M R Pridiyathorn Devakula: FSAP from the Thai banking perspective

Statement by Mr M R Pridiyathorn Devakula, Governor of the Bank of Thailand, at the United Nations Conference Center, Bangkok, 15 October 2004.

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Distinguished guests and participants, Ladies and Gentlemen,

Good morning. It is a great pleasure for me to open this important workshop and give a keynote speech. The objective of today’s event is to introduce the joint IMF-World Bank initiative called the Financial Sector Assessment Programme, otherwise known as FSAP, so that at the end of today we will all have a common and thorough understanding of what FSAP is about, how much work it would require of whom, and what benefits there would be for Thailand to participate in. This is a tall order to be achieved in one short day, but I am sure we can do it because we are fortunate enough to have with us two senior and highly experienced staff from the IMF: Mr Stefan Ingves and Mr. Udaibir Saran Das. On behalf of the Bank of Thailand and all the participants, I would like to thank both of you very much for making the time to be here despite your busy schedule. We are indeed grateful for your assistance.

By way of introduction, let me very briefly give you an overview of the FSAP and how it might complement and enhance our ongoing efforts to improve corporate governance and promote safety and soundness of the financial system in Thailand.

FSAP was jointly developed by the IMF and World Bank in 1999 in response to the financial crisis of the late 1990s, when it became clear that financial sector weakness played a critical role in triggering and contributing to the severity and contagion of the economic crisis that ensued, and that both the standard macroeconomic surveillance by the IMF and the financial sector development work of World Bank were inadequate. Thus, FSAP was conceived with the twin objectives of helping countries to identify and resolve financial sector vulnerabilities and thereby helping to prevent future crises. It also aims to foster financial sector development and efficiency. I think these are indeed admirable objectives to which we can all agree.

As for the implementation, there are essentially three aspects to the FSAP:

The first involves an assessment of the health of the country’s financial system, its short-term vulnerabilities, medium-term risks, and resilience to economic und financial shocks. A range of analytical tools can be used tot this purpose, including stress testing, macro-prudential analysis, and financial soundness indicators. It is here that private sector involvement becomes crucial. Stress testing, as a means to gauge institutional capacity in responding to crises, requires real-world data. And such can only come from financial institutions.

The second aspect of the FSAP is an assessment of the country’s compliance with international standards and codes that are considered best practice. Some would be tempted to say that nowadays there are really too many international standards and codes. Thus, to keep things manageable, one needs to be selective. Specific standards and codes included in the FSAP therefore differ from country to country depending on their relevance and significance to its financial system. In the case of Thailand, I suppose the scope of the FSAP would likely include most, if not all, of the following core modules:

- Banking supervision
- Securities market regulation
- Insurance sector regulation
- Payment system
- Monetary and financial policy transparency, and
- Anti-money laundering and combating the financing of terrorism.

In order to attest to the efficacy of each of these regulatory mandates, the FSAP assessment process also involves face-to-face interviews and discussions with a number of private sector institutions.

The third aspect of the FSAP involves identification of follow-up measures for the authorities to address any gaps in the country's regulatory framework; which also provides a foundation for future technical assistance programmes, if necessary.

In the course of today's workshop, our experts from the IMF will no doubt enlighten us on what the FSAP process would entail in practice. So please feel free to ask any question you may have, especially those who have already embarked on the self-assessment exercise for the relevant modules. I guess that given the comprehensiveness of the FSAP process that I have just briefly outlined, you can readily imagine that undergoing the FSAP would require a lot of work, a lot of time, and a lot of information from people involved with the financial sector - be they regulators, government agencies, bankers, market participants, and industry associations. Because of the enormity of the tasks ahead and the fact that a country's participation in the FSAP is entirely voluntary, it is natural to ask: Why is Thailand contemplating participation in the FSAP? Is it really worth it? The short answer is probably yes.

First of all, it is simply good discipline to have a competent external party conduct a thorough assessment of our financial system in a holistic and objective manner.

Second, the FSAP would present a good opportunity for regulators and relevant government agencies to enhance or confirm our understanding of where potential vulnerabilities in the financial sector lie, and whether existing policy frameworks are adequate in preventing or responding to any financial instability.

Third, the FSAP process would benchmark our existing regulatory arrangements against international standards and codes and, hopefully, provide impetus to the responsible authorities in their efforts to plug any gaps in the regulatory framework. Having said that, I must hasten to emphasize that we do NOT seek to blindly follow every international standard and code without due regard to our own characteristics and needs. Some differences in our practice as compared to international standards may not warrant any further action at all, for they reflect our conscious intention to adopt rules that best suit our own unique situation as well as rules that should be phased in gradually to comply with international standards only at an appropriate time. We welcome the opportunity to discuss and share this understanding with the FSAP assessors, who are drawn not only from IMF and World Bank staff but also from other countries' central bankers, regulators, and international experts.

Before I let you get on with the workshop, I would like to conclude by saying that, with or without the FSAP, the Bank of Thailand will continue to strive for a safe and sound financial system, both through efforts to restructure financial institutions under the Financial Sector Master Plan, and through continued strengthening of prudential standards and supervisory practice. Risk-based supervision approach has been adopted. Loan classification and provisioning requirements have been and will be tightened further. Good corporate governance has been enforced, including appropriate composition of the Board of Directors and, most recently, fit and proper criteria for the top management of commercial banks.

We have come a long way since the 1997 crisis and we do not intend to look back. Yet, many formidable challenges lie ahead. On the international front, a lot of preparations and adjustments are needed in response to the introduction of IAS39 and the new Basel Capital Accord. Though it might be worth underlining here that FSAP is independent of the Basel 2 process. As a contemporary assessment of a financial system relative to its current regulatory and macro environment, FSAP assessment will finish well before the end of 2008, when Basel 2 is scheduled to go 'live' in this country. Domestically, it is imperative that the new financial institutions law be enacted to give us the necessary power to implement, among other things, the all-important consolidated supervision and prompt corrective action over financial institutions.

Finally, I would like to thank you all for participating in this workshop, especially those of you who have contributed to the self-assessment exercise that has already been in progress. Your continued cooperation and support will certainly be much needed in the months and years ahead. I wish you all an interesting and useful workshop. Thank you very much.