



## Exchange of views

**Ana Botín** - Executive Chair, Banco Santander

**David Wright** - President, Eurofi

### David Wright (Chair)

David Wright welcomed and introduced Ana Botín, giving thanks for Banco Santander's support. Ana Botín has immense experience and knowledge of the challenges facing European banks, and as Chair of Banco Santander serves about 150 million customers worldwide. David Wright asked about the crucial role the banks have played in bridging the disruption of the pandemic and why it has been so different from the previous crisis.

### Ana Botín

Ana Botín stated that this is a very different type of crisis. This is a health crisis which has created an economic shock; that is very different from 2008, which was a financial crisis. Back then banks were in large part the source of the instability but, this time, they have been a source of stability. If banks have been part of the solution this time, it is because they learned the lessons of that crisis. They now have strong balance sheets and are able to support people and business. For example, Santander lent €1 billion euros a day during 2020, and its peers did likewise.

The nature of the public health response created an urgent need for liquidity support for otherwise generally viable businesses, which is a very important point. This was a gap that banks could step into with state backing. Emergency lending has played a much bigger part in this crisis than in the 2008 crisis, in part because banks were deleveraging in 2009.

The third point, which is crucial, is that financial regulators and governments moved together, working with the banks, very quickly to support economies. From the point of view of the banks, the biggest difference compared to 2008 is the speed and scale of the response from authorities. Given that the last crisis was a financial crisis, in some cases authorities were reluctant to be seen to be rescuing banks and creating morale hazard, and they intervened only when there was no alternative. This time the response was almost immediate, with monetary and fiscal measures in Europe coming into place within days. The response

was ahead of the problems, and banks were there to help, because they had strong balance sheets and were agile.

### David Wright

David Wright asked whether Ana Botín is worried about corporate insolvencies and non-performing loans as there is now a transition to a more normal economy.

### Ana Botín

Ana Botín believed the lesson is that when governments, regulators and banks work together at speed they can actually make a huge difference, and a once-in-a-century shock has been withstood. These plans require trade-offs. Loan moratorium programmes, for example, require banks and governments to work together. Commercial banks were used as a route for state-backed lending, and so, looking to the future, it is critically important that any consequent bad debt be dealt with constructively and in partnership, that contracts should be respected and that if direct aid is desired that it is not at the expense of changing the conditions of the loans that were given. This is really important, because it is going to be an issue in many countries.

There is still a health crisis. The best economic policy, the best thing for citizens, companies, banks, the economy and society is to deal with what is still here: a very severe health crisis that has not finished. Vaccination is the best economic policy for 2021.

Looking ahead in terms of how best to handle a rise in insolvencies, there is substantial capital and substantial loan reserves. Losses have not yet materialised, but this is a risk to profitability and not to solvency. For example, Santander's pre-provision profit, even after increasing its loan reserves by 50% last year, could still increase again by that same amount without getting to zero profit. Others doubtless have similar, albeit slightly different, numbers. Losses will come in 2021 and 2022, but there are provisions. If more provisions are eventually needed, it has to be added at a lower cost of risk. It is a risk to profitability, but not to solvency.

Where solvency rules have been temporarily relaxed, it is crucial that companies still need help, and that depends on the depth and the quality, as well as the speed, of the recovery. The vital message is that growth matters. Clear action on NPLs is needed, probably with a gradual approach, and a gradual approach to returning to prudential standards. Regulators must be worked with to ensure that the regulatory framework is not focusing on stability at the expense of growth, and that there is a capital framework which is not procyclical.

### David Wright

David Wright queried whether there is concern about the implementation of Basel. Europeans are apparently concerned about the output floor and capital for non-rated SMEs, for example.

### Ana Botín

Ana Botín confirmed that there are concerns. The biggest challenge is making sure that a cliff-edge effect is avoided, not just on the fiscal side but also on the banking side, and so banks need to be able to lend more to business. Banks need to be able to deploy more of the capital they have built up, which means being able to attract investors. That is a starting point. Without a good, profitable model it is going to be very difficult. Basel matters and their implementation is a very immediate challenge. There is a risk that the Basel implementation will restrain banks much further at a time when they need to be able to support recovery. Rules need to be simplified and properly calibrated to take into account European specificities.

Strong economies are powered by strong banks. In Europe, SMEs depend on banks for 70% of their external financing. There was a €400 billion financing gap for eurozone SMEs in 2019. That is 3% of gross domestic product (GDP). There is a need to calibrate capital to remain prudent and strong, but also to be able to support the economy and use balance sheets responsibly. Then there is the whole issue of the digital transformation and how to compete.

### David Wright

David Wright noted that Ana Botín has been positioning Santander for the new digital and green world. Both trends are irreversible. David Wright asked whether Ana Botín is worried about the level playing field.

