Acting Under Secretary for Domestic Finance Anthony Ryan
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Anthony W. Ryan
U.S. DEPARTMENT OF THE TREASURY

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New York - Good afternoon. I appreciate the opportunity to be with you today. At the Treasury Department we appreciate the efforts that the Investment Company Institute has taken recently and encourage this important work to continue.

Our economy has been facing a prolonged period of uncertainty and our financial markets are experiencing unprecedented and extraordinary challenges. In the past few months, the federal government has taken many steps to protect our economy and our citizens from the financial market turmoil. However, as participants in and beneficiaries of open, robust global capital markets -- you too have an important role to play.

Let me begin by discussing the current state of play in Washington. The last few months have been a whirlwind of activity and the Treasury, along with the Fed and other government regulators, have been working to resolve challenges.

When I joined Secretary Paulson for his transition to the Treasury Department in July of 2006, we expected to face challenges, but few predicted the magnitude, breadth and severity of what we have been confronting over the past year.

While these are challenging times, I am confident we will emerge from this current period with stronger capital markets, stronger financial institutions and an even more robust economy.

That being said, make no mistake, there is a great deal of work ahead of us. It will take our collective best efforts and a good deal more time.

Last week, Congress passed and the President signed into law the Emergency Economic Stabilization Act of 2008, paving the way for the Treasury to begin standing up a new program.

While we have been taking proactive steps over the last few weeks to prepare and begin to design a program, much of the hard work is yet to come. With its enactment into law, Treasury has moved into implementation mode.

When we emerge from the turmoil, we should expect the financial landscape to be quite different. Certain financial instruments, structures and institutions will not survive. The practices defining the new environment will reflect changed conditions brought about by many of the lessons learned. Market participants and regulators will have re-defined the practices and rules by which we operate.

The challenge for all of us is executing this transition – from the excesses of past --- through the turmoil of the present ---- to the model of the future.

Today, I would like to discuss two key topics. First, I would like to discuss a policy framework for how we can work together to execute this transition, and second, a practical effort to expedite the process while mitigating the negative economic consequences.

Let me begin with the policy framework. Science often provides us with models that can serve as useful analogies. To help illustrate my point, I'll borrow from the work of Alfred Wegener, the geologist who first proposed the scientific theory of plate tectonics. The ground underneath our feet is shifting. Like an earthquake, the pressure had built up for years, there were warning signs and tremors, and now the rift has been exposed.

The balanced tension within our financial market system was weakened by deficiencies on both sides, and the resulting chasm has emerged. How will this be filled? Who will fill it? When will stability be restored? These are important questions. Just as in nature, there is no predetermined solution.

As it relates to the capital markets from a public policy perspective, we must restore equilibrium. We must strike the optimal balance between private-sector market discipline and regulatory oversight. Aligning the interests of the private sector and the public sector is critical to the long term success of our economy. When market discipline and regulatory oversight is balanced, market participants better
Equilibrium in this context translates to market stability. Market discipline failed us. It is not the time to point fingers at any one group of market participants. There’s enough blame to go around. We need to focus on moving forward and each party must contribute to the effort.

Regulatory efforts were also compromised. Rules, guidance and oversight did not mitigate failures of market discipline. So here too, regulators need to be part of the solution. Both market practices and regulatory practices must be reviewed with a critical eye towards improvement and materially strengthened.

The U.S. Treasury plays an important role in the formation of financial policy and regulatory structure. We need to ensure this leadership is maintained and enhanced. At Treasury, we are addressing both tactical and strategic challenges. Moreover, we have been confronting these challenges in collaboration with the regulatory community – both at home and abroad, as well as the private sector. The public and private sector must share the responsibility to address the challenges, define and design the best collective prudent practices, and most importantly, implement these new policies. In doing so, we will enhance investor confidence, market stability and improve liquidity.

One of my roles at the Treasury is to coordinate the efforts of the President’s Working Group on Financial Markets (PWG). In March, the PWG issued its "Policy Statement on Financial Market Developments," which contained an analysis of underlying factors that contributed to the market turmoil. We identified weaknesses in global markets, financial institutions, and regulatory policies, and made a set of comprehensive recommendations to address those weaknesses. Since that time, the PWG has worked to ensure the implementation of its recommendations.

Later this week, the PWG will release an update on the progress that has been made since we originally issued our statement and recommendations. The PWG recommendations focused on six areas: mortgage origination, improving investors' contributions to market discipline, reforming the ratings process and practices regarding structured credit, strengthening risk management practices, enhancing prudential regulatory policies, and enhancing the infrastructure in the OTC derivative market.

The PWG recommendations cover the practices of a broad array of market participants, as well as supervisors, addressing all links in the securitization chain: mortgage brokers, mortgage originators, mortgage underwriters, securitizers, issuers, credit rating agencies, investors, and regulators.

While progress has been made, more must follow. Let me highlight four areas:

1. **Transparency and disclosure.** Many of the weaknesses in the market and the resulting challenges in addressing them were exacerbated by complexity and opacity. The best antidote to opacity is transparency and better and more useful disclosure. Issuers and underwriters must provide such disclosure, and investors and asset managers must demand, use, and independently evaluate information more effectively.

2. **Risk awareness.** Regulators and all market participants must be more aware of, and better able to respond to, risks. Credit rating agency practices must reevaluate their methodologies and practices, and the users of their services must rely less on, and appreciate more the limitations of ratings products.

3. **Risk management.** We need improved risk management practices by investors and financial institutions, and continued review and guidance from regulators, including the areas of exposure aggregation, concentration risk, and stress testing. Risk management is everyone’s business.

