Financialization, household wealth and voter attention: The changing politics of regulating systemically important banks


This article argues that much of the literature has underplayed the role of voters and elections in post-crisis regulatory politics. Instead, the real politics of financial regulation are mostly seen as an arena of elite contestation between industry lobbies and specialized bureaucratic agencies, resulting in regulatory outcomes that substantially favour globalized finance. I argue that the interests and the attention of middle class households have steadily become more closely linked to financialization, financial crises and large financial institutions in recent decades, and that this has influenced the trajectory of regulation of the most globalized banks. I argue that this can push politicians of varying partisan affiliations, particularly those in the most financialized systems, to support more regulatory tightening than in less financialized systems. At the same time, however, this regulatory tightening remains highly contested and its sustainability is uncertain, in part because of the heightened interest of households in the promotion as well as the protection of their wealth.

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“It is hard for me to imagine having a useful and informative popular debate about bank capital, but people keep trying. It seems to me that bank capital regulation has three drawbacks as a subject for public discussion in U.S. politics:

1. It is complicated.
2. Beyond the complexity, it is just sort of conceptually mysterious. Banking is a weird business. Did you know that bank deposits are actually debt, for the bank? Of course you did, come on. But when politicians and pundits try to have popular discussions about bank capital, they can’t assume that knowledge. And so they have to start from a weird place of not-quite-right metaphor. Capital is money set aside for a rainy day, or the delicious frosting on a layer cake of debt, or something.
3. It is very boring.”


As Levine suggests, quality public debate about the details of banking regulation is difficult to sustain, but almost a decade after the onset of the global financial crisis (GFC), debate continues nonetheless. Dan Tarullo, the hawkish Fed Governor responsible for financial regulation and the man that Wall Street most loved to hate, recently left office. President Trump and his Republican allies in Congress have argued for a repeal the Dodd-Frank Act and to provide Wall Street banks with an “off-ramp” intended to reduce the “burden” of financial regulation via the *Financial Choice Act* (Richardson, Schoenholtz, Tuckman, & White, 2017). In Europe, British threats to cut taxes and regulation to attract mobile firms were met with suggestions that some EU countries would seek to attract banks fleeing the City of London.¹ In the Basel Committee, progress on important details of the post-crisis regulatory agenda has stalled.² Post-crisis financial regulation therefore seems to be in a process of politicized retreat.

Many would go further to argue that this retreat began much earlier, reflecting the continuing instrumental and structural power of globalized finance and its ability to resist substantive constraint (Helleiner 2014). Critics pointed to the international regulatory proposals that have emerged from the Basel process since 2009 as a substantive watering down of early proposals for radical reform and re-

They claimed that the biggest banks had (re-)captured the policymaking process, successfully exercised their structural power in major polities, and emerged more dominant than ever. “Wall Street’s political influence”, one said, “is just too strong and too pervasive for reform advocates to overcome.” (Wilmarth 2013, 1295). Some policy insiders concurred, calling attention to how “…a handful of Wall Street financial institutions and their executives...were able to exert their power and influence to protect and reinforce a dangerous status quo that worked brilliantly for them but has left the rest of the country behind.” (Barofsky 2013, foreword).

Others argue that the financial crises of 2007-9 attenuated the political influence of finance and permitted a significant strengthening of financial regulation, including for the largest global banks (Drezner, 2014). Bell and Hindmoor, for example, argue that the crisis reduced the policy influence of finance by politicizing regulation, promoting ideational revision by elites, and empowering the state to reassert its authority over large financial institutions (Bell & Hindmoor, 2015). In this vein, The Economist opined that:

“Bankers had hoped that, after seven years of penance for their part in the financial crisis, the end of wrenching overhauls forced by fierce new regulations might be nigh. But to their dismay, the regulators’ zeal is undimmed. Far from giving banks respite, they are toughening up old rules and devising new ones, perhaps heralding a new wave of restructuring.”

Hence, not only are there significant disagreements concerning the nature and extent of post-crisis financial re-regulation, there are also basic disagreements over how the crisis affected the relative power of state and major private sector actors.

This article argues that much of the literature has underplayed the role of voters and elections in post-crisis regulatory politics. A number of authors point to how the crisis “politicized” financial practices, generating public anger and incentives for regulatory agencies and politicians to respond with more stringent regulation (e.g. Bell and Hindmoor 2017: 114). But in most accounts “the public” tends to be

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3 For an extensive and popular critique, see Admati and Hellwig (2013, 186 and infra).
seen as a dull mass exerting a temporary background effect on policymaking. It moves from pre-crisis passivity to a phase of sudden post-crisis collective “anger” that soon dissipates as the system stabilizes, complex and technical discussions about regulation take over, and as voter interest refocuses on the more standard topics of everyday politics. The real politics of financial regulation are mostly seen as an arena of elite contestation between industry lobbies and specialized bureaucratic agencies.

What is lacking, I suggest, is a deeper account of how voter interests have steadily become closely linked to financialization, financial crises and large financial institutions in recent decades, and how this influences the trajectory of regulation. Wealth accumulation for “middle class” households has increased dramatically since the 1970s in many developed democracies, which has sharply increased the stake of many households in financial markets and in policies that affect wealth held as savings, pension assets and housing assets (Jordà, Schularick, & Taylor, 2016; Knoll, Schularick, & Steger, 2017; Schwartz & Seabrooke, 2009). We have argued that this has been a major driver of financial fragility, of the increasingly extensive interventions that have occurred during successive systemic banking crises, and of far higher rates of political turnover related to the financial cycle (Chwieroth and Walter, forthcoming). In this paper, I argue that it also has two important consequences for post-crisis financial regulation.

First, the political salience of and public interest in such regulation is now higher and more sustained than in the past. This is partly because financialization increases the stake of many households and voters in financial regulation, but also because of other consequences of financialization. These include rising economic inequality, distributional conflict and a growing incidence of financial scandal. I argue that this can push politicians of varying partisan affiliations, particularly those in the most financialized systems, to support more regulatory tightening than in less financialized systems.

Second, these post-crisis surges in financial re-regulation are often neither politically sustainable nor especially radical in nature. Structural power theories have often emphasized the importance of bank lending to nonfinancial firms and thus for jobs and growth, but the interest of middle class households in their wealth
portfolios and the provision of credit makes them another key source of demand for a liberal financial system. The result is that tighter post-crisis regulation in highly financialized economies does not mean a return to the postwar model of financial repression (Helleiner, 1994). Calls for “utility banking” or making “finance the servant rather than master” of the so-called “real” economy overlook how the political ground has shifted decisively against this option (e.g. Bell and Hindmoor 2017, Kashkari 2016). Politically, highly financialized countries are caught between satisfying widespread demands for the protection of accumulated wealth and demands for its promotion, including via the continued flow of credit. This places substantial political limits on the potential for post-crisis regulatory tightening and engenders continuing contestation over the regulatory innovations that are adopted.

