BANK FOR INTERNATIONAL SETTLEMENTS

Elements of Effective Macroprudential Policies

Lessons from International Experience

A summary of the IMF-FSB-BIS report

https://www.bis.org/publ/othp26.htm

Financial Cycles and Policy response in Latin America

IDB-BIS-BCRA Workshop

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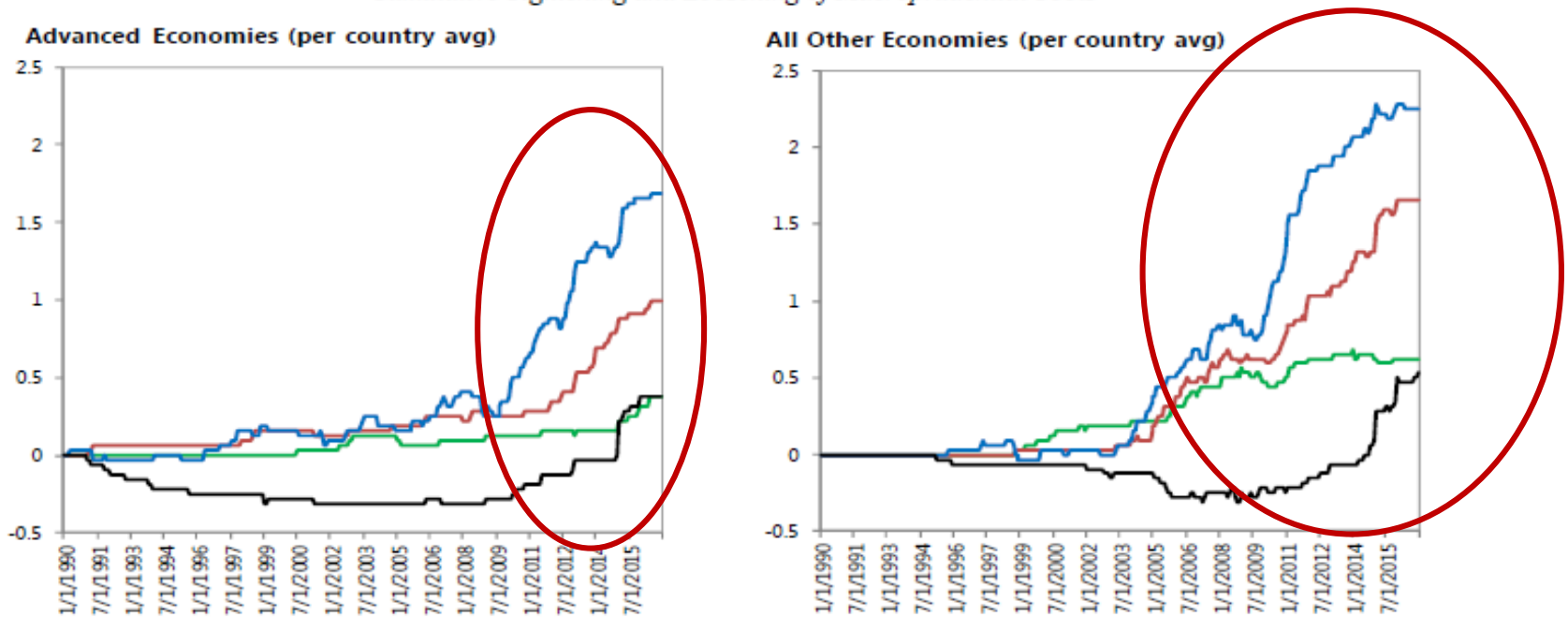
Enrique Alberola, BIS Chief Representative for the Americas

Intro

- IMF-FSB-BIS at the core of macroprudential policies monitoring and assessment (*G-20 mandate, 2010*).
- Macropru policies preexist current hype (eg Latin America).
- Growing international experience enables **stocktaking.**

Cumulative Tightening and Loosening of Macroprudential Tools



Note: Each tightening (loosening) episode is coded as a +1 (-1) in the database. For each group of instruments, the charts show a cumulative sum of tightening and loosening episodes over time.

