

To what extent does the market concentration of large asset managers (e.g., BlackRock, Vanguard) pose systemic risks to global financial markets?

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ABSTRACT

In the past decades, large asset managers such as BlackRock, Vanguard, and State Street have risen to center stage in global finance. Unlike banks, which profit from lending and leverage, asset managers collect savings from households, pension plans, and institutions and buy securities through mutual and exchange-traded funds (ETFs). Their rapid growth created benefits and risks. They provide investors low-cost exposure to diversified portfolios, direct capital across industries, and stability over the long term. However, concentration of trillions of dollars in a few firms creates key problems for finance stability and corporate governance. System risks arise through liquidity mismatch, by which day-by-day redemptions face illiquid assets, or through herding and passive flows, which amplify market swings. Their pervasive ownership of competitors may further weaken rivalry, and their vote control entitles them to massive influence over company decisions. Their frailties were unleashed by the COVID-19 crisis, and central banks' interventions were needed to soothe markets. Our work examines the new systemic challenges of the dominance of a few asset managers and explores potential reforms so that their role reinforces rather than undermines the global capital formation system.

I. Introduction

During the past decades, big money managers have become crucial actors in the world's financial system. Differently from banks, whose business is very much based on leverage and lending, money managers are essentially intermediaries: they gather funds deposited by households, pension funds, and institutions and invest them in financial markets through products such as mutual funds and exchange-traded funds (ETFs). This has turned money managers into the cornerstone of how today's finance works, as they channel capital within industries and nations and provide relatively inexpensive and diversified means of accumulating wealth to their investors.

This trend is reflected in the assets of the very largest firms. BlackRock now has around \$12.5 trillion and Vanguard around \$10.4 trillion in assets (Reuters, 2025). With State Street, these firms are sometimes dubbed the "Big Three" of the asset management industry. Combined funds under management now equal the economic output of big world economies. This concentration of capital in very few firms has been alarming to policymakers, scholars, and regulators about the risk to corporate governance and financial stability.

Concentration here is the observation that very few firms control very large pools of capital. This is important in several ways. First, since these firms have huge stakes in thousands of listed companies, corporate governance is in their hands. The Big Three vote in shareholder meetings on behalf of millions of investors at once and so get to determine executive pay, board composition, and corporate strategy. Secondly, their size is so huge that when their portfolios change—even in the normal course of index rebalancing—the impact has ripples in world markets.

Another related idea is "common ownership" where the same asset managers are stakeholders in several firms within the same industry. As much as it diversifies portfolios, it may lower competition among firms if large stakeholders opt for stability rather than competition. For instance, if an asset manager is a shareholder in several rival airlines, it will hardly encourage fierce competition among them. This is an example of how concentration in the asset management industry has an impact on both financial markets and industry structure in the wider economy.

The growth of passive approaches to investing has intensified these problems. Passive funds like index funds and ETFs mimic market indices rather than attempting to select victorious stocks. Passive funds are less expensive and tend to match or surpass active funds in performance. This is why they are gaining popularity. The implication is that huge amounts of money are channeled automatically into the same pool of businesses, their fundamentals notwithstanding. At tiny levels this won't be an issue, but when trillions are invested this way, it saps market dynamism and allows shocks to propagate faster across assets.

These structural changes bring potential systemic risks. Unlike banks, asset managers do not typically borrow heavily, but their business model still creates vulnerabilities. For instance, many funds allow investors to redeem their money daily, even when the underlying assets—such as corporate bonds—are not easy to sell quickly. This mismatch between liquid liabilities and illiquid assets can create stress in times of market turmoil, forcing funds to sell assets at a loss. Such dynamics were evident in March 2020, during the COVID-19 crisis, when bond markets came under pressure and central banks had to step in partly to stabilize funds.

Aside from fiscal prudence, centralizing assets in management is controversial on grounds of governance and accountability. As "universal owners" owning equity in the entire economy, they are in an ideal position to pressure firms to address long-term challenges such as climate change and inequality. That is posited to make them a force for stability, reconciling corporate behavior to broader social ends. Detractors worry their motivations are still too short term in a financial sense and their huge sizes bring too much concentration of influence over society with too little direct authority.

As a whole, these asset managers like Vanguard and BlackRock are now pillars of the global financial system. Their growth has had clear advantages—like increased convenience in accessing diversified holdings and a predictable source of funding for companies and governments—while simultaneously their market concentration brings forth new vulnerabilities: liquidity mismatches, reduced competition by virtue of common ownership, and concentrated governing power. These considerations suggest that asset management, once considered a relatively benign and inactive segment of finance, needs to be examined in greater detail in considerations of systemic risk.

This essay will explore these dynamics in greater detail by comparing and contrasting the asset managers to banks and tracing historical parallelisms and considering policymaking alternatives to ensure these players are a source of stability in the global economy and not a source of vulnerability.

