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# Frankfurt as a financial centre after Brexit

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## Introduction

Frankfurt's financial sector is often identified as a potential beneficiary of Brexit. However, no comprehensive analysis of the positioning of actors within Frankfurt since the Brexit vote has been conducted. In this brief, we outline some central findings from fieldwork we conducted in Frankfurt in November 2017. For the research, we conducted semi-structured interviews with a broad range of elite stakeholders based within Frankfurt's financial sector. Six central observations emerge from the research.

1. Stakeholders consistently claim that Frankfurt enjoys a number of comparative advantages over rival EU financial centres, including the political and economic stability of Germany and Frankfurt's position as a centre of EU financial supervision.
2. A distinct complex of public and private actors - including the local political authorities, marketing agencies and banks with regionally-focussed business models - drive efforts to promote Frankfurt as a financial centre.
3. Global financial institutions with a presence in Frankfurt such as foreign investment banks adopt a more ambivalent perspective on the location of business activities after Brexit.
4. There is a widespread perception that those promoting Frankfurt have 'played to its strengths', focussing on its stability and the competence of its regulatory authorities. Respondents contrasted this with the more 'aggressive' approach pursued by other EU financial centres, most notably Paris and Luxembourg.
5. Stakeholders acknowledge that the City of London will remain Europe's primary financial hub and that alternative EU financial centres with non-banking specialisations will also benefit from Brexit. That said, respondents consistently note that they expect between 5,000 - 10,000 jobs to move to Frankfurt over the next four years.
6. Stakeholders acknowledge that the German Federal government has played a limited role in 'promoting' Frankfurt as a financial centre but were split on the implications of this dynamic.

## Background

- Frankfurt is Germany's leading banking centre. Approximately 75,000 people are employed in its financial sector and the city plays host to a large number of foreign banks.
  - Frankfurt is also the site of important European and German regulatory institutions, including the European Central Bank (ECB), the European Insurance and Occupational Pensions Authority (EIOPA) and the Bundesbank.
  - When the UK leaves the EU, banks based in the City are likely to lose their 'passporting rights'. This means that wholesale banks currently domiciled in the UK have a strong incentive to apply for an EU banking licence in another EU member state.
  - A number of EU financial centres - notably Frankfurt, Paris, Dublin, Amsterdam, Luxembourg and Milan - have sought to position themselves as beneficiaries of the Brexit process.
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- Since before the June 2016 vote, political actors and marketing agencies from Hesse have sought to ‘pitch’ Frankfurt as a site for financial investment.
- There have been numerous reports of international banks - for example Goldman Sachs as well as other institutions - acting on plans to set-up subsidiary entities in Frankfurt as a means to retain their European ‘passporting’ rights.
- As a result, actors within Frankfurt expect to see employment in the financial sector expand by 5,000 – 10,000 over the next four years.

## Evidence and Analysis

We conducted semi-structured elite interviews with a wide range of stakeholders based within Frankfurt’s financial sector. Respondents included senior representatives of trade associations, international banks, regional banks, national regulators, regulatory authorities, marketing agencies, international financial institutions, private investment firms and representatives of the Hesse region. In the briefing all personnel and organisations have been anonymised.

The semi-structured interviews were organised around a number of core questions, including:

- What risks and opportunities does Brexit pose to Frankfurt’s financial sector?
- In what ways has Brexit impacted upon the work streams of organisations in Frankfurt?
- What supervisory/regulatory challenges does Brexit pose to Frankfurt as a financial centre and the European financial system more broadly?
- Who has been behind attempts to lobby on behalf of Frankfurt? Has this effort been successful?

**Six central themes emerged from our research. These are outlined in the sections below.**

### 1. Frankfurt has a number of distinct advantages over alternative EU financial centres

Respondents consistently identified a number of core advantages which Frankfurt enjoys over other EU financial centres such as Paris, Luxembourg, Dublin and Amsterdam. These include: the economic and political stability of Germany; the location of the ECB and other regulatory institutions such as EIOPA and the Bundesbank within Frankfurt; the reputation of German supervisors - the Bundesbank and the Federal Financial Supervisory Authority (BaFin) - for competence in regulating financial institutions; the locational advantage of Frankfurt at the ‘heart’ of continental Europe.

