2019

Europe - U.S. Symposium on Building the Financial System of the 21\textsuperscript{st} Century
Threats to Cross-Border Banking: Resolution and Brexit

• Cross-border resolution – global dimensions
  – Ringfencing has become the global norm
    • Subsidiarization, internal TLAC
    • Is SPOE effectively dead?
  – Lack of legal clarity - definitions, functions, regulation of branches vs. subs
  – Coordination in case of actual resolution
    • Trust and ringfencing – “trust” and coordination are easier when the cash is in place (TLAC, MREL, etc)
  – Lingering questions:
    • Is fragmentation reasonable price to pay to protect taxpayers?
    • Fed’s toolbox to stop contagion limited by Dodd-Frank
    • Is banking more or less fragile in this new world?
Threats to Cross-Border Banking: Resolution and Brexit

• Cross-border resolution – Europe
  – Even within EU, cross-border resolution is challenging
  – Italy examples: bail-out rather than bail-in
  – Gaps persist among ESRB, EC, and national authorities
    • EU resolution directive superimposed on varied national bankruptcy laws
    • Actual bank failures follow political, not just legal, logic
  – SRF still not fully funded
  – Basic problem: EU is trying to solve political problems through regulation, but outcomes ultimately depend on social impact
Threats to Cross-Border Banking: Resolution and Brexit

- Brexit and “enhanced equivalence”
  - Is this a promise or a threat?
    - UK may face higher information and legal requirements, extraterritorial supervision
    - Implications for US?
  - Opening the black box of equivalence
    - Reducing UK uncertainty of future – reciprocity? procedural transparency?
    - Is there a multilateral solution to the web of bilateral agreements?
  - Equivalence should be outcomes-based, non-politicized
    - Should not require submission to extraterritorial supervision
  - Goals of actors differ
    - EU: accommodating Brexit is secondary to CMU, SRF; seeking competitive advantage
    - UK: bank branches in EU limited, so main concern is markets and CCPs
Threats to Cross-Border Banking: Resolution and Brexit

• Fragmentation as the new normal in Europe
  – Limited European financial market so far, despite CMU dreams
    • Fragmentation results from regulation, supervisory practices, politics
  – MiFID II effects – liquidity pools, localization of CCPs, etc
  – Effects of fragmentation
    • Liquidity down, costs up
    • May be price of being global for banks, but damaging to asset managers
    • Does not improve resolvability
  – Politics of fragmentation
    • Are European countries looking again to national champions?
    • Is Brexit just one example of populist-driven fragmentation?
The Evolution of the Asset Management Industry

• Changing face of asset management
  – Key question for regulators and industry: how well are end-investors being served?
  – Competition and tech
    • Changing trading and allocation strategies
    • Driving down costs for investors
  – Changing balance of active and index funds
    • Debate on impact of index investing on liquidity, price determination
    • Retail distributors shifting from selling funds to selling portfolio allocation
The Evolution of the Asset Management Industry

**EU asset management**
- Market liquidity and efficiency lag US
- EU regulators still see asset managers as big, bank-like SIFIs
  - But end-users actually own shares, not funds, & mutual funds not leveraged
  - Lingering suspicions of foreign asset managers, preference for domestic
  - Is ECB the right regulator?
- Structural challenges
  - Lack of private pension funds retards both growth of asset management sector and feasibility of CMU
  - Lack of culture/tradition of risk capital in much of Europe
- Effects on allocation of capital, economic growth
The Evolution of the Asset Management Industry

• Composition of indexes
  – Bespoke “indexes” subvert the whole point
    • Not really indexes
    • Grading on their own curve
  – Is there a role for government?
    • Standard setting, transparency, “taxonomies”
    • May be a slippery slope!
  – Potential benefits of competition among indexes and index funds

• Benchmarks and the EU
  – Desire to protect investors (lessons of LIBOR)
  – Increasingly assertive regulation
    • What are pros and cons?
    • Extraterritoriality: will EU regulate the entire extended family of IBORs? How?
The Evolution of the Asset Management Industry

• ESG and asset management
  – Europe is asking asset management to solve societal issues
    • Comprehensive strategy or just shifting responsibility?
    • Should bear in mind that regulation of asset management means regulation of household assets
  – ESMA is building ESG agenda
    • Taxonomy of green companies
    • Will it go beyond mandated disclosure (e.g., risk-weighting of bonds)?
    • How to integrate with benchmarking rules?
  – How will Europe’s ESG agenda affect the world
    • Global leader?
    • Effects on US firms?
The Evolution of the Asset Management Industry

- **US approach is still private, voluntary**
  - Private standard-setting bodies
    - E.g. Sustainability Accounting Standards Board
  - Market-driven
    - Disclosure remains voluntary (but will this change under President Warren?)
  - Very different political status of sustainability from EU

- **ESG and risk**
  - Increasing sense that ESG aligns with long-term profitability
  - How to measure ESG commitment and impact?
    - Need better, more standardized data – who will provide?
    - What are the necessary tools and models?
UPCOMING EVENTS

2019

China - U.S. Symposium
*June 5 – 7, Washington, D. C.*

Japan - U.S. Symposium
*October 4 – 6, Odawara, Japan*

To receive an invitation to other PIFS Symposia, or to recommend your colleagues for participation, please contact:

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