Federal Reserve
Bank of Boston®

Financial Stability

Eric S. Rosengren
President & CEO
Federal Reserve Bank of Boston

Official Monetary and Financial Institutions Forum

Fed Week: Financial Stability Session

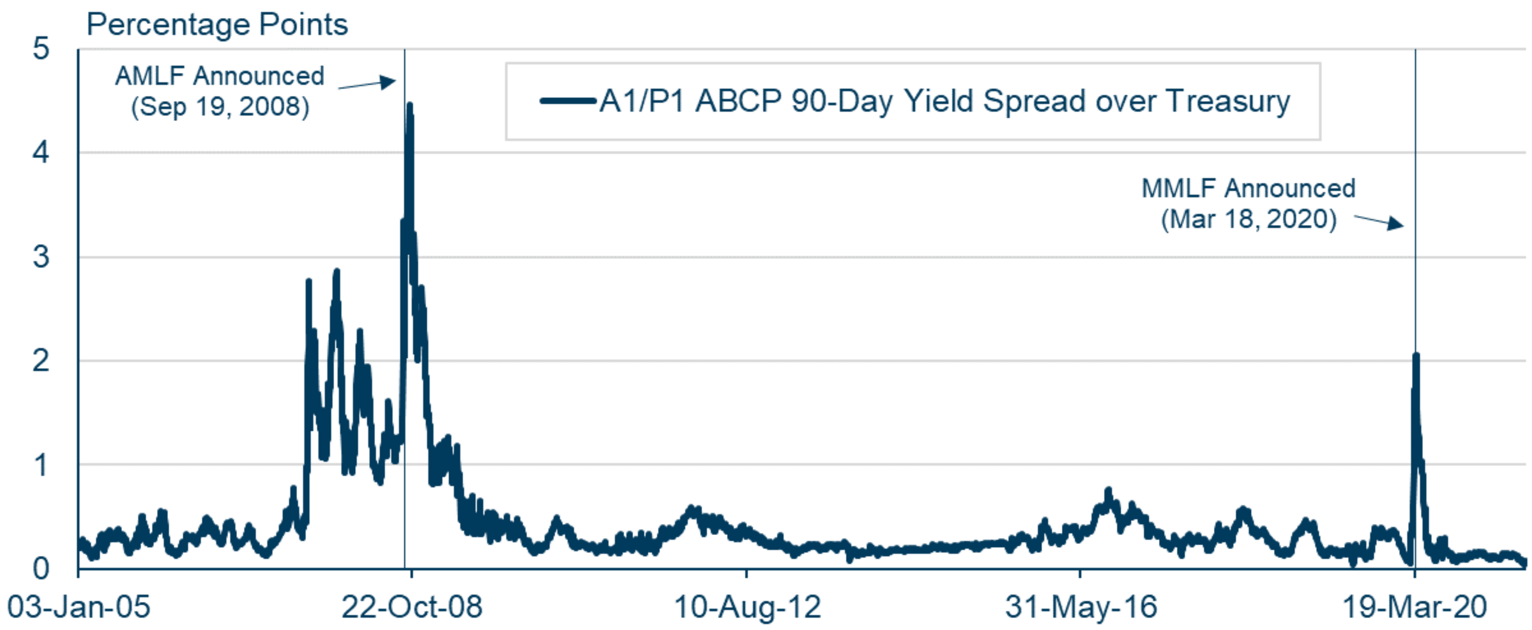
June 25, 2021

Exploring Three Financial Stability Challenges

- Periodic disruptions to short-term credit markets
  - Role of Money Market Mutual Funds (MMMFs)
  - Other potential cash management alternatives
  - New disruptors – for example Tether
- Need for emergency lending facilities and regulatory changes in crises
  - Extraordinary actions were required
  - Despite efforts, many programs seem better suited to larger institutions and firms
  - Need a less ad hoc approach
- Possible risks in housing
  - Residential housing prices showing some exuberance
  - Real estate has played a role in financial stability problems in the past

Figure 1: Spread Between 90-Day Highly-Rated Asset-Backed Commercial Paper Yield and the 3-Month Treasury Yield

