Towards a European Banking Union:

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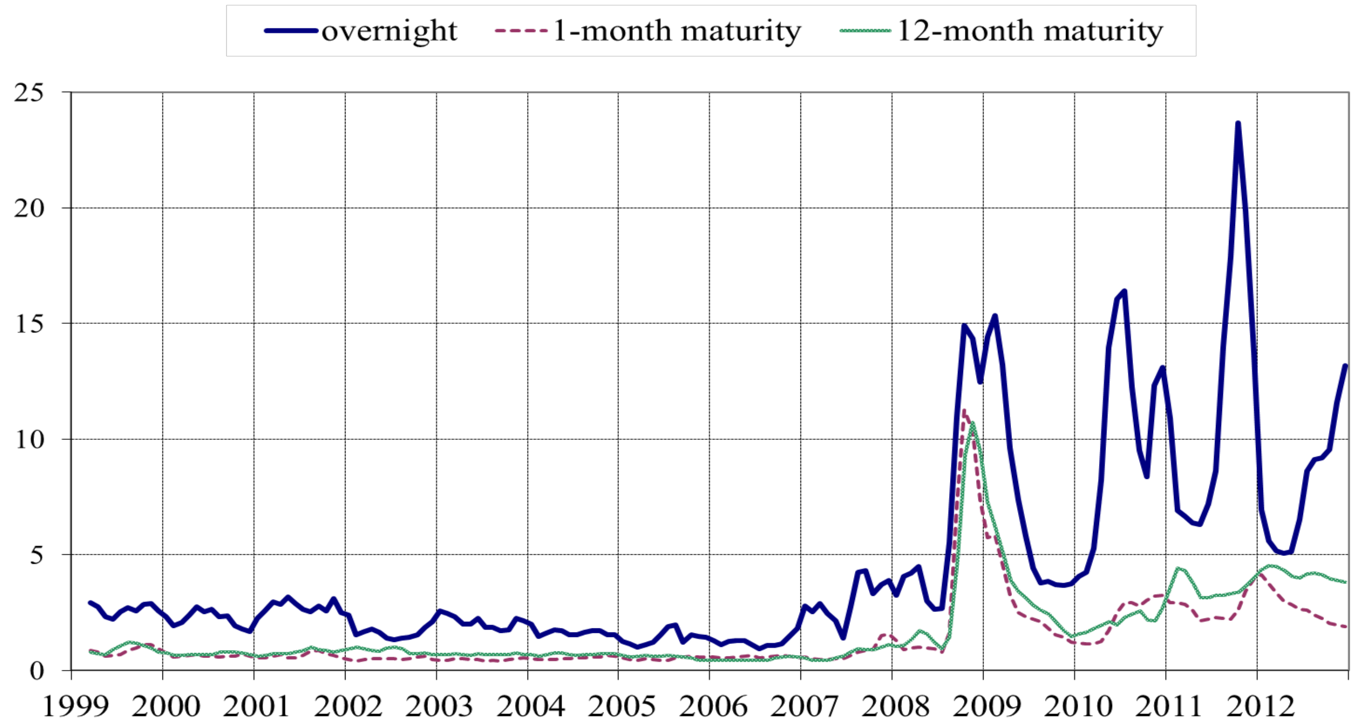
ABI Convention "BASILEA 3"

