Oral Statement of Kenneth E. Bentsen, Jr.

October 9, 2013

Chairman Johnson, Ranking Member Crapo, and Members of the Committee, my name is Ken Bentsen and I am President of the Securities Industry and Financial Markets Association. Thank you for the invitation to testify today regarding the risks associated with a default on the nation's public debt. Given the important role U.S. Treasury debt plays as a world currency and store of value, any such default would negatively impact the economy and certainly disrupt the operations of our financial markets. Indeed the market has already signaled increasing concerns regarding the public debt limit, resulting in dramatic pricing effects on the short end of the Treasury market and re-purchase agreements or repos. Investors are voting with their wallets and feet. While we firmly believe that the time is long overdue for the Administration and the Congress to come together and develop long-term solutions to our very real fiscal challenges, voluntarily defaulting on the nation's debt obligations should not be an option for policymakers to consider. Should Congress fail to raise the debt limit and the Treasury is unable to meet interest and principal payments coming due, it would trigger a series of events which inevitably would lead to American taxpayers paying more to finance our debt. Even a short-term failure to fulfill our obligations would seriously impair market operations and could have significant consequences to our fragile economic recovery.

Since the threat of default first arose in the summer of 2011, SIFMA has been engaged with its members in developing scenarios to better understand the consequences of a failure to pay on Treasury securities. Based on our work, we do in fact believe that market participants are operationally prepared to deal with the scenarios that a Treasury failure to pay would present. However, as you know, a default by the U.S. government would be unprecedented and the consequences for the market and the economy would be dangerously unpredictable so no amount of planning can identify and mitigate all of the potential short and long term consequences of a default.

While we assume that any missed payments will eventually be made, the impact of missed payments on the broader market for Treasury securities may impact the price of Treasury securities which could impact the value of collateral held at clearing houses and central counterparties. Further, it is entirely possible that for purposes of any escrow, collateral or margin arrangement involving such securities, the defaulted securities could be deemed non-eligible and subject to replacement resulting in a drain of liquidity.

Since filing our written testimony just yesterday, market participants have continued to meet and review enhancements that could mitigate operational risks that had been identified, particularly in the repo market. It is important to avoid disruptions in the Treasury repo market and market participants continue to review ways to improve overall resiliency in this market. Treasuries are the world's safest asset and the most widely-used collateral for both risk mitigation and financing. Shrinkage in the financing market would further pressure rates as haircuts or discounts on Treasuries would increase, raising costs, reducing the financing capability and disrupting the collateral market because of margin calls throughout the financial system that would reflect the overall repricing of Treasury collateral.

Given the significant uncertainty surrounding a failure to pay, market participants and SIFMA have developed a playbook that is intended to provide key market participants and service providers a forum to share information about the latest developments including decisions from the Treasury, the Administration and Congress and the status of the infrastructure and settlement providers. Of particular concern to market participants is an early indication from Treasury that securities will be extended and whether processes are being—or can be—delayed. It is important for the market to know as early as possible if Treasury intends to extend the payment date of any due interest and principal. Treasury securities are traded in a global market with the global trading day beginning in Asia at 8:00pm eastern standard time. Market participants normally run their own internal processes prior to the Asia open in order to provide a clear cut-off to reflect positions in their books and records. Failure to provide early indications of intention could further obfuscate positions and could cause trading confusion in the Asian markets. The disruption to pricing and trading behavior is impossible to predict.

U.S. debt obligations are the currency of the global financial markets and the real economy and their soundness should not be questioned. No amount of planning can anticipate all the potential consequences of a default. Short and long term costs to the taxpayer can be anticipated but the further limits on the ability to transfer, sell, finance and post as collateral defaulted securities would only serve to undermine investor confidence and hurt our fragile economic recovery. SIFMA and its member firms have frequently called on Congress and the Administration to work together to put our fiscal house in order but unnecessarily triggering a voluntary default will result in dramatic and possibly permanent damage to our economy and markets in ways both anticipated and unanticipated and must be avoided. Again, SIFMA appreciates the opportunity to testify today and I look forward to answering your questions.

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