



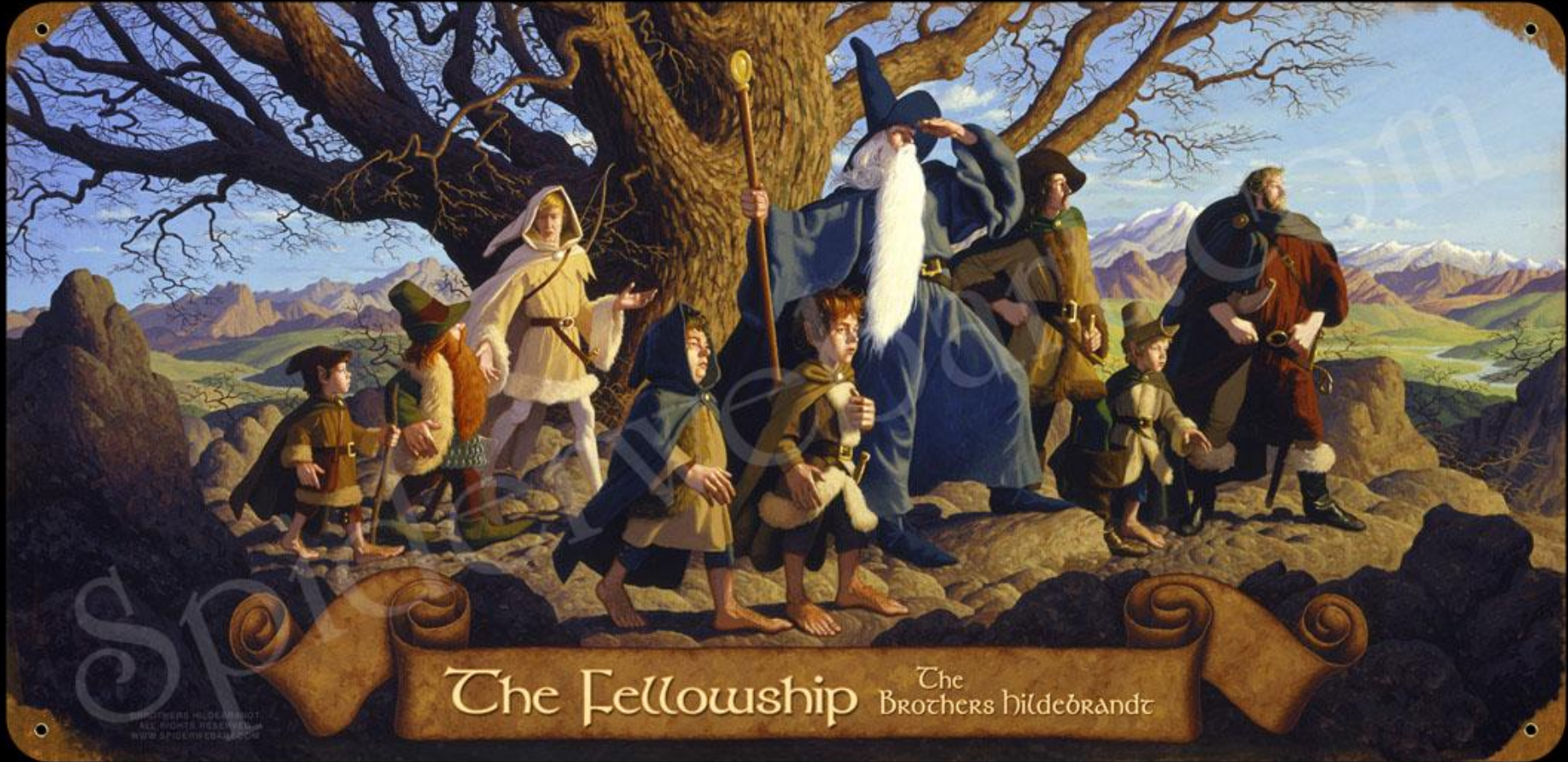
The risk management quest: A Reserve Bank approach

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The risk management quest: A Reserve Bank approach





“It's a dangerous business, Frodo, going out your door. You step onto the road, and if you don't keep your feet, there's no knowing where you might be swept off to.”

JRR Tolkien – Lord of the Rings



Managing system-wide risk: Outline

1. Why we get involved
2. What trade-offs we face
3. The importance of supporting dynamism and innovation through sound risk management
4. How we perform our role

