The Union's financial market as an element of a stable monetary union?

Speech by Jörg Asmussen, a member of the Executive Board, Handelsblatt Conference "Banks in Transition", Frankfurt am Main, 4th September 2012

Ladies and Gentlemen,

A phrase in the final declaration of the Euro Summit of 28 June this year caused a listen and much discussion over the summer - and I quote: " *As soon as the involvement of the ECB an effective single regulatory mechanism for banks in the euro area has been established, though the ESM recapitalize after a proper decision on the possibility of banks directly .* "

Here is the beginning of a financial union was decided. As a contribution to this discussion, I would like to take up in the following three aspects:

1. Where we stand on the regulation of financial markets? So what does currently represent the state of financial markets?
2. Why a Union financial market has become necessary? How should it look like?
3. What role can the ECB to come within the new supervisory architecture, what conditions must be met?

Where we stand on the regulation of financial markets? What is the situation in the financial markets?

Since 2008, the leaders of the G20 have repeatedly adapted to a common approach for more and better regulation. There was consensus on a key lesson of the crisis should be that all systemically important institutions, markets and instruments are properly regulated and supervised. Europeans increased their efforts to develop a so-called "single rule book", by a variety of regulations and guidelines, more than a dozen since the crisis began. That the designation of which is usually a veritable alphabet soup - CRD IV, MiFID, EMIR, etc. is an indication that the matter is highly complex.

The first three G20 summit of leaders in Washington, London and from all Pittsburgh have produced in the regulation of financial markets is far above average results, other summits have in other areas can be successful, for example, the Seoul Summit in the IMF reform. Meanwhile, the G20 process has also lost respect to the regulation of financial markets to drive. We must strive, the lost "drive" to recover. The accumulation of at least individual misconduct in major financial institutions shows that a sharp adjustment is necessary because either the external or internal control oversight did not work. I am now more convinced of it than ever before. It applies in principle in law states the presumption of innocence, but if the allegations prove true, should be the impact of LIBOR manipulation is far from his sight.

The monitoring of the Financial Stability Board (FSB) shows that many national legislators are overloaded given the plethora of new financial market legislation and in the implementation of time-lag. The European Union is confronted with the challenge of "the same rules - uneven implementation" confronted. Despite the great efforts made by the European Banking Authority (EBA), the approach suffers from the "single rulebook" under a different implementation. The new legislation - such as the Directive and Regulation on improved capital requirements - leaving national regulators considerable discretion.

Many of the new financial market regulations are very complex. Rightly so we can ask the question whether the high complexity of the regulation does not lead to lack of transparency and uncertainty for market participants, and therefore achieved with respect to the financial stability, the opposite of what should be achieved. Simpler rules would not be a better alternative? This question is for example Andrew Haldane of the Bank of England followed up in a research paper, which he presented a few days ago in Jackson Hole. I use briefly below his findings.

If one side of the scope of the regulation as a measure for the complexity of the rules takes what is certainly an oversimplification, but gives a good first indication, then it is as follows: Basel 1 was 30 pages. Basel 2 and Basel 3 350 pages already has 620 pages. There are also thousands of pages of regional and / or national implementation. Haldane comes through empirical analysis, not only by page count to the conclusion that simple rules are not less effective than complex.

Of course I know that simpler rules often violate the so-called fairness in individual cases. I know also that the complexity of the rules is often due to a successful lobbying to find a specific business model for a suitable solution. But I think the fundamental question of Andrew Haldane properly, and will continue to think about it.

Currently, the situation is in the financial markets is as follows: We are seeing in the euro area a process of fragmentation of the single financial market, it will be held re-nationalization. For example, the share of cross-border loans in the money markets between mid-2011 and has dropped from 60 percent to 40 percent. In several countries, foreign bank deposits have reached their lowest level since early 2008. Banks are increasingly using domestic security in access to ECB facilities.

The core of this - figuratively speaking - reconstruction of the barriers is the strong financial links between individual states and their banking systems. Lack of confidence to the banks in the Member States concerned also leads to a strong dependence of some banking systems of central bank liquidity.

This downward spiral has decisively contributed to the situation has been in the financial markets for the euro area since the middle of last year again. The risk premiums on government bonds reflect now reflect not only the risk of insolvency of individual states, but also an exchange rate risk, which is in a monetary union should not exist theoretically. The market prices ie a breaking apart of the euro area.

