Treasury Committee

Oral evidence: The economic and financial costs and benefits of UK membership of the EU, HC 499

Wednesday 6 January 2016

Ordered by the House of Commons to be published on 6 January 2016

Watch the meeting

Members present: Andrew Tyrie (Chair); Mark Garnier, Helen Goodman, Stephen Hammond, George Kerevan, Chris Philp, Mr Jacob Rees-Mogg, Rachel Reeves, Wes Streeting

Questions 435 - 509

Examination of Witnesses

Witnesses: **Mark Astaire**, Vice Chair, Investment Banking Division, Barclays plc, and **James Chew**, Group Head of Regulatory Policy and Strategy, HSBC Holdings plc, gave evidence.

Q435 Chair: Thank you very much for coming in to give evidence to us this afternoon. We have quite a bit to get through and there will be a vote at 4 pm, I understand, so we will certainly be ending the session by then, I hope. Can I begin by asking both of you briefly, first of all you, Mr Chew, if it is fair to assume that large internationally active banks like yourselves find attractions in a high degree of regulatory harmonisation?

James Chew: Yes, I think that is true. Harmonisation makes it easier for us. There needs to be some variation between countries to reflect differences in underlying economies, how economies operate and business practices but, in general, harmonisation makes life easier.

Mark Astaire: I would agree with that. I would also say that, in a sense, as a bank we are the servants of our clients and, in the round, harmonisation is an important part of what they do and the way they think about conducting business.

Q436 Chair: By the way, could I just ask each of you if you are here in a personal capacity or if you are speaking on behalf of the institution that you work for? Mr Chew.

James Chew: I am representing HSBC.

Mark Astaire: It is the same; I am representing Barclays.

> **Q437 Chair:** Could I ask you one more question, which is about the degree of discretion at the moment in the regulatory system, given the proposals on maximum harmonisation that have been out there for some time from the EU? The UK is going several steps further with ring-fencing. Do you think that the EU might serve as a brake or might be an opportunity to serve as a brake on ring-fencing? Both your institutions, in various ways, have expressed doubts and concerns about aspects of ring-fencing and the way it is being implemented. Do you support full implementation of those reforms now?

James Chew: Let us start on the question of eligibility of ring-fencing and whether ring-fencing will be going ahead. In general, in the regulatory environment, coming from the Basel Committee and coming through the EU, we have seen minimum standards being established in terms of capital, liquidity, etc. We have not seen the effect of maximum harmonisation at the moment. Actually, the UK has been in a position to do things in a way that it wants to do. It has accelerated the capital regime, it has put in place specific rules for the capital regime and it has done other things, including ring-fencing in the UK.

If we look at the European proposals on ring-fencing, they are different to the UK law, as it is being implemented. They are not finalised yet.

> **Chair:** To put it mildly.

James Chew: Yes. An enormous amount of work has been done certainly in the Council and by the Commission, to accommodate the UK's position on ring-fencing and to enable the UK to have the ring-fencing that it wants to have without creating a double jeopardy. By double jeopardy, I mean having to split the bank once for the UK and then having to split it again to suit the European dimension.

We still have to finish that process. The Parliament has not arrived at its conclusion and that could take some time, but there has been a real effort. The Treasury here and in other member states has been very helpful, in terms of recognising what the UK wants to do and seeking to accommodate it, so that has been very helpful.

Mark Astaire: I make a slightly different point, in the sense that the ring-fencing within the UK is broadly established. As you say, it is part of law—we are implementing it; we are working on it. One of the challenges, not just for our bank but also for a lot of companies where Europe is important to them, is trying to deal with certainties. One of the issues around a Brexit is the uncertainty that is being created, but I would say, at the moment, we are dealing with what we have got. Of course, we are working alongside others to understand what is happening in terms of European legislation. It is one of the challenges of being a British bank that we are subject, potentially, to three ring-fencing regimes, with having a substantial US business as well. That is one of the big challenges for us and other financial institutions.

Q438 Chair: You are now supporting what we are doing and you do not think that EU membership gets in the way of it.

Mark Astaire: None of us who went through the last few years would say that there did not need to be some significant regulatory change.

Chair: I am asking you about these regulatory changes.

Mark Astaire: In the round, we feel that they are appropriate. As with any massive change to the way in which a system is managed, there are going to be some challenges from dealing with it.

Q439 Chair: You want to see it implemented. You do not want the EU to get in the way of it.

Mark Astaire: I do not think, at this stage, that we would say that that was particularly helpful and we certainly would not rely on it. We have to get on with what we have at the moment.

Q440 Helen Goodman: At the moment, there are 34 pieces of legislation in this area, in the European process. I wanted to ask each of you how easy you find it to engage with the Commission when they are making the initial drafting proposals for this legislation.

James Chew: I probably deal with regulation more than Mark does. The process for European legislative proposals is reasonably clear. It is a reasonably long process and we have opportunities to interact at various stages of it, through pre-consultation or informal discussions. We often see Green Papers; we see White Papers, and we can comment on them. We then have the process in the Council and we have the process in the Parliament, so there is a good range of opportunities to interact.

The Commission has been helpful, in terms of creating expert groups to consider particular areas. That is an area where, I feel, if more could be done that would be useful. It is very difficult on some of the technical issues of legislation, for example on clearing and settlement, etc., for officials to understand precisely what is going on. Therefore, it is very helpful.

We are invited by the Commission to have discussions with them. We ask to go and see them. We are members of these expert groups, so there is a working arrangement between ourselves, as a bank that is going to be affected by the legislation, the Commission and indeed the Parliament and, through the member states, the Council on discussing the legislation and the impact of legislation.

Q441 Helen Goodman: That is very encouraging. I was involved in the capital markets directive in 1985, and it sounds as if it is a lot more sophisticated now than it was then. When it comes to the consultations, the length of time varies quite considerably, does it not? We have here an example of something that was 26 days and something that was 142 days. What sort of length of time do you think is appropriate?

James Chew: I can see why it is going to vary depending upon the nature of the legislation and what is being put in front of people. We have to remember that, in the period after the crisis, there was a sense that things had to be done. Standing back from that, what would I like to see as the norm, because it works?

I think three months is a good period, assuming this is a reasonably complicated piece, in terms of being able to take the piece of legislation, understand where it might impact the bank, divvy that out among the people who need to look at it within the bank, get their responses back and collate them, make certain that senior management see it and then get it back to the Commission. You can do that a little faster, but there is an awful lot going on. It is not the only thing we are doing. My instinctive reaction is that three months—90 days—would be a good time.

Q442 Helen Goodman: I just want to ask you how much resource you are putting into dealing with European legislation. Obviously banks are quite well resourced institutions and maybe can deal with this better than some other people who might be interested in this area of legislation. How many people do you have working on this?

James Chew: We have a relatively small central team working on this. One of the things we feel is very important is that you have to get the subject matter experts—the people who are actually going to have to deal with the day-to-day results of this legislation—to look at what it is going to mean. You cannot have those in policy teams; they actually have to be working on the front line.

Helen Goodman: You are pulling people in and out.

James Chew: You are pulling people in and out. You have a central co-ordinating team. Ours is actually very modest; we have about 10 people in London. We do not even have a personal staff in Brussels. Brussels is pretty accessible. We are signed up to the transparency register in Brussels, so we have good access to Brussels. You do not need a lot of people. We have consultants in Brussels who alert us to legislative proposals.

You also have to be quite focused, in terms of saying what things are going to have a specific impact on us and what things trade associations could address. There are matters that, frankly, are best addressed when trade associations can look across a body of banks and get a feel, so you have to be economical and you have to make some decisions about how you are going to deal with those things.

Mark Astaire: There is only one thing I would add to that. I should say that I am not involved on the regulatory side of the business; I am a client person. One of the big efforts being made at Barclays, taking into account what you rightly say has become sophisticated and complex, is to try not to take people from their day jobs of trying to generate revenue to deal with some of these very complex regulatory issues, unless it is absolutely necessary. We are pretty well resourced, relatively speaking. I do not know the numbers, but there are people who are dedicated to this.

