



## **Future politics of the EU in the financial services market**

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# Outline

- **The EU banking sector**
- **The EU perspective**
- **Retail banking markets**

## Main goals of the presentation

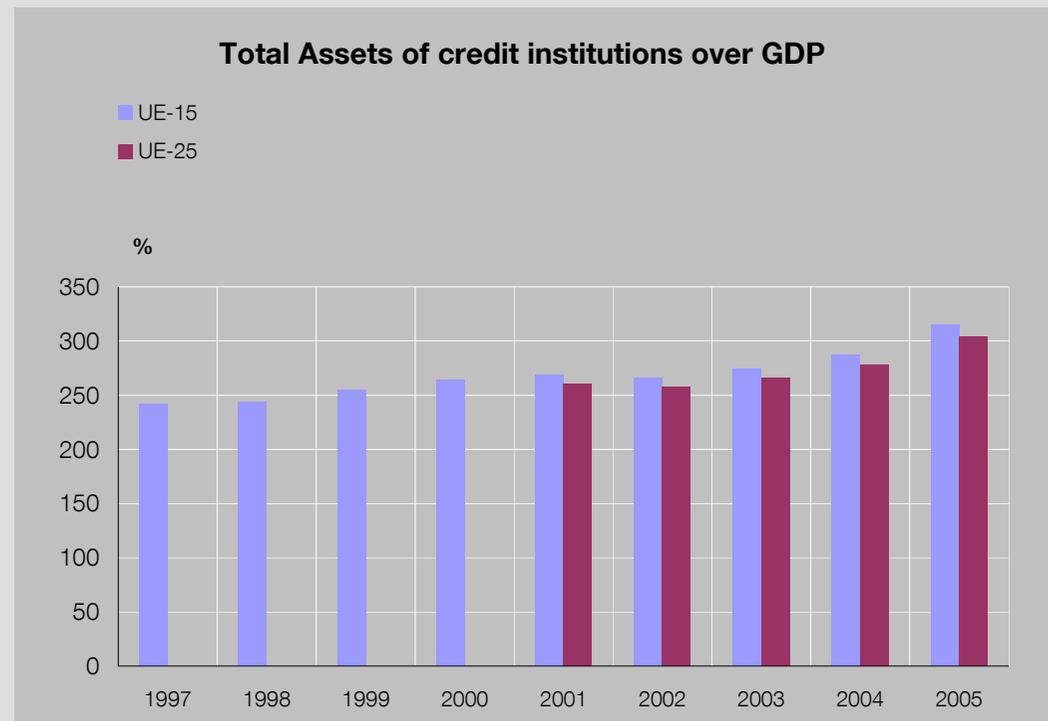


- To emphasize the progress made during last years towards a single financial market in the European Union ...
- ... but also to highlight that it is necessary to be cautious regarding retail markets integration
  - It is fair to recognize the legitimacy of the political idea of extending the benefits of a single financial market to consumers, but at the same time it is relevant to take into account the intrinsic characteristics of each country retail market

## The EU banking sector \_ general trends (1)



- In past years, banking activity in the EU has been increasing ...
- ... as well as the relative importance of the banking system in the economy

