Sabine Lautenschläger: Countdown to November – European supervision ready for lift-off

Speech by Ms Sabine Lautenschläger, Member of the Executive Board of the European Central Bank, at the Handelsblatt Konferenz "Banken im Umbruch", Frankfurt am Main, 3 September 2014.

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Summary

European banking supervision will draw on the long-standing experience of 18 – soon 19 – Member States and incorporate it into a new European supervisory culture, said Sabine Lautenschläger, Member of the Executive Board of the European Central Bank (ECB) in a speech at the "Banken im Umbruch" conference in Frankfurt am Main.

A significant advantage of the new Single Supervisory Mechanism (SSM) is the possibility to make cross-country comparisons. "I am not just thinking of the assessment of specific portfolios here, but also of the early identification of risks, which only become visible, or are at least easier to identify, in horizontal analysis", she said. The asset quality review has already given us a deeper insight into the banks' procedures, thereby making it possible for us to check "which differences between banks are justified and to ascertain where we need to probe critically".

Ms Lautenschläger stressed that, although decision-making in the new European banking supervision will be organised centrally, the SSM can build on regional knowledge and experience. "As national supervisory authorities participate in the supervisory process, the ECB remains close to regional market and banking structures", she said. Also in terms of staffing, the SSM will bring together people from different supervisory cultures. The heads of Joint Supervisory Teams will come from a country other than that in which the institution it is supervising is established. "In concrete terms: the head supervisor for Deutsche Bank will be a French lady; BNP Paribas will be supervised by an Italian man."

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Ladies and gentlemen,

In precisely two months' time, we will usher in a new era in the euro area. With the establishment of the Single Supervisory Mechanism (SSM) on 4 November 2014, the European Central Bank (ECB) will assume key competencies in the field of banking supervision. However, unlike the introduction of the euro banknotes and coins in 2002, this step towards further integration will not entail a major symbolic change that is tangible for all citizens. Nevertheless, the start of the SSM means progress, not only in European integration, but also in day-to-day supervisory work.

The ECB – one of the world's largest supervisors

The ECB will take on the direct supervision of around 120 credit institutions and more than 80% of the aggregated balance sheet for the euro area banking sector. In absolute figures, this means a total of more than €21 trillion as per 30 June 2014. In addition, the ECB will be indirectly supervising the less significant institutions, of which there are just over 3,500. Here, we will shape supervision by setting binding supervisory standards.

This will make the ECB one of the world's largest supervisors. I anticipate that, over the next few years, the geographical area under our remit will expand and that the number of directly and indirectly supervised banks will continue to grow. On the one hand, further countries will join the euro area. On the other hand, the regime of "close cooperation" gives EU Member

States who do not yet have the euro as their currency a chance to participate in the banking union. When this option was introduced into the SSM Regulation, sceptics thought it unlikely that a Member State would exchange its exclusive supervisory competences for membership of the supervisory mechanism. Developments over the last few months have shown, however, that the ECB has significantly more to offer than just a seat on the Supervisory Board. The ECB enjoys trust and credibility – valuable assets for both monetary policy and banking supervision alike.

Credibility, however, has to be earned anew each day. In this respect, the ECB's monetary policy can already look back on a solid track record. In the area of banking supervision, we stand at the very beginning. But that does not mean that we will only start to find our way on 4 November. For many months now, my colleagues and I have been working to determine, among other things, the focus of our supervisory approach, both conceptually and thematically. The critical issues are: how can the ECB reap the intrinsic benefits of supervising 19 national banking systems? And how can we ensure that institution-specific insights of the national supervisors are best maintained and incorporated? Allow me to give you a few examples to explain the conclusions we have reached. I will focus on the specific features of the SSM. So do not be surprised if I do not mention things that are self-evident, such as a preventative, forward-looking and risk-oriented supervisory approach.

18 perspectives – one best practice

Let us start with 18 perspectives and what is deemed best practice. In developing the SSM's supervisory culture, we are in a unique starting position. Following the financial market crisis, many countries adjusted their supervisory structures. The reforms generally focused on addressing country-specific experiences of the crisis and on international recommendations. We are in a similar situation in setting up the SSM – but with one major difference: we are not just looking at the experiences of one country; we are incorporating the perspectives of 18 – soon 19 – Member States into a common European supervisory culture. For me personally, this is one of the most exciting aspects of creating the supervisory mechanism. An example of this is the weekly meeting of SSM management. Every Friday, Danièle Nouy and I meet with the heads of the four SSM business areas. Around the table we therefore have representatives of the French, German, Finnish, Spanish and even US supervisory traditions. Another colleague brings to the table many years of experience at a systemically relevant bank. That is of course just one example, among many, of how we are drawing on the various approaches to establish what is "best practice" as the basis for our supervisory activity. This process will not be completed by 4 November, but will rather be further refined over the coming years.

