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Welcoming Remarks at the FSB RCG Americas Meeting

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Welcoming words

Good afternoon, and welcome to Santiago. It is my great pleasure to host this year's meeting of the FSB Regional Consultative Group for the Americas, organized jointly by the Financial Stability Board, the Financial Markets Commission of Chile and the Central Bank of Chile. Let me extend a warm welcome to our distinguished guests, esteemed colleagues, and participants. We are honored by your presence here today, particularly as we gather together to address some of the most pressing challenges and latest developments in the realms of financial stability, market development and regulatory coordination.

Allow me to especially acknowledge the presence of Mr. Klaas Knot, Chair of the Financial Stability Board and Tiff Macklem and Kenneth Baker, Co-Chairs of the Regional Consultative Group for the Americas, whose work and commitment have contributed greatly to shaping our global and regional efforts aimed at enhancing financial stability.

I am also glad to extend a warm welcome to Mr. Rodrigo Coelho, Head of Policy Benchmarking of the Financial Stability Institute, who will be our keynote speaker today, whose expertise and perspective I am sure will provide us with key concepts and insights to foster today's discussions.

Lastly, let me express my sincere gratitude to the organizing teams of the Secretariat of the Financial Stability Board, the Financial Markets Commission, and our team in the Central

Bank of Chile, for their hard work and dedication that have been instrumental in making this event possible.

The Role of Macro-prudential Policies and Institutional Arrangements

The topic of our seminar today—macro-prudential policy frameworks, and the coordination and interaction of micro- and macro-prudential policies—is both timely and critical given the increasing complexity of global financial markets and the emergence of risks whose impact could become systemic.

In that regard, macro-prudential policy has become a crucial element to safeguard the stability of the financial system by addressing the systemic risks that can accumulate across financial institutions, markets, and instruments. While micro-prudential supervision focuses on the soundness of individual institutions, macro-prudential regulation aims to prevent the build-up of vulnerabilities that could lead to widespread financial distress, hence focusing on potential systemic risk[1]/.

The origins of the term macro-prudential date back to the late 1970s, with the term generally denoting a systemic orientation of financial regulation and supervision linked to the macroeconomy. The objective of these earlier macro-prudential policies aimed initially at achieving financial stability through smoother economic and financial cycles[2]. Under that premise, several jurisdictions[3] started implementing tools like Loan-to-Value ratios, Margin Requirements and Dynamic Provisions.

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[1] ECB. Financial Stability Review. May 2014

[2] "The distinction between the micro- and macro-prudential dimensions of financial stability is best drawn in terms of the objective of the tasks and the conception of the mechanisms influencing economic outcomes. It has less to do with the instruments used in the pursuit of those objectives." The term "macro-prudential": origins and evolution - BIS Quarterly Review, part 6, March 2010.

[3] Notably the USA and Europe. Macro-prudential regulation: history, theory and policy (bis.org)

However, it was not until the aftermath of the 2008 global financial crisis that international organizations and regulatory bodies began to decisively develop, adopt, and implement macro-prudential policies aimed at mitigating systemic risks that can accumulate over time. This shift was informed by the crisis, which showed that, while traditional micro-prudential approaches are essential, keeping individual financial institutions sound is not enough to protect against unchecked system-wide risks and safeguard from systemic crises. Therefore, policymakers need a broader approach and a toolkit to safeguard the financial system as a whole.

The Basel III framework, as introduced by the Basel Committee on Banking Supervision (BCBS), is a critical step in this direction, providing regulators with tools such as the countercyclical capital buffer (CCyB) and liquidity coverage ratios that aim to enhance financial system resilience during times of stress. The introduction of the CCyB incorporates for the first time a macro-prudential tool within the Basel Standards, aimed at strengthening the resilience and ability of the financial system to withstand shocks and to continue providing financial services, without amplifying the original shock. In this context, Basel III "directly addressed" the risks associated with the "procyclicality" of the financial system[4].

The recent experience with the COVID-19 pandemic, showed that countries where CCyB was activated and accumulated, had some advantages over others where the buffer was not active, mainly by having greater room to liberate this capital buffer during a crisis that was unrelated to a credit boom. Mounting empirical evidence shows that the release of capital buffers worked as it supported the provision of credit.

This pandemic-driven experience with the usability of releasable capital buffers has sparked an ongoing debate regarding the objectives and optimal implementation of tools like the CCyB. There is still heterogeneity in the implementation of CCyB around the globe. Some

[4] The term "macro-prudential": origins and evolution - BIS Quarterly Review, part 6, March 2010

jurisdictions maintain it as originally intended, as a macro-prudential tool linked to the financial cycle. Others have added a resilience-focused approach, informed by its use during the pandemic. Additionally, more recently some jurisdictions followed an approach where the tool is applied considering a positive cycle-neutral rate, that results in a capital buffer that is available most of the time. Some of these countries left room for a more dynamic application of CCyB over a neutral rate linked to the financial cycle.

In Chile, we have also moved towards the full implementation of the Basel III standards, through the 2019 amendment to the General Banking Act, which introduced legal provisions aligned with the Basel standards for the Chilean banking industry and allowed a degree of flexibility so that, through regulations, the banking supervisor —in coordination with the Central Bank— could implement the regulatory standards in force at the international level.

