# New trends in the Nordic - Baltic region


## Sirpa Pietikäinen

MEP, Committee on Economic and Monetary Affairs, European Parliament


### Opportunities and challenges in the financial services agenda - Nordic perspective

Entering a new five-year term is a right moment to look at where the previous reforms landed. Most regulatory priorities for the Nordic region are best solved at EU level. Key trends such as digitalisation and sustainable transformation represent areas where the Nordic-Baltic region can lead the way.

European capital markets continue to have a national bias. While there are more funds in the EU, the size of the market remains smaller than in the US. One of the first actions should be to launch a CMU 2.0 to continue measures to deepen European capital markets.

A typical element of European, and Nordic, financial markets continues to be a reliance on bank funding. Despite efforts taken in the past legislature, Europe lacks integrated cross-border venture capital funds and business angles to ensure innovative European start-ups and non-listed companies access much-needed risk financing to grow endogenously.

> *"The Nordic-Baltic region has the potential to lead in digital and sustainable transformation."*
>
> \- SIRPA PIETIKÄINEN

In global competition, efforts are needed to remove remaining obstacles to cross-border investment funds. Diversification of financing and access to different investment products will grow of importance as European citizens look for ways to invest and save for old age. This will be particularly urgent in Nordic-Baltic societies preparing for a demographic change in the near future.

A high priority should be taking forward the reforms to deepen the Economic and Monetary Union and to complete the Banking Union. The marching order should be risk reduction before risk sharing. The doom loop between bank risk and sovereign risk that still exists in some Member States, such as Italy, needs to be solved first. FinTech, artificial intelligence and distributed ledger technology are bringing households and businesses with new choice of payment and investment tools. While emergence of innovation, such as crowdfunding, virtual currencies and new

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>>> payment systems needs to be supported, the ultimate regulatory approach should be one of technology-neutrality. A similar activity, service or a product warrants to be regulated to the same extent regardless of the platform or technology through which it is being offered. Same applies to customer protection.

Digital innovation, such as open banking and real-time payments, is making accessing and using financial services easier and speedier. At the same time, it also leaves us vulnerable to new, hybrid risks. While digitalisation facilitates collection and processing of data and creates opportunities for more standardized Know Your Customer (KYC), Anti-Money-Laundering (AML) and Terrorist Financing (TF) measures, it raises questions regarding cyber security, systemic risk and customer protection. The Nordic region has been in the forefront of a dialogue on cyber resilience in terms of cooperation between financial institutions and supervisors.

Sustainable finance is entering into the mainstream of the financial system. By changing the incentives of market actors, it is bringing about a transformative reform into the real economy and underlying business models. At the core of the change can only be full transparency of risks, environmental impact, and opportunities that allows markets themselves bring forward the transition to a low-carbon, circular economy. In the next five-year mandate, sustainability indicators will be a systematic part of future revision of financial regulation across sectors.

Measures targeted to financial intermediaries, such as disclosure and due diligence rules, consultation of end-investor preferences, or transparency of benchmark methodologies, will not suffice alone. They need to be combined with modernisation of corporate reporting rules to ensure standardised and meaningful data based on audited, integrated annual management reports. In the coming years, key regulatory questions will surround on the issue of access and openness of sustainability data, supervision of standards, and liability of reporting.

Common approach to innovation and risks, sharing of best practise and effective cross-border supervision are the basis for a level playing field and integrated markets to bring the European financial market to its full potential. ●


# Liga Kļaviņa

**Deputy State Secretary on Financial Policy, Ministry of Finance of the Republic of Latvia**


## Nordic-Baltic financial sector linkages and challenges

The combined Nordic-Baltic financial sector is the fifth largest in Europe. Historically the Nordic financial groups played an important role in the process of Baltic region financial sector integration. Large Nordic financial groups in the Baltic region created financial institutions that became of systemic importance in different countries and sectors. Today the key word of the Nordic Baltic region is integration – since the region is characterized by tight trade and financial ties within itself. The Nordic banking groups have extended the concept of the home market well beyond their country`s borders. Nordic parent banks continued to provide liquidity to their Baltic affiliates during the deepest crises in the Baltic economies.

