BANCO DE ESPAÑA
Eurosistema

18.11.2019

International banking regulation reform and current and future challenges

2019 Annual Convention of the *Asociación de Mercados Financieros*

Pablo Hernández de Cos
Governor

Ladies and gentlemen, good afternoon:

I should like to thank the *Asociación de Mercados Financieros* (the Spanish Financial Markets Association) and its Chair, Enrique Prados, for the invitation to participate in this annual convention, and also Sebastián Albella, Chair of the National Securities Market Commission (CNMV), for his kind introduction.

With such a distinguished group of financial market professionals as yourselves, I would like to share today an overview of the current priorities of the work programme of the Basel Committee on Banking Supervision, which I have had the honour of chairing since March. I would also like to highlight the main perceived challenges and risks to financial stability at global level and also in Spain.

A decade of regulatory reform in the international banking system …

LAS REFORMAS ACOMETIDAS POR EL COMITÉ DE BASILEA DESPUÉS DE LA CRISIS (BASILEA III) Y LAS REFORMAS ADICIONALES DE LA REGULACIÓN BANCARIA INTERNACIONAL EMPRENDIDAS POR EL FSB TIENEN UN ALCANCE AMPLIO Y EXHAUSTIVO...

BANCO DE ESPAÑA
Eurosistema

- Aumento de los requerimientos mínimos de capital
- Revisión de la definición de capital
  - *Mayor hincapié en el capital con capacidad real de absorción de pérdidas*
- Introducción de colchones macroprudenciales
  - *Colchón de conservación del capital, colchones para entidades de importancia sistémica, colchón de capital anticíclico*
- Revisiones exhaustivas del marco de ponderación por riesgo
  - *Riesgo de crédito, riesgo de contraparte, titulización, riesgo de mercado, riesgo operacional*
  - *Exposiciones frente a ECC, inversión de capital en fondos, riesgo de step-in y entidades no bancarias*
- Introducción de una ratio de apalancamiento
  - *Nivel mínimo y colchón para entidades de importancia sistémica mundial (G-SIB)*
- Marco de grandes exposiciones
- Ratio de cobertura de liquidez
- Ratio de financiación estable neta
- Requerimientos de información más detallada
- Requerimientos de capacidad total de absorción de pérdidas (FSB)
- Elementos Fundamentales para el Régimen de Resolución Efectivo de Instituciones Financieras (FSB)

The Basel III reform package addresses the shortcomings identified in the regulatory framework prior to the world financial crisis, in order to strengthen regulation, supervision and banking practices in the international environment, with a view to financial stability.

Basel III is the result of a decade of work and lengthy negotiations within the Basel Committee, under the leadership of my predecessors as Chair, Nout Wellink and Stefan Ingves.

The response of the Committee to the evident weaknesses in the banking system has involved an increase in the minimum capital requirements for institutions, and the introduction of improvements to the definition of capital, with greater importance given to the highest quality capital, known as common equity Tier 1 (CET1). The aim is to improve the capacity of institutions to absorb losses while remaining viable. Also, a number of supplementary requirements have been introduced: an internationally harmonised leverage ratio, two liquidity standards, limits on large exposures and a new macroprudential dimension.

Although many of these reforms are well known, let me remind you of their main characteristics.

The purpose of the leverage ratio is, on one hand, to check an excessive build-up of debt within the banking system and, on the other, to supplement the capital requirements, irrespective of risk measurements. It includes both a minimum requirement for all internationally active banks and an additional buffer for global systemically important banks (G-SIBs). This latter buffer has been designed to ensure that risk-weighted requirements are consistent with the leverage ratio requirements applicable to G-SIBs.

For the first time, international liquidity requirements have been incorporated in the form of two ratios: one short-term one and another more structural one. These requirements ensure that banks are more resilient to possible short-term distortions in funding access, while encouraging a more stable funding structure.

In order to mitigate excessive concentration risk, a framework has been introduced for large exposures, which includes a macroprudential consideration, insofar as it places stricter limits on exposures between global systemically important banks.

The financial crisis also highlighted how a microprudential focus is by itself insufficient to identify and, in the final instance, avoid or mitigate the build-up of systemic risk. Thus, the need for macroprudential instruments that contribute to safeguarding the stability of the financial system as a whole was made evident.

The new macroprudential dimension introduced by the Basel Committee has been an important step in this direction. For this purpose, in addition to the elements mentioned above, various capital buffers have been incorporated into the prudential framework, such as the buffer for global systemically important institutions, which seeks to address the externalities generated by such institutions, and the countercyclical capital buffer, which seeks to prevent and mitigate the systemic risks associated with excessive aggregate credit growth.

Another of the main objectives of the reform package has been to reduce the excessive variability of risk-weighted assets (RWAs), the denominator of the regulatory capital ratio. For this purpose, an output floor has been introduced, which establishes a minimum level for the RWAs obtained by applying the standardised approaches. This output floor has been set at 72.5%. Floors have also been introduced for certain parameters of the internal models that institutions may use to calculate their RWAs. The aim of these revisions is to re-establish credibility in the calculation of RWAs and to improve the comparability of the risk-weighted capital ratios declared by different institutions.