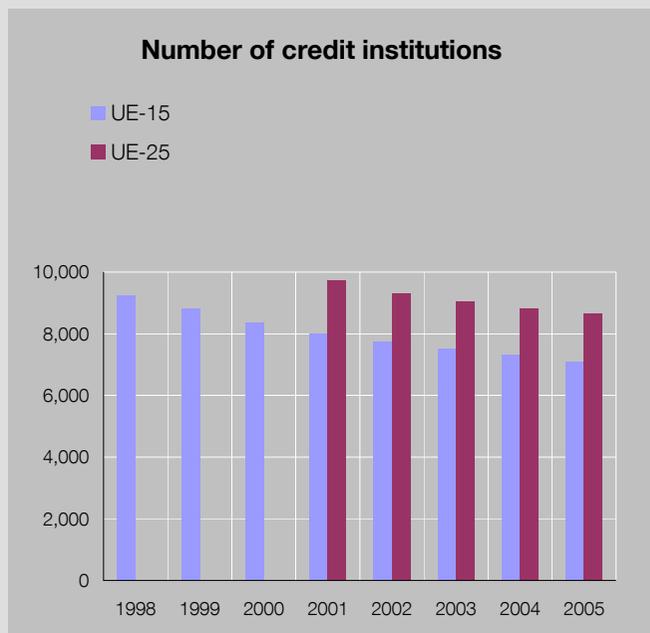


Source: EU Banking Structures, ECB

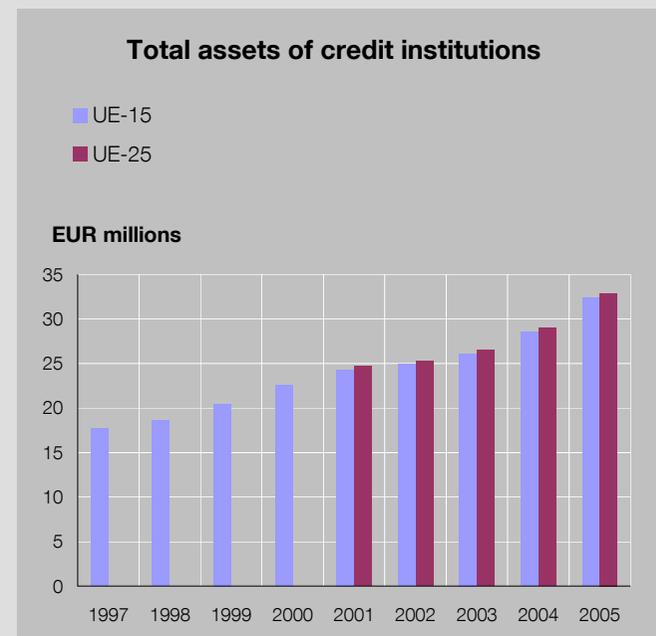
## The EU banking sector \_ general trends (2)



- The number of credit institutions has been decreasing over the years, while banking assets have been increasing...
- ... indicating a trend towards market consolidation



Source: EU Banking Structures, ECB



## The EU banking sector \_ general trends (3)



- Market consolidation is also observed when looking at the buoyancy of the activity of mergers and acquisitions
  - At first, more intense at the national level and in recent years with an increasing relevance of consolidation processes at EU level
- This process of market consolidation is related with an attempt made by credit institutions to diversify their risks and sources of business, and to achieve efficiency gains, among others.