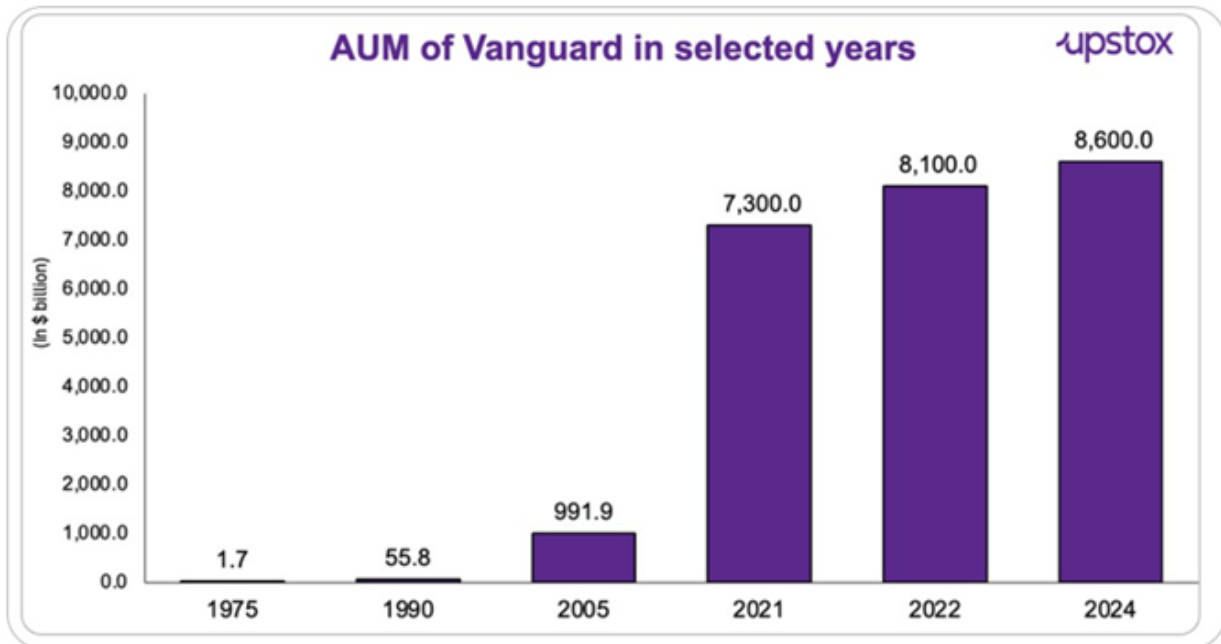
II. Theoretical Background and Historic Foundation

The role of asset managers in the contemporary system of intergenerational finance is best understood by reference to the historical evolution of financial intermediation. For much of the twentieth century, banks were dominant in finance. Households and firms remitted deposits to banks, and banks remitted loans to firms, governments, and households. The system has been dubbed "bank-based" with the implication then that discussions of financial stability were focused on capital adequacy, leverage, and risk of bank runs. As compared to this system, asset managers played only a subordinate role and mainly served high-net-worth households or specialist institutions.

This all started to change in the latter part of the twentieth century, specifically from the 1970s onward. Various factors were responsible: removal of regulatory barriers to competition on financial markets, increases in household contributions to retirement funds, and innovations in the creation of financial instruments. The innovations of the 1970s in index funds by Vanguard were particularly important because it brought market tracking within the reach of even very low-cost funding. This over time redirected funds away from banks and toward capital markets

themselves, where the dominant intermediaries now became the asset management firms like Vanguard or BlackRock (Blakeley, 2025).

The following figure illustrates the remarkable growth of Vanguard's assets under management across selected years, reflecting the broader expansion of the asset management industry.



Source: Statista, via Upstox

Theoretically speaking, asset managers belong to the bigger picture of financial intermediation. As banks, they minimize transaction costs and deliver diversification and make it easier to invest on the part of savers. However, their logic is different. Banks generate credit through the expansion of their balance sheet, whereas asset managers deploy available capital given by their investors. Accordingly, their risk profile is varied: whereas banks are concerned about solvency in the conventional sense, asset managers are challenged by liquidity risk, investor behavior risk, and market risk. Economists term it a "market-based" paradigm of financing as compared to the earlier "bank-based" paradigm prevalent in broad swathes of the twentieth century (Economic Liberties, 2023).

Another crucial theory lens is "too big to fail," long used to describe banks. These were firms so big and interconnected their failure might destabilize the system. Ever more often now academics and regulators wonder if big asset managers might be "too big to fail" too. As they do not leverage to the same degree as banks, their massive size, interconnected funds, and

dominance in world capital markets mean their strain in times of trouble could still be systemic. For instance, if in a crisis investors simultaneously try to pull their money from bond funds, the ensuing fire sales can spillover to prices in the overall system.

Finally, historical parallels show that financial concentration is not new. At various times, from the dominance of early merchant banks in the nineteenth century to the rise of conglomerates in the twentieth, the accumulation of financial power in a few hands has raised stability concerns. What is different today is the scale and structure of asset management: trillions of dollars under management, spread across thousands of companies and countries, but controlled by only a few large firms. This makes the study of their historical evolution and theoretical underpinnings crucial for understanding their systemic importance today.

III. Systemic Risk Transmission Channels in Asset Management

The growth of the asset management industry has restructured the landscape of modern-day finance. Mutual funds and exchange-traded funds (ETFs) have provided investors with low-cost diversification and brought to the financial markets an important alternative to bank intermediation, but their growing size has brought with it new vulnerabilities. Most asset managers are not highly levered to the same extent as banks but are nonetheless at risk of causing systemic risk through fund structure, management, and interconnectedness with markets. IMF and FSOC reports indicate several key paths through which systemic risk will likely arise in asset management: liquidity mismatches, herding and procyclicality, crowded trades, fire sales and contagion, operational concentration, and episode of stress such as the COVID-19 pandemic.

Liquidity

One of the most widely discussed risks comes from liquidity mismatches in open-ended investment funds. These funds typically promise investors daily redemption, meaning they can withdraw their money at any time. However, a significant share of these portfolios—especially in bond funds—consists of assets that cannot easily be sold on short notice. This mismatch creates a vulnerability: if many investors redeem simultaneously, fund managers may be forced to sell less liquid securities at steep discounts to meet withdrawals.

