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I. Introduction

Honorable members of the European Parliament, dear Mr Chair, dear Ladies and Gentlemen,

First I would like to express my sincere thanks for inviting me to this hearing of the Economic and Monetary Affairs Committee. My name is Martin Grüll, I am the CFO of Raiffeisen Bank International. RBI´s headquarters are based in Vienna, Austria and we regard Central and Eastern Europe as our home market. For nearly 25 years RBI has been operating in Central and Eastern Europe (CEE), where today it maintains a closely knit network of subsidiary banks, leasing companies and numerous specialized financial service providers in 17 markets. A team of 54,000 employees services almost 15 million customers.

II. Interconnection between financial regulation, economic stability and economic growth

From the perspective of a “bread&butter” commercial banker, the topic of the hearing aims at the right direction: A more efficient and effective EU framework for Financial Regulation! The right direction because more consistent and efficient Financial Regulation in Europe will not only strengthen financial market stability, but will also boost economic growth!

There is a direct link between a fair and effective financial regulation framework and a healthy banking sector which acts as an intermediary for a growing economy. It is very important that the regulatory environment does not crush its players and makes them incapable to act effectively.

Banks are confronted with
- low interest rates,
- weak credit demand and unpredictable national budgets,
- low profitability and reduced access to capital markets,
- ever increasing regulatory capital requirements and
- additional new contributions, levies and fees introduced in the context of Financial Market Regulation

Such an environment creates major challenges for the whole industry which
may ultimately impede economic growth. The capital and liquidity requirements of CRD4/CRR and the Banking Union are necessary steps to strengthen the stability of the European financial market. In future no taxpayer should pay for the recovery of a bank. However, a precondition for this new system to work in practice, is an appropriate implementation period in order to build up the required equity. Otherwise lending to the economy will be reduced which paralyses economic growth.

It is evident that supervisors tend to accelerate the implementation periods and demand capital buffers much faster than required by law.

The newest developments regarding Basel IV (consultation paper of the Basel Committee on risk weights) might even foster this trend and further hamper client financing. The new proposal increases risk weights which would restrict lending to SMEs even more. Let’s not forget –SME business is the backbone of Europe’s economy!

III. Inconsistencies of the current financial regulatory framework

I would like to mention four areas of inconsistency of the current financial regulatory framework which significantly tie up crucial human and financial sources and make it harder for banks to build up the necessary capital to promote lending.

1. Supervisory practices

a. Reporting Requirements

The relevant EBA-Standards for reporting requirements encompass almost 1800 pages. There are various authorities (ECB, national authorities, SRB) which should be obliged to coordinate their reporting activities. An effective Banking Union requires a strong coordination between the different supervisory authorities. Already today we are faced with duplication of reporting requirements. On the top of this, reporting requirements will be extended in the near future. ECB plans to introduce reporting of every single loan exceeding a threshold of EUR 25,000 (“AnaCredit”). Especially smaller
banks are overloaded with these requirements.

b. Capital Requirements

In addition, it is crucial how capital requirements of national supervisory authorities and decisions of ECB interlink with each other. There is still a high degree of uncertainty. For instance: At the moment it is not clear how capital buffer requirements of national supervisory authorities are integrated in the SREP decisions of the ECB.

RECOMMENDATION

Consequently, we ask for a clear and consistent framework for fixing and implementing capital buffers. For smaller banks it is necessary that supervisory authorities adapt regulatory requirements to their business models. A smaller bank should not be obliged to fulfill the same requirements imposed on bigger banks (e.g. reporting requirements, internal governance requirements and remuneration policies).

2. Bank levies

Bank levies weaken the stability and jeopardize the Single Market and hence fair competition in Europe: Since the financial crisis, we observe a significant increase in the number of national bank levies being implemented, with the purpose to avoid citizens to pay for failing banks. Bank taxes are currently imposed at the national level, with 16 countries in Europe having introduced a bank levy. This has led to a fragmented landscape of bank levies, leaving banks operating cross border to cope with varying requirements in Europe. Some levies, for example in the UK, have been introduced as taxes funding the general budget, others (e.g. Germany) as regulatory levies feeding a resolution fund separate from the general state budget.

