



Financial markets survey

Autumn 2018

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With effect from autumn 2018, the Riksbank will send out a recurring questionnaire (the Financial markets survey) to participants active in the Swedish fixed-income and foreign exchange markets.¹ The purpose of the survey is to obtain an overall picture of the participants' views on the functioning of the Swedish financial markets, market activity and risks perceived in the Swedish financial system going forward. This report describes the results of the survey where responses were received between 6 and 16 November 2018.² The account is based solely on the participants' responses and does not reflect the Riksbank's assessments.

Survey results – autumn 2018

The Swedish housing and property market is the risk factor most often mentioned

When the participants are asked to describe which external events risk having a negative effect on the Swedish financial system going forward, they see a severe deterioration in the Swedish housing and property market as the main risk factor. In addition, they mention credit and liquidity risks, market risks arising from for instance Brexit, as well as increased regulations.

A majority of the participants consider themselves as taking low or neutral risks

Most of the participants describe their general risk taking on the market as low or neutral, and only a few participants consider their general risk taking to be high or very high. A clear majority of the respondents consider their risk taking as reduced or at the same level in comparison to the last six months. Most participants consider themselves as generally well prepared to deal with potential risks, such as credit and counterparty risks, market risks, liquidity risks and legal risks, but one in six participants say that they are poorly prepared for cyber risks.

Most participants perceive the market for the Swedish krona to be functioning smoothly

Most say that they perceive the market for the Swedish krona as functioning well. The normalisation of low interest rates is considered positive for the functioning of the market in the coming six months.

Opinion is divided on how well the Swedish fixed-income market is functioning

The number of participants who consider the fixed-income market to be functioning well or very well is around the same as the number who consider it to be functioning poorly or very poorly. A majority of the latter mention limited or poor liquidity as the main reason for their opinion and several mention the Riksbank's government bond purchases as one of the reasons. Many also consider a normalisation of the Riksbank's expansionary monetary policy, with quantitative tightening and interest rate increases, as an improvement of the market functioning over the coming six months.

Electronic trading platforms and algorithms often used by participants in the market for the Swedish krona

Almost all of the respondents who are active on the market for the Swedish krona state that

¹ The Riksbank conducted a semi-annual risk survey during the years 2008 to 2017, which was intended to provide an overall picture of the participants' views on financial risks and the functioning of the financial markets. In spring 2017, a review of the form for the Risk Survey was begun and this has now resulted in an updated survey that covers functionality, market activity, risks, risk taking and other overall questions with regard to both the fixed-income and foreign exchange markets. The name of the survey has therefore been changed to Financial markets survey. The Financial market survey supplements the regular contacts the Riksbank has with market participants.

² The survey was carried out with the aid of the survey tool Epsilon, which is supplied by the European Central Bank (ECB). The autumn survey was sent out to 99 participants, both Swedish and non-Swedish, who are active in the Swedish fixed-income and foreign exchange markets. 43 per cent of those surveyed are the Riksbank's monetary and foreign exchange policy counterparties, while the remaining 57 per cent are other participants on these markets, investors as well as issuers and market makers. The response frequency was 56 per cent for the survey as a whole.

they use electronic platforms in their trading in the Swedish krona, and around half of these state that they always use such platforms. Among the participants who are active on the Swedish fixed-income market the corresponding figure is much lower, and one in three participants never use them when trading with Swedish government bonds. The majority of foreign exchange market participants state that they rarely or never use algorithms, although the usage has increased over the past year.

