EUROPEAN CENTRAL BANK

EUROSYSTEM

ECB-PUBLIC

Christine LAGARDE
President

Mr Billy Kelleher
Member of the European Parliament
European Parliament
60, rue Wiertz
B-1047 Brussels

Frankfurt am Main, 21 April 2020

L/CL/20/107

Re: Your letter (QZ-008)

Honourable Member of the European Parliament, dear Mr Kelleher,

Thank you for your letter to Mr Andrea Enria, Chair of the ECB's Supervisory Board, which was passed on by Ms Irene Tinagli, Chair of the Committee on Economic and Monetary Affairs, with a cover letter dated 9 March 2020. As you raised an issue which is beyond the scope of the ECB's supervisory tasks, Mr Enria forwarded your question to me.

You refer to the heterogeneity of bank lending rates across euro area countries and, in particular, the comparatively high level of lending rates on mortgages and loans to small and medium-sized enterprises (SMEs) in Ireland.

Bank lending rates to euro area firms and to households for house purchase have declined substantially, by around 140 basis points and 150 basis points respectively, since the ECB announced credit easing measures in mid-2014. Borrowers have benefited from very favourable lending rates, which are currently hovering around historical lows. In addition, the dispersion in rates for new lending to euro area firms declined between 2013 and February 2020 (the latest available data). During that period, the level of heterogeneity in lending rates across euro area countries was generally lower and more stable for housing loans than for loans to firms. The EU institutions, including the ECB, and national governments have announced – and are currently working hard on – measures to alleviate financing pressures on firms and households, which are suffering from the impact of the coronavirus (COVID-19) on bank lending.

In the specific case of Ireland, there have been considerably smaller declines in bank lending rates since mid-2014, by around 50 basis points for loans to households for house purchase and by around 40 basis points for loans to firms. Over the same period, lending rates for very small loans have declined by around 90 basis points in Ireland, while they have declined by more than 230 basis points on average across the euro area.

Bank lending rates are determined by a number of factors, such as the economic situation and outlook, the creditworthiness of borrowers, interest rate fixation periods, loan maturities and market reference rates, as well as by specific features of the banking system. The need for consolidation of bank balance sheets after the financial and sovereign debt crises, high levels of non-performing loans and a lack of competition in the banking sector can lead to higher levels of bank lending rates in certain jurisdictions. Households and SMEs are likely to be more severely affected by low levels of competition in the banking sector, as they have a weaker negotiation power than large firms. These factors explain a large part of the heterogeneity in bank lending rates across euro area countries.

In Ireland, lower levels of competition in the banking sector, the stock of non-performing loans and the need for consolidation after the financial crisis are relevant factors which have contributed to the more limited pass-through of the ECB's accommodative monetary policy stance compared to other countries.

In addition to national measures to increase competition, which fall outside the scope of the ECB's monetary policy mandate and prudential supervision tasks, and ongoing improvements of the resilience of the banking system, further progress towards completing the banking union could help to strengthen the banking sector, enhancing cross-bank mergers and acquisitions, cross-border lending and competition between banks.[1] Furthermore, the EU's work towards a capital markets union should also help to diversify further the range of external funding sources available to borrowers, reinforcing financial integration in the EU. One condition for progress in this direction is to further harmonise legislation and regulations across the EU. Overall, completing the banking union and the capital markets union should contribute to reduced financing costs for firms and households.

Yours sincerely,

[signed]

Christine Lagarde

[1] See also https://www.oireachtas.ie/en/debates/debate/joint_committee_on_finance_public_expenditure_and_reform_and_taoiseach/2018-11-08/2/

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