The design of the incentives itself aggravates the problem. As investors withdrawing in earlier periods are able to avoid the expenses of involuntary redemption, it is a case of first-mover advantage. Others might then come in once redemption commences attempting to cover themselves, potentially creating a run-like event. The IMF has been critical of how such very same mechanism turns even "plain-vanilla" products like mutual funds and ETFs into potential amplifiers of shocks despite these funds having no leverage (IMF, 2015). FSOC has also emphasized liquidity mismatches in open-ended funds as a principal vulnerability in American

capital markets (FSOC, 2016).

Bond funds demonstrate the problem most explicitly. Contrary to equities, numerous corporate and municipal bonds are listed in relatively thin markets. As funds try to liquidate massive amounts in times of duress, pressures on prices are extreme and serve to further erode investor trust and catalyze additional redemptions. Liquidity mismatches are therefore not merely a fund-level risk but an avenue of systemic risk diffusing into wider fixed-income markets.

Procyclicality and Herding

Another systemic risk channel is herding and procyclicality in asset management.

Despite diversification rhetoric by fund managers, it has been found in empirical examinations that their behavior often converges. Managers might imitate colleagues to avoid lagging behind references or to react to flows. Managers performing poorly might increase risk to "catch up" and bring their portfolios even more into alignment.

The consequence is that asset managers can act in ways that reinforce market trends rather than dampen them. During periods of rising prices, herding into popular assets can inflate valuations. Conversely, during downturns, simultaneous selling by many funds can deepen losses and accelerate market declines. The IMF has documented that herding has become increasingly prevalent in recent decades, with managers often responding to common signals or benchmarks rather than independent assessments (IMF, 2015).

This procyclical behavior is significant because fund managers now represent a significant portion of equity and fixed-income marketplace transactions. Their coordinated behavior could thus magnify volatility and spread shocks worldwide notwithstanding broad-based worldwide coverage by several large fund families.

Crowded Trades and Price Dislocations

Related to herding is also the problem of crowded trades, where large numbers of funds converge on the same assets. The crowding is particularly obvious in passive products such as ETFs and index funds whose money is automatically committed in accordance with the constituents of indices.

This system has the risk of inducing feedback loops. When an issue is added to a large index, huge passive inflows tend to drive up the price, fundamentals aside. When an issue is dropped from an index, forced sales may lower the price. These flows are capable of inducing price dislocations—temporary misalignments of prices relative to underlying values—especially in less liquid markets.

The March 2020 panic presented a stark illustration. Certain ETFs were changing hands at prices well lower than the levels of their underlying bond holdings, indicating the challenge of unwinding bonds promptly in stress. The gaps were an indication of strains elsewhere in credit markets and showed how index-tracking funds' mechanics magnify pressure (FSOC, 2020). Highly crowded trades also reduce diversification benefits. If multiple large funds hold identical securities, shocks to these securities will spread through portfolios simultaneously. This co-movement might increase inter-market correlations and reduce the stabilization effect of independently made choices and leave the investor exposed to system shocks.

Fire Sales and Contagion

During big redemptions, money managers have to carry out fire sales, offloading assets promptly at discounted prices. The former might propagate contagion to other markets.

The process usually unfolds in stages. First, redemptions draw down liquidity in certain funds. Then, managers sell assets, driving down prices. Then prices falling reduce the value of similar assets elsewhere owned by other funds and external investors, causing them to redeem or sell in turn. The cycle may repeat itself and spread anxiety through markets.

This dynamic has been pinpointed by FSOC as an important risk: because individually and collectively asset managers control huge shares of equity and credit markets, their liquidation procedures have the potential to induce larger market spirals (FSOC, 2016). The IMF similarly warns that fire sales risk spread shocks from a single fund to the entire system of finance, primarily in situations in which assets are thinly traded (IMF, 2015).

More particularly, fire-sale dynamics are in no way restricted to crises. Even normal rebalancing by large funds is enough to unsettle prices but in stress scenarios, the impact multiplies. When redemptions congregate in a few large fund families, then contagion risk spreads across markets and geographies.

Operational Concentration

Apart from portfolio risk, operational concentration is another issue faced by the industry. There is an absolute scarcity of platforms whose technology and infrastructure become the basis of world-wide asset management. For example, BlackRock's Aladdin system is utilized not only by BlackRock itself but by many other financial institutions to carry out risk management and portfolio analytics.

This engenders a certain sort of single-point dependency. If such a system is to be hit by a disruption—via technical failure or cyberattack—the consequences might begin to cascade

through several asset managers and markets at once. FSOC has identified that reliance on a few service providers, from custodians to risk-management platforms, brings into being vulnerabilities less obvious but possibly systemic (FSOC, 2016).

Operational concentration highlights that systemic risk in asset management is not solely about balance sheets or investment flows, but also about the infrastructure underlying the industry.

COVID-19 as a Stress Test

The COVID-19 pandemic gave the world a real-world stress test on asset management. Open-ended bond funds and ETFs saw significant redemptions in March 2020 when financial markets responded to the shutdowns in the economy. The liquidity in corporate bond markets dried up and ETFs tracking these bonds were trading at historical lows compared to their net asset values.

As part of the initiative to reestablish market functioning, the Federal Reserve established the Secondary Market Corporate Credit Facility (SMCCF), whose corporate bond and bond ETF purchases reduced liquidity shortages. This was unprecedented: a central bank was directly funding segments of the asset management industry (Federal Reserve Bank of New York, 2020). The bailout brought into sharp relief big funds' and ETFs' systemically significant roles. Without central-bank facilities, stresses in asset managers may well have spilled over to become a full-blown financial crisis.

The COVID-19 episode engendered several of the vulnerabilities highlighted by regulators in anticipation of the crisis—liquidity mismatches, crowded trades, and external backstops required—while it demonstrated the degree to which asset managers are today an integral to financial stability even if they are separate in structure and regulation from banks.

