Key priorities for the incoming Commission

Roberto Gualtieri

Chair, Committee on Economic and Monetary Affairs, European Parliament

A new political way towards the Economic and Monetary Union

During the last European legislature, important progress has been achieved in the area of financial services. The SSM and the SRB have become operational, the risk reduction measures have been agreed on the basis of a balanced compromise, paving the way for the agreement on the backstop to the resolution fund, nearly all the major legislative initiatives under the umbrella of the CMU have been finalized, the Juncker Plan has introduced a new tool to successfully mobilize private and public investments and to address market failures.

We have now a better capitalized and more resilient banking system, an efficient common supervision and resolution. A number of encouraging indicators are showing the increase of equity investment and non-bank financing and the good state of the new STS securitization framework. Moreover, many of the legislative innovations in the area of CMU have not yet had the time to show their benefits and will boost the capacity of our financial system to support growth and enhance stability.

However, we have to recognize that in a number of crucial areas the necessary results to achieve a true Financial Union have not been reached. We do not have yet the third pillar of the Banking Union in order to provide the same level of protection to deposits across the monetary union, and we have not been able to remove the regulatory limitations that prevent cross-border institutions from managing own funds and liquidity requirements more efficiently within the Banking Union. These two problems are strictly interconnected, and the solution of the latter is strictly connected to the capacity to give a proper answer to the former. In the CMU area, the ESAs review has been an important success but Member States have prevented the necessary progress towards a common supervision of capital markets, while in the decisive field of the harmonization of insolvency frameworks we have not moved yet at all. As a result, financial fragmentation remains significant in the EU and in the Banking Union and the development of capital markets is still insufficient.

In the current challenging economic and political global environment, deepening integration, boosting growth and strengthening financial stability are all necessary and interconnected goals, which require to completing the Banking Union and to significantly advancing in the Capital Markets Union. However, it is evident that in order to overcome the obstacles that have so far prevented the necessary progress we need to define a new political approach.

In this respect, the political guidelines for the next European Commission presented by the new President Von der Leyen are positive and innovative. The guidelines, which have been elaborated in close dialogue with political groups in the European Parliament, >>>

>>> identify the completion of the Banking Union and the Capital Markets Union, in strict connection to the deepening of the Economic and Monetary Union, as some of the key tools of a comprehensive political strategy aimed at launching a European Green Deal, based on a Sustainable Europe Investment Plan, and at strengthening the European social market economy in order to boost at the same time growth and social cohesion.

By linking more clearly financial integration to specific policy goals, instead than making of it a goal in itself, it could be a key to strengthen the political support and ownership to an ambitious agenda and to overcome some of the deadlocks that have so far prevented the necessary progress on the basis of more transparent and robust trade-offs between member states, citizens and political groups. At the same time, such an approach will require a more targeted and tailor-made identification and selection of priorities and of tangible results, in the spirit of what Francois Villeroy de Galhau have often defined a "Financing Union for Investments and Innovation", and in the framework of the concept of environmental and social sustainability.

What have been often defined "lack of ambition" in the completion of the internal market for financial services is in reality the result of the too narrow political basis of such an agenda. Let's hope that the pursuit of a "new political way" towards the Banking Union, the Capital Markets Union and the Economic and Monetary Union, will prove to be more effective. ●

Jean Lemierre

Chairman, BNP Paribas

The future of the European financial system: a new agenda

After ten years of unprecedented regulatory overhaul to strengthen financial stability, the European financial system faces now a different type of vulnerability, as bank profitability is under pressure, under the combined impact of higher capital requirements and accommodative monetary policy rates.

As the European Union enters in a new legislative cycle, the financial services agenda needs to be revisited to address those issues, and to define new priorities.

One of the major stated goals of the Banking Union is to enable cross-border mergers, to address over-banking and develop "private sector risk sharing". Given higher compliance cost of doing business, coupled with fast-changing clients 'expectations, concentration is unavoidable, but it is very slow, whether domestically or cross-border. Rigid resolution framework, and absence of true Banking Union certainly doesn't help, but even more fundamentally, mergers can only happen if the franchise value is sustainable, and if risks are correctly priced, which is currently not the case given the current pricing of liquidity. The Eurozone needs to find other avenues to incentivize cross-border flows.

While banks are struggling on the profitability front, they also face the challenge of digitalization, which requires massive IT investments to compete with new entrants and third country competitors. Today, European banks have to fully deduct from capital any investment in software, whereas third country banks (US, CH) are treating them as tangible assets and applying a 100% RW. This means that for any 1bn€ of capital allocated to software developments, a US or Swiss bank can spend 12.5bn€ in IT developments, while EU banks can only spend 1bn€! Such a major competitive disadvantage needs to be fixed urgently, to unlock EU banks' investment capacity to offer cutting edge customer experience, and compete with incoming big tech. European authorities should also rethink the "open banking" concept to ensure that the value chain of financial services is fair and that zero-cost banking >>>

>>> doesn't favor clandestine passenger strategies, by new entrants that would enjoy access to data and infrastructure financed by incumbents without to contribute to support market infrastructures.

