Axel A Weber: Developing a long-term investment perspective favouring financial stability and growth

Introductory remarks by Professor Axel A Weber, President of the Deutsche Bundesbank, at the Eurofi Financial Forum plenary session 16 on “Defining a common regulatory and supervisory basis to achieve resilience, growth and competitiveness”, Brussels, 29 September 2010.

* * *

Ladies and gentlemen

The financial crisis has painfully demonstrated vulnerabilities of our financial system. Strengthening the resilience of the financial system, that is of financial markets and their players, is therefore the top priority when it comes to learning the lessons of the crisis. Closing the regulatory gaps which the crisis has revealed – however important that is – would be too little. Financial reform has to go beyond that and establish the necessary institutions and regulations to deal with systemic risks.

Financial reform will not save us from any future financial crisis but it can significantly dampen the frequency and intensity of financial crises in the future. Reducing the likelihood of individual bank failures may act in this respect as a first line of defence. The most important project in this regard is the revision of Basel II. This reform will significantly increase the risk buffers of individual financial institutions by introducing stricter requirements regarding the quality and quantity of bank capital. While the new rules require banks to increase their capital, the provision of transition periods enables them to adapt to the more restrictive capital and liquidity requirements. Hence, I am not afraid that the implementation of Basel III might significantly impair the lending capacity of banks or hamper economic recovery. While being subject to considerable uncertainty, recent comprehensive impact studies by the Basel Committee and the Financial Stability Board suggest the economic impact during the transition period will be moderate and that the long-term net benefits will be positive. Now it is up to the G20 Heads of State and Government to approve the package at their Seoul summit in November. Its global implementation afterwards is of utmost importance in order to guarantee a level playing field and to prevent regulatory arbitrage.

In addition, some elements of the package require further work in the process of finalising the whole. In particular, the extent of anti-cyclicality of capital buffers might be strengthened further, and the requirements of the liquidity buffer in its currently proposed form warrant further adjustment as well: requirements for eligible assets of private issuers, for example, appear rather strict.

While the new Basel rules will certainly help to make the financial system of the future safer and more stable, a second line of defence is required. The recent crisis has shown that a systemic crisis may quickly pose a threat to institutions that are actually sound. Systemic risk, however, cannot be dealt with by microprudential supervision alone. Regarding the establishment of an effective macroprudential toolset, important measures are still due. Our major concern in this respect is the too-big-to-fail issue. Efforts are being made by the FSB to present an approvable base solution to the G20 summit. Essential details, however, will have to be finalised afterwards, in particular the formal definition of “systemically important financial institutions” (SIFI’s). In order to find a credible solution to the too-big-to-fail problem strong political commitment would act as a helpful support.

Taking the time constraints into account, I want to conclude my remarks. Nevertheless, I do not want to fail to mention that macroprudential surveillance has to go beyond the focus on individual national institutions. Close cooperation at the European and international levels is indispensable in order to supplement microprudential supervision with a systemic view. The establishment of the ESRB is an important step in the right direction. Now the challenge for its members is to make it a success.

Thank you very much.