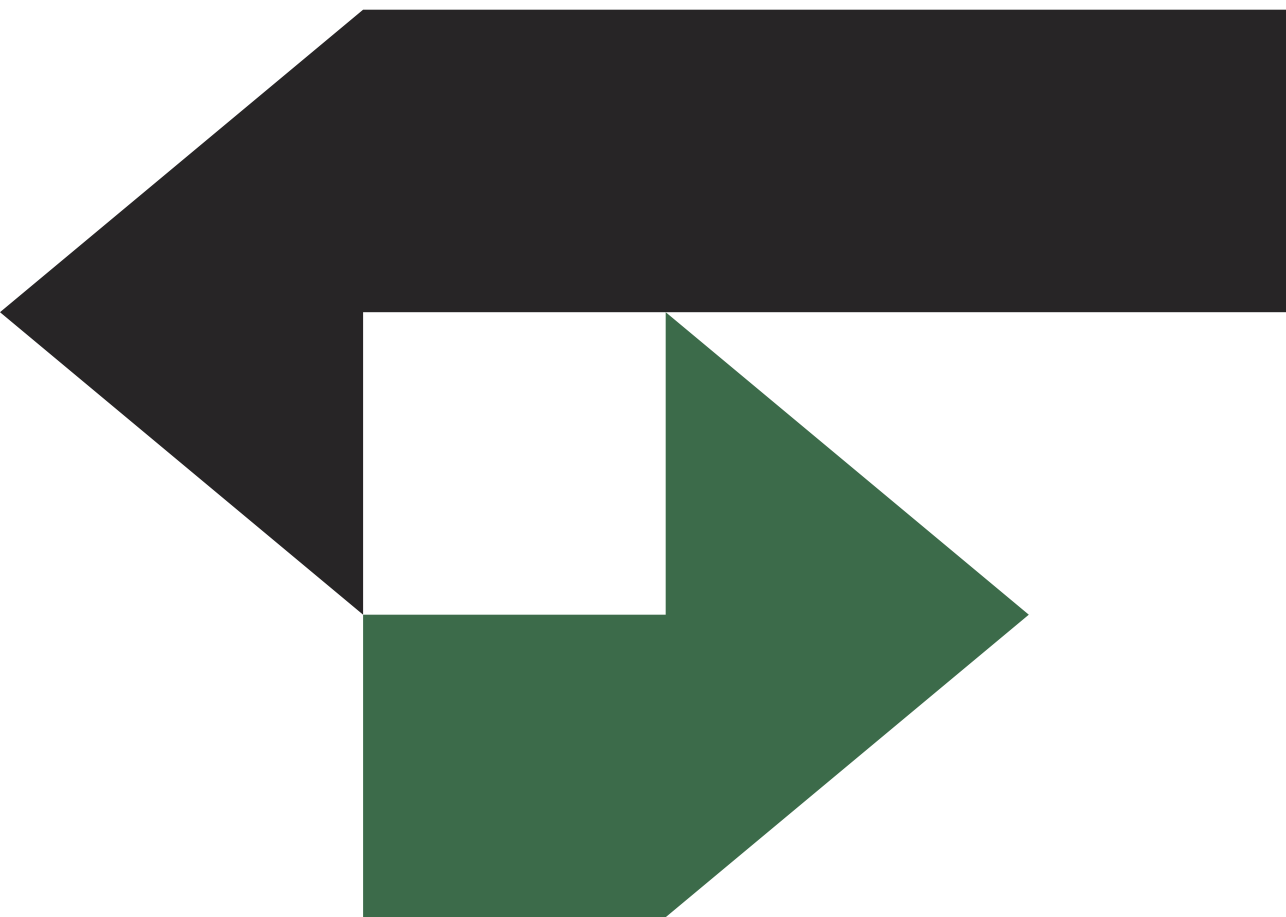


FINANCE FOR GROWTH IN LONG-TERM EUROPE

ADVANCING INVESTMENT,
SUSTAINABILITY AND REFORMS

PAOLO GARONNA (ed.)





60th Anniversary of the Rome Treaties. Family picture (Rome, 25 March 2017).



60th Anniversary of the Rome Treaties. Joint statement by the banking, insurance and finance communities of the six countries signatories to the Treaties (Rome, 3 April 2017).

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Finance for Growth in Long-Term Europe

Advancing Investment, Sustainability and Reforms

Paolo Garonna (ed.)

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PREFACE

Paolo Garonna*

“The problems that our countries need to sort out are not the same as in 1950. But the method remains the same: a transfer of power to common institutions, majority rule and a common approach to finding a solution to problems are the only answer in our current state of crisis” (Jean Monnet, *L'Europe et la nécessité*, 1974)

EUROPE IS BACK

The European economic policy environment in 2017 has registered a significant upturn. The gloomy prospects foreseen until recently have given way to a return of confidence and a burst of self-esteem and determination.

Part of the change is in the perceptions, the popular mood and the expectations for the future, as the worst scenarios daunting the aftermath of past shocks did not materialize. But there is more to it. The economic recovery has picked vigour and spread broadly across the continent. The financial sector appears in a much stronger shape after the thorniest legacy issues have been addressed. Investment growth has turned positive and accelerating. Also, the labour market is showing fledgling signs of improvement. The geo-political risks linked to European elections have subsided.

All this looks obviously reassuring. After all, Brexit, while still looking threatening and obscure, did not open the way to the disintegration of the EU. And the new Trump administration did not pull the sprint to emboldened nationalism, protectionism and anti-establishment attitudes in Europe. Fears created by terrorist attacks, illegal immigration and global war risks have contributed positively to raising awareness of the seriousness of the matters at stake, and to seek a new sense of responsibility and a more enlightened leadership in the “old world”.

The common sentiment prevailing now can be summarized in the following propositions: the European agenda must move on; concrete and practical solutions must be found on the most urgent questions; this will require a compromising attitude, give and take and a mind-set open to innovation; the time has come to make it work, correct the worst imbalances, and prepare for the future. European leaders, be it in

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governments, European institutions, business, financial intermediaries, all stakeholders, and the citizenship at large, must be capable to work together, share the burdens of change, and deliver on what peoples basically need and expect of them.

An unprecedented window of opportunity has been unlocked. It must be filled with content, substantive planning and priorities, so that we can move on swiftly to concrete action and deliverables.

“FINANCE FOR GROWTH” IS FINALLY WORKING

“Finance for growth” is a relatively new approach to policy making in Europe, which has been at the centre of the discussions and policy analyses of the previous editions of the Rome Investment Forum since the end of 2014. Until recently, this new concept, though innovative and promising, had remained elusive.

The idea that reforms and development in the financial sector should drive a new phase of economic development in Europe had gained increasing traction and support in official circles. But how this policy approach would translate in more growth and jobs, better functioning markets and more cohesive societies, proved to be quite hard to demonstrate and, even more, to secure the support of public opinion at large. Above all, concrete outcomes were missing, and the recovery seemed to drag on by-and-large fragile and uncertain.

In theory it looked plausible that a more stable integrated and developed financial sector could substantially contribute to striking a better balance between security and innovation, stability and growth, and help produce a healthier and more cohesive European integration process. But in practise... Has it worked? Can it work? At times, it seemed more a gamble than a calculated risk taking. And then came Brexit, making financial development even more haphazard, and putting into question the future itself of European finance.

But now the wind has changed. Moreover, it is blowing in the right direction. “Finance for growth” has started to respond to expectations and deliver on its promises. After the stagnation of the previous period, outstanding bank credit to non-financial enterprises has had a significant revival since 2015. This reflects among other things the healthier conditions of the banking sector, which is more capitalised, with better asset quality and a stronger balance sheet. Concerns for the high stock of Non-Performing Loans (NPLs) have receded, considering the improvements underway, well above expectations. The most difficult components of the legacy question, particularly after the pragmatic decisions of June and July 2017, appear to be behind our shoulders. This rosier picture is completed by recovery in profitability and better quotations on the stock exchange. So, Banking Union is showing resilience and vitality, and it is starting to take hold. Capital Markets Union is also gradually moving on, after taking stock of the terrible shock of Brexit. There is a growing awareness of the importance of providing alternative sources of financing for SMEs and infrastructure projects, and the first signals are emerging of shifting practises: minibonds, IPOs, fintech, venture capital, securitization, etc. In the mid-term review

of the Action Plan, it is shown that 20 out of the 33 actions envisaged there have been completed, while the others are well underway. Above all, the Plan has been revamped and adapted to account for the likely impact of Brexit. The CMU response to the formidable challenge has meant more determination and more ambitious goals, including in the fields of taxation (the debt equity bias), insolvency legislation, proportionality and the strengthening of the supervisory authorities.

As far as investment is concerned, the Juncker Plan is making progress, fully on schedule in its implementation. Moreover, the Plan has been expanded and extended, banking on the growing recognition that it represents a cultural shift in the approach to bridging the investment gap and in the relationship between public funding and the market.

In sum, in the last period we have seen an intensification of policy efforts for financial reform both at national and European levels, and at the same time a marked improvement in the economic outlook, with an economic recovery that appears not only more robust and wide-spread, but also more consistent with fundamentals, and therefore more sustainable. Moreover, the two trends seem to amount to more than a simple correlation. A causal relationship linking financial development and economic growth can be argued, in line with the “finance for growth” philosophy, even though more data, and time, will be needed for getting a full proof.

A NEW POLICY ENVIRONMENT: EUROPE'S ADULTHOOD

The European awakening is taking place in a policy scenario that is undergoing profound changes and facing unprecedented challenges. The Global Risks Report of the World Economic Forum at the beginning of 2017 showed remarkable foresight in anticipating the major challenges of the year: extreme weather events and natural disasters, large-scale migration pressure, terrorist attacks, cybercrime, and social and political polarization. To make the picture bleaker, add war and instability, the threat of nuclear confrontation and the growing appeal of protectionism.

Turmoil and disruption inevitably generate chain reactions that may lead into positive or negative directions depending among other things on the clear thinking of leaders and the maturity of the public opinion. On both scores, the response coming from the “old world” has been reassuring, and promises well for the future. The wave of electoral outcomes in significant European countries dispelled the scourge of populist uprising and triumphant anti-establishment coalitions. During 2017, the perception of geo-political risk affecting the economic and social landscape in Europe improved significantly. Many commentators and forecasters attributed to changes in geo-political risks the major responsibility for the substantial upward revisions in confidence and economic growth estimates that have been issued by the major sources of economic forecasts (e.g. the IMF).

European peoples and their leaders are gradually realizing that major discontinuities are taking place in the global exchequer. Not only in terms of the scale and depth of the challenges we are facing, but also, and above all, in relation to the new

players, and the traditional partnerships and alliances we have been counting on all along the post-war period. It is undoubted that these alliances and partnerships have represented one of the major factor underlying the long period of peace stability and prosperity Europe, and the developed world, has enjoyed. These discontinuities have created fears and uncertainty, but also a new sense of resolve and adulthood. It is not easy for instance for the 27 EU member countries after Brexit to come to terms with the fact that, at least for the time being, they have to give up the belief that they can count on the British to provide leadership, economic and social models, best practise and inspiration in the process of European integration. This has obviously a lot to do with the key role that London has plaid, and even more could play, in a fully functioning European Capital Markets Union. But it goes well beyond. It calls into question the primary role that Britain has plaid in projecting a pro-market, liberal, empiricist and “open society” culture into the European construction. From now onwards, continental Europe will have to do without it. And it will be a big loss. The UK will be looking inward, searching for a redefinition of its identity and mission, and its relationship with Europe, and the world.

Likewise, the US superpower appears vulnerable and polarized, uncertain on how to accomplish its role of upholding freedom and democracy in the world. For the first time in its recent history, the U.S. probably will not be able to act as a catalyst for European integration, as a guarantee of peace and stability at the regional and global level. The Europeans will have to do more for their defence, for safeguarding their competitiveness in the world economy, for promoting a rules-based free trade and investment system, for fighting terrorism, and addressing the challenges and conflicts arising in their “near abroad”, from the Middle East to Russia, from the Gulf to Africa, from the Euro-Mediterranean to Central Asia.

Europeans therefore have entered adulthood. They must take in their own hands their destiny. They must invest more in foreign policy, multilateral and bilateral cooperation, and defence. They will have to take responsibility and fight for maintaining and enhancing the global trade system, managing demographic pressures and technological change, cooperating for conflict prevention and resolution, climate change and the environment, democratic values and the rule of law. They will have to be more effective in fighting against terrorism and patrolling their common borders. Orphans, but heirs, of the fundamental Anglo-Saxon and transatlantic roots of the European ethos.

It is a quantum change, and a heavy burden to carry. But European leaders seem to have understood the lesson, and perceived what and how much is at stake. A window of opportunity is there, and should be exploited. Moderatism, vision and determination are the key words of mainstream European politics, and the future of Europe figures prominently in their programs. Public opinion seems overall to follow suit.

“IL TEMPO È GALANTUOMO” “TIME IS AN HONOURABLE MAN”

“Le temps retrouvé” is the seventh and last volume of Marcel Proust’s masterpiece “In search of lost time”. Marcel, the protagonist, comes to term with his past, and discovers that things acquire with time a different and more profound meaning. The equivalent say in English is: “Truth is the daughter of time”. Many commentators thought that the time elapsing from the British referendum to the various elections (until the German one), covering the most part of 2017, would be wasted, since no major decision could be taken at the European level. The various consultations, green papers, opinions and conventions would be mere stopgaps, useful only to gain time. I admit I was thinking along those lines myself. I felt the sense of urgency was missing for adopting a few measures that were necessary to accelerate the transition, complete the Banking Union and fix the Euro.

We were wrong. The time spent discussing the future of Europe has not been lost. It was precious, and did contribute significantly to the change in the policy landscape. There has been a considerable mobilisation of minds, energies, resources and institutions around this topic with contributions from academics, think-tanks, business, political parties and institutional players. It was felt that the question had a burning impact on everyday’s life and the future of ordinary citizens. The process itself generated ownership and participation. Populist, anti-EU and nationalist rhetoric were muted, and understood that the popular sentiment versus Europe, even in the most rebellious anti-establishment quarters, should not be taken for granted and exploited with impunity.

The discussion is still raging, and has produced a host of visionary and practical suggestions, with various degrees of ingenuity feasibility and wisdom. It is probably still early day to try to distil agreed structured programs out of it. But the general sentiment that is accompanying it has already been reaped, and has produced a significant environmental benefit. With three unambiguous indications: on, sustainable and multi-speed.

On. “Adelante Pedro, con juicio”. The European integration process must go on. There is no alternative. With gradualism, pragmatism, but without any hesitation. Only a more integrated Europe can be more authoritative and effective in pursuing her citizens’ interests and her mission in the world.

Sustainable. Europe, like Rome, was not built in a day, and will not. A long-term vision and plan is needed, and steadfast determination in moving on step by step.

Multi-speed. This principle is now accepted, has been elaborated upon by official statements (lastly the State of the Union address in 2017), and applied in practise in several occasions. Nobody should be left behind if she is willing to participate. But no-one should have a veto power, and impress to the process the speed of the slowest wagon.

These conclusions may look vague and abstract. But they respond firmly to opposite principles, and practises that were taking roots in the European narrative of the past. A strong reaction to: “we have gone too far, too soon”; “from one quick fix to the next”; resignation to the paralysis imposed by the laggards.

Ambitions therefore must be set up at the level that is required by the challenges and the demands of the citizens, not what bureaucracies and national politicians think is realistic. This puts on top of the list issues on which governments have been recalcitrant for a long time, and progress has been lacking. Defence and the common fight against terrorism. Illegal immigration and the common control of the Schengen borders. Relationships with our close neighbours, from Russia to Turkey, from South Eastern Europe to the Mediterranean. A European budget sufficient to provide backstops to the Economic and Monetary Union, anticyclical buffers against asymmetric shocks, and support for filling the investment and infrastructure gaps that drag down the growth potential in Europe.

THE AVOIDABLE CLASH BETWEEN THE DESIRABLE AND THE ABSOLUTELY NECESSARY

We should not expect, neither wish, that the exciting discussion on the future of Europe finish quickly, and that we move then quickly to action. This discussion is here to stay. It is not only a means to an end, but it is a policy objective in itself, because it engages all the relevant players, including the citizens, in an exercise of democratic participation and institution building. It prepares the ground for a new social contract, and fills the gap between Europe and the people, the local communities and the European techno structures, the contingent pressures and the construction of the future.

The dialogue on the future of Europe should be continued, extended, deepened and made more systematic. The financial community should not only be an active participant in this dialogue, but a promoter and a leader, in line with the “finance for growth” philosophy. It should be also understood that some of the agreed solutions that are emerging do not lend themselves to easy and quick implementation. Take the question of Brexit, which, as much as all would like to reach right away clarity and pragmatic solutions, will require deeper understanding, imaginative compromises and a long digestion of the practicalities involved. Defence will require close coordination with NATO, a new relationship with the UK and, in my view, with Russia. Support for Africa implies a new focus on our “near abroad” in the Mediterranean and South East Europe, a reappraisal of the EU enlargement prospects, and a leap forward in the common foreign and security policy. The most ambitious proposals for fiscal Union, the ones requiring debt mutualisation, large-scale income transfers and risk sharing will not pass unless a climate of mutual trust can be restored, and the fear of moral hazard can be neutralised; which once more will take probably time, and persistent mutual engagement. The long view is Europe’s best ally, and dialogue her most powerful tool.

But long-term Europe cannot afford to become complacent with the short-term dangers and vulnerabilities that confront us. Instead, it is exactly in the present favourable environment that we find the best opportunity for tackling the structural weaknesses and imbalances, which are still there and must be addressed. This opportunity should not be missed. It requires to act quickly and boldly to maintain and repair the most serious faults in the structure.

STRUCTURAL WEAKNESSES IN THE EUROPEAN POLICY FRAMEWORK

The past crises have clearly shown where Europe is most vulnerable. They also offered indication on the required adjustments. Therefore, the diagnosis of what does not work and must be fixed is not new. The needed therapies are also well known. As a matter of fact, following Jean Monnet method, after each stage of the crisis, a pragmatic response has been found and swiftly acted upon. European integration has made progress in this way: as a pragmatic reaction to crisis. Think for instance how, after the peak of the sovereign debt crisis, the Banking Union was agreed upon in order to break the vicious bank – sovereign debt circle. Think also of how rapidly the Banking Union new institutional framework has been set up and made operational, including the most delicate shift from the bail-out to the bail-in principle; which amounts to a “cultural revolution” not only in banking practises, but above all in the investors’ perception of risks (particularly at the retail level).

However, the response to the past crises has not been complete and thoroughgoing. It is still unfinished business. This has repercussions in the functioning of European institutions, and in the economic performance of the Union. I refer in particular to the Economic and Monetary Union that from the start was supposed to require comprehensive reforms in order to function properly.

Four aspects come to the fore:

1. The persistent fragmentation of the financial services single market, in spite of the Banking Union
2. The asymmetric and uncoordinated adjustments to common shocks
3. The lack of a central demand management and stabilisation function
4. The insufficient economic convergence of national economic performance

European banks still operate in a fragmented market, with great obstacles to cross border operations and very limited capital flows between EU countries. Cross border banks face additional burdens in terms of liquidity and capital requirements. In spite of the Single Supervisor and the single rule-book, and with a common currency, banks still operate in multiple jurisdictions, where there are significant national discretions and different practises in implementing banking rules. We are far even from recovering pre-crisis level of cross-border market interconnection. Lack of a single Europe-wide capital market prevents risk-sharing through debt and equity, creating bottlenecks of liquidity and affecting the transmission channels of monetary policy.

A single currency requires symmetric adjustments between surplus and deficit countries, determining otherwise economic and political tensions and a deflationary bias in economic policies. In other terms, with a single currency, restoring relative competitiveness requires symmetric adjustments in terms of internal devaluations, real wages and labour costs, structural reforms. Otherwise, one would need federal transfers and sufficient fiscal capacity to maintain cross-border flows and cushion asymmetric shocks (this is the case of the U.S.). So far economic policy coordina-

tion has not been able to achieve consistency and burden sharing in the adjustment to the economic cycle.

Forcing economic convergence through fiscal constraints as in the Stability Pact has not worked. For two reasons. First, because the rules of the Pact were not applied strictly, neither on deficit nor on surplus countries. But also, and more importantly, because when the rules – due to market pressures – became more stringent (as for instance in occasion of the sovereign debt crisis), the asymmetric adjustment meant that the correction was severely deflationary and created a double dip recession. Where austerity failed, flexibility accompanied by economic reforms enabled a more balanced recovery. But the adjustment was slow and painful, much more than necessary.

FIXING ECONOMIC AND MONETARY UNION: AN URGENT TASK

The outcome of these persisting structural deficiencies is that in the common currency area economic convergence is not taking place. On the contrary, the current imbalances – not matched by effective adjustment mechanisms – create in-built disincentives to convergence. The bottom line is that the Euro-zone remains a sub-optimal currency area, a fragile environment that – if not fixed – would not be sustainable in the long-run, and would fail to withstand the impact of a future crisis.

This vulnerability, which the markets are now ignoring, but know very well, must be corrected. It does not concern the optimal design of Europe's future, for which there is time. Rather, it is a matter of urgency sustainability and crisis prevention. Therefore, it should be faced up to with that frame of mind. As an absolute priority.

What does it take? In a few words, the completion of the banking union, with the final breaking of the bank sovereign nexus, and a significant advancement in capital markets union enabling private sector risk sharing. It also requires the provision of fiscal backstops and some form of stabiliser in relation to asymmetric shocks. It requires strengthening economic reforms at national level in both deficit and surplus countries.

Does it take bold and painful decisions? Yes! And No! Yes, because the additional measures imply a transfer of prerogatives and sovereignty at the European level. No, because those measures can be made consistent with a framework of minimum further integration, no additional permanent transfers (no transfer Union) and no debt mutualisation.

It requires from political leaders a full understanding of the technical aspects, and an appreciation of the difference between what would be desirable (but can wait) and what is necessary (that cannot wait).

Above all, it requires the political determination to do it, i.e. to do “whatever it takes” to achieve it. This will most likely imply give and take, pragmatic compromises. It means reconciling conflicting interests in the name of the superior exigency of safeguarding the Euro. It means understanding the value of the Euro for the stability of financial markets, economic growth and jobs, and its political significance.

“THE CHALLENGES ARE GREATER THAN IN THE PAST:
FURTHER PROGRESS IS NEEDED” (M. DRAGHI)

We conclude these introductory remarks with a quote from the ECB President Mario Draghi, who well captured with his words the *Zeitgeist* of our epoch.

“This year marks the 60th anniversary of the Treaty of Rome that created the European Union and the 25th anniversary of the Maastricht Treaty that created the Monetary Union. Further progress is needed. The institutional architecture of the Economic and Monetary Union remains incomplete in a number of aspects. The crisis has exposed structural weaknesses in our construction and has forced us to address them. The repair has started with the creation of the Banking Union. But the work is far from over and the challenges we face go beyond Economic and Monetary Union. They pertain to security, migration, defence, and generally all those challenges that can be addressed only by pooling sovereignty. And these challenges are greater than in the past. Today we can sense a rising wave of energy in demanding joint European action. The European Union and the euro always commanded the support of the majority of European citizens, but, often, it was only the vocal opposition that was heard. Now, this silent majority has regained its voice, its pride, and its self-confidence. Only by working together can the nations of Europe overcome these challenges. The opportunity for progress is real.” (Speech at Tel Aviv University, 18 May 2017)

FINANCING LONG-TERM EUROPE

This volume collects a series of essays, essentially drawing on the contributions to the International Conference that took place at the end of 2016 in Rome, the Rome Investment Forum. The perception then, and now at the time of publication, is that Europe, and the world economy is at a turning point. The reasons are many, and relate to a set of different and interacting coordinates: geopolitical, social, institutional, regulatory and economic.

After a decade of gloomy and erratic performance, the European exchequer has shown a new vitality, and promises to provide an anchor of moderation and hope for its citizens, its neighbours, and a growingly unsettled world.

“Finance for growth” has been the leit motiv of the Rome Investment Forum in its different editions from 2014 onwards. This concept has come to encompass the many dimensions of policy efforts aimed at a better balance between stability and development, innovation and security, continuity and change. Finally, “finance for growth” has started to work, after proving rather elusive in the past. The European recovery is more robust, widespread and consistent with fundamentals. The vicious circle between austerity and depression has been broken. The dichotomy between core and periphery appears less acute. The resilience of European institutions, markets and society, has passed the test of unprecedented stress: from Brexit to unfo-

reseen developments in American leadership. The world of finance appears to-day more able to play its role of bridging savings and investment, supply and demand, merit and need, the present and the future.

The challenges however are daunting. Mainly because, while sailing through unchartered waters, the “European project” itself has appeared at times uncertain and fuzzy. It is in any case unfinished business.

The essays in this volume give evidence that there is finally a new policy environment, a new vision and sense of responsibility, from the point of view of a prominent group of business leaders, policymakers and international stakeholders. Moreover, they contribute ideas with the aim of moving on the reform agenda in the business and policy context, at national and European level.

A new policy environment in Europe. In response to unprecedentedly serious challenges, there is greater determination to face up to the backlog of unresolved contradictions: fixing the Euro, completing the Banking Union, advancing the capital market union in a post-Brexit perspective, extending the Investment Plan (Juncker Plan) to the Euro-Mediterranean, reforming Schengen and Dublin, etc.

A new vision of the future of Europe. A lively discussion is underway on the new frontiers of European integration, from defence to infrastructure, from the digital to the fiscal union, from migration to climate change. Even though it is unlikely that we will reach easily, nor shortly agreement on such controversial questions, it is important that we have engaged in the discussion and shown commitment to confront differing views on it. The vision of the future must come before or at least accompany the action plans and the road maps. The basic question is: “Where are we going?” and “Where do we want to go”?

Finally, Europeans seem to have a better perception of the critical importance of the time dimension. There are urgent things that require immediate deliverables and a pragmatic and compromising approach. This is the case for instance of certain measures to strengthen the economic and monetary union and the response to unsustainable migration pressures. Others need to be carefully worked out and thought over, avoiding short cuts and quick fixes. We need both to promote a sense of urgency for immediate action, and at the same time remain focused on the long-term objectives of the European journey. Time consistency is the most delicate task of to-day’s policy making and business strategies.

Two concepts have appeared particularly promising, and were focused upon at the Rome Investment Forum. First, the idea that different speeds and concentric circles are not only unavoidable, but also desirable, to avoid stalemates and roadblocks. Second, long-term development, supported and driven by long-term financing, is central to attain structural solutions to complex structural problems. Both concepts were, and remain central to the “finance for growth” philosophy, which has inspired the contributions to this volume, and the discussions at the Rome Forum.

The volume starts with the Rome Declaration on the future of European Integration in the economic financial and monetary field. The Declaration was signed in Rome in March 2017, on the occasion of the 60’s Anniversary of the Treaty of Rome.

Following the structure of the previous editions of this volume, and the discussion that took place at the Rome investment Forum, the contributions have been grouped in seven sections. First, the most urgent tasks: fixing and completing the Economic and Monetary Union in Europe, with reference in particular to the unfinished and still vulnerable Banking Union.

Second, a focus on financing for innovation infrastructure and long-term investment. Follows then a reconsideration of the Finance for Growth approach, what still represents a new and innovative vision for the future of Europe. Forth, finance for competitiveness, entrepreneurship and Small and Medium Enterprises, the role played by pensions, start-ups, private equity and venture capital, and the points of view of two main Supervisory Authorities in Europe, like ESMA and EIOPA.

In the following sections, the global risk scenarios and the resilience of the world economy, and society, are focussed upon. The importance of financing for sustainable development is then discussed, with contributions targeting an area of special interest to the stability and prosperity of Europe: the Euro-Mediterranean. The final section deals with broader issue, on which finance can, and should have a significant impact, i.e. solidarity, inclusion, social responsibility and ethics: finance for the common good. The volume concludes with an intervention on the next steps and priorities in the policy agenda for financing long-term Europe.

We thank all the contributors to this volume, who provided texts or revised the transcription of their interventions at the Rome Investment Forum. Special mention deserve the various institutions that contributed to the organisation of the Forum, i.e. Cassa Depositi e Prestiti, the Long-term Investment and Reindustrialisation Intergroup of the European Parliament, Confindustria, the Long-term Investor Club, Paris Europlace, Frankfurt Main Finance, the City UK, the Consiglio Italiano del Movimento Europeo, the Forum per la finanza sostenibile, Integrate, the CEEP (European Centre of Employers and Enterprises providing Public Services).

Also thanks to the European Parliament (Rome Information Office) and the European Commission, under whose patronage the event took place, and to our media partners Data Stampa and EUNews.

Finally I wish to thank the Rome office of Febaf, and in particular Elia Lofranco, for helping out in the collection of the essays, the preparation and the finalisation of the book, and Gianni Rizzuti for coordinating the whole production.

Paolo Garonna
Rome, October 2017

Celebration of the 60th Anniversary of the Treaty of Rome

“Savings Investment and Finance at the Service of the European Idea”

Joint statement by the banking, insurance and finance communities of the six founding countries signatories to the Rome Treaty: Belgium, France, Germany, Italy, Luxembourg and the Netherlands



On 25th March 2017, Europe celebrated the 60th anniversary of the signing of the Treaty of Rome, one of the most significant historical moments of our time. The Treaty marked the beginning of an economic and social process in Europe that fundamentally contributed to peace and prosperity in the continent, and the world.

The Treaty of Rome, which was signed on 25 March 1957, by Belgium, France, Germany, Italy, Luxembourg and the Netherlands, and came into force on 1 January 1958, represented a landmark. It started our nations on the path to the European Union, the establishment of which accounts for six decades of peace and prosperity, the longest continuous period of peace in over 200 years.

In 60 years the European Union has made remarkable progress. Step by step, through dialogue and negotiation, it brought together peoples and cultures, economies and societies, markets and policies, capital and labour. It enabled the tearing down of historical barriers to mobility, mutual understanding and partnership.

Inevitably, the path was neither smooth nor linear, nor has it attained yet its promised destination. But the journey has continued forwards in a way that has no precedent in human history: through peaceful interaction, crisis management, finding ways around the stumbling blocks, learning from mistakes, sharing risks and exchanging views.

We owe it to the visionary and courageous leadership of Statesmen such as Konrad Adenauer, Jean Monnet, Robert Schuman and Alcide De Gasperi, among others, that today over 500 million citizens can work, travel, exchange goods and services, do business, communicate and move freely across the whole of the European Union.

The time has come to reaffirm our strong commitment to the construction of Europe. We need to take stock of the impressive results so far accomplished, but also recognise shortcomings. We need to build on these achievements to bridge still existing gaps and face up to the present difficulties. The 60 years' anniversary is a chance to newly reflect on the opportunities, goals and instruments of the European Union, as done in the European Commission's White Book.

That is why, on this historic anniversary, we, the representatives of the financial communities of the six founding countries that signed the Rome Treaty, convened in Rome, at Palazzo Altieri, and issued a Joint Declaration on a sound, efficient and competitive financial sector at the service of the European idea.

The Rome Declaration calls for the leadership of the European Union and its Member States, to take courageous political and economic steps forward to continue the journey of European integration and strengthen efforts to create together stability, growth and jobs. The determination of each Member State of the EU to reform its economy and reach sustainable economic growth is key for the success of the European project.

Since its inception, European integration has aimed at creating a common space for savings, investment and effective financing of households and enterprises. From the customs union to social cohesion, from the Werner Report to EU enlargement, from the Single Market to Social Europe, from the Regional policies to Europe 2020, from the common currency to the Lisbon Treaty of constitutional reforms, the importance of economic and financial policies has been widely recognised.

Following the latest crisis, which started in the financial sector, but then extended to the real economy and the labour market, affecting industrial production, incomes and standards of living, the role of banking, insurance and finance has come to the forefront of the European policy agenda. Rightly so. Creating a common space for economic growth and investment is a pre-condition for the single market in Europe to work. Above all, the single market contributes to giving greater opportunities for all, to be active members of the economy and society, to realise their potential. This is the ultimate objective of European projects such as Banking Union, Capital Markets Union, the Union of Investment and Financing, and Economic and Monetary Union. These projects figure prominently on the policy agenda of the European construction, helping to drive forward European integration, eliminate barriers to cross-border activity and create better and more equal opportunities for European citizens, no matter where they live or work.

For the reasons above, we, the representatives of the financial communities of the six countries who were signatories to the Treaty of Rome, Belgium, France, Germany, Italy, Luxembourg and the Netherlands, commit ourselves to engaging with European institutions, national governments, regulators, investors, consumers and all other stakeholders to make progress in the agenda of economic and social integration in Europe, while championing the diversity of our industry from which the EU has benefitted in the past.

We, the six founding countries' financial markets, would like to make use of the 60th anniversary to launch a dialogue on the future of European integration by involving the Federations, the Financial Centers and the main Associations (banking, insurance and financial) of all the countries of the EU. We wish to contribute in an active and forward-looking manner to ongoing reflections on the revival of the European ideal and the economic and financial future of Europe.

Let us continue to work together to make the European dream of our founding fathers come true, and live in a Europe of peace, economic prosperity and social progress.

Rome, 3rd April 2017



The Netherlands, Dutch
Banking Association



Luxembourg, Luxembourg
for Finance



Belgium, Belgian Financial
Sector Federation - FEBELFIN



France, Paris Europlace

Bundesverband der Deutschen Volksbanken und Raiffeisenbanken e. V.
Bunderverband deutscher Banken e. V.
Bunderverband Öffentlicher Banken Deutschlands e. V.
Deutscher Sparkassen- und Giroverband e. V.
Verband deutscher Filialbankbanken e. V.

Die Deutsche
Kreditwirtschaft

Germany, DK (VOEB, BDB, DSGV, BVR, VDP)



Finanzplatz Hamburg
Finanzplatz Hamburg

Finanzplatz München Initiative 

Finanzplatz München



Frankfurt Main Finance (FMF)



Stuttgart Finance



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FINANCE FOR GROWTH: A NEW VISION FOR EUROPE

INVESTING IN EUROPE

Jyrki Katainen*

I plan to talk about the investment environment, investments and what the European Commission is doing in order to improve the business environment and the investment climate in Europe.

I would therefore like to focus on four things – 1) delivering on investment, 2) removing barriers to investments, 3) building a capital markets union, and then I will round off by saying a few words about 4) modernising our economy.

DELIVERING ON INVESTMENT

Growth, jobs and investment in Europe are the number one priority of this Commission. The Investment Plan for Europe is an integral part of our comprehensive strategy.

The economic recovery is ongoing but economic growth in the euro area is expected to remain modest, relying mainly on domestic consumption. And investments have slightly picked up recently, suggesting that the favourable conditions – such as improved borrowing conditions, capacity utilisation above its long-term average and lower corporate deleveraging pressure – are starting to have their long-awaited impact. However, we are still behind the long term average.

The European Fund for Strategic Investments is a key part of the Investment Plan for Europe. Our first proposal aimed at mobilising at least €315 billion until mid-2018 in new investments in areas of strategic importance to the EU economy to support growth and jobs in Europe. Given the success so far, we plan to bring the mobilised investments to half a trillion euros by 2020.

I am proud to say that, since its launch in July last year, the Fund has been delivering on its promise. The European Fund for Strategic Investments is delivering. Approximately €30 billion of public EU guarantees have been used. And we are not only delivering on numbers – investments approved for backing by the European Fund for Strategic Investments in 27 Member States are worth €163.9 billion and almost 388,000 SMEs and midcaps stand to benefit (of which by the way around 190,000 are in Italy.)

* Vice President European Commission; European Commissioner for Jobs, Growth, Investment and Competitiveness.

And crucially, we are delivering on additional investments that would not have happened without the European Fund for Strategic Investments.

I already mentioned that Italy has been an active user of EFSI, especially for small and medium sized enterprises. And having said this, I must congratulate Italian financial institutions, banks and funds for being active users of EFSI. This has been the pre-condition for allocating more resources for small and medium sized enterprises in Italy.

As a result of this, there are 28 industrial and infrastructure projects approved by EIB under EFSI financing. This will mobilise around €8.5 billion additional investments in Italy. And this is only the result of the first one and a half years.

REMOVING BARRIERS TO INVESTMENTS

However, investment prospects are still held back by a range of factors, including weak global demand, the legacy of the crisis, sluggish medium-term growth prospects, and political risks and uncertainties, not only in Europe but also in other parts of the world. These elements and the outlook for a prolonged period of uncertainty could affect investment decisions.

The Commission supports an ambitious agenda of structural reforms to sustain growth and job creation. And this can only be achieved through complementary actions at EU and at country level.

At EU level, the Commission is taking actions to enhance regulatory predictability, reduce barriers, and reinforce the Single Market. In particular, it has launched initiatives regarding the development of a Capital Markets Union, the further deepening of the Single Market for goods and services, and a true Digital Single Market.

Other initiatives have also been adopted in the context of the Energy Union, and the Circular Economy package. All contain specific measures that will remove concrete obstacles to investment and further improve the framework conditions in which firms operate.

So, the EU will be a more harmonised and better market in three to five years' time than it is at the moment.

So far Member States have implemented quite a number of reforms. Italy is a good example of a reforming country. To my mind, Italy is probably one of the most innovative economies in Europe, if not the most innovative economy. But the societal structures are not translating this capability for creating added value into growth. And this is the reason why structural reforms are needed, also in Italy.

All the European countries are more or less in a similar situation, where they have to recognise that the world around us has changed and that our societies must change accordingly.

As I said Italy is probably the most innovative economy in Europe, and in order to translate this phenomenal capability to create added value for jobs and growth, reforms are needed.

In some countries, investment challenges may include a lack of transparency in public administration, a high level of taxation and overly complex taxation systems, product and labour markets distortions, weaknesses in research and innovation frameworks, and barriers to accessing finance, particularly for small and medium-sized enterprises.

The barriers to investment and for economic growth vary between the Member States. There are good examples of addressing these barriers.

One good example of reforms to improve the business environment was introduced in Italy, to reduce the debt-equity tax bias in order to improve firms' capitalisation and diversify access to finance.

The Italian government has introduced in 2011 the "allowance for corporate equity", which allows Italian firms to deduct a notional return on new equity and on reinvested profit from corporate income tax. In the course of 2014, the government has further strengthened the framework and adopted the so-called super-ACE in order to give Italian firms an incentive to make their equity base more robust.

This is exactly the same kind of measure as the European Commission has just proposed as part of the Common Consolidated Corporate Tax Base (CCCTB) proposal and this is very important for improving capital markets in Italy, and more broadly in Europe.

As part of the European Semester, the Commission has placed a particular emphasis on the identification of investment barriers and priority reforms to remove them. These reforms are well reflected in the Country Specific Recommendations for Member States.

BUILDING A CAPITAL MARKETS UNION

What is very important for financial markets and investments in Europe is strong capital markets.

The Capital Markets Union seeks to better connect savings to investment and to strengthen the European financial system by enhancing private risk-sharing, providing alternative sources of financing and increasing options for retail and institutional investors.

The Capital Markets Union Action Plan of September 2015 set out a comprehensive programme of 33 actions to put in place the building blocks for the Capital Markets Union of which around half are already delivered. Several more will be completed in the coming months.

Let me mention some examples:

- Overhaul of the prospectus rules to improve access to finance for companies and simplify information for investors.
- On 23 October we published the proposal to re-launch the Common Consolidated Corporate Tax Base, which included an equity tax allowance that was modelled on Italian legislation, as I mentioned before.

- Last May we published a report explaining the market and regulatory landscape in crowdfunding, in order to expand the options for financing for EU businesses. Italy being the first to introduce legislation on equity crowdfunding shows the support for alternative ways of investing.
- We are reviewing the functioning of EU corporate bond markets. A group of experts has been set up to find practical solutions to improve the efficiency and resilience of corporate bond markets.
- Minibonds are a prime example of Italy leading innovation in this field. Borsa Italiana's ExtraMot Pro market is home to 196 listed minibond listings. These have raised more than €8 billion at the end of last October.

The Capital Markets Union is one of our primary targets. It is one of our main Single Market projects at the European level. But more must be done also at the national level in order to implement all those reforms which will lead to more diversified financing, especially for small and medium sized enterprises.

MODERNISING OUR ECONOMY

Now finally, let me say a few words about Europe's need to modernise its economy and strengthen its competitiveness.

For many sectors experiencing fast and disruptive changes which are challenging established norms and approaches, investment and new ways of working are particularly needed.

Investment in Research, Development and Innovation is also crucial and EU funds are limited compared to the investment needs of the European economy.

It is therefore essential to mobilise private investment in RDI-related sectors, such as key enabling technologies, bio-economy, circular economy, health and well-being, new transport energy technologies, as well as access to finance for innovative SMEs or research infrastructures to fill the investment gap.

The Investment Plan for Europe represents an opportunity to scale up private and leverage public spending, build a pipeline of quality projects and remove the barriers to investment in RDI. Of the EFSI transactions approved by the European Investment Bank so far, 20% are in the RDI sector. This financing does not replace, but complements support for fundamental research.

And crucially – Europe needs to invest in its people. Skills are a key factor to boost competitiveness and drive innovation. They are a pull factor for investment and a catalyst for job creation and growth.

We need to ensure high quality education and training. And this is my message to public authorities. Imagine if all teachers in Europe in primary education had a higher university degree in teaching. What would it mean? First it would mean more equal societies, more social justice, higher productivity, higher competitiveness, more innovation, and more economic growth and jobs.

To me this is a low hanging fruit. Even more so, as a former finance minister I

am always interested in public expenditure. If we look at the OECD PISA study, which is comparing education systems in Europe, you can see that those countries on the top of the list are sometimes spending even less public resources on education than those, in which the results are not as good.

Therefore, money spent on education does not always correlate with the quality. That is why structural reforms in the education sector are often more important than the amount of money spent. The same amount of money can be spent well or less well.

I would like to make a proposal to the finance ministers. Take this to your Council formation and look at it as an investment for the future. Education is something which needs to be reformed in Europe, otherwise we will lag behind our competitors.

I will stop here. We are at a moment in time where we have to reinvent ourselves. In our Member States we have excellent assets. We have lots of creativity. But the world around us has changed, and this is the reason we need to be ready to reform ourselves.

Reform does not mean taking something away from someone. It means just changing the way we are operating or running our societies. And education reform is a good example of this.

Italy would not be as prosperous a country today without reforms carried out in previous years and decades. This illustrates why we have to look forward with a courageous mind, as we have the opportunity and the chance to reform our excellent societies.

FINANCE FOR GROWTH: MOVING THE AGENDA ONWARDS¹

Pier Carlo Padoan *

This is the most appropriate venue to reflect upon recent developments in the banking industry, starting from the context within which these developments have occurred. Back in 2014, the Country had put behind it two years of recession. Still, in the course of the previous thirteen years, between 2001 and 2013, our growth achieved 1-2% five times, stood at 0-1% for four years and was followed by four years of recession. This trend of the economy, that reflects the combination of structural obstacles and the impact of recession, was accompanied by volatile public finances. Italy's public deficit fluctuated around 3%, with spells of improvement to 1.5% and sharp deterioration beyond 5%.

From 2007 to 2013, the Debt/GDP ratio went from 100% to 130%. In 2014 the country's economic structure had been profoundly wounded by two rounds of recession, in 2008-2009 and 2012-2013 respectively, and the country was faced with the twofold need to fix public finances in order to stop public debt from skyrocketing while underpinning economic recovery. It was necessary to support the weakest groups of the population, encourage businesses and favour the recovery of household consumption. At the same time, international markets and European partners had to be reassured.

The country's economy has been recovering since 2014. ISTAT (Office for National Statistics) analyses show that measures such as the Irpef (personal income tax) bonus, the pensioners bonus and REIS (guaranteed minimum income) combined have reduced inequalities and poverty alike. Growth acceleration coupled with progressively improving public accounts is the right avenue to reduce debt, curb its pace first and subsequently revert its trend.

Italian businesses are overcoming the crisis, supported by labour and income tax cuts and by a taxation regime that promotes investments and innovation.

The GDP deficit and stabilisation of debt over the last four years seem to indicate that the pace of consolidation during this period has led to positive achievements, notwithstanding the surrounding context, including very weak inflation.

The first economic policy implication is that all of the foregoing suggests that we should keep going along the way that we are.

1. This is a revised version of the paper presented at the Annual Conference of the Italian Banking Association, 12 July 2017.

* Minister of Economy and Finance, Italy.

Of course, one should consider not just the performance of public accounts policies but also their composition and the quality of the measures taken. The spending review of the last several years has been very deep, making it possible to structurally finance accommodative measures. Tax cuts have boosted consumption and supported businesses, with the latter also benefitting from specific incentives for private investments, which are gaining momentum.

Much remains to be done, instead, on the front of public investments, the decline of which has been stemmed also because across-the-board expenditure cuts have been replaced by selective ones and by an effort to urge public players to invest more in infrastructures. The ability of the public administration system to spend – and “to spend well” – remains limited. The introduction of the new public procurement code in 2016 is a step in the right direction, but like many structural reforms it requires a period of adjustment during which results may temporarily worsen. The recent fine-tuning of the code has allowed to overcome the issues found during its implementation and we expect investments to recover during the current year. We have to resolutely capitalize on this driver, being aware, though, that much needs to be done to improve the planning and spending ability of the public administration system.

The second economic policy implication is that it is necessary to carefully consider how to use the fiscal space, especially when it is limited. Not all tax cuts equally impact growth and employment. Public investments are crucial, but their size does not depend solely on the resources available. The double crises years, between 2008 and 2013, have profoundly changed also the context within which financial intermediaries operate. In particular, the effect of the economic crisis on the quality and quantity of bank loans has become clear. There is a time lag between the economic crisis and the dynamics of NPLs that explains also why the amount of NPLs peaked in 2015 while the economy is already showing signs of recovery. At the same time, the build-up of NPLs helps hold back, though partly, the recovery.

In the meantime, the new European rules are coming into force, which, as is now clear to all, require the Italian system as a whole to take a leap forward quality-wise: more awareness is needed in the choices of savers, actions need to be taken at source on the governance of banks so as to make it more functional, by strengthening management incentives. It is within this context that the Government approved the reform of people’s banks. The outcome of that reform is that we now have banks that are more accountable and reactive to the market and a banking group that is larger and more efficient than the two banks that have originated it, whereas the banks that have been mismanaged for years, to the detriment of their shareholders and other creditors, have been driven out of the market with no consequences for their customers, savers and employees.

The reform of cooperative credit banks followed in the same furrow, the aim being that of establishing a stronger system, one that is capable of better reacting to crises. There have been crises in these years, but their number is fairly limited. The resilience of the Italian banking system is shown, amongst other things, by the very limited use of public resources in the management of these crises, including thanks to the contribution of the banking system itself. The savers who have been adver-

sely impacted by the improper conduct of banks have been compensated by the banking system, without using the resources of taxpayers; also, by setting up the Atlante Fund, industry players have proven that they are capable of creating a shared tool for managing their common interests.

Still, this has not prevented a sizable amount of criticism. In Italy, it has been said that the search for specific solutions for each of the different crises shows the absence of an organic and overall approach by the Government. I disagree. Quite to the opposite, I think that in the course of the transition to a new regulatory framework, the implications of which have not yet been well considered, case-by-case solutions are needed, and in each case such rules should be applied as are most appropriate to minimize the social and economic impact of each specific situation.

Italy has also been accused of having found a way to respect the letter but not the spirit of the rules. In the Eurogroup and Ecofin meetings of yesterday, the European institutions involved in the recent banking cases have confirmed that the actions taken fully comply with the rules and that in any case they have shown a high level of flexibility, greater than might be envisaged. European rules allow the State to intervene in a liquidation, as provided for in the 2013 communication of the Commission. Such intervention must be justified by the need to contain the costs of a disorderly liquidation, as has been the case. It should be reminded that the shareholders and subordinated creditors have had to bear the cost of the crisis before the intervention of taxpayers, who are reasonably likely to recover the amount spent. This case-by-case resolution mechanism has allowed to improve the overall situation, in the light of improving economy. In 2016, NPLs declined over 2015 and in the first 4 months of the current year they have continued to decrease sharply. The liquidation of the two people's banks headquartered in the Veneto region and the NPLs disposal announced by Monte dei Paschi and other banks lead to believe that at the end of this year we can record a clear decrease.

We can say that we have reached a turning point. At the origin of this turning point is, amongst other things, the recovery of the economy, thanks to which those businesses that are temporarily having difficulties are better able to fulfil the obligations undertaken vis-à-vis lenders. Also the reforms have played a crucial role: not only structural industry reforms but also the innovations introduced in the insolvency and credit recovery procedures as well as the specific support instruments for this transition phase, including, in the first place, the guarantees for securitizing NPLs.

There follows another economic policy implication: the reform effort must be maintained and increased.

Private initiatives have been taken within this framework with the support of the Government, such as the setting up of the Atlante Fund, which has helped revive the NPLs market. Its shareholders have been courageous enough to put together resources and share the effort to solve their common problems. One has to acknowledge this merit. Likewise, one should also acknowledge the personal commitment of those directors who have tried to find market solutions to overt crises.

We can say that the worst is over. But we have to be aware that the financial crisis of the last several years has spread across Europe a strong propensity to risk re-

duction. Yesterday, Ecofin draw its conclusions in a report on the actions to be taken in Europe and by member states in order to make it easier for banks to reduce the volume of non-performing loans and return to profitability, to free up capital to be used for funding the economy and forestall the risk of distress of worst-case banks. The report identifies four areas of intervention: powers of supervision; impediments to the development of an efficient secondary market; reform of foreclosure and bankruptcy procedures; exit from the market. There follows another policy implication: in this framework, it is necessary for banks to be resolute and incisive in actively managing their outstanding balance and define a credible strategy for a progressive reduction of the amount of NPLs.

In conclusion, on this theme, the possibility to take action in a range of different ways highlights that the European regulatory framework has ensured room for flexibility, so much so that the bail-in has not been used in the three cases tackled in Italy; senior bondholders and depositors have been protected and the funding of the real economy has been safeguarded, just like employment levels. Moreover, these cases have emphasized a number of criticalities in the European construction, to be faced and solved in the coming months, as part of the completion of the Banking Union.

