EUROPEAN CENTRAL BANK

EUROSYSTEM

ECB-PUBLIC

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FINAL

Summary of Banking Industry Dialogue on 30 June 2021

Participants

- Members of the Governing Council of the ECB or their alternates.
- Representatives of Banco Bilbao Vizcaya Argentaria, Banco Comercial Português, Banco de Sabadell, Banco Santander, Bank Degroof Petercam, Banque Internationale à Luxembourg, Barclays, Crédit Agricole, Deutsche Bank, DZ Bank, Eurobank Ergasias, Hellenic Bank Public Company, Intesa Sanpaolo, Nordea, OP Financial Group, Permanent tsb Bank, Raiffeisen Bank International, Société Générale and UniCredit.
- Senior ECB officials from the Directorate General Macroprudential Policy and Financial Stability, Directorate General Communications, Directorate General Secretariat, and the ECB's Chief Services Officer and the Chief Compliance and Governance Officer.

Financial stability challenges in the macro-financial environment and the financial system

Bank participants noted that conditions in the macro-financial environment have improved in recent months, although it was acknowledged that the pandemic continues to pose risks. The public support measures for corporates and households that have been deployed during the Covid-19 health crisis were seen to mitigate the impact of the pandemic and reduced credit risks. It was, however, noted that the design and use of support measures have differed across countries and that an early withdrawal of the support could lead to higher credit risks in the macro-financial environment. At the same time, the support measures have increased public sector vulnerabilities, with bank representatives expressing concerns that sovereign risks could spill over to the banking sector in case of an unexpected withdrawal of monetary stimulus.

Vulnerabilities in the non-financial corporate sector were characterised as differing substantially across segments, with, in general, small and medium-sized companies and sectors such as hospitality and commercial real estate more impacted by the pandemic. Bank participants noted that the real levels of credit losses will emerge during the next 12 months after support measures are lifted, although it was mentioned that credit losses for loans, where moratoria have ended, have so far been lower than what had been feared. Looking ahead, although loan demand is expected to remain muted in the period ahead, some improvements have been observed. It was mentioned that corporates had learned lessons from previous crises and built-up liquidity buffers, while some sectors were already benefitting from renewed cash inflows, which resulted in a reduced demand for credit. Loan demand was also seen as being muted in some cases, as corporates are in a wait-and-see mode, due to the pandemic and, therefore, postponing large scale investments.

Bank participants noted that somewhat higher inflation (marginally above 2%) would be welcome and beneficial for the banking sector. Concerns were, however, expressed that a more permanent and notable increase in inflation could pose challenges. Developments in labour markets, and in commodity and energy prices, were seen as key factors in shaping the inflation outlook at present.

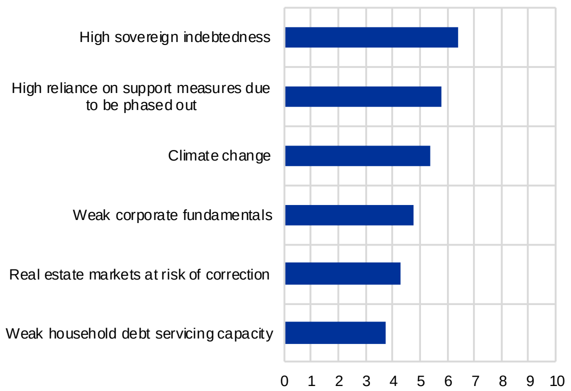
It was emphasised by bank participants that the banking sector had been in a sound position going into the pandemic and had, therefore, been able to continuously provide lending to the real economy. It was noted that bank profitability remains weak in parts of the sector and when compared with international peers, notably in the United States. The low level of interest rates was considered as one important factor weighing on banks' profitability. Although credit losses had so far been lower than expected during earlier phases of the pandemic, further losses in the period ahead could not be excluded. Bank participants noted that the sector was well capitalised to withstand such losses and, therefore, argued that there would be no need for the ECB to extend its recommendation to banks to refrain from or limit dividends beyond the current expiry date on 30 September 2021.

Bank participants noted that the potential introduction of central bank digital currencies is an important topic for the banking sector and that banks stand ready to support the ECB, should it decide to proceed with the launch of the digital euro project.

Finally, participants from the banking industry provided a ranking of existing vulnerabilities in the macro-financial environment and the financial system (see Charts 1 and 2).

Chart 1 Ranking of vulnerabilities in the macro-financial environment according to bank participants

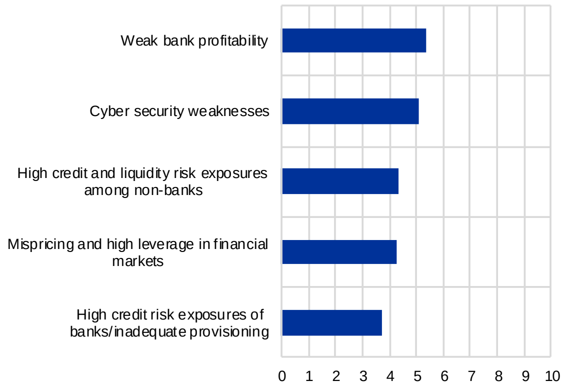
(1 = low concern; 10 = high concern)



Source: ECB survey with bank participants to the Banking Industry Dialogue.

