World Conference of Banking Institutes – London, 17 September 2019

The Role of Banking in a Sustainable Global Economy

Keynote address by François Villeroy de Galhau,
Governor of the Banque de France

Press contact: Mark Deen (mark.deen@banque-france.fr; +33 6 88 56 54 03).
Ladies and Gentlemen,

I am delighted to be with you today. The topic that you have asked me to address – “The Role of Banking in a Sustainable Global Economy” – prompts us to think about the future. However, let me first say a few words about the present. The current context is one of increased uncertainty, which is already weighing on growth at the international level. Two threats are contributing to this: above all, trade tensions coming from the US, and second – of course – Brexit. Needless to say, this situation is not sustainable. It is the responsibility of politicians more than central bankers, to restore confidence. The latest example of this uncertainty is the spike in oil prices after the attack last Saturday on Saudi Arabia’s oil infrastructure. It is too early to rush to hasty conclusions; we should closely monitor the consequences on the oil market, which is characterised by a rather flexible supply and a subdued demand. Oil price has significantly decreased since June, by about 20%. If it lasts, this latest oil shock could increase inflation and hamper growth. In my remarks today, I will briefly start with Brexit before addressing two of our shared challenges for the future: digital transformation and green finance.

**

I. The prospect of Brexit and our future relationship

Let me say from the outset that Brexit is and remains bad news, not only for the United Kingdom, but also for Europe. But we respect the British choice, whatever it turns out to be. At this stage, both the British and Europeans are faced with great uncertainty surrounding the outcome. We are still hoping for a deal, but we have to be ready for a no-deal and all the risks it entails. Supervisors both at national and European levels have encouraged and monitored the implementation of contingency plans by the financial industry: on our side, we are ready.

Let me add one word on the future relationship between the UK and the European Union. After Brexit, we will obviously no longer belong to the same European club, but we will hopefully remain close partners and friends. The
UK will continue to participate in international forums – such as the G7, G20 FSB, BIS, etc. – where cooperation will be much needed to face our common challenges such as financial stability, digitalisation and the regulation of Bigtechs, as well as the challenge of green finance. In a context where the multilateral order is being put at risk, let me express the wish that the UK, together with the EU, may resolutely strive to renew multilateralism. On our side of the Channel, our collective response to Brexit may possibly be a further integration of Europe, with the new and promising Commission led by Ursula von der Leyen, rather than isolationism or paralysis. Europe should build on its most valuable assets: the euro, which is celebrating its 20th anniversary this year, the single market and its shared social and environmental model.

II. Making the digital leap with lucidity

Let me now turn to our shared common challenges. Digitalisation is shaking up the way we live and consume, opening up a world of possibilities for corporates and customers alike. Worldwide, it clearly represents both an opportunity and a challenge for banks, as well as for supervisors.

**New players** are becoming increasingly important. Fintechs do not have the capital resources to disrupt incumbent banks and can even be acquired by them. By contrast, Bigtechs do have the potential to fundamentally redefine financial intermediation: they have strong brand recognition, a worldwide customer base and privileged access to cutting-edge technologies. This new situation is a major challenge for regulators and supervisors. Of course, financial regulation should remain technologically neutral: the basic principle “same activity, same rules” must apply. This is a good thing for the level playing field. However, beyond traditional financial regulation, international cooperation should be developed in four areas, four cornerstones of the regulation of digital finance. First, **cybersecurity** is a sine qua non for a reliable and sustainable digital future. It was a clear priority of the G7 French Presidency this year. Second, regarding **data protection**, financial supervisors
and authorities in charge of privacy have to invent new ways of cooperation to address data issues that have become central to financial services. Third, regarding competition and anti-trust policies, situations where “the winner takes most” while staying outside the scope of financial regulation should be adequately anticipated and addressed. And fourth, fair taxation, thanks hopefully to OECD work.

“Stable coin” projects, including Facebook’s Libra, are a case in point. “Stable coins” are quite different from speculative assets like Bitcoins. However, regulators will have to keep a very close eye at the global level, and believe me, we will do it. At their meeting in Chantilly in July, G7 members have expressed a clear position: stable coin projects raise a sovereignty challenge, and “serious regulatory and systemic concerns, as well as wider policy issues, which both need to be addressed before such projects can be implemented.”

France, as Chair of the G7 this year, has created a dedicated task force – as soon as the project was announced by Facebook. The task-force, chaired by Benoît Coeuré, will make its conclusions public and make recommendations in October. Our aim is to formulate a response that is common across all jurisdictions, and holistic, covering all the issues. And to quote only two of many requirements: it is imperative that such projects comply with anti-money laundering regulations; the anonymity of the users creates heightened risks. In addition, if issuers of stable coins also want to offer banking services such as deposits, financial investments and loans, then they will have to obtain a banking license in all countries where they operate. Otherwise these activities would be illegal.

