

International Financial Co-operation

The Reserve Bank actively participates in work aimed at improving the global financial architecture and addressing the ongoing challenges facing the global economy. It does so through its membership of global and regional fora and its close bilateral relationships with other central banks.

Group of Twenty (G-20)

The G-20 continues to play a prominent role in co-ordinating international efforts to address global economic and regulatory issues. G-20 leaders met in Seoul in November 2010, and the ongoing work of the G-20 continues to be overseen by G-20 finance ministers and central bank governors and their deputies.

At the Seoul Summit, G-20 leaders released the 'Seoul Action Plan' outlining policy commitments by G-20 members as part of the 'Framework for Strong, Sustainable and Balanced Growth'. The Framework initiative, which was launched at the Pittsburgh Summit in September 2009, provides a mechanism for countries collectively to assess the consistency of their policies with a durable global economic recovery. A recent focus of the Framework exercise has been members' external positions, and finance ministers and central bank governors announced at their April 2011 meeting that they had agreed on a set of guidelines to assist in identifying 'persistent imbalances' that may require policy actions. It is intended that a more detailed assessment of the nature and causes of such imbalances will inform the 2011 'Action Plan', which is due to be discussed by leaders at their Summit in Cannes in November. The Reserve Bank and the Australian Treasury are members of a working group that is guiding the Framework exercise.

In Seoul, G-20 leaders also endorsed measures to strengthen international financial regulatory arrangements, including new bank capital and liquidity standards. Ongoing work on other regulatory issues such as regulation of shadow banking remains a priority for the G-20. Another priority for the G-20 has been to ensure that the international financial institutions, including the International Monetary Fund (IMF), have appropriate resources and governance arrangements. As discussed below, there were some significant reforms in this regard over the past year.

Two additional areas of focus for the G-20 to which the Reserve Bank is contributing are reform of the international monetary system and issues pertaining to commodity prices. On the former, the Bank is represented on a working group that is considering issues regarding the management of global liquidity and capital flows, including the composition of the Special Drawing Right (SDR), financial safety nets, the development of local currency capital markets, and members' experiences with managing capital flows. On commodity prices, the Bank is represented on a G-20 study team that has been analysing the main determinants of commodity prices, and on an experts' group on fossil fuel price volatility. The Australian Treasury is also participating in each of these groups.

Financial Stability Board (FSB)

The FSB has an ongoing role in assessing vulnerabilities in the global financial system, as well as co-ordinating the reform of the financial system architecture to minimise the probability and severity of future financial crises. The FSB has a broad membership, including representatives from 24 economies (including all of the G-20

countries), the main international financial institutions (including the IMF, the Bank for International Settlements (BIS) and the World Bank) and the standard-setting bodies, such as the Basel Committee on Banking Supervision (BCBS) and the Committee on Payment and Settlement Systems (CPSS).

The Reserve Bank and the Australian Treasury jointly represent Australia on the FSB. The Governor is a member of the FSB Plenary (the ultimate decision-making body) and two of the FSB's committees. The Head of Financial Stability Department is a member of a group that provides analytical support on assessing global financial vulnerabilities.

A major area of the FSB's recent work relates to systemically important financial institutions (SIFIs). In late 2010, the FSB presented a report and policy options to G-20 leaders on reducing the moral hazard posed by SIFIs. A key feature of this report was to distinguish between those institutions that are systemically important in a global context – termed global SIFIs (G-SIFIs) – and those that are important only in a domestic context. Given the greater risk they pose to the global financial system, the G-20 agreed that, along with other measures, G-SIFIs should have higher capital than the new Basel III minimum. Senior Bank staff are also involved in a macroeconomic assessment of the impact of the FSB's G-SIFI recommendations, especially the likely capital surcharge; this task is being undertaken by the FSB in co-operation with the BCBS, the BIS and the IMF.

