

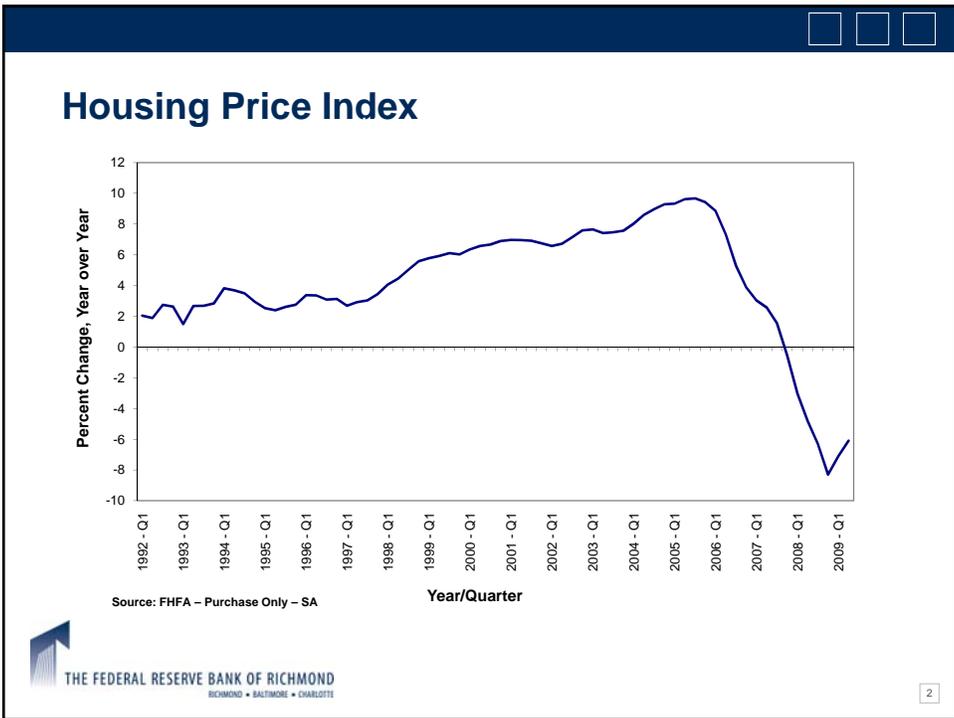
ECONOMICS MADE EASY  09

# A Journalism Workshop

**The Fed's Response to the Financial Crisis**  
John Walter  
October 21, 2009



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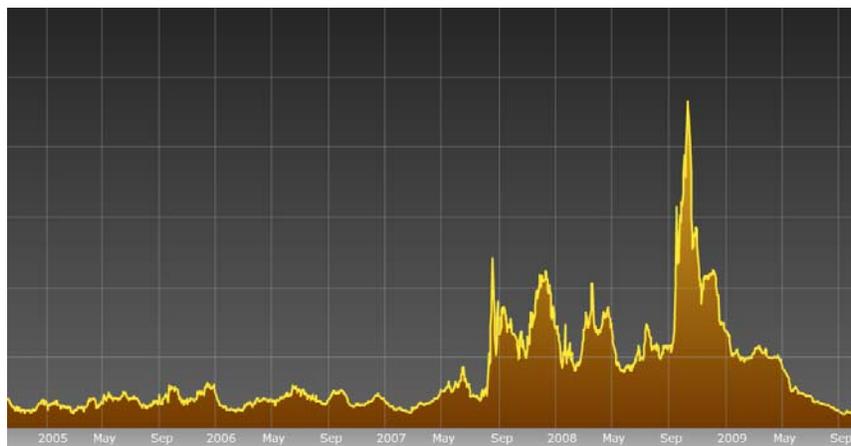


## Evolution of the Financial Crisis

- Housing market problems shifted to financial markets in Summer 2007 – Losses at financial institutions across major countries
- Unclear which financial institutions held worst loans
  - Mortgages had been sliced and resold
- Uncertainty about how bad problems would become
- Financial institutions and investors became highly conservative

