

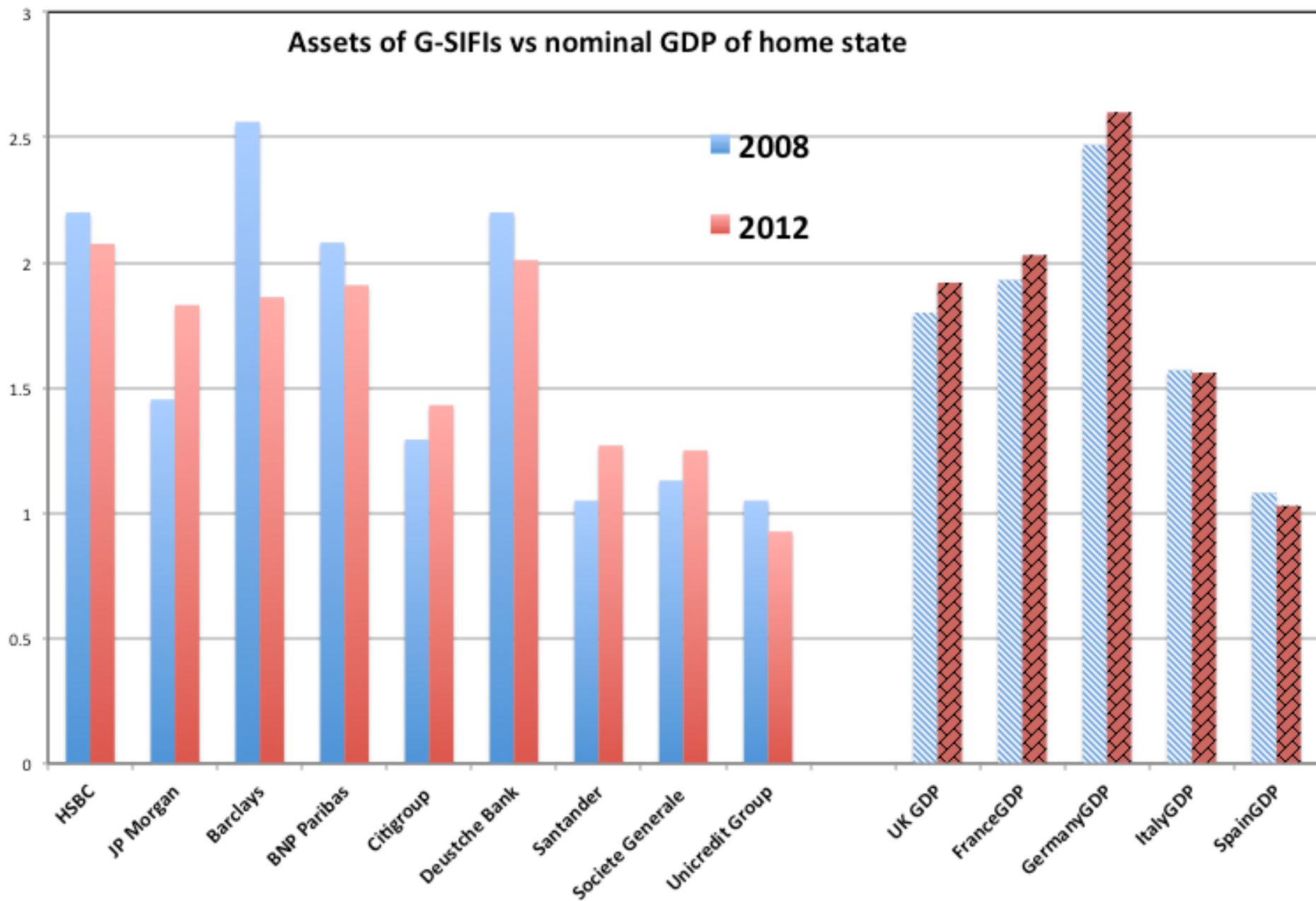
European (shadow) banking union

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EUR trillion

Assets of G-SIFIs vs nominal GDP of home state



Banking/Capital Markets Union: the good news

- Single supervision/resolution of banks systemic at European level
- Step forward in dealing with challenges of European banking
- Harnessing capital markets to restart growth in Europe + addressing fragmentation of single financial space (monetary policy)

