After Adjusting for Economic Growth, as Pledged, GSIB Surcharges Should be 50 Basis Points Lower

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This post updates the growth adjustment to the systemic indicator scores of the eight U.S. global systemically important banks (GSIBs) that BPI calculated in May 2018 using the most recent estimates of trend economic growth reported by the Congressional Budget Office (CBO). On average, the corrected GSIB surcharges would be about 50 basis points lower if the Federal Reserve were to make the growth adjustment, as it committed to doing when it released the Final Rule on the GSIB Surcharge.

Four of the five bank categories in the systemic indicator score—complexity, interconnectedness, cross-jurisdictional activity, and size—are calculated as the sum of balance sheet and off-balance sheet items for GSIBs at the end of each year, divided by the average over the 2012 and 2013 levels of the aggregate sum across global GSIBs of those same items. These four measures will trend up over time with both inflation and with economic growth. The fifth bank category, short-term wholesale funding (STWF), is calculated as the ratio of the GSIB’s weighted STWF divided by its average risk-weighted assets over the previous four quarters. Because the STWF measure is divided by a balance sheet variable that also grows over time, it does trend up with economic growth and inflation.

We use the CBO’s estimate of potential nominal GDP to adjust the systemic indicator score for economic growth. By using potential nominal GDP rather than actual nominal GDP, we avoid the procyclicality that would otherwise be caused by adjusting for higher growth in good times and lower (or even negative) growth in bad times. Potential nominal GDP was 23 percent higher than the average of its level in 2012 and 2013. We use this estimate to deflate the four bank categories that are growing over time. We find that the aggregate score across all eight U.S. GSIBs would have been 13 percent lower, resulting in a decrease of 47 basis points in the average GSIB surcharge as of the third quarter of 2019.

In aggregate, the eight U.S. GSIBs hold about $6.7 trillion in risk-weighted assets. The lack of adjustment for economic growth requires the largest banks to hold an unintended $33 (CET1) capital. According to a review of the academic literature on the impact of higher billion more in common equity tier 1 capital requirements on lending, the eight U.S. GSIBs have had to reduce lending to businesses and households between $3 billion and $14 billion over the past 6 years as a result of the 1/2 percentage point increase in capital requirements.

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