Editorial

Monetary policy implementation in changing times

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The coronavirus pandemic has brought monetary policy operations back into the spotlight, as central banks around the world have taken up new monetary policy measures. We too at the Eurosystem have swiftly launched new measures which support price stability and growth and employment in the euro area.



As a member of the ECB Governing Council, the Governor of the Bank of Finland participates in monetary policy decision-making. For these decisions to have an effect on the finances of European households and businesses, practical measures must first be taken in the financial markets—monetary policy has to be implemented.

Over the past decade, as a result of the global financial crisis, the European sovereign debt crisis and the coronavirus pandemic, implementing monetary policy has become considerably more multifaceted. Instead of largely relying on the main interest rate to guide economic activity, monetary policy implementation has been expanded to include targeted longer-term lending to banks, large-scale asset purchases, and forward guidance.

Euro area national central banks, such as the Bank of Finland, are responsible for implementing

monetary policy. We issue central bank loans to banks operating in Finland. We purchase Finnish government bonds, covered bonds issued by Finnish banks, and corporate bonds as part of the Eurosystem's monetary policy purchase programmes. The benefits of cooperation are highlighted in crisis situations: as part of the euro area, Finnish banks and financial markets have access to the same funding channels at similar requirements as other entities in the area.

The Bank of Finland has currently issued over EUR 20 billion of central bank credit to banks. We issue credit at a negative interest rate. If and when our counterparties maintain their lending to the real economy, we reimburse them one percent of their loan amount during the first 12 months. In other words, a EUR 20 billion loan will shrink to EUR 19.8 billion in 12 months, even without amortisation. By offering central bank funding at exceptionally affordable rates we facilitate domestic bank lending to Finnish businesses and households. In doing so, we support economic growth and employment in Finland, which is needed for ensuring price stability in the euro area.

When we lend to banks, we always require that the loans be fully collateralised. Sufficiency of collateral can become an issue as credit volumes increase. To ensure that this does not prevent monetary policy from achieving its desired impact, the eligibility criteria for collateral have been relaxed in the euro area during the crisis. Most recently, the Bank of Finland decided to adopt its own framework for Additional Credit Claims (ACC) as of 1 September 2020. This means that, going forward, bank loans which do not satisfy all the standard eligibility criteria for collateral will exceptionally be accepted as such for monetary policy credit operations. These bank loans include, for example, loans guaranteed by Export Credit Agency Finnvera due to the coronavirus pandemic.

At the end of July the Bank of Finland's balance sheet contained nearly EUR 57 billion in securities held for monetary policy purposes. The majority of these securities comprise Finnish sovereign bonds. The Eurosystem currently holds a total of about EUR 40 billion of Finnish government and government-related bonds acquired for monetary policy purposes, which is nearly one-third of Finland's sovereign debt. When we purchase bonds, this lowers yields in bond markets and creates more favourable financing conditions for Finnish government, banks, households and businesses. This ultimately supports investment and consumption, as is currently required by the weak outlook for economic activity and inflation.

In addition to conducting monetary policy in the financial markets, the Bank of Finland manages financial assets currently totalling about EUR 11 billion. These assets include Finland's gold and foreign exchange reserves and the Bank of Finland's euro-denominated financial assets. We maintain foreign exchange reserves for monetary policy purposes and to safeguard liquidity in Finland in crisis situations. They are therefore invested in a secure and liquid manner. Our primary goals for managing our other financial assets are—within the constraints of monetary

policy—maintaining the real value of our balance sheet (i.e. generating a return), ensuring financial intermediation to domestic firms, and safeguarding financial stability.

In the early stages of the coronavirus pandemic, the Bank of Finland helped stabilise the market for Finnish commercial paper with its euro-denominated investment activities. Here investors had largely retreated from a market important for domestic corporate finance. In the acute phase of the crisis, the Bank of Finland purchased domestic commercial paper at a total of nearly EUR 1 billion. This helped restore normal market conditions and eased the pressure put on bank lending to firms when uncertainty was at its highest.

In managing our financial assets, we have recently increased the role of sustainability in our investment activities. As evidence of this, in December 2019 the Bank of Finland undersigned the UN Principles for Responsible Investment. The Bank has applied practices of responsible investment for several years already. By undersigning the Principles, we strengthened our commitment to the continuous development of responsible investment practices.

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Keywords

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