I assess these claims by comparing the post-crisis regulatory trajectories of the two most prominent and highly financialized cases, the United Kingdom and the United States. I focus on their treatment of the very largest, “global systemically important” banks (G-SIBs), since it is precisely these financial institutions that much of the literature would expect to possess the greatest ability to resist regulatory tightening. I show that in fact both countries, despite their partisan differences, have adopted new regulations that have gone further than those that their less financialized partners have supported. Nevertheless, this relative “overcompliance” has done little to reverse the extensive financialization that has occurred in both countries, or to reduce the dependence of American and British households on the credit and financial markets on which much of their wealth depends. In both cases, overcompliance has also brought with it rising political contestation over the regulatory tightening that has occurred since 2009.

The rest of the paper is organized as follows. Section 1 provides a brief overview of the political economy literature on post-crisis financial regulation and Section 2 outlines how my own argument differs. Section 3 compares the post-crisis regulatory trajectory in these two countries, focusing on the treatment of G-SIBs. Section 4 assesses these outcomes in light of the earlier theoretical discussion and a final section concludes.
The political economy of post-crisis financial regulation

There is a large and varied literature on crises as “critical junctures” associated with policy and institutional change. Crises can delegitimate existing practices and the ideas that sustain them, while providing opportunities for political entrepreneurs to promote new solutions and institutional forms (Blyth, 2002; Boin, Hart, & McConnell, 2009; Collier and Collier 1991; Capoccia 2015; Haüsermann 2010). The literature on “punctuated equilibria” argues that crises can provide new information to boundedly rational actors that suddenly shifts politics into new territory (Jones & Baumgartner, 2012; Weyland, 2008). An extensive literature in international relations/political economy sees great power wars and global depressions as drivers of domestic policy change, institutional innovation and systemic change (Frieden 1988; Gilpin 1981, 1987; Krasner 1976; Widmeier, Blyth and Seabrooke 2007). In a classic example of crisis-driven change, the financial crises of the early 1930s, the associated Great Depression and the experience of World War Two are commonly seen as having engendered a new consensus on economic management and and financial regulation (Helleiner, 1994; Ikenberry, 1992; Ruggie, 1982).

Many scholars see such change as exceptional and emphasize the ability of business coalitions, especially those from industries essential to the generation of jobs, income and growth, to exercise “structural power” via exit or capital strikes (Lindblom 1977; Strange 1994). The ability of reform opponents to block change may also depend on their access to institutional vetoes (Tsebelis 2002). The role of institutional forms of influence such as “regulatory capture” by industry due to revolving doors, lobbying and campaign donations have become common claims in relation to the financial sector and sources of deep pessimism regarding post-crisis reform in highly financialized political economies (Hacker and Pierson 2010, 2016; Igan, Mishra and Tressel 2012). Past policies can also shape industry structure, which in turn can affect the ability of business to mobilize and build political coalitions. As historical institutionalists emphasize, distinct past national political

6 This is also a common position among activists, journalists and radical theorists on the political left and the right. E.g., see Matt Taibbi, “Why the Banks Should be Broken Up,” Rolling Stone, April 8, 2016.
bargains and institutional choices can constrain the possibilities for change in the present.

Culpepper (2010) notes with other scholars that the structural and instrumental power literatures fail to explain why business sometimes loses major policy battles, and builds on an earlier literature to argue that the potential for regulatory reform will depend on the political salience and complexity of particular issue areas. Disruptive policy and institutional change is more likely in policy domains with high political salience, since this tends to move contestation from the “quiet politics” that prevails in areas of low salience and high complexity to the “noisy politics” in which industry and bureaucrats lose influence, and politicians of all stripes must respond to voter concern. Crises can delegitimise the claims of business groups to special expertise, increase the incentives of politicians and the media to invest in the acquisition of expertise, and open up new possibilities for reform (Culpepper, 2010; Gormley, 1986; Meier, 1988). In areas like financial regulation in which “quiet politics” usually prevails in normal times, the effects of crises in increasing their political salience can be significant but temporary (Coffee 2013, 1029). As public attention wanes, regulatory politics in this view gradually shifts back to contestation between industry and policy technocrats, where business tends to be more powerful.

Bell and Hindmoor (2015) add that ideational innovation in the aftermath of crises can reduce the potential for the exercise of structural power by industry opponents of regulatory reform, by politicizing regulation and revising policymaker understandings about the costs and credibility of business exit threats. Structural power, they argue, does not simply derive from the material position of finance in the economy, but is mediated by ideas that are prone to be revised in the aftermath of crises. They go further to argue that this can generate institutional change that at least to some extent locks in post-crisis regulatory tightening (Bell & Hindmoor, 2017, pp. 115–116).

Financial globalization can also alter the nature of post-crisis regulatory responses in important ways. Singer (2007, 21-32) argues that it requires regulators seeking to reestablish banking systems after crises to forge approximately harmonized regulations with their international counterparts, removing the
incentive of political principals to object on the ground that tighter regulation would undermine the competitiveness of national firms.\(^7\) Shared crises and financial globalization, in this view, produce convergent policy trajectories shaped by international negotiation. The prospects for regulatory convergence are also increased by the potential for new ideas to spill across borders and to be clarified and disseminated in the international institutions in which policymakers now so often collaborate intensively, especially in the aftermath of shared, deep crises.

2 Financialization, regulation, and voter interests

The role of electoral politics in this literature is usually modest and often non-existent. Culpepper (2010) emphasizes this factor most, arguing that crises and scandals act to raise temporarily the political salience of arcane policy matters such as financial regulation. This requires politicians of all partisan persuasions to pay attention, reducing the dominance of industry and bureaucratic interlocutors, providing a (perhaps brief) window of opportunity for reformers. During such periods, governments – including those most closely associated with business interests – have strong incentives to align policies with the dominant policy preferences of voters.\(^8\)

Building on this, I emphasize the way in which processes of financialization and associated wealth accumulation have steadily increased the importance of financial markets and their regulation for many households and voters in developed democracies. Financialization is a process of financial deepening and increasing complexity, characterized by ‘the substitution of trading and transactions for relationships, and the [associated] restructuring of finance businesses.’\(^9\) Banks have

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\(^7\) An alternative theory is that regulatory divergence is sustainable if it reflects intra-industry preferences. “Tiebout sorting” occurs when different firms locate activities in different regulatory jurisdictions in ways consistent with niche strategies (e.g., banks cultivating a reputation for safety might gravitate towards more stringently regulated jurisdictions) (Carruthers and Lamoreaux 2016, 78-82).


become steadily more important in modern economies as facilitators of the payments system, as brokers who match lenders with borrowers, and as managers of other actors’ savings and financial risk. This rising complexity raises the potential for systemic risk in the financial system, or ‘the risk that the inability of one or more participants to perform as expected will cause other participants to be unable to meet their obligations when due.’

Many middle class households have growing stakes in this interconnected system, including savings in money market and investment funds and housing equity leveraged by mortgage finance. The growth of housing equity and the move towards defined contribution pension schemes have increased households’ stake in a much broader class of underlying financial assets. Since systemic banks and other financial institutions are so closely involved in the financing, management and trading of housing and financial assets, the stake of the middle classes in the activities of these firms has grown significantly.

Figure 1 shows the sharp rise in real net private wealth per capita in a number of advanced countries since 1970. Much of the wealth that has been accumulated by the middle classes has been in the form of housing equity and pension assets, with the latter held increasingly in market-sensitive defined contribution schemes. One indication of the extent of this shift over the long run is in rates of owner-occupied housing, which increased in Britain from about one-fifth to more than two-thirds of households over the twentieth century. Similar trends occurred elsewhere.

