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French turn against risky trading

By Scheherazade Daneshkhu and Hugh Carnegie in Paris

BANKS Universal model will survive reform Separation within subsidiaries sought

The French government will ban high-frequency trading, agricultural-commodities derivatives trading and other "highly speculative" activities but will allow banks to keep intact most market-making activities in its forthcoming banking reform law.

Pierre Moscovici, finance minister, told the Financial Times yesterday that the law would be "very bold, very radical but it will preserve the French universal banking model".

Banks would also have to present supervisors with a resolution plan in case of a crisis and would be required to pick up the bill for failure.

He also confirmed that: "We are in the final stages of this reform," the draft text of which will be discussed at a cabinet meeting on December 19.

The reform will require banks to set up subsidiaries into which speculative activities that are not linked to financing the economy - such as proprietary trading - will have to be separated. The subsidiary would be subject to higher capital and supervisory requirements than the rest of the bank.

However, "activities that are necessary for financing the economy" will be excluded as the government recognised the "increasingly sophisticated needs of our companies in terms of finance and access to markets," Mr Moscovici told a Paris conference organised by the AMF, the French markets regulator, yesterday.

This suggested that most market-making activities would be spared from separation.

He said that the French reform drew its inspiration from the European Union-commissioned Liikanen report, published last month, which recommended "legal separation of certain, particularly risky financial activities from deposit-taking banks within the banking group". However, under Liikanen, most market-making operations would have to be legally separated from the deposit-taking bank within a holding company structure. Mr Moscovici

told the FT that the draft reform would be "more Volcker than Vickers", referring, respectively, to the plans by the former US Federal Reserve chairman and the UK's proposals.

The first would ban commercial lenders from certain risky activities, such as proprietary trading, while the latter recommended separating retail from investment banks.

Complete separation "would be too far from the European banking model", Erkki Liikanen, governor of the Bank of Finland, told the conference.

French banks appear to have succeeded in their hard lobbying to ensure that market-making activities are not separated from their retail bank structure, arguing that most of these activities are to ensure liquid markets for clients. Some bankers said that banning activities could drive them offshore.