

Surviving the Crisis- Neither Magic nor Luck

Rungporn Roengpitaya

Senior Examiner

Risk Management and Information System Examination Department

Supervision Group

Following every financial crisis, the most popular questions asked by economists and central bankers are: What went wrong? Why didn't we see it coming? and How can we prevent the next crisis?

In Thailand, we asked these questions in the aftermath of the Asian Crisis. Over a decade since then, the Bank of Thailand has worked continuously to strengthen the financial system in accordance with international standards. It has upgraded regulations and supervisory vigilance on risk management and governance practices to enhance the stability of the financial system. The underlying concept used is known as the "macro prudential framework". Examples of the measures used in Thailand included limiting the loan to value on high value real estate loans and implementing Basel II at the end of 2008. These macro prudential measures have worked the magic of limiting the financial system wide distress.

As different crises are never the same, we can depend neither on magic nor luck in preventing and coping with potential systemic distress. On the contrary, the best way to strengthen crisis prevention is to go beyond just "learning from one's own mistakes" to "learning from others' mistakes" as well. In this connection, my colleagues and I look at what we can learn from the crisis in advanced countries in the context of the Thai financial system.

In particular, we set out to study the following. First, regarding the mystery of the sequential bank failure or the "domino" effect of the crisis, we ask: "How should we measure and mitigate these systemic risks in financial markets?" and "Which market players contributed to these risks more than others?" Second, you may recall the news headline "Why can't banks lend more during the bad time like this?" Here, we questioned, "What are the potential causes of credit crunch and what can be done to lessen it?" Third, there is a question of "Can bank governance and efficiency in the financial system be enhanced and how can they be promoted?" 2

Answers to these important questions will guide us toward understanding how best to build a resilient financial system that also contributes to the efficiency of financial markets and intermediaries. Indeed, striking the right balance between stability and efficiency in the financial system has always been the ultimate goal for central banks around the world. Achieving this balance will ensure that the real economy will benefit from financial sector growth and vice versa.

We invite readers to explore "Developing the Efficient and Resilient Financial System for Thailand: Lessons from the Crisis and Challenges Ahead" one of the research papers to be presented at the upcoming Bank of Thailand economic symposium. We will also be discussing important challenges and policy options in crafting future supervisory policies for financial institutions. Surviving the financial crisis is neither magic nor luck, unless one follows the saying of Roman philosopher Lucius Annaeus Seneca: "Luck is what happens when preparation meets opportunity".

(The views expressed are the author's own.)

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