FINANCIAL SERVICES FORUM

# Large Bank Resiliency in the Post-Crisis Era

June 2019

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# About the Financial Services Forum

The Financial Services Forum is an economic policy and advocacy organization whose members are the chief executive officers of the eight largest and most diversified financial institutions headquartered in the United States.  Forum member institutions are a primary source of lending and investment in the United States and serve millions of consumers, businesses, investors, and communities throughout the country. The Forum promotes policies that support savings and investment, deep and liquid capital markets, a competitive global marketplace, and a sound financial system.

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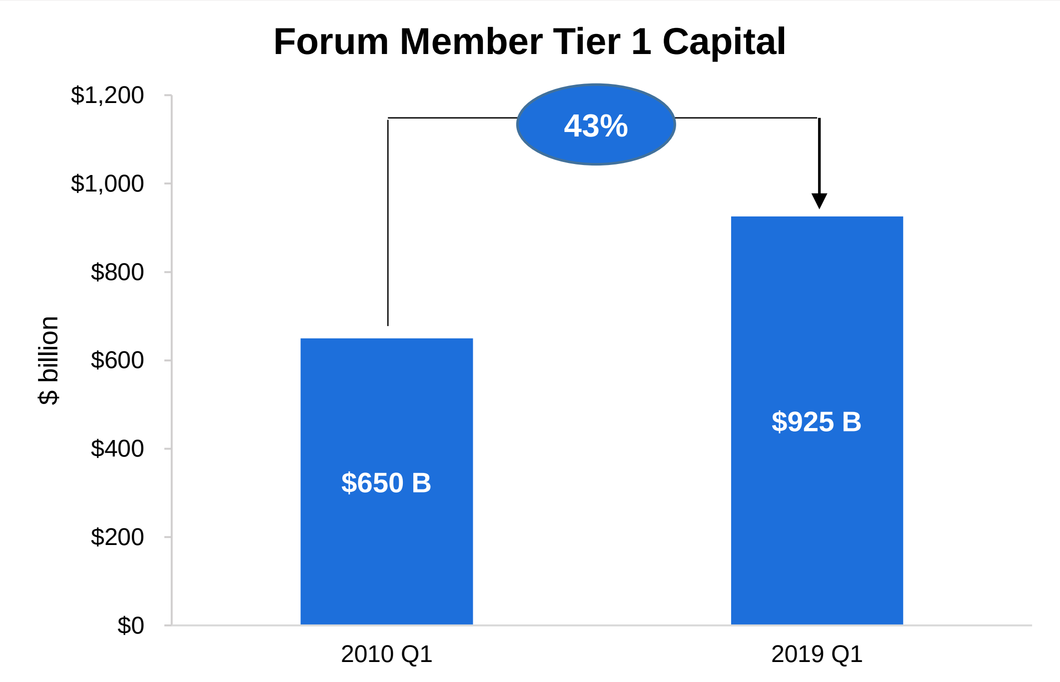
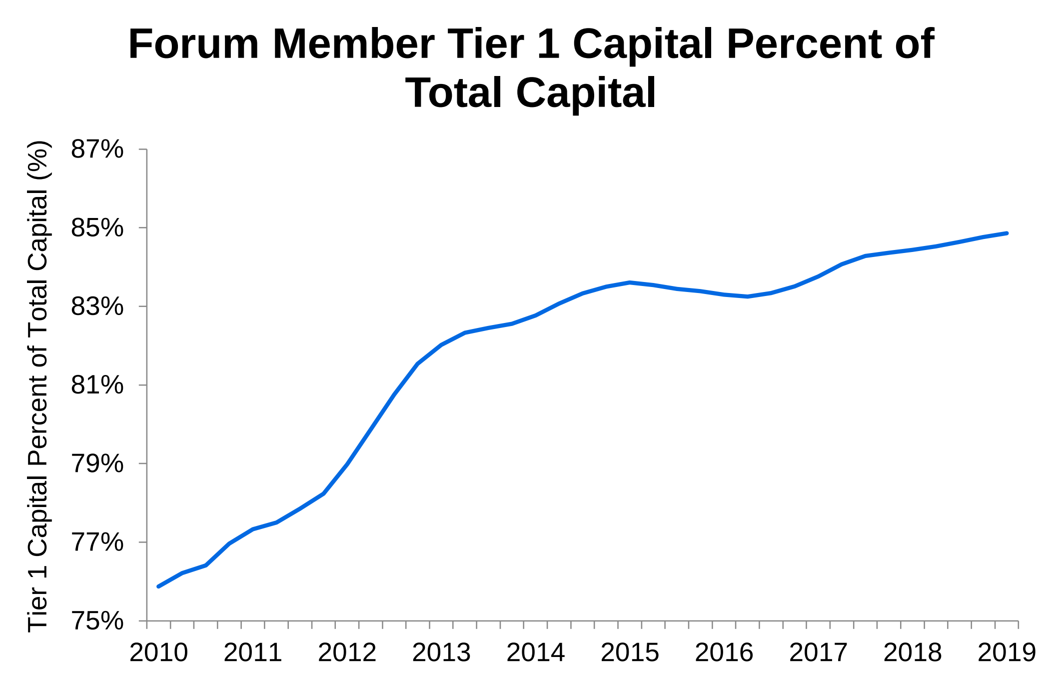
# Improvements in Tier 1 Capital and Resiliency

