

Brussels, 14 January 2009

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For information: Executive Committee
Subject: *Minutes of the 27th Meeting of the Associates,
Brussels, 4 December 2008*

Dear Sir/Madam,

Please find enclosed the minutes of the 27th Meeting of the Associates that took place on 4 December 2008 in Brussels, approved by the Chairman, Mr. Giuseppe ZADRA.

Yours sincerely,

Viktorija PROSKUROVSKA
Adviser

Enclosure: (D2521a) – Minutes of the 27th Meeting of the Associates

DRAFT MINUTES OF THE 27th MEETING OF THE ASSOCIATES

- 4 December, 2008 @ 10.00 -

The Meeting was chaired by Mr. Giuseppe ZADRA

Participants: see list enclosed

ITEM	DISCUSSION
1. Welcome	Chairman of the EBF Executive Committee, Mr. Giuseppe ZADRA, welcomed the participants to the meeting.
2. Minutes of the previous meeting (EBF Letter 1141-C)	Minutes of the 26 th meeting of the Associates, held in Tirana, Albania, on 5 June 2008, were approved.
3. Responding to the financial and economic crisis	Speech by Mr. Martin POWER, Head of Commissioner Charlie McCREEVY's Cabinet, DG MARKT, European Commission

Mr. POWER opened his speech with the questions "Where are we now?" and "What is the future?" He emphasised that the main issue at the root of the current problem is that of **risk**: its pricing, management and supervision.

Current task of the EU is to strengthen and improve the regulatory framework. In this respect, work has been undertaken *inter alia* on the Credit Rating Agencies, methodology has been developed on Colleges of Supervisors, and progress has been made with Solvency II:

- **Banking Supervision.** The European Commission has established a [high-level expert group](#) chaired by Jacques de Larosière, to make recommendations to the Commission on strengthening European supervisory arrangements covering all financial sectors, with the objective of establishing a more efficient, integrated and sustainable European system of supervision and also of reinforcing cooperation between European supervisors and their international counterparts.
- **Deposit Guarantee Schemes (DGS).** In order to prevent bank runs, the payout period of the DGS was reduced from 35 days to just 3, which is a much more efficient measure for bank-run prevention than increasing the amount of coverage. The Commission's [proposal](#) is to ensure that the DGS cover €50,000 when the new legislation enters into force at the end of 2008, and to €100,000 by the end of 2009.
Should uncertainty in the market prevail further, more government intervention should be expected.
- **Insurance industry.** Parallel requirements are being addressed in the Capital Requirements Directive (CRD) and in Solvency II. The key proposal for the insurance industry concerns the support of large cross-border group functioning, which is an important element of supervision regulation. Current debate evolves around the ways to get the solution right. Mr. POWER postulated that while it takes time to find a common solution, it is better to spend longer time and arrive at the right solution, than to take hastily less-than-perfect decisions.
- **IASB.** Governance of the International Accounting Standards Board (IASB) is being improved. IASB Supervisory board's governance needs significant improvement in order to merit the role of the international standards settler.
- **Hedge funds.** A consultation is currently open that examines the adequacy of arrangements, *inter alia* to strengthen the supervisory measures.
- **Accounting.** Pro-cyclical effect of current measures on accounting rules is being discussed. By mid-

March a proposal will be prepared for G-20.

- **Derivatives.** Regulators and supervisors need to have a better overview over the derivatives markets. Central clearing is a big step in the right direction of improved transparency and oversight.

Liquidity risk and stress testing is also part of the G20 work programme.

- **Government Support.** State aid and the recapitalisation measures have been put in place in the different EU countries. However, banks must remain attractive for private investors and the lending process continue. This is why the exit strategy must be factored in for the state as soon as the situation improves and to allow private investors to step in.
- **Economic situation:** the current recession is not an easy one to step out of. Total losses from the crisis have been estimated at € 2-3 trillion, so another € 800-1000 billion of losses (including consumer debt) are to be declared. Consolidation of banks is envisaged. Banks will adopt a more conservative approach to working and will earn lower profits. Consumer-led recovery is not to be expected in 2009. It will take long to restore consumer confidence as dramatic rise in unemployment has already started, and the hope that the emerging markets will pull the developed world out of recession will not be fulfilled as the BRIC countries are facing their own challenges. Overall, 2009 is expected to be difficult.

