

Plan: Global Financial Forum

References to France are on the rise in the English-speaking countries.

(I) Has the world gone French?

Massive government intervention around the world

Historic G20 agreement

The “French touch” at the G20

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Conclusion: Friedman and Colbert

Mr. Chairman, dear Robin Niblett (Chatham House Director)
Lord Turner,
Mr. Duncan Niederauer,
Mr. Stephen Cecchetti,
Ladies and Gentlemen,

When the U.S. federal government stepped in to save Fannie Mae and Freddie Mac in early September, **one Republican Senator** [Jim Bunning, Kentucky] declared: “I thought I woke up in France.” A few months later, **an American editorialist** [Bill Saporito, in *Time Magazine*] entitled an article: “How We Became the United States of France.” Then, this past March, **an eminent British political figure** [Lord Mandelson, Britain’s Business Secretary] praised France’s economic model, even asserting that “We have something to learn from continental practice.” So the question I’d like to ask you today, perhaps slightly tongue-in-cheek, is this: Has the world gone French?

(I) Has the world gone French?

In the last several months, government intervention in the economy has been massive. In its last *World Economic Outlook*, the IMF calculated that the fiscal stimulus packages introduced by the various countries in 2009 were equal on average to 2 percent of GDP. The measures adopted by the French government came to a total of nearly 50 billion euros, or roughly 2.4 percent of GDP – a fairly average figure, then. By definition, these are temporary interventions: it is the job and duty of government to turn on the fire hoses when the system is burning. During his 1936 re-election campaign, Roosevelt denounced the prior administrations for their failure to react and said that the nation had been afflicted with “hear-nothing, see-nothing, do-nothing Government.” Confronted today with a crisis of equal magnitude, we can’t afford to make that mistake. Around the world, governments have heard the complaints, seen the issues, and done what was possible to do in order to stem the crisis. The coordinated plans to stimulate the world economy provide ample proof of that.

What is unprecedented today is the universal consensus on the need to overhaul finance industry regulation.

Embodying that consensus is the G20, and **the number 20 marks a new development in and of itself.** Those twenty countries total 85 percent of world GDP – from the United States to China, from Australia to Brazil, from South Africa to Indonesia, not to mention the European Union. The crisis is global, and it calls for global governance.

But the G20 agreed on more than just governance; they agreed to rebuild the international financial system on more sustainable foundations. In the Leaders' Statement, "major failures in the financial sector and in financial regulation" are described as fundamental causes of the crisis. The G20 issued a separate, 6-page declaration on **Strengthening the financial system**, accompanied by an action plan.

There is unquestionably **a certain "French touch" in the agreement.** I would like to stress that while France held the presidency of the Council of the European Union, President Sarkozy was the one who persuaded the G20 at the Washington Summit in November to include the statement that "all financial markets, products and participants [should be] regulated or subject to oversight." It is our strong belief that efforts to restore growth should go hand in hand with a wide-ranging overhaul of our financial system. Never in the recent history of economics, so few have done so much damage to so many. We can not allow a return to business as usual after such a crisis. I worked with my German counterpart Peer Steinbrück on a number of far-reaching proposals, which were officially adopted at the Franco-German Council of Ministers on March 12th, and endorsed by the members of the European Union on April 2nd in London. The final communiqué contains a large portion of those proposals, so I would now like to review them with you.

(II) Financial regulation of a new kind

Businesses and capital have never been more mobile, and they should stay that way. There is a broad consensus on the need for greater regulation to deal with the crisis. But if that consensus produces nothing but regional and national responses, we might wind up with regulatory fragmentation. In other words, the cure would be worse than the disease, and could even hinder and jeopardize globalization.

The G20 has wisely called for an international regulatory roadmap to address that danger. The approach agreed to is both realistic and cooperative. The G20 will be relying on the international bodies in charge of international cooperation and standard-setting such as the newly expanded Financial Stability Board, the Basel Committee and the IOSCO to ensure implementation of its decisions. Through our trust in these international institutions, we can avert the risk of fragmentation.

A- Systematic regulation.

The first outcome of the G20 Summit is that those who previously operated beyond the scope of international regulation will no longer be doing so. This goes for (1) territories, (2) institutions and (3) individuals.

