

Banking Union as a means of strengthening EMU

Policy Brief no. 6

October, 2014

ISSN 2014-7457

The effects on the eurozone of the crisis unleashed in the US in the summer of 2007 have revealed not only latent macroeconomic imbalances in some economies forming part of the Monetary Union (EMU), excesses and malpractice on the part of some of its economic agents, but also limitations in the original design and structure of monetary integration itself.

Today there is a broad consensus on the need to consolidate EMU through a greater fiscal integration and a complete banking union. While only minor progress has been made in the former aspect, steps of certain significance have been taken in the latter, to the extent of that in the current year and the next their main elements will come into operation.

The aim of this Briefing is to describe the structure and functions of the Banking Union and to analyse its contribution to the fundamental aim of improving EMU. It will also analyse the conditions necessary for its launch to contribute to the definitive elimination of the risks associated with the perverse linkage between sovereign debt and banking stability, so that it should never again be the taxpayer who pays most of the cost of banking crises.

Though it has moderated, that vicious circle continues to exist. The prices of public debt have improved notably, but this was not due essentially to significant improvements in economic fundamentals, but to the ECB's actions, or readiness to act, in ways similar to those already taken by the Federal Reserve and the Bank of England. In reality, concerns about the adequacy of capital in banking systems have not disappeared. Nor have the signs of financial fragmentation within the eurozone, especially those reflected in the unequal treatment meted out to business borrowers in different countries in the eurozone. The elimination of these obstacles are

necessary conditions for the consolidation of the economic recovery, and this should form part of the design and implementation of the Banking Union for it to be sufficiently credible.

1. The banking crisis in the eurozone and its linkages with public debt

For a more complete vision of the impact of the crisis in the eurozone, it is necessary to start from the features that characterize the area, in terms of both its macroeconomic imbalances and those of a structural nature. Among the latter, a key aspect is the configuration of its financial systems, in which the commercial banks have a much higher weight than in the anglo-saxon financial systems, which are more dominated by direct financing, based on the markets.

1.1. Banking penetration in the eurozone. Indicators

The malfunctions that the crisis has originated in the banking systems of continental Europe are more significant, and have a greater impact on the real economy, than in other economic zones, given the degree of "banking penetration" of the eurozone, as highlighted in various works, among others ESRB (2014) and Berges and Ontiveros (2014). European banking systems are excessively large compared with the size of their economies or with other indicators such as household income and wealth. Of course, they are also too dominant in comparison with other forms of financial mediation, such as those provided by bond and equity markets. Moreover, in the past decade the eurozone's banking systems have grown more than those in other advanced economies, increasing their prominence in the provision of credit at the same time

as they have accentuated a trend of concentration around large banks which, as shown in those works, have similarly increased their leverage ratios. In short, since the start of this decade, Europe has increased its vulnerability to possible banking crises. In any case, the increase in the degree of concentration does not facilitate the management of crises which end up forcing the authorities to rescue banks with public funds, as this crisis has shown.

As can be seen in Table 1, which illustrates the structural characteristics of the EU's banking systems, the size of the eurozone banking sector means that it is extremely important. Eurozone commercial banks channel a much higher volume of financial assets and liabilities of families, companies and Public Administration than the banking systems of the US or United Kingdom. In the latter two economies, business financing is less dependent on bank finance, as reflected in Table 1, which shows the split in the funding of non-financial companies between bond

issues and bank loans. This is indicative of a lesser development of direct financing markets in the eurozone. In reality, that difference between the financial systems of the eurozone and the US has deepened in the past decade. This magnifies the importance of any anomaly in the functioning of the banking system of continental Europe, or any modification in its structure, for the economy as a whole.

The available evidence (Véron, 2013) also highlights the existence of a correlation between the development of non-bank financing and resistance to systemic risk in the advanced economies. The recent experience of economies such as Spain, where small and medium companies are almost totally dependent on bank finance, is sufficiently illustrative. The importance of that dependence on bank finance has been increased by the reduction of the number of banks during the crisis.

Table 1. Structural characteristics of the EU banking sector

	Relative size of the banking system ¹	Total assets / GDP (%)	Credit to the private sector / GDP (%)	Concentration (%) ²	Branches / Million inhabitants	Foreign penetration (%) ³
Germany	17,4	284	97	33,0	451	5
Austria	2,7	379	112	36,5	530	9
Belgium	2,4	279	75	66,3	344	38
Bulgaria	0,1	106	71	50,4	523	71
Cyprus	0,3	636	326	62,5	1005	85
Denmark	2,1	376	199	65,6	252	4
Slovakia	0,1	78	50	70,7	196	85
Slovenia	0,1	139	85	58,4	338	53
Spain	8,9	377	160	51,4	815	59
Estonia	0,1	119	77	89,6	132	81
Finland	1,4	311	99	79,0	260	26
France	15,7	335	106	44,6	587	18
Greece	0,9	211	118	79,5	326	73
Netherlands	6,2	449	178	82,1	147	70
Hungary	0,2	111	54	54,0	335	17
Ireland	2,3	609	155	56,9	232	86
Italy	6,5	182	112	39,7	548	15
Latvia	0,1	124	65	64,1	196	55
Lithuania	0,1	66	49	83,6	229	81
Luxembourg	1,7	1725	302	33,1	387	91
Malta	0,1	785	152	74,5	256	62
Poland	0,8	88	54	44,4	394	9
Portugal	1,1	300	152	70,0	594	50
UK	24,4	550	155	40,6	184	50
Czech Republic	0,4	116	55	61,5	200	86
Romania	0,2	63	39	54,7	285	84
Sweden	3,7	400	135	57,4	198	8

