BETTER MARKETS

CAPITAL

FACT SHEET

The Truth About Wall Street's Massive Misleading Lobbying Campaign Against Necessary Capital

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Banking regulators have proposed new, long overdue, capital requirements which will only be applicable to less than 40 of the largest bank holding companies in the country and none of the more than 4,000 community banks. The new rules will be focused on megabanks' dangerous, higher risk trading and investment activities. Bank capital is critical to protect Main Street families, jobs, small businesses, community banks, the financial system, and the economy.

But Wall Street and its supporters are making more and more false, baseless, and dangerous arguments about capital to protect their bottom line. Reported bank lobbying had already increased 20% and now Wall Street is doubling down on influence tactics that they do not have to report, which include a television ad campaign (with placements on television's top-rated program- Sunday Night Football), expensive Beltway media sponsorships, social media advertising, and a bank lobbyist website filled with false claims about capital and its importance to our economy.

Below are factual responses to some of the most frequent false claims made by the banking industry and its allies.[1]

False Claim: Higher capital will harm the economy and the American people.

TRUTH: Higher capital requirements actually result in higher lending to the real economy and more credit to the American people, and promote economic growth, and financial system stability, thereby also protecting Main Street from bank failures, crashes, and bailouts.

- The biggest threat to Main Street families comes from banks that do not have enough capital like Silicon Valley Bank, Signature Bank and First Republic Bank, which all failed in early 2023 because they didn't have enough capital. The problem is that ***under***capitalized banks are incentivized to engage in high-risk and dangerous activities that increase the likelihood and severity of bank failures, devastating crashes, and taxpayer bailouts. Wall Street's misinformation campaign is based on the false claim that adequate capital would result in ***over***capitalized banks which they claim would harm the economy.
- The evidence definitely proves that the banks' claims to be false and that increased

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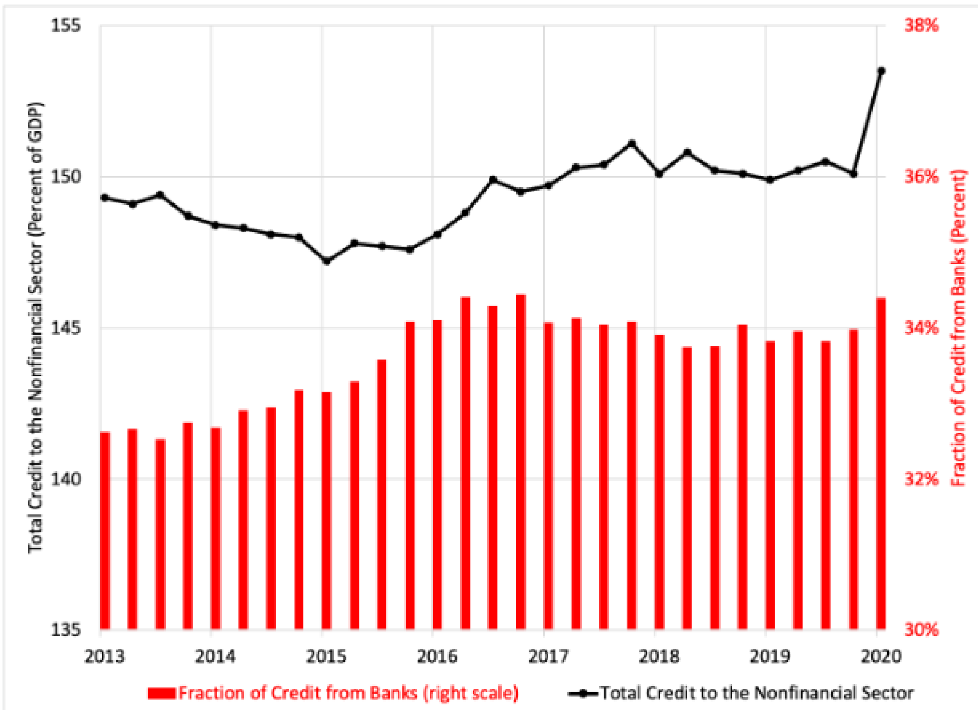
[1] For those who want a more comprehensive list of the megabanks false claims about capital with detailed rebuttals, Stanford Professor Anat Admati has complied, posted, and updates such a document here, which currently addresses 44 such claims!

capital requirements do not reduce lending. In fact, as regulators required banks to increase their capital after the 2008 crash, those very same banks increased their lending to the nonfinancial sector, as clearly shown here[2]:

Quantity and sources of credit to the nonfinancial sector, 2013-2019



Source: BIS.

