

# *Five Years after Lehman's Collapse: Where are we going to?*

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Governor

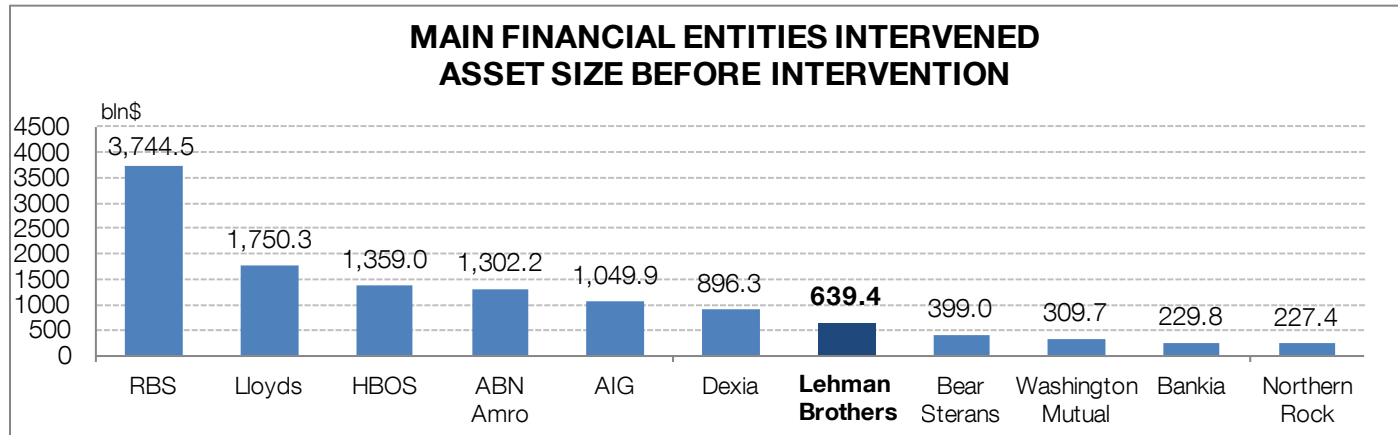
XCVII MEETING OF CENTRAL BANK GOVERNORS OF THE CENTER FOR LATIN AMERICAN MONETARY STUDIES

