



FedFin Client Report

Wednesday, July 14, 2021

Powell Clarifies CBDC/Merger Stance

Client Report: **FEDERALRESERVE62**

Executive Summary

Although much of today's HFSC hearing with Chairman Powell was preoccupied by hot debate over the extent to which inflation is "transitory," key financial-policy questions also surfaced for substantive discussion. CBDC and stablecoins were another major consideration; the Fed's schedule for a CBDC consultation is now pushed to early September, with Mr. Powell today also saying that it will additionally focus on stablecoins and crypto. Although still noncommittal on a CBDC, the Fed chair also said that the risks posed by private stablecoins were perhaps the best argument for a fiat digital currency for the U.S. Asked about the President's new competition policy ([see Client Report MERGER6](#)), Mr. Powell said simply that the Fed will continue to view mergers as it always has under law, not expressly challenging the White House's plans but making clear that the Fed will retain its full independence in this critical arena. Republicans and one Democrat (Rep. Brad Sherman of California) supported a second term for Mr. Powell, advocacy that may further strengthen progressive opposition to a nomination.

The hearing also featured a lively exchange on Karen Petrou's *New York Times* [opinion piece](#). Rep. Richie Torres (D-NY) pressed Mr. Powell on whether ultra-low rates increase inequality; the Fed chairman rebutted this as discussed below and also disputed any Fed economic-inequality responsibility. Ms. Petrou will shortly provide a substantive answer on these key points.

Analysis

Opening Statements

Chairwoman Waters (D-CA) pressed the Fed to focus on climate change and financial stability while also exploring CBDC, implementing faster payments, and strengthening its "outdated" approach to bank mergers. Ranking Member McHenry

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(R-NC) endorsed Chair Powell for another term while urging the Fed to focus less on climate change.

Subcommittee on Monetary Policy Chair Himes (D-CT) thanked Mr. Powell for highlighting the economic reasons to explore economic disparities while Ranking Member Barr (R-KY) also endorsed Mr. Powell for another term.

Testimony

Chairman Powell reiterated the findings of the Fed's July *Monetary Policy Report*, highlighting improved labor market conditions and "notably" increased inflation. He maintained, however, that this inflation is transitory.

Q&A

- **China:** Rep. Luetkemeyer (R-MO) asked if China is trying to weaponize its economy; Mr. Powell believes that the U.S. is in a strategic and economic competition with China.
- **Economic Inequality:** As noted, Rep. Torres asked for Mr. Powell's opinion on Ms. Petrou's recent op-ed; Mr. Powell does not believe that the Fed's low rates contribute to economic inequality, arguing that low-interest rates support a strong labor market. Noting that wealth inequality goes up over the course of a business expansion, he believes that the Fed can help decrease inequality by supporting maximum employment.
- **Housing:** Chairwoman Waters and Rep. Meeks (D-NY) worried about the impact of rising home prices on first-time home buyers; Mr. Powell noted that, although housing prices are increasing, this is not driven by the "reckless, irresponsible lending" that led to the last financial crisis, agreeing that this increase does make it more difficult for new home buyers. Chairwoman Waters asked if increasing interest rates would impact housing supply, wondering also if increased housing supply would help alleviate inflation; Mr. Powell does not believe that increased interest rates would affect supply, but agreed that increased supply would help alleviate inflation. Chairwoman Waters also announced that she is re-introducing the Housing is Infrastructure Act to increase investments in affordable housing.
- **CBDC:** Ranking Member McHenry asked about the Fed's CBDC whitepaper; Mr. Powell expects the report to be released in early September, noting that it will begin a public consultation on CBDC, stablecoins, and crypto. Rep. Lynch (D-MA) worried that the slow development of CBDC could threaten the U.S.

dollar's reserve currency status; Mr. Powell does not believe that the U.S. is in any danger of losing its reserve-currency status to China or any other country. Rep. Lynch also wondered if swift action on a CBDC could have a "calming effect" on crypto; Mr. Powell agreed, describing this as a "strong argument" in favor of CBDC. Rep. Sherman (D-CA) asked if a CBDC would include KYC and AML standards; Mr. Powell said it would.

- **Crypto:** Ranking Member McHenry and Rep. Gonzalez (R-OH) worried about stablecoins; Mr. Powell noted that stablecoins resemble MMFs and bank deposits but lack regulation. Mr. Powell believes there needs to be a strong regulatory framework as stablecoins could become a significant part of the payments system.
- **Climate Change:** Rep. Maloney (D-NY) asked about the Fed's work on climate change; Mr. Powell noted that the Fed is in the beginning stages of a "program" that will engage financial institutions to ensure they are capable of understanding and managing climate risk. The Fed also has an overlapping effort that examines how climate change will affect financial markets.
- **Bank Mergers:** Rep. Meeks (D-NY) asked how the Fed plans to coordinate with DOJ in light of President Biden's recent executive order; Mr. Powell noted that the Fed will continue to coordinate with DOJ on bank mergers, although the Fed's standards on mergers have not changed.
- **LIBOR:** Rep. Huizenga (R-MI) argued that, while there does need to be "legal certainty" for legacy contracts, he worried that the Fed might try to impose SOFR as a "one-size-fits-all" benchmark; Mr. Powell reiterated that institutions should have a choice among benchmarks. Rep. Huizenga further asked if SOFR should be included in legislation; Mr. Powell said it would be appropriate to include but not exclusively. Rep. Sherman added that it is not the federal government's job to mandate SOFR.
- **ONRRP:** Rep. Hill (R-AR) worried that there may be too much cash in the Fed's overnight reverse repo facility; Mr. Powell said that this may be due to a shortage of short-term safe assets.