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Potential for Cooperation: Polish and Czech Standpoints on the Banking Union[1]

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Czech and Polish banking systems are similar in many aspects, such as the predominance of euro area banks in the market and a strong banking supervisory authority. These common features of banking systems translate to similar Czech and Polish positions towards the Banking Union. Their main proposals are to include the specificity of so-called host countries and to maintain the strong position of national supervisory authorities. Although Poland and the Czech Republic will have more reasons to sign up to the Banking Union if they join the euro, these countries should continue to stress the importance of maintaining financial independence between parent banks abroad and their branches and subsidiaries in Poland or the Czech Republic. These countries should promote their monitoring systems as effective methods of providing financial security.

A well-functioning banking system is a crucial part of any large and complex economy, such as that of the Czech Republic, Poland, or Europe. The role of the central banks is to supervise this system and make sure it functions properly. The current debt crisis in Europe was caused, among other things, by banks granting too many high-risk loans. Their problems became the problems of the nation states, and in turn of the whole eurozone, as rising uncertainty in the financial market had a negative impact on real economies, and as governments were forced to offer aid packages. Conversely, rising government debts also affected banks' performances negatively. The weaker banks were cut off from the inter-bank market, and some of them went bankrupt or were taken over. Additionally, as the capital market dried up, real economies deteriorated not only in any particular country, but, because of strong interdependence of the national financial markets within the eurozone, it affected the entire system. That is why the ECB, in its June 2012 Euro Area Summit Statement, highlighted the importance of breaking what it called the "vicious circle" between national governments and banks at the EU level.[2]

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[2] EC (2012): Euro Area Summit Statement, 29 June 2012, www.ecb.europa.eu/ssm/pdf/statement/Euroareasummitstatement2012-06-29EN.pdf.

The EU, notably the highly interrelated eurozone, needed to address several issues linked with the sustainability of the banking sector. One important issue is who should pay for the reckless behaviour of the banks. Is it the taxpayers, the bank bondholders or the banks themselves? Deposit insurance is also an important topic, as the different ways that it operates in various countries can lead to the movement of capital. On the one hand, the banks' risky behaviour can be supported by a high level of insurance, while and on the other, a low level can cause outflow of capital and further economic problems. Another issue is the way in which the banks should be redesigned to be more resilient to the external shocks.

The highly interconnected and mutually dependent banking system of the EU thus requires either a single regulation or a lower level of interconnectedness. As the second option seems unlikely, the eurozone members decided to create a framework package designed for the banking sector, called the Banking Union. This consists of the Single Supervisory Mechanism (to centralise supervision of the banks in the union), a single rule book (particularly in regard to capital requirements), the Single Resolution Mechanism (responsible for efficient risk management of banks facing serious difficulties), and a unified deposit insurance system across the eurozone. The shape of these mechanisms is important not only for the eurozone's highly interconnected banking sectors, but also for Central and Eastern Europe. This is because many of the banks in these regions are subsidiaries of banks with headquarters in the eurozone. Hence the situation of the parent banks affects their operations in the region. The particularities of the Czech and Polish banking sectors and political elites suggest much room for cooperation between Prague and Warsaw—and among Central European Member States more generally—on the issue of the Banking Union.

Similarities and Differences between the Czech and Polish Banking Sectors

Among the similarities between the Polish and Czech banking sectors, the most important is their general good health. Many experts, and certainly most politicians, state that the Czech banking system is very strong. According to Andrej Babiš, the minister of finance, the banks "are very liquid and in very good shape."[3] The governor of the Czech National Bank, Miroslav Singer, also claimed that the Czech financial sector is liquid and well capitalised, and added that it hosts foreign capital and is a net creditor in relation to the eurozone financial sector.[4] The net profit of the Czech banks in 2013 was €2.23 billion and the Core Tier 1 ratio[5] was 16.77 %.