São Paulo

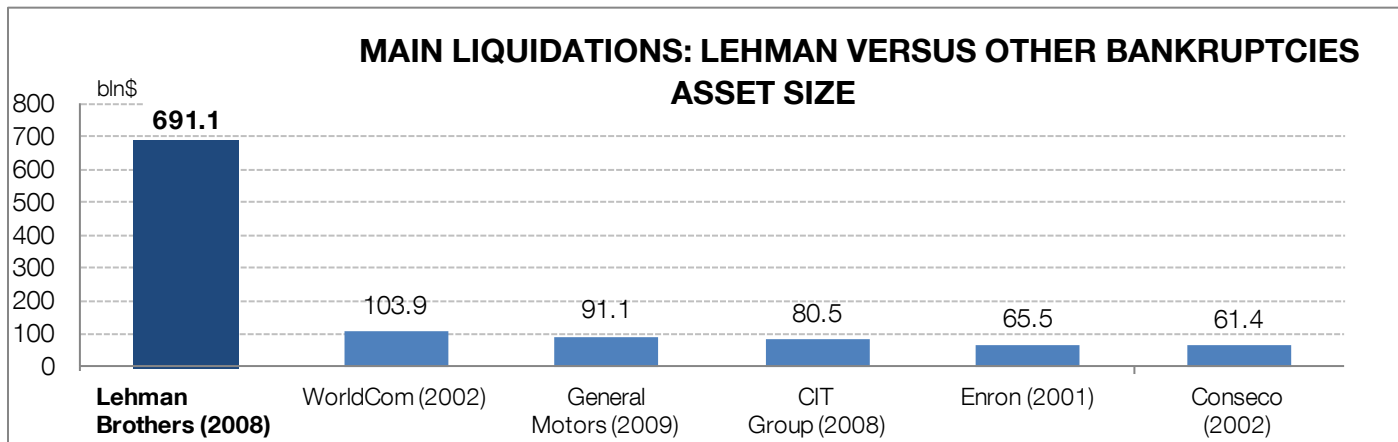
28 April 2014

# LEHMAN BROTHERS:

## Lehman was not one of the biggest failed banks

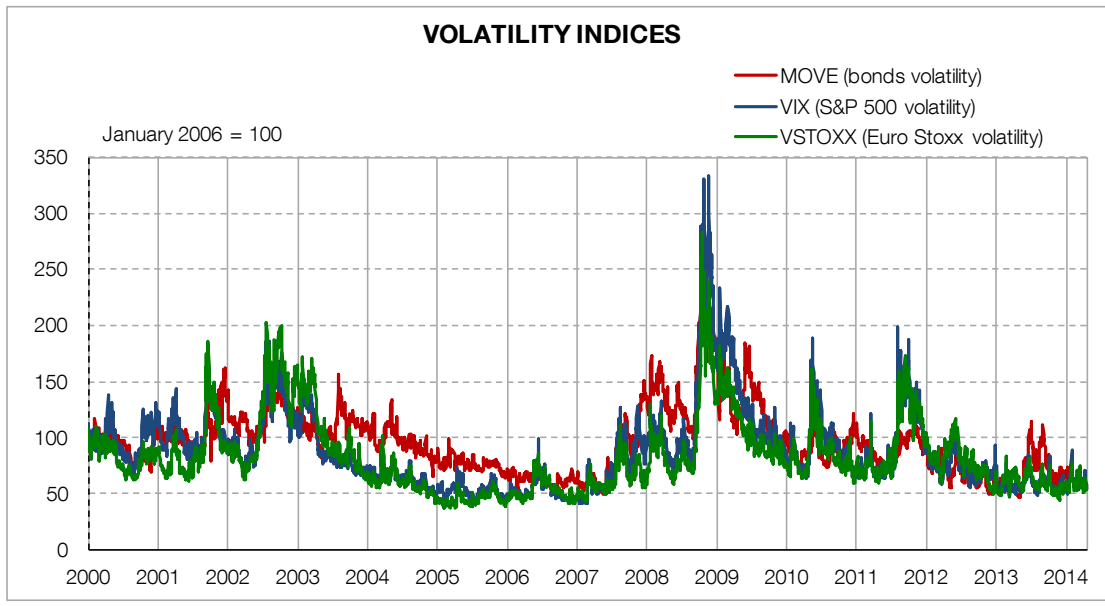


... but it was one of the biggest and more complex firms to be orderly liquidated by traditional channels

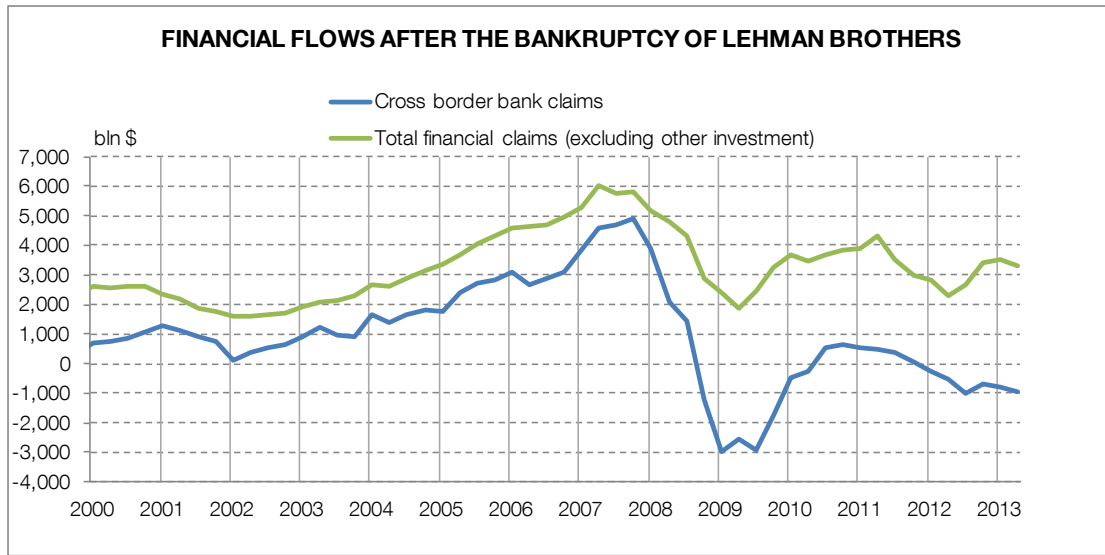


# Lehman's liquidation revealed how demanding was to solve complex and interconnected financial firms

Something that exacerbated global uncertainty



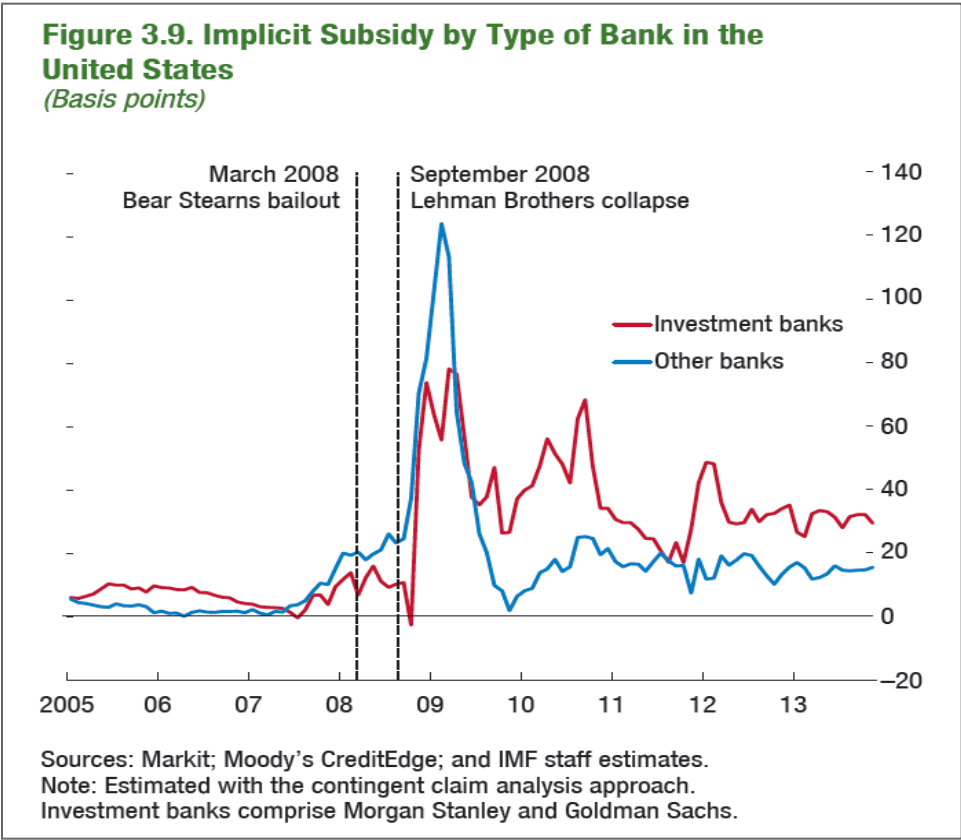
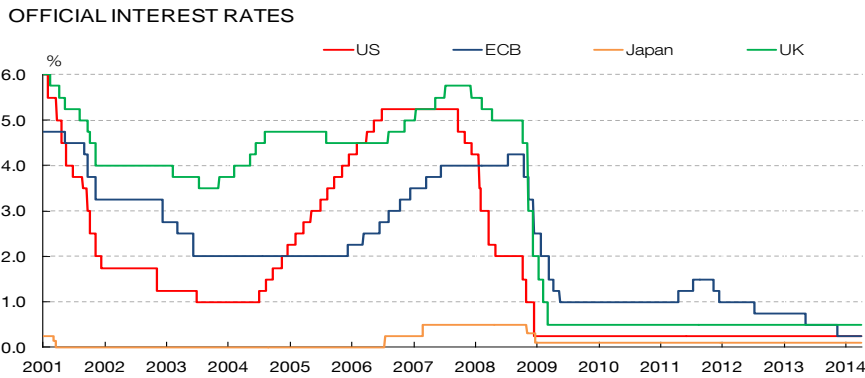
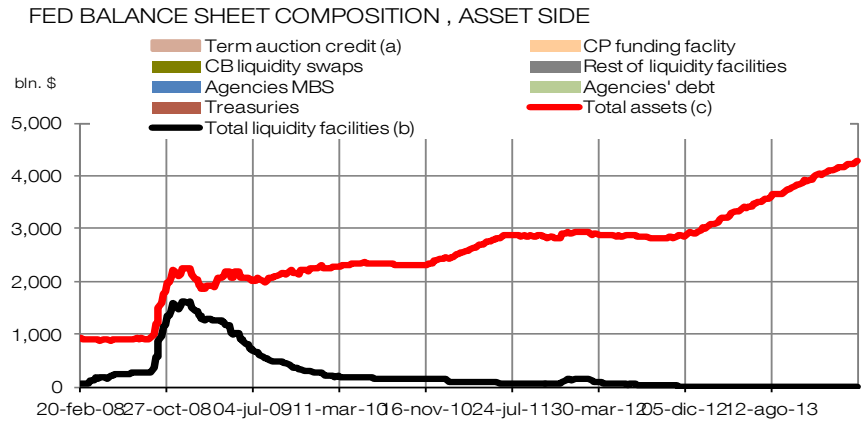
and reduced cross border financial flows



