



GLOBAL REGULATORY REFORMS

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FELABAN, IDB, ASBA Public Sector-Private Sector Dialogue

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Outline

I. **What** went wrong?

II. **Where** do we need to go?

III. **How do we get there** – **how far** have reform polices come?

IV. **What more** needs to be done?

I. WHAT WENT WRONG?



What went wrong?

Conditions present
for a perfect storm

MACRO

- Very low interest rates
- Abundant liquidity

OVERSIGHT

- Inadequate regulation
- Weak supervision
- Weak resolution tools

FINANCIAL SYSTEM

- Highly complex and opaque
- Poor risk management
- Too-important-to fail aura

Supervisory vulnerabilities

- **Too complacent** – not sufficiently intrusive/skeptical
- **Not proactive** in dealing with emerging risks; did not adapt
- **Not comprehensive** in scope
- **Weak** follow-up

Financial sector vulnerabilities

Complacent risk management:

- Low lending standards
- Aggressive risk taking (high profit targets & remuneration)
- Low provisions
- Heavy reliance on wholesale funding
- High leverage

Result:

- Under-pricing of risk => Low capital and provisions
- Aggressive expansion
- Risk concentrations
- Vulnerable liquidity position
- Some comfort in “TITF”

II. WHERE SHOULD WE BE HEADED?



GOAL: More reliable financial system that supports sustained growth

- More resilient financial institutions
- Globally consistent regulatory standards
- More transparency
- Better oversight of non-bank and “shadow banking” sectors
- No TITF/TBTF institutions

III. HOW DO GET THERE?



How do we get there?

A. Tightened prudential **regulations**

B. More effective **supervision**

C. Robust **resolution** frameworks (TITF)

D. **Macro-prudential** (systemic) dimension

A. Tightened prudential regulations

Objectives:

Increase the quantity and quality of capital

More bank liquidity and more stable funding

Reduce concentration risks

Status of tightened regulations:

Increase the quantity and quality of capital

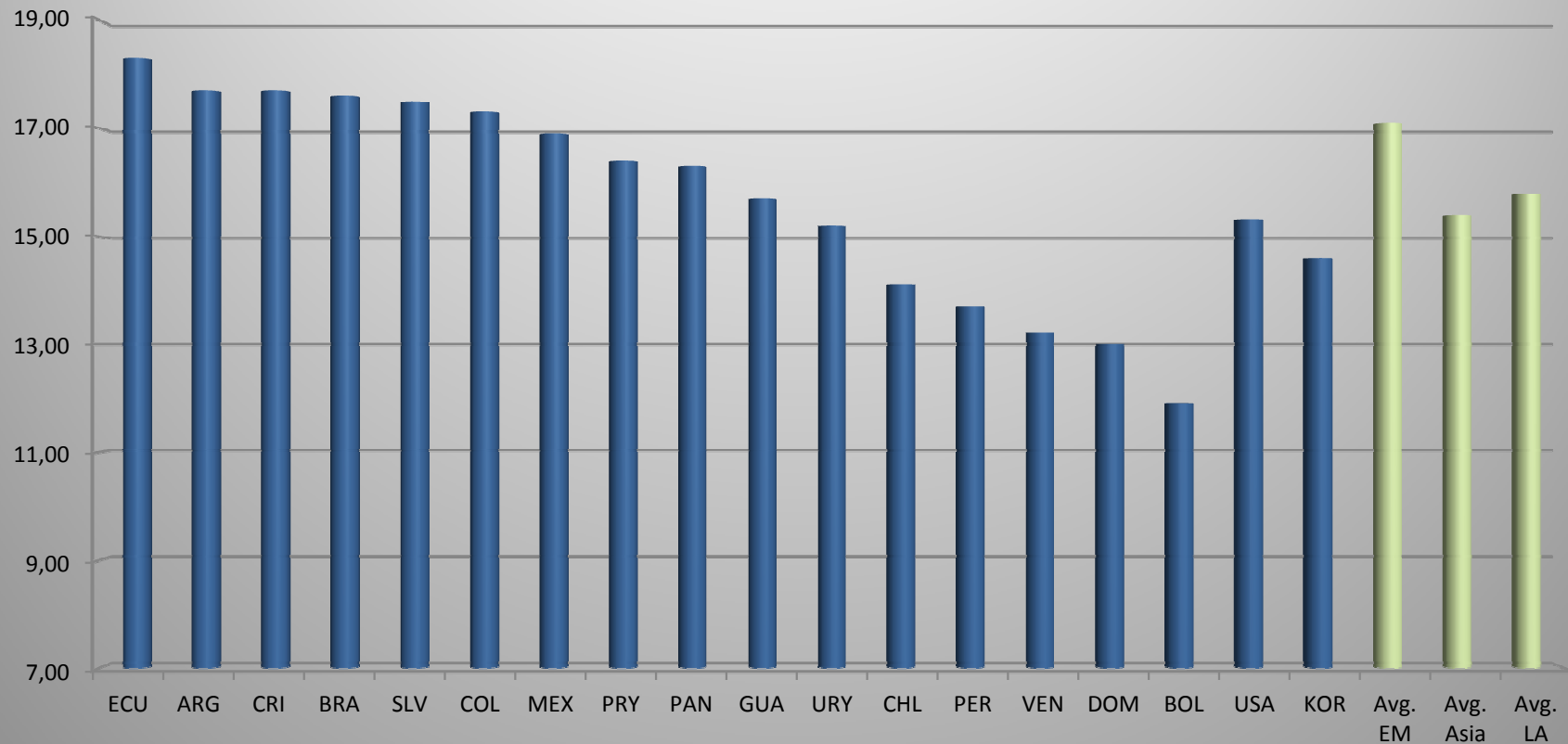
- Increase Core Tier 1 ratio
- Introduce capital conservation buffer
- Leverage ratio
- Phasing out of hybrids & subordinated debt

