



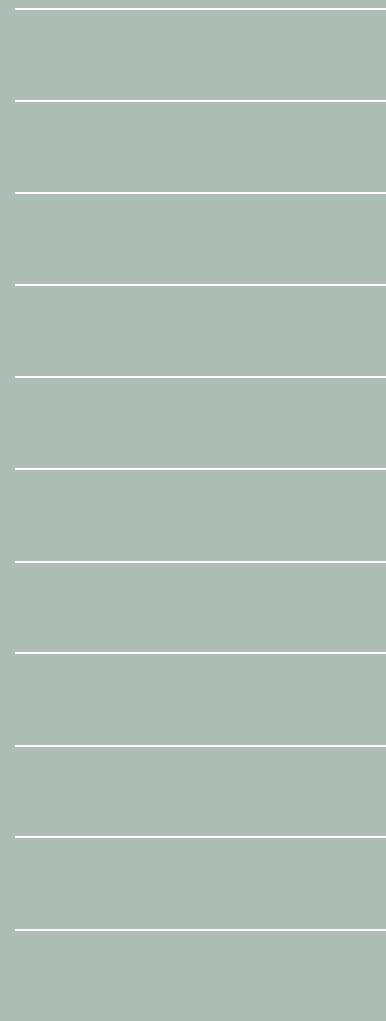
**LIETUVOS BANKAS**  
EURO SISTEMA

# REVIEW

OF THE SURVEY OF RISKS TO  
LITHUANIA'S FINANCIAL SYSTEM

2018

2



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## AIMS, METHODS AND PRINCIPLES OF THE SURVEY

*In order to assess the views of Lithuania's financial institutions towards potential challenges to sustainable development of the financial system, the Bank of Lithuania conducts a Survey of Risks to Lithuania's Financial System. The survey is conducted on a biannual basis (in May and November). Banks, insurance undertakings, leasing companies, investment management companies and other financial institutions assess the sources of major risks to Lithuania's financial system, the probability of adverse events and their potential impact on the domestic financial system over the upcoming 6 months.*

*24 respondents, of which 6 banks operating in Lithuania, 7 insurance undertakings and 11 other financial institutions (leasing companies, financial brokerage firms, management companies, credit unions and consumer credit companies), took part in this survey. Questions were presented to the executives of the financial institutions surveyed. In summarising the opinions and calculating the proportion of financial institutions that have chosen a particular answer, the responses of all institutions were given the same weight, regardless of their market share. Participation in the survey is voluntary, respondents may choose which questions to answer.*

## REVIEW OF THE SURVEY RESULTS

**The three key risks to Lithuania's financial system have remained unchanged over the past two years.** A snapback in risk premia, cyberattacks and unsustainable real estate market developments continue to pose greatest concern for financial institutions. In the second half of 2018, a snapback in risk premia in global financial markets became the key threat to Lithuania's financial system (see Tables 1 and 2). According to the surveyed, the probability of a snapback in risk premia as well as its potential impact on the financial system is the highest, although the possibility of mitigating this risk is quite high.

**In the period under review, the importance of cyberattacks to Lithuania's financial institutions has slightly diminished** (see Table 2). As before, banks remained prudent when assessing this risk, while insurance undertakings and other financial institutions were less cautious (particularly in terms of the probability of its emergence). The survey results suggest that over the recent half-year 3 out of 24 financial institutions were subjected to cyberattacks, but none of them incurred any losses (see Chart 2).

**Over the recent two and a half years, unsustainable developments in real estate prices or imbalances in the real estate market have also been one of the key risks to Lithuania's financial system.** According to the surveyed, the importance of this risk remained unchanged over the last half-year (see Table 2), while the possibility of mitigating it was seen as quite limited. Other financial institutions' assessment of the potential negative effects of this risk was higher than that of banks and insurance undertakings. The possibility of mitigating this risk was seen as the lowest compared to other risks.

**According to the respondents, the importance of risks that are likely to emerge within the Lithuanian market declined, while the significance of external risks increased.** Among internal risks, unsustainable developments in real estate and credit markets as well as the potential deterioration in corporate and household financial health were the source of greatest concern to financial market participants in the second half of 2018. The majority of the surveyed financial market participants named deterioration in corporate financial health as the main risk emerging within the internal market (see Chart 3). When comparing external risks, in the second half of 2018, financial market participants attached greater importance to risks related to the possible negative impact of weakening European sovereign debt sustainability on Lithuania's financial system. Risks related to the deceleration in Lithuania's exports due to the slow-down in main trading partners and imbalances in Scandinavian countries remained important as well.