1. Territories.

It is common knowledge that two thirds of all hedge funds are registered in non-cooperative jurisdictions, often referred to as tax havens. We in the G20 succeeded in getting **the OECD to publish lists of those jurisdictions**. The effect was immediate: a number of countries have made commitments to apply the best standards international standards on the exchange of tax information. It is clearly the beginning of the end of bank secrecy. This has moved a number of countries out of the black list onto the “grey list” of countries that have pledged to implement those standards but have not yet done so.

Those are the countries that the international community needs to monitor and assist in achieving compliance.

2. Institutions: hedge funds and credit rating agencies.

Hedge funds total 1.2 trillion dollars in assets under management; they account for more than 50 percent of market trading volume daily. Now that governments are being called on to support the banks, we must make sure that tomorrow, those banks will not be undermined by entities that are among their most important clients, but about which the authorities currently have no information. For that reason, the G20 will be adopting a specific regulatory framework that requires hedge funds to register and to increase transparency on how they invest, while also monitoring bank exposure to hedge funds. We have tasked the FSB and the IMF to come-up with criteria in order to define the systemic nature of financial institutions, including hedge funds.

We also made **significant headway with regard to credit rating agencies**. They bear more than their share of blame for a crisis provoked to a large extent by the underestimation of risk. They, too, will have to register, and to avoid conflicts of interest, they will be expected to follow an international code of good practice. The credit rating agencies will also be required to differentiate the ratings they issue. The same yardstick clearly cannot be applied to companies, States and structured products.

3. Individuals

Irresponsible compensation policies also contributed to the crisis. The concern here is not with the actual size of bonuses, but with economic governance. The amount of money earned by traders should depend on the ultimate profitability of their trading positions over the medium term. **It was time to clamp down**. The G20 has set clear guidelines that match bonuses for traders to actual performance.

B. More powerful organizations to oversee the new regulatory framework.

The “too big to fail” doctrine has been around for a long time. Since the onset of the crisis, there has also been talk of institutions that are “too big to manage.” But we must now take a look at the “too big to supervise” problem. The challenge ahead involves setting up a system of **international cooperation among supervisors** that offers a comprehensive view of markets and that makes it possible to supervise systemically important transnational financial firms. We have entrusted the Financial Stability Board with this task.

The G20 has also emphasized the need to strengthen our international financial institutions, above all the IMF, whose expanded role will include both monitoring financial risks and supporting emerging countries affected by the crisis. This is clearly a great achievement of the London summit in order to restore confidence globally and we have started this week-end implementing our commitment to provide the Fund with more resources.

We expect the IMF to fulfill **a genuine early warning function in relation to financial risk and macro-economic imbalances**. The Fund should link up with the new Financial Stability Board. These two organizations will be asked to present us twice a year with a global map of financial and economic risk – as the IMF already did last Saturday.

At a bank, sound risk management begins with a high-profile risk manager who reports directly to the CEO. By the same token, now that the IMF has been given early warning responsibility and the Financial Stability Board has been established, the international community finally has an adequate risk control structure that is directly accountable to the G20.

Our institutions will not only be more powerful; they will also be more inclusive. The new Financial Stability Forum has been

enlarged to include the G20 countries, Spain and the European Commission. At the same time, the IMF will be working toward a review of the quota subscriptions of member countries.

C- Progress on prudential and accounting standards.

Lastly, and however technical this point may sound, I would like to mention that we have made unquestionable progress on the road to accounting and prudential standards reform, even though we would have liked to go further.

The G20 Leaders' Statement clearly stresses the need to revise accounting standards to deal with assets for which fair value measurement is irrelevant and with long-term investments. It also calls for the adoption of dynamic provisioning, which requires banks to build up equity reserves during upswings so that it will be unnecessary to raise capital requirements during downswings, when the economy is most in need of credit.

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In *Capitalism and Freedom*, Milton Friedman wrote, “The existence of a free market does not of course eliminate the need for government. On the contrary, government is essential both as a forum for determining the ‘rules of the game’ and as an umpire to interpret and enforce the rules decided on.” It follows that when we strive to establish new international rules and organizations capable of enforcing them, we are in no way attacking the tenets of free market capitalism. In the last analysis, we are simply working to reconcile Friedman with Colbert.