The Next Phase of Government Financial Stabilization and Rehabilitation Policies

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THE NEXT PHASE OF GOVERNMENT FINANCIAL STABILIZATION AND REHABILITATION POLICIES

Executive Summary

In late 2008 and early 2009, our financial system was in the midst of one of the most severe financial crises of the past century, and was in danger of even further deterioration or collapse. The initial actions taken by the Federal Reserve and the U.S. Government at the onset of the financial crisis and the comprehensive, forceful and sustained commitment to fiscal stimulus and financial stability made under the Obama administration represented the first stage of our policy response. Now, in part as a result of these actions, we are entering the next phase of our efforts: moving from rescue of our financial system to a period of stabilization, rehabilitation, and rebuilding.

This next phase will focus on winding down those programs that were once necessary to prevent systemic failure. The use of those programs, by design, continues to decline as the financial system recovers, and the U.S. Government is being repaid for its investments. But this phase will also involve ensuring that those policies and programs that are still necessary for financial and economic recovery are maintained and well executed, making clear that the U.S. Government still stands ready to do whatever is needed to ensure a lasting recovery.

As we focus on the future and move further away from acute crisis, we must not forget the lessons we have learned from this period. Rebuilding our regulatory system in a way that is stronger and better-suited to manage risk and ensure safety and soundness must be our highest priority.

The next phase will have four key elements:

1. Exiting from Some Emergency Programs as Financial Conditions Normalize

As the risk of catastrophic failure of the financial system has receded, the need for some of the emergency programs put in place in during the most acute phase of the crisis has receded as well.

In early 2009, the financial system was still very fragile. In that context, the Obama Administration included a $250 billion “placeholder” in the President’s Budget to support an additional $750 billion in total expenditures to stabilize financial markets if necessary. Following the successful conclusion of the “stress test” for the country’s largest financial institutions, the resulting ability of banks to raise private capital, and growing signs of financial stabilization, this placeholder was removed from the Budget in the August Midsession Review.

At the height of the crisis last fall, Treasury established the Money Market Mutual Fund Guarantee Program to prevent a run on money market mutual funds in the wake of the failure of Lehman Brothers and the well-publicized troubles of several large funds. This program – which currently provides protection for about $2.5 trillion in investments – will expire on

September 18. Due to improved market confidence, Treasury has determined that it does not need to establish a successor program. Since inception, Treasury has had no losses under this program. In fact, it has earned the U.S. Government $1.2 billion in fees.

In October 2008, the Federal Deposit Insurance Corporation (FDIC) established the Temporary Liquidity Guarantee Program (TLGP) to stabilize the financial system and to facilitate bank lending. Through the TLGP, the FDIC provides a guarantee on both transaction accounts and newly-issued senior debt issued by banks. The last day to issue new debt under the Debt Guarantee Program of the TLGP is currently October 31, 2009. Due to market improvements, the FDIC anticipates that this program will not need to be extended. However, the FDIC recently announced that it is considering establishing an emergency facility for up to six months that could allow current participants in the Debt Guarantee Program to issue additional guaranteed-debt under limited circumstances at substantially higher fees.

2. Diminishing Reliance on Federal Support

Utilization of most of the financial support programs put in place over the last few years has been declining in recent months as financial markets have recovered. To a significant degree, this decrease in utilization reflects the fact that these programs were designed with terms that make them increasingly unattractive as financial conditions normalize.

For example, monthly issuance of TLGP guaranteed debt has fallen from a peak of $113 billion in December to $5 billion in August. And assets covered by Treasury's Money Market Mutual Fund Guarantee Program have fallen by approximately $750 billion since December.

Credit extended under Federal Reserve programs that provide liquidity to banks and non-bank financial institutions has also declined significantly as market conditions have improved. For example, as the Federal Reserve explains in its monthly report[1]:

- Credit provided to depository institutions through the discount window and the Term Auction Facility has fallen from peak of $560 billion to $251 billion.
- Borrowing at the Term Securities Lending Facility has stopped as a result of further improvement in the conditions in money markets. There has been no borrowing at the Primary Dealer Credit Facility since mid-May.
- The amount of commercial paper held in the Commercial Paper Funding Facility has fallen from peak of $351 billion to $48 billion, as improvements in market conditions have allowed some borrowers to obtain financing from private investors in the commercial paper market or from other sources.

[1] See *Federal Reserve System Monthly Report on Credit and Liquidity Programs and the Balance Sheet*, which is available at www.federalreserve.gov/monetarypolicy/bst.htm.

- Dollar credit extended to foreign central banks under liquidity swaps to facilitate their efforts to address pressures in dollar funding markets has dropped from a peak of about $580 billion to $63 billion as global financial conditions have improved and short-term funding pressures have receded.

3. From Infusing Capital to Repaying Capital

From September through January, Treasury provided $239 billion to support banks. Since January, Treasury has invested $11 billion through its Capital Purchase Program in more than 350 financial institutions, a large number of which have been small community banks.

Today, banks have repaid more than $70 billion of these capital investments. The conclusion of the "stress test" for the largest banks provided the backdrop for those institutions to raise over $80 billion in high-quality capital, without additional government infusions. We expect banks to repay another $50 billion over the next 12 to 18 months. For the 23 institutions in which Treasury's Capital Purchase Program investments have been fully repaid, Treasury has earned an annualized average return of roughly 17 percent.

4. Ongoing Role for Policy

While meaningful progress has been made in rehabilitating the financial system, the normalization of financial markets achieved to date is partial and fragile, and the economic recovery is, at best, in its very early stages. To create conditions for financial stability and sustainable economic growth, we must implement comprehensive regulatory reforms. In addition, there is still a substantial need to continue some of the extraordinary policies put in place over the course of the financial crisis.

Programs that continue to provide essential support to key channels of credit for households and businesses should be sustained. The housing market is still under pressure and the Administration's Home Affordable Modification Program is just ramping up. Similarly, the issuance of new debt instruments backed by new consumer loans, so-called asset back securities, has recovered with the support of the Term Asset-Backed Securities Loan Facility (TALF). This is a critical channel for supply of new credit to households.

In addition, programs that are still making a material contribution to confidence in financial markets should also be sustained. Even if utilization of a program is low, its existence alone can help stabilize markets to the extent that market participants know it is available if conditions worsen.

Although we are rolling back emergency support programs that are no longer needed, significant parts of the financial system remain impaired. Unanticipated events could intensify pressure on the financial system. In this context, it is prudent to maintain capacity to address unforeseen developments. By bolstering confidence, having such capacity may actually reduce the need to use it.

I. Introduction

At the beginning of the year, the incoming Obama Administration faced a combination of acute economic and financial challenges. The viability of many major financial institutions remained in doubt, vital aspects of the financial system were deeply impaired, and the economy was deteriorating rapidly. President-Elect Obama made the key decision to make major commitments to both fiscal stimulus and financial stability. The Financial Stability Plan announced in February laid out the Administration's comprehensive, forceful and sustained commitment to ensure the stability of the financial system, assist in the cleanup of legacy assets, jumpstart the provision of new credit for households and businesses, and support distressed housing markets. That plan, in conjunction with fiscal stimulus, has helped to stabilize financial markets and the nation's economy, and to pull the financial system back from the brink of systemic collapse.

We are now moving into a new phase of our strategy to stabilize and rehabilitate financial markets. Utilization of the extraordinary government programs put in place to contain the financial crisis has already declined substantially. Most of these programs were designed to become unattractive once financial markets normalized. Going forward, when programs are no longer needed they should end. To that end, the President has removed the $250 billion "placeholder" for contingent future stabilization efforts in financial markets from his proposed budget, and later this month Treasury's $2.5 trillion guarantee program for money market mutual funds will end.[2] These developments are tangible evidence of our commitment to eliminate as soon as practicable the government's extraordinary involvement in the financial sector.

But the process of terminating crisis-related programs must be done in a measured way that does not derail the nascent economic recovery. Unemployment remains elevated, output has fallen significantly, foreclosures continue to rise, and credit to households and businesses remains constrained. We must continue to provide support where it is still needed to rehabilitate disrupted markets that provide critical credit to households and businesses. It would be a mistake to withdraw abruptly from programs supporting these channels for new credit before a self-sustaining economic recovery has taken hold.

History suggests that exiting too soon from policies designed to contain a financial crisis can significantly prolong an economic downturn. Thus, it would also be a mistake to eliminate prematurely our capacity to address potential future market disruptions. Credit losses in some parts of the system are still increasing and bank failures, which tend to lag economic cycles,

[2] The placeholder was expected to provide $750 billion of additional resources, but it was "scored" as $250 billion. Scoring reflects the expected cost of a budgeted item to the government. Because the vast majority of Treasury's extraordinary financial commitments have been structured as investments, we expect to be repaid a substantial amount, and we are receiving income from outstanding investments. Thus, the credit score for the funds committed under TARP is much lower than the total allocated amount.

are still on the rise. These conditions create an environment in which new shocks can still have outsized effects. We must therefore maintain for some time our capacity to respond if financial conditions worsen. Such flexibility provides the vital insurance for stability.

While we must not waver in our resolve to ensure the stability of the financial system and to support the nascent recovery that the Administration and Congress have worked so hard to achieve, we also must address the structural weaknesses in our financial system that this crisis revealed. That requires a significant overhaul of our financial regulatory system. The Administration has put forward specific proposals for such reform, which should reduce the risk of another episode of financial upheaval.

II. Extraordinary Financial Policy Initiatives and the Status of the Recovery

A. Background to the Crisis

The severity of the recent financial crisis reflected long-term structural changes that had made the financial system significantly more fragile. Financial intermediation and risk taking grew rapidly in the relatively stable economic environment that preceded the crisis, while rising asset prices hid weak underwriting standards and masked growing leverage throughout the system. Further, financial innovation, driven in part by rapid improvements in information technology, outpaced risk management systems as securitization allowed for more credit to rely on securities markets. This financial innovation made the system both more interconnected and opaque. Our regulatory system was ill-prepared to handle the rapid growth of complex financial activity. In addition, unregulated markets and structures provided an increasing share of short-term credit to fund long-term assets. Such gaps and weaknesses in the supervision and regulation of financial firms presented challenges to the government's ability to monitor, prevent, or address risks as they built up in the financial system.

Starting in 2007, unanticipated mortgage-related losses weakened the balance sheets of major institutions, thereby reducing their capacity to provide credit and liquidity support to the economy and the rest of the financial system. Given the interconnections throughout the system, problems at individual institutions severely compromised confidence in the system as a whole, both in the United States and abroad. These pressures became acute one year ago, as evidenced by the need to put Fannie Mae and Freddie Mac into conservatorship, the failure of Lehman Brothers, and significant problems at American International Group (AIG).

B. Containing the Panic

In the days and weeks following the Lehman bankruptcy, the Bush Administration, in conjunction with the Congress, the Federal Reserve, and the Federal Deposit Insurance Corporation (FDIC), made substantial commitments to shore up confidence in the financial system. The Federal Reserve, with Treasury's support, stepped in to support AIG. Treasury

implemented a guarantee for money market mutual funds. The Bush Administration asked Congress to establish the Troubled Asset Relief Program (TARP). Under TARP, Treasury established the Capital Purchase Program (CPP) and injected capital into nine large financial institutions initially, and hundreds of other banking organizations subsequently. The FDIC established the Temporary Liquidity Guarantee Program (TLGP) to provide guarantees for new medium-term bank debt and non-interest bearing transaction accounts (typically used by businesses). FDIC deposit insurance was also increased to $250,000 per account. The Federal Reserve reduced interest rates further and took a range of actions that dramatically expanded its liquidity support for the banking system, money market mutual funds, commercial paper issuers, and securitization markets. Treasury agreed to extend short-term loans to General Motors and Chrysler. Collectively, the actions taken between September and December 2008 averted catastrophic failure, although they significantly increased the government's commitment to the financial system.

C. Policy under the Obama Administration and the Response in Financial Markets

The incoming Obama Administration faced a very difficult set of economic challenges. The economy was contracting sharply in response to the severe tightening of financial conditions. While the emergency actions taken at the end of 2008 had averted catastrophic failure, the financial system remained extremely fragile. Significant doubts persisted about the viability of major financial institutions, owing in part to unresolved questions about the quality of "legacy" assets still on their books. The unfolding recession added new concerns about potential credit losses on more conventional consumer and commercial real estate loans. Forecasts signaled continued deterioration in home prices and accelerating foreclosures. Moreover, key channels supporting credit flows to consumers and businesses were effectively shut down (see Appendix A[3], Figure 19).

President-Elect Obama made the critical decision to make major commitments to renew and expand the government's commitment to financial stability, and to push for a major fiscal stimulus package. The two initiatives were linked. One could not succeed without the other.

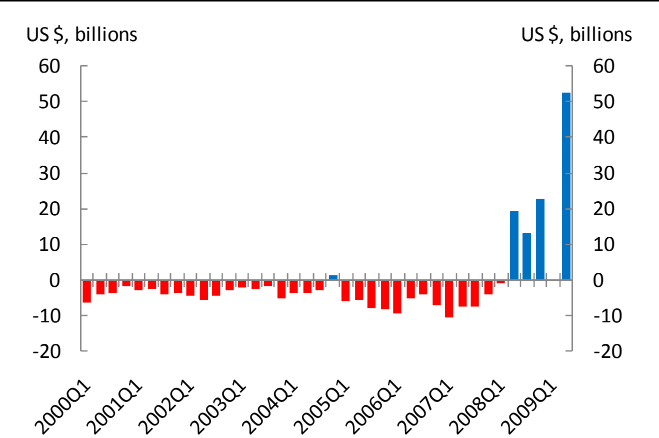
The Administration's financial policies were designed to achieve four broad objectives. First, the Administration made an unequivocal commitment to ensure that the financial system continued its core functions in support of the broader economy without interruption. Second, the Administration sought to ensure that the financial system had enough capital to provide new credit to the economy by reducing uncertainty and mobilizing private sources of new capital for financial institutions. Third, the Administration sought to restart key non-bank channels of credit intermediation that had been effectively shut down by the crisis. Finally, the Administration sought to moderate the impact of the adjustment in the real estate sector on

[3] Appendix A contains Figures 9-33, which illustrate conditions in various financial markets.

households by making new mortgage credit more available and by reducing the number of unnecessary foreclosures. The Financial Stability Plan (FSP) announced in February laid out the Administration's comprehensive, forceful, and sustained strategy to meet these objectives.

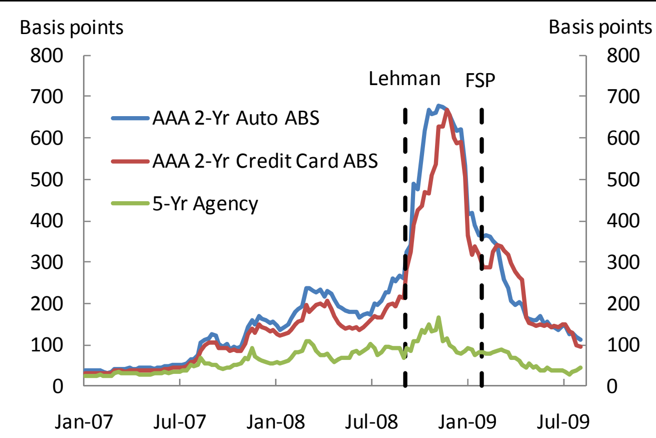
Major U.S. banking organizations were subjected to a "stress test" of their medium-term prospects under an adverse economic scenario under the Supervisory Capital Assessment Program (SCAP). These institutions did not welcome the exercise. While markets were initially skeptical, an unprecedented level of transparency in this supervisory exercise contributed to the program's credibility and, combined with the government's commitment to provide a capital backstop if needed through the Capital Assistance Program, furnished needed confidence in the financial sector. In the wake of the stress test, major banks were able to raise substantial amounts of new private capital very quickly (see Figure 1).

Figure 1: Private Capital Raising by Banks: Net Bank Common Issuance (US $, billions)



Source: SNL Financial.
Notes: Excludes equity generated through asset sales and preferred conversions. Negative figures represent net repurchases of equity.

Figure 2: Credit Spreads for Key Markets: Spreads for Agency Debt and Asset-Backed Securities (basis points)



Source: Bloomberg.

The FSP also committed resources to rehabilitate key channels of credit to households and businesses. The FSP dramatically expanded the scale and scope of the Term Asset-Backed Securities Loan Facility (TALF). Announcements about TALF helped narrow spreads even before the program began operating (see Figure 2), and issuance of consumer-related and other asset-backed securities (ABS) has improved substantially since the launch of the program.

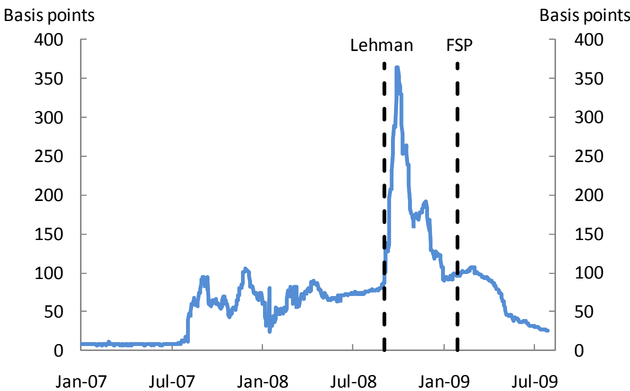
The FSP also proposed the creation of a Public-Private Investment Program (PPIP) for legacy loans and securities. The objectives of this program were both to re-liquefy key markets for financial assets and to help to clean up the balance sheets of major financial institutions. The program for legacy securities has recently been launched, although not in the scale and scope that was originally anticipated, as market conditions and confidence have improved. Nonetheless, program announcements have had a notable impact on securities prices (see

Appendix A, Figure 12). The government's willingness to commit resources to this area likely contributed to improvements in these markets, even with the more limited program.

In addition, the Administration created a broad program to stabilize the housing market by helping to drive down mortgage rates and making it easier for millions of families to refinance their mortgages and avoid foreclosure. Treasury continues to provide capital support to the Government Sponsored Enterprises (GSEs) Freddie Mac and Fannie Mae, and to buy the mortgage-backed securities guaranteed by these institutions. These initiatives, along with complementary policies implemented by the Federal Reserve, have helped to narrow GSE spreads and hold down mortgages rates (see Appendix A, Figures 25-26). The Obama Administration has also put in place the Making Home Affordable Program to support homeowners through refinancing and loan modifications. The refinancing portion of the program provides the opportunity for up to 4-5 million homeowners who took out loans owned or guaranteed by Freddie Mac and Fannie Mae to refinance through the two institutions over time. The modification portion of the program assists homeowners struggling to make their monthly mortgage payments, perhaps because their interest rate has increased or they have less income. The modification portion of the program is on track to meet its objective of helping 3-4 million homeowners over its lifetime.

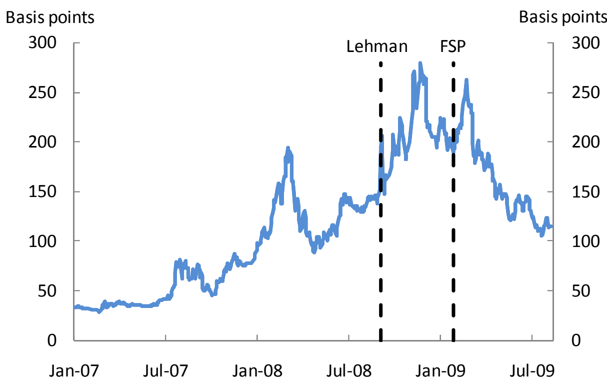
One year since the panic in September 2008 and six months since the launch of the FSP, financial markets are much more stable. Overall measures of systemic financial stress (e.g., interbank lending spreads and credit default swap spreads) have declined substantially from their peaks and in some cases have returned to levels associated with stable conditions (see Figures 3 and 4; see also Appendix A, Figures 9-14). Credit spreads in general have declined, including those for corporate, municipal, and GSE bonds. However, the largest declines have come in those markets -- such as agency debt and high-grade consumer asset-backed securities -- where policies are providing direct support (see Figures 2, 16, 26, and 27).