Stable coin projects reveal gaps in existing cross-border payment systems. Hence, at the European level, we should aim at promoting a genuine European strategy for retail payments. Payments are no longer a mere boring back-office technicality. They are innovative, and they provide two strategic assets: data, and daily customer relations. The raw truth however is that the European payments market is already dominated by non-European stakeholders. Furthermore, the growing role of non-European digital firms – be
they American or Chinese – offering payments solutions should be taken seriously. Despite the creativity of the European ecosystem of payments, our market remains too fragmented. We don’t have much time left. We – the Eurosystem and the Banque de France – call for the creation of pan-European payment solutions, building on a common brand and on a state-of-the-art instant payment such as the Target Instant Payment Settlement infrastructure (TIPS) managed by the Eurosystem, and contributing to much more efficient international payments including for remittances.

Some also suggest that the right answer to Libra is accelerating the creation of a **Central Bank digital currency** (CDBC). This is a scintillating subject, but a separate one. We Central banks should investigate the many questions it raises – and we have started this work at the Banque de France –, and then decide on its own merits.

**III. Green finance, “a new frontier for the 21st Century”**

Let me now turn to green finance. For me, it is “a new frontier for the 21st Century”. First and foremost, I would like to pay tribute to the Governor of the Bank of England, my colleague and friend Mark Carney, who was a pioneer when he pointed out “the tragedy of the horizon” in 2015. Much has already been undertaken since then.

We are currently witnessing a **growing awareness** from central banks, supervisors and financial institutions about climate-related risks. Clearly, green finance and climate risks management have gone from the “nice to have” to the “must have”, from emotion to reason. In financial institutions, climate change is no longer confined to Corporate Social responsibility (CSR) policy. Concerning central banks and supervisors, the creation of the Network of Central Banks and Supervisors for Greening the Financial System (NGFS) in Paris in December 2017 has been a decisive step forward. In 18 months, this coalition of the willing has increased from 8 founding members to almost 50 members and observers from all 5 continents, with the Banque de France acting as its permanent Secretariat and the active involvement of the Bank of
England. This momentum has an important meaning: supervisors and central bankers have collectively acknowledged that climate change-related risks are a source of long-term financial risk. In April 2019, the NGFS published its first comprehensive report issuing four recommendations for central banks and supervisors, and two additional recommendations for policy makers.

Looking down the road, I see three priorities for the near future. First, we will require enhanced disclosures that need to be built on sound taxonomies. The taxonomy framework published by the Technical Expert Group (TEG) on Sustainable Finance of the European Commission on 18 June is a welcome step. Second, we have to better anticipate long-term climate-related risks, through what I call “the video of the risks”. We must push for the development of comprehensive climate stress tests in order to build a forward-looking approach of the impacts of climate risks. Third, green finance needs to mature and upgrade its professional standards. The financing needs for the energy transition are huge; in Europe alone, it is estimated that an additional EUR 177 billion per year will be necessary over the period 2021-2030 to reach the EU’s energy and climate objectives for 2030. The European Green Bond Standard proposed by the TEG should ultimately help to further develop the green bond market and channel more investments towards green projects.

Furthermore, many proposals have been made to allow monetary policy to play a direct and sector-focused role in financing the transition to a low-carbon economy. For example, some suggest a “green quantitative easing” by introducing a bias towards green assets in the purchase programme framework. Despite its apparent simplicity, this proposal is somewhat incomplete and has some limitations: monetary policy targets a macroeconomic objective (inflation) and it does not single out specific social or sectoral objectives; and massive purchases on a relatively shallow pool of green bonds could seriously distort the market. I prefer a more “integrated” and holistic approach – and hence more ambitious, consistent with our financial stability and monetary policy mandates. This is what I pointed out in the latest issue of the Financial Stability Review of the Banque de France in
June. Climate change is a source of financial risk, but it can also provoke both upward price pressures and a slowdown in activity – and can thus generate a long-term stagflationary shock. In the light of this, central banks have two main tools at their disposal that should be activated. First, it is essential that they contribute to the collective research effort in order to better understand and anticipate the economic effects of climate change, and still more that they integrate these into their macroeconomic models. Second, in operational terms, this involves integrating the results of climate-related risks into the assessment of collateral. This requires the development of a robust methodology to accurately assess the impact of climate change on the credit risk of eligible assets.

**

Let me conclude with a strong conviction: these shared challenges for tomorrow require immediate action from us today. Political philosopher Thomas Paine said: “If there must be trouble, let it be in my day, that my child may have peace.” Let us hope that beyond Brexit, we will find common grounds to build a desirable future for the next generations. Thank you for your attention.

References

i Chair’s summary: G7 finance ministers and central bank governors’ meeting, Chantilly, 17-18 July 2019
iii Source: European Commission