We have significantly enhanced the quality and quantity of our capital over the past nine years. Since 2010, **Tier 1 capital has increased by over 40 percent** and has grown as a share of risk-weighted assets and total capital. Our members currently maintain **$925 billion of Tier 1 capital.**




- Both dollar amounts of capital and capital ratios have improved markedly since 2010

- The share of capital accounted for by high-quality and loss -absorbing Tier 1 capital has improved markedly

Source: FR Y-9C data, available at https://www.ffiec.gov/nicpubweb/nicweb/HCSGreaterThan10B.aspx
Note: Capital amounts are reflective of the regulatory definition of capital at each point in time; Chart represents a rolling, previous four quarter average of data

# Forum Capital Resiliency and Stress Tests

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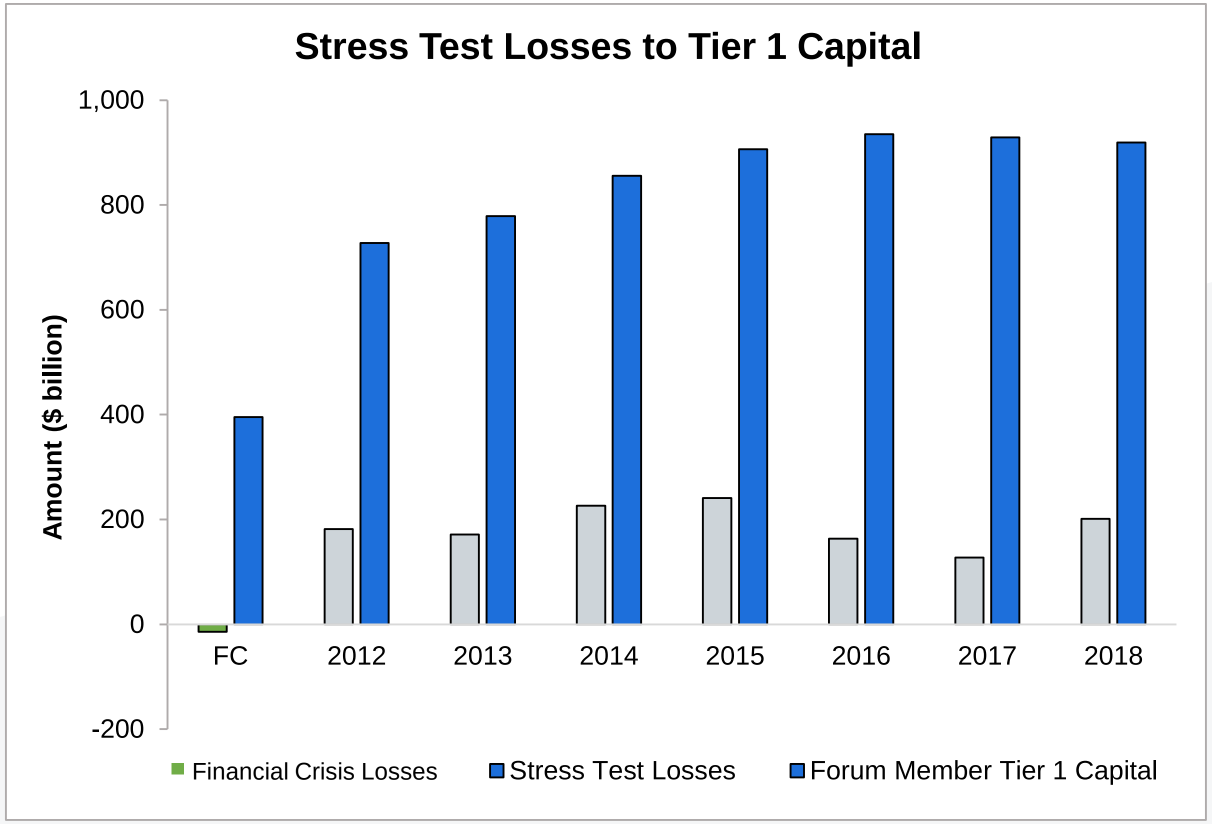
Stress tests have become an important part of the capital regime for Forum members. While losses sustained from stress tests are significant, they pale in comparison to the amount of Forum member Tier 1 capital.



