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The Fed and Treasury Market Contingency Planning: What's in the Toolkit?

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October 2026

Highlights

- The minutes of the September FOMC meeting indicated that a few participants suggested that it would be useful to develop contingency plans to address periods of distress in the Treasury market.
- The Federal Reserve has a wide range of authorities and existing tools that could be used to help address various types of strains in the Treasury market.
- Similar to other central banks, the Federal Reserve could develop explicit contingency facilities aimed at addressing market dysfunction in the Treasury market and related liquidity pressures.
- Developing contingency plans of this type entails tradeoffs between the desire to be fully prepared for various contingencies while at the same time avoiding creating adverse incentives or distortions in financial markets.

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"Regarding balance sheet policy, a few participants observed that Treasury markets had been functioning smoothly but noted the importance of planning for market stress. They suggested strengthening the Federal Reserve's strategy, communications, and tools for addressing market dysfunction, should it occur, while limiting the Federal Reserve's footprint in the Treasury market."

Minutes of the September 2026 FOMC Meeting

"We need an emergency, break-the-glass plan which is targeted and short-term and on the shelf so that it's ready to go when we hit the wall."

Henry Paulson, Bloomberg Interview, April 16, 2026

Treasury rates have moved up sharply over recent months with the most notable increases for securities with longer maturities. Many factors may be underlying the runup in longer-term rates this year including strong investment spending and associated heightened demands for long-term financing, persistent Treasury supply pressure stemming from large structural fiscal deficits, and softening global demand for longer-term Treasury securities.

Against this backdrop, many prominent observers have worried about the potential for stress in Treasury markets if global investors pull away from the Treasury market. That risk has likely been compounded by structural shifts over recent years including the increasing role of price-sensitive investors in the Treasury market, uncertainties surrounding the behavior of foreign investors in light of geopolitical tensions, the weaponization of finance in an era of global fragmentation, constraints on dealer intermediation capacity, and cyber threats.[2]

Common measures of Treasury market liquidity such as yield volatility, bid-ask spreads, and order book depth deteriorated sharply during the period of regional banking stress in 2023 and again following the announcement of tariffs in April of 2025. Since then, these measures have returned to more normal levels.[3] That said, vulnerabilities are apparent. The rapid rise in Treasury debt outstanding over recent years was accompanied by a steep rise in primary dealer net positions in Treasury coupon securities through the early part of this year (Figure 1). The rather steep decline in this series over recent months suggests that some large financial intermediaries may be growing wary of interest rate risk or other exposures in the Treasury market. And the fiscal outlook may be stoking those concerns; the Congressional Budget Office (CBO) projects debt held by the

[2] See Duffie et al. (2023) for a discussion of dealer intermediation capacity and Treasury market functioning.
[3] See Dyer and Fleming (2026) for a useful summary of these metrics over recent years.

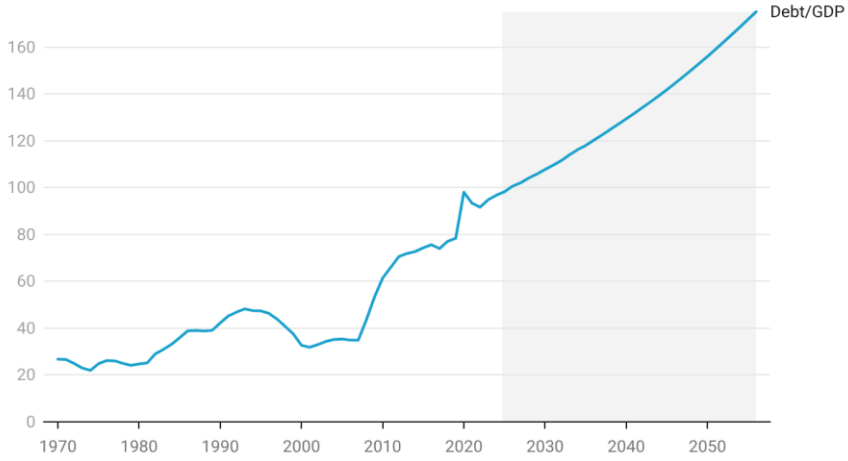
Figure 1: Primary Dealer Net Positions in Treasury Coupon Securities



Source: Federal Reserve Bank of New York primary dealer statistics; last data point for week of October 7, 2026.

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Figure 2: Debt to GDP Ratio: Historical and Projected



Federal debt held by the public as a share of nominal GDP. Projections for the debt/GDP ratio are shown in the gray shaded region and are taken from the CBO's February 2026 long-run budget projections.

