

The change in Business Risk in Banking: Implications for Nordea

A Scenario Analysis for the Board of Directors

By Halvard Bø, Even Riber Haugland, Emil Zachariassen Hurv, Brede Espelid and Markus Langfeldt Nicolaisen

Introduction to Business Risk



- BUSINESS RISKS TURNED STRATEGIC



- SHIFT FROM TRADITIONAL BANKING RISKS TO CONSUMER SHIFT RISKS



- IMPORTANCE OF ADDRESSING THESE RISKS FOR NORDEA'S FUTURE

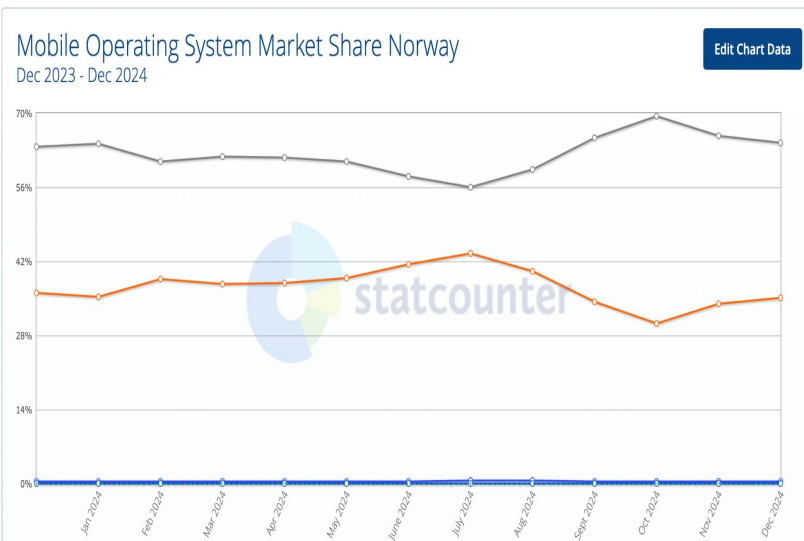
Scenario: Apple's Financial Super App



- Hypothetical scenario: Apple launches a comprehensive financial services app

- Features: Payments, investments, loans, and banking services

- Leverages Apple's brand, user base, and technology



Threat to Nordea's Business Model

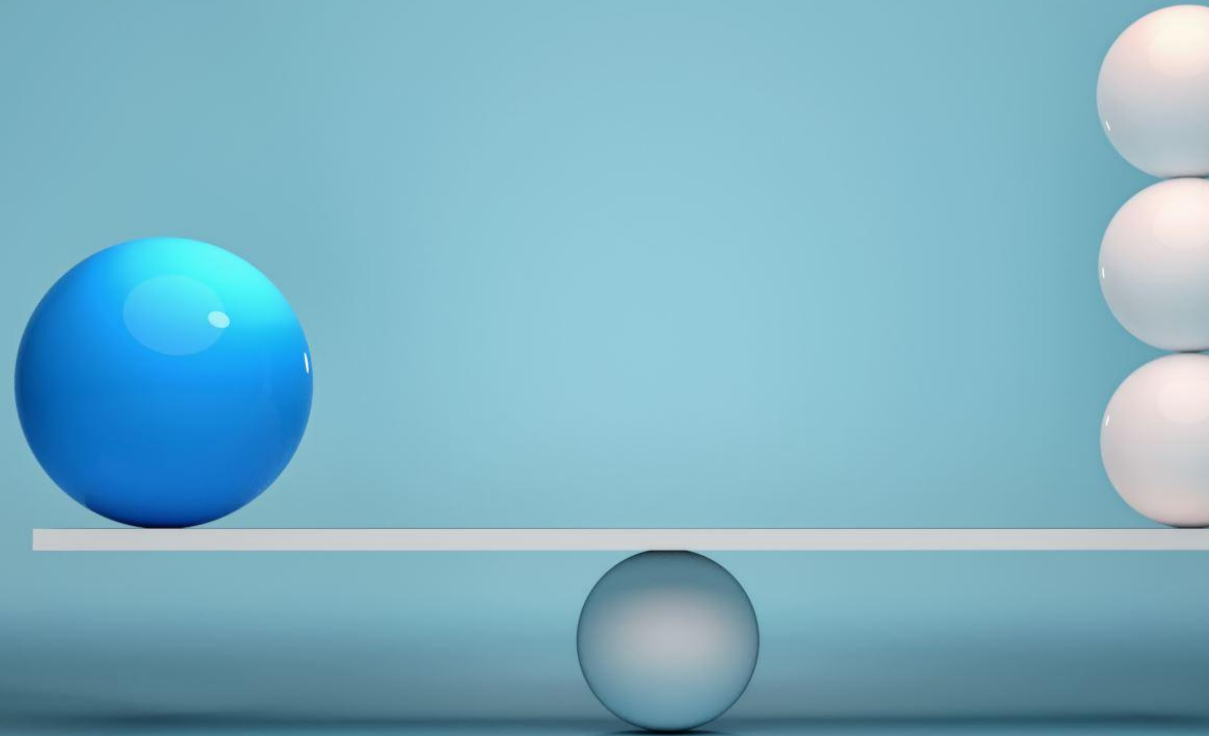
75% of Millennials would switch financial institutions for a better mobile banking experience. They expect clean, easy-to-navigate interfaces requiring minimal effort to accomplish tasks, quick transactions and interactions, minimal loading times, and consistency across devices.

