

Government to the Rescue Dream or Nightmare ?

- **The Swedish Financial Crisis - How it was managed**

**ULI Europe Annual Conference
Paris, February 3, 2010**

Arne Berggren / Eusticon AB

Origins and results

The Swedish economy in 1992

- Diversified small open economy
- Large Public sector deficit and current account problem
- Rapid financial sector growth: from 90 to 140% of GDP over 4 years
- Rapid Real Estate prices growth: 25 % a year since 1985 to 1992

Origins of the crisis

- Mismanagement of macroeconomic policy
- Badly timed deregulation of capital markets and tax cuts
- External shocks (Unification of Germany, Gulf war etc)
- Adjustment of asset prices to the new macroeconomic environment and expectations
- Devaluation 1993

Main Problem in the banks

- High exposure to the real estate sector (where prices fell by 50% in one year)
- Sudden increase in NPLs leading to solvency problems

Structure of the banking system

- Before:**
- 252 finance companies and 107 banks
 - 6 largest bank groups: 75% of the system
 - 40% of bank lending in foreign currency

After: 133 finance companies, 4 of the largest banks remained

Duration of The crisis

- First signs in the finance companies 1990/91. The first bank failures came during 1992 and the peak was during 1993 following the devaluation when 5 of the biggest 6 banks applied for support. The General bank guarantee was withdrawn 1995.

Result

- Expenses/asset guarantees 6% of GDP. Final cost less than 0,5% of GDP

Managing the crisis

Objective

- **Restore confidence** in the payment and credit system as quickly as possible to **minimize macro costs**
- Main focus: international capital markets

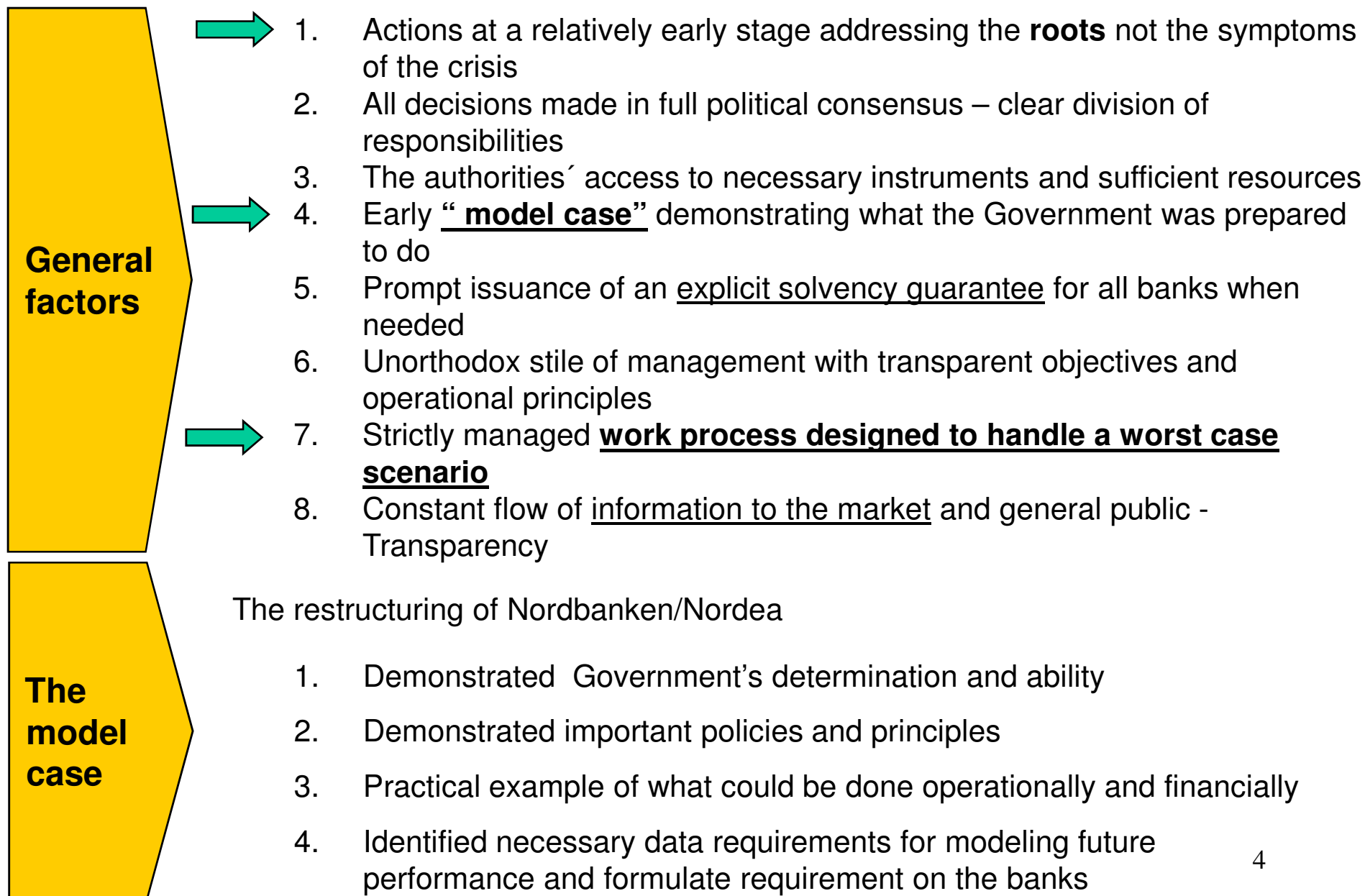
Strategy

- The State guarantees that banks and certain other institutions of systemic importance can meet all their commitments on a timely basis .The state shall meet its undertaking by providing support for viable institutions.... or for the restructuring or orderly wind-up those that can not be expected to become profitable

Basis for the strategy

- A worst case scenario
- Management issues and solvency

Success factors



Principles and Conditions for Bank Support

Support should:

- Be voluntary and adapted to the specific conditions of each institution
- Be based on commercial principles so as to minimize the long term costs
- Be structured so that the banks had no grounds for requesting more than needed

Considerations:

- Non-viable institutions restructured or closed in on orderly manner
- Measures taken should be competitive neutral and account for factors like efficiency and variety
- The Government's expenditures should be minimized and to the largest extent possible recovered

Requirements:

- Institutions applying for support should be required to produce plans for their handling of problem assets and for improving their core operations.

