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New Markets and New Demands: Challenges for Central Banks in the Wholesale Market Infrastructure - Speech by Nigel Jenkinson

In a keynote speech today at the joint Bank of England/European Central Bank conference on 'Payments and monetary and financial stability', Nigel Jenkinson - Executive Director of the Bank of England - discusses some of the structural changes in the trading, clearing and settlement infrastructure supporting financial markets and considers associated challenges for central banks and financial regulators.

Pointing out that a central bank's typical objectives of monetary and financial stability emerged from an early role in settling claims between banks, he observes that over time the financial infrastructure has broadened and deepened, stretching beyond the traditional locus of central bank influence. And it continues to evolve, with ever faster technological and financial innovation, regulatory change and the globalisation of banking reshaping the infrastructural landscape, exposing new sources of risk and posing fresh policy challenges.

Nigel Jenkinson stresses the importance of retaining influence in this sphere, citing the example of the recent market turbulence. Volumes and values hit new records in several markets and "any interruption to normal service" within the supporting infrastructure "could have had particularly serious implications: further clouding judgements as to individual participants' solvency; undermining agents' risk management; or affecting asset prices in dependent markets." In the event, the infrastructure passed this stress-test "with flying colours", but the risks were clear. Among the key trends and developments in the financial infrastructure, Nigel Jenkinson observes that banks seek infrastructural solutions to match the international scope of their business, remarking that "while, historically, financial infrastructure has typically evolved along national lines, cross-border alliances and mergers are now more common". He also acknowledges the fresh wave of competition, particularly in trading and clearing, but suspects that what we are seeing is a process which will "lead in time to greater consolidation at international level but is currently manifesting itself in terms of fragmentation at the national level" as local incumbents are challenged.

Whatever the ultimate end-game, Nigel Jenkinson identifies several immediate issues for policymakers. In an increasingly international and interdependent market place, a public policy challenge lies in allowing market participants to reap the benefits of globalisation, while ensuring that the risks are adequately controlled. He

observes that central banks will have to work "more closely together in risk assessment and oversight and ensure that cross-border operational arrangements are robust."

And with new players emerging on the scene, including commercial bank providers of infrastructure, he notes the value in consistent and objective criteria for the scope of oversight of infrastructure. He highlights the importance of maintaining a level regulatory playing-field and promotes a "risk-based functional" approach to regulation.

<http://www.bankofengland.co.uk/archive/Documents/historicpubs/speeches/2007/speech328.pdf>