Roma, 27 June 2013

Money market fragmentation

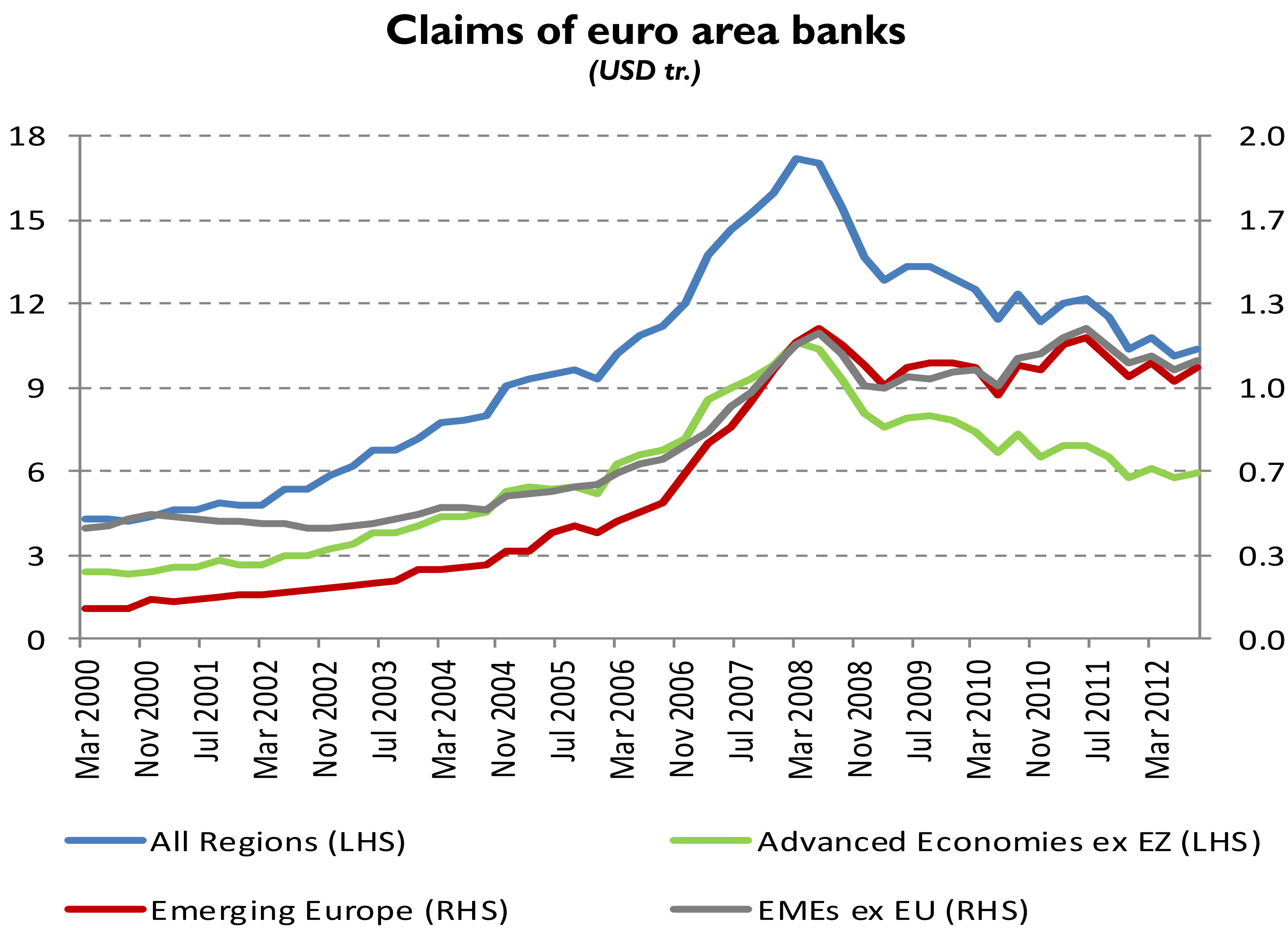
Cross-country standard deviation of average unsecured interbank lending rates across euro area countries (EONIA/EURIBOR)

(61-day moving average: basis points)



