



UNIVERSITY OF GOTHENBURG
SCHOOL OF BUSINESS, ECONOMICS AND LAW

**Basel III and the Latest Requirements on Liquidity Risk
Reporting**
-implications for SEB

Maria Månsson and Johanna Rådström

Graduate School
Master of Science in Finance
Master Degree Project No. 2011:163
Supervisor: Ted Lindblom

TABLE OF CONTENTS

Abstract.....	4
1 Introduction.....	5
1.1 Problem discussion.....	6
1.2 Purpose.....	7
2 Methodology.....	9
2.1 Choice of method.....	9
2.2 Information.....	10
2.3 Choice of respondents.....	11
2.4 Interviews.....	12
2.5 The trustworthiness of the study.....	13
3 Study framework.....	15
3.1 Motives behind the liquidity risk regulation.....	15
3.2 Basel I.....	16
3.3 Basel II.....	16
3.3.1 Pillar 1 – Minimum capital requirements.....	17
3.3.2 Pillar 2 – The supervisory review process.....	17
3.3.3 Pillar 3 – Market discipline.....	17
3.3.4 Shortcomings of Basel II.....	18
3.4 Basel III.....	18
3.4.1 Liquidity Coverage Ratio.....	19
3.4.2 Net Stable Funding Ratio.....	20
3.0 From Basel directives to Swedish law.....	20
3.5.1 Capital Requirements Directive.....	20
3.5.2 Sweden's previous regulations and developments on liquidity risk reporting.....	21
3.5.3 Statement of opinion, FFFS 2011:X.....	23
3.6 Strength and weaknesses with the new liquidity risk regulation.....	24
3.6.1 “Sweden does not need higher restrictions than other countries”.....	24
3.6.2 The quantitative measures.....	25
3.6.3 Overregulation.....	26
3.6.4 The regulatory framework needs to be improved.....	26

3.7 Consequences of a new regulation	27
3.7.1 Competitive environment	27
3.7.2 Transparency and economic welfare	28
3.7.3 Costs	29
4 Case study	32
4.1 Jonas Svärling, Head Risk and Capital Management, SEB Group Treasury	32
4.2 Lars Söderlind, Senior Risk Analyst, the Swedish Financial Supervisory Authority	34
4.3 Olof Sandstedt, Head of Banking Analysis Division, the Swedish central bank	35
4.4 Anders Kragsterman, Liquidity Risk Analyst, the Swedish Bankers' Association	37
5 Analysis and results	38
6 Conclusions	43
6.1 Major findings	43
6.2 Suggestions for further research	45
References	46
Appendix	50

ABSTRACT

The recent financial crisis and the lack of transparency in the banking industry have been the main arguments for the Basel Committee on Banking Supervision to strengthen liquidity risk regulations. This case study based thesis aims to investigate how Skandinaviska Enskilda Banken, SEB, will be affected by the Basel III guidelines concerning the banks liquidity risk reporting. We conduct interviews with representatives from SEB, the Swedish central bank, the Swedish Bankers' Association and the Swedish financial supervisory authority. Previous research studies reject one-size-fits-all models and regulations in general, however the recent financial crisis is a motive of introducing a common regulatory framework. This is necessary for preventing financial turbulence. This thesis has provided us with evidence to conclude that the transparency as an enhancer of banking system robustness is not without controversy. Our findings suggest that SEB as a global actor will be affected in terms of competition since the regulation is not harmonized internationally, the quantitative measures will disfavor SEB's business model and the implementation costs are likely to be transferred to the customers. This thesis show that a common regulatory framework is necessary but the suggested liquidity regulation is not the way to achieve it.

1 INTRODUCTION

As a result from the recent financial crisis Basel Committee on Banking Supervision, BIS, has designed the Basel III accord that highlights the importance of banks' liquidity risk management. The recent financial turmoil manifested the speed of which liquidity may change and that illiquidity may last for a long period of time. The intention with the Basel III regulatory framework is to strengthen banks' capital, liquidity requirements and reporting activities for the global financial system (BIS, 2010a). There has been lack of transparency in the banking system as a result from no common liquidity regulations and liquidity measurements (FS, 2010b). The international guidelines from BIS, motivated SFAS to perform a renewal of the previous regulatory code for public disclosure during the end of 2010; FFFS 2010:12. This constitution adds the liquidity risk perspective since the former regulation under Basel II was limited to cover only the credit-, market- and operational risks. At the same time, SFAS also settled a new regulation with instructions for how the liquidity risk should be managed by the banks, FFFS 2010:7. In order for SFSA to monitor the banks' ability to follow these guidelines they have also presented a new regulation regarding the banks reporting on liquidity risk, defined as FFFS 2011:X (FFFS 2010:3) that will be put into force on 31 July 2011. SFAS goal is to a larger extent obtain information that allows for an improvement of monitoring the liquidity risk among the banks and to achieve a greater and a more comprehensive view of the liquidity position.

This thesis reflects the effects of the new liquidity reporting requirements on one of the four largest banks in Sweden; Skandinaviska Enskilda Banken, SEB. The emphasis on SEB is motivated since the bank is a global actor operating in twentieth countries (SEB, n.d.), and will indeed be affected if there exist differences internationally in the regulations followed by Basel III. It should also be kept in mind that SEB's Baltic investments have been highly criticized and that during the recent financial turbulence the share price decreased several percent in May 2009 when the Swedish central bank claimed an increased share of foreign currency in order to provide the bank with liquidity (Forsberg, 2009). To conclude, it stands clear that SEB will be affected by the new liquidity regulation. The regulatory focus on banks liquidity risk reporting is carefully chosen since the problem with illiquidity was clear during the recent financial crisis. In addition, the importance of banks liquidity risk management has been widely discussed in the public debate and SFAS has argued that liquidity is one of the largest threats in the Swedish banking system (FS, 2010a). It should be mentioned that this thesis is limited to involve the reporting part of the new regulation and does not include the changes on the capital requirements.

1.1 PROBLEM DISCUSSION

The following section represents the benchmark for this study. Previous research and the subsequent stated hypotheses form the base for the structure of this thesis. This section serves as a reference frame for how to investigate the effects on SEB as a consequence of the new liquidity reporting requirements.

Financial crises have a huge impact on the worldwide economy. Contagion bank runs may cause aggregate liquidity shortages (Diamond and Rajan, 2005) and risk-based capital requirements may be regarded as socially desirable (Parlour and Plantin, 2008). Also more informative and timely reporting will result in a decreased likelihood of a future financial crisis (Tadesse, 2006) and Nier and Baumann (2006) argue that transparency gives a lower probability of default. It should however be kept in mind that private monitoring has nothing to do with banking fragility (Barth, Caprio and Levine, 2004). The phenomenon of bank runs applies even if the causes of the problems are only rumors and the bank is fundamentally sound. Providing external information enables the bank to reflect that it truly understand its business and the potential risks of its operations. This is also a chance to attract investors by showing that it is able to run operations prudently. If the bank successfully accomplishes this it will have taken a huge step towards rebuilding confidence and restoring the health of the financial system (Barfield and Venkat).

A result of non-confidence for the banking sector is unexpected withdrawals, which are pointed out by Song and Thakor (2007) and Schertler (2009), who argue that financial institutions may use different marketable securities in order to avoid banking fragility. Previous research creates a reason for investigation: Will the new reporting guidelines be a sufficient instrument for rebuilding the lack of confidence in the banking system? Banking operation is a commission of trust and SEB together with the banking industry need to rebuild the confidence for the financial sector. This is a challenge since liquidity risk is complex, noisy and hard for banks to manage and for the supervisors to monitor. The complex hazard can quickly cause harm that can easily be spread into the entire banking system. The soundness in the banking industry will indeed affect SEB as a result from a more integrated banking sector; this highlights the need for analyzing how a higher regulating discipline will affect SEB in terms of economic welfare.

The new accord is not likely to fully eliminate systemic risks and does not involve the issue of shadow banking as stated by Atkinson and Blundell-Wignall (2010) and Jaffee and Walden (2010). Further Atkinson and Blundell-Wignall (2010) question the importance of one-size-fits all models. Basel III suggests quantitative ratios to measure the banks liquidity risk management, which raises a question of how SEB will be affected in terms of fulfilling the quotes and communicating them? Since SEB recently has managed to complete the challenges from Basel II there is also a reason for discussing the risk of overregulation in the banking system, as the banks might be forced to deviate from core functions and the task of providing an efficient resource allocation. Thakor (1996) claims, that stricter regulation reduce aggregate bank lending. Banks with higher costs of capital lend less and will be more affected by capital

requirements. Bonds will replace a high degree of the founding of mortgages, which nowadays are short-term certificates (FSR, 2010 and Anonymous, 2010f). This creates reasons to believe that the new regulation will result in higher costs, however what type of costs will arise, and what impact will they have on the customers? Furthermore, SEB is highly affected by the competitive environment which makes it important to investigate how stricter transparency requirements for Swedish banks will affect SEB in terms of national and international competition? Based on the background from these underlying issues the following research question is defined as;

How will SEB be affected by the Basel Committee suggestion of an increased regulation of reporting regarding the banks liquidity risk management?

1.2 PURPOSE

Illiquidity and the following consequences were obvious during the latest financial crisis when the banks' liquidity reserves were not sufficiently liquid (Atkinson and Blundell-Wignall, 2010 and FS, 2010a). As a result banks experienced difficulties to manage liquidity in a prudent manner during the early phase of the financial crisis in 2007 (BIS, 2010a). The purpose of this thesis is to explore the effects on SEB due to the new liquidity regulations as a result of the latest financial crisis in terms of competition, costs, risk of overregulation and changes in economic welfare. Also, the paper attempts to provide an overall presentation of SEB's challenges and benefits during the implementation.

This study is motivated since the problem discussion creates reasons to investigate if the latest regulation "will throw out a baby with the bath water". We believe that the intention with the new regulation is good but there is a need for analyzing how it will hold in practice. By identifying how SEB and their stakeholders will be affected we hope that the regulators will gain information to evaluate the new rules and help them maintain the good part and divest the bad part. The baby (the positive part of the regulation) in this sense would be the need for liquidity regulations that has been motivated. The bathwater (the dirty part) represents consequences that might not be straightforward and might even worsen the situation for the banks. This study is of interest since it investigates how SEB as a global actor will be affected of stricter liquidity reporting requirements. Liquidity risk is complex which makes it hard to determine the consequences of such regulation (FS, 2010a). The following motive with this study is therefore to show customers, regulators and SEB itself what effects that will appear and that factor such as business models and competitive environment will contribute to differences when facing stricter liquidity regulations. This thesis attempt is to provide a guideline for the effects that will occur and also function as a reminder that regulators should include a broader perspective such as the previous mentioned factors when implementing liquidity regulations.

This thesis is organized as follows: Section 3, reference frame of the study, presents a short background of the regulatory development for the Basel accords in order to understand what the latest requirements will add to the previous framework and what the international suggestions will entail. The next part of this

section describes how these recommendations will affect SEB and how SFSA governed by EU-directives will put them into Swedish law. It is necessary to know at which extent SFSA follows the international guidelines in order to analyze their impact on SEB. Section 3 ends with findings from empirical research and comments of the new liquidity regulation from the public debate. This part identifies strengths and weaknesses with the new regulation that is needed to create an implementing overview for SEB. By presenting consequences of the new regulation in the environment where SEB operates, gives inputs and impressions of the operational and strategic implications that will affect SEB's liquidity risk management. The section focuses on economic welfare, competition, implementing costs, banks' ability to meet the standard ratios and the risk of overregulation. This selection developed as these subject appeared most frequently in the public discussion and earlier studies. The study framework provided the outline for the questions given to the respondents. The section gave an understanding of the type of information that needed to be collected and from whom. The choice of respondents is straightforward; the regulators that set the liquidity framework and the industry that will be the subjects to it. The former is represented by SFSA and the Swedish central bank, SEB and the Swedish Bankers' Association represents the latter.

Section 4 involves a summary of four interviews based on the previous mentioned topics with respondents representing both the industry as well as the regulatory side. The meetings with the respondents add a closer interpretation of how the Swedish banks will be affected by SFSA's latest regulatory codes on liquidity risk reporting. The goal is to explore the implementing challenges and assess possible contribution for SEB using representatives from different businesses. Section 5 provides the findings from the performed study and compares the result to the information gathered from the case study and the study framework in order to discuss and link new input and the own hypothesizes stated above with former research on the subject. This is the basis for the final part, section 5, which presents conclusions about how the new liquidity regulation will affect SEB.

2 METHODOLOGY

Since the latest liquidity requirements are newly introduced and part of the rules has not yet been settled, it is natural to use a case study approach to explore possible future outcomes. We do not see another possible method to explore the chosen research area. A limitation of this study is the inability to provide an elaboration in the research area. This is a consequence of the fact that part of the new liquidity requirements has not been put into force and that this thesis is written in an early phase of the implementation period of the new liquidity requirements. It is therefore appropriate to exclude financial data since SEB have not revealed information concerning its current status and its ability to meet the new requirements. Information about financial data in this stage is regarded as confidential and SEB does not expose such since it will harm its competitiveness. Previous annual reports do neither include SEB's liquidity position nor comments on the liquidity situation since this has not been regulated in earlier frameworks such as Basel I and Basel II. Since this thesis focuses on liquidity reporting, the financial data given in annual reports is not of interest and will not be presented.

2.1 CHOICE OF METHOD

The thesis assesses a discussion of possible positive and negative outcomes for SEB due to SFSA's regulatory suggestion FFFS 2011:X as well the public disclosure FFFS 2010:12. Since the effects are hard to determine (FSR, 2010) we have been using an explorative case study design and for that purpose it is necessary to use a descriptive research approach. Since a case study based approach is chosen this thesis explores how the new regulation will affect SEB by generating hypothesis. Esaiasson, Gilljam, Oscarsson and Wägnerud (2004) argue that a case study approach is flexible and invites to a closer contact with the real world by interacting and discussing the underlying issues with the respondents. The thesis involves an investigation and descriptions, connected to individuals with experience that are active in different industries (Patel and Tebelius, 1987). When using a descriptive research it is appropriate to apply a qualitative approach. The qualitative approach allows us to search information from different sources and will increase the flexibility with the study of a new research issue (Lundahl and Skärvad, 1999).

