FEDERAL RESERVE BANK of NEW YORK

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Minutes of the Investor Advisory Committee on Financial Markets

July 19, 2013

Federal Reserve Bank of New York

Committee attendees:

Nicole Arnaboldi, Credit Suisse Group
Louis Bacon, Moore Capital Mgmt
Mary Callahan-Erdoes, JP Morgan Asset Mgmt
James Chanos, Kynikos Associates
Garth Friesen, III Associates
Joshua Harris, Apollo Management LP
Alan Howard, Brevan Howard Asset Management
Derek Kaufman, Citadel LLC
Scott Minerd, Guggenheim Partners
Michael Novogratz, Fortress Investment Group
Rick Rieder, BlackRock, Inc
Lawrence Schloss, NYC Public Pension Funds
Morgan Stark, Ramius Capital Group
David Tepper, Appaloosa Management LP

FRBNY attendees:

William Dudley, Chair
James Bergin
Terrence Checki
Christine Cumming
Jennifer Fortner
Steven Friedman
Lorie Logan
Jamie McAndrews
Meg McConnell
Michael Nelson
Simon Potter
Kevin Stiroh

Monetary Policy

The meeting commenced on the topic of U.S. monetary policy developments. Members noted that recent FOMC communication has led market participants to expect a slowing in the monthly pace of purchases in late 2013. Some aspects of recent FOMC communications were characterized as unclear. Committee members also discussed the impact of communication on volatility in the market-implied path of policy rates in recent months.

Members also addressed the U.S. economic growth outlook, characterizing the realized drag on growth from fiscal tightening as less than many had anticipated. Committee members highlighted the tightening in financial conditions that accompanied the rise in U.S. rates over recent months, though noted that rising home prices and recent equity market gains have helped counteract the tightening associated with higher rates.

Financial Market Developments

The Committee next discussed recent financial market developments. Committee members did not describe any widespread, systemic stresses amongst institutions or investor types emanating from the sharp rise in rates and concurrent decline in higher-yielding asset prices. Committee members described losses in momentum-driven investment vehicles such as CTAs as well as risk parity strategies as a result of the sharp rate rise. Members stated that mutual funds and other fixed income investment vehicles have maintained relatively high cash liquidity buffers in recent years, diminishing risk associated with large outflows. Members noted that dealer participation in fixed income and other asset classes continues to decline amid changing business models and new regulatory regimes and discussed the extent to which this shift results in higher market volatility.

The Committee next discussed recent stresses in the Chinese banking system and potential impacts on that country's economic outlook. The rapid growth of wealth management products and other forms of credit expansion were characterized as posing potential risks, with some uncertainty as to whether authorities' attempts to address these risks will be sufficient to prevent economic or political strains.

Regarding Europe, members deliberated progress towards unifying euro-area banking supervision, emphasizing the importance of establishing a credible resolution framework and strong central supervision authority. The Committee also discussed potential risks around ongoing weakness in portions of the European banking sector, continued uncertainty associated with peripheral European structural and fiscal reform, and political considerations surrounding upcoming German elections and next year's European Parliament elections.

Financial Landscape

The meeting concluded with a discussion of how investor views towards large financial institutions as counterparties have evolved since the financial crisis. Members variously observed that counterparty risk management has become a stronger focus of investors, due diligence measures have improved, and tools to manage risks have grown more robust and sophisticated. As new regulations and business model changes have led to increased central clearing, Committee members noted that the focus of risk management continues to shift from broker-dealers to clearinghouses and exchanges.