Banking Union for All of Integrated Europe

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A banking union for all?

Premise: A Eurozone-based banking union is a good idea to save the Eurozone.

Question: But is it attractive for non-EZ countries?

Current proposal:

1. Single supervisory mechanism for Eurozone banks controlled by ECB
2. This mechanism would provide access to the European Stability Mechanism (ESM) to recapitalise banks directly
3. Non-Eurozone countries could join the mechanism, but would not have access to ESM
4. No common resolution authority or common deposit insurance for now.

The answer from an EME host perspective

Banking union can be good idea, provided that:

- Incompleteness of current proposal addressed or at least mitigated
- Non-eurozone members of the European financial area offered reasonable deal that also works for the Single Supervisor/ECB

What worries EME host countries?

In the Euro Zone

1. Loss of supervisory control to an ECB that might not care enough about national (as opposed to EZ-level) financial stability
2. Coordination problem in resolution not addressed
3. Sharing fiscal responsibility for crises elsewhere

Outside the Euro Zone

1. Tilting of playing field against local stand-alone banks without access to ESM "shield" (subsidiaries of Eurozone banks can, via parent).
2. Problems of governance of cross-border banks not addressed (supervision, resolution …);
3. Even less influence over just one, large, home supervisor (the ECB)?

What incentives for the “outs”?

1. A governance structure that gives small countries sufficient voice in determining systemic risk

2. Underpin “trust” with insurance:

   - “Escrow” part of bank group capital for subsidiaries
   - Allow local authorities to impose additional macro-prudential buffers

3. Cross-border stability groups (ECB, home authorities including finance ministries and host authorities) work out rules for burden sharing and crisis management ex ante (following NBSG model)

4. A first loss sharing rule that mitigates moral hazard

   - ESM should be primarily about catastrophic loss insurance.
   - National government can influence costs of banking crises: resolution, but also housing policy, fiscal instruments ….

Extending the banking union to non-EZ countries

1. Full membership: allow opting in
   - Legal obstacles (ESM treaty)
   - But no conceptual obstacles: non-EZ members contribute to and benefit from first loss sharing mechanism; extend swap lines.
2. “Membership lite”
   - No membership in ESM or single supervisor
   - But ECB liquidity support (swap lines) in exchange for ECB surveillance over local supervision.
3. “Trade supervision rights”
   - ECB gets a supervision role over subs, in exchange for host supervisor getting a voice/information access in supervision of parent.

Next step : identify list of conditions for opting in

1. By host countries
2. By the ECB
3. Key input from bank groups