EUROPEAN CENTRAL BANK
BANKING SUPERVISION

Five years of European banking supervision – things past and future

Speech by Andrea Enria, Chair of the Supervisory Board of the ECB, at the ECB Forum on Banking Supervision, in Frankfurt am Main, 6 November 2019

Just last week, on the very day that Brexit was supposed to take place, I left for London to give a speech on the banking union. But by the time I arrived, the Article 50 deadline had been postponed and Brexit had not happened after all. But it has still come much closer. And with Brexit approaching fast, I feel an even stronger attachment to the European project and an even greater sense of urgency to deliver the objectives of the banking union.

As in almost all discussions on the banking union these days, the focus in London was on the parts that are still missing and on the remaining challenges for our banks.

But we should not forget that, back in 2012, not everyone would have put money on the survival of the euro area. Thanks both to the ECB's commitment to preserve the euro and to the EU's agreement on setting up the banking union, the European project was able to survive and to emerge stronger from its worst crisis. The European institutions and Member States swung into action and decided to move closer together and deepen our Union. We celebrated the ECB's commitment during former President Mario Draghi's farewell last week; the banking union we celebrate today.

Because here we are; seven years later, and five years into our European banking union. Once again, in difficult times we have more proof that Europe does indeed work, that tackling problems together is far more effective than tackling them alone.

Celebrating five years of banking union

It is hard to believe that European banking supervision is only five years old. It all happened so very quickly – by European standards. But it is now well established and has become an irreversible feature of our institutional environment. And it was designed to very high standards, learning from the lessons of the crisis and building on the best supervisory practices from all national authorities. I don't think many people outside our profession can appreciate how difficult the challenge was. I have to pay tribute to my predecessor, Danièle Nouy, and to the previous Vice-Chair, Sabine Lautenschläger, for deftly steering the project during the demanding start-up phase.

The success of this endeavour also hinged on the strong commitment from national competent authorities. European banking supervision is a joint project; it is a system. Getting used to this requires time, of course. And it requires effort. We have launched many initiatives to bring together supervisors from across the euro area, always being mindful of the goal of forging relations, exchanging views, devising a common approach and forming a European team – not just at the level of the Supervisory Board but at all levels.

Future generations of banking supervisors will know only this new, European world. For them, it will be natural to work as a team across countries, to join forces with others and pursue a common goal. But looking back, even the first generation has adapted quickly and achieved a great deal.

European banking supervision greatly helped to speed up the post-crisis repair of banks' balance sheets. Banks now have much stronger capital and liquidity positions. The ECB's pressure on banks to reduce non-performing loans, or NPLs, has led to a significant clean-up: since 2014, the amount of NPLs has dropped almost by half, from €1 trillion to less than €600 billion. And we have ensured that future NPLs will be adequately provisioned.

We have engaged in a number of foundational projects that have allowed us to raise the bar in all areas of supervision. We are about to finalise our targeted review of internal models, for instance, which is a good example of the efforts to reset supervisory standards, also with a view to ensuring consistency and fairness across banks.

Things to come

Thanks to the progress achieved, European banking supervision is no longer a start-up and is now evolving into a more mature system.

But what does mature mean? For me, it means that we have agreed on a joint supervisory approach, assembled the tools we need and set up stable processes. In other words, we are approaching a steady state, and our actions now have to become more and more predictable. In practice, we can only be predictable when we are transparent. Because only then will banks, markets and the public be able to understand our principles and policies; only then will they be able to anticipate our actions. This is crucial. After all, banking supervision should be a source of stability, not of surprises.

We have seen a lack of restructuring in the European banking sector. We did not see consolidation reaching a level that would have absorbed the excess capacity that had built up before the crisis. So the system remains highly fragmented. Low interest rates put pressure on banks' margins, while most bank managers struggle to bring down costs. On average, European banks have not been able to ramp up their investments in new technologies and so lag behind their international competitors.

