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Opening remarks

The views expressed in these opening remarks are those of the author and do not necessarily represent the views of the Federal Reserve Bank of Dallas or the Federal Reserve System.

Welcome and acknowledgments

- Good morning. Buenos días a todos. It is my pleasure to join Dr. Ramos Francia in welcoming you to this year's Workshop on Financial Stability, the third edition of this collaborative event jointly organized by the Federal Reserve Bank of Dallas and CEMLA. Over the years, this workshop has grown into a meaningful tradition, enriched this year by the participation of the International Banking, Economics and Finance Association (IBEFA). It is inspiring to see such a distinguished and diverse group, whose expertise underscores the value of this forum in fostering the dynamic exchange of ideas essential to addressing today's financial stability challenges.

- I would like to extend my deepest gratitude to our co-organizers. My heartfelt thanks go to Dr. Ramos Francia, CEMLA's General Director, for his pivotal leadership and vision, and to Matias Ossandon Busch, CEMLA's Director of Financial Stability, for his exceptional insights and organizational efforts. I also wish to recognize the contributions of Lars Norden, Executive Director of IBEFA, and Björn Imbierowicz, IBEFA's President-Elect, whose support has been instrumental. Collaboration with CEMLA and its member institutions is a cornerstone of the Dallas Fed's commitment to strengthening partnerships across the Americas and beyond.

- This year's workshop also marks a milestone for the newly launched Global Institute at the Federal Reserve Bank of Dallas. Established in November 2024, the Institute builds on a strong legacy of international research, advancing policy-relevant work on global trade, capital flows, migration, and technology transfer, with a particular focus on the U.S.–Mexico relationship. By leveraging the Eleventh District's unique strengths, the Institute aims to provide insights that address global challenges, including those related to financial stability, and inform monetary policy in an interconnected world.

- It is fitting that one of the Institute's first major engagements is this workshop, which delves into critical topics at the intersection of financial stability and global economic challenges. Our discussions during the workshop will address pressing issues, including external dollar funding and the global role of the dollar, the rapid evolution of fintech and payment systems, the reshaping of global value chains, the risks of housing, and the far-reaching impacts of climate-related risks. These themes highlight the interconnectedness of global markets and the urgent need for effective safeguards amid rapid financial innovation, heightened risks, and ongoing structural shifts in the global financial landscape.

External dollar funding and the role of the dollar

- The role of the U.S. dollar as the world's reserve currency has profound implications for monetary policy, financial stability, and payment systems. The dollar underpins much of international trade and financial activity—external dollar funding is a cornerstone of global finance—yet non-U.S. financial institutions, particularly Eurozone G-SIBs (global systemically important banks), rely heavily on dollar liquidity, creating systemic vulnerabilities for the entire global monetary and financial architecture. Basel III regulations, while aimed at bolstering financial resilience, have inadvertently heightened dependence on synthetic dollar funding through FX swaps, increasing risks during stress periods. These vulnerabilities extend to payment systems, where disruptions in dollar liquidity can impair cross-border transactions and amplify systemic strains. Addressing these issues demands a balance between regulatory efficiency and market functionality. For instance, how can central banks, including the Federal Reserve, optimize tools like dollar swap lines to ease liquidity pressures while minimizing moral hazard and safeguarding payment systems?

- Dollar funding markets are tightly interwoven with global financial cycles, amplifying the spillover effects of U.S. monetary policy. Stress-induced deviations from covered interest parity highlight heightened dollar liquidity demands and underlying systemic pressures. Moreover, the growing role of non-bank financial intermediaries (NBFIs) in dollar funding adds a layer of complexity, both for regulation and the stability of payment systems that rely on seamless liquidity flows. These dynamics have broader implications for monetary policy by influencing benchmarks like r-star, the neutral rate at which monetary policy neither stimulates nor restricts economic growth to achieve the inflation target. They also affect what researchers term r-double-star, a range of interest rate paths consistent with financial stability, complicating policymakers’ efforts to steer the economy toward its potential while maintaining price stability. Evolving trade patterns, shifting capital flows, and geopolitical tensions further complicate dollar liquidity provision, underscoring the urgent need for research to help us better understand how these factors interact with funding vulnerabilities and emerging risks to payment systems.

- International cooperation has proven essential during past crises, such as the Global Financial Crisis (GFC) and the COVID-19 pandemic, when the Federal Reserve's dollar swap lines stabilized global markets. However, evolving global dynamics, including fragmented trade patterns and attempts to bypass dollar-centric payment systems, add new layers of complexity. Research is crucial to explore how these shifts affect dollar funding mechanisms and the broader financial system, enabling more effective alignment of monetary and macroprudential policies to address emerging risks while maintaining resilient payment and funding (liquidity provision) systems.

Fintech, Payment Systems, and Global Value Chains

- The rapid evolution of fintech and payment systems is transforming the global financial landscape, offering opportunities to enhance efficiency and inclusion but also introducing new risks to financial stability. Innovations like interoperable payment data and decentralized finance are revolutionizing cross-border transactions, reducing costs and increasing speed. However, these advancements create regulatory challenges, including privacy concerns, cybersecurity threats, and systemic vulnerabilities exacerbated by the growing role of NBFIs. Policymakers must grapple with questions about how to harness fintech's benefits while safeguarding financial systems from the associated risks.

