**“Being a European banks supervisor:
Building the dreams or burying the hopes”**

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1/ So we shall start this roundtable by about the perception of the regulatory construct in European banking. It seems to have stalled a little bit versus going very strongly after the various crises. What is your perception of this and where do the arbitrage pan-European vs. Local stand?

The creation of the Banking Union aimed at two objectives: (i) improving our crisis prevention and crisis management tools, and (ii) creating a truly integrated banking market. Their concurrent completion was intended to enable:

- improving the financing of the European economy;
- and to increase the resilience of its euro area banking and stabilising of the euro zone through the diversification of assets in balance sheets and the establishment of cross - border banks.

The first objective was partially achieved through the successful transfer of supervision to the European Central Bank (ECB - SSM), the reduction of Non Performing Loans (NPLs) and the creation of a framework for resolution.

However, little progress was made in achieving the second objective, which was not shared by all the Member States which are *mainly host* countries, compared to the singular pattern of the French banking sector (France is the seat of 4 of the 8 global systemically important banks in the euro area, its banking system is therefore a priori rather positioned to consolidate neighbouring sectors).

2/ There seems to be a general consensus that pan-European consolidation is probably the way forward but it seems that banks remain very reluctant to get it done. Some claim the digital transformation is a factor, others the inability to get the Banking Union completed, some other the constraints on liquidity circulation within the Eurozone. Can you update us on this with maybe what are the strongest hurdles against consolidation and when (if ever) we can expect things to change?

2.1. The economic benefits of consolidating the banking union are manifold:

- The creation of the Banking Union in 2012 was first and foremost the requirement to reduce links between banks and sovereign;

- The ultimate objective of the Banking Union is to enable a better allocation of savings to investment needs (financing union and investment union), fostering the absorption of economic shocks, common growth (including for highly investment-intensive projects such as energy transition);

- the consolidation of financial players at the European level makes economies of scale possible and promotes the competitiveness of the European economy through the emergence of pan - European players: promoting the construction of a European financial market that is deep up to its own economy, in order to diversify the sources of financing of corporates; increase availability and scale of capital to support innovation and growth; and ultimately increases long-term capital reserves.

2.2. However, the **European banking** industry is **still** fragmented: the concentration of the European market is relatively low compared with its peers: the 5 largest banks account for 20% of the European market, compared with 40% in the United States. While it can certainly be argued that it may also be appropriate not to encourage the creation of too big a systemic entity. The European banking sector appears to be «oversized» in number of entities (with a negative impact on profitability and possibly financial stability as a result of increased risk taking) and total assets.

2.3. The **main obstacles** to **the consolidation** of the banking union relate to the issue of risk sharing and responsibilities between home and host supervisors for cross - border banking groups, and the final impact on national public finances of a possible bank failure.

In most cases, the «host» supervisor seeks to maximise the level of capital and liquidity that the subsidiary of a cross-border banking group is required to maintain at the local level, fearing the lack of intra-group support in case of significant difficulties in the parent and/or its subsidiary.

2.4 Within the EU and especially within the Banking Union, our **goal is to reduce cross-border regulatory differences** in order for banks licensed in the Banking Union to operate seamlessly within the Union. A useful step towards this goal could be to lower capital requirements for European subsidiaries, while safeguarding their financial position, through credible cross-border guarantees provided by the parent company, which could be triggered both in normal times and in crisis situations. This would be based on European Union law and enforced by European Union authorities.

3/ The recent Draghi announcements seem to carry the risk of bringing the European banking sector further away from any sort of normality assuming tiering is announced and if bank debt is included into QE. In your opinion, should we privilege the short term profitability of the sector or its structural integrity – accepting bad profitability but at least under normalised conditions?

As a supervisor, I can only prioritise structural integrity. A bank is a firm, it must be structurally profitable. Low rates are a challenge for banks. After a rather positive balance thanks to lower refinancing costs, the more sustainable maintenance of low rates is weighing on the profitability of the industry at the same time as it has to undergo structural change related to digital transformation.