Third, Europe should implement Basel IV with care and mitigate the tightening impact of ongoing regulatory pressure by setting up a truly workable securitization framework, allowing banks to shift assets into Capital Markets and providing investors with access to previously illiquid exposures such as mortgages or loans to corporates and infrastructure projects.

Securitization should be one of the key pillars of the CMU. It can also become a major driver for private sector risk sharing across the Banking Union, and, if combined with appropriate high-quality criteria, serve as quasi-safe asset.

Securitization is the main gap compared to the US financial system. Every banking regulation has a disproportionate impact on the European economy compared to the US one.

Fourth, as the European societies are embracing the fight against climate change, it should be recognized that banks are uniquely positioned to finance energy transition and ESG goals at large, from mortgages to infrastructure and savings products. Policy makers should focus on incentivizing this move, rather than on implementing additional regulatory constraints. Sustainable Finance should be seen as an opportunity, rather than a financial risk.

Finally, as the EU action plan 2019-2024 aims at designing an industrial policy fit for the future, it is time to stress upon that the financial sector is an element of European competitiveness, and that there cannot be a resilient European economy without a competitive and resilient European banking sector.

Bruce R. Thompson

Vice Chairman and President, EU and Switzerland,
Bank of America

Future EU financial services priorities

The new European Commission faces both challenges and opportunities, as does the financial services sector itself. Uniting all parties should be the need to maintain financial and economic stability, which will provide the best foundation for continued growth in the EU.

Among the challenges are European businesses' greater reliance on bank borrowings, rather than capital markets activity. With constraints on the banking sector since the financial crisis, increasing the availability of different sources of finance will help both businesses and consumers in the EU. Continuing work on the Capital Markets Union (CMU) is therefore critical.

However, further development of the CMU must be undertaken with an outward-looking approach. While deeper integration of capital markets should result in a stronger European economy, it is important that the CMU develops within the context of global markets, and ring-fenced capital markets are avoided. And, in the context of Brexit, policymakers should avoid erecting barriers to cross-border market activity that do not have a sound prudential basis.

Further developing the CMU will also help boost market liquidity across a range of asset classes – this will be important if the EU is to continue to attract financial services activity following Brexit. Again, an important factor in enhancing liquidity will be taking steps to avoid market fragmentation. >>>

>>> Regulatory fragmentation is also a concern for international firms. Both in the context of Brexit and beyond, therefore, we would encourage policymakers and regulators – in the EU, the UK, the US and other jurisdictions – to work together. The role of international standard-setters such as the FSB and IOSCO is critical in this regard. Regulatory harmonisation, and co-operation between supervisors, benefits financial services firms through reducing costs, savings which can then be passed on to our clients – this is the case both within the EU and at international level.

Likewise, finalising the implementation of Basel III in the EU will be a positive step in further strengthening the Banking Union, and should be done in a way that limits divergence from global standards, in order to maintain a global level playing field.

Turning to environmental sustainability, implementing the Sustainable Finance Action Plan will help the EU to meet the challenges of climate change in a way that continues to support economic growth and encourages a longer-term approach in investing and development.

There is also a pressing need for a co-ordinated global response to climate change and, should the EU take a standard-setting role, as with wider financial services regulation there is a need to avoid regulatory fragmentation. International and well-integrated capital markets will have a key role to play in supporting the transition to a more sustainable economy.

Technology already plays a vital role in our business and personal lives, and the speed of change is only likely to increase over coming years. Implementation of the FinTech Action Plan will help ensure the EU is well-placed to address the challenges and opportunities that technology brings, balancing the potential rewards of new technology with appropriate oversight of the risks. Importantly, implementation of the FinTech Action Plan should be done in a way that promotes innovation while ensuring that same services are subject to same rules.

The coming years promise to be challenging but exciting ones for financial services in the EU and internationally, as we seek to embrace new opportunities while not forgetting the lessons of the financial crisis. The EU has a critical role to play in managing the development of its financial markets in a way that provides security and opportunity for its citizens while remaining open to global developments. With our post-Brexit EU entities now fully established in Dublin and Paris, we look forward to participating in this important debate.

Vittorio Grilli

Chairman of the Corporate and Investment Bank EMEA, J.P. Morgan

Prioritising a single market in services for the new political cycle

Forty years ago, Europe understood that in order to compete internationally, a Common Market was needed to allow for economies of scale in goods. Today, services play an increasingly vital role in the global economy yet Europe has not responded with the same vigour.

