FHLBANKS
A NATION OF LOCAL LENDERS

February 15, 2024

The Honorable Andy Barr
Chair
Subcommittee on Financial Institutions and Monetary Policy
Committee on Financial Services
United States House of Representatives
Washington, DC 20515

The Honorable Bill Foster
Ranking Member
Subcommittee on Financial Institutions and Monetary Policy
Committee on Financial Services
United States House of Representatives
Washington, DC 20515

Dear Chairman Barr and Ranking Member Foster:

On behalf of the Council of Federal Home Loan Banks (the Council), I am writing regarding the hearing entitled, "Lender of Last Resort: Issues with the Fed Discount Window and Emergency Lending." The Council is the trade association for the Federal Home Loan Bank System (FHLBanks) which includes the 11 FHLBanks and the Office of Finance. We appreciate the opportunity to submit this letter for the record of the hearing.

FHLBanks' role as a reliable liquidity provider to their members is fundamentally different than the role of the Federal Reserve Discount Window (the discount window), which typically offers limited duration liquidity and functions as the lender of last resort. In contrast, FHLBank members – banks, credit unions, insurance companies, and community development financial institutions – actively and continuously depend on, plan for, and incorporate our liquidity into their financial strategies. FHLBank advances and mortgage finance activity play a critical role in supporting community economic development, mortgage lending activity, maintaining mortgage market liquidity across varying economic cycles, and reducing mortgage costs. Each FHLBank operates as a member-owned, privately funded cooperative, with strong relationships within its district and a focus on ensuring members have reliable access to liquidity in all market environments. The ability of members of all sizes and varying charter types to rely on ready access to FHLBank liquidity maintains the diversity and vibrancy of the U.S. financial system.

Among other things, FHLBank liquidity allows members to offer longer-term mortgage loans at stable and lower interest rates, directly benefiting American homebuyers. The availability of FHLBank financing options is crucial for the health of the housing market and for broader economic stability. A 2020 study from the University of Wisconsin showed that the FHLBank System saves borrowers $13 billion in mortgage interest payments every year and leads to a more than 16 percent increase in mortgage originations.[1] Community lenders also rely on FHLBank liquidity to support small business, agricultural and agri-business lending.

We recognize the Federal Reserve's role as the lender of last resort for banks and credit unions. However, during times of market instability the FHLBanks have traditionally played a critical role of the first responder for otherwise healthy members, including during the Great Financial Crisis, the early days of the COVID-19 pandemic, and throughout March 2023. As financial first responders, the liquidity we provide serves to stabilize the mortgage market and the broader financial system. Economists Mark Zandi and Jim Parrot noted in a recent paper:

[1] Zhang, Dayin. "Government-Sponsored Wholesale Funding and the Industrial Organization of Bank Lending." October 2, 2020. https://business.wisc.edu/news/federal-home-loan-bank-may-save-borrowers-money-level-the-playing-field-for-small-banks/.

> This stabilizing role has been critical several times in recent memory alone, as alternative sources of capital fled the system, and the Fed was yet to step in as the lender of last resort. Without the FHLBs, these downturns in the economic cycle would have been significantly more painful, with greater swings in the cost and availability of credit, exacting greater damage on the economy.[2]

When FHLBank members face troubled circumstances, FHLBanks go through a methodical credit and liquidity analysis of the member, engage in regular communication and coordination with financial regulators, which have the authority at any time to instruct the FHLBank not to lend to a troubled member. The interaction and cooperation with our members' regulators positions FHLBanks to play a supportive role in the resolution of troubled institutions and enhances the resilience of the financial system. Importantly, in these circumstances, FHLBanks help ensure orderly resolutions and reduce costs to the deposit insurance fund.

In the aftermath of the March 2023 banking turmoil, FHLBanks have redoubled their efforts to coordinate with their respective Federal Reserve banks and members' regulators to ensure that members have established relationships and have tested their lines with the discount window. Work is also underway to ease the transfer of collateral between FHLBanks and Federal Reserve banks when necessary. This work will further facilitate cooperation and efficiency during times of crisis, enhancing overall financial stability.

While increased FHLBank coordination with the Federal Reserve Banks may be beneficial – and the FHLBanks are working with their members to ensure that they establish relationships with their Federal Reserve Banks – the longstanding role of the FHLBanks as a continual and reliable liquidity provider for their members should not be disrupted. The FHLBanks and the Federal Reserve have distinct, but complementary, roles within the U.S. financial system, both of which are ensconced in statute. Any reforms should recognize the importance of preserving both roles and both sources of financial institution support during a crisis.

FHLBanks have demonstrated throughout their nearly hundred-year history that they can work collaboratively with financial regulators and federal deposit insurers in crisis situations. The Council stands ready to work with Congress, the FDIC, the FHFA and the banking and credit union regulators, to constructively ensure that the FHLBanks remain a reliable liquidity source for their members and the mortgage market and continue to contribute to overall financial stability.

Thank you for holding this hearing and taking our views into consideration.

Sincerely,

Ryan Donovan
President and CEO

[2] Parrott, Jim, and Mark Zandi. "In Defense of the Federal Home Loan Banks." Urban Institute, April 2023. https://www.urban.org/sites/default/files/2023-04/In%20Defense%20of%20the%20Federal%20Home%20Loan%20Banks.pdf.