January 3, 2005 - June 23, 2021

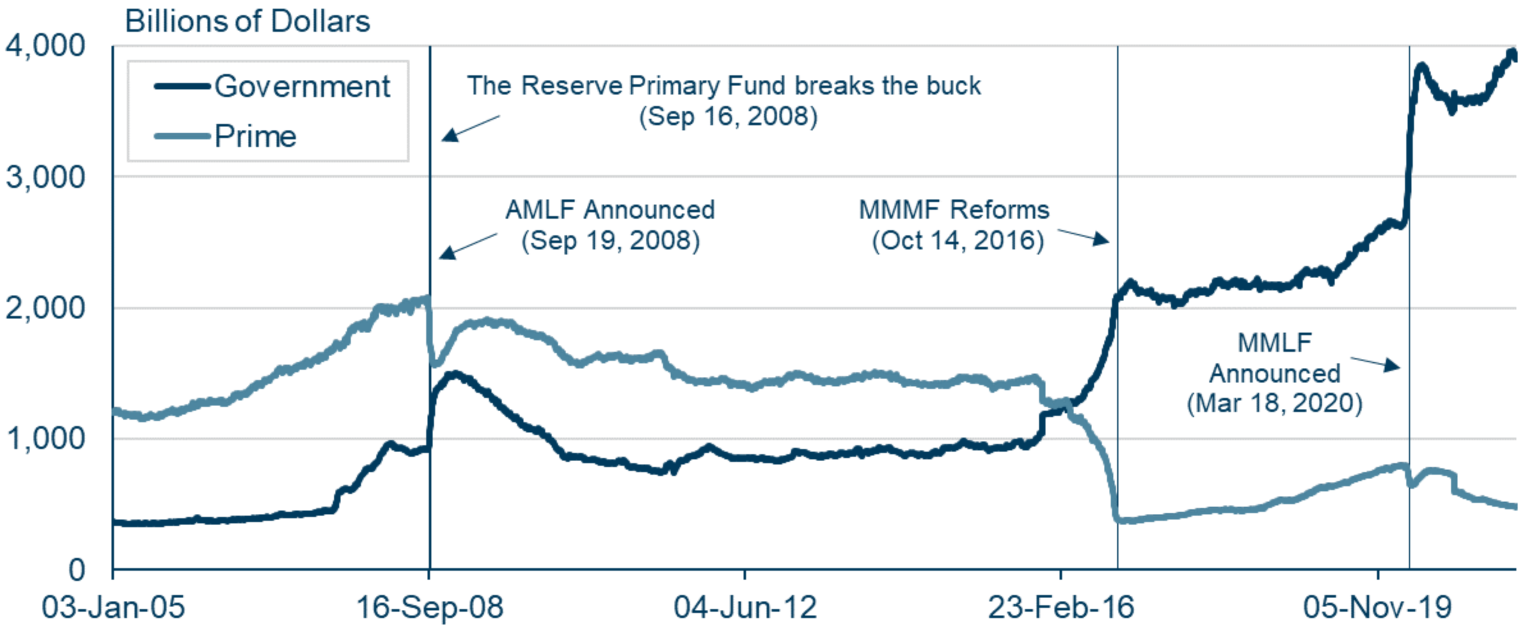


Note: In addition to ABCP-UST spreads, other measures of short-term funding market stress also spiked in 2008 and 2020, including unsecured CP-UST, etc.

