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?

- **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?
Systemic Risk

SO WHY HAVE REGULATORS?

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