Remarks by
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More than 200 years ago the founders of this country first presented an overwhelmingly hostile world with the idea of a commercial millennium based on three pillars: free trade, non-discrimination, and peaceful competition.

Many organizations and individuals since then have dedicated themselves to that cause. Since 1966, the Institute of International Bankers has vigorously defended the right of international banks operating in the United States to enjoy the same commercial opportunities available to domestic institutions. For the Office of the Comptroller of the Currency, the struggle has been to ensure that the national banking system can adapt freely and fairly to the continuing innovations in financial services -- once again, without preference or discrimination.

As we approach the new millennium, I believe we're closer than ever to realizing the vision of America's founders. Barriers are crumbling. Openness and integration are being increasingly embraced. The perils of protectionism and discrimination are better understood than ever. So are the benefits of competition and access to the global marketplace for capital, customers, and ideas.

It goes almost without saying that, for domestic as well as foreign bankers, the global environment holds risks as well as rewards. We've had quite a few blunt reminders recently: economic turmoil in Asia, Latin America, and Eastern Europe, and closer to home the near-collapse of a giant hedge fund that, among other things, took unwarranted risks in foreign currency trading. Each of these situations produced big losses for a small number of large U.S. commercial banks. They also raised compelling questions about the stability of the international economic order.

No one can be certain where the next trouble spot will be. Certainly there's no shortage of candidates and scenarios. Volatility in financial markets is something we must now take for granted. Technology -- a blessing in most respects -- virtually guarantees it. The Year 2000 looms on the horizon. The speed with which news can now travel makes for hair-trigger market responses. Investors can react instantly -- and just as easily overreact -- to events halfway around the world.

It's a certainty that economic crises will occur in the future and spill over national borders. The challenge is how we go about managing and containing their impact. That's the question I'd like to discuss with you this morning.

Both within our own countries and in cooperation with our colleagues around the world, financial supervisors bear a major part of the front- line responsibility for preventing financial crises and for managing them, when they do occur. Most analysts agree that supervisory errors -- of omission and commission -- were at least

partly to blame for the financial difficulties from which many of the economies, of East Asia in particular, are still striving to recover.

It seems clear that a more robust, independent, and pro-active supervisory presence in those countries would have mitigated, if not averted, some of their problems. Just as clearly, supervisory vigilance beyond the afflicted countries has played an important role in keeping the Asian problem from spreading beyond the Pacific Rim to other shores.

As I've already said, banks in the United States and elsewhere have not been unaffected by the fallout. Many did not appreciate the extent of their vulnerability to these external shocks. Banks that may have viewed themselves as too small or too isolated to worry about such distant developments have had a painful lesson in the reach of the new global economy.

Let me give you just one example. In fiscal 1996, U.S. farm exports were worth just under $60 billion. For 1999, the total is expected to be in the neighborhood of $49 billion, with more than 80 percent of the decline attributable to the problems in East Asia. The result, predictably, has already been a small increase in the number of problem loans to afflicted farmers. Even more importantly, we have seen a dramatic increase in problem loans to those who depend upon spending by farmers for their own livelihoods.

Larger banks may have understood in advance the risks of foreign lending, foreign currency trading, and lending to domestic customers whose fortunes were intertwined with those of emerging Asian economies. But foreknowledge of the risks has not made the losses they've suffered any less painful to their pride, their bottom line, or their reputation with investors.

It's important, however, that we not lose sight of the fact that, despite many dire predictions to the contrary, such losses have not, to date, compromised the overall safety and soundness of our banking system or that of other major countries outside of Asia. That's itself partly a byproduct of globalization and diversification.

With their loans and investments so widely dispersed over product and place, and the growing importance of fee income generated by new products and services, commercial banks in this country seem more resilient and more resistant to sectoral downturns than at virtually any time in their history.

Many have taken a portfolio approach to managing risk: riskier loans and investments are offset with safer ones to produce an overall profile suitable to the institution's own appetite for risk. And they have adopted advanced systems that enable the risk of individual loans within the portfolio to be more accurately measured, monitored, and priced.

For example, robust risk management systems today include provisions for stress-testing loans -- that is, subjecting them to a variety of hypothetical adverse scenarios. Stress-testing provides bankers with insights into the levels of risk threatened by various changes in the economy, which they can then use in evaluating total risk exposure.

While bankers themselves deserve most of the credit for their apparent success in weathering the international storms, bank

supervisors, as I've suggested, have not been mere bystanders in this process. In some respects, the principles of bank supervision -- and banking itself -- are not fundamentally different today than they were thirty years ago, at the dawn of the global economy.

The most successful bankers have always been those who excelled at the business of managing risk. For their part, bank supervisors have always been in the business of developing and applying prudential rules to help control those risks, regardless of the size or business focus of the bank to which they pertain.

Today, those rules cover examination of capital adequacy, loan loss reserves, asset concentrations, liquidity, internal controls, and risk management itself. This list of concerns represents an expansion -- but not by much -- of the supervisor's traditional repertoire.

But supervision today is certainly more sophisticated and -- shall I say -- more worldly than it was three decades ago. Assessing risk in internationally active institutions with complex corporate structures and diverse product menus often involves evaluating activities and processes taking place around the globe and in related corporate entities. Supervision across borders -- and across functions -- requires collaboration with other supervisors who may not share the same legal mandate or operational philosophy or even speak the same language.