Further discussions with the meeting's participants revealed the following:

- Current crisis showed the need for stronger **supervisory coordination**. The current reality is that of increased mistrust. The core of the problem lies in the lead supervisors not informing supervisors from other countries on the bad situation. Therefore, time is needed to get back on track. To make the supervision in Europe function, more confidence in supervision is needed. The current realisation is that the existing system will not work. Colleges are not politically easy. This solution is being discussed under the CRD review, but the current proposal is not optimal, because crisis has reduced supervisors' confidence.
- The European Commission is not part of the **G20** and their work. However, G20 already has 4 European Union seats. The EU Members need to harmonise their position internally, because their presence at the G20 will not increase. However, the Commission is an EU legislator, and progress has been made on some issues already. This said, it must be recognised that the financial markets are **international**, so the response should also be international.
- **Standardisation of the derivatives markets** will be addressed by the Commission in its work towards the end of March. Most urgent area is the credit default swaps. The US market is well-advanced; and in Europe the focus is on the regulators. One way to do it is to move towards *central clearing*. However, the industry exerts resistance to standardisation owing to large associated costs and consequently reduced fees. The European Commission expects a European-based clearing facility. Even though the ECB could be well-placed to conduct this role, the fact remains that much of the activity takes place outside the euro area, so the ECB coverage would not be sufficient. The Commission believes that a central clearing house in Europe is an important element for stability.
- Guidelines for **recapitalisation measures** are to be issued, certain principles are expected to be seen in the Rescue Package, to refer to, *inter alia*, clarity; to the restrictions and conditions which should still allow the banks to continue their operations; and to fees. This crisis will inevitably lead to restructuring and merger of weaker players. DG Competition will work on the recapitalisation scheme. The system must work but not lead to a bubble.

Unlimited coverage of the private **Deposit Guarantee Schemes** is implemented only in Germany (and Norway). Unlimited coverage causes large movement of capital. The Irish example: customers of Irish banks saw the difference in the legislation between Ireland and the UK, and moved their capital from Ireland to Northern Rock (UK bank in Ireland). Lots of capital moved. Following that, the UK authorities put a cap of EUR 100,000 on deposit guarantee insurance, which triggered the panic across the depositors. The discussion therefore evolves around the payout period of the deposits: they must be paid out *rapidly*.

3. Responding to the financial and economic crisis (cont-d)	<i>Round-table discussion</i> of the impact of the financial crisis in the Associate countries, and the government and market response
<p>Mr. Garegin TOSUNYAN, president of the Association of Russian Banks, gave a presentation on the economic situation and the impact of the financial crisis in Russia (see presentation, EBF Ref. 1856C). The main messages of the presentation included:</p> <ul style="list-style-type: none"> • Banking sector growth has slowed down, and inflation increased. This causes a great problem, because the economy requires growth of capital funds, but the banks cannot meet the demand. In September – October 2008, following the announcement of the Lehman Brothers’ bankruptcy, the Russian stock exchanges fell and a significant outflow of bank clients and their deposits took place; however, by November the outflow has decreased. Growth of deposits decreased from 5% to 2%. • A lot of resources in Russia are in the hands of the State, and nowadays it is an advantage, even though in general it is unfavourable for business. Current challenge for the country is to use local resources more efficiently. • A number of bank bankruptcies have been registered; however, the overall number for 2008 will not exceed that of 2007 or 2006. The State allocated over RUR 200 billion (more than € 5 billion) to support troubled banks. This support is provided on the condition that banks will continue operating, but that the owners of the banks will change. Nationalisation will not take place; the State is planning an exit-strategy. The bank bail-out policy, practiced already before the crisis, is as follows: big banks are bailed out without revoking their licence; small banks (i.e. of minor social importance and with poor risk management) are let to fail. In 1990s Russia had around 2500 banks; ten years later the number had halved, and by 2008 the number had dropped to 1100. • DGS: total amount of guarantees by the State to private deposits was raised to RUR 700,000 (from RUR 400,000) and is 100% guaranteed. The pay-out term is 2 weeks by law. • The State provided USD 50 billion to cover obligations to external creditors. Current state allocation to banking sector is more than USD 100 billion. • Special attention is to be paid to the mortgage market. Over the last 6 years the mortgage market in Russia has been doubling every year, however the size of the market is still extremely low. • Support of SMEs is a very important problem in Russia. The financial markets, as well as the economy in general, are poorly diversified. SMEs are the most under-credited and therefore most vulnerable enterprises in Russia. This is why over the past 2 years, the issue of the SME support has been discussed and developed. Mr. Vladimir Putin organised a conference meeting “Council of Entrepreneurship” to work on the special programmes for improving the competitiveness of the SME, which is a hard task because Russia has a tendency to monopolise. • The impact of crisis on Russia is unexpectedly big. The difference between Russia and other countries is that it is still under-credited owing to the lack of internal resources (unlike in the over-credited US market). The capacity of the Russian market is huge, and it will attract a lot of resources from abroad. At the same time, the Central Bank and the government will ensure the stability of the economy, thus making the country attractive for foreign investors. <p>Mr. Zoran BOHAČEK, Managing Director of the Association of Croatian Banks (see presentation, EBF Ref. 1856C) spoke about the economic situation in Croatia in the context of the crisis. His main messages were:</p> <ul style="list-style-type: none"> • Banking sector experiences lower growth (banks’ profits grew by 26% in 2008). Return on assets (ROA) and return on equity (ROE) are incrementally falling, but are still at high levels. • Inflation jumped this year, mostly owing to the increase in the commodity prices and oil prices. 	