Conclusion

The conduits through which systemic risk may be routed by fund managers are varied but interrelated. Liquidity mismatches offer the threat of runs; herding and crowded trades grow volatility; fire sales and contagions propagate shocks from market to market; operational concentration amplifies interdependencies; and duress episodes such as COVID-19 demonstrate how these vulnerabilities converge. What sets asset managers apart from banks is the lack of significant leverage but what renders them systemically significant is their size and design. With trillions of dollars in assets and ubiquitous reach in markets, big asset managers are now at the center of the soundness of global finance. The IMF and FSOC report evidence coupled with recent crises shows that systemic risk in asset management is not theoretical—it is tangible and repeatable and will in all probability exist unless adequate protections are in place.

IV. Market Concentration and Common Ownership

Concentration Trends

Over the past few decades, asset management has become one of the strongest elements of world finance. Increasingly few firms now dominate an absolutely huge proportion of world savings. It is the "Big Three" — BlackRock, Vanguard, and State Street— however, which are the leaders. Combined, these three firms are in charge of over US\$20 trillion worth of assets and are by far the biggest shareholders in numerous of the world's largest firms.

The following figure shows the ranking of leading global fund managers by assets under management in 2025, highlighting the concentration of capital in only a few firms.



Source: SWF Institute

This high level of concentration is significant because if so few firms are so wealthy, their decisions will affect capital markets and the overall economy. Compared to smaller money managers, these giants are "universal owners" in the respects their money is diversified in nearly all industries and sectors. That puts them in a central position in world capitalism.

The Common Ownership Problem

Another important trait of this concentration is mutual ownership. This is where the same fund managers are key players in several competing firms. Research has it that the Big Three hold a significant percent of shareholdings in numerous firms listed in the S&P 500 index (Azar et al, 2018). For example, they are key players in multiple airlines or pharmaceutical companies at the same time.

The following figure illustrates how Vanguard and BlackRock rank among the largest shareholders of leading global companies, such as Apple, underscoring the concentration of ownership.

Company	Largest investor	2nd largest investor
Apple	Vanguard Group (7.6%)	BlackRock (6.2%)
Microsoft	Vanguard Group (8.1%)	BlackRock (6.7%)
Alphabet (Class C)	Vanguard Group (6.6%)	BlackRock (5.9%)
Alphabet (Class A)	Vanguard Group (7.5%)	BlackRock (6.7%)
Amazon	Vanguard Group (6.4%)	BlackRock (5.4%)
Facebook	Vanguard Group (7.6%)	BlackRock (6.5%)
Tesla	Vanguard Group (5.9%)	BlackRock (5.1%)
Berkshire Hathaway	Vanguard Group (10.1%)	BlackRock (8.1%)

Source-blackrockvanguardwatch.com, via Upstox

The problem is mutual ownership might reduce competition pressures. If the same investors share in the benefits of all the firms in an industry, then the same investors might be content with overall stability and earnings rather than an individual company each trying to pull ahead of the rest. This is compared to typical forms of ownership, where an individual shareholder might wish

to have a leading company over rival firms.

Effect on Competition

The consequences of common ownership are already observable in certain sectors.

Research on American airlines has found routes with greater shares of common ownership to be characterized by greater prices for tickets because airlines will compete less effectively if their dominant investors are the same (Azar et al, 2018). The same issue is present in pharmaceuticals, in which mutual ownership will be disincentive to innovate. If rival firms in drugs share the same shareholders, then less will be the motivation to innovate in the creation of medicine.

While it is debated how widespread these costs are, the problem is simple: if a few massive firms control shares in big slices of the economy, markets may be less competitive and consumers may be overpaying.

Corporate Governance Risks

Another problem is corporate governance. Although index funds are "passive" in their approach — namely, tracking stock market indices — they are still voting at shareholder meetings. This implies that the Big Three vote on behalf of millions of individual investors in matters of executive rewards, mergers, or ecological policies.

The size of their voting powers is massive. For instance, collectively they vote on an estimated one-quarter of all votes within big U.S. companies (Bebchuk & Hirst, 2019). This positions them at the center of determining how big companies are managed. The criticism is that it presents a paradox. On the one hand, they might be too inactive and merely rubberstamp management's actions with insufficient scrutiny. Conversely, if active enough, their influence on corporate strategies in the overall economy may be too great.

The "Goldilocks Dilemma"

This is in many ways referred to as the "Goldilocks dilemma." If the asset managers become too hands off, then they do not look after the investors by leaving poor management to carry on unchecked. If too hands on, then they become like world regulators but are neither elected nor answerable. It is hard to hit the right note here given the fact these firms have thousands of firms to watch simultaneously.

Some steps have been taken, like attempts to provide individual shareholders with greater control over voting their shares. Thus far, though, Big Three stewardship has been debated as being either "too little" or "too much."

COVID-19 as a Stress Test

The COVID-19 pandemic acted as a real-world stress test for asset management. In March 2020, open-ended bond funds and ETFs faced heavy redemptions as liquidity in corporate bond markets collapsed, causing ETFs to trade far below their net asset values. To restore stability, the Federal Reserve launched the Secondary Market Corporate Credit Facility (SMCCF), buying corporate bonds and bond ETFs—an unprecedented move that revealed how vital asset managers have become to financial stability. The crisis exposed key vulnerabilities regulators had long warned about, including liquidity mismatches, crowded trades, and reliance on external backstops.

Conclusion

Overall, the concentration in the asset management sector has posed challenges to society and markets. Only a few firms now possess massive pools of funds and are controllers of significant blocks in large companies. Through common ownership, competition and innovation are potentially stifled. Through voting powers, corporate governance is exerted by them either in an over-submissive or over-dominant way.

