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# Conference on European Economic Integration 2022

## Economic and monetary policy under wartime conditions – implications for CESEE

*Compiled by Antje Hildebrandt<sup>1</sup>*

This year's Conference on European Economic Integration (CEEI) was held in November 2022. The annual conference hosted by the Oesterreichische Nationalbank (OeNB) was organized in a time in which the world is facing a concurrence of crises: the war in Ukraine and the ongoing recovery from COVID-19 on top of the effects of climate change. While differing very much in nature, these crises all have a decisive effect on economic and monetary policy. The aim of the CEEI 2022 was to develop a deeper understanding of how these transformational crises are likely to impact the economies of Central, Eastern and Southeastern Europe (CESEE) in the short and medium term. More than 400 participants from various countries attended the conference in person or online.

OeNB Governor *Robert Holzmann* opened the conference by pointing out that unlike in pre-industrial times, there is little economic rationale for war today. He quoted the German philosopher Immanuel Kant who stated as long ago as the end of the 18<sup>th</sup> century that “the spirit of trade cannot coexist with war.” Austria's chief central banker stressed that military conflicts usually benefit only a few individuals and companies, while inflicting suffering on the vast majority. Pivoting to the current Russian invasion of Ukraine, Governor Holzmann acknowledged that economic sanctions have not left as deep a mark on the aggressor's economy as was largely expected. However, he expressed confidence that sanctions will bite harder in the longer run. Looking at the European economy, even though it has fared better than expected so far in 2022, the Governor cautioned that the economic consequences of the conflict have darkened the short-term economic outlook and pushed up inflation. In contrast, medium- and long-term impacts of the war will depend on future evolvment. However, they might bring opportunities for the European economy e.g. in the form of nearshoring or trade diversion in its favor. Governor Holzmann moved on to stress that while the war has pushed other enormous challenges the human race has been facing, namely the pandemic and climate change, somewhat into the background, they will have to be brought back to the forefront soon. The host of the conference concluded his introductory statement on a positive note. He believes that despite the widespread doom-mongering, there is no compelling reason to be too pessimistic about global developments in future. No matter how improbable it may seem today, it is well possible – and in fact necessary – that the West and (hopefully a new) Russia will find a way to co-exist peacefully, while meeting the security needs of both Ukraine and Russia.

In the ensuing keynote lecture, *Graciela L. Kaminsky* from George Washington University compared the current triple crisis in the form of the pandemic, global

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economic crisis and war on European soil with past crisis episodes (particularly) in CESEE. A general stylized observation is that the severity and persistence of past crises tend to be larger in the case of crises which started in the financial sector. Professor Kaminsky sketched out imbalances that had built up in the run-up to the global financial crisis in CESEE. Large current account deficits, external debt and exuberant credit growth fueled by dramatic capital inflows amid falling USD interest rates had created a lot of intrinsic instability and overheating. After the crisis was triggered in the US and spread out across the world, CESEE countries faced partially large exchange rate depreciations and reserve losses. In contrast, the genesis of the current crisis was very different as there were no signs of worrisome economic overheating this time. The current economic malaise was not preceded by massive current account deficits. External debt – even though still partially high – has declined over the last decade. Moreover, there was no credit bonanza prior to the current crisis. While real estate prices did increase, the extent of this was nothing in comparison to the bubble before the global financial crisis of 2008–2009 (GFC). Professor Kaminsky allocated the roots of these crucial differences to the fact that the GFC started out in the financial sector in the US and that the current crisis was thus not heralded by dramatic bonanzas. She concluded her lecture by saying that even though the impact of the crisis is likely to be less severe this time there are still risks that need to be kept closely monitored as we look ahead. In particular, a close eye needs to be kept on rising global economic uncertainty, mounting financial fragilities and sovereign risk especially in Latin America, South Asia and Africa. In the ensuing discussion, participants from the audience remarked that it is crucial to make a distinction between the role of private and public borrowing. In order to safeguard financial stability in the aftermath of the GFC, the public sector had to bail out the private sector thus increasing its indebtedness. While capital controls could help, they also bear the risk of introducing distortions. Another conference participant commented on the first signs of a bust that we are starting to observe. Against this background he was wondering about the odds that deflation rather than inflation will be Europe's main concern in two years' time.

