



Monday, October 4, 2021

## Fed Staff Study Ratifies GSIB Scoring; We're Not So Sure

Late last week, the Fed published a [new staff note](#) using a novel approach – high-frequency stock trading – to identify SIFIs. Looking to determine if one firm's negative stock return creates market-wide contagion risk in a short time period, the study finds that the eight U.S. designated GSIBs demonstrate this systemic market correlation. The study asserts that this methodology better accounts for negative causality and the inherent correlation risk of financial companies by using lagged returns and a larger data set that includes major nonbanks. Its results have a 38 percent correlation with GSIB scores, increasing to 74 percent when State Street is excluded and using additional regressions. The paper does not explain why State Street's data are so important to its findings; to us, they suggest that the bank's GSIB score may be ill-calculated due to remaining uncertainties about the "substitutability" criterion, but this linkage may also suggest a fundamental robustness problem with the study's methodology. Regardless, the paper uses these conclusions to affirm the current GSIB scoring methodology ([see FSM Report GSIB7](#)) even though it readily acknowledges an array of considerations that to us suggest it is both data and model dependent. Still, as the paper suggests, it may prove useful for assessing nonbank system impact where data limitations or the GSIB methodology are inapplicable.

## USPS Experiments with New Banking Services

Following an *American Prospect* [story](#) today, a number of news sources have confirmed that the U.S. Postal Service has launched a pilot postal-banking proof of concept. Advancing a proposal in the [Democratic platform](#) despite the fact that the Postmaster-General is a controversial Trump holdover, the trial tests several services in four post offices in the Washington area, Baltimore, and the Bronx. The most significant new service is check-cashing, with participating post offices now cashing payroll and business checks up to \$500 at a considerable fee savings. Check proceeds are converted into single-use gift cards, with one news story indicating that no identification was requested when a check was cashed. If this is general practice, postal-banking opponents may well argue that this service facilitates money laundering. Advocates will counter that post offices are critical retail-banking delivery points in the growing number of banking "deserts." Sen. Kirsten Gillibrand (D-NY) also applauded the pilot, saying it also demonstrates the need for the broader services authorized in her longstanding legislation to establish postal banking ([see FSM Report POSTAL9](#)).

## Warren Demands Still More Retribution for Fed Trading Practices

Based in part on [news today](#) that Vice Chairman Clarida also engaged in trading some believe has the appearance of impropriety, Sen. Warren (D-MA) has [expanded her campaign](#) demanding not just a Federal Reserve inquiry, but now also an [SEC investigation](#). She asserts that trading by Messrs. Clarida, Rosengren, and Kaplan may violate rules against insider trading, describing these trades as "personal profiteering." However, Sen. Warren's campaign is not limited to these three officials, asking the SEC also for an investigation of overall investing practices by senior Fed officials. No deadline is given for SEC action and we doubt the Commission will undertake any given the difficulties this would pose for inter-agency action on an array of pending initiatives. However, it makes clear that Sen. Warren is relentless in her efforts not only to impose tougher trading rules on Congress and the Fed, but also to block Mr. Powell's renomination.

## Fed Plans Single-Day Implementation for ISO 20022 in 2023

The FRB [today](#) issued notice that Reserve Banks will adopt the ISO 20022 message format for the Fedwire Funds Service. Although adoption was previously proposed to be phased in, the FRB now intends Reserve Banks to adopt the ISO 20022 message format on a single day no earlier than November 2023. While a specific date is not yet proposed, all Fedwire Funds Service participants would be required to be able to

send and receive fully enhanced ISO 20022 messages on the implementation date, when the proprietary message format currently used would no longer be supported. Comments are sought on support for the single-day implementation strategy, implementation timing, any constraints that could impact implementation readiness, and testing. Comment is due ninety days after *Federal Register* publication.

