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Charge for Task Force on Financial Stability

Hutchins Center on Fiscal & Monetary Policy, Brookings Institution

Initiative on Global Markets, University of Chicago Booth School of Business

Many actions have been taken in recent years to reduce vulnerabilities in the financial system that were revealed in the global financial crisis and resulted in a deep recession in the U.S and elsewhere around the world. Law and regulations have been changed and private practices have adapted to lessons learned in the crisis to make the system more resilient to adverse developments. This task force will consider which additional steps might be required to better assure that the financial system in the U.S. can meet the credit and other financial needs of households and businesses through the economic and financial cycle, thereby supporting economic growth. Do the US authorities have the tools and the processes for deploying them to promote financial stability in the United States and reduce the risk of harm to the economy from bouts of financial instability? Importantly, to the extent the task force identifies tools in areas of greatest potential and unaddressed vulnerabilities and its recommendations are acted on, the risks to the financial system arising from accommodative monetary policies that promote very low interest rates over long periods would be significantly attenuated.

The task force will address first principles, such as the appropriate goals for financial stability, the trade-offs between safety/soundness and prudent risk-taking, the types of activities and institutions that are systemically important, and the issue of who absorbs losses and when. It will look for gaps in authority and assess the adequacy of existing tools to address systemic risks posed by certain assets, transactions, or market characteristics in banks, nonbank financial firms, and market- intermediated finance, as well as those arising from migration across these domains. It will examine potential stability risks posed by the financial characteristics and behavior under stress of borrowers as well as lenders.

The task force will look for major risks to financial stability and recommend ways to mitigate them. Its focus will be on the architecture for dealing with risks that might emerge over time, more than on any immediate challenges to financial stability. For example, with respect to housing finance, this inquiry could include examining the risks and regulatory frameworks of different types of mortgage lenders, and whether limits on loan-to-income, loan-to-value, or debt service ratios would be desirable to damp the tendency of housing and mortgage markets to cause or amplify economic cycles. With respect to insurance, this study could include evaluations of exposures of insurers to capital market fluctuations, and the efficacy of the state regulatory system for protecting financial stability. With respect to leveraged loans and speculative-grade debt, this analysis might focus on how this debt is securitized and distributed among investors and the resilience of these investors over a market cycle, as well as the effect of the debt on business spending in a downturn. The task force may consider other ways to mitigate *procyclicality* in finance and financial regulation, for example that might result from the much larger importance of mutual funds and other investment vehicles in market-based finance. With financing increasingly market based, the task force might look at the implications for financial stability of the evolution of market liquidity, including the effects on market making of regulations since the financial crisis. The task force may also consider the effects of *structural* changes in, say, fintech and cybersecurity on financial stability and how to mitigate any resulting increases in risks to financial stability. It will take into account the role of global markets and regulators in addressing financial stability risks in the United States.

The task force expects to identify new tools or new ways to deploy existing tools that are already available under current legal authorities. In addition, it may also make recommendations to the Congress for new authorities that are essential for preserving financial stability. It does not expect to address the basic structure and division of responsibilities in the US regulatory system. Rather it likely will recommend incremental reform within the existing regulatory architecture and it may make recommendations to mitigate the informational (*e.g.*, inter-agency gaps in data sharing) and other challenges that can result from the fragmentation of regulation. The task force will not focus on crisis-response tools and issues.

The panel does not include current public officials in the United States, members of Congress or current employees of financial institutions or their trade organizations. But the panel will consult members of Congress and their staff early in the process as well as stakeholders in the financial system. The Task force will strive for consensus recommendations, though individual members will be entitled to dissents. The Task Force expects to report its findings in early 2021.

Members

Glenn Hubbard, co-chair

Donald Kohn, co-chair

Laurie Goodman

Kathryn Judge

Anil Kashyap

Ralph Koijen

Nellie Liang

Blythe Masters

Sandie O’Connor

Kara Stein

Staff

David Wessel