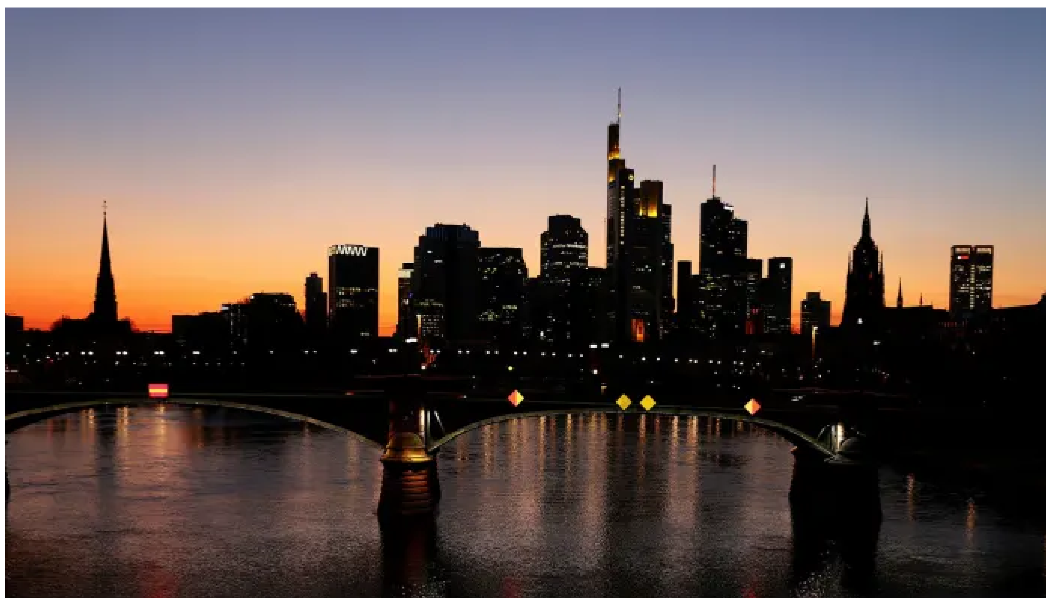
Coronavirus

Regulators free up $500bn capital for lenders to fight virus storm

Moves by central banks around the world designed to add $5tn in extra credit for the real economy



Policymakers hope banks will play a more constructive role than in the 2008 financial crisis, when they were widely criticised © Kai Pfaffenbach/Reuters

Martin Arnold in Frankfurt 19 MINUTES AGO

Financial regulators have freed up about $500bn of capital for lenders around the world to help them absorb the impact of the Covid-19 pandemic, according to calculations by the Financial Times.

By relaxing capital requirements in the past few weeks, central bankers have aimed to keep credit flowing to businesses and households and mitigate the economic turmoil caused by mass quarantines put in place to slow the spread of the virus.

Data released last week showed the global economy is on track for its sharpest slowdown since the Great Depression, while millions of people around the world have lost their jobs.

The freed-up capital provides lenders with the capacity to make an extra $5tn of loans globally.

The FT has counted $492bn in capital relief by central banks and regulators from Washington to Hong Kong, which has mostly come from cutting extra capital buffers that were designed to strengthen lenders' balance sheets after the 2008 crisis.

Some regulators have ordered banks to conserve capital by freezing dividends and reining in bonuses, while others have postponed the introduction of tougher capitalisation rules or provided temporary exemptions in the calculation of capital requirements.

The moves highlight how policymakers hope that banks will play a more constructive role than in the 2008 financial crisis, when they were widely blamed for being the source of many problems.

In a way the banking sector has suddenly been transformed from a nominally capitalist enterprise into effectively a state entity. It's temporary, but it is significant

Nicolas Véron, Bruegel think-tank and Peterson Institute

This time they are seen as a vital "transmission mechanism" for the trillions of dollars in aid that governments have unleashed to save the global economy from collapse.

"The buffers were built up in order to be released, so this is a textbook way to use them," said Nicolas Véron, a senior fellow at the Bruegel think-tank and the Peterson Institute for International Economics.

He added: "In a way the banking sector has suddenly been transformed from a nominally capitalist enterprise into effectively a state entity. It's temporary, but it is significant."

