Comment

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Tommaso Padoa-Schioppa's presentation was a very clear and well structured one. As he rightly pointed out, there have been really fundamental changes which took place over the last two decades or so in the financial market and also in the players in it, which financial supervisors have to deal with. First of all, in the market there has been the big trend of globalization.

In my view, it was originated, supported and accelerated by several factors. One of these has been the competitive deregulation which all major financial markets have been pursuing. Another factor has been the tremendous progress made in the information technologies. Also, we should recall the global glut of financial resources which are looking for higher returns; this made the process of globalization all the more substantive and rapid.

As a result of globalization, there is an enormous amount of cross-border financial transaction. Also, as we have seen in Asian markets recently and as many of you are very much aware of, there is certainly a serious concern about a so-called contagion phenomenon and the work of a very large and volatile flow of short-term money.

Well, on the player side there is a strong trend towards a universal type of financial institutions which cross over the traditional boundaries of different financial services. Also, there is another strong trend on their part to expand operation globally, seeking the best business opportunities and higher returns; these financial institutions are producing ever-increasing varieties of commodities and services, and they are quite willing to take risks of all kinds.

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BNL Quarterly Review, Special Issue, March 1998.

Perhaps Padoa-Schioppa could have put a greater emphasis on the fact that the very nature of the financial services industry has changed tremendously: as we are very much aware of today the financial services industry is a computer industry, an electronics industry and an information industry. As a result, the financial services activities have become highly technological and have lost much of their traditional human character.

I think that this transformation of the financial services industry has a serious implication for the financial supervision, because it changes the type of instruments which can be employed in carrying out the supervision and it also changes the type of necessary resources that supervisors have to possess.

While the environment of the financial supervision has changed, as I described briefly, the fundamental objective of the supervision has not changed. The objective of the financial supervision is still the protection of depositors, investors and also to maintain market stability by preventing a systemic risk. By pursuing these objectives, supervision ultimately aims at facilitating national and global economic welfare.

Then, what is the best set up for the financial supervision under the very much changed environment, yet pursuing the same objective?

As Padoa-Schioppa very eloquently spelled out, and I agree, geographically and functionally segmented system of supervision has become very much ineffective. In that sense, I certainly support the three propositions that Padoa-Schioppa has made, about what the financial supervision framework should aim at: first, it has to be market friendly; second, it must be objective oriented; third, it needs to be internationally structured. These three propositions are very perceptive ones.

In an ideal world we should have universal standardized rules, which are implemented by a global institution of supervision. In reality, however, it is very difficult to achieve these goals. There is a great amount of political and economic inertia, which is created by different groups of vested interests with a strong desire of protecting their own turf; there is also the fact that each economy is in a different developmental stage and a different political and legal structure, which

makes the transformation into a universal supervisory structure very difficult.

Of course, there is concern that if we have too much simplified and consolidated supervisory structures, that may result in too much concentration of authority in economic management.

After giving due consideration to these practical difficulties, we can start with three points. The first one is that after all a supervisory reform should start at national supervisory level. We should aim at establishing an internationally compatible and least complicated system for our national financial supervision. In this respect, in Japan we have separated the financial supervisory function from the Ministry of Finance, and set up an independent agency directly reporting to the Prime Minister; it has supervisory functions not only for banking but also for securities and insurance business as well. So I think that Japan is one country that is making an effort in that direction.

The second proposal on my part is that we should establish adequate strict criteria for global players. I think that the national authorities can apply higher hurdles for those who want to be active in global market. In this respect the basic accord for the management of market risks, which was agreed upon at BIS last year and will be implemented next year, can play a very important role, because national authorities have to decide what criteria they are going to establish for their institutions. The Japanese authorities are planning to set up quite a strict threshold for those who will be allowed to be active in the global market in a wide range of financial activities. The Japanese authorities are contemplating to limit the number of those global players to no more than 15 to 20 institutions.

I think this is another effort on our part to achieve the abovementioned goal.

Thirdly, great emphasis should be placed on the self-discipline on the part of the individual institutions, particularly in the area of prudential requirement, disclosure, etc.

In conclusion, there is no question that the world economy is now driven by market forces. The market is always the hero of the show today; that means supervisors will have to be market friendly. But at the same time the situation poses a serious challenge for us. In Asia one of the most popular topics these days is the debate between the Malaysian Prime Minister and George Soros. Certainly speculation is a normal type of market function, nobody can blame that, and speculators usually do not penalize truly innocent countries. But at the same time it is quite obvious that the objective of the speculation is just to make profit, not to support the development of the emerging countries. I still believe that Adam Smith was right when he said that eventually the market will be guided by the invisible hand of God, but the problem is that God is not always on duty. So I think financial supervisors sometimes have to act as agents of God.