The study framework provides different views from empirical research and the public debate concerning the new liquidity framework and is the starting point for the questions given to the respondents. It did also provide information regarding the choice of suitable respondents and their contribution to this study. The choice of respondents is straightforward; the regulators that set the liquidity framework and the industry that will be the subjects to it.

In total this thesis includes four case studies that are representatives from each business that they operate in, separated into two groups representing the industry as well as the regulators side. From the industry angle the representatives are from Swedish central bank and SFSA, and SEB and the Swedish Bankers' Association represent the industry side. As already described, those are chosen since they represent the regulators as well as the target of the liquidity requirements. The choice of respondents will now be described more carefully. SFSA is chosen since the authority develops and sets the national regulations based upon Basel III. SFSA is a supervisor and the Swedish banks are required to submit their reports to the authority¹. The Swedish central bank is preferred since it is responsible for the financial stability and is engaged in questions regarding regulatory frameworks². It is necessary to include this angle since it will give a deeper insight in how the Swedish economy will be affected. The Swedish Bankers' Association represents 28 national and international members that are banks, real estate and financial institutions and presents statistics, publications and newsletter to the society regarding the situation on the Swedish banking market³. Since the association represents the banking industry in general, it is valid as a source in the case study and provides an overall view from the industry as a consequence of the liquidity requirements. Lastly, SEB is chosen since this thesis focuses on this financial institution and it is desirable to use a respondent from this bank as a source to reveal opinions and shortcomings due to the new regulation.

2.2 INFORMATION

The reference framework of the study is based on publications from BIS, SFSA, the Swedish Bankers' Association, papers from financial journals, other reports and internet sources revealing information considering regulations and the following consequences as well as transparency. BIS and SFSA are chosen since they propose the regulation. They are well known authorities and we do regard them as reliable and valid. The Swedish Bankers' Association represents as already mentioned several banks. This source is regarded as valid since the association represents the members towards authorities both nationally and internationally. The criteria for the choice of other references are that they have to be published by well-known publishers and journals. The empirical section is based upon data collected by interviews. We attempt to relate all sources in a critical manner throughout the thesis. It should however be kept in mind that the theoretical base is limited due to the fact that Basel III is a new regulation. Since this thesis is based upon interviews, it is necessary to mention following shortcomings. Esaiasson et al (2004) argues that a problem that might arise when conducting the interviews is the risk of interviewer effects, and the possibility of affecting the answers provided by the respondent. This risk of unwanted effects in the interplay between the respondent and the interviewer is higher in personal, face-to-face interviews, however this problem is somewhat counteracted by its strengths in the form of a greater control of the answer situation.

¹ Source: <http://www.fi.se/Om-FI/Verksamhet/Det-gor-FI/Tillsyn/>

² Source: <http://www.riksbank.se/templates/Page.aspx?id=27347>

³ Source: <http://www.swedishbankers.se/web/bf.nsf/pages/ombank.html>

2.3 CHOICE OF RESPONDENTS

The respondents are considered as sufficient representatives for expressing their view and the employers' official perception of how the Swedish banks will be affected by the latest regulation. The selected input from interview people is valued as reliable since we have controlled their resume of former job assignments. The trustworthiness of the respondents are high since they share working experience from risk management, and also that they have a jointly background from the banking sector where all have had SEB as an employer. This secures a trustworthy reference frame for the final discussion and analysis of how the SEB will be affected of the new liquidity requirements. Below is a background presented to each respondent. The referencing to these sources is interview and e-mail correspondence.

Jonas Svärning was recruited to SEB as a capital manager 2004 and has developed internally and becoming Head of Risk & Capital Management at SEB Group Treasury. Svärning has both a Master of Science degree in economics as well as a master of science degree in engineering. Svärning qualifies to be our main contact person in SEB since his role involves managing and controlling for SEB's financial stability, and ensuring that the bank has a suitably large buffer of equity and adequate liquidity position. He is currently mainly concentrating on the task of implementing the rules from SFSA followed by BIS.

Lars Söderlind was recruited to SFSA in 2005 as a senior risk analyst for his proficiency in the area of market and liquidity risks and Basel II. Prior to this he held the position as a finance risk consultant at Ciceron where he provided independent consultancy services to banks, savings banks and credit market companies. At the same time he also worked as a regional director at PRMIA Sweden focusing on asset & liability management, ALM, and financial risk management and Basel II. Until this employment Söderling work as a director and senior analyst at KPMG Consulting where he was engaged as an expert in ALM for banks, financial risk management as well as Basel II. Söderlind has also worked within the SEB Group as a manager for the Trading & Capital Markets Department. Further, he has been Vice President for Group Treasury as well as Vice President for Group Risk Control at SEB. Söderlind has a Master of Science degree in economics. His expertise in the area of Basel regulations and liquidity risk management is broad and useful. This together with his career at SEB makes him an important candidate for providing valuable inputs to this study since he has experienced both the industry as well as the regulatory side. The motivation for meeting Söderlind is strengthened by the fact that he is SEB's contact person during the implementation of Basel III. Further, he has a personal contact with Svärning and visits the bank on a regular basis in order to control and monitor SEB's risk operations.

Anders Kragsterman currently works as a specialist at the division of economic analysis at the Swedish Bankers' Association. Until this employment he worked as a deputy head of the financial stability department at the Swedish central bank. Prior to this, Kragsterman worked at SEB group at the unit of Group Credits. Since the mid 1990's he has been one of the senior executives in the development and implementation of SEB's quantitative risk models. Kragsterman has a Master of Science degree in

economics. He has, in comparison with Söderlind, also worked on the regulatory as well as the industry side, which has provided us with input in terms of perspectives from both sides. The fact that Kragsterman has experience from working with forming SEB's quantitative ratios in a period before the new standards has been introduced might cause an bias view since he is used to the previous methods. This adds a risk of subjective input that favors the period before when the banks were able to choose their own methods for communicating the risk. On the other hand, he has knowledge in SEB's ability to meet such regulations.

Olof Sandstedt has been employed at the Swedish central bank since 2007 where he currently holds the position as Head of the Banking Analysis of the Financial Stability Department. Before this he worked at JP Morgan in London with risk Management during 2005 - 2007 and prior to that he worked at SEB. He has a Master of Science degree in economics. Sandstedt and his unit controls for the soundness in the Swedish banking sector and identify the major banks' ability to meet the risk that they are exposed to. These monitoring operations as well as the experience from the industry make him an important candidate to analyze SEB's current position and the ability to meet the restrictions from SFSA.

Tobias Lindqvist has been employed at SFAS since 2009 and is currently working as a senior risk analyst. Prior to this he operated at Econ as a consultant with focus on risk management for two and a half year. Lindqvist will finish his employment at SFAS in august 2011 for an employment at SEB Group Treasury as liquidity risk manager. Lindqvist has a doctor of philosophy in economics. His competence regarding SFAS regulatory codes and the implementation of Basel makes him a good complementary source to Söderlind. It should be mentioned that Lindqvist is not a respondent in the conducted interviews, however we have used him as a source using e-mail correspondence. This source should not be confused with the publication written by Lindqvist that is also used in this thesis.

2.4 INTERVIEWS

In qualitative research the interviews tend to be less structured. This is a result from the fact that individuals tend to interpret questions in a different manner. There are two interview methods that are used in qualitative research, the unstructured and the semi-structured interview. The latter is known as the interviewer prepares questions before the interview. Furthermore the respondent gives a larger space in which the answers will be made (Bryman, 2001).

In this thesis we have chosen a semi-structured method. The method is chosen since the chosen research area demands a particular structure in order to compare the answers of the respondents. Such a method is preferred since it allows the interviewer to ask attendant questions (Bryman, 2001). The interviews have given different answers even though the same questions have been asked.

All interviews have occurred through personal meetings. This is motivated by the fact that individual contact will create a stronger relationship and allows for a more qualified and gradate analysis of the

answers. However, in order to avoid misunderstanding we were promised to contact the respondents if further questions appeared. This caused complementary telephone and e-mail dialogues in order to meet approaching wonderings during the study.

It is necessary to mention the ethical aspect of the performed interviews. This issue is of particular importance when a participation in an interview creates a risk of hurting the respondent. Such a situation may arise when confidential information appears during an interview without being treated in a trustworthy manner (Bryman, 2001). We believe that the respondents have the knowledge to decide whether to leave appropriate information or not. We assume that they have received the awareness of what is classified as confidential material from their employer and that they are familiar with the purpose of the interview. All of the respondents have in advance received the questions that have given them time to prepare and the possibility for creating a standpoint. The answers from Svärning (2011) have been given in general terms since specific strategies and data are private information. This action is a pure competition issue and it should be kept in mind that more detailed information about NSFR and LCR at this point in time not has become public information. The risk of causing any personal or businesslike harm has been avoided in the sense that the respondents have been asked if they would like to be anonymous or not.

2.5 THE TRUSTWORTHINESS OF THE STUDY

Since the research area is not widely discussed and that the results are based upon interviews this paragraph is of great importance. In order to judge the trustworthiness of the thesis it is appropriate to regard the concepts of reliability, simultaneously and independency (Bryman, 2001).

We do regard this study as highly reliable. The arguments behind the statement are that the respondents have relevant experience and knowledge and that we have had a deep contact with SEB. Since the interviews might be infected by self-interest this can be regarded as a problem. Such self-interest might be avoided due to the participation of independent authorities such as SFSA and Swedish central bank.

In order to argue for the requirement of simultaneous information we regard this as fulfilled. Basel III is in an implementation period and the banks do prepare the new framework. All respondents are updated in this area and have been provided with the same guidelines that ensure that all given information are based upon most actual facts.

Another aspect is the conflict of interest that might have developed during the study. Our empirical research has a strong connection towards the industry, which might have influenced us to be driven in certain direction. If that is the case, it is of importance that the reason is presented. As already mentioned we have an established relationship with SEB, but we do not reject the possibility that this has caused an impact of the content of this thesis.

Since our questions to the respondents were sent in advance we consider the conditions for equality to be fulfilled. We are aware of the problem that the respondents might have prepared to answer the questions in a particular manner in order to hide certain information.

3 STUDY FRAMEWORK

The following sections 3.1 until 3.5 are of relevance since they contribute to an understanding in the developments of the Basel regulations. These sections give a background to Basel III by introducing Basel I and Basel II. It is necessary to include those as two components since this thesis is based upon the latest regulatory framework Basel III and its contribution to maintain stability on the financial markets. Since this thesis in particular focus on liquidity reporting in the Swedish market it is clear to include the developments of the Swedish constitutions that are based upon the general guidelines from BIS.

Section 3.6 and 3.7 are important since they provide the general view of consequences facing banks due to regulatory frameworks in general and Basel III in particular. The sections give an insight in how the Swedish banks will be affected of stricter regulations and are a guide of understanding how SEB will be affected of the new liquidity requirements. The sections do also give a deeper understanding of the current environment and what challenges SEB will face before and after the implementation phase.

The section as a whole serves as a benchmark for the questions during the conducted interviews. This gives the stated results and conclusions reliability since we are able to compare the answers from the interviews with empirical findings and comments from the public debate.

3.1 MOTIVES BEHIND THE LIQUIDITY RISK REGULATION

Liquidity is one of the largest threats in the Swedish banking system and the degree of transparency regarding this is insufficient. The liquidity exposure and the following consequences stress the importance of promoting financial stability and the ability to measure the solvency of banks. There is a need for techniques in order to identify the strengths and weaknesses in the banking liquidity risk management. One explanation for the latter is that there has not been any harmonized ways to measure liquidity risk (FS, 2010a).

Before the recent crisis occurred the banks provided a low degree of information revealing exposure to liquidity risk. Since the liquidity framework was unclear, the provided information was in general not comparable among the banks. There are several reasons to support stronger actions towards a higher transparency in the banking system. A new regulation will promote a sound market, as investors will be able to measure the risks facing a bank, which reduces uncertainty in the sector. The increased reporting requirements will create opportunities for the banks to analyze liquidity risk exposure in relation to the competitors (FS, 2010a).

The US banks as well as the European banks were hit by the liquidity problems when Lehman Brothers went bankrupt in the autumn 2008. The whole global banking system was negatively affected as a

consequence of the break down which forced the central banks worldwide to intervene. Two factors did contribute to the recent financial crisis, partially that the banks were dependent on short-term financing and that the liquidity reserves were not sufficiently liquid. The liquidity risk management was neglectful before the crisis as a consequence of a clear regulatory framework. This was manifested in several ways. The banks reduced their share of deposits which were replaced largely by financing on the market. Market funding was often of a short-term nature, which means a refinancing risk, as the bank will not be able to renew debt as it matures. Meanwhile the liquidity reserves for covering unexpected outflows were not as liquid as the banks did expect (FS, 2010a). As a result from the recent financial crisis, the Basel Committee proposed under the Basel III framework two liquidity risk ratios; the Liquidity Coverage Ratio (LCR) and the Net Stable Funding Ratio (NSFR), these are elaborated in sections 3.4.1 and 3.4.2. Also a new non-risk weighted leverage ratio is suggested in order to ensure regulatory capital and underlying risk, this ratio will not be further investigated since it involves the capital part of the new Basel III regulation.

3.2 BASEL I

New capital regulations were suggested in the 1980s by BIS in order to avoid competitive conflicts and to ensure that banks had enough capital for absorbing losses. This regulatory framework is later known as Basel I and the capital regulation was implemented in 1992 after developments and consultations (Atkinson and Blundell-Wignall, 2010). The introduction of Basel I was followed by two new risk-based capital ratios with the purpose to minimize capital risk by having minimum capital requirements. By using risk weights and risk categories for off balance sheet (OBS) items, the banks were able to calculate the minimum capital levels. Basel I was revised in 1998 since it suffered from lacks on market risk exposure measurements (Cornett and Saunders, 2009).

This one-size-fits-all approach was criticized among financial institutions and scholars. It was claimed that this and the asset risk-weights in combination with other issues provided an opportunity for “regulatory arbitrage” (Lindblom, Olsson and Willeson, 2008), underestimation of liquidity risk and encouraging of OBS activities (de Larosière, 2009).