Our priority should be advancing a single market in services to remain competitive, deepening integration, boosting growth and strengthening financial stability. We must continue developing our capital markets and maintain openness, ensure our banks are stable, liquid and resolvable and consider increasingly important issues such as fintech, sustainable finance and AML. >>>

>>> Strengthening the Capital Markets Union and completing a Banking Union should be a key priority. These initiatives are essential to establishing deep and liquid capital markets, supporting an increased international role of the euro and its reserve currency potential by improving the Eurozone's long-term resiliency. Policymakers should be careful though that this does not create barriers with global capital markets.

Europe needs growth and a dynamic economy for its citizens given a scarcity of pension savings and an ageing population. Delivering efficient outcomes will be difficult if harsh restrictions are placed on the financial sector's business models. For example, in asset management, delegating portfolio management to third countries allows investors to access global centres of excellence but certain legislative proposals could lead to restrictions on well-established market practices and European funds' openness.

The EU should consider the impact of politicising equivalence decisions on market participants' location decisions and their ability to operate efficiently across borders. Equivalence decisions should be based on respective rules' merits, the outcomes achieved and made in a transparent and predictable manner.

Post-crisis reforms have fundamentally improved the financial system's strength, stability and resiliency. The Commission should faithfully implement Basel and FSB agreements to ensure the proper capitalisation of Europe's banks. Some EU banks may find regulatory capital increases challenging, but systemic stability demands that banks are properly capitalised. Banks should not retrench from, rather support, the economy in another downturn. Without better institutional cooperation and a mandate for authorities to act, EU institutions could face difficulties in making decisions on achieving financial stability and economic growth through an efficient financial sector.

"Our priority should be advancing a single market in services to remain competitive."

\- VITTORIO GRILLI

National regulators' focus on their own markets' financial stability makes sense from a country's perspective but can lead to inefficiencies and trap financial resources. "Home" and "host" Member States highlight the lack of integration between regulators; a system founded on flows of information, not just trust, between authorities is needed with robust processes to guide cooperation.

Supervisory convergence towards innovation should be enhanced and the EU's financial sector should better embrace new technological opportunities, for example through adopting the Commission's fintech action plan. Any new regulatory framework should be flexible, graduated and principles-based; oversight should be tied to scale and risk.

Europe is a global leader in sustainable finance. Customers need more clarity and transparency; financial firms need better and consistent disclosure at the corporate level to provide useful information for investment decisions. We would caution that EU authorities should approach climate and environmental factors for financial institutions from a risk-based perspective and appreciate that firms have varying exposure to these factors.

On AML, we support enhanced supervisory cooperation through the creation of a single supervisor and converting the Directive into a Regulation. This may be politically complicated, but greater efforts can lead to increased confidence in our financial services.

The next Commission should prioritise integrating Europe's financial sector, but further integration means breaking down barriers in the cross-border trade of services and integrating human capital through labour laws, education and pension systems and professional qualifications. The priorities should be those related to CMU, Banking Union and trends posing new risks and opportunities for the sector. ●

Harald Waiglein

Director General for Economic Policy and Financial Markets,
Federal Ministry of Finance, Austria & Member of the Board of Directors,
European Stability Mechanism (ESM)

The EU setting its priorities in financial services

The past five years have been successful for the financial services sector, as the EU has taken the opportunity afforded by the benign market climate to advance an ambitious reform agenda to strengthen the financial services sector and the EU at large, in order to make them more resilient and ready for future challenges and to support integration. Clearly, Europe's financial sector has become more stable over the past years. Nevertheless, Europe faces increasing financial, geopolitical and environmental challenges that need to be addressed at the highest political level.

As the EU is now setting its priorities for the next five years, it is necessary to focus on finalizing already tabled core European projects, as well as introducing new approaches with a clear view to the future. The different aspects that affect the EU financial services sector, such as political stress factors, fast-changing technology, low interest rates combined with low profitability and challenges to traditional business models, need to be taken into account when thinking about priorities.

> *"Participation of households, start-ups, SMEs and high growth companies in capital markets is vital."*
>
> - HARALD WAIGLEIN

The Banking Union is still incomplete and thus the new Commission will play a fundamental role in strengthening and completing the Banking Union without delay. Strong decisions must be taken to reduce the fragmentation in the Eurozone and to create an integrated and stable market for banking. Further, the priorities must focus on stimulating the Capital Markets Union and hence market-based finance across the EU single market. The participation of households, start-ups, SMEs and high growth companies in the EU capital markets, the attraction of international investors and the removal of national barriers to the free movement of capital are vital elements in this regard. The principle of proportionality should be kept in mind, as the European financial market is characterised by a variety of business models and market actors.

