SYMPOSIUM ON BUILDING THE FINANCIAL SYSTEM OF THE 21ST CENTURY: AN AGENDA FOR JAPAN AND THE UNITED STATES

OCTOBER 21-22, 2017

Hilton Odawara Resort & Spa, Japan

AGENDA

FRIDAY, OCTOBER 20

7:00 p.m. **WELCOME** Nagame

- Hal Scott, Nomura Professor and Director, Program on International Financial Systems, Harvard Law School

7:00-9:00 p.m. **DINNER BUFFET** Nagame

SATURDAY, OCTOBER 21

7:45-9:10 a.m. **BREAKFAST BUFFET** Arena

9:15-9:45 a.m. **PANEL SESSION** Take

Update on Governor Koike's Advisory Board to Revitalize Tokyo as a Global Financial Center

- Jesper Koll, CEO, Wisdom Tree Japan
- Andy Saito, Chairman, KKR Japan

9:50-9:55 a.m. **WELCOME** Take

- Hal Scott, Nomura Professor and Director, Program on International Financial Systems, Harvard Law School

10:00-11:10 a.m. **PANEL SESSION** Take

Surviving the monetary policy exit & possible causes for the next financial crisis

- Yoshinori Nakata, Director-General, International Department, BOJ
- Nathan Sheets, Chief Economist, Prudential Global Investment Management
- Paul Sheard, Executive Vice President and Chief Economist, S&P Global
- Takumi Shibata, President and CEO, Nikko Asset Management Co., Ltd.
- Akinari Horii, Special Advisor/Member of the Board of Directors, The Canon Institute for Global Studies (moderator)

11:15-12:35 p.m. **SMALL GROUP SESSIONS**

Possible causes for the next financial crisis

Group	Room	Facilitators	Reporter
1	Take Foyer	Takayoshi Hatayama/David Asher	William Grimes
2	Oshima	Ken Takamiya /Doug Hymas	Akihiro Wani
3	Hatsushima	Etsuko Katsu/Rick Katz	Rich Mattione
4	Board Room	Shigeki Kimura/Jesper Koll	Hamilton Lin
5	Asagiri	Yoneo Sakai/Allan Smith	Kyoko Altman
6	Ashigara	Tsuyoshi Oyama/Jim Walsh	Osamu Yamamoto
7	Hakone	Tsutomu Watanabe/Hugh Patrick	Fabiana Fedeli

12:40-2:10 p.m. **LUNCHEON AND KEYNOTE ADDRESS** Arena

- Masatsugu Asakawa, Vice Minister of Finance for International Affairs, Ministry of Finance, Japan
  Introduced by: Akira Ariyoshi, Specially Invited Professor, International University of Japan
- David Malpass, Under Secretary for International Affairs, U.S. Department of Treasury
  Introduced by: Hal Scott, Nomura Professor and Director, Program on International Financial Systems, Harvard Law School

2:10 p.m.- 2:45 p.m. **PANEL SESSION** Take

Where is financial regulation headed? Deregulation, fragmentation and the demise of Basel framework

- Adam Gilbert, Financial Services Advisory Global Regulatory Leader, Pricewaterhouse Coopers
- Tsuyoshi Oyama, Partner/Head of Center for Risk Management Strategy, Deloitte Touche Tohmatsu Japan

2:45-4:05 p.m. **SMALL GROUP SESSIONS**

Where is financial regulation headed? Deregulation, fragmentation and the demise of Basel framework

Group	Room	Facilitators	Reporter
1	Take Foyer	Akira Ariyoshi/Arthur Mitchell	William Grimes
2	Oshima	Akinari Horii/Brian Kelly	Akihiro Wani
3	Hatsushima	Yoshio Okubo/Shigesuke Kashiwagi	Rich Mattione
4	Board Room	Toru Otsuka/Paul Speltz	Hamilton Lin
5	Asagiri	Takumi Shibata/Cliff Shaw	Kyoko Altman
6	Ashigara	Hiroyuki Kamano/Glen Wood	Osamu Yamamoto
7	Hakone	Shinichiro Nakano/Don Kanak	Fabiana Fedeli

4:05-6:30 p.m. **FREE TIME**

4:05-6:30 p.m. **RAPPORTEURS MEETING** Board Room

6:30-7:15 p.m. **RECEPTION** Arena Foyer

7:15-7:45 p.m. **KEYNOTE ADDRESS** Arena

- Nobuyuki Hirano, President & Group CEO, Mitsubishi UFJ Financial Group, Inc.
  Introduced by: Akinari Horii, Special Advisor, The Canon Institute for Global Studies

7:45-9:15 p.m. **DINNER** Arena

9:15-10:00 p.m. **AFTER DINNER COCKTAILS** Nagame

SUNDAY, OCTOBER 22

7:30-8:30 a.m. **BREAKFAST BUFFET** Arena

8:40-9:45 a.m. **PRESENTATION & DISCUSSION** Take

Where is financial regulation headed? Deregulation, fragmentation and the demise of Basel framework

- Akihiro Wani, Senior Counselor, Morrison & Foerster, LLP
- Doug Hymas, Japan Country Executive, Managing Director, BNY Mellon

9:45-10:45 a.m. **PRESENTATION & DISCUSSION** Take

Possible causes for the next financial crisis

- Tsutomu Watanabe, Professor, University of Tokyo
- Bob Dohner, Deputy Assistant Secretary, International Economics Analysis and Senior Asia Advisor, U.S. Department of the Treasury

10:45-11:00 a.m. **REFRESHMENT BREAK**

11:00-12:30 p.m. **PLENARY PANEL SESSION** Take

What we have learned since our first symposium in Cape Cod of summer 1998

- Hal Scott, Nomura Professor and Director, Program on International Financial Systems, Harvard Law School (moderator)
- Hiroshi Watanabe, President, Institute of International Monetary Affairs (IIMA)
- Akira Ariyoshi, Specially Invited Professor, International University of Japan
- Robin Radin, Co-Founder, Harvard Law Japan-U.S. Symposium

12:30-1:15 p.m. **BUFFET LUNCHEON** Arena





Program on International Financial Systems

Symposium on Building the Financial System of the Twenty-First Century: An Agenda for Japan and the United States

Odawara, Japan | October 20-22, 2017

Final Report

Program on International Financial Systems

Founded in 1986, Program on International Financial Systems (PIFS) fosters the exchange of ideas on capital markets, financial regulation, and international financial systems through its acclaimed portfolio of Symposia on Building the Financial System of the 21st Century. PIFS also conducts research and organizes special events on these topics.

Each year, PIFS bilateral Symposia bring together senior financial leaders, high-ranking government officials, and distinguished academics from the United States and their counterparts from China, Europe, Japan, and Latin America for intensive dialogue on issues affecting international capital markets.