As organisations, banks are a lot better equipped, which is perhaps what you were alluding to, than many other very large corporations, in some cases, to deal with European law and some of the changes that might come, in the event that the UK was to leave the Union.

Q443 Helen Goodman: Do you feel that the Commission has adequate expertise or, in so far as there may be deficiencies, they are adequately made up by the expert groups?

James Chew: I would like to see more initial discussion, so that you can bring in wider views. I would like to see more use of expert groups, because they are very powerful. We have seen the use of practitioner panels within the UK as being very successful and members of HSBC have contributed to those practitioner panels. It is very difficult to take a very broad overview and say whether the Commission has enough resources, as opposed to whether the Commission's resources are properly deployed. That is a slightly different question.

Q444 Helen Goodman: It is. You mentioned in your first answer the fact that, after the crisis, quite a lot had to be done more quickly. Has that produced regulation that you are now seeing is perhaps not quite what it could have been? Do you see any problems in the quality of that? Do you think that, yes, it has, but there is nothing to be done about it, because everyone was necessarily in a hurry?

James Chew: If everybody is necessarily in a hurry that does not mean that, if problems are found, you should not try to fix them. For example, at the end of last year, we had been dealing with a very specific regulation within the Banking Recovery and Resolution Directive, on the bail-in of not primary liabilities of debt, but the bail-in of other liabilities and how that was framed. It has proved to be an absolute nightmare, because you are trying to bail in liabilities that are way beyond the scope of the EU—so they are outside of the EU—trying to bail in trade finance liabilities and trying to bail in liabilities that, frankly, are very, very difficult to do. This is not the primary bail-in responsibility; this is very secondary.

When you look at the legislation, it is clearly not framed right. It was due to be enforced on 1 January 2016. The PRA has turned around and said, "We are going to delay that, because clearly this is something we have to look at." When you are trying to get this piece of legislation through—and the Banking Recovery and Resolution Directive, BRRD, is an incredibly important piece of legislation—I imagine, at three o'clock in the morning, whether we have properly defined "other liabilities" is not something that somebody is entirely focused on, when that is the second or third tier of defence on bail-in.

Mark Astaire: The CMU is crucial in that respect, in the sense that of course not all the legislation is right. There is a clear recognition that things need to be re-looked at and that there are unintended consequences, particularly with so much legislation coming through in such a short period. Certainly, as an organisation, we welcome those sorts of initiatives, because it is inevitable that, while they may be roadworthy, performance can be improved if you want. We are very supportive of that initiative and it is crucial.

James Chew: The cumulative impact analysis, which is going on at the moment under Jonathan Hill, is very useful, because it is also drilling down in a very granular way. You have to fill in the form and you have to say which clause it is that you find difficult and why you find it difficult. It is not, "I want a general whinge about things." It is, "Tell me what actually does not work." That is a really good way to go, so I am encouraged. We are all getting better at this as we go along.

Q445 Helen Goodman: One of you, I am not sure which, also said earlier that it is important to have European harmonisation, but it is also important to be sensitive to different national situations. How do you feel the European supervisory authorities manage with that?

James Chew: We know that the European Central Bank is trying to reduce, within the eurozone, the number of national discretions. If I was sitting in their shoes, that is probably something I would be doing, because you are having to deal with a lot of variation. They are going to have to feel their way through that. They are going to have to recognise that the way the mortgage market is structured in one jurisdiction is not the same as the way the mortgage market is structured in another jurisdiction, and they are going to have to think about what the regulatory and supervisory consequences are that flow from that.

Q446 Rachel Reeves: My questions build on some of Helen's about regulation. Particularly I would be interested in your views about to what extent the regulatory market failures that contributed to the 2008 crisis have been mitigated by the financial regulation that we have seen from the EU since then.

James Chew: My view is that we have gone an enormously long way. It is really striking when you look at Governor Carney's letter from the Financial Stability Board to the G20. We have to remember that European legislation is a reflection of priorities that are being set by the G20, established by the Financial Stability Board, established by the Basel Committee and then flowing through Europe. Europe has been pretty good at faithfully reflecting those priorities that have been established.

In his letter to the G20, he says that we have substantially changed the resilience of banks. We now have—I am paraphrasing here—a toolkit for the resolution of globally systemically important banks. The way I see it is that we have made a pretty good job in terms of addressing the issues that arose in the last crisis. He then goes on to say that we have to be alert to new risks; and we have to be alert to the issues that arise from the growth of market finance; and we have to be alert to issues about liquidity and market finance structures.

We have done a good job in addressing the problem that was in front of us. There were things that came out of the G20 that are now in train. There is still work to be done and there is still implementation to be done, but that is on the track. We have addressed OTC markets. We have addressed capitalisation. We have addressed too big to fail. We have to be alert to what else there is. What are the knock-on effects? Where has the market moved on to?

Q447 Rachel Reeves: That makes it sound a little like you are driving the car looking in the rear-view mirror, rather than looking forward, and you are addressing the causes of the past crisis, rather than future ones.

James Chew: Governor Carney is saying that we need to think about what the other things are. I do not think it is something that people are not alert to. We just have to be careful not to build the wall and rely on the wall too much to address the last crisis. We have to think about flexibility, being flexible and continuing to look across the landscape, saying, "What is going on?"

Rachel Reeves: Is that your view?

Mark Astaire: There is perhaps a broader point. The evidence suggests that we have a more stable environment in which to operate, that some of the systemic problems that we had have been dealt with—the recapitalisation of the banks and all those requirements. One of the big focuses now is whether that is so restrictive that we cannot generate economic growth. That is one of the big concerns that our business has and other businesses have. That is as much a challenge to the CMU in creating an entrepreneurial environment as making sure that we do not enter into the sort of crisis that we have.

There is a view that it is more difficult, in some respects, to do business, not just within banks but more generally, post the crisis. That is certainly a big area of focus that both our bank and the sorts of companies I talk to would like to see more of and will, unquestionably, be a big area of debate as we move towards a referendum.

Q448 Rachel Reeves: That was the question that I was going to come on to about the costs versus the benefits. You have already alluded to this, Mark. Some of the costs of those additional regulatory burdens make it harder to do business. Are there any of the regulatory burdens in particular that you feel do that?

Mark Astaire: As we were saying before, the banks are relatively well resourced and set up, to a degree, to deal with regulatory challenges. Clearly, as we were suggesting, there are things that we do not like or that we do not think work as effectively as they might: extra-territoriality and some issues that we deal with that create extra costs. Whether you are talking about clearing, which perhaps is not controversial, or remuneration, which is clearly a lot more controversial, these are challenges that British and European banks have, doing business internationally.

More broadly, there is concern about how you finance businesses effectively in Europe. That is a big factor. People who are running technology businesses look over to the US quite enviously, in terms of the ability to fund outside the banking system. That, to our mind, is a major issue and a major challenge for the CMU. We would hope that it will not be stuck simply in terms of legislation, but will actually free up the market, obviously regulated in an appropriate way.

Q449 Rachel Reeves: Do you think that that difference is a regulatory difference or a cultural difference?

Mark Astaire: It is a mixture of both. There is a culture of entrepreneurialism in the US that is slightly different to the UK and certain European countries. The lack of a securitisation market in Europe is a disadvantage. We all know that it needs to be regulated appropriately; it has its attendant dangers. Again, under the CMU umbrella, revisiting that and shifting it away from the banks as being a source of funding for particularly smaller businesses has to be part of the challenge. It is not the businesses that I deal with very regularly but the SMEs that find it challenging, in a way that they would not in the US.

Q450 Rachel Reeves: You think that has changed because of the amount of regulation that has come in the last seven years.

Mark Astaire: It is the amount of regulation and the ability of banks to lend. It is more difficult. There is not a bank in Europe that is not looking very hard at the returns they are generating. There are some countries where one in four requests for a bank loan is rejected. It is a pretty uncomfortable place to be.

Q451 Rachel Reeves: James, I wonder whether you have anything to say, particularly about bad regulation and legislation in the last few years.

James Chew: There are areas where there have been some unintended consequences. We have seen a real decline in liquidity in markets, and people do not quite understand the role of that, but it has proved to be incredibly important, in terms of getting investors to access markets. That is an area where central banks and the regulators are now going, “Hang on, how did we end up where we are today?”

