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European Banks Have Already Enhanced Their Balance Sheets Ahead Of EU Banking Reforms, Says Report

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PRIMARY CREDIT ANALYST

Bernd Ackermann
Frankfurt
(49) 69-33-999-153
bernd.ackermann
@spglobal.com

SECONDARY CONTACT

Giles Edwards
London
(44) 20-7176-7014
giles.edwards
@spglobal.com

ADDITIONAL CONTACT

Financial Institutions Ratings Europe
FIG_Europe
@spglobal.com

- Regulatory reforms on banks' capitalization, liquidity, and resolution will become effective in the EU toward the end of this month.
- Banks have strengthened their balance sheets in the past few years in anticipation of these reforms.
- We already reflect this improvement in our ratings, and expect few changes in how European banks manage their capital and liquidity because of these regulatory reforms.
- Various features of the legislation could mean that regulators still find many banks difficult to resolve if they are failing.
- In addition, the reform package only includes a few elements that will foster stronger integration of banking markets in the EU.

FRANKFURT (S&P Global Ratings) June 18, 2019--S&P Global Ratings considers the EU's latest package of banking reforms--a milestone in Europe's financial reform agenda--to be evolutionary rather than revolutionary. (See "EU Banking Reform Package: Enhanced Balance Sheets, Incomplete Market Integration," published today.)

We understand lawmakers' claims that the reform package will reduce risks in the EU's banking systems and strengthen the EU's Banking Union. However, many of the changes are necessary simply to implement reforms agreed years ago at an international level. Other reforms adopt, harmonize, and fine-tune policies that EU bank supervisors and resolution authorities are already putting into practice.

That said, we think the reforms are timely. After years of favorable economic conditions across most of the EU, economic growth is slowing and a reversal of macroeconomic trends is possible. As a result, credit risks could increase in many countries where the cost of risk has reached a low point in the cycle. In the same way, liquidity could become topical again if the European Central Bank became less accommodating. All this highlights the usefulness of the new rules in avoiding a repeat of the mistakes of the last financial crisis.

We don't expect the reforms to have any impact on our ratings on European banks, based on our current understanding of the legislation. This is because banks have strengthened their balance sheets in the past few years in anticipation of the reforms, and we already reflect this improvement in our ratings. We expect few changes in how European banks manage their capital and liquidity because of the regulatory reforms.

The reform package will become effective toward the end of this month. It contains amendments to the capital requirements regulation and directive, which will reinforce banks' capital and liquidity and the framework for the resolution of banks that fail.

This report does not constitute a rating action.

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