

The Sixth International Conference

“A Perspective of Asian Financial Sector under the Global Financial Crisis”

Session II Macro-prudential regulation and the perimeter of regulation

The Perimeter of Regulation

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Abstract

The global financial crisis has highlighted the need to identify and mitigate sources of systemic risk in the financial system. It has also illustrated that all types of financial intermediaries or markets are potentially systemic, with some of the key sources of risk and vulnerability in entities that were outside the regulatory perimeter.

The presentation will explain the nature of systemic risk and critical issues that should be taken into account in assessing which entities should be considered of systemic importance. It will explain the implications of these assessments for regulatory and crisis management frameworks and for extending the perimeter of regulation. In particular, different regulatory approaches and solutions can be used to mitigate systemic risk in unregulated entities. Part of the response is to enhance the capacity of the **regulated sector** to handle shocks, through reducing the probability of failures, improving resolution capacity and contingency planning, and strengthening core financial infrastructure. Part of the response is to level the regulatory playing field by regulating by functions rather than by institutional types. Part of the response is to extend the perimeter in a **graduated** manner that reflects the systemic importance of the unregulated entities. Graduation could cover reporting requirements, risk management frameworks, and capital and liquidity requirements. Entities that might be affected could include complex financial groups with unregulated components, hedge funds, credit risk transfer products and unregulated mortgage originators and lenders. A number of challenges will need to be overcome in assessing unregulated entities, and deciding when to extend the perimeter of regulation, and the presentation will outline some of the next steps that are being followed internationally.