There are some areas where Europe has been smart. It took Basel and said, “No, I want to support trade finance. I am going to change the capital treatment of that.” It changed the capital treatment on SMEs, so you can encourage things, and those are really helpful. We have some unintended consequences where it has damped down. The regulations will undoubtedly make lending in certain areas much more difficult. We have seen Basel is preparing an approach to standardised risk-weighting models and that, we felt, would have had some pretty material impacts on lending, for example to SMEs. They are rowing back from that now, in the latest proposal that came out in December. That is helpful because, otherwise, Europe would have had some difficult choices to make about whether it goes with a Basel-compliant model or does not. There are some not good things.

There are areas where we have been smart. The CMU proposals show there are other areas where we can revisit it. It is really good that we are revisiting Solvency II for insurance companies and saying, “How are we going to get these guys to invest in infrastructure?” That is good.

Q452 Rachel Reeves: Finally, do you detect a hostility in the rest of the EU to London’s dominance as an international centre or do you think that that is not a problem?

Mark Astaire: I think that is overstated. There may be a difference. I do not spend a lot of time in Brussels talking to legislators or whatever, so I do not have a perspective there, although I would guess that there is probably more of an issue there. Within business, I do not think there is. If you came to Barclays, it is full of people from across Europe. It is an extraordinarily international collection of people. People like working in London. It is an aspirational place to be. One of the reasons we get good people is they all come over; they do their second degrees in London, often financed by their Governments, and they end up trying to get jobs in the City. I think that issue is overstated. How different it would be in the event that we left the Union is a moot point.

James Chew: I do not think there is hostility. There is a respect for London as a major provider of financial services. We have a lot of technical expertise to offer Europe, and people understand that we do this job very well.

> **Q453 Stephen Hammond:** Can I pick up on some of your answers to the questions that Rachel was asking, in terms of unintended consequences, for instance? We will come back to the liquidity crisis in a moment, if we may. But, first of all, financial services is not just banking, and there has been a widespread perception inside the industry and in other areas that the legislative response has been such that all the benefits you laid out about the banking regulation and getting rid of some of the systemic issues have caused some considerable problems in other parts of the financial services world. There has been a general view by Europe that there has not been enough distinction between various parts of the financial services world. I wondered whether you would like to comment on that.

James Chew: It goes back to this issue: we have to remember that financial services legislation starts at the G20, the FSB and the Basel Committee, and flows down. Europe is a pretty faithful interpreter of what is going on there, so a lot of the issues that are coming through there are not European-generated issues. They may come across our desks as European directives, but they were started from principles that were established above that, as it were. The Basel Committee establishes Basel III. That is the thing that has specific impacts.

> **Q454 Stephen Hammond:** For instance, one of the odd issues of it is that you are regarding asset managers as deposit takers, which is an unintended consequence that is directly harming. Wherever it comes from, would you accept that one big unintended consequence of what was put in place is that it has been directly harming pretty successful parts of the financial services industry within the UK?

James Chew: I would agree with that, but I would also say that there are quirks in legislation coming out of every Government. I spent some time trying to deal with the multitude of definitions of “US person” under the Dodd-Frank Act. It beggared belief as to how certain businesses taking place in Australia or wherever could be deemed to be US persons. There are always unintended consequences that come through, and you just have to keep on trying to address those and trying to get to common-sense solutions.

Q455 Stephen Hammond: Do you think there is any chance that the CMU review will reverse some of those consequences?

James Chew: I would hope so. It is a really good opportunity to sit down and say, "Sorry, I really do not understand why we have five definitions of X. I really do not understand why this is set out the way it is. Can we please address it?" As I said before, it is very helpful that it is set at a granular level so that institutions like ourselves, and also the trade bodies, the legal bodies, etc., get down to the thing that we really find does not work, and are not just saying, "Oh, it is all too difficult." You have to get down to the nitty-gritty. The devil is in the detail.

Q456 Stephen Hammond: In the nitty-gritty and the devil in the detail, the Alternative Investment Fund Managers Directive, the short-selling regulations and the money market fund regulations have all been singled out as provisions where technical robustness was compromised by political objectives. In the regulation that we are seeing come through from Europe at the moment or overall, how much political compromise is there against what the regulatory process was previously?

James Chew: I do not think that we have the same level of political compromise that there was at the start with those elements. If you look at the Banking Recovery and Resolution Directive, it is pretty vanilla in some respects. I would say that there is an element of political showboating, if I can call it that, in the bank structural reform. We know that there is a political element in CRD IV, the Capital Requirements Directive, where it was interpreting Basel III, which was a capital directive, but we have an element of remuneration in there. I think that has become less prevalent. This is a very broad characterisation: it is a much more workmanlike job.

Stephen Hammond: We are about to settle the directives on MiFID II, as you are well aware.

James Chew: The question is: are those going to be delayed? That reflects the fact that people are sitting back and saying, "We have to do a job that works."

Q457 Stephen Hammond: You anticipated my question. My question to both of you was going to be: do you think that part of that delay or revision of what is going to come through is because there is a view that, potentially, it is disproportionate or indeed may cause regulatory arbitrage with the US?

James Chew: I am not the world's greatest expert on MiFID II.

Stephen Hammond: You are a greater expert than me, certainly.

James Chew: I think people have worked out that what we currently have on the table is not necessarily going to work as people intended it to work. First of all, there is going to be a delay. The question is whether that delay means adjustments.

Mark Astaire: All I would add—I am absolutely not an expert on MiFID—is that when I talk to my colleagues in the regulatory space within the bank, they would all say it is positive that the CMU is recognising that there may need to be some changes, so that is a good starting point. It really depends more generally, as I can see it, where you stand—

whether you have a positive view or otherwise of the regulators in Europe. Some say that it is all talk and nothing will change, and others say it will be a very sensible process and a very productive one. It has the right leadership and the right intentions, so it is six of one and half a dozen of another. Very often, those views are coloured by a political view as well.

Q458 Stephen Hammond: I would like to ask you two final questions, if I may, Mr Astaire. You alluded to the fact that some of the regulation would compromise or undoubtedly impinge or inhibit economic growth. Do you want to give us some feel of the balance there and what your view is in terms of how much or where?

Mark Astaire: It is a generally held view that, post the crisis, changes needed to be made and, in the main, appropriate changes were made to protect the system. The fact that we still have pretty low economic growth with unbelievably low interest rates is indicative of the fact that the European economies are not necessarily firing on all cylinders. One of the factors is the ability to get hold of finance and seed capital. Crowd funding is something that every household in America understands. In the UK, it is not like that at all.

I am not sure I would blame the legislation. I would blame the fact that we had a crisis and we needed to react to it. We have a relatively slow-growth economy in Europe, although admittedly, in the current environment when we are looking at what is happening in other parts of the world, it is looking a bit more benign and attractive than perhaps it was a few years ago.

Q459 Stephen Hammond: You are right, in that one of the reasons why the previous structures were in place, notwithstanding some of the issues they created, was that they allowed access to capital for economic growth through the late 1980s and onwards. My final question goes back to Rachel's rear-view—as opposed to forward-view—mirror. How concerned are you about the ramifications of legislation causing or partially causing a liquidity crisis, which is likely to be the next economic crisis in Europe?

Mark Astaire: There is always a danger of looking back to the good old days and saying it was much easier then. Of course it was, and we had a crisis. Liquidity is not necessarily a cause for a crisis but, in terms of economic growth more generally, freeing the markets in an appropriate way is—

Q460 Stephen Hammond: Potentially, if you cannot redeem your savings, there could be a run on an institution.

Mark Astaire: Of course. We could create some pretty nasty scenarios, but I will try to be a little more positive than that today.

Stephen Hammond: Many in the asset management or financial services world view this as a potentially highly likely consequence.

James Chew: Liquidity is something that needs a lot of focus. There is a danger that you have liquidity that vanishes at the point of crisis, and we can talk about that. How you create a structure that gives the right level of liquidity, while making certain that the providers of that liquidity are not taking undue risk, is something that we are going to have work through. I would say that it is definitely an area that has to be focused on. I know the authorities are thinking about it because, at the end of the day, it comes back to whether I can get my money today or tomorrow. That is a really important factor.

