Mojmír Hampl: Should non-euro area countries welcome the banking union?

Speech by Mr Mojmír Hampl, Vice Governor of the Czech National Bank, at the Europolis Conference "Auf dem Weg zu mehr Stabilität", Technische Universität Berlin, Berlin, 5 April 2013.

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My remarks today focus on non-euro area countries' attitude to the SSM (Single Supervisory Mechanism), as it is the key part of what is called the banking union (BU) which is "almost" finalized.

Let me start with a statement that the so-called BU is currently only an emerging concept. We are very far from the final version and it is difficult to guess what the final outcome might be. Nevertheless, what we get in the end will be critical for the position of non-euro area countries.

So, what is it all about? The proposed BU is based on four/five pillars, or "legs":

a. CRD IV – the Capital Requirements Directive, or single rules

b. SSM, or the Single Supervisory Mechanism under the ECB

c. Single resolution and recovery mechanisms a rules

d. A single system of deposit guarantees

e. Finally, a fiscal back-up through the ESM

Problems emerge immediately, because each pillar is at a different stage of negotiation and approval, involves different rules of approval and, more importantly, so far each applies to a different group of countries:

a. The ESM already exists. But it will have to be clarified under what conditions it may be used for direct recapitalization of financial institutions. What's important for our discussion is that ***exclusively euro-area countries*** are covered with the ESM.

b. CRD IV will apply to all ***27 EU members*** and is close to be approved.

The SSM has recently been negotiated for ***euro-area countries plus volunteers*** from other

c. EU countries, but has not been approved yet. Germany is currently blocking its approval. Its political sensitivity is not negligible, but do not forget that "money" is not involved directly yet. Nevertheless, its future functioning will require money, and that will be crucial.

d. The single resolution and recovery rules for banks are proposed and meant ***for the whole EU27***, while the resolution authority will most likely cover only the ***members of the SSM***. All these are now under preparations and discussions, exactly as the new rules for the DGS.

The resolution rules and the single DGS are where the political clashes will inevitably happen. Two reasons for that:

1. First, this is where the money enters. One has to realize that the incentives of the various countries and pan-European institutions are different. "Northern" countries want to cut the banking sectors of "southern countries" free from local politicians, but at no additional cost. "Southern countries" want money. And many pan-European institutions and politicians across the board support anything heading towards a European political union. Different incentives mean different positions in negotiations.

2. Second, some EU bodies are obsessed with the “all EU countries must be same” approach. While there may be some point to this, why insist on it in the case of the single resolution system, for instance, if it has been negotiated that the SSM only applies to euro-area countries plus volunteers? One can hardly expect non-euro area countries not participating in the SSM to jump at the single resolution system if it means sharing the burden with those inside the banking union without the same treatment in the area of a fiscal back-stop. At the same time, would you join the SSM if you did not have a clue how the single resolution rules were going to work?

The CNB’s position was: let’s discuss the whole thing (BU) in one shot as a one compact and coherent package where the balance between powers, duties, responsibilities and money always remains assured. And negotiate everything as a single animal, so that illogical inconsistencies are not being produced all along. Sure, that would take much more time, but the final outcome might look better and we would not build up the house from the roof down.

We are debating the supervisory part first, while burden-sharing (money) is being left for the future. The sequence of steps should ideally be exactly the opposite one. Why? My observation is that the way the various bail-outs and the SSM have been negotiated so far shows that the readiness and willingness even among euro-area countries to share money is declining over time. And this is exactly the opposite of what should have been happening if a functioning banking and contingent fiscal union had been emerging. So we are risking creating a half-baked BU which will not necessarily be ready for future bad times. And it is also a partial answer to the question of potential participation of some non-euro countries in the SSM. Simply, it is too premature to judge whether the BU is going to be a good project worth participating, or not. Only after the whole project with all it “legs” is created can one seriously answer this question.