European Principal Group

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Germany´s Presidency of the Council of the European Union 2020 The Financial Markets Agenda

A Presidency in unusual times

Germany has taken the Presidency of the European Union in HY 2/ 2020, and this will be the 13th German EU Presidency and the first after 2007. And whereas any EU Presidency has its own options, in terms of setting the agenda and defining the priorities, and its limitations, in terms of acting as a moderator rather than a partisan, the German EU Presidency comes at a historical moment implying huge extra challenges for the European Union:

(1) The **Corona pandemic** has put both the societies and the economies of the EU member states under an enormous stress. Thus, a further containment of the pandemic as well as an economic recovery that overcomes the deep economic slump caused by the measures to fight the pandemic, will be top priorities for the European Union in the months to come. Against this backdrop, other priorities, including those of the financial market agenda during the German Presidency, had to be redefined.

(2) One other challenge is **preserving the unity of the European Union in a world of increasing geopolitical tensions**. Earlier in the year, an ardent conflict among members states over the launch of “Coronabonds”, a poor disguise for the old plan of launching “Eurobonds”, brought the EU dangerously close to the edge of the abyss. Hence the plans for a 750 bn EUR recovery program at the European level, and new forms of EU budget financing and providing financial assistance to member states are therefore planned to be pushed forward in the context of the motto of the German Presidency “Together for Europe’s recovery”.

(3) The negotiations over the recovery package coincide with the definition of the **Multiannual Financial Framework from 2021 to 2027**, which is a challenge in itself.

(4) With regard to **Brexit** and a further extension of the transition period now being ruled out categorically without a comprehensive trade agreement between the EU and the UK in sight, authorizations to provide financial services from the UK across the EU will very likely stop applying, as the EU and the UK might fall back to WTO rules as the level of agreed cooperation as of 1st January 2021. In some parts of the financial system, the EU will have to decide over **equivalence of financial regulation and supervision in the UK**, and on whether or to what extent, as a consequence, the provision of financial services from the UK will be allowed in the EU even after the end of the transition period. These decisions, tentatively scheduled for the Ecofin Council meeting on 4th November, will prove all the more difficult given the UK government’s stated intention to diverge from EU regulatory and supervisory frameworks in the area of financial services after the transition period and the failed providing of the requested necessary information by the UK government.

(5) Other ambitious projects include the newly announced **European Green Deal**, addressing climate change and environmental degradation by means of a new growth strategy, transforming the EU into a resource-efficient economy where there are no net emissions of greenhouse gases by 2050, the **digital transformation** in Europe**,**

preserving the liberal values of the EU or finding an answer to the burning issue of **migration and refugees**.

The financial markets agenda: The institutional background

All these challenges coincide with the rather sluggish taking office of the new EU Commission after the European elections in May 2019. After the delayed start of the new EU Commission on 1st December 2019, and the confirmation of Valdis Dombrovskis as the European Commissioner for Financial Stability, Financial Services and Capital Markets Union (FISMA), it took many months before the new directors-general were in office – the new FISMA director-general John Berrigan has only been officially appointed on 4th May 2020.

In Germany, the Federal government and, for the work program in the field of financial services, the Federal Ministry of Finance had long prepared for the German EU Presidency. Special task forces and responsibilities in charge of coordinating the EU Presidency have been installed in many Federal ministries, including the financial markets department.

As a consequence of the Corona crisis, the Ecofin Council had switched to digital instead of physical meetings. The German Presidency "inaugural" Ecofin, held on 10th July, setting out the work program for the next 6 months, has also been held via digital technologies. Indeed, the Informal Ecofin scheduled for 11th -12th September 2020 in Berlin might be the first physical attended meeting of the Ecofin Council after the outbreak of the pandemic and could be followed by either more physical or digital meetings. Of these, the meetings on 6th October, 4th November, 1st December, and very likely 17th December, will be crucial for the respective financial market dossiers.

The financial markets work program: Overview

The work program of the German Presidency in the field of financial services is coined by three factors: 1. a new Commission taking office, 2. the new definition of priorities, due to the corona pandemic and its massive consequences and 3. overarching projects, like the European Green Deal or digital transformation, spilling over to the area of financial services.

That a new Commission is taking office is mainly mirrored in the over-proportional number of action plans, or strategies, to be presented by the Commission and to be discussed in the Council, and the relatively low number of proposals for new European legislation. Over HY 2/ 2020, the EU Commission is meant to present I. the Digital Finance Package, including the FinTech Action plan, II. a Renewed Sustainable Finance Strategy and the III. Action Plan on the Capital Markets Union to the Council. On the latter, conclusions from the Council are to be adopted possibly as part of the 1st December meeting.

On the other hand, many dossiers originally scheduled for and to be dealt with in HY 2/ 2020 have now been postponed given the new priorities. The most prominent example of this is the implementation of Basel III, with the deadline for implementation postponed to 1 January 2023, i.e.by one year, by the Basel

Committee on Banking Supervision (BCBS) itself. Other prominent examples include the Review of Solvency II or of the Markets in Financial Instruments Directive II (MIFID II). Rather, the main priorities of the German Presidency in the area of financial services will lie in a further strengthening of the Banking Union, in further advancing the Capital Markets Union (CMU), and in a number of legislative issues in the field of digital finance. One other priority is the continuous fight against money laundering and terrorism financing. Sustainable Finance also remains a priority, but there is not much to be done in this field by the Council in HY 2/ 2020.