3.3 BASEL II

The response came when BIS introduced Basel II that involves different possible approaches for measuring risk that was implemented in 2007. Basel II consists of three pillars, where the first pillar covers capital requirements for credit, market and operational risk. The second pillar includes a regulatory review process and provides tools for dealing with risks such as concentration risk, strategic risk, reputation risk, systemic risk, legal risk and liquidity risk (BIS, 2005).

3.3.1 PILLAR 1 – MINIMUM CAPITAL REQUIREMENTS

The purpose of pillar 1 is to ensure that financial institutions have a minimum level of capital for covering credit risk, market risk and operational risk (Thoraval, 2006).

Capital is divided into two parts, tier I, tier II and tier III. Tier I includes common stockholders' equity, qualifying cumulative and non-cumulative perpetual preferred stock, called tier I. Tier II involves allowance for loan and lease losses and is also known as supplementary capital. The total capital is then tier I + tier II less deductions. The core capital has to equal or exceed 4 percent and the total capital has to equal or exceed 8 percent (Cornett and Saunders, 2009). Tier III involves capital that is held in order to meet market risks, commodities risk and foreign currency risk. Tier III capital must be limited to 250% of tier I capital, be subordinated, have a minimum maturity of two years and be unsecured (BIS, 2010a).

3.3.2 PILLAR 2 – THE SUPERVISORY REVIEW PROCESS

Pillar 2 requires banks to use and develop risk management techniques in terms of monitoring. Banks are expected to demonstrate that the internal capital targets are consistent with their risk profile and operating environment (BIS, 2005). Pillar 2 captures bank-specific uncertainties that are not fully considered under pillar 1 (basic minimum requirements), e.g. interest rate risk in the banking book, strategic and business risk. The pillar involves a process of supervision which strengthens and complements pillar 1 and uses a methodology in order to measure risk and internal processes used by institutions to monitor them (Thoraval, 2006).

The supervisor has to ensure the requirements are fulfilled on an ongoing basis. The supervisor should evaluate the capital needs in relation to the risk profile and when appropriate intervene to fulfill the minimum requirements (Thoraval, 2006). The interaction should promote a dialogue between supervisors and the banks. Furthermore the supervisor may use a focus approach on the bank that needs special attention if there is a certain risk profile or operational experience (BIS, 2005). More precisely, principle 2 of pillar 2 states that: "Supervisors should review and evaluate banks' internal capital adequacy assessments and strategies, as well as their ability to monitor and ensure their compliance with regulatory capital ratios. Supervisors should take appropriate supervisory action if they are not satisfied with the result of this process." (BIS, 2005, p. 167). The senior management or board of directors should receive regularly reports that reveals the current risk profile and capital levels (BIS, 2005). Adequate systems in order to monitor and report risk exposures shall be used. If there is a need for capital due to changes in the risk profile this is required to be revealed (BIS, 2004).

3.3.3 PILLAR 3 – MARKET DISCIPLINE

Pillar 3 is developed in order to increase the transparency of financial institutions by requirements of rules, regarding i.e. disclosure of risk exposure and capital adequacy (Cornett and Saunders, 2009). Market discipline is encouraged by a set of disclosure requirements that allows market participants to assess key information on risk exposure and capital adequacy (it should be noted that liquidity risk is not

included). The purpose of pillar 3 is to complement minimum capital as stated by pillar 1 and supervisory review process (pillar 2) and that it does not conflict with the requirements under accounting standards. A general summary of the risk management policies and objectives, reporting shall be published annually. On quarterly basis tier I and capital adequacy ratios and components are expected to be reported. Banks are required to submit information as soon as viable and not exceed deadlines (BIS, 2005).

3.3.4 SHORTCOMINGS OF BASEL II

The recent financial crisis has shown that the previous regulatory framework for the banks, Basel II, does not capture the risks of banks' adequately. Even though the capital level has been higher than required due to Basel II several large banks in USA and Europe went bankrupt in the recent financial crisis. None of the Swedish banks have failed, but Swedbank was forced to issue new stocks despite the fact that their reported core capital exceeded the required level. Further, the main problem with Basel II is not the limits; it is the measure of the risk-weighted capital. The more supply, the fewer shares have to be reported which gives a higher core capital degree given the same equity level. Since equity is expensive, the reported rate of return will be smaller. This in turn has caused a race towards lower levels of risk-weighted capital (Billing, 2009), which also has been stressed by Ingves (2011).

BIS proposed several changes in the banking book requirements in Basel II due to the financial crisis. The disorders in the asset-backed commercial paper (ABCP) caused banks to buy such papers issued by conduits. As a result the banks did raise liquidity and/or credit enhancement. The Basel Committee solves the issue whether a bank could use ABCPs to risk-weight when the rating depends in part upon the bank's own ratings and support. Further in Basel I, ABCP are classified differently in the IRB and standardized approaches where eligible asset are tested in how they prevent liquidity providers from funding assets that are significantly delinquent (Bake, Hawken, Hitselberger, Hugi and Kravitt, 2010).

Previously capital requirements for trading book exposures have focused on market price and interest rate risk, conversely to credit risk, i.e. banking book capital requirement. The market risk rule is referred as credit and related risks which are meant to address general market risk and specific risk. It is in the trading book that the majority of losses have occurred and the Basel Committee has developed the capital framework in order to capture the missing key risks (Bake et al, 2010).

3.4 BASEL III

Despite adequate capital levels many banks experienced difficulties to manage liquidity in a prudent manner during the early liquidity phase of the financial crisis in 2007. The following severe stress that occurred in the banking system is a proof of how fast liquidity can change and that illiquidity may last for a longer period of time (BIS, 2010a). There has been a lack of transparency as a result of no common liquidity regulation, system of rules and how to measure liquidity (FS, 2010b). A more tightened regulation will lower the risk for future financial crisis as a consequence of a more efficient allocation of capital and a financial system with more robust banks (PR, 2010).

The overall aim of the new framework, Basel III, is to strengthen the ability to withstand losses and to reduce the likelihood of a new financial crisis. Basel III requires banks to hold more capital, to improve the quality and the liquidity (FS, 2010b). It is suggested to change the requirements of tier II and tier II and to remove tier III (BIS, 2010a). The various components of the Basel III accord will be rolled out over the coming years, starting in 2013. However, market forces might require the banks to meet the rules on an earlier stage (FS, 2010b).

The difference between reporting regulation between Basel II and Basel III is the introduction of stronger disclosure standards. The Basel Committee has increased the supervisory review process under pillar 2 with additional areas such as corporate governance, risk appetite, risk aggregation, and stress testing (by the liquidity coverage ratio, see below). Complex capital markets activities under pillar 3 is also revised.

3.4.1 LIQUIDITY COVERAGE RATIO

LCR is developed in order to promote short-term resilience of the risk profile by securing that the bank has sufficient high-quality liquid assets (defined as easy to convert into cash with no or a small loss of value) in order to survive a stress test scenario lasting for a month (FS, 2010a). The ratio is built upon the coverage ratio used internally by banks to assess exposure to uncontrollable liquidity disorders. LCR is introduced as a consequence of the events that occurred in the global financial crisis in 2007 with both systemic and institution-specific shocks. It assumes a significant downgrade of the institution's credit rating, loss of deposits, losses of unsecured wholesale funding and increase in contractual and non-contractual OBS exposures and derivative collateral calls (BIS, 2010b). Banks are expected to meet LCR requirement continuously and the standard requires that the stock of high-quality liquid assets should be (at least) equal to the total net of cash outflows, i.e. the ratio should be no lower than 100% (BIS, 2010a). The liquidity cash is allowed to contain government bonds and at most 40% of corporate and mortgage bonds (FS, 2010a). A report from the Swedish central bank⁴ states that some of the Swedish banks do not fulfill LCR. In order to increase the ratio it is necessary to raise government bonds or reduce their 30 days net outflow. Securities and deposits with more than a one year maturity classifies as 100% stable (FS, 2010b). LCR is defined as⁵;

$$\frac{\text{Stock of high quality liquid assets}}{\text{Net cash outflow over a 30 days period}} \geq 100\%$$

The term total net cash outflow is defined as the total expected cash outflows minus total expected cash inflows in the specified stress scenario for the subsequent 30 calendar days. Retail deposits are defined as deposits placed in a bank by private customers. The retail deposits are divided into "stable" and "less stable" where stable deposits are deposits fully covered by an effective deposit insurance scheme or by a public guarantee that provides equivalent protection. It is also important that the depositors have

⁴ Source: http://www.riksbank.se/upload/Dokument_riksbank/Kat_publicerat/Rapporter/2010/FS%202010_2/fs_2010_2_sv_ruta5.pdf

⁵ Source: www.liquidity-coverage-ratio.com

established relationships with the bank so that deposit withdrawals are unlikely. The relationship can be defined as transactional accounts in which salaries are automatically deposited. The deposit insurance itself is not enough to consider a deposit “stable”. If a bank is not able to determine which deposits that are covered by effective deposit insurance scheme or a sovereign deposit guarantee it should place the full amount in the “less stable” buckets as established by its supervisor. Foreign currency deposits will be considered as “less stable” if there is a reason to believe that such deposits are more volatile than domestic currency deposits (BIS, 2010a).

3.4.2 NET STABLE FUNDING RATIO

NSFR is developed in order to promote resilience over a longer period of time by forcing the banks to fund their activities with more stable sources of funding. The ratio provides a sustainable maturity structure of assets and liabilities. Further, NSFR is structured to ensure that long-term assets are funded with at least a minimum amount of stable liabilities in relation to the liquidity risk profile. None of the Swedish largest banks fulfills NSFR (FS, 2010a). NSFR is defined as⁶:

$$\frac{\text{Available amount of stable funding}}{\text{Required amount of stable funding}} \geq 100\%$$

The available amount of stable funding (ASF) is defined as the total amount of capital, preferred stock with maturity of equal to or greater than one year, liabilities with effective maturities of one year or greater. Also portions of non-maturity deposits and/or term deposits with maturities of less than one year that would be expected to stay with the institution for an extended period in an idiosyncratic stress event and the portion of wholesale funding with maturities of less than a year that is expected (BIS, 2010a). The required amount of stable funding (RSF) is the sum of the value of the assets held and funded by the bank multiplied by a specific required stable funding. This is added to the amount of OBS activity, or liquidity exposure, multiplied by the associated RSF factor. RSF is determined by supervisors and reflects the need of stable funding. Lower RSF indicates assets that are more liquid and more available in a stressed environment, which requires less stable funding and vice versa (BIS, 2010a). NSFR is based on net liquid asset and cash capital methodologies that are used internally by bank analysts, rating agencies and banking organizations. The methodology when computing amount of all illiquid assets and securities that should be backed by stable funding is regardless of accounting treatments. Funding is also required to back up at least a small part of potential calls on liquidity arising from OBS activities (BIS, 2010a).

3.0 FROM BASEL DIRECTIVES TO SWEDISH LAW

3.5.1 CAPITAL REQUIREMENTS DIRECTIVE

The Basel Committee on banking supervision presents recommended regulatory changes, in practice governed by EU directives and local regulators following Basel framework. The European Commission will present proposals regarding the capital adequacy requirement, CRD IV, during spring 2011, which

⁶ Source: www.net-stable-funding-ratio.com

means that the final arrangements can be expected to be completed at the earliest in the end of 2011 (SBA;1, 2010). The new banking supervisory authority, European Banking Authority (EBA) develops the implementation of Basel III into the CRD IV and the reform of EU legislation as well as binding technical standards. The main objective is to establish a single rulebook for banks with liquidity and capital regulation as the most important components (Huertas, 2011). In order for CRD IV to be applied in Swedish law it has to be approved in this EU directive (European Commission, 2010).

The proposed CRD IV supplements CRD III (adopted in July 2009) and CRD II (adopted in October 2008). CRD II covers improvements related to exposures, supervision, qualitative standards related to liquidity risk. CRD III is covering amendments of capital requirements for the trading book, disclosure of securitization and remuneration policies. Since the financial markets are weak due to the latest crisis, the Commission is attaching both macro- and microeconomic effects of the suggested measures and their potential impacts on the financial recovery (Anonymous, 2010a).

CRD IV suggests the two regulatory standards for liquidity risks, LCR and NSFR. Further it is proposed that tier I (going concern capital) should be based on core tier I, which is common equity, and non-core tier I, hybrid capital. Tier II is defined as the gone concern capital. It is also, as already mentioned, proposed to eliminate tier III, i.e. subordinated debt instruments with an initial maturity of at least 2 years. CRD IV will also introduce charges for counterparty credit risk and introduction of counter cyclical measures (European Commission, 2010).

CRD IV will strengthen the requirements of higher quality of capital, increased requirement of the liquidity buffer, different contra cyclical buffers and a minimum level of capital (Anonymous, 2010b). The aim of regulatory capital is to absorb unexpected losses. There are two types of such capital; capital that absorb losses on an ongoing concern basis and capital that absorb losses on a gone concern basis. The first allows the financial institution to continue its activities, and the latter secures that the depositors and senior creditors are paid in case of default (European Commission, 2010).

Basel III rules are developed for large international banks and it is a challenge for EU to consider the European conditions and to extend it to small and nationally active banks (SBA;1, 2010). Also the eligibility criteria for core tier I capital must be evaluated (Europaparlamentet, 2010). During 2011 a technically binding constitution will be presented regarding the reporting requirements of these quantitative measures. A tighter liquidity framework is needed, but there is a risk that higher capital requirement and liquidity standards while the financial markets still are weak could slower the recovery in the economy (Anonymous, 2010a).

3.5.2 SWEDEN'S PREVIOUS REGULATIONS AND DEVELOPMENTS ON LIQUIDITY RISK REPORTING

SFSA announces regulatory codes known as FFFS. These constitutions are complementary rules in the form of regulations that are binding as well as general guidelines. The Swedish supervisory authority

works in compliance with the Swedish law, EU rules and regulations as well as international rules (FI;1, 2011).