More liquidity and more stable funding

- Banks to hold more high quality assets to meet short-term stresses
- Net stable funding ratio (more long-term funding; better matching of asset and liability)

Strong capital base in region

Regulatory Capital as a Share of RWA, 2010
(In percent)



Source: IMF's FSI Website

Issues:

Risk weight for sovereign debt

- When should an asset be considered zero credit risk?

Concentration & leverage limits

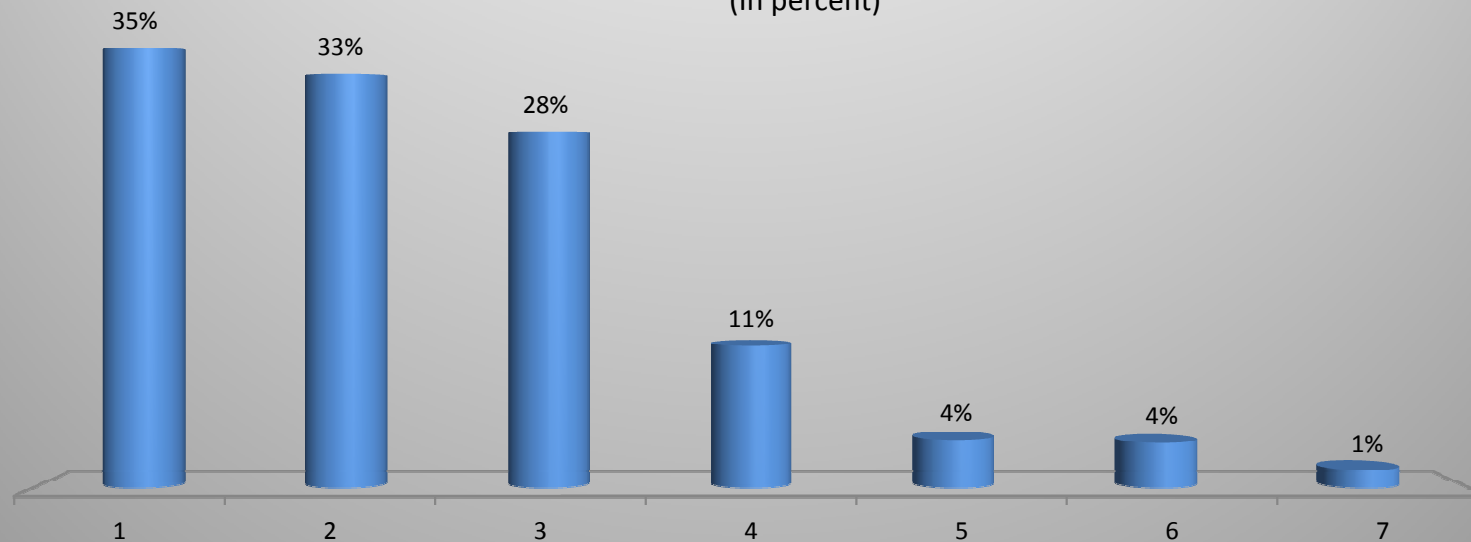
- No international standard yet in place

Challenge of recalibration

- Use of models -- reassessing relative risk among asset classes

In some Latin American countries, significant exposures to Government

Claims on Central and Local Government Compared to Bank Assets,
2010
(In percent)



Source: BCRA, BCB, International Financial Statistics (IFS) and IMF's FSI Website

B. More effective supervision

Issues:

- Regulations only as good as their implementation
- Supervision needs to be comprehensive
- Cooperation across supervisors

Guidance & Principles:

- **FSB: *Recommendations for improving the Intensity and Effectiveness of Supervision*** (Nov. 2010)
- **IMF: *The Making of Good Supervision, Learning to say No*** (May 2010)