**According to the surveyed, the probability of a high-negative-impact event in the financial system has increased.** For the second consecutive half-year the surveyed assessed the probability of such an event as elevated (see Chart 4). In general, there were no respondents in the second half of 2018 who would consider the likelihood of a high-negative-impact event in the financial system as diminished. At the same time, the share of respondents who viewed this risk as unchanged contracted, while the share of those who assessed the probability of such an event as increased almost doubled. The surveyed financial institutions saw the United Kingdom's withdrawal from the European Union, adjustment of imbalances in Scandinavian countries and changes in interest rates underpinned by the possible tightening of monetary policy as the most likely high-impact events.

**Over the half-year, the risk appetite of financial institutions followed a moderate upward trend.** Half of the surveyed financial institutions stated that they assumed medium risk, while 8.3% – rather high than low risk (see Chart 5). Compared to the results of the survey carried out half a year ago, the share of financial institutions assuming low and high (or rather low and rather high) risk declined; however, the share of those assuming medium risk grew. Banks, as well as insurance undertakings, assessed their own risk appetite more moderately than that of other market participants (see Chart 6).

## KEY CHARTS AND TABLES

**Table 1. A snapback in risk premia in global financial markets is the main and most likely risk to the financial system**

Assessment of risks to Lithuania's financial system

Risks	Importance	Probability	Potential impact	Possibilities of mitigating
I. Snapback in risk premia in global financial markets	3.0	3.0	3.0	2.3
II. Cyberattacks	2.8	2.7	2.9	3.0
III. Unsustainable developments in real estate prices or imbalances in the real estate market	2.7	2.4	3.0	3.3
IV. Weakening European sovereign debt sustainability and the potential contagion effect on Lithuania's financial system	2.7	2.4	3.0	1.9
V. Deceleration in Lithuania's exports due to the slowdown in main trading partners	2.5	2.2	2.8	2.0
VI. Imbalances in Scandinavian countries and potential contagion effects on Lithuania's financial system	2.5	2.2	2.8	2.0
VII. Problems in the European banking sector and potential contagion effects on Lithuania's financial system	2.4	2.1	2.7	2.0
VIII. Unsustainable credit dynamics or imbalances in the credit market	2.4	2.0	2.8	3.2
IX. Deterioration in corporate financial health	2.3	2.0	2.7	2.6
X. Geopolitical tensions and their implications for Lithuania's financial system	2.2	2.5	2.6	1.7
XI. Deterioration in household financial health	2.2	1.8	2.6	2.6
XII. Drop in profitability of Lithuania's financial institutions during a prolonged period of low interest rates	2.1	2.0	2.2	2.5

Notes: Risk importance is calculated as a geometric mean of estimates for its probability and potential impact. **Probability:** 1 – low; 2 – lower than medium; 3 – medium; 4 – higher than medium; 5 – high. **Potential impact:** 1 – low; 2 – lower than medium; 3 – medium; 4 – higher than medium; 5 – high. **Possibilities of mitigating risk:** 1 – high; 2 – higher than medium; 3 – medium; 4 – lower than medium; 5 – low. Risks were classified according to importance.

**Table 2. After a year and a half, cyberattack risk gave up its leading position to the risk of a snapback in risk premia**

