Virtual Executive Panel:
Navigating Global Uncertainty and Building Financial Resilience

Panelists:

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Moderator:

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Transcript:

Babak Abbaszadeh:

Hello, everyone. It's a pleasure to be with you. Welcome to today's webinar: Navigating Global Uncertainty and Building Financial Resilience. We knew this was going to be popular, but it's exceeded our expectations. We have over 400 registrants from 86 countries, so the letters of A are led by Algeria and Angola, and we go all the way to Zambia and Zimbabwe, developed countries, developing countries. If I was going to read them, would be an alphabet soup like Sesame Street show. So, I'm going to spare you that. But just to let you know that we are extremely delighted to have you with us. And today we have convened a panel of distinguished experts. Trust me, you're not going to be disappointed. Each of them is verified. I've seen them speak. They are provocative and they would love to get your questions.

We are in the midst of global uncertainties, including geopolitical tensions, economic turbulence, and shifts in global development policies. I'm not aware of any other supervisory authority or capacity building institution that has convened this kind of a talk yet. And so, if we are the first, excellent because more conversation needs to happen. So recent global tariffs imposed and then temporarily paused by the US have stirred significant uncertainties and anxieties bringing us dangerously close to the brink of economic turmoil and potential financial crises. Based on what I'm hearing from the financial regulatory community, supervisors are also not immune to these anxieties. Another form of uncertainty is that the situation remains very fluid changing almost daily, which renders many existing plans obsolete. How do you plan in the middle of a turbulence? These developments underscore the importance of today's discussion and how supervisors can adapt to these evolving risks. It is vital to discuss what policy measures can be taken to future-proof our financial systems against such profound shifts to protect people's hard-earned savings and investments and to prevent a crisis that will throw more people into poverty.

We're always told not to be emotional, not to be emotive when you talk about these things, but if our speakers choose to do that, trust me, I'm not going to stop them because I don't know where the role of rationality is in all of this. I am pleased to introduce our esteemed panelists, Dr. Stefan Ingves is the chair of Toronto Centre and former governor of Riksbank in Sweden and former chair of the Basel Committee on Banking Supervision. Ms. Elsie Addo Awadzi is a board member of Toronto Centre and former deputy governor of Bank of Ghana. Mr. Nicolas Véron is senior fellow at the Peterson Institute for International Economics in Bruegel, spends half of his time in Europe and in the United States, so will have a lot to offer here. I'm not reading their full bios which have been distributed to you because we want to get to the conversation.

At Toronto Centre, we're committed to enhancing the capacity of financial supervisors and regulators to promote financial stability and inclusion in the face of these challenges. For the past 26 years, we've trained 30,000 of yourselves and your colleagues and our recent publication, I ask you to please take a look at it, called "Supervisory Implications of Global Fragmentation and Uncertainties", highlights the pressing need for proactive supervision. We appreciate your participation, look forward to your questions. And just one last bit of commercial, thanks to the Government of Canada, Government of Sweden, and the IMF for their steadfast support of Toronto Centre.

Let's begin. Stefan, I'm wondering if I can ask you to help us understand. With your vast experience in managing financial crises, how do you assess the current threats to global financial stability, particularly in the context of recent US tariffs and the ripple effects across the global markets? And an associated question to that would be what are the key blind spots that supervisors need to be aware of in today's environment of heightened geopolitical risk and monetary policy divergence? Thank you.

Stefan Ingves:

Thank you, Babak, and thank you for giving me the opportunity to say a few words here. Oh, let's see. I have to get my notes. There. Remarkably, many are logged on, so, apparently, this is a highly, highly relevant topic given the circumstances and it's hard to figure out really where to start. But let me say the following, we can worry about many things, but at the same time do not get carried away because this is not a financial crisis, at least not as of yet. And that is quite different compared to many other things that you deal with at the national level or at the global level. So, if you think about this and what is going on presently and you think about it from a supervisory perspective, then the key issue here is to make sure that it does not turn into a financial crisis either.

And that's really the hard part because there are, if you think about this in terms of risk weights, when it comes to banks, there are known unknowns and there are unknown unknowns, and here we're really talking about unknown unknowns. Babak asked about blind spots, and it almost goes by definition that when we're talking about blind spots, we just don't know about them because if we knew about them, they wouldn't be blind spots anymore. The hard part, of course, when you are a supervisor is that unfortunately you tend to know about the blind spots after they have become visible and that usually means that something has been going wrong.

But in general though, when it comes to this, I would say that go and chase the leverage, and try to tie whatever leverage you find out there, or particularly if you come to the conclusion that a certain phenomenon is over-levered, try to tie that type of buildup of leverage to the macro picture, when it comes to what is going on in your own jurisdiction and what is going on at the global level because that gives you actually an element of guidance. This won't tell you whether things will blow up or not, absolutely not, but at least it gives you some kind of a map. It gives you a way of thinking about these things in advance and that is always very, very helpful.

The hard part, of course, when you are a supervisor is that unfortunately you tend to know about the blind spots after they have become visible and that usually means that something has been going wrong.

