

1. FINANCIAL MARKETS

1.1. THE INTERNATIONAL FINANCIAL ENVIRONMENT

International financial markets¹

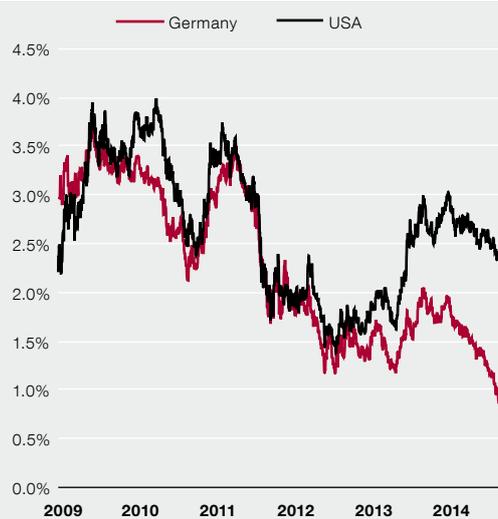
International financial markets have been influenced this year by the consistently accommodative **monetary policy** of the major central banks, which has been deployed in response to weak global economic growth and very low inflation. As inflation expectations are exceedingly low, the European Central Bank announced additional measures to stimulate the monetary policy environment at the start of September. This move has held interest rates and the volatility of financial asset prices exceptionally low.

Investors are searching for yield, and prices of financial assets have been rising constantly. Interest rates on corporate and **sovereign bonds** have fallen to their lowest levels since the crisis (see Figure 1.1.1). Interest rate spreads on sovereign bonds have also fallen very low, and the conditions for debt financing for the governments of the euro area countries with the worst problems have improved markedly as a result (see Figure 1.1.2). The high demand for yield has led to increased issuing of low-grade **bonds**, while **stock markets** have climbed to new peaks (see Figure 1.1.3).

Higher prices for riskier assets indicate a **build-up of risk** in the financial system. The relative improvement in the performance of the US economy compared to those of other advanced regions, and the increase in economic growth there, will lead the Federal Reserve to raise base interest rates. After substantial rises in asset prices, the **end of monetary policy stimulation** may create instability in the financial markets. As bond prices are very high, even a small change in interest rates will have a significant effect on them.

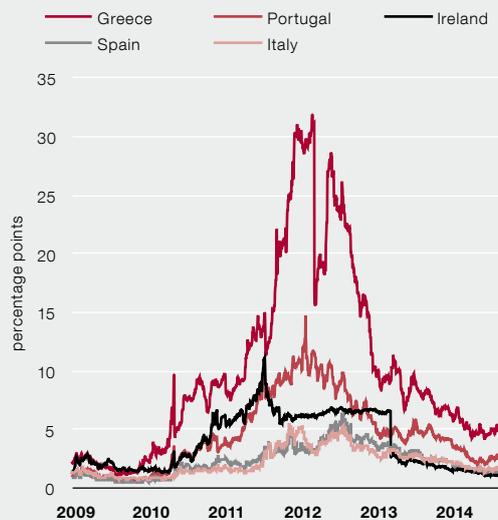
¹ This review covers market data from the end of March 2014 to the middle of September.

Figure 1.1.1. Interest rates on ten-year government bonds of Germany and the USA



Source: Bloomberg

Figure 1.1.2. Spread of ten-year bonds of Greece, Portugal, Ireland, Italy and Spain over Germany



Source: Bloomberg

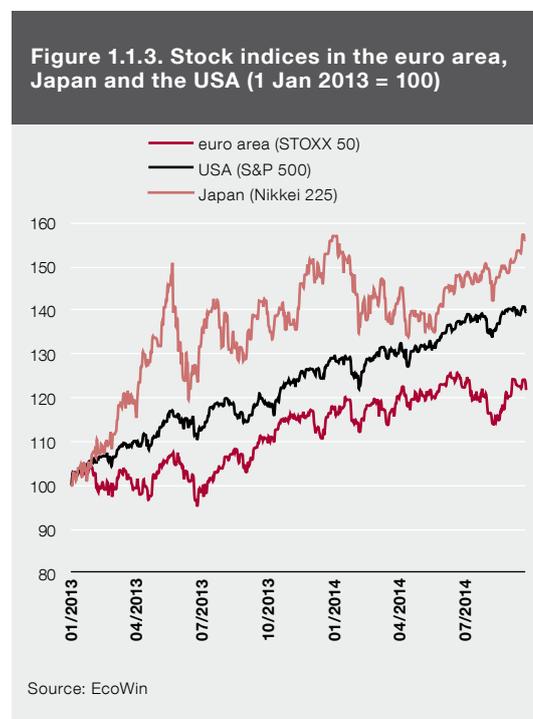
If interest rates start to rise and investors then decide to change their strategy in the new circumstances, the market for **lower-rated bonds** will be vulnerable, as will the shares that were bought in the search for higher yield. If interest rates for risk-free assets start to rise, then some money will be re-directed to higher quality bonds with more stable yield. Another danger for the lower-grade bond markets is that banks are not holding as many bonds on their balance sheets because of changes in the legal requirements. The **liquidity** of this segment of the bond market may as a result be much lower during a downturn in the market than many investors are assuming. This in turn will increase the risk of a major fall in the prices of financial assets.

