FedFin Daily Briefing

Friday, November 4, 2022

Big Banks Pressed on Sluggish, Inequitable Deposit-Rate Hikes

Advancing an initiative with political "legs," Sen. Jack Reed (D-RI) has demanded answers from the nation's largest banks on why small-deposit rates have barely budged even as the Fed sharply hiked interest rates now reflected in higher loan costs. Building on questioning at September's Senate Banking hearing (see *Client Report* **REFORM213**), Sen Reed's letters differs for each bank only by the rates and revenue data he cites. All of the letters argue that disparities between short-term savings account rates for small-balance accounts and those for longer-term, higher-minimum funds are "exploiting" higher rates to benefit executives and shareholders at grave cost to average households. The letters also note that some smaller banks are now paying higher rates to transaction or overnight savings products, asking each of the largest-bank CEOs to respond to Mr. Reed's charges by November 23. Earlier this year, CFPB Director Chopra asserted that bank failure to raise deposit rates might be an unfair or abusive practice (see *Client Report* **CONSUMER40**). If the Bureau has any bandwidth, it is likely to return to this issue now that a Senate Democratic leader has done so.

FRB-NY Official Details Wholesale CBDC Prototype

Remarks today from a senior FRB-NY official, Michelle Neal, continued the Fed's ambivalent stand on a CBDC (see FSM Report **CBDC10**). However, she goes on to describe Project Cedar, a wholesale CBDC experiment exploring the settlement of foreign exchange transactions. The New York Fed project developed a prototype wholesale CBDC that settles transactions in fewer than ten seconds, designed modularly to allow for scalability. This a part of ongoing FRB-NY research to define the potential technical design for wholesale CBDCs specific to the Fed's context, differentiating it from ongoing BIS pilots.

Fed Fixes Advanced-Approach Glitches

The FRB is proposing to implement three changes to Regulation Q data collection/disclosure rules governing advanced-approach capital adequacy at BHCs, SLHCs, and state member banks. This process is largely formal as the Board has approved these requirements in practice. The first change would more clearly require Board approval of internally-set haircuts on financial collateral used as credit risk mitigation and on any changes to the stress assumptions on which these haircuts are set. The second change affects the public notices required when an advanced-approach banking organization acquires a bank using the standardized approach, allowing the acquirer to calculate the target's capital under the SA. Finally, anti-evasion provisions related to capital adequacy applicable to advanced-approach BHCs would govern SLHCs. Comment is due by January 3.

Fed to Name Master-Account Names

Reflecting ongoing concerns on Capitol Hill, the Fed is proposing to make what our analysis suggests were opaque payment-system access guidelines (see FSM Report **PAYMENT24**) "a bit more transparent." It has thus released a proposal requiring Reserve Banks to release a quarterly list of institutions granted master accounts, a move which does not make clearer the criteria for doing so but would address complaints that failure even to name names obscured critical market and Fed-process information. Preliminary review does not indicate if the list would differentiate depository from non-depository institutions, a process that would make it easier quickly to spot non-traditional institutions with payment-system access, but the Board has decided on a list rather than a searchable database due to technical considerations. We will shortly provide clients with an in-depth analysis, on which comment is due sixty days after *Federal Register* publication.

Toomey Presses for SLR Rewrite

Ranking Senate Banking Member Toomey (R-PA) today released his letter to Chairman Powell cautioning the central bank not to handle any Treasury-market liquidity events with new backstop facilities. To the extent that illiquidity derives from factors such as more Treasury debt and/or bank leverage rules, Sen. Toomey urges structural reform, not intervention. In particular, the Fed should follow through with its 2020 promise to review the SLR, noting that the rules restored after the worst of the 2020 crisis now encourage large banks to take additional risk. The letter also urges the Fed to treat reserves and Treasury obligations as HQLA equivalents. Sen. Toomey also urges the Fed to look deeper at the all-to-all trading initially favored by Vice Chair Brainard. Answers are requested by November 17 to questions not only on these policies, but also on how the Fed differentiates systemic market risk from Treasury-market volatility, noting that volatility provides necessary price information, not a signal of imminent collapse.

