EUROPEAN CENTRAL BANK
BANKING SUPERVISION

Andrea ENRIA
Chair of the Supervisory Board

COURTESY TRANSLATION

Mr Frank Schäffler, MdB
Member of the German Bundestag
Platz der Republik 1
11011 Berlin

Frankfurt am Main, 21 August 2020

Re: Your letter of 19 June 2020

Honourable Member of the Bundestag, dear Mr Schäffler,

Thank you for your letter on the impact of a low interest rate environment on the banking sector, which was passed on to me by your President, the honourable Dr Schäuble, accompanied by a cover letter dated 23 June 2020.

In line with the principle of separation between the European Central Bank's supervisory and monetary policy functions[1], I will address your question from a supervisory perspective.

The potential impact of the low interest rate environment on credit institutions has to be examined from a broad perspective, especially as regards the impact on bank profitability. On the one hand, low interest rates do put downward pressure on banks' interest rate margins. On the other hand, an economic recovery or expansion driven by low interest rates makes it easier for borrowers to repay their loans, leading to better credit quality and thus lower impairments on financial assets. In addition, a favourable macroeconomic environment also supports the reduction of non-performing loans. Moreover, an accommodative monetary policy stance also contributes to an increase in lending volumes.[2] In this regard, I would like to point out that lending has increased in the first two quarters of 2020, especially due to customers drawing on committed credit lines. At the same time, lending standards have tightened only slightly, also because of the government guarantees on new loans. On the whole, these positive effects can offset or even overcompensate for the negative impact of shrinking net interest margins. Nevertheless, the overall effects of low rates on the banking sector need to be carefully monitored. In any event, banks should take the interest rate environment as a given and try to operate as best they can in the current circumstances.

1 As set out in Article 25 of Council Regulation (EU) No 1024/2013 of 15 October 2013 conferring specific tasks on the European Central Bank concerning policies relating to the prudential supervision of credit institutions (OJ L 287, 29.10.2013, p. 63).

2 See https://www.bankingsupervision.europa.eu/press/speeches/date/2019/html/ssm.sp190917~ef6d09493e.en.pdf.

European Central Bank
60640 Frankfurt am Main

Tel.: +49 69 1344 0
E-mail: info@ecb.europa.eu
Website: www.bankingsupervision.europa.eu

Low bank profitability receives a lot of supervisory attention, as shown by the in-depth profitability analysis conducted as part of the thematic review on profitability and business models[3] and the ongoing careful monitoring of the issue. In addition, the ECB had already planned participating in the 2020 EBA EU-wide stress test aimed at capturing the risks for banks from a scenario in which interest rates would remain low for a prolonged period of time. However, the stress test was postponed following the outbreak of the COVID-19 pandemic. Also, the recently published ECB COVID-19 vulnerability analysis assumes a continuing low interest rate environment. The continuing low profitability of significant institutions in the euro area can also be affected by different structural and bank-specific aspects that are unrelated to low interest rates, such as strong competition resulting from overbanking in certain regions. The profitability analysis highlighted the importance of banks' strategic steering capabilities[4] for profitability.

Yours sincerely,

[signed]

Andrea Enria

[3] See https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.thematicreviewprofitabilitybusinessmodels_201809.en.pdf.

[4] Strategic steering capabilities refer to aspects such as banks' cost management and cost allocation across business lines, their loan pricing frameworks, their strategy setting processes and their understanding of income and expense drivers.