

Keynote address: Have we fixed the fractures in the global financial system revealed by the financial crisis

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Have we fixed the hidden fractures in the financial system?

Howard Davies

Chair – RBS

Professor – Sciences Po

FSI 20th Anniversary

13 March 2019, Basel



in association with the
Securities and
Investments Board



FINANCIAL STABILITY

r e v i e w



IN THIS ISSUE

Culture of regulation

Following the Bank of England's Review of Supervision, the Deputy Governor looks at two different views of the relationship between institutions and their supervisors.

Electronic money

Several different types of 'electronic money' are currently under development. What new public policy issues arise, and how might central banks best respond to them?

Building society conversions

Many building societies are converting into banks. This will involve changes for them and for their regulators. What are the reasons for this trend, and how should the conversion process be handled?

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Consensus on the policy response to the crisis remains elusive

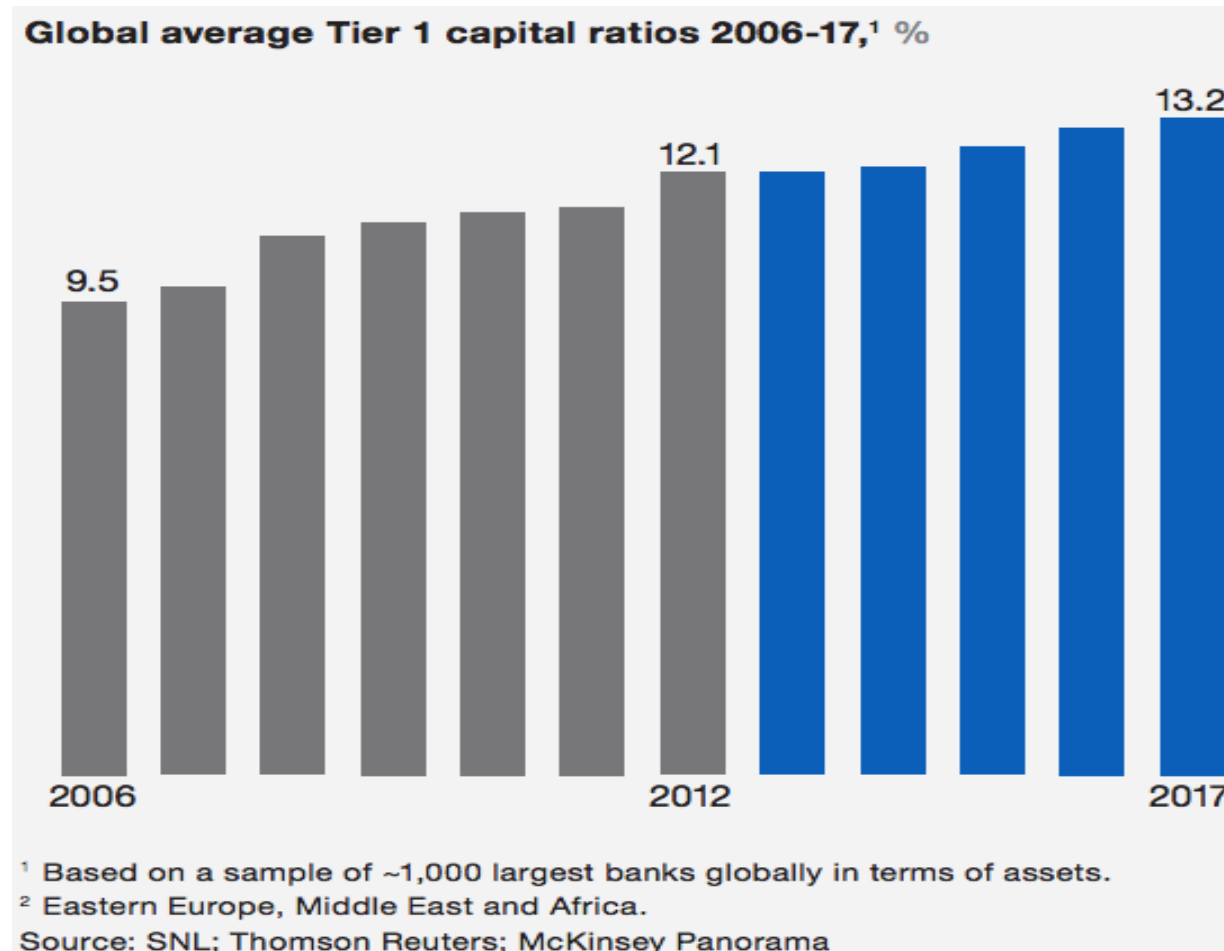


Three songs are sung:

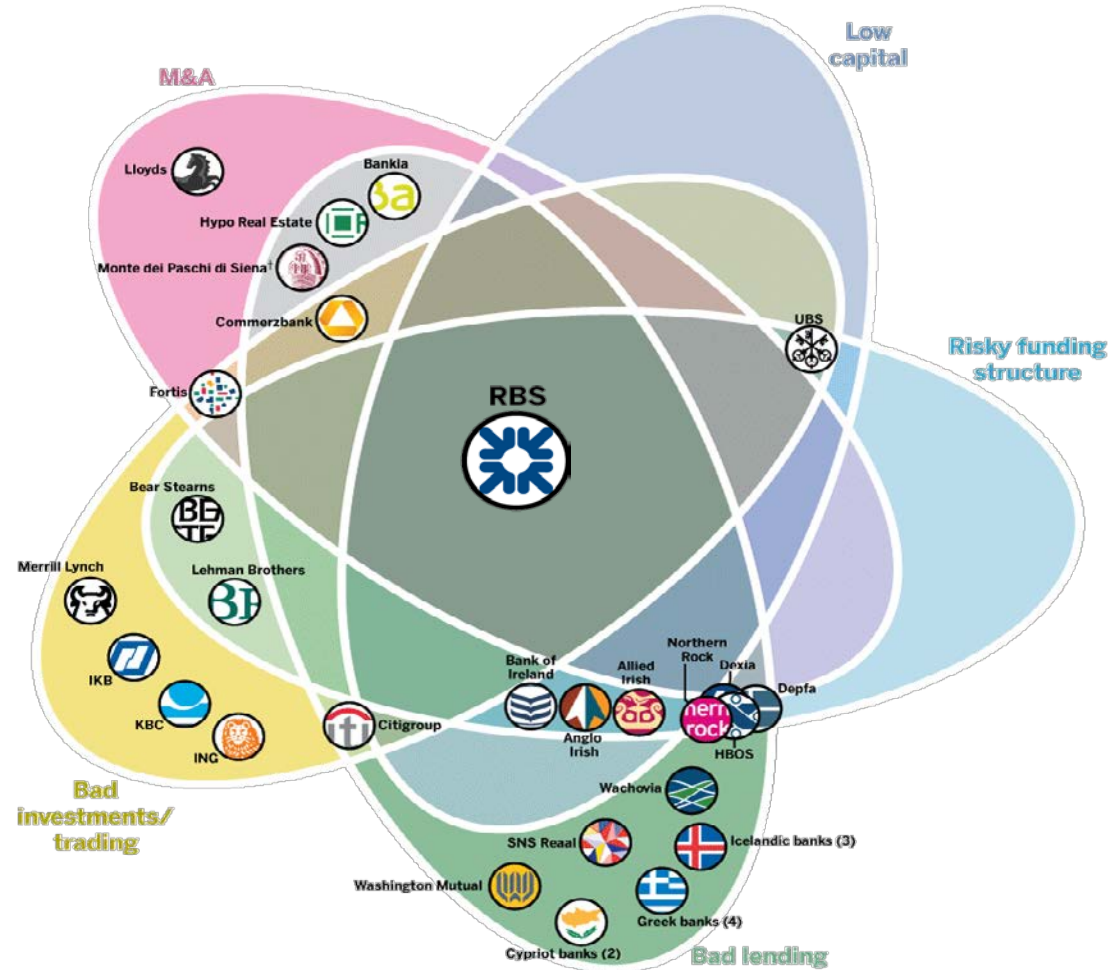
1. We don't need no education...