- That is exactly the same time when significantly higher capital requirements were imposed on megabanks because they were so undercapitalized leading up to and causing the devastating 2008 global financial crash.
- Moreover, in addition to there having been no meaningfully negative effect on bank lending or economic support in normal, non-stress periods, it has been shown that higher capital requirements reduce the impact of economic and financial downturns. For example, a review of academic literature on the effects of capital requirements by the Bank for International Settlements, containing bank data going back to 1870, concludes that higher bank capital "***significantly lower[s] the cost of a crisis by sustaining bank lending during the resulting recession***."

False Claim: Banks survived the pandemic, so they don't need more capital.

TRUTH: The COVID-19 pandemic did not prove that banks were a source of strength. Instead, the scope and scale of U.S. government's fiscal policy and unprecedented Fed actions to support financial markets served as a back-door bailout of the banking system during the

[2] Stephen G. Cecchetti & Kermit L. Schoenholtz, *Setting Bank Capital Requirements*, MONEY AND BANKING (Oct. 12, 2020), https://www.moneyandbanking.com/commentary/2020/10/11/setting-bank-capital-requirements.

pandemic. Without those trillions of dollars to support the financial system and economy, numerous banks would undoubtedly have failed almost certainly causing a financial crash.

- Large banks only had to be a "source of strength" for about two weeks after the onset of pandemic-caused market stress in early March 2020. That's because the Fed began providing enormous support to the financial system in mid-March via direct capital injections, monetary policy (zero interest rates and quantitative easing), and innumerable rescue programs aimed at almost every financial market. For example, within just the first 90 days of the pandemic, the Fed injected $3 trillion into the markets to prop up the financial system -- in which the largest banks are the dominant participants – and provided massive funding to banks and bank-owned securities dealers. On top of that, the government provided the economy with more than $5 trillion of fiscal support, which also dramatically helped banks by reducing the level of business and consumer loan defaults.
- The banks and their advocates consistently fail to mention the immense Fed and taxpayer-funded support they received throughout the COVID 19 pandemic, without which many of them would have faced catastrophic losses and certain failure. In fact, this support was so massive that it not only prevented losses, but it also led to increased bank earnings. For example, net income at the four largest banks in in 2021—the middle of the pandemic—was 120% higher than their net income in 2019.
- The Federal Reserve's own analysis says that claims the 2020 pandemic somehow proved banks were sufficiently capitalized and thus a "source of strength" are wrong. While the capital requirements for the largest banks did make them more resilient entering the crisis than they otherwise would have been, those requirements simply bought the Fed a little time to roll out programs that prevented the banks from running out of capital and failing. Thus, the banks' capital levels were not adequate to prevent their collapse; that was due to the trillions of dollars of fiscal and Fed financial market support as well as regulatory relief and related actions.

False Claim: Higher capital requirements will make borrowing more expensive for all Americans.

Truth: The proposed increase in capital requirements related to lending activities is small and if banks choose to pass the cost to borrowers, it is because they are also choosing to prioritize maximizing executive bonuses and shareholder payouts.

- As Fed Vice Chair Michael Barr detailed, the estimated increase in capital required for lending activities on average—inclusive of both credit risk and operational risk requirements—is very limited. Barr stated that the rise is expected to increase the cost to banks for funding the average lending portfolio by at most 3 basis points out of 100, which is just 0.03 percentage points.
- If the banks choose to pass that very minimal cost of slightly higher capital to their customers, that is a choice that they make – it is not the result of the rule. Additionally,

even if some banks choose to increase rates on borrowers, that doesn't necessarily mean that borrowers will have to pay more. Borrowers could—and should—shop around to other banks—such as community banks—to find the best rate. Of course, banks could also just decide not to pass along these costs to consumers and instead remain competitive within the lending marketplace by building capital in other ways, such as reducing dividends, bonuses, and stock buybacks.