Instruments to promote strong supervision:

- Technical assistance to supervisory agencies
- Financial Sector Assessment Program (FSAP)
- Self assessments, peer reviewed on a global basis

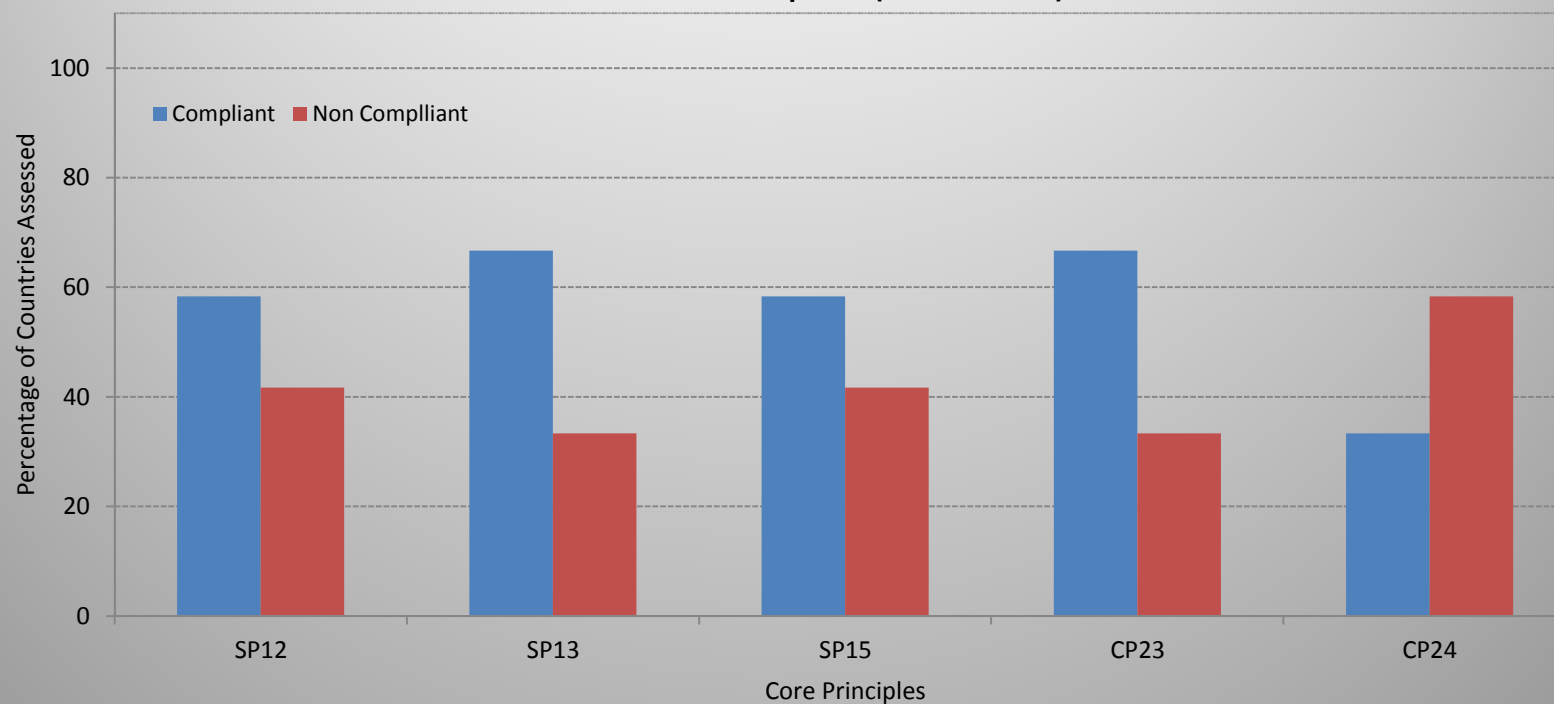
Strengthening supervision principles

Ability and will to act

- Legal authority & operational independence
- Clear and unambiguous mandate
- Adequate resources
- **Skilled senior experienced staff**
- Accountability
- Effective working relationships (cooperation) with other agencies
- A healthy relationship with the industry

Bank supervision has a number of strengths but some gaps remain

Compliance with selected BCP Principles of Banking Supervision
Western Hemisphere (2006 Version)