Stefan Ingves

Toronto Centre

Now, I take it that given that we have an audience today with participants all over the world, there are probably huge differences within the audience as of today, but one way of thinking about it, regardless of where in the world you happen to be when you're watching, is to think about it in terms of scenarios. Let's say scenario A, scenario B, and scenario C. The hard part when you think about and talk about scenarios is that those scenarios are highly unlikely to ever happen. But if you have chosen your scenarios carefully with a fairly high likelihood, you're going to end up when things do change with the linear combinations of those scenarios, and that is actually helpful because that makes it easier to start and to figure out where to go and where to head next if things get difficult.

But bottom line for now, at least, is that in an uncertain world we can worry about many, many different things, but as of yet, this is not a financial crisis. This is about trade, politics, and a whole bunch of other things and let's hope that it stays that way. Thanks.

Babak Abbaszadeh:

No, thank you very much, Stefan. That's very useful. Also, I want to give you the Oscars here, Stefan, because you stayed within the four minutes that we had asked you. We had imposed a very strict time limit on our speakers because each of them can give a dissertation on these questions, but we want to be able to roll through. So, thank you, Stefan. Thanks for calming us

down a little bit. I don't think necessarily everybody in the audience would necessarily see it the way you do, but it's still good to get the perspective of someone who's brought to an end many of the financial crises we've experienced in our modern time.

Nicolas, let me turn to you. The elephant in the room is the rising economic nationalism and the imposition of the new global tariffs that we just talked about, but how significant is the risk of financial market fragmentation becoming a systemic threat? And it's like in a bit of a game theory, every country seems to be wanting to make their own deals.

So, the difficulty here is really to integrate in your scenario planning and in your supervisory thinking to take risks, and to take risks that have a chance to materialize.

Nicolas Véron

Peterson Institute for International Economics; Bruegel

Are you seeing any convergence or coalition of like-minded countries coming together to form collective action at this point or are we in a mode of every country for itself? Thank you.

Nicolas Véron:

Thanks for having me. And it's a privilege to be part of this panel with Elsie and Stefan. I will pick it up where Stefan left, that this is not a financial crisis, I agree, and how could I not agree with Stefan? But I think we've come very close, a week ago and before Trump sent his famous Tweet (not Tweet), on rolling back the tariffs he had announced the week before. I think what we saw at the beginning of last week was the beginning of a sequence of unraveling that was rapidly taking the form of a financial crisis.

So, I agree with Stefan that we're not in a financial crisis right now, but we saw the making of the financial crisis as recently as a week ago and it could have gone very wrong and maybe that will happen again. So, to just come back to this idea of scenarios, Stefan is right, scenarios are the way to go, but scenarios have to be very bold in times like these. If you were a supervisor in 1989, you had to make a scenario of the unraveling of the Soviet Union. To my knowledge, nobody did that in the supervisory community. If you were a supervisor in the mid-2000s in the Eurozone, you had to make a scenario of the bank sovereign vicious circle.

So, Eurozone, as it happened, did two rounds of stress test, in 2005 and 2006. For obvious political reasons, it didn't go nearly far enough in their scenario planning during those stress test exercises to really test the boundaries of the resilience of the system. And now, with retrospect, we know not only that those scenarios were inadequate, but that the banks in the Eurozone were tremendously undercapitalized and that explains a lot of what happened in the following decade.

So, the difficulty here is really to integrate in your scenario planning and in your supervisory thinking to take risks, and to take risks that have a chance to materialize. Now, we're very lucky because we saw it at the beginning of last week, so we know what to scenario plan and what the scenario plan is displacement of the dollar at the center of the system because that's exactly what started to happen in those days early last week. So, that would be my advice at this point. It is extraordinary the extent to which we see the unraveling, almost the evaporation of US institutions, and I say this from Washington DC. You take every single one of them, Congress, the judiciary, the independent media, the legal profession, maybe the universities - we'll see, the military, possibly. Institutions are not resilient in the US and that's already a fact, it's not a risk. So, that's I think as a scenario, unfortunately, that has to be planned for, and I'll stop here.

Babak Abbaszadeh:

Thank you, Nicolas. So, I guess just a quick follow-up to you is. you're talking about both you and Stefan talked about scenario planning scenario analysis and looking at tail risks. So that's one thing for regular supervisor, but they also have to react to in the industry decisions. Industry has to make some kind of a decision where to invest. And right now, the rules keep shifting all the time.

So, would you say that any scenario you have, you have to be ready to actually change that scenario right away?

Nicolas Véron:

We're clearly in the moment of high uncertainty and I don't think anybody had exactly predicted the developments of the last three months. Even so, many people had predicted this or that element of it in the context of the presidential campaign in the US, last year. And I omitted, sorry Babak, to answer your question about coalitions of like-minded countries. Actually, I would be very interested in Stefan and also Elsie's viewpoints on this, but I'm not too worried about the international networks that banking supervisors are familiar with. So, BIS, the Basel Committee, international standard setters like the IFRS Foundation for accounting, that kind of thing. I view those as reasonably resilient because at this point, it is the US that is moving away from a global consensus rather than a global consensus unraveling altogether. Of course, we'll see contagion effects, but we will also see effects of different organizations, different countries, different actors coming together to protect themselves against the turmoil that is currently coming from the US, and frankly, leaving aside of course regional situations not from other players.