Other main areas of the FSB's work over the past year include¹:

- Improving resolution frameworks, including through the development of key attributes of effective resolution regimes that identify the essential features that countries should have in their resolution regimes for financial institutions. A package was released for public consultation in July. Related to this, national authorities are being asked to improve the 'intensity and effectiveness of SIFI supervision' – with such efforts guided by an FSB report in this area. National authorities are also assessing how existing frameworks for banking and insurance supervision compare with relevant standards.
- Strengthening the regulation and oversight of the 'shadow banking system', that is, those non-bank financial institutions that engage in bank-like activities and hence are in the credit intermediation chain but do not face the same prudential regulation as banks. The Head of Financial Stability Department has been on an FSB task force developing initial recommendations for discussion, while senior staff from that department have also participated in a group providing information and data to the task force.
- Working jointly with the IMF and the BIS on macroprudential frameworks and tools. A report was released on this issue in February, with a progress report expected later in the year outlining advances in the state of knowledge and covering national and international developments.
- Examining options for reform of over-the-counter (OTC) derivatives markets and market infrastructure, to reduce the scope for contagion (discussed further below).
- Establishing regional consultative groups to broaden the circle of countries engaged in work to promote international financial stability. Six regional groups comprising FSB members and non-members have been established, with Australia included in the grouping for Asia. The first meetings of the groups will take place later in 2011. The Bank, along with the Australian Treasury, will participate in these meetings as required.

The FSB undertook a country peer review of Australia in 2011. The review is part of an FSB program that examines all of its members' financial sectors, especially reviewing progress in implementing the IMF Financial Sector Assessment Program recommendations. The Reserve Bank contributed material to help inform the review, along with other agencies of the Council of Financial Regulators. The results of the review will be published later in 2011. The FSB also recently published thematic reviews on risk-disclosure practices of financial institutions and mortgage underwriting and origination practices. The Head of Financial Stability

¹ For details on these measures, see RBA, *Financial Stability Review*, March 2011.

Department was part of the expert team reviewing mortgage practices and is part of a follow-up group developing an international principles-based framework for sound lending practices. A senior official from the Australian Treasury is participating in a follow-up thematic review of compensation practices to assess country progress since a 2010 review. A thematic review of deposit insurance systems was initiated in July 2011.

Bank for International Settlements (BIS)

The BIS and its associated committees have continued to play an important role in the response to recent challenges, by bringing together high-level officials from central banks and other financial regulatory bodies to exchange information and consider lessons from the crisis.

The Governor or Deputy Governor attends the regular bimonthly meetings of governors at the BIS, which discuss the global economic and financial conjuncture. They also participate in meetings of the Asian Consultative Council (ACC), which focuses on financial and monetary developments in Asia and provides direction for the work of the BIS in Asia.

The Assistant Governor (Financial Markets) represents the Reserve Bank on two BIS committees: the Committee on the Global Financial System (CGFS) and the Markets Committee. The CGFS discusses vulnerabilities in the global financial system and structural developments in financial markets, while the Markets Committee focuses on the implications of current events for the functioning of financial markets. In the past year, the CGFS has considered issues such as: the interactions of sovereign debt management with monetary and financial stability; sovereign credit risk and bank funding conditions; macroprudential frameworks and instruments; the financial stability implications of fixed-income strategies of institutional investors; and access to central counterparties in OTC derivatives markets.

The Assistant Governor (Financial Markets) is chairing a Markets Committee study group on high-frequency trading in foreign exchange markets. The Head of International Department is participating in a CGFS working group on global liquidity, and a senior manager from the Financial Markets Group is participating in a CGFS study group on the system-wide implications of liquidity regulation.