SP1.2. Independence, accountability and transparency of the supervisor

SP1.3. Legal framework

SP1.5. Legal protection

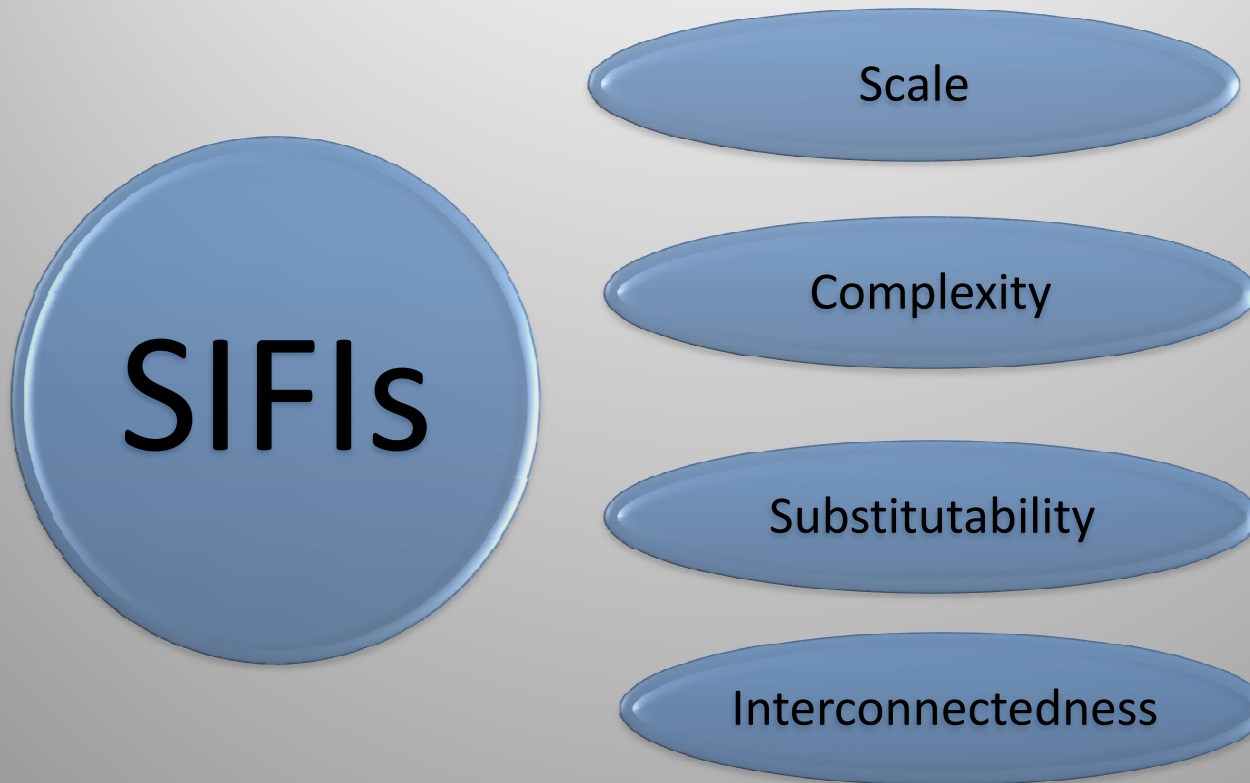
CP 23 Corrective and remedial powers

CP 24 Consolidated supervision

C. Robust resolution frameworks

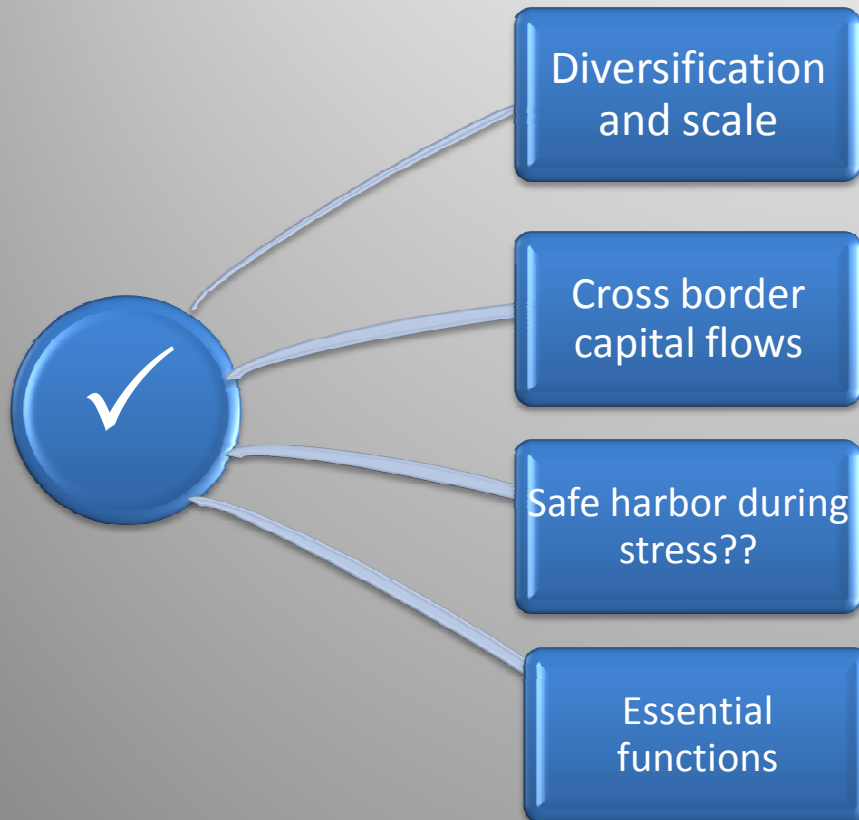
- Effective resolution framework and authorities
- Credible tools to resolve a TITF institution
- Cross-border cooperation & coordinated solutions
- Recovery and resolution plans (RRPs) for all Systemically Important Financial Institutions (SIFIs)