Some of these taxes are currently paid on top of the contributions to the national resolution funds or the European Single Resolution Fund. This is an unbearable burden. This money could be otherwise used to strengthen our capital base, for granting loans and for developing new client service models (e.g. digital banking).
RECOMMENDATION

Therefore, we recommend that national bank tax shall be used as contribution to the resolution funds (national funds and European fund). In future, only the Single Resolution Fund should be the instrument to foster the stability of the financial markets and to break the link between sovereigns, taxpayers and bank failures. Any additional national tax for the same purpose should therefore be banned.

3. Cross border activities

For a cross-border banking group, active in EU, Non-EU, EURO and Non EURO countries, harmonized supervisory practices are key for a functioning business model. But in practice supervisory procedures differ significantly from country to country as the European Banking Authority rightly identified in its report from April 2015.

a. SREP decision

Differences are observed in the terms of imposing specific prudential requirements pursuant to CRD IV on institutions. The competent authorities assess the adequacy of own funds held by supervised institutions and in almost all cases require a specific minimum level of capital, taking into account the risk profile. However, the way that the minimum level of capital is actually communicated and effectively imposed on institutions is very different. Some authorities prefer to articulate it in the form of an “expectation” or “recommendation”, while other ones prescribe the minimum level as a binding legal requirement. In a few cases, competent authorities recommend ICAAP improvements which generally translate into higher internal capital requirements. Such inhomogeneous decision-making results into unfair competition and regulatory arbitrage.

b. Composition of capital

Supervisory practices also differ in terms of eligibility of capital instruments which may be used to meet new target levels, with some competent authorities being quite restrictive and others allowing a wider range of instruments.
RECOMMENDATION
A harmonized approach is most necessary in order to avoid national ring-fencing actions and solo attempts of single countries.

4. IFRS 9
IFRS 9 will transform banks’ financial statements in a fundamental way. It will require banks to use risk models to calculate future expected losses in their loan book. When credits deteriorate, banks will take a provision for the future lifetime expected loss of the credit. Offsetting future profit streams will not be taken into account.

This leads to the following:

- Accounting information will become even more complex, judgmental and difficult to compare. It will suffer from the same problems that are dogging the Basel IRB approach.

- Accounting values will take a one-time hit, as the standard is applied for the first time on a catch-up basis. Reported bank equity levels could fall substantially.

- Accounting values will be highly volatile and pro-cyclical. In stress tests and at the onset of crises, banks will see provisions volatility going up significantly, resulting in hits to their equity. They will need to have much more equity to absorb this volatility. This results in higher cost-of-capital and lower lending activity.

These cumulative effects with the already mentioned new Basel IV capital requirements might have a detrimental effect on banks’ capital.

RECOMMENDATION
Interdependencies between accounting rules and Basel IV capital requirements should be seriously taken into account. Policy-makers, regulators and supervisors need to decide how they can best limit the cumulative negative impact on the regulatory capital of Europe´s financial institutions.
IV. Final remarks and outlook

Banks need a breathing space! Appropriate time should be given for evaluation and assessment of the current financial regulations as well as for coordination and harmonization of specific regulatory measures.

In particular, supervisory practices and reporting requirements should be in the focus of evaluation as well as interdependencies between accounting rules and capital requirements.
It should be reconsidered if all requirements on reporting and internal steering are also to be applied to smaller banks having simple business models.

National bank levies should be channeled into Resolution Funds.

Addressing a new way forward, then a Capital Markets Union is generally welcomed; but in parallel it is also necessary to support banks’ lending activities through a balanced regulation in order to guarantee the principle of proportionality throughout Europe.

Europe’s economy needs more than financial stability and tighter regulations. Banks also need earnings to fulfill their role as financial intermediaries to stimulate growth in Europe!

Thank you for your attention.