The completion of the Banking Union is certainly crucial in the process of European integration. We all need European integration. It is the answer to the growing challenges of global competition and to the new geopolitical scenario. Paradoxically, we are faced with a new window of opportunity:

- economic: because the growth that is stabilizing globally makes it easier, but also all the more necessary, to have a new wave of structural reforms;
- political: because it offers a perspective of integration and opening as compared to the nationalism and bilateralism that seems to prevail in some cases.

Italy and the Italian Government have prepared specific proposals to contribute to the debate on the future of Europe. This debate originated from the report of the five presidents and the discussion paper on the deepening of the economic and monetary union recently produced by the Commission.

I wish to remind some aspects which the European agenda for the coming years should include, according to the Government:

- the banking union should be completed by balancing risk-reducing and risk-sharing measures;
- the instruments to support private investments should be enhanced, starting from Industry 4.0 and the Juncker plan, the results of which are better than expected, but which should extend its scope of action, including in terms of geographies covered;
- solutions should be found allowing to increase public investments, which are indispensable in order to bridge geographic and social gaps, though within the context of European public finance.

A reform of common accounts is desirable, which, looking forward, can be governed by a European Finance Minister subject to the democratic control of the European Parliament. The European Finance Minister should also govern the funding of European public assets, like the construction of physical and digital infrastructures, border protection, homeland security and migrants' flows.

The countries that are best positioned in terms of economy and employment fear that risk-sharing measures can entail a permanent transfer of resources to the weaker economies. This concern can be tackled with formulas allowing to recover over time the funds employed, while overcoming the crisis. But integration can and must be pursued only in the presence of a strong political commitment to promote the reallocation of resources and the ability to make citizens perceive long-term benefits. All of the European Union member countries must give their contribution in terms of resources and joint efforts.

Against an international backdrop in which democracy is being challenged on many fronts, Europe is uniquely positioned. The development model built in our continent has enhanced the role of citizens, promoted equal opportunities and protected the weakest. However, these achievements must not be taken for granted. Europe remains the best solution to respond to the challenge of the global system; still, in order for it to be effective, Europe must transform itself, its structure and its institutions.

I say it again, the Italian banking system has reached a turning point: it can and must become a fundamental component for accelerating the pace of growth; at the same time, it must finalise adjustments inside the Banking Union. Also, the economy is changing: in recent years, it has moved forward along a narrow path, hemmed in between the need to strengthen public finance and slash debt and the need to support growth: it cannot be denied that the main avenue to slash debt is more growth.

These two strategic lines must be fully supported within a European scenario that requires a response to the reform efforts, in both structural and institutional terms; domestic and European reform efforts are fundamental in order to translate the cyclic recovery underway into an increase in the potential GDP, productivity, investments and hence a long-lasting and sustainable expansion. This window of opportunity must not be wasted.

SETTING OUR SIGHTS ON THE FUTURE

Pierre Gramegna*

One could say that the choice of this topic clearly illustrates the fact that we have definitely moved on from the crisis debate and are now firmly setting our sights on the future.

I believe that the most important thing in an environment such as the one we are currently experiencing and which is characterized by a certain amount of uncertainty is to restore confidence – the confidence of citizens, consumers, investors and markets.

First of all, allow me to highlight that, unlike many commentators or outside observers, my view of the current economic environment and the future outlook in Europe has always been and will continue to be positive, despite the events we have witnessed throughout 2016. We have skillfully weathered the most acute phase of the crisis that erupted many years ago in the US and we are witnessing today a nascent recovery all across Europe.

To illustrate my point and being in Rome today, it might be worth to look at a few facts regarding the Italian economy. In 2016, Italy is expected to have achieved a primary budgetary surplus of 1.5% of GDP. After years of significant increases, public debt is now expected to stabilize around 133% of GDP and should in fact decline significantly by the end of the decade. Finally, employment has been gaining pace since 2013, with over 600'000 new jobs having been added and this pace is even expected to continue going forward. I could obviously continue with this list, but the message is clear: the Italian economy is slowly recovering.

Yet, when you have a look at the international press since the constitutional referendum in Italy, you would be tempted to think otherwise. It is always important to be critical and vigilant; especially as policy-makers we need to be forward-looking and tackling all relevant challenges for the benefit of our citizens, but one should never let “negativity” gain the upper hand.

To sketch out a new “Vision for Europe” – as the title of this session suggests – first and foremost, I firmly believe that we need to sketch a positive outlook for the future. At the same time, it is of course just as important to remain mindful of the challenges that persist.

* Minister of Finance, Luxembourg.

In Europe, we can undoubtedly say that strong foundations have already been laid for the future when it comes to finance and its contribution to long-term growth. Banking Union, SSM, SRM... to name but a few. But they also need to be completed, such as through the establishment of a common European deposit insurance scheme, also known by its acronym EDIS. So, collectively, the EU member states have strengthened the resilience of their financial systems as a result of the crisis, but policy makers need to look ahead now.

Building on the experience of the last few years, there is perhaps a need to “re-adjust the screws” where some measures may have been over-ambitious or where they might have in fact have hampered growth and job creation. I regularly tell my colleagues at the ECOFIN Council meetings in Brussels that we need to be mindful of the effects that any new measure can have on the competitiveness of Europe vis-à-vis the rest of the world. We should not get ahead of ourselves but ensure a level-playing field wherever possible at the global level, and thus preserve the attractiveness of Europe as a whole for international investors.

At the same time, it is also vital that companies and SMEs continue to have access to sufficient resources for their investments into infrastructure, research and innovation. Here, I am notably thinking of the Capital Markets Union, which plays an important part in mobilizing finance for growth and diversifying the sources of funding. Non-bank based financing – in addition to the existing bank channel – can be a catalyst for growth in the future, but for this market to develop we need to move ahead with this ambitious project.

Looking at all other relevant facets of growth, one quickly realizes that the right policy mix is key. Monetary policy cannot do everything, but the very accommodative policy of the ECB, under the skillful chairmanship of its President Mario Draghi, has provided ample breathing space. It needs to be used wisely.

Structural reforms should also be continuously implemented to boost productivity and to create a supportive environment for investments, notably by removing any existing barriers or bottlenecks. I believe that investments, by both the public and the private sector are key. In this context, the so-called Juncker Plan brings together the best of both worlds and shows promising first results. We are therefore considering to double the volume of this Plan.

My colleagues in Brussels – and specifically Pier Carlo, with whom I discuss this subject regularly – know that for me, “more” and “better” investments are key to accelerate growth in Europe. With the Juncker Plan and the added flexibility in the budgetary rules, the EU has made a huge leap forward to increase public investments in a wide range of areas such as infrastructure or education.

But the public sector cannot do everything.

The private sector needs to be able to step up its efforts too. In particular, because it is the private sector that will have to create the jobs so dearly needed in many parts of Europe. So, in addition to the efforts to strengthen the availability of finance and to diversify the sources of funding – i.e. the supply side of the story –, I return to the main point that I made at the beginning of my speech: confidence. Because confidence is key for a new Vision for Europe and confidence is necessary for the demand

side of the story, given that we need new and exciting investment projects to go hand in hand with the improved availability of financing.

With a vibrant young generation in Italy and all across Europe, a generation full of ideas and motivation, it is important to nurture a positive outlook and lay solid foundations for the future.

Structural reforms in areas such as education and business regulation are indeed necessary to create a favorable environment for new companies to set up shop and new ideas to develop. The public sector should pair up with the private sector wherever possible and thus support the development of such new businesses.

FinTech is one of those areas, I am thinking of here – where we have made enormous efforts in Luxembourg over the past months and in which I personally take a keen interest. But there are many other exciting fields that decision makers should look at to bring the best out of finance in order to support growth for the future.

To conclude, I believe that Europe has made significant efforts over the recent past, which are clearly bearing their fruits today. I am confident that all relevant stakeholders will now seize the many exciting opportunities that lie ahead of us.

THE CHALLENGE OF REGULATORY REFORMS IN EUROPE

Maurizio Sella*

Since the financial crisis, rules governing world financial markets have undergone a major overhaul, in the main following the regulatory agenda set by the G-20 and Financial Stability Board (FSB).

The impact of regulatory reform on the economy has been seen as benign since reform I quote FSB would “promote a safer, sounder and more resilient financial system [...], rebuilding confidence and reducing pro-cyclicality [...], which will enhance the system’s ability to intermediate financial flows through the cycle and for different investment horizons” (FSB 2014).

However, over time some aspects of regulatory reform have come to the fore for their possibly adverse direct impact on incentives to lend and borrow long-term, as well as short and medium term.

In Europe, given the paramount weight of banks in the financing of the economy, these concerns relate first and foremost to the strengthened capital requirements under Basel III Accords, including stronger expected-loss provisioning.

It has been argued that higher capital requirements and stronger provisioning according to the expected-loss approach will inevitably constrain the supply of credit. Others have argued that it is unclear whether forcing banks to hold more equity would raise the cost of credit to the economy, as the reduction of the risk premia paid by banks for their (non-deposit) funding could well compensate for forgone interest-rate tax deductions on their debts.

In any case, more stringent regulatory requirements should be designed so to lead to a reduction in ‘financialization’ rather than lending to the real economy.

This is, indeed, the core of the ongoing debate about the revision of global banking regulation, through the evolution of the “Basel III” package.

The main (technical) issue under discussion by regulators is how banks can use their internal models to determine the riskiness of their loans. In particular, the Basel Committee is about to introduce two floors (*input* and *output floors*) that will strongly limit the use of internal ratings. Cited by Dr. Gualtieri.

In the view of regulators, the proposed measures aim at reducing excessive variability in risk-weighted assets and, by doing so, avoiding the possibility by banks of ‘gaming’ the rules.

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However, the goal of the regulators of achieving higher harmonisation of existing risk-weighted systems, and reducing differences between different banking systems should not result in a disruption of the financing of the real economy. A more gradual approach in the implementation of the reform, with specific steps clearly identified by regulators, might help to reduce market pressure to anticipate the final outcome.

For banks who have already invested considerable resources in the last decade to develop and implement complex internal ratings systems to revise their capital and credit portfolios, there is the fear that the new rules would result in an additional burden that will strongly limit their lending ability.

In particular, European banks are especially sensible to the topic since many of them rely on internal ratings, while most American banks, which continue to follow the standard models, are actually less worried.

Additional capital requirements and stronger provisioning by the Basel committee should not have a significant impact in any region, including Europe, in order not to alter the global playing field in banking.

The resilience of the banking system is the key issue for the European economy and it is the necessary condition for creating financial markets more supportive of long-term growth strategies by all the actors, both investors and issuers.

The 2016 EU Banking Reform package proposed by the Commission (to review the CRR/CRD IV, the BRRD and the SRM) aims at building a regulatory framework more conducive to growth in the EU, but there are elements that must be carefully reviewed in order to create an efficiently regulated single market for finance in which European banks are not put in a competitive disadvantage.

The introduction of additional capital requirements for the implementation of the international standards will result in heavier constraints on banks' lending ability, not only for large banking groups, and further limit their profitability in a still too fragile recovery environment.

Those measures are only partially compensated by the provision of lower requirements for bank lending to SMEs and for funding infrastructure projects that instead go into the direction of increasing funding for the real economy.

The outcome of the regulatory debate is even more crucial for the Eurozone since it is still plagued by severe imbalances in its banking system.

According to a 2016 IMF's Global Financial Stability Report, one in three banks in the Eurozone must confront severe challenges due to legacy issues (900 billion of non-performing loans and an unspecified amount of toxic assets), and the need to revise business models to respond to a sharply modified economic environment, and adapt to taxing regulatory changes.

Moreover, there is also an issue of low profitability of many Eurozone banks which are constrained by the low level of interest rates on one side, and increasing capital requirements on the other side.

The topic is relevant also with respect to bail-in and resolution framework: under the current interpretation of burden-sharing rules by competent authorities, this situation may be perceived by investors as foreshadowing the risk of write-down or conversion of banks' debt instruments.

In particular, once it is acknowledged that the banking industry has to confront head-on its substantial requirements for fresh capital, and that private sources of capital may be insufficient, then the competent authorities should be ready to open the way to well-designed precautionary recapitalisations, supported by public back-stops.

Many member states in the Eurozone and the European Union are still enmeshed in stagnating economic conditions, which are due in no small part to the inability to tackle decisively the structural weaknesses of banks and restore their ability to support the real economy with adequate lending.

Resolving this issue cannot and should not be delayed by an unduly restrictive interpretation of EU rules, which already contain all the required margins of flexibility.

**FIXING AND COMPLETING THE ECONOMIC AND MONETARY
UNION: THE COSTS OF AN UNFINISHED BANKING UNION**

NEXT STEPS TOWARDS THE BANKING UNION: CHALLENGES AND MEASURES

Roberto Gualtieri*

The Banking Union is a fundamental pillar of the monetary and economic Union, and the foundation of the Single Supervisory Mechanism and the Single Resolution Mechanism in the framework of the Single Rulebook, objectively representing the institutional innovation of major importance so far, after the introduction of the Euro. These institutional changes have remarkably underpinned the faith in the European banking system, its solidity and its capacity to provide resources to the real economy.

Nevertheless, the Banking Union is still young and incomplete. With the aim of completely reaching its goals (i.e. fixing financial stability, sustaining the credit supply, endorsing the transmission of monetary policy, allocating capital efficiently, contributing to shock absorption) we need to face three challenges, which require to find some delicate equilibria between stability and growth, between traditional differences among member states' banking systems and a higher level of integration, and finally between risk reduction and risk sharing. In essence, the above-mentioned challenges attain to the realm of politics, rules, and institutions.

The first is related to the capacity of defining concretely an effective pattern of supervision and resolution. The results achieved can be judged positively, both under the perspective of the operative functioning and of the quality of supervision, even though some critical points remain, such as the excessive imbalance between the high attention given to credit risk and the insufficient capacity to measure and to value bank's financial portfolios starting with *level 3 assets*. Moreover, at all levels it is still difficult to coherently define a unifying trend of supervision. Finally, these problems are sometimes even worsened by a not so clear distinction – I am referring to the NPL issue, for example – between supervisory competences and management methods.

At the same time, certain significant improvements that should not to be undervalued have been recorded.

For instance, the reform of second pillar capital requirements (Basel regulation), solicited by the European Parliament, due to the split between requirements and guidance, appears to be a positive innovation, and one which has already contributed to the stabilisation of the capital requirements under the recently finalised new SREP

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cycle. These innovations seem to reinforce the picture of a significantly recapitalised and sounder banking system, both at European and national level.

In addition, and concerning specifically troublesome situations, it appears that the awareness of the possibility and the opportunity to use the narrow flexibility margins allowed by the current legislation for the recovery and resolution of credit institutions and by current State-aid discipline has finally matured. These margins allow implementing measures of precautionary recapitalization to solvent institutions, whenever it is necessary to preserve their financial stability.

In this framework, even if the possibility of exempting subordinated creditors from the application of burden sharing, originally contemplated in the 2013 Communication on the Banking Sector, has been materially suppressed by State-aid orientations one notes the recognition of the need to secure a significant level of reimbursement to bondholders.

Even if long overdue, these developments indicate a positive evolution in the current debate, and a first step towards the much needed overcoming of a purely ideological and abstract vision in favour of a more realistic acknowledgement of the limits and the implications of the BRRD, and as well as the too rigid and restrictive standards of the ESM direct recapitalization instrument for banks.

The second challenge concerns the completion and refinement of the regulatory framework provided in Basel, through the legislative package presented a few weeks ago by the Commission (CRR/CRD update and TLAC/MREL integration) and the ongoing review of the *banking book* by the BIS. It is a demanding challenge, because it requires to expand the solidity of the system of rules, closing the remaining gaps, and at the same time not to compress, but enforce the capacity of the banking system to sustain the real economy. The first steps accomplished so far seem to be encouraging. The Commission's legislative proposals are well balanced and contain different positive elements, some of which strongly demanded by the European Parliament. I am thinking, for example, about the extension of the SME Supporting Factor, and the reduction of the capital requirements for the exposures related to the financing of some infrastructure projects.

Also, the proposed measures for the TLAC/MREL are balanced, starting from the articulation of the MREL in *requirement* and *guidance*, even if in my opinion there are some margins along the ongoing co-decision procedure which could allow us to introduce improvements in order to avoid an excessive and sharp increase of the *funding* cost. In the first place, the *guidance* should not imply subordination requirements, while regarding requirements, that apply to non-systemic institutions, these *requirements* should be avoided or be introduced with proportionality in mind. Finally, it would be useful to introduce an appropriate transitory phase, and avoid a contradiction between current MREL calculation methods adopted by the SRB and the new criteria from the FSB.

It is widely known that the ongoing negotiation in Basel on *risk weighted average* has generated and is still generating serious worries. It is necessary to clarify that robust global standards are essential, especially if faced with threats posed by unilateralism like those emerged after the American elections or from the British refe-

rendum. Furthermore, it is undoubtable that the excessive variability of risk weighted assets is real and should be reduced.

All the measures we have mentioned should take place preserving the prudential supervision sensitivity to risk, and respecting the principle according to which the revision should not determine a substantial increase in capital requirements, nor have an asymmetric impact that penalizes the European banking system, which is far more based on (bank) credit than any other jurisdiction.

As a matter of fact, the original proposal presented by Basel did not meet these characteristics, but let me say that during the past few years the European institutions were able to react in an effective way. It is well known that the negotiation is still ongoing and the sensitive issue of the *output floor* is still unfixed. However, and referring to operational and credit risks, we have to recognize that significant improvements have been made. Therefore, I hope that an acceptable agreement about the *floor can be reached and that it will allow for a positive conclusion of the whole negotiation*, as well as the final conclusion of the negotiations on the overall regulatory framework for prudential requirements.

If the challenge posed by the different policies and rules has in the meantime recorded important steps forward, certainly the most complex one remains the institutional challenge posed by the completion of the Banking Union.

The present asymmetry between common rules and institutions and national resources does not only determine an imbalance between risk reduction and risk sharing, but ultimately it undermines the same risk reduction efforts and the stated will of breaking the doom-loop between banks and sovereigns. This is why we need to proceed without hesitation towards the realisation of a *backstop* for the *Single Resolution Fund*, and swiftly proceed to finally build the third pillar of the Banking Union. In fact, currency is largely created by bank deposits. As a consequence, and for the currency to be effectively unique, the level of confidence in deposit protection schemes needs to be the same regardless of their geographic location.

Certainly, one needs to be aware of the extreme political sensitivity concerning this issue, as well as the difficulty of connecting different principles and demands, including those that provide for efficient institutional protection schemes, already able to manage alternative and precautionary measures. In order to obtain this result, we should avoid taking the wrong path, such as the unilateral intervention over exposures in sovereign bonds.

To discourage this kind of intervention, an objective cost-benefit analysis of the different options that have been proposed would be sufficient. However, in all the cases discussed by the working group of the Council disadvantages (costs) are likely to outweigh advantages (benefits). Fortunately, the Council, the Commission, and the Parliament share an orientation of wise cautiousness, and the question has been transferred to Basel, even if we will continue to supervise in order to prevent the revival of improper conditions when discussing the EDIS framework.

On the contrary, in the legislative process that we have started around this theme we will concentrate on the “internal” problems raised by the European proposal of EDIS, and we will try to regulate intervals and methods of our work in order

not to let our efforts run aground. While keeping in mind the busy European political agenda, we will not however be settling for any watered-down solutions. In this regard, the text that will probably appear in the Conclusions of the European Council – speaking of the necessity to make progress both on the *risk reduction* and the *risk sharing* side with the presented package – could represent a positive albeit not fully sufficient element.

Clearly, the path towards the completion of the Banking Union is intimately connected with the more general and difficult issue of the rebuilding of European citizens' faith in European institutions. The elements needed for such a rebuilding exercise are different. However, one of the key factors is the capacity of re-launching growth and reinforce social and regional cohesion. This is why one needs to break the vicious circle between expectations of low growth and low investments, before it compromises the potential for economic growth. Also, we need to endorse the expansionary monetary policy with a *policy mix* of fiscal and structural policies that are more growth oriented. In order to achieve an effective *policy mix*, it is essential to have a healthy financial system, which can allocate the savings in an efficient way and lead them towards productive investments.

This forum certainly represents an important occasion to establish this vision and to push forward an agenda which promotes finance as a true element of growth and development.

FOCUSING EUROPEAN REFORMS ON GROWTH AND COMPETITIVENESS

Vincenzo Boccia*

By way of introduction, I wish to start my talk with a paradigm of thought: it is fundamental to define together the effects that we want to bring about in the real economy, identify the resources and instruments needed and then take action on budget balances in respect of an issue that affects Europe and Italy alike, in a world where sector averages are no longer meaningful and the data mentioned by President Abete is the algebraic sum of the gap that exists between enterprises, citizens and countries. We have to counter inequalities and poverty with the notion of an inclusive society, be more ambitious when it comes to our purposes, combat neo protectionism through a more integrated Europe in order to foster growth. Also, in a geo-economic dimension that becomes geo-political, we have to enhance the value of the central role of Italy, set between Europe and the Mediterranean.

In recent years, an impressive reform process has swept through the European financial and credit system, one that aims to ensure that the entire financial system gains stability, by boosting its resistance to crises. The establishment of the Banking Union is a milestone of such reform process. We have highlighted since the beginning that the Union was an unavoidable step forward in the planning of its construction.

The Single Supervisory Mechanism (SSM) came into being two years ago. Since then, it has enhanced the transparency of accounts; also, it can spread confidence in the system. Still, alongside this has come the revision of the supervisory rules, which may potentially tighten the credit supply.

The Single Resolution Mechanism (SRM) has come on stream recently but, while there have been implementation issues, it has put systemic stability at risk. There is no such a thing as a single deposit insurance scheme and debate is rife over its design.

The Banking Union as has been implemented so far is therefore neither perfect nor complete. Those who, like us, see it as being a must and take its destiny to heart, should work with fresh determination to strengthen it. Still, in order to do so, it is necessary to think over the criticalities that have emerged in this initial stage, what has remained unaccomplished, the pressure brought to bear against the introduction of new rules that would make even more fragile the ambitious construction we are working on.

* Chairman, Confindustria.

First of all, I believe it is necessary to make a few remarks about the European Banking Resolution Mechanism (which, amongst others, also provides for bail-in) and the recent European norms on aids to banks. Under the SRM, banks will be required to keep a certain amount of eligible debts in the event of a bail-in. Overall, subsequent to such reform the cost of funding might increase and loans to enterprises might be curbed.

The new rules, which are at the center of a debate in these months, have been gradually phased in starting from 2013 and, overall, they have led to a regulatory framework that prevents public intervention unless action is first taken by the banks' shareholders, bondholders and even current account holders. However, this occurred after other European countries – Germany, but also the United Kingdom, France, Spain, Ireland and Portugal – had forged sizeable plans to bail out their respective domestic banking systems. The problems of the Italian system – which, in any case, prior to 2012 could not have taken significant action in respect of banks due to the sovereign debt crisis and public finance issues – have surfaced, showing their real size, after 2013, i.e. when, in the absence of a stable economic recovery and with loan recovery timings well above the European average, matters came to a head relative to NPLs in the balance sheets of banks.

On balance, Italy, as compared to the other EU core countries, is the one that has allocated the lowest amount of resources to support banks. The goal of the new rules was not to place the burden upon the taxpayers. However, this goal should be pursued in the long term, only after the European system has been made safe. Above all, one should consider the effect of systemic difficulties, which may increase and, as a result, it may not be possible to curb the costs for taxpayers. Indeed, if the crisis were limited to just one bank, the bail-in could act as a deterrent against moral hazard and thus be an acceptable instrument.

Still, in the event of a systemic crisis sprawling across the whole of the banking industry, taxpayers would have to “pay the bill” four times. First, as their assets would be impaired due to the collapse of stock prices and housing prices; second, as a result of income erosion; third, because of job loss and, fourth, subsequent to the increase in taxation and/or public spending cuts required to cover the public deficit caused by the worsening state of the economy.

Regardless of any thoughts on a possible revision of bail-in (necessary as such thoughts are, however, not so much in respect of the situation of a given country but because of the misevaluation of its real economic effects, which are by all means counterproductive vis-à-vis the understandable reasons that have led to its introduction) flexibility is required (the very flexibility that both the rules on banks' bailout and those on State aids to banks provide for in relation to the cases in which the financial stability of one or more European Regions is at risk rather than the continuity of a single bank).

Hopefully, where the market solutions that are being considered for Italian banks do not produce the expected outcomes, a shared European solution will promptly be found so as to overcome the current problems of the Italian banking system, as has been the case before in other countries and especially to safeguard household savings.

The Banking Union must be completed with the elements that were provided for in its original design. The single resolution fund has been set up, but the contributions paid in by banks, initially split into national compartments, will only be shared in the long term; there seems to be no clear determination to actually use it.

Besides, as pointed out on several occasions by Confindustria, a third component is still missing, i.e. a “Single Deposit Guarantee Mechanism” going beyond the existing domestic guarantee schemes, thus ensuring more protection, thanks to an increase in the resources available, for all deposit holders of the banks that are subject to ECB supervision. The European Commission has presented a proposal, but this one as well will feature a long period of transition. What is missing in both cases is the European public financial support already foreseen in the 2012 Report and which is indispensable for the Banking Union to ensure systemic stability.

The European deposit insurance scheme appears to be stuck due to the resistance of countries that maintain that they are concerned by the existence of cases of prior difficulties in the banking sector and which intend to bind completion to the reduction of the exposure of banks to their country’s sovereign risk, so as to help, according to them, break the vicious circle between banks’ debt and sovereign debt. Having regard to this, a digressive rating has been proposed for government bonds so that the market would judge the solvency of a country and there would be no limits to the purchases of government bonds by Eurozone banks. Both hypotheses are a criticality for Italy and for the European periphery. Also, where there is a criticality for one Member State, to us, it means that there is a criticality for Europe.

The point is that, even when the Banking Union will have been completed, the banking systems will in any case remain linked to their respective local dynamics, meaning that the cost of funding will still be tied to the returns of the government bonds of each country, including in the event that banks held a lesser amount of government bonds.

Indeed, Italy (and other countries) feature a very tight correlation between the returns of sovereign bonds (in particular, the return of the reference bond, i.e. the 10-year BTP) and the returns of bank bonds. If the exposure of banks in their balance sheets to the government bonds of each country were to be expressly capped or if the weighting of such bonds were to be increased, compared to its current zero-level, in the construction of risk-weighted assets required to calculate the banking capital ratio, a major source of demand for such bonds would be missing, especially in the Eurozone countries that feature higher public debt levels. This would in turn translate into higher government bonds returns and would impact the cost of lending in such countries, which would limit access to credit and curb growth.

It should be borne in mind that Italian banks have massively purchased national sovereign bonds when the crisis was at its worst, with their portfolio shifting from €205bn at the end of 2011 up to €402bn in June 2013 and not declining since then.

This has limited the increase in the returns of sovereign bonds, which were already way above the values warranted by the actual country risk and has allowed banks to improve their accounts. If banks had had to limit their purchases, Italian banks would have had to face more difficulties and therefore the credit crunch would

have been worse and the higher returns on government bonds would have adversely impacted public accounts and economic performance.

Finally, it will be of strategic importance to discuss in depth the macro-economic impact of the international regulation that governs the credit and financial systems. Concerns on this front are real: further restrictions are being discussed internationally.

I therefore believe that it is vital for enterprises, banks and institutions to work together to correct the rules that restrict credit supply and to avoid the introduction of new rules which are doomed to have the same effect. In particular, I'm referring to the revisions proposed by the Basel Committee which, amongst others, provide that the internal rating models of banks be replaced by the standardized method. With respect to this, we are working with our colleagues of the European general confederations of industry to ensure that the new rules will be actually aimed at economic growth, forestalling further adverse effects on enterprises.

Though the Committee had committed not to make changes that might entail a significant increase in the capital requirements for banks, according to the estimates of the European Banking Federation, the risk is there that the proposals put forward, as a whole, may result in a significant increase in capital requirements. Furthermore, the potential impact would be even worse if one also takes into account the new TLAC standards, i.e. an additional capital requirement for systemically relevant global banks aimed to reduce the risk of contagion within the financial system should a system bank face a crisis.

Therefore, while financial stability must be ensured, it is also necessary to avoid in all possible manners that the banks' capital requirements are too stringent as this would bring along a new and further credit crunch.

Finally, on the regulatory front, I can but reiterate the importance of the proposal put forward by the Commission to retain the SME Supporting Factor and remove the cap in respect of €1.5mn loans. Confindustria has been working for a long time on this proposal alongside ABI: it is fundamental for it to be approved in order to support lending to SMEs.

Hopefully, in the end common sense and a focus on the real economy will prevail upon rules. They are decisive for stability, which in turn only makes sense if related to growth.

COMPLETING THE BANKING UNION: OPPORTUNITIES, RISKS AND OBSTACLES

Valeria Sannucci*

The Single Supervisory Mechanism, which was completed in an extraordinarily short period of time, entails very extensive and deep integration of national authorities. While the Monetary Union mostly consisted in the sharing of decision making, the SSM envisages the integration of daily operational processes to be carried out at national and centralized level. Its establishment could have been a prelude to a paradigm shift in the level of European integration. However, this has not yet materialized. On the contrary, the Banking Union is still under construction and significant obstacles remain on the path to its completion.

It was no accident that the original blueprint for Banking Union rested on three pillars (banking supervision, crisis management, and deposit insurance): each one is an integral part of the financial architecture needed to safeguard the soundness and the stability of any banking system, and to break the vicious circle between banks and sovereigns.

If the Banking Union were to remain as it is today, the result would neither be compliant with best practices, nor would it have achieved its intended effects. In fact, as Dirk Schoenmaker put it, now that the immediate crisis is past, 'governments have started to shop selectively on the Banking Union list'.¹ In this 'à la carte' Banking Union, the absence of common deposit insurance increases the risk of contagion, while a blunt implementation of the resolution framework with no public backstop in place would heighten financial stability risks.

European leaders must therefore not lose sight of the end goal and instead complete the project in a reasonable timeframe. The need to press ahead is made even more urgent by the fact that while the European banking and financial system has demonstrated its resilience, its stability is still at risk.

Indeed, risks to Europe's macro-financial stability have recently intensified. While the expansionary monetary policy stance is supporting the liquidity of financial markets, curbing tensions on government securities, and easing bank funding conditions, uncertainties have nevertheless increased following the UK referendum and, though perhaps less so, the Italian referendum. Nor, given political events, expected policy changes in the United States, and fragilities in emerging economies, are

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1. Schoenmaker D., "Firmer foundations for a stronger European banking union", Bruegel Working Paper, 2015/13, November 2015.

they likely to be dispelled over the medium term. European banks' profitability and their business model are under extraordinary pressure, due to sluggish growth, low interest rates and, to a differing extent across countries and banks, excess capacity, large stocks of non-performing loans and difficult-to-value (level 3) assets. Meanwhile, low nominal interest rates are squeezing the profit margins of European insurance companies and pension funds.

While they are more solid today than they were in the pre-crisis period, in the absence of an adequate, proportionate and properly functioning safety net, Europe's banks are also more exposed than before to substantial risks to their individual stability.

A common EU deposit guarantee scheme is a crucial component of the safety net and should be set up as swiftly as possible. While its introduction is generally accepted in principle, controversy has arisen recently regarding its timing and negotiations are at a standstill due to the opposition of some countries.

Introducing common deposit insurance is not enough, though. In order to bolster public confidence and to ensure that the Banking Union has the capacity to safeguard financial stability in adverse circumstances, we also need a common public backstop covering both resolution and deposit insurance.

Furthermore, it is important to acknowledge that the ability of the new EU resolution framework to counter systemic crises has been somewhat overstated, especially when combined with the European Commission's approach to competition and State aid. A 2016 paper by Emiliós Avgouleas and Charles Goodhart warns against large-scale, bail-in centred, recapitalizations and illustrates the "danger of over-reliance on bail-ins" by providing a very insightful description of the risks involved in triggering the bail-in process when risk is not idiosyncratic.² While the bail-in tool is actually well-designed for addressing the crisis of individual banks, in the event of a systemic crisis its use risks exacerbating the threats to financial stability rather than stabilizing the system. In those circumstances, the possibility of temporary public support, without necessarily involving banks' creditors, should not only be considered but favoured, to dispel the fear of contagion and prevent the seeds of another crisis from being sown.

Of course, envisaging public support in exceptional circumstances should not undermine efforts to reduce forms of moral hazard. The risk of imprudent behaviour by banks can be tackled by strengthening the prudential framework, by adapting the structure of remuneration schemes to reduce incentives for excessive risk-taking, and by making management fully liable in the event of the failure of an institution. At the same time, the burden for taxpayers could be lightened by requiring that public funds be recouped from the banking system at a later stage, when financial stability is no longer at risk – as envisaged by the Financial Stability Board.³

2 Avgouleas E., C. Goodhart, "An anatomy of bank bail-ins – Why the Eurozone needs a fiscal backstop for the banking sector", *European Economy*, 2016.2., 5 December 2016.

3. Financial Stability Board, "Key Attributes of Effective Resolution Regimes for Financial Institutions", principle 6.5, 2011.

Let me stress that an incomplete Banking Union is a source of risk in itself. If neglected for too long, it will discourage banks' reorganizations and consolidation processes as the cost of funding and capital remain subject to excessive uncertainty, with likely undesirable effects on banks' ability to support both investment and consumer spending. In this transitional phase, when banks are still building up adequate loss-absorbing buffers and Governments are without their traditional tools of intervention, the risks are even greater.

As it is a priority *per se*, completing the Banking Union should not be conditional on other interventions. I refer, in particular, to the much debated possible change of prudential treatment for sovereign exposures, which is among the measures called for in order to move forward with the creation of the EDIS. A draft report presented to the Committee on Economic and Monetary Affairs of the European Parliament (ECON)⁴ makes the entry into force of the insurance phase of EDIS conditional on reducing risks in the banking sector. In this regard, while recognising that changing the prudential treatment for sovereign exposures could help to break the bank-sovereign nexus, I believe that it should not be considered as a pre-condition for, or an alternative to, the completion of Banking Union.

A clear timeline for deposit insurance, as we had for the Single Supervisory Mechanism and the Single Resolution Mechanism, would help reassure markets as to the soundness of the overall banking framework and the willingness of Member States to pursue the final design of the Union.

In the meantime, the Single Supervisory Mechanism should continue to focus on further strengthening the resilience of the banking sector. However, we should avoid over-calibration and possible inconsistencies between different measures that might impair the ability of European banks to support the real economy.

A path must be identified to guide banks towards adequate levels of capital and loss-absorbing capacity to increase their stability and readiness to withstand adverse market conditions without compromising their capacity to finance the economy and sustain the economic recovery. This is especially true today when banks' profitability remains low and the recovery in the EU is still struggling to gain momentum.

After substantially strengthening capital levels in recent years, EU banks will now be required to increase their loss-absorbing capacity to meet the minimum requirements for own funds and eligible liabilities (MREL). In this regard policymakers face a trade-off: on the one hand, large stocks of liabilities that can feasibly and credibly absorb losses in resolutions contribute to the resolvability of banks and to financial stability, while simultaneously protecting taxpayers; on the other hand, the build-up of adequate buffers of loss-absorbing capacity may be very costly for banks, impair their lending capacity to the real economy, and require time. The review of

4. See European Parliament, Committee on Economic and Monetary Affairs, Working Document on EDIS and Draft Report on the Proposal for a regulation of the European Parliament and of the Council amending Regulation (EU) 806/2014 in order to establish a European Deposit Insurance Scheme (COM(2015)0586 – C8-0371/2015 – 2015/0270(COD)), Rapporteur Esther De Lange.

the legislative framework, starting with the European Commission's proposals, should strike the right balance. In any event, it is indispensable to avoid a needlessly high MREL requirement disproportionate to the effective needs of a resolution.⁵

Let me conclude with two quotations. In a 2016 speech at the EMU Forum, Peter Praet said "Completing the union is sometimes framed in terms of a trade-off between risk sharing and risk reduction [...] I believe both routes need to be followed and to move forward in parallel [...]. A European Deposit Insurance Scheme would enhance overall depositor confidence ... This is the very foundation of insurance: by pooling resources and risks across a larger and more diverse group, the overall shock-absorbing capacity of the system increases. In this sense, risk sharing turns into risk reduction".⁶

In a working paper published a few months ago on the economic governance of the euro area, a group of researchers at the Bank of Italy reviewed the measures taken concerning sovereigns and banks since 2010 and concluded that Europe is now at a crossroads: "either it finds the strength to return to its roots and embraces a second (and deeper) round of reforms based on enhanced risk sharing, or it risks running into pro-cyclical excesses that may finally tear it apart".⁷

This forum may therefore provide a valuable contribution to enhancing the awareness of policymakers about the dramatic, yet possible outcomes of a piecemeal, short-sighted approach to the completion of Banking Union.

5 Bank of Italy, Financial Stability Report No. 2 / 2016, November 2016, p. 36-37.

6. "The importance of a genuine banking union for monetary policy", Vienna, 24 November 2016.

7. Balassone et al., "Economic governance in the euro area: balancing risk reduction and risk sharing", Occasional Papers, Banca d'Italia, 344, 2016.

RESILIENCE, STABILITY AND SOCIAL CONSENSUS

Francesco Mazzaferro*

I would like today to briefly discuss three questions.

First, has EU financial regulation already increased resilience to the point that markets have learned how to withstand important political shocks? Second, how can we help create a Europe-wide social consensus on the macroprudential agenda? And third, how can the ESRB contribute to more stable financial conditions in the single market?

On the first point, let me first observe that we have recently witnessed a number of unprecedented geopolitical events. The United Kingdom, the largest financial market of the European Union – and the European country that is home to the European Union’s lingua franca – is unfortunately leaving the EU, as a political project and as a single market. The result of the recent US presidential election was a surprise to most of us, not least given the extent to which the key planks of the electoral platform differed from the themes and priorities that had become consolidated over time. Given this precedent, the markets might well expect the results of forthcoming political events in a number of other EU countries to be equally surprising.

Some of us may remember how – a few decades ago – political events led to prolonged periods of market turbulence. Take, for instance, Denmark’s refusal to ratify the Maastricht Treaty in June 1992. That confounded all expectations of a smooth transition from the European Monetary System to the single currency and opened up a long period of exchange rate instability which led first to the exit of the United Kingdom from the exchange rate mechanism in September 1992, and soon after to a period of high volatility among core EU member states, which lasted until 1995. We may well be wondering why no such financial shock has materialised now. Of course, with the single currency tensions cannot translate directly into effects on the exchange rate, at least within the euro area. But they can affect other indicators, like spreads, and lead occasionally to overshooting. As we can observe, market movements have been much more moderate in recent times. It is in the markets’ nature to be volatile, and there is no problem with that, provided that volatility does not spiral into fundamental disruptions and even, at worst, into the disappearance at times of transactions in some segments of financial markets, as in 2010-2011.

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Well, that has not happened recently, in spite of the unprecedented shocks. Perhaps this is because the new regulations governing financial markets in general – the packages of rules which were first agreed at the international level, like the ones on banking, but also those governing other areas at the EU level (therefore going beyond international agreements), like solvency requirements for the insurance sector – are delivering exactly what was expected: more resilience. I also think that – despite the surprise factors already mentioned – risks and vulnerabilities are better identified now and corporate governance within the financial sector is generally stronger. The markets can therefore focus more on fundamentals. As today's conference is hosted by the financial sector, I would like to call for a greater appreciation of the medium and long-term merits of a strong regulatory framework: without such a framework, we would perhaps be confronted with more imminent risks of market dislocation.

Turning now to the second topic, let me observe – in a frank and candid way – that almost all of the speakers before me have signalled a sort of national consensus around priorities to complete the European agenda. They have also expressed similar views about certain aspects of EU regulation (for example, the bail-in rules) which are clearly creating concern in this forum. As an Italian citizen living abroad, it is my duty to explain, with respect, that these concerns are not shared elsewhere. For some time now, I have been reflecting on the cultural factors that underpin our work to support financial stability across the European Union. I am more and more convinced that the difficulty of identifying common responses to crucial issues (how to reduce financial risk? what risks to share?) is above all due to the different narratives voiced by public opinion in each of our countries. More than the divergence in views, what is really striking is the ease with which a domestic consensus can be created in different countries around different priorities. In this respect, we are faced not only with technical questions, but also with diverse social preferences. If this conference had been held in a different location, but – in terms of professional and sociological composition – with the same set of participating institutions, most probably the general tone of the discussion would have been similar. The conclusion, however, would have been very different: in some cases, diametrically opposite. This must be a matter of serious concern for anyone wishing to pursue our common European endeavour.

If there are such differences in public opinion across Europe, the duty of all those searching for a European solution must be – first and foremost – to understand the arguments of the other side. This implies that those in favour of risk sharing should consider that they have to work towards risk reduction as well, and must be aware that risk reduction should be proportionate to the risk concerned. In this country, debt is mostly issued by government, in other countries borrowers are mostly households and businesses. Across Europe it is our common duty to think about measures that would reduce the incentives for indebtedness – with a few exceptions, we are over-indebted economies – and correctly price the risks that arise when the economy generates vulnerabilities. It should be our duty as citizens of this country to think openly – in conferences like this one – about whether sovereign exposures need

to be differently treated in regulatory terms, and what commitments we would be ready to propose in this respect. Rejecting any discussion will not help us reach consensus.

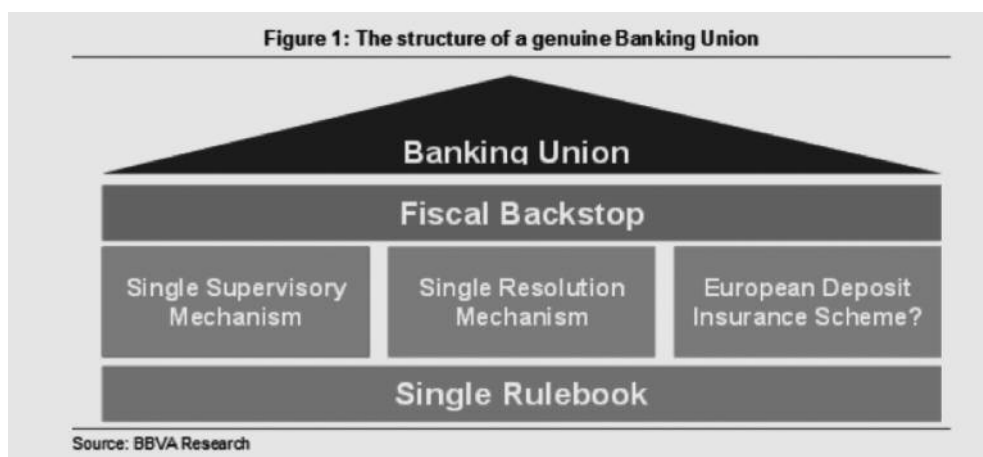
Finally, let me turn to my third point. One of the features of financial markets in Europe in recent years has been the perceived scarcity of safe assets. In fact, in the periods when this perception was strongest, there was only one international safe asset in Europe at the disposal of global financial markets: the Bund, that is, the bonds issued by the Federal Republic of Germany. This has produced a situation where the perception of changes in risk assessment has led to capital movements to Germany, transforming changes in risk sentiment into cross-border transactions. That is why the ESRB has been working – as also explained in a 2016 public consultation – on ways to establish securitised debt representing different tranches of the same set of government debts. The synthetic European bond, which would represent a non-mutualised basket of European public bonds, would consist of senior tranches – offering security – and more junior tranches – offering higher yields. Buying and selling these tranches, market operators would express their investment behaviour in terms of diverse risk sentiment vis-à-vis the same countries and not express national preferences. Work is still ongoing and I hope it will be possible to make more detailed announcements one year from now.

FIXING EMU AND STRENGTHENING EUROPEAN INSTITUTIONS

José-Manuel González-Páramo*

Several years have passed since the outburst of the worst financial crisis in decades and its length and depth have put literally our European economic and political institutions at risk, forcing them to make decisions and take steps into uncharted territory. In 2012, when Europe was on the edge of the cliff, our authorities rightly recognized that the construction of the European Economic and Monetary Union (EMU) was flawed and that we required further strengthening of European institutions.

On the financial side of these reforms, Banking Union emerged as a quantum leap for the monetary union, a major stride towards financial integration and towards the completion of the construction of the euro. The progress so far on achieving Banking Union has been tremendous, indeed inconceivable just a few years ago, as it represents a significant transfer of sovereignty from those countries sharing the common currency to the new supranational authorities. This agreement relies on an unprecedented extent of the solidarity since the birth of the euro. As of today, the first three pillars of the Banking Union – the Single Rule Book, the Single Supervisory Mechanism, and the Single Resolution Mechanism – are up and running. But Banking Union remains unfinished. A European Deposit Insurance Scheme (EDIS) is still missing, as well as a common public backstop to the new Single Resolution Fund. While starting the Banking Union without EDIS or a public backstop was accepted



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temporarily as a lesser evil in order to get Banking Union under way in 2015, it will need to be completed in the near future.

Deposit insurance mechanisms were already established in most advanced countries after the Great Depression of the 1930s. The rationale for insuring bank deposits has always been quite evident; it seeks to reduce the risk of devastating bank runs, such as those which occurred repeatedly during crises in the past. In the particular case of the Eurozone, area-wide supervision and resolution arrangements call for an area-wide deposit insurance scheme which would guarantee that each euro deposited in a bank is equivalent throughout the Eurozone, regardless of the geographic location of the bank that received it.

In November 2015, the European Commission made a proposal for an EDIS: the idea is to build on the basis of the existing national schemes, gradually moving towards a European-wide mutualised system.¹ After more than a year of discussions, there are strong opposing views on this proposal. The main objections are related to the idea that EDIS implies a risk transfer from weak financial systems to sound financial systems, increasing moral hazard problems. Critics argue that a mutualised scheme cannot be put in place until the risks inherent in the national banking sectors have been contained and have become more homogeneous. They argue that progress on EDIS should be conditioned on the introduction of more risk reduction measures, particularly regarding the treatment of sovereign exposures for prudential purposes.

In October 2016, the European Parliament's Rapporteur for EDIS proposed an alternative approach which eliminates the idea of a fully mutualised system. Instead, this alternative proposes a more limited mutualisation with a stronger national component. This alternative would not help to break the sovereign-bank nexus, which is one of the main objectives of the Banking Union. Furthermore, in order to move along different stages in EDIS, this alternative introduces strong conditions in terms of risk reduction (including the revision of sovereign's treatment).

While these concerns, in terms of risk reduction, have to be taken seriously, two facts should be borne in mind. First, the European Commission already launched in November 2016 a comprehensive set of risk reduction measures focused on increasing the resilience of EU institutions and enhancing financial stability, so-called CRD5.² Second, the debate regarding sovereign exposures intersects with discussions held by global regulators in Basel. This debate has just started and different approaches are on the table. The Basel Committee may lead to the establishment of an international

1. Three steps are foreseen in the Commission's proposal. The starting point is a re-insurance mechanism built on top of the national schemes. The second step would see the re-insurance mechanism progressively evolving into a co-insurance arrangement with an increasing share of mutualisation. The third step would be taken in 2024: from then on, EDIS would fully insure all deposits in the euro area.
2. For example, more risk-sensitive capital requirements, in particular in the area of market risk, counterparty credit risk, introducing a binding leverage ratio, Net Stable Funding Ratio and new loss absorbing requirements – TLAC and MREL.

standard in the following years and any change in Europe should be consistent with the global framework to maintain the level playing field.

Ultimately, the asymmetry of the current incomplete Banking Union is paramount and should be solved in the near future. While decisions on supervision and resolution are taken at European level, the mechanisms to protect depositors are still purely national – further perpetuating the sovereign-bank nexus. Therefore, in order to speed the progress on EDIS and complete the banking union, it should not be tied to a specific risk reduction measure, particularly sovereign exposures. It is essential to keep these lines of work decoupled. Pursuing them in parallel as conditioning the progress on EDIS to the revision of sovereign treatment will unnecessarily complicate both. Nevertheless, if conditioning EDIS to some risk reduction measures is ultimately the chosen path, specific and realistic milestones should be set in order to prevent any unnecessary delay on the implementation of EDIS.

Taking a broader view, leaving the Banking Union unfinished is in itself the opposite of risk reduction. In fact, it would increase the fragmentation among financial systems of the member states. As long as national governments remain liable for depositors' protection, markets will discriminate banks based on their location, perpetuating the sovereign-bank vicious circle. Conversely, in a perfect Banking Union, credit rates will keep converging and funding conditions will depend more on the fundamentals of the banks rather than on the country in which they are located. To that effect, transnational banks could operate freely in a broader market of more than 300 million potential customers, which in turn, would benefit from increased competition.

Several experts regard the lack of a safe security as a major weakness in the euro area architecture³. They believe it fuels the vicious circle between governments and banks, as well as destabilising capital flows between member states, particularly in times of crisis. In this vein it is important to note the work that is being developed by the ESRB regarding the potential creation of European Safe Bonds (ESBies). ESBies are the senior tranche of a diversified portfolio of euro area sovereign bonds. These new assets could work as a solution to this problem, since they would constitute a new safe euro area security class without an explicit mutualisation of risks (the combination between diversification and tranches is what confers ESBies the consideration of risk-free asset).

Either way, completing the Banking Union is one of the prerequisites for the long-term economic, financial and social stability of the European Union. Something that becomes more needed than ever when geopolitics threatens less coordination and

3. In a 2016 article Brunnermeier, Langfield, Pagano, Reis, Van Nieuwerburgh and Dimitri Vayanos ("ESBies: Safety in the tranches" VOX, 2016) argue that in the absence of a union-wide safe asset, the Eurozone would be subject to cross-border capital flights when facing financial stress. This situation has the potential of creating important distortions within the Eurozone. On a related paper Brunnermeier, et al. ("The sovereign-bank diabolic loop and ESBies" *The American Economic Review*, 2016) find that the creation of a safe asset would enhance financial stability, and help in the transmission of monetary policy.

more financial fragmentation. As ECB's President Mario Draghi said, "One important lesson from the crisis is that a half-built house is not stable, it is fragile"⁴. Seen from a broader perspective, the process towards a deeper EMU has to be a common challenge: we need a closer economic and political integration in Europe. European Authorities need to tackle the unavoidable, but complex, review of the European Union's Treaties and the necessary transfer of sovereignty to strengthen fiscal and political union. They should focus on more ambitious aims that require a profound rethinking of European and national institutions. However, European countries have expressed differences in terms of their long-term goal with divergent levels of ambition, which could be a stumbling block on the road ahead. Current challenges need all the ability and the far-sightedness of the European political authorities.