Figure 3: Interbank Lending: 3-Month LIBOR-OIS Spread (basis points)



Source: Bloomberg.

Figure 4: Cost of Insuring Against Risk of Default: CDX 5-Year Investment-Grade Index, Spread (basis points)



Source: Bloomberg.

Credit creation in securities markets has surged, but much of the new issuance has occurred with the backing of government support. Nearly $700 billion in issuance of new debt securities has been concentrated in GSE-backed mortgage bonds, TALF-supported ABS, and new investment-grade corporate bonds (see Appendix A, Figures 19-20). New issuance of corporate bonds this year has been substantially larger than the decline in bank lending to businesses (see Appendix A, Figures 21-22). However, the net impact on the availability of credit likely varies across lending markets. And most small businesses do not have the ability to substitute credit from bank loans with revenue from issuing bonds. Still, there are signs that credit markets for small businesses are improving. The secondary market for guaranteed Small Business Administration loans, for example, had essentially stopped working last fall and had only $86 million in January re-sales. That market improved notably this spring, with $325 million in sales by May.

III. The Next Phase: Beginning the Process of Exit

We are now moving into a new phase of our strategy to stabilize and rehabilitate financial markets. As the need for the emergency programs that were put in place during the most acute phase of the crisis declines, those programs will wind down. At the same time, the use of those programs, by design, continues to decline as the financial system recovers. Maintaining extraordinary government support where it is no longer needed could undermine our goal of restoring a vibrant financial system driven by market discipline.

But the financial system is still fragile, and some of the improvements that we have seen in many financial markets are still largely dependent on the support of extraordinary policies. We will continue to provide support where it is necessary to sustain confidence in the financial system and to support critical channels of credit to households and businesses.

A. Exiting from Some Emergency Programs as Financial Conditions Normalize

As the risk of catastrophic failure of the financial system has receded, the need for some of the emergency programs put in place in during the most acute phase of the crisis has receded as well.

In early 2009 the financial system was still very fragile. In that context the Administration included a $250 billion "placeholder" in the President's Budget to support an additional $750 billion in total expenditures to stabilize financial markets if necessary. Following the successful conclusion of the "stress test" for the country's largest financial institutions, the resulting ability of banks to raise private capital, and growing signs of financial stabilization, this placeholder was removed from the Budget in the August Midsession Review.

At the height of the crisis last fall, Treasury established the Money Market Mutual Fund Guarantee Program to prevent a run on money market mutual funds in the wake of the failure of Lehman Brothers and the well-publicized troubles of several large funds. This program – which currently provides protection for about $2.5 trillion in investments – will expire on September 18. Due to improved market confidence, Treasury has determined that it does not need to establish a successor program. Since inception, Treasury has had no losses under this program. In fact, it has earned the U.S. Government $1.2 billion in fees.

In October 2008, the FDIC established the TLGP to stabilize the financial system and to facilitate bank lending. Through the TLGP, the FDIC provides a guarantee on both transaction accounts and newly-issued senior debt issued by banks. The last day to issue new debt under the Debt Guarantee Program of the TLGP is currently October 31, 2009. Due to market improvements, the FDIC anticipates that this program will not need to be extended. However, the FDIC recently announced that it is considering establishing an emergency facility for up to six months that could allow current participants in the Debt Guarantee Program to issue additional guaranteed-debt under limited circumstances at substantially higher fees.

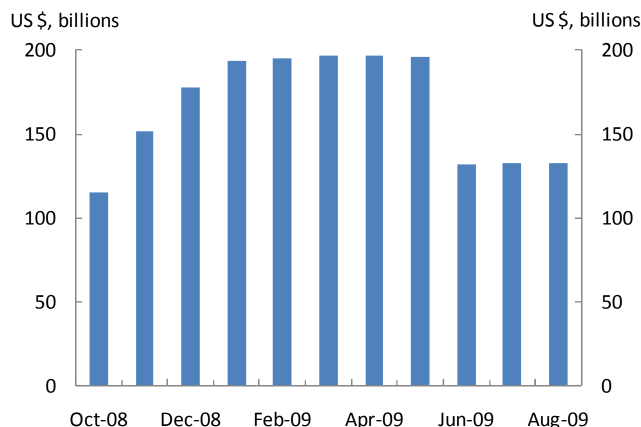
B. Diminishing Reliance on Federal Support

Declining utilization of programs put in place to contain the financial crisis is a sign that the financial system is healing. Many of the crisis-related programs were designed to unwind naturally. Fees and other aspects of their pricing were intended to make them unattractive as financial conditions normalize. As a result, utilization of many of the programs has already decreased substantially.

Treasury has made approximately $200 billion in capital injections in banks through the Capital Purchase Program (CPP), and provided an addition $50 billion in support for banks through other programs. In return, Treasury received preferred equity, subordinated debentures, and warrants. The preferred equity provides dividends of five percent for the first five years and nine percent thereafter. Over $70 billion of preferred equity received under the CPP has already been repaid (see Figure 5). In addition, Treasury has received roughly $10 billion in income from CPP investments, including dividends, interest, fees, and proceeds from the sale of warrants. For the 23 institutions in which Treasury’s CPP investments have been fully repaid, Treasury earned an annualized average return of 17 percent.

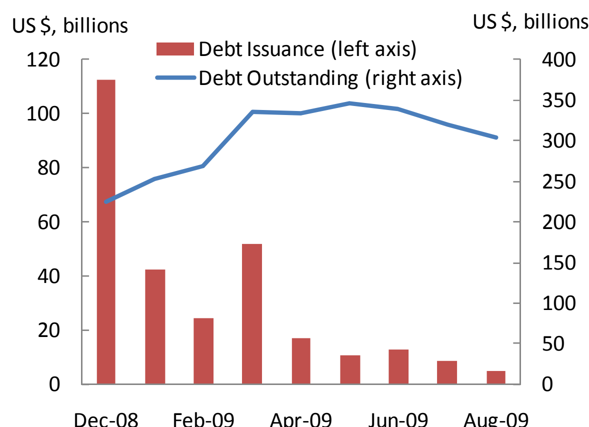
Treasury's Money Market Mutual Fund Guarantee Program has experienced a similar decline in utilization. At the program's inception, 93 percent of money market mutual funds (by asset size) participated. Utilization has fallen to 68 percent of the market. In return for the guarantee, Treasury charges an annual fee of four to six basis points of a participating fund’s asset base, which has yielded the U.S. Government $1.2 billion in income to date.

Figure 5: Utilization of Treasury CPP Program: Cumulative Net CPP Disbursements (US $, billions)



Source: Treasury.

Figure 6: Utilization of FDIC TLGP Senior Debt Guarantee: Issuance and Outstanding Debt (US $, billions)

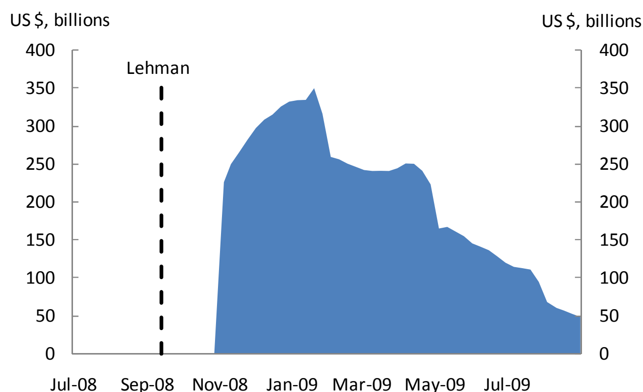


Sources: FDIC; Bloomberg.

FDIC's TLGP senior debt guarantee program was also designed to be uneconomic once market conditions improved. Early in the program, fees to issue debt under the TLGP ranged between 50 to 100 basis points, depending on maturity. The FDIC increased those fees on April 1, 2009, by 25 to 50 basis points. To date, the fees have generated roughly $9 billion in income. As markets have stabilized, the cost of borrowing in private markets has declined to levels that make TLGP fees less attractive, and utilization of the TLGP debt guarantee program has fallen. Issuance peaked at about $113 billion in December and was roughly $5 billion in August (see Figure 6). In addition, the stock of guaranteed debt has fallen by nearly $50 billion since early June.

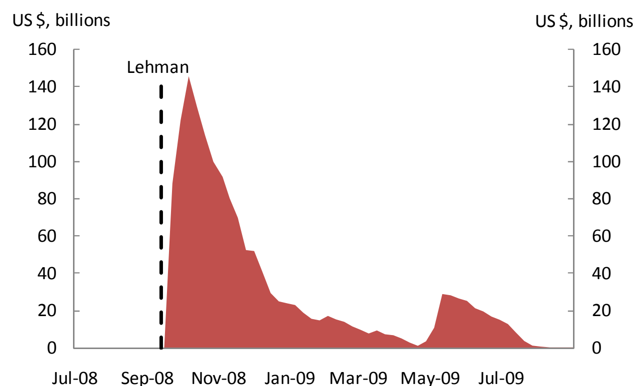
All of the Federal Reserve liquidity programs have experienced significant drops in utilization. For example, credit extended in money markets through the Commercial Paper Funding Facility (CPFF) has declined from a peak of $350 billion in January to $48 billion recently, and lending under the Asset-Backed Commercial Paper Money Market Mutual Fund Liquidity Facility (AMLF) has fallen from $152 billion to $79 million (see Figures 7 and 8). Similarly, lending under the Term Auction Facility (TAF)—which provides liquidity to depository institutions—fell from a peak of $493 billion in March to roughly $212 billion currently. The Federal Reserve charges interest on loans under each of these programs. Further, utilization of swap lines with foreign central banks--which satisfy demand for U.S. dollar funding overseas--dropped from a peak of $583 billion in December to $63 billion recently.

Figure 7: Utilization of Fed CPFF Program: Net Portfolio Holdings of Facility (US $, billions)



Source: Federal Reserve.

Figure 8: Utilization of Fed AMLF Program: Loans Outstanding Under Facility (US $, billions)



Source: Federal Reserve.

Appendix B provides details regarding utilization and pricing for the major government and Federal Reserve financial programs put in place since the crisis began. Concrete commitments under these programs include net funds paid out or loans extended, plus guaranteed liabilities. Those commitments have fallen in the aggregate, especially for Treasury and Federal Reserve programs. For example, Treasury commitments under TARP have fallen from $370 billion to $298 billion.[4]

C. Ongoing Role for Policy

The normalization of financial markets achieved to date is partial and fragile, and the economic recovery is, at best, in its very early stages. In residential real estate, although the rate of deterioration has slowed, the market has not established a firm bottom (see Appendix A, Figures 28-33), and foreclosures continue to rise across all classes of mortgages, with prime mortgages now leading the way. The restructuring process for the commercial real estate market has only recently begun. The pace of bank failures has increased and it is expected to remain elevated for some time. However, liquidity-induced failures have steadily decreased given the existence of deposit insurance and the orderly resolution of failed banks. Moreover, the FSP in general and the SCAP in particular were designed to ensure that the financial system as a whole had the capacity to continue to perform its vital functions while dealing with these challenges.

During this difficult period of adjustment, the system could be sensitive to unanticipated market events. Further, in those markets where conditions have improved, it is unclear whether the improvements achieved to date will persist without a period of continued government support. We must temper our desire to terminate our extraordinary financial support with the recognition that there is still a risk of market disruption that would have a significant negative impact on

[4] Treasury's current net disbursements under TARP are $293 billion, and it has guaranteed $5 billion of Citigroup assets under the Asset Guarantee Program.

American families, workers, and businesses. Some programs must continue until it is clear that the financial recovery achieved to date is fully self-sustaining.

D. International Coordination

Just as the financial crisis and recession have been global, so too have the challenges for policy. As policymakers around the world begin the long process of unwinding financial support programs put in place over the last year, they must be mindful of the international spillovers from their policy choices. Our financial institutions operate in a global marketplace. Maintaining a level playing field with high standards will be essential in ensuring that the global financial system recovers as quickly as possible, and that we do not soon repeat the financial turmoil we have experienced over the last year.

IV. Status of Major Programs

The extraordinary financial programs put in place during this crisis will evolve in different ways depending on circumstances. For some programs, we are moving from declining utilization to termination. For others, although utilization has declined, the programs continue to make meaningful contributions to market confidence. And programs such as the increase in the FDIC's deposit insurance coverage to $250,000 per account and the FDIC's recently-extended TLGP transaction account guarantee continue to be utilized and have been important to market stability. Still other programs, such as PPIP and TALF for commercial MBS, are just taking hold and rehabilitating key markets.

A. Additional Stabilization Funding in the President's Budget

The President's Budget, which was released in the spring, included a $250 billion "placeholder" for contingent future stabilization efforts. Those budget resources could have supported an estimated $750 billion in gross commitments, depending on how they were used. When the President's Budget was presented in the spring, given the magnitude of the stress still evident in financial markets, it was prudent to make it clear that the Administration's commitment to maintaining financial stability would not be undermined by inadequate fiscal resources. As policies have taken hold and market conditions have improved, we believe that remaining TARP authority should be adequate to maintain market confidence and address unforeseen risks. As a result, the President removed the "placeholder" in his Midsession Review of the FY 2010 Budget.

B. Treasury Money Market Mutual Fund Guarantee

Treasury's Money Market Mutual Fund Guarantee Program is scheduled to terminate on September 18. Currently this program covers about $2.5 trillion in money market mutual fund

investments. The Program served its purpose of adding stability to the money market mutual fund industry during market disruptions last fall. Treasury does not plan to establish a successor program, as it does not view such a program as necessary to preserve market confidence.

C. FDIC Programs

The Emergency Economic Stabilization Act of 2008 (EESA) expanded the FDIC's deposit insurance from $100,000 to $250,000 per account, which the Helping Families Save Their Homes Act of 2009 extended through 2013. Although the expanded coverage will not terminate in the near-term, the FDIC can alter the fee structure, and the Administration and Congress can revisit what the appropriate coverage level will be after 2013. That level should be a function of depositor confidence at that time and going forward.

After receiving comments and determining that the program was still necessary for market stability, the FDIC recently extended the guarantee on transaction accounts to June 30, 2010. However, in doing so it increased the fee from 10 basis points to 15-25 basis points, depending on an institution's risk category. This fee increase will help ensure that the program is self-funding and does not impose losses on the Deposit Insurance Fund.

The last day for new issuance under the TLGP senior debt guarantee program is currently October 31. On September 9, 2009, the FDIC Board of Directors approved the phase out of this program as scheduled. In conjunction with this phase out, the FDIC is seeking comment on whether a temporary emergency facility should be put in place for six months after the expiration of the current program. Such a facility could provide additional guarantees for new issuance, at a substantially higher fee, in the event that participants are unable to access credit markets due to market disruption or other events beyond their control.

D. Federal Reserve Programs

Most of the special Federal Reserve liquidity programs are scheduled to terminate this year or in early 2010. Specifically, the Federal Reserve's Money Market Investor Funding Facility is scheduled to terminate in October, and its asset purchase programs are scheduled to wind down over coming months. The Federal Reserve recently extended expiration dates for the majority of its liquidity programs to February 1, 2010. In conjunction with Treasury, the Federal Reserve also extended the TALF program for newly issued commercial MBS to June 30, 2010, and for all other asset classes to March 31, 2010. In announcing these extensions, the Federal Reserve noted that although conditions have improved, "market functioning in many areas remains impaired and seems likely to be strained for some time." The Federal Reserve has the authority to extend these programs again, which would in most cases require a finding that "unusual and exigent circumstances" remain. Further, although the TAF program does not have a fixed expiration date, the Federal Reserve has trimmed the size of TAF auctions in

light of declining demand and has indicated that it expects to further reduce the size of TAF auctions gradually if financial conditions continue to improve.

E. TARP Programs

The authority established by Congress under EESA is supporting a number of programs that are making an essential contribution to stabilizing and rehabilitating a financial system still under stress.[5] For example, adjustment in the housing market is far from complete (see Appendix A, Figures 28-33). Construction activity and sales appear to have bottomed out over the summer, but there is still a substantial overhang of vacant and unsold homes. Housing prices appear to have stabilized in many markets. Nonetheless, a very large proportion of homeowners now have mortgage debt that is greater than the value of their homes, and the labor market is still weak. In this challenging environment, the modification portion of the Administration's Home Affordable Modification Program is just ramping up.

The issuance of new debt instruments backed by new consumer loans, known as ABS, has improved with the support of the TALF program. This is a critical channel for supply of new credit to households. But there has been little new issuance of ABS that is not supported by TALF, either directly through TALF-related purchases or indirectly because the instruments are eligible for such purchases. Recognizing the importance of this program, the Federal Reserve, in conjunction with Treasury, has recently extended deadlines for the program into next year.

The Securities PPIP program has just been launched. Program announcements have had a positive impact on asset prices in advance of actual transactions. Treasury expects that the initial PPIP securities funds will be fully funded before the end of the year. Depending on how financial markets evolve, more engagement may be needed for additional classes of securities. And Treasury and the FDIC continue to evaluate applications of the legacy loans purchase program, which may contribute to market stabilization.

Treasury continues to provide new capital to small banks under the CPP to stimulate a recovery in lending for viable businesses, large and small. Many small banks have relatively high exposures to commercial real estate loans, where credit problems are still growing, and other troubled investments. We will be monitoring these areas closely.

The Administration has set clear principles to ensure that our investments in AIG, General Motors, and Chrysler are limited and temporary. We will not seek to influence their day-to-day operations. Rather, we are providing support while they restructure. And we will seek to dispose of our interests as soon as practicable. The termination of the Auto Warranty Commitment Program demonstrates this commitment. The government invested $641 million

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[5] Pursuant to EESA, the Treasury Secretary's authority to guarantee, purchase, and make and fund commitments to purchase assets with TARP funding is scheduled to terminate on December 31, 2009. The Secretary may extend that authority to October 3, 2010 by submitting written certification to Congress.

in the program to give confidence to GM's and Chrysler's customers during a period of substantial uncertainty. Following the companies' emergence from bankruptcy, the money invested in the program has been returned, along with interest payments from New Chrysler.

Key parts of the financial system are still substantially impaired and the system as a whole remains somewhat fragile. Uncommitted TARP resources give the government the capacity to respond to unanticipated financial shocks. That capacity to respond with TARP resources continues to provide a critical backstop for financial stability.

V. Conclusion

As utilization of the extraordinary policies put in place to address the financial crisis declines, we remain committed to ensuring the stability of financial markets and rehabilitating channels of credit creation that are critical to American families and businesses. The process of exit will be prudent, not hasty. At the same time, we must address the structural weaknesses in our financial system that this crisis revealed. The Administration is working to gain approval of a detailed set of proposals to reform our regulatory system to address these weaknesses and keep our financial markets and economy on track to a sustainable recovery.