SIFI failure can disrupt the financial system

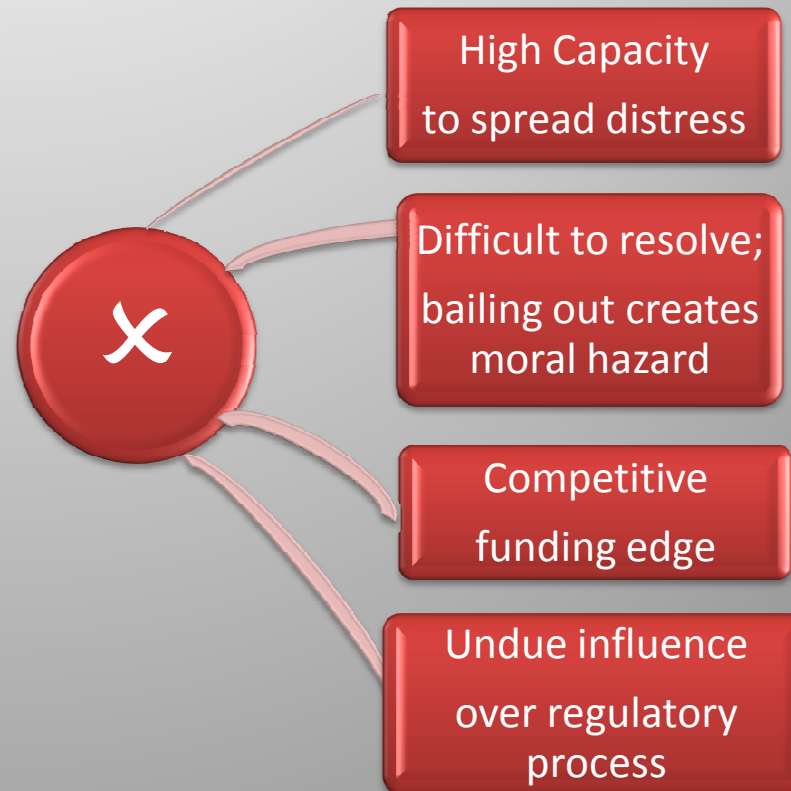


Understanding SIFIs

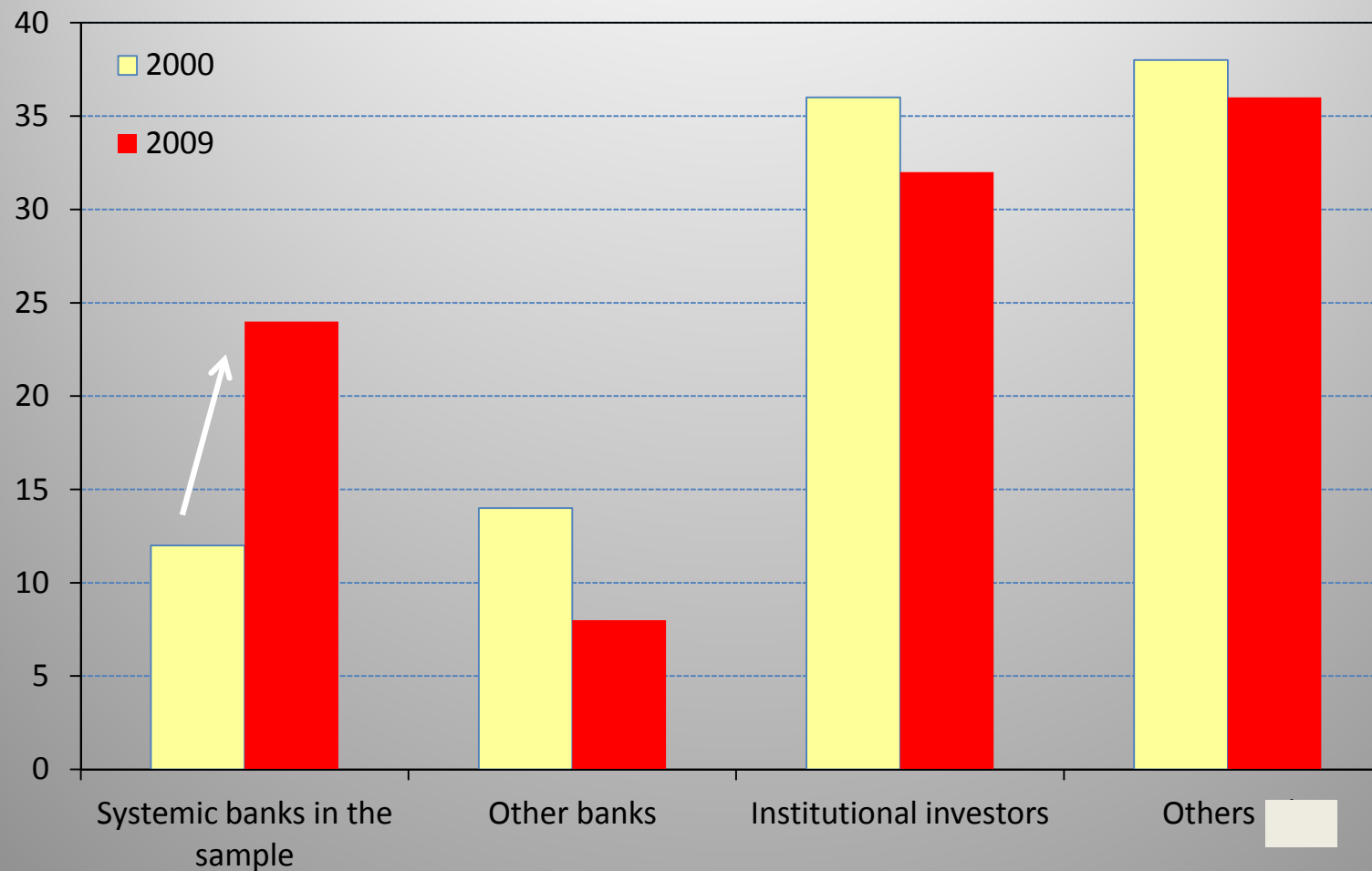
