Together, the initiatives to make banks both less likely to fail and safe to fail will have a significant impact on banks, especially the G-SIBs that are at the heart of the global financial system.

Reform of regulation (see Chapter 2), supervision (see Chapter 3) and resolution (see Chapter 4) will change the environment in which banks must operate. Banks will have to comply with the rules if they are to survive. But to thrive, banks will also have to make the right choices – about the targets they aim to meet; about the business models they employ; about the markets in which they stay, enter or leave; and about developing the capabilities they will need in order to win. In short, banks have to set themselves up for success.

Regulation offers banks the opportunity to do so. In order to comply with regulatory and supervisory standards banks will have to spend vast amounts of money and time over the coming years to revamp their technology, their data and their systems and procedures. Banks that view these requirements simply as added cost will wind up with just that, added cost. Banks that recognise that much of the new regulation represents sound business practice can potentially make this spending do double duty. They can use the spending to improve their business model as well as comply with regulation. Those banks which do so will
have significantly better prospects for success in the new environment.

*Regulation and supervision establish the framework in which banks must operate*

In broad terms, regulation and supervision establish (i) the boundaries within which a bank must choose its strategy, and (ii) the guidelines that banks must follow in implementing that strategy.

Regulation will frame the activities in which banks may engage, the structure banks may have, the capital that banks must keep, the liquidity that banks must maintain, the governance that banks must employ, the conduct banks must exhibit and the customers banks may serve. Supervisors will not only enforce these regulations, but seek to cut off the bank’s ability to conduct a high-risk strategy.

Resolution reform will assure that market discipline reinforces supervisory discipline. Resolution reform will assure that investors, not taxpayers, will bear the cost of bank failure. Bail-in will replace bail-out. Consequently, investors will demand higher premiums to fund banking groups that take higher risk.

The boundaries set by regulation and resolution limit the risk a bank can pose, not only to depositors and the economy at large, but to some extent to investors. Although banks may complain that the guidelines are overly prescriptive, much of the guidelines in fact reflect good business practice. And if supervision is done well, investors as well as depositors and the economy at large will benefit.

*Setting the overall risk boundary*

In finance terms, regulators and supervisors are seeking to force banks into assuming lower risk. Resolution reform aims to eliminate the ratings pickup that banks derive from implicit government support so that there is no difference