Hey, teachers, leave us kids alone (*Pink Floyd*)

Bank capital has risen



RBS managed a unique full house of problems



Source: Financial Times

Consensus on the policy response to the crisis remains elusive



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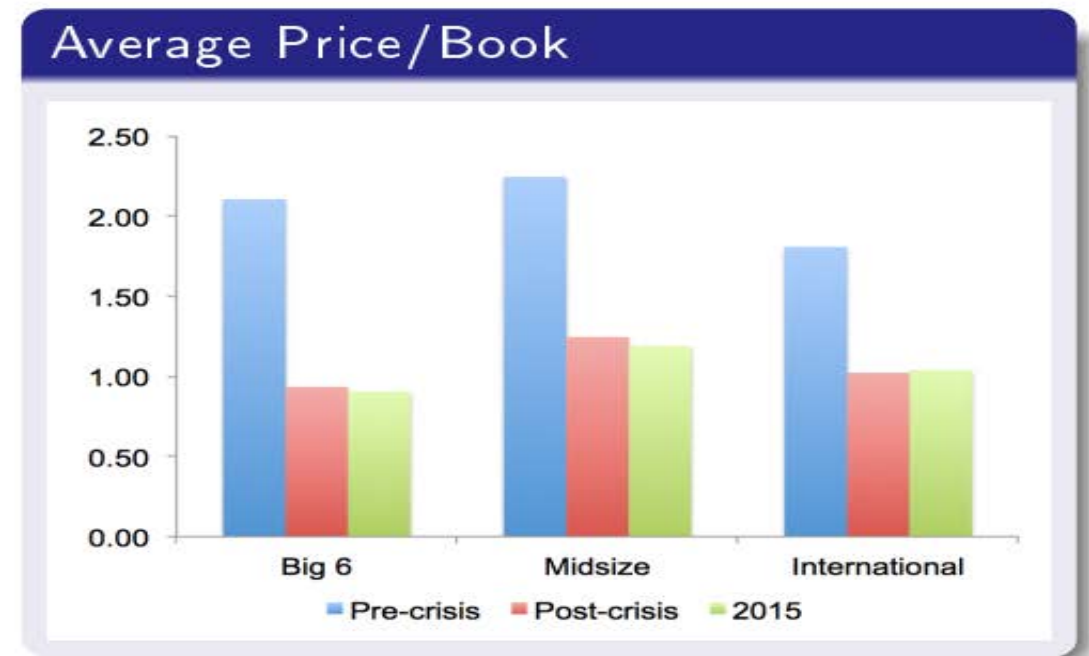
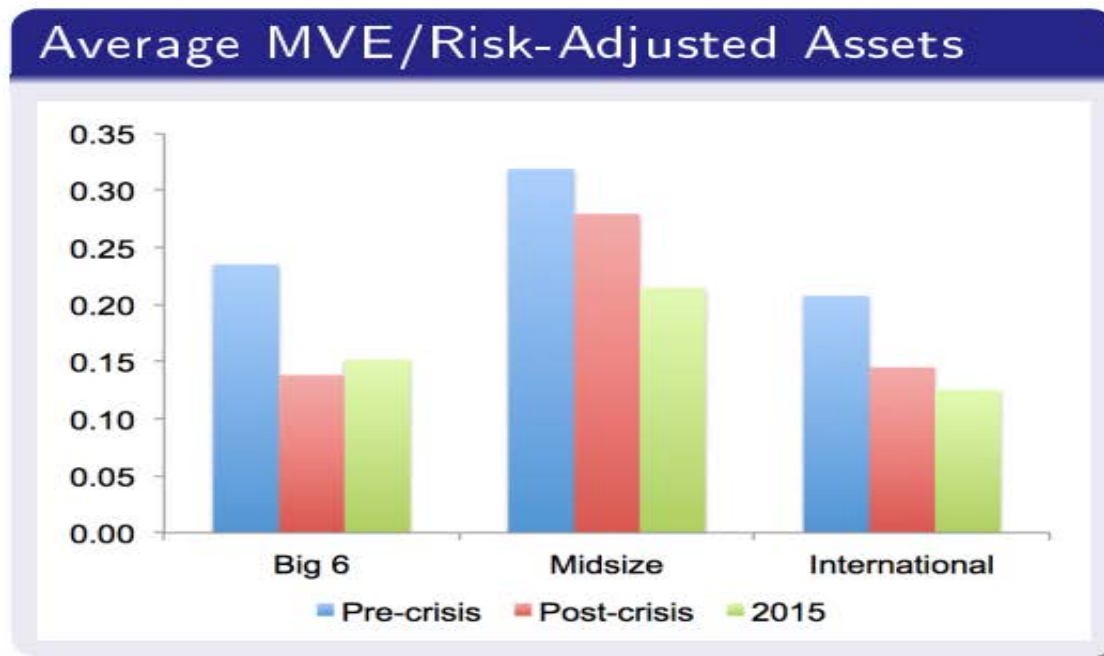
Hey, teachers, leave us kids alone (*Pink Floyd*)

