Federal Reserve Official Statements on Macro Prudential Reforms

CAFIN Conference UC Santa Cruz
April 25-26, 2014

Mark M. Spiegel
Vice President
Federal Reserve Bank of San Francisco

Views expressed are my own and not those of the Federal Reserve
Liquidity concerns

• Yellen 4/15 FRB Atlanta:
  – Maturity transformation is central part of economic function of banks
  – But exposes system to liquidity risk

• Short-term creditors ran from Northern Rock, Bear Stearns, Lehman Brothers, money market mutual funds and asset-backed CP

• “Primary engine” of financial crisis
Policy responses

• BCBS strengthened capital requirements
  – Concentrate on assets
  – Don’t directly address liquidity risk

• Formal liquidity standards
  – LCR: Have enough liquidity to withstand 30-day stress scenario
  – NSFR: Banks with less liquid assets need enough stable funding for a 1-year horizon
What’s missing

• Yellen: “LCR and NSFR ... do not fully address ... short-term wholesale funding”
  – Focus on liquidity positions in isolation
  – Don’t apply to shadow banks
• Also looking at measures to limit reliance of largest banks on wholesale funding
• Minimum margin requirements for repurchase agreements and other could “at least in principle” apply on a marketwide basis.
Lopez Spiegel (2014) supports systemic concerns

• Identify spillovers in funding practices at national level
  – Bank profits increasing in NSFR of national banking systems
  – Also in stability of asset side of balance sheets of rest of banking system

• Only so much liquidity in system
  – Prudent funding and lending decisions at bank level depend on rest of system
Daniel Plainview: “I drink your milkshake”
Large bank growth raises spillover concerns

**Assets of Top 3 and Top 10 Global Banks as a Percent of Global GDP**

<table>
<thead>
<tr>
<th>Year</th>
<th>Top 3 Banks</th>
<th>Remaining Top 10 Banks</th>
</tr>
</thead>
<tbody>
<tr>
<td>1974</td>
<td>8%</td>
<td>3%</td>
</tr>
<tr>
<td>1988</td>
<td>15%</td>
<td>6%</td>
</tr>
<tr>
<td>1997</td>
<td>16%</td>
<td>6%</td>
</tr>
<tr>
<td>2007</td>
<td>43%</td>
<td>17%</td>
</tr>
<tr>
<td>2013</td>
<td>33%</td>
<td>11%</td>
</tr>
</tbody>
</table>

Sources: Bank quarterly and annual reports, *The Banker* rankings, and staff estimates.
Large financial institutions

• Important source of vulnerability
• Don’t answer to a single regulator
• Major strengthening of capital and liquidity requirements have occurred
  – Including surcharge for global systemic banks
• Not all implemented yet
• Tarullo: More to be done, including additional measures to deal with run risks associated with short-term wholesale funding
Strength of home government backstop?

Assets of Top 3 Global Banks as a Percent of Home Country GDP

Percent of Home Country GDP

<table>
<thead>
<tr>
<th>Year</th>
<th>BankAmerica (US)</th>
<th>Citicorp (US)</th>
<th>Chase Manhattan (US)</th>
<th>RBS (UK)</th>
<th>Deutsche (GER)</th>
<th>BNP Paribas (FRA)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1974</td>
<td>4%</td>
<td>4%</td>
<td>3%</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2007</td>
<td></td>
<td></td>
<td></td>
<td>134%</td>
<td>89%</td>
<td>96%</td>
</tr>
</tbody>
</table>

Sources: Bank quarterly and annual reports and *The Banker* rankings.
Conclusion

• Much has been done since the crisis
  – Renewed focus on liquidity, as measured by LCR and NSFR
  – Greater awareness of issues at system level

• Regulatory arbitrage remains a concern
  – Shadow banking
  – International regulatory differences
Thanks