Statement of Mark Carney
Chairman of the Financial Stability Board
to the International Monetary and Financial Committee

Washington, DC, 18 April 2015

Vulnerabilities in the financial system

Recent market portfolio adjustments and asset re-pricing have occurred in response to the divergence in economic growth and policy expectations in the global economy. Market adjustments to date have occurred without significant financial stress. However, the risk of a sharp and disorderly reversal remains, given compressed credit and liquidity risk premia. As a result, market participants need to be mindful of risks of diminished market liquidity, asset price discontinuities, and contagion across markets. The impact of lower commodity prices, a stronger US dollar and moderating economic growth may lead to further challenges for the financial resilience of some emerging market and developing economies (EMDEs), including the risk of capital flow volatility.

Market liquidity and asset management

While the trend towards greater market-based intermediation through asset management entities is welcome and should contribute to the overall resilience of the financial system by providing alternative sources of funding, it is important to ensure that any financial stability risks are properly understood and managed. For example, concerns arise about rising risks stemming from the overestimation by investors of the degree of liquidity fixed income markets as well as the growth of assets under management in funds that offer on-demand redemptions but invest in less liquid assets.

The FSB has agreed a work plan to identify financial stability risks associated with market liquidity in fixed income markets and asset management activities in the current conjuncture, as well as longer-term structural financial stability issues that may arise. This work will evaluate the role that existing or additional activity-based policy measures could play in mitigating potential risks, and make policy recommendations as necessary. The FSB will discuss the initial findings at its next meeting in September.

Market-based finance

The FSB agreed last year numerical haircut floors for securities financing involving bank-to-non-bank transactions against non-government collateral. Following consultation responses, it has now agreed to extend the application of floors to include non-bank-to-non-bank securities financing transactions, to counter the risk of regulatory arbitrage. These extended standards will be finalised by September 2015.

The FSB has also completed an initial information-sharing exercise among jurisdictions on their implementation of the FSB's high-level policy framework for shadow banking entities. The FSB will conduct a comprehensive information-sharing exercise, which will be peer-reviewed, in 2015.

Ending too-big-to-fail

Agreement was reached last year on two key steps forward in ending too-big-to-fail for global systemically important banks (G-SIBs). The first agreement was on a proposal for a common international standard on the total loss absorbing capacity (TLAC) that G-SIBs must have. The second was an industry agreement to prevent cross-border derivative contracts being disruptively terminated in the event of a G-SIB entering resolution; national authorities will use regulatory and supervisory actions to support comprehensive industry adoption of the agreement.

The FSB is considering the responses to its public consultation on the proposed TLAC for G-SIBs and impact assessment studies are underway. The new standard will be finalised in November.

The FSB's guidance on statutory and contractual approaches to the cross-border recognition of resolution actions is being finalised, following a recent public consultation. Work is underway to promote broad adoption of contractual recognition clauses to make temporary stays of early termination rights effective in a cross-border context.

To fully realise the financial stability benefits of clearing through central counterparties (CCPs), the FSB has agreed a work plan to promote CCP resilience, recovery planning and resolvability. The work will be taken forward in close coordination between the Committee on Payments and Market Infrastructures (CPMI), International Organization of Securities Commissions (IOSCO), Basel Committee on Banking Supervision (BCBS) and the FSB.

Market conduct issues

Misconduct in financial institutions has the potential to create systemic risks by undermining trust in financial institutions and markets. To address misconduct risks, the FSB has agreed a work plan that will examine:

- how the incentives created by reforms to risk governance, compensation structures and benchmarks have helped to reduce misconduct and whether any additional measures are needed;
- whether steps are needed to improve standards of conduct in the fixed income, commodities and currency markets; and
- together with the World Bank and other relevant bodies, the extent of potential withdrawal from correspondent banking, its implications for financial exclusion, as well as possible steps to address this issue.

Implementation monitoring

FSB members are committed to the full, consistent and timely implementation of the agreed international financial regulatory reforms. The FSB will this year provide the first consolidated annual report to the G20 on the implementation and effects of these reforms. The report will be published at the time of the Antalya Summit.

A thematic peer review report on supervisory frameworks and approaches for systemically important banks will be published in the coming weeks. It will examine how authorities are implementing the FSB recommendations for a more intensive and effective approach to supervision, particularly for G-SIBs.

Data gaps

The FSB is reviewing a proposal for the third and final phase in the implementation of its initiative to collect data on G-SIB exposures and funding through a common data template. From 2016, granular balance sheet data would be collected on a quarterly basis covering five dimensions: instrument, counterparty jurisdiction and sector, maturity and currency. Data is shared between home supervisors, central banks and, from 2016, selected data will be shared with international organisations with a financial stability mandate such as the Bank for International Settlements (BIS), FSB and IMF.

New FSB members

In March 2015, the FSB welcomed five institutions as Plenary members – the ministries of finance or treasuries for Argentina, Indonesia, Saudi Arabia and Turkey and the South African Reserve Bank. Increased representation for emerging markets delivers a key objective of the FSB's review of the structure of its representation last year.

Emerging Markets Forum

The FSB held an Emerging Markets Forum in March to discuss issues related to implementation, home–host, proportionality and sequencing raised by EMDEs. These included issues related to Basel III, over-the-counter derivative reforms, resolution, macroprudential policies in emerging markets, concerns about reduced availability of correspondent banking services, and the continued need to make local capital markets deeper and more resilient as well as sovereign debt restructuring processes. The FSB, the standard-setting bodies and international financial institutions will consider how they can best incorporate the issues raised into their work plans.