Basel Committee on Banking Supervision (BCBS)

The work of the BCBS over the past year has focused on finalising the reforms to the key capital and liquidity standards for banks and other deposit-taking institutions. The reforms, known as Basel III, aim to increase the resilience of the global banking system and ensure greater financial stability, by requiring banks to have more, and better quality, capital and hold larger amounts of liquid assets than prior to the crisis. The changes represent a major overhaul of the standards under which banks will operate. The reform efforts have been led by the BCBS and its oversight body, the Group of Governors and Heads of Supervision (GHOS). The Assistant Governor (Financial System) and the Chairman of the Australian Prudential Regulation Authority (APRA) represent Australia on the BCBS, while the Governor and Chairman of APRA represent Australia on GHOS. Key details of the reforms were announced by GHOS following its meetings in July and September 2010. The final package of reforms was presented to the November 2010 G-20 Leaders' Summit in Seoul before being published by the BCBS in December 2010.

As reported in the March 2011 *Financial Stability Review*, one of the key issues requiring clarification was the treatment under the liquidity reforms of countries such as Australia, where the supply of government and quasi-government securities is limited and banks therefore cannot hold enough eligible liquid assets to meet the liquidity requirement in that way. To make the requirement workable for countries in Australia's position, the BCBS' framework incorporates three alternative treatments for the holding of liquid assets. The first option, and the one that APRA and the Reserve Bank have agreed should be adopted in Australia, involves allowing banks to establish contractual committed secured liquidity facilities with their central banks, subject to an

appropriate fee; the committed amount would cover the shortfall between an ADI's liquid asset holdings and the regulatory requirement (see chapter on 'Operations in Financial Markets'). The Reserve Bank has been working with APRA on finalising the details of how the facility would work, including its pricing and the range of assets that would be eligible as collateral.

The BCBS has also worked, at the request of the FSB, on developing a methodology for identifying global systemically important banks, and for determining the size of, and instruments to be used for, the additional capital that such institutions will be required to hold. A consultation paper outlining this methodology was released by the BCBS in July 2011. A senior manager from Financial System Group has been involved in the Macroprudential Supervision Group of the BCBS that has undertaken much of this work.

Committee on Payment and Settlement Systems (CPSS)

The CPSS serves as a forum for central banks to monitor and analyse developments in payment and settlement infrastructures and set standards for them. The primary focus of the CPSS over the past year has continued to be the setting of international standards for financial market infrastructures. In conjunction with the Technical Committee of the International Organization of Securities Commissions (IOSCO), the CPSS released a draft of the new Principles for Financial Market Infrastructures in March 2011 for consultation. The principles seek to consolidate, update and strengthen existing standards for systemically important payment systems, central counterparties and securities settlement systems, and extend their coverage to trade repositories. The principles also incorporate specific guidance for infrastructures serving OTC derivatives markets. The Head of Payments Policy Department is a member of the Steering Group undertaking the review, and the department also continues to contribute to specific work streams. The final principles are expected to be published in early 2012.

A key issue arising from the work on the new principles, along with the ongoing reform of OTC derivatives markets, is how to achieve fair and open access to central-clearing services. The Reserve Bank has been engaged in this work from an early stage through its membership of the OTC Derivatives Regulators' Forum, an international group that provides regulators with a means to co-operate and share information in relation to OTC derivatives, central counterparties and trade repositories. Questions of access to central-clearing services are now being addressed by two complementary working groups, one under the CGFS and another under the CPSS and IOSCO. Payments Policy Department continues to be involved in this ongoing work.

The Reserve Bank is also participating directly in two further working groups: a CPSS working group on innovation in retail payments; and a joint CPSS-BCBS working group considering settlement risk in foreign exchange transactions.

International Monetary Fund (IMF)

The IMF has continued to play a prominent role in the international response to the lessons of the financial crisis. In the past year, the IMF has provided a substantial amount of financial assistance to its members. There has also been ongoing reform in areas such as governance and surveillance.

In 2010/11, the most prominent forms of assistance to IMF members were the loan facilities provided to Ireland and Portugal and the ongoing assistance to Greece. These lending packages were organised in conjunction with the European Union, with the IMF providing around one-quarter of the €85 billion pledged to Ireland and one-third of Portugal's €78 billion assistance package. This followed the IMF's contribution of €30 billion to the May 2010 assistance package for Greece.

