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YPFS Lessons Learned Oral History Project: An Interview with Lorie Logan

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Lorie Logan

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Yale SCHOOL OF MANAGEMENT
Program on Financial Stability

Lessons Learned Oral History Project Interview

Interviewee Name and Crisis Position	Lorie Logan[1] Director of Treasury Markets, Open Market Trading Desk, Federal Reserve Bank of New York
Interviewer Name	Mercedes Cardona (Contractor) Yale Program on Financial Stability
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Introduction:

The Yale Program on Financial Stability (YPFS) reached out to Lorie Logan via email to request an interview regarding her role in the development and implementation of the Federal Reserve's crisis-era policies, including the expansion of the Federal Reserve's balance sheet and the creation of liquidity facilities to mitigate systemic risks to the financial system[2].

Ms. Logan is executive vice president in the Markets Group of the Federal Reserve Bank of New York, the System Open Market Account (SOMA) manager for the Federal Open Market Committee (FOMC), and head of Market Operations, Monitoring, and Analysis (MOMA). This is the area responsible for the execution of monetary policy at the direction of the FOMC, provision of fiscal agent services to the U.S. Treasury Department in support of debt issuance and foreign exchange operations, analysis of financial market developments, and production of the New York Fed's reference rates, including the Secured Overnight Financing Rate. She is also the senior New York Fed representative on several public-private committees advancing industry best practices, including the Treasury Market Practices Group, the Alternative Reference Rates Committee, and the Foreign Exchange Committee.

[This transcript of a telephone interview has been edited for accuracy and clarity.]

YPFS: **As I mentioned, we're doing this oral history of the global financial crisis, putting together an archive for researchers in the future, for economists, for scholars, maybe even journalists who need information. We're talking to people who were involved in the management of the global financial crisis in 2008. So just to get some housekeeping out of the way, I am recording this conversation and I will send you a transcript when it's completed so you can**

[1] The opinions expressed during this interview are those of Ms. Logan, and not those any of the institutions for which the interview subject is affiliated.
[2] A stylized summary of the key observations and insights gleamed from this interview with Ms. Logan is available here in the Yale Program on Financial Stability's *Journal of Financial Crises*.

review it. It'll be part of our archives after it's corrected and fact checked. I just wanted to get that out of the way; also if you had any sort of advisory.

Logan: I would note that the views that I discuss today are my own and do not necessarily reflect those of the Federal Reserve Bank of New York or the broader Federal Reserve System.

YPFS: Why don't we start with a little chronology. Where were you at the time? You were the New York Fed, if I am correct, about 10 years before the global financial crisis. You've been there for a while. What were you working on when this whole thing came to a head?

Logan: I've been at the New York Fed since 1999, so I'd been there for some time before the global financial crisis really took hold. In the fall of 2008, I had the position of being Director of Treasury Markets. That's an area on the Open Market Trading Desk, which has a responsibility for a couple of key things.

First, the Desk is responsible for implementing monetary policy at the direction of the FOMC. In the pre-crisis framework, part of that managing of the federal funds rate was the ability to purchase and sell treasury securities or to do repos (or repurchase agreements) or reverse repos to adjust the supply of reserves in the banking system. One of my responsibilities was the purchase and sale of treasury securities.

The second big thing we did was, we were responsible for being fiscal agent for the U.S. Treasury, which meant we conducted Treasury auctions on their behalf. We also did a lot of market monitoring for policy makers, both in the Federal Reserve System and also with the U.S. Treasury. My team, in particular, was responsible for understanding and reporting on developments in the U.S. Treasury market.

YPFS: As you were doing your market monitoring in 2008, were you seeing all the various factors that brought about this crisis coming together and shaping up in the year before, as the housing market bubbled up and you saw institutions like Bear (Stearns) and Lehman (Bros.) start to experience trouble? Was there some urgency to address some of these factors before it all came to a head on that September of 2008?

Logan: When I think about the beginning of the crisis period, I really go back to the first quarter of 2007. That's when we first started to see developments beginning to emerge. I would say that a lot of the work that we did in the crisis really began over the first and second quarter of 2007—a lot of the preparations and thinking about liquidity and some of the challenges we were working on in the background throughout that year.

That really came together later in 2007 when the FOMC introduced one of the first liquidity facilities, which was the Term Auction Facility (TAF), in response to those liquidity pressures. That facility was very similar to the discount window in providing liquidity to banks, but it used a new, unique form to auction that, instead of as a lending backstop. The purpose of that was really to remove stigma through the auction format. So we really did start to identify issues in 2007 and then to begin to make adjustments in the type of operations that we had within the framework. That first one was the TAF in 2007.

By 2008, those liquidity pressures, even with the TAF and the swap lines that had also been introduced by that point, were still growing. We developed two other liquidity facilities that I was actively involved in.