These tendencies illuminate the manner in which concentration in the financial sector is less about markets and more about power. With the trend of the asset management industry growing in prominence, the key will be to ensure it is competitive and remains accountable to the greater public interest.

V. Policy and Regulatory Implications

The concentration of assets in a handful of global asset managers has provoked increasing discussion on how regulators should react. As much as asset managers offer advantages like reduced costs and easier access to financial markets, their concentration results in posing systemic risk through their sheer size, common ownership, and corporate control. Policymakers thus are challenged to make the industry an ally of financial stability, fair competition, and responsible corporate conduct.

Microprudential Regulation: Strengthening Firm-Level Oversight

Another essential approach is microprudential regulation, focusing on risk at the individual-firm level. Supervisors might require asset managers to have better information, to carry out stress testing, and to issue higher disclosure of the risk in their portfolios. For example, open-ended bond funds face liquidity mismatches while withdrawing on a daily basis but having assets whose liquidity is low. Supervisors might require stricter rules on liquidity management in order to

reduce the risk of runs by investors at short notice (IMF, 2015).

Another microprudential tool is improving reporting standards. If asset managers disclose more details about their holdings and redemption practices, investors will have a clearer understanding of risks. This can help reduce panic in times of stress and allow regulators to spot vulnerabilities before they escalate.

Macroprudential Policy: System-wide Risk Approach

While regulation at the firm level matters, concentration in fund management also presents system-wide risks. This necessitates macroprudential reforms — policies taking into consideration the effects of the overall financial system and not at the institution level. The Financial Stability Oversight Council (FSOC) in America has debated whether giant fund managers are systemically important like large banks. However, upon industry lobbying in opposition to this idea, regulators turned their attention to risky behavior and not calling out firms by name (FSOC, 2016).

This activities-based method requires regulators to scrutinize activities like securities lending, mismatch of liquidity and crowded trades, irrespective of which company is practicing them. The plus-point is that it prevents undue targeting of individual companies but the minus-point is that it may overlook the systemic risk being generated by virtue of sheer size and concentration.

Liquidity Management Instruments

Another reform priority is the manner in which funds manage liquidity. Open-ended funds usually give investors the right to redeem on short notice even if the fund is invested in illiquid assets. This presents the risk of "first-mover advantage" in which investors are expedited to redemption before losses become deeper. As a corrective measure, regulators have proposed using tools like:

- **Redemption fees:** charging investors a low fee to withdraw earlier, to prevent frequent runs.
- **Swing pricing:** adjusting the share price of the fund in large redemptions so the exiting investors cover the expenses and not the remaining ones.
- **Minimum liquidity coverage:** to require funds to maintain an amount of their assets in cash or other readily marketable securities.

These procedures are aimed at making redemption policies less biased and preventing firesales from spilling over the entire financial system (IMF, 2015).

Addressing Market Concentration and Governance

Regulators are even considering how to tackle concentration of voting and ownership power. Big Three dominance raises the question of whether a few companies should control so great a percentage of shareholder votes in big corporations. Others suggest ownership stake restrictions or reforms allowing index fundholders to vote shares directly in their own names rather than leaving all voting in the hands of fund management (Bebchuk & Hirst, 2019).

Another idea is to introduce greater competition within the industry of asset management itself. As the Big Three possess market share in part because their low-cost passive funds crowd their competitors out of the market, smaller players cannot compete.

Regulators might introduce greater competition by facilitating market penetration by newcomer firms or by blocking mergers to further concentrate ownership.

The Role of Central Banks

The 2020 COVID-19 pandemic brought to light the systemically critical nature of asset management. As bond markets seized up, the U.S. Federal Reserve stepped in and purchased corporate bond exchange-traded funds (ETFs), several of whose underlying assets were managed by BlackRock. This demonstrated that governments in emergencies might be forced to come to the rescue of big asset managers to preserve financial markets.

While these kinds of interventions bring markets back in balance, however, they introduce the issue of moral hazard: if firms believe someone is always going to bail them out, they will be riskier. Regulators can avoid this by creating firmer rules on how and when to bail out asset managers in crisis so taxpayers' money is not used to bail out private companies unnecessarily.

Conclusion

Large asset management has brought stability and efficiency to world finance but has generated new systemic risk. Policymakers must grapple with how to design rules to mitigate both system-wide and firm-level risk. Steps like improved liquidity management, enhanced disclosure, oversight based on activities, and governance reform are all possible contributors.

VI. Political Economy of Asset Management

Large asset management is political as well as an economic force. Through their size, scope, and reach, large asset management companies are inextricably linked to governments, regulators, and central banks. Politically speaking, in some respects, the political economy of asset management is the story of how private capital institutions are able to influence public policy and yet always

be rewarded.

Lobbying Power

Perhaps the best-established case of political influence is the lobbying muscle of the "Big Three." During the early 2010s, the U.S. Financial Stability Oversight Council (FSOC) considered whether big asset managers were "systemically important financial institutions" and thus deserving of such a designation. That would have subjected them to tighter regulation comparable to that imposed upon giant banks. However, after intense lobbying by the industry, FSOC moved away from calling out individual firms and towards calling out certain activities, like liquidity mismatches. This result registered the success of asset managers in framing the regulatory conversation to steer clear of direct regulation (FSOC, 2016).

