

Financial Stability Institute

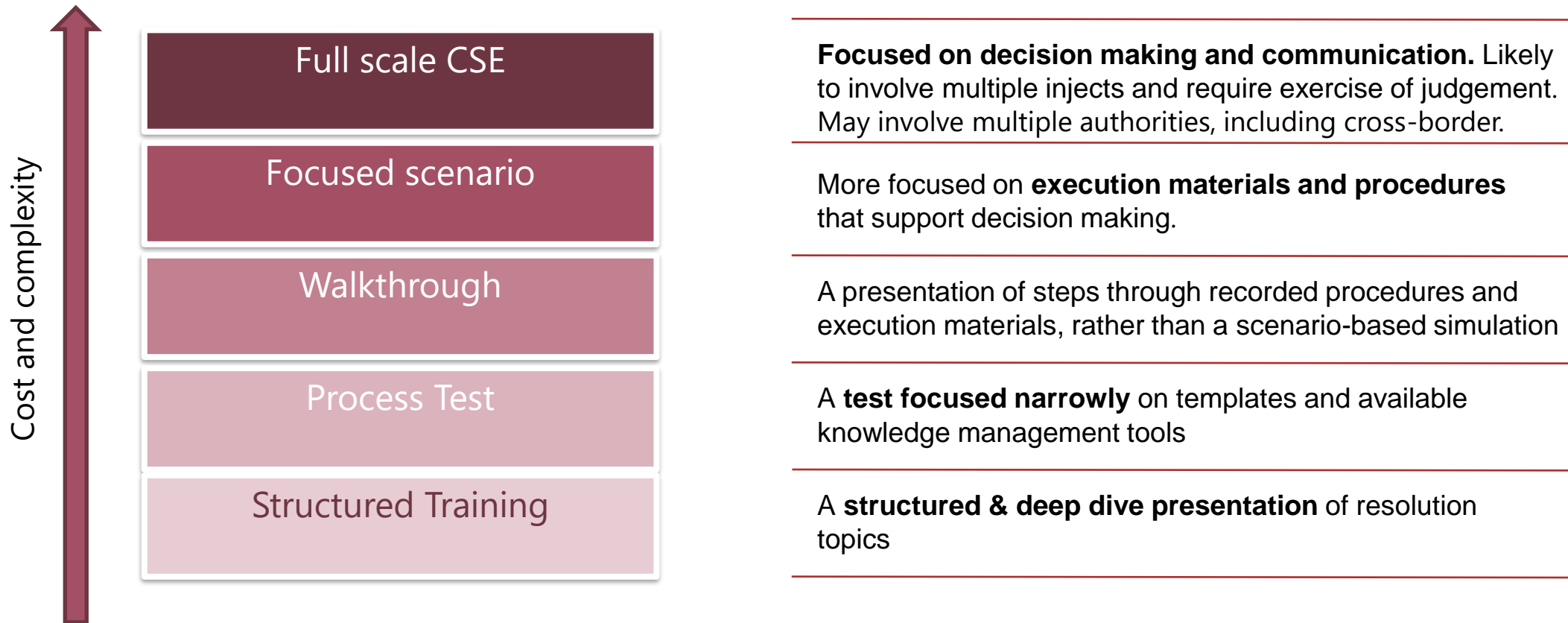


FinSAC Annual International Conference 17-18 May 2022

Session 4 - Hoping for the best, preparing for the worst: bank resolution

Ruth Walters, Financial Stability Institute, BIS

Options for testing



Crisis Simulation Exercises

LATAM - Banco São Francisco

Broad scope: early intervention, triggering and implementing resolution

6 countries
10 authorities
~15 project team members
~40 senior officials
~70 support staff
CSE conducted March 2021

FICTIONAL ENTITY

- Banco São Francisco (BSF) is a large, multinational bank headquartered in Brazil
- Subsidiaries of **systemic relevance** in Chile, Uruguay and Paraguay, a large subsidiary in Colombia, and 49% ownership of systemic bank in Argentina
- Significant exposure to **infrastructure project** in Iguazu
- BSF failure driven by:
 - **Growing NPLs** and poor asset quality
 - **Liquidity issues** accentuated by bank runs

