Joachim Wuermeling: International cooperation in financial regulation - between myth and reality

Speech by Prof Joachim Wuermeling, Member of the Executive Board of the Deutsche Bundesbank, at a reception to welcome the new chief representative of Deutsche Bundesbank's New York office Gabriele Kabelac and to bid farewell to Dr Claudia Stirböck, New York City, 11 September 2018.

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1 Introduction

Ladies and gentlemen,

It is wonderful to be back in New York City, a city so rich in American and international flair.

We are here today to welcome the Bundesbank's new chief representative, Gabriele Kabelac. For us at the Bundesbank, this event is much more than a simple changeover – it symbolises the importance of our transatlantic partnership and friendship.

But tonight is also the final night of Rosh Hashanah, the Jewish New Year. Rosh Hashanah, I learned, is also referred to as the Day of Remembrance. It requires an "accounting of the soul", a deep reflection on the past year.

Before coming here, I reflected not only on my personal year, but also on the political year behind us. I thought, for instance, about the still-looming trade war and its possible repercussions on economic growth throughout the world. But I also thought about the negotiations over finalising Basel III – which have been completed, thankfully, but were difficult, quite frankly – and the deregulation debate. It became clear to me that the values of international cooperation and multilateral alliances are being visibly threatened by growing political tensions within our nations as well as between them.

I have reflected then on what would be necessary to enter into a healthier new year for our transatlantic friendship and for international cooperation. Let me make a few remarks about what – in my opinion – won't work and what can work. I will focus on banking and financial supervision, my main responsibility as a member of the Bundesbank's Executive Board.

2 The illusion of national sovereignty

The first approach that won't work is in my opinion the illusion of national sovereignty. This means the idea that – as the Brexit cheerleaders led the British people to believe – if you pull your country out of the web of international agreements, you can go it alone and even be better off.

Unfortunately, reality has been demonstrating how much of a myth that is. Regarding Brexit, many people in the UK are only now beginning to realise how dependent their economy has been and still is on EU membership. Many problems became only obvious during the exit negotiations – most of which were never an issue during the leave campaign.

I think that compartmentalisation helping the national economy is a dangerous illusion which does not provide substantial solutions to serious challenges. There has never been such a mythological nation-state, and it certainly doesn't exist in the era of the internet, smartphones and mass air travel.

What then is sovereignty in the 21st century? It is the capacity to decide rationally about where cooperation is, on balance, better than going it alone, even if it entails unpleasant compromises.

3 The rationale for international cooperation in financial regulation

Following that, it seems reasonable to approach many areas of the economy in an internationally cooperative, rules-based manner. Financial regulation, in my opinion, continues to be one area conducive to this approach, as we want to prevent a regulatory race to the bottom and to ensure fair competition, i.e. a level playing field.

It was in that spirit that the G 20, led by the United States, spearheaded the efforts to tackle the financial crisis.

The G 20 efforts have created a rational, viable approach to international cooperation that is in the interest of all member states – its principles should therefore remain pillars of the regulation of international finance.

It is built on close transatlantic and international cooperation between our central banks and our regulators and supervisors. It also rests on the joint work in international regulatory fora to foster our mutual understanding and the common language we have developed over the past thirty years.

This approach also builds on a whole body of international minimum standards, like the Basel III regime for internationally active banks that we have developed over the last ten years. The Basel III standards have proven to be a success story, as they are the foundation for banking regulation in more than 100 countries.

4 The illusion of the global level playing field

Ladies and gentlemen, as we strive to prevent a race to the bottom and maintain a fair, level playing field, I am convinced that international, rules-based cooperation is – and should remain – the method of choice not only, but in particular in the area of financial regulation.

