FedFin Daily Briefing

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HUD's Controversial Fair-Lending Rules Go Live

The *Federal Register* today includes HUD's final rule on disparate-impact standards (see FSM Report **FAIRLEND8**). It is now effective October 26. As noted, the final rule largely retains the approach initially proposed (see FSM Report **FAIRLEND6**) but does not implement the proposed, express safe harbor for algorithmic underwriting. Even so, it has gained new protections under HUD.

EU Crafts Sweeping Digital, Payment Regime

Continuing its push for both functional and innovative financial regulation, the EU today advanced a new framework for digital payments and cryptography. The European Commission notes that it believes its standards will set those for the global financial system and this could well be true at least for the United States. It of course has significant financial interconnection with the EU and has yet to craft anything other than the partial national-bank framework only outlined by the OCC (see FSM Report **DIGITAL5**); we will shortly provide clients also with an assessment of the OCC's latest action to approve idiosyncratic offerings, this one a stablecoin-reserve service.

The EC package has five parts: 1) a digital finance strategy setting an EU framework for AI, DLT, data management and sharing, open finance, privacy, and consumer protection in a single framework for banks and all other providers; 2) a retail payment strategy focused on instant payments across the EU; partly to repair all the damage unveiled by Wirecard; 3) legislative proposals establishing a statutory framework for cryptoassets creating legal certainty, systemic protections, an EU passport and tougher rules for cross-border stablecoins; 4) a pilot allowing trading in cryptoassets; and 5) additional legislation on digital operational resilience expanding the EU's reach to outsourced technology providers and all other firms engaged in or supporting digital finance to prevent cyberattack or other threats. The EC's approach to global stablecoins tracks the FSB's recent proposal (see FSM Report **CRYPTO14**), but would implement it considerably more quickly.

BIS: Fintech/Big-Tech Share Small, Growing, Worrisome

Earlier this week, the BIS released a working paper establishing a database on fintech and big-tech credit offerings and warning of emerging stability concerns. Detailing growth and key drivers, the paper concludes that fintech and big-tech credit is likely to grow still more formidable in the wake of the COVID crisis, although still a small (less than one percent share) of global credit flow. In 2019, fintech had $223 billion and big tech amassed $572 billion of credit, with various survey challenges suggesting actual numbers are larger and, for big tech, considerably so. In general, big-tech finance is much more profitable than fintech. Most of this activity is housed in advanced nations, those with lax regulation, where bank mark-ups are high, when bank branches are scarce, and/or where there is legal certainty. In general, fintech and big-tech credit is found to increase credit rather than substituting for existing providers such as banks, although we note that conditions in key nations are so different and the reasons for fintech and big-tech so various that jurisdiction-specific conclusions are challenging to infer from these aggregate data. Overall, fintech and big-tech stress resilience remains uncertain, the paper concludes, urging study of issues such as the extent to which big-tech diversification, overall lack of reliance on collateral, and new scoring models will fare under sustained stress.

FRB-NY: No Need to Worry Now About Moral Hazard

In a new blog post today, Federal Reserve Bank of New York staff discount moral hazard concerns stemming from the scale of government market backstops. The paper rejects moral-hazard assertions echoing now in many quarters largely on grounds that intervention was sparked by the pandemic and market participants cannot foresee the odds of another pandemic against which to arbitrage risk-taking. The paper also doubts the potential moral-hazard impact such large intervention might have on assumptions that current exposures are risk-free due to the FRB's windows or that markets may expect similar support under like-kind stress due to non-pandemic factors.

Using the principal-agent construct, FRB-NY staff note that while government intervention theoretically encourages undue risk-taking, this risk-taking now is said to be the result not of moral hazard but the "bad luck" of being in business under acute pandemic stress. The paper also asserts that, because it is now possible to tell the difference between luck and effort, government intervention now not only does not stoke moral hazard, but is also essential. Future risk-taking is also unlikely, the paper asserts, because the risk of future pandemics is small. The paper acknowledges that government intervention could well encourage risk-taking even without a pandemic to take advantage of, but it again rejects moral-hazard worries first due to stringent post-crisis bank regulation and second because of structural weaknesses in wholesale-funding markets due to MMFs that have nothing to do with moral hazard. Corporate risk-taking due to moral hazard is also discounted on grounds that market participants cannot foresee the likelihood of government intervention.