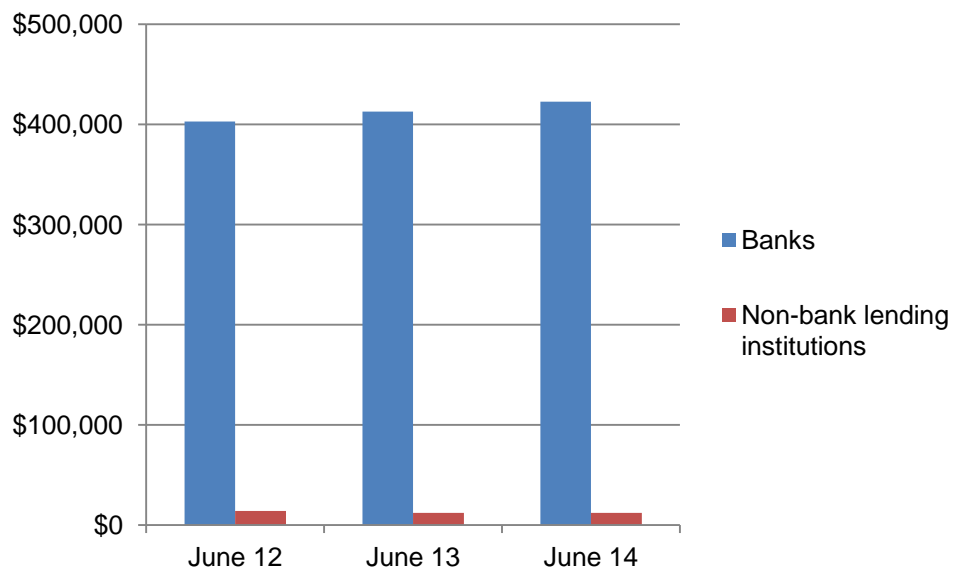


Risks in the NZ financial system

1. BAU risks
2. Tail risks



Total assets: Banks and non-bank lending institutions



Source: <http://www.rbnz.govt.nz/statistics/>



“Happy financial systems are all alike; every unhappy financial system is unhappy in its own way.”

Adapted from Tolstoy



Risks we worry about

1. Natural disasters
2. Asset bubbles
3. Risks from offshore
4. Extreme losses
5. The unknown and unknowable



Soundness and efficiency

1. Cost of a severe financial crisis:
Our estimate - 10 to 20% of GDP
2. Dynamic efficiency



New entrants in NZ financial system

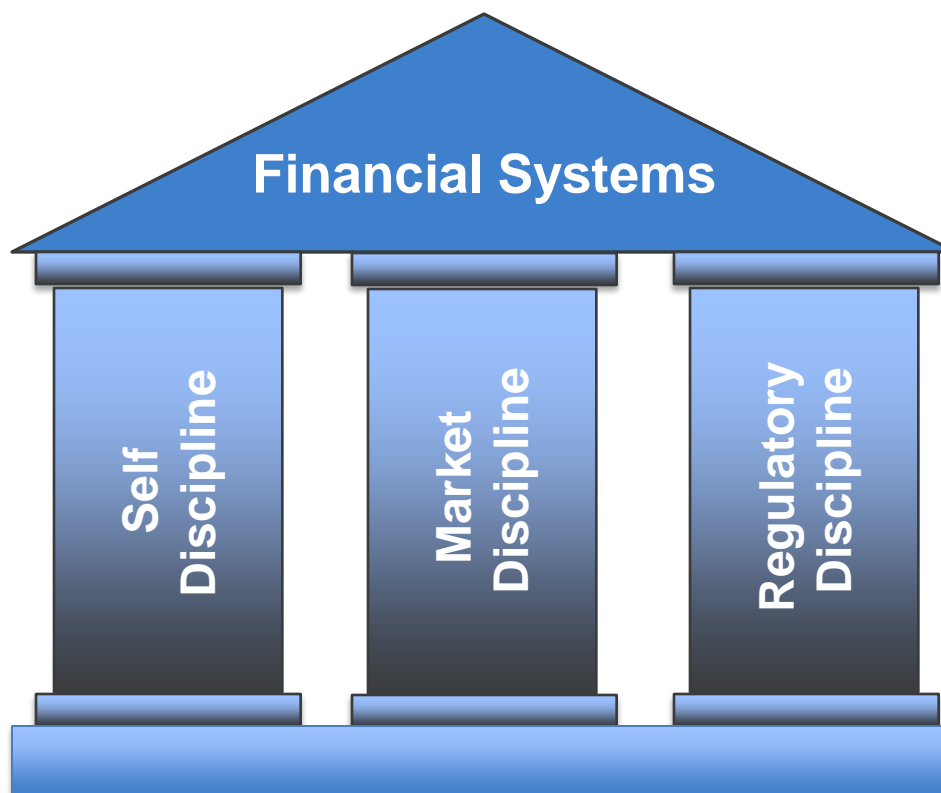
1. Six years: Banks increase from 16 to 24
2. 12 months: Two new insurers

But we also tolerate failure!



Effective system-wide management

Three pillars of supervision





Levels of risk

1. Institution
2. System-wide
3. Time-varying



Working with the market

Align, where sensible and suits New Zealand, with:

1. Basel Committee
2. International Association of Insurance Supervisors

Balance in our regulations



Conclusion

1. Toleration of failure
2. Alert to severe tail risks
3. Stable and well-managed system



“I will take the ring’ he said, ‘though I do not know the way.”

JRR Tolkien – Lord of the Rings