The need for transitioning to a more sustainable economy cannot be ignored by the financial sector and must be followed up by the EU. The Paris Agreement on Climate Change as well as the Sustainable Development Goals are setting the way forward with ambitious targets that require significant financial contributions. The Sustainable Finance Action Plan needs to be completed and discussions should be held on investment predictability, estimation of climate risks, disclosure of information and the need for specific initiatives to be taken by the financial markets as well as by regulators.

Another topic that needs the attention of the new Commission is the accelerating pace of technological advancement and its applications in across the financial services sector that create opportunities to serve customers in new ways. Customers increasingly expect flexible and personalized services specifically tailored to their needs at >>>

>>> times and in places of their choice. Existing market participants need to adapt their business models to the changing environment, and new innovative businesses will be entering the market. Supervisory practices and legislation needs to address the changing environment in order to create a fair and stable market without hampering innovation and technological progress. Apart from the opportunities offered by digitalisation, market actors and regulators need to take into account cyber risks and prepare accordingly. The past few years have also shown the risks from money laundering and terrorist financing for the financial services sector. The work of the new Commission, building on previous initiatives to address this challenge, will be of great relevance.

The priorities in the financial services sector need to have a long-term perspective and steer the path to a more integrated, resilient, competitive and innovative European financial market. The new Commission needs a concrete political vision and plan for defining the role that the European financial market should play in the global economy and facilitate investments in Europe in order to ensure competitiveness and growth.

Odile Renaud-Basso

Secretary, Directorate-General of the French Treasury, Ministry of Economy and Finance, France

Financing the future of the European Union

Between 2015 and 2019, the Banking Union and Capital Markets Union (CMU) have made some progress towards a more resilient and consistent framework for financial services in Europe, covering aspects such as prudential ratios, securitization, central clearing or transparency. In doing so, these initiatives have deepened the approach initiated in the aftermath of the 2008 financial crisis, which aimed primarily at restoring buffers, increasing reporting and tightening supervision. The CMU has been conceived mostly as one of the pillars of risk-lowering and private risk-sharing in the EU alongside the Banking Union.

> *"Despite the high level of household savings, European financial markets remain poorly integrated."*
>
> \- ODILE RENAUD-BASSO

Despite the high level of European households' savings, European financial markets remain underdeveloped and poorly integrated. They suffer from a lack of liquidity and the financing of the economy relies mostly on the national and "traditional" banking channels. Following its agenda for investment in Europe, the Juncker Commission acknowledged the relevance of the subject and proposed an action plan bringing together a range of technical initiatives.

The essential function of a financial market is to provide them with diversified and interesting investment opportunities that will fund the growth everywhere in the EU. This is a critical task for the CMU, one that ought to transcend the different pieces of legislation that have and will continue to underpin it. This is a strong political >>>

>>> message which we should focus on during the next five years, on a pragmatic and results-oriented manner.

European savers hold the key to the future of our financial markets. European markets should first and foremost serve European consumers, savers and investors. This implies streamlining current documentation and granting seamless and accurate access to two types of information that are critical in making informed investment decisions: performance (net from fees) and risk.

EU companies are less inclined to go listed than ever before. It is of course a widespread phenomenon among developed capital markets. But the fact remains that European entrepreneurs today are skeptical that their business can be valued in Europe as much as it could be abroad. Private equity has gathered a lot of momentum but should scale in size in the field of venture capital, as we still see too few European unicorns. In that regard, the review of Solvency 2 should facilitate investments in equity, as this would offer alternatives to bank financing while benefiting to clients.

Europe was undoubtedly right when pioneering the field of sustainable finance. The drawback of this dramatic uptake is the looming risk of further market fragmentation, across too many labels and definitions. The Commission should therefore strive to harmonize the concepts of "sustainable" and "green" finance, making it a European standard that can then be a reference for the rest of the world. The taxonomy of environmentally sustainable activities will be a crucial tool in this respect.

Data sciences and technologic disruption are also a core component of financial markets. Spearheading this revolution would position Europe at the forefront of innovation in customer services, payment systems, market infrastructure and collateral management models. Two technologies in particular should focus our attention: blockchain and its applications in the realm of virtual assets, and the advent of a more pervasive use of artificial intelligence and machine learning. An SME raising funds in 2030 may resort to classic issuance, crowdfunding, token emission all at once with instant knowledge of their investor base and infinite possibilities to tailor the parameters of the instruments they offer, most likely embedded with a strong component of automation and smart execution.

As a conclusion, one should recall that the single market in the field of financial services will obviously not be achieved without the support of existing European financial players. Thus, the effect of Basel 3 on EU banks, and more specifically on corporate and investment banking business, must be carefully assessed – there is indeed a serious gap between the impact recently measured by EBA and the political guidance from ECOFIN and G20 that the reform should not lead to a "significant increase" of capital requirements. Besides, initiatives such as STS, or a supplementary facilitation of securitisation may help European banks adapt and increase their performance in the future. ●