Source: Bloomberg Finance L.P., Federal Reserve Board, Haver Analytics

Figure 2: Prime and Government Money Market Mutual Fund Assets Under Management

January 3, 2005 - June 23, 2021

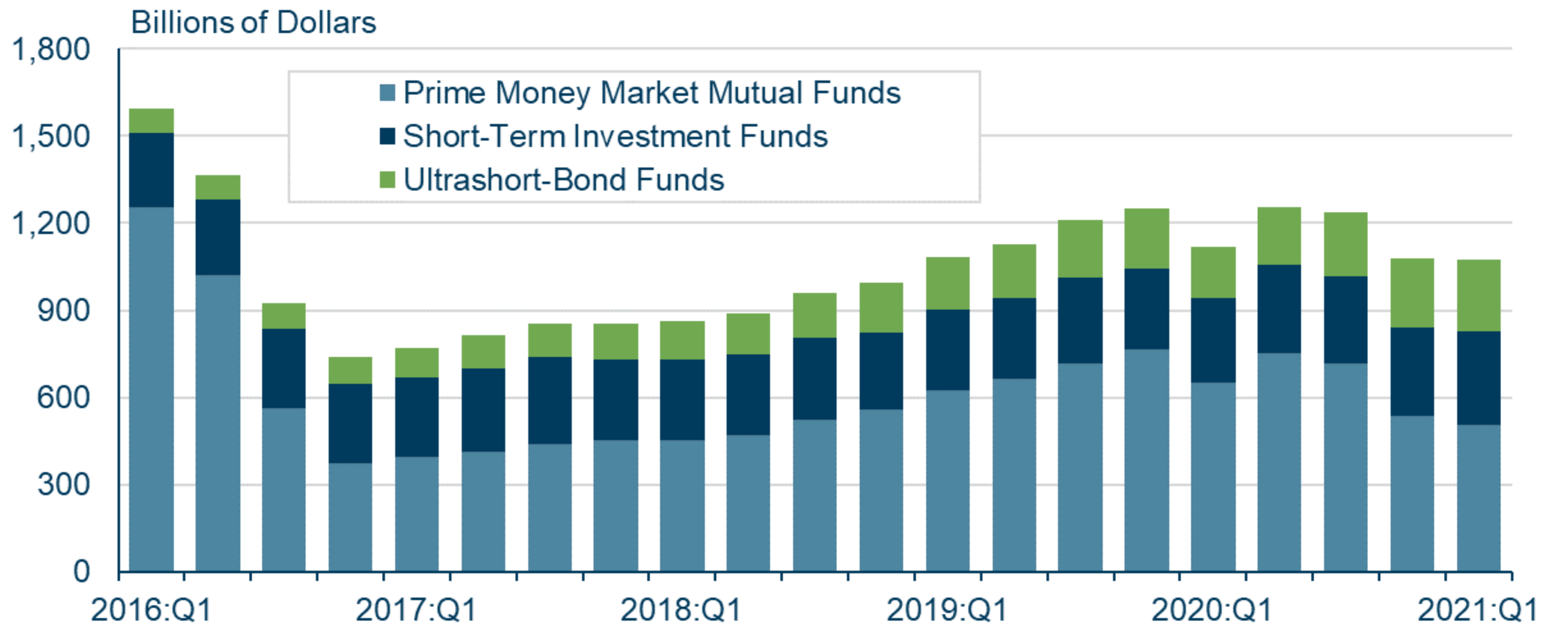


Note: In 2014, the SEC adopted MMMF reforms that had two main components: (1) a requirement that institutional prime and tax-exempt MMMFs transact at a variable price rather than the fixed price that had previously been used, (2) a requirement that the board of prime and tax-exempt MMMFs be permitted to levy fees or freeze redemptions if the fund's weekly liquid assets were to fall below 30% of its net assets. The effective date of these reforms was October 14, 2016.

