



FedFin Weekly Alert

Monday, February 1, 2021

❑ GAMESTOP STOPS THE GAME

As the week unraveled, it became more and more clear that the GameStop story was not just about gambling day traders, but the systemic implications of the stock market's structure and the expectations investors have of it. During the dotcom bubble twenty years ago, high-flying retail investors lost their shirts but most considered it just their bad luck because, in that way-back, markets were known to go down as well as up and most households with a bit of extra money put it in the bank, not in the stock market. Ultra-low rates of course now give such households no choice – money must go into the market or lose its value every moment it's in a savings account. And, there's one other difference from the early 2000s – following two financial crises, large financial institutions now live in an enormous credibility gap. This makes it almost natural for Members of Congress to blame hedge funds – never the most adorable institutions – not their constituents. See statements from [Chairman Brown](#) (D-OH), [Chairwoman Waters](#) (D-CA), [Sen. Warren](#) (D-MA), and more than a few others if you doubt this. [Sen. Toomey](#) (R-PA) spoke to the need for market discipline, but he's likely to get run over on the way to a string of hearings. Sen. Toomey and his GOP allies will resurface with a vengeance if any legislation comes of this flurry, but between now and then, we'll be watching:

- How to Ensure Market Equity? In the current political mood, both Democrats and Republicans – [even Ted Cruz](#) (R-TX) – are upset that brokerages halted their trades and reportedly gave hedge funds time to reduce losses before the games began again. That at least one private-equity firm reportedly profited handsomely doesn't exactly put this unusual alliance of progressives and populists to rest. Given ongoing political anger at what [Donald Trump, Jr. called the "rigged" game](#), demands for market reform that puts the "little guy first" will surely resonate. We expect this to be the major focus of SEC inquiry following pointed Congressional questioning, but it's far from clear what the Commission could do about it under current law. If the furor continues, the Commission will find at least one large institution at which to throw a very large enforcement action. Given all the pressure Gary Gensler will face on this question when he comes before Congress, he will surely have to promise something and the Commission will then do its best to deliver on it.
- What happens to new-age retail brokers? Robinhood has already made a dash for cash, a sharp reminder of the slim reed on which broker net-capital rules stand. In 2007, the SEC launched an inquiry into broker capital standards ([see FSM Report](#)

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[MUTUALFUND43](#)), but nothing much came of it. Under Gary Gensler, something might.

- What Happens to Prime Brokers: The bulk of these entities are owned by a few very large banks, coming under the SEC's net-capital rules along with having their assets consolidated for purposes of BHC risk-based, trading, and leverage-ratio requirements. There is considerable talk of easing prime-broker capital standards or – [Janet Yellen's preferred option](#) – giving them access to the discount window. While retail brokers may wobble, prime brokers will almost surely be fine throughout this market chaos, but that doesn't mean that they'll be immune from capital inquiry, making relief still harder to get.
- What happens to ILCs? The other major new-age broker, Interactive Brokers, is also under stress but it's different than Robinhood – it wants to own an insured depository ([see FSM Report ILC12](#)), or at least it did prior to withdrawing this application last year. The FDIC's rule late last year setting standards for ILC parents ([see FSM Report ILC15](#)) sets a source-of-strength standard but is hard pressed to ensure it can actually be met under stress. This case will highlight the challenges of nontraditional charters and accelerate action toughening the existing rule and, over time, rewriting it.
- Will the Fed Touch Reg T? At his [Wednesday press conference](#), Chairman Powell looked positively annoyed when asked if the Fed planned to review broker margin rules in light of the GameStop fracas. With heavy pressure now from the Hill on brokerage incentives and retail-investor losses, we doubt Mr. Powell will be able to remain aloof. As a result, margin requirements not touched since 1974 are in for a tough review.

Headlines From the Past Week's Daily Briefings

[January 25](#)

- **Ginnie Issues First All-Digital MBS** - Marking a major step forward in digital finance, Ginnie Mae issued its first MBS backed by digital pools.
- **UN: COVID Central Banking Boosts Bubbles, Not Growth** - The UN's semiannual World Economic Situation and Prospects report highlights changes to central banking brought on by the COVID crisis, concluding that lenders of last resort are becoming the "buyers of last resort" and that this exacerbates asset bubbles and slows growth.

[January 26](#)

- **Comment Deadline Extended Again on VC, Digital Asset Reporting Proposal** - Further conceding to pressure from the crypto community, FinCEN again extended the comment period on its proposal to require banks and money service businesses to submit reports and verify the identity of customers for transactions involving

convertible virtual currency (CVC) or certain digital assets with legal tender status (LTDA).

