

Monetary policy and financial stability: past lessons for future resilience*

di Christine Lagarde

It is a pleasure to be here in Amsterdam.

At today's symposium, we are saying a fond farewell to an outstanding colleague and friend. Klaas, you can look back on a remarkable career in public service at the national, European and global levels.

You were at the helm of De Nederlandsche Bank for over 5,000 days.^[1] In that time, you were a gifted communicator, conveying complex themes to the Dutch public in clear but never simplistic terms.

As a member of the Governing Council, you participated in over 330 meetings, overseen by three different ECB Presidents. I won't put you on the spot by asking you who your favourite was. You can tell me later – no pressure.

Being one of the elders on the Governing Council, your voice carried a weight that helped to forge policy consensus at the most critical of moments – be it during the pandemic or during the sharpest inflation shock in a generation.

And with experience comes wisdom. As Chair of the Financial Stability Board (FSB), you used that wisdom to advance the global agenda on financial stability, shaping international standards and coordination.

Klaas, you are known for reminding colleagues who tend to talk at length to be more “impactful” in their interventions. Well, now the pressure is on me. I promise to be as “impactful” as I can.

So today, I would like to focus on the two themes that have defined your career: monetary policy and financial stability. And in so doing, I will discuss the powerful role that regulation and supervision can play in reducing the potential trade-offs between them.

The interaction between monetary policy and financial stability

Financial stability and price stability are preconditions for each other.^[2] Yet history shows that in the pursuit of price stability, monetary policy can face two key trade-offs with implications for financial stability.

* Intervento al Farewell symposium for DNB President Klaas Knot, “Europe in the world - Challenges and Opportunities”, 3 ottobre 2025

The first can occur when monetary policy rapidly tightens. Higher interest rates help to curb inflation, but they can put pressure on banks by eroding asset values and asset quality, even as rising net interest margins offer them some relief.^[3]

We saw this during the 1980s, when the Federal Reserve rapidly tightened monetary policy to bring down high inflation.

Combined with US deregulation in the late 1970s, which encouraged riskier lending and weaker oversight, this monetary tightening was one of the key factors in the emergence of the savings and loan crisis. That led to the failure of roughly 1,300 savings institutions owing to the maturity mismatch on their balance sheets.^[4]

The second trade-off for monetary policy can arise during or following an extended period of monetary accommodation.

When inflation is below target, low rates can help stimulate demand and push inflation back towards target. But in an environment where regulation is relatively weak and especially where rates remain low for an extended period, they can also encourage borrowing, risk-taking and the build-up of financial imbalances.

These dynamics highlight how monetary policy can affect financial stability not only through banks' balance sheets but also via market valuations and investor risk appetite.^[5]

Crucially, financial vulnerabilities may keep building even *after* rates begin to rise. We saw this in the lead-up to the global financial crisis of 2008.

Low rates earlier in the decade fed the US credit and housing boom that later unravelled – years after the Federal Reserve had begun to gradually tighten. And in the euro area, the sharp rise in private debt in some countries was a key driver of imbalances that built up before the crisis.

The lesson for policymakers was clear. Insufficient regulation and supervision had allowed risks to build unchecked, leaving monetary policy as *de facto* the only tool available to confront the fallout.

This placed an undue burden on central banks, forcing them to shoulder responsibilities that could have been better managed through stronger safeguards in the first place. That insight powered the construction of a stronger regulatory and supervisory framework after 2008.

The post-2008 regulatory and supervisory framework was a turning point for the interaction between monetary policy and financial stability. It served as a powerful lever in mitigating the trade-offs between them and, accordingly, increased monetary policy's room for manoeuvre.

Monetary policy in extraordinary times

This was most visible during two extraordinary periods for monetary policy that followed in the wake of the global financial crisis.

The first period was when inflation was too low.

Central banks across advanced economies turned to a set of new – and, at the time, unconventional – tools to meet their price stability mandates, including large-scale asset purchase programmes and the introduction of negative interest rates.

