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***Panel Discussion: Why do we  
need bank regulation?***

20 August 2001  
Risk 2001 Australia

- ❁ **Many “good” trades don’t happen !**
- ❁ **Many “bad” trades do happen !**
- ❁ **Regulatory, tax, accounting, legal questions more vexing than true risk**
- ❁ **Most important problem today:  
capital for a portfolio of credit risk**

- ❁ **Unfunded commitments**
- ❁ **Guarantees and credit risk hedges**
- ❁ **Risk weights are wrong**
- ❁ **No “credit” for diversification**

## *SO WHY HAVE REGULATORS ?*



**Run on  
a bank  
in the  
US, 1933**

## *SO WHY HAVE REGULATORS ?*

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- ✿ **Protect depositors**

**Why can't depositors take the credit risk of a money market fund?**

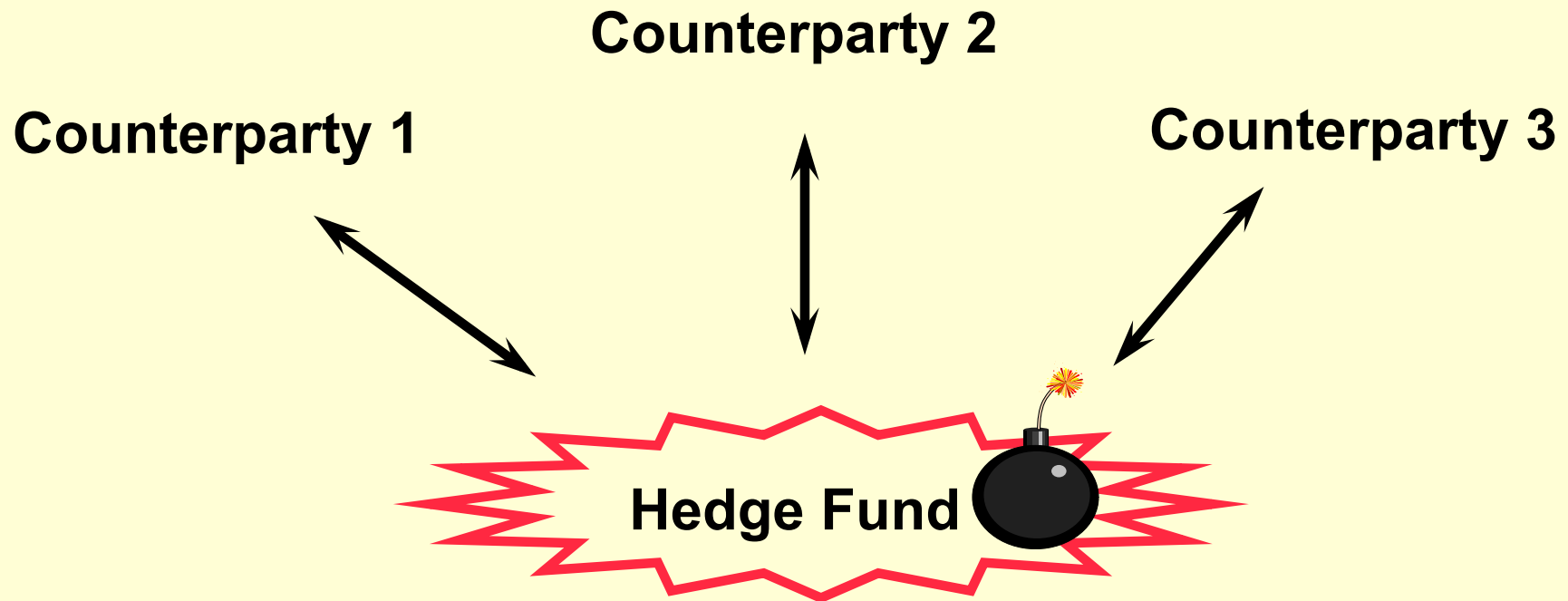
- ✿ **Thwart “systemic risk”**

**What is “systemic risk”?**

**Does it really exist?**

# *SO WHY HAVE REGULATORS ?*

## **Systemic Risk**



**Systemic Risk (?): A hedge fund defaults and thereby causes the default of a counterparty which precipitates default of ANOTHER counterparty, and so on ....**

## ***RATING AGENCY COMPROMISE***

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- ❁ **Replace BIS capital adequacy with “good” agency credit ratings**
- ❁ **Regulators set minimum rating and reserve right to grant exceptions**
- ❁ **Rating agencies assess all relevant risks and do not apply simple formulas that obfuscate true risk**