GSE Activity Report

Thursday, September 22, 2022

The Cryptoverse Has A Big Black Hole

Summary

In this report, we follow our earlier analysis of Treasury's CBDC recommendations and housing finance with an analysis of another Treasury report in response the President's executive order focused on the overall construct of cryptoassets in the U.S. Treasury here makes its views even clearer than it did when favoring a CBDC. It simply sees no "natural use case" for cryptoassets or cryptocurrency beyond speculation in the lending and investment arenas where, it states, very stringent rules should quickly spoil the funding. This isn't to say that Treasury disses digital assets – quite the contrary – but its views on cryptoassets make clear that crypto-mortgages are a long, long way away if they are anywhere at all.

Impact

As our in-depth analysis of Treasury's new crypto-policy makes clear, Treasury has taken an unequivocal stand against giving crypto companies the open field granted to them so far in the name of advancing innovation at a scale still too small to pose systemic risk. Treasury's thinking on financial stability will come in a subsequent report, but its findings in this one are that crypto even at a scale still more or less miniscule compared to the financial system as a whole is still too much crypto without regulatory constraint.

Treasury reaches this conclusion by virtue of its analysis of structural, operational, market-integrity, and liquidity risk across an array of cryptocurrency and asset products. Given this, Treasury urges all of the relevant regulators to go beyond the enforcement tactics that have controversially characterized the SEC and, to a lesser extent, banking agencies. They want lots of tough enforcement, but also a new era of regulatory certainty. Although Treasury does not take a stand on the jurisdictional battle between the SEC and CFTC, its crypto-critical views align far more closely with Chairman Gensler than his colleague at the CFTC, Rostin Behnam.

Treasury also focuses directly on vulnerable consumers, going beyond its overall assessment of depositor, borrower, and investor exposures also to conclude that crypto products pose so much risk to so many that none should be offered without a lot more restrictions from the CFPB, FTC, and anyone else with power to inflict them. These concerns are of course of direct relevance to any consumer-facing housing-finance product.

Outlook

Treasury's grim assessment of crypto-finance does not extend to digital finance conducted in well-regulated companies. The report also notes an array of high-impact digital settlement, clearing, and processing products already demonstrating considerable efficiency and finality benefit. Based on this and the Treasury results briefly summarized above, we conclude that the GSEs, FHA, and Ginnie can and perhaps even should proceed with DLT or other forms of smart-contract products that facilitate the

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secondary-market backroom and/or mortgage guarantee and insurance process. Coin-based products in permission-based systems akin to JPM's wholesale-processing system could be of particular interest given the market appeal of a "GSE coin" or similar medium of exchange given the GSEs' status and the size of its market universe.

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