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OPENING REMARKS

at the

"Basel II Workshop for Bank Supervisors"

hosted by

The Central Bank of Trinidad and Tobago and CARTAC

by

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Ladies and Gentlemen, I am pleased that the Central Bank is hosting this workshop. I would like to welcome you all - the international presenters, our regional colleagues, other invited guests and members of staff.

Let me also take the opportunity to congratulate CARTAC for organizing this Workshop and more generally for the very useful work it is doing in the region. It is exactly the type of intervention that was envisaged.

I am also happy to have another chance to better understand this Basel II. While I recognize the importance of the topic, I must confess that most discussions of Basel II are made to sound like rocket science. I sometimes feel that it is a convenient way for Bank regulators and other risk management experts to look down on lesser mortals like me.

If I understand the story well, modern asset-pricing theory had its early development in academia, but its growth and application have been taken over by bankers and investors who were looking for new ways of quantifying and measuring risks. Moreover, while large banks began to develop these complicated quantitative models for their own purposes, bank regulators saw the opportunity of using these advanced risk-management techniques as a new capital standard.

One of the Vice Chairmen of the U.S. Federal Reserve Bank affirmed that Basel II was designed to harness the best new techniques, but also to ensure their application by those large banks that were less aggressive in adopting them.

So Basel II was initially meant for large banks; it was not meant for us "small fry" in the Caribbean. But the world being what it is, we can't avoid it.

Developing countries worldwide recognize that even though Basel II is intended for implementation by internationally active banks, **the non-adoption of this or a similarly rigid standard by developing countries** would put these countries at a disadvantage. Developing countries, including us in the Caribbean, are justified in being concerned that **international creditors and lending agencies will tend to assess the**

strength of our financial systems by established global standards and practices.

And therefore we in the region need to seriously examine the provisions of Basel II and to see how it could be modified to be suit our Caribbean environment.

I understand that the Technical Working Group of the Caribbean Group of Bank Supervisors, which has the mandate to consider the implementation of the New Accord from a regional perspective, has not been working assiduously on the issue. While there may be good reasons for this, our regulators need to get together so that we are not left behind.

Mr. Chairman, I don't want to feign in-depth knowledge and start name-dropping about **Pillars I, II and III** and the **Internal Ratings Based Approach** and the **Standardised Approach** and the **Advanced Measurement Approach** for operational risks. I am not sure I fully understand these things. **What I know is that for us in the Caribbean to implement the least ambitious of these initiatives, we need to lift our current level of supervisory oversight.**

Specifically, even as we prepare for Basel II, we need to achieve full compliance with the Basel Core Principles (BCPs) and to the 1996 Amendment having to do with market risks. Recent FSAPs conducted in this region revealed that there was not full compliance with these core principles or with the 1996 amendment.

A recent World Bank-sponsored study indicated that only about 7% of developing countries (which includes the Caribbean) were in full compliance with the Board Core Principles. The study noted that the lack of compliance was of particular concern in the following areas: (i) effective consolidated supervision; (ii) supervisory independence, resources, and authority; and (iii) the ability to impose effective, prompt corrective action. **If supervisors lack resources and the basics of effective banking supervision, correcting this should be the first priority, and more complex rules on capital requirements may well be counterproductive**.

In recent years, financial conglomerates have emerged in several of our countries and some are expanding across the region at a fast rate. These developments bring to the fore the need for consolidated supervision and raise issues such as home-host supervision, capital adequacy and the effectiveness of risk management processes of conglomerates. Basel II assumes the presence of consolidated supervision, but many of our jurisdictions do not comply with the more modest versions of this. The introduction of legislation to deal with financial holding companies - with complex groups, the sharing of information and cross border supervision - is therefore an urgent requirement in the region.

The Central Bank of Trinidad and Tobago is currently in the process of amending the legislation for both the banking and insurance sectors to include the areas mentioned above. I believe that several other jurisdictions are also updating their legislation and I am aware that efforts are being made to harmonise financial legislation across Caricom jurisdictions in keeping with the concept of the Caricom Single Market and Economy.

These are critical tasks …….

But, don't get me wrong: **we must prepare for Basel II or some variant thereof and in so doing, we must become fully aware of the type of challenges that this new standard will impose**. Sessions like these go a long way in assisting with this objective.

There is a strong view, for instance (that under Pillar I) a less complex regime called the Standardized Approach may be more appropriate for regional banks. However, some still argue that this methodology will not adequately align risk with capital, which is the basis of the Basel 11 Accord. There is also concern that under the standardized approach, **domestic banks may require higher capital than the international banks** which will be using the more advanced approach. If this is so, it will put our domestic banks at a competitive disadvantage.

In addition, in a financial system where the domestic banks will be using the **Standardized Approach** and the international banks a more **Advanced Approach**, supervising both structures will provide particular challenges for regulatory authorities. **It is evident that solutions are needed to these and a myriad of other questions and I am pleased to see that several of the issues will be discussed during this workshop**.

We know for sure that in order to prepare for Basel II, all the regional regulatory agencies will need to make significant investments in the retooling and retraining of staff. It will also be necessary for several banks to upgrade information technology platforms.

I am very pleased that representatives from our banking sector are participating in this workshop, since this will give them the opportunity to get a feel for what is required of them for the implementation of the new Accord. The interest shown by our domestic banks in the Basel II

Accord, tells me that they recognise that they are operating in a global environment and that international best practice is essential for their survival.

Caribbean jurisdictions also need to begin to depend more on market discipline and to intensify efforts to encourage more disclosure and transparency by banks. We need to realise that disclosure and greater transparency are essential to create more efficient markets and to reduce the potential for moral hazard, by allowing enhanced monitoring by the public. What this means is that regional regulators can no longer be satisfied with annual audited financial statements and the periodic publication of macro prudential indicators. We also need to ensure the adoption of international accounting standards, which entail more onerous reporting requirements but provide greater disclosure.

Against this background, I am convinced that this workshop is critically important and very opportune. I have observed from the Agenda that there will be many panel discussions where participants will be sharing their experiences. The structure of the programme also provides for participation by private bankers and regional regulators in many of the panel discussions. This should facilitate different perspectives on the feasibility of Basel II or some alternative for the region.

I did not see it on the Agenda but I hope there would also be time to discuss the use of Quantitative Impact (Survey) methodologies. It is important that all jurisdictions conduct these analyses to get some idea of the likely impact on capital requirements, implied by the new Accord.

In this regard, the region also looks forward to CARTAC's continued support for in-depth training in this area.

Clearly there is much work to be done as we first need to play catch-up, and then prepare ourselves for a new and more challenging standard. But I believe that we are up to the task. I am certain that your sessions over the next few days will be stimulating and I hope that by the end of this workshop, there will be greater clarity on the way forward for your respective jurisdictions, as well as for the region as a whole.

Welcome again to our beautiful country and have an enjoyable stay.

Thank you.