So, I think that's very important, but your point about uncertainty is very apt. At this point, we're navigating tremendous uncertainty in a way that's a reminder of what happened at the beginning of the COVID-19 pandemic when nobody knew whether this thing would last three days, three months, or three years. And we have something of a bit the same nature right now. In the case of the pandemic, it lasted a few days, maybe a few weeks before we knew more or less the time horizons that we were talking about. Here, I think there is not really a prospect that things will settle that quickly.

Babak Abbaszadeh:

Thank you so much, Nicolas. Let me turn to Elsie. Elsie, so good to see you again. It's always nice to have you on our panels. We talked so far, a little bit about the developed countries, but I really am very interested about your perspective, and you are no stranger to populism and its impact. But let's come to your question directly. Considering the impact of developed countries' trade policies, notably the recent introduction of global tariffs, how are these developments affecting emerging markets? What strategies should central banks and financial supervisors, in these economies, employ to mitigate the adverse effects of external shocks and ensure economic resilience? And the subtext to this question, Elsie, so far, none of us have been talking about people, we're talking about institutions, systems, but there is a risk to actual people in all of this. I'd be very interested to hear your perspective on this question, and I made it more complex for you. Sorry about that.

Elsie Addo Awadzi:

> Countries have not quite recovered from the pandemic as well as the impacts of the war in Ukraine. You still have high inflation in these countries and have fiscal situations that are quite dire.
>
> **Elsie Addo Awadzi**
>
> Toronto Centre

Thank you so much, Babak, and it's really great to be back here, this time with Stefan and Nicolas, whom I have the greatest respect for. So yes, this question is really germane to emerging markets and developing economies. And I might add very quickly, that even there, there's a wide range of experiences and viewpoints depending on market power as well as geopolitics. But I can speak for sure for the great majority of middle-income countries, some low-income countries, and to say that the view there is not as optimistic, maybe in as balanced as Stefan advocated for, which I totally understand anyway, but it just feels like for those on receiving end of this, the picture is quite gloomy.

Let me start from the fact that a lot of these countries have not quite recovered from the pandemic as well as the impacts of the war in Ukraine. You still have high inflation in these countries, used to have fiscal situations that are quite dire. I think the IMF recently talked about 37 or so odd countries in the emerging markets in developing economy world that are at very high risk of debt distress. Countries like Ghana have had to go through a sovereign debt restructuring, including a domestic debt restructuring that hugely affected the banking system. You have Zambia, you have Ethiopia, and so these are already pre-existing conditions. And then, you add on top the fact that aid money has been cut almost overnight, and USAID plays such a key role in some of these economies.

And so, Ghana, for example, almost had $1 billion just wiped out from aid money that was going to go into education, health, and some agriculture. It's also the suddenness of these measures so that these countries haven't had a chance to even plan how to exit from aid, for example. If you take the view that the budget for the year's already entrained, being implemented, then it begs the question, how do countries readjust their fiscal positions?

And then, you have the recent trade measures where, in Africa, for example, you had anything from 10% tariffs, introduced on countries like Ghana with whom the US had no trade deficit, to 50% for countries like Lesotho. And then, we've heard about the pause, the 90-day pause. Well, all of that is fine. It gives some breathing space and as Nicolas said, it provides some learning. At least we know that this is a possibility, but the uncertainty is quite real, and I think whatever happens, trust in the global economic order is probably dented in forever.

But what does this mean? It means that countries are going to have to figure out how they survive, some more quickly than others depending on the buffers in place. And Babak, he talked about people. It so happens that in many of these countries, social safety nets are also very weak, and so people are very likely to fall out of a job, or to lose your business, or generally have a hard time dealing with high inflation from trade wars and et cetera. Currency impacts, a lot of these currencies might crash as FDI flows cease as investors pull out of these markets and et cetera.

The question really becomes, how are these countries situated and positioned to mitigate the risks, these macroeconomic risks that are looming very quickly? Invariably, these countries have very fragile banking systems, very shallow capital markets. And so, again, the resilience of these financial systems is very... not where you want them to be. And therefore, my advice, and I don't mean to paint a gloomy picture, but my advice is for these countries to get into planning mode. So, the scenario analysis, as what Stefan and Nicolas alluded to, but I think now more than ever, central banks and supervisory authorities for those that don't exist in the same institutions must begin to work very closely together. What kinds of monetary policy interventions are going to be needed and to preserve currency valuations and et cetera, to manage inflation in a way that does not spill over even more to the banking systems and to the financial systems.

Banks are going to have to deal with non-performing loans. They're going to probably have to deal with exposures, high exposures to the sovereign for countries in high debt distress who could actually get into worse situations with their debt. The banking systems are going to have to figure out how to manage those exposures. And all of these require very close coordination, even for central banks that also are regulatory and supervisory authorities. There's more of a need for the various schemes working in these central banks to work very closely because I find that sometimes, there are silos and because price stability happens to be the primary mandate, many people don't pay a lot of attention to the financial stability mandate, but those need to be coordinated very carefully so that reactions and policy responses to price stability do not exacerbate already assistant fragilities in financial systems. So, that's my number one thing.

