Eric S. Rosengren, President and CEO, Federal Reserve Bank of Boston

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Members of the Commission – Representative Hill, Mr. Ramamurti, Representative Shalala, and Senator Toomey – thank you for the opportunity to speak with you about the operationalization of the Federal Reserve's Main Street Lending Program, a facility authorized by the Board of Governors of the Federal Reserve System ("Board of Governors") under section 13(3) of the Federal Reserve Act, with approval of the Secretary of the Treasury. As you know, the Department of the Treasury ("Treasury") has committed to make an equity investment of $75 billion in the Program – and the funds available for investment by the Treasury were appropriated to the Exchange Stabilization Fund under section 4027 of the Coronavirus Aid, Relief, and Economic Security Act (the "CARES Act").

The Federal Reserve Bank of Boston, which I lead, administers the operations of the Main Street Lending Program ("Main Street" or "Program") for the Federal Reserve System. As such, I am very pleased to be here today to provide information that I hope will be useful to you in your important oversight work.

Background to the Program

In addition to the tragic loss of life, all of us know that the COVID-19 pandemic poses a shock to the U.S. economy that is unprecedented in our lifetimes. With real GDP in the second quarter falling by more than 30 percent, it is clear that businesses, nonprofits, and individuals across the country are being challenged by the fallout from the virus. We have seen a

disproportionate impact on entities whose operating models require significant social interaction, stemming from consumers' concern with their own health and safety as well as more formal restrictions on movement and commerce. For example, hotels, airlines, retail stores, entertainment venues, restaurants, and tourism-related enterprises have all suffered significant disruptions to their businesses and cash flow, with more difficulties possible if the public health concerns persist. Nonprofit entities like medical service providers and educational institutions also are challenged.

Both fiscal and monetary policymakers have acted swiftly to address the economic impacts of the pandemic and cushion the blow. The Federal Reserve, for example, has taken a number of aggressive policy actions since late winter, aimed at blunting the economic effects of the crisis. Seeing unusual volatility and troubled financial markets, the Federal Open Market Committee reduced short-term interest rates to near zero and purchased significant amounts of securities, and the Board of Governors established a variety of emergency facilities under section 13(3) of the Federal Reserve Act in order to restore market functioning and facilitate lending.

These actions helped to restore financial stability and significantly reduced spreads on short- and long-term corporate and municipal securities – spreads which had increased due to uncertainty, and challenged the flows of credit that underpin our economy. And the facilities helped to unlock a great deal of private credit, as well.

Many of the emergency lending facilities are similar to facilities rolled out during the 2008-2009 financial crisis. However, many of the businesses most impacted by the pandemic are smaller firms that rely on banks for loans, rather than accessing public credit markets (i.e., issuing bonds). The Main Street Lending Program is designed to facilitate lending to small and medium-sized businesses that have suffered disruptions from the pandemic, and were in sound

condition prior to the pandemic. The program, like all emergency lending facilities, was authorized by the Board and Treasury, and in this case is being implemented and administered by the Federal Reserve Bank of Boston.

The terms of the Main Street Program were enhanced and expanded by the Board and Treasury prior to the Program's opening, and more recently a term sheet has been released that makes the Program available to non-profit organizations as well as for-profit businesses. I would note that in addition to providing loans for borrowers in current need of funds, the Program offers a credit backstop for firms that do not currently need financing, but may if the pandemic continues to erode the financial condition of these firms over late summer and fall.

Importantly, the Main Street Lending Program differs from other programs for businesses made possible by the CARES Act, reflecting the parameters of what the Federal Reserve is authorized by Congress to do. Unlike the Paycheck Protection Program, where many loans could turn into *grants* funded by the CARES Act, the Main Street program involves loans that must be repaid. The Program has no loan guarantee like the Small Business Administration provided for the Paycheck Protection Program, and requires both the borrower and lender to be eligible to participate in the Program.

We engaged in a great deal of consultation with potential borrowers and lenders as we set up the Program. In addition to soliciting public comment, staff at the Board of Governors, Treasury, and the Federal Reserve Bank of Boston conducted outreach to potential borrowers and lenders of all sizes – ranging from community banks to the largest lenders in the country – in an effort to gather information to inform policy judgments and operational decisions related to the Program. In addition to the variety of outreach calls, we have hosted a series of 14 (so far) webinars that have been tailored to borrowers and lenders, and in which presenters review the

terms, conditions, and operational details of the Program. All of the sessions have been well attended with many having more than 1,500 participants.

To ensure the Program is widely known, in conducting these webinars and otherwise sharing information we have made an intentional effort to reach nonprofits, minority and women-owned businesses, minority depository institutions, and tribal businesses. In addition, robust Frequently Asked Questions documents provide detail on many aspects of the for-profit and non-profit program facilities, and are updated with some frequency.

