

Conversations with the St. Louis Fed

Friday, April 10, 2020

11:30 a.m. – 12:00 p.m. CT

Jim Fuchs:

Thank you, Dagma, and good morning to everybody. Thank you for joining us for our April 10 edition of the Conversations with the St. Louis Fed teleconference. I am Jim Fuchs, and I am happy to be with you again this week. We're looking forward to highlighting a number of topics today, responding to questions that we've heard from you throughout the week.

Before I turn the call over to Carl, just a quick recap from last week's call. So first up, we talked about collateral requirements of the discount window, we talked about signature requirements for loans used to collateralize discount window borrowings, we talked about the e-signature policy, also adding authorized borrowers, and we also heard from economist Bill Emmons, who gave us an update on how the economy was faring at that point in time; things are very, very dynamic right now, as you know. All Conversations calls are archived; we know our bankers are extremely busy navigating this crisis, serving their customers. So if you're joining us in real time, welcome.

If you have questions, please email us at conversations@stls.frb.org. We monitor that constantly through the week, through the weekend, and also during this call and we will do our best to get to your questions. But also, this session is archived and all sessions that we do through the Conversations program are archived, so if you heard something today or in a past session, you can go to supervisionoutreach.org, look for the Conversations program and you can hear all past sessions. Share them with your colleagues.

So we're going to jump right in, and I'm going to turn it over to our host, the head of Supervision at the Federal Reserve Bank of St. Louis, Carl White. Carl?

Carl White:

Thanks, Jim. And hello, everyone, again and thanks for joining us this week. So many of you, I'm sure, have had the opportunity to hear President Bullard speak before at one of our many banker events held either at the Fed or throughout the district. I will say, even during the crisis, he's continued to be very visible, even though we're all working from home. He's been vocal on his thoughts on the economy. One great resource—and I've mentioned this in prior calls—is our public website at stlouisfed.org, right there you can see his media interviews. We also have the On the Economy blog, which is available, which I've mentioned. So great resources. So today, obviously we're very honored to have President Bullard with us and hopefully he can share some comments for a few minutes. So, Jim, I'm going to turn it over to you.

Jim Bullard:

Okay. Thanks, Carl. Welcome to everyone on this call. I thought I'd just talk for a few minutes about where we are in this crisis and some of my thoughts on it. This is a big shock to the U.S. economy, but also to the global economy. But it's a shock that's very different from the ones you might have seen in the past in your career or reading about U.S. macroeconomic history.

In this case, we have a situation where we're sending workers home intentionally in order to invest in the nation's public health. So if people are being sent home, obviously, we're not going to produce very much during that period. And things like GDP are going to look very, very bad, especially for the second quarter. And we have to compensate those workers whose lives have been disrupted, and one way to compensate them is to use the existing unemployment insurance program—which I would call pandemic relief in this situation, I wouldn't call it necessarily unemployment insurance, but we need to be able to get money in the hands of these households that have been disrupted so they can continue to pay their bills.

So it's very different from times in the past when economic activity has declined. Usually, we don't know why it has declined. In most cases and in those situations, there's a lot more uncertainty, but here we know exactly what's going on. We're trying to get past the pandemic, and we're trying to get control of this virus. Now, I think the spirit of the times is to try to keep everyone whole in this situation, and the small business lending program through the Small Business Administration (SBA) is certainly part of that.

You guys have been in the thick of that, and we have some comments later in this call on what's going on there. We've also got these cash payments going on, and the St. Louis Fed has been active in helping the Treasury think about just, logistically speaking, how can we get the cash payments out to people. Those are about ready to go. I don't quite know if they're going today or very soon here, but they're about ready to go, at least the first wave of them. So, that is happening as well, so that should provide relief for people.

Some people in the media are still calling this stimulus. I would push back against that and urge you to push back against that. We're not really trying to increase the level of economic activity during the period when we told everybody to go home so that we could invest in national health and get control of the virus. We don't really want them to get back on the planes right now. We don't want them to go to the restaurants right now. We're telling them not to do those kinds of things, and that's why economic activity is going to be unprecedentedly low, and the unemployment rate, as conventionally measured, is going to be unprecedentedly high.

But, once we get control of the virus—and I think the indications on that are positive and Wall Street is getting optimistic about this, based on numbers out of Europe and to some extent numbers out of the U.S.—we'll get to a point where we have very few cases and very few fatalities in the U.S., and we'll be in a situation where we can reopen the economy.

Now when we reopen, I think all of you need to manage—starting right now—about how would we do that. We're going to have to do that in a situation where there is no vaccine, but you still want to get back to work. So you're going to have to take all kinds of precautions around the

office that you wouldn't normally want to take. It's going to be unpleasant, but that's what we're going to have to do to get back to work and to stop disrupting everybody's life here.