> **Q461 Chris Philp:** I would like to start by exploring your views on the importance of our European Union membership to London's success as a financial centre. Clearly, we are a globally successful financial centre. Can you comment, perhaps starting with Mr Astaire, on the extent to which you think that our EU membership is an important part of that and to what extent you think it is irrelevant or inconsequential?

Mark Astaire: To start with, I would agree with you that the City of London is a great success story, despite the challenges that it has had. It is one of our leading industries and it is clearly the European leader. London has thrived within the Union. I have to say, I think it will continue to thrive outside the Union, although there will inevitably be some challenges in the event that it leaves. Do I think that, if the UK were to leave the Union, London will not be the leading financial centre in Europe in 10 years' time? No, I think it will.

James Chew: London always had a load of intrinsic advantages: location, language, law, liquidity—all those things. Having access to the single market has undoubtedly bolstered that and enhanced the status of London as a hub. You can look at the number of international banks that are based here and then passporting from here into Europe. I think it has enhanced London's position.

How London's position would sit if there were a vote by the British people to exit would depend very much on the nature of the exit. The position under a soft exit where we are EEA members would be very different to the position under a hard exit. It would depend on the institutional arrangements that are put in place between the EU and the UK.

> **Q462 Chris Philp:** Those mood questions will be addressed by a colleague later. I really wanted to get a feel for the benefits. In terms of the UK's influence on the regulatory issues that we have been discussing already, could you comment on how effective you think we have been at securing reasonable regulation that is in our country's interests within the European Union to date?

Mark Astaire: Going back to the point I just made, London has continued to thrive within the Union. There is a generally held view that we fight our corner pretty well within Brussels, in terms of defending the position of London. That is one point.

The second point would be that the number of Europeans who now work in London is supportive of the case that we make. The fact that there are so many European banks that thrive within London is positive, in terms of us being able not just to represent UK interests, but to represent European interests. One of the concerns that a lot of Europeans have is that the position of Europe as a financial centre would be damaged by a UK exit, because it is the leading force within European finance.

Q463 Chris Philp: An organisation called Business for Britain, which is campaigning for an exit, has written recently that there is a general consensus that the UK's influence over EU financial laws has declined dramatically since 2008. It sounds like that is an analysis that you do not share.

Mark Astaire: No.

Chris Philp: What do you think on that particular point, James?

James Chew: It goes back my point that you have to start at the top of the tree: G20, FSB and Basel Committee. Those are setting a lot of the principal prudential regulations and they are cascading down. The UK has enormous influence at the top of the tree, in the FSB and the Basel Committee. The Chairman of the Basel Committee is the Governor of the Bank of England. As it cascades down and things are worked through the European dimension, we have good influence. We sit on the expert groups. We are consulted on what is going on. We have been quite successful in providing technical expertise and telling people, "Look, sorry, this is how it is going to work," because we are there.

The other thing I would say is that much of the European legislation is of a minimum standard. You have to reflect on the fact that we still have the flexibility to add things on top as well. I am not convinced that that dimension has constrained us as to what we want to do in the UK.

Mark Astaire: When I talk to my German colleagues, they feel that the UK influence is a positive one. We are one of the most entrepreneurial factors within the European debate and they would miss us being around the table, in terms of our ability to influence things, very often more positively than they are perhaps prepared to do on their own.

Q464 Chris Philp: To take an example of where we apparently did not have the influence we might have wished, many of your colleagues may have some concerns about the question of a bonus cap, and probably you do as well. Given what you have just said about our influence in Europe and our contribution to the entrepreneurial culture of the European Union, why do you think we were unable to prevent this bonus cap being implemented? Do you think it was a mistake that it was?

James Chew: Mark Carney's speech in Oxford in October is quite interesting where he looks at the things where the European Union has infringed on the flexibility of the Bank of England to regulate as it wants. No. 1 on his list is the bonus cap, because it reduces this flexibility to claw back remuneration from people and, therefore, to set the right incentive policies.

Q465 Chris Philp: It also fixes the cost base of banks at a high level, and they cannot respond to changing market circumstances. Given those two points, which are very powerful, why did we fail to stop that?

James Chew: Partly, there was a political sentiment in Europe that said we had to do something. Secondly, I do not think that enough time was spent in Europe, not necessarily by the Brits but by other people, in trying to understand what the outcome was going to be. The European machine as a whole just did not predict what the outcome was going to be. I suspect that they are sitting there now saying, "Oh, we did not expect that."

Q466 Chris Philp: A few minutes ago, you mentioned the benefits that you saw flowing from European membership from a financial services perspective. Given that that is an example of a cost, is that bonus cap cost one you are happy to pay as a price for the benefits you mentioned earlier?

James Chew: You have to look it all in the round. Maybe that is something where you turn around and say, "That one did not go too well." There are a lot of other things that are benefits. The problem is that the benefits fall generally and the costs tend to fall individually. Therefore, individual institutions will naturally feel a bit aggrieved if they are bearing the costs and the benefits are quite wide.

Q467 Chris Philp: What do you think about this? Do you take the bonus cap issue as evidence that the UK perhaps is not always that effective at getting its own way?

Mark Astaire: To respond to your first question, there was a political desire to be seen to do something about bonuses, what bonuses really mean and the controversies around that. That is understandable, in a way. If you are a European bank trying to employ people in the US, that is a disadvantage relative to American banks. It is not in London, because they are subject to the same laws but, in America, that is a disadvantage. It is a negative in the broadest sense. Without wanting to get stuck into a debate about remuneration, one of the big challenges for European banks is to be able to compete on an even playing field with what are largely the American banks. Our two institutions are two of the very few non-American banks that are, if you want, competing in the Premier League. Our ability to do so is very important. It is a people business.

Q468 Chris Philp: Finally, Mr Chew, you obviously take a significant interest in regulatory issues. Does it help particularly that a UK appointee, Lord Hill, is serving in the financial services brief, or is the nationality of particular post-holders, in your view, largely irrelevant?

James Chew: Nationality is not necessarily the thing that is important. We have a number of businesses across Europe, so we deal with the French Treasury, the UK Treasury, the German Treasury, etc. We are used to dealing with lots of nationalities, and English, frankly, is the language in which most business is conducted.

What is really important with Lord Hill is to have somebody who is sitting there saying, "We have to review the work that is being done. We have to think about the competitiveness of Europe." It is the approach. In that approach, by the way, Lord Hill is not walking on his own. The Commission as a whole has changed its approach somewhat.

We also talk to Katainen and those guys. It helps a little that he is British, but not a lot really.

Q469 Mr Rees-Mogg: Can I just follow up very briefly on the bonus cap and the short-selling rule, both of which came in from the EU, both of which the UK was opposed to and both of which are disadvantageous? They are not rules, Mr Chew, from the top of the tree; they are ones that the EU chucked in right at the bottom. If we were out, we would not have had to follow them. We could have had our own rules while still being very influential at the top of the tree in the G20 and so on.

James Chew: That is the case. There are some rules that have come in, in Europe, and you have picked out two examples. There have been some good things that have come in from Europe, or people would perceive them as good things. Europe has intervened, as I said, on risk-weighting for trade finance. Europe has intervened on the capital allocation for SMEs. There are some things on one side and some things on the other, and the UK has done a load of things on its own that go beyond the global rules. Yes, you are right to say that these are two things. I guess it is a question of being part of the mix. It would have been better if the short-selling rules had been structured differently. It would have been better if the remuneration rules had been structured differently.

Q470 Mr Rees-Mogg: The UK is thought to be 75% of Europe's capital markets and banking revenue. Why are we taking our rules from the EU? Why do we not do it for ourselves? We are overwhelmingly dominant.

James Chew: What I am trying to say is that there are a very few areas where the EU is deviating from the global agenda and the UK is also deviating from the global agenda.

Q471 Mr Rees-Mogg: Yes, but as we are such an important part of that—75% of the EU's revenue in these areas—our interest is so much greater than other EU member states, yet by qualified majority voting, we have ultimately quite a small say in it, and certainly not 75%.