The Committee has sought, through the orientation of the reforms, to maintain a balance between the comparability and simplicity of the prudential regulatory framework, while maintaining risk sensitivity. For this purpose, a comprehensive review of the standards for credit, market and operational risks, among others, has been performed to increase the robustness and risk sensitivity of the standardised approaches, and to increase the comparability and reduce the complexity of internal models. Also, “new” risks have been incorporated, such as those arising from banks’ exposures to central counterparties.

Also, in order to strengthen market discipline, the Committee has substantially reformed the transparency requirements. These now cover a broader set of risks and information, and the way in which this information is transmitted to the market is more standardised in order to foster comparability across institutions.

These reforms are supplemented by those implemented by the Financial Stability Board (FSB). Notable among these, in relation to the banking sector, is the introduction of a number of requirements in relation to the total loss-absorbing capacity of global systemically important institutions, to ensure additional loss-absorbing and recapitalisation capacity in the event of resolution.

These requirements are based on the FSB document "Key Attributes of Effective Resolution Regimes for Financial Institutions," which sets out the core elements necessary for authorities to be able to resolve institutions in an orderly manner, without having to resort to taxpayer funds, in the event of idiosyncratic crises, even in the case of the largest, most complex and globally interconnected banks. In the European Union these requirements for total loss-absorbing capacity also apply to institutions that are not G-SIBs in the form of minimum requirements for own funds and eligible liabilities (MREL).

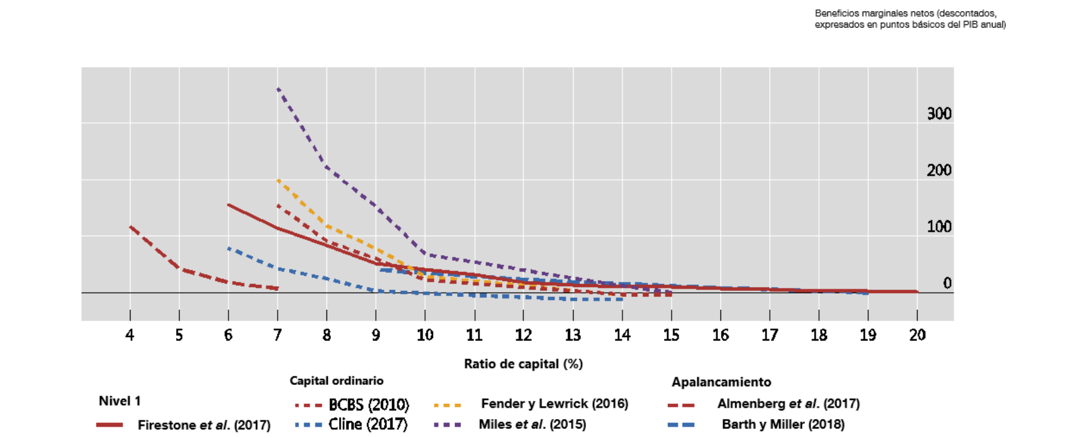
…has generated a significant increase in the resilience of the world banking system

As was to be expected, the Basel III reforms have resulted in a significant strengthening of the resilience of the world banking system.

... Y LOS BENEFICIOS MACROECONÓMICOS NETOS DE BASILEA III SON POSITIVOS...

BANCO DE ESPAÑA
Eurosistema

Beneficio macroeconómico marginal neto del capital



Fuente: Comité de Supervisión Bancaria de Basilea (2019): «The costs and benefits of bank capital – a review of the literature», junio.

Thus, since 2011, the common equity tier 1 (CET1) capital of internationally active banks has increased by 91%, to more than €3.7 billion. And the average risk-weighted CET1 capital ratio has risen from 7.2% to 13%.

High quality liquid assets have increased by more than 50% over this period to stand at more than €13 billion.

The average CET1 capital leverage ratio for banks has increased from 3.5% to 6%.

Also, it is likely that these figures will continue to rise over the coming years, since the introduction of some Basel III reforms will not be completed until 2022, with a transitional period for the output floor, which limits by how much RWAs may vary when using standardised and IRB approaches, that may not end until 2027.

Are all these reforms leading to adequate levels of bank capitalisation?
One way of answering this question is to refer to the findings of the economic literature that analyses the marginal macroeconomic impact of increases in financial institutions' capital ratios.

A paper published by the Basel Committee last June reviews the recent academic literature on the macroeconomic costs and benefits of higher capital requirements.[1]

This paper concludes that the net macroeconomic benefits of capital requirements are positive over a broad range of capital levels. Comparing Basel III with these estimates shows that the Basel III minimum requirement of 4.5% for CET-1 is clearly at the lower end of the capital levels that are estimated to have net positive benefits.