Banking regulation and Banking Union

Even if the banking sector has not yet been badly affected by the economic consequences of the Corona pandemic, it is obvious that the stress on the business sector will translate into a sharp rise of non-performing loans (NPLs), probably to be observed from early 2021 onwards, and will thus weigh heavily on the banking system. In June 2020, European legislators have already approved the Capital Requirements Regulation II ("CRR Quick Fix"), with the intention to help credit institutions ease the burden and mitigate the impact of the Corona crisis. It is unlikely that there will be a need for more legislation in this vein during the German Presidency.

With regard to the action plan to tackle NPLs, originally agreed back in 2017, the state of play is to be discussed in the Council meeting on 4th November. Here, whereas a couple of legislative projects have run into difficulties in the trialogue, which will probably not be resolved during the German Presidency, the strive to bring down NPL levels in the banking sectors of member states will very likely suffer a severe set-back as a consequence of the Corona pandemic and the resulting economic crisis. It is an open question whether these observations will provide the necessary tailwinds for a further strengthening of the banking union, including an efficient framework for crisis management and discussions on an European deposit insurance scheme (EDIS), as currently foreseen by the German Presidency. It also hopes to have a first round of discussions on the implementation of Basel III, currently scheduled for the Council meeting on 1st December.

Capital Markets Union (CMU)

One major field of action during the German Presidency will be the relaunch of the CMU project. After the presentation of the Final Report of the High-Level Forum on CMU in the Council on 10th July, the presentation of a new action plan from the Commission is tentatively scheduled for the 6th October Council meeting. There are ambitions to reach conclusions from the Council on the dossier in HY 2/ 2020, potentially as part of the 1st December meeting.

The Wirecard scandal in Germany has triggered a new round of discussions on the adequacy of financial supervision in Germany and Europe. But then, given the painful negotiations over ESA review during the last Commission's term, it is unlikely that any party involved will feel the appetite to bring this dossier back to the table in HY 2/ 2020.

Digital Finance

In the field of digital finance, the German Presidency hopes to reach conclusions from the Council on legislation for a Digital Operational Resilience Framework for financial services, currently scheduled for the 1st December Council meeting. The Commission will submit to the Council the new Digital Finance Package, including the FinTech Action plan, that is very likely to be discussed in the Council as part of the 6th October meeting. Also, a progress report on the intended legislation on crypto assets is scheduled for discussion in the Council in HY 2/ 2020.

Combating money laundering and terrorism financing

The continuous fight against money laundering and terrorism financing is another priority. After the Commission had presented a respective action plan back in May 2020, the German Presidency hopes to reach conclusions from the Council here, thus paving the way for legislative proposals to follow. This would be dealt with by the subsequent Presidency in its first quarter of HY 1/ 2021. Reaching conclusions on this topic is currently scheduled for the 4th November Council meeting.

Sustainable Finance

Sustainable Finance also remains a priority, but there is not much to be done in this field by the Council in HY 2/ 2020. Rather, the German Presidency plans to second the publication of a renewed Sustainable Finance Strategy by the Commission. A first round of discussions on the topic is scheduled for the 1st December Council meeting. Nevertheless Germany hopes to go ahead and issue green bonds to be defined as part of the European legislation in the field of sustainable finance even in advance of the EU Green Bond Standard (GBS). Also, legislation on a revised non-financial reporting directive (NFRD) will not start before 2021.

After the political agreement on the Taxonomy Regulation back in December 2019, and its imminent publication in the Official Journal of the European Union, its implementation is now to be brought about by means of delegated acts, largely relying on the work of the Technical Expert Group on Sustainable Finance (TEG). As an impact assessment is foreseen for the autumn of 2020, and given strong concerns in the financial services industry and the business sector more generally as to whether compliance with the taxonomy as put forward by the TEG will actually prove manageable and feasible, it may well be that a revision of the taxonomy could become part of the EU Commission's renewed Sustainable Finance Strategy.

Other possible issues covered in the renewed Sustainable Finance Strategy can be inferred from the respective consultation document, as published in April 2020: reporting will be an important issue, and the establishment of standards and benchmarks, as well as the issue of sustainability research and ratings and the role of credit rating agencies (CRAs). Also, very likely, the possible integration of ESG factors into the prudential supervision of banks and insurers might come back to the table, an issue which had been highly controversial earlier.

The outlook

Under the German EU Presidency, and with the new EU Commission gathering pace, HY 2/ 2020 is meant to provide major dossiers in the field of financial markets legislation, as e.g. a new agenda on Capital Markets Union (CMU), on sustainable finance and on digital finance, including a fintech action plan. Other important pieces of legislation will start, as e.g. the implement>ation of Basel III. As a result of the redefinition of priorities in the course of the Corona pandemic, other issues have been postponed and might only be taken up in the course of Germany's trio Presidency with Slovenia and Portugal, as the Solvency II or the MiFID II review. Furthermore, all this hinges on the assumption that we will not see a second wave of, or other forms of new rounds in, the Corona pandemic, or more severe repercussions of the economic crisis in the banking and financial system. Both would distract policymakers' attention and work capacity from the financial markets work program as currently foreseen.

Dr. Ansgar Tietmeyer, Partner at Berlin Global Advisors
Dr. Michael Wolgast, Senior Advisor at Berlin Global Advisors

About Berlin Global Advisors

Contact Details

Ralf Welt
COO, Senior Partner and Head of Government Affairs at Berlin Global Advisors

Berlin Global Advisors
Berlin. Hamburg. London. New York. Frankfurt.
Email: ralf.welt@bga.global
Phone: +49 (0) 30 88 47 54 70
www.berlinglobaladvisors.com

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