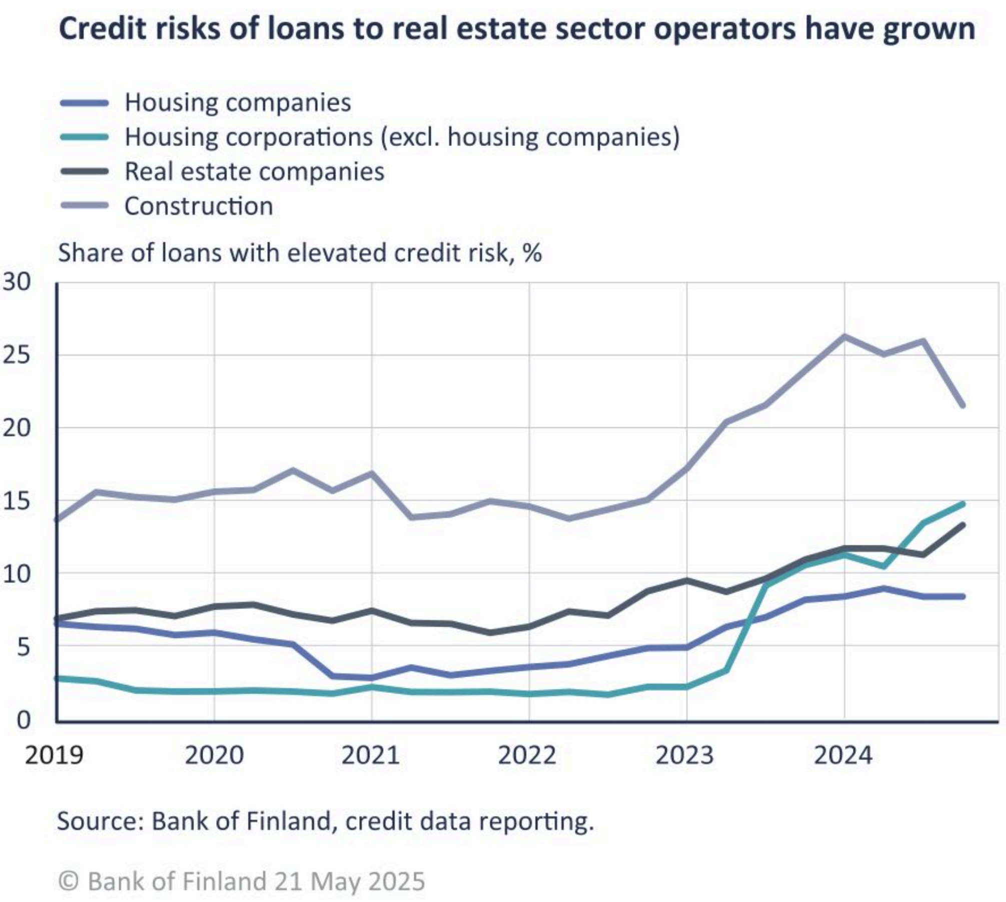
A further indication of the easing of the real estate sector's plight is the slight improvement in access to finance, as real estate companies returned to the debt securities market in 2024 as issuers.[9] Despite the positive signs, the number of investment property transactions was very low in 2024 and early 2025.

Chart 5.

Slower economic activity and more difficult access to finance from the international financial markets could endanger the nascent recovery of the real estate market. The debt-financed real estate and construction sectors are usually very sensitive to changes in economic conditions, and the operating environment has already long been difficult for companies (see: Trade war weakens export outlook for Finnish companies – Bank of Finland Bulletin).

Cyclical conditions have been the most difficult for construction companies, among which bankruptcies have increased. Banks' credit risks from loans granted to the construction sector have also grown (Chart 6). Open-end real estate funds have been the worst hit among real estate investors (see information box 'Real estate funds' liquidity tools protect against forced sales'), and their liquidity difficulties could be further exacerbated by a prolonged economic downturn.

Chart 6.



The housing and real estate market downturn has increased credit risks on the loans of some housing companies and other housing corporations (Chart 6). Non-performing loans have mainly concerned property-holding sectors other than households. Therefore, the growth in non-performing housing company loans is more a reflection of the financial difficulties of some professional operators that provide rental housing than of households' problems with debt servicing.

The situation in the housing market is expected to strengthen gradually and cautiously when the economy picks up. Consumers' weak confidence and unemployment fears could nevertheless hinder the recovery of housing sales and borrowing, although lower inflation and interest rates have already eased consumers' finances and debt servicing. A pick-up in housing sales would also benefit the construction sector and the real estate investment market, where housing is the most important investment.

Real estate funds’ liquidity tools protect against forced sales

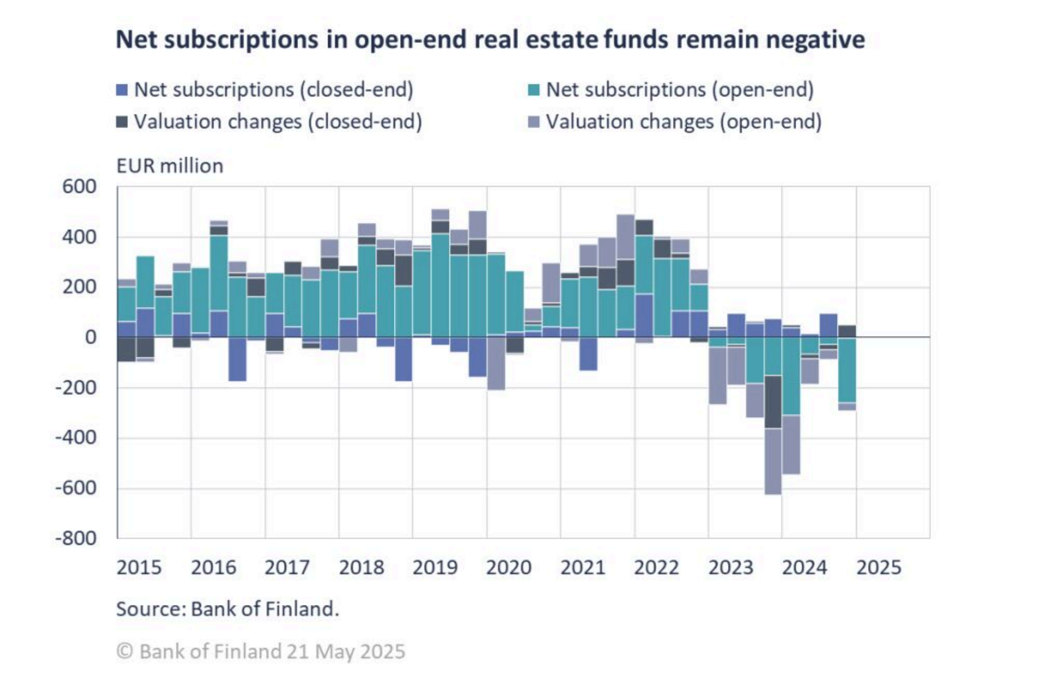
A recovery in the real estate market is important especially for real estate funds, redemptions from which have increased in recent years. Open-end real estate funds are exposed to changes in the investment behaviour and risk appetite of their investors. Although the net asset value of Finnish funds has developed favourably overall, the value of open-end real estate funds has decreased as a result of falling property values[10] and redemptions of fund units. Redemptions from Finnish open-end real estate funds have been substantial since early 2023 (Chart 7).

