
CONFERENCE OPENING REMARKS

Welcome to the Federal Reserve Bank of New York, and thank you for coming to this conference on central bank liquidity tools.

As acting manager of the Federal Reserve’s System Open Market Account (SOMA), I am responsible for reporting to policymakers on the implementation of monetary policy in pursuit of the objectives that they have set. This includes the ways in which the Fed’s balance sheet is being used as well as the ways in which financial conditions are impacting both the stance of monetary policy and its transmission to credit markets. In recent months, of course, this has also included the impact of what some have called our “alphabet soup” of liquidity facilities and programs.

I am very pleased to lead off this conference—the first of many conferences, I am sure—on central bank liquidity tools. When the organizers put this conference together many months ago, we knew there would be much to talk about. Little did we know that the number of liquidity tools and the depth of the financial crisis would continue to expand and to challenge us in the intervening months.

The expansion of the Fed’s liquidity tools has been nothing short of extraordinary. In normal times, we essentially use four tools to manage the SOMA portfolio: temporary open market operations (OMOs), permanent OMOs, the discount window, and securities lending. By March 2008, when this conference was organized, we had nine tools; now, if we include the Term Asset-Backed Securities Loan Facility (TALF) and our new purchase programs, we have sixteen according to my count.

We tend to group the Fed’s liquidity tools into three broad categories. In the first group, we have facilities that provide term liquidity to financial institutions—particularly to large, systemically important ones. These exist to reduce the systemic risk associated with the inability of a financial institution to get wholesale funding, which could in turn lead to a widespread deleveraging cycle involving forced asset sales that would ultimately become self-reinforcing, particularly for the largest financial institutions. In short, these facilities exist to forestall runs. These include the Term Auction Facility (TAF), foreign central bank swap lines, and the Primary Dealer Credit Facility (PDCF).

In the second group, we have facilities that provide liquidity directly to borrowers and lenders in key credit markets to prevent further declines in credit formation. These include the TALF, the Commercial Paper Funding Facility (CPFF), and the Money Market Mutual Fund Investor Funding Facility (MMIFF).

In the third group, we have programs involving the direct purchase of assets, particularly housing-related ones. These include our purchases of agency debt and mortgage-backed securities (MBS).

It is no accident that the Fed started with the first group in the early stages of the crisis. When this conference was organized, the Fed was addressing the crisis by rearranging its balance sheet, expanding lending programs, and reducing its holdings of Treasury securities. Many of the papers in this conference directly address the use of these types of tools and their links to funding and market liquidity issues.

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Among the many issues that we are hoping this conference will address are: What has the current crisis taught us about the use and effectiveness of traditional and new liquidity tools? To what extent might the expanded toolkits of central banks be useful for policy implementation in normal circumstances? Which tools are better kept as extraordinary measures?

Of course, last fall the balance-sheet constraints of large financial firms and funding pressures became a full-blown financial crisis with seriously impaired credit formation, a deep recession, capital assistance to large banks, and a significant feedback loop between financial and macroeconomic weakness. In response, the Fed has begun to use the asset side of its balance sheet to affect credit provision directly in key markets, such as those for commercial paper and MBS. To the extent possible, the Fed attempts to do this in a way that improves market functioning and liquidity, in order to set the stage for the private sector to return in the future. As a result, our balance sheet has ballooned with the expansion of both the size and number of our programs—our alphabet soup.

But a policy of credit easing in the currently very extreme situation raises a host of questions that I encourage everyone here to pursue in future research. Among these are: How can

we measure the effectiveness of such policies? In Chairman Bernanke's terminology, "How should the central bank think about the impact and stance of monetary policy when pursuing a policy of credit easing?" How does one think about the size of the central bank's balance sheet? For example, some of the Fed's facilities are designed to expand when credit and market conditions deteriorate sharply, and to contract when conditions improve. During the last few weeks, for instance, the swaps program decreased by \$150 billion.

As I mentioned at the outset, this will certainly not be the last conference on this topic. It is fair to say that economists, central bankers, and historians will be analyzing this financial crisis and the policy responses to it for decades to come. Nonetheless, we here at the Federal Reserve Bank of New York—who sometimes feel we are in the trenches every day—appreciate the insights that this conference can provide, preliminary though they may be. Because we are so close to many of these programs, we also appreciate the distance and perspective that your research can give. We particularly look forward to your future work in this area. I am guessing that central banks have provided you with a rich research agenda.

Again, welcome, and thank you for coming.

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