The global financial crisis and the euro area crisis have triggered a fundamental reform of banking regulation, but eventually financial stability has been undeniably strengthened and confidence has increased as the link between banks and their sovereigns has eroded. Currently, the context of Brexit and many other Eurosceptic events point to the imperative to act quickly to further strengthen the Eurozone. It is vital to complete the work begun to fully enjoy the benefits of Banking Union. There can be only one rational and sensible European approach to this unfortunate and sad turn of events: a programme to deliver key reforms and to fix an irreversible and demanding timeline, which will help over time to restore the European Union's political and economic confidence among citizens. Europe must not relent or weaken when faced with new uncertainties, but should press forward even more urgently with its key financial reforms. Nothing seems more urgent or necessary at the current juncture.

4. Hearing of the Committee on Economic and Monetary Affairs of the European Parliament, Brussels, 28 November 2016, https://www.ecb.europa.eu/press/key/date/2016/html/sp161128_1.en.html.

BETTER REGULATION AND THE FINANCING OF THE REAL ECONOMY

Giovanni Sabatini*

It is a notable opportunity to share with you our concerns about the future not only of the banking industry but of the European economy as a whole, considering the close links between them.

I'll address you in my capacity as Chairman of the Executive Committee of the European Banking Federation, as I believe the issues we face today – namely getting the European economy back to stable, sustainable, and inclusive growth – need a banking sector that's efficient and profitable at European level, governed by appropriate and balanced regulation.

Let me emphasise that in Europe, where almost 80% of SME funding is based on bank credit rather than on capital market fund raising as it is in the US, we cannot ignore the importance of a stable, profitable and competitive banking sector for sustainable economic growth – the latter being one of the main objectives of the European Union, as clearly expressed in the Constitutional Treaty.

After seven years of new rules and important results, such as the creation of the Banking Union (with regard to the two pillars already completed), I believe that to find the right way forward, a major task facing us is to assess the consistency of current regulation and supervision against the so-called “better regulation” principles.

This is not a theoretical issue for academics, but an aspect that has real practical consequences, of which I will give some examples.

The five main principles of better regulation are accountability – on the part of the regulator and the supervisor – transparency, consistency, proportionality and the focus of the regulations.

In each of these fields there is, unfortunately, still a lot of work to do: before proceeding to produce new rules, I think we should consider whether the current regulatory and supervisory environment is effective and able to produce the best possible results.

The first issue is accountability: the current supervisory framework provides for the European authorities' accountability to Parliament and to the mandate assigned to them.

The first thought that comes to my mind on this issue, and on the issue of the relationship, within the ECB, between the supervisory function and the monetary

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policy function, is the following: are we sure that the mandate of the SSM – which focuses only on stability, without considering how the search for stability impacts on growth – is not due for a rethink?

The issue is the relationship between monetary policy, which – given the weakness of growth and levels of inflation still far from the ECB target – remains extremely expansionary in its efforts to transmit liquidity to the economy, and supervisory policy, whose increasingly detailed rules lead it to constrict the channels that bring this liquidity flow to the economy.

This brings us to the second theme of consistency: are we sure that the whole regulatory framework, informed by the urgency and emergency of the crisis, is wholly consistent?

A Basel Committee publication includes data showing that in 2015 120 documents (including consultative papers and new rules) were issued: a document virtually every two days! Is this really necessary?

I believe the answer to this question also depends on finding the right balance between what needs to be regulated, what needs to be subject to supervision and what, if anything, needs to be subject to enforcement.

The rules should specify and regulate the average behavior of intermediaries – rather than consider every possible dissimilar behavior – including those in the tail of the distribution; otherwise the result is excessive regulation.

It seems that the supervisor, not trusting his supervisory and enforcement capacities, leverages a huge set of rules that can detect all deviant behavior, and the consequence is what we are seeing today: the gradual blurring of the boundary between supervisory regulation and management of intermediaries.

Without going into the details of the non-performing loans management guidelines, put to consultation by the ECB, I will merely observe that the document gets so detailed as to recommend how many phone calls you must make to the debtor in a past due or impaired or non-performing situation. This is no longer just supervision, it is management.

The third principle of transparency is required, for example, in relation to supervisory processes such as the SREP. The requirement is not there in order to know the method to be able to bypass it, as some argue. On the contrary, it exists to help show us how banks are evaluated, or to strengthen the aspects that will be subject to supervision. Transparency also means knowing the competitors against which bank ratios are compared in order to assess the sustainability of the bank business model.

Proportionality is also important, meaning that the measures taken must be proportional to the risk being prevented.

I believe that each of these themes must be assessed and discussed.

One example of something that, in my view, does not reflect the principle of transparency and consistency is the new package of rules proposed by the Basel Committee. It focuses on the output floor, aiming to fix the banks' minimum capital levels using the Internal Rating Based (IRB) models rather than the standardized approach. It is still an open issue and may be subject to compromise. The point is that

the output floor tends to overlap with another prudential requirement, the leverage ratio, without any clear consistency between these two standards.

Finally, I'd like to comment on the issue of weighting of sovereign risk exposure, which has long been the subject of far-reaching discussions across Europe. I think it is only a European issue. We talked about it in the context of the IBfed – the International Federation of the national banking associations – at a meeting in Beijing: Americans, Canadians, Indians and Japanese, for example, do not consider it an important issue. They said, "Why do you have this problem? You are the only ones with this problem"

It is perhaps no coincidence that the Basel Committee working group dealing with this matter is not making great progress. Also, I think this issue needs careful thought in order to establish whether it is appropriate and indeed necessary to amend the existing regulatory framework; i.e. we need to assess the actual risks and possible implications of sovereign risk weighting.

In conclusion, before proceeding to propose new rules, I think it would appropriate to pause to reflect and to develop a "comprehensive assessment" of what has been done. This does not mean being critical in a destructive way. Indeed, I believe that strengthening the existing institutional and regulatory frameworks, in line with the general principles of better regulation, is in the best interests of the relevant institutions, to strengthen their credibility and their understanding and acceptance by European citizens.

FINANCE FOR INNOVATION AND INFRASTRUCTURE

THE ROLE OF INSURANCE FOR LONG-TERM INVESTMENT

Maria Bianca Farina*

At present, the issues of innovation and infrastructure are crucial: in a globalized economy, they represent two key drivers for a country's competitiveness and growth. They are also linked to the issue of sustainable development.

As far as Italy is concerned, the infrastructure gap is a well-known problem and we are aware that a lot remains to be done; the same is true for innovation.

In order to progress in these two areas, an adequate flow of financial resources is needed, aiming at supporting future projects in a long-term perspective.

At the moment, however, financial flows are largely insufficient, both at private and public level (in this latter case, also because of budget constraints). In short, supply and demand for long-term financing do not fully meet.

In my speech I would like to say a few words about this issue, seen from the perspective of the industry I am representing, namely insurance.

INSURANCE AND LONG-TERM INVESTMENTS

Official data confirm the importance of insurance companies as institutional investors: nearly 700 billion euro were invested by Italian insurers in 2015, mostly in the financial market.

Another important feature is that the insurance business model – especially for life insurers – is typically based on a long-term horizon. In other words, the long duration of commitments towards policyholders reduces – in comparison with other intermediaries – the insurers' exposure to liquidity risk and allows the adoption of long-term investment strategies.

In addition to this "structural" feature, some other factors are at work: they are linked to the current economic and financial situation and explain why the insurance industry is more interested than in the past in some specific forms of investment: for instance, the financing of small/medium-sized enterprises (SMEs) or of infrastructure projects. I am referring to the current scenario of low interest rates, which urges insurers to look for alternative investments, in search of higher returns. As a matter

* President, Italian National Association of Insurers Companies – ANIA.

of fact, such returns are necessary in order to cope with commitments towards policyholders and to achieve a wider portfolio diversification.

But let's stick to the Italian case, where the current scenario of low interest rates is putting insurance segregated funds returns under heavy pressure. At the end of 2015, guaranteed savings represented 73% of total life insurance products, while investments covering such savings were still concentrated (66% of the total) on Government bonds.

This situation emphasizes the need to pursue further diversification, both for insurance products and the related investments.

A STILL LIMITED INVOLVEMENT

Therefore, at least in principle, we have the required conditions for greater involvement of insurers in infrastructure and innovation projects financing. However, figures show that the involvement is still limited, both in Italy and in Europe.

At European level, some big players¹ have already made a step towards an increased diversification of asset allocation: while Government bonds represent roughly 40% and corporate securities 30-40% of total assets, the weight of alternative investments is growing and accounting for 12-14% of the total.

However, there is still room for further growth.

At present, for example, the insurance industry globally contributes for only 8% to private equity investments. More important, but still with further potential for growth, is the insurance participation to the private debt market (about 14% of the total).

As to the Italian insurance market, the results of a sample survey – carried out by ANIA in 2016 – showed that insurers have invested about 7% of total assets covering technical provisions in alternative investments, exposed to credit risk, largely represented by private placement.

Despite the real interest, both infrastructure and SMEs financing from insurers still have a modest extent.

What are the reasons?

An answer is partly provided by a 2016 survey carried out by Insurance Europe – the Federation of European insurers – on the issue of infrastructure financing².

On the one hand, the survey has confirmed insurers' interest in such forms of investment; on the other hand, it has also shown a serious flaw, concerning the real supply/availability of infrastructure projects eligible for investments.

The Juncker plan has represented an important step to ease the flow of private funds towards long-term financing. However, despite recent improvements both in

1. Reference here is to Allianz, Axa and Zurich.

2. Insurance Europe, "Survey: Insurers' interest in investing in infrastructure growing, but supply of suitable assets must increase", Bruxelles, 19 Dec. 2016.

transparency and accessibility, the visibility of such projects is still insufficient. Besides, the associated political risk is high.

WHY REGULATION IS IMPORTANT

When assessing the still limited insurers' involvement in SMEs and infrastructure financing, another issue to be considered is regulation.

As it is known, several regulatory changes have been introduced in Italy during the last two years, aimed at broadening the investment opportunities for the insurance industry (for example, through the "Competitiveness" Decree" in 2014). Furthermore – on the European side – the "Solvency II" framework took effect on Jan. 1st, 2016, establishing a direct link between investment risks and capital requirements.

As regards infrastructures, for instance, the original calibration of capital requirements treated them – depending on their technical form – as investments in bonds or in unlisted equities, with heavy charges in terms of required capital (for instance, referring to unlisted shares, the capital requirement is calculated on a shock assumption of 49%).

A "last-minute" change in the Delegated Acts has improved the treatment of investments in "eligible infrastructure" (those featuring a better risk profile), which now differ from ordinary investments in bonds and equity. However, definition criteria for "eligible" investments are still very restrictive, with the result that only a few infrastructure projects can be included.

Besides, further work is foreseen in order to improve investments in infrastructure corporates, currently excluded from the "eligible" category.

Further progress in the regulatory framework might derive from the "Capital Markets Union" project: the introduction of a specific treatment for "*Straight, Transparent and Standardized Securitization*" (STS) is envisaged, as well as a review of the treatment applied to private placement and private equity.

In the regulatory field, an important initiative for the insurance industry is the "Solvency II Review", to be completed not later than 2018. The Review should be an opportunity to refine the current prudential framework, in order to remove any unjustified constraints on long-term investment. In that context, an improvement of the treatment of equity investments, for example, should be carefully considered.

CONCLUSIONS

In all countries, infrastructure and innovation projects represent two major drivers for competitiveness in a globalized economy.

In Italy, the infrastructure gap is still high and innovation is held back by lack of adequate financial resources.

It is necessary to support and develop initiatives in these two areas, through an adequate flow of long-term funds.

The insurance industry is a major institutional investor, and some peculiar structural/economic features (nature of the business model, prolonged scenario of low interest rates) increase the appetite for alternative forms of investment.

At the moment, however, the involvement in infrastructure and SMEs financing is quite limited, given the still scarce supply – in Italy as in Europe – of “suitable” projects (in terms of risk/return/transparency). Besides, the European legislation is still penalizing long-term investments.

We need to work together to overcome these difficulties, encouraging investments aimed at supporting firms and economic growth, a source of benefit for the whole Country.

THE EUROPEAN PARLIAMENT FOCUS ON FINANCING INFRASTRUCTURES AND INNOVATION

Simona Bonafé*

Today I am taking the floor as the Vice-president of the Long Term Investment and Reindustrialisation Intergroup. A few words to present this experience. The Intergroup was created in 2014, at the very beginning of this legislature. At that time, the discussion on the effects of the austerity dogma was ready to begin. We were well aware of the huge work ahead of us, in view of facing both a deeply damaged economic situation under the effects of the crisis and an impressive investment gap. Without a strong boost to investments, the desirable return to growth would have never been possible. For this reason, with other colleagues from different political groups, we took the initiative of constituting a cross-party context where promoting vibrant debates on investments and on the real economy. The Intergroup was therefore created in the full knowledge that the lack of investments was not only linked to the crisis but also to structural and regulatory limits of the European economic and financial architecture.

Our main goal was, and remains, to gather around the same table those actors that, through structured discussion and coordination, can make the right choice for Europe in terms of boosting and promoting investments; I am talking about decision makers, investors as well as project makers.

Coming back to the actual topic of the panel, I believe that the strategic role finance can play in the infrastructure's modernization process is a paramount point in the context of this debate. When discussing infrastructure, the role of material facilities, such as roads, ports and railways, essential in stimulating national economies, isn't the only variable at play. Digital infrastructures, as broadband internet, digital platforms or networks, are key sectors to look out for when planning of the economy of the future. Moreover, global challenges are closely linked to infrastructure's developments: first among all, the fight against climate change. Supporting the energy transition, aiming at a low carbon and resource efficient society in accordance with our commitment following the Paris agreement requires, beforehand, the development of new smart infrastructure. Focusing on infrastructure is not only about modernisation, but it also means working on interconnection within a truly European dimension. And, turning back to energy, the potential of an efficient Energy Union with strong interconnections is more than promising, both in terms of security of supply and savings for consumers.

* Vice-President, Long-Term Investment and Reindustrialisation Intergroup, European Parliament.

There is inevitably a reason why I'm bringing these points to your attention: we all know that one of the financing streams of the new EFSI will be devoted to the so-called green infrastructure.

Obviously, the challenge posed by infrastructure cannot be faced by public budgets alone. As of today, the EU budget is still extremely weak and constantly exposed to new emergencies: let us recall the migration crisis or the natural disasters, such as the extremely damaging series of earthquakes, which have recently shaken up Italy or the floods in Germany. On top of that, Member States' budgets are characterized by an increasing asymmetry, further widened by the crisis. In this situation, we must value developments at the European level in the field of investments. In this way, the European Fund for Strategic Investments is now reality, together with the important Communication on flexibility, a concrete first step forward, though still inadequate.

Have we solved our investment problem through the EFSI? Clearly not. The depth of the current gap would require initiatives on a completely different scale. However, the "Juncker Plan", with its logic of combining public guarantees with private investments, is finally giving its contribution in "pressuring" the political level onto dealing with the most controversial points regarding European investments. This includes strengthening related projects and their visibility, facilitating private investors' participation and, last but not least, implementing the blending of funds while differentiating the sources of financing.

On the quality of projects, the Advisory Hub set up under EFSI is up and running, but still presents some space for improvement; to this regard, the Commission has expressed its intention to extend the Plan in view of further improving and strengthening its functioning. A first priority would need to be set to strengthen the interaction with financial institutions characterized by a more rooted knowledge, such as National Promotional Banks.

Coming to the private contribution to infrastructure's modernisation, the peculiarity of such investments should be properly assessed in terms of risks. While in the context of Solvency II some progress has been made within the insurance field, there are strong concerns that under the revision of Basel 3 there might be some negative effects on the involvement of banks. Under political responsibility, we value the importance of prudential criteria; however, we need to remember that being unable to differentiate among different types of exposures can potentially generate negative effects.

Finally, turning to the issue of financing sources. The current European system is still highly centred on bank credit. If we compare our situation with the one of the United States, our delay is quite evident. The US share of investments collected through venture capital is currently five times higher than ours. A Commission's initiative under the work-in-progress Capital Market Union would be more than welcomed. On the same level, we will keep our eyes focused on the implementation of the blending of different funds, especially Structural Funds and EFSI.

Moving from infrastructures to innovation, once again it easily comes to mind the explicit reference to "reindustrialisation" our Intergroup calls for in its name. Our concept of industry is based on innovation: let's call it an industry 4.0. If we really want the industrial sector to get back representing the 20% of the overall European GDP, we will have to move away from traditional tracks and make arrangements in order to proceed at a fast pace. This also means creating the right conditions to allow the most dynamic sectors, which have shown impressive growth potential on global markets, to prosper also within the European economic framework.

From decision makers' point of view, this requires efforts in drawing up a consistent and forward-looking legislative framework. When dealing with structural changes within the industrial and economic paradigm, we need to be very clear on rules and targets or, otherwise, the EU investments' level cannot be expected to rise up again at its pre-crisis levels.

In conclusion, given that the greatest incentives for innovation usually come from within market, we need to focus our attention on how hard it is for European innovative enterprises to see their projects properly financed. During today's debate, the topic will be discussed in all its aspects. Progress in the field of the capital market, steps to be taken in the Single Market, diversification of financing sources, standardisation for more attractive and measurable investment opportunities as well as the completion of the Banking Union, are only a few among the many priorities. Finally, yet importantly, let me also mention the need for more uniform fiscal rules, which could put the EU on the right path towards a more effective Economic and Monetary Union.

A few words on innovation: in 2016 we have held in Brussels a debate with the founder of Bla Bla Car, one of the most promising realities born in Europe in the field of the digital economy. He clearly explained the company's difficulty in facing 28 different regulatory frameworks. Now, if for a successful case, deemed to reach a turnover of over 2 billion euro, this represents a serious challenge, I'll leave to you to imagine what this can mean for a start-up moving its first steps.

Coming to my conclusions, it is worth repeating that economic growth must reflect developments in the real economy. If this link is not preserved, any political projects will face social unrest as well as the lack of perspectives for citizens. Anyone familiar with the European institutions should keep this in mind, by drawing attention to this essential condition among the priorities in Brussels' political agenda.

The EU is currently going through one of the most challenging periods of its young history, and that especially within its relations with its own citizens: for the first time, the European project is perceived more as a limit than as an opportunity. This trend can and must be inverted.

On the International scene, only united we can count and, therefore, guarantee precious growth opportunities to our citizens. For this reason, it is not the time to be shy. We must move forward with ambitious projects, such as the completion of the Banking Union, the Capital market Union and the strengthening of the Economic and Monetary Union's goals. Those are the only steps that can provide real opportunities of growth and development.

A NEW PARADIGM ON INVESTMENT

Valeria Ronzitti*

INTRODUCTION

CEEP represents, at EU level, employers and providers of public services and SGI, active in sectors such as central & local administrations, healthcare, education, waste management, energy, transport, water, environment and telecommunications. As one of the three general cross-industry social partners (alongside with the ETUC and BUSINESSEUROPE), CEEP is active in the European Social Dialogue, exchanging on a regular basis with the EU institutions on the investment strategy set in place by the European Commission.

Since 2014 and the election of Jean-Claude Juncker as President of the European Commission, the mindset changed at EU level. The focus slowly but surely moved away from deficit reduction and budget cuts, and bringing investments back to Europe became a new priority. A “virtuous triangle of structural reforms, responsible fiscal policies and investment”¹ has been put in place. Two years later, we will be able to assess the new policy mix, and see how we could improve it, by engaging in further reflections on the macro-economic governance of the European Union.

A NEW PARADIGM ON INVESTMENTS

For the past few years, the narrative and the policy choices made around “investment” has drastically changed. Since Jean-Claude Juncker and his team entered the European Commission, a clear impetus has been given to trigger investments in the EU. Launched in 2014, the Investment Plan for Europe best showed the new political will, with a vision and a call to act quickly. So far, the balance sheet of the European Fund for Strategic Investments can be seen as fairly positive. Since December 2016, investments related to EFSI have been approved for a total of €163.9 bln. However, we believe

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1. COM(2016) 359 final – Europe Investing Again – Taking Stock of the Investment Plan for Europe and Next Steps, Communication from the Commission to the European Parliament, the European Council, the Council, the European Economic and Social Committee and the Committee of the Regions.

that not enough is being done regarding social infrastructures, accounting for less than 5% of that total, and not enough is done for investment in innovation, compared with "classic" physical infrastructures.

There are obviously exceptions, and some projects which received funding through the Investment Plan promote a

different vision, such as the project on Smart Public Building in Greece and the project promoting the development and the better use of Internet of Things technologies in public buildings. Those remain exceptions, and are all too rare since the launch of the Plan in 2014.

In this context, CEEP welcomes the proposal of the European Commission to prolong the lifespan of the EFSI, and believes that a step forward should be taken by fixing the loopholes observed in the first version of the plan. Providers and employers of public services call for:

An increased focus on the additionality principle;

An improved coordination between EFSI and the other financial instruments (ESIF, Horizon 2020, Connecting Europe Facility, structural funds);

A reinforcement of the diversity of the geographic coverage.

A CALL FOR A HONEST AND NON-DOGMATIC REVIEW OF THE STABILITY AND GROWTH PACT

However, the Investment Plan alone will not be enough. Investments in social infrastructures, and in general all kinds of investments in public infrastructures, will not reach the desired level if policy makers do not adopt a comprehensive approach to tackle the obstacles to investment. There is a paradox at EU decision-making level between the calls for increasing budgetary discipline, and pointing out at the same time to the lack of investments as one of the main reason for the persistent slow pace of the economic recovery.

We must now end the stagnation in the public capital stock which we have witnessed since the crisis. Investments aimed at increasing productivity is the best way to achieve this. It seems at times as if we suffer from a lack of understanding of the added value of public investments. For example, in the field of education and health care, investments contribute to reinforcing the human capital stock, enhancing the supply side of the economy and contributing to growth. However, it is still mostly considered to be current expenditure rather than investment.

The main problem is that the fiscal rules do not make a distinction between operational expenditures and investments. The situation has become even worse since the application of the European System of National and Regional Accounts (ESA 2010, in force since September 2014). It means in practice that public investments are calculated in the Stability and Growth Pact's deficit and debt criteria over the short period of the construction duration, whereas they should rather be considered as long-term investments, and be written off over a far longer period of 15 to 20 years.

This issue may only be the tip of the iceberg when we consider the full consequences of the Stability and Growth Pact on public investment in Europe. To address this issue, we must now take a step back and decide collectively which form of expenses are indispensable to our relaunch and should accordingly be supported by the EU and Member States, not only politically but also technically. This implies an honest and non-dogmatic review of SGPs, including its interpretative communication of 2015.

CONCLUSION

In conclusion, we can try together to figure out what the missing link is. The evidence supporting the call for investments is clear. The academic case calling for increased investment to support economic growth has been made. Only the political will to go further must be tackled. My advice would be to use events such as the Rome Investment Forum as a means of pressure. We need to stop “speaking to ourselves”, and now need to reach out to those who still need to be convinced.

THE CASE FOR AN INVESTMENT/PRODUCTIVITY COMPACT IN THE EMU

Rainer Masera*

A key feature of the macroprudential paradigm of political economy is the focus on: (i) the links and interactions of the various economic policies (and, therefore, the effectiveness and potency of the policy mix), (ii) the role of fallacies of composition/division and (iii) the prominence of a medium term reference framework, to capture transition and aggregation processes. In the Euroarea, this complex approach goes beyond political economy and addresses directly the issue of political union. The Eurozone must be seen as a network of economic policies, governance and political integration. This broad approach should not however become an excuse to avoid a critical analysis of the economic policies pursued since 1999: there is the need for an in-depth rethink of the Euroarea economic policies. A key point is the alleged “fact” that a close relationship exists between the monetary base, money supply and prices.

The links between fiscal, monetary, credit and bank capital policies should be reassessed, without putting into question the objectives of fiscal rehabilitation, price stability and sustainable growth. The issue is not so much that of flexibility, but primarily of redefinition of the appropriate policy mix, which now puts an excessive reliance on monetary policy, and may ultimately result in perverse effects on systemic risks, and possibly – over time – on inflation itself.

The overburdening of monetary policy opens up also the issue of corporate governance of the ECB, which has full institutional responsibilities for monetary, liquidity, and bank surveillance policies and de facto plays key roles in lending of last resort, in macro prudential policy and in the elaboration of the Basel capital standard regulatory framework. Additionally, with the EAPP, it has acquired important institutional spillovers (which fall outside the traditional domain of central banking) and external role, notably in respect of the exchange rate of the Euro (according to Art. 111 of the Treaty foreign exchange policies should be jointly decided by the Council of Ministers and the ECB). All these competencies may lead to potential conflicts of interest. In any event, the approach of the Maastricht Treaty (single instrument, single goal, fully independent central banking) requires review.

A central point is represented by the contradictory effects of (i) ever increasing capital/liquidity and other requirements on banks – including incomplete/unsati-

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satisfactory rule-making on resolution mechanisms –, and (ii) the simultaneous pursue of continued loosening of monetary policy/negative interest rates. The constraints on banks affected and continue to affect growth. This creates a vicious circle. The aim of microprudential safety and soundness becomes contradictory with the macro prudential requirement of balanced growth. Financial stability requires soundness of the banking system. But, financial stability also requires growth: the trade-off between regulation and growth is an issue of social cost-benefit analysis: the EU (one-size-fits-all) approach has gone too far in increasing requirements on banks. This affected growth and thwarted monetary policy. Also of great concern is the “collateral damage” resulting from the conjunction of: (i) the EC untired banking regulation and (ii) the ECB negative interest rate policy. This has a profound negative effect on the profitability of banks, and notably of “traditional” small and medium sized banks, and hence on their possibility to raise fresh capital. On the other hand, wholesale-finance specialty banks (notably leasing, factoring, consumer loans...) benefit from the availability of low-interest funding from the Central Bank and the parallel decline in borrowing and lending rates.

The United States experience offers evidence of a radically different approach to these issues (TARP, GSE, temporary suspension of mark-to-market accounting, support to securitisations and, above all, a tiered regulatory framework). The tiered approach is in the realm of the American law balancing principle. It is somewhat surprising that the corresponding German (Prussian) proportionality model has not been followed in the area of (level 1) Banking Regulation by the EU. An important recognition of the need to reassess the regulation/growth trade-off had been made by the former Commissioner Hill.

A second clear instance of a wrong policy mix is offered by monetary and fiscal policies. Fiscal rehabilitation and the reduction of debt/income ratios are a highly desirable objective, but the austerity approach – as concretely applied, with emphasis on the short-term budget balance in all countries simultaneously – contributed to vicious loops. The outcome in terms of lower output and higher unemployment has been underestimated: hence, the ratios of debt to income increased in many countries with high debt ratios. In Italy, for instance, the increase in the ratio was especially high during the austerity-driven Monti and Letta governments. These perverse effects were heightened because of (i) the insufficient thrust of consistent structural policies, (ii) the inappropriate burden of the banking regulation concretely implemented in the Banking Union framework, and (iii) the fact that certain countries have been characterised by very high current account surpluses which exacerbated the paradox of saving (let it be recalled that the cumulative current account surplus of Germany and Netherlands since the introduction of the Euro is close to €3 trillion). The burden on monetary policy to avoid deflation/depression became higher and higher: the ECB had to stand alone for nearly a decade to prevent the dissolution of the Euro, but the collateral negative effects create increasing damage.

There is a clear need to combine the appropriate fiscal and monetary actions with well-designed, mutually consistent structural policies. This underlines the medium term nature of economic policy processes. A key structural policy to be adopted through

a concerted action by Eurozone countries would consist in ensuring tax neutrality of debt and equity, which is key to overcoming the paradox of de-leveraging in the private sector. This is especially important now: the perverse effects of the combination of very low/negative interest rates and of tax incentives for debt are evident: financial bubbles may put at risk the long-term stability of the Euroarea. Saving is penalised in the attempt to reduce the imbalance between saving and investment! More specifically, pursuit in the area of a single overburdened monetary policy, of constrained fiscal impulses and of uncoordinated structural policies may prove inconsistent with complementarities over time and space of successful trajectories of structural change, and therefore with an effective inclusive political economy of interdependence.

It has been argued that interest rates are negative in the Euroarea fundamentally because of an excess of saving over investment. Also from this point of view, it is necessary to foster investment from the lows recorded in the past decade. The European investment plan – as is certified by the EFSI and the EIB – shows that there are ample opportunities for public and private investments in infrastructure, human capital, the environment, innovation, with positive social and private returns. These investments also yield significant returns in mitigating the adverse impact on low income groups of fiscal consolidations.

If public investment projects are rigorously selected and undertaken on the basis of economic return, effectiveness and cost-efficiency – preferably within a PPP framework – public and private investment become fundamentally complementary. Under the conditions outlined, public capital has a crowding-in effect on private investment: increases in public capital raise the marginal productivity of private capital. These arguments carry special weight in the current situation of excess saving, negative nominal interest rates, and slowing multi-factor productivity. The Ricardian equivalence preoccupations recede (the marginal productivity of new investment outlays is higher than the nominal and the real cost of funding).

A compelling case can therefore be made to adopt now in the Euroarea a, say, three-year productivity-investment compact to reinforce the Juncker Plan. More specifically, public investments selected by the EFSI – with direct country contributions to its capital, in the form of guarantees or cash – would be exempted from the Stability and Growth Pact, possibly up to predetermined ceilings. The proposal made here: (i) ensures the effectiveness and productivity of new public capital, financed at negative interest rates; (ii) helps overcome the current market failures and inappropriate burden of monetary policy; (iii) ensures that EFSI – financed projects are allocated on their merits in a European perspective, and not on the basis of national keys. The problem of “juste retour” would thus be overcome. Under the special circumstances of the EMU process and the vital need to foster growth, innovation, productivity, a forward-looking D/Y fiscal policy framework would therefore temporarily be adopted (with the emphasis on the sustainable decline of the ratio, and not on the actual decline of the stock of public debt). Admittedly, this might require in Germany a rescheduling of the debt-brake policy at the federal level (e.g. from 2016 to 2020 as already envisaged at the level of the regional governments). As in-

licated, this programme would be accompanied by precise commitments of Member Countries to ensure coordinated in-depth structural reforms to help raise sustainable, inclusive economic growth, and to enact the Capital Markets Union.

A final point is the need to reconsider also the international financial architecture in which Eurozone policies are necessarily inserted: in particular, the simplistic approach to the exchange rate and to external imbalances must be questioned. The assumption according to which the market is left to determine the Euro exchange rate, so that the ECB can direct money and credit policies to the domestic objective is evidently reductive. EMU growth should be anchored to sustainable expansion of domestic demand in the internal market, not to net exports and a depreciating Euro.

**FINANCE FOR COMPETITIVENESS, ENTREPRENEURSHIP
AND SMALL ENTERPRISES**

COMPETITIVENESS AND SMES IN THE CONTEXT OF CAPITAL MARKETS UNION

Steven Majoor*

I am delighted to have been invited to discuss the issues of competitiveness and Small Medium-sized Enterprises (SMEs) in the context of the Capital Markets Union or CMU.

As you are no doubt aware, the objective of the CMU is to develop stronger and deeper capital markets in the EU to allow funds to flow to European companies, benefiting the real economy, through growth and investment. In light of the relatively recent vote in the United Kingdom, I believe it is crucial to maintain, and even increase, the momentum of the CMU. I say this because while the European economy needs to be able to rely on funding provided by the banking system, the current over-dependence on banks is not optimal for developing our businesses and consequently, economic growth.

There are, of course, a number of alternative sources of finance which together can create a more diversified system of funding, with greater involvement from institutional and non-bank investors. I will focus shortly on the opportunities which crowd funding, asset management and FinTech can offer to help us accomplish this funding diversification and the work we at ESMA are doing in these areas. Increasing the role of the non-banking sector will not only help businesses access much needed capital but should also help the EU in making a shift from debt to equity funding. This is an important shift to make if we are to remove the barriers that prevent our entrepreneurs and SMEs from flourishing.

The CMU is so important for SMEs because they are an important source of economic growth and job creation, yet many of them face challenges accessing financing. In the EU, less than half of SMEs (44% in 2016 compared to 41% in 2015) say that they do not feel there are limitations on their access to finance and indeed, SMEs do not enjoy the same level of direct access to capital markets as large companies do. In the EU especially, where bank financing has the lion's share, they remain overly reliant on bank credit.

Credit conditions have generally improved recently thanks to an accommodative monetary policy. However, while interest rates have tended to trend downward, the interest rate spread between loans to SMEs and to large companies remains high when compared to pre-crisis levels, suggesting that banks remain wary of SME financing. Also, conditions vary greatly across countries in the EU. In Italy, SME in-

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terest rates declined by 21% between 2012 and 2014 but the interest rate spread between loans to SMEs and to large enterprises is three times what it was in 2007.

Against this backdrop, access to finance, and the need for alternative funding channels, facilitating this access for start-ups and other unlisted firms, including SMEs, is more acute than ever. So now let me turn to some of these alternatives and ESMA's work on them, starting with crowdfunding.

CROWDFUNDING

Crowdfunding enables small businesses and SMEs to raise finance directly from the public, potentially at a relatively low cost and in the current climate may be the only way these firms can raise capital, e.g. because of their small size, elevated default risk or high associated costs. Crowdfunding, therefore, provides a much needed alternative to traditional funding sources and by offering an online marketplace to match potential investors and businesses, crowdfunding can bring more competition into retail and capital markets.

That being said, and although crowdfunding is growing quickly, capital raised in this way remains limited compared to other financing sources. 2016 estimates suggest that between EUR 4.1 and EUR 5.2 billion were raised through crowdfunding platforms in 2015 across the EU. Investment-based crowdfunding alone – the focus of ESMA – accounted for about EUR 0.5 to 0.6 billion, i.e. around 10% of the total. Business finance, i.e. financing provided to businesses, represented EUR 0.5 billion and 9,442 businesses. Those figures are pretty small when compared to other sources of funding. For example, stocks of loans to businesses from EU banks totalled EUR 5.3 trillion at the end of 2014; the amount of venture capital invested in European private equity totalled EUR 5.3 billion in 2015.

Also, crowdfunding is not exempt from risks. In ESMA's 2014 Opinion and Advice, we highlighted those risks, such as the significant potential for investors to lose some or all of their capital, the lack of exit options and the limited information available on the investment. We also advised EU legislators to consider the gaps and issues in the current regulatory framework in relation to crowdfunding with a view to both supporting the growth of the industry in the EU and addressing the risks that may emerge.

PROSPECTUS

Let me now turn to prospectuses, those documents which are often seen as the gateway to capital markets.

On 7 December, the European Council and Parliament agreed on a new set of rules that support companies raising money on capital markets. These new rules will exempt the smallest capital raisings from the burden of producing a lengthy and expensive prospectus: start-ups and SMEs will be able raise up to EUR 1 million on lo-

cal markets without a prospectus. Member States will also be able to set higher thresholds of up to EUR 8 million to support growth in their domestic markets.

There will also be a new EU growth prospectus for SMEs and mid-caps which want to raise money across the EU. While the broad parameters of this growth prospectus have been set out by the co-legislators, ESMA is developing the precise disclosure that will be required in such a document and we aim to consult on the precise provisions towards the middle of 2017. The disclosure burden of this document should be significantly alleviated in comparison to issuers seeking to raise funds on regulated markets.

ASSET MANAGEMENT

In addition to our work on crowdfunding and prospectuses, earlier this year ESMA started developing what it considers to be the key elements of a common European framework for loan origination by investment funds as another strand to fostering a more diversified range of funding in the EU. In April we published an Opinion on this issue.

In the Opinion, we made some suggestions regarding organisational requirements for managers of loan originating funds. These recommendations take account of the fact that direct lending is an activity that requires specific expertise and internal structures. While it would not be appropriate to impose exactly the same rules as those which apply to banks, there are certain key elements which we believe should be in place before a fund can originate loans. These include having the requisite policies, processes and procedures with respect to credit monitoring, renewal and refinancing, assessment and scoring of borrowers, and identification of problem debt management. Such requirements should help reduce the risks that could arise from liquidity and maturity transformation, as well as imprudent lending.

As a final remark on this topic, I would like to highlight our recommendations on eligible debtors of loan funds. In line with one of the overall objectives of CMU to increase funding to the real economy, we took the view that loan funds should not be able to grant credit to financial institutions, other investment funds or the alternative investment fund manager itself.

Looking to the future, to help increase competitiveness in the asset management sector overall, which is a key goal of the CMU Action Plan, ESMA will shortly embark, together with the other European Supervisory Authorities, on an exercise to bring greater transparency to the fees and performance of long term retail investment products. Providing European investors with a better basis for comparing investment alternatives is expected to be useful for investors as well as for supervisors, notably to identify areas of weaknesses across the EU. In doing so, this exercise will also shine a light on the level of competitiveness in the asset management sector.

FINANCIAL INNOVATION

In terms of competitiveness more generally, ESMA does not have a mandate to support competition as such but we do have an objective to ensure market integrity, and as part of this objective, we focus on safeguarding a level playing field for market participants.

Technological innovation in financial services is not new but FinTech investments have sky rocketed recently: KPMG estimates that they have risen six-fold in the past three years globally. We see FinTech as another evolutionary step in the long history of financial innovation rather than an abrupt departure. In the FinTech sector there are many start-up firms which may compete with or collaborate with established firms as well as established firms also developing FinTech innovations themselves.

Although the level and pace of FinTech disruption varies across sectors and products, three elements are common to the broad range of FinTech phenomena, namely (i) improved service and convenience, (ii) greater efficiency and (iii) decentralisation and disintermediation. These three elements support greater competition in the market place and help create better outcomes for customers.

From a regulatory standpoint, FinTech poses specific challenges to regulators as existing regulation was not designed with these innovations in mind. We have taken a balanced approach to innovation in general and FinTech in particular. We are vigilant in analysing any new risks that the technology may introduce that threaten our objectives of investor protection, financial stability and orderly markets. At the same time, we do not want to stifle innovations that will benefit consumers and markets.

Specifically in the FinTech context, we are looking at areas such as automated advice and distributed ledger technology (DLT), both in terms of the risks that are inherent in both and their potential to make it easier for parties to transact directly with one another, thereby reducing the costs of intermediation.

Let me very briefly conclude by saying that the CMU is an ambitious initiative which pushes in the right direction. The combination of the initiatives that I have mentioned today should go some way in terms of making capital easier to access for small business and SMEs.

SUSTAINABLE LONG-TERM INVESTMENT AND THE PAN-EUROPEAN PERSONAL PENSION PRODUCT

Gabriel Bernardino*

In my intervention I would like to point out:

- First, the EIOPA's work linked with long-term infrastructure investment.
- Second, EIOPA's work on a Pan-European Personal Pension Product, the PEPP, in the context of the Capital Market Union.

To my first point, about EIOPA's work linked with long-term infrastructure investment.

Solvency II is a huge step forward in policyholder protection but also a game changer as regards the capacity of insurers to invest over the long-term. In fact, the implementation of a risk-based capital regime comes with profound changes in the way investments are treated from a regulatory perspective. First, the prudent person principle eliminates regulatory restrictions and limits on investments but creates the responsibility for insurance undertakings to establish their own limits and investments restrictions. Second, there are now granular capital requirements for individual investments. They reflect the underlying risks and are calibrated to the overall confidence level established in the Solvency II Directive. While differences in risk charges based on differences in the risk profile can influence investment behaviour they are not "designed" to provide incentives for any specific asset. Concerns were raised that the standard formula calibration did not contain enough granularity and so it was not reflecting the lower risk profile of infrastructure investments. EIOPA looked into the matter and performed a very thorough and evidence-based analysis. We consulted representatives of public authorities, insurance undertakings, investment managers and academics in a very transparent process. As a result, EIOPA developed a pioneer approach with the creation of a separate asset class under Solvency II standard formula for investments in infrastructure projects allowing a specific treatment for qualifying infrastructure project debt and equity. The qualifying infrastructure investments need to satisfy conditions relating to the predictability of the cash flows, the robustness of the contractual framework, and their ability to withstand relevant stress scenarios. Regarding calibrations, EIOPA recommended changing the spread risk charge within the Solvency II standard formula for qualifying infrastructure debt investments according to a modified credit risk approach

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resulting in a reduction of around 30% in the risk charge for BBB rated qualifying infrastructure. Risk charges for infrastructure equity investments were proposed to be in a range between 30% and 39%. In terms of risk management, insurers should in particular conduct adequate due diligence prior to the investment; establish written procedures to monitor the performance of their exposures and regularly perform stress tests on the cash flows and collateral values supporting the infrastructure project. This has been incorporated in the Solvency II legal framework. In a next step EIOPA recommended to extend the new asset class in two ways: First, to allow certain infrastructure corporates to qualify for the treatment for infrastructure projects provided that there is an equivalent level of risk. Second, to create a separate differentiated treatment for equity investments in high-quality infrastructure corporates. In this work we followed an important principle: asset risk calibration in Solvency II should not be used to privilege or incentive any specific asset class. If the regime creates incentives that are not properly aligned with risks we will see the emergence of price distortions and vulnerabilities that will ultimately create financial stability risks. I believe that Solvency II brings the right approach to investment by insurers. The risks arising from a mismatch in the duration of assets and liabilities are reflected in a higher regulatory capital requirement. This can be seen as an incentive to invest in the longer term. Moreover, asset diversification is recognised as a key prudential element. EIOPA will closely monitor the consequences of the Solvency II implementation on the asset side in order to ensure that long-term investments in infrastructure are made on a sustainable basis.

To my second point, EIOPA's work on a Pan-European Personal Pension Product, the PEPP, in the context of the Capital Markets Union.

One of the major challenges for countries in the European Union is the provision of safe, adequate and sustainable pensions to their citizens. While there is a broad consensus that both private occupational and personal pensions can play an important role in diversifying the sources of retirement income on top of the public pension regimes, the context of labour and demographic changes and the prolonged low interest rate environment creates particular challenges also to private regimes. At the same time, particularly in the area of long-term retirement savings, it is evident that the European Union internal market is far from delivering its full potential. There is a huge fragmentation of products available to consumers, from low-performing deposits, to very often too complex and costly life insurance and mutual funds, many of them not truly retirement saving products. Also consumer protection rules are very different in the various European Union Member States. This fragmentation is a serious obstacle to cross-border business, increases the costs, reduces the average returns for savers and ultimately undermines consumer confidence in private pension provision. This year, in February, EIOPA submitted to the European Commission its final technical advice on a Pan-European Personal Pension Product, the PEPP, a safe, transparent and cost-effective personal savings product. In our view the PEPP could be the catalyst for efficiency gains through economies of scale and opportunities for risk diversification as well for competition and innovation for the benefit of consumers. We proposed a number of standardised and flexible features for the PEPP:

- Standardised information provision
- Standardised limited investment choices, with one core “default” investment option, where the investment strategy takes into account the link between accumulation and decumulation
- Regulated, flexible caps on costs and charges
- Flexible biometric and financial guarantees

The PEPP should have a long-term perspective in its investment policy to better reflect the long-term nature of retirement savings. This is particularly welcomed from a macro-perspective because long-term investors are needed to provide stable funding to the European Union economy. In order to allow this long-term investment horizon, the PEPP should envisage minimum holding periods to mitigate the surrender risk. Sustainable investment in illiquid assets should match liabilities with a correspondent illiquid profile. The analysis conducted brought us to the conclusion that the PEPP, enacted through a 2nd regime, is a powerful tool to close the pension savings gap in Europe. This conclusion has been supported by the vast majority of stakeholders that responded to our public consultation. From the development of a Capital Markets Union the PEPP can be one of the most tangible outcomes and benefits for European Union citizens. Together, we have to do everything to regain the trust of Europe’s citizens in the European Union and its financial services industry. Europeans request concrete solutions to their very pertinent problems such as the lack of adequate retirement savings. With the PEPP European citizens could see the benefits of building a true single market for capital. EIOPA stands ready to continue to work on PEPP, namely in the design of „product pilots“. We intend to explore pure individual Defined Contribution Schemes but also collective Profit Sharing Products. While pure individual Defined Contribution Schemes can be designed to adjust investment risk throughout the live of the contract, thus reducing risk for members, the development of collective Profit Sharing Products could allow the pooling of investments with the smoothing of returns across members of the pool, so that all members benefit from average long-term returns of the fund and are protected from extremely negative outcomes in stressed market situations.

The design of the PEPP “product pilots” need to ensure conditions to allow European Union citizens to invest in a balanced portfolio that should include assets such as equities, property, infrastructure and green technologies. With the appropriate safeguards, this will provide a good chance to accumulate a pension that outperforms inflation and grows to levels that can provide a decent standard of living. Provided that by design these collective Profit Sharing Products avoid the exposure to short-term market volatility the regulatory treatment in Solvency II could be aligned to the risks effectively incurred, resulting possibly in lower capital requirements. Finally, the PEPP “product pilots” need to be designed in a way to ensure the highest standards in transparency, fairness, governance and risk management. Very importantly, in my view, the Capital Markets Union can only succeed if we are capable of regaining confidence of the European Union citizens in the financial markets. In this sense I strongly believe that supervisory convergence needs to be a high priority of

the Capital Markets Union. The implementation of the Capital Markets Union needs to be accompanied with an evolution in the powers and tools available to EIOPA. To break the current market fragmentation and to increase cross-border provision of services we need to ensure that there are proper arrangements to achieve high quality supervision across the European Union. This should entail an appropriate mix of centralised powers and tools and a clear mandate to reinforce supervisory convergence.

Financing long-term Europe needs to be a common objective; an objective that preserves sustainability of businesses; an objective that benefits citizens.

EARLY STAGE INVESTORS: THE H-FARM EXPERIENCE IN ITALY

Paolo Cuniberti*

H-FARM is an innovative platform that supports the creation of new business models, implementing new digital systems and education programs for young people and Italian companies. We started 12 years ago, from the idea of our visionary founder, Riccardo Donadon, one of the most influential Italian entrepreneurs, who had already established his reputation in the digital market with great achievements. Being early stage investors in Italy is almost as crazy as bungee jumping from the Shuttle. We are in a market that is almost non-existing, there is not a spread culture of investing and betting on innovative ideas, as there is in the U.S., for example. Here people tend to finance their own companies, and invest in what they know instead of taking the risk on something new and with high potential. In Italy, Venture Capital investments are only 0,002% of GDP and compared to European countries, we are on the last positions. We started in 2005, so in only twelve years of life we have transformed ourselves, in order to become a sustainable financial institution, which is in fact what we are now.

Choosing the companies to accelerate is crucial: there is both a bit of science and a bit of heart in our decisions. On average, we receive more than 300 applications per acceleration program. We invite here 20 of them to present their project to our investment committee and then we select 5 startups for a 4-months acceleration program. During this period, startups define their vision, the structure of the team, and their business plan. We have developed a corporate accelerator program. Basically the sponsor is a corporation, that together with us defines a brief. Benefits are for both sides: this process allows us to charge the expenses to the corporation and the corporation is outsourcing its R&D or part of it. We believe that if a company wants to disrupt its own business, it usually does not get disrupted by its own people, but it needs to go out and start looking for external talents who can disrupt the company. The idea is to team up with the corporation and define a way to operate and to partnership with other companies. This approach is becoming the new best practice among accelerators. In Europe, 80% of accelerators' revenues is coming from corporate partnerships and sponsorships. We keep startups together in our campus, for 4 months, and then they fly out of the nest to become a huge company, or to become part of a corporation. Therefore, in this way we create labour, we generate employment and

* CEO and Executive Vice Chairman, H-Farm.

form professionals. Hopefully some of those entrepreneurs will turn into the next Zuckerberg or Bill Gates, but that's not the purpose: the idea is to create entrepreneurs, big or small doesn't matter, as long as they are going to be independent and effective members of this society (and produce taxes).

Statistically, 1 out of 5 startup per program have a successful story, and by that we do not mean Google-like successful story: we are not in Silicon Valley. Anyway, we like to think in this way: we are located by a river called Sile, and we are next to the "valle" (the valley), that in Venetian is the lagoon, so we are Sile-con-valle!

Thanks to a number of visionary investors and entrepreneurs we have created this business. Last year, we decided to raise more money and become financially more sustainable: we want to produce ebitda and not just dreams, binary or digital payouts. We decided to go public, so we got listed in the Italian AIM, which has been a significant experience for us. AIM has provided us with new institutional investors, and has increased the awareness of our brand. We have been able to raise money, permanent capital, in order to follow and keep on following all the ventures we want to finance.

We do not consider ourselves a subsidised venture: we are privately funded, equally, we managed to get the recognition of State's institutions to be sustainable funded. We have just launched a very large infrastructure project, H-CAMPUS, that will underpin our growth. It is a form of private

public investment, huge and meaningful in the sector we are investing in: Education. Yes, education... because once you are crazy you just go for it! We want to produce winners, we want to support those winners, both from an educational and a financial point of view. Offering resources to young talents has always been our job, from the beginning. So that's what we are doing, with positive attitude and energy.

PRIVATE EQUITY AND VENTURE CAPITAL SUPPORTING INNOVATION

Gabriele Todesca*

The developments in the economies of Western Europe over the past decade have raised the profile of European public finance institutions, on one hand by broadening their scope of action with new funding and new activities, on the other by raising public awareness and scrutiny of the role of these institutions.

This is especially the case for the investment arm of the European Union, the European Investment Bank Group. The Group's entity that is focusing more proactively on the finance of innovation and SMEs is the European Investment Fund, a subsidiary of the European Investment Bank which also includes the European Commission and a number of private and public financial institutions as its shareholders.