One of those was the Term Securities Lending Facility or what we called the TSLF. That's something that we started thinking about in broad terms probably over the third and fourth quarter of 2007, but really came together in 2008.

TSLF was a weekly loan facility to primary dealers, so this was moving the liquidity provision beyond the banks to broker-dealers or our traditional counterparties to open market operations. This program - the TSLF – was really using a traditional program we had called securities lending, but in a novel way. And this program was really instrumental in supporting market functioning and liquidity over the next year.

We also, at that time—I guess it was around the Bear (Stearns) time in March 2008, because the TSLF had been announced but not yet operational (there was still some more work to do to make it operational)—the key weekend when the liquidity was needed, we introduced a new facility called the Primary Dealer Credit Facility to augment lending to broker dealers. Instead of being bond-for-bond, this was bond-for-cash, more like what the discount window could do, but for broker-dealers. So that facility was developed at that time – in a weekend.

They had a lot of similarities, those two programs. Both were born out of infrastructure that we had for our existing operations and both similar in nature to other programs that we did, but novel in their liquidity provision to broker-dealers.

YPFS: **There have been a lot of changes in bank liquidity practices since that Great Recession. I believe I read somewhere there was some talk about quote unquote normalizing the balance sheet and then the Fed stepped in to stabilize the repo market recently. I saw some remarks about how the Fed may need to buy even more funds than before the recession to sort of manage the rate fluctuations. Was this sort of flexible approach, this flexibility in managing liquidity and the balance sheet one of the lessons learned from the financial crisis? Can you talk a little bit about how this helps shape the policy that we have today?**

Logan: I really do think that's right. We really do value active learning and maintaining operational flexibility. Both were core principles that guided our implementation of monetary policy then and do so today.

In recent years, we've been normalizing the balance sheet, which obviously grew during the crisis and then after the crisis, through unconventional policies. But we've been normalizing it by gradually reducing the securities holdings that were accumulated in the stages during and after the crisis. And by reducing, we were also reducing the supply of reserve balances in the banking system.

This year was a really important year in the culmination of a lot of work. The FOMC, in January, announced that it intended to implement policy in a framework based on an ample supply of reserves. And under this framework, the control of the Fed funds rate is achieved using the Fed's administered rates and active management of the supply of reserves is not required.

So, the type of operations that I talked about that we were doing and in 2007 are not the type of operations we would do in this new framework, because we wouldn't actively manage the supply of reserves. So that was a really big decision for the FOMC.

More recently, the committee said that it had concluded the reduction of that normalization of the balance sheet and then it would allow the amount of reserves to continue to decline through the growth in our non-reserve liabilities. That's what was happening over the course of this summer, and then when we got into September and we experienced some unexpected volatility in money markets, at that point the FOMC determined it would be appropriate to maintain reserves back at the level that was prevailing in early September.

One of the key lessons here is that, post-crisis, banks' business models have adjusted both based on the regulations and the supervision as well as their risk management practices such that their demand for liquidity is higher. And so the amount of reserves we'll supply in this new system will be higher and part of this new regime that we're in is as a result of that change in the financial system. So, as part of this ample reserves regime, we'll be continuing to monitor and understand banks demand for reserves based on these surveys and outreach we do to banks and learning from our monitoring money markets developments. So, it really is kind of coming full circle, over the course of this year.

YPFS: **I read the chapter you wrote about normalizing the Fed's balance sheet and the policy implementation. You were talking about how there's been changes in bank reserves, the regulation and the appetite for risk. Has that appetite for risk returned since? As you mentioned, there's been some moments when you've had to step in. Or have the lessons of the housing bubble being taken to heart among the financial institutions?**

Logan: Reserves are the most reliable and safest source of liquidity. They're immediately available for payments that a bank needs to make and the market value of them doesn't change. That was true before the crisis, but it's also true today. But I think the way that we manage liquidity, because of the introduction of interest on reserves and the increased focus that banks now place on managing their liquidity, has changed the overall demand for those reserves, even if the characteristics of reserves are the same.

Also banks' willingness to borrow from the Federal Reserve post-crisis has changed because of stigma. That stigma was there before the crisis, but it grew during the crisis. Banks have an increased precautionary demand for reserves as well, partly related to that.

I think an important thing to always keep in mind is that banks demand for reserves really isn't static and we've seen that evolve. It shifts because of the change in regulation, or supervision, or risk management. And that risk management then can change based on business models, or economic, or financial conditions. And so, we have to have a good way of understanding how that demand for liquidity is changing.

We've really done a couple of key things in the last two years. We've developed a new survey, which we call the Senior Financial Officer Survey that covers, about 70 or 80 banks in that whole group right now, or about three quarters of the reserves in the banking system. We asked them a number of questions about how they think about their demand for liquidity and demand for reserves, so that we can better measure and understand the drivers and the overall size.