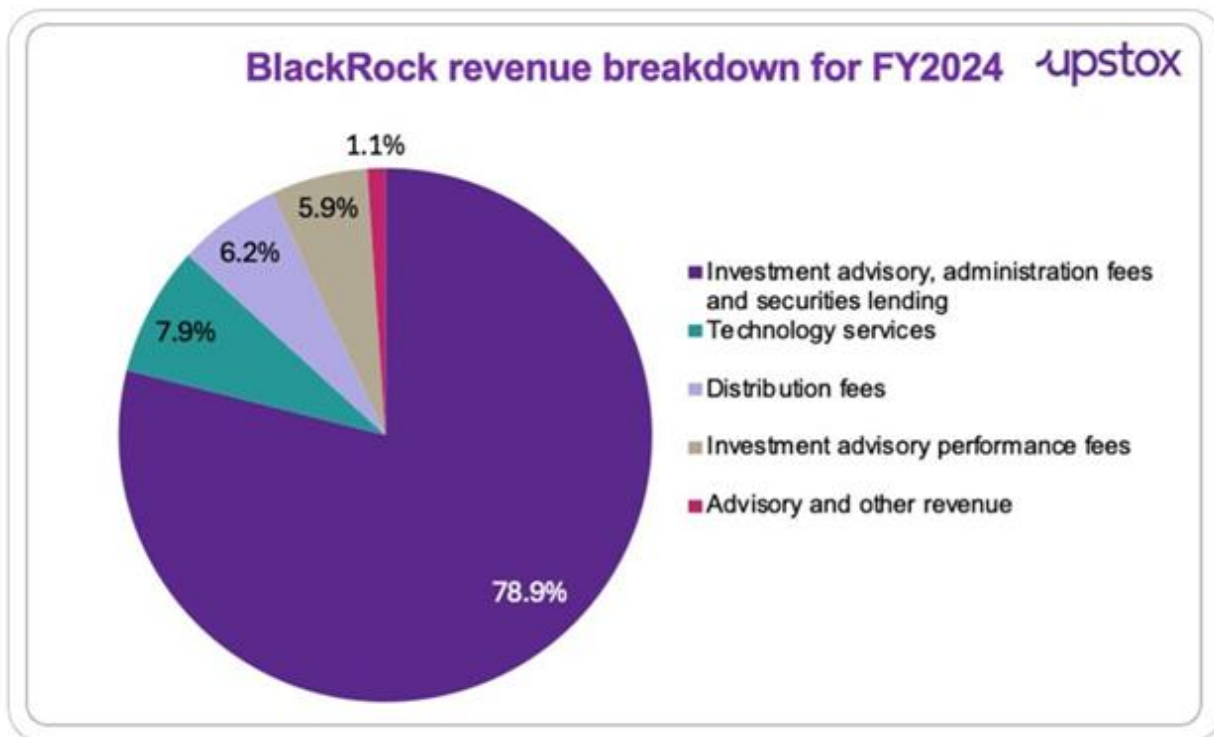
The Revolving Door

Another feature to their political role is the "revolving door" between asset management and government. BlackRock officials, for example, have moved to senior roles in the U.S. Treasury, European Union institutions, and central banks. Brian Deese, former worldwide sustainable chief at BlackRock, in 2021 became the Director of the U.S. National Economic Council. Similarly, within the European Union, BlackRock has been chosen to advise the European Commission on sustainable finance, despite concerns about conflict of interest. These are signs of how the professional experience of the assets managers allows them to exert influence over policymaking even at the very highest political levels.

Privatized Public Activities

The influence of asset managers goes beyond lobbying and personnel. In times of crisis, governments and central banks have often turned to BlackRock for advice and operational support. During the COVID-19 pandemic in 2020, the U.S. Federal Reserve hired BlackRock to help administer its bond-buying programs, including purchases of corporate bond exchange-traded funds (ETFs). At the same time, the European Union also sought BlackRock's advice on sustainable investment rules. Critics point out that these advisory roles give the firm access to sensitive policymaking processes while it continues to manage large investments in fossil fuels, banks, and other regulated industries. This has raised concerns that public functions are being —privatized in ways that benefit one dominant player.

The following figure presents BlackRock's revenue breakdown for FY2024, highlighting the firm's diversified business model and its sources of influence.



Source: BlackRock.com, via Upstox

The "Shadow Government" Critique

As a result of this combination of lobbying, revolving doors, and advising, companies such as BlackRock have been characterized by some scholars and policy-makers as forming a "shadow government." They are neither directly elected nor accountable in an election-based system but their recommendations and decisions impact millions of citizens ranging from pensioners to consumers of products and services. Through exercising control over massive capital pools, advising at central banks, and exercising influence on corporate governance, asset managers are in a position to influence market forces and public policy in an interfading combination of private and public authority. This critique raises fundamental queries on accountability and transparency in modern capitalism.

Comparison with Previous Eras

This present ascendancy of asset managers has even been likened to other periods in U.S. financial history. In the early 20th century, J.P. Morgan exerted vast powers over the system. Before the establishment of the Federal Reserve in 1913, Morgan personally orchestrated bailouts of banks in crises using his private fortune and networks. These "gentlemen's

agreements" showed how private agents effectively could be regulators of last resort. BlackRock and its colleagues today exert an analogous influence on an infinitely greater and global scale. As J.P. Morgan's ascendancy led to the establishment of the Federal Reserve System, the expanding influence of the asset managers might yet encourage governments to reevaluate the separation of private and public authority (Braun, 2020).

Conclusion

The political economy of asset management reveals these firms to be more than mere financial intermediaries. By lobbying, personnel movements, and consulting contracts, they influence regulation and public policy to an extent that challenges democratic accountability. Their experiences in crises such as that of COVID-19 amplify their significance but betoken dangers of relying on private companies for public services. Histories of comparable concentrations of influence in earlier periods, such as by J.P. Morgan, are available to illustrate how recent this concentration is. Policymakers face the task of reconciling the virtues of the expertise of the asset managers with restraints so as to avoid an excess of private influence in public decision-making.

