# GSE Activity Report

**Monday, November 21, 2022**

# *We're Starting to See SIFIs*

## Summary

As came out into the open last week, FSOC will finally turn to rewriting the Trump era rewrite of the Obama Administration's FSOC protocols regarding systemic financial institutions and activities. Could the SIFI reaper be coming for Fannie and Freddie? We doubt it, but then again...

## Impact

When the Trump FSOC's systemic standards were finalized, then-FHFA Director Calabria went out of his way to emphasize that Fannie and Freddie might warrant designation. We thought this improbable at the time for as long as the conservatorships lasted not only due to the new, elaborate proceedings required to designate any company as a systemically-important financial institution (SIFI), but also because the Fed – which is each SIFI's uber-regulator – had no interest in taking them on in light of Calabria's capital rewrite and the many other Fed-like rules that were then in the works.

As far as we can tell, the Fed has no more appetite now to govern Fannie and Freddie atop FHFA than it did in the last decade. However, the White House faces a significant dilemma if it wants to recraft the GSEs for the post-conservatorship future that FHFA hopes is ever nearer thanks to rising capitalization levels: the continuing impossibility of enacting anything via statutory change. Now that the FHFA director serves at the pleasure of the president, Fannie and Freddie could be cast in a very different role in the next Administration should that be another one led by a Republican, especially a Republican of the ilk likely to be nominated in 2024 by the GOP.

Advocates of GSE designation believe, as Mel Watt did before mark Calabria, that SIFI designation would create a construct in which other companies might come to challenge Fannie and Freddie. To us this seems as far-fetched now as it did then because of the awesome advantages of GSE incumbency and the impossibility of giving any new entrant any form of a US guarantee without statutory change.

We also doubt FHFA has much enthusiasm for reporting to the Fed unless – and this is a super-big except – if FHFA is persuaded that the only way to preserve the current equitable-finance regime is via SIFI designation insulating these requirements unless or until another FSOC follows the Trump approach and de-designates anyone designated by its predecessor.

To be sure, one credible argument we have heard for designating the GSEs as SIFIs is that it would permit FHFA more quickly to end the conservatorships via contractual rewrite with Treasury ahead of any budget-balancing plans Republicans are able to enact trying to put the GSEs on-budget and sell off all the warrants. Both approaches would generate tidy hauls, hauls that might come in handy even if a bit smaller but implemented instead by contractual changes that keep the GSEs off budget but recapture Treasury's warrants. The Treasury line could be allowed to drop if markets are convinced – as they easily could come be – that any GSE that hits the wall would be rescued via Dodd-Frank's

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orderly-liquidation authority (OLA) provisions. These didn't exist in 2008 and thus couldn't have been deployed at the time. Now, they do and authorize the FDIC to provide unlimited support to a systemic failure as long as prior clearances have been obtained as they likely would quickly be in a crisis.

## Outlook

Is GSE designation what the White House wants via the imminent rewrite of SIFI-designation standards? We think it's part of what's wanted as at least an option, but it's important to remember also that OLA can be deployed even if a financial company hasn't previously been designated by Treasury and the White House thinking its failure could cause a systemic crisis. We think the new Biden SIFI standards are largely aimed at reinstating systemic activity-and-practice designation options so these can be deployed for other purposes and/or entities. Who's on the list? Some have told us it's Citadel and other giant brokers unlikely to get what Gary Gensler thinks is their due via his PFOF rules. Stablecoin issuers are another very of-the-moment target and progressives are also pushing for sweeping, if largely unenforceable, systemic standards for fossil-fuel lending and related climate-risk activities. Word comes to us every now and then also of systemic activity-and-practice designation for nonbank mortgage companies, but this genie seems largely back in its bottle.

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