The Swedish housing and property market is the risk factor most often mentioned

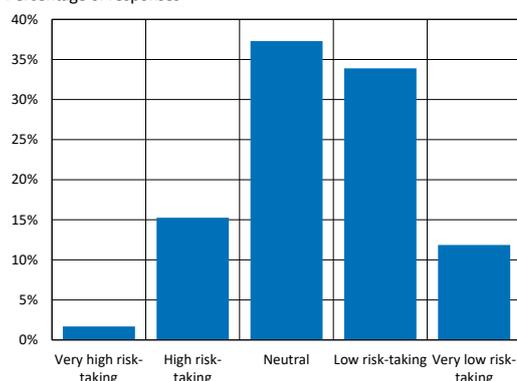
Participants were asked in the survey to describe which external events risk having a negative effect on the Swedish financial system in the coming six months. The risk that participants are most concerned about is a severe decline in prices of Swedish housing and property. For example, the participants emphasise that a deterioration in the housing and property market might scare off foreign investors from the Swedish fixed-income market. Several participants also mention liquidity risks,³ for instance related to the shrinking of central banks' balance sheets, potential credit and counterparty risks,⁴ and a potential bank crisis that could spill over to the rest of the Swedish financial system. One in five participants mention liquidity risks and an equal share mention credit and counterparty risks. Risks linked to the failure of a Swedish bank are mentioned by one in ten participants. Separate risk factors mentioned include increasing regulations (not specified by the respondents) and market risks⁵ arising from Brexit or the Italian sovereign debt.

A majority of the participants consider themselves as taking low or neutral risks

Most respondents say that they take low or neutral (that is, neither high nor low) risks on the market in general, and only a few consider their risk taking as high or very high regarding their positioning (see Diagram 1). Among those who mention a housing and property crisis as the primary risk factor, only one in eight take large risks and none take very large risks. The participants were also asked to assess whether they have changed their risk taking in the past six months. A clear majority of the respondents say that they have reduced their risk taking or take the same level of risk as before, which is illustrated in Diagram 2. They mention, for instance, lower volatility and poor liquidity as reasons for reducing their risk taking. Furthermore, the participants were asked how well prepared they consider themselves in dealing with a number of risk factors: *credit and counterparty risks*, *market risks*, *legal risks*, *liquidity risks* and *cyber risks*. Most respondents consider that they are generally well prepared for these types of risk, but one in six say they are poorly prepared for cyber risks.

Diagram 1. In terms of positioning, how do you assess your risk-taking in the market today?

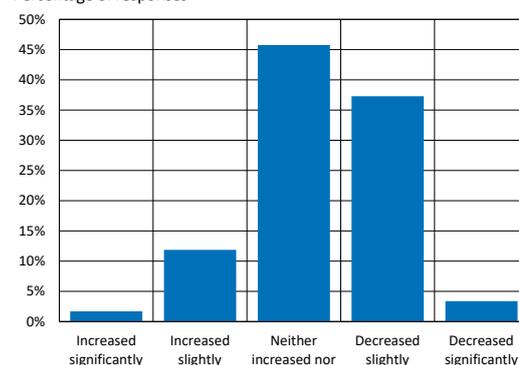
Percentage of responses



Note. 59 responses in total.

Diagram 2. How do you consider that your risk-taking has changed over the past six months?

Percentage of responses



Note. 59 responses in total.

³ Market liquidity refers here to the ability to rapidly buy or sell large volumes of a financial instrument at a low transaction cost and with limited market price impact. See also *Market liquidity on the Swedish bond market and its importance for financial stability*. Article in the Financial Stability Report 2016:1. Sveriges Riksbank.

⁴ Credit and counterparty risk refers here to the risk of a loss arising because a counterparty does not meet its commitments and the risk that a loss of value will arise due to poorer credit quality.

⁵ Market risk here refers to the risk of a decline in the value of financial instruments as a result of fluctuations in market prices.

The market for the Swedish krona is perceived to be functioning smoothly by most participants

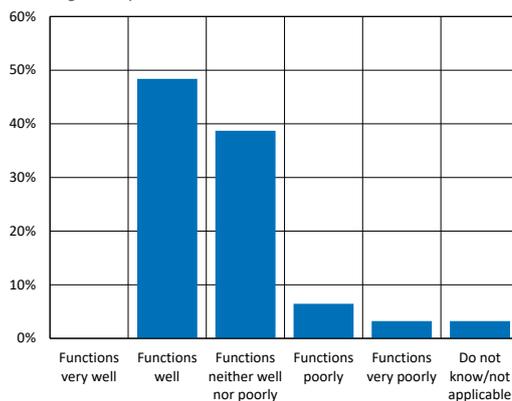
Almost half of the respondents consider the market for the Swedish krona to be functioning well (see Diagram 3). Two in five perceive the market as functioning neither well nor poorly. A forthcoming normalisation of the Riksbank's expansionary monetary policy, with quantitative tightening and interest rate increases, is considered to enable the market functioning to improve over the coming six months. A few responses also mention that regulations, such as the resolution fee,⁶ might have a negative effect on the market in the future.