*Gerhard Fenz*, Head of the OeNB's Business Cycle Analysis Section, chaired session 1 on economic prospects beyond the war. In his introduction, he pointed to the sequence of crises and their combined effects on economic development, the effects of the decoupling of Russia, and the reconstruction of Ukraine as important issues for discussion.

The first speaker in session 1, *Elena Flores Gual*, Deputy Director General, European Commission, highlighted that EU economies were coming out of the COVID-19 crisis when Russia's war against Ukraine started. Some challenges were already present, such as signs of emerging inflation. The war brought about rising commodity prices, further supply chain disruptions and uncertainty. Flores Gual drew attention to risks of economic divergence in the EU due to different exposures to war-related shocks. She emphasized that it was important to get the mix between fiscal and monetary policies right. Fiscal support for high energy prices should be temporary and well-targeted, while excessive distortions in price signals should be avoided. She argued that the green transition has to continue, which would entail a large need for investment. With regard to Ukraine, Flores Gual pointed to the EUR 18 billion support package for 2023 that the European Commission proposed recently.

Subsequently, *Franziska Ohnsorge*, Manager of the Prospects Group at the World Bank, gave a global perspective on the outlook for growth and inflation. She showed that currently the global economy is facing the fourth-steepest slowdown since 1970. Moreover, she highlighted the sharp downward revisions of short-term growth forecasts made in the course of 2022. Then she elaborated on inflation developments, globally and in different regions of the world. The World Bank's model-based global CPI inflation projections show that inflation is expected to decline from record highs but will remain above the 2015–2019 average until the end of 2024. In this projection, energy prices will no longer drive up inflation starting from 2023. Finally, she made the point that even under a global recession scenario triggered by sharp monetary tightening, inflation would stay elevated through 2024.

The third speaker of this session *Mario Holzner*, Executive Director, The Vienna Institute for International Economic Studies, focused on CESEE. He highlighted the region's dwindling importance in the world economy. Holzner also showed that some CESEE countries are among the most open economies worldwide. Based on a survey conducted among German companies, Holzner brought in some thoughts about the potential for nearshoring. He pointed to the unprecedented demographic decline in CESEE countries as a major challenge, particularly in the working age population. With regard to the upcoming economic slowdown, he argued that the EU Recovery and Resilience Facility will act as an important shock absorber. In this context, Holzner stated that Western Balkan countries should get more access to the EU budget and that the NGEU package was a missed opportunity in this respect. He also made clear that Ukraine will not be able to finance the enormous costs of reconstruction from its own resources.

After delivering their presentations, the speakers discussed questions and comments from the audience. Issues addressed included the new EU fiscal rules, model assumptions with regard to the World Bank scenarios as well as dependence on Russian energy and essential nonenergy imports. It was also discussed how far it would be realistic for the EU to increase its transfers to Western Balkan countries.

In opening the first panel discussion, OeNB Governor *Robert Holzmann* pointed to continuously high and still rising inflation and high uncertainty and invited his colleagues from two inflation-targeting countries, Poland and Romania, to explain how they assess the role of global policy spillovers and what role exchange rate developments play in their conduct of monetary policy. Deputy Governor *Leonardo Badea* from the National Bank of Romania (NBR) noted that spillovers from euro area policy are felt primarily in exports, but nevertheless the NBR puts its focus primarily on inflation rather than on the exchange rate. The NBR started its tightening cycle by reducing unconventional measures before raising interest rates. The fight against inflation was conducted in a balanced way without harming economic growth. *Marta Kightley*, First Deputy Governor of the National Bank of Poland (NBP), explained the current high inflation level in Poland (almost 18%) by the rather successful performance of the country in the pandemic. With a relatively mild recession of only  $-2\%$  in 2020, Poland mastered the first recession since the start of transition relatively well. This was followed by a fast recovery, backed by the fiscal impulse, strong export demand and low unemployment, which in turn led to faster consumer price growth than in the euro area. Yet, the NBP started its hiking cycle somewhat later than other central banks in the region. Given a high