- **Economic and Political Stability**

- Numerous respondents noted that Germany’s economic and political stability is a key advantage for Frankfurt.
- One senior representative of an organisation which promotes the Hesse region stated, *“Germany is an anchor of stability in a world that is becoming very ‘interesting’ in political and economic terms. Within Germany – in that anchor of stability – you have Frankfurt as a financial centre”*.
- Respondents also stressed that the reputation of the German regulators - the Bundesbank and BaFin - are a key asset for Frankfurt.
- The head of an institution representing foreign banks in Germany stated that BaFin, *“are strong regulators but predictable and you can rely on what they and the Bundesbank are telling you. Another interesting thing is that you can have a discussion with the German supervisors. They are open and constructive, which our members tell us is not the case with some of the other national regulators. You can talk more openly with BaFin about what infrastructure needs to be in place. It’s not “send us a letter and we will say whether it’s yes or no”; it’s a process of collaboration...BaFin offered to do bilateral meetings with banks and they have specific teams dedicated to each bank in order to assist them with the application and to support them during the procedure. They also agreed to provide documents and discuss in English. Some formal letters have to be in German, but a lot of documents can be in English, which is quite important”*.
- Respondents contrasted these bodies with regulatory authorities in other EU jurisdictions. Some claimed that other EU financial centres may be willing to engage in ‘regulatory arbitrage’ - loosely or inadequately applying EU regulations - in order to induce post-Brexit investment. However, they noted that the German regulators’ reputation for robust application of the rules was an advantage for Frankfurt. For example, one representative of financial lobby group in Frankfurt stated, *‘we [Frankfurt] haven’t had to pull off any tricks or special offers to attract people to come here. No special tax rates or anything. We’re competitive as is.’*
- This sentiment was echoed by representatives of foreign banks. One senior executive from a US firm based in Frankfurt told us that, *“When you’re going through a process of political instability – which is what Brexit injects into the equation – there’s a natural tendency to not look for the next ‘cool deal’. You’re looking for stability and clarity – a paradigm with which [one] can work, understand and feel comfortable.”*

- **The location of the ECB and other supervisory institutions within Frankfurt**

- Numerous respondents stated that the ECB’s location within Frankfurt is a further advantage for the city relative to other EU financial centres.
- One interviewee – a senior researcher at a large regional bank – stated that, *“foreign banks want to be where the cluster is [...] in Frankfurt there are lots of foreign banks [and] Frankfurt is a supervisory hub. We have the ECB, the Bundesbank, EIOPA... a lot of supervisors are already here”*.

- A senior official we interviewed who works closely with the German regulators echoed this view, stating that *“personal contact and onsite inspections are an important part of supervision. Proximity to the Single Supervisory Mechanism (SSM) and the Bundesbank are an advantage for Frankfurt”*.
- A representative of an organisation marketing Frankfurt as a financial centre echoed this sentiment, stating that, *“When you start pooling organisations in one place...you can realise different synergies and be more efficient...having the ECB and its regulatory functions in Frankfurt is advantageous because you can have a good relationship with your regulator because they’re close by. The ECB also attracts a talent pool and this adds to the weight of the financial centre”*.
- The ECB and the German regulators insist that they are neutral in relation to where financial activity is located inside the Eurozone, emphasising their mandate to ensure price and financial stability. However, the majority of our interviewees claimed that an unintended consequence of the ECB and Bundesbank’s location in Frankfurt is that this deepens the financial ‘ecosystem’ of the city, making Frankfurt more attractive as a location for business activities after Brexit.

