Christian Sewing

Chief Executive Officer, Deutsche Bank AG

A partnership for growth: financing recovery and growth in Europe

The German Presidency of the European Council comes at a critical time. In the midst of the unprecedented global health challenge of the COVID-19 pandemic, Europe needs to focus on recovery and averting an economic crisis. The financial sector has a critical role to play in supporting recovery and, in partnership with governments and regulators, can ensure that recovery is aligned with the strategic objectives of a digital and low carbon Europe.

The EU financial system has proved resilient in the face of the extraordinary economic challenge posed by COVID-19. This was the first real test of the regulatory reforms put in place following the financial crisis of 2008 and, for the most part, the new regime worked as intended. Capital and liquidity buffers provided the cushion required to absorb the initial shock and banks have been able to provide significant additional lending to support the economy, whilst markets have continued to function. Prompt action by regulators to provide targeted relief from aspects of the regulatory regime ensured unhelpful pro-cyclical effects have been avoided in the short-term.

However, the economic fallout from the pandemic will continue to be felt for some time and that will put pressure onto a European financial system which was already facing headwinds. Long-term negative interest rates, tensions in international trade (including Brexit), structural challenges arising from digitization of finance and competition from non-financial technology companies, as well as inflation in resolution fund contributions, pre-dated the COVID crisis. Pressure will increase as emergency government support packages are withdrawn and insolvencies of companies and households will inevitably surge.

The European financial sector, particularly the banking sector, wants to support immediate recovery and deliver the investment required to put Europe on to a sustainable growth path. But we cannot do it alone – or under the current regime. Europe needs action with political and regulatory focus on reform in the following key areas:

1. **The Banking Union needs to be completed and its benefits realised.** This is essential to underpin the efficient operation of the banking system and to remove the deadweight cost of trapped liquidity and capital within the Eurozone. It is also critical to facilitate consolidation and rationalization within the EU banking sector necessary to support profitability and growth of capital to support lending.
2. **Changes to the EU capital regime should be paused** until the impacts of COVID-19 are clearer. The existing framework has proved robust and Europe should coordinate with other regions in taking forward implementation of final Basel III rules.
3. **The Capital Markets Union must become a reality.** Deep and liquid capital markets are critical to deliver efficient finance, cost effective risk management and access to international investment for European businesses. In the short-term, developing an active securitization market in the EU could play a critical role in freeing up bank balance sheets to support new lending and allowing them to manage the challenge of increasing NPLs. The package of proposals published by the European Commission on 24 July is an important first step to delivering some of the changes required to enable capital markets to support recovery, but further bold steps will be required to achieve real change.
4. **The ambition for a true digital single market must be delivered.** To realise the opportunities afforded to European citizens and business of digitalization there needs to be legal and regulatory certainty, but also consistency across Member States. A fragmented legal and regulatory environment will undermine scale efficiencies, disincentivise innovation and open the door to regulatory arbitrage.
5. **The framework for sustainable finance needs to be further enhanced.** The EU has taken a lead in legislating to support the shift to a low carbon economy with the green taxonomy and climate disclosure requirements. The COVID recovery provides an opportunity to accelerate that agenda. Regulatory incentives need to be put in place to encourage the flow of sustainable projects and to support the development of new channels of 'green' finance.

To achieve this change will require political ambition, policy vision and a strong partnership between public and private sectors. ●