For release at
5:30 p.m. EDT
May 25, 2022

Statement by

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before the

Committee on Financial Services

U.S. House of Representatives

May 26, 2022

Chairwoman Waters, Ranking Member McHenry, and other members of the Committee, I am pleased to join you today. With technology driving profound change, it is important we prepare for the financial system of the future and not limit our thinking to the financial system of today. No decision has been made about whether a U.S. central bank digital currency (CBDC) will be a part of that future, but it is important to undertake the necessary work to inform any such decision and to be ready to move forward should the need arise.

There has been explosive growth in an emergent digital financial system built around new digital assets and facilitated by crypto-asset platforms and stablecoins as settlement assets. In recent weeks, two widely used stablecoins have come under considerable pressure. One widely used algorithmic stablecoin declined to a small fraction of its purported value, and the stablecoin that is the most traded crypto asset by volume temporarily dipped below its purported one-to-one valuation with the dollar.

These events underscore the need for clear regulatory guardrails to provide consumer and investor protection, protect financial stability, and ensure a level playing field for competition and innovation across the financial system. The recent turmoil in crypto financial markets makes clear that the actions we take now—whether on the regulatory framework or a digital dollar—should be robust to the future evolution of the financial system. The rapid ongoing evolution of the digital financial system at the national and international levels should lead us to frame the question not as whether there is a need for a central-bank-issued digital dollar today, but rather whether there may be conditions in the future that may give rise to such a need. We recognize there are risks of not acting, just as there are risks of acting.

Congress recognized the importance of safe, efficient, and widely accessible payments when it created the Federal Reserve and included payments as a core part of our mission. It entrusted to the Federal Reserve the issuance to the public of government, risk-free currency. The Federal Reserve has operated alongside the private sector, providing a stable currency and operating key aspects of the payments system, while also supporting private-sector innovation.

Today, physical currency provides the public with access to safe central bank money, exchangeable without concern for liquidity or credit risk. The share of U.S. payments made by cash has declined from 31 percent to 20 percent just over the past five years, and the share is even lower for those under age 45. As we assess the future digital financial system, it is prudent to consider how to preserve ready public access to safe central bank money, perhaps through the digital analogue of the Federal Reserve's issuance of physical currency. At present, consumers and businesses do not consider whether the money they are using is a liability of the central bank, as with cash, or of a commercial bank, as with bank deposits. Confidence in commercial bank money is built upon deposit insurance, banks' access to central bank liquidity, and banking regulation and supervision.

New forms of digital money such as stablecoins that do not share these same protections could reintroduce meaningful counterparty risk into the payments system. As we have seen, such new forms of money can lose their promised value relative to fiat currency, harming consumers or, at large scale, creating broader financial stability risks. We have seen before the risks posed by the widespread use of private monies. In the 19th century, active competition among issuers of private paper banknotes led to inefficiency, fraud, and instability in the U.S. payments system, which ultimately necessitated a uniform form of money backed by the national government. A predominance of private monies of this type could introduce consumer protection and financial stability risks because of their potential volatility and the risk of run-like behavior, as was demonstrated at a smaller scale in recent weeks.

In addition, if private monies—in the form of either stablecoins or cryptocurrencies—were to become widespread, we could see fragmentation of the U.S. payment system into so-called walled gardens. In some future circumstances, CBDC could coexist with and be complementary to stablecoins and commercial bank money by providing a safe central bank liability in the digital financial ecosystem, much like cash currently coexists with commercial bank money.

It is also important to consider the potential risks of a CBDC associated with disintermediating banks, given their critical role in credit provision, monetary policy transmission, and payments. In some circumstances, a widely available CBDC could serve as a substitute for commercial bank money, possibly reducing the aggregate amount of deposits in the banking system. And a CBDC would be attractive to risk-averse users during times of stress. Accordingly, if the Federal Reserve were to move forward on CBDC, it would be important to develop design features that could mitigate such risks, such as offering a non-interest bearing CBDC or limiting the amount of CBDC a consumer could hold or transfer.

The future evolution of international payments and capital flows will also influence considerations surrounding a potential U.S. CBDC. The dollar is the most widely used currency in international payments and investments, which benefits the

United States by reducing transaction and borrowing costs for U.S. households, businesses, and government. In future states where other major foreign currencies are issued in CBDC form, it is prudent to consider how the potential absence or presence of a U.S. central bank digital dollar could affect the use of the dollar in global payments. For example, the People's Bank of China has been piloting the digital yuan, and several other foreign central banks are issuing or considering issuing their own digital currencies. A U.S. CBDC may be one potential way to ensure that people around the world who use the dollar can continue to rely on the strength and safety of the U.S. currency to transact and conduct business in the digital financial system. More broadly, it is important for the United States to play a lead role in the development of standards governing international digital finance transactions involving CBDCs consistent with the norms of privacy, accessibility, interoperability, and security.

In January, the Federal Reserve issued a discussion paper, *Money and Payments: The U.S. Dollar in the Age of Digital Transformation*, to solicit input from the public on this important matter.[1] The paper's comment period closed on May 20, and as of that date, we had received nearly 2,000 comments from a wide range of stakeholders. We plan to publish a public summary of comments in the near future.

The paper emphasizes that a CBDC would best serve the needs of the United States by being privacy-protected, intermediated, widely transferable, and identity-verified. Consistent with these principles, many commenters emphasized the importance of privacy, suggesting innovative ways to protect the privacy of consumers and how to

[1] See Board of Governors of the Federal Reserve System, *Money and Payments: The U.S Dollar in the Age of Digital Transformation* (Washington: Board of Governors, January 2022), https://www.federalreserve.gov/publications/money-and-payments-discussion-paper htm.

balance privacy with the prevention of financial crimes. It is very important to strike the right balance here, just as commercial banks provide strong privacy protections alongside robust controls to combat money laundering and the financing of terrorism. Other commenters emphasized the importance of a continued role for banks as intermediaries, as suggested by our paper. An intermediated system, in which private intermediaries, including banks, would offer accounts or digital wallets to facilitate the management of CBDC, would leverage the private sector's existing identity frameworks and service provision to consumers while mitigating the risk of disintermediation.

As we move forward, it is essential that we continue to engage with Congress. I appreciate that members of this Committee are bringing a critical focus to this issue.