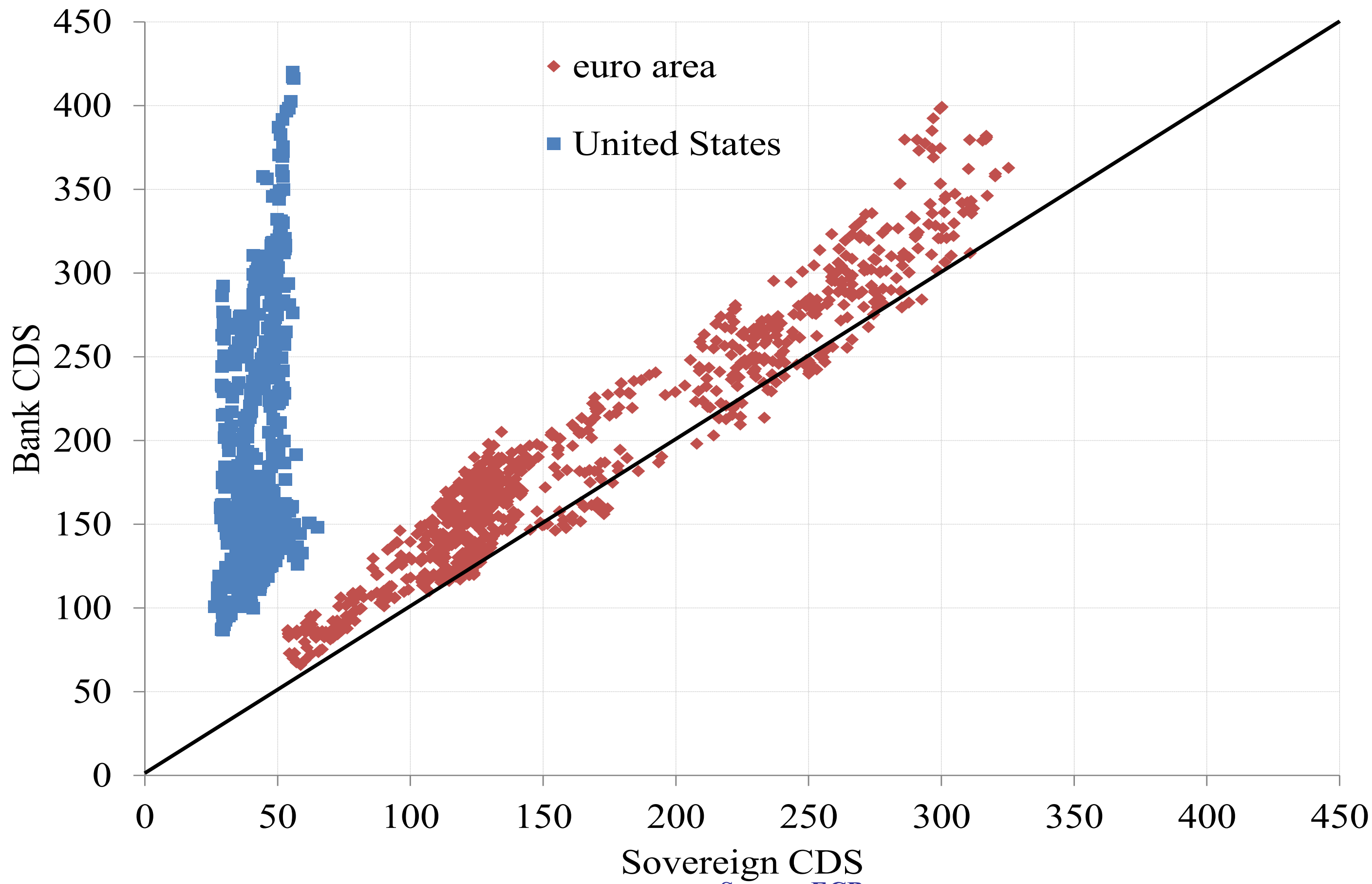
Source: EBF and ECB calculations.
Notes: All countries means here the following countries: AT, BE, DE, ES, FI, FR, GR, IE, IT, LU, NL, PT, "non-distressed countries" are in that sample AT, BE, DE, FI, FR, LU, NL.

