



Research Department & Systemic Risk

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**Presentation to G20/IMF senior
officials 31 March 2011**



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Research Department & Systemic Risk

- I. Introduction
- II. Discussion Paper
- III. Research Department Work Program
- III. Hedge Funds Survey
- IV. Standing Committee on Risk and Research

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Introduction

1. IOSCO Strategic Direction

New Mission and Goals:

Identify and seek to address systemic risks to the fair and efficient functioning of markets, especially through:

- Building an independent research capacity to identify risks to the fair and efficient functioning of markets; and
- Liaising with other international financial standard setters and other global bodies having a mission complementary to that of IOSCO, applying the research capacity to inform and enhance such liaison

Introduction

2. New Principles:

Principle 6:

The Regulator should have or contribute to a process to monitor, mitigate and manage systemic risk, appropriate to its mandate.

Principle 7: The Regulator should have or contribute to a process to review the perimeter of regulation regularly.

3. The creation of the IOSCO Research Function:

- a. Independent Research Department at the Secretariat
- b. Standing Committee on Risk and Research

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Discussion Paper

1. Discussion Paper on Securities Regulators and Systemic Risk & Promotion of Financial Stability to discover the scope and the methodologies that securities regulators can use in this new task

Discussion Paper

The paper's preliminary findings are that:

1. Disclosure and transparency are critical to identifying the development of systemic risk and to arming regulators with the information needed to take action to address it. Transparency in markets and products is crucial to understanding and mitigating systemic risk, in addition to allowing market participants to better price risk. Securities regulators have a particular responsibility and interest in promoting transparency at the market level as well as adequate disclosure at the product and market participant level;

Discussion Paper

2. Robust regulatory supervision of business conduct is essential to managing conflicts of interest and the build-up of undesirable incentive structures within the financial system. Without it, incentives can quickly become distorted with drastic consequences such as increased leverage and risk in the system. With it, investor confidence is likely to provide greater stability to the market;

Discussion Paper

3. Financial innovation and its implications for financial stability should be a focus for securities regulators. Innovation should be encouraged and facilitated where it has the potential to improve the efficiency of the markets or to bring useful products and new participants to the market. Innovation which involves opacity or improper risk management should be carefully monitored;

Discussion Paper

4. Given the central role of markets in the overall financial system and their capability to generate and/or transmit risks, securities regulators should work with other supervisors to improve the overall understanding of the economics of the securities markets, their vulnerabilities and the interconnections with the broader financial sector and the real economy. Sharing market information and knowledge, will be essential to deliver a truly efficient regulatory response to systemic risk; and

Discussion Paper

5. It is important for securities regulators to develop key risk measurements relevant to systemic risk arising within securities markets, and improve their understanding and application of tangible steps to mitigate identified systemic risk.

Discussion Paper

Next Steps:

1. Kick-off of Standing Committee on Risk and Research, Chairman Carlos Tavares, early April. Main products:
 1. Creating a methodology for securities regulators about how to carry out research into systemic risk
 2. Systemic Risk indicator on specific securities market elements, especially with regard to shadow banking
2. Research Department, Head Werner Bijkerk, is currently being built up at the IOSCO Secretariat.
 1. First product will be a report on systemic risks related to Hedge Funds, based on a data gathering exercise
 2. Second product a Global Securities Regulators Risk Outlook. Research to start in April. If resources allow, report ready by end 2011, begin 2012.

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Research Department Work Program

What is it?

- The Independent Research Department (official start 1 January 2012, until then building up phase)
- A small research staff at the General Secretariat