## **2. A distinct complex of public and private sector interests - notably local political authorities, lobby groups and regionally-focussed banks - have taken the lead on ‘promoting’ Frankfurt as a financial centre**

- On the political side, the authorities of the state of Hesse and the Frankfurt city government have a clear interest in expanding the size of Frankfurt’s financial sector in order to boost employment and tax revenues.
- These political actors have worked in deep collaboration with Frankfurt-based marketing agencies in order to promote Frankfurt as a financial centre.
- In particular, Frankfurt Main Finance, Frankfurt-Rhein-Main GmbH and Hesse Trade and Invest have adopted a coordinated approach to promoting Frankfurt as a financial centre.
- One representative of a leading Frankfurt-based marketing group emphasised the ways in which public and private actors have worked collaboratively and strategically in promoting Frankfurt, stating that local political authorities, *“have been good. We have a weekly call with our partners from the city, with other marketing organisations [...] such as Hesse Trade and Invest [the economic development company of the Hesse state] and Frankfurt Rhein Main GmbH. This has been going on since before the Brexit vote. Collaboration has been good. We’ve done these joint delegation trips to London, had events here [in Frankfurt], we promote each-others’ marketing material and pool our resources in order to have a unified message which has worked well”*.
- Some private sector institutions – notably regional banks (‘Landesbanken’) and market infrastructure providers – are also keen to promote Frankfurt as a financial centre.
- In the case of Landesbanken - German banks with a strong regional focus - the deep integration of their business models with the surrounding region ensures that these institutions have a strong incentive to promote their resident city and region as a site for external investment.

### **3. Global banks with a presence in Frankfurt are more concerned with minimising disruption than with ‘promoting’ one financial centre over another**

- Representatives of large global investment banks we interviewed were far more ambivalent about efforts to promote Frankfurt and the Hesse region.
- We asked a senior researcher from a global bank whether Brexit might present opportunities for Frankfurt as a financial centre. The respondent stated, *“it depends on who you ask. If you are asking a local policymaker in some of the cities that now may benefit from an influx of investment bankers and so on, of course they will probably say that Brexit is a good deal for us. For the financial industry [however], it is definitely a ‘lose-lose’ situation. There is no gain in an increase in fragmentation. There will be additional costs. You will have to build new infrastructure elsewhere. You will duplicate resources. The whole industry loses synergies, because part of the business is moving to Dublin, part of it is moving to Paris, part is moving to Luxembourg, part of it is moving to Frankfurt. Together, this embodies a disintegration of the European wholesale market.”*
- This concern with fragmentation was echoed by other respondents. In relation to the clearing of euro-denominated derivatives, for example, the head of an institution representing foreign banks told us that, *“the industry side is not really interested in moving the euro-clearing to another place to avoid fragmentation. From the viewpoint of cost efficiency, it is preferable that all the infrastructure and liquidity is in one place”.*
- This shows that the principal concern of global banks based in Frankfurt is not to ‘promote’ one city over another but rather to minimise disruption and inefficiencies caused by Brexit.
- Globally-oriented institutions tend to be more concerned about the global competitiveness of the European financial market. One respondent from a globally-oriented institution stated that, *“Some people tend to think that [Brexit] is a positive thing for Frankfurt or Paris or Dublin, but in the long run, it’s a fight against other places [outside the EU].”*
- Numerous respondents concurred, noting that the ‘real’ post-Brexit competition was not necessarily between financial centres based inside the EU but rather between the EU and rival ‘third country’ centres such as New York, Hong kong and Singapore.

### **4. Respondents state that Frankfurt has ‘played to its strengths’, running a well-structured and unified campaign which emphasises stability and competence. Many respondents noted that this contrasts with the more ‘aggressive’ approach of other financial centres in the EU, most notably Paris.**

- There was a perception that Frankfurt’s emphasis on ‘stability’ and ‘reliability’ is a key asset, setting the German city apart from its competitors.



