Andreas Dombret: Financial regulation as a global challenge

Remarks by Dr Andreas Dombret, Member of the Executive Board of the Deutsche Bundesbank, at a reception to say goodbye to Mr Jakob Orthacker, Financial Attaché, and to welcome his successor, Ms Julia Becker, London, 11 June 2014.

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Ladies and gentlemen

Thank you, Ambassador Ammon, for hosting this event here at the German Embassy in London. I am happy to have the opportunity to officially thank the Bundesbank's departing representative, Mr Jakob Orthacker, and to welcome his successor, Ms Julia Becker.

I am particularly happy that Sir Jon Cunliffe, Deputy Governor of the Bank of England, is here today. Thank you, Jon, for your remarks.

Now let me say a few words on financial regulation and the need for international cooperation. My argument begins with the idea that a global financial system requires global regulation. To push this idea further, I would define the term "global" in at least three dimensions and argue that regulation should be consistent in all of them.

First, regulation needs to be consistent across jurisdictions. This is necessary to provide a level playing field and reduce the scope for regulatory arbitrage. Against this backdrop, recent regulatory initiatives in some countries indicate that the "balkanisation" of the regulatory space represents a genuine risk. We have to be aware of that.

Second, regulation needs to be consistent across sectors. This is again necessary to prevent regulatory arbitrage. In practical terms this means that we have to deal with the shadow banking system. Consequently, the G20 have moved shadow banking high up on their agenda.

Third, regulation needs to be consistent across asset classes. Take the regulatory treatment of government bonds as an example. I cannot see a single good reason why banks should not have to back government bonds in their balance sheets by capital, but I see many reasons why they should – not least the objective of breaking the sovereign-bank nexus.

Financial regulation that is consistent along these three dimensions will help to make the financial system a safer place.

However, while being a safer place in the aggregate, the financial system is not necessarily a safe place for individual banks. After all, we live in a market economy and creative destruction is a central element. Individual banks must be able to fail like any other enterprise.

This must also hold for large banks which are often labelled "too big to fail". To allow them to fail without destabilising the entire system we need resolution mechanisms. And here again, we have a global dimension. Banks that are deemed too big to fail are globally operating enterprises; resolving them requires a great deal of international cooperation.

I think it is obvious that to make the financial system a safer place we have to cooperate in regulation, in supervision, and in the resolution of banks.

However, these are not the only challenges we face. Last week, the ECB Governing Council took far-reaching decisions in reaction to the long period of very low interest rates. It lowered the key interest rates for refinancing operations to 0.15% and cut the interest rate on the deposit facility to –0.10%. At the same time, it decided to conduct a series of TARGETed longer-term refinancing operations aimed at improving bank lending to the euro area non-financial private sector.

While the decision of last Thursday was appropriate given the present economic environment, we should now analyse the effects of these decisions before starting the next round of monetary policy easing. And let me make one thing clear: Monetary policy has played a very important role in fighting the crisis but it cannot solve the euro area's problems.

Another challenge we face concerns the United Kingdom and Germany, in particular. Both our countries are confronted with rising property prices and with the overarching question of whether there is a bubble building up. At least in Germany, we do not see a bubble at this point in time. Price increases are focused on large cities; for the country as a whole prices rose by a moderate 4.5% last year.

Nevertheless, further monitoring and in-depth analysis are certainly necessary. And in this regard, the Bank of England certainly leads the way. Although the structures of our property markets differ in many respects, there is still a lot we can learn from each other's experience. Thus, I highly value the cooperation between the Bank of England and the Bundesbank.

In any case, international cooperation always starts at the personal level. This is where our representatives in London come into play. Their task is to build networks, to share information and ideas, to explain the Bundesbank's positions and to facilitate cooperation.

For the past three years Mr Orthacker has filled this position here in London. And judging from the distinguished crowd gathered today, he has done an excellent job. I would like to thank him personally and in the name of the Bundesbank for his service.

I would also like to take the opportunity to welcome his successor, Ms Julia Becker. She is an expert from the Bundesbank's Financial Stability Department and has considerable experience in market infrastructures and related regulatory issues. Some of you have already met her, and I am certain that she will be a worthy successor to Mr Orthacker.

Thank you.