And then, supervisors need to understand better how to incorporate these into their stress test, into their risk, into how they oversee banks risk management and incorporate governance frameworks. Basically, the quality of governance and risk management in banks is more important now than ever. How are banks going to navigate these? Another key for me would be banks should already begin to preserve capital. So, I think that as we did in the pandemic and as we've done in every major crisis, how banks may perhaps suspend the payments of dividends to shareholders. Shareholders don't like that, but in times like this with such high uncertainty, particularly for emerging markets and developing economies, capital in the banking system is going to be more critical than ever. And so, supervisors need to keep their eye on these, how MPLs are rising, how risks overall to balance sheets are rising, and then how banks are able to conserve whatever capital is left because access to additional capital at this point will seem almost impossible. Thank you.

Babak Abbaszadeh:

Well, that's great. Thank you so much, Elsie. I think you helped round out the conversation in this panel and you provided a lot of good granular examples and highlighted that different experiences are different in different parts of the world, but I tell you, Canada developed jurisdiction, we are beginning to feel the economic impact. Our auto industry right now is beginning to lay people off, and sooner or later we're going to feel the impact in a broader and Canada was in front lines of the brunt of the tariffs.

> Standard-setters are certainly not going to disappear, because in many cases when it comes to creating global standards, people have been at it for 50 years and participants come and go because you have different kind of domestic political developments.
>
> **Stefan Ingves**
>
> Toronto Centre

So, we're going to now move to the second and last round of the questions. This is structured ones. I encourage you if you have not asked your question, please put your question down so that you can get into the queue, and I'll do my best to get to as many questions as possible. This round is about future-proofing financial systems, policy responses to a shifting global order. Stefan, if I may come back to you again. Amidst the ongoing deregulation and fragmentation of regulatory frameworks, there are heightened vulnerabilities within the global financial system. Considering the Comprehensive Safeguards Institute, since the global financial crisis, and I think you were in the front seat on that, do you believe these are sufficient to withstand the current wave of global tariffs and emerging financial shocks or are we on the cusp of another major financial downturn if certain things don't work out? Thank you.

Stefan Ingves:

Thank you, Babak, for the question. But before I get into answering what you just asked me, let me also quickly comment on what Nicolas said and I agree with him that standard-setters are certainly not going to disappear, because in many cases when it comes to creating global standards, people have been at it for 50 years or something like that and participants come and go because you have different kind of domestic political developments. But given that it's in the interest of most countries to actually create these standards and participate in the work, the work will continue. I'm convinced about that. And to Elsie, it was music to my ears, all the examples that you mentioned in terms of what can go wrong and how you deal with it. I've seen it all from within myself and I couldn't agree more.

Now to your question, Babak, broadly speaking, I think that what was done after the great or global, whichever title you want to use, financial crisis, the things that were done were in the right direction and all those changes that were made, they have later from time to time in various jurisdictions actually served as well. But the thing is that the global financial crisis happened in 2008, and now we're almost 20 years later, and 20 years later, there is a risk of what I would call implementation fatigue because it takes a long, long time for the plumbers to produce these rules. And the politics of this is almost always cyclical, and the cyclicality leads to thoughts and ideas and demands for dilution sooner or later and I think that that's not the right way to go.

What this actually also means is that there is a great danger now that there is a race to the bottom or that there will be a race to the bottom. And that's because we humans always tend to argue that this time is different. Now we have really understood everything, and it is safe to run the system with less capital, which exposed proves to be rarely, rarely the case. More often, it's actually about more capital, not less capital. Whether we have a financial downturn or not, I do think that, and again alluding to what Elsie just said, you will find probably huge differences in different parts of the world and in different countries. So, we just do not know. But at the national level, watch out what is happening on the macro level in order to try to translate the macro into micro.

And when I was dealing with the banking crisis many, many years ago, some of the bankers came to me and said that they were not responsible for what happened because the macro went wrong. And my reply was always, if you are a banker, you are responsible for understanding the macro and no one can save you from that.

So, one common thread in many, many places right now is debt and too much debt and in particular, public-sector debt. And this is the so-called doom loop. Banks holding a lot of public sector debt, and public sector debt in many, many places, if not all places have zero risk weights. And I truly hope that we can handle this issue better than what we have done in the past because it's a terrible thing to work yourself out of that hole because on the one hand you have a fiscal issue, on the other hand, badly manage the fiscal issue translates into a banking sector problem as well. And if history gives us any guidance, it takes you usually many years, and in some instances it's also an IMF program to dig yourself out of that hole.

Now, then when it comes to the global financial system and how it will evolve, that is also an open issue. So, in my view, things are likely to be more unstable than in the past. This does not mean that people will very quickly move away from the US dollar to other currencies, but we do know over longer time periods that if countries one way or the other try to defy gravity, then the rest of the world will slowly move out of that currency into other currencies. Thank you.

Babak Abbaszadeh:

Thank you very much, Stefan. It's good to know that some of the measures that were put together are holding steady. I really liked what you said about implementation fatigue. That's something we don't think about very often. I mean, oftentimes policymakers feel like once they set the rules and all of that, their job is done, let's move to the next challenge. But you're absolutely right, you got to see it all the way through.