Importance dynamics of risks to the financial system

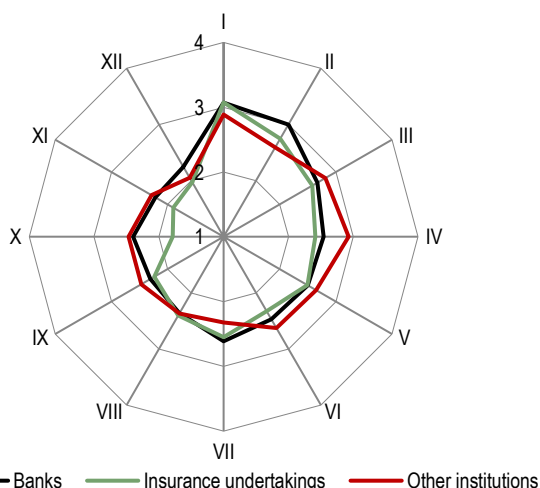
Risks	H1 2016	H2 2016	H1 2017	H2 2017	H1 2018	H2 2018
I.	2.6	2.8	2.8	2.7	2.7	3.0
II.	2.8	2.6	3.0	3.1	3.1	2.8
III.	2.5	2.7	2.8	2.9	2.7	2.7
IV.	2.5	2.6	2.4	2.3	2.3	2.7
V.	2.7	2.6	2.3	2.5	2.5	2.5
VI.	2.4	2.7	2.5	2.8	2.7	2.5
VII.		2.5	2.4	2.3	2.2	2.4
VIII.	2.2	2.2	2.1	2.3	2.3	2.4
IX.	2.3	2.6	2.2	2.6	2.4	2.3
X.	3.1	2.7	2.3	2.5	2.3	2.2
XI.	2.2	2.4	2.2	2.3	2.3	2.2
XII.	3.4	2.8	2.6	2.5	2.3	2.1

Notes: Risk importance is calculated as a geometric mean of estimates for its probability and potential impact. Risks are enumerated in line with the risk sources in Table 1. The level of risk importance is marked in the following way:

■ Low importance    
 ■ Medium importance    
 ■ High importance

**Chart 1. All financial market participants believed that a snapback in risk premia in global financial markets is the key risk**

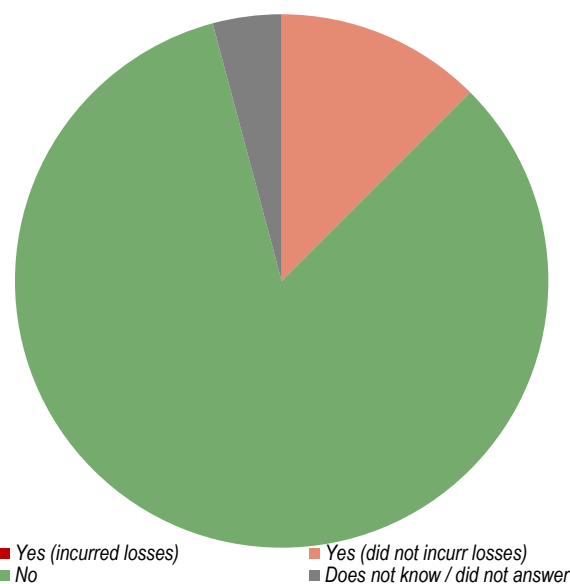
Importance of risks by financial institution sector



Note: Risks are enumerated in line with the risk sources in Table 1; risk importance is calculated as a geometric mean of estimates for its probability and potential impact.

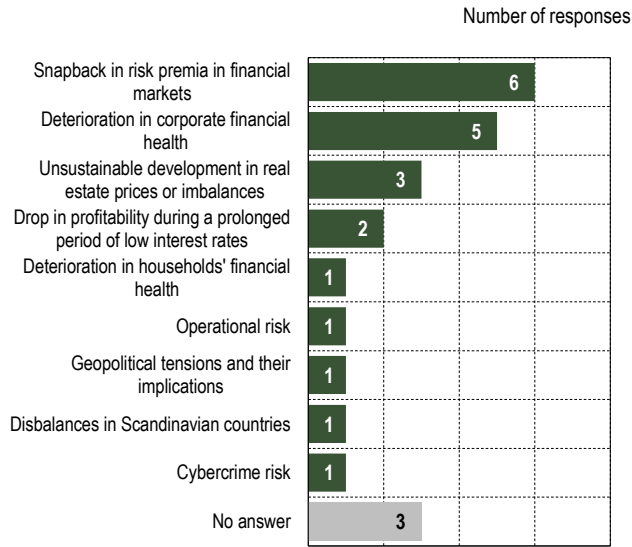
**Chart 2. In H2 2018, three financial market institutions were subjected to cyberattacks, but none of them resulted in losses**

