



Federal Reserve Bank of St. Louis

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James Bullard
President and Chief Executive Officer
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February 23, 2010

The Honorable Evan Bayh
United States Senator, Indiana
131 Russell Senate Office Building
Washington, DC 20510

The Honorable Jim Bunning
United States Senator, Kentucky
316 Hart Senate Office Building
Washington, DC 20510

The Honorable Bob Corker
United States Senator, Tennessee
185 Dirksen Senate Office Building
Washington, DC 20510

Dear Senators Bayh, Bunning and Corker:

The financial markets of the United States have seen considerable improvement over the past 18 months. This improvement is due in large part to actions taken by the Federal Reserve to avert a complete financial collapse, which would have had dire consequences for employment and economic growth. The Federal Reserve's ability to deal effectively with this crisis is directly attributable to the expertise and information that it acquires as a supervisor of banks and bank holding companies. It is now my understanding that the Senate Banking Committee may be considering legislation that would remove the Federal Reserve from the supervisory process.

The Federal Reserve's involvement in the supervision of both large and small banks arms it with the information and knowledge needed to carry out its role as lender of last resort, a role that is mandated by Congress. A testimonial to how this involvement can pay off is the successful and innovative lending programs the Fed implemented in the fall of 2008. Our experience in the supervisory process was also vital in getting the Term Auction Facility (TAF), up and running within weeks in late 2007. Since the implementation of TAF, the Federal Reserve has extended more than \$3.5 trillion in secured short-term credit to provide liquidity to healthy institutions. I am quite confident that we would have seen more liquidity failures, including failures of mid-sized financial institutions, had the Fed not been able to respond so quickly.

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The link between supervisory knowledge and financial stability was also evident in the Fed's response to the devastating crisis of Sept. 11, 2001. Had the Fed not fully understood all of the vital components of the payments system and the linkage to financial institutions, the system would have locked up, threatening U.S. and global financial stability. Our hands-on knowledge allowed us to push liquidity where it was needed so that payments were settled by day's end. Both large and small banks benefited.

Some suggest that the Federal Reserve could rely on information provided by other supervisors to carry out its role in financial stability. My primary concern with this idea is simple: In a financial crisis, there is no time to acquire information from other sources. Moreover, there could be a question as to the reliability of information acquired elsewhere, possibly leading to hesitancy in accepting the data, which would further delay needed action. If another regulator did not provide the Fed with complete and timely information, the Fed might risk lending to a troubled institution. In its 97 years, the Fed has never lost money on discount window loans or, more recently, its Term Auction Facility. Why introduce incentives now that would expose the Fed to risks akin to those of a subprime lender?

A critical function in any modern economy is to have a central bank that can effectively and independently help stabilize financial markets in times of turmoil by carrying out its role as a lender of last resort. Removing bank supervision authority from the Federal Reserve would, in my view, adversely impact this effectiveness. As the president of the Minneapolis Federal Reserve Bank, Narayana Kocherlakota, recently said, "Stripping the Federal Reserve of its supervisory role would needlessly put a Great Depression on the menu of possibilities for our country."

Sincerely,

A handwritten signature in dark ink, appearing to read "J. Bullard". The signature is fluid and cursive, with a large initial "J" and "B".

James Bullard
President

cc: Eighth District Senators
Eighth District Directors
Eighth District State Banking Associations
Eighth District State Banking Commissioners