



Federal Financial Analytics, Inc.

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The New Systemic Risk: Structural Market Change Flummoxes Monetary-Policy Transmission, Effective Regulation

“The greater the transformation of financial markets into those in which banks don’t much matter, the less effective monetary-policy transmission becomes. The less effective the monetary policy, the deeper the rut into which the macroeconomy is mired, the larger the new class of TBTF financial firms, and – the most perverse result of all – the higher the risk that the U.S. financial system stumbles into another round of disastrous systemic risk.”

WASHINGTON, DC, October 7, 2015—Karen Petrou, managing partner of Federal Financial Analytics, Inc. today called for urgent analytical attention to the interaction between structural financial-market changes, Federal Reserve monetary policy, and the ability of regulators to handle emerging “macroprudential” risks. Citing recent research, including that newly released by the Federal Reserve, Ms. Petrou lays out several areas in which structural changes clearly have perverse effects on macroeconomic growth and financial stability, as well as several emerging issues that, she says, require immediate attention before still more risks are evident.

For example, it is at best unclear if asset-management firms, including mutual funds, can safeguard cash deposits at banks, urgently needed if funds are to handle redemption calls in unstable market conditions, including those likely with a debt-ceiling breach. Another top priority: understanding what will happen when interest rates rise to the ability of banks to gather deposits and, should this drop, to credit availability. Risks are also increasingly correlated on large-bank balance sheets because of cross-cutting incentives from the array of new rules to which these banks are subject,

correlations that Ms. Petrou says also could pose systemic peril.

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Federal Financial Analytics, Inc. is a proprietary think tank providing analytical and advisory services on legislative, regulatory, and public-policy issues affecting global financial-services companies. Since 1985, the firm's practice has been a unique blend of strategic advice and policy analysis, serving as a thought leadership resource for boards of directors and senior management seeking a forward looking assessment of risks, opportunities, governance, and other matters critical to success. Clients also include senior regulators and policy-makers around the globe, who rely on the firm's objectivity for confidential forecasts of the market impact of actions under consideration.