

Changes in Global Banking Regulation: Roadmap & Implications for Capital Markets and the Economy

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Views are my own and not those of any entity I am
associated with.

Never Again?

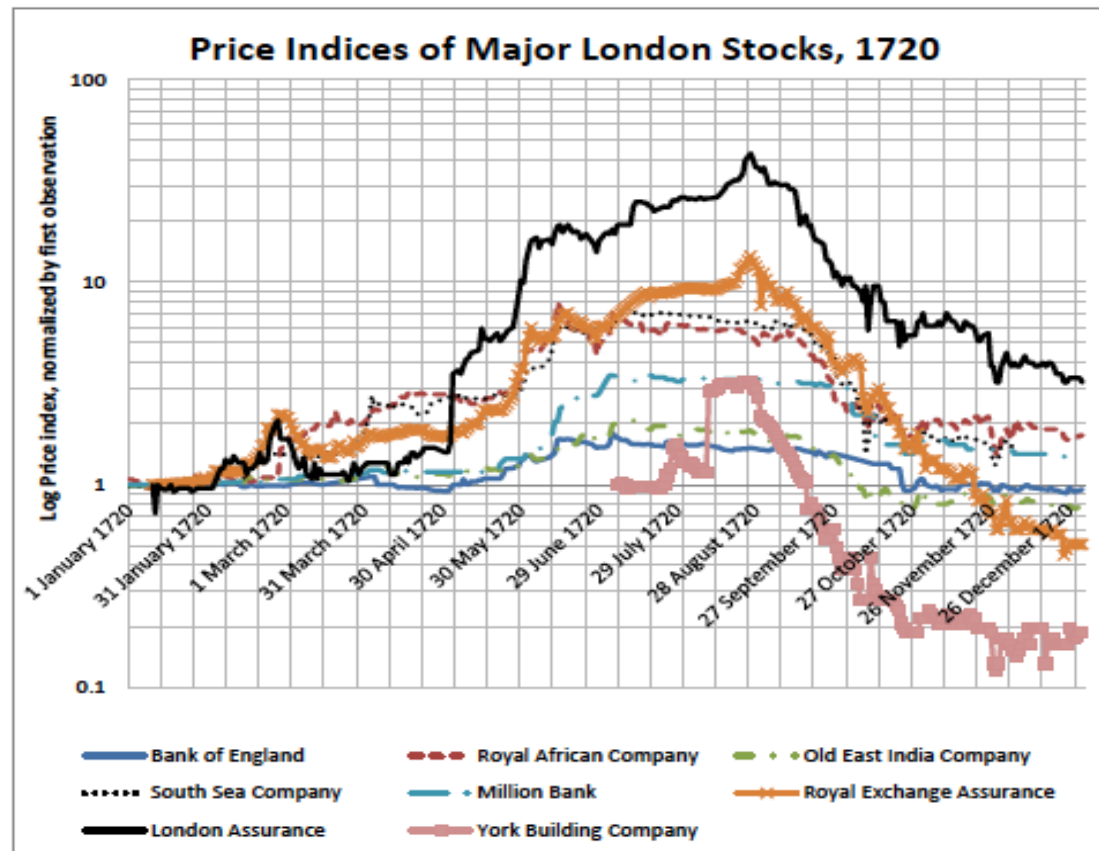


Figure 1: Price Indices of Major London Stocks, 1720. Daily price indices on a Julian calendar for the major stocks trading on the London market, from January 1, 1720 to December 31, 1720. Major stocks are Bank of England, Royal African Company, Old East India Company, South Sea Company, Million Bank, Royal Exchange Assurance, London Assurance and York Building Company. Prices are divided by the January 1st value for all series except the York Building Company, where prices are divided by the first available data point (June 28, 1720 [J]). Price indices are plotted on a logarithmic axis. Prices are interpolated between trading days.

Enough Blame to Go Round



Who is This Man?