ADVANTAGE. (2024, June 4). Technology trends to attract younger generations. JMFA.
https://advantage-fi.com/technology_trends_attract_new_generations/

-
- Potential loss of market share in Nordic countries
-
- Erosion of customer base, especially younger demographics
-
- Challenge to Nordea's digital banking initiatives

Impact on Nordea's Efficiency Ratios

- Potential increase in cost-to-income ratio
- Comparison: Nordea's current ratio vs. Apple's projected ratio
- Need for significant cost-cutting or revenue growth to remain competitive



Effect on Credit Risk

- Potential loss of prime customers to Apple's offering

- 
- Increase in non-performing loans ratio

- 
- Impact on Nordea's credit risk models and provisioning



Liquidity Risk Considerations

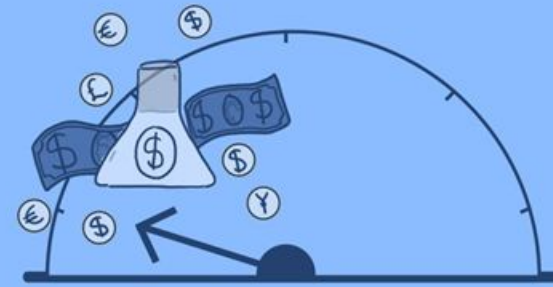
- Possible outflow of deposits to Apple's platform

- Stress on Nordea's liquidity coverage ratio (LCR)

- Need for more expensive funding sources

Effecting the Liquidity Coverage Ratio (LCR)

- I.Reduced High-Quality Liquid Assets (HQLA):
 - Customer deposits, especially retail deposits, support stable, low-cost funding.
 - Outflows require banks to liquidate assets or reduce HQLA buffers to meet short-term obligations.
 - Required 50% for NOK and 100% for other currencies.
- II. Increased Net Cash Outflows:
 - A loss of deposits increases short-term cash outflows as the bank must replace them with more expensive, short-term wholesale funding or repay liabilities.
 - This raises the denominator in the LCR formula.
- III. Stress on LCR Compliance:
 - A lower HQLA numerator combined with higher cash outflows results in a reduced LCR, potentially dipping below the regulatory 100% threshold.