Many Finnish open-end housing and real estate funds have reacted to the growing redemptions by changing their rules and by using various liquidity management tools, including deferred redemption payments. Some of the funds have sold investment properties to other investors. By restricting and temporarily suspending redemptions, widespread forced sales of dwellings can be avoided, which helps to curb the strong price decline in a difficult market.

On the other hand, future sales could reduce prices further if the supply remains high in relation to demand. With funds having been major purchasers of domestic properties in previous years, the redemption pressures could contribute to slowing the recovery in housing sales and construction.

The temporary suspension and restriction of redemptions raises questions regarding investor protection. It is important to ensure that financial products are not marketed to investors as being safer or more liquid than they actually would be in difficult market conditions where restrictions on redemptions might be justified to ensure the interests of investors who remain in the fund.

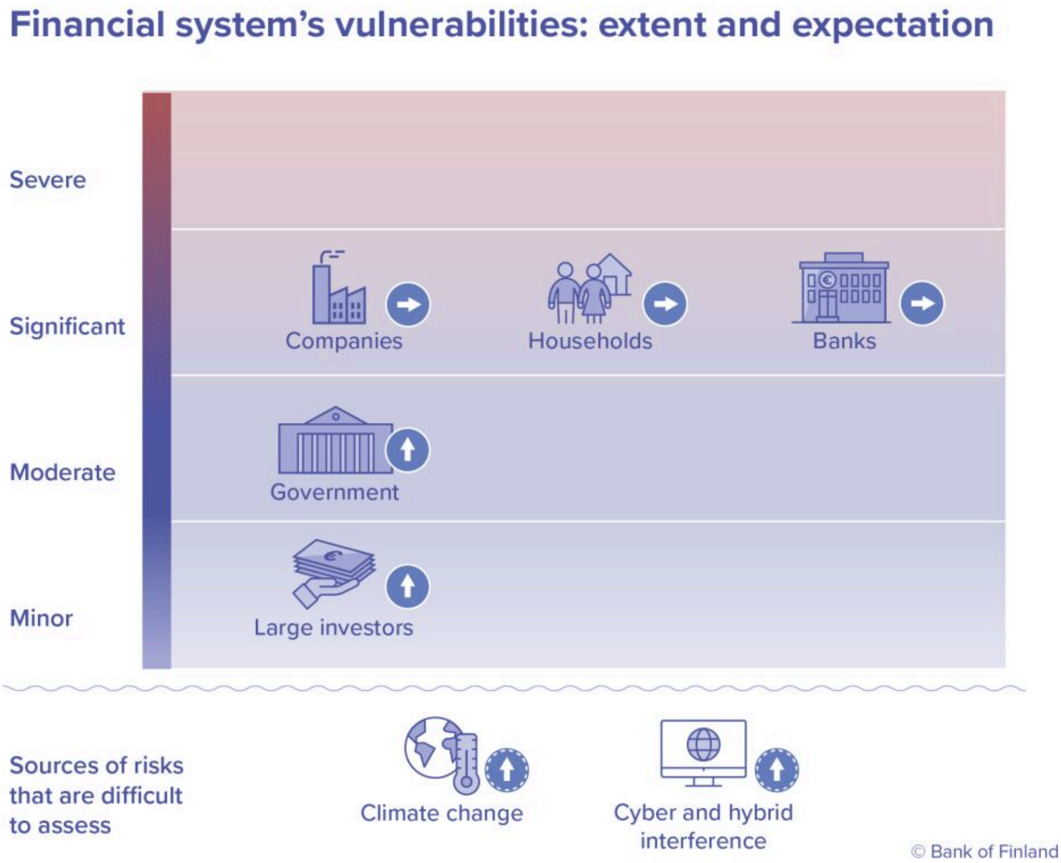
Chart 7.



Volatile operating environment increases threats to financial stability

The financial system's vulnerabilities and their expected future path have remained largely unchanged (Chart 8).[11] In contrast, the likelihood of risks materialising has increased. Heightened tensions between superpowers are increasing the risk of disruption in the financial markets and weakening the economic outlook, elevating the risk of a prolonged downturn in the credit and real estate markets. Erosion of the international rules-based system would weaken financial stability in the long term through, for instance, increased climate risks, added infrastructure vulnerabilities and possible structural changes in the financial system. Geopolitical tensions are also increasing pressure for higher defence spending, which could further increase public debt if permanent increases in government spending are not matched by increases in revenue.

Chart 8.



A weakening of the economy would increase credit risks and reduce banks' capital adequacy

The key vulnerabilities of Finland's financial system are related to structural factors in the banking sector which, as a rule, are fairly unchanging.[12] A large proportion of bank lending consists of housing and real estate finance, which exposes banks to the cyclical variations of the real estate markets and to household and corporate default risks.

