The New Regulatory Paradigm: A Tectonic Shift for the Banking Industry

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I. Regulation after crisis

- Rationale
  - 29 crisis led to new rules: Glass Steagall Act; the creation of the SEC; the FDIC/Deposit Insurance;etc
  - After a crisis people demand more (not less) and better regulation
  - This crisis, naturally, also is leading to a deep change

- But we need to recognise the risks
  - unintended consequences (Regulation Q after 29 and MMFs)

II. Regulatory Paradigm after the 2007 Crisis

II.1. Content

- Dealing with the TBTF problem
- Increasing capital requirements: more quantity and higher quality
- Prudential supervision reinforcement
- Avoiding volatility and counter cyclical effects: buffers
- Liquidity
- Resolution
  - the single most important measure
  - huge discretionary powers of resolution authorities
- Others
  - Commercial banking vs investment banking:
    - Propietary trading / Vickers / Barnier
  - Bank levy

II. Regulatory Paradigm after the 2007 Crisis

II.2. Rules vs discretion

- A lot of rules <u>and</u> a lot of discretionary powers

- Difficulties for multiyear capital planning of banks

II. Regulatory Paradigm after the 2007 Crisis

II.3. Multiplicity of Authorities and international standards setters

- International
  - IMF / WB
  - G20 - FSB
  - BCBS / IOSCO / IAIS
  - IASB

- European
  - European Commission
  - ECB
    - Macroprudential ⇨ ESRB
    - Supervision: SSM
    - Monetary Policy
  - NCAs: for bank solvency, SECs, etc
  - Resolution: SRB and NRAs
  - European Supervisory Authorities: EBA, ESMA, EIOPA

II. Regulatory Paradigm after the 2007 Crisis

II.4. Complexity

- History of Time (S. Hawking): No one understands B III in full!!
- K planning 5 years ahead is mission impossible:
  - Pillar 1 floors
  - SREP: Pillar 2
  - MREL / TLAC
  - Buffers
  - Stress Test
- New one for this year: MDA in Europe

II. Regulatory Paradigm after the 2007 Crisis

II.5. Neverending history

- FSB: the end of the reform process
- Supervision: ok with K of banks
- But... B IV !!

II.6. Buffers…for nothing?

- LCR, CCB, KCB, etc.
- But practical difficulties to use in stress times. For instance, K buffers: supervisor will allow run down ?

II. Regulatory Paradigm after the 2007 Crisis

II.7. Internal Model Conundrum

- B IV: restrict models
- IFRS 9: EL Provisioning means the use of models
- Insurance in the EU: solvency II allows full portfolio models!

II. Regulatory Paradigm after the 2007 Crisis

II.8. Business Models

- Shadow Banking
  - Inconsistencies across sectors !
  - Same risk, same business, same rules !!
- I.T.
  - Challengers vs incumbents: remember Kodak…
  - Internal processes:
    - branches reduction
    - cost cutting opportunities
  - Reputation / Millenials
- Utilities model for banking
  - False: always cyclical

III. Impact on EME markets / banks

III.1.Complexity

- Airbus 380 vs “drone” banks!!

III.2.De - risking

- Focus in EU: reset the size of the banking sector
- Focus in US: reduce the size of banks (TBTF)
- But EME:
  - Financial deepening ⇨ bigger banks and bigger banking sector are needed

III. Impact on EME markets / banks

III.3.Renationalisation

- De-risking also at international level
- Not just regulation, also (even mostly) conduct of business rules / reputation / fines
- Two problems for EME:
  - Lack of basic services acces (money transfers, currency exchange, long term funding in USD, EUR,…)
  - Who fills the gap left by western banks?

IV. Conclussions

- Tectonic Shift
- New Regulatory Paradigm is here to stay…
- … but prepare for unintended consequences
- EME markets impact: role of IFC?

Thank you very much