share of variable loans in Poland and the strong impact on the economy, this hiking cycle has now been paused and the peak of inflation is expected to be passed soon. In Kightley's view, exchange rate developments are mostly driven by the geopolitical situation and less by NBP policy. Yet, in her view, spillovers from the euro area's monetary policy help to tame inflation as this policy implies an appreciation of the PLN against the USD.

Prompted on comparatively lower inflation in Albania, Governor *Gent Sejko* from the Bank of Albania referred to two factors: lower energy prices as a result of low import dependence for electricity as well as a strong exchange rate which results from capital inflows related to FDI, tourism and remittances. In contrast, the rather high inflation in the Baltic countries is ascribed to the special consumption basket in the region with above-average weights for heating and fuels according to Governor *Gediminas Šimkus* from the Bank of Lithuania. Referring to Lithuania's exposed position, he emphasized the advantage of being a member of the EU, NATO and the euro area. While Lithuania failed to join the euro area before the global financial crisis, it has entered the pandemic with strong fundamentals which were also backed by euro area membership. Marta Kightley countered that, for Poland, the same recipe would not have worked as the exchange rate acted as a buffer in the global financial crisis, thus helping Poland to avoid a recession then. Leonardo Badea joined the discussion by pointing to the importance of credibility. He stated that Romania would be better inside the euro area even though current monetary policy independence can help to alleviate idiosyncratic shocks.

Governor Holzman inquired about the role of ECB liquidity lines to the region during the pandemic, which were likely helpful in stabilizing capital flows and asked about potentially remaining pockets of risks in local housing markets or from the fiscal side. Gediminas Šimkus noted the important role of macro- and micro-prudential policies which have to be considered a marathon, not a sprint. Gent Sejko saw a major challenge from banking sector consolidation in Albania while housing market risks appear to be well manageable. In Poland, the situation was stable as house prices had long been rising in tandem with incomes. Although rising interest rates and the high share of variable rate loans pose a challenge, the banks are well capitalized. The BNR also considers the banking sector to be resilient in Romania but is remaining vigilant according to Leonardo Badea.

Prompted on a potential financial stability risk arising from the high share of variable rate loans in Poland, Marta Kightley emphasized that this also supports the monetary policy transmission. However, the rapid increase in installments for households may justify targeted measures. Gediminas Šimkus added that risks for households can and should be limited via borrower-based measures, such as debt service-to-income ratios and the like. On Governor Holzman's initial question on the future of repo lines, Gent Sejko underlined the usefulness of the instrument and noted that Albania had already renewed its repo line with the ECB. Gediminas Šimkus pointed out the clear set of rules by the ECB according to which liquidity lines are granted.

In session 2, chaired by *Soňa Muzikářová*, macroeconomist and policy advisor, three panelists discussed the topical issues of flight and migration, brain drain and population aging in the CESEE region. In her introductory remarks, *Olga Popova*, senior researcher at the Leibniz Institute for East and Southeast European Studies, drew attention to the high share of people with migration intentions in CESEE

