Exchange of views

Jean Lemierre - Chairman, BNP Paribas

David Wright - President, Eurofi

David Wright (Chair), President, Eurofi

The Chair introduced Jean Lemierre and noted that Eurofi had heard a great deal about the positive role that banks have played in the Covid crisis. He asked about the role of the banks in the recovery and whether there are concerns about a spike in non-performing loans (NPLs) that could have systematic consequences.

Jean Lemierre, Chairman, BNP Paribas

Jean Lemierre stated that 2020 was a challenging year and many have done well in these extraordinary and difficult times. Governments have done well. Supervisors and regulators have done well in taking decisions. Central banks have done extremely well, fuelling support to the economy. The EU Commission has done the job. The official sector was there with quick and ample positive reactions.

The private sector – and mostly the corporate sector – has done well at a difficult time. There may have been some difficulty in adapting, but, as a rule, they have done well. This needs to be said because it shows that economies everywhere are reactive and tend to adapt, and entrepreneurship has been high at a time of difficulties. Banks have done their job. Banks are there to be open, to be with clients, and to use balance sheets to support the economy. That has been done.

Banks have acted, first, alone, and then with governments. In March and April 2020 when markets were closed, there was a burst of support, mainly liquidity facilities, to the economy that had a big social impact. It has avoided massive disruption. Then governments joined with state guarantees in many countries to support the economy. Looking at the level of risk today shows that most of the provisions that were made at the end of 2020 are forward-looking, which is fine. There is a need to be careful about the future while being aware that, in this unique environment, banks were able to control risk with governmental support.

It is not over. Vaccination helps a great deal. The speed is different country by country and the recovery will hopefully be led by vaccination. The beginning of a strong recovery is visible, and International Monetary Fund (IMF) forecasts show that perhaps in a few months some economies will be moving, especially in the US. This is welcome. However, some sectors have been hurt massively and in Europe that is transport, tourism, hospitality, bars and hotels. They have suffered and will continue to suffer greatly. To a large extent, the loss of gross domestic product (GDP) is concentrated in these sectors, so these companies will suffer.

There is still much work to be done by banks, mainly in offering liquidity facilities to recover, grow and invest; and secondly, in these difficult sectors, company by company, to find solutions for how to manage the debt. Some cases may show a wall of debt that must be managed in order to give companies an opportunity to recover. Some of them will have real difficulties and, unfortunately, there is the fear that some of them will go bankrupt, although hopefully not too many. Hopefully, by working together, the job will be done.

This is a response to having listened carefully to the governor of the Bank of Spain. Banks were part of the solution last year by doing the job. It is essential to continue to do it and to have the capacity to do it. To a large extent, it is based on knowledge of clients. Hopefully, banks know their clients, and they showed this in 2020. Room for manoeuvre in terms of capital requirements is essential.

With this in mind, there are two points: stress tests and, further ahead, implementation of the Basel III review. Without going into detail, the point can be understood. Banks can do the job if there is the capacity to do it. This requires careful attention and implementation. Time is not a problem. The time can be taken to do it if there is a simple, honest and well discussed assessment of various aspects, and then the job is done for the people. The system is safe. If it was not, it would have collapsed in 2020. Now is the time to move step by step, carefully and openly. This is based on banks' commitment to clients and to the economy, and willingness to deliver and, hopefully, a continued understanding by the official sector of what banks do and letting them do it step by step, and carefully.

David Wright

The Chair asked if there is a feeling of increasing optimism around banking and if that optimism encompasses a sense that banking union could be completed reasonably soon. The Portuguese Presidency has hinted that it could be in the European Council in June with a roadmap. He asked if those hints have been heard and about the importance of this.

Jean Lemierre

Jean Lemierre considered that a great question. Not being a politician means not creating large headlines, but speaking about real life day in, day out. Banking union would be profoundly welcomed. It is essential. Good decisions have been made, with the main one being the creation of the Single Supervisory Mechanism (SSM) for the eurozone. It is a huge step forward. It works, it delivers, and it creates value for all.

At the same time, there is hesitation and setbacks. Banking union is a single market for banking activities to better finance the European economy. At present, the capacity to move liquidity freely and optimally, or to move capital or equity freely, does not exist. The debates behind this are well known by now, so it is time to do it.