So just generally speaking across the economy, thinking is only just now starting about how that would occur and how you are going to be able to coax workers to come back into the workplace without fear that they're going to get infected and get sick, and especially, I think, with this virus, they're especially concerned maybe not so much for their own health, but that they'll carry the disease to someone else who is at high risk, and they would feel terrible if they have it. So, we're going to have to reopen but under constraints about how that is done and how we handle workplace issues and all kinds of things.

So I think you need to get mentally prepared starting now about how that's going to work. And I don't think the country is quite ready for that yet, but we're going to have to start thinking about it very rapidly here. The Fed also has initiated a lot of liquidity-type programs that are helpful in making sure that key markets are trading and not frozen up. That part, we think, has been successful so far. We're certainly willing to do more, but initially as the crisis hit, even U.S. Treasury market—the most liquid market in the whole world—was having liquidity problems and so we started purchases of Treasury securities more aggressively than we have been doing in the past, also mortgage-backed securities. But also many other types of financial instruments have been addressed through various programs that we have in mind, and I think the key message about those programs is that they're designed to make sure that there is price discovery and there is market functioning in these key markets.

I think what you don't want in this situation is that a person that wants to trade is unable to trade, because the market's completely shut down. You don't want that kind of situation; you want prices to be there, and you want the traders to be able to rearrange portfolios as appropriate given everything that's going on both in the U.S. and all around the world. So far, our liquidity measures are looking better across markets, and I think we're in better shape on that dimension than we were even ten days ago, and hopefully we'll be able to continue to address liquidity concerns in key markets.

I think I'm starting to be a little bit more bullish about what's going to happen here. I'd like to focus on the second quarter. I think the second quarter will be the quarter of maximum disruption. We did get some at the end of the first quarter, obviously, but the second quarter will be a different animal. You really have only essential services being produced, and the amount of goods that you can produce by working at home. I've maintained that that's probably less than 50% of the economy. So if you think that's going to continue all the way through the end of the first quarter, we'd be out about 50% of a quarter's output and therefore 50% of a quarter's income.

The U.S. economy produces north of \$5 trillion worth of goods and services in a quarter. So if the shutdown lasted the whole quarter, and we only produce at 50% then, that would be \$2.5 trillion so that's a big hit. That's a lot of income that doesn't go to various households all around the country, but I do think that there are a couple ways to handle that.

One is that this is just a quarter where we consume a lot less than we otherwise would. If income is down by half, we're probably also consuming much less than we normally would, partly because you can't consume because all the stores are closed and the restaurants are closed. You can't travel, so a lot of the things that we would do that would be on the high side of the consumption spectrum are not occurring. So that's one way to handle this, and that just means a lower standard of living during the second quarter. But then, also the fiscal response, I think, has been scaled appropriately.

It was the first—the most recent package was valued at \$2.3 trillion. So that's kind of the right number, at least the right ballpark for what I'm talking about for the second quarter. And so I've taken some heart from that, if we can figure out logistically how to get this money to the disrupted parties, we can keep everybody whole through this period. They can continue to pay their bills, and we can get back to work at some point, at the end of the second quarter or longer, depending on what kind of twists and turns the virus takes here.

So, I do feel like there is a way out, and I think we're taking all the right steps. I did like it that the Congress took dramatic action. I think the Fed's actions have also been dramatic and appropriate in the circumstance, and it is a different kind of a shock than what we've seen in the past. So there is light at the end of the tunnel because all viruses are temporary all through the history of mankind. So, this will go away at some point. And plus, you could probably get some breaks from the science on this, that is, developing all kinds of new therapies and tests and eventually a vaccine. So I think we have lots of ways to live with the virus up until the time we get the vaccine.

So it's a chaotic period. There's a lot going on. I appreciate all the work everyone's doing to try to get through this. I think the innovation across the economy is very important. You have businesses, banks, households all thinking about what kinds of things that they can do a little bit differently than they've done in the past in order to get work done and get income coming in the door. I think we'll see a lot more of that in the weeks ahead after the initial shock wears off and people start to better adjust their minds to the situation and get more focused on how we can recover and get back to normal.

So I'm going to stop talking there but, again, I appreciate you joining us on this call today, and we have some other comments before we get to questions, so thanks very much.

Carl White:

So, Jim, I will jump in and ask you a quick question. One thing when you mentioned returning to normalcy, one thing you've been vocal on is universal testing. Maybe share some comments and thoughts on that.

Jim Bullard:

Yeah, I was kind of alluding to the idea that we left our workplaces—at least at the Fed here I guess we're going on four weeks here—so we left our workplaces and we will go back, but when we go back we're going back without a vaccine. So you're going to go back to the workplace,

but people are scared to death. There's a shark in the water, and they don't want to get bit by the shark, so you have to somehow reassure people that you're creating a safe workplace. So there are lots of ideas floating around about how to do that.