countries. She further touched upon employment gaps between immigrants and refugees in the EU: Refugees start with a larger disadvantage in terms of employment probability than (economic) immigrants. While both groups eventually catch up with natives, the process takes considerably longer for refugees. Relying on Czech data, she argued that current refugees from Ukraine are economically very active and half of the economically active are in paid work. Wages of refugees are low, however, not least due to skill mismatches. She concluded that support in language acquisition as well as the recognition of qualifications are particularly important integration policies. *Isilda Mara*, senior economist at The Vienna Institute for International Economic Studies, highlighted changing mobility patterns in CESEE. While most countries in the region were net senders of migrants, more recently some had turned into net receivers. Changes are also visible in terms of migrants' education: while Western Balkan countries still face net outward migration of the highly skilled, other countries such as Estonia, Poland or the Czech Republic became net receivers of highly skilled migrants. She also emphasized that the pandemic increased remote and online work – telemigrants are becoming more frequent and might reverse the trend of brain drain. *Róbert Iván Gál*, senior researcher at the Hungarian Demographic Research Institute, focused on demographic developments in the region and painted a rather optimistic picture: he emphasized the considerable increase of the effective retirement age in most countries of Central and Eastern Europe and highlighted that life expectancy at the age of retirement was not increasing. Gains in life expectancy were thus absorbed by the labor market and did not increase the years spent in retirement. Pointing toward strong improvements in human capital, he saw scope for further increases of the retirement age in the future.

The subsequent discussion focused on refugees from Ukraine and their potential to alleviate labor shortages in the CESEE countries. Panelists argued that while Ukrainian refugees tend to be highly educated, the majority of refugees are women, many with childcare duties. Also, labor shortages prevail largely in male-dominated professions and for these reasons panelists' confidence in Ukrainians easing labor shortages in a significant way was limited. Panelists further doubted that the current influx of Ukrainian refugees would lead to a paradigm shift in CESEE countries' openness toward immigration.

Amid the overall gloomy and highly challenging outlook which was at the heart of many discussions, the day ended on a positive note when *Sanja Tomićić*, Executive Director, Hrvatska narodna banka, delivered her dinner speech, reviewing Croatia's successful integration process, which will culminate in the adoption of the euro on January 1, 2023. The preparations for this important step started a rather long time ago and she reminded the audience that joining a monetary union is a marathon, albeit one that includes some sprints. Croatia had pursued an ambitious time frame and started from a difficult initial position. After the global financial crisis, it fell into a six-year-long recession which almost caused enthusiasm for the project to disappear. In addition, the procedure for entering ERM II was anything but clear for the Croatian authorities. Yet, in mid-2013 the country joined the EU and the 2016 New Year's meeting hosted by the Prime Minister revived the process. A strategic document was launched including a detailed cost-benefit analysis, the discussion of economic policies consistent with euro introduction started and after the presentation in October 2017 a road show started throughout



the country. Sanja Tomićić shared her experience that sometimes fast moves are necessary to capture opportunities when they arise: the time of good economic performance in Croatia allowed tightly set fiscal targets to be achieved so that Croatia could exit the excessive deficit procedure. The rest – so to say – is almost history: Croatia joined the ERM II in July 2020 and engaged in close cooperation within the newly established Single Supervisory Mechanism. Yet, two more unexpected stumbling blocks appeared in late 2019 when an earthquake struck the capital city area and the pandemic broke out. But there was no time to be paralyzed by these events; instead Croatia made the best out of the EU presidency, which it was holding at this time. Thus, since July 2020, focus could be put on administrative and operational issues until sharply rising global inflation and the Russian attack on Ukraine suddenly threatened the timeline for euro adoption. Fortunately, the inflation criterion was met and the EU and ECB convergence reports gave the green light in June 2022. Despite some criticism, financial market indicators show that Croatia's economy is ready for the euro. Also the majority of the population supports it, even though this is already the third currency changeover since the start of transition. Tomićić concluded by expressing gratitude for the support that Croatia has received from the European Commission, the ECB and not least from the OeNB through a bilateral informal dialog that had started back in 2005. The discussion centered around potential inflationary effects from euro introduction as well as Croatia's experience in dealing with high inflation that the new member would be able to bring to the ECB's governing council.

