

**Round Table**

***Post G20: Milestones to Restore Confidence within  
Financial Markets and New Business Opportunities  
in the Post-Crisis Environment***

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# **Post G20: milestones to restore confidence within financial markets**

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## **1. Post G20 guidelines: what priorities for the market professionals?**

- **Last year, here in Tokyo, I delivered three messages regarding the bilateral investment opportunities between France and Japan:**
  - First, there are many opportunities in France for investors, issuers and financial intermediaries due to the characteristics of the Paris financial place
  - Second, the crisis provided evidence of the needs for further cooperation and convergence
  - Third, France-Japan is a financial axis to be developed, especially considered to comparability between the financial system of these two countries

## **1. Post G20 guidelines: what priorities for the market professionals?**

- **The situation has changed.**
- **Last year, the financial system was severely impacted by Lehman's failure: the disappearance of interbank markets implied that there wasn't any possibility to access liquidity except towards central banks**
- **Today, we all can envisage a new period of economic growth**
- **The three messages are still accurate, but G20 has put in the limelight some directions the industry has to take**
- **Indeed, G20 has made important decisions which I propose to classify in three categories:**
  - Organization of financial markets: standardization of OTC products (mainly securitization), transparency on the markets (bond markets and securitized products)
  - Prevention of systemic risks: prudential rules, central clearing of credit derivatives and potentially of all standardized derivative products, and accounting standards (even if this last item is less advanced)
  - 'Moralization' of financial system: provisions about non cooperative jurisdictions, bonuses of markets professionals

## **1. Post G20 guidelines: what priorities for the market professionals?**

- **While adapting to G20 regulatory consequences, banking activities are led by two priorities:**
  - First, the restoration of profitability in a context where the margins of retail banking activities will be durably low. From the Japanese experience in the 90s we know that the difficulty for a banking sector to restore its position is one of the cause of the difficulty for the entire economy to come back to a high level of economic growth
  - Second, actions to re-launch some markets whose role is of paramount importance for the financing of economic growth: securitization, covered bonds, secondary bond markets, listings of small and medium companies

## **1. Post G20 guidelines: what priorities for the market professionals?**

- **France and Japan are legitimate to have a leading role in the revitalization of markets**
  - Their banking system was resilient, with an equilibrium between commercial activities (for both retail and professional clients) and proprietary trading
  - No failure of major banks, no durable recapitalization by public funds
  - Efficient architecture of Regulation and Supervision (incoming reform in France)
  - Major market and post market infrastructures. In Paris: NYSE Euronext Paris (first Euro stock exchange), LCH Clearnet (first integrated clearing house for both securities and derivative instruments), Euroclear France for settlement
  - Strong currencies: Euro and Yen

## **1. Post G20 guidelines: what priorities for the market professionals?**

- **Direct consequences of the G20 decisions provide evidence of this legitimacy:**
  - Need of efficient infrastructures for trading, clearing (at least for CDSs) and settlement
  - Need of resilient and conservative banks that do not create systemic risks even when large
  - Need of proposals for revitalization of financial markets
  - Need of currencies which could be an alternative to the leadership of the dollar

## **1. Post G20 guidelines: what priorities for the market professionals**

- **In the same time, the two greatest financial places – New-York and London-, have been deeply impacted by the crisis for several reasons:**
  - Real estate crisis
  - Credit policy
  - Failure of major banks
  - Need for massive public intervention in the private sector (hundreds of billions USD in the USA, more than one hundred billion GBP in UK)
  - Fragility of a pure investment banking model dominated by own account activities
  - Fragility of a retail banking model built around securitized and risky real estate loans
  - Volatility of currency valuation

## **1. Post G20 guidelines: what priorities for the market professionals?**

- **In this global context, France is ready to activate these new market segments and French banks have a leading role:**
  - As regards securitization, by the creation of a label for new products based on three characteristics: simplicity, standardization, transparency. Securitization is vital for the financing of economy, even more since capital requirements will increase
  - As regards covered bonds, by the widening of possibilities to issue these tools for the financing of the banking sector in order to enhance its capacity to finance the economy
  - Commitments to animate secondary bond markets; primary markets have known a spectacular revitalization in 2009 but have to be accompanied by at least a 'sporadic' secondary market which would allow investors to value the products
  - Small Business Act to help the of listing small and medium enterprises on regulated markets



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## 2. New strategies and business opportunities in the post-crisis environment

