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Lessons Learned: Matthew Rutherford

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Yale Program on Financial Stability Lessons Learned

Matthew Rutherford

By Mercedes Cardona

Matthew Rutherford served as the deputy assistant secretary for federal finance at the US Department of the Treasury from 2009 to 2012, before becoming assistant secretary for financial markets. During his tenure, Rutherford generated reports on the status of mortgage-backed securities wind-downs purchased by the Treasury to stabilize financial and housing markets under the Housing and Economic Recovery Act (HERA). Before joining Treasury, Rutherford worked for the Federal Reserve Bank of New York (FRBNY) and served as liaison with Treasury on the Bank's behalf. He also helped establish the Department's Markets Room. This "Lessons Learned" is based on an interview with Rutherford in July 2021; the full transcript may be accessed here.

Weaknesses in the regulatory environment should be identified and addressed ahead of a crisis, or they will have to be accounted for and worked around in fighting the crisis.

In the early months of the Global Financial Crisis (GFC), Rutherford was the debt management liaison from the FRBNY's Markets Group to the Treasury Department. This gave him a unique perspective across two critical agencies. At the time, "the Debt Management Group at the Treasury was a relatively small group that didn't have a lot of markets experience or resources to follow markets," Rutherford said. "It's hard to respond to what's happening in the world if you don't have a good sense of what's actually happening in the financial system," he added. Treasury arranged to "borrow" him from the FRBNY so he could establish a Markets Room, which maintained relationships with market participants, completed daily real-time analysis, and tracked market activity providing policymakers with much-needed market intelligence.

According to Rutherford, another weakness in the US system was how regulation over the financial system was fragmented and distributed across many agencies, which contributed to the difficulty in mounting a crisis response. "If you were going to devise a regulatory system, I guarantee you, you would not devise it the way it's structured today," said Rutherford.

A number of important players had no statutory authority to act when the markets were in turmoil. Rutherford noted that, to this day, the Securities and Exchange Commission (SEC), a key market regulator, has no authority by statute to act to stabilize trading markets, and in the GFC, coordination with the Fed was less than ideal:

> I'm not sure it would have really changed the course of history tremendously, but it certainly would have helped if it was more streamlined. If you remember, the Federal Reserve started to put people [examiners] in the broker-dealers. I think we had some sort of agreement with the SEC. I can't remember how all of this worked, but we had people monitoring their liquidity. Why couldn't we just get that from the SEC? I never quite understood that.

Rutherford cited the Office of Federal Housing Enterprise Oversight (OFHEO) as another ineffective regulator. In charge of supervising the government-sponsored enterprises (GSEs), such as Fannie Mae and Freddie Mac, OFHEO had limited powers. So, when the mortgage finance giants faltered, it could not do much. Only after Congress passed the Housing and Economic Recovery Act (HERA)-could the government put the GSEs into conservatorship. HERA created a new regulatory agency (the Federal Housing Finance Agency) and gave the Treasury authority to put money into the firms, and the Troubled Assets Relief Program (TARP) later gave Treasury even more authority to act. Before HERA, Rutherford said, "I think the senior leadership of Treasury had a lot of anxiety about what was going on, but it was very difficult for them, because they had no tools. So, they were kind of a bystander."

To be effective, crisis-fighting program goals must be clearly defined, and the program has to be rightsized.

Rutherford managed the Treasury's mortgage-backed securities purchase program, which he termed "a nice-to-have, but it wasn't the solution to our problems." He had initially advocated for the Fed to carry out that function because he thought it needed to be much bigger than the Treasury's authority to be effective: "we needed someone with an unlimited balance sheet, like the Fed, to actually buy mortgages." While Treasury allocated $250 billion to the program, that was not enough to meet the severity of the situation, said Rutherford.

That the size of the budget was unmatched to the problem at hand meant the goals were also scaled down. The program's goals were vaguely defined, which didn't help the perception that the government stepped in to bail out banks, while leaving homeowners to foreclosure. Rutherford explained:

> Two hundred and fifty billion dollars wasn't enough to contain spreads. So, you couldn't outline that as your objective because you'd fail, because it's just not enough. So, I think it had a more ill-defined role that was something like "to assist in market functioning" or something like that. And it certainly helped, don't get me wrong, but it was never a program that was going to lower mortgage rates to people in this country, let's put it that way.

The Treasury ultimately purchased a total of $225 billion of GSE MBS, a number dwarfed by the similar program undertaken by the Fed a month later. Under its Large Scale Asset Purchase Program, the Fed purchased $172 billion in agency debt and $1.25 trillion in agency MBS. Given the Fed's program, Treasury was able to narrow the focus of its program to increase its effectiveness, said Rutherford.

> We sort of changed the goal of the program once the Fed came out with their trillions of dollars of bond buying. I think their pretty explicit goal was to move mortgage spreads lower. We started trying to provide liquidity to a different part of the agency mortgage market, the specified pool market, which was under some liquidity strain. It's a smaller corner of the mortgage market. We were trying to provide liquidity there, and I think that was successful and played a smaller role than the Fed,

> obviously, in correcting or alleviating the strain in the mortgage market. So, in that sense it was successful.

Applying the lessons learned in previous crises can improve the effectiveness of responses to later ones.

By comparison to 2008, said Rutherford, the management of the COVID-19 crisis in 2020 was much better and reaped better results; he gives Treasury and the Fed an A+ for stabilizing the economy after the initial shock of the quarantine lockdown. In his opinion, the government's response was aided by having many of the same people around that were in the government 13 years earlier—and also by building on earlier experiences. He explained: "Obviously, a lot of what was rolled out was a template. They used the template of 2008, as well as a bunch of new programs, which obviously was hugely important." He credited the successful effort to coordination across the agencies, the work of the Financial Stability Oversight Council (FSOC), and the Treasury's Markets Room, which provided up-to-date information.

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