

The Global Financial Crisis and Policy Responses

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Today's Presentation

- I. Overview of the Chronology of Events**
- II. Achievements in the G20 Seoul Summit**
- III. The report on SIFIs**
- IV. Progress on Basel III**
- V. Issues for Discussion**

Global Financial Crisis and Policy Responses- Chronology of Events

2007	22 Jun	Bear Stearns provided financial support to one of its funds
	9 Aug	BNP Paribas suspended its funds
	14 Sep	The UK government provided liquidity support to the Northern Rock (the first bank run in 140 years in the UK)
2008	22 Jan	NY State Insurance Department announced that it was considering possible capital injection to monoline insurance companies (25 Feb MBIA raised capital / 5 Mar Ambac raised capital)
	16 Mar	<u>JP Morgan acquired Bear Stearns</u>
	11 Apr	Report of the Financial Stability Forum on Enhancing Market and Institutional Resilience was submitted to the G7
	7 Sep	The US government published a plan to take over Fannie Mae and Freddie Mac
	15 Sep	<u>Lehman Brothers Holdings Inc. filed for Chapter 11 bankruptcy protection</u>
	16 Sep	<u>FRB published rescue plan for the AIG</u>
	18 Sep	<u>Six central banks including Japan, US and Europe announced coordinated measures to increase liquidity</u>
	3 Oct	<u>The Emergency Economic Stabilization Act of 2008 was enacted in the US</u>
	14-15 Nov	<u>The First G-20 Summit was held in Washington. The leaders declared common principles for reform and an action plan to implement the principles.</u>
23 Nov	The US government announced the rescue plan for Citigroup	
2009	16 Jan	The US government announced the rescue plan for Bank of America
	10 Feb	<u>The US government published the Financial Stability Plan, which included a comprehensive stress test and establishment of a Public-Private Investment Fund</u>
	18 Mar	The UK government published the Turner Review on global banking regulation
	1-2 Apr	<u>The Second G-20 Summit was held in London and leaders issued the declaration on strengthening the financial system</u>
	7 May	<u>The US government published the results of the stress test</u>
	17 Jun	<u>The US government announced a comprehensive plan for regulatory reform</u>
	19 Jun	<u>The European Council endorsed proposals to reform financial supervision (Establishment of European systemic risk board)</u>
8 Jul	The UK government published the White Paper on Reforming Financial Markets	

Global Financial Crisis and Policy Responses- Chronology of Events

2009	24-25 Sep	<u>The Third G-20 Summit was held in Pittsburgh.</u>
	9 Dec	The UK government published a temporary bank payroll tax in the 2009 Pre-Budget Report
	11 Dec	the Wall Street Reform and Consumer Protection Act of 2009 was passed in the House in the US
	17 Dec	<u>The Basel Committee announced consultative proposals to strengthen the resilience of the banking sector</u>
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2010	14 Jan	<u>The US government announced Financial Crisis Responsibility Fee</u>
	21 Jan	<u>The US government announced Restriction on Size and Scope of Financial Institutions</u>
	17 Feb	The Basel Committee published Workbook and Instructions, etc. for the Comprehensive Quantitative Impact Study(QIS).
	8 Apr	the Financial Services Act was enacted in the UK.
	23 Apr	The Greek government requested a monetary rescue plan.
	7 May	The heads of state/government of the Euro area approved the support package for Greece
	10 May	The Economic and Financial Affairs Council of EU agreed to establish the European Financial Stabilization mechanism
	26 May	<u>The European Commission proposed the establishment of the bank resolution funds</u>
	17 Jun	<u>The UK government announced Reforming the Institutional Framework for Financial Regulation</u>
	22 Jun	The UK government announced the introduction of a bank levy in the June 2010 Budget. <u>The Fourth G-20 Summit was held in Toronto</u>
	26-27 Jun	<u>The Dodd-Frank Wall Street Reform and Consumer Protection Act was enacted in the US</u>
	21 July	<u>The results of the EU-wide stress testing exercise was published</u>
	23 July	<u>The Group of Governors and Heads of Supervision(GHOS) reached a broad agreement on Basel</u>
	26 July	<u>Committee capital and liquidity reform package(Basel III)</u>
	13 Sep	<u>The GHOS announced higher global minimum capital standards</u>
	4 Oct	An expert group commissioned by the Swiss government recommended that more capital than agreed by the GHOS be required for UBS and Credit Suisse
	11-12 Nov	<u>The Fifth G-20 Summit was held in Seoul</u>
	17 Nov	<u>The Economic and Financial Affairs Council of EU adopted legal texts for establishing the new framework for financial supervision</u>
	16 Dec	<u>The Basel Committee published the rule text of Basel III and the result of the QIS</u>