The second main danger for international financial markets is **geopolitical circumstances**, notably a worsening and widening of the conflict between Russia and Ukraine, a further spread of the crisis in the Middle-East, or the emergence of any other geopolitical clashes. The impact of geopolitical tensions on financial markets has so far been short-lived and small. Depending on the nature and extent of tensions, they could yet cause a sharp change in prices of financial assets.

The state and the risks of European Union banking

Although confidence in banking in Europe has improved somewhat in the past half year, vulnerabilities still remain in the banking sector. Banks have had to deal with new legislation coming into force, particularly changes resulting from the introduction of the banking union (see Box 1). The biggest problem for banks remains the vulnerabilities in their balance sheets.

Banks have continued **cleaning up their balance sheets**, and **provisions** have increased



significantly. The clean-up of the balance sheets can be attributed to the comprehensive assessment and to preparations for the launch of the banking union. The stock of problem loans grew in the early part of this year, albeit at a somewhat slower rate. The growth in the stock of problem loans means that larger loan loss provisions are needed, and this is currently one of the main reasons why profits are still small. In the current economic climate, asset quality could deteriorate for those banks that have large exposures in emerging market economies.

There remain limits on the ways that profitability and bank lending can be increased. The **profitability** of the biggest banks in the euro area² improved slightly both in 2013 and in early 2014 from a year earlier (see Figure 1.1.4). However, many banks still made a loss in the last quarter of last year. This was primarily because of the

² Under the definition of the European Banking Authority this applies to 56 large banks.

Figure 1.1.4. Return on equity ratio of large European banks

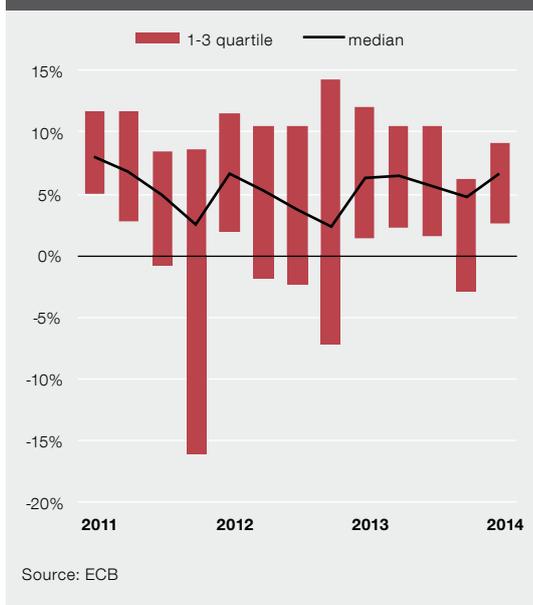
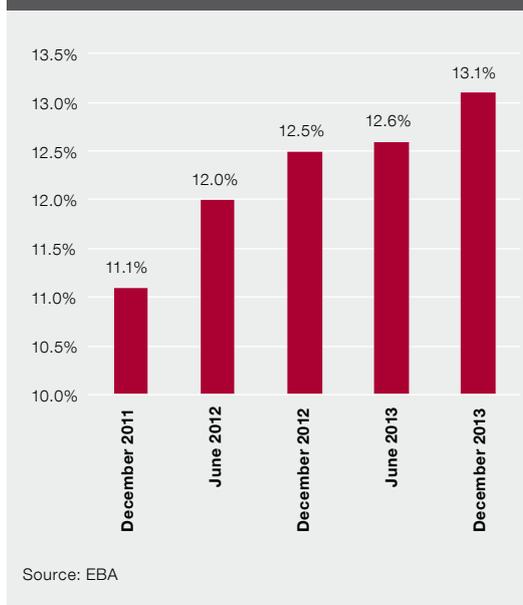


Figure 1.1.5. Tier 1 capital ratio (weighted average) of large European banks



increased provisions, though there were also one-off factors in the form of changes made in advance of the comprehensive assessment, high litigation charges, and a significant decline in fixed-income trading revenues. Profitability will also be held back in future by the low interest rate environment and the prospect of a weak macroeconomic outlook.

Despite the weak profitability and low economic growth, the **capital positions** of European

banks as a whole have strengthened significantly (see Figure 1.1.5). The levels of capitalisation vary from country to country, and in some countries the banks haven't even managed to attain the required levels of capitalisation. With loan losses and weak profitability, balance sheets have been strengthened mainly through equity issuance. Improved confidence among investors and consistently favourable market conditions have helped in raising additional capital.

Box 1: The current state of the single European banking union

Following the global financial and debt crisis, the European Council decided in June 2012 to strengthen the European Union's financial framework and set out the aim of creating a banking union. This was based on three pillars: a single supervisory mechanism for banks, a single resolution mechanism and a bank deposit scheme (see Figure B1.1). The banking union covers all the member states of the euro area, but it is expected that states that are not in the euro area will also join. Preparations were started in autumn 2013 for the first pillar of the banking union and discussions about the second pillar started at the end of 2013. The third pillar has been put

on hold for now and deposit insurance will continue to be regulated in future by the EU directive on deposit guarantee schemes.

