CITY UNIVERSITY LONDON

CITYPERC
City Political Economy Research Centre

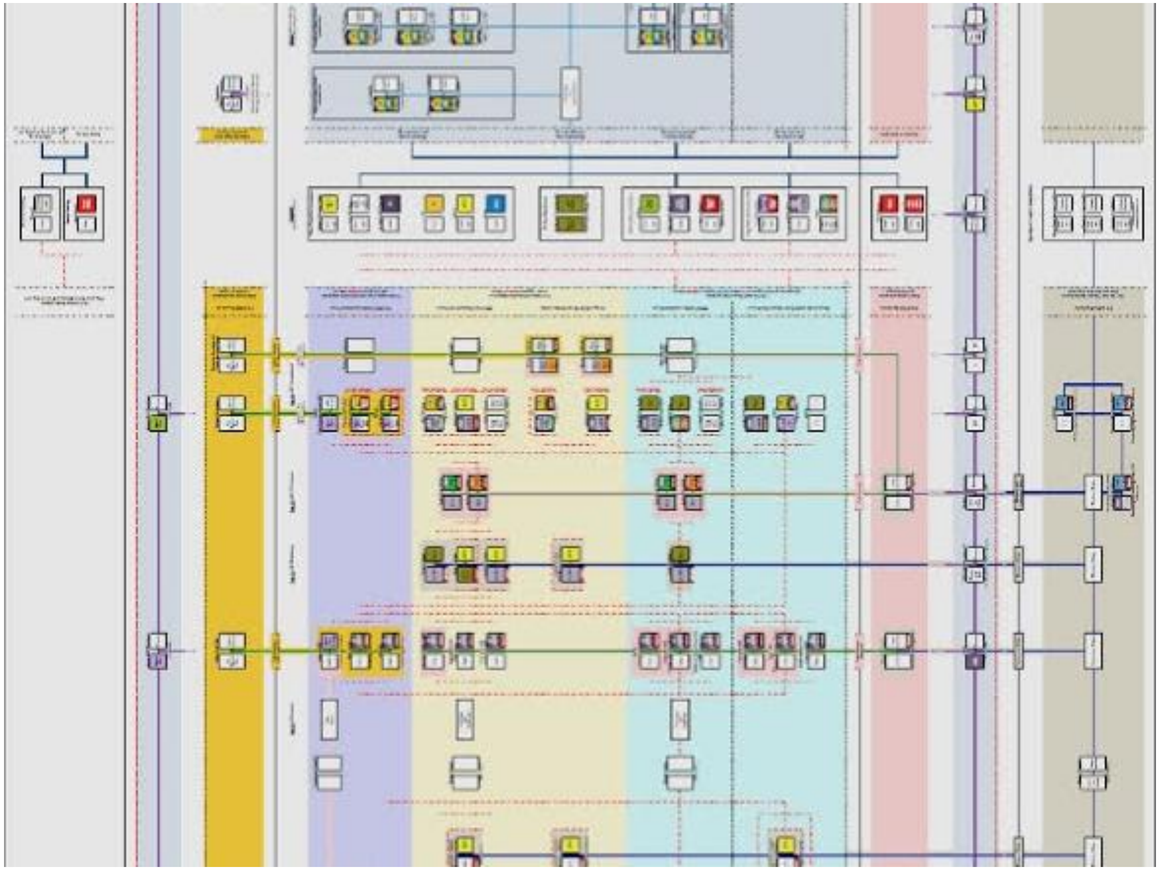
cost
EUROPEAN COOPERATION IN SCIENCE AND TECHNOLOGY

Shadow Banking or Market Finance? Regulatory Politics in the EU and UK

Brooke Masters, Financial Times

City University, London

1 February, 2013



The Scale of Shadow banking

In July 2010, researchers at the Federal Reserve Bank of New York tried to represent shadow banking on a graphic.

This is a small section of the 4 ft by 5ft. Poster.

Financial Assets by Type of Institution

Total assets of financial intermediaries in 20 jurisdictions and euro area

In USD trillion

	Central Banks	Banks	Insurance Companies and pension funds	Public Institutions	Other Financial Intermediaries
2007	10.1	103.6	40.3	11.8	62.0
2008	14.7	118.2	35.8	12.8	59.4
2009	15.1	116.8	40.4	12.7	63.8
2010	16.6	120.7	43.6	12.6	66.9
2011	20.4	130.2	42.9	12.5	66.6

Source: National flow of funds data, FSB

Other Financial intermediaries has dropped slightly from 27 per cent to 24 per cent since the crisis

The Financial Stability Board

- Five goals unveiled in November 2012
  - Limiting the spill over between shadow banks and the banking system
  - Reducing the vulnerablity of money market funds to runs
  - Spotting and controlling risks from new and unregulated forms of shadow banks
  - Dampening the procyclicality of securities lending and repo and other secured lending

What the Global Regulators Say

"Shadow banking is like cholesterol. There is good and there is bad. Now we've got the really difficult job of getting the national authorities to dive in and determine [which part] of that $67tn really worries us,"

Lord Adair Turner, FSA Chair

European Commission

- Green paper on shadow banking put out in March 2012 defines shadow banking as
  - accepting funding with deposit-like characteristics
  - performing maturity and/or liquidity transformation
  - undergoing credit risk transfe
  - using direct or indirect financial leverage

What the Commission thinks

- *"What lessons have we drawn from the crisis if we allow risky activities to prosper alongside better regulated and more solid ones?"*

- *"We must still proceed with caution. I am aware of the complexity of the issue, and especially of the need to ensure consistent regulation for all players while not calling into question the alternative sources of financing that can be so beneficial to the real economy."*

  -- Michel Barnier, EU Commissioner

European Commission

- Focused on
  - Special purpose vehicles
  - Money market funds
  - Investment funds including ETFs that provide credit or use leverage
  - Finance companies and securities entities that provide credit
  - Insurers who provide or guarantee credit products

EU Regulatory attitudes to nonbanks

- AIMFD – rein in the “rapacious” hedge funds and “asset stripping” private equity houses
  - Introduced 2009, passed 2010, technical standards Dec 2012
  - Switzerland adopting similar rules so that its funds will be able to market in the EU
- ETFs – fear they are being used like SPVs and may contribute to runs (Esma guidelines 2012)

Changing tone?

– FSB consultation in November 2012 specifically noted that shadow banking provides

“a valuable alternative to bank funding that supports real economic activity”

– Mark Carney repeated this view on Monday in Zurich

– But the FSB also said it would work this year on resolution plans for nonbanks, suggesting they still believe large nonbanks pose a threat