One highly significant change in our approach to supervision involves the growing emphasis on qualitative assessment of bank management and its information and control systems. Experience has repeatedly taught us that numbers alone do not tell the whole story of a bank's health. In fact, in some circumstances, such numbers can be quite misleading. A growing global economy can make bad credit judgments look good.

An abundance of liquidity in the marketplace, bringing increased competition for loans, has caused some banks to relax established standards and in some cases to take foolish risks. We know two things from experience. First, economic conditions inevitably change. And second, compromises and concessions made in good times have a likelihood of increasing losses when times change.

That's not to say that banks should not strive to be competitive. Prudent risk-taking that's based on good information and is understood by management and given proper oversight, is the essence of the banking business.

But risk-taking in an information vacuum, based not on sound credit judgments but on the stylishness of the borrower, can never be prudent. Any loan officer who asks a "hot" borrower for financial information only to be told "we never give that out," should walk away from the credit. Advancing hundreds of millions of dollars without adequate information simply because other creditors may be scrambling to provide funds to some group perceived as market geniuses, is not prudent lending. It's Russian Roulette.

Moreover, it's one dangerous game whose potential risks are not limited to those seated at the table. As we have seen, in an increasingly interconnected world, private financial decisions can have far reaching public consequences. And that demands a

multidimensional -- and multinational -- approach to financial supervision.

On the one hand, we must all work to promote the adoption of fundamental supervisory principles in those parts of the world where they have not been adopted already. On the other hand, supervisors must be endowed with sufficient discretion to accommodate the wide range of variations in business strategies and structural arrangements under which financial institutions operate in the real world. And, finally, provision must be made for more regular, ongoing dialogue between supervisors than ever before.

That's a daunting challenge. Yet progress is being made on several fronts. The adoption in October 1997 of 25 "core principles for effective supervision" by the Basle Committee on Banking Supervision was a major step in this direction.

The Basle core principles, which codify prevailing supervisory practice in the advanced nations -- particularly (though not exclusively) the United States -- embody an important assumption: that banking crises stem from common causes, whether they take place in industrialized or developing countries. In other words, the principles of effective supervision and the principles of sound lending -- principles that have withstood the test of time and experience in the United States and elsewhere -- are likely to apply to financial institutions everywhere.

It's encouraging to me that the core principles -- and the assumptions on which they're based -- are being rapidly embraced in the non-G-10 world. At last year's International Conference of Banking Supervisors in Sydney, Australia, supervisors representing 120 countries gave the core principles a ringing endorsement. The Basle Committee continues to issue guidance elaborating on the core principles.

This activity has been matched by activity on other international fronts. Just in recent months, the G-7 heads of state and finance ministers have gone on record reiterating their calls for strengthened supervision, increased information exchange between and among functional and national supervisors, and improved transparency and accountability.

Similar calls are made in papers released by the so-called G-22, which included emerging market countries along with the G-7. Two weeks ago, the Joint Forum on Financial Conglomerates, a cooperative body of banking, insurance, and securities supervisors, issued a set of papers on principles for supervision and information exchange.

One recent illustration of the critical importance of these cooperative, cross-industry, and cross-border efforts is the work being done to promote international Y2K readiness. The mechanisms for multilateral communications developed for that purpose should prove useful in promoting enhanced dialogue on the whole range of supervisory issues in the future.

Of course, there's a world of difference between commitments to action and action itself. We have no illusions that each of the countries that subscribed to the Basle core principles are in a position to fully implement them in the near future. We are not even certain about what constitutes adherence, although a joint task force

consisting of representatives from the Basle Committee, the International Monetary Fund, and the World Bank is even now wrestling with that question and with developing ways to measure progress.

Certainly, serious obstacles remain to be overcome. The international supervisors who assembled at Sydney last year spoke very nearly in unison, but they were not always authorized to fully commit their governments. The degree to which political leaders will provide the resources, operational independence, and moral support to their own bank supervisors is sure to vary dramatically across the spectrum.

We will also need to enlist the cooperation of other interested parties, such as the bodies that set accounting standards. But one hopes that self-interest and the lessons of recent history will convince leaders around the world -- and financial institutions themselves -- that in the new integrated economy, there is no viable alternative to strong, professional financial supervision.

Conclusion

The crises in international finance that we've undergone in recent years have certainly been traumatic. They've caused hardships for millions of people and set back development in parts of the world that desperately need it.

Unfortunately, we sometimes learn best from the hardest lessons. Upheaval and dislocation have driven home the basic fact that healthy banking systems are a prerequisite for sound national and global economies. Financial instability has proved the importance of effective supervision. Let me close by emphasizing my belief that it's in your interest, as representatives of non-U.S. banks in America, to support the efforts I've described to strengthen financial supervision world-wide. No one has more to gain from effective international supervision than the financial institutions that operate under its umbrella. Conversely, no one has more to lose when financial supervision goes awry, as events in East Asia demonstrated.

Strengthening international financial supervision is one important means of providing for a safe and sound banking system and a prosperous international economy. I encourage you to join in that effort.

Thank you.