The B.I.S. and its Role in International Financial Governance

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S. Griffith-Jones with J. Kimmis*

Institute of Development Studies
University of Sussex
Falmer
Brighton
BN1 9RE

Tel: 01273 606261
Fax: 01273 621202
e-mail: s.griffith-jones@ids.ac.uk

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I INTRODUCTION

Over the last two decades, financial crises have tended to occur with increasing frequency. Many of these crises have affected developing countries, often with devastating effects on their growth and development. The crisis which started in mid 1997 in East Asia, and then spread to several parts of the developing world as well as affecting also the developed economies, has illustrated the seriousness of these crises' effects, and the need to urgently improve international mechanisms for both crisis prevention and management.

As a consequence, financial stability – both domestically and internationally – emerges as a key objective of economic policy. The BIS has particularly in recent periods had a mandate to promote international co-operation on monetary and financial issues, with the pursuit of international financial stability at the heart of its activities. Initially, the BIS's activity focussed very much on financial stability in the major industrial countries but it has increasingly widened its activities to include developing countries. It is also interesting to mention that the BIS is not just an international organisation but also a bank; as such it offers banking services to virtually all central banks.

From the perspective of developing countries, it seems particularly important that the activities of the BIS – and of the committees that constitute the Basle process – increasingly achieve the two following objectives, which are of great importance to developing countries: 1) contribute as much and as effectively as possible to greater international financial stability and greater efficiency in financial markets world-wide, efficiency particularly in the sense of helping sustain growth and development. This pursuit of international stability by the BIS needs to include both the long-term objective of achieving greater financial market efficiency to help sustain both economic stability and growth, as well as future crisis prevention and better crisis management, to make financial crises less likely and less costly if they unfortunately do occur; and 2) have greater participation of developing countries in the management and activities of the BIS itself and in the different committees which are part of the Basle process, as these constitute an important part of the process of global financial governance. Given the seriousness of recent crises and of their dramatic negative effects on developing countries' economic evolution, the first objective seems particularly important and urgent; however, from the perspective of developing countries and the G-24 the second objective is also important, to assure that developing countries' concerns are addressed and their interests are sufficiently well represented. Furthermore, the effectiveness of BIS work related to LDCs would clearly benefit from greater involvement by LDCs in BIS work.

The BIS itself was created under international law with a specific mandate of promoting central bank cooperation for the purpose of maintaining global financial stability and providing additional facilities for international financial operations (Giovanoli, 1989; Helleiner, 1994).

However, the informal modality through which the BIS committees at present operate influences both their contribution to international financial stability and the participation of developing countries within this process. International co-operation at the BIS is based firmly on the principle of national (home) country control (Kapstein 1994). This starts from a diagnosis that sovereignty still resides at the level of the nation-state, and that Parliaments, particularly of large countries, (and especially the US Congress) are often unwilling to cede power to international bodies even though the economies – and particularly financial systems and capital flows – are increasingly globalised. Thus, the BIS committees do not operate as a supranational or multinational entity. Indeed, interestingly, there is no international law that provides a basis for all their global activities. Instead, in the BIS context, national central bankers and regulators meet regularly and negotiate among themselves – each pursuing national objectives and perceptions – and then reach compromise consensus agreements collectively. It is interesting that these collective agreements are when necessary often ratified by Ministers and Governors in their respective countries, and subsequently implemented using national legislation or regulation. Furthermore countries not participating in these discussions, e.g. developing countries, often also adopt the agreements reached through the Basle process. This is well illustrated by the capital adequacy standards adopted by the Basle Committee, which have been accepted by bank regulators world wide as effective global standards. The fact that agreements reached via this very ad-hoc process are accepted by national legislators and regulators world-wide is seen by senior BIS officials (White, 1998) to testify to the perceived legitimacy of the process itself. It could of course be argued that, as Central Banks world-wide increasingly become independent, they become less accountable to their national democratically elected institutions; to the extent that this weakens legitimacy of Central Banks at a national level, (which has as yet not emerged as a major issue, but may do so increasingly, especially where Central Banks are seen as excessively concerned with inflation, and not concerned with growth) the BIS could indirectly see its legitimacy weakened. In this respect, it may be desirable for the BIS - or its member Central Banks - to report to national Parliaments on its activities on a regular basis, to ensure transparency. (It should, however, be mentioned that most of BIS studies are either published or available on the internet.)

More broadly, an important question for the future role of the BIS is whether this process (of "bottom up" global regulation or "global governance on the quiet") continues to be appropriate as financial globalisation deepens and as the role of developing countries increases. If this is so, then the Basle ad-hoc methods of global governance need to be deepened and expanded, to include for example closer collaboration between different regulatory bodies (e.g. the Basle Committee, IOSCO and the Insurance Regulators). Indeed, a very important step along this path was taken by the G-7 Finance Ministers and Central Bank Governors when in February 1999 they created the Financial Stability Forum, with the purpose of ensuring more effective coordination between national and international authorities, relevant supervisory bodies, as well as reduce systemic risk. The Forum will be chaired for the first three years by Andrew Crockett, General Manager of the BIS. It will be supported by a small secretariat located in Basle. If however, this approach becomes increasingly insufficient to deal with the difficult and complex challenges of financial globalisation, a transition towards a more supranational approach may in the medium term be required, along the line of proposals made for a World Financial Authority (Eatwell and Taylor, 1998) though this will probably require more complex international negotiations and an international law or treaty.

Another important challenge, if the path chosen is a continuation and deepening of the BIS ad-hoc international governance, as the creation of the Financial Stability Forum indicates, is the growing need to include more participants from developing countries, which are playing an increasingly important role in international financial matters, and who suffer most from the effects of financial instability and currency crises. According to some observers, it may be difficult to make compatible an expansion of BIS membership with maintaining the intimate club-like modus operandi, which reportedly facilitates agreement and consensus decision-making. From the perspective of developing countries, the issue is, however, how they can become as integrated as possible into the BIS and its surrounding committees, in ways that assure that their interests are sufficiently represented. This issue has become also particularly relevant for the Forum for Financial Stability as no developing countries that are recipients of capital flows and that are prone to currency crises have as yet been invited to participate.

We will first (in Section II) examine the main features and functions of the BIS as well as of the Basle process.

Section III will first focus on the work for promoting financial stability and preventing crises, mainly carried out by the key BIS committees, of which the best known one is the Basle Committee; also of great importance are the Euro-currency Committee (recently renamed as the Committee on the Global Financial System) and the Committee on Payments and Settlements. Section III will then examine the role of the BIS in crisis management, particularly its contribution to the international financing packages put together for developing countries in crises. Both sections II and III will start by looking at the broad contribution of the BIS (which is mainly linked to G-10 countries) and then examine its specific and growing contribution to developing countries.

Section IV will examine fairly briefly the issue of membership and management of the BIS, as well as the participation of different countries, both in its broad meetings and in the work of its committees. The fairly limited, though increasing, role of developing countries will be examined.

Section V will look at how the BIS's work should continue to be deepened and above all broadened, particularly in relation to including developing countries and their interests in the BIS activities, but also in relation to integrating the regulatory activities of non-banking financial sectors more closely with the activities of the BIS and its committees.

Section VI concludes with specific policy recommendations including those for possible G-24 Ministerial action.

II MAIN FEATURES AND FUNCTIONS OF THE BIS AND THE BASLE PROCESS

A The BIS

The Bank's predominant tasks are summed up most succinctly in part of Article 3 of its original Statutes; they are "to promote the co-operation of central banks and to provide additional facilities for international financial operations". An important aim of this increasing central bank co-operation has been to promote international financial stability. With rapidly integrating financial markets in the world, and with risks of crises also increasingly spreading internationally, international central bank co-operation is becoming even more essential. Naturally central bank coordination at the BIS has also focussed on improved coherence of monetary policies in particular, and macro-economic policies in general, important subjects which escape the scope of this paper. Thus, the BIS is an important forum for international monetary and financial co-operation between central bankers and, increasingly, other regulators and supervisors. As the BIS (1998) itself puts it, "the stability of the international monetary and financial systems has long been a central concern of the central bankers' meetings at the BIS".

The BIS was founded in 1930 and is therefore the oldest international organisation in the field of international monetary cooperation (its first - temporary - mission was to channel payments linked to German reparations) (Giovanoli, op.cit., Helleiner, op.cit) It is interesting to note that in 1944, on the occasion of the Bretton Woods Conference, it was recommended that the BIS be liquidated, following the founding of the IMF. In the event, the BIS experienced a great expansion after World War II, and increasingly started collaboration with the IMF. The BIS played a key role in both the creation and operation of various intra-European payments arrangements in the post-World War II era, the Basle Governors' meetings generated initiatives which attempted to fight successive waves of speculation against different developed countries between 1960 and 1971, and it was the forum for the creation of the General Arrangements to Borrow (GAB), under which the G-10 plus Switzerland make resources available to the International Monetary Fund, outside their quotas. The Governors of the G-10 central banks meet regularly on the occasion of the Basle monthly meetings. These G-10 meetings of central bankers in Basle have become an important forum in which much wider activities –including setting up the key Basle Committees – have been put in motion by the G-10 central banks in the pursuit of international financial stability, for example in the fields of financial market monitoring, banking supervision, payment and settlements systems. While these meetings and activities traditionally focussed on events in the G-10 countries (looking at developments in LDCs more in terms of their impact on developed countries), an increasing number of meetings now focus on developments in emerging markets as well, or on the world economy. However, even when emerging markets countries are the focus of discussions, still too often the perspective from which developments in them are analysed is that of the G-10 countries. Indeed, some of the important meetings at which developing countries are discussed, are still reportedly only attended by G-10 country representatives, though Governors of the major developing countries (particularly from Asia and Latin America), as well as Russia are increasingly invited to attend.

Though much of the focus of the work done by the BIS (and of this paper) is on the financial system – both domestic and international - it is also important to underline the role of the BIS and its meetings in international co-ordination of monetary policy, as well as technical work and research on the conduct of monetary policy. In this context, it is interesting to stress that between 1964 and the end of 1993 the BIS hosted the Secretariat of the Committee of Governors of the Central Bank of the Member States of the European Economic Community (EEC). In this context, the Secretariat of the European Committee of Governors – based at the BIS – performed a number of key functions for the growing European integration, both of an operational nature – the BIS acted as Agent for the European Monetary Co-operation Fund – and in the context of preparation for the ERM and EMU. Indeed the Committee of

European Governors and the European Monetary Co-operation Fund, both serviced by the Secretariat based at the BIS, were the European Community bodies which provided for monetary co-operation in the European Community. It is interesting to note that these tasks were then taken over first by the European Monetary Institute which was headed by the former General Manager of the BIS, Alexander Lamfalussy (in January 1994), and then by the European Central Bank. The interesting point in the context of this study is that the loss of much of the work at the BIS on European monetary integration in 1994, was reportedly a fairly important incentive in encouraging the BIS to "fill this gap" by increasing its activities in relation to developing countries since 1994. It should, however, be stressed that this coincided with a period in which the need for a greater role for the BIS vis-à-vis developing countries sharply increased, particularly but not only due to the Mexican peso crisis and the East Asian crisis. Thus, the willingness and the need for a greater role for the BIS in relation to LDC's both sharply increased in the mid 1990's.

