IN THE MOOD FOR LIQUIDITY: NON-BANKS IN THE SHADOW OF BANKS & FINTECHS

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The financialisation of economic relations is the result of the current financial repression which has served to distort the behaviour of both the banks and other agents concerned as money creators and credit intermediaries. In this inflationary scenario, money holders will continue to need assets to protect the value of their savings, but banks will not need to compete either by providing loans or through the capture of deposits.

The simple reason for this is that central banks provide commercial banks with all the money they supposedly require, and almost for free ─remember the ECB's LTROs series? But all for what? In a nutshell ─and contrary to the official narrative─, all to purchase some form of securities, like public debt or the so-called green businesses' issues. Taking deposits and granting loans keep banks in touch with the real economy, but this is in exchange of severe requirements for regulatory capital. All of which entail uncomfortable outcomes: runs on deposits, borrower insolvency, and regulator whip. The atrophy of the banks' critical mass for draining and pumping money into the productive economy comes along with the hypertrophy of the regulatory apparatus of central banks. In order to bypass all this, the alternative circuit to banking is well-known, the debt-liquidity chain sustained by the commercial flow of payments and, why not, financial markets. Once the link between loans and deposits fades, money circulates through different channels of credit.

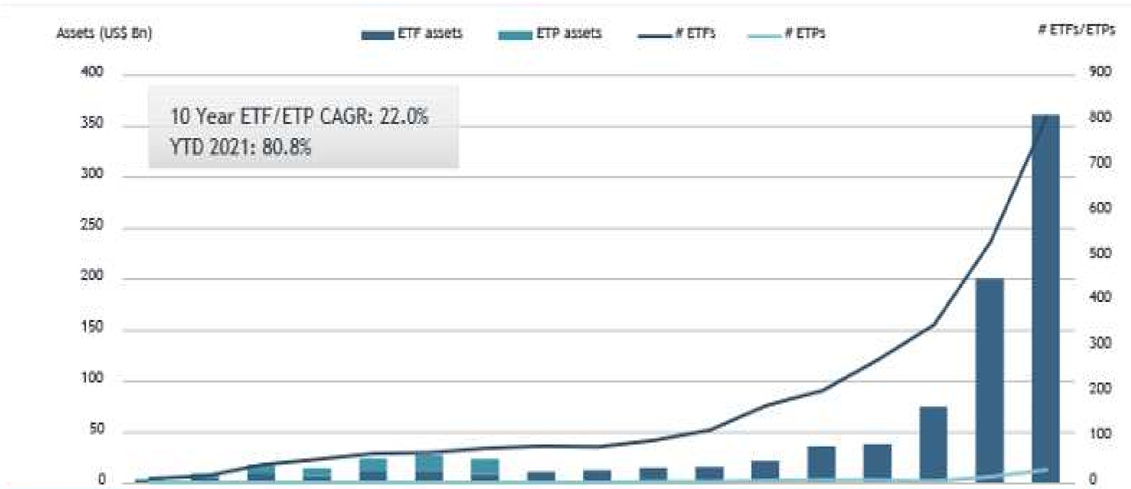
The amount of resources allocated to investment funds has skyrocketed since the aftermath of the Global Financial Crisis, above all ETFs. For the period 2009-2019, the total amount managed by ETFs has surged from $1,353bn to $6,181bn[1]. Such a gigantic leap could be attributed to collective madness, but I'd much prefer to look for another explanation by paying attention to the behaviour of real people in the real world. Amazingly, the label of opacity and blame that hangs over 'creative' financial products has not impeded the unprecedented growth of the shadow banking sector. In short, financial arrangers simply cocktail companies' liabilities, transform them into fund assets and place the shares on the stock market via flotation. The savoir-faire for credit intermediation has shifted the focus from commercial banks to investment banks and other financial service providers. But it is not without side-effects, the main one of which might be the financial exclusion of small and medium-size companies and ordinary savers, forced to suffer inflationary tax and the reluctance of commercial banks to remunerate deposits and provide loans.

Liquidity is seen by central bankers as their monopoly, and no single alternative source must be tolerated. Complex instruments, like OTC derivatives, which are crucial for the liquidity of the financial markets, are demonized, while heavy informational, red-tape duties must be borne by the parties in those transactions. The response to the exodus from financial repression is bureaucracy. In this context, the upsurge in fintechs and neo-banks seems, to me, like an attempt to erode the conventional banks' market share in non-banking activities, and consequently there is no relevant additional value for credit risk management. If you pay peanuts, you'll get monkeys.

ETFs provide liquidity to both companies and their investors, but they transfer a great deal of risk onto financial markets whose abrupt reactions in times of need could contribute to serious

[1] According to STATISTA; see: es.statista.com/estadisticas/634622/activos-bajo-gestion-de-los-etf-mundial/. ETFGI, a private, independent consultancy and financial sector data provider points out the intensification of the trend by the end of 2021, with a yearly increase of the 80.8% in the global amount of assets: https://etfgi.com/news/press-releases/2021/11/etfgi-reports-record-year-date-net-inflows-esg-etfs-and-etps-listed.

disruption in the whole banking and monetary system[2]. Liquidity is inevitably about short-term gains and losses, not about money printing, and the adequate discernment of credit risk is the specific role of commercial banks in a market economy; that of the central banks is last resort lending at a penalty rate, and against good collateral, but to commercial banks, not to States.



Year	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Oct-21
# ETFs	6	12	37	49	62	64	74	79	77	91	114	168	201	270	348	529	806
# ETFs/ETPs	6	12	37	49	62	64	74	79	77	93	116	172	206	275	351	541	834
ETF assets	2	5	9	6	11	11	8	10	12	14	15	21	35	37	74	200	360
ETF/ETP assets	3	9	18	14	24	27	23	10	12	14	15	21	35	38	74	200	361

My main concern goes to the restrictions on the means for liquidity derived from the last decade's regulatory trends. My contention is about the severe distortions caused to all stakeholders and economic agents by the Humpty-Dumpty mantra of (global) financial stability, which entails a number of overlapping controls directed to channel every single stream of liquidity to the banking sector, devised as a mere elongation of central banks and regulatory authorities. To spur the debate, I'd like to pose a couple of questions: (1) does it make sense the financial repression exercise over OTCs through the duties of notice to the regulators? (2) does the unprecedented proliferation of ETFs since the GFC show the flight by investors from conventional financial vehicles which are seen unreliable and too close at politicians' hands?

[2] See, K. TODOROV, "Passive funds affect prices: Evidence from the most ETF dominated asset classes", *BIS Working Papers*, No 952, July 2021, 67 pp.