- Simultaneously, the reshaping of global value chains, driven by geopolitical tensions, nearshoring, and technological shifts, further complicates cross-border payment systems. For instance, the "great reallocation" of trade away from China to countries like Mexico alters the flow of funds and demands rapid adaptation in payment infrastructure. The growing prominence of digital platforms in facilitating cross-border payments underscores the need for some international regulatory harmonization to address fragmentation and mitigate regulatory arbitrage and risks like cybercrime. What implications does this reallocation of global trade have for capital flows, and how can payment systems evolve to support seamless transactions while minimizing systemic shocks?

- These trends are also reshaping monetary policy transmission mechanisms. Fintech's ability to bypass traditional intermediaries affects how central bank policies influence capital flows and currency dynamics. Moreover, the increasing fragmentation of payment systems, coupled with the rise of private digital currencies and efforts to internationalize the renminbi, could challenge the dollar's dominance as a global reserve currency. How can central banks regulate emerging technologies while encouraging innovation, and what strategies can foster resilient payment systems in an increasingly fragmented global economy?

Housing Markets, Asset Pricing, and Bubbles

- Housing markets remain a critical driver of financial stability risks, as evidenced by the 2007-09 GFC. Asset price bubbles, particularly in housing, disrupt resource allocation, fuel speculative overinvestment, and often lead to sharp corrections. Advances in real-time bubble detection, such as the exuberance detection methodology developed by Peter C.B. Phillips and others, provide policymakers with tools to identify speculative pressures and implement timely interventions. These initiatives, like the Dallas Fed's International House Price Database, offer actionable insights to mitigate systemic risks tied to housing markets.

- The pandemic-driven housing boom underscored the vital role of macroprudential policies in managing credit growth and curbing bubbles. While many countries preserved stability through these tools, their uneven application highlights the need for stronger and more consistent frameworks. This raises key research questions: How can macroprudential tools be tailored to housing cycles? What strategies and real-time monitoring can enhance risk assessment and intervention? And how might these measures influence r-star or r-double-star and their implications for financial stability?

- Housing markets have far-reaching implications for monetary policy, particularly given the global synchronization of housing cycles driven by credit growth and financial spillovers. This interconnectedness highlights the need for a more coordinated approach that integrates monetary and macroprudential policies to address systemic risks effectively. Proactive measures, including preemptive actions and clear communication strategies, can reduce reliance on monetary policy to "clean up" after a market correction. But delving deeper into these interconnections is essential for strengthening housing market resilience and mitigating the potential for major disruptions to the broader financial system.

Climate-Related Risks and Financial Stability

- Finally, I would be remiss not to note that climate-related risks present a growing challenge to financial stability, with significant implications for macroprudential policy and monetary frameworks. Physical risks, such as extreme weather events, and transition risks associated with the shift to a low-carbon economy pose aggregate shocks that strain financial institutions. Differentiated capital requirements and other such tools to incentivize green investments, as highlighted in current research, can help manage these risks while supporting climate resilience. How can these policies be effectively integrated into macroprudential frameworks, and what role should emerging tools and data play in monitoring and mitigating climate-related vulnerabilities?

- Housing markets are particularly sensitive to climate-related risks, as demonstrated by the role of green certifications in promoting sustainable investments. Policies encouraging green housing can reduce systemic risks while influencing monetary transmission, such as through the compression of risk premia on green mortgages. However, concerns about "greenwashing" and uneven policy implementation highlight the need for robust oversight and a greater degree of international cooperation. How can policymakers ensure that green initiatives are effective and equitable while minimizing unintended consequences?

- Global financial systems face additional challenges as climate risks intersect with international capital flows and funding structures, amplifying vulnerabilities through cross-border contagion and synchronization of financial cycles. Strengthening international cooperation and aligning macroprudential policies with global climate goals might be important for mitigating these risks. By fostering interdisciplinary research and dialogue, we can develop innovative strategies to address climate-related challenges and build a more resilient and sustainable global financial system.

Final remarks

- The agenda is ambitious, reflecting the scope and significance of these issues. Each theme we tackle—from external dollar funding to climate risks—underscores the need for forward-looking research that offers actionable insights for policymakers. This workshop provides a platform to advance these efforts, fostering interdisciplinary collaboration and dialogue among academics, central banks, and other stakeholders.

- In conclusion, I would like to thank you all for your participation and extend my appreciation to CEMLA and all our co-organizers for their exceptional efforts in making this event possible. Your collective expertise will be instrumental as we explore these critical themes. This workshop was designed to promote dialogue and collaboration between academia and central banks on the pressing challenges to financial stability, and I look forward to the enriching discussions ahead. Together, we can deepen our understanding of global vulnerabilities and opportunities, working toward a more resilient and efficient international financial and monetary system. I wish you all a productive and engaging workshop. Thank you.