



**ESRB**

European Systemic Risk Board  
European System of Financial Supervision

# **Non-Bank Finance and Financial Intermediation: A story telling in six pieces from a macroprudential policy practitioner**

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## Outline: Thinking about 'macropru beyond banking' in a highly imperfect world

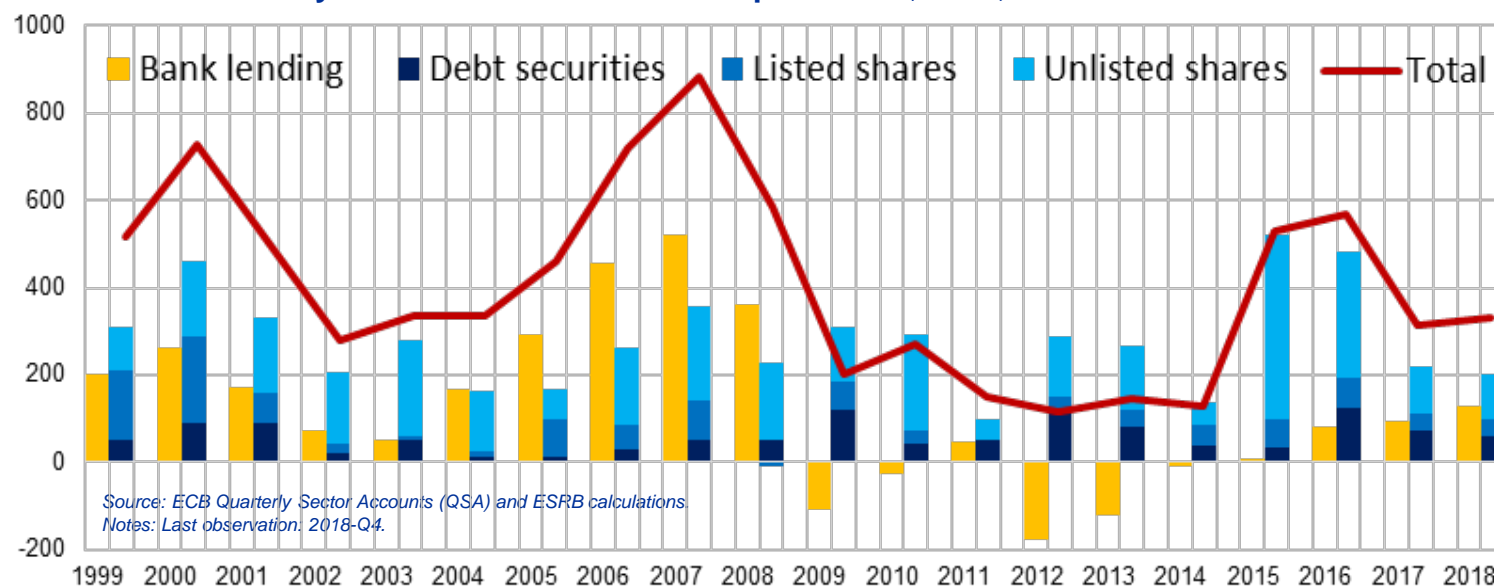
- A case study: the role of market finance to support non financial corporations in the euro area during the crisis
- The need to address implications: the French measure to limit exposures to highly indebted firms in 2018
- What else to do when you do not have instruments at your disposal? A macro use of micro prudential stress simulations
- The role of soft law in a step by step approach: extending the availability of useful contractual tools across the financial sector



# Story telling 1 - Fortunately, during the crisis market finance replaced bank lending to NFCs ...

- In the euro area, after the crisis the issuance of financial markets instrument has replaced banking lending to NFCs in net terms. This is a welcome development, through which corporations have been often able to withstand the weakness of an impaired banking sector.

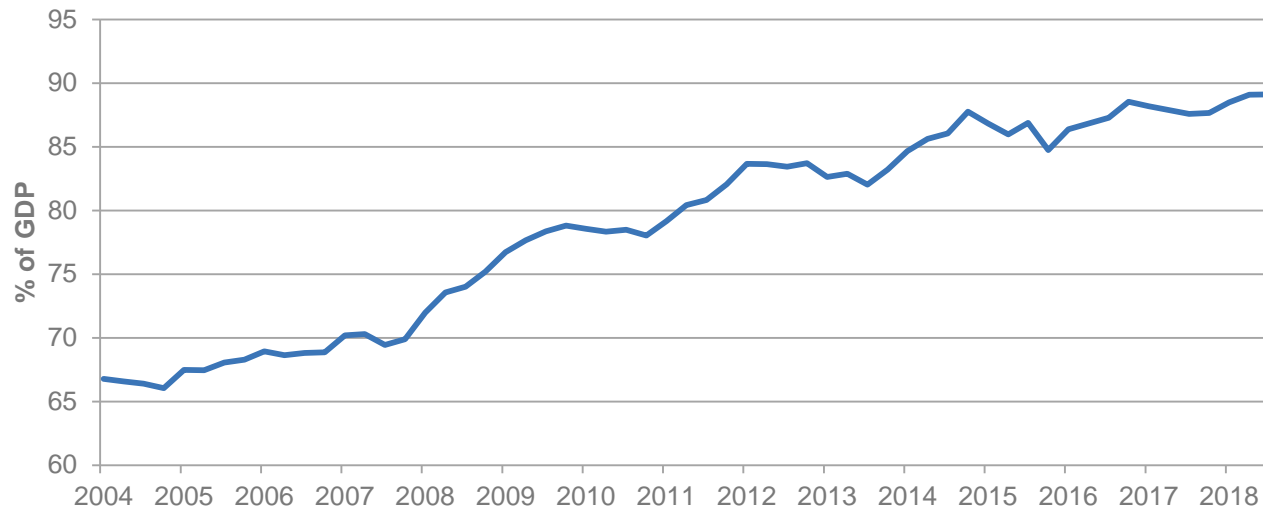
**Net finance raised by euro area non-financial corporations (EUR bn)**



# Story telling 2 – ... but also what is highly welcome may have its drawbacks ...

- However, the unabated availability of funding may have helped fostering a steep increase of the indebtedness of NFCs (for instance in France).

