



Towards a banking union in a deeper EMU

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The financial crisis 2008/09

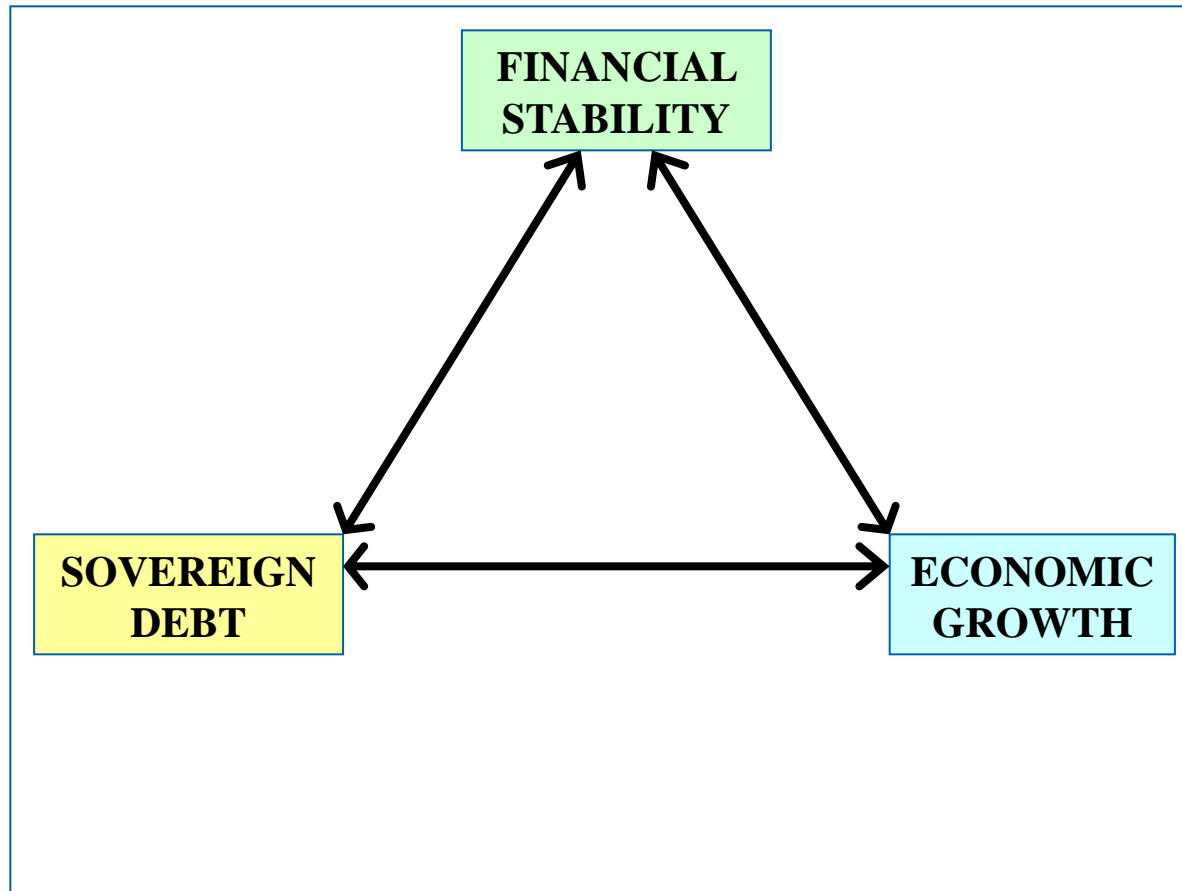
Immediate EU policy response:

- International coordination (G20)
- Stabilising the financial sector (liquidity support, guarantees, recapitalisation, regulation)
- Cushioning the impact on the real economy (European Economic Recovery Programme)
- Addressing the social impact