The participants are asked in the survey to assess market liquidity for the spot and forward markets for the Swedish krona in relation to the other G10 currencies.⁷ Around half of the respondents said they assess market liquidity on both the spot and forward markets in Swedish krona to be good or very good. One in six respondents considers market liquidity on the spot market to be poor or very poor, while the corresponding figure for the forward market is one in five respondents. There is no clear link between the type of participant⁸ and their impression of market liquidity. When the participants were asked to assess the change in market liquidity on the krona market (both for spot and forward markets) over the past six months, most considered that market liquidity remains unchanged or has deteriorated slightly, which is illustrated in Diagram 4 and Diagram 5. The participants stated similar or the same reasons for their assessments of current and future market liquidity and for the functioning of the market, which indicates that liquidity on the market is perceived to be one of the most important factors for how well the market is functioning. Respondents were given the opportunity to justify their responses, and several did so by referring to liquidity in the market. However, opinion was divided among those justifying their responses, with regard to whether liquidity is high or low.

Nine out of ten responded that the Riksbank's monetary policy, in particular the low interest rates, had been the most important driving force behind the development of the krona in the past six months. Interest rate increases in the United States, resulting in real interest rate differentials, are also mentioned as a driving force, as is the Swedish parliamentary election.

Diagram 3. In general, what is your assessment of the functioning of the market for SEK today?

Percentage of responses



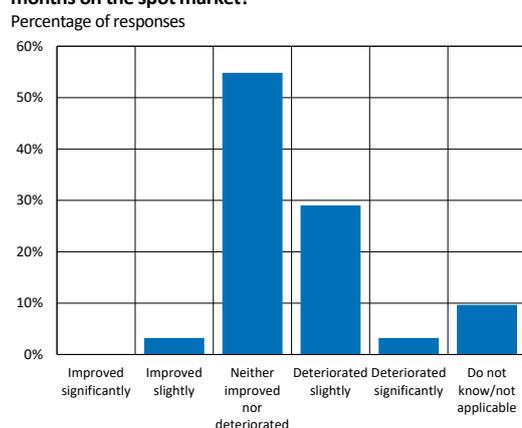
Note. 31 responses in total.

⁶ This fee is paid annually by credit institutions and securities companies and is aimed at building up the resolution fund that forms part of the new crisis management directive introduced into Swedish legislation in 2016. The size of the annual resolution fee is primarily based on the individual institutions' balance sheets at the end of the year.

⁷ The G10 currencies and the ten most traded currencies in the world: *US dollar, euro, pound sterling, Japanese yen, Australian dollar, New Zealand dollar, Canadian dollar, Swiss franc, Norwegian krone* and *Swedish krona*.

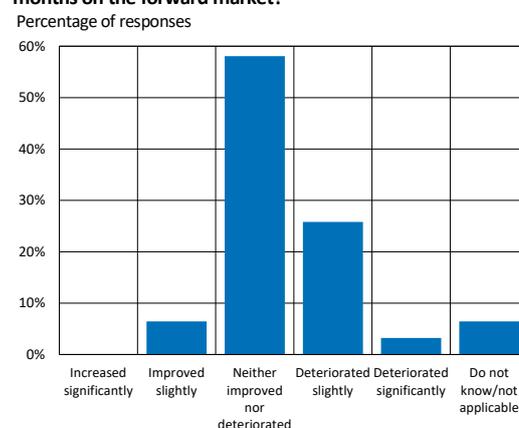
⁸ The respondents were asked to categorise their role in the market as either issuer/borrower, investor/lender or market maker/broker.

Diagram 4. What is your view on how market liquidity in the SEK (against G10 currencies) has changed over the past 6 months on the spot market?



