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The return to long-term viability

Check Against Delivery
Seul le texte prononcé fait foi
Es gilt das gesprochene Wort

Address at Kangaroo Group Breakfast Debate, European Parliament

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Ladies and gentlemen,

The Kangaroo Group is an optimistically named group – I understand you chose it because of the Kangaroo's ability to cross boundaries and take great leaps forward.

I too am an optimist. I believe that we can turn around the crisis and rebuild our economies for a prosperous future. But we need to be careful. If we are not vigilant and resort to the wrong type of policies, we can also make a depression out of this recession.

Once-in-a-lifetime situation

So let me set the record straight this morning, and also offer some thoughts on how we can return to long-term viability.

We are obviously in a rare situation. But far from being left wanting by this challenge, the competition system has coped quite well with the new demands.

It is hard to say no to protectionism. But you can be certain that is what the Commission is doing and what I will continue to do.

We are working with a speed and flexibility few would have thought possible a year ago. But dealing with these new market failures has not required us to throw out our principles. We will not do that.

Winning that debate – saving the single market - will require strong and sensitive advocacy from people who believe in it, including all of you here today.

Sticking with state aid control

In the current crisis, it is probably necessary that governments step in and use taxpayers' money to help the economy. But let me insist that this spending should be an investment in Europe's future. If state aid does not boost economic growth, it is wasted money. It is not a way out of this recession, only a tax burden on future generations.

And governments can not bail all the sectors that will soon call for help.

Fixing the financial sector

One thing is certain however. The financial sector is a special case – both because of its systemic role in allowing other sectors to function and grow and because of its fragility in times of crisis. It is both the hardest sector to get right and the most important.

The first step of avoiding meltdown has been achieved. After rescues we moved onto recapitalisation. Next we must deal with impaired and toxic assets, and move forward with restructuring banks and the sector at large. Next week, the Commission will therefore present some guidelines explaining how Member States should design State aid schemes to relieve banks from their impaired assets.

Where we are today?

The increasing size and breadth of write-downs borne by financial institutions, and the immediate infections this seems to spread to the real economy is testing policy-makers

This is no time for half-measures or vainly waiting for a perfect solution. It's going to be messy and it's going to be hard.

The costs of the crisis will increase if the root problem of lack of confidence in the financial market is not addressed very quickly.

To fill this trust gap the most crucial thing for governments to do is increase transparency and push the bank restructuring process forward – as part of that process cleansing balance sheets of impaired assets will be a necessary but not necessarily sufficient feature in many countries.

It is true that we can either muddle through with partial guarantee/recapitalisation schemes that leave banks alive but too weak or too afraid to lend – but that would potentially repeat difficulties Japan faced from the early 1990s.

I prefer that we take structural measures that clear balance sheets, restructure or wind down banks and allow the survivors to resume lending without looking back. This is the clearest path to both financial stability of the sector and viability of its major players. This is much better than contemplating mergers between troubled banks. As I heard at the OECD yesterday: two turkeys do not make an eagle.

In this context, the process towards a more stable financial system and viable players needs to be based on clear and consistent rules. To restore confidence, transparent and clear processes and conditions are essential.

And we have to do this in a consistent fashion, without forgetting the long-term. If nations act separately and inconsistently for short-term gain it will be nothing less than a disaster.

This is why I would like today to make an appeal to governments and banking regulators. Please oblige the banks to come clear about the true amounts of the toxic assets they are holding! Let us start again with a clean sheet, knowing the full scope of the problem.

Transparency and truth is the way to re-building trust.

The future

I am convinced that we can rebuild our banking industry for a prosperous future. But we need serious restructuring before the end of 2009. Financial institutions must recognize that for them the future will not be like the past. And by that I mean more than dealing with the bonus issue.

Banks in the future will certainly be subject to stricter governance. Unsustainable, overleveraged structures will be replaced by simpler, less leveraged, more risk-averse and more transparent forms of banking. Banks will predominantly rely on retail funding, and they will need to focus on their core-business.

In other words, we may well see the return to "classic banking", driven both by increased regulatory pressure and the need for banks to adapt their businesses to new capital constraints.

Banks will also need to improve their risk-management capabilities and consider exiting from products and markets where they have little sustainable competitive advantage. They may also finally realise that diversification across countries can stabilise their revenue streams. This should result in new banking structures, with smaller leaner banks but maybe also with bigger cross-border banks, and hopefully the emergence of global players headquartered in Europe.

Secondly, whilst being neutral as to ownership or business models for financial institutions, it is essential that the future market structure is competitive. A lack of competition would not only lead to the usual monopoly distortions (extraction of monopoly rents to the detriment of customers, productive and allocative inefficiencies, etc.), it may also contribute to the creation of banks which are deemed too big to fail. Finally, it may make banks depend on taxpayers' money for longer than necessary as they would not be pushed to restructure with a view to return to viability.

The Commission will in any case support the restructuring process that has to come from European banks, through its State aid control procedures.

Uniting into the future

I don't think we at the Commission have all the answers.

I am here today – to listen as well as to inform; to remind you that there is much we can agree on and to ask for your support. The Commission will need it to keep the single market functioning and to get banks and the economy back on the right track.

It's going to be a case of needing 'all hands on deck' and I hope I can count on yours amongst them.