



FINANCIAL
STABILITY
BOARD

THE CHAIR

24 February 2021

To G20 Finance Ministers and Central Bank Governors

For the past year, the imposition of containment measures across the globe (the “COVID Event”) in response to the outbreak of COVID-19 has overshadowed the global economy. At the outset of the COVID Event, the Financial Stability Board (FSB) focused on emergency measures and actions for what we hoped would be a short-term shock; however, the duration of the Event continues to test our resolve in many ways. Although the FSB, like many others, faced unprecedented challenges, this year also highlighted certain strengths that the FSB has honed since its inception.

Building on this foundation, three key features of the FSB have characterized members’ actions over the past year: i) responsiveness to crisis; ii) coordination in action; and iii) adaptability. These attributes will certainly help us tackle our most pressing needs going forward, which include addressing vulnerabilities in the global financial system exposed by the COVID Event, as well as ongoing vigilance and monitoring of new and emerging risks. Through the resilience and adaptability already shown, we will meet our charge of identifying and addressing these risks.

Moving into 2021, the pathway to a post-COVID world is still uncertain. The responsiveness and coordination of the global regulatory community therefore remains as critical now as it was during the past year.

Against this backdrop, the FSB 2021 work program remains ambitious. It seeks to address vulnerabilities directly related to COVID-19 and to increase resilience of non-bank financial intermediation (NBFIs). It also aims to support strong, sustainable, balanced and inclusive growth in a post-COVID world, not least by improving efficiency and access to cross-border payments, and by enhancing our understanding of climate-related financial risks and measures to address these risks, among other key topics.

Addressing COVID-19 Related Vulnerabilities

We have seen some easing of financial market conditions, in part as a result of the significant policy actions taken by G20 members last year; however, challenges to financial stability persist. The continual assessment of vulnerabilities in the global financial system, therefore, remains a priority and provides a robust basis for cataloging and assessing the impact of COVID-19 policy responses. Our work to support international coordination on these policy responses includes examining factors needed to prepare for an orderly unwinding of COVID-19 support measures when it is appropriate to do so, including avoiding adverse cross-border spillovers. Additionally, developing a better understanding of challenges that rising debt levels in the corporate sector may pose is another crucial area of focus. We will report to you on this work in April.

Further, the FSB will provide the G20 an assessment of initial lessons learned from the COVID Event for financial stability, with an interim report in July and a final report in October. In coordination with other standard setting bodies (SSBs), we will look at financial institutions' use of capital and liquidity buffers and how well crisis management and operational resilience arrangements have functioned. This work will also examine whether and how procyclicality has affected the financial system. Any lessons learned at this stage will be preliminary due to the ongoing nature of the COVID Event, but we must begin developing those lessons now, including whether the reforms the G20 put in place following the 2008 Global Financial Crisis are working as intended, and where they may not be. The FSB will also continue addressing issues identified by the evaluation of too-big-to-fail reforms for banks, the final version of which will be sent to you in April.

Increasing the Resilience of Non-bank Financial Intermediation

One area where we have already begun to draw lessons is NBFi. Our Holistic Review of the Market Turmoil in March 2020 is the basis for a comprehensive and ambitious work program for strengthening the resilience of NBFi. My November 2020 letter to G20 Leaders highlighted the key areas of this work program, including: examining and addressing specific risk factors that contributed to amplification of the shock; enhancing understanding of systemic risks in NBFi; and investigating policies to address systemic risks in NBFi. This work remains a top priority.

A key deliverable this year will be policy proposals to enhance the resilience of money market funds (MMFs). The March 2020 market turmoil highlighted some structural vulnerabilities in MMFs (particularly non-government MMFs) stemming from liquidity mismatches and from investors' perception of these funds as being cash equivalent, both of which may have reinforced redemption dynamics. Identifying policy options to enhance MMF resilience will include consideration of the appropriate structure of the sector and the role of potential vulnerabilities in the underlying short-term funding markets. We are working in close collaboration with SSBs and will provide a consultative report to the G20 in July with policy proposals to enhance MMF resilience, and a final report in October.

Other work will entail examining the frameworks and dynamics of margin calls in centrally cleared and uncleared markets, and the liquidity management preparedness of market participants to meet margin calls. It will also include examining the experience of open-ended fund types that faced redemption pressures during the March turmoil and the effectiveness of liquidity management tools, the structure and liquidity provision in core funding markets during stress, including the role of leveraged investors and factors that limit dealer capacity or willingness to intermediate. Further, we will deepen the analysis of structural and interconnectedness issues in NBFi, including the interaction of USD funding pressures and fund outflows in emerging market economies, as input into enhanced risk monitoring and discussions on policies to address systemic risks in NBFi. To effectuate this important agenda, close cooperation and coordination between the FSB and other SSBs on complex NBFi issues is of the utmost importance. We will update the G20 on overall progress in our NBFi work program in October.

Making Cross-border Payments Cheaper, Faster, and More Inclusive

Work has begun on the implementation of the FSB Roadmap to enhance cross-border payments. G20 Leaders endorsed this comprehensive and ambitious plan to make cross-border payments cheaper, faster, more transparent, and more inclusive.