Higher public deficits and debt

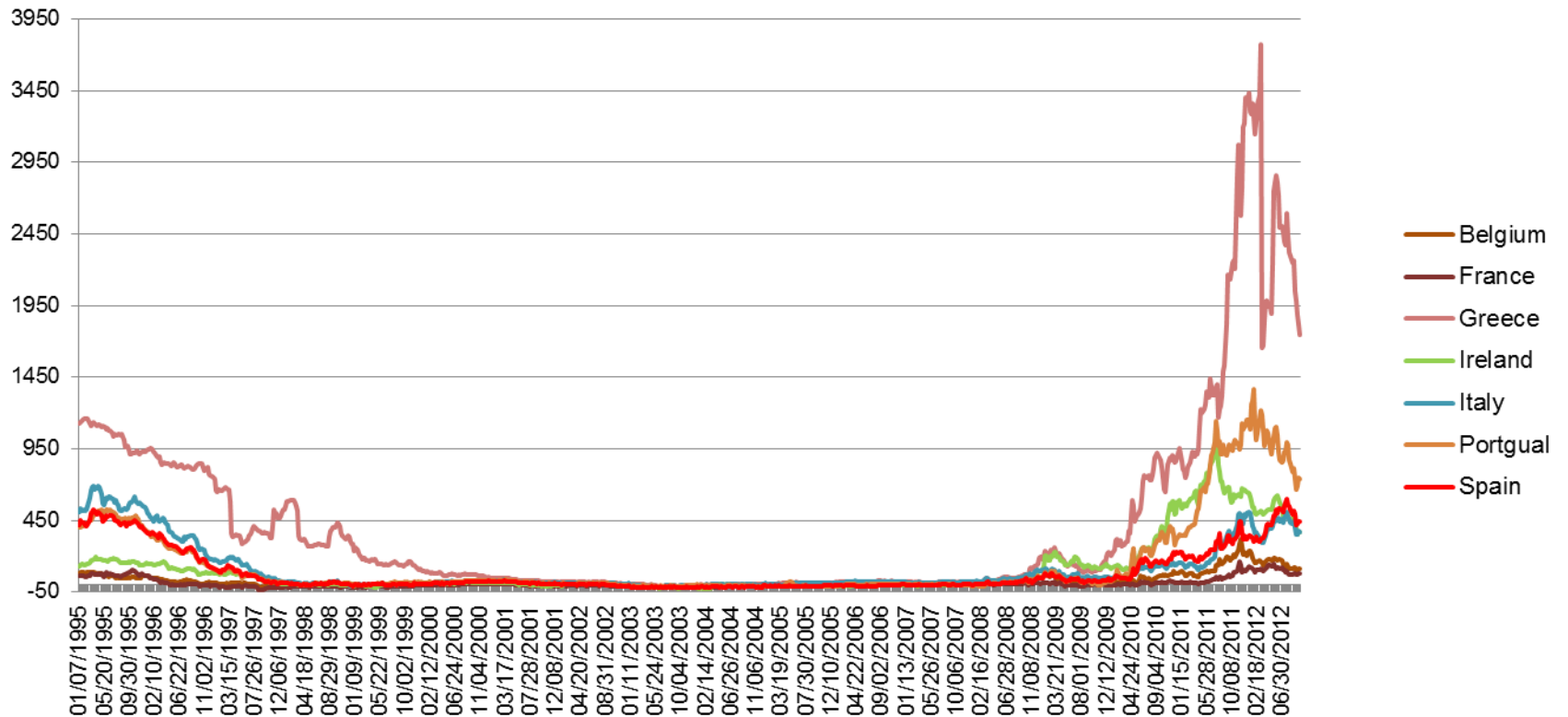
Negative feedback loops



Confidence crisis in the euro area

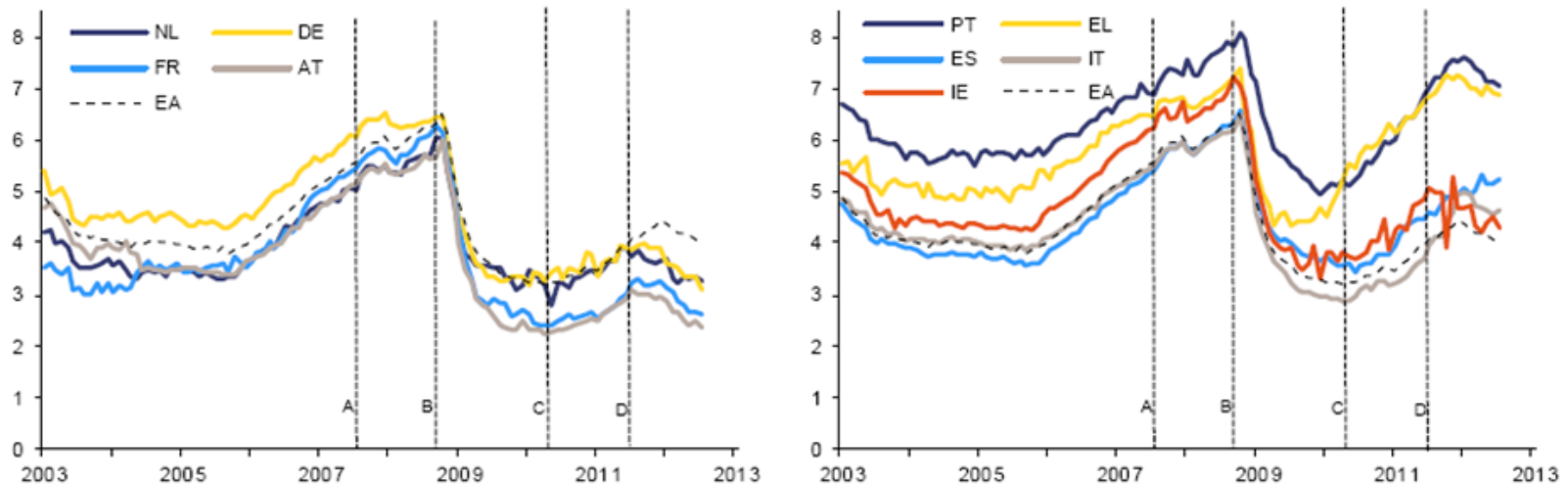
- New assessment of sovereign risk
- Fragmentation of financial markets
- Rating downgrades
- Redenomination scenarios