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public as a share of GDP to increase from the current level of about 100 percent to about 175 percent over the next 30 years (Figure 2). Moreover, the recent announcement of increases in

the size of the Treasury's buyback operations for longer-term securities points to official concerns about rising rates and perhaps also liquidity pressures for longer-term Treasury securities.

As noted in the opening quotes, Federal Reserve policymakers and prominent figures in financial markets among others have discussed the importance of contingency plans for a period of stress in the Treasury market.[4] All this raises the basic question: What tools do Federal Reserve policymakers have at their disposal to address adverse scenarios if conditions in long-term Treasury markets were to deteriorate sharply?

Selected Tools in the Toolkit

The Federal Reserve has an array of tools that could be used to provide support to segments of the Treasury market.[5] Broadly speaking, the tools rely on either the Federal Reserve's authority to conduct open market operations or its lending authorities. The discussion below provides a thumbnail summary of some of the most prominent tools in each of these categories.

Selected Tools Based on Open Market Authorities

The Federal Reserve's most important authorities for open market operations are provided in section 14(b) of the Federal Reserve Act (FRA). Under these provisions, the Federal Reserve is authorized to purchase securities that are direct obligations of, or fully guaranteed by, the United States or an agency of the United States. Such purchases must be conducted "in the open market" and are subject to rules and regulations established by the Federal Open Market Committee.[6] Some of the basic Fed tools relying on this authority are listed below.

Outright Purchases: The Federal Reserve coordinates purchases of Treasury and agency securities through the System Open Market Account (SOMA). The SOMA securities portfolio currently stands at about $6.5 trillion composed largely of about $4.6 trillion of Treasury securities

[4] The FOMC has prepared contingency plans for various types of scenarios over time. Preparations for debt ceiling contingencies have been discussed on several occasions (see, for example, the discussion at the August 2011 FOMC conference call and an associated staff memo.) In advance of Y2K, the Committee discussed a range of steps to ensure adequate liquidity over the year end including a special financing facility offering options on repo operations; see Drossos and Hilton (2000) for more detail on the special financing facility. In the period from 1965-1967, the Committee developed plans to address pressures in the U.S. government securities market that could arise in connection with a depreciation of sterling.

[5] The Treasury and other agencies may be able to bring additional tools to bear in addressing a period of stress in the Treasury market. The Treasury could increase buyback operations, for example, or lend in repo markets as discussed in the May 2026 report of the Treasury Borrowing Advisory Committee and at the 2026 Treasury Market Conference.

[6] Section 14 also provides authority for purchases of selected other assets including sovereign debt, banker's acceptances, cable transfers, and certain types of municipal securities.

and $1.9 trillion of agency mortgage backed securities (MBS). Rollovers of the Fed's maturing holdings of Treasury securities are accommodated through "add ons" to regular Treasury auctions. Purchases of securities under large scale asset purchase programs or for the purpose of maintaining ample reserves are conducted in the secondary market through competitive open market operations with primary dealers as counterparties.

Standing Repo Operations: The Federal Reserve established the standing repo facility in 2021. The facility provides overnight financing at a fixed rate to approved counterparties including primary dealers and selected banks. Dealers may pledge Treasury securities, agency debt, or agency MBS as collateral with standard haircuts in tri-party operations applied. The rate charged is the same regardless of the collateral type pledged. The rate is set by the FOMC at each meeting and announced in the implementation note accompanying the FOMC statement. Currently the rate is set at the top of the target range for the federal funds rate. Since March of 2025, the Fed has conducted two standing repo operations each day, one in the morning and one in the afternoon. Propositions are limited to $40 billion per security type per operation. In December of 2025, the FOMC eliminated the $500 billion aggregate operational limit on standing repo operations as part of an initiative to enhance the effectiveness of standing repo operations in policy implementation.[7]

FIMA Repo Facility: The Federal Reserve also established the FIMA repo facility in 2021; that facility allows foreign official institutions to borrow against Treasury securities they hold in custody with the Federal Reserve. As specified in the FOMC's continuing directive for domestic open market operations, the rate on overnight FIMA repo operations is set equal to the rate on standing repo operations and the per-counterparty limit for FIMA repo operations is currently set at $60 billion.[8] Aggregate draws under the program are published weekly in the Board's H.4.1 statistical release.