*"Today the key word of the Nordic Baltic region is integration."*

- LIGA KĻAVIŅA

Today the Baltic financial sector shares the common priorities and challenges within the region:

- **Digital transformation.** The Nordic-Baltic financial sector is fully committed to continue its digital transformation. The sectors strong traditions for collaboration, combined with consumer confidence and integration with the public sector`s data and registries, have been key for the digital transformation of the Nordic Baltic countries. >>>

- **Sustainable finance.** The Nordic - Baltic governments and societies have high commitment to the objective of more sustainable economy. The financial sector of the region is actively engaged in the process of transition to a green and sustainable economy in Europe, to ensure that the sector is an integral contributor and participant in this transition, actively discussing challenges and using opportunities created by the transition. For several years we have seen growth in investment products that recognize and promote environmental and social aspects.
- **Fight against money laundering and terrorism financing.** A high level of confidence in the financial system is vital to the financial sector. Regrettably, the recent serious incidents in several European banks underline the magnitude of the problem of serious financial crime for the public and private sectors. The Nordic - Baltic region has shown leadership at the European and international level to promote reforms aimed at preventing the use of financial institutions for money laundering and terrorism financing and implementing needed reforms in their financial sector.
- **Building an effective Capital Markets Union.** The Nordic-Baltic countries support the continued development of the EU capital markets as a key element in strengthening the Single Market, diversifying financing means and investment opportunities. It also helps to make the EU more resilient to shocks reducing the dependency of bank intermediation. The Baltic States have committed to create a pan-Baltic capital market with harmonization of capital market regulations and dismantling of investment barriers. The initiative will overcome constrains the Baltic States often face due to their limited individual size. ●


# Erik Ekman

Head of Commercial & Business Banking, Acting Head of Group Business Risk Management, Nordea Bank Abp


## Opportunities and challenges in the Nordic financial services sector

The Nordic region has a longstanding high level of integration. The level of intra-Nordic trade is significant and large banks have activities across the Nordic-Baltic region. Within the countries there is a long history of cooperation across banks to make use of economies of scale and positive network externalities.

Now cooperation is moving to the Nordic level. Six Nordic banks are working on P27, the worlds' first cross-border payment infrastructure for multiple currencies. P27 will simplify for corporates and households in the Nordic region to make payments across the region and increase competition in trade and the banking sector. Moreover, Nordic banks have created a joint venture, KYC (Know Your Customer) utility to facilitate compliance with anti-money laundering and counter-terrorist financing regulation.

*"Regulatory harmonisation would support integration and help addressing challenges for our societies."*

\- ERIK EKMAN

Digitalisation is present in all activities in the Nordic societies. The quick reduction in demand for cash services is driven by demands by customers for easy, accessible financial services available anywhere, anytime. Digital financial services encompass most financial services from payments and loan applications to financial advice. Visits to bank branches are replaced with online meetings and the use of AI for customers interactions and financial advice. Many Nordic customers prefer to use the mobile bank app and demand for real-time payments has led to a quick adoption of mobile payments.

Further harmonisation of regulation would enable more integration, but also help addressing challenges for our societies. The risks associated with financial crime were in the past underestimated by the financial sector. Significant amounts of efforts and resources have been spent to enhance banks' capabilities to detect financial crime. Reports of suspicious transactions to the Financial Intelligence Units have increased significantly, but the level of convictions and assets claimed has not increased to the same extent. From a societal perspective there is a need to further strengthen collaboration between authorities and banks in order to ensure a more efficient use of both private and public resources. Financial crime often takes place across national borders, therefore cooperation between authorities in different jurisdictions should be strengthened.

Nordic banks have supported the efforts to strengthen the resilience of the banking sector by requiring better quality and higher levels of capital. Capital requirements should continue to be risk-sensitive in order to set correct incentives for the financial industry and to ensure that well-managed corporates are not punished. This is particularly important for Nordic banks which have a relatively large share of low-risk assets on their balance sheets. Moreover, a more similar interpretation and implementation by regulators would lead to competition on more equal terms between banks.