10-year spreads against German Bund yields



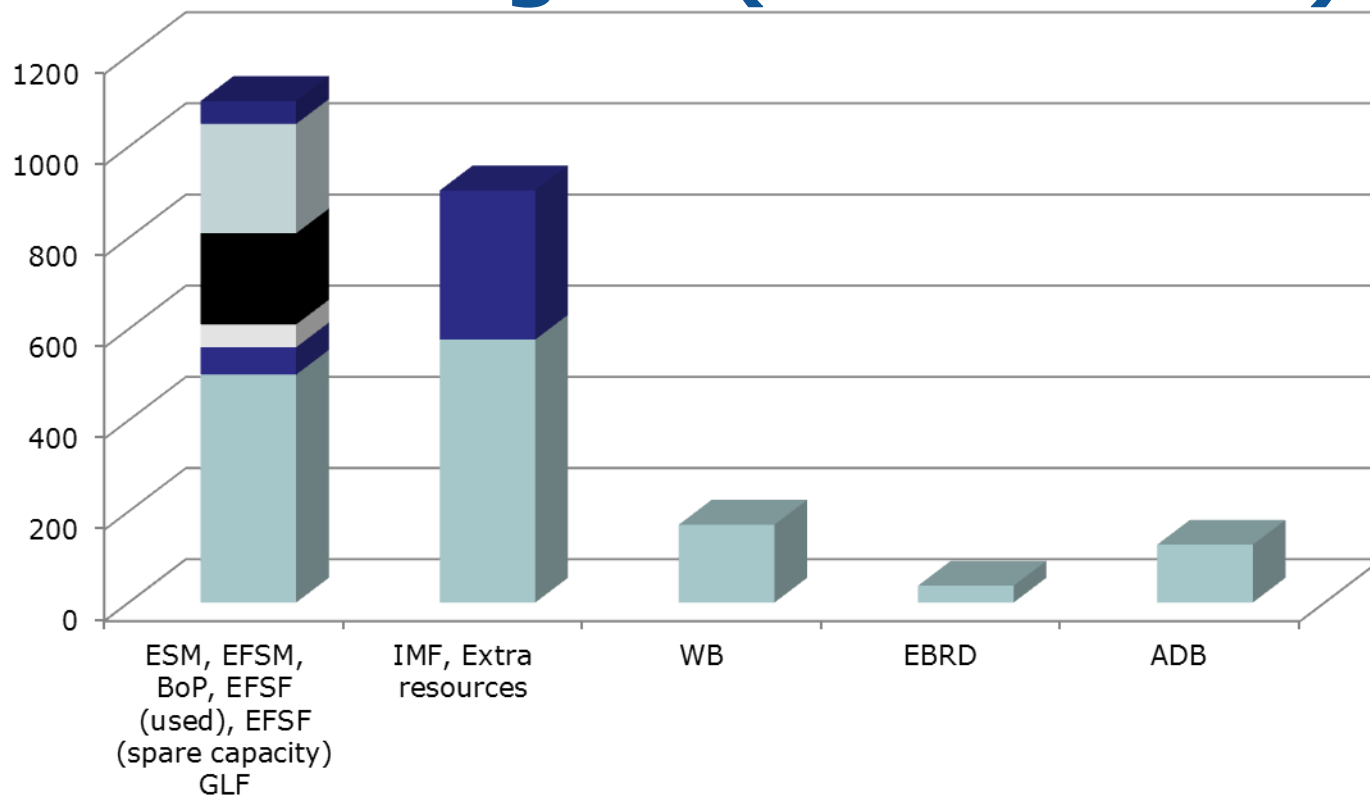
Interest rate divergence

Chart 03: Retail interest rates: Loans to NFCs
Loans with an initial rate of fixation of less than one year, %
Small loans (up to one million Euro)