But still, even with those efforts through the survey and through our outreach that we do regularly, it's important to note that that demand for reserves and liquidity is unobservable and does change. So it will be a continual effort that we'll be doing, as we move forward.

YPFS: **So getting back to the narrative of 2008, what was the atmosphere like that weekend in September when suddenly on Friday you had the stock market cratering and AIG coming to a head and Lehman and all these various institutions? What were the priorities on that immediate moment when everybody started meeting to figure out what to do next? Was it mainly to avert the bank collapses immediately? Was there a larger picture? Can you walk us through some of the debates in those early days?**

Logan: I definitely think that, the Federal Reserve System and other policy bodies were extremely active across a number of fronts. From the seat that I was in at that time, we were focused on two things. One was understanding what was happening in financial markets and the other was understanding liquidity needs and how the operations that we had already built and had in place were working and what new liquidity provision may be required because of the developments we were seeing.

A key thing for us was after the collapse of Lehman and the reserve primary money market funds broke the buck, there was a real run on repo that threatened to spread to all the remaining firms and money market funds. And so, one of the two things I was most focused on: we had the commercial paper market that we were focused on, and we were working on a solution to that, and one of those key solutions was what we called the Commercial Paper Funding Facility, which was a really critical response to that time period.

That was announced in early October and then became operational later that month, but it involved a really novel approach to liquidity provision and the development of a special purpose vehicle to purchase CP (commercial paper) and ABCP (asset-backed commercial paper) directly from the issuers with funding provided by loans from the Federal Reserve. This was under Section 13(3) of the Federal Reserve Act.

It was a really broad market backstop to those markets and it really met the need for term funding by purchasing three-month paper at spreads that were significantly narrow then that was prevailing earlier. So that was a really key development.

But by far the most difficult and I think contentious issue was how to think about the credit extension and that SPV. And we talked a lot about that in the paper that we wrote.

Some of the other things were continuing to adapt the PDCF (Primary Dealer Credit Facility) and the TSLF (Term Securites Lending Facility) programs during that time period and understanding their usage and the drivers behind that usage.

YPFS: **The political environment has changed a lot in 10 years because before the financial crisis. These were very opaque organizations--the Fed, the regional feds, and the Treasury Department were seen as standing above it all. But now bank bailouts and "too big to fail" got into the popular imagination. Do you see this sort of opacity ever returning or are we going to have a more open Fed where decisions like these are a little bit more transparent, to get the public on board with some of these changes?**

Logan: There's been a real and permanent shift in thinking about transparency and accountability. Transparency's vitally important and is a key component of the way we think about the work that we do. This transparency can be seen, at least from my own vantage point, in all of the different major areas of the Federal Reserve.

From a monetary policy perspective, Chairman Bernanke began conducting press conferences on a quarterly basis. Chair Powell's now doing that after each meeting. They released the Summary of Economic Projections and are much more transparent about how they're thinking about their views on the uncertainty and

risks around the economic outlook. In the supervisory realm, there's been a lot of efforts to increase transparency with stress tests and other elements to restore and sustain public confidence in the system. On the financial stability side, where there's now an official assessment of financial stability discussed four times a year at the FOMC meetings and then the minutes are released from those discussions.

Where I sit, the most meaningful is in the area of monetary policy implementation. We've just made concerted efforts to become more transparent with our operations. On our public website we publish all of our statements, in-depth FAQs, and all the parameters about our operations, but really importantly, we publish transaction-level data with a two-year lag now across all of our operations. This came about with the Dodd-Frank Consumer Protection Act of 2010. We've always published an annual report, but that report now is over 60 pages and has just numerous charts and data that's also provided to the public. So I would say overall, the Fed has just become a much more transparent and open place and I think that's here to stay.

YPFS: **Also, in communicating among decisionmakers and regulators, I spoke to Chris Seefer, who was with the Congressional Crisis Inquiry Commission, and he was talking about how before the crisis, some regulation was very compartmentalized, which might have contributed to the housing market situation going unchecked, because the right hand didn't know what the left hand was doing. What about communication between the regulators today?**

Logan: I'm not personally on the supervisory side, but I think there are two really visible examples of how this collaboration and communication has improved and are critically important to understanding the landscape in the financial sector. But there's also been real changes in efforts that are closer to home for me.

The two that I would say more broadly have enhanced communication, first is the development of the Financial Stability Oversight Council. I think you know the details on the makeup and the management of that council already. From where I sit, that has been a really important development and has generated a lot more cross-agency communication even at the staff level, but also in joint work that emanates from those relationships and from the committee itself.

