FedFin Daily Briefing

Thursday, October 19, 2023

OIG Blasts FDIC's Crypto-Policy Delay

Late yesterday, the FDIC's Office of Inspector General (OIG) issued a report critical of the FDIC's supervisory crypto policy. Although the OIG does not say so, its findings are particularly interesting in light of continuing indications that barriers to inter-agency U.S. standards come from the FDIC. The OIG found that the FDIC has only begun to develop crypto policies. Further, the FDIC adopted "pause" requirements in 2022 and again in 2023 for FDIC-supervised banks with crypto activities, but did not then establish a timeframe for evaluating paused activities or make clear when its review ended. The OIG notes also that the absence of clear FDIC policy may lead it to miss key risks and/or FDIC-supervised institutions to take undue ones in this sector. Signature Bank is one case in point, as the FDIC's analysis of this failure itself makes clear (see *Client Report* **REFORM222**). The FDIC agreed with the OIG and promises to improve its policies by the end of January of 2024.

Fed May Signal Possible Compromise as GOP Barr Demands Capital Answers

Amid press reports that Chair Powell has implicitly promised capital-rule compromise, HFSC Financial Institutions Chair Barr (R-KY) released a letter today pressing Vice Chair Barr still harder on the cost-benefit analytical (CBA) and cumulative-impact issues raised at the September hearing at which Karen Petrou testified. Rep. Barr says that Vice Chair Barr's response to a letter seeking CBA details was wholly non-responsive, now reiterating his initial request on the end-game, GSIB-surcharge and other proposals and demanding a reply in thirty days.

Fed Data Show Increases in Household Financial Resilience, Profound Home-Affordability Gap

The Federal Reserve yesterday released its triennial Survey of Consumer Finances (SCF). As always, we here highlight data with financial-policy implications; Petrou blogs and other releases will update economic-equality indicators. Unsurprisingly, the overall SCF found significant gains in household wealth regardless of income or demographics due to pandemic-related stimuli and economic growth. Although income inequality still widened, households making use of payday loans slipped to two percent – the lowest level in the SCF's history. Households with transaction or other accounts (including prepaid cards) rose to 98 percent, an interesting indicator despite continuing concerns about the levels of un- and under-banked households as measured differently by the FDIC. Although the home-ownership rate slightly increased, median net housing value rose 44.5 percent due to rising house values and steady debt loads despite all the refi (doubtless because much of this was for cash-out and/or higher principal obligations). These housing values are historic and were evident across all income levels, but corresponding housing affordability also fell to historic lows, and with the median home worth more than 4.6 times median household income.

BIS Head Calls for Review of Large Bank Supervision

BIS General Manager Agustin Carstens today said that the mid-March failures show the need for nations to review how they supervise larger banks, specifically highlighting liquidity risk and setting frameworks for emergency liquidity assistance. Reflecting recent FSB and Basel doubts (see *Client Report* **REFORM228**) re AT1 contingent capital, Mr. Carstens also called for improving bail-in credibility via better disclosures of AT1 instruments. More work is also needed on cross-border resolution cooperation.

OCC Analysis Shows Broad IRR Resilience With Startling Risk Pockets

Showing some pockets of severe risk but overall resilience, the OCC today released a statistical analysis of interest rate risk based on projected changes in twelve-month net interest income as well as the economic value of equity in parallel interest rate shock scenarios ranging from -200 basis points to +400 bps. Although the data show resilience across the industry as a whole regardless of size, distributional analysis shows significant outliers and potential problems. For example, across all banks, the largest loss in the economic value of equity based on a 400-bps rise was -93 percent while the median was -11 percent. For large banks – those with $10 billion or more in assets – the largest economic value of equity loss was -56 percent while the median was -13 percent. The OCC also examines earnings risk, finding less dramatic shocks with a 400 bps increase across the median for larger banks of 4 percent, with one bank experiencing a -26% hit. The OCC also looks at a -200 bps drop in rates, with bank exposures from both an earnings and equity perspective less dramatic under these scenarios.

