Barry Whiteside: Risk focused supervision

Address by Mr Barry Whiteside, Governor of the Reserve Bank of Fiji, at the APEC-FRTI workshop on "Risk focused supervision", Nadi, 18 November 2013.

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Dr Sungbok Lee – APEC FRTI/KSP Secretariat

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Distinguished Resource Persons

Workshop Participants

Ladies and Gentlemen

Introductory Comments

Good morning and *Bula Vinaka*.

I am delighted to be asked to deliver the welcome address and open this very important workshop organised by the APEC Financial Regulators Training Initiative (FRTI) in conjunction with the Knowledge Sharing Programme of the Republic of Korea (KSP). I might add that the Reserve Bank of Fiji is also honoured to host this event and showcase our country to our visitors.

Let me take this opportunity to extend to you, and especially to our foreign guests, a warm Fijian welcome to this workshop, which is being held at this famous tourist destination of Denarau Island.

I am informed that apart from the resource persons who are from Korea, the Philippines and Australia, we have assembled with us participants from as far away as Mongolia and Zambia. We don't often have visitors from these parts of the world, so let me say a warm welcome to Gaadulam, Said and Joseph! Indeed I see this gathering as an opportunity for great cultural exchanges, in addition to the specialised knowledge and skills you will be acquiring.

Importance of the workshop

Ladies and Gentlemen, there could not have been a better time for this workshop than now, given the strategic importance of financial stability to the overall performance of our economies. Risk-Based or Risk-Focused Supervision is a subject area which continues to receive the attention of supervisory authorities worldwide.

The international banking scene has, in recent years, witnessed strong trends towards globalization and consolidation of financial systems. Stability of our respective financial systems has become the central challenge to bank regulators and supervisors throughout the world. The multi-lateral initiatives leading to the evolution of international standards and codes, and evaluation of our compliance to these standards and codes, represent solid attempts to address this challenge.

The key objective of prudential supervision is to maintain stability and confidence in the financial system in our jurisdictions, thereby reducing the risk of loss to depositors and other creditors. In addition, supervision is also directed towards verifying compliance with laws and regulations governing financial institutions and their activities.

We cannot deny that the growing diversities and complexities of banking business, the spate of product innovation with complex risk phenomena, the contagion effects that a crisis can spread given the linkages and interdependence of financial institutions, and the growing trend of businesses without borders, all call for a new approach to ensuring the financial health of our economies. And that, ladies and gentlemen, is what Risk-Focused Supervision is all about.

Role of the supervisor in risk focused supervision

The role of the supervisor in modern financial system supervision is to ensure that the risk management systems in place and the capital held, are appropriate for the variety of identifiable risks to which supervised financial institutions expose themselves on a day-to-day basis.

The supervisor must have the authority and expertise to review and intervene in risk management processes, where necessary. This involves monitoring and evaluation of the risk profiles of supervised institutions in relation to their business strategies and risks. Regulators and supervisors must fully understand any new financial innovations, instruments and market practices in order to have the expertise to develop models, assumptions and views of financial institutions, and certify the risk management of those supervised institutions.

Of course, the effectiveness of any risk-based approach owes a lot to the supervisor's ability for early identification and monitoring of new and emerging risks. Supervisors can devote a lot of time and effort toward trying to prevent or mitigate a risk incident but, as we have been taught, a good supervisor should target patterns of behaviour that give rise to excessive risk-taking in the first place.

When it comes to supervising for risk, behaviours matter. Things like:

- corporate governance
- risk appetite;
- risk management;
- alignment of incentives to risk taking; and
- organisational culture;

  are all important.

Institutions that have, and effectively implement these things, are likely to be well-run and would portray a good grasp of their risk environment. Institutions that merely have them and do not effectively take action in ensuring that these are implemented, are inviting trouble.

Ladies and gentlemen, getting to grips with matters of risk management requires a more pro-active approach from supervisors.

- It takes ***a deep understanding*** of an institution's operations and appetite for risk for its significant activities;
- It takes frequent interaction with regulated institutions at both board and management levels;
- It takes ***a capacity to assess the effectiveness of risk management*** and control functions, (including how the institution is governed and the prevailing risk culture); and,
- It takes ***a capacity and willingness to act*** when inadequacies are identified.

None of these are easy to implement. Risk-based approaches are resource-intensive. They require a hands-on, active approach to prudential supervision. They require experienced supervisors with deep industry knowledge. Even after all that, there is no guarantee that supervisors will always make the right calls on risk.

However in spite of such isolated moments where we as supervisors may not have made the right call, by targeting specific risk outcomes, risk-focused approaches to prudential supervision are better placed to enable us to make a material difference to the prudential health of the institutions we supervise, for any given level of resources.

Concluding remarks

Let me take this opportunity to thank the APEC Financial Regulators Training Initiative and the Knowledge Sharing Programme of the Republic of Korea for organising this workshop.

I wish you a productive and exciting week and encourage you all to draw on the wealth of knowledge of the facilitators, as well as the rich experience of your fellow participants.

Do take some time to explore our wonderful islands, if this is at all possible. Your Fijian colleagues will only be too pleased to assist. We are known to be pretty friendly!

On this final note, it gives me great pleasure to declare this Workshop on Risk-Based Supervision open.

Vinaka vakalevu.