Note. 31 responses in total.

Diagram 5. What is your view on how market liquidity in the SEK (against G10 currencies) has changed over the past 6 months on the forward market?



Note. 31 responses in total.

Opinion is divided on the functioning of the Swedish fixed-income market

The number of participants who consider the fixed-income market in general to be functioning well or very well is roughly the same as the number who think it is functioning poorly or very poorly (see Diagram 6). Three quarters of the latter mention limited or low liquidity as the main reason for their opinion of the functioning of the fixed-income market in general, and several mention the Riksbank's government bond purchases as one of the reasons for this. Several respondents say that the market for interest derivatives is functioning well, and this is stated as the main reason by those who have a positive perception of the functioning of the Swedish fixed-income market. Issuers respond to a greater extent that they perceive the market's general functionality to be good rather than other response alternatives, while investors to a greater extent respond that the market's general functioning is poor.

Market liquidity on the secondary market for treasury bills and government bonds is currently perceived to be low or very low by a majority of the respondents (see Diagram 7 and Diagram 8). Investors and market makers respond to a particularly large degree that they perceive market liquidity on these markets to be low or very low, while a large share of issuers state that they have no opinion. Market liquidity on the secondary market for covered bonds is perceived by one in two participants as satisfactory or high, while the corresponding figure for interest rate swaps⁹ is two out of five participants (see Diagram 9 and Diagram 10 in Appendix 1).

The participants are also asked to make an assessment of the change in market liquidity on the secondary market¹⁰ over the past six months, and to describe which driving forces they consider to have been the most important in this. Most consider that market liquidity in the secondary market for all types of Swedish assets is unchanged or has deteriorated. The Riksbank's monetary policy, and in particular the government bond purchases, are described as the most important driving force behind the change in market liquidity in the past six months. The respondents state that the Riksbank's government bond purchases have limited market liquidity, particularly on the government bond market. A

⁹ An interest-rate swap is a bilateral agreement to exchange a specific interest rate in return for another interest rate for a predetermined period according to specific conditions. In the survey the respondents are asked to assess functionality and market liquidity in interest rate swaps (SEK/SEK).

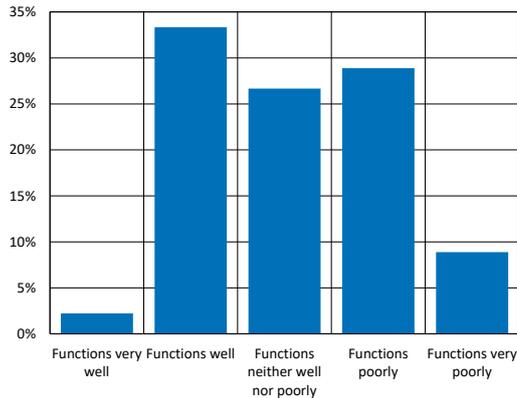
¹⁰ The secondary market for *treasury bills, government bonds, covered bonds, corporate bonds, interest rate swaps (SEK/SEK), repos with government securities, repos with covered bonds and FRA contracts*.

couple of the respondents who think that the Riksbank's monetary policy has contributed to lower liquidity on the fixed-income market state that the market is functioning relatively well given the unconventional monetary policy.

It is generally thought that a normalisation of the Riksbank's expansionary monetary policy could improve market functioning in the coming six months. A severe deterioration in the property market is thought to potentially have a negative effect on the functioning of the market for covered bonds in the coming six months, and a couple of respondents mention the risk of Brexit affecting the clearing of a large percentage of Swedish interest derivatives, which in turn will lead to a deterioration in the functioning of the markets concerned.

Diagram 6. In general, what is your assessment of the functioning of the Swedish fixed-income market today?

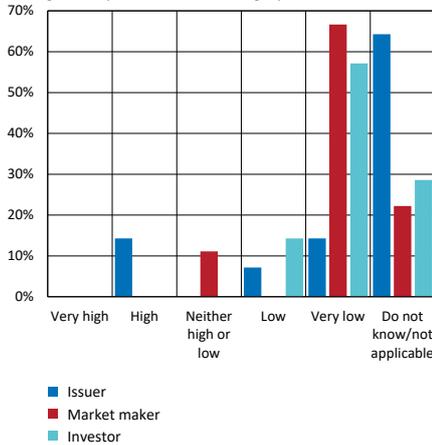
Percentage of responses



Note. 45 responses in total.