CFPB Thinks Big on Open Banking

As anticipated, the CFPB today advanced from a review of consumer data rights (see FSM Report **DATA3**) to a specific "open banking" proposal. We will shortly provide clients with an in-depth analysis of standards Director Chopra believes will make it possible for consumers to walk away from poor bank service epitomized by low savings rates as interest-rates rose and better community-bank competitiveness. The proposal principally covers banks but now brings in any entity offering transaction account services on technology such as prepaid cards and digital wallets. Credit cards are also considered transactional accounts for purposes of the proposal and these accounts would thus also come under new protections; mortgage servicing would not despite a statement from Mr. Chopra that it is characterized by customer abuse limiting provider choice.

The proposal also includes strong personal-privacy and data-rights protections, for example banning use of consumer data for anything other than satisfying express customer requests. Mr. Chopra says that these prohibitions also prevent use of personal financial data for algorithmic purposes such as digital marketing, but bigtech and payment firms doing that are currently most adept and aggressive in these arenas would not be covered by the CFPB's standards unless they also offered transaction accounts or credit cards. The proposal would prevent screen-scraping as a principal data-transfer mode, but the extent to which it could still be used and resulting security challenges will be among the issues on which FedFin focuses in our in-depth assessment. Although our initial assessment leads us to conclude that fintechs are covered by the proposal if they offer covered products, the application of standards only to large providers may functionally exempt them; again, we will assess this key strategic question along with the CFPB's plans to expand its data-rights requirements, limit fees, and cover additional entities. Comments are due by December 29.

Barr Lays Out New Stress-Test Construct

Building on his prior comments about stress-test challenges at a hearing in May (see *Client Report* **REFORM224**), FRB Vice Chair Barr today outlined the Fed's plans for incorporating multiple stress

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tests in supervision and capital regulation. Exploratory macroeconomic scenarios and additional market shocks are being developed for next year's stress tests, although Mr. Barr highlighted that any use of these tests that directly affect capital requirements will be implemented via a "transparent, public" process – whether this is one incorporating public notice-and-comment was not made clear. Mr. Barr also emphasized that some new tests – e.g., re bank risk management – will affect supervisory assessments and broader Fed thinking on financial stability. Separately, Mr. Barr strongly pushed back against assertions that the agencies' capital proposal (see FSM Report **CAPITAL230**) will lead to risk double-counting, calling this conceptually incorrect on grounds that risk-weights determine minimum RBC while stress tests determine buffers above that minimum. The Vice Chair also called for further research on social media's role in bank stress as well as agent-based models and network approaches for understanding financial risk and contagion effects. The Fed is broadly seeking comment from stakeholders and academics on stress testing, although Mr. Barr did not provide a timeline or specific questions on which comment is particularly sought.

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.

- **DEPOSITINSURANCE122:** Bipartisan senators have introduced legislation to provide FDIC coverage for certain noninterest-bearing transaction accounts, a move designed to prevent the stress and potential systemic risk evident when Silicon Valley and Signature Banks failed in March.
- **GSE-101723:** As we noted earlier this month, the Federal Reserve inserted a significant capital provision for credit-linked notes in an otherwise-obscure FAQ.
- **GSE-101623:** The White House today rolled out a new housing plan that smacks mightily of many old housing plans.
- **GSE-101323a:** With smaller lenders today joining MBA, NAR, and HomeBuilders' campaign to squeeze the 30-10 spread, we take a look at the odds the White House, Fed, or Treasury will do as hoped.
- **GSE-101323:** As we noted yesterday, OMB's Office of Information and Regulatory Affairs (OIRA) has pronounced a new pro-competition standard for all existing and prospective federal regulations.
- **CONSUMER52:** Using its advisory process to issue guidance that may lead to enforcement actions, the Bureau has for the first time set standards for the obligations of large banks and credit unions to respond to certain consumer inquiries.
- **REFORM228:** As we noted yesterday, the Basel Committee's October meeting concluded not only with plans for new disclosure consultations, but also a report on lessons learned from the 2023 crisis.
- **GSE-100223:** As we noted earlier today, the FRB has issued a seemingly technical FAQ liberalizing the treatment of certain credit-linked notes.
- **GSE-092523:** In her Congressional testimony last week, FedFin managing partner Karen Petrou

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focused on the unintended consequences wrought by new banking proposal based on their cumulative impact.

- **GSE-092023:** Or maybe it is, but not everyone has heard.

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