Jens Weidmann: Welcome remarks - "The G20 Agenda under the German Presidency"

Welcome remarks by Dr Jens Weidmann, President of the Deutsche Bundesbank and Chairman of the Board of Directors of the Bank for International Settlements, at the 9th Annual IIF G20 Conference "The G20 Agenda under the German Presidency", Frankfurt am Main, 15 March 2017.

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1. Introduction

Timothy Adams

Ladies and gentlemen

It's a great pleasure for me to welcome you to this conference, which is a joint event of the Institute of International Finance (IIF) and the German G20 presidency.

Many thanks to you, Tim and the IIF team, for organising this conference, which is taking place for the ninth time, this year just ahead of the meeting of G20 finance ministers and central bank governors in Baden-Baden.

The economist John Kenneth Galbraith is quoted as joking that "Business conventions are important because they demonstrate how many people a company can operate without."

I don't want to get too drawn into the merits of his humorous remark, or whether it applies to banking conferences as well, but I will say that there are compelling reasons why this conference is, indeed, an important event.

One reason is that it provides a good opportunity for dialogue between official and private sector leaders. This dialogue is particularly important in such challenging times, which is also reflected in the focus on very topical issues over the next two days.

"A global crisis requires a global solution."

This simple statement by the G20 heads of state or government back in April 2009 – in the middle of the financial crisis – captured the essence of the cooperation between the key industrial countries and emerging market economies. And although the G20 is an informal body – or perhaps precisely for that reason – it is an important source of impetus.

As the financial crisis unfolded, the G20 grew in status to become the dominant forum for economic cooperation worldwide. It played a key role in drawing the right conclusions from the crisis. But the job isn't finished yet. Additional efforts are necessary to make the global financial system more stable and the world economy more prosperous.

There are therefore several issues of global importance on the permanent agenda of the G20 that will continue to be pursued. In this regard, the German presidency is building on the important achievements of preceding presidencies, with the aim of ensuring continuity in the G20's activities. Just think, for example, of the growth strategies of the Brisbane summit or the structural reform agenda of the Chinese presidency last year. And some of you may also remember the debt reduction targets of the Toronto summit.

Beyond continuing the work of the existing G20 work streams, it is also the privilege and, indeed, the duty of every presidency to generate new inputs.

2. Priorities of the German presidency

The German G20 agenda rests on three main pillars: building resilience, improving sustainability and assuming responsibility.

To this end, Germany has set three main priorities for discussions between finance ministers and central bank governors and among the G20 working groups within the “Finance Track". These are

- Enhancing resilience
- Promoting investment, especially in Africa; and
- Shaping digitalisation

Let me go a bit deeper into these issues, starting with resilience.

The recent financial crisis has underpinned how important resilience is. While the crisis is considered to have passed, its negative consequences have not yet been completely overcome. Making our economies more resilient means improving their ability to cope with economic shocks, but also responding appropriately to longer-term structural challenges like demographic change or digitalisation.

The more resilient national economies are, the more resilient the world economy is as a whole. In economic terms, strengthening national resilience is a positive externality.

In order to strengthen national resilience, the German presidency is seeking an agreement on a set of principles in Baden-Baden.

Rather than prescribing specific measures or reforms, such principles can act as a guide for G20 members when considering different actions aimed at enhancing the resilience of their economies. Moreover, they complement other ongoing G20 initiatives and priorities, including the 2016 Hangzhou Enhanced Structural Reform Agenda.

The principles on resilience, which are currently being discussed in the G20, should aim to ensure sound public finances and to reduce vulnerabilities in the private sector. With respect to the real economy, they should advocate a favourable business environment, flexible labour market conditions and efficient social security systems.

Furthermore, monetary policies should be in line with central banks’ mandates and should not overstretch them or undermine the legitimacy of central banks’ independence.

Finally, G20 members should remain committed to the principle of open markets and cross-border trade – a point I come back to later in my speech.

The second priority of the German presidency within the Finance Track is related to the objective of stimulating investment, particularly in Africa. In an increasingly interconnected world, it is more important than ever to build global partnerships.

In order to create new and competitive jobs, the conditions for private-sector investment and investment in infrastructure need to be improved. Setting up a ‘Compact with Africa’ initiative is therefore intended to create better investment conditions, for example by improving legal certainty, making taxation more reliable, and reducing investment risks with the help of international guarantees.

Furthermore, the G20 will provide political support for specific investment agreements between

African countries and international organisations and – if desired – with developed partner countries.