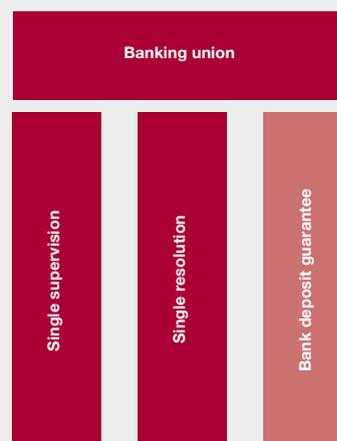
Single supervision

Single supervision will increase Europe's financial integration and stability. To improve the sustainability of the European banking system, a single framework is being introduced for banking supervision that will strengthen and harmonise the supervisory practices used up until now. When the regulation on the single supervisory mechanism³ comes into force from 4 November 2014, the European Central Bank will directly supervise more than 120 systemically important banks in the euro area. The ECB is responsible for single supervision and will work with the national competent

authorities at the same time to coordinate their work. National authorities will retain supervisory responsibility for less important banks. The banks licensed in Estonia that will pass under the direct supervision of the European Central Bank are Swedbank and SEB⁴.

Before it assumes its direct supervisory role, the European Central Bank worked with the national authorities to carry out comprehensive assessment of the banks⁵ to get a sufficiently clear picture of the financing of the commercial banks. The stress test is being complemented for the first time by an asset quality review. More detailed results from the assessment will be published for individual banks and for countries and also as an aggregated report. The reports on the banks will contain a summary of their main financial figures and detailed results from the asset quality review and the stress test. This will be accompanied by further important information on additional capital issuance in 2014. The results will be published in the second half of October 2014, immediately before single banking supervision starts. If the baseline or adverse scenarios of the stress tests reveal that any bank is short of capital, that bank will have two weeks to submit a capital plan to the national competent authority, describing how the shortfalls will be covered and from where.

Figure B1.1. The three pillars of banking union



3 EU regulation 1024/2013

4 Banks covered by single supervision: <http://www.ecb.europa.eu/pub/pdf/other/ssm-listofsupervisedentities1409et.pdf?d719f862cf7c9cef3b85830f463bda3f>

5 A more detailed assessment is given in Financial Stability Review 1/2014.

Single resolution mechanism

Detailed discussions for the second pillar of the banking union started in summer 2013, and in July 2014 the Council of the European Union approved the regulation for the single resolution mechanism⁶. Single resolution means that decisions on resolving crises in banks in participating countries will be taken centrally and tax payers will be protected effectively. Decision-making is coordinated to a defined extent. A central single resolution board will be set up to make sure that crises are handled the same way throughout the European Union, and to reduce problems of coordination between member states.

The single resolution board will also manage the single resolution fund that will be set up. The target size of the fund will be 1% of covered deposits, or around 55 billion euros, which will be collected in contributions paid by the banks over eight years. Each bank's contribution is based on the fixed amount determined from that institution's liabilities and a risk adjusted contribution that depends on the risk profile of that institution.

The new single resolution mechanism will start operating from 1 January 2016. The resolution tools are set out in the directive on the recovery and resolution of credit institutions and investment firms⁷, which came into force in summer 2014.

From deposit guarantees to a directive on deposit guarantee schemes

The third pillar of the banking union, the harmonisation of guarantees for bank deposits, remains on a back burner for now. The current deposit guarantee system of the European Union was extended by changes to the current directive on deposit guarantees. Among the changes was the harmonisation of definitions for the scope of covered deposits and the shortening of the deadline for repayment from twenty days to seven by 2024 under the directive on deposit guarantee schemes⁸. The directive entered into force in summer 2014.

6 EU regulation 806/2014

7 EU directive 2014/59

8 EU directive 2014/49

1.2. ESTONIAN FINANCIAL MARKETS

Bond and stock markets

The local Estonian securities markets are small in size and quiet in activity. The total capitalisation of bonds issued and stocks quoted on the exchange stood at 2.3 billion euros at the end of August 2014, or 12% of GDP. The small size of the market means that the risks to Estonian financial stability from the local securities markets are small.

A rapid increase in the last quarter of 2013 in the volume of bonds issued proved temporary and was caused by large issues by individual companies (see Figure 1.2.1). The increase in activity in the bond market was not broad based and 19 million euros of new bonds were issued in the first half of 2014, which was about the same as a year earlier.

Because issue volumes for new bonds were low, the total capitalisation of bonds shrank by 4.3% from the start of the year to 541 million euros by the end of August, or 2.8% of GDP.

The secondary market for bonds became even more passive in the first half of the year and an average of around 900,000 euros of transactions were made in each quarter, which is around one third of the quarterly average of the last two years.

The OMXT index of the Tallinn stock exchange fell at the start of March because of geopolitical tensions to below where it had started the year, and the rise in subsequent months was not enough to offset that fall, meaning prices remained down on the exchange (see Figure 1.2.2). By the end of September the index had lost 6% of its value from the start of the year.