Like in the Czech Republic, Poland's banking sector is very healthy. Its net profit in 2012 amounted to €2.5 billion, the Core Tier 1 ratio amounted to 12.6%[6] and there were no banks with capital adequacy ratio below 8%, which is set as the minimum value for guaranteeing a bank's stability (or of a bank's ability to absorb risks). These good conditions are thanks to the relatively long tradition of a strong and conservative domestic supervision authority, which discouraged banks from loosening their credit policies. The Polish Financial Supervision Authority (UKNF) has stated clearly that the Polish banking sector performed well during the crisis because of the high autonomy of the sector making it resilient to external shocks, a high level of prudence, the actions of state institutions towards the stability of the sector, increasing liquidity, and recommended banks recapitalisations.[7] For instance, in order to increase capital in 2011, the Polish Financial Supervision Authority recommended that the banks did not pay dividends. Also, the UKNF monitored the structure of banks' balances.

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3 "Ministři financí zatím nenašli dohodu na pravidlech záchrany bank," *Investiční web*, 11 March 2014, www.investicniweb.cz/zpravy-z-trhu/2014/3/11/ministri-financi-zatim-nenasli-dohodu-na-pravidlech-zachrany-bank.
4 T. Zavadilova, "Bankovní unie se piblížilam, Česku ještě nehrozí," *E15.cz*, 19 December 2013, http://zpravy.e15.cz/zahranicni/ekonomika/bankovni-unie-se-priblizila-cesku-jeste-nehrozi-1048351.
5 That is, the equity capital and disclosed reserves—the best form of capital to support all of the risk that a bank takes.
6 In Europe, Core Tier 1 amounts to 12%, while Spain's Core Tier 1 equalled 10.6% in June 2013 (see: Spain: Financial Sector Reform—Final Progress Report, International Monetary Fund, February 2014).
7 www.knf.gov.pl/Images/Polski_rynek_finansowy_w_obliczu_kryzysu_tcm75-22870.pdf.

The second point is that, while the Czech and Polish banks are most often subsidiaries of the European banks, they are also quite often their most profitable assets.[8] This may be due to several factors such as high fees or high interest rates. The fact that the banks are subsidiaries (and therefore governed by Czech or Polish regulations), and not branches of the foreign banks (governed by the regulations of their home countries) is crucial for the Czech and Polish positions regarding the common regulation framework of the banks, and to the overall idea of the Banking Union. However, some banks are controlled by domestic capital, either public or private. In Poland, the biggest bank—PKO BP—is largely owned by the state, as is the smaller BOŚ Bank, while Getin Bank is controlled by a Polish private investor.[9] At the end of 2013, Plus Bank emerged after a rebranding, with a name suggesting capital links and strategic cooperation with one of the biggest telecoms companies in Poland, both owned by a Polish private investor. On top of that, there is a well-developed network of Polish local cooperative banks. In the Czech Republic, there are two state owned banks that are supposed to support exports, and only one, FIO Bank, that is fully owned by the domestic capital.

Although Poland's banking sector resembles the Czech one in some ways, there are some differences. While less than 70% (that is, seven banks) of banks' assets in the Czech Republic are subsidiaries of eurozone parent companies,[10] this is true of less than 50% (16 banks) of the assets of banks in Poland. The value of the Polish banking sector (measured in total assets), which amounted to the around €350 billion in April 2014,[11] is also greater than that of the Czech sector, which amounted to €188 billion in March 2014.[12]

The third important issue is that neither country has yet adopted the euro yet, and it is difficult to say precisely when either might enter the eurozone. The Czech Republic is close to fulfilling the necessary criteria to become part of the eurozone (inflation rate, interest rates and budget deficit requirements will probably be met in the near future), although it does not take part in the Exchange Rate Mechanism (ERM II).[13] But, according to a survey from May 2013, 77% of Czechs do not want the euro to be their national currency.[14] This represents a change in public opinion, which until 2005 was largely in favour.[15] One could ascribe this move to, among other things, the strong Eurosceptic discourse at the political level, represented also by the centre right part of the political spectrum.

This reluctance to adopt the euro exists despite the Czech Republic being close to fulfilling all the necessary convergence criteria. But maybe the last factor—the current economic situation—is decisive. The Czech Republic was hit quite hard by the crisis, and it seems that the cuts that followed the economic slowdown added to the recession.