- **Stock markets** fell by 50% in October-November with the announcement that the Lehman Brothers were let to fail. This radical drop represents a major loss for the financial system. Spreads were falling to very reasonable levels in 2007, but have widened again in the crisis. Croatian Central Bank abolished the marginal reserve.
- On the positive side, international reserves remain high. Deposit growth is healthy (both in domestic and foreign currency). Amount of loans is growing, but at a slower pace.
- On the negative side, the current account and foreign debt in Croatia is huge. Exports comprise only 40% of imports, which is a negative factor.
- The strong side of the Croatian banking sector is that banks' assets are only 65% of the loans, the rest being more liquid. At the same time, 67% of liabilities are deposits. Capital adequacy is 12% (although in reality it is 15%), as enforced by law in 2008. The Croatian Central Bank has the capacity to cover the deposits of the banking system.

Ms. Sladjana SREDOJEVIĆ, Adviser at the Association of Serbian Banks gave a presentation on the impact of the financial crisis on the Serbian economy and financial sector (see presentation, EBF Ref. 1856C).

Mr. Nebojsa ĐOKOVIĆ, Adviser at the Association of Montenegrin Banks spoke about the impact of the financial crisis in Montenegro (see speech, EBF Ref. 1856C).

Chairman suggested introducing a round table discussion about the economic and financial situation in the Associate countries at every EBF meeting.

4. Public-private financial sector modernisation: progress made since the last meeting (EBF Letter 1786-C)

Address by Mr. Luigi PASSAMONTI, Head of the Convergence Program of Financial and Private Sector, World Bank

Mr. PASSAMONTI presented the results of the work carried out with the EBF on the SPI Project up till the moment of reporting. He invited the Associates to consider implementing the SPI Project in their countries, and the EBF Members to contribute to the modernisation of EBF Associates' financial sector (see presentation, EBF Ref. 1856C). The consequent discussion evolved around the following points:

- No country is used as a benchmark to the way of modernisation of financial services. The approach used by the SPI Program is programmatic and evidence-based, based on the weigh-and-evaluate method. This approach seeks to find the best way to import the pieces of good practice and put them together.
- The SPI Platform is a mechanism that takes time to put in place. It is designed to prevent bad regulation, to build up capabilities for making informed choices for each individual country.
- The World Bank (WB) *name* was essential to establishing the programme. The SPI system reflects the institutional knowledge and experience. It is embedded in the way the SPI operates. However, *who* becomes the operator, becomes progressively irrelevant, and the WB has no ambition for the monopoly of the Program (WB's mandate is expiring within a year's time).
- SPI aims to create a tradition of better regulation that is to remain in the country and to prevent the possible unexpected situations in the national parliament when adopting laws.
- In the case of Croatia, if the full SPI package (i.e. with the support of the ECB, of the Commission, *etc.*) had been introduced at the time when it was first discussed a few years ago, then Croatia would have immediately implemented it.

