Making the Global Financial System Work for All
= A Truly Resilient System


Erik Berglöf, London School of Economics and Political Science

Financial Resilience and Systemic Risk conference
London School of Economics and Political Science
January 30, 2019
A Truly Resilient Financial System

- Resilience - about surviving and thriving, regardless of the challenge. (Rockefeller Foundation)
- Climate change
- Forced dislocation => political shocks
- Cyber security
- Pandemics => economic and political shocks
- The global financial system critical to addressing these challenges, but is also vulnerable to them
Eminent Persons Group on Global Financial Governance

- Group established by G20 Finance Ministers and Central Bank Governors in April 2017

- **Recommend reforms to global financial architecture and governance of the system of international financial institutions**

- 16 people (8 advanced + 8 emerging economies (Chair: DPM Tharman)

- Final Report presented to the G20 at its meetings in Bali in October 2018 ([www.globalfinancialgovernance.org](http://www.globalfinancialgovernance.org))
Now face different realities, particularly from Bretton Woods:

- **Economic, social and political divides widened**, undermining social contracts and support for international cooperation

- A **steady and irreversible shift towards multipolar world**, more equal players and decentralization in decision-making

- **Challenges of unprecedented scale, urgency and complexity** – securing jobs, and environmental and financial sustainability.

- **More deeply inter-connected** (trade + capital + ideas) challenges stability - cannot be tackled by nations on their own
EPG Approach

- **Build credible and coordinated global financial architecture** for a world that is more decentralized in decision-making, more interconnected and more challenged in the future.
- **Mold this decentralized system into a new multilateralism** that is more resilient and stronger than the sum of its parts.
- **Recognize that** helping countries get their national policies **right** is at the heart of achieving mutual prosperity.
- **Focus work and recommendations in three areas:** Development; Finance; and Governance.
How to get resilient downhill flows?

- **Attract private capital + institutional investors**
- **Developing and emerging economies**
  - Improve governance and human capital – country ownership
  - Develop local financial system
  - Mobilizing local long-term capital (institutional investors)
- **International community**
  - Use international financial institutions more effectively
  - Monitor debt levels to ensure sustainability
  - Improve framework for regulating capital flows + safety net
EPG Recommendations:
Making Capital Flows More Stable

Get full benefits without risks from excessive volatility:

• IFI community should accelerate efforts to help countries develop deep, resilient + inclusive financial markets.

• IMF policy guidance enabling countries to move toward long-run goal of openness and better manage risks.
  o Benefit from capital flows while maintaining financial stability + assure markets measures taken appropriate
  o Enable sending countries to meet domestic objectives while avoiding large adverse international spillovers
**EPG Recommendations:**

**Stitching Together Global Safety Net**

- Stitch together the various layers of the GFSN to achieve scale and predictability.

- Establish a standing IMF liquidity facility for timely access to temporary support during global liquidity shock
  - Use pre-qualification in considering the activation of RFA supports

- Enable the IMF to rapidly mobilize additional resources in large and severe global crises
**EPG Recommendations:**

**Strengthen Risk Surveillance**

- Integrate surveillance efforts of IMF, FSB and BIS in a coherent **global risk map**, while preserving independence of each of the institutions’ perspectives (incorporate non-official and contrarian views)

- Build on IMF-FSB Early Warning Exercise (EWE) to ensure policy follow-up from the global risk map
**EPG Recommendations:**

**Governing the System as a System**

**G20 providing strategic guidance in global governance**
- Refocus on strategic agenda, rationalize work streams, and devolve to IFIs

**Governance of system-wide reforms**
- A G20-led group, including key non-G20 constituencies and IFIs, should steer reorientation of development finance over next three years
- Building complementarity among all development partners, and clear system of metrics to track impact and value for money.
- A biennial strategic forum convened by the IMFC and DC should identify development risks before they manifest, and the required collective responses.

**Governance within IFIs**
- Executive Boards to focus on strategic priorities + advance system-wide goals
- Adopt practical, risk-based approach to delegate responsibility to Mgmt
- Increase diversity and skills – match shift in business models + complexity
Today: de facto rating agencies “regulate” IFIs
  - State-owned financial institutions without access to liquidity backstop (all institutions, but for EIB)
  - Half-a-notch downgrade

Create liquidity backstop
  - Collaboration among subset of central banks (IMF?)
  - New form of contingent capital (cf. ESM callable cap.)
  - Would increase WBG lending capacity by 10 percent (more for RDBs)
Global Financial Resilience

- Developing local (currency) financial systems
- Building domestic resource mobilisation
- Enforcing standards of debt sustainability
- Establishing framework for capital controls
- Stitching together the global financial safety net
- Developing regulatory framework for IFIs