- For example, the four largest banks - JP Morgan Chase, Bank of America, Citibank, and Wells Fargo - have about $4 trillion in loans and leases currently outstanding. 0.03 percentage points, or 3 basis points, of this total is about $1.2 billion – an amount that could certainly be covered by other sources of funds at these banks, with no cost increase for borrowers.
- Remember, since 2013, those four megabanks paid out $584 billion in dividends and buybacks to shareholders. That was 80% of their entire net income. They didn't have to pay out that much income to shareholders and themselves (given CEOs and executives have large shareholdings). Instead, for example, they could have paid out only 70% of their earnings. That would have freed up $58 billion in more capital funding. Going forward, the megabanks could pay out a minuscule amount less which would easily cover the potential maximum costs, even adjusting for additional loan growth. Thus, there is no need for even the possible minimal increase in costs being passed along to borrowers – unless the megabanks choose to do so.

False Claim: Higher capital will hurt Main Street small businesses.

Truth: Higher capital on Wall Street's megabanks will not hurt small businesses, but will protects the banking system and enables banks to continue lending, through ups and downs in the economic cycle, to small businesses and all borrowers.

- It's important to note that these claims are mostly being made by a tiny number of small businesses that are funded by Goldman Sachs which has organizing its borrowers into a lobbying and PR group. The claims are, however, a smokescreen that distracts from the facts.
    - First, Goldman's survey is biased and grossly unrepresentative. It is based entirely on its own "10,000 Small Business Voices" program, but there are 33,185,550 small businesses in the U.S. Thus, Goldman's survey of its 10,000 borrowers about a third of 1 percent of all small businesses.
    - Second, the capital rules are focused on megabanks high risk and dangerous trading and investments, not small business activities.
    - Third, Wall Street megabanks only provide a very small percentage of small business loans. In fact, Goldman's small business lending is less than 2 percent of its total loan portfolio and only half a percent of its total assets.
    - Fourth, the capital rules will actually help ***all borrowers***, including small businesses because well-capitalized banks that are able to lend no matter the economic environment.
- Maybe most importantly, community banks are, in fact, far more dedicated supporters of and lenders to small businesses than Wall Street megabanks. An FDIC study shows

that community account for 36 percent of all small business loans. That is more than double their 15 percent share of the banking industry's total loans. Put differently, community banks provide only 15 percent of all banking industry loans but provide 36 percent of small business loans. Wall Street megabanks simply don't focus on small business lending and no amount of lobbying by an unrepresentative sample of the very small number of small businesses that borrow from Goldman can change those facts.

False Claim: Higher capital requirements will force banks to limit mortgage lending, especially to minority borrowers.

Truth: Banks do very little mortgage lending, have been reducing it dramatically for decades, especially to minorities, and that reduction has not been related to capital requirements. Most mortgage lending is done by nonbanks and none of the capital rules do apply them.

- The proposed capital rules should actually help ***all borrowers***, including low and moderate and minority borrowers. Stronger banks that should have a lower cost of capital, won't fail, cause an economic crisis, and throw people out of the jobs and homes, and will be able to lend throughout the ups and downs of the economic cycle.
- However, in addition to the ***ability to lend***, banks must have ***the willingness to lend*** and that is where they have fallen short. Banks have been reducing their mortgage lending for decades as developments in primary and secondary mortgage markets, securitization, and technological innovation have evolved. Mortgages have become relatively easy to provide and have low margins; consequently, nonbanks have increased mortgage lending dramatically and banks have reduced their participation in the market. To illustrate, in the third quarter of 2023, the six largest megabanks held just 7 percent of all outstanding mortgages, well below their 35 percent share of total loans and more than 43 percent share of total assets in the banking industry. This reduction in mortgage lending isn't new, isn't being caused by higher capital requirements, and isn't focused on any one minority group.
- Moreover, despite making pledges and setting ambitious goals for increased mortgage lending in minority communities, the megabanks have fallen short and broken promises to support minorities' goals of homeownership. For example, in 2017, Wells Fargo, the megabank that has historically focused most on mortgage lending, announced $60 billion to create 250,000 Black homeowners within the next decade. But, in 2021, Wells underwrote ***42% fewer*** mortgages to Black buyers than in the year it announced its target. Even counting mortgages purchased from other lenders (which is of questionable utility), Wells Fargo backed successively fewer mortgage loans in each of the past five years, hitting a 15-year low in 2021. And that is the record of the "best" mortgage lending megabank. Of course, none of this even addresses the all too frequent charges of redlining and discrimination against the megabanks, who are now conveniently professing concerns about dubious implications from capital requirements.
- Even more disturbing are the inflammatory and misleading "studies" and claims from organizations that appear to be independent of the banks but which receive massive donations from megabanks. For example, one study about the potential impact of the new capital requirements on mortgage lending at first glance suggests that new rules

will have a large and negative impact on lending. However, the study fails to focus on the fact that the proposed rules will only affect a small fraction of all mortgage loans−only those made by the largest banks that would be risky enough to be subject to the new rules.

