Fed Brief

18 March 2020

Another crisis-era program returns: Primary Dealer Credit Facility

Late Tuesday, on 17 March and after the close of most financial markets in the United States, the Federal Reserve announced the creation of the Primary Dealer Credit Facility (PDCF) effective 20 March. This reprises a step taken during the financial crisis in 2008 (as did an earlier announcement of the Commercial Paper Funding Facility (CPFF)). With the PDCF, the Federal Reserve will make collateralized loans up to 90 days to primary dealers of the Federal Reserve Bank of New York, at a rate equal to the primary credit rate (the "discount rate"), which is currently 0.25%. This step is intended to insure sufficient short-term funding for primary dealers. Those institutions, about two dozen in number, are important intermediaries in the implementation of monetary policy and help to make markets for Treasury securities.[1] The PDCF is authorized under section 13 (3) of the Federal Reserve Act and has been approved by the Treasury Secretary.

The details

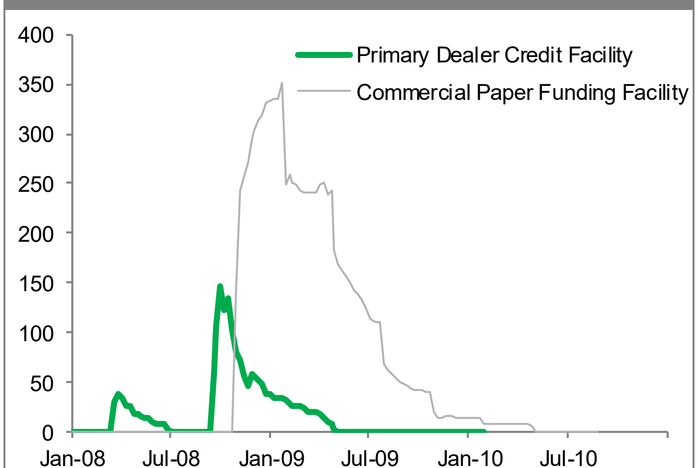
In essence, the PDCF extends credit to the primary dealers from the Federal Reserve similar to that extended to depository institutions (banks) at the Fed's discount window. Reflecting that similarity, loans to primary dealers will be charged interest at the primary credit rate (the "discount rate"), which is currently 0.25%. Loans may be extended for any maturity up to 90 days and may be prepaid by the borrower. All loans will be fully collateralized. Collateral may take many forms of investment-grade securities, including Treasury securities, commercial paper, mortgage-backed securities, collateralized loan obligations, collateralized debt obligations, municipal bonds, other asset-backed securities, and a range of equity securities.[2] Collateral values used to establish maximum allowable credit will be determined by a schedule similar to that governing collateralized loans made to banks at the discount window. Eligible securities must be denominated in US dollars. Loans are with recourse to the primary dealer institution.

Credit extended under the PDCF will be provided by the Federal Reserve Bank of New York. Unless offset, loans made under the PDCF will expand the balance sheet of the Federal Reserve system.

Historical backdrop

The Federal Reserve operated a broadly similar primary dealer credit facility (also abbreviated as PDCF) from 2008 to 2010, during the last financial crisis. Total disbursements during the life of the previous PDCF cumulated to $8.95 trillion, with a maximum outstand-

Amounts outstanding
Billions of dollars



Source: Federal Reserve Board © 2020 IHS Markit

1. Primary dealers are trading counterparties of the Federal Reserve Bank of New York in its implementation of monetary policy and participate in Treasury auctions with bids provided on a competitive basis.

2. Eligible equity securities *exclude* exchange-traded funds, mutual funds, unit investment trusts, rights, and warrants.

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ing, in October 2008, of $148 billion. The latter is less than one-half the maximum amount of credit provided under the previous Commercial Paper Funding Facility, which peaked at $334 billion in late 2008.

Fed concerns and future actions

The over-arching goal of the two programs announced on 17 March, the Primary Dealer Credit Facility and the Commercial Paper Funding Facility, is to ensure that market conditions remain orderly with ample liquidity, to support the flow of credit to households, businesses, and other institutions that are or will be impacted by the COVID-19 pandemic. Among the Fed's concerns is that surging demand for dollar liquidity will create stresses in funding and securities markets that could inhibit credit provision and result in unsettled conditions in markets for financial assets, leading to fire sales and further declines in asset prices.

As we wrote on 17 March following the announcement of the Commercial Paper Funding Facility, the Federal Reserve is likely to take further steps to support credit-provision and funding markets in coming days and weeks.

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