Appendix A

Financial Market Indicators

Section 1: Indicators of Financial Stress

Figure 9: LIBOR – OIS Spread

Figure 10: Spread Between 3-Month LIBOR and T-bills

Figure 11: CDX Investment Grade Corporate Index, Spread of Credit Default Swaps to Treasury Securities

Figure 12: Indicative Legacy Asset Prices

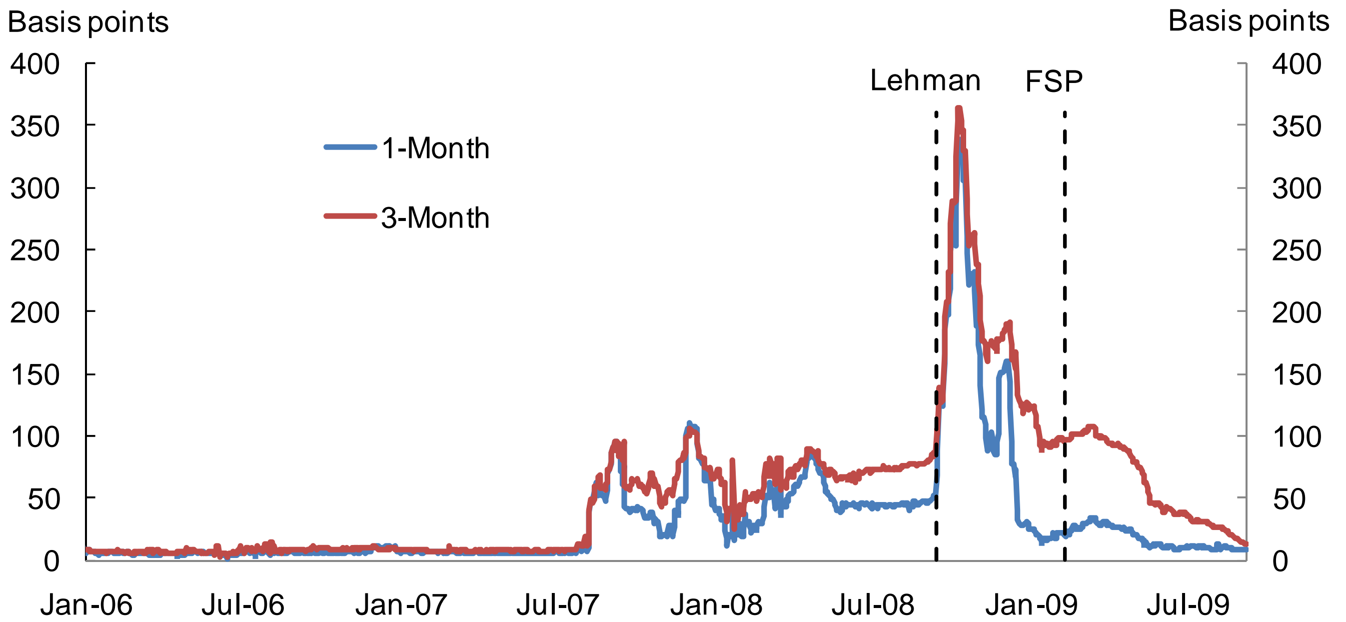
Figure 13: U.S. Equity Indices

Figure 14: Implied Volatility of S&P 500 (VIX)

Note: "Lehman" indicates the date of the Lehman Brother bankruptcy, and "FSP" indicates the date on which the Obama Administration announced its Financial Stability Plan.

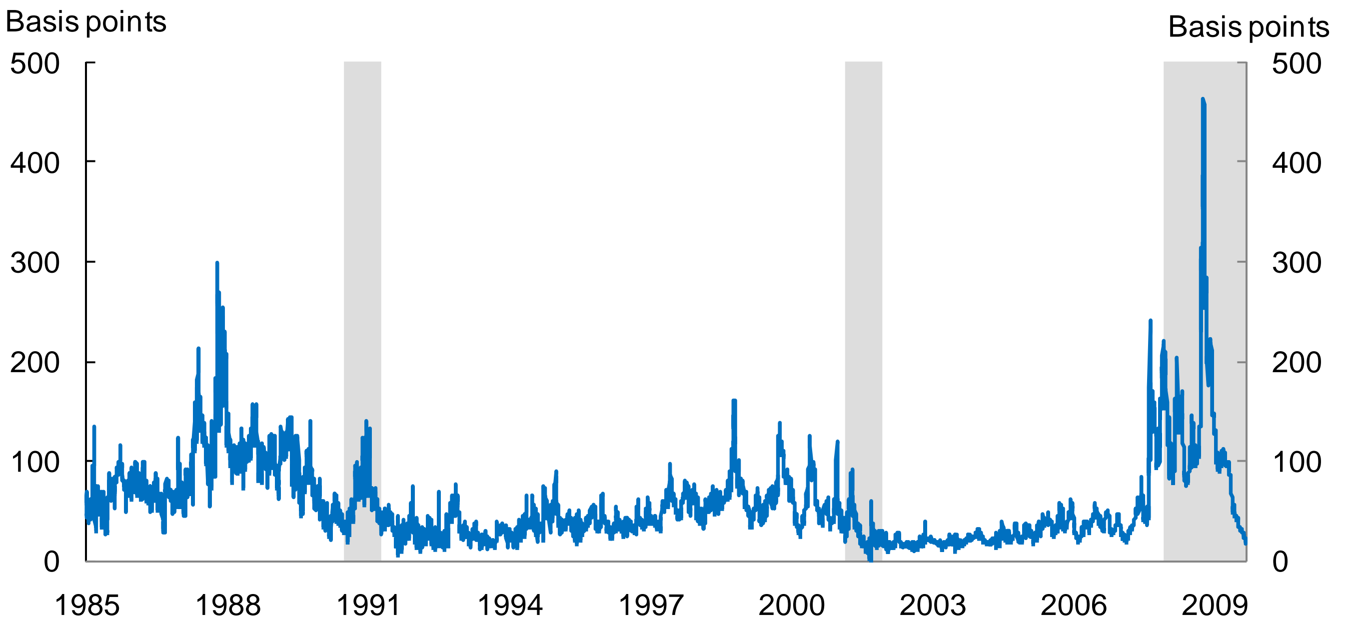
Indicators of Financial Stress

Figure 9: LIBOR – OIS Spread (Basis Points)



Source: Bloomberg.

Figure 10: Spread Between 3-Month LIBOR and T-bills (Basis Points)



Note: Gray shading represents recessions.

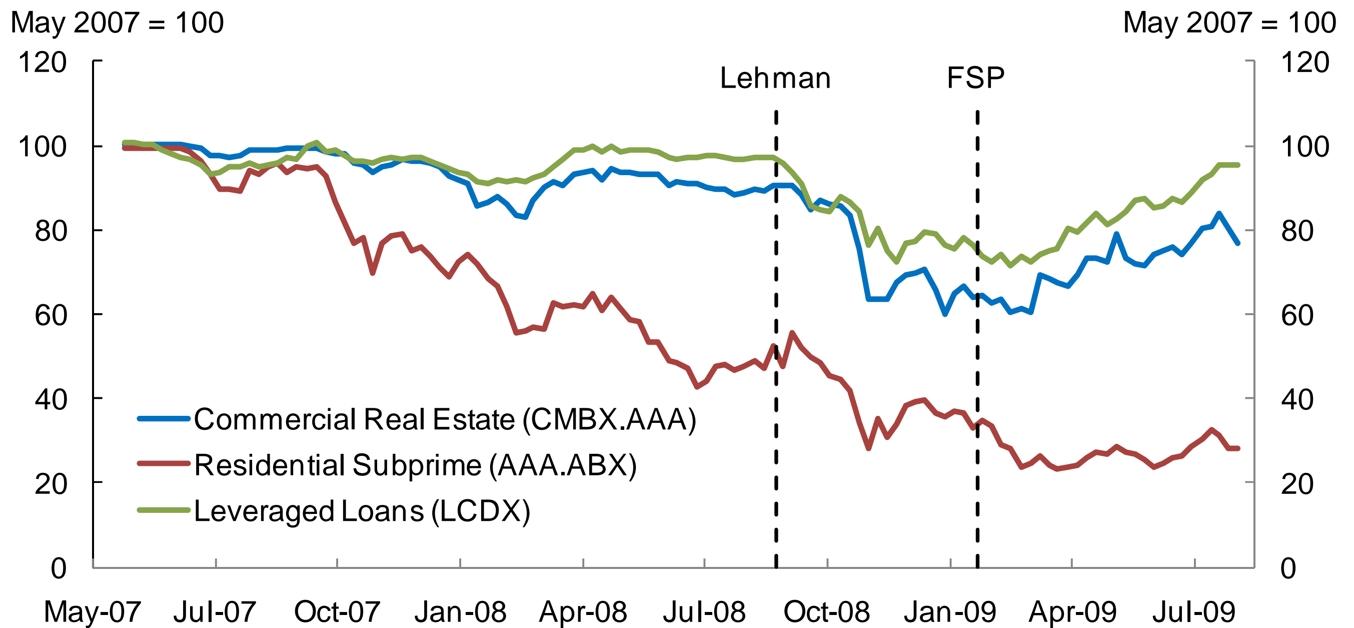
Source: Bloomberg.

Indicators of Financial Stress (continued)

Figure 11: CDX Investment Grade Corp. Index, Spread of Credit Default Swaps to Treas. (Basis Points)

Source: Bloomberg.

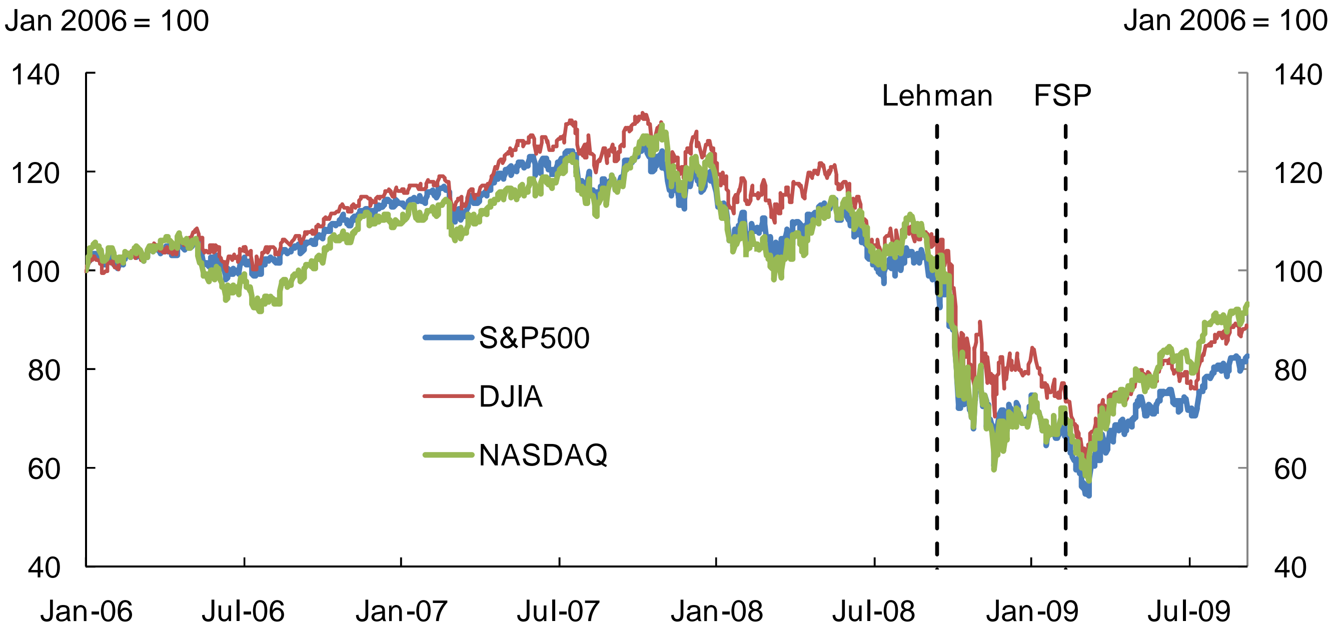
Figure 12: Indicative Legacy Asset Prices, Index (May 2007 = 100)



Sources: Bloomberg; JPMorgan.

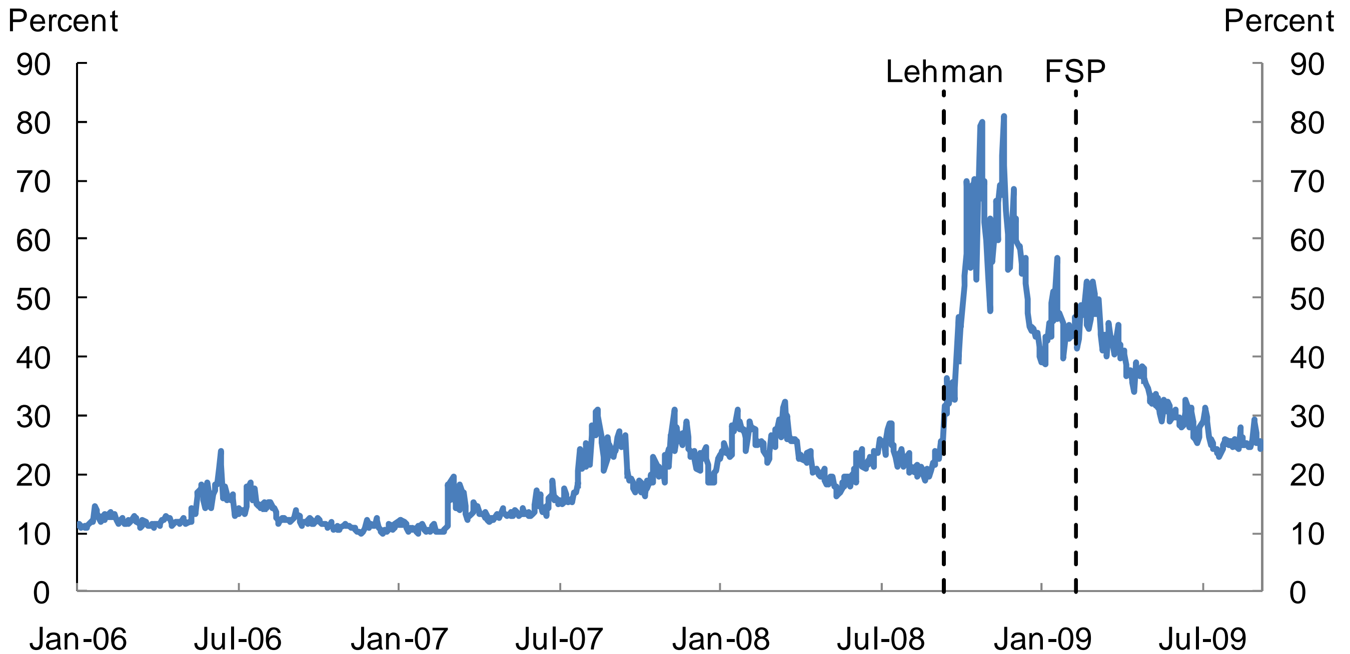
Indicators of Financial Stress (continued)

Figure 13: U.S. Equity Indices, Jan 2006 = 100



Source: Bloomberg.

Figure 14: Implied Volatility of S&P 500 (VIX)



Source: Bloomberg.

Section 2: Indicators of Bank Conditions

Figure 15: Average CDS Spreads of Selected Financial Institutions

Figure 16: Spreads of “A”-Rated Industrial and Financial Corp. Bonds to Treasury Securities

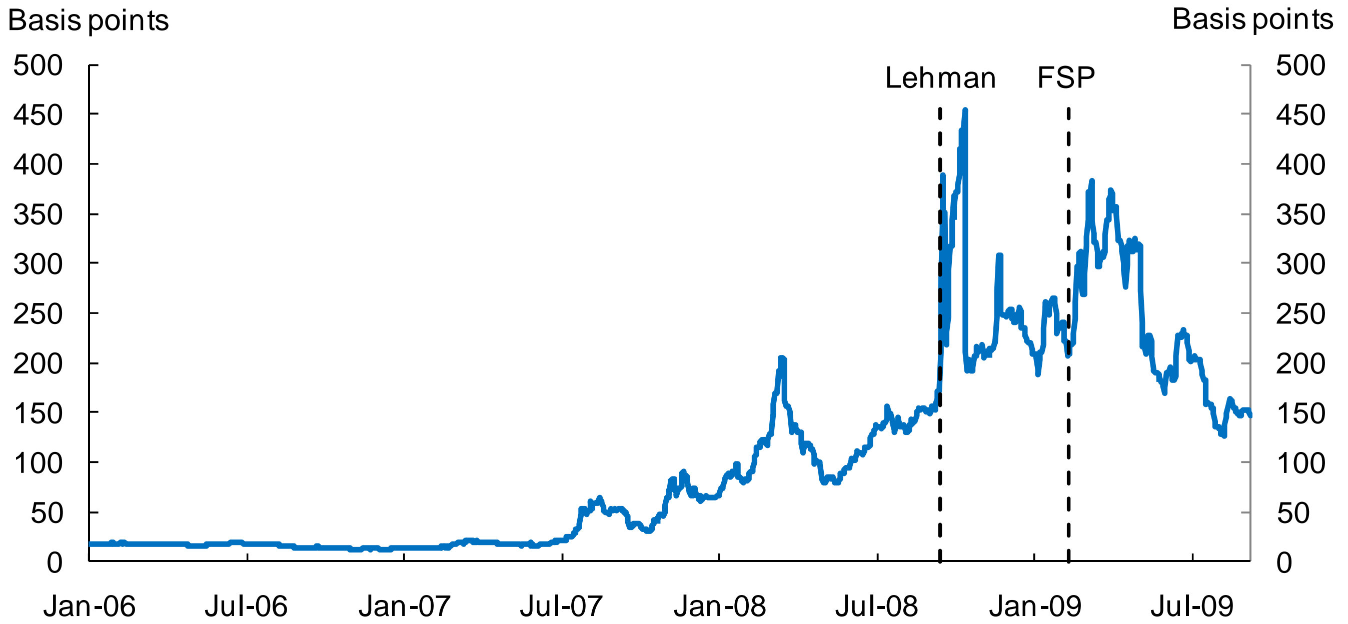
Figure 17: Equity Prices, S&P 500 and Financial Firms

Figure 18: Price for Preferred Stocks, Primarily Financials

Note: “Lehman” indicates the date of the Lehman Brother bankruptcy, and “FSP” indicates the date on which the Obama Administration announced its Financial Stability Plan.