If the capital conservation buffer is added, we come close to the midpoint of the range and when the additional buffers for systemically important institutions are included, assuming that the countercyclical capital buffer is activated up to a maximum level of 2.5%, the final result is that the total capital requirements are still within the range of capital levels that are estimated to make a net positive macroeconomic contribution.

Overall, therefore, it can be affirmed that the Basel III reforms have resulted in capital levels that are within the estimated range of those that appear to have a net positive macroeconomic benefit for society as a whole, as a result of the greater financial stability and shock absorbing capacity they provide.

In short, there is no evidence to suggest that the capital requirements under Basel III are excessive.

The current priorities of the Basel Committee are full and timely implementation of the reforms and their evaluation …

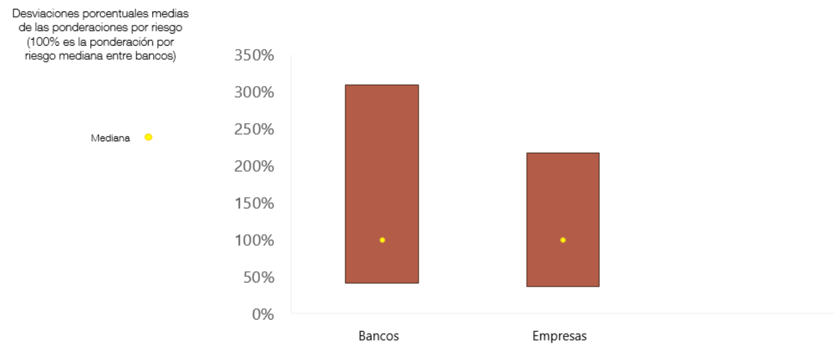
[1] Basel Committee on Banking Supervision (2019): "The costs and benefits of bank capital – a review of the literature", June, available at https://www.bis.org/bcbs/publ/wp37.htm.

Given this regulatory drive, we are frequently asked whether the reform process can be considered to have been completed. The completion of Basel III is certainly an important landmark and, in this respect, the priority must now be for the jurisdictions to fully apply the rules, within the periods agreed and consistently, as the G 20 leaders have repeatedly stated.

... PERO PARA OBTENER LOS BENEFICIOS DE BASILEA III ES NECESARIA LA APLICACIÓN PLENA Y A TIEMPO Y LA SUPERVISIÓN CONTINUA Y HOMOGÉNEA DE LAS NORMAS...

BANCO DE ESPAÑA Eurosistema

Excesiva variabilidad de los activos ponderados por riesgo: requerimientos de capital basados en modelos internos para carteras hipotéticas en la cartera de inversión (banking book)(a)



Fuente: Comité de Supervisión Bancaria de Basilea.
(a) El gráfico muestra la distribución normalizada de las ponderaciones por riesgo (el 100% representa la ponderación por riesgo mediana entre bancos utilizada como referencia) comunicadas por los bancos en el contexto del estudio de variabilidad de los APR de la cartera de inversión realizado por el Comité.

An important part of the current work of the Basel Committee is precisely to support this objective, through its Regulatory Consistency Assessment Programme (RCAP). The RCAP has contributed – and continues to contribute – decisively not only by highlighting the deviations of the locally implemented rules with respect to the standards agreed within the Committee, but more importantly, by reducing these deviations. This will continue to be the objective of the programme in future and, in fact, we are going to assess the programme to identify ways of increasing its efficacy.

... Y ES PRECISO EVALUAR DE FORMA EXHAUSTIVA EL IMPACTO Y LA EFICACIA DE LAS REFORMAS POSTERIORES A LA CRISIS...

