



Discussion of the Survey

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***WORKSHOP on FINANCIAL MARKETS
Policy Challenges and the Research Agenda***

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The survey is aligned with the past, ongoing and future work of the EC Joint Research Centre



JRC is the EC's Research-Based Policy Support Centre

The **Financial and Economic Analysis** Unit supports the Commission Services in their effort to strengthen economic governance and to build a stable financial system in the EU

SYMBOL: the JRC model of the banking system

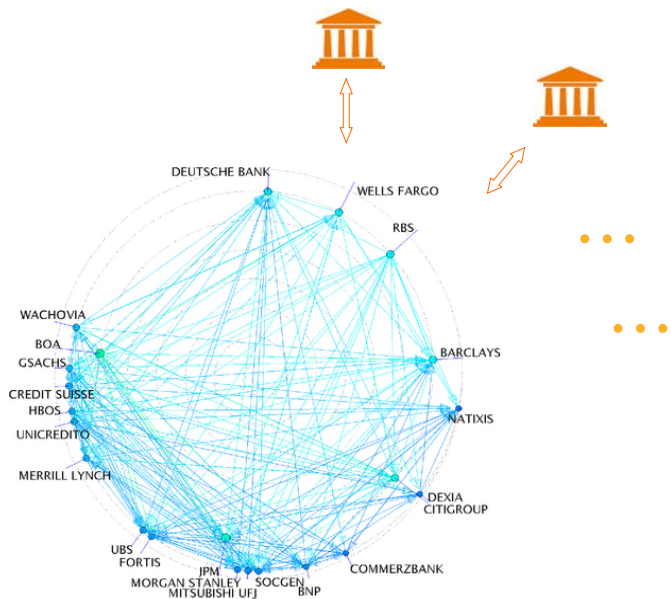
SYMBOL is the tool used by EC policy makers for impact assessment of banking regulation

SYMBOL:

- Uses balance sheet data of ~4000 EU banks
- Uses Monte Carlo simulation derive the probabilities of bank failure and distribution of losses in the banking sector
- Incorporates safety net tools and contagion

EC Directives using SYMBOL

- Deposit Guarantee Schemes
- Capital Requirement IV
- Bank Recovery and Resolution
- Bank Structural Reform (proposal)



Remarks on the survey

- **Complexity vs. simplicity:** the issue of having simple balance-sheet based measures has already shown up for policy makers, e.g. Structural Reform
- **Focus on resolution:** the importance of feasible options for resolution of banks, but we need to understand where the losses go
- **Dynamic approach to regulation:** focus on new risks

Complexity vs. simplicity

Example: relationship between SYMBOL and SRISK contributions to systemic risk in the context of Structural Reform (SR)

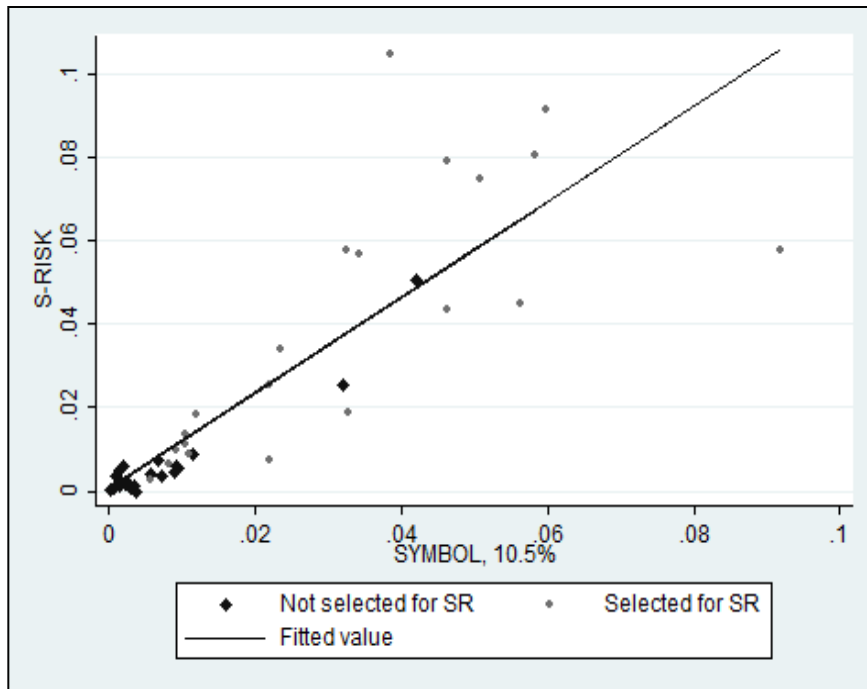


Figure: Scatterplot of SYMBOL and SRISK contributions to systemic risk

We also focus on other, simpler balance sheet indicators:

- Interconnectedness
- Relative size of trading assets
- Leverage of trading
- Others!?

Focus on resolution

- A good resolution framework is needed not only for ex post but also for ex-ante incentives effects
- Open issue: where do the losses go?

According to SYMBOL, in a systemic crisis bondholders will cover the vast majority of the losses (losses in recent crisis amount to ~500 b€)

Where do these losses go?

We know that most of the bank bonds are owned by banks, insurances and pension funds

Focus on resolution

- A Single Resolution Fund of 55bn Euros would not cover any major bank failure

True. But the fund is not intended to absorb losses alone!

The bail in come first and than ESM may come into play for systemically relevant institutions

- A public back stop is missing

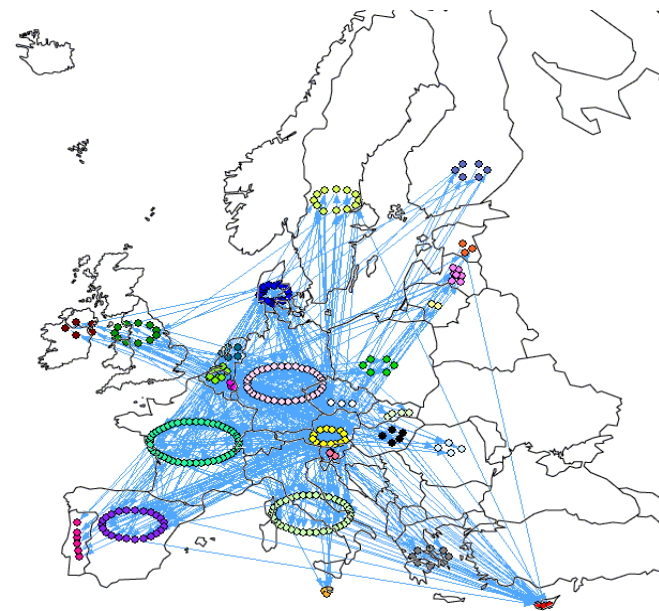
The ESM acts as EU-level back-stop although limited to €60 billion

Dynamic approach to regulation

Sources of systemic risk can originate outside the banking system

JRC lines of research:

- Hidden dynamics of financial markets (e.g. **shadow banking**)
- New forms of finance such as **crowd funding and digital currencies** (BITCOIN)
- Contagion effects across financial sectors (e.g. **pension and insurance**)



Conclusions

- Research is needed to support policy makers in their choices
- The survey highlights several important topics and issues on which also the JRC is working
- The survey focuses on banking regulation but there are other aspects that are relevant for EU policy makers