Should financial sovereignty be a key objective for the EU?

Harald Waiglein

Director General for Economic Policy, Financial Markets and Customs Duties, Federal Ministry of Finance, Austria

Integration is the key for achieving a higher degree of sovereignty

Sovereignty in a strictly legal sense means the power and authority to rule. In an economic sense, sovereignty may be more adequately described as the ability to control outcomes and respond to fundamental challenges. In today's globalised economy, domestic policy autonomy may be more constrained compared to earlier decades, but at the same time, the ability to trade, work and invest internationally has increased economic opportunities for all. Sovereignty arises from working together rather than policy independence.

In the financial sphere, sovereignty is necessarily incomplete due to spill-overs from other jurisdictions. As regards exchange rates, there are even political commitments not to target them for domestic purposes. The free flow of capital is among the basic principles of EU integration and the global market, and no other sector is more integrated worldwide than finance. Thus, the quest for more sovereignty in the financial sphere has to strike a balance between maintaining open markets and protecting legitimate interests. Rather than making an increase in financial sovereignty an explicit political objective, policy makers should work towards improving the conditions for economic and financial stability and strength to maximise global influence.

The EU and the euro area have progressed on many fronts since the 2009 crisis. The Banking Union has supported financial stability through harmonising supervisory standards and cutting feedback loops between banks and their sovereigns. The ESM was established as a lender of last resort to distressed euro area Member States. The ECB has expanded its toolbox to address the fragmentation of financial markets and support the transmission of monetary policy. Economic and financial surveillance was strengthened with a view to detecting and addressing risks early on.

Still, there remains untapped potential for the EU to further develop its financial and capital market, and thus to strengthen financial sovereignty. Euro area exporters would benefit from an extension of Euro-based payment infrastructure outside the euro area, which would bolster the euro's role in global payments and exchange market transactions. Further developing equity and venture capital markets would help mobilise private capital for investment and release pressure from banks to provide financing to the real economy.

Yet there are limits to the EU's financial sovereignty, due to the EU being a union of nation states rather than a single nation. Financial interests cannot be traded against geopolitical interests, as practiced by other global powers. There is not a single EU President other nations could talk to, but there are several EU Presidents + 27 Heads of State or Government. This certainly complicates decision making and international economic relations and influence. Therefore, the EU's influence in the international arena should not be measured by comparison to other global powers, but by comparison to the influence EU Member States would be able to exercise individually. Against this measure, the achievements of the EU over the past decades are unprecedented. Internal integration, ultimately also including political integration, rather than restraining market forces, is the key for reaching a higher degree of sovereignty. ●

Sylvie Goulard

Second Deputy Governor, Banque de France

Finance, sovereignty and a pangolin

Sovereignty is a concept that refers to states. It usually designates an exclusive power on a territory and a population, limited only by its own international commitments. The European Union (EU) has a genuine character, it is not a state. From an institutional point of view, the EU combines elements of a federal state such as a federal Central Bank and a common legal order under control of the Court of Justice, and elements of international cooperation, such as unanimity of member states.

In the financial field, the EU has nevertheless already achieved a lot. The creation of the "banking union" in 2012, with a single rule book and a common supervisor, was a major step forward, even if it is still a work in progress. Large cross border investments are now needed to finance greener infrastructure, digitalization and costs linked to ageing. In times of crisis, it is also critical not to be dependent from banks located outside the common legal framework. Banks have played a crucial role throughout Europe by channelling state guaranteed loans to business and industry. The joint supervisor ▶

(SSM) and the European Systemic Risk board (ESRB) have contributed to a more coordinated response in terms of pay backs and dividends. Persistent fragmentation partly explains the lack of cross border mergers. It is also damaging for the economy, as pan European banks would be a powerful catalyst for growth and development, scale effects boosting intermediation, specialization and productivity. Profitability of European banks remains lower than those in the U.S. The European Commission intends to facilitate further the integration of capital markets. This initiative could help to better mobilize European savings for investments. Hundreds of billions of Euros could be made available for European projects, with positive side effects such as increasing private risk sharing and facilitating the transmission of monetary policy.