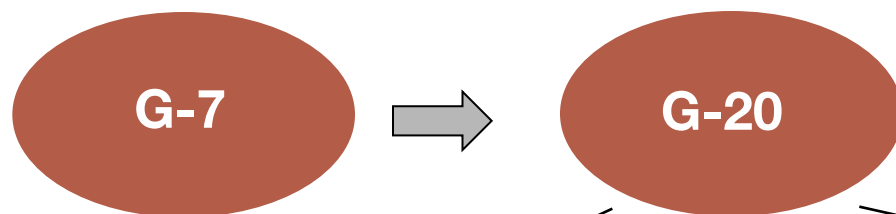
# Public authorities reacted with all the available tools to avoid a financial collapse

With conventional and unconventional monetary policies...

... at the risk of validating expectations that failed systemic banks will eventually be bailed out

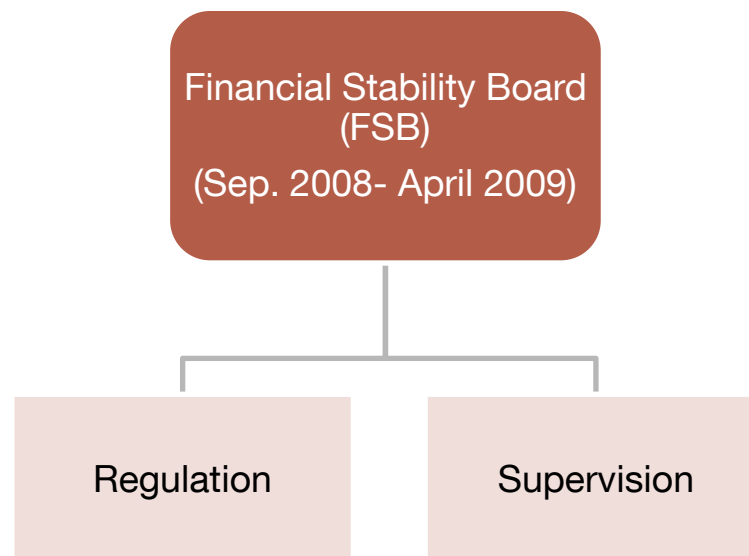
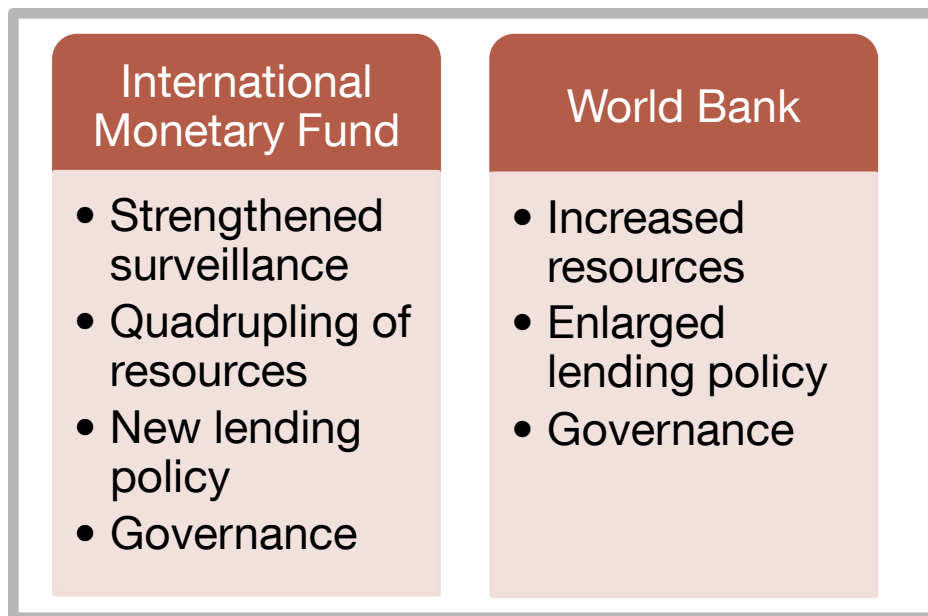


