

Yannis Stournaras: Financial stability, macroprudential regulation and microprudential supervision

Welcome address by Mr Yannis Stournaras, Governor of the Bank of Greece, at the 1st Annual Workshop of ESCB Research Cluster 3 “Financial stability, macroprudential regulation and microprudential supervision”, Athens, 2 November 2017.

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It is with great pleasure that I would like to welcome you to this first workshop of the ESCB Research Cluster looking at issues related to financial stability, macroprudential regulation and microprudential supervision.

Since 2008, the global financial crisis and the European sovereign debt crisis have had profound implications for how central banks think about financial stability and the toolkits which are employed in its defense. In the past, emphasis was placed on supervising individual institutions – so-called microprudential supervision. The most obvious example of such supervision is that of capital adequacy regulations which are harmonised across countries and have through the years become ever more complex. However, discussions about how much capital banks should hold and what counts as capital are still the subject of on-going research. Moreover, other supervisory tools are being examined such as rules surrounding bank leverage and liquidity.

Perhaps, however, the most important challenge facing European banks is that of non-performing loans. There are two broad areas where research is needed.

First, how do we deal with the legacy NPLs, those that built up during the crisis? Questions which arise include: what is the best way to reduce NPLs quickly? To what extent are there issues of strategic default? What institutional reforms are required in the wider economy to facilitate the smooth work-out of NPEs? What are the implications for financial conditions of NPEs and the smooth transmission of monetary policy?

The second broad area is how we treat new NPLs going forward. Here I consider it important to have some research input to issues such as appropriate provisioning policies and balancing the need for provisions whilst at the same time not interfering too much with banks’ ability to do their job, namely, oiling the wheels of the real economy.

In addition to microprudential supervision, we can now add macroprudential regulation. This type of regulation focuses on the stability of the financial system as a whole. Tools are used to try to understand the build-up of systemic risk in order to provide early warnings and prevent systemic crises. Interlinkages between financial institutions are mapped out in order to understand how vulnerable the system is to a specific shock and the extent to which the shock will be contagious. The input of research has been invaluable in guiding central banks and the output of the Macroprudential Research Network (or MaRs as it was known) was surely vital in helping central banks get macroprudential regulation up and running.

At the same time as research has been progressing, the institutional structure of regulation and supervision has also undergone considerable reform. The European Systemic Risk Board was created in the wake of the global financial crisis following the recommendations of the High Level Group chaired by Jacques de Larosiere. The de Larosiere Report focused on the need to move beyond microprudential supervision and give due attention to ensuring the stability of the financial system as a whole. As part of the process of implementing its recommendations, macroprudential regulation became a central bank core task. The research conducted in fora such as this one provides valuable inputs to this work.

We have also seen major changes in the area of microprudential supervision with agreement on

the goal of European Banking Union and the creation of the Single Supervisory Mechanism and the Single Resolution Mechanism. The Single Supervisory Mechanism seeks to provide a consistent method of supervising 120 significant European banks. Once again research input is crucial to building up that method. To reap the full benefits of these institutional changes, it is important that the Banking Union be completed by creating a common Deposit Insurance Scheme and setting up a credible common fiscal backstop to the Single Resolution Fund that underlies the Single Resolution Mechanism. Perhaps strengthening the financial resources of the ESM could provide a way forward in this respect.

Research Clusters were only recently set up by the Heads of Research in order to encourage interaction and collaboration between ESCB researchers working on fields of common interest. It is planned that each research cluster will have an annual workshop where papers, selected on the basis of academic quality, will be presented and discussed. The workshops will provide an opportunity for researchers from national central banks and the ECB to get together and discuss advances in their respective fields – something that will have particular benefits for researchers who work in smaller central banks. I trust that you will find the atmosphere at the first workshop of this cluster conducive to encouraging such cooperation in order that policy in this area can move forward. If the global financial crisis has taught us anything it is surely that we, as central bankers, have a duty to preserve financial stability. Otherwise the costs for the real economy and, ultimately, our fellow citizens are significant.