The Role of the Macro-Prudential Financial Regulation in enforcing Financial Stability: An Evolutionary Model

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Résumé

The motivation of this investigation lies on the awareness that economic systems are nothing else than complex organisms, which in order to survive they need to evolve through time and adapt themselves to the new environmental conditions. Such an evolutionary adaptation must take into consideration not only similarities among agents involved, but also their own differences from previous periods (in a word their heterogeneity). Along all the considerations within this investigation, the concept of time and highly time dependence, of the way in which agents such as households, production firms, banks, governments and financial regulators take their decisions and interact with one another, will be always present. However, since it is basically impossible to derive analytic solutions which describe how a modern "monetary economy" as a whole it evolves, particularly, due to its intrinsically dynamics, constantly reshaped by the change of both its institutions and its behavioural patterns through historic time, the present investigation will be conducted on the implementation of an evolutionary model by means of an Agent Based-Stock Flow Consistent macroeconomic model, in the vein of Caiani et al. (2016). The framework upon which this investigation will be build is the Macro-Prudential Financial Regulation. The concern to focus this investigation upon the Macro-Prudential Financial Regulation, banking regulation in particular, arises out of belief that banks play a paramount role in the creation of money, role that can not be neither neglected nor underestimated in the analysis of financial instability. The concern increases, even more, considering the globalisation of money markets and the recurrent danger of global financial disruption, cause money markets are imperfect. Not surprisingly, the Global financial crisis 2007-2009 and the widespread financial turmoil that it caused have exposed the inadequacy of the light-touch regulation. The broad purpose of this investigation, along all its facets, is to reach a better understanding about what the Macro-Prudential Financial Regulation, banking regulation in particular, has been done so far to ensure financial stability and to promote a sustainable growth, through the promotion of green investments. Formally, the model will be build considering a closed economy populated by five sectors (households, production sector, financial sector (essentially banks), pure government, and the central bank, and implementing a financial resolution mechanism which adopt five crisis resolution mechanisms in case of distress of a financial institution. The main purpose of this model is enable the investigation to explore the performance of these five financial crisis resolutions mechanisms in reducing financial contagion risk; enhancing financial stability; enhancing the overall economic output and growth by creating additional means of payments; and reducing the level of unemployment.

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Mots-Clés: Financial Instability, Macro, Prudential Financial Regulation, Crisis resolution mechanisms, Agent Based, Stock Flow Consistent model