Questions for Dr. Janet Yellen
Distinguished Fellow in Residence at the Brookings Institution

July 17, 2020 Hearing: "Former Federal Reserve Chairs On Responding To Our Nation's Economic Crisis"

Questions from Rep. Mark Green (TN-07)

---

1. For the first time ever, the Federal Reserve is buying municipal bonds. We know that blue states like Illinois have been spending recklessly for decades, with severely underfunded pensions, while many red states like Tennessee have been responsible and have fully funded pension plans. If we bail out irresponsible states, what is their incentive to get their fiscal houses in order?

ANSWER FROM JANET YELLEN

Many financial markets, including those for corporate bonds and municipal debt, became volatile and extremely illiquid after the onset of the pandemic in March. The Federal Reserve established, with the agreement and backing of Treasury, a number of facilities to insure that credit continues to flow in these securities markets. The Fed's Municipal Liquidity Facility only purchases short-term notes backed by anticipated revenues, and the facility is only available for entities that, as of April 8, 2020 were rated investment grade (at least BBB-/Baa3) by two or more recognized statistical rating organizations. The interest rates offered on the loans are in line with market spreads. Conditions in municipal bond markets have improved, partly due to the establishment of the facility as a backstop. As a result, it has been little used. As of July 9, there was only one loan outstanding.

2. American consumers and businesses have record debt in part due to the Fed's low interest rates and previous Administration programs which encouraged excessive borrowing. Do you believe there is any chance that the Federal Reserve could enact negative interest rates in the next year or two? Is this something you would advise? Why or why not?

ANSWER FROM JANET YELLEN

The Federal Reserve has expressed a strong disinclination to enact negative interest rates and, to the best of my knowledge, negative interest rates are not under active consideration. I think this is a sensible policy stance. Although negative rates have been implemented in the euro area, Japan, and some other developed countries, their effects on overall credit conditions are uncertain and researchers differ in their views. Negative interest rates tend to diminish the profitability of banks: most banks have not been able to pass them on to retail customers. The resulting pressure on banks may lead them to tighten credit, which, in turn, would have an adverse economic impact. Negative interest rates could also create significant strains in U.S. money markets.