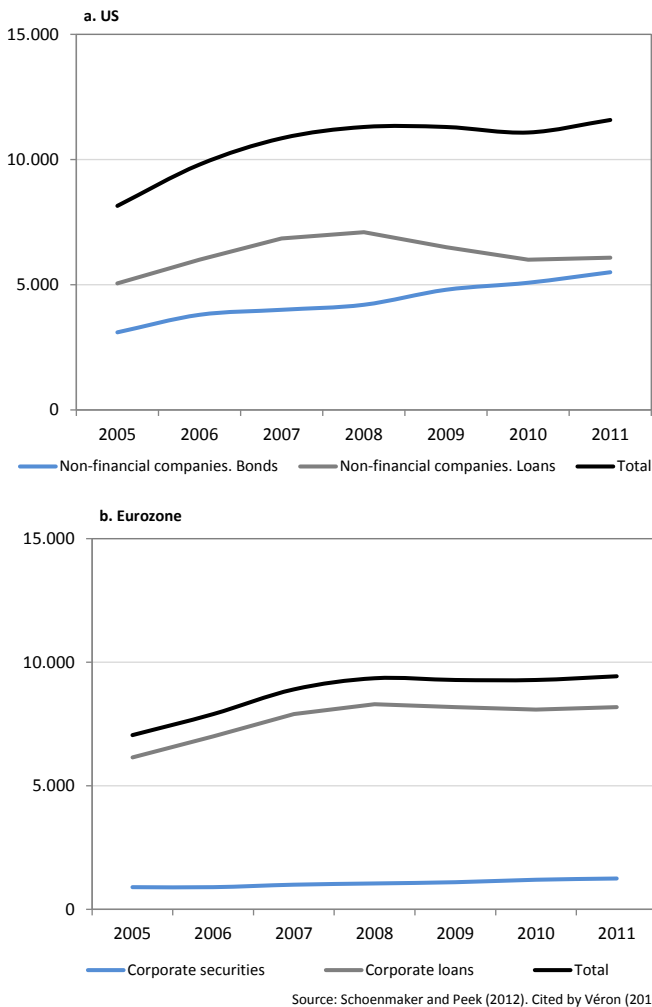
¹. Country's banking assets / Total EU banking assets

². Share of assets of 5 largest institutions by balance sheet

³. Number of foreign institutions (EU and non-EU) / Total institutions (domestic and foreign)

Source: AFI using ECB data (consolidated)

Graph 1. Bank and bond finance (US\$ million)



1.2. The vicious circle

This is the context of the most noticeable impact differentiating the financial crisis in the eurozone from that experienced elsewhere: the generation of a vicious circle between the public debt crisis and the deterioration of bank balance sheets. This feedback between sovereign risk and the corresponding banking risks has passed through several phases, as reflected in Table 2.

The deterioration of bank balance sheets increased the probability of public assistance, which in turn contributed to reduce the quality of public debt securities, in which the main investors were the country's banks themselves. In February 2014, public debt still represented 6% of all eurozone banking assets, compared with 4.3% in January 2012, with the

largest increase due to banks' investments in the public debt of their home countries, which was more notable in the peripheral economies, around 10% in the case of Spanish and Italian banks.

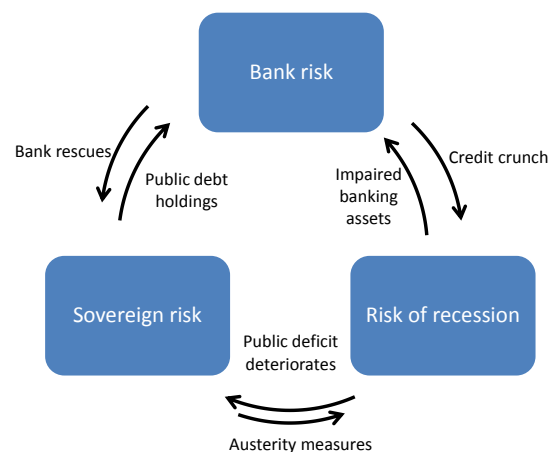
One of the results of these anomalies in the banking systems is the amount of public funds that governments have committed to achieve adequate capitalization of banks, constituting one form of feedback in the above-mentioned vicious circle (Table 3). According to ECB data (2014, p.39), between October 2008 and 1st October 2013 the European Commission authorized more than 400 instances of state aid to the financial sector, involving around €4.5 trillion of taxpayers' money, of which €1.6 trillion has been utilized to save banks in the EU. The European Systemic Risk Board's study (2014, p. 37) updates those figures: between August 2008 and February 2014, the Commission received 440 requests to authorize state assistance, which was granted in 413 cases.