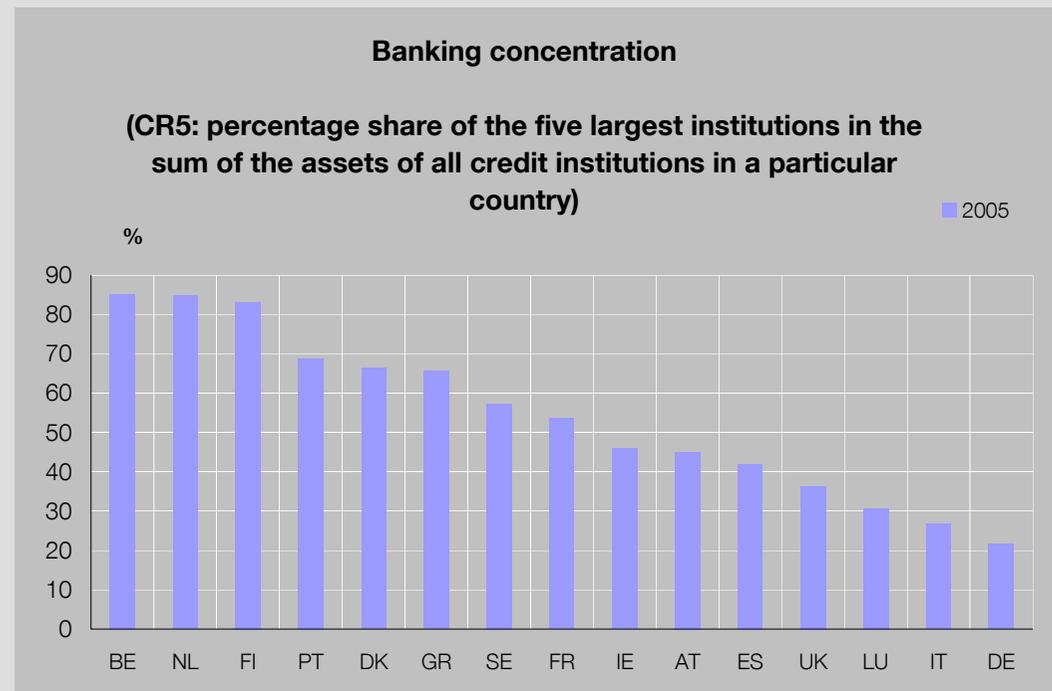


Source: EU Banking Structures, ECB

## The EU banking sector \_ diversity (1)



- Despite these general trends, there is a high level of diversity in structure of the different EU banking systems
- For instance, the dispersion among countries in terms of the degree of market concentration is high ...