FFFS 2007:3 concerns reporting of liquidity risk and was put in force on 1 February 2007. The regulatory code imposes quarterly reporting combined with the capital adequacy regulations. The information should be submitted to SFSA on the twentieth day of the second month following the balance sheet date if that day corresponds with the annual accounting date. The requirements for reporting cover the net cash flow that the banks generate in future periods. The submitted reports should also include the liquidity reserve and un-drawn credit accommodations remaining in each period after accounting for the net cash flow. The principles for producing the future cash flows should be based on internal estimation of figures generated from current business contracts. Cash flows denominated in foreign currency should be converted to SEK and be aggregated to a total net cash flow. When reporting cash flows the firm shall distinguish between contracted cash flows with fixed payment dates and demonstrated cash flows (FI 2007:3). FFFS 2007:5 is SFSA's former regulatory code regarding general guidelines for public disclosure of information concerning capital adequacy and risk management and was also put into force on 1 February 2007. This regulation presented directives concerning how the banks should disclose information covering capital adequacy and risk management. SFSA advises what information that should be disclosed, when it should be released, where it should be available and how frequently it shall be revealed (FI 2007:5).

SFSA announced an introduction of a new more demanding regulation for reporting of liquidity risk on the 30th of September 2010 with the aim of replacing FFFS 2007:3. The rules will improve SFSA's ability to monitor that the banks comply with the regulations on liquidity risk management (FFFS 2010:7), as mentioned above. FFFS 2010:7 was put into force on 31 December 2010 in order to support the management of liquidity risks in credit institutions and investment firms. The goal is to contribute to a stable and well-functioning financial system by requirements for the banks to maintain a higher standard in their liquidity management than has hitherto been required (FI 2010:7). The provision is based essentially on changes in the EU's Capital Adequacy Directive and the Basel Committee's recommendations. The regulation repeals the sections relating to liquidity risk (FFFS 2000:10) in SFSA's general guidelines for market and liquidity risks management for credit institutions and securities companies. The regulation place stringent requirements on companies that have a stated risk tolerance, strategies and guidelines on liquidity management. The principles regulate how internal control and independent review will be organized in this area. It establishes rules concerning the measurement of liquidity risk which inter alia require that the banks should perform stress tests. A particularly important section determines what assets that may be included in the liquidity reserve, and also governance issues such as limits and contingency planning (FI 2010:7).

FFFS 2010:12 is SFSA's latest regulation and general guidelines regarding public disclosure of information concerning capital adequacy and risk management. The establishment was put in to force on 31 December 2010 and replaced FFFS 2007:5 as a consequence of the latest Basel III framework (FI

2010:12). The revised regulatory code is an extension of pillar 3 from the former Basel II framework (FI;3, 2011 and Lindqvist, 2011). In addition to FFFS 2007:5 the latest version FFFS 2010:12 includes a new chapter. The bank publications should not only include the credit risk, counter party risk as well as the operational risks, but also a quarterly presentation of the banks liquidity risk status to the market (FI 2010:12).

The proposal FFFS 2011:X provides stringent requirements on the major credit institutions and securities companies to more frequently and more rapidly transmit data concerning the current liquidity situation to SFSA. Companies must provide the information every month, instead of quarterly as in 2007:3, and the data must be received within 15 calendar days. This supervisory process will give SFSA opportunities to assess liquidity risks and how they affect the stability of financial markets (FI 2011:X). This introduction made SFSA one of the first supervisory authorities, together with UK, to adopt the suggested guidelines under Basel III (e-mail correspondence with Tobias Lindqvist, 2011-04-11, find appendix and section B for more details). The early introduction is motivated by the fact that shortcomings of the current reporting and current turmoil in the international financial market. Also fiscal problems in several countries occurred, which made it important to introduce the new regulations for reporting (Lindqvist, 2010). The regulatory code is not fully determined and has recently been revised. It is expected to be statutory on the 1th of July 2011 and is currently defined as FFFS 2011:X. Both FFFS 2010:7 and FFFS 2011:X is an extension of pillar 2 from Basel II (FI;2, 2011 and Lindqvist, 2011).

The regulation is extended to cover the size of the liquidity reserve and its composition, projections of future cash flows, brokering cases, dependencies of the major lenders and credit-sensitive markets, and secured bonds. The banks must also provide information on liquid assets and cash outflows and inflows, so that SFSA can do a stress test that shows payment readiness for the next 30 days (FI 2011:X).

3.5.3 STATEMENT OF OPINION, FFFS 2011:X

The first reporting under the new suggested regulatory framework FFFS 2011:X is settled to be applied on 31 July 2011. The Swedish banks were encouraged to respond to the proposal by expressing their experience during the test period and to submit their thoughts to SFSA on 28 February 2011. As a member of the Swedish Bankers' Association SEB presented a written comment through the association (FI;4, 2011).

SEB and the other members in the Swedish Bankers' Association present a strong rejection against the proposed regulatory framework. The main argument is that SFSA should coordinate the test period with the rest of the Europe and proceed with the test reporting instead of an own implementation of the new liquidity framework, in particular Sweden should not differ from the rest of Europe. The banks express a demand for the regulations to be harmonized on a European level since banks often operate internationally and provide different reporting for different international units. Also the development of an own national regulation will be inefficient and time consuming. Further, the demands for reporting are too

frequent and the banks suggest quarterly reporting and to replace banking days with calendar days in order for the banks to synchronize figures from the balance sheet and control for the quality of the reported information (SBA;5, 2011).

In contrast to SFSA the banks considers that they will be negatively affected by the drawbacks followed by necessary conversion after EBA has presented their guidelines on 1 January 2012. The new liquidity regulation will be based upon the liquidity measures suggested by Basel III but also other relevant information that is necessary for establishing a sufficient supervision. If EBA develops common liquidity requirements it is of importance to consider those instead of using own reporting methods and regulations (SBA;5, 2011).

The association further claims that small banks will suffer since they are in the early stage development of the new liquidity requirements. As far as the Swedish Bankers' Association concerns only a few have received feedback from SFSA regarding how the test reporting really works. It should be mentioned that this feedback was a main argument to the test reporting implementation in 2010 (SBA;5, 2011).

SFSA requires the Swedish banks to report on their website but does not fully explain the procedure in doing this. This will cause an operational risk since reporting of daily cash flows with different currencies will be made manually. The Swedish Bankers' Association argues that the banks must have time to prepare for this new reporting routine and cannot wait for further information. The reporting system through SFSA's website creates an operational risk and stresses the importance of a European standard and an alliance with the system developed by EBA. The Swedish Bankers' Association argues that the process and lack of knowledge will only result in higher cost for the Swedish banks in terms of administration (SBA;5, 2011).

Finally the banks demand a safe transition period between 2007:3 and 2011:X which means that they do not want to provide information according to both of the regulatory codes at the same time. Currently the banks are in need for more information regarding how to perform the reports and about how the methods are defined. Furthermore, the banks express a wish for a clarification regarding the liquidity reserve, pledging of assets, definitions regarding cash flows, secured bonds and the stress testing for LCR. The banks require SFSA to publish guidelines that can provide answers in order to clarify concerning the procedures of reporting (SBA;5, 2011).

3.6 STRENGTH AND WEAKNESSES WITH THE NEW LIQUIDITY RISK REGULATION

3.6.1 "SWEDEN DOES NOT NEED HIGHER RESTRICTIONS THAN OTHER COUNTRIES"

Financial regulations are important when creating confidence in the financial markets. Still, there exists a strong consensus from the Nordic banks, government agencies and policy makers in the criticism of the proposals by the Basel Committee (SBA;2, 2010).

It is important that Sweden follows the new framework on an international level and do not deviate from the other countries. The European countries are currently under intensive preparation in order to implement the international agreement under the Basel III package. The focus should be on achieving a uniform and effective regulation in the EU. The fact that the Swedish supervisors diverges from other authorities when implementing the new requirements will destroy the harmony and send unfortunate signals (SBA;2, 2010). Global standards for the banks during the preparation work of the Basel III framework are important. It is not reasonable for the Swedish banks to get higher restrictions than the rest of the Europe since SEB also competes internationally and has staff, customers and products in different countries (Anonymous, 2010c).

3.6.2 THE QUANTITATIVE MEASURES

Song and Thakor (2007) find that banking profitability and fragility activities are a result of the asset and liability activities. Fragility is a consequence of where the banks invest and how they fund themselves. Parlour and Plantin (2008) shows that more liquid bank assets will have a positive effect on the asset and liability management. By using this banks are able to redeploy capital to more profitable business opportunities and are resilient to negative shocks. Atkinson and Blundell-Wignall (2010) state that the cause of the recent financial crisis was the insolvency and the following liquidity problem, but if banks are solvent and have an adequate capital level then the liquidity and funding management should be left up to them. Since maturity transformation is fundamental in the banking business then the banks should be able to handle their own business.

In practice, there are several potential problems with the Basel III accord. First LCR has a bias towards government bonds. While budget deficits are large and the interest rate risk attracts buyers, the process will have a negative impact on lending to the private sector especially the small and medium-sized enterprise. Furthermore, bonds may still be risky with a high default risk that is not captured by rating agencies (Atkinson and Blundell-Wignall, 2010). LCR must be tested before it is put into force and the identified weaknesses must be rectified (SBA;3). The one-size-fits-all approach might cause solvency issues for banks. Hörngren (2010) is critical to liquidity quotes and argues that by locking up the liquidity assets will force the banks to use illiquid assets in order to survive. This is inefficient. The buffered assets are not available for the banks itself or to other banks which causes a risk of infection in the whole banking system. In addition, the secured liquidity buffers will make strong markets to have a weaker ability to stand against a crisis during financial turbulence.

The use of the quantitative measures will disfavor SEB and their focus on corporate deposits. The ratios will turn out relatively more supportive to other banks (Anonymous, 2010c). NSFR is weak since it is based upon the ability of supervisors and companies to model investor behavior and to classify those as stable or unstable during an ongoing crisis. The liquidity ratios require more liquid assets, which ceteris paribus, may result in lower rate-of-returns. The consequence is excess risk taking in other areas of the business (Atkinson and Blundell-Wignall, 2010). A consequence of to the new regulation the banking

industry is in need for common equity, senior unsecured debt and covered bonds. Such a supply shock can be absorbed by domestic and global financial markets without price pressure. Still this issue has reduced substantially due to the reduction in the NSFR requirements in July 2010 and the smooth implementation of the ratio until 2018 will identify potential weaknesses and allows a calibration of the details (Jaffee and Walden, 2010).

The construction of the banks liquidity risk was a driving force of the recent financial turmoil. Banks were confident that their securities were liquid and marketable without a sufficient loss. Lehman Brothers is an example for illustrating that the extent of interbank loans in fact may create instability (Frisell, 2010). Liquidity regulations cannot and should not prevent a major crisis in the system, as a post Lehman panic, but it can reduce the likelihood of a crisis (Anonymous, 2010d). Frisell (2010) claims, that quantitative regulation should be a well-balanced minimum requirement. It is impossible to capture all aspects of liquidity with one or two dimensions and quantitative rules. The alternative solution to support the banks liquidity risk management is to impose tax on short-term borrowing. This will provide incentives but not in the beginning phase of a problem. Further the central bank should be given bank liquidity to all (solvent) institutions “on demand”. The solvency requirements must be strict in order to prevent taxpayers to avoid bearing the risk. Liquidity is easier to monitor and control in comparison with solidity.

3.6.3 OVERREGULATION

There exists a common fear of overregulation in the banking system. Banks suffers from lassitude from the period of regulation from the Basel II framework. An increased regulation will create inflexibility in the market and create a false sense of security and it is necessary to improve the balance between risk and reward as a consequence of the aggressive lending activities along with insufficient internal controlling. (Zachrisson, 2010). Higher discipline is necessary after the financial crisis, but it is important that the reforms do not adversely affect the financial system's ability to meet its social utility functions (Nyberg, 2006). It should be noted that financial crisis is a common argument and justification to implement regulations. The underlying motives are private interests to extract rent from others using a self-serving regulation rather than public interests protecting the underserved (Benmelech and Moskowitz, 2010).

3.6.4 THE REGULATORY FRAMEWORK NEEDS TO BE IMPROVED

Ingves (2011) suggests even tighter rules regarding liquidity risk management for Swedish banks than has been suggested by Basel III. The reason is the size of the Swedish banking sector, the dependency of other countries and credit growth. He mentions tighter regulations of mortgages and an earlier start of tighter liquidity. It will be profitable to introduce stricter rules and a faster development of the Basel III accord (Hassler, 2011). Further, Basel III does not address fundamental regulatory problem, e.g. promises that make up any financial system are not treated equally, and banks are able to transform risk buckets with financial instruments such as derivatives. Activities in shadow banking system are also a part of the problem that is related to similar promises treated by regulators. Treating promises in different way will

require substantial thinking about shadow banking since it is not incorporated in the Basel III regulation (Atkinson and Blundell-Wignall, 2010 and Jaffee and Walden, 2010).

Hörngren (2010) argues that the Basel III suggestion is based upon a tough stress scenario where the higher demand for buffering liquid assets will increase the cost for the banks. He further argues a state reinsurance process and states the question whether it is reasonable to have large private stocks that are rarely put into use when you can provide liquidity from a central bank when it is needed? Basel III is unclear concerning the central bank's role and should be clearer when it comes to the banks liquidity management.

3.7 CONSEQUENCES OF A NEW REGULATION

3.7.1 COMPETITIVE ENVIRONMENT

Basel III motivates higher transparency of common equity holding in order to address the problem with over leverage in the banking system. In the sense of market competition this creates entry barriers and a more concentrated market where the ones who already have the ability to meet the regulations will dominate even more. Weaker banks will be forced to decrease lending rather than raise capital to meet the new guidelines (Anonymous, 2010e). Basel III rules are developed for large international banks. It will be a challenge for EU to consider the European conditions and to extend it to the small, national banks. The new framework is unreasonable for small businesses and may therefore hamper competition (SBA;3). Different implementation and views about how to use the regulations would cause difficulty to compete on similar terms (Anonymous, 2010c).

The short term funding the latest twentieth years has increased and was initially a natural consequence due to the new regulations and the competitive environment. It is however during the latest 10-15 years hard to motivate such sort term financing and the social gain of those. Furthermore the competitive environment will even make it worse (Anonymous, 2010d).

