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The Financial Stability Board: Beyond the Fog of Battle

Remarks by

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Thank you for the opportunity to join you. I am grateful for the chance to speak with such a diverse and distinguished group of academics, industry leaders, and colleagues in regulation and central banking. Conversations like these always remind me that, while we all approach our roles in the financial sector differently, we share a deeper commitment to a common goal: a safe, stable, and resilient financial system, capable of supporting strong and sustainable economic growth.

A decade ago, that common goal became an imperative. The financial regulatory community worked frantically to repair the vulnerabilities that the global financial crisis exposed and to address a set of financial risks that failed to respect national borders. The financial system we have today bears the imprint of our response a decade ago. Basel III is now final. Derivatives markets are now safer and better regulated. Levels of capital and liquidity at the largest banks are now higher, and with reforms to recovery and resolution, the risks and potential costs of a catastrophic failure of a major institution are lower. These are profound accomplishments of international cooperation, which returned the global financial system from the brink of collapse to stability and health. But health does not make cooperation or vigilance any less necessary. On the contrary, as the G20 leaders said in creating the Financial Stability Board (FSB), “a sense of normalcy should not lead to complacency.”<sup>1</sup>

The FSB exists to help sustain the common efforts made in the throes of the crisis--to identify and address systemic vulnerabilities, to develop stronger regulatory and supervisory policies, and to create a more resilient global financial system. It is a platform, and a place for its 24 members and 73 representatives to coordinate their work; to identify and address issues that span financial products, intermediaries, and markets; and to avoid the pre-crisis regulatory

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<sup>1</sup> Leaders’ Statement, The Pittsburgh Summit (G20), September 24–25, 2009, [https://www.treasury.gov/resource-center/international/g7-g20/Documents/pittsburgh\\_summit\\_leaders\\_statement\\_250909.pdf](https://www.treasury.gov/resource-center/international/g7-g20/Documents/pittsburgh_summit_leaders_statement_250909.pdf).

fragmentation that left financial stability risks unaddressed. The relevance of this platform, to its members and to a changing financial system, is critical to preserving our last 10 years of hard-earned gains.

Today, I want to briefly outline three tenets that I believe are essential to preserving the relevance and vitality of the FSB: engagement, vigilance, and analysis. These principles, which I discussed more fully in remarks last week, underlie the most successful elements of the post-crisis reforms.<sup>2</sup> They should remain the foundation of the FSB's work, as we turn from drafting new standards to implementing them and devote more time and attention to the emerging vulnerabilities.

### **Engagement**

Regulatory cooperation has long been essential to financial stability--not only because it fosters consistency in global rules, but also because it fosters trust. When authorities develop new policy together, when they identify common standards and implement them in their home countries, and when they plan and debate the nature of emerging risks, they also develop a common understanding of each other's work and a common approach to addressing new problems.

However, trust among regulators means little on its own. It must come with the trust of the constituencies regulators serve, and the trust of those whom our decisions affect. The FSB is a conduit for this trust, as it is accountable to the G20 and to the nations and people the G20 leaders represent. We have an obligation to make the most of that conduit, by engaging in genuine, substantive dialogue with a wide range of stakeholders, to a greater and more effective

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<sup>2</sup> Randal K. Quarles, "The Financial Stability Board in 2019" (speech at the Joint Conference of the European Central Bank and the Journal of Money, Credit, and Banking, Frankfurt, Germany, March 28, 2019), <https://www.federalreserve.gov/newsevents/speech/quarles20190328a.htm>.

degree than in the past. We should invite reflection on the design and impact of our efforts, solicit input on risks to financial stability, and better communicate our mission and activities to the public, without the veneer of technical jargon.

The FSB can begin this work at home, by strengthening the role of the regional groups that are already part of the organization. In 2011, the FSB established six consultative groups representing large regions of the globe. The intent was to expand our outreach beyond the membership of the G20 and to better reflect the FSB's global mission and impact. Today, the groups meet once or twice a year and help the FSB obtain broader input into its policy development agenda. They can, and should, have the opportunity to do more--not only to promote implementation of international policy initiatives but also to give a clear view of financial stability developments in their respective regions. A study of the groups' operations is now underway, which will shed light on how to upgrade their effectiveness as an outreach and feedback mechanism.

We can also engage more effectively outside the FSB--with businesses, public institutions, market participants, and scholars--and give the public the means and the opportunity to provide meaningful feedback on our work. Some steps are already underway. We established a new expectation that all FSB policy recommendations will be open for at least 60 days of public comment, instead of the shorter periods used in the past. We began a recent effort around the differences in regulatory environments and market conditions across jurisdictions--known as "market fragmentation"--by convening key stakeholders and academics for a full-day workshop, which I hope will be the rule for future projects, not the exception. Earlier this year, we released publicly the FSB work program for the first time.<sup>3</sup>

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<sup>3</sup> See <http://www.fsb.org/2019/02/fsb-work-programme-for-2019/>.