4. **Capital and liquidity management.** Well-capitalized and liquid institutions are better prepared to deal with challenges and enhance market confidence. We need improved practices in capital and liquidity management to ensure that cushions are sufficiently robust to absorb extreme system-wide shocks.

Recent market events have also highlighted that our existing financial regulatory structure is suboptimal and that comprehensive regulatory reform is required to restore confidence in financial markets and institutions. Our 21st century global capital markets and financial services industry remains regulated largely by outdated 20th century laws and structures.

Earlier this year, the Treasury published a blueprint that would modernize our financial regulatory structure. Our current regulatory framework is not optimally positioned to address the dynamism of the modern financial system. Given the diversity of market participants, the constant innovation undertaken by market practitioners, the growing complexity of financial instruments, and the convergence of financial intermediaries and trading platforms – all within a global context – establishing a more robust, nimble regulatory structure is critical.

One of the recommendations in the Financial Regulatory Blueprint was the creation of a market stability regulator with broad powers focusing on the overall financial system. The market stability regulator would have the ability to evaluate the capital, liquidity, and margin practices across the entire financial system and their potential impact on overall financial stability.

To do this effectively, the market stability regulator would collect information from commercial banks, broker dealers, insurance companies, hedge funds, and commodity pool operators. Rather than focus on the health of a particular organization, the market stability regulator...
would focus on whether a firm's or industry's practices threaten overall financial stability. It would have broad powers and the necessary corrective authorities to deal with deficiencies that pose threats to our financial stability.

While the Treasury Department commenced our work on the Regulatory Blueprint before the financial market turmoil began, the current turmoil has proven the necessity for this kind of regulatory oversight and monitoring. Credit and liquidity conditions, as well as capital requirements are at the heart of the challenges our financial system still faces.

We all realize that as a result of the many excesses, significant deleveraging, and the corresponding actions taken by market participants, our credit and cash markets have effectively been locked up. Just as anxious neighbors lock their doors, anxious market participants have locked down our markets. An unwillingness to extend credit to counterparties and extreme risk aversion has closed the financial community --- compromising its ability to function and choking economic growth. While a key can unlock a door, there is no single key to unlock our financial markets. The lock is too complex. A host of complementary actions will be required to open credit markets and restore the flow of capital.

The second topic I want to discuss is our effort to expedite the transition while mitigating the negative economic consequences.

As we've worked through this period of market turmoil, we have acted on a case-by-case basis --- addressing problems at Fannie Mae and Freddie Mac, working with market participants to prepare for the failure of Lehman Brothers, and lending to AIG so it could sell some of its assets in an orderly manner. We have also taken a number of proactive, tactical steps to increase confidence in the system, including the establishment of a temporary guaranty program for the U.S. money market mutual fund industry.

Despite these steps, more efforts are needed. We saw market dislocations reach a new level last month, and we must now take further, decisive action to fundamentally and comprehensively address the root cause of this turmoil.

And that root cause is the illiquid mortgage-related assets that are choking off the flow of credit. This flow of credit is vitally important to our economy. We must address this underlying problem, and restore confidence in our financial markets and financial institutions so they can perform their mission of supporting future prosperity and growth for all Americans.

We proposed and recently received legislation to establish a troubled asset relief program, one that is sufficiently large to have an impact, and one that includes features to protect the taxpayer to the maximum extent possible.

The current situation is already posing great risk to the taxpayer. When the financial system doesn't work as it should, the ability of consumers and businesses to finance spending, investment and job creation – as well as the personal savings of Americans - are threatened.

The ultimate protection to the taxpayer will be enhanced market stability. A continuing series of financial institution failures and frozen credit markets is certainly not in our nation's interest.

Congress and the Administration have now come together quickly and effectively to enact this new legislation. We now need to complete our preparations, and begin to implement the multi-dimensional program.

There is no one-size-fits-all solution to alleviating the stress in our financial system. Each situation will be different and we must implement this new program with a strategy that allows us to adapt to changing circumstances and conditions, and attract private capital. The broad authorities in this legislation, when combined with existing regulatory authorities and resources, gives us the ability to protect and recapitalize our financial system as we work through the stresses in our credit markets.

In the coming days we will hire the expertise to help us optimally design and implement our new authorities. Transparency throughout this process will be important, and I look forward to providing regular updates as we move ahead to implement this strategy.

Summary

Never more than today has it been more evident that what happens in our financial markets affects not only Americans in all 50 states, but people and markets around the world.

Only through stable markets and sound financial institutions can capital be available for small and large companies to borrow and grow, for the entrepreneur to start a new business, for families to buy homes and cars and pay for their children's educations. When people and companies save, borrow, and invest, they place their trust in our markets and our financial institutions.

Our country must continue our strong record of confronting challenges, developing solutions, and being innovative and competitive. By doing so, we will work through the current challenges and facilitate sustainable economic growth. We must redouble our efforts to ensure that our financial markets are the strongest in the world and inspire confidence by market participants.

Progress will not come in a straight line, and we need to remain focused as we work through these challenges. Policymakers and regulators must remain vigilant, use all available tools and as necessary seek new ones, not merely to address immediate concerns but also to close the rift that was created by the breakdown of robust market and regulatory practices. We must realize that our nation's economy is dependent on healthy, well functioning financial markets where credit flows from providers to users of capital in an orderly manner.
I believe that the United States is on the right path to resolving market disruptions and building a stronger financial system. Increasingly, our capital markets will reflect the underlying economy, and here we are fortunate that our long-term fundamentals are strong. Thank you.

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