Swap Lines: The Federal Reserve maintains standing liquidity swap lines with five central banks—the European Central Bank, Bank of England, Bank of Japan, Swiss National Bank, and the Bank of Canada. In addition, the Federal Reserve has separate swap lines for Canada and Mexico under the North American Framework Agreement (NAFA). Foreign central banks could find it useful to draw on such facilities to provide liquidity to entities in their jurisdiction that might otherwise seek to sell their Treasury holdings. Central banks that borrow under such

[7] See Statement Regarding Standing Overnight Repo Operations. The minutes of the December 2025 meeting noted that market participants had suggested that removing the aggregate limit was one of several steps that could improve the effectiveness of standing repo operations.

[8] See the Continuing Directive for Domestic Open Market Operations for additional details. The FOMC has also approved term FIMA repo operations of 7-day maturities with the rate set equal to the one-week overnight index swap (OIS) rate plus 25 basis points. The Foreign Exchange Subcommittee of the FOMC may approve changes in various terms of FIMA repo operations.

arrangements are free to distribute the proceeds to counterparties in their jurisdictions as they wish. The Federal Reserve's counterparty in these operations is the foreign central bank. The operations are structured in a way that neither party is subject to exchange rate risk. Aggregate draws under swap lines are reported in the H.4.1 statistical release and information about individual draws by counterparty is reported by the Federal Reserve Bank of New York.

Securities Lending: The Federal Reserve Bank of New York conducts auctions in which it lends individual Treasury securities from the SOMA portfolio to market participants and accepts other Treasury securities as collateral. The operations are helpful in addressing market demands for specific securities that may be in short supply in the market.

Selected Tools Based on Lending Authorities

Another set of tools that could be used to address a period of stress in Treasury markets is based on the Federal Reserve's lending authorities. Some of the key tools are listed below.

Discount Window: The Federal Reserve's traditional tool for providing liquidity to depository institutions—discount window lending authorized under section 10B of the FRA—would be readily available to depository institutions experiencing liquidity pressures and problems in liquidating Treasury holdings. Over recent years, Reserve Banks have made important strides in enhancing the efficiency of discount window operations and establishing stronger relationships with the Federal Home Loan Banks on matters related to collateral.[9]

Emergency Lending Under Section 13(3): Section 13(3) is an emergency lending authority under which the Federal Reserve can lend to individuals, partnerships and corporations against a wide range of collateral. The Board must determine that such facilities are necessary to address "unusual and exigent circumstances" and all such programs must be approved by the Secretary of the Treasury. Moreover, the Board must meet a number of reporting requirements in conducting such programs and the programs must be broad-based facilities not designed to aid a specific institution and structured in a way that protects U.S. taxpayers against losses.[10]

Section 13(3) authority provided the basis for many of the emergency lending programs implemented during the global financial crisis (GFC) and the pandemic. The Federal Reserve and the Treasury have sometimes developed facilities including a layer of capital or credit support for the facility using funds from the Treasury's Exchange Stabilization Fund (ESF). Several such facilities were established during the COVID period with funding from the ESF provided through

[9] See Jefferson (2026) for more details on these efforts.
[10] See section 201.4 (d) of the Board's Regulation A for the full list of requirements for extending credit under section 13(3).

the CARES Act. Some portion of ESF current resources might be available to provide a level of capital support for a 13(3) facility as long as such a facility is not deemed to be "the same as" facilities established in connection with CARES Act funding programs.[11]

Section 13(3) authority has also been used to create special lending programs for banks that are not subject to some of the constraints for regular lending programs under section 10B. For example, the Federal Reserve used emergency authority under section 13(3) to provide long-term financing for depository institutions with Treasury, agency, and agency MBS securities pledged as collateral (the Bank Term Funding Program (BTFP)). The use of 13(3) was required in this case because the term of BTFP loans (one year) exceeded the statutory limit on the maximum maturity of discount window loans (four months) under the Federal Reserve's regular lending authorities in section 10B. Motivated by the desire to mitigate run risks in the banking system, the terms for the BTFP were very generous, thus providing strong incentives for banks to replace short-term flighty deposit funding with stable long-term financing from the Federal Reserve.[12]

Emergency Lending Under Section 13(13): Section 13(13) is a little used provision that allows the Federal Reserve to provide advances to individuals, partnerships and corporations for periods up to 90 days with loans secured by Treasury and agency collateral. Section 13(13) is not subject to the statutory requirements that apply to section 13(3) lending authority. As a result, the Board could establish a program under this authority without all the statutory restrictions and requirements that apply for lending under section 13(3). That said, section 13(13) has long been considered an emergency lending authority, and the Board's Regulation A establishes a high bar for any lending under this authority[13]; any use of 13(13) authority to lend to nondepository institutions would undoubtedly attract considerable attention.