Off-the-record and closed to the media, the invitation-only PIFS Symposia convene leading market practicioners at off-site retreat venues. The Symposia model features candid, intimate exchanges between global counterparts within small-group discussions. Keynote addresses and panel sessions serve to initiate and enhance the interactive, small-group dialogue, which is conducted under Chatham House Rules in order to foster an open exchange of ideas. These discussions are synthesized and presented on the final day of the Symposium in a plenary session, and then summarized and published in the following Symposium Final Report.

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Symposium Final Report

The twentieth Japan-U.S. Symposium on Building the Financial System of the 21st Century was held in Odawara, Japan, from October 20-22, 2017. Sessions addressed the development of Tokyo as a global financial center, exit from quantitative easing policies, possible sources of the next financial crisis, and new directions in financial regulation. Participants also reflected on the experiences and achievements of the Japan-US Symposium over its two decades of promoting dialogue to address mutual challenges.

Session 1

Revitalizing Tokyo as a Global Financial Center

In Session 1, participants discussed the prospects for revitalizing Tokyo as a global financial center. They addressed several recommendations that arose from Tokyo Governor Koike's advisory board on the subject. Opinions were mixed as to whether proposed changes would significantly improve the attractiveness of Tokyo markets for international financial institutions, investors, and issuers.

Participants noted that there had been a number of efforts over the past three decades to promote Tokyo as a global financial center, and that over time significant progress had been made in improving the functioning of Japanese financial markets.

Liberalization efforts dating back to the 1980s and culminating in the Big Bang (1998-2001) and Financial Instruments and Exchange Law (2006) had brought Japanese financial regulation to global standards, and participants lauded the quality of supervision by the Financial Services Agency. A number of tax issues that had deterred foreign investors had also been dealt with. However, on a variety of measures, Tokyo had not improved its ranking among global financial centers.

Recognizing the extent of reform to date (but also the limited internationalization of Tokyo markets), Gov. Koike's advisory board had focused on a series of issues, including creating an overseas promotion team to invite global asset managers to Tokyo, establishing the Tokyo Prize for cutting-edge research in finance, introducing the Emerging Manager Plan to attract new asset managers, cutting corporate tax rates, and establishing cooperative memorandums of understanding with other global financial centers. Participants reported progress on some of these recommendations, including a new MOU with the City of London, a corporate tax cut by the Tokyo Metropolitan Government (but not yet the national government), and an accelerator program that reduced by two-thirds the time required for asset managers to get licenses. Some participants saw considerable opportunity for Tokyo to develop a new model of a financial center. For example, the eventual unwinding of the Bank of Japan's massive quantitative easing (which had left the BOJ holding half of all public debt in addition to a variety of other assets) could offer asset managers an attractive opportunity to participate in the "re-privatization" of the market. There was also an argument that political conditions could support decisive action. At the national level, the Government Pension Investment Fund had already shown leadership in promoting new asset managers, while the Abe administration had formally committed itself to economic liberalization and improving corporate governance. In Tokyo, Gov. Koike was seen as politically ambitious and prepared to push the Abe administration on corporate taxes and regulatory reform,

perhaps through the use of the "special administrative zone" *(Tokku)* program. It was also suggested that the emphasis on fintech and entrepreneurship could reduce some of the natural political resistance of voters to the usual narrative of enriching "greedy bankers."

While many participants lauded the goal of revitalizing Tokyo markets as well as some of the specific efforts, a number of them were skeptical of the prospects for success—either because they felt that the proposals were premised on an incorrect understanding of the obstacles to internationalization of Tokyo or because they saw the proposed remedies as too timid.

Participants raised a number of issues that they felt were key obstacles to bringing international investors back to Tokyo. One point of contention related to taxes. While the advisory committee had identified corporate taxes as a particular problem, some participants argued that personal tax rates were much more important for asset managers. For example, one noted that the marginal rate for high-income individuals in Japan was 55%, compared to 22% in Singapore. Others disputed the idea that tax rates were the primary issue—as one pointed out, real estate investing in Japan had been transformed not by tax policy changes, but rather by introduction of J-REITs. They argued that creating opportunities and incentives for new asset managers to enter the market was at least as important as tax cuts. Some participants also raised the issue of lackluster opportunities in Japanese capital markets. They argued that it was essential to have a strong corporate sector in order to have a strong financial sector; in this respect, the fact that Japanese equities had underperformed other markets for most of the last twenty-five years was seen as very problematic. Moreover, recent news about scandals and lack of transparency in some Japanese companies (an historical problem) could compound the lack of confidence. To fix this problem, these participants argued that the authorities should redouble their focus on transparency, disclosure, and market discipline by promoting stronger corporate governance standards and encouraging institutional investors to take more seriously their role in holding companies accountable.

Participants also brought up some structural concerns that would be challenging to change quickly. One was the lack of English-language fluency among financial service professionals and supervisors. Another was the continued prevalence of bank financing of Japanese corporations. Some participants felt that this had retarded capital market development and slowed the growth of services such as asset management, private equity, and venture capital §

Session 2

Surviving Monetary Policy Exit and Possible Causes of the Next Financial Crisis

In Session 2, participants discussed the economic implications of central banks' expected exit from quantitative easing in the major economies. Most participants expressed confidence that the shift in monetary policy in the US and Europe would not lead to new financial crises either at home or in major emerging economies. Participants also discussed other issues that could be triggers for financial crisis, including military conflict, natural disaster, and cyber attacks, and contemplated whether the global financial system was prepared to handle such contingencies.

EFFECTS OF QUANTITATIVE EASING AND EXIT

Participants discussed at length the effects of exit from quantitative easing. They noted that in the US, the Fed had begun a cycle of tightening in late 2016 through a gradual rise in the Fed Funds rate and had also clearly communicated its intention to start unwinding its vast holdings of securities. Meanwhile, the European Central Bank's announcement that it would halve its asset purchases in 2018 showed a similar, albeit slower, path to exit and signs also pointed to exit by the Bank of England (which in fact raised the policy rate a few days after the Symposium). Participants anticipated that the Bank of Japan's eventual exit from quantitative easing would be longer in coming, but several felt that market participants should start thinking about the possible consequences when it did happen.

Despite concerns raised in the media about the disruption that might arise as central banks withdrew from quantitative easing, participants were generally sanguine about the ability of central banks to reduce asset holdings without disrupting markets. There were two main reasons given for this assessment. First, many participants emphasized that quantitative easing, though often characterized as "unconventional monetary policy," was in fact just an extension of normal monetary policy. Like conventional policies that targeted short-term interest rates, quantitative easing was meant to shift investment incentives by lowering long-term rates and strengthening asset prices. Thus, they argued, the key question was whether a particular economy was ready for tighter monetary policy, not whether the particular policy target was interest rates or the central bank balance sheet. Second, participants were confident that there would be investors eager to purchase the securities that central banks would be gradually selling off, and saw no reason to expect disruptions in government debt markets. They also noted that if disruptions did occur, central banks could scale back or change the timing of their plans for selling assets.

