

Schuman/Dutko Financial Weekly *Providing a global solution in finance*



Top line

The Federal Reserve temporarily provides a “lift” for the stock market. Where did the \$700 billion in TARP money go? When and how will U.S. tackle the toxic assets on the books of the banks?

The EU’s commitment to addressing the financial crisis head on was reinforced by a major report by a group of high level experts setting out several key recommendations on financial supervision. Regarding hedge funds and private equity, the European Commission remains cautious about over-regulation, suggesting that any future policy should take account of existing regulation in the Member States and should support global consensus on the regulation of such funds.

Key developments this week

US

Federal Reserve Chairman Ben Bernanke, in addition to providing some “hope” for the end of recession in 2009, this week laid out the outline of the plan for “fixing” the banks: The steps he outlined (1) Stress Test - The results of the stress test by the regulators on the 19-20 (banks over \$100 billion) will dictate how much capital each will require that the government will be providing. (2) Asset Purchase Plan - This part is still unclear – but this is what Bernanke refers to as the public/private partnership with market-based pricing “to insure the government doesn’t overpay.” This is where we were with the auction

concept Paulson outlined a few months ago. (3) Restored confidence will ultimately bring in private investment.

The \$700 billion in TARP money so far disbursed: \$281 billion to prop up banks and AIG; \$24.8 billion for GM and Chrysler; \$50 billion home mortgage foreclosure mitigation; and \$100 billion to the Federal Reserve for liquidity facility for the credit markets.

On the toxic asset front – from 2005 to mid-2007, some \$450 billion of CDO of asset-backed securities were issued, one third of which were created from risky mortgage-backed bonds. Some “unwinding” of these has been attempted, and of the so-called mezzanine collateralized debt obligations, recovery rates on these formerly triple A –rated assets have been as low as 5%.

EU

EU recommendations to overhaul financial supervision: Coordinated supervision of financial markets rather than a single EU regulator was among the recommendations of a high level EU expert group this week. The group, chaired by former IMF Managing Director Jacques De Larosière, also called for a review of Basel II rules on bank capital requirements, registration and supervision of credit rating agencies and regulation and greater transparency of hedge funds. It also suggested the creation of a new body, called the European Systemic Risk Council, to be chaired by the European Central Bank, to pool and analyze all information relevant for financial stability.

EU leaders prepare for G20: German Chancellor Angela Merkel headed a meeting of the largest EU Member States, including Germany, France and the UK, on 22 February to try to hammer out the EU’s position ahead of the G20 meeting in London 2 April. The leaders agreed on the need to regulate hedge funds, crack down on tax havens and compel banks to save more capital. The conclusions will feed into the EU Summit meeting of all Member States in March.

Commissioner guidelines on EU regulation of hedge funds and private equity: Addressing a major EU conference, European Commissioner for financial services, Charlie McCreevy, set out a number of lessons for considering any regulation of hedge funds and private equity. These included a recognition of the distinction between hedge funds and private equity and that any action should build on the already extensive experience with regulation of investment funds in Europe.

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