Key Messages

- Financial Architecture
  - Interconnected, concentrated

- Requires better work at “macro-level”
  - Better mapping of systemic risks
  - Strengthening of institutional arrangements for macro-prudential supervision

- But also at “micro” level
  - More effective/intrusive supervision
  - Stronger cross-border arrangements
MACRO LEVEL
Increasing Interconnectedness

Index of number of bilateral links between economies as a share of all possible links
Mapping Systemic Risk: Qualitative Tools

- Active engagement with market participants: 84.3%
- Reviewing financial institutions' strategies and business plans: 80.4%
- Analyzing trends and complexity in new products: 78.4%
- Active engagement with other stakeholders (e.g., auditors): 45.1%
- Bank survey (e.g., loan survey): 13.7%
- Market intelligence: 9.8%

Source: Cheng Hoon Lim, 2010
Mapping Systemic Risk: Quantitative Tools

Source: Cheng Hoon Lim, 2010
Mapping Systemic Risk: Network Analysis

Chile: Interbank System, January 2009

Source: Chan-Lau (2010)
Mapping Systemic Risk: Network Analysis

Chile: Interbank System, November 2009

Source: Chan-Lau, 2010
Institutional Setting

- Central Bank: 19
- Financial stability committee: 9
- Ministry of finance: 5
- Banking regulator/supervisor: 5
- Insurance regulator/supervisor: 3
- Deposit insurance agency: 2
- Securities regulator/supervisor: 1
- Integrated regulator/supervisor: 1
- Other: 2

Source: Cheng Hoon Lim, 2010
Institutional Setting

- A macroprudential authority should be designated
  - With clear powers (information collection, designation authority and calibration of other policies)
  - and a framework for accountability

- A body or other formal mechanism of coordination should be in place to ensure coordination among relevant policies to address systemic risk
Instruments and Objectives

Size, complexity, interconnectedness

Capital flow reversals risk

Currency risk

Leverage/liquidity risk

Pro-cyclicality

Credit growth/asset price inflation

Source: Cheng Hoon Lim, 200

- Capital surcharges for SIFIs
- Countercyclical provisioning
- Caps on loan-to-value ratios
- Limits on maturity mismatch
- Limits on net open currency positions
- Reserve requirements for non-residents
The choice of instruments should be based on a set of desirable features:

- Effectiveness
- Limited opportunity for arbitrage
- Aimed at the roots, not the symptoms
- As little distortionary as possible
- Low cost

A mix of rules and discretion may be optimal under current circumstances
MICRO LEVEL
Better Supervision

- More intrusive on-site inspections
  - Frequency of inspections
  - Depth of work and resources allocated
- Stronger reporting requirements
  - Currently gaps on “unregulated” entities
  - But also on regulated entities (granularity, periodicity)
- Proactive enforcement
  - Many regulators rely heavily on moral suasion
- Continue strengthening supervisory colleges