- Finally, the regulators have made it clear that the focus of the rules are on the megabanks high risk trading and investments, not legitimate lending to Main Street Americans, the real economy, or communities of color. To the extent there is an unintended adverse consequence or disproportionate impact, the regulators have made it clear that they will address that in the final rule. After all, that's what the comment process is for and we are highly confident that the regulators will ensure that there will be little if any impact on lending, including in particular mortgage lending to minority borrowers.

False Claim: "Large banks have more capital now than in 2008, so therefore they don't need any more."

TRUTH: Banks were extremely undercapitalized in 2008. This undercapitalization was a primary cause of the devastating 2008 crash, which required trillions of dollars in bailouts, and resulted in the Great Recession that put tens of millions of Americans out of work and crippled the U.S. economy for years. Of course, capital requirements were increased after that, but the starting point for determining adequate capital levels now cannot be when they were historically and catastrophically low in 2008. The key issue is not how much higher capital levels are now compared to 2008; it's how high capital levels should be to protect the American people. Furthermore, key changes were made during the Trump Administration that significantly weakened the post-2008 crash improvements, making the need for enhanced capital even more imperative.

- Between 2001 and 2006, risk-based capital ratios for the largest banks in the country (GSIBs) were around 7 percent and fell below 5 percent in the fourth quarter of 2008. Tier 1 leverage ratios for the GSIBs between 2001 and 2006 were even lower, between 5 and 6 percent. Risk-based capital levels are now around 12 percent, but that was still not high enough to prevent the failure of three large banks in the spring of 2023, causing contagion, a credit contraction, and massive deposit flight.
- Although the post-2008 crash reforms increased capital relative to banks' risks, regulators stopped well short of requiring as much capital as many academics, public interest groups, regulators, and even banks' own risk managers have argued is needed.
    - The largest banks' capital must minimize the potential that they could once again cause or contribute to a devastating financial crisis and require massive taxpayer-funded bailouts, as well as economic misery for tens of millions of American families.
- Many independent parties have determined that substantially stronger capital standards are both necessary and would be beneficial:

- The Federal Reserve Bank of Minneapolis, in its "Plan to End Too Big to Fail", estimates that increasing bank capital requirements to 23.5% of risk-weighted assets and 15% of total assets (leverage-based requirement) would substantially reduce the likelihood of future taxpayer-funded bailouts while strengthening the economy by making the banking and financial system more resilient.
- The Federal Reserve Board in one of its own proposals, regarding so-called convertible long-term debt requirements, discussed analysis it conducted that showed the most severe loss of a bank holding company during the 2008 Crash to be 19% of risk weighted assets—far higher than current or proposed capital requirements. This figure would have been even larger without all the government support that had been provided at that time.
- Economists at the International Monetary Fund have estimated the benefits of capital for large banks set at 23% of risk weighted assets would outweigh the costs, and that if such a requirement had been in place prior to 2008, it would have substantially reduced the need for taxpayer funded bailouts to address the 2008 crash in the US and Europe.
- Economists Anat Admati and Martin Hellwig, in their 2013 book (with a new, updated version being released on March 23, 2024) *The Banker's New Clothes*, determined that capital leverage requirements of at least 20% - 30% of total assets (leverage-based requirement) would make the banks substantially stronger without sacrificing economic growth.
- The Basel Committee on Banking Supervision (BCBS), in its 2010 paper "An Assessment of the Long-term Economic Impact of Stronger Capital and Liquidity Requirements," estimated risk-based capital requirements of 16% would be appropriate, substantially higher than the requirements the BCBS itself ultimately agreed upon for even the largest banks for post-Crash global standards.
- A 2019 survey of bank risk management professionals showed that nearly half of respondents felt that the bank leverage capital ratio requirement should be 15%. In other words, professionals that manage bank risk for a living believe that current capital minimums are insufficient and should be significantly increased.
- Unsurprisingly, none of the industry's "studies" and "analysis" are independent or credible. Those are little more than purchased propaganda (with the conflicts of interest often undisclosed or actively concealed) that have not been peer-reviewed or subjected to independent analysis and confirmation. Indeed, most of those materials do not disclose the data underlying their baseless claims which prevents third parties from subjecting those claims to independent analysis.

