

The Future of Investment Banks

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Is there a future?



PHOTO: JOHN R. COUGHLIN

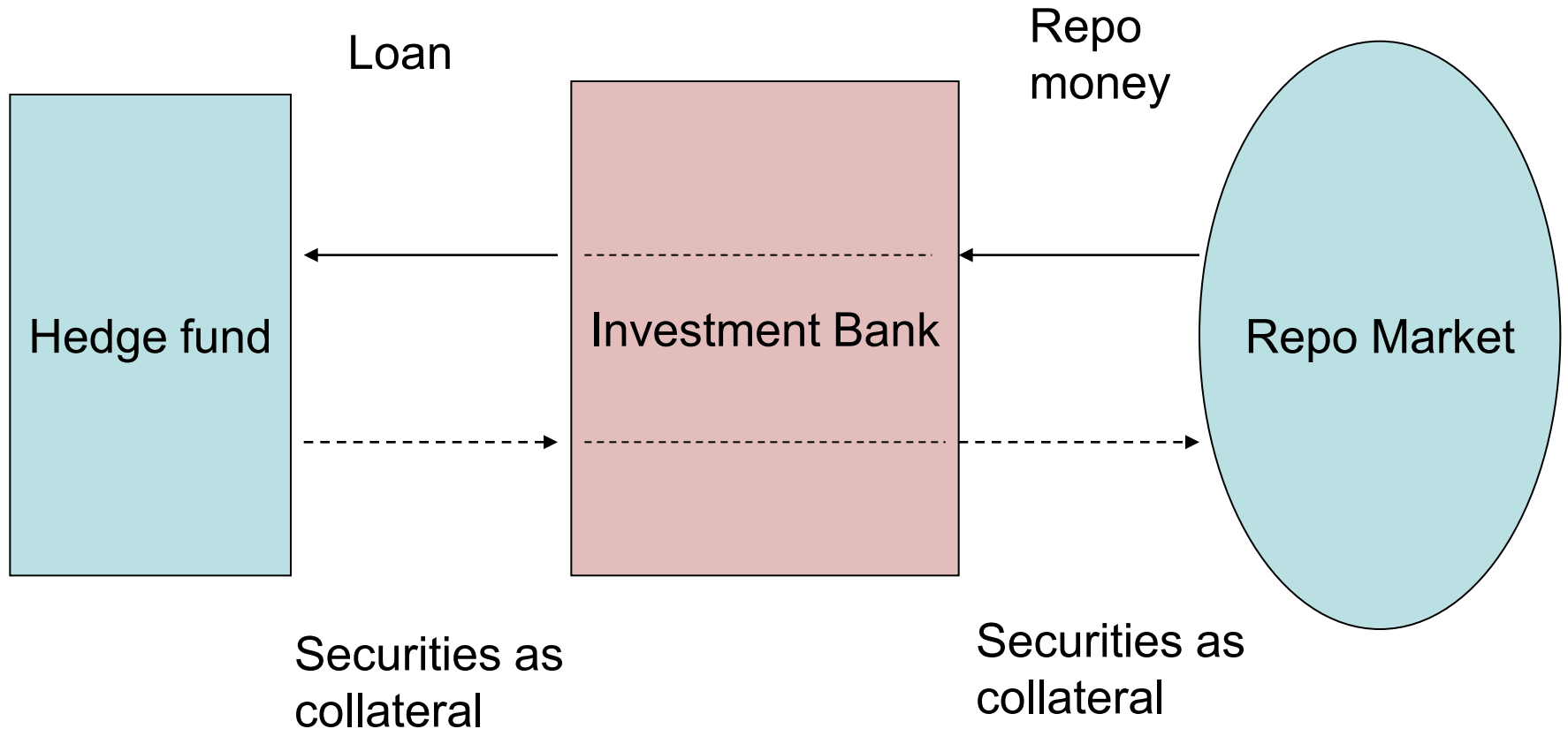
It depends on the regulations



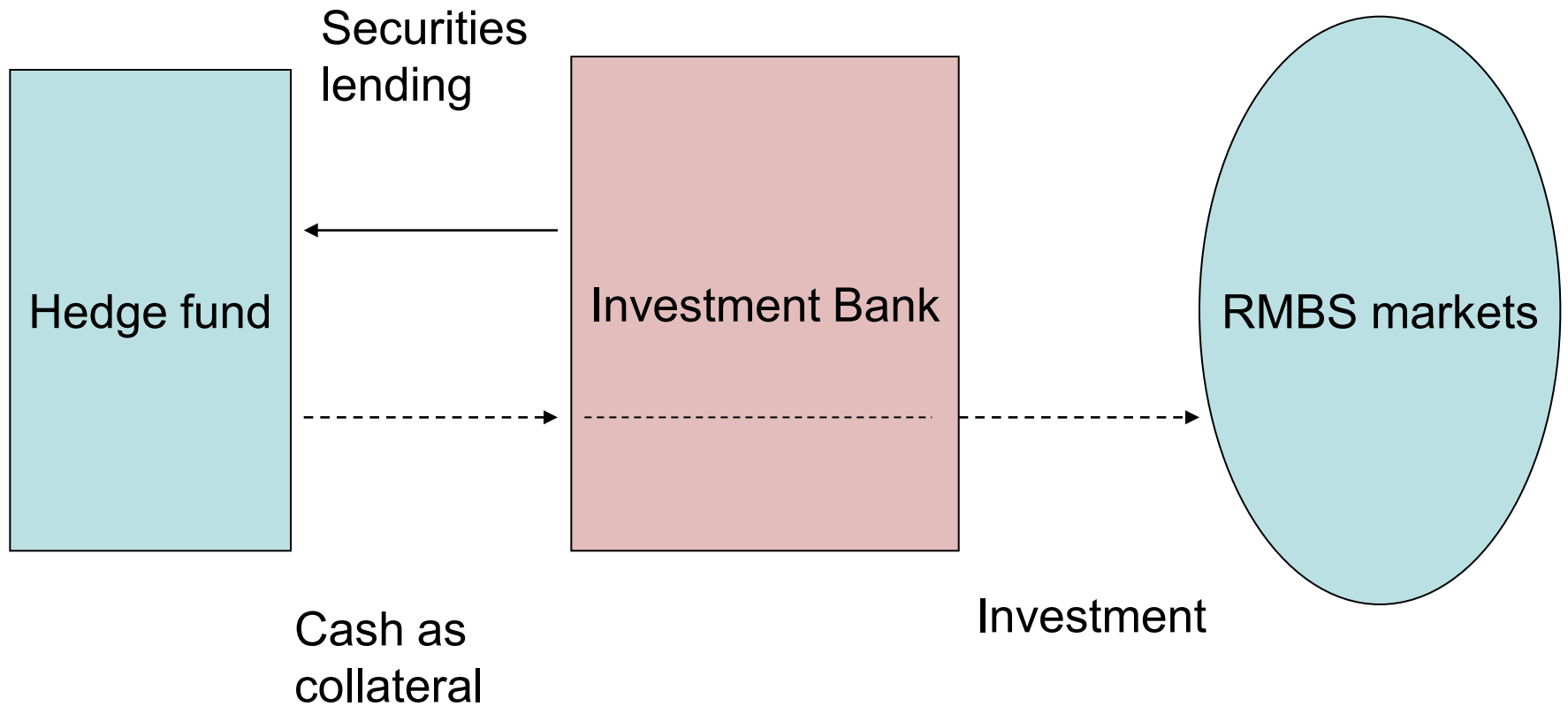
Yes, IBs did cause systemic risk

- They are among shadow banks.
 - Maturity mismatch.
 - Dependency on market liquidity and funding liquidity.
- But, should shadow banks be regulated as or like commercial banks?
- Market-driven systemic risk is different from bank-driven systemic risk.

Collateral run, not bank run (1)



Collateral run, not bank run (2)



Bank like regulations for shadow banks are not the answer

- Reform tri-party repo market.
 - In Japan, major participants including IBs have accounts in BOJ.
 - Payments and settlements through the central bank account = Real time monitoring of liquidity by BOJ.
 - Use only government bonds.
- Limit re-hypothecations.
- Segregate client assets.

CCP for collateral finance

- CCP can limit counter-party risks.
- CCP can monitor and limit exposures of participants.
- CCP can manage collateral safely.

New infrastructure, not new regulations

- Hershtadt crisis in 1974 led to the creation of Basel committee.
- Heshtadt risk is now minimized by CLS (Continuous Linked Settlement) bank.
- Did those Basel requirements brought any comparable benefits for global financial markets?

Leverage through CP?

Net capital rule, rating reform,
MMF reform will be enough