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12 Piketty and Zucman, ‘Wealth and Inheritance in the Long Run’.


Mortgage lending in particular grew rapidly over the course of the twentieth century, facilitating what Jordà, Schularick, and Taylor refer to as the ‘democratization of leverage’: ‘Nearly all of the increase in the size of the financial sectors in Western economies since 1913 stems from a boom in mortgage lending to households and has little to do with the financing of the business sector.’

The result has been rising household sector leverage and greater financial fragility in many advanced economies. The dependence on leverage to acquire housing assets has been particularly marked in countries experiencing house price booms and increasing inequality. Figure 2 shows the general increase in mortgage

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debt in advanced countries, which in many cases accelerated sharply from the 1980s.

**Figure 2:** Mortgage loans to non-financial private sector, selected countries 1945-2014, per cent of GDP.

As Ansell points out, these trends have had important consequences for individual social policy preferences.\(^{18}\) Households in developed and many developing countries have acquired a much greater interest in the maintenance of the flow of credit, particularly mortgage credit, than before World War Two (Chwieroth and Walter, forthcoming; Schwartz and Seabrooke 2009). The rapid growth in household wealth that began in the 1980s has also tied their interests more than ever before to

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the activities of SIBs, who operate at the core of these financial markets. Relevant household surveys in advanced democracies reflect this high consumer demand for financial stabilization.¹⁹

These developments have also increased the political salience of financial regulation over time, especially in countries in which financialization is most extensive. A plausible measure of this, as Epstein and Segal (2000) and Culpepper (2010) have shown, is front page coverage of the topic in major national newspapers. Such coverage indicates investment by journalists in relevant expertise and an expectation of heightened public interest and political relevance. Figure 3 provides counts by decade and year of front page articles related to financial regulation in the New York Times since the 1920s.

[N.B.: I am still compiling similar counts for The Times (London) as a UK comparator].

Figure 3: Front page stories, count by decade/years, *New York Times*: “regulation AND (finance OR financial OR bank)”

Note: 2010-2019 includes only 4 years.
Min=343 (1920s); Max=983 (1930s)

Note: 2010-2019 includes only 4 years
Min=373 (1950s); Max=951 (1990s)

Min=1 (2000); Max=82 (2011).

These data suggest that financial regulation in the United States suddenly became politically salient in the 1930s during the Great Depression years. Salience
then declined significantly in during the Bretton Woods era, then rose again from the 1970s. There is a strong correlation with systemic banking crises, with a sudden increase in front page newspaper coverage in 2008; salience remained high for four years after the peak of the crisis before tailing off from 2012. It remains substantially higher today compared to the early 2000s: there were still 21 *New York Times* front page stories on this topic in 2016 compared to only 1 in the whole of 2000.

There is also considerable evidence that financialization is strongly associated with more financial fraud and scandals that hits the headlines. Figures 4 and 5 indicate the incidence of financial fraud or scandals in newspapers and books respectively over the long run. These fell to low levels in the Bretton Woods era of financial repression and reached new heights from the 1980s.

**Figure 4**: Decade counts of financial “fraud” or “scandal”, *New York Times*

![Figure 4](image)

Note: Search term on Proquest: (finance OR financial OR bank) AND (fraud OR scandal). All articles are included. Note that the final decade includes only 4 years of data. Min=2,357 (1940s), Max=13,472 (2000s).

**Figure 5**: Google Ngram: relative incidence of “financial scandal”, all English books, 1860-2000

![Figure 5](image)
To summarize, financialization and the associated increases in household wealth and financial leverage have increased the political salience of and public interest in financial regulation as a means to the protection and promotion of wealth. Although crises and financial scandals are strongly associated with periods of relatively high political salience of financial regulation, there is also an underlying trend for such regulation and scandals to become increasingly salient over time. It is also possible that the high cost of bailouts and headlines concerning high financial sector compensation have played a role in increasing the political salience of financial regulation (Chwieroth and Walter, forthcoming).

The implication of this argument is that deep crises should induce politicians to respond to high voter interest in this domain to deliver more stringent post-crisis regulation than their peers in less financialized systems. This expectation is different from those theories that predict international harmonization of post-crisis regulation in major jurisdictions (Singer 2007), and from theories that emphasize the ability of major banks to deploy effectively their structural power or “capture” of the political process in the most financialized political economies.

I am not claiming that average voters have a strong interest in or understand the detail of financial regulation. As financial complexity has grown sharply in recent decades, so too has the complexity of financial regulation. Most voters are unlikely to sustain a strong interest in the technical details of financial regulation in the aftermath of crises, even if they have a strong interest in a regulatory response that protects and promotes their wealth. As the political salience of such regulation tails off in the aftermath of crises, we would expect industry experts to gain more influence over regulatory outcomes (Culpepper 2010). Whether this is sufficient to reverse the tendency for more financialized economies to adopt relatively stringent post-crisis regulation is unclear. Such reversals may depend on the scale and frequency of post-crisis scandals, variations in the relative structural power of the financial sector across different jurisdictions (Culpepper and Reinke 2014) and in the relative autonomy of national regulatory agencies (Keefer and Stasavage 2003). But
it also depends, I suggest, in the conflicting preferences of households in both protecting and promoting their wealth.

3 G-SIB regulation in the UK and USA

I now turn to assess these expectations by comparing the post-crisis regulatory treatment of G-SIBs in the two most financialized major economies, the United Kingdom and the United States, compared to their major peers. I focus primarily on formal regulatory standards and rules, though I also pay attention to bank-level outcomes. I show that there has been a broad increase in regulatory stringency since 2012-13 in both countries that goes beyond the regulatory phase-ins associated with new Basel III regulatory standards, but that trend was more marked in the US than in the UK case.

As in other crisis-affected countries, incumbent governments in the UK and USA responded to public pressure both to stabilize their banking systems through extensive intra-crisis interventions and to deliver significant increases in regulatory stringency for systemically important banks. Obama’s victory over his Republican counterpart as a relative political outsider in the November 2008 Presidential elections owed a good deal to the crisis that had reached a peak only two months earlier. It is important to recognize that the Republican candidate, John McCain, was also forced to adopt a more interventionist stance in the wake of the crisis. He did so explicitly in the context of protecting household wealth:

“we also need to do more to build confidence that American investments and retirement accounts are safe, so I will reform the markets and Wall Street. I will make sure that the SEC enacts and enforces rules that keep our markets safe and competitive. I will demand complete transparency into the accounts and activities at all banks and insurance companies so they cannot take on the kind of risk that brought down the financial system. We will have strict rules of conduct on Wall Street and if they are broken executives will be severely punished. I know -- and the smartest people in business and industry agree -- that these actions will restore confidence, get stock prices moving up again and increase the value of your hard earned savings and investments.”