International risk sharing



Fiscal-banking loop

Sovereign and bank CDS spreads: euro area and US
(2010 – July 2013; basis points)

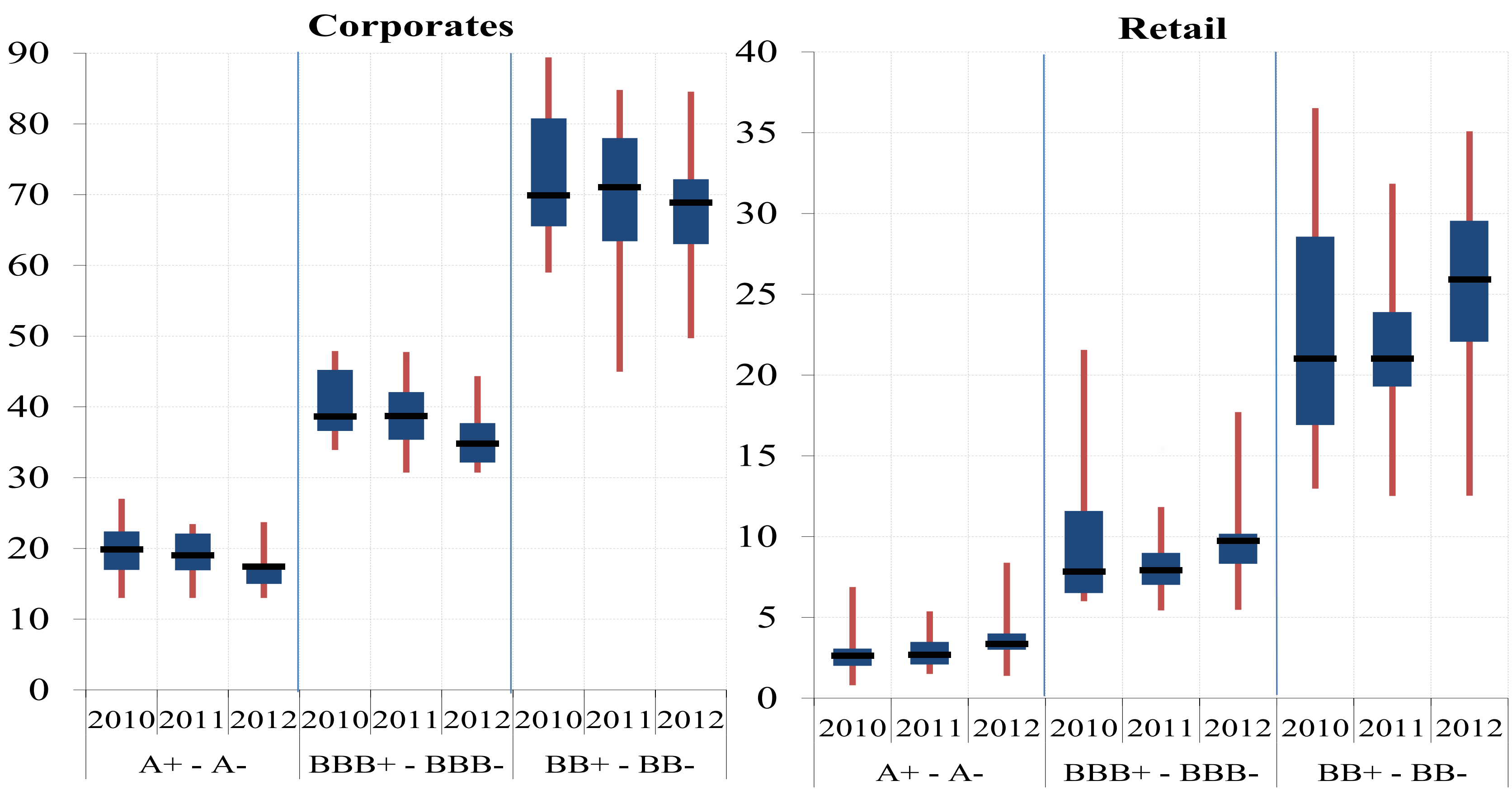


Source: Bloomberg.
Note: Average CDS spread for euro area and US LCBGs and countries where LCBGs are located.

Source: ECB.