2. Towers of gold are still too little

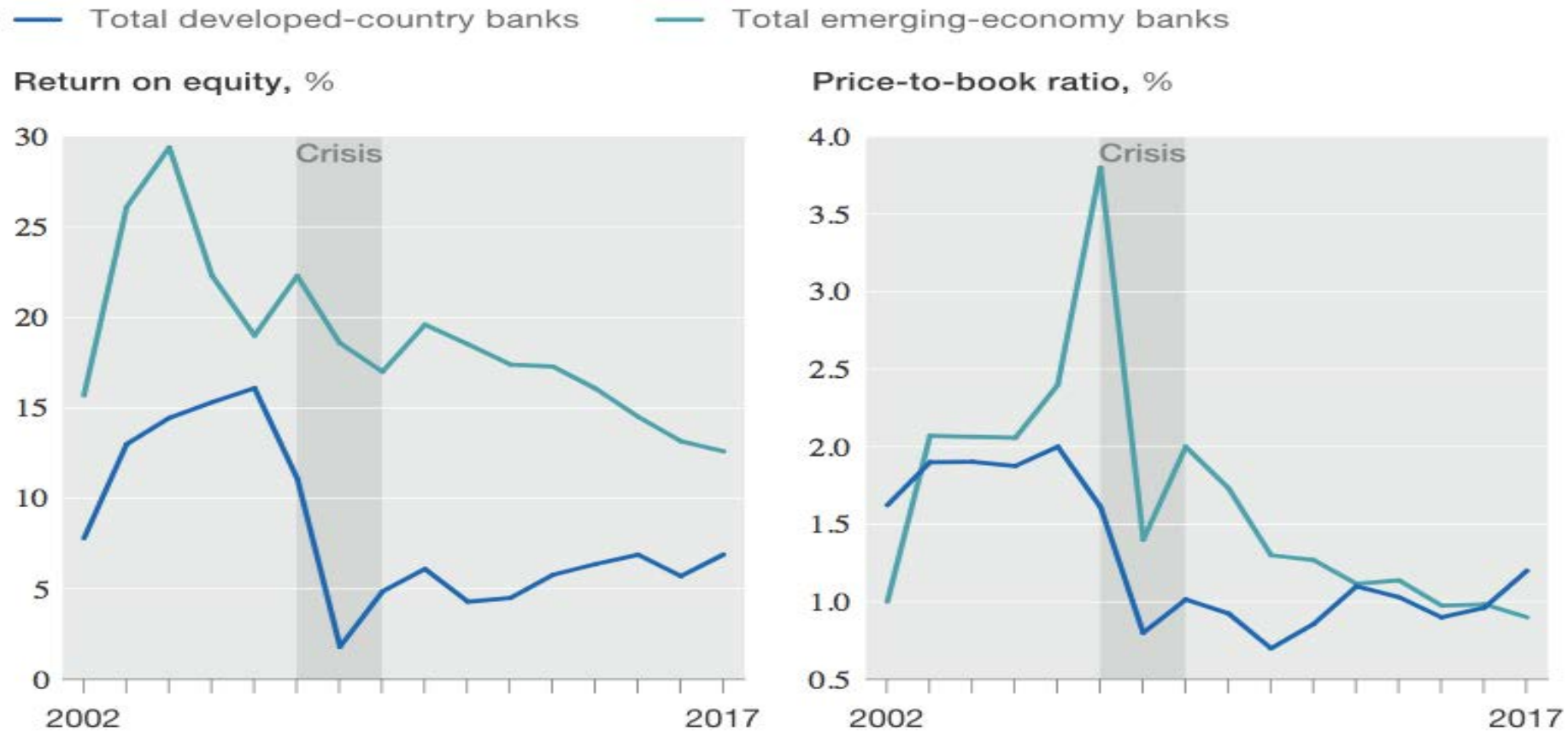
Their hands could hold the world but it'll

Never be enough (*Loren Allred*)

Market measures of equity capital suggest limited improvement



Banks remain weakly profitable and poorly rated by investors



Note: Analysis includes ~1,000 banks in 70 countries, each with total assets exceeding \$2 billion. They account for ~75 percent of global bank assets.

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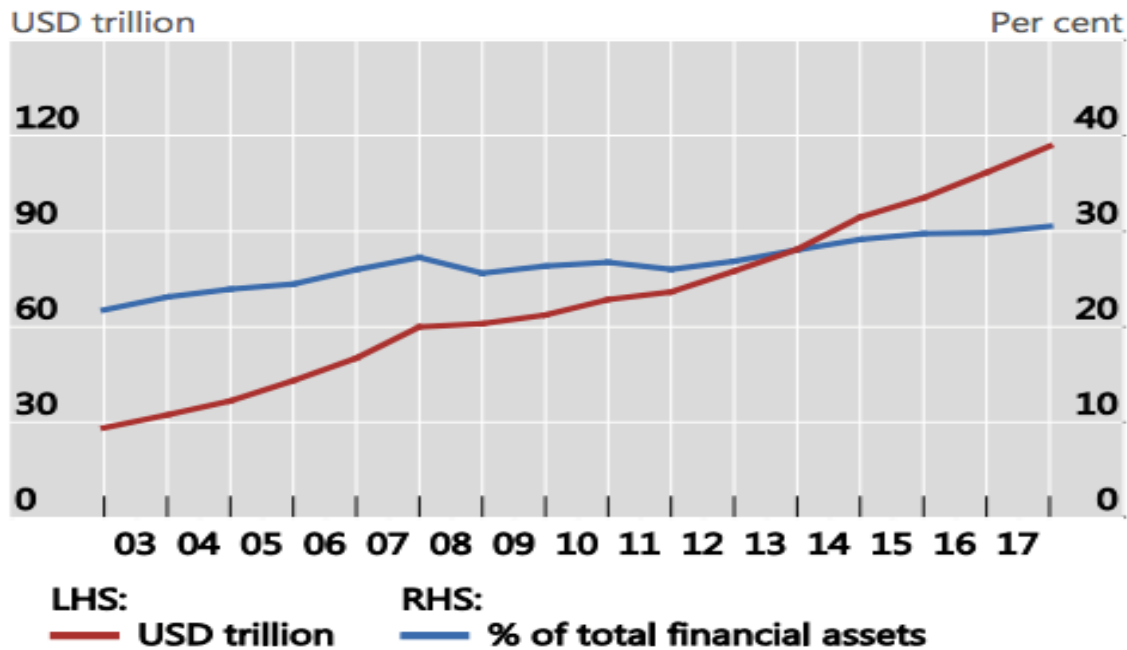
Never be enough (*Loren Allred*)