For a monetary union such systemic doubt unacceptable. Only one currency, to their constituents, there is no doubt, is a stable currency. After all these doubts have serious consequences for the common monetary policy: a monetary policy signal, as the ECB has set example with the interest rate cut in July comes, inconsistent or in part at all in the real economy.The ECB yesterday published data showing that impressive: So pay small businesses in Spain for a loan of up to EUR 1 million and a maturity of more than one and up to 5 years is currently 6.5% interest, as much as ever since 2008. In Italy there are currently 6.24%, while the same corporate credit in Germany can be had for around 4% with no increase in interest rates.

The fed funds rate, the "lead" is actually supposed to do, this is only limited.

Second Why a Union financial market has become necessary? How should it look like?

Despite the fragmentation of European financial markets, we are seeing recently, and the one I just described, the development has been shown since the banking crisis of 2007/2008 in Europe above all: the banking sector in Europe is often so intertwined with the state funding that problems in one area can lead to contagion in the other area, both to waver and to develop pan-European problem, to be solved not within a Member State, because the funds are lacking and there are structural weaknesses.

The problem cases are known to you: In Ireland, the government jumped the oversized financial sector to the side and then became even stumble, like we're seeing now in Cyprus.

In Greece, we found the reverse situation. Ailing public finances weigh heavily on the domestic bank balance sheets because the buyers were mainly Greek banks on Greek government bonds. Subsequently turn the state funding is more difficult because the local banks can no longer absorb the bonds.

Spain has been in the financial crisis, often praised for that supervision will be successfully able to prevent the conflagration through to complex, structured products. Non toxic assets have been a problem for Spanish banks, but the bursting of a housing bubble and many classic implicated were Spanish savings banks, which now support the regions and the Spanish central government heavily burdened.

In addition to this fatal link between banks and states the crisis has raised the general question of what weight considerations for financial stability in Europe, when the overseer is part of the national executive and thus primarily responsible to a national parliament and ultimately to the national taxpayer .

We have seen in recent years, can that individual interests may be in conflict with the interest of financial stability in Europe.

If financial stability is at risk in all of Europe, then we should find a common European response to this, and the answer is: we should create a financial union.

This brings me to the question: How would such a financial Union? The new architecture should be at the end of the process include the following three pillars:

- First, a European Banking Supervisors, which has adequate tools and skills. You must ensure a uniform implementation of European rules. These banking supervision must also be able to close non-viable institutions and over for execution.
- Secondly, a European resolution authority and a single set of rules for handling unstable systemic banks. This authority must in case anything goes to a fund financed by the financial services industry. This prevents that national budgets and taxpayers will be charged.
- Thirdly, the deposit guarantee will be organized at European level or at least further harmonized.

All three elements are interdependent. Imagine a three-legged stool in front: Missing one leg, the stool falls over. Banking supervision can only act effectively and meaningful if they. Also have complete information, for example, has on deposit insurance and they can only operate effectively if it can order such as the settlement of an institution What good is a fire alarm when disengaged in case of emergency can not fire, or the fire department does not know what really burns.

In addition, consideration should be given to extend the competence of the Union financial market to another area. I am thinking particularly of central market infrastructure such as central clearing houses (Central Counterparties - CCPs).

The creation of a single banking supervision for the euro area is an absolute prerequisite for a direct recapitalization of the banks by the European Stability Mechanism (ESM). This linkage between the funds and control is essential.

Third What is the role of the ECB within the new regulatory architecture?What conditions must be fulfilled

But the role of the ECB is now within the new regulatory architecture? In one week, on the 12thSeptember, the European Commission will present its legislative proposals for a European bank supervision. Some details of the proposal through an interview by Commissioner Barnier in the Süddeutsche Zeitung already become known. It wants the ECB to play an important role in a European Banking Supervisors.

The ECB, together with the national central banks already confirmed that it is willing to take on responsibility as a regulatory body.

This has met with some incomprehension. Some argue that a central bank should always stay out of supervision of individual banks. Too large is the conflict of interest, for example, obtain a business partner of monetary policy operations alive, although a settlement would be necessary.Others fear a concentration of power at the ECB as a European super-authority.

