A bird eye (re)view of key readings

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This section of the journal indicates a few and briefly commented references that a non-expert reader may want to cover to obtain a first informed and broad view of the theme discussed in the current issue. These references are meant to possibly provide opposing views of the debates. More detailed and specific references are available in each article published in the current issue.

On the cost of additional capital requirements

The Bank for International Settlements (BIS, 2011) estimates that the macroeconomic costs of additional capital requirement is expected to be low and the macroeconomic benefit (in terms of strengthening the resilience of the macroeconomic system) much higher. Consistent with these results, the general manager of BIS argues in favour of increasing capital requirements illustrating that the observed increase of requirements after the crisis had not the strong feared negative effects and is in favour of the use of TLAC (Caruana, 2014). On a similar line, Admati et al. (2013) argue that the cost of additional capital is less than what is normally claimed, because more capital increases banks' resilience thus reducing the risk so that the cost of capital must decline with the bank's capital. Kashyap et al. (2010), and Miles et al. (2012) report empirical estimates of the costs of higher capital requirements, also showing that the socially optimal capital of banks is higher than what is currently contemplated in Basel III. Along the same lines, also Roger and Vitek (2012) have estimated a small macroeconomic cost of a synchronized global increase in bank capital adequacy requirements under Basel III.

Contrary to these views, the Institute of International Finance, the leading global association of financial institutions, stated that Basel III rules may reduce GDP by 3.2% by 2015 (IIF, 2011). Aiyar et al. (2015) also argue that the banks' cost of rising capital requirements is high and may thus lead to strong adverse effects on banks' lending. Hence, these authors strongly advocates the use of contingent convertibles (CoCos) as opposed to simply imposing higher capital requirements. Estimates of the first effects of additional capital requirements imposed post-crisis are provided by Cohen and Scatigna (2014). A preliminary study by Bloomberg (2015) argues that the cost of meeting the additional requirements of TLAC regulation will be very high.

Finally, a rich and balanced discussion of theoretical and empirical evidence on the effectiveness and costs of capital requirements is in the contributions of the current issue, in particular, Beck (2015), Clerc (2015) and Rochet (2015).

On contingent convertible securities, bail-in securities and structural reforms

The functioning and role of Contingent Convertible Securities (CoCos) is explained in details by Calomiris and Herring (2013). For earlier references, see also Flannery (2005), who proposed ten years ago the introduction of an instrument that would convert to common equity when a bank's market capital ratio falls below a pre-stated value), and Raviv (2004). French (2010), in his chapter of the Squam Lake Report, also proposed the introduction of an hybrid security converting debt into equity on the basis of simultaneous triggers. Krahnen and Moretti (2014) presents a comprehensive review on the treatment and functioning of CoCos and of other bail-in procedures. For a relatively recent account of actual CoCos issuance see Bank of Norway (2014). Criticisms on CoCos have been put forward by Admati et al. (2013), who state that these instruments are not convincing because of complications on triggers and conversion rules, and of the implicit tax subsidy of debt financing as compared with equity. Strong criticism on bail-in securities is purposed in

Persaud (2014). A deep and detailed analysis of loss absorbing capacity of international banking groups is offered by Gracie (2014).

For a detailed discussion on CoCos and total loss-absorbing capacity (TLAC), see also Salleo (2015) in this issue. A clear and streamlined illustration of the FSB 2014 proposal on TLAC (see the "Regulatory framework section" in this issue) is in BBVA research (2014).

A different approach with respect to increasing the loss-absorbing capacity of banks with higher capital requirements or asking them to issue bail-in securities advocates the introduction of structural reforms on the structure of banking activities. Vickers (2013) and the Vickers' report (2011), for example, suggest to ring-fence retail activities from other banking activities. Instead Crawford (2014) and Guynn and Kenadjian (2015) are strongly against the structural solutions to the TBTF problem, and are in favour of the introduction of bail-in securities and TLAC in particular.

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