### Ana Botín

Ana Botín stated that due to COVID-19 everyone has to become digital. Car companies are now saying that they have to be software companies. The financial sector is essentially dealing in a digital currency anyway. 80% of all Santander UK sales in 2020 were digital. Competition and innovation are positive, but it has to be fair competition. This has to be addressed, especially regarding data and payments. If data is opened up to other companies, those other companies should do the same, but that is not happening. The Revised Payment Services Directive (PSD2) is focused on banks opening up data on customers, but it is not reciprocal. A much better service and a much better price on risk can be offered if banks get data from other companies that are willing to share. In the European Banking Federation (EBF) and other fora, the principle of same services, same risks, same rules and same supervision is defended. Data access is cru-

cial, but there are many other issues. For example, this relates to both the green and the digital issues.

Recently everything became software, and this is very good news. Previously, software was not treated as capital. Software is one of the biggest assets companies can have. American banks were able to treat it as capital. When European banks invested in software, it was deducted one-to-one immediately, so this is a major progress. More rules like this that are adapted to the reality of today are needed, and the reality is that most things are becoming digital. This is interesting for Europe, for the consumer, for the banks, and for growth; on green issues it is the same. Basel is looking at this. There should be awareness of the optimal level of capital. There are questions on how to calculate risk ratings on assets helping to green the economy and how to agree on a common set of data taxonomy standards. There is an alphabet soup of different standards and rules; common and hopefully global agreements must be reached.

### David Wright

David Wright asked whether Europe has carved out intellectual leadership, particularly on green issues and on some of the digital issues, but with too slow decision-making.

### Ana Botín

Ana Botín stated that Europe has a huge opportunity to become the standard setter for green, digital and data issues. The Digital Markets Act, and several other initiatives in the Commission, are very encouraging. Banks and companies should provide input for the Commission when they ask for consultation. Sometimes they are too shy. Specific cases should be chosen and evidence given to the Commission. There is a need to move faster, but it is also important to do it the right way, and it is not easy. Getting input, as the Commission is trying to from the private sector, is hugely important. To the broader question of Europe and the US, Europe is at a disadvantage. A common question asked is what the gap is between regulation, or why the financial market in Europe is so different from the US.

### David Wright

David Wright asked why the valuations of European banks' profitability are much lower than those of the US. Many excuses have been given, such as securitisation, no banking union and no capital markets union.

### Ana Botín

Ana Botín confirmed that the short answer is that it is the sum of all of those. There is not one answer. Santander was worth the same as JP Morgan 10 years ago, and today JP Morgan is eight times larger. Santander was the largest bank in the eurozone; it is still number one or two depending on the month or year. JP Morgan is 10 times more, and Santander has done well in terms of growth. One important factor is the macro context. The US rebounded very quickly after 2011, whereas Europe entered the euro crisis in 2011-12, with three years of very poor growth, ultra-loose monetary policy and negative growth. There is much debate about negative rates, but this is very important. The commodity is interest rates, so a small difference there has a huge impact on profitability.

It is not just a difference in interest rate. It is the construction of the financial system itself, the Fannie and the Freddie. Mortgages need to be kept in a balance sheet in Europe; in the US, they sell them off. Americans have enough space to support the economy much more. The regulatory regime is also much more constructive. There are fewer intrusive business limitations. In the US, there is a single market. There are economies of scale, which are hugely important on digital. In Europe, the capital markets union has been discussed for years. There is also the question of innovation. There is a long list that should be understood, because stronger banks are needed for a stronger economy.

### **David Wright**

David Wright agreed and noted that the projected growth rate for the United States is at 6.5% according to the governor of the Fed, while Europe is at 3.5% or maybe 3.7%. Some think that the US growth rate could even be in double digits. David Wright asked what the position will be in 10 years' time.

### **Ana Botín**

Ana Botín noted that the consequences of Covid-19 will only be seen after a couple of years but these will accelerate change, and in a direction that might not have happened without Covid-19. It is going to have a huge impact on the political side. Government intervention means that there is more debt. That is going to cause a great deal of rethinking of public policies, which is right. A new social contract is needed, and this is aligned with the green and digital issues. It also has huge implications for taxes, competition and many aspects of political, public and business life.

For Santander as a business, change is driven by consumers. Behaviour is going to be very different. There will be 5G. The Internet of Things (IoT) means people will be connected in a way unimaginable today. Again, speed is very important.

Europe is excellent on the economic and public sides. It has done a fantastic job on the monetary side through the European Central Bank (ECB), and also on the fiscal side. It could do better on health. It now has to shape its future correctly to allow businesses to be agile.

To create new jobs, we need to be agile. How SMEs are financed has to be reinvented, because they do not have a factory or a bar; they have talent and brains. There are questions of how to finance start-ups and incentivise banks. Different business models are needed. Santander calls it 'one Europe, one Santander'. The question is how to create a global platform, and how to do that at the European level for all industries. The future driven by the consumer is much more digital, with the likes of payments. Payments will not be measured; it is going to happen, so there will be a need to learn how to provide more value added for clients, and more help for succeeding on a personal basis or as a small company entrepreneur.

### **David Wright**

David Wright thanked Ana Botín.