5. EU supervisory architecture	<p>Presentation by Mr. Enrico GRANATA, Director, Italian Banking Association, on “The question of Colleges of supervisors: an European Overview”</p>
	<p>Mr. Enrico BERNARDI, EBF Adviser and Secondment from the Italian Banking Association, presented the ABI study on Colleges of Supervisors on Mr. GRANATA’s behalf (see presentation, EBF Ref. 1856C).</p> <p>The work of G20 focuses, <i>inter alia</i>, on the colleges of supervisors, aims to be delivered by March 2008. The goal is to amend the Capital Requirements Directive by creating the colleges of supervisors for the EU banking groups. The ABI conducted a study of the EU banking groups, involving over 4,000 intermediaries (and no branches) across the EU MS.</p> <p>There are currently schemed 24 countries which are chairing different number of Colleges (e.g. Germany would chair 24 Colleges, Italy 11, Hungary 2). The countries will also have a seat in the Colleges which they will not chair (e.g. Germany will participate in 37 such colleges, Italy in 17, Hungary in 16). The total number of the cross-border Colleges of Supervisors estimated by the study is 139.</p> <p>The relevance of the Colleges of Supervisors differs from country to country, depending on the market share held by cross-border groups of a given Member State in the other EU Member States. Countries that will be most affected by the introduction of Colleges of Supervisors in the Capital Requirements Directive (in the diminishing order of relevance) are: United kingdom, Belgium, Sweden, Switzerland, Italy, Netherlands, Germany, France, Austria, Ireland.</p> <p>At the moment, the role of the lead supervisor is not clear. If the lead supervisor has the last say, it will be hard to obtain an agreement on this legislation, however, it will bring more efficiency to the functioning of the colleges of supervisors.</p> <p>Current system of supervision is mediated by the Committee of European Banking Supervisors (CEBS). In the event of a disagreement between the supervisors of different countries, CEBS would find a solution. The statement of CEBS is not binding, however.</p>
6. Latest developments in EU legislation in financial services (EBF Letter 1787-C)	<p>Ms. Viktorija PROSKUROVSKA, EBF Adviser, presented an update of the EU legislation in the financial services over the last six months (see presentation and a complete document, EBF Ref. 1856C). Mr. Guido RAVOET, EBF Secretary General, contributed to the presentation with the information on the EBF work and positions regarding the various EU legislative steps.</p>
7. Any other business (EBF Letter 1785-C)	<p>Ms. Viktorija PROSKUROVSKA, EBF Adviser, informed the participants of the meeting about the Secretariat’s work on the update of the EBF Integration Report.</p>
8. Date of next meeting	<p>The 28th meeting of the EBF Associates will be hosted by the <i>L’Association Monégasque des Activités Financières</i> on the 18th June 2008 in Monaco.</p> <p>More information will follow closer to the meeting date.</p>

All presentations were circulated by the EBF Secretariat on 5 December 2008 (EBF Ref: 1856C).

LIST OF PARTICIPANTS OF THE 27th MEETING OF THE ASSOCIATES

- 4 December, 2008 @ 10.00 -

<u>Chairman</u>	Mr	Giuseppe ZADRA
<u>Secretariat</u>	Mr	Guido RAVOET
	Ms	Viktorija PROSKUROVSKA
	Mr	Enrico BERNARDI (AM)
<u>Albania</u>	Messrs	Elvin MEKA Edvin LIBOHOVA
<u>Austria</u>	Ms	Maria GEYER
<u>Andorra</u>	Ms	Claudia CORNELLA DURANY
<u>Azerbaijan</u>	Messrs	Eldar ISMAYILOV Nazim IMANOV
<u>Belgium</u>	Messrs	Michel VERMAERKE Geert VAN LERBERGHE
<u>Croatia</u>	Mr	Zoran BOHACEK
<u>Estonia</u>	Ms	Katrin TALIHARM
<u>Finland</u>	Mr	Erkki KONTKANEN
<u>France</u>	Ms	Ariane OBELENSKY
	Mr	Jean-François PONS
<u>Germany</u>	Mr	Bernd BRABÄNDER
<u>Hungary</u>	Mr	Rezso NYERS
<u>Liechtenstein</u>	Mr	Michael LAUBER
<u>Monaco</u>	Mr	Jean DASTAKIAN
<u>Montenegro</u>	Messrs	Nebojsa DJOKOVIC Mirko RADONJIC
<u>Norway</u>	Mr	Alf Arne HAGELER
<u>Russia</u>	Messrs	Konstantin N. MOZEL Garegin TOSUNYAN Oleg PREKSIN
<u>Serbia</u>	Mr	Veroljub DUGALIC
	Ms	Sladjana SREDOJEVIC
<u>Slovenia</u>	Mr	Dusan HOCEVAR
<u>Spain</u>	Mr	Pedro Pablo VILLASANTE
<u>Sweden</u>	Ms	Ulla LUNDQUIST
<u>Switzerland</u>	Mr	Urs ROTH P.
<u>Turkey</u>	Ms	Melike MUMCU

Guest Speakers

Mr. Martin POWER, Head of Commissioner Charlie McCREEVY's Cabinet, Directorate General Internal Market and Services, European Commission

Mr. Luigi PASSAMONTI, Head of the Convergence Program of Financial and Private Sector, World Bank