Now, if we could test everybody in the whole economy on a regular basis, then we would know exactly who's sick and who isn't, and we could allow the healthy people to go to work. What we're doing right now is crazy inefficient. You've got all these healthy people who are sitting at home in their houses just because some people are sick. You've got all these healthy people that could be working but are sitting at home. So if you knew who was sick and who wasn't and you had everybody tested, and may have results on your phone or something like that, you could go back to work with confidence, you could go to stores with confidence, you could interact with people with confidence because you would know who was sick and who wasn't.

Now we do have a 15-minute test that Abbott Labs put forward, so the technology is there today and is being deployed today, but can we deploy it at a scale of 150 or 160 million workers? I think that's a good question. Other kinds of things that you can do: You can take people's temperature before they go into a building. You can say everyone's got to wear a mask—all these kinds of unpleasant things that you wouldn't do in a normal circumstance, but you're probably going to have to do here in order to prevent reinfection, which will be the key issue as the first wave of the pandemic goes past.

So, I think it can be done; there's no reason it can't be done. A good analogy is 9/11. After 9/11 we were very concerned about another terrorist attack, and we put a lot of restrictions and much heavier security all around the country in various ways. We created a whole new Department of Homeland Security, and that created some disruptions in our lives because we were more concerned about security than before. And I think something similar is going to happen here in order to get the economy reopened. You have to think about how to cope with the virus in an environment before you get the vaccine, and you're going to have to do a lot of things that you'd rather not do but that you're going to have to do in this environment that make it a little bit different. So I think it's going to be very tricky, but I think it all can be done, and it's a lot cheaper to do those things than it is to just have everybody sit at home. That's a very blunt and very costly way to try to control the virus. We've gotten into that because we got kind of taken by surprise by the virus. But I don't think that's the long-term approach to how to deal with the virus before the vaccine.

Carl White:

Great. Well, thanks, Jim, for spending some time with us. I will tell you that we checked the registration for this call, and this is a record number of folks on this program, and I think that's directly tied to the fact that you were going to join us today. So thank you so much. So we are going move on to cover some specific topics that we're kind of tracking as we speak, so I'm going to turn it over to Jim Fuchs, and he's going to talk a little bit about some of the programs that are going on that specifically tie to the discount window.

Jim Fuchs:

Great, Carl, thank you very much. And again, thanks to President Bullard for joining us on today's conversation and also to all of you. You may have seen—and you probably have a number of questions at this point—an announcement that came out from the Federal Reserve yesterday, April 9, right at 7:30 a.m. Central, announcing a series of new facilities.

I'm going to focus on one of those facilities today because I think it's probably the most pressing and you probably have the biggest questions around it, and that is the Paycheck Protection Program Lending Facility or the PPPLF. So, again, the idea was—and I would think of this as it's through the discount window, but it's with some much different parameters. So I'll quickly go through that; I know you're going to have a lot of questions. So let me also just say that Ask the Fed[®], which is our national program—which if you're a bank in this district, and that's who I know the participants are on this call, I know you were very much aware of Ask the Fed[®].

We did a double session knowing there's going to be a lot of demand today. So one just happened at 10:00 a.m. As you know, those sessions are archived and you can find it on our website, but also, we will be doing another one at 2:00 p.m. Central this afternoon, so identical session. So if you're not able to get to that first one, there is still time to register, so please do that, that's askthefed.org and you'll hear directly from folks at the Board, Board legal, and in the discount window community talking about this program. There's still a few unknowns, and I will address those as well.

So first off, that's a great source of information, we can even put a link to Ask the Fed, even on our Conversations website. I do want to say that contrary to some early news reports on the facility that came out, I believe on Wednesday—so a day before—the Federal Reserve is not buying outright Paycheck Protection Program loans, nor is it lending directly to small businesses through this program. So I just want to set that out there, right? So these are loans basically at the discount window, backed by Paycheck Protection Program loans. The Paycheck Protection Program loans that banks got from the SBA, those serve as collateral; collateral is valued at the principal valuation of the underlying PPP loan. There are no fees associated, and the rate is 35 basis points right now.

I know there are some capital questions, so Paycheck Protection Program Lending Facility loans have a risk weight of zero and, as of now—and it's effective immediately—collateral is excluded from a number of calculations, overall banks' total leverage exposure, average total consolidated assets, and calculation for advanced approaches, risk-weighted assets. I know that's not a common calculation for banks in our district, but also from banks adopting standard approach for calculating risk-weighted assets. And also, based on this treatment, these should also be excluded from your Federal Deposit Insurance Corporation (FDIC) insurance premium calculations.