Notes: A: Crisis outbreak; B: Lehman Brothers; C: First Greek programme; D: Sovereign contagion. Last data: July 2012.
Source: ECB.

EU financial firewall against contagion (~ €1 trillion)



ESM policy instruments



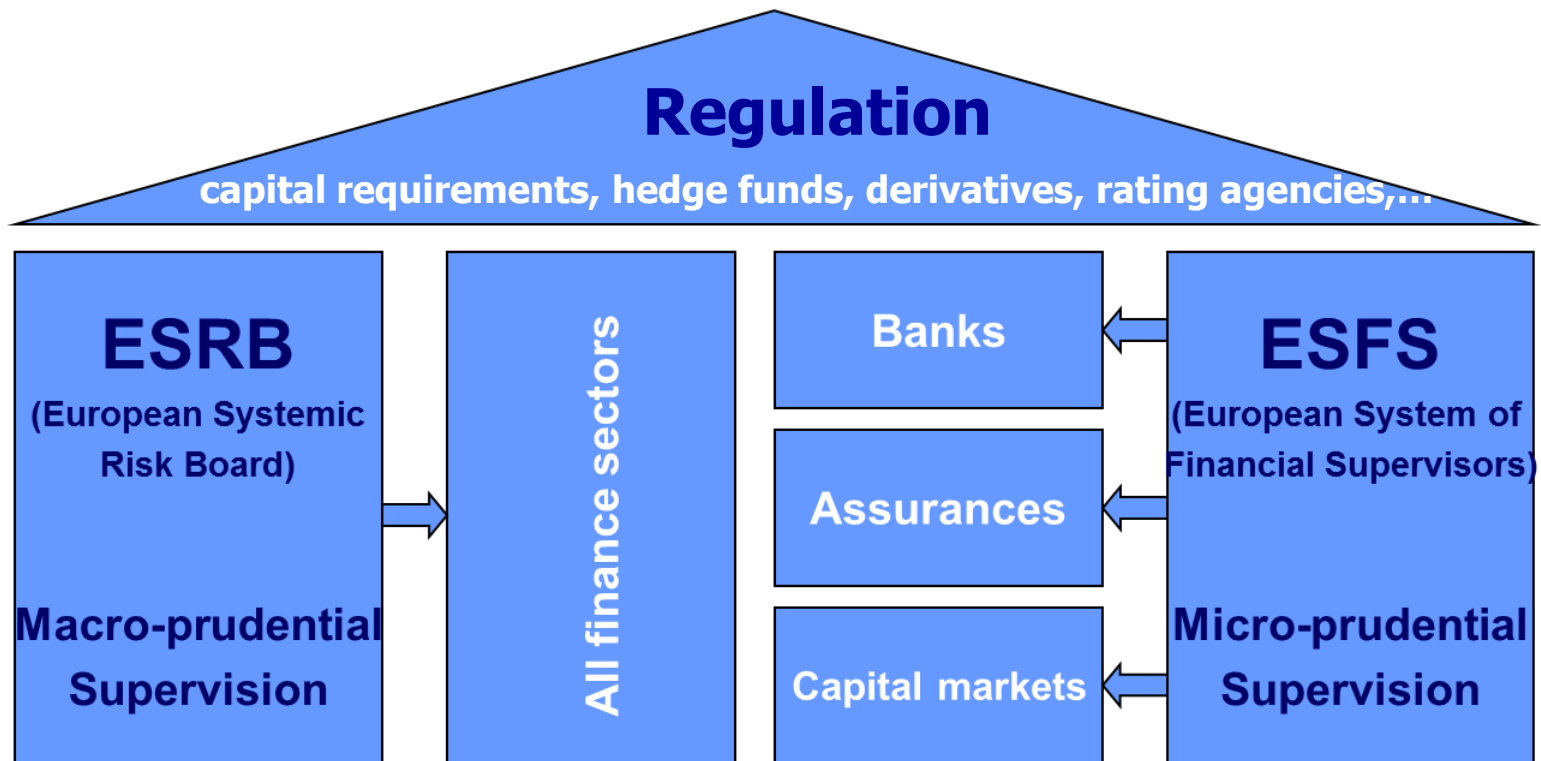
ESM loans for the recapitalisation of financial institutions

