Sabine Lautenschläger: State of play in the European banking sector

Speech by Ms Sabine Lautenschläger, Member of the Executive Board of the European Central Bank and Vice-Chair of the Supervisory Board of the European Central Bank, at the IIF Annual Meeting, Washington DC, 13 October 2017.

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It is quite difficult to present my views on the state of the euro area banking sector in such a short statement – there are more than 100 large and medium-sized banks in 19 countries, with substantial differences between them.

But what I can say is that the banks are in a better position than they were. They are better capitalised and have improved their liquidity situation and their governance. They are making slow but steady progress in tackling all the well-known challenges and adapting their business models.

Still, supervisors are paid to demand more. So we want quite a few banks to adapt more quickly to the new environment.

- Digital technology is rapidly gaining traction in the banking world. It brings new opportunities but also new competitors for each and every bank. And we are seeing more and more banks incorporating a digital dimension into their strategies. However, they are doing so at varying speeds and we are not always satisfied with their progress. All banks need to focus on transforming their services more quickly.
- Interest rates are still low, weighing on the profits of many banks. This situation makes it imperative for them to adjust their business models. Some banks still need to diversify their sources of income, manage their costs more diligently and become more efficient.
- Legacy assets, such as non-performing loans, are still high in some parts of the banking sector in Europe. They depress banks' profits and curb their ability to finance the economy. The good news is that we are seeing some progress here. The proportion of non-performing loans in the euro area fell from more than 7% in the second quarter of 2015 to below 6% at the beginning of 2017. Still, I think the banks need to be more ambitious. We are not satisfied with the strategy of each and every bank. Some need to act more decisively – and we will push them to do so.
- And finally, Brexit is on the horizon, and will have a major impact on the banking sector. Most of all, it will affect those banks which access the European market from the United Kingdom and vice versa. They have to prepare themselves for other forms of market access – and quickly.

All this is happening at a time when the banking sectors of some countries still need to consolidate.

Let's turn to Europe's banking union. It now rests on two pillars: alongside banking supervision, there is a mechanism that allows us to resolve banks without disrupting the financial system. Banks can fail, and they will fail. That became clear earlier this year when the new system passed its first test.

What is still missing, though, is the third pillar of the banking union: a joint deposit insurance scheme. But the first two pillars alone ensure that the most critical aspects are covered. Banks, their owners and their creditors not only have to comply with stricter rules and more intrusive supervision; they are also subject to greater market discipline as it has become clear that they can be allowed to fail.

It is up to each bank to endeavour not only to survive but also to prosper in these circumstances. And the good news is that it is possible to do so. Our analyses have revealed that there are a number of banks which consistently outperform their peers. So there is progress and hope, but only for those who understand this new world, accept it, and act accordingly.

Thank you for your attention.