Waters Adds To Fed's Political Woes

In a letter today, HFSC Chairwoman Waters (D-CA) joined Sens. Warren (D-MA), Brown (D-OH), and Hickenlooper (D-CO) in sharply criticizing the recent Fed "super-sized" rate hike. As with the other letters, Chairwoman Waters argues that corporate profiteering and temporary supply-chain problems are exacerbating inflation which will ease of its own accord without the need to strain low-and-middle -income households or risk a recession. She focuses in particular on housing, noting that rate hikes increase inflation, apparently confusing mortgage-payment increases with the house-price ones usually used to measure inflation in this sector. The letter includes no questions or other requested responses, but signals yet again that Democratic political pressure is growing on the Fed in the wake of yet another rate hike and despite some suggestions on Wednesday that the rate of increase may slow as soon as December. As we have noted, Democrats are increasingly fearful of severe midterm losses due in large part to inflation and may be less willing to spare the Fed to save the Biden Administration in its wake.

Fed Worry Level Goes Up

The Federal Reserve likely hoped for the torpor of a Friday afternoon to quell frightened replies to the latest financial-stability report released today. As Vice Chair Brainard's accompanying statement indicates, the report notes the sharp risk increases many observers and market participants have identified, although the report reaches no overall high-level conclusion about the current systemic-risks level. House-price drops are a strong concern as is Treasury and financial-market illiquidity. "Hidden leverage" also has come to be what seems a permanent Fed concern, but it is stressed still more emphatically in this report. We will shortly provide clients with an in-depth analysis of the paper's conclusions and financial-policy implications. The readout also release this afternoon by Secretary Yellen following the closed FSOC meeting says little beyond the fact that the Council heard a New York Fed report on market vulnerabilities.

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

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.

- **DATA3:** Beginning a long-awaited rulemaking process on the extent to which consumers have rights to their own data and how these rights may be exercised, the CFPB is seeking views on an array of ideas and questions to guide future action.
- **OVERDRAFT11:** In conjunction with a Presidential speech and new White House initiative against "junk fees," the CFPB has accelerated its own efforts in this arena with two new policy directives.
- **GSE-102522:** As we noted yesterday, FHFA has decided not only to unbundle second and high-dollar loans from its flat-fee paradigm, but now to do the same for about one in five conventional conforming purchase loans outside these categories.
- **DEPOSITINSURANCE116:** The FDIC has finalized its proposal largely unchanged to raise base Deposit Insurance Fund (DIF) assessments by two basis points (bps) to replenish the DIF by the statutory deadline to reflect deposit inflows that the FDIC no longer expects to be temporary.
- **RESOLVE48:** The FRB and FDIC have moved beyond the resolution-planning requirements mandated in the Dodd-Frank Act then implemented over the years to what could be a new resolution regime for banking organizations considered category II or III companies under the inter-agency tailoring rules.
- **MERGER11:** As promised, this analysis focuses on the OCC and FRB approvals of the acquisition by U.S. Bancorp of MUFG's Union Bank in California.
- **DEPOSITINSURANCE115:** The FDIC board today voted 3-0 to increase DIF assessment rates by 2bps, finalizing its proposal (see FSM Report **DEPOSITINSURANCE114**) and rejecting industry arguments on grounds that a small DIF premium increase now would make a more damaging procyclical assessment increase under adverse economic conditions less likely.
- **CRYPTO34:** Speaking for global banking, securities, and insurance regulators, the Financial Stability Board has taken its firmest stand to date on cryptoassets and outlined high-level and often principles-based global standards to govern them going forward.
- **INTERCHANGE11:** Leaving its interchange-fee restrictions intact – at least for now – the Federal Reserve has finalized its proposal expanding on its existing requirement that all debit- card transactions must be enabled for processing on at least two unaffiliated payment-card networks for card-not-present transactions.
- **GSE-100622:** FHA's request for input on small-dollar loans could mean much for this equality-essential product or little beyond a lot more public debate.
- **CRYPTO33:** In this report, we build on our initial assessment of FSOC's conclusion that cryptoassets now pose systemic risk and the Council's recommendations about what should be done to curtail it.

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