Although it may not be surprising for a centre-left Obama administration to pursue financial re-regulation, Gordon Brown’s Labour government in the UK also

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20 John McCain, Remarks After Holding a Meeting on the State of the Economy in Cleveland, Ohio, October 27, 2008.
committed itself to major regulatory reform in the wake of the crisis. Its subsequent loss of office in the May 2010 elections also owed much to the crisis. The victors in this election, David Cameron’s traditionally very pro-City Conservative Party, responded to public pressure by committing themselves to “reform the regulation and structure of the banking system to ensure lower levels of leverage [and] less dependence on unstable wholesale funding.” (The Conservative Party (UK), 2010, p. 5). Responding to anti-bank public sentiment, they also pledged to give the Bank of England authority to empower the Bank of England “to crack down on risky bonus arrangements” and to impose a tax levy on banks (ibid. 29). There was, in short, substantial cross-party consensus on the need to re-regulate finance in ways that had not been contemplated since the 1970s.

Both newly elected governments in the UK and USA were also willing to give independent regulatory agencies located in their central banks substantial discretion to implement these policies, against the wishes of major banks and their lobby groups. As I outline below, the British and the American regulatory authorities chose to go somewhat further than agreed international regulatory minima, which senior figures in both the Bank of England and the US Federal Reserve saw as insufficiently stringent.

a. Basel benchmarks

A series of proposals emerged in the Basel Committee for Banking Supervision (BCBS) to increase capital requirements for all banks as political and policy elites revised their views about the risks posed by financialization, especially for the large and often complex “systemically important banks”. This represents a substantial divergence from pre-crisis consensus, when policymakers encouraged the adoption of “internal models” of risk assessment, pioneered by some major global banks, dangling the carrot of potentially lower future capital requirements for banks that deployed such technologies. Since the crisis, major banks went gone

21 The Basel Committee hedged its bets by applying transitional “capital floors” to banks using advanced internal approaches to ensure that their capital levels did not fall sharply – in part to assuage the objections of smaller banks that Basel II would place them at a competitive disadvantage (BCBS 2006, 13-14; Herring 2007). However, the implication of Basel II, as for the earlier (1996) Market Risk Amendment that permitted the use of internal models for the calculation of trading book
from being relatively favoured in regulatory terms to being penalized for their systemic importance and the associated “systemic risk” they pose.\(^22\)

There are three main areas of regulatory innovation of special relevance since 2008: capital surcharges for G-SIBs, loss absorbing capital, and risk weighting practices. All three were foreshadowed in the early phase of post-crisis international regulatory reform, but more recent proposals from the Basel process have contributed to a growing perception of regulatory tightening, especially for G-SIBs. Banks, their lobby groups, industry consultants and many journalists now commonly refer to these post-2010 standards on G-SIB capital surcharges and TLAC requirements as a new “Basel IV”, with the strong implication that they are significantly more onerous than Basel III.\(^23\) Although this is an exaggeration, tightening has been significant regarding the regulation of risk-weighting since 2013.

New “capital surcharges” for SIBs (including G-SIBs and their domestic counterparts, “D-SIBs”) were prefigured in Basel III in 2010 (BCBS 2011, 7). At the request of the G20 leaders, the BCBS and FSB subsequently negotiated and agreed the details over 2011-12. In November 2011, the FSB announced agreement on, among other things, capital surcharges from 1% to 3.5% for a list of 29 G-SIBs and called for “more intensive and effective supervision of all SIFIs” (FSB 2011).\(^24\) These capital surcharges would be phased in between January 2016 and January 2019, when they will become fully effective, and applied as an addition to the required capital conservation buffer (CCB) contained in Basel III. BCBS members agreed that implementing legislation and regulations would be adopted by 1 January 2014.

The G-SIB capital surcharge must consist of Common Equity Tier 1 (“CET1”) capital and be calculated as a percentage of risk-weighted assets (RWAs). Accordingly, the minimum CET1 Basel III capital requirement could in principle be as

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\(^22\) G20 Leaders’ Statement, September 24-25, 2009, Pittsburgh.


\(^24\) The list of designated G-SIBs is now updated annually.
high as 10.5% for some G-SIBs. Table 1 provides the G-SIB list from late 2015, which allocates each bank to specific “risk buckets” and associated capital surcharges. Figure 6 shows how they vary by risk bucket and asset size. As of November 2015, the highest surcharge was 2.5%, applied to HSBC (UK) and JP Morgan Chase (US), implying a minimum CET1 requirement of 9.5% of RWAs for these two banks. This is well above the effective Basel II minimum equity capital requirement of only 2% of RWAs, though this understates the increase in equity capital requirements because the RWA calculation methodology has also been tightened.

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25 I.e. the standard 4.5% CET1 minimum plus the 2.5% CCB that applies to all banks, plus any applicable G-SIB surcharge.
27 Cecchetti (2015, 133) estimates that using Basel III definitions, the minimum required capital under Basel II was a mere 0.50-0.75% of RWAs.
Table 1: G-SIBs in alphabetical order within each systemic risk bucket (November 2015 FSB list)

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It is clear that there has on this important measure been a substantial increase in regulatory stringency for these banks since the crisis. Vocal complaints by major banks are consistent with this. For example, JP Morgan’s chief risk officer called the capital surcharge “a bridge too far, and creates costs that risk exceeding the diminishing benefits of higher capital requirements above Basel III minimums” (Zubrow 2011, 4). The Institute for International Finance, a major bank lobby group, also opposed the surcharge on principle, arguing that it had “fundamental concerns about designating groups of firms as potentially systemic and applying additional loss absorbency requirements to these” (IIF 2011, 13).

Also prefigured in Basel III was a new requirement that all SIBs issue additional “loss absorbing capacity beyond the minimum standards” (BCBS 2011, 7). As opposed to standard capital requirements, which are intended to ensure that banks issue sufficient capital to maintain their businesses as “going concerns”, loss-absorbing capital is intended to provide an extra capital buffer for “gone concern” banks that have failed so as to avoid the need for public bailouts. This is one component of a host of new rules relating to the resolution of insolvent large financial institutions. In September 2013, the G20 leaders’ meeting at St Petersburg welcomed an FSB (2013) report on a strategy for ending TBTF and asked it to
develop proposals to ensure that G-SIBs had adequate loss-absorbing capacity in the event of failure so as to ensure orderly resolution, continuity of critical functions, and avoid taxpayer losses. Regulators negotiated new standards on Total Loss-Absorbing Capital (TLAC) requirements for G-SIBs over 2014-15. TLAC will consist of “bail in” debt that can be written down or can be converted into equity during the resolution of a failed G-SIB. Minima were set at 18% of RWAs, 6.75% of the Basel III leverage ratio denominator, and one third must be long term unsecured debt – all to be implemented by 2022 and 2028 for emerging countries (FSB 2015, 10).

A third area of increasing regulatory scrutiny is asset risk weighting practices. This was also prefigured before 2013. The crisis revealed serious weaknesses in the internal value-at-risk (VAR) models that were used to measure risks in banks’ trading portfolios from the mid-1990s. In mid-2009, the BCBS issued modifications to Basel II that substantially increased average risk weights for banks’ trading books (BCBS 2009). The results of their investigations of banks’ internal risk modelling for the banking book increased regulator concerns (BCBS 2014; see also BCBS 2013; BoE 2011, 51; BIS 2013, 54-65; Haldane 2013). The BCBS’s own “studies confirmed that there are material variances in banks’ regulatory capital ratios that arise from factors other than differences in the riskiness of banks’ portfolios. These variances undermine confidence in capital ratios”. Some major banks were suspected of engaging in “window dressing” by managing downwards the risk weights on substantial portions of their asset portfolios so as to reduce their aggregate capital requirements (BIS 2013, 54-55).