The fall in share prices reduced the capitalisation of the Tallinn exchange by 141 million euros over

Figure 1.2.1. Total volume of bonds issued and new bonds issued quarterly

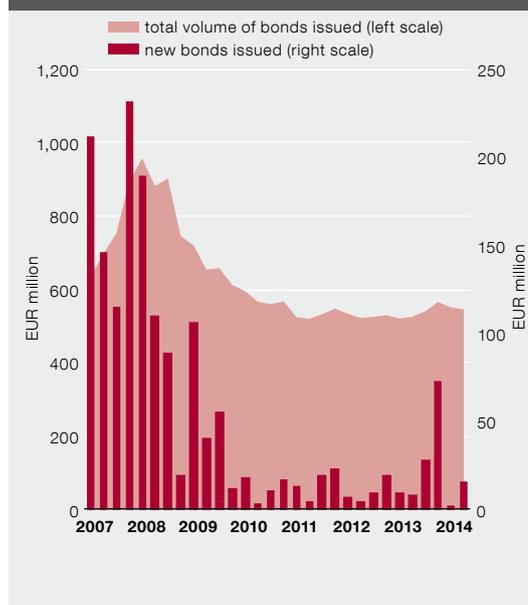
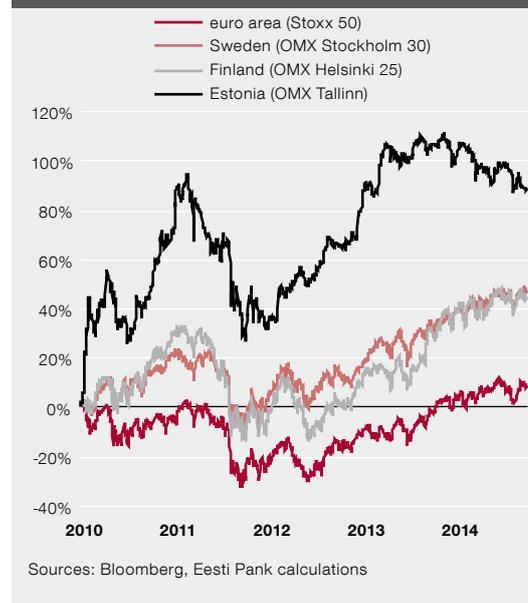


Figure 1.2.2. Tallinn Stock Exchange OMXT index and euro area, Finnish and Swedish indices, change from the beginning of 2010



Sources: Bloomberg, Eesti Pank calculations

eight months, so that it stood at 1.7 billion euros or 9.1% of GDP at the end of August.

Trading was thin on the Tallinn exchange throughout the first eight months of the year and turnover was lower in all of those months than the average monthly turnover of the past five years at 11 million euros a month. A majority of the transactions were with the shares of six companies, which together accounted for 90% of all the transactions on the exchange.

The share of non-resident investors was somewhat lower than at the start of the year and their investments provided 40.3% of the capitalisation of the exchange by the end of August, having ended last year with 42%. The biggest retreats were among investors from the Cayman Islands, the USA and Finland. The largest foreign investors were those from Luxembourg, who accounted for 10.7% of the total market value, and those from the Cayman islands, who accounted for 6.9%.

Investment and Pension Funds

The value of the assets of investment funds increased over the year to the end of August by 14.6%. This came from both growth in the value of investments and inflows of cash into the funds. Assets of the second pension pillar were up 18.7% from the start of the year and those of the third pillar by 10.5%. The assets of investment and pension funds were worth almost 2.9 billion euros at the end of August (see Figure 1.2.3) or 15% of GDP. The majority of the assets of the funds were accounted for by the 2.2 billion euros of the pension funds.

The annual returns of both investment and pension funds was positive at the end of August (see Figure 1.2.4). The net value of units in equity funds increased on average by 12.3% over the year and those in interest funds by 3.3%, while

Figure 1.2.3. Structure of investment and pension fund assets and the share of investments in funds

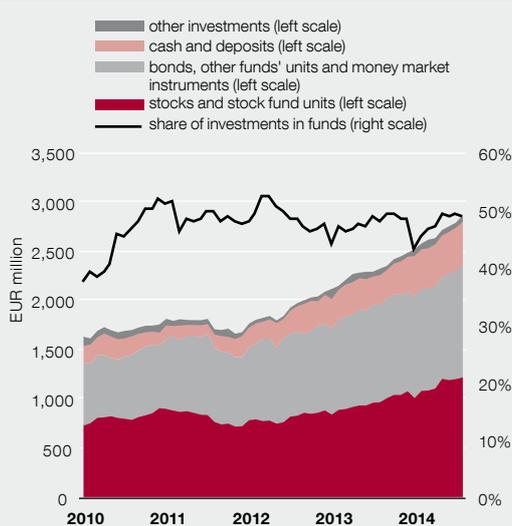
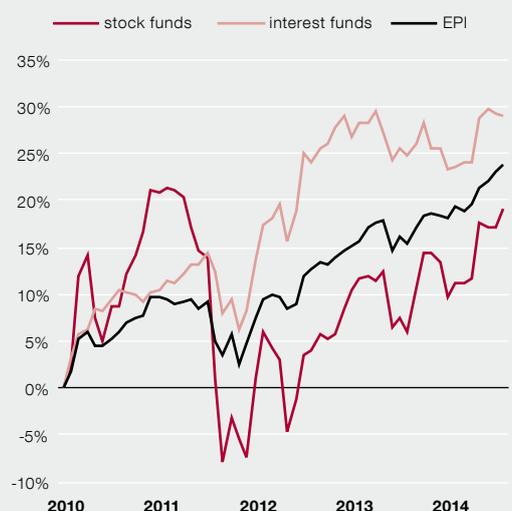


Figure 1.2.4. Changes in the net asset value of investment fund units and the EPI index of Estonian Pension Funds from the beginning of 2010



the EPI index showing the general return of pension funds was up 7.4%.

The structure of investment and pension fund assets has not changed particularly over the past year. Shares and equity funds held 42% of total assets at the end of August, bonds and bond funds 39% and deposits 16%. There was again a relatively large share of fund investments in the structure of investment assets, as almost half of the assets of investment and pension funds were in units of other funds in August this year.