Source: iMoneyNet

Figure 3: Net Assets in Other Cash Management Funds

2016:Q1 - 2021:Q1

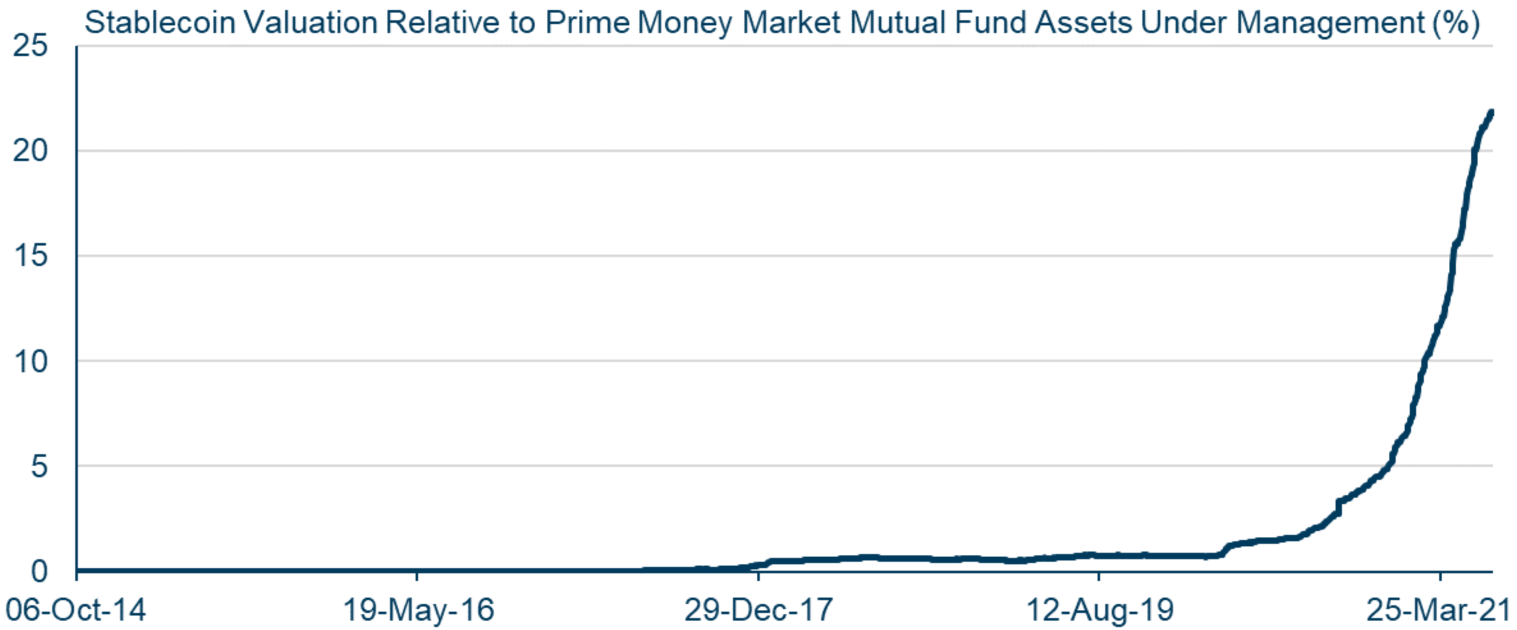


Note: Short-term investment fund data are limited to the six largest short-term investment fund sponsors that are Call Report filers.

Source: iMoneyNet; Morningstar, Inc.; Quarterly Bank Call Report, Schedule RC-T, Memoranda 3.f.

Figure 4: Stablecoin Market Capitalization Relative to Prime Money Market Mutual Fund Assets Under Management

October 6, 2014 - June 23, 2021



Source: Coin Metrics, iMoneyNet

Figure 5: Tether's Asset Breakdown
as of March 31, 2021

Assets	USD Billions	Percent
Cash	1.2	2.9
Treasury Bills	0.9	2.2
Reverse Repo Notes	1.1	2.7
Fiduciary Deposits	7.5	18.4
Commercial Paper	20.3	49.6
Secured Loans	5.1	12.5
Corporate Bonds, Funds, and Precious Metals	4.1	10.0
Other Investments	0.7	1.6
Total Assets	41.0	100.0

Source: Tether

Regulatory Relief Instituted to Promote Lending during Crisis

- Allowed lenders to provide loan modifications without classifying the loan as a troubled debt restructuring
- Capital ratio adjustment for large banks (SLR) which removed Treasuries and deposits at Federal Reserve Banks from the denominator of the capital ratio
- Reduced the impact of the new accounting rules (CECL)
- Reduced capital requirement on community banks from 9 percent to 8 percent (for Community Bank Leverage Ratio “CBLR” adopters)
- Encouragement to use capital buffers
- Suspension of share repurchases and limitations on dividends