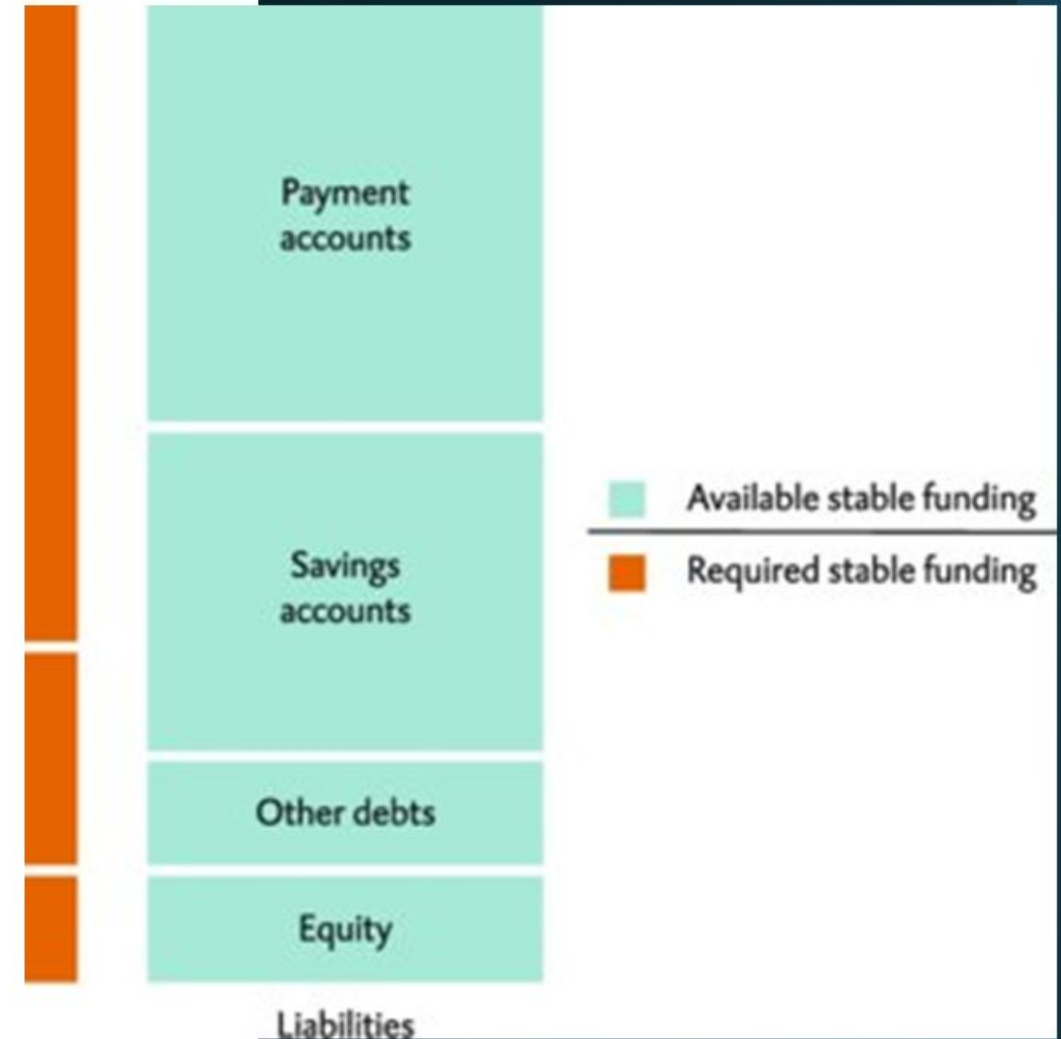
Liquidity Coverage Ratio (LCR)

[li- 'kwi-də-tē 'kəv-rij 'rā-shē-,ō]

The minimum amount of highly liquid assets that financial institutions are required to hold by international regulations.

Effecting the net stable funding ratio (NSFR)

- Reduced ASF from lost deposits (Retail deposits rated as safe)
- Potential reliance on less stable (often short-term) wholesale funding
- Overall pressure on the NSFR to dip below regulatory requirements (100%) (Finanstilsynet)
- **Ways to overcome:**
 - Attract or retain more stable retail deposits (e.g., higher deposit rates)
 - Issue longer-term debt or equity to boost stable funding
 - Adjust the asset mix by shedding less-liquid assets or investing in more liquid ones



