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EU systemic banks capture huge amount of implicit subsidies

A Greens/EFA study

The Greens/EFA Groups has released today a study on implicit subsidies in the EU banking sector. According to the study, the best estimate of subsidies amounts to 233.9 billion euro. The Study shows that that without these implicit subsidies the large banking institutions in the EU would be making substantial losses. Furthermore, it compares the orders of magnitude of implicit subsidies with the upcoming capital charges and levies that will be imposed on financial institutions and concludes that current policy proposals will only have a marginal effect and will not fundamentally eliminate the distortions created by these implicit subsidies. According to **Philippe Lamberts**, Green member of the ECON committee, who commissioned the study : "This raises fundamental questions about the effectiveness of the combined CRR/CRDIV and BRRD policies to really address the distortions created by implicit subsidies."

FAQ on the implicit subsidy of banks

What are implicit subsidies? Implicit subsidies refer to the gains that banks implicitly obtain due to the expectation that governments will act as guarantor of last resort during a financial crisis. These implicit guarantees bring substantial gains to banks in the form of an implicit subsidy, as creditors on financial markets factor in these guarantees and therefore those that benefit from them can borrow at lower funding rates. They are called implicit - as opposed to explicit - because there is no contractual agreement specifying the amounts or conditions of government support. Currently, governments do not charge taxes or any contribution for these implicit subsidies. **What are the distortions created by implicit subsidies?** Implicit subsidies create significant distortions to markets and are therefore an important policy concern. A first distortion is in the domain of financial stability. Implicit subsidies create incentives for financial institutions to take more risk whilst using a free guarantee. Secondly, in the aggregate this has an impact on the size of the financial sector as a whole because financial institutions use the implicit subsidy to grow larger than they would in its absence. A third distortion is the competitive advantage that receiving banks have over banks without implicit subsidies, which intervenes with the principle of the single market. A fourth issue relates to budgeting transparency as these guarantees are not recognised in fiscal budgets, which leads to problems of fiscal transparency and accountability. Fifth they create an on-going transfer of resources from the real economy and its tax payers to the financial economy and banks. Sixth, these implicit subsidies interfere with the principle of market discipline as depositors, bondholders and shareholders have fewer incentives to monitor the risk profile of banks. Last but not least, they also weigh on public spending via a negative effect on the country rating which increases the total cost of public debt.

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Responsible MEPs

Philippe Lamberts

Member

Attached documents

Implicit subsidies in the EU banking sector study January 2014

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