Andreas Dombret: Global rules for global financial markets

Speech by Dr Andreas Dombret, Member of the Executive Board of the Deutsche Bundesbank, as a response to the Note of the Pontifical Council of Justice and Peace, Frankfurt am Main, 19 September 2012.

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I was asked to share my views today on the note of the Pontifical Council of Justice and Peace on reforming the international financial and monetary system.

Lack of global financial regulation

I highly welcome the general tone of the Pontifical Council's note which stresses the need for the financial sector to serve the overall economy and, accordingly, the common good. With respect to financial regulation, the note rightly points to the lack of truly global regulation for global financial markets as a key factor for the financial crisis that started in 2007. While financial markets around the globe became more and more integrated and interconnected over past decades, financial regulation remained largely national – despite of ongoing coordination efforts in international committees and groupings. The crisis highlighted some inefficiencies of international coordination in financial regulation and necessitated numerous ad-hoc interventions by public authorities. Those events made clear that although rules and regulations were partly agreed on internationally, their transition into national rules and legislation was fragmented and, at times, even inconsistent. Not surprisingly, financial institutions had a strong incentive to engage in regulatory arbitrage. An internationally coordinated regulatory response is therefore warranted.

Minimum body of internationally agreed rules

I agree with the conclusion of the Pontifical Council that we need a minimum, shared body of rules and regulations for global financial markets. But one size does not fit all. Accordingly, and in line with the principle of subsidiarity, the rules should be set at the international level but allow for sufficient flexibility to adapt them to peculiarities of national financial systems. However, I do not see the need to create a new "global authority" for that purpose. Over the past years, the Financial Stability Board (FSB) has emerged as the central body coordinating the international financial sector reform agenda set in train by G20 Leaders at their Washington Summit in 2008 and further developed at subsequent meetings. The FSB brings together international institutions and standard-setting bodies as well as regulators, central bankers and finance ministers from advanced and emerging economies with the most important financial sectors globally. In the meantime, the FSB has gained a track record and several important cornerstones of the reform agenda have been set in place. Take the policy framework for dealing with systemically important financial institutions or the new regulatory standard for bank capital adequacy and liquidity – commonly termed as Basel III – as examples. G20 Leaders, in late 2011, agreed to further strengthen the FSB's role in order to enable it to keep pace with its growing role in promoting the development and implementation of regulation. Accordingly, in June 2012, G20 Leaders endorsed the FSB's recommendations on strengthening its capacity, resources and governance. I strongly support the further development of the FSB because I am convinced that it will further improve the elaboration of international rules and regulations as well as international cooperation in regulation and supervision and help to achieve an international level playing field.

Rigorous monitoring of national implementation

While rule-making at the international level is a necessary condition for financial stability, it is by no means sufficient. For the rules to be effective, they have to be translated in national laws and regulations in a timely and consistent manner. Therefore, we need to strictly monitor implementation, disclose the respective findings, and let peer pressure work its magic. The FSB and international standard-setting bodies have jointly developed a coordination framework for implementation monitoring to ensure consistent implementation of the reform agenda. As another important part of implementation monitoring, the International Monetary Fund together with the World Bank is regularly assessing the adherence of its member countries to international standards. Thereby, the Fund is promoting international monetary cooperation and exchange rate stability. In response to weaknesses detected during the financial crisis, the Fund initiated various reforms with the aim of strengthening its internal governance as well as its analytical capabilities. I highly welcome those reforms which will further improve the Fund's work.

To sum up, I regard strengthening existing bodies in the field of global financial regulation and the international monetary system as the right way forward for two main reasons. Firstly, it allows building upon the substantial expertise gathered in existing institutions. Secondly, jurisdictions are obviously reluctant to further cede national sovereignty to a supra-national level. The enduring debate about the creation of a fiscal union in Europe is providing just one vivid example in this regard. Accordingly, the creation of a global regulatory authority does not seem to be practical at this point in time. Moreover, I regard the current practice of setting rules for the global financial markets as appropriate. In a first step, set the rules at the international level. As a second step, rigorously monitor their translation in national laws and regulations to ensure consistency and a global level playing field. As I have pointed out, we have adequate institutions at the global level to fulfill these tasks, so currently I do not see the need to create new authorities for that purpose.

Thank you for your attention!