The financial standing of Finland's banks has remained good despite the difficult operating environment in recent years.[13] The capital position and profitability of banks are very good even by international standards (Chart 9). However, profitability is no longer improving strongly, as it was when interest rates were rising. Although banks' credit risks have grown to some extent, they are assessed as being manageable if the economy performs as forecast. However, a sudden economic slowdown could increase banks' credit losses, which would contribute to weakening their capital adequacy and could, in the worst case, limit the supply of loans. According to stress tests, Finland's banking sector could withstand even a harsh recession.[14]

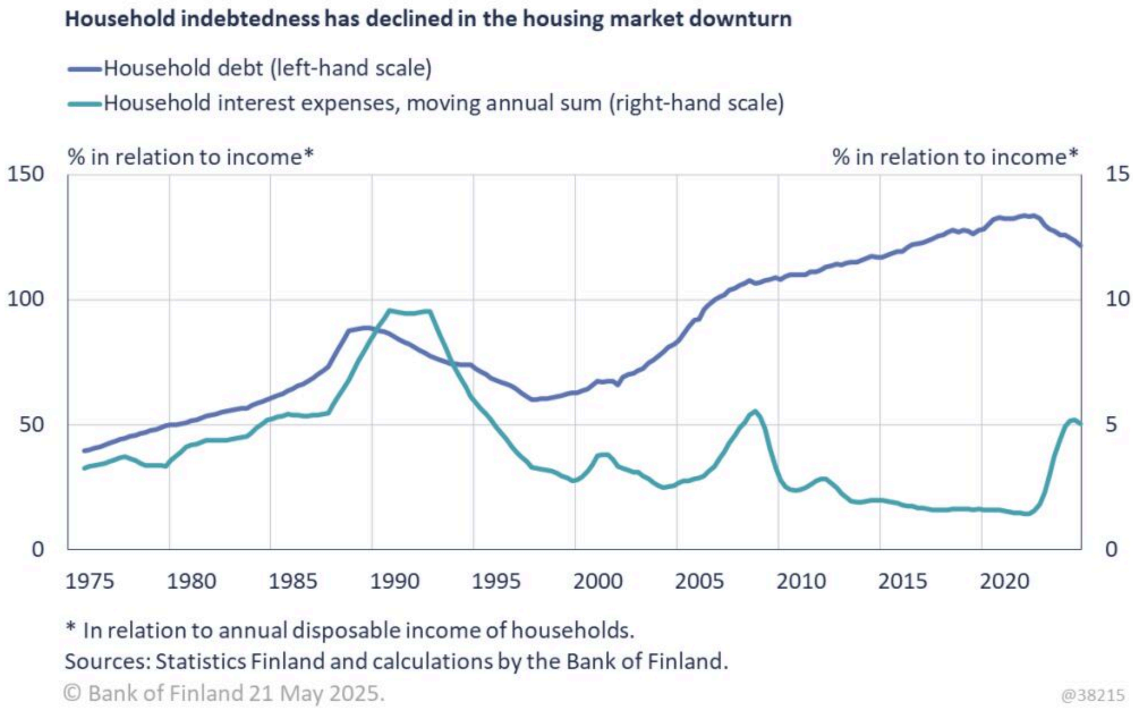
Chart 9.

Note: EA refers to the weighted average of countries in the euro area. The return on equity is expressed on an annual basis, derived from the figures for the first three quarters.
Sources: European Central Bank's consolidated banking statistics and calculations by the Bank of Finland.

The biggest vulnerabilities in the household sector are the high indebtedness in relation to income and the concentration of wealth in housing assets, which leave households exposed to the fluctuations in interest rates and housing market conditions.[15] Some of the risks associated with indebtedness and with the sensitivity of the housing market to interest rates have already materialised, as interest rates have risen, unemployment has increased and housing prices have decreased substantially. However, banks' credit risks from loans granted to households have remained relatively low, as households have been able to adjust their finances and service their debts well overall (see: Mortgage borrowers have proved resilient against the interest rate risk of their loans – Bank of Finland Bulletin).

Household indebtedness has decreased during the downturn in the housing market, but it remains high by historical and international standards (Chart 10). The risks associated with indebtedness will remain in check in the immediate years ahead if the economy and the housing market recover as forecast. Debt servicing would be eased and household purchasing power improved if interest rates remain at their current levels or fall, while economic recovery would reduce the threat of unemployment and boost confidence. On the other hand, below-forecast economic growth would be a strain on households' debt servicing capacity, especially if the labour market situation deteriorates further.

Chart 10.

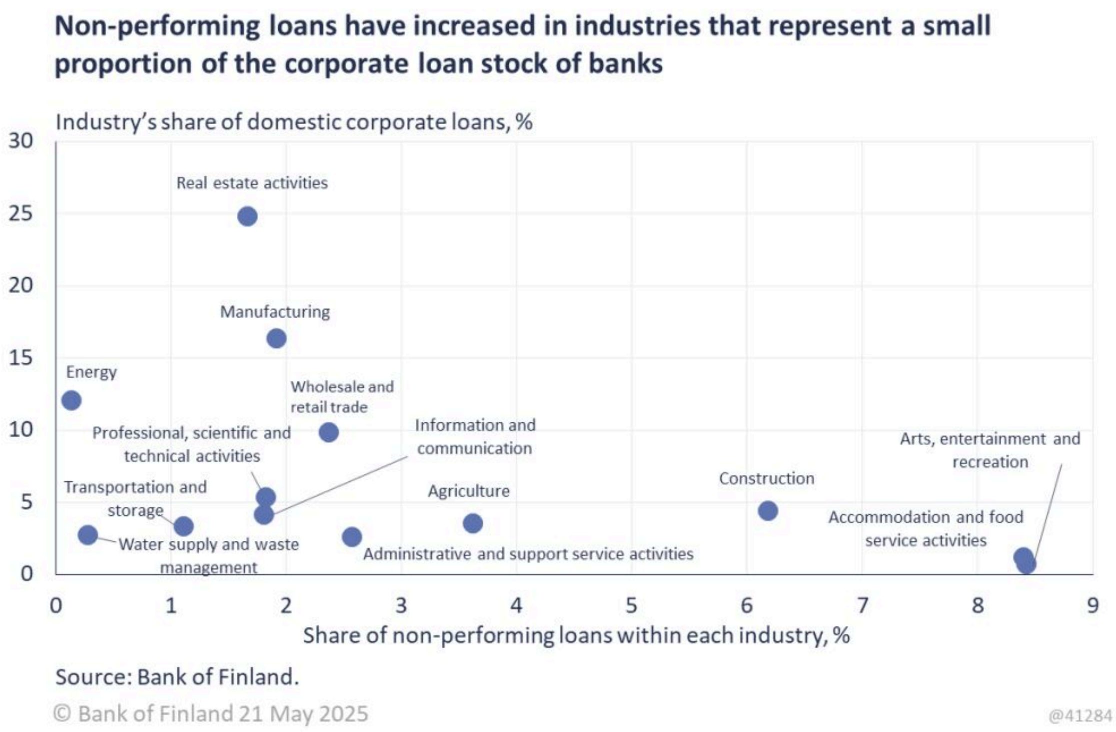


Companies have coped fairly well with the difficult circumstances of recent years, but there are large differences between industries and among companies. Corporate bankruptcies have become more common, and the debt servicing capacity of smaller companies, in particular, has suffered, which has increased the volume of non-performing loans. However, the risks in the corporate sector have not jeopardised financial stability, as debt servicing problems have been most prevalent in industries whose loans account for a small share of the banking sector's entire corporate loan stock – in accommodation and food service activities, construction and agriculture (Chart 11).

