

# François Villeroy de Galhau: Beyond Brexit, our common challenges and our common answers

Speech by Mr François Villeroy de Galhau, Governor of the Bank of France, at the City Week 2018, London, 24 April 2018.

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Ladies and Gentlemen,

It is a pleasure to be in London again and allow me to thank you for inviting me to speak

at City Week 2018. As is to be expected, Brexit is omnipresent on the agenda. But, as the Belgian friar Dominique Pire said when he received the Nobel Peace Prize in 1958, “men build too many walls and not enough bridges”. That is why I am not going to speak about what divides us, but rather about what unites us. We are and will always remain close friends and partners, even if we will no longer be in the same European club. Today I will elaborate on two challenges that should unite us in the near future: the utmost need for active multilateralism and the finance of tomorrow in an interconnected world.

## 1. The need for active multilateralism

International cooperation between countries is more important than ever to preserve

the current improvement in the global economic environment: according to the latest IMF forecast, global growth should stand at 3.9% in 2018, after 3.8% in 2017. And we should together resist two temptations: financial complacency, and protectionist escalation.

On the financial sector, beyond the European Union’s borders, and with all our partners, we have to strive to maintain the collective rules of the game that we have put in place since the G20 summit of London in 2009. Nine years later, some actors may be tempted to have short memories and forget the lessons of the crisis. But diluting financial regulation would pave the way for the next financial crisis. So we must now be firmly committed to the “full, timely and consistent implementation” of Basel III, as successfully agreed last December and stated in the last G20’s Buenos Aires communiqué. Neither the United States today, nor the United Kingdom tomorrow, should take the path of unilateral deregulation, and we welcome their commitment. Evaluation and simplifications are obviously possible, under the common FSB umbrella: but regulatory competition would be nothing less than a lose-lose scenario with disastrous consequences.

However, we are not done with financial regulation yet. We still have to finalise ongoing initiatives, especially on shadow banking. Indeed, the regulatory priority is no longer the solvency of banks, but the liquidity of non-banks: we stressed these financial stability risks in our Washington meetings last week. Tomorrow, we at the Banque de France will publish the 2018 Financial Stability Review that is focused on fast-growing market-based finance.

I stress that we have to better monitor it, test it – through liquidity stress-tests –, and regulate it when necessary.

Financial stability is our common good, and we should also face a more subtle threat to it: debt complacency on a global level, in the context of accommodative monetary policies which will be less warranted in the near future. Global debt was already about 200% of world GDP before the crisis (2007), but is up to 220% today. Sound fiscal policies for public debt, responsible lending by financial actors for private debt and – if needed – macroprudential measures, should react against this debt complacency.

More broadly on multilateralism, we should continue to work together to preserve the world economic and trade order. We Europeans, shoulder-to-shoulder with Canada, Japan and others, must resolutely defend international economic relations based on commonly respected rules and multilateral institutions: we are all aware that an escalation of protectionist threats from the United States would dampen growth everywhere. The recent uncertainty is probably already having some negative effects on investment: you saw it in the British economy since the Brexit vote in 2016. And real tariffs would hurt more: according to most calculations including ours, a 10% increase in tariffs would diminish world trade by double digit figures, and decrease global GDP by more than 2%, starting in the United States.

## 2. The finance of tomorrow

Let me now turn to my second point: the finance of tomorrow in an interconnected world.

Let me first remind you that France and the United Kingdom have already developed a similar – and I believe promising – approach to regulating innovation. Call it “proportionality” in Paris or “sandbox” in London. But it is the way of solving an apparent paradox: for many, regulation is the enemy of innovation. In fact, regulation has a role to play in order to boost and secure innovation at the same time. To give an example, by allowing third parties to safely access payment data, the revised European Directive on payment services (PSD2) is a significant driver of innovation. More broadly, since its creation in 2016, around 300 Fintechs have been guided by France’s ACPR Fintech Innovation Hub.