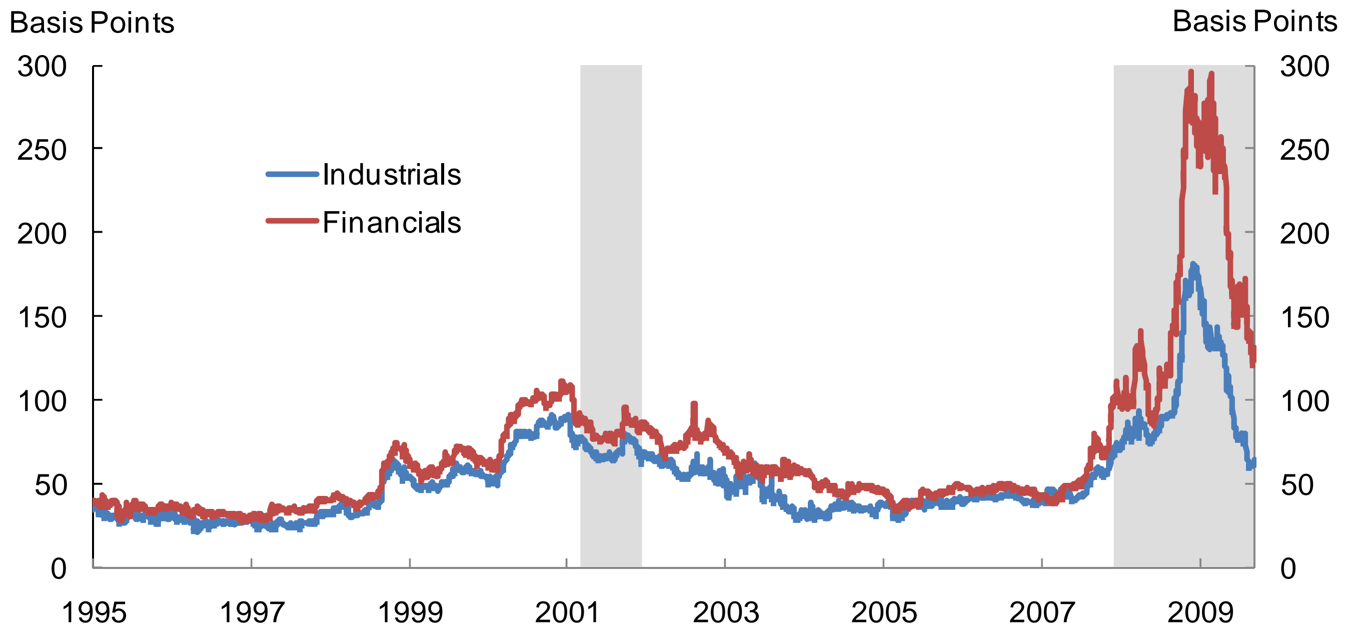
Indicators of Bank Conditions

Figure 15: Average CDS Spreads of Selected Financial Institutions (Basis Points)



Note: Includes BAC, C, GS, JPM, MS, and WFC. Source: Bloomberg.

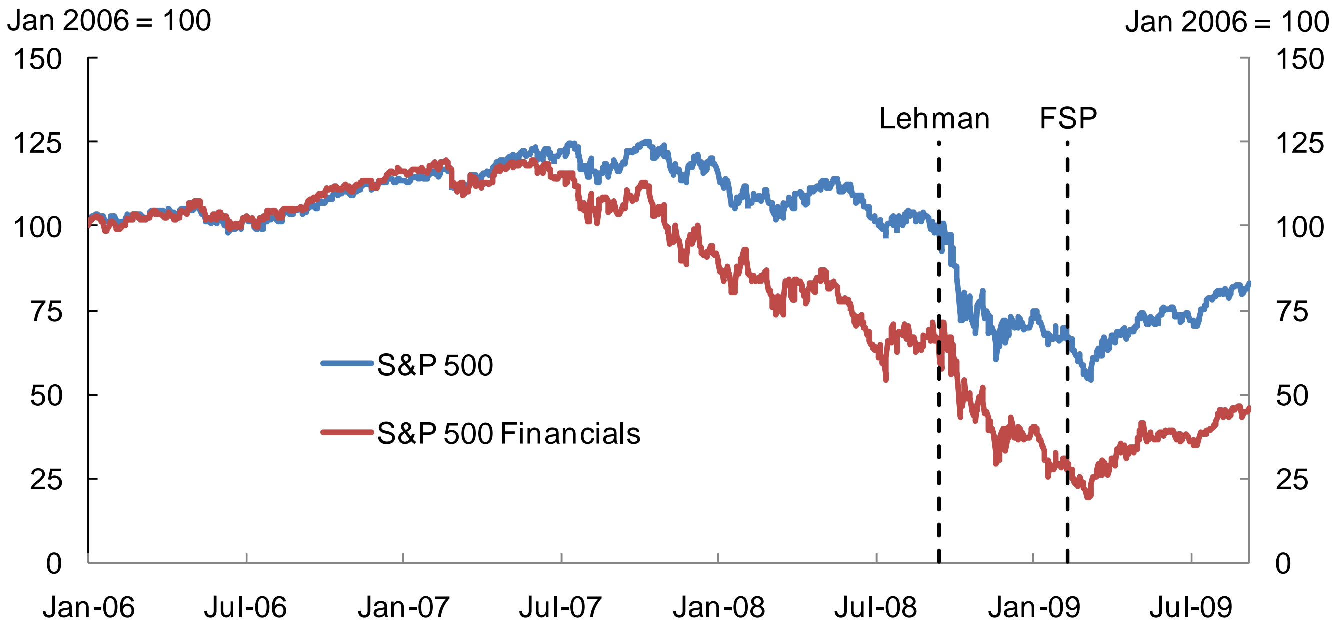
Figure 16: Spreads of "A"-Rated of Industrial and Financial Corp. Bonds to Treas. (Basis Points)



Note: Gray shading represents recessions. Source: Bloomberg.

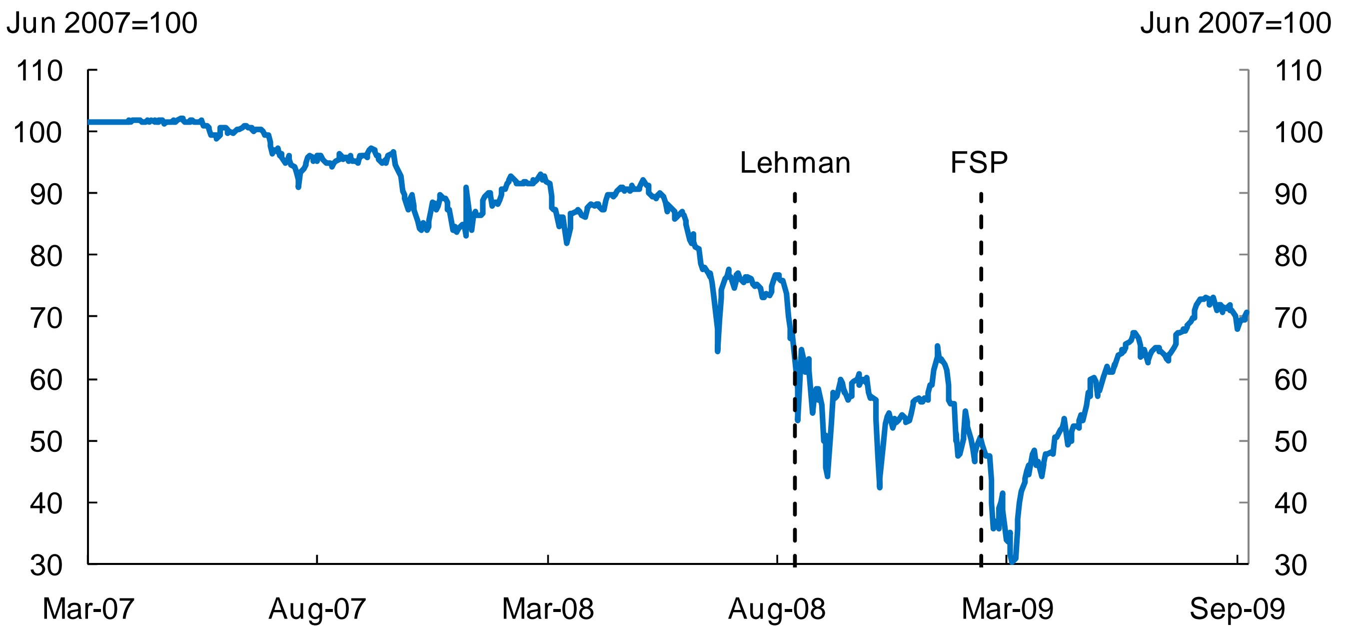
Indicators of Bank Conditions (continued)

Figure 17: Equity Prices, S&P 500 and Financial Firms, (January 2006=100)



Source: Bloomberg

Figure 18: Price for Preferred Stocks, Primarily Financials, (June 2007=100)



Note: Price of fund that includes predominantly preferred share of financial firms. Source: Bloomberg.

Section 3: Indicators of Credit Flows

Figure 19: Consumer ABS Issuance

Figure 20: U.S. Corporate Bond Issuance

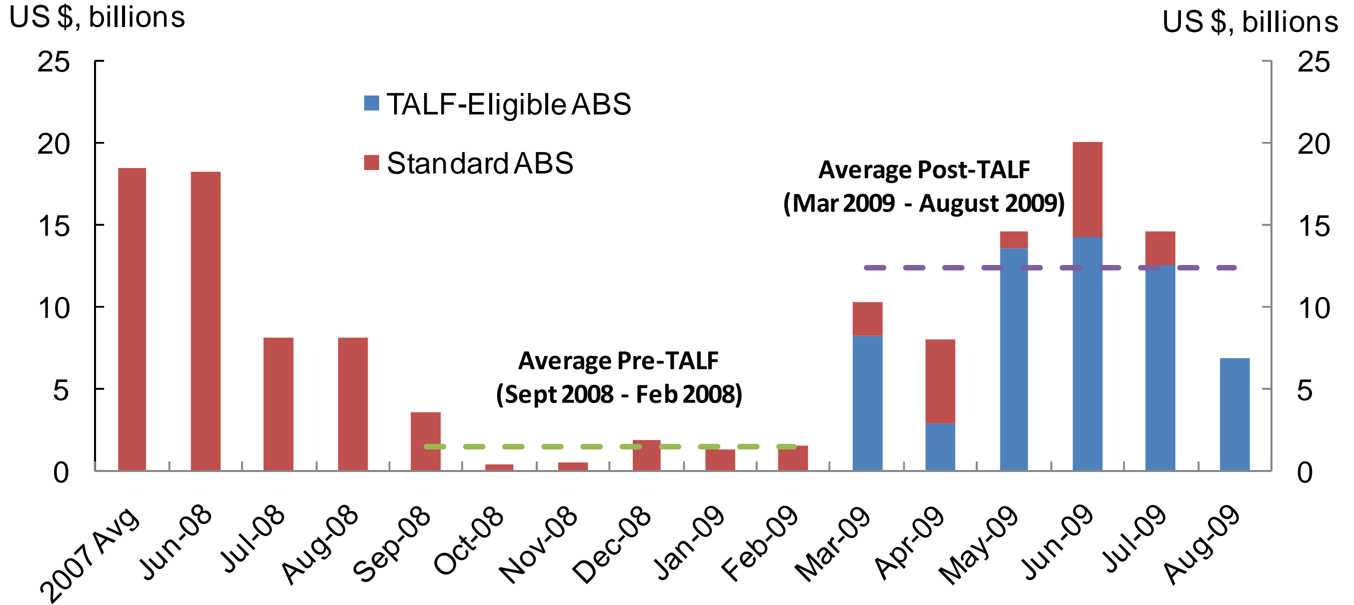
Figure 21: Change in Real Commercial and Industrial Loans Held by Commercial Banks

Figure 22: Change in Real Commercial Real Estate Loans Held by Commercial Banks

Note: “Lehman” indicates the date of the Lehman Brother bankruptcy, and “FSP” indicates the date on which the Obama Administration announced its Financial Stability Plan.

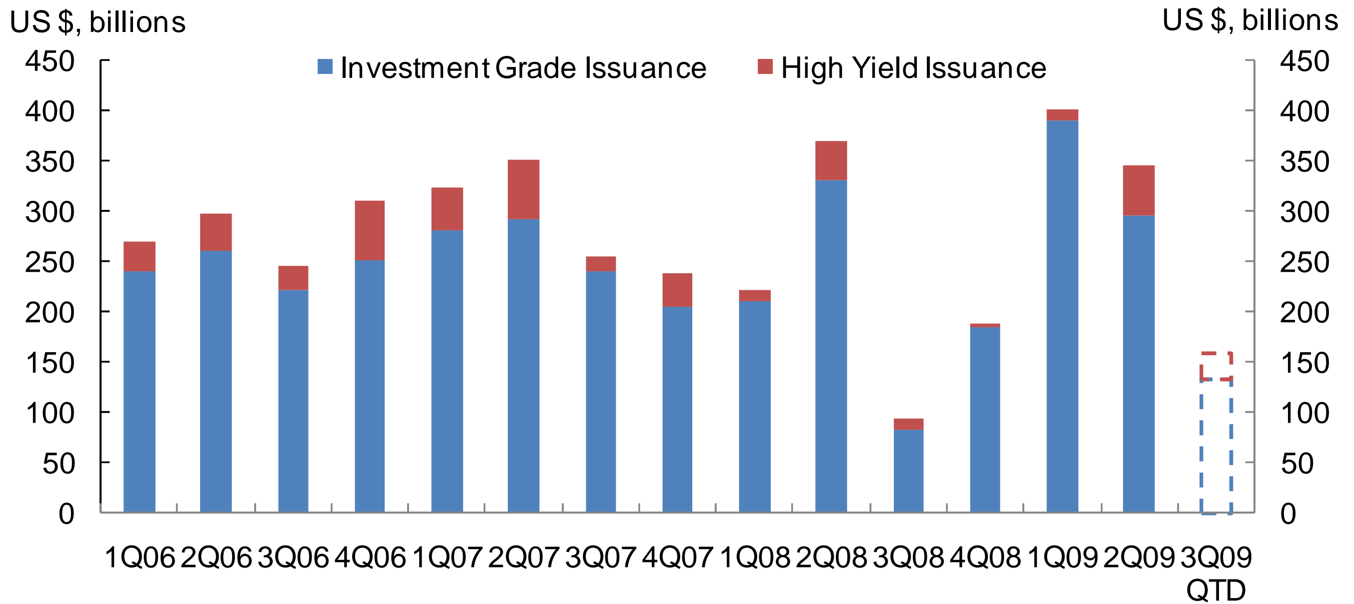
Indicators of Credit Flows

Figure 19: Consumer ABS Issuance (US$, billions)



Source: Federal Reserve.

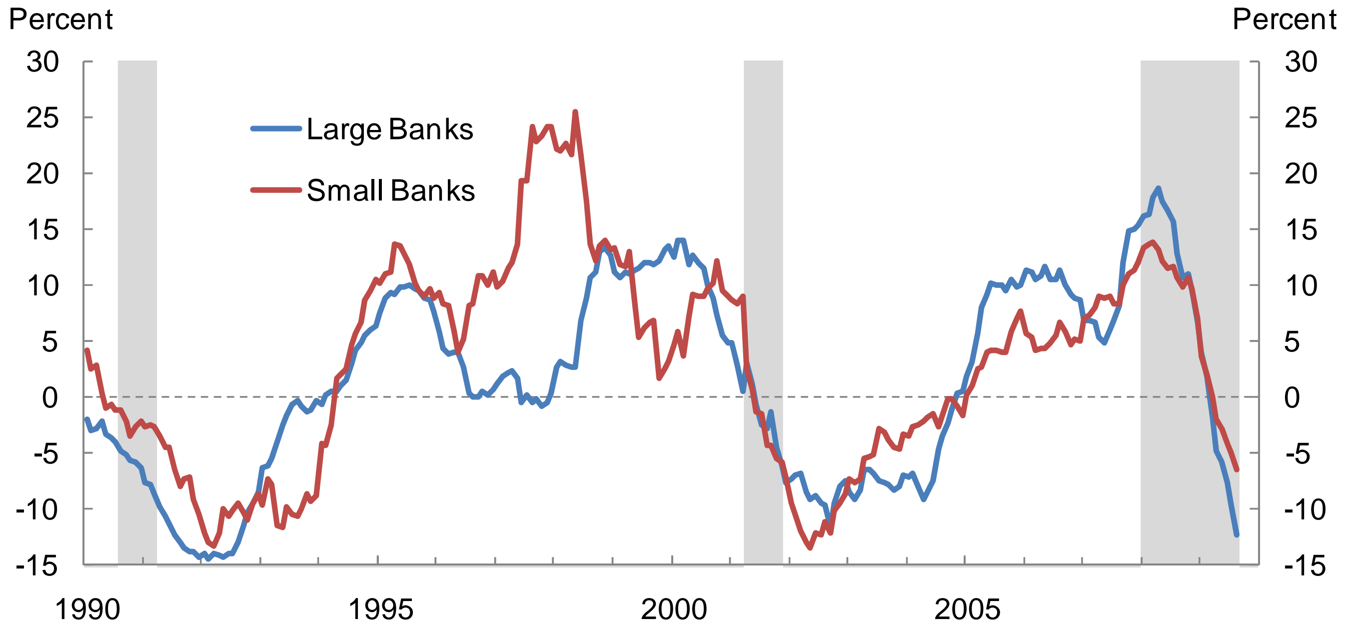
Figure 20: U.S. Corporate Bond Issuance (US$, billions)



Source: Bloomberg.

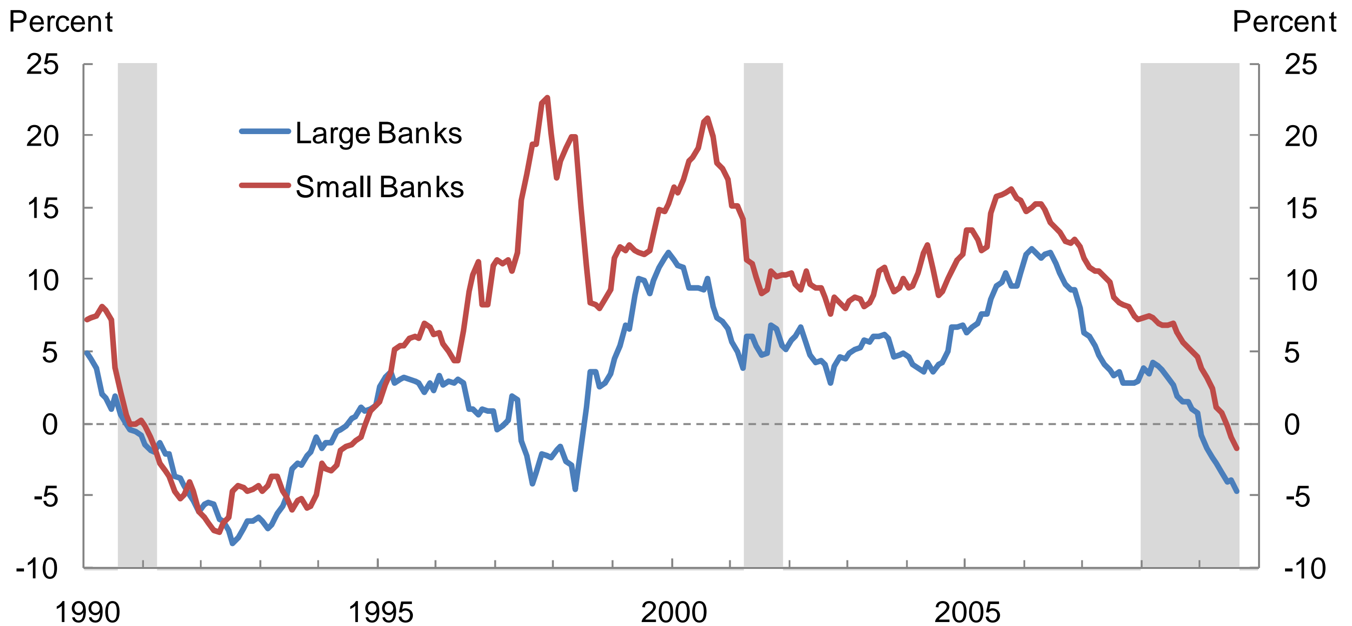
Indicators of Credit Flows (continued)

Figure 21: Change in Real Com. and Indus. Loans Held by Commercial Banks (y/y, Percent)



Notes: Deflated by Core PCE prices; gray shading represents recessions. Sources: Federal Reserve; BEA.

Figure 22: Change in Real Com. Real Estate Loans Held by Commercial Banks (y/y, Percent)



Notes: Deflated by Core PCE prices; gray shading represents recessions. Source: Federal Reserve; BEA.

