FedFin Daily Briefing

Monday, June 24, 2024

FHFA Gives Freddie Yellow Light on New Home-Equity Product

Late Friday, FHFA conditionally approved Freddie's request to provide second mortgages backed by home equity, a product that substitutes for HELOCs. As we noted in our initial in-depth analysis of FHFA's request for comment, this new program is in some respects limited in ways that make it easier for lower-income households to draw on equity without a refi, but the product also has considerable market consequences given the scope of Freddie's operations and the even larger ones at Fannie sure to follow Freddie's lead once FHFA allows it. Given this, the final approval – required under time limits set in law for an FHFA decision – is not only conditional, but also limited to a small percentage of possible Freddie volume and lasts for only eighteen months. These and other restrictions are doubtless intended not only to address competitive concerns, but also the broader mission-compliance criticism the program drew from GOP members of Congress. We will shortly provide clients with an in-depth analysis of the FHFA's action and its market and policy consequences.

Chopra Says Network-Based Competitors Threaten Economic Freedom

In remarks to the Federalist Society last week, CFPB Director Chopra linked the concerns about financial "censorship" outlined before Congress earlier this month (see *Client Reports* **CONSUMER58** and **CONSUMER59**) to his longstanding opposition to concentrated market power. Reiterating concerns not only about Venmo, but also Visa and MasterCard, Mr. Chopra said these payment-service firms operate outside the reach of democratic norms much like powerful entities linked to the Chinese government. Drawing a link between today's network-based competitors and those addressed in the Packers and Stockyards Act of 1921 And the Communications Act of 1934, he argued that U.S. companies with de facto control over critical payment infrastructure now threaten economic liberty much as network-based monopolies did over a century ago. Remedies to these threats are said to include the CFPB's pending open-banking rule (see FSM Report **DATA4**), but Mr. Chopra argued that the threat of network- and algorithm-based threats to economic liberty are even more profound than the ability now of large financial-services companies to preclude portability. He does not go on to say what else he believes needs to be done, but Bureau and FTC work underway on both product terms and conditions and payment market power appear to be part of his preferred solution.

FRB-NY Post: NBFI/Bank Correlations Pose Systemic Risk

Building on its posts last week about NBFI risk, the Federal Reserve Bank of New York's blog on Thursday released a final post on a prior paper's conclusions that NBFIs pose systemic risk. Correlated risk between banks and NBFIs is found to have grown from about 65 percent before the GFC to eighty percent now thanks to significant acceleration since the pandemic and again following SVB's failure. While bank/NBFI inter-connections may lead to direct-risk migration, these correlations are found to pose fire-sale and related risk of market shock. The post also lays out how stresses due to bank/NBFI connections could quickly propagate into non-financial firms and the broader economy. As noted last week, the Fed is expanding the data it seeks on NBFI/bank exposures doubtless due to these concerns, concerns backed by much recent global regulatory work on NBFIs. Current single-counterparty credit concentration standards (see FSM Report **CONCENTRATION11**) are not designed for NBFIs; if the new Fed data validate growing concern, regulatory changes in this and other areas are likely to follow.

FedFin Assessment: New ILC Doesn't Mean More ILCs

We have reviewed the process by which the FDIC late last week approved an ILC charter for a subsidiary to TFL, a Fortune 500 company focused only on providing financial services owned in whole by a religious organization (the Lutheran Church). Notably, TFL now provides financial services to any customer, not just those affiliated with its church, but it also provides nonfinancial services that are impermissible for a BHC. TFL could not, however, become a BHC by virtue of its structure. As with GM's decision to withdraw its ILC application last week even though Utah approved it along with TFL, the unique nature of this application makes it of no precedential value for other entities seeking to establish ILCs under an FDIC and Administration generally opposed to them. TFL's decision to merge its large credit union into the new ILC – also approved by the FDIC board – is similarly not a precedent for other credit unions. The new ILC remains tax-exempt despite its corporate status by virtue of its non-profit operations. Chair Gruenberg's statement accompanying the approval notes that the new ILC could be a useful competitor due to its plans to offer an array of online banking services to the general public, although Acting Comptroller Hsu called the resulting ILC the equivalent of a community bank. The statement also lays out how TFL satisfied the FDIC's requirements to demonstrate its ability to serve as a source of strength for the ILC (see FSM Report **ILC15**).