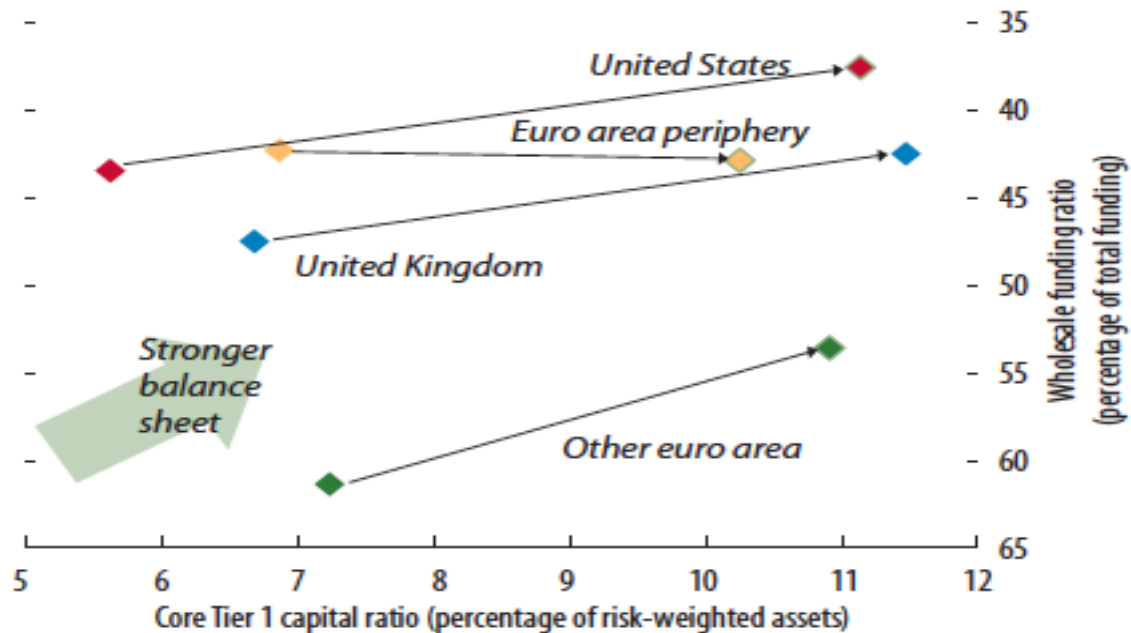


Healthy Banks Support Economic Activity

- Requires timely action to resolve problems.
- Rebuild balance sheets.
- Recognize imbedded losses
- Reasonable policy certainty and reasonable predictability of returns--how else to attract shareholder capital?
- But 5 years on.....

