PRE- AND POST CRISIS BANK BUSINESS MODELS

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BANK MODELS

	Traditional	*Securitisation*	*CDS*
(1) Accept deposits	✓	(✓)	✓
(2) Originate loans	✓	✓	✓
(3) Utilise comparative advantage: •Information •Risk analysis •Monitoring	 ✓ ✓ ✓	 ✓ ✓	 ✓ ✓
(4) Transform into loans	✓	✓	✓
(5) Accept risk	✓		
(6) Hold on balance sheet	✓		✓
(7) Capital Backing	✓		
(8) Insurance	Internal	Shift	Insure

Traditional: *Originate and hold*
Securitisation*: Originate and selll*
CDS: *Originate and insure*

KEY COMPONENTS OF BUSINESS MODELS

(1) Range of business

* bank assurance / trading etc

(2) Business Objectives

* growth /ROE

(3) Balance sheet management

* funding strategies / gearing / liquidity

(4) Conduct of core intermediation business

* securitisation / CRS

(5) Management of regulation

* regulatory arbitrage

EVOLUTION OF BUSINESS MODELS

(1) Traditional Model [1990-2002]

(2) Pre-crisis period [2002-2008]

(3) Post Crisis: short-term [2008 - ?]

(4) Post Crisis: long term [? To ?]

NEW BUSINESS MODELS

- Diversification
- Loans rose relative to RWA
- Securitisation
- Sharp rise in CRS instruments / derivatives
- Investment and trading activity
- Banks trading in complex derivatives and structured financial products
- Lower liquid assets on banks' balance sheets
- Wholesale funding v. retail deposits: funding gap
- Increased maturity transformation
- ROE and short-termism
- Increased leverage and intra-sector leverage
- Complex business structures

END RESULT

Banks stopped behaving like banks!

METHODOLOGY

Is regulation for Objective 1 part of the solution or part of the problem?

- the *endogeneity problem*

RISK MIGRATION

“Risk migrates to where regulation is weakest, so there are natural limits to what regulatory strategies can reasonably achieve”

(Haldane *et al*, 2010)

QUOTATIONS

“[We plan] to manage the hell out of RWA”

(Jamie Dimon, CEO of J P Morgan]

“We are scouring the balance sheet and looking for assets that could be structured differently so as to achieve lower risk weights”.

POST CRISIS BUSINESS MODELS: TWO PHASES

(1) Stock-Adjustment phase

(2) New Steady-State scenario

(1) STOCK-ADJUSTMENT PHASE

- De-leveraging
- Lower cross-border banking and flows
- Enhanced liquidity
- Reduced maturity transformation
- Enhanced forbearance by banks: low interest rates and capital position
- Credit crunch: credit tightening
- Reduced CB liquidity transfers
- Reduced EU banking in global finance: trade-finance / CB leasing etc
- Less market trading
- Cost management strategies
- Divesting from non-core business

(2) NEW STEADY-STATE BUSINESS MODELS

- Traditional model of banking ?
- Core business
- Less investment banking
- Less reliance on wholesale funding
- Less reliance on rating agencies
- Less complex business structures
- Less trading
- Less use of credit derivatives
- Greater liquidity
- Lower gearing
- Securitisation ?
- Structures: Living Wills / Ring Fencing
- More focussed on core business
- Less cross-border business
- Cost strategies

“The evolution of European banking and its business models over the coming years is likely to be dominated by the legacy of the crisis and the regulatory and supervisory responses to it”

“Business Models in European Banking: A Pre- and Post-Crisis Screening”, CEPS, 2011.

FUTURE STRUCTURE: DIVERSITY

"Our judgement, however, is that European banking will not converge on a single business model. Diversity will remain with a spectrum of models……."

Business Models in European Banking: A Pre- and Post-Crisis Screening", CEPS, 2011.