

**Remarks
by
Mrs. Marlene Bayne
Director, Bank Supervision Department
Central Bank of Barbados
at the
Rotary District Conference
on April 13, 2011
Lloyd Erskine Sandiford Centre**

Bank Regulation in Barbados: Recent Challenges and Responses

Introduction

District Governor, W. Anthony Watkins, District Governor-Elect, Lara Quentrall-Thomas, Members of the District Executive, Rotarians and other distinguished guests

I wish to first thank you (and particularly John McKenzie from Consolidated Finance) for your kind invitation to speak to you today. I have noted your Conference theme of Building Healthier Communities, Bridging Regional Cultures and would like to convey my best wishes for a successful conference.

At the Central Bank of Barbados we are also focused on *building*. Our concern, however, is with the health of the financial system. The Bank has two key objectives in this regard, 1) to regulate and monitor the financial environment and 2) to provide a stable monetary framework and sound financial structure.

Regulatory Framework and Supervision

To achieve our objectives, we have ensured that the fundamentals are in place. Barbados' regulatory framework has been developed to conform with international standards and best practices, as contained in the Basel Core Principles for Effective Banking Supervision.

Barbados is subject to the Financial Sector Assessment Programme conducted by the International Monetary Fund every five years. The last assessment in 2008 revealed that Barbados continues to do well in the area of compliance with the banking core principles.

Good regulation starts with licensing sound institutions and taking great care, at this stage, to determine the fitness and propriety of the shareholders, directors and senior management of applicants. It is also important to examine the source and capital adequacy of the proposed licensee. The source of capital is critical, in light of money laundering concerns, and the need to avoid the entry of tainted funds into the capital of a financial institution!

Regulators must also safeguard depositors' funds. Therefore, on an ongoing basis, we examine the operations of financial institutions to ensure compliance with safety and soundness requirements and with relevant laws and standards.

At the end of December 2010, we supervised seven commercial banks, 14 near banks and 45 international banks. Commercial banks are engaged in

traditional types of financial services, including mortgages, personal loans, commercial and corporate loans, treasury operations, brokerage, trust and limited capital market activity. Additionally, advances in technology have allowed our banks to offer value added services to customers, including credit and debit cards, electronic banking and telephone banking services.

Commercial banks in Barbados are exclusively branches and subsidiaries of international and regional banks. At the end of 2010, the assets of commercial banks totalled BDS\$11.15 billion, while the total assets of the 14 near banks amounted to \$1.81 billion. The near banks to which I am referring include merchant banks, mortgage and finance companies, as well as trust companies.

International banks differ significantly in terms of their size, capital structure and activity. These banks are involved in deposit taking, assets under management, treasury operations and several are high net worth licensees investing the wealth of their shareholders. Total assets of the international banks operating in Barbados at the end of 2010 stood at BDS\$73.8 billion. This sector is dominated by a few large Canadian banks. To illustrate, the combined assets of the ten largest¹ international banks at the end of last year totalled BDS\$65.6 billion (which represented 88.8 percent of the total assets in this sector).

¹ The largest banks are defined as all banks with total assets in excess of \$1 billion and this number may vary between 8 to 11 banks.

In 2007, the Central Bank adopted a risk-based supervisory approach based on the model used by the Office of the Superintendent of Financial Institutions (OSFI) in Canada. This approach allows us to allocate scarce supervisory resources toward those institutions that have a higher risk profile, resulting in improved efficiencies in supervision.

In the past decade or so, we have noticed increasing cross-border expansion of regional financial institutions. In response, the Bank has improved its ability to supervise banks with cross border operations, and to monitor risks on a solo and consolidated basis. Barbados is a founding member of the Caribbean Group of Banking Supervisors which has been in existence for over 20 years, and this Grouping allows for active interchange of information relating to regional banks and for sharing of supervisory experiences. To facilitate cooperation and information sharing, Caribbean regulators have signed a Memorandum of Understanding and meet twice yearly at supervisory colleges of pan Caribbean banks.

The Central Bank continues to be an active member of other regional and international regulatory groupings, e.g. the Association of Bank Supervisors of the Americas, and the Group of International Finance Centre Supervisors and the Caribbean Financial Action Task Force.

In addition, the Central Bank continues to work closely with the other sectoral regulators of non-banking institutions that comprise the financial system in Barbados and a domestic MOU is in place to allow for information sharing

among domestic regulators. In an effort to improve supervision of the non-banking sector and to address some concerns identified in the last FSAP review, a Financial Services Commission (FSC) was established earlier this month to amalgamate the supervision of all non-banking institutions, i.e. credit unions, securities and pensions and insurance. The Central Bank will of course continue to work closely with the FSC.

One lesson from the crisis is the need to take a macro-prudential view of the financial system and in response, the Central Bank established a Financial Stability Unit in the first quarter of 2010. The FSU conducts ongoing financial stability analysis, taking account of the impact of macroeconomic variables on all players in the financial system, and performs intermittent stress testing and scenario analysis. We look forward to publishing Barbados' first Financial Stability Report soon.

