The financial crisis 10 years on: what's been done to make the system safer?

Ten years ago an unsafe financial system caused financial crisis and economic disaster. Global production plummeted, the number of people who lost their jobs soared, and governments around the world used taxpayers' money to save banks from failure in order to prevent a global depression. Since the crisis, the Bank of England has been building a safer system bolstered by two important institutional innovations. First, it has been given responsibility for the supervision of individual banks and building societies. Second is the creation of an authority in the Bank with new powers – the Financial Policy Committee – tasked by Parliament to monitor risks in the financial system that could cause problems for the wider economy.

How are banks safer?

Globally, banks can withstand much larger losses without failing:

- With capital requirements on large banks ten times higher than before the crisis, banks have raised more than $1.5 trillion of capital.
- Banks are now disciplined by a leverage ratio. This protects the system from risks and uncertainties that are hard to measure through risk weights and models.
- Large global banks are taking fewer risks trading in financial markets. Trading assets have halved.
- Banks are less dependent on each other - interbank lending has fallen by two thirds since the crisis.

In the UK specifically:

- Banks have raised over £130bn of true loss absorbing capital. As a result, the average ratio of capital to risk weighted assets has increased from 4.5% to 14.3%.
- The Bank of England's first line of defence is intrusive supervision of banks and building societies.
- Our second line of defence is to stress test lenders to make sure they have the strength to deal with very severe recessions without cutting back on lending. Last year's test showed that even after suffering losses of £44bn – losses that would have wiped them out ten years ago – major banks would have a capital base more than twice as strong as in the run up to the crisis.
- Banks are less dependent on short term wholesale market funding which has fallen from 25% of total funding in 2006 to just 10% now.

How is the rest of the financial system safer?

- The Financial Stability Board has been created to monitor and address risks from institutions and activities across countries and has helped develop international collaboration on financial regulation.
- Toxic forms of shadow banking at the heart of the crisis – with their large funding mismatches, high leverage and opaque, off-balance sheet arrangements – no longer represent a financial stability risk and have shrunk by 40% since 2007. Other risks have been addressed, turning shadow banking into resilient forms of market-based finance.
- Businesses have diversified their sources of funding, with non-banks continuing to grow in importance. Bond financing has accounted for almost all corporate credit growth since the crisis in the US, UK and euro area. In the UK, as banks reduced their business lending by £90bn, non-banks stepped in and increased lending by £130bn.
- Complexity in derivatives markets has been reduced. Over 60% of over-the-counter interest rate derivatives are now centrally cleared, three times more than before the crisis. Collateral for over-the-counter derivatives has more than doubled to over $1.7trn. These reforms have significantly reduced dependencies between banks. At least 90% of over-the-counter derivatives trades are now reported to authorities in major jurisdictions.
- In the UK and internationally, laws have been developed to make senior management in banks more accountable. Remuneration rules better align incentives and rewards to discourage excessive risk-taking and misconduct.

How are your savings safer?

- In the United Kingdom, the Financial Services Compensation Scheme (FSCS) protects savings and deposits up to £85,000 compared with £31,700 prior to the crisis. Since 2001 it has helped more than 4.5 million people and paid out more than £26 billion. The financial services industry pays for FSCS through a compulsory levy.
- UK banks now hold over £700bn of high quality liquid assets ensuring they could withstand 30 days of funding difficulties (which includes large withdrawals of deposits).
- UK banks will separate (or "ring-fence") their consumer banking services from their investment and international banking activities in January 2019. Ring-fencing will protect UK consumer banking deposits from shocks to the wider financial system and make banks easier to resolve.

How have taxpayers been protected?

Resolution regimes have been established for banks that mean if they fail, they could be dealt with quickly and fairly.

- International standards have been introduced to end reliance on public funds. All the home jurisdictions of the global systemically important banks now have legal frameworks for handling bank failure.

In the UK specifically,

- Prior to the crisis there were no resolution arrangements for UK banks. Now, the UK has a comprehensive and effective bank resolution regime. This gives the Bank of England a wide toolkit to ensure that if a bank fails, the shareholders and creditors of the failed bank bear its losses, and that the taxpayer is not called upon to bear the costs.
- Banks in the UK are also being required to change the way they are funded and operate. These changes will make them easier to resolve in an orderly way so that households and businesses can continue to access the banking services they need.
- The actions taken to address the problem of banks being "too big to fail" mean that investors are incentivised to pay closer attention to the risks banks take.