

Axel A Weber: Current developments in the financial system

Welcoming remarks by Professor Axel A Weber, President of the Deutsche Bundesbank, at the 5th Bundesbank Lecture, Berlin-Brandenburgische Akademie der Wissenschaften, Berlin, 16 September 2008.

* * *

Ladies and gentlemen

I am very pleased to welcome you to this year's Bundesbank Lecture at this beautiful location here in the very heart of Berlin. I am particularly grateful that Mr Mario Draghi, Governor of the Bank of Italy, will be our speaker today. Mario, my special welcome to you and thanks a lot for not hesitating one moment to accept our invitation to be the lecturer at our event. It is an honour to have you here.

Let me briefly say a few words regarding both this event and our speaker for today. On the event: The Bundesbank Lecture Series aims to achieve two things. First, we intend to provide a high-level forum for public debate on economic and monetary policy issues. Second, we want to raise the Bundesbank's profile in the German capital. With today's gathering, our Lecture Series, which started in 2004, is celebrating its fifth anniversary. Alan Greenspan, Jean-Claude Trichet, Tommaso Padoa-Schioppa, and Ben Bernanke have shared their thoughts with us at previous lectures.

We are proud to have Mario Draghi as speaker. The title of his speech will be "Restoring stability in the financial system". He is a distinguished expert on financial stability issues. As the current chairman of the Financial Stability Forum he is in a focal position to discuss necessary measures to restore financial stability. Obviously, the topic of his speech could not be more topical given the current developments on financial markets. The financial market crisis – alongside rising inflationary pressures – has been the dominant topic for more than a year now. One does not have to be a prophet to forecast that it is likely to stay with us in the months ahead, too.

Of course, I do not want to anticipate Mario's remarks, but let me say some words on the current developments.

The filing of chapter 11 bankruptcy petition by Lehman Brothers Holdings inc. and the sale of Merrill Lynch to Bank of America has certainly further increased uncertainty and risk aversion on financial markets.

We observe flight to quality behaviour by investors and rising spreads on credit markets. This had to be expected. All in all, however, market participants have not overreacted and remained cool-headed. This is a positive sign.

Central banks, including the Eurosystem, have reacted decisively to the situation with liquidity provisions and other measures. German banks do not report liquidity problems.

The German financial system is stable and over the past years its resilience against adverse shocks has markedly improved. Moreover, the universal banking model – a characteristic feature of the German financial system – has proven its robustness and stability.

These structural achievements will help to cushion current tensions due to higher perceived counterparty risk and a necessary unwinding of positions on the market for credit risk transfer – both unavoidable outcomes in the face of an insolvency of one of the major market participants.

The financial turbulence has created the most challenging situations for financial intermediaries, for central banks, for supervisory agencies, and for regulatory bodies in decades. And since the causes of the crisis are deeply rooted, a comprehensive coordinated response at the international level is evidently warranted.

In this context, the Financial Stability Forum – the FSF – in particular is playing a crucial role in the process of mitigating the ongoing difficulties and making the financial system more resilient to future shocks. The FSF was established in 1999, following a report by the then Bundesbank President, Hans Tietmeyer.

The FSF brings together senior representatives of national financial authorities (for example, central banks, supervisory authorities and treasury departments), international financial institutions (such as the IMF or the BIS), international regulatory and supervisory groupings (for example, Basel Committee on Banking Supervision, International Accounting Standard Board), committees of central bank experts (such as the Committee on the Global Financial System) and the European Central Bank.

The FSF's mandate is to assess vulnerabilities affecting the international financial system, to identify and oversee action needed to address these, and to improve coordination and information exchange among the various authorities responsible for financial stability.

In doing so, the FSF aims to promote international financial stability, improve the functioning of financial markets, and reduce the tendency for financial shocks to spread from country to country, thus destabilising the world economy. The FSF seeks to give momentum to a broad-based multilateral agenda for strengthening financial systems and the stability of international financial markets. The necessary changes are enacted by the relevant national and international financial authorities. In a nutshell, the FSF acts as a central hub for all the issues that are relevant from a global financial stability perspective.

On the speaker: Mario Draghi, Governor of the Banca d'Italia, has been chairing the FSF in a personal capacity since April 2006. This position – together with the economic and international expertise he has gained during his career – makes him an excellent speaker in current times, given the backdrop of the financial market turbulence.

Mario Draghi graduated from the University of Rome, received his Ph.D. in economics from the Massachusetts Institute of Technology, and subsequently served as professor of economics at the University of Florence from 1981 to 1991. Prior to taking the helm at the Banca d'Italia, he was vice-chairman and managing director of Goldman Sachs and a member of the firm-wide management committee (2002-2005). He was director general of the Italian Treasury (1991-2001), chairman of the European Economic and Financial Committee, a member of the G7 Deputies, and chairman of OECD Working Party 3. Finally, from 1984 to 1990, he was an executive director of the World Bank.

A few weeks ago, during the annual central bankers' meeting in Jackson Hole, Mario delivered a speech entitled "The current crisis and beyond". In his speech, he pointed out three elements that mark the cornerstones of the work plan of the FSF for the month ahead.

More precisely, he talked about the need to look more closely at the incentives for appropriate risk control frameworks, efforts to improve the resilience of the financial system to shocks frameworks for dampening the cyclicity of risk-taking. Not only was it a pleasure to listen to him, I also fully endorse the proposals he made.

The title of his speech today is "Restoring Stability in the Financial System", a topic that is evidently highly relevant and of interest to all of us. Mario, I am looking forward to your insights during the fifth Bundesbank Lecture. The floor is yours.