

The Eurofi Financial Forum

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Ensuring the coherence of EU financial regulations

Exchange of views

[Full transcript](#)

DAVID WRIGHT:

Ladies and gentlemen, I have the great privilege of moderating this discussion between two very distinguished people both of whom I have worked with over the years.

On my immediate left is Jean Lemierre the President of BNP Paribas and to his left is Andrea Enria, the Chair of the European Banking Authority (EBA). If I recount a little anecdote, I remember very well Jean, in September 2000 when you were the “Directeur du Trésor”, a particularly pertinent discussion in your office with Anne Le Laurier. It was made very plain that France wanted to progress on the implementation and harmonisation of the European rulebook and you were quite right. Without that passion from you and others at the time I am not sure we would have the institutional structure that we have today in Europe, so we owe you a great debt. Andrea, everyone who knows you knows about your tremendous technical knowledge and your great skill of drawing up the single rulebook in Europe, which is not yet finished but has made great progress.

We have decided to talk about two particular issues. One is the impact of the large number of changes there have been on banks, particularly regulatory changes, so many that they cannot be summarised quickly. Bank capital is ramped up eight to ten times; there have been huge changes in Eurozone supervision, and so forth. I read from Andrea's contribution to the Eurofi magazine that 109 technical rules have been adopted by the European Banking Authority. We have TLAC. This is a big change being discussed very actively right now by the Financial Stability Board.

My first question to you, Jean, is how do you see all these impacts? Is this manageable? Is it too much? Has the bar gone too far? Do we have a level playing field – not just in Europe, I see that you also raised the same questions in your contribution about the rest of the world. So, how do you see the regulatory pressure you have been under and how is it going to

affect the financing of the European economy?

JEAN LEMIERRE:

You are correct: regulators have done a lot, and banks have delivered a lot. What we see today is not what we knew five or ten years ago. Progress has been achieved.

I fear now we may lose the broad picture.

We must make them the 2 first goals compatible.

The third goal is to integrate the banking industry in the Eurozone. This is the level playing field in the Eurozone: better competition and better efficiency. Six months ago, Jacques de Larosière raised the question: is integration the source of efficiency? I would probably reply 'yes', because it would reduce a great deal of tension, costs and difficulties.

Fourth, we need to be able to continue to offer our clients in the corporate sector a quality of service which helps them to make a choice among many suppliers of banking services: Northern American, Chinese and European. They must be able to choose.

We have extensive debates about TLAC and now about the Bank Structural Reform (BSR) in particular following the compromise negotiated by the Latvian EU Presidency. Indeed the agreement of the EU Council includes surprising measures such as the famous "de minimis" threshold (€35 billion of retail deposits or 3% of retail deposits in relation with assets), exempting wholesale banks from any restrictions. Why do we have such a threshold? Do EU decision makers know its impacts notably in terms of level playing field?

There is another debate which is growing about the appropriate level of core Tier 1. The Americans have published their figures and methodology and the British have done the same although using another methodology. We need to go through this; this is crucial and we must keep in mind the goals I have mentioned.

In such a context, it is essential to ensure that in the Eurofi discussions, in each of the panels, speakers make sure that at the end of their presentation they are satisfied with all of these criteria and calibrations. We should never forget that we need to do the job: we need to finance the economies, we have clients and these clients have questions. Some parts of the world are doing better, some parts of the world are doing worse and there are doubts. Economic agents need us; this is our job and it is our job to deliver. We can work well together if we agree on the technical details of these prudential requirements and reforms.

DAVID WRIGHT:

I am going to pressure you to say a little more about what really concerns you later, Jean. I think we already have a flavour of that, so now let's hear from Andrea. Andrea, I see that you now also emphasise the implementation of internal models of banks, and of course we have the risk weights of the Basel agreement which are very variable. What do you see as the key issues now confronting the EBA and your work?