Financial institutions that were subjected to cyberattacks



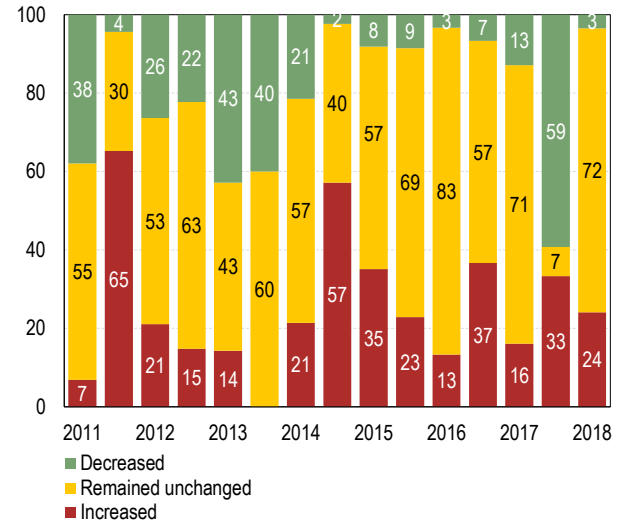
**Chart 3. The majority of institutions indicated a snapback in risk premia in global financial markets as the main risk to their activities**

Assessment of key risk



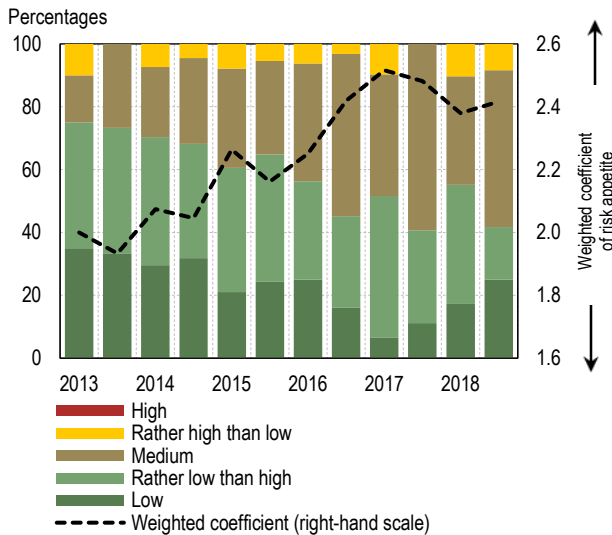
**Chart 4. The share of institutions that assessed the probability of a high-impact event as heightened increased**

Change in the probability of a high-impact event in Lithuania's financial system in the near future over the past 6 months



**Chart 5. The risk appetite of half of financial institutions is medium**

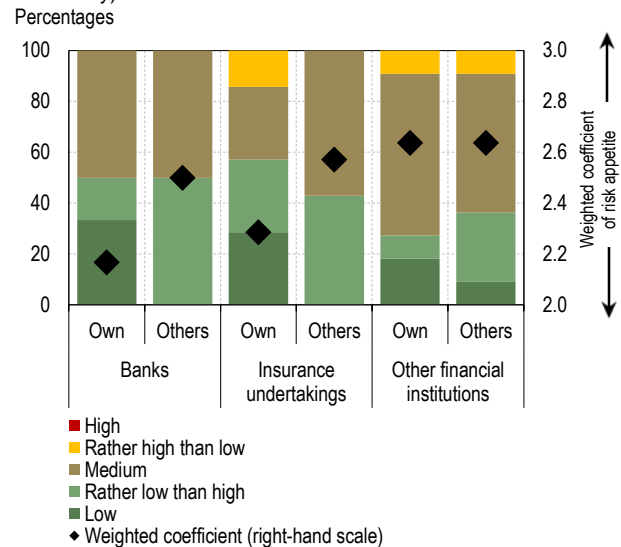
Level of own risk appetite (during the survey)



Note: The weighted coefficient is calculated by giving numerical values to risk appetite levels from 1 to 5 (where 1 is low and 5 – high risk appetite) and adding weights to them against the share of each selected answer.

**Chart 6. Most of the respondents assessed their risk appetite as lower than others in the same**

Level of own and other financial institutions' risk appetite (during the survey)



Note: The weighted coefficient is calculated by giving numerical values to risk appetite levels from 1 to 5 (where 1 is low and 5 – high risk appetite) and adding weights to them against the share of each selected answer.