Table 2. Phases of the eurozone financial crisis

PHASE I (2008)	<ul style="list-style-type: none"> States support banks, due to a strong decline in confidence in them: guarantees, almost unlimited deposit guarantees, capital injections, fiscal stimulus packages, etc.
PHASE II (2010)	<ul style="list-style-type: none"> Markets penalize states, assuming that these contingent liabilities may endanger the sovereign's solvency.
PHASE III (2011)	<ul style="list-style-type: none"> Doubts about states penalize their banks, with regard to when debt issuance, their share prices and their capacity to grow their deposits.

Source: AFI

Table 3. The three components of the vicious circle in the current crisis



As the ECB itself emphasizes, the absence of a common mechanism for the resolution of banking crises intensified the destabilizing linkage between banks and the sovereign debt of their home countries. Nor did the successive stress tests on banking systems carried out from September 2009 on contribute to reduce risks. Fortunately, the spiral moderated significantly when the ECB abandoned its passivity and on 26th July 2012 announced that it was prepared to do everything possible to avoid the break-up of the euro, and more specifically in the announcement of its program of OMT (Outright Monetary Transactions) in September 2012, although the other malfunctions in the periphery's banking systems remain, including the lack of credit growth and financial fragmentation (inequality in the conditions applied to similar borrowers of the eurozone).

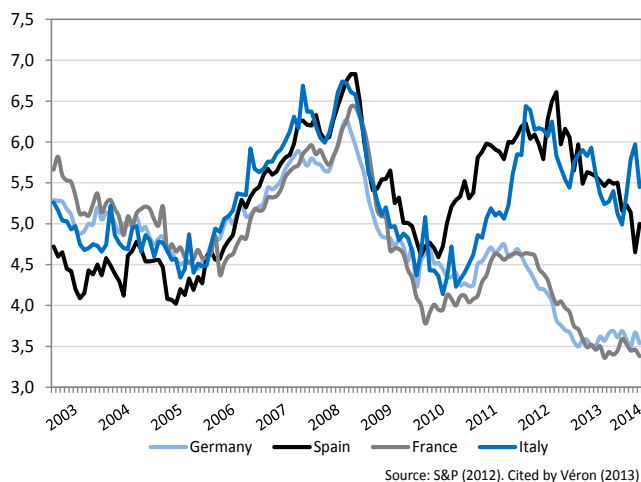
1.3. Rationing and financial fragmentation

Indeed, although the neutralization of that linkage has been the main motivation in the definition of the banking union, the crisis has also revealed weaknesses in the very dynamics of financial integration. In reality, it has weakened it enormously. The credit crunch has been very significant during the crisis in the eurozone as a whole. European Commission data (2014) indicate that, while in Germany 80% of the SMEs that requested a banking credit obtained it, in the economies of southern Europe that percentage fell to 40%.

Other signs have been the situations of fragmentation which persist today, such as the breakdown of the principle of a single price in the different segments of the financial markets, from the interbank market to credit for non-financial companies.

In addition to the contraction of credit in the eurozone as a whole from 2010 on, most noticeably in the peripheral economies (Italy, Spain, Greece, Ireland and Portugal), the variations in final interest rates is a reflection of incomplete financial integration. This has led to a divergence in the competitive fundamentals of the companies in the single market of which the EMU forms part. As can be seen in Graph 2, companies in the European periphery have been much more heavily penalized. The more important their SME sector compared to the eurozone's central economies, the greater the damage they suffer.

Graph 2. Interest rates of new credit transactions for SMEs
Amounts of less than €1 million and a term of 1-5 years (%)



In addition to the above, the abnormal situation of the eurozone banking system was similarly reflected in falls in the market prices of many institutions and, no less significant, in the decline of the exposure of the main banks to other eurozone countries, especially notable from 2010. This generalized "return home" in banking systems after the onset of the crisis is particularly notable within an area intended to perfect the single financial market. This kind of "renationalization" was explicitly reflected in the banks' public debt investments.

2. The Banking Union as a means of strengthening the Monetary Union

The Banking Union (BU) was designed to avoid such malfunctions and to strengthen the architecture of monetary integration. In the acceleration of the transition to that goal, the intensification of the Spanish banking crisis in July 2012 and the terms of the conditionality required in the corresponding "Memorandum of Understanding" linked to the rescue of the sector played an important role. In accordance with the bases of the BU design, European banks, at least those of the eurozone, should be able to count on the same set of rules, the same playing field, if the aim is to ensure a real single financial market. The guarantee of identical regulation and supervision, of sufficient quality, is the way to achieve it. A

complementary goal, the elimination of the vicious circle between the deterioration of banks and that of the sovereign debt, dominant during the crisis, is the most immediate aim.

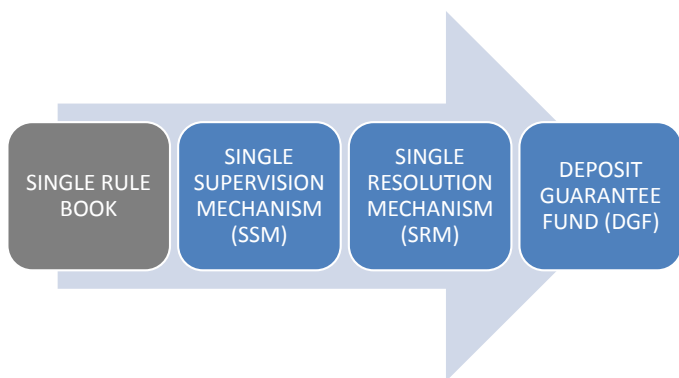
The structure of the Banking Union

In December 2012, the European Council agreed the basic structure of the Banking Union. It would be constituted by the components that appear in Table 4.