ANDREA ENRIA:

In my opinion, in the debate between regulators and industry it is important to make a strong conceptual distinction from the G20 package agreed in 2009 and the current work on internal models. The 2009 package tightened the overall stance of prudential regulation, with a gradual phasing in through time in order to avoid an excessively harsh impact at the moment of the crisis. These reforms are now being finalised. The EBA will present a report on the calibration of the Net Stable Funds Final Ratio (NSFR) at the end of this year and a similar report on the calibration of the leverage ratio will be by mid-2016. The Total Loss Absorbency Capacity (TLAC) requirements have been rather a late addition to the G20 reforms, and a relevant one. We need to close this fast in order to give clarity to the industry and allow bank management to plan ahead, although I must say that our standards on minimum requirement of own funds and eligible assets (MREL), which were mandated under the Bank Recovery and Resolution Directive (BRRD), were already pointing in that direction.

There is also the issue of consistency of Risk-Weighted Assets (RWA). This is not a package aimed at further tightening the requirements, but an issue that we must address. Market analysts and investors perceive that banks with similar portfolios have produced very different calculations of risk weighted assets and they do not understand this. The EBA has undertaken a lot of analytical work to better understand the drivers of such variability of outcomes and identified a number of issues that need to be fixed. The regulatory framework leaves too much flexibility to supervisors and banks and we need to narrow this down. In several areas, it is supervisors themselves that are generating inconsistencies via different definitions and approaches. More guidance is needed also in areas where differences are stemming from banks' modelling choices. For instance, important elements to be harmonised are the definition of default or the treatment of defaulted assets. This work will require more time but it is no longer in our view a tightening of the framework, it is more about achieving consistency. This will rank very high in our priorities going forward.

DAVID WRIGHT:

Are you optimistic about this? Is it something that you believe over time you will get convergence on or are we going to see a lot of political resistance to change and convergence?

ANDREA ENRIA:

I am comforted. We received positive feedback from the industry to a discussion paper issued in February which identifies possible solutions and suggests a sequence of regulatory fixes, aimed at enhancing consistency. The industry is concerned about the timeline because they say this is a very long term project. There will be indeed a need for a lot of work. Banks will need to revise their models, so this cannot be concluded in the next year; in their responses to our consultation banks have argued that three to five years will be needed, with some arguing – maybe exaggerating a bit – that we should give them up to seven years. The industry is also concerned about the level playing field. Many banks are complaining because they do not understand the differences between the outcomes of their internal models and their competitors' outcomes; this is a request that is also coming from the industry.

DAVID WRIGHT:

Jean, is that one of your major concerns? This type of unevenness and randomness in terms of the application of the rules? Can you say a bit more about how you see the level playing field? Is it very uneven in Europe, is it even worse when you think about global markets?

JEAN LEMIERRE:

I do agree with what has been said. We know very well that there is a degree of fragmentation in the implementation; not in the rules, but in the way they are understood and implemented. It is a priority for the Eurozone to put an end to this situation. It will create a better level playing field. It will be done with clarity, probably allowing some time. I am confident that the SSM is doing the job.

Regulators should pay attention on the global level playing field

Now, you have raised another question about the level playing field, the global level playing field. We share the view that rules can be different and regulations can be different across the Atlantic. However, we compete in a global competition and we expect the regulators to pay attention to this and to coordinate what they do. We hope that nobody will create difficulties in this, but for different reasons, and some are highly politicised, we see differences.

My simple message is this one: what do we want? Do we want European banks once more able to serve their clients in fair competition or not? One very well-known question is the debate about the structure of banks and the organisation of market-making activities, and this is a crucial subject. Some countries, large constituencies, impose rules on their foreign banks. I do not see why we do not impose in Europe the same rules on non EU banks. I think everybody understands what I have in mind, and this is extremely important in the global competition. A fair level playing field is a question of making sure that ultimately there will be a fair offer of service for the European industry. I hope that the corporate sector in Europe understands very well that it is about competition.

DAVID WRIGHT:

Let me ask you one another question before I turn to Andrea. We hear all the time about Fintech and traditional banking and every other sector being blown apart by new technologies, do you see this as a major threat to the business model of your bank or are the things that you have just been talking about a bigger threat to your business?

JEAN LEMIERRE:

It is a challenge, it is not a threat. We need to adapt. I am very confident that banks in Europe will do as well as banks elsewhere.

I have two concerns outside the banking industry. The first one is about the CMU. We need it but it is much too slow. There is no strong movement, or push. Little progress has been made during the last six months. The EU Commission and member states must show leadership. There should be a clear and strong political initiative in the coming weeks of the same magnitude as for the Euro project.