Though the direct role of the BIS in European monetary integration has diminished, the influence of European countries in the BIS (particularly amongst its staff) may be somewhat higher than in the IMF. This may be one important factor why the BIS has always tended to be more pragmatic on issues such as capital account and financial liberalisation in developing countries, tending to stress both costs and benefits, and always emphasising issues of timing and pre-conditions for successful liberalisation.

B The process of achieving agreements

The process of achieving agreements – on matters such as international standards for regulation of the financial sector in different countries – is a difficult one, as each country starts off with different traditions, accounting systems and domestic regulations; domestic firms press for minimising the extent and costs of any changes arising from international agreements. As pointed out briefly in the Introduction, the modality through which the BIS and, in particular, the Committees under the aegis of G-10 Central Bank Governors have operated has been via international co-operation based firmly on home country (state) control, rather than through entrusting it to some international institution. Members of the various committees which meet at the BIS negotiate positions amongst themselves, each reflecting more their national interests; each has also consulted with private sector actors, especially financial institutions, in his/her own country[1]. The aim is to reach a negotiated agreement acceptable to all G-10 countries, and to the public and private sector actors

[1] As matters are – and above all are perceived to be – broadly "technical", there tends to be little consultation at a more general level in national contexts. The question needs to be asked whether, in the interests of greater democracy and accountability, consultations should be broader at the national level, to include for example discussions in Parliament.

involved. These agreements are often ratified by Ministers and Governors of the G-10 countries, and – if required – are approved by G-10 legislatures. Even though the committees meetings at the BIS are basically drawn from G-10 countries, most of the agreements reached have been accepted and implemented by developing countries. The acceptance by non-G-10 countries, of standards agreed by G-10 countries, has been encouraged by the fact that non G-10 countries see them as broadly desirable. This is not only due to efforts made by various Basle committees to disseminate their agreements, but also because private rating agencies consider meeting Basle capital adequacy standards as an important element in rating financial institutions. The IMF, the World Bank and the regional development banks have also played a big role, especially through their surveillance and through conditions attached to their loans, in the spreading of the standards adopted by the BIS committees. Indeed, it was stressed in several of the meetings held at the BIS that there was a fairly sharp and important distinction, broadly seen as desirable, whereby institutions like the BIS, and the Committees linked to it, formulated standards and norms for financial sectors and institutions like the IMF and the World Bank, which help disseminate them and surveille their implementation in developing countries. As described below, the process of formulation of standards and norms is mainly done by G-10 representatives, though with increasing participation – and especially consultation – with some developing countries. The fact that basically the G-10 committees formulate standards and developing countries "accept" them assumes, possibly sometimes incorrectly, that the same standards are equally applicable to different categories of countries. Furthermore, the fact that LDCs are only partly represented in the deliberations on determining these standards, could reduce their legitimacy for developing countries. As Gerry Helleiner clearly puts it[2], the reaction from LDCs could be "no standardisation without representation".

It needs to be stressed that even though the process has been functional to achieving very important international agreements, it has not really been successful in preventing crises, even when the risk that provoked or contributed to the crisis had already been identified before the crisis. Thus, the Basle Committee on Banking Supervision was only set up in the wake of the failure of the Bankhaus Herstatt in 1974, even though it had been recognised for some time that banks with large operations posed special problems. Concrete work on forging international capital adequacy standards was encouraged by the Mexican debt crisis of 1982. The G-10 Committee on Payment and Settlement Systems was set up in 1990 following various periods of financial distress with international repercussions, as well as better understanding of the nature of risks in payments and settlements, particularly as a large increase in financial transactions occurred in the 1980s. On some occasions, the process has moved forward very slowly. Herstatt risk was identified (and named) in 1974, yet the first

[2] At UNCTAD meeting, January 1999.

initiatives were promulgated by the Committee on Payment and Settlements Systems only at the end of March 1996, that is 22 years later! Fortunately, Herstatt risk did not cause any major international problem during that period, arguably mainly due to luck. Thus, to a certain extent, the CPSS does provide an example of central bank preventative actions being implemented before a crisis happens.

More generally, the agreements which have been reached probably have contributed to prevent crises that would have otherwise happened or moderated ones that have occurred. Furthermore, it should be stressed that the tasks of regulators, both nationally and in their international co-ordination, are made particularly difficult due to two types of problems. First, information asymmetries normally identified for market actors, also operate, to a certain extent, for regulators. When a new instrument or sector is developed, it is difficult also for regulators to determine precisely the nature and seriousness of the risks involved, although previous experience, as well as theory, can help sketch the broad contours of the risks involved. Secondly, when new financial markets or instruments are being developed, there is a sense of excitement in the markets, which is encouraged both by the novelty and the large profits that are normally made. A wave of "market knows best" sentiments is frequently transmitted to governments and regulators. Once an important failure – or crisis – has occurred, both information on the precise risks involved and awareness of the dangers involved increase substantially; as a result, regulatory action is usually taken.

It also seems interesting to mention that, though the process broadly operates via consensus agreements amongst the G-10, the more powerful members of the G-10 have, at various times, forced the process in rather unconventional ways. In the mid-1980's, progress in harmonising approaches for capital adequacy standards were seen as "too slow" by US authorities. The US and the UK, representing the two largest financial centres by far, struck a bilateral deal, based on the UK approach to risk-weighted capital standards. This sharply increased the intensity and speed of negotiations in the Basle Committee, and contributed to the Capital Adequacy agreement (Helleiner, op. cit., Kapstein, op. cit. and White, 1996).

One important future challenge for the Basle process is the clear need to include participants from developing countries directly in the Committees, on a more systematic and formal basis (for progress, see below). This is so not only because several developing countries are major financial and economic actors; it is also because many of the key issues relating to international financial stability relate to and deeply affect developing countries. The increase of the participants in the meetings should be done in ways that do not detract from the efficiency involved in making decisions through the Basle Committees. It has, for example, been argued that one of the reasons why the Basle Committees are more efficient in reaching agreements than the world-wide organisation of securities' regulators (IOSCO) is because the former have a far smaller membership, which has shared values and conceptual frameworks, and allows it to operated in a "club-like" atmosphere. However, these problems should not be over-stated, as mechanisms (such as a rotating membership) can be found to make consistent a far broader representation in the Basle process (to include different categories of developing countries including poorer and smaller countries) with continued efficiency in decision-making.

It is also extremely important that not only offshore centres be increasingly incorporated into the Basle process, but also that mechanisms be found that such offshore centres do not continue to make difficult or impossible desirable changes in regulation. Indeed, in recent discussions on the possible need to regulate institutional investors - such as mutual funds or hedge funds – the main argument against such regulation (even by those who see it as desirable to diminish the risks of currency crises) has been that any such regulations would be avoided by a flight to offshore centres. Therefore, a crucial element for improving global regulation is to explore ways in which – at least for those aspects, though also ideally for taxation purposes – offshore centres come onshore. It is in this respect very encouraging that one of the three Working Groups of the Financial Stability Forum is devoted to offshore centres. It is to be hoped that it will address not only its main brief, which is the important issue whether offshore centres undermine global stability, but also the issue of whether offshore centres make desirable regulation less feasible.

III HOW DO THE BIS AND THE BASLE COMMITTEES PROMOTE FINANCIAL STABILITY?

A Introduction

Actions to encourage financial stability – both nationally and internationally – can be broadly classified as directed either to prevention of crises and/or to crisis management and resolution.

Clearly crisis prevention is better, cheaper and more effective for sustaining growth than crisis management or resolution. The parallels with medicine are clear here. However, good crisis management is also important if crises do occur. As the British Chancellor of the Exchequer, Gordon Brown, clearly put it (Brown, 1998), "our aim must be crisis prevention where possible, crisis resolution where necessary". In this context, it is interesting that the BIS and the Committees round it have focussed particularly strongly on activities relating to financial crisis prevention, especially on measures that strengthen the financial sector both within countries and internationally. Indeed, it should be emphasised that the BIS and its Committees are clearly the main focus of international co-ordination of financial sector regulation. This is particularly true for banking systems, but is also increasingly true in relation to co-ordination with regulators of insurance; indeed, the Secretariat of the International Association of Insurance Supervisors (IAIS) is now based in Basle, in the BIS building (for a summary of activities by the IAIS, please see Appendix 1). Links are also growing with IOSCO, particularly in the context of the Joint Forum (see below). Several senior BIS officials even expressed the hope that the IOSCO Secretariat could move to – or at least be permanently represented in – Basle, so that the three main official sectors' regulators would be fully represented there. The BIS has made an offer to IOSCO to relocate its secretariat in Basle (White 1999). This seems a very good suggestion. The fact that the BIS and the Basle Committees increasingly play this absolutely central role in the co-ordination of international financial regulation seemed to make it the obvious starting point for any future even more integrated global financial regulation, such as an international supervisory surveillance secretariat, first proposed by the Canadian government in April 1998, built on in the Standing Committee for Global Financial Regulation proposed by Clare Short and Gordon Brown to the October 1998 Development Committee or indeed for a super-regulator, that at a later stage would attempt to fully integrate global regulation between the different financial sectors and internationally.

The Financial Stability Forum

In October 1998, the G-7 finance ministers and central bank governors approved this idea in principle and asked Hans Tietmeyer, then president of the Bundesbank, to develop the UK proposal and more generally consider the cooperation and coordination between the various international regulatory and supervisory bodies and to make recommendations for any new arrangements. Tietmeyer's report, released in February 1999, outlined areas where improvements to current arrangements were necessary, but stated that 'Sweeping institutional changes are not needed to realise these improvements' (Tietmeyer, 1999). Instead it was proposed that a Financial Stability Forum, which would meet regularly to discuss issues affecting the global financial system and to identify actions needed to enhance stability, be convened. The Forum was formally endorsed by finance ministers and central bank governors from the G-7 at their February meeting in Bonn (see Appendix 2), and met already for the first time in the spring of 1999.