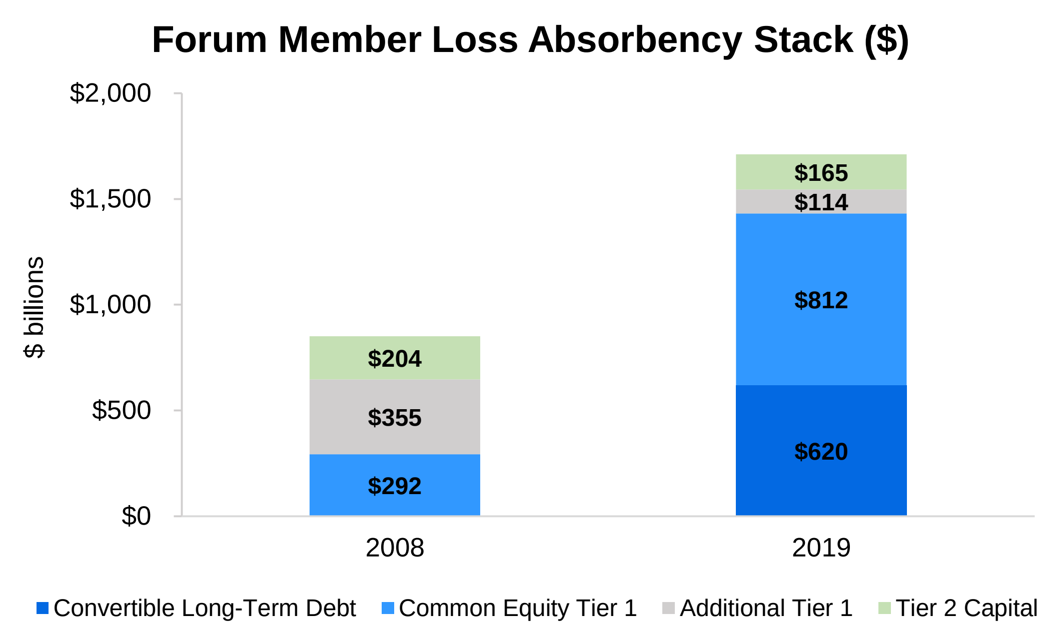

- Forum aggregate stress test losses range from 13.7 percent to 26.5 percent of Forum aggregate Tier 1 capital, demonstrating that Forum members maintain substantial capital to sustain losses as severe as those contemplated in the stress tests

