A backstop to the Single Resolution Fund now!

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On Monday, euro area ministers of finance agreed to proceed with the reform of the ESM, to sign the revised Treaty in January 2021 and to launch the ratification process. They also agreed to advance the introduction of the ESM's common backstop to the Single Resolution Fund (SRF) by the beginning of 2022. This is especially important at a time when the pandemic has stalled improvements to banks' health that followed the euro crisis. In this post, we argue that although banks emerged better equipped from the last crisis, their residual vulnerabilities, combined with the effect of the pandemic, confirm the benefits of a swift implementation of the backstop.

Banks are in a better position than during the euro crisis...

Banks were better prepared for a downturn. Policymakers and banking supervisors learned from the past crisis, tightened up the regulatory toolkit and set the right system of rules and incentives to make banks develop their risk management capabilities and decrease their risks. Banks have been increasing their capital cushions; levels are, on average, higher than ever (Figure 1). The average Common Equity Tier 1 (CET1)[1] ratio observed in the second quarter of 2020 is around 14.6%, significantly higher than the 10.6% average requirement set by the supervisor at the end of 2019.