The European Investment Fund pursues its objective through two primary sets of financial instruments: on one side, structured finance and securitisation instruments, targeting mainly portfolios of loans to European SMEs; on the other, equity instruments mainly in the form of investments into private equity and venture capital funds.

My intervention focuses on the role of private equity and venture capital in the support of innovation, in particular from the perspective of a public finance institution such as the European Investment Fund. In this respect, there are three main points that I believe are important to address: the primary role of equity (rather than debt) finance in the innovation ecosystem, the need to ensure that finance made available by policy institutions reaches the right end-beneficiaries, and the role of non-financial factors in the support of equity investments. Each of these points will be discussed below in more detail.

Debt finance has never been as cheap in Europe and globally as over the past decade. Policy institutions and central banks globally have provided a monetary stimulus of unprecedented scale, which contributed to keeping afloat the global economy during the crisis. However, there are limits to what can be achieved through the provision of cheap debt finance. In fact, the small companies and start-ups that are the backbone of a dynamic and innovative economy are arguably also those that have the least need of debt finance. These companies tend to finance their product development and growth plans with equity capital, mainly because of the flexibility it provides and its longer-term investment horizon. Therefore, the massive monetary

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stimulus put in place in the past years by governments worldwide had to be complemented by an equally strong support for the real economy in the form of equity finance. At the EU level, this was one of the objectives of the Investment Plan for Europe (also known as the “Juncker Plan”), a EUR 315bn investment programme launched by the European Commission in co-operation with the European Investment Bank Group, which among its key areas of focus includes the provision of junior debt and equity finance to SMEs and other innovative companies. The success of the European Investment Bank Group in delivering equity finance to end-beneficiaries over the first two years of the Juncker Plan led to a proposal in September 2016 to extend its duration and increase its funding.

The second point that I would like to address is about ensuring a correct transmission mechanism of equity capital from the public finance providers to the end-beneficiaries. In this respect, it is noted that investing equity in a company involves a complex financial and commercial assessment, usually achieved through a due diligence exercise on the target company. The complexity of this exercise makes this activity difficult to scale, when performed directly by a financial institution. This is one of the reasons why the European Investment Fund chose as its main delivery model an intermediated mechanism, operating as an investor in private equity and venture capital funds managed by independent fund managers, which in turn invest in end-beneficiaries. This solution allows the European Investment Fund to multiply its effort and to reach significant scale, funding thousands of innovative companies through its network of fund managers. However, the other side of the coin in using this indirect delivery model is the limited degree of control on the actual investment decisions made by fund managers, raising the question of how to ensure that equity finance is made available to the right end-beneficiaries. The European Investment Fund achieves this objective through two control mechanisms: on the one hand, by negotiating clear and binding investment guidelines with fund managers, ensuring they invest in companies that not only offer a good financial return, but also correspond to a specific profile targeted by the European Investment Fund and other investors. On the other hand, the European Investment Fund sees its indirect delivery model as a partnership with its network of fund managers, where each partner must be correctly incentivised. This is primarily achieved through ensuring a full alignment of interests with fund managers, which benefit when investments are successful, and are penalised when investments are unsuccessful. Sometimes investments involve other stakeholders, like other private investors or sponsoring institutions, and in all cases the European Investment Fund seeks to ensure that each party is correctly incentivised and that the right alignment of interest is achieved among the different stakeholders.

The third and last point that I would like to address is the key role of non-financial factors in stimulating the growth of equity finance. It is evident that the supply of capital acts as a catalyst for the industry but the growth of equity finance in Europe cannot only rely on the supply of new funding by public or private investors. Most importantly, the legal and regulatory framework must be supportive of this type of investments. Examples of such support are to be found in government actions, such

as for instance the legal framework on Innovative Start-ups put in place by the Italian government in 2012. This framework acts at various levels of legislation (administrative simplification, labour law, tax law, insolvency law) in order to define a favourable regulatory regime for innovative companies that meet certain requirements. Support can also be provided by making it easier or more interesting for private investors to invest in private equity or venture capital funds: an example of such action can be found in Italy in the Budget Law for 2017, which introduces a number of tax advantages (deductibility from an investor's tax base of investments in start-ups, tax breaks for capital gains on investments in unquoted companies) that make investments in the asset class more interesting for investors. The second non-financial factor that is worth mentioning is the economic environment and more particularly the approach to risk-taking of investors, business owners and entrepreneurs. In today's Europe, entrepreneurs and investors tend to have a more conservative approach to risk-taking than in other markets. What an investor (often rightly) considers as sound financial management can sometimes be a hindrance to the rapid growth and development of a European start-up company, which is potentially competing with peers developing the same product or market in faraway places in Silicon Valley or Asia, which may have vastly larger financial resources at their disposal. More generally, a business environment that encourages risk-taking may lead to more failures, but also more and larger successes.

By focusing on three aspects of innovation financing – the trade-off of equity and debt finance, the need to align interests with stakeholders, and the need to put in place the right non-financial incentives – I tried to illustrate the fact that the provision of funding is not and should never be considered as an end in itself. It is only one of the measures (necessary but not sufficient) to be put in place for supporting a dynamic and innovative economy.

**FINANCE FOR THE NEW RISK SCENARIOS
AND GLOBAL RESILIENCE**

POLITICS AND LEADERSHIP IN THE TIME OF UNCERTAINTIES: GLOBAL AND EUROPEAN RESPONSES

Bernard Spitz*

We have entered the Time of Uncertainties. Only a year ago, the FT's "Forecasting the world in 2016" roundup predicted that Hillary Clinton would win. That the United Kingdom would not leave the EU. That by Christmas 2016, Angela Merkel would no longer be Chancellor. And that Belgium would win the Euro.

In all fairness, most of us would not have done better. Nothing is happening as planned. This is a worrying issue for our financial sector, which hates uncertainty above all else. And it is a particularly sensitive issue in my own industry, insurance, which must precisely adapt to this uncertain world and efficiently manage its risks. Furthermore, it must do so within its own horizon: the long-term horizon.

Nothing is happening as planned in politics. We witnessed it in the United Kingdom as well as in the United States. This year, five Eurozone countries, as well as Russia and Turkey, face key elections.

If anything, 2016 taught us that politics matters. The disastrous image of political parties, abstentionism, the new influence of social networks all contribute to the downgrading of politics. It is politics that stripped their European citizenship away from the British young generations. Similarly, politics, by giving the Europhobes the power to call for referendums, can unravel European construction.

In three months' time, here in Rome, we shall celebrate the 60th anniversary of the treaty that gave birth to Europe. Yet we cannot see any adequate political response today to meet this challenge. There's no leadership in Brussels. Confusion in London. In all major continental capitals, the focus remains on short-term and resolutely national issues. All populist scenarios remain possible. Rightly, markets keep re-evaluating political risk ahead of any investment policy.

Nothing is happening as planned in politics. Nor in economics! We did learn the lessons of the Great Depression: we did decide on unconventional quantitative easing policies. Central banks have been printing money. This led to negative rates in order to avoid deflation and re-establish financing channels. Three months ago, you saw that Henkel and Sanofi became the first private companies to borrow at negative rates. This policy has been effective. But it has toxic side effects: on the profitability of banks, on the commitment of the states to carry out their structural reforms, on the risk-return scales; And, in particular, on life insurance yields, within the asphyxiating framework imposed by Solvency II.

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Traditional economic mechanisms no longer work. Low rates combined with lower oil prices did not stimulate investment and growth. Heavily indebted states have been content to see the cost of their debt stabilize, without using this reprieve to reform. Monetary creation did not bring inflation. Some, Larry Summers or Daniel Cohen along them, endorse the thesis of secular stagnation. Others are waiting for Janet Yellen and the Fed to start rising rates. Others still imagine increasingly heterodox solutions: no cash societies, helicopter money. In Europe, there is no alignment between the ECB and the main member countries.

Then markets were suddenly unlocked, not because of monetary, nor economic, but political change. Donald Trump's election, contrary to all expectations, heralds a return of inflation. Ironically, Trump succeeds where central banks have failed. How? Simply by waving the prospect of a Keynesian policy, however unorthodox in the current employment levels in the United States. The four determinants of stimulus according to Trump are:

- major infrastructure investment programs;
- expectations that the promised tax cuts will be re-injected into the economy;
- anticipating of wage increases, subject to a restrictive immigration policy;
- rising prices of goods resulting from trade protectionism.

Long-term US interest rates have therefore actually increased since the election, from 1.8 to 2.35% for 10-year government bonds. At the same time, we see a spontaneous and moderate rise in inflation, which is at a two-year high in the euro area and the United States. In China, ex-factory prices rose for the first time since 2012. Markets shifted from deflation in February to a rise in inflation, mostly due to commodities' rising prices and OPEC's shift in policy, extended for the first time to include a dozen non-OPEC countries. In Europe, rates will be capped by the intervention of the ECB, normally expected to last until the end of 2017. They will remain at historically low levels; but still with some countries – present today – experiencing a wider spread relative to the Bund, essentially based on assessments of their respective political situations, as well of the uncertainty related to the upcoming elections.

Politics matters, not only because it carries in itself risks, but also because it may solve economic conundrums. Almost all risks are in my view contingent on politics. Not necessarily because of their nature, but because we look at them, talk them up or down, deal with them in ways from which politics is never absent.

I do not need to stress that the terrorist risk is political par excellence. Other risks indeed do not belong to the strict realm of political phenomena: I mean natural risks, technological risks and regulatory risks. Take natural disasters risk. These risks will increase with climate disruption. Last year, led by the French insurers' Federation, insurers from 26 countries launched a Climate Appeal at the COP 21 Paris summit, stressing the urgency of our fight against global warming.

The tools we offer to manage this new climate situation are prevention, insurance and risk culture education, all of which fall under public policy. Allow me to express

regrets, by the way, that European policy in this matter is practically non-existent, whereas natural hazards do not stop at borders and therefore should concern us all.

Take technological risks and, first and foremost, cyber-risks caused by recklessness, maliciousness, crime, not to mention attacks from hostile states or terrorist organizations. In these matters, Europe's awareness is only awaking now. The EU has only made a start to unify its legal framework. Every day, businesses are the first victims of cybercrime, but states are no less at risk. By way of illustration, Lloyd's has estimated the damage of an attack on 70 power stations on the East Coast of the United States at \$1 trillion.

Finally, we should take a hard look at regulatory risk. It is massive and strongly shaped by politics. Europe's Solvency II regulation of insurance companies is inadequate: all of us here in this room know it. It is short-termist, to the disadvantage of long-term investment. It discourages infrastructure financing. It removes insurers from the real economy. It disadvantages equity investment.

Worse, the new PRIIPS regulation is about to replace Solvency II as the worst threat ever looming over on European savers. The European Parliament rejected it by an overwhelming majority of 602 votes to 4. But this political victory is only an optical effect: if PRIIPS were to be adopted as it is, all of life insurance in Europe, particularly in France and Italy, would be badly affected by it.

Policy issues require policy responses. Some will be national. This is both unavoidable and desirable. Others will be collective. I hope that Europe will be able to invent them for itself and that the anniversary of the Treaty of Rome will provide an opportunity for a revival of the Union. Time is short and we must hurry.

Global questions that call for global responses. They bring us back to analysing the political risk affecting so many countries and continents. We know the causes: a feeling of exclusion among the richest countries' middle classes. The rise of inequalities. Fear of migration. A persistent mass unemployment among younger and older workers. The fear of downward social mobility as new technologies change the face of work. The rejection of globalization and free trade. We also know, only too well, where, in history, xenophobia, inward looking attitudes, protectionism, nationalism have all led.

These global trends call for a global response, linking economic progress and social progress. After the Second World War, the Bretton Woods Agreements laid the foundations for a new type of global economic and financial governance. Other major issues were dealt with at that time: diplomacy with the UN, as well as culture and health. More recently, we started tackling together environmental issues, with the success of the COP 21. But social issues, so evidently important in today's crisis, lagged behind, relegated to a framework of international institutions dating mainly from the Treaty of Versailles in 1919.

The time has come to respond to the fear running through our public opinions. Such a response can only come from members of the G20, via a process that would set social issues at the heart of policy decisions, eventually under the auspices of UN. We must construct a new Bretton Woods devoted to key social issues. This French proposal was one of the highlights of the Berlin B20 that brought together repre-

sentatives of business in the 20, only a few days ago. Why not make it the major thrust of the G20 in Germany next year? To do so with, together, business leaders in the B20 and major unions in the L20 could bring about decisive change.

As the first formal initiative of a postcolonial, post-Cold War and post-populist globalized world, such an initiative, calling for for an international New Deal, would have the merit of voicing the kind of political response that our fellow citizens have been expecting. Until then, we must beware. The rise of inflation could be beneficial at first. But it would place debtor countries in a situation where their debt will become increasingly difficult to finance. The only real long-term solution for global resilience therefore lies in decisively reconciling politics with economics. Politics, by recognizing the need for a better social inclusion. Economics, by creating the conditions for sustained growth, firmly grounded in productivity gains and innovation.

THE NEW LANDSCAPE FOR INFRASTRUCTURE FINANCE

Sonja Gibbs*

CHANGES FOR THE BANKING SECTOR

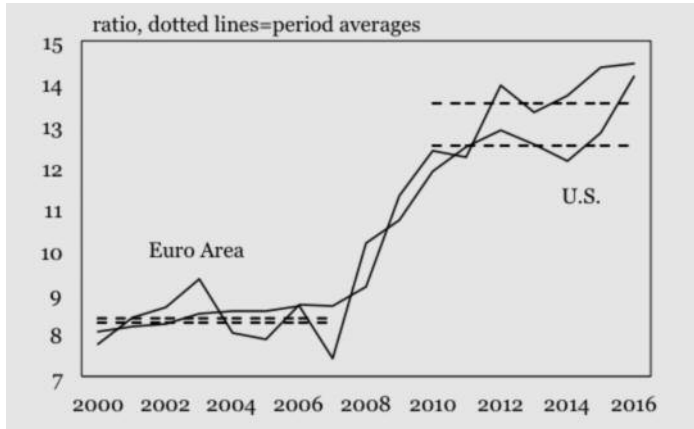
I would like to start with a few thoughts on the outlook for the banking sector in the post-crisis regulatory environment. The push for higher bank capital requirements has been a fundamental element of the post-crisis regulatory agenda. The rationale for asking for banks to hold more capital comes in part from the Modigliani-Miller theorem, which is predicated on capital structure irrelevance – meaning that higher capital levels should reduce balance sheet leverage and risk, leading to a decline in the cost of equity capital. In practice, however, there are tradeoffs. Although much capital has been raised for global banks (Tier 1 capital has risen from around 8% in 2000-2007 to over 14% – Chart 1), the *cost* of bank capital has actually risen, from 8-9% to 13-15% – a bit less for U.S. banks, and more for European banks. Why? Certainly, concerns about legacy problems on balance sheet – NPLs, bad assets etc., have played a role. Balance sheet vulnerabilities also prompt concerns about the ability to cope with shocks – one reason for the emphasis on stress testing. But at a more basic level, the lack of profitability in recent years challenges Modigliani-Miller. Return on equity has dropped from 15% pre-crisis to 8% for U.S. banks and 5-6% for European banks (Chart 2). This poor profitability, coupled with uncertainty about future earnings, has depressed bank valuations. For example, price-to-book ratios are still well below 1x for European banks – pushing up the cost of equity (Chart 3). There is also evidence that investors will not accept utility-like returns from banks given their central role in the economy, which implies an inherent cyclicity and volatility in earnings.

Hence increasing capital and related requirements beyond some point – which many believe has already been reached – could do more to reduce the volume and increase the cost of lending than to increase stability in the system. This is a key concern as discussions of proposed reforms to Basel III continue: although not intended to raise capital requirements significantly, these reforms could well do so, not least here in Europe.

So, what can the financial sector do to support growth and increase resilience? A complex question, but the first step is clearly to be able to fulfill the basic function

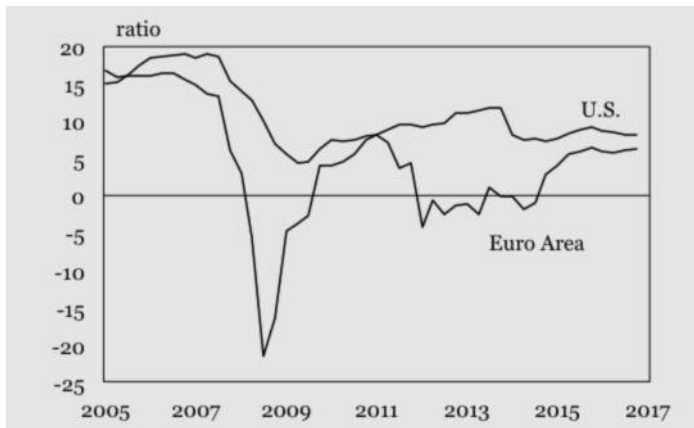
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Chart 1: U.S. and Euro Area Banks – Tier 1 Capital Ratio



Source: Bloomberg, IIF.

Chart 2: U.S. and Euro Area Banks – Return on Equity



Source: Bloomberg, IIF.

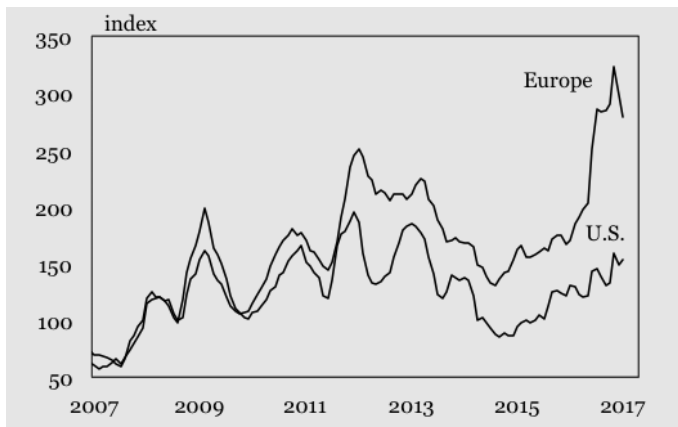
of financing the economy, whether via traditional bank lending, capital markets funding, or new innovations – e.g. digital finance which in many countries is helping promote financial inclusion. Both public and private sector efforts will be needed – to address balance sheet issues including troubled assets, to build forward-looking business models making full use of new financial technologies, and to ensure a balanced and effective regulatory framework.

Chart 3: U.S. and Euro Area Banks--Price-to-Book Ratio



Source: Bloomberg, IIF.

Chart 4: Economic Policy Uncertainty Index



Source: Bloomberg, IIF.

International consistency in regulation is also vital to strengthen the international financial architecture, allowing capital to flow efficiently across borders. However, given the growing risk that multilateralism will give way to more fragmentation in policymaking, achieving international consistency in financial regulation may become even more challenging. The momentous events of the past year, including Brexit and the election of Donald Trump as U.S. President may well represent additional obstacles to cross-border coordination. More broadly, these events highlight the growing importance of political risk as a key factor in strategic planning and investment decisions (Chart 4). We cannot work to improve growth and resilience without understanding political risk and its underlying causes (including income inequality and hollowing-out of the middle class).

INFRASTRUCTURE AS A SOURCE OF GROWTH

Infrastructure has tremendous potential to improve economic growth prospects in both the short and the long term. For many countries – particularly those with highly efficient public investment – the multiplier effect of infrastructure spending is significant. For example, for the Euro Area one euro of infrastructure spending is estimated to deliver two euros in additional economic growth.

At the same time, the need for infrastructure finance – particularly if we incorporate commitments to a lower-carbon environment (including green buildings, transport, and energy provision) – is estimated to be over \$90 billion through 2030. Even this vast sum does not include investment in social infrastructure, such as health, education, and digital infrastructure. This type of investment is essential to improve future social welfare and to propel countries into the digital era.

While the public sector and banks will continue to play a key role, expanding the investor base – in particular, to channel more funding from institutional investors – will be an essential element of addressing the infrastructure gap. Developing infrastructure as a full-fledged asset class, with a spectrum of investment opportunities – including project/infrastructure bonds, listed and unlisted infrastructure securities, open-ended funds, and securitization – will help mobilize private capital to foster sustainable growth, reduce poverty and combat climate change.

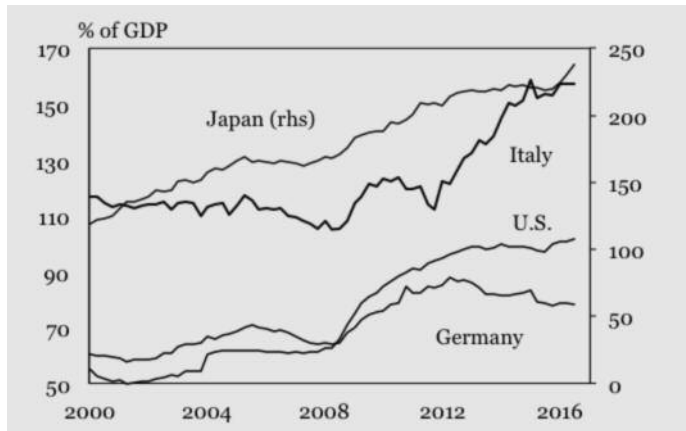
This helps explain why the G20, the European Union, international institutions and governments around the world are so focused on promoting infrastructure investment. Currently, the gap between projected needs and available funding is estimated at about \$3.5 trillion per year through 2030. But with debt-to-GDP in many countries at very high levels across mature economies, governments no longer have as much fiscal space to support infrastructure spending as they have had in the past (Chart 5). Hence without more private sector involvement, there are limitations to what can be accomplished, both in financial and in political terms.

Changing circumstances have also limited bank participation in infrastructure finance. Market and regulatory changes have led to significant deleveraging since 2007, with disincentives to longer-term, more illiquid investments. The landscape for global project finance has thus changed significantly since the financial crisis, with an overall decline in the volume of private bank loans – especially in greenfield and to emerging market infrastructure.

ROLE OF INSTITUTIONAL INVESTORS

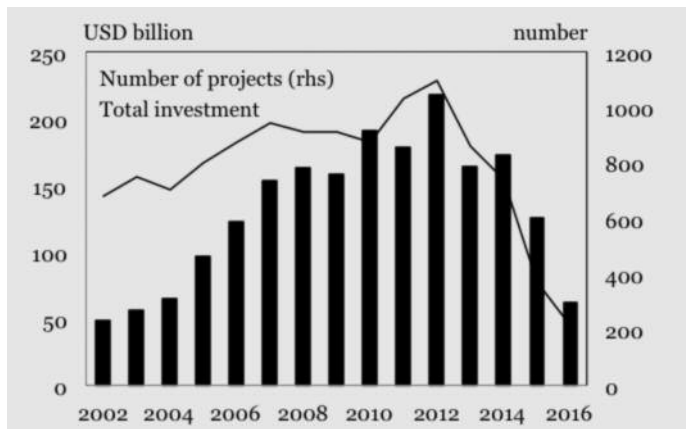
As public sector and bank financing for infrastructure diminished in the wake of the financial crisis, capital markets financing has provided some offset. However, for emerging markets, all forms of private sector participation in infrastructure financing declined in 2015-16 with the fall in commodity prices and increase in political uncertainty (Chart 6). Along with efforts to develop capital markets more broadly, such as designing hedging instruments to facilitate local currency financing or facilitating ca-

Chart 5: General Government Debt-to-GDP Ratio



Source: IIF Global Debt Monitor.

Chart 6: Private Participation in Infrastructure in EMs



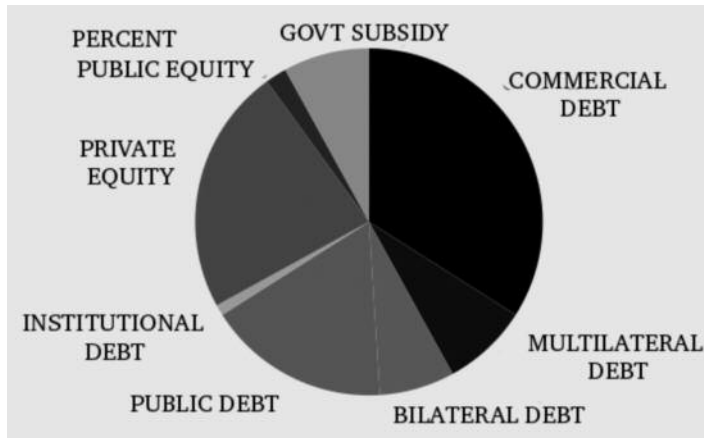
Source: World Bank, IIF. 2016 = H1 annualized.

pital mobility, it will be vital to develop the infrastructure market to help channel funding from institutional investors – both in mature and emerging markets.

Raising awareness and improving the transparency of funding and co-funding arrangements will help expand the investor base and support new infrastructure projects. As active players in infrastructure financing have a range of objectives, time horizons and investment preferences, their diverse profiles allow for flexibility in risk sharing:

- National governments: Despite pressure for fiscal consolidation, national governments will remain a key source of funding, able to absorb idiosyncratic risks,

Chart 7: Sources of Infrastructure Project Finance



Source: World Bank, IIF.

offset cyclical and collaborate with the private sector. Moreover, national governments have the capacity to create a conducive regulatory and investment environment, helping to channel resources to projects able to bring benefits to the economy.

- Multilaterals, regional, national development banks: these are well-positioned not only to provide financing, risk sharing and credit enhancement tools, but also to promote best practices and disseminate information, bridging the gap between project development, project finance and investors.
- Banks: Traditionally the dominant force in project finance, banks maintain a deep repository of deal structuring expertise and close ties with project sponsors. Despite de-risking and retrenchment in recent years, they will continue to play a major role.
- Large institutional investors, including insurers, pension funds, asset managers and sovereign wealth funds may benefit most from establishing benchmarks and developing infrastructure as an asset class more broadly.
- More specialized investors such as private equity firms are increasingly active in infrastructure, including on the more illiquid end of the investment spectrum. Establishing benchmarks and setting out the range of available instruments could greatly facilitate further engagement, improving liquidity of secondary markets.
- Retail investors too have become more involved in infrastructure, including via listed infrastructure equities and innovative mechanisms like crowdfunding.

CHALLENGES IN ATTRACTING MORE PRIVATE SECTOR INVESTMENT

More progress is needed in building a pipeline of bankable/investible projects and providing a supportive regulatory framework. Ensuring a continuum of infrastruc-

ture investment vehicles across the risk and liquidity spectrum is crucial. Given the unique risk-reward profile of the asset class (offering yield, duration and portfolio diversification, along with an inflation hedge), scaling the asset class would greatly improve prospects for more portfolio allocations to infrastructure. Surveys suggest that large pension funds, for example, have a desired allocation of about 5% for infrastructure, but are only allocating about 1%. With estimated global assets under management near \$70 trillion, even a small increase in allocations would shift hundreds of billions of dollars toward funding the infrastructure gap.

A full spectrum of investment vehicles, including highly illiquid stakes, unlisted and listed infrastructure securities, open-ended funds along with more risk sharing options (including more standardized project bonds, partnerships between banks and institutional investors; securitizations, REITs, etc.) would propel infrastructure investment and channel resources to underfunded projects. For instance, while attractive brownfield projects in mature markets are often many times oversubscribed, greenfield investment and infrastructure in emerging markets tend to be much harder to fund. Such projects involve more complex assets, management challenges, deal structuring, and potential downstream exposures that require monitoring. Greenfield investment also tends to entail more environmental, contractual and counterparty risks.

Other important steps that will help channel more private-sector funding to infrastructure include a greater range of partnerships between banks and institutional investors; revitalizing securitization markets with an emphasis on infrastructure debt; development of specialized derivatives products that can help mitigate risks related to infrastructure investment; and development of local infrastructure markets, including in emerging markets.

SUPPORTING MORE ALLOCATION TO INFRASTRUCTURE INVESTMENT

The OECD estimates that Basel III will more than triple the capital reserves that banks must hold against losses. Proposed Basel III reforms – should they move ahead – could further raise charges on infrastructure financing. More broadly, the net stable funding ratio (NSFR) requires that long-term lending be matched with long-term liabilities – this has been a key driver of the reduction in allocations to long-term lending, including infrastructure. Of note, the average maturity of infrastructure loans in Europe is now about 7 years vs. 15 years before the crisis.

In sum, addressing the gap between demand for and available supply of infrastructure funding is a complex and challenging task. Important steps include ensuring a fair and stable regulatory framework; better transparency around bankable/investible project pipelines; efficient government coordination; promoting sound and stable macroeconomic policy, and supporting investor/creditor rights including via a robust framework for dispute resolution.

RISK SCENARIOS AND GROWTH OPPORTUNITIES: THE OUTLOOK

Carlo Cottarelli*

A discussion of risk scenarios and global resilience must necessarily start with an assessment of the global growth baseline around which risks may materialize.

The growth projections published by the International Monetary Fund in January 2017, which essentially confirm for the whole world, if not for specific economies, the September 2016 projections available at the time of the Rome Investment Forum, give a mixed picture of the growth outlook. The world is projected to grow, in real terms, by 3.4 percent in 2017, a bit above the preliminary estimate for 2016 (3.1 percent) and a bit below the growth rate projected for 2018 (3.6 percent). In spite of the repeated references, including by the International Monetary Fund and the G20 community, to an “anemic growth”, these growth rates are not particularly low by historical standards, especially in per capita terms. Granted, in the run up to the 2008-09 financial and economic crash, global GDP growth was much higher, averaging 4.5 percent per year during 2000-07. But that was, indeed, before the crash and thanks, at least in part, to the macroeconomic policies, including expansionary monetary policies, that contributed to the crash. If, instead, we look at the previous thirty years, the world growth rates were much more contained: in the average of the 1970s, the 1980s, and the 1990s, the world economy grew by 3.6 percent per year in absolute terms and by 2.3 percent in per capita terms, against an annual per capita growth rate of 2.4 percent projected for 2016-17.

So, the good news is that growth rates are not too bad for the global economy. The bad news is that the growth rate of advanced economies is much lower, and not only with respect to that of emerging markets, but also with respect to their own past. Advanced economies are projected to grow at an annual rate of 1.7 percent in 2016-17, well below the growth rate recorded in the 1970-99 period (3.1 percent). That is not all. This lower growth rate is achieved in spite of the extremely expansionary monetary policies undertaken by the central banks of all major advanced economies since the 2008-09 crisis, pointing at a severe underlying weakness of aggregate demand. Such weakness could have different origins: on the one hand, private sector indebtedness (further discussed below) and the related deleveraging attempts imply higher saving rates by the household sector, as well as prudence in undertaking new investment projects by the business sector; on the other hand, the deep chan-

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ges in income distribution occurred over the last few decades (also discussed below) may have weakened structurally the ability of the middle class of advanced economies to consume.

Given the relative weakness of growth in the baseline projections for advanced economies, it is even more important than usual to look at possible sources of risks around the baseline, as well as at the resilience of the growth process to shocks.

Broadly speaking, there are two categories of risks: those arising from shocks that are not anticipated in the baseline; and those arising from the difficulty of managing the exit from the current very supportive macroeconomic policies and, hence, to the inadequacy of the economic policies assumed in the baseline.

Prominent among the first group are the political risks. While, in the immediate future, these risks are closely connected to some high-profile political elections (first and foremost the forthcoming general elections in France and Germany), the underlying theme is the rise of populism, intended as anti-establishment political movements that benefit from a widespread feeling of unhappiness, impoverishment and lack of economic prospects. Globalization and the related process of income redistribution towards the “rich” that has emerged over the last two-three decades in several advanced economies (including in the United States) has been a key factor behind the rise of populism. The world is changing rapidly and not everyone has been winning, especially in advanced economies. Uncertainties related to the Trump presidency, not unrelated to the rise of populism, are also high, and give us perhaps an early taste of the kind of risks coming from other elections ahead of us. In the specific case of the United States key geopolitical risks arise from the possible deterioration of its relationship with China, as well as with other smaller countries like Mexico and Iran (the latter with potentially severe developments for oil prices). The medium-term risks arising from Brexit should also not be underestimated, although, under normal circumstances and assuming no domino effect within the EU, those risks could remain confined primarily to the United Kingdom itself.

Among the second group of risks, the most important ones relate to the exit from the super expansionary monetary policies that have characterized the last few years, coupled with the potential risks arising from unusually high levels of public debt, including for euro area countries. At present, the liquidity overhang in bank portfolios is unprecedented. Since 2008 the increase in base money (the sum of banknotes in circulation and commercial banks’ deposits at central banks) has been in the range of 300-400 percent in real terms (at least using the CPI deflator) in the main advanced economies (the increase has been a bit lower in the euro area, which is, however, catching up rapidly). This surge in liquidity has taken place primarily through the purchase of government securities by central banks. Alongside, money market interest rates have fallen sharply, and, while edging up, are still close to zero in most countries. The reasons why this surge in liquidity has not had much effect on economic activity are not yet well understood. It may have a lot to do with the tightening of capital requirements that has made commercial banks very cautious in extending new loans: not only capital requirements have been raised over the last ten years, but there is still a lot of uncertainty about how much they will be raised in the fu-

ture, including in the context of the so-called Basel 3.5 or Basel 4. At the same time, the cost of bank equity has increased, as bank profits have been depressed, especially in the retail sector, by low interest rates. Be this as it may, there will be sooner or later a need to exit from these super expansionary monetary policies and the exit may not be too smooth. To start with, these policies may have given rise to bubbles in asset prices, which may be pricked by the eventual monetary tightening. Moreover, when interest rates start rising, the full implications of the post-2008 public debt surge will become apparent. All this could cause renewed pressures on the countries that are failing in bringing their government primary surplus to a level sufficient to put their public debt-to-GDP ratio on a clearly downward trajectory.

How resilient is the world economy to these shocks? Not much, I am afraid. The main issue is the accumulation of debt and the related balance sheet vulnerabilities. The last issue of the International Monetary Fund's Fiscal Monitor (dated October 2016) informed us that "The global debt of the nonfinancial sector has more than doubled in nominal terms since the turn of the century, reaching \$152 trillion in 2015. About two-thirds of this debt consists of liabilities of the private sector... current debt levels, at 225 percent of world GDP... are at an all-time high."

High private sector debt implies the exposure of part of the private sector to interest rates shocks. The public debt is also exposed to the risks of interest rates hikes, the risk is particularly high for those high-debt countries which may suffer not so much from a gradual interest rate increases but from a sudden surge in spreads with respect to countries with higher credibility. This said, high public debt may constrain the action of most countries. The average public debt-to-GDP ratio of advanced economies has increased by almost 40 percentage points between the end of 2007 and the end of 2016, and is now close to 110 percent. High public debt means that, in case of shocks hitting the whole economy, the public sector will have limited or, in some cases, no fiscal space to support the economy, including its financial sector. There are of course some countries where fiscal space does exist (for example, Germany, Korea, Canada), but the majority of countries do not have much room, taking also into account demographic pressures, and the related sizable implicit public debt. Monetary policy's capability to respond to exogenous shocks remains constrained by a transmission mechanism that, for whatever reason, is not working as in the past. Monetary policy could become more effective if financial regulations were relaxed but that would be unlikely to happen (as it would probably be seen negatively and perhaps counterproductive) if that relaxation occurred at a time when financial markets are hit by a confidence shock,

Altogether, the baseline growth is not great, at least in advanced countries, downside risks are sizable, the degree of resilience of advanced economies is not high, and policy ammunitions to muffle the shocks are limited. In a nutshell, it is not really a great outlook.

APPROACHING NEW RISKS AND IMPROVING RESILIENCE: A PRACTITIONER'S PERSPECTIVE

Mark Garvin*

I would like to take a practitioner's perspective on the new risks we are facing and how we can improve our resilience to them. Addressing resiliency issues is a prerequisite to facilitating jobs and growth in Europe and safeguarding the so-called 'real economy'. While much has been done in improving the resiliency of the financial system, we have more work ahead. Likewise, policymakers are dealing with major political challenges and risks. We need to improve resiliency on both fronts as this is a prerequisite to the growth for which we all yearn.

MARKET CONDITIONS AND LIQUIDITY

One of these risks is market liquidity. An evolution in market structure, combined with changes to participant behaviour, new participants, new regulations and monetary policy have impacted liquidity dynamics in fixed income markets. The proliferation of multilateral trading facilities and the increased automation of markets have contributed to this trend, especially as many of these platforms are new with untested robustness. And there is evidence of this trend:

- Banks' liquidity portfolios are growing:
The largest banks hold about 20 percent of their balance sheet in the form of liquid assets, nearly double the share they held pre-crisis.

Markets have become more volatile, especially in response to political events. Recent examples include:

- October Pound Flash Crash: The GBP dropped more than 8% from \$1.26 to \$1.1491 in just eight minutes – the worst one-day drop since the 10% fall in the immediate aftermath of the result of the Brexit vote in June. Just 30 minutes later the pound had recovered to \$1.24.
While the cause has yet to be officially established, Brexit uncertainty would not have helped.

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This is important because, without a market, investors have few options and can get stuck with big losses. This has a direct impact on decisions around issuance and pricing. It is encouraging that the European Commission has recognised this problem in their 2016 follow-up report on the cumulative impact of financial regulation. However, some forthcoming requirements will likely further constrain liquidity.

- **Total Loss Absorbing Capacity (TLAC):** The increased issuance of bank debt may crowd-out demand for subordinated corporate debt, potentially resulting in higher rates for corporates. This assumes, however, that investors view TLAC debt as safe; the ultimate effects on market liquidity remain unknown. This would be especially concerning in the EU if it impedes development of a Capital Markets Union.
- **Fundamental Review of The Trading Book (FRTB):** The final version of Basel's FRTB resulted in a notable rise in industry aggregate capital requirements for market risk. As firms adjust to this new constraint, it could potentially put further pressure on market depth and business revenue.
- **MiFID II/ MiFIR:** Post-trade reporting requirements under MiFID II could also put at risk the capacity or willingness of intermediaries to execute in size in thinly-traded securities.
- **Money Market Funds rules:** SEC rules have seen dramatic shift of investment from prime MMFs (those investing in corporate bonds) to government MMFs (investing predominately US Treasuries). This has led to a significant widening of credit spreads in the short end of the curve and increased difficulty for corporate issuers in financing short term paper. EU rules will also have an impact but still not entirely clear.

The prospect of further constraints on market liquidity is even more worrying considering the macroeconomic environment, specifically the possibility of rising dollar interest rates. Rising rates are often correlated with increased volatility and stresses in the system.

GEOPOLITICAL RISKS

So all of these changes have already weakened markets. Then you have to layer on the intrusion of heightened geopolitical risk and shocks. This risk is not new. It is something which we as a firm have always tried to monitor and manage. However, over the past year, it has taken on a new form; in some ways, it has shifted from the realm of risk to the realm of uncertainty.

Brexit is a democratic decision and we should, and do, respect that. However, it produces a degree of risk and uncertainty that could hurt European jobs, growth, markets and the real economy if not managed correctly. The terms of Britain's exit will be decided (hopefully in an amicable and constructive environment) between UK and EU politicians. As a firm, we believe continued access to the EU Single Market for UK-based firms would be the best outcome, however challenging.

But whatever the final terms of the UK's departure from the EU, it is only sensible that the transition to that end state is managed in such a way as to preserve European jobs and growth and limit market uncertainty. There is no excuse for a Brexit outcome that is both damaging in the end and damaging in the means. That is why we ask the UK and the EU to agree to preserve the status quo for a minimum of 3 years from the end of negotiations so that there is time to implement any necessary changes on an informed basis, and avoid a "cliff-edge". This makes as much sense for the European financial stability and economics as it does for the UK.

As Carney said in 2016, "Additional risks to the euro area could emerge as a consequence of the UK's withdrawal from the European Union. Banks located in the UK supply over half of debt and equity issuance by continental firms, and account for over three quarters of foreign exchange and derivatives activity in the EU... If these UK-based firms have to adjust their activities in a short time frame, there could be a greater risk of disruption to services provided to the European real economy, some of which could spill back to the UK economy through trade and financial linkages".

A sensible transition period would help create a safer situation for all European financial markets. How are we going to achieve Juncker Plan goals of increased investment if we're simultaneously damaging Europe's financial markets? What would be the implications for European jobs and growth? All of these are reliant on well-functioning markets. How can we expect to achieve the ambitious objectives of the Capital Markets Union (CMU) project in that environment? We have to be careful not to allow the fragmentation and Balkanisation of capital markets. For example, new European Commission proposals could require non-EU banks to establish an EU-located Intermediate Holding Company (IHC). This could put barriers in place for firms willing to commit capital to Europe's capital markets and could precipitate decisions by firms about whether certain activities remain economically viable, reducing the number of market participants/competition. This, as well as Brexit and the election of President Trump, may hint at a broader question of whether we are heading towards some sort of financial regulatory de-globalisation.

However, while we work on managing Brexit, we should not let Brexit suck the oxygen out of the room from all the other issues that are already on the table.

CYBER-RESILIENCE

One of these is cyber security. As banking assets are increasingly digitised and as the sector becomes more interconnected, often through the introduction of new infrastructure, cybersecurity has become a growing concern for the industry and policymakers alike. Cyber risks present new challenges to all market participants as no entity is safe from a cyber attack.

Banks have responded to cyber threats with greater cybersecurity oversight, management, controls, and expenditure. J.P. Morgan's own investment in cybersecurity will be about \$600 million in 2016. At the same time, cybersecurity has beco-

me a government-wide concern across the globe, with law enforcement, intelligence agencies, legislators, and financial regulators all making cybersecurity a top policy priority. Greater collaboration is needed between industry and regulators, as well as among regulators across different jurisdictions, to ensure that we do not end up with fragmented and duplicative approaches to cyber that do not leverage the collective knowledge and skills from across the globe. The U.S. National Institute of Standards and Technology (NIST) Cybersecurity Framework is widely regarded as a best practice across sectors – and should serve as the foundation of a globally collaborative and consistent policy approach to cybersecurity. Moreover, we support a commonly accepted penetration testing framework that enables regulators and firms to use testing events and results to satisfy multiple firm self-assessment and regulatory supervisory objectives, and to provide a common standard for comparison.

CENTRAL COUNTERPARTIES

The use of central counterparties (CCPs) is now mandated by G20 commitment, making them a concentration point of risk in the financial markets. Moreover, we expect CCP activity to grow further over the next couple of years. It is critical that CCP recovery & resolution are addressed in a manner that limits market contagion (the ultimate goal of the market reforms), provides clarity and confidence to market participants, avoids pro-cyclicality, moral hazard within CCPs and ensures the continuity of critical financial market functions.

The global nature of CCPs makes a globally consistent regulatory framework imperative. Cross-border cooperation is critical. To this end, we support the work of both CPMI-IOSCO and FSB on resiliency & recovery standards, and resolution guidance. We also support the European Commission's work in this area. The European Commission just published a legislative proposal on November 28th. These proposals will be discussed and amended by the European Parliament and EU Member States. We're hopeful that this process stays aligned to the global work streams and encourages sound CCP governance, and discourages moral hazard. Rules should contain well-calibrated resolution tools and provides transparency around recovery and resolution to allow the market to plan and adjust appropriately.

CONCLUSION

I have laid out some of the new risks and uncertainties we face and some thoughts on how we could respond and remain resilient to them. As I said, it seems uncertainty has become the new normal. While this situation is not ideal, we are in the business of managing risk and most of these risks are largely manageable. We may not like low interest rates, or anticipate volatility around rising rates, but we can deal with them. We may not like to see a lack of liquidity in our markets, but we can help mitigate this by crafting regulation with this in mind. Whatever our views on Brexit prior

to the referendum, now is the time to think intelligently and make it work. I do not take this lightly, addressing these issues of course will involve a great deal of effort. We would all prefer to be laser-focussed on creating jobs and economic growth in Europe – we should not lose sight of important growth-driven measures. But if we haven't addressed uncertainty both to financial system and the political system, we won't see the economic growth we'd like.

THE NEW WAVE OF POPULISM: THREATS AND RESPONSES

Rony Hamaui*

INTRODUCTION: WHAT DO WE MEAN BY POPULISM?

Populist ideas and parties are present in every single historical epoch, in every region of the globe and under numerous ideologies. The “Peoples” were, for example, a faction in the Roman senate, who wanted to govern through the mobilization of Roman masses. Among the most famous populist we can remember Tiberio Gracco, Gaio Mario and Cesare Augusto, who used the referendum to bypass the Roman Senate. In the modern age, populist ideas could be found during Protestant reform, where groups such as the Anabaptists in Germany or the Puritans in England based their policy on a theocratic ideological society in which peasants would be able to read the Bible alone and to govern themselves¹. Even during the French Revolution many leaders, led by wealthy intellectuals, displayed populist ideas against the excessive privileges of the Ancient Regime elite.

It is, however, in the middle of the nineteenth century where the first political-cultural movement called the explicitly “populist” was born in Russia. The proponents had identified in the peasants the revolutionary force capable of overthrowing the authoritarian Tsarist system, moving directly to socialism without the need to pass through the capitalist stage of industrialization. The United States also saw at the end of the nineteenth century the birth of a “People’s Party”, also known as the Populist Party, supporting the less wealthy southern classes and strongly opposing to banks, railways and in general to elites.

Clear we can find populist connotations in the Italian Fascism and German Nazism, as well as, in many Latin American leaders such as Aprismo in Peru, Getúlio Vargas in Brazil, Perón in Argentina, Lázaro Cárdenas in Mexico, and Hugo Chavez in Venezuela.

As we understand, at the basis of these different experiences are equally diverse ideologies, not always easily framed in a single scheme. All this makes very difficult to even define the concept of populism, a term frequently used in a questio-

* Chairman, Assifact.

1. T. Scott, “The Early Reformation in Germany: Between Secular Impact and Radical Vision”, Ashgate, 2013. Christopher Hill, “The World Turned Upside Down: Radical Ideas” in the English Revolution.

nable way. The more general definition of populism emphasizes how these movements use a very aggressive language to defend “the common man” against the privileged elites. Other authors, such as Dornbusch and Edwards, referring to South American, call populist those political groups that, in the name of a fairer distribution of income, pursue hyper-expansive economic policies that end up harming the poorest, or better, masked right wing interests with apparently leftist politics (leftist bias)². Noam Gidron and Bart Bonikowski of Harvard University then attempted to build a taxonomy of populist policies based on ideologies, styles and strategies³.

THE BEST DEFINITION OF THE POPULIST APPLICABLE TO MODERN WESTERN COUNTRIES

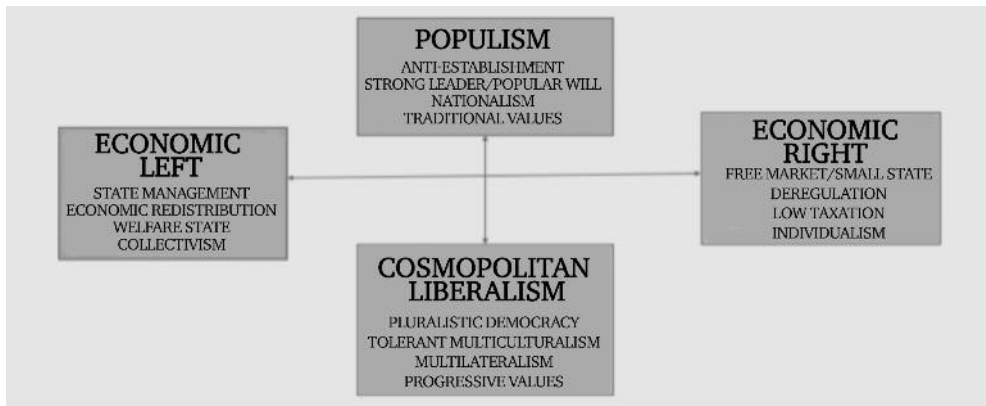
Perhaps, the best definition of the populist applicable to modern Western countries is the one coined by Cas Muddle, according to which populist philosophies are a set of ideas that contain three main components⁴:

1. *Anti-establishment*. That is a strong criticism of existing authorities, politicians, media, elite, experts, multinationals, banks..., generally considered corrupt. These strong powers are opposed to the honesty of ordinary people, who are seen in a homogeneous and positive manner (the silent majority).
2. *Authoritarianism*. Almost always, populist movements are led by a charismatic leader, who favors direct representation, referendums, and plebiscites. Indirect representation and administrative bureaucratic structures are instead seriously criticized.
3. *Nationalism and Xenophobia*. The defense of national interests over international cooperation, racism and border closure are then salient features of modern populism.

This kind of conception contrast with a liberal cosmopolitan culture, in which the values open borders are emphasized and where the diversity of peoples and cultures are seen positively. In this framework the importance of the weights and counterweights, typical of representative democracy, are highlighted. The values of tolerance and the protection of minorities are fundamental and equal rights to minorities, women and homosexuals are the natural complement.

2. R. Dornbusch, and S. Edwards, eds. (1991) “The Macroeconomics of Populism in Latin America”. J. Sachs, (1989) “Social Conflict and Populist Policies in Latin America,” NBER Working Paper No. 2897. See also D. Acemoglu, G. Egorov, K. Sonin (2011), “A Political Theory of Populism” NBER Working Paper No. 17306.
3. Noam Gidron and Bart Bonikowski (2013), “Varieties of Populism: Literature Review and Research Agenda”, Working Paper Series, Weatherhead Center for International Affairs, Harvard University, No. 13-0004.
4. C. Muddle (2007), *Populist Radical Right Parties in Europe* NY, Cambridge University Press.

Chart 1: A heuristic model of party competition in Western societies



Source: Inglehart and Norris (2016).

In this context the traditional contrast between left and right parties is overcome. Especially in the economic sphere. Indeed, populist parties often say that they want to pursue leftist policies, which involve a significant state intervention, a strong redistribution of income, and a non-district struggle for monopolies (Chart 2).

THE STATE OF POPULIST PARTIES IN EUROPE

A 2016 inquiry into the parties' nature of about thirty European countries shows that, although in general, more open-minded formations tend to pursue Keynesian-style policies, the more populist parties are equally divided between right-wing and left economic policies (Chart 2)⁵. On the front of parliamentary representation in the European elections, Inglehart and Norris also show that the strong growth of the populist parties observed since the 1960s is almost equally distributed among those pursuing right and left economic policies (Chart 3)⁶.