These were significant measures to fight a significant challenge. And at the time, there were vocal concerns that these measures would fuel financial instability.^[6] Certainly, asset prices and housing valuations *did* rise notably during this period.

But crucially, given the stronger regulatory and supervisory regime, rising asset prices did *not* translate into excessive leverage in the banking system. In fact, banks in the euro area deleveraged in the decade after the global financial crisis. Similarly, private sector debt as a share of GDP also fell during that time.^[7]

And here in the Netherlands, we saw how macroprudential policy acted as the first line of defence against financial imbalances.

Under your leadership, Klaas, the DNB strengthened the macroprudential framework, introducing higher capital buffers and stricter risk weight requirements to guard against housing market risks. These measures kept in check vulnerabilities that might once have spilled over into broader financial instability.

After years of below-target inflation, the second period came unexpectedly – when euro area inflation surged to record highs after the pandemic and the energy shock sparked by Russia’s invasion of Ukraine.

In the Netherlands, for example, inflation rose rapidly, peaking just above 17% in September 2022 – almost six times the rate recorded a year earlier.^[8]

Once again, we faced an extraordinary situation – and the ECB had to step up. Alongside the unwinding of its asset purchases, it raised rates ten times by a cumulative 450 basis points, the fastest tightening in its history.^[9]

And once again, there were concerns about the financial stability implications of such a rapid tightening.^[10]

Tighter financing conditions risked straining borrower debt service and triggering market repricing. That, in turn, could have exposed financial institutions to vulnerabilities from falling asset values, maturity mismatches and weaker asset quality.

While there were some notable bank failures during this period, the global financial system overall remained broadly resilient to rising rates.

In the euro area, for example, banks were supported by stronger capital and ample liquidity buffers. Strong supervision also helped. Even before the inflation shock hit in full, the Single Supervisory Mechanism had factored interest rate risks into its supervisory work programme.^[11]

Moreover, in line with the outcome of its strategy review, the ECB's Governing Council was regularly assessing the links between monetary policy and financial stability as part of its policy deliberations.^[12]

The experience across these two monetary policy eras confirmed the lessons of 2008. Stronger regulation and supervision were able to contain financial exuberance and limit vulnerabilities. They allowed monetary policy to focus on its job of delivering price stability.

In this regard, Klaas, you have a knack for good timing. When you left the Governing Council last July, inflation had fallen substantially from its historic peak and stood at our target of 2% that same month.

A global financial system in transformation

Does the progress we have made in strengthening the regulatory and supervisory framework mean that policymakers can now let their guard down? The answer, of course, is no.

Today's global financial system looks very different from the one that stood on the brink in 2008.^[13] Two key shifts stand out compared with then.

The first has been the massive structural transformation that has taken place, the most striking change of which has been the growing footprint of non-banks in financial intermediation.

In the euro area, non-banks – ranging from investment funds and insurance corporations to money market funds and securitisation vehicles – have grown from about 250% of GDP in 2008 to more than 350% today.

Non-banks are also highly interconnected with the banking sector.^[14] In the euro area, banks' asset exposures to non-banks are sizeable, averaging around one-tenth of significant institutions' total assets.^[15]

At the same time, a second key shift is becoming increasingly evident – namely, signs of regulatory fatigue, which is creating an uneven playing field for financial institutions.

In particular, investment funds, despite their increasing systemic importance, operate under far lighter rules compared with the banking sector. That has in part helped to fuel their growth.

One of the reasons behind this regulatory fatigue is that the post-2008 global regulatory framework has arguably been a victim of its own success.

In policymaking, 17 years is a long time. Not only do painful memories fade, but so too does the recognition that the financial stability the world now enjoys is thanks to the robustness of that global regulatory framework established back then.

