

Challenges & Opportunities for the Eurozone: Capital Markets Union & Brexit

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Introduction by Simon Lewis, CEO, AFME

Good morning everyone.

Welcome to the sixth event in AFME's Brexit seminar series, in which, almost one year on from the UK referendum, we pause to reflect on the present and future challenges facing the European Union, including Capital Markets Union and Brexit and their impact on European and Italian markets.

This series began with a single AFME event in partnership with Clifford Chance back in March 2016 looking at the theoretical impacts of Brexit. In no way could we have anticipated the political tumult that has unfolded across the world in the year since. We have brought the series to EU27 financial centres – to Frankfurt, Brussels, and Paris already - and Milan today because at AFME, as the pan-European trade

association for Europe's capital markets, we are looking at Brexit through both sides of the lens. We are examining not only the implications for the UK and UK businesses, but also for EU27 and our many members with headquarters and operations here.

Before I comment on AFME's Brexit work in more detail, perhaps I could say a few words about the extraordinary outcome of last week's General Election in the UK. I am sure Chris Bates will want to comment himself, but let me just make a few points.

First, and not surprisingly, again the pollsters got it wrong. There was even one well-known pollster who was texting people on the night of the election saying the Conservative party would have a majority of 100 seats! Clearly there are lots of reasons why the outcome was not a working majority for the Conservative party, but a part of that is the fact that the UK has now returned to two party politics after a long time of multi-party politics. It is worth noting that between them the

Conservative and Labour parties attracted 80% of the vote for the first time since the 1970's. The only outright pro-EU party, the Liberal Democrat party, achieved just 7% of the vote.

Secondly, although Theresa May is endeavouring to put together a working majority with the help of Northern Ireland's Democratic Unionist Party, we should be in no doubt that this is a long way from a coalition, or even a minority government. It will be a 'confidence and supply' agreement. The DUP will only commit to support the government in any confidence vote and to support them on budget bills. Other than that, it will largely be agreed on a case by case basis. That is a large part of why, what is known as the government's Queen's Speech, which sets out the new legislative programme, has been delayed. This is highly unusual.

Thirdly, it is quite clear that although the negotiations with the EU will commence next week, the Prime Minister has a much weaker hand. There is now much more talk of a consensus for a so-called 'soft Brexit', although this is

somewhat difficult to define. It would appear that this might entail either rethinking membership of the customs union or indeed the single market and/or a version of membership of the EEA, at least for a transition period.

We won't know much more about these possibilities for a while but what is also emerging is a sense that the next stage of the Brexit negotiations in the UK may need to be on a bipartisan basis so we may well see the Labour party and Conservative party working more closely together on Brexit. This would be unprecedented in modern British politics, but these are unprecedented times.

My final comment, and do bear in mind that I am not a great political predictor, is that paradoxically I do not think we will see another General Election in the UK for at least a year, because the Conservative party has an awful lot to lose in calling what would be a third General Election in three years.

Turning back to Brexit, AFME is, as a pan-European trade group, very well equipped to play a pivotal role in the coming period by representing the views of our members across Europe's Capital Markets. We are uniquely positioned to consider both UK and EU 27 perspectives on the Brexit debate. In the 12 months since the referendum result, our Brexit work has been distilled into three distinct streams:

1. Firstly, In January we published a report in conjunction with PwC examining the operational impact of Brexit on wholesale banking groups. The report was distributed to a selected range of regulators, policymakers and other stakeholders across the EU and was cited by 25 media outlets across Europe including by the FT, Politico and newspapers in across EU27.

2. Our second Brexit work stream focused on the implementation challenges of Brexit. An AFME paper published in March examined the various aspects of the

wholesale banking transition requirements, to inform EU27 (and UK) policymakers on the practical implications and challenges of implementing Brexit. Operationally, the restructuring of wholesale banking business caused by Brexit will have a major impact on three main sets of actors: (i) wholesale banks; (ii) clients and end users; and (iii) supervisors. The paper explores the issues for each set of actors in detail, building on the messages and findings in the PwC report. Given the scale, complexity and risk of the Brexit implementation challenges for wholesale banking, market participants will need significant support from policymakers to help them safely navigate the process. The paper sets out three key sets of recommendations for action at European and Member State level to provide: (i) coordination; (ii) flexibility in implementation; and (iii) sufficient time.

Copies of these reports are available here today and on our website.

3. *Our next work stream on Brexit looks at the potential impact of a hard Brexit on wholesale banking for EU corporates and investors.* Working with management consultants BCG, we have interviewed over 60 SMEs, large corporates and investors from a wide range of industries and countries, as well as 11 European trade associations (including multiple trade associations representing SMEs, large corporates and investors). The feedback and insights from these interviews, including quotes and actual case studies, will be presented in the report to be published on 3 July 2017.

Of course, Brexit has cast uncertainty over the flagship project of the current Commission: Capital Markets Union.

AFME has supported the CMU initiative throughout the political tumult of the last year and continues to do so. The

Commission has now conducted its Mid Term Review, to which AFME submitted a detailed consultation response identifying a range of policy options that could be pursued to continue to drive forward the project. The Commission published its response to the Mid Term Review and further CMU actions last week, and we particularly welcome the following priorities:

- Review of the European Supervisory Authorities, in particular, to strengthen ESMA's powers and increase the effectiveness of supervision for specific functions to support a functioning CMU;**
- A renewed focus on key growth areas, such as improving access to risk capital for small businesses throughout Europe, as well as infrastructure investment;**
- Stronger focus on fintech, with the need for an EU licencing and passporting framework for fintech activities being assessed later this year;**

- **A strong push to develop a European policy programme on sustainable finance and the transition to a low-carbon economy;**
- **Improvements to the EU's secondary markets for distressed debt, where the European Commission will consult on improvements to the Non-Performing Loans framework to enhance data quality and value recovery; and**
- **Developing local ecosystems in the EU, particularly in Central Eastern Europe**

There has been progress to date on the CMU project, in particular the recent reaching of agreement on STS securitisation is a key development, however there is much work still to be done. We remain committed to working with the Commission to move the initiative forward.

So, despite this period of uncertainty across the European Union, our core work continues. AFME has continued to advocate our belief that integrated capital markets in Europe are essential to driving the jobs and growth agenda. We

continue to approach our work as we have always done, focusing on practical considerations. We want to remain true to our fact-based approach, producing analysis which will help policymakers and others weigh up different courses of action. The E in AFME is more important than ever as we enter this new landscape. We are continuing to build on and develop our existing European institutional, corporate and other relationships in the EU27. During this period of uncertainty, open lines of communication are crucial in Paris, Frankfurt (where we have recently opened an office), Milan, Madrid and elsewhere.

Let's now turn to our guest speakers for this morning. I'd now like to hand over the floor to Marco Valli, Chief Eurozone Economist at UniCredit. Marco has responsibility for the bank's view on the euro area economy and ECB policy. Thank you for taking the time to address us today and for agreeing to take questions from the audience.

Marco will be followed by Chris Bates, head of Clifford Chance's financial regulatory practice in London, with whom we have a longstanding partnership and who wrote the seminal piece on the legal and regulatory issues of Brexit, in early 2016 when Brexit remained a largely theoretical concept. Today Chris will review how Brexit has moved on a year since the referendum result and examine some of the many outstanding areas of uncertainty. Chris' remarks will also be followed by a Q&A with audience members.

Let me close by thanking Clifford Chance for their hospitality once again and for their continued productive relationship with AFME – on Brexit and a host of other issues of importance to our industry.

Without further ado let me welcome Marco Valli.