BETTER FINANCE FOR ALL

The European Federation of Financial Services Users
Fédération Européenne des Usagers des Services Financiers

EPFSF event 29 January 2013
Reform of EU Banking Structures

EuroFinUse Managing Director speech

1. A real separation of commercial banking from market and investment banking

EFU MD first reiterated EFU's main position, which is to operate a real separation of trading and investment activities from commercial banking activities via a Glass-Steagall like regulation: a split, not a "ring-fencing".

He recalled the audience of MEPs and industry representatives that Bill Clinton considers that repealing the Glass-Steagall Act in 1999 was one of the two major mistakes of his presidency:

> *"I made some mistakes too..: aggressively enforcing the Community Reinvestment Act and signing the bill repealing the Glass-Steagall Act, the Depression-era law requiring commercial and investment banking to be done by separate institutions"* (Bill Clinton, Back to Work, 2011).

2. The separation is needed not only for reasons of financial stability

House of Lords / House of Commons

Parliamentary Commission on Banking Standards:

"Investigations into LIBOR have exposed a culture of culpable greed far removed from the interests of bank customers, corroding trust in the whole financial sector. The separation of deposit-taking from certain investment banking activities can offer benefits not just for financial stability, but also in helping to address the damage done to standards and culture in banking. The Government has proposed a ring-fence to achieve separation, but any ring-fence risks being tested and eroded over time" (19 December 2012).

This is one reason why now, US employee shareholders and unions of large US banks are asking JP Morgan, BoA and Citigroup to split their investment banking activities[1].

Also, EFU already pointed out other major reasons for a split:

[1] http://www.reuters.com/article/2013/01/24/us-jpmorgan-aflcio-idUSBRE90N0ZY20130124

- Central bank funds were meant to refinance commercial banking only, i.e. the transformation of deposits into loans to the real economy, nothing else. This public support was never meant to fund other activities such as investment banking and trading.

- Also, one obvious solution to the "too big to fail" issue also known as "SIFIs" is for these groups to become smaller: evidence produced by EFU and others shows that a split would dramatically reduce the balance sheets of the biggest European banks. Recent systemic risk evaluation by HEC Lausanne (Le Temps, 14/01/13) shows that out of the world's ten most risky banks: seven are big European commercial banks

- Finally, only a split can eliminate the conflicts of interest between commercial banking and investment banking.

3. The financial crisis does not only come from "deposit taking" banks and property lending

Contrary to the premise of the EPFSF's first question, the financial crisis also comes from banks' capital market activities (Dexia, JP Morgan London last year and most recently Monte Paschi di Siena in Italy), and the extended securitization of US mortgage loans, which is not a commercial banking activity but a capital market one.

4. Interestingly the Liikanen Group took on EFU's proposal to limit property lending "bubbles"

This Liikanen proposal seems to have been largely overlooked.

<u>EFU proposal to the Liikanen Group</u> (May 2012): "*Controlling the effects of greed on mortgage credit, national supervisors should limit the amount of mortgage loans as a percentage of the collateral fair value and limit the interest charge as a percentage of borrowers' income, and review or audit the enforcement of those limits every year*."

<u>Liikanen proposal</u>: "*As a direct measure to limit the risks stemming from real estate markets, the ESRB recommends that loan-to-value (LTV) and/or loan-to-income (LTI) caps are included in the macro-prudential toolbox. The Group fully supports this recommendation and further recommends that strict caps to the value of these ratios should be provided in all Member States and implemented by national supervisors*".

It means commercial banks are no longer trusted to manage their core business: property credit risk management.