There are also a lot of other inter-agency efforts that have been formed. On October 15th, 2014, there was a really big rally in the U.S. Treasury market that was very unexpected, very large, very notable. And after that event, the Treasury, the Fed, the SEC and the CFTC came together to develop an inter-agency research effort to understand what happened on that day and what might've led to it.

This is another great example of how those processes have changed. And that report led to a regular conference that's now held every year and as well as efforts

to seek more data about the treasury market to better understand how it's changing. So, you can really see that coming together in concrete ways.

On the monetary policy implementation side, where I have responsibility, there's a lot more interaction between supervision and markets in understanding liquidity that was developed during the crisis and has been maintained. Those are just a few examples of ways that collaboration and communication have changed. There was always communication between the U.S .Treasury and the Open Market Trading Desk, given the nature of our work and our responsibilities, our fiscal agent, and that continues to this day.

YPFS: **Looking forward, I was reading recently an interview with John Williams in the New York Times and he name-checked you. He said "Lorie and her team were preparing for years." And as you mentioned, you had been working from 2007, been seeing the signs and making preparations. If we were to drift into another financial crisis--which do tend to happen with some cyclicality--do you feel that the New York Fed is well-prepared at this point? What are some of the learnings that have been put into place?**

Logan: It's certainly difficult to predict future crises and my experience over the last two decades suggests that they're usually different from the ones before, but I think there are a couple of key things that we've changed that make us better positioned. I know there are many others, but three that I've really been involved in.

One is: The market analysis and monitoring that we do has certainly changed. It was very focused on the primary dealer community and the banks and the dealers that we directly dealt with before the crisis. Since the crisis, we've really expanded our outreach and our relationship across the financial sector to the buy-side to electronic trading firms. Our whole understanding and outreach of the financial markets has expanded both in size and in depth.

The second is: from an operational perspective, we took some really important lessons in terms of how to be ready and positioned. During the crisis we developed a number of new liquidity operations and tools. We wanted to be able to have a system for maintaining the ones that were most important, through normal times to have them here and ready, but also to have other tools that maybe weren't important in the implementation framework at the time but could be important under certain states of the world. So we developed a full operational readiness framework for cataloging, for assessing which operations to have ready and to maintain and to practice them.

Out of that came a regime of small-value testing, that we do on a regular basis, of tools that may not be important today but could be important in the future. Just recently, we needed to conduct repo operations again, which we hadn't done in over a decade, since the crisis. But we had been doing these small-value tests of

them and that was critically important in our ability to respond quickly in September.

The last thing I'd mention is the development of a new area within the New York Fed called the Applied Critical Thinking Team. This is run by Meg McConnell who's been involved in this work. We do a lot of work with that team, thinking about how to examine decision making and learning to bolster our capacity to learn and to adapt and to innovate in the face of challenges that are unexpected.

In other words, the work that they're doing is to ask tough questions and push us to think about what we could be missing and to challenge our assumptions and biases in the work that we're doing. This is a critical change in our approach to help us be better prepared for the next crisis and to really, as Meg always says, to shift the lens and look for puzzles, rather than the stories that we already know. And so I think that's important both for our analytical work and our market outreach, but also in how we prepare the operations that we're conducting.

Logan: Meg would be a great person to talk to, and was a leader during the crisis within the New York Fed. And now, Meg’s role and the work that the ACT does is unique and tremendously value to us. It’s important to have someone come in with a third-person perspective, to make us familiar with and comfortable with complexity and uncertainty, and to ask us to take a step back and evaluate things we think we know and things we don’t.

YPFS: Summing up, if you were to say what would the topline lessons that you've learned from the global financial crisis? What would you do your PowerPoint slide with?

Logan: This is a really tough question and something that I've been reflecting on a lot lately. I guess if I had to write a memo to myself, I would focus on at least three things. First is around preparation and testing. Testing your operations, your infrastructure and your thinking. This really comes from lessons I took from the crisis that formed the basis of our operational readiness framework, our small-value testing process and lessons I've learned from the Applied Critical Thinking Team that Meg has developed. Doing regular tabletop exercises to stimulate your thinking about scenarios and getting comfortable making judgements with imperfect information along the way. So preparation, in particular, and spending a good amount of your time preparing for what could happen, as opposed to what you're working on today.

The second is really about people. My experience from the crisis underscored the importance of being surrounded by an experienced, diverse, and well-rounded team. It's really important to be around people who can come at a problem in different ways and who bring different viewpoints to the table. And that's really important: to have a team that will challenge thinking, who aren't afraid to bring up points and views that are different. This diversity of thought is just absolutely essential.

And lastly, just a core principle of humility. You have to be humble about what you know and what you don't know; to be curious about things you think you know about and things you don't know about. And be flexible to make decisions, and knowing that you're making decisions most of the time with imperfect information. Having that humility and that curiosity will allow you to adjust in real time as more information comes in.

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