# NEW INTERNATIONAL ECONOMIC ORDER

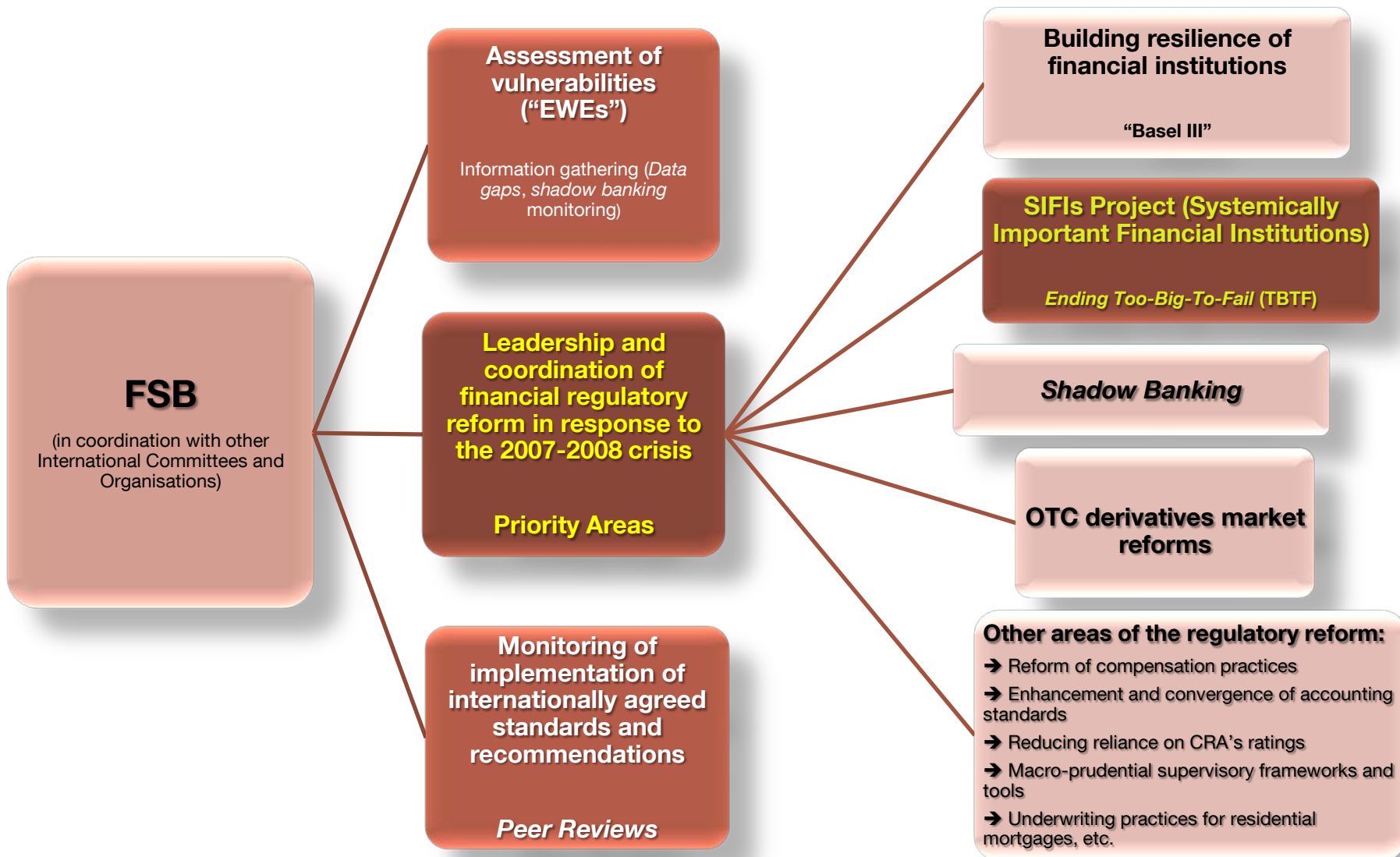


**Reform of Bretton Woods IFIs**

**New pillar of the International Economic Order**



# FSB. – PRIORITY AREAS OF THE REGULATORY REFORM



# FSB. – “ENDING TOO-BIG-TO-FAIL” PROJECT



## Identification of G-SIFIs capital surcharges

- **TARGET:** Reducing probability of failure of a G-SIFI
- Annual publication of the list of G-SIBs (Global Systemically Important Banks)
- Capital surcharges, 5 buckets: 1%, 1,5%, 2%, 2,5% and a 5th “empty bucket” with a 3,5% surcharge (to avoid that firms become more systemic)

## Resolution

- **TARGET:** Reducing the impact in case of failure of a G-SIFI
- *Key Attributes of Effective Resolution Regimes* (“KA”) → New international standard for the resolution of financial institutions