It is important to act on the different elements:

- reduce cost basis (in some cases transformation/evolution of banking networks)

- pursue diversification strategies (a model of universal banks "French" - retail banking, CIB, asset management, insurance)

- benefit from the single European market (cross-border consolidation)

4**/ It seems that the United States are pushing towards less regulation and have loosened the knots on a certain number of topics – which is clearly helping the success of US banks in Europe. Is there any chance the European supervisor could take that view and be slightly more lenient on capital?**

The US are pushing towards less regulation for small and medium banks

In the EU, we have made the choice of the principle of maximum harmonization which is essential to the deepening of the Banking Union. Institutions with a European banking license are allowed to conduct cross-border activities within the EU due to their pass porting rights. Due to the potential risks of these cross-border activities, it is in our view necessary to apply the most stringent rules (the whole Basel III agreement) to these banks.

Moreover, the history of financial crises has shown that disruptions in the financial system often originate from small- or middle-size institutions. It would be a mistake to decrease regulatory requirements and the intensity of supervision on these institutions.

5/ Basel IV remains a big shadow overarching European banks stocks. I would like us to assess it under two different perspectives: first, the political perspective. When do you think B4 is likely to be transcribed in European law and how loyal the European transcription is likely to be versus the initial Basel text? And second, more technically, how is the ECB likely to look at the solo vs. consolidated requirement? Is there a danger for the French mutualist model? Isn't it very toxic to rewrite a history that has proved consistently successful?

The EBA delivered its call for advice, which allows the Commission to launch the work with the aim of having a proposal in early 2020. After the uncertainty is still strong, the time frame for the discussions in the Council and Parliament is still strong.

The content of the Basel agreement is to implement the Basel accord. We have 3 main issues:

- As regards the application of the level of capital floor (output floor), we need to ensure that the application only takes place at the consolidated level of the group, in order to avoid unnecessary and costly ring - fencing of capital in some subsidiaries - more generally, an application at the level of subsidiaries would condemn the project of a true single banking market. This is the spirit of the Basel 2017 Basel accord and an unjustifiable and unjustifiable over-transposition would be an incomprehensible and unjustifiable over-transposition.

- balanced treatment of housing loans**,** taking into account characteristics that could make such exposures much less risky in Europe than in the United States.

- less penalising specialised financing activities, a business at the heart of French and crucial investment and investment banks for the European economy (aeronautical financing, infrastructure, energy transition etc.). In this respect, it can be recalled that the Union of Financial Markets cannot be achieved without strong European investment and investment banks; this is an issue of improving the sovereignty of the Union's financing, facing competitors in particular US.

7/ PSD2 is revolutionising the payment industry. It seems that so far all new regulation in open banking etc is favouring customers as opposed to incumbent banks. Is it realistic to supervise new entrants? How can the supervisor ensure fair competition by looking that are using banks' networks and engines without directly paying for it? Also can BigTech be forced into complying to some modicum of financial supervision? Is it all too late?

Obviously, we all need to take the digital turn. Digitalisation shatters our way of living and consuming, and offers businesses and consumers a world of opportunities. Globally, it clearly represents an opportunity and a challenge for banks, as well as for supervisors.

The ACPR is actively working on these issues. Last year, it published a discussion paper on the implications of IA for the financial sector. And this year we are working with financial industry players on the implications of IA algorithms in three areas: AML-CFT devices, internal models and customer protection.

Beyond traditional players, new entrants are now becoming increasingly important.

- Fintechs position themselves in niche markets but do not have sufficient capital resources to destabilise traditional banks, which can even acquire them.

- Instead, Bigtechs have the potential to fundamentally redefine financial intermediation: they have a strong brand image, a global customer base and privileged access to advanced technologies. This new environment poses a major challenge for regulators and supervisors.

