

FEDERAL RESERVE BANK of NEW YORK *Serving the Second District and the Nation*

New York Fed 101: Term Asset-Backed Securities Loan Facility (TALF)

The Term Asset-Backed Securities Loan Facility (TALF) began lending in March 2009 to help restore credit to millions of Americans during the financial crisis. Restoring the flow of credit to consumers and small businesses helped to support overall growth throughout the U.S. economy.

TALF helped restore credit to consumers and small businesses by providing financing to investors willing to invest in securitizations backed by small business and consumer credit including student loans, small business loans and auto loans in the asset-backed securities (ABS) market.¹ (Securitization and the ABS market are explained in detail below.)

Providing financing under TALF to investors was essential because many lenders financed new loans to consumers and small businesses by bundling loans into securities that were then sold to investors.

During the financial crisis, many investors that had traditionally invested in the ABS market stopped investing in ABS. Without investors to buy consumer and small business loans, many lenders stopped making loans to consumers and small businesses altogether.

TALF loans were available to any U.S. company not controlled by a foreign government, but could only be used for the purpose of investing in ABS.

Investors who received TALF loans to invest in ABS had to keep the "first loss" position—meaning that if the underlying loans performed badly, the TALF investors would lose their entire investment before the Federal Reserve, the U.S. Treasury or the taxpayer suffered any losses.

A wide range of investors participated, including mutual funds, pension funds, insurance companies, investment funds and hedge funds, and others.

TALF worked. It helped revive the ABS market. As investor demand for ABS increased, lenders started making new loans again, which helped to restore the flow of credit to qualified consumers and small businesses.

TALF could not ensure that every American who wanted credit could get it: in hard times, many still struggled to qualify for loans. But at a time when millions of Americans needed credit, TALF supported 3 million auto loans, 1 million student loans, nearly 900,000 small business loans, 150,000 other business loans and millions of credit card loans.

The New York Fed, which operates the program, has taken great care to manage the risks associated with TALF loans and, as of May 2011, there has not been a single dollar of loss under the program. Furthermore, as of May 2011, TALF has earned \$1.2 billion in interest income for the U.S. taxpayer. Any profit from TALF—as with all other Fed programs—is remitted to the U.S. Treasury for the benefit of the taxpayer.

The questions and answers below explain TALF in more detail.

What is TALF?

TALF, authorized by the Federal Reserve Board under section 13(3) of the Federal Reserve Act, was a program set up by the Federal Reserve with the support of the U.S. Treasury. The program was part of a multi-faceted approach taken by the Federal Reserve, along with the U.S. Treasury, to help avert what could have been a much longer and deeper recession.

TALF, managed by the New York Fed, made loans available from March 2009 until June 2010 to eligible investors for the purpose of investing in ABS.

The size of TALF's portfolio of loans continues to decline.

Why was TALF created?

TALF was designed to support the economy by encouraging lending to consumers and small businesses by restarting ABS markets that were virtually frozen by the financial crisis starting in late 2008. TALF provided financing to eligible investors for the purpose of investing in ABS.

What did TALF achieve?

At a time when millions of Americans needed credit, TALF supported nearly 3 million auto loans, more than 1 million student loans, nearly 900,000 loans to small businesses and about 150,000 other business loans.

How did TALF help?

TALF helped by getting the ABS market to function again. At a time when the ABS market was virtually frozen, TALF provided financing to eligible investors for the purpose of investing in ABS.

As investor demand for ABS increased, lenders started making new loans again. As the ABS market continued to improve over time, more investors started to return to the ABS market, which increased the demand for ABS. As demand rose, prices began to recover, attracting even more investors back to the market. This positive loop helped to restore the flow of credit to qualified consumers and small businesses, thereby reducing the reliance on TALF. TALF loans were available from March 2009 until June 2010; the last loan was made in March 2010 and the size of TALF's portfolio of loans continues to decline.

What is securitization and how does it work?

Securitization is the process by which loans are turned into securities called asset-backed securities, or ABS. ABS are bonds backed by pools of

Beth Caviness of the New York Fed explains how TALF helped restart the flow of credit to American households and small businesses.



In order to make loans, lenders need cash. To get that cash, lenders—such as auto finance companies—bundle together the loans they make to consumers and small businesses. The lenders sell bonds backed by the cash flows from the bundle of loans to investors. The money that investors pay to the lenders for the bonds provides the cash that the lenders need to make new loans. Securitization began in the mid-1980s.

Why did securitization virtually stop working during the financial crisis?

Beginning in mid-2007, the number of consumers and small businesses experiencing financial difficulty started to rise. As some of these consumers and businesses could not make loan payments, the number of loan defaults started to rise. Investors, along with the lenders who provided loans to these consumers and small businesses, started to fear that more defaults were coming, which in turn could result in losses on their ABS investments. As a result, investors either could not or did not want to continue buying ABS. This decline in demand for ABS caused the interest rates paid to investors to rise dramatically.

In short, fewer investors were left to buy ABS—and many of the investors who remained kept to the sidelines. Without anyone to buy their consumer and small business loans, many lenders were not willing to approve any new loans. As a result, consumers and small businesses ended up having a hard time getting loans to buy a car, to pay for school, use a credit card or run a small business and so on. In addition, lenders had started charging higher interest rates for the few loans they were making to consumers and small businesses. The securitization process had virtually stopped.

How much did the Fed lend?