Section 4: Interest Rates

Figure 23: Yields for Treasury Securities, Various Maturities

Figure 24: Spread Between 2-Year and 10-Year Treasury Yields

Figure 25: Mortgage Rate, Conventional 30-Year Fixed

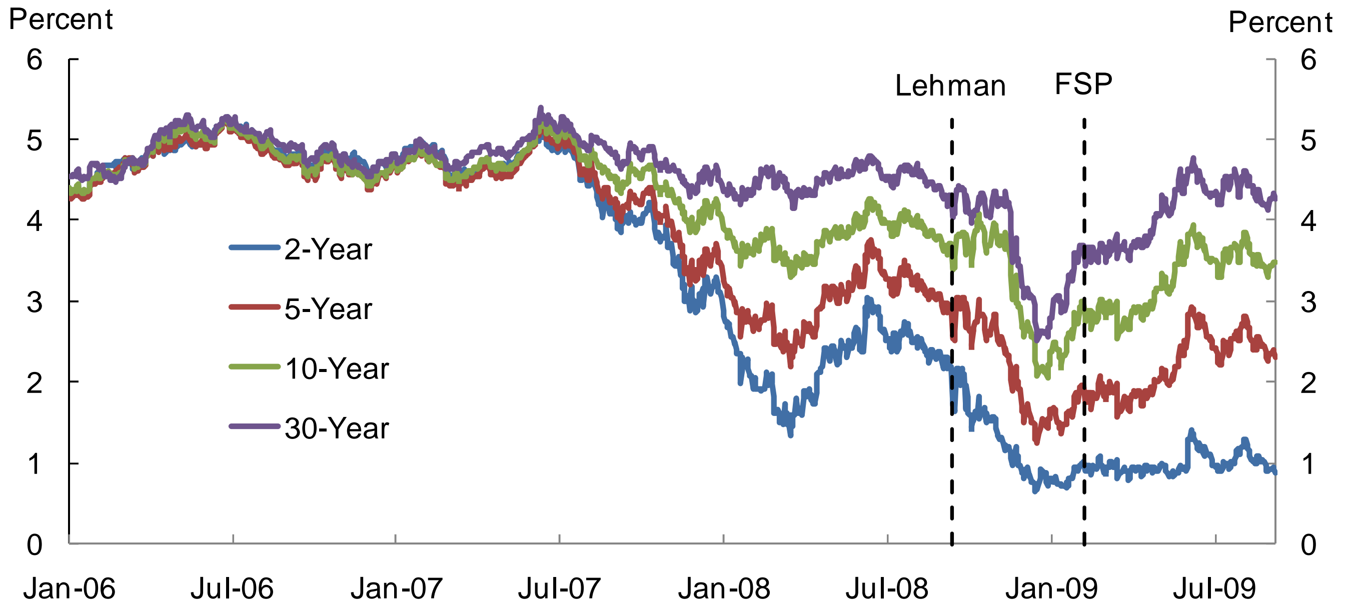
Figure 26: Spread Between Fannie Mae Debt and Treasury Securities of Comparable Maturity

Figure 27: Municipal Bond Yields, AAA-Rated, 10-Year

Note: “Lehman” indicates the date of the Lehman Brother bankruptcy, and “FSP” indicates the date on which the Obama Administration announced its Financial Stability Plan.

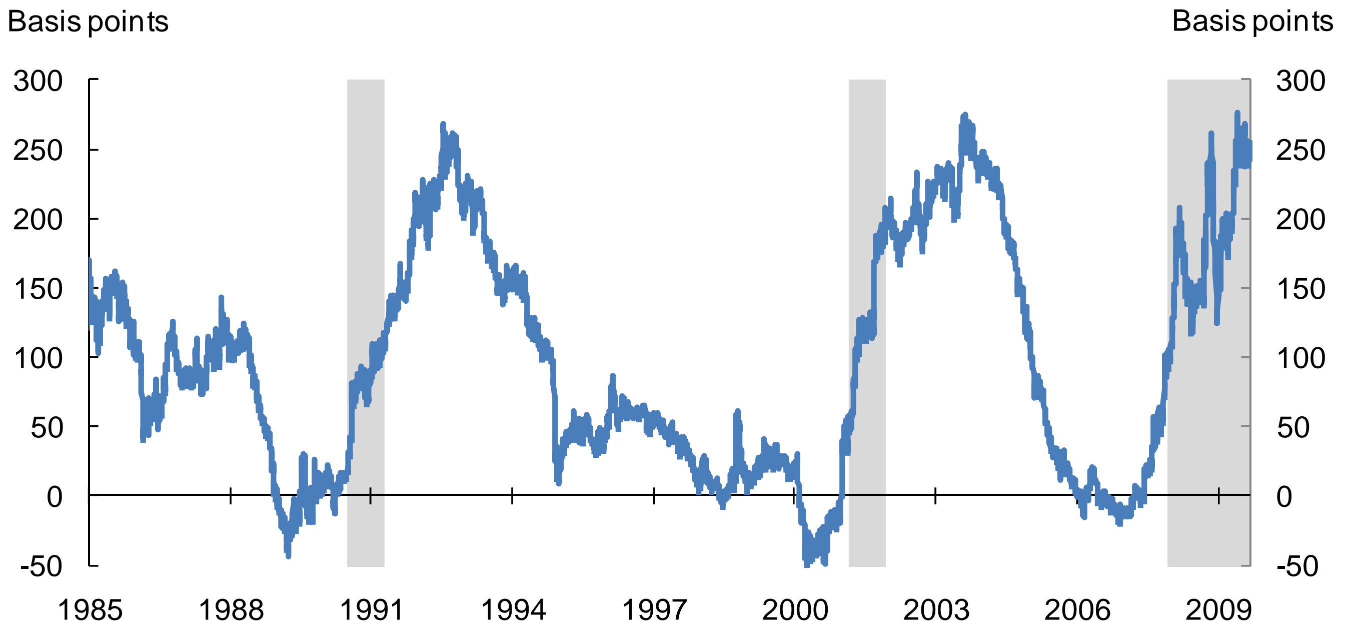
Interest Rates

Figure 23: Yields for Treasury Securities, Various Maturities (Percent)



Source: Bloomberg.

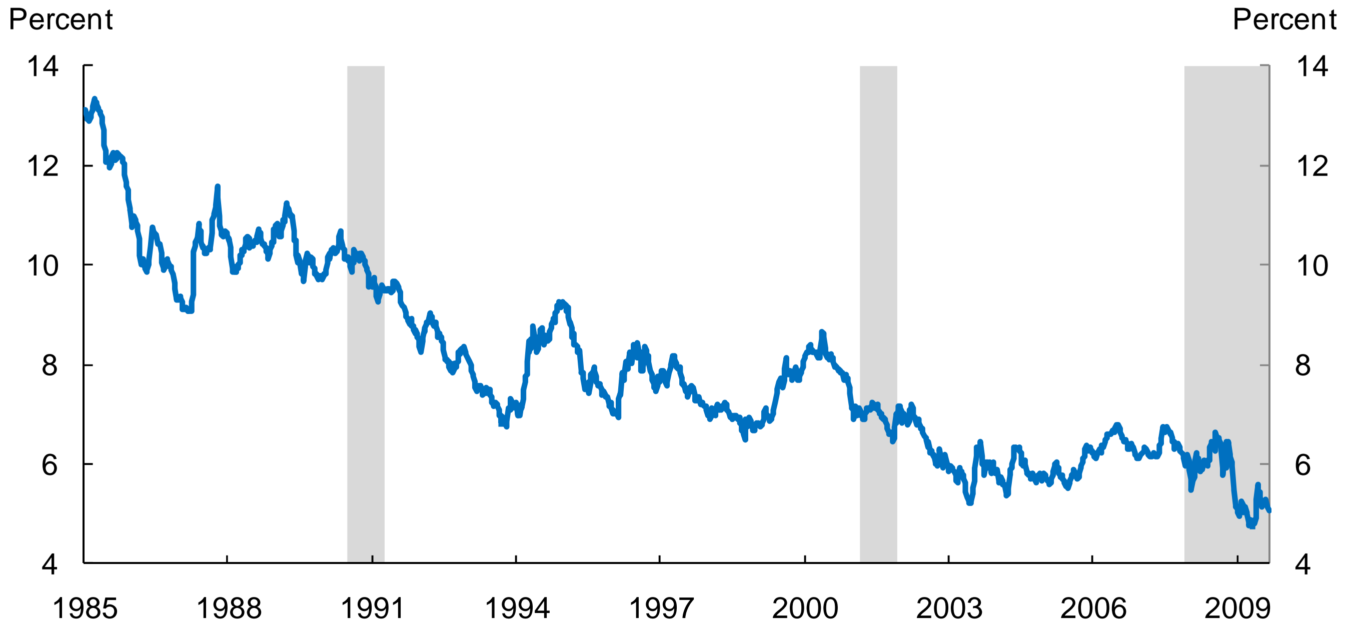
Figure 24: Spread Between 2-Year and 10-Year Treasury Yields (Basis Points)



Note: Gray shading represents recessions.

Source: Bloomberg.

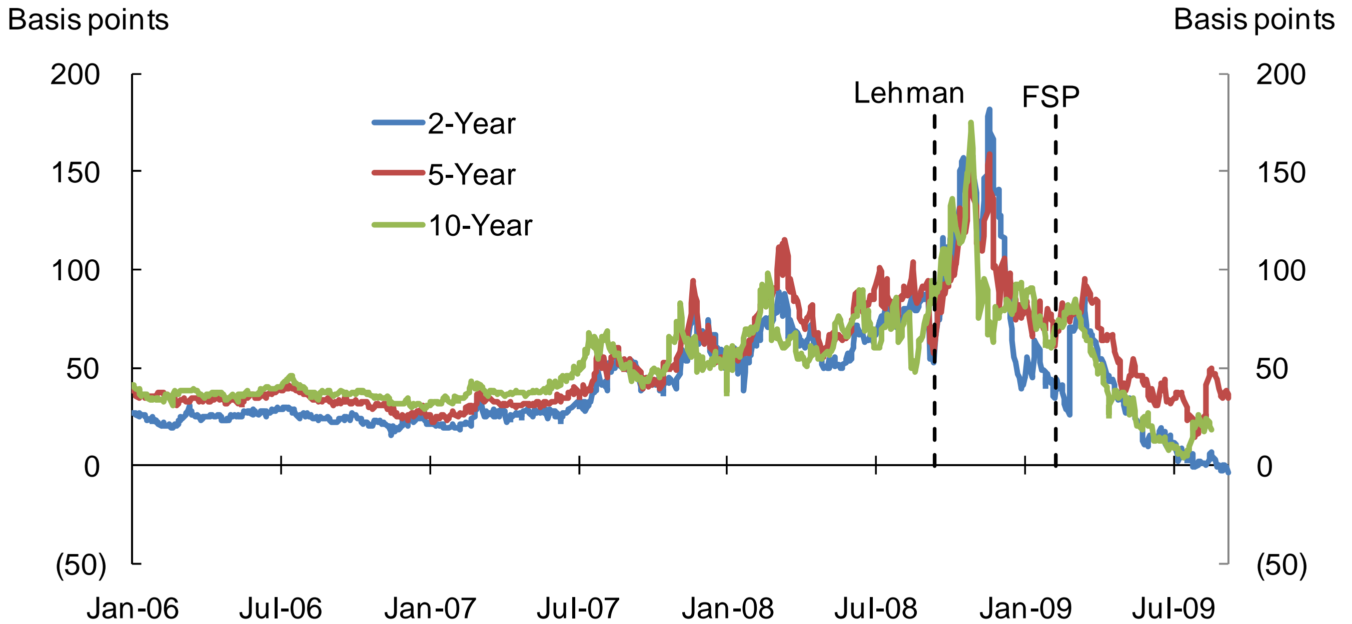
Figure 25: Mortgage Rate, Conventional 30-Year Fixed, (Percent)



Note: Gray shading represents recessions.

Sources: Federal Reserve; FHLMC.

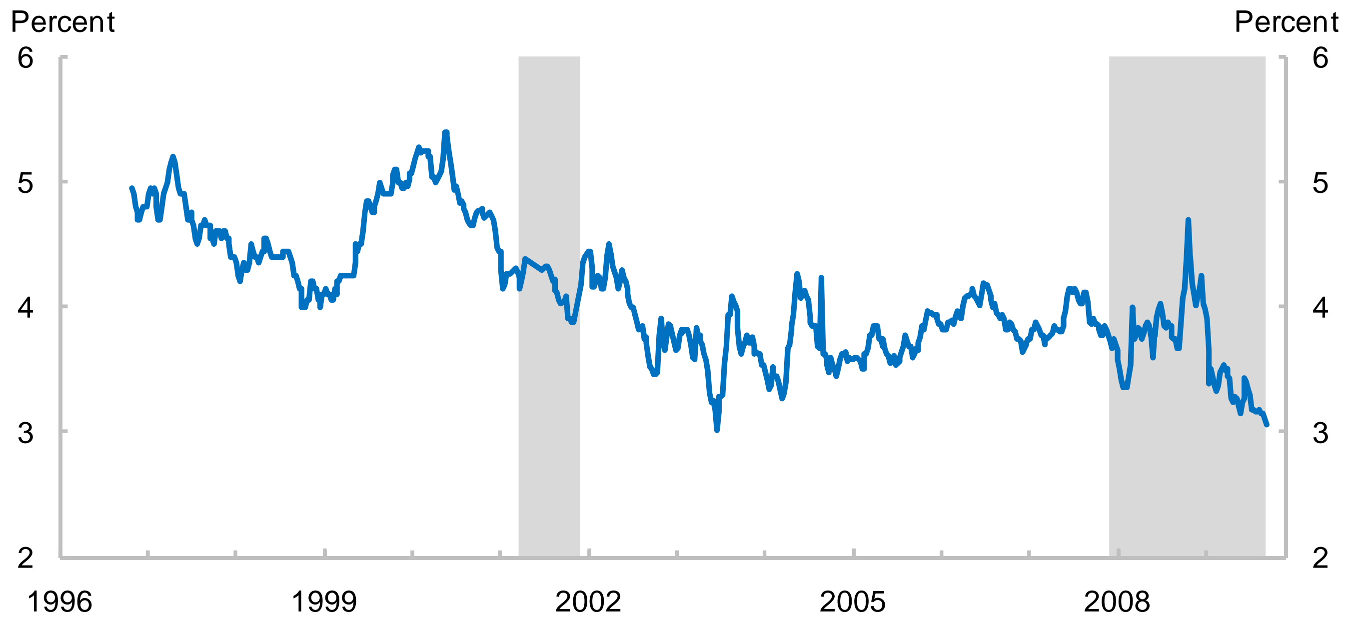
Figure 26: Spread Between Fannie Mae and Treasury Securities of Comparable Maturity (Basis Points)



Source: Bloomberg.

Interest Rates (continued)

Figure 27: Municipal Bond Yields, AAA-Rated, 10-Year (Percent)



Note: Gray shading represents recessions.

Sources: Wall Street Journal; Haver.

Section 5: Indicators of Housing Markets

Figure 28: Mortgage Applications for Purchase and Refinancing

Figure 29: Mortgage Originations by Product and Refinancing as a Share of Originations

Figure 30: Sales of Single Family Homes, Existing and New

Figure 31: Housing Starts

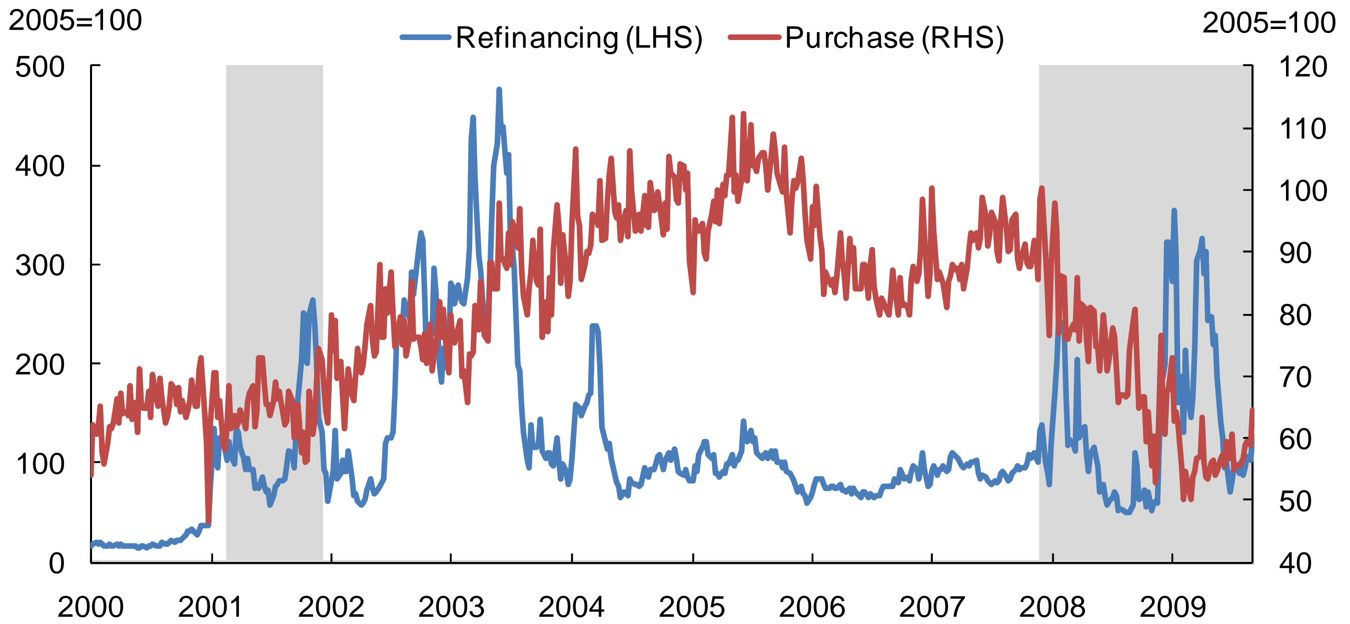
Figure 32: Real House Prices, Level and 6-Month Change

Figure 33: Mortgage Delinquencies, Conforming and Subprime

Note: “Lehman” indicates the date of the Lehman Brother bankruptcy, and “FSP” indicates the date on which the Obama Administration announced its Financial Stability Plan.