In addition, transfers of money from migrant workers to their home countries are an important source of funds for many countries – not only in Africa. In several countries, these remittances account for more than one fifth of GDP and significantly contribute to domestic consumption and investment. The aim is therefore to improve the conditions for frictionless and efficient money transfers. Rules against money laundering and the financing of terrorism are important, but they should be applied in a way that does not discourage banks from providing correspondent banking services.

Last but not least, the third priority of the German presidency relates to digital finance and its implications for the financial sector.

From an economic point of view, digital finance can deliver a wealth of benefits. First of all, digital financial services can bring about significant efficiency gains – and I'm sure all of you know this much more than I do.

But digitalisation can also boost competition within the financial system, because new competitors, like fintechs, are stepping onto the field. What some of you might regard as a threat to your business – because it could intensify the problem of narrowing profit margins among traditional banks – has, on the other hand, a positive impact on overall welfare.

The question of whether digitalisation will lead to a revolution in financial services and infrastructure, as some commentators argue, remains unanswered for the time being, in my view. However, one certainly can't deny that new technologies like blockchain, robo advisors or crowd funding could have the potential to make financial markets and services faster, more efficient, more convenient, and more inexpensive for everyone.

This is why some central banks are carrying out research, especially with regard to the implications of blockchain technology. And the Bundesbank is among them.

To identify the requirements which central banks might need to meet in future in connection with blockchain-based instruments, the Bundesbank and Deutsche Börse AG have jointly unveiled a prototype for a securities settlement system based on blockchain technology. The idea behind this joint project is to analyse the technological performance and scalability of blockchain-based applications. It is not the intention to issue a digital euro coin.

New technologies may also represent a source of financial stability risk. Herding behaviour, for example, could be amplified by automated advisory services in portfolio management. Robo advisors might exacerbate financial volatility and pro-cyclicality if the assets under management reach a significant level, which is not yet the case.

Pro-cyclicality might result from weaker customer relationships and the interoperability of access points.

This calls for the regulation of fintechs, at least to a certain extent. A lot of corporations using technology-enabled financial innovations operate either on a global scale or carry out a large number of cross-border transactions. Identifying key regulatory issues to safeguard financial stability is therefore a goal that the German presidency is aiming at in cooperation with the Financial Stability Board and other standardlsetting bodies.

Another pressing issue in a digitised world is cybercrime. Cyber-attacks can potentially undermine peoples' trust in the financial system. In order to avoid jeopardising the positive impact of digital finance, it will be crucial to address these cyber risks. It is therefore on the Baden-Baden agenda to start work in this area at the G20 level.

A further implication of digitalisation, which was already an important topic at the G20 digitalisation conference in Wiesbaden, in January, is financial literacy.

It is an indisputable benefit that new technological developments have enabled the financial inclusion of people who would otherwise lack access to financial services – for example, there are five countries in Sub-Saharan Africa where more people have a mobile money account than a conventional bank account.

That said, more and more people with insufficient knowledge and understanding of financial concepts and risks are getting easier access to financial services. And this is true not only for developing countries but for industrialised countries, too.

If it becomes easier for people to become their own “fund manager", so to speak, they should at least have basic knowledge of economic concepts like compound interest. Therefore, financial literacy is not just an issue for consumer protection authorities, but also for schools and the financial industry as well.

For central banks, financial education is an issue, too, because effective monetary policy communication relies on people having a basic grasp of concepts such as inflation and interest rates. Ensuring the public has basic knowledge of these issues is therefore important for the success of central banks, as the ability of the latter to maintain price stability depends, not least, on public support for a stability-oriented monetary policy.

Ultimately, all of us should have an interest in consumers being well-informed about financial services.

In addition to the key topics I have mentioned, Germany will also be continuing the G20 agenda in a number of other fields. This includes a further strengthening of the international financial architecture and additional progress on the international regulatory agenda.

3. G20 achievements

Ladies and gentlemen

What are the greatest achievements of the G20 so far?

In my view, there are two.

The first is that the G20 member states by and large resisted temptations to implement protectionist measures to stimulate their national economies after the great recession in 2008/09. “Beggar-thy-neighbour” policies were not chosen to improve the economic situation at home at the cost of other economies.

This success was due, not least, to the explicit rejection of protectionism by the G20 and the renewed commitment to an open, global economy.

The other great achievement of the G20 is that, through common efforts, important lessons were drawn from the financial crisis.

All the milestones of regulatory reform were endorsed by the G20. The tightening of bank regulation under Basel III, for example, would hardly have been imaginable without the political support of the G20.

It’s now all the more important that these achievements are not given up.