The Tietmeyer report had correctly outlined three main areas for improvement to current arrangements which have been highlighted by recent events in international financial markets: a) identify vulnerabilities in national and international financial systems and sources of systemic risk and to identify effective policies to mitigate them; b) ensure that international rules and standards of best practice are developed and implemented, and that gaps in standards are identified and filled; and c) improved arrangements are needed to ensure consistent international rules and arrangements across all types of financial institutions.

The Financial Stability Forum was initially limited in size to 35 members, in order to allow for an effective exchange of views and decision making. Each G-7 country will have three representatives on the Forum, from the finance ministry, central bank and supervisory authority. The G-7 stated that while the Forum will initially be limited to G-7 countries, it is envisaged that other national authorities, also from emerging market countries, will join the process at some stage. The International Monetary Fund (IMF) and the World Bank will have two representatives each, as will the Basle Committee on Banking Supervision, the International Organisation of Securities Commissions (IOSCO), and the International Association of Insurance Supervisors (IAIS). The Bank for International Settlements (BIS), the Organisation for Economic Co-operation and Development (OECD), and the two BIS Committees will all have one representative on the Forum.

The Forum will be chaired by Andrew Crockett, general manager of the BIS, for the first three years and it will have a very small secretariat in Basle. The Forum will initially meet twice a year, beginning in the spring of 1999. One of the key aims of the Forum will be to better coordinate the responsibilities of the main national and international authorities and supervisory bodies, and to pool the information held by these various bodies, in order to improve the functioning of markets and reduce systemic risk. Subsequent to its meeting in Washington on 14th April, the Financial Stability Forum has defined three ad hoc working groups, to tackle recommendations on three subjects defined as key:

a) to recommend actions to reduce the destabilising potential of institutions employing a high degree of leverage (HLIs) in the financial markets of developed and developing economies; this group will be chaired by Mr Howard Davies, Chairman of the UK Financial Services.

b) to evaluate measures in borrower and creditor countries that could reduce the volatility of capital flows and the risks to financial systems of excessive short-term external indebtedness; this group will be chaired by Mr Mario Draghi. Amongst developing countries, Chile and Malaysia are participating.

c) to evaluate the impact on global financial stability of the uses made by market participants of financial offshore centres, and the progress made by such centres in enforcing international prudential standards and in complying with cross-border information exchange agreements. As regards offshore centres, an assessment will be made of the additional efforts required to avoid under-regulation or inappropriate disclosure in offshore centres contributing to global financial instability. This group will be chaired by Mr John Palmer, Superintendent of Financial Institutions.

It is important to stress that the working groups comprise officials of developed and developing market economies, international financial institutions and supervisory groupings, and will draw on work completed or under way in various public and private sector forums. It is interesting that senior officials from developing countries have been included, where their expertise is seen as particularly relevant. For example, the group that will study measures to study volatility of capital flows includes senior representatives from Chile and Malaysia, two countries that have implemented measures to curb inflows and outflows (Malaysia for both, and Chile for inflows).

The setting up of the Financial Stability Forum is clearly a very necessary, and valuable first step towards improving the coordination and cooperation of the various bodies which work towards improving the way markets work in order to improve global stability. The question lies, however, in whether the Forum, as it has been proposed, will be a representative enough and strong enough body to address all these complex issues.

First, the omission of any developing country authorities in the initial years of the Forum itself appears to be an important error. It has been increasingly accepted, especially since the Mexican peso crisis and the current international financial crisis, that international finance is more and more globalised, that developing countries are important actors in this globalised financial system, and that currency crises in LDCs pose both systemic threats to the international financial system and threats to their development prospects. The experiences of developing countries, will not be directly represented at the Forum itself. Representation of developing countries on the Forum would be desirable for both legitimacy reasons, and because it would provide the body with a wider range of expertise and perspectives. However, the representation of developing countries in the ad-hoc Working Groups is clearly a positive development.

Ways could easily be found to include developing countries in the Forum without making it too large. If three developing countries representatives were included, the membership of the Forum would rise from 35 to 38, that is by less than 10%. Developing country representatives, from countries with large levels of private capital inflows or who have major financial centres could for example be chosen on a regional basis; there could be one Asian, one Latin American and one African. This would also ensure that the interests of poorer countries are represented. The representatives could be appointed for a fairly short period (e.g. 2 years) and then rotated. This type of representation by developing countries has been working rather well in other contexts, for example in the Boards of the Bretton Woods institutions.

The Forum for Financial Stability is a very important initiative, that hopefully will reduce vulnerabilities in the international financial system, by promoting coordination and cooperation among G-7 regulators, central bankers and international financial institutions. Adding a small representation from developing countries to the Forum would increase those countries' commitment to its aims, as well as add valuable insights to its decision-making process. It would seem to be beneficial to all involved.

Second, doubts have been voiced over the institutional strength of the new Financial Stability Forum. With a very small secretariat in Basle (currently it has only three staff members), meeting only twice yearly, and no power of enforcement, will the Forum have the sufficient institutional muscle to deal with the tasks that have been identified? Can its response be speedy and agile enough to a rapidly changing international private system? The setting up of the Forum represents a significant enhancement of the system of global regulation by agreement and peer pressure that has been shown to work reasonably well in the context of the Basle Committees of the BIS, as discussed above. However, in the medium term, in a world of open financial markets, an international body whose Board meets regularly and has the power to make and enforce policy may well be needed. This would point towards a body more akin to some kind of World Financial Authority, which would be endowed with executive powers along the lines of a WTO for finance.

In the meantime, however, the Financial Stability Forum is a very important step in the right direction. Time will tell whether this body is sufficient to promote international financial stability, and to fill the important gaps in financial regulations which undermine such stability.

The BIS also plays an important role, though a somewhat more secondary one, in crisis management and resolution, especially as relates to crises affecting developing countries. The lead role here is played by the IMF which not only puts together the main financial package, but also imposes conditionality on developing countries in crises. However, even if secondary, the role which the BIS plays in contributing to the financial packages is very important and growing for at least three reasons. Firstly, given the size of the financial packages required, particularly in the context of capital account–led balance of payments crises, the contributions that the BIS can assemble – drawing mainly on credits from the G-10 central banks – have the advantage of additionality and of flexibility. The flexibility relates to the fact that the scale of the contributions are not linked to formal limits, such as the size of the IMF quotas, but depend solely on the scale of the problem and the political willingness to lend. Secondly, the loans co-ordinated by the BIS are not explicitly linked to additional conditionality for developing countries, though their disbursement may be linked to meeting IMF conditionality. Loans without policy conditionality are particularly appropriate for providing finance to developing countries with capital account led crisis not caused by their own policy mistakes, but by external factors, such as contagion and imperfections in international capital markets. Thirdly, the most recent loan co-ordinated by the BIS – that for Brazil (see below) – was not a bridge loan as all other BIS loans to developing countries have been, but a proper credit facility, granted for one year. This is an interesting innovation, as was the fact that the BIS loan was part of what could be called a preventive financing package rather than one of full crisis management.

B Crisis prevention

A central element in crisis prevention, both in developing countries and internationally, is strengthening financial systems, to make them more robust, so they do not spark off financial crises and do not amplify them if the crisis is caused by other factors, such as macro-economic or external.

As White (1996, 1998) has suggested, the international financial system can be seen to be based on three pillars: financial institutions, financial markets, and payment and settlement systems. In this context, measures to prevent crises can be classified in a three dimensional matrix. The columns comprise the different categories of financial institutions, including banks, investment dealers, insurance companies, hedge funds and others. The rows are the markets for the individual operations, a growing proportion of which are tradable. Behind this façade is a third dimension comprising the supporting infrastructure (or "plumbing" as it is known in the jargon) for the international financial system, including the payment systems, as well as the clearing, netting and settlement systems. The infrastructure is one of the most rapidly changing dimensions in the international financial system, as new systems emerge (e.g. in trading in derivatives) and others are greatly modified. Disturbances at the level of financial institutions, markets or infrastructure can not only interact very negatively with each other (e.g. sharp changes in the prices of financial assets determined in financial markets can contribute to undermine the solvency of financial institutions, as occurred in East Asia); disturbances in some or all of these dimensions can also have very large and disruptive implications for key macro-economic variables, such as interest rates and exchange rates.

A number of international agreements have been reached over the years to strengthen the three dimensions of the matrix, financial institutions, financial markets, and financial infrastructure. A very central part – though not all – of the work has been carried out by three BIS Committees; indeed, there exists a BIS committee dealing with each of these individual pillars. Thus, the Basle Committee on Banking Institutions deals with one of the key sectors of financial institutions (banks), though not with other institutions, where the co-ordination of the regulation is either carried out by other regulators (e.g. securities and insurance) or there are regulatory gaps (e.g. hedge funds). The former Euro-currency Standing Committee deals with financial market developments thought likely to have systemic implications, as well as collecting crucial data on market developments. Finally, the Committee on Payments and Settlements Systems deals with international agreements on the crucial issue of strengthening the financial infrastructure.

THE BASLE COMMITTEE ON BANKING SUPERVISION

The Basle Committee on Banking Supervision, which is the most well known of the committees which have their secretariat at the BIS, was established by the central bank governors of the Group of Ten countries in 1975. Since its creation, the Basle Committee has been working to improve banking supervision at the international level. The work of the Committee covers three main areas. Firstly, it provides a forum for discussion on supervisory issues. Secondly, it co-ordinates the supervision of international banking groups and their cross border activities. Thirdly, it aims to improve financial stability by improving standards of supervision. The Basle Committee is made up of senior representatives of bank supervisory authorities and central banks from twelve countries; the G-10 plus Switzerland and Luxembourg.

While the work of the Basle Committee was originally centred on supervisory issues arising in the context of the G-10 countries, the rapid pace of globalisation, and the resulting need for international co-operation to involve a wider group of countries, have been reflected in the recent efforts of the Basle Committee to extend its reach. In the last few years, the Basle Committee has been expanding its links with non-member countries in order to strengthen prudential supervisory standards in all the major markets (for details, see below). For developing countries pursuing financial integration in the global economy, a sound banking system with an adequate regulatory and supervisory framework is one of the main prerequisites (World Bank: 1997). The Basle Committee has made a contribution to promote financial stability, through the definition of sound supervisory practices, both within countries and internationally. It is also increasingly active in helping their implementation in non-member countries (see below). Especially due to the complexities of properly implementing banking supervision in developing countries, further efforts in this direction seem desirable and urgent.