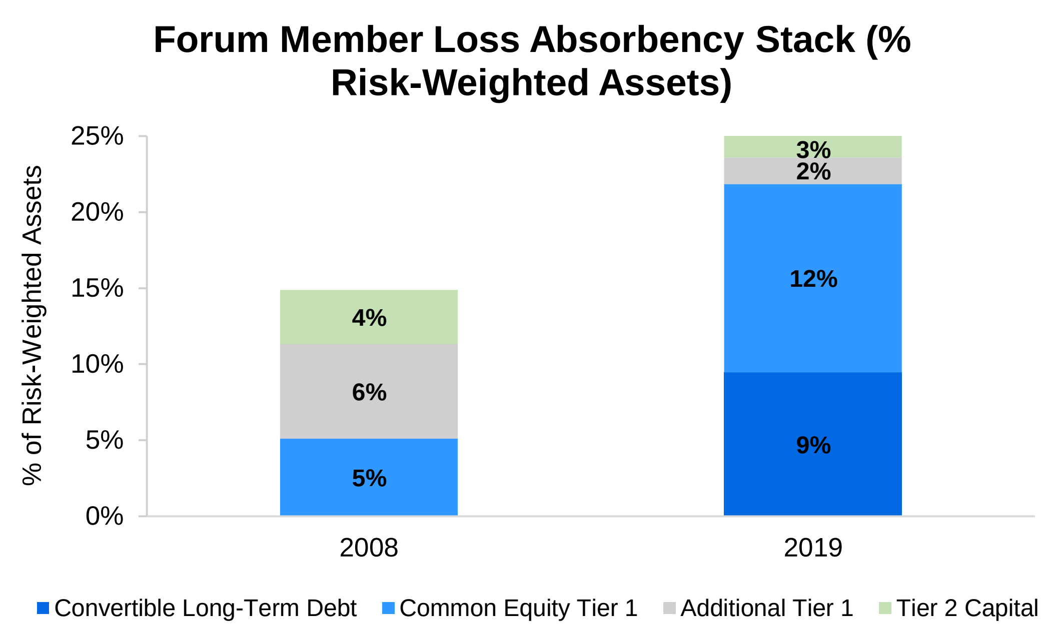
- In addition, stress test losses are significantly more severe than the experience of the financial crisis

Sources: FR Y-9C data, available at https://www.ffiec.gov/nicpubweb/nicweb/HCSGreaterThan10B.aspx; Federal Reserve Board Dodd-Frank Act Stress Tests, available at https://www.federalreserve.gov/supervisionreg/dfa-stress-tests.htm, staff calculation. Note: Capital amounts are reflective of the regulatory definition of capital at each point in time.

# Forum Member Total Loss Absorbency

Since 2008, **Forum member's total loss absorbency**—measured by convertible long-term debt, Tier 2 capital, common equity Tier 1 and additional Tier 1 capital—**has grown by $850 billion, a 100 percent increase that substantially improves Forum members' ability to withstand losses.**