Unexpected events contributed to this growing scepticism. The US Senate subcommittee that investigated the large trading losses suffered by JP Morgan Chase in its “London Whale” unit, which first surfaced publicly in April 2012, found that the bank engaged in deliberate attempts to manage down its RWAs. This was disconcerting because JP Morgan Chase had been considered one of the best managed and more conservative of the major US banks, and one of the few that might have weathered the GFC without government assistance (US Senate 2013, 14,

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28 G20 Leaders’ Declaration, September 6, 2013, St Petersburg.
29 The TLAC requirement is in addition to the CET1 minimum of 4.5%; CET1 capital above this minimum cannot not count towards TLAC.
Unsurprisingly, market investors have also become increasingly sceptical of the value of internal models (Haldane 2013).

The policy responses to these concerns have been significant and cumulative in their impact and of substantive consequence for SIBs (BCBS 2014b). The first has been to impose a minimum unweighted leverage ratio (Tier I capital of 3% of “total exposures”) as a backstop to risk-based capital ratios, as proposed in 2010 in Basel III.\(^\text{30}\) Perhaps more importantly, the BCBS has increasingly restricted the use of internal models for risk assessment. This includes eliminating its use in a number of important areas (including most recently for assessing operational risks), and placing permanent, higher “floors” under internal risk weights in both the banking and trading books.\(^\text{31}\) In short, major banks are increasingly being required to rely much more heavily on the standardized approach to risk assessment, making it much more difficult for them to use internal models to achieve lower capital requirements than other banks.\(^\text{32}\) On the trading book side alone, which particularly affects the major G-SIBs, the BCBS estimates that compared with the existing framework (itself revised substantially in 2009), the new market risk framework will require a weighted average increase of 40% in banks’ market risk capital requirements by 2019 (BCBS 2016b, 7).\(^\text{33}\)

In sum, the Basel process has proposed a substantial cumulative and coordinated tightening of regulation since 2009 that is targeted specifically at the largest banks, especially the G-SIBs. Critics argue that this increased regulatory stringency is sub-optimal, but the direction of change is not in doubt.

\(^{30}\) Critics like Admati argue this is far too low. “Total exposures” includes a measure of off-balance sheet assets, as specified in BCBS (2010, 61-63) and clarified in BCBS (2014a). The BCBS asked for comments on whether there should be a higher leverage requirement for G-SIBs to maintain proportionality between their risk-weighted capital requirements and the leverage ratio requirement, though as yet there is no agreement to do so (BCBS 2016f, 8).

\(^{31}\) The floors are set with the “standardized approach” to risk weighting that is used by less sophisticated and usually smaller banks. Furthermore, the BCBS has increased some risk weightings in the standardized approach (BCBS 2014b, 2015, 2016a, 2016d, 2016e). The BCBS is also conducting a separate though highly contentious review of how banks should calculate risk weightings for sovereign exposures, which currently remain at zero for OECD exposures (including, for example, exposure to Greek debt). After the Eurozone debt crisis, which reached a peak after agreement on Basel III, the status quo in this area is unlikely to stand.

\(^{32}\) See the responses to the standardized capital floors proposal by the Institute for International Finance et al. (2015).

\(^{33}\) This compares with an estimated impact of a 74% increase for the BCBS’s earlier proposals, suggesting some reduction in the level of stringency in the final version, but still a substantial increase on the “Basel 2.5” 2009 revision.
b. G-SIB regulation: US and UK cases

How, if at all, has G-SIB regulation in the US and UK cases differed from the minimum harmonization achieved in the Basel process? I argue that the trend in the US case has until very recently been towards further regulatory tightening since 2013, including going beyond Basel minima in a number of key areas. In the UK too, early post-crisis proposals suggested that the British authorities – with the support of the Conservative-dominated government – would also exceed Basel minima in their regulation of SIbs, though there was more substantial backtracking on these early pledges than in the US case.

**The United States**

In December 2014, the US Federal Reserve Board (FRB) outlined how it would implement the BCBS framework for US G-SIBs. It proposed changes to the calculation methodology that official and private analysts believe will require “significantly higher [capital] surcharges for US G-SIBs compared with their global peers” (PwC 2014, 1). The final rule was issued in August 2015. These requirements would be phased in over 2016-2019 along with the capital conservation buffer. Together, they imply that some US G-SIBs will be subject to minimum CET1 requirements of up to 11.5% of RWAs (plus any countercyclical capital buffer required by authorities), or up to 2% more than Basel minima.

US regulators also proposed in July 2013 a new minimum 5% leverage ratio for the largest US bank holding companies (BHCs), including all current US G-SIBs, and a 6% requirement for their bank subsidiaries. All other banks that qualify for

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34 The proposal is to calculate the capital surcharge applicable to G-SIBs by the higher of two methods. The first method is aligned with the BCBS framework, based on a bank’s size, interconnectedness, cross-jurisdictional activity, substitutability and complexity. The second method is a US-specific calculation that replaces the substitutability factor with the bank’s reliance on short-term wholesale funding. The FRB estimates that this second method would lead to an additional capital requirement of 1%-4.5% of risk-weighted assets, whereas the first method would add 1%-2.5% (consistent with the Basel standard). See also (US) Office of Financial Research (2015, 1).


the advanced approach to capital calculation will be subject to the minimum 3% Basel leverage ratio and to the US minimum Tier 1 leverage ratio minimum requirement of 4% of Tier 1 capital to total on-balance-sheet assets (US GAAP definition) that applies to all US banks. US regulators finalized this proposal in April 2014 despite concerted opposition from major banks. In September 2014, regulators brought the denominator calculation for this leverage ratio into conformity with changes agreed to in the BCBS in January 2014, ensuring that the higher US leverage requirement would have practical effect.

In October 2015, the Federal Reserve issued its TLAC proposals. These called for US G-SIBs to issue TLAC of no less than the greater of 18% of RWAs (consistent with the FSB standard) and 9.5% of the BHC's total leverage exposure under the supplementary leverage ratio rule. The latter is significantly more stringent than the FSB standard of 6.75% of total leverage, with the same implementation schedule. BHCs would also have to maintain an additional external TLAC buffer that is not contained in the FSB standard. The Fed’s justification for leverage ratio will apply from 2018 to all BHCs with more than $700 billion in consolidated total assets or more than $10 trillion in assets under custody and to their insured depository institution subsidiaries.

37 Banks complained that the enhanced leverage ratio will become a “frontstop” for minimum Tier 1 capital requirements rather than a backstop, reducing lending, growth, and putting them at a disadvantage vis-à-vis foreign banks (The Clearing House 2013; “Leverage Ratio Rule puts U.S. Banks at International Disadvantage,” Financial Services Roundtable, April 8, 2014). A failure to meet the enhanced ratio would lead to restrictions on the ability of US G-SIBs to pay dividends or to make discretionary bonus payments to staff.


