Statement by
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Secretary
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before the
Committee on Banking, Housing, and Urban Affairs
United States Senate
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Thank you, Chairman Brown, Ranking Member Toomey, and Members of the Committee. I am pleased to speak with you today about the Financial Stability Oversight Council’s (Council) 2021 annual report. The report is a collaborative effort of the Council member agencies. It is a vehicle for providing Congress and the public with the Council’s collective assessments of potential risks to U.S. financial stability. Today, I will highlight a few topics in the report and provide an update on the Council’s activities since the report’s publication.

First, the report discusses vulnerabilities in the nonbank financial sector, which were highlighted by the turmoil in financial markets in March 2020. While the Dodd-Frank Act reforms increased the resiliency of the U.S. financial system, the market turmoil in March 2020 demonstrated that the liquidity mismatch and use of leverage by some nonbank financial institutions can make them vulnerable to acute financial stresses, and these stresses can be transmitted and amplified to the broader financial system. The Council has taken steps to examine these risks, including re-establishing its Hedge Fund Working Group to develop an interagency risk-monitoring system and to propose options to mitigate identified risks. And earlier this year, the Council issued a statement to express support for the Securities and Exchange Commission’s (SEC) efforts to reform money market funds and their work to consider potential reforms of open-end funds.

The Council is also working to support improving the resilience of the Treasury market and is coordinating with the Interagency Working Group on Treasury Market Surveillance (IAWG). Potential steps to be taken include improving data quality and availability, evaluating expanded central clearing, and enhancing trading venue transparency and oversight. The SEC has proposed certain reforms to enhance transparency and oversight over alternative trading systems that trade government securities. The SEC has also proposed updating the definition of a government securities dealer to include market participants that play an increasingly significant liquidity providing role in overall trading and market activity. Additionally, the Office of Financial Research is working to fill identified data gaps for uncleared bilateral repurchase agreements through a pilot data collection, which should improve visibility into a major source of financing for non-bank financial institutions in Treasury markets.

Additionally, the Council is working to ensure that financial institutions better understand their climate-related financial risks. In its October 2021 Report on Climate-Related Financial Risk, the Council outlined how climate change can be a source of shocks to the financial system and increase risks to financial stability. To address these risks, the Council recommended that regulators build their capacity and expand their efforts to address climate-related risks, improve the availability of data, enhance and standardize disclosures, and assess and mitigate risks to financial stability. The Council has also formed its staff-level Climate-related Financial Risk Committee, which will serve as a coordinating body for the Council to share information, facilitate the development of common approaches and standards, and foster communication across FSOC members. In addition, the Council is establishing the Climate-related Financial Risk Advisory Committee. This advisory body, which will include a broad array of external stakeholders, will help the Council gather information and analysis on climate-related financial risks.

With respect to digital assets, new products and technologies may present opportunities to promote innovation and increase efficiencies. However, digital assets may pose risks to the
financial system, and increased and coordinated regulatory attention is necessary. On March 9, 2022, President Biden signed an Executive Order calling for comprehensive approach to digital asset policy. The Council is drafting a report that will identify financial stability risks and regulatory gaps. I look forward to working with you on the issues and opportunities posed by digital assets. We are also eager to work with you to ensure that payment stablecoins and their arrangements are subject to a federal prudential framework on a consistent and comprehensive basis.

Finally, there is the potential for continued volatility and unevenness of global growth as countries continue to grapple with the pandemic. Russia’s unprovoked invasion of Ukraine has further increased economic uncertainty. The U.S. financial system has continued to function in an orderly manner, though valuations of some assets remain high compared with historical values. We stand firmly with the people of Ukraine and have implemented an unprecedented suite of sanctions on Russia that have been implemented by financial institutions. On February 28, I convened the Council in the wake of the invasion, and we will continue to monitor developments and coordinate actions as the risks and threats evolve.

The Council’s report also discusses other potential emerging threats and vulnerabilities that the Council continues to monitor, including short-term wholesale funding markets, central counterparties, alternative reference rates, cybersecurity, corporate credit markets, and real estate markets.

The Council remains committed to its mission of identifying and responding to risks to U.S. financial stability, and I look forward to working with this Committee to promote a more robust and resilient financial system. Thank you.