Thus, the question came down to whether the timing was right for an exit to quantitative easing, i.e., whether economies were operating close to full employment and whether inflationary expectations were anchored near central banks' inflation targets. Participants' views on these criteria varied. Most felt that

US inflationary expectations were anchored close to the inflation target and that the US economy was strong enough that it made sense to start drawing down the Fed balance sheet and normalizing interest rates, although some cautioned that the continued low inflation could mean that the economy was not yet ready for a tightening cycle. One question was whether long-term rates would move up in concert with short-term rates or would continue to be unresponsive, which would lead to a flattening or even inversion of the yield curve. There was more concern expressed about the potential effects of exit from quantitative easing in the Eurozone and UK. In the Eurozone, some participants worried that growth remained weak and inflationary expectations remained below the ECB target. Thus, they anticipated that the tightening process could be somewhat drawn out. In the UK, several argued that Brexit would affect growth negatively while contributing to inflation; while they expected that the BOE would continue to tighten, they felt there could be some painful choices facing monetary policy makers. Finally, participants felt that Japan was still at least a year away from beginning to execute an exit strategy, as inflation remained stubbornly low (albeit positive) despite tight labor conditions. Indeed, some questioned whether Japan would be able to exit at any point in the medium-term future. They argued that Japan continued to suffer from low investment demand and structural factors (including demography and automation) that would continue to contribute to deflationary tendencies in the economy.

There were also questions about the effects of exit. Despite the sense among many that the US was ready for exit and that the UK and Eurozone might well be soon, participants acknowledged that the impact on consumer confidence and investment demand were unpredictable, as established relationships between economic variables (e.g., the Phillips Curve) had become unstable. Several noted the recent speech by former Fed Governor Daniel Tarullo, on "monetary policy without a working theory of inflation," which argued that it had become ever more problematic for policy makers to rely on model-driven predictions of monetary policy effects. Thus, they called for monetary policy makers to be theoretically flexible and to focus on data rather than expectations.

While acknowledging the difficult of prediction, participants raised several scenarios for how quicker exit from quantitative easing in the US, Eurozone and UK could affect Japan. A number of participants argued that Japan was likely to face both currency depreciation (from which it stood to benefit in terms of both inflation and employment) and reduced demand growth in North America and Europe. A number of participants saw this as a likely positive for the Japanese economy. However, some warned that the beneficial effects of currency depreciation would not persist, and that a move by the BOJ to exit from its own quantitative easing in response to those effects could have a negative impact on Japan's growth prospects. Another issue that was raised was about the effect of simultaneous tightening by the US, ECB, and BOE on global demand. Several participants argued that monetary policy makers would need to keep a close eye on what their counterparts were doing in order to avoid accidentally slowing global demand in their efforts to contain potential inflationary forces.

A final issue with regard to timing of exit from

quantitative easing was coordination with fiscal policy. A number of participants raised concerns that monetary authorities might be entering into tightening cycles at the same time that political leaders and fiscal authorities were calling for fiscal consolidation (i.e., debt reduction) in many developed countries. While the US appeared to be moving in the opposite fiscal direction in the wake of the recently-passed budget authorization that allowed for an expansion of the fiscal deficit of up to $1.5 trillion through a major tax cut, many European countries were seen to be refocusing on fiscal consolidation. Several participants worried that the combination of tighter fiscal and monetary policy would choke off growth. A number of participants saw this as a challenge for Japan as well—they worried that, with the consumption tax hike set for 2019, a simultaneous exit at that time from quantitative easing could again derail growth. Participants also discussed the potential impacts of exiting quantitative easing on emerging economies, some of which had been negatively affected by the so-called "taper tantrum" in 2013 when inward capital flows reversed in response to expectations that the Fed would soon withdraw from its quantitative easing efforts. Despite the 2013 experience, few participants expressed concern that exit by the Fed, ECB, and/or BOE would lead to currency crises or dollar shortages in emerging markets. Most felt that markets had priced in that risk already and so would not respond in a panicked way. They also argued that the emerging economies were now better prepared for managing any outflows or deflationary pressures that might result when leading economies exited from quantitative easing. As some put it, the earlier taper tantrum had been useful in "inoculating" the emerging economies from a crisis resulting from exit.

Finally, there was the question of whether current valuations of assets were so high as to be considered bubbles that were ready to burst and create a new global financial crisis. Despite widespread media attention to the possibility that historically high equity and real estate prices in the US and other markets were an unsustainable asset bubble, most participants did not express much concern (although it was noted that similar dismissals were made before the financial crisis of 2008). They also argued that, on the basis of expected profits, interest rates, and tax policies, stock market prices were not out of line with historical standards, despite their high level. While there might well be corrections, participants did not expect sharp price drops of the sort associated with financial crises.

POTENTIAL CRISIS TRIGGERS

Participants also discussed other potential triggers for a new financial crisis: classic economic triggers such as macroeconomic policy errors and mispricing of risk, as well as triggers arising from politics, natural disaster, or technology.

Thanks largely to enhanced regulation and supervision since the global financial crisis, participants did not express concern about excessive risk-taking by financial institutions in the developed world—and even if there were a failure of a major financial institution, many felt confident that it would be contained thanks to stricter capital requirements and resolution procedures. Some participants also brought up the question of how Japan and other developed countries would manage their fiscal and pension obligations under conditions of aging economies and low growth potential. But the issue was not discussed at length, as

participants considered these to be long-run problems that were unlikely to spark a crisis in the short term.

There were, however, concerns expressed by a number of participants about the possibility of a debt-driven crisis in China. They pointed to the rapid build-up of debt across the Chinese economy (with excess debt amounting to up to 80-90% of Chinese GDP, according to some participants) at a time of slowing growth. It was argued that the growth of debt was driven in particular by three types of borrowing, the sustainability of each of which was questionable. One of these was real estate, where debt and prices continued to rise, possibly because of investors' reaching for yield as corporate profitability slowed. Moreover, due to efforts by the government to curtail real estate lending by banks, much of the recent rise in real estate lending was moving through an under-regulated shadow banking sector characterized by opaque lending and collateral standards, as well as nebulous relationships with banks that could lead to broader contagion. Participants also expressed concern about public debt in the form of borrowing by state-owned enterprises (SOEs) and local governments. They argued that many SOEs that were no longer cost-competitive, particularly in old-line manufacturing industries such as steel and cement, were being propped up by taking on more and more debt from state-owned banks that might never be paid back. Meanwhile, local governments with limited revenue bases were also increasing their borrowing.