Swedish banks have a large share of mortgages on their balance sheets and therefore a lower risk compared with their international competitors. The issue is that the new regulations will create incentives to decrease the allocation of mortgages and instead gather high risk funding such as private equity. A measure that captures OBS activities should therefore be introduced. This measure should however not be as binding as a pillar 1 measure, but a more softened pillar 2, which is not the case now (Anonymous, 2010d). This matter has been under several discussions. Further the new capital requirements will put more pressure on management. Since the banks still operate in a competitive environment and their shareholders demand a certain return on equity the desire for high return investments becomes even greater (Anonymous, 2010e).

3.7.2 TRANSPARENCY AND ECONOMIC WELFARE

Wellink (2010) is confident that the Basel III is a strong toolset with high capability to prevent financial turbulence, however since the appearance of a financial crisis is a random process it is impossible to fully eliminate the likelihood of such event. Hörngren (2010) argues that strengthened supervision of liquidity risk is a positive way of solving the liquidity risk problem. A sufficient amount of liquidity risk is essential to keep the banks main operating function. Without a certain amount of liquidity risk there will be a problem with “narrow banking” with no real asset transformation. However, binding liquidity ratios might be expensive without resolving the underlying problem.

The recent financial crisis showed that the Swedish financial sector is vulnerable to disruptions in financial markets and that liquidity risk is fundamental. The financial turmoil clearly shows that the large negative effects on the economy are followed by financial instability. Companies' access to cash and financing markets depends largely on the confidence of economic actors in general and the financial stability in the system. The banks' access to funding is not only a consequence of the situation of the individual company but also influenced by the situation and circumstances in the outside world. Policy makers in a company do not carry the full cost of any problems affecting the rest of the market - and therefore they cannot be assumed to take adequate measures against the risks. This motivates a strengthening of the regulation towards common standards. Information and supervision of liquidity risk would not eliminate the risk of another crisis like the one occurred in autumn 2008 to appear again. However, an increased discipline regarding the banks reporting may help to reduce the likelihood of another crisis to occur by limiting the risks, increasing transparency and enhancing confidence (Lindqvist, 2010).

Financial crisis are less likely to occur if financial reporting regimes is more comprehensive with more informative and timely reporting (Tadesse, 2006). Improved public disclosure strengthens the markets' ability to encourage safe and sound banking practices. Market discipline can only work if the information is reliable and timely, and truly reflects the activities and risks. In order to achieve maximum benefit of public disclosure it is of interest for supervisors and other public policy makers to create policies that involve relevance, reliability, timeliness and comparability of the information disclosed (BIS, 1998).

Bliss and Flannery (2002) present empirical evidence supporting the importance of transparency by identifying two components: Investors' ability to truthfully measure the financial health of a bank based on disclosure and investors' ability to essentially influence and make changes. The absence of the markets ability to influence appears as a consequence of agency problems between the bank management and market participants incensed by poor regulation and supervision. Nier and Baumann (2006) argue that transparency motivates banks to hold larger capital buffers, which demonstrates a lower risk-taking and lower probability of default. Furthermore, they argue that government protectionisms and the absence of competition in the interbank markets reduce the effectiveness of these market mechanisms.

Jordan, Peek and Rosengren (2000) highlight the possibility of the fact that the effectiveness of market discipline depends on the regulatory environment. They suggest that the regulations might need to complement supervisory actions and prudential regulation that also retain responsibilities in influencing bank behavior. Tadesse (2006) reports a robust positive relation between mandated disclosure requirements and national banking system stability. Banking transparency should be defined broadly to include disclosure requirements, the degree of information gathering activity by investors and the extent of information dissemination in the country. The study shows strong evidence that increased transparency is related to a lower likelihood of banking system fragility.

Public disclosure does also come with drawbacks. First, private and public interests do not always concur. Especially in terms of undesirable behavior from the market if a bank is in a weakened position and the lack of confidence may spread other banks. However if the disclosure is adequate and ongoing the likelihood this contagion effect is unlikely. The second drawback is the costs. It is hard to evaluate if the benefits of additional disclosure are higher than the costs. Policy makers do often take for granted the net benefits of additional disclosure, however there might occur substantial costs. It should however be kept in mind that in well-managed banks information that is relevant should already be available and used by the management to operate (BIS, 1998). Further Barth, Caprio and Levine (2004) explore the relation between bank regulation in general and banking system stability. They find that although private monitoring increases individual bank performance it has a small relationship with banking fragility.

3.7.3 COSTS

If the banks do not fulfill the requirements of Basel III they will suffer due to higher costs. The higher costs will arise if the banks need more core capital which is more expensive compared to other sources of funding. A higher liquidity buffer will also give higher costs since it generates less return than other assets. Furthermore a longer time to maturity will cause higher interest rates. Still, this might be reduced since Basel III will decrease the overall cost of financing. Banks can therefore lower their dividends or raise the costs for its customer by higher interest rate gaps or higher fees for their banking products or by reduce lending (FS, 2010a).

The Swedish central bank has analyzed to which extent the major Swedish banks are capable to meet the requirements of the new banking regulation. The analysis shows that the Swedish banks not fully meet the new liquidity regulation. This implies that the banks will need to extend the maturity of their funding (FS, 2010a). Furthermore, in the performed estimation the Swedish central bank assumes that the lending rates could increase by up to 10 basis points as banks increase their holdings of liquid assets to meet the future liquidity regulation. They also assume that the banks will transfer all cost increases due to Basel III to the borrowers. The Swedish central bank also suggests that if the banks would rather increase the payouts to the shareholders the increase in lending rates may be less (FS, 2010a).

The new regulatory code will increase the fixed costs for the banks. The direct costs are mainly the development and operation of IT systems and personnel costs. Changes in IT systems will be necessary as the new demands requires a comprehensive process in order to quickly be able to act out the basis for reporting and centralization of data from all parts of the company. Furthermore, the banks may need to allocate additional staff to quickly set-retrieve and manage data each month. A central unit in the company will then compile the data from the company's various units and analyze its relevance and meaning for ensuring good data quality before reporting to SFSA. Small businesses are often affected more strongly by the regulatory reporting requirements since a major part of the firm's resources must be used for administration (Lindqvist, 2010).

There is a risk that some of the additional costs that the proposed regulation does ultimately passed on to customers. Financial market's consumers will have to pay higher prices and consume less banking services, on average. However, as the costs of implementing the reporting requirements are considered to be relatively small, the impact on consumers to be small. The benefits of SFSA's improved access to information on liquidity risk are therefore estimated to be greater than the costs that regulation entails (Lindqvist, 2010).

Basel III is in many aspects an improvement of the rules and it is in the interest of the industry that there is a sound regulatory framework. Still, the new rules cause higher costs for the banks and their customers. Those costs will depend on how the policies are implemented in the EU. The broad regulatory framework, in combination with any other changes, may have significant unintended consequences for the financial markets (SBA;3).

The increased regulations will have a negative impact on the real economy. The costs for banks will increase and create a situation where nobody wants to borrow since it will be too expensive in terms of increased rates. Further, no one will provide capital to the banks because it may appear that the banks are not profitable enough. The increased cost of credit will hit hard on the growth of the economy (Östlund, 2010). This might cause an additional crisis and reduce the recovery from the latest financial crisis (SBA;2, 2010). Jaffee and Walden (2010) argue that Basel III will decrease systemic risk and the costs to society and that the steps to obtain this will be marginal for the Swedish economy.

It is obtained that a reduction in the loan supply will cause less debt for non-financial firms. The financial crisis in 2007 and 2008 caused a sharp decline in new debt issued. It is also found that non-financial firms are more likely to borrow if banks are less regulated concerning branching. Competition between banks will increase the loan supply from banks. To conclude, credit competition will give lower interest rates. If no barriers to bank expansion, the competitive pressure will lead to an increase in larger credit supply. However there is a little variation in access to credit in case of less branching restrictions, still the credit rationing increases. It stands clear that branching does not fully explain credit demand (Rice and Strahan, 2010).

An increase in risk-based capital requirements and regulations reduce aggregate bank lending. Banks with higher costs of capital lend less and will be more affected by capital requirements (Thakor, 1996). Anonymous (2010f) states that bonds will replace a high degree of the financing of mortgages, which nowadays are short-term certificates. This will cause higher costs due to the new long-term financing. This higher cost may be transferred to the customers in terms of higher interest rates on their loans. The variable and the longer and tied interest rate will converge. This might result in a higher degree of financing by deposit accounts since it will be cheaper, which in turn will cause an increase in bank deposit rates. Furthermore, the higher costs followed by Basel III may cause a competitive disadvantage since Swedish banks will have to use more long term financing compared with banks in other countries. Anonymous (2010d) argues that if this is the case it is worth it since the liquidity situation is in urgent need for improvement. Jaffe and Walden (2010) state that there is a positive side effect of the transportation of the higher costs to the customers since those may seek out alternative markets in order to obtain financial services. This should be encouraged by Swedish regulators and the government.

4 CASE STUDY

SEB was founded in 1856 and is one of the four major banks in Sweden with operations in twenty different countries. Retail banking is offered in Sweden and in the Baltic countries. In Denmark, Finland, Norway and Germany the focus is mainly on corporate- and investment banking. The latest financial crisis was characterized by a weak economy worldwide and SEB was negative affected of its Baltic investments. The new issue of stocks in 2009 secured the banks ability to increase its support to its customers despite the financial turbulence. In the Baltic countries continued SEB's quest to find sustainable solutions for the customers and the bank (SEB, n.d.). It is clear that SEB has been a subject to illiquidity and that SEB as a global actor will be affected if the regulations are not harmonized on an international level. This information supports our objective to view both the industry and the regulators perspective when presenting the context and factors that will influence SEB when meeting the new regulation.

This section is based on an in-depth investigation of a selected group of representatives from the industry side as well as from the regulatory side. The chapter presents a summary of four interviews performed during spring 2011 and forms a platform for the following analysis, results and conclusions. It is clear that the given conclusions in section 6 would have been further strengthened if additional interviews were conducted. The choice of one respondent from each sector is particularly a result of time constraints. Also, since the headquarters and consequently the expertise are located in Stockholm in a period when both were living in Gothenburg, we were simply not able to regularly visit the capital city to conduct personal interviews. We are aware of the bias that might occur since the information conducted from the interviews does not necessarily reflect the opinion from the sectors, but rather personal judgments.

We do believe that one interview per sector will serve as a sufficient benchmark for understanding how SEB will be affected of the new liquidity requirements. This assumption is resulting from the fact that a general view is presented, combined with view from the target bank SEB. The questions given to the respondents are presented in appendix, section A.

4.1 JONAS SVÄRLING, HEAD RISK AND CAPITAL MANAGEMENT, SEB GROUP TREASURY

Personal meeting on 2011-02-04, this section presents a summary.

There is a common perception in the industry is that the regulatory codes presented by SFSA for liquidity risk reporting are unmotivated and that SFSA response to Basel III is far too ambitious. It is unjustified that Sweden is one of the very first countries to implement increased reporting standards. Svärling describes SFSA's behavior as accelerated and do not agree with their motives to introduce new rules

before EBA has settled the directives for EU. The new regulations are harsh and will have a negative effect. In the end, SFSA should consider that BIS suggestions are only recommendations.

Different requirements for monitoring the risk management create an unfair competitive environment for the Swedish banks on an international level. The rules need to be harmonized globally with a jointly goal and frequency of reporting. Svärling highlights the problems followed by global standards and believes that banks are not comparable at an international level due to the fact that banks provinces and activities are not directly translatable for such an assessment. The fact that the standard tools for reporting are suggested in European terms is a disadvantage for the Nordic banks in particular. Currently none of the Swedish banks holds a NSFR above 100%. This is explained with an example; the Swedish market for deposits is mainly based on funding activities and securities, which are not visible in the banks' balance sheet. Banks are being punished even though they have been well managed throughout the crisis. Svärling highlights that SEB has recovered well with a sound short term financing and safe liquidity reserve.

Svärling is confident with SEB's liquidity risk management and believe that SEB has a strong capital and liquid position as well as a strong balance sheet. According to the new demands from Basel III SEB faces a challenge and needs to improve some factors. As an example the bank needs to extend the duration of the funding profile, change the liquidity buffer (which will affect the return), and change several of instruments in the business model.

A higher transparency based on the latest directives from BIS will not deliver a more developed support for the banks but will provide necessary information for the market, rating firms and the supervisors. The monthly reporting is unmotivated since the banks will not be ready with the closing of the books and the balance sheet will not be fully affirmed with that frequency. In addition the reporting structure is costly to change and in terms of time, working capacity, education, IT et cetera. SFSA seems to have forgotten the fact that SEB is a global actor with 16 affiliates that makes the information gathering complicated and hard to collect in such a short time.

Regarding the role of the short term liquidity requirement, as well as the long term liquidity requirement, these suggestions will be a challenge for the Swedish banks. LCR will lead to a need for holding a large liquid buffer and NSFR will increase the funding cost and make deposit more attractive. Svärling highlights that SEB is critical towards the quantitative measures and prefers the previously situation when the banks were allowed to use their own methods for communicating the liquidity risk. The main difference with publishing the liquidity status in qualitative ratios is that these do not respect the fact that the four major banks in Sweden is not universal but have their different business model. Svärling argues that since SEB is focused on corporate clients actually disfavors them from the assumptions behind the ratios. Swedbank is mentioned as a contrary that might be favored by the ratios since private and households deposits are categorized as relatively more valuable liquid assets. SEB is working on proving

the fact that historically this niche has not been more risky than other segment of investors, and this will be a strong point in the bank submission for comment to SFSA. Covered bonds must be given a higher price. Svärning is not rejecting the idea of common tools for communicating the liquidity risk but is critical towards the current definition and the assumptions behind the ratios. Generally there is not much to say about NSFR since the ratio will not be implemented until 2018, but the liquidity asset eligibility is too narrow under LCR. Svärning is positive towards the fact that the major banks have together with the Swedish Bankers' Association been working on a common solution with a jointly ratio which will support a safe national competitive environment. There is a risk for a higher concentration and harder competition among the banks and that it will be costly for niche banks and the free standing saving banks in order to implement the Basel suggestions. Smaller bank will suffer since they have a more mobile customer base that is more sensitive towards price changes.

