Financial IT
Innovations in Technology

Dodd-Frank an Unintended Assault on Business

06.02.2017 11:15 am

The Dodd-Frank Act was intended to reduce levels of systemic risk in the banking sector, such that we would never again see highly leveraged balance sheet positions causing the failure of banks, and those failures causing contagion in other institutions and whole economies.

Unfortunately, the Act became an unintended assault on lending to businesses with capital adequacy provisions causing banks to stop lending for commerce. Loans were called in or withheld; overdrafts, materials financing and factoring agreements were not renewed; and, as a result, rates of business failures exploded. In some regions, banks refusing to fund the growth (i.e. not the decline) of small and medium sized enterprises has become the biggest single cause of business failure. The Act and much of the other related regulation since the financial crash also caused banks to divert most of their discretionary project budgets towards regulatory compliance initiatives – including meeting the needs of more demanding regulatory reporting.

Regardless of your personal and professional view on the value of increased regulatory reporting (Is anyone doing anything with the data? What difference has it made?), diverting funding away from projects that could improve products and services to customers should be a concern for everyone. It is in no-one's interests for our banks to become moribund.

Another highly ironic unintended consequence of the whole explosion in regulation (including Dodd-Frank, Basel X, EMIR, MiFid etc) has been that it punishes small banks and financial institutions more than the big guys. Ie the institutions that represent the biggest source of systemic risk are impacted less negatively than those that present almost no systemic risk. This is because the smaller institutions lack the resources (people, money, skills) to do the wholesale legacy system upgrades and rationalisations, and new systems developments to meet regulatory reporting and risk management requirements. Review and reform is very much required, otherwise our western banking system, business environments and economies will be stuck in a nose dive that could become a death spiral.

We should welcome a review of Dodd Frank and the Volcker Rule, and all other recent financial regulation. We will not see proprietary trading in banks returning to the extent that it puts the whole institution at risk (when it does come back – and it will come back - there will be severe ring-fencing of assets at risk) but we should all want to see our businesses better financed with a wide range of financial products.

Original article — https://financialit.net/blog/dodd-frank-unintended-assault-business