2.1. Single rulebook

Although formally the existence of a single banking regulator forms part of the fundamentals of the "single banking market", which would take shape prior to the definition of the scope of the BU, the existence of common regulations constitutes an essential base permitting the two basic mechanisms of the BU to come into play. A single rulebook is therefore the first pillar of the BU.

Table 4. Structure of the Banking Union



Source: EuropeG

The single rulebook is the way to unify the regulatory framework of the EU financial sector, in order to complete the single market of financial products. The most immediate action in this respect is to ensure the uniform application of the Basle III rules. The ultimate aim is to have a truly European banking system with sufficient resilience, transparency and efficiency. The responsible body in this matter is the European Banking Authority (EBA), which is the coordinator of all the national regulators.

The prudential requirements for banks are essential components of those regulations, particularly their solvency and the capital that supports it, together with the guidelines for bank rescues and the resolution of banking crises, which are the essential basis of the Single Resolution Mechanism for crises (SRM), discussed below.

In short, the single rulebook consists of the two essential regulatory components for the operation of the Supervision Mechanism: those rules established in the Capital Requirements Regulation and the Capital Requirements Directive (CRR/CRD IV).

2.2. Banking supervision

The pillar constituted by the Single Supervisory Mechanism (SSM) constitutes the necessary condition for providing uniform conditions for banks' activities and an adequate quality of supervision, without national biases and acceptable without reservations by the international investment community. It was the eurozone summit of 29th June 2012 which demanded that the European Commission prepare proposals for the creation of the supervisory mechanism, as a basic condition for the possible recapitalization of banks. This coincided with the Spanish government's request for a rescue specifically for the banking sector, the first of its kind in the management of the crisis to incorporate a "memorandum of understanding" with extensive conditionality.

The specific regulation of said mechanism was passed by the European Parliament in September 2013 and approved by the European Council on 15th October 2013, coming into effect the following month. It will be a year later, on 4th November 2014, when the ECB will assume its supervisory powers over the 6,000 banks currently existing in the eurozone. In parallel, new rules will come into force, adapting the functions of the European Banking Authority (EBA).

The ECB will directly supervise the eurozone's largest banks, deemed significant credit institutions, and the smaller institutions will be covered by their current supervisors, but under the instructions and ultimate responsibility of the ECB. Indeed, the ECB may decide at any time to take responsibility for these entities, which are considered less significant credit institutions, according to the legal framework of SSM.

The exercise of these responsibilities by the ECB is one of the necessary conditions for the SSM to be utilized as an instrument for the direct recapitalization of eurozone banks. The body directly responsible for that function within the ECB will be the Supervisory Board, which will have complete independence in the performance of its responsibilities.

It should be emphasized, as noted by Berges, Ontiveros and Valero (2014), that the SSM does not represent a simple unification of the supervisors in this field, but an integrated banking supervision system, that will be developed on two levels, as occurs with the eurozone monetary policies: a central level, under the responsibility of the ECB, and a national level, corresponding to the national supervisory authorities. Unlike the Spanish case, the latter are not always under the responsibility of the central banks.

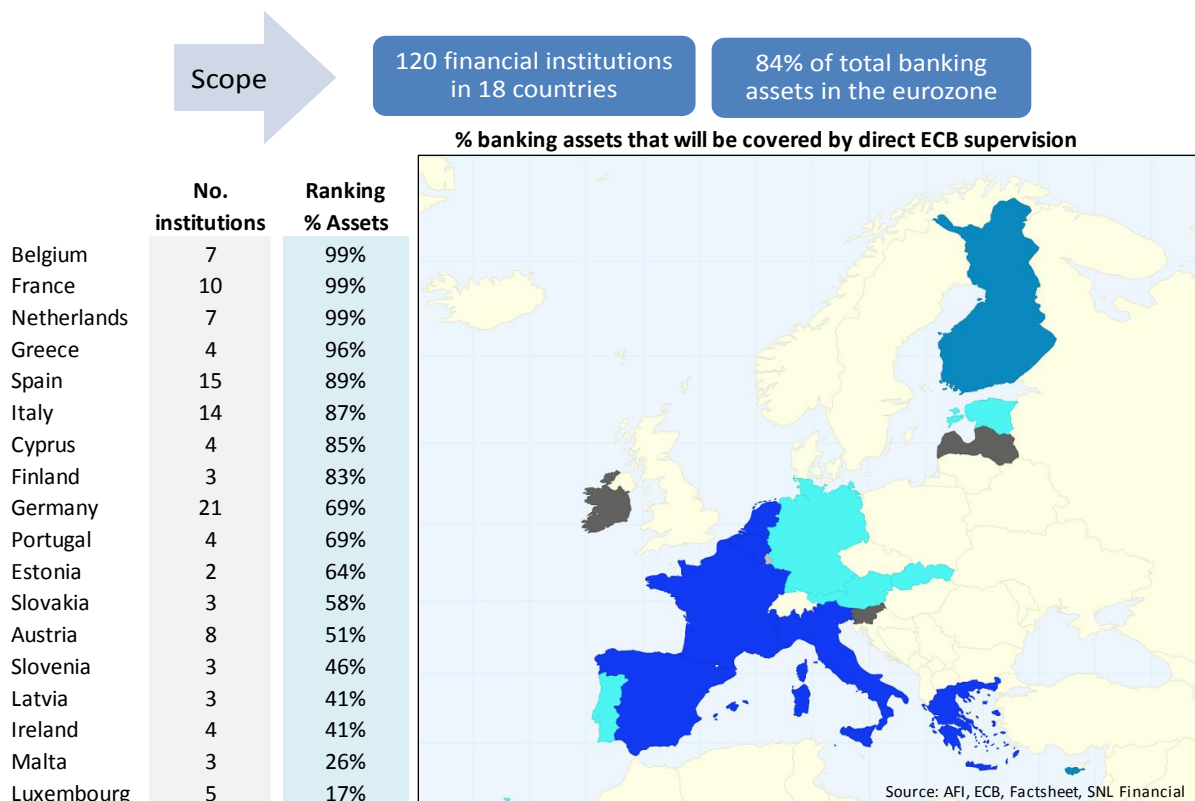
The decision-making in the SSM is based on a new “non-objection” procedure, whereby the entity responsible for supervision, the Supervisory Board, shall propose the decisions to the Governing Council of the ECB and, if this one does not object within a defined period of time, the decision is deemed adopted.