There is a potential risk of a second-round effect, from reduced lending and reduced maturity transformation capacity that may lead to an increased risk for another crisis to appear. There is a risk of overregulation and is critical when the regulations are too strict and inflexible. Bail outs and liquidity support from the central banks always should be the last way out for the banks and the increased transparency regulation affects the need for liquidity support. In addition, the complexity of liquidity risk makes the public reporting complicated. Signals about poor liquidity status and lack of knowledge about the interpretation may accelerate by a malicious tongue effect and create more problems than necessary in the banking system.

4.2 LARS SÖDERLIND, SENIOR RISK ANALYST, THE SWEDISH FINANCIAL SUPERVISORY AUTHORITY

Personal meeting on 2011-02-04, this section presents a summary.

Söderlind highlights the motivation for the new constitution for stricter liquidity reporting by the recent financial crisis. The liquidity information reported from the banks has been hard to monitor and has always been reported with a lag. The aim is to secure the quality of the reporting material since the banks have had a variation of different modeling strategies before without any requirement for standards. The introduced reporting requirement will lead to a higher communication between the banks and SFSA and especially during the test period of FFFS 2011:X which will due to end on 1 July 2011.

Söderlind reveals an internal tension when he goes along with Svärning's (interview with Jonas Svärning, 2011-02-04) opinion about that the reporting requirement needs to be harmonized on a European level. The decision from SFSA regarding the increased reporting guidelines is unmotivated. The latest regulatory codes will most likely be replaced. However, Swedish banks will have a competitive advantage in contrast to other international banks since they have had the chance to prepare for a higher degree of reporting, in terms of knowledge and data systems et cetera.

Söderlind meets Svärling's (interview Svärling) critics of a monthly reporting with the fact that SFSA encourages higher frequency rather than precise information and argues that higher transparency is always motivated and that it has no negative effect; the banking system needs a higher level of discipline. More information is positive not only for the supervisors monitoring ability but also for all the banks stakeholders; shareholders, investors, analysts, rating agencies et cetera. The quantitative ratios LCR and NSFR presented under Basel III should be revised since they do not respect important differences in the banking system. Söderlind believes that they are inflexible not only because he rejects one-size-fits-all-models but is also questioning the mathematical structure. LCR and NSFR will change several times during the observation phase and before they will be used in public reporting. The starting time for using the liquidity ratios in the banks public disclosure is today unknown and Söderlind claims that this will be a matter of market anticipation. It is likely that one bank will be first in the field and then after a while the market will force the rest of the banks to also present their figures until SFSA finally makes legal requirements. There is a risk of NSFR not being put into use and suspects that in 2018 there will be new members of the Basel Committee with new ideas about how to define the ratio. The quantitative liquidity requirements that are discussed internationally, NSFR and LCR, has not yet been settled and are currently not put into force by SFSA. The ratios are not included in FFFS 2010:7 and FFFS 2010:12. However FFFS 2011:X requires banks to use LCR.

There is a risk of overregulation in the banking system since there is always an uncertainty involved with regulations. It is always hard to foresee the consequences and there are always waves of regulation demands as an effect of booms and busts in the economy. In addition, liquidity risk is complicated and can cause more problems if it is not communicated properly. The analysts have a large responsibility to interpret the reporting materials.

Söderlind is certain of the fact that the bank clients will need to bear the cost when the banks are forced to hold a higher liquidity discipline according to the latest constitutions. However, the increased transparency will reduce the banks need for liquidity support from the central bank. The transfer of the cost to the banks and their customer is preferable in comparison with a bank disorder where the taxpayers need to bear the full cost. Söderlind agrees with Svärling (interview Svärling) about the fact that the stressed reporting will be more costly for small banks in terms of investing in expertise and system for implementation. This will contribute to relatively more consolidation in the banking system, and the cost for the banks will be transferred to the clients.

4.3 OLOF SANDSTEDT, HEAD OF BANKING ANALYSIS DIVISION, THE SWEDISH CENTRAL BANK

Personal meeting on 2011-02-18, this section presents a summary.

Sandstedt responds positively towards SFSA's early implementation of Basel III and updates of their regulatory codes, by highlighting some factors that motivates Sweden's needs for relatively stronger regulations of disclosure. First of all, Sweden is a small open economy that depends on the international

environment. Sweden has a banking system with a lot of assets relative to GDP, and is dependent on market funding, especially foreign currencies. Sandstedt supports the suggested techniques for monitoring and the strong reporting requirements since liquidity risk is important and can be managed by supervisory.

The access to liquidity is perishable and requires frequent reporting to authorities in order to ensure an opportunity of a safe monitoring. The new disclosure directives will contribute and help the banking system to be safe and reduce the likelihood of another financial crisis. Therefore there is not a risk of overregulation in the banking system as a consequence of the newly introduced reporting requirements. A contributing factor to the crisis and the collapse of Lehman Brothers and the application for Chapter 11 was the lack of transparency. The rules must have a healthy balance between ensuring the risk level while allowing the banks to provide risk services, such as converting short-term savings to long-term lending. The purpose of Basel III is to reduce risk in the banking sector and considers that the Basel III is a good tool to achieve it.

Lack of transparency is harmful because it causes unnecessary uncertainty, for example, in terms of investors' inability to properly evaluate the banks' balance sheets and risk taking. Sandstedt stresses that increased transparency, not least around liquidity, is necessary. The suggested quantitative ratios LCR and NSFR are efficient for liquidity risk reporting. Sandstedt motivate this by highlighting that one of the triggers of the recent crisis was the poor quality of international banks' liquidity reserves, and an excessive dependence on short-term financing and the objective of LCR and NSFR is to correct this. Concerning the Swedish central bank's role as a lender of last resort it is clear that an increased discipline and disclosure will reduce the need of liquidity support from the government. The idea of the Basel III framework is to reallocate costs between banks and government. Furthermore, today the state carries a lot of bank risk through implicit government guarantees. With Basel III banks will be forced to bear a larger share of the cost through to self-insure, i.e. by keeping more and more capital while keeping more liquid assets and have a better match between assets and liabilities. Sandstedt claims that even if the reporting burden and investment in IT systems may increase for small banks the benefits of reporting will exceed the cost of compliance.

The higher cost of meeting the higher demands for transparency will cause an unfair competitive environment where the small banks will suffer. Basel III will place great demands on the legal system support which Sandstedt assumes perhaps will be easier to manage for large banks than for small. Small banks will also have less ability to build and manage liquidity risk in the portfolios. This could contribute to some competitive disadvantage for small banks. But on the whole, there is no major risk in terms of increased competition.

4.4 ANDERS KRAGSTERMAN, LIQUIDITY RISK ANALYST, THE SWEDISH BANKERS' ASSOCIATION

Personal meeting on 2011-02-18, this section presents a summary.

Kragsterman is critical towards that Sweden is one of the first countries to strengthen the reporting directives. The Swedish banks will suffer in terms of stronger regulation in comparison with their international competitors. This will be the main argument in the letter of comment that will be submitted to SFSA on February 25 2011. Kragsterman argues that it is unmotivated to introduce FFFS 2011:X since it will only last until the end of the year after being put in to force on 1 July since the introduction of CDR IV by EBA in the end of the year will make FFFS 2011:X invalid. The upcoming European standard will use different tools and definitions which will force the constitution to be reformulated. The European framework will also include additional monitoring directives and strengthen the reporting directives to an even greater extent than BIS guidelines under Basel III, which will further unjustified the current regulations presented by SFSA. The motivation of a noisy banking system and the inability to handle the liquidity reporting properly does not hold to justify the overstrained implementation of the reporting directives.

Kragsterman argues that monthly reporting is frequent and has also suggested in the letter of comment to SFSA that the figures should not be submitted by calendar days but banking days. Still, he is positive to that a greater transparency will help the banks to internally tide up the risk management and externally calm the system. Thus the quantitative measures, LCR and NSFR are not good tools for reporting the liquidity risk management. The liquidity status should be communicated in qualitative terms instead of using the ratios that are incomparable. Liquidity management reporting should be based in own terms and present the figures leaving SFSA their own mandate to analyze and interpreted the risk management. The negative views against LCR and NSFR are based upon the fact they generate an unfair competitive environment since the measures will appear to be relatively more favorable to certain banks with a certain business model. This will create problem in the public discourse. There is a risk of overregulation and more information is not always preferable. Regarding the competitive environment among the Swedish banks the small banks will not suffer since they (balance sheet total below 5 billion) can apply for facilitation. The greater reporting activities demanded by SFSA will cause costs in terms of administrative changes and structural transformations which are likely to be transferred to the banks customers.

5 ANALYSIS AND RESULTS

The Basel III accord aims to encourage the discipline in the banking system by developing a set of disclosure requirements regarding banks' liquidity risk management. This is an extension of the public disclosure directive under Basel II and pillar 3, which was limited to cover only the credit, market and operational risk reporting. In the light of the latest financial crisis, the objective of the latest Basel accord is to improve bank transparency by introducing stricter liquidity reporting requirements (FS, 2010b). With the Swedish banking industry in focus, SFSA has strengthened the former guidelines concerning public disclosure and developed FFFS 2010:12 (2007:5). New methods for managing the liquidity risk has also been suggested which are defined under FFFS 2010:7 (2000:10). The new regulatory codes will accomplish the ability to make use of the reporting activities to a much greater extent in terms of controlling for liquidity risk management. The new regulation will create opportunities for SFSA to benchmark in comparison with the previous situation where the banks were allowed to use their own models for reporting liquidity risk. In order to monitor the banks use of these guidelines SFSA is currently updating the regulations concerning banks liquidity risk reporting by replacing 2007:3 with the new regulatory code FFFS 2011:X.

Considering our interviews, the representatives from the regulatory side (interview with Anders Kragsterman, 2011-02-18 and interview Svärling) claim that the previous liquidity reporting has been insufficiently organized and that the information submitted from the banks have been of low quality. Furthermore, they argue that there has been a lack of transparency as a result of insufficient standards for reporting the liquidity risk. Those issues have created a need for common directives (e.g. interview Svärling and FS, 2010b) and an extension of pillar 2 and pillar 3 from Basel II (FI;2-3, 2011 and Lindqvist, 2011). Barfield and Venkat highlight some positive effects from the improvement of the public disclosure and liquidity risk management for the banks and argue that the distribution of external information enables banks to reflect that they truly understand their business and the potential risks from their operations. The new reporting requirements will have a positive effect on the Swedish banks if they are well managed. If banks successfully accomplish and run their business prudently they will take a huge step towards rebuilding confidence and restoring the health in the financial system.

There is a need for even stricter regulations for Swedish banks than has been suggested by Basel III (Hassler, 2011 and Ingves, 2011). The arguments are the size of the Swedish banking sector, the dependency of other countries and the credit growth (Ingves, 2011). The case study reveals a contrary view from the industry by reflecting exhaustion and a fear for overregulation (e.g. interview with interview Kragsterman and interview Svärling). The case study also presents the regulators response, where Sandstedt (interview with Olof Sandstedt, 2011-02-18) rejects the risk of overregulation and argues that a

precipitating factor in the crisis around the time of Lehman Brothers was the lack of transparency and that a greater amount of such is necessary. Moreover, the purpose of Basel III is to reduce the total amount of risk in the banking sector and considers that Basel III is a good tool to achieve it (interview Sandstedt). On the other hand, it is not clear if there will be a positive future outcome since it is impossible to estimate the consequences and argues that there is always a risk of overregulation (interview with Söderlind, 2011-02-04). Liquidity risk in particular is unpredictable which makes it complicated to analyze and problems might arise if it is communicated in the wrong way. Also the complexity of liquidity risk makes it particularly hard to determine the effects since the liquidity situation changes daily due to the risk management (FS, 2010a).

The respondents (interview Kragsterman and interview Svärling) express that in general more information is not necessary better. Historically there has been both positive and negative outcomes and private and public interests do not always concur (BIS, 1998). The cost of the higher regulation might cause an additional crisis and reduce the recovery from the latest financial turmoil (SBA;2, 2010) and there is a risk for a second-round effect (interview Svärling). Conversely, Tadesse (2006) finds that more informative and timely reporting will result in that financial crisis are less likely to occur. Furthermore, Nier and Baumann (2006) argue that transparency motivates banks to hold larger capital buffers, which demonstrates a lower risk-taking and lower probability of default. Prudent risk taking is being evaluated against negative information spillovers through the banking system.

All of the respondents (interview Kragsterman, interview Sandstedt, interview Svärling and interview Söderlind) show a positive view towards the general idea of a higher discipline in the banking system with global standards. However, all of the respondents, except from Sandstedt (interview Sandstedt), reflect a jointly rejection towards the suggested tools for reporting the liquidity risk since they are regarded as inadequate (interview Kragsterman, interview Svärling and interview Söderlind). This is in line with previous research showing one-size-fits-all models in general are a subject of discussion (e.g. Atkinson and Blundell-Wignall, 2010, Lindblom et al, 2008). There is a risk of using the quantitative ratios LCR and NSFR in the public disclosure since wrong signals may occur if they are not formulated in a justified matter. The stakeholders have to be well aware of the determinants behind the figures in order to create soundness in the banking system (interview Svärling). The analysts are responsible to interpret and communicate the material properly (interview Söderlind). Also LCR and NSFR are inflexible and will create an unfair national competitive environment since they favor banks with a certain business model (Frisell, 2010, interview Kragsterman and interview Svärling). SEB will be negatively affected since the focus is on corporate deposits that are not valued as high as private and household savings (interview Svärling).

Atkinson and Blundell-Wignall (2010) state that LCR is biased towards government bonds that may result in solvency issues for banks. Parlour and Plantin (2008) argue that more liquid assets will result in that banks are able to redeploy capital to more profitable business opportunities. Banks will to a larger extent

be more resilient to negative shocks. Moreover NSFR is based upon the assumption that supervisors and companies have the ability to classify investor behavior during an ongoing crisis (Atkinson and Blundell-Wignall, 2010). Still, the smooth implementation of the ratio until 2018 will identify potential weaknesses and allow a calibration of the details (Jaffee and Walden, 2010). The ratios are based upon weak assumptions that disfavor banks in the Nordic countries. Swedish banks are financed with a large amount of funding which they are not able to show in the balance sheet (interview Svärning). Conversely, Hörngren (2010) argues that strengthened supervision of liquidity risk is a positive way of solving the liquidity risk problem. However binding liquidity ratios might be expensive without resolving the underlying problem. It should be kept in mind that shadow banking is one part of the problem and is not solved by the new regulation (e.g. Atkinson and Blundell-Wignall, 2010 and Jaffee and Walden, 2010).

