Financial Institutions, Markets and Regulation: A Survey

by T. Beck, E. Carletti and I. Goldstein

Discussion by A. De Vincenzo, Banca d’Italia

EUI, 6 June 2015

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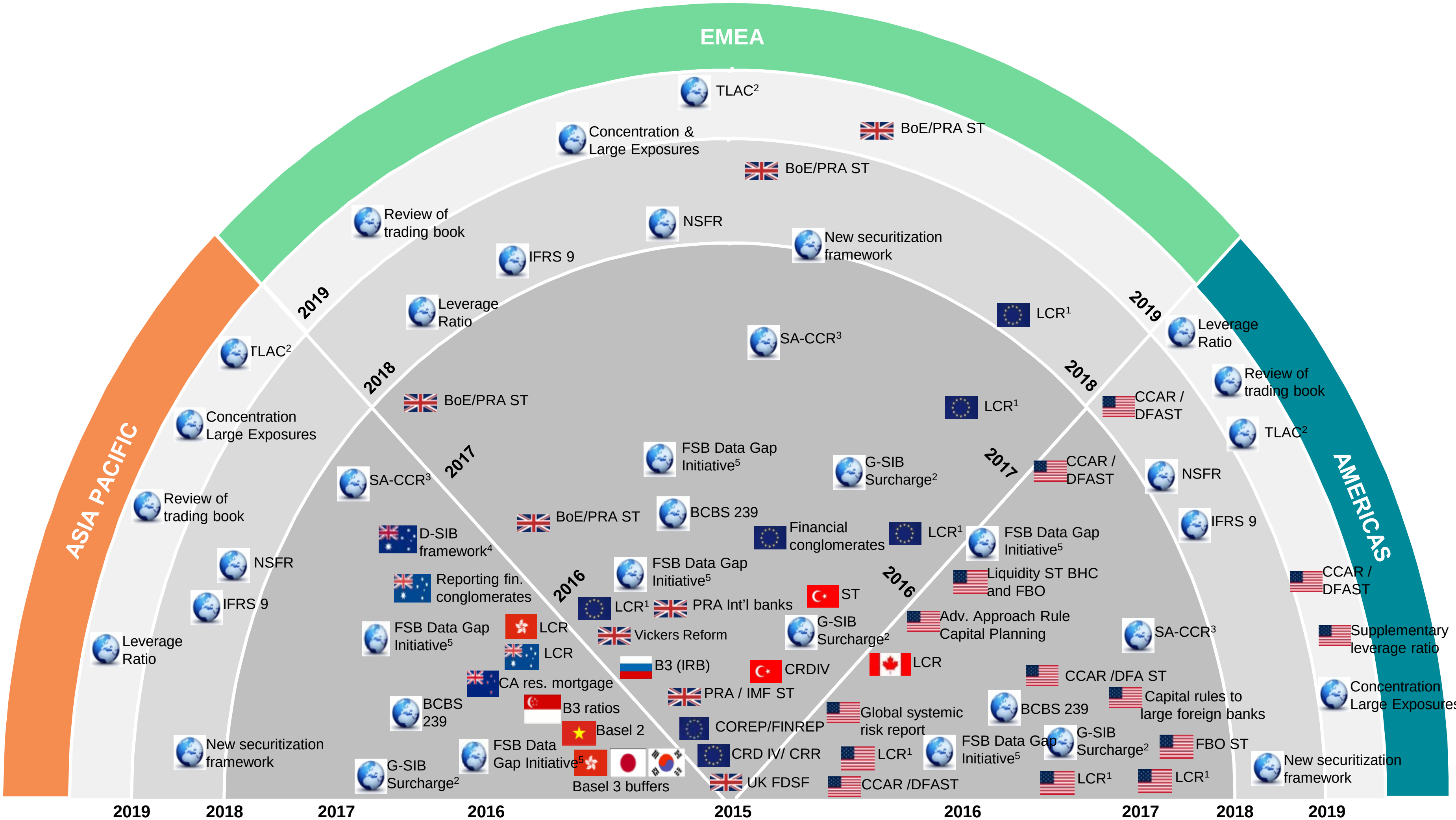
Global Banking Regulatory Radar



Source: Moody's Analytics. Analysis as of January 2015.

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Beck, Carletti & Goldstein Survey (I)

- Is there a way to rationalize regulatory reforms undertaken so far?

- Consider the following

PC x EAC x LGC = ELC, where:

- PC is the probability of a financial crisis;

- EAC is the exposure of the financial system to a crisis;

- LGC is the loss given crisis; and

- ELC is the expected loss of a financial crisis.

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Beck, Carletti & Goldstein Survey (II)

- The objective of the regulatory reforms is to influence PC, EAC and LGC, with a view to minimise ELC
- Then:
  - ✓ New capital, liquidity, leverage rules tend to decrease PC
  - ✓ New G/D-SIB buffers, leverage, structural (activity restrictions), market infrastructures measures tend to limit EAC
  - ✓ New resolution mechanisms, TBTF, TLAC tend to reduce LGC
- Regulatory and institutional reforms: the Banking Union

Beck, Carletti & Goldstein Survey (III)

- Many reforms have been agreed, but only partly implemented (some measures still need “calibration”); others are in the pipeline (for instance, IRRBB)

- Some fundamental contributions from economic and financial research are (still) needed:

  - ✓ Steady state vs Transition to new equilibrium (starting points matter!)

  - ✓ Macroprudential tools, early-warning models and (still diverse) economic/financial cycles

  - ✓ Institutions vs Markets (i.e., shadow banking and securitization): US vs Europe

Beck, Carletti & Goldstein Survey (IV)

"*The overhaul of the regulatory frameworks across the globe was not only the result of lessons learned from the recent crises but was also accompanied by extensive academic work. We have become better at measuring risk and designing regulatory tools to reduce build-up of systemic risk and manage it more effectively*"

- Partly agree…

"*[…] this leaves us with the unknown unknowns, including financial innovation leading to new business models and new structures in the financial system and thus new and future sources of financial fragility. As the financial system develops, research and analysis has to adapt to the dynamic nature of the financial system*"

- Fully agree!!!

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