40 This buffer must be at least 2.5% of RWAs plus banks’ Method 1 G-SIB surcharge, plus any applicable countercyclical capital buffer (potentially up to 8% in total, a provision). The BHC would also be required to maintain outstanding eligible external long term debt of not less than the greater of 6% of RWAs plus the applicable (Method 2) G-SIB capital surcharge and 4.5% of total leverage exposure (the FSB standard does not add the G-SIB surcharge to the requirement). This is the equivalent of the standard G-SIB BHC minimum CET1 and leverage requirements, less a standard allowance of 1% and 0.5% respectively for “balance sheet depletion” in the event of failure.
this standard was in part that this greater stringency was needed to ensure that TLAC would have been sufficient to exceed “a substantial majority of the [historical] loss-and-recapitalization experiences surveyed.”\textsuperscript{41} The five major US bank lobbies objected collectively to the proposals.\textsuperscript{42} The finalized rule is yet to be issued, but past experience suggests the US agencies are unlikely to grant the banks’ wishes.

The US authorities have also been relatively aggressive in acting against perceived misuse of internal risk models. Daniel Tarullo argued vocally instead for greater reliance – including among all BCBS members – on a combination of the leverage ratio and stringent stress-testing, which it has pioneered.\textsuperscript{43}

The Fed has also applied relatively stringent Comprehensive Capital Analysis and Review (CCAR) annual “stress tests” to all US G-SIBs. JP Morgan complained that these scenarios envisaged losses for it exceeding those of the 2008-9 crisis and on a par with those in the Great Depression.\textsuperscript{44} In the 2016 CCAR exercise, the minimum required leverage ratio for BHCs is 4% and the minimum CET1 ratio was 4.5%, as in 2015, but all banks are required to use standardized approaches to calculate RWAs (FRB 2015, 2016). In June 2016, Governor Tarullo announced that the Fed would add capital surcharges into the G-SIB post-stress test minimum capital requirement from 2018 – a further indication of increasing regulatory stringency for the largest banks. At the same time, stress test requirements for mid-size US banks were slightly relaxed.\textsuperscript{45}

In short, since 2013 the US regulatory agencies have been willing and able to impose increasingly tight regulatory requirements on its G-SIBs than Basel minima. They have concentrated this tightening of regulation on these eight largest banks, reflecting a concern to deal with the very largest banks first and perhaps to effect a divide and rule strategy.

\textsuperscript{41} \textit{80 FR 74932.}
\textsuperscript{42} The Clearing House et al., “Comment Letter on the Notice of Proposed Rulemaking on External TLAC, Long-Term Debt, Clean Holding Company and Other Requirements Applicable to U.S. G-SIBs,” February 19, 2016, 12. On the latter, they argue that banks should be free to meet the TLAC requirement with equity if they choose.
\textsuperscript{44} “JPMorgan chief Dimon warns on dangers of undermining US banks,” \textit{FT.com}, April 7, 2016.
The United Kingdom

The UK, while it remains a member of the EU, has somewhat less autonomy in setting its domestic financial regulation than the United States. It is subject to the requirements of the EU’s Capital Requirements Regulation (CRR) and the revised Capital Requirements Directive (CRD), collectively termed the “CRD IV package”, in force since 1 January 2014 (with various provisions phased to 2019). The CRR, which is binding across the EU, contains common rules for all EU credit institutions and investment firms. The CRD contains provisions that must be implemented by member states in ways relevant to their national circumstances, and thus allows an element of national discretion.

As regards G-SIBs, Article 131 of the CRD on “global and other systemically important institutions” is the most relevant; the CRR (Article 441) only deals with a few reporting requirements. Thus, national implementation, as in the US case, remains crucial. Article 131 section 4, in force since 1 January 2016, implements the BCBS/FSB regime on G-SIBs. National authorities can choose to reallocate a G-SIB to a higher risk sub-category. Article 133 also allows national authorities the right to introduce a CET1 systemic risk buffer applied to the whole or part of the financial sector to prevent and mitigate long term non-cyclical systemic or macroprudential risks not covered by the CRR.46 Thus, the UK’s capital surcharges for G-SIBs are currently largely set at the EU level.

However, significant national discretion remains, and key figures in the Bank of England pushed strongly for higher degree of regulatory stringency for SIBs in the UK compared to elsewhere in the EU. This included Mervyn King, former Governor, Andy Haldane, former Executive Director of Financial Stability and now its Chief Economist, and David Miles, a former member of its Monetary Policy Committee (Haldane 2012; King 2016, 280; Miles et al. 2012). This was also supported by John Vickers, who chaired the post-GFC Independent Commission on Banking (ICB), and other members of this committee. The result in practice has been that the UK G-SIB regime has evolved towards a somewhat greater stringency than the Basel benchmarks, but less so than in the US case.

46 For SIBs, the higher of this and any institution-specific additional capital buffer applies, though authorities may apply both if the systemic risk buffer only applies to domestic exposures.
In April 2015, the UK government handed the Bank of England’s Financial Policy Committee (FPC) formal powers of direction over the leverage ratio and related capital buffers applying to all UK financial institutions. The UK government gave the FPC authority to set requirements in this area ahead of agreement within the BCBS on the final calibration of the leverage ratio in 2017, and ahead of the EU’s adoption of a leverage ratio, on the grounds that the UK is home to a relatively large number of G-SIBs (four), the large size of its financial sector, and the risks these pose to financial and economic stability.

In July 2015 the FPC (2015, 8) proposed a minimum 3% leverage ratio for UK banks from 2018 and as early as practicable for UK SIBs, the same as the Basel benchmark. It also proposed supplementary leverage ratio buffers and a countercyclical leverage ratio buffer at 35% of the relevant capital surcharge requirement for SIBs, to maintain a stable relationship between the leverage ratio and the various risk-weighted capital requirements. The proposed supplementary leverage ratio buffer rates for UK G-SIBs would reflect their additional CET1 supplementary risk-weighted capital requirements. Since these currently range from 1% to 2.5%, the FPC has proposed supplementary leverage ratios for current UK G-SIBs of between 0.35% and 0.875% (35% x 2.5% = 0.875%), or up to 3.875% in total. This is above the Basel minimum but below that applied to major US banks.

Overall, the British authorities’ view on the amount of total Tier 1 capital required by major UK banks appears to have settled on 11% of RWAs (excluding any CCB requirements) as “about the right amount” (FPC 2016, 5). Of this, 9.5% should be CET1 capital. This is lower than the BoE’s own earlier estimates of the desirable level of large bank capital, but significantly above the Basel minimum (BoE 2015b, 4). The FPC also argues that greater relative stringency can be achieved via bank resolution regimes and by imposing additional countercyclical capital requirements (FPC 2015, 15-16; FPC 2016, 9).