3. Close the door, they're coming through the window (*Strargazers*)

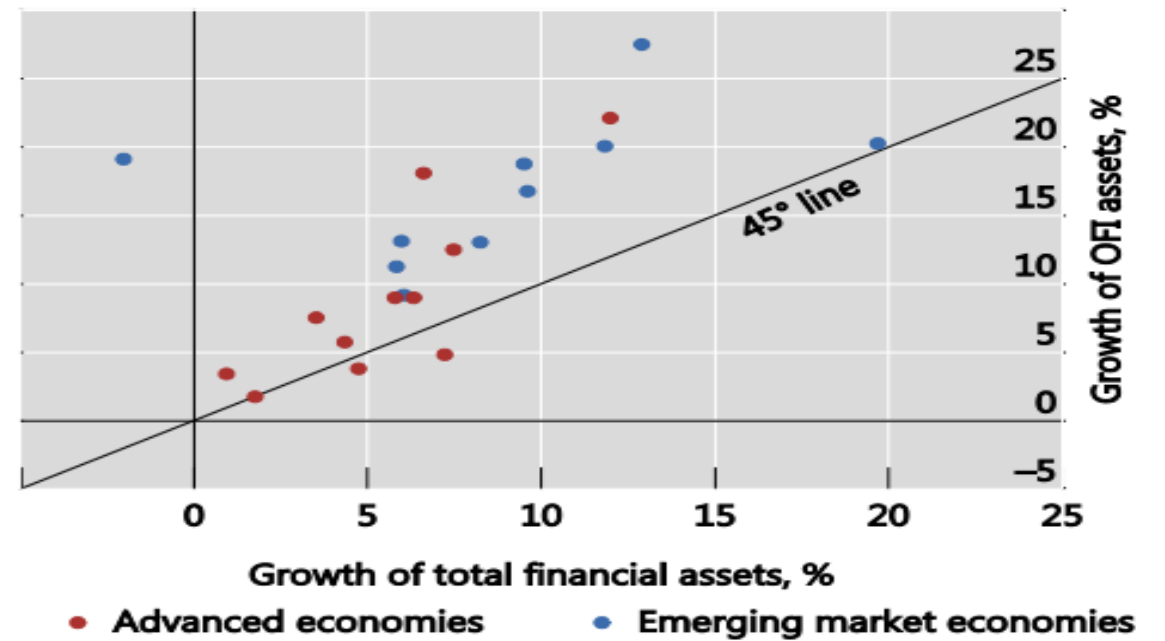
Other Financial Institutions are growing fast



Financial assets of OFIs



Growth rate in 2017

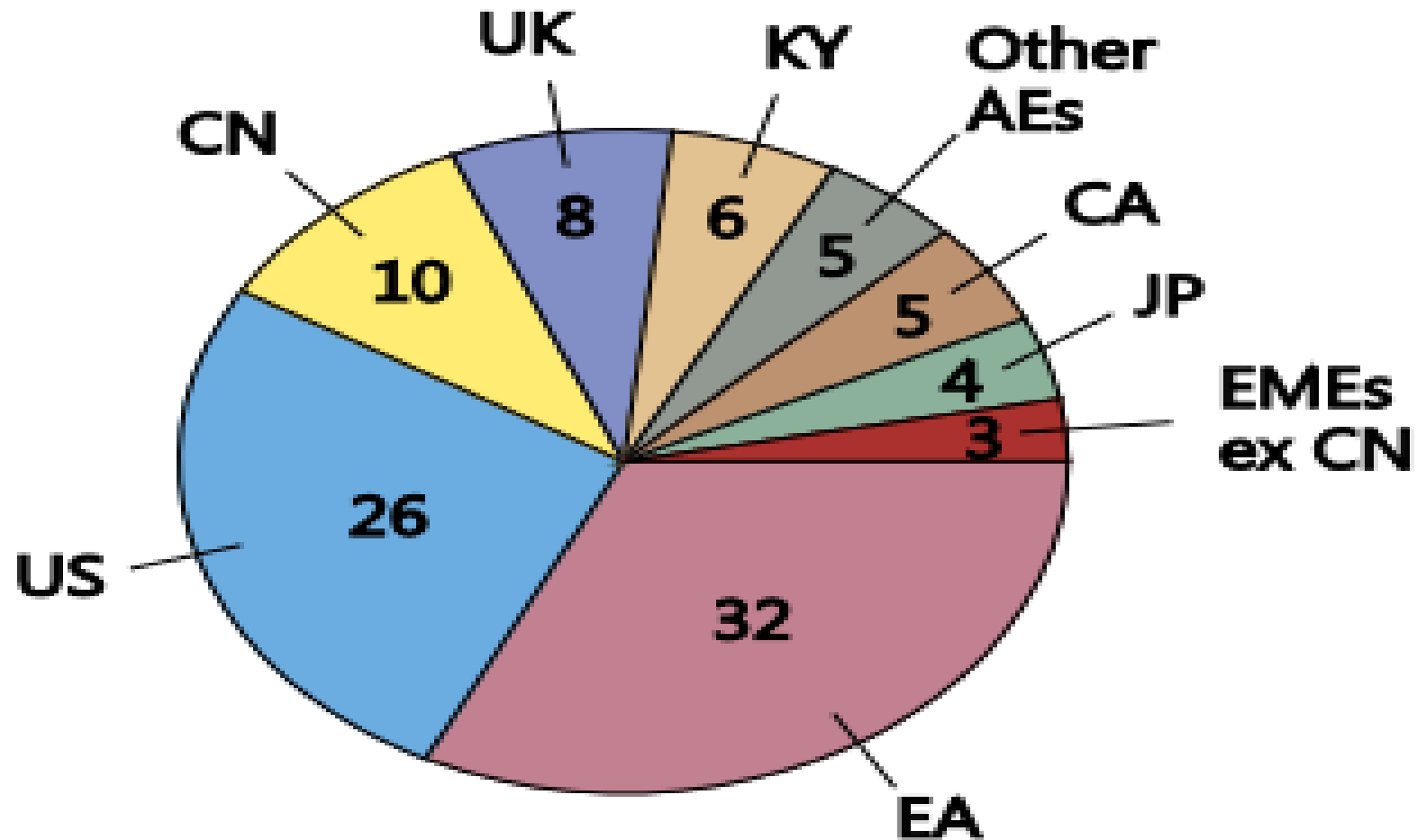


¹ Some exchange rate effects have been netted out by using a constant exchange rate (from 2017).