The difficulties of companies would increase if the economic recovery from recession were to be delayed and the economy were to weaken. The biggest cause for concern is real estate companies, whose increasing problems would raise banks' credit risks and the risks of other real estate investors. In addition to credit risks for banks, the growing difficulties faced by small and medium-sized enterprises could also affect financial stability via households if rising unemployment were to weaken households' debt servicing capacity.

The United States is a key export destination for Finnish companies, and increases in tariffs could enlarge the credit risks concerning loans to export industry companies in particular (see: Trade war weakens export outlook for Finnish companies – Bank of Finland Bulletin). It is still difficult to make detailed estimates of the impact of the tariffs on corporate profitability and credit risks, as the extent and focus of the tariffs are not yet finalised and may still change.

Chart 11.



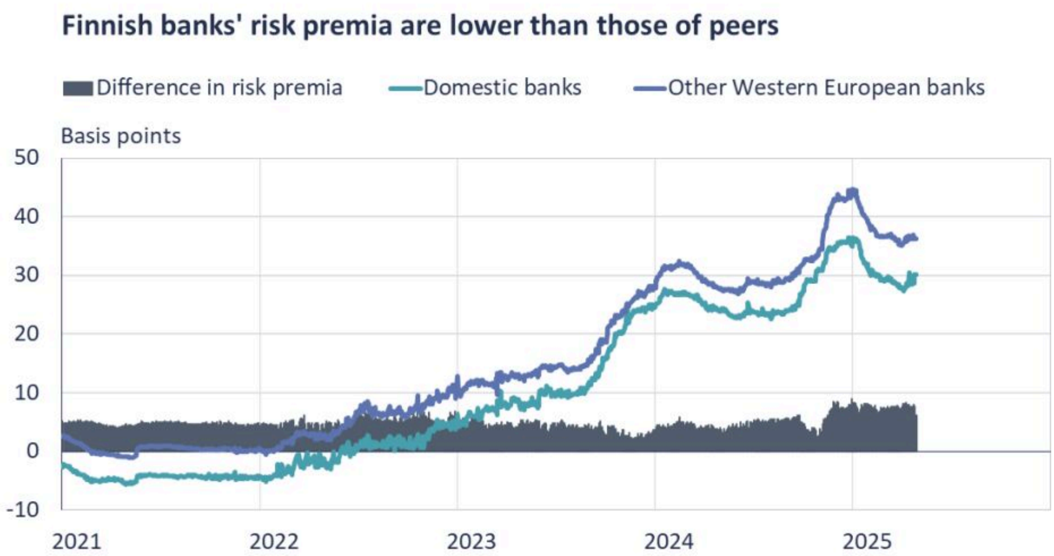
Volatility in the securities markets could tighten financing conditions and cause losses to investors

A volatile geopolitical and geoeconomic landscape is reducing investors' willingness to take risks. Negative political surprises could continue to shake up the securities markets in the same way as in April 2025. Sudden fluctuations also increase the risk of a serious disruption (see information box 'Large market fluctuations include risk of liquidity spiral').

The large fluctuations in securities prices and reduced risk appetite among investors will have a broad and diverse impact on financial system entities. The impacts will be greatest on major domestic professional and institutional investors, such as investment funds, employee pension companies and life insurance companies, which have considerable investments in the international interest rate markets and stock markets. Uncertainty is expected to remain elevated in international securities markets, which increases the vulnerabilities of large investors.

The strong corrections in securities prices and the general tightening of financing conditions also affect banks. An increase in risk premia in financial markets could raise the funding costs for banks. Investors’ lack of confidence in the banks could, in the worst case, spread quickly and unpredictably, which would expose the banking sector to liquidity risks. Finnish banks’ risk premia have increased less in recent economic crises than their international peers, which indicates that investors have confidence in the sector’s resilience (Chart 12).

Chart 12.



Note: The risk premium describes the difference between the bond yield requirement and the risk-free yield requirement derived from swap rates for the same maturity. Includes all euro-denominated covered bonds whose price at issue exceeded USD 0.3 billion.

Sources: Bloomberg and calculations by the Bank of Finland.

Disintegration of the international rules-based system would be detrimental to financial stability

The power politics of the superpowers and their increasing competition economically and in technology are hampering international relations and cooperation. The international financial system is a complex network of highly interconnected cross-border activities. These include short-term and long-term financing agreements, international financial firms and global financial infrastructure, such as payment and settlement systems. This interconnectedness allows capital to move smoothly across borders, but it also creates significant dependencies and vulnerabilities.

Climate change and biodiversity loss have an adverse impact on the global economy and, by extension, on the European and Finnish economies. Changes in global policy priorities make it harder to combat climate change[16] and increase the likelihood of a climate crisis.[17] The Finnish financial system's vulnerabilities due to climate change have been assessed as relatively moderate in the short and medium term.[18] However, to date there is relatively little knowledge of the total impact of climate and biodiversity loss risks in Finland.

As climate change progresses, the risks caused by extreme weather events will increase, for example in the form of higher compensation obligations for non-life insurance companies. Delaying measures to curb climate change could, in the long term, increase the transition risks, as faster measures to reduce emissions will be needed in the future.

The uninterrupted functioning of the financial system infrastructure[19] is a prerequisite for financial stability. Strong interdependencies between the components of infrastructure systems increase the risk that disruptions in one location could spread and cause damage to the entire financial system.[20] Services provided by these infrastructures are widely produced both globally and in different regions of Europe, which means that the infrastructure of the Finnish financial system is also dependent on service providers and technologies outside the country's borders. Although these services generally function well, there are critical services that are widely distributed geographically in which interdependence is strong and requires extensive cooperation between countries.