This fading sense of urgency, together with concerns that banks' competitiveness vis-à-vis non-banks is threatened by the uneven playing field, has ignited calls to revisit the existing set of financial rules and regulations.

The importance of levelling up regulation and supervision

So how should policymakers react to these shifts in the financial system?

In short, it is vital that policymakers adapt regulation and supervision to this challenging environment. They should do so not by *lowering* standards for banks, but by *levelling them up* for non-banks that are involved in bank-like activities, or with significant links to the banking sector.

That helps to address banks' concerns about the uneven playing field. And better supervision of non-banks would make potential financial stability risks that have lain dormant in darker corners of the economy more visible, allowing policymakers to pre-empt them.

Klaas, as FSB Chair, you have been a powerful voice in warning against the dangers of regulatory rollback.^[16] And under your leadership, the FSB advanced ambitious policy recommendations on strengthening rules for non-banks.

They covered money market fund resilience^[17], liquidity mismatches in open-ended funds^[18], margin preparedness^[19] and, most recently, leverage in non-banks.^[20] This is not to mention the FSB's important work on other areas of financial stability risk.^[21]

As a central banker, I cannot pretend to be an unbiased observer in these discussions. Because if the regulatory and supervisory spotlight were to be broadened to non-banks, monetary policy would benefit too.

If risks were to build outside the banking system, beyond the current reach of regulators and supervisors, the trade-offs that were evident before 2008 may re-emerge, with monetary policy *de facto* being the only tool to "get in all of the cracks" and rein in financial exuberance.^[22]

That would be a suboptimal outcome, one that potentially constrains central banks' full freedom to defend price stability.

So as referees on the playing field, it is vital that policymakers resist regulatory fatigue and redouble their efforts to extend stronger global rules to non-banks involved in bank-like activities, or with significant links to the banking sector.

At the same time, after a decade of adding regulation, this is a good moment to take stock and assess how regulation can be simplified to avoid duplication and unnecessary burdens on financial institutions.

In this respect, the ECB High-Level Task Force on Simplification is developing proposals for simplifying the European prudential regulatory, supervisory and reporting framework for the European Commission's consideration.

The goal is not to relax rules, nor undo what has been achieved. Instead, the task force is exploring how to reduce undue complexity in selected aspects of the capital structure, reporting and supervision, while also maintaining the resilience of banks and fostering greater integration and harmonisation in EU frameworks.

Conclusion

Let me conclude.

I have spoken this evening about one Dutch elder – you, Klaas. Hopefully I have done so in a relatively impactful manner. But I would like to finish by citing another Dutch elder.

In his *Adagia*, the humanist Erasmus gathered the wisdom of past centuries for the benefit of those living in the present. Among the proverbs that still resonate today is, “Prevention is better than cure”.^[23]

In the Netherlands in particular – often said to have witnessed the world's first financial bubble, though historians debate its true scale^[24] – that lesson endures: vigilance is wiser than complacency.

This principle lies at the heart of sound regulation and supervision. As the financial system evolves, regulators and supervisors must retain visibility of potential risks, since preventing instability is always less costly than repairing the damage afterwards. It also helps to limit the potential trade-offs between monetary policy and financial stability.

Policymakers should not wait for another financial crisis to be reminded of how high the stakes are. It is imperative to extend oversight to non-banks involved in bank-like activities, or with significant links to the banking sector – and policymakers must do so sooner rather than later.

Thank you.