Resiliency

Figure 1.32. Bank Core Tier 1 and Wholesale Funding Ratios, 2008:Q4 to 2012:Q3

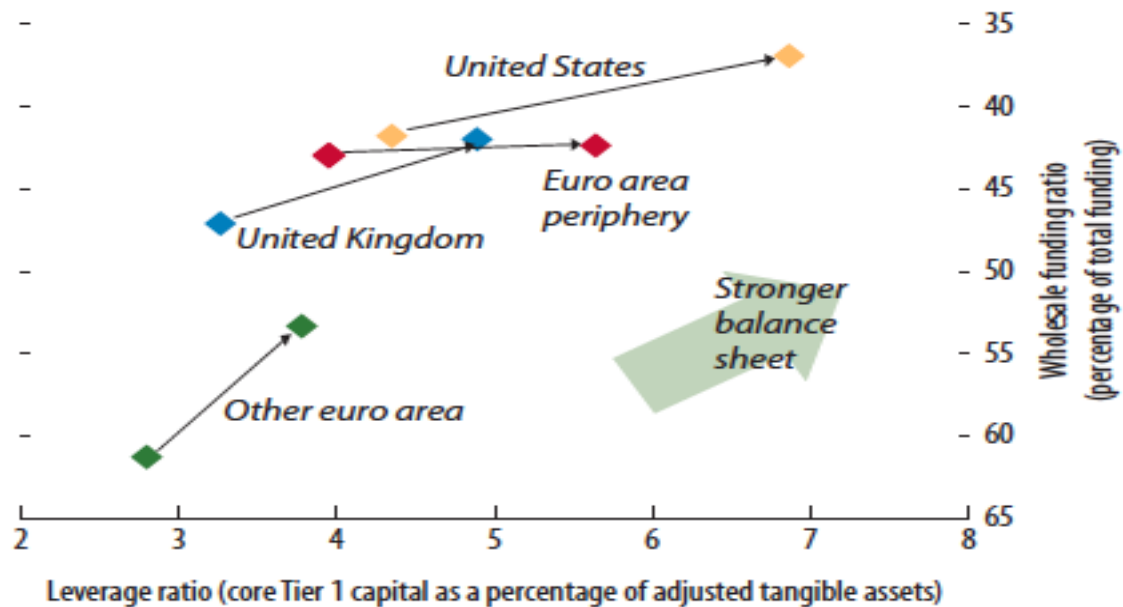


Sources: SNL Financial; and IMF staff estimates.

Note: Euro area periphery = Cyprus, Greece, Ireland, Italy, Portugal, and Spain. Wholesale funding is debt, repo, and interbank deposits. Total funding is wholesale funding plus customer deposits.

Resiliency

Figure 1.33. Bank Leverage and Wholesale Funding Ratios, 2008:Q4 to 2012:Q3



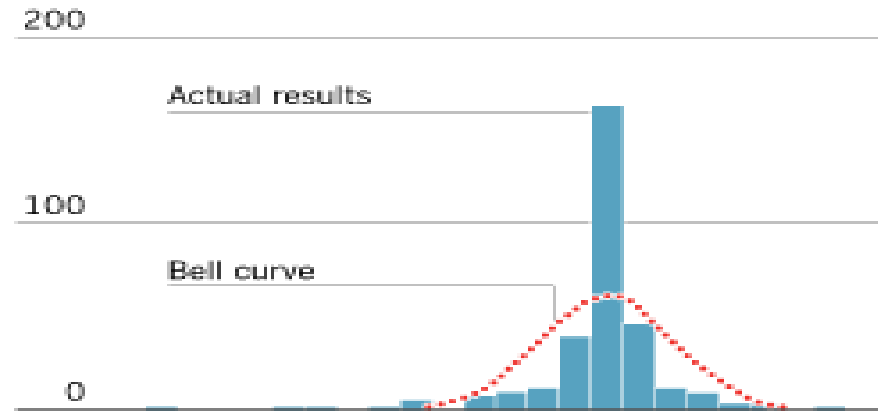
Sources: SNL Financial; and IMF staff estimates.

Note: For European banks, tangible assets are adjusted by subtracting derivative liabilities, but some differences in accounting definitions may remain. Wholesale funding is debt, repo, and interbank deposits. Total funding is wholesale funding plus customer deposits.

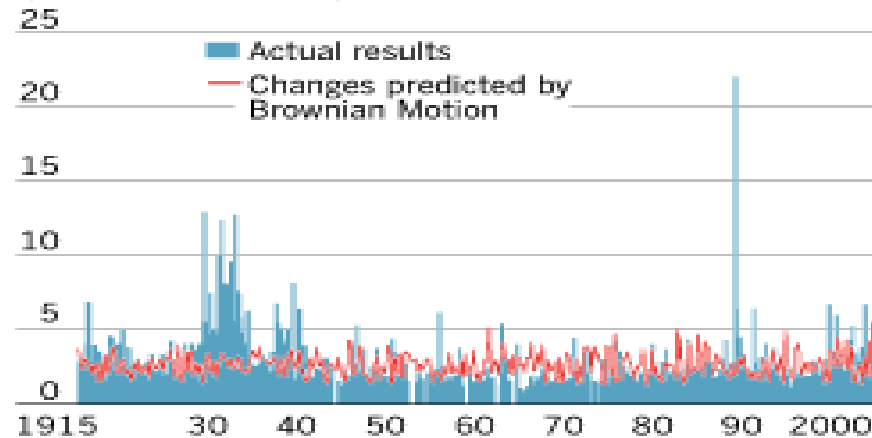
Do Economists and Analysts Get It Yet?