Many participants agreed that the build-up of uneconomical debt, combined with an immature financial system, opaque shadow banking, and excessive optimism, looked like the classic ingredients for a financial crisis. However, there was disagreement as to whether a financial crisis was actually likely to occur and whether it could spread internationally. A number of participants argued that, despite the build-up of non-performing loans, a large-scale financial crisis in China was extremely unlikely, because the state would step in to bail out the (predominantly state-owned) banking system—and probably local governments as well—if things got bad enough. While such a strategy might create misallocation of credit, slower growth, and moral hazard, the resources of the Chinese government were seen as more than sufficient to socialize losses. Meanwhile, even those participants who considered a financial crisis to be likely generally did not expect that there would be global contagion, as the Chinese financial system remained relatively closed.

Turning from classic financial or economic causes of financial crises, participants discussed the challenges of geopolitics and even natural disasters (such as a devastating earthquake in Tokyo) as potential triggers for the next financial crisis. A number of participants expressed unease about what they saw as global financial markets' apparent insensitivity to these risks, which they considered to be rising. There was considerable discussion of dangers emanating from North Korea, due to what many participants saw as the regime's willingness to engage in brinkmanship and provocation as it developed its nuclear and missile programs. Participants speculated about the possibility of missile launches toward—or even the detonation of a North Korean nuclear device near—Japan or Guam, a US first strike on nuclear facilities, or miscalculation that could lead to a military conflict. Others worried that confrontation between China and

Japan in the East China Sea or between China and the US in the South China Sea could result in conflict between the US and China, in addition to a variety of other potentially disruptive political scenarios. It was argued that such conflicts could touch off a regional or global financial crisis through disruption of global commerce and supply chains.

Other participants worried less about the potential for international conflict than about the impact of populist political movements. They argued that populism, characterized by xenophobia, distrust of elites, and scapegoating, was becoming increasingly prominent in many countries in the aftermath of the global financial crisis. One concern was that the rise of populist movements on both the right and the left would make governance more difficult in democratic countries, and perhaps even threaten the legitimacy of democratic institutions. A more direct impact on the global economy could arise from policies that targeted foreign people or countries, such as protectionist measures on trade or investment. Some participants raised the concern that the Trump administration's hostility to international trade agreements and its intent to use protectionist measures to reduce bilateral trade deficits could disrupt the global trading system, with serious repercussions for the global financial system as well.

Perhaps the greatest concern among participants was the potential for technology-driven or technology-enabled disruptions that could spark a global financial crisis. One set of concerns was about how financial technologies themselves could create unanticipated vulnerabilities in markets. Some participants raised the possibility that algorithmic, machine learning, or artificial intelligence-based trading could lead to a run on a financial institution or a seizing up of market liquidity. Alternatively, new methods of risk management could have blind spots that would allow for accumulation or concentration of risk that regulators could not detect or prevent. A second set of concerns, which some participants considered potentially more dangerous, revolved around cybercrime and cyberattacks. In particular, it was argued that a state-sponsored cyberattack on key financial records or infrastructure (such as payment or settlement systems) could wreak havoc in contemporary financial systems. Several participants argued that North Korea had already engaged in a number of audacious cyberattacks, including the Wanna Cry virus and the Bangladesh Bank heist—and warned that in the event of conflict with the US, North Korea would likely unloose wide-ranging cyberattacks on the US, Japan, and/or South Korea. Participants agreed that it was important for financial institutions, regulators, trade repositories, and central banks to prioritize cybersecurity and redundant recordkeeping to minimize both the threat of cyberattack and cybercrime and the damage if they were to occur.

TRANSMISSION AND FINANCIAL MARKET DYNAMICS

In addition to spending considerable time discussing potential triggers for a financial crisis, participants also considered how financial stress in one jurisdiction or market sector could spread more broadly throughout national and global financial markets. Looking back at the global financial crisis, participants noted how the crisis had spread from US subprime housing loans to financial institutions and markets around the world, including

through channels such as repo markets, money markets, and commercial paper that had been considered extremely safe and liquid at the time. Thus, the question arose of what would be the major transmission channels for financial crisis in the post-crisis world.

Participants focused in particular on three types of transmission mechanisms: unregulated entities, market liquidity, and financial technology. One concern of many participants was that heavy regulation in some financial sectors (e.g., banking and insurance) was leading investors, lenders, and borrowers to shift their business to less regulated sectors and entities. The migration of risk from the banking system to shadow banking entities could allow for a build-up of risk (for example, in the form of direct lending portfolios or unhedged holdings of derivative products like credit default swaps) in the system that was not visible to regulators or other market participants. If those entities held less capital and lacked access to central bank lending, they could fail rapidly in a crisis.

The second transmission mechanism discussed was financial markets. The subprime crisis had demonstrated the dangers to financial systems of loss of liquidity in key short-term funding markets, such as repos and commercial paper, which had proved to be the key mechanism for contagion. While many participants agreed that post-crisis reforms had had positive effects on the stability of many financial institutions, some worried that those reforms had actually reduced market liquidity, with potentially serious consequences in the event of a crisis. One particular concern was that post-crisis banking regulations (particularly the Volcker Rule in the US, but also provisioning rules for banks) had led to the withdrawal of many traditional market makers. Without market makers, they argued, liquidity could dry up rapidly, leading to fire sales of assets under some circumstances. Other participants were less concerned about the banks' withdrawal from market making. They argued that that function was now being fulfilled by new actors, including asset managers and hedge funds, and that liquidity in most key financial markets remained high. This was a point of contention, with some participants countering that much of the apparent liquidity being measured from high frequency trading was in fact "phantom liquidity" that arose from spoofing and other trading practices. Some participants also argued that quantitative easing by central banks (particularly the BOJ) had left the stock of securities limited and their prices potentially much more volatile.

Finally, a number of participants pointed to what they described as potential "accelerators" of herd behavior and runs. One of these was the rapid rise of autonomous high-frequency trading systems based on algorithms, artificial intelligence, or machine learning. Another was the vast expansion of passive investors. While index funds and ETFs did not pose the same problem of rapid unwinding of positions that could lead to fire sales, some participants worried that the prevalence of passive investment would inevitably mean herd behavior and significant correlation risk.

RESPONDING TO CRISES

The final set of questions addressed in Session 2 revolved around whether governments around the world could be expected to effectively respond to the next financial crisis, whatever its causes or means of transmission. Both national and international responses were discussed.

