The impact of the COVID-19 event on the financial stability of US banks

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Abstract

The use of changes in investors' forward-looking net long hedging choices — an indicator of investors' risk-based growth expectations — to determine the effect of a change in the Federal Reserve's capital buffer requirement on banks' financial soundness is the study's primary innovation. I show that net hedging factor data reveals significant causal relationships between financial soundness indicators and the Federal Reserve's capital buffer requirement. My findings also show that lowering the capital buffer requirement for banking systems improves both regulatory capital and Tier-1 capital.

Keywords- financial stability of US banks

Introduction

In this episode of Dollar & Sense, we flip the format and ask host David Dollar what new data can tell us about how the COVID-19 pandemic and the associated recession are affecting U.S. trade. Dollar shares insights on which industries have been hit hardest, how the recession will alter the U.S. trade deficit and the phase one trade deal with China, and the likelihood American companies begin reshoring their manufacturing and value chains. So the U.S. publishes very detailed trade statistics in terms of products and partners. They just came out with data through the first half of 2020 providing a snapshot on the effects of the coronavirus pandemic and the associated economic recession on U.S. trade. So, my first question just has to do with trade imbalances. It looks like the overall U.S. trade deficit is contracting modestly this year. So the coronavirus recession is affecting both U.S. imports and U.S. exports. For the moment, it’s having a somewhat stronger effect on imports. We import quite a bit more than we export, so if they both go down by a similar percentage, imports actually go down more in U.S. dollars. And, frankly, the recession is more serious in the United States than in some of our trading partners. We can get into talking about some specific trading partners, but in general, the recession is worse here, so the compression of imports is greater than the decline in exports. But I wouldn’t get too excited.

I think in the first half of the year the trade deficit went down by about 20 billion dollars. That’s basically a rounding error in our GDP, so I wouldn’t get too excited. The other thing I would

say is we don’t really want the trade deficit to go down because we’re in a serious recession. As we come out of recession, probably our trade balance will go back to about where it was. It’s been about three percent of GDP, that deficit, for a few years. Most economists are not too worried about that. We import quite a bit more than we export, so if they both go down by a similar percentage, imports actually go down more in U.S. dollars. And, frankly, the recession is more serious in the United States than in some of our trading partners. We can get into talking about some specific trading partners, but in general, the recession is worse here, so the compression of imports is greater than the decline in exports. But I wouldn’t get too excited.

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