Currently, the near completion of the process of implementing these standards in Chile and a broad number of jurisdictions, has not only strengthened the micro-prudential requirements to boost individual bank solvency, but has also provided central banks and supervisors with additional macro-prudential tools, like the Capital Buffers (capital conservation and countercyclical capital buffers, CCoB and CCyB, respectively), to enhance the resilience of the financial system, to help contain the buildup of systemic risks and address structural vulnerabilities within the financial system[5]/.

However, having access to a tool and implementing it efficiently are two different things. While the powers and possibility of use of a macro-prudential or micro-prudential tool may be available, their effective application requires a deep understanding of the objectives and their impact, as well as proper coordination with other active measures. Depending on the financial regulatory architecture, this may also involve coordination among different authorities. This necessary coordination cannot be achieved successfully without the

[5] BIS-FSB IMF (2016)

implementation of formal arrangements under the specific institutional frameworks of each jurisdiction that suit the countries' specific circumstances[6]/.

The Role of Institutional Arrangements

The evolution of institutional arrangements to achieve the regulatory objectives and promote financial stability is a topic that demands special attention, as we navigate an increasingly complex financial landscape. In such a scenario, a narrow approach to regulation is insufficient in addressing systemic risks. Consequently, macro-prudential policies emerged as a key tool for safeguarding financial stability, complementing the traditional approach of micro-prudential regulation[7].

As I mentioned, the value of macro-prudential policies became particularly evident during the COVID-19 pandemic, which tested the resilience of the global financial system. Unlike in 2008, the financial system was better capitalized thanks in part to the joint requirements and actions implemented by micro- and macro-prudential authorities. During this time macro-prudential tools played a significant role as a complement to monetary and fiscal measures, helping to preserve financial stability and support the real economy during a period of unprecedented uncertainty[8].

However, it is important to bear in mind that the implementation of these measures that bring additional resilience to the financial system is not without costs. Then, this entails permanently evaluating in detail and balancing its benefits and costs.

[6] BIS-FSB IMF (2016)

[7] The sum of micro-prudential risk is less than systemic risk because of externalities. Integrating Micro-prudential Supervision with Macro-prudential Policy (torontocentre.org)

[8] However, macro-prudential policy was constrained by the fact that the accumulated macro-prudential buffers existing at its onset were small or non-existent in many jurisdictions, given the precrisis context of very limited signs of any build-up of financial systemic risk. "The role of macro-prudential policy in the stabilization of macro financial fluctuations." Pablo Hernandez de Cos (2023)

The lessons from this crisis are still being processed. Several studies aim to provide empirical evidence regarding the usability and impact of macro-prudential measures during the pandemic, many focusing particularly on the effects that Capital Buffers had on the credit channel. So far, the evidence suggests that Capital Buffers may help to strengthen banks' solvency and mitigate the risk that banks' lending standards amplify an economic downturn as well as all the spillovers implied. It also adds an additional "resilience" perspective over instruments, like the CCyB, originally thought to act mainly over the financial cycle.

However, while macro-prudential policies have proved their worth during difficult times, the challenge of coordinating them with other policies remains. Financial systems are interconnected, and financial risks can easily spill across borders. Effective regulation, therefore, requires a coordinated approach that integrates both macro- and micro-prudential measures under a cohesive institutional framework.

Institutional arrangements need to support the regular exchange of information through clear communication channels and decision-making processes that balance the potentially conflicting goals of different regulators. The objective is to make the different measures taken by regulators during time of stress more efficient and allow for a consistent implementation of micro- and macro-prudential policies while mitigating potential frictions[9].

In that sense, the implementation of macro-prudential policies like the CCyB must incorporate not only an overall assessment of the financial stability outlook and the potential risks to it, but also a comprehensive evaluation of the level and composition of regulatory capital of the banking industry as well as the capital requirements and other prudential measures implemented by the micro-prudential authority. This evaluation must

[9] Coelho and Restoy. Capital buffers and the micro-macro nexus. BIS. 2024

carefully consider the potential impact of these requirements on banks' cost of capital and the broader economic implications. The procedures with which to advance towards this objective as well as the pending challenges in terms of coordination will be the main topics of discussion at this workshop.

Conclusion: Looking Ahead

As we move forward, the future of financial stability will require a more holistic, integrated approach to macro-prudential and micro-prudential policies. Institutional frameworks must continue to evolve, becoming more adaptive and forward-looking, particularly as we confront emerging risks like climate change and cybersecurity. Likewise, cross border cooperation will continue to play a key role in the years ahead.

Strengthening the channels of communication between micro-prudential and macro-prudential regulators, as well as between domestic and international bodies, is essential.

International cooperation is particularly important in today's globalized financial system. Risks do not stop at national borders, and neither should our efforts to address them. The work of the Financial Stability Board in promoting global standards and facilitating dialogue among regulators is invaluable in this regard.

In the case of CCyB it is a crucial task to ensure a better understanding about the appropriate balance between the macroprudential and the resilience approach. We have a unique opportunity today to share the experiences and perspectives of different FSB members with macro-prudential policies and how their institutional arrangements facilitated their implementation and coordination with other regulatory measures.

But before we delve into that, we will first hear from our Keynote Speaker, Rodrigo Coelho, on the role that institutional coordination arrangements can have in enhancing the

application of both macro-prudential and micro-prudential policies to foster financial stability, particularly on the implementation of the CCyB and Pillar 2 requirements.

I encourage all of you today to engage deeply in the discussions that lie ahead. This meeting is an opportunity to learn from each other's experiences motivated by our common goal of strengthening the resilience of the financial system.

Thank you, once again, for your participation.

I wish you all a very fruitful rest of the day.