De-risking Strategies of Canadian and American Banks Discussed at the Montreal Meeting of the Regional Consultative Group for the Americas

At a meeting of the Regional Consultative Group for the Americas (RCG_A) in Montreal on May 27, Central Bank Governor Dr. DeLisle Worrell moderated a panel where bank regulators, representatives of the IMF, World Bank, CARICOM and other institutions, representatives of the US Treasury and the Federal Reserve Board and commercial banks, engaged in an informative and constructive dialogue on the strategies that banks have taken in response to global initiatives designed to reduce the riskiness of international finance.

In his introductory remarks, Governor Worrell spoke of the magnitude and pervasiveness of the problem of de-risking in the Americas, noting that "Although the RCG_A began its current investigation in response to issues of *correspondent banking*, the phenomenon we have uncovered goes far beyond that, and it is now evident that *de-risking* (a term used to cover any strategy that is designed to reduce risk exposure) is a more appropriate description of what is being observed in international financial markets. The first task must be to gain a full understanding of the motives, sources and effects of de-risking strategies, which are varied, but pervasive."

Worrell added that de-risking should be seen as a manifestation of complex and uncoordinated regulatory reform at national and international levels, which is changing the global financial landscape in profound and unpredictable ways. He invited participants to share their stories about their efforts to cope with the several changes that have impacted the global financial market since 2008 and suggested the focus of the meeting should be to document, analyse and deepen our perception of what is happening, and why it is happening.

The international regulatory drivers Worrell identified include:

- The complexity and inconsistency of the international regulatory framework, comprising:
    - higher capital costs under the Basel framework for bank supervision;
    - much higher compliance costs under the global anti-money laundering framework;
    - higher information costs under the Global Forum arrangements for the exchange of tax information;
    - much higher and additional information costs under the US FATCA requirements;
    - the potential for additional costs under the Common Reporting Standard and other guidelines still in the process of development; and
    - the information and compliance costs of sanctions regimes of the US and other countries.

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- The uncertainty that arises because national authorities are not obliged to follow international guidance, leading to instances where countries individually or collectively ignore the institutionalised international certification process (as in the case of the arbitrary EU blacklisting of some small international financial centres in 2015).
- The fact that the cost of failure for banks is very high, in terms of fines and penalties imposed by regulators and the law courts, in terms of the reputation of the bank concerned, and in terms of the fall in the bank's share price as a result.
- The fact that the marginal costs of doing some kinds of international banking business are now very much higher than the marginal returns.

The effects in the Caribbean have been:

- The reduction of efficiency and the increase of risks to international financial markets by diverting business from competitive, highly regarded small international financial centres (such as Barbados) to mainland jurisdictions which are less competitive and in some instances, do not maintain international standards to levels comparable to those practiced in Barbados;
- The diversion of remittance business from regulated money service business to unregulated informal markets;
- The withdrawal of correspondent banking services from indigenous banks and other financial institutions;
- A pull-back by international banks from small Caribbean markets where they have been conducting business for almost a century, in some cases.

In the discussion, banks shared experiences and spoke about the factors that have motivated de-risking strategies, and the unintended consequences of the actions that have been taken and are being taken. This is a still evolving, truly global phenomenon, which is still being played out. The Montreal meeting was an opportunity to share experiences and deepen understanding of what motivates the actions of all players. In deciding on the best way forward, the common objective is to maintain a level playing field internationally, to avoid distortions in international financial markets, and to encourage international competition and efficiency.

The Regional Consultative Group for the Americas is one of six such bodies established under the charter of the Financial Stability Board (FSB), the institution which coordinates work around the globe to promote international financial stability. Dr. Worrell shares the chair of the Americas group with Carolyn Wilkins, Senior Deputy Governor at the Bank of Canada, for the period 2015-2017. The Financial Stability Board is chaired by Dr. Mark Carney, Governor of the Bank of England. The final Press Release of the Montreal meeting of the RCG_A may be found on the FSB website at www.fsb.org.

2016-05-30