*Birgit Niessner*, Director of the OeNB's Economic Analysis and Research Department, opened the second day of the conference by referring to the fast-changing nature of Europe's energy dependency. In particular, dependence on gas from Russia has been high in Europe, especially so in the CESEE countries, and Russia had already ceased to be a reliable supplier of gas to Europe before it invaded Ukraine and triggered sanctions. As a consequence, many countries, in particular the Baltic countries, Poland, Romania and Croatia, decreased their dependence on Russian gas sharply. The EU Economic and Investment Plan for the Western Balkans will also work in this direction. *Guntram Wolff*, Director and CEO of the German Council on Foreign Relations, started his speech by pointing to the important role of gas for Europe. While prices rose sharply in response to supply shortages, the industry reacted very flexibly by relocating energy-intensive parts of production. He distinguished between short-term and medium-term consequences of the supply shortage caused deliberately by Russia: the redirection of gas flows occurred in a very short time. The importance of Norwegian gas and liquified natural gas (LNG) have increased and Germany has become a hub from West to East. In addition, measures such as the German gas price cap also include incentives to save gas. Wolff emphasized that adjustment must take place with the fewest possible frictions in order to avoid any suffering of the deeply integrated EU supply chains. In the medium term, Europe must build on projects of common interest with a strong focus on Southern and Southeastern European countries. The increase in wind and solar energy in the last few years was moderate and energy generation from renewables peaked in 2020. If all measures from the REPowerEU plan were to be implemented, Russian gas could be entirely replaced within five years. The huge increase in imports of solar panels from China observed since the start of the war can partly be attributed to price increases (which he also considered temporary)

but there was also an increase in terms of gigawatts to be produced. In addition, the significant buildup of LNG import capacity via floating or fixed terminals represents good news for Europe. Wolff concluded by alluding to the necessity to maintain the integrity of the energy market. Germany will increasingly function as a transit hub and the West-East flow of gas will be complemented by North-South flows including the Baltics and the Balkans. European, and especially Norwegian, infrastructure needs to be protected against hybrid attacks. Yet, the EU must be mindful to avoid building up new dependencies. In the ensuing discussion he clarified that this does not mean that Europe should reshore energy supply and production processes entirely. However, diversification of sourcing countries is key. Prompted on fiscal coordination in Europe he referred to the fact that the powerful “double ka-boom” in Germany has made this discussion obsolete.

The third session chaired by *Bernhard Grossmann*, Head of the Office of the Fiscal Advisory Council and Productivity Board at the OeNB, focused on what fiscal policy can do to alleviate the negative impact of high inflation and commodity price surges on the economy in the short run. How to avoid social unrest while stepping up sanctions against Russia? And how to preserve fiscal space in times of crisis?

*Baiba Brushārde*, Chief Economist of the Macroeconomic Analysis Division at Latvijas Banka discussed the short-term fiscal policy response of Latvia that aims at both protecting all vulnerable low- and middle-income households against extreme price increases and retaining incentives to save energy. Only households that have insufficient disposable income after deducting all necessary housing and heating expenses are eligible for direct benefits. The monitoring of the state support by the central bank shows that the targeted measures dampened the inflation increase in 2022 and will contribute positively to GDP growth in 2023. The Latvian experience demonstrates that a broad information campaign is necessary since vulnerable households are typically less informed.

*Belma Čolaković*, Chief Economist at the Central Bank of Bosnia and Herzegovina emphasized the role of country specifics in tailoring short-term fiscal policy responses to the energy crisis in CESEE. For instance, Western Balkan countries have a comparably higher share of vulnerable households with little savings and very low incomes. Price shocks hit consumers differently due to the high weight of food items in the consumption basket, which amounts to about 33% compared to 11% in the euro area. She also pointed to the strong dependence on fossil energy, which goes beyond consumption patterns and also implies labor market dependencies. Hence, the region appears to be locked into unsustainable energy production and consumption. Alluding to stepped up sanctions against Russia, she mentioned the rather low direct economic impact on Western Balkan economies, including Bosnia and Herzegovina, due to comparatively low trade volumes and low dependency on Russian oil and natural gas. Only Serbia may be somewhat more dependent.