Positive attributes



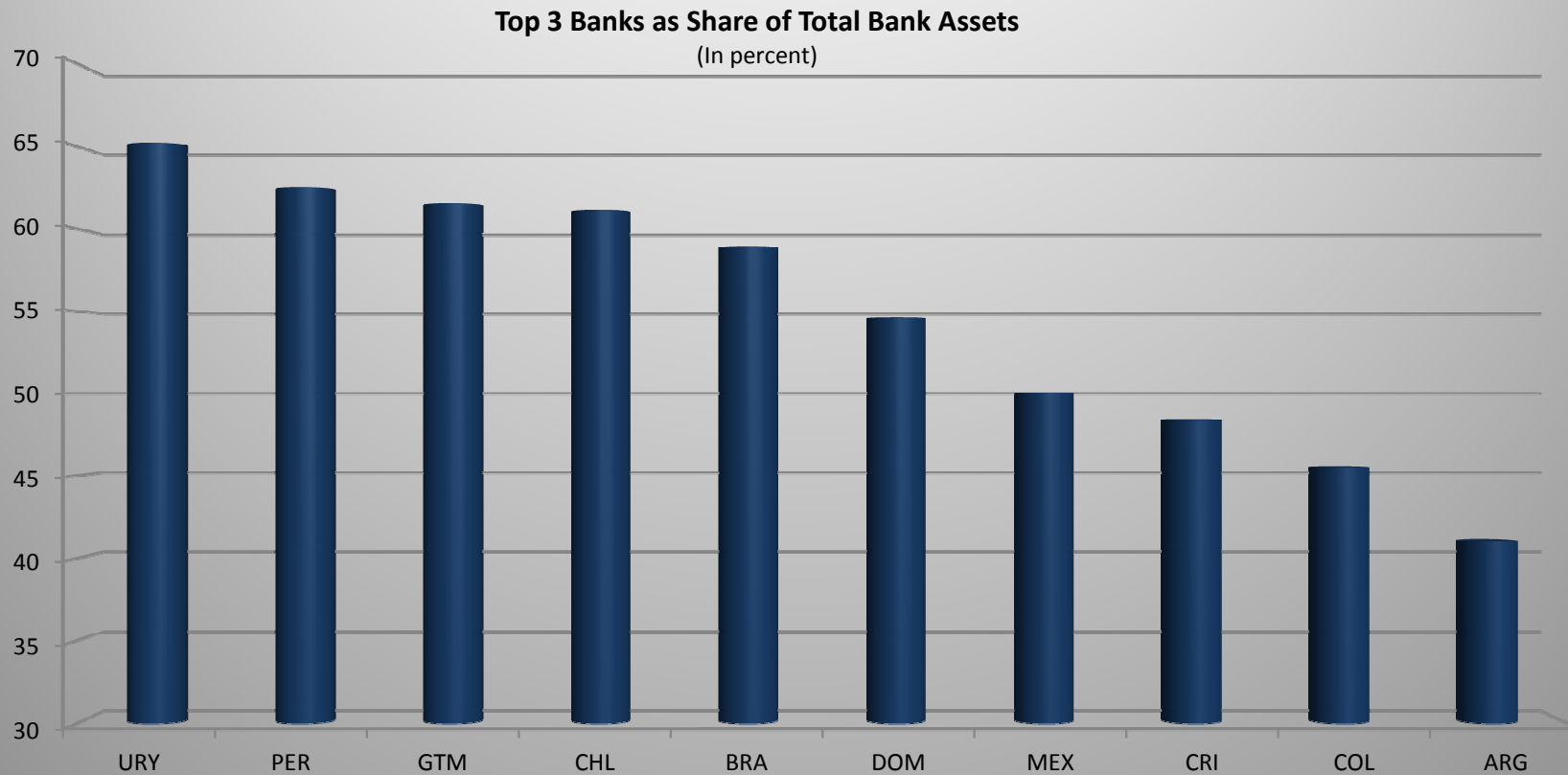
Risky attributes



SIFIs' share of the global financial system has doubled