In order to ensure proper differentiation between jobs monetary policy and banking supervision tasks, the ECB has created a Mediation Panel to resolve differences of views regarding an objection by the Governing Council to a draft decision of the Supervisory Board.

It is hardly necessary to point out the functional complexity that will rule from now on in the ECB. Its sole function of defining monetary policy, on the basis of a simple target, price stability, gives way to a notably more complex structure, as can be appreciated in Table 6. Even though the national supervisors will continue to play an essential role in the new supervisory functions, especially regarding the smaller institutions, the ECB's acquisition of power is certainly significant. This is hardly a unique situation. In reality, 14 of the eurozone's 17 national central banks have responsibility for banking supervision, as do central banks in other advanced economies.

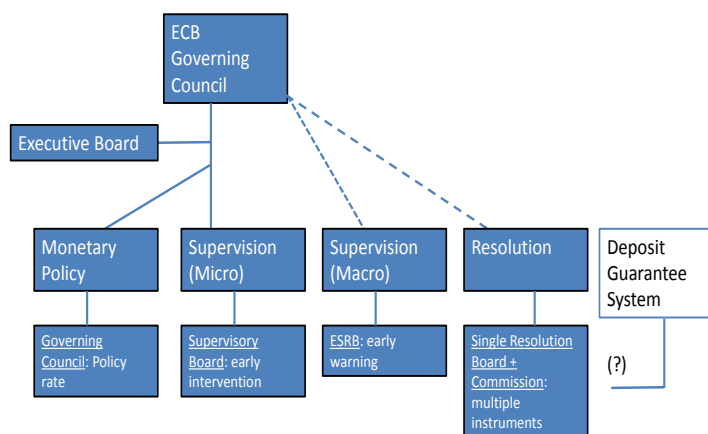
It should be remembered that the SSM's scope is not limited to the eurozone, but may extend to those non-eurozone EU countries which decide to sign up to it, on the same basis as those belonging to the eurozone.

Table 5. Single Supervision Mechanism (SSM)



It is worth recalling that the definition of monetary policy and banking supervision are complementary functions, and even give rise to synergies, as the President of the ECB has indicated on several occasions, which does not mean that this is an easy task, especially at the present moment. The start of the crisis was precisely when the crucial role of the banking systems in the transmission of monetary policies was revealed. It is in this context that this common supervision can contribute additional advantages by providing greater guarantee of the autonomy of the supervisory function, by removal of the risk of "supervisor capture" by financial institutions, particularly the larger ones.

Table 6. Distribution of the ECB's tasks



Source: Eijffinger, S. C. W. (2013)

2.3. Resolution of banking crises

Once in operation, at the beginning of January 2015, the Single Resolution Mechanism (SRM) will define the basic principles for managing banks' viability problems. For all the countries participating in the SSM, it will provide a uniform system for resolving banking crises that will not consist fundamentally in rescuing banks in difficulties with the taxpayer's money. In future, it will be the shareholders and principal creditors who take priority in absorbing the losses.

The fact that the EU's current orientation with regard to bank rescues and the resolution of banking crises clearly establishes priorities in the assumption of losses by shareholders, bondholders and other creditors does not mean that public finances remain unaffected. The need for EU assistance may be clear, as occurred in the

case of Spain's banking rescue and its recourse to the European Stability Mechanism (ESM). Consequently, the provision of the corresponding mechanism and its operation is essential.

At the European summit of June 2012, discussed above, at which the scope of the BU was defined, it was established that the European rescue mechanism, the ESM, should include the possibility of directly recapitalizing the banks.

However, contrary to what happened with the SSM, there are significant differences between governments in this respect. The reason is the budgetary impact of any future banking crises, in the light of the past painful experiences, not only in the management of the current banking crisis in the eurozone.

