

Comment on “Promoting International Financial Stability: The Role of the BIS,” by William R. White

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I would like to begin with underpinning the main aspects of Bill White’s presentation, which tackled the issue of financial stability as a whole. I will then focus on the way in which the Basle Committee contributes to addressing the issue of financial stability.

Financial Stability: The G-10’s Response

Given the prominence of financial markets in the globalisation and de-regulation process, it is worth underlining the increasing responsibilities of central bankers and other regulators, who are often closer to the markets than governments. Moreover, financial stability has become one of the major priorities for international organisations, although the more traditional macroeconomic preoccupations remain an area of considerable concern as well. In short, monetary stability and financial stability are the “two sides of the same coin”, thus justifying the central bankers increasing involvement.

The strategy to promote financial stability has taken place within the G-10 Deputies Report proposals, which were released last year. In this respect, it is important to highlight that the strategy has to be global – involving developed and emerging markets – and that those overseeing the policy have to endorse new responsibilities in order to reflect the required complementarity between market discipline and regulatory oversight. It induces a strong cooperation between policymakers from different countries as well as an increasing involvement of both public sector and private sector participants.

In this context, the BIS has demonstrated that it has many assets to enhance international cooperation. For years, it has been the best place for G-10 central bankers to meet, and its role is being extended to emerging countries. It is a talking shop where national experts have become used to a high level of cooperation. The Committees wherein this work has taken place have dealt with topics related to the three “pillars of the financial

system”, that is: (i) the financial institutions; (ii) the financial markets; and (iii) the payments and settlements systems.

The cooperation between the Committees dealing with these three issues has led to crucial decisions with significant international implications. However, we should avoid understating past shortcomings nor keep silent regarding the future challenges the BIS will have to face. One such challenge is that the trend of enlarging the number of participants (mainly including more emerging countries) and the maintenance of a club-like atmosphere (which has proven very efficient up to now) will have to be reconciled. Other challenges I would like to emphasise are: (i) the far-reaching consequences of the vanishing barriers between different markets and different financial institutions, requiring the different supervisors to set up adequate communication links; and (ii) the growing influence of the business community, which is primarily responsible for avoiding possible failures on financial markets.

Regarding the specific measures the Basle Committee has taken to promote financial stability, I will focus on the first “pillar” and on the Basle Committee which, to my mind, implements the relevant approach towards improving efficiency in all the topics under review. This will lead me to focus on: (1) the dissemination of universal principles for banking supervision; (2) the initial outcomes of the international supervisory cooperation on financial conglomerates; and (3) the development of current prudential issues.

Core Principles for Sound Banking Supervision

The trend of extending the influence of the BIS standards to the non-G-10 countries – especially the emerging countries – and of welcoming them as participants in the standardisation process, is a major challenge for the G-10 and, therefore, also for the BIS. The strain on the banking system, which several major emerging countries are currently witnessing, reinforces the necessity to address this issue. The 25 “Core Principles for Effective Banking Supervision” is the first remarkable outcome of a global action, involving the main multilateral institutions. It establishes a universal standard for creating a sound supervisory environment.

The purpose of these achievements – to promote the Principles and to monitor the responses to their implementation – and the way they have been elaborated, rely on the cooperation between G-10 and non-G-10 countries, as well as between the BIS, the IMF and the World Bank. The BIS has monitored the conception process and has the leadership role in the promotion of the principles through the Liaison and the Consultation

Groups. The IMF and the World Bank instead have focused on the implementation of these principles. Such a joint action ensures the legitimacy and the enforceability of the resulting standards. Combined they form a strong leverage for financial stability. To summarise, on a global and cooperative basis the Basle Committee has managed to set a universal standard, within a reasonable time period, and has provided the practical tools to promote its implementation.

The Core Principles are not only a successful example of a widespread cooperation, but they also ensure the progressive shift from basic quantitative prudential standards – to be enforced by the banks – to global ones, including both qualitative and quantitative criteria, involving the banks and other participants (mainly the supervisors). All of these elements are critical in reaching the target of financial stability which encompasses many different concerns: financial, organisational or institutional, all of which require a global oversight.

The BIS has clearly demonstrated that these achievements do not result from a short-term strategy, but that they are a permanent response to the present challenges. The BIS has planned to set up, towards the end of 1998, a Training Institute for Financial Stability, which will provide assistance to G-10 and non-G-10 supervisors concerning either banking or non-banking issues.

Cooperation Between Supervisory Institutions and the Leadership of the Basle Committee on Prudential Issues

As we have seen, the cooperation has improved between G-10 and non-G-10 countries, as well as between the major institutions which are involved in promoting financial stability. Nevertheless, the cooperation process may require further efforts. Indeed, the barriers have fallen between the actors of the different financial market segments, i.e. banks, insurance companies, and other financial institutions. However, on the regulators' and supervisors' side, adequate cooperation remains to be improved. Realising this, the joint Forum on Financial Conglomerates, in which the Basle Committee, the IAIS and the IOSCO operate jointly, tackles the following issues: (i) appraisal of a conglomerate capital adequacy on a group basis; (ii) information-sharing between supervisors and an easing of legal impediments; and (iii) coordination of supervisors' actions, as well as identification of the main coordinator.

We must acknowledge that this process has been a long-standing one. One may point out here the weakness regarding the process of addressing the Herstatt risk issue. Even having taken into account the complex techni-

cal background, the practical outcomes may appear minimal at the moment. As a matter of fact, the pending legal impediments concerning information sharing remain an obstacle.

It is clear that, as a talking shop, and in its role of creating consensus, the BIS structures have reached a limit in terms of their influence on national regulations. Nevertheless, as barriers have fallen throughout the financial markets, the different regulators will acknowledge that a joint action on common concerns is necessary. In that respect, the in-depth research and the consistency of the works-in-progress under the aegis of the BIS are the essential factors from which to expect some practical outcomes in the long term.

Obviously, the Basle Committee's works do not encompass only the international and trans-sectorial cooperations. Despite the fact that the mandate of the BIS, and of its hosted committees, does not include the direct management of crisis (e.g. in Asia), they are strongly involved with crisis management. This raises the question as to whether the BIS can practically contribute to ensure and/or restore financial stability. The answer is "yes" by all means. Hence, many of the issues which have emerged from the present crisis have been or are being addressed by the Basle Committee.

Let us just briefly point to the results of the Basle Committee's work so far:

- The creation of a practical framework for the assessment of banking internal control systems.
- The setting of principles for the management of interest rate risk.
- The introduction of market risks to the 1988 Amendment, which includes the possibility to use the banks' own risk measure with internal models.
- The continuous promotion of the markets' transparency and the harmonisation of accounting practices in banks.
- Finally, in addition to financial and accounting issues, the Basle Committee has extended its action to more operational matters, such as preparing the information systems for the year 2000 and the management of both electronic money and electronic banking activities.

This approach is consistent with the release of the Core Principles, since the same comprehensive approach has been implemented for the more specific workshops. As a result, a complete toolkit of best-practice standards is being created, step by step, in order to develop sound, global banking management, which is the minimum requirement to ensure financial stability.