Regarding Poland, the Ministry of Finance said that the country fulfilled the criteria of price stability and long-term interest rates, in October 2013. In the same year, the debt-to-GDP ratio was 57%, so below the reference value. The general government deficit in 2013 was forecasted to reach 4.3% of GDP. Therefore, Poland finds itself in the Excessive Deficit Procedure, with the deadline for correction set for 2015. Still, Poland has not stated when it would enter ERM II, or given any details about a possible date for joining the eurozone. However, increasing number of officials, including Radosław Sikorski, minister of foreign affairs,[16] have pointed to additional arguments in favour of joining the eurozone, linked with the country's security in

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[8] See, for example, M. Novotný, 2014, "Je vstup do bankovní unie pro Českou republiku výhodný?," *Patria Online*, 28 March 2014, www.patria.cz/zpravodajstvi/2598607/je-vstup-do-bankovni-unie-pro-ceskou-republiku-vyhodny.html and UNKF, www.knf.gov.pl/Images/Polski_rynek_finansowy_w_obliczu_kryzysu_tcm75-22870.pdf.

[9] http://biznes.pl/magazyny/finanse/banki/najpotezniejsze-banki-w-polsce-aktywa-pecznieja,5523807,2,magazyn-detal.html.

[10] D. Zsolt, W. Guntram, *Should Non-Euro Countries Join the Single Supervisory Mechanism?*, Bruegel Policy Contribution, 2013.

[11] www.nbp.pl/home.aspx?f=/statystyka/pieniezna_i_bankowa/naleznosci.html.

[12] ČNB, "Rozvaha bankvního sektoru- 2a – Aktiva," https://www.cnb.cz/cs/dohled_financni_trh/souhrnne_informace_fin_trhy/zakladni_ukazatele_fin_trhu/banky/bs_ukazatele_tab02a.html.

[13] MF, CNB, "Vyhodnocení plnení Maastrichtských konvergenčních kritérií a stupně ekonomické sladěnosti ČR s eurozónou," Ministry of Finance of the Czech Republic, 2013

[14] J. Verner, "Češi začínají věřit v přijetí eura, sami jej ale nechtějí," *E15.cz*, 10 May 2013, http://zpravy.e15.cz/domaci/ekonomika/cesi-zacinaji-verit-v-preziti-eura-sami-jej-ale-nechteji-987097.

[15] *Ibidem*.

[16] www.msz.gov.pl/pl/aktualnosci/wiadomosci/informacja_ministra_spraw_zagranicznych_o_zadaniach_polskiej_polityki_zagranicznej_w_2014_roku.

the context of the Ukrainian crisis. The same applies to other Polish politicians.[17] This suggests that the government wishes to introduce the euro sooner than later. The question of a referendum on joining the eurozone is unclear.

The Czech Position on the Banking Union: Cautious Support

The official position of the Czech government, adopted in the coalition agreement, was to assess the possibility of joining of the Banking Union.[18] The government was a little more direct in a policy statement, claiming that it would actively defend its interests in the emerging banking union, including preparations for accession.[19]

The previous caretaker government did not block the process, either and its aim was similar. According to the former prime minister, Jiří Rusnok, the goal was to make sure that Czech supervision over the national financial market would not be weakened.[20] After the deal was agreed in the European Council, Rusnok declared that he was happy with the result, especially regarding maintenance of competences in relation to subsidiary companies of transnational groups.[21]

The discussion about the banking union took place during negotiations within the EU. Due to many uncertainties at the time, the positions of political, economic and academic elites were restrained. For example, Mojmír Hampl, the vice-governor of the Czech National Bank, claimed in April 2013 that it was premature to judge whether the BU would be a project worth participating in. He stated that serious consideration of the value of the union could only happen once the whole project had been created.[22] The analyst Pavel Kohout, from Partners Group, was, in January 2014, also unsure whether the Czech Republic should join. This was simply because it is still an experiment that had yet to be tested, that it was unclear of how is the supervision of 6,000 banks would work, and whether it would be better than supervision by the Czech National Bank.[23] Jiří Dolejš, a member of the reformist wing in the Communist Party of Bohemia and Moravia, endorsed the EU-wide regulation due to the fact that the financial capital also operates at the transnational level, but he also mentioned the stability of the Czech banking sector and did not support joining of the Banking Union quickly.[24] However, economic journalists complained that, unlike in Germany, where the Banking Union was a hotly debated topic (in February 2014), there was no such discussion in Czech political discourse.[25]

In general, the idea of the Banking Union and of the bail-in principle is supported among the decision-makers, but the specific position of the Czech Republic leads to prudent tactics. The stability of the Czech banks means that no immediate decisions are required, and the politicians can wait for the results of the new system. They have secured their authority over the foreign subsidiaries operating in the Czech Republic, and do not have to act until the new institutional framework proves itself useful.