- To address situations where the source of a crisis is in the financial sector so as to limit contagion of financial stress
- Available to a Member State with a sound fiscal policy, ensuring the capability to repay the ESM loan
- Complementing measures of private sector and government of the Member State
- Financial sector-specific conditionality with a bank restructuring programme and financial sector reform as specified in the MoU

Financial Sector Regulation

- **Creation of the European System of Financial Supervisors**
- **EU Regulation on Credit Rating Agencies**
- **EU Directive on Alternative Investment Fund Managers**
- **Tougher capital requirements and better cross-border bank crisis management**
- **Other regulations (e.g. OTC derivatives, short-selling).**

New EU supervisory framework

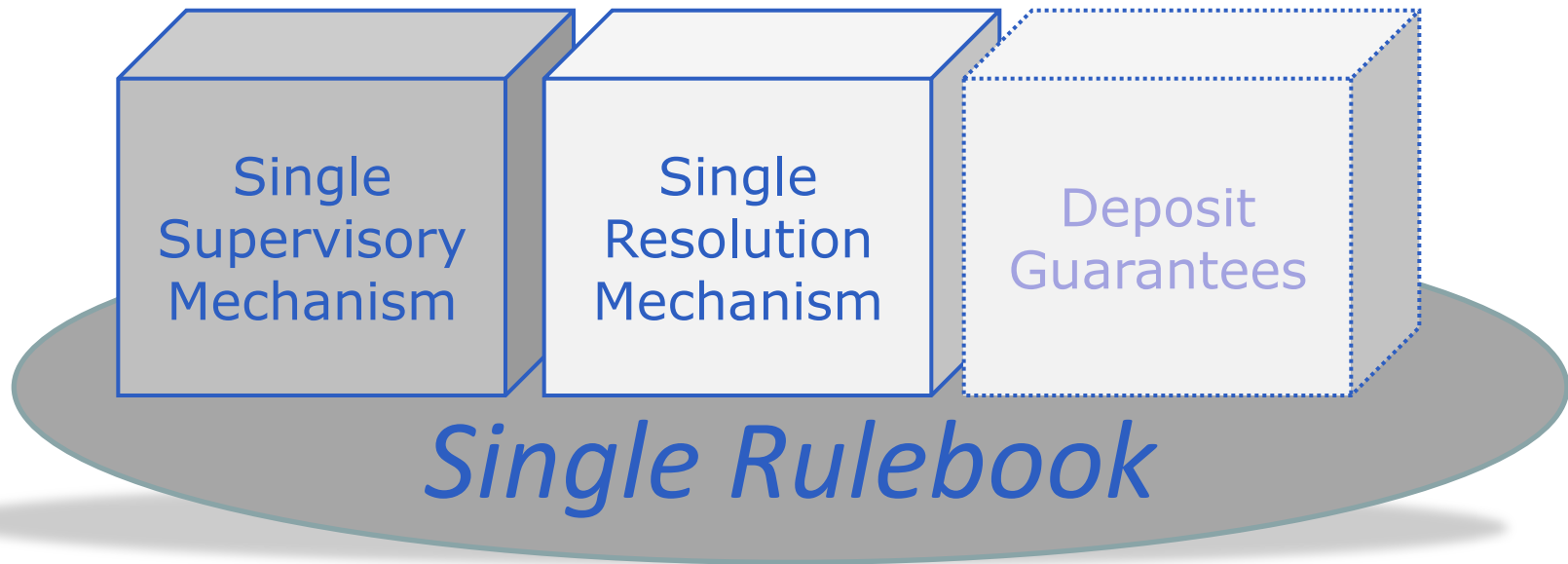


June 2012 report by 4 Presidents: towards a genuine Economic and Monetary Union

→ 4 building blocks:

- **An integrated financial framework:** single European banking supervision and a common deposit insurance and resolution framework
- **An integrated budgetary framework:** build-up of fiscal capacity, common decision-making on budgets, common instruments of stabilisation/adjustment, issuance of common debt... towards a fully-fledged fiscal union
- **An integrated economic policy framework:** stronger economic coordination, broader scope
- **Democratic legitimacy and accountability:** articulation EP, national parliaments, etc.

A roadmap towards a banking union



The Commission Blueprint: The short term (6-18 months)

- **Full deployment of on-going comprehensive response** ('Six-Pack'; 'Two-Pack'; Single Supervisory Mechanism)
- **A Single Resolution Mechanism** matching the Single Supervisory Mechanism
- **Ex-ante coordination of major structural reforms.**
- **Detailing and incentivising structural reforms for rebalancing:** the 'Convergence and Competitiveness instrument'
- **A rapid decision on the MFF**
- **Promoting public investment in the Euro Area**
- **External representation of the Euro Area**

The Commission Blueprint: The medium term (18 months to 5 years)

- **Greater control of national budgetary policies:**