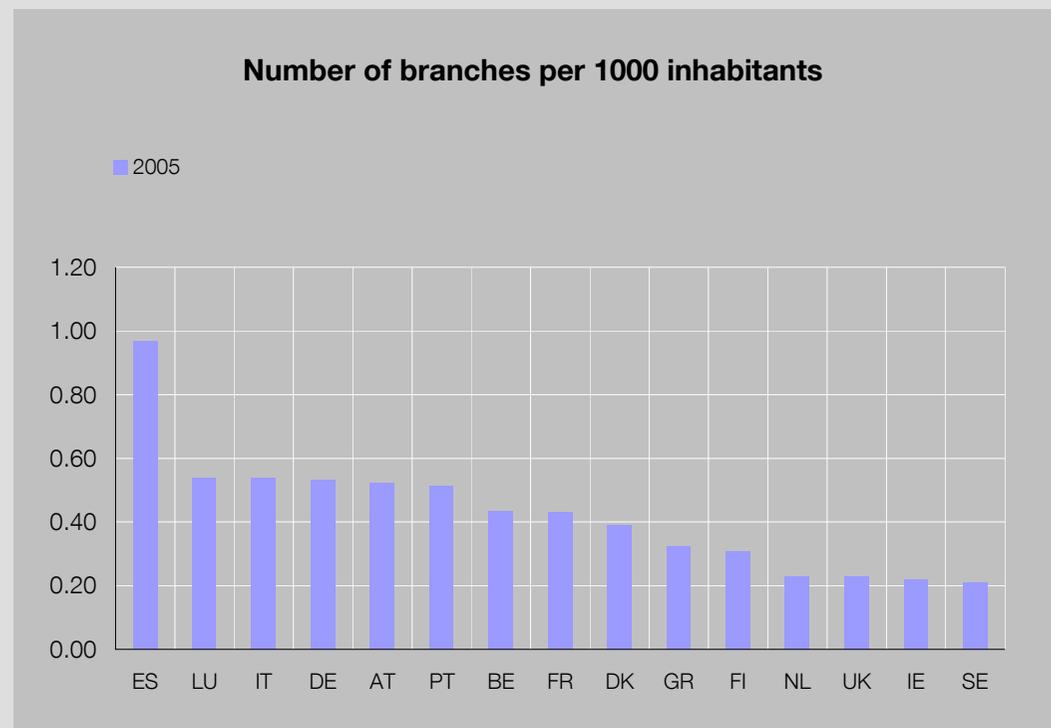


Source: EU Banking Structures, ECB

## The EU banking sector \_ diversity (2)



- ... as it is in relation to the number of branches



Source: EU Banking Structures, ECB

## The EU banking sector \_ diversity (3)

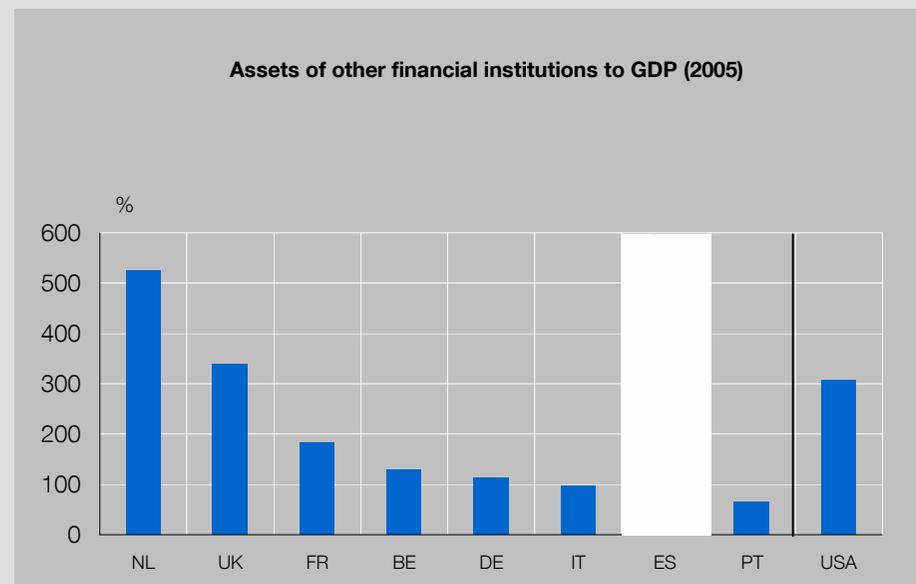


- Diversity among different banking systems is, to some extent, related with distinct manners of doing banking.
- For instance, in some countries, relationship banking is more intense than in others, where transactional banking and direct funding available in the financial markets are more prominent
  - Relationship banking tries to obtain clients-specific quantitative and qualitative information, and generally it exploits this information in a context of multiple transactions with customers
  - Transaction-oriented banking, by contrast, focuses on a single transaction with the client, or multiple transactions with a set of clients, typically using hard, quantitative data
  - Relationship banking implies, among others, proximity and long term relationships with clients

## The EU banking sector \_ diversity (4)



- These differences in the way of doing banking, and in more general terms finance, are observed, for instance, when looking at the relative importance of financial companies different from banks in terms of GDP



Source: FMI, Financial Soundness Indicators

## The EU banking sector \_ diversity (5)



- Differences are not only observed at national level but also among banks

–in most countries, there are local banks operating together with global companies

–12 out of 25 largest banks in terms of market capitalization are from the EU

25 largest world banks by market capitalization

		market capitalization
1	CITIGROUP	266,370
2	BANK OF AMERICA	241,823
<b>3</b>	<b>HSBC HOLDINGS</b>	<b>208,355</b>
4	JP MORGAN CHASE	177,645
5	ICBC	167,316
6	CHINA CONSTRUCTION BANK	140,412
7	mitsubishi UFJ FINANCIAL GROUP	135,124
8	UBS	131,508
<b>9</b>	<b>ROYAL BANK OF SCOTLAND</b>	<b>129,065</b>
10	WELLS FARGO & CO	121,568
<b>11</b>	<b>SANTANDER CENTRAL HISPANO</b>	<b>119,843</b>
<b>12</b>	<b>BNP PARIBAS</b>	<b>102,354</b>
<b>13</b>	<b>BARCLAYS BANK</b>	<b>99,973</b>
<b>14</b>	<b>UNICREDIT</b>	<b>99,382</b>
<b>15</b>	<b>BANCO BILBAO VIZCAYA ARGENTARIA</b>	<b>93,223</b>
16	WACHOVIA	91,535
17	CREDIT SUISSE	90,240
18	MIZUHO FINANCIAL GROUP	85,962
<b>19</b>	<b>HBOS</b>	<b>84,549</b>
<b>20</b>	<b>SOCIÉTÉ GENERALE</b>	<b>81,797</b>
21	SUMITOMO MITSUI FINANCIAL GROUP	75,741
<b>22</b>	<b>DEUTSCHE BANK</b>	<b>73,216</b>
<b>23</b>	<b>CREDIT AGRICOLE GROUP</b>	<b>69,810</b>
<b>24</b>	<b>LLOYDS TSB</b>	<b>66,823</b>
24	US BANCORP	62,334
25	ROYAL BANK OF CANADA	59,567

Source: Datastream , 15/02/07, m. \$

## The EU perspective \_ integration



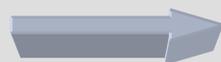
- Effective market integration in the EU financial markets has been one of the main objectives of European policy makers
- The reason is related with the expected benefits incorporated by financial integration:

### – Monetary policy

- *In a well-integrated market it is easier to transmit the monetary policy in a smooth manner*