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[17] www.gazetaprawna.pl/artykuly/795504,po-expose-sikorskiego-tusk-gani-kaczynskiego-psl-chwali-a-rp-chce-przyjac-euro.html.

[18] ČSSD, ANO, KDU-ČSL, "Koaliční smlouva mezi ČSSD, hnutím ANO 2011 a KDU-ČSL na volební období 2013–2017," 13 January 2014, www.cssd.cz/aktualne/aktuality/koalicni-smlouva-mezi-cssd-hnutim-ano-a-kdu-csl.

[19] Czech government, Policy Statement of the Government of the Czech Republic, 14 February 2014, www.vlada.cz/en/media-centrum/dulezite-dokumenty/policy-statement-of-the-government-of-the-czech-republic-116171.

[20] F. Zbyněk, "Bankovní unie nakoniec bude," *Parlamentní listy*, 20 December 2013, www.parlamentnilisty.cz/arena/nazory-a-petice/Zbynek-Fiala-Bankovni-unie-nakonec-bude-297752.

[21] T. Zavadilova, "Bankovní unie se piblížilam, Česku ještě nehrozí," *E15.cz*, 19 December 2013, http://zpravy.e15.cz/zahranicni/ekonomika/bankovni-unie-se-priblizila-cesku-jeste-nehrozi-1048351.

[22] M. Hampl, "Should Non-euro Area Countries Welcome the Banking Union? Auf dem Weg zu mehr Stabilität," Europolis Conference, Technische Universität Berlin, 5 April 2013, www.cnb.cz/en/public/media_service/conferences/speeches/hampl_20130405_berlin.html.

[23] O. Tůma, "Očima expertů: Máme vstoupit do bankovní unie?," *Penize.cz*, 17 January 2014, www.penize.cz/ucty-karty/280022-ocima-expertu-mame-vstoupit-do-bankovni-unie.

[24] J. Dolejš, "Evropský projekt bankovní unie, šance a rizika," *Deník Referendum*, 10 April 2014, http://denikreferendum.cz/clanek/17784-evropsky-projekt-bankovni-unie-sance-a-rizika.

[25] J. Macháček, "Žhavé téma bankovní unie," *Rozhlas Plus*, 4 February 2014, www.rozhlas.cz/plus/nazory/_zprava/jan-machacek-zhave-tema-bankovni-unie--1311861.

Poland's Stance: In Support of an Open Banking Union

Poland has taken a position on each of the elements of a Banking Union. Regarding the initial steps (in COM(2012) 510), Poland supported actions to increase the stability of the eurozone banking sector, restoring confidence in the financial sector and cutting the link between public finances and the situation in the banking sector. Simultaneously, it underlined that supervision could be moved to the EU level only if responsibilities are moved there too. This is because Poland wished to increase the power of the local supervisory (home) authorities, whereas the initial roadmap gives more power to host authorities. It also called for the rules of the single market and the specific conditions and interests of all Member States to be respected.[26]

Poland advocated the concept of the "open Banking Union," but this does not mean that it will eventually join this framework. It took the position that participation in the Banking Union cannot be asymmetric, giving advantage to the eurozone states in terms of decision-making within the Single Supervisory Mechanism (SSM).[27] This standpoint was not only underlined by Mateusz Szczurek, minister of finance,[28] but also by Marek Belka, head of the National Bank of Poland.[29]

Poland supported maintaining a balance between the banking systems under the SSM, and those that were not covered by the SSM, and stated that the proposed regulations gave them excessive powers over the non-SSM authorities. Although the concept of SSM seems to be a step in generally the right direction, Poland cannot accept this asymmetry.[30] Neither was Poland convinced about the proposal to include small, local banks in the SSM. A solution could be for non-eurozone states to be represented on the Supervisory Board, as well as giving them access to extraordinary liquidity support. A head of the UKNF underlined that the SSM should be analysed jointly with the CRD IV (Capital Requirements Directive IV) and CRR (Capital Requirements Regulation) package, which negatively affect the powers of national supervisory authorities. These two legal documents allow the capital groups higher level of capital mobility, which could be unfavourable for host countries.

