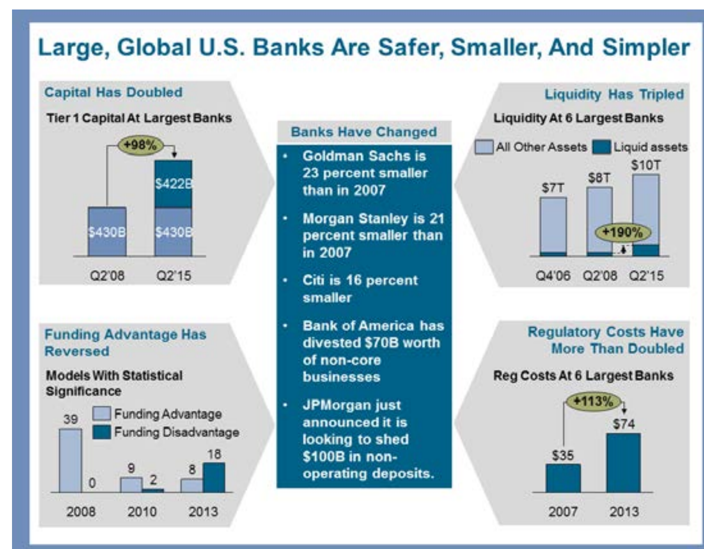
The Financial Sector Has Changed – What Now?

Financial regulation is designed to protect taxpayers and the broader economy. Recent reports, data, and market moves have shown that America's largest banks – which serve customers of all sizes, including America's largest companies – have become smaller and simpler. Capital has doubled and liquidity has tripled among the largest firms. Furthermore, among all banks, new capital surcharges and long-term debt requirements are forcing leaders to reconsider scope and scale.

These are not peripheral changes: Goldman Sachs is 23 percent smaller than in 2007, Morgan Stanley is 21 percent smaller, and Citi is 16 percent smaller. Meanwhile, Bank of America has divested $70 billion worth of non-core businesses and JPMorgan just announced it is looking to shed $100 billion in non-operating deposits. This reality stands in stark contrast to claims from critics suggesting nothing has changed or that its business as usual among large banks.

At the same time, the goal of financial regulation should not be to engineer de facto break-ups, nor hinder U.S. banks' international competitiveness. Going forward, policymakers should ensure reforms do not hamper large banks' ability to serve their customers, supporting sustainable economic growth.



America's Largest Banks Are Getting Smaller…

- **Goldman Sachs "Shrank 6 Percent Since 2010 While The Pay Per Employee Fell 13 Percent Since 2010 And 43 Percent Since 2007."** "'We have significantly adjusted both compensation levels and fixed expenses,' the chief executive of Goldman, Lloyd C. Blankfein, told the industry conference in Florida. 'We have transformed the financial profile of the firm.'" (Nathaniel Popper And Peter Eavis, New Rules Spur a Humbling Overhaul of Wall St. Banks, *New York Times*, 2/19/15)
- **Citigroup "Has Shed Nearly $700 Billion In Noncore Assets And Divested From More Than 60 Noncore Business Lines.**" [Citi] recently said it would sell its consumer businesses in Spain and Greece." (Victoria McGrane And Julie Steinberg, "Wall Street Adapts to New Regulatory Regime," *WSJ*, 7/21/14)

- **The Bipartisan Policy Center Finds That "The Largest Five Bank Holding Companies Have Seen Their Market Share Decline Slightly Since 2010."** "As a result, (of regulations) nearly all the U.S. G-SIBs are effectively prohibited from acquiring additional U.S. or foreign corporations, meaning that any future expansion will have to be generated by market growth. This provision, among other factors, may explain why the largest five bank holding companies have seen their market share decline slightly since 2010." (The Big Bank Theory: Breaking Down The Arguments, *BPC*, 10/14)

…They Are Getting Simpler

- **Bank Of America Has Divested $70 Billion Worth Of Non-Core Businesses And Eliminated 36 Percent Of Its Legal Entities Since 2009.** "[BofA] has shed more than $70 billion worth of businesses and other assets since 2010, including those requiring the bank hold a lot of capital against them. It has also eliminated 746 legal entities—a 36% reduction since the end of 2009. Among the assets jettisoned: private-equity investments, some credit-card businesses and big chunks of its mortgage business." (Victoria McGrane And Julie Steinberg, "Wall Street Adapts to New Regulatory Regime," *WSJ*, 7/21/14)
- **The IMF Finds That Global Banks Are Transitioning By Exiting Capital Market Activities, Rebalancing Business Models Away From Capital-Intensive Activities, And Retrenching From International Markets.** "Global banks have already begun their transition to new business models. First, many global banks are shrinking or exiting from capital market activities, especially in fixed income, currencies, and commodities. Only a few large investment banks are expected to maintain a strong presence in these activities. Second, most global banks are also rebalancing their business models away from capital-intensive activities to more fee-based activities, such as mergers and acquisitions and securities-underwriting activities, as well as asset management and private wealth management. Third, a large number of global banks are retrenching selectively from international markets and refocusing on commercial banking activities in home markets and regional markets where they enjoy a leading presence." ("Improving The Balance Between Financial and Economic Risk-Taking," *IMF*, 10/14)