The share of foreign assets in the assets of investment and pension funds was no different at the end of August from what it was at the end of last year at 74%. A dominant proportion of the foreign assets were securities registered in other European countries, which made up 63% of total assets at the end of August. The share of total fund assets that were invested in registered securities in Russia and Ukraine at the end of August was only very small at 1.2%, meaning the direct impact of geopolitical tensions on the value of the assets of Estonian pension and investment funds was also very small.

Box 2: Returns on mandatory funded pensions and the factors affecting them

Mandatory funded pension funds are intended to ease the problems caused by demographic changes and to provide additional income for people beyond retirement age. Everyone born after 1983 must join a mandatory pension fund and this means many people are affected, so in consequence the return on the funds needs to be sufficient and should help achieve the aims of the mandatory funded pension.

The return on mandatory funded pension funds is measured using the EPI indices. There are four of these with different risk levels, called EPI-00, EPI-25, EPI-50 and EPI-75, which cover pension funds which have 0%, 25%, 50% and 75% respectively invested in shares⁹. When considering the return on pension funds it is important to look at real returns as well as nominal returns, as these take account of changes in general price levels and allow assessment of whether the real value of the savings going into the pension is actually increasing.

The nominal value of units in pension funds had risen by the end of July this year by between 2.9% and 4.5% a year on average since the funds were set up, depending on their level of risk. The average real return has been positive for most of the pension funds covered by the EPI-50 and EPI-75, which have larger weightings of shares (see Figure B2.1). However, the value of the other funds with less than 50% in shares has fallen on average.

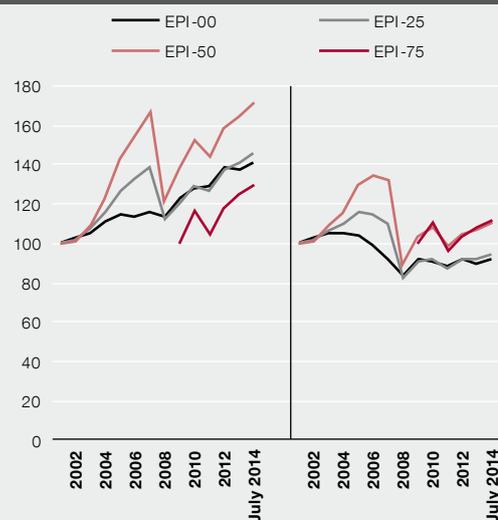
The return of pension funds is mainly affected by three factors: the overall return of securities markets, the structure of pension fund assets, and the operating costs of the funds.

The average return on securities markets since the pension funds were started does not compare well with earlier returns, and the returns in 2002–2013 were clearly lower than the average

⁹ The EPI-75 index is not directly comparable with the other three as it was first calculated only in 2010.

for the preceding years (see Figure B2.2). The overall return on securities markets was affected a lot by the major fall in share prices during the global financial crisis, as the S&P 500 in the USA was down 38% in 2008 and the Stoxx 50 index in Europe was down 44%. The sharp fall in share prices had a negative effect on the returns of pension funds, and the EPI indices fell between 2% and 27% in 2008. The largest losses in value were in pension funds with a heavy weighting of shares. The fall in the pension funds with larger investments in shares in 2008 was almost three times the average annual return prior to that. Investments in shares have historically been riskier than investments in bonds due to the higher volatility of the stock market, but in the longer term investments in shares have had higher returns than investments in bonds.

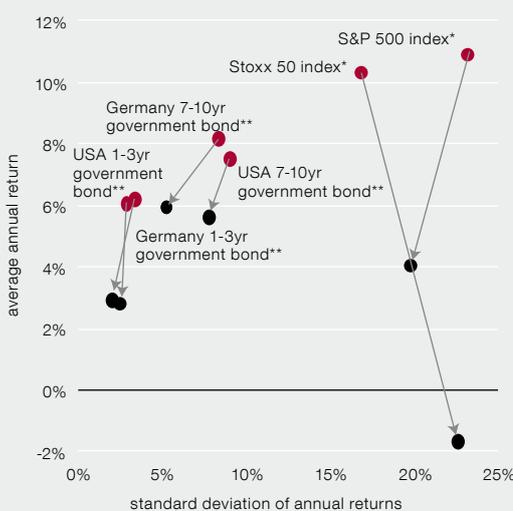
Figure B2.1. Estonian Pension Fund indices and inflation-adjusted Pension Fund indices



Sources: Pensionikeskus, Statistics Estonia, Eesti Pank calculations

The assets of Estonian pension funds include a relatively large share of fund investments, which have been at around 50% for five years. This is reflected in the relatively passive investment strategy of the pension funds, as only a relatively small 6% of total pension fund assets are invested directly in company shares. The share of fund investments varies quite widely though and there is no major link between a fund's return and the share of fund investments for the pension funds with larger exposure to shares. This means the relatively large share of investment in funds does not have a significant impact on the return of funds exposed to shares. The average return on bond funds with a larger share of fund investments has in the past three years in general remained

Figure B2.2. Changes in average annual returns of securities markets and changes in standard variations of annual returns



* 1990–2001 vs. 2002–2013
 ** 1992–2002 vs. 2002–2013
 Source: Bloomberg, Eesti Pank calculations

below that of funds with a smaller share in fund investments (see Figure B2.3).