It is necessary to clarify the uncertainties regarding the new routines of reporting. The rules should be harmonized on a European level since different reporting requirements for different international units will be inefficient if a bank operate internationally (interview Kragsterman and interview Svärning). The Swedish banks will be negative affected by the drawbacks followed by necessary conversion after the EBA has presented their guidelines. This will result in higher costs in terms of administration, operational risk and investments in knowledge and expertise (SBA;5, 2011). The Basel Committee is being to “loose” and unspecific when suggesting the reporting directives to the authorities (interview Svärning). However Sweden is a small open economy that is dependent on the international environment (interview Sandstedt). Conversely, since Sweden is an open economy it is indeed exposed to higher global systemic risk, therefore the tradeoff should be reconsidered before implementation of the new regulation (Jaffee and Walden, 2010). Swedish banks will have a competitive advantage since they will have time for preparation and have priority in terms of functions and systems (interview Söderlind).

Jaffee and Walden (2010) argue that Basel III will support a decrease in systemic risk and the costs to the society and that the steps to obtain this will be marginal for the Swedish economy. However, banks will suffer from higher cost in order to meet the Basel III accord. The rate at which and how much the price will increase depends largely on how the policies are implemented in the EU (SBA;3). Banks can lower their dividends or raise the costs for its customer by higher interest rate gaps or higher fees for their banking products or by reduce lending. However a common view, presented by both the industry and the regulators, is that the cost will be transferred to the customers (FS, 2010a, interview Kragsterman, SBA;3, interview Svärning and interview Söderlind) still they are likely to gain from higher interest rates on deposit accounts (Anonymous, 2010f). Hörngren (2010) argues that the Basel III suggestion is based upon a though stress scenario where the higher demand for buffering liquid assets will increase the cost for the banks. Sandstedt (interview Sandstedt) believes that the costs due to the new regulation are justifiable and claims that the idea of the Basel III framework is to reallocate costs between banks and government. Still it is likely, as a result from the new requirements, to reduce the banks need for liquidity support from the central bank. It is preferable to transfer the cost to the banks and their customer in comparison with a

bank disorder where the taxpayers need to bear the full cost. Another positive side effect of the increased cost for the customers is the increased demand of alternative markets to obtain financial services. An expansion of those markets is therefore necessary and should be encouraged by the government and the Swedish central bank (Jaffee and Walden, 2010).

Östlund (2010) states that the cost for SEB will increase and create a situation where nobody wants to borrow since it will be too expensive in terms of increased rates. This is a result of the required long term financing due to Basel III (SBA;2, 2010). Anonymous (2010f) also expects the mortgage lending to decrease in the coming quarters due to the impact of rising interest rates and lending criteria tightening. Further, no one will provide capital to the banks because it may appear that the banks are not profitable enough (Östlund, 2010). A decrease in loan supply will have a negative impact on new debt issued (e.g. Atkinson and Blundell-Wignall, 2010 and Rice and Strahan, 2010). If Basel III results in less lending, then small and medium sized enterprise growth potential will decrease. This will have a negative impact on SEB since one part of their customer base is corporations (interview Sväriling). In the broader perspective, the fact that large companies do not have to rely that much on bank credits will hamper the competition and lead to consolidation in the real economy.

Anonymous (2010f) states that the higher costs followed by Basel III may cause a competitive disadvantage since Swedish banks will have to use a longer term financing compared with international competitors. The higher costs are motivated since the liquidity situation is in urgent need for improvement (Anonymous, 2010d). Swedish banks have a large share of mortgages on their balance sheets that may create incentive for “excess return investments” (Anonymous, 2010e). Higher costs will arise, and also incentives, if the bank needs more core capital that is more expensive compared to other sources of funding. A higher liquidity buffer will also give higher costs since it generates less return than other assets. The chief economists of the Swedish Bankers' Association share the jointly view that the Basel III framework punish the well managed Nordic banks. Also unfortunate signals will occur since Swedish supervisors deviate from the line of harmonization (SBA;2, 2010). It is important with global standards that are harmonized on an international level in order to protect the competitive environment (Anonymous, 2010c).

There is a potential for harder national competition among the banks as a consequence of higher transparency and the new reporting requirements. This will not affect SEB but it will be more costly for smaller banks to implement the new regulatory framework in terms of administration, expertise and the fact that they are exposed to a customer base that is more sensitive towards price changes (interview Sväriling). Söderlind (interview Söderlind) agrees with Sväriling (interview Sväriling) about the increased costs for smaller banks that will contribute to more consolidation in the banking industry. The higher costs due to the new regulation will cause an unfair competitive environment where small banks will suffer. Small banks have less ability to manage a liquidity risk which could contribute to some disadvantage but that generally speaking there is no risk for higher concentration (interview Sandstedt). On a national level

it is important with a dialogue and an agreement between the large banks in terms of liquidity risk reporting to increase a fair base on a national level. This is necessary in terms of time and cost savings as well as providing a sound competitive environment (interview Kragsterman and interview Svärting).

6 CONCLUSIONS

6.1 MAJOR FINDINGS

How will SEB be affected by the Basel Committee suggestion of an increased regulation of reporting regarding the banks liquidity risk management? The new reporting requirements will create an opportunity for SEB to strengthen the confidence in the financial market since they are forced to reveal their liquidity position. A higher level of transparency enables SEB to submit high quality information revealing that it is aware of their business with current liquidity exposure. SEB will be negative affected by the current definitions of the quantitative ratios and their business model. The procedures of submitting information to SFSA will increase the operational risks since the information shall be submitted manually on their website and that there is lack of instructions concerning this issue. On the international level SEB will suffer since rules are not harmonized and probably will be revised. This will create additional costs. On the national level it is uncertain whether SEB will cause any harm or not, it is however likely that there will be an increased demand for alternative markets, and this is of course a disadvantage for SEB.

The recent financial crisis has created an urgent need for policy reforms to improve robustness towards future unexpected shocks. The crisis has put liquidity risk and the role of increased transparency under the spotlight with the regulatory goal of creating stability in the banking system. This thesis supports the regulators proactive actions towards a higher discipline in the banking system but rejects the capability of the suggested toolset for managing and monitoring the liquidity risk. There is a need for greater liquidity risk management among the banks on a global level. There are shortcomings in the regulatory framework, but also possibilities for improvements, which provide a result showing both negatively and positively effects for SEB. Still the new regulation does not fully eliminate systemic risk, consistent with Jaffee and Walden (2010). Especially a higher level of discipline cannot support the exposure towards liquidity risks or SFSA's monitoring capacity, since this complex hazard quickly can put a bank together with the whole banking system into failure and that the downsides of such regulation is a matter of discussion (Anonymous, 2010e).

A clarification of the motives behind the new directives is necessary since there is a lack of information and guidelines from SFSA about the implementation. This creates reasons to fear a risk for overregulation as a consequence of the fact that the Basel Committee was to "loose" and unspecific when they suggested the reporting directives to the national supervisory authorities. This triggered a precipitated implementation and it is doubtful whether Sweden in particular needs harder requirements or not. The whole banking system must share a jointly goal of working towards an improvement. Apparently, the recent financial crisis proves this as SEB was hit even though they were managing the liquidity risk

relatively well in comparison with international actors (interview Svärning). Still, the requirements of more liquid assets will be efficient since there will be room for reallocation to more profitable areas if necessary.

It stands clear that SEB will encounter a challenge when meeting the new reporting regulation. The implementation of FFFS 2011:X will be costly for SEB in terms of fixed costs and operational risk. In order to meet the requirements of Basel III SEB needs to extend the duration of the funding profile, change the liquidity buffer (which will affect the return), and change several of instruments in the business model. In addition, SEB will suffer from alternative costs as the bank will be forced to deviate from the main business focus. The question is whether SEB will transfer the costs to the customers, lower the rate-of-return for their shareholders or to which extent they will bear the costs themselves. As revealed during the interview (interview Svärning) and as stated by Lindqvist (2010) and SBA;³ this paper gives us reason to believe that SEB's clients will bear the majority of the implementation costs.

The new regulation will result in a higher degree of consolidation among the banks and an increased level of concentration in the banking system since it will create barriers to entry in terms of fixed costs. This will not affect SEB negatively in terms of national competition since it is reasonable to believe that small banks have less ability to manage liquidity risks in contrast to SEB. It will be more costly for smaller banks to implement the new regulatory framework in terms of fixed costs and the fact that they are exposed to a customer base that is more sensitive towards price changes (interview Svärning). In addition, smaller banks are more exposed by a decreased lending supply. To conclude, the new regulation does not promote competition on a national level but SEB will remain relatively unaffected in this sense. This should however not be confused with that the following higher costs will create a demand for alternative markets, this will indeed affect SEB.

In terms of international competition SEB will suffer since the rules are not harmonized. As a global actor, SEB will be affected since they are required to meet different standards depending on which country they operate in. SEB would benefit from a scenario where the test period is coordinated with the rest of the Europe. It is not reasonable to implement the requirements as one of the first countries, especially since the rules most likely will change. Furthermore, since mortgage lending is expected to decrease SEB will suffer from a competitive disadvantage as they it will have to use more long term financing compared with banks in other countries. SEB will be disfavored by the European standard since the Swedish market for deposits is mainly based on funding activities and securities, which are not visible in the banks' balance sheet.

In general, this thesis questions the value of one-size-fits-all-models and the quantitative ratios. Those must be reformulated before put into force since they are inflexible. The quantitative ratios disfavor corporate deposits and SEB will have a tougher challenge relative to national competitors in meeting these requirements due to their business model. The measures contribute to a situation where a bank may choose to use high risk assets in their portfolios (Atkinson and Blundell-Wignall, 2010 and

Anonymous, 2010e). The excess-risk taking that will occur affects SEB negatively since the bank will be exposed to other banks risk management in the sector, it should be kept in mind that bank failures are contagious and that reputation for the financial sector is of great importance. This motivates a rejection of the new regulation ability to reduce the risk in the banking system. The present regulation fails to develop an integrated view of the value of liquidity risk management among the banks and transparency is beneficial for signaling confidence, but the problem with “information overspill” remains. A common standard will not facilitate for investors to make a fair judgment since the current ratios are weakly defined.

It is not clear if SEB will use the new regulation as an advantage to analyze their liquidity situation and compare it with the competitors. In fact liquidity is complex and liquidity management changes daily. Also different banks have different business models. Still the higher discipline will support SEB’s ability to control for the quality of the short term assets and ensure that the buffer covers unexpected outflows. In this sense, transparency is motivated and will help SEB to secure a safe risk management. A higher level of transparency among the banks will create an opportunity for SEB to benchmark their management in comparison with the competitors.

6.2 SUGGESTIONS FOR FURTHER RESEARCH

This thesis has proposed scenarios of possible outcomes for SEB when facing the new reporting directives from SFSA based on the latest Basel III accord. The next step would be to investigate the ex post scenario after the FFFS 2011:X has been implemented as well as the affect from meeting the requirements of FFFS 2010:12 and FFFS 2010:7. Another subject would be the study of how this constitution differs from the EU-directive that expects to be stated in the beginning of next year. Lastly, another research field could be to analyze the long run effects that the higher discipline will bring in terms of costs, competition and sense of flexibility in the banking system. The open minded structure of our thesis has opened several potential angles for further investigation and we are sure that some of them will be explored in the future.

REFERENCES

- Anonymous (2010a): "Public consultation on the Capital Requirements Directive ('CRD IV')", *Gateway to the European Union*, published on 2010-02-26 [online source] <http://europa.eu/rapid/pressReleasesAction.do?reference=MEMO/10/51&format=HTML&aged=0&language=EN&guiLanguage=en>
- Anonymous (2010b): "Förslag till nya kapitaltäckningsregler", *Price Waterhouse Coopers*, published on 2010-07-09 [online source] <http://www.pwc.com/se/sv/bank-kapital/publikationer/forslag-till-nya-kapitaltackningsregler.jhtml>
- Anonymous (2010c): "Jag vill ha ett globalt regelverk", *E24*, published on 2010-02-10 [online source] http://www.e24.se/business/bank-och-finans/falkengren-jag-vill-ha-ett-globalt-regelverk_1853923.e24
- Anonymous (2010d): "Level playing field en utopi", *Bankföreningens nyhetsbrev*, no. 1, p. 10-11
- Anonymous (2010e): "Basel III; Third time's the charm", *the Economist*, published on 2010-09-30 [online source] http://www.economist.com/blogs/freeexchange/2010/09/basel_iii
- Anonymous (2010f): "Banking Sweden – The market underestimates capital", *Öhman* [online source] <http://www.hgu.gu.se/Files/CFF/The%20market%20underestimates%20capital%20needs%20CFF%208%20Dec%2010.pdf>
- Atkinson, P. and Blundell-Wignall, A. (2010): "Thinking beyond Basel III: Necessary solutions for capital and liquidity". *OECD Journal: Financial market trends*, vol. 2010, issue 1
- Bake, M., Hawken, K., Hitzelberger, C., Hugi, R. and Kravitt, J. (2010): "Basel II modified in response to market crisis". *the Journal of Structured Finance*, vol. 15, no. 4
- Barfield, R. and Venkat, S.: "Liquidity risk management". *the Journal of Global Perspectives on Challenges and Opportunities* [online] <http://www.pwc.com/gx/en/banking-capital-markets/pdf/liquidity.pdf>
- Benmelech, E. and Moskowitz, T. (2010): "The political economy of financial regulation: Evidence from U.S. State usury laws in the 19th century". *the Journal of Finance*, vol 65, no. 3
- Billing, A. (2009): "Dags för Basel III", *Affärsvärlden*, published on 2009-01-23 [online source] <http://www.affarsvarlden.se/hem/nyheter/article497425.ece>
- Bryman, A. (2001): "*Samhällsvetenskapliga metoder*". Malmö: Liber
- BIS (1998): "Enhancing bank transparency: Public disclosure and supervisory information that promote safety and soundness in banking systems", *Bank for international settlements*, September 1998 [online source] www.bis.org/publ/bcbs41.htm
- BIS (2004): "International convergence of capital measurement and capital standards", *Bank for international settlements*, June 2004 [online source] <http://www.bis.org/publ/bcbs107.pdf>
- BIS (2005): "International convergence of capital measurement and capital standards: A revised framework", *Bank for international settlements*, November 2005 [online source] <http://www.bis.org/publ/bcbs118.pdf>
- BIS (2010a): "Basel III: International framework for liquidity risk measurement, standards and monitoring", *Bank for international settlements*, December 2010 [online source] <http://www.bis.org/publ/bcbs188.pdf>

BIS (2010b): "A global regulatory framework for more resilient banks and banking systems", *Bank for international settlements*, December 2010 [online source]
http://www.bundesbank.de/download/bankenaufsicht/pdf/basel3_capital_rules.pdf

Cornett, M. and Saunders, A. (2009): "*Financial Markets and Institutions*". New York: McGraw-Hill.