Geopolitical tensions and the undermining of international cooperation are adding to general uncertainty and increasing the operational risks to infrastructure.[21] This underlines the need to increase the independence of Europe's financial infrastructure as well. The transformed security environment in regions neighbouring Finland has increased the risk that infrastructure and individual financial corporations, in particular, may become the targets of hybrid interference, i.e. cyberattacks or other disruptions performed or directed by nation-state actors.

Cyberattacks against Finnish banks have become more common in recent years, especially denial-of-service (DoS) attacks. However, such attacks have not diminished the confidence of investors or customers in the banks. Cybercrime is growing and is increasingly targeting citizens and businesses. Phishing attempts and other scams targeting bank customers have increased, and banks must take greater responsibility for preventing these and protecting their customers.

Digitalisation of the economy and the financial system unfortunately also presents new opportunities for criminal activity. Factors such as skilful scams, the rapid spread of disinformation in the digital environment and the increased popularity of securities trading on multilateral platforms may create risks that could be amplified by the rapid advances in artificial intelligence.[22]

Reasonable to reassess financial regulation but not to carelessly dismantle it

Following the global financial crisis, the stability of the financial system was strengthened by significantly tightening banks' capital and liquidity requirements and other financial regulation. However, recent efforts to boost economic growth and improve international competitiveness have created pressure for lighter regulation both internationally and in Finland.

The European Commission plans to review the EU banking system and the competitiveness of banks in 2026. The Commission is also likely to examine ways to simplify financial regulation. In its mid-term policy review in April 2025, the Finnish Government outlined a number of measures that would ease the restrictions on the maximum size and duration of new mortgages and housing company loans.

While it is reasonable to assess the need for regulatory reform, efforts to ease financial regulation in both Finland and the EU must be viewed with caution. There is a risk that key economies will start to compete over who can ease regulation the most. An example of this is the US administration's consideriation of whether to loosen the regulation of crypto-assets. An expansion of crypto-asset markets could create new risks to financial stability if these markets become more integrated with the traditional financial system.[23]

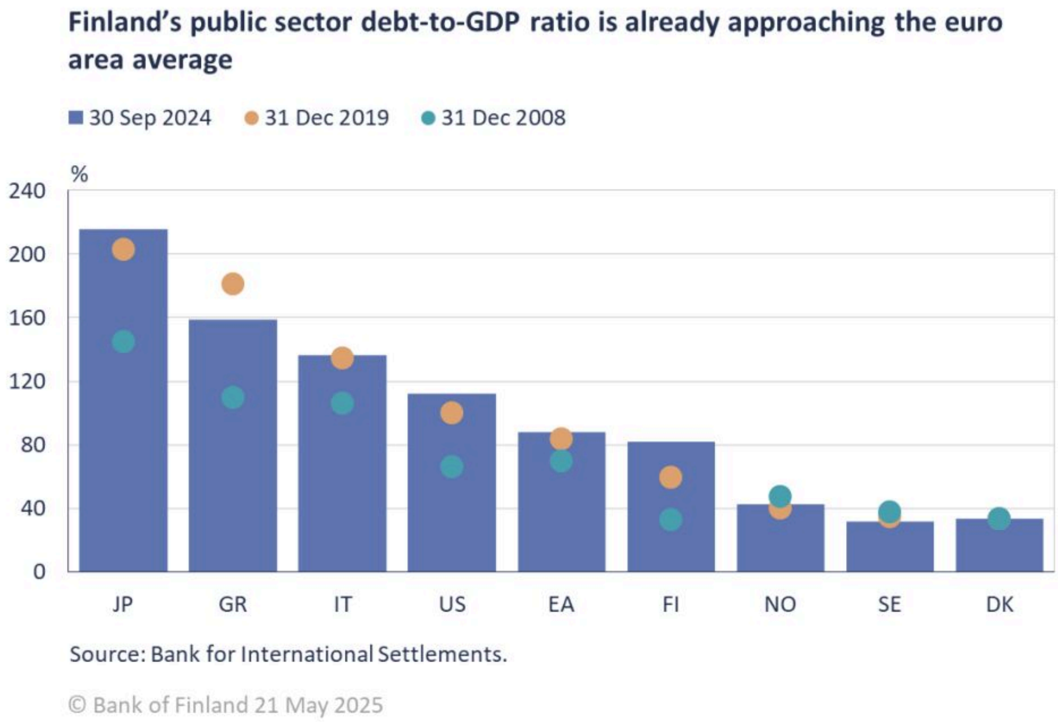
Financial regulation has proved its worth particularly in the turbulence of recent years.[24] Straightforward deregulation would increase the probability of a financial crisis in the long run. However, strengthening economic growth and competitiveness is also important for financial stability, as banks and investors cannot remain profitable and solvent in the long term in a dwindling economy.

Finland's persistently low country risk supports financial stability

Finland's public debt has increased rapidly in recent years and the state of the public finances continues to be difficult (Chart 13).[25] A high level of debt weakens the government's ability to use expansionary fiscal policies to respond to crises in the economy or the financial system. Turning Finland's debt ratio onto a declining path requires fiscal rebalancing measures that take into account of factors such as higher spending on defence.

Geopolitical risks will affect investors' assessments of the risk level of Finnish government debt. So far, Finland's risk premia have remained low and stable. For example, the increase in hybrid interference has not pushed up the risk premia on Finnish government debt (See: Investors' confidence in Finland as an attractive country for investment has remained strong – Bank of Finland Bulletin).

Chart 13.



Ensuring that Finland has an attractive national brand and low level of country risk is important for financial stability. Finland's stable institutions and its focus on comprehensive security help investors to view Finland as a safe country to invest in both now and in the future. If investors' confidence in the Finnish Government's solid debt servicing capacity and the low level of sovereign credit risk were to weaken, this could raise the price at which the government, credit institutions and large corporations access finance from the international financial markets.

Unpredictable operating environment must be taken into consideration in risk management

The resilience of Finland's financial system has been strengthened in numerous ways in recent years. The loss-absorbing capacity of the banking sector has been reinforced with capital buffer requirements included in the macroprudential toolkit.[26] The requirements have been set and calibrated based on vulnerabilities identified in the banks and the banking sector. Without sufficient capital buffers, disruptions and crises in the banking sector could even turn very severe and threaten financial stability.

The resilience of borrowers has also been strengthened in a variety of ways in relation to housing loans and housing company loans.[27] Credit decisions must always be based on a careful assessment of creditworthiness. The launch of the Positive Credit Register in spring 2024 has helped the assessment of loan applicants' credit standing (See: Mortgage borrowers have proved resilient against the interest rate risk of their loans – Bank of Finland Bulletin).