## Gensler's Next Grilling

Ahead of its hearing with SEC Chair Gensler tomorrow, HFSC's majority [staff memo](#) indicates that the session will cover the full SEC agenda. Mr. Gensler's priority will be the SEC's budget request, as it was when he appeared before Senate Banking last month ([see Client Report PUSH-OUT14](#)). Additional items sure to be considered include payment for order flow and gamification, corporate bond market efficiency, cryptocurrencies, stablecoins, and ESG issues including climate-related financial disclosures for publicly-traded firms and ESG funds. Treasury markets and MMFs are also targeted, although how much time they get given the controversies surrounding almost everything Mr. Gensler does remains to be seen. Democrats may also raise recent Fed trading with Mr. Gensler given Sen. Warren's (D-MA) demand [today](#) for an SEC investigation. The session will also build a legislative record on several draft bills focusing on investor and whistleblower protection.

## Recent Files Available for Downloading

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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](http://www.fedfin.com) or clients may obtain the reports/analyses by e-mailing [info@fedfin.com](mailto:info@fedfin.com) giving the requested item name, firm, and e-mail address. To learn more about *GSE Activity Reports*, click [here](#).

- [CBDC8](#): As we [noted](#) last week, the BIS and seven major central banks have advanced global CBDC policy with three new reports evaluating key design features.
- [GSE-093021a](#): Now that we have FHFA's comment deadline – November 26 – we expand our [initial analysis](#) of FHFA's capital rewrite into a more detailed assessment of its strategic impact.
- [REFORM209](#): In very sharp contrast to the Senate Banking session on Tuesday with Chairman Powell and Secretary Yellen ([see Client Report REFORM208](#)), today's HFSC session was largely devoted to partisan wrangling over monetary policy, the debt ceiling, and the Biden Administration's overall fiscal policy.
- [GSE-093021](#): Late yesterday, Senate Banking Ranking Member Toomey sent letters [to Secretary Yellen](#) and FHFA [Acting Director Thompson](#) strongly protesting the [PSPA rewrite](#) and [pending capital proposal](#).
- [MERGER7](#): In a wide-ranging hearing today, HFSC's Consumer Protection and Financial Institutions Subcommittee showed the extent to which Chairwoman Waters (D-CA) and progressive Democrats are wary of large-bank mergers.
- [REFORM208](#): Although today's Senate Banking hearing with Chairman Powell and Secretary Yellen was largely taken up by the debt ceiling, Sen. Warren (D-MA) made it very clear that progressives will mount an aggressive campaign against Mr. Powell, calling him a "dangerous" man.
- [GSE-092421](#): According to a group of Senate Democrats, the answer to this question for a new class of

federally-backed mortgages is "out of debt."

- **[GSE-092221](#)**: Getting a bit ahead of FHFA's new [equitable-finance mandate and its express demand for appraisal equity](#), Freddie Mac has released a detailed [study](#) of one of the most significant barriers to housing-finance equity: discriminatory appraisal practices that reduce the chances for wealth accumulation.
- **[DATA2](#)**: Today's HFSC Fintech Task Force Hearing featured an appearance by Full Committee Chairwoman Waters (D-CA) arguing against consumer opt-out.
- **[PUSH-OUT14](#)**: As [we noted](#), SEC Chairman Gensler's written Senate Banking [testimony](#) included a short – but very significant – statement prioritizing Commission review of key fixed-income market sectors.
- **[GSE-091621](#)**: As [we noted](#), FHFA wasted no time after the [PSPA revision](#) with its proposed changes to GSE capital [regulation](#).
- **[GSE-091521](#)**: As noted [yesterday](#), Treasury and the FHFA pulled the Trump PSPA's plug, although importantly and widely overlooked is that this is true only when it comes to near-term asset-purchase considerations.
- **[INVESTOR18](#)**: As is often the case, Senate Banking's hearing today with SEC Chairman Gensler did not touch on the fixed-income structure questions highlighted in his [written testimony](#) even though these could be among the most consequential for long-term capital-market regulation and the balance between the Fed and SEC in this key arena.
- **[GSE-091021](#)**: Soaring house prices have of course aroused lofty housing-bubble worries.
- **[GSE-090821](#)**: As Karen Petrou's [Monday memo](#) forecast, FHFA is doubling down on an already-ambitious work plan to make Fannie and Freddie the epitome of mortgage-finance equity.