Waters Reiterates Big-Bank Diversity Critique

In a statement today, HFSC Chairwoman Waters (D-CA) extended her sharp criticism of Wells Fargo CEO Charles Scharf's comments on qualified Black job candidates to all large banking organizations. Chair Waters reiterates that the panel has issued a staff report highly critical of diversity at large banks and subsequently sent out a survey on this question to 44 banks, but she does not indicate any near-term plans for action. We doubt remaining time before the election will permit scope for hearings, but those in a lame-duck session could lead to legislation in the next Congress depending on the election's outcome; we will shortly provide clients with in-depth analysis of H.R. 8160 which might then take center-stage in the House.

Mnuchin Working on PPP Forgiveness, Powell Faces Racial-Equity Drubbing

Although today's Senate Banking hearing with Secretary Mnuchin and Chair Powell ramped up partisan fiscal-policy battles (see Client Report **COVID15**), Secretary Mnuchin said that he is talking today to SBA on ways to streamline PPP forgiveness applications without additional legislation. Under questioning from Sen. Rounds (R-SD), Mr. Mnuchin said that forgiveness simplification should advance as long as SBA retains the right to audit decisions. However, legislation is necessary to set a forgiveness threshold and/or make it automatic. Under questioning from Sen. Kennedy (R-LA), Chair Powell and Secretary Mnuchin said reallocating funds from Title IV of the CARES Act to replenish PPP would be beneficial for the recovery, although Mr. Powell stressed that funds should be reallocated from the $200 billion in currently unallocated Title IV funds rather than from those backstopping the Main Street Program as Sen. Kennedy proposed.

Sen. Warren (D-MA) demanded that the Fed take additional steps to eliminate racial economic inequalities, pressing her legislation (see FSM Report **FEDERALRESERVE58**) to create a racial-equity mandate. Chair Powell argued that the law needs no change because the Fed is already addressing disparate economic outcomes to the extent possible within its mandate. Sen. Warren did not take this as sufficient, stating firmly that the FRB must do more than develop new unemployment indices, instead taking actions such as rejecting M&A applications from banks that do not enhance financial inclusion. Notably, FRB-Atlanta President Bostic today said that banks are at fault for barriers that make it difficult for Blacks to do business with them, urging banking organizations to take immediate action to address the challenges that others have characterized as "banking while Black."

Chairman Crapo (R-ID) reiterated that temporary regulatory relief offered on the CBLR, troubled debt restructurings, and CECL should be extended given economic conditions.

Recent Files Available for Downloading

The following reports and analyses have been sent to retainer clients recently. Copies are also available to retainer clients on the Archives section of Federal Financial Analytics' website: www.fedfin.com or clients may obtain the reports/analyses by e-mailing requests@fedfin.com giving the requested item name, firm, and e-mail address. To learn more about GSE Activity Reports, click: http://www.fedfin.com/index.php?option=com_content&view=article&id=18&Itemid=18

- **AML132**: FinCEN is beginning a process that, while apparently not revising or eliminating any existing anti-money laundering (AML) requirements, would add an over-arching principle that AML programs be efficient, "reasonably-designed," and capable of providing high-quality information to law enforcement and other government entities.
- **COVID15**: HFSC's second CARES Act-required hearing with Treasury Secretary Mnuchin and FRB Chair Powell continued to stress the theme that has become apparent ever since negotiations on a Phase IV relief bill stalled: Democrats primarily want additional direct fiscal support and Republicans are pushing for adjustments to existing relief programs funded by unused 13(3) Treasury backstops.

Federal Financial Analytics, Inc.
2101 LStreet, N.W. – Suite 300, Washington, D.C. 20037
Phone (202) 589-0880
E-mail: info@fedfin.com www.fedfin.com

- **GSE-092220**: As usual, FHFA's new strategic plan is more rhetorical than real. Still, it has a noteworthy emphasis on ending the conservatorship, promulgating new standards, and enhancing inclusion not just at the GSEs and within FHFA, but also in credit access.