The management fees for pension funds in the Estonian second pillar are fixed and do not generally depend on the volume of assets in the fund or on its returns. The global pension statistics published by the OECD in 2013 show that the operating costs of Estonian pension funds as a ratio to assets were among the highest of any nation in 2012 (see Figure B2.4¹⁰). This means the operating costs of Estonian pension funds are eating away relatively more of the net return than is the case elsewhere. As the total size of assets of Estonian pension funds is smaller than in other countries, the cost economies of scale are also modest.

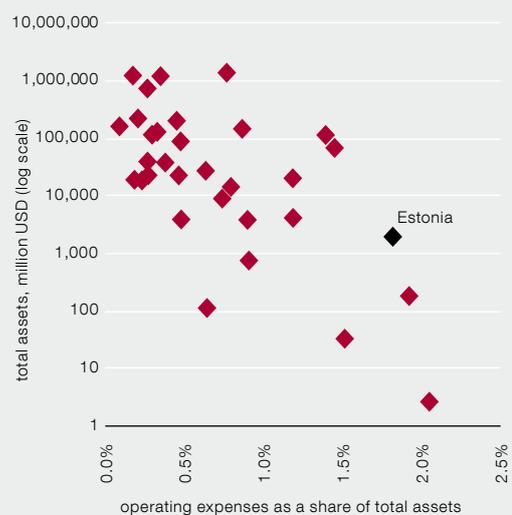
The biggest impact on the average return of Estonian pension funds since they were started has come from the fall in securities prices caused by the global financial crisis, which significantly reduced the value of the assets of the funds. The return has also been brought down by operating costs, which are relatively larger than those in other countries. Pension funds with larger investments in shares have managed to make a positive real return since they were set up, but the real net value of units of pension funds with larger investments in bonds has on average fallen at the same time. As the negative impact of low interest rates will probably continue in the near future, the return on funds investing mainly in bonds is likely to remain poor for the time being.

Figure B2.3. Annual average return of pension funds (2011–2013) and share of investments in funds



Sources: Pensionikeskus, Eesti Pank

Figure B2.4. Pension funds' operating expenses as a share of total investments and total assets in selected OECD and non-OECD countries, 2012



Source: OECD Global Pension Statistics

10 The structures of the national pension systems in the Figure may be different.

1.3. MARKET-BASED FINANCING OF BANKING GROUPS

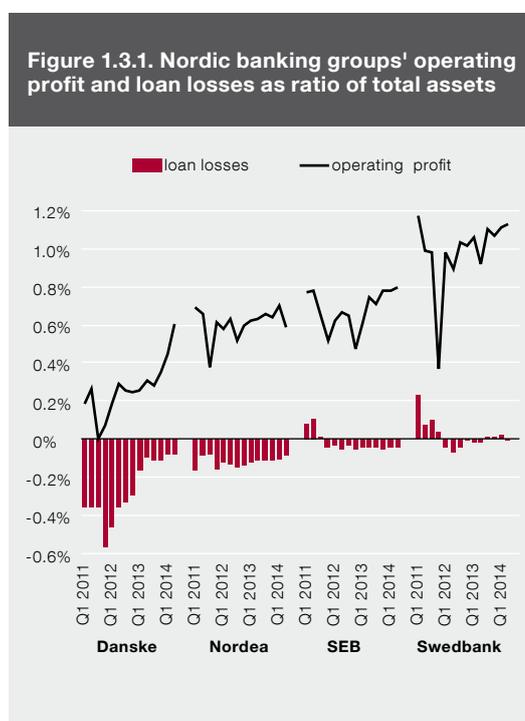
Financial strength of the groups of parent banks

The **operating environment** of the Nordic banks has been affected by low interest rates in the past half year, and together with continuing confidence in the banks this has lowered the cost of market based funding, though at the same time it has also reduced the net interest margin earned from the difference in the prices of lending and deposits. Low base interest rates have reduced the cost to clients of servicing loans and have encouraged investment activity. Rises in stock markets have led to increases in the value of assets under management and have also increased the income earned from service fees.

The **profitability** of the four biggest bank groups operating in Estonia was stable or increasing in the first half of 2014 (see Figure 1.3.1).

Improved profits and the expectation of stricter requirements have led to improved **capitalisation of the banking groups**. The Common Equity Tier 1 of Swedbank stood at 20.9% of risk weighted assets at the end of the second quarter, while the figure for SEB was 16%, for Nordea it was 15.2%, and for Danske Group it was 14.5%.

Figure 1.3.1. Nordic banking groups' operating profit and loan losses as ratio of total assets



The banking groups consider that the main danger ahead is that the economies in their regions of operation will recover more slowly than expected. It is expected that the effect of tensions and sanctions between the European Union and Russia will mainly be felt via domestic clients. The banks only have small direct positions in Ukraine and Russia (see Table 1.3.1). The biggest loan positions, at around 2% of total assets of the group, are held by Nordea, which finds that the lending volumes and margins of its subsidiary in Russia did not change significantly in the

Table 1.3.1. Geographic distribution of the positions of Nordic banking groups

	Danske	Nordea	SEB	Swedbank
Sweden	9%	25%	72%	86%
Norway	9%	16%	2%	3%
Denmark	67%	24%	1%	0%
Finland	12%	28%	1%	1%
Baltic states	1%	2%	8%	10%
Germany	0%	0%	13%	0%
Russia	0%	2%	0%	0%
Ukraine	0%	0%	0%	0%
other	2%	3%	3%	0%

Source: Banks public reports, Riksbank

first half of 2014. The Finnish economy is most vulnerable to a worsening of trade relations with Russia as Russia takes around 9% of Finnish exports. However, the overall impact of sanctions in the near future is expected not to be very significant.