*Zsolt Darvas*, Senior Fellow at Bruegel, agreed that the current situation warrants government support to vulnerable households. Fortunately, surprise inflation temporarily increases the fiscal space of governments through higher tax revenues and falling debt-to-GDP ratios. However, state support measures should restore affordability without fueling further inflation. Particularly, they should not weaken the price signal because some underlying factors of the inflation spike will



be long-lived. Hence strong price signals are important to foster adjustment and reallocation – accompanied by structural reforms. Finally, measures need to be (and should have been more) targeted, temporary and tailored to preserve fiscal space even during crisis times. The EU Recovery and Resilience Facility will play an important role in stepping up the short-term fiscal policy response and fostering the urgently needed transition to less dependency on fossil fuels and more generally to a green economy. In the medium- to long-term, fiscal sustainability also requires countercyclical policies during good times.

Zsolt Darvas noted that energy and producer prices had already started to increase rapidly prior to the Ukraine war. Moreover, the drop in the supply of gas to the EU was caused by Russia and not by EU sanctions. Additionally, EU sanctions are gradually becoming more and more effective, impacting Russia's manufacturing adversely and eroding its productive capacity. According to mirror trade statistics, Russia is cut off from high technology from non-EU countries too, and Russian imports and exports dropped except for fossil fuels. Moreover, people need to be reassured on energy security.

Session 4 under the title “Addressing long-term supply challenges via structural policies and green transition” was chaired by *Julia Wörz*, Head of the OeNB's Central, Eastern and Southeastern Europe Section. She asked whether the current multiple shocks, and responses to them, are accelerating or slowing down the green transition. *Veronika Grimm*, Member of the German Council of Economic Experts and Professor at Friedrich-Alexander-Universität Erlangen-Nürnberg, spoke of a gas price tsunami that had already started before the war and will not disappear before 2024. Gas prices will stay structurally higher in Europe than in America and Asia, which implies that here hydrogen will sooner become competitive to gas. Grimm commended Germany's well-targeted gas cost subsidies. EU policies, however, should ease the subsidy pressure with new energy supplies mobilized through common gas procurement, expansion of renewables, temporary reactivation of nuclear power sources and coal, and energy efficiency. She also stressed the need to prepare for green hydrogen. In order to avoid new dependencies on raw materials critical for the green transition she advocated diversity, not to be confused with “friend-shoring.”

*Elena Paltseva*, Associate Professor at the Stockholm Institute of Transition Economics, asked whether the EU gas crisis is mobilizing the green transition. She said that the share of Russian gas fell from 45% to 18% of EU imports while LNG increased its share to 39%. However, the massive gas infrastructure investment currently being undertaken is not necessarily good news for the green transition, since natural gas is essentially methane, and LNG imports – typically shale gas from the US – emit twice as much greenhouse gases (GHG) as Russian pipeline gas. Moreover, new investment creates carbon lock-ins and eventually would become stranded assets. To reduce the implied uncertainties, Paltseva proposed first to assess LNG infrastructure investment correctly, second to mobilize existing infrastructure and third stimulate sustainable energy investment.

*Thomas Reininger*, Senior Principal at the OeNB, spoke about the green transition in CESEE EU member states, most of which have lagged behind in terms of reducing their carbon intensity relative to GDP per capita. While their GHG emissions had fallen sharply from 1990 due to economic transition, since 2008, they have made only small progress. Energy industries' emissions are substantially

larger in CESEE than in the EU-16, while the opposite is true regarding the transport sector – of course, these region-wide aggregates mask great variability at the country level. On the upside, the post-pandemic EU funds envisaged for spending in 2021–2026 appear to appropriately address climate-related weaknesses in energy industries, energy efficiency and transport in CESEE EU, according to their national recovery and resilience plans. These countries tend to benefit most from the EU grants, generally dedicated by more than 40% to climate-related measures. The subsequent discussion on all three presentations covered a variety of issues such as labor shortages, the role of biogas, cycle economy, the insufficiency of funds alone and the low public acceptance of green transition in CESEE.