> *Europeans share an incredible savoir-faire in transnational governance, at a time where it is needed more than ever.*

The decision taken by the last European Council to create a recovery fund constitutes a quantum leap. The cross-border recovery fund renews the promise of stability already enshrined in the treaties, which means a lot for investors: the EU, the euro are here to stay and the Union is indeed becoming "ever closer", providing grants and loans. Until now, the EU had a single currency but no treasury, no significant common budget, very few bonds issued in common. Though exceptional, the recovery fund linked to the EU budget, partly financed by jointly issued debt, as well as the creation of EU own resources, confirm that the euro is irreversible. It does not only provide help for countries severely hit by the COVID-19, it provides insurance for a common future. The evolution of spreads even before the money is distributed, shows that the message was well received by markets. Disputes between the "frugal" and the "southern countries" are minor in comparison with the political shift this decision represents. It is perfectly normal that the countries with strong ratings ask for conditionality. It is also legitimate that, in an Union based on cooperation, wounded peoples receive help from the partners.

The cumbersome decision-making process of the EU could certainly be improved. However, it would be a mistake to continue to oppose an uncompleted EU with fully fledge sovereign states. Europeans share an incredible savoir-faire in transnational governance, at a time where it is needed more than ever. In 2020, few states, if any, are entirely sovereign. Interdependence is the new reality. When markets are interconnected, financial crises ignore borders. Global value chains, as well as global phenomena like climate change or pandemics put the state-based world order into a new perspective. Everywhere national rhetoric insists on taking back or keeping control. Let's be pragmatic and remember that a pangolin may suffice to block the world economy.

Stéphane Boujnah

Chief Executive Officer and Chairman of the Managing Board, Euronext

Europe must be a continent of finance makers, not finance takers

Europe must be a continent of finance makers, not finance takers. This should translate into policies that encourage European solutions, recognising the immense challenges facing the Union. The current crisis raises the prospect of greater nationalistic tendencies, particularly as its socio-economic impact is increasingly felt. July's agreement of a European Recovery Package by EU leaders was therefore a major step in providing support to the recovery and resilience of Member States' economies.

A reformed CMU will be a critical factor. Covid-19 has underlined how important public capital markets, equity investment, and accordingly an effective CMU, will be for the recovery of the EU's economies. But this will need to be a fundamentally different CMU.

As anticipated for months, it will have to factor in the consequences of Brexit. But it will also have to adapt to the lasting impacts on markets of the recent massive central bank interventions and fiscal stimulus measures, as well as to the very real risks of fragmentation of European capital markets. In order to mitigate these risks CMU should be built on a European competitiveness ambition.

If Europe wants to provide citizens, businesses and society at large with the tools to turn current challenges into opportunities, it needs a vibrant single market for financial services. In this respect, Europe must be a continent of strong and competitive finance makers, not an open territory of finance takers. For many global players in the finance industry, the European Union is often part of a "Europe, Middle-East and Africa" division. For Euronext, as for many European financial institutions and market infrastructures, the European

Union is home. And the European Union cannot build a strong united capital market without strong European financial institutions and market infrastructures. This is not to suggest the promotion of a protectionist approach, as innovation and competition are key to building any strong industry. But we must stop the unilateral disarmament of the European financial system. This is how we should understand European financial sovereignty. There are three core building blocks for this ambition.

First, every measure contemplated in designing the new CMU should be assessed by a systematic "competitiveness test", which would be more specific than the usual Commission overall impact assessments. This test should be used to analyse, before new rules are introduced, whether they will make the EU's capital markets, financial institutions and infrastructures, stronger or weaker on a global level. If we want to unite European capital markets, we need capital markets in Europe to be united. What the EU must avoid is causing unwanted damaging consequences for Europe which would be experienced a few years down the road, when it is often too late to recover lost competitive positions.

The financial sovereignty of the EU is key to overcoming the challenges ahead.

Second, countries representing 85% of the EU GDP use the Euro currency. The new CMU will have to create the conditions to establish the Euro as a strong reference asset currency, in particular through a revitalized securitization market of Euro denominated assets, and measures to establish sovereign green bonds as a flagship product for the EU's capital markets. The EU's competitiveness and financial sovereignty requires accelerated progress in the use of Euro. This is simply because there is no lasting strong financial centre without a strong international currency.

Third, years ago, the EU decided to shape the telecom industry with the GSM standard, and the aerospace industry with Airbus. The EU is today a legitimate player to build an ambitious Digital Finance Action Plan.

In the global competition where non-European digital players build dominant positions, the new CMU must foster the emergence of global players in the fields of cyber security, pan-European digital payments, innovative digital markets, cloud data management and artificial intelligence.

The financial sovereignty of the EU is key to overcoming the challenges ahead. If the EU were to live up to its ambition to bolster Europe's competitiveness through a stronger CMU, it could pave the way for a real single market for financial services, enabling the emergence of European global players and strengthening both the role of the Euro and the resilience and sovereignty of Europe in the future.