Open markets and a competitive economic system are the pillars on which the prosperity of our economies rests. A greater variety of inexpensive and good-quality products are available on open markets, and this increases citizens' purchasing power. In this way, free trade and competition result in a quantifiable increase in prosperity, particularly for those who have to consider their spending carefully. Moreover, spurred by international competition, industries are more innovative and new ideas are spread more rapidly.

But today we are seeing mounting scepticism of globalisation, a sentiment by no means confined to the United States. In Europe, too, globalisation fears are on the rise and people are increasingly shunning open markets. According to a recent poll, 45% of Europeans view globalisation as problematic, and among the voters of populist parties more than two thirds see globalisation as a threat.

Public concerns like these need to be taken seriously. It can't be denied that globalisation puts particular pressure on certain groups of people. Although open markets boost prosperity overall, they don't necessarily boost it for all people all of the time. But it's also safe to say that barriers and exclusion would be the wrong response to these concerns.

In advanced economies, low-skilled workers feel the pressure of globalisation, particularly those who work in industry sectors that are exposed to low-cost competitors from abroad. And that's why inclusive growth is so important.

In order to have more inclusive growth, however, we need to ensure that enterprises and their employees are properly equipped to harness the opportunities presented by globalisation and technological progress and that they are able to manage structural change.

I already mentioned the need for a favourable business environment. That means, for example, less red tape, limits to increasing social-security contributions or creating innovation-friendly conditions by an efficient product market regulation.

Investment in education and lifelong learning are important for improving employees' adaptability to a changing environment. People who lose their job have to be able to find another position swiftly.

And a targetIdriven and transparent tax and transfer system is able to act as a cushion for those who are not able to benefit from new job creation. Policy must help those who lose from globalisation, and the positive effects of trade should provide scope for such policies.

Regarding the second great achievement of the G20, I am somewhat concerned, too. While, on the one hand, the regulatory agenda has not been completed yet, calls for de-regulation are on the rise again.

I already mentioned Basel III. I'm fully aware that the implementation of the new standards is challenging for banks worldwide. But the new standards have significantly improved the capital adequacy of the banking system and have made the global financial system more stable. And although banks sometimes criticise the higher capital requirements, a more stable financial system is beneficial for them as well – as greater stability is also reflected in lower funding costs.

Nevertheless, in contrast to the original plans, there was no final agreement on Basel III last year. While most of the residual work has been completed, one important issue still remains unresolved. This is the question of how far credit institutions should be permitted to use their own internal models to determine their capital adequacy requirements for credit risk – or to be precise, whether to fix a lower threshold for capital adequacy requirements calculated with the aid of the internal model and if so, how to calibrate this threshold.

The negotiations on that issue are currently on hold because the positions of the US chief negotiators have not yet been filled. A swift resumption of negotiations would be in our common interest, especially as the ongoing regulatory uncertainty caused by the delay in finalising Basel III is undoubtedly a burden for the banks.

And so I hope that the upcoming meetings in Baden-Baden and Basel will lead to a return to the negotiation table.

Ladies and Gentlemen

One lesson of the financial crisis was that banks, especially the global systemically important ones, need more capital. The second lesson was that public bail-outs of banks should be avoided in future.

And so it is completely understandable that President Trump recently declared, in his executive order of 3rd February, that the prevention of taxpayer-funded bailouts is a core principle of regulation.

That said, achieving this aim also makes it essential to refrain from adopting regulatory measures which would make public bailllouts more likely or which would destroy the level playing field.

Thus, I fully agree with Mario Draghi, who recently said that “the last thing we need at this point is a relaxation of regulation.” That does not, of course, exclude us from regularly evaluating our regulation and its effectiveness and fine-tuning it if necessary. But the G20 should stick to its commitment to regulatory reforms and its clear rejection of regulatory arbitrage.

Carrying out deregulation in the hope of stimulating the economy could backfire. Insufficiently regulated financial markets can do significant harm to economic prosperity if a crisis occurs, as the latest financial crisis has painfully demonstrated.

Back in 2013, the then Secretary of the US Treasury, Jack Lew, said that “(…) the global financial crisis (…) underscored the need for strengthening financial sector regulation across the globe. In particular, the crisis highlighted the need for building much stronger and more resilient financial institutions, greater market transparency, and a high quality level playing field across borders that protects against regulatory gaps, arbitrage, and a race to the bottom."

I think this is still true.

4. Conclusion

Ladies and gentlemen

On this note, I would like to bring my speech to a close.

In times of uncertainty, international cooperation is particularly important, and we are certainly living in a period of heightened uncertainty at the moment.

In times like these, the G20 is a precious treasure. The German presidency is seeking to guard this treasure and ensure its value is further enhanced.

Thank you for your attention.