Regulatory Capital Implications

- Potential decrease in return on equity

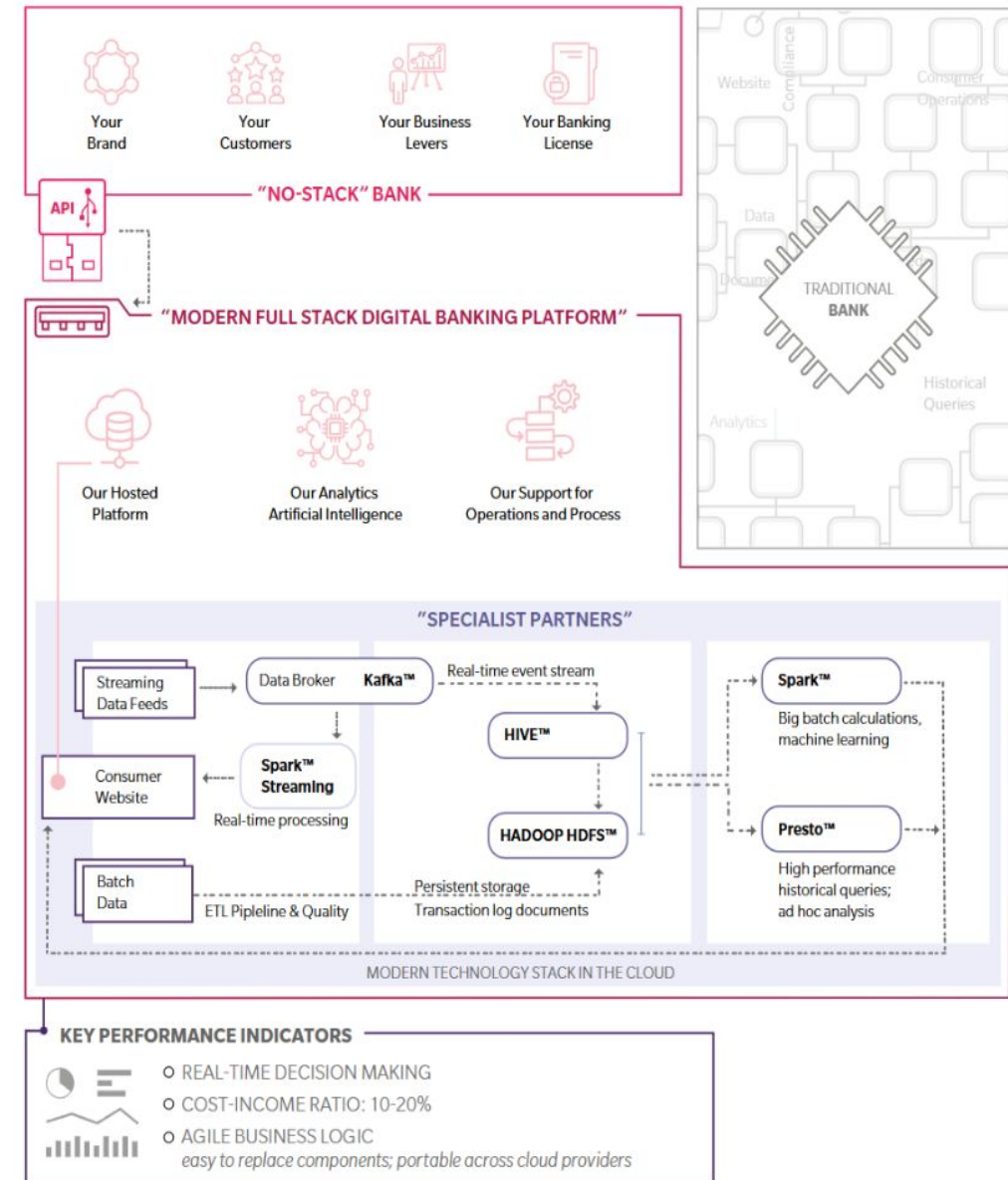
- Pressure on capital adequacy ratios

- Need for balance sheet optimization and capital raising

Strategic Responses

- Invest in advanced data analytics and AI for better services
- Explore potential partnerships with fintech companies
- Consider a "no-stack" banking model ?

EXHIBIT 1: NO-STACK BANKING



Source: Oliver Wyman analysis

Barrie Wilkinson is a London-based partner in Oliver Wyman's Digital practice.