Four views of the US financial system

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Summary
Four views of the US financial system

• **Business line view:** Financial system businesses generate > $1 TN in annual revenue across five major business lines

• **Structural asset-liability view:** Financial gearing of real economy has increased, while securitization further multiplied claims within the financial system

• **Comparative view:** US financial system is big, unbundled, less bank-centric, and complex

• **Evolutionary pressure view:** Financial system innovations and practices have been driven by the wish to reduce the amount of credit evaluation that must be done
US financial services – by business line

Revenues by financial services business, total = $1.2 TN
$BN, 2010

- Insurance: $430
  - Property & Casualty
  - Life

- Retail: $355
  - SME Lending
  - Consumer Lending
  - Credit Cards
  - Mortgage
  - Deposits

- Corp. Bank: $105
- Inv. Bank: $100
- Asset Mgt: $175

Source: Oliver Wyman analysis
Today, total financial claims are ~10 times GDP

Financial assets held, by economic sector
2011

- **Households**: Own: $50 TN
- **Rest of world**: Own: $19 TN
- **Pensions**: Own: $10 TN
- **Inv. Funds**: Own: $10 TN
- **Money mkt**: Own: $3 TN
- **Fed**: Own: $3 TN
- **Banks**: Own: $15 TN
- **GSEs**: Own: $6 TN
- **Insurers**: Own: $7 TN
- **Rest of FS**: Own: $11 TN
- **Firms**:Own: $19 TN
- **Gov’t**: Own: $4 TN

Financial system (43% of financial assets)

Scale: 2011 GDP
$15 TN

Source: Flow of Funds Accounts of the Unites States
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Thirty years ago, financial claims were less than 5 times GDP

Financial assets held, by economic sector
1981

- **Households**
  - Own: $7.0 TN

- **Rest of world**
  - Own: $0.5 TN

- **Fed**
  - Own: $0.2 TN

- **Financial system (34% of financial assets)**

  - **Pensions**
    - Own: $0.8 TN

  - **Inv. Funds**
    - Own: $0.1 TN

  - **Banks**
    - Own: $2.4 TN

  - **Insurers**
    - Own: $0.7 TN

  - **GSEs**
    - Own: $0.2 TN

  - **Rest of FS**
    - Own: $0.4 TN

- **Gov’t**
  - Own: $0.6 TN

- **Firms**
  - Own: $1.8 TN

Source: Flow of Funds Accounts of the Unites States
Nonfinancial sectors have taken on more debt per unit of economic activity…

Credit owed by US nonfinancial sectors, as a percentage of GDP
1981-2011

Source: Flow of Funds Accounts of the Unites States
…while daisy-chaining of credit via securitization increased the “credit multiplier” applied to claims on the real economy

Financial sector credit assets, as a percentage of credit owed by nonfinancial sectors
1981-2011

Source: Flow of Funds Accounts of the United States
How the US financial system is different

- More credit intermediation via markets and nonbanks, less dominant role for banking system
- Lots of small banks
- GSEs
  - Subsidized mortgage asset funding
  - Hold mortgage credit risk, and significant amount of prepayment (convexity) interest rate risk
- Many different regulatory bodies, but increasingly same rules for major players
  - BHCs (including absorbed/converted dealers and finance companies), nonbank SIFIs, foreign IHCs: similar prudential requirements
  - Orderly Liquidation Authority, the universal (in)solvent
- Big domestic economy
US – world’s most credible bank guarantor

Assets as a percentage of home country GDP for world’s largest banks
2011

Source: Bankers Almanac, Economic Intelligence Unit
Evolution of US financial system has been driven by the desire to reduce (or avoid) the burden of credit evaluation

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