47 These include a supplementary leverage ratio buffer for UK G-SIBs and other D-SIBs subject to a systemic risk buffer, as well as a countercyclical leverage ratio buffer (CCLB) applying to all regulated firms. The former is to be phased in over 2016-2019 for G-SIBs alongside their capital buffers and for D-SIBs from 2019.
48 So HSBC would currently face a minimum leverage requirement of 3.875% (as of end-2015, its actual Basel III leverage ratio was 5.0%), and minimum CET1 and Tier 1 ratios of 9.5% and 11% of RWAs respectively. Elsewhere, the BoE has said that UK banks should hold Tier 1 capital of no less than 3.75% of total assets (Brazier 2016).
The FPC is proposing a capital surcharge for ring-fenced banks of 1.3% of RWAs on average, compared to the 3% recommended by the ICB, which also proposed in 2010 a much lower asset threshold for such surcharges. Regulators argue that this is not a regulatory retreat, but John Vickers is doubtful (Carney 2016, 6; Vickers 2016b). In October 2015 the Prudential Regulatory Authority (PRA), housed within the Bank of England, also issued more flexible rules regarding the ability of RFBs to transfer capital to other parts of their business, diluting the stricter separation proposed by the ICB.

Regarding TLAC requirements, the Bank of England has indicated that it expects to apply the minimum Basel standards to UK G-SIBs (BoE 2015a, 11).

As for risk weighting, the Bank of England has been a prominent critic of the large variation in internal risk modelling and is supportive of the ongoing review of their use in the Basel process. It appears likely to implement the various BCBS proposals. Like other major regulatory authorities, the Bank now conducts annual stress-testing exercises. The 2016 stress scenario outlines a downturn similar to that experienced over 2008-9 with a larger (30%) fall in UK house prices (BoE 2016). However, the capital hurdles required of major banks are somewhat lower than those for US G-SIBs. In 2016, the minimum hurdle leverage ratio was 3.13%, and the minimum CET1 ratio is 4.5% plus individual banks’ pillar 2a capital surcharges. The Bank uses G-SIB capital buffers as a “reference point” in its assessments. But in contrast to the Fed it is explicit that these buffers are available for use (i.e. can be run down) in stressed conditions.

In sum, UK regulatory agencies settled on a position that expresses general satisfaction with the current level of risk-weighted capital in major UK banks at levels higher than Basel minima, but which places less emphasis than US regulators on the alternatives of more stringent stress testing and leverage ratios. There has also been some retreat in some important areas from earlier proposals, notably those of the ICB on ringfenced banks. Thus, as table 2 summarizes, US authorities adopted rules

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49 The FPC proposal is also liberal regarding the ability of G-SIBs to “downstream” their G-SIB surcharge to their RFB (Vickers 2016a, 2016b).
51 So for Barclays, the minimum CET1 ratio is currently 6.57% and for HSBC, 5.72%.
that significantly exceeded Basel minima, especially regarding G-SIBs, while the UK has done so more modestly.

**Table 2**: Regulatory minimum requirements for SIBs compared: Basel, US and UK (percentage of risk-weighted assets except where specified)

<table>
<thead>
<tr>
<th>Minimum requirement</th>
<th>Basel</th>
<th>US</th>
<th>UK</th>
</tr>
</thead>
<tbody>
<tr>
<td>CET1 + CCB</td>
<td>7.0%</td>
<td>7.0%</td>
<td>7.0%</td>
</tr>
<tr>
<td>G-SIB capital surcharge</td>
<td>1.0-2.5%</td>
<td>1.0-4.5%</td>
<td>1.0-2.5%</td>
</tr>
<tr>
<td>D-SIB capital surcharge</td>
<td>unspecified</td>
<td>not finalized</td>
<td>1.0-2.5%</td>
</tr>
<tr>
<td>TLAC (banks)</td>
<td>18% &amp; 6.75% of total exposures</td>
<td>18% plus 2.5%+(1.0 to 4.5%)+(0 to 2.5%), &amp; 9.5% of total exposures</td>
<td>18% &amp; 6.75% of total exposures</td>
</tr>
<tr>
<td>Leverage ratio (G-SIBs)</td>
<td>3% of total exposures</td>
<td>6% of total exposures</td>
<td>3.35-3.85% of total exposures</td>
</tr>
<tr>
<td>Stress tests (G-SIBs)</td>
<td>unspecified</td>
<td>CET1: 4.5% (standardized approach), plus G-SIB surcharges from 2018; Tier 1 leverage ratio: 4% (2016)</td>
<td>CET1: 4.5% + 53% of pillar 2a requirement; Tier 1 leverage ratio: 3.13% (2016)</td>
</tr>
</tbody>
</table>

*Source: Regulator websites and documents (see text for details). CCB = countercyclical capital buffer.*

Have British and US G-SIBs responded by manipulating RWAs to achieve higher reported capital? This is unlikely as there is an upward trend in G-SIB Tier 1 unweighted leverage ratios over the same period. Market pressure seems also to have encouraged major banks to exceed minimum requirements well ahead of required regulatory schedules. Figure 7 compares a “tangible” IFRS leverage ratio for US and UK G-SIBs with their counterparts in the BCBS countries. With the exception of Chinese banks, which are far less globalized and arguably not comparable, US and UK G-SIBs have similar and rising leverage ratios that exceed those of their counterparts in other countries, particularly those of most major European G-SIBs. In short, US and UK authorities appear to have been successful in promoting a degree of greater capital stringency than in other major democracies.
Figure 7: Average IFRS leverage ratios, G-SIBs by country, 2012-2016.

These outcomes diverge from the expectation that common crises in a globalized financial sector provides national regulators with an incentive to agree to harmonized regulatory tightening with their peers (Singer 2007). They also diverge from the expectation of those theories that suggest that the extensive regulatory capture of politics by US banks in particular will result in little real increase in regulatory stringency for the largest and most globalized banks. It is also at odds with those versions of structural power theory that claim that no real increase in post-crisis regulatory stringency towards the largest and most globalized banks is possible.

More nuanced theories of structural power do have explanatory value. Culpepper and Reinke (2014) argue that large US banks possess significantly lower structural power vis-à-vis the state because of their much heavier revenue dependence on the larger US economy. This is plausible reason why US regulatory authorities have ultimately had more scope for greater regulatory tightening for their G-SIBs compared to their British counterparts.
Nevertheless, overall these outcomes reflect the sharp increase in the political salience of financial regulation since 2007 and the perceived need of governments of different partisan orientations to respond to public concern (Bell & Hindmoor, 2017, p. 114). As Culpepper (2010) argues, in such circumstances business lobbies can suffer a serious reduction in their capacity to prevent the adoption of more onerous regulation. That this increase in regulatory stringency as applied to the largest global banks has been sharper in two of the world’s most financialized economies suggests that financialization can have political costs for these banks.

This politicization was also sustained in part by a series of scandals that continued to maintain public interest in financial activities and regulation well after the crisis had dissipated. Woolley and Ziegler (2011, 2016) argue that these scandals bolstered the political position of US regulatory hawks by mobilizing a “stability alliance” of activists, policy entrepreneurs and think tanks, and by “mainstreaming” anti-big bank and inequality rhetoric previously championed by the Occupy movement.\(^{52}\) JP Morgan Chase’s London Whale losses and two large financial trading scandals regarding Libor-fixing and foreign exchange kept big finance in the news in the UK and the US and further eroded banks’ reputation for technical competence. That the London Whale scandal occurred in JP Morgan Chase, until then viewed as the best risk manager among major US banks, may have been particularly important (US Senate 2013, 1). The scandals also sustained finance-focused reform groups and the persistence of anti-finance rhetoric in election campaigns in both countries as late as 2017.\(^{53}\)

Certainly, as the politicization of financial regulation began to wane after 2012, a degree of regulatory retreat emerged in both countries. It was apparent first in the UK case, where the early proposals for greater regulatory stringency than international minimum standards were watered down by the government. The

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\(^{52}\) The Occupy movement emerged well after key legislative reforms and rapidly dispersed after 2012.