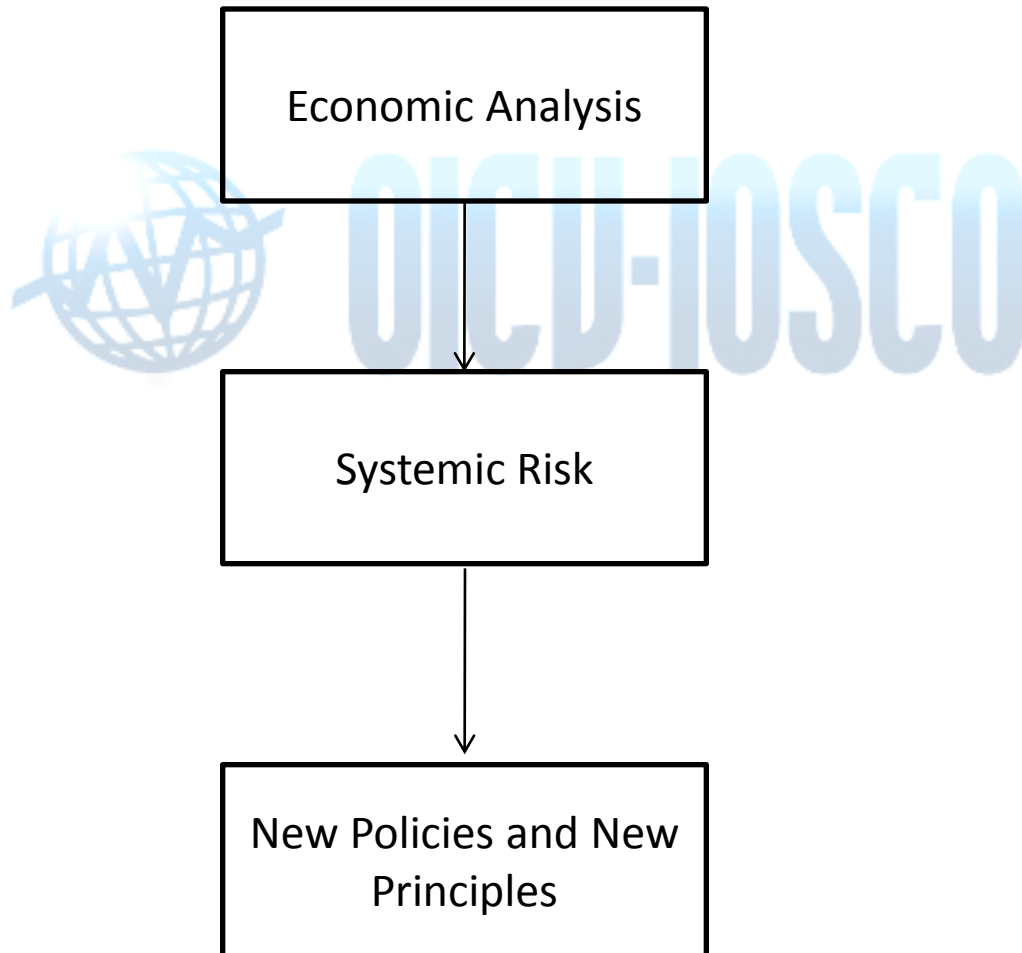
Research Department Work Program

Why does it exist?

- Created by the IOSCO membership to execute part of the Strategic Direction, especially with regard to identification and mitigation of systemic risk
- Objective fact based analyses needs to be independent from members political interests

Research Department Work Program

Why does it exist?



Research Department Work Program

What does it do?

- Build a network of internal (SCRR) and external experts (SROCC members, market, academia)
- Production of an *Annual Global Regulatory Risk Outlook* and *Exploratory Analyses* into specific risks
- Production of *Ad hoc analyses, calculations* and *data analysis*
- Helped creating Standing Committee on Risk and Research
- Helped writing of Discussion Paper

Research Department Work Program

How does it do its work?

Methodology

- Plain data analysis
 - Publicly available data
 - Shared work with other global researchers (IMF, BIS etc.) and stakeholders
- Intelligence system
 - Experts from IOSCO members (SCRR)
 - Experts from the academic world
 - Experts from other global researchers (IMF, BIS etc.)
 - Experts from the markets
 - Visits to market participants

Research Department Work Program

How does it do its work?

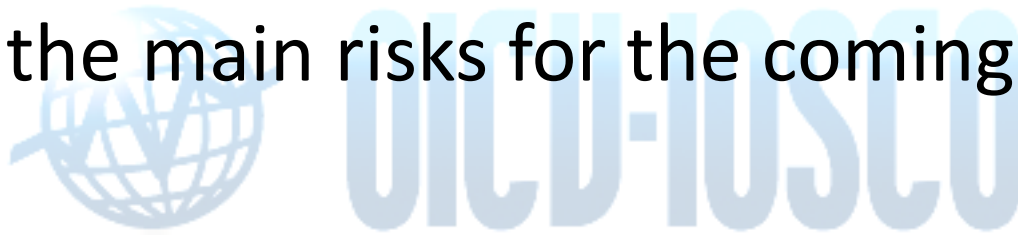
Methodology

- Production of readable, fact based reports that bring new information and insights to the public
- Written and oral input to agendas of IOSCO Policy Work, and to FSB, IMF etc.

Research Department Work Program

Annual Global Securities Markets Risk Outlook

What are the main risks for the coming years?



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Hedge Fund Survey

Research Department is actually executing a survey into systemic risk that hedge funds can pose

Task Force on Unregulated Entities (TFUE) analyzed hedge fund from 2008 onwards on request of the FSB

TFUE developed a methodology (data needs) for the survey

Delivery date first survey: Q2 2011.

Later 2011: Survey of the TFUE on implementation of the new IOSCO Principles on Hedge Funds (request of the G-20)

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Standing Committee on Risk and Research

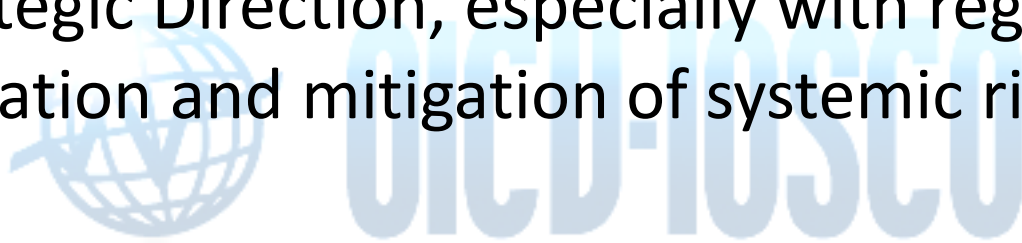
What is it?

- The Standing Committee on Risk and Research has been created by the Executive Committee of IOSCO in January 2011
- Chairman Carlos Tavares, of the Portuguese Securities Markets Regulator
- A network of 25 highly experienced economists and researchers of IOSCO members both from mature and emerging markets
- First meeting on 6-7 April in Madrid

Standing Committee on Risk and Research

Why does it exist?

Created by the IOSCO membership to execute part of the Strategic Direction, especially with regard to identification and mitigation of systemic risk



Standing Committee on Risk and Research

What does it do?

1. Development and maintenance of a research methodology for systemic risk research by securities regulators (including producing aggregate risk indicators)
2. Review of analyses and research on relevant risk assessment and interaction with external experts
3. Carry out impact assessment when requested by the Executive Committee
4. Expert input to the products of the Research Department
5. Advice on the IOSCO Objectives and Principles and the Methodology in relation to Principles 6-7