BANCO DE ESPAÑA Eurosistema

Evaluaciones que está llevando a cabo el Comité de Basilea

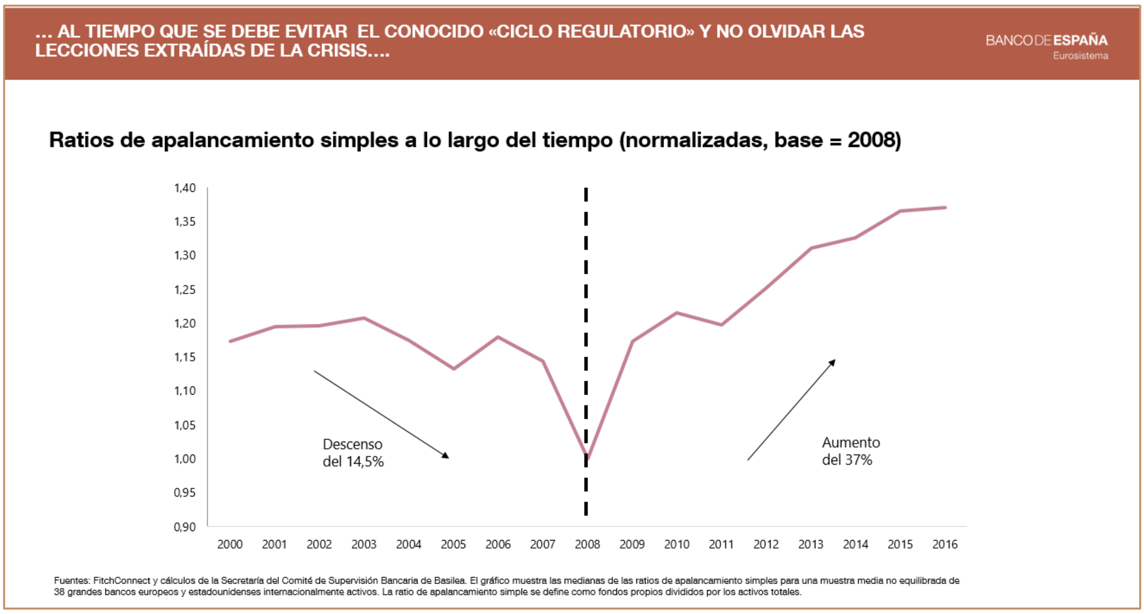
EVALUACIÓN DE REFORMAS INDIVIDUALES			
1) Definición de capital	2) Marco de riesgo de contraparte	3) Marco de titulización	4) Normas de liquidez
5) Marco de la ratio de apalancamiento	6) Marco de riesgo de crédito	7) Marco de ajuste de valoración del crédito	8) Marco de riesgo de mercado
9) Marco de riesgo operacional	10) Marco de grandes exposiciones	11) Suelo de Basilea III (*output floor*)	
INTERACCIONES Y COHERENCIA			
12) Interacciones entre las métricas de capital y de liquidez			
IMPACTO MÁS AMPLIO			
13) Impacto macroeconómico de los requerimientos de capital y de liquidez			

Beyond the necessary implementation of the standards agreed, now is also the time to initiate evaluation, without preconceptions, of the effectiveness and impact of the reforms.

In my opinion, it is imperative for any body responsible for implementing public policy, including, of course, the Basel Committee, to evaluate the measures and reforms approved. These evaluations should consist of a rigorous and transparent analysis and assessment of the impact of the reforms following their introduction. As such, they play a fundamental role in strengthening the credibility and answerability of the institutions.

For this purpose, the Basel Committee has launched a programme for comprehensive evaluation of the standards agreed, which includes an assessment of the effectiveness of each of the individual reforms, the interactions and coherence among them, and their macroeconomic and structural impact.

This is a multi-year programme that will be based on rigorous empirical analysis, supplementing the cross-sectoral evaluations being carried out by the FSB, in which the Basel Committee also participates actively.



Evaluation exercises should not be used as an excuse for relaxing the stringency of the agreed standards. Indeed, one of the main objectives I have set myself in my mandate as Chair of the Basel Committee is to combat what has come to be known as the “regulatory cycle”, according to which – and empirical evidence confirms this – our memory of crises and their negative effects tends to fade with time, the pressure of private interests grows and the temptation to relax regulatory standards increases.

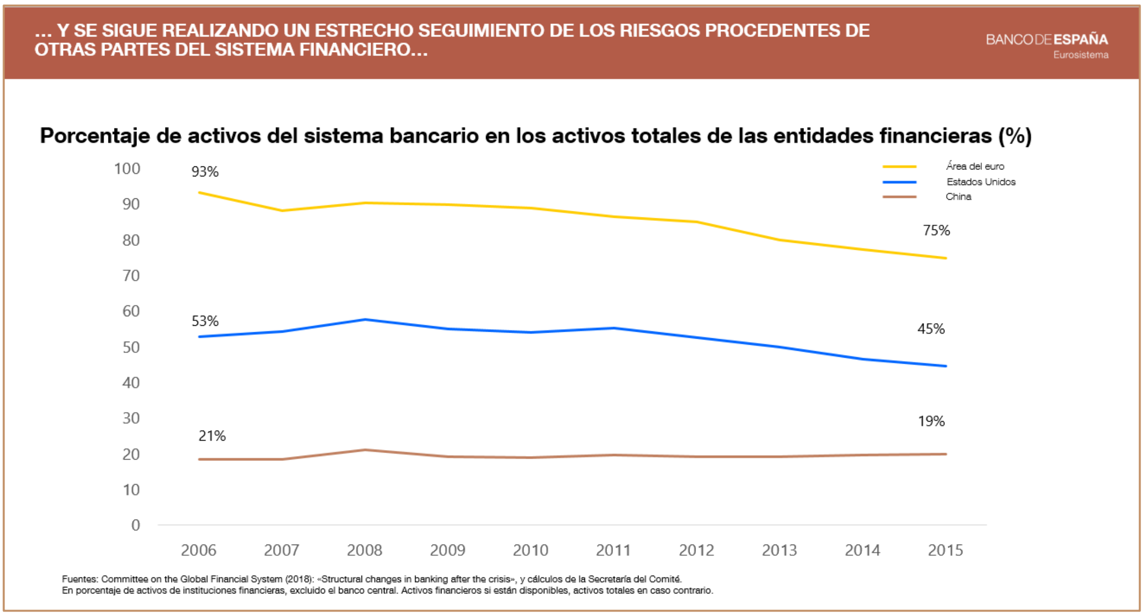
That said, we should keep an open attitude about the results of evaluations. If we were to find conclusive empirical evidence suggesting the need to review certain elements of the regulatory framework, either because undesirable effects are observed or because the goals pursued are not achieved, we should undoubtedly review them, and even adopt new measures if necessary.

