



Opening Address

by

Dr. Bandid Nijathaworn

Deputy Governor,

Bank of Thailand

at

**2nd SEACEN-OCC Advanced Seminar on
Quantitative Techniques for Macro Surveillance and
Determining Resilience of the Banking Sector**

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Let me begin by extending a warm welcome to all of you to Bangkok, and to the second SEACEN-OCC Advanced Seminar on Quantitative Techniques for Macro Surveillance and Determining Resilience of the Banking Sector. The Bank of Thailand is pleased to be hosting this seminar, jointly with the US Office of the Comptroller of the Currency and the SEACEN Centre.

Today's seminar reflects another important effort in forging a closer cooperation and network between US regulators and the central banks and regulators of the Southeast Asian region. Such a close tie is most valuable for it is a platform that helps facilitate supervisory coordination that is necessary for an efficient home-host relationship, as well as for exchanging views on important market developments and supervisory issues such as on financial innovation, on the implementation of Basel II, and on accounting standards. Going forward, such a close tie will be even more valuable, because an important component of a good macro-surveillance process is an open and timely dialogue, and exchange of views among regulators from different jurisdictions.

With a deepening process of financial globalisation that we are now seeing, supervisors and central banks are faced with increased challenges to analyse and manage risks, especially in the context of more complex

interlinks between financial institutions and financial markets, as well as between domestic and the global economies. In such an environment, the risk management ability of financial firms and supervisors is important and rests crucially on the ability to assess quantitatively and in a forward-looking manner, the possible impact of each risk scenario on the economy and its financial sector.

In this light, a sound and practical approach to integrate the quantitative assessment into financial stability and into risk-based supervision is most crucial, as it will allow the potential key risk affecting the financial sector to be identified, to be assessed, and to be ranked in order of importance. Through this, the approach will help focus policy dialogue and facilitate communication between all the key stakeholders, namely--the supervised financial institutions, the home and host supervisors, other related supervisory agencies especially in the case of complex financial conglomerates, and between the monetary authority and the Finance Ministry.

In moving forward, it is important to recognize that, while these quantitative techniques are valuable tools, they are no substitute for a thorough understanding of the overall risk dynamic of financial institutions, the related systemic implications, as well as the behaviour of institutions and markets.

The emphasis here is that a good macro-surveillance framework must balance technical excellence and technical complexity with sound rationale and good qualitative judgment in order to make real contribution to policy decision. The robust framework of risk-based supervision such as Basel II places a strong technical demand on supervisors not only on Pillar I but also for the Supervisory Review work in Pillar II, which requires dynamically assessing on-going risk and changing risk profile of financial institutions. Therefore, macro-surveillance, stress-testing, as well as model validation, will fast become the norm for good risk management.

Macro-surveillance and its parallel policy framework—especially macro-prudential policy—are now exciting fields for central banks and supervisory agencies. But in my view, the needed pioneered framework is yet to be developed. The quantitative models and tools so far are at its early stage of development compared to those more established in monetary policy, such as the inflation targeting framework.

The frontier work currently undertaken by central banks of advanced economies are, for example, developing macro-stress testing model which incorporates interlinkages between financial and real sectors. Such work is quite demanding due to the complexity of the

evolving linkages and behaviour linked to rapid developments in economic and financial sector, and all the more so with globalisation. In response, community of experts are emerging, and many such experts are now using virtual network such as stress-testing internet platform to share knowledge and experience.

For emerging economies such as most SEACEN members, it is even more challenging in light of data limitations and continued structural changes that are taking place in our markets, particularly the proliferation of new financial products that consumers are less familiar with, and are less able to manage risk because of market limitations in terms of the availability of hedging instruments. This type of situation, if not properly monitored and supervised, can lead to a build-up of financial vulnerability and risks, for example in consumer finance, real estate, and the housing market. Therefore, supervisors need to work closely with their counterparts in the monetary policy wing to monitor and assess possible risks.

The timeliness of this seminar is all the more important in light of the on-going developments in the global financial markets. Global imbalance between economies continues to be an important underlying risk upon which more financial market volatility can emerge. Linked to this, the geopolitical risk and oil price uncertainty, as well as the volatility

emanating from the sub-prime mortgage markets in the US, could also bear down on the prospect of global growth.

Against this backdrop, emerging markets in Asia have experienced large and volatile capital flows with important implications for currency and for domestic financial conditions. Going forward, the combination of volatile financial markets and downside risk to global trade and growth could have implications for the region's growth and inflation outlook, as well as for credit and market risk for our financial institutions.

Thus, now more-than-ever, macro-surveillance process, early warning models, stress-testing, ever more vigilant risk-based supervision, and strong internal risk management by financial institutions will be instruments crucial for safeguarding our financial stability.

In closing this introduction, I am certain that this seminar will be extremely useful and provide an important opportunity for building a close network amongst supervisors in SEACEN, as well as for fostering a closer cooperation between regulators in our region and the US-OCC.

So, without further ado, let me declare the second SEACEN-OCC Advanced Seminar on Quantitative Techniques for Macro Surveillance and Determining Resilience of the Banking Sector open, and wish you all

every success in this seminar, as well as in your career, and have a pleasant stay in Thailand.

Thank you.