

Opening Statement of Chairman Evan Bayh
Subcommittee on Security, International Trade and Finance
Hearing on “Equipping Financial Regulators with the Tools Necessary to Monitor Systemic Risk”
February 12, 2010

PRE-OPENING REMARKS

Good morning. I am pleased to call to order this Subcommittee for a hearing entitled “Equipping Financial Regulators with the Tools Necessary to Monitor Systemic Risk.” I want to thank the Ranking Member, Senator Corker, and his staff, for requesting this hearing on an issue that may seem technical to some, but will prove critical as we work to reform and modernize our regulatory structure for the future.

I would also like to welcome and thank Senator Jack Reed. He has been instrumental on the technical and analytic aspects of systemic risk regulation, specifically on the proposal of a National Institute of Finance. I am happy to continue the dialogue he has already begun on how we equip our regulators to move beyond examining individual institutions and towards monitoring and managing systemic risk across our financial system.

To our witnesses that will appear on two separate panels, welcome and thank you for appearing before the subcommittee to give an outline on regulators’ current capabilities to collect and analyze financial market data; and most importantly, what additional resources and capabilities are necessary to provide effective systemic risk regulation. I understand that the weather in Washington the last few days has not been ideal, so I appreciate the dedication you have all show in making it here today.

Before we turn to Governor Tarullo, I would like to make a few remarks on why this issue is essential to the safety and soundness of our financial system moving forward.

OPENING STATEMENT

Over a year ago, our country experienced a financial crisis that exposed the complexity and interconnectedness of our financial system and markets. The globalization of financial services and the increasing size and intricacy of major market players enabled the build up and transferring of risk that was not fully recognized or understood by our regulators, or, in some cases, by the institutions themselves. These vulnerabilities made it clear to policymakers here in Washington that our financial system, as whole, needs its own overseer. As a result, systemic risk regulation has become a central part of our efforts to modernize our financial regulatory system.

Creating a new regulatory structure to monitor systemic risk is no easy task. My colleagues here in the Banking Committee, including Chairman Dodd, Senators Corker, Reed and Warner have been working diligently to determine what tools and technical capabilities may be necessary for the regulation of systemic financial risk. To that end, the National Research Council held a workshop in November at the request of Senator Reed to identify the major technical challenges to building that capacity. While it is clear that our regulatory system currently lacks the technical resources to monitor and manage risk with sufficient sophistication and comprehensiveness, we should figure out what capabilities our regulators currently have. That involves assessing what data and analytical tools are currently available to

regulators to collect real-time, consistent market data. We have Governor Tarullo here to discuss what data and analytical methodologies prudential regulators currently have in place to see real-time financial market data and how our current financial regulators collaborate in aggregating and analyzing data.

Next, we can focus on the biggest challenge of this exercise—determining what further capabilities are necessary, as well as identifying the barriers and challenges to meeting the goals of systemic risk regulation. This involves much more than aggregating information, but making sure we are filling the information gaps, asking the right questions, and putting that information into the broader context of the risk dynamics in the system. Currently, risk analysis has developed solely to manage firm-specific risks. That approach needs to evolve beyond the individual institution, and work to include the complex interaction and linkages amongst the system to assemble a holistic perspective.

In debating the capabilities needed, the next obvious question centers on developing the right infrastructure for the enhanced data aggregation, mathematical modeling and all the other issues that go into systemic risk regulation.

An idea that has the support of six Nobel Laureates, including Professor Engle who is on our second panel this afternoon, is the creation of a National Institute of Finance. Supported by the Committee to Establish the National Institute of Finance, this proposal urges the creation of an independent institute to collect and standardize the reporting of financial market data, as well as develop tools for measuring and monitoring systemic risk. On February 4th, my colleague Senator Reed introduced legislation to create such an institute. We have some of the founders of that Committee with us today to outline what they envision in the creation of an independent NIF.

I am also open to other ideas, including whether or not a separate additional agency is necessary or if these new technical capabilities can be housed in an existing independent federal agency, such as the Federal Reserve. I look forward to hearing our witnesses' perspective on this issue, as well.

Lastly, in a discussion on systemic risk and data aggregation, we would be remiss to ignore the international implications to our domestic systemic risk regulation. As I've said before, we live in an interconnected global economy, and as we've seen, that means interconnected global problems. Vulnerabilities and gaps in financial markets abroad, can impact us here at home. A key element of this discussion should focus on how we encourage global financial market reporting, aggregating and analytic capabilities, as well as identifying any legal or legislative barriers to international data sharing.

Ultimately, all of us here know our country cannot afford another financial crisis that will have a devastating impact on household wealth, unemployment and our economy, at large. While seemingly technical in nature, these issues are critical to our national interest and necessary to strengthen and provide credibility to our financial system. I look forward to working with my colleagues to ensure these issues are addressed in our comprehensive regulatory reform bill.