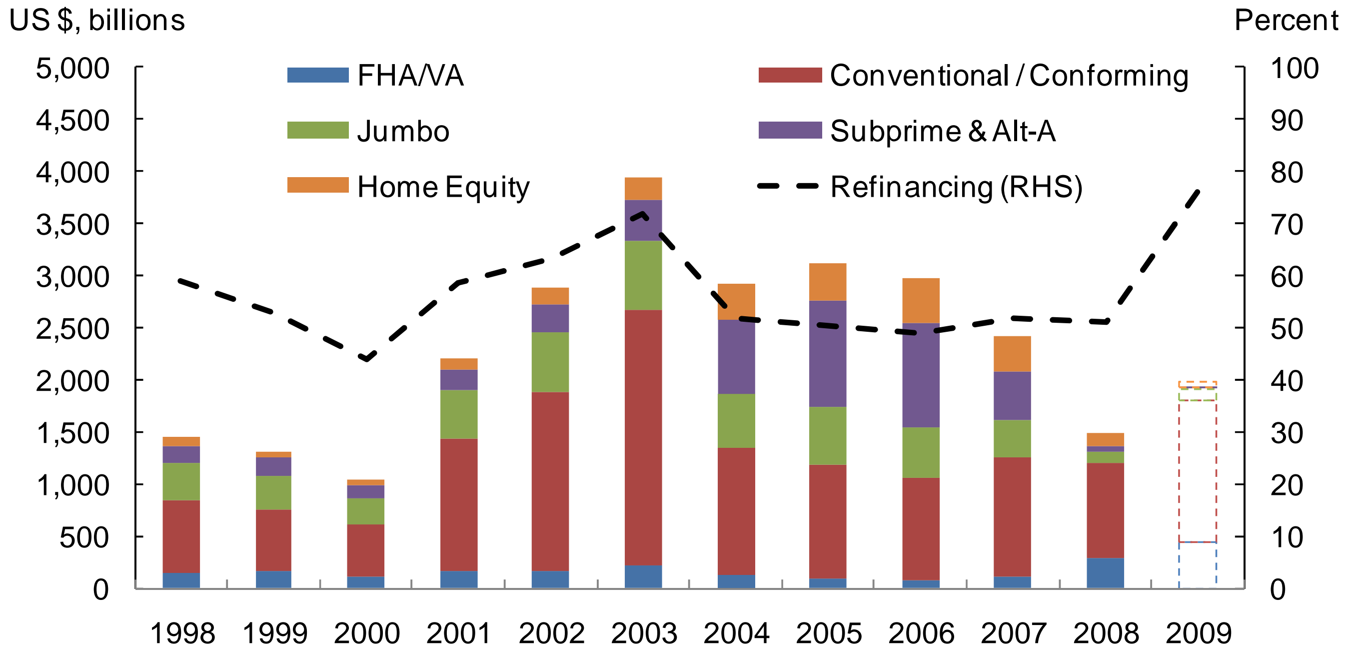
Indicators of Housing Markets

Figure 28: Mortgage Applications for Purchase and Refinancing (2005=100)



Note: Gray shading represents recessions. Source: Mortgage Bankers Association.

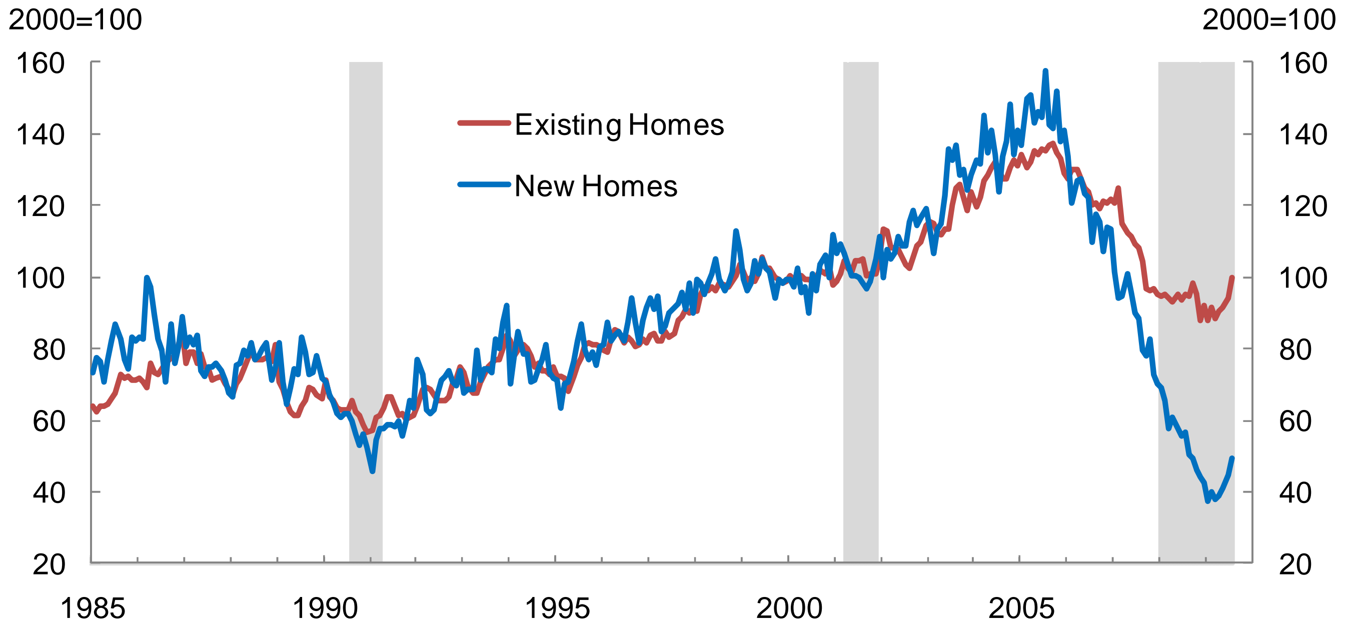
Figure 29: Mortgage Originations by Product (LHS) and Refinancing as a Share of Originations (RHS)



Note: 2009 estimates reflect annualized data from the first half of the year. Source: *Inside Mortgage Finance*.

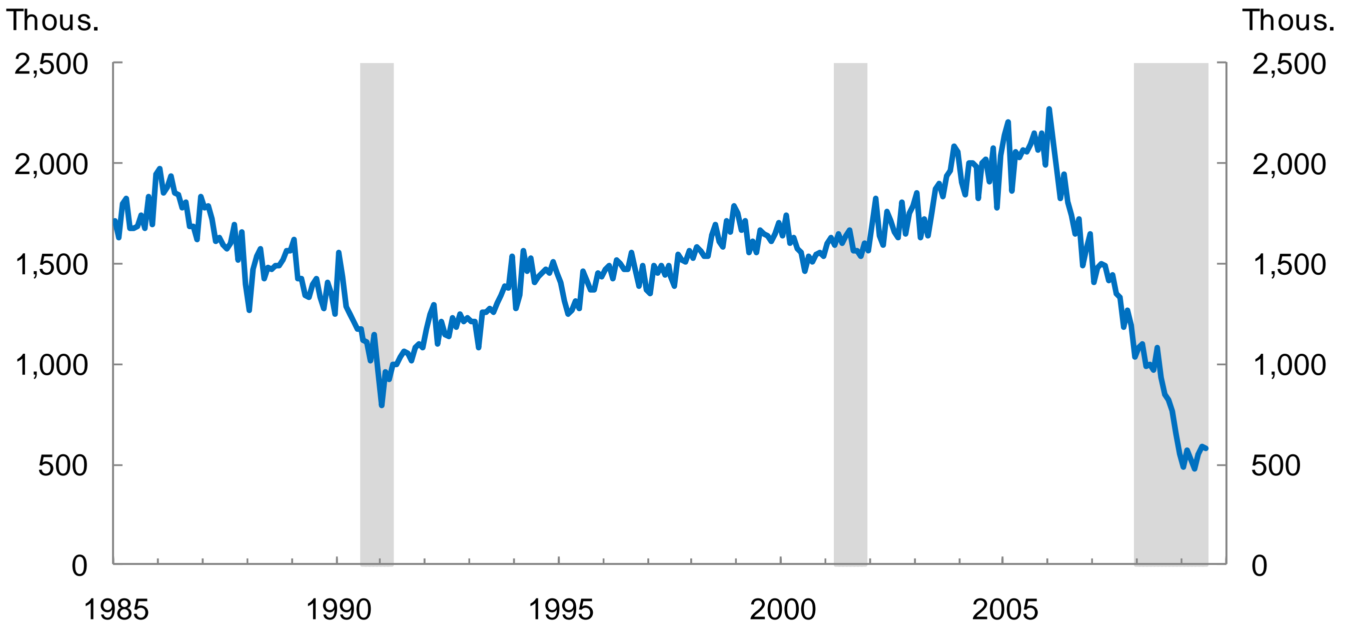
Indicators of Housing Markets (continued)

Figure 30: Sales of Single Family Homes, Existing and New (2000=100)



Note: Gray shading represents recessions. Source: Census Bureau.

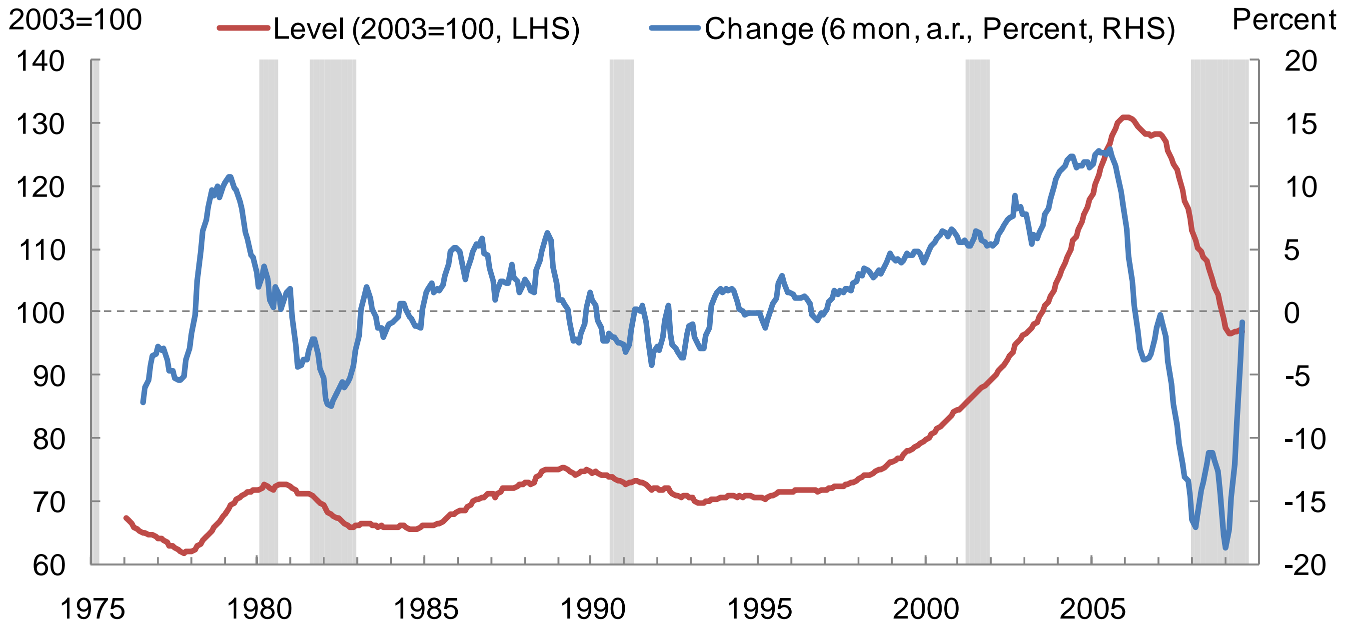
Figure 31: Housing Starts (Annual Rate, Thousands)



Note: Gray shading represents recessions. Source: Census Bureau.

Indicators of Housing Markets (continued)

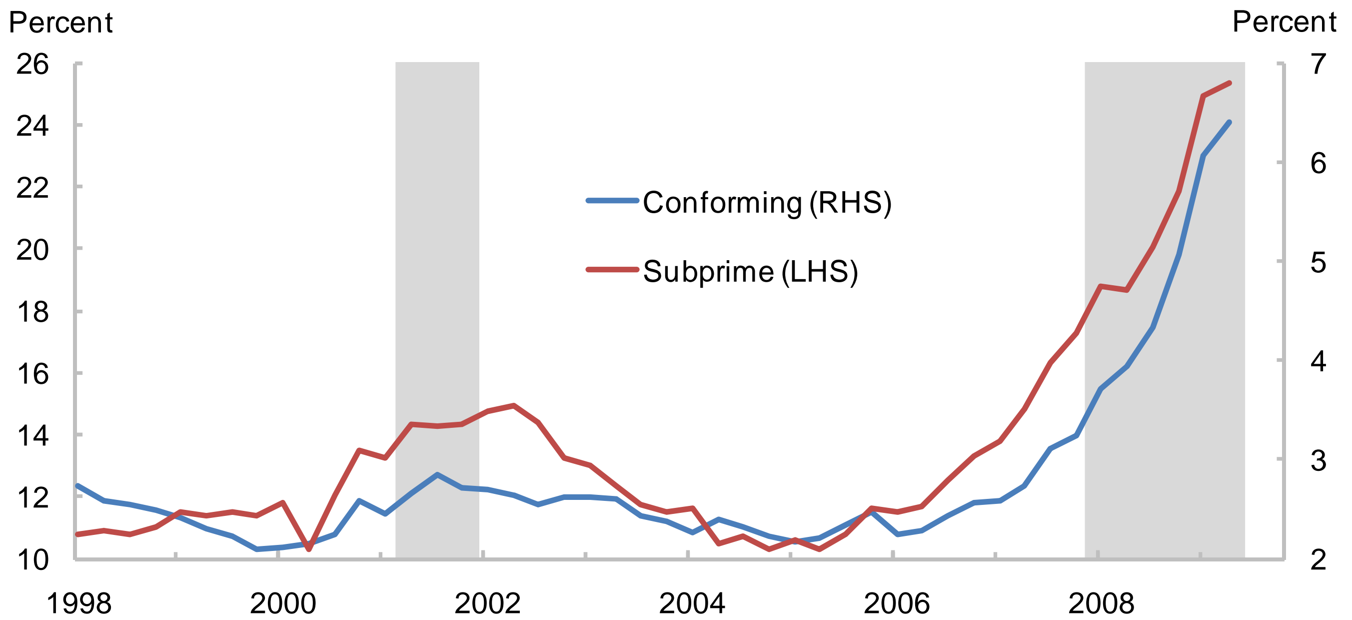
Figure 32: Real House Prices, Level and 6-mon. Change



Note: Deflated by core PCE prices.

Source: LoanPerformance; BEA.

Figure 33: Mortgage Delinquencies, Conforming and Subprime (Percent)



Source: Mortgage Bankers Association.

Appendix B

Extraordinary Financial Policy Initiatives
2008-2009

Section 1: TARP and Other Treasury Programs

- Capital Purchase Program (CPP)
- Supervisory Capital Assessment Program (SCAP): Stress Test
- Term Asset-Backed Securities Loan Facility (TALF)
- Legacy Securities Public-Private Investment Program (S-PPIP)
- Home Affordable Modification Program (HAMP)
- Exceptional Assistance: AIG and TIP
- Asset Guarantee Program (AGP)
- Automotive Industry Financing Program (AIGP)
- Money Market Mutual Fund Guarantee Program (MMMF)

Capital Purchase Program (CPP)

Description

Purpose: Treasury created the Capital Purchase Program (CPP) in October 2008 to stabilize the financial system by providing capital to viable financial institutions of all sizes. With a strengthened capital base market participants have greater confidence in both individual banks and the financial system as a whole. In addition, more capital gives banks an increased capacity to lend to U.S. businesses and consumers and to support the U.S. economy.

Details: Treasury provides capital to qualified financial institutions of all sizes by purchasing senior preferred equity or subordinated debentures. Treasury also receives warrants to purchase common equity, additional preferred shares, or additional subordinated debentures, allowing taxpayers to participate in the "upside" of an institution's recovery. Institutions may repay Treasury subject to terms of purchase agreements or the American Recovery and Reinvestment Act and after consultation with the appropriate regulator. Treasury may sell preferred shares, subordinated debentures, and warrants when market conditions stabilize. Participating institutions are subject to limitations on executive pay. Treasury is no longer accepting applications under the CPP except for small banks, defined as having total assets less than $500 million.

Number of Banks that Have Received CPP Investments

Total	672
Repaid to date[1]	38

[1] Including partial investments/repayments

Timeline

Oct. 14, 2008	Announced, nine large banks accept capital injections
Nov. 21, 2009	Last day for small banks to apply
Dec. 31, 2009	Deadline for new commitments

Taxpayer Protection – Structure

- Dividends at 5 percent per year for first 5 years; 9 percent per year thereafter
- S-corporations and some mutuals pay 7.7%, stepping up to 13.8% after 5 years
- Warrants to purchase common stock, preferred stock, or subordinated debentures

Utilization and Income

Commitments[2] Through CPP (US $, bn)

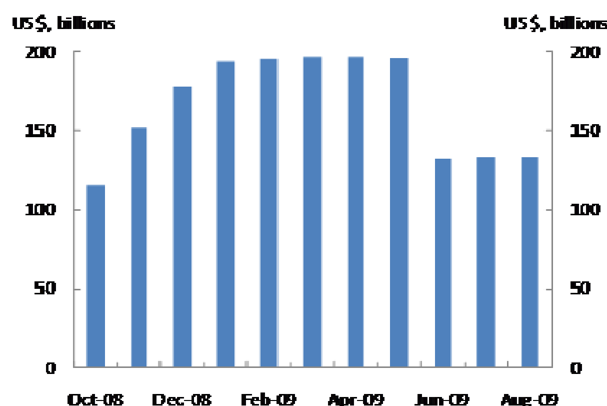
Current commitment	$134.1
Peak commitment	204.5
Announced limit	218.0

[2] "Commitment" is defined as net funds disbursed.

Cash Received Through CPP (US $, bn)

Dividends, interest, fees	$ 6.7
Principal repayments	70.4
Warrant proceeds	2.9
Total	80.0

Cumulative Net CPP Disbursements (US $, bn)



Termination

The Treasury Secretary's authority to purchase and to make and fund commitments to purchase preferred equity through CPP is scheduled to terminate on December 31, 2009. The Secretary may extend that authority to October 3, 2010.

Program details available at http://www.financialstability.gov/roadtostability/capitalpurchaseprogram.html.

Description

Purpose: The Federal Reserve, Office of the Comptroller of the Currency, and FDIC designed the Supervisory Capital Assessment Program (SCAP or "stress test") to perform a comprehensive, forward-looking assessment of the 19 largest U.S. bank holding companies. The goal was to allow supervisors and the market to judge whether these companies, which hold two-thirds of the assets in the U.S. banking system, had sufficient capital to withstand losses and sustain lending for households and businesses, even if the economic downturn is more severe than was anticipated in spring of 2009. While each company was encouraged to raise any needed capital from private investors, Treasury offered a backstop through the Capital Assistance Program (CAP) to ensure that each could meet its capital needs.

Details: Supervisors applied an historically high set of loss estimates on securities and loans, as well as a conservative view towards potential earnings that could act as a buffer against those losses. The stress test estimated that total losses in a deeper-than-expected recession would total nearly $600 billion, which would be partially offset by $363 billion in revenue and other non-capital resources available to absorb losses. While the stress test revealed that 10 of the 19 largest banks needed to increase their capital buffers by approximately $75 billion, the release of the results enabled U.S. banks to issue record amounts of common equity and to issue non-guaranteed debt for the first time in many months. Although Treasury has not funded any investments through CAP to date, the program increased market confidence that the federal government would provide capital support to the banking system if needed.

Participating Institutions

The 19 U.S. Bank Holding Companies with assets > $100 billion. These firms hold two-thirds of the assets and over half of the loans in the U.S. banking system.