Of course, financial regulation must remain technologically neutral: the core principle «same activity, same rules» continues to apply, and the level playing field among players is welcome.

Beyond traditional financial regulation, however, international cooperation needs to be developed in three areas, the three cornerstones of the regulation of digital finance.

- First, cyber security: a sine qua non for a secure and sustainable digital future, it clearly represents a priority for the French Presidency of the G 7.

- Second, with regard to data protection, financial supervisors and privacy authorities must invent new forms of cooperation to deal with data issues that have become central to financial services.

- Third, with regard to competition and anti-trust policies, the situations in which an actor is the winner (the winner takes most) while remaining outside the scope of financial regulation should be anticipated and adequately addressed.

8**/ Anti money Laundering (AML). This major theme should be one in which the SSM should excel. Do you think it is the case? What has to be done to improve the fight here? Does the SSM have enough resource to supervise this area efficiently? What is the mission of the EBA and what can they do in AML? Are they credible?**

The Commission has proposed a plan with 26 **non-legislative** actions to be implemented by the end of 2019. These actions are mainly entrusted to the European Supervisory Authorities (ESAs). In particular,

(i) strengthen cooperation between supervisory and AML-CFT supervisors;

(ii) better capture the risk of money laundering and terrorist financing in prudential supervision and increase convergence of practices in this area;

(iii) improve the capacity of the ESAs to make better use of their powers and competences.

Several actions have already been implemented, but efforts must be continued[1].

Adopt guidelines or draft Level 2 European regulations provided for by the CRD V or the amended EBA Regulation to take full advantage of the European reforms in response to the various cases of CB-FT since 2018.

The CRD V provides for the adoption of a number of EBA guidelines in the area of AML-CFT, including:

- on the fit and proper checks of the managers of financial institutions in the event of an attempted AML-CFT operation;

- on the modalities for cooperation between supervisory supervisors, financial intelligence units (such as Tracfin) and AML-CFT authorities, in particular with regard to cross-border groups and in the context of detecting serious breaches of the AML-CFT rules.

The EBA (ESA*s Review*) Regulation provides that a Commission Delegated Regulation defines the information on the shortcomings of financial institutions in relation to AML-CFT that are to be collected by the EBA-CFT and national supervisory authorities, as well as the modalities for analysing and sharing such information. **This is a particularly important point for the EBA to exercise its full mandate towards national AML-CFT authorities.**

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[1]Signature of the Agreement on the Exchange of Information between the ECB and the National AML-CFT Authorities in January 2019; strengthening peer reviews of national AML-CFT authorities. Other actions are being finalized: the guidance of the ESAs on the establishment of AML-CFT Supervisory Colleges, the updating of the advice of the ESAs on the risks of the European financial sector, etc.

Promote a strong network of European AML-CFT supervisors that brings together EBA and national supervisors, using a risk-based approach

In its Action Plan, the Council invites the **Commission** to ***propose longer - term actions*** *aimed* at *improving the prudential and anti - money laundering frameworks based* on *a thorough assessment, including a rigorous post mortem exercise*.

The aim is to promote the establishment of a strong network of AML-CFT authorities, conducted by EBA, which should have the human capacity and resources, in the most serious cases, to carry out joint emergency actions or to temporarily replace a national supervisor in the most exposed countries or sectors at the risk of CFT-CFT, which should have the capacity to do so, This would ensure greater vigilance. This proposal implies the adoption of a new European Regulation aimed in particular at amending the EBA Regulation.

Furthermore, **a reinforcement** of **AML-CFT requirements is desirable at the European** level, in particular with regard to the internal control of the AML-CFT framework. This implies an amendment to the *Anti* - *Money* Laundering Directive.

9/ The ACPR and the Banque de France have been widely criticised by the introduction of a countercyclical buffer on banks‘ French exposure. What did motivate this decision? Isn’t this a little bit too much for French banks considering the uncertainties of Basel IV and also considering their risk track record (which is authentically good)?