Nicolas, I'm going to come back to you now and ask you a two-part question. I hope hopefully you remember both parts because they're both very interesting to me. We've always taken the rule of law, international trading order and other norms for granted, certainly as long as I've been around. And considering the recent drastic policy shifts in the US, I'm hearing from a lot of different sources that is it reasonable to consider it as a safe jurisdiction for investment anymore? So that's one question. And how should international financial governance structures evolve to curb excessive risk-taking and prevent regulatory arbitrage in this new geopolitical climate? Thank you.

> Fortunately for Europe, they adopted the last bit of Basel III just a year ago in their capital requirements regulation. And therefore, I think there's a general sense that a little bit more time is needed to think about the next step.
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> **Nicolas Véron**
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> Peterson Institute for International Economics; Bruegel

Nicolas Véron:

These are great questions, and they gravitate again to what we were discussing at the beginning. So, Stefan was telling us, "Look for leverage in the system." So most leveraged organizations, entities in the system, are typically banks. So, banks are really central to the concerns that we're talking about here. Fortunately, thanks to Stefan's leadership and others when he was at the Basel Committee, we have Basel III, that's an excellent set of standards. I wish the EU would comply with it. It's not quite there, but at least it has strived for some, at least, pretend compliance with Basel III, which is better than the alternative.

So, we're having this vibe now coming from the US Treasury Secretary Bessent has said that the aim was to deregulate the banking sector, to unleash the energies in the US economy, and for other jurisdictions, obviously the question is should we align with the US because there's a reference jurisdiction, and therefore do we enter a race to the bottom in terms of moving away from Basel III? Or should we, on the contrary, heighten, raise our defenses against potential financial instability coming from the US, which all things equal would militate in favor of raising, not decreasing or relaxing capital requirements?

And I think that the whole thing is a debate in many places right now, it certainly is in Europe - fortunately for Europe, they adopted the last bit of Basel III just a year ago in their capital requirements regulation. And therefore, I think there's a general sense that a little bit more time is needed to think about the next step, but it's a very active debate.

So let me circle back to your question. Is the US a safe haven for your investment? This is not investment advice, of course, and I'm not going to make a predictive statement in a very, very uncertain situation, but I think you refer to the rule of law, Babak, that's exactly what we're seeing unraveling right now. So, I mentioned the rapid erosion, not to say collapse of US institutions. And frankly when we have seen that kind of phenomenon elsewhere at different points in history and sometimes it was before living memory, but we have pretty good records of what happened then, it's not gone well.

So, at this point, I think again, not making a predictive statement, maybe things will be more or less okay, they're not going to be entirely okay. Too much damage has already been done in the last few months, but maybe things will be more or less okay, but it's entirely prudent and appropriate for people who are in charge of systemic financial stability to plan for rapid unraveling and rapid acceleration of the institutional unraveling in the US, and that has financial consequences as it has non-financial consequences. And I think frankly, a range of scenarios, not to be too emotional about it, is very wide. So that's what the rest of the world has to plan for.

What are the venues for that? I would say, everything that centers on Basel are still pretty functional. Again, echoing what Stefan said, it's probably likely to stay functional for the foreseeable future. So, I think that kind of coordination that people have in Basel and around Basel in the different committees, regional bodies, and so on and so forth, I think this is more needed than ever. This is why this framework has been put in place back in the early '30s. It didn't prevent World War II, but it was useful ever since.

Babak Abbaszadeh:

Actually, a very, very potent answer. Thank you so much, Nicolas. This was very useful. And one thought that comes to my mind, it's not a question to you or Stefan, but we're talking about how everything is holding, great, but we are beginning to see some tremors, for example, the discussion about climate and climate risk. We're not really hearing about it, and I don't want to introduce that, but this morning I was talking to my daughters, they're both university graduates, fairly young and they're saying, "Dad, I'm not hearing any of this in any of this election discussions in Canada or anything globally. And just a few months ago, that was all the rage." So, there is some sort of a retraction is happening in certain areas and I'm just pointing that as one example, but maybe there is certain degree of self-control that's going on and maybe that's just par for course.

Elsie, let me come to you. And I'm wondering if within a span of four minutes, you can help us get a hold of this question so that we can go to the participants' questions I'm basically taking a lead from your earlier answer. With declining in international aid and a shift in global development priorities, there's a risk of undermining financial inclusion initiatives and throwing more people back into poverty. What are the most critical policy interventions needed to ensure the resilience of financial sector development amidst these adversities? Thank you.

Elsie Addo Awadzi:

Thank you, Babak. I mean, I think that I'll pivot from your last point about climate. I think that there's really the danger that, with these shocks that are evolving and the uncertainties that go with it and then what countries must do in response or in preparation, there's a tendency to lose focus on some of the other underlying risks: exclusion for emerging markets, developing economies, climate, technology-based risks, and cybersecurity risks, all of those things. AML, CFT, some of these countries have assessments, FATF assessments coming up, and pulled on another list means that they're out of the international banking system for a few years and et cetera.

So, it's absolutely important just to start with that supervisors keep their eyes on all of these other important areas of risk and it's not time to backtrack on all of those efforts that have been made. On your specific question on exclusion, yes, if people are out of a job or if people's businesses are failing, they probably cannot keep their banking relationships going and they cannot access loans or insurance products and all of the other key financial services they need to help them get out of crisis. So, they're plunged into crisis almost overnight, and it may be that they don't have any help at all.