- A senior executive from the Frankfurt office of a US firm stated, *“the entire German marketplace – the associations, the regulators and the German government itself – have exerted a lot of effort in demonstrating that the market is open for banking. They have played very well to their strengths. They haven’t tried to make crazy promises in relation to tax structures [...] they’ve played the themes of stability, clarity, reliability and consistency in what they’re doing.”*
- This view was echoed by a representative of a globally-oriented financial institution. The respondent stated, *“stability is one of the biggest assets that we in Frankfurt have. Frankfurt has a good infrastructure, is solid and so stable that this makes it quite attractive.”*
- A representative of a Frankfurt-based lobby group stated that this approach - to adopt a less aggressive posture and to play the ‘stability’ card - had been a conscious element of the city’s strategy in the aftermath of Brexit. The respondent stated, *“Before Brexit, we had regular calls with the decision makers in the state government, in the region, the city and the chambers of commerce five months before the referendum. This close cooperation was critical. We spoke about promotional measures and we agreed that we did not want to have an aggressive marketing strategy. We agreed that if politicians would go to the UK, we agreed on the wording that would be used. Whether they were city politicians or state politicians, we agreed the wording would be the same.”*
- The theme of Frankfurt’s ‘stability’ in a context of post-Brexit uncertainty has therefore been consciously adopted as the central ‘pitch’ of leading representatives of the Hesse region.
- Some respondents were keen to contrast Frankfurt’s ‘stability’ pitch with the more ‘aggressive’ pitch of other financial centres - most notably Paris. One respondent representing business from the Hesse region stated that, *“we didn’t want to be loud and aggressive...and I think it was a good strategy. Paris had another strategy. They were very pushy and populist in their attempts to attract firms. Frankfurt was a little bit less loud, less aggressive.”*

##### **5. Although Frankfurt-based stakeholders expect significant relocations to take place during 2018/2019, they also recognise that there are limits to the ‘gains’ which are now made possible by Brexit**

- Respondents already see a “Brexit effect” taking place. One representative of a leading Frankfurt financial lobby group stated that, *“a dozen banks have actually made on-record announcements of their intention to move to Frankfurt. There’s also a few more on top of that who asked not to be named who have discussed their plans with us. Our real estate research shows that there’s been a big increase in take-up and movement in the market”.*
- The respondent continued, *“big leases are being signed, Goldman Sachs is one of them. They signed a lease on a high-rise that is not yet complete, to up their capacity. We’re expecting the first staff movements in the first half of 2018. The first wave will be about 1,000 positions. We’ve said all along that we expect 10,000 jobs to be relocated here over a span of 5 years after Brexit. Based on the announcements that are being made we are comfortable with that number.”*



- A senior researcher from a large regional bank echoed this view, stating that a Brexit jobs boost “*will start to materialise in Frankfurt in 2018. The clock is ticking and if you look at the timetable for the EU-UK negotiations, there’s only one year left to reach an agreement, if you count in the necessary ratification time. For a foreign bank, it takes around the same time to get a banking licence from BaFin and to get the EU passport....this process is already on its way. BaFin reported as early as spring that a double-digit number of institutions had indicated an intention to relocate business to Frankfurt*”.
- Based on in-house calculations, the respondent stated that, “*we forecast that in the next couple of years a minimum of 8,000 financial sector jobs will be relocated from London to Frankfurt. This is our conservative estimate counting only banking and insurance and not any of the adjacent, non-financial sector jobs.*”
- Stakeholders estimate that a significant number of banks will trigger their contingency plans by mid-2018. This would allow for enough time to secure a banking licence.
- Despite their willingness to ‘benefit’ from Brexit, respondents were also concerned not to overstate the ‘gains’ which might be possible for Frankfurt once the UK loses its passporting rights.
- Respondents also noted that relocation of financial activities after Brexit would - in part - be determined by the extent to which alternative financial centres have existing comparative advantages and ‘specialisations’.
- One respondent stated that, “*The truth of it is there is not going to be one winner, as far as financial centres go. Different financial centres are equipped to take on different business lines better than others. Asset managers are obviously going to Dublin and Luxembourg. It’s always been clear that that’s where they were going. Dublin will also take on back-office jobs along with Warsaw and other eastern European financial centres. Trading platforms should gather in Amsterdam. Insurance will scatter across Europe. Paris and Frankfurt overlap a little bit as far as trading and front-office goes. But banks are deciding where to go based on where they already have operations built up and where there is a good talent pool. So everybody is winning different parts of it*”.
- Respondents working within globally-oriented financial institutions echoed this view. One respondent stated, “*What I can observe is that we see specialisations emerging, where currently Luxembourg and Dublin are qualifying for ‘specialised’ industries, Amsterdam more for the technology side, and now it’s a question of where the classical banking business goes: Paris or Frankfurt?*”
- Pre-existing linkages between financial institutions and specific financial centres was also identified as an important determinant of post-Brexit investment decisions. One respondent from a global institution based in Frankfurt stated that, “*traditional linkages of individual institutions to different markets are key. HSBC has a long standing and large presence in France whilst German and many Swiss banks have Frankfurt as their traditional hub. Many US investment banks have a link towards Dublin. That seems to me an important driver of fragmentation. Individual institutions have established capacities and resources in some existing centres and they decide it’s easier to ‘scale up’ their existing resources rather than building something from scratch in another centre*”.