The question of ownership:

- Government ownership should be avoided unless considered appropriate with reference to capital requirements and the commercial interest of the state. In such instances the aim shall be to dispose of the shares when this is commercially suitable

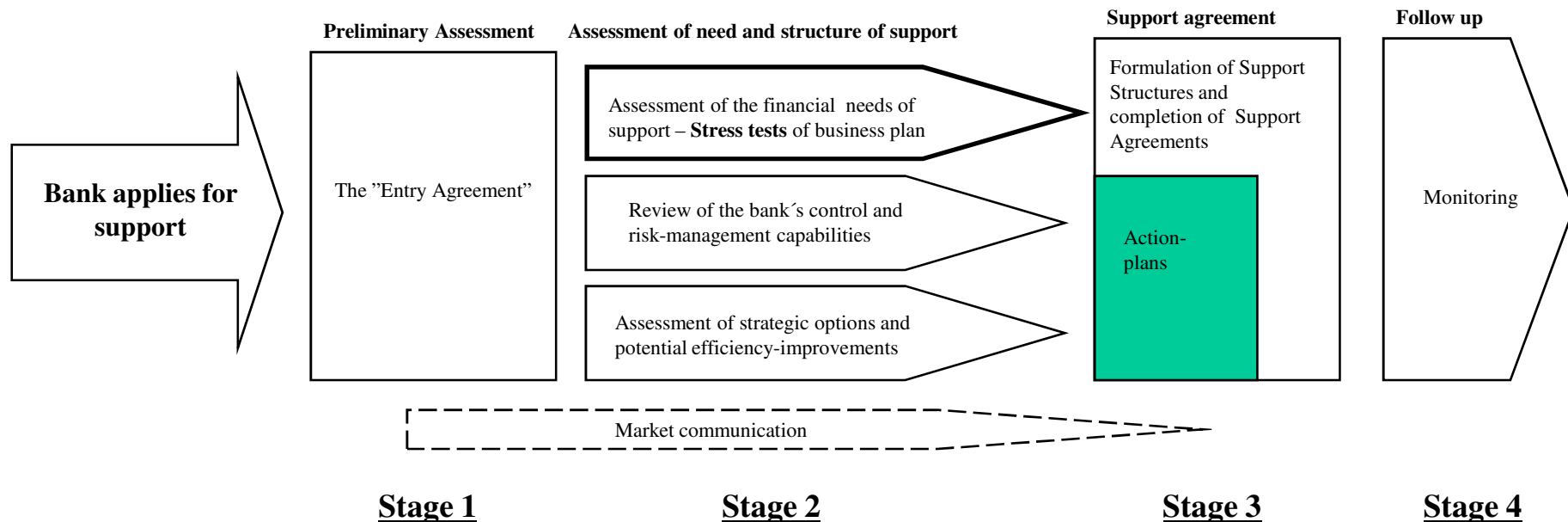
The Bank Support Process

Main components

- Macro economic forecasts -

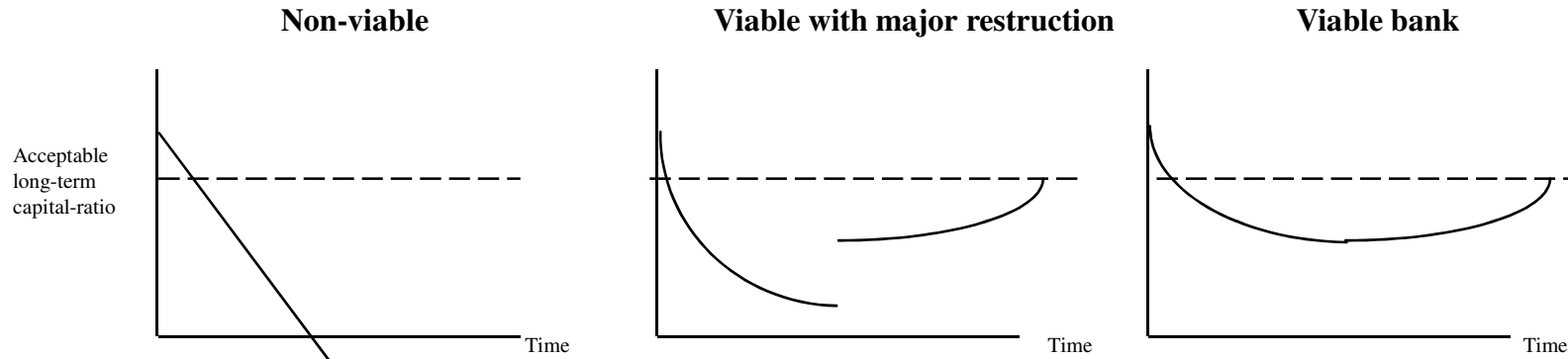
A perspective on the future structure of the banking industry

- Areas with potential for improvements
- Operational benchmarks



Type of bank support - Amount and structure

Projected performance



Measures:

- Liquidation
- Merger with viable bank

- Capital injection
- Cost-cuts and reorientation of operations
- Measures to improve operations
- Create specialised workout entities

- Asset guarantees
- Measures to improve profitability

