FedFin Daily Briefing

Monday, March 22, 2021

Banking Agencies Implement Capital Break for Treasury's CDFI, MDI Support

Facilitating COVID-related relief, the Federal banking agencies today as required issued an IFR providing that preferred stock issued under the Emergency Capital Investment Program (ECIP) qualifies as additional tier 1 capital. Subordinated debt issued under ECIP would also qualify as tier 2 capital. Under the law, Treasury is authorized to make capital investments in CDFIs and MDIs by acquiring senior preferred stock or subordinated debt, with these investments intended to support loans, grants, and forbearance for small and/or minority-owned businesses and consumers in low-income and underserved communities. Participating institutions will be barred from paying dividends until two years after the issuance of senior preferred stock. Banks will face restrictions on executive compensation and share buybacks, provisions that may well quash much industry interest in the program. The IFR is effective today; comment is due May 21.

Fed Steps Warily Towards CBDC

Chairman Powell's comments today make it clear that the Fed is set on CBDC only after extensive study despite strong Congressional pressure (see Client Report **FEDERALRESERVE61**) to move quickly. A recent Fed note analyzing the preconditions necessary to ensure successful launch provides considerable detail on the issues the U.S. central bank believes must be in place. It posits five preconditions that are necessary, but not also sufficient, for a general-purpose CBDC akin to FedAccounts (see FSM Report **CBDC**), with its focus on the most ambitious CBDC proposal on the table suggesting that narrower versions – which seem to be more what Mr. Powell has in mind – might advance at least a bit more quickly.

Concluding that operationalizing its version of CBDC is a complex task that requires significant technology upgrades, the paper's preconditions for success include a clear expectation of the CBDC's purpose, observing that CBDCs established for monetary-policy transmission or government-payment distribution are structurally different than those intended for cash alternatives or other objectives. Despite this analytical delineation, the paper argues that U.S. CBDC should support an array of goals ranging from payment speed and financial stability to consumer protection.

The second precondition is said to be broad stakeholder support, with the paper listing an array of parties that would need to be at least reconciled to CBDC, including end-users requiring enticements such as discounts to switch to CBDC from private-sector alternatives. Citing a recent FRB-Atlanta paper, this note also describes ways it believes CBDC would enhance inclusion and thus attract end-users. Reflecting a recent BIS paper, the Fed note also addresses legal uncertainties and the need to resolve them to ensure successful CBDC launch. Mr. Powell today emphasized that he would prefer to advance only after express statutory authorization but that this was also not absolutely required to launch a U.S. CBDC.

The fourth precondition for CBDC according to this paper is technology; an array of obstacles and issues thus is detailed. Finally, the Fed would need to ensure market readiness, launching CBDC only when end-users are likely to want it.

USD LIBOR to Meet Certain Death

FRB Vice Chairman Quarles today said that "there is no scenario in which a panel-based USD LIBOR will continue past June 2023." Mr. Quarles also reiterated that U.S. entities should cease using LIBOR as soon as possible or by year-end 2021. Using LIBOR after that date in new contracts would create safety-and-soundness risk the agencies would sanction, although legislation in New York and/or Congress is necessary to ensure that contracts continuing after that date without fallback language do not create market chaos. Mr. Quarles also warned that no one should expect a synthetic USD LIBOR, with the balance of his speech reiterating regulatory expectations during the LIBOR transition.

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.

- **GSE-032221:** As we predicted, federal banking agencies didn't back down: the SLR exemption for central-bank reserves and Treasuries is no more as of April 1.
- **GREEN7:** Today's Senate Banking Committee hearing on climate risk made it clear that the partisan divide evident earlier this week on housing (see Client Report **MORTGAGE119**) and much else extends to what financial regulators should do about climate risk.
- **GREEN6:** Reflecting views of the Biden Administration and those of its nominee to chair the SEC, Acting Chair Allison Herren Lee is requesting public views ahead of more formal proposals revising the climate-risk disclosures to be required of publicly registered companies.
- **GSE-031721:** As our in-depth report makes clear, the Senate Banking (and Housing!) Committee's hearing yesterday showed the wide partisan chasm between what Democrats and Republicans want of the GSEs.
- **MORTGAGE119:** Reflecting Chairman Brown's (D-OH) prioritization of the "housing" jurisdiction under Senate Banking, the panel's hearing today addressed not only GSE reform, but a sweeping range of rental and affordable-housing considerations in concert with lending discrimination and housing finance.
- **UDAP7:** Continuing the quick reversal of numerous Trump-era policies, the CFPB has ended a controversial policy statement providing consumer-finance companies with considerable protection from assertions of abusive acts or practices.
- **GSE-031621:** A new FEDS Note unpacks the unprecedented patterns of mortgage default risk during the pandemic to find that unemployment will tell the default tale.
- **REFORM202:** At a wide-ranging hearing, HFSC today launched its inquiry into racial equity in the financial system. Democrats offered a sweeping array of solutions, with witnesses alleging discrimination in lending and the failure of the banking system for people of color.

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-031021:** As previously noted, the CFPB has decided to restore the DTI-based QM along with the patch without withdrawing its price-based QM or the seasoning rule, essentially allowing mortgage lenders to do pretty much anything and sell as much of their volume as Fannie and Freddie will bear.

- **INVESTRO16:** While Senate Banking's GameStop hearing today continued many of the partisan battles fought when HFSC held its first hearing on the matter, at least one area of consensus emerged today: the need to decrease settlement times.

- **REFORM201:** Although today's Senate Banking hearing on Wall Street's role was poorly attended, it nonetheless captures the theme Chairman Brown (D-OH) intends to guide his work this Congressional session: "Wall Street" incentives adversely affect equity, equality, economic growth, and social welfare and thus require structural, sweeping reform.

- **INVESTOR15:** The Senate Banking Committee today took up two of the more contentious nominations so far to come its way: those for Gary Gensler to chair the Securities and Exchange Commission and for Rohit Chopra to head the CFPB.

- **GSE-030221:** Critics of FHFA policy are finding still more affordable-housing ammunition to add to their anti-PSPA armament.

- **GSE-022521:** In a new paper, Lew Ranieri, who needs no introduction, and Mike Calhoun of the Center for Responsible Lending float an important new idea along the way to turning the GSEs into the utilities presaged by actions under the Trump Administration to recast the conservatorship.

- **FEDERALRESERVE61:** At today's HFSC hearing, Chairman Powell not only delivered the same testimony, but faced many of the same questions to which he provided the same answers. He would not, for example, commit to ending the SLR exemption (see FSM Report **LEVERAGE23**) or to condition any continuing exemption on capital-distribution restrictions.

- **GSE-022421:** As anticipated in an earlier FedFin report, we confirm that U.S. banking agencies plan to turn quickly to U.S. implementation of the 2017 "Basel IV" package.

- **FEDERALRESERVE60:** As usual, Senate Banking's hearing today with Chairman Powell strayed from monetary policy and post-pandemic prospects to a range of financial-policy critical questions.

- **REALESTATE24:** Continuing the OCC's recent actions to expand national-bank powers into unprecedented arenas, the OCC has now proposed major liberalization of the ways in which federally-chartered organizations may use commercial real estate owned as bank premises.

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