Promoting Credit Availability during Crisis

- Emergency lending facilities to support key asset market functioning:
  - PDCF (Primary Dealer Credit Facility)
  - MMLF (Money Market Mutual Fund Liquidity Facility)
  - CPFF (Commercial Paper Funding Facility)
  - TALF (Term Asset-Backed Securities Loan Facility)
- Direct lending to private businesses/corporations that replaced bank lending/bond issuance:
  - PPP (Paycheck Protection Program)
  - MSLP (Main Street Lending Program)
  - PMCCF and SMCCF (Primary and Secondary Market Corporate Credit Facilities)

Figure 6: Programs Established to Provide Credit to Small- and Mid-Sized Borrowers

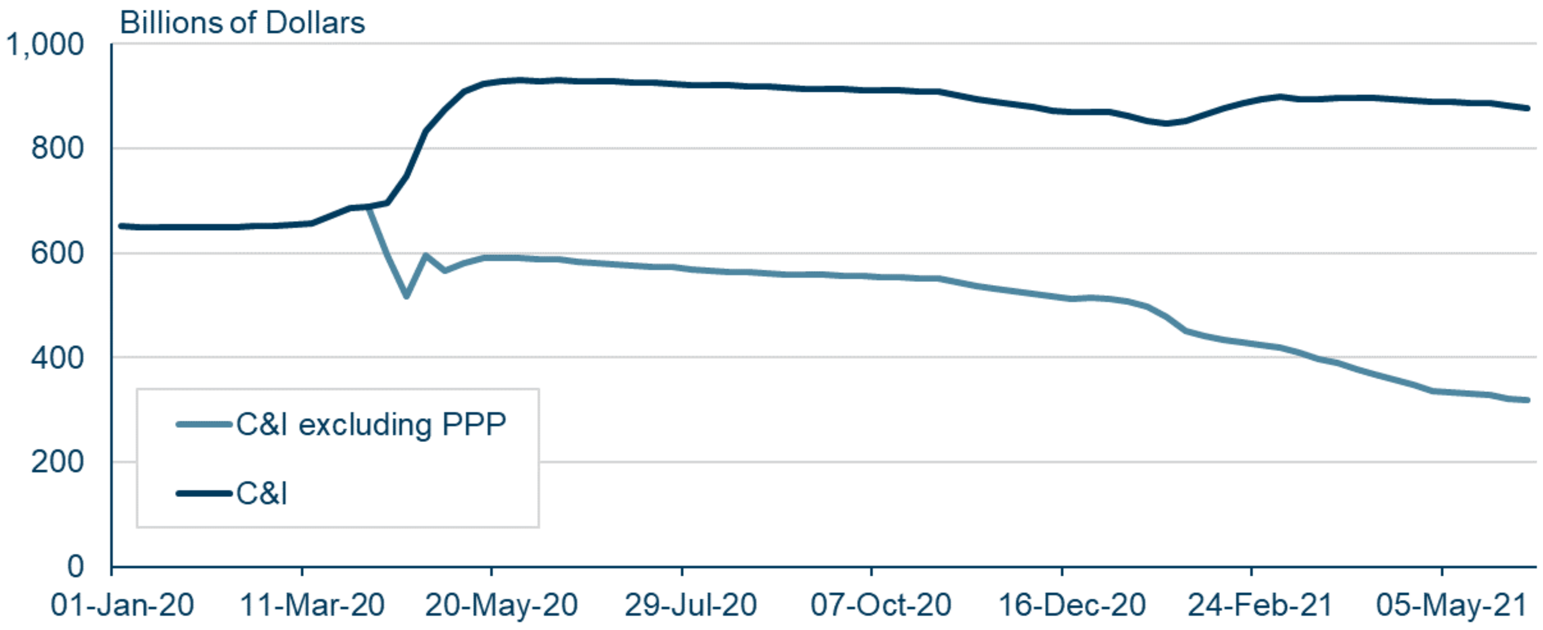
Program	Paycheck Protection Program	Main Street Lending Program
Target Firms	Small-sized (≤500 employees)	Small- and medium-sized • <15,000 employees OR • <$50 billion in revenue
Loan Size	Max = $10 million Average = $67,600	Max = $300 million Average = $9.5 million
Max Outstanding Balances	$800 billion	$17.5 billion
Number of Loans	11,823,594	1,830

Note: The Paycheck Protection Program is a Small Business Administration program. The Main Street Lending Program is a Federal Reserve program. Paycheck Protection Program loans are potentially forgivable if certain criteria are met. Main Street Lending Program loans are full-recourse loans and not forgivable.

