DEBATE

Jean-Claude Trichet, former President, ECB

We will now have another round of questions. Mr Ambassador, you have the floor.

From the floor

Thank you very much. I would very much like Benoît Coeuré to say a few things about the resolution mechanism because, after all, if only supervisory mechanisms are put in place we would find ourselves in a very delicate and perhaps even dangerous situation. If we got a supposedly efficient supervisory system underway to go through the asset quality tests and the stress tests and so on you might not know exactly and precisely what to do about a problem, possibly a very big problem, identified through this supervisory system.

Negotiations are underway, and hopefully they will achieve results, but there is one specific aspect that intrigues me. You mentioned that in the supervisory system there is a distinction between the 130 or 140 banks that are directly supervised and the others where the ECB can go in, if I understand correctly, at any point in time and insist on direct supervision. How will this be constructed in the resolution mechanism? Will you have the equivalent discipline there so that you have an authority for the European resolution mechanism to go in directly for the 130 banks and you could do the same for the rest of the banks? That particular aspect seems quite important to me. It would also be interesting if you could say something in regard to a deposit guarantee system being envisaged in the original scheme of things at the European level. I know there is massive resistance to that. How do you see that? Can the system function properly with deposit guarantee schemes remaining at the national level? Thank you.

Renaud Girard, journalist, Le Figaro

We have never had as much liquidity in Europe as after the kind of quantities easing done by Mario Draghi with EUR 1 trillion into the bank and three years at 1% interest. Though we have that, all middle- and small-sized companies that I have come across in France told me that it did not improve the capacity to borrow money. It goes to the big companies, but it does not go to the middle- and small-sized companies. Why does it not do so? I would just like a very simple answer to that. Thank you.

Carlos Perez Verdia, Mexican Foreign Ministry

Mr Belka is wrestling with the question of how the ECB or the banking union will face future crises. I am still trying to figure out what a banking union would mean for the past crises, i.e. would the response have been different. What does a banking union imply for the ECB as a lender of resort and will it be easier for national governments to point the finger at the ECB and say, 'It is your problem now'?

My second question is whether there is a difference of going into the banking union under the current asset and liabilities of the ECB, i.e. different banks from different countries have assets and liabilities with a very large unbalanced balance sheet. The last time I looked at the balance sheet you could easily see German creditor banks vis-à-vis the ECB and you could see all the other countries that were in trouble. If you go into a banking union under these conditions does that make the future harder for the ECB?

Jean-Claude Trichet, former President, ECB

Those are very good questions indeed. As regards the size of the balance sheets of the system, the full system not just the ECB, you know that it is much lower as a proportion of GDP than in the other large advanced economies such as Japan, the UK and the United States of America.

Steven Erlanger, New York Times

Thank you, Jean-Claude. Perhaps this is a naive question, but clearly the banking union is a response to a crisis and it was designed to fix a hole, but the hole sits there like an unexploded bomb, to mix metaphors. There is a huge amount of debt of a variety of collateral, some of it good, some of it bad. The ECB has decided it is all good, or maybe that is unfair. I would like to get a sense of the size of the problem this is intended to fix. In other words, is it a prophylactic or is it a real act that will cure something? Also, I would like to get a sense of where in the end Germany has come down on this issue. Thank you.

Jean-Claude Trichet, former President, ECB

Thank you very much indeed. Those questions are all very interesting, stimulating and pertinent. You have the floor.

Benoît Coeuré, Member of the Executive Board, ECB

These are all good questions. I may not fully address the questions about the size of the ECB's balance sheet and liquidity because those issues are linked to unconventional monetary policies which will be discussed in the next session.

On resolution, we certainly need a single resolution mechanism. Otherwise incentives remain partly local. The only way to fully disconnect the incentives surrounding a bank from the national environment is a single resolution mechanism. Mervyn King was quoted saying that banks are global in life and national in death. That is very true and relates to what you said on international coordination. We should have banks that are global or European in life, whichever suits the shareholders, but that are European and not national in death. That is the definition of the single resolution mechanism. The ECB's view is very clear that the single resolution mechanism should be a European authority and it should be efficient in the sense that it should be able, as with any resolution authority, to wind up a bank within a weekend, which puts some constraints on the governance of the mechanism. It should be able to make decisions very quickly.

There should also be a single resolution fund which should be funded by a levy on banks, but we know that it may not be enough to start with because you need to build the fund up, so there is a need for a fiscal backstop. The ESM, the European Stability Mechanism, is ideally suited to provide that backstop. That may seem like a very complex mechanism, but that is exactly how the FDIC works, which has a fund and a backstop from the Treasury. ESM is the closest thing we have to a European treasury in terms of current organisation. However, this ESM backstop should of course be temporary. It should then be recouped from taxes on the financial system.

