François Villeroy de Galhau: Ten years of Single Supervisory Mechanism (SSM) - great achievements, and new journeys to complete

Speech by Mr François Villeroy de Galhau, Governor of the Bank of France and Chair of the Prudential Supervision and Resolution Authority (ACPR), at the Conference held at the ACPR, Paris, 24 June 2024.

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Ladies and Gentlemen,

I am pleased to welcome you, alongside Denis Beau, First Deputy Governor of the Banque de France, and Nathalie Aufauvre, Secretary General of the ACPR, to this conference organised by the ACPR *(Autorité de contrôle prudentiel et de résolution*), in this year when the ECB is celebrating the 10th anniversary of our single supervisory mechanism (SSM). It is also a very great pleasure and honour to welcome prominent architects and builders of the SSM: Jean-Claude Trichet, the three consecutive Chairs of the SSM, Danièle Nouy, Andrea Enria and Claudia Buch, as well as Christian Noyer, Elizabeth McCaul and Edouard Fernandez-Bollo.

The SSM is undeniably a success story; it is acknowledged as one of the most efficient supervisory bodies in the world. It has a key human foundation: the successful integration of teams, and ever greater convergence. I would like to pay tribute to the remarkable commitment of the staff at the ECB and the national supervisors, including that of the women and men at the ACPR. The ACPR provided the SSM with its first Chair, the talented and highly-committed Danièle Nouy, and more than 80 colleagues. The ACPR was also a major driver in the adoption of an integrated and intrusive supervision model, in which independent on-site inspections play an important role. Building on these strong credentials, the SSM can now evolve towards a more qualitative and risk-focused supervision (I). Taking a broader perspective, completing the Banking Union remains an utmost necessity to further strengthen European banks (II).

I. Relying on its strong credentials, the SSM can now evolve towards a more risk-focused supervision

The SSM is the result of the strong and common determination of European political authorities and supervisors alike, in the wake of the great financial crisis. From its inception in 2014, the SSM went to tremendous lengths to reduce European banks' vulnerabilities and enhance their risk management, and quickly created the conditions for effective supervisory harmonisation. All in all, the SSM significantly improved resilience of, and confidence in the European banking sector. It forcefully demonstrated its ability to prevent crises – notably in 2023 after the bank failures in the United States and the forced takeover of Credit Suisse. Basel rules and European macroprudential policies have also served our financial system well. Together, these elements have effectively protected the euro area – throughout the pandemic and then the sharp rise in interest rates.

Now is the time for regulatory stabilisation. European supervisors and legislators are determined to ensure a level playing field between different jurisdictions and, consequently, a fair application of Basel III everywhere. With this in mind, the Commission envisages a one-year delay for implementing the FRTB; but we strongly hope the US authorities will transpose Basel 3 in a full and consistent way and in the not too distant future.

Coming back to the SSM, its supervisory practices are now sufficiently mature to make processes leaner, in order to enhance risk-based supervision and make use of the full supervisory toolkit – notably by focusing on qualitative measures. That was the main conclusion of the Wise Persons report in April 2023[i]. Fernando Restoy is also with us today, and I would like to take this opportunity to pay tribute to this collective work. This report paved the way for the improvement of the existing Supervisory Review and Evaluation Process (SREP) and the launch of several new projects and initiatives.

Last month, the Supervisory Board decided on concrete measures to incorporate a more risk-proportionate approach into the SSM's methodologies, processes and tools, starting in the second half of 2024 as recently stated by Claudia Buch.[ii] Let me highlight a few complementary upcoming improvements in the SREP. First, the reinforcement of the multi-year approach to better plan and spread the detailed analysis over time and, provided there is no material change in a bank's risk profile, the possibility to update SREP decisions every two years instead of yearly. Second, a greater focus on key expectations and results, with a better use of the escalation ladder should deficiencies remain non-remediated for a long time. Overall, we will have a shorter SREP process, with decisions to be sent to the majority of banks by the end of September, compared with December as currently the case. All these measures are significant steps forward: they will make supervision swifter, more responsive and more intrusive where needed.

To go further, we can and should pursue our efforts towards a more qualitative and risk-focused supervision. The forthcoming new SREP methodology is a real opportunity to prioritise our supervisory tasks according to our risk assessment and incentivise further SSM banks to achieve the necessary changes to improve their risk profiles. With regard to our internal functioning, there is still room to fine-tune the articulation between vertical and horizontal supervisory activities to enhance our effectiveness, optimise our resource allocation and thereby reduce the "supervisory burden" both for banks and supervisors. As bottom-line, we need to engage even further into a constructive supervisory dialogue; and this requires commitment on both sides of the table, we as supervisors, and banks alike.