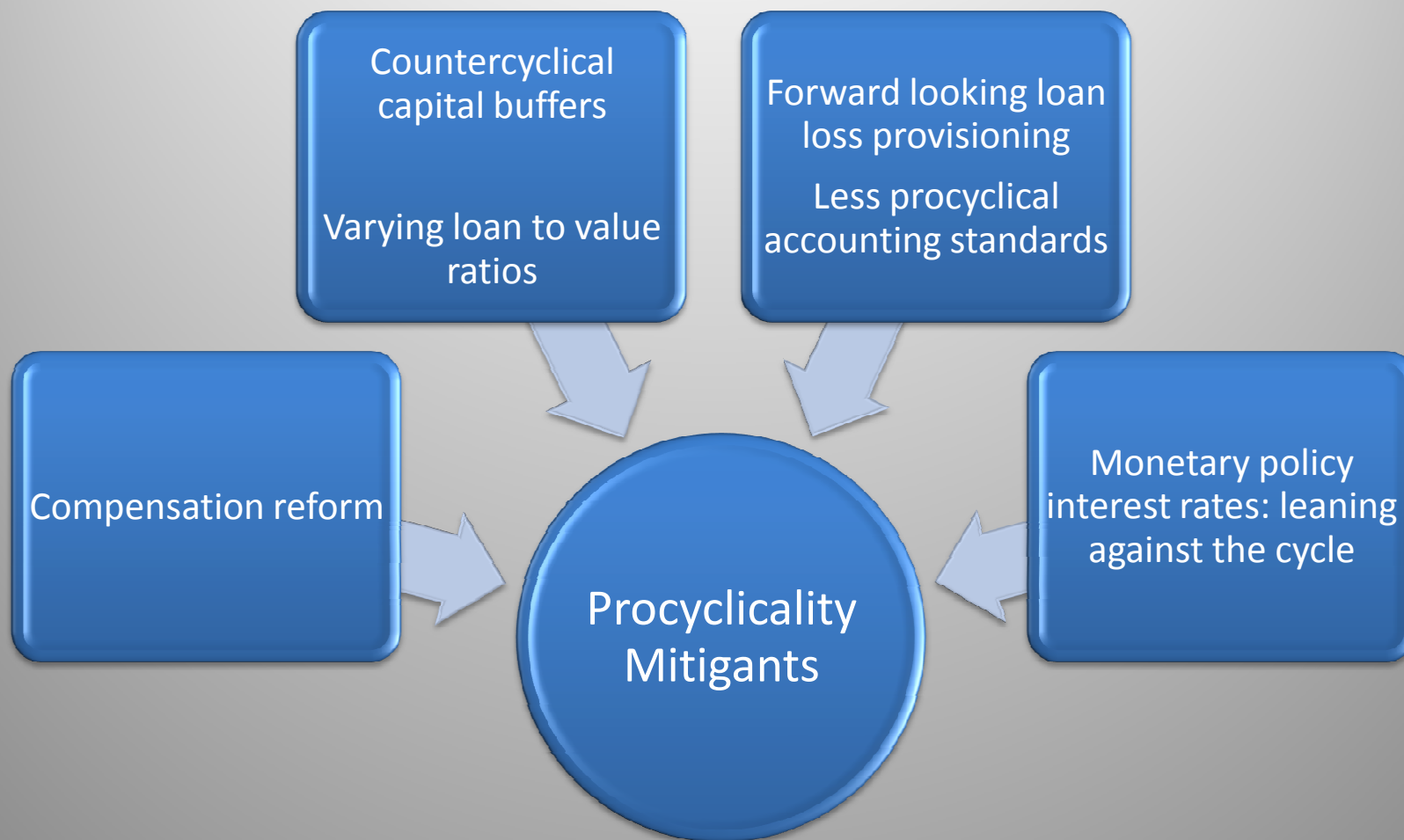


Throughout region, banking systems are very concentrated



Source: Bankscope (2009 data)