### – Enhance the efficiency of financial markets

- *Improves the channelling of funds to its most productive uses*
- *Improves the available possibilities for risk diversification and risk-sharing*
- *Promotes deeper and more liquid markets*
- *Enhances competition and innovation, reducing intermediation costs*



**ECONOMIC GROWTH**

## The EU perspective \_ FSAP (1)

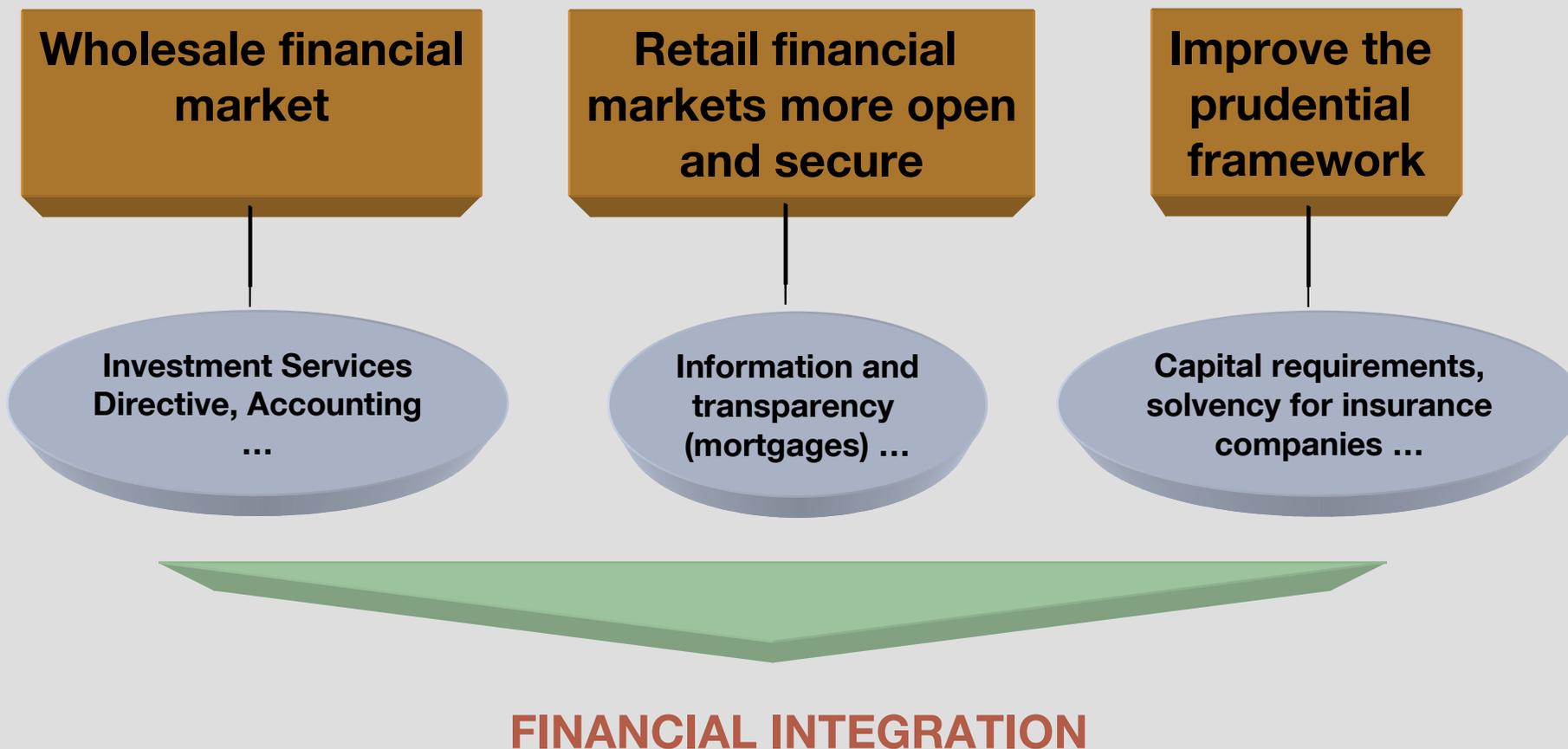


- The Euro has been an important step forward towards the direction of financial integration ...
- ... but not enough ...
- ... in 1999 the Financial Services Action Plan (FSAP) came into force with the final goal of acquiring the integration of financial markets in Europe.
- The FSAP incorporates a huge number of initiatives (42) and Directives (23 in five years)
  - Most of them have already been implemented (or will be implemented in the near future, as for instance MiFID or the Capital Requirements Directive)