Jacques Beyssade

Secretary General, Groupe BPCE

Financial sovereignty - a pre-condition for real EU decision-making

Geopolitics and economics are closely intertwined. The current health and economic crisis proves yet again that our world is uncertain, disruptive and often divided. For European citizens and corporates, the EU is a safeguard and a stabilizing force. For this to remain so, Europe has to ensure its financial sovereignty. What does that mean for financial services?

First, EU companies need diversified and competitive sources of financing. Reliable financing is a condition for long–term and sustainable growth – to a large part it needs to be available within the EU if we do not want to become the dominion of a larger Empire. During the earlier days of the current pandemic, third-country banks have pulled back from lending to European companies. Conversely, European banks, including BPCE, have mobilized forces for the interests of their European clients.

Second, our sector needs fair regulation and a level playing field adapted to EU economic specificities. A competitive financial sector rewards efficient business models, fosters growth and is distinguished by strong actors. This implies applying the principle of "same activities, same rules", to non-banks undertaking bank-like activities.

The original Basel Accord of 1988 sought to harmonise capital regulation across jurisdictions, i.e. to create a level playing field. However, the Basel rules are turning into a one-size-fits-all approach, and there is increasing concern on whether they are still compatible with the realities of financing the EU economy.

We need a regulatory level playing field and practicality of rules in their daily application.

Looking forward, the clear goal of the Banking Union and the Capital Markets Union has to be a better future for everyone. The EU has the largest pool of savings in the world, this potential should not be wasted by failing to efficiently allocate these savings, invest in Europe and therefore finance European growth.

For the Banking Union, concrete ambitious and pragmatic decisions are needed to ensure a suitable transposition of the Basel agreement, notably: a) to boost specialized lending - crucial because of its link to sustainable finance,

b) to support unrated corporates – crucial providers of activity and jobs in Europe, and c) to avoid increasing fragmentation and address the output floor issue. IFRS and especially IFRS 17 should be geared toward a more long-term and sustainable design.

Third, we live in an increasingly technological world. Yet there are no EU companies amongst the large digital corporations. This has implications for our sector, as banks have become trusted Fintechs, technological actors and third parties, where they ensure the security of their customers' funds and data. If EU regulation succeeds in remaining neutral vis-à-vis technology, the principle of "same activity, same rules" can help avoid hurdles to digitalising the EU financial sector. More specifically, the EU is rightly stepping up on critical infrastructure, cybersecurity, and cloud services.

We especially welcome that the EU is launching an own Digital Strategy and private initiatives such as the European Payment Initiative. GDPR is another cornerstone of the European digital transition. The recent judgement of the ECJ on the EU-US privacy shield further underpins the moral and economic imperative to ensure an autonomy in digital matters.

Fourth, Europe is a leader in developing a sustainable economy and in channelling private investment to climate neutral activities as promoted by the European Green Deal. For this to succeed the EU needs to remain autonomous in its decision-making, i.e. a sovereign in its financing and definitions of standards.

EU banks like ours have shown that EU clients can count on their banks, asset managers and insurers to be key partners in adverse times that are marked by both the challenges of a pandemic and the necessary ambition of sustainable transition. For us the way forward is to grow as trusted partners alongside the European real economy. For this to be realistic, EU decision-makers need to ensure a level playing field in terms of regulation and the practicality of rules in their daily application.

Christian Edelmann

Co-Head EMEA Financial Services, Oliver Wyman

Strengthening European financial sovereignty

Europe's banks are set to take a large financial hit from the COVID-19 crisis, both in terms of credit losses and in several years' worth of weaker earnings that are expected to follow. After a decade of strengthening balance sheets, however, the industry looks sufficiently robust to sustain the economic shock and expected credit losses. Banks have worked hard to maintain their operations and to support their customers during the lockdowns thus far, and they are partnering with governments to protect the economy. Some goodwill, in short supply for years, is now being replenished.

However, ultra-low interest rates and massive liquidity programs challenge the core role and business model of commercial banks. Liquidity transformation is simply of less value in a world where central banks provide a wash of liquidity and money is free.

Hence, a bold vision for Europe's financial system needs to be imagined: robust, providing great services for customers, built on modernized infrastructure, and governed in Europe's best interests in the vanguard of social challenges. However, on their own banks will not deliver the banking system Europe needs. This will take collective endeavour: from management and shareholders, but also employee groups, regulators, and policymakers. Individual bank transformation programs will not be successful without broad stakeholder support, and broader reforms are also necessary outside of individual institutions.