Chart 2 Ranking of vulnerabilities within the euro area financial system according to bank participants

(1 = low concern; 10 = high concern)



Source: ECB survey with bank participants to the Banking Industry Dialogue.

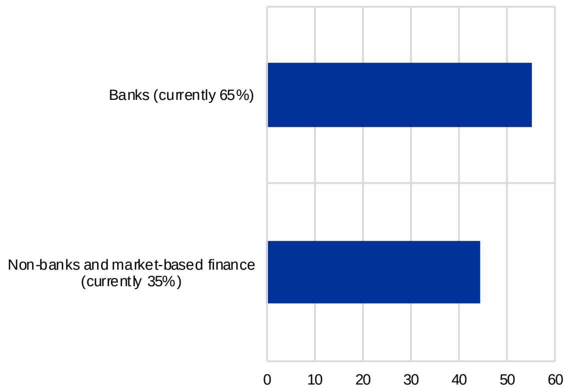
What will the banking sector look like in 2030?

Bank representatives highlighted that the euro area banking sector is undergoing an important transformation. Various internal and external factors have led to a need for the banking sector to adjust the way it operates. Such factors include, i) higher competition from non-bank financial intermediaries, Bigtech and Fintech companies, which, according to bank participants, are not subject to a regulatory framework that assures a proper level playing field, ii) the ongoing digitalisation of financial services provision and of the society at large, and iii) the need to support the transition to a green economy to address climate change.

Bank representatives argued that the banking sector will remain the most important sector providing credit to the real economy in the future. The movement in the euro area financial structure from strong bank dominance towards a more balanced composition was, however, expected to continue (see Chart 3). It was argued that regulation will play a crucial role in determining what the banking sector will look like in 2030. The importance of having a resilient banking sector was acknowledged but at the same time it was argued that European banking regulation needs to allow for banks to compete with banks in other regions and with non-bank financial institutions.

Chart 3 Expected shares of bank and non-bank credit provision to euro area non-financial corporates and households in 2030 according to bank participants

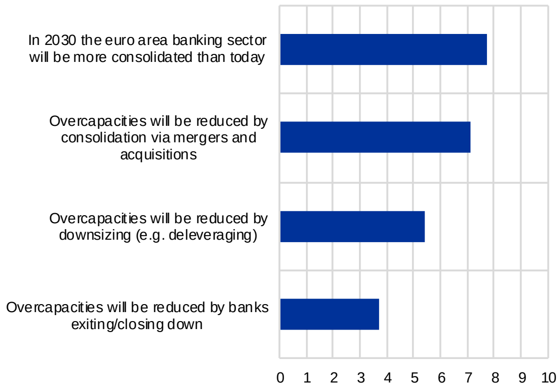
(percentages)



Source: ECB survey with bank participants to the Banking Industry Dialogue.

Chart 4 Expectations around bank consolidation according to bank participants

(1 = strongly disagree; 10 = strongly agree)



Source: ECB survey with bank participants to the Banking Industry Dialogue.

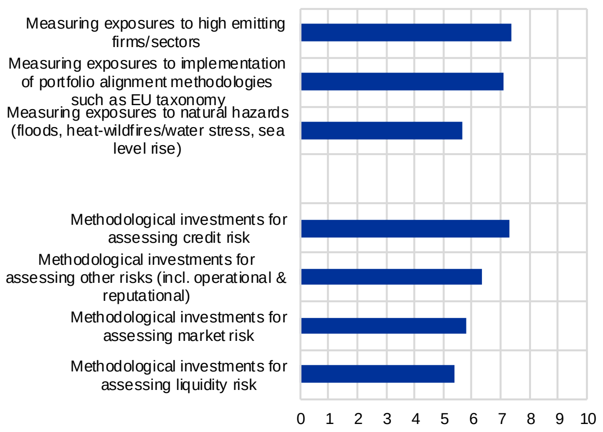
Technological innovation was expected to change the banking system and reshape the market structures. Bank representatives foresaw the decline in the number of bank branches to continue and to further develop digital products and interactions with customers, with, for example, artificial intelligence and cloud services, being technologies that will improve the way the banking sector operates. It was noted that the banking sector, even with fewer branches, will continue to support customers via close, albeit via more virtual, interactions.

Bank representatives expected the euro area banking sector to be more consolidated in 2030 (see Chart 4). Consolidation will help close the gap which has been widened since the financial crisis between US and European banks. Mergers and acquisitions were seen as the main way to consolidate the banking sector (see Chart 4). It was, however, noted that such consolidation is expected to mainly take place within countries, as there are some obstacles to cross-border consolidation, especially among smaller banks, and due to a still incomplete banking union. It was also mentioned that there are good reasons for the existence of smaller, more specialised, banks so consolidation should only take place where it brings clear benefits.

Bank representatives argued that the most important task for banks in the coming years is related to climate change. Banks need to have an active role in helping the economy transforming onto a sustainable path. To adjust to climate change banks currently focus on, among other things, measuring exposures to high emitting firms and sectors and are making methodological investments for assessing credit risks (see Chart 5). It was claimed that time is needed to transform the economy, including for further implementing Environmental, Social, and Governance (ESG) criteria. In this context, the lack of common definitions of ESG activity was seen as hindering an efficient implementation.

Chart 5 Urgency and importance of climate change aspects for the financial system according to bank participants

(1 = not urgent/unimportant; 10 = very urgent/important)



Source: ECB survey with bank participants to the Banking Industry Dialogue.