European Securities and Markets Authority

EBA EUROPEAN BANKING AUTHORITY

EUROPEAN INSURANCE AND OCCUPATIONAL PENSIONS AUTHORITY

JOINT COMMITTEE OF THE EUROPEAN SUPERVISORY AUTHORITIES

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PRESS RELEASE

ESAs see continued risks in EU financial markets and call for rigorous action on assets and liabilities

The European Supervisory Authorities (ESAs) for securities (ESMA), banking (EBA), and insurance and occupational pensions (EIOPA) have today issued their August 2015 Joint Committee Report on Risks and Vulnerabilities in the EU financial system. The joint risk report informs on risks in the EU financial system (banking, securities and insurance sector), with a particular focus on cross-sectoral vulnerabilities and developments.

The joint risk report identifies that risks to the EU financial system have persisted since March 2015. Risks resulting from low interest rates, search for yield and low profitability of financial institutions remain present, along with risks related to reductions in market liquidity and their possible implications for asset managers. The fragile recovery of European economies continues to adversely affect profitability and asset quality of the EU's financial sector.

Currently, the main risks challenging financial stability in the EU are:

- the low interest rate environment and its impact on the profitability and business model sustainability of financial institutions;
- the continued search for yield by financial institutions and the associated mispricing of assets;
- political and economic risks due to residual uncertainty around Greece's financial situation;
- financial market volatility and structural concerns about economic prospects of emerging market economies, in particular in China; and
- reductions in market liquidity;

ESAs call for rigorous action on asset quality and business models

The ESAs' report highlights the need for further efforts by financial entities to clean-up balance sheets, to address legacy assets and non-performing loans – this includes assessing the sustainability of business models as a key supervisory concern. The report stresses a specific need for coordination when conducting such assessments for cross-border and cross-sector institutions. It also points to the risks of valuation risks in illiquid markets and emphasises the transparent disclosure of risk exposures (e.g. as part of periodic financial reporting). The report also calls for further appropriate and harmonised regulation promoting the adequate marketing of investment products and complementing recent plans to support market-based funding.

ESAs see further risks looming ahead

The joint risk report also identifies some potential risk drivers for the developments ahead. It highlights the possible re-emergence of concerns on sovereign debt sustainability, reflecting high public and private sector indebtedness, large fiscal deficits and insufficient fiscal consolidation in some countries. This could trigger a change in market sentiment if a further tightening in credit spreads would not be in line with future economic developments. Such concerns apply particularly in the euro area, also in reaction to potential adverse developments regarding the long-term development of the Greek economy. Another potential trigger for a change of sentiment in European markets could be increasing international risks, e.g. following heightened market volatility, structural concerns about China's economy, fluctuations in commodity prices or divergence of monetary policy conditions between major jurisdictions. Adverse spill-over effects from China, or other emerging market economies facing reduced growth, could provide further challenges to the EU economy.

Notes for editors

1. August 2015 Joint Committee Report on Risks and Vulnerabilities in the EU financial system

2. The Joint Committee is a forum for cooperation that was established on 1st January 2011, with the goal of strengthening cooperation between the European Banking Authority (EBA), European Securities and Markets Authority (ESMA) and European Insurance and Occupational Pensions Authority (EIOPA), collectively known as the three European Supervisory Authorities (ESAs).

3. Through the Joint Committee, the three ESAs cooperate regularly and closely and ensure consistency in their practices. In particular, the Joint Committee works in the areas of supervision of financial conglomerates, accounting and auditing, micro-prudential analyses of cross-sectoral developments, risks and vulnerabilities for financial stability, retail investment products and measures combating money laundering. In addition to being a forum for cooperation, the Joint Committee also plays an important role in the exchange of information with the European Systemic Risk Board (ESRB).

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