The rapid changes in the economy, technology, the environment and geopolitics are hampering the assessment of financial risks. The consequences of unprecedented sequences of events are difficult to assess with conventional risk management models. Both the financial sector and the authorities responsible for the stability of the financial system should take into account the unpredictable operating environment in their assessment and management of risks. In a volatile environment, it is essential to be able to respond rapidly to crises that in a modern digital world can spread and intensify instantly.

The Finnish authorities responsible for financial stability are well prepared for a wide range of different crises. They maintain and improve their crisis management preparedness by carrying out regular crisis exercises.[28] In recent years, various improvements have also been made to the operational resilience of the financial system, as part of the comprehensive preparedness arrangements within Finnish society. In addition, the Financial Stability Authority recently assessed the resolution capabilities of Finnish banks.[29] According to the assessment, the banks are well prepared financially, but further improvements are needed in crisis management processes, procedures and IT systems.

Banks should have more buffers that are releasable during disruptions

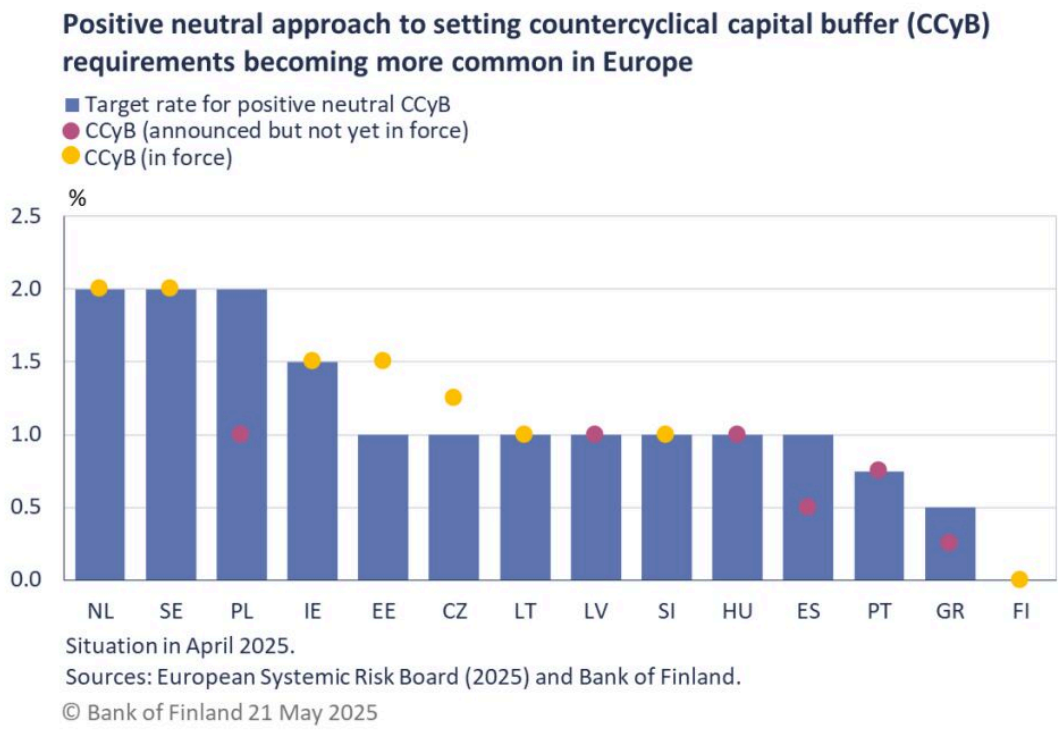
The strong resilience of banks is particularly important for the stability of the Finnish financial system because households and businesses in Finland rely mainly on banks for their financing. Ensuring that banks have sufficient capital adequacy and liquidity is essential in the current volatile geopolitical and geoeconomic landscape. Macroprudential policy must continue to be used to maintain the strong loss-absorbing capacity[30] of the banks and the resilience of households to risks.

Macroprudential policy should also be developed further.[31] Macroprudential authorities are permitted to strengthen the lending capacity of banks, if necessary, by lowering their additional capital requirements in severe stress or crisis situations in the economy. With this in mind, the Finnish macroprudential authority, i.e. the FIN-FSA Board, should have at its disposal more capital buffers that are rapidly releasable than it has at present.

National macroprudential authorities in the EU countries can impose on their credit institutions a countercyclical capital buffer (CCyB) requirement if lending is at risk of overheating. In an economic and financial system crisis, these authorities can, if necessary, lower the requirement in order to strengthen the lending capacity of the banking system.

The CCyB requirement can be relaxed only if the authority has already set a positive rate for the buffer before the onset of the crisis. Many EU countries have started to increase the CCyB rate in the neutral phase of the credit cycle, well before any overheating in the lending market (Chart 14) (see: 'Positive neutral – Proactive use of countercyclical capital buffers increases flexibility in a crisis' (in Finnish)). As a result, the authorities will have at their disposal releasable capital buffers when the situation warrants this. In Finland, the authorities should be allowed to apply a similar procedure for increasing the responsiveness of macroprudential policy.

Chart 14.



