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We need to breathe

During the covid crisis, banks have been part of the solution, together with the support of monetary and fiscal policies. They provided liquidity to the European businesses and households, to bridge their cash needs when the economy stopped due to the pandemic. This has been crucial, because the European financial market is too small to substitute banks' ongoing external financing. Banks have enough liquidity and capital to weather this "live" stress test, as recognised by supervisors (SSM vulnerability analysis, July 2020).

So far, the impact of the economic crisis on banks' balance sheets has been limited. It is no wonder, since public institutions absorbed most of the shock. They were indeed the only ones able to do so, due to the nature and magnitude of the crisis. Bankruptcies and NPL have not soared. For the time being, most of the impact on banks comes from the ex-ante provisioning of possible risks.

In any case, banks will absorb part of the shock. However, the materialisation of these risks depends on public policies. The pandemic crisis is not over. We still need strong support from public authorities to back the economy and the most affected businesses. If this occurs, casualties will be limited. In the meantime, pessimistic forecasts feed old habits: self-protection, mistrust and the comeback of the usual bureaucracy.

The implementation of Basel IV is especially worrying. Indeed the Commission plans to release its draft legislation next July, in the middle of the economic crisis.

First, legislators should not transpose the Basel agreement until the EBA has completed a deep analysis to provide the full picture of the Covid impact on banks. An estimated impact by supervisors of between 200 to 800 bp on solvency ratios confirms that additional capital requirements may destabilise the financial sector by seriously narrowing capital buffers European banks now have over regulatory minima. The trick of a long phasing-in has already proved its inefficiency in in the past, since markets always priced a fully loaded approach of regulations such as Basel III.

Second, at the very time when Europe needs financing to continue supporting businesses and to support the green and digital recovery, this reform would freeze hundreds of billion euros representing a financing capacity of thousands of billion euros, with no possible compensation by the financial market. As supervisors have repeatedly said that the capital level of European banks is adequate, the urgency is not to increase it further. Rather than finalising the answer to the previous and different crisis, we should try to solve the present one, with timely solutions. Americans are pragmatic. They are faithful to the political mandate of no significant increase in capital requirements. They said they would stick to it, noticeably for FRTB. This will not hamper their recovery.

Third, Europeans are not lagging behind as regards prudential regulations! They have gold-plated Basel III with pillar 2 and MREL. Another layer of gold plating is not necessary.

All we need is appropriate implementation, respecting the political mandate of not significantly increasing overall capital requirements, and not resulting in significant differences for specific regions of the world.