## Intensity and Effectiveness of Supervision

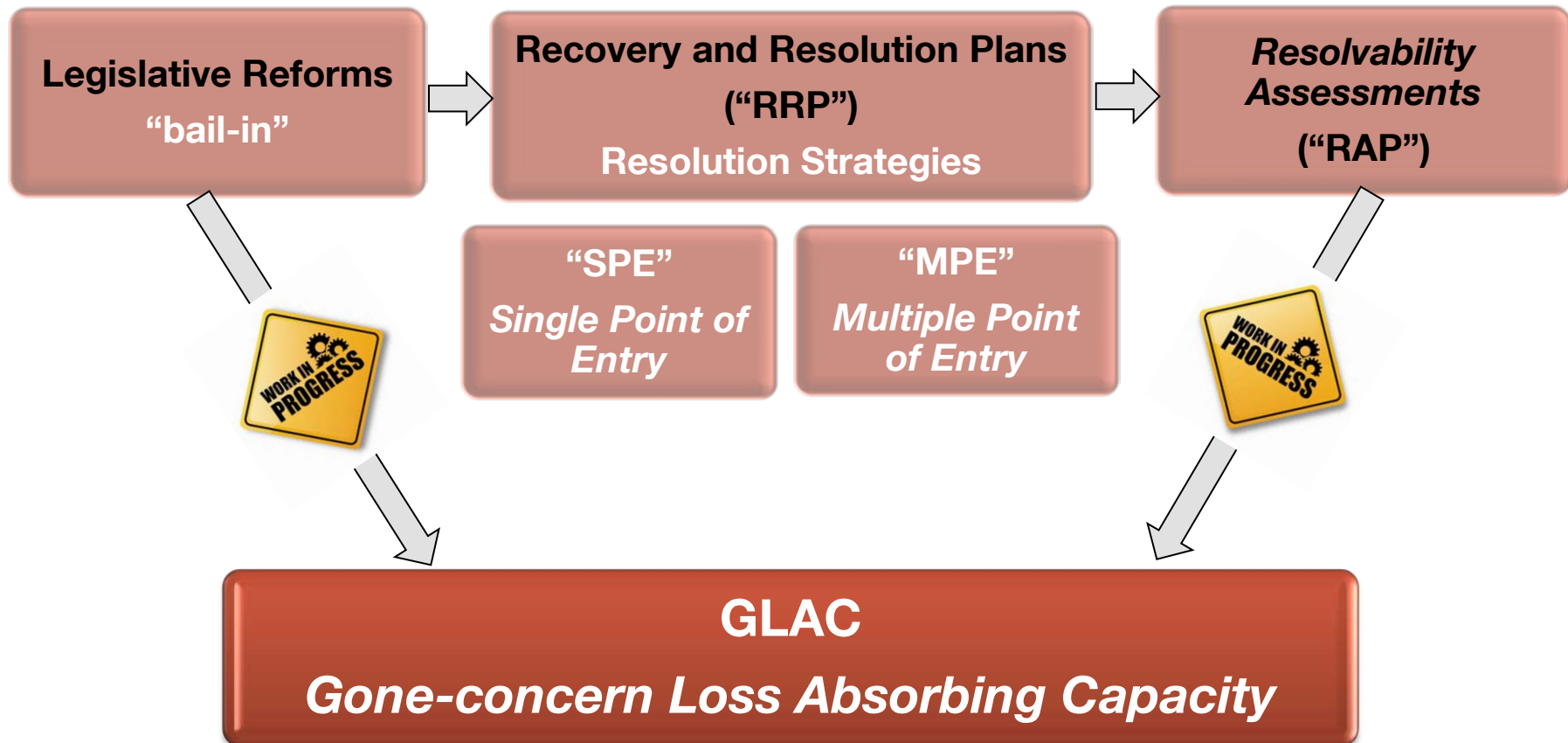
- **TARGET:** Reducing probability of failure of a G-SIFI
- Supervisory Independence and Resources
- Enhancing supervisory practices of systemic groups.





## Key Attributes of Effective Resolution Regimes

(FSB, October 2011)







# STRUCTURAL REFORM PROPOSALS



## A comparison of selected structural reform proposals

	<b>Volcker</b>	<b>Liikanen</b>	<b>Vickers</b>
Broad approach	<b>Institutional separation</b> commercial banking and investment activities have to be separated	<b>Subsidiarisation</b> Proprietary and high-risk trading activity in separate legal entities	<b>Ring-fencing</b> Structural separation of activities via a ring fence for retail banks

- **Alternative domestic initiatives**

- **Need for international coordination**



# **FIVE YEARS AFTER LEHMAN'S COLLAPSE: WHERE ARE WE GOING TO?**



- ❑ Regulatory and supervisory initiatives in response to the international financial crisis (in particular after Lehman failure)**
  - ❑ New institutions + significant reform of existing ones**
  - ❑ New rules, especially for internationally active banks**
- ❑ A credible and effective global resolution regime for SIFIs**
  - ❑ Advances but still some key aspects under discussion**
- ❑ Impact of regulatory and supervisory changes in financial intermediation**
  - ❑ Financial stability, financial complexity and financing of growth**
  - ❑ Perspectives for bank businesses**
    - Structural reforms**