The CEEI concluded with a second panel discussion titled “Banks in transition: is there a need for rescoping toward sustainable markets and products?” The OeNB’s Vice-Governor *Gottfried Haber* kicked off the exchange of views among distinguished bank practitioners by sketching out the turning points that we are currently facing in several respects. These include inflation, recession, rising interest rates, limitations on the supply side and at the same time globally rather tight labor markets. Vice-Governor Haber pointed out that European banks have built up resilience over the last decade, but it remains to be seen whether it will suffice in the future.

*Elena Carletti*, Professor at Università Bocconi, pinpointed three key elements of the current uncertainty. First of these is the geopolitical instability in Europe, which is neither predictable nor controllable. Second, in a striking contrast to the pandemic, during which economic policies were largely aligned, currently there is a significant divergence between monetary and fiscal policy. Third, while it is relatively easy for banks to assess their direct exposure to the countries involved in the war, it is much more difficult to assess the spillover effects. Models based on history are no longer informative so that much more forward-looking analysis is needed. Turning to the issue of high interest rates, Professor Carletti explained why they are boon and bane for banks at the same time. Banks not only benefit from high rates but also face risks from them. It is not only credit risk that needs a watchful eye but also interest rate risks related to banks’ derivatives exposures. In reaction to a question about the risks of a rising sovereign-bank nexus, Professor Carletti stressed that the banks are not only exposed to (worldwide) increased government debt but also to government guarantees stemming from the pandemic. Nonetheless, despite the intensified sovereign-bank nexus, she senses a bigger risk in the fragmentation of sovereign spreads in Europe.

*Gunter Deuber*, Head of Research at Raiffeisen Bank International, started out by referring to the main theme of the conference and emphasized that his bank is conducting banking under war conditions, which has only been possible thanks to thousands of employees in Russia, Ukraine and Belarus. He moved on to point out that Western banks have been de-risking and shifting away from Eastern European countries toward more predictable EU markets since 2014. Yet a turning point has occurred not only on the geopolitical level but also on the funding side. This is because times of ample deposit funding are coming to an end and at the same time bond market funding has become more expensive. There will be a certain competition for deposits because major disposable income losses are still ahead of us. However, green funding provides an interesting opportunity, especially in the CESEE region, where this market segment is still rather underdeveloped.

*Boštjan Jazbec*, board member of the Single Resolution Board, played – in his own words – the devil’s advocate by pointing out that despite significant efforts there is still not much of a European banking system. We rather have competing national banking systems which are mainly preoccupied with supporting their national economies as the rather stagnant level of cross-border lending over the last twenty years suggests. Even the Basel regulation does not treat the euro area as a common market since it requires additional capital buffers for cross-border activities. On a more positive note, Jazbec stated that we have managed to build rather resilient banking systems and that despite recent major shocks the prophecies of doom about the next financial crisis have not materialized. This is not least due to the stricter regulatory and supervisory framework which, however, at the same time is reaching the point where it obstructs banks’ profitability and business models. Jazbec also cautioned against the view according to which the European market as a whole is overbanked as two out of three banks in Europe are in Germany and Italy. He concluded his initial statement by saying that we have still not completed the banking union. We are still only at its second pillar – the Single Resolution Mechanism (SRM) – which is still very fragmented in the sense of different insolvency regimes in different countries. The third pillar – the European deposit insurance scheme (EDIS) – is a complete “dead end” according to Boštjan Jazbec.

In the lively ensuing discussion, the panelists agreed that the main – though not the only – obstacle to green investment is the lack of policy credibility and the regulatory risk. This starts with the taxonomy, which not only keeps changing but is also being watered down by political compromises. The issue of the incomplete banking union also resonated a lot in the discussion. While Gunter Deuber argued that his bank has contributed a lot to banking market integration, Boštjan Jazbec countered that this is just reaching out to non-banking union jurisdictions when what we need is a common banking system in the EU. Jazbec sees one reason for the fragmented banking market in the lack of trust as there is a strong instinct to resolve ailing banks on the national level. National resolution authorities have a lot of power in contrast to supervisory authorities.