James Chew: This is a political decision that was made, as I understand it, at the time of the Lisbon treaty that we would accept qualified majority voting. That applies to financial services and it applies, if you are France, to wine and, if you are German, to cars, and various other things.

Mr Rees-Mogg: We are dealing with financial services today. Let us stick with financial services.

James Chew: All I am saying is that that rule applies across all things.

Q472 Mr Rees-Mogg: Let us concentrate on financial services and whether it is in our interest to have our rules on financial services set by people who make up only 25% of the total revenue of the European Union.

James Chew: If the rules that the European Union set out were significantly different from the rules that are established at the global level, that might be a point at which one would want to revisit it. The question is: are they significantly different?

Mr Rees-Mogg: The bonus cap and short-selling rule are both significantly different. Mr Astaire has already said that it is difficult for EU-based banks to employ people in the United States.

James Chew: One has to look across the whole body of rules and there are an awful lot of rules that are the same. This is a question of balance.

Q473 Mr Rees-Mogg: It is the rules on the margin that make the difference. Let us come to one that may be very importantly different, and that is the financial transaction tax. Mr Astaire, let me bring you in. Incidentally, I ought to remind people of my interest as a chairman and shareholder in an investment management company, which is not relevant to my particular questions, but has been relevant to some of today's business. Mr Astaire, the financial transaction tax.

Mark Astaire: It is a simple answer. If you want the ambitions of the CMU, it is not helpful. It is not good for liquidity; it is not good for the markets.

Q474 Mr Rees-Mogg: If we are in the European Union and there is enhanced co-operation among a minimum of nine member states, a transaction by an entity based in one of those member states that takes place through London would be subject to the financial transaction tax. If it took place through Singapore, it would not. Can that be in the interests of the City of London?

Mark Astaire: The simple answer—the yes/no answer—is no, but I would take a similar line to James that one perhaps has to see it rather more in the round. For a lot of financial people—though I recognise there is a difference between the fund management industry and the banking industry—being part of the European Union is, in the round, a largely positive thing for business.

Q475 Mr Rees-Mogg: What evidence is there for that—facts, rather than just bold assertions?

Mark Astaire: I talk to a lot of business people. I have not gone through polling; there is nothing scientific about it. In the main, I have two levels of conversation with business people. If it is purely an economic one, they would say, "In the round, we think we should stay in." If you broaden out the conversation into some other broad, political issues—

Q476 Mr Rees-Mogg: I was not really asking for your conversations with your friends. Even the opinion polls get it hopelessly wrong and they are far more scientific. You made the assertion that economically it was beneficial. Can you point to pounds, shillings and pence—or even euros—where this has been an advantage to the UK specifically?

Mark Astaire: I would answer the question a slightly different way, if I may, which is to say that London has thrived as a financial centre within the European Union. Now, that is not to say that there are not rules that we think are unhelpful, both to the UK and also to the European economies more generally, so I am not disagreeing with you; I just think that London's—

Q477 Mr Rees-Mogg: Thank you. That is helpful on that point.

Mr Chew, you mentioned that London had lots of European banks in it and this was part of being in the single market. I seem to remember going back to 1987, before the single market had become functional, that there were already 100 international banks in London. I remember this because one of them closed, and it went down to 99 after the crash in October, which I think was the Wells Fargo bank, but I would not swear to it. It was quite a long time ago. Does this not show—as I think one of you said slightly earlier on—that the City of London had been remarkably successful at doing business globally before the European Union was regulating it, and is quite capable of carrying on with its success that predates the single market?

James Chew: There is no doubt that London has been successful for a long, long time and we have a series of intrinsic advantages that have helped London. We can go through location, language, law, liquidity, etc. We need to reflect on the fact that opening access to the single market through London has enhanced those. It has made them stronger. It has enhanced those hub effects.

One also has to understand that some of those hub effects will deteriorate over time. Language is becoming less of an issue, as everybody speaks English. Location is becoming less important, as we see things being done in the digital space. Lots of people can write things under English law, under New York law or whatever. The hub things that have made London great are not eternal, and the advantages that have been granted by access to the single market have helped to bolster that and, in some respects, meant that those hub effects have perhaps endured for longer.

As to your question about pounds, shillings and pence, I can send you our economists' work, but I am not an economist and it takes an economist to look at what the economic effects are.

Q478 Mr Rees-Mogg: I was asking Mr Astaire, because he said specifically that there were these benefits, and I just wanted to find out whether there were. It turned out it was his mates in the pub, and that is great. Hold on, I want to continue, Mr Chew. Thank you for that. That is a very helpful answer and I accept what you are saying about the hub effect.

What I might suggest is that one of the things that helped us greatly to recover post-war was the Eurodollar market. The reason that that was such a success was because we had different, more flexible regulations than the US, which would have been the natural market otherwise. I seem to remember it was a Kennedy regulation that changed the terms of trade and moved the business to the UK.

Would it not therefore follow that, if we have flexible and intelligent regulation, that is going to be the one advantage that will remain in our hands even when the French are all speaking English and Greenwich mean time has been merged into continental European time?

James Chew: That assumes that what we are talking about is a discussion between European financial centres. You talk about the Eurodollar market; that was between the US and the UK. You have to see London as part of a series of global hubs with a European extension to it, rather than just as a European hub. Europe has to be concerned about the competitive position of Europe, both in financial services and in everything else it does. I think that Europe is aware of that. Europe is aware—

Q479 Mr Rees-Mogg: That is a completely different argument. It is a very interesting one, but it is a different one. That is saying that Europe recognises that it is uncompetitive and needs to make itself more competitive, but in the process it can be making the UK—which is more lightly regulated—less competitive, and what we should be looking at is the interest of the United Kingdom. I absolutely agree with you: it is not about being a European hub; it is about being a global financial centre, and therefore having regulations that people around the world are willing to trust and deal with, rather than a narrow European sphere that I think you are looking at.

James Chew: What you may be saying is that the UK could not rely on European regulators—

Mr Rees-Mogg: To become more competitive.

James Chew: —to look after the competitiveness of the City in a global sense.

Q480 Mr Rees-Mogg: We have a much better chance of doing that for ourselves.

Mark Astaire: But we have done that. Leaving my friends to one side for the moment—

Mr Rees-Mogg: I am sorry about that.

Mark Astaire: No, it is absolutely fine. I also can go back to 1988. A lot of those European banks were two men and a dog. They were very small institutions and I am sure that the number of people that European banks in London employ is massively greater. I could not put a figure on it, but I am sure that that is the case. London has thrived despite some of the issues, and one of the reasons why it has thrived is our ability to access European talent, and to have very often the securities head offices of banks in the City. There are clearly some negatives but, going back to the question of whether Europeans are jealous of our position, I do not think that is the case. It is an aspirational place to work. It is the right place to work, and the fact that it is so easy for someone simply to get on their EasyJet plane, fly into London and work here is a big positive.

Q481 Mr Rees-Mogg: Accessing European talent is a very interesting point, because, as it has become easier for Europeans to come here and work, we have made it increasingly more difficult for non-Europeans. Unless you become

Governor of the Bank of England, it is quite hard to get a work permit if you are Canadian. We are therefore cutting ourselves off, because so many people have come from Europe that the only bit we control is the non-European immigration, and therefore businesses are finding it harder to employ the talent they want from India, China or even the United States.

Chair: Do you agree with that, witnesses?

Mark Astaire: Certainly not. That is not my experience in banking.

James Chew: We have a range of talent from all over the globe, so I do not—

Q482 Chair: The point that Jacob is making is that you will have trouble in future.

Mr Rees-Mogg: Getting a work permit for an Indian.

James Chew: That is not something I am aware of. The HR department deals with work permits, sorry.

Mark Astaire: It is certainly a lot more difficult to get an Indian or an American to come and work here—

Mr Rees-Mogg: Thank you, so we are cutting ourselves off.

Mark Astaire: But it is by no means impossible. It is probably easier as an American to come and work in London than it is as a Brit to go and work in New York, for instance. I am not convinced that we are cutting ourselves off.