Emergency Lending to Designated Financial Market Utilities under Section 806 of the Dodd-Frank Act: Section 806 of the Dodd-Frank Act provides authority for the Federal Reserve to lend to designated financial market utilities (DFMUs) in "unusual or exigent circumstances" based on a vote of the Board and after consultation with the Secretary of the Treasury.[14] This authority has never been used. Designated financial market utilities include the Clearing House Payments Company, CLS Bank, the Depository Trust Company, the Fixed Income Clearing Corporation, the

[11] This limitation was imposed by provisions in section 1005 of the Consolidated Appropriations Act of 2021.
[12] See the term sheet for the BTFP for more details.
[13] Both 13(3) and 13(13) lending authorities were enacted by Congress in the early 1930s to address the banking and financial crisis. Regulation A, section 201.4(d)(13) indicates that prior to extending credit under 13(13), a Federal Reserve Bank must obtain evidence that credit is not available from other sources and failure to obtain such credit would adversely affect the economy.
[14] See section 806 (b) of the Dodd-Frank Act. The statutory language indicates that credit may be extended only if the borrower demonstrates that it is unable to obtain adequate credit accommodations from other banking institutions.

National Securities Clearing Corporation, the Options Clearing Corporation, the Chicago Mercantile Exchange, and ICE Clear Credit. The operations of a number of these entities are quite important for the smooth functioning of the Treasury market. Unlike section 13(3) programs, lending under this authority could be limited to a specific institution.

How Might the Federal Reserve Use Its Tools to Address a Period of Strains in the Treasury Market?

As detailed above, the Federal Reserve has many tools at its disposal that could be used in various ways to address a period of stress in the Treasury market. Exactly which tools would be used and how they would be deployed would depend greatly on the circumstances. It seems likely that the first line of defense might include changes in the terms for existing tools for liquidity provision—standing repo operations, FIMA repo operations, and discount window lending. The FOMC could also enhance the availability of dollar funding provided through standing liquidity swap lines. In addition, the Federal Reserve could conduct targeted purchases of securities specifically aimed at addressing market dysfunction with the understanding that the securities acquired would be sold relatively quickly once the period of market stress had passed.

Liquidity Provision Tools

Lowering Rates on Existing Liquidity Tools: A severe disruption in the Treasury market could result in funding difficulties for firms that invest heavily in Treasury securities or that actively intermediate in Treasury markets. Particularly if these types of disruptions were apparent in repo markets, the Federal Reserve might take steps to relax some of the terms for its existing liquidity provision tools including standing repo operations, FIMA repo operations, and the discount window.

As noted above, the rates for standing repo operations, FIMA repo operations, and primary credit through the discount window have all been set equal to the top of the target range for the federal funds rate. A natural first step to take might be to reduce these rates, perhaps all the way to the level of the interest rate on reserve balances. The rate for standing repo operations is set by the FOMC after each FOMC meeting in the implementation note accompanying its rate decisions. Similarly, the Board approves changes in the primary credit rate following each FOMC based on the recommendations of Reserve Banks. The FOMC's continuing directive for domestic open market operations sets the rate on FIMA repo operations equal to the rate for standing repo operations.

Adjusting Non-Price Terms of Existing Liquidity Tools: The Fed could also take steps to increase the availability of liquidity by adjusting the non-price terms for some of these facilities. For

example, the Fed could relax some of the limits that apply for standing repo operations and FIMA repo operations and could consider adjustments to the programs to make longer-term financing available. In addition, particularly for standing repo operations, the FOMC could consider a temporary expansion of the counterparties eligible to tap the facility. This might be important if the entities that currently have direct access to standing repo operations are unwilling to borrow at the facility and lend to others.

The Fed could also consider relaxing the non-price terms for primary credit loans although there may be less scope for this than in the case of standing repo operations and FIMA repo operations. The Federal Reserve currently provides term primary credit loans for as long as 90 days. That could be extended to the statutory maximum of 120 days (four months). There is a provision in 10B that would allow the Federal Reserve to extend primary credit loans with maturities longer than 120 days but only if such loans are secured by 1-4 family mortgages.