## The EU perspective \_ FSAP (2)



- To attain its general goal of financial integration, the FSAP covers three main objectives:



## The EU perspective \_ Lamfalussy



- Legislative measures were important in terms of promoting financial integration, but there was also a need of more efficient regulation
  - Directives were too complex and detailed
  - The regulation process was too rigid and there were long lags in the implementation
- The Lamfalussy approach tries to reduce these complexities
  - Level 1
    - *Basic regulation, high level principles*
  - Level 2
    - *Proposal, definition and decision on technical elements that need legislative force*
  - Level 3
    - *Transposition and execution – committees of supervisors*
  - Level 4
    - *Enforcement*

## The EU perspective \_ cooperation



- As a result of the FSAP and the Lamfalussy approach, today's framework is more flexible and rapid in terms of its response to changes in the financial markets
- At the same time, cooperation among supervisors has been enhanced in last years, and we should keep on working in that line:
  - It is not a simple endeavour
    - *25 different countries need to reach a consensus on very technical and complex issues*
  - But there is no need to convince supervisors that cooperation is necessary:
    - *Harmonised prudential rules are necessary but no sufficient: more effective and consistent supervision promotes a sounder financial system*
    - *Greater commonality of supervision helps banks located in several countries*
- In this process of increasing cooperation, CEBS as well as initiatives like the CRD are playing an important role

## The EU perspective \_ CEBS



- CEBS is playing a key role in this process
  - Level 3 committee, which formally commenced its duties on 1 January 2004
  - It is comprised of high level representatives from the banking supervisory authorities (voting members) and central banks of the European Union, including the ECB
- What are its tasks?
  - To advise the Commission on banking policy issues, in particular for the preparation of draft measures for the implementation of the EU legislation*
  - To contribute to the consistent implementation and application of Community Directives: guidelines, recommendations and standards*
  - To enhance supervisory co-operation, including the exchange of information*

## The EU perspective \_ CRD



- The Capital Requirement Directive provides a very powerful framework to foster consistent implementation:

- **Additional tasks for the consolidating supervisor, for instance**

- *Coordination responsibilities for the gathering and dissemination of relevant information*
- *Planning the supervisory activities*
- *Responsibilities in relation to the validation of group wide approaches for the advanced measurement of credit and operational risks*

- ... while ensuring the involvement and proper access to information to all the supervisors involved in the process

- **Supervisory disclosure**

- *National authorities will have to publish information about how they implement CRD*

## The EU perspective ... and the global dimension



- In the process of regulating the European financial markets and institutions it is relevant to keep in mind that regulation should be balanced
  - Efficiency of supervision and best regulation are key
  - Excessive regulation can impose unnecessary costs, hamper innovation and deteriorate the competitiveness of markets and institutions
- In connection to that, and as I have already said, main EU banking groups are global players
  - Centralisation of key business functions at group level, international ramification of their activities etc.
  - There is a need to enhance supervisory cooperation also at international level