A far from random walk

Distribution of returns (sterling vs Dutch guilder 1609-2000)



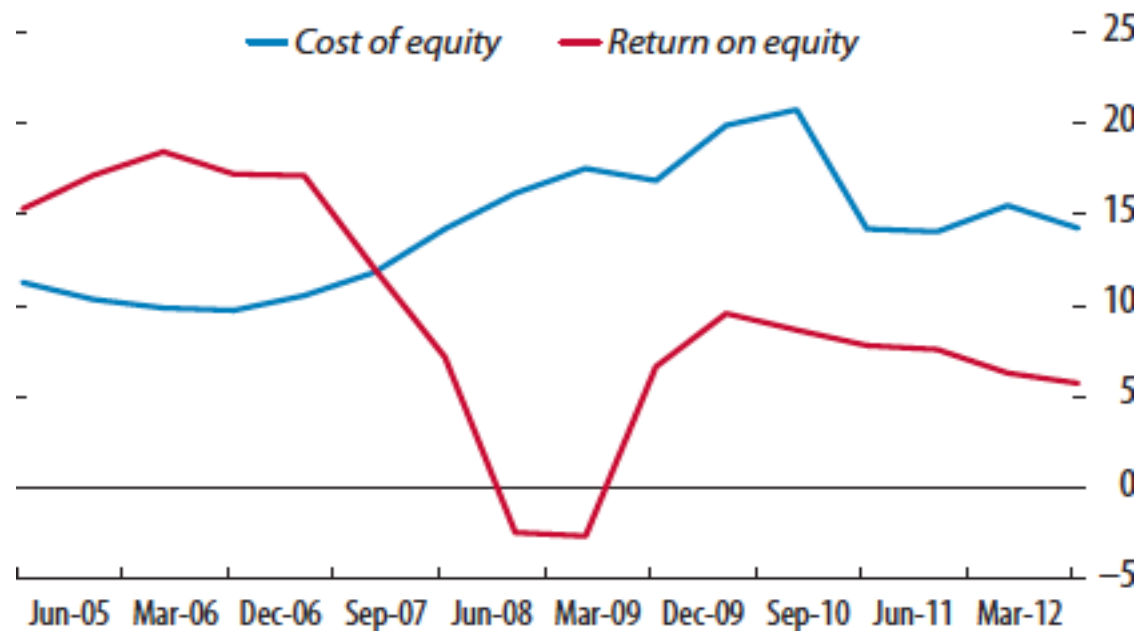
Daily changes in the Dow Jones Industrial Average (standard deviations)



Source: *The (Mis)Behaviour of Markets* by Benoit Mandelbrot & Richard L. Hudson

Hmmmmmm!

Figure 1.41. Average Return on Equity, and Cost of Equity
(In percent)