We are well aware of these concerns. Therefore, the ECB will take over responsibilities for the supervision only if certain conditions are met:

- First, the primary objective of price stability will remain untouched. Monetary policy needs of the banking supervision to the outside and inside are separated organizationally and in terms of personnel. Means to be Chinese walls and the creation of a new decision-making body in addition to the Governing Council, which is responsible for all oversight responsibilities. The fact is that today 14 of the 17 national central banks of the euro area have supervisory responsibilities.
- Second, the ECB will ensure that their independence is in no way can hamper. Same time it is clear that functions of banking supervision must be under the parliamentary and judicial control. For banking supervision is sovereign action, action can be taken in by the fundamental rights of the persons concerned. We have the necessary accountability of European Banking Supervision at the ECB with an open mind. This applies both to the European Parliament, including with respect to the EU Council of Ministers.
- Third, the law must provide the ECB with all the tools that are necessary in order to exercise the functions of a bank supervision effectively. It must be possible for the ECB to take advantage of the wealth of experience and the technical expertise of the national central banks. Because it is clear that many supervisory tasks can only be performed tomorrow on site. At the same time a uniform implementation of European directives can be ensured. Of particular relevance is the direct access to all necessary information on the regulated institutions, such as audit reports on audits of banking operations and analysis on financial statements. The ECB must also have sufficient rights to intervene and, as already mentioned, have the right not to close viable banks if necessary. Without this

minimum configuration, the ECB will take no responsibility, in my view, because the risk to the reputation of the institution would be too great, the reputation risk lies solely with us. Until the implementation of the Commission's proposals must include these aspects a number of important design issues are clarified.

- How would the division of responsibilities between the ECB and other European regulators - in particular the European Banking Authority (EBA) - look like? It would be possible, in my view, that the EBA is to further develop the "single rule book" in the internal market of the EU-27 still in charge.
- Will European Banking Supervisors oversee only the banks of the euro zone or the whole EU? A functioning financial market Union is primarily a concern of the monetary union. From this perspective, would be a useful focus on the institutions of the euro area. Non-euro countries but it should be free to their institutions also to be placed under European supervision.
- Will it go to banks of all sizes or just to the systemically important? In my personal view, it makes sense to limit at least initially the European view of Europe and the national systemically important institutions. At the beginning of 2013 to organize an oversight of all euro area banks is neither purposeful nor represented. It is important that the European supervision is operational to efficient supervision from the start in the position as well.
- What is the division of labor between the ECB and the national authorities? In the operational division of labor, we face a key challenge. Firstly, the local expertise be safely used. At the same time, however, must also be a uniform supervisory standards throughout the euro area is guaranteed - not least in order for the banks themselves, the system is not further complicated. This could be achieved if each institute a mixed supervisory team of national and European experts would be formed. This team could also act as a single contact to the bank. European supervision should have the opportunity zurückzudelegieren the daily supervision of smaller banks to the national authorities. Individual cases but it would have easily again can attract. Although the ESM must as soon as possible to be able to recapitalize banks directly. But it is also about making things right, and not to lay down under pressure half-finished solutions. I would also remind you that a Union financial market alone can not solve the crisis. Even a perfectly established financial Union could not ensure that the Greek budget comes into balance and the increased competitiveness of Portugal.Because the reasons for the crisis are to be found in the areas of common fiscal policy and economic policy. Europe must decide now. Either we complete the integration of the euro area, by at financial market policy, fiscal policy, economic policy and democratic control share sovereignty with Europe. Or we choose the other way, a decentralized Europe. This then means also that we are the major economic benefits that have brought us to monetary union and the single market, gamble with. To avoid this, we should complete the architecture of Economic and Monetary Union. In addition to the financial market Union, three other components are essential:

1. A fiscal union
2. A genuine economic union
3. A legitimate political union

These four blocks go together and are interdependent. Advances in only one of the four areas will not be enough, all four aspects for the functioning of Economic and Monetary Union, are essential to the future of a stable euro.

My answer in this situation is clear: More Europe, a better Europe. But not as an end in itself.But as the way the European citizens prosperity, freedom and security in the globalized world of the 21st Century secures.

Ladies and gentlemen,

Your conference is themed "Banks in Transition." The institutional architecture of the euro zone is currently "in transition". In order for this "break" a "departure" is, to a more stable, prosperous and depressed monetary union, we need a broad discussion - here and now equal with you. I look forward to.

Thank you for your attention.