A foundational step in the roadmap consists of setting quantitative targets at the global level for pursuing these objectives. Clear targets will be important for defining the ambition of the work and for creating accountability. The FSB will deliver a final set of targets in October for G20 endorsement, together with an overall progress report on the implementation of the roadmap.

The FSB will also continue its work on so-called global ‘stablecoins’ including as part of the roadmap. Last October, the FSB submitted to the G20 high-level recommendations to address the regulatory, supervisory and oversight challenges raised by global ‘stablecoins’. Continued sharing of information on regulatory and supervisory approaches is important to ensure the effective implementation of these recommendations in a rapidly evolving environment. In October, we will update the G20 on how national and international frameworks capture regulatory issues of ‘stablecoins’ in light of our high-level recommendations.

Bettering Our Understanding of Climate-related Risks

The need for understanding the relationship between climate-related risks and the financial system continues to grow in importance. Following last year’s report on the financial stability implications of climate change, the FSB will assess the availability of data through which climate-related risks to financial stability could be monitored, as well as any data gaps.

At the request of the Italian G20 Presidency, the FSB will also explore ways to promote globally comparable, high quality, and auditable standards of disclosure based on the recommendations of the Task Force on Climate-related Financial Disclosure. In this context, the FSB welcomes the recommended approach by the Trustees of the IFRS Foundation to initially focus on standards for climate-related financial disclosures. The FSB will coordinate closely with the other SSBs, and with the Network for Greening the Financial System, which are also working to achieve this goal. Additionally, the FSB will review regulatory and supervisory approaches to addressing climate-related risks at financial institutions.

These initiatives will provide a meaningful contribution as market participants and financial authorities seek to ensure that financial markets have the information and tools they need to manage risks, and seize opportunities, stemming from climate change.

Addressing Other Financial Stability Topics of Ongoing Importance

As the COVID Event endures, so does the important task of addressing challenges to, and opportunities for, enhancing financial stability that existed before the term COVID-19 became part of our collective vocabulary. There are several efforts that cannot be paused while we address vulnerabilities stemming from COVID-19.

First, the FSB remains committed to ensuring a smooth transition away from LIBOR. The 2020 disruption to global financial markets associated with the COVID-19 Event further highlighted fundamental weaknesses in LIBOR, reinforcing the need for the FSB’s roadmap to ensure a smooth LIBOR transition by end-2021 to more robust benchmarks.

Second, work to enhance central counterparty resilience, recovery, and resolvability must continue. Recent periods of market turmoil have further demonstrated the positive effect that central clearing can offer for global financial stability, underscoring the systemic importance of central counterparties (CCPs). The international policy framework for CCPs should reflect the evolving role of central clearing in order to address risks to financial stability in an effective

manner. To this end, the Chairs of the FSB, Committee on Payments and Market Infrastructures, International Organization of Securities Commissions and the FSB Resolution Steering Group will collaborate on further joint CCP financial resources work in 2021.

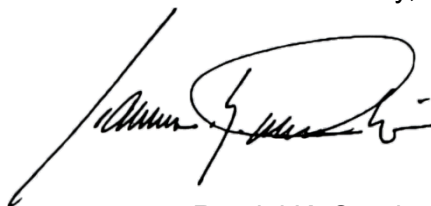
Finally, prolonged remote work environments have made all of us even more aware of the potential for cyber risks. FSB work on examining cyber incidents and revising the FSB Cyber Lexicon is increasingly important. One aspect of this work is exploring further harmonization of regulatory reporting of financial institutions, including financial market infrastructures, to their financial regulators or supervisors. This would help reduce the risk of fragmentation in cyber incident reporting. In addition, a stocktake will help capture the range of information on reported cyber incidents that is shared across borders and sectors, and the extent authorities in jurisdictions are leveraging the cyber incidents reported to help inform quantitative financial stability analyses and stress testing

Road Ahead

The FSB, with its broad and diverse membership, is well positioned to tackle the global financial stability issues outlined above. In doing so, we will continue to be guided by the FSB Principles, endorsed by the G20 last April, which stress the importance of maintaining the objectives of recent regulatory reforms, while using their inbuilt flexibility to address COVID-19 stress. These Principles continue to underpin the official community's response to the COVID Event and guide our member's actions. Moreover, in developing our work, the FSB will continue to engage with external stakeholders, including representatives from emerging markets and developing economies, through workshops, public consultations on key policy reports, and other mechanisms. Thoughtful, measured analysis, that can act as a basis for identifying common solutions will help policymakers and financial institutions alike better address challenges when they arise.

No doubt, the ongoing COVID pandemic will also necessitate adjustments and additional analysis for topics we have not yet foreseen. With that acknowledgement, I especially look forward to delivering in the fall the final reports on policy proposals to enhance MMF resilience and lessons learned from COVID-19, in addition to the various progress reports on the FSB's other important endeavors. I expect that the FSB's work in 2021 will result in robust analysis and proposals to help define a path forward on topics we have planned, and on issues that may arise as we continue to navigate these unpredictable times.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Randal K. Quarles', written over a white background.

Randal K. Quarles