The second point is about liquidity. I am worried when I hear that there is such a debate. The first victim of liquidity may well be the banks themselves. What is being done on this issue? Where are the regulatory fora in which this debate is being addressed, both with asset managers and all the important market players?

DAVID WRIGHT:

I very much share your view and I said that the CMU deserves a big political push and, of course, we are waiting for the Commission. Proposals are due very shortly and I hope there will be an ambitious technology element.

Andrea, I want to ask you: we hear a lot about incoherence between different parts of the rulebook, whether it is banking, insurance, or securities; what do you see as the big incoherencies? Does it affect what Jean was saying about securitisation? We are not going to revive securitisation with the capital rules that we have today, for example. Is it on long-term financing? What do you think from your perspective are the biggest impediments? One final question is about your views on Mr Maroni who limits the delegation of powers to the European authorities such as your own.

ANDREA ENRIA:

Securitisation is a good bridge. Are we slow? In my opinion we can be proud of what we have done in this field. An issue was raised that the market for securitisation had basically collapsed and that the calibration that was done after the crisis, which was generated to a large extent from the malfunctioning of the securitisation market, it had gone too far.

We issued a discussion paper in October last year and opened a debate with the market participants. We made an in-depth analysis of what the problems are and advised the Commission in June this year. The Commission is going to propose legislative action at the end of this month together with a roadmap for the CMU. In European terms this is not a very slow process and also in terms of approach it signals an open attitude on the regulatory side. If we are convinced that what we have done is having unintended consequences then we stand ready to revise it. We are proposing a revision of the capital requirements, which is a positive development.

Securitisation is an area in which we have worked quite closely with ESMA and EIOPA at the Joint Committee. We have also undertaken joint work on inconsistencies and gaps between level I and level II legislation in the three sectors on the diligence, reporting, and disclosure related to structured finance products. The work of Simple, Standard and Transparent (SST) securitisation was developed very closely with EIOPA, which has had a similar initiative, so we have worked quite well together there.

I also understand that there is another problem related to the issue of market liquidity. The industry argues that this is one of the unintended consequences of regulation. But the Liikanen report stated that there had been an explosion in the trading book of banks from 2000 to 2008, with a spike in 2007-08. As a consequence of regulatory action we now see reduced level of trading book exposures, approximately back at the 2006 levels. Overall, I do not consider this to be an excessive contraction of these activities. But still the point is market-making.

What I was expecting from the regulations was better pricing of liquidity risk, so maybe banks repricing their market-making services. Instead, what we have seen has been an impact on availability of the service, on quantities and not on prices. So there is something that is not working there. We need to understand why this is happening and we need to understand if there are regulatory drivers leading to these results. What are they and how

can we deal with them? So far, from the analysis presented by the industry are excessively high level. They simply argue that regulatory reforms are generating this contraction. I need to identify the specific elements that might be driving this behaviour and to define what type of action we could take there.

With regard to the Meroni doctrine, we surely do not seek more power, actually we have too much work and too few resources so the problem is the opposite. The key point is that there are areas in which the process is relatively slow and possibly the delegation does not work well. The classical example I always make is reporting. In which jurisdiction in the world do you see the reporting templates in the Official Journal? It was the longest issue of the Official Journal ever. The process of change or revision is too cumbersome. We have enough experience now with the new setting and we have worked reasonably well in terms of accountability to the Parliament and to the Council. We report on everything we do, so Council and Parliament have all the powers to call back what we do if they don't like it. Being given a little more leeway in some technical areas could also help to address the problem of being faster to respond to market developments.

DAVID WRIGHT:

When I was in the Commission, of course, I was very aware of that but I think from the outside you are absolutely right.

Let me just conclude with two remarks. Jean rightly said to keep in mind the vision and from the other side of the fence, I don't think that happens enough, particularly at the global level. Because of the crisis we have just had layering, one thing on top of the other, and not really sufficient thinking through of the impact of one policy on another.

This leads to the second point: the data on which to make these judgements is poor, and our understanding is pretty poor. If we put margin requirements on OTC derivatives, do we know the impacts on other parts of the market? No, we don't. Do we make the intellectual effort to really think hard about those impacts? I am of the view that not enough work is done in that respect.