Discussion of

"Designing a Crisis Liquidity Facility with Nonbank Counterparties: Lessons from the TALF"

by Covitz, Meisenzahl & Pence

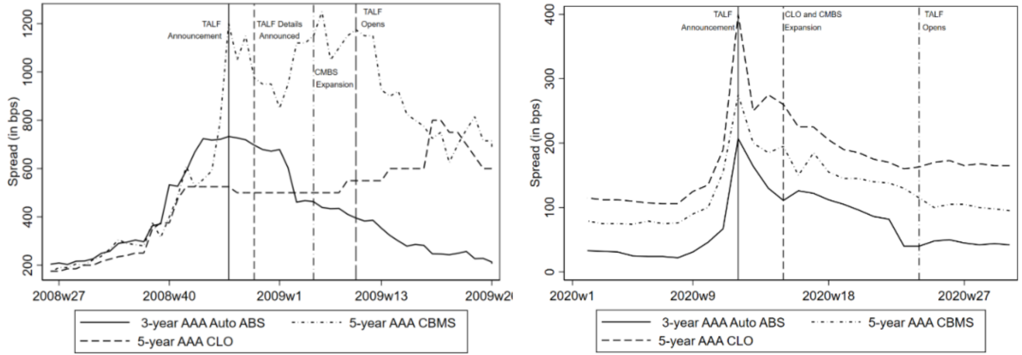
Miguel Faria-e-Castro
Federal Reserve Bank of St. Louis

AREUEA, Online, June 2021

Term Asset-Backed Securities Loan Facility (TALF)

- Major liquidity facility overseen by Federal Reserve & US Treasury
- Offered 3y/5y term loans to nonbanks, ABS/CMBS as collateral
- Two iterations:
    1. TALF 1.0, March 2009 - June 2010
    2. TALF 2.0, March 2020 - December 2020
- **Goal**: stabilize (nonbank) demand for ABS/CMBS, which have become key feature of financial intermediation in the US

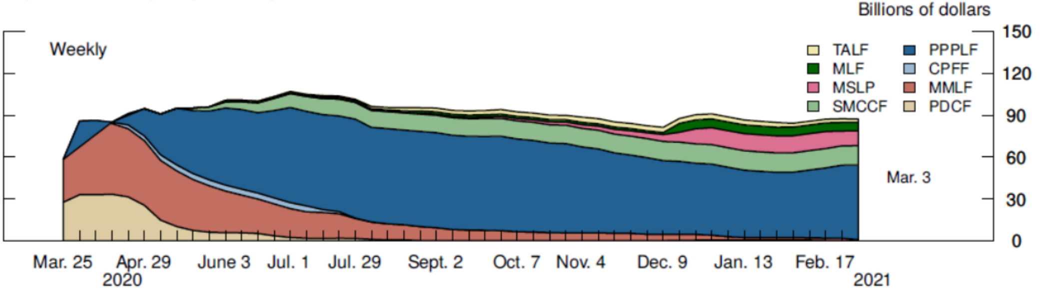
TALF: Aggregate Effects



Source. Courtesy J.P. Morgan Chase & Co., Copyright 2021.

Note: Spreads shown are spreads over swaps in the case of Auto ABS and CMBS.

TALF: Size



Note: The values shown are outstanding amounts. TALF is Term Asset-Backed Securities Loan Facility; MLF is Municipal Liquidity Facility; MSLP is Main Street Lending Program; SMCCF is Secondary Market Corporate Credit Facility; PDCF is Primary Dealer Credit Facility; MMLF is Money Market Mutual Fund Liquidity Facility; CPFF is Commercial Paper Funding Facility; PPPLF is Paycheck Protection Program Liquidity Facility.
Source: Federal Reserve Board, Statistical Release H.4.1, "Factors Affecting Reserve Balances."

Source: Clarida, Duygan-Bump & Scotti (2021)

This Paper

- Did the two iterations of TALF comply with "Bagehot's Rules"?
    1. Quick stabilization of target markets
    2. Protect taxpayers from losses
    3. Provide broad liquidity support (beyond target market)
    4. Orderly exit upon normalization of market conditions
- Document in detail the key characteristics of the two TALF iterations
    1. Who borrowed from TALF and when?
    2. How important were collateral reviews/rejections?
    3. Did TALF participation provide liquidity support for risky assets?
    4. Who exited the program first?

