

# CSFI

## CENTRE FOR THE STUDY OF FINANCIAL INNOVATION

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**'Banking Banana Skins 2010'. A round-table discussion on the CSFI's latest banking survey with the author, David Lascelles, Thomas Huertas (FSA), Andrew Gray (PwC) and Charles Haswell (HSBC).**

**Held on Wednesday, April 14, 2010, at Watermen's Hall, 16-18 St Mary at Hill, London, EC3R 8EF, from 12:30-2:15pm.**

A group of bankers, observers and regulators, representative of the three respondent groups of the CSFI's latest survey of banking risk, came together to discuss the findings of 'Banking Banana Skins 2010' at a recent round-table. The discussion centred on why exactly political interference, a novel risk ranked highest by bankers and non-bankers alike, and second by regulators, was so frightening. One speaker suggested that the prioritising of political interference by all three respondent groups was indicative of a wider change in the nature of perceived risk in the banking sector, marked by a post-crisis shift in focus from short-term to structural and institutional risk. He accredited 'Banana Skins' with providing an important insight into risk mentality.

An attempt was made to clarify why each respondent group regarded political interference as a threat; bankers were deemed to be concerned with its capacity to distort commercial judgement, observers with its moral hazard aspects, and regulators with the huge uncertainties inherent in governments withdrawing their support for banks.

One speaker made reference to the potentially conflicting objectives of the 'political establishment' and someone running a commercial organisation. Expanding upon this perceived discrepancy between political and commercial interests, another speaker noted the adverse effects of interference- such as the raising of capital requirements- at a time when banks should be releasing capital buffers. He went on to say that reducing capital reserve requirements by 3% would allow banks to make available £300bn in new lending to the economy. Another speaker conceded, with the benefit of hindsight, that it was political interference to recapitalise banks that had prevented a recession from turning into a depression.

The round-table discussion was also future-oriented (though the predictive credentials of 'Banana Skins' reports themselves were called into question), and the way forward was explored. One speaker stressed the need for a more joined-up response, as no single government, regulator or institution alone could successfully alleviate all of the risks identified in the survey. Another, in the same vein, highlighted the need to ensure that the same set of data was being monitored at national, European and global levels. Trust was singled out as a crucial building-block for a better banking system going forward.

One speaker spoke extensively of the need to repair the disconnect that he perceived as existing between microeconomic supervision and systemic analysis. Others agreed that this disconnect was a defining feature of the crisis. Assessing Basel III, the speaker favoured the setting of a range for core capital ratios, to ensure that ratios matched the level of systemic risk, which fixed ratios, in his view, would not facilitate. Fixing core capital ratios would sow the seeds for 'credit crunch two', which, this time around, couldn't be blamed on the banks. Another speaker provided a more positive assessment of Basel III, describing it as a disciplined and broad look at the full range of measures, including new capital and liquidity regimes.

The discussion concluded with a final look at political interference, with one speaker suggesting that banks and bankers get what they deserve. Others broadly agreed on the danger posed by 'knee-jerk reactions' and overhasty, politically-driven action. There was general consensus that an evident public backlash, and the emerging demand for heightened consumer protections, had left banks on the defensive. The way to mitigate political risk was by rebuilding trust - the major challenge which now lay ahead of the banks.