- These quotes underline an important point: that ‘lobbying’ actively on behalf of a financial centre can only go so far. Path dependencies and pre-existing ‘specialisations’ will be important factors which shape where business activities are relocated.
- In addition, respondents widely acknowledged that the City of London would remain far and away the dominant hub of finance within Europe after Brexit. One respondent stated, *“Obviously the centre of gravity will move a little bit. Some [EU financial centres] will take a lead, but it’s not going to be a lead like London has in comparison to other financial centres. It will be a small lead”*.
- Another respondent, representing business from the Hesse region, stated that, *“London will remain the most important financial centre in Europe. I don’t think there will be significant losses in importance for London. But some parts of the business will relocate to the continent. It’s not a race but a changing of the balance and every location will take its part of the cake.”*

**6. Stakeholders acknowledge that the Federal government has not been involved in the promotion of Frankfurt as a financial location, with the exception of supporting the bid for the European Banking Authority (EBA). This is not expected to change in the immediate future.**

- Some respondents voiced their frustration that there had not been proactive engagement from the German Federal government to promote Frankfurt as a financial centre. One stated that Frankfurt stakeholders, *“would have appreciated more involvement [from the Federal government] in this process...the view from Berlin is that ‘Frankfurt is a case for the state of Hesse, not the Federal state’. This is not very helpful. I would have appreciated if they had shown a little more engagement”*.
- Respondents noted that the Federal government had adopted a more proactive stance on promoting Frankfurt as a location for the EBA. One stated, *“they got involved in the EBA case - Schäuble was open-minded in this case”*.
- However, the prevalent attitude towards the Federal state’s lack of involvement is relaxed acceptance. One senior representative of an organisation which promotes the wider region around Frankfurt stated, *“I’m not frustrated with the national government; we’ve been successful without broad support from the federal government. I don’t think it would have made a major difference if Merkel had said ‘we support Frankfurt’... it’s nice to have but not crucial”*.
- The lack of engagement from the national level contrasts markedly with the case of France, where national politicians - first President Hollande and now President Macron - have taken a far more proactive approach to promoting Paris as an alternative financial centre.

## Conclusion

A distinct constellation of private and public interests - most notably Hesse's local political authorities, Frankfurt-based marketing agencies and German regional banks - have taken the lead in 'promoting' Frankfurt as a financial centre after Brexit. These actors have engaged in regular dialogue, ensuring that a unified marketing strategy is applied. The key theme pushed by the Frankfurt financial lobby is that of *stability*. This operates on two levels. On the one hand, Frankfurt lobbyists point out that Germany enjoys a high degree of political and economic stability. On the other hand, they claim that the German regulators - BaFin and the Bundesbank - are consistent, reliable and competent. This makes Germany and Frankfurt in particular an attractive site in a period of deep uncertainty. Furthermore, Frankfurt sustains a wider financial 'ecosystem' - playing host to the ECB, EIOPA, the Bundesbank and advanced business service firms - which, it is claimed, makes the Hesse region a particularly attractive site for investment. These factors form core elements of Frankfurt's 'pitch' to potential investors after Brexit. However, important barriers to Frankfurt's further expansion also endure. Other EU financial centres have pre-existing linkages to large investment banks and sustain particular 'specialisations' which could make them attractive for post-Brexit investment. Furthermore, the City of London's internationalised character makes it unlikely that it will be supplanted as Europe's premiere financial centre in the medium term. That said, stakeholders in Frankfurt recognise that even a relatively small expansion in Frankfurt would have a big impact for the region.



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