

Press release

Press enquiries:
+41 61 280 8037

press@bis.org

Ref no: 50/2011
20 October 2011

Report on Financial Stability Issues in Emerging Market and Developing Economies

The Financial Stability Board (FSB), International Monetary Fund (IMF) and the World Bank published today a report on financial stability issues of particular interest to emerging market and developing economies (EMDEs).

The report, which was prepared in response to a request by G20 Leaders at the November 2010 Seoul Summit, focuses on five key financial stability issues in EMDEs. It makes a number of recommendations on policy measures by national authorities in EMDEs to address these issues and on ways that the international community can support them in their efforts.

Application of international financial standards. The report recommends that EMDEs further strengthen supervisory independence, resources and capacity with guidance from international standard-setting bodies as well as targeted and well-coordinated technical assistance and other capacity building activities from donors and other relevant bodies. The report also recommends that the international community send a clear and consistent message on the appropriate pace of adoption of Basel II/III in EMDEs, and that the Basel Committee should provide guidance on the application of new measures included in Basel III to EMDEs that do not intend to adopt the advanced approaches of Basel II.

Promoting cross-border supervisory cooperation. In countries where foreign banks play a significant role, the inherent conflicts of interest between the home and host jurisdictions can prevent adequate supervisory cooperation and information sharing and complicate risk assessments and cross-border resolution. The report recommends that home supervisors for large international banks should provide host supervisors, particularly when those banks are systemically important in the host jurisdiction, with timely, accurate and comprehensive information on the parent bank. It also calls for international standard-setters to work with EMDEs to promote adoption of multilateral arrangements to facilitate cooperation and information exchange in the securities and insurance sectors.

Expanding the regulatory and supervisory perimeter. In many EMDEs, small-scale non-bank lending and deposit-taking institutions play an increasingly important role. As it has expanded, this sector has become increasingly complex and interconnected with the rest of the financial system. The rapid pace of growth, sometimes combined with deteriorating asset quality, may potentially have adverse consequences to financial stability in some EMDEs. The report recommends adjusting prudential frameworks in EMDEs to reflect the growth in, and the risks arising from, these institutions.

Managing foreign exchange risks. The volatility in nominal exchange rate movements, compounded by sizeable capital flows, can create important foreign exchange risks. These risks are especially prominent in EMDEs with thin domestic financial markets, significant financial dollarization, or limited markets to hedge currency mismatches. Banks may be exposed to such risks either directly via net open positions that cannot be efficiently hedged, or indirectly as a result of lending to borrowers whose asset-liability profiles and revenue sources expose them to exchange rate fluctuations. The report recommends that EMDEs strengthen the management of direct and indirect foreign exchange risks, that the Basel Committee should provide additional guidance in this area.

Developing domestic capital markets. Capital markets in EMDEs tend to be more shallow and susceptible to sudden price movements and greater disruption that may undermine confidence in their integrity. The development of a domestic investor base, measures at both national and regional levels to deepen capital market liquidity, and improvements in market infrastructure – including for clearing and settlement systems – are important building blocks to address some of the related financial stability issues.

The report points out the need to continue to bring issues of relevance for EMDEs to the attention of the international community. It notes that the IMF, the World Bank and the FSB, particularly via its regional consultative groups, have an important role to play in that regard. In addition, international bodies should take into account EMDE-specific considerations and concerns in designing new international financial standards and policies.

Sangche Lee, Chair of the EMDEs Task Force, said “This report is an important first step towards ensuring greater prominence of EMDE-specific financial sector issues in the G20.” Jose Viñals, Financial Counsellor and Director of the Monetary and Capital Markets Department at the IMF, noted that “The report enriches the G20 agenda by highlighting issues that are critical for a broad range of countries that play an increasingly important role in the global economy.” Janamitra Devan, Vice President of the Financial and Private Sector Development Vice Presidency at the World Bank, added that “The Bank will continue to help client countries to implement measures along the lines of the report’s recommendations.”

Notes to editors

The FSB has been established to coordinate at the international level the work of national financial authorities and international standard setting bodies and to develop and promote the implementation of effective regulatory, supervisory and other financial sector policies in the interest of financial stability. It brings together national authorities responsible for financial stability in 24 countries and jurisdictions, international financial institutions, sector-specific international groupings of regulators and supervisors, and committees of central bank experts.

The report on financial stability issues in EMDEs was prepared by an FSB Task Force comprising FSB members, staff from the IMF and the World Bank, and senior policymakers from some emerging market and developing economies outside the FSB. Dr. Sangche Lee, Commissioner of the Korean Financial Services Commission, chaired the Task Force.

The FSB is chaired by Mario Draghi, Governor of the Bank of Italy. Its Secretariat is located in Basel, Switzerland, and hosted by the Bank for International Settlements.

For further information on the FSB, visit the FSB website, www.financialstabilityboard.org.