This Paper: Results

1. **Who borrowed from TALF and when?**
   - TALF 1.0: mix of "traditional" ABS investors and opportunistic investors
   - Traditional investors came first, opportunistic investors came later
   - TALF 2.0: lower participations, opportunistic investors only
2. **How important were collateral reviews/rejections?**
   - Significant price effect on rejected securities (10bps)
   - Possible effects at the extensive margin (especially for CMBS)
   - Rejections more frequent towards the end of the program
3. **Did TALF participation provide liquidity support for risky assets?**
   - Opportunistic investors held/pledged riskier collateral and with longer WALs
4. **Who exited the program first?**
   - Opportunistic investors prepaid TALF loans earlier as markets normalized

Comment 1: Learning about Liquidity Facilities

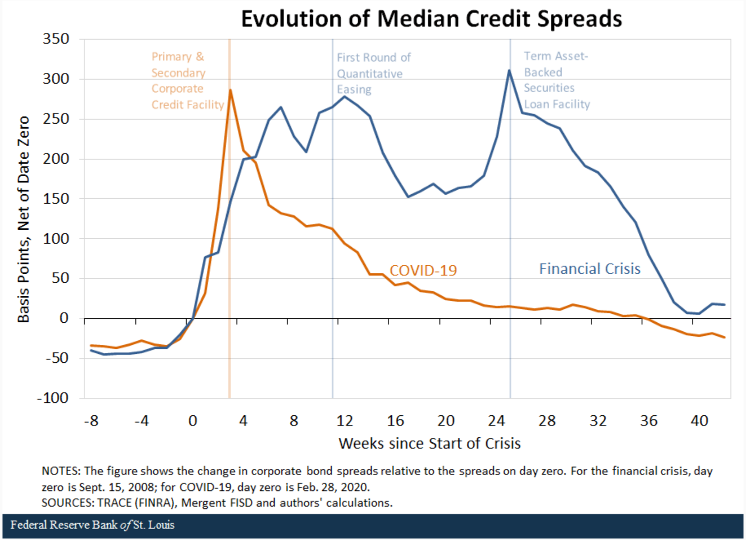
- Paper as a case study on how markets learn about unconventional monetary policy
- TALF 1.0 was a brand new program, uncertainty about effectiveness/functioning
  - Smaller (initial) announcement effects
  - larger "detail announcement"/facility opening effects
  - Possible to test difference?
  - TALF-specific opportunistic investors appear later for TALF 1.0, quickly set up for TALF 2.0
- TALF 2.0: markets already knew what it was/how it worked
  - Larger announcement effects
  - By 2020, TALF was already well-established as a true LOLR "off-equilibrium" tool
  - Real effects even with no utilization by tradititional ABS investors
  - TALF 2.0 more similar to "late" TALF 1.0
- Interesting point that paper could emphasize a bit more

Comment 2: Pledged vs. Non-Pledged Securities

Do *acceptances* have a price impact in a broad panel of CMBS?

$$\Delta\text{Spread}_{it} = \beta_1 \text{Rejected}_{it} + \beta_2 \text{Accepted}_{it} + \theta_i + \alpha_t + \epsilon_{it}$$

- Identification of β_2 requires sample inclusion of CMBS that were *not* pledged but potentially eligible (i.e. AAA before purchase)
- Any significant differences between pledged securities and those that were not pledged?
- Even if no effect is found $\Rightarrow$ potential evidence of far-reaching market stabilization benefits
- Does the type of investor matter for the price impact of the program?
- Even if inclusion of non-pledged securities not feasible, some comparison with the avg security outstanding would be welcome



Source: Ebsim, Faria-e-Castro & Kozlowski (2021)

Minor Comments

1. Ex-post, back-of-the-envelope "profits" by type of institution
2. Are the rejections from traditional and opportunistic investors different in any sense? Table 7 for rejected securities only?
3. Would like to know a bit more about the 3 banks that participated in TALF 1.0 for "idiosyncratic reasons", even if the reasons/evidence is merely anecdotal.
4. Evidence on rejections is interesting, but link to protection against taxpayer losses not very solid in my opinion
5. Are there long-term price effects from rejection? Regression in p22: try with Rejected(it) as a dummy that is equal to 1 for longer.
6. More details on how the haircuts were defined would be welcome. Conceptual question: why would the Fed reject collateral instead of simply demanding a higher haircut, as the ECB does with its haircut schedules for MROs/LTROs?
7. Is there any relationship between type of investor accessing facility and behavior of (aggregate/average) ABS/CMBS spreads over t?

Conclusion

- The reference paper for the details and effects of the two rounds of TALF
- Case study on how liquidity facilities are established and developed
- Encourage authors to further leverage the fantastic granular data on TALF participation and pledged collateral
- Enjoyed reading the paper and learned a lot!