Resolution on the contribution of the financial sector to an economic upturn

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Approved by the Central Council on December 6th 2013

1. The Social & Economic Commission and the Monetary Commission of the European League, gathered in Brussels on December 5th, 2013, and debated on the topic « How to reinforce the contribution of the restored financial sector to the economic upturn in Europe ? », with key personalities : Mr. Miguel DE LA MANO, European Commission, General Director Internal Market ; Professor Jean- Paul Betbèze, former Chief Economist of Crédit Agricole, Economic advisor to Deloitte ; Mr. Bernard HADDAD, President of the Financing Commission of CGPME, Mrs. Jeanne-Marie PROST, French Credit Mediator to Enterprises, and Mr. Robert PRIESTER, Deputy General Director of the European Banking Federation. After intensive debates, they came to the following conclusions :

    a) The crisis of confidence that periodically hindered the proper functioning of the interbank market is now over. Transactions are flowing again and counterparties are diversified. Nevertheless, the unconventional practices of the European Central Bank – ECB (Eurosystem) (in particular, the widening of the criteria for collaterals, the unlimited supply of fixed rate liquidity and Outright Monetary Transactions (OMT) as well as the Long Term Refinancing Operations (LTRO)) have played a great role in tempering tensions. Underlying lack of trust between operators justify nevertheless maintaining these tools fully operational.

    b) Bank recapitalization efforts have been tremendous since the beginning of the crisis: prudential ratios (tightened in the context of Basel 3) have improved across the continent by several points; 2019 minimum targets are already outreached by many credit institutions. Nevertheless, these improvements need to be put into perspective with the evaluation of bank assets, the quality of which is under review by ECB. Besides, these have been achieved not only to the disadvantage of shareholders through a reduction in dividend distribution (implying a lesser profitability with a fall in ROE) but also to the disadvantage of borrowers through more limited access to credit and tightened credit conditions. Even though we cannot talk about a « credit crunch » the restriction on bank financing which is an essential source of financing for SMEs is dangerous. Moreover, envisaged liquidity ratios will strongly limit the capacities of transforming short term savings into long term loans.

    c) In addition, the issue of systemic risk (even though partially covered) cannot be only tackled through prudential ratios and continues to be worrisome, all the more that fearing this risk has led member states to get exposed to the banking sector up to the level of 4 trillion euro (2 trillion in the form of guarantees) in the preceding phase. Finally, the progress to be made in the field of banking separation between retail and risky activities, as proposed under the « LIKAANEN report » is still heavily debated.

    d) Views regarding the supply of bank credit to non-financial companies remain very divided: credit institutions in general believe that access to finance is not unduly restricted and that any good project can be financed; the indisputable slowdown, the decline in the volume of outstanding credit (-1.7 % over the past year for the entire euro zone) apparently rather result from the economic crisis and a spontaneous freeze of investment projects. Companies on the contrary, especially the smaller ones, complain of a strong hardening of the conditions for granting a credit and for collateral requirements, including higher rates; it seems particularly the case with regard to cash loans and to the financing of working capital . It is difficult to disentangle these views, it seems reality varies greatly from one country to the other and from one sector to another – e.g. the restriction of credit to businesses is very strong in Southern Europe and Central Europe.

e) The new European standards - primarily prudential, are designed to prevent the recurrence of mistakes and excessive risk-taking that triggered the crisis in 2007/2009. However, it seems undeniable that they exert a restraining effect on the financing of the economy including businesses; loans to States, despite the recent crisis "sovereign debt" remain favored - implying a serious risk of crowding out effect of credit to the private sector in some countries. This is much sharper in the field of equity financing, the "Basel 3" standards for banks and moreover "Solvency 2" for insurance heavily weighting the risks associated with such operations. Whereas the ability to rebound and the competitiveness of the European Union depend largely on the availability of such funds to encourage "start- ups " , innovation and business growth .

f) However, progress towards a unified ECB supervision of large banks and towards harmonization of guarantees to depositors represents an undeniable breakthrough, even if it is not yet finalized to date. Similarly, the possibility for the European Solidarity Mechanism (ESM) to recapitalize (although ultimately) troubled banks is positive, reassuring markets and therefore likely to promote economic recovery.

g) Finally, the bank disintermediation, mainly in the form of direct issuance of securities to markets, as well as increased securitization of loans, direct loans between economic actors or "shadow banking" provide interesting new opportunities to supplement the supply of credit that would be too small, especially when rapid restart of European economies. However, these forms of financing, lightly regulated or unregulated, also pose real dangers, including distortions of competition, formation of "bubbles" and / or fraudulent transactions.

2. Wishing to contribute to appeals to help Europe escape stagnation and re-enter the path of a strong, sound and lasting growth – the only way for us to curb unemployment - our Commissions adopted the following recommendations :

a) The ECB (Eurosystem)'s role in reinstating open and efficient money markets remains crucial. We underscore the necessity of keeping open an unrestricted access to short-term Central bank financing and the opportunity to use OMT[1] and LTRO[2] whenever an excessive tension looms. Moreover, the question of asserting excess liquidity deposits of banks in the ECB's books with a negative interest rate should be seriously considered (howbeit at a low level, it would be an important signpost): additional liquidity granted by the ECB is actually meant to comfort markets and to facilitate

[1] OMT : Outright monetary transactions, meaning that unlimited amounts of liquidity at pre-set fixed rates are offered to banks by the Eurosystem in case of unwarranted tension on the money market.
[2] LTRO : Long Term Refinancing Operation, that the Central bank buys securities with a maturity up to three years on the market (Open market intervention).

financing of the economy, whereas their sterilization through idle deposits within the Central bank contradicts this policy.

b) Beyond the new « Basel 3 » prudential regulation, the question of controlling systemic risks should be closely scrutinized, so as to establish precautionary measures going further than the mere presence of additional« security cushions » in equity. More specifically, the ECB should be able to play its role as an early warning system and to enforce in due time any corrective measures deemed necessary.

c) The protection of bank depositors (and of public authorities, who feel compelled to rescue them, thus worsening their indebtedness) calls for a course of action much stronger than what is being presently done, so as to shield retail banking activities from speculative risk. Topically, allowing retail banks to continue to act as investment banks with no set limits seems to lead to depositors running into excessive risk.

d) The new banking and insurance sector regulations, « Basel 3 » and « Solvency 2 » should be at least partly revamped before being applied, aiming at : on the one hand, reducing the over-weighting of corporate and equity risks (in particular for SMEs) ; on the other hand, taking into account the reality of « sovereign risks » (lending to public authorities). Still more importantly, the liquidity ratios that are being considered should be conceived so as not to impair or constrain excessively the much needed « transformation » of short-term funds into medium-term financing of business.

e) Quick and concrete progress must be made in the way of putting together resources allowing to secure the guaranty given to depositors in bank accounts with an amount currently up to 100.000 euros. These resources can be mustered by earmarking, as of now, a flow of resources drawn from current retail banking revenue; these funds would accrue a Fund set at the European level. We underscore that risk mutualization at E.U. level would ascertain a much more effective guarantee of deposits, at a lesser cost – with the requisite of avoiding moral hazard. It is also most necessary to succeed in setting up a system to resolve bank failures, which should give our common institutions enough authority and means to act in due time.

f) Finally, credit disintermediation, in all its aforesaid modalities, should be encouraged, as it brings additional possibilities to finance the economy's needs. However, it also presents a high level of instability and entails strong risks of going astray ; it seems necessary, as of now, to frame and to regulate these activities, by submitting them to a corpus of rules and to supervisory authorities - while avoiding to stifle them, the aim is to allow a sound development of their contribution to growth..

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