To ensure that the IMF has adequate resources to cover members' future financing needs, the Executive Board approved an enlargement of the New Arrangements to Borrow (NAB). Under the expanded NAB, a total of SDR 211 billion (around US\$335 billion) was made available, if required, to supplement the resources from members' subscription payments (quotas) to the Fund.

Some significant changes to the IMF's governance arrangements were approved over the past year. Following earlier G-20 commitments to better align IMF quota shares with members' present importance in the world economy, the IMF Board of Governors approved both a doubling of IMF quotas and a shift of around 6 per cent in quota shares to dynamic emerging market and developing countries. Other governance reforms agreed included a shift to electing all members of the Executive Board and increasing the number of representatives from emerging market and developing countries.

The Reserve Bank works with the Australian Treasury to provide regular briefings to Australia's Constituency Office at the IMF on issues being considered by the IMF Executive Board. During the year, some of the main issues discussed by the Executive Board have related to: the ongoing review of the IMF's surveillance, particularly its multilateral and financial sector surveillance activities; potential reforms to the international monetary system, including the role and composition of the SDR; and the governance reforms noted above. The Bank supports the Constituency Office directly by providing an advisor with expertise in financial markets and financial sector issues. It also provides support to other IMF activities – for example, the Assistant Governor (Banking and Payments) has participated in the IMF's Financial Sector Assessment Program in China over the past 12 months.

As part of its regular annual review of the Australian economy and policy, known as the Article IV Consultation, an IMF team visited Australia in July 2011. In November 2010, the IMF released its 'Report on the Observance of Standards and Codes', which reviewed the quality of economic data gathered by various Australian agencies including the Reserve Bank.

Organisation for Economic Co-operation and Development (OECD)

The OECD is an international organisation comprising the governments of 34 countries, which is committed to promoting policies that improve economic and social development globally. The OECD conducts economic research as well as regular assessments of member countries' economic conditions and policies. Australia joined the OECD in 1971, and the Bank has participated in its activities mainly through staff secondments and membership of several economics-related working groups and committees. More recently, in December 2010, the Assistant Governor (Financial System) was elected Chair of the OECD's Committee on Financial Markets, which is the main OECD body dealing with issues in financial markets, such as banking, securities, and derivatives.

Executives' Meeting of East Asia-Pacific Central Banks (EMEAP)

EMEAP brings together central banks from 11 economies in the East Asia-Pacific region – Australia, China, Hong Kong SAR, Indonesia, Japan, Korea, Malaysia, New Zealand, the Philippines, Singapore and Thailand – to discuss monetary and financial stability, seek ways to foster closer co-operation, and exchange information and expertise on issues of common interest. The Reserve Bank participates in EMEAP at a number of levels, including the Governor and Deputy Governor. The Governor of the Reserve Bank was Chair of the EMEAP Governors in 2010, with the responsibility having passed to the Governor of the Bank of Korea, Dr Choongsoo Kim, for 2011.

At the Deputy Governor level, the Monetary and Financial Stability Committee (MFSC) considered ways to further enhance regional co-operation and the monitoring of economic and systemic risks. In addition, the Bank continued to participate in the three working groups that report to the Deputies and support the surveillance work of the MFSC: the Working Group on Financial Markets, the Working Group on Banking Supervision, and the Working Group on Payment and Settlement Systems.

EMEAP also retained responsibility for the ongoing oversight of Asian Bond Fund 1, a US dollar-denominated Asian bond fund, and Asian Bond Fund 2, comprising eight local currency-indexed bond funds and a Pan Asia Index Bond Fund (PAIF). The Reserve Bank's Deputy Governor continued to chair the PAIF Supervisory Committee.