The remedies have been clear for some time: complete the banking union; create a true capital markets union; eliminate unnecessary obstacles to banking consolidation and tackle the fragmented and costly regulatory system. Adding on competing regulations for data protection or digital is only going to make things worse and should now receive much more coordination.

Furthermore, a mutual understanding should be built on the future of banking. Banks would fast-track transformation plans to drive greater efficiency and consolidation and set out an ambitious role in the social and environmental challenges of the next 20 to 30 years, even if this is not always directly aligned with shareholder value.

> *Banks on their own will not deliver the banking system Europe needs - this will take collective endeavor.*

Doing so will substantially increase Europe's financial sovereignty, by giving EU-based financial institutions and markets the ability to provide for Europe's needs. It will also reduce dependency on outside financial firms which can create some risk in times of crisis, as there is a home bias that can cause firms to pull back to their home bases, just as many European banks reduced their overseas operations during the global financial crisis. The analogy that comes to mind is supply chains and the issues the EU faced with medication and masks at the peak of the Covid outbreak. The answer – also for banking – lies not in national efforts but a European response.

Alban Schmutz

Senior Vice-President, Business Development & Public Affairs, OVH

GAIA-X : reinforcing sovereignty of financial institutions using cloud services

Sovereignty of our financial infrastructures are essential for Europe's success. Who controls IT infrastructure is a central question towards sovereignty, and the European financial industry needs to ensure that all its cloud suppliers endorse European values.

Therefore, the European financial institutions not only have to rely on the European regulatory framework (data protection, free flow of data, financial services regulations), but have to take a major stake in the vehicle that will bring the Cloud ecosystem at the next level: GAIA-X.

Gaia-X will ensure that European values will be at the heart of all cloud offerings across Europe in the interest of all European industries' data sovereignty. Avoiding vendor lock-in, transparency of suppliers regarding non European extra-territorial regulations, data protection, security... These questions are at the center of any IT policy. Therefore GaiaX developed a unique set of "Policy Rules" that maps all these principles in points of controls which values will be transparently attached to every single cloud service declared within GaiaX. This set of rules covers both a) infrastructure and b) software and data, in order to be adapted to the market needs.

All industries, including financial institutions, will be able to map automatically which services and which suppliers are able to comply with their internal compliance matrix, based on technical capabilities, quality of services and these very key policy rules. This means that for each workload, a different set of services and / or suppliers will be exposed by GaiaX with machine readable formats and help ensure scalability and reversibility of services.

All these policy rules are not specific to GaiaX and do not seek to reinvent the wheel, but take the best of bread of existing frameworks, already helping to comply with some of the European regulatory obligations. This includes for example the Cispe Data Protection code of conduct (Cispe.cloud) to ensure cloud infrastructure services meet GDPR requirements, the future Enisa European cyber security scheme (Cybersecurity Act), or the Swipo codes of conduct regarding data portability of non personal data (Free Flow of non personal data regulation).

This work has been performed based on the work done for years through already existing non profit organizations like the International Data Spaces Association (IDSA) and Cloud Infrastructure Services Providers in Europe (CISPE). A dedicated code of conduct or framework ad hoc for financial institutions could be envisaged to fully fulfill regulatory and supervisory requirements ensuring the highest standards of a European cloud and preserving a level playing field with other industries.

Presented by German and French Ministers of Economic Affairs Atmaier and Le Maire, GAIA-X gathers 22 founding members (with a balanced representation of providers and cloud users: BMW, EDF, Safran, Bosch, Siemens, Orange, Telekom, OVHcloud, Cispe...) and close to 300 organisations. The GaiaX foundation, a non profit organization based in Belgium, will start its operation in September 2020 as announced by the ministers and founding members the 4th of June.

A dedicated code of conduct or framework ad hoc for financial institutions could be envisaged to fully fulfill regulatory and supervisory requirements ensuring the highest standards of a European cloud.

Some financial institutions are already taking part in some of the GaiaX working streams. But more needs to be on board to ensure that further developments will perfectly fit to European financial institutions needs. GaiaX is also a very unique opportunity to support the evolution of some financial services business models becoming cloud providers on their own, and GaiaX and its framework could enable acceleration of the taking off of such services.

Joining the GaiaX foundation is a major opportunity for financial institutions to push forward their expectations and meet other stakeholders working already together to give Europe some data sovereignty back.