**NFC indebtedness in France (source: ECB and ESRB)**



## Story telling 3 – ... and tools may not exist to address them

...

- Unfortunately, macropru instruments to limit indebtedness of NFCs do not exist.
- This has forced French authorities to take action to protect the economy from the excessive indebtedness of the largest NFCs, imposing tighter concentration limits of large exposures (again, indirectly via banks!).
- The concentration limit has been tightened to 5% of the eligible capital under certain circumstances. The measure has been authorized by the European Commission, after having been received a positive opinion of ESRB and EBA.
- Looking ahead, an alternative in the future might be to apply borrower-based measures to NFCs, broadening it however to all lending institutions (the Dutch already do it for households, why not to follow them for all borrowers?)



## Story telling 4 – ... while we should not always ‘touch’ banks to protect the economy from finance ...

- The US experience shows that microprudential stress test may be used as a macropru instrument. For instance, the Federal Reserve is using bank stress testing as a tool to keep excessive procyclicality of lending to the economy in check (they do not have a Countercyclical Capital Buffer in use, like in several EU countries).
- Europe has an extensive experience in stress testing beyond banking.
- The European Supervisory Authorities (ESAs – EBA for banking, EIOPA for insurance and pension funds, ESMA for financial markets) are requested by legislation to use stress tests, in cooperation with the ESRB, in order to assess the resilience of financial institutions or market participants to adverse market developments.
- As part of this cooperation, the ESRB designs scenarios of adverse economic and financial market developments as input also for non-bank finance.
  - For the insurance sector, since 2014
  - For pension funds since 2015
  - For CCPs since 2016
  - For money market funds since 2019



# Story telling 5 – ... and might make more use of stress testing of the financial system beyond banking.

- The adverse scenarios are based on the ESRB risk assessment and the ESAs' expertise to identify the most important risk factors to be shocked.
- From risks to shocks: an example

## Main risks:

- 1 – Repricing of risk premia in global financial markets
- 2 – Persistent weaknesses in balance sheets of EU banks, insurers and pension schemes
- 3 – Debt sustainability challenges in EU sovereign, corporate and household sectors
- 4 – Vulnerabilities in the EU shadow banking sector and contagion to the financial system



## Risk factors shocked:

- Global equity prices
- Yield curve in advanced economies
- Interbank money market spread
- EU sovereign credit spread
- EU corporate credit spread
- ...



# Story telling 6 – Finally, we should learn to make a macro use of existing microprudential tools

- Some microprudential tools can also have a macroprudential impact (like in the case of liquidity management instruments for the fund industry). What is crucial is to eliminate limitations to their use (see ESRB Recommendation on leverage and liquidity in investment funds (2018))

Availability of the liquidity management instruments in Union Member States

	AT	BE	BG	CY	CZ	DE	DK	EE	ES	FI	FR	GR	HR	HU	IE	IS	IT	LI	LT	LU	LV	MT	NL	NO	PT	RO	SE	SI	SK	UK	
Gates	no	no	no	yes	no	no	no	yes	yes	no	yes	no	no	no	yes	no	yes	yes	no	yes	no	yes	yes	yes	yes	yes	yes	no	no	yes	yes
Side pockets	yes	no	no	yes	no	no	no	yes	yes	no	yes	no	no	no	yes	no	yes	yes	no	yes	no	yes	yes	yes	no	no	no	yes	no	no	
Anti-dilution levy	no	no	no	yes	no	no	no	yes	no	no	yes	no	no	no	yes	no	yes	yes	no	yes	no	no	yes	no	yes	yes	no	no	no	yes	
Redemption fees	yes	no	no	yes	no	yes	no	yes	no	yes	yes	no	no	no	yes	no	yes	yes	no	yes	no	no	yes	no	no	no	no	no	no	yes	
Redemption-in-kind	yes	no	no	yes	no	yes	no	yes	yes	yes	yes	no	yes	no	yes	no	yes	yes	no	yes	no	yes	yes	no	yes	no	no	yes	no	yes	
Suspension of redemptions	yes	yes	yes	yes	yes	yes	yes	yes	yes	yes	yes	yes	yes	yes	yes	yes	yes	yes	yes	yes	yes	yes	yes	yes	yes	yes	yes	yes	yes	yes	yes
Swing pricing	yes	no	no	yes	no	no	no	yes	no	yes	yes	no	no	no	yes	no	no	yes	no	yes	no	no	yes	yes	no	no	no	no	no	yes	
Short-term borrowings	yes	no	yes	yes	yes	yes	no	yes	yes	yes	yes	yes	no	no	yes	yes	yes	yes	no	yes	no	yes	yes	no	yes	yes	no	yes	yes	yes	
Mandatory liquidity buffers	yes	no	no	no	no	no	no	no	yes	no	no	no	no	no	no	no	no	no	no	no	no	no	yes	no	no	no	no	no	yes	no	
Side letters	yes	no	no	no	no	no	no	yes	yes	no	no	no	no	no	yes	no	no	yes	no	yes	no	yes	yes	no	no	no	no	no	no	yes	
Other tools/measures	no	no	no	no	no	yes	no	no	yes	no	yes	no	no	no	no	no	yes	no	no	yes	no	no	no	no	no	no	yes	no	no	yes	

Source: ESMA, 2018

