Statement

Topic: Consultative proposals to strengthen the resilience of the banking sector announced by the Basel Committee

Addressee: Bank for International Settlements

Closing date of consultation: 16.04.2010

Joint Statement of BVMW, Bundesverband mittelständische Wirtschaft, and CEA-PME, Confédération Européenne des Associations de Petites et Moyennes Entreprises.

Key arguments of this statement:

1.) Impact studies are necessary to evaluate the effects of the new rules on SME financing.

2.) Loans to SMEs are subject to higher risk weights (RWA) than other assets. Therefore an increase of overall capital requirements will have a disproportionately negative effect on credit supply to SMEs. Diminishing the asymmetry between the asset class would stabilize the banking sector, rather than penalize SMEs.

Don’t ignore the consequences for small and medium-sized enterprises in Europe!

SME view about CRD4 consultation

Preface

The German Association for Small and Medium-sized Enterprises (BVMW) and its affiliated associations represent the interests of more than 150,000 members. The “Confédération Européenne des Associations de Petites et Moyennes Entreprises (CEA-PME)” is an independent confederation of national business associations from all across Europe. As a service provider for our members we observe the current revision of the Capital Requirements Directive (CRD), i.e. future regulation for financial stability must not restrict financing opportunities for SMEs.

The role of the banks

The most important economic task of the banks is the transformation between private savings and loans. Banks finance corporate activities. Twenty million SMEs in the European Union are dependent on bank loans because they have no direct access to capital markets. SMEs are the backbone of the economy representing 99.8 percent of all non-financial companies[1].

Regulation of financial institutions has to enable and support banks in fulfilling this pivotal economic task. Banks play an important role in society in ensuring the financing of sustainable growth. Therefore the European Commission should be taking more than just a single sided view regarding the stability of the banks and stop neglecting the terms and conditions of SMEs access to financing. The current crisis has not been caused by SME's defaulting on their loans. The large diversity of SMEs enables banks to achieve a risk diversification even without the use of the securitisation market.

But the Basel II capital requirements discriminate bank loans to SMEs in favour of other, riskier asset classes. Some of them were kindly certified with gracious ratings by external rating agencies. Examples are securitizations of US-real estate loans or bonds offered by Greece. In contrast, loans to SMEs are carrying higher risk weights of seventy-fife to hundred percent and above[2]. Because of this asymmetry an increase of overall capital requirements will have a disproportionately negative effect on credit supply to SMEs. Diminishing the asymmetry between the asset class would stabilize the banking sector, rather than penalize SMEs.

Credit Crunch and Rating

We agree that banking regulation has to be revised. Several studies describe the interdependencies between external rating agencies, leveraging, short-term orientation, salary systems, monetary policy etc., which led to the crisis[3]. Because of the interplay between ratings and capital requirements we suggest that the approaches which limit the

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[1] Eurostat statistical books (2009): European Business – Facts and figures, p. 47 f.

[2] Ohoven, Mario (2009): Commentary: The credit crunch is a failure of regulation, ifo Schnelldienst 15/2009, vol. 62., August 14, 2009, p. 13-15

[3] For example: Welfens, Paul J. J. (2009): Transatlantische Bankenkrise, Europäische Integration und Digitale Weltwirtschaft Band 1, Lucius & Lucius Verlag, Stuttgart
Larosière, Jacques de (2009): The high-level group of financial supervision in the EU – Report, 25 February 2009, Brussels

power of external rating agencies should be an element of CRD4, too. Also transparency requirements regarding the internal ratings must be addressed, so that the rating process will no longer be a black box for bank customers.

With the CRD propositions, the risk of a severe European credit crunch is increasing. The installation of additional internal and external capital buffers, the accountability of only high quality capital and permanent liquidity tests may push the bank lending behaviour in an even more restrictive direction. If this isn't counterbalanced, countercyclical measures and the tighter definition of capital could negatively influence the terms and conditions of SMEs financing. The credit crunch of 2003 should be a warning as to the effect of asymmetric banking regulation on the real economy.

BVMW and CEA-PME warned against the pro-cyclical effects when the Basel II regime was introduced. Current regulation is restricting the financing opportunities for SMEs in the current recession. Also there is no guarantee that in the future the planned "Capital Conservation Buffer" will be used to finance the economy in a downturn rather than to finance salaries, bonuses or losses resulting from high-risk speculations. We question a bank's ability to behave in a countercyclical manner consciously, even when CRD 4 is enforced. Therefore the first solution would be to change the "automatic" downrating procedure, which further weakens SMEs in a recession.

Independent Impact Study necessary

Because of the pivotal role of banks and the real consequences of bad regulation policies we strongly recommend an evaluation of the impact on SMEs financing under the new regulatory regime, which also has to take into account the measures planned outside the Basle consultation process such as national levies on banks. The effects on the financing opportunities for SMEs should be analyzed within two independent impact studies. At least one study should focus on "side conditions" such as the collateral requirements or bank margins.

According to the European Central Bank forty-two percent of the SMEs in Europe reported problems after having asked for bank loans in the second half of 2009. Eighteen percent of the SMEs in Europe reported a denial of bank loans and thirty-five percent were confronted with rising levels of interest rates. In all sectors European SMEs reported

tighter loan conditions[4]. This highlights the alarming situation. To avoid further macroeconomic damage, changes in banking regulation have to take this into account. However, the planned impact study only refers to the direct impact on banks' balance sheets, which shows a single sided view.

BVMW and CEA-PME will observe the ongoing process actively and constructively. We are awaiting details on how to balance the need of better regulation and the need of financing economic growth.

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[4] European Central Bank (2010): Survey on the access to finance of small and medium-sized enterprises in the euro area: Second half of 2009, 16 February 2010 p. 1 ff., p. 8