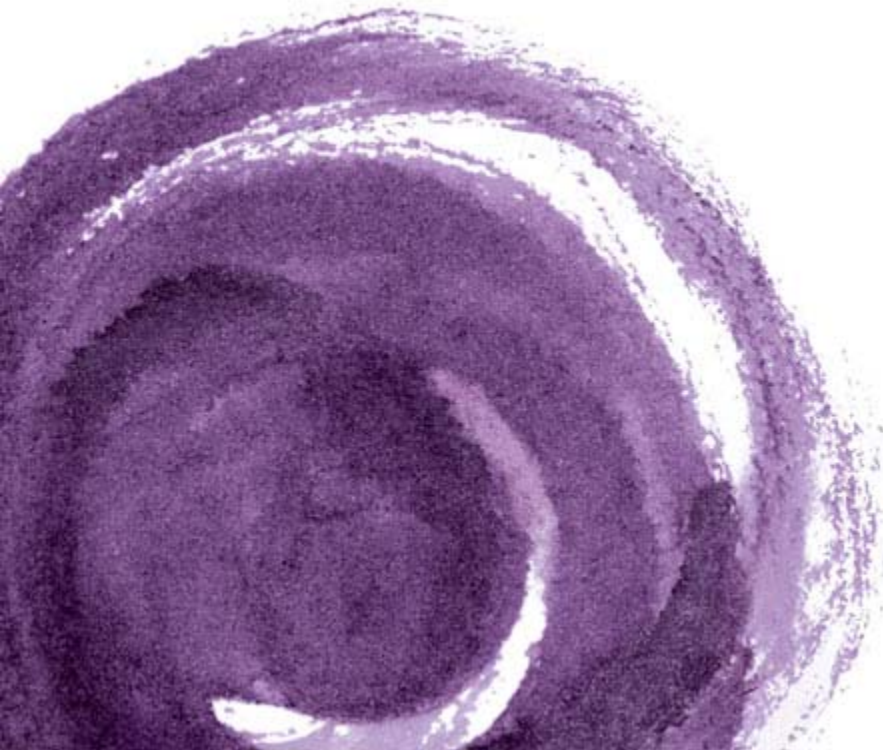




The solutions to reform finance are they the good ones?



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# Why did we have a financial crisis ?

- **We see three major reasons:**
  - High level of debt of some economic agents and repayment capacity supported by value of assets and not by income
  - Lack of regulation in some countries and for certain activities and failure of ABS-models by rating agencies
  - Poor assessment of risks in banks, notably in trading activities, which led some banks to hold too many risky assets

# The objective of political authorities to strengthen the global financial system

- **Some reforms decided by G-20 Leaders in Pittsburgh and London:**
  - Stronger capital requirements
  - Enhanced liquidity requirements
  - Leverage ratio
  - Global framework for regulation of derivatives markets
  - Stronger crisis management and resolution tools
  - Accounting and regulatory convergence
- **Other reforms planned by some governments:**
  - Implementation of a tax on banking activities
  - Restriction on proprietary trading for banks who benefit from deposit insurance funds (in the US)

## Effects on economic growth

- All political leaders concerned with resolving crisis
- Certain measures will be useful though they will affect economic growth, which benefited from the increasing indebtedness of economic agents
  - More capital and liquidity requirements will constrain volume of bank loans and increase their cost
  - It will amplify the macro-economic depression
- One of the key subjects : strength of new measures
- For cooperative banks and retail businesses, not easy to significantly and rapidly enhance capital

## Strengthening of capital requirements and reducing procyclicality

- Excessive use of leverage in period preceding crisis supports this approach
- Building up capital buffers can prevent excessive reductions in the supply of credit when the crisis starts
- Distinction between banking models :
  - Commercial banking model in France, Germany or Canada already requires much less economic capital than regulatory capital
- However, trading requires more capital when a Company holds assets which are not suitably liquid in a crisis
- We hope the forthcoming decisions on this matter will be balanced

# The strengthening of liquidity requirements

- **Lessons from financial crisis: market financing may disappear or at least reduce sharply for some weeks or months. However, after this period of time, circulation of information and intervention of central banks will stabilize market conditions**
- **Transformation of maturities (reconciliation between short-term investment horizons of investors and credit maturities expected by borrowers) is one of the principal foundations of financial intermediaries according to Economists**
- **Therefore, the NSFR (one-year ratio) may be very dangerous for sustaining economic growth**

# Convergence between financial standards and between regulatory rules

- One of the best results of these discussions is an objective to « reduce the scope for regulatory arbitrage and to work toward greater regulatory convergence »
- Still to be accomplished, particularly between US and Europe, though apparently a common goal
- Possibility of identical definition of capital and same application of regulatory rules
- Both sides of Atlantic seem to agree with common implementation in 2011 for Basel trading book rules

## The new framework must take into account the specificity of business models

- It's difficult to have rules that will treat different business models with the same severity (e.g. degree of disintermediation). The diversity in existing business models is itself likely to be a source of systemic resilience.
- Quantitative constraints (on risk, capital, balance sheet or liquidity) will not succeed in themselves. The evaluation of the effectiveness of bank management is important.
- The key elements that has been overlooked by the committee is the importance of improved supervision. More regulation will not compensate the failure of supervision observed in a number of countries.

# Regulation of global financial markets

- Reinforcing financial regulations depends on historical and legal traditions and certain countries (e.g. the US) fear impact of excess regulation
- However, all financial markets are connected and, if weaker regulation exists elsewhere, it will undermine the entire financial system
- Improve the clearing house role will reduce the illiquidity of the derivatives products
- What type of regulation for rating agencies?
- We hope the G-20 Leaders and the Basel Committee will finally succeed in creating a « level playing field » and coordinate the resolution of the crisis better than in the past

# Banking tax

- **The last topic of the states is a plan for creating a new banking tax**
  - Context of plan: need for money from European States
- **We strongly disagree with this tax**
  - It will increase the cost of credit
  - It seems to be an answer for lack of supervision in the past - We think that better regulation is the right answer
  - Depending on how it will be managed, it may increase moral hazard
  - Furthermore, State intervention during crisis in French banks was highly beneficial (€2 bn in revenue)

## Split between banking activities

- The US Congress wants to separate proprietary trading and commercial activities, even if this will not be a revolution
- Not easy to implement and characterizes US banking to date
- European banks are not very enthusiastic though this is an interesting question in light of poor management of trading portfolios
- Vocation of commercial bank as hedge fund?