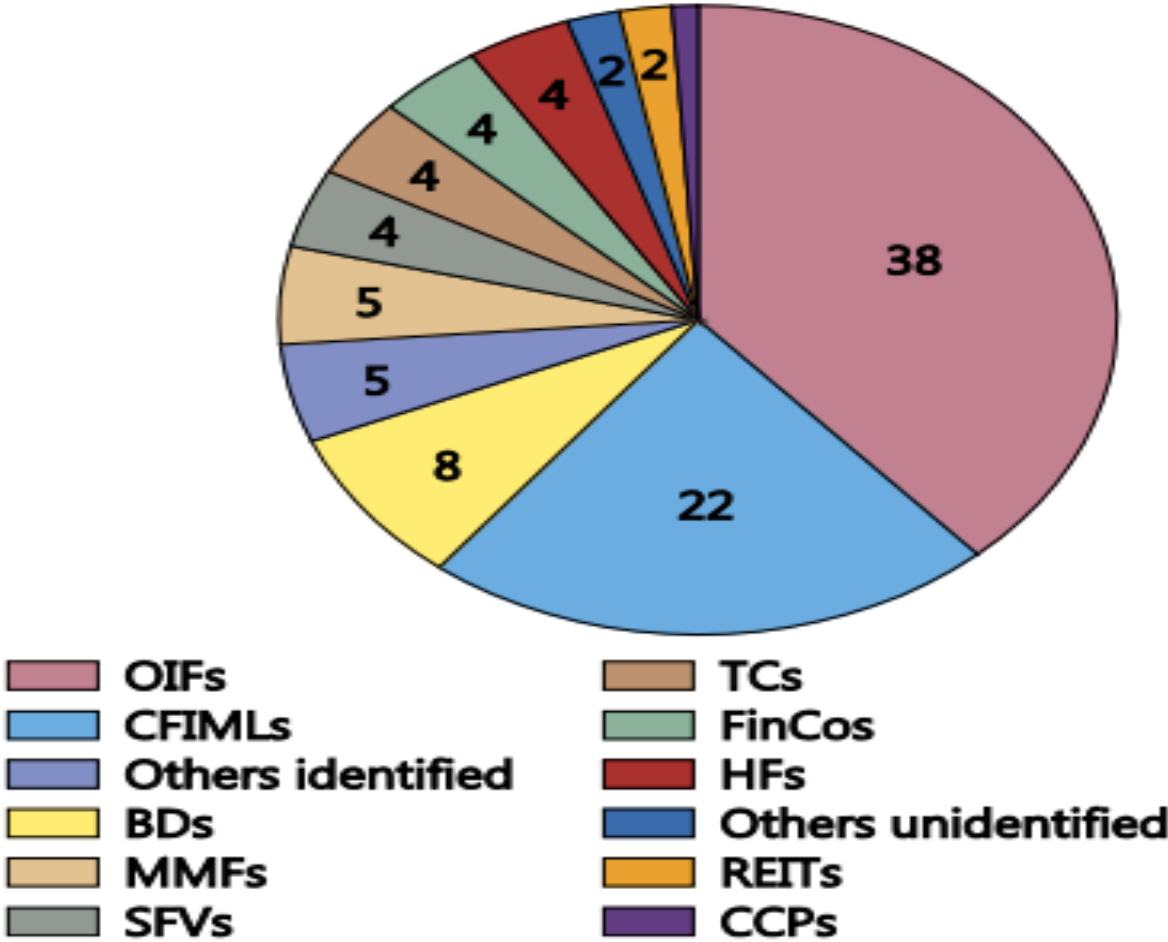
Sources: Jurisdictions' 2018 submissions (national sectoral balance sheet and other data); IMF *World Economic Outlook*; FSB calculations.



The Eurozone and the US dominate

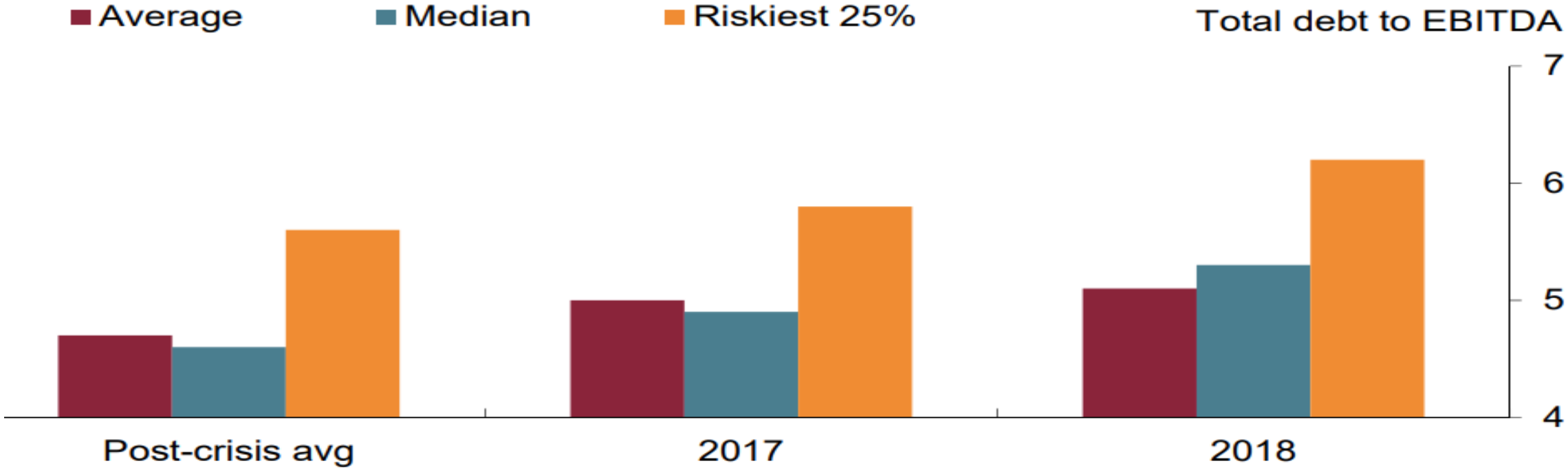


With investment funds of various kinds most prominent



Source: FSB 2019 'Global Monitoring Report on Non-Bank Financial Intermediation 2018'

Leveraged loans are becoming riskier

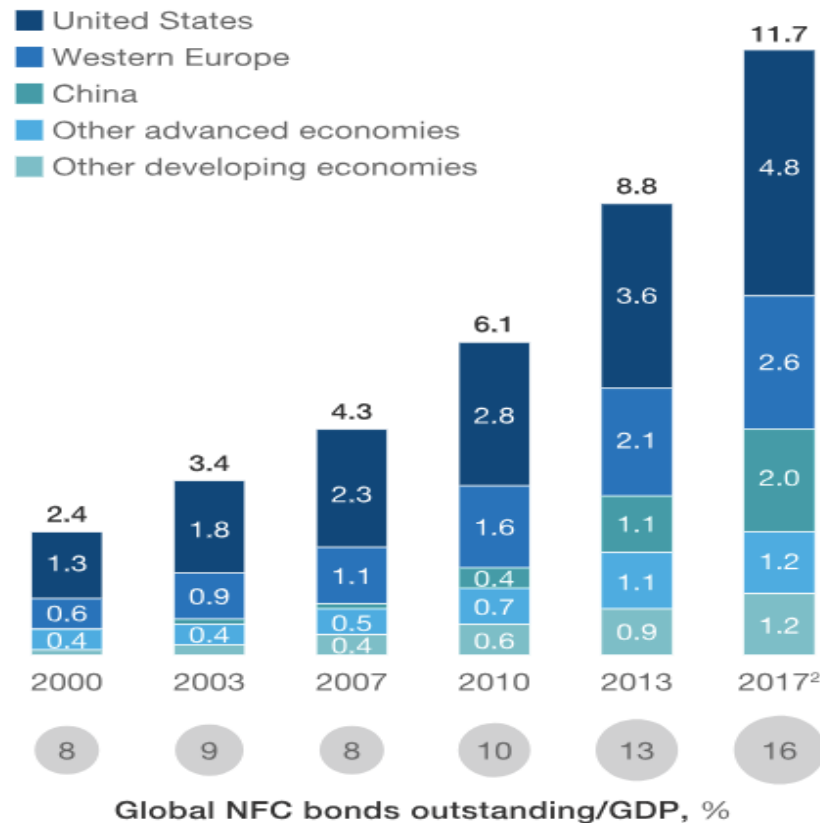


Source: Mark Carney BoE Feb 2019 – ‘The Global Outlook’