Q483 Chair: We will move on for the time being; other colleagues will be wanting to get in. I just want to clarify one point, Mr Chew. When you talk about the access to the single market bolstering the other advantages—law, location, time zone, language—again, what is really the evidence for that? What is the evidence for the fact that we are getting business that we would not otherwise get?

James Chew: It goes back to what I see, and maybe it is my anecdotal view, having worked in the City for a number of years, of more international banks being based in London but having a perspective that looks out across Europe. There are a lot of people who see EMEA—

Q484 Chair: To be fair, you have not really answered Jacob's point—that they were there before.

James Chew: It is a question of the scale of their operation, etc. It is a different scale of operation, and people see Europe as a region rather than the UK as a region.

Chair: To pursue this a bit further, Mark Garnier.

Q485 Mark Garnier: Yes, I would very much like to pursue exactly this. You talk about Europe being the destination, as opposed to the UK being the destination. The experience I have had—I am curious to see if both of you have had the same experience—is that whenever I go, for example, to America, China, India or wherever and talk to people about the UK and its value to the rest of the world, the sense I get is that the UK is seen as a gateway to Europe, not necessarily a destination in Europe in its own right. Does that concur with your experience?

James Chew: There are some areas where the UK is a destination in its own right, in terms of some of the markets we provide. We have by far and away the deepest and most liquid market in foreign exchange, for example. In that case, it is a place where people want to do business because they will get very good prices, etc. We are a destination in our own right for certain elements of the financial services industry, but we are also a gateway. We are both: a gateway to Europe and a destination for certain things. I suspect that that is the case for other industries as well as financial services.

Q486 Mark Garnier: Mr Astaire, funnily enough, I am very interested in the comments of your chums whom you chat with. You run the corporate broking side of Barclays, as a result of which you, I would hope, would spend a great deal of time talking to a number of counterparties, institutions and clients—a great many people who use the City of London and use your services. You have already said that you are canvassing them on a very informal basis. I suppose it depends on whether you are talking to a market counterparty or a corporate, but how do they feel about the City of London and financial services, in terms of it being part of Europe? Do they think it is important? Do they think that London will lose out as a result of coming out of Europe, or the other way round?

Mark Astaire: Not to avoid answering your question at all—

George Kerevan: We will assess that in a minute.

Mark Astaire: —but I would make the general observation that certainly corporates, and indeed market practitioners, are a lot less interested at the moment in this debate than one might expect or hope, as a general observation. The level of knowledge, I would suggest, even among pretty sophisticated people who look at screens all day, where the global economy is crucial to the work that they do, is at perhaps a disappointing level. To that extent, if in a very small way we can help along those lines, that is a good thing.

I would say, partly answering your first question as well, because London is universally recognised as the European financial hub, in financial services alone a lot of people see London as a destination. If you are sitting in New York and you are saying, "I am going to go and work in London," that is seen as being, if you want, a prestige appointment at the moment, whereas going to work in most other financial centres is not seen as being as significant or necessarily as important. But I would guess it is a very different thing if you are sitting in Tokyo and thinking about the car industry: you are probably thinking of the UK as a gateway more than a hub.

Q487 Mark Garnier: Mr Rees-Mogg made a very interesting comment about two rules, which I happen to think are perhaps the most unhelpful rules that have been brought about by the European Union: the bonus cap and the short-selling rule. The bonus cap probably increases risk within banks by increasing costs, as people have to raise base salaries. It was a very foolish and very political move, driven by a Belgian MP, if I remember rightly.

I think Mr Rees-Mogg's point is exactly right, but here is a slightly counter view on that. If we are doing 75% of the transaction value in Europe in London and we are a global financial centre, is it not fair that, in order to make sure we continue to be a global financial centre, we need to have quite a keen eye on the rules being driven by those people whose money we are transacting? If you are a European—let us say BMW—and for one reason or another you want to use the UK capital markets, is it not perfectly acceptable that you would expect to have some recognisable form of rules in the UK? The same pretty much applies if you are American, Chinese or wherever you come from, in that being a global hub means that you have to take inference from global rules to meet the expectations of those people who use the City, as, James, you will know.

Chair: Given that time is pressing, crisper questions and answers would be appreciated.

James Chew: I do not disagree.

Q488 Mark Garnier: I have a couple of questions, more specifically on the City itself. While the City or financial services seem to be pretty keen generally on Europe, there is a bit of a division between those international banks that are here, or banks in general, which seem to be quite keen on it, and asset managers. Hedge fund managers in particular seem to be pretty relaxed about whether we are in or out, since half of them keep moving their domiciles to Zurich and then coming back again when it gets boring. Do you think that is a reflection of who is affected most by the rules and who is less affected? Is there a pattern within it?

James Chew: I could not really comment. I sit in the bank and am very focused on the bank.

Mark Astaire: They are much smaller businesses, in the main. One of the questions is that there is a lot less sunk cost in financial services, in terms of remaining in the UK, than if you put up a car plant. I have already said that I do not think that London is going to collapse whatever happens—far from it, there are lots of other good reasons why London will continue to be successful—but there is clearly a risk at the margin that people will just get up and go, whereas you cannot move your car plant from Sunderland that easily. There is a differentiation, and, within the industry itself, if you are one guy who is the wizard at your hedge fund and you have 10 people who work for you, you can be quite a substantial business, but it is pretty easy to move anywhere.

Q489 Mark Garnier: That is very interesting. I have one last question, which I do not think anybody has really addressed yet. Notwithstanding the economic effect of banks moving in or out of London depending on what the outcome of this election is, if we come out, there will presumably be quite substantial costs in terms of redrawing contracts, redrawing any number of different deals that you may have done, and any regulations that may change. Has either of you done any estimate as to the cost to your institutions of exit, in terms of just the administration of coming out of Europe?

James Chew: I do not think we have got down to numbers. We are sitting here not at the start of the process, but relatively early on in the process. We still have the negotiation to happen, which is ongoing at the moment. We have the referendum, and the British people have to decide. Then we have two years of discussions about whether it is hard or soft, and the outcome of the hard or the soft, talking about the spectrum of exit scenarios, is quite considerable. People might put a wet finger in the air around some of those numbers, but, frankly, we know that under any circumstance it is going to be a very big disruption. I do not think that we have sat down and said, "It is going to cost us X billion pounds to do this."

Mark Garnier: It is pretty substantial, though.

James Chew: Yes.

Mark Astaire: Equally, we recognise that, if the British people vote to leave, there will need to be a lot of work done. We have plans to make sure that, if that is what happens, we know who is going to do what and who is going to look at which, and it will inevitably be an expensive exercise.

James Chew: Part of it will depend on the enabling legislation that is passed to do things, as opposed to what we have to do.

Q490 Mark Garnier: Very quickly, Mr Chew, should we come out of Europe, would that make HSBC more likely or less likely to move its domicile away from the UK?

James Chew: The domicile debate is a totally separate one to the European debate.

Q491 Chair: Mr Chew, you have a head of risk there. He must have spoken to you, as group head of regulatory policy, about whether you have some idea of what structure you would like to see if there was Brexit. You talk about hard and soft, but it is a spectrum, and you must have a view about what you would like.

James Chew: No, I do not think we have a view on what we would like. We have a view on what the position would be in that scenario. I remember having this conversation with a set of accountants, when they said, "There is only an X per cent chance," and I said, "Actually, that is a reasonably big chance. We have to plan for that scenario." Then you plan for that scenario and you plan for scenarios within it.

I do not think it is a question of what we would like. We are not the people here who are going to determine the outcome. It is the British people who decide, and we then have to deal with it. We just sit there and say, "If it is this, this is what we are going to do." This is a political decision.

Q492 Wes Streeting: I am going to continue to develop the theme of life in the event of Brexit. First, you talk about the contingency planning you are doing in the event of a Brexit vote. Do you think it is important that the Government set out, before the referendum, the approach that the Government would take? We have been looking, as a part of our inquiry, at different models, whether it is the Swiss model or the Norwegian model. Do you think it is important, for both the choice of the voters but also your contingency planning, that the Government set out the sort of relationship they would seek to establish in the event of a Brexit vote?