- **As regards the financial place of Paris, I recall that:**
  - As shown in the “Global Cities attractiveness survey 2008”, Paris is a financial place worth investing
  - French banks are among Leaders in Europe: BNP Paribas is the 1st retail bank in Eurozone; four banks among the ten first in Europe: BNP Paribas, Société Générale, Crédit Agricole and BPCE (born after the merger between Caisses d’Epargne and Banques Populaires)
  - French banks have proved their resilience due to four reasons:
    - Credit activities based on the capacity of the borrower to repay, absence of real estate bubble, majority of fixed rate credits
    - Only a few banking loans have been securitised
    - A high level of bank deposits
    - A high level of equity
  - Investment banks are very dynamic on sectors less damaged by the crisis:
    - A strong asset management industry (19% market share in Europe)
    - Leaders in OTC Equity derivative markets
    - Major actors in structured finance (25% of market shares in Europe)

## **2. New strategies and business opportunities in the post-crisis environment**

- **I also recall that Paris is the N°2 Financial place in Europe and the first in continental Europe:**
  - 14,5% of market share in Europe
  - 237 foreign institutions established in Paris
  - 2,5 trillion euro of assets under management
  - Leader in OTC Equity derivatives, in structured finance
  - First in Europe for custody and securities services (33% of market share in Europe)

## **2. New strategies and business opportunities in the post-crisis environment**

- **Many opportunities in Paris for investors, issuers and intermediaries:**
  - Creation of a new label for securitisation
  - Covered bonds
  - Secondary bond markets
  - Small business act for listing of SMEs
  - Private equity
  - Real estate funds
  - Alternative asset management (including hedge funds indices)

## **2. New strategies and business opportunities in the post-crisis environment**

- **Paris and Tokyo mustn't be afraid of the competition with other financial centers while keeping their own characteristics.**
- **But while the most injured financial systems were not the French nor the Japanese one, global decisions could have side effects on robust systems while they were designed mostly to address the failure of the most fragile systems: unwarranted new capital requirements or constraints on “too big to fail” institutions**

## **2. New strategies and business opportunities in the post-crisis environment**

- **As a consequence, French banks are primarily focused on their development and on the business opportunities which appeared during the crisis in order to accompany future economic growth**
- **But they are also focused on the propositions made after the Pittsburgh G20 meeting in order to address the so-called “too big to fail” or systemic issue**

## 2. New strategies and business opportunities in the post-crisis environment

- **Several ideas have recently been raised in the UK or in the US:**
  - More capital, higher quality capital (more equity to address moral hazard), contingent capital
  - Reducing interconnectedness (contract counterparties)
  - Narrow banks: separating “utility” from “casino” banking
  - Stand-alone national subsidiaries, addressing “too big to rescue”

## **2. New strategies and business opportunities in the post-crisis environment**

- **These ideas find their cause in the failure of banking systems in the US or the UK but are not replicable for systems like the French or the Japanese one.**
- **In the end, the role of banks is to finance the economy, and this would lead to impair their capacity to lend.**

## 2. New strategies and business opportunities in the post-crisis environment

- **French banks have other views to address systemic risk issue:**
  - Considering capital requirements for market risks:
    - Replacing VaR by Stressed VaR
    - Making illiquid financial instruments ineligible to the trading book treatment
    - Exempting main government bonds from credit risk capital requirement
    - Making banks' internal models trustworthy
    - Checking their reliability through stress testing
    - Verifying their comparability through the benchmarking of standard portfolios
  - Considering liquidity rules:
    - Customization of the requirements through validated internal models
    - Regular implementation of “stress tests” helping to envisage the bank's solutions in the event of a specific or systemic exceptional shock, with central banks interventions
    - Healthy governance and an appropriate organization in terms of liquidity management.

## **2. New strategies and business opportunities in the post-crisis environment**

- Considering systemic risk:
  - Making crisis management plans compulsory and elaborating resolution procedures
  - Building up liquidity buffers and promoting prudent funding policies
  - Using Pillar 2 to assess risk concentration, business diversification and financial resilience through regular global stress testing
- In this specific area, we strongly believe that:
  - More capital is not an answer: among others Lehman Brothers and Citigroup were well capitalized
  - Separation between activities is not relevant and would lead to regulatory arbitrage in favor of less regulated institutions
  - Size is not, in itself, a systemic risk criteria

## Conclusion

- **The opportunities in post-crisis environment exist and can benefit to French and Japanese financial centers**
- **The regulatory evolutions have to be considered carefully since their consequences could be detrimental to the ability of banks to take these opportunities**
- **French and Japanese institutions are well prepared for the future revitalization of the markets and have many reasons to believe their model is efficient and competitive**

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