FSB FINANCIAL STABILITY BOARD

THE CHAIR

25 October 2021

To G20 Leaders

The Rome Summit is taking place amid signs of the global economy recovering from the impact of COVID-19 and related containment measures (the COVID Event). At the same time, the global financial system confronts significant structural challenges. These include rapid technological innovations within the traditional financial sector as well as outside, such as in the form of various crypto-assets. They also include a growing focus on potential risks to financial stability from climate change, whether from severe weather events or from uncertainties related to policy actions by governments.

During the Italian G20 Presidency, the Financial Stability Board (FSB) has continued to support policymakers in preserving financial stability during the COVID Event and laying the foundation for a more efficient and resilient financial system in the future. We have done so in two key ways. First, by setting out lessons for financial stability made apparent by the COVID Event, which define a path forward for the G20 on financial stability policy. Second, by coordinating international work on key structural issues, not least through the FSB roadmap to address climate-related financial risks and by taking forward the roadmap to enhance cross-border payments.

Lessons from the COVID-Event for global cooperation on financial stability

One key lesson from the COVID Event is that international cooperation through the G20 has made an important contribution to global financial stability. The financial reforms that the G20 agreed to after the 2008 financial crisis put the global financial system in a more resilient state entering the COVID Event than it had been in 2008. Those parts of the system where implementation is most advanced – banks and financial market infrastructures – displayed greater resilience and were able to cushion, rather than amplify, the shock of the COVID Event. More generally, established international cooperation through the FSB and other mechanisms helped to support the swift and broad-based policy response taken by our member authorities and was critical for containing the economic and financial fallout of the COVID Event.

Making a difference for global financial stability requires stamina. This means completing the job we began a decade ago by implementing any remaining post-2008 reforms without delay. It also includes ensuring that reforms are working as intended and being ready to adjust in response to unintended consequences. Indeed, our report on *Lessons learnt from the COVID-19 pandemic from a financial stability perspective* identifies areas that warrant further consideration at the international level. These include the functioning of capital and liquidity buffers and factors that may give rise to excessive procyclicality in the financial system.

The COVID Event has served as a reminder that financial stability calls for a system-wide perspective. Not all sectors displayed the same strengths, and shortcomings in one sector can

have harmful spillover effects in others. Short-term funding markets, in particular, experienced acute stress in March 2020. The FSB has been working to address weaknesses in certain sectors of non-bank financial intermediation (NBFI) that were brought into sharper focus during this time. The recently published *Policy proposals to enhance money market fund resilience* is the first in a body of work that aims to address the vulnerabilities identified in our *Holistic Review of the March 2020 Market Turmoil*. Our report on *Enhancing the resilience of non-bank financial intermediation* presents the progress we have made this year in assessing and addressing vulnerabilities in specific NBFI areas, including on liquidity risk in open-ended funds and the dynamics of margin calls. The FSB will continue to deepen our understanding of NBFI-related issues to develop a systemic risk perspective that can better inform the design and use of appropriate policy tools. Importantly, the progress report sets forth a work program that reflects the years of sustained commitment and international coordination that are required to effectively address vulnerabilities.

Finally, we also drew important lessons regarding operational resilience, cyber threats, and third-party relationships, among other issues. More specifically, the COVID Event highlighted the importance of having operational risk management arrangements in place well in advance of any shock. The extended remote work environments also raised concerns about cyber risks, particularly in an environment of greater reliance on outsourcing and third-party service providers. We are cooperating to address these risks.

Harnessing the benefits of technology while containing its risks

The COVID Event gave a boost to the use of digital financial services, in particular various forms of digital payments. Growth in this area reinforces the need to assess the financial stability implications of financial innovation, particularly innovation with a technological component. We should also ensure that supervisory and regulatory frameworks and approaches provide a solid foundation for harnessing the benefits of such innovation while containing their risks.

Crypto-assets in their various forms raise particular challenges. The markets for such assets have evolved rapidly over the past year. With market capitalization for crypto assets rising and links to the rest of the financial system growing, the FSB will continue to closely monitor these markets and their implications for financial stability. Our review this year demonstrated that several jurisdictions have been analyzing and updating their legal and regulatory regimes to ensure that they have the ability to identify and address the specific risks arising from 'stablecoins'. Further, authorities identified several issues that warrant further consideration at the international level, and we are working to address them.