Participants noted that national regulators had more tools at their disposal to deal with the failure of major financial institutions. In many countries, these included new authority to resolve failed financial institutions while maintaining them as going concerns and without going through full bankruptcy proceedings. For Japan and the US, which already had such authority, the development of resolution plans (single point of entry and living wills) for systemically important financial institutions created further assurance that a failure could be contained.

However, a number of participants raised serious questions about the ability of public authorities, particularly in the US, to respond to a new crisis. Primary among these was the weakening of the Federal Reserve's lender of last resort function under the Dodd-Frank Act. In particular, lending to non-banks was described as facing serious new restrictions, including the requirements that any Fed lending program to a non-bank include a broad program for which at least five institutions must be eligible, that details on any lending to non-banks be publicly disclosed almost immediately to congressional leaders, and that loans to non-banks must be approved by the Treasury. Given the very large role that non-banks continue to play in the US financial system and the fact that they are less tightly regulated than banks, these participants raised concerns that the failure of a non-bank could have systemic effects; however, the Fed might not be able to prevent contagion as it had in the subprime crisis, with potentially catastrophic results.

More generally, some participants questioned whether governments would have the political will—or in some countries, the fiscal capacity—to bail out systemically important financial institutions in order to head off a larger crisis. In all of these discussions, Japan was seen as a bright spot—indeed, a number of participants suggested that Japanese financial supervision, orderly liquidation authority, and BOJ lending authority offered a model to which other countries should aspire.

There was also some discussion of the international level. While there had been success in promoting global cooperation on regulatory standards, many participants remained nervous about the effectiveness of cross-border cooperation to resolve a major financial institution or to stem a broader financial crisis. Extending the discussion of the changing role of the US Federal Reserve, some participants questioned the Fed's continuing ability to act as international lender of last resort. While the Fed retained the ability to establish and activate swap lines with other central banks, these participants worried that it may be slow to use that ability early in a crisis, out of fear that populist backlash would lead Congress to curtail such action in the future. Finally, a number of participants noted that the global safety net had become more extensive and multi-layered than ever before. In addition to the International Monetary Fund, which had expanded both its access to funds and the variety and size of its facilities, they pointed to

the growth of regional liquidity arrangements (especially the $240 billion Chiang Mai Initiative Multilateralization (CMIM)) and of bilateral swap lines. Japan and China had been especially active in setting up bilateral swap lines, ensuring that countries in Southeast Asia would have ample access to liquidity in the face of a currency crisis. A lingering question was how the US government would respond to currency crises, given the suspicion of international bailouts that had been expressed by President Trump and some Treasury appointees. Would the US use its veto power over an IMF-led plan to manage a crisis? And, if it did so, how would other states and regions respond? In East Asia, for example, it was suggested that this might be an impetus for CMIM to decouple from the IMF, to which it was now functionally connected §

Session 3

Where is Financial Regulation Headed?

In Session 3, participants discussed financial regulation, including the progress of the post-crisis global financial regulatory agenda and its effects on national and global financial systems. Much of the discussion revolved around whether financial regulation and supervision were achieving the right balance between ensuring financial stability and supporting economic growth. They also considered some of the challenges and opportunities that fintech had created for financial regulation.

GLOBAL REGULATORY AGENDA: ACHIEVEMENTS AND UNINTENDED CONSEQUENCES

Many participants expressed hope that the elaboration and implementation of the post-crisis G20 agenda was finally coming to a close. With capital and liquidity rules, enhanced supervision of systemically important institutions, stress testing, and resolution plans mostly in place, banking regulation was seen as basically complete, as were regulations concerning derivatives trading and insurance, and macroprudential supervision. Participants agreed that this was a good time to evaluate the accomplishments of the new regulations, as well as to assess whether there were gaps, overlaps, or contradictions that remained.

While most participants agreed that regulatory reform had made the global financial system more stable compared to a decade before, many expressed concern that this stability had come at the cost of overregulation. Participants offered a variety of examples of what they considered to be overregulation in the US and Europe. (In contrast, there were few complaints about Japanese financial regulation—as noted in the discussion of the Tokyo financial market, most of the reticence for foreign financial institutions to enter or expand their Japanese operations had to do with other factors, such as taxes and slow economic growth.) In the US, participants noted that the Dodd-Frank Act had not only served to implement the G20 regulatory standards, but had "goldplated it," for example by adding higher capital requirements and imposing the Volcker Rule on banks, and by imposing its rules on derivatives trading in an extraterritorial manner. In the EU, participants offered examples such as Solvency II in insurance and rules on derivatives trading that went beyond the G20 standards.

There was some disagreement about whether particular rules or practices constituted "overregulation," but participants agreed that increases in costs of compliance had been substantial. In banking, some participants questioned whether it was necessary to have such strict standards for risk-based capital and liquidity and leverage. (There was particular unhappiness about the leverage ratio.) Meanwhile, some participants also expressed frustration at what they saw as the imposition of a bank model of regulation

to other financial sectors and instruments, including insurance, asset management, and money market funds. A number of participants complained that the Fed's implementation of stress testing was based on ambiguous standards and unjustified models, introducing excessive uncertainty and costs. There were similar concerns raised about the way in which living will resolution plans were reviewed and approved. Some questioned whether all the new regulations were worth it, pointing out that there had been little cost-benefit analysis in the production and implementation of the new regulations. While some participants felt that this was understandable given the urgency and complexity of post-crisis regulatory reform, there was a general feeling that it was now time to analyze empirically the effects of regulation on financial institutions, financial markets, and the real economy, with an eye to reducing unnecessary or overly costly regulations.

Participants also worried about variations in the implementation of the reform agenda among jurisdictions, leading to fragmentation and inefficiencies. There was a consensus that regulators in some jurisdictions—particularly the US and EU—had not taken seriously the need to coordinate standards, leading to the proliferation of overlapping or contradictory rules. Compliance with a complex web of requirements was seen as not only vastly increasing costs for multinational financial institutions, but also forcing them to reorganize their business structures and internal procedures in ways that could reduce internal coordination and require duplicative investments across multiple jurisdictions. Multinational banks were increasingly facing ring-fencing by regulators, preventing them from having global strategies for capital and liquidity management—and potentially preventing them from shifting needed capital or liquidity to a subsidiary or branch that might need it, which participants feared could make them more brittle. Meanwhile, the de-globalization of derivatives markets was seen as raising costs and reducing the ability of financial institutions and end-users to hedge—for example, some argued that MiFID II, whose purpose was partly to improve economic outcomes by increasing competition, might actually lead to higher spreads in securities and derivatives because of the lack of concentration of trading. While US and EU financial institutions were frustrated by the difficulty of doing business in each other's jurisdictions, it was noted that in many cases Japan's internationally-active financial institutions were doubly burdened by the need to comply not only with their home rules but also with those of both the US and EU.