Corporates are borrowing more from the markets



Global nonfinancial corporate (NFC) bonds outstanding by region,¹ \$ trillion, nominal exchange rate



2007–17 change, \$ trillion

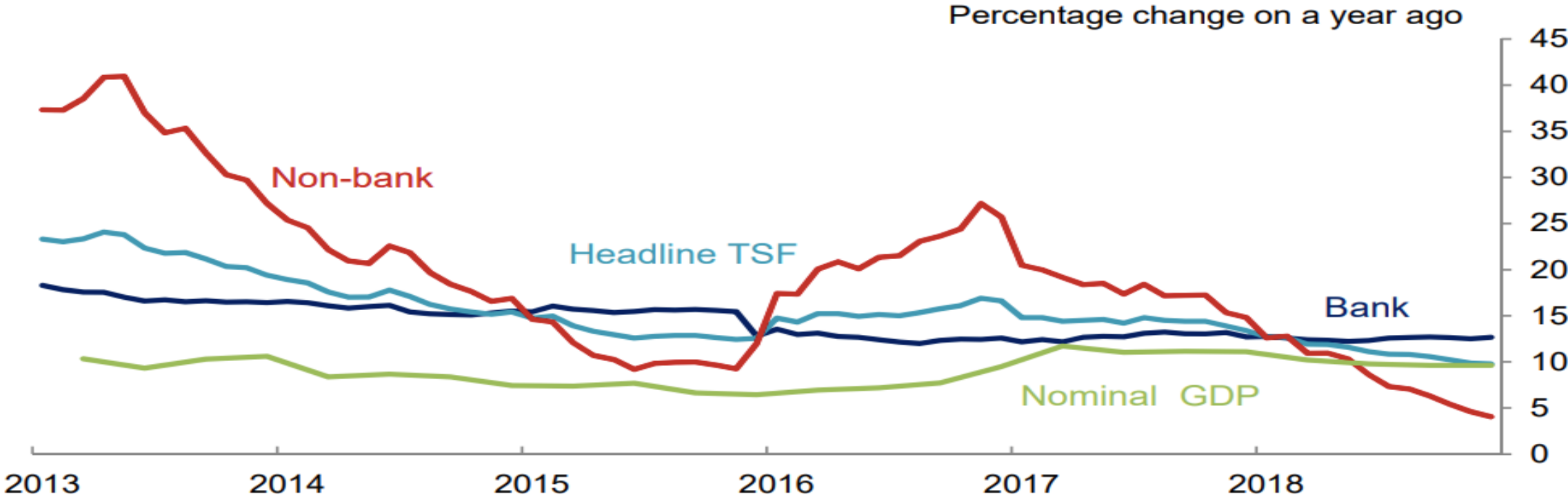


2007–17 compound annual growth rate, %



Source: McKinsey 2018 'A decade after the global financial crisis: What has (and hasn't) changed?'

Chinese credit growth has slowed



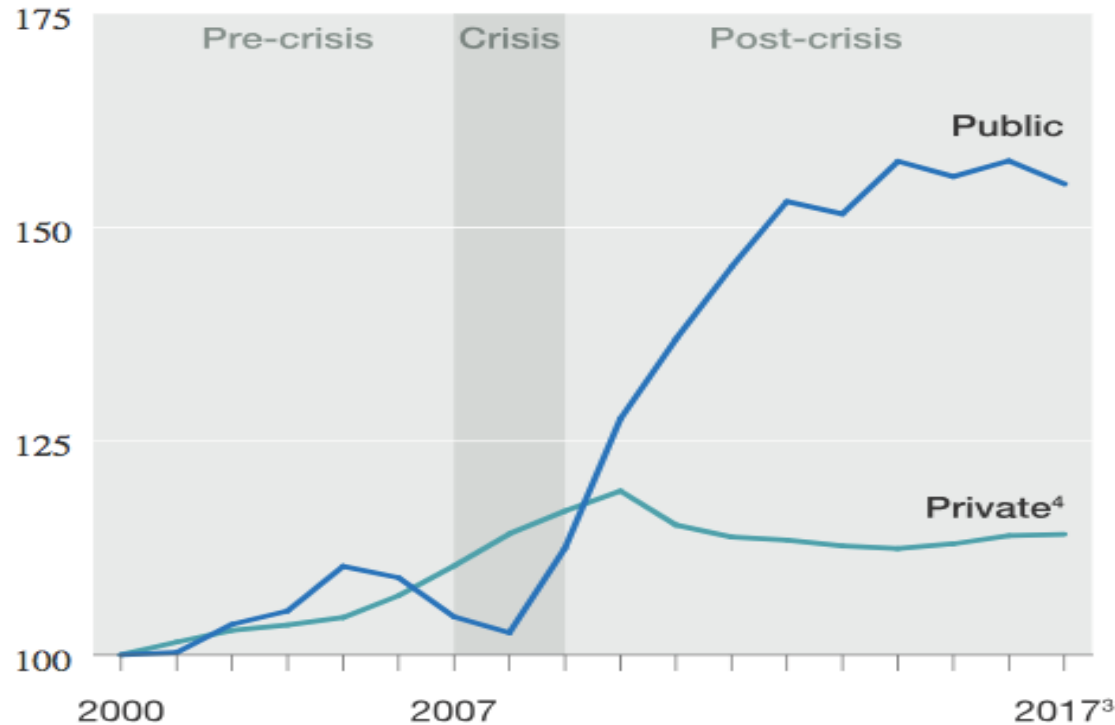
Source: Mark Carney BoE Feb 2019 – ‘The Global Outlook’