\(^{53}\) These include independent expert bodies such as European Shadow Financial Regulatory Committee, NGOs such as Finance Watch and the Tax Justice Network, think tanks such as New City Agenda (London), and specialist academic research centres such as the LSE’s Financial Markets Group and Systemic Risk Centre.
Conservative Party’s unexpected victory in the May 2015 elections enabled it to form a single party, more pro-business, government more closely aligned with City interests. The previous coalition with the Liberal Democrats, in which ministers such as Vince Cable supported the ICB approach, had projected a tougher regulatory policy stance.\textsuperscript{54} Publicly, Mr Osborne announced a “new settlement” with the City after the election, saying that “I want Britain to be the best place for European and global bank HQs.”\textsuperscript{55} We should also remember, however, that this is the same government that took the decision to hold a national referendum on UK membership of the EU. This decision, and particularly the referendum result, was diametrically opposed to the dominant preference of the City of London.

The relatively centralized institutional structure of the British political system allowed the government to place pressure on the regulatory agencies to adapt. The new Financial Policy Committee (FPC) is chaired by the Governor of the Bank of England, who is appointed by the Chancellor, as are two other senior members (the chief executives of the FCA and PRA) and five other expert members. The FPC is also subordinated to government policy by statute:

“[T]he FPC is not required to achieve resilience at any cost. Its actions must not, in the provisions of the legislation, have a ‘significant adverse effect on the capacity of the financial sector to contribute to the growth of the UK economy in the medium or long term’. Subject to achieving its main objective, the FPC is required to support the Government’s economic policy, including its objectives for growth and employment.” (FPC 2015, 5).\textsuperscript{56}

At least until recently, the greater institutional decentralization in the US case allowed the US regulators greater discretion to tighten the regulation of G-SIBs. Obama’s re-election victory in 2012 ensured more consistency of executive branch support for a policy of increased regulatory stringency for major banks despite the continued support of Republicans for the dismantling of Dodd-Frank.\textsuperscript{57} The Dodd-Frank Act (section 165) also delegates more extensively than the UK Financial


\textsuperscript{55} See the UK Financial Services Act 2012, section 9C. The FPC’s formal powers of discretion are also narrow, concerning the implementation of the countercyclical capital buffer, the setting of sectoral capital requirements, measures relating to residential property lending, and the leverage ratio.

\textsuperscript{56} “Top Republican outlines plans to rip up Dodd-Frank,” \textit{FT.com}, June 7, 2016.
Services Act (2012) in assigning responsibility to the regulators for the setting of prudential standards for SIBs. The Board of Governors of the Fed themselves, or acting on a recommendation of the Financial Stability Oversight Council (FSOC), determines which prudential rules are appropriate. Dodd-Frank does not limit the Fed’s ability to impose rules on SIFIs by requiring as explicitly as in the UK case that these rules to take account of the government’s economic policy and their wider effect on the economy.58

The clearest example of this greater Fed policy autonomy has been on the leverage ratio, on which French and German negotiators, pressured by their own large relatively highly leveraged banks, strongly resisted a more stringent international agreement over 2013-14.59 US regulators reacted by choosing to impose a leverage ratio double the international minimum for American G-SIBs, despite the fears of some insiders that the banks would regain influence after the Republican electoral surge in 2012 (Bair 2012, 357).

It is important to recall in this regard that both the Fed in Dan Tarullo and the Bank of England in Andy Haldane had prominent regulatory hawks in charge of financial regulation from 2009. Both looked worryingly radical to G-SIBs. Haldane, the Bank of England's Executive Director of Financial Stability from 2009 until June 2014, was among the most outspoken regulatory officials regarding the need to reign in systemic risk (Haldane 2012, 2013).60 Individual policy entrepreneurs and the ideas they deploy certainly matter, but since 2009 the US institutional framework allowed them greater scope to undertake more sustained regulatory tightening for large banks. Whether this will persist after the Republican victory in November 2016 is now uncertain.

4 Conclusion

This paper argues that much of the literature has underplayed the role of voters as an important factor in post-crisis regulatory politics. Almost all major crisis-

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58 Section 120 of Dodd-Frank requires FSOC to take into account the impact of its recommendations on long term growth, and the Act specifies the need for some specific cost-benefit studies.
60 In fact, senior figures in British regulatory agencies in the early years after the GFC (including Haldane, Mervyn King, and Adair Turner) made the UK look like a hotbed of regulatory radicalism.
hit countries saw incumbent governments lose office after the crisis,\textsuperscript{61} and voters generally elected governments that favoured more stringent financial regulation. The US and UK cases were not exceptional in this regard and both new governments, despite their underlying ideological differences, accepted the need for more stringent regulation of their largest, global banks. Both allowed hawks within their regulatory agencies to propose significantly more stringent regulation than they were able to achieve with their counterparts in the Basel Committee. This has had real effects on major bank capitalization.

Many scholars accept that the crisis forced politicians to accept, at least for a time, that big finance needed more stringent regulation. But in focusing largely on the effect of the crisis of 2007-9 on the sudden “ politicization” of financial practices and regulation, and the role of post-crisis scandals in sustaining it, many miss a longer run trend. The political salience of finance has been rising steadily since the 1970s and reached new heights in 2008 and after.

I have argued that this is connected to the wider process of financialization, which has generated increasingly frequent and virulent financial crises \textit{and} prominent financial scandals. Middle class wealth accumulation since the 1970s in developed democracies has sharply increased the stake of many households in financial markets and in policies that affect this wealth. Financialization has been especially associated with a rapid growth of housing finance and a growing obsession of households and the media with house prices. It has also helped to drive rising economic inequality and perceptions of distributive unfairness, as expensive financial sector bailouts and high financial sector compensation are contrasted with post-crisis fiscal austerity and household wealth losses. This has forced governments in the most financialized and advanced economies to respond with much more stringent regulation of their major banks than was conceivable before 2008.

This analysis also suggests that the rising embeddedness of finance in middle class lives (cf. Seabrooke 2007, 2008) places considerable limits on the re-regulation of globalized finance. The far greater dependence of middle class housing and defined contribution pension asset values on this complex financial system limits

\textsuperscript{61} Germany (in part) and Sweden were exceptions.
political support for any move back to extensive financial repression. Much political economy literature suggests that resistance to a return to the financial repression of the Bretton Wood era is due to the political power of the financial sector itself. Our analysis suggests, however, that financialization has deeper, even democratic roots, and that too many households would lose for mainstream political parties to adopt more radically restrictive policies. This also helps to explain why financial regulation remains a matter of deep contention in contemporary politics in the major countries.
References:


Floors: the design of a framework based on standardized approaches’.”

March 27.