The Basle Concordat (1975) to The Supervision of Cross-border Banking (1996)

The early concerns of the Basle Committee focused on ensuring that all internationally active banks were adequately supervised on a consolidated basis. In 1975, the Basle Committee issued the Basle Concordat which established the principle that no foreign banking establishment should escape supervision, and that the home supervisor is responsible for the global operations of banks headquartered in their territory and should supervise them on a consolidated basis. The Concordat has been revised a number of times since then, but the basic principles have remained the same.

In 1992, the Basle Committee produced its report '*Minimum Standards for the Supervision of International Banking Groups and their Cross-border Establishments*'. In this report, basic standards were set out to ensure that home supervisors do undertake effective supervision, and that they have adequate access to information about the cross-border activities of banks. If these standards are not met, host countries can refuse to grant a banking license or home supervisors can close a bank down. However, continued concern over the adequacy of the information available to supervisors prompted the preparation of a further report by a joint working group of the Basle Committee and the Offshore group of Banking Supervisors. This report, *The Supervision of Cross-border Banking*, presents 29 recommendations designed to strengthen the effectiveness of supervision of home and host-country authorities of banks which operate beyond their national borders.

The Capital Adequacy Agreements

In 1987, the Basle Committee published proposed guidelines for the measurement and assessment of the capital adequacy of banks operating internationally. In 1988, the guidelines were approved by bank supervisors of the G-10 countries plus Luxembourg and Switzerland. Under the agreement, known as the *Basle Capital Accord*, bank supervisors of these countries were obliged to impose a minimum risk-adjusted capital asset ratio of eight per cent on all banks operating under their jurisdiction by the end of 1992.

The agreement was intended to establish common regulatory conditions among the banks of participating countries in order to prevent unfair competition arising due to lighter regulatory conditions in some countries, and also to raise the levels of bank capital in the G-10 countries. Despite some drawbacks, to which we will turn below, the Capital Accord succeeded in establishing standards by which all banks can be compared, and resulted in a strengthening of bank capital among the G-10 countries. The widespread compliance with the Basle Capital Accord among the G-10 countries can be put down to a combination of pressure from domestic supervisors, acting under international peer pressure, and market discipline (White:1996). For reasons discussed above, the capital adequacy guidelines have been voluntarily accepted also by an increasing number of countries, including many of the developing economies.

Originally, the Capital Accord centred on credit risk in the calculation of capital adequacy. During the 1990s, the Basle Committee has been working on refining the capital adequacy standards to take account of market risk, particularly that arising from the huge increase in bank trading in futures and options. A major revision was introduced in 1995 when the Committee issued a set of recommendations extending the capital requirements to market risk, in which the Committee accepted the use of internal risk management systems (subject to certain restrictions) of financial institutions to determine their exposure to market risk. This was seen by some observers as an important step towards regulators working more closely with the market. There are, however, several concerns about this new approach including worries that the internal analysis of risk for capital adequacy purposes may result in lower requirements than a standard approach would (Griffith-Jones, 1998a). Supervisors will need to bear this concern in mind when looking at the capital requirements of financial institutions.

While the Capital Accord has been an extremely useful tool for the universal comparison of financial institutions, it has been shown to have certain shortcomings and further work on revising capital adequacy requirements will be necessary. One example, which became evident in the analysis of the recent international financial crisis, is that the current categories for risk weighting bank assets introduce a bias in favour of short-term lending. The current BIS recommended risk weight for claims on non-OECD institutions with a residual maturity of up to one year is 20 per cent, whereas claims over one year have a recommended risk weight of 100 per cent. This makes short-term lending to non-OECD countries more profitable than long-term lending for international banks, and this may have contributed to the heavy build-up of short-term debt in some East Asian countries immediately prior to the recent crisis. It may therefore be desirable to diminish the regulatory incentive towards short-term lending, for example by narrowing the difference between capital adequacy requirements for long and short-term credits (Griffith-Jones, 1998b). A further distinction in the capital adequacy rules which may require revision is that between OECD and non-OECD countries, as has repeatedly pointed out in G-24 communiqués. A more appropriate distinction may be one based on the quality of banking supervision. Well after the first draft of this paper was written, the Basle Committee on Banking Supervision published a consultative paper outlining on the Capital Accord the planned shape of a broader reform of capital adequacy ratios (June 3, 1999). It was somewhat disappointing both in that it took such a long time to produce, and its proposals are still at an early stage of development, and have now been submitted for consultation. However, urgent action is required.

As regards the acceptance of the capital adequacy guidelines by developing countries, problems have arisen due to the failure to adjust bank capital adequately for non-performing loans. This is because emerging market countries often have poorly developed accounting standards and insufficient information on the quality of bank assets (Fitzgerald, 1998). This problem was also highlighted by the recent crisis in East Asia, when apparently well capitalised banks were revealed as insolvent as the crisis unfolded (BIS, 1998). This raises the broader issue that capital adequacy and provisioning requirements should possibly have either an explicit or an implicit countercyclical element whereby standards are tightened during periods of "booms" and surges of capital, and somewhat loosened during periods of "busts" and capital out flows. (see Griffith-Jones and Ocampo, 1999). Such regulatory practice could help moderate excessive swings in bank lending, which currently exaggerate both overheating of the economy and recessions. Current practice – where regulation is introduced more rigorously during a crises – has the opposite and often undesirable procyclical effect[3]. The fact that LDCs seem to be more prone to crises – and that these often lead to numerous company bankruptcies - raises the issue of whether capital adequacy standards in those countries should be higher (as is the case for example in Argentina). The costs and benefits of such higher capital adequacy standards for developing countries need to be carefully evaluated, and it seems far more desirable that this is done by developing

[3] Remarks by Joseph Stiglitz, at UNCTAD meeting, January 1999.

countries themselves, and not that general standards are imposed. However, analysis of international experiences in this area, by the Basle Committee or the BIS could be very valuable.

The capital adequacy agreements will also face new challenges in the future, such as those presented by bank lending to hedge funds or for derivative operations, which may require further changes to regulation. Moreover, in the context of developing countries, it is important to bear in mind that standards set among G-10 nations, such as the capital adequacy standards, represent minimum requirements and that in the case of some LDCs it may be prudent to set higher capital/asset ratios.

The Core Principles

In April 1997, the Basle Committee released a set of *Core Principles for Effective Banking Supervision* backed by a three-volume Compendium of guidance documents. These guidelines, which were mainly based on the work and decisions of the Committee over the previous two decades, cover all aspects of banking and are intended to be applied to all banks. The 25 Core Principles, which are designed to serve as a basic reference for national agencies world-wide to use in the supervision of all banking organisations within their jurisdictions, cover seven broad topics: (1) the preconditions for effective banking supervision; (2) licensing and structure; (3) prudential regulations and requirements; (4) methods of ongoing banking supervision; (5) information requirements; (6) formal powers of supervisors; and (7) cross-border banking (BIS:1997).

In developing the principles, the Committee worked closely with the supervisory authorities in fifteen emerging market countries. The document was prepared by representatives of the Basle Committee and from Chile, the Czech Republic, Hong Kong, Mexico, and Russia. Nine other countries were also closely associated with the work: Argentina, Brazil, Hungary, India, Indonesia, Korea, Malaysia, Poland and Singapore. This was a major step for Basle Committee towards increasing the participation of emerging market countries in their discussions and decision-making processes.

The Asian crisis revealed distinct weaknesses in the supervisory structures in many emerging market countries, and highlighted the relevance of the Core Principles. The Basle Committee believes that achieving consistency with the Core Principles in all countries will be an important step towards improving financial stability, both within countries and globally. However, while the Principles represent a set of extremely useful minimum standards with which all countries can strive to comply, it is important not to see them as a panacea to financial instability. Additionally, implementing the Core Principles in all countries is likely to be a lengthy and complex process, complicated by issues such as varying accounting standards in different countries.

Thus, the main challenge for the BIS, and other institutions such as the IMF, is to ensure that the Core Principles are implemented globally. The BIS began by asking supervisors around the world to endorse the Core Principles. To provide a forum for the discussion of problems associated with implementation, the Basle Committee has created a Liaison Group and a wider Consultation Group of G-10 and non G-10 countries. In 1998, the Liaison Group conducted a survey on implementation designed to identify the steps that supervisory authorities are taking to implement the Core Principles, the problems they face, and the assistance which they may require (BIS:1998). It would be very important and urgent for the BIS to expand its activities in this field, so as to assist developing countries - including the poorer and smaller ones - with technical assistance in matters such as implementing the Core Principles for Banking. The BIS Financial Stability Institute described below would provide a natural basis for this, but complementary action - focussed more on in-country training - seems also to be required. Given the BIS's expertise and role in setting standards it seems very well qualified to play a complementary role to that beginning to be developed by the IMF and the World Bank. This seems a very important function for the BIS, if one looks from the perspective of developing countries and their needs to improve the strength of their financial systems.

While the Basle Core Principles are intended to serve as a basic reference for supervisory bodies world-wide, they represent minimum requirements and may need to be supplemented by other measures designed to address particular conditions and risks in the financial systems of individual countries.

Broadening the Work of the Basle Committee - The 'Joint Forum' and the involvement of Non-Member Countries

In order to address new challenges presented by the breakdown of barriers between different sectors of the financial world and the growth of financial conglomerates, the Basle Committee has been strengthening its links with international supervisors working in other financial sectors. In early 1996, the Joint Forum on Financial Conglomerates was established, bringing together representatives from the Basle Committee, the International Organisation of Securities Commissions (IOSCO), and the International Association of Insurance Supervisors (IAIS). Thirteen developed countries are represented in the Joint

Forum: Australia, Belgium, Canada, France, Germany, Italy, Japan, Netherlands, Spain, Sweden, Switzerland, the United Kingdom, and the United States.

The Joint Forum has reviewed the means to facilitate information sharing between supervisors, both within their own sectors and in different sectors, and ways to enhance supervisory co-ordination. The Joint Forum is also working on issues concerning intra-group transactions and exposures within financial conglomerates. In February 1998, the Joint Forum issued a package of consultative papers addressing several different aspects relating to the supervision of financial conglomerates. Despite these efforts to enhance supervisory co-ordination, progress in establishing a consolidated supervisory framework has been slow.