Mark Astaire: Yes. In the event of a Brexit, if you have a clear idea of what the potential parameters are and which are going to operate there afterwards, clearly that would be welcomed. Going back to the Chairman's question, our people do not want to spend too much time arguing over what might be the regime in which we operate outside. They want to be in a position where they try to take a view on what might be the regime and then react accordingly.

Q493 Wes Streeting: You talked about the disruption in that two-year period where discussion about the nature of Britain's relationship with the common market would take place. How disruptive would that market uncertainty be to the UK economy as a whole?

Mark Astaire: One can make a general point that a lot of businesses are innately quite conservative in terms of wanting to have as much control over their business as possible. Brexit is seen by many people as being perhaps in the long-term interests of the British economy, but being an uncertainty that they would prefer not to have to deal with as a leader of a business, because there will be changes, needs and uncertainties.

We saw, in a very narrow way, what happened to the stock market once the YouGov poll came out on that famous Sunday: markets were flying and all of a sudden they went the other way. People are very cautious and nervous about the uncertainty that will be created by a Brexit, even if fundamentally they might think it is the right thing for the country to do.

Wes Streeting: Is that your view as well, Mr Chew?

James Chew: Yes. Uncertainty is the enemy of investment, and therefore there will undoubtedly be some sort of investment pause. Some people will see it as an opportunity, but I would say that the majority will see it as a time to reflect and pause, and wait until they know more.

Q494 Wes Streeting: Some have argued that, on leaving the EU, the UK would still have to abide by all the EU financial services legislation, both now and in the future, if it wanted to retain access to EU financial markets. Is that your view?

James Chew: This is a political question about how the exit is negotiated. If you want to be in the EEA and you want access to the single market, inevitably you are going to have to abide by a whole load of rules that already come from Brussels. If you are characterising it as the hard exit route, where you are relying much more on World Trade Organisation rules, etc., you are in a different space, and that is a very broad discussion.

Q495 Wes Streeting: Absolutely. In the event of either a soft or a hard exit, are you concerned about the lack of influence that the UK would have inside the Commission, the Council and the European Parliament, in terms of the development of EU financial regulations? Is the absence of the UK voice in that scenario something that would concern you?

Mark Astaire: If you start from the point of view that being within the EU is, at the least, neutral to the UK position as a financial leader, if you exit then having less influence over what is a very important market for us is going to be a cause for concern. In the short term, there are going to be a lot of issues that most businesses will have to deal with, and they will not particularly enjoy having to deal with those. Most companies do not want to have to be setting up groups of people to look at a possible Brexit. The longer-term issues are something for which there will be a cost, even if in the long-term it is a positive thing.

Q496 Wes Streeting: Thinking about some of the practical implications then, under current European legislation, passporting provisions allow firms located inside the EEA to conduct many cross-border financial activities while remaining under the supervision of their home regulator. What proportion of your international business is dependent on the passport?

James Chew: In HSBC, we have a reasonable spread of European operations. I have to say that the majority of our continental European operations by value are locally incorporated. We have a pretty material bank in France, which is locally incorporated. We have one in Germany. We are a very big bank in Malta. We have branches around Poland. If passporting were prohibited, we would have to do a degree of realignment. At the moment, our operations in Spain, Italy and some other countries are branches of the UK. Hypothetically, we would switch them to be branches of a European entity, so that resolves that issue.

Wes Streeting: Mark?

Mark Astaire: It is not an area of expertise that I have. I am sorry.

Q497 Wes Streeting: No, that is fine. In the event of an exit vote, it is likely that the European Central Bank would require clearing houses dealing with significant volumes of euro-denominated transactions to be located within the remaining European Union. What impact would that have on your firms?

James Chew: This really depends upon the institutional arrangements that are put in place between the eurozone, or Europe, and the UK when it leaves, as to whether the location policy of the European Central Bank is enforced. In the summer of last year, we saw that an agreement was reached between the Bank of England and the European Central Bank, which put in place arrangements, and the British Government then dropped their legal challenge to the ECB location policy. I do not know whether those structures that were put in place could persist. If they could, clearly that policy may remain as it is today. It really depends upon the nature of the exit and the arrangements that are negotiated.

It would be unhelpful for a lot of people if those arrangements were not in place and clearing of euros had to move into Europe. More euros are traded in London than are traded probably anywhere else, so that would not be a good outcome.

Q498 Wes Streeting: That leads me on to a broader question about the impact on the UK, not just on your particular firms. We are a leader in euro-denominated wholesale banking, as you have already alluded to. Do you think that position as a leader would be threatened by a Brexit vote?

Mark Astaire: Just to lead into that question, in the event of a Brexit, there will inevitably be some horse-trading across a whole variety of industries, and some will probably be easier to negotiate than others. My guess would be that, while I think in some respects the UK could be damaged, the importance of having financial stability across Europe will focus people's minds pretty quickly on making sure that there are fairly clear arrangements for having a fit-for-purpose financial system across Europe. The consequences of people not being pretty sensible during those two years of the negotiation, as I think we would all accept, could bring a crisis much earlier than a liquidity crisis. People will be very cautious about it. The markets will be very concerned about the noises that come from both our Government and the Europeans.

Q499 Wes Streeting: One of the scenarios that we have considered and has been cited in previous sessions around the hard exit is a scenario where the UK effectively has a complete realignment of its relationship, both in economic policy terms and foreign policy terms, to a much greater reliance on trade with China and Russia. How important for you and your organisations would continued unfettered access to the European Economic Area be?

Mark Astaire: We do a lot more business with European countries than we do with either China or Russia. We believe in the single market. We absolutely recognise there are weaknesses in it and it can be improved, and we have talked about some of the improvements that need to be made, but as an institution, along with many other businesses, we would just like a more efficient single market. To us, that is the crucial thing, as well as being able to access other global markets more successfully. That leads into a whole variety of other conversations, but having access to Europe is crucial.

Q500 Wes Streeting: A final question: as you have already alluded to in your answers, the decision ultimately rests with the public. Thinking about your customers and your staff, what sort of impact do you think Brexit would have on them?

James Chew: I would have to go back to the fact that it really depends on the nature of the Brexit. If that is what the British people vote for, it depends upon the nature of the Brexit, but fundamentally we are still going to have customers in the UK. We are still going to need to serve those customers. Those customers are still going to want money lent from us. It will take time for the economic consequences of any Brexit, if that is the vote, to sink in.

Chair: Jacob Rees-Mogg has one very quick rejoinder.

Q501 Mr Rees-Mogg: Mr Chew, we got the answer from Mr Astaire on the importance of China to his business, but I thought it would be a pity not to allow the representative of the Hongkong and Shanghai Banking Corporation to say how important it was to his business.

James Chew: I would look at it from the other point of view. Of course, it is not whether we would like to develop our relationship with China, but whether China would want to develop its relationship with us. China would continue to want to develop a relationship with the European Union, as is left. It is a two-way street that you have to be aware of.

Q502 Wes Streeting: Mark gave an indication of this to my first question about the Government's position. James, your answers have repeatedly said that it very much depends on the nature of the exit. Do you share the view, therefore, that it is really important that the Government set out before the referendum a clear course of action and a clear direction in the event that the UK votes for Brexit?

James Chew: I would imagine that people will want that set out because they will want to know what they are voting on.

Chair: I can imagine the Government will give us a relatively sketchy reply.

Q503 George Kerevan: Good afternoon, gentlemen, and particularly good afternoon to Mr Astaire, because we went to the same university. I am warning you: this Committee is dominated by Oxford, not Edinburgh. Some of my questions may overlap a bit because there is a general centrality to the issue, but I am interested in what happens if we vote to leave and the impact that has on the flexibility of our regulatory regime, regardless of whether you think it is good enough or not. If we leave, what scope, in your professional expertise, is there for Britain modifying substantially its regulatory regime in the financial sector, before it falls foul of a European wish to make us equivalent so that we can operate in their financial regime? Basically, is there much scope for change, really, if we are to maintain market access to Europe?