Overall, public debt remains high

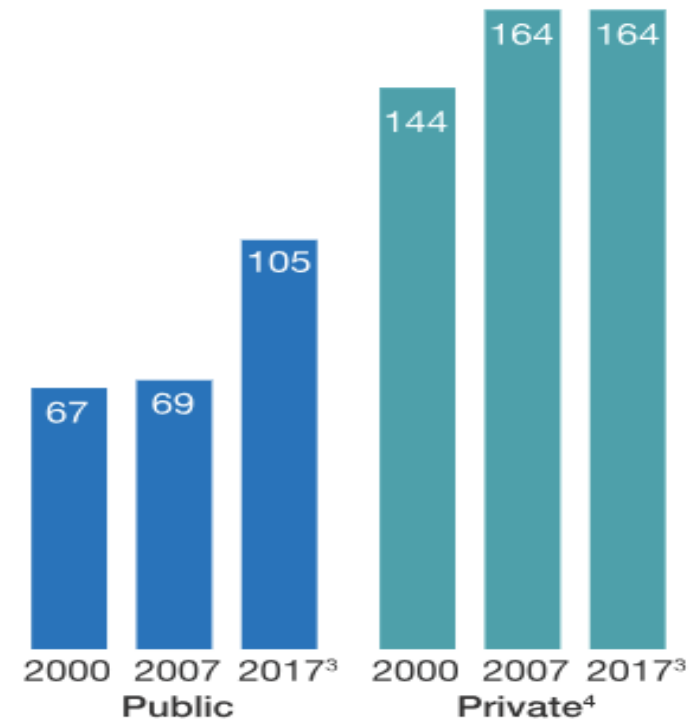


Public debt increased rapidly after the crisis in advanced economies.

Debt in advanced economies¹ by sector,
% of GDP,² Index: 100 = 2000



Actual debt-to-GDP ratio in
advanced economies, %



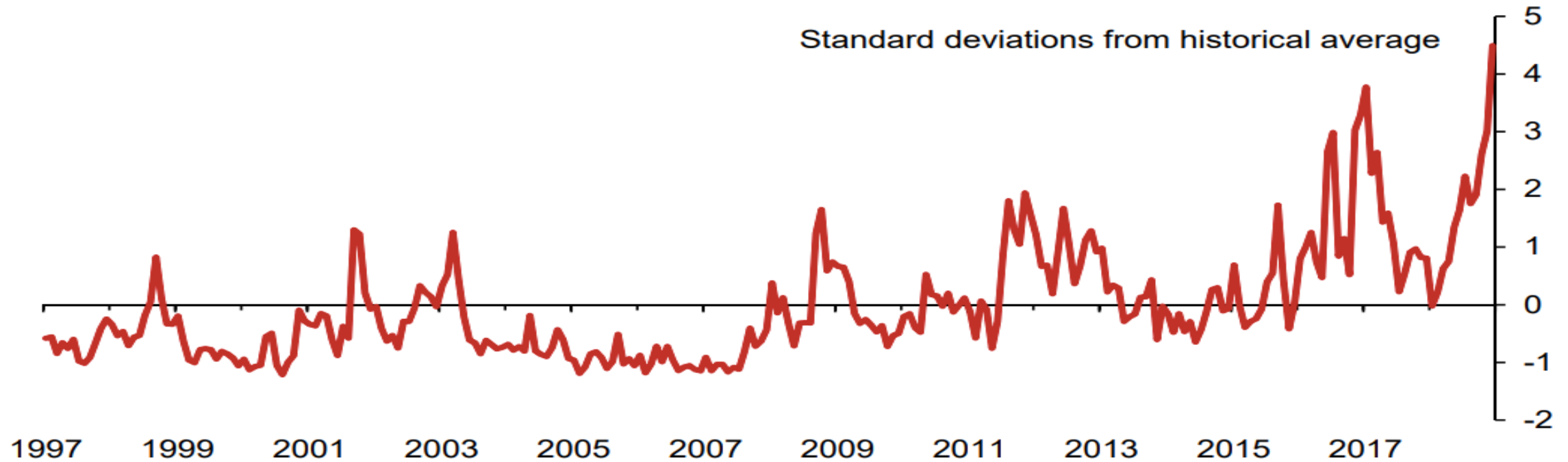
Source: McKinsey 2018 'A decade after the global financial crisis: What has (and hasn't) changed?'

We can find many other risks if we wish to look



- Cyber security threats
- Fintech disruptors
- Big Tech entrants hollowing out the banking system

Indices of global economic policy uncertainty are at record highs



Sources: Bloom et al (2015)² and Bank calculations

But the biggest concerns may lie in the policy arena:



- Policy uncertainty is at a record high
- The opportunity to strengthen the foundations were missed
- Policy co-ordination remains weak
- The scope for dangerous errors has grown



'Global Banking Regulation: The Limitations of Voluntarism'

by

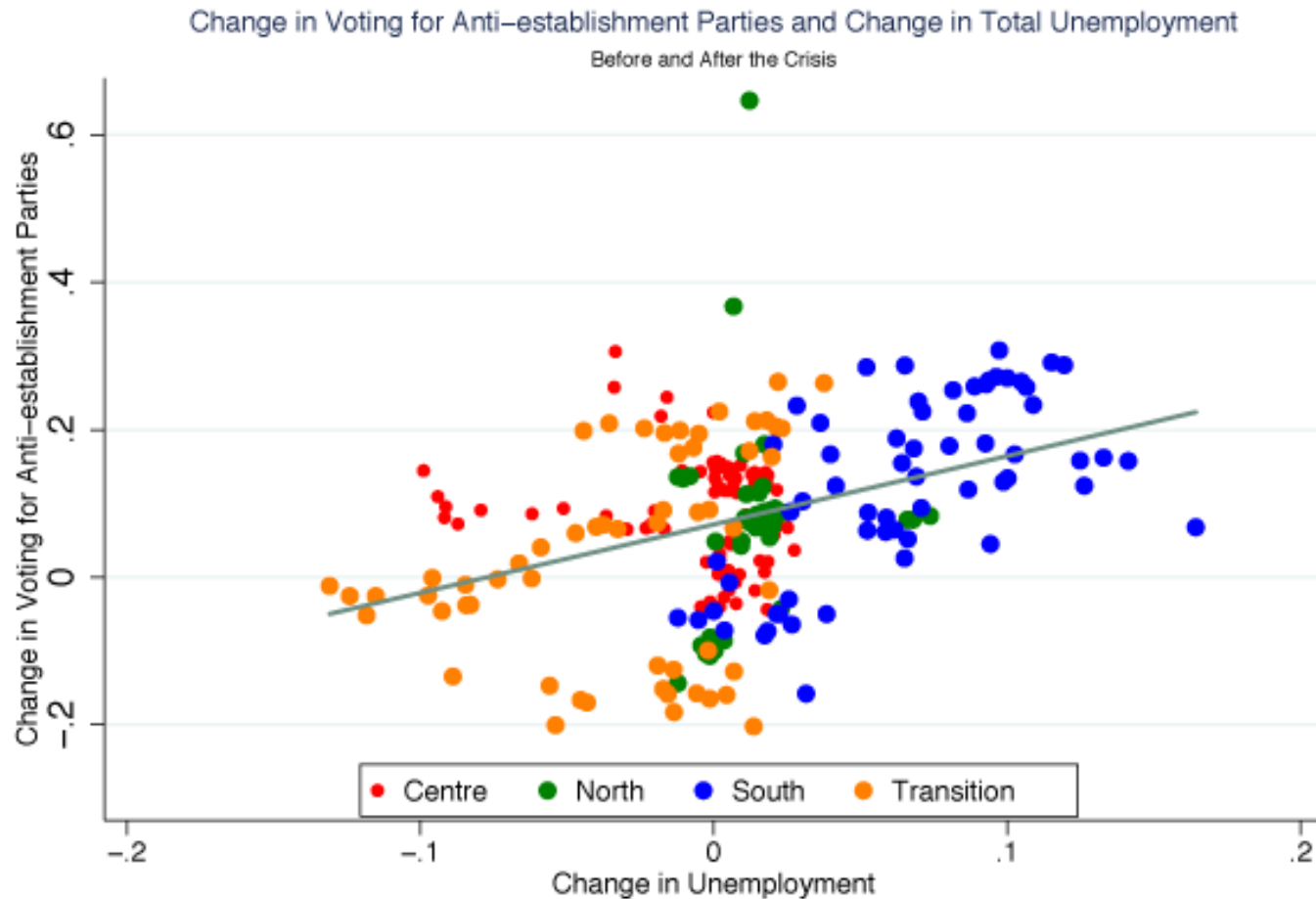
Howard Davies and Dr. Maria Zhivitskaya
forthcoming in April 2019