VII. ESG, Stewardship, and Universal Ownership

In the last couple of decades, environment, social, and governance (ESG) investing went from a niche strategy to a global finance mainstream approach.

Large fund managers, such as BlackRock, Vanguard, and State Street, have been called "universal owners." Because they hold diversified portfolios in nearly every part of the economy, they confront systemic risks, which affect the entire market. Climate change, pay inequality, or corporate transgressions might lower the aggregate value of their holdings. It provides these companies with a motivation for examining the performance of the constituent company but, moreover, the broader economic and social impacts of investments (Bebchuk & Hirst, 2019). By taking account of ESG issues in investments, universal owners attempt to secure long-run returns and promote sustainability across the market.

There are indications of ESG activism in a few forms. Asset managers file shareholder proposals, engage in talks with boards, and employ climate-risk hedging policies to push companies to reduce carbon emissions or upgrade labor standards. Major funds, for instance, have pushed energy companies to release climate risks and transition toward more resilient business models. Such efforts indicate asset managers' role not merely as passive investors but active company guardians in whose names they own stakes. However, there have been criticisms of ESG investing, as well.

Some scholars suggest ESG policies amount to little more than window dressing rather than

prevention of stronger regulation or public criticism. Large asset managers have shown a tendency to shy away from voting against executive pay or holding stocks in fossil fuels, challenging the effectiveness of ESG engagement. There is risk, critics warn, of ESG intentions amounting to little more than symbolism rather than substance absent real enforcement and accountability.

Transitions between generations have also been key in propelling ESG demand.

Millennials and young investors care deeply about social and environmental responsibility, and they're pressing asset managers for opportunities in sustainable investing. Their urgency has accelerated the integration of ESG into core portfolios, and in the future, sustainability will be at the center of business and investing strategy rather than on the perimeter.

Together, stewardship and ESG investing encapsulate both opportunities and challenges of modern asset management. Universal ownership is an influential catalyst for large funds to consider systemic risk, and we see many embracing discussion with firms in pursuit of promoting ESG targets. Critics of weak voting records and token gestures, in turn, remind us that promise of ESG is not always fulfilled. Will the future witness sustained pressure from investors, regulators, and future generations, getting ESG strategies to deliver real economic and social change?

VIII. Comparative Systemic Risks: Asset Managers and Banks

The 2008 Financial Crisis underscored the ability of banks to create systemic risk.

Banks had become extremely reliant on leverage, borrowing extensively in order to fund their business. As the housing bubble burst, the resulting large leverage multiplied losses, resulting in insolvencies of major banks. Transparency of their balance sheets and interdependent derivatives complicated assessments of risk by regulators and investors. These conditions resulted in the collapse spreading rapidly throughout the entire financial system, eventually needing government bailouts in order to avert a larger economic catastrophe.

Asset managers operate differently, though. Their leverage is typically lower, since mutual, index, and ETF funds depend more on customer deposits than on borrowed money.

That difference placed the asset managers, initially, in favorable risk comparison, from a perspective of financial stability, to banks. However, research and more recent developments suggest asset managers will continue producing systemic risk, though through different channels. One of their key weaknesses is the risk of liquidity mismatch. Open-ended funds typically grant investors the right of rapid redemption of shares, while keeping less liquid assets, such as

corporate or municipal bonds. Under stressful conditions, large-scale redemptions will encourage funds to divest assets very rapidly, creating "fire sales" which drive prices down and affect markets more broadly (IMF, 2015).

Another source of risk is size and concentration. Mega-asset managers such as BlackRock, Vanguard, and State Street control enormous parts of global equities and bonds. Their buying and selling have the ability to shift markets by the sheer volume of assets under administration. And passive investment flows—index funds and ETFs—can amplify market movements further. If there are several funds replicating the same indices, buying and selling pressure can create price dislocations, a phenomenon whereby prices have no underlying fundamentals. By sheer virtue of this, asset managers, even unlevered, can influence asset prices and bring about system-wide ramifications.

Governance influence is also at play. Since big asset managers vote on behalf of millions of investors, at scale, they have the ability to shape corporate behavior, and thus, entire swaths of the economy, in a similar manner to the lending and investing choices of banks, which can have sweeping impacts. While this is usually presented in the guise of stewardship, this equally creates the possibility of concentrated power that can amplify financial shocks.

The COVID-19 outbreak presented an overt example of similarities between banks and asset managers in the sense of "too big to fail." During 2020, when bond markets froze up, the Federal Reserve stepped in by buying corporate bond ETFs, many of which were owned by the biggest asset managers. It underlines the fact that, just as banks were backstopped in 2008, giant asset managers can be backstopped in the event of systemic strain, demonstrating their value to financial stability.

These evolutions imply a new systemic perimeter for regulators. Although banks continue to be important, asset managers have become larger, more interconnected, and influential, and cannot be overlooked by regulators anymore. Generic bank-centered frameworks lack a proper capture of large investment fund specific risks, such as liquidity mismatches, passive flows, and concentration of governance. Managing these risks implies both microprudential practices (e.g., liquidity control and stress tests) and macroprudential oversight taking into account system-wide ramifications.

In short, though asset managers fundamentally differ from banks, their scale, market influence, and business models can create risks negatively impacting financial stability.

History from the 2008 crisis thus verifies the danger of underestimating vulnerabilities at the system level, while subsequent trends, up to and including 2020 Fed interventions, suggest asset managers now belong in the same "too big to fail" group. Regulators accordingly need to accept

asset management as a core of the new landscape and derive policies suited to its own risk profile.

