

# International Financial Co-operation

International co-operation increased through the global financial crisis and has remained high over the past year as conditions in financial markets have improved. Various groups are currently addressing shortcomings in the global financial architecture that were revealed by the crisis. The Reserve Bank is an active participant in these efforts 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 has taken a lead role in co-ordinating the global efforts to address issues arising from the crisis. In the past 12 months, G-20 leaders met in Pittsburgh in September 2009 and in Toronto in June 2010. The ongoing work of the G-20 has been overseen by G-20 finance ministers and central bank governors and their deputies.

At their Pittsburgh Summit, G-20 leaders committed to policies to secure a durable economic recovery, while also discussing strategies to return policy to more normal settings as the recovery took hold. The leaders launched a 'Framework for Strong, Sustainable and Balanced Growth', under which countries collectively assess the consistency of their policies with these three aims. At the Toronto Summit in June, G-20 leaders agreed that this mutual assessment process would proceed at the individual country and European level. Advanced G-20 economies also committed to develop plans to reduce fiscal deficits and stabilise debt to GDP ratios.

The Reserve Bank and Australian Treasury are contributing to the Framework initiative through membership of a G-20 working group established to guide the process. The Reserve Bank is also represented on an experts' group that is considering potential enhancements to global financial safety nets.

In both Pittsburgh and Toronto, leaders reiterated their commitment to strengthen international financial regulatory arrangements, including measures to improve the quality and quantity of bank capital and discourage excessive leverage in the financial sector. Leaders have called on national authorities to establish crisis management groups for major cross-border financial firms.

Another priority for the G-20 has been to ensure that international financial institutions, including the IMF, have appropriate resources and governance arrangements. To support this, G-20 leaders committed to enlarge the IMF's New Arrangements to Borrow. They also committed to shift IMF quota shares by at least 5 per cent to under-represented countries. The Australian Treasury is co-chairing a working group on IMF reform.

## Financial Stability Board (FSB)

The FSB is playing a key 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, with representatives from the national financial authorities of 24 economies (including all of the G-20 countries), the main international financial institutions, including the Bank for International Settlements (BIS) and the IMF, and standard-setting bodies, including the Basel Committee on Banking Supervision (BCBS) and the Committee on Payment and Settlement Systems (CPSS).

The Reserve Bank is an inaugural member of the FSB (and its predecessor, the Financial Stability Forum). The Governor represents the Reserve Bank on the FSB, and the Head of Financial Stability Department is a member of a group that provides analytical support on assessing vulnerabilities. With the transformation and enlargement of the Financial Stability Forum to the FSB in April 2009 (discussed in the 2009 Annual Report), the Australian Treasury joined the Bank in representing Australia on the FSB.

Key areas of the FSB's work over the past year include:<sup>1</sup>

- commissioning, jointly with the BCBS, an assessment of the macroeconomic impact of the proposed major reforms to banks' capital and liquidity requirements, which the BCBS had released in December 2009 and are discussed further below;
- developing, jointly with the IMF, early warning indicators of financial vulnerabilities;
- assessing the usefulness of macroprudential measures to reduce excess build-up of system-wide risk in the financial system, for example, by reducing procyclicality in bank capital;
- working jointly with the IMF and BCBS on the issue of capital and liquidity surcharges on systemic institutions, and systemic levies and taxes;
- analysing options to reduce the moral hazard posed by systemically important financial institutions, often described as 'too big to fail' institutions (to this end, the FSB provided a list of policy options in this area to the G-20 leaders at the Toronto Summit);
- developing firm-specific contingency and resolution plans (or 'living wills'), particularly for the large cross-border banks;
- examining options for reform of over-the-counter (OTC) derivatives and market infrastructure, to reduce the scope for contagion between (systemic) entities (discussed further below); and
- strengthening accounting standards, including improved converged standards for financial instruments and their valuation.

Another important area of the FSB's work has been to improve international adherence to standards, such as in the banking and insurance sectors. In this context, the FSB has commenced periodic 'thematic' reviews across countries as well as more wide-ranging reviews of individual countries. The initial thematic review on compensation concluded in early 2010; a senior official from the Australian Treasury participated in the review team. Australia has volunteered to undergo a country peer review in 2011.

## Bank for International Settlements (BIS)

The BIS and its associated committees have continued to play an important role in the response to the challenges posed by the global crisis, 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 attended the regular bi-monthly meetings of governors at the BIS and participated 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. In February 2010, the ACC met in Sydney as part of the series of high-level meetings that coincided with the Reserve Bank's 50<sup>th</sup> anniversary.

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

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<sup>1</sup> For details on these measures, see RBA *Financial Stability Review*, March 2010.

on the implications of current events for the functioning of financial markets. Over 2009/10, the CGFS published reports on the functioning and resilience of cross-border funding markets; funding patterns and liquidity management of internationally active banks; long-term issues in international banking; the role of margin requirements and haircuts in procyclicality; macroprudential instruments and frameworks; and credit risk transfer statistics.