I deeply believe that we can now leverage on SSM expertise and in-depth knowledge of the European banking sector to trust our supervisory judgement, and adopt a more strategic and holistic approach to risk assessment. While benchmarking is an important input into the process, notably to ensure a level playing field, it is clearly not the only one; the individual assessment of each bank's risk profile, based on constrained expert judgement, should remain the core of our assessment.

II. Banking Union: why and how to move forward again

Let me now turn to a far-reaching issue that we still need to tackle, after several years of deadlock: a fully integrated banking market in Europe. Let us acknowledge it: we have been very successful in building a Supervision Union – which we celebrate today – less so in a complete Banking Union. This slowness has hampered the emergence of pan-European banks, and our banks are becoming smaller compared with their global rivals. In 2023, the domestic market share of the top five US banks stood at 42%, compared with around 28% for the top five in Europe.[iii] Meanwhile, the most active European bank on investment banking activities ranks only ninth worldwide, far behind the top five – which are all American. Euro area banks accounted for only 29% of investment banking fees generated by the top 10 players in Europe in 2023, compared with 34% a year earlier.[iv]

For banks – and we see this in the United States – scale is objectively a major determinant of competitiveness, particularly as it enables banks to amortise the cost of critical investments in digital technology and artificial intelligence. European banks will have to innovate in the tokenisation of their deposits, and in building "cutting-edge" payment and market infrastructures in conjunction with public authorities. We shouldn't fear larger, cross-border European banks, provided they are managed and supervised closely; on the contrary, we should foster them. It is high time we took advantage of the size of the European market. We Europeans need to find a way to make real and significant progress: step by step, in the right direction, and I know dear Claudia you share this conviction.

In particular, efforts still need to be made to put into practice the notion of a "single jurisdiction", and to put aside some of the nationalistic debates and ring-fencing practices, particularly in "host" countries. The effective implementation of cross-border liquidity waivers, although prescribed by the European legislation, remains far too limited in practice. Waivers for capital requirements should not only be treated as a heritage but new ones should be envisaged as well, including the extension of intra-group waivers for resolution purposes. Consequently, many of us have proposed solutions for completing the Banking Union, notably Andrea Enria and his concrete proposed ways-forward;[v] our workaround solutions need to tackle the home/host issue to succeed.

In the same vein, I suggested a few years ago that instead of a fully-fledged EDIS (European deposit insurance scheme) we could work on more targeted solutions.[vi] In the words of my German colleague Joachim Nagel last April,[vii] "a hybrid model would offer multiple benefits over a centralised, purely European model". We could keep the national deposit insurance schemes as they currently exist, but support them when specific payout interventions require additional liquidity. We could also significantly improve the coordination between supervision and resolution, and better incorporate the cross-border dimension in our requirements for MREL and own funds.

One final word to state the obvious: French banks are very solid in their liquidity as well as in their capital, and these strengths have not been anyway affected by the recent moves in stock exchanges due to political uncertainty. Still more important, the French banking model is conducive to sound financing of the real economy and favourable to banks' customers (households as well as businesses), with its three components: moderate intermediation margins, high lending volumes and a low cost of risk. French banks are and will remain a positive asset for the French economy, and for Europe as well, being among the largest and most resilient ones.

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I will conclude with Marcel Proust and Swann's Way – the first volume of In Search of Lost Time. "The real voyage of discovery consists not in seeking new landscapes, but in having new eyes" (« *Le véritable voyage de découverte ne consiste pas à chercher de nouveaux paysages, mais à avoir de nouveaux yeux* »). Well, when it comes to our matters, new eyes can enable us not only to complete our supervisory and Banking Union journeys, but also to change the European landscape on competitiveness, growth and innovation. The former goal will support the latter. Thank you for your attention.

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[i] Dahlgren (S.), Himini (R.), Restoy (F.) and Rogers (C.), *Assessment of the European Central Bank's Supervisory Review and Evaluation Process, Report by the Expert Group to the Chair of the Supervisory Board of the ECB*, April 2023

[ii] Buch (C.), Reforming the SREP: an important milestone towards more efficient and effective supervision in a new risk environment (europa.eu)

[iii] Expressed in terms of consolidated domestic assets. Sources: Federal Reserve, ECB and Banque de France calculations.

[iv] London Stock Exchange group, ACPR calculations

[v] Enria (A.), *Of temples and trees: on the road to completing the European banking union*, speech, 17 May 2022

[vi] Villeroy de Galhau (F.), *The Banking Union: Time to move forward again*, speech delivered at Eurofi Financial Forum, 10 September 2021

[vii] Nagel (J.), *Monetary union, capital markets union, banking union – a triad for Europe's prosperity and resilience*, speech, 23 April 2024