- **President Targets Disparate-Lending Rule** - The flurry of Presidential actions includes a memorandum directing federal agencies quickly to reform practices related to racial inequities and other discrimination in U.S. housing policy.

January 27

- **President Biden Demands Agencies Address Environmental Justice** - Included in an Executive Order President Biden will sign is a requirement that each federal agency make environmental justice part of its mission.
- **Powell Non-Committal on 13(3) Facilities, Dividend Restrictions** - At his press conference, FRB Chair Powell sidestepped a question asking whether the 13(3) facilities now set to expire on March 31 would end as planned or be extended, saying only that, if the emergency continues, then the tools will remain.

January 28

- **Fair-Access” Rule Put in Deep Freeze** - As anticipated, the OCC has put a hold on Brian Brooks’ controversial “fair access” rule. The rule has yet to be published in the Federal Register and pausing this will, the announcement says, give the next confirmed Comptroller an opportunity to reconsider it.
- **BIS Head: CBDC, Not Stablecoin, Meets the Need for Digital Currency** - In remarks, BIS General Manager Agustín Carstens renewed his attack on bitcoin, arguing that central-bank payments systems can and will adapt to ensure sound digital currency in ways private providers simply cannot.
- **HUD Nominee: U.S. Needs Holistic Housing Policy** - At her Senate Banking nomination hearing, HUD Secretary-designate Fudge said in response to a question from Sen. Rounds (R-SD) that the U.S. needs a holistic housing-policy process combining FHA, FHFA, Treasury, and HUD. Still, Congress must make final decisions.

January 29

- **Racial Equity Top CFPB Priority** - In a blog post, Acting CFPB Director Uejio made clear that the Bureau will not only get tough ([see Client Report CONSUMER36](#)), but also tackle racial equity.

This Week

Wednesday, February 3

HFSC, Committee Organizational Meeting [11:00am, 2128 Rayburn HOB].

Thursday, February 4

HFSC, Virtual Hearing: More than a Shot in the Arm: The Need for Additional COVID-19 Stimulus [10:00am, Cisco WebEx] Witnesses not yet available.

HFSC, Virtual Hearing: Supporting Small and Minority-Owned Businesses Through the Pandemic [3:00pm, Cisco WebEx] Witnesses not yet available.

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 info@fedfin.com giving the requested item name, firm, and e-mail address. To learn more about *GSE Activity Reports*, click [here](#).

- **[CAPITAL227](#)**: Although the FRB in its proposal indicated that this rulemaking would also begin consideration of the U.S. large-bank capital framework post-COVID, its final rule largely confines itself to aligning stress-test standards with the 2019 tailoring rule and stress capital buffer (SCB) for Category IV banking organizations.
- **[GSE-012221](#)**: The failure of yet another Administration and Congress to conquer the conservatorships does not augur well for constructive policy action anytime soon.
- **[INVESTOR14](#)**: In this report, we expand on prior forecasts to assess broad financial-regulatory and structure issues under the SEC's jurisdiction under what seems likely: a Chairman Gensler. His will be an activist SEC, one sure to throw broker-dealers, asset managers, and investment funds from the relative comfort of the last four years.
- **[GSE-012121](#)**: As forecast following a landmark CFTC-committee [report](#) and the Fed's financial-stability assessment, [FHFA has now](#) turned to the climate risk that worries them the most: residential real estate.
- **[GSE-011521](#)**: Last night, Treasury and FHFA [announced](#) an agreement on the GSEs' conservatorship unsatisfactory to all concerned and highly objectionable to many of those on the Hill with the power to change it.
- **[GSE-011321](#)**: Setting Senate Banking's [agenda yesterday](#), incoming Chairman Brown highlighted refi inequality as a top committee priority.
- **[CRYPTO17](#)**: This interpretive letter (IL) follows an OCC advance notice of proposed rulemaking that suggested a notice-and-comment process before the agency made substantive changes to the digital-currency powers of federally-chartered banks.
- **[AML133](#)**: In a cliff-hanger before the end of the 116th Congress, the National Defense Authorization Act was enacted into law with an array of provisions significantly revising U.S. anti-money laundering (AML) and countering the financing of terrorism (CFT) requirements.
- **[ELECTION25](#)**: It will take considerable time for Congress to absorb the meaning of yesterday's insurrection not only in institutional terms, but also and more immediately with regard to each Member's thinking about his or her own policy and political agenda.