De Larosière, J. (2009): "The high-level group on financial supervision in the EU", published on 2009-02-25 [online source] http://ec.europa.eu/internal_market/finances/docs/de_larosiere_report_en.pdf

Esaissaon, P., Gilljam, M., Oscarsson, H. and Wägnerud, L. (2004): "*Metodpraktikan. Konsten att studera samhälle, individ och marknad*". Stockholm: Norstedts Juridik AB

E24 (2010b): "Uppenbar risk för överregleringar", *E24*, published on 2010-02-05 [online source]
http://www.e24.se/business/bank-och-finans/uppenbar-risk-for-overreglering_1843547.e24-regelverk_1853923.e24

European Commission (2010): "Possible further changes to the capital requirements directive" [online source] http://ec.europa.eu/internal_market/consultations/docs/2010/crd4/consultation_paper_en.pdf

Europaparlamentet (2010): "New Basel bank capital standards need fine-tuning, say MEPs", published on 2010-07-10 [online source]
<http://www.europarl.europa.eu/en/pressroom/content/20101006IPR85262/html/New-Basel-bank-capital-standards-need-fine-tuning-say-MEPs>

FI 2007:3: "Regulation FFFS 2007:3", *Finansinspektionen*, published 2007-01-29

FI 2007:5: "Regulation FFFS 2007:5", *Finansinspektionen*, published 2007-01-29

FI 2010:X: "Regulation FFFS 2011:X", *Finansinspektionen*, published 2011-02-24

FI 2010:12: "Regulation FFFS 2010:12", *Finansinspektionen*, published 2010-12-13

FI 2010:7: "Regulation FFFS 2010:7", *Finansinspektionen*, published 2010-12-31

FI;1 (2011): "Regulations", *Finansinspektion* [online source] <http://www.fi.se/Folder-EN/Startpage/Regulations/>

FI;2 (2011) Riskbedömning och tillsynd (Pelare 2)", *Finansinspektionen* [online source]
<http://www.fi.se/Regler/Kapitaltackning/Riskbedomning-och-tillsyn-pelare-2/>

FI;3 (2011): "Informationskrav (Pelare 3)", *Finansinspektionen* [online source]
<http://www.fi.se/Regler/Kapitaltackning/Informationskravbrpelare-3/>

FI;4 (2011): "Förslag till nya föreskrifter om rapportering av likviditetsrisk", *Finansinspektion*, published on 2011-01-18 [online source] <http://www.fi.se/Regler/FIs-forfattningar/Forslag-nya-FFFS/Listan/Forslag-till-nya-foreskrifter-om-rapportering-av-likviditetsrisk/>

FS (2010): "Effects of liquidity requirement for banks on Swedish mortgage rates", *the Financial Stability report*, vol. 1/2010

Forsberg, B. (2009): "Baltiska spöken i Swedbank och SEB", *Affärsvärlden*, published on 2009-05-27 [online source] http://www.affarsvarlden.se/hem/hausse_baisse/article2591691.ece

Frisell, L. (2010): "Varför kvantitativ likviditetsreglering?", (report) published on 2010-04-28

FS (2010a): "Basel III effekter på de svenska bankerna och Sverige", *Finansiell Stabilitet*, vol. 2/2010

FS (2010b): "Metod för stresstester av bankers likviditetsrisk", *Finansiell Stabilitet*, vol. 2/2010

- Hassler, J. (2011): "Borg har rätt", *Affärsvärlden*, published on 2011-03-08 [online source] <http://www.affarsvarlden.se/tidningen/article3120810.ece>
- Huertas, T. (2011): "Test under stress for the EBA", published on 2004-16-11 [online source] http://fw.ifslearning.ac.uk/Libraries/April_2011/17_FW_Focus_on_five_key_tasks.sflb.ashx
- Hörngren, L. (2010): "Likviditetskrav och likviditetsstöd några kritiska tankar", (report) published on 2010-04-28
- Ingves, S. (2011): "Basel III – Välbehövliga regler för en säkrare banksektor", (report) [online source] http://www.riksbank.se/upload/Dokument_riksbank/Kat_publicerat/Tal/2011/110201.pdf
- Jaffee, D. and Walden, J. (2010): "The impact of Basel III and Solvency 2 on Swedish banks and insurers – An equilibrium analysis". *Financial Markets committee*, report 3
- Jordan, J., Peek, J. and Rosengren, E. (2000): "The market reaction to the disclosure of supervisory actions: Implications for bank transparency". *Journal of Financial Intermediation*, vol. 9 no. 3
- Kaufman, G. (1994): "Bank contagion: A review of the theory and evidence". *Journal of Financial Services Research*, vol. 8 no. 2
- Lindblom, T., Olsson, M. and Willeson, M. (2008): "Operational Risk under the Basel II Capital Adequacy Framework". (report) Gothenburg.
- Lundahl, U. and Skärvad, P.-H., (1999): "*Utredningsmetodik för samhällsvetare och ekonomer*". Lund.
- Lindqvist, T. (2010): "Förslag till nya föreskrifter om rapportering av likviditetsrisk", *Finansinspektionen*, published on 2010-01-18 [online source] http://www.fi.se/upload/30_Regler/10_FFFS/11_remiss/20110118_likviditetsrisk/remiss-pm_rapport_%20likviditet_10-4148.pdf
- Nier, E. and Baumann, U. (2006): "Market discipline, disclosure and moral hazard in banking". *Journal of Financial Intermediation*, vol. 15
- Nyberg, L. (2006): "Finansiella reformer och finansiell kris – svenska erfarenheter", [online source] <http://www.riksbank.se/templates/Page.aspx?id=21039>
- Patel, R. and Tebelius, U. (1987): "*Grundbok i forskningsmetodik*". Lund: Studentlitteratur
- Parlour, C. and Plantin, G. (2008): Loan sales and relationship banking". *the Journal of Finance*, vol. 63, no. 3
- PR (2010): "Basel III skärpta regler för banker", *Penningpolitisk rapport*, vol. October 2010
- Rice, T. and Strahan, P. (2010): "Does credit competition affect". *the Journal of Finance*, vol. 65 no. 3
- SEB (n.d.): "Strategi", [online source] <http://www.sebgroup.com/pow/wcp/sebgroup.asp?website=TAB1&lang=se>
- SBA;1 (2010): "Swedish Bankers' Association: "Basel III färdigt – stora konsekvenser för bankerna", *the Swedish Bankers' Association*, published on 2010-12-16 [online source] [http://www.swedishbankers.se/web/bf.nsf/\(\\$All\)/2024B9516FB9C2F6C12577FB0044A224?OpenDocument](http://www.swedishbankers.se/web/bf.nsf/($All)/2024B9516FB9C2F6C12577FB0044A224?OpenDocument)
- SBA;2 (2010): "Det är inte försent att rädda nordiska banker från Basel III", *the Swedish Bankers' Association*, published on 2010-07-21 [online source] [http://www.swedishbankers.se/web/bf.nsf/\\$all/FFFF8F6172BF1434C125774900285F13?OpenDocument](http://www.swedishbankers.se/web/bf.nsf/$all/FFFF8F6172BF1434C125774900285F13?OpenDocument)

SBA;3: "Bankföreningen vill se harmonisering", *the Swedish Bankers' Association* [online source] [http://www.swedishbankers.se/web/bf.nsf/\(\\$All\)/54249949F5CEE2C125782A0050AEDA?OpenDocument](http://www.swedishbankers.se/web/bf.nsf/($All)/54249949F5CEE2C125782A0050AEDA?OpenDocument)

SBA;4: "About the Swedish Bankers Association", *the Swedish Bankers' Association* [online source] <http://www.swedishbankers.se/web/bf.nsf/pages/ombank.html>

SBA;5 (2011): "Statement of opinion", *the Swedish Bankers' Association*, [online source] [http://www.swedishbankers.se/web/bfmm.nsf/lupgraphics/1110225y.pdf/\\$file/1110225y.pdf](http://www.swedishbankers.se/web/bfmm.nsf/lupgraphics/1110225y.pdf/$file/1110225y.pdf)

Schertler, A. (2009): "Prudential Liquidity Requirements and Bank Behavior", *Christian-Albrechts-Universität, Kiel*

Standard and Poor's Global Credit Portal Rating Direct (2010): "Basel III For Global Banks: Third Time's The Charm?", (report) published on 2010-03-04 [online source] http://www2.standardandpoors.com/spf/pdf/fixedincome/Basel_III.pdf

Tadesse, S. (2006): "The economic value of regulated disclosure: Evidence from the banking sector". *Journal of Accounting and Public Policy*, vol. 25 no.1

Thakor, A. (1996): "Capital requirements, monetary policy, and aggregate bank lending: Theory and empirical evidence". *the Journal of Finance*, vol. 51, no. 1

Thakor, A. and Song, F. (2007): "Relationship banking, fragility, and the asset-liability matching problem". *the Review of Financial Studies*, vol. 20, no. 5

Thoraval, P.-Y. (2006): "The Basel II framework: The role and implementation of Pillar 2". *Financial Stability Review*, no. 9, Banque de France

Turner, A. (2009): "The Turner Review: A regulatory response to the global banking crisis", *Financial Services Authority*, vol. March 2009

Wellink, N. (2010): "Basel III - ett kraftfullt paket", published on 2010-11-29 [online source] [http://www.swedishbankers.se/web/bf.nsf/\\$all/CFB5E2806FC05475C12577E5005864A0](http://www.swedishbankers.se/web/bf.nsf/$all/CFB5E2806FC05475C12577E5005864A0)

Zachrisson, O. (2010): "Överregleringar bankernas största skräck", *E24*, published on 2010-02-10 [online source] http://www.e24.se/business/bank-och-finans/overreglering-bankernas-storsta-skrack_1854155.e24

Östlund, A. (2010): "Bankvärdens blickar riktas mot Basel", *E24*, published on 2010-07-14 [online source] http://www.e24.se/business/bank-och-finans/basel-iii-reglerna-kan-ge-hogre-rantor_2179117.e24

Case study

Lindqvist, Tobias, Senior Risk Analyst, FI, e-mail correspondence, 2011-04-11

Meeting with Lars Söderlind, Senior Risk Analyst at FI, 2011-02-04

Meeting with Jonas Svärning, Head Risk and Capital Management SEB Group Treasury, 2011-02-04

Meeting with Olof Sandstedt, Head of Banking Analysis Division, Financial Stability Department of the Swedish central bank, 2011-02-18

Meeting with Anders Kragsterman, Liquidity Risk Analyst, the Swedish Bankers' Association, 2011-02-18

APPENDIX

SECTION A

Case study questions

Main question 1: What will be the effects for the Swedish banks when implementing the new regulation for reporting?

General questions:

- What will be the costs of the new regulations?
- What will be the greatest challenges?
- What weaknesses do you identify with the new regulation?
- What will be the greatest differences due to the implementation of increased liquidity reporting?
- Comments on FI's ambition with updating the liquidity risk regulation, even before the EU commission has published its directives based on Basel III?

Main question 2: How will the liquidity risk management change?

General questions:

- Which role should the quantitative measures LCR and NSFR play?
- What weaknesses/advantages will follow LCR and NSFR?
- How do you experience these higher requirements?
- Which costs will occur due to the change in liquidity risk management?

Main question 3: How will the new stronger regulations affect the risk for overregulation in the banking system?

General questions:

- Is there a risk of overregulation? Why?
- Why do you believe new requirements have been introduced?

Main question 4: What will the effect be on the economic welfare?

General questions:

- Will the need for liquidity support decrease or increase?
- How will the competitive environment change nationally and internationally?
- What will be the social benefits?

SECTION B

This section reveals the e-mail correspondence with Tobias Lindqvist regarding which countries that were the first to adopt stricter liquidity regulations.

Från: Tobias Lindqvist [<mailto:tobias.lindqvist@fi.se>]
Skickat: må 2011-04-11 13:07
Till: Månsson, Maria
Ämne: SV: Bankernas likviditetsrapportering under Basel III

Förslaget introducerades i slutet av 2009 har jag för mig. Mer formuellt så skrevs projektplanen under våren 2010. Vet inte exakt vilka länder som var före men vi var tidigt ut med LCR, kanske först. Problemet är att LCR är ett mått som förändrats över tiden och om andra länder tagit in en tidigare version eller något liknande vet jag inte. Vet dock att UK redan har en inrapportering efter finanskrisen som är på plats.

Mvh
/Tobias

-----Ursprungligt meddelande-----

Från: maria.mansson@seb.se [<mailto:maria.mansson@seb.se>]
Skickat: den 11 april 2011 11:45
Till: Tobias Lindqvist
Ämne: SV: Bankernas likviditetsrapportering under Basel III

Hej Tobias!

Tack för snabbt svar! Beträffande om FI är först eller inte vill jag bara ha ett förtydligande vet du vilket land som var först med högre krav på bankernas likviditets rapportering? Var det möjligen så att Sverige var först och sedan kom UK, Norge etc. ? Vi har nämligen haft det som en motivering till ämnesområdet i vår uppsats så jag måste bara klargöra detta (!) När exakt introducerade FI detta förslag var det i samband med 2010:7 dvs i december 2010?

Tack återigen för svar!

Vänligast,

Maria