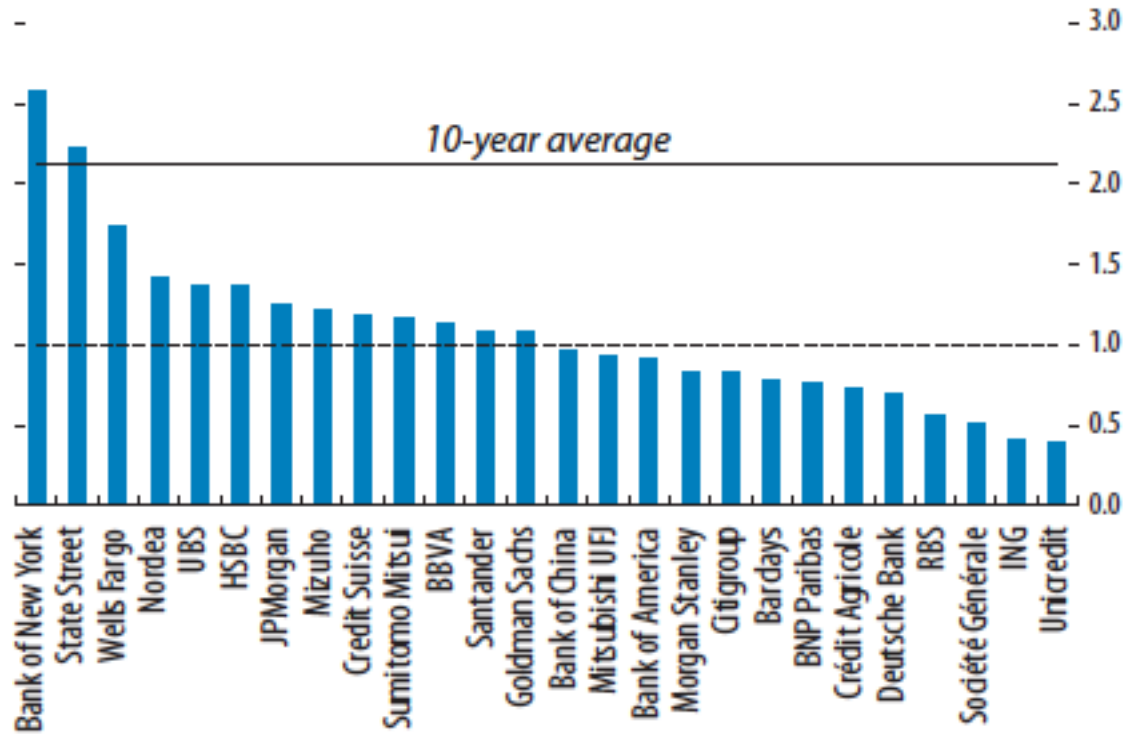


Source: Bloomberg L.P.

Note: The cost of equity is derived using the Capital Asset Pricing Model (CAPM).
The sample consists of global systemically important banks.

Hmmmmmm!

Figure 1.42. Ratio of Equity Price to Tangible Book Value, April 2013



End 'Never Again!' Mentality

- Breeds complacency
- Undercuts credibility
- Policy makers think more rules are better
- Reinforces moral hazard
- Get crisis thinking into analysis and models and investment decisions and prevention discipline

Rules, Regulation, Supervision

- Increasingly there is not an international set of rules
- Country Balkanization and ring fencing rising
- Important proposals not part of the international process
- Multi-speed implementation of agreed rules
- Little holding to account in IMF peer reviews
- Supervision under-appreciated and under resourced

‘Never Again!’, A Scorecard

- What matters (score authorities/banks)
 - Enhance bank resiliency-----B+/B
 - Deal with TBTF-----F/NA
 - OTC derivatives reform-----???
 - Market infrastructure reform-----C
 - Improve supervision-----F/B+
 - Longer term liquidity management-----D/B
 - Better incentives in comp.-----C/B
 - Better risk man./governance-----C/B

'Never Again!' Misplaced

- What is misguided or a muddle
 - Shadow banking regulation
 - Bank Structural measures (Volker etc.)
 - Macro prudential regulation and counter cyclical regulatory actions
 - Better monitoring of concentrations/funding
 - SIFI notion

Some Implications

- Finance a smaller share of global GDP?
- Some financial markets overbought?
- Push for more disintermediation?
- Less available cheap credit for longer term investments.
- Another crisis? Yes, just different.
- Are banks becoming utilities?—yes
 - Can some exceed?
- Non traditional financial entities more growth opportunities.

Some Implications (2)

- Widely differing returns on banks bundled businesses—implications?
- ‘Old’ economy financial systems vs those in emerging markets.
- Need healthy banks and financial intermediation and maturity transformation for growth.
- How much can ‘shadow’ banking sector take up the slack?
- Will macro prudential policies help markets overshoot less?