In short, the reforms adopted are extremely far-reaching, and now is time to implement and evaluate them.

…and close monitoring of the new risks associated with the banking sector, such as those associated with financial disintermediation, the technological revolution and climate change

Above and beyond these objectives, the Committee has to keep up its continuous monitoring of the risks and vulnerabilities to which the global banking sector is exposed and adopt, where applicable, the required measures.

Indeed, the challenges currently facing the international financial sector are considerable. Some reflections will suffice to illustrate these new risks to which we must be alert.



First, it is obvious that the financial landscape after the crisis has changed. Specifically, in some jurisdictions such as the euro area and China, the percentage of assets held by the banking sector with respect to the total assets of financial institutions has progressively decreased. Thus, in China the weight of the banking system relative to the total financial system dropped from 93% in 2006 to 75% in 2015. In the case of the euro area, the decrease was somewhat less, but also significant (from 53% to 45%) in the same period. In jurisdictions in which banks have traditionally played a relatively smaller role in the financing of the economy, such as the United States, this percentage has not changed significantly.

Against this background, it is important to ensure that the risks associated with so-called "non-bank financial intermediation", and those derived from non-banks' interrelationships with the banking sector, are appropriately regulated and supervised. This requires, among other things, close monitoring of the regulatory perimeter of the whole financial system to ensure that market participants operate under the principle of regulatory neutrality.

Second, and partly related to the previous point, the impact of technology on the financial sector is having highly significant consequences.

Specifically, in the last few years we have observed growing interest by global technology, or "big tech", firms in the provision of financial services. It is clear that their size, customer base, lean cost structure and the huge amount of data they have, along with their technological capabilities, give these companies the potential to change the current structure of the financial system.

In view of this, we should keep in mind that, although "big tech" firms may help to improve the provision of some financial services, they may also generate risks to financial stability, consumer protection, competition and data privacy, among others. It is therefore necessary to analyse in depth these potential risks and, if necessary, change the regulatory framework so as to mitigate them.

Further, these developments may affect banks in different ways ranging from possible over-dependence on a small number of technology service providers to additional pressure on their profitability and effects on their current business models.

An example of the destructive capacity of technology on the financial environment is the development of so-called crypto-assets, particularly those known as *stablecoins*, of which the Libra project has received most attention. As the G7 has pointed out,[2] innovations of this type pose various legal, regulatory and supervisory issues. To respond adequately to

[2] G7 Working Group on Stablecoins (2019), "Investigating the impact of global stablecoins", October, available at https://www.bis.org/cpmi/publ/d187.pdf

these challenges, the FSB plans to analyse in the coming months the current supervisory and regulatory approaches and determine whether they are adequate to address the financial stability and systemic risk issues which may be posed by specific characteristics of a *stablecoin* or its overall functioning. After this review, we will, if considered necessary, propose multilateral responses, possibly including the development of global supervisory and regulatory approaches capable of addressing these financial stability and systemic risk issues.

The Basel Committee is currently assessing the implications for banks and supervisors of an increase in the use of *stablecoins*, looking at both the possible role that banks may play in the ecosystem of *stablecoins* and the risks which may arise. Specifically, one of the matters analysed will be whether supervisors have sufficient resources and an appropriate regulatory framework to monitor them.

Regarding crypto-assets, the Committee will shortly publish a discussion paper calling for opinions on what form its prudential treatment should take, and we will continue analysing what the implications of these developments are for banks and supervisors.

Lastly, the Committee is deepening its analysis in various technology-related aspects such as the use of artificial intelligence and so-called machine learning, the dependence of banks on unregulated third-party suppliers and data governance.

Furthermore, it is evident that the growing use of technology exposes financial institutions to more frequent, serious and sophisticated cyber-incidents. Recent surveys found that 80% of banks' risk managers consider cyber risks to be a priority issue, compared with only 10% in 2013. In this connection, in December last year the Committee published a report describing and comparing cyber-risk management practices of banks and bank regulators and supervisors,[3] and is currently reviewing operational resilience principles and guidelines in order to reflect more fully the risks associated with technological innovation.