False Claim: If bank capital requirements are increased, financial activity will shift from banks to the dangerously unregulated "shadow banks."

TRUTH: Systemically significant large banks, which are deeply interconnected with the shadow banking system, need to have enough capital to protect the financial system, the economy, and

Main Street families from devastating economic crashes. If activities migrate from those banks to systemically significant shadow banks, then the solution is not to underregulate and undercapitalize banks; it's to properly regulate those shadow banks. This false claim is really based on an argument that both systemically significant large banks and shadow banks should be undercapitalized, but that would be the worst of all worlds. Properly regulating systemically significant financial firms of all types is the right solution.

- There is no question that the systemically significant nonbanks are un- and under-regulated. But the response to a poorly regulated non-bank financial sector is not to allow banks to operate with too little capital; it is to better regulate the nonbank sector.
- In the absence of sufficient standards for shadow banking firms and activities, banks actually need more capital to protect themselves from the threats posed by poorly regulated shadow banking firms. That's because, as was evidenced in the crashes of 2008 and 2023, banks are deeply interconnected with nonbanks and, when nonbanks get into trouble, they can and do endanger banks.
    - If interconnected shadow banks were properly regulated, including facing adequate capital requirements, then large banks may have less risky exposures to them and might need relatively less capital to absorb potential losses than would otherwise be the case.
- With its recently adopted analytic framework and process for regulating systemically important nonbanks, the Financial Stability Oversight Council ("FSOC") must be held accountable for recognizing systemic risks in the nonbank sector and mitigating them. The FSOC must use its power to identify, assess, and address the full range of financial risks that can threaten the country by systemically significant nonbanks. FSOC must designate and properly regulate systemically significant nonbanks. It is unacceptable that there is not one financial firm designated as a systemically significant nonbank in the United States today, especially in light of the many significantly significant nonbanks that received extraordinary support from the Fed in 2008 and again in during the 2023 pandemic-caused crash.

False Claim: Higher capital requirements put U.S. banks at a global disadvantage.

TRUTH: Higher capital standards for U.S. banks have not resulted in a competitive disadvantage relative to foreign banks. In fact, U.S. banks dominate the world's banking system where there is little if any genuine competition. Moreover, even if there was some competitive disadvantage, that would not justify threatening the U.S. financial system and economy with undercapitalized banks.

- U.S. banks have consistently outperformed their foreign counterparts since U.S. capital standards were strengthened following the 2008 crash, due at least in part to the greater financial strength that resulted from regulatory requirements they had fought so hard against.

- As a result, the six largest megabanks had profits of $1 trillion in just the last ten years and the four biggest U.S. lenders alone made 45 percent of total banking industry profits in the third quarter of 2023 (and a 10 year average of 39 percent).
    - And that is all AFTER the capital increases following the enactment of the Dodd Frank Act, which the banks fought using the very same arguments they are using now.
        - And which were proven baseless and false then as much as they are now.
- U.S. banks have far outperformed their global counterparts for years. One striking study compares two equal investments of $100 in a US bank index fund and €100 in a European banking index fund, beginning in January 2008. By January 2019, the US banking index investment would have been worth approximately $170 (a return of 70 percent) while the European fund investment was only worth €40 (a return of negative 60 percent). The study breaks down performance in three periods.
    - 2008- 2010: Both the US and European banking sectors struggled during this period, recovering from the 2008 crisis, with comparable losses in index value.
    - 2011 – 2015: US banks began to outperform their European counterparts in 2011. Europe was weighed down by a variety of factors including the euro crisis, doubts about the viability of a single currency, and concerns about specific countries such as Greece while US banks enjoyed a period of recovery and growth.
    - 2016 – 2018: Growth continued for US banks while European banks continued to suffer because of political risk, largely driven by Brexit and the Italian elections, and negative interest rates that resulted from European Central Bank monetary policy.
- London has lost ground in its ranking as the world's top financial centre, according to the latest (2023) study by the City of London Corporation comparing London to other global cities across a range of competitiveness factors. On the overall scale, London lost ground and tied New York, but New York far outperformed on the "Reach of Financial Activity" measure.
    - The US increased its share of worldwide lending and with 18 percent of the global total overtook the UK, which has 16 percent of lending, in the global financial ecosystem.