At the same time, I am less convinced that Basel III is a "one size fits all" approach and that adherence to international standards makes national supervision redundant. Basel standards are minimum standards that cannot cover each and every national specificity – in these few selected areas, national authorities need to fil these gaps, and adjust the standards accordingly. Another legitimate, but limited deviation concerns the reduction of administrative burdens for smaller institutions – like they are currently pursued in the US and the EU. Further, if a non-EU bank has substantial activities in the EU, it should have a consolidated subsidiary that is supervised in that jurisdiction. An internationally active bank cannot have core capacities of risk management, capital and liquidity only in one spot.

We have seen that the Intermediate Holding Corporation laws in the US work quite well; and the same will be true of the forthcoming EU equivalent, the Intermediate Parent Undertaking Regulation. The subsidiarisation requirement will also enhance the systemic stability of the financial ties between the UK and the EU after Brexit. Generally speaking, it is also a useful backstop against a regulatory race to the bottom, as it will make it difficult to provide cross-border services from less well-regulated locations.

So I do understand that in light of Brexit and the end of London's direct access to the EU single market fears of regulatory fragmentation are worsening and leading to more calls to maintain a global level playing field.

That's why the important achievements of non-discrimination against foreign firms on the one hand and the G 20's minimum standards should be upheld.

However, our approach to international cooperation is to make sure that every supervisor can oversee the entities active in its jurisdiction.

5 Conclusion

Ladies and gentlemen,

Simple answers to complex problems are comforting, but they divert our attention from the real issues.

The concept of splendid isolation is a myth; it solves no problems.

If the transatlantic partnership and close multilateral cooperation are to be resilient cornerstones of the world economy, we need rational, careful decision-making, policy case by policy case; where some cases will be better dealt with in the national realm, while others will turn out to require coordinated or even cooperative approaches.

The Bundesbank has a reputation as being principles-oriented – sometimes maybe even too much so. We will continue to seek our US partners' advice and work towards mutually beneficial solutions, where cooperation is rational and viable.

Our New York representative office plays an important role in those efforts, and to end my remarks, I want to introduce four persons who play important roles in furthering cooperation.

Let me start with the Executive Board member inter alia responsible for our New York office since September 1: Burkhard Balz. With twenty years of banking and regulatory experience, he will be an understanding partner for discussions on any financial topic. And, as a former member of the European Parliament, he is internationally well connected and speaks the language of diplomacy. At the Bundesbank, he will not only be responsible for our representatives abroad – and therefore the New York office – but also for the important area of payment and settlements systems.

We are both grateful for the excellent job that Ms Claudia Stirböck has done over the past five years as our chief representative in New York: she played a vital role in the exchange between the Bundesbank and the Federal Reserve and was instrumental in shaping our understanding of US regulatory policy during her tenure. I am pleased that she will continue to apply her broad expertise back home at the Directorate General Economics in our Central Office.

Ms Stirböck leaving our New York office is a loss, but I am confident that Ms Gabriele Kabelac will be an excellent successor. Coming from our Directorate General Economics, she brings profound financial sector knowledge with her. Moreover, with her experience in coordinating the Bundesbank's participation in international forums, she will not only be a highly effective and creative contact to all of you, but will also be a joy to work with.

Our new team now has the honour of welcoming – and I have the pleasure of introducing – tonight's keynote speaker: Professor Stanley Fischer.

What is there to say about a man who has served as Governor of the Central Bank of Israel – where he successfully guided the country through the global financial crisis of 2008 – but also Vice Chair of the Federal Reserve? And all that after having been the World Bank's Chief Economist, the IMF's Deputy Managing Director, and Vice Chairman of Citigroup.

The most fascinating item, to me, on his CV is that he was professor at the MIT Department of Economics, where he was the Ph.D. thesis advisor not only to Ben Bernanke, but also to – you guessed it – Mario Draghi.

I have therefore decided to let someone else find the right words: former US President Barack Obama. Four years ago, he said that Stanley Fischer would "bring decades of leadership and expertise" with him, and that he was "widely acknowledged as one of the world's leading and most experienced economic policy minds." I have nothing more to add, and I am honoured to give the floor to Professor Fischer.