With these shocks that are evolving and the uncertainties that go with it and then what countries must do in response or in preparation, there's a tendency to lose focus on some of the other underlying risks: exclusion for emerging markets, developing economies, climate, technology-based risks, and cybersecurity risks, all of those things.

Elsie Addo Awadzi

Toronto Centre

This always comes back to the banking system because it results in loans that are not paid, and it results in banking services that are interrupted or truncated. And so, what should be done, a lot of this has to be done by government more than the supervisory authority. So, the underlying policies that have to take into account what's going on and see what social safety nets can be deployed to mitigate these risks on the ordinary person, and it may be that there are cash transfers, there are other programs that are in place, but of course carefully designed and targeted and implemented.

For the supervisor, I think one of the key areas to keep their eyes on would be the consumer protection side of things, the market conduct side of things. How are people being treated? I mean, in the pandemic, we saw how supervisory authorities all came to provide clear guidance to banks to say, "here is how you should consider providing moratoria," for example, for those whose inability to continue to pay loans has arisen only as a result of the pandemic. But there was clear guidance as to how debt restructuring or loan restructuring by banks would be treated from a prudential standpoint, from an accounting standpoint. So, that gave banks some room and some confidence to have a human face in how they dealt with their customers. So, that's going to be important.

Basically, the idea is to try not to push as many people out of the banking system as possible and regulators must continue to figure out how the regulations are impacting the excluded already or even those who are included and risking exclusion at every moment in time. A lot of work has gone on FinTech-driven financial innovation and stuff like that, all of which operate within carefully crafted regulatory and supervisory frameworks like supervisory sandboxes and et cetera. I really would hope that supervisors keep these in place because it's to nobody's interest if we get people excluded out of the financial system. These economies will not have the resilience they need to be able to bounce back from the impacts of these shocks. Thank you.

> To be on the safe side is very, very helpful to think hard about "what if?" scenarios. How do I manage a situation, for example, where I'm losing one leg of my hedge, and what do I do when that happens? And where do I go to then and where do I get the money?
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> **Stefan Ingves**
> Toronto Centre

Babak Abbaszadeh:

Well, thank you. That's great. And once again, thanks so much for the granularity of your responses. So, Stefan, Elsie, and Nicolas, I'm going to ask you to please help me. We're going to shift to the CNN mode, so I'm going to ask you really complex questions and ask you to break it down in 30 seconds. We have a lot of questions. So, if this is not an opportunity for a dissertation, this is about really getting as many questions as possible and I see a number of questions from a lot of people. I'm going to ignore for now the courageous anonymous questions. Let's go with the people I've actually put their names down and I'll cherry-pick the order here, but I'm going to get to as many of them as I can.

Our good friend Udaibir Das asks, "Trade shocks have repeatedly triggered financial crises from Latin America to Asia to the Eurozone. With today's emerging market banking systems carrying high effects exposures and tidying trade finance, are advanced economy supervisors too complacent? What tools can they actually use now to prevent spillover from trading balances turning into global financial stress?" Nice and provocative. Stefan, can I ask you to please take this on?

Stefan Ingves:

I mean, Udaibir's reflection is relevant in the sense that, I think that if you look at what has happened many times in the past expressing this in very general terms is that markets function the worst when you need them the most. And that means that you have a position, whatever it is, let's say in some currency, and then you take for granted that you can always trade out of your position or close your position. But when things go wrong, that is not always the case. And then you get stuck, and then you run into all sorts of difficulties.

So, to be on the safe side is very, very helpful to think hard about "what if?" scenarios. How do I manage a situation, for example, where I'm losing one leg of my hedge, and what do I do when

that happens? And where do I go to then and where do I get the money? I mean, the traditional way of doing this is to have the major central banks in the world to step in and provide that liquidity. But whether it will happen this time or not, time will tell. But that's what one has to be mindful of and never assume that everything will be just fine and never assume that I can head for the exit faster and sooner than all the other ones because usually, it's pretty hard to get through the door because everybody wants to get through the same door at the same time.

Babak Abbaszadeh:

Stefan, thank you. That's great. So, a question from another friend of ours, George Brady, I think Nicolas, I'm going to give this to you. The question is Stefan's point about implementation fatigue is playing out in jurisdictions emphasizing local regional interests. Stefan, you're becoming famous with that phrase. Example, US, EU, UK. Looking for greater competitiveness and smarter regulation as the emphasis on good risk management and capital adequacy produced adequate expertise within supervisory authorities and regulated entities? Thank you.

> My baseline expectation remains that there will be a kind of minimalistic adoption of the Basel III endgame just for G-SIBs in the US, but that's certainly being delayed.

Nicolas Véron

Peterson Institute for International Economics; Bruegel

Nicolas Véron:

So, I would be nuanced about this. It is true that the US has delayed Basel III adoption. It has not abandoned Basel III adoption for G-SIBs, as we speak. Actually, my baseline expectation remains that there will be a kind of minimalistic adoption of the Basel III endgame just for G-SIBs in the US, but that's certainly being delayed. And, somewhat shamefully in my view, the UK has decided to delay its own implementation without providing a very compelling narrative for that.