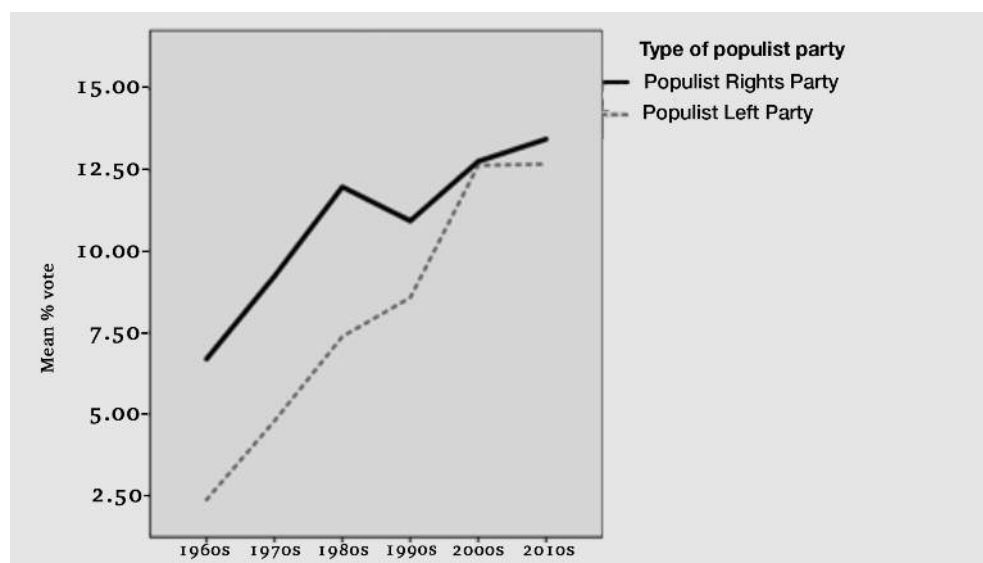
WHAT ARE THE REASONS FOR GROWTH OF POPULIST IDEAS?

In general terms it can be stated that there are three different schools of thought, not necessarily incompatible, behind the reasons why the populist parties find a fer-

5. Chapel Hill Expert Survey 2014.

6. R. F. Inglehart and P. Norris, (2016), "Trump, Brexit, and the Rise of Populism: Economic have-Nots and Cultural Backlash", HKS Faculty Research Working Paper Series, No RWP16-026.

Chart 3: The growth of populist right and left parties in Western countries



Source: Calculated from Holger Döring and Philip Manow. 2016. *Parliaments and governments database* (ParlGov) ‘Elections’ dataset: <http://www.parlgov.org/>.

tile ground for growth in some historical moments and countries. First, there are *theories related to the structure and quality of institutions* such as the nature of the constitutional charter and the electoral law. In particular, proportional-based electoral systems, often requiring the formation of large coalitions of parties, make it more difficult for populist parties to emerge⁷. The same happens in uninominal colleges system with ballots.

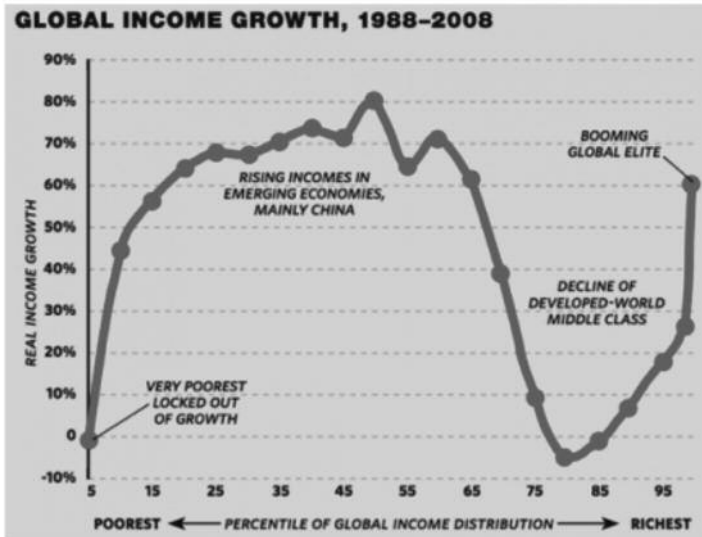
Secondly, there are *theories related to the offer* of leaders and parties able to propose tempting alternatives in term political programs. For example, Michael Broning argued that with the collapse of ideologies, both the left parties, such as Tony Blair’s New Labor, and right parties, like Democratic Christians of Angela Merkel, have increased their centered connotations⁸. This allowed populist parties to pick up discontent and represent the interests of the “defeated”. A sort of Darwinism that can change the political landscape.

Finally, there are *theories related to the demand side*, that is related to the needs of the people. The latter can be distinguished into economic theories, in which the growth of populist movements depends on economic crises, increase in inequality or transformation of productive structures caused by technological innovations or

7. A. Lijphart (1994), “Electoral Systems and Party Systems”, Oxford University Press. P. Norris (2005), “Electoral Engineering”, Cambridge University Press.

8. M. Broning (2016), “The rise of Populism in Europe”, *Foreign Policy*, June.

Chart 4: The Elephant Curve



Source: MA. B. Milanovic (2016), “Global Inequality, A New Approach for the Age of Globalization”, Cambridge, Harvard University Press.

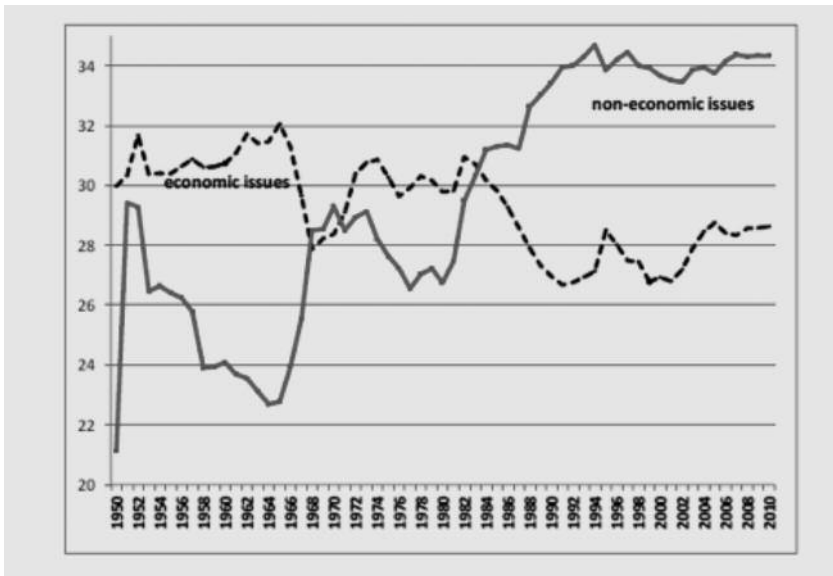
globalization, and theories where populist movements arise from changes in cultural values, which some social groups cannot accept.

Many historians, sociologists and economists have thus explained the birth of Nazism as a result of the economic crisis and the state of frustration and impoverishment of the small bourgeoisie followed by the great war and German hyperinflation of the 1920s. In the 1980s, Jeffrey Sachs pointed out that in Latin America, at the base of both right and left populist governments, there were the huge inequalities and the resulting social conflicts that characterize those countries. In this situation, the poorest urban classes believed they could find a solution to their problems in populist leaders, who proposed strong stimulus to the economy. However, these policies, after a few years in which they appeared to have achieved good results, caused heavy deficits in the balance of payments, repeated currency crises, hyperinflation, and ultimately a heavy reduction in real wages, which made nothing less than to increase popular discontent.

More recently, the strong growth in inequality has been well documented by Thomas Piketty, and Branko Milanovic⁹. The latter, with its famous elephant curve, shows

9. T. Piketty (2014), *Capital in the Twenty-First Century*, Cambridge, The Belknap Press of Harvard University Press. MA. B. Milanovic (2016), “Global Inequality, A New Approach for the Age of Globalization”, Cambridge, Harvard University Press.

Chart 5: Non-economic issues the party manifestos of Western Democracies



Source: Party Manifestos data from Austria, Belgium, Canada, Denmark, France, Germany, Ireland, Italy, Netherlands, Norway, Sweden, Switzerland and United States, in Zakharov (2013).

how between 1988 and 2008, while many of the poor in the Third World were able to get out of poverty, and few rich in advanced countries showed growth rates close to 70%, Western middle classes were struggling to defend their purchasing power (Chart 4). Globalization, relocation, outsourcing, capital mobility, technological change and consequently the automation of production processes and the development of the so-called knowledge economy, as well as the weakening of trade unions and parties traditionally defending the working class explain these dynamics. The subsequent long and profound economic crisis and the austerity policies that, above all in Europe, were followed by strong public deficits, have made nothing but to impoverish and frighten a broad slice of middle and low classes. Thus increasing inequalities in terms of income and wealth come together with the much more insidious diminishing opportunities for the future.

However, since the late 1960s, the opulent Western societies have also experienced an extraordinary change in cultural values. Attention to gender differences and sexual preferences, tolerance to diversity and minorities, secularization, multi-cultures and environmentalism have become the central value of a wide range of well-educated young people. For the first time, homosexual, ecologist and human rights movements were born. Over time, these trends have also had an impressive effect on traditional parties. So non-economic themes, typical of a post-materialist society, have taken on a very significant weight in the political programs of all major parties (Chart 5).

SOME CONCLUSIONS

It is evident that both economic and cultural explanations interact with each other, making them sometimes indistinguishable from an empirical point of view. For example, the economic crisis may have increased polarization between classes/groups with different cultural values. So the middle class, bearer of traditional values, is obviously more attracted to populist movements where its economic situation deteriorated in relative terms: In the same way it is likely that young, precarious or uneducated persons are more likely to be tempted by nationalistic populist movements and parties. In some respects, it resembles the ancient Marxian memory discussion between structural and superstructure in a modern key, where, of course, we are no longer talking about ideologies or religion, as Weber did, but about the values of a post-industrial society.

Whatever the reasons, it is clear that populist movements are one of the major threat that the rich Western societies are running. Risks to which the traditional right wing and left wing parties are have not yet found adequate response.

DISASTER RISK REDUCTION: A SHARED RESPONSIBILITY

Paola Albrito*

In 2015 alone, 346 disasters were reported, 22,773 people lost their lives and 98.6 million people were affected by those disasters with US\$66.5 billion of economic damages. Globally, disaster losses have increased to \$250-300 billion a year; over 80% of economic losses from disasters are due to weather-related hazards.

Last year in Europe, the number of hydrological disasters showed a 45% increase compared to its decennial average. Still last year 19.2 million people were displaced by natural hazards in 113 countries.

This is a trend that heavily undermines development capacity of affected but also neighboring countries and reverses hard-won development gains, whilst also driving humanitarian needs.

Europe is overall experiencing a challenging moment (migration crises, terrorism, conflict and diplomatic tensions). This situation has given way to the rising of individualist, short term and “inside looking” approaches where values and principles needs to be constantly reminded.

The first consideration that I would like to share with you is that this particular challenging moment requires dialogue, the application of humanitarian principles and human rights approach to ensure a societal constructive commitment. Finding the right narrative to stimulate positive responses to such challenges and addressing their underlying causes has to be part of our common engagement.

One positive development to build upon has been the international community capacity to create coherence in the post-2015 international agendas (Sendai Framework for Disaster Risk Reduction, the 2030 Agenda on Sustainable Development, and the Paris Agreement on Climate Change, the New Urban Agenda). The endorsement of these international agreements and their coherent and mutually reinforcing approaches to their implementation allows avoiding programmatic overlapping of activities and improving financial allocation. Taken together, they urge attention to a wide range of risks facing communities around the world, guide public and private investments towards greater resilience and push delivery towards maximum impact.

The Sendai Framework for Disaster Risk Reduction 2015-2030, the first international agreement adopted in Sendai, Japan in March 2015, recognized that en-

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sureing credible links between these processes contributes to building resilience and achieving the global goal to eradicate poverty in a changing climate.

Implementing disaster risk reduction activities addresses the underlying causes of fragility including migration/crisis situations. Displacement is often an indication of the breakdown of normal coping strategies when resilience is undermined by a severe disaster event. The majority of displacement by natural hazards in 2015 was caused by extreme weather events due to a record number of droughts, widespread flooding and 90 major tropical storms. Much of this was fuelled by a very strong El Niño occurring in the context of climate change.

The recognized reality that disasters due to natural hazards have no borders has allowed for disaster risk reduction to be a topic that has no diplomatic sensitivities attached to it, while national and regional dialogue is consistently valued.

The second consideration is that we are leaving in an interlink society where silos practices are not longer an option. The 2010 volcanic eruption in Iceland led to major economic losses in travel, tourism and trade, amounting to \$4.7 billion globally in just the first week. Similarly, the private sector bore about 95 per cent of the colossal economic losses (\$44 billion) incurred during the 2011 Thailand floods. The Fukushima disaster proved the complexity of cascade effects – an earthquake commenced the incident, causing significant damage on land; the earthquake, then, triggered a series of large tsunami waves; the tsunami caused a major nuclear accident at the Fukushima nuclear power station – and reminded us of importance of ensuring a multi hazard approach in viewing risks. The Great East Japan Earthquake and Tsunami resulted in suspension of production in 80% of automotive plants in Japan, at enormous economic cost, both in Japan and globally. Often, cascade effects of disasters include damages to the ecosystem, to economic activities, disruption of services and damages to cultural heritage, which are fundamental to the prosperity of other economic activities not directly affected by the disaster but rather result from the disruption of the social system of the community.

An interlinked society needs to reflect on the concept of shared responsibility. Disaster risk is rarely made explicit to investors and is often only discovered in the event of a disaster. The short-term profitability of speculative urban development does not encourage consideration of disaster risks, which may only manifest as losses after the development has been sold. Investors or developers rarely take responsibility or accountability for the disaster risk that may be generated and sold on. It is therefore crucial to ensure an all-of-society inclusive approach in looking at disaster risk. The Global Assessment Report on Disaster Risk Reduction (GAR) – a biennial global assessment of disaster risk reduction and comprehensive review and analysis of the natural hazards that are affecting humanity – provides a number of comprehensive examples on the concept of shared responsibility of risks. In its 2013 edition dedicated to the private sector and disaster prevention, the GAR highlights in particular the example of sea level risk and investments in Miami.

My last consideration is that if we want to get ahead of the risk curve, we need to ensure that new developments will be risk proof. This approach systematically applied in shaping up our built environment, our schools, our houses, our bridges and

our roads will ensure that we avoid the creation of new risks in our society. This important reflection is at the heart of the Sendai Framework that outlines seven clear targets and four priorities for action to prevent new and reduce existing disaster risks. It therefore goes without saying that steps towards a more sustainable responsible finance can have a massive impact on economic, social and environmental standards and developments. It equally implies that the private sector needs to be sensitized. New approaches to sustainable urban development provide opportunities for engaging private investors and the construction sector in new public-private partnerships for resilient investments. It also allows for innovation to stretch its muscles and get actively applied. UNISDR has been working on this domain together with the private sector through the ARISE – a private public partnership initiative facilitated by UNISDR – aiming to facilitate risk-sensitive business investments.

Europe is going through a number of financial reforms and we know that reforms are targeting financial requirement. Many of them are related to critical infrastructure: hospital, schools, but also power plants. Let's ensure that the decision taken will be risk informed – this would be a solid step in helping their sustainability.

We need to ensure that a long term approach is applied in our decision making with a constant reconciliation between values and interests. The implementation of the Sendai Framework strongly contributes to the positive narrative in Europe allowing for our society to engage in their resilient and sustainable future.

HOW TO ADDRESS NEW RISKS WITHOUT FORGETTING ABOUT THE OLD ONES

Carlos Ignacio Montalvo Rebuelta*

PREFACE

More than 2,000 years old, Insurance has been dealing with risk since inception... to the extent that, providing risk coverage, was the service that the Sector was built upon, with such concepts as Service becoming the logical evolution, in a more mature market, of the original idea. It goes without saying that, during these very early days, Insurers were confronted with the challenge of addressing new risks. The fact that Insurance remains playing the same role today is a tribute to their success to constantly adapt to risk and to deliver protection, helping Society evolve.

To do so, the very same basics that apply today, namely identification of risk, its quantification, management and mitigation (sometimes including transferring, always embedding law of large numbers and mutualization of risk) as the elements used by Insurance undertakings to be able to take, absorb and place risk in the right place at the right time.

Lord Byron used to say that “the best of the prophets for the future is the past”, and past performance of Insurance provides us with the much needed trust that it will continue to deliver.

THE BUSINESS MODEL: ASSETS AND LIABILITIES

Insurance, although originally focused on the liability part of its business, has gradually balanced such situation, increasingly giving the importance it deserves to the asset part of its balance sheet, maximizing (or at least trying to) the fact that, as a direct consequence of its unique business model, and the embedded reversion of the normal economic cycle (leading to premia being collected before claims are to be paid), Insurance holds a unique liquidity position that should allow it to be active investors for the Economy, thus creating a virtuous circle by which it takes, mitigates and holds risks and at the same time it becomes a key institutional investor to the Economy, with a privileged position, particularly in the Life Business, to take long term asset risk (and earn a liquidity premium for it), enhancing profitability and, most interesting,

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allowing it to reinvest part of this profit in reducing the price for risk to the Economy, thus de facto taking more risk from it... at a better price.

From a liability viewpoint, one question pops up immediately: Is Insurance able to take all risks, including new ones for which not sufficient data and experience is available? Although we will further elaborate this idea with the example of Cyber risk in the next paragraphs, this seems to be the case... albeit the pricing issue remains there.

From an asset perspective, Is Insurance already playing its role as institutional investor? The response is again affirmative, as any asset it holds, from Equities to Bonds, is already financing the Economy. At the same time, the issue of how to properly factor in the way volatility should be treated remains a hot topic.

It goes without saying that all this can only be maximized with a proper ALM strategy that exploits opportunities in terms of earning liquidity premia and minimizes the so called reinvestment risk created by a mismatch of assets and liabilities. Good ALM is an integral part of any sound risk management policy by an insurer, and as such needs to be approached... and even incentivized.

THE SITUATION TODAY... AND TOMORROW

Today's reality is a fascinating one for Insurance, yet perhaps the most challenging one it has been confronted with during its long history. All the elements intrinsic to Insurance, namely the risks, the products, the information available and, equally important, the client and his expectations, are changing at an unprecedented speed. At the same time, external elements are changing as well, with political uncertainty, monetary policy or demographics, inter alia, becoming powerful drivers for change.

Interestingly enough, Insurance has been known as a Sector where risk aversion is part of its DNA, particularly when it comes to change... So how will the two mingle will define the future of Insurance (not necessarily the way we know it today).

Among the range of so called "new" risks that emerge in this period of time, I would like to focus on two, as I consider them as particularly relevant as potential obstacles to growth and development: Cyber risk and Climate risk.

Cyber risk is nothing more than the "dark side of the moon" when it comes to Digital transformation and the underlying opportunities it brings. The European Commission has quantified the opportunity in the range of 500 billion euro... whilst the first quantifications of cyber risk are in the range of 400 billion, out of which barely 3 billion is covered by Insurance. It is paramount that cyber risk doesn't stop digital innovation, and Insurance must be there to help. However, there is still a long way to go. The complexity of the subject, the lack of historic series and data, a proper claims management system or the size of the tails are among the issues that need to be addressed. The good news is that none of them should be a stopper, the better news is that Insurance is approaching them with prudence, avoiding the unintended consequences of a false "euphoria" triggered by the idea of a massive busi-

ness opportunity, in a completely new area... without proper underwriting and controls. There is no better way to exploit an opportunity than understanding it, and this is precisely the journey Insurance is currently embarked on. A final consideration on cyber risk: if we approach it as a pure IT issue, we will certainly get it wrong. Board education and integration within the business model come as the right way forward.

Climate risk, although always present, has never been as prominent as today, nor as potentially devastating to the Economy. It is worth mentioning that the protection gap has increased significantly in the last 20 years... even in developed markets! Looking at different catastrophes in the last years, we can extract some findings: In New Zealand, following its last earthquake, the GDP grew thanks to proper use of Insurance money paid. Both the country's high coverage and the smart and forward looking thinking of the country and its society led to this outcome. In Nepal, however, the impact was in the range of 40% GDP loss... still to be recovered, but this is nothing compared to the human dimension of it, with more than 8,000 casualties. Again, insurance and reinsurance undertakings can be part of the solution, playing the social role that our sector has, and doing so under the assumption that, like with any other business, it can be done with a profit. Diversification of risk as a way to take more risk, of course, but also knowledge and pre-emption, shall become success factors in this race to close the current gap. Private-public initiatives such as the IDF (Insurance Development Forum) are steps in the right direction.

THE "HIDDEN RISK" OF FOCUSING ON NEW RISKS

As relevant as it is to make sure that sufficient time is allocated to discuss, understand and address new risks, it should not lead to removing the attention to existing ones, perhaps less fancy or trendy, definitely not less important.

Among the range of "old risks" that risk getting ignored or downgraded, one comes on top of the list: Demographics.

Indeed, not a new issue, particularly in developed markets, but one that is always pushed out of the agenda, either because of political reasons, social ones or because short term views tend to prevail over long term ones, and it becomes easier to let someone else take the hit that it implies addressing the demographic challenge we are confronted with.

Demographics imply higher reliance and dependency in Health coverage. This can be provided by the State, but by stepping in, Insurance is de facto alleviating the bill to Society, allowing governments to continue providing the same level of coverage, regardless of the current public debt levels and budgetary pressure.

Most importantly, demographics implies looking at Pensions sustainability. The good news is that we have time to take action, the bad news is that time has in the past been the excuse for inaction. Insurers should become key players in terms of the solution, by providing long term protection to citizens that will complement their Pillar 1 or Pillar 2 pensions. Initiatives like the PEPP (Pan European Personal Pen-

sions), initiated by EIOPA and integrated by the European Commission within the CMU (Capital Markets Union) programme will become part of the solution... today better than tomorrow.

EPILOGUE

At the end, it all comes to the basic question of How can Insurance enhance Resilience? The long story short is that it should be a preferred owner to certain risks, particularly long term ones, and a key partner to mitigate and reallocate others. By so doing, it will be adding value not only by allowing business to move ahead when taking the risk, but also indirectly via enhanced preemption or better recovery by its clients. On top of that it will continue playing a key role as institutional investor, providing with much needed capital to the Global Economy. Who can do better?

**FINANCE FOR DEVELOPMENT:
A EURO-MEDITERRANEAN PERSPECTIVE**

INVESTMENT IN A EURO-MEDITERRANEAN PERSPECTIVE

Giovanni Ajassa*

We discuss the issue of development of real investment and finance, taking a Euro-Mediterranean perspective. I am an Italian economist working at a major European bank with strong ties and presence on the southern and eastern shores of the Mediterranean. For BNP Paribas the Euro-Mediterranean relationship represents not only an important part of our history. For us, the Euro-Mediterranean relationship means future. A future of sound economic development for our clients working in the area, among them hundreds of Italian SMEs. A future of innovation and inclusion for social communities, starting from the thousands of colleagues working with BNP Paribas from Maghreb to Turkey.

I well know that the association between development and Mediterranean may sound quite hazardous today. After great hopes, Arab springs turned into disillusionment, although not everywhere. Threats from a new and wicked form of terrorism have challenged geo-political stability. Pressures from increasing flows of migrants heading north from sub-Saharan Africa risk to tilt the European perception of the Mediterranean to a source of serious problems instead of a sea of shared opportunities.

Notwithstanding this complex background, my task this morning is to submit to you a few numbers from the economic scenario which may support the case for investment into the Euro-Mediterranean perspective. I will start from a more global perspective: the need for higher investment as the only way to escape the doldrums of secular stagnation.

THINK GLOBAL: INVESTMENT TO ESCAPE SECULAR STAGNATION

John Maynard Keynes stated the point very clearly. It was exactly 80 years ago, at the time of writing the General Theory:

(...) there has been a chronic tendency throughout human history for the propensity to save to be stronger than the inducement to invest. The weakness of the inducement to invest has been at all times the key to the economic problem.

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Eighty years after, what the global economy is experiencing again is a massive disequilibrium between the abundance of saving and finance and the scarcity of investment and development projects. It is not only a matter of quantities. What is becoming more and more evident is also a kind of fatigue in the ability of drafting a new model of growth: a growth which has to be sustainable in a context of binding limits from long-run factors such as planet-population increase and ageing, nonrenewable resource depletion, pollution generation and the affirmation of labor-squeezing digital technologies. So, coming out from the current experience of secular stagnation is getting much more difficult now than it was 80 years ago as it requires not only to run more investment, but to do the right investment. Putting it in another way, what we need now is to combine the activist attitude from the General Theory with the long-run view on sustainability of the Club of Rome's seminal workings¹.

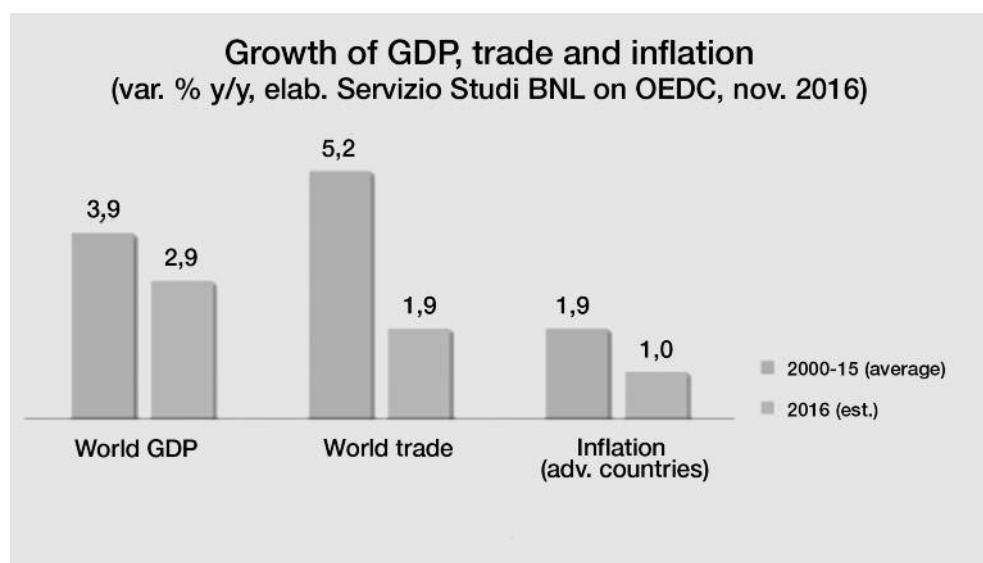
From words to numbers, let me now turn to some snapshots about the current global growth's problem. I make reference to OECD and IMF data and estimates.

According to latest forecasts, in 2016 the world's GDP is going to grow by a mere +2.9%, slightly below the +3% threshold that marks the limit for a global recession. Low growth in volumes combines with a fairly dramatic deceleration of world trade, which this year may fall below 2%, less than one half of the average growth of the 2000-15 period. The picture of overall stagnation is then completed by a third element which is as important as low growth and low trade. This third actor in the play is a very low inflation: too low for a too long time to be any more deemed as a blessing. With a +1.0% forecast, inflation in advance economies is going to be just half of what central banks' wisdom considers as appropriate. For Italy, average inflation in 2016 will mark an even weaker result, with several unpleasant consequences: to name just one, a negative effect on the public debt to nominal GDP ratio.

How to break the vicious circle of low growth, low international trade and low inflation? Sound and simple, the answer is with more investment. Monetary stimuli in the form of conventional or unconventional measures can help, but cannot suffice. Quantitative easing cannot last forever, on both shores of the Atlantic. By the way, as for any cure unpleasant trade-offs do exist also for monetary expansions. So resuming fixed capital formation is now worldwide viewed as the tool for giving growth a stronger, a more domestic and a better drive.

From the European "Juncker Plan" to the latest plans from the new American administration, economic policies have finally embarked into concrete measures for accelerating investment, both public and private, and through public-private partnerships. The good news is that the move has globally started. A question to be answered is whether the Euro-Mediterranean will join.

1. Donella H. Meadows, Dennis L. Meadows, Jorgen Randers William W. Behrens, *The Limits to Growth*, A Report for the Club of Rome's Project on the Predicament of Mankind, 1972.

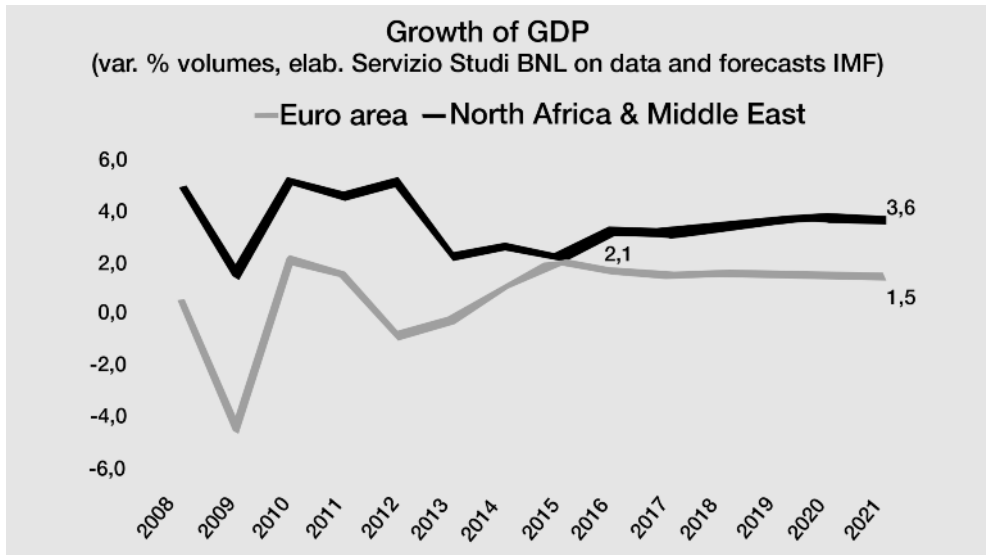


INVESTMENT IN THE MEDITERRANEAN? YES, WE CAN

Investment pave the way for future growth. And better economic prospects are needed to stimulate investment and to convince foreign capital to flow in. Past years have seen many sorts of troubles burdening the scenarios of the economies of North Africa and the Middle East. However, starting from last year economic ex-post performances as well as future projections have improved. According to the latest forecasts released by the IMF, the growth rate of GDP of the whole group of MENA countries may go up from 2 per cent to close to 4 per cent in five years time.

Economic recovery will benefit from a common and exogenous factor that is the firming of oil price movement after the sharp downward correction occurred in 2014-15. In my view, stable and remunerative oil prices will be helpful for non-oil producers in the area too, thanks to indirect advantages from higher prices of non-oil raw materials. Moreover, oil price stabilization may positively interact with the reduction of geopolitical risks that the advances in the international fight against terrorism are already obtaining. On this ground, a key passage will be represented by the full restoration of political stability in Lybia. Besides future improvement, what already supports the economic case for making investment on the southern shores of the Mediterranean are the virtuous results obtained by countries such as Morocco.

As this morning I have the privilege to sit close to His Excellence, the ambassador of Moroccan Kingdom, Mr. Hassan Abouyoub, let me just remind us how only a few days ago the International Monetary Fund has very positively judged the macroeconomic development in that country. The IMF mission stated that “in recent years, the Moroccan economy has benefited from the continuation of prudent macroeconomic policies and structural reforms as well as favorable developments in oil



prices. Improved fiscal management and diversification of the economy have strengthened its resilience.”²

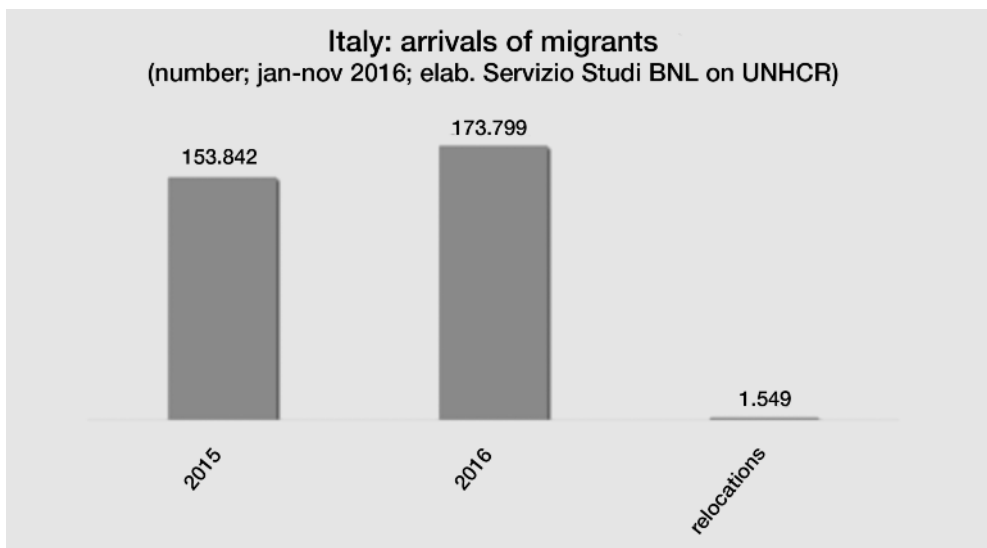
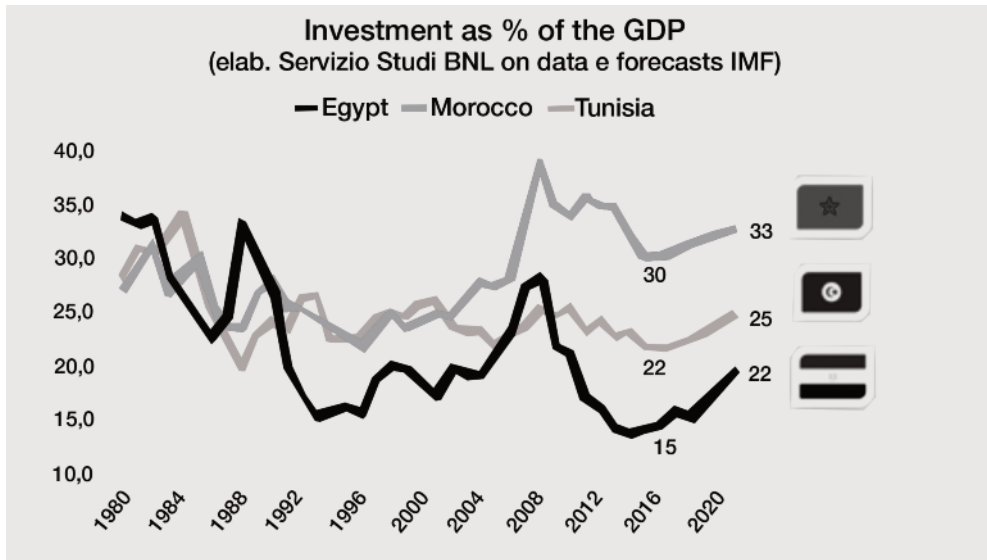
Diversification of the sources of economic growth, together with reforms and measures aimed at improving the business environment, increasing productivity, and raising the quality of the education system are key priorities in countries such as Morocco. Diversification, reforms, productivity, and education are key-issues that come together with higher investment as parts of a medium-term strategy whose final goal is a more inclusive growth with lower unemployment, particularly among young people. Lead by example: what Morocco is doing, I think, may set a kind of benchmark for the entire area and for an increasing Euro-Mediterranean cooperation on investment.

FINALLY, INVESTMENT IN THE MEDITERRANEAN? YES, WE MUST

As I run short of my five minutes, let me now conclude with a final thought on an even deeper reason to back the case for higher investment from Europe into the Mediterranean. More than Keynesian, I turn to the long-run viewing of Aurelio Peccei’s Club of Rome. So, moving from current issues to a more forward-looking perspective, the reason why Europe must invest more into the Mediterranean has anything but one name: demography.

In the last number of the *Journal of Economic Perspectives* two influential American scholars illustrate how in the coming three decades, because the Americas are entering an era of uniformly low population growth, labor flows across the Rio Gran-

2. IMF, End-of-Mission Press Release of 2016 Article IV Consultation and First Review of the Precautionary and Liquidity Line Mission to Morocco, December 1, 2016.



de will slow markedly. On the contrary, Europe will face substantial demographically driven migration pressures from across the Mediterranean for decades to come³.

Being the recipient of hundreds of thousands of sub-Saharan migrants who risk their lives to cross the Mediterranean, Italy is well aware about the need for higher investment from Europe into Africa. Not walls, but yards are needed to improve employment and economic growth in Africa, thus moderating migration pressures. Time for Europe is to invest into a “migration compact”.

3. Gordon Hanson, Craig McIntosh, “Is the Mediterranean the New Rio Grande? US and EU Immigration Pressures in the Long Run”, *Journal of Economic Perspectives*, Vol. 30 No. 4 Fall 2016.

TIME, SPACE AND FINANCE:
A PRAGMATIC APPROACH TO THE MEDITERRANEAN

Domenico Arcuri*

I'm glad of the opportunity to add my thoughts to the somewhat dated debate about the Mediterranean whose glorious and extraordinary history we can admire on one horizon, and whose present and future we can observe on another.

In today's world, time has won its battle against space and money. I have long been firmly convinced of this.

What do I mean by time having won its battle against space? I mean that the places where goods and services are produced or can be produced – places where wealth can be created – are no longer necessarily those where the basic conditions for this happening. They are no longer, as we were told years ago when we were students, the places that have the primary factors of production, nor are they the places where consumers, able to transform the production of goods and services into wealth, live. This model no longer exists. Today, a growing quantity of goods and services, which means an increasing amount of wealth, is produced in the places where their production is easier and faster.

I believe that time has also won its battle against money. The financial assets available for allocation and conversion to investment – and thus to produce wealth – are not necessarily assigned where national systems provide financial incentives to make this happen, but where investors feel confident that such investment will produce a profit in a short period and with a reasonably high probability. A large international investor does not invest in Italy because the government and Invitalia give him money to reduce the shortfall between the amount of investment needed and assets available for the investment, but only because he is certain that the investment will be converted into wealth in a reasonable time.

Let me give you two examples. The first concerns COSCO, a large Chinese multinational company that spent €3.3 billion in 2010 to obtain a 35-year permit for a second quay in the port of Piraeus in Greece, where during that time it will handle large quantities of goods, and will produce greater wealth than in the past. The company did not choose the Italian ports of Taranto or Gioia Tauro. An average of 17 days is needed to move a container in Italy today, against 11 in Morocco which thus has a 6-day advantage over Italy. Without considering incentives that governments offer, COSCO chose to invest in Greece because this offers a shorter time to produce

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returns. So time won against space and against money. (The Italian government has in fact launched an important and welcome reform of the ports, an effort that needs to be continued.)

The second example concerns tourism. During the past 10 years the percentage of GDP that tourism brought to the Mediterranean countries has been characterized by a substantial increase. In southern Mediterranean countries the increase has been 500%, in Turkey 400% and in Morocco 170% while in Spain, Italy and France it has only been 20%. Yet again time has won against space and money.

I trust that these two examples make my opinion clear about the possibility of looking to the future of the Mediterranean and not dwelling on its past. European countries on one side and Mediterranean on the other need to respond coherently to the realities of today's economic world. Time has won against space, and time has won against money. Countries will develop if they are on the side of the winner. As for those that side with the loser, indulging in talk and still believing that the economic incentives are enough for GDP growth, I hope this reflection will be useful.

ALTERNATIVE FINANCE FOR DEVELOPMENT IN EUROPE AND THE MEDITERRANEAN

Innocenzo Cipolletta*

Alternative finance, represented by firms operating in private equity, venture capital, and private debt, is playing a fundamental role within the disintermediation process from the banking system. In fact, banks are facing growing obstacles in adjusting their assets along tighter European rules.

The credit crunch has affected – and still affects – particularly SMEs, which mostly depend on domestic demand. In spite of accounting for the greatest majority of the Italian entrepreneurship, this kind of enterprises has been receiving less credit from the banking system.

Traditionally, financing channels of enterprises in Italy have relied mostly on banks. Therefore, the current system needs to be supported by complementary channels for the supply of credit; thus, the presence of a “private capital/equity systems” can be seen as a guarantee for sustaining the growth of SMEs. Actually, this private equity system can facilitate an orderly disintermediation of the banking sector, providing an adequate amount of equity, which could counterbalance debt capital, as repeatedly stressed by the European Commission.

How does the alternative finance system operate? Alternative Investment Funds enter the company through private equity injections, typically un-listed SMEs, thereby trying to support their development plans both on a domestic and on an international level. To that aim, they offer financial resources, along with the skills that fund managers have acquired in their professional career.

Now, under the European Directive on Alternative Investment Fund Managers, whose intention was to harmonise organisational rules of alternative funds, such financial subjects can do their business everywhere, starting from the country selected as operation basis (European Passport).

Therefore, I want to draw on what was said by Giovanni Ajassa and by Ambassador Abouyoub about entrepreneurship development in the South-Mediterranean area, in order to reflect on possible business opportunities which could be promoted by Italian private equity funds already used to operating on an international level.

Both enterprises and infrastructure projects can be supported by private capital operators, able to carry on international development plans, grow responsive enterprises, finance technological start-ups as well traditional ones.

* Chairman, Italian Association of Private Equity, Venture Capital and Private Debt – AIFI.

We should not forget that operators specialising in alternative finance have the advantage of combining both private capital for growth and professional managerial skills, which they bring to the firms where they invest. This means that they contribute not only through finance, but also through renewed management skills. Opening up to this opportunity would have the undoubtable benefit of putting enterprises that operate south of the Mediterranean into a net of enterprises which would accelerate their growth path and reinforce their competitiveness.

As President Pittella has recalled, Europe is also promoting a strong recapitalisation of the industrial system: firstly, the fundamentally important role played by the European Investment Fund (EIF), which has already been mentioned and specifically created in order to underpin SMEs risk capital. Moreover, we should not forget that one of the aims of the Capital Markets Union, as it appears from the Commission's documents, is the broadening of financial resources for innovation, start-ups and non-listed enterprises, particularly for SMEs and innovative enterprises.

Given all this, and in order to make North-African companies an attractive target for investors, not only from Italy but from the whole of Europe, a suitable system of guarantees should be ensured. If, on the one side, it is clear that private capital investments naturally imply also an entrepreneurial risk, related to the ability of generating entrepreneurial capacities, on the other side it is not obvious that private equity investors must automatically also bear the political and institutional risks, which could derive from their investments.

Starting with public guarantee systems already in place, it would be appreciated that they be reinforced by European guarantee systems, which could cover investment risks in more politically risky areas, in order to let the investor assume only its natural entrepreneurial risk.

From my experience as General Director of the Italian Association of Enterprises (Confindustria), I remember that together with other colleagues of the South Mediterranean area, we had launched a dialogue between the North and South side of the Mediterranean, notwithstanding the multiple obstacles that this platform had to encounter. On this path, and wishing for a continuation of the physical and virtual Mediterranean dialogue, we should prevent North-Africa from abandoning mutual exchanges. On the contrary, we should continue to encourage a process of increased integration with the rest of Europe, in order to attract Europe's abundant amount of investors and capital.

IMPROVING THE MEDITERRANEAN FINANCIAL ENVIRONMENT: A PARTNERSHIP APPROACH

Giuseppe Papaleo*

INTRODUCTION

Before the birth and evolution of the Barcelona Process (1995), the European Union only entertained bilateral relations with the countries of the Mediterranean basin, and not a single policy for the region was present. In 1995, during the Spanish Presidency of the EU, the Barcelona Process was launched by 15 EU members and 12 Mediterranean partners, as a framework to manage both bilateral and regional relations. The Barcelona Process – based on the Barcelona Declaration – formed the basis of the Euro-Mediterranean Partnership, and its aim was to establish a common area of peace, stability, and prosperity, by reinforcing three key aspects: political and security dialogue; economic and financial partnership; social, cultural and human partnership. The Barcelona Process foresaw the adoption of a series of bilateral Association Agreements between EU Member States and the Mediterranean partner countries. While certain aspects are common to all of them (political dialogue, economic cooperation, etc.), details differ from country to country. Since the 1995 Barcelona Conference, several more Euro-Mediterranean Conferences of the Ministers for Foreign Affairs have been held, where important decisions have been taken. From a political standpoint, results have been scarce in terms of the stabilization of the region, the promotion of democratic reform, and the liberalization of politics. As regards the economy, the gap separating the North and South rims of the Mediterranean in terms of GDP per capita has not been reduced, and the creation of a productive trans-Mediterranean system isn't being fostered. In addition, the trade relations between the EU and the Mediterranean partners remained unbalanced, and due to low foreign direct investment (FDI), economic integration has remained weak.

THE MEDITERRANEAN ECONOMIC SITUATION: WHERE DO WE STAND?

The Mediterranean region has experienced significant social, political, and economic transformation during last year. Examples of these include widespread social protests and change of governments in southern Mediterranean countries, and grave

* President, Institute of High Euro Mediterranean Studies – IASEM.

concerns about fiscal health, banking systems and stagnant growth across a number of northern Mediterranean countries that are also members of the Eurozone. These events, which have created significant uncertainty for markets, policy-makers, and individuals in the short term, make it even more important today to consider how these changes and the underlying trends and uncertainties that shape the region may play out in the long term. The aim of our project, MCH Alliance for Finance and Banking is specifically directed to the creation of a series of fruitful meetings in order to implement an integrated reporting system, which connects the financial and banking actors with the entrepreneurial one, the politics' representatives with the world of culture. Monetary and private financial integration between the European Union and the Mediterranean is a crucial hub for the development of trade, the expansion of financial markets and the strengthening of cultural contacts between the two shores of the Mediterranean. As part of the financial globalization process, this area reaps great success, but with strong emphasis on environmental and religious aspects, which always make the relationships between the two shores of the Mediterranean permeated by a strong character of informality (which implies widespread pegging processes, cross-fertilization and transnational dialogue). This makes the ability to fit into a structured system of relations and fluid at the same time, able to adapt to fluctuations in the political, economic, and cultural scene, an essential point. MCH – Alliance for Finance and Banking is a strategic way to build or expand relationships in the Euro-Mediterranean Area. The network is a structured container, but in constant reorganization, with the aim of taking into account environmental factors and the evolution of "human factor" in the construction of financial and banking projects. MCH – Mediterranean Common House was born from the expertise of the IASEM Steering Committee, active for 10 years in the Euro-Mediterranean relations, which intends to make available to international finance and banking system, its networking capabilities. Furthermore, the Network offers the possibility of structured multilateral meetings between partners two times per year:

- MED FINANCE&BANK – Annual Meeting among the Members of the Alliance for Finance and Banking.
- INTER-MEDITERRANEAN MEETING – Annual Meeting among all the MCH (Mediterranean Common House) Partners.

The aim of the network is also to encourage bilateral relations and the right exchange of information among the Partners with the intention of implementing joint projects. In addition, MCH – Alliance for Finance and Banking develops ad hoc services, with the aim of assisting the Partners in developing networking strategies, public relations, or lobbying.

To join the Network is required to sign the Memorandum of Understanding between the partners and the Leading Proponent (IASEM). It must be signed by the legal guardians or their delegates.

Last but not least, the aim of our alliance is to get involved with all the different financial intermediaries and all the banking actors eager to interact with their pe-

ers in the Mediterranean region. The construction of deep relations between all actors interested in the Mediterranean would be implemented under the supervision of Mediterranean Common House. We believe that, at this time of great social, political, and economic uncertainty, there are huge gains to be made by focusing on the opportunities of collaborative investment in the long term. Yet, there are equally significant risks that we have to deal with. In any case we hope that our experience could lead us to meaningful and productive strategic conversations between local stakeholders.

The Mediterranean today is a highly fragmented region, composed of a wide variety of sub regional groups, exposing one of the sharpest divides in GDP per capita in the world. Recent economic trends, however, indicate a gradual change in regional economic dynamics: fiscal pressures have negatively affected northern Mediterranean growth rates while economic reforms and greater openness to trade have been associated with surging growth rates in several southern Mediterranean countries, before the developments of 2011 again diminished the short-term growth outlook. In 2015, the average income per capita in the South and East Mediterranean countries was 2.5 times lower than the average income in the EU Mediterranean countries. The GDP growth rate in the south and east Mediterranean countries were much higher than those of the EU Mediterranean countries. However, they are considered low when compared to the population growth rates, as the demographic growth is still high in the southern Mediterranean countries. The share of the Mediterranean GDP in the world GDP is also decreasing: from more than 13.5% in 1990 to 11.5% in 2010 and 9.5 % in the two-year period 2015-2016. Meanwhile, the share of the Mediterranean population remains constant in the World population (about 7%). For what concerns trade patterns across the region, they are very variegated. While north-south trade across the Mediterranean is strong, southern Mediterranean countries have the lowest levels of trade integration globally between neighbouring countries, with on average only 5.7% of their total trade being conducted within the southern Mediterranean region. Competitiveness varies significantly among the countries of the region, with rankings from 16th to 116th out of 138 economies take in consideration in The Global Competitiveness Report 2016-2017 (which providing insight into the drivers of their productivity and prosperity). In comparison to other regional groupings, such as the North American Free Trade Agreement (NAFTA) region, we can note that the competitiveness of the Mediterranean as a whole lags behind considerably across all areas, but in particular with respect to market size, innovation, labour market efficiency and financial market development.

