



FedFin Daily Briefing

Tuesday, March 30, 2021

BIS Study: Bank Rules Do Not Raise MMF Risk

A new [BIS paper](#) seeks to counter assumptions that post-crisis capital rules limiting bank market-making capacity exacerbate asset-management systemic risk, finding instead that bank rules reduce asset-management instability. The paper deploys a theoretical model to correlate bank rules and redemption risk, assuming herding behavior among asset managers that leads some firms to take undue fire-sale risk despite longstanding assumptions that internal risk-reduction incentives mitigate against it. Prime MMFs are found to be particularly prone to herding, a result sure to intensify work already well underway to govern them in the FSB ([see Client Report NBF1](#)) and U.S. ([see Client Report MMF16](#)).

Although nonbank dealers may be willing to absorb at least some of the risk resulting from the combined impact of herding and capital rules, the paper concludes that regulated banks must charge for doing so, discouraging asset managers from risk and enhancing market welfare. This conclusion to us seems somewhat quixotic given the 2020 crisis, which suggested little such discipline materialized despite the binding impact of bank capital requirements.

Fudge: No FHA Premium Cut on the Horizon

HUD Secretary Fudge [today](#) made clear that HUD will not in the near term reduce FHA premium pricing as many in the industry have urged. Despite the impact of the pandemic on FHA-insured mortgages, the Mutual Mortgage Insurance Fund has remained resilient, although it is threatened by heightened delinquency and forbearance levels. This policy continues GSE competitiveness for high-LTV mortgages, which some fear reduces affordable loans for low-income borrowers due to the GSEs' more stringent credit standards. Secretary Fudge also praised recent Administration moves to extend foreclosure and eviction moratoria as well as additional funding in the recent stimulus package for homeowner assistance.

FSB Continues Fast Track to MMF Rewrite

In [remarks today](#), FRB Vice Chair for Supervision and FSB Chairman Quarles updated FSB priorities, the most immediate of which address NBFIs. The FSB remains on track to publish an MMF-reform consultation in July based on the findings of its holistic review ([see Client Report NBF1](#)). This report will examine the relationship between MMFs and short-term funding markets, with additional NBFIs work on open-end funds taking longer than 2021 to complete. The FSB has now followed up an earlier proposal shifting NBFIs systemic standards from designation to activity/practice ([see FSM Report SIF14](#)) with a decision in favor of activities-based designation, echoing Secretary Yellen's preference for this approach ([see Client Report REFORM204](#)).

Another FSB priority is cross-border payments, on which the FSB plans to issue a consultation in May followed by quantitative goals for the G20 in October. However, Mr. Quarles underscores that cross-border payment system improvements are difficult as underlying frictions often span multiple legal, operational, processing, technological, and structural barriers that also vary by region. Mr. Quarles also reiterated the rest of the [FSB 2021 agenda](#), including reporting on TBTF reform and unwinding COVID support in April, continuing LIBOR-transition work, and advancing CCP reform. Under questioning, he also noted that his views on the countercyclical capital buffer have changed, questioning its effectiveness given that it did not improve lending in jurisdictions that used it last March.

GOP Ramps Up Mandate Pressure on FSOC

Ahead of FSOC's meeting tomorrow, senior HFSC Republicans [today](#) demanded that FSOC Chair Yellen ensure that any discussion of financial risks associated with climate change remain free from "political agendas." This demand reflects continuing GOP pressure most recently [expressed by Sen. Toomey \(R-PA\)](#) that, while it will likely not change FSOC deliberations, nonetheless puts the Administration on the defensive as climate and social-welfare policies advance through financial rulemakings and other actions.

The HFSC letter from the GOP seeks a report from Secretary Yellen within a month on how the Council will fulfill what is described as its proper role: focusing on the resiliency of the financial system, not dictating for private-lending or investment decisions. We expect Secretary Yellen to answer this letter much as she answered Sen. Toomey last week ([see Client Report REFORM204](#)), emphasizing that FSOC does not seek to govern specific private-sector decisions.

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](#).

- [REFORM204](#): Following yesterday's HFSC session ([see Client Report REFORM203](#)), Secretary Yellen and Chairman Powell today faced Senate Banking and, as before, a raft of questions with little to do with the hearing's ostensible focus on CARES Act programs.
- [REFORM203](#): At today's HFSC hearing on pandemic-relief programs, Members asked also about key financial-policy questions.
- [GSE-032321](#): Last week, [we analyzed](#) a Federal Reserve study showing that unemployment is still inexorably linked to mortgage-default risk.
- [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.
- **[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.