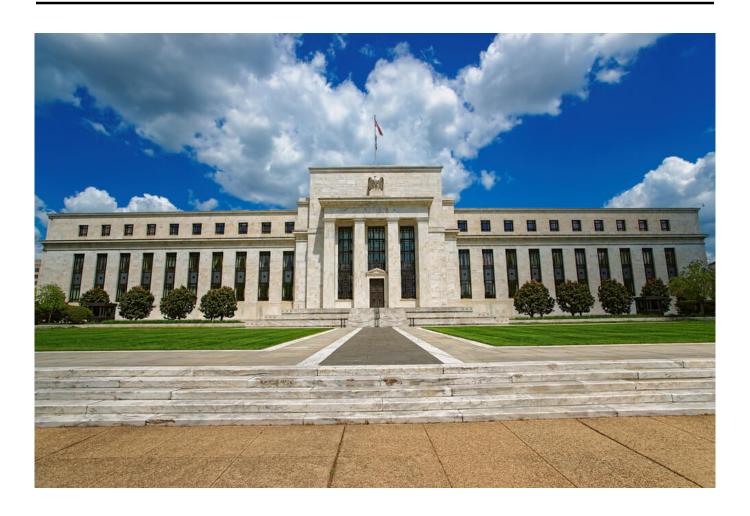


Analysis of today Assessment of tomorrow



By: Howard Davies

Behind the façade of unity the Basel Consensus is cracking



Ask a room of central bankers how many want a less stable financial system, and you will see few (if any) hands go up.

Ask how many support intrusive, costly supervision, endless box-ticking, and process-heavy enforcement, and the result will be the same.

This tension lies at the heart of the Basel Committee's recent statement – backed by all members, including those from the United States – calling for the Basel III rules to be implemented "in full and consistently."

In reality, the façade of unity conceals substantive divisions among regulators.

Some argue that the current framework promises the "stability of the graveyard" – a system that is stable only because nothing is allowed to move. Others warn that any relaxation risks a repeat of the 2007-09 financial crisis.

But attitudes are shifting, and not just in the US. Former European Central Bank President Mario Draghi's 2024 report on EU competitiveness, for example, suggested that bank regulation may now be constraining development.

In the United Kingdom, regulators have been instructed to factor competitiveness and growth into their decision-making.

Prime Minister Keir Starmer has even asked them to submit proposals for stimulating growth, which is like asking a lawyer to ghostwrite a love letter.

But what does that shift mean in practice? Will policymakers in the US, UK, and European Union ultimately settle on an approach they can all claim is Basel-compatible?

Internal arguments

Over the past few weeks, we have been given a rare glimpse into the internal arguments that central banks usually keep behind closed doors.

After Michelle Bowman, the US Federal Reserve's new Vice Chair for banking supervision, outlined her regulatory approach, her predecessor – who still sits on the Board of Governors – issued a swift dissent.

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Bowman was notably succinct. Her approach, she explained, "is not about narrowing our focus, it is about sharpening it."

By sharpening, she meant reducing supervisory staff by 30%, increasing the Board's reliance on state-level oversight, sharply scaling back enforcement, and carving many community banks out of the Basel framework altogether.

Michael Barr, Bowman's predecessor, was predictably critical, pointing out that past periods of relative calm have often led to weakened supervision, with "dire consequences."

He also argued that the Fed's supervisoryratings framework is being softened in ways that "diminish its strength and credibility," producing a kind of regulatory "grade inflation" that makes banks look healthier than they are. The consequences, he warned, will become clear once the next crisis hits.

Barr, alas, is on his way out, while Bowman's view is ascendant.

The Fed's evolving posture

Another signal of the Fed's evolving posture came from Trump-appointed Governor

Stephen Miran – known as the architect of the aborted Mar-a-Lago Accord, which aimed to boost American exports by weakening the dollar – who also supports reducing banks' capital requirements.

Miran's push for lower capital requirements has more to do with monetary policy than with regulatory concerns.

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He argues that the size of the Fed's balance sheet is inflated by regulations that drive credit creation into the shadows, and that market forces – not regulatory arbitrage – should determine how and where credit is created.

He was openly critical of the supplementary leverage ratio, which is already slated for elimination.

Strikingly, Miran also questioned the global systemically important bank (G-SIB) capital surcharge, imposed by the Financial Stability Board and long accepted by the Fed.

Abandoning the surcharge would represent a major regulatory shift, given that it is the FSB's primary policy tool.

Undermining Basel would come at a high cost

For now, it is impossible to say whether such a shift would lead to the emergence of a new US regime that is ultimately incompatible with Basel III.

Global supervisors are adept at framing departures from international standards as minor variations when expediency demands it.



If Basel III unravels, regulatory equivalence may collapse with it - Klaas Knot

But that flexibility has usually been reserved for short-term deviations – not for endorsing a deliberate swing in the opposite direction.

Before stepping down as FSB chair, Klaas Knot – widely viewed as a successor to European Central Bank President Christine Lagarde – issued a stark warning to US banks campaigning against Basel III reforms, the so-called "Basel Endgame."

If Basel III unravels, he said, regulatory equivalence may collapse with it. Such an outcome, Knot observed, would end up hurting US banks, which "will no longer be able to profit from open and mutually accessible markets."

The message could not have been clearer: undermining Basel would come at a high cost.

Whether that warning is heeded remains to be seen. With the battle lines now drawn, the coming policy confrontation will show whether US policymakers still value prudence over politics.

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