Some may place the blame on regulatory uncertainty. The markets seem to feel that European banks have to deal with steadily increasing capital requirements. I strongly dispute this idea and believe there is plenty of evidence in support of my disagreement. Still, we have to address this misconception and go the extra mile to provide clear targets and rules of engagement. Transparency, predictability and overall stability in supervisory requirements are essential to enable the structural adjustment that our banking sector needs. It seems, for instance, that our approach to bank mergers is not well understood by the markets, which appear to believe that we require more capital from merged entities. That is not necessarily the case. The capital we require from any entity, whether newly merged or not, is based on a medium-term assessment of the relevant business plan.

Now, what about banks? What does European banking supervision offer them? Well, it obviously offers more stability which, after the financial crisis, banks should particularly value. At the same time, it provides a level playing field. Banks no longer have to deal with different supervisory regimes when doing business across the euro area. And it's important to keep in mind that the standing of the supervisory authority is fundamental to the banking industry's reputation.

Banks nonetheless tend to complain about the burden that they have to shoulder under the new regulatory and supervisory framework. They see a clear link between tighter regulation, stricter supervision and lower profits. But there are other factors that explain why European banks' profits are low, many of which are related to how well, or how poorly, the banks are managed. So weakening regulation simply to give banks a helping hand would not solve the problem. My memories of the crisis are still very vivid, and I believe that the stability brought to us by Basel III comes at a fair price.

But in other areas I also hear some constructive criticism and see ways to slightly ease the banks' compliance burden. Reporting is a promising area in this regard. Two things stand out. First, it's not just European banking supervisors to whom banks have to report. They also have reporting obligations towards other authorities such as national supervisors, macroprudential authorities and central banks. More coordination among these authorities might ease the burden for banks. Second, we sometimes collect data ad hoc and on top of regular reporting. We need to do this in order to spot new risks or deepen our understanding of existing risks. But I acknowledge that we could improve our planning and our communication and exercise some discipline. We are working on this right now.

And this brings us to my final point: European banking supervision is not an island; it is just one part of the banking union. And now I'm going to repeat myself, because, as the US author Napoleon Hill said, "Any idea, plan, or purpose may be placed in the mind through repetition of thought".

So here it is: our success in making banks safer and sounder hinges on completing the banking union. We still need to erect the banking union's third pillar: European deposit insurance. Depositors must be sure that their money is well protected, no matter whether it is deposited with a bank in France, Italy, Greece or Germany. And only a European deposit insurance scheme can decouple this protection from the financial firepower of national schemes. At the same time, it would instantly justify the removal of the remaining obstacles that still hinder full integration of banking business across the entire banking union. During the crisis, countries started to ring-fence their national banking systems, leaving a burdensome legacy of segmentation in the European banking market. Our banks cannot yet consider the banking union as their domestic market, as a truly single jurisdiction. I am well aware that a political agreement could be difficult to achieve and take time to be practically implemented. But we cannot accept that the current segmentation of the market remains unaddressed. Hence, even without European deposit insurance, we have a duty to pursue the goal of a more integrated market with all the tools that we have at our disposal.

Single European supervision also requires single European regulation. We do have a single European rulebook for banks, but it is not as harmonised as it should be. From fit and proper rules for new bank managers to insolvency laws, we often have to deal with 19 different legal frameworks. This makes European banking supervision less effective and more costly. So, we do need to harmonise regulation further, and sooner rather than later.

Conclusion

Ladies and gentlemen, we can now look back at five years of European banking supervision. And we can look ahead to many more. I have presented a few aspects that will be relevant in the future. The list is not exhaustive, of course, and we are as much driven by events outside our control as anyone else.

But we do have a vision: a truly European banking market, in which safe and sound banks serve the economy. We have come closer over the past five years, but we are not there yet, and we cannot get there alone. It’s a task for all of us: banks, policymakers, national institutions, European institutions and many others.

As we step into the future, let us carry forward the victories of the past. By winning each other’s trust, we have become stronger, expanded our cooperation and flourished as a community. Now the time has come to nurture that trust and protect that community. In order to move forward and complete this European project, trust is all we have, and trust is all we need.

Thank you for your attention.

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