The Basle Committee has also been broadening its work in respect of expanding its links with non-member countries. As discussed above, the Core Principles were drawn up with the active participation of official representatives from emerging markets. This marked an important step in encouraging the formal involvement of non-member countries in the deliberations of the Committee. Other recent efforts to expand the work of the Basle Committee to non-member countries include: the dissemination throughout the world of policy papers on a wide range of supervisory matters; the creation of a network of supervisory authorities who meet at an international conference every two years; the creation of regional supervisory committees to enhance supervisory co-operation at the local level; and the provision of some supervisory training both in Basle and regionally.

THE COMMITTEE ON THE GLOBAL FINANCIAL SYSTEM (TILL RECENTLY THE EURO-CURRENCY STANDING COMMITTEE)

The Global Financial System committee works on another of the three pillars of financial systems, that of financial markets. The Committee monitors developments in international financial markets and discusses issues which affect their functioning and stability. The tasks performed by the Committee have been recently re-defined to fall into three categories (for details, please see Appendix 3): systematic short-term monitoring of global financial system conditions, so as to identify potential sources of stress; in-depth longer-term analysis of the functioning of financial markets; and the articulation of policy recommendations aimed at improving market functioning and promoting stability. The Euro-Currency Committee was originally established to examine the expansion of bank lending, and was concerned with issues arising from the debt crisis during the 1980s.

More recently the Committee has been concerned with issues such as the growth of credit derivatives markets and capital flows to developing countries, as well as broader issues such as the implications for the banking industry of changes resulting from technological progress, increasing globalisation and product innovation.

The BIS compiles, analyses and publishes a wide range of statistical data on developments in international banking and financial markets under a mandate from the Euro-Currency Committee. The *BIS Consolidated International Banking Statistics* (formerly, The Maturity, Sectoral and Nationality Distribution of International Bank Lending), which is a key source of information on creditor exposures and countries' external debt, is an important example. Under a mandate from the Committee, the BIS collects and publishes these statistics from national (creditor) sources, in order that risks arising from this area of market activity can be monitored.

The banking statistics produced by the BIS can be used to draw attention to strains in international markets, as was the case in the period immediately preceding the recent troubles in East Asia. In the *1997 BIS Annual Report*, the financial fragility in some Asian countries, particularly Indonesia, Malaysia, the Philippines, and Thailand, had been highlighted (see pages 107-114). The report drew attention to the heavy exposure of some of the region's banks to short-term foreign currency financing, problems encountered by countries with recently liberalised financial sectors, and other issues, such as directed lending, which were later to feature in many analyses of the financial crisis in East Asia.

Unfortunately, although the BIS was able to use its data to compile an extremely accurate picture of the weaknesses building up in some Asian economies, the low-key expression of their concerns, presumably designed not to be alarmist, meant that the warnings went unheeded. Partly in response to the Asian crisis, the Euro-Currency Standing Committee has to agree a number of proposals for improving the *BIS International Banking Statistics* in terms of coverage, quality and timeliness. It was decided that lags in the reporting of data to the BIS and in the release of data to the public are to be reduced, reporting will now be on a quarterly best-efforts basis, there will be a move to report exposures on an 'ultimate risk' basis, and efforts to add new reporting countries will be intensified (BIS:1998:174). While these improvements will be very valuable, there is also a case for an analysis based on this data to be made more widely available and for concerns to be more strongly voiced.

The BIS is now also maintaining an extensive data base on international securities markets and has also expanded its coverage of derivatives markets. The growth of financial innovations, such as over-the-counter derivatives, while designed to facilitate the transfer of market risk and therefore enhance financial stability, have also made financial markets more complex and opaque. This has created difficulties in monitoring patterns of activity in these markets and the distribution of risks in the global financial system for regulators, central banks, market participants and other authorities. BIS studies have suggested that improved information on the size and structure of derivatives markets is needed to enhance their transparency and facilitate a more comprehensive monitoring for systemic risk.

In response to this situation, the Committee on the Global Financial System has also drawn up a framework for the regular collection of statistics on over-the-counter derivatives markets on the basis of reporting by leading market participants. These statistics will be compiled by national central banks and published by the BIS on a semi-annual basis. In addition the BIS also publishes the results of the triennial survey conducted by central banks (*Central Bank Survey of Foreign Exchange and Derivatives Market Activity*). These efforts to improve transparency, particularly in relation to derivatives, are widely welcomed. However, this sector is constantly evolving and there is a concern that regulatory reporting will never be able to keep pace with this complex and dynamic market. Difficulties are made greater by the fact that there are already many gaps in reporting derivatives; it would seem appropriate for major Central Banks and the BIS to attempt to improve registration of derivatives, by making it obligatory.

This Committee also works on longer-term analyses of structural developments which impact on financial stability. In 1997, the reports from two working groups, set up the previous year, were presented to the Committee. The first examined the implications for systemic risk of recent structural changes in financial markets, such as the emergence of non-bank financial institutions as providers of services traditionally carried out by banks. The second working group examined changes in portfolio management practices with the aim of developing a better understanding of cross-border capital flows.

THE COMMITTEE ON PAYMENT AND SETTLEMENT SYSTEMS

The Committee on Payment and Settlement Systems works to identify, define and promote ways to reduce risks and improve the efficiency of national and cross-border payment and settlement systems, including those for securities and foreign exchange market transactions.

With the increase in the volume of financial transactions in recent years, the exposure of firms to possible non-payment by a counterparty has risen significantly and the Committee has made many proposals on how payment and settlement systems could be strengthened. Much of the Committee's work focuses on interbank fund transfer systems, as banks continue to be at the centre of the international financial system. In 1997, the Committee produced a *Report on Real-Time Gross Settlement systems*. This report provides an overview of real-time settlement systems, which are now in place in most G-10 and some other countries, as well as looking at the risks associated with such systems.

In recent years, the Committee has also extended its work to cover settlement systems for securities and foreign exchange, and clearing arrangements for exchange-traded derivatives. To further this work, the Committee has extended its co-operation with other international regulatory authorities, such as a recent joint initiative with IOSCO which set out a disclosure framework for securities and settlement systems. In 1996, the Committee reached an agreement on exposure to settlement risk in foreign exchange markets (or Herstatt risk). In their report, the Committee established that such settlement exposures are much larger than had been estimated and also indicated ways in which market participants could reduce risks.

In order to further their work in these areas, the Committee has also been fostering closer links with non G-10 central banks, particularly those of developing economies. This has taken the form of meetings between the Committee and non G-10 central banks, and payment systems seminars and workshops which have been organised in conjunction with the BIS for various regional central bank groups. In developing a *Core Principles* for Payment and Settlements Systems, the Committee involved the central banks of a number of emerging market countries; Brazil, Mexico, Russia, Hungary, West African Central Banks, Malaysia, Hong Kong, Saudi Arabia, South Africa and Singapore. Such co-operation is very positive. However, it is important to note that countries which are at different stages of financial development do have different concerns and priorities. Whereas some emerging market countries are primarily concerned with establishing efficient and quick, basic payment and settlement systems, such as cheque clearing, the G-10 countries are more concerned about reducing risk in payment and settlement systems. Therefore, some division of labour may be justified in the operation of this Committee.

THE FINANCIAL STABILITY INSTITUTE

In response to the need to strengthen financial systems worldwide, the BIS and the Basle Committee on Banking Supervision have recently established the Financial Stability Institute. The Institute will focus on promoting better and more independent supervision of banking, capital markets and insurance services. The Institute will also promote the implementation of the Core Principles for Banking Supervision. The Institute will mainly achieve these objectives through workshops, seminars and other activities that will disseminate best supervisory practice. As discussed above, it would seem desirable for these activities to be complemented by training in developing countries.

The Financial Stability Institute will try to facilitate interaction between the private sector, central banks and supervisory authorities and is hoping to establish close links with organisations such as the IMF and the World Bank. The Institute will also develop links with the Toronto International Leadership Centre for Financial Sector Supervision ('The Toronto Centre'), sponsored by the World Bank and the Government of Canada, which helps bank supervisors from emerging market countries to share experiences with other bank supervisors and facilitates the exchange of information.

As the blurring of the barriers between the different areas of the financial sector increases, the need for a co-ordinated approach to financial sector supervision becomes more pressing. It is planned that in the future the Financial Stability Institute will broaden its coverage to include other areas of the financial sector, looking at issues such as the implementation of *Core Principles* currently being developed for the securities and insurance sectors.

C The role of the BIS in crisis management

Efforts to promote financial stability, such as the work of the three committees based at the BIS, are essential. However, in the increasingly complex global economy, financial crises have unfortunately occurred with increasing frequency. The experience of the 1990s has shown this all too clearly, with the crises in Mexico and East Asia having the most profound effects on the developing countries.

Crises are unpredictable, and often unfold extremely quickly. It is therefore essential that good lines of communication are established and maintained between the major actors in a crisis (the central bank, the Treasury, supervisory bodies of different countries) in order that each is well informed and decisions can be reached quickly. As we have seen in Part II, the BIS seems to play a positive role in facilitating communication between major international financial actors, particularly central bank governors and other regulators. As White (1998) points out, the BIS's most important contribution to crisis management is ensuring that policymakers know each other well and have open lines of communication.

The international community, in particular the G-10 central banks, have also provided bridge loans through the BIS to countries experiencing financial difficulties which are waiting for funds from the World Bank or other IFIs. Bridge loans can provide necessary liquidity and can also signal international support for policy changes undertaken by an economy which has run into financial difficulties.

In 1995, in response to the Mexican peso crisis, the BIS co-ordinated two international financial support programmes for Mexico and Argentina. As part of the international support programme for Mexico put together in early 1995, the BIS arranged a short-term credit facility of up to US$10 billion in favour of the central bank of Mexico. This facility, which was backed by a group of participating central banks, was available from March to September 1995, but was never activated. In the same year, the BIS granted a bridging loan of up to US$1 billion to the central bank of Argentina. This facility was made available in six separate tranches, from April to September 1995, to prefinance loans from the World Bank and the Inter-American Development Bank.

The BIS has also played a role in the international response to the financial crisis which unfolded across the globe in late 1997 and throughout 1998. Firstly, the BIS participated in a multilateral initiative of the G-10 and other Asian and European countries to provide liquidity to the Bank of Thailand in the form of short-term bridging finance. However, this facility was not activated.

In addition to providing bridge loans, the BIS has recently co-ordinated a credit facility of up to US$13.28 billion in favour of the central bank of Brazil. This loan is part of the US$41.5 billion international financial support programme put together by the IMF in November 1998 to try to save Latin America's largest economy from financial collapse (though Brazil has been forced to float its currency, it can be agreed that its problems would be worse without the financial package, even though we do not yet know the final outcome). The BIS credit facility had the backing of 19 central banks from the G-10 and certain European countries.