But that's not been the case for the EU. The EU is late on Basel III implementation but has now set its timetable except for the fundamental review of the trading book. And again, the EU, to its shame, is not compliant with Basel III, but I think what they have implemented remains the bulk of the accord. So, the picture is nuanced. It is true that in the EU there is a lot of discussion about relaxing the requirements to avoid a competitive disadvantage to the US and especially to large US investment banks. But if we end up in a situation where large US investment banks are actually compliant with Basel III, that argument which is put forward by bank lobbyists in the EU kind of collapses. So then, it becomes a question of coordination of timetable.

In that sense, I think what the EU has done, which is adopting Basel III, albeit with shameful variations and delaying the FRTB, actually makes sense, and I would be curious about Stefan's view of that because indeed, the FRTB is the piece where the competitive dynamics can be most disruptive if there is a variation in adoption between players from different places.

But the bottom line is that, at this point, I wouldn't say that there has been a cycle of deregulation or relaxing of capital requirements in the EU. There's a lot of talk about it, but there hasn't been action. The EU has, the commission has said they would deliver a big report on banks and competitiveness in the course of 2026. So, that's kicked into what by the current standards counts as a long grasp, and I think at this point we're seeing dramatic realization at all levels of the financial risk coming from the US. Just a couple of days ago, Friedrich Merz, who is going to be the next German Chancellor, said there is a risk of financial crisis coming from the US. This is very different from what we were hearing before and I think it's only the beginning.

Babak Abbaszadeh:

Well, thank you. That's great. And I think maybe this can capture, Stefan, maybe you agree with me the essence of the conversation here, which, hey guys, calm down, we're not in a financial crisis, but at the same time, let's keep planning. Let's keep planning, keep our tools sharp. And that's really what the essence of this is. Elsie, I'm going to pitch this question to you.

Flavio is asking, and you've worked in some of the multilateral institutions, "What do you think are the main threats facing multilateral organizations like the World Bank or IMF right now, and how do you think US policy might impact them?" So, take it from wherever you want. It's a good question.

Elsie Addo Awadzi:

I wish I had gone to Nicolas. He's in Washington DC after all, but hey, I think it's anyone's guess. Everyone is nervous. Everyone is anxious and I think that's as much as we know because the US also happens to have the largest quota in these multilateral organizations. And we've seen that it's pulled out of certain multilateral organizations and it's threatening to review its presence or its participation in others. And so, no one really knows. I don't think anyone feels that the US is about to pull out of the IMF and the World Bank. But, I think there are questions as to how the US would use their vote at these institutions and are they going to use their votes to align with the measures that we've seen the executive roll out or when it comes, I mean these institutions are going to be hopefully fighting for the whole world to draw attention to the impact of these measures to other regions and et cetera.

But are the US reps going to be able to speak along those lines? And so, I think there are questions. Now, we all expect these institutions to continue to function properly within their terms of reference, and the whole world is hoping that they step up and do the work that the world expects them to do. How well will that be done? It's anybody's guess. So, I think that's part of the uncertainty, and we'll see how it goes.

Babak Abbaszadeh:

Thank you. And Stefan, I'm going to go to you with this question and you can agree, disagree with the premise of it, but it's an interesting question. Javier asks, "What are your views on risks coming from dysfunctionality in the US bond markets and proposals to reduce leverage ratios to allow dealers to absorb more treasuries?"

Stefan Ingves:

I'm always against lowering the leverage ratio regardless of where this conversation shows up and it shows up again and again and again and again. And basically, the bottom line is that when you're trading using OPM, other people's money, or your own money, and you should use enough of your own money because that keeps your alert. And if that is not the case, you end up with a very asymmetrical system where things tend to go wrong sooner or later. But this is a perennial discussion. This just shows up time and time again. And it's a bit to what Nicolas talked about; this thing called the fundamental review of the trading book. In some sense, as far as I recall, there has always been a review of the trading book in one way or the other. And it seems to be incredibly difficult to bring it to a conclusion.

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And that's because when it comes to the technicalities of these things, it gets very, very technical and it's just very hard to fully understand what is going on. And eventually, you always have to dissect the whole thing in such a way that you keep an eye on the elaborate ratio. But I'm biased when it comes to this and I have managed to upset bankers and traders many, many times in the past, but that doesn't bother me because I have cleaned up so many messes in different parts of the world. So, you have to make sure that you have enough capital there. But it's always also something about the time perspective. Because of course in the short run, you can always argue that if I lower the leverage ratio, then I can do more things in the short run, but usually that comes back to bite you in the long run.

Babak Abbaszadeh:

Well, thank you. That's good advice. Nicolas, I'm going to give this question to you: "How well do countries plan for uncertainties and bring financial resilience on such unilateral decisions of countries that affect several countries as a result?" So, I guess the way I understand this question is you can deal with your own crisis planning, but some other country does something and all of a sudden, the spillover effect. We live in an interconnected world. But so how would you approach that? Thank you.