While \$200 billion was authorized under the program, the Fed lent a total of \$71.1 billion but never had more than \$49 billion outstanding at any one time. As of May 2011, only \$14.2 billion of the \$71.1 billion in loans made remains outstanding.

Did TALF cost taxpayers any money?

No. As of May 2011, there has not been a single credit loss.

Also as of May 2011, TALF loans have earned \$1.2 billion in interest income for the U.S. taxpayer. This interest income and any additional profit earned from TALF—as with all Federal Reserve programs—is remitted to the U.S. Treasury for the benefit of the taxpayer.

Who participated in TALF?

TALF was open to any U.S. company not controlled by a foreign government. This allowed the Fed to reach the widest set of investors possible. Investors of all kinds participated, including mutual funds, pension funds, insurance companies, investment funds and hedge funds.

What did borrowers gain by participating in TALF?

To receive a TALF loan, investors had to buy an ABS and pledge it as collateral against the requested TALF loan. By buying an ABS, the investor stood to gain from any interest earned on the ABS and any potential capital gains (if the investor's selling price was higher than the original purchase price).

Who did TALF benefit?

The investors who participated in TALF, including mutual funds, pension funds, insurance companies, investment funds and hedge funds—did benefit from their investment. However, the ultimate beneficiaries were the American consumers and small businesses.

The program succeeded in helping to restart the securitization market and restore the flow of credit so qualified consumers and small businesses could get a loan to buy a car, pay for school, use a credit card or fund a small business. TALF supported nearly 3 million auto loans, more than 1 million student loans, nearly 900,000 loans to small business and about 150,000 other business loans.

About the Facility

List of TALF borrowers and investors [OFFSITE](#) [EXCEL](#)

How investors accessed TALF

Terms and conditions

Program documentation

FAQs

2010 audited TALF financial data

Why didn't the Fed lend directly to the consumers?

Restarting the ABS market was the quickest way to get credit to consumers and small businesses flowing again: the Fed lacked the operational infrastructure to lend directly to consumers, and it would have taken a long time to create this infrastructure from scratch. Further, by restarting the ABS market, TALF helped enable lenders to start making new loans.

TALF was available to a wide set of market participants beyond the Federal Reserve's traditional bank counterparties. This feature reflected the program's broad focus on a financial market rather than a particular set of financial firms. Given the wide range of market participants, the program's broad reach was necessary to effectively support the entire market.

THE DETAILS

Did the Fed guarantee profits on TALF loans?

No. Investors bought ABS with their own capital and at their own risk. The Fed gave no guarantees on the performance of the ABS.

The objective of TALF was to help restart the ABS market, which had virtually frozen during the financial crisis. If the program succeeded in meeting its objective, which it did, then ABS values might rise and investors could see gains in their ABS investments. So we acknowledge that profits have been made by TALF investors in exchange for the risks they took in buying ABS at a time when this market had virtually stopped operating.

If the ABS performed badly, the investors would lose their entire investment before the Federal Reserve, the U.S. Treasury or the taxpayer suffered any losses. There was also a risk that the ABS purchased by the investor or the investor itself might not be deemed eligible for TALF funding given the stringent program requirements.



TALF's design helped minimize risk exposure. TALF accepted only high-quality ABS. During the course of the program, the New York Fed used credit ratings and performed its own independent credit review of ABS. In addition, the market value of the ABS pledged by the investor exceeded the amount of the TALF loan received. This difference, called the 'haircut,' provided further protection.

How did the Fed set the loan rates?

The Fed set the loan rates lower than rates prevailing during the crisis, but above rates that would be found during normal market conditions. In setting these rates, TALF offered rates that were sufficient to attract investors back to a market that had come to a virtual halt. But as the markets have recovered, investors have found the TALF loan rates to be expensive, which has provided an incentive for TALF borrowers to start prepaying their loans before the respective TALF loan maturity date. The Fed lent a total of \$71.1 billion, but never had more than \$49 billion outstanding at any one time. As of May 2011, only \$14.2 billion of the \$71.1 billion in loans extended remains outstanding.

The Fed did not lend 100 cents on the dollar. It set 'haircuts' by asset class. These haircuts—reductions in the value of the ABS being pledged as collateral—were greater for longer-term ABS. Because of this risk-based haircut, the market value of the ABS pledged exceeded the amount of the TALF loan. This helped protect the Fed, the U.S. Treasury and the taxpayer from potential losses. As of May 2011, there has not been a single credit loss.

What loan terms were available?

Initially, eligible investors could only receive three-year loans. Later, the Fed also made five-year loans available for select asset classes.

Related Links from the Board of Governors

Congressional testimony on TALF by William R. Nelson, Board of Governors of the Federal Reserve System

TALF data disclosure related to Wall Street Reform and Consumer Protection Act of 2010

Federal Reserve Act: Section 13 Powers of Federal Reserve Banks

List of TALF borrowers and investors [OFFSITE](#) [EXCEL](#)

Is the securitization market functioning now?

Yes. TALF-eligible ABS comprised the majority of new ABS issuance in 2009, but the private-sector investors took the lead in 2010. TALF deals accounted for roughly \$100 billion of issuance in 2009 and more than \$10 billion in 2010. Deals that were not TALF-eligible accounted for roughly \$45 billion in 2009 and more than \$60 billion in 2010. As of the first quarter of 2011, more than \$40 billion of new ABS have come to market.

*TALF also provided financing for the purchase of newly issued and existing (legacy) commercial mortgage-backed securities, or CMBS. However, for simplicity, New York Fed 101 will focus on consumer and small business loans.

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