Despite participants' frustration with costs and complexity of managing differing regulations and supervisory practices across borders, many participants did see some benefits to the variation. They argued that regulation (and especially supervision) should be adapted to local conditions, even though they should share common principles and standards as agreed in global regulatory bodies. It was noted that national financial systems varied significantly across a variety of dimensions, including reliance on banks vs. capital markets, usage and size of derivatives markets, concentration in particular financial sectors, and business models and complexity of financial institutions. Thus, participants reasoned, jurisdictions could be affected quite differently by identical regulations. For example, a number of participants noted that public authorities in the EU and Japan, where bank lending was much more important relative to other forms of

credit, had recently become much more eager than in the US to reduce obstacles to bank lending in order to promote economic growth. Thus, the question was how to respect the need to adapt to local conditions without making cross-border financial activity prohibitively complicated and expensive. A number of participants argued that this was possible, as long as national regulators were willing to accept the legitimacy of other countries regulatory regimes through mutual recognition or substituted compliance ("equivalence"). They encouraged regulators to move decisively in that direction.

Participants considered other unintended consequences of the post-crisis financial regulatory regime. A major one was the effect on competition. They noted that, despite ongoing concern about the problem of overconcentration in key financial services such as banking and insurance—epitomized by the label "too big to fail"—the effect of many of the new rules and policies of the post-crisis period had actually been to increase concentration. While one reason for increased concentration had been the mergers and acquisitions brought on by the failure of major financial institutions in the US and EU, many participants saw regulation as a major driver. They felt that regulations had the effect of both raising costs (the costs of legal compliance, increased capital requirements, higher costs of liquidity and hedging instruments, living wills, etc.) and reducing potential for revenue (through restrictions on some activities such as by the Volcker Rule), leverage rules, strict rules on risk-weighting, etc.). They saw this as squeezing profitability and thus creating significant incentives for consolidation. Moreover, the high cost of doing business in multiple jurisdictions was causing many financial institutions to sell off their marginal operations, which led to higher concentration within any given jurisdiction.

This point on concentration linked to a larger set of concerns about the effects of overregulation and regulatory overlap on the real economy more broadly. Many participants raised concerns about what they saw as the lack of financing opportunities for SMEs, which accounted for most employment, production, and growth in any economy. They argued that current rules on risk-weighted capital harmed SMEs because in many cases they required banks to hold much more capital against SME loans than against loans to more established, larger firms, and more capital than the riskiness of SME loans warranted. More broadly, many participants felt that the growth of bank loans—which constituted the bulk of credit in Japan, the EU, and many other countries—was slowed by capital requirements and other regulations that increased banks' cost of capital and reduced their profitability. Thus, some argued that loosening these rules would help to spur more economic growth.

Finally, some participants raised the concern that the current regulatory landscape might not have reduced risks to the extent that its designers had intended. In particular, they argued that strict bank regulations were shifting a great deal of financing away from banks toward alternative sources of finance. Moreover, because of risk-weighted capital rules, they argued that it was risky loans in particular that were shifting to less regulated financial institutions. Thus, they worried that the attempt to make the banking system safer might be leading to an invisible build-up of risks in shadow banking; depending on how those financial institutions got their financing,

this could lead to financial failures and perhaps contagion through the system. While the shift of financial activity away from bank lending was of concern to many participants, some hoped that financing might shift away from banks and public markets toward private equity. They argued that private equity offered many advantages, including stable funding and better-aligned incentives that could lead to better growth prospects for firms that accessed it.

Despite considerable concern about the extent, costs, and incompatibility of regulation within and across jurisdictions, some participants expressed optimism that the tide might be turning. They noted movements in some countries to rethink at least some regulation—particularly in the US under the Trump administration, but also to some extent in Japan and the EU. Some argued that there was a rising political tide in these jurisdictions that favored the pursuit of economic growth over financial stability and punishing financial institutions. Others were more cautious, arguing that resentment against "Wall Street" and the financial industry remained strong, particularly among the populist movements that had become increasingly prominent in the US and EU. (Japan was seen as an exception in this regard.) A number of them agreed that major extensions of regulation were unlikely in the near future, but argued that the political environment to roll back financial legislation was very unfavorable in most countries. In general, they felt that regulatory relief was much more likely to come from regulatory and supervisory agencies than from legislation—even in the US, where both Congress and the presidency were controlled by pro-business Republicans, albeit quite narrowly in the Senate.

CHALLENGES TO REGULATION AND SUPERVISION

Participants discussed at length the relationship between regulation and supervision. Many participants expressed frustration with what they saw as a "checklist" approach to oversight of the financial system. They argued that this approach overemphasized enforcement of detailed rules at the expense of the principles on which the rules were originally based. Moreover, the checklist approach was seen as focusing on the details rather than the larger picture—i.e., building a financial system that efficiently allocates capital and prices risk, prevents build-up of imbalances, and is resistant to economic, technological, or other shocks. It was important, they argued, for regulators and supervisors to adopt a more holistic and supportive approach.

Many participants cited with approval a 2016 speech by Japanese Financial Services Agency Commissioner Mori in which he called for a shift "from static regulation to dynamic supervision." They made two points. First, the rapidly changing nature of finance meant that rules that were devised at one point in time to apply agreed principles to a particular set of circumstances could easily become outdated, irrelevant, or even counterproductive over time. Thus, they argued that finance required a dynamic and flexible approach to governance. Second, they suggested that this required a shift in focus from regulation to supervision. While the terms have often been used interchangeably, participants made a clear distinction: they saw regulation as being about telling all financial institutions what they are and are not allowed to do, whereas supervision was an interactive process between particular financial institutions and supervisors, thus

allowing more flexibility.

Participants also made a distinction between enforcement and supervision. Many felt that fears of being accused of collusion with financial institutions had created incentives for regulators and supervisors to adopt an arm's-length, adversarial relationship toward financial institutions. While the supervisory function necessarily involved elements of enforcement, participants argued that enforcement and punishment should be reserved for cases in which financial institutions had willfully violated rules and endangered either their customers or financial markets. They felt that a supervisory approach that focused primarily on enforcement reflected a breakdown of trust and communication. If supervisors became purely enforcers, financial institutions would be less likely to communicate with them when problems arose (such as an inadvertent violation) that might best be worked out in a cooperative manner. Also, these participants argued, the process of communication was essential to making rules more responsive to changing conditions.

While many participants advocated a more two-way street in the supervisory relationship, in which supervisors supported development of the industry and financial industries sought to inform supervisors and regulators of challenges and all parties worked together to address those challenges, others were somewhat skeptical. They worried that cooperative relationships between financial institutions and supervisors could easily become too close, citing examples in Japan prior to the establishment of the FSA and in the US in the run-up to the subprime crisis. While agreeing that communication and constructive dialogue might be important to effective supervision, they felt that ultimately supervisors needed to be prepared to impose discipline in order to ensure fairness and financial stability.