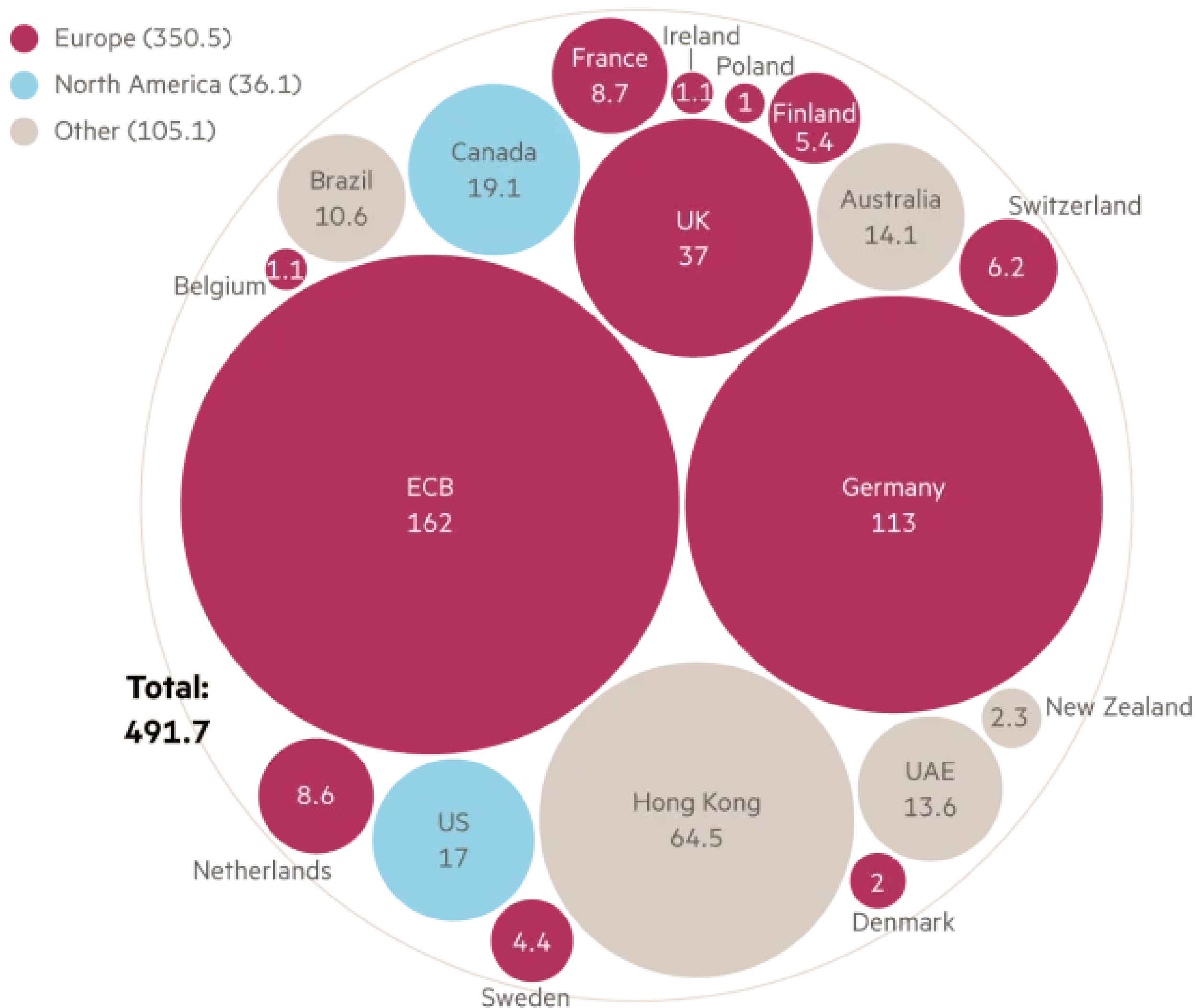
While central bankers are confident that the banking system is in much better shape than the 2008 crisis, they are worried that the economic downturn could be amplified if there were to be a pullback from lending to companies and individuals to conserve capital.

Bank capital is made up of shareholders' equity and retained earnings and is used to absorb losses while staying solvent, making it a crucial measure of a bank's financial strength.

By allowing banks to operate with lower levels of capital, regulators are boosting their firepower to absorb higher demand for loans as well as rising customer defaults and a deterioration in credit quality in their loan books.

“The key dynamic for banks in this coronavirus crisis is duration,” said Joseph Dickerson, banking analyst at Jefferies. “It is unlikely that any banks will need to raise more capital from investors if it is resolved by the summer. But if it drags on to the autumn that is going to be a bigger problem.”

The world’s biggest economies have granted nearly half a trillion dollars in capital relief to banks because of the Covid-19 crisis



Graphic: Alan Smith, Martin Arnold
Source: FT analysis of IMF and national central bank data, other reports, as at April 4 2020
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Apart from freeing up capital, central banks have supported lenders by injecting vast amounts of ultra-cheap loans into the banking system and lowering the amount of reserves or liquid assets they must hold.

Anat Admati, professor of finance at Stanford University, said banks should "conserve cash every way you can", including by "stopping dividends and share buybacks". She added: "I would not frame this step as a change in requirement but more as

forbearance . . . conceptually it means you are not in compliance but I am not enforcing at the moment, but it means extra vigilance on the part of regulators."

The biggest chunk of capital relief has come from the European Central Bank, which last month freed up €120bn at the 117 eurozone banks it supervises by allowing them to eat into various buffers while preserving a further €30bn by telling them to freeze dividend payments.

Other eurozone countries, such as Germany, France and the Netherlands, have gone beyond the measures announced by the ECB, by rolling back the extra “rainy day” requirements — known as countercyclical capital buffers — that they imposed at a national level and giving their country’s lenders extra flexibility on other buffers.

Several other national regulators have unveiled measures to free up tens of billions of dollars in capital for the banks they supervise, including the US Federal Reserve, the Bank of England, the Hong Kong Monetary Authority, the Central Bank of the UAE, the Australian Prudential Regulation Authority and the Bank of Canada.

Recent regulatory moves have released the equivalent of more than a quarter of the €1.78tn extra capital that was added to the biggest banks’ balance sheets between mid-2011 and the end of 2018 to comply with tougher rules introduced after the 2008 financial crisis.

The world’s 106 biggest international banks increased their common equity tier one capital — the mostly closely watched measure for regulators — from €1.95tn in mid-2011 to €3.72tn in December 2018, according to the Bank for International Settlements.

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