…And Capital Is At The Top Of Everyone's Mind.

- **Credit Suisse CEO Brady Dougan Says Considerations Of Capital Were Now A Part Of His Everyday Management Of The Bank.** "Brady W. Dougan, the chief executive of Credit Suisse, one of the world's biggest Wall Street banks, said considerations of capital were now a part of his everyday management of the bank. "It's become much more a game of driving the highest returns from the businesses that are most suited to the new environment," he said." (Nathaniel Popper And Peter Eavis, New Rules Spur a Humbling Overhaul of Wall St. Banks, *New York Times*, 2/19/15)
- **JPMorgan CEO Jamie Dimon Says They Are Looking To Cut Costs Due To Size Down And JPMorgan Is Now Looking To Shed $100 Billion In Non-Operating Deposits By Year End.** Mr. Dimon conceded that the bank faces higher compliance and other costs as a result of its size. "It's our job to get [those costs] down," he said…In perhaps the biggest shift, J.P. Morgan announced that it aims to reduce certain deposits by as much as $100 billion by year-end and is preparing to charge large institutional customers for some deposits, thanks to new rules that make

holding money for the clients too costly. (Emily Glazer, "J.P. Morgan Aims To Get Leaner," *Wall Street Journal*, 2/2/4/15)

Yet, Policymakers Should Keep In Mind Banks of All Sizes Are Necessary to Meet Customer's Needs…

- **Yale Professor Charles Calomiris Argues Some Banks Need To Be Large, "Because Their Clients Are Large And Operate Globally."** "They need to be large to operate on a global scale—and they need to do so because their clients are large and operate globally. Small, local banks simply could not provide global corporations the same physical capabilities for trade finance, foreign exchange contracting, and global capital access that large global financial institutions can." (Charles Calomiris,"In the World of Banks, Bigger Can Be Better," *Wall Street Journal*, 10/19/09)
- **Big Banks Are Valuable In A Global Economy Says Former Treasury Official Phillip Swagel.** "In a global economy, there is a need for financial institutions with scale and global capacity. Large banks offer their customers products, services and infrastructure that smaller banks cannot match, from multicity branch networks to global coverage that lowers costs. Philadelphia-based chemical company FMC Corp. (FMC), for example, relies on large banks to fund its $1.5 billion revolving credit line and to offer worldwide support for its financing needs." (Phillip Swagel, "Don't Make Banks Too Small To Succeed," *Bloomberg*, 9/5/12)

…And The Goal Of Regulation Should Be To Improve Safety And Soundness, Not Engineer De Facto Break-Ups.

- **Citing Slow Loan Growth Among Large Banks, OFR Argues "It Is Possible The New Capital And Liquidity Standards Could Reduce Banks' Ability To Lend."** "With these new measures, regulators have sought to strengthen banks' ability to weather stress. However, analysis of the economic and financial stability impacts of the regulations is warranted. For example, it is possible the new capital and liquidity standards could reduce banks' ability to lend. Large banks' loan growth has been slow relative to the growth in gross domestic product in recent years." (Office Of Financial Research, "2014 Annual Report," *OFR,* 12/1/14)
- **Mester And Hughes Find That Breaking Up Large Banks Significantly Raises Cost And "Could Seriously Affect Their Competitiveness In Global Financial Markets."** "If these 17 banks were broken into smaller banks with $100 billion in assets but with no change in their output mix, costs would increase from $410 billion to $1.48 trillion. This scale effect means the average cost per dollar of assets would increase from 4.5 percent to 16.3 percent, an increase of 11.8 percentage points. This increase in average cost per dollar of assets suggests that restricting the size of financial institutions in a manner consistent with this exercise could seriously affect their competitiveness in global financial markets if institutions in other countries were not similarly constrained in size." (Joseph Hughes And Loretta Mester. "Who Said Large Banks Don't Experience Scale Economies? Evidence From A Risk-Return-Driven Cost Function," *Wharton Finance*, 4/13)