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2. ECB (2025), [*An overview of the ECB's monetary policy strategy*](#), 30 June.
3. Enria, A. (2022), "[Monitoring and managing interest rate risk along the normalisation path](#)", keynote speech at the Deutsche Bundesbank symposium "Bankenaufsicht im Dialog", 8 November.
4. Hane, G. (1997), "[The Banking Crises of the 1980s and Early 1990s: Summary and Implications](#)", *History of the Eighties: Lessons for the Future. Vol. 1, An Examination of the Banking Crises of the 1980s and Early 1990s*, Federal Deposit Insurance Corporation (FDIC), Washington DC.
5. Workstream on macroprudential policy, monetary policy and financial stability (2021), "[The role of financial stability considerations in monetary policy and the interaction with macroprudential policy in the euro area](#)", *Occasional Paper Series*, No 272, ECB, Frankfurt am Main, September.
6. See, for instance, the discussion in European Parliament (2015), "[The ECB's Quantitative Easing – Early results and possible risks](#)", December; see also BIS (2015), [*85th Annual Report: 1 April 2014-31 March 2015*](#), June.
7. Private sector debt as a share of euro area GDP fell by 11 percentage points from its 2009 peak to 138% by the end of the following decade. See Eurostat, [*Private sector debt, consolidated - % of GDP*](#).
8. HICP in the Netherlands was 3.0% in September 2021.
9. In parallel, it also established the Transmission Protection Instrument in July 2022. See ECB (2022), "[The Transmission Protection Instrument](#)", *press release*, 21 July.
10. For the euro area, see ECB (2023), [*Financial Stability Review*](#), May; for the United States, see Office of Financial Research (2023), "[OFR Finds Elevated Threats to U.S. Financial Stability Due to Inflation, Ongoing Geopolitical Risks, and Global Conflicts](#)", *press release*, 6 December; for a global

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11. As noted in Enria, A. (2023), “[Well-run banks don’t fail – why governance is an enduring theme in banking crises](#)”, speech at the 22nd Annual International Conference on Policy Challenges for the Financial Sector organised by the World Bank, International Monetary Fund and Federal Reserve System, 1 June.
 12. ECB (2025), “[An overview of the ECB’s monetary policy strategy – 2025](#)”, 30 June; and ECB (2021), “[An overview of the monetary policy strategy – 2021](#)”, 8 July.
 13. Paulson, H.M., Jr. (2010), *On the Brink: Inside the Race to Stop the Collapse of the Global Financial System*, Business Plus.
 14. Acharya, V.V., Cetorelli, N. and Tuckman, B. (2025), “[Where Do Banks End and NBFIs Begin?](#)”, ECB Annual Research Conference 17-18 September.
 15. Franceschi, E. et al. (2023), “[Key linkages between banks and the non-bank financial sector](#)”, *Financial Stability Review*, ECB, May.
 16. Knot, K. (2025), “[How is the water? Continuing our work to preserve financial stability](#)”, speech at the Bank of Spain and CEMFI Fifth Conference on Financial Stability, Madrid, 12 June.
 17. FSB (2021), “[Policy proposals to enhance money market fund resilience: Final report](#)”, 11 October.
 18. FSB (2023), “[Revised Policy Recommendations to Address Structural Vulnerabilities from Liquidity Mismatch in Open-Ended Funds](#)”, 20 December.
 19. FSB (2024), “[Liquidity Preparedness for Margin and Collateral Calls: Final report](#)”, 10 December.
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 21. See, for instance, FSB (2023), “[High-level Recommendations for the Regulation, Supervision and Oversight of Crypto-asset Activities and Markets: Final report](#)”, 17 July; FSB (2023), “[High-level Recommendations for the Regulation, Supervision and Oversight of Global Stablecoin Arrangements: Final report](#)”, 17 July; and FSB (2025), “[FSB Roadmap for Addressing Financial Risks from Climate Change: 2025 Update](#)”.

22. Stein, J.C. (2013), "[Overheating in Credit Markets: Origins, Measurement, and Policy Responses](#)", speech at the "Restoring Household Financial Stability after the Great Recession: Why Household Balance Sheets Matter" research symposium sponsored by the Federal Reserve Bank of St. Louis, St. Louis, Missouri, 7 February.
23. Erasmus (1500), *Adagia*.
24. See, for instance, Goldgar, A. (2007), *Tulipmania: Money, Honor, and Knowledge in the Dutch Golden Age*, University of Chicago Press.