Policy errors have become more likely



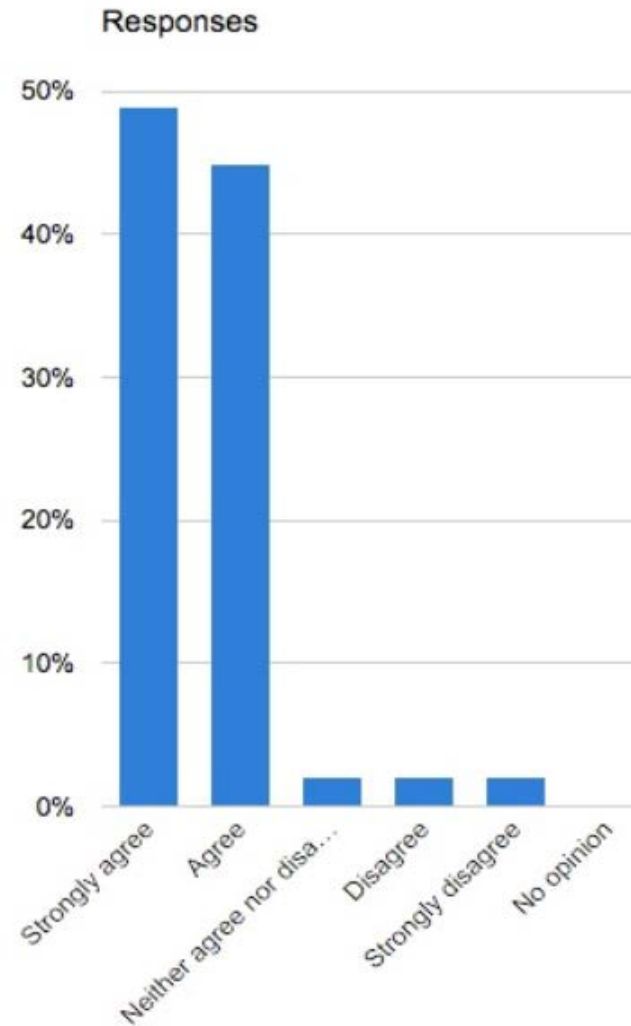
- Tariff wars
- Brexit could disrupt European capital markets
- Central Bank Independence under threat in many countries

In most of Europe unemployment has remained high, and populist parties have benefited



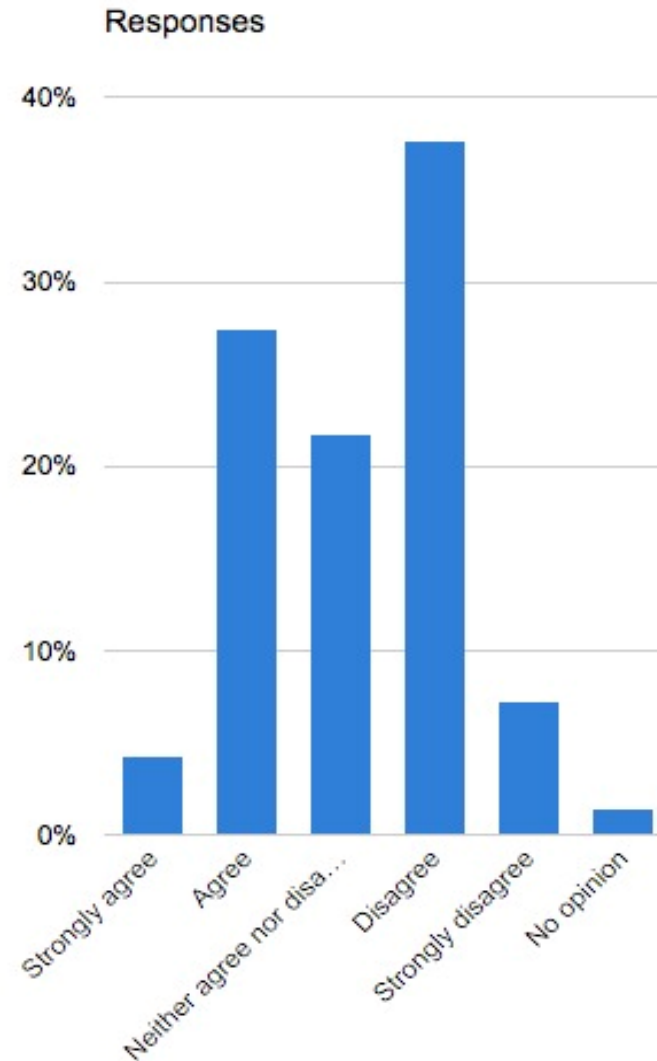
Source: National Election Sources and Eurostat

Do you agree that it is desirable to maintain central bank independence in the future?



Source: LSE (2017) - Is the era of central bank independence drawing to a close?

Do you agree that central bank independence in the Eurozone & the UK will decline over the next 48 months?



Source: LSE (2017) - Is the era of central bank independence drawing to a close?



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