Diagram 7. What is your assessment of market liquidity on the secondary market for treasury bills at present?

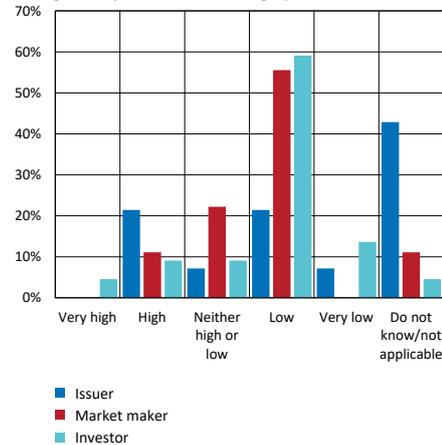
Percentage of responses for each category



Note. 44 responses in total, of which 14 issuers, 9 market makers, 21 investors.

Diagram 8. What is your assessment of market liquidity on the secondary market for government bonds at present?

Percentage of responses for each category



Note. 45 responses in total, of which 14 issuers, 9 market makers, 22 investors.

Electronic trading platforms and algorithms often used by participants in the market for the Swedish krona

The extent to which participants use electronic aids in trade differs substantially between the respondents active in the market for the Swedish krona and those active in the fixed-income market. Almost all of the respondents who are active on the market for the Swedish krona

state that they use electronic platforms¹¹ in their trading with the Swedish krona, and around half of these state that they always use such platforms (see Diagram 11 in Appendix 1). One in five state that they often use algorithms¹² in their trading with the Swedish krona, while two in five respondents state that they never use them (see Diagram 12 in Appendix 1). One fifth of respondents state that they have increased their use of electronic platforms over the past six months, and one in six state that they have increased their use of algorithms. The responses do not differ substantially between the different types of participants.

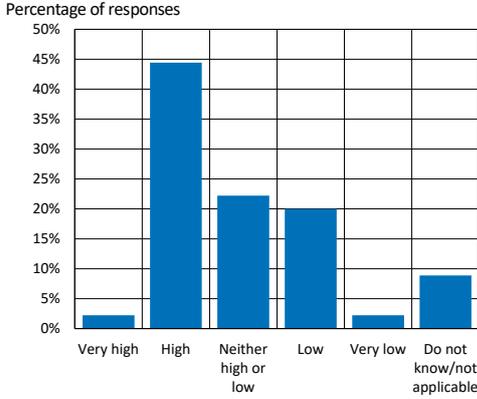
For the participants active on the Swedish fixed-income market, the corresponding figures are much lower (see Diagram 13 and Diagram 14 in Appendix 1). Electronic platforms are used always or often by two in five respondents when trading with Swedish government bonds, while one third state that they never use them. Two thirds state that they never use algorithms in their trading with Swedish government bonds. More than half of those responding that they never or rarely use electronic platforms are issuers, while the responses do not differ notably between different types of participant with regard to the use of algorithms. One in three participants state that they have increased their use of electronic platforms in the past six months with regard to trading in Swedish government bonds. Only one participant states that they have increased their use of algorithms.

¹¹ Electronic trading platforms are computerised dealing rooms that mediate contact between the purchaser and the seller, and provide information on current prices for various currency pairs. See also *Algorithmic trading in the foreign exchange market*. Article in Economic Review 2013:1. Sveriges Riksbank.

¹² Algorithms are mathematical models and formulas that create specific sets of rules in foreign exchange trading whereby orders can be placed and transactions executed. See also *Algorithmic trading in the foreign exchange market*. Article in Economic Review 2013:1. Sveriges Riksbank.