The Assistant Governor (Financial Markets) chaired the working group that reported on the impact of the crisis on cross-border funding patterns and liquidity management of international banks. The Head of the Reserve Bank's International Department participated in the working group on long-term issues in international banking. A senior manager from the Financial Markets Group participated in a CGFS Workshop on Macroprudential Instruments. Another senior manager from the Financial Markets Group was involved in the CGFS working group that reported on credit risk transfer statistics and in the Review Group for the BIS/ECB/IMF Handbook on Securities Statistics.

## Basel Committee on Banking Supervision (BCBS)

As with the FSB, the BCBS also underwent an expansion in membership in 2009, to include Australia and all the remaining G-20 countries, as well as Hong Kong SAR and Singapore. The BCBS is the international standard-setter in the area of bank regulation and supervision. As such, it has played a central role in the international response to the inadequacies in the capital and liquidity management of a number of banks that became apparent during the financial crisis. In December 2009, the BCBS released consultation papers that outlined major reform proposals for capital and liquidity requirements for banks, including:

- raising the quality, consistency and transparency of the capital base;
- strengthening the risk coverage of the capital framework;
- introducing a leverage ratio as a supplementary measure to the Basel II risk-based framework;
- considering measures to promote the build-up of capital buffers in good times that can be drawn upon in periods of stress; and
- introducing two new measures of liquidity risk exposure developed for internationally active banking organisations.

The Assistant Governor (Financial System) and the Chairman of APRA represent Australia on the BCBS. The Reserve Bank and APRA are both actively involved in the reform of the Basel standards. The potential effects of these changes on banks have been assessed via a cross-country quantitative impact study (QIS); APRA co-ordinated the participation of Australian banks in this study. APRA is also involved in a 'top-down calibration group', which will determine the overall calibration of the new regulatory standards for capital and liquidity, factoring in broader macroeconomic considerations. A senior Reserve Bank officer from the Financial Markets Group is participating in the related joint FSB-BCBS group assessing the macroeconomic impact of the proposals. The BCBS and its oversight body considered the output from this work and the public consultation process at meetings in July 2010 and announced a broad agreement of the main design elements of the proposed reforms. A package of finalised measures is to be released by the end of 2010.

## Committee on Payment and Settlement Systems (CPSS)

Since November 2009, the Head of Payments Policy Department has represented the Reserve Bank on the 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. Over the past year, the primary focus of the CPSS has been on the international standards for financial market infrastructures. With the Technical Committee of the

International Organization of Securities Commissions (IOSCO), the CPSS is undertaking a comprehensive review of three sets of international standards: core principles for systemically important payment systems; recommendations for central counterparties; and recommendations for securities settlement systems. While financial market infrastructures generally performed well during the financial crisis, it had been some time since the standards were established. The CPSS and IOSCO therefore agreed to review the standards, with a view to strengthening them where appropriate. The Head of the Reserve Bank's Payments Policy Department is on the Steering Group undertaking this review and two managers in the Financial System Group are contributing to specific work streams. A draft of the work for public consultation is expected in early 2011.

During 2010, the CPSS and IOSCO also drafted guidance for central counterparties and trade repositories in the OTC derivatives market. This guidance is currently under consultation, the results of which will ultimately be folded into the comprehensive review of the standards discussed above.

In addition to contributing to the CPSS and IOSCO work on OTC derivatives, a senior manager from the Financial System Group represents Australian financial regulators at an OTC Derivatives Regulators Forum established in September 2009. The Forum provides regulators of OTC derivatives markets around the world with a means to co-operate, exchange views and share information related to OTC derivatives, central counterparties and trade repositories.

## International Monetary Fund (IMF)

The IMF has also been involved in responding to the financial crisis and in the host of international work that is seeking to reduce the likelihood of, and better prepare for, any future financial crisis. There has been ongoing reform of the IMF over the past year, including to its resourcing, governance, lending facilities and surveillance mandate.

In late 2009, the IMF undertook around US\$285 billion of allocations of Special Drawing Rights (SDRs), to supplement member countries' foreign currency reserves and thereby help to address the shortage of liquidity.<sup>2</sup> Australia supported this initiative by establishing an arrangement by which it stands ready to exchange SDRs for foreign currency, especially from countries that wish to reduce their SDR holdings.

The IMF has continued to provide financial assistance to member countries, with the assistance for Greece a recent high-profile example. As noted above, G-20 leaders agreed to increase the IMF's funding through an expansion of the New Arrangements to Borrow, and there are ongoing discussions about increasing quota resources. In late 2009, G-20 countries also agreed to a shift in quota shares that would give emerging market and developing countries greater voting power in the IMF. More generally, the IMF has been actively involved in several aspects of the G-20 work agenda, such as the G-20 Framework for Strong, Sustainable and Balanced Growth and examining options for financial sector burden sharing.