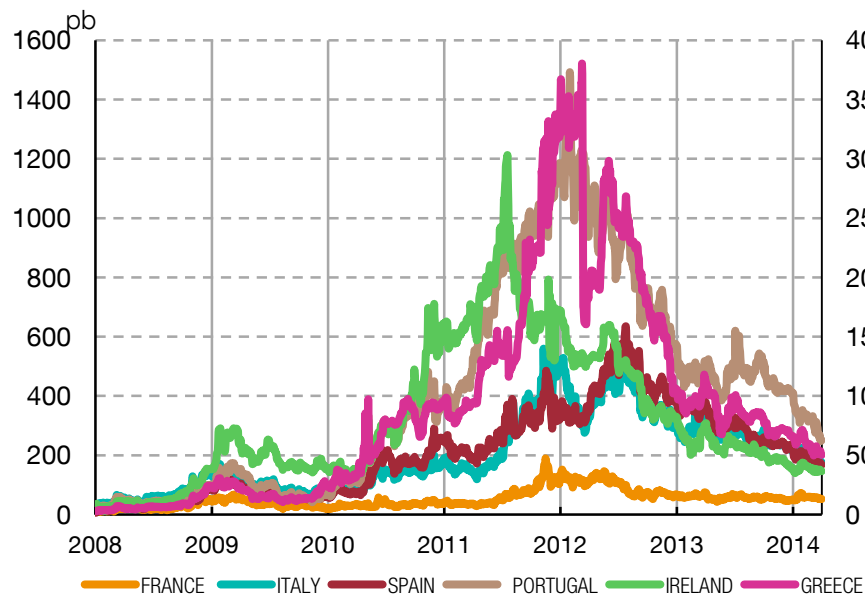


# **EURO AREA : CRISIS AND AUTHORITIES' RESPONSE**

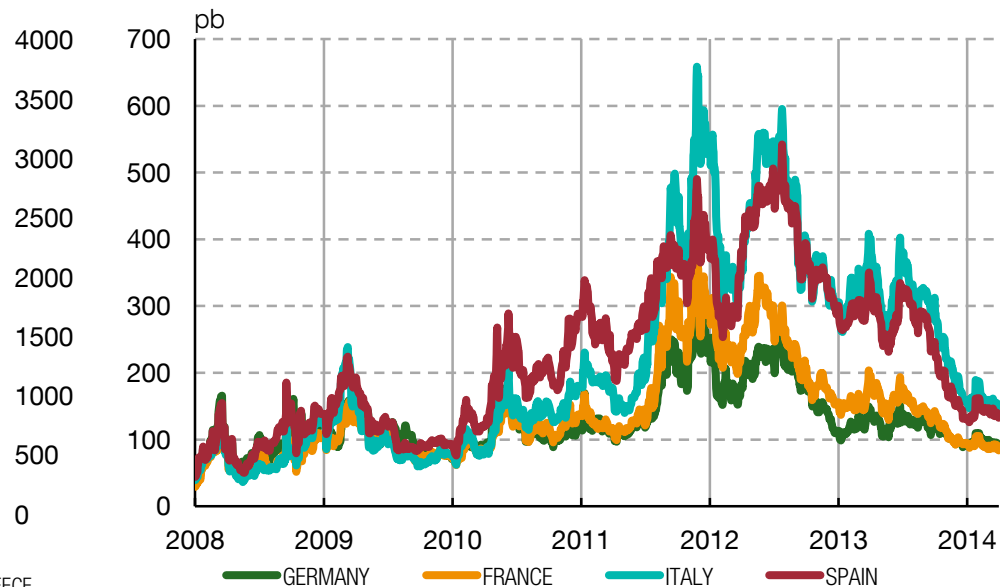
# THE EUROPEAN SOVEREIGN DEBT CRISIS

- The Greek crisis expanded to Euro area countries that had accumulated macroeconomic imbalances and vulnerabilities.
- Fragmentation of financial markets
- Sovereign and banking risk link

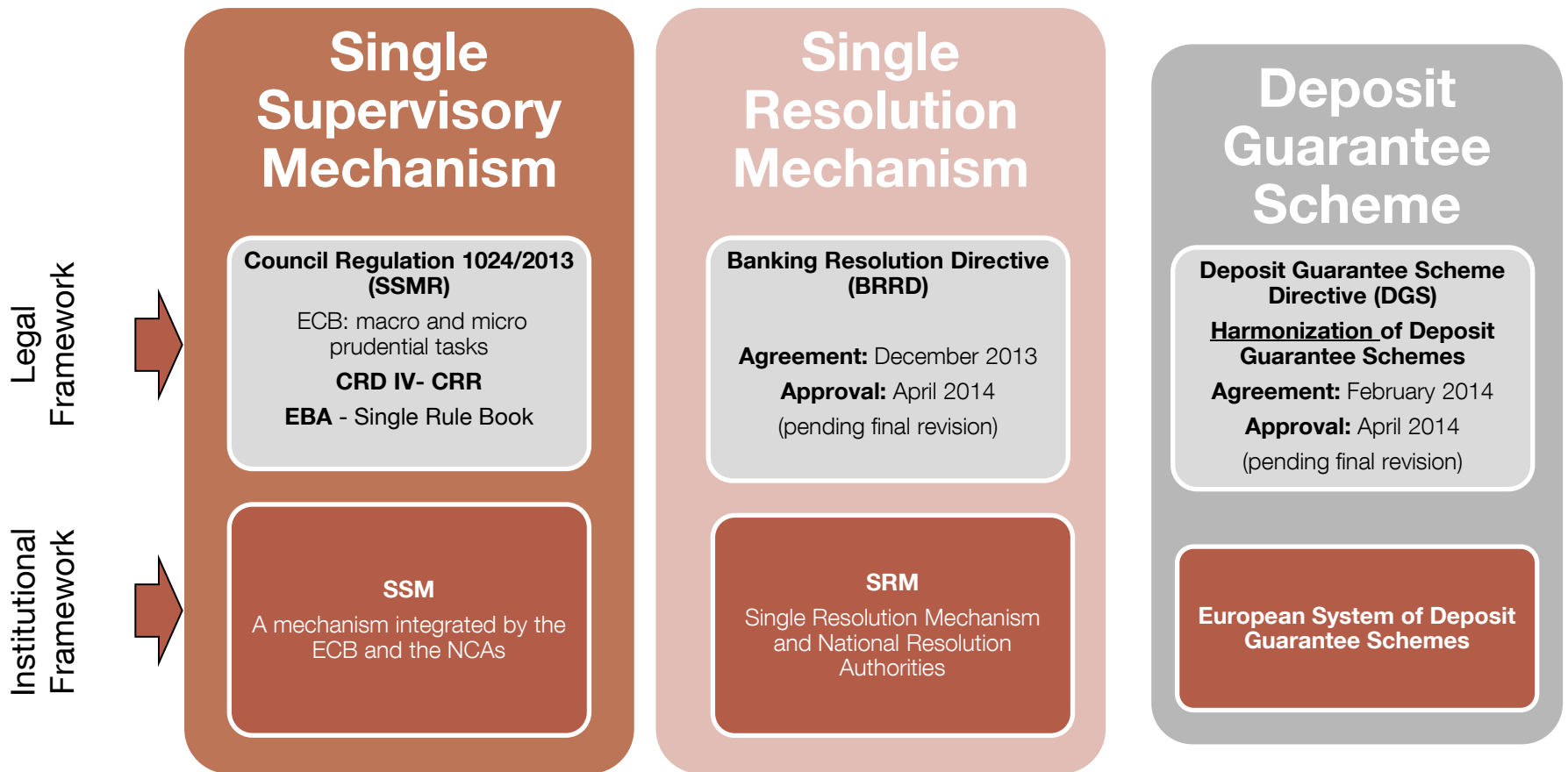
TEN YEARS SOVEREIGN SPREADS OVER GERMANY