Nicolas Véron:

I think this issue of the leverage ratio is a good example. Because in a way, the introduction of the leverage ratio on top of or parallel to the risk-weighted capital ratio is one of the biggest advances ever in the supervisory framework. For a very long time, leverage ratio was something in the US, maybe in some other jurisdictions, but escaped by many jurisdictions including important fees of European Union plus the UK. So, the fact that everybody has adopted a leverage ratio and a rigorous definition of a leverage ratio, thanks to Stefan's leadership at the Basel Committee and others, Udaibir being one of them, has seen enormous progress over the last decade. And I think this shouldn't be reversed.

So, in that sense, what the US authorities are talking about, and this is not an entirely new debate, we saw it during COVID-19, is really very detrimental to global financial stability and global discipline because if the US says we remove US treasuries from the calculation of the leverage ratios and inevitably other jurisdictions will be tempted to do that. So, I think what should happen is that whatever the US does, other jurisdictions should resist the temptation, but that will be hard. We know it.

Now, the US fiscal trajectory has been unsustainable for quite a long time now, this is not new, it's getting worse, but it has been a long time coming. What is new and what really crystallized last week is the prospect of capital controls of financial repression coming to the US. So, the US, basically, are using tools that have been interconnected, a perception associated with emerging markets and developing economies in terms of management of the financial system. And we're not there. I mean, the definition of capital controls is very elastic. So, in a way, the US already does that, but in a mild way. But I think we could see, and this is a whole Stephen Miran paper, the discussion about Mar-a-Lago, et cetera, we could see more drastic implementation of capital controls and financial repression in the US going forward.

I think it's very important for every jurisdiction at this point, irrespective of their direct exposure, but you know, Babak, very well, that it's not just the direct exposure that matters back to the questions that had been asked, it's also the indirect exposure and the turmoil that comes from a change in expectations. Countries really have to revisit financial histories. They have to understand the pros and cons, the trade-offs associated with financial repression and ultimately, the virtues of good capital discipline.

Babak Abbaszadeh:

Thank you very much. Again, excellent answer in such a short period. Elsie, I'm going to come to you again. "As a security regulator, I'm concerned about current volatility international markets." I mean, most of us are. You don't have to be a securities regulator. "Are there any lessons that emerging capital markets can learn and how can we support our markets to reduce any negative impacts?" I guess I put you back to when you were at the Bank of Ghana. I'm sure you dealt with these issues all the time. What perspective do you have that we can benefit from? Thank you.

Elsie Addo Awadzi:

Well, thank you. And also, going way back in time when I was a securities regulator here in Ghana, so I've worn both hats, but I totally agree with him. Even on the international stage, we're concerned about fragmentation of markets. I think Nicolas had talked about, and for emerging markets and developing economies, we see real danger because our markets are very fragile, we have non-resident investors coming in, they sell out very quickly to go look for safer havens and then this really would cause the currency crashes that we have seen in the past. Stefan has seen that in his time working with Asia and et cetera. So, it is a real problem, and our markets are very shallow. They don't provide the depth and the breadth that allow the banking system to manage the risks that they're exposed to. Then, you have the government debt side that also banks get very exposed to, and when these governments are debt distressed, when the state is debt distressed, then it really increases the risk for the banking system.

And so, how do we go forward? I think it's very important for banking supervisors to work very closely with the capital market supervisors and with the finance ministries to really strategize on how to strengthen these markets in Africa, for example, in other emerging markets. In Africa, for example, my view is that we probably should really begin to think of some kind of a cross-border, some kind of a regional market tagging on to some of the more established markets in the region to provide more depth for the other countries because there are too many small stock exchanges and debt markets and really they don't do the work, and frankly, and they get very exposed in times like this. So, I think, but that's a multi-year effort that will take 5 to 10 years of really coming up with strategies as to how emerging markets develop in economies, particularly those in low-income countries are able to get access to markets that work, particularly in times of turbulence and uncertainty like this.

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> **Elsie Addo Awadzi**
> Toronto Centre

Babak Abbaszadeh:

Okay. We have time, Stefan literally, if I can give you, please one minute because I want to close the webinar after that. We have a question from Claudette, and she's been patiently waiting. "Given the current global uncertainties, what scenarios insurance industry could consider for stress testing?" I wonder if throughout your career, you ever across that question. Thank you.

Stefan Ingves:

It really depends on what kind of insurance you're talking about, but if it's life insurance in one way or the other, then it's of course all about your investments. And if it's a lot of cross-currency, cross-border, and then you need to be aware of that, or if it's only domestic. And if it's only domestic, then of course it depends on the size of your bond portfolio and the size of government debt. So, those are the traditional issues that one needs to be mindful of.

Babak Abbaszadeh:

Thank you. It also speaks to the cross-sectorality of the financial system and how we're dealing with it. So, it's my pleasure to bring this webinar to a close. I mean, I love doing these webinars and especially when we have amazing speakers like that. And Nicolas, thank you so much, Stefan and Elsie. We are recording this and we're going to use it in our training programs. I think some of the questions you answered are questions that a lot of people have in mind. And thanks again for your time and have a wonderful day, evening, wherever you are. I think Nicolas and Stefan are close to their, and Elsie, I guess where you are, you guys are close to your glass of wine. I'm still on my second or third coffee at this time. So, thanks again and I hope to see you soon and maybe in Washington. Bye-bye.