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PRESS RELEASE

FINANCIAL STABILITY REVIEW SUGGESTS ALLEVIATION OF FINANCIAL MARKET TENSIONS, CHALLENGES REMAIN

- Stress indicators and euro area fundamentals suggest alleviation of financial market tensions, especially on the banks' funding side
- However, financial stability conditions remain fragile and euro area adjustment process is incomplete

Euro area financial stress has remained moderate over the last half year despite bouts of considerable global financial market turbulence, according to the new Financial Stability Review of the European Central Bank (ECB), released today. Indicators measuring systemic stress have fallen back to close to their pre-crisis levels. Euro area fundamentals have continued to improve, albeit at an uneven pace. Several countries need to continue to strengthen government balance sheets as well as carry forward structural reforms. At the European level, further steps are needed to create a genuine banking union. While an on-going strengthening of capital and liquidity buffers enhances banking sector resilience, further efforts are needed to correct losses in countries' competitiveness and improve profitability in the banking sector.

More generally, the comprehensive assessment launched this month by the ECB should contribute to (i) enhance the quality of information available on the condition of euro area banks, (ii) identify and implement necessary corrective actions, if and where needed; and (iii) assure all stakeholders that these banks are fundamentally sound and trustworthy.

Building on a thorough overview of macro-financial developments, this Review identifies four key risks to euro area financial stability:

1. **Economic and financial shocks that affect asset valuations and bank profitability, eroding confidence in the euro area financial sector.** Continued action is needed to mitigate lingering scepticism regarding euro area bank balance sheets. The ECB's comprehensive assessment will be a significant step forward in that respect.
2. **Renewed tensions in sovereign debt markets as a result of delayed national reforms, unforeseen bank recapitalisation needs or a rise in global bond yields.** Amid a fragile return of market confidence, policy progress needs to continue – complacency or reform fatigue must be avoided.

3. **Global financial market turbulence, with asset mispricing and low market liquidity.** Banks, insurers and pension funds need sufficient buffers for an eventual normalisation of compressed risk premia. Stable and predictable macroeconomic policies, including notably forward guidance, should help facilitate a smooth exit from central banks' non-standard policies.
4. **Bank funding challenges in stressed countries that force banks to deleverage excessively.** While there has been some improvement in bank funding conditions, remaining fragmentation requires further steps towards a genuine euro area banking union.

The report is available on the ECB website, www.ecb.europa.eu.

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