Why No Silver Bullet For TBTF?

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Disclaimer

- The Views Expressed Here Are the Presenter's and Not Necessarily Those of the Federal Reserve Bank of Minneapolis or the Federal Reserve System
Flannery’s Paper Recognizes the Challenge

• “The discussion so far suggests that we should not expect a single policy change to set things right.”

• “No one policy change will adequately address TBTF distortions, nor will any be immune from potential drawbacks.”

• “If the TBTF situation is subject to an easy, straightforward solution, I’ve yet to identify it.”
I’m Glad He Does!

- “We doubt that any single policy change will dramatically reduce expected [TBTF] protection.”

- “We do not seek to eliminate all TBTF bailouts.”

Rationalizing the “Multi-Weapon” Strategy

1. Flannery Stresses Incomplete Information
   - Limits on Supervision (e.g., when to act?)
   - Limits on Regulation (e.g., how to price?)

   - Are We Really Sure About These Benefits?
   - Hard to Argue With Spontaneous Market Phenomenon Across Countries and Time!
Rationalizing the “Multi-Weapon” Strategy

3. Time Consistency
   – Irrelevance of History

4. Multiple Source of Spillovers
   – Importance of Commercial Bankruptcy Code as Source of Spillovers?
Do These Challenges Also Explain Lack of Pre-Crisis Action?

• Mixed Assessment
  – Yes: “You Cannot End TBTF”

  – No:
    • “We Already Ended TBTF”
    • “Moral Hazard is not a Problem”
    • “The Chance of Failure is Low”