Parameters of the Program

The Main Street Lending Program was designed to provide credit support for business or nonprofit borrowers that have temporary cash-flow problems due to the pandemic – and given the uncertain outlook might otherwise have difficulty in obtaining credit from a lender that would have to hold 100 percent of the loan. Main Street can provide a loan to bridge the borrower over this current challenge. Main Street loans have no interest or principal payments in the first year, and indeed no principal payments until year three, making the cash-flow aspects of the loan attractive to borrowers experiencing a pandemic-related, temporary disruption of their business model.

The Program includes three lending components for for-profit businesses. They have similar interest rates, maturities, and terms, but have somewhat different collateral arrangements, loan-size limitations, and underwriting. For mid-sized businesses with existing term or revolving lines of credit, the Main Street *Expanded* Loan Facility (MSELF) allows businesses to upsize their current loans, with additional lending of $10 million to $300 million. For smaller businesses, the Main Street *Priority* Loan Facility (MSPLF) allows businesses to borrow from

$250,000 to $50 million. Under each of these facilities the Main Street loans must be senior or *pari passu* (of equivalent status) with the borrower's other loans and debt instruments (excluding mortgage debt).

For smaller business loans without collateral, there is the Main Street *New* Loan Facility (MSNLF) that provides loans from $250,000 to $35 million dollars, which cannot be contractually subordinated to other debt. Because these loans do not have security or collateral requirements, they are only available for firms whose debt including the Main Street loan does not exceed four times the borrower's EBITDA – a more restrictive underwriting criterion than the other two loan types, which set maximum loan size based on six times the borrower's EBITDA.

The two *nonprofit* lending components of Main Street are announced but not yet live. They will have broadly similar terms as the for-profit Main Street facilities, for example in maturity and interest rate. The Nonprofit Organization *Expanded* Loan Facility (NOELF) and the Nonprofit Organization *New* Loan Facility (NONLF) have similar priority and size requirements to their for-profit counterparts. They differ in that the underwriting is tailored to the special characteristics of nonprofits.

Lending, and Lenders

We have taken great care to operationalize the Main Street program to ensure it functions smoothly and securely. Of course, setting up a program to serve many different borrowers and lenders is inherently complex, but I believe the Commission in its oversight role can feel confident that this challenge is being met in strong fashion, in the public interest.

Unlike the corporate credit and muni facilities, which purchase largely standardized credit instruments, Main Street purchases interests in loans that are, by nature, bespoke agreements between borrowers and lenders. Loan agreements and loan terms can be quite different across banks, and even within a bank the agreements are the result of negotiation between borrower and lender that often result in complex, borrower-specific terms and conditions. For example, banks differ on whether they require personal guarantees or collateral in excess of Program requirements; and those policies may vary based on the financial condition or business model of the borrower.

Constructing a Program that handles this complexity is something we have been intensely engaged with these last few months at the Federal Reserve Bank of Boston. We are pleased to have the opportunity to do this important work, in the spirit of public service that runs through our work and our staff.

Shifting to how the program works, to become an eligible lender for the Program the financial institution must first register via our Main Street lender portal. As part of the enrollment process, the institution must verify that it meets our eligibility requirements, and make attestations regarding CARES Act provisions which require the signature of the principal executive officer and principal financial officer. Furthermore, the institution must set up and verify arrangements to transfer funds effectively and safely, to ensure security and resilience.

Since our portal opened for lender registration on June 15, 509 financial institutions have registered with the Program, and their assets represent $14.25 trillion, which is approximately 58 percent of total banking assets in the United States. The attached **Figure 1** shows the size distribution of registered MSLP lenders. It includes the largest universal banks and regional

banks, and a sizable number of banks in the $1-10 billion asset range as well as in the under $1 billion asset category. Participation is of course strictly voluntary for financial institutions.

During the extensive outreach that we did prior to launching Main Street, we heard concerns from some businesses that their current lender would not be participating in the Program or that they might find it difficult to locate a participating financial institution that would work with new customers. In aiming to address these concerns, we ask lenders during the registration process if they plan to accept loan applications from new customers. We contact each lender that says they would consider loan applications from new customers, and ask whether they will join a public list of such lenders. **Figure 2** shows the interactive map we created that allows borrowers to identify which lenders in their state are registered with Main Street, are prepared to consider new customers, and are willing to be listed as such. The interactive map is available on the program website, www.bostonfed.org/mslp, and we update the list daily as new lenders register. Currently it contains 153 lenders. Figure 2 shows, for an example, the financial institutions on the map for my home state of Massachusetts.

It is important to note that Main Street relies on lenders to underwrite the loans, and indeed the lenders have "skin in the game" by retaining 5 percent of the loan participation. Borrowers need to meet the underwriting standards of the financial institution, and the terms and conditions of the Main Street Lending Program, whether they have an existing relationship with the lender or are a new customer.

Borrowers also must meet the eligibility criteria set out in the Program term sheet, and must be able to make the certifications and commitments required by the Program, including those required under the CARES Act. Also, while the loan interest rate of 300 basis points over LIBOR is likely attractive to somewhat higher-risk borrowers, those businesses that have strong

balance sheets and have *not* been significantly impacted by the pandemic may very well find their lender can give them more attractive terms than the Main Street Program. Because the loans are not forgivable by the Federal Reserve and lenders retain a 5 percent interest in the loan, borrowers must have the ability to pay back the loan. For borrowers with severe problems, additional debt may not be helpful, and neither the lender nor the borrower will find taking additional debt attractive. But for many others, the program can serve as a vital bridge to address cash flow interruption ushered in by the pandemic.