There are so many promising innovations which will increase customers’ satisfaction, enhance competition and reduce costs. And clearly each of them – from big data to payment services – requires a specific monitoring and response by regulators, with an open and evolutive view. “One size fits all”, and “one time seizes all” would be two bad answers to financial innovation. Let me however share some thoughts on four common challenges and opportunities: cyber risks, crypto-assets, artificial intelligence and climate change.

**Cyber risks** are a major threat, and so investing in cybersecurity is the first booster to innovation. It is clear that the current level of coordination of cyber-attacks can only be mitigated by a similarly coordinated response. We should strengthen the G7 Cyber expert group, and the “Bari principles” adopted last May. Therefore I welcome the creation of a G7 group dedicated to cross-border cyber exercises, and I confirm today that the Banque de France will coordinate the G7 test in 2019. Cybersecurity will indeed be one of the priorities of the forthcoming French presidency of the G7 next year.

Besides cyber risks, we need to seriously deal with the emergence of **crypto-assets**.

The underlying technology clearly promises sustainable innovation. The Banque de France was the first central bank to offer a service to the market based on blockchain and we intend to carry on experimenting with this technology. But support for blockchain doesn’t mean blind support for bitcoin and the like speculative assets. We were clear in the G20 last month, and let me be clear today. First, the frequent use of the term “digital or virtual currency” misleads the general public on what those assets really are: they are not currencies, with none of a currency’s key functions – store of value, medium of exchange, unit of account. Moreover, crypto-assets carry obvious risks in terms of consumer and investor protection, as well as money laundering and terrorist financing. Therefore they require internationally harmonised answers: the Financial Stability Board, in consultation with other standard-setting bodies and the Financial Action Task Force (FATF), should make recommendations by next July. In particular, we should work on exchanges and platforms which provide services at the interface between crypto-assets and the real economy.

From a more prospective point of view, **artificial intelligence** (AI) will be among the most

impactful technologies in the financial industry for the upcoming years:<sup>1</sup> up to 30% of major French banks' projects in current development are heavily focused on AI and the potential for insurers is equally huge both for the traditional damages insurance as for life insurance products. The expected benefits of AI in customer relationship and risk management are numerous: we don't know the limits, and we shouldn't be frightened of AI. To allow its wider use in a secured way, we have set up a Task Force on AI, led by the ACPR and gathering all relevant industry representatives. And I already stress that we have to collectively implement at least three core principles: (i) promoting a greater understanding of algorithms to avoid the 'black box effect'; (ii) ensuring a sound governance of AI-based systems; (iii) fostering an ethical use of data so that bias-free AI applications promote inclusiveness.

Last but not least, **green finance** represents a new frontier for the 21<sup>st</sup> century for us as central bankers and supervisors. One of our priorities is to better measure the long-term risks associated with climate change: we need both a "snapshot of the risks" – namely the identification and disclosure of exposures – and a "video of the risks" provided by forward-looking carbon stress tests. But we also intend to develop the huge opportunities related to the financing of the transition towards a low-carbon economy – up to USD 90 trillion are needed till 2030 –, while preventing the risk of "green washing". It would certainly make sense to promote a convergence towards a harmonised European standard for green bonds – including UK –, leveraging the Green Bond Principles approach in terms of processes and transparency, and building on the Climate Bond Initiative approach with regard to taxonomy. Much has to be done in the coming years. In that regard, I am very happy to count the Bank of England among the founding members of the Central Banks and Supervisors Network for Greening the Financial System (NGFS) that was launched by the Banque de France last December. This is an enthusiastic and rapidly developing "coalition of the willing": the nine founding members should shortly be joined by three new members and two observers: the BIS and the OECD. Several other major central banks and supervisors are on the verge of applying.

Stephen Hawking once famously said about the Internet: "We are all now connected [...] like neurons in a giant brain". This could also apply to the finance of tomorrow in an interconnected world. Each of us – whether regulators or professionals – is at least a neuron; we need to be connected to other neurons to produce innovative ideas. Similarly, no country or financial institution can adequately respond to the challenges of this changing world on its own: we must definitely join our efforts to build our future. Thank you for your attention.

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<sup>1</sup> ACPR study on the digital revolution in the French banking and insurance sector, March 2018.