Statement of Senator Tim Johnson
Senate Committee on Banking, Housing and Urban Affairs
"Turmoil in US Credit Markets: Examining the recent actions of Federal Financial Regulators"
April 3, 2008

Thank you, Chairman Dodd, for holding this hearing today. There is no doubt in my mind that all of us sitting on this side of the dais have many questions regarding the recent actions by the Federal Reserve since our last Banking Committee meeting; questions not only for the Federal Reserve, but for all of the stakeholders involved in the actions that resulted in JPMorgan Chase's purchase of one of the largest investment banks—Bear Stearns.

I had the opportunity to discuss the Bear Stearns purchase and subsequent actions taken by the Federal Reserve with Chairman Bernanke in the days following Sunday March 16. I am pleased that all the panelists before us today have taken time out of their schedules to talk with members of the Committee about these recent actions and the implications on the markets, the regulators and taxpayers.

There appears to be little consensus on the effects of the recent Federal Reserve action. There has been criticism waged from a large spectrum of people. I have received letters from my constituents with concerns that this is a federal bailout of a big bank that creates a moral hazard. Others have wondered if it is appropriate to offer help to Wall Street firms, while insisting on market discipline for troubled homeowners. There has also been applause for the decision from some quarters. The US markets responded favorably; other investment banks believed to be in trouble saw their stock value rise; foreign governments applauded this as a positive move for global markets, and other analysts suggested that the Federal Reserve actions averted what could very well have been a modern-day run on the bank. The reality of the situation is probably somewhere near the middle.

While I will save my questions for later, there are a couple issues I want to raise. Credit markets continue to be volatile in part because banks and other financial institutions do not know what their subprime mortgages and related securities are worth. Yet, in the transaction for JP Morgan Chase to purchase Bear Stearns, the Federal Reserve extended a $29 billion line of credit for subprime mortgage and related securities based on an arbitrary value of those securities. What assurances are there that the numbers add up?

Additionally, banking and Wall Street firms have reported over $200 billion of losses from CDOs and residential mortgage-backed securities related to subprime mortgages, as well as from loan commitments and obligations related to leveraged corporate buyouts. The 10 largest firms account for about two-thirds of those losses. Many banks and investment firms have been experiencing difficulties, yet Bear Stearns is the firm that was "rescued" by the Federal Reserve. Why Bear Stearns? And if Bear Stearns had not been helped, what would the failure of Bear Stearns or any of the largest securities firms have done to the economy? What about their situation at the moment warranted the help? Will other firms, should they find themselves in the same position as Bear Stearns, receive the same help?

Confidence, liquidity, and transparency are key to a stable market. The hearing today regarding the current turmoil in the U.S credit markets is an important discussion to be had as we attempt to restore confidence, liquidity, and transparency in the markets. I look forward to hearing from the panelists what the Federal Reserve, Treasury, SEC, other regulators can and should do. Most importantly, I look forward to the regulators and other panelists suggestions on what Congress can and should do to help restore confidence, liquidity and transparency.