## Retail banking markets (1)

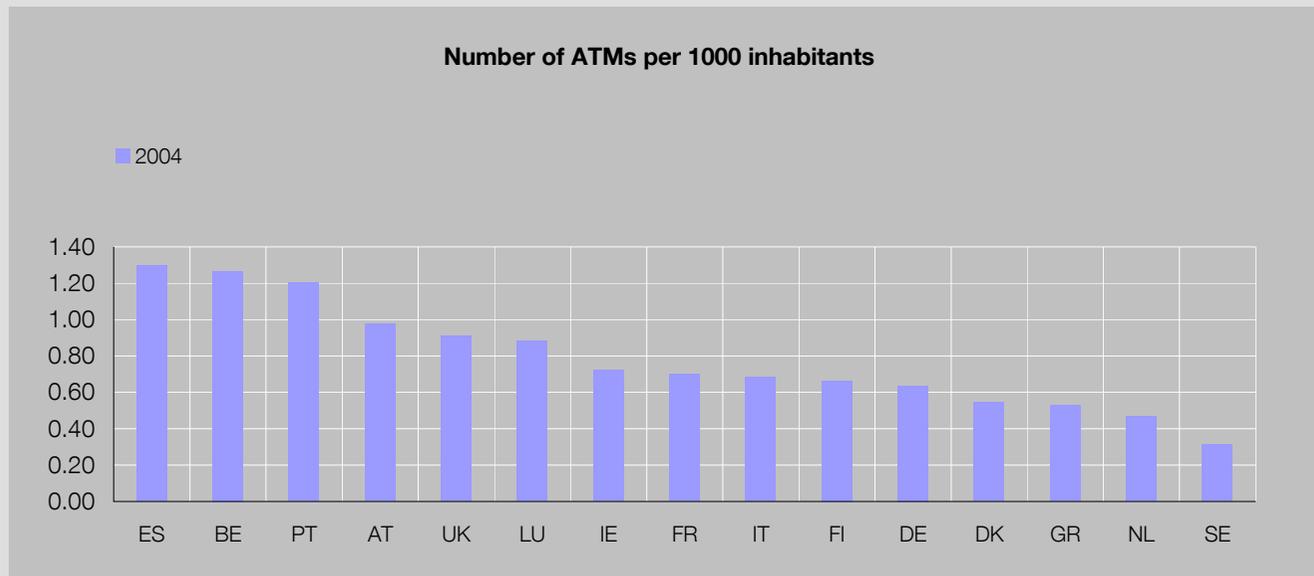


- Other relevant elements to take into account when designing the regulatory and supervisory framework of the EU are the specificities of the retail banking sector
  
- In retail banking, lack of integration does not necessarily imply the existence of barriers or lack of competitiveness
  - It is reasonable to expect that market shares in retail markets will show a significant degree of persistence
    - *National banks keeping a significant part of the retail business*
  
  - Retail banking is based in detailed and long term knowledge of the clients
    - *Households can also find beneficial a high density of ATMs and/or branch networks*

## Retail banking markets (2)



- For instance, the number of ATMs per 1000 inhabitants varies greatly from country to country, showing that in some markets consumers find a high density of ATMs beneficial



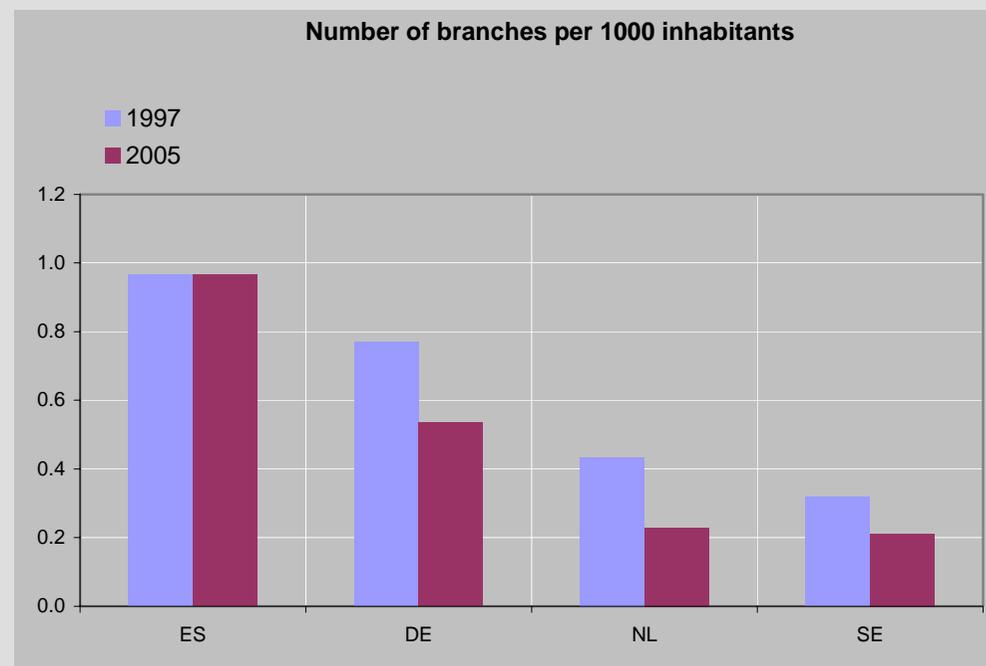
Source: EU Banking Structures, ECB

## Retail banking markets (3)



- Another example that shows that clients' preferences are different depending on the country is the density of branches and its evolution over time

