BANK FOR INTERNATIONAL SETTLEMENTS

Would macroprudential regulation have prevented the last crisis?

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Discussion by

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The views expressed are the presenter only and not necessarily those of the BIS

The paper in a nutshell

- Research questions
  - How well equipped are today's macroprudential regimes to deal with a re-run of the factors that led to the GFC?
  - What are the main differences between the US Financial Stability Oversight Council (FSOC) and the UK's Financial Policy Committee (FPE) in implementing policy actions?
- Methodology
  - Identification of the key fault lines that arose prior to the GFC
  - Ask what MaPs tools would be necessary to address these fault lines

Main results

- Two broad factors were crucial for the GFC (at least in the US)

  1. Fragilities in the financial system associated with excessive leverage and use of flighty short term funding
     - Broker-dealers, CP, MMFs, REPOs and credit lines
  2. Lending boom to household sector
     - Home equity lines of credit, subprime and flat LTV

- Total US GDP shortfall is 8.5%
  - Credit crunch 3% + household deleveraging 4.6%

- Could MaPs have prevented the GFC?
  - "Perhaps". UK FPE better chance than US FSOP because it has necessary mandate and powers

Two main comments

I. Future threats to financial stability may come from very different sources

II. Need for a more holistic approach

I. What will be the source of next fragility?

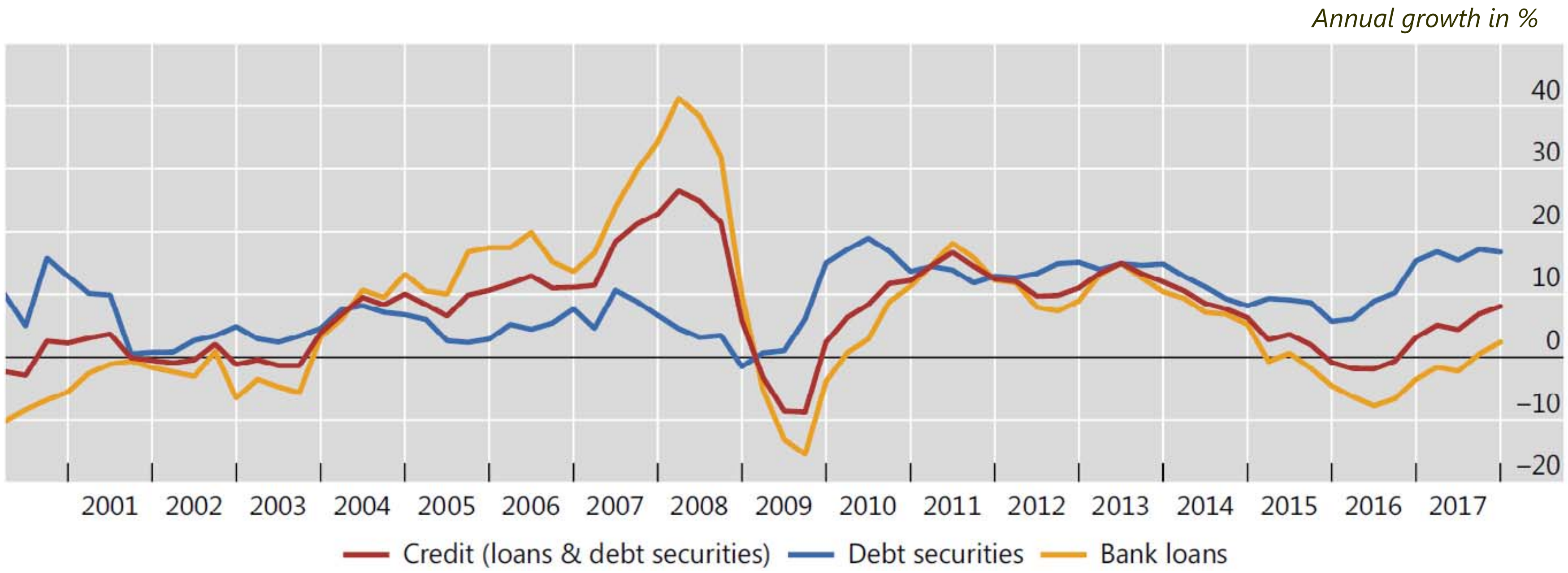
Financial intermediation is evolving

- Changes in bank business models
  - Reduction in cross-border funding
  - Impact of structural reforms on internal capital markets

- Technology advances and entry of new players (Fintech)
  - More “transactional” lending
  - Different “originate-to-distribute” model

- Move towards more marked-based finance
  - “Second phase of global liquidity” (Shin, 2013)
  - Long period of subdued cross-border bank flows, associated with a surge in the issuance of international debt securities

US dollar-denominated credit to EME non-banks



Source: Avdjiev et al (2018); BIS global liquidity indicators.

II. Need for a more holistic approach

MaPs and other policies

- MaPs and monetary policy
  - Risk taking channel (Adrian and Shin, 2014; Borio and Zhou, 2014)
  - Complements vs substitutes (Gambacorta and Murcia, 2017)
- MaPs and Fiscal Policy
  - Tax code could influence credit and asset prices
  - Sovereign-Banks nexus (Borio et al, 2018)
  - Necessity to create sufficient fiscal space to address crisis
- MaPs and Structural Policies
  - Flexibility in labour and product markets

Conclusions

- Well developed analysis, but what next?
- Driving factors and response to the next GFC will be different
- Need to consider how MaPs interact with monetary policy, fiscal policy and are influenced by structural polices on labor and product markets
- MaPs are more effective if embedded in a broader macro-financial stability framework and coordination with other policies (BIS, 2018)

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