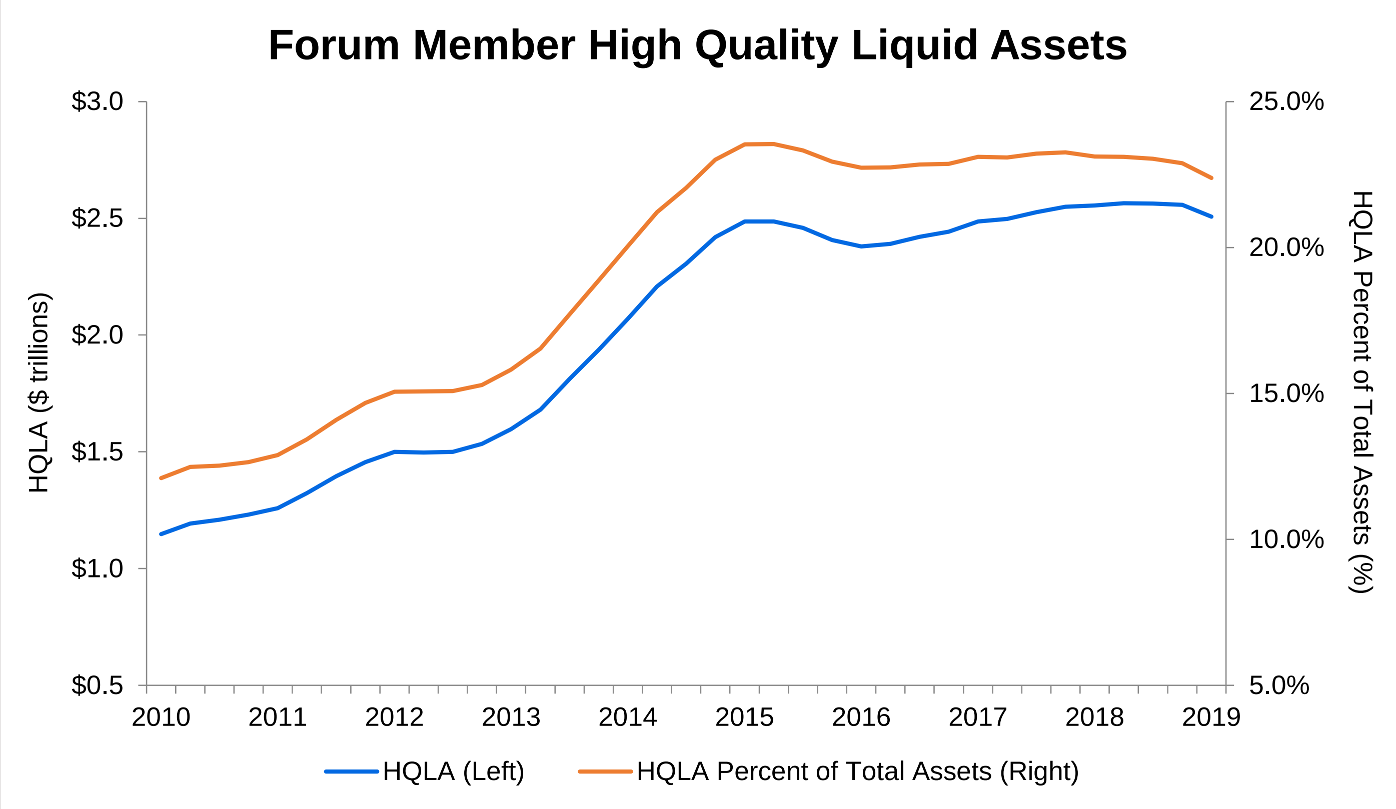

- Common equity Tier 1, the most loss absorbing form of capital, has grown more than $515 billion since 2008, and has increased as a percent of total Tier 1 capital, from 45 percent to 87 percent

- Estimated convertible long-term debt, debt that may be converted into equity to absorb losses, will be required and in place by January 1, 2019

Sources: FR Y-9C data, available at https://www.ffiec.gov/nicpubweb/nicweb/HCSGreaterThan10B.aspx; Federal Reserve Board "The Supervisory Capital Assessment Program: Overview of Results, available at https://www.federalreserve.gov/newsevents/files/bcreg20090507a1.pdf

# Improvements to Liquidity Profile

We have also greatly increased our liquidity profiles and now hold **nearly $2.5 trillion in high-quality liquid assets** (HQLA). Since 2010, HQLA has doubled.



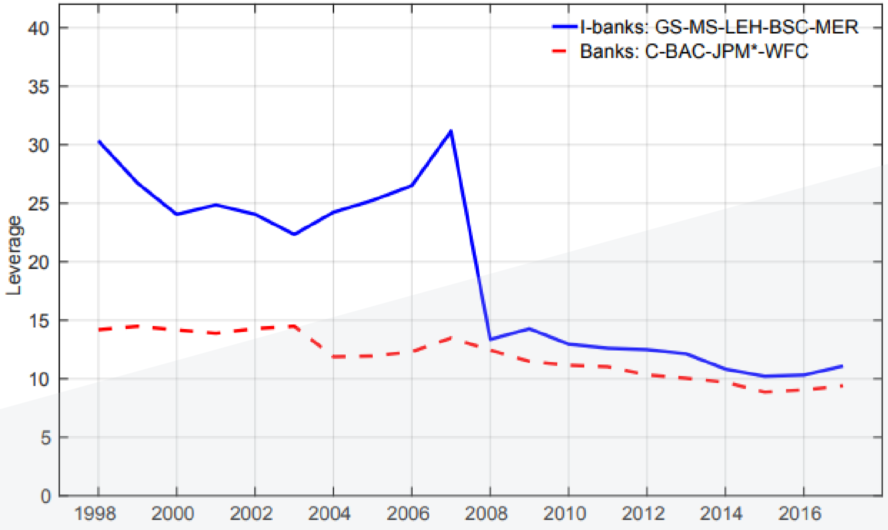

- Increased liquidity complements increased capital and improves resiliency to adverse shocks
- We have substantially increased HQLA, both in dollar amount and relative to total assets

