



FedFin Client Report

Wednesday, March 24, 2021

Capital Distributions, SIFIs, CBDC and More

Client Report: REFORM204

Executive Summary

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. Many questions again addressed fiscal policy, inflation, and macroeconomic growth. However, as in the House, senators also used the session to broach regulatory concerns. As Secretary Yellen admitted, she has now reversed her opposition to big-bank capital distributions, deeming the sector healthy enough to absorb them. She also committed to review the systemic risk posed by asset managers, noting her preference for activity/practice designation instead of the firm-specific one sought by Sen. Warren (D-MA) for BlackRock. Chairman Powell for the first time came out squarely against FedAccounts, noting the radical change it would make to the Fed's mandate. He did, however, continue to argue that the mandate includes climate risk due to its safety-and-soundness impact. Even so, climate-risk policies will proceed cautiously, an approach even Democrats who once pressed for fast-track stress testing now seem to support.

Analysis

Opening Statements

Chairman Brown (D-OH) urged the FRB to use all of its tools to help workers, highlighting the gap between corporate profits and wages and the impact of the pandemic on minorities and women. Ranking Member Toomey (R-PA) worried that, without a reduction in the FRB's footprint, quantitative easing will monetize government debt, warning also that accommodative policy may lead to inflation.

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Testimony

Today's testimony matched yesterday's at HFSC.

Q&A

- **Systemic Regulation:** As noted, Sen. Warren pushed Secretary Yellen to look at designating large investment firms such as BlackRock, citing the risk she believes they pose to the economy. Ms. Yellen believes designation may not be the correct tool, citing open-end fund risk as evidence of the need to focus on activities rather than the size of investment firms. Sen. Warren then asked if the FSOC will investigate designation, leading the Secretary to commit to doing so.
- **Stock Buybacks:** Chairman Brown asked if stock buybacks promote economic recovery; Ms. Yellen noted that, although she was opposed to the practice earlier in the recovery, she now believes that the renewed health of financial institution allows for capital distribution.
- **Climate Change:** Chairman Brown asked what regulators can do to make the financial system more resilient to climate change; Mr. Powell reiterated that, although the FRB has no specific climate mandate, its safety-and-soundness mandate covers work in this sector. Ms. Yellen agreed that regulators need to assess climate risk. Sen. Cramer (R-ND) worried about government pressure on businesses to make lending decisions; the Secretary noted that, although the government should mitigate risk and encourage financial institutions to think about potential adverse impacts, lending is not regulated.
- **FedAccounts:** Sen. Daines (R-MT) discussed Sen. Brown's proposal to allow the Fed to hold retail and commercial deposits ([see Client Report CBDC](#)), asking if the FRB is equipped to service these accounts; Mr. Powell believes the FRB is not equipped nor permitted under current law to do so, with the Chairman noting that this would be a "dramatic change" to the FRB's role in the economy and would require much careful thought.
- **PPP:** Sen. Menendez (D-NJ) asked if the economy is recovered enough to safely end PPP, arguing it would be "reckless and cruel" to let the program expire; Ms. Yellen supported an extension.
- **Illicit Cash Act:** Sen. Rounds (R-SD) asked if Treasury has a plan to implement beneficial-ownership reporting ([see Client Report AML133](#)). Although Ms. Yellen did not provide a concrete timeline, she noted FinCEN and Treasury are focused on the issue.

- FRB Independence: Sens. Kennedy (R-LA) and Cramer emphasized the importance of the FRB's independence, urging Mr. Powell to resist involvement in social policy; the chairman agreed only that FRB independence is important.
- Community Bank Leverage Ratio: Sen. Cramer asked what factors the FRB will consider when addressing leverage ratio pressures; Mr. Powell noted the FRB is closely monitoring the issue and will give plenty of notice ahead of any changes.
- Housing: Sen. Menendez asked if current mortgage and rental delinquency rates indicate the housing crisis is over; Mr. Powell agreed it is not. Sen. Cortez Masto (D-NV) asked for a timeline for FAQs on recent homeowner assistance; Ms. Yellen could not provide a timeline, but indicated Treasury's commitment to ensuring funds are quickly and effectively distributed.
- Diversity: Sen. Menendez criticized the FRB's lack of diversity, asking if it might be missing material issues because of a lack of diversity; Mr. Powell and Ms. Yellen agreed, both affirming diversity in hiring as a top priority.