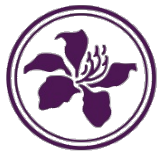

Remarks on fitting macroprudential stress testing into the broader policy framework

For IMF (MCM)-LSE (SRC) Symposium
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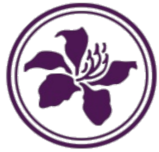
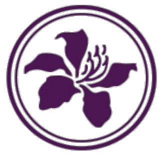
Interactions between macroprudential and mircroprudential policy tools



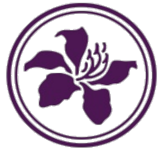
- In some circumstances, macroprudential policy tools are the first line of defend for a safe and sound system
- Mircroprudential policy tools ensure individual financial institutions to have robust financial condition
- For example, countercyclical capital buffer enhances the overall capital requirement in a banking system, while banking supervisors impose targeted capital adequacy ratios to individual banks.
- Countercyclical capital buffer has improved resilience of the system as a whole.
- However, individual banks with prudential concerns should have capital planning for additional capital requirements.

Implications for macroprudential stress testing



- Given that both macroprudential and mircroprudential policy tools are likely applied to the system at the same time, macroprudential and mircroprudential stress tests should be designed with consistent objectives and input parameters
- As macroprudential policy may have impact on the macro economic condition (e.g. through the credit channel: loan growth and rates), the stress-testing framework should consider the macro-financial feedback effect induced by the macroprudential policy.

Interactions of macroprudential policy tools with other policies



- Interactions of macroprudential policy with other policies (in particular monetary policy) are an ongoing research topic in the community.
- Given that Hong Kong has significant presence of international banks, their home countries′ monetary policies will affect those banks′ international lending business and therefore international capital flows.
- Our research is to study how our macroprudential policy tools interact with other economies′ monetary policies.

Interactions of macroprudential policy with other economies monetary policies (1)

- The study finds evidence of an international transmission of foreign monetary policies to the Hong Kong banking sector. The extent of monetary policy transmission from a country is found to be dependent on how much net cross-border funding of foreign banks in Hong Kong raised from that country.
- In response to looser monetary policies in major advanced economies (such as the US, the UK and Japan), banks with higher net cross-border funding from these countries' banking sectors are estimated to increase their USD loan growth more than their peers in Hong Kong.
- A one percentage point decrease in the US monetary policy shadow rate (which takes into account the effect of unconventional monetary policy), foreign banks in Hong Kong are estimated to increase USD loan growth by 1.5 percentage points if the share of net cross-border funding from the US banking sector increase by one standard deviation.

Interactions of macroprudential policy with other economies monetary policies (2)

- This suggests that a bank's net cross-border funding from foreign banking sectors is an important factor affecting the spillover effect of monetary policies internationally.
- We consider a macroprudential policy tool – the Stable Funding Requirement (SFR), which was introduced by the HKMA in October 2013. The SFR requires those banks with rapid (USD) loan growth to maintain longer term stable funding to support their lending business.
- Our preliminary findings show that SFR tends to reduce the spillover effect of foreign monetary policies. Those banks in Hong Kong that are subject to the SFR are found to have a lower sensitivity of their USD loan growth to foreign monetary policies.