Another challenge is the increasing presence of non-banks in the Nordic financial services sector. The following questions need to be answered:

- Is this development driven by efficiency gains or by cost advantage of lighter regulation?
- Will this lead to a more diverse and competitive financial system, or to new forms of concentration, market power and systemic importance? ●

# Lauri Rosendahl

President, Nasdaq Nordics
and Nasdaq Stockholm

## Cross-ecosystem dialogue is key to growth in the Nordics and Baltics

As a hub of the Nordic and Baltic financial market ecosystem, Nasdaq is committed to maintaining a central role in the ever-ongoing dialogue for development of the financial market ecosystems in the region. We continue to do this by building on local market strengths and shared best practices towards gradual integration and expansion.

The unique characteristics of the financial markets in Northern Europe are founded on a mix of cross-border integration and local ecosystems that have been allowed to develop according to local conditions and requirements. Such a diverse landscape of relatively small, successful and unique economies do need some common ground to thrive, something which Nasdaq is able to provide and develop.

Nasdaq enables market participants to access seven national equity and fixed income markets, all using the same technology, combined with our derivatives clearing house that serves the whole region. Another example of integration is the launch of the pan-Baltic market, including the combination of the three Baltic CSDs into one.

Over the last five years, Nasdaq Nordics has seen an average of about 100 new listings yearly, of which ca 80% are small caps. With its deep liquidity pool and great mix of different types of investors, the Swedish market has become the leading example of how to support companies in earlier stages of growth. Notably, a high level of participation from retail investors contributes to the success. Multiple factors explain this, including a relatively mature equity investment culture, a pension system allowing individuals to choose capital allocation and also a high degree of digitalization, which has enabled retail investors direct market access via online brokers.

Across the region, Nasdaq has adapted First North, the growth market MTFs for SMEs, to the needs of not only smaller companies, but also smaller investors. For instance, for issuances too small to require a prospectus, issuers instead deliver a standardized 'company description', a cost-efficient document which is easy for investors to digest and compare. Nasdaq also produces free-of-charge 'company fact sheets', with data points for every single listed company on the Nordic and Baltic markets, providing a basis for visibility, comparability and further research.

*"Founded on a mix of cross-border integration and local ecosystems."*

\- LAURI ROSENDAHL

What is important to underline however, is that one size does not fit all. Local ecosystems need to be adapted to the needs of especially early stage growth companies. Hence, in addition to its European headquarters in Stockholm, Sweden, Nasdaq also has significant presence in all the countries where it operates markets, as well as in key financial hubs such as London.

I truly believe that the success of our well-integrated, safe, transparent and liquid markets for both small and large investors, domestic and foreign, and for issuers, could serve as an inspiration for others. In the coming years, Nasdaq will launch a number of initiatives that go beyond our traditional home markets in the Nordics and Baltics. Our ambition is to expand our regional footprint and become a truly European financial services provider, leveraging the success of the financially integrated, yet very different, regional markets, in which Nasdaq's European presence is founded. ●

# Piia-Noora Kauppi

Managing Director,
Finance Finland (FFI)

## New trends in the Nordic-Baltic financial services sector

The Nordic-Baltic financial markets, serving almost 33 million citizens, are at the forefront of rapid modernisation. Northern Europe has the same on-going main trends as the rest of the finance industry but is also leading the way in some developments.

Regional integration: across borders is developing rapidly, and cross-border projects are underway in for example payments infrastructure and the sharing of know-your-customer (KYC) data. Project P27 is to establish the world's first integrated region for domestic and cross-border payments in multiple currencies through an open-access, common infrastructure. This should enable state-of-the-art payment experiences to customers across the Nordics. With KYC, the banks' top priority has been to develop a Nordic platform with standardized processes for handling KYC data. The objective is to >>>

>>> simplify the KYC processes for corporate customers while strengthening financial crime prevention.