Early Results

Figure 3 shows the flow of potential loan participation purchases through the Program's portal as of the end of the day on Tuesday (August 4). As you see on the summary bottom line, currently over $530 million in loans are active in the portal, representing 54 loans. Of that total, 18 loans with a combined value of $109 million have commitments for purchase or have been settled. In addition, over $421 million in loans are in various stages of review in the portal. As a reminder, the program opened for loan purchases on July 6. The numbers I share with you today are consistent with what I would characterize as a gradual pace of initial activity, which is more recently expanding.

The 54 loans submitted in the portal currently represent 29 distinct lenders. Almost all the loans currently in the portal have been initiated by financial institutions with under $50 billion in assets. Additionally, there are 36 lenders with *draft* entries in progress in the system. I mention these draft entries because they reinforce that additional lenders are active in the portal and getting familiar with Program operations.

Figure 4 breaks out the total of potential loans in the portal by the particular branch or facility of the Program. The largest number of loans – 29 – are in the New Loan Facility. The Priority Loan Facility currently has 24 loans valued at $328 million in the portal. And currently there is only one loan utilizing the Expanded Loan Facility in the portal. The Expanded loan facility will generally encompass larger loans and require current participating banks to alter existing loan agreements to upsize existing credit facilities.

Figure 5 provides the size distribution of potential loans currently in the portal. While the largest number of loans are in the size cohort between $1 million and $2.5 million dollars, there are loans under $1 million and greater than $30 million. The industries represented include construction and design firms, dental offices, retailers, and entertainment-related firms like movie theaters. Thus, the loans we have seen to date have reflected what one might broadly expect of small and mid-sized firms whose businesses have been disrupted by the current efforts at social distancing.

Figure 6 shows the potential loan distribution by the asset size of the lender registered in the Program. The largest number of loans are by financial institutions in the $10-50 billion size range. However, there has been participation by relatively small community banks as well. To date, there has been only limited activity by banks with more than $50 billion in assets.

As I alluded to a moment ago, the Program's relatively modest initial numbers seem to be giving way to more uptake as participants become familiar with the program's parameters. I believe the gradual uptake is a function of participants adjusting to a few unavoidable factors. First and foremost, loans are bespoke, and the Program needs to accommodate lending across a wide range of industries, jurisdictions, and business profiles, which makes for operational challenges. Also, the Program's complexity reflects the underlying loan agreements, the terms

and conditions in the Program, and requirements related to the CARES Act. As a result, it can take some time for borrowers and lenders to gather the required documents for submission to the Program. Loan documents not in compliance with terms and conditions have slowed some of the intake. We are working to help participants understand and avoid common errors that can slow the process down.

Summary Observations

Designing and operationalizing a program of this breadth and nuance, delivered through highly secure technology, is a significant achievement in a few months' time. Everyone involved is focused on helping to provide important credit support to businesses and nonprofits at this critical and challenging time.

As we speak today, in early August, I can say that we have worked through many challenges. Among the emergency lending facilities established by the Federal Reserve since late winter – and indeed in comparison to the emergency programs of the 2008 financial crisis – the Main Street Lending Program is operationally complex. Quickly scaling up a program that purchases participations in bespoke loans – from a very diverse group of borrowers in a decentralized market that lacks standardization – is inherently difficult. There are also tradeoffs between limiting credit risk, targeting support, reaching scale, and achieving operational efficiency. Considerations such as these have made the Main Street Lending Program one of the most challenging emergency lending programs the Federal Reserve has ever put in place. The Commission can be assured that the Federal Reserve and Treasury have sought to design a program that is well managed with respect to risks, efficiency, and resilience, while being responsive to the needs of borrowers experiencing difficult times.

The eventual size of the Program will be determined by the path of the pandemic and the economy, generally. Should the pandemic and the economy worsen, or financial institutions experience larger than expected loan losses and depletion of capital – all things we hope do not happen – then I would expect interest in using this Program to expand more rapidly.

In conclusion, the pandemic's shock to our economy is unprecedented, and the pain for businesses, organizations, and workers has been unparalleled in our lifetimes. It is important that the Federal Reserve stands ready at this time of distress, in the public interest and in pursuit of our Congressional mandates, to support lending to for-profit businesses and nonprofit organizations of many sizes at reasonable rates. From many decades of research and policymaking, I can attest that credit interruptions prolong recessions and ultimately harm individuals on Main Streets across America. I pledge to you that in administering the Program, the Boston Fed and the Federal Reserve as a whole will do all that is in our power and purview to effectively support the firms, nonprofits, and individuals that make up our nation's economy.

Thank you for the opportunity to provide this high-level overview of the Program. I would now be happy to address any questions.