5 YEARS BANKS CDS



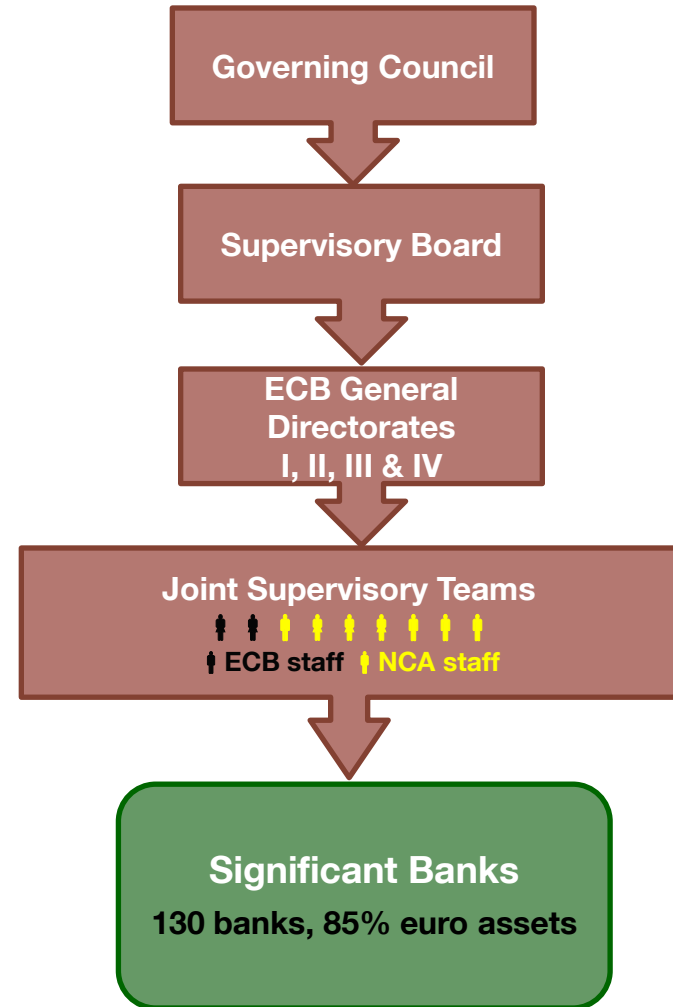
# BANKING UNION



# SINGLE SUPERVISORY MECHANISM (MICRO PRUDENTIAL SUPERVISION)

**SSM = ECB supported by National Competent Authorities (NCAs)**

- ❑ **Perimeter: euro zone plus opt-in non euro countries**
- ❑ **Significant banks**
  - ❑ Size: Assets > €30 billion
  - ❑ Importance: > 20% GDP
  - ❑ Cross-border activities
  - ❑ The three most significant credit institutions in each jurisdiction
- ❑ **Micro prudential supervision**
  - ❑ Significant Banks → ECB Direct supervision → Joint Supervisory Teams
  - ❑ Other Banks → ECB indirect supervision → NCAs
- ❑ **Joint Supervisory Teams (JST)**
  - ❑ ECB Coordinator
  - ❑ National Subcoordinators
  - ❑ Supervisors ≈ 1 BCE by 3,3 NCAs





