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REUTERS

#TOP NEWS

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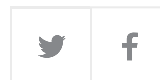
Fed opens curtain on $3.3 trillion of crisis lending

Pedro Nicolaci da Costa and Rachelle Younglai



WASHINGTON (Reuters) - The Federal Reserve on Wednesday released details on $3.3 trillion (2.11 trillion pounds) in emergency loans made during the financial meltdown that showed Citigroup and Bank of America leaning on overnight loans from the central bank well into the spring of 2009.

The findings, published in accordance with a deadline set by a wide-ranging rewrite of U.S. financial rules enacted in July, shed light on who benefited most from the central bank's controversial efforts to support financial institutions and credit markets.

The results could reignite debate about whether some bailouts, such as the support for insurer AIG, were appropriate, although financial markets largely ignored the report.

"It will serve to remind folks that we were in a bad place and the Fed stepped in to help, but might also reopen some old political wounds," said John Cannally, economist at LPL Financial Boston. "It's interesting historical background but the market has largely moved on."

As the financial crisis that began in the summer of 2007 spread beyond the housing sector to the nation's biggest banks, the Fed, under the leadership of Chairman Ben Bernanke, devised

increasingly complex facilities to help restore confidence.

Among these were loans to broker-dealers made outside the Fed's usual discount lending window for troubled institutions, which is reserved for deposit-taking commercial banks.

Barclays Gets $47.9 Billion

The Fed made more than 1300 loans under the Primary Dealer Credit Facility, or PDCF, set up for broker-dealers, with the largest -- $47.9 billion -- going to London-based Barclays, the Fed's data showed. The facility marked the first time since the Great Depression that the Fed had lent to non-depository institutions.

Many banks tapped the facility after it was launched in the wake of investment bank Bear Stearns' collapse in March 2008 but borrowing dried up by late summer.

However, after Lehman Brothers filed for bankruptcy in September 2008, the Fed faced a crush of demand as financial markets froze and banks scrambled for cash.

Borrowing from the PDCF peaked that month at $156 billion, but Citigroup kept borrowing into late April 2009, while Bank of America took out its last loan in May 2009.

Other key emergency lending measures included an attempt to revive commercial paper markets with funding from the Fed, as well as a program aimed at securitization markets that also tapped central bank money as an incentive for new deals.

Most of the loans have been fully repaid, although analysts say the Fed is still exposed to market risk both through its purchases of long-term assets and its loans to financial companies Bear Stearns and AIG. The asset purchases will total $2.3 trillion once the latest round of bond buying ends in June.

"The Federal Reserve followed sound risk-management practices in administering all of these programs, incurred no credit losses on programs that have been wound down, and expects to incur no credit losses on the few remaining programs," the central bank said in a statement.

Foreign Banks Get Support

Arguably, the Fed's most contentious and politically costly decision was the rescue of insurance giant American International Group. Criticism of the Fed grew after it emerged the AIG's counterparties were paid off with taxpayer funds.

The Fed's support for foreign banks that operate in the United States, such as Barclays, was controversial as well. In addition to Barclays, BNP Paribas Securities, Daiwa Securities America, Deutsche Bank Securities, Mizuho Securities USA, Dresdner Kleinwort Securities and UBS Securities LLC all received support from the PDCF.

Questions linger as to why the Fed and U.S. Treasury decided to let Lehman go, touching off the most virulent phase of the crisis, after they had acted to save Bear Stearns. The Fed has argued it could not extend a loan to Lehman because the firm was insolvent.

Through it all, the Fed was criticized for being too close to the banking sector, while not doing enough to support the broader economy. In recent months the financial sector has recovered smartly but that rebound has failed to translate into a vigorous economic expansion.

The controversy led to efforts by Congress, eventually thwarted, to curtail the central bank's regulatory authority and regularly audit its emergency lending. The one-time disclosure of its crisis lending emerged as a compromise.

Reporting by Pedro Nicolaci da Costa; Editing by Kenneth Barry

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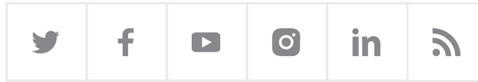

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