The loss of Anglo-Saxon capital markets are behind new proposal for completing EU banking Union

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Germany's Finance Minister Scholz proposal to break the deadlock in discussions over the European banking integration looks, at first glance, quite striking, although not surprising. Discussions over a European common deposit insurance scheme have always been opposed by Germany and fiscally conservative countries, who have sofar refused to accept a potentially vast liability from other EU's member states' financial woes, especially in Southern Europe.

Germany is however now signalling that progress on further integration of the EU's banks is needed to avoid being" pushed around on the international stage". Admittedly, Germany's change of policy can be explained by a series of recent events – primarily, the final realisation of the loss of London as the EU's largest financial centre after Brexit. It also signals the unwillingness to continue to depend on the US or China for financial services. The recent election of a new German run European Commission has also created the momentum for the completion of a banking union which it has announced as one of its top priorities.

Undoubtedly, the EU's growing reliance over the years on the US and UK banking institutions to underwrite the amount of its market capital activities, and the prospect of barriers to European lenders in accessing London based capital, explains this urgency. The financing of the European economy continues to depend heavily on the US and UK banking sectors, after efforts to develop a capital markets union delivered only limited results. A closer banking market is intended to pave the way for cross-mergers and help the EU's beleaguered lenders become more profitable internationally. EU banks, not least Deutsche Bank and Commerzbank AC, have been suffering from negative interest rates and a slowing economy.

In particular, in equity underwriting, Deutsche Bank's market share has more than halved in three years, while Anglo-Saxon banks are becoming more dominant, controlling more than 40% of underwriting business. Similarly, Anglo-Saxon banks are top lead underwriters for international bonds, with a market share of almost 8% for the past three years, double that of Deutsche Bank. BNP, another big player in the EU's 27, also remains well behind Wall Street and the City of London in this category.

Hence, the long-awaited break-through, which would entail the creation of a "European Reassurance System for bank deposit". The guiding rationale would be to "enhance financial stability by increasing depositors' confidence in the safeness of their deposits", and is intended to prevent a run on credit institutions in the event of a crisis in a fragmented EU market. Mr Scholz claimed his proposal "would significantly enhance the resilience of national deposit insurance".

The German offer to the EU comes however with notable caveas and familiar conditions. Despite Mr Scholz commenting that this "was no small step for a German Finance Minister", the proposal is not very generous.

Tellingly, national deposit guarantees would still remain the first source of defense, despite member states' being able to borrow from a European deposit insurance fund to cover extra losses. The final backstop would still continue to remain national, leaving additional financing to the relevant member state. In reality, the European Stability Mechanism is already in place to help a EU member state in need of funding. Moreover, outright transfers would only be considered over an unspecified period of time.

Mr Scholz also expressed Germany's demand to introduce risk-weights for sovereign bonds by changing its regulatory treatment – something Eurozone member states with lower sovereign credit ratings than Germany find unpalatable and have sofar refused to accept. The idea is highly contentious especially in countries with high stock of public debt where domestic government bonds make up a relatively large share of a bank's total assets. Italy has already signalled it will not accept restrictions on banks' sovereign debt purchases, as it would constrain reliable buyers from purchasing new bonds. Germany on the other hand, will only agree to a Reassurance Scheme under certain conditions, including a tough requirement from banks to hold reserves against government bond purchases.

According to the German proposal, Eurozone members would also need to make progress on a common consolidated corporate tax base (CCTB), - a minimum effective tax rate, which is opposed by low tax countries, notably Ireland.

As part of the package, Mr Scholz also included a highly controversial initiative of making progress on the requirement for harmonizing national insolvency laws, seen as a tool to end the fragmentation that allowed some banks to escape the European Resolution System, which imposes losses on bondholders and shareholders.

Furthermore, it is unclear how much risk reduction in non-performing loans would satisfy Germany and its banks and what shape a "single European set of laws on bank insolvency" would take.

The eye-catching omission however, is the lack of a single deposit guarantee scheme across the Eurozone. Savers with deposits of up to 100,000 Euros will still be rescued by individual states ' bills in case of a bank failure. This would create an unacceptable disparity between European citizens in a so called monetary union, and there is no reason why the Eurozone cannot make progress on a joint deposit scheme before these problems would be sorted. Such a proposal, as it stands, would be unambitious and not what the Eurozone is in need for. It would be a recipe for fragmentation and would not eliminate the asymmetry between savers in different member states. The banking union would not work effectively without closer collaboration and a real sharing of risks.

Admittedly, Mr Scholz's initiative goes beyond the completion of a banking union. It also aims to boost the EU's political weight on the international scene in a post Brexit era, and keep the shaky German government in power for another couple of years. His unexpected move is also geared to help him win the leadership of the Social Democratic Party (SPD), which forms part of the present coalition. Germany has key political interests in ensuring the Euro's survival and has very effectively used the development of the European Union to legitimise its own position and return to power. Needless to say, should Mr Scholz's initiative succeed in providing the political impetus needed to address the lack of integration in the European financial sector in December, the Eurozone banking union will deepen the divide between euro and non - euro countries in the EU and beyond. With London now leaving the bloc, squaring the difference with the City of London and Wall Street may well become the EU's most difficult competing task.