Clarifying sufficiently that mechanism, and endowing it with sufficient financial resources, is central to achieving the main objective of accelerating the banking integration process, as is the elimination of the vicious circle between banking risks and sovereign risks. There is agreement on the creation of the Single Resolution Fund (SRF), which would be funded by contributions from the banks. Its initial configuration is based on national compartments, but with the intention of integrating them over a period of eight years, after which they would be completely unified: the pooling of risks would be then effective. There is no automatic link between the SRF and the ESM, meaning that, should a crisis arise unexpectedly and the SRF does not have sufficient resources, it would have to borrow in the markets.

The attitude of the German authorities limited the scope of the initial intentions by conditioning direct access to ESM for the direct recapitalizations of banks, save in very exceptional circumstances. As indicated above, there is great reluctance to impose the costs of possible crises on national budgets. Formally, the German authorities demanded a modification of EU treaties, which today certainly seems a difficult task, but the EU opted for the incorporation of an intergovernmental agreement (IGA) containing the terms finally agreed, without the need for ratification by all the EU member countries. More detail on this issue may be found in Berges, Ontiveros and Valero (2014). The IGA was signed on 21st May 2014 by 26 countries, all the EU except Sweden and the United Kingdom, indicating the maximum immediate potential

of the BU, although it is not sufficient to join the agreement: countries should also belong to the SSM and SRM.

However, the European Parliament's attitude was more flexible. Thanks to that institution, in March an agreement in principle was reached on the Single Resolution Mechanism, with a fund reaching €55 billion after a transitional period of eight years. This amount is insufficient, inasmuch as it does not completely cover the risks that may emerge in some institutions or in whole national banking systems, however much it is intended that private agents will assume most of the eventual losses. In short, these are levels which fall short of the necessary risk pooling in this area. In any case, this is a first step, that should be completed as soon as possible.

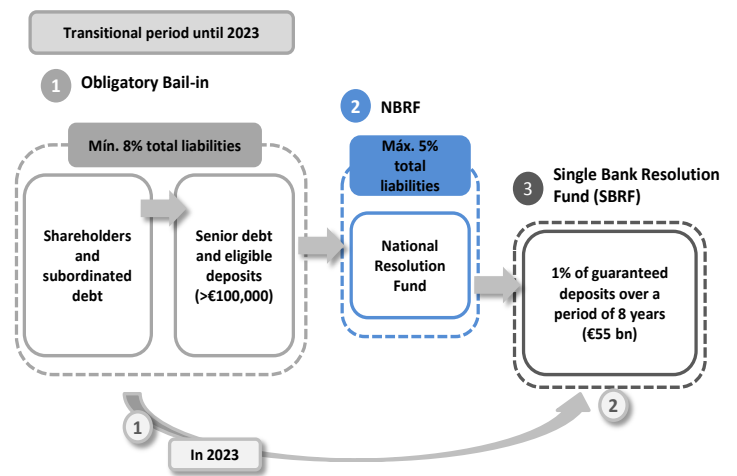
The decision on the resolution of a bank subject to common supervision would correspond to the Single Resolution Board (SRB), after notifying the ECB or the national authority responsible for resolution. The great underlying question in this regard is the flexibility of the decisions to be adopted. Fortunately, in this same agreement in March, the European Parliament favoured simplifying decision-making by granting more weight to the ECB vis a vis the member States. Even so, the voting system is still proportional to the contributions of the countries, unlike the decisions of the Governing Council of the ECB itself.

It was also the European Parliament which managed to reduce the term for financing the fund, with the contributions of the banks, to eight years, instead of the ten initially planned. Nevertheless, it did not prove possible to prevent the fund from being being compartmentalized on a national basis until the eight years are up. After the first year, the common component will stand at 40% and after the third year it will rise to almost 70%. The fund will be able to issue debt in the financial markets (Table 8).

To summarise, it is worth noting that despite the progress made, the second pillar of the BU is very far from constituting the guarantee that was planned in the initial approach. There continues to be room for doubt about its speed and flexibility: it is difficult to see how decisions can be reached in a weekend as was established, given the steps required for the approval of action and the number of parties involved in decisions in the case of a crisis, especially if large institutions are

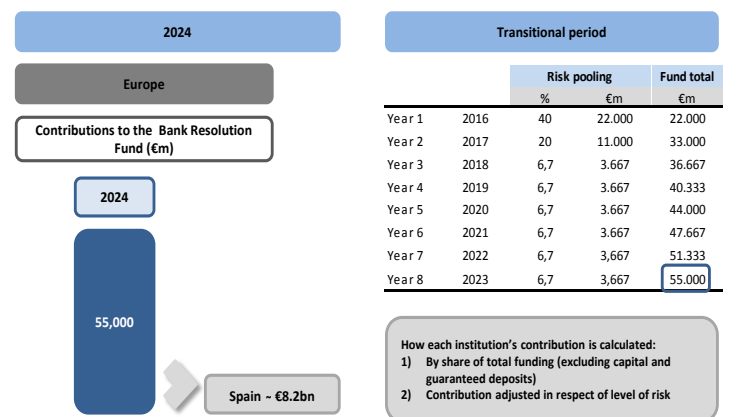
involved or a systemic crisis arises. The scope for rescues on a eurozone, rather than national, basis is likewise very limited. In its place, the bail-in criteria have been prioritized, meaning that in practice a good part of the potential cost of a rescue has been shifted toward the creditors, fundamentally the bond-holders. In the last instance, it will be the national governments which continue to bear most of the responsibility. The size of the SRF, €55 billion, is certainly small, as well as taking eight years, as noted, before it is available.