Supervisory fragmentation

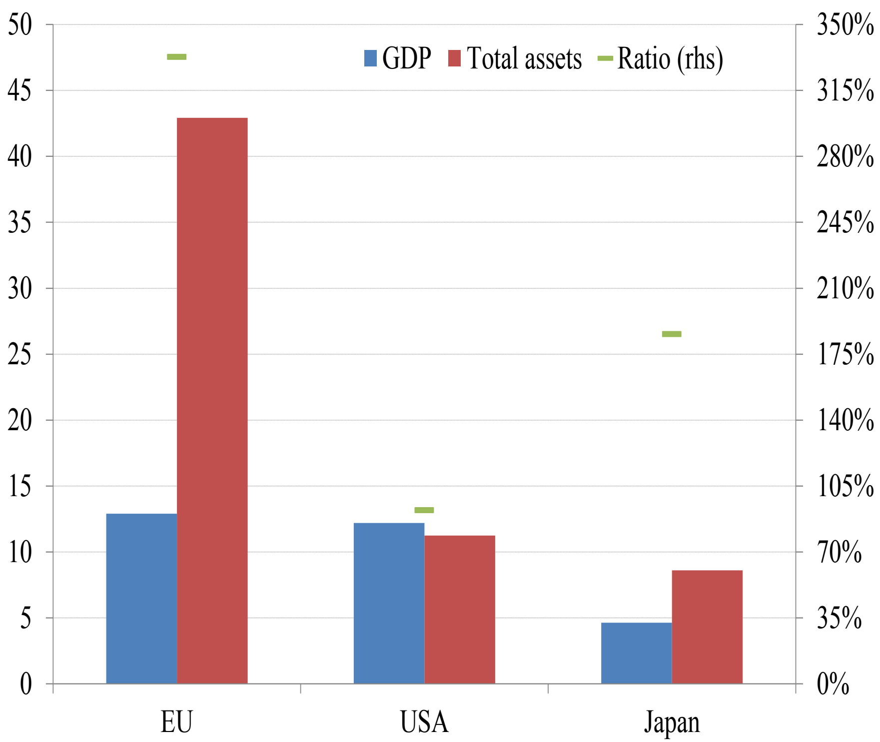
Euro area large and complex banking groups' risk weights for corporate and retail credit exposures
(percentages; maximum, minimum, interquartile distribution and median)



Sources: Individual institutions' Pillar 3 reports and ECB calculations.

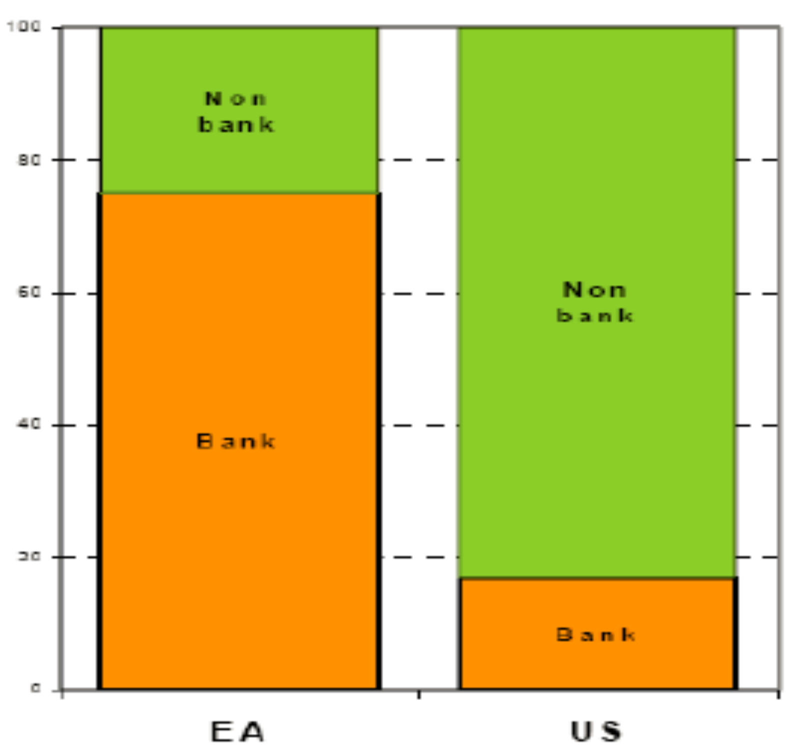
Overbanking

Total bank assets in the EU, Japan and the US
(2012, EUR trillion; percentage of GDP)



Source: ECB, FDIC and Bank of Japan.