Source: Federal Reserve Bank of Boston, Federal Reserve Board, Small Business Administration

Figure 7: C&I Lending and the Paycheck Protection Program (PPP): Small Domestic Banks

January 1, 2020 - June 2, 2021

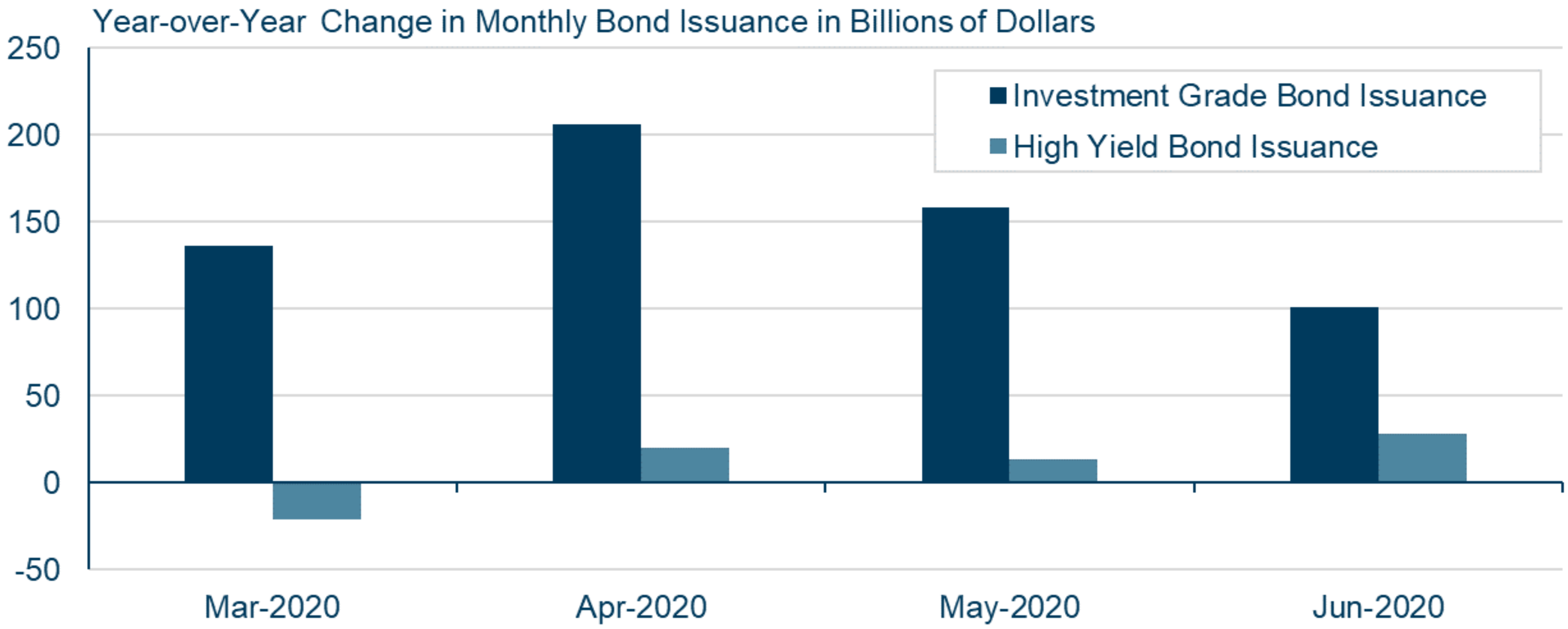


Note: Small domestic banks are defined as all domestic commercial banks minus the 25 largest domestically chartered commercial banks. Data are weekly.