It is still somewhat of a fiscal union, and this relates to what Marek said about banking union being something of a substitute for fiscal union. It is very important to understand that the single resolution mechanism as such does not create liabilities for taxpayers, and it should not because any fiscal backstop should be recouped by a levy on the banking sector. However, is a common tax on the banking sector not already something of a fiscal union? It is a common tax, so it goes some way in that direction.

What is the state of the discussion taking place in the Council among finance ministers? It seems that it is going in that direction with an agreement to have a single European resolution board, which would be an authority, and then decisions would be formally taken by the Commission. For legal reasons that I will not dwell into, you cannot create a new institution like that within the existing treaty, so it has to be the Commission, but with all decisions being prepared by this resolution board. What is less clear is what will happen with this fiscal backstop, i.e. the discussion in connection with the ESM. That is really a fiscal issue so it is in the hands of the finance ministers, and I appreciate the political difficulty. That is certainly not for the central bank to decide, but I think I have been clear that we believe that this backstop is needed.

On the deposit guarantee scheme, it is true that a fully-fledged banking union should include a single deposit guarantee scheme. It is a much more complex discussion, so it will come later. It should be the third pillar of the banking union. What we have now is an agreement in the Council on a directive to harmonise the national deposit guarantee schemes. That agreement also makes sure that those schemes are pre-funded, which is not currently the case in all European countries. I am pretty sure that it will come. Let me note however that the new bail-in rules that are written down in the bank resolution and recovery directive make the single deposit guarantee scheme a bit less important since they impose on banks a sizeable minimum loss absorption capacity. . It is still important, but they relieve a bit of the potential burden on the deposit guarantee scheme.

On SME lending, it is an important question. SMEs face tighter credit conditions in all Eurozone countries, although that situation is less acute in France. The issue still exists in France, but it is much more acute in some other countries. You can see that in the ECB surveys on lending to SMEs. It is not an easy discussion in terms of what monetary policy can do because there is a mix of factors. There is economic risk. There is no reason why the rate on a loan to a Portuguese SME should be the same as that on a loan to a German SME. The economic risk is not the same. We therefore cannot aim to equalise lending risk to SMEs throughout Europe. This will not happen.

The element of economic risk may have to be subsided in some way with guarantee schemes, but again that is a fiscal discussion and beyond the reach of the central bank. This has to be done by public development banks at the national level or at the European level by the EIB. There has been thought at the EIB on stepping up guarantees to SME lending.

What we can do as a central bank is to provide the liquidity, provided that our risk criteria are met. For instance, we have agreed with the EIB and the Commission that on schemes where they would sponsor ABSs of loans to SMEs with an element of guarantee with EIB money and Commission money we would then be prepared to take some tranches – the senior tranche and maybe even the mezzanine tranche – as collateral to ECB lending, and recognize the public guarantee. That is an allocation of tasks where capital is provided by the fiscal authority, as it should be, and liquidity is provided by us. We are working on schemes like this.

Finally, regarding the extent of risk in the banking system, this is precisely why we are doing this comprehensive balance sheet assessment. We want to know the answer to that. You will know more in the course of 2014 when we will have run through the three pillars. The risk assessment will come first. The asset quality review will follow and then the stress test will be done. Only then will have the full picture of what is going on arrived at through a consistent methodology.

I fully agree with you that we are not addressing the underlying risks, meaning public and private debt. This has to be addressed through other means. That means in particular achieving more balanced budgets and bringing down the level of public debt. This banking union does not achieve that. This is an entirely different discussion. We are not curing that disease at the root. This has to be achieved through different mechanisms.

Jean-Claude Trichet, former President, ECB

Would you address the question about Germany?

Benoît Coeuré, Member of the Executive Board, ECB

Germany has agreed to the single supervisory mechanism, as all EU countries have. I see a lot of support from the German authorities, both the Bundesbank and the BaFin. They are very supportive. They want to send us their best people. They want to be fully onboard. They are very much involved in this process of setting up the single supervisory mechanism, which incidentally will be based in Germany, in Frankfurt, as part of the ECB. On resolution, it is again a political discussion but we see elements of an agreement in the Council that includes all member states.

Jean-Claude Trichet, former President, ECB

Thank you. Marek, would you answer some of the questions?

Marek Belka, President, National Bank of Poland

No, none of the questions were addressed to me.

Jean-Claude Trichet, former President, ECB

Maybe all questions are for you. Thank you very much. Do you have a last point?

Benoît Coeuré, Member of the Executive Board, ECB

I have a message for Marek actually, which is that the SSM, the single supervisory mechanism, at least initially is Eurozone only, so that is 18 member states. It is very important to us that anything we do does not contradict the single market. That is an obvious legal requirement and the Commission is very keen on achieving that, but they are right. We have a single market for financial services and we have seen a lot of capital market fragmentation which has many negative consequences. One of the negative consequences of fragmentation is that it is harmful to the single market and the single market has enormous economic benefits, so we want to keep that single market up and running and we therefore have to make sure that the single supervision does not create fragmentation by itself in the single market. We will have to cooperate very closely with non-participating countries to achieve that.

