How Banco Popular put a spotlight on the EU's Single Supervisory Mechanism

Blog post by Practice Lead Carmen Bell, 21 June 2017

I listened this week to SSM head Danièle Nouy defending the sale of Spain's Banco Popular to Banco Santander in front of the ECON committee of the European Parliament. It was notable how hard Spanish and Italian MEPS in particular pushed her on the ECB's declaration that the transfer of ownership had been a success for the SSM and the EU's new approach to resolution and recovery. Nouy implied that the SSM process couldn't have been more seamless: producing a win for the bank's depositors, Spain's taxpayers and, ultimately, the ECB.

Many MEPs differed, and in a way that emphasises the difficulty of the SSM's position. They argued that Banco Popular's situation in fact demonstrated the limits of the ECB when it comes to addressing financial stability threats. Nouy wanted to focus on the coordination of the rescue itself. MEPs wanted to know why the EBA stress tests had suggested a bank in sufficient health despite a large toxic mortgage loan portfolio; when and for how long Banco Popular's liquidity threshold was violated and if the ECB was aware of the rumours that "privileged insiders" had withdrawn billions of euros worth of deposits just prior to the ECB's resolution declaration. MEPs also worried that the division of eurozone banks between debt-laden weaklings and banks in a position to buy them was not good for competition. Nouy could only really protest that these were questions of national competence and beyond the scope of ECB policy.

What should we conclude from this? One thing would be that politically the ECB is accruing formal responsibility for banks in death but it may often be hard to disentangle that from the decisions that are taken (or not taken) as they slide into failure or before. So long as the ECB remains limited in its ability to deal with issues of fraud, money laundering or insider information, it will face questions about its role in enforcing standards at the banks it ultimately has to resolve. The suggestion from some MEPs that the backstop of the SSM stepping in and 'assuming responsibility' was now itself acting as a form of moral hazard for national supervisors is important.

There may yet be some common ground for Nouy and the MEPs – a closer partnership, if not potential merger, between the SSM and the EBA. This could address MEPs' concerns over lack of oversight for national supervisory practices while supporting Nouy's belief that a more prominent, "European voice" from EBA Chair Andrea Enria would align day-to-day supervision and resolution. Giving Enria voting rights equal to national supervisors may be countered with some resentment from member states, but it would, at a minimum, potentially underscore the SSM's own supervisory reach. Whether such a development could evolve from the European Commission's current work on the review of the European Supervisory Authorities remains to be seen.

It would be fair to say the Banco Popular case illustrates some headway has been made in the area of eurozone resolution policy. But it is also hard to escape the conclusion that that the SSM got lucky with Banco Popular because a buyer was available. Things could have looked less 'seamless' – and Nouy perhaps less optimistic - if it had not been; or if a solution closer to the compromise for Monte di Paschi had been required. Current events in Italy demonstrate the danger of too much confidence in the market. The European Commission is determined to shift losses to the private sector as two more Italian banks face potential collapse, but so far available buyers are scarce, and despite Monte dei Paschi's public rescue, it has yet to find investors willing to take 26 billion euros worth of bad debt off its balance sheets.

Policymakers looking to promote the European Deposit Insurance Scheme and fiscal backstop to the Single Resolution Fund will look to Banco Popular for validation – arguing that these things are backstops that need never be touched, not bailout funds. But it is also the case that, in the absence of these things, the SSM is politically exposed and more liable to get pulled into compromises of the Monte dei Paschi kind. What we witness today in Spain and Italy suggests a system that is half-built, with all the problems of a half-built system.