a European collective control over national budgetary policy in defined situations
- **Scaling up the Convergence and Competitiveness Instrument:** a Euro area fiscal capacity, including borrowing
- **Towards conditional steps in debt mutualisation:**
 - European Redemption Fund → tackling legacy debt
 - Eurobills → financial market efficiency, conduct of monetary policy

The Commission Blueprint: The long term (beyond 5 years)

- **A full banking union** (supervision, resolution, deposit insurance) including 'fiscal backstop'
- **An EMU cyclical stabilisation instrument:**
 - for asymmetric shocks only
or
 - including symmetric shocks (implying borrowing)
- **Common public debt**

ECOFIN Council decisions of December 2012 on single supervisory mechanism

- ECB supervisory board will have direct oversight of eurozone banks, but differentiated and in cooperation with national supervisors, as of March 2014 (or 1 year after legislation in force)
- Will give ESM the possibility to recapitalise banks directly
- National supervisors remain responsible for consumer protection, money laundering, payment services and branches of third country banks
- EBA regulation to be changed on voting modalities
- Non-euro area members can opt in

European Council of December 2012: Roadmap for the completion of EMU

- Ex ante coordination of Member States' major economic policy reforms
 - Social dimension of EMU
 - Mutually agreed contracts for competitiveness and growth
 - Solidarity mechanisms for such contracts
 - Euro area governance
 - Democratic legitimacy and accountability
- ➔ *Proposals by June 2013*

Conclusions

The Single Supervisory Mechanism...

- ... is an important element to break the negative feedbacks between banks and sovereigns, also through the ESM
- ...is part of the crisis response and the steps towards a deeper EMU in order to bolster confidence and maintain the stability of the euro
- ... will preserve the integrity of the Single Market and reduce the fragmentation of financial markets
- ... will be followed by a proposal for a Single Resolution Mechanism before the summer to make further progress towards the banking union