# COMPREHENSIVE ASSESSMENT

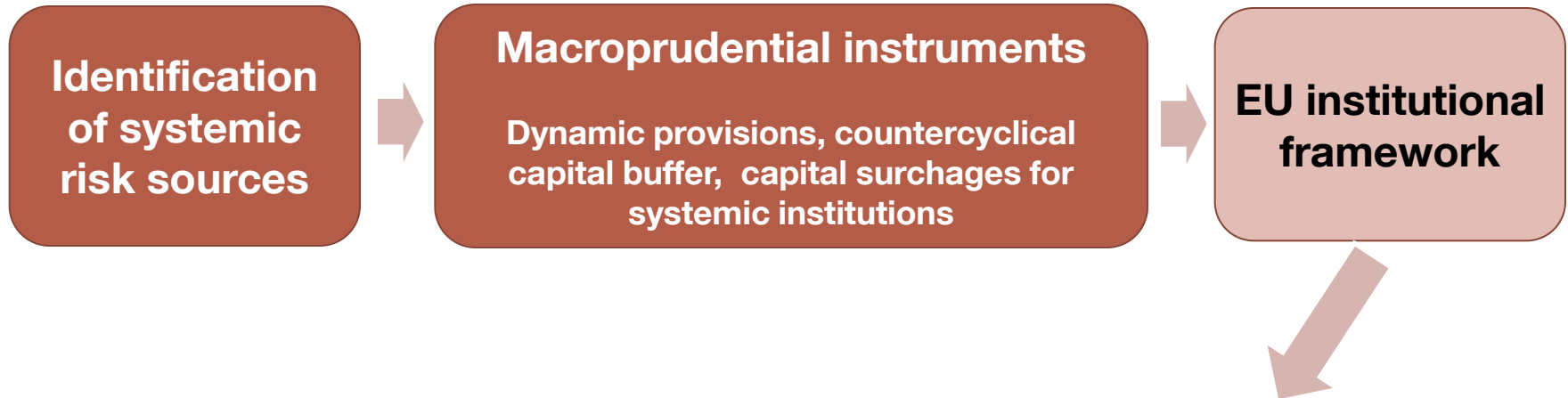


- Two main elements: **Asset Quality Review and Stress Test**
- Objective twofold: improve transparency and recapitalize viable banks with inadequate solvency levels → **final objective: strengthen confidence in the soundness of European banks**
- The **Asset quality Review** will examine the asset side of bank balance sheets as at 31 December 2013
- **The stress test** is a forward-looking exercise, which analysis the ability of institutions to maintain adequate solvency levels in stressed scenarios
- The relevant **thresholds already established**: 8% CET1 in the baseline scenario ; 5.5% under the adverse scenario
- **Publication of the results in late October**, before the ECB takes over the supervision of significant institutions on 4 November





- ❑ **Microprudential policy was not enough , there is a need to address system-wide risks**
  - ❑ **Risks across the banking sector:** Size, interconnections, complexity, etc.
  - ❑ **Cyclical risks: Excessive credit growth, possibly concentrated (eg: real estate),** excessive maturity mismatch, misaligned incentives, excessive leverage, etc.



- ❑ **ESRB:** Macroprudential oversight of the financial system within the EU
- ❑ **ECB:** Share macroprudential powers with SSM national authorities
- ❑ **National Authorities:** Implement macroprudential policies at national level

# SINGLE RESOLUTION MECHANISM (SRM)

## Geographical Scope: as the SSM

## Single Resolution Board (SRB):

- Plenary Board → General Rules
- Executive Board: 5 members and the National Resolution Authority on an ad-hoc basis → For a specific bank

## Single Resolution Fund (SRF)

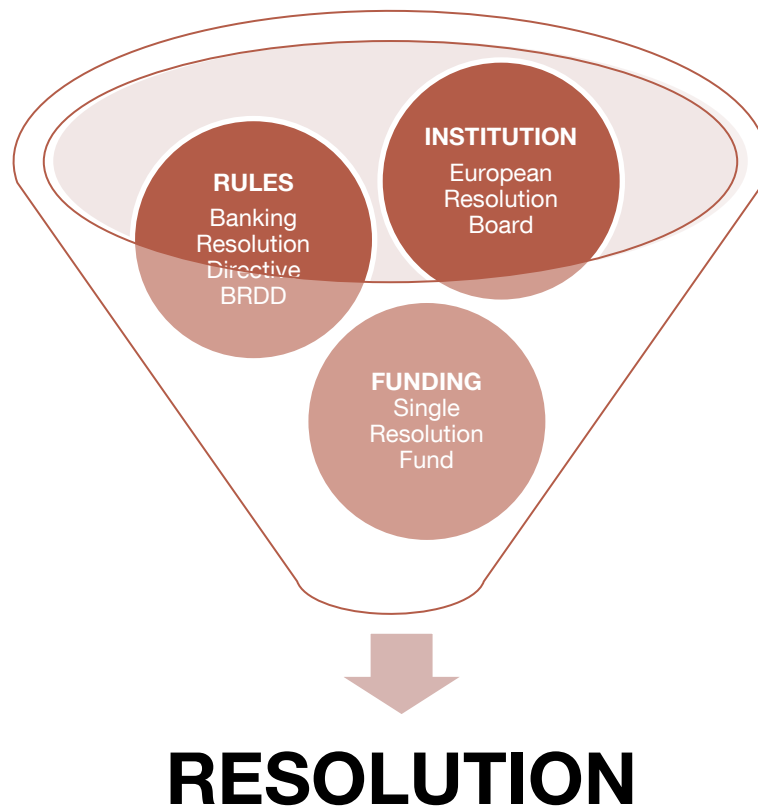
- Industry contributions ranging from €55-60 billion
- National buckets
- Progressive mutualization from 40% in 2016 up to 100% in 2023

## Decision process: as in the SSM

- SSM Significant banks and cross border entities → Direct Resolution by the SRB
- Other entities → National Authorities

## Resolution steps

- Bail-in: minimum 8% assets
- Single Resolution Funds
  - 1<sup>st</sup> National buckets
  - 2<sup>nd</sup> Other buckets (mutualization calendar)
- Additional industry contributions, or national public backstop





- **International Coordination:**
  - How much international coordination of financial regulation is needed? Are we making (un)even progress depending on the topic at stake? Are there any areas requiring further harmonization? Is the system becoming too complex?
  - Banks versus other intermediaries and their role in financial intermediation: Implications for financial stability and economic growth.
  - Is there a need for greater cooperation and harmonization on entities' supervision and resolution?



**THANK YOU FOR YOUR ATTENTION**