FINANCIAL INTEGRITY OF THE MEDITERRANEAN COUNTRIES

When assessing the trade finance environment in the Mediterranean region, one has to differentiate carefully between the countries they are looking at, as they differ substantially in terms of legal environment, transparency, sophistication and political structure. This is probably one of the reasons for which the region has never come

together to form a trade union similar to the African ones, like COMESA (The Common Market for Eastern and Southern Africa). Such trade unions can indeed support trade flows significantly and there have been initiatives for the Mediterranean region in the past, to no avail. Mediterranean region represents 21 countries and over 500 million people speaking at least 20 different languages. Trade patterns have clearly changed in recent years, which means that major emerging economies are likely to collectively take on a larger and rising international net asset position, albeit at a diminishing rate given the general market situation. Over the last couple of years the Mediterranean partner countries have gone through an unprecedented phase of transformation, forcing them to tackle a multitude of economic, political and social challenges. While the region benefits from a vast growth potential, arising not only from its geographical location and climate, but also from its young and well-educated population, it has in the past failed to generate the growth required for sustained and inclusive economic development. Banks are thus increasingly being called upon to support private sector development by increasing credit supply to businesses and entrepreneurs. This is a role that the sector, despite its size, has only partly fulfilled in the past. Throughout this challenging period, the European Investment Bank through the Trust Fund Internship Programme has sustained its support for the Mediterranean partner countries. The EIB has received a reinforced mandate, and has consequently adapted its activity to the new economic and social reality in the region. Overall, the bank has been very active in supporting the private sector's access to finance over the past decade, and it is ready to increase its efforts in this area in order to contribute to the development of a dynamic private sector and job creation in the region.

BANKS' FUNCTIONING IN THE MEDITERRANEAN PARTNER COUNTRIES

The Mediterranean partner countries (MPC) face the common challenge of improving their economic performance, especially in the aftermath of the Arab Spring. GDP per capita has increased only slowly over the last decade, particularly compared to some other emerging market economies. At the same time the population in the region has been growing at a rapid pace. The combination of low growth and a rapidly increasing working age population has caused unemployment to skyrocket-especially among young people. In addition to structural shortcomings, the implications of the Arab Spring coupled with a difficult international economic environment have put strains on the MPC economies. GDP growth has slowed down and recovery is sluggish; increased expenditure has deepened government budget deficits; and current account deficits have widened especially as the European economy has weakened. The difficult economic situation of some of the MPCs has been reflected in a deterioration of their sovereign risk ratings. The private sectors in the MPCs are largely dependent on the banking sectors for external debt financing as financial markets are dominated by banks. Banking sectors in the region are generally large. However, financial inclusion is still relatively low in the FEMIP region, with more than half

of the adult population without an account in a formal financial institution. The relatively low access to financial services in the region often hits SMEs particularly hard. Bank lending is traditionally concentrated in large, corporate customers, and banks in some FEMIP countries use a substantial amount of their available liquidity to fund government debt. Generally, banking intermediation remains relatively weak in the region. Private sector credit as a percentage of GDP is particularly low in Egypt, where the government finances its increasing debt mainly through the domestic banking sector and over a third of the banking sector's balance sheet consists of government securities. At the same time, some countries exhibit low loan-to-deposit ratios, e.g. Lebanon where less than half of the banking sector's large deposit base is used to extend loans to the economy. In contrast, Morocco and Tunisia have loan-to-deposit ratios in excess of 100%. In both countries the banking sectors have difficulties matching rapid loan growth with adequate deposit growth, which leaves them in a difficult liquidity position. This can, on the upside, lead to banks looking for a diversification of their funding sources, such as bond markets, which is a trend observable to some extent in Morocco. The overall soundness and profitability of banking sectors in the region have deteriorated but nevertheless remain reasonable despite the difficult domestic and international economic environment of recent years. As expected, the economic downturn in some countries is impacting the performance of banks and especially the loan quality of banks' loan portfolios. The most affected banking sectors are in Tunisia and Egypt given the severity of the economic and political struggles in the aftermath of the revolutions in both countries. In other countries in the region the repercussions are also tangible, for instance through liquidity squeezes. Regulators in most countries in the region have reacted by implementing different measures to support banks. However, further measures to strengthen the banking sectors and improve regulation and supervision will be necessary in some countries to increase the capacity of banks to support more efficiently the development of the private sector.

POSSIBLE WAY TO INCREASE FINANCIAL SERVICES IN MEDITERRANEAN PARTNER COUNTRIES

Access to financial services across most Mediterranean partner countries is relatively low, as only 36% of the population aged over 15 has an account with a formal financial institution. Excluding Israel, whose access to finance ratio (at 90%) is at par with that of high income countries, the average of the remaining seven MPCs stands at 28%. This is lower than the average for the upper middle income group of countries (of which Algeria, Tunisia, Jordan and Lebanon are part) and approximately the same as the average for lower middle income countries (of which Morocco, WBG and Egypt are part). Thus, countries in the region face an important challenge in terms of access to finance which, to some extent, jeopardizes their economic development and contributes to income inequality. In sharp contrast with relatively low access to finance, mobile phone penetration is very high across almost all MPCs – the avera-

ge penetration rate is 106%. This combination of high mobile penetration and low access to financial services suggests that mobile financial services can be a useful instrument to increase the use of formal financial services in all the countries in the region – perhaps with the exception of Israel. That large potential notwithstanding, mobile banking offerings can only become a useful tool in expanding access to finance to households and small businesses in MPCs if they meet potential customers' needs. Supply should adjust to prevailing conditions and not give in to the temptation of blindly adopting models that were successful in other parts of the world. In particular, it needs to recognize that financial sectors in MPCs are bank dominated and that mobile banking services should complement existing banking products and serve as a means to expand banking services to larger segments of the population. That said, even well designed business models face a significant number of implementation challenges, of which the flexibility and adaptability of existing regulatory frameworks is undoubtedly the most relevant. But the success of those offerings will also depend critically on a few basic infrastructures such as (dense) distribution networks, risk analysis databases and methodologies as well as retail payment architectures that ensure interoperability and decrease transaction costs. On the other hand, some favourable conditions such as international remittances can provide the necessary lever for a successful uptake of mobile banking in MPCs.

**FINANCE FOR THE COMMON GOOD: NEW APPROACHES
TO SOLIDARITY, INCLUSION AND SOCIAL RESPONSIBILITY**

FINANCE FOR THE COMMON GOOD: SOLIDARITY, INCLUSION AND SOCIAL RESPONSIBILITY IN THE LIGHT OF THE SOCIAL DOCTRINE OF THE CHURCH

Archbishop Silvano Maria Tomasi*

The title of my contribution on the topic: “Finance for the common good: new approaches to solidarity, inclusion and social responsibility”, contains in itself many important concepts that I will try to address in the light of the Social Doctrine of the Church. First I will explore the concept of finance for the common good and secondly I will report on new approaches to solidarity, inclusion and social responsibility in the domain of finance, to which the Pontifical Council for Justice and Peace, now incorporated in the new Dicastery, has been looking at in recent conferences and international gatherings.

FINANCE IN CATHOLIC SOCIAL TEACHING

Let me begin with looking at the idea of finance, or better of “finance for the common good”, present in the Catholic Social Teaching. Finance is not something new to the Catholic tradition. Indeed, in Italy in the second half of the 15th century the Franciscans were responsible for the birth of pawnbroking – in Italian known as *Monti di Pietà* – the first experience of microfinance destined to the more vulnerable sectors of the population. The weakest members of society were in this way helped to defend themselves against usury and to derive real benefit from this tool of economic development. In the case of these first pawnbroking, finance – or better microfinance – was conceived as an instrument directed towards improved wealth creation and development of the poor.

In November 2008, on the eve of a Conference sponsored by the United Nations General Assembly in Doha on “Finance and Development to Review the Implementation of the Monterrey Consensus”, the Pontifical Council for Justice and Peace published a Note titled “A New International Financial Pact”, which declares that the “true” nature of finance consists in favouring the use of surplus resources to promote the real economy, which means the well-being and development of the whole person and of all people¹. Indeed, finance for the common good is a finance de-

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1. Cfr. Address of Pope Francis to the General Assembly of the United Nations, 25.9.2015.

voted to serving the real economy, it is a finance conceived as an instrument for reaching the common good meaning by that the sum total of social conditions which allow people, either as groups or as individuals, to reach their fulfilment more fully and more easily².

Now one interpretation of the global financial and economic crisis that began in 2007-2008 – and still has not been completely overcome – attributes it to the loss of this “intrinsic” nature of finance. Finance had failed to fulfil its authentic function of a bridge between the present and the future, because its operators’ timeframe had been reduced essentially to the present, to the search for the maximum achievable short-term profit.

Hence, economics and finance should be brought back within the boundaries of their real vocation and function, including their social function, in consideration of their obvious responsibilities to society – for example that of nourishing markets and financial institutions which are really at the service of the person and are capable of responding to the needs of the common good and universal brotherhood³.

In his address to the participants in the 2016 International Conference of the Christian Union of Business Executives (UNIAPAC), on the past 16th of November, Pope Francis declared the urgency of restoring the social meaning of financial and banking activities. “Credit must be accessible to households, to small and medium-sized enterprises, to farmers, to educational activities, especially at the primary level, to general healthcare, to the improvement and integration of the poorest urban areas. A market-based financial logic makes credit more accessible and cheaper for those who already have resources, and more expensive and difficult for those who have less, to the point of leaving the poorest segments of the population in the hands of ruthless usurers”⁴.

NEW APPROACHES TO SOLIDARITY, INCLUSION AND SOCIAL RESPONSIBILITY

Moreover, Pope Francis in his more recent encyclical letter *Laudato Si'* calls for a renewed sense of responsibility on the part of all for the common good and for our fellow brothers and sisters worldwide⁵ and this in a spirit of fraternity. Indeed, fraternity is an essential human quality, for we are relational beings. A lively awareness of our relatedness helps us to look upon and to treat each person as a true sister or brother; without fraternity it is impossible to build a just society and a solid and lasting peace⁶.

2. Cfr. Compendium of the Social Doctrine of the Church, LEV, 2005, § 64.

3. Cfr. Pontifical Council for Justice and Peace, “Towards reforming the financial and monetary systems in the context of global public authority”, 2011, pag. 15.

4. Pope Francis, address to the participants in the International Conference of the Christian Union of the Business Executives (UNIAPAC), 16th November 2016.

5. Cfr. Pope Francis, Encyclical Letter, “*Laudato Si'*”, n. 25 and n.196.

6. Cfr. Pope Francis, Message for the World Day of Peace, 1st January 2014.

The world truly needs renewal of the sense of responsibility on the part of all. To achieve this, it is necessary to connect with people's deepest moral being through education in responsibility for the common good, which should be offered to all actors on all levels: financial agents, businesses, financial institutions, public authorities, and civil society – and even families⁷ and which can find its solid foundation in fraternity and in other principles of the Social Teaching of the Church, such as the universal destiny of goods and the priority of labour over capital⁸.

There are important signs of hope in this regard. For instance, a new generation of value-based investors is arising in every part of the world; people who are willing to align their financial choices with their personal beliefs. Indeed, separating one's moral values from one's financial choices leads to living a divided life. This parallels the technocratic ideology which makes technology absolute and thus minimizes the value of the concrete human individual by reducing choices to merely technical or financial variables⁹. Only the reintegration of moral values in financial investments will avoid the risk of living a divided life and, hence, bring to all financial actors the peace to which they aspire as human beings¹⁰.

Today the awareness of the huge impact of finance on the real economy, of its social and environmental impact, is growing rapidly. From the beginning of his Pontificate, Pope Francis is tireless in calling for a financial system that is inclusive, that cares for the environment and takes seriously our responsibility to future generations. In response to Pope Francis' invitation, the Pontifical Council for Justice and Peace has organized – in collaboration with Catholic Relief Services (CRS) – two Conference on the topic of impact investing. These two gatherings demonstrated how impact investing can be consistent with Catholic Social Teaching, how individual and institutional investors are working to align the deployment of their assets to support positive social and environmental impacts. In the case of impact investing priority is not given to profit – financial returns are usually smaller than those of traditional investments – but rather to pursuing the common good by making a difference for the environment and the poor.

One way to generate a positive social and environmental impact on the lives of individuals, their families and the community, could be that of investing in businesses with a social purpose – in Italian the so called “imprese sociali” – which, without rejecting profit, aim at a higher goal than the mere logic of the exchange of equivalents,

7. Cfr. Cardinal Peter Kodwo Appiah Turkson, “Sustainable Finance and Care in the light of *Laudato Si'*”, 15 aprile 2016.

8. Cfr. Pontifical Council for Justice and Peace, “A new International Financial Pact”, November 2008.

9. Cfr. Pontifical Council for Justice and Peace, “Towards reforming the international financial and monetary systems in the context of a global public authority”, 2011.

10. Cardinal Peter Kodwo Appiah Turkson, “Sustainable Finance and Care in the light of *Laudato Si'*”, 15 aprile 2016.

of profit as an end in itself¹¹. In the month of November 2016, as previously already mentioned, the Pontifical Council for Justice and Peace organized, in collaboration, with the International Christian Union of the Business Executives (UNIAPAC) an International Conferences titled “Business Leaders, as agents of economic and social inclusion”, in which several successful business experience aimed to overcome social exclusion and directed to support integral human development were presented. I would like to recall just one case in this occasion: a company dedicated to hiring and providing work to people with disabilities which became in the long term a major company in the US market, not despite disabled people, but precisely thanks to disabled people hiring. Indeed, disabled people stay much more loyal to their professional commitment and are rarely absent from the workplace, and their presence creates a better and more virtuous environment of work as well as had a deep and remarkable impact on culture. People around them started to think at the company’s system as a community looking at the other as a person to get to know better, appreciate and to respect¹².

Furthermore, we are seeing today also an increase of investments in businesses focused on decarbonisation for the reduction of climate change. *Laudato Si’* has increased people’s understanding that an economy founded on fossil fuels is unsustainable because of its destructive impact, not only on the environment but especially on the most vulnerable people, in opposition to the idea of infinite or unlimited growth, a dominant idea in economics and finance “based on the lie that there is an infinite supply of the earth’s goods”.

CONCLUSION

The challenge we face today is the shift in the financial paradigm; it is that of rethinking our way of doing finance; it is that of enriching and – why not – changing our vision of finance. It is a matter of openness to different possibilities which do not involve stifling human creativity and its ideals of progress, but rather directing that energy along new channels! Indeed if we look at the larger picture, we can see that more diversified and innovative forms of investing, which impact less negatively on the society and on the environment, can prove profitable as well¹³.

The challenge we face is also that of humanizing – next to economics – also finance which must not rule, but serve the common good. This is a key principle that Pope Francis explained in his address to the participants in the 2016 International

11. Pope Benedict, Encyclical Letter “*Caritas In Veritate*”, n. 38.

12. Cfr. Randy Lewis, Walgreens former senior Vice-President, International Conference, “Business Leaders as agents of economic and social inclusion”, 16-17 November 2016.

13. Cfr. Pope Francis, “Encyclical Letter *Laudato Si’*”, June 2015, n. 129.

Conference of the Christian Union of the Business Executives (UNIAPAC). He stated: “money must serve, not rule. Money is only a technical instrument of intermediation, of comparison of values and rights, of the fulfilment of duties and saving. Like any technical instrument, money does not have a neutral value, but acquires value based on the aims and circumstances in which it is used. When we claim that money is neutral, we fall under its power”.

Finally, the challenge we face is that of giving the ethical dimension of the economy and of finance not an incidental but an essential status. The economy – and by extension finance too – “needs ethics in order to function correctly – not any ethics whatsoever, but an ethics which is people-centred”¹⁴. “Insofar as they are instruments, the entire economy and finance, not just certain sectors, must be used in an ethical way so as to create suitable conditions for human development and for the development of peoples”.¹⁵

14. Cfr. Pope Benedict XVI, “Encyclical Letter *Caritas in Veritate*”, June 2009, n. 45.

15. Cfr. *ibid*, n.65.

**FINANCE FOR THE COMMON GOOD:
A DISASTER RISK REDUCTION PERSPECTIVE**

Robert Glasser*

It is interesting to look at this topic through the lens of disaster risk and how we manage it, and how they cope with them.

Nothing tells us more about social inclusion or the lack of it, in many parts of the world, than the percentage of the population regularly exposed to disaster events and how they cope with them.

We know that in terms of absolute economic losses, it is the rich developing world that pays the most. However, the poor pay an even higher price in terms of losing whatever shelter they might have, their livelihood and access to basic services such as health and education.

A Latin American politician, recalling his poverty-stricken childhood, described it in these few sentences: “When our house flooded, I sometimes woke up at midnight to find my feet in water, cockroaches and rats fighting over space, and various objects floating around the living room, so I had to get up in the middle of the night.

“Our biggest concern was preventing the furniture from getting ruined. Not that we had much to get ruined. Every time it rained, we used to nail another piece of wood across the doorframe, and dump another truckload of earth to reinforce the barricade. But every time it rained the water level rose further. And the authorities never did anything.”

He was describing an era which one hopes is long gone in most places when he said the authorities never did anything because today disaster management is something that most countries and local government authorities have had to learn.

And over the last twenty years there has been a concerted push to shift the focus from disaster management to disaster risk management, and this has come sharply into focus with the adoption of the Sendai Framework for Disaster Risk Reduction in March 2015 by all UN Member State. The Sendai Framework seeks a reduction in disaster mortality, numbers of disaster affected and economic losses.

What kind of numbers are we talking about here? Analysis of twenty years of data on over 7,000 disaster events from 1996 to 2015, in which 1.35 million people died, shows that earthquakes and tsunamis are the biggest killers overall followed closely by climate-related disasters. In an average year the lives of some 100 million people are disrupted by disasters.

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High income countries suffer huge economic losses in disasters but it is low income countries which suffer the most when it comes to loss of life. A 2016 estimate from the World Bank states that annual economic losses are running at US\$500 billion from just weather-related disasters which are estimated to push 23 million people into poverty every year.

“Where you live should not be a factor in how you die,” said the Secretary-General in a message for International Day for Disaster Reduction on October 13. He was referring to the fact that over 90% of all disaster deaths occur in low and middle-income countries.

The vast majority of climate-related deaths occur in low and middle-income countries which contribute least to greenhouse gas emissions. These countries also bear the brunt of earthquake deaths.

These mortality statistics have implications for the achievement of the Sustainable Development Goals. Disaster deaths are a strong indication for poverty and underdevelopment and 90% of disaster deaths happen in low and middle income countries.

It is clear that when impoverished countries like Haiti or Nepal lose huge chunks of their GDP to recurring disaster events that that eats away at funding available for social expenditure as they pay for recovery and rehabilitation.

So what are the solutions? How can we show solidarity and demonstrate corporate social responsibility when it comes to disaster risk management.

The richest 2% of the world’s adult population now own over 50% of global wealth, whereas the bottom 50% own less than 1% of global wealth. This stark income disparity can only lead to growing risk inequality across territories and social groups unless we make a conscious effort to correct it.

The private sector has a huge role to play in reducing existing levels of disaster risk and helping to avoid the creation of new risk. This can be done at a number of levels facilitated by the fact that some 80% of all investment decisions are made by the private sector.

Let’s look at a number of areas where the common good needs to take precedence over shareholder value, remembering that the most precious thing we have a share in, is this planet.

It is critically important that the business world gets behind implementation of the Paris Agreement on reducing greenhouse gas emissions and leads from the front. Keeping the rise in global warming at 2°C or below is to relieve the world of an existential threat.

Success depends on industry and commerce providing the technology and innovation which will move us towards a carbon free world where fossil fuels are left where they belong, in the ground.

Otherwise, the words in a famous tweet from your neighbour the Pope, will become more our every day reality than it already is. “The earth, our home, is beginning to look more and more like an immense pile of filth.”

The truth of this is nowhere more obvious than in another great driver of disaster risk, the destruction of the environment which is often motivated by short-term profit which translates into long-term loss for all of humanity.

Deforestation, desertification, pollution, acidification of the oceans, over-fishing are in nobody's long-term interests and the human activity which propels these phenomena needs to be stopped. The private sector needs to support a vision of consumerism which is responsible, sustainable and lasting.

One of the downsides of globalization is that the search for lower costs, higher productivity, and just-in-time delivery are driving business into hazard-prone locations where resilient infrastructure is often not a priority.

The temptation to cut corners and avoid the costs associated with resilient infrastructure must be avoided in a world which is embarking on one of the greatest building sprees in the history of the human race.

Over 60% of the land projected to become urban by 2030 has yet to be developed. Additionally, nearly one billion new housing units will need to be constructed to house the world's growing population by 2060.

It is essential to ensure that this is done in a risk-informed manner if we are to make significant progress on reducing disaster losses. A disaster-prone urban future must be avoided at all costs.

This means we must put greater effort into addressing the urbanization of disasters and disaster risk especially in low and middle income countries where endemic poverty leaves many especially vulnerable to disaster events.

One only has to look at the destruction wrought on cities and towns in Haiti, the poorest country in the western hemisphere, by the 2010 earthquake and the hurricane Matthew to realise how challenging this can be.

While cities are the drivers of economic development and social progress in most countries, accounting for more than 80% of global GDP, they are also home to many of the world's poor and vulnerable.

That is why urban resilience is such a critical element of the 2030 Development Agenda. If we are to eradicate poverty we must reduce urban risk to allow low-income communities to thrive and develop in an environment free from the threat of recurring floods and storms, and in earthquake-resistant housing where required.

This last point I am sure is one well understood by people here in Italy given the tragic loss of life you have suffered in recent years from earthquakes.

The arguments for the common good are also based on sound economics. Over the coming years, trillions of dollars will be invested into hazard-exposed regions. How and where these funds are placed will determine how much disaster risk is accumulated and whether underlying risks are addressed.

Markets have placed greater value on short-term returns than on sustainability and resilience. Reducing your investment's exposure to disaster risk is not a cost but an opportunity to make that investment more attractive in the long-term.

The continuous mispricing of risk is another area that needs to be addressed by the finance community. If the main metric for success is GDP growth, questions of solidarity and social inclusion take a back seat along with reducing disaster risk and accepting the need for regulation – for the common good – of potentially harmful, risk generating economic activity.

Our extensive research for the Global Assessment Reports on Disaster Risk Reduction has shown that risks, losses and impacts are often not borne by the risk takers but instead are transferred to other social sectors or territories.

A classic example would be speculative urban development that may increase flood risk for households in informal settlements in other parts of the city. Other risks are transferred to the whole of humanity because of climate change and the destruction of biodiversity.

There is no single magic number for benefit-cost ratios for investments in disaster risk reduction. What is beyond doubt is that DRR is a good investment strategy. Typical benefit-cost-ratios seem to lie in the range of 3 to 1 and 15 to 1, and the most quoted as an order of magnitude is four to one.

This reality has yet to sink in for many governments as we saw two years ago for example in Australia where the Australian Government's Productivity Commission published a report which found that Governments overinvest in post-disaster reconstruction and underinvest in mitigation that would limit the impact of natural disasters in the first place. As such, natural disaster costs have become a growing, unfunded liability for governments.

Even in a high income country like Australia, the rising cost of disasters can be explained by the rising exposure and vulnerability of communities to natural disasters. For example:

- the number of houses, businesses, infrastructure and other assets exposed to natural disasters has increased (partly in line with population growth)
- the value and size of assets at risk has increased
- an increasing number of people have settled in areas prone to natural disasters, such as along the coast and urban fringe.

Australia has the advantage of having a thriving well established insurance industry which is not the case in emerging economies across Latin America, Africa, and Asia which currently contribute 40% to global GDP, yet represent only 16% of global insurance premiums.

When a disaster strikes this level of underinsurance can reverse development gains and damage future growth. There is a huge gap between reported insured disaster losses and the reality.

Last year eight Lloyd's syndicates joined forces to develop new solutions to help developing economies tackle underinsurance and improve their resilience against the economic impact of natural catastrophes.

The eight Lloyd's syndicates have committed capacity of US\$400m towards solutions that address risks associated with natural hazards in emerging and developing economies. Key to its effective deployment will be well designed risk sharing initiatives and the diversification of risk.

This is further evidence that private companies and investors are starting to take disaster risk into account when deciding where to invest. This trend was accentuated after heavy business losses in 2011 after earthquake and tsunami in Japan and

the floods which hit the industrial heartland of northern Thailand.

More recently, UNISDR's Private Sector Alliance, ARISE, has worked with the Economist Intelligence Unit to add the threats posed by natural and human-induced hazards to its widely-respected country analyses.

The Economist Intelligence Unit is the world's leading provider of country intelligence, with its timely, reliable and impartial research offering governments, institutions and businesses the evidence base that they need to set strategy and make critical decisions.

These are just some examples of initiatives we are supporting to encourage new approaches to solidarity, inclusion and social responsibility which are themes which run throughout the Sendai Framework for Disaster Risk Reduction which identifies the private sector as a key stakeholder in achieving a safer world through risk informed decision making and investment decisions.

RESPONSIBLE AGRICULTURAL INVESTMENT AND THE UNITED NATIONS SUSTAINABLE DEVELOPMENT GOALS

Kostas Stamoulis*

Let me start by saying that so much of what is being discussed today is at the heart of the 2030 agenda and the Sustainable Development Goals (SDGs). Mobilizing and re-orienting private finance investment to achieve the transformational changes demanded by the SDGs is one of the preeminent challenges of our time.

I think we all agree on this. The question is how? How can we incentivize private action when so many of our objectives have the nature of public goods? How do we make growth more inclusive, reaching the very poorest of our societies? How can we guarantee a minimum social floor that begins with ending the scourge of hunger for everyone, everywhere? How can we transform food systems to make them “nutrition-driven”? How can we move whole economies from a high- to a low-carbon pathway? How can we bring our production and consumption of the necessities of life fully sustainable and consistent with the environments we want to live in?

These are not rhetorical questions – they are the question we have imposed on ourselves by adopting the 2030 Agenda for Sustainable development. These are questions we now have a duty to answer. And at FAO, these are questions we believe can be answered.

But to develop and implement workable solutions, we need to think differently. One the first steps is to enable the demanders and beneficiaries of change, to become more effective agents of change.

European ministers of labour met in Bratislava last year to look at the question of achieving the EU’s objectives of smart, sustainable and inclusive growth. At the heart of that discussion were the role of social enterprises as key actors in the provision of services of general interest to European citizens and, especially, to vulnerable persons. According to an EC Expert Group on Social Enterprises, these enterprises meet many social needs and contribute to the fight against exclusion and poverty. In Spain, for example, the social economy created more than 31,000 enterprises and 210,000 jobs in the 2008-2015 period. In the United Kingdom for instance, 40 % of social enterprises were managed by women in 2015, compared to only 18 % in traditional SMEs.

For FAO, social enterprises– in the forms of small family farms, rural cooperatives, and farmers associations – have clear links to food security, poverty eradica-

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tion, women's economic empowerment, decent employment creation, social protection, adaptation to climate change and good governance.

Now, let me link this with the big picture – the SDG Zero Hunger vision of a “world free from hunger and malnutrition, where food and agriculture contribute to improving the living standards of all, especially the poorest, in an economically, socially and environmentally sustainable manner.”

To meet the challenge of zero hunger in 2030 – Sustainable Development Goal no 2 – agricultural production will have to increase significantly.

This means that much more investment in the agricultural sector and in food systems is needed.

Many studies show that investing in agriculture is one of the most efficient and effective ways to reduce hunger and poverty.

And FAO's own research has demonstrated that the largest and most important investment in agriculture comes from farmers themselves.

In essence, if we want to transform food and agriculture systems, we need to begin by creating incentives for farmers themselves to begin producing more and better food, and to do so in ways that are sustainable and resilient, and that maximize the contribution of agriculture to climate change mitigation.

To achieve this, especially where farming is a low-productivity activity, and where people who grow food are consequently both poor and food insecure, we need to think in new ways.

Analysis of country experiences shows that relatively small investments in social protection can be a truly powerful mechanism for inducing farmers' own investment in production and productivity.

Contrary to popular myths, we have found, small farmers do not consume or waste social protection money. Instead, they use it to experiment with new techniques and seeds, and, over time, to acquire productive assets – land and equipment – that help them to escape poverty.

We have also found that this approach, when combined with other supports for farmers, can be quite cost effective.

The Rome-based UN agencies estimate that to eradicate hunger and poverty sustainably by 2030, the additional public investments required are – on the order of USD 265 billion per year over the period 2016-2030.

The vast majority of these funds will be paid by large middle-income countries out of their own tax receipts; the amount of money that will be required for the very poorest countries is only a few percent of the total.

Over time, however, this public investment will trigger many multiples in private investment, led by the farmers themselves.

In the case of the European region, the overall financing needs are high, but if we break down the balance of public and private investment, we see a different picture.

We see that small, targeted public investments can unlock very large significant cascades of downstream investment.

To increase productivity, investments are required not just at the farm level, but

also in market infrastructure and processing and distribution activities that connect producers and consumers.

The growth of on-farm investment creates a need, and hence also an opportunity, for large-scale off-farm investment in storage and transport, in infrastructure, in market development, in food quality and safety assurance.

Making food systems nutrition-driven and fully sustainable and climate compatible needs to be seen for the investment driver that it is. Governments can set standards that drive investment in all the systems needed to transform food and agriculture.

This investment should focus not only on technological innovation, but also in the engineering of innovative business models seeking to enhance the efficiency and stability of agricultural value chains.

In the case of many developing countries, the share of the market captured by local agribusiness actors is growing faster than the one captured by international investors in agriculture.

The proportion of medium and small agribusiness actors along value chains in national and local agricultural markets tends to be high and the local agricultural markets they participate in are less understood given large degree of informality.

However, the aggregate statistics in the performance of agricultural markets suggests these markets are expanding rapidly and have been a strong motivator for business model innovations that enable finance and investment in the sector.

Although the coverage of financial services in rural areas by formal financial institutions improved between 2011 and 2014, the percentage of the rural population that obtains financial services from informal actors has grown much more rapidly within the same period.

It is possible to infer from existing data that the informal financial service providers that are beginning to dominate rural financial markets possess significant informational advantages that allow them to identify client needs and viable investment opportunities, and to deliver financial services in a feasible manner in rural areas.

They also assess and manage the risks associated with providing such services more accurately than their formal counterparts.

As most investments already come from the private sector, the role of Governments should focus on fostering an enabling environment for responsible private investments, both on- and off-farm.

Efforts by governments and development partners should reduce the constraints that farmers and other value chain actors face and stimulate their investments. Investments with strong multipliers that raise the yields and productivity of farmers, such as investments in agricultural research, development, training and extension, should be prioritized. This will contribute to the twin goals of reducing hunger and poverty in rural areas.

Government investment in essential public goods and services should include productivity-enhancing research and development, science and innovation systems, institution building, legal framework, advisory services, rural transport, health, education and social protection. They represent a fundamental part of the enabling environment. To stimulate private investments, governments need to secure proper-

ty and tenure rights, and develop robust well-governed, public-private partnerships for rural infrastructure and public services, adapting and strengthening existing institutions for the new policy environment.

To help countries enhance the quality of agricultural investment, FAO has supported the development of guidance tools, in particular the Principles for Responsible Investment in Agriculture and Food Systems (CFS-RAI) negotiated by the Committee on World Food Security (CFS) in 2014.

These voluntary principles benefit from widespread support, as they were developed through a broad consultation process that included representatives from governments, private sector and civil society organizations. FAO is now launching an Umbrella Programme to translate these general principles into action at national level.

We look forward to collaborating with Italy's financial sector for its implementation.

CONSTRUCTING ALTERNATIVES TO PROMOTE HUMAN DIGNITY THROUGH ECONOMIC AND SOCIAL POLICY¹

Domingo Sugranyes Bickel*

INTRODUCTION

When confronted with appeals for solidarity and inclusion, business normally refers to the well-known policies of corporate social responsibility (CSR). The generally accepted approach to CSR appears in several indexes and sets of guidelines for company codes of conduct. And still, CSR policies are far from having conquered a central position in financial and business decisions. True, many companies have developed their own codes of conduct or adhered to existing sets of principles; investors pay more and more attention to CSR performance of listed companies; consumers, even if slower in adopting new criteria, also start paying attention to producers' records regarding the environment, local working conditions in producing countries, child work and so on. Companies also use from time to time their own CSR performance as a marketing argument. But this change in decision criteria and perceptions of business policies, though started more than 40 years ago, is still in the making.

In the meantime, profound changes are affecting the context: digitization is changing work, perceptions and culture. The future of employment as we know it is being questioned. The stakeholders concept, which was the base for CSR, needs to be revised as deep changes are affecting the roles of some of them. Consumers are becoming directly involved in designing and production in electronic products and services: the blurring of roles of consumers and producers translates in a new category of *prosumers*. Shareholders' rights and shareholder value are frequently invoked, but management power has in fact overcome that of shareholders in public companies: shareholders' decisions follow exclusively short term or long term investment criteria – the investors often are pension funds and insurance companies – while strategic business decisions rely totally on management. These examples show how the problems which any 'social responsibility' approach needs to focus on now may be different from those of the decades previous to 2008.

The Centesimus Annus pro Pontifice Foundation, a Vatican-based, lay-led think tank on applied Catholic Social Thought, tries to understand and to translate the principles of a human-centred economy contained in the Popes' encyclicals since 1891

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1. This contribution draws on the 2017 statement of the CAPPF (The Vatican, March 2017).

in the context of real actual economic life. The following document contains the essential lines of our work and some of the conclusions we propose as new approaches to solidarity, inclusion and social responsibility.

THE POPE'S BRIEF

In his address of May 13th, 2016, Pope Francis asked the Centesimus Annus pro Pontifice (CAPP) Foundation² to “contribute to generating new models of economic progress more clearly directed to the universal common good, inclusion and integral development, the creation of labour and investment in human resources”.

Translating these aims into practice requires changes in economic behaviour and personal commitment at various levels, from political institutions to business management, to workers and consumers. Such changes question underlying attitudes, as the Church consistently does in Catholic Social Thought, namely the prevailing utilitarian, positivistic, or emotive versions of ethics or, at another level, the idea of ‘shareholder value’ as a sufficient goal to ensure on its own that the economy will work for the common good. Questioning moral attitudes is ever more urgent in the context of a digital economy, which offers new possibilities for inclusion but also poses new ethical challenges. As the Popes tirelessly repeat for more than 125 years, the dignity of all human persons must be the true compass in this search. And the message can be understood and shared by Christians and non-Christians alike.

The Centesimus Annus pro Pontifice Foundation addresses people who are active in economic life. Within our brief, it is useful to contrast moral exhortations with the analysis made by academic experts and with the experience of professionals, thereby contributing a dimension of feasibility to the search for alternative models.

In the last two years, the Foundation has focused its work on three main themes. All of them offer possibilities to focus on constructive alternatives:

- Business initiative in the Fight against Poverty
- A Digital Economy at the Service of the Common Good
- New alliances in the search for Inclusive Economic Reforms.

2. The Centesimus Annus pro Pontifice Foundation is a Vatican based, lay-led platform on Catholic social teaching applied to social and economic life. This statement is based on the Foundation's recent activities and was approved by its Board on March 3, 2017. More details on www.centesimusannus.org.

1. *Business initiative in the fight against poverty*³

“To enable these real men and women to escape from extreme poverty, we must allow them to be dignified agents of their own destiny. Integral human development and the full exercise of human dignity cannot be imposed. They must be built up and allowed to unfold”.⁴

Economic growth and a market embedded in institutions and social relations are the only contexts in which poverty has been effectively reduced in large numbers. But this is not enough: there are permanent demands of human development which economic growth does not solve by itself.⁵ We need better measurement and better understanding of poverty. A process of human and participative development is best served by autonomous and responsible entrepreneurial initiative.

- Poverty is not adequately measured by income figures. The experts are the poor themselves, and what is measured should match their experience of multidimensional, overlapping deprivations. The CAPP Foundation wishes to support research and recognition of new methodologies like, for example, the Fordham Francis Index (FFI) developed by Fordham University’s International Political Economy and Development Program. This is based on the Holy Father’s priorities and includes seven easily accessible indicators: water, food, housing, employment, education, gender equity and religious freedom.
 - The real alternative to bureaucratic utilitarian approaches is a person-based path, internally fostered by entrepreneurship, and effectively helped from outside. The aim should be to promote small- and medium-sized enterprises, which are the bone of developed economies. In this process, profit is not to be considered an evil in relation to poverty reduction. Poor people are poor because they are excluded from networks of productivity and exchange. Small business owners should be supported on the way to reach critical mass; credit and government policies should aim at this wealth-creating process, not just at mitigating poverty.
 - Business in general is responding to ethical responsibility towards the poor through philanthropy projects, and this is both positive and necessary for certain activities, which need ongoing subsidies. But more creatively, a growing number of companies and financial institutions are using their own business models to contribute to poverty reduction as well, particularly for the promotion of entrepreneurship, small business development, affordable housing and the support of women’s groups. Good practice of this kind must be known and extended.
3. From debates held at the Vatican CAPP international conference, Vatican, May 2016 and at the CAPP-USA/Fordham University conference, New York City, September 2016.
 4. Pope Francis, “Meeting with the Members of the General Assembly of the United Nations Organization”, 25 September 2015.
 5. Centesimus Annus pro Pontifice Foundation, 2015 Statement, “A Reformed Market Economy: Entrepreneurship for Human Development”.

- There are possible ways to share risk by working together across corporations and banks in development impact investment projects designed in dialogue with the parties involved. In the light of the social teaching of the Church, there is need for ‘goodwill brokers’, mediators rather than intermediaries⁶, who can bring together corporations and banks with local initiatives and development groups. Church members can lend institutional strength, credibility, knowledge and unbiased generosity to these contacts.
- The refugee crisis and the fight against human trafficking requires specific action. But the long-term objective should be, as indicated by Pope Francis, “to defend each person’s right to live with dignity, first and foremost by exercising the right not to emigrate and to contribute to the development of one’s country of origin”.⁷
- Income inequality, even in developed countries, implies threatening vulnerability for many persons and families. To help people helping themselves and avoid falling back into poverty, we need to foster new sharing initiatives involving a larger number of people, especially within the Church. This is the idea behind the Voluntary Solidarity Fund network, which is being set up as a follow-up to debates held in several CAPP Foundation instances.

2. *Work and wages in developed economies: digital technology, fear of job loss and education*⁸

“Work should be the setting for this rich personal growth, where many aspects of life enter into play: creativity, planning for the future, developing our talents, living out our values, relating to others, giving glory to God. It follows that, in the reality of today’s global society, it is essential that we continue to prioritize the goal of access to steady employment for everyone, no matter the limited interests of business and dubious economic reasoning”.⁹

Decent work is a vital part of human development. Nowadays, industry, commerce and financial activities as well as public institutions face deep challenges and opportunities in the context of digitization and ‘big data’. These transformative innovations offer great potential for inclusive finance and economic development, but they also pose challenges about the future of jobs. And they raise a range of new ethical questions relating to truth in communication, extreme time pressure, uncertainties about the future of meaningful work, lack of interpersonal relations and the question of moral agency in machine driven self-learning processes. The strength and effects

6. Interview with Pope Francis, *El País*, January 22, 2017.

7. Message for the World Day of Migrants and Refugees 2016.

8. From debates at the CAPP/Civiltà Cattolica Italian conference, Rome, November 2016 and at CAPP/Universidad Pontificia Comillas/BBVA consultation, Madrid, January 2017.

9. “Laudato Si’”, 127.

of the underlying technology imperative are difficult to discern: technology is a means, but sometimes it is not easy to distinguish the ends it pursues. Church groups need to update their thinking on the legitimacy of the technology imperative and on the ethical issues typical of hyper-connectivity.

A full picture of the present digital revolution on jobs will not emerge until new technologies are standardized and consolidated. As ‘robots and computers are eating jobs’, we need a serene analysis about jobs disappearing and others emerging, taking history into account, and without cultivating utopian proposals of universal income and the ‘end of work’, which would undermine human dignity and freedom. We also need to identify the existing obstacles to change, whether legal, managerial or educational: lay-offs sometimes are not caused by technology, but are the consequence of changes in consumer behaviour or the price paid for past mismanagement. The Church has an important role to play in educating consumer choice. Digitization needs to be seen together with demographics and intergenerational tensions. There are also some positive signs of a new work mentality, still the fact of a small minority, where flexibility is seen as an opportunity for autonomous and meaningful community-oriented activities.

- The public sector, both as regulator and as sponsor of many technical developments, has a role to play in influencing the direction and the pace of technical change so as to minimize its negative effects on employment and working conditions. The debate in the field of education, social safety nets, public and private policies in the digital era also requires a new start in the dialogue among employers and workers. Catholic Social Thought could offer a platform for such free and constructive dialogue among social partners.
- We support transparent, co-operative use of ‘big data’ technology for common good purposes: for instance for inclusive finance, better sectorial risk management, protection against natural catastrophes, well-functioning job markets, international business relationship developments.
- Education policies need to revalue the prestige of professional vocational training. Financial support should go to practical educational institutions. Corresponding bridging possibilities towards university should be available for those academically most gifted.
- Permanent education of workers is an essential business responsibility as a way to allow a balance between flexibility and security.
- Portability of welfare rights and the principle of contribution are essential to continue shifting protection from jobs towards the working person.
- Managers and workers should join efforts to monitor the digital environment in a way that promotes knowledge and a sense of purpose.
- New ways of combining public and private initiative are necessary to address the possibilities of the unemployed (young and old) to find employment. Personal care activities need to be re-valued and better paid.

3. *New Alliances For Change*¹⁰

“I urgently appeal, then, for a new dialogue about how we are shaping the future of our planet. We need a conversation that includes everyone, since the environment challenge we are undergoing, and its human roots, concern and affect us all”.¹¹

The Holy See exercises through its teaching and through diplomatic action a permanent role as world-wide moral authority. For instance, on the question of “populations and entire regions being displaced, trying to flee from war, from persecution, from exploitation and poverty, (...) the Holy See will continue to encourage Governments to overcome every form of narrow nationalism and, above all, to recognise the unity of the human race. (...) Migrants are men and women who enjoy the same universal rights, above all the right to life and to dignity. It is the task of all civil societies, including the commercial sector of those societies, to accompany this action and to engage actively in welcoming and integrating migrants and refugees”.¹²

The message is being addressed not only to members of the Catholic Church. Its effectiveness depends on believers and non-believers, Christians or otherwise, to join forces on a common basic program which is essential for sustainability of our planet and for a reasonable pursuit of dignity for all. We need to leave aside the old, often sclerotic established ways and promote possibilities for new alliances based on shared responsibility and shared interest. This requires new ethical conversations: “We are challenged to be people of depth, attentive to what is happening around us and spiritually alert. To dialogue means to believe that the ‘other’ has something worthwhile to say”.¹³

To foster new alliances for change translates into two immediate practical guidelines:

- For a useful dialogue, we need to be capable of arguing convincingly against moral ills in a way which is neither exclusive nor relativistic. For this purpose, as Christian lay people we should commit more time and effort to self-education and training, abandoning a passive attitude as Church members and being able to sustain mature, constructive debate on moral issues with all people of good will.
- Business corporate policies and our public engagements should include listening to the poor and including their aims as fully legitimate criteria.

10. From CAPP international conference, Vatican, May 2016.

11. “Laudato Si’”, 14.

12. Archbishop Paul Gallagher, Secretary for Relations with States, Address to the CAPP Foundation conference on 14 May, 2016.

13. Pope Francis, World Communications Day Message, 2014.

THE WAY FORWARD

The CAPP Foundation will continue to debate practical and realistic ways of applying the Pope's teachings, in the search for constructive alternatives to promote human dignity. It will do it through the analysis and understanding of new social facts, and with an eye to current international challenges. CAPP members are expected to help elaborate and disseminate its findings and translate them into action within their circle of contacts and within their possibilities.

In the present turbulent political environment, with far-right and far-left movements seeming to gain traction while a majority appears to be disillusioned with politics, people who wish to reconcile their Christian faith with their social and political commitment need to abandon prejudice and open up for dialogue in what Pope Francis calls *the culture of encounter*.

Participating in a group like the CAPP Foundation means adhering to a new humanism, oriented to the present and future, with the aim to integrate, to dialogue and to produce creative new answers.

THE IMPORTANCE OF PARTNERSHIP FOR THE PERFORMANCE OF A SUSTAINABLE FINANCIAL SYSTEM

Davide Dal Maso*

The 17th Sustainable Development Goal (SDG) recalls the importance of partnerships for the achievement of the Goals themselves. Maybe because it is the last one, its importance is often overlooked or taken for granted. But partnership is in fact a key element to deliver sustainability: most if not all SDGs can hardly be achieved by either institutional, economic or social actors alone, but require strong cooperation amongst all of them, at both local and global level.

This is the first reason why the Italian National Dialogue on Sustainable Finance (NDSF) is a good example of how an effective process can generate positive effects that go beyond its immediate outputs. Convened by the Italian Ministry of Environment (MATTM), the dialogue was launched in February 2016. At that moment in time, a group of pioneering countries from China to France and the UK had launched a range of initiatives to boost flows of private capital for climate and sustainability. The G20 had also just set up its ‘green finance study group’, bringing together finance ministries and central banks to work out how to scale up private capital flows to green investments. And the Financial Stability Board had made its first foray into the sustainability arena with its Task Force on Financially-related Climate Disclosures.

What was striking about the dialogue was the way in which key players in Italy’s financial community took responsibility for identifying the way forward. Representatives from leading banks, investors and insurers as well as the stock exchange, regulators and foundations did not just review experience to date, but also pinpointed practical options that could make a real difference in Italy’s specific circumstances.

Along with other countries, Italy has seen a growing commitment by financial institutions to international initiatives such as the Principles for Responsible Investment and the Principles for Sustainable Insurance. Italy was one of the first developed countries to introduce a disclosure obligation for pension funds on how environmental, social and governance (ESG) concerns are integrated into their investment policies. Italy’s Sustainable and Responsible Investment (SRI) assets under management now account for 6% of Europe’s total. Among G7 stock exchanges, Borsa Italiana has the highest proportion of green revenues from the listed companies on its exchange and

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has just opened a new segment on its ExtraMOT PRO market dedicated to the issuance of green and social bonds.

The core of Italy's financial system remains bank-centric and focused on serving an economy dominated by nearly 4 million small and medium-sized enterprises (SMEs). Here, the challenge is one of improving access to tailored financial services both for SMEs wishing to improve their sustainability performance as well as those seeking to provide goods and services for the growing green economy.

Another reality is Italy's vulnerability to natural hazards, ranging from earthquakes to floods. The onset of climate change can exacerbate the natural fragility of the country bringing potentially far-reaching consequences for the economy and the financial system. Banca d'Italia has found that over 15% of households and 18% of local businesses are exposed to flooding risk, and that most are uninsured. Positively, early findings from Banca d'Italia's analysis suggests that a reduction in flooding risk is associated with an increase in outstanding loans to SMEs.

Harnessing the financial system is essential for achieving a successful transition to a low-carbon, inclusive and sustainable model of development. Sustainable finance involves the integration of environmental, social and governance (ESG) factors across the financial system with the goal of strengthening resilience, targeting capital allocation and improving accountability. The dialogue focused mainly on the environmental dimension of financing sustainable development, often called 'green finance'. Green finance aims not only to guarantee finance for needed environmental projects but also to make more sustainable all finance ("greener finance"). The dialogue clearly demonstrated that a shift is already under way both domestically and globally. There is growing recognition that ESG factors are now material for value creation. Environmental threats such as climate change and water scarcity are creating risks to financial assets – and new challenges particularly for the insurance sector. Banks, capital markets and institutional investors are starting to incorporate environmental and social factors in capital allocation decisions. Public finance will be key to enabling this shift, but the bulk of the capital required will need to come from the private sector.

In the end, the dialogue involved well over 100 participants from across the financial system.

The seven working groups (Banks, Insurances, Asset management, Capital markets, Risk, Governance & Disclosure, Measurement of progress) were led by market leaders and supported by the secretariat provided by MATTM and Unep (the United Nations Environment Programme). Its results were launched in Rome in February 2017, symbolically in the Headquarters of the central bank, in the presence of Governor Visco, the Environment minister Galletti and the Finance minister Padoan. The dialogue's report pointed to four broad areas where action could be taken. The first was improving the national policy framework to support green finance, for example through the country's forthcoming Strategy for Sustainable Development. The second area was focusing financial innovation on critical priorities, for example, the untapped energy efficiency opportunity. A third priority was to strengthen disclo-

sure and governance standards (including by investors to their clients). And the fourth priority was to boost awareness and capacity on sustainability among both financial consumers and financial professionals.

Clearly, this ambitious agenda has to be seen as part of the wider programme of structural reform of the economy, that means reforming rules and incentives so that actual financial behaviour is changed and concrete results can be achieved.

Besides the intrinsic value of the policy options identified in the final report, one of the unattended outcomes of the Dialogue is the creation of a cooperative network of private and public actors that, while pursuing their interests, did their best to find proposals and solutions that actually respond to the real needs of the economy and the society. All of them, aware that environmental and social challenges require for everyone's contribution, have put their competences and skills at disposal of the group, in a spirit of service for the Country.

In order not to lose the momentum, the Italian financial community is now called to mobilise and accelerate progress on climate and sustainable development goals. An open and inclusive platform should be established with the goal to monitor progress, to launch new projects and specific initiatives at sector level, to promote the Milan marketplace as a global leader in green finance, to enhancing the level of awareness of both the demand and the supply side, to stimulate product and process innovation, to contribute to the public debate at national and global level, to feed into policy frameworks.

Italy faces a strategic opportunity to align its financial system with sustainable development. Reforms to green the finance sector can help to identify new growth areas, new ways of ensuring the soundness of financial institutions and new ways to serve clients at home and abroad. This can contribute to wider financial stability and long-term economic recovery.

What is clear, however, is that green finance is no longer regarded as a constraint. Instead, it offers a way to restore credibility and trust.

THE ROLE OF THE EUROPEAN FINANCIAL INDUSTRY FOR THE FINANCING OF THE COMMONGOOD

Pier Virgilio Dastoli*

2015 and 2016 were key years reshaping the 'sustainability' path. 2017 will be the year to restart the European project.

The adoption of the Sustainable Development Goals, the Paris Climate Change Agreement, the Encyclical Letter "Laudato si'" and then the COP22 in Marrakech were three major milestones.

Brexit before and then the election of Donald Trump are marking the beginning of the end of the Anglo-Saxon leadership in place since World War. These events could give the chance for the European Union to regain its role as international actor.

What role for the European financial industry in such context?

