Sabine Lautenschläger: Interview in Süddeutsche Zeitung

Interview with 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, in *Süddeutsche Zeitung*, conducted by Ms Meike Schreiber and Mr Markus Zydra and published on 2 November 2016.

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Ms Lautenschläger, you have been supervising banks for 20 years, first at BaFin, then at the Bundesbank and now for nearly three years at the ECB. What has changed in that time?

Supervision has become more objective and more intensive. We benefit on a daily basis from the fact that knowledge, experience and supervisory traditions from 19 countries come together to form a new supervisory approach. That sharpens our focus and makes supervision better. But it's now also become more complex, as we don't have just one legal system to take into account. A supervisor usually has considerable room for manoeuvre, and in our case this room for manoeuvre can, for certain topics, be based on up to 19 different legal frameworks. Everything thus has to be well-founded.

So you can pretty much do what you want as long as you can explain it properly?

That's putting it too simplistically. But let me give you an example: German law requires banks to have appropriate risk management measures in place, and the term "appropriate" is defined in more detail. These German requirements do not necessarily have to correspond with the ideas of national legislators in other countries.

And?

This sometimes complicates our task of treating banks with similar risk profiles in a similar way.

Was it easier when you were at BaFin?

It was different. The decision-making process was that of a typical German authority: individual people, or a small number of people, took the most important decisions and determined the approach to be followed. Within a European body that combines different traditions and points of view, things are – and should be – different.

When you were at BaFin you often used to pop into the offices of your staff and see how things were going. Do you still do that?

I still like to speak directly to colleagues and staff, but this has unfortunately become a rarer occurrence because I spend a lot more time in meetings.

One of the issues is how stable Europe's banks are. Hand on heart, how many German banks would take the global financial system down with them if they were to go bankrupt?

It depends not just on the bank, its size and its interconnectedness with other banks, but also on the sentiment of market participants. I'm sometimes surprised at how stock market investors take certain pieces of news calmly that I consider to be relevant, and then at other times information that I consider to be fairly harmless or only relevant for an individual bank or a handful of banks pushes down stock prices for many. Do you remember Lehman?

Yes, absolutely.

You see, the failure of Lehman in 2008 did not just affect those market participants that had a business relationship in the broadest sense with the company; whole segments of the market were affected and became illiquid. Hardly anybody expected the effects to be so far-reaching. So if anyone tells you now that they know exactly how the markets will react in such circumstances, I would start to get sceptical.

So it can't be ruled out that there might be another financial crisis of the kind we saw in 2008?

A financial crisis can never be ruled out entirely. But much has been done since 2008 to make the banking system more stable and to give us greater scope for action. Banks now have greater capital and liquidity reserves and better risk management than in 2008.

So no need to worry?

Banks are now much more resilient, and we as supervisors are able to take more far-reaching action in dangerous situations now that we have more instruments at our disposal.

The IMF recently described Deutsche Bank as the most dangerous bank in the world. As the responsible supervisory authority, you surely can't stand for that, can you?

You'd have to ask the IMF what criteria they applied in coming to this conclusion. The IMF also put it differently.

It said that Deutsche Bank appeared to be the most important contributor to systemic risks.

You see, that means something different from saying that it's the "most dangerous" bank in the world. The Financial Stability Board has published a ranking of the large, globally active banks according to their systemic relevance – that serves as a good guide.

So Deutsche Bank doesn't have any problems? It isn't dangerous?

I don't comment on individual banks.

Let's talk about Europe instead. Doesn't Italy's banking crisis, for example, demonstrate that many legacy problems are now emerging that were overlooked by your predecessors, namely the national supervisors?

A bank which is in the traditional lending business can by and large only do as well as its customers are doing. Transactions that were deemed safe when they were concluded can for various reasons, such as an environment of persistently weak economic growth, end up being anything but, turning into non-performing loans that are expensive for the bank. The supervisory authority cannot influence economic developments, but what we can do is ensure that the affected banks make appropriate loan loss provisions for non-performing loans, improve their processes for dealing with such loans and find sustainable solutions. This we have done and will continue to do.

Do you have a vision of what an ideal stable banking market should look like? Should there be fewer banks?

There is no European banking market as such – there are too many differences between the banks and the environments in which they operate for that – and so there is no single vision either. For us it is important that banks are in a strong position – with regard to both business model and profitability – in terms of capital and liquidity. That is why we are constantly reviewing their business models and the conditions under which they need to be viable. And there are certainly differences within the euro area in this respect. Some banks have to deal with non-performing loans and large loan loss provisions, while others are competing with many other banks for the same customers. And so the question of consolidation does then arise, and rightly so. But please not in the form of a merger of two weak banks. It would be better to see two strong banks come together, maybe in a cross-border merger – that would have many advantages.

This obstinacy is not popular with the banks, and many politicians also fear that banks will no longer be able to lend sufficient volumes as a result of all the regulation. What political pressure do you face?

As supervisors, we want to have banks that are able to finance the real economy not just in the short term, but also in the medium and long term. Some see a contradiction between banks granting loans and at the same time meeting tough regulatory requirements, but I don't see a contradiction here. Quite the opposite: a bank that has to fulfil strict supervisory conditions will be able to service the economy not just for the next few years, but also in the longer term.

The current business strategy of most banks mainly involves raising fees. Doesn't that mean that consumers are also paying for the ECB's zero interest rate policy in this way?

I have a question for you: would you like to give away your newspaper for free?

Not really...

Quite! But you would like your bank to manage your account, say, for nothing? I think that we need fair prices for services in the banking sector just like in any other sector. Everything cannot always be free. And that has nothing to do with low interest rates, it is a general truth.

Are you saying that the low interest rates are not a problem for the banks?

In the long term, the low interest rate environment can represent a considerable challenge, in particular for banks in the traditional lending business. But I would like to point out two things. First, the low interest rates are the result of persistently weak growth and structural factors such as demographic change. So many factors, both national and global, play a role here, not just the central bank's key interest rate. And second, the period of low interest rates also has benefits for the banks. They can obtain refinancing at better rates, and expansionary monetary policy also supports the economic recovery, which is also beneficial for banks.

Yet banks now even have to pay a penalty rate if they deposit money with the central bank. Is the ECB not putting the stability of banks at risk in this way?

It isn't easy at present, but banks have to find a way of dealing with the economic environment in which they find themselves. The banking business means constant adjustment. And a large number of the banks that have clear weaknesses in their business models had income that was too low and costs that were too high even before interest rates were low.