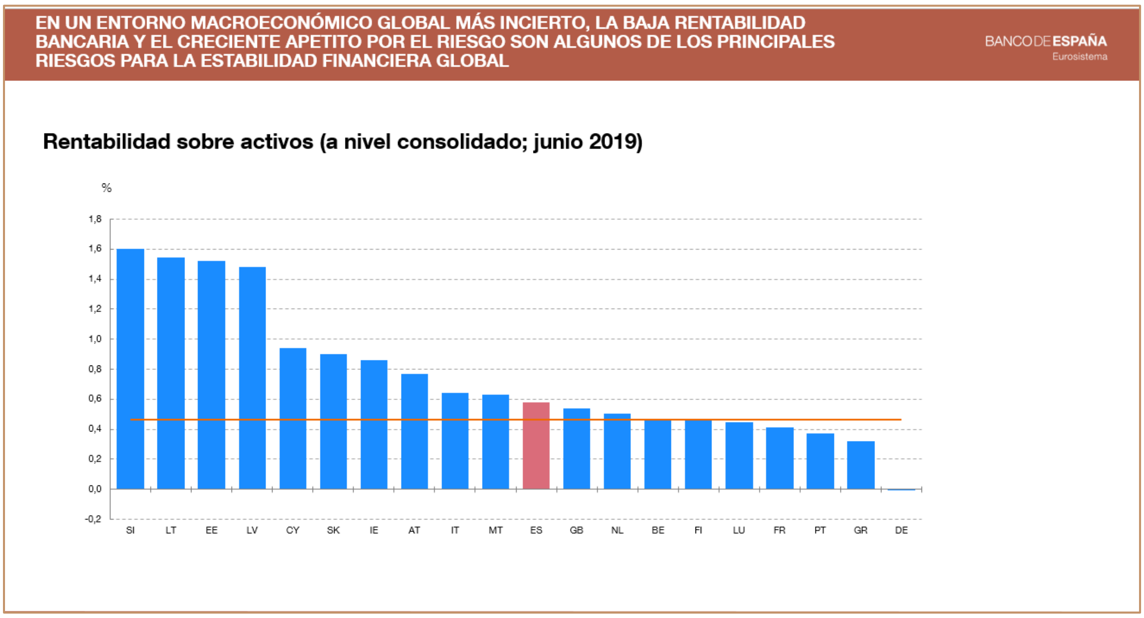
The third challenge facing the banking sector to which I wish to refer is environmental sustainability and climate change. On the one hand, the banking sector is exposed to both physical and transition risks deriving from climate change which include both credit risk and market and operational risk. On the other, the financial system has a crucial role to play as a provider of the funds needed to make the investments required for a more sustainable economy.

Against this backdrop, some months ago the Basel Committee joined, with observer status, the *Network for Greening the Financial System*, of which the Banco de España already formed part. This network will allow regulators and central banks to share experiences and best practices in the assessment and management of risks derived from the ecological transition in banks and at overall financial system level. In this same respect, last October the Committee decided to undertake various projects on the financial risks associated with climate change.

[3] Basel Committee on Banking Supervision (2018), "Cyber-resilience: Range of practices", December, available at https://www.bis.org/bcbs/publ/d454.htm

In a more uncertain global macroeconomic environment, low bank profitability and the growing appetite for risk are among the main risks faced by banks

Besides these structural challenges facing the financial sector, let me also mention some others of a more conjunctural nature relating to the world macrofinancial situation.



In the past year the global growth outlook has worsened and become more uncertain. Consequently, interest rates will probably remain low for a longer time in a large number of countries. Also, global indebtedness is at an all-time high. This macrofinancial setting poses risks of varying types to financial stability.

First, the macrofinancial setting to which I have just referred, together with the additional pressure exerted by some of the aforementioned structural changes and the persistence of some legacies of the crisis, means that in many jurisdictions the banking sector is finding it difficult to achieve levels of profitability which exceed its cost of capital.

It should be kept in mind not only that the ability to generate profits is financial institutions' first line of defence against the materialisation of risks, but that insufficient levels of profitability hinder the strengthening of their solvency.

In this setting, it is essential for banks to continue working to improve the quality of their balance sheets and raise their efficiency. One of the ways they can do this is by adapting their business models to technological change.

Second, the current low interest-rate setting and the pressure on bank profitability may encourage financial institutions to take greater risks.
The abundance of high-yield corporate debt and the participation of banks and other financial intermediaries in the funding of this market segment at world level, may be a paradigmatic example of this trend towards greater risk-taking.

Specifically, the available information indicates that the volume of high-risk debt in the form of leveraged loans and related securitisations (CLO) remains at high levels at international level and the vulnerabilities in this market segment have increased in recent years, since these products have lower credit protection and changes in the structure of the market have made it more complex and opaque.

Moreover, the available information suggests that banks are among the main direct holders of products of this type. These global developments have to be analysed in greater depth to fully understand their potential systemic implications.

In any event, in the environment described above, the capital and liquidity requirements of the Basel III framework help to prevent and contain the effects of excessive risk-taking.

What is more, microprudential supervisors have an important role to play. In this respect, the Basel Committee is a forum for enhancing cross-border cooperation in microprudential supervision through the exchange of supervisory approaches and techniques.

Macroprudential instruments also have a place in helping to mitigate the potential accumulation of risks to financial stability in a world macrofinancial setting like that at present.

Risks to financial stability shared by the Spanish economy…

Let me finish by looking at the Banco de España's assessment of the risks to financial stability in Spain.