Impact of the Crisis on Barbados' banking sector

A large percentage of our banking institutions originate in Canada (over 50% of the number of domestic banks and about 78% of the international banks). Hence, Barbados has developed a strong relationship with the Canadian regulators and, in 2010, the Central Bank of Barbados and OSFI signed an MOU to facilitate cooperation and information sharing. This relationship allows us to share experiences at annual supervisory colleges arranged by OSFI on Canadian parent banks with branches and subsidiaries in Barbados, and to maintain ongoing contact by way of quarterly conference calls.

The limited impact of the financial crisis on Barbados' banking sector can partially be attributed to the fact that our banks are mostly Canadian in origin. You may be aware that the Canadian financial system fared relatively well during the crisis, when compared to many of their international peers. The *Global Competitive Report 2010-2011 produced by the World Economic Forum* rated Canada as having the soundest financial system in the world. Barbados ranked 12th, and Trinidad & Tobago 21st, both well ahead of USA which ranked 111th and the United Kingdom which ranked 133rd.

Canada's strong rating can be attributed to good macroeconomic fundamentals², a conservative risk appetite and a credible and sound regulatory environment. The relatively conservative nature of Canadian banks helped to secure them against large losses as these banks did not originate subprime mortgages to any material extent, are well diversified geographically and across business lines and do not participate heavily in markets for the more exotic instruments.

Similarly, Barbadians are not high risk takers and our banks tend to be conservative and offer relatively unsophisticated products. Hence, there was limited direct impact of the financial crisis on the banking system in Barbados. The financial system did not escape entirely however, since the indirect effects of the global financial uncertainty associated with the crisis continues to have spill-over effects on the sector. We have noticed increased credit risk with

²Canada's banking system has benefited from strong macroeconomic fundamentals that include credible monetary policy and sound fiscal management, with years of government surpluses, together with an enhanced focus on system-wide financial stability by the Bank of Canada.

higher loan delinquencies being recorded across banks. Tourism, as the major income earner, was heavily impacted by the downturn in the major international markets, and hence the increase in non-performing loans was largely concentrated to the tourism sector. In spite of these challenges, commercial banks and near banks were able to maintain acceptable levels of capital, well in excess of the minimum prudential requirements.

Another indirect impact relates to liquidity. Although liquidity remains at an acceptable level, by the end of 2010, there was a noticeable downward trend in the excess liquidity ratio. Banks in Barbados have two levels of reserves in case of liquidity challenges. In her review of the impact of the crisis on Barbados in 2009, past Central Bank Governor, Dr. Marion Williams, noted “while many developed economies had abandoned reserve requirements, commercial banks and non banking financial institutions in Barbados are still required to hold cash reserve requirementsand securities requirements. These can act as a source of support should banks experience liquidity problems”.

International financial centres have continued to come under intense scrutiny. More recently, the G20 has called for international agencies, such as the Financial Stability Board (FSB), the Financial Action Task Force (FATF) and the OECD to re-evaluate financial centres, specifically with respect to their level of cooperation and information exchange in the areas of taxation and in relation to sharing other financial information. As an international financial centre, like several of our regional neighbours, Barbados has been subject to increased scrutiny, which we have had to address by providing in-depth information

regarding consolidation supervision, and by making adjustments to our tax law to meet ever changing requirements. Failure to meet the demands of the changing standards could result in jurisdictions being blacklisted which, of course, would threaten the continued existence of these financial centres. One success which we can mention is the fact that arising from the intervention of Barbados along with a few other financial centres which do not have a voice in the Financial Stability Board (FSB), Barbados expects to receive an invitation to become a member of one of the Regional Consultative Groups recently established by the FSB.

Priorities going forward

What then are our priorities? We recognize the need for continuous improvement in regulation and are currently focused on enhancing the regulatory framework by amending existing legislation and guidelines, by strengthening consolidated supervision and improving our data collection capabilities and prudential reports.

Barbados was in the process of implementing Basel 2 capital Framework when the crisis broke. Since then several enhancements to the Framework have been made. These are commonly referred to as Basel 111. We have taken the opportunity to review our Implementation Roadmap and are focussing initially on implementing Pillar 2, which emphasises the importance of strong regulatory oversight and strong industry risk management practices. The pending amendments to the existing legislation, the issuance of Guidelines and the

revision of our prudential reporting forms are part of the Pillar 11 implementation process.

Another priority will continue to be the strengthening of information exchange and cooperation among domestic, regional and international authorities, leveraging on existing MOUs. Barbados is a member of a CGBS Technical Working Group which is developing a Regional Crisis Management Plan. Out of the Regional Plan the need for a National Crisis Management Plan for Barbados was clear, and this work has commenced. Crisis Management Plans seek to identify all the key stakeholders and to establish their respective roles in crisis times. It is important that these Plans are tested intermittently and revised as necessary. If Crisis Management Plans are comprehensive, it is hoped that crisis situations can be handled with greater efficiency.

I think we can all agree that another important lesson we can take away from the crisis is that while it may not be possible to prevent future crises, one can plan, to mitigate the possible fallouts. Caribbean Banking regulators have taken this on board.

Thank you for your attention.