Euro-area financial sector

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growing and changing

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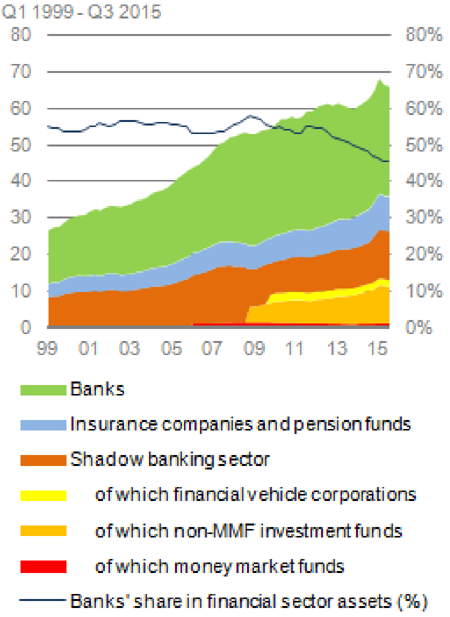
Despite a small dip in Q3 2015, the assets of financial institutions in the euro area are still broadly at a record level of about EUR 66 trillion. The financial sector – composed of banks, insurance companies & pension funds, and “shadow banks” – more than doubled its size over the past 15 years. Shadow banks have grown the most and now represent 40% of the financial sector with assets estimated at EUR 26 trillion.

Euro area financial sector: growing and changing

Assets in EUR trillion (left); bank share in financial sector in % (right); Q1 1999 - Q3 2015



Sources: ECB, Deutsche Bank Research

Despite a small dip in Q3 2015, the assets of financial institutions in the euro area are still broadly at a record level of about EUR 66 trillion. The financial sector – composed of banks, insurance companies and pension funds, and “shadow banks” – more than doubled its size over the past 15 years as business grew in most periods. “Shadow banking” is defined as credit intermediation that involves entities and activities outside the banking system. Shadow banks, often defined as “other financial institutions”, are subject to regulations, too – albeit operating under very different regimes than banks.

Asset growth in the euro area has not been distributed evenly across different financial institutions, especially since 2008. This divergence has changed the composition of the financial system. Before 2008, banks held about 55% of all assets in the financial sector whereas shadow banks accounted for around 30%. Since then, banks’ balance sheets showed some moderate ups and downs but overall assets remained flat at around EUR 30 trillion. Shadow banks, meanwhile, continued to expand their business, with assets now estimated at EUR 26 trillion. This translates into a 40% share in the financial sector while the banks’ weight decreased to 46%. Insurance companies and pension funds have steadily accounted for 12-14% of the financial sector.

As available statistics are not geared to measuring shadow banking, the respective figures are instead calculated as residuals from MFI statistics and national accounts data and give only a rough picture of the size and the type of entities involved. However, more recent data has shed some light onto the situation. Investment funds have contributed strongly to the expansion of the shadow banking sector since the financial crisis whereas financial vehicle corporations (often special purpose vehicles of banks) and money market funds have shrunk assets or stagnated over the past few years. They play an only minor role.

Given the data gaps, over half of the “other financial institutions” are difficult to identify and future developments are hard to forecast. However, as long as extremely low interest rates persist, investment fund assets will probably continue to rise. Credit institutions, though, are unlikely to grow their balance sheets considerably. Low interest rates, a sluggish euro-area economy and the effects of tighter regulation are taking their toll on banks’ business.

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