There is nothing "simple" about the European Commission's securitisation proposal

Eight years after what was arguably the biggest financial crisis since the 1930s, the European Commission is on the verge of giving up some of the regulatory gains made since. We are referring to that part of the Commission's Capital Markets Union (CMU) that purports to set up a European market for so-called "simple", "transparent" and "standardised" (STS) securitisations. While years of recession and sluggish recovery do of course warrant an urgent search for policies that promise jobs and growth, we are concerned that a new market for STS securitisations is not going to do the trick and may instead run counter to some of the most important lessons of the crisis. For that reason we call upon the honourable Members of European Parliament who are currently preparing their response, to carefully consider the future ramifications of these plans and to launch a more thorough future impact analysis than is now provided.

Our concerns are fourfold.

First, regarding its objectives, it is not clear that reviving securitisation would help SMEs as the European Commission maintains. Even before the crisis the market of securitised SME-loans in Europe was marginal due the opaqueness of these loans. What instead can be expected is to receive a boost from the European Commission's proposals are securitised mortgage loans. Sizeable before the crisis, especially in The Netherlands, Spain and the UK, it allowed European banks to tap into international credit markets to allocate credit towards the buying and selling of already existing assets, resulting in real estate bubbles and economic dislocations, as research of the Bank of International Settlements has shown. The current plan portents a post-crisis replay of that pre-crisis scenario. More "financialised" growth, instead of real growth.

We were surprised to see that the Commission does not even concede the possibility of new real estate bubbles. Instead, readers are given data that intend to show that European securitisations performed better during the crisis than US ones and hence should be treated differently in terms of capital requirements. The proposal talks about a "significant reduction" of capital charges, for both buyers and sellers of STS securitisations. That will immediately improve the bottom line of banks but does nothing for growth and jobs.

Second, it is unclear how reviving securitisation would help to diversify risk and make the financial system more stable, as the Commission maintains. The buyers of these securitisations are already heavily interconnected with banks through repo markets and will be even more so through the securitisation channel. The promotion of non-bank credit intermediation, which is the official goal of Capital Markets Union, in fact boils down to a regulatory subsidy for market-based banking and will increase interconnectedness, procyclicality and leverage. This proposal is hence not a break with the pre-crisis world of finance but a re-enactment of it, despite the language it employs.

Which brings us to our third concern. The legal description of the kind of securitisations that would be eligible to receive the STS stamp suggests that these would be anything but "simple", "transparent" or "standardised". Tranching is fully allowed, as are credit enhancements such as credit default swaps, while interest rate swaps are even obliged. All three suggest not simplicity but the same kind of complexity that caught investors as well as
regulators off guard before the crisis. No wonder that industry insiders have expressed their bemusement over the level of complexity allowed by a proposal whose headline aim is simplicity, transparency and standardisation.

Our fourth concern deals with one of the main lessons of the crisis, namely that in order to overcome endemic conflicts of interest, originators should be forced to have more skin in the game. The current risk retention paragraph is both too lax and too arbitrage prone. The Commission wants banks to keep five percent of every batch on their balance sheets. This is not enough to meaningfully address conflicts of interest. For that reason, sophisticated buyers demand at least 20 percent skin in the game. The Commission has failed to follow this best practice using the industry argument that it would make transactions too costly, since it would give banks insufficient regulatory capital relief. Given the size of the crisis, we would have expected the Commission to align itself with citizens and their interest in financial stability, not with banks and their preference for higher profits. Similarly, under the current proposal banks can pick the tranches they want to fulfil their risk retention requirements. Again, this smacks of letting profitability concerns prevail over stability considerations.

The European Parliament faces a momentous decision on a highly technical and hence hard to politicise issue that, we fear, is going to be a first step in a longer journey of financial deregulation in which banks will use the leverage they have over policy makers eager for jobs and growth to again get their way. The details of the proposal contain insufficient guarantees to the contrary. Hence our urgent call on the Members of European Parliament to initiate a thorough, independent impact assessment that addresses the sort of concerns we have raised here.

What is at stake is nothing less than the future of Europe. Will it be a future of financial stability, albeit at the cost of some bank profitability? Or will it instead be a future of highly profitable banks again, at the cost of sizeable risks to the taxpayer?

Members of European Parliament, the choice is yours.

List of signatories:

Ewald Engelen, Professor of Financial Geography, University of Amsterdam
Stephany Griffith-Jones, Professor of Economics, Financial Markets Director, Initiative for Policy Dialogue, Columbia University
Avinash Persaud, Nonresident Senior Fellow, Peterson Institute for International Economics
Daniela Gabor, Associate Professor of Economics, UWE Bristol
Nicholas Dorn, Associate Research Fellow, Institute of Advanced Legal Studies (IALS) School of Advanced Study, University of London
Vincenzo Bavoso, Lecturer in Commercial Law, University of Manchester
Laurence Scialom, Professor of Economics, University Paris West
Matthias Thiemann, Professor for the Sociology of Money, Banking and Finance, Goethe Universitaet Frankfurt am Main
Gunther Capelle-Blancard, Professor of Economics, Université Paris 1, Panthéon-Sorbonne
Philip Arestis, Professor of Economics, University of Cambridge
Anna Glasmacher, University of Amsterdam
Jakob Vestergaard, Senior Researcher, DIIS Copenhagen
Manuel Aalbers, Associate Professor of Social and Economic Geography, KU Leuven, Belgium
Malcolm Sawyer, Emeritus Professor of Economics, Leeds University
Esther Jeffers, Associate professor, Université Paris 8, France
Dominique Plihon, Emeritus Professor, University of Paris North
Andrew Baker, Reader in Political Economy, Queen's University Belfast
Gary Dymski, Professor of Applied Economics, Leeds University Business School
Mark Sanders, Associate Professor of International Macroeconomics, Utrecht University
Irene van Staveren, Professor of Economics, Erasmus University
Denis Dupré, Professor of Finance and Ethics, University Grenoble-Alps
Paul Lagneau-Ymonet, Associate Professor, Paris-Dauphine, PSL Research University, IRISSO.
Antoine Henrot, Professor of Mathematics (including financial mathematics), Université de Lorraine, France
Bernard Paranque, Professor of Economics, Kedge Business School, Marseille, France
Ludovic Halbert, CNRS Researcher at Université Paris-Est
Vlad Mykhnenko, Lecturer in Human Geography, University of Birmingham
Nicholas Shaxson, Author, Treasure Islands
Richard Murphy, Professor of Practice in International Political Economy, City University, UK
Martin Sokol, Assistant Professor, Trinity College Dublin
Anne-Laure Delatte, CNRS research fellow
Wojtek Kalinowski, Co-Director, Veblen Institute for Economic Reforms
Annina Kaltenbrunner, Lecturer in the Economics of Globalisation & The International Economy, Leeds University Business School
Stefan Gärtnner, Head of Research Unit Spatial Capital, Institute for Work and Technology
Prem Sikka, Professor of Accounting, University of Essex Business School
Ismail Ertürk, Senior Lecturer in Banking, The University of Manchester
Thomas Rixen, Professor of Public Policy, University of Bamberg
Dany Lang, Associate Professor, CEPN, University of Paris 13
Angela Wigger, Associate Professor Global Political Economy, Radboud University, The Netherlands
David Bassens, Assistant Professor, Vrije Universiteit Brussel
Peter Dietsch, Associate Professor, Université de Montréal
Clement Fontan, Post-doctoral researcher at the Center of Ethics, University of Montreal
Adam Leaver, Professor, Alliance Manchester Business School, University of Manchester
Charles Dannreuther, School of Politics and International Studies, University of Leeds
Andrea Lagna, Lecturer, School of Business and Economics, Loughborough University
Timo Walter, Lecturer, Staatswissenschaftliche Fakultät, Universität Erfurt
Aurore Lalucq, Co-director, Veblen Institute
Paul Langley, Reader, Durham University
Jon Cloke, Research Associate, Loughborough University
Rodrigo Fernandez, Postdoc researcher at KU Leuven and associate researcher at SOMO
Philip G. Cerny, Professor Emeritus of Politics and Global Affairs, University of Manchester (UK) and Rutgers University (USA)
David Bassens, Assistant Professor of Economic Geography, Cosmopolis (Vrije Universiteit Brussel)
Nina Haerter, PhD candidate, Vrije Universiteit Brussel
Reijer Hendrikse, postdoctoral researcher, Vrije Universiteit Brussels
Joscha Wullweber, University of Kassel
Jo Michell, Senior Lecturer, University of the West of England
Christine Oughton, Professor of Management Economics, SOAS, University of London
Victoria Chick, Emeritus Professor of Economics, UCL
Michiel van Meeteren, Postdoctoral Researcher, Vrije Universiteit Brussel
Daniel Detzer, Research Associate, Institute for International Political Economy, Berlin School of Economics and Law, Germany
Trevor Evans, Emeritus professor of economics, Berlin School of Economics and Law
Mary Robertson, Lecturer, University of Greenwich
Jérôme Creel, Associate professor of economics, ESCP Europe
Elisa van Waeyenbergen, Lecturer, SOAS University of London
Jesus Ferreiro, Associate Professor in Applied Economics, University of the Basque Country UPV/EHU, Spain

Roland Pérez, Emeritus Professor (Economics and Management Science) - Université Montpellier (France)

Laura Horn, Associate Professor, Department of Social Sciences and Business, Roskilde University, Denmark

Thomas Lagoarde-Segot, KEDGE Business School and LEST, Aix-Marseille Université, France

Maëlys Waiengnier, Doctoral Researcher, Vrije Universiteit Brussel & Université Libre de Bruxelles

Nuno Teles, Researcher, Centre for Social Studies, University of Coimbra, Portugal

Kobil Ruziev, Senior Lecturer, UWE Bristol

Janusz J. Tomidajewicz, Emeritus Professor, Poznan University of Economics

Karen Maas, Program Director CSR Executive Program, Erasmus Universiteit Rotterdam

Eric Clark, Professor of Human Geography, Lund University

Sérgio Lagoa, Assistant Professor of Economics, Instituto Universitário de Lisboa (ISCTE)

Włodzimierz Dymarski, Researcher in Economic Policy and Financialisation, Poznan University of Economics and Business, Poland

Yannis Dafermos, Senior Lecturer, UWE Bristol

Ana Cordeiro Santos, Senior Researcher, Centre for Social Studies, University of Coimbra

José Caldas, Senior Researcher, Centre for Social Studies, University of Coimbra

José Reis, Full Professor, Faculty of Economics and Centre for Social Studies, University of Coimbra

João Rodrigues, Assistant Professor, Faculty of Economics and Centre for Social Studies, University of Coimbra

Lina Coelho, Assistant Professor, Faculty of Economics and Centre for Social Studies, University of Coimbra

Hans-Jurgen Bieling, Professor for Political Economy, Eberhard Karls Universität Tübingen

Ana Costa, Assistant Professor, ISCTE-IUL and Dinâmia’CET-IUL, University Institute of Lisbon.