There was also some discussion of the goals and methods of enforcement. Some participants expressed concern that few individuals in the US had been prosecuted for their contributions to the global financial crisis. They felt that holding financial institutions responsible for the actions of individuals was not a sufficient deterrent against future wrongdoing, and was also unfair to the shareholders who ultimately had to pay the fines for their wrongdoing. They argued that holding individuals responsible was far more likely to promote a culture of respect for the law within the financial sector. Some participants also commented that refocusing on individual responsibility could be politically meaningful; demonstrating to the public that wrongdoers were paying a price would add to the legitimacy of the regulatory system, and potentially provide political space for a more collaborative supervisory regime. Nonetheless, punishment of individuals required substantial due process, and often involved proof of intent of wrongdoing that was difficult to obtain. Another challenge that participants identified for regulation and supervision was cross-border cooperation. They pointed out that one goal of the G20 in putting together the post-crisis regulatory agenda had been the creation of a truly global system of regulation for internationally-active banks. However, as noted above, significant differences separated regulatory standards across many jurisdictions, particularly between the US and EU. This also created difficulties for supervision, particularly where specific rules or standards contradicted each other. In some important cases, such as derivatives clearing, US and European authorities had been able to negotiate

memorandums of understanding that allowed for US central clearing parties to qualify for EU clearing, and vice versa, based on a finding of regulatory equivalence. Participants considered this a practical approach, and urged supervisors to continue to follow it. But they expressed skepticism about the value of MOUs for handling failures of multinational financial institutions through resolution. A number of participants argued that the difficulty of enforcing such agreements helped to explain supervisors' increasing tendency to ringfence capital so as to ensure that local taxpayers would not find themselves paying for the failure of a foreign financial institution. Some participants suggested that regulatory reform had raised a new challenge for regulators and supervisors. They argued that the complexity and costs of expanded regulation had led many financial institutions to outsource an increasing number of functions—including, in some cases, core functions such as compliance and risk management, but it was unclear how to supervise or regulate the outsourced function. Although ultimately a financial institution was understood to be responsible for its lending and compliance with laws and regulation, there was a real question of whether existing supervisory bodies should also be supervising such service providers or at least the process by which a regulated financial institution managed and monitored its outsourcing relationships.

Finally, participants returned to a common theme of Symposium discussions, the need to ensure that regulators and supervisors had the capacity to do their jobs effectively in a rapidly changing environment. They called for governments to prioritize the hiring of capable individuals, as well as investing in ongoing training. They also noted that changes in financial markets, such as the rapidly transformations driven by information technology, called for expanding the scope of hiring and training beyond the traditional fields of law and economics to also include areas such as computer science and software engineering.

FINTECH AND INNOVATION

Participants discussed at length the impact of technological innovation on financial markets, institutions, and regulation.
There was considerable excitement about the potential for fintech and regtech to improve the functioning of financial systems. For example, participants noted that financial institutions had been experimenting with blockchain-style distributed ledgers as a way of reducing costs, ensuring accuracy, and improving resiliency for a variety of recordkeeping functions, including for trading. Big Data and new data mining and machine learning techniques also were seen as promising as a means of improving customer service, better gauging risk through behavioral credit ratings, offering new trading strategies, and perhaps offering lower-cost, more efficient anti-money laundering (AML) enforcement. Cloud storage could not only reduce costs of data storage, but also make financial institutions' records less geographically concentrated and thus more resilient.

At the same time, participants realized that new technologies offered many new challenges as well. One of these was data privacy. A number of participants pointed out that much of the promise of Big Data relied on obtaining and using large amounts of personal data, and that many people and governments were increasingly wary of giving firms and financial

institutions carte blanche in that regard. They urged financial institutions to work with regulators in defining responsible use and protection of personal data. Differences in data privacy standards across jurisdictions added to the complexity. Data protection was also understood to be a major issue, whether in the form of cybercrime or attacks by state actors. Participants expressed concern that continually increasing reliance on complex IT systems with multiple entry points was making financial institutions and markets more vulnerable to theft, destruction or alteration of data, and stoppages of key services. They worried that even technologies that could improve resilience, like cloud storage, might also make financial data more vulnerable to determined hackers.

Many participants also worried that new technologies could contribute to build-up of risk within the system, as well as new forms of contagion. Two issues in particular were highlighted. First, some participants noted that technological shifts and unfamiliar financial products had often been associated with bubbles, as investors and financial institutions had too much confidence in their understanding of how they managed or distributed risk. In this regard, some participants drew an analogy to the way that credit rating agencies' reliance on historical data had blinded them to new risks in subprime loans and CDOs. Second, many participants worried about the prospect of herd behavior by autonomous trading systems, which could lead to runs, fire sales, and freezing of liquidity in a variety of markets. Participants agreed that these issues raised significant new challenges for regulators. In some cases, they felt that regulations that were developed to oversee conventional financial institutions would be obsolete. Meanwhile, new actors would arise that did not fit neatly into existing categories. For example, if social media firms were facilitating digital financial transfers, how could they be incorporated into existing financial regulation? A different issue arose with autonomous trading systems. Participants asked who should be held legally responsible for legal violations or vulnerabilities created by the software itself (which in some cases might be adaptive, and thus out of the hands even of programmers) rather than by the users. To get a better sense of the risks of various new technologies and business models, a number of participants advocated a "sandbox" approach that would encourage innovation while also limiting or quarantining risk. Participants also agreed that the challenges called for much more proactive efforts by regulatory agencies to build their capacity; this was seen to be a particular challenge for emerging markets, and a number of participants called for enhanced information sharing and technical assistance among regulators and supervisors to help emerging markets deal with it §

Session 4

What We Have Learned Since Our First Symposium in Cape Cod in the Summer of 1998

In Session 4, participants reflected on the two past decades of the Japan-US Symposium. They discussed the many ways in which Japanese and US financial systems had changed as a result of crisis, reform, and innovation over that period. A number of participants noted that in the early years Japan was seen by many Americans to have much to learn from the US, but over time the dialogue had become much more of a two-way street. Overall, participants expressed considerable appreciation for the role of the Symposium series in fostering high-quality dialogue and mutual trust among policymakers and financial professionals in the two countries.