In its Communication «Next steps for a sustainable European future, European action for sustainability» the Commission states: Sustainable development has since long been at the heart of the European project. The UN 2030 Agenda reflects for the first time an international consensus that peace, security, justice for all, and social inclusion are not only to be pursued on their own but that they reinforce each other.

In our view, the Sustainable Development Goals are defining the new 'economic and financial development' framework for a financial industry willing to lead at global and European levels and 'Invest for the Common Good' so that 'no one is left behind'.

The European Movement in Italy – together with EPE – European Partners for Environment and CSF – Centro Studi sul Federalismo – organised on 14 –15 April 2016 with Value Based Investors a Conference in Rome on how to mobilize public and private capital in support of the Sustainable Development Goals.

The meeting addressed in particular "Sustainable Finance and Care in the Light of Laudato si'".

This meeting with value based investors and representatives of the Catholic, Orthodox and Protestant Churches addressed what should be the roadmap of Long Term Investors aiming to contribute to the Common Good.

As underlined by Cardinal Turkson in his speech introducing the Conference, "the 'true' nature of finance consists in favouring the use of surplus resources to promo-

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te the real economy, which means the well-being and development of the whole person and of all people".

Our initiative aimed to contribute to develop a "reset action plan" by the "transformative cooperation" of value-based investors, workers, civil society organisations, faith groups and public authorities.

As European Movement in Italy we are engaged in two main projects.

The first one (LADDER) is about development education and awareness raising as a process for a change of attitudes within local Authorities and civil society working at local level, understood as multipliers. We will meet in Sardegna in July 2017 with all our Mediterranean Partners in the framework of the ENPI CBC programme..

The second one is in the follow-up of our conference in Rome.

We will meet again the 8th and the 9th, September 2017 for a second Conference In Rome on valued based investors. This Conference will be opened again by Cardinal Turkson as President of Pontificia Congregazione Giustizia e Pace.

Will 2017 be the time for a metamorphosis of Europe to face the challenges of the 21st century inside and outside Europe, a 'Transformed EU' to be called after the 60th anniversary of the Treaties of Rome ??

In view of this challenges , the European Movement in Italy, France and Spain have taken the lead of a large network of civil society associations united in a common awareness about the state of the Union and the need of a citizens' initiatives until the European election in 2019.

The European Union risks disintegration due to serious errors of political and economic strategy, to the inadequacy of its institutions and the lack of democracy.

Walls have been rebuilt with the bricks of national egoisms, and they are stifling the idea of a Europe establishing the right of citizens to free movement.

In the last ten years, austerity has blocked the investments in the real economy, exacerbating inequalities, creating uncertainty and precariousness, and dismantling the European social model.

Europe has to be the land of rights, welfare, culture, and innovation. Europe should have learned the values of peace, hospitality, equality, and coexistence from the best part of its history and from its tragedies.

The European Union must face the grand challenges of our times restoring the hope in the well-being of the whole community, assuring common good, the strength of rights and solidarity.

The European Union must reject wars and pursue the respect of rights and human dignity; ensure the reception of those asking for refuge, the freedom to migrate and the right not to migrate by engaging in solving those global problems that are at the origin of many migratory flows such as wars, hunger and natural disasters; equip with an effective plan for cooperation and development and with a Mediterranean policy for peace, democracy, and equality

It is fundamental to restore the meaning of politics, in order to eliminate inequalities by stopping austerity policies; to provide the European budget with its own resources in order to finance a great plan to support a New Deal capable to create employment in a low carbon economy, to sustain the circular economy, and a new produc-

tive and sustainable model to win the fight against climate change; to create social and territorial cohesion, contrasting poverty by investing in costs, in rural and internal areas and governing the economic dynamics triggered by new technologies.

It is urgent to reduce the generational and gender divides by fighting youth and female unemployment; to promote active participation and citizenship also through a European Civil Service, education and training; to set the bases for a European welfare system to guarantee social inclusion and raise the standards of protection for the most vulnerable and less advantaged groups; to defend and valorize the cultural and natural heritage.

In this regard the role of Value Based Investors, supporting the implementation of the SDGs, cannot be overestimated.

This is why we are calling to join champions of the sustainability agenda to elaborate a 'new narrative for the EU' based on the 2030 UN agenda and to establish their own scenario for the future of Europe..

Financing the greening of the economy and the management of new risks are, on the agenda of the G7 to be hosted in May 26-27 by Italy in Taormina, the G7 of the Environmental Ministers in Bologna to be hosted in June and the G20 to be hosted in July 7-8 by Germany in Hamburg.

European Union has to maintain and develop its engagements for the Sustainable Development Goals and to push the International organizations and its partners to adopt the same approach.

Which new steps?

In our opinion, in the present geo-political turmoil, it's the time for a new EU Alliance with our Neighbors from Russia to Morocco to lead the implementation of the Sustainable Development Goals and the Paris/Marrakech Climate Change Agreements.

In both fields, the financial industry has a key role to play. We need leaders of the Financial Industry to partner with other European leaders of the Sustainability agenda to explore these two major steps which would demonstrate that – in the present global turmoil – Europe is back and, thanks to a partnership between State actors and non-State European actors, has engaged a transformation for a "good life for all" in Europe and in the world.

We very much hope that the European Champions of the Financial Industry committed to contribute to the implementation of the SDG's and Climate Change Agreement will join us.

The 8th of September 2017 event in Rome will offer the opportunity to present a new EU narrative and strategic vision where the universal SDGs are for the European Citizens programmatic rights and a lever for new forms of cooperation with our neighbors as well as with ACP and Asian Partners. For the Europeans, it is the opportunity to build a new software for a 'transformative cooperation' intended to better manage our interdependence between Europeans and between Europeans and our neighbors and their neighbors, on a planet facing profound changes.

We need a tremendous amount of social long-term investments on a large scale for an unprecedented number of human beings and in a very different perspective from the one that has dominated the financial agenda till recently.

Financing the transition demands some drastic changes in financial rules and generally in the European and international governance, aimed at providing concrete incentives to redirect public and private capital towards the real needs of humankind.

Broadening and sharing a vision on finance for sustainable development and through innovative multi-stakeholders partnerships is vital.

You rightly raised the questions of which are our priorities in order to mobilize more financial means for inclusive investment and to bring it to critical mass and success.

What kind of investment do you envisage? Who is going to move it: Banks and financial institutions? European institutions? Associations? New alliances? Public-private joint action?

The UN, the OECD, the EU have announced the launch of platforms for scaling up innovative finance solutions to support the achievement of the Sustainable Development Goals.

The Rome April 2016 Conference suggested that, in addition, there is a need to set up a 'Capital Stewardship and SDG's' Platform' to register 'commitments' of non-state actors (financial institutions, regions and cities, companies and foundations, workers organizations and the immense crowd of individuals) to mobilize private capital and foreign direct investments to reach the whole UN 2030 goals. This platform could be a place for dialogue.

Such 'Capital Stewardship and SDG's' Platform' could be launched at the EU or Member State level as well as at the Euro-Mediterranean level.

We don't expect that this will be decided by the EU itself soon. This is why we are encouraging Banks and financial institutions to partner with representatives of the Business sector as well as presidents of European Regions and Civil Society and launch together such 'Capital Stewardship and SDG's' Platform' which should indeed be the testimony that European Champions of the 2030 Agenda implementation are building new alliances and Public-private joint action. Such Platform should contribute to accelerate the global transition towards an inclusive, low carbon, resource efficient, just economy, basic condition for 'ensuring that no one is left behind' and to meet the SDG's by 2030.

These 'Capital Stewardship and SDG's' Platform' would work in synergy with the Non State Actor Zone for Climate Action (NAZCA) platform already launched in support to the climate change agenda and which should continue to be used by institutional investors.

Let us build a vision for our citizens of a European financial industry leading in "Investing for the Common Good".

TOWARDS A MORE SUSTAINABLE FINANCE: THE ROLE OF RESPONSIBLE INVESTMENT

Flavia Micilotta*

When it comes to sustainable finance, Sustainable and Responsible Investment (SRI) is an integral part of the equation. SRI is a long-term oriented investment approach which integrates ESG factors into the research, analysis and selection process of securities within an investment portfolio. It combines fundamental analysis and engagement with an evaluation of these ESG factors to better capture long-term returns for investors, and to benefit society by influencing the behaviour of companies. To this end, Eurosif strives to promote SRI as a key part of policy-making and raise awareness throughout Europe of more responsible investment practices.

Today, SRI has come to the fore of strategic investments and is increasingly recognised as that part of finance which can help make a difference beyond returns. It can contribute to solving some of the more pressing issues, which are so much part of the international debate about more sustainable economies and more resilient businesses in the context of a general increased awareness of climate change and its impact.

Junker's Capital Market Union plan recognises the importance of including long-term and sustainable investment as a key requirement for Europe to maintain its competitiveness while shifting to a low-carbon and resource-efficient economy. Important regulatory initiatives have included the European Long Term Investment Fund (ELTIF) Regulation and the significance of ESG has been deemed crucial in adding value to the efficiency of financial markets with a view to increased transparency and a better risk assessment. It is safe to say that the Commission is working in favour of the sustainable investment community. This much is clear from the interest in long-term and sustainable investments expressed through consultations, its work on the upcoming guidelines on non-financial disclosure, the revision of the shareholder rights directive and the decision to include ESG consideration as part of the European pension directive, better known as IORPs.

In the ambition to be the EU reference point for SRI, with the renewal of its strategy and mission, Eurosif has tried to bring further clarity to the SRI industry, in light of the on-going debate on definition. To encourage not more but better EU regulation, Eurosif and its members produce research and bring forward examples of what

* Executive Director, Eurosif.

truly works when it comes to integrating the principles of sustainability in finance.

Thanks to the European SRI Market Study, we accomplish another one of our missions, focused on providing research and analysis on the development and trends within the SRI market across Europe.

This year's Study puts the emphasis on the strong relation between SRI and policy developments. Today, several practitioners apply at least some form of extra-financial evaluation in their portfolio, though this is not sufficient to fall under an SRI denomination or to meet the requirements of one specific strategy. The fact that there are no set parameters indicating what constitutes an SRI product leaves ample room for creating products which reflect the specific needs of clients, legislative requirements at country level, specific themes or trends. Regardless of the fact that there is currently no specific regulation in place, practitioners closely follow the developments on the policy side at a national level. The Article 173 of the French Energy Transition Law clearly shows how legislation at a country level can be a game changer for the industry. It also shows the strategic relevance of strong legislation at national level and the influence this can have on European dynamics.

Some key highlights of this year's SRI Study:

- Exclusions are still the most dominant SRI approach in Europe, with over €10 trillion of assets under management, showing a 48% increase in the past two years. This is in line with a wave of divestments, fuelled by the climate change debate and supported by so many players today.
- Norms-based screening remains a popular strategy, becoming the second most significant SRI approach with over €5 trillion in Assets under Management and a growth rate of 40%.
- The increased relevance of stewardship within Engagement & Voting and the ever more present debate around fiduciary duty have given further impetus to the strategy which grew by 30% since the last review. The significant policy drive for this approach is reflected in the debate around the Shareholder Rights Directive (SRD), as part of the Commission's action plan to modernise corporate governance and increase corporate transparency. The aim of this directive is to increase the shareholder's ability to demonstrate further accountability and engagement – both key characteristics of SRI.
- Sustainability Themed Investment grew by 145 percent. There are a variety of themes that comprise this strategy, mostly preferred by investors who are keen to focus on one or more areas, typically with a close link to sustainability. COP21, the ratification of the Paris Agreement on climate change by the EU and the adoption of the SDGs by the international community – and which commit the EU member states to a universal agenda to deliver social, environmental, economic and governance sustainability – are just some of the events with international resonance that led to this growth. European sustainability themed assets have now grown to reach €145 billion.

Impact Investing has registered an astonishing growth of 385 percent in the last two years. As the fastest growing strategy, Impact Investing puts a clear emphasis on financial return, and could well represent the future face of SRI, in terms of making it mainstream. We're counting on European member states to continue supporting the potential of SRI by leading the way and we count on policy makers to continue to facilitate the debate and ease the investing process, allowing for the retail market to become more dominant and fulfil the promise delivered in the findings of our research.

MOBILISING FINANCE FOR THE INVESTMENT IN SOCIAL INFRASTRUCTURE

Jonathan Watson*

CONTEXT

Resilient and innovative social infrastructure is a foundation for creating vibrant communities that in turn leverages economic capital and social justice. How to secure financing that helps make social infrastructure work in this way does not have easy answers.

Social infrastructure is about tangible ‘in place’ assets (schools, health and social care, affordable housing, cultural centres) that are able to generate intangible benefits (e.g. ambient living for older people) and connected using community network assets (ICT as part of closer to home care and social networks, urban green and public transport). These need to happen in ways that do not isolate individual social groups, especially young people post school and older people post retirement. Unfortunately, there are too few public resources available to address the infrastructure gap especially in the EU. This is compounded by a degree of uncertainty among public authorities about whether, when and how private investment is the right path to take.

Good solutions will need, among other things, new thinking and approaches to private sector investing in social infrastructure and associated public service renewal. Putting into play some predictable pre-conditions are essential for generating investable and resilient social infrastructure projects that are to scale for long-term investing. In particular, credible evidence for appraisal by investors of financial returns and monetary and non-monetary social, economic and environmental benefits: a triple bottom line.

In this context, the priority is to rework how the public sector (public authorities, public services, third sector) mobilises finance for social infrastructure. This has three primary elements for answering why and how mobilisation can be better realised: prevention as a strategic principle for planning and investment; local capacity to absorb financial capital and; playing up the externalities of social infrastructure investment.

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PREVENTION AS A STRATEGIC PRINCIPLE FOR PLANNING AND INVESTMENT

Across Europe just now public systems are under pressure. The combination of demographic change, environmental change, migration pressures and downward pressure on current spending is creating a gap between demand growth and capacity to meet it using current public sector models. This has led to the conclusion in many countries that we need new service models much more focused on “prevention” and “early intervention”.

What this means is that rather than health services designed to respond to ill health and disease once it has occurred, focus on what will keep the population healthy in the first place. Rather than intervening expensively to support children who fail to thrive in the education system, identify the factors that lead to failure to thrive and prevent them (or at least intervene very early to address it).

This all seems self-evident but there are major issues with it. Because we have not operated effectively in this way in the past, we have embedded patterns of demand that drive up the resources needed in reactive services rather than prevention. It becomes very hard to shift declining current budgets to prevention if demand on current services is rising.

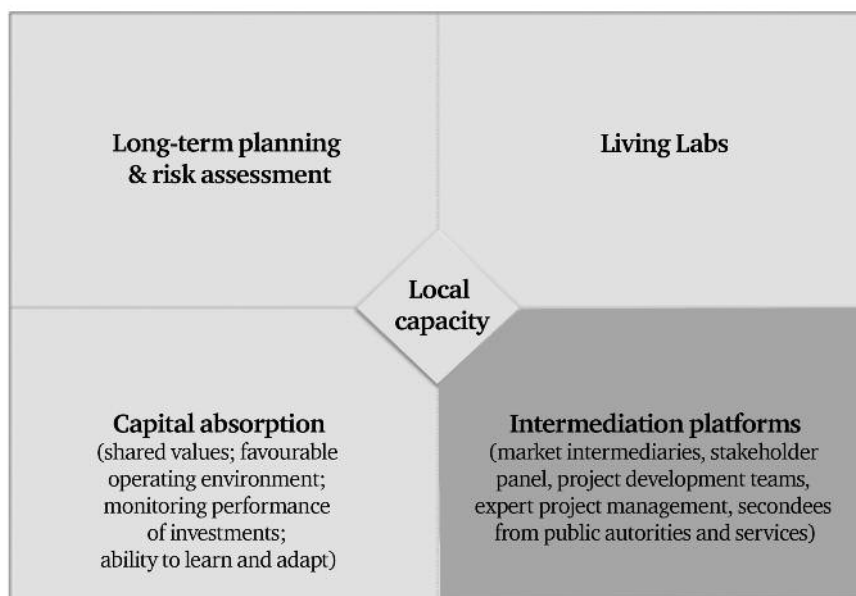
“Prevention” as a concept includes a focus on preventing factors or circumstances likely to lead to negative outcomes as well as focus on the consequences of these factors or circumstances, if we have failed to prevent them. The urgent focus tends to be on the latter. For example, all evidence suggests that low income, high unemployment or underemployment, and low value housing are statistically associated with poor health, educational and negative community safety outcomes. These are hard to address and require a long-term resolution so the short term focus tends to be on addressing their consequences, not their causes.

The case for adopting prevention as a principle for planning and investment is not new. Specifically, we have lost the late 19th and early 20th century understanding that getting infrastructure right is central to prevention. The biggest gains in health and life expectancy across the last 150 years come from investment in water supply, sanitation and housing, before the period of public universal healthcare. The biggest reduction in assaults came from lighting city streets, not the development of police services.

Municipal investment across Europe created an infrastructure we now take for granted and was based on an understanding of prevention as investment: invest now and a flow of benefits will follow over time. As major infrastructure could not be funded out of current budgets, municipal bonds and borrowings were necessary to fund it. All prevention is investment in the sense that up front spending delivers a flow of benefits over time. Given this, it is entirely unclear why it should, or even could, be funded upfront from the current budget. Like any other investment, we need to find funding mechanisms that allow the phasing and linkage of costs and benefits over time.

KEY MESSAGE – Prevention is investment and needs to be designed and financed within an investment paradigm, and given declining and pressurised current budgets, signifi-

Figure 1. Capacity to match local needs with investment



cant investment in prevention is very unlikely if it has to be funded “upfront”. Social infrastructure needs to be brought back into our understanding of prevention: preventing the circumstances that lead to negative outcomes.

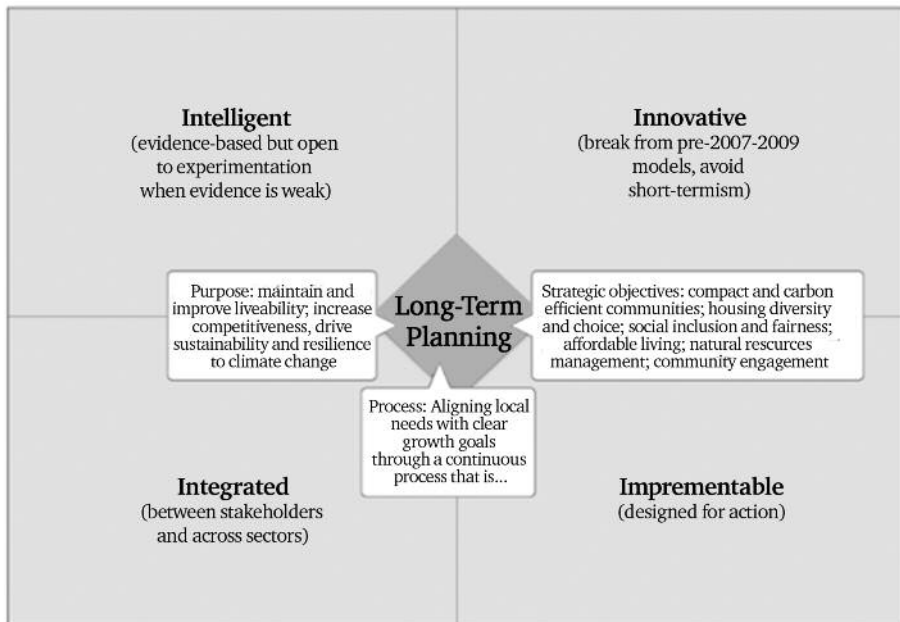
LOCAL CAPACITY TO ABSORB FINANCIAL CAPITAL

The key for generating investable social infrastructure projects that match local needs with investors needs for scale, can be found in capacity and capabilities within four interdependent functions (i) long-term planning and associated risk assessment (ii) living labs that provide a real life test and experimentation environment where end-users, industry and investors co-create solutions (iii) capital absorption capacity that helps us know when private investment for social need is the right path to go down¹ and (iv) intermediation platforms that maximises public value and delivers resilience-focused performance (see Figure 1).

Long-term planning and risk assessment – Something that needs particular attention in Europe but is unpopular politically and often misused is long-term plan-

1. For recommended reading about this function go to: Initiative for Responsible Investment at Harvard University – http://iri.hks.harvard.edu/files/iri/files/the_capital_absorption_capacity_of_places_self_assessment_tool_4.1_2013.pdf.

Figure 2. An overview of long-term planning



ning. Institutional investors, governments, public authorities, business and financial markets have different experiences of what is meant by 'long-term': 10 years from start to finish for projects relying on Structural Funds; 5 years is seen as long-term for public authorities; 4-5 years for politicians although re-election seems to be a priority after 18 months; 12 months for a SME and 60 seconds is long-term for financial traders. But cities, regions and sectors in the US, Australia, Canada etc. understand that 30-40 year plans/forecasts are needed in the competition to attract investment, generate economic growth and build vibrant and attractive communities. The confidence of institutional investors relies on these strategic plans, risk assessment and projections. In the EU, some of the regions we have worked with have gamed local, national and EU-level systems to plan and deliver long-term (e.g. Norbotten, Berlin-Brandenburg and Kymenlaasko). For them, long-term planning is about aligning local needs with clear growth goals through a continuous process that is: intelligent, innovative, integrated and implementable (see Figure 2).

The essence of long-term planning is not a static list of investment priorities. It is about having a clear and transparent set of strategic principles to guide planning decisions informed by big data analytics for prevention, prediction and localisation. And then blending this with participation through genuine consultation to identify the needs and priorities of the people you provide services for. Perhaps most important, long-term planning and associated risk assessment supported by informed consultation can help communities work the economy to achieve their priorities rather than hollow-out communities to serve the economy.

Living labs – A Living Lab is a real-life test and experimentation environment where users and producers co-create innovations. Living Labs have been characterised by the European Commission as Public-Private-People Partnerships (PPPP) for user-driven open innovation. A Living Lab employs four main activities: co-design by users and producers; discovering emerging usages, behaviours and market opportunities; implementing live scenarios within communities of users; assessment of concepts, products and services according to socio-ergonomic, socio-cognitive and socio-economic criteria.

There are opportunities for Living Labs to contribute to pre-procurement projects aimed at supporting public authorities and services to undertake relevant actions that show how multiplier effects from social infrastructure investment can be achieved². For example, Amsterdam is the Living Lab run by a partnership between the City Council and the Amsterdam Institute of Advanced Metropolitan Solutions. Research and valorisation are integrated through a network of ‘test beds’. The first 3 of these are: rain sense, urban pulse and urban mobility³.

Intermediation platforms for project preparation – A key problem is that despite rhetoric, for over two decades the public sector has been locked into an embrace with short-termism by national governments. This is largely driven by political resistance to thinking and acting strategically (compounded by 2007-2009) combined with the financial pressure on public services to continue fighting fires by pursuing further efficiency savings instead of looking ahead. Cuts are sold as growth enhancing. But all EU countries that pursued austerity since 2010 now have more debt and not less.

This is not to say that regions, cities and municipalities are sitting still. New initiatives such as R2o (regions for climate action with green infrastructure using innovative financing); 100 Resilient Cities (pioneered by the Rockefeller Foundation), the Amsterdam Institute for Advanced Metropolitan Solutions and the European PPP Expertise Centre provide examples of how public authorities are innovating in order to address the challenges and stresses of macro-trends and how preventive and resilient actions are reinventing the public sector.

That said, there is a need for a new type of intermediary between the public sector and investors. In the United States, there is growing attention to alternative financing vehicles for infrastructure investment. These suggest ways that the public sector, investors, and local communities might adapt to new roles in infrastructure finance⁴. One response to the challenge of developing deals of this type has been the seeding of capacity-building organizations (or platforms) that can work to develop effective local demand for socially valuable infrastructure investment e.g. the West

2. <http://www.openlivinglabs.eu/aboutus>.

3. <http://www.ams-institute.org/category/research-programs/>.

4. Wood D, Organizing demand for infrastructure investment with high social value. In: Garonna P and Reviglio E (eds.) (Pending) *Investing in long-term Europe: re-launching fixed, network and social infrastructure*. FEBAF/CDP, Rome

Coast Infrastructure Exchange and Partnerships British Columbia⁵. The need for such intermediation platforms is underlined by a 2016 Ford Foundation funded report ‘Unlocking the market for more and better infrastructure’. The report identified 5 key barriers (and then solutions) to more and better investment for cities that are relevant to regions, cities, and municipalities across the EU although these need to navigate the obstacles provided by EU rules (e.g. Stability and Growth Pact, Treaty on Stability, Coordination and Governance and European Accounting Standards (ESA 2010)).

KEY MESSAGE – Intermediation platforms combined with living labs, capital absorption capacity and long-term planning are important as a means of unlocking investment and political cycles while maintaining local value for social infrastructure investments.

PLAYING THE EXTERNALITIES OF SOCIAL INFRASTRUCTURE INVESTMENT

Over and beyond the evident output of sectors such as lifelong education, health and social care and affordable housing, there are very substantial “externalities” generated (otherwise termed added value, multiplier effects or high road outcomes) from social infrastructure investment. Indeed, this is the reason why markets alone do not work well here if left alone. Government needs to step in to provide services, or otherwise subsidize provision if not delivered directly by the public sector. The measure of the externalities should help the public sector, among other things, to better calculate the amount of direct grants which it may have to provide aside from other private or public forms of financing.

A focus on social infrastructure and asset secured investment may seem restrictive but it is quite possible to identify a multiplier effect when combining prevention and a secure asset base. Consider the social and environmental performance areas in the Figure 3

Social performance – For example, in the UK there is currently a chronic shortage of good housing for frail older people and a development sector focused largely on competitively priced family housing. (Low-land footprint, two stories, small bedroom sizes, steep stair throws, etc.) This exposes older people to risk (falls, etc.), obstructs the delivery of care at home in later life, and results in higher spending on hospital and residential care. A “home for life” programme could create appropriate de-risked housing, with telecare protection designed in at the outset, and bedroom sizes that would permit intensive nursing support at home if necessary.

Environmental performance – Equally, poor designed, poorly constructed, energy inefficient social housing makes it harder to prevent environmental damage through emissions, and is also a major factor in fuel poverty. A major programme to upgra-

5. West Coast Exchange <http://westcoastx.com/>. Partnerships British Columbia, <http://www.partnershipsbc.ca/>.

Figure 1. Capacity to match local needs with investment

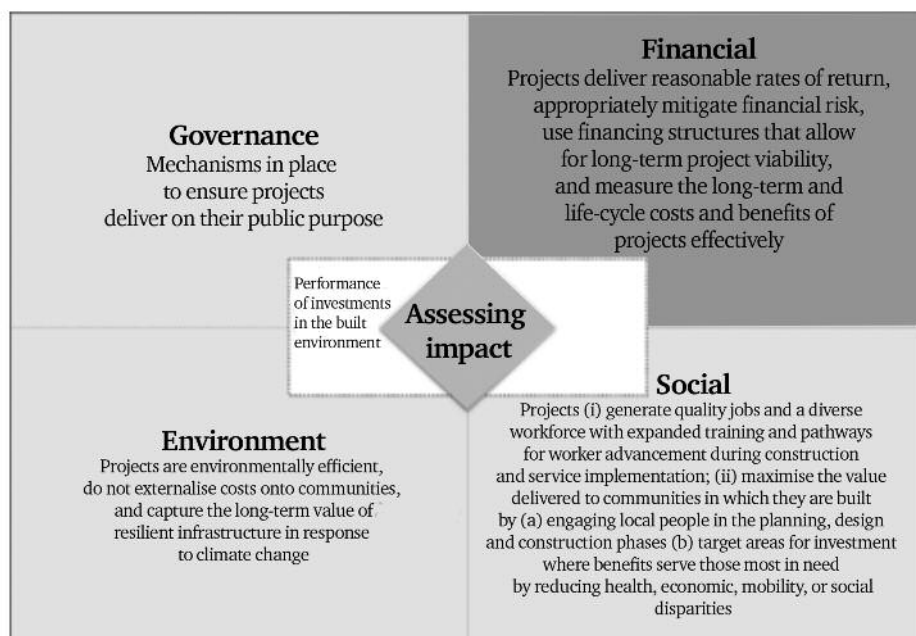


Figure 3. Assessing the performance of investments in the built environment. (Adapted from: High Road Infrastructure Working Group (2015), *Unlocking the market for more and better infrastructure*, Draft Report for the Ford Foundation).

de all affordable housing to a high environmental standard, sensibly commissioned, could prevent environmental damage, prevent fuel poverty, and prevent unemployment/benefit dependency through targeted training and employment requirements built into procurement.

KEY MESSAGE – Attention to externalities as well as governance and financial returns would create a secured asset, an income stream, reduce hospital and care costs through prevention, and the employment opportunities created through construction and delivery could be targeted on economically disadvantaged communities. The merits of an investment model would be that repayment could be phased across 20 – 30 years so that full benefits realisation supports repayment.

CONCLUSIONS

In the EU, public authorities and public services are not building or repairing infrastructure in sufficient quantities to meet existing needs or future demand; nor do

their infrastructure investments “take the high road” by being designed, built, and operated to meet standards other than short-term capital costs and minimum service requirements. To this end, putting prevention into an investment paradigm creates a framework for a more disciplined approach to governance and performance and would contribute to ensuring scale and credibility that are likely to be essential in attracting investors (public, institutional, third sector, foundations, retail).

This chapter is illustrative only but indicates the potential for major investment in social infrastructure to deliver a range of preventative benefits if designed and commissioned intelligently. But achieving this needs more informed dialogue between investors, intermediation platforms and end-users that place investments in physical, human, and social capital.

CONCLUSIONS: NEXT STEPS IN FINANCING LONG-TERM EUROPE

ENSURING CONFIDENCE IN THE FUTURE OF EUROPE

Robert Ophèle*

In most euro area countries investment dropped sharply after the 2007 peak and it has only slightly recovered; as a share of GDP, investment is still well below its 2007 level in almost all euro area countries, and this is particularly the case in Italy where investment represents around 16.5% of GDP, compared with 5% higher before the crisis. We now have a huge investment gap that needs to be closed if we want to have a chance of avoiding the “secular stagnation” menacing our ageing countries

But investing means risk taking and at the same time the household saving rate remains high but with savings mostly invested in the form of short-term, very liquid, financial instruments. Also, non-financial corporations have turned from net borrowers into net lenders in most euro area Member States, including Italy.

The gap between savings and investment is therefore huge and the current account surplus of the euro area reached EUR 350 billion on a yearly basis in September 2016, which is more than 3% of GDP, with Italy being in the euro area average.

Is it a saving glut or an investment crunch or even an investment dearth? Probably a mixture of all three, but if there is a real desire to finance long-term Europe there is an urgent need for some radical changes in three different areas: we need to introduce the right incentives, achieve an efficient institutional environment and reinforce or restore confidence in the future of Europe. Let me elaborate along these three lines.

First, the right incentives; this means promoting long-term savings products as opposed to short-term ones in order to safely finance infrastructures and favour equity over debt; as Europe’s economy is close to the “technological frontier”, businesses need to innovate more. As such, they need to be able to take more risks, which means more equity financing, rather than debt financing. But Europe is lagging behind: equity capital amounts to only 52% of GDP in the euro area, compared with 121% in the United States. The efficient tools are well known: some targeted tax incentives, a favourable regulatory treatment and positive real returns.

In this respect, two European Commission proposals are particularly welcome:

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- In order to reduce the fiscal bias against equity funding the proposal by the European Commission for a Common Corporate Tax Base including the proposal for a new tax allowance encouraging equity issuance should be warmly welcomed. The fiscal bias that favours debt financing, via a tax deductible interest expense, may contribute to economic distortions that can result in high and inefficient debt-to-equity ratios in firms.
- In order to develop long-term European savings products, the Commission closed a public consultation on a potential EU personal pension framework. This initiative is also welcome as it could develop cross-border long-term savings products with a retirement objective. These products would supplement social security-based and occupational pensions while contributing to pan-European long-term investments. The development of long-term savings products, harmonised at EU level, could help intermediaries (banks, insurers, asset managers) to diversify their investments. They would invest in geographically diversified assets including both listed and non-listed equities and possibly hybrid debt. These investments could therefore support the shift towards more equity financing. The development of such products requires putting in place relevant prudential rules for those intermediaries taking into account the long-term holding period constraint of the products.

We should not discourage intermediated risk taking. In order to ensure the robustness of financial intermediaries there is a tendency to transfer risks from these players to customers. There are many variations on this theme: for banks it could mean switching from fixed-rate mortgages to variable-rate ones, for insurers it could mean switching from euro life insurance contracts to unit-linked contracts, for pension funds it could mean switching from defined benefit to defined contribution schemes; the possible switch from bank lending to crowdfunding is another illustration of this tendency. Such developments are straightforward for financial institutions, they are even encouraged by some regulations and, to some extent, they are facilitated by the emergence of Fintechs. Such changes, while massive, would actually imply a transfer of risks from institutions prepared and equipped to manage them to individuals largely unable to do so efficiently as well as the loss of many benefits deriving from inter-generational risk-sharing. This will not be a success and, at the end of the day, after many disillusionings, all the savings will end up in banknotes or sight-deposits, which is exactly what we want to avoid.

Positive real returns are also key in order to provide the right incentives. Many economists have highlighted the unintended consequences of long lasting very low interest rates. Instead of favouring consumption by households and investment by firms, low interest rates can stimulate saving without boosting investment, in which case this would aggravate the imbalances between savings and investment and trigger a downward spiral of interest rates. Many factors could contribute to explaining such a negative outcome: from the household point of view, the need to increase savings could stem from the lack of a home equity channel in continental Europe or from the sharp increase in future savings needed during working life to provide the

same level of pension, a situation which is worsened if you take into account the fact that housing and health costs, two key consumption items for retirees, usually increase more rapidly than the HICP. From the corporate point of view, the low level of investment could be explained in some cases by the need, for sponsors of specific pension schemes, to cover the liability gap deriving from the low interest rate environment and, more generally, by the lack of consumer-driven demand. Fortunately, the situation is evolving rapidly and while both the slope of the yield curve and the slope of inflation expectations are steepening, long-term real interest rates are significantly less negative than some months ago.

Second item on our agenda: achieving an efficient institutional environment.

The Five Presidents' Report rightly called for a Financial Union, encompassing the completion of the Banking Union as well as the launch of the Capital Markets Union (CMU). Strengthening the integration of capital markets must be seen as a complement to Banking Union since both share the same objectives of the free flow of capital and the better financing of the economy by allowing savings collected in one part of the Union to finance investment in another part of the Union. In the end, deepening the Banking Union and the Capital Market Union would allow a better allocation of savings in Europe and a more effective financing of the real economy.

Let me focus on the completion of the Banking Union since, while being one of our major successes, it still needs to be finalised. If one rightly considers that the ultimate goal of a banking union is to facilitate the financing of the Unions' economy by developing Union-wide banking services allowing for the collection of deposits in one part of the Union in order to fund credit in other parts of it, we are still far from achieving such an aim. Having a Single Supervisory Board and a Single Resolution Board would make it possible to treat banks under their remit in a harmonised manner but it would not, in itself, create an effective Banking Union.

We need to increase financial integration, fight the fragmentation of the European banking sector and foster cross-border investments. In this regard, the free flow of capital and liquidity is one of the fundamental principles of the EU as it is a prerequisite for the efficiency of capital allocation and the smooth funding of the economy. Indeed, it means treating the euro area as a single jurisdiction and not as a collection of 19 jurisdictions, and each of the three pillars of the Banking Union needs to be revisited with that aim.

- The first pillar – the Single Supervisory Mechanism – is completely operational and has now fine-tuned its supervisory stance. But if we really want to favour the emergence of a true euro area banking sector we need to make progress on three fronts:
 - First, we should refrain from trapping liquidity and capital on a purely national basis; for the supervisor this means limiting Pillar 2 requirements at a national subsidiary level and granting intra-group liquidity waivers.
 - Second, instead of discouraging banks from developing cross-border activity within the euro area, we should encourage them to do so; this means avoi-

ding the automatic increase in their systemic buffer when they increase their cross-border operations; since the euro area is both a monetary and a banking union, it should be treated as a single jurisdiction in the calculation of the SIFIness score (cross-jurisdictional activity weighs 20% in the overall calculation). This is currently under discussion at the Basel Committee.

- Third, we should encourage the restructuring of our banking industry by ensuring the favourable accounting treatment of goodwill, and by ensuring that losses booked on legacy assets (i.e. on sales of large stocks of NPLs) do not affect automatically the calculation of RWAs (i.e. the capital requirements) for other assets.
- While a banking union could be a fashionable issue in good times, it often becomes nasty in bad times, when resolutions and bail-ins are envisaged. Whatever the resolution strategy – and we assume that at the euro area level it would be a single-point-of-entry approach – if a resolution were to be implemented and a bail-in triggered, it would be on a solo basis, i.e. at the national level. The national level means applying the national rules in order to assess compliance with the “no creditor worse-off than in liquidation” principle and possibly the “8% minimum of total assets bail-in” principle in order to be able to use public support. Both have still significant national features: the hierarchy of creditors in a bankruptcy process differs between euro area countries, as do the accounting standards applied by banks and the calculation of the amount of total assets. The Commission proposal clearly goes in the right direction. But it is clear that our resolution stance can only be implemented either if you start with a completely clean banking sector or when banking consolidation is encouraged and facilitated at the euro area level, or with a strong common Deposit Guaranty scheme. None of these three conditions are fully met in Europe today. Should we ask for a BRRD holiday? Certainly not. Rapid progress is possible regarding the consolidation of the banking sectors and if necessary we can use the possibility provided for in the BRRD to implement precautionary recapitalisation with a limited bail-in complying with general State Aid rules.
- This means that, in my view, the third pillar, i.e. a fully-fledged European Deposit Guaranty System, is not a prerequisite for an effective European Banking Union but its ultimate step; we have to initiate this journey but a progressive approach is the most realistic one in this area.

My third and last point will be on the necessity to ensure confidence in the future and confidence in the future of Europe; without this confidence players will never invest long term.

This is evidently first a political issue, linked to the governance of the euro area. But I would like to stress two more financial issues: the need to reinforce the euro area as a major independent financial jurisdiction and second the need to implement an investment strategy which fully takes account of climate risks.

First, the need to reinforce the identity of the euro area as a major independent financial jurisdiction. I have already mentioned the usefulness of treating the euro

area as a single jurisdiction in order to encourage banking reorganisation, but we should go further by:

- Promoting a review of third-country regimes. Current third-country regimes were adopted in a context where most of the financial transactions pertaining to the European Union were located within its borders, complying with EU rules and consistently supervised within the EU. Accordingly, third-country regimes were designed to be applicable to relatively remote or secondary financial services flows, which did not concentrate a significant part of the EU's financial risks and services and were by no means comparable in volume or significance to flows within the Union. Now that the landscape is likely to significantly evolve, the focus of the discussion should be to properly scrutinise existing third-country regimes. The equivalence regime should be made much more stringent for significant financial activities pertaining to the European Union but carried out outside it in order to establish an effective level-playing field and to avoid the build-up of offshore risks, with a regular review of the provisions. This could be done using a tiered approach, with thresholds above which stringent requirements would apply.
- Second, promoting the relocation in the euro area of the most systemic activities for our financial markets. Some entities or activities play such a systemic role in the EU financial system that they should be deterred from providing services to European actors from an offshore place. They should be located within the EU so that they can be primarily supervised by the framework in place in Member States of the EU, to avoid systemic financial stability risks building up beyond the reach of the supervisors in the EU. This includes most importantly the clearing of euro-denominated financial instruments or the trading of EU sovereign debt. The introduction of thresholds, above which the activity would be required to be located or relocated in the EU should therefore be considered.
- And, third, implementing the proposal made by the European Commission to re-group foreign banking activities under the umbrella of an intermediate holding company in order to supervise and regulate them on a consolidated European-wide basis.

I can't conclude without mentioning one key driver for confidence in the future which needs to be addressed in order to unlock significant long-term investment: the fact that climate risks are properly tackled. Most of you have in mind the seminal speech by Mark Carney on this issue, "Breaking the Tragedy of the Horizon – climate change and financial stability" in September 2015 and I do not wish to return to these risks, which are either direct when a catastrophe occurs or indirect through the increase in the scope of possible "stranded" assets. But almost everyone is now aware that, in the medium run, risks are huge and no sensible investor would now invest long term without measuring these risks. That is the reason why the release last Wednesday of the Recommendations of the Task force on climate-related Financial Disclosures (TCFD) is an important step in the right direction. I do hope that these

standards, that are open to a 60-day public consultation period, will be endorsed by the FSB and the G20 and widely implemented. The German authorities have clearly stated that climate challenges will be high in the Agenda of their Presidency. Let me quote them: “During its G20 Presidency, Germany not only aims to ensure the stability of the global economy, but also, and this is the second pillar, to make it more fit for the future. One main concern is to make progress on realising the goals of the 2030 Agenda for Sustainable Development and the Paris Agreement on climate change.”

“Fit for the future”, this is precisely our ambition for Europe.

LIST OF AUTHORS



GIOVANNI AJASSA

Chief Economist, BNL – Group BNP Paribas

Born in 1959, married with one child, Giovanni Ajassa joined BNL in January 1987 as economist. He holds a degree in Economics from the LUISS Guido Carli University and completed his studies of monetary and industrial economics at Oxford University. He has published a considerable number of economic essays. Mr. Ajassa serves as Director of Associazione per lo Sviluppo degli Studi di Banca e Borsa (Association of the Development of Bank and Stock Exchange Studies) and as Member of Board of Advisors for Nomisma S.P.A.



PAOLA ALBRITO

Head, of Regional Office for Europe, United Nations Office for Disaster Risk Reduction – UNISDR

In her current role, she supported the delivery of disaster risk reduction coordinated actions and partnership development within the Hyogo Framework for Action implementation and braced the preparation of the Third UN World Conference on Disaster Risk Reduction and the Sendai Framework for Disaster Risk Reduction 2015-

2030. Paola joined UNISDR in 2004 during the preparations for the Second UN World Conference on Disaster Reduction, where she fed the conference with the Outcome Analysis Document on the status of risk reduction implementation at the global level. Between 2005 and 2008, Paola worked on policy issues related to building resilience to disasters, including the development of guidelines on indicators assessing disaster risks, and the mainstreaming of disaster risk reduction into sustainable development policies and programmes. Her previous work experience includes the coordination of Common Country Assessment and the United Nations Development Assistance Framework (programmes addressing sustainable development issues) in Djibouti as part of the UN Resident Coordinator Office (1999-2003); supporting the UN Country Teams in developing sustainable development policies as part of the United Nations Staff System College in Turin; and conducting programme evaluations as independent consultant at the International Labour Organisation. Paola holds a Master's Degree in International Relations and Political Science from the University of Turin, Italy. She is a member of the International Institute of Strategic Studies (London, UK) and Editorial Advisor at the Crisis Response Journal. She speaks Italian, French, English and some Russian.



DOMENICO ARCURI
CEO, Invitalia

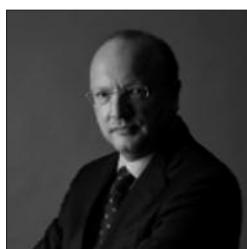
Mr. Domenico Arcuri is Chief Executive Officer of Invitalia SpA. He served as Chief Executive Officer and Partner at Deloitte Consulting Italia S.r.l. and as a Partner at Arthur Andersen SpA. Mr. Arcuri holds a degree in Economics from the University LUISS Guido Carli of Rome.



GABRIEL BERNARDINO

Chairman, European Insurance and Occupational Pensions Authority – EIOPA

Gabriel Bernardino is Chairman of the European Insurance and Occupational Pensions Authority (EIOPA). He is responsible for the strategic direction of EIOPA and represents the Authority at the Council of the European Union, the European Commission and the European Parliament. Mr. Bernardino prepares the work of EIOPA's Board of Supervisors and also chairs the meetings of the Board of Supervisors and the Management Board. Mr. Bernardino is the first Chairperson of EIOPA. He was elected by the Board of Supervisors of EIOPA on 10 January, 2011. His nomination followed a pre-selection of the European Commission and was confirmed by the European Parliament after a public hearing held on 1 February, 2011. Mr. Bernardino assumed his responsibilities on 1 March, 2011 for a first five-year term. On 16 December 2015 the European Parliament confirmed the re-appointment of Mr Bernardino for a second five-year term, which started on 1 March 2016. Prior to his current role, Mr. Bernardino was the Director General of the Directorate for Development and Institutional Relations at the Instituto de Seguros de Portugal (ISP). He has served in several positions of increasing responsibility since he joined the ISP in 1989 and represented EIOPA's preceding organisation, CEIOPS, as Chairman between October 2009 and December 2010.



VINCENZO BOCCIA

Chairman, Confindustria

Vincenzo Boccia was born in Salerno in 1964. He graduated in economics, and became CEO of Arti Grafiche Boccia Spa, the family firm that operates in the graph. He joined Confindustria in the early 1990s, actively participating in the Group of young

entrepreneurs; a regional leader of the youth of Campania and President of under 40 of Salerno, in 2000 is chosen as national youth Vice-President. In 2003 he was elected regional President of Piccola Industria della Campania, becoming National Vice-President two years later. He was appointed national Chair of small industry in 2009, and automatically becomes Vice President of Confindustria. On 31 March 2016 Vincenzo Boccia was elected National President of Confindustria.



SIMONA BONAFÈ

Vice-Chair of the Long Term Investment Intergroup

Simona Bonafè ran as head of list of the Italian Democratic Party (PD) for the European Parliament election in May 2014 and was elected, for her first mandate, with the highest number of preferential votes among Italian MEPs. In the European Parliament she is a member of the Progressive Alliance of Socialists & Democrats (S&D) and sits as Member in the Committee for Environment, Public Health and Food Safety (ENVI), and as Substitute Member in the Committee on Industry, Research and Energy (ITRE). She is vice-chair of the Long Term Investment Intergroup. MEP Bonafè was elected to the Italian Lower Chamber in 2013, sitting in the Committee for Economic Activities and Trade. Prior to that, for over 10 years she was engaged in local politics in Tuscany, where she served as Municipal Council Member for Environment.



INNOCENZO CIPOLLETTA

Chairman of UBS Italia SIM SpA, Chairman of AIFI, Deputy Chairman of the Italian Banking Insurance and Finance Federation

Born in 1941, Innocenzo Cipolletta is Senior Advisor of UBS Limited Italy Branch,

Chairman of The University of Trento, Chairman of Fondo Strategico Italiano and Chairman of AIFI (Italian Private Equity and Venture Capital Association) and Senior Advisor of UBS Limited AG. He's also Deputy Chairman of Assonime (Association of the Italian joint stock companies), FeBAF (the Italian Banking, Insurance and Finance Federation) and member of the board of S.p.A, Lunelli S.p.A. and of Laterza-Agorà Srl. He was Chairman of Ferrovie dello Stato S.p.A., the Italian state-owned Railways (from 2006 to 2010), Chairman of the daily financial newspaper *Il Sole 24 Ore* (from 2004 to 2007), and of the Marzotto Group (from 2000 to 2003). He also held the position of Director General of Confindustria (the Italian Industry Association) from 1990 to 2000. Cipolletta is a component of numerous Scientific Committees. As a professor of economics, he has taught at the University of Rome "La Sapienza", at the University of Reggio Calabria, at the University of Florence "Cesare Alfieri" and at the Roman University "LUISS-Guido Carli". Innocenzo Cipolletta is a publicist and economics commentator of the Italian magazine *Espresso* and for other newspapers. He is also the author of a large number of scientific publications and books and member of a number of non-profit organisations such as the Italian Statistics Society, the Italian Economists Society, Demographics and Statistics, the ISTAO (Istituto Adriano Olivetti per la Gestione Economica dell'Azienda) and of the Italian Institute for International Affairs (IAI). Innocenzo Cipolletta has been appointed Cavaliere di Gran Croce.



CARLO COTTARELLI

Executive Director, International Monetary Fund – IMF

Carlo Cottarelli, a citizen of Italy, served as Director of the Fiscal Affairs Department from November 2008 to October 22, 2013. After receiving degrees in economics from the University of Siena and the London School of Economics, he joined the Research Department of the Bank of Italy where he worked from 1981 to 1987 in the Monetary and Financial Sector Division. After working for about one year as head of the Economic Research Department of ENI (the main Italian energy company), Mr. Cottarelli joined the IMF in 1988, working for the European Department, the Monetary and Capital Markets Department, the Policy Development and Review Department, and the Fiscal Affairs Department. He was Deputy Director both in the European Department and the Strategy, Policy and Review Department. Mr. Cottarelli has worked on several advanced, emerging market, and low-income countries in the context

of surveillance, IMF-supported programs, and technical assistance, including Albania, Croatia, Hungary, Lebanon, Russia, Serbia, Tajikistan, Turkey, Italy, and the United Kingdom. He is currently Director of the Fiscal Affairs Department, which provides advice in public finance matters to some 100 advanced, emerging and low-income economies every year. As head of the Fiscal Affairs Department, he was responsible for the development and publication of the Fiscal Monitor, one of the three IMF flagship publications. He has written several papers on fiscal and monetary policies and institutions, and edited books on inflation, monetary policy, and exchange rates.



PAOLO CUNIBERTI

CEO and Executive Vice Chairman, H-Farm

Paolo Cuniberti has worked for years at JPMorgan in London where he held managerial positions such as: Head of Equity Derivative origination in Emea, Head of Equity Capital Market and head of Alternative Fund Coverage. In 2007 he joined Mediobanca. As Head of the office based in London Mr. Cuniberti worked on the new platform Mediobanca UK Capital Market. He served as CEO of MedioBanca Securities. Financing partner since 2012 he joined H-FARM as Executive Chairman in 2015.



DAVIDE DAL MASO

Coordinator of the National Dialogue on Sustainable Finance, UNEP

Davide Dal Maso has worked for years as a business consultant, specialising in environmental management and innovation. Among the founders of the Milan-based Avanzi – a think tank for sustainability, he has focused his studies on the relationship between financial activities and sustainable development. He currently runs re-

search and consulting activities for the design and the implementation of strategies and management systems for corporate social responsibility. He is author of several articles and books on this topic. Davide is President of Make a Cube3, an incubator that assists start ups with high potential for creating social and green value, by providing comprehensive business support services, including back-office, governance expertise, access to knowledge and financing. He is the coordinator of the National Dialogue on Sustainable Finance, a joint initiative of UNEP, the United Nations.