Table 7. Structure of the transitory period



Source: AFI and European Commission

Table 8. Single Resolution Fund



Source: AFI and European Commission

Box 1. 2014 stress test: basic criteria

Scope: European scope, covering 123 institutions in 22 states. Minimum coverage: 50% of the national banking sector. In the case of Spain, 15 institutions will be analysed, with a coverage of 89% of the total assets of the national banking system.

Modelling: Static balance sheet 2014-16, with the possibility of excluding restructuring plans from consideration.

Risks to be assessed: Credit, market, sovereign, securitizations and funding costs.

Accounting impact by portfolio:

Trading => P&L

Available for sale: mark to market => against capital, although the relevant authorities will be able to maintain prudential filters (exemption).

Held to maturity: impact of stress scenarios through PD and LGD, that could give rise to increased provisions

Capital required:

Base scenario: 8.0% CET1

Adverse scenario: 5.5% CET1

Capital requirements:

Base: recapitalize in the short term

Adverse: more time to cover the capital shortfall (they will agree a capital plan) and they will be able to use additional Tier 1 capital to cover them.

2.4. Deposit guarantee fund

The common regulations on deposit guarantees is the final aspect of the BU architecture. The amount insured is €100,000 per depositor per bank. This will be paid when the bank is liquidated. Each institution's contributions to the fund will depend on its risk profile: the initial contribution will be equivalent, in principle, to 0.8% of the protected deposits annually for 10 years. It is planned for Deposit Guarantee Funds to support each other mutually in case of a shortfall in one of them.

3. The transition. Review prior to the entry into force of the single supervision regime

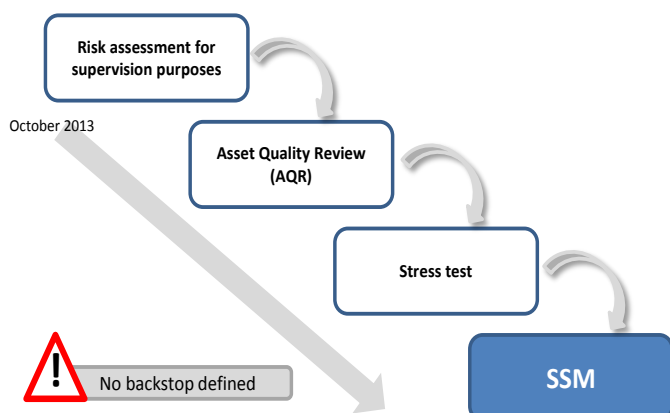
When the European leaders approved in June 2012 the use of the ESM for the recapitalization of banks, they similarly agreed that the ECB would assume the role of banking supervisor and hence would carry out a previous comprehensive assessment of 130 banks from 19 countries focused on two areas: asset quality review

and stress tests. The aim of the first one is to undertake a detailed review of the banks' balance sheets to determine whether the classification of financial instruments, provisioning levels and valuations of certain assets are appropriate. The stress test tries to assess the resilience of banks in hypothetical scenarios. The ECB is responsible for the assessments with the support of the national supervisors and independent experts. The results will be published at the end of the process, by countries and by institutions, together with the corrective measures proposed by the ECB.

The European Banking Authority (EBA) has prepared the methodology and macroeconomic scenarios, which have been developed by the European Systemic Risk Board (ESRB) for the stress tests destined to test the resilience of bank balance sheets to hypothetical external disruptions. That methodology will be used by all the banking supervisors in the EU so that all the banks, not just those of the eurozone, will be analysed using the same, easily compared, hypotheses.

Table 9. Asset quality

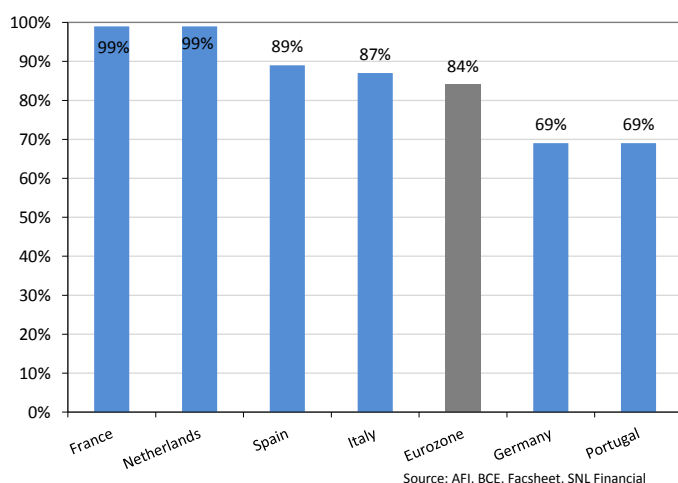
Before the SSM: overall assessment



The starting point of the stress tests for 123 banks is the Asset Quality Review (AQR), which includes the classification of risks and the calculation of the provisions and capitalization needed to cover those risk exposures.