The G20 Seoul Summit Leaders' Declaration (11-12 November 2010) on Financial Sector Reforms

1. Transformed financial system to address the root causes of the crisis

- Endorsed agreement reached by the BCBS on the new bank capital and liquidity framework and are committed to adopt and implement fully these standards within the agreed timeframe.
- Endorsed the policy framework, work processes, and timelines proposed by the FSB to reduce the moral hazard risks posed by systemically important financial institutions (SIFIs) and address the too-big-to-fail problem.
- Endorsed the policy recommendations prepared by the FSB in consultation with the IMF, on increasing supervisory intensity and effectiveness.

2. Implementation and international assessment, including peer review

- It is essential that we fully implement the new standards and principles.
- International assessment and peer review processes should be substantially enhanced in order to ensure consistency in implementation across countries and identify areas for further improvement in standards and principles.
- Firmly recommitted to work to strengthen regulation and supervision on hedge funds, OTC derivatives and credit rating agencies. Reaffirmed the importance of fully implementing the FSB's standards for sound compensation. Endorsed the FSB's recommendations for implementing OTC derivatives market reforms and the FSB's principles on reducing reliance on external credit ratings
- Re-emphasized the importance of achieving a single set of improved high quality global accounting standard

3. Future work: Issues that warrant more attention

- (1) Further work on macro-prudential policy frameworks
- (2) Addressing regulatory reform issues pertaining specifically to emerging market and developing economies (including the management of foreign exchange risks, information sharing between home and host supervisory authorities and trade finance)
- (3) Strengthening regulation and supervision of shadow banking
- (4) Further work on regulation and supervision of commodity derivative markets
- (5) Improving market integrity and efficiency
- (6) Enhancing consumer protection

- The next G20 summit will be held in France in November 2011.

The Report on Systemically Important Financial Institutions (SIFIs)

- The FSB submitted a report to address “too-big-too-fail” problems of SIFIs to the G20 Leaders at the Seoul Summit. The report sets out timelines for implementing measures regarding SIFIs (details are below).
- Discussions about the specific methodology to identify global SIFIs (G-SIFIs) and a menu of viable alternatives to raise loss absorbency of G-SIFIs will continue.

(1) Identifying G-SIFIs

- ⇒ (i) The BCBS should propose a provisional methodology by end-2010 and finalise the methodology in early 2011.
- (ii) The FSB and national authorities will determine G-SIFIs by mid-2011

(2) Raising loss absorbency

- ⇒ Depending on national circumstances, this could be drawn from a menu of viable alternatives. The FSB, in consultation with the BCBS, will recommend an additional degree of G-SIFI loss absorbency and the instruments to meet these by December 2011

(3) Making effective resolution regimes

- ⇒ (i) national authorities will report their assessment of national resolution regimes by end-March 2011 and set out plans to address areas where changes or improvements are needed, by end-2011. The FSB will undertake a peer review on national resolution regimes in 2012.
- (ii) The FSB will assess and report on the progress in the development of institution-specific recovery and resolution plans for G-SIFIs by end-2011.
- (iii) Relevant home and host authorities will draw up for all G-SIFIs institution-specific cooperation agreements that specify the respective roles and responsibilities of the authorities in crisis, by end-2011,

(4) Strengthening SIFI supervision

- ⇒ National authorities should conduct a self assessment against the relevant BCBS Core Principles and make necessary changes.