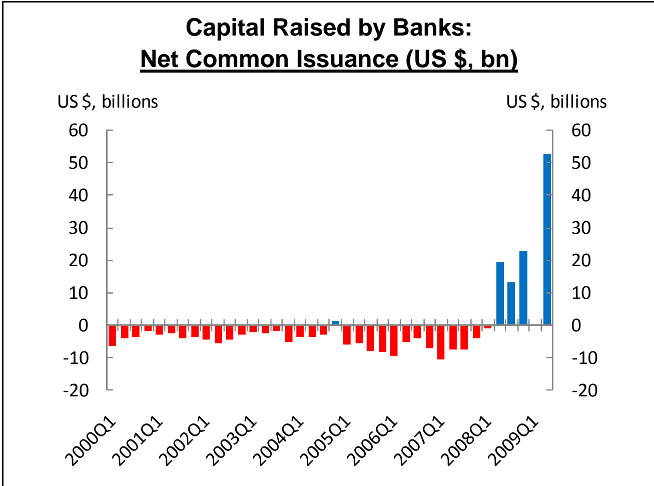
Stress Test Results (US $, bn)

Position on December 31, 2008	
Tier 1 Capital	*$ 837*
Risk Weighted Assets	*7,815*
Projections for 2009 and 2010 in Adverse Scenario	
Total Estimated Losses	*599*
Resources to Absorb Losses	*363*
Net Losses (Losses minus Resources)	*236*
Capital Buffer and Total Capital Needs	
Capital Buffer Needed	*185*
Less Prior Capital Raising	*110*
Total Capital Need	*75*

Timeline

Feb. 10, 2009	Stress test announced
Feb. 25, 2009	Publication of economic assumptions underlying the stress test
April 24, 2009	Publication of detailed stress test methodology
May 7, 2009	Stress test results released
June 8, 2009	Deadline for Bank Holding Companies to submit capital plans to regulators
Nov. 9, 2009	Deadline to implement capital plans and to apply for and fund transactions under CAP

Capital Raised by Banks: Net Common Issuance (US $, bn)



Term Asset-Backed Securities Loan Facility (TALF)

Description

Purpose: Treasury and the Federal Reserve announced the creation of the Term Asset-Backed Securities Loan Facility (TALF) in November 2008 to help market participants meet the credit needs of households and small businesses by supporting the issuance of asset-backed securities (ABS) collateralized by auto loans, student loans, credit card loans, equipment loans, floorplan loans, insurance premium finance loans, loans guaranteed by the Small Business Administration, residential mortgage servicing advances or commercial mortgage loans.

The ABS market had been under strain for some months. This strain accelerated in the third quarter of 2008, and the market came to a near-complete halt in October. At the same time, interest rate spreads on AAA-rated tranches of ABS rose to levels well outside the range of historical experience, reflecting unusually high risk premiums. The ABS markets historically have helped to fund a substantial share of credit to consumers and businesses. Continued disruption of these markets could significantly limit the availability of credit to households and businesses of all sizes and thereby contribute to further weakening of U.S. economic activity. The TALF is designed to increase credit availability and support economic activity by facilitating renewed issuance of consumer and business ABS at more normal interest rate spreads.

Details: Under the TALF, The Fed provides non-recourse funding to any eligible borrower owning eligible collateral. On fixed days each month, borrowers can request one or more three-year or, in certain cases, five-year TALF loans. If the borrower does not repay the loan, the Federal Reserve will enforce its rights to the collateral and sell the collateral to a special purpose vehicle (SPV) established specifically for the purpose of purchasing and managing such assets. Treasury provides a subordinated loan to the special purpose vehicle but does not directly provide loans to TALF borrowers.

TALF Activity Since March 2009 Launch[1]	
Total New Issuance ($ mln)	$79,657
Total TALF Loans Requested ($ mln)	$46,485
% Financed Through TALF	55%

[1] Through September 2009. September 2009 numbers are reported as pre-settled.

Timeline

Date	Event
Nov. 25, 2008	Announcement
Feb. 10 2009	Treasury's FSP Significantly Expands Potential Size
Mar. 03, 2009	Launch
Mar. 19, 2009	Expansion of eligible ABS assets
May 01, 2009	Expansion of eligible ABS assets and new issue CMBS
May 19, 2009	Expansion of TALF to include legacy CMBS
Aug 17, 2009	Extension of TALF for new issue ABS and legacy CMBS through March 31, 2010 and for new issue CMBS through June 30, 2010

Taxpayer Protection – Structure

- Investors are required to supply risk capital in the form of haircuts
- The TALF haircut methodology is risk sensitive across asset class and maturity
- The TALF accepts only collateral that has received two credit ratings in the highest investment-grade rating category or the principal and interest of which is fully U.S. government-guaranteed

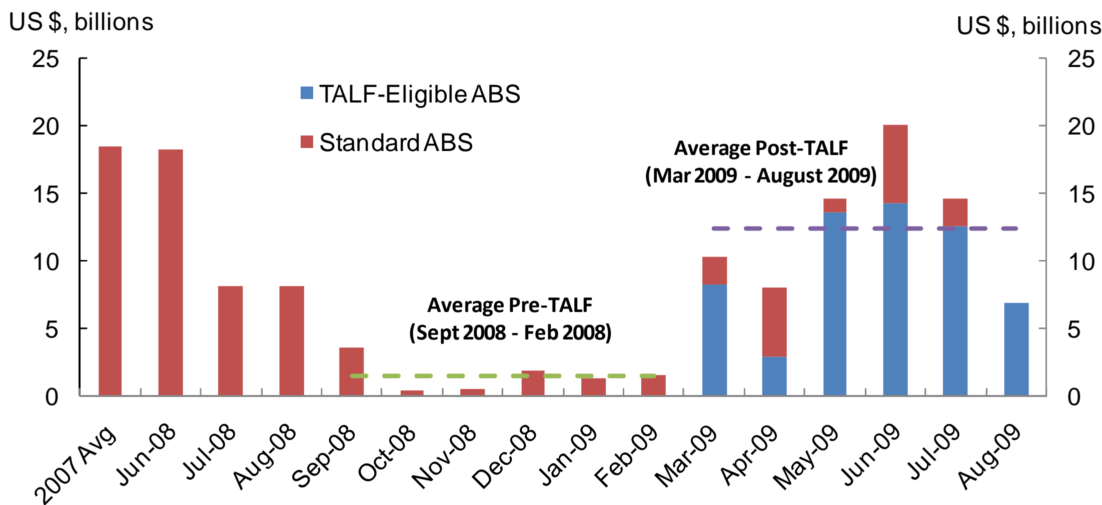
Utilization and Income

- As of Aug 31, 2009, $39.9 bn in TALF loans backed by ABS had been originated, $2.1 bn of TALF loans backed by legacy CMBS, and $0 of TALF loans backed by new issue CMBS.
- As of Aug 31, 2009 the average "haircut" was approximately 8.2% of the originated balance.
- As of Aug 31, 2009, all TALF loans are performing as expected

Treasury Credit Support to TALF (US $, bn)

Obligations to date	$20.0
Disbursements to date	0.1

Consumer ABS Issuance (US $, billions)



Source: Markets Room, U.S. Treasury Department (08/31/09)

Secondary Market ABS Spreads Relative to Benchmark

Source: Markets Group, Federal Reserve Bank of New York (09/08/09). Benchmark rates are LIBOR, for Credit Card and Student Loan; Swaps for Auto.

Termination

To promote the flow of credit to businesses and households and to facilitate the financing of commercial properties, the Federal Reserve and Treasury recently extended TALF into 2010. The facility will cease making loans collateralized by newly-issued CMBS on June 30, 2010, and loans collateralized by all other types of TALF-eligible newly-issued ABS and legacy CMBS on March 31, 2010. The Federal Reserve and Treasury have the authority to extend the program further.

Program details available at http://www.newyorkfed.org/markets/talf.html.

Legacy Securities Public-Private Investment Program (S-PPIP)

Description

Purpose: The Legacy Securities Public-Private Investment Program (S-PPIP) is part of the broader Financial Stability Plan, announced in February 2009, which outlined a framework to bring capital into the financial system and address the problem of legacy real estate-related assets. S-PPIP is designed to support market functioning and facilitate price discovery in the asset-backed securities markets, allowing banks and other financial institutions to re-deploy capital and extend new credit to households and businesses. S-PPIP will participate in the market for legacy commercial mortgage-backed securities and non-agency residential mortgage-backed securities.

Details: Under S-PPIP, Treasury will invest up to $30 billion of equity and debt in Public-Private Investment Funds (PPIF). Following a comprehensive two-month application evaluation and selection process, during which over 100 unique applications to participate in S-PPIP were received, Treasury has pre-qualified nine fund managers to participate. Each pre-qualified S-PPIP fund manager will have up to 12 weeks to raise at least $500 million of capital from private investors for the PPIF. The equity capital raised from private investors will be matched by Treasury. Upon raising this private capital, pre-qualified Legacy Securities PPIP fund managers can begin purchasing assets.

S-PPIP Participants

Pre-qualified fund managers	9
Minority partnerships[1]	10

[1] Selected by fund managers

Timeline

Mar. 23, 2009	Program announced
Apr. 24, 2009	Application deadline
Jul. 8, 2009	9 pre-qualified fund managers announced
Late September	Target closings

Taxpayer Protection – Structure

- Treasury S-PPIP compliance regime
- Minimum asset coverage covenant to protect Treasury debt investment
- Minimum $20 million fund manager equity co-investment to align incentives

Utilization and Income

Commitments[2] Through S-PPIP (US $, bn)

Current commitment	$ -[3]
Peak commitment	30.0[4]
Announced limit	75 - 100.0[5]

Cash Received Through S-PPIP (US $, bn)[6]

Dividends, interest, fees	$ -
Return of capital	-
Warrant proceeds	-
Total	-

[2] Commitment is defined as net funds disbursed to date.

[3] Closings (and legal commitments) expected to occur in late September.

[4] Up to $30bn of Treasury matching equity and debt can be committed.

[5] Represents TARP allocation to Legacy Asset Program, which also includes the Legacy Loans Program and Legacy TALF.

[6] Fund closings expected in late September.

Termination

Investment period is three years and fund life is eight years with two one-year extensions, subject to Treasury approval. Treasury can unilaterally terminate the investment period and the requirement to fund additional capital after one year.

Program details available at http://www.financialstability.gov/roadtostability/publicprivatefund.html.

Assistance for Homeowners

Description

Purpose: The Administration, in conjunction with the Federal Reserve and Congress, has launched several initiatives designed to support housing markets by expanding the supply of mortgage credit, providing direct aid to home buyers, and preventing avoidable foreclosures. These policies are being implemented through three main channels: (1) support provided through Government Sponsored Enterprises (GSEs), including Fannie Mae and Freddie Mac; (2) assistance authorized by the American Recovery and Reinvestment Act (ARRA); and (3) Making Home Affordable Program.

Support for GSEs

- Fannie Mae and Freddie Mac play a central role in providing mortgage credit. They buy home mortgages from original lenders, repackage them as mortgage-backed securities (MBSs), and either sell them--with a guarantee of payment--or hold them in their own portfolio. In 2008, Fannie and Freddie owned or guaranteed about half of the $12 trillion U.S. mortgage market.
- Actions
  - On September 7, 2008, pursuant to the Housing and Economic Recovery Act of 2008, the Federal Housing Finance Agency (FHFA) placed Fannie Mae and Freddie Mac into conservatorship. At the same time, Treasury purchased preferred equity in the companies to ensure that they have sufficient capital in the face of rising losses. Absent these interventions, doubts about the GSEs could have caused severe disruptions in financial markets, made home mortgages more expensive to obtain, and had negative repercussions throughout the U.S. economy.
  - In addition, Treasury and the Federal Reserve have been purchasing MBS guaranteed by Fannie and Freddie, and the Federal Reserve has also been purchasing their debt. Treasury and the Federal Reserve also established secured credit lines for the GSEs.
- Impact
  - The above actions have supported low mortgage rates by strengthening confidence in Freddie and Fannie. Each 0.5 percent reduction in mortgage interest rate saves the median home purchaser $600 per year in mortgage payments. The spread between GSE debt and Treasury Securities has decreased from a peak of 2.5 percent to less than 1 percent today.

ARRA Assistance

- ARRA (1) raised the limits for GSE loans from a previous maximum of $625,500 per loan to $729,750, thus supporting conforming loans in high-cost markets; (2) implemented an $8,000 first-time home buyer credit; (3) expanded Neighborhood Stabilization grants; and (4) created the Tax-Credit Assistance Program (TCAP) and the Low Income Housing Tax Credit Exchange.

Making Home Affordable Program

- Announced on February 18, Making Home Affordable Program (MHA) offers assistance to millions of homeowners by reducing mortgage payments and preventing avoidable foreclosures.
- MHA gives homeowners the opportunity to refinance GSE loans to lower monthly payments. This program, plus lower mortgages rates, has contributed to over 2.7 million mortgage refinancings since the program was announced. MHA also provides a modification option for up to 3-4 million at-risk homeowners, i.e., Home Affordable Modification Program (HAMP).

Program details available at http://www.financialstability.gov/roadtostability/homeowner.html.

HAMP Details: Using TARP funds, Treasury provides incentives for mortgage servicers, borrowers and investors to modify loans that are delinquent or at imminent risk of default to an affordable monthly payment equal to 31 percent of a borrower's gross monthly income. Borrowers must be owner occupants and demonstrate an ability to support the reduced payment during a three-month trial period before the modification becomes permanent. HAMP includes a modification option for second lien mortgage loans and additional incentives for foreclosure alternatives if modification of the loan is not viable.

Number of Servicers Participating	
Mortgage servicers	47

Number of Trial Modifications Started	
Trial Modifications Started (as of 8/31/2009)	360,165

HAMP Timeline

Feb. 18, 2009	Announced
Mar. 4, 2009	Issued basic program guidance
April 6, 2009	Issued detailed program guidance and participation contracts
	April 28 – Announced Second Lien Program
	May 6 – Announced Foreclosure Alternatives Program
	July 28 – Treasury Meeting with Servicer Executives

HAMP Taxpayer Protection

- Incentives paid only for successful modifications.
- Program Compliance performed by Freddie Mac as Treasury's compliance agent.
- Transparency through public reporting on a servicer-by-servicer basis.
- Operational metrics to measure servicer performance on implementation.

HAMP Utilization

Commitments[2] Under HAMP Program (US $, bn)

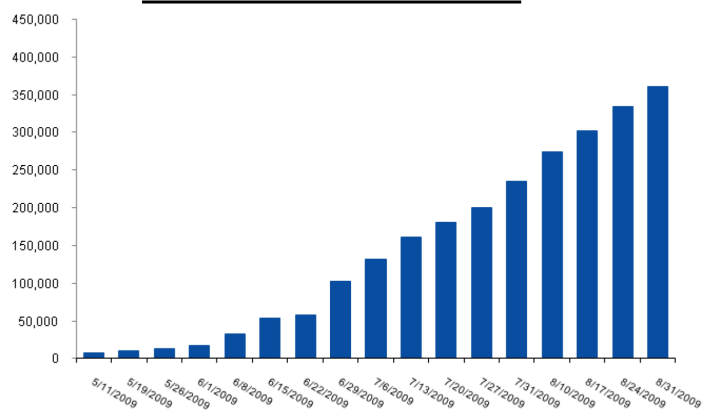
Current commitment	$22.1
Announced limit	50.0

[2] "Commitment" is defined as net funds obligated.

Issuance Under HAMP Program (US $, mn)

Aug. 2009	$0.3

HAMP Trial Modifications Started



HAMP Termination

Servicers must enter into the program agreements with Fannie Mae, which is Treasury's financial agent for the program, on or before December 31, 2009. Borrowers may be accepted into the program if a fully executed Home Affordable Modification Trial Period Plan is in the related servicer's possession on or before December 31, 2012. Modifications will continue for 5 years from starting date of modification, and incentive payments will continue to be paid out over that period.

Description

Treasury has provided exceptional financial assistance on a case-by-case basis in order to stabilize key financial institutions. Such assistance was provided to prevent broader disruption of the financial markets. Treasury has provided this assistance by purchasing preferred shares of the institutions. As part of those transactions, Treasury has also received warrants to purchase common shares of the institutions[6]. Assistance has been provided to AIG, as well as to Citigroup and Bank of America through the Targeted Investment Program (TIP).

- **AIG** – In November 2008, Treasury purchased $40 billion in cumulative preferred shares from AIG. In April 2009, it exchanged those cumulative preferred shares for $41.6 billion in non-cumulative preferred shares and also created an equity capital facility, under which AIG may draw up to $29.8 billion as needed. The Federal Reserve also provided loans to AIG. In connection with such loans, the FRBNY received convertible preferred shares representing approximately 79.8% of the current voting power of the AIG common shares. These preferred shares were deposited in a trust, which exists for the benefit of the U.S. taxpayers.
- **TIP** – Under the TIP, Treasury purchased $20 billion in preferred stock from Citigroup, Inc. and $20 billion in preferred stock from Bank of America Corporation. These investments were incremental to CPP investments in these institutions. As part of an exchange offer designed to strengthen Citigroup's capital, Treasury recently exchanged all its preferred shares in Citigroup for a combination of common shares and trust preferred securities.

Timeline

Date	Event
Nov. 25, 2008	Treasury purchases $40bn in preferred shares from AIG
Dec. 31, 2008	Treasury purchases $20bn in preferred stock in CItigroup
Jan. 16, 2009	Treasury purchases $20bn in preferred stock in Bank of America
Mar. 2, 2009	Treasury and the FRBNY announce plans to restructure assistance to AIG, including creation of equity capital facility

Taxpayer Protection – Structure

- Preferred equity
- Dividends
  - AIG: Non-cumulative dividends at 10 percent per year
  - TIP: Cumulative dividends at 8 percent per year
- Warrants to purchase common stock
- Directors
  - AIG: Treasury gains ability to appoint 2 directors if dividends on its preferred shares aren't declared for four quarters

Utilization and Income

Recipient	Current Obligation (US$, bn)	Disbursed (US$, bn)
AIG	$69.8	$43.2
Bank of America	20.0	20.0
Citigroup	20.0	20.0
Total	$109.8	$83.2

Cash Received (US$, bn)	
Dividends, interest, fees	$ 1.9
Principal repayments	0.0
Warrant proceeds	0.0
Total	$ 1.9

Termination

The Treasury Secretary's authority to purchase and to make and fund further commitments to purchase preferred equity through Exceptional Assistance is scheduled to terminate on December 31, 2009. The Secretary may extend that authority to October 3, 2010[7].

[6] Under certain circumstances, the AIG warrants are exchangeable for preferred stock.

[7] Note that AIG can continue to draw on the equity capital facility until April 17, 2014 as long as it still meets certain conditions.

Description

Purpose: Treasury created the Asset Guarantee Program in November 2008 to stabilize the financial system by providing guarantees against unexpectedly large credit losses on certain assets held by qualifying financial institutions on their balance sheet. The program was designed for financial institutions whose failure could harm the financial system and has been used in conjunction with other forms of exceptional assistance.

Citigroup: Treasury has guaranteed up to $5 billion of potential (realized) losses incurred on a $301 billion pool of loans, mortgage-backed securities, and other financial assets held by Citigroup (Citi). Treasury does not become obligated to pay on its guarantee unless and until Citi has absorbed the first $39.5 billion of losses on the covered pool. Treasury covers $5 billion of the next loss, with Citi covering an additional $0.55 billion. The FDIC guarantees the next $10 billion in losses, and Citi covers an additional $1.1 billion. The Federal Reserve would then provide a secured loan equal to 90 percent of the remaining value in the pool and collateralized by those assets, with Citi covering other losses.

Bank of America: In January 2009, Treasury, the Federal Reserve and the FDIC agreed to share potential losses on a $118 billion pool of financial instruments owned by Bank of America, consisting of securities backed by residential and commercial real estate loans, and corporate debt and derivative transactions that reference such securities, loans and associated hedges. However, Bank of America has stated that it does not intend to use the guarantee, and no final documentation has been entered into.