PIER VIRGILIO DASTOLI

President, Italian Council of the European Movement

Pier Virgilio Dastoli was born in Anzio (Rome) 12.5.1949. He is a journalist and a lawyer since 1974. He has been researcher in Istituto Affari Internazionali in Rome from 1972 to 1976 in the fields of scientific and technological cooperation and Mediterranean policies and personal assistant of Altiero Spinelli in the Italian and European Parliament. He has been also special advisor of the Italian government in the Dooge Committee (1984-1985), special advisor of the European Commission (1986-1987), official of the European Parliament in the fields of fiscal, cultural, information and cultural policies. He was also appointed as head of the Representation of European Commission in Italy, advisor of the Conference of “governors” of Italian Regions in the field of EU policies, member of the “Spinelli Group” board (2011-2014). He has been general secretary of the International European Movement (1995-2002), speaker of the EU Permanent Forum of Civil Society (1996-2003). He is president of the Italian branch of the International European Movement, Senior Fellow of the School of Economic Policy in Rome and “Jean Monnet” teacher in Italian universities. He is author of books and essays on European affairs.



MARIA BIANCA FARINA

President, ANIA and President ANIA Foundation for Road Safety

President of Poste Italiane; Degree with honor in Economics at “La Sapienza” University of Rome; Knight of the Order of Merit for Labour of the Italian Republic from 2016; Commendatore of the Italian Republic from June 2012; From 2014 member of the AIF, the Financial Information Authority of the Holy See, appointed by Pope Francis; From September 2015 part of the Board of Directors of the “Bambino Gesù Onlus” Foundation; Member of the Board of “Save the Children”; Member of the Board of Directors of FeBAF (Banks, Insurance and Finance Federation).



PAOLO GARONNA

Secretary General of the Italian Banking Insurance and Finance Federation

Full Professor of Political Economy at the LUISS Guido Carli University of Rome, Paolo Garonna was Director General of the Association of Italian Insurers (ANIA), Director General of the Italian National Institute of Statistics (ISTAT) and, from 1989 to 1992, Deputy Director for Labour, Social Affairs and Education at the Organisation for Economic Co-operation and Development (OECD) in Paris. He was also Deputy Executive Secretary of the United Nations Economic Commission for Europe (UNECE) in Geneva, and Chief Economist of Confindustria from 2003 to 2005. He carried out research in America as Fulbright scholar, and in Cambridge, Great Britain, where he co-operated with the Nobel Prize winner Richard Stone. He has published a considerable number of books and essays on Applied Economics, Statistics and Finance. He has been the Secretary General of the Italian Banking, Insurance and Finance Federation since October 2012.



MARK GARVIN

Vice Chairman for the Corporate & Investment Bank at J.P. Morgan

Mark Garvin is Vice Chairman for the Corporate & Investment Bank at J.P. Morgan. He is also Chairman of J.P. Morgan Europe Ltd and Chairman of the Supervisory Board of J.P. Morgan AG. Mr Garvin has worked for J.P. Morgan and its predecessor banks since 1978. After serving in various capacities in the Latin American division he became credit officer in Paris in 1982. He transferred to London in 1985 where he assumed responsibility for UK client coverage. In 1988 he was appointed deputy general manager of the London branch and in 1992 became UK Senior Country Officer. In 1997 he was appointed Chief Operating Officer – Europe, Middle East & Africa, and in 2004 became Chairman, Treasury & Securities Services International, a position he held until assuming his current role in 2012. He is Senior Independent Director of Euroclear Plc, Deputy Chairman of The British Bankers Association and a Director of British American Business. Education: BS Georgetown University, 1974 and MBA American University, 1977.



SONJA GIBBS

Senior Director Global Capital Markets Department, Institute of International Finance – IIF

Sonja Gibbs is Senior Director of the Global Capital Markets Department at the Institute of International Finance (IIF). Her research interests include systemic risks in financial markets, portfolio flows, global banking sector analysis, emerging/frontier market development, and investing in infrastructure and green finance. Her work on policy includes issues related to the G20 and the international financial institutions. She co-authors a number of regular IIF publications including the Weekly In-

sight, the monthly Capital Markets Monitor, and the quarterly Capital Flows to Emerging Markets. Ms. Gibbs has spent over 20 years in banking and financial markets, most recently with Nomura International in London, where she was Chief Equity Strategist. Previously she was Head of East European Economics and Senior European Bond Analyst for Nomura International; earlier positions included stints as a bank credit analyst and U.S. economist for First Interstate Bank and the Industrial Bank of Japan. She has also worked in academia, teaching undergraduate microeconomics, and spent several years with the Berkeley-Stanford Program on Soviet International Behavior.



ROBERT GLASSER

Special Representative of the Secretary-General (SRSG) for Disaster Risk Reduction

From 2008 to (March) 2015 he was the Secretary General of CARE International, one of the world's largest non-governmental humanitarian organisations, active in over 80 countries. From 2003-2007, Dr Glasser was the Chief Executive of CARE Australia, overseeing aid programmes in Cambodia, Vietnam, Papua New Guinea, and in the Middle East, among others. Prior to joining CARE, he was Assistant Director General at the Australian Agency for International Development (AusAID) where he held responsibilities in a variety of areas including the Papua New Guinea and Mekong programmes, Corporate Policy and Infrastructure and Environment. Dr Glasser has also worked on international energy and environmental policy for the US Department of Energy and on peace and conflict issues at a variety of institutions, including the Cornell University Peace Studies Program and the Centre for International and Strategic Affairs at the University of California. Dr Glasser is a member of the board of the Global Call for Climate Action (GCCA), a global alliance of more than 450 national and international organisations focussing on climate change advocacy; and serves as Chairman of the Board of the CHS International Alliance, a new organisation resulting from the merger of People in Aid and the Humanitarian Accountability Partnership (HAP). He was formerly the Chair of the Steering Committee for Humanitarian Response, comprised of the Chief Executives of the largest international Non-Government Organisations involved in humanitarian relief, a member of the Advisory Panel of the Climate Vulnerability Monitor 2012, a member of the Principals Steering Group of the United Nations Transformative Agenda for Humanitarian Action; and a member of the Project Steering Group for the World Economic Forum project on The Future Role of Civil Society.



JOSÉ MANUEL GONZÁLEZ-PÁRAMO

Executive Board Director Banco Bilbao Vizcaya Argentaria S.A. (BBVA)

José M. González-Páramo is Ph.D., M.Phil. and M.A. in Economics from Columbia University. He also holds a Ph.D. from Universidad Complutense. His professional record is a blend of central bank decision-making and private sector responsibilities, academic experience and advisory positions. In 1988 he was appointed Professor of Economics at UCM. In addition, he has taught advanced courses in economic analysis of public policies at the Centro de Estudios Monetarios y Financieros in Madrid and at other research centres. From September 2012 he is a Professor at IESE Business School. From 1985 to 1994 he was an economic adviser to various public and private institutions including the Banco de España (1989-1994), the European Commission, the IMF and the World Bank Group. He has been involved in working groups on economic and financial matters at the Bank for International Settlements and the Organisation for Economic Co-operation and Development. José M. served as a member of the Executive Board of the European Central Bank (ECB) from 2004 to 2012. He was also a member of the Governing Council of the ECB. In June 2013 he was appointed Executive Board member of BBVA. As Executive Board Director, he is the Chief Officer, Global Economics, Regulation & Public Affairs, and the Chairman of its International Advisory Board. He is also Chairman of European DataWarehouse GmbH, the first central data warehouse in Europe to provide high transparency standards for asset-backed securities (ABS) transactions. Since January 2015, he is the Europe chair of the TransAtlantic Business Dialogue (TABD), the official business advisory group to the European Commission and U.S. administration.



PIERRE GRAMEGNA

Minister of Finance of the Grand-Duchy of Luxembourg

Pierre Gramegna was born on April 22, 1958. He is married and has two children. After finishing high school in Luxembourg, he studied law and economics at the University of Paris II (Panthéon-Assas) where he graduated with a degree (Maîtrise) in civil law in 1981 and a degree (Licence) in economics in 1982. Pierre Gramegna also holds a Master of advanced studies in European community law. Since December 2013 Pierre Gramegna is Minister of Finance of the Grand-Duchy of Luxembourg. He was the Director of the Chamber of Commerce of Luxembourg from September 2003 to December 2013. From 2002 to 2003 he has been the Director of International Economic Relations at the Ministry of Foreign Affairs of the Grand-Duchy of Luxembourg. From 1996 until 2002, he was Ambassador Extraordinary and Plenipotentiary of Luxembourg to Japan. He is a dedicated amateur of tennis and photography. Pierre Gramegna is fluent in English, French, German, Italian, Luxembourgish.



ROBERTO GUALTIERI

MEP, Chair of the Committee on Economic and Monetary Affairs

Roberto Gualtieri (born in Rome, 19/07/1966) has been a member of the European Parliament since 2009. In July 2014, he has been elected Chair of the Committee on Economic and Monetary Affairs. He graduated in literature and philosophy (1992) and has a research doctorate (PhD) in contemporary history (1997). Mr. Gualtieri is an associate professor of contemporary history at 'La Sapienza' University, Rome. He is member of the National board of the Partito Democratico (Italy), since 2008.



RONY HAMAUI
Chairman, Assifact

Rony Hamaui is president of Intesa SanPaolo Forvalue and Assifact (Associazione Italiana per il factoring), adjunct professor of Monetary Economic at Catholic University of Milan, Board Member of the LSE Alumni Italy and CDEC (Centro di documentazione ebraica). He graduated at Bocconi University and London School of Economics and Political Science. He was General Manager of Mediocredito Italiano (a leading bank for factoring, leasing, and medium term loans) and head of Financial Institutions at Banca Intesa. He formerly headed the Economic Research Department of Banca Commerciale Italiana and was a lecturer at University of Bergamo, Bocconi University and a research assistant at the Institute for Social Research. He was member of the board of Société Européenne de Banque– Luxembourg, ZAO Banca Intesa– Moscow, Montetitoli, Assilea and EBA Clearing for several years. He has published articles and books mainly in international economics and finance.



JYRKI KATAINEN
Vice President European Commission, European Commissioner for Jobs, Growth, Investment and Competitiveness

Finnish nationality. Married with two children. Prime Minister of Finland (2011-14); Finance Minister and Deputy Prime Minister of Finland (2007-11); Vice-President of the European People's Party (2006-12); President of the Finnish National Coalition Party (2004-14); Vice-President of the Finnish National Coalition Party (2001-04); First Vice-President of the Regional Council of Northern Savonia, Finland (2001-04); Member of the Finnish Parliament (1999-14); Vice-President of the Youth of the European People's Party (1998-2000); Master's degree in Social Sciences (1998).



STEVEN MAIJOOR

Chairman, European SecuritiesMarket Authority – ESMA

Steven Maijoor has been the Chair of the European Securities and Markets Authority (ESMA) since taking up office 1 April 2011. He is the first chair of the authority and is currently serving his second five-year term. He is responsible for representing the Authority as well as chairing ESMA's Board of Supervisors and the Management Board. The role of the Board of Supervisors is to give strategic guidance to ESMA and make all main regulatory and supervisory decisions. The Management Board's purpose is to ensure that the Authority carries out its mission and performs its tasks. Prior to taking up this role, Steven was Managing Director at the AFM, the Dutch financial markets regulator, where he was responsible for capital market supervision, including financial reporting and auditing, prospectuses, public offerings, and the supervision of the integrity of financial markets. During his term, the scope of activities of the AFM vastly expanded and he was responsible for building and implementing supervision in the capital market area. In his regulatory role at the AFM, Steven has held a number of international positions, including the Chairmanship of IFIAR (International Forum of Independent Audit Regulators). Before joining the regulatory world, Steven was the Dean of the School of Business and Economics at Maastricht University, and had pursued a long career in academia which included a variety of positions at Maastricht University and the University of Southern California. He holds a PhD in Business Economics from Maastricht University, was a research student at the London School of Economics, and has a master in Business Economics from the University of Groningen. Steven is married and has two daughters and a son.



RAINER MASERA

Dean of the School of Business at the Università degli Studi Guglielmo Marconi in Rome

He served as technical Minister for the Budget and Economic Planning in the Dini Government and was appointed one of the 5 “Wise Men” for the review of the “Lamfalussy” process (IIMG) and Member of the High Level Group of European Commission on Financial Supervision in the EU (Group de Larosière). He was Member of the Board of the Bank for International Settlements and Member of G10 Deputies, Central Director in Bank of Italy (Rome), Managing Director of IMI SpA, Chief Executive Officer and Chairman of the Group Sanpaolo IMI (Turin) and of RFI SpA, Chief of the Italian Delegation of the Franco-Italian Government Committee for the new Turin-Lyon railway link and Expert Member of the Board of the European Investment Bank. He is currently Chairman of the Advisory Committee on Financial Management of Fondazione Roma.



FRANCESCO MAZZAFERRO

Head of the Secretariat European Systemic Risk Board (ESRB), Frankfurt a. M.

Francesco Mazzaferro has been the Head of the Secretariat of the European Systemic Risk Board (ESRB) since January 2011. Following legal studies, he began his career in the field of financial market analysis at the Istituto Bancario San Paolo di Torino (today part of Intesa Sanpaolo) in Turin in 1987. Mr Mazzaferro joined the European Commission in Brussels in 1992, starting his international career in the Directorate General for Economic and Financial Affairs, where his work focused on the European Currency Unit (ECU) and preparations for the introduction of the single currency. In 1995, he joined the European Monetary Institute – which later became the European Central Bank – in Frankfurt as the Officer of Policy Planning. In 1998,

Mr Mazzaferro became Senior European Relations Officer. From 2000, he worked as Principal in the EU Neighbouring Regions Division, becoming the Head of Division in 2003.



FLAVIA MICILOTTA
Executive Director, Eurosif

Flavia came on board Eurosif in December 2015. Ms Micilotta joined from the Brussels based Foreign Trade Association (FTA), the umbrella organisation that promotes social compliance (BSCI) and environmental performance management (BEPI), where she worked as Sustainability Consultant. Over the years, Ms Micilotta has accumulated a wealth of experience on Corporate Social Responsibility and SRI, with a particular focus on valuing intangibles through ESG performance, across sectors. She worked on SRI for Vigeo group and KBC group and as sustainability consultant for Deloitte and EY. She is one of the founding members of the UN Global Compact in Belgium and a former board director of the Belgian Sustainable Investment Forum, BELSIF.



CARLOS MONTALVO REBUelta
Partner, PricewaterhouseCoopers Spain

Carlos has joined PwC as EMEA Insurance Regulatory leader, anticipating regulatory trends and providing coordinated responses that benefit from his expertise in the Global and European regulatory landscape. Carlos has recently joined PwC (May 2016) following a career of more than 15 years in the area of Regulation and Supervision of Insurance undertakings and groups. Until end March 2016, and since

2011, Carlos was the first Executive Director at EIOPA (European Insurance and Occupational Pensions Authority), in charge of its management, work program, organisation, people and finances. During his mandate, EIOPA moved from less than 20 staff to 150 and became a key stakeholder regarding, amongst others, the Solvency II project. Prior to that, Carlos was appointed (2007-2010) as Secretary General of CEIOPS, the Committee of European Insurance and Occupational Pensions Supervisors, responsible of its regulatory agenda and the day to day management of the institution. In addition to his international roles, Carlos played a number of relevant roles at the Spanish Insurance Supervisor (2000-2007), including representing it at Council meetings during Solvency II negotiations, or at CEIOPS Board. His role coordinating group supervision in Spain provided him with an in-depth view of the Market and the business. Carlos is also a Member of the Board of Trustees at the ILF (Institute of Law and Finance) in Frankfurt, where he also lectures risk management for Insurance undertakings. Additionally, he has been a frequent speaker in different fora, invited professor by a number of universities and author of different articles on Insurance and Pensions related issues.



ROBERT OPHÈLE

Second Deputy Governor, Banque De France

Robert Ophèle was born in 1956 and graduated from the ESSEC business school with a specialist degree in finance. He joined the Banque de France in 1981 and spent three years in banking supervision before joining the Monetary Studies and Statistics Directorate as an economist, specialising in the interaction between financial market developments and monetary policy. Following a secondment to the Federal Reserve Bank of New York between 1990 and 1991, he returned to the Banque de France as Head of the Budget Division, and subsequently took up the position of Director of the Management Control and Budget Directorate. In this role, he represented the Banque de France on various Eurosystem committees, including the AMICO, the COMCO and the Budget Committee. In July 2006 he was appointed Deputy Director General Economics and International Relations, with responsibility for monetary policy issues and for the Bank's collaboration with universities. In June 2009 he was promoted to the position of Director General Operations, and took charge of market operations, the oversight of French payment systems, financial stability and customer banking services. While in this post, he actively participated in the work of

various financial bodies (Chairman of the National SEPA Committee, Chairman of the Paris Robustesse group and of the Market Infrastructure group). Robert Ophèle has been Second Deputy Governor of the Banque de France since 6 January 2012, and has also been appointed by the Governor to represent him as Chairman of the Autorité de contrôle prudentiel et de résolution (French Prudential Supervision and Resolution Authority – ACPR). He is a member of the college of the Autorité des marchés financiers (French Financial Markets Authority – AMF) and of the Supervisory Board of the Caisse des Dépôts, and in January 2014 became a member of the Supervisory Board for the European Central Bank’s Single Supervisory Mechanism. Robert Ophèle is a Chevalier of the French Legion of Honour.



PIER CARLO PADOAN

Italian Minister of Economy and Finance

Pier Carlo Padoan was appointed Minister of Economy and Finance in the Government led by Matteo Renzi on 24 February 2014. Mr. Padoan was Professor of Economics at the University La Sapienza of Rome, and Director of the Fondazione Italianeuropei, a policy think-tank focusing on economic and social issues. On 1 June 2007 Mr. Pier Carlo Padoan was appointed Deputy Secretary-General of the OECD. As of 1 December, he was also appointed Chief Economist while retaining his role as deputy Secretary-General. In addition to heading the Economics Department, Mr Padoan was the G20 Finance Deputy for the OECD and has also lead the Strategic Response, the Green Growth and Innovation initiatives of the Organization. From 2001 to 2005, Mr. Padoan was the Italian Executive Director at the International Monetary Fund, with responsibility for Greece, Portugal, San Marino, Albania and Timor Leste. He served as a member of the Board and chaired a number of Board Committees. During his mandate at the IMF he was also in charge of European Co-ordination. From 1998 to 2001, Mr Padoan served as Economic Adviser to the Italian Prime Ministers, Massimo D'Alema e Giuliano Amato, in charge of international economic policies. He was responsible for co-ordinating the Italian position in the Agenda 2000 negotiations for the EU budget, Lisbon Agenda, European Council, bilateral meetings, and G8 Summits. He has been a consultant to the World Bank, European Commission, European Central Bank. Mr. Padoan has a degree in Economics from the University of Rome and has held various academic positions in Italian and foreign universities, including the College of Europe (Bruges and Warsaw), Université Libre de

Bruxelles, University of Urbino, Universidad de la Plata and °University of Tokyo. He has published widely in international academic journals and is the author and editor of several books.



GIUSEPPE PAPAleo
President, IASEM

Giuseppe Papaleo is an Italian civil engineer and entrepreneur, specialized in civil constructions, roads and paves. Since 2013 he has held the role of sole director of Papaleo Srl and within the family company he has developed high and specific expertise, both in the implementation and management, in Quality and Factory Production Control System, as well as in Safety in workplace matters. He has been General Director of C.R.O.Med. – Center for Research on East and Mediterranean. He is founder and, since 2011, President of IASEM – Institute of High Euro Mediterranean Studies; in this role he has focused especially in developing international relations network and strengthening public relations with several Mediterranean Countries and European Institutions. His work moves from his personal belief that Mediterranean integration represents the most important challenge to reintroduce and realize efficient international policies.



VALERIA RONZITTI
General Secretary CEEP (European Centre of Employers and Enterprises Providing Public Services and Services of General Interest)

Ms. Ronzitti is General Secretary of CEEP since May 2012. She reached this position after having worked for the organisation for nine years. Jurist, she joined CEEP Ge-

neral Secretariat as legal advisor in 2003, after having started her career practicing labour and civil law in a law firm in Italy. In her function as Head of Social Affairs from 2005 to 2009 she represented CEEP General Secretariat in several negotiations. Amongst others: the European cross-sectoral negotiations on the orientations for reference on managing change (2003), the lessons learned on European Work Councils (2005), the autonomous agreement on work-related stress (2004), the autonomous agreement on violence and harassment at work (2007), the joint labour market analysis (2007), the revision of the parental leave agreement (2009). Alongside her functions in CEEP she was also, from 2005 to 2010, Director of HOSPEEM, the European Hospital and Healthcare Employers Association, that she contributed to set up as a sectoral member of CEEP. In that function she negotiated the sectoral agreement on sharps instruments, which was transposed into a directive. In her function as Director from 2009 to 2012 she continued to represent CEEP General Secretariat in European cross-sectoral negotiations such as the autonomous agreement on inclusive labour markets (2010) and the (failed) revision of the working time directive, while also supervising CEEP policy implementation, communication to CEEP members and managing CEEP staff. In her function as CEEP General Secretary she is responsible for managing the organisation, including overall policy making and implementation, external representation, communication to members, management and coaching of CEEP staff. The main achievements of her first mandate as General Secretary (2012-2015) have been either directly related to CEEP such as the establishment and consolidation of a new and lighter governance structure and a complete internal restructuring in compliance with budgetary needs or more broadly positively affecting the public services community, such as the positive definition of “in house” in public procurement and concessions or the re-launch of the CEEP-CSR Label, which awards Services of General Interest providers with outstanding Corporate Social Responsibility commitments demonstrating that public services providers do more than just fulfilling their services. Her current mandate is focussed on positioning high performing public services as a key component for EU competitiveness and a driver for jobs and growth EU wide.



GIOVANNI SABATINI

General Manager ABI. Chairman of the Executive Committee of the EBF

Giovanni Sabatini, General Manager of the Italian banking association (ABI) since 2009, has been appointed as the new Chairman of the Executive Committee of the

European Banking Federation for a two-year term from January 2016. He's also Chairman of Consorzio Bancomat. Giovanni Sabatini graduated in Economics and Business from the LUISS university in Rome and later returned there in the capacity of lecturer. He has been Co-Manager of CONSOB (the Italian Stock Exchange Authority) as well as overseeing its Issuers Information Division since June 2008. From September 2004 to May 2006 he headed the Intermediaries Division and before that he was in charge of the Markets Division (September 1986-May 2001). From June 2006 to June 2008 he was the Head of the Banking and Financial System – Legal Affairs Department of the Italian Ministry of Economy and Finance. At this time Giovanni Sabatini was also the Ministry's representative on the High Council of the Bank of Italy. From May 2001 to September 2004 he was CEO of Monte Titoli S.p.A (a company owned by the Italian Stock Exchange Group) and Chairman of ECSDA (the European Central Securities Depositories Association). From July 2009 to 2014 he was Chairman of the Consultation Committee of the Italian stock exchange Borsa Italiana.



VALERIA SANNUCCI
Deputy Governor Bank of Italy

Valeria Sannucci has been a Member of the Governing Board and Deputy Governor of the Bank of Italy since May 2013; as such, she is also member of the joint Governing Board of the Insurance Supervisory Authority (IVASS). Born in Rome, 19 April 1953, she joined the Bank of Italy in 1977, assigned to the Foreign Exchange Unit of the Milan regional branch. In 1979 she moved to the Head Office in Rome, in the Research Department, first with the international and then with the monetary sector, where she headed the Financial Accounts Office. From 1986 to 1992 she was part of the Historical Research Office, contributing to the works published in 1993 for the 100th anniversary of the founding of the Bank of Italy. In 1996 she joined the Personnel Management Department and then, from 2006 to 2012, she was Head of that Department. During this period she worked on the organizational reform of the Bank and was a member of the Human Resources Conference (which groups the heads of personnel of the ESCB central banks) as well as a number of collegial bodies for human resources management within the Bank. In December 2012 she was named Managing Director responsible for coordinating the activities related to the Bank's participation in the Eurosystem, including the Banking Union project. Ms Sannucci graduated from the University of Rome "La Sapienza" in 1976 with a degree

in business and economics. She was awarded the Banca Nazionale del Lavoro's Arturo Osio fellowship and took an M.A. in Economics from Columbia University in New York.



MAURIZIO SELLA

Chairman of Banca Sella Holding, holding company of Gruppo Banca Sella, as well as of Banca Sella, of Banca Patrimoni Sella & C. and of Maurizio Sella S.A.A., the family holding

His other present appointments include: Chairman of ASSONIME, Board member of the Italian Association of Banks (ABI) and member of its Executive Committee, Board member of the Fédération Bancaire de l'Union Européenne (FBE) and “alternate” of the Chairman Frédéric Oudéa in the Euro Retail Payments Board (ERPB), Board member of Buzzi Unicem and Chairman of its Control and Risk Committee, member of the Council for the U.S. and Italy and of its Board, member of the Italian Group of the Trilateral Commission, Chairman of Istituto Luigi Einaudi (Istein). In 1991 he was conferred the honour of Cavaliere del Lavoro by the President of the Republic of Italy. He is member of the National board of the Partito Democratico (Italy), since 2008.



BERNARD SPITZ

President International & Europe, MEDEF; President, French Federation of Insurance – FFA

Bernard Spitz is the President of the French Insurance Federation (FFA) which gathers the French Federation of Insurance Companies (FFSA) and the Association of

Mutual Insurance Companies (GEMA) since 8 July 2016. Mr Spitz was the chairman of FFSA since 2008. A Board member of MEDEF, the French employer's organization, Bernard Spitz has chaired International and Europe since July 2013. From the 2011 French Presidency of the G20, Bernard Spitz has represented MEDEF and worked on the B20 Task Forces related to employment and the financing of growth. Bernard Spitz is a graduate of the Institut d'Études Politiques de Paris and the École supérieure des Sciences Economiques et Commerciales (ESSEC), as well as of École nationale d'administration (ENA) from 1984 to 1986. He was an adviser to Prime Minister Michel Rocard from 1988 to 1991 ; a Maître des Requêtes at the Council of State ; and an executive Director at the head of Canal+ from 1992 to 1996. From 2000 to 2004, he was Chief Strategy Officer of Vivendi Universal. Bernard Spitz has served as a rapporteur to the French Competition Council, a member of the French Economic and Social Council and of the Security Council. He has overseen a number of public reports and efforts, among which President of the Diversity In Media Committee (2010); Coordinator of the Estates General of the Print Media, commissioned by President Nicolas Sarkozy (2009); and in charge of the 50th anniversary celebrations of the Universal Declaration of Human Rights for Prime Minister Lionel Jospin (1998). Bernard Spitz sits on the Policy Board of the Aspen Institute (France), and is a member of several leading European think tanks, including Astrid (Italy), The Lisbon Council (Belgium) and En temps Réel (France). Bernard wrote several books on how to reform the State, including *Notre Etat (In Our State)*, with Roger Fauroux, published by Robert Laffont in 2001; *C'est possible ! Voici comment... (It's possible : Here's How)*, with Michel Pébereau, published by Robert Laffont in 2007 ; *Le Papy Krach (The Grandfather Krach)*, published by Grasset in 2006 and *On achève bien les jeunes (Our children betrayed)* published by Grasset in 2015.



KOSTAS G. STAMOULIS

Assistant Director-General a.i. of the Economic and Social Development Department at the Food and Agriculture Organization of the United Nation

Kostas G. Stamoulis is currently the Assistant Director-General a.i. of the Economic and Social Development Department at the Food and Agriculture Organization of the United Nations. He served as Director, Strategic Programme Leader, Food Security and Nutrition in FAO. He led through 2015 the design and provided strategic guidance of FAO's Strategic Programme on Food Security and Nutrition which cuts across

several disciplines and geographical regions. Between 2008 and 2015 he was the Director of the Agricultural Development Economics Division of FAO. ESA carries out the bulk of analytical and evidence-based policy work of FAO with about 150 staff members. From 2007 to 2015 he has been the Secretary of the Committee on World Food Security (CFS) and played a key role in the reform of the committee. Since joining FAO he has held progressively responsible technical and management positions. Before joining FAO in 1989, he was Assistant Professor of Agricultural Economics at the University of Illinois in Urbana Champaign. From 1985 to 1987 he was a post-doctoral fellow at the University of California at Berkeley. His work includes issues related to the role of agriculture in rural development and rural poverty reduction in developing countries; the impact of changes in food systems on smallholder farmers and on rural poverty; the linkages between the agricultural sector and the rural non-farm economy and the integration of food security and nutrition in sectorial policies and programs. He has also carried out work on the assessment of the role of macroeconomic and exchange-rate policies on agriculture and the rural sector and the interdependence between exchange rate, financial and commodity markets. He has published a large number of papers, articles, books and monographs on a variety of subjects. He holds a degree in Economics from the Economics University of Athens (Greece), a Master's Degree in Agricultural Economics from the University of Georgia (USA) and a Ph.D. in Agricultural and Resource Economics from the University of California at Berkeley.



DOMINGO SUGRANYES BICKEL

Chairman of CENTESIMUS ANNUS – PRO PONTIFICE Foundation

Born 29 April 1945 in Fribourg (Switzerland). Spanish nationality. Resident in Madrid. Married to Cecilia Foletti Moschini – 3 daughters and 11 grandchildren. Graduated from the University in Fribourg, Switzerland (Licence en Sciences Économiques et Politiques). Training periods in Barcelona, Geneva, Madrid, London, Rome. Active from 1969 at UNIAPAC (International Christian Union of Business Executives), Brussels. Secretary-General from 1974 to 1981. From 1981 with MAPFRE insurance group in Madrid, Spain; at the beginning of the group's international development. Responsibilities in Reinsurance, Credit and Guarantee Insurance, Corporate Finance and Investors Relations. Managing Director in charge of CORPORACIÓN MAPFRE, the public listed holding controlled by MAPFRE MUTUALIDAD. Since 2000, Mem-

ber of the Group Executive in charge of Finance. After completion of the demutualization process, Executive Vice-Chairman of MAPFRE Group until retirement from executive office in 2008. Member of the Board of FUNDACIÓN MAPFRE and of several group subsidiaries until April 2015 (statutory age limit). Member of the Board of SOCIETÀ CATTOLICA DI ASSICURAZIONE, Verona, Italy. Past-President of UNIAPAC, International Christian Union of Business Executives (1997-2000). Since 2009, Chairman of FONDAZIONE CENTESIMUS ANNUS – PRO PONTIFICE, The Vatican.



GABRIELE TODESCA

Head of NPI Platform, European Investment Fund – EIF

Mr. Todesca joined EIF in 2006. He served as Associate at Francisco Partners and Soros Fund Management. He has worked as Analyst at Citigroup. Mr. Todesca holds a degree in Law from the University of Trento and a Master of Laws in Banking and Finance Law from the London School of Economics.



ARCHBISHOP SILVANO M. TOMASI, C.S., PH. D.

Apostolic Nuncio, Delegate Secretary of the Dicastery for promoting human integral development, Holy See

Archbishop Silvano M. Tomasi's formative education was both in Italy, where he was born in the Veneto region in 1940, and in New York, where he studied theology and was ordained a priest in 1965. He holds a masters' degree in social sciences and a doctorate in sociology from Fordham University in New York. He was assistant professor of sociology at the City University of New York (Richmond College, City Col-

lege) and at the New School of Social Research (1970-74). As founding Director of the Center for Migration Studies, Inc., of New York, he established and edited the quarterly journal *International Migration Review*. He carried out pastoral work in the New York area and served as Provincial Superior of his religious Congregation, the Missionaries of St. Charles – Scalabrinians. He has published books and articles related mostly to migration issues. From 1983 to 1987 he served as first Director of the office of Pastoral Care of Migrants and Refugees (PCMR) of the United States Conference of Catholic Bishops (NCCB/USCC). From the end of 1989 to his appointment as Archbishop and Apostolic Nuncio on June 27, 1996, he served as Secretary of the Pontifical Council for the Pastoral Care of Migrants and Itinerant People, a department in the Roman Curia. From 1996 to 2003 Archbishop Tomasi served as Apostolic Nuncio to Ethiopia, to Eritrea and to Djibouti and as Observer to the African Union, formerly the Organization of African Unity (OAU), whose headquarters are in Addis Ababa. During his tenure, among various initiatives undertaken, began the Catholic University of Ethiopia. In September 2003 Archbishop Tomasi began his service as Permanent Observer of the Holy See to the United Nations and Specialized Organizations in Geneva and to the World Trade Organization, a responsibility he carried out until the beginning of 2016. The Cambridge University Press is publishing a selection of Archbishop Tomasi's interventions.



JONATHAN WATSON, PHD

Managing Director, INTEGRATE; Executive Director and Founder of Health ClusterNET (UK)

Stichting INTEGRATE is a think tank focused on practical thinking for long-term investing in innovative social infrastructure across EU regions (2012+). It is a member of the Secretariat (with CDP, COM, EIB, ELTI and CEEP) for the High-Level Task Force in Financing Social Infrastructure while Maximising Public Value. It will also act as rapporteur and knowledge lead for the two Working Groups of this exercise that will report in December 2017. INTEGRATE has also been a co-promotor and contributor for the annual Rome Investment Forum: Financing Long-term Europe hosted by FEBAF since its launch in 2014 and Health ClusterNET is a non-profit R&D performing SME with a focus on optimizing value chains for health and innovation. As part of this, HCN has been and is a partner in relevant EU funded projects. HCN led the EUREGIO III project that assessed the use of Structural Funds for health care

investment. The evidence from this informed the EU Council Conclusions Towards Modern, Responsive and Sustainable Health Systems (6 June 2011). Additionally, Jonathan is commissioned to co-write major transnational research and innovation action proposals that focus on improving the diagnostics and treatment cancer care; he has been an external expert for DG REGIO and is an external evaluator for H2020 and the EU Health Programme 2014-2020. He was an Honorary Professor (2010-2013) and Special Professor of Health and Public Policy (2001-2010) at the School of Community Health Sciences, University of Nottingham and a Visiting Chair in Healthy Public Policy at the University of York (1999-2001). He did the formative work for an Erasmus Mundus funded European Master's degree in Sustainable Regional Health Systems (launched 2008) and has published several books and articles.

ANNEXES

THE EUROPEAN COMMISSION'S MID-TERM REVIEW OF THE CAPITAL MARKETS UNION

FeBAF Contribution to the public consultation

In response to the European Commission's call for feedback and suggestions on the progress made in the Capital Markets Union (CMU), and in preparation of the Mid-term Review of the corresponding Action Plan, the Italian Banking Insurance and Finance Federation is glad to provide its input, bringing together the views of the different organizations affiliated to FeBAF that represent the main business associations of the Italian financial sector.

In the CMU Action Plan (September 2015), it was clearly stated that a Mid-term Review would have to be undertaken to assess the progress made and the achievements obtained so far, and at the same time single-out remaining gaps and new challenges. We think that this Mid-term Review takes place at a critical and delicate time for the EU, and therefore welcome the opportunity of having an in-depth discussion on CMU, and being able to participate in it.

The topsy-turvy world of CMU: an in-depth rethinking and a substantial re-orientation is required.

The CMU is one of the most ambitious and significant projects of the EU. It is a fundamental component of the European reform plan to re-launch investment, growth and jobs in the European economy, and marks a leap forward in achieving the Single Market and promoting social and economic integration.

We concur with the Commission's view that "the CMU pipeline is delivering" and express satisfaction for the initiatives of the Action Plan that have already been completed or are in the process of completion. We appreciate that European institutions show great attention to alternative investment tools, as demonstrated by the EuVECA Regulation and the AIFM Directive. However, we believe that it must be recognized that the context within which the project was designed and initiated has profoundly changed, and that those changes affect not only the implementation of the Plan, but above all the concept itself and the strategic orientation of the CMU. This has happened to such an extent that much more than a simple mid-term review is now required. Rather, an in-depth rethinking of the aims, objectives, time-table and priorities of the CMU should be undertaken.

When we talk of unprecedented changes in the context, we obviously refer to Brexit in the first place, which is taking out of the EU framework the most important financial center of the EU to date, i.e. the City of London. Other important novelties have upset and turned upside down the whole picture of capital markets in Europe, and their prospects for the future. These unanticipated and unsettling developments

must be accounted for, and taken into consideration. Moreover, the CMU was meant from the start to be a European process moulded and inscribed in a global framework, as it was directed at promoting wider financial integration in the global economy, open economies and societies. The new Trump administration in the U.S. appears to be challenging the long-term tenets of global finance, alongside with trade liberalization and transatlantic relations. This is also a factor that should lead to a fundamental resetting of CMU.

Recently, and significantly, the President of the ECB Mario Draghi reaffirmed the concept that deep financial integration (as implied by the CMU) and the single currency are to be two sides of the same coin. He argued that integrated financial markets in Europe would be necessary for an effective single currency. The CMU project therefore not only affects the wide community of the 27 countries of the EU, but impacts more deeply into the Euro-zone. It represents a necessary ingredient for the stability and performance of the Euro-area, as a single currency area. It is a required complement of the Banking Union and an integral part of the inescapable strengthening of EMU. As a matter of fact, the operationalization of Target2-Securities (T2S) by the ECB (2015) should be seen as laying one of the basic foundations for CMU, by providing the necessary market infrastructure. Therefore, the implications of CMU for, and its impact on, the Euro-area give CMU an added component of synergy, consistency and urgency.

For the reasons above, we cannot help giving the *Mid-term* Review a much broader significance, and place it in the context of the revisitation and adaptation of the whole approach, and of the concept itself. CMU needs a new beginning and an overall redesign, moving from CMU mark 1 to CMU 2.0, and correspondingly re-adjust deliverables, priorities and methods of work.

This reconsideration should follow *five basic directions*, summarised below, which will be spelled out in more specific terms and comments in our response to this consultation:

1. *Put institutional reforms at the fore-front.* The first point to consider is the institutional framework, and the need for institutional adjustment at the European and national level. Following the “British inspiration” of the initial approach, CMU was thought to proceed very softly and with great prudence on introducing changes in the institutional architecture and the legislative frameworks. This reflected not only pragmatism, but above all the fact that the City of London, which was evidently going to play the leading role in the CMU, had already developed institutional arrangements capable of providing some of the necessary infrastructure. The basic frameworks therefore of legislation and oversight required by the markets, particularly wholesale markets, were to some extent already operational, and had only to be marginally adjusted and adapted to accommodate the extension of capital markets to the whole of the EU, in areas where they were absent or not well developed. As a matter of fact, we – among others – had already expressed some doubts and hesitation on accepting the dominant view at the launch of CMU that the issue of simplification and consolidation of the com-

plex and baroque architecture of 27-28 different legislations and institutional frameworks were to be put on the back-burner. The assumption then was that the market itself should be able to adopt the best practice in terms of institutional performance, and operate accordingly. However – we objected – if the market could accomplish the CMU by itself, it would have already done so. In other terms the market is imperfect, and only institutional reforms can correct for market imperfections and thus eliminate institutional obstacles and barriers, particularly cross-border. A similar line of reasoning was put forward in the Five Presidents' Report. After Brexit, the issue of institutional adequacy takes on a sense of much greater momentum and significance. The risk is in fact, with the UK out of the EU capital markets institutional infrastructure, that fragmentation, duplication and overlap severely hinder the operation of capital markets, creating greater obstacles (and higher costs) to capital market development, particularly where it is most lacking and needed, and notably for cross border operations. Think for instance of the convoluted system of oversight for capital markets in Europe that would result from Brexit. The issues therefore of regulatory harmonization and supervisory convergence for European capital markets become a priority, particularly for the Euro-area. More in general the CMU financial institutional architecture becomes highly relevant to insure a consistent regulation and oversight of critical financial infrastructures after Brexit, and reconcile regulation with financial innovation and sustainable growth.

2. *Multiple speeds capital markets integration: Euro and non-Euro.* The reform of the institutional arrangements for an effective CMU would also benefit from a more flexible (variable geometry) pattern, such as the *two or multiple speeds approach* suggested by Chancellor Merkel and other European leaders. However, this should not be a way of crystallizing double standards or fragmenting the single market space. The CMU should remain a project open to all the 27 countries of the EU, as it was originally conceived. But its design and implementation would have to reflect both the Euro and the non-Euro possibly different requirements, the willingness of different countries to cede prerogatives to the European levels, and the different speeds of individual countries in getting ready for accessing higher and higher levels of institutional integration.
3. *A level playing field of uniform norms and regulation across the single capital market space.* The other area where a change of pace and priorities is required is that of regulatory convergence. The notion of a “single rule-book” was inscribed from the beginning in the role and mandates of the EU financial regulatory authorities. However, insufficient progress has been made on creating a really level playing field of norms and rules, considering the number of players involved (the several national regulators), the wide-spread practice of gold-plating and the comprehensible reluctance of individual agencies to give up their specific national or sectoral prerogatives. In the end, therefore, the “single rule book” principle has become nothing more than a myth, or a polar star to enlighten the complex and tortuous road of intergovernmental and inter-agency coordination. In this context, the appearance on stage of the Banking Union has marked a definite U-turn.

Consolidating the different supervisors into a single mechanism, and standardizing the various national and local practices has given a strong push toward the simplification and the harmonization of the regulatory space. The Italian financial community has greatly appreciated the simplification and harmonization implied by the SSM, but it has also lamented that the normative framework for Banking Union has not yet been adjusted correspondingly. Hence the demand that “Testi Unici” at the European level – the Italian formulation of the “single rule book” philosophy – be enacted in all areas relevant for banking operations. The European Commission in its 14 September Communication has rightly called for an acceleration of reforms, and has recognized the “need to speed up the legislative process”. We appreciate that in the above-mentioned Communication the Commission has reaffirmed its commitment to the CMU. We appreciated also that as a consequence, and considering the new scenario, the Commission has reviewed its priorities and shown a new thrust towards bolder legislative and harmonization initiatives. Concrete examples of such a more ambitious and more effective approach can be found in the September Communication: for instance, the new initiatives undertaken for the harmonization of the fiscal and insolvency frameworks. This new approach – in our view- should be highly commended and supported. It is well known that divergent legislative frameworks, particularly in insolvency regimes and around tax barriers, represent major obstacles to (cross-border) capital market development. In the field of the fiscal treatment, the advantages offered to debt vis-à-vis equity are a major obstacle to equity investment, risk-sharing, and more broadly financial stability itself. Europe continues to be characterized by excessive levels of debt. Moreover, the negative interest rate environment has exacerbated this problem. As, in principle, fiscal affairs are issues of national responsibility, efforts of fiscal harmonization have proceeded very slowly in the past, often without tangible results. Therefore, the Commission’s proposals for an integrated European approach to corporate taxation mark a significant break-through and an instance of bold and effective reform. The same should be said of insolvency regimes: achieving a consistent and harmonized framework at the European level in this field would give a formidable boost to cross border deals and improve the effectiveness and timeliness of jurisdiction by national courts.

4. *Safeguarding the diversity of the financial eco-system: the principle of proportionality.* This fundamental approach that can be dated back to the Prussian times had been until recently neglected and ostracized in Europe, creating obstacles to the operation of small financial institutions, which in many countries play an important role in local communities, and a competitive disadvantage with those countries, like the U.S. where proportionality is highly respected, including in legislation and regulation. Recently, the issue of proportionality has gained wider support in Europe, as indicated also by the European Commission. It must be recognized that proportionality finds greater recognition and support in some countries, like Germany or Italy, but also in the European periphery. Moreover, an application of this principle would benefit start-ups and fintech, and promote therefore financial innovation.

5. *Putting ordinary citizens first: the focus on retail markets.* A fifth direction to consider in the overhaul of the CMU approach is the role of consumers, both savers and investors, in financial markets. We are glad to notice that in the Action Plan one of the six policy areas on which CMU should focus is devoted to “fostering retail investment and innovation”. Moreover, this area appears to move up in the priority scale of the plan. This is the right approach: the ultimate beneficiary of CMU in fact is the European citizen. But this truth is not generally perceived and appreciated by the public opinion and the man of the street. A way to contribute to bridging this gap is by placing much greater emphasis on retail markets. Making capital markets more inclusive, and giving ordinary citizens access to it, should be a top priority of the whole CMU project. We also support the emphasis placed on financial “culture” and education. In this context, specific initiatives of dissemination and information should be undertaken to enable the widest possible picking up of the opportunities offered by CMU. For instance, a “roadshow” on the opportunities offered by CMU particularly for retail markets – consumers and SMEs – could be organized in Italy, and elsewhere, and organisations such as Febaf could offer support to such initiatives. Attention to the interests of “retailers/consumers” is to some extent intertwined with the issue of proportionality, but it can also have a broader application. This focus appears especially relevant in the case of personal pensions and Fintech products, but it could also apply to the mortgage market or advisory services. It must be recognized in this respect that an effective CMU would bring to the fore the issue of competition or competitive complementarity, between markets and intermediaries, an obvious example being that of shadow banking and of securitisation schemes. The balancing of retail vs wholesale and, more generally, the costs and benefits of regulation, and its sometimes-excessive burden, requires pragmatic, concrete and equitable measures.

The comments and suggestions provided below in response to the questions of the consultation span a wide range of policy areas and issues: from regulation (or legislation) to information and reporting; from accounting standards to financial innovation; from financial education to capital requirements, from infrastructure to start-ups and green finance; from consumer protection to financial inclusion.

We provide here a *listing of a few topics raised in the paper*, to give an idea of the breadth and scope of our approach:

- Prudential rules affecting the capacity of banks and insurers to invest in the real economy, particularly SME and innovative enterprises.
- Conditions for encouraging the development of Private Placement.
- Simplification of international accounting standards for SMEs.
- Reduction of administrative and bureaucratic burdens for innovative start-ups.
- Encourage crowdfunding through ad-hoc European platforms and tax incentives.
- Improve and extend the more favorable capital treatment for infrastructure investment.

- Provide Government guarantees to support EFSI investment, particularly by insurers.
- *Explore financial instruments to finance supply chains or clusters of SMEs.*
- Eliminate information overload and duplication stemming from the cumulative application of the Solvency II Directive, the PRIIPs Regulation and the Insurance Distribution Directive (IDD), etc.
- Consider the long-term features of EU personal pension products (PEPP).
- Promote identification at distance through harmonisation of rules, interoperability of systems and common databases.
- Promote portability of data and effective exchange of information across Member States while respecting privacy requirements.
- Diversify transparency rules to focus protection on those investors that most need it.
- Invest in financial education and promote an equity culture among investors.
- Ensure a level playing field in supervisory requirements between traditional financial services and FinTech providers.
- Extended to retail investors suitable products, such as the senior tranche of simple and transparent securitization.
- Promote securitization (particularly by insurers and pension funds) through standardisation, more appropriate calibrations of rules and better information.
 - Promote the establishment of a single market for covered bonds across the EU through the harmonization of quality and information standards.
- Review the treatment of intragroup exposures, recognizing a single European jurisdiction and facilitating cross-border capital and liquidity flows.
- Remove barriers that currently hinder competition, such as tax distortions, different sanctions envisaged by fiscal and accounting prescriptions, and different supervisory practices, etc.

THE INTERIM REPORT OF THE HIGH-LEVEL EXPERT GROUP ON SUSTAINABLE FINANCE

FeBAF Contribution to the public consultation

The Italian Banking Insurance and Finance Federation is pleased to provide its contribution to the High Level Expert Group consultation on Sustainable Finance. This contribution has been prepared in co-operation with our members, which are the main financial associations operating in Italy representing banks, insurance companies and funds. The present consultation is strictly intertwined with the EU Action plan on the Capital Markets Union (CMU), that includes sustainable finance as one of its main pillars and is one of our Federation's main fields of activity at European, international and domestic level. The commitment to sustainability plays a fundamental role in the mission of the Italian Banking Insurance and Finance Federation (FeBAF). Please note that:

- The Federation signed in 2012 a joint declaration with its members. The Charter of Sustainable and Responsible Investment of Italian Finance (see attached) promotes the dissemination of three main principles: 1. Sustainable and Responsible Investments; 2. Disclosure; 3. Medium-long term view.
- FeBAF is a supporter of United Nations Environment Programme – Finance Initiative (UNEP FI) and it's a supporter member of the Principles Responsible Investment (PRI) and of Principles of Sustainable Finance (PSI) of the United Nations.
- FeBAF is supporter member of ARISE, the UNISDR (the UN secretariat responsible for the implementation of the International Strategy for Disaster Reduction) Private Sector Alliance for Disaster Resilient Societies. As such, we are committed to raise awareness with respect to Disaster Risks, aiming at the implementation of projects and activities to achieve the targets of the Sendai Framework.
- In 2015 FeBAF joined the Paris Pledge, the declaration of commitment of the civil society against the climate change, with regards to the 2015 United Nations Climate Change Conference, COP21.
- FeBAF is one of the 160 members of the Italian Alliance for sustainable development (ASVIS). Under its aegis of this alliance FeBAF and other business organizations signed a joint Declaration of commitment on sustainable development.
- FeBAF strongly supports the Italian National Dialogue for the Sustainable Finance which involves Italian Ministries and National Authorities under the leadership of the Italian Ministry of Environment and the involvement of UNEP. We co-chair

a group of experts in order to develop Milan as a hub of the sustainable finance.

- FeBAF organizes periodical seminars dedicated to these subjects, often in cooperation with other associations and institutions, as i.e. the European Movement-Italy, Integrate, and the Italian Forum for Sustainable Finance (FFS).
- Since 2014, the Federation has organized The Rome Investment Forum, an annual international Conference where we host a session dedicated to sustainability, resilience, ethics in finance and impact investing.

Given the above, we feel committed to support all initiatives – including the present Interim Report – aimed at sharing and disseminating a common culture of sustainability, and provide hereby our response to the questionnaire.