**Statement of FDIC Vice Chairman Hoenig on Bank Capitalization Levels and Semi-Annual Update of the Global Capital Index**

**September 28, 2015**

The semi-annual update of the Global Capital Index, showing the capital ratios for Global Systemically Important Banks, was released Monday by FDIC Vice Chairman Hoenig.

The Global Capital Index relies on International Financial Reporting Standards (IFRS) to measure a firm's tangible equity (loss-absorbing capital) against a more complete reporting of balance sheet assets, as shown in column 8 of the table.

Among the data:

- For the largest U.S. banking firms, the average tangible equity capital ratio – known inversely as the leverage ratio – is 5.73 percent (column 8). In other words, each dollar of assets is funded with about 94 cents of borrowed money.
- The largest regional and community banks, shown in the last three rows of column 8, have tangible capital ratios ranging from 7.58 to 8.92 percent. That is, they operate with between 1.32 and 1.56 times more funding from their ownership than do G-SIBs.
- The largest financial firms continue to report that their risk weighted measure (column 3) computes to a relatively higher level. This occurs because assumed risk weighted assets represent only 48 percent of total assets. The effect is to reduce assets used in computing the leverage ratio, which overstates the capital available to absorb losses relative to the total balance sheet.

"While relative loss-absorbing capital remains low among the largest firms, it is encouraging that the G-SIBs' tangible capital levels reflected in the GCI calculation increased 76 basis points from the last reporting period. This is especially noteworthy as their lending and net income levels also reached record levels," Vice Chairman Hoenig said. "Still, the largest financial firms remain less well capitalized and carry a greater concentration of assets compared with the remainder of the industry. Therefore, I hope to see continued improvement in the building of loss-absorbing capital and less leveraged funding for these largest, most important firms on which the economic system is so dependent."

The tangible capital measurement is calculated by comparing equity capital to total assets, after deducting goodwill, other intangibles, and deferred tax assets from both equity and total assets. The IFRS's balance sheet also reports the fair value of derivatives and other assets that are otherwise off-balance-sheet in US Generally Accepted Accounting Principles (GAAP). The tangible leverage ratio measures funds available to absorb loss against total balance sheet assets reported under the IFRS standard. It does not attempt to predict or assign relative risk weights among asset classes. “It is more difficult to game, and it provides the most clear and complete picture of a banking firm’s ability to absorb loss regardless of source,” Vice Chairman Hoenig said.

In contrast, the ratios of Tier I capital to risk-weighted assets for all banks (column 3), largest to smallest, are above 10 percent and some of the largest have ratios of more than 15 percent. “This higher capital ratio is achieved by reducing on-balance sheet assets by a pre-assigned risk weight and excluding off-balance sheet assets, such as derivatives. This measure is misleading and overstates the strength of these firms’ balance sheets. No other industry is allowed to make these kinds of adjustments,” Vice Chairman Hoenig said. “The tangible leverage ratio provides a more accurate measure of assets and risks than the balance sheet reported under either GAAP or Basel Risk Weighted measure.”

Global Capital Index **(**PDF Help) - As of 2nd half 2015

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*The views expressed are those of the author and not necessarily those of the FDIC.*