(5) Strengthening core financial infrastructures

- ⇒ The FSB should provide regular assessments of progress regarding the recommendations set forth in the report of the FSB OTC Derivatives Working Group, with an initial report no later than end-March 2011

(6) Peer-reviewing national policies for G-SIFIs

- ⇒ (i) The FSB should complete an evaluation framework for the application and review of G-SIFI policies by end-2011.
- (ii) The FSB will establish a peer review council by end-2011 and conduct the initial review by end-2012.

Progress on Basel III

Summary of the Press Release by the GHOS : 26 July 2010

➤ Raising the quality of capital

It was made clear that Common Equity Tier1(CET1) must consist of common shares and retained earnings (highest form of loss absorbing capital). DTAs and intangible assets should be deducted from CET1.

→However, the following treatments of deduction items were allowed by considering national circumstances.

	December 2009 proposal	GHOS agreement (26 July)
DTAs	Full deduction from CET1	DTAs that arise from timing differences can be recognized up to 10% of CET1. (Note)
Intangible Assets	Full deduction from CET1	Allow IFRS treatment where different from national GAAP (e.g. software)
Minority interest	Not eligible for inclusion in CET1	Minority interest supporting the risks of a bank subsidiary can be recognized in CET1 up to the regulatory minimum of the subsidiary

(Note) The aggregate amount of DTAs, MSRs, and significant investments in the common shares of unconsolidated financial institutions can be recognized up to 15% of CET1.

➤ Introduction of the Leverage Ratio

→ Based on the results of the parallel run period (a minimum Tier 1 leverage ratio of 3% will be tested), any final adjustments would be carried out in the first half of 2017 with a view to migrating to a Pillar 1 treatment on 1 January 2018 based on appropriate review and calibration.

➤ Introduction of the Global Liquidity Standard

Banks are required to hold adequate level of liquid assets (e.g. cash and government debt).

→e.g. Deposits' run-off rates during a stress period were made in line with realistic assumptions.

Progress on Basel III

Summary of the Press Release by the GHOS : 12 September 2010

Increased Capital Requirements and Transition Arrangements

Calibration of the Capital Framework (%)			
	CET1 (after deductions)	Tier 1 Capital	Total Capital
Minimum	4.5	6.0	8.0
Conservation buffer	2.5		
Countercyclical buffer range	0-2.5		

- National implementation will begin on 1 January 2013. The new standards will be fully implemented by 1 January 2019 in accordance with the transition arrangements.
 - The minimum requirement for common equity of 4.5% and Tier 1 capital of 6% will be phased in by 1 January 2015.
 - The capital conservation buffer (2.5% of common equity) which can be used to absorb losses during periods of financial and economic stress will be phased in from 1 January 2016 to 1 January 2019.
- The regulatory adjustments (the improvements on the quality of capital) will be phased in from 1 January 2013 to 1 January 2018.
- Capital instruments that no longer qualify as non-common equity Tier 1 capital or Tier 2 capital will be phased out over a 10 year horizon beginning 1 January 2013.
- The liquidity coverage ratio (LCR) will be introduced on 1 January 2015, after an observation period beginning in 2011.
- The net stable funding ratio (NSFR) will move to a minimum standard by 1 January 2018.

Issues for Discussion

- Have all of the fundamental causes of the financial crisis been appropriately addressed by the reforms that have been undertaken? What are the areas requiring further attention?
- Are the arrangements regarding the structure, governance, and transparency of the FSB and the standard-setting bodies adequate in view of their important roles?
- How will it be possible to implement the various reform measures across countries in a consistent manner?