ORIGINS

Participants from the earliest Symposiums discussed the origins of the series. At the time of the first Symposium, in 1998, the Japanese economy was facing serious problems including a full-blown banking crisis and the Asian Financial Crisis. The US, meanwhile, was in the midst of rapid economic growth, improving fiscal position, and the dot.com boom, although US participants had their own recent memories of financial fragility in the form of the savings and loan crisis. That Symposium brought together a group of people who wanted to find solutions to Japan's challenges, including some participants who had had important roles in the resolution of the S&L crisis. Conversations at the 1998 Symposium were seen by a number of participants as having contributed to the implementation of some of the major changes introduced in Japan that year, including bank nationalizations and recapitalizations.

The early years of the Symposium focused on problems in the Japanese financial system rather than giving equal time to issues in the US. Some participants felt that this was not surprising: Japan was facing the daunting challenges of working its way out of a post-bubble financial crisis that had led to the failures of several major banks and insurance companies, continued stagnation in its stock market, and concerns about the effects and sustainability of fiscal and monetary stimulus. At the same time, it was implementing an ambitious restructuring of financial regulation in the form of the Big Bang and the establishment of the Financial Supervision Agency (later, Financial Services Agency). Soon, however, significant challenges hit the US financial system, including the bursting of the dot.com bubble and the Enron scandal, which sparked major changes in accounting and auditing practices under the Sarbanes-Oxley Act. Nonetheless, a number of participants felt that, until 2008, most of the energy of the Symposium was focused on how to improve the Japanese financial system—sometimes in the form of complaints by US officials and financial institutions, but often also in conjunction with Japanese policy makers who envisioned a more open, market-based, and efficient system.

After 2008, the Symposium had spent considerably more time on issues related to the US financial system and the G20 global financial regulatory agenda. Participants noted

that the Japanese financial system had been one of the world's most resilient in the face of the global financial crisis, whereas the US and UK—which were previously seen as models of financial regulation and supervision—were at the epicenter of the global crisis. As a result, there was newfound interest among US participants in how Japanese authorities had managed systemic risk. After 2008, there was also renewed attention to macroeconomic issues on both sides of the Pacific—quantitative easing in particular, but also fiscal and pension sustainability. Along the way, a variety of challenges had arisen that Japan and the US had to navigate together, including implementation of the G20 agenda, sovereign debt crises in Greece and other EU countries, the rise of the Chinese economy, exit strategies for quantitative easing, Brexit, and the rise of a new global populism.

MUTUAL DIALOGUE

Participants agreed that the Symposium series had benefited from bringing together insights from government, academia, and business. By attending in their individual rather than professional capacities and encountering a variety of practitioners and observers, they agreed that participants had been able to discuss issues from a variety of perspectives, allowing for more open and disinterested discussions. It was also an opportunity for non-confrontational discussions between US and Japanese governments, which proved to be a useful tool for reformers in Japan. Several argued that the Symposium series served an important role in helping Japan to find solutions to its financial crisis.
While the success of the early dialogues laid the groundwork for the Symposium to become an important annual event, a number of participants described the initial tone and agendas in the early years as having been skewed toward lecturing to Japan by the US side. After the advent of the subprime crisis in 2008, a number of participants observed much greater equality and mutuality. In the early years, cultural and language differences (proceedings were always entirely in English) may have made the Japanese participants unwilling to speak out. But this reluctance was overcome through a significant continuity in the identity of and trust among participants.

Over time, many participants crossed national and organizational lines to create enduring friendships. Several participants complimented the Japan steering committee for having played a critical role in identifying the right people to participate and to define the agenda each year.

LESSONS AND CHANGE OVER TIME

The past two decades had seen extraordinary changes in the financial systems and economies of both Japan and the US. These were reflected in changes in both the themes and membership of the Symposiums.
Some participants were particularly struck by changes in the Japanese side. In 1998, they argued, internationalists were still relatively marginal in many Japanese financial institutions and regulatory bodies. While they had considerable expertise in their fields, most of the decision makers in Japanese banks, the Ministry of Finance, and the Bank of Japan were men who had risen through the domestic ranks. Two decades later, it was

evident that there had been a "mainstreaming" of English-speaking professionals with extensive international expertise who were taking leadership roles in core functions rather than just serving as intermediaries to deal with international audiences. This was symbolized by the success of internationalists in reaching the top positions even in organizations that had previously been seen as highly traditional and domestically oriented, such as the Tokyo Stock Exchange, FSA, and even major commercial banks. While some participants felt that Japan had a ways to go in internationalizing its financial sector and business world, it was agreed that there had been significant change in that regard.

The US side had seen more limited change, with the core participants having consistently been "Japan hands" and people doing business in Japan. However, there was a period in the early 2000s when there was an infusion of new investors in Japan, as private equity firms purchased distressed assets and financial institutions. Some of these investors participated in the Symposium in those years, bringing new insights and concerns about issues like corporate governance that had not been in the initial agendas. Over time, however, many of those participants drifted away from a focus on Japan.

Several participants observed that when the Symposium began, Japanese and US participants were not just representing different governments or financial institutions, but in many cases different worldviews as well. Over time, it was noted that there had been increasing convergence over core principles, like the responsibilities of managers and shareholders and the role of markets. It was suggested that this reflected in part the internationalization of the Japanese financial system already noted, and the increasing role of US- and UK-trained officials and financial practitioners. A number of participants saw the changed worldview increasingly being reflected across the Japanese economy. Corporate governance was one example. Also, many felt that the ongoing dialogue had contributed to the development of a very different regulatory mindset that valued innovation and efficiency among financial institutions and markets, as well as the development of a supervisory style that supported the development of the financial sector while also ensuring prudent business practices.

Looking back over two decades of profound financial challenges and crises, some participants drew what they saw as enduring lessons that had been reinforced through the Symposium dialogue. One of these was that financial crises were not the province only of emerging economies, but could also arise in developed economies with sophisticated financial systems. The participants observed that the specific origins of crises varied significantly, but the underlying causes could nearly always be found in bad lending and bad governance. Thus, improving risk assessment and risk management should always be a key focus of regulators and financial institutions. Another lesson that some participants drew from the first two decades of the Symposium was the essential role of public authorities in backstopping economies in the midst of financial crises. The Japanese government had prevented runs on the banking system by offering unlimited deposit insurance and by recapitalizing weak banks. The US had also backstopped the financial system with recapitalization through TARP, but also—

because the US crisis was contagion-driven—vigorous use of the lender of last resort function. It was argued that one of the lessons from both Japan and the US was that in a financial crisis, public support of the financial system was an essential element of protecting the economy as a whole. Still, Symposium discussions over the years had made clear that this support had important costs, including moral hazard and political backlash.

Several participants argued that the effectiveness of the US response to the subprime crisis and Lehman failure could be partially attributed to the previous decade of discussions in the Symposium. Some of the key actors on the US side had participated in Symposiums and had gained direct insight from the Japanese participants about issues ranging from recapitalization to non-performing loan disposal to quantitative easing §

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