

No one can say Bernanke is resting on his laurels now

Written by ReggieMiddleton

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Bernanke is showing that he is willing to go far and wide to right what he sees as wrong. To think, just a few weeks ago, screaming heads such as Cramer were saying the Fed needs to do more, yada, yada. Well, it appears that this Fed is potentially doing too much. An interesting excerpt from [Bloomberg](#) :

Fed Chairman [Ben S. Bernanke](#) , trying to restore confidence to financial markets by averting a collapse of Bear Stearns, is pushing the central bank into new territory. Yesterday's announcement shows the Fed acting like a bank liquidator -- a role traditionally performed by the Federal Deposit Insurance Corp. -- for Bear Stearns, a firm whose main regulator is the Securities and Exchange Commission.

"Bernanke has taken the bit in his teeth," said [Tom Schlesinger](#) , executive director of the Financial Markets Center in Howardsville, Virginia. "I can think of nothing in recent or distant memory that remotely resembles what the Fed is doing here, certainly within the context of the central bank's operations."

The Fed last week agreed to help JPMorgan acquire Bear Stearns after a run on Bear, once the second-biggest underwriter of U.S. mortgage bonds. In an effort to shore up Wall Street's other firms, it also agreed to become lender of last resort to all 20 primary dealers in Treasury notes.

BlackRock Selected

The Fed said March 16 it would provide financing to JPMorgan for \$30 billion of Bear Stearns assets. Yesterday, it released terms of the funding, including some details on the company managed by BlackRock. The Fed said JPMorgan will shoulder the first \$1 billion of any losses, disclosed that the loan will be for 10 years and carry the 2.5 percent [interest rate](#) charged to commercial banks at the discount window.

Fed officials defended their role in the Bear Stearns rescue as necessary to prevent a broader

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financial panic. Credit markets have been roiled by concerns that borrowers won't repay debt, and funding has dwindled for securities firms, hedge funds, and mortgage banks.

Still, Bernanke and New York Fed President [Timothy Geithner](#) may have overstepped and altered the role of the government in financial markets, said

[Joe Mason](#)

, associate professor of finance at Drexel University in Philadelphia.

'Far Outside'

"The Fed is so far outside the traditional bounds," said Mason, a former economist at the Office of the Comptroller of the Currency, one of five federal bank regulators. "It isn't innovative, it is taking a step back in time to a system of direct credit" where the government decides "who gets funding and who doesn't," he said.

Under the terms of the deal, the Fed will loan \$29 billion, and JPMorgan will loan \$1 billion, to a new company based in the U.S. state of Delaware.

The new company will then send \$30 billion to JPMorgan in exchange for some Bear Stearns assets valued at that amount as of March 14. BlackRock has been hired by the central bank to manage and liquidate the assets to repay the loans, interest, and management expenses of the company. JPMorgan will be first to absorb losses on the assets, to \$1 billion, if there are any.

"This sounds like a purchase of a portion of Bear Stearns's portfolio," Vincent Reinhart, a former head of Fed's Division of Monetary Affairs, and now a scholar at the American Enterprise Institute in Washington, said in a Bloomberg Television interview. "The Federal Reserve Bank of New York seems to have an equity interest. It's not your father's kind of loan."

RTC Similarities

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The structure resembles that of the Resolution Trust Corp., the agency created in 1989 to dispose of the assets of insolvent savings and loans banks, said Schlesinger of the Financial Markets Center.

From 1986 through 1995, 1,043 savings banks with over \$500 billion in assets failed, costing taxpayers \$75.6 billion, according to an FDIC analysis.

“What they're doing is setting up a mini-RTC within their own domain,” said Schlesinger. “The Fed is not only breaking new ground with respect to policy initiatives, but breaking new ground functionally in taking on a bad-asset resolution capacity without any authority from Congress to do so, without any oversight.”

Bernanke testifies to the Joint Economic Committee of Congress on April 2. Senator Charles Grassley, an Iowa Republican member of the chamber's finance committee, said last week he wants details of the Fed's involvement in the rescue of Bear Stearns.

“I want to understand what the downside risk for the taxpayer is and any upside potential,” Grassley said in a statement on March 20.