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Not yet safe and sound

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The credibility of our Banking union is at stake unless serious problems, in including Deutsche Bank and the Italian banking sector are fully and urgently addressed. What is needed, in political terms, is that Member States fully commit to a proper clean-up and recapitalisation of bank’s balance sheets - even and especially when it comes to their own national champions. We should be honest and admit that a degree of consolidation in Europe’s banking sector is unavoidable. Not all banks in Europe have sustainable business model and it is precisely those banks without viable business models that do most harm to the real economy and financial stability as they gamble for resurrection, misallocating capital on a grand scale and posing a permanent danger to taxpayers.

To address the too-big-to-fail problem, a reversal in the burden of proof for major EU banks should be introduced within the framework of the Banking Structural Reform. Such banks would need to demonstrate to the satisfaction of regulators that the risks in their enormous and highly complex balance sheets are under control rather than regulators having to uncover the hidden risks in the haystack of those balance sheets. In case of disagreement, this reversal of the burden of proof would materially strengthen the position of the regulator in court. Should major banks fail to convince their regulators, they should either be required to increase their capital significantly or be split up.

In this context, we welcome the Basel committee’s proposal to rely less heavily on internal risk models of banks. Unsurprisingly, the lobbyists of the sector are up in arms against this. We would hope, however, that the Christian democrats can free themselves from the grip of the sector’s special interests. Instead, it must be our common goal to reconcile increased capital requirements for a safe and sound banking systems with the specificities of Europe’s bank-based financing model and to address the problem of sovereign risks on bank’s balance sheets in a way that is properly tailored to the requirements of our common currency. In addition, we should use upcoming European legislative files to make sure that banks hold sufficient subordinated and bail-in-able debt to allow for a bail-in of debt instruments as set out by the rules of Banking Union.

Unfortunately, all of still won’t be enough in case of a major market panic. In a crisis situation Europe needs to be in a position to address problems as they emerge even over a weekend. Unfortunately, the European decision-making procedures are still too cumbersome and the European bank resolution fund is still too small to deliver on this objective.

The problems of Deutsche Bank are a wake-up-call against the Siren songs of the banking lobby claiming that economic growth will resume if it wasn’t for cumbersome regulation and capital requirements. In reality, the opposite is true: one important reason for the chronically low economic growth in the Eurozone is precisely that we failed to clean up our banking sector swiftly and thoroughly.