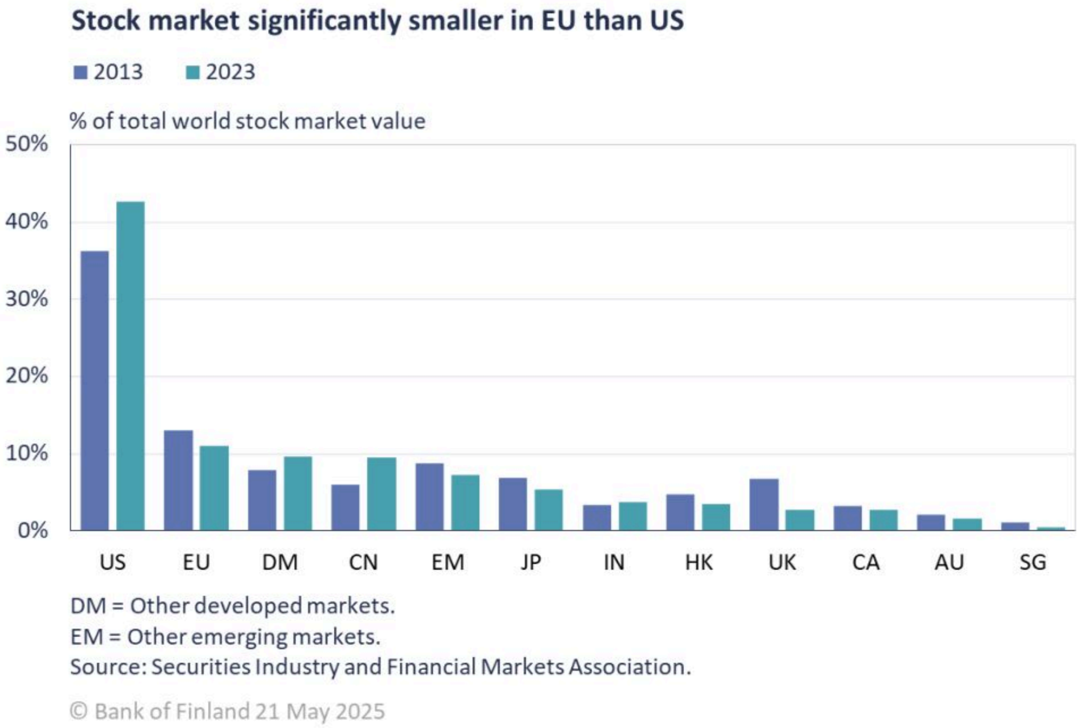
Development of Europe’s capital markets needs new impetus

The European financial system is very bank-centric, and the capital markets are small and fragmented relative to the size of the economy (Chart 15).[32] Efforts have been made for many years to harmonise the capital markets, but with little result.

The European Commission’s new strategy for developing the capital markets was published in March 2025, bringing fresh impetus to the initiative. This is the Savings and Investments Union (SIU) strategy, which is based on earlier plans for a capital markets union and the parallel efforts to complete the banking union.

The aim of the SIU is to improve the way the EU financial system channels savings to productive investment[33] in a difficult geopolitical and geoeconomic landscape in which climate change and technological developments are creating their own challenges. Deeper and more liquid capital markets would boost the competitiveness of Europe, enhance its strategic autonomy and bring greater prosperity to EU citizens.

Chart 15.



Actions to support the integration of capital markets could include harmonising the national legislation of Member States. The SIU objectives include improving the regulation of market infrastructures and dismantling national barriers to the cross-border activity of EU-wide funds. In connection with the harmonisation measures, the European Commission's initiative[34] for a '28th legal regime' should also be analysed. This 28th legal regime would provide innovative start-ups the opportunity to operate in the EU's single market under harmonised European regulation instead of national regulation. Achieving more unified supervision of capital markets and stronger convergence of national supervisory practices would also be useful.

There are large differences between the EU countries in the level of development of their capital markets. Sweden, for example, is significantly ahead of most other countries in this respect. The EU should permit multi-speed regional progress in, for example, the integration of financial market infrastructure.[35]

In parallel with the European project, it is important to develop the domestic and Nordic capital markets.[36] Various indicators show that Finland's capital markets are more highly developed than those of the other EU countries on average, and there is a relative abundance of risk financing for startups. Nevertheless, in Finland there is a need for more equity financing for companies experiencing a strong growth and internationalisation phase. As part of the development of capital markets, Finland could also benefit from the modernisation of the commercial papers market into a more electronic and European market. The EU commercial papers market is quite immature overall, so reforms are necessary in this respect too.

Europe needs more investment and an attractive, diverse array of investment products. Europe has relatively few securities that are safe and have a high credit rating, and for which there is typically high demand.[37] Public sector defence expenditure[38] will lead to European markets having more government bonds to invest in. Countries with the highest debt ratios have little room for manoeuvre in taking on further debt, and Member States must also ensure their debt sustainability. The more robust the credit standing of Member States, the more attractive their government bonds would be to investors.

One way of creating new investment products and freeing up banks' funds for lending is securitisation. Regulation should channel securitisation to forms other than synthetic securitisation, the risks of which are not transparent. Risks to financial stability from synthetic securitisation could increase significantly before they can be identified and prevented.

Banks are significant actors in the capital markets as well. Therefore, the completion of the banking union, an increase in supranational banking mergers and the promotion of cross-border banking business would all speed up the integration of capital markets.

Notes

1. See: Norring, A. (2025), 'Abrupt deterioration in global economic outlook' (in Finnish) – blog post, Euro & talous. ↑
2. See: Kerola, E., Koskinen, K. and Laakkonen, H. (2025), 'Risks arising from international financial system's dollar dependence have increased' (in Finnish) – Euro & talous. ↑
3. In early April, the Trump administration announced a 10% minimum tariff on nearly all US imports of goods and tariffs many times higher for all its key trading partners. Earlier, the US had imposed high import tariffs on China, Canada and Mexico and on, for example, steel, aluminium and cars. Since then, the higher country-specific tariffs have been postponed and, as a rule, 10% tariffs are in force for most trading partners and 30% tariffs for China. ↑
4. If the imposed tariffs remain in force in the long term, they will significantly dampen economic growth worldwide. Likely countermeasures by the United States' trading partners would cause the trade war to spread, further weakening growth. In March 2025, the Bank of Finland assessed that even if the increases in import tariffs were to be lower

than announced in April, this could significantly impair global economic growth in the coming years. See: Anttonen, J., Ikonen, P., Kurronen S., Rönkkö, R. and Vilmi, L. (2025), How will the trade war hit the economy? – Bank of Finland Bulletin. ↑