Funding of non-financial corporations in the euro area and the United States
(2002 – Q1 2012; cumulated debt shares)



Source: Cour-Thimann and Winkl (2013)

Problems to be addressed

- **Adverse loop between banks, public finances, macro performance**
- **Financial fragmentation**
- **Fragmented and ineffective banking supervision, national bias**
- **Incoherent bank crisis management, no transparent burden sharing**

Banking Union: elements

Banking Union

1. Single Supervisory Mechanism (SSM)

2. Single Resolution Mechanism (SRM)

3. Harmonised Deposit Guarantee Schemes (DGS)

Common rules (EBA Single Rulebook)

Common supervisory practices (SSM Supervisory Manual)

Institutional scope

Significant credit institutions:

1) size: assets >30 bn; ratio assets/GDP exceeds 20% (but >5 bn)
2) importance for the economy of the EU or any MS
3) direct financial assistance from EFSF or ESM
4) 3 largest banks in each country
5) ECB decision

ECB supervision, with assistance of national authorities in the preparatory and implementing activities.

Less significant credit institutions

→ National supervision with ECB controls

Functional scope

- **All classic micro-prudential tools:**
  - Authorisation of banking activity, mergers and acquisitions
  - Prudential requirements (own funds, large exposure limits, liquidity, leverage and disclosure, internal governance and controls, "fit and proper", …
  - Supervisory reviews, stress tests, additional prudential requirements
- **Macro-prudential tools:**
  - National authorities remain competent for national macro-prudential requirements (e.g. loan-to-value ratio).
  - For instruments in EU law (CR Directive), e.g. countercyclical and SIFI buffers:
    - ✓ national authorities have to notify the intended decision to the ECB
    - ✓ ECB can apply more stringent macro-prudential measures

Remain at national level: supervision over non-banks; anti-fraud; consumer protection

Geographical scope

Single supervisor automatically includes all euro countries. Right to enter for the "outs"

- **Non-euro member states can join in "close cooperation" by:**
  - ✓ Adopting appropriate legislation and committing to abide to any guidelines or requests by the ECB
  - ✓ provide all information on its credit institutions that the ECB may request

Key institutional features

- **Supervision separate from monetary policy**
- **Independence**
- **Accountability**

Timing

- June 2012: Euro area Summit launches the Banking Union
- September 2012: Commission first draft
- December 2012: agreement in EU Council
- 1st half 2013: agreement with European Parliament

Next steps:

- Formal adoption of the SSM Regulation (this Summer)
- Secondary legislation, public consultations (end-year)
- Bank balance sheet assessment, "due diligence": June 2014
- Operational start: second half 2014

Main preparatory works

Mapping of Euro Area Banking System

Legal issues relating to Framework Regulation

"Supervisory Model" and "Supervisory Manual"

Supervisory Reporting Issues - reporting template

Comprehensive review

incl. a balance sheet assessment

Organogram and staff (about 800 people to start, plus support)

Crisis management framework

- **Why a crisis management framework:**
  - ✓ Prevents moral hazard
  - ✓ Limits systemic risks
- **EU "bail in" framework** (creditor hierarchy)
- **EU Bank resolution authority**
  - ✓ Orderly bank failures
  - ✓ Limits taxpayer exposure
- **EU resolution framework (ex-ante and ex-post funding, backstop)**
- **Depositor protection** (national, for now)

Conclusions

Opportunities:

- Break bank-fiscal interactions
- Break national supervisory silos, home biases
- Reduce fragmentation, improve single market
- Help stabilise the euro

Challenges:

- Proper crisis management framework
- Exploit synergy between national authorities (information, experience) and the ECB (level-playing field, European orientation)
- Transitional issues (avoid early mistakes, reputational loss)