This facility, which has a draw down period of one year, is linked to disbursements under a Supplemental Reserve Facility provided to Brazil by the IMF.

The role of the BIS in crisis management may change in the near future. Firstly, the introduction of the IMF's Emergency Financing Facility - and especially the new Contingency Credit Line - may mean that there will be less call for the BIS bridge loans in the future. Secondly, the huge amounts now involved in cross border private financial flows may well imply that the IMF will not always have adequate resources to restore market confidence in troubled economies as we saw recently in East Asia. This may mean that the BIS will be called upon to provide some of the loans which make up an international rescue package.

At present, the BIS sees its main contribution as being in crisis prevention, principally through the setting of internationally accepted standards and facilitating international co-operation, more than in crisis management, even though it has played quite an important role in the latter.

IV MEMBERSHIP AND MANAGEMENT; PARTICIPATION OF DEVELOPING COUNTRIES

As discussed above, the BIS is playing an increasingly important role in relation to developing countries, and it is likely and desirable that it will continue expanding in the future (see sections V and VI below). However, its membership and very particularly its management structure does not reflect sufficiently the rapidly growing role of developing countries in its activities, even though some important steps have been taken to remedy this.

As regards BIS membership, before 1996, it was constituted by the G-10 and Switzerland, as well as other developed countries, the main East European countries and only two developing countries, South Africa and Turkey (see Table 1). In 1996, several large developing countries were invited to joint the BIS; they were Brazil, India, China, Korea, Saudi Arabia, Hong Kong, Mexico and Singapore. Russia also joined that year. The developing countries invited to join were clearly the largest ones – both in GDP and population – as well as those which are very large financial centres and/or have very high incomes. It is clearly a very positive step that the BIS has broadened its membership, to include several key developing countries. Two issues can be raised in this context. Could and should this membership be broadened further? With what criteria? Should all categories of developing countries be represented (like in the G-24), or should more key developing countries be included? Should at some point in the long-term the BIS aim at having – like the IMF – universal membership, but with weighted and rotating representation in the Board? This seems particularly valuable if, as discussed above and below, the BIS is having a very important role in the Financial Stability Forum, as it would facilitate it having a truly global perspective (but, as discussed above, via mechanisms that would maintain the productive intimate style of work that has characterised the BIS and its Committees). Some of the changes suggested may require modifications of the BIS Statutes, particularly of its Article 8(3).

The BIS has three administrative bodies: the General Meeting, the Board of Directors and the Management. At present, the Bank's Board of Directors is drawn exclusively from the G-10 countries. The Board of Directors comprises the Governors of the central banks of Belgium, France, Germany, Italy, the UK and the Chairman of the Board of Governors of the US Fed, as ex-officio members, each of whom appoints another member of the same nationality. The Statutes of the BIS also provide for the election to the Board of not more than nine Governors of other member central banks (BIS, 1998). The currently elected members of the Board are currently all from developed countries, as they are Canada, Japan, the Netherlands, Sweden and Switzerland. Presumably there are no restrictions in the BIS Statutes for having one or more representatives from developing countries on the Board, and this clearly seems a desirable step.

TABLE 1
Membership of BIS, March 1998

G-10 Members

Belgium	Canada	France
Germany	Italy	Japan
The Netherlands	Sweden	Switzerland
United Kingdom	United States	

Other Pre-1996 Members

Australia	Austria	Bulgaria
The Czech Republic	Denmark	Estonia
Finland	Greece	Hungary
Iceland	Ireland	Latvia
Lithuania	Norway	Poland
Portugal	Romania	Slovakia
South Africa	Spain	Turkey
Yugoslavia		

Joined in 1996

Brazil	China	Hong Kong
India	Korea	Mexico
Russia	Saudi Arabia	Singapore

Joined in 1997 (a)

Bosnia and Herzegovina	Croatia	Republic of Macedonia
Slovenia		

(a) The countries that joined in 1997 were the successor states to Yugoslavia, as that country split.

A very important recent positive step that the BIS has taken to enhance its developing country work is to open a representative office for Asia and the Pacific in Hong Kong, to facilitate its activities in the region. Reportedly, the BIS is evaluating the possibility of establishing a branch in Latin America.

The staff of the BIS (including temporary staff) is fairly small (around 500 people), and of an extremely high professional standard, as reflected in the very high quality of the BIS's publications, and in particular of the BIS Annual Report (which has, for example, drawn attention systematically to risks in the international financial system, especially those relating to developing countries, often before other international institutions have done so). Though the staff is very international (drawn from twenty-nine countries), developing countries are very little represented, even though their representation is growing somewhat. Indeed, senior BIS staff expressed a positive interest in attracting more staff from developing countries. This seems highly appropriate, and special actions may need to be taken for this purpose. At a later stage, it seems important that also some management positions are allocated to colleagues from developing countries. There may also be a case to broaden the staff, from other perspectives (to include academics, private sector practitioners, etc.). Again new mechanisms, like secondments or visiting staff may be useful; this could build on the BIS Visiting Fellowship scheme for short-term secondees from emerging market central banks.

In Section III, we have described the incorporation of developing countries into some of the work of the BIS related Committees. As regards the monthly Governors' meetings discussed above, these are two-day meetings. Typically, only one session in the whole two days tends to have participation from all LDC Governors; thus, the majority of those key meetings seem to be exclusive to G-10 Governors. Greater developing country participation here seems very desirable. However, there are a number of other international meetings at the BIS in which senior LDCs increasingly participate. There is also a growing range of specific activities for LDCs, organised by the BIS, such as the two regional conferences (one for Asia and one for Latin America). Though these are clearly very valuable, it seems even more essential to integrate more fully LDCs into the mainstream work of the BIS and its Committees. An important question is whether developing countries wish to organise, probably best on a regional basis, BIS like arrangements/meetings, beyond what already exists. Such arrangements/sets of meetings amongst regional regulators could be strongly linked to – but be broadly autonomous from – the BIS and its committees. An advantage of such complementary arrangements would be that they could draw more and better on common regional issues in – and features of – financial systems, within regions.

V THE FUTURE: BROADENING THE BIS, AS A BASIS FOR ENHANCING ITS ROLE IN THE NEW FINANCIAL ARCHITECTURE

A Increased role in global regulation

The BIS and its Committees are clearly the main focus of international co-ordination of regulation in banking; as the Secretariat of the International Association of Insurance (IAIS) is now based at the BIS, there are very close links with the international regulation of insurance. There are also growing links between the BIS and its Committees with the securities' regulator, IOSCO, for example via the Joint Forum, on regulating the increasingly important financial conglomerates.

As a result, the BIS, its Committees and its links with other regulatory bodies, would seem to make it a natural base for the construction of a future body of global regulation. A very important intermediate step for the creation of such a body was the above mentioned UK proposal made by Clare Short and Gordon Brown, for a new and permanent Standing Committee for Global Financial Regulation that would be charged with developing and implementing a mechanism to ensure that the necessary international standards for financial regulation and supervision are put in place and properly co-ordinated. The broader aim would be to deliver the global objective of a stable financial system. Indeed, the UK proposal suggested that this Standing Committee brings together not just the Basle Committees and other regulatory groupings, but also the World Bank and the IMF on a regular —perhaps monthly – basis. The President of the Bundesbank, Hans Tietmeyer, was in charge of preparing detailed recommendations on the operation of this institution. This report led to the creation of the Financial Stability Forum, which as discussed above is an extremely valuable step, as is the establishment of the three Working Parties.

In the medium-term future, such a Standing Committee could evolve into a far more ambitious institutional development, a global super-regulator, along lines suggested by Kaufmann (1992) and Eatwell and Taylor (1998). Such a global super-regulatory body would have the authority and expertise to generate a level regulatory playing field between countries and sectors as well as fill the many existing regulatory gaps, both within specific financial sectors (e.g. mutual funds, hedge funds) and within certain jurisdictions, as for instance off-shore centres. More broadly, such a body would set mutually acceptable minimum risk-weighted capital or reserve requirements for different financial sectors, establish uniform trading, reporting and disclosure standards and monitor the performance of markets and financial institutions. Such a global super-regulator would thus integrate and make compatible regulation between different financial sectors (to take account of growing de facto integration between markets of banking, securities and insurance) and deepen global regulation (to take account of the global nature of these markets). Though very desirable as it would correspond to the new needs of the global economy, such an institution may be complex to establish, and very difficult to agree internationally, especially if it would require an international treaty to be approved by national Parliaments. This may be more feasible for the 22nd Century!

Therefore, it seems better to focus in the short-term on the recently created Financial Stability Forum. As Gordon Brown (1998: 5) has pointed out, this will "not be an additional institution but a process of monitoring development in global finance, ensuring that necessary world-wide standards are put in place, and providing timely surveillance of financial conditions and international capital flows".

It seems appropriate that a leading role for the Forum rests on the BIS and its Committees, on the IAIS and on IOSCO, given the great accumulated technical expertise in each of their fields of regulation. As the ultimate aim is the pursuit of global financial stability, the perspective of the BIS (drawing on its Central Bank constituents), of examining financial markets from the angle of avoiding possible systemic risk, seems particularly appropriate for this task. It would be complementary with a perspective focussing more on country (especially macro-economic) problems, as possible causes of crises, which is the perspective that the IMF adopts in its work and is likely to continue pursuing. Thus, a fairly clear division of labour seems to emerge, whereby the BIS – jointly with IOSCO and the IAIS coordinated with the IMF and the World Bank – takes the lead on global financial regulation, with the IMF and the World Bank playing a primary role mainly in helping dissemination and surveillance of the standards and norms formulated by the forum of global regulators. The central role of the IMF will, however, continue to focus on monitoring of macro-economic policies.

B New possible roles in crisis management

The BIS has also played a role of provision of official liquidity to developing countries either as part of a mechanism for crisis prevention like recently in the case of Brazil, or more frequently, as part of a crisis management package. The financing provided by the BIS is only in a small proportion based on its own resources, but is mainly based on pooling of financing from G-10 central banks. Till recently, the BIS organised financial facilities for developing countries had always been bridge loans (to IMF loans) whereas in the case of Brazil the BIS organised a self-standing loan, though reportedly this was exceptional.

Clearly the lead role in providing official financing to countries in crises has till now been taken by the IMF.

The future of the BIS in crisis management needs to be based on a clear diagnosis of the nature of developing countries capital-account-led currency crises today which are different from the mainly current-account-led crises of the past. These recent crises are partly caused by mistakes or problems in the countries themselves; however, a very significant cause of these crises – particularly in situations of contagion – are due to important occasional imperfections in international capital markets, which can lead to rapid and large withdrawals of capital from countries whose underlying fundamentals are basically sound.