5. For more information, see the Bank of Finland's March interim forecast: Grey clouds hanging over Finnish economy's recovery – Bank of Finland Bulletin. ↑
6. See: Ikonen, P., Koskinen, K. and Laakkonen, H. (2021), 'Robust measures by central banks returned stability to international dollar markets when COVID-19 hit' (in Finnish) – Euro & talous. ↑
7. The decline in residential property prices seemed to stabilise during the course of 2024, but the beginning of 2025 was still subdued. ↑
8. See: Järvenpää, M. (2024), 'Challenges of property investment market have not undermined financial stability' (in Finnish) – Euro & talous. ↑
9. Finnish real estate companies did not issue any debt securities in 2023. The terms of new bonds issued in 2024 were in many cases stricter than before, especially for higher risk participants. ↑
10. The challenging conditions in the real estate market are making it more difficult to determine property values. ↑
11. The assessed vulnerabilities and their expected trajectories were examined in further detail in last year's stability assessment. Thus, the current assessment focuses more on changes in vulnerabilities and risks that have taken place during the past year. See: Geopolitical tensions and a standstill property market are casting a shadow over financial stability – Bank of Finland Bulletin. ↑
12. The Finnish banking sector is large, concentrated and interconnected with other financial systems, especially those of other Nordic countries. The banking sector is also highly dependent on international market-based finance. ↑
13. See the FIN-FSA's assessment: 'The resilience of Finland's financial sector has remained strong: Risks of a volatile operating environment are challenging risk management' (in Finnish) – Bank of Finland's institutional repository. ↑
14. The Bank of Finland and the FIN-FSA carried out stress testing on banks in 2024: Finland's banking sector could withstand even a harsher recession than forecast – Bank of Finland Bulletin. The European Banking Authority (EBA) is currently performing EU-wide stress tests on European banks. In addition to the EBA's stress tests, the FIN-FSA, together with supervised entities, will conduct a separate national extension of the stress test covering the eight banks directly supervised by the FIN-FSA. The results of the test will be published in August 2025. See: The EBA launches its 2025 EU-wide stress test – European Banking Authority. ↑
15. Loans to households are mainly variable rate loans. Households' vulnerability is further

increased by the fact that a higher proportion of their debt than before consists of housing company loans and unsecured consumer credit. ↑

16. In early 2025, US President Donald Trump signed a decision to withdraw the United States from the Paris Agreement once again. International cooperation between central banks to prevent climate change and its effects also took a step backwards when, in January 2025, the Federal Reserve System announced its withdrawal from the Network for Greening the Financial System (NGFS). ↑
17. See: As the climate crisis worsens, the warming outlook stagnates – Climate Action Tracker. ↑
18. For more information see: Freystätter, H., Kauko, K., Kärkkäinen S. and Määttä, I. (2024), Climate change and biodiversity loss as systemic threats to financial stability in Finland – Bank of Finland Bulletin, and Tolkki, V. (2025), 'Banks are pricing climate change transition risks into their corporate loans' (in Finnish) – Euro & talous. ↑
19. See: 'Key Finnish financial market infrastructure' (in Finnish). ↑
20. International systems, such as SWIFT, connect banks and financial institutions in different countries. Disruptions in these systems could prevent payment transactions worldwide. Technical problems in large stock exchanges and trading platforms could reduce market liquidity and increase volatility in securities prices. Cyberattacks could paralyse banks and payment systems, causing severe economic damage. ↑
21. See: Valtanen, A. (2025), Role of cooperation highlighted amid escalating global tensions – Bank of Finland Bulletin. ↑
22. For more information see: Räsänen, T. (2024), 'Generative AI could revolutionise the financial sector' (in Finnish) – Euro & talous, and Korpinen, K. (2025), 'Payment scam losses have continued to grow in Finland' (in Finnish) – Euro & talous. ↑
23. See: e.g. Määttä, I., Nurminen J. and Räsänen, T. (2023), Instability in crypto-asset markets is a reminder of the risks and underlines the need for regulation – Bank of Finland Bulletin. According to a recent wealth survey commissioned by the Bank of Finland, crypto-assets are owned by approximately 4% of all households in Finland, most of whom own them for investment purposes (approximately 77%). ↑
24. For more information see: Asplund, T. and Vauhkonen, J. (2024), Financial regulation has proved its worth in the turbulence of recent years – Bank of Finland Bulletin. ↑
25. See the Bank of Finland's assessment of public finances 2024: Sustained efforts needed to turn Finland's public debt ratio around – Bank of Finland Bulletin. ↑
26. The FIN-FSA Board has imposed on the entire credit institution sector a systemic risk buffer requirement, due to the sector's long-term structural characteristics and consequent vulnerabilities. In addition, so-called O-SII buffer requirements have been set for three large credit institutions, based on their significance for the Finnish financial

system. Furthermore, the additional capital requirements imposed by other Nordic countries are applied to Finnish banks that have significant lending activity in those countries. ↑

27. Measures that are applied in Finland include the maximum loan-to-collateral ratio (loan cap) for new residential mortgages and the FIN-FSA's recommendations on affordability testing of mortgage borrowers and the stressed maximum debt-service-to-income (DSTI) ratio. July 2023 saw the entry into force of legislation that limits the maximum maturity of new housing loans and housing company loans and the size of housing company loans granted for new-build construction relative to the unencumbered price of the homes for sale. The statutory interest rate cap on consumer credit and the restrictions on the marketing of consumer credit improve the level of consumer protection. ↑
28. The latest joint Nordic crisis simulation exercise was conducted in autumn 2024. See: Nordic Baltic Crisis Simulation Exercise 2024. ↑
29. For more information see: Financial Stability Authority's assessment: banks' resolution capabilities need improvement. ↑
30. For more information see: Topi, J. (2023), Capital buffer requirements included in the macroprudential toolkit are supporting the risk-bearing capacity of banks – Bank of Finland Bulletin. ↑
31. For more information see: Topi, J. (2023), How can Finland's use of the countercyclical capital buffer requirement be further developed? – Bank of Finland Bulletin. ↑
32. See: Ahoniemi, K., Kerola, E., Koskinen, K. and Laakkonen, H. (2025), 'Europe's capital markets must be developed to support investment and growth' (in Finnish) – Euro & talous. ↑
33. For example research by Hoffman et al. (EconL 2020) shows that financial integration is positively associated with economic growth in the EU countries. Heller (Research Pol 2024), in turn, finds evidence on the basis of patents, that banking market integration has spurred corporate innovation in Europe. ↑
34. The Commission introduced the concept of a 28th legal regime in January 2025 in connection with its communication on a Competitiveness Compass for the EU. The Commission will present its proposal for a 28th legal regime at the end of 2025 or in the first quarter of 2026. See: https://commission.europa.eu/document/download/10017eb1-4722-4333-add2-e0ed18105a34_en. ↑
35. See: Nurkka, E. (2025), Trends in European securities settlement (in Finnish) – Euro & talous. ↑
36. See: 'Nordic capital markets could provide a boost for growth financing' (in Finnish) – Euro & talous. ↑

37. See: Välimäki, T. (2025), ‘A safe haven for investment is an anchor for the capital markets’ (in Finnish) – blog post, Euro & talous. ↑
38. For example Germany has approved extensive defence and infrastructure investments to be implemented via debt financing. In many other EU countries too, defence spending will or should be increased significantly. ↑

Key words

banks, financial stability, financial system stability, geopolitics, investment, real estate market