OPENING STATEMENT OF REP. MELVIN WATT

Financial Services Committee Hearing Entitled, "An Examination of the Extraordinary Efforts by the Federal Reserve Bank to Provide Liquidity in the Current Financial Crisis"

Tuesday, February 10, 2009

In these difficult economic times which, by all accounts are unprecedented at least since the Great Depression, the Federal Reserve has had to consider every lever and tool at its disposal. We are here today to review some of these extraordinary levers and tools.

The tools being used by the Fed are authorized by Section 13(3) of the Federal Reserve Act which allows the Fed in "unusual and exigent" circumstances to lend broadly to individuals, partnerships or corporations in any industry, if the Board determines that such entity cannot secure adequate financing from other banking institutions, and that entity has produced collateral to the Board's satisfaction. Using this authority, starting in 2008 and continuing this year, the Federal Reserve has set up emergency lending facilities to address severe market strains in commercial paper by activating a Commercial Paper Funding Facility, to address severe strains related to money market funds by activating a Money Market Liquidity Facility, and announced earlier today that it plans a substantial expansion of its Term Asset-Backed Securities Loan Facility.

In a recent lecture at the London School of Economics, Federal Reserve Chairman Bernanke described three policy tools (other than reducing the federal funds rate) that he reaffirmed that the Federal Reserve has the authority to use to directly extend credit or purchase securities: (1) the provision of short-term liquidity to sound financial institutions; (2) the provision of liquidity directly to borrowers and investors in key credit markets; and (3) the direct purchase of longer-term securities to support the credit markets. The use of each of these tools will, of course, expand the balance sheet of the Federal Reserve and subject the Fed to more attention, scrutiny, second guessing and oversight. Otherwise, we run the risk that authority granted in a 1933 statute could be "out of control" or subject to abuse.

The use of each of these tools also raises the question: what happens when the "unusual and exigent circumstances" are over? What is the "exit strategy" for winding down the various Fed lending programs when we return to normal times?

Today's review of the Fed's power under Section 13(3) of the Federal Reserve Act is the first in a series of hearings and other actions that we must take to evaluate steps that certainly appear to be necessary to combat the economic crisis that confronts us. I trust that our evaluation will be transparent, open and fair and welcome Chairman Bernanke's testimony.