APAC - APB group

Narrower scope focused on design of resolution strategy

6 countries
11 authorities
~30 project team members
Early July 2022

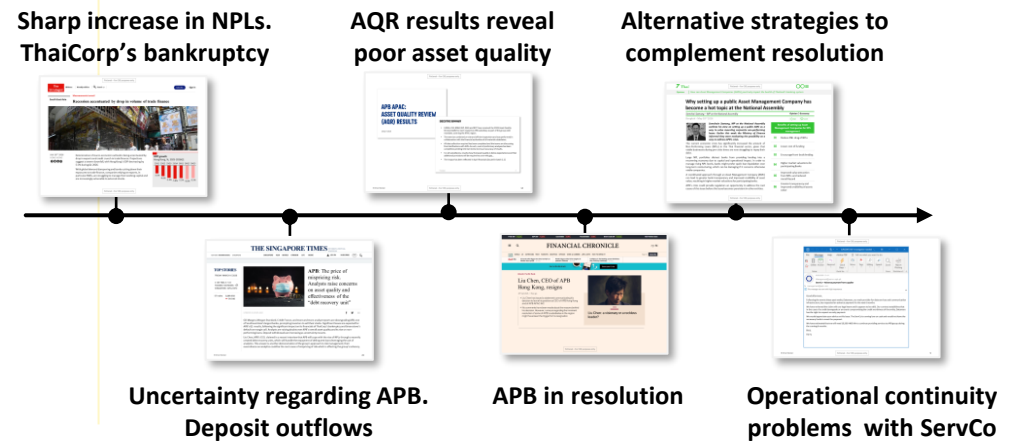
FICTIONAL ENTITY

- APB is a leading **global bank**
- The bank has grouped its APAC material subsidiaries under an **intermediate holding company headquartered in Hong Kong**
- Strong digital offering and an innovative approach to data analysis
- APB's subsidiaries failure driven by:
 - **Growing NPLs** and poor asset quality
 - Bankruptcy of a large corporation
 - **Liquidity issues**
 - **Trading losses**

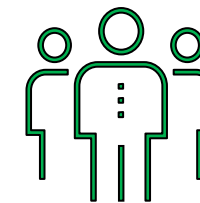
Africa - Cape bank

Expected broad scope: early intervention to resolution / insolvency

8 countries, including CMA (monetary union)
11 authorities
~20 project team members
Q1 2023



Design of Cross-Border CSEs

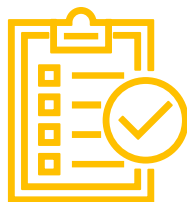


CLARITY ON OBJECTIVES AND SCOPE



- Agree in advance what CSE will test
- Do not be over-ambitious!
- Tailor scope of exercise to agreed objectives

FOLLOW-UP PROCESS



- How will lessons learnt be identified?
- What is the follow-up process?
- Institutional buy-in for that process

PARTICIPATION

- Seniority of participants
 - Objectives and materials need to be aligned with seniority
- Key question – involvement of Finance Ministries

SCENARIO AND MATERIALS

- Undue complexity undermines effectiveness – simple is better
- Focus materials on what you want to test
- A decision-menu can help build materials
- How dynamic?



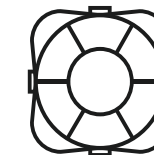
The Latin American CSE

Failure of fictional South American banking group (BSF)

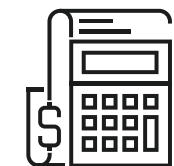
Three rounds



1. Keeping the ailing bank afloat in distress, assessing viability



2. Deciding resolution strategy and tools, pulling the trigger



3. Implementing the resolution: weighing up alternative offers



Selected Findings

Resolution Mandates and Powers

- Some frameworks focussed predominantly on liquidation
- Gaps in resolution tools, eg limited bail-in powers, lack of clarity re bridge bank
- May not be sufficient to deal with the failure of a systemic bank

Resolution planning and resolvability assessments

- Not yet carried out in most participating countries
- Factors such as operational continuity not sufficiently considered
- Authorities' readiness and capabilities could be improved through protocols, playbooks

Funding in resolution

- Lack of clear frameworks for liquidity provision in resolution
- Heavy reliance on deposit insurance funds, and caps on funds available
- Resort to public funding without clear frameworks or recovery arrangements