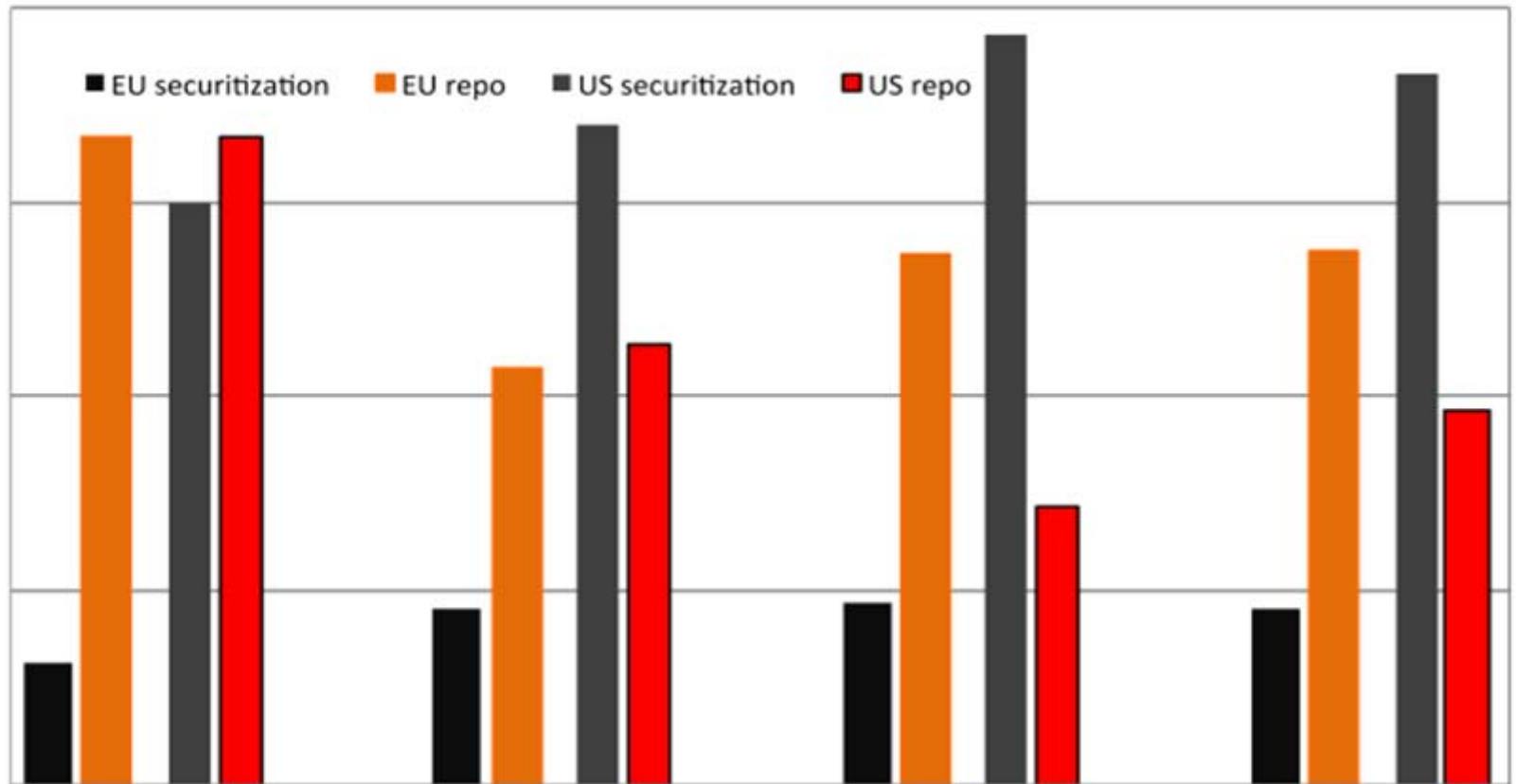
Banking Union vs Capital Markets Union

- Different logics: regulatory (stability) vs growth
- Distinctive positions of member states: centralization of market supervision
- Towards market-based banking: bank lending into tradable assets

How does shadow banking fit with this?

- European support for a shift from bank to market-based financial systems
- Shadow banking: ‘money market funding of capital market lending’ (Mehrling 2012, Pozsar 2014)
- CMU: incentivize ‘shadow’ markets (securitization)

Shadow banking universe: 2007 - 2012



Source: ICMA, Singh and Stella (2012), Gorton and Metrick (2011)

Capital Market-making coalitions

- ECB: ABS purchase program (making markets in private capital)
- European Commission: take into account possible future increases in the liquidity of securitization products' (2013 Green Paper)

The elephants in the room

- What about reform of wholesale funding markets (eg the repo market)?

Shadow fragilities

- SB generates financial fragility (leverage cycles; mark-to-market accounting; tranching practices in securitization; pro-cyclical repo haircuts; interconnectedness through re-hypothecation)
- SB crises: fire sales, liquidity and haircut spirals, runs on collateralized funding markets
- Stabilizing SB: central banks (collateral swaps; outright purchases of assets - QE) and regulatory (Basel III liquidity rules; FSB reform of repos; CCP clearing derivatives & repos; additional K req for G-SIFIs)

The elephants in the room

- What about reform of wholesale funding markets (eg the repo market)?
- What about structural reform of banks?
 - Shadow banking in Europe in banking in the shadows!
- The ‘liquidity’ fetish: regulatory trade-offs?
- How do government bond markets fit in the CMU plans?