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 mandate, the instruments that the IMF has to respond to periods of financial distress, and the Fund's governance arrangements. The Bank supports the Constituency Office directly by providing an advisor with expertise in financial system and markets issues. The Bank also provides assistance to other IMF activities – for example, the Assistant Governor (Banking & Payments) has participated in the IMF's Financial Sector Assessment Program in both Indonesia and China over the past 12 months.

An IMF team visited Australia in July 2010 for the regular annual consultation on the economy and policy, known as the Article IV Consultation. As is customary, the team spoke with the Governor, Deputy Governor and

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2 For further information, see Doherty E (2009), 'IMF Initiatives to Bolster Funding and Liquidity', RBA *Bulletin*, November.

Assistant Governors of the Reserve Bank. Another team from the IMF visited Australia in March to assess observance of the IMF and World Bank standards and codes relating to the dissemination and quality of statistics. The team spent time with several agencies involved in the production and dissemination of data, including the Reserve Bank, and a range of users of macroeconomic and financial statistics.

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

EMEAP is an important regional forum, in which the Reserve Bank is extensively involved. It brings together representatives from 11 economies in the East Asia-Pacific region – Australia, China, Hong Kong SAR, Indonesia, Japan, Korea, Malaysia, New Zealand, the Philippines, Singapore, Thailand – to discuss monetary and financial stability, and exchange information and expertise on issues of common interest. The Governor of the Reserve Bank is the Chair of the EMEAP Governors in 2010.

The focus of discussion at EMEAP meetings in the past year has been on economic conditions and policies in the aftermath of the financial crisis. Most EMEAP economies experienced milder downturns than the large advanced economies at the centre of the crisis, and economic activity has recovered relatively quickly. Reflecting these outcomes, attention has focused on issues such as the appropriate timing of exit from the stimulatory policies that were introduced to mitigate the effects of the crisis, and the potential risks associated with strong capital inflows to the region. At the deputy governor level, the Monetary and Financial Stability Committee (MFSC) focused on the implications for EMEAP members of the proposed changes to international regulatory standards.

The Reserve Bank participates 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 is also responsible 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).

In addition to the regular EMEAP meetings, the Reserve Bank hosted the 5<sup>th</sup> EMEAP-Eurosystem High-level Seminar in February 2010. This event brought together governors from EMEAP and euro area central banks to discuss issues of mutual interest and to develop closer ties between the two regions. Governors and their representatives discussed economic policies in the aftermath of the financial crisis, the challenges posed by cross-border banking and the prospect of strengthening macroprudential supervision. The Reserve Bank also hosted the EMEAP Governors annual meeting in Sydney in July 2010.



EMEAP Governors in session, Utzon Room, Sydney Opera House, July 2010

## Government Partnership Fund (GPF)

The Reserve Bank has continued its program with Bank Indonesia (BI), under the auspices of the Australian Government's GPF. This program supports an exchange of skills and knowledge between Australian public-sector institutions and their Indonesian counterparts; the first phase of the five-year program concluded in 2009/10 and the second phase is now under way.

The Reserve Bank's program with BI has expanded over time to encompass all aspects of central banking. In 2009/10, there were 40 staff exchanges between the Reserve Bank and BI, bringing the total number of exchanges to 145 officers since the start of the program in 2005/06. In the past year, attachments of BI officers to the Bank ranged from one week to four weeks and covered both policy and operational aspects of the Bank's activities. In May 2010, staff from the Economic Group participated in a workshop on inflation and potential output, which represented the culmination of research work by BI over the previous year. Several officers from the Financial Markets Group participated in a workshop on monetary operations, while other Reserve Bank officers visited BI to discuss risk management, human resources, auditing and payments issues.

## South Pacific Central Bank Co-operation

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

In December 2009, South Pacific Central Bank Governors met in the Solomon Islands. 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 also participated in the meeting. The main issues discussed were the effects of global developments on the Pacific islands, economic prospects for the region and financial literacy. The South Pacific Governors met again in April 2010 in New Zealand, to discuss economic and financial sector developments.

Among the staff exchanges, a Reserve Bank officer returned from a 12-month secondment to the Reserve Bank of Vanuatu and was replaced by another officer for a further nine months. Reserve Bank staff also presented at a workshop of South East Asian Central Banks in July 2009 and at the annual meeting of the Association of Financial Supervisors of Pacific Countries in November 2009. Several officers from the Central Bank of Samoa participated in a Reserve Bank training course, and the Bank's Economic Group hosted officers from the Bank of Papua New Guinea to discuss economic analysis and monetary policy.

## 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 Argentina, China, Ghana, Malaysia, South Korea, Sweden, Thailand and Vietnam. In addition, the Bank welcomed two delegations from Iraq. The first delegation included academics, trainers and officials from the Centre for Accounting and Finance Training (which operates from within Iraq's Ministry of Finance), and the second delegation included representatives from the Iraqi Ministry of Finance and the Central Bank of Iraq, among others.