Sabine Lautenschläger: After one year of European banking supervision, have expectations been met?

Speech by Ms Sabine Lautenschläger, Member of the Executive Board of the European Central Bank and Vice-Chair of the Supervisory Board of the Single Supervisory Mechanism, at the Austrian Bankers' Business Lunch, Frankfurt am Main, 13 January 2016.

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Ladies and gentlemen,

With Christmas and New Year now behind us, this is a good opportunity for a brief look back at the last 12 months – the first full calendar year of the Single Supervisory Mechanism (SSM). I will also look ahead to the forthcoming year, turning my attention to the issues facing banking supervision in 2016.

After a year or so of operations, it is time for the SSM to ask itself whether European banking supervision has succeeded in fulfilling the high expectations that people had of it.

Our task is to make the SSM a truly European institution, combining the experience of 19 different national supervisory authorities and establishing a common standard that allows banks to be supervised without the influence of national interests. It is important in that regard that the SSM identifies risks in good time, reacts quickly, and acts both efficiently and effectively.

Has the SSM lived up to these expectations? I believe it has. As Vice-Chair of the Supervisory Board of the ECB, I am of course biased, so I would like to offer some evidence in support of this assertion.

Last year saw the successful completion of our Supervisory Review and Evaluation Process (SREP), which was conducted on the basis of a uniform methodology. That enabled us, for the very first time, to measure institution-specific risks in the euro area's largest banks using a common yardstick. What is more, we also plan to make full use of the options and discretions that European law makes available to competent supervisory authorities, exercising them in a uniform manner across all euro area countries. Thus, we have begun to foster harmonisation in this area as well.

Such efforts over the last year have helped us to lay the foundations for truly European banking supervision. Consequently, our focus this year will shift slightly – from the methodology and structures of banking supervision to its content.

Banking supervisors are effectively tasked with worrying. That is what we are paid to do. Our work involves looking for risks that could potentially pose a threat to the stability of the banking system. Looking ahead to 2016, we have identified a series of risks and, on the basis of those risks, chosen to focus our supervisory efforts in five specific areas.

The first concerns banks' business models. At the heart of our work lies the question of the consequences that the sustained period of low interest rates will have for the various institutions and their business models. If they are forced to adjust their business models, banks could potentially move into riskier areas in search of yield. That would increase not only the risk of bubbles in financial markets, but also the level of risk within individual banks. We will therefore be looking very closely to see whether banks are adjusting their business models, what direction they are moving in, and what risks that involves.

Our second priority concerns credit risks. We are continuing to see large stocks of non-performing loans in certain banks. In order to address this problem at European level from a supervisory perspective, we established a dedicated working group last year. That working group has been tasked with developing and implementing a consistent supervisory approach aimed at supporting a reduction in those large stocks of non-performing loans. However, this second priority is not just about non-performing loans; it is also about cluster risks – the concentration of exposures in specific sectors, such as the property sector.

The third priority is banks' capitalisation. It is clear that banks have significantly increased their capital since the crisis; and from our perspective, the capitalisation of the European banking system as a whole is satisfactory. Our focus will be on two things. First, we will be looking at the new requirements concerning the capital components that absorb losses in the event of a bank becoming insolvent. "TLAC" and "MREL" will be the key terms in this respect. Second, we will again be looking very closely at what exactly constitutes capital, as well as establishing an overview of the banks' internal models and processes used to determine the capital requirements.

The fourth priority is banks' internal risk management. Against the background of low interest rates, cheap refinancing and low profitability, it is increasingly important that banks manage risk in an appropriate manner. To do that properly, managers need sound data on which to base their decisions. We will therefore be formulating specific requirements concerning risk management and data quality.

Our fifth priority will be banks' liquidity. The 2008 financial crisis showed how dangerous liquidity problems can be – not just for individual banks, but for the financial system as a whole. Some banks are failing to meet our expectations in terms of the management of liquidity risk. We will therefore be paying particular attention to banks' internal liquidity management – i.e. the Internal Liquidity Adequacy Assessment Process (ILAAP).

Alongside these five substantive priorities, we are continuing to work on supervisory structures and methodology. That includes the issue of national powers. In many countries, national legislation provides that supervisory authorities are competent to deal with specific issues in the area of solvency supervision that are not expressly referred to in European legislation. The question, then, is whether the ECB, as a European institution, can directly exercise such competences. Thus far, this question has only ever been answered on a case-by-case basis, which is certainly not ideal. We need a consistent approach in this regard.

We also need to look at the delegation of decisions. At present, all of the Supervisory Board's decisions go to the Governing Council of the ECB in draft form for adoption. In 2015 alone, we took a good 1,500 supervisory decisions by means of that process, including many routine decisions. In order to allow the ECB's decision-making bodies to concentrate on important cases, we are considering delegating at least routine decisions.

What we need here is a framework allowing the unobjectionable delegation of less important decisions – i.e. decisions that have only minor implications for the bank in question, or routine decisions that involve little in the way of discretion. The delegation arrangements will be such that ECB staff have a clear framework enabling them to take the routine decisions that are delegated to them.

Ladies and gentlemen, that concludes my brief review of 2015 and my look ahead to 2016. Thank you very much for your attention. I am now at your disposal for questions.