Horizontal analyses and a level playing field

Another considerable advantage of European banking supervision will be the possibility to draw comparisons across European countries and to establish a level playing field. The banking sectors of many European countries are dominated by a few large banks. The national supervisory bodies were therefore faced with the problem of having to assess circumstances on the basis of just one bank, or on that of a very small group of banks. I am not just thinking of the assessment of specific portfolios here, but also of the early identification of risks, which only become visible, or are at least easier to identify, in horizontal analysis. Although international working groups and the European Banking Authority (EBA) have addressed this problem, it is only with the establishment of the SSM that a quantum leap forward can be made. The SSM is able to draw on detailed supervisory information from across the euro area and prepare comparative analyses. And I am using the present tense here on purpose. With the ongoing comprehensive assessment, we are already active at the European level. With great efforts on the part of the authorities and banks involved, we have submitted the assessment of the bank portfolios to a unified assessment scheme. The asset quality review has given us a deeper insight into the banks' procedures, thereby making it possible for us to check which differences between banks are justified and to ascertain where we need to probe critically. We will use the knowledge that we have obtained through the peer group review for other supervisory activities as of 4 November. Thus far, these processes have been carried out at the national level. We are now going to harmonise them throughout the euro area, thereby making it easier to compare the respective risk situations of banks, thus enabling us to target our supervisory activities better.

Federal structure – central decision-making

Critical voices have warned us in the past about losing sight of the diversity of the European banking sector and wanting to typify a "European" bank. I admit that, in the process of harmonising and centralising decision-making powers, there is always also a danger of seeing everything at par. The ECB is, however, protected from such developments by institutional barriers. As national supervisory authorities participate in the supervisory process, the ECB remains close to regional market and banking structures. Moreover, the ECB's staff will take a keen look at the business models and risk profiles of each directly supervised bank. The kick-off meetings, which have been taking place since early summer between the current supervisors, the ECB and the banks, are simply a first step.

In this connection, allow me to stress the inherent dangers in supervision not only of being too far removed, but also of being too close. Other viewpoints and new supervisory approaches and methods may sharpen our perception and mitigate the danger of accepting a bank's unjustified customs merely because they have long been familiar to us. The comparisons and analyses I referred to earlier will also help to counter this danger.

But that is not all. We will also address this issue in terms of our staffing policies. The head of a Joint Supervisory Team (JST) must come from a different country to the country in which the institution it is supervising is established. In concrete terms: the head supervisor for Deutsche Bank will be a French lady; BNP Paribas will be supervised by an Italian man. In addition, there will a rotation of staff members among the JSTs. All in all, this will not only enable us to reach more objective judgements about a bank, but will also foster the development of a common supervisory culture.

Banking supervision in a central bank

Allow me to say a few words about banking supervision in a central bank. Housing the SSM within the ECB will enable us to benefit from synergy effects. Exchanges with colleagues from market operations, payment systems and economic analysis will help the supervisors to develop a different viewpoint on current market developments, the importance of a specific institution for payments and the economic environment. One area in which cooperation will be particularly intensive is macro-prudential supervision. Our aim here is to bring together insights from both the macro-prudential and the micro-prudential areas, and to address undesirable developments in a targeted way.

Conclusion

Ladies and gentlemen, the European supervisory landscape is facing a major change. With the SSM, we have created a strong, new supervisor at the European level. The SSM will be able, and have the responsibility, not to do everything differently, but to do some things better. With the conclusion of the comprehensive assessment, and the publication of the results in the second half of October, and the start of our supervisory activity on 4 November, we have a few stressful months ahead of us. But we must also remember to occasionally pause for a moment and to reflect beyond the immediate tasks at hand. The SSM may have been created as a consequence of, and as a solution to, certain problems in Europe. But it is destined to be able to achieve much more and – at least that is my hope – to have an effect over and beyond Europe.

Thank you for your attention. I am now at your disposal for questions.