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Pros and Cons of Banking Supervision

Banking supervision stands out as one of the most feasible tools to assess the banking safety and security of financial transactions, which is also believed to have saved the entire globe from the financial recession caused by the financial crisis of 2008. The crucial point is that banking supervision was neglected and disregarded in the pre-2008 era, mainly because of the belief that the banking system should be warranted with non-interference policies. Following the adverse economic implications of the 2008 financial crisis, the entire banking industry reassessed the necessity of conducting the regular supervision facilities to ensure both the stability and resilience of the banking system as a whole.

With regards to the post-2008 epoch, banking supervision was held to accomplish three sophisticated objectives, including the enhancement of the resilience rates of individual banks, the development of the banking system as a whole, and the reduction of risk for taxpayers to bear the costs of future banking backlashes. Conversely, supervision facilities until the 2010s were criticized because of the intentional enforcement of delays to the data procession of individual banks. While critics point out that the operational capacity of the banking system has significantly slowed down because of banking supervision, the findings of alternative pieces of research emphasize the obligatory conduction of the supervision due to the focus on resilience, risk management, and the involvement of the central bank in securing the stability of the system as a whole.

The Concept of Non-Interference

First and foremost, one may point out that the tensest issue regarding banking supervision is the conduction of the actual supervision by the central bank, which is believed to be a violation of the banking system. In some sense, the opposition to bank supervision insists on ensuring the stability of the transaction capacity of individual banks due to the absence of direct ties with central financial institutions. Smaller banks per se receive less attention and are generally reviewed around full-scope examinations, meaning that the construction of a single design may be troublesome for policymakers (Eisenbach et al. 26). In other words, the main drawback of banking supervision is the act of intervention, which may disrupt operational processes or other vital processions of the banking system as a whole. It should be noted that banking supervision took place prior to the 2008 financial crisis, yet the supervision outcomes showed no direct threats to the banking system, whereas the flaws of those supervisory acts were related to either institutional design or incentive problems (Eisenbach et al. 35). Judging from the evidence-based fact that supervision ultimately failed to prevent the world from a crisis in 2008, the notion of supervision as a mediocre financial regulation may be justified. Although the mere essence of banking supervision is a controversial subject in the discourse of the financial system, researchers have sufficiently identified the above disadvantage of banking supervision as a single one, yet most convincing for further consideration.

Building Resilience

Secondly, the alternative perceptions of banking supervision are focused on portraying it as a useful instrument in maximizing the resilience of both individual banks and the banking system as a whole. Since the element of the jurisdiction in relation to the executor of banking supervision is crucial, the examination of resilience should be performed in relation to the historical discourse of the pre-crisis times. The time frame of 2000-10 in the banking system was associated with the commonly accepted trend of integrating the external agencies to conduct independent audits, supervisions, and annual critical assessments (Melecky 120). Since the entire course of the 2008 financial crisis was linked to fraud and intentional efforts to devalue mortgages, most of the supervision findings demonstrated the unprecedented stability and absence of apparent threats before the real estate bubble collapsed.

With regards to the takeaways of the 2008 financial crisis, the banking systems in various states across the globe decided to comply with delegating the supervision capabilities to central banks. The analysis of the aftermath of the 2008 financial crisis demonstrates that states with greater financial deepening and those with greater liquidity risk are more prone to banking crises (Melecky 119). Considering such an empirically based finding, banks in the post-2010 period conducted drastic measures to skyrocket the resilience of their accounts by continually receiving bank supervision in a central bank. Having acquired this lesson from history, it becomes evident that the banking system switched from the tendency of having external supervision services to such of the central bank, eventually making the system more transparent and resilient to the recidivism in the form of recession.

Risk Management and Stability

Since the instability of the banking system is interrelated with the essence of risk management, one of the most remarkable benefits of banking supervision is the minimization of risks, which have once led to the global financial crisis. The wave of reforms, which took place in the aftermath of the crisis, was useful for reconsidering and re-evaluating two important aspects, namely the quality and quantity of equity capital. The imposed reform-based emphasis on the higher quality of bank capital, coupled with the quantity of common equity, meant that the minimum requirement was increased from 2% to 7% (Sironi 47). By doing so, the banking system accomplished the objective of having decent back-up resources to overcome the fluctuations related to political or economic climates. The same series of reforms were directed to transform liquidity, which was also improved in banks' main liquidity ratios (Sironi 57). Consequently, the implementation of the suggested reforms was crucial to establish the pro-cyclicality of the banking system, whereas the increased awareness over risk minimization has become the objective of the highest priority in individual banks and the financial system as a whole.

In a similar manner, the historical background of banking supervision presents another worthy benefit, which relies upon the stability of the banking system. The trends of delegating the obligations to conduct supervision to central banks were coupled with the establishment of numerous reforms. Subsequently, the reassessment of the idea that banks' safety and soundness were directly related to the state of the economy in which they operate was unquestionably a merit of the post-crisis era (Sironi 57). As for stability, which incorporates the sub-elements of resilience, equity capital, and transparency, banking supervision is capable of providing valid reports that may be used to artificially stabilize the financial domain. In such regard, the stability of the central bank is believed to be the unquestionable status quo, which under the circumstances of having the power to conduct banking supervision, may assist individual banks, even the smallest ones (Melecky 111). Indisputably, the previously held supervision facilities, which neglected the institutional design or reviewed the banks in the form of clusters, are inadequate to accomplish stability. Notwithstanding, the already conducted reforms in aggregate with the rapid enhancement of resilience is the most evident representation of how banking supervision is beneficial for the banking system.

Final Remarks

Having scrutinized the basics of banking supervision, various opinions on the necessity of supervision, the historical background related to the 2008 financial crisis, and the reformation of the financial domain, one may say that banking supervision at its core contains both negative and positive consequences. On the one hand, the concept of non-interference is highly valued in the banking system, resulting in the opposition to banking supervision because of intentional backpedaling of the banks' operational capacity. On the other hand, the underlined aspects of resilience, risk management, and stability seem to outweigh the aspect of central regulation. The merger of numerous research studies also points out that despite the banking supervision from the central bank is heavily criticized, its role is immeasurable in terms of maintaining the resilience and stability of the banking system.

The historical discourse of the question points out that the world of finance has changed the approach to banking supervision after experiencing the adverse implications of the 2008 financial crisis. The implementation of a series of reforms has allowed individual banks to grow equity capitals, at the same time being supervised and critically assessed by central agencies, and not external ones. With regards to the continually transforming and digitalizing financial system, the future of banking supervision relies upon the persistence of the existing status quo concerning the sophisticated dilemma over the usability of banking supervision, which still remains unquestioned.

Works Cited

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