James Chew: I go back to what the Governor said in his speech at Oxford—it was Oxford—in October. He said there were three areas where we needed flexibility in terms of financial regulation—he said there were some, but he mentioned three—which I think were remuneration, the triggers on contingent capital instruments, which is pretty arcane stuff, and national discretion in insurance supervision. There is a very, very close alignment between European regulation and UK regulation. It is not as if we are going to wake up the day after Brexit and say, "Wow, I really want to change my regulatory environment, because I have been out of step with Europe for a very long time." I do not think that will be the case, and, therefore, I do not think people will be saying, "I want to radically change it."

Q504 George Kerevan: But, if they wanted to change, if there was a mix of regulatory policies that people felt would make the financial sector more competitive in the UK, how far could we genuinely go down that road before we would then have to put in extra rules to deal with access to Europe?

James Chew: The honest answer is that I do not know. It depends on—I am sorry that I keep on coming back to this—the nature of the exit. It depends on whether you have a model where you take the rules lock, stock and barrel; whether you have an a la carte mechanism, as Switzerland might; or whether you have a WTO-style exit, where you have said, "This is what I am going to rely on." If you are on WTO, your access to the single market is very difficult. Switzerland does have access to the single market and negotiates on an a la carte basis. Whether it can continue to do that is a question that I know some people have raised. Whether the UK would be allowed to start off on that basis is a question people have raised. I am sorry not to be helpful, but it is really difficult, until you get to the particular circumstances, to say, "What can you squeeze out?"

One thing I would say is that there are areas where the UK is already super-equivalent to the European regime, so in some respects it could just bring itself back from where it has taken itself beyond Europe and become more like Europe.

Mark Astaire: It is a fascinating question. To my mind, it depends on the leadership of the Government at that point and what sort of ambition they have. If there is Brexit, it should be an opportunity. To then have a Euro-lite relationship, it seems to me, may prove to be a missed opportunity. My sense is that, as far as financial services are concerned, because of the sensitivity to the City and to markets, the opportunity for radical change will be quite limited, because both a UK Government and European Governments generally will be very nervous about shaking that particular tree too hard.

James Chew: Just to add one thing, there is a pretty complex equivalency process that Europe goes through when looking at other jurisdictions, which we see in places such as the US, etc. I agree with Mark that it would not be easy to go very far.

Q505 George Kerevan: Moving down that road, much of the discussion has been about implementing the post-crisis regulatory regime and the reforms that have been brought in. Let us look 20 years ahead. Let us suppose that Britain has come out of the EU. We are looking far ahead. Essentially, the European financial arrangements are the City of London here, with the pound, and the eurozone. Looking very long term, are there implications for the UK and London if the eurozone recovers—some people say it never will—its competitiveness and its economic dynamism post the euro-crisis and the European banking system grows in line with it? Looking longer term, are we likely then to find that Britain and London have to become more and more complaint with European rules governing financial regulation?

James Chew: We already have institutions in place—the European supervisory authorities, the ESAs—that are intended to make sure we have harmonisation across Europe and to reflect the different circumstances of the countries across Europe. Those remain in place. Within, for example, the European Banking Authority, voting arrangements have been put in place specifically to protect the euro-outs, if I can call them that, from the caucusing of the euro-ins. It is something I know the UK Government have been legitimately concerned about, and it is one of the areas where they are looking to secure additional protections. I can understand that.

If those institutions and those protections are in place, the scenario that you suggest would not be concerning for the UK. If those are weak and if those protections are not in place—as I said, we already have some in place—undoubtedly you would see a greater focus on the regulation to suit the eurozone than the regulation to suit the whole EU. Now, that is why those protections are being discussed. That is why we have some protections in place. It is a legitimate area of concern.

Q506 George Kerevan: Are you satisfied with the protections?

James Chew: You could always have more protections, and it is up to the Government to determine that. I do not know the details of the protections that are being discussed. We have seen some set out in David Cameron's letter to Donald Tusk. Those are important areas that people will have to consider when they come to sit down and say, "What are the potential risks that we face?"

Q507 George Kerevan: Let me try and tempt you to say a bit more. Let us suppose that Jacob has his wish and we come out. Are there any current EU financial regulations that you would do away with, if you had the opportunity?

James Chew: I hope the current Government would do away with the remuneration rules, and that is pretty widely supported within the supervisory sector. The bonus cap is not seen as effective and is seen as hampering our flexibility, so that is clearly one that we would do away with. It would very much depend upon the exit arrangements and where we had got to in the regulatory environment—we still have a massive regulatory agenda going on—on things like the reporting for OTC derivatives. I know this is very much down in the weeds, but these will all be things that are operationally very important and cost money.

The question is: if you have already established a standard for doing something that has been accepted by other countries, do you want to go and change it, just so that it is in blue rather than red, or whatever the colour is, or do you just accept what you have and say, "I am not going to go back and change that, because we have got used to it now. It is not the greatest thing, but it is fine"?

There may be some elements of how the Banking Recovery and Resolution Directive has been enacted. We have a concept of minimum required eligible liabilities, which is a measure of how much bail-in capacity you need and is set in Europe, which is not the same as the way the Financial Stability Board has measured it. They call theirs total loss-absorbing capacity. Would I want to switch from one to the other? Frankly, I prefer the total loss-absorbing capacity measure. I find it a bit easier to understand than the MREL. On that, I might want to switch, but, if I have been living for six years with MREL by the time we get out, maybe I will say, "Oh, I cannot be bothered."

George Kerevan: Mr Astaire?

Mark Astaire: To be frank, it is far too much in the weeds for me, as a non-regulatory person. Looking 10 or 20 years forward, the success of London in relative terms will, I believe, determine our ability to negotiate things that are in our interest. I do believe in power blocs and I think one of the risks over time is that the UK gets side-lined. I do not think it is inevitable, but we clearly have disproportionate influence in financial services and global markets because of the strength of London, which is a big positive for Europe. A lot of Europeans appreciate that having London is a great plus for Europe. That is the only perspective I would really add to that.

Chair: You have said that twice. I would be very grateful if you could put something down on paper to set out why we are a great plus for them—not now, because we are short of time, and I do not want to take up George's time and remaining questions.

Q508 George Kerevan: My final point goes back to something you were discussing at the very beginning: the influence of the G20 laying out the overall architecture of the current reforms. How do you see this playing out? If the UK came out of the EU, would we be less influential or more? How would it affect our influence on the G20, in the current situation where the G20 is driving things? How long do you, from your professional perspectives, think the G20 will remain in that position? Would, over a period of time, its influence dissolve, going back to regulation determined on a geographical basis?

James Chew: What I would say is that I think the G20 will persist—that is my view. The balance of influence within the G20 will change, and that will naturally reflect the economic changes we are going to see over the next 20 or 30 years between the US, China, Asia, etc. The UK's influence at the Financial Stability Board and the Basel Committee has been very strong historically. We have a particular influence at the moment because Mark Carney is the chair of the Financial Stability Board. At some stage, he will step down, and that inevitably reduces the influence to some extent.

We have fewer globally systemically important banks in London; we have four. I imagine that that may decrease as some of the banks rationalise their operations and focus a bit more. The European Central Bank now has eight, so it has the same number of globally systemically important banks as the US. The eurozone as a whole is a very, very large economy, so it is supervising a lot more banks than London is supervising. Inevitably, it will begin to form and put forward opinions about bank supervision in a way that it has not before. I would also say that I expect the Chinese to put forward ideas on bank supervision in a way that they have not before, because we are going to get changes. Inevitably, if we have a number of powers rising in percentage terms, that means that the UK's influence has to decline. It still has to add up to 100%.

Q509 George Kerevan: It would be better to stay in, then.

James Chew: You have to remember that we are not part of the banking union, so the ECB operates separately to the Bank of England in that sense. The question is whether, as part of the European Union, that enables us to buddy up to the ECB in a way that we might otherwise not. That is speculation.

Chair: We have done quite a bit of speculating this afternoon, on some very interesting generalities and one or two particulars as well. We have asked for a bit of further information on one or two points. Thank you very much, both of you, for coming to give evidence. We really appreciate it. If you have further points you would like to put on paper when you reflect on what you have said, we would be very happy to receive those as well. Thank you very much.