Enhanced Availability of Liquidity Through Standing Liquidity Swap Lines: As in past episodes of financial distress with global repercussions, the Federal Reserve in coordination with other central banks could take actions to expand the availability of dollar liquidity through standing liquidity swap lines. In the past, the FOMC has approved increases in the frequency and tenor of dollar funding made available under these lines. In addition, the FOMC has at times temporarily expanded counterparties for swap lines to include central banks beyond those with permanent lines.[15] Draws on such swap lines might be an important source of funding for foreign institutions that are experiencing funding pressures related to their holdings of Treasury securities.

Conducting Temporary Repurchase Agreement Operations: The Federal Reserve could also conduct temporary repurchase agreement operations with its usual set of counterparties. Such operations were common in the policy implementation framework prior to 2008 but have not been necessary in the regime with ample (or abundant) reserves. However, the Federal Reserve could find it useful to announce repo operations of a fixed size with prices then determined at auction. Dealers in need of additional funding could bid relatively aggressively at these auctions. These types of operations could be useful in addressing a wide range of funding issues. As in the past, the FOMC could authorize term repo operations to address persistent liquidity pressures.

Emergency Liquidity Provision Programs: As the experience in the GFC and pandemic attest, the Federal Reserve can move quickly and creatively in many different ways to erect new liquidity facilities on short notice. Many of these types of liquidity facilities would rely on one or more of the emergency lending authorities discussed above. Two types of emergency liquidity facilities

[15] See the announcement of temporary swap lines established for a number of central banks during the pandemic.

may deserve special mention in the context of a disruption in the Treasury market—variations on the primary dealer credit facility (PDCF) and the possibility of lending to DFMUs.

- *The PDCF*: The PDCF was first established in March of 2008 in response to the market turmoil associated with the failure of Bear Stearns and was implemented again at the outset of the pandemic. In broad outline, the PDCF was much like the current program of standing repo operations with the critical difference that eligible collateral was expanded greatly beyond Treasury and agency securities. This expansion required the use of 13(3) authority. For a very severe Treasury market disruption, some variant of the PDCF that provided credit against a broad range of collateral could be used to address liquidity issues. In today's context, this could be a temporary expansion of the collateral accepted in standing repo operations. In addition, the PDCF established during the pandemic provided financing with terms as long as 90 days.

- *Lending to DFMUs*: Another type of emergency lending program that may have special relevance for a Treasury market disruption would be lending to a DFMU. As noted above, section 806 of the Dodd-Frank Act provides authority for the Federal Reserve to lend to DFMUs under certain conditions. Particularly given the role of Treasury securities as collateral in clearing and settlement arrangements, one could imagine scenarios in which one or more DFMUs (or their direct participants) could experience funding issues. The failure of a participant in a Treasury market clearing arrangement (such as the Fixed Income Clearing Corporation) could disrupt the entire net settlement process for Treasury market transactions in some very adverse scenarios. DFMUs do have contingency plans and liquidity arrangements in place to address problems of this type but a major disruption in the Treasury market could present unforeseen challenges.

Asset Purchase Tools

Apart from its tools for short-term liquidity provision, the Federal Reserve may be able to use its authority to purchase Treasury and agency securities to help address a severe disruption in the Treasury market. Some possibilities in this vein are listed below.

Changes in Reinvestment Practices: At present, the Federal Reserve is reinvesting principal payments from its maturing Agency MBS holdings into Treasury bills. Those reinvestments have been running at about $15 billion a month. The FOMC could choose to reinvest those proceeds instead in segments of the Treasury market under stress. For example, in some scenarios, the commitment to reinvest $15 billion each month for the foreseeable future could be useful in

supporting market liquidity at the longer end of the Treasury yield curve. That said, this would be a modest step given the magnitudes and might be difficult to explain.

Purchases of Shorter-Term Assets: In some situations, the Federal Reserve might be able to help address a period of market strain by purchasing short-term securities such as Treasury bills and agency discount notes. Purchasing Treasury bills or agency discount notes, for example, might be useful if money market mutual funds were attempting to sell large volumes of these short-maturity instruments to meet strong redemption demands. Purchases of agency discount notes could also help to stabilize the short-term funding cost of agencies such as the Federal Home Loan Banks that could be experiencing strong demand for liquidity from their member institutions.

Temporary Purchases of Longer-Term Assets: The Bank of England's use of temporary targeted asset purchases to address the liability driven institution (LDI) crisis in 2022 might be a model for the use of open market operations to address market dysfunction in the Treasury market. Under this sort of arrangement, the Federal Reserve would serve as "market maker of last resort" in the Treasury market by standing ready to purchase Treasury securities at a price somewhat above a distressed market level