Source: Federal Reserve Board, Small Business Administration, Haver Analytics

Figure 8: Change in U.S. Bond Issuance

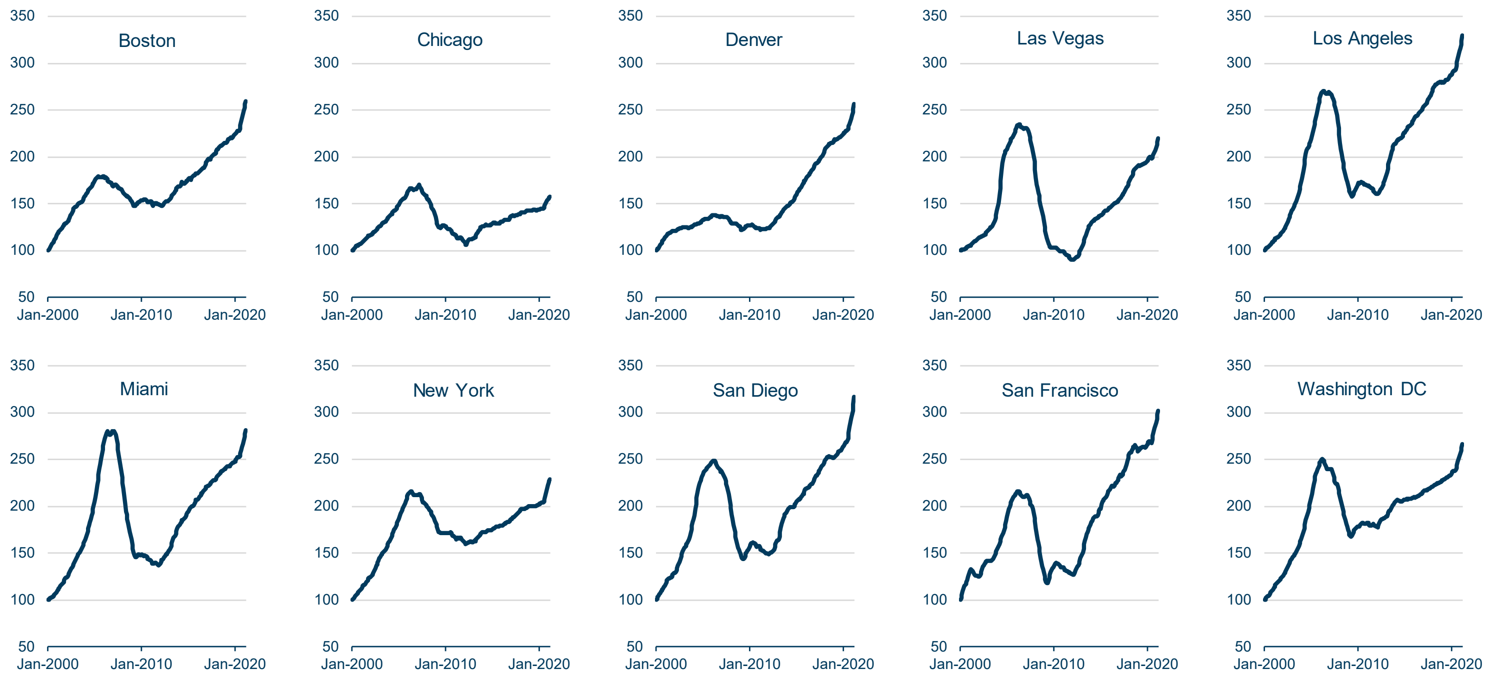
March 2020 - June 2020



Source: SIFMA

Figure 9: U.S. Metro Area Home Price Indices

January 2000 - March 2021
Index, January 2000=100



Note: Indices are repeat-sales indices.

Source: S&P/Case-Shiller, Haver Analytics

Concluding Observations

- Short-term credit markets have been disrupted in the past two recessions, and significant risks remain
- Substantial actions were taken to support lending during the pandemic
  - We need to be less dependent on ad hoc measures
  - A properly implemented CCyB would avoid some of these issues
- Emergency facilities were more effective at supporting large firms
  - We need better ways to reach small firms in economic downturns
  - Without better facilities for small firms, the situation will increase economic concentration
- Housing prices have caused financial stability problems in the past
  - Recent housing price trends should be monitored closely by policymakers