The decision on the contra cyclical buffer is not the responsibility of the ACPR. The High Council for Financial Stability, the body chaired by the Minister, is the authority of the macro prudential authority in France.

The indebtedness of the French corporates increases much faster than in the other EU countries. We are now significantly above the euro area average. The sustainability of this debt, and the impact of an upward shock on interest rates or on the downside on activity, arises. This is especially the case since the macroeconomic environment is becoming more uncertain (trade stress, Italian budget, *Brexit*, yellow gilets).

Faced with this situation, it was necessary to avoid an unlimited race to debt, which was the decision to set the cyclical buffer at 0.25% on 1 July 2019 and 0.5% on 1 April 2020.

It is not a question of curbing credit today but rather of holding underlying reserves in the face of a turn of the cycle tomorrow.

10/ To finish on a positive note maybe, a bit of perspective on the Banking Union and its three pillars, four years after its launch: areas of satisfaction and aspects to be improved

We have made good achievements on the first two pillars even if there is still place for improvements.

The Single Supervisory Mechanism (SSM) is now well established. Looking at its main objectives, it is clearly a success:

1 - Restoring confidence in the banking sector: bank capital was raised, credit risks are tackled, in particular the large volume of legacy non-performing loans and inconsistency and high variability in the capital requirements are addressed.

2 - Breaking the adverse link between banks and sovereigns: risk reduction has been achieved to a large extent, **however** there is no agreement at international level how to consider sovereign risk and building of an effective area-wide safety framework, including common resolution and deposit insurance frameworks, is lagging behind.

3 - Fostering a level playing field and banking integration: European norms directly applicable to banks (such as the Capital Requirements Regulation, or CRR),

however, still provisions established by European directives (such as the Capital Requirements Directive) that are not directly applicable but are transposed into national law and provisions that are purely national and still ring fencing requirement by host countries (Pillar 2).

4 - Exploiting the synergies between the ECB and the national supervisors: the Joint Supervisory Teams (JSTs), which form the operational core of the system in charge of day-to-day supervision, include ECB and national staff; a common supervisory culture among staff of different institutions is fostered; convergence to higher supervisory quality and global standards with a risk assessment methodology established to determine banks' capital requirements (the Supervisory Review and Evaluation Process).

5 - Bringing independence, transparency and accountability up to the best global standards: board's members are independent in the exercise of their functions and are supposed to serve in the European interest; conduct of public consultations for all new regulations and a right to be heard for banks affected by any decision.

The Single Resolution Mechanism (SRM) has made good progress but there is still lot of work to be done.

1 - Strengthening resolvability of banks: drafting resolution plans; identifying impediments to resolvability and making banks address them; binding targets for MREL at consolidated level (2019) and solo level (2020), **however** need to be more bank specific

2 - Fostering a robust resolution framework: development of SRB policies **but** need for more transparency (consultation process is needed); the Internal Resolution Teams (IRTs), which form the operational core of the system, include SRB staff and national resolution authorities.

3 - Preparing and carrying out effective crisis management: simplifications of processes to increase their efficiency; improving and developing ICT solutions for

crisis management, optimizing standardization of data request for valuation purposes; drawing lessons learnt from crisis cases and training SRB staff.

However, completing the Single Resolution Mechanism is needed:

First, the euro area needs a system for providing liquidity to financially sound banks after resolution

Second, it is necessary to have a consistent framework of the plans in the event of liquidation.

On the third pillar, deposit insurance, a compromise will have to be found in order to make headway on this pillar of the Banking Union. Once we have completed the resolution framework, we will be less in need of a shared European scheme. A pragmatic approach could be to introduce a system of loans between national deposit guarantee schemes (DGS), with guarantee mechanisms to ensure that liquidity advances do not lead to losses for the lending DGS. This would lead to a sharing of liquidity without sharing risks, which would be a first step towards shoring up financial sector confidence and strengthening depositor protection.