Building common digital infrastructure has a natural way of enhancing cooperation. The strong traditions of digital economy and mutual collaboration, combined with consumer confidence and the sector's integration with public sector data and registries, have been key for the digital transformation of our region.

Collaboration between the traditional financial sector and new fintech is important for us to succeed in the global financial market competition. Caution should also be kept in mind: the many new digital services also increase the risk of cyber-attacks against the financial sector and businesses in general. The Nordic-Baltic financial sector invests heavily in cybersecurity and engages in mutual information exchange within the limits of the current legal framework.

The Nordic-Baltic financial sector seeks to contribute to the EU's driving force for sustainable finance. We feel that the financial sector plays a key part in the decisive European effort to transition to low carbon economy, and we aim to be actively involved in the process.

Investment products that recognise and promote environmental and social aspects have been growing for several years already. Professional asset managers who offer these products play an important part in supporting sustainable economic growth, but the direction of development is ultimately driven by the investors. A similar beneficial trend in the development of sustainable products should ultimately spread to the entire financial sector.

*"The Nordic-Baltic financial sector plays a key part in the transition to low-carbon economy."*

\- PIIA-NOORA KAUPPI

The Nordic-Baltic financial sector has looked into ways of financing the welfare of our ageing population and managing the rising age-related expenses. Common to our region is broad public support for publicly financed welfare with elements of market solutions. We want care services, and especially long term-care, to be more open for market solutions, and private insurance to be a more pronounced complement to the publicly financed welfare.

All in all, the strategic agenda for the Nordic-Baltic finance industry is driven by the quest to constantly improve the customer experience and the ability of the sector to bring benefits to the society. ●

# Dan Sørensen

**Member of the Executive Board, Nykredit Bank**

## Basel III finalisation will be a major challenge for the Danish financial system

From an outsider's perspective, the last 18 months must have seemed like rather turbulent times in the Danish financial sector due to the AML issues discovered in a large Danish bank. But if we look beyond this very specific issue, it emerges that Danish credit institutions recently have come under much stronger national AML legislation while the Danish FSA has been further empowered in this area in terms of both funding and enforcement tools. Denmark has come far on AML in a very short time and is maybe now even ahead of the curve in terms of stronger regulation and possible future sanctions. Going forward it will be interesting to see the effects of these recent developments as they mature and are fully implemented.

Looking forward, the main issue for the Danish financial sector will therefore rather be Basel III Finalisation. European banks have a much larger share of low-risk lending on their balance sheets compared to e.g. US banks, something that will be severely punished by the new 72.5% output floor which will greatly increase REA levels and thus capital requirements in spite of no clear risk reduction effects. Danish mortgage lending is especially low risk and therefore even more susceptible to this. Danish credit institutions will need another EUR 10bn in capital – corresponding to a 34% increase in capital requirements. In spite of this, EBA has made clear that they recommend a full implementation of the Basel III Final standard with no accommodations to the European context and applying the output floor to the full stack of European capital requirements. This seems ill advised. There is no clear reason why the European financial sector – and thereby the real economy – should be treated so harshly in spite of the lower risk on balance sheets. A better solution could be implementing the output floor as a parallel backstop requirement based on the Basel capital requirements only rather than the full stack of European requirements. Such an approach would even be closer to the letter in the Basel standard and would retain the incentives for real risk management in European low risk lending.

*"European banks will be severely punished by the new 72,5% output floor."*

\- DAN SØRENSEN

Another big challenge is sustainable finance. It is clear that the financial sector must participate in the sustainable transformation of the economy. Albeit, in order to achieve meaningful transitioning it is necessary to develop common terms of reference for sustainability risk management within the existing risk management framework. The taxonomy proposed by the Commission TEG is a major step forward. However, economics of scale is key for liquidity in the large Danish covered bonds market. A 'shades of green' approach rather than a binary focus on either 'brown' or 'green' activities seems more suitable for fueling the transition. This way, splitting the cover pool into smaller parts could be avoided. As a result, pools of loans to different activities could have different shades of green depending on the contribution to a more sustainable development. ●