IX. Policy and Reform Choices

The development and concentration of big asset managers have raised concerns and calls for reforms to mitigate systemic risks and maintain financial stability. Policymakers can regulate these risks through a framework of microprudential instruments, macroprudential supervision, market reforms, and structural reforms.

Microprudential Tools

At the firm level, microprudential tools can be used by regulators to enhance resilience. Stress tests at the fund level can model severe market conditions in order to determine how lone asset managers would survive shocks, such as mass redemptions or sudden drops in asset prices. Enhanced data collection enables supervisors to keep track of portfolio composition, liquidity, and exposure to illiquid assets. Comprehensive liquidity rules can provide assurance that there will be enough liquid assets in place at the funds so as to satisfy investor redemptions, and thus limit the possibility of "fire sales" potentially destabilizing markets (IMF, 2015).

Macroprudential Oversight

In addition to the level of individual firms, regulators require macroprudential oversight of system-wide risks. It targets interlinkage between several asset managers and markets, including the influence of passive fund flows and concentrated ownership. Sectoral buffers, analogous to bank capital buffers, might buffer shocks in a few markets, e.g., municipal debt or corporate bonds, which are significantly impacted by large funds. Macroprudential policies seek mitigation of localized risks' contagion across the entire financial system.

Market Structure Reforms

Structural market structure revisions may also limit vulnerabilities. Swing pricing and redemption fees, for instance, change fund share prices at the moment of mass redemptions, which discourages first-mover benefits and shields other investors. Securities lending limits—funds lending securities for additional compensation—can minimize interconnectedness and latent risks. All these collectively enhance the stability of investment funds and diminish chances of systemically important crises prompted by fund behavior.

Ownership Limit and Network Separation

Excess common ownership, in which several asset managers own significant stakes in rival firms,

may impact corporate governance and competition. Antitrust-type regulation or ownership limits might keep undue concentration at the level of firms or industries in check. Moreover, structural severability of key platforms, including BlackRock's Aladdin system, from fund managerial activities might contain operational risks. By decoupling infrastructure services from asset managerial choices, regulators might contain conflicts of interest and undue concentration of the system risk at the level of a firm.

Global Coordination

As asset managers control assets worldwide, risks become cross-border in nature.

There is a requirement for coordinated international action so as not to leave gaps in regulation. International authorities such as the Financial Stability Board (FSB), International Organization of Securities Commissions (IOSCO), and IMF can set forth standards of fund liquidity, stress tests, and disclosure. Supervision at a coordinated level ensures large asset managers will not capitalize on disparity between national regulation and ensures global financial stability is maintained.

Conclusion

Asset management policy and reform decisions involve firm-level solutions, system-wide regulation, and structural reforms. Microprudential tools of stress tests, macroprudential oversight, and market reforms through redemption fees strengthen the resilience of funds.

Structural separation and ownership caps address concentration and operational risk. Finally, international cooperation ensures global asset managers will be subject to the same standard.

All these policies collectively can maintain the benefits of large asset managers but limit the system risk these asset managers impose over worldwide financial markets.

X. Conclusion

Restating the Paradox

Asset managers have come to the heart of finance, promising investors diversification, professional expertise, and global market access. Mutual, index, and ETF funds give individuals exposure to capital markets at minimal cost, relative to old-line banking firms, and bring stability through diversification and pooling of assets and risks. Yet, the decentralization of power into a handful of gigantic firms, in this case, BlackRock, Vanguard, and State Street, creates new system vulnerabilities. Although these firms, by virtue of their size, market power, and interlinkage, serve as natural stabilizers, shocks may be enlarged, and risks of the kind created by

banks in earlier crises may be engendered (IMF, 2015).

Major Risks

Some significant risks arise from the control of large asset managers. Initially, open-ended fund liquidity mismatches create vulnerabilities. Funds offer investors a guarantee of rapid redemption of shares, while maintaining less liquid assets, which cannot be sold fast without encountering market prices. It can contribute to first-mover advantages and fire sales, transmitting their effects throughout markets. Second, horizontal shareholding or common ownership allows a few firms to dominate large stakes of competitors, and this might reduce competition and affect corporate governance. Third, asset managers' control over policymakers and central banks demonstrates the possibility of political capture. By lobbying, revolving doors, and advisory services, asset managers can shape regulation and public policy, which might facilitate their business objectives but affect the overall economy (FSOC, 2013).

Scale, Focus, and Interconnectedness It's good to keep in mind, though, that risk is not solely facilitated by scale. Even though the Big Three are enormous, their system risk depends on the way they operate, what assets they own, and the extent they remain linked to markets and infrastructure. Risks occur wherever incentives, fund structures, and operating linkages come together to amplify shocks. Herding, crowded trades, and use of key platforms like BlackRock's Aladdin serve to illustrate vulnerabilities derive from interlinks and concentration, not scale by itself. It's important to understand the distinction so we may introduce the appropriate sort of regulation into the equation.

Prospective View

The long-run stability of worldwide finance relies on reforms geared toward dealing with these structural weaknesses. Microprudential policies, including stress tests, liquidity requirements, and enhanced data collection, can make firms stronger individually.

Macroprudential control, including system-wide surveillance and sectoral buffers, can control contagion risks. Redemptive fees, swing pricing, ownership limits, and the severability of important infrastructure can avert over-concentration and conflicts of interest at the level of the firm. Lastly, global cooperation ensures cross-border risks are controlled uniformly, due to the international activities of key asset managers.

By managing concentration, incentives, and interconnectivity, regulators can enable asset managers to keep delivering diversification and stability without bringing in the vulnerabilities typical of earlier banking crises. It's a lesson learned: progressive reform is needed to make the evolution of asset management a source of strength and not the eventual trigger of the next

systematic jolt.

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