–In some countries it was high and remained high, while in other it was high (but lower) and it has been showing a decreasing trend over time



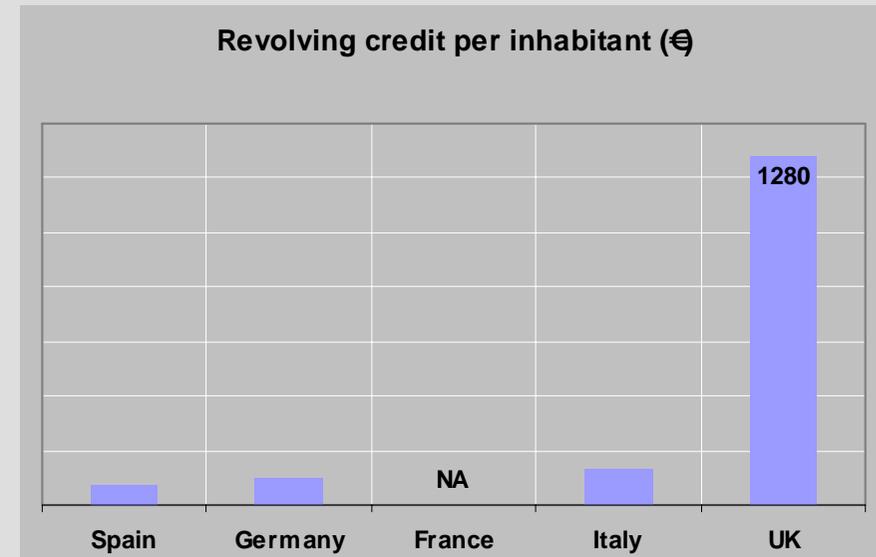
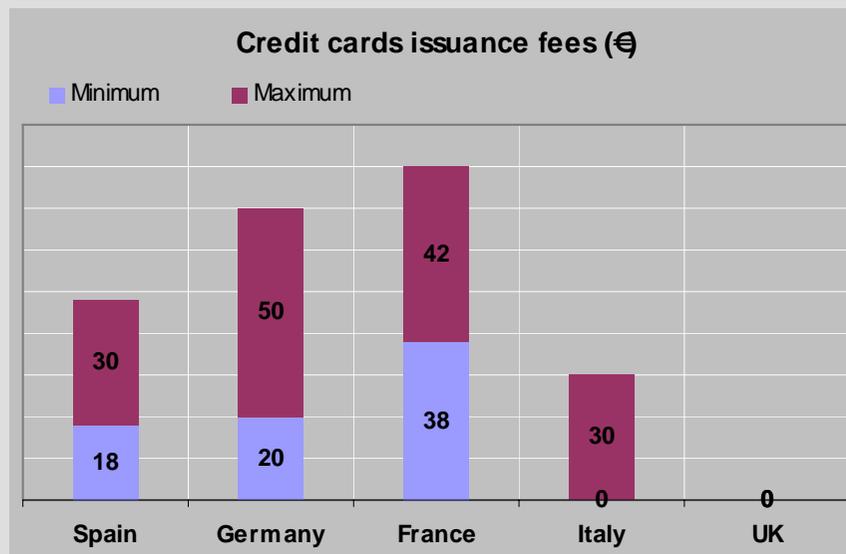
Source: European Banking Structures, ECB

## Retail banking markets (4)



- When analyzing the level of competitiveness and other characteristics among countries ...

- ... structural differences and the particular characteristics of the business must be taken into account



## Conclusions



- The political aim of increasing market integration and the goal of extending the benefits of a single financial market to consumers is commendable

–But be aware that reality is complex

- In that sense, and given the high degree of national specificities in retail markets, it is necessary to give time for measures to be effective

–We should be patient, and be careful not to over-regulate financial markets

- There are some target areas of action in the short-run

–Increase the level of transparency as well as the degree of competition in order to offer consumers better and more adequate products and services

•*Cross-border mergers and acquisitions are relevant*

–And at the same time, enhance consumer education to promote informed and responsible decisions taken by clients



**Thank you for your attention**