Timeline

Date	Event
Nov. 22, 2008	Announced Citigroup AGP
Jan. 15, 2009	Citigroup AGP transaction closes
Jan. 16, 2009	Bank of America AGP transaction announced

Taxpayer Protection – Structure

- Treasury and FDIC received approximately $7 billion in Citi preferred equity, plus warrants to purchase Citi common stock
- Dividends at 8 percent per year
- Federal Reserve loan would be at OIS+300 bp

Utilization and Income

Commitments Through AGP (US $, bn)	
Treasury commitment	$ 5.0
FDIC commitment	10.0
Federal Reserve commitment	221.0

Cash Received Through AGP (US $, bn)	
Dividends, interest, fees	$ 0.2
Principal repayments	0.0
Warrant proceeds	0.0
Total	0.2

Termination

Treasury's obligations to make any loss coverage payments to Citi under the AGP terminates in 2013 for non-residential assets and in 2018 for residential assets, or upon mutual agreement by Citigroup, Treasury, Federal Reserve, and FDIC.

Automotive Industry Financing Program (AIFP)

Description

Purpose: Treasury created the Automotive Industry Financing Program (AIFP) in December 2008 to prevent a significant disruption of the U.S. automotive industry, because the potential for such a disruption posed a systemic risk to financial market stability and would have had a negative effect on the economy. AIFP loans have helped to enable General Motors and Chrysler to go through orderly bankruptcies and emerge as more viable companies.

Details: Treasury has provided approximately $76 billion in loans and equity investments to General Motors, GMAC, Chrysler, and Chrysler Financial. Short-term funding was initially provided to GM and Chrysler on the condition that they develop plans to achieve long-term viability. In cooperation with the Administration, GM and Chrysler eventually developed satisfactory viability plans and underwent speedy restructurings: Chrysler's business was restructured through the bankruptcy process in 42 days, and GM's bankruptcy restructuring process lasted 40 days. Treasury provided additional assistance during the respective periods.

Number of Participants

Total	4
Repaid to date[1]	1

[1] Chrysler Financial

Timeline

Dec. 19, 2008	Announced, GM and Chrysler participate
Dec. 29, 2008	GMAC participates
Jan. 16, 2009	Chrysler Financial participates
Dec. 31, 2009	Deadline for new commitments

Taxpayer Protection – Structure

- Bank loans, preferred equity, voting common equity
- GM and Chrysler bank loan interest at L+300 to L+790; GMAC dividends at 8% to 9%
- Ability to appoint directors to boards of GM and GMAC

Utilization and Income

Commitments[2] Through AIFP (US $ bn)

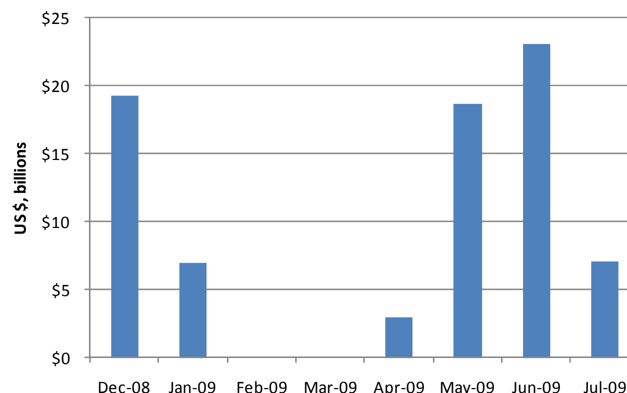
Current commitment	$81.1
Peak commitment	85.0
Current net disbursements	73.8
Announced limit	N/A

[2] "Commitment" is defined as net funds disbursed.

Cash Received Through AIFP (US $ bn)

Dividends, interest, fees	$ 0.6
Principal repayments	2.1
Warrant proceeds	0.2
Total	3.0

Cumulative Net AIFP Disbursements (US $ bn)



Termination

The Treasury Secretary's authority to purchase and to make and fund commitments to purchase securities through AIFP is scheduled to terminate on December 31, 2009. The Secretary may extend that authority to October 3, 2010.

Money Market Mutual Fund Guarantee Program

Description

Purpose: Treasury created the Money Market Mutual Fund (MMMF) Guarantee Program in September 2008 to stop a run on money market mutual funds in the wake of the failure of Lehman Brothers. These funds are an important investment vehicle for many Americans and a fundamental source of financing for our capital markets and financial institutions. Maintaining confidence in the money market mutual fund industry is critical to protecting the integrity and stability of the global financial system. The program enhances market confidence by alleviating investors' concerns about the ability of money market mutual funds to absorb losses.

Number of Participating Series/Classes of Funds	
Total	1,486

Details: Treasury guarantees the share price of any publicly-offered eligible money market mutual fund – both retail and institutional – that applied for and pays a fee to participate in the program. The guarantee will be triggered if a participating fund's net asset value falls below $0.995, commonly referred to as "breaking the buck." While the program protects the accounts of investors, each money market fund made the decision of whether to sign-up for the program. The guarantee covers shareholders of record as of September 19, 2008, up to the shareholder's balance as of that date. The program is supported by fees from participating funds and by the Exchange Stabilization Fund.

Timeline

Sep. 19, 2008	Announced
Nov. 24, 2008	First extension through Apr. 30, 2009
Mar. 31, 2009	Second extension through Sep. 18, 2009
Sep. 18, 2009	Guarantee terminates

Taxpayer Protection – Structure

- Annualized fee of 4-6 basis points of the fund's asset base

Utilization and Income

Commitments[2] Through MMMF (US $, bn)

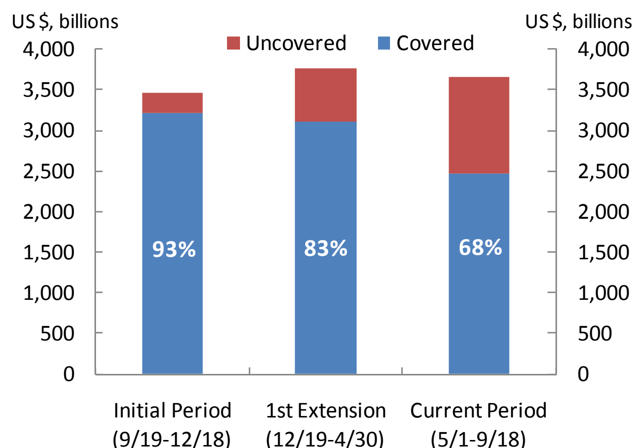
Current commitment	$2,470.0
Peak commitment	3,217.4
Announced limit[3]	3,655.8

[2] "Commitment" is defined as net funds disbursed.
[3] The current value of total assets in eligible funds.

Cash Received Through MMMF (US $, bn)

Total	$ 1.2

Money Market Mutual Fund Assets Covered by Treasury Guarantee (US, bn)



Termination

The program terminates on September 18, 2009, and may not be extended under its current funding structure.

Program details available at http://www.treas.gov/offices/domestic-finance/key-initiatives/money-market-fund.shtml.

Section 2: FDIC Programs

- Temporary Liquidity Guarantee Program (TLGP): Debt Guarantee
- Temporary Liquidity Guarantee Program (TLGP): Transaction Account

Temporary Liquidity Guarantee Program (TLGP): Debt

Description

Purpose: FDIC created the Temporary Liquidity Guarantee Program (TLGP) for debt to strengthen confidence and encourage liquidity in the banking system by guaranteeing newly-issued senior unsecured debt of banks, thrifts, and certain holding companies.

Details: FDIC guarantees senior debt issued by eligible institutions between October 14, 2008 and October 31, 2009. Eligible debt must have a stated maturity of more than 30 days and may include, for example, commercial paper and unsubordinated unsecured notes. The program is funded through special fees, not taxpayer funding. More than half all eligible entities opted into the program.

Number of Institutions Currently Participating	
Depository institutions with assets <= $10 billion	44
Depository institutions with assets > $10 billion	20
Bank and thrift holding companies, and others	33

Timeline

Oct. 14, 2008	Announced
Jun. 3, 2009	Deadlines extended for issuance and guarantee
Oct. 31, 2009	Last day to issue new debt
Dec. 31, 2012	Guarantee expires

Taxpayer Protection – Structure

- Fee ranges from 50 to 100 basis points depending on maturity
- Additional 10 basis points for certain issuers, including bank holding companies
- For debt issued after April 1, 2009, 25 basis point surcharge if issued by insured depository institution; 50 basis point surcharge for others

Utilization and Income

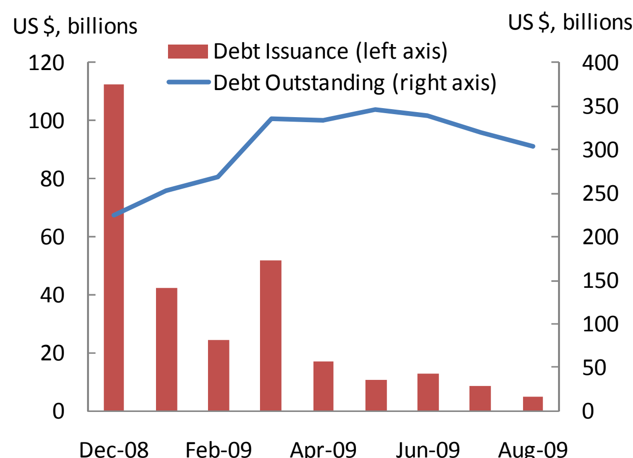
Commitments[2] Under TLGP Debt Program (US $, bn)	
Current commitment	$304.1
Peak commitment	350.0
Announced limit	788.9

[2] "Commitment" is defined as outstanding debt guaranteed.

Issuance Under TLGP Debt Program (US $, bn)	
Dec. 2008	$112.6
Aug. 2009	5.0

Cash Received Under TLGP Debt Program (US $, bn)	
Total	$9.4

TLGP Issuance and Outstanding Debt (US $, bn)



Termination

The last day to issue debt under the program is currently October 31, 2009, and the guarantee currently expires December 31, 2012. The FDIC recently reaffirmed its intentions in this regard and is seeking comment on whether a temporary emergency facility should be left in place for six months after the expiration of the current program at a substantially higher fee.

Temporary Liquidity Guarantee Program (TLGP): Transaction Accounts

Description

Purpose: FDIC created the Temporary Liquidity Guarantee Program (TLGP) for transaction accounts to strengthen confidence and encourage liquidity in the banking system by providing full coverage of non-interest bearing deposit transaction accounts.

Details: FDIC provides participating depository institutions with full deposit insurance coverage for non-interest bearing deposit transaction accounts, regardless of dollar amount. These are mainly payment-processing accounts, such as payroll accounts used by businesses. Frequently, these exceed the current maximum limit of $250,000. The program is funded through special fees, not taxpayer funding. Nearly 87 percent of depository institutions are participating in the program.

Percentage of Institutions Currently Participating

Depository institutions with assets <= $10 billion	87%
Depository institutions with assets > $10 billion	93
Total depository institutions	*87*

Timeline

Oct. 14, 2008	Announced
Aug. 27, 2009	Deadline extended for guarantee
Jun. 30, 2010	Guarantee expires

Taxpayer Protection – Structure

- Fee is 10 basis points annually through Dec. 31, 2009
- From Jan. 1, 2010 through Jun. 30, 2010, annualized fee ranges between 15-25 basis points, depending on institution's risk category

Utilization and Income

Commitment[2] Under TLGP Transaction Account Program (US $, bn)

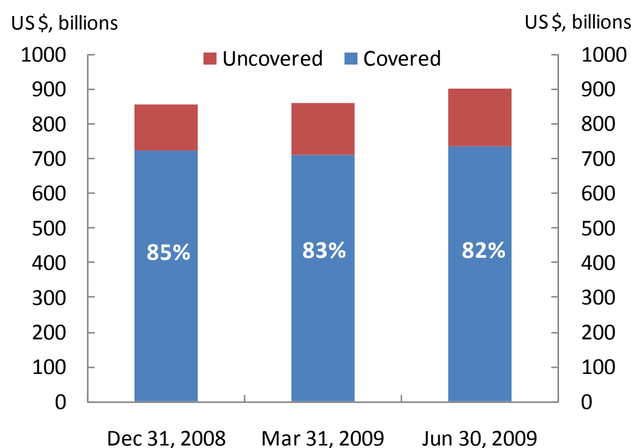
Current commitment	$736.1

[2] "Commitment" is defined as account balances guaranteed.

Fees Received Under TLGP Transaction Account Program (US $, bn)

Total	$0.3

Amount in Transaction Accounts Over $250,000 (US $, bn)



Termination

A final rule extending the Transaction Account Guarantee component of the TLGP by six months, to June 30, 2010, was adopted on August 26, 2009. Depository institutions that remain in the extended program will be subject to increased fees that are adjusted to reflect the institution's risk. The FDIC has the authority to extend the program further.

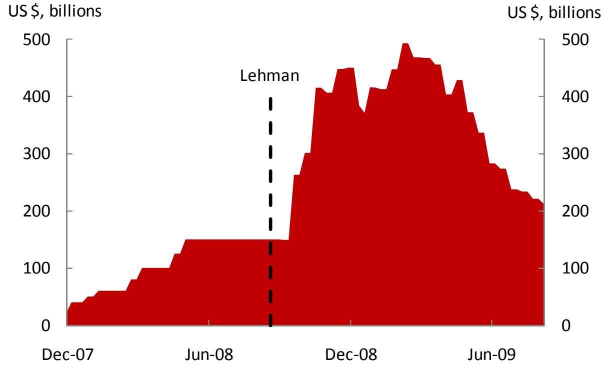
Program details available at http://www.fdic.gov/regulations/resources/tlgp/index.html.

Section 3: Federal Reserve Programs

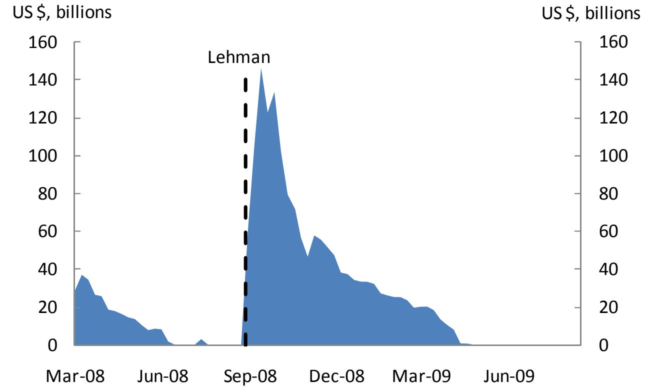
- The Federal Reserve provides details on the new policy tools that it has implemented since the summer of 2007 to foster market liquidity and financial stability in the *Federal Reserve System Monthly Report on Credit and Liquidity Programs and the Balance Sheet*, which is available at www.federalreserve.gov/monetarypolicy/bst.htm.
- In the context of the above discussion regarding the next phase of financial stabilization and rehabilitation, the report explains that continued improvements in financial market conditions have been accompanied by further declines in credit extended through many of the Federal Reserve's liquidity programs.
    - Credit provided to depository institutions through the discount window and the Term Auction Facility (TAF) has continued to decline, primarily reflecting reductions in loans outstanding under the TAF. Combined credit outstanding through these facilities has fallen from a peak of $560 billion in March to $251 billion currently.
    - Borrowing at the Term Securities Lending Facility (TSLF) has stopped as a result of further improvement in the conditions in money markets. There has been no borrowing at the Primary Dealer Credit Facility (PDCF) since mid-May. Credit outstanding under the PDCF peaked at $147 billion in October 2008.
    - The amount of commercial paper held in the Commercial Paper Funding Facility (CPFF) has recently declined considerably, as improvements in market conditions have allowed some borrowers to obtain financing from private investors in the commercial paper market or from other sources. At its peak, credit outstanding under the CPFF was $351 billion. Currently, it stands at $48 billion.
    - Dollar credit extended to foreign central banks under liquidity swaps to facilitate their efforts to address pressures in dollar funding markets has declined sharply over recent months as global financial conditions have improved and short-term funding pressures have receded. Credit extended through liquidity swaps with other central banks has dropped from a peak of about $580 billion to $63 billion.
    - Although credit extended under the liquidity programs has declined, the Federal Reserve recently extended deadlines for many of the programs to February 1, 2010, to provide a backstop while financial market conditions remain somewhat fragile.
- All loans under Federal Reserve liquidity programs are fully collateralized.
- The Federal Reserve continues to support key channels of credit, increasing its lending under the Term Asset-Backed Securities Loan Facility (TALF). To help reduce the cost and increase the availability of credit for the purchase of houses, the Federal Reserve continues to purchase direct obligations of Fannie Mae, Freddie Mac, and the Federal Home Loan Banks and mortgage-backed securities guaranteed by Fannie Mae, Freddie Mac, and Ginnie Mae.

Federal Reserve Liquidity Programs and Asset Purchases

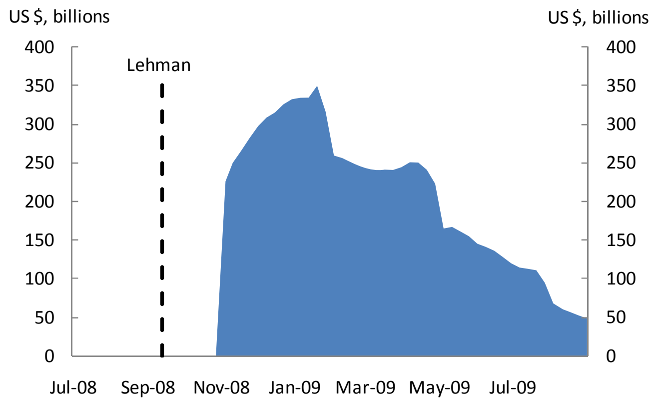
TAF Credit Outstanding (US $, bn)



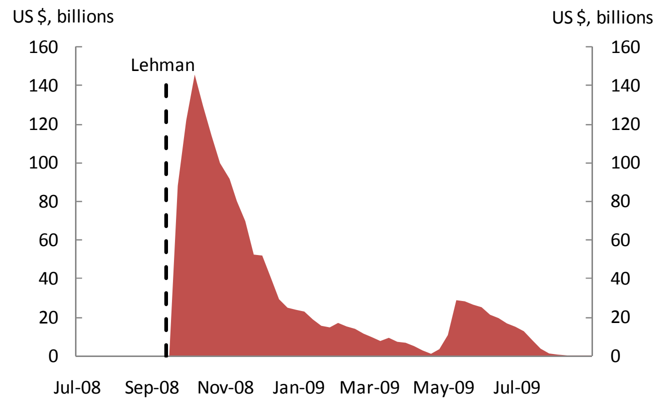
Credit Outstanding Through the PDCF (US $, bn)



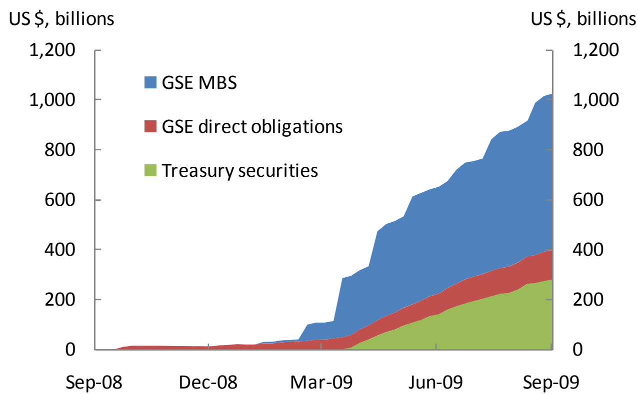
Net Portfolio Holdings of CPFF (US $, bn)



Credit Outstanding Through the AMLF (US $, bn)



Net Purchases of Agency and Treasury Securities (US $, bn)



Credit Extended to AIG Under Revolving Credit Line (US $, bn)