So, put that out there. There is a process to this, so even if you are a borrower with documents on file, you will still be required in addition to your traditional discount window lending documents on file, you will be required to fill out a letter of agreement for the program. That letter is still forthcoming; we've received a lot of questions on that, so it's going to be posted on the discount window website, which we will put in our resources for the Conversations program. Check that frequently, but we will also get some information out next week once we know these documents are posted and reminding you of some ways to contact us. Also, you'll have to sign a

certification agreement, which is required to use an emergency lending facility under Section 13.3. Again, that specific certification agreement has not been finalized. We are expecting something early next week.

So again, those are two major pieces of documentation that will be required, and we will do our best to let you know when those are uploaded. For those institutions—insured depository institutions—that are interested in using/accessing this facility but do not have borrowing documents on file for discount window usage, you are not excluded from this, and you don't necessarily have to go through the full process as you normally would. When beginning a borrowing relationship of the discount window, you would of course need to sign the letter of agreement, the certification agreement. In addition, you would need a board resolution. So there's one extra step, and again, these documents in these steps will be a little more prominent once we get a little more information.

So I know—again, not to take all the time on this call—questions, and I would recommend maybe holding those till next week, please call our toll free number. And this is an 8th District toll free number, not a national toll free number, so I don't want you to think you're going to get in some national queue; we've heard some frustrations with some other programs out there. Our number is 866-666-8316. That is something that we operate locally; we've got a call tree here and it's designed to be responsive to your questions. There's also a unique email address, PPPcredit@stls.frb.org, which is also unique to this program.

So again, I went through a number of features of the program. I'm sure you have a lot of questions. Documentation is going to be key at this point, and some of those key documents are still forthcoming. Again, we will make sure that you have ready access to that toll free number. I did want to tell you in addition to just having our normal processes, we have staffed up to handle an expected increase in calls. But I will tell you, if you want to get a jump on this, if you are a Paycheck Protection Program—if you use that program through the SBA and are ready to start the process for this new lending facility, the documentation is just not available yet. We will alert you through some of our channels as soon as we know it's available.

So again, and if you have questions, obviously use the conversations@stls.frb.org. That's one of many tools to get in touch with us. But you know we'll continue to provide some information to you, and we'll also provide a link in the resources section to the April 9 announcement. There's one that announces the program, and then there's another one that highlights the interim final rule that outlines the treatment of these loans, the collateral in relation to your leverage exposure, and other calculations. So those are both out there. So, Carl, with that, let me turn it back to you.

Carl White:

Thanks, Jim. So, Allen, is there anything we need to cover? I know we only have a few more minutes, but anything you wanted to cover from the Supervision perspective?

Allen North:

No, I don't think so, other than to say hello, everybody. I've heard from many of you over the last week or so about the PPP program and just a couple of real quick points I'll share with the group. According the National Association of Government Guaranteed Lenders, about \$125 billion has already been approved, and I know many of you understand some of the issues that we're facing. I heard Mr. Bullard say—I've certainly heard you say it, Carl—that given the amount of time that the SBA has had to stand up this program, it's not surprising that there's been some snafus and some things that haven't worked according to plan. But I guess what I'll leave the group with—if you have any questions at all, I know all of you, and please feel free to give me a call and I'll be glad to try to address your questions.

Carl White:

Great. Thanks, Allen. Well thanks, everybody, for joining us today. That's all I had. Jim, if you want to wrap us up, we'll conclude today's call.

Jim Fuchs:

Great. Thanks again. Thanks again, Carl. Special thanks to President Bullard for joining us today and Allen as well. We are going to keep these Friday calls going throughout this pandemic and even beyond, so please give us your feedback. Even if you don't have a question, please—conversations@stls.frb.org, as I mentioned the top of the call, we're monitoring that constantly. We'd like your feedback of what would you like more of on these calls.

Again, we're committed to keeping them to a half hour because we know you have a lot of things going on, but at the same time, we want to make sure we have a vehicle to update you on the economy, on supervisory issues, clearly on discount window matters, and a whole host of other tools and programs as we learn about them during this crisis.

So this call, like all Conversations calls, is archived on our site. We should have that audio file up later today. So again, go to supervisionoutreach.org. You'll see the Conversations tab, and you'll be able to download the audio from this and all those other resources that were mentioned the during this call, including links to the On the Economy blog and other items from President Bullard and also some of the releases and information that we mentioned.

So again, we will talk to you next Friday. Appreciate your participation today, appreciate your ongoing engagement. Please send us your questions but also your comments on the program, and we look forward to speaking with everybody next week. Thank you and have an enjoyable weekend. Take care.