## TED Spread

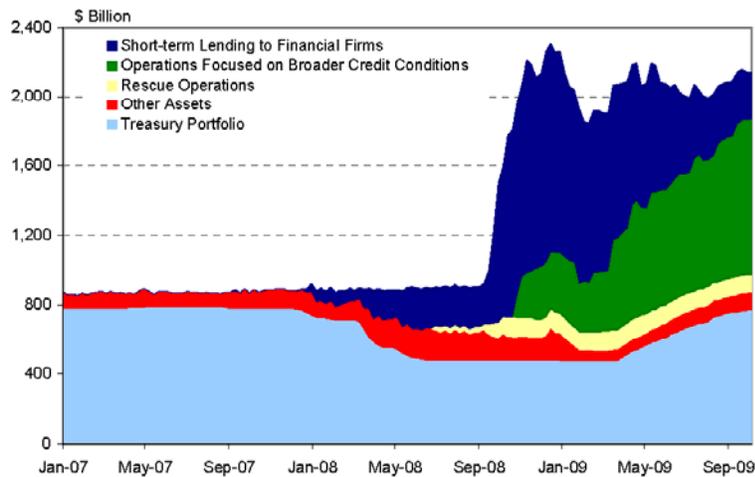
September 2004 – September 2009

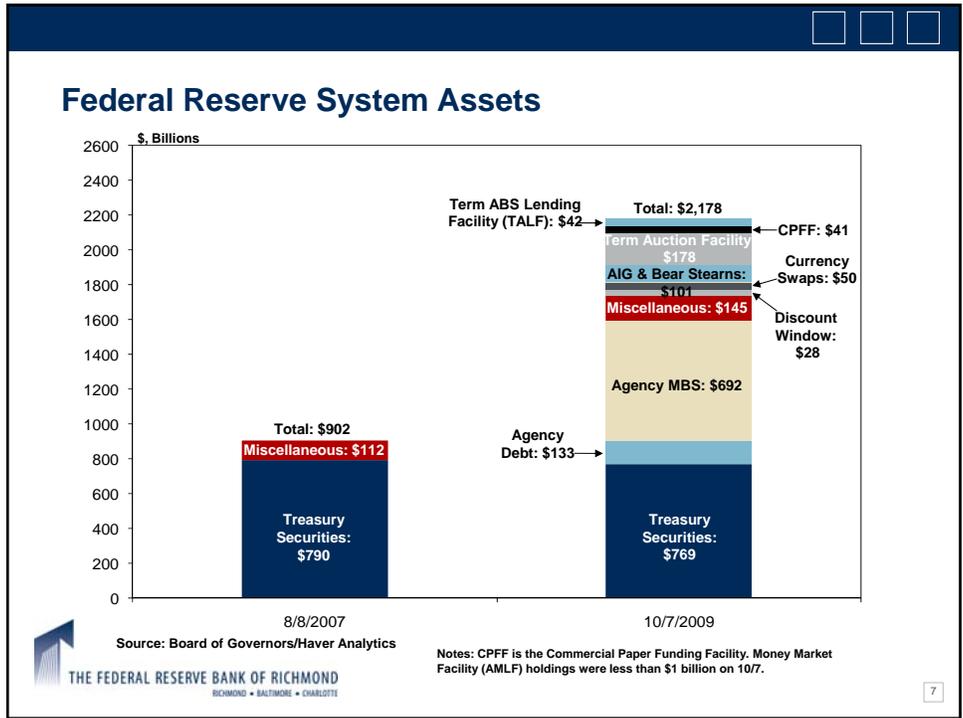


## Relief Programs

- Relief programs began in fall of 2007
- Goal of programs
  - Provide a transfusion
  - Provide funding to lenders – so that they would be willing to lend to consumers and businesses
- The Federal Reserve introduced a total of 14 programs
  - FDIC has introduced several of its own as has the Treasury

## Federal Reserve Balance Sheet





- ### Loan Programs
- **Term Auction Facility (TAF)**
    - Term loans (up to 84 days) to banks while funding markets are under stress
  - **Primary Dealer Credit Facility (PDCF)**
    - Discount window loans to Primary Dealers
  - **ABCP Money Market Fund Liquidity Facility (AMLF)**
    - Non-recourse loans to banks to fund purchases of asset-backed commercial paper from money market mutual funds
  - **Money Market Funding Facility (MMFF)**
    - Funding for private-sector SPV purchases of CDs, bank notes and commercial paper from money market funds

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## Loan Programs, continued

- **Term Asset-Backed Securities Loan Facility (TALF)**
  - Non-recourse loans to purchasers of recently issued consumer or small business asset-backed securities
- **Term Securities Lending Facility (TSLF)**
  - Treasury securities lent to Primary Dealers which provide less liquid securities as collateral
- **Central Bank Swap Lines**
  - Reciprocal currency arrangements with a number of other central banks – U.S. dollars lent in exchange for foreign currencies

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## Asset Purchase Programs

- **Commercial Paper Funding Facility (CPFF)** – Fed purchases (through an Special Purpose Vehicle) commercial paper directly from issuers
- **Purchase of agency debt**
- **Purchases of agency mortgage-backed securities**
- **Treasury Securities Purchase Program**

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## Institution-Specific Assistance

- **Bear Stearns** – Acquired a block of Bear Stearns troubled assets to facilitate JP Morgan Chase's purchase of Bear Stearns
- **AIG** – Loans, asset purchases, and liability acquisitions to prevent AIG's failure
- **Citigroup and Bank America** – Guaranteed specified blocks of assets



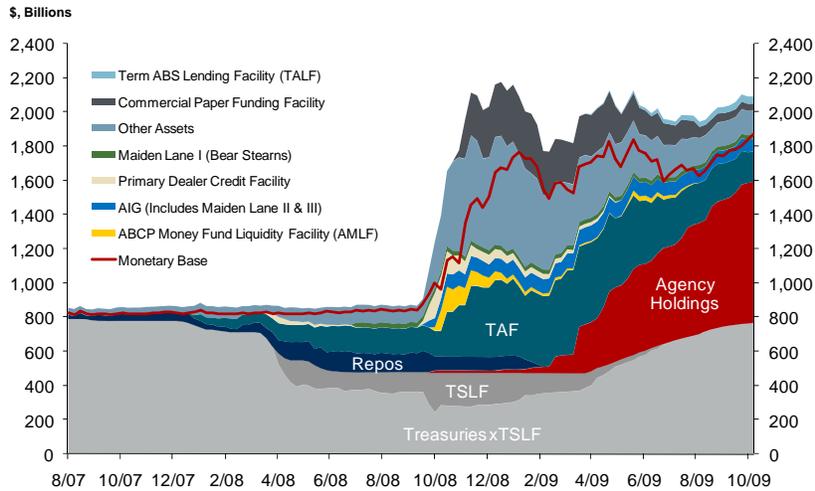
## Loan Program –Term Auction Facility

- Begun in December 2007 – currently \$178 billion
- Term loans (up to 84 days) vs. typical Fed lending – overnight
- Avoids stigma associated with typical Fed lending

### Asset Purchases – Agency MBS

- Fed is purchasing mortgage-backed securities guaranteed by agencies: Fannie Mae, Freddie Mac, and Ginnie Mae
- Currently the Fed holds \$692 billion
- Goal – to lower interest rates on home mortgages, thereby propping up house prices and improving conditions in financial markets

### Federal Reserve System Assets



Source: Board of Governors/Haver Analytics



## Conclusions

- Broad declines in home prices led to defaults on loans.
- Many financial firms were heavily exposed to home loans so they began to suffer financial problems.
- Financial markets tightened up significantly.
- Fed stepped in with a number of interventions meant to prop up.
- Financial markets seem to be on the mend – use of several Fed programs has fallen.



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The views and opinions expressed herein are those of the author. They do not represent an official position of the Federal Reserve Bank of Richmond or the Federal Reserve System.