As markets can be not only very imperfect, but also move so fast, it is essential that mechanisms for emergency official financing operate very speedily when a crisis explodes, to stop the crisis deepening in the country and spreading – via contagion – to other countries.

A solution that may be appropriate is therefore to stress preventive programmes. One desirable strategy could be that during Article IV consultations with the Fund, some countries could be approved by the IMF as having good policies and not being likely – if the good policies were to be continued – to be crisis prone. Should, however, such a country still be hit by a crisis – due, for example, to contagion – it would be appropriate for the country to receive emergency official financing fast, but not appropriate for it to have additional policy conditionality imposed on it. One mechanism recently made available for this purpose is the IMF Contingency Credit Line (CCL). However, the CCL is not automatically disbursed, even if the crisis is caused by contagion, as it requires a new approval by the IMF Board. An alternative or complementary mechanism could be for the BIS to play a key co-ordinating role for rapidly assembling financial packages with resources mainly provided by G-10 Central Banks, combined where feasible with private credit lines; to a small extent, the BIS could also draw on its own resources. Though the BIS would take the lead in arranging the initial financing, the IMF would have taken the lead in previously defining that the country's policies did not make it crisis prone.

Such distinctions would provide strong incentives for countries to have good policies; this should make crises less likely. If, nevertheless crises did occur, large lending without conditionality by G-10 Central Banks and commercial banks could possibly be quickly co-ordinated by the BIS for countries that had been deemed to have good policies by the IMF; for countries having an IMF CCL, a crisis would be followed by an IMF loan disbursed also speedily, although it would still need to be ratified by the IMF Board (under the current terms of the CCL), which could imply some crucial delay.

The role of IMF conditionality would be far greater in the preventing crises phase, but smaller in the managing crises phase, which would make it more effective and less controversial. Financing could be arranged speedily, which would also be extremely positive. A third advantage would be that policy conditionality would not be applied during crises situations if not caused by bad policies.

C Widening the presence of LDCs in the BIS

We have outlined above why it seems desirable – both from a global and a developing country perspective – to extend the role of the BIS particularly in crisis prevention, via its key role in global prudential regulation, but also in crisis management. As regards an enhanced role of the BIS and its Committees in global prudential regulation, the case rests mainly on its obvious leading expertise in this area. As regards the BIS' enhanced role in crisis management, this may be desirable for LDCs for two reasons: a) it may provide genuinely unconditional and rapid financing to countries following good policies, but suffering crises due to contagion or other external factors; b) unconditional lending by the BIS may be particularly appropriate because the BIS is perhaps more technical and less "political" than the IMF, because it has a greater tradition of sensitivity to – and analysis of – imperfections in international financial markets, and has not focussed on imposing conditionality on developing countries. As a consequence, the above suggested division of labour may play to the strengths of both the IMF and the BIS, and would therefore be more beneficial both globally and – especially – for developing countries in crises.

To provide an even more solid base for the BIS to play these bigger roles in a future financial architecture, it seems very important to increase representation of developing countries in the BIS and its Committees. The increased role of the developing countries in the BIS would not only be appropriate for representation and legitimacy reasons, but also because it would provide expertise and perspectives that are essential, given the increasing global integration of financial markets and the larger role LDCs play in them; in particular, it will provide the BIS with useful insights on areas of the world, where its work is likely to be expanding significantly.

Two caveats seem important in relation to the increased role of developing countries in the BIS. Firstly, as stressed by BIS officials, probably this needs to be done in ways that do not undermine the effectiveness and intimacy of the "Basle style", that reportedly so much facilitates agreement and decisions-making on the basis of consensus, though maybe the importance of small size for efficiency is a bit overplayed. Possibly instead of thinking of expanding too much – or expanding at all – membership of the BIS's Board or Committees, it may be more desirable for developing country participation to be included, at least initially, on a rotating basis. This should be more acceptable to the large G-10 countries, whose representation would not be likely to be affected, but may be less acceptable to some of the smaller G-10 countries, as they may have to yield some representation. However, this process may be somewhat facilitated by the creation of the European Central Bank, (which in some BIS fora could represent eleven countries). Secondly, there may be some aspects or issues such as of regulating very sophisticated instruments used mainly in developed economies, or of issues such as reducing risks in settlements systems – where developed countries do have greater concerns and/or expertise. In these – relatively rare – cases, it may continue to be appropriate for G-10 countries to play the dominant or even an exclusive role, though it always seems valuable for developing countries to participate, as this gives access to information on future trends and issues.

It seems important and urgent to: a) ensure participation of developing countries in the Board of the BIS; b) ensure greater – and more formalised – participation of developing countries in crucial meetings, for example in monthly meetings of Central Bank Governors; c) increase their participation in the three key BIS Committees, on some formal and not just on an ad-hoc basis; d) increase the number of developing country staff in the BIS; (have some LDC participation in BIS management; some experts on developing countries, e.g. from academia or the private sector in developed countries, may also add useful insights), and e) possibly expand the number and types of developing countries included in the BIS and its Committees, thus including representation from low-income small countries.

It would seem important to achieve progress on several of these fronts simultaneously; this is not a particularly radical proposal, but basically implies a fairly significant acceleration of existing trends. In this sense, the growing importance of regional LDC meetings, the bi-annual meetings with Deputy Governors of emerging markets, need to be continued and deepened.

D Providing additional information on markets to developing countries

As described above, one of the valuable functions that the BIS carries out is the provision of very useful and high quality information on trends in financial and banking markets.

However, particularly during the crisis that started in Asia, emerging country policy-makers (and specifically emerging country Central Banks) have found important limitations in the essential information available on the functioning of international capital and banking markets[4]. The type of information required is both on more long-term structural changes in these markets, but particularly on almost day to day changes in the functioning of markets – and their key actors – globally and regionally.

In the same way that the IMF has led the way in improving information – and its dissemination – on emerging market economies, particularly useful to markets, a parallel symmetric effort needs to be done to gather and provide timely information on market evolution to emerging market policy-makers; this task should obviously be led by the BIS, though inputs from other institutions, as the IMF, the private sector, would be very valuable. Though possibly not giving it sufficient emphasis, suggestions in the October 1998 G-22 Report of the Working Group on Transparency and Accountability provide important elements for this task. These suggestions (some of which were mentioned above) relate not just to better statistics on international banks' exposures, but also on "compiling data on international exposures of investment banks, hedge funds and other institutional investors"; the latter would include presumably pension funds and mutual funds. It seems essential that developing countries – and possibly a representative of the G-24 – should participate in the Working Group recommended in the G-22, and other similar relevant groups.

Given the speed with which markets move, it seems particularly important that the frequency with which relevant data is produced is very high (and possibly higher in times of market turbulence, when it becomes particularly crucial), and that dissemination is instant to all countries' Central Banks. Indeed, a special additional service could be provided by the BIS, in which it would play the role of a clearing house of information. For this purpose, it could draw not just on information it can gather directly from markets, but by collecting and centralising information on their markets that individual Central Banks have, and where the aggregate picture is not easily available to any individual Central Bank. This could possibly include both quantitative and qualitative information. Via the internet, the BIS could standardise the information requirements, collect the information, aggregate it, and disseminate it rapidly to all central banks, as well as to other relevant institutions. Such a service would be of the greatest usefulness to developing country policy-makers, especially immediately before and during crises; naturally, it would also be very valuable to developed country policy-makers and international institutions (including the BIS itself) in handling crisis prevention and management.

[4] Interview material; own experience

VI RECOMMENDATIONS, INCLUDING FOR POSSIBLE G-24 MINISTERIAL ACTION

The BIS is already playing an increasingly important and positive role in international financial governance. In the light of recent currency crises, and of the resulting discussion of a new international financial architecture, that will try to prevent them and manage them better if they do occur, it seems desirable that the role of the BIS be both increased and modified.

Four key areas have been detected in this study, where changes are both desirable and urgent

a) The BIS as a base for global regulation. The BIS and its Committees seem a natural base for the construction of a future body of global prudential regulation, to promote financial stability globally and in individual countries, especially but not only developing ones. A crucial step in this direction is the creation of the Financial Stability Forum, in which the BIS and its Committees are working jointly with other key regulatory groupings, such as IOSCO and the IAIS, as well as the IMF and the World Bank. It seems appropriate that the small Secretariat of this new Forum is based at the BIS, given the accumulated expertise there, and that many central bankers and regulators already meet in this context.

   It would seem desirable that this Financial Stability Forum not only pools information, but also is given or develops - in the Basle style – authority for co-ordinated decision-making. Two crucial areas for action seem to be: i) the co-ordination, where possible and appropriate, of consistent prudential regulatory norms (on risk-weighted capital adequacy, liquidity, etc) and ii) evaluate and – where appropriate – try to fill crucial regulatory gaps, both within specific financial sectors and certain jurisdictions (see also, Eatwell and Taylor, op. cit. and Kaufmann, op. cit. for proposals on global regulation).

   The creation of the Financial Stability Forum seems clearly in the interest of developing countries, as it will hopefully make currency crises, that are particularly damaging to developing countries, less likely. However, it is very important that developing countries' concerns and interests are appropriately and directly represented in the Forum. It also seems important that developing countries adopt a position on issues that should perhaps best be excluded from such a Forum, as well as from the IMF. A good example of issues to attempt to exclude would be authority on capital account liberalisation in developing countries, as such a policy seems clearly best decided by the individual developing country itself (see Griffith-Jones and Ocampo, 1999, for a discussion of these issues).

For the development of the Financial Stability Forum, it may be valuable to draw on the recent British experience of establishing the Financial Services Authority, which co-ordinates and – as far as possible – integrates regulation across financial sectors in the UK; a study on the subject may be useful.

b) Enhancing the role of the BIS in official lending. Particularly for those developing countries with good policies (and with the IMF having approved them as such during Article IV consultations), the BIS could play an important role in assembling official financing if they were still hit by a capital-account-led crisis, purely by external factors such as contagion. This facility would be alternative to the recently created IMF Contingency Credit Line, which though designed for countries with crises caused not by bad policies but by contagion is still not fully automatic. A BIS arranged facility could be fully automatic (for countries approved previously by the IMF as having good policies) and would not have limits of scale, other than those designed for each case by the lending Central Banks.

