

## SHADOW BANKING

**Text of reference:** consultation du FSB on shadow banking from 18 November 2012

**Link:** [http://www.financialstabilityboard.org/publications/r\\_121118.pdf](http://www.financialstabilityboard.org/publications/r_121118.pdf)

### Description

The Financial Stability Board (FSB), created in April 2009 by the G8, has defined « Shadow Banking » as a system in parallel of credit intermediation, activity traditionally the preserve of banks. It involves entities and activities outside the traditional banking system.

According to the FSB, economic systems adopted by this finance in parallel allow it being governed by a different regime from traditional banking activities in particular controls or taxation. Further to the FSB Report, Shadow Banking would take mainly 2 forms which are **securitization** and the development of the **High-yield Bond market**.

But this term «Shadow Banking» covers also activities like securities lending and repos and more widely activities carried out by Money Market Funds and other investment funds (capital investment, hedge funds, etc ..)

Right or wrong politicians and regulators have considered that Shadow Banking activities had played a crucial role in the financial crisis of 2008, deriving from real economy money from traditional banking system.

The report of the FSB estimated the banking system in parallel to USD 67 000 billion allocated between USA (USD 23 000 billion), the EURO zone (USD 22 000 billion) and the UK (USD 9 000 billion). In 2011 cumulated assets of the sector would represent 111% of the aggregated GDP of G20 countries and 25% of assets of the financial sector.

USA, the euro zone and the UK hold together 81% of these non banking assets. The FSB Report unveils a strong growth of some *Shadow Banking activities* in emerging countries: China, Indonesia and Russia.

### Past Events

- 2010 – The Financial Stability Board (FSB), mandated by G20 to issue recommendations to strengthen oversight and regulation of the Shadow Banking.
- 19 March 2012 - Green Paper of the European Commission on Shadow Banking.
- 18 November 2012 - The FSB published a series of recommendations to strengthen oversight and regulation of the Shadow Banking. Comments were expected for 14 January 2013.
- 20 November 2012 - The European Parliament voted a resolution aimed at improving the *shadow banking regulation*.
- 28 January 2013 – *FSB was set up as an association under Swiss Law.*
- 29 January 2013 - The FSB published replies received to the 4 reports published on 18th November 2012. These answers will contribute to finalize recommendations of the FSB by September 2013.
- June 2013 – The SEC published its consultation (700 pages) on Money Market Funds (3 months) <http://www.sec.gov/rules/proposed/2013/33-9408.pdf>
- 29 August 2013 – The FSB publishes 3 new reports including recommendations to address Shadow Banking risks in the securities lending & repo activities
- 4 September 2013 – The European Commission (EC) publishes a draft regulation for money market funds out of the scope of the UCITS 4 Directive
- 29 January 2014 – The EC adopted a proposal for a regulation to stop the biggest banks, TBTF (\*) from engaging in proprietary trading and to give supervisors the power to require those banks to separate other risky trading activities from their deposit-taking business.

- This proposal provides a set of measures aiming to enhance regulators' and investors' understanding of securities financing transactions (STFs). These transactions have been a source of contagion, leverage and procyclicality during the financial crisis and they have been identified in the Commission's Communication on Shadow Banking as needing better monitoring
- In parallel of this reform, the EC imposes the transparency of some transactions in the shadow banking sector (And in particular **operations of securities/lending activities** because they enter the scope of SHADOW BANKING). If this reform is adopted, it would **impose to UCITS and AIF a reporting of financing operations on securities**.

### Situation as of today

The EC received lots of comments on the draft regulation as of 4<sup>th</sup> September 2013. More than 800 amendments have been made to the Bill. But no approval has been reached within ECON and project has not been submitted to the European Parliament in April 2014. We need to wait until September to see how this project will be reactivated by the new *Rapporteur* within ECON Commission.

In March 2014, the European Commissioner Michel Barnier indicated that securitization could be re-visited, in particular for pushing the growth in Europe, if it is well designed with a regulatory framework

At international level after G20 summit of St Petersburg in September 2013, the FSB will render an account to the G20 in November 2014 on progress made regarding different actions planned within its recommendations/publications.

Regarding the draft banking reform published on 29 January 2014, possible impacts on our business remain to be identified, even if it is still difficult at this stage, in the absence of a vision clear and precise.

Finally the SEC has published its new rules on Money Funds on 23<sup>rd</sup> July 2014. These rules might influence new discussion on MMF European regulation draft.

### To know more:

- [www.financialstabilityboard.org](http://www.financialstabilityboard.org)
- [http://ec.europa.eu/internal\\_market/finances/shadow-banking/index\\_fr.htm#140129](http://ec.europa.eu/internal_market/finances/shadow-banking/index_fr.htm#140129)
- Fact sheet on Money Market Funds
- Fact sheet on Securities Financing Transactions
- Summary Sheet of Money Market Funds In U.S.

**Contact SGSS/SMI:** Jean-Pierre Gomez ([Jean-Pierre.Gomez@sgss.socgen.com](mailto:Jean-Pierre.Gomez@sgss.socgen.com))

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(\*) **TBTF: Too big to fail**