This October 2014, the EBA will publish the final results of the stress tests for the whole of the EU in October 2014, bank by bank, including the capital position of each, its risk exposures and holdings of sovereign debt.

Graph 3. Amount of assets that come under the single supervision of the ECB (% total assets of the system, on a consolidated basis)



The assessment will affect a sample of 123 financial institutions in 22 member states, representing at least 50% of each national banking system (on the basis of

consolidated assets at end 2013) and 85% of total eurozone assets, belonging to 18 countries. That assessment will show the need for support in the form of additional capital to be calculated for those banks that need it and will be submitted to the supervision mechanism. The institutions subject to assessment are those belonging to the eurozone. In the case of Spain, they are 15 banks, with assets of close to 90% of the total.

4. Conclusions

The crisis in banking systems

- Among the world's economic regions, the eurozone has one of the highest rates of banking penetration. Its banking systems are too big. Bank finance is dominant compared to the contribution of direct financing markets.
- One of the characteristics of the economic and financial crisis in the eurozone has been its impact on banking systems. In addition to the deterioration in asset quality in some countries, a perverse linkage has arisen between sovereign debt prices and the stability of the banking sector.
- As a result of the crisis, there has been a prolonged credit crunch and an increase in financial fragmentation, both inappropriate to a monetary union.

The scope of the Banking Union

- Among the limitations of the initial design of the EMU, it is necessary to highlight the absence of mechanisms appropriate to a banking union, including a sufficient degree of coordination in the supervision of the banks. The definition of the scope of the Banking Union is one of the few favourable consequences of the crisis. It will help to strengthen financial integration in the area and the credibility of its banking supervision institutions. When all the banks in the eurozone are submitted to common regulations, supervisor

and resolution mechanism, the perception of risk will depend much less on the country of origin and more on the bank in question. The strengthening of the architecture of the Monetary Union and the definitive reduction of the exposure of banking systems to new crises will depend on the quality of the common supervisory institutions which are constructed.

- As with any decision on the strengthening of European integration, the Banking Union constitutes an important transfer of sovereignty in a field which is essential to the smooth functioning of the eurozone's economies. This is even more the case given the high degree of banking penetration in these countries and the strong dependence of smaller companies on bank credit for their financing.
- Though there are few doubts about the application of the supervision mechanism, the same is not true of the crisis resolution mechanism, compromised today by the limited amount of resources available to deal with crises, and by the lack of flexibility of the decision-making procedures in those cases in which action may be needed.
- The Banking Union will not necessarily facilitate increased competition in financial systems with high levels of banking penetration. In reality, the management of the sectoral crisis has led to an increase in banking concentration that will reduce the bargaining power of the users of financial products. Spain's banking systems is one of those where the reduction of the number of suppliers has been greatest. Hence it would be desirable to move toward a greater supply of non-bank services and financial institutions, to guarantee increased possibilities of business financing.

References

- ANALISTAS FINANCIEROS INTERNACIONALES (2014).- "El sistema bancario español ante los test de estrés: impacto en capital y carteras de renta fija", *Análisis y seguimiento de Banca y Seguros*, Nota Bancaria, 17th February.
- BCE (2014).- "[Financial Integration in Europe](#)". April.
- BERGES, A., ONTIVEROS, E. and VALERO, F. J. (2014).- "[La Unión Bancaria: avances e incertidumbres para el año 2014](#)" Documento de Trabajo Opex No 75/2014. February, Fundación Alternativas.
- BERGES, A. and ONTIVEROS, E. (2014).- "[Financiación de la economía. Bancarización frente a mercados](#)" *Mediterráneo económico* No. 25. Colección Estudios Socioeconómicos. Fundación Cajamar.
- EUROPEAN COMMISSION (2014).- "[Banking Union: restoring financial stability in the Eurozone](#)", Memo, 15th April
- DIRECTORATE GENERAL FOR INTERNAL POLICIES (2013).- "[Re-capitalisation of banks supervised by the SSM](#)", Policy Department A: Economic and Scientific Policy. *Monetary Dialogue*, December.
- EIJFFINGER, S. C. W. (2013).- "The various roles of the ECB in the new EMU architecture" in Directorate General for Internal Policies (2013) "[Re-capitalisation of banks supervised by the SSM](#)", Policy Department A: Economic and Scientific Policy. *Monetary Dialogue*, December.
- EUROPEAN SYSTEMIC RISK BOARD (2014).- "[Is Europe Overbanked?](#)", *European System of Financial Supervision*, No. 4, June.
- SCHOENMAKER, D. and PEEK, T. (2013).- "[The state of the banking sector in Europe](#)". OCDE, ECO/WKP 94.
- VÉRON, N. (2013).- "[Bank versus non-bank credit in the United States, Europe and China](#)". *Bruegel Policy Contribution*. Issue 2013/07. June.

EuropeG is composed of Antoni Castells (director), Manuel Castells, Josep Oliver, Emilio Ontiveros, Martí Parellada and Gemma García (coordinator).

This Policy Brief reflects the group's position, and the contributions of its members, on the basis of a first draft prepared by Emilio Ontiveros

EuropeG

Parc Científic de Barcelona
Baldri i Reixac, 4
08028 Barcelona
Tel. +34 934 033 723
www.europeg.com



With the support of:

