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Statement by

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Chair

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before the

Committee on Financial Services

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Chairwoman Waters, Ranking Member McHenry, and other members of the Committee, thank you for the opportunity to update you on our ongoing measures to address the hardship wrought by the pandemic. The Federal Reserve, along with others across government, is working to alleviate the economic fallout. We remain committed to using our tools to do what we can, for as long as it takes, to ensure that the recovery will be as strong as possible, and to limit lasting damage to the economy.

Economic activity has picked up from its depressed second-quarter level, when much of the economy was shut down to stem the spread of the virus. Many economic indicators show marked improvement. Household spending looks to have recovered about three-fourths of its earlier decline, likely owing in part to federal stimulus payments and expanded unemployment benefits. The housing sector has rebounded, and business fixed investment shows signs of improvement. In the labor market, roughly half of the 22 million payroll jobs that were lost in March and April have been regained as people return to work. Both employment and overall economic activity, however, remain well below their pre-pandemic levels, and the path ahead continues to be highly uncertain. The downturn has not fallen equally on all Americans; those least able to bear the burden have been the most affected. The rise in joblessness has been especially severe for lower-wage workers, for women, and for African-Americans and Hispanics. This reversal of economic fortune has upended many lives and created great uncertainty about the future.

A full recovery is likely to come only when people are confident that it is safe to reengage in a broad range of activities. The path forward will depend on keeping the virus under control, and on policy actions taken at all levels of government.

Since mid-March, we have taken forceful action, implementing a policy of near-zero rates, increasing asset holdings, and standing up 13 emergency lending facilities. We took these measures to support broader financial conditions and more directly support the flow of credit to households, businesses of all sizes, and state and local governments. Our actions, taken together, have helped unlock more than $1 trillion of funding, which, in turn, has helped keep organizations from shuttering, putting them in a better position to keep workers on and to hire them back as the economy continues to recover.

The Main Street Lending Program (Main Street) has been of significant interest to this Committee and to the public. Many of the businesses affected by the pandemic are smaller firms that rely on banks for loans, rather than public credit markets. Main Street is designed to facilitate the flow of credit to small and medium-sized businesses. In establishing the facility, we conducted extensive outreach, soliciting public comment and holding in-depth discussions with lenders and borrowers of all sizes. In response to feedback, we have continued to make adjustments to Main Street to provide greater support to small and medium-sized businesses and to nonprofit organizations such as educational institutions, hospitals, and social service organizations.

Nearly 600 banks, representing well more than half of the assets in the banking system, have either completed registration or are in the process of doing so. About 230 loans totaling roughly $2 billion are either funded or in the pipeline. Main Street is intended for businesses that were on a sound footing pre-pandemic and that have good longer-term prospects but which have encountered temporary cash flow problems due to the pandemic and are not able to get credit on reasonable terms as a result. Main Street loans may not be the right solution for some businesses, in part because the CARES Act states clearly that these loans cannot be forgiven.

Our credit facilities have improved lending conditions broadly, including for potential Main Street borrowers. The evidence suggests that most creditworthy small and medium-sized businesses can currently get loans from private-sector financial institutions.

Many of our programs rely on emergency lending powers that require the support of the Treasury Department and are available only in unusual circumstances. By serving as a backstop to key credit markets, our programs have significantly increased the extension of credit from private lenders. However, the facilities are only that—a backstop. They are designed to support the functioning of private markets, not to replace them. Moreover, these are lending, not spending powers. Many borrowers will benefit from these programs, as will the overall economy, but for others, a loan that could be difficult to repay might not be the answer. In these cases, direct fiscal support may be needed.

Our economy will recover fully from this difficult period. We remain committed to using our full range of tools to support the economy for as long as is needed.

Thank you. I look forward to your questions.

Summary of Section 13(3) Facilities Using CARES Act Funding

The Municipal Liquidity Facility

The Municipal Liquidity Facility (MLF) helps state and local governments better manage the extraordinary cash flow pressures associated with the pandemic, in which expenses, often for critical services, are temporarily higher than normal and tax revenues are delayed or temporarily lower than normal. This facility addresses these liquidity needs by purchasing the short-term notes typically used by these governments, along with other eligible public entities, to manage their cash flows. By addressing the cash management needs of eligible issuers, the MLF was also intended to encourage private investors to reengage in the municipal securities market, including across longer maturities, thus supporting overall municipal market functioning.

Under the MLF, the Federal Reserve Bank of New York lends to a special purpose vehicle (SPV) that will directly purchase up to $500 billion of short-term notes issued by a range of eligible state and local government entities. Generally speaking, eligible issuers include all U.S. states, counties with a population of at least 500,000 residents, cities with a population of at least 250,000 residents, certain multistate entities, and revenue-bond issuers designated as eligible issuers by their state governors. Notes purchased by the facility carry yields designed to promote private market participation—that is, they carry fixed spreads based on the long-term rating of the issuer that are generally larger than those seen in normal times. With funding from the CARES Act (Coronavirus Aid, Relief and Economic Security Act), the Department of the Treasury has committed to make a $35 billion equity investment in the SPV.

As of September 18, the facility had purchased two issues for a total outstanding amount of $1.7 billion.

The MLF has contributed to a strong recovery in municipal securities markets, which has facilitated a historic issuance of more than $250 billion of bonds since late March. State and local governments and other municipal bond issuers of a wide spectrum of types, sizes, and ratings have been able to issue bonds, including long maturity bonds, with interest rates that are at or near historical lows. Those municipal issuers who do not have direct access to the Federal Reserve under the MLF have still benefited substantially from a better-functioning municipal securities market.

The Main Street Lending Program

The Federal Reserve established the Main Street Lending Program (Main Street) to support lending to small and medium-sized businesses and nonprofit organizations that were in sound financial condition before the onset of the COVID-19 pandemic and that have good longer-term prospects but which have encountered temporary cash flow problems due to the pandemic, and are not able to get credit on reasonable terms as a result. In addition to providing loans for borrowers in current need of funds, Main Street offers a credit backstop for firms that do not currently need funding but may if the pandemic continues to erode their financial condition.

Under Main Street, the Federal Reserve Bank of Boston has set up one SPV to manage and operate five facilities: the Main Street New Loan Facility (MSNLF), the Main Street Priority Loan Facility (MSPLF), the Main Street Expanded Loan Facility (MSELF), the Nonprofit Organization New Loan Facility (NONLF), and the Nonprofit Organization Expanded Loan Facility (NOELF). The SPV will purchase up to $600 billion in Main Street loan participations, while lenders retain a percentage of the loans. Main Street loans have a five-year maturity, no principal payments in the first two years, and no interest payments in the first year. Businesses with less than 15,000 employees or 2019 revenues of less than $5 billion are eligible to apply for Main Street loans. Available loan sizes span from $250,000 to $300 million across the facilities and depend on the size and financial health of the borrower. With funding from the CARES Act, the Department of the Treasury has committed to make a $75 billion equity investment in the SPV.

The business facilities (MSNLF, MSPLF, and MSELF) and nonprofit facilities (NONLF and NOELF) have broadly similar terms, but differ in their respective underwriting standards.

The business facilities use the same eligibility criteria for lenders and borrowers and have many of the same terms, while other features of the loans extended in connection with each facility differ. The loan types also differ in how they interact with the borrower's outstanding debt, including with respect to the level of pre-crisis indebtedness a borrower may have incurred. Similarly, the nonprofit facilities have many of the same characteristics, but some features of the loans extended in connection with each facility differ. Eligible lenders may originate new loans under MSNLF, MSPLF, and NONLF or may increase the size of existing loans under MSELF and NOELF.

Main Street became operational on July 6. The Federal Reserve and Treasury have modified the program several times to reflect extensive consultations with stakeholders. As of September 18, nearly 600 lenders representing more than half of U.S. banking assets have registered to participate in the program, and the program has purchased over $1 billion in participations.

Since Main Street became operational, the number of registered lenders and the amount of loan participations continue to increase. Program usage, will depend on the course of the economy, the demand for credit by small and medium-sized businesses, and the ability of lenders to meet credit needs outside the Main Street program. Demand for Main Street loans may increase over time if the pandemic continues to affect the ability of businesses and nonprofits to access credit through normal channels and as other support programs expire.

The Secondary Market Corporate Credit Facility

The Secondary Market Corporate Credit Facility (SMCCF) is designed to work alongside the Primary Market Corporate Credit Facility (PMCCF) to support the flow of credit to large investment-grade U.S. companies so that they can maintain business operations and capacity during the period of dislocation related to COVID-19. The SMCCF supports market liquidity by purchasing in the secondary market corporate bonds issued by investment-grade U.S. companies, U.S. companies that were investment grade before the onset of the pandemic and remain near-investment-grade, and U.S.-listed exchange-traded funds (ETFs) whose investment objective is to provide broad exposure to the market for U.S. corporate bonds.

Under the SMCCF, the Federal Reserve Bank of New York lends to an SPV that purchases in the secondary market both corporate bond portfolios in the form of ETFs and individual corporate bonds to track a broad market index. The SMCCF purchases ETF shares and corporate bonds at fair market value in the secondary market and avoids purchasing shares of ETFs when they trade at prices that materially exceed the estimated net asset value of the underlying portfolio. The pace of purchases is a function of the condition of the U.S. corporate bond markets. With funding from the CARES Act, the Department of the Treasury has committed to make a $75 billion equity investment in the SPV for the PMCCF and SMCCF, with a $25 billion allocation toward the SMCCF.

The SMCCF staggered its launch of ETF and bond purchases in order to act as quickly and effectively as possible. Through ETF purchases beginning on May 12, the SMCCF provided liquidity to the corporate bond market relatively quickly. The Federal Reserve began direct corporate bond purchases under the broad market index purchase program on June 16. In its first week of bond purchases, the SMCCF was purchasing about $370 million per day. As of

September 18, purchases have been slowed to a current daily pace of approximately $20 million of bonds and no ETFs, and the total SMCCF outstanding value has reached $12.8 billion.

The SMCCF's announcement effect was strong, quickly improving market functioning and unlocking the supply of hundreds of billions of dollars of private credit. Since late March, more than $800 billion in corporate bonds have been issued without direct government or taxpayer involvement. The SMCCF has materially reduced its pace of purchases over the past few months as a result of the substantial improvements in the functioning of the U.S. corporate bond markets. The pace of purchases going forward will continue to be guided by measures of market functioning, increasing when conditions deteriorate and decreasing when conditions improve.

The Primary Market Corporate Credit Facility

The Primary Market Corporate Credit Facility (PMCCF) is designed to work alongside the Secondary Market Corporate Credit Facility (SMCCF) to support the flow of credit to large investment-grade U.S. companies so that they can maintain business operations and capacity during the period of dislocation related to COVID-19. The PMCFF supports market liquidity by serving as a funding backstop for corporate debt.

Under the PMCCF, the Federal Reserve Bank of New York lends to an SPV. The SPV will purchase qualifying bonds and syndicated loans with maturities up to four years either as the sole investor in a bond issuance or as a participant in a loan or bond syndication at issuance, where the facility may purchase a maximum of 25 percent of the syndication. With funding from the CARES Act, the Department of the Treasury has committed to make a $75 billion equity investment in the SPV for the PMCCF and SMCCF, with a $50 billion allocation toward the PMCCF.

As of September 18, there have not been any PMCCF transactions, nor have any indications of interest been received.

The dual announcement of the SMCCF and PMCCF was well received by the market. Between March 23 and April 6, credit spreads for investment-grade bonds declined substantially. While the PMCCF has not purchased any bonds since it opened, it serves as a backstop should markets enter another period of stress.

The Term Asset-Backed Securities Loan Facility

The Term Asset-Backed Securities Loan Facility (TALF) supports the flow of credit to consumers and businesses by enabling the issuance of asset-backed securities (ABS) guaranteed by newly and recently originated consumer and business loans.

Under the TALF, the Federal Reserve Bank of New York lends to an SPV. The SPV will make up to $100 billion of three-year term loans available to holders of certain triple A-rated ABS backed by student loans, auto loans, credit card loans, loans guaranteed by the Small Business Administration (SBA), and certain other assets. The Federal Reserve lends an amount equal to the market value of the ABS less a haircut and the loan is secured at all times by the ABS. With funding from the CARES Act, Treasury has committed to make a $10 billion equity investment in the SPV.

As of September 18, the TALF has extended $2.9 billion in loans since its launch on May 20. Loans have been collateralized by SBA-guaranteed ABS, commercial mortgage-backed securities (CMBS), and premium-finance and student-loan ABS.

The announcement and presence of the TALF has helped improve substantially liquidity in the ABS markets, including those for CMBS and collateralized loan obligations, with spreads in some ABS sectors returning close to normal levels. The TALF interest rates are attractive to borrowers when market conditions are stressed, but not in normal conditions. While the facility is authorized to extend up to $100 billion in loans, total take-up will likely be much less unless ABS market conditions worsen.