EXECUTIVE BOARD MEETING

SM/20/118
Correction 1

July 27, 2020

To: Members of the Executive Board

From: The Secretary

Subject: **United States—Financial System Stability Assessment**

Board Action:	The attached corrections to SM/20/118 (7/17/20) have been provided by the staff:
Evident Ambiguity	**Page 1**
Typographical Errors	**Page 12**
Questions:	Ms. Erbenova, ICD (ext. 38723)

INTERNATIONAL MONETARY FUND

UNITED STATES

FINANCIAL SYSTEM STABILITY ASSESSMENT

July 17, 2020

KEY ISSUES

Context: Much of the Financial Sector Assessment Program (FSAP) work was conducted prior to the COVID-19 pandemic. The lockdown of the economy has led to a massive growth shock. Following the precipitous fall, risk asset prices have rebounded, and financial conditions eased. The vulnerability analysis has been updated and largely captures this shock. Recommendations on strengthening policy and institutional frameworks remain pertinent. The approach to financial regulation and supervision was risk-focused given the high degree of compliance against international standards assessed during the 2015 FSAP.

Findings: The financial system entered the crisis with strong buffers, but the rise in corporate leverage and migration of risks to nonbank financial institutions compounded with ongoing economic disruption could result in a severe financial strain. Banks' capital depletion rates in the stress test are high, yet manageable, and limiting shareholder payouts would help conserve banks' capital. Most investment funds would be able to meet severe redemptions. Some life insurers face a significant capital reduction in the adverse scenario, but the valuation and capital framework largely mitigates the impact. The Federal Reserve's response to market dysfunction was timely and forceful helping to preserve financial stability. Relaxation of prudential requirements has led to fewer banks being subject to full Basel standards. There are few tools to deal with the ongoing migration of risks to nonbanks. Key insurance reforms remain outstanding. Recent changes require fewer banks to prepare recovery and resolution plans.

Policies: The development of macroprudential tools to deal with the growing risks in nonbanks is a priority. The overall stringency of prudential requirements for non-internationally active banks should be maintained. The Federal Reserve should take measures to durably bolster money market resilience and strengthen liquidity backstops. More comprehensive system-wide supervisory stress tests should be developed for central counterparties (CCP) and the consistency of risk management outcomes by CCPs should be strengthened. Group capital requirements should be developed for insurers. The Commodity Futures Trading Commission (CFTC) and the Securities and Exchange Commission (SEC) should be granted greater budgetary independence. The authorities should mitigate the impact of reduced firm-developed recovery and resolution plans through recovery plan requirements, their own resolution plans, and intensified crisis preparedness.

Table 1. United States 2020 FSAP: Key Recommendations (concluded)		
	Responsible Authority	Horizon[1]
Securities Regulation and Supervision		
Give CFTC and SEC greater independence to determine their own resources, with appropriate accountability.	Congress	ST
Assess financial stability risks related to mutual funds and stable net asset value (NAV) money market funds (MMFs), including through SEC-led liquidity stress testing.	SEC	I
Conclude implementation of new broker-dealer capital rules; finalization of market-wide circuit breakers, and delivery of the Consolidated Audit Trail.	SEC	ST
Increase scrutiny of new registrants and reduce reliance on self-attestations where applicable.	SEC, CFTC, NFA	I
AML/CFT		
Legislate to collect beneficial ownership information on formation of U.S. corporations, maintain it, and ensure timely access for authorities.	Congress	ST
Ensure that investment advisers, lawyers, accountants, and company service providers are effectively regulated and supervised for AML/CFT in line with risks.	Treasury	ST
Systemic Liquidity		
Promote the fungibility of Treasury Securities and Reserves by adjusting assumptions about firms' access to the Discount Window in liquidity metrics.	FRB	ST
Continue to operate regular fine-tuning OMOs.	FRB	I
Advance arrangements for providing liquidity to systemic nonbanks and CCPs under stress, and reconsider restrictions on bilateral emergency liquidity assistance (ELA) to designated systemically important nonbanks.	FRB, Treasury & Congress	ST
Develop robust and effective backup plans in the event the sole provider, Bank of New York Mellon (BNYM), is not able to settle and clear repo transactions.	FRB	MT
Enhance arrangements to provide liquidity support in foreign currencies to banks and designated systemically important CCPs.	FRB	MT
Crisis Preparedness and Management		
Intensify crisis preparedness. ~~(¶119–121)~~	FSOC, FBAs, UST	ST
Continue to use agency discretion actively to subject a wider array of firms to RRP. ~~(¶106)~~	FBAs	ST
Continue to undertake, at least yearly, Dodd-Frank Act (DFA) Title II plans, resolvability assessments, and crisis management group (CMG) discussions of RRPs and assessments. ~~(¶106)~~	FRB, FDIC	ST
Extend OLA powers to cover FBOs' U.S. branches; ensure equal depositor preference ranking for overseas branch deposits with domestic deposits; introduce powers to give prompt and predictable legal effect to foreign resolution measures. ~~(¶108)~~	Congress	MT

[1] I: Immediate; ST: short term= less than 1 year; MT: medium term= 1–5 years.