Although the economic outlook for the Nordic countries has been corrected downwards in recent months, particularly because the recovery in export markets is expected to be slower, a resurgence in the external environment is still expected in the longer term.

While companies are continuing to be quite conservative in their borrowing, the borrowing behaviour of households has not been affected so much by geopolitical tensions or downward revisions of expectations for economic growth, despite high debt burdens¹¹ (see Figure 1.3.2). As lending has increased, so real estate prices have risen (see Figure 1.3.3).

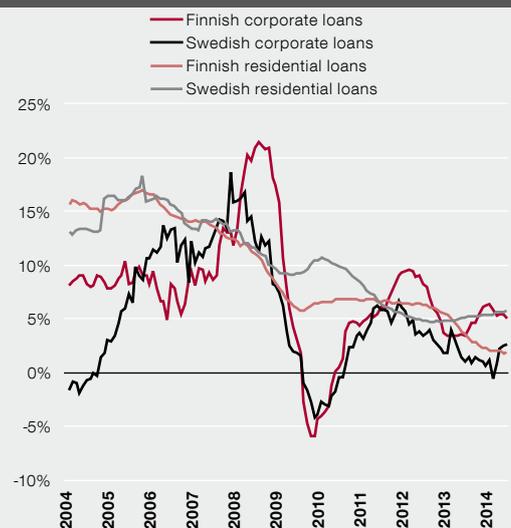
Household debt burdens are seen as a possible accelerator of negative trends in the Nordic countries. It is assumed that any decline in confidence will restrict household consumption, and this will then reduce domestic demand.

To boost confidence in the banks and to head off the dangers that may have been underestimated, the central banks, supervisory authorities and ministries of the Nordic countries have already taken and planned various **measures to increase confidence in the banks**.

In **Sweden** the financial supervision authority announced in September that bank groups there will have to follow a risk weight floor of 25% for real estate loans issued in Sweden (see

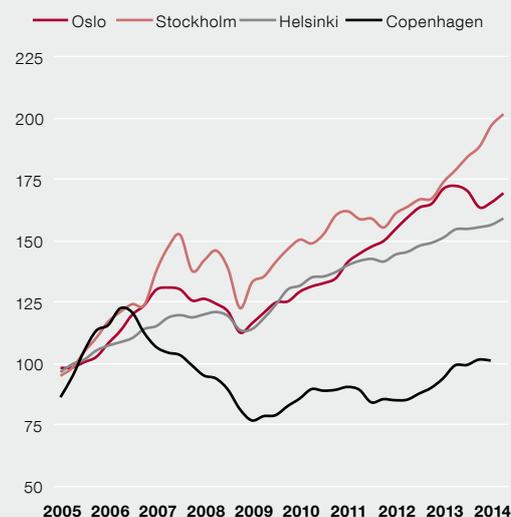
11 The household debt burden in Denmark exceeds 250% of gross disposable income, in Norway it is about 200%, in Sweden it is 150% and in Finland it exceeds 100%.

Figure 1.3.2. Annual loan growth in Finland and Sweden



Source: European Central Bank

Figure 1.3.3. Price indices of apartments in capital cities of Nordic countries



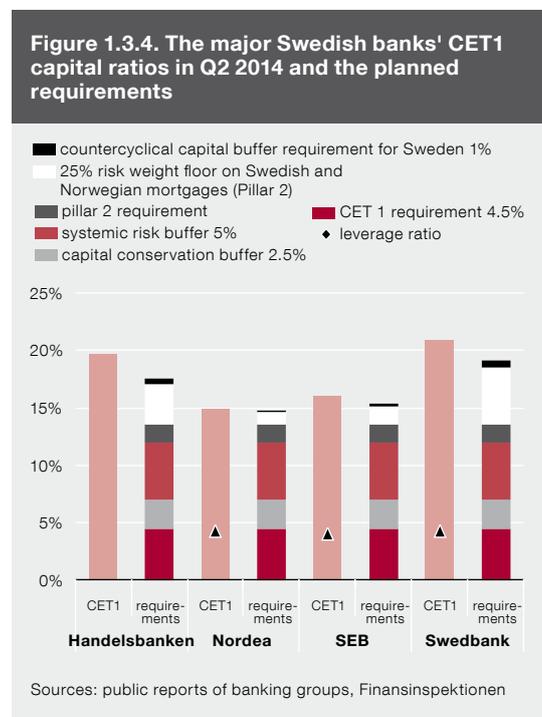
Sources: statistical offices, Valueguard, Association of Danish Mortgage Banks

Figure 1.3.4). Norway had already announced a plan to introduce a risk calculation methodology for real estate loans issued in Norway that will have a similar effect to a risk weight floor of 20-25%, and so the Swedish authorities have decided to ask the banks to apply a minimum risk weight of 25% in solidarity on real estate loans issued in Norway. On top of this, from summer 2015 banks will also have to hold common equity tier 1 funds of 1% of loans issued in Sweden to meet the countercyclical buffer requirement. It is expected that in future banks will further reduce their share of non-amortising loans and the principles for assessing the ability of bank clients to service their loans are to be further harmonised.

