Ring-a-ring-a-fences [1]

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The Parliamentary Commission on Banking has reported this morning and, like most of the talk leading up to and since the Vickers Report, is pre-occupied by ring fencing. Vickers, as you will recall, dealt with the demands for separating retail and investment banking by proposing that those banking groups involved in both should have separate subsidiaries for those sectors with no links between them.

Government discussions since then have been seen by some as, under pressure from the bankers, watering down the Vickers proposals. The Parliamentary Commission, au contraire, claims that Vickers did not go far enough and the fences should be ?electrified?, i.e. any infringement would lead immediately to full separation. Sir John Vickers himself, in an email to the Today programme, quickly responded by saying that full separation would be an own goal.

What is weird about all this is that the financial crisis had little if anything to do with the lack of such separation. Retail banks, like Northern Rock, and building societies created a bubble of huge unrepayable debts and, quite separately, banks packaged up those ?assets? to conceal their true nature and then played pass the parcel with the packages. Lehman Brothers was purely an investment bank. The entities that created the crash were already separated and separating the other groups would do nothing to prevent a future crash.

What is even weirder is the failure to recognise that banking today is an international, if not fully global, market. Financial solutions have to be found internationally. The Basel group are doing their best to achieve that and we now have three ?Accords?. They focus, quite sensibly, on ensuring banks are adequately capitalised for the businesses they run. One can, and I have, criticised their proposals as an over-reaction which will penalise small businesses, but the point here is that the rest of world?s top regulators are not worrying at all about ring-fences.

Another part of the international dimension which the Parliamentary Commission fails to recognise is the EU involvement. Uncertainty about that undoubtedly contributed to the Northern Rock crash as Professor Tim Congden and others, including Sir Mervyn King, have pointed out. The UK is in course of handing financial regulation over to Brussels but what is for us to do and what for Brussels is unclear. The only thing that is clear is that the EU?s interventions will damage the competitiveness of UK banks and increase the costs for taxpayers.

So, not unusually, British chattering classes are dancing around playing ring-a-ring-a-ring-fence when the rest of the world gets on with regulating the real financial market. It is truly astonishing that this Commission should choose to focus its entire attention on the area that matters least. The consequence of adopting their suggestions, as Vickers himself seems to be pointing out, can only be that we will hobble our own financial sector at great cost to the economy and the British taxpayer.

Links:
[1] http://www.adamsmith.org/blog/money-banking/ring-a-ring-a-fences
[2] http://www.adamsmith.org/taxonomy/term/5859
[3] http://disqus.com/?ref_noscript
[4] http://disqus.com