We are also working to make cross-border payments cheaper, faster, more transparent, and more accessible. Work in 2021 focused on laying the foundational elements that support our *G20 roadmap for enhancing cross-border payments*. A key part of the foundation has been the publication of specific quantitative global targets that address the challenges of cost, speed, transparency, and access that cross-border payments face. These targets play an important role in defining the ambition of the work and creating accountability. But the Roadmap will not be achieved merely through analyses and recommendations. The next stage of work in 2022 includes the development of specific proposals for material improvements of underlying systems and arrangements, as well as the potential development of new systems. This practical work will

require global coordination and sustained political support. It will also require investment in systems, processes, and technologies.

Strengthening our understanding of climate-related risks

The large and growing number of international initiatives underway to understand financial risks posed by climate change reflect the increased attention to this topic but also highlight the need for coordination. In July, we published the FSB's Climate roadmap to support international coordination for addressing climate-related financial risks.

A key current focus is on developing globally consistent and comparable disclosures for climate-related financial risks, in order to provide market participants with needed information to manage climate-related risks and make investment decisions on a global basis. The work being carried forward by the International Financial Reporting Standards (IFRS) Foundation and International Organization of Securities Commissions (IOSCO) provides a promising path toward a needed global baseline standard for such disclosures. As this develops, the FSB will continue to promote globally comparable, high-quality climate-related disclosures, using a framework based on the Task Force on Climate-related Financial Disclosures (TCFD) Recommendations.

Looking toward the future, we will continue work to understand and address climate-related financial risks. Properly reflecting climate risks in all financing decisions is critical for financial stability. Our climate roadmap lays out a comprehensive work program to help us move forward. We will work with others to assess the availability of data to monitor climate-related financial stability risks, fill data gaps, and develop forward-looking metrics on the financial impacts of climate change. We will monitor and assess climate-related financial vulnerabilities and promote consistent regulatory and supervisory approaches to address climate-related risks at financial institutions.

Charting a path forward

The COVID Event underscored that threats to global financial stability can emerge quickly and from a wide variety of sources. A top priority for the FSB has therefore been to develop a more systematic way of assessing vulnerabilities across the global financial system. Our new *Financial Stability Surveillance Framework* draws on the collective perspective and collaborative efforts of FSB members in order to identify vulnerabilities in a comprehensive, disciplined, and forward-looking manner. This framework will increase the effectiveness of our assessments of vulnerabilities, improve the timeliness of any follow-up actions, and strengthen public communication.

Recognizing the wide-reaching effects of the FSB's work, we have sought to increase input from a broad range of stakeholders, each of whom brings a different perspective. We have enhanced our transparency and expanded our outreach across regions and sectors. We have made significant changes to ensure businesses, institutions, and market participants are engaged in the conversations that help develop FSB policy recommendations. This outreach, I believe, has improved the depth, quality, and effectiveness of our work, which has been reflected in the actions we have taken over this past year.

Building on these strengths, the FSB is developing its workplan for 2022 in concert with the incoming G20 Indonesian Presidency to build a cohesive path forward.

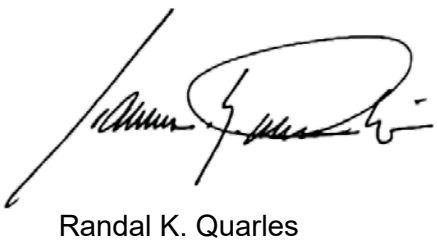
Conclusion

During the COVID Event, the FSB has proven its effectiveness as a mechanism to further global financial stability and support swift recovery. One reason is the institutional setup of the FSB. The FSB process provides, through its committees, the international coordination and cooperation required to assess vulnerabilities, coordinate policy responses, and evaluate effectiveness. Another reason is the FSB's broad and diverse membership. Coordination across our members, like the interconnectedness of the financial system itself, continues to deepen and evolve to be responsive to change. Our members, and the partnerships we have built, remain our greatest asset.

It has been an honor to serve as the FSB Chair these last three years and to lead this important global organization during such a critical time. Despite the inability to meet in-person and the ongoing remote working environment, we have continued to effectively collaborate to address the challenges to financial stability. I would like to thank my fellow policymakers for their unwavering support and willingness to share their expertise. Our progress is a testament to their dedication and tireless contributions in pushing forward critical work.

I would like to thank G20 Leaders for your support of the FSB's efforts. Much progress has been made, and your continuing commitment to promote a resilient global financial system provides a foundation for strong, sustainable growth. Thank you for giving me the opportunity to serve alongside you all. FSB Vice Chair Klaas Knot will take over from me as Chair on December 2 to advance the FSB's work program. I therefore leave the FSB in safe hands. While much progress has been made, the COVID Event reminds us that we cannot be complacent. Your commitment, along with the FSB's continued work, will allow us to improve our understanding of global financial stability risks, now and in the future, and to promote a stable foundation for a robust global financial system.

Yours sincerely,



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