

Statement by Mario Draghi
Chairman of the Financial Stability Forum
International Monetary and Financial
Committee Meeting

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The Financial Stability Forum (FSF) held its eighteenth meeting on 25-26 September 2007 in New York. The issues discussed included: risks and vulnerabilities in the international financial system following the recent market turmoil, including experiences with crisis management and valuation issues; follow-up work on Highly Leveraged Institutions (HLIs); effective and efficient regulation, and offshore financial centres (OFCs).

Assessing and addressing risks in the financial system

FSF members reviewed the recent strains in global financial markets. In recent weeks, authorities have taken a number of actions to provide assurance of the availability of adequate liquidity in money markets. Members noted signs of stabilisation in money and to some extent in credit markets, although liquidity remains low in several market segments. The period of adjustment to this re-pricing of risk may take some time, depending among other things on the restoration of confidence in valuations of credit instruments and in assessments of counterparty creditworthiness. The FSF encouraged the adoption of common guidelines for valuation, particularly for complex illiquid products. It also welcomed the progress being made with regard to the implementation of Basel II.

Members agreed that global macroeconomic conditions generally remain strong, underlying credit problems have been limited to a small proportion of credit instruments, and the capital of regulated institutions has remained at sound levels.

Establishment of FSF working group on market and institutional resilience

The events in financial markets of recent months, and their underlying causes, have raised issues that require careful consideration by market participants and financial policymakers. Many of the weaknesses in the underpinnings of the structured finance markets and in risk management practices will be addressed through adjustments in the private sector. The authorities will need to monitor and reinforce these changes and take action where additional discipline is required to make markets more resilient. To help formulate an appropriate and coordinated international response, the FSF has formed a working group of national authorities, the chairs of the relevant international supervisory, regulatory and central banking bodies and other international organisations. The working

group will investigate the causes of these events, identify the weakness that merit attention and recommend actions needed to enhance market discipline and institutional resilience. The work of the international supervisory and regulatory bodies will play an important role in this regard. The group will facilitate co-ordination across work streams, ensure that any gaps in the work of international bodies are addressed, and serve as a vehicle for co-ordinated reporting of authorities' responses. Amongst areas that the group will address are liquidity and credit risk management practices at regulated financial institutions; valuation, risk disclosure and accounting practices related to structured credit instruments; the role of credit rating agencies in the structured finance market; and principles and practices of prudential oversight. The group will also review issues that have arisen in the authorities' responses to the events. The FSF will submit a final report and recommendations to G7 Finance Ministers and Governors for their April 2008 meeting.

Hedge funds and counterparty risk management

In May this year, the FSF issued an update of its report on Highly Leveraged Institutions. While the hedge fund sector has not been the primary source of the recent market turmoil, the severity of market problems has highlighted the importance of ensuring sound counterparty risk management at regulated institutions and fostering the exchange of relevant information between hedge funds and their counterparties. The HLI Update examined important issues in these areas and made a series of recommendations. At the New York meeting, the FSF took stock of progress in work to address these recommendations. An international supervisory review group is working to enhance the risk management practices of core intermediaries. The FSF also welcomed private-sector initiatives launched in the UK and US to enhance sound practices guidance for hedge fund managers and investors in hedge funds. The FSF reported on the progress made on the recommendations to G7 Finance Ministers and Governors in October.

Effective and efficient regulation

As part of the FSF's work to promote effective and efficient regulation, national regulatory members have completed a stocktaking exercise on the principles and procedures they follow in the development and interpretation of new regulations and other policy initiatives. The information on national members' procedures will be posted on the FSF's website.

Offshore financial centres

The FSF recently reviewed its OFCs initiative, based on a report of its OFC Review Group. The Forum acknowledged the significant progress made by OFCs, although some concerns remain. The FSF restated its commitment to foster compliance with international standards, including better cooperation and information exchange. Political support from the FSF for the work of its members on OFCs is undiminished. The range of potential follow-up actions identified in 2005 remains available to be used.