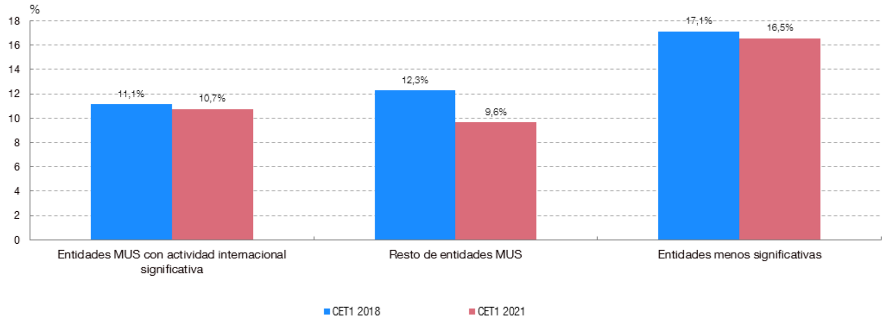
As you know, we published our autumn Financial Stability Report on 31 October. In line with the situation I have just described for the global economy, the report highlights a certain worsening of the balance of risks to financial stability in Spain.

The sources of risks to financial stability identified in Spain are similar to those identified at global level.

LOS EFECTOS DE LA RALENTIZACIÓN ECONÓMICA GLOBAL Y LA INCERTIDUMBRE GEOPOLÍTICA, LA BAJA RENTABILIDAD DE LAS ENTIDADES DE DEPÓSITO Y LOS RIESGOS LEGALES SON LOS PRINCIPALES RIESGOS IDENTIFICADOS PARA LA ESTABILIDAD FINANCIERA EN ESPAÑA

BANCO DE ESPAÑA
Eurosistema

Ejercicio de stress del Banco de España: impacto en Ratio CET1 FL bajo el escenario adverso



FUENTE: Banco de España.

The risks derived from the global economic slowdown and geopolitical uncertainty are affecting Europe and the emerging economies most strongly. A lower economic dynamism and a possible materialisation of geopolitical risk may affect financial stability in Spain in various ways. First, they may lead financial market participants to reassess their perception of risk. This would mean that the risk premia on financial instruments, currently highly compressed, would rise, which would reduce asset values and, consequently, wealth and collateral values. The segments hardest hit by these developments may be the most vulnerable ones such as that of lower-quality debt and the markets enjoying the highest valuations, subsequently extending to other assets.

Second, they might affect agents' income flows, with implications for their consumer-spending decisions and for investment. In the case of households, it may reduce job creation and wage growth. In the non-financial corporations sector, it would cut profit growth. In the public sector, the balance of non-financial revenue and expenditure would be affected by the operation of automatic stabilisers. As a result of all this, the levels of public- and private-sector debt may end up being higher than expected, with an additional impact on spending decisions and on the financial markets' perception of the course of debt sustainability.

Naturally, a worsening of the macroeconomic environment would also affect deposit institutions. The value of some of their assets would decrease and the demand for credit would weaken. Furthermore, asset quality would worsen, because the ability to pay of their borrowers would be adversely affected. They would also find it more difficult to continue disposing of their unproductive assets. As a result, their income statements would come under downside pressure.

This is particularly significant in a setting like that at present in which bank profitability is low. Indeed, this is the second most serious risk to financial stability identified in our report. Once again, it is not specific to the Spanish financial system. Although the profitability of Spanish banks is higher than the European average, it continues to be lower than the cost of capital, and this, as mentioned above, makes it difficult for them to strengthen their solvency.

Indeed, one means of assessing the suitability of banks' solvency levels involves subjecting them to stress tests. The Banco de España conducts these types of exercises annually for all Spanish banks. It takes as a starting point highly granular data from bank balance sheets at the close of the previous year. It then defines a baseline macroeconomic scenario, coinciding with the Banco de España projections available at the time the exercise is conducted, and another, stressed scenario, which attempts to reflect the effect of the previously identified risks materialising. The difference between the two scenarios shows the degree of stress of the exercise. The test performed this year is slightly more stressed than that of the previous year owing to the heightening of the risks to which I have referred.

The results obtained on the resilience of Spanish banks overall are generally positive. The capital requirements arising in the adverse scenario are moderate at the aggregate level, although there is substantial heterogeneity across banks. Specifically, the reduction in the CET1 capital ratio for large institutions with a significant international presence is 0.4 pp, while it is 2.7 pp for the other SSM-supervised institutions and 0.6 pp for less significant institutions.

