

CSFI

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Brussels for breakfast (42): A breakfast discussion meeting on EU regulatory issues, with Graham Bishop (grahambishop.com), Mike Vercnocke (City of London Corporation) held on Thursday, November 27, 2008, at the London Capital Club, 15 Abchurch Lane, EC4N 7BW from 8:30-10:15am.

November's summit of the G20 countries marked a clear shift from the old Group of Seven (G7) bloc towards a wider grouping, which was significant for Europe. Europe had put together a co-ordinated and unified stance ahead of the summit, the first speaker said. Their proposals include better risk management in the financial industry, closer supervision of credit rating agencies and hedge funds and reinforcing the role of the IMF as the rescue agency for troubled countries.

The next step is the formation of the five G20 working groups. Members thought little would happen until the next summit in London in April when President Obama will attend. One member said membership of those groups was being held up a debate over membership of the Financial Stability Forum. The European Commission wants a permanent seat but the US is resisting unless some EU member states get chucked off.

Charlie McCreevy delivered a hard-hitting speech criticising "regulatory deficiencies" and calling for strengthening of international regulatory standards. He said a strong element of the reform of the international financial architecture should be the consolidation of European representation. He now has 40 measures on his roadmap including prudential risk management and supervision, crisis management, and the strengthening of supervision and coordination. The first speaker said compared with five when he began as commissioner for international markets. Worryingly the Germans have set out of a very hard-line position, demanding a uniform regulatory authority for large banks.

McCreevy also insisted the Commission would put a clear roadmap in place to ensure that credit default swaps were cleared through a central clearing counterparty by the end of this year. One member said several companies were competing to offer clearing services so this was not so outlandish. The problem was that the EU was asking European firms to commit to using a European solution as well any US solution.

On Solvency II McCreevy criticised countries that wanted to remove the group support regime – which would allow integrated groups to move capital across subsidiaries. Small countries feared they would suffer capital flight if troubled insurers repatriated capital. One member said France was guilty of "really appalling abuse of power" by using its presidency of the European Council to sacrifice the group support regime in order to win small countries' support for its demand that insurers equity portfolios be deflated by 20% rather than a more prudent 40%.

In a separate keynote speech Jean-Claude Trichet at the ECB highlighted three factors that must be tackled: excessive focus on near-term returns; a lack of transparency; and the excessive pro-cyclicality of the financial system. He recommended tighter capital regulations for banks and a stronger role for the IMF in macro-prudential supervisions, among other things. In a further sign of a push towards greater regulation the Basel Committee laid out an extensive work agenda including issues such as leverage and the quality of capital. Meanwhile IOSCO is looking at four issues: accounting standards; “abusive” short-selling; transparency in markets; and credit ratings agencies (CRAs).

EU plans on CRAs were a huge cause of concern to members. McCreevy has finally published his plans. CRAs will have to be authorised and operate in full conformity with EU rules. They will be supervised by EU supervisors and face the sanction of the withdrawal of their licence. It is also proposing setting corporate governance standards for ratings agencies’ boards. One member said this raised the possibility that CRAs would leave the EU, which in turn make it impossible for EU banks to buy or sell products that lacked a rating. McCreevy might be determined to find a sacrificial lamb, one member said, but it was the investment community rather than CRAs that would pay the ultimate price.

The other major development was on insurance accounting standards and the decision by the IASB to allow EU member states to deviate from the common standard. One member said this was a repeat of the 2003 when Chirac unsuccessfully pressured the Commission to get the IASB to change policy. This time Sarkozy applied the pressure and the IASB gave way and allowed banks to apply internal models to calculate the value of products when an active market no longer insists. Members could not agree whether the IASB had shot itself in the head, or only the foot.

To change the tone the second speaker outlined what the City of London was doing in Brussels. Paul Sizeland, the new director economic development, was bringing a new focus to economic issues, he said. The City’s Brussels office was now permanent for the first time. Their officials were heavily involved in areas such as lobbying and was setting up supervision groups on key issues. But the general aim was to facilitate the work of financiers in the City in their dealings with Brussels. A much-needed function if the rest of the roundtable’s discussion was anything to go by.