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Hedge Funds and Financial Stability - Speech by Sir John Gieve at the HEDGE 2006 Conference

In a speech given today to the HEDGE 2006 conference, Sir John Gieve – Deputy Governor for Financial Stability – discussed the impact of hedge funds on the financial system and risks to financial stability.

He suggested that the recent explosive growth of hedge funds was a response to technological advance and the innovation and specialisation that allowed. It was also part of a wider shift towards arms length finance. He concluded: “In the long term that shift should be good for stability”. Adding detail, he said “The active trading of hedge funds makes markets more liquid and facilitates genuine hedging activity by others – including systemically important banks. Increasingly, hedge funds – led by those managed from London – have become an important part of the risk transfer process”.

However, he argued that there were risks in the short term. “Periods of rapid growth and innovation in financial markets have often led to difficulties and overshooting and we should not assume that this one will be different.” And he noted that “after a short pause in May and June, we have seen the return of aggressive risk taking in many financial markets this autumn”.

He concluded by describing how the authorities were working with the industry to address and mitigate the risks.

<http://www.bankofengland.co.uk/archive/Documents/historicpubs/speeches/2006/speech285.pdf>