BANK OF ENGLAND

Press Office
Threadneedle Street
London EC2R 8AH
T 020 7601 4411
F 020 7601 5460
press@bankofengland.co.uk
www.bankofengland.co.uk

News release

21 September 2010

Remarks by Andrew Bailey on Financial Reform

Andrew Bailey, Executive Director for Banking Services and Chief Cashier for the Bank of England, speaking at Mansion House on financial reform, looks at the challenges of re-building financial stability.

Andrew Bailey, designated Deputy CEO of the new Prudential Regulation Authority (PRA), emphasises that "It is a task that belongs to all of us...history now tells us - painfully - that on the way to higher standards there was a terrible lapse in which too many people in our industry forgot that preserving financial stability is the duty that we all owe to the public. The fact of the matter is that the public has every right to expect us to act in their interest."

He points out that we can only ensure the lessons of the crisis stick if financial stability is well understood. Andrew Bailey explores what the public should want as part of the overall stability of the financial system:

- that they can have confidence in the safety and soundness of the institutions that hold their money and savings and write policies to protect them against risks;
- that institutions have the capacity to undertake the stable and sound provision of financial services to the economy, including of course lending;
- that the system does not do business and exist on the basis of an implicit commitment that the State will have to use public money, the public's money, to bail out firms that get into trouble; and
- that the public can place trust in firms and markets based on their reputations and the transparency of their dealings.

Highlighting the consequences of the public interest, Andrew Bailey points out that financial stability is not about preventing all financial firms from failing. He says, "We will not truly have solved the too big or important to fail problem and thus the public money problem until we have tools at our disposal which enable us to resolve large institutions if they get into trouble. This will create the right incentives for risk management." Also, "...regulators must use their judgement to mount a robust challenge to stop dangerous business models and investment practices." On Basel III he says "...if the capital buffers are in future genuinely loss bearing capital with no tricky wrinkles, and we keep to this outcome, we have taken a good step forward."

Commenting on the proposed new institutional and regulatory framework, Andrew Bailey goes on to look at what a judgement-focused approach by regulators means including both a micro and macro prudential view, stress testing and the use of recovery and resolution planning. He raises the prospect of "...a proactive intervention framework akin to the US Prompt Corrective Action within its supervisory approach to deal with the inevitable situations where firms get into the danger zone." He concludes that "Above all, these tools should support competition in the industry, by accepting that there will be winners and losers."

Andrew Bailey ends his speech with "There is a great deal to be done to implement the new system of regulation, to articulate and build the public interest in financial stability, and thereby to improve the stability of the system itself. Basel III, macroprudential tools, countercyclical buffers, ...are important foundations of good policy. But on their own they don't win the public interest argument for financial stability. To do that, we have to build the case that the industry will serve the needs and interest of the public. The authorities cannot do this alone. Building confidence in the financial system takes effort and time. It is a common goal and in the interest of everyone."

Key Resources

Full speech
http://www.bankofengland.co.uk/archive/Documents/historicpubs/speeches/2010/speech447.pdf