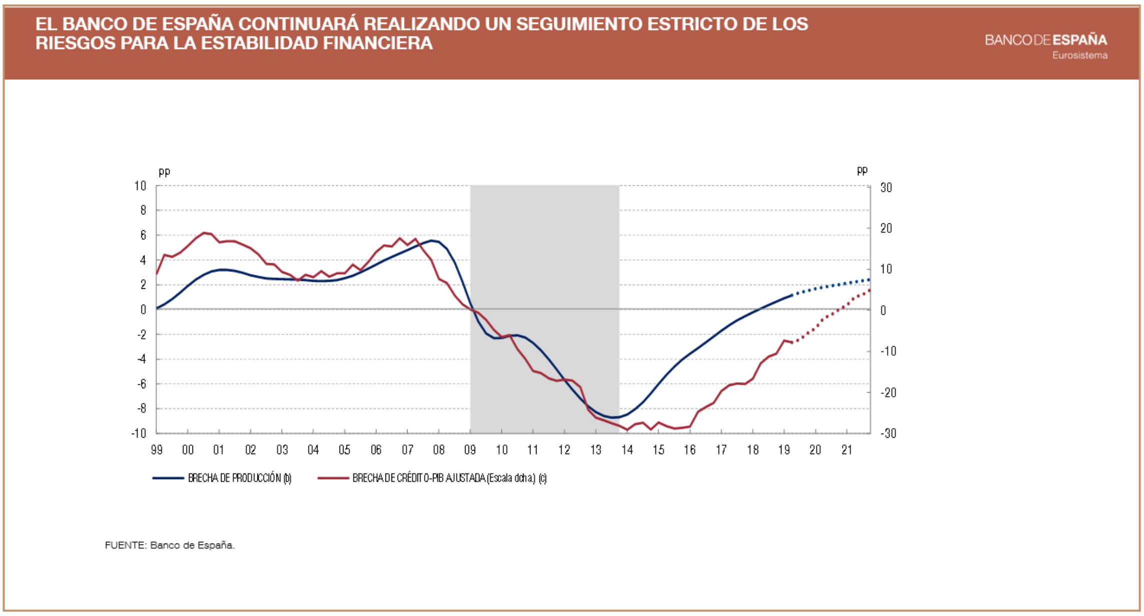
These results are broadly more favourable than last year. Institutions have used the past year to reduce their exposure to changes in the prices of some assets, such as foreclosures. Specifically, in 2018 and to date in 2019, banks have jettisoned sizeable packages of foreclosed assets.

The last identified source of risk in the report relates to financial institutions' operational risk. Operational risk accounts for 9.3% of the volume of Spanish deposit institutions' risk-weighted assets, slightly below the European average (10.5%). In any event, the deterioration in solvency associated with an operational risk event may be high based on past experience. In Spain's case, the potential materialisation of costs associated with legal risks continues to contribute to deposit institutions' operational risk. Processes linked to past litigation such as that of the floor clauses have had an estimated cost for the sector of over €2.2 billion to June 2019. Moreover, there are other significant legal processes that have yet to be resolved.

In any event, legal risk and some other factors relating to institutions' conduct have significantly impacted the banking industry's reputation, and not only in Spain. In this respect, we should recall that reputation and customer confidence are the key elements on which banking business is based. Accordingly, banks should strive to reverse this tendency by providing their customers with financial products and services tailored to their needs and capacities, as well as furnishing them with the relevant information clearly and transparently.

…which will be subject to strict monitoring by the Banco de España

Against this background of potential risks, and following a technical analysis combining quantitative indicators and qualitative information, the Banco de España has kept the Countercyclical Capital Buffer (CCyB) at 0% in the fourth quarter of 2019.



Specifically, the set of quantitative indicators steering decisions on the CCyB include indicators that attempt to capture the course of the private non-financial sector's credit cycle and its excessive growth, the position of the business cycle, the potential overvaluation of house prices, the affordability for households and firms of interest and principal repayments (debt service), the external imbalance and the macroeconomic environment.

The technical analysis assesses the recent trend of the indicators, their current situation and also their expected behaviour in the coming quarters consistent with the macroeconomic forecasts prepared quarterly by the Banco de España. Forward-looking analysis is particularly significant in this context since, if the CCyB is activated, institutions have 12 months in which to comply with the requirement.

In particular, the credit cycle indicator continues to post values below the activation thresholds (having regard to the credit/GDP ratio, which remains below its long-term trend), although it is progressively converging on equilibrium. The output gap, for its part, has been in positive figures since the start of the year, and forecasts about its future course continue to point upwards. Some supplementary quantitative indicators also suggest a rising trend over the next two years.

Overall, the analysis performed substantiates holding the CCyB at 0%, although it highlights the need to continue strictly monitoring both short-term risks together with the trends and projections for the indicators.

Conclusion

In sum, let me return to the legitimate question many of you have about whether we can declare the financial reform process to be over. The best reply I can give by way of conclusion is that, with the Basel III regulatory framework now completed, the main challenge is to ensure its full and timely implementation in all jurisdictions, while concurrently evaluating its effects. In parallel, we must remain alert and respond to the new risks the banking system faces. These include risks associated with growing financial disintermediation, technological disruption, climate change and those stemming from the macro-financial environment and its consequences for banks' business models and appetite for risk.

The objective of our work should remain the same: to safeguard and reinforce financial stability using macro- and micro-prudential instruments within a framework of cooperation and coordination between supervisory authorities at the national and international level.

Thank you.