As well as tightening the capitalisation requirements for real estate loans and imposing a requirement to hold countercyclical buffers, Sweden will introduce a systemic risk buffer of 5% on a consolidated basis for systemically important banks from 1 January 2015. Two percentage points of this is planned as a supervisory requirement.

In **Norway**, increased minimum requirements for risk calculations will apply for domestic real estate positions approximately equalling a risk weight requirement of 20-25%. In addition, a 1% countercyclical buffer will apply for domestic positions from July 2015, and an additional requirements of 1% for systemically important institutions will come into force from July 2015 and July 2016 on top of the 3% systemic risk buffer that currently applies.

In **Denmark** the principles for provisioning for problem loans and risk assessments for banks have been made stricter. Changes are planned to regulations to put more of the risk arising from mortgage-backed securities onto the buyer of the securities. The long-term goal for capitalisa-



tion is gradually to raise the CET1 requirement to 10.5% for all banks, while it is planned that requirements for systemically important banks will rise to 13.5% by 2019.

In **Finland** the focus has mainly been on economic policy measures outside the banking sector.

Financing and liquidity of parent banks

Market-based financing supplies almost half of the funding base for Swedish banks and a large part of it is in bonds issued in foreign currencies (see Figure 1.3.5). This makes the funding of Swedish banks vulnerable to shocks in the financial markets that could cause foreign investors to lose their desire to invest in such securities.

Almost half of the funds from financial markets are covered bonds, which are mostly backed by mortgage loans that the banks have issued. Although the value of the collateral provided by

mortgages is sufficiently higher than the value of the covered bonds, with excess coverage of more than 40% for the most part, there remains the danger that it could become harder and more expensive for banks to issue new covered bonds if households should have difficulties meeting repayments.

One possible risk identified by Riksbank in its 2014 Financial Stability Review¹² was the structural liquidity risk of Swedish banks, which reflects the relatively large difference in the maturities of the liabilities and assets of the banks. A large part of the long-term assets of the Swedish banks in the form of housing loans and corporate loans are covered by short-term financing from the financial markets. The structural liquidity ratio¹³ calculated by Riksbank is below the average for other comparable European banks for all the larger Swedish banks.

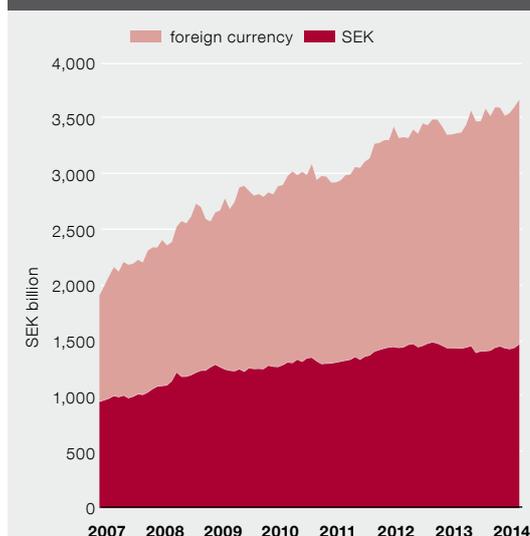
The structural liquidity risk of the Swedish banking system is also exacerbated somewhat by the interlinkages in the market-based financing of the banks. The Riksbank finds¹⁴ that the larger banks held nearly 20% of each other's covered bonds. Some of these are held to maintain liquidity buffers and to fulfil market-maker obligations, which are often financed with very short-term funds like certificates and repos. This means that a part of the long-term loans, principally mortgages, are funded in the banking system by funds that have a maturity of less than a year. Although there is usually sufficient liquidity in the covered bond market, the arrival of tensions could significantly harm liquidity in the market and could lead to problems with funding.

¹² Financial Stability Report 1/2014, Riksbank.

¹³ The structural liquidity ratio shows the proportion of less liquid assets that are covered by stable financing.

¹⁴ Financial Stability Report 1/2014, Riksbank.

Figure 1.3.5. Wholesale funding of the major Swedish banks



Source: Riksbank, Financial Stability Report 1/2014

To strengthen the funding structure of the banks, the eight largest banks in Sweden have been subject to a minimum liquidity coverage ratio, LCR, of 100% since 2013, both in overall terms and for the euro and the dollar separately. The Swedish central bank has recommended to the supervisory authorities that a separate LCR of 60% should be set for the positions of the banks in Swedish krona.

The latest economic reports from the banks make clear that their short-term liquidity is good and their buffers are sufficient. The banks exceeded the minimum liquidity coverage ratio, both overall and for the euro and the dollar separately. As a relatively large part of the funding from financial markets is in foreign currency however, the liquidity buffers of the banks are also mainly in foreign currency, and the liquidity in Swedish krona is backed by foreign exchange swap contracts. This is why the LCR in krona is

lower and was 50% for the biggest bank groups last year in the estimate of Riksbank.

Market participants have so far considered Swedish banks to be relatively secure and this has allowed them to get funding from the markets easily and cheaply. The market interest rate of the covered bond, the main market-based funding instrument used by the Swedish parent groups, fell even further this year (see Figure 1.3.6).

Figure 1.3.6 Average covered bond yields of Swedish parent bank groups*