- **CRA29**: Emphasizing its new focus on racial equity ahead of several Congressional hearings this week, the Federal Reserve Board today unanimously approved a long-awaited ANPR revising its CRA regulations.

- **GSE-092120**: Late last week, the Federal Reserve Bank of New York announced that the Fed bought almost $56 billion in agency MBS over the past two weeks.

- **GSE-091720**: As anticipated, today's marathon HFSC hearing with FHFA Director Calabria covered a wide-range of issues we will shortly analyze in detail due to the policy and strategic importance of several exchanges.

- **FAIRLEND8**: HUD has largely finalized a controversial fair-housing rule as proposed, with the new standards for adjudicating fair-housing disputes giving defendants numerous additional protections.

- **GSE-091020**: As we noted yesterday in our in-depth analysis, a CFTC subcommittee has issued a landmark report laying out an array of climate-change risks it urges policy-makers to prioritize to prevent systemic and sector risks.

- **COVID14**: Today's Senate Banking hearing on the status of emergency Fed facilities showed even more clearly the dividing lines between Democrats and Republicans on changes to the Main Street Lending program than the CARES Act Congressional Oversight Commission's recent hearing.

- **GREEN4**: In this report, we analyze an influential and possibly even game-changing paper released today by the CFTC's Climate-Related Market Risk Subcommittee.

- **GSE-090320**: As noted in our three summaries of key FHFA comment letters, FHFA was not exactly overwhelmed by heartfelt praise for its GSE capital rule.

- **COVID13.pdf**: As anticipated, today's House Select Subcommittee on the Coronavirus Crisis hearing with Treasury Secretary Mnuchin reflected contentious negotiations over a phase four rescue package.

- **GSE-090120:** In this analysis, we continue our assessment of comment letters to FHFA on the capital proposal.

- **GSE-083120a**: In this report, we begin our assessment of the comment letters on FHFA's capital proposal that we believe carry the most weight in terms both of FHFA's final rule and what Congress may care to do about it.

- **GSE-083120:** A new Fed staff study finds wide disparities among the mortgage rates borrowers pay on exactly the same loan that has nothing to do with risk and apparently everything to do with borrower sophistication.

- **MORTGAGE118**: Despite its pending proposal to overhaul the entire definition of loans eligible for qualified-mortgage (QM) status, the CFPB proposes also to establish an additional class of first-lien, fixed-rate mortgages that are QMs or given a rebuttable presumption of QM status.

- **GSE-082520**: The CFPB's proposal to allow QM treatment for certain seasoned mortgages will rewrite a decade's worth of securitized lending if macroeconomic and interest-rate conditions turn favorable.

- **GSE-082020**: A new study from FDIC staff challenges the predictive models on which much mortgage underwriting increasingly depends, discrediting both workhorse predictive models used across the spectrum of consumer credit as well as the ML-based mortgage models that fare still worse as macroeconomic, policy, and borrower conditions change.

- **GSE-081920**: Weighing into the GSE-evolution question with its formidable analytical might, CBO today assesses a likely administrative solution in which the GSEs retain all of their earnings for a limited period of time following which common stock goes again on offer to the public and Fannie and Freddie go back to being Fannie and Freddie more or less as they were pre-2008.

- **OPSRISK21**: Although the Basel Committee believes that its post-crisis capital and liquidity framework significantly enhanced bank resilience evident in a robust industry response to the pandemic, this crisis and other developments are said to highlight the need for additional regulatory and supervisory work to improve operational resilience.

- **GSE-081720**: With the release late Friday of Chairman Crapo's letter to FHFA, the GSEs' refi fee announcement has taken fire from a high-impact Senate Republican along with Ranking Member Brown and HFSC Democrats.

Federal Financial Analytics, Inc.
2101 LStreet, N.W. – Suite 300, Washington, D.C. 20037
Phone (202) 589-0880
E-mail: info@fedfin.com www.fedfin.com