

**LAPSE OF  
TIME**

SM/20/99  
Supplement 1

July 9, 2020

To: Members of the Executive Board

From: The Secretary

Subject: **Denmark—Financial System Stability Assessment—Draft Press Release**

Board Action:	Executive Directors' <b>consideration</b> on a lapse of time basis
Deadline to Request Board Meeting:	<b>Monday, July 13, 2020 12:00 (noon)</b>
Publication:	Yes*
Questions:	Mr. Elekdag, MCM (ext. 34835)

**\*Unless an objection from the authorities is received prior to the conclusion of the Board's consideration, the press release will be published.**





## IMF Executive Board Concludes 2020 Financial System Stability Assessment with Denmark

FOR IMMEDIATE RELEASE

**WASHINGTON, DC – August 12, 2020** the Executive Board of the International Monetary Fund (IMF) concluded the Financial System Stability Assessment<sup>1</sup> with Denmark on July 15, 2020 without a meeting.<sup>2</sup>

Much of the work of the Financial Sector Assessment Program (FSAP) was conducted prior to the COVID-19 pandemic. Given the FSAP's focus on medium-term challenges and vulnerabilities, however, many of its findings and recommendations for strengthening policy and institutional frameworks remain pertinent. This report reflects key developments and policy changes since the FSAP mission work was completed, and includes illustrative scenarios to quantify the possible implications of the COVID-19 shock on the solvency of systemically important financial institutions (SIFIs).

Prior to the COVID-19 pandemic, the Danish authorities had taken important steps to improve financial system resilience. The authorities had actively used macroprudential tools to bolster the robustness of the financial system. The supervision of the banking and insurance sectors had improved. Likewise, recent legislation has strengthened anti-money laundering and combating the financing of terrorism (AML/CFT) supervision. Major reforms such as a new bank resolution framework had also considerably improved Denmark's financial safety net and crisis management frameworks.

According to the FSSA, solvency stress tests indicate that while the COVID-19 shock would have a significant and differentiated impact on capitalization ratios, all SIFIs would meet their minimum capital requirements. Given the unprecedented nature of the ongoing pandemic, these findings are associated with a substantial degree of uncertainty and subject to downside risks: A further deterioration of macrofinancial conditions could bring about a situation where some SIFIs breach their minimum capital requirements. Mortgage credit institutions play a central role in the domestic interbank system and can generate significant contagion effects.

Danmarks Nationalbank (DN) promptly provided liquidity support in response to the intensification of the crisis and has launched liquidity facilities and has reactivated swap lines. Looking ahead, DN should continue to enhance its operational preparedness for nonstandard liquidity support, including by refining the framework for accepting credit claims as nonstandard collateral. Notwithstanding a significant strengthening of the crisis management framework in recent years, the autonomy of the resolution authority should be strengthened, resolution planning for systemic institutions should be accelerated, and strategies for liquidity assistance to institutions in resolution should be defined. The operational independence of the Danish Financial Supervisory Authority (DFSA) should be safeguarded and it would benefit from a further increase in resources. The DFSA must complement its strong credit risk skills in banking with equal rigor in other areas (such as governance, compensation practices, and risk

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<sup>1</sup> The Financial Sector Assessment Program (FSAP), established in 1999, is a comprehensive and in-depth assessment of a country's financial sector. FSAPs provide input for Article IV consultations and thus enhance Fund surveillance. FSAPs are mandatory for the 29 jurisdictions with systemically important financial sectors and otherwise conducted upon request from member countries. The key findings of an FSAP are summarized in a Financial System Stability Assessment (FSSA).

<sup>2</sup> The Executive Board takes decisions under its lapse-of-time procedure when the Board agrees that a proposal can be considered without convening formal discussions.

culture). Insurance supervision should be further strengthened by increasing on-site inspection frequency, completing a solid risk assessment framework, and enhancing the oversight of cross-border business. Denmark should continue strengthening AML/CFT supervision, including by intensifying on-site inspections of higher-risk financial institutions. Going forward, to reduce inaction bias, the institutional arrangements for macroprudential policy can be improved by streamlining the decision-making process to reduce inaction bias.