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Opening Remarks
IMF-FSC/FSS Macroprudential Supervision Conference: Challenges for Financial Supervisors

November 7-8, 2006, Seoul, Korea

Distinguished Guests, and Ladies and Gentlemen,

On behalf of Financial Supervisory Commission and Financial Supervisory Service, I would like to welcome all of you to the Macroprudential Supervision Conference. We are very pleased to host this conference with the IMF, and we thank you for joining us today.

We have a long list of distinguished speakers, scholars, business leaders, and guests who will be with us today and tomorrow. I would like to thank all of them for taking part in the conference. But since it may take a while, let me quickly thank Tomas Balino, Deputy Director, IMF, for all the support we received in organizing the conference.

I would also like to thank Callum McCarthy, Chairman of U.K. Financial Services Authority, John Laker, Chairman of Australian Prudential Regulation Authority, William Ryback, Deputy Chief Executive, Hong Kong Monetary Authority, and Park Yung Chul, Research Professor and Director of International Studies at Seoul National University, for chairing the four sessions we have for you.

The idea of holding a conference on macroprudential supervision came to us late last year when we had consultations on macroprudential supervision with the IMF. The technical assistance we received from the IMF proved instrumental in setting new directions and fine-tuning our approach to macroprudential supervision.

So it is my hope that this conference will provide a useful forum for discussions on macroprudential supervision so that it may further contribute to building a consensus on how macroprudential supervision should be understood and practiced.

As we all know, financial instability undermines financial intermediation and interferes with the credit creation process. It also distorts our economic decisions and thus resource allocation. In short, the cost we pay for financial instability can be enormous. According to a study by the IMF of 12 countries that experienced financial crisis in the past 15 years, the direct cost of a financial crisis exceeded 10% of the GDP. The indirect cost was found to be even greater.

It has been observed that financial instability often originates from within a financial system rather than from outside macroeconomic shocks. In fact, we find that financial instability often results from the herd behavior of financial institutions or under-estimation of sizable underlying risks in the financial system.

Most of the risk estimation tools we have today are designed to measure risk at the individual level, for example, the price of an asset or an investment contract. But when it comes to dealing with risks that are intrinsic to the financial system or the economy, the usefulness of these “micro” risk estimation tools are often limited.

It is also important to note that risks to financial stability can be compounded by the dynamic interactions between the financial and the real sectors. The same may be said for failure to respond promptly to the ever-changing risk levels of the economy.

We also know that risks that seem well controlled in an economic upswing can easily turn into a real threat in a recession. The credit card crisis Korea faced in 2003 represented a failure of macroprudential supervision by Korea’s financial supervisors and policymakers.

At the time, credit card consumption was encouraged with what can be fairly described as legitimate and desirable policy objectives. What was NOT anticipated, however, was the reckless behavior of credit card companies giving credit to almost anyone who asked for it. The risks that this posed on the financial system were also not fully appreciated or dealt with in a timely fashion by the policymakers.

So what is clear to us is that we need macroprudential mindset and perspectives on financial institutions and financial markets in order to effectively prevent systemic disturbances or instability.

The reason is that financial markets can be exposed to systemic risks even with a high level of soundness of individual financial institutions that can be achieved with “microprudential” supervision. Indeed, the “fallacy of composition” tells us that actions that may seem perfectly rational from the standpoint of an individual financial institution could, in aggregate, leave everyone worse off. Risks to the financial system can also be particularly acute when the market is too small or too under-developed to absorb a shock from outside.

We recognized this and established Macroprudential Supervision Department in 2005 to keep an eye on the financial system and preempt systemic risks to our markets. It has been a valuable addition to our supervisory framework. And we hope to improve upon what we hear from this conference.

Let me add that, as we move forward with market deregulation, we will continue to fine-tune our approach to macroprudential supervision to make sure that our market stays safe and sound.

As markets converge, I believe that macroprudential supervision must be understood as a collaborative and collective endeavor by all of us.

The global financial system has proven robust and resilient even in times of severe disturbances and imbalances in the global economic environment. But the risks we face are becoming more complex and more troublesome to control than ever before. This is not likely to change any time soon.

So the need for continued dialogue among financial supervisors under cooperative framework and in collaboration with the IMF and other key international institutions is obvious. Indeed, this conference is intended to facilitate and contribute to that very dialogue we need to have for our common interests.

Again, I would like to welcome everyone to our conference. We are delighted to have you join us today. I thank the IMF for hosting this meeting with us and speakers from abroad for their generous time and contribution.

Thank you.