D. Macro-prudential dimension



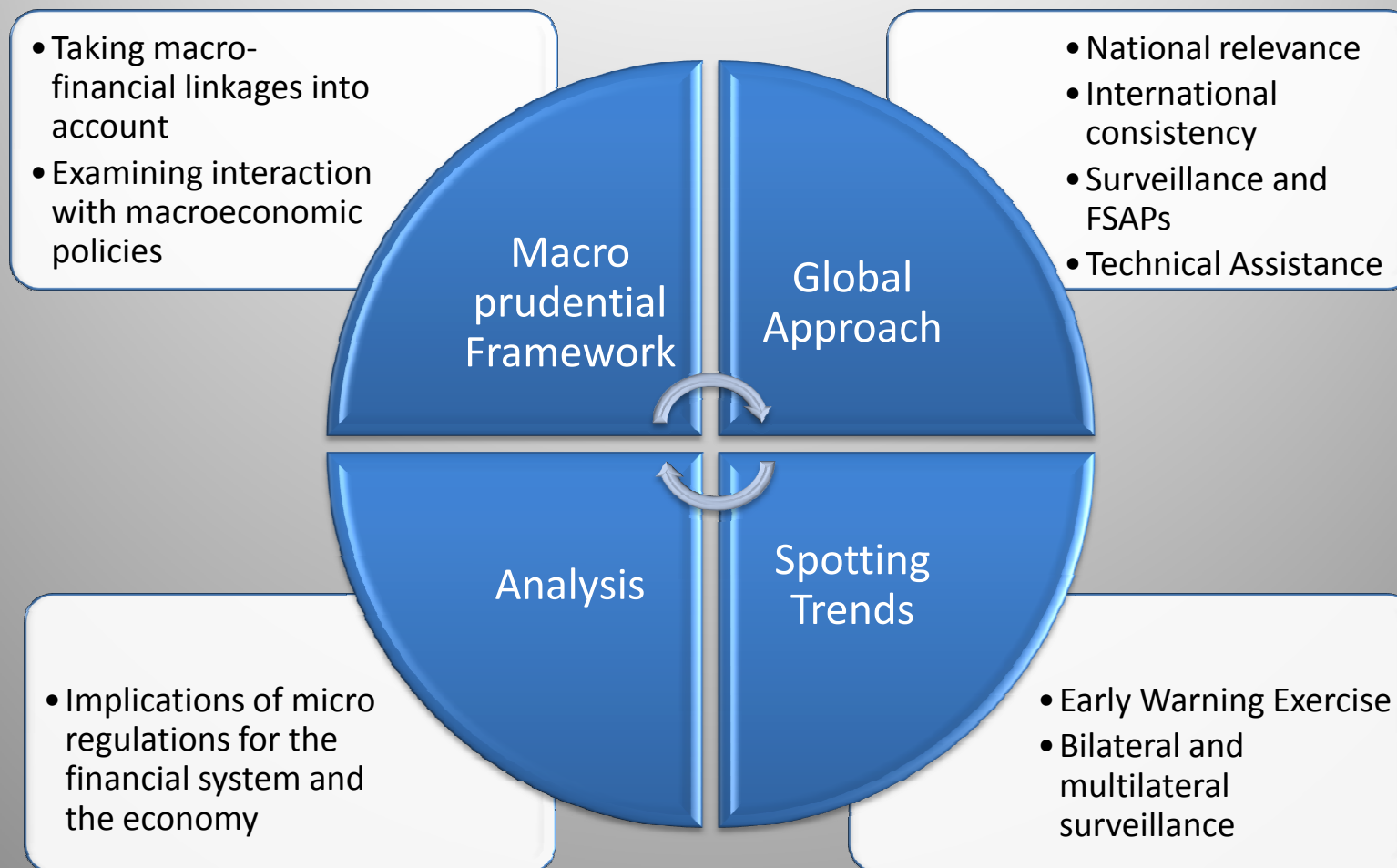
IV. WHAT MORE NEEDS TO BE DONE?



Overall progress... but more challenges ahead

- How to improve governance and risk management capacity of SIFIs?
- How to ensure a level playing field in regulations?
- How to improve quality of supervision?
- How appropriate is the current RWA regime?
- How to reduce risk of TITF while keeping benefits of national and global institutions?
- How much capital is enough?
- How to develop coherent resolution mechanisms, at a national and cross-border level?
- What does a comprehensive macro-prudential framework entail?
- How to address shadow banks?

IMF contributions





Thank you