The US also far exceeds all global asset manager competitors with the most assets under management (£37 trillion), more than three times the UK with (£11.6 trillion).

False Claim: We need more time to understand the effects of higher capital.

TRUTH: The financial industry uses and abuses the rulemaking process to protect its profits instead of protecting the American people by needlessly delaying and then weakening or killing essential rules. The banking agencies must not allow that to continue and must act as decisively to prevent the next banking crisis as it does when reacting to a crisis.

- The traditional rulemaking process was intended to enable and ensure that agencies received ample public comment to ensure that the best rules were adopted. However, the financial industry repeatedly abuses the rulemaking process to delay, weaken, or kill as many rules as possible to protect their profits regardless of how necessary those rules are to protect the public. In effect, the "public comment" process has been largely hijacked by the industry and transformed into an "industry comment" process where the pubic and the public interest gets drowned out. The evidence for this is overwhelming and already present here regarding the capital rules:
    - Wall Street's CEOs were opposing the capital rules sight unseen. As CNN reported on July 19, 2023, "Bank CEOs are already complaining about new regulations they haven't even seen yet." That's because the CEOs don't have to see the proposed capital rules; they are already against the rules no matter the merits or how necessary they may be.
    - The five most powerful financial industry trade groups representing the country's largest banks sent a letter to Chairman Powell on July 12, 2023, asking for a comment period of 120 days, rather than the typical 60- or 90-day comment period, to respond to the proposed changes to bank capital requirements. These trade groups, with vast if not unlimited resources, influence, and access, including hundreds of lawyers, lobbyists, and staff, are fully capable of responding within any time period to any proposed rules.
    - Even though the 120-day comment period was granted, the same five trade groups submitted another letter on October 6, 2023 asking for even more additional time. These pleas are just the latest example of an attempt to abuse and delay the rulemaking process, which endangers the financial system and increases the risks to the American people.
    - These actions followed the financial industry's failed attempt through their political allies to prevent the capital rule from even being proposed. For example, ten Republican members of the Senate Banking Committee, clearly on behalf of Wall Street's biggest banks, wrote to Fed Chair Powell on March 3, 2023, in a preemptive strike on Vice Chair for Supervision ("VCS") Barr's then-ongoing holistic capital review. Better Markets sent a letter to Chair Powell rebutting the Senators' premature, unwarranted, unnecessary, unfair, and baseless claims and suggestions against VCS Barr and potential capital increases.
        - Proving how wrong those Senators were, their March 3, 2023, letter was literally just days before Silicon Valley Bank collapsed on March 10, 2023, due to a lack of capital which required an FDIC bailout of $16.1 billion, i.e., the FDIC injected $16.1 billion of capital to cover the lack of capital the bank should have had to prevent its collapse in the first place.
- Banking regulators acting decisively and with urgency could avoid the next bank failure, expensive clean up, extraordinary actions, and taxpayer bailouts. There is no justification for delay or an even longer rulemaking process to address long overdue, well known, and abundantly demonstrated weaknesses, including insufficient capital at the megabanks.

Better Banks | Better Businesses

Better Jobs | Better Economic Growth

Better Lives | Better Communities

Better Markets is a public interest 501(c)(3) non-profit based in Washington, D.C. that advocates for greater transparency, accountability, and oversight in the domestic and global capital and commodity markets, to protect the American Dream of homes, jobs, savings, education, a secure retirement, and a rising standard of living.

Better Markets fights for the economic security, opportunity, and prosperity of the American people by working to enact financial reform to prevent another financial crash and the diversion of trillions of taxpayer dollars to bailing out the financial system.

By being a counterweight to Wall Street's biggest financial firms through the policymaking and rulemaking process, Better Markets is supporting pragmatic rules and a strong banking and financial system that enables stability, growth, and broad-based prosperity. Better Markets also fights to refocus finance on the real economy, empower the buyside, and protect investors and consumers.

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