This broad engagement is essential to understanding new developments that are relevant to financial stability. Take, for example, the “fintech” trends I discussed in remarks last week, to which the FSB is dedicating significant attention. Claims about fintech run the gamut from the utopian to the apocalyptic--yet the mantle of fintech covers a wide range of new business models, products, and trends. Their contours and their impact also vary across national boundaries, from mobile wallets in Kenya, to online mortgages in the United States, to money market funds founded by technology companies in China. Understanding one of these new uses of technology is not the same as understanding all of them. Identifying the risks and opportunities they pose requires context, information, and insight that can only come from a variety of stakeholders with experience developing, using, and monitoring them.

I will continue to seek ways to invite and encourage engagement during my chairmanship, and to give the public a clearer and fuller view of FSB’s decisionmaking process. Few efforts are closer to the heart of our collective work or to the accountability and trust that the FSB helps foster.

## **Vigilance**

Trust and accountability are also prerequisites for the FSB to pursue its mission. The first prong of our mandate, now a decade old, is to “assess vulnerabilities affecting the global financial system, and identify and review . . . the regulatory, supervisory, and related actions needed to address them . . . .”<sup>4</sup> The FSB’s primary role, and its principal contribution to international financial regulation, is to look forward--to see past the issues and practices of the day, and identify new vulnerabilities, long before they lead to widespread economic distress.

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<sup>4</sup> “Financial Stability Board Charter,” April 2, 2009, [http://www.fsb.org/wp-content/uploads/r\\_090925d.pdf](http://www.fsb.org/wp-content/uploads/r_090925d.pdf).

The FSB's Standing Committee on Assessment of Vulnerabilities (under the leadership of FSB Vice Chair Klaas Knot of De Nederlandsche Bank, here today) is an important forum and catalyst for this work. In the months ahead, the committee will develop a new framework for the identification and assessment of financial vulnerabilities. Their efforts will rely on transparent engagement with a wide range of stakeholders--including banks and nonbank financial institutions, the academic community, financial regulators, national authorities, and standard-setting bodies. This kind of broad outreach is essential. The causes of financial crises rarely announce themselves ahead of time, and only a wide range of views can give us the perspective and understanding to address them in advance. The right model for this work is not a small team of detectives--it is a search party.

The FSB's efforts on nonbank financial intermediation, which I discussed last week, reflect a similar approach. Nonbank financing has grown since the financial crisis, and it has been a source of systemic risk, often involving high leverage, maturity and liquidity mismatches, opaque structures, and concentrated holdings of risky assets. Nonbank financing can also lead to lower lending standards, bidding up the price of risky assets and sending an encouraging signal to credit underwriters. These channels played a role in the recent global financial crisis, and more recently, new forms of interconnectedness between nonbank financial firms and the banking system have emerged. In some scenarios, both domestically and internationally, such ties could amplify risks.

These developments raise important issues. Is the growth of nonbank financing altering existing market structures? Are there new vulnerabilities in the financial system? How will nonbank financing develop, and how should it do so? The FSB is taking a variety of complementary approaches to answering these questions.

First, we produce an annual report that outlines the developments in nonbank financing, detailing global trends and potential risks and providing reliable information to foster public discussion. Second, the FSB develops policies to promote the resilience of these firms (without impeding the growth of sustainable nonbank financing models), and we work closely with other multinational organizations to monitor implementation. Finally, and going forward, we must begin analyzing the effectiveness of the policies on nonbank financing that have been implemented.

### **Analysis**

The same spirit of self-reflection should guide the FSB's efforts in other policy areas. Stakeholders trust the FSB to undertake thoughtful, detailed work on emerging risks to financial stability. Yet identifying those risks before a crisis means dealing in uncertainty, and making policy on evolving issues, where no one can claim complete expertise. To maintain that trust, we must be willing to make improvements when the evidence justifies it--to undertake rigorous analysis, before and after issuing new standards, and to follow that analysis where it leads.

Many post-crisis policies, including those aimed at the implicit subsidy for "too-big-to-fail" institutions, have been in place long enough to allow for evaluation. We can now begin to ask fundamental, critical questions: What have the effects of these reforms been, whether intended or unintended, salutary or adverse? Have we successfully reduced or eliminated the problem? Has there been a tradeoff, in the form of new, unintended risks or costs?

As I have described elsewhere, the FSB is launching a global study with multinational policymakers to start answering these important questions as part of its broader effort to evaluate the effects of post-crisis reforms. We intend to bring analytical rigor to these questions, and we recognize that the academic community has undertaken much work in this area. As a result, we

will draw extensively on academic advisors during all phases of the work we are undertaking. I also encourage other experts in this field to look closely to the consultative document that will be coming from the study next year. We welcome the input as we undertake the study of this signature issue from the crisis.

The task of this project, like the task of the FSB itself, is to foster insight on the road ahead. The work of the FSB reflects the fact that, in a global financial system, we cannot see and address emerging problems alone. Working as allies and colleagues, we have bound up most of the wounds from the last financial crisis. To avoid reopening them--and returning to a fragmented international regime--we will have to recommit to collaboration, embrace insight where it emerges, and follow evidence where it leads. With broad engagement, rigorous vigilance, and committed analysis, the risks ahead of us can be less dangerous than the ones we left behind.