Financial Stability Forum meets in Rome

The Financial Stability Forum (FSF) met in Rome on 28-29 March. Members discussed the current challenges in financial markets, the steps that are being taken to address them and policy options going forward.

Financial system risks and responses

The financial system faces a number of significant near-term challenges. With many securitisation markets effectively closed, assets are accumulating on bank balance sheets. Together with valuation losses on mortgages and other assets, this is straining capital positions and contributing to tightening credit conditions. Hoarding of liquidity and counterparty concerns are leading to a shortening of the maturity of banks’ funding profiles and causing severe strains in interbank and other lending markets.

While the necessary deleveraging has been ongoing since last summer, the process is being complicated by the lack of transparency and valuation difficulties for some credit instruments. Financial institutions should continue enhancing their disclosures of risk exposures and refining valuation judgements concerning structured credit activities and poorly performing assets on and off the balance sheet. Banks, securities firms and financial guarantors have made progress in replenishing capital levels and should continue to do so where necessary. The raising of capital and the repairing of credit markets will facilitate balance-sheet management by financial institutions and help to counteract the potential cycle of financial market and economic weakness.

National authorities have taken a variety of exceptional steps to facilitate adjustment and to dampen the impact on the real economy. Authorities in the main financial centres are in continuous contact and closely monitoring developments. Supervisors are working with firms so that risks in current market circumstances are effectively identified and appropriately managed. Central banks have provided liquidity to address market pressures, both individually and in concert, and will continue to do so as long as needed. Authorities will also act cooperatively and swiftly to investigate and penalise market abuse or manipulation.

Strengthening market and institutional resilience

The FSF discussed the report to be delivered to G7 Finance Ministers and Central Bank Governors in April that identifies the key weaknesses underlying the turmoil and recommends actions to enhance market and institutional resilience going forward. The report has been prepared by a working group comprising senior officials from major financial centres and from the international financial institutions and the chairs of international supervisory and regulatory bodies. It sets out specific policy recommendations in the following areas: prudential oversight of capital, liquidity and risk management; transparency, disclosure and valuation practices; the role and uses of credit ratings; the authorities’ responsiveness to risks and their arrangements
to deal with stress in the financial system. These recommendations are concrete and operational and, if approved, the FSF will report on their prompt implementation.

**Hedge fund industry**

In its 2007 report on highly leveraged institutions the FSF called on the hedge fund industry to review and enhance sound practice benchmarks. In response, best practice standards have been developed by the UK-based Hedge Fund Working Group, and are to be released shortly by a similar US-based group. Both groups have established boards which will keep the standards up to date and monitor the take-up of the standards by hedge funds. The FSF would welcome regular reports on the adoption of the standards by the hedge fund industry and how well these standards are meeting the objectives of increasing transparency and improving risk management practices.

**Sovereign wealth funds**

The FSF discussed work underway at the IMF and OECD with regard to sovereign wealth funds (SWFs). The IMF in close partnership with the SWFs is coordinating work to identify a set of voluntary best practice guidelines, focusing on the governance, institutional arrangements and transparency of SWFs. The OECD is developing guidance for recipient countries’ policies toward investments from SWFs. Members welcomed these efforts and the participation of the SWFs in the development of these guidelines.
Institutions and Groups Attending the Meeting of the FSF
28-29 March 2008
Chairman, Mr Mario Draghi

National Authorities

Australia
Reserve Bank of Australia

Canada
Department of Finance
Bank of Canada
Office of the Superintendent of Financial Institutions

France
Ministry of the Economy, Finance and Industry
Banque de France
Autorité des Marchés Financiers

Germany
Federal Ministry of Finance
Deutsche Bundesbank
BaFin

Hong Kong
Hong Kong Monetary Authority

Italy
Ministry of the Economy and Finance
Banca d'Italia
CONSOB

International Financial Institutions

International Monetary Fund
World Bank
Bank for International Settlements
Organisation for Economic Co-operation and Development

International Regulatory and Supervisory Groupings

Basel Committee on Banking Supervision
International Accounting Standards Board
International Association of Insurance Supervisors
International Organization of Securities Commissions
The Joint Forum

Japan
Ministry of Finance
Bank of Japan
Financial Services Agency

Netherlands
De Nederlandsche Bank

Singapore
Monetary Authority of Singapore

Switzerland
Swiss National Bank

United Kingdom
H M Treasury
Bank of England
Financial Services Authority

United States
Department of the Treasury
Board of Governors of the Federal Reserve System
Securities and Exchange Commission

Committees of Central Bank Experts

Committee on Payment and Settlement Systems
Committee on the Global Financial System

European Central Bank