Outline

- Definition, objectives and scope of macroprudential policy
- Institutional arrangements
- Operational considerations and effectiveness
- International dimension

Definition, objectives, scope

- Use of primarily prudential tools to limit systemic risk
  1. increase the resilience of the financial system ←buffers
  2. contain build-up of vulnerabilities ←cyclicality, sustainability
  3. control structural vulnerabilities arising through common exposures, interconnectedness, systemic players ←cross-sectional, structural
- Considerations
  - Interactions with other policies
  - Risks of overburdening macropru
  - Potential overlap: macropru & capital flow management measures
  - Leakages (scope of macropru) & international spillovers

Institutional arrangements

- No "one-size-fits-all", determined by domestic environment:
  - Desirable: Clear mandate & objectives, power & ability to act, cooperation, accountability
  - Powers vary: hard (*toolbox*), semihard (*comply or explain)*, soft (*broadest)*
  - Central banks typically play a central role, but different models coexist

Finance ministries also key role

Illustrative Macroprudential Policy Institutional Framework Models

Selected Country Examples

	Central Bank Model		**Separate Committee Model**
	Model 1 (Board or Governor)[1]	**Model 2 (Internal Committee)**	**Model 3 (Committee outside the central bank)**
Countries	Argentina, Belgium, Brazil*, Cyprus, Czech Republic, Estonia*, Hong Kong (SAR)*, Hungary, Indonesia, Ireland, Israel, Italy* […].	Algeria, Malaysia*, Morocco, Saudi Arabia, South Africa, Thailand, and the UK.	Austria (M), Chile (M), Denmark (C), France (M), Germany (M), Iceland (M), India (M), Korea (M), Malta (C), Mexico (M), Poland (C), Romania (C), Turkey (M), and the US (M).

*: Jurisdictions that have an additional council including other supervisors that plays a coordinating role.
(C): Council is chaired by the central bank. (M) Council is chaired by a government minister.

Operational considerations

- Comprehensive framework for monitoring systemic risk is key
  - Types of risks
    - Economy wide risks
    - Sectoral risks
    - Vulnerabilities from maturity or currency mismatches
    - Structural risks due to interconnectedness *(common exposures, linkages, systemic intermediaries & infrastructure)*
  - Assessing a variety of indicators, not focusing on one
    - Early warning indicators
    - Measures of leverage, debt service
    - Macroprudential stress tests
    - Supervisory information

Operational considerations (continued)

- Tools (*examples*)
  - Broad based capital tools: *dynamic provisioning, countercyclical capital buffer*
  - Sectoral capital and asset side tools: *Loan to value, debt service to income*
  - Liquidity related tools: *reserve requirements, liquidity coverage ratio*
  - Mitigating contagion from systemic institutions: *capital surcharges, TLAC*
  - Adressing risks non-bank activities and interconnectedness: *central clearing OTCs*
- Making tools operative
  - Calibration is complex: commensurate to risks
  - Consider costs and benefits: *adjustment, efficiency and output costs*
  - Assessing and addressing leakages
  - Considering potential for tools to be relaxed
  - Improving info base: *closing info gaps, improve data collection*

Assessing effectiveness

- Impact on resilience, credit dynamics and agents' behaviour
- No consensus yet, but some emerging patterns as experience is growing:
  - Capital based tools can support resilience and credit growth during downturns, but appear to have limited effects in the upswing.
  - Sectoral capital requirements increase resilience via additional buffers, but evidence on the effect on credit growth remains inconclusive.
  - Asset side tools support resilience of borrowers and limit procyclicality.
  - Reserve requirements may help moderate credit growth, but experience with other liquidity tools remains limited.
- Evidence from CCA Working Group on Macropru policy - **credit register data**
  - Effective in dampening credit cycles and reducing banking sector risks.
    - Policies used counter-cyclically have successfully reduced credit growth.
  - Complementarity with monetary policy boosts impact on credit growth
  - Provisions and capital requirements) particularly effective in reducing banking sector risk

International consistency

- Cross border effects
  - Create positive externalities in terms of resilience, buffers but…
  - … potential for cross-border leakages, risk migration & spillovers.
  - Can undermine effectiveness of domestic macroprudential policy.
- Externalities highlight the usefulness of cross-border coordination of macroprudential policies
  - Example: reciprocity arrangement for Basel III countercyclical capital buffer