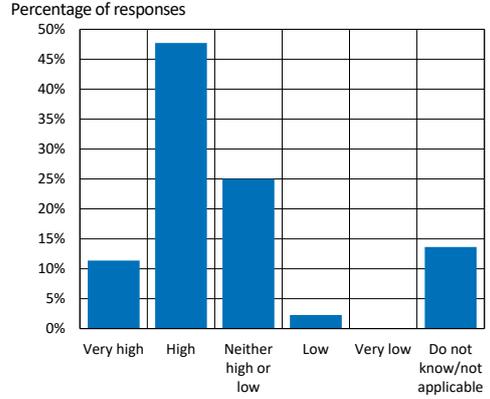
APPENDIX 1

Diagram 9. What is your assessment of market liquidity on the secondary market for covered bonds at present?



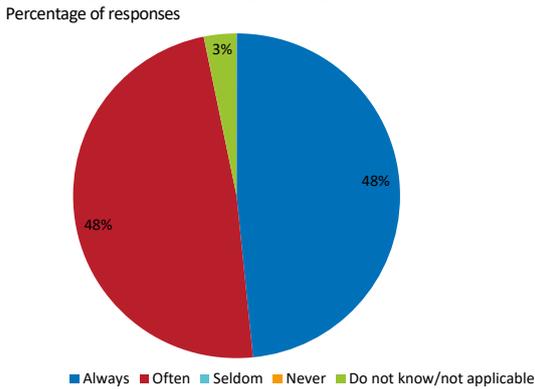
Note. 45 responses in total.

Diagram 10. What is your assessment of market liquidity on the secondary market for interest rate swaps (SEK/SEK) at present?



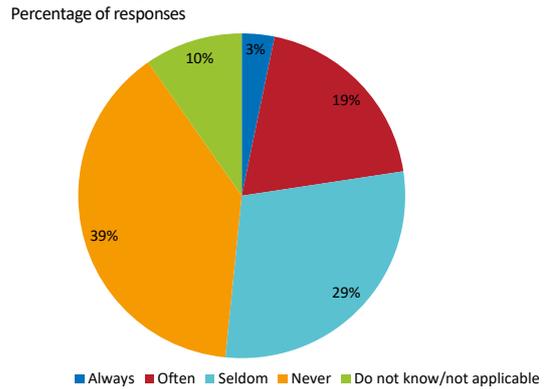
Note. 44 responses in total.

Diagram 11. To what extent do you use electronic platforms in your foreign exchange trading with regard to SEK?



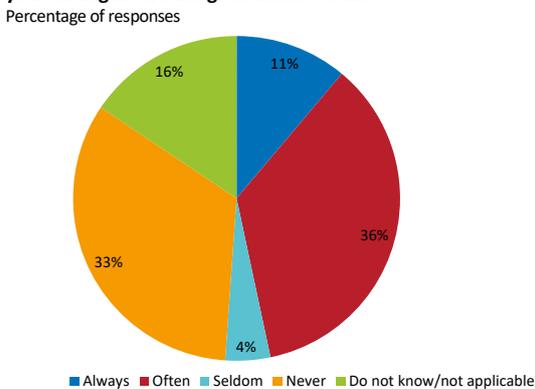
Note. 31 responses in total.

Diagram 12. To what extent do you use algorithms in your foreign exchange trading with regard to SEK?



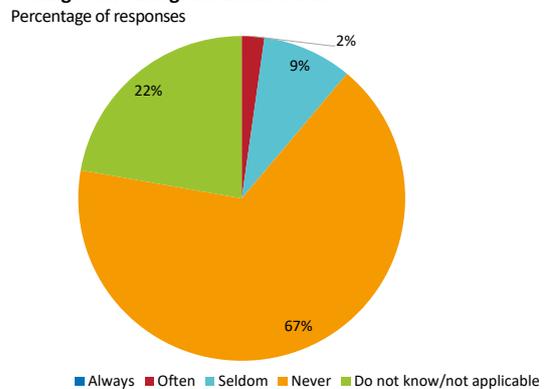
Note. 31 responses in total.

Diagram 13. To what extent do you use electronic platforms in your trading in Swedish government bonds?



Note. 45 responses in total.

Diagram 14. To what extent do you use algorithms in your trading in Swedish government bonds?



Note. 45 responses in total.



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