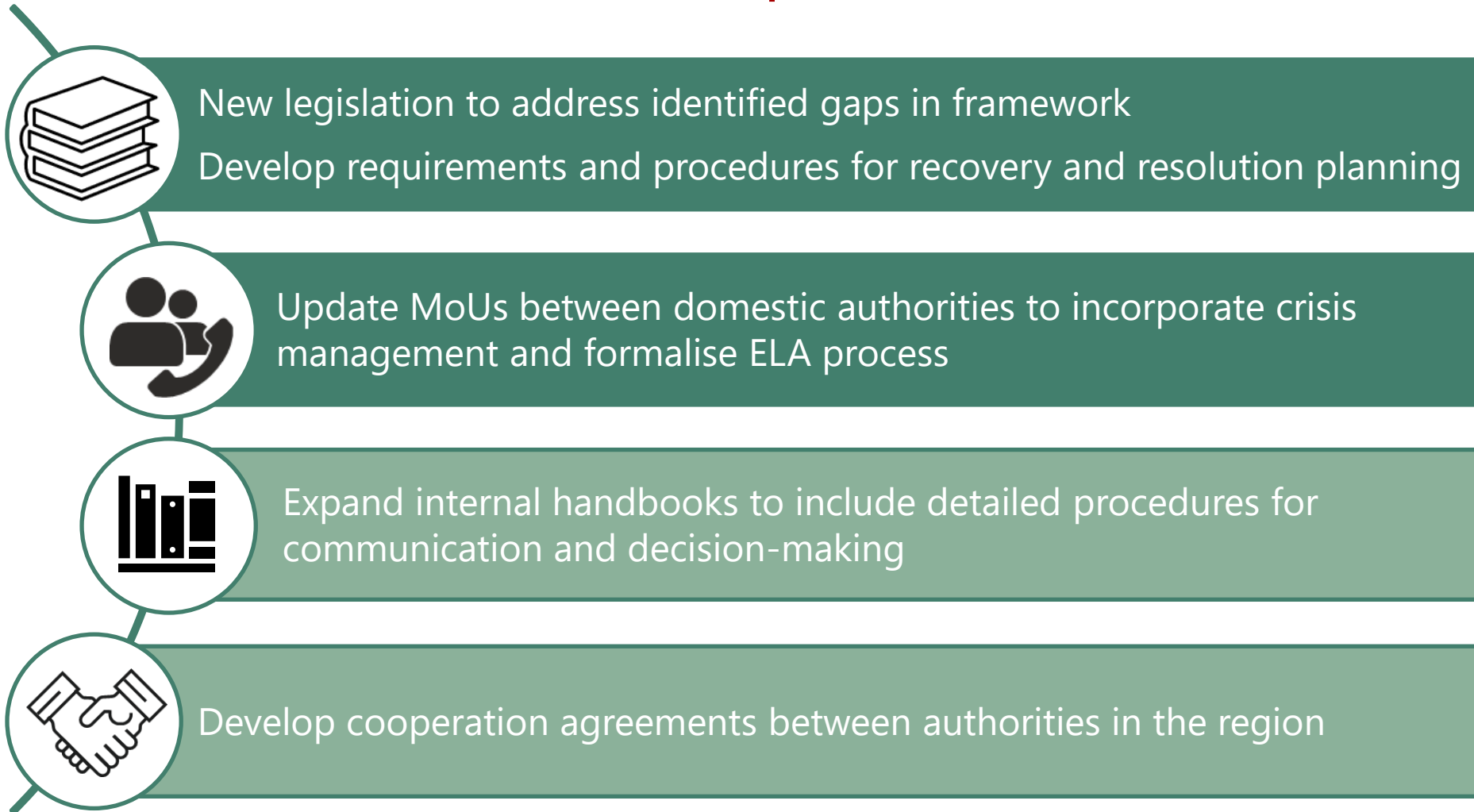
Domestic coordination

- Arrangements for coordination unclear in some countries
- Lack of formal arrangements for timely provision of information to deposit insurer

Cross-border cooperation

- Existing arrangements have supervisory focus
- Obstacles to implementation of a group solution: funding, tools, mandates

Follow-Up Actions



What did we learn?

Topic	Lessons
<p>Exercise preparation Be clear about objectives Do not underestimate time and resources required</p>	<ul style="list-style-type: none"> • Agree in advance what CSE is intended to test, and be realistic about the scope • The local knowledge of Project Team (PT) members is essential to ensure that material is relevant for their own authorities • Dry-runs are crucial, and should be carried out at least a month before exercise to give time to adjust material
<p>CSE narrative Ensure all authorities are engaged but avoid excessive complexity</p>	<ul style="list-style-type: none"> • Keep it as simple as possible, while ensuring materials are realistic and relevant to authorities • Encourage cross-border discussions through information asymmetries and intra-group dependencies • Start a resolution-focussed exercise close to point of failure, and provide enough time to discuss resolution options
<p>Exercise format Be as dynamic and adaptable as possible</p>	<ul style="list-style-type: none"> • Increase the relevance of role-players to foster dynamism of exercise and ensure they are well-briefed • Quantitative materials should be simple and relevant to the decisions required • Shorter sessions in a virtual exercise allows material to be adapted between rounds
<p>Execution and reporting Effective operations team (OT) and well-briefed observers</p>	<ul style="list-style-type: none"> • Ensure that the OT has sufficient capacity to exercise full control and oversight of activities, and to act as key stakeholders to shape the exercise (e.g. Minister of Finance, investors or potential purchasers) • Involve PT members in conduct of CSE (role players, observers) • Ensure observers have clear instructions and are familiar with the legal framework of the country they are overseeing

THANK YOU!

[Cross-border crisis simulation exercise in South America \(bis.org\)](https://www.bis.org)