Europe has built up a big institution in the resolution fund. It is often said that there are too many banks in Europe and some banks could disappear. This comes from the official community. The result is the accumulation of billions of euros, and even more each day, because of the current situation, in a resolution fund that is only used in a few cases. This could be used to improve the system.

Circumstances require a new system, which is the European Deposit Insurance Scheme (EDIS). EDIS guarantees national funds to guarantee deposits. There is no difficulty in guaranteeing deposits, but it raises the question of how these funds are used in a preventive way to avoid putting in place a deposit guarantee. In some countries, this money has been used at a national level to continue to support existing banks that normally should have disappeared. It is difficult to understand the rationale behind piling up a new fund to continue to do this, because the national funds are exhausted or close to exhaustion.

If banking union is a single market, opening flows of liquidity and equity, creating a more consolidated and better banking system, and getting rid of banks that are seen as useless by governments and the official sector, that is fine. However, if it is continuing to build up funds for banks that do not go to resolution or merger, that is a problem, because competition and state aid are at the core of Europe. If banking union is maintaining inefficient banks, it is a waste of money. If banking union is creating an efficient single market, it is welcomed. There is a commitment to the second one with a fear of having to pay for the first one.

David Wright

The Chair agreed completely and raised a common complaint that is heard from many banks, around the challenge of digitalisation. There are new players coming into the market challenging all sorts of business lines. He asked if there is an understanding among regulators that there should be a level playing field and that an elephant should be regulated as an elephant. He asked if there are worries about creating an unfair regulatory disadvantage for what might be called 'the classic banking sector.'

Jean Lemierre

Jean Lemierre agreed that there are and referred to what China is doing. Earlier discussions with the People's Bank of China (PBOC) were clear and speeches have been made that well explain the danger of non-regulated financial-services providers, so it is right to put this in order. Europe will see the same and it is a surprise to see the flow of money being invested in some of these competitors. Current catastrophes are not far from this, so supervisors and regulators need to know what is required. It is important to know if they want to continue to guarantee deposits and offer a safe environment for people and if they want institutions that are able to lend to the economy, knowing their clients over the cycle. 2020 showed that it is better to have it than not. Not paying attention not only to unfair competition but to the unsafe world is a problem.

Maybe the market is more aware of this. When looking at the valuation of some initial public offerings (IPOs), people begin to have doubts about this type of competition and to tell others to be careful as it cannot stand for too long. Monetisation is key and digital is paramount – and banks must do it – but there is a need to ensure that this type of new entity is used to put banks under pressure to move forward, not to simply kill them. When it is dead, it is dead, so fair competition is needed. The same is heard from China and from others. When the head of JP Morgan is making a speech about this, it is a warning. The problem is any opposition is responded to as if it is out of a fear of competition. Competition is fine. Competition should be fair, and about efficiency and the protection of people.

There are worries about this type of entity, but, going a step further, non-banking financial activities also need a careful review, because there is plenty of liquidity in the world. Money is cheap, which is exactly what is needed and decided by the central banks. They are right, but it does create unintended consequences. Banks, as well as regulators and supervisors, need to be careful around unintended consequences, because they may have a big impact on the banking industry and on people. There will be destruction of value and bad reputations and the blame will not fall on the non-banking financial industry but on the banks.

This is a strange world, but it cannot be reasonable to see highly leveraged – to the point of tens of billions – non-transparent institutions that have not done the job, not from a legal but a moral point of view. There are serious questions about this. There is a lot to do, and it needs to be done together, so Eurofi is helpful in sharing views. Banks have to take part of the blame. Action is needed, while being careful, notably on risk management. Regulators should also be careful about non-banking entities, which, in some cases, are based on the new technologies mentioned. There is a lot to do, and more discussions on this are welcome.

David Wright

The Chair noted that it is always stimulating to talk to Jean and there is never enough time. Sir Jon Cunliffe participates in the Financial Stability Board (FSB), which, as is well-known, is now looking carefully at non-bank financing, because some of the problems that have arisen have come in that sector. In a way, the global regulators are on the job. He thanked Jean Lemierre and looked forward to the next conversation.