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Press Release 5/2018

Halle (Saale), 21 March 2018

What is holding back the banking union?

The European Commission wants to better regulate and monitor the European banking sector. In many EU Member States, however, the necessary directives are being implemented extremely slowly. Surprisingly, the reasons for this do not lie in politics and banking structures, but in the institutional framework conditions and existing regulations in the Member States, as argued by Michael Koetter, Thomas Krause and Lena Tonzer from the Halle Institute for Economic Research (IWH).

The European banking union has set itself the goal of harmonising banking regulations across national borders, in order to improve financial stability within the European Union (EU). The aim is that taxpayers will no longer have to bail out insolvent banks in the future. To achieve this, the banking union is based on three pillars: firstly, a common banking authority that is intended to supervise the major banks in the eurozone. Secondly, a standard mechanism for winding up insolvent financial institutions and establishing rules for the assumption of losses of the banks' creditors. And thirdly, consistent guidelines for deposit protection.

Most EU Member States have failed to implement these directives within the deadline set by the European Commission. Belgium, Lithuania, Poland and Slovenia, in particular, have taken a long time to incorporate the directives into national legislation, while Germany and Austria have been the quickest to do so.

There are several reasons for these delays: "Governments may want to protect their national banking sector from stricter regulations or are in principal unwilling to delegate any more control to the EU. Technical obstacles are also a possibility if the national banking system to which the new directives are to be applied is highly complex," says Koetter, Head of the Financial Markets Department at IWH. However, the research group also considered other options: "Existing regulations or even political and institutional framework conditions could also be responsible for the delays, for example if a Member State's fiscal room for manoeuvre is restricted or if a particularly large number of parties and officials are involved in decision-making. Differences in the efficiency of Member States' legal systems are another possibility. We therefore looked at a whole range of options," says Koetter.

Among the many possible explanations, primarily national regulations were found to be standing in the way of rapid implementation. The economists discovered that the more heavily a financial market is regulated, the greater the process is delayed – possibly because an already heavily regulated banking system requires greater adjustment. If, however, existing regulations are already compatible with the new directives and the corresponding banking union pillar is based, as it were, on existing regulations, the process is accelerated. Political factors also explained the de-

Press embargo:
21 March 2018, 12:00 noon CEST

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Keywords
banking sector, banking union, banking regulations, European Union, financial stability, financial system

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lays, but not to the same extent as regulation. “In particular, the number of political parties in a country plays a role. Implementation of the banking union is noticeably slower when lots of parties are involved in the decision-making process,” says Koetter.

The banking union will only be successful if, despite national differences, the directives are uniformly implemented without any further major delays, to allow the banking union to operate effectively. Only then will market players recognise the banking union as an institution and adjust their risk behaviour accordingly.

Publications

Koetter, Michael; Krause, Thomas; Tonzer, Lena: Delay Determinants of European Banking Union Implementation. IWH Discussion Papers 24/2017. Halle (Saale), 2017.

Koetter, Michael; Krause, Thomas; Tonzer, Lena: Welche Faktoren verzögern die Umsetzung der Bankenunion?, in: IWH, Wirtschaft im Wandel, Jg. 24 (1), 2018, 5-7.

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