Economic activity in most EMEAP economies has been growing at a faster pace than in the large advanced economies that were at the centre of the global financial crisis, and there have been strong capital inflows to the region. As a result, the focus of discussions at EMEAP meetings in the past year was on the potential risks arising from capital flows and possible policy responses, as well as the implications of recent developments in commodity prices.

The Reserve Bank hosted one of the biannual EMEAP Deputies' Meetings, as well as meetings of the MFSC and the ABF Oversight Committee and the PAIF Supervisory Committee, in Perth in May 2011. The Bank also hosted:

- the Working Group on Bank Supervision (with APRA) in Sydney in October 2010 to discuss the implications of the Basel III reform proposals for EMEAP economies and issues related to financial system stability across the region; and
- an EMEAP/BIS Forum on Foreign Exchange Markets and a meeting of the Working Group on Financial Markets in Sydney in December 2010.

In addition to these meetings, the Reserve Bank attended the 6th EMEAP-Eurosystem High-level Seminar in June 2011 in Amsterdam, which brought together Governors or Deputy Governors from EMEAP and euro area central banks to discuss issues of mutual interest and develop closer ties between the two regions. The seminar discussed economic policy challenges facing both regions, against the background of the sovereign debt issues in the euro area.



Four meetings in Perth in May 2011 were attended by senior EMEAP representatives and co-ordinated by a team of Reserve Bank staff

Government Partnership Fund (GPF)

The Reserve Bank continued its activities with Bank Indonesia (BI) under the auspices of the Australian Government's GPF. The GPF program supports an exchange of skills and knowledge between Australian public-sector institutions and their Indonesian counterparts through a series of attachments and workshops.

In 2010/11, there were 26 staff exchanges between the Reserve Bank and BI, bringing the total number of exchanges to around 175 officers since the start of the program in 2005/06. In the past year, attachments of BI officers to the Bank covered both policy and operational aspects of the Bank's activities, including economic analysis, financial markets, financial stability, auditing and financial administration. The Bank's Information Department hosted an attachment of BI officers for the first time. Reserve Bank officers visited BI to discuss regional and industry analysis and risk management issues.

South Pacific Central Bank Co-operation

The Reserve Bank maintains close relationships with the central banks of the South Pacific region through regular meetings, staff exchanges, participation in workshops and the regular sharing of information on technical issues.

In December 2010, the annual meeting of the South Pacific Central Bank Governors was held in New Zealand. This group comprises the central banks of those countries in the region with their own currencies – that is, Australia, Fiji, New Zealand, Papua New Guinea, Samoa, Solomon Islands, Tonga and Vanuatu. Representatives from the IMF's Pacific Financial Technical Assistance Centre (PFTAC) and the World Bank also participated in the meeting. The main issues discussed were recent economic developments and the transmission mechanism of monetary policy in the island states, with the World Bank also providing an update on a project relating to payments systems in the region. The Governors and a representative from APRA also met with the major commercial banks operating in the Pacific to discuss banking developments, including interest margins, the cost of remittances and access to banking services.

Among staff exchanges, a Reserve Bank officer completed a nine-month secondment to the Reserve Bank of Vanuatu. Reserve Bank officers also participated in the annual meeting of the Association of Financial Supervisors of Pacific Countries in Fiji and the Bank of England's Centre for Central Banking Studies/PFTAC workshop in Tonga.

Several staff from the National Reserve Bank of Tonga attended a Reserve Bank management training course and the Bank hosted officers from the Central Bank of Solomon Islands and the Reserve Bank of Fiji. The Bank has also renewed a scholarship scheme to enable Bank of Papua New Guinea staff to pursue postgraduate studies at an Australian university.

Bilateral Relations and Co-operation

As in previous years, the Reserve Bank continued to receive a number of visitors from overseas. Predominantly from foreign central banks, the visits covered the full range of the Bank's activities and included delegations from Brazil, China, Ghana, Malaysia, Tonga and Vanuatu.