On the Single Resolution Mechanism (SRM), Poland underlined the importance of such a framework for enabling an effective resolution process for the banks. However, in Poland's view, the proper way to implement such a framework is to harmonise the national solutions on this issue, including the specific conditions of the each financial market. Like with the SSM, Poland did not support giving excessive powers to the home countries' authorities at the expense of the host authorities and thus it was not satisfied with the EU's proposal, which seemed to shift powers to a Europe-wide level, while leaving financial responsibilities at the national level. In other words, Poland is concerned about the proposed imbalance of powers between the host and home countries, as well as the solutions on financing of costs resolution and liquidation on the European level (i.e., the resolution would be financed by the local guarantee systems, while decisions on whether to resolve the banks or not will be made on the EU-level, by the European Banking Authority—EBA).[31] In consequence, these solutions would destabilise financial sectors in particular countries. Additionally, the need to build a common resolution fund would mean redirecting resources from the financial markets, thus slowing their development.

Conclusions and Recommendations

Because of the relatively similar characteristics of the Czech and Polish banking sectors, the overall positions are generally also similar. Both are described as host countries, and threatened by the fact that the subsidiaries operating on these markets are not under the control of national regulatory and

[26] Stanowisko Rządu, 25 September 2012.
[27] Projekt stanowiska Rządu, 12 September 2012.
[28] www.ekonomia.rp.pl/artykul/1073923.html.
[29] wyborcza.biz/biznes/1,100896,14132749,Marek_Belka_sceptyczny_wobec_unii_bankowej.html.
[30] Stanisław Kluza, former head of UKNF, presents a similar standpoint to the government regarding the competences and responsibilities (*Gazeta Wyborcza*, 12 October 2012).
[31] Stanowisko Rządu, 13 July 2012, and Stanowisko Rządu, 12 August 2013.

supervisory authorities. Both countries are outside the eurozone. This makes their influence on the behaviour of the bank subsidiaries relatively moderate within the Banking Union. While the ECB is interested in the stability of the financial sector in the eurozone, the non-eurozone financial sectors are not, from the Banking Union perspective, important. Simultaneously, for Poland and the Czech Republic, the financial stability of the eurozone is important as these countries are strongly interlinked with the Euro Area. That is why the Banking Union is a necessary framework for these countries, even if they are not covered by it.

Both countries should draw conclusions from the fact that their regulatory and supervisory authorities were extremely prudential before and in the first phase of the crisis, discouraging banks from taking unnecessary risks and encouraging them to increase their capital. This is contrary to the authorities in several eurozone states, which provided too relaxed rules to the banks, and thus a common financial framework appeared to be necessary. Poland and the Czech Republic should promote their financial authorities as models of best practice for resisting external shocks. That is why they should argue for solutions that include a substantial supervisory power for the national conservative institutions within their jurisdictions.

While Poland and the Czech Republic would have more incentives to join the Banking Union if they acceded to the eurozone, they would also lose the instrument of exchange rate, leading to a weakened ability to absorb external shocks in the financial markets, and increasing the requirement to stabilise finances via the Baking Union. Still, the problems with the uneven competences and responsibilities of the national authorities of the host countries (such as Poland and the Czech Republic) regarding the European banks and their subsidiaries in the host countries would be unresolved. Thus both countries should further promote greater financial independence between the parent banks and their subsidiaries within the Banking Union framework.

In regard to the features of their banking systems, Poland and the Czech Republic do not differ greatly from the other Central and Eastern European countries (CEECs) in the EU. Even if they differ in their stage of participation in the EMU (Slovakia, Slovenia and some Baltic States have already joined the eurozone), they are still host countries with relatively prudential financial supervisory authorities. This translates to a common interest regarding the Banking Union. Thus, Poland and the Czech Republic should seek support from these countries, with a view to influencing the issue of the responsibilities and competences of the host-home authorities and ECB within the framework of the Banking Union.

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