In other cases, where the IMF considers that significant additional policy conditionality is required, clearly the IMF would take the lead role, as it would both negotiate the conditionality, and lead the financing, including from its own resources. Continuing current practice, the BIS could – where required – support the Fund's financing efforts.

c) Increasing participation of LDCs in the BIS, its activities and Committees. Greater participation of developing countries in the BIS is important not just to strengthen further the legitimacy of the BIS for its key tasks, both present and future, but would also provide it valuable insights in areas where its work will be significantly expanding. It seems clearly also in the interests of developing countries to participate more in the BIS and its Committees, as it would give them access to discussions and expertise on increasingly important issues, without burdening them with additional political demands.

In recent years, the BIS has initiated an important process of expanding participation of LDCs, particularly but not only in its membership. This process clearly needs to be accelerated. It would seem important to ensure LDC participation in the BIS Board, in other crucial BIS meetings, formalise their growing participation in BIS committees, increase BIS staff from LDCs, (hopefully later including some at more senior level) The possibility of increasing LDC membership of the BIS could also be evaluated. As discussed above, also there should be LDC participation in the recently created Financial Stability Forum, which though far broader than the BIS is based in Basle and has as its first Chairman, Andrew Crockett, who is the General Manager of the BIS.

In some of these areas, relating for instance to more developing country representation among BIS staff and others, it seems very likely that senior BIS management and the Board would agree with such proposals. The problem may just be one of effective implementation. For this purpose, it may be desirable to establish a small liaison group, between the BIS and the G-24 for example, to help make suggestions for creating mechanisms and incentives to assure greater developing country presence within the BIS staff.

d) Expanding the role of the BIS in providing information on international markets. Crucial information on capital and banking markets available to policy-makers, especially in LDCs, is clearly insufficient, especially just before and during currency crises.

The BIS seems ideally placed to build on the useful information it already provides, and on its network of links with central banks and markets by expanding it in two directions: i) broadening coverage, for example to include more information on institutional investors and in rapidly growing instruments, such as derivatives and ii) increasing significantly frequency of information, to provide timely inputs to policy-makers on rapid changes in financial market trends.

This exercise would be in some ways symmetrical to the efforts being led by the IMF to improve information available on developing countries, mainly of use to markets; the proposed activity would improve information on markets, mainly for the use of country and international policy-makers.

If approved, a meeting or a set of meetings, including representatives from LDCs, working with BIS staff or the respective Committees, seems appropriate for effective implementation. The G-24 (or representatives of LDCs Central Banks) and/or UNCTAD could for example identify desirable additional information on international financial markets, especially from a developing country perspective, that the BIS could provide, its frequency, etc. The feasibility, frequency and value of such additional information could then be explored.

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APPENDIX 1

International Association of Insurance Supervisors (IAIS)

In 1994 insurance supervisors from around the world established their own association, the IAIS. Its membership now constitutes insurance supervisors from over 80 countries who resolved:

- to co-operate together to ensure improved supervision of the insurance industry on the domestic as well as on an international level in order to maintain efficient, fair, sage and stable insurance markets for the benefit and protection of policyholders;
- to unite their efforts to develop practical standards for supervision of insurance that members may choose to apply;
- to liaise or co-operate with other relevant international entities;
- to provide mutual assistance to safeguard the integrity of markets;
- and to exchange information on their respective experiences in order to promote the development of domestic insurance markets.

The IAIS issues global insurance principles, standards and guidance, provides training and support on issues related to insurance supervision and organises meetings and seminars for insurance supervisors. Annually, it holds a conference where insurance supervisors, insurance industry representatives and other insurance professionals discuss topical issues affecting insurance regulation. The 1997 conference was held in Sydney, Australia, the next conference will take place in September 1998 in Cancun, Mexico.

The IAIS is headed by an Executive Committee that has members representing different geographical regions. It is supported by three main committees, the Technical Committee, the Emerging Markets Issues Committee and the Budget Committee. Eleven subcommittees and working groups – Accounting, Education, Electronic Commerce/Internet, Exchange f Information, Financial Conglomerates, Insurance Fraud, Insurance Laws Regulations Practices and Standards, Investment, Reinsurance, Solvency and Year 2000 Issue – report to the main committees.

The IAIS is supported by a Secretariat at the Bank for International Settlements, Basle Switzerland.

John R Thompson
Chairman, Executive Committee
Canada

Knut Hohlfeld
Secretary General
Switzerland

APPENDIX 2

Communiqué of G-7 Finance Ministers and Central Bank Governors

February 20, 1999

Petersberg, Bonn

Financial Stability Forum

15. We are grateful to Hans Tietmeyer for his report on international cooperation and coordination in the area of financial market supervision and surveillance. We welcome his proposal that the G-7 should take the initiative in convening a Financial Stability Forum to ensure that national and international authorities and relevant international supervisory bodies and expert groupings can more effectively foster and coordinate their respective responsibilities to promote international financial stability, improve the functioning of the markets and reduce systemic risk.

While the Forum will initially be the initiative of the G-7 countries, we envisage that over time additional national authorities would be included in the process. The issues to be addressed affect all countries, including both industrial and emerging market economies, and the G-7 regards this initiative as a step toward broader participation.

- We agreed that the Forum will meet regularly to assess issues and vulnerabilities affecting the global financial system and identify and oversee the actions needed to address them, including encouraging, where necessary, the development or strengthening of international best practices and standards and defining priorities for addressing and implementing them.

- We agreed that the Forum will be comprised of representatives of national authorities responsible for financial stability, the relevant international financial institutions and organisations as well as the relevant international supervisory bodies and expert groupings. The Forum will be supported by a small secretariat located in Basle. Its first Chairman will be Mr Andrew Crockett, General Manager of the BIS, for a term of three years. We ask our Deputies to make the necessary preparations so that the first meeting of the Forum could be held in Spring 1999.

APPENDIX 3

BANK FOR INTERNATIONAL SETTLEMENTS

CH-4002 BASLE, SWITZERLAND

Press release

Press enquiries: +41 61 / 280 81 88
Ref. No.: 06/1999E
8th February 1999

Committee on the Global Financial System

Mandate

The Governors of the central banks of the Group of Ten countries today decided to clarify the mandate of the Euro-currency Standing Committee (ECSC) in order to strengthen the effectiveness of the overall Basle-based process in promoting monetary and financial stability. Concomitantly, the Committee has been renamed Committee on the Global Financial System.

The Committee on the Global Financial System will act as a central bank forum for the monitoring and examination of broad issues relating to financial markets and systems with a view to elaborating appropriate policy recommendations to support the central banks in the fulfilment of their responsibilities for monetary and financial stability. The tasks performed by the Committee will fall into three categories: systematic short-term monitoring of global financial system conditions, so as to identify potential sources of stress; in-depth longer-term analysis of the functioning of financial markets; and the articulation of policy recommendations aimed at improving market functioning and promoting stability (see the attached mandate). This mandate recognises that the causes of financial instability can arise from both the behaviour of markets and the complex interrelationships that exist between institutions, markets, infrastructures and macroeconomic policy.

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Notes for the press

After having acted in the 1960s as an informal forum for the regular exchange of views on international monetary and financial issues among senior central bank officials, the ECSC first received a formal mandate from the Governors in 1971. This mandate was stated publicly in 1980, when the Governors announced their intention to monitor international banking markets more closely. The initial focus of the Committee was on the monetary policy implications of the rapid growth of the euromarkets. In the late 1970s, attention shifted to concerns relating to financial stability. After the international debt crisis had subsided, the Committee's work was principally devoted to an examination of financial innovation and of the longer-term changes in the structure of the financial system, with particular reference to their potential impact on systemic risk. Over the years, the Committee has published a number of reports on issues addressed within its remit. In addition, it has been responsible for developing and overseeing the implementation of the various sets of BIS statistics on international banking, derivatives and foreign exchange market activity.

Besides its regular monitoring tasks, the Committee is currently working on a number of initiatives. Following the recommendation of a template for the disclosure of foreign currency reserves and potential drains on them endorsed by the Governors in late 1998, the Committee is now investigating ways of enhancing the transparency of the financial activities of market participants more generally. Two working groups, including representatives of emerging market countries, are addressing this issue. One group is concerned with disclosure practices by individual financial institutions. Building on a previous report issued by the ECSC in 1994, it is focusing on the disclosure of information that would allow users to form a meaningful view of the institutions' risk profile. The second group is examining what kind of aggregated information would help improve the functioning of markets. These efforts are a natural complement to initiatives undertaken by the Basle Committee on Banking Supervision in related areas, including its recent report on banks' interactions with highly leveraged institutions. In addition, a third working group is exploring the possibility of aggregating information drawn from risk management models of individual firms in order to facilitate the assessment of market vulnerabilities. These efforts run parallel to other initiatives aimed at studying the preconditions for well-functioning and liquid markets and which could serve as a basis for future policy recommendations in this area.

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Committee on the Global Financial System

Mandate

The Committee on the Global Financial System is a central bank forum for the monitoring and examination of broad issues relating to financial markets and systems with a view to elaborating appropriate policy recommendations to support the central banks in the fulfilment of their responsibilities for monetary and financial stability. In carrying out this task, the Committee will place particular emphasis on assisting the Governors in recognising, analysing and responding to threats to the stability of financial markets and the global financial system. More specifically, the Committee's primary objectives will be the following:

- To seek to identify and assess potential sources of stress in the global financial environment through a regular and systematic monitoring of developments in financial markets and systems, including through an evaluation of macroeconomic developments;

- To further the understanding of the functioning and underpinnings of financial markets and systems through a close monitoring of their evolution and in-depth analyses, with particular reference to the implications for central bank operations and broader responsibilities for monetary and financial stability;

- To promote the development of well-functioning and stable financial markets and systems through an examination of alternative policy responses and the elaboration of corresponding policy recommendations.

In its analysis, the Committee should pay particular attention to the nexus between monetary and financial stability, to the linkages between institutions, infrastructures and markets, to the actual and potential changes in financial intermediation and to the incentive structures built into markets and systems. The Committee should seek to increase the transparency of financial markets and systems by promoting the design, production and publication of statistics and other information by central banks - including through the BIS - and by recommending the adoption of appropriate disclosure standards by both the official and private sectors. Where relevant, the Committee should also contribute to the development of an international consensus on sound principles and norms.

The Committee is encouraged to co-operate with other national, supranational and international institutions with responsibilities for pursuing related objectives. In particular, it shall co-ordinate its activities with other Basle-based committees, such as the Basle Committee on Banking Supervision and the Committee on Payment and Settlement Systems, in order to strengthen the overall effectiveness of the process.