Source: FR Y-9C data, available at https://www.ffiec.gov/nicpubweb/nicweb/HCSGreaterThan10B.aspx.
Note: HQLA is reported according to Basel III at the Bank Holding Company level; Chart represents a rolling, previous four quarter average of data

# Improvements in Resiliency Are Substantial and Widely Recognized

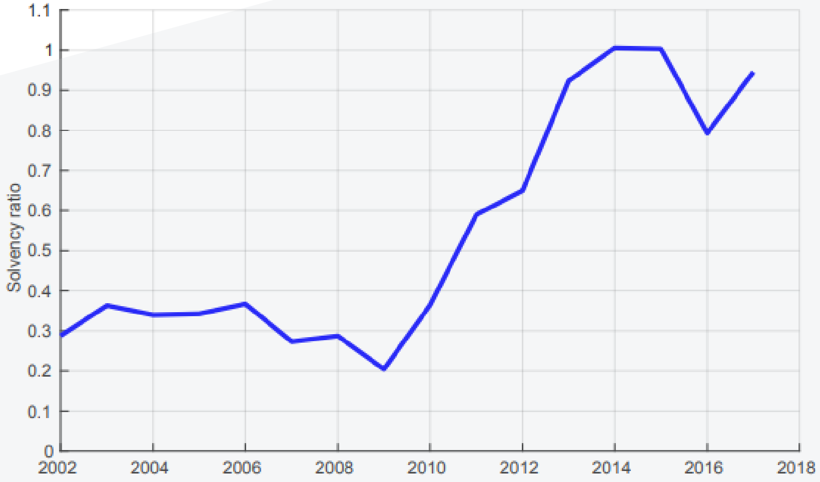
Darrell Duffie (Stanford University) recently released a research paper documenting improvements in large bank solvency and resiliency post-crisis. These improvements are well-documented and widely recognized

Average leverage of systemic banks and investment banks




Data source: 10K filings. J.P. Morgan includes preceding mergers, pro forma.

The solvency buffers of big U.S. banks have gotten much larger




Tangible equity divided by an estimate of the standard deviation of the annual change in asset value. Asset-weighted average of nine banks and I-banks. Source: Berndt, Duffie, and Zhu (2018).

Source: Darrell Duffie, "Prone to Fail: The Pre-Crisis Financial System," Darrell Duffie, available at http://papers.nber.org/conf_papers/f114468/f114468.pdf

# What Are The Effects on the Economy?

- Reforms have clearly improved resiliency but at what cost to the real economy? Evidence on the cost side of the ledger is mounting:

1. **Dodd Frank and Small Business Lending** (Borda and Duca 2018) -
   "By increasing the fixed regulatory compliance requirements needed to make business loans and operate a bank, the DFA disproportionately reduced the incentives for all banks to make very modest loans…"

2. **Stress Tests and Small Business Lending** (Cortes et. al. 2018) –
   "Post-crisis stress tests have altered banks' credit supply to small businesses. Banks most affected by the stress tests reallocate credit away from riskier markets and toward safer ones. They also raise interest rates on small loans."

3. **Forward Looking Statements by Large Banks About Corporate Lending** (JPMorgan Investor Day Presentation 2019)
   "focus on high quality loans – expect slower pace of growth"

- Post-crisis regulatory reform is affecting the broader economy

# Where is Large Bank Capital Headed?

- Regulators have stated that the level of big bank capital is "about right"

- Several recent capital proposals, however, would result in a measurable increase in required capital for large banks

  1. **Stress Capital Buffer** (SCB) proposal measurable increases required capital for large banks

  2. Capital requirements for derivative transactions (**SA-CCR**) increases required capital for large banks

  3. Other (as yet unproposed) elements of **Basel III finalization** have the potential to further increase large bank capital requirements (market risk, operational risk, standardized credit risk, Basel-Collins floor)

- The combined effect of all extant and forthcoming capital proposal should be considered holistically before finalizing these proposals

- The combined impact of all relevant capital requirements should be measured **holistically** and its impact on economic growth should be considered in a **clear** and **transparent** fashion by regulators (show your work)