OCC Toughens Recovery-Planning Guidelines

The OCC today proposed to rewrite its own recovery-planning standards for insured banking organizations under its jurisdiction. This proposal differs from the final FDIC resolution-planning standards released last week and pending FRB/FDIC resolution requirements (see FSM Report **LIVINGWILL22**), focusing as it does on recovery in order to, the agency hopes, avert resolution. The rule builds on the OCC's 2015 recovery guidelines (see FSM Report **RESOLVE41**), revised in 2018 to cover only affected banks with assets over $250 billion. Reversing this threshold as the agencies have done since the 2023 failures, the proposal would drop the floor for banks filing recovery plans to $100 billion. It also toughens the 2015 guidelines to mandate testing and makes other substantive changes we will address in a forthcoming in-depth report. Comments are due thirty days after publication in the *Federal Register.*

Stress-Test Hearing Tries to Set Tone for Stress-Test Results

Although the HFSC subcommittee memo ahead of Wednesday's hearing on stress testing contains little new, the hearing is clearly intended to set the tone of discourse on this year's results and lay pipe for next year. The memo does note that the hearing establishes a record for a bill to be introduced mandating "fair audits" of bank examination processes. The panel will also consider a bill already reported on a partisan vote from the full committee forcing significant changes and more transparency in the FRB's stress-test process (see *Client Report* **STRESS32**). The hearing comes the same day the Fed is set to release the results of this year's tests that then fold into each large bank's SCB, with the hearing clearly designed to cast doubt on stress-test results in a year when analysts expect them to reduce capital distributions at least at some large banks. This the hearing may well do, but the markets will focus on results and Senate Democrats will block further action on the bill if it passes the House.

Yellen Demands More FHLB AHP

In campaign-focused remarks today, Treasury Secretary Yellen announced additional Biden Administration programs to support housing supply. She also called on Federal Home Loan Banks to hike their AHP contributions above the voluntary fifteen percent to which the System is already committed in the face of ongoing FHFA pressure. Ms. Yellen wants the Banks to dedicate twenty percent or more to affordable housing and to focus on new construction. We expect the System to balk at still higher AHP contributions but agree to focus funds more closely on new construction.

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.

- **GSE-062424:** Late Friday afternoon, FHFA hoped quietly to announce that, while it was approving the gist of Freddie's request to purchase certain closed-end second liens, it heard many critics and would sharply curtail the approval and, should it go any farther, seek still more public comment.

- **CONSUMER59:** Although today's HFSC hearing with CFPB Director Chopra opened with partisan fireworks, the panel quickly got down to substantive debate on issues such as the Bureau's open-banking proposal (see FSM Report **DATA4**) and data privacy.

- **CONSUMER58:** As anticipated, Senate Banking Republicans today grilled CFPB Director Chopra about the agency's funding.

- **AI6:** Although pressed by Congress to reach conclusions about AI's risk in the financial sectors, Treasury is following up the worries in the most recent FSOC report with only a request for information (RFI) from the public.

- **CONSUMER57:** Deciding against finalizing a proposal to require a registry from nonbanks of their contractual terms, the CFPB has instead issued a circular – i.e., a de facto rulemaking – telling both banks and nonbanks and their service providers that contractual terms and conditions may not require consumers to waive rights to which they are entitled under applicable state or federal law or which the Bureau believes likely to be "unenforceable."

- **GSE-060524:** As anticipated, the CFPB has advanced its campaign to quell mortgage closing costs.

- **LIQUIDITY35:** In addition to controversial provisions affecting bank-merger applications and stress-test transparency, legislation recently approved by the House Financial Services Committee includes a less-contentious provision forcing the Federal Reserve to reckon with longstanding problems affecting the use of its discount window, especially under stress conditions.

- **STRESS33:** Legislation passed by the House Financial Services Committee would require the Federal Reserve to open the stress-test methodology behind the stress-capital buffer (SCB).

- **MERGER17:** New legislation approved largely on partisan lines in the House Financial Services Committee would force federal banking agencies to recraft bank-merger policy to increase procedural certainty and reduce the influence of third parties in both approval-review process and substance.

- **CREDITCARD38:** Using one of its tools for edicts without a formal rulemaking, the CFPB has issued an "interpretive rule" governing BNPL issuers as card issuers for purposes of the rules governing credit cards in areas such as periodic statements and dispute resolution.

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