Jean-Claude Trichet, former President, ECB

Thank you very much. We will take the last question now.

From the floor

If the German Landesbank, which is not one of the 130 directly-supervised banks, turns out to be in deep trouble when you go through the supervisory method would that be resolved through the common resolution mechanism or would it be left for the national system to resolve?

Jean-Claude Trichet, former President, ECB

They would probably be able to solve the problem at their layer and it would not be necessary to go to the ESM. That is the working assumption.

From the floor

It could, however, be a number of such banks in a similar situation simultaneously and it could be a bigger problem than just one bank.

Benoît Coeuré, Member of the Executive Board, ECB

That is part of the discussions that are taking place now. We would of course like to achieve maximum consistency with ECB supervision. What is important is that all banks, including the smallest ones, will be bound by the bank resolution and recovery directive. That already goes a long way to harmonising the methods both in recovery and in resolution. This was agreed this week and this covers all EU countries and banks that fall under the Commission’s vigilance, particularly in terms of state aid. This will already force a lot of consistency in the way bank failures will be addressed.

Jean-Claude Trichet, former President, ECB

Thank you very much indeed. This is now really the last question.

From the floor

I have a very short question. Concerning the asset review how would you assess the credit risk associated with government bonds? Are those risk-free assets?

Benoît Coeuré, Member of the Executive Board, ECB

I was surprised that that question was not asked earlier. It is very simple. The asset quality review is a snapshot and it is a way to very thoroughly audit the level of capital under the regulatory standards. It is under current European law, namely the capital requirement directive ("CRD4"), which is the way Europe has enforced Basel III. There is a zero risk weight for government exposure in the CRD4. We have no margins in the AQR to put a different weight on or to have a different risk weight for sovereign exposure because it is under CDR4 and as the supervisor we are not mandated to change the law, and we should not be. What we can and should do – and what I am pretty sure we will do – in the stress test, which is a different kind of exercise because it is about scenarios – is to stress all of the items on the balance sheets of the banks, including sovereign exposure. However, it is a different exercise with different supervisory consequences.

Jean-Claude Trichet, former President, ECB

Thank you very much. Yes, Marek, please go ahead.

Marek Belka, President, National Bank of Poland

If you are interested in this issue and would like to dig into this question more, look at the December BIS quarterly review. There is a box on pages 10 and 11. It is sometimes asserted that the Basel capital framework prescribes a zero-risk weight for bank exposures to sovereigns. The guys from BIS tell us this is incorrect. Basel II and Basel III call for minimum capital requirements commensurate with the underlying credit risk and so on and so forth. You can read there that they say this is a matter of false interpretation. It is not the rule.

Benoît Coeuré, Member of the Executive Board, ECB

That is a very important point from Marek and I fully agree. That is why I spoke not of Basel III but of the way Europe has enforced Basel III, which are two different issues. If there is a discussion about the risk weights for sovereigns for capital requirements it should take place in Basel as an international forum and there is room for it within Basel III, as was just said. It is just that it has to be discussed at the international level and, frankly, I see no reason why we should treat, say, Portuguese, Slovenian or German bonds differently to US or Japanese bonds both from a conceptual point of view and, I would even say, as a matter of principle.

Jean-Claude Trichet, former President, ECB

Thank you very much. I noted that you had said that the decoupling of the credit-worthiness of the banks and the credit-worthiness of the state was of course reliant on banking union itself and also on the good management of the countries themselves. You will remember we have a new governance structure with the SGP and the MIP and I understand you reserve intense cooperation if needed with the Commission on the MIP, which directly impacts macroeconomics in the countries.

A second point is that we should not forget that Germany is an exemplary parliamentary democracy, so whatever decision has to be taken you have all the pros and all the cons because everything is discussed by the Bundestag and the Bundestag decides, not the executive branch. That makes a difference compared with a number of countries where decisions are made at the top by the executive branch and the parliament follows suit. That is the case in my own country and it would be the case in the UK and in many other countries. That is one of the reasons why global observers are regularly very surprised because they read about all the cons in their papers, which is all the papers find interesting, but the decision which is ultimately made is positive rather than negative. Observers are very surprised by that, but again I think it is because the interaction between communication in the press and the exemplary parliamentary democracy of Germany makes that a permanent feature.

Another point I would like to make is that it is not surprising, Marek, that it is difficult to get a bank which would be obviously a multinational in Europe when you do not have such multinationals apart from EDS. EDS, of which I am a director, is the only real multinational in the industry in the manufacturing sector that you have in Europe. All the others more or less have headquarters based in one of the other countries, even if many of them are fully pan-European or fully global. I think therefore that we should not necessarily say that the banking sector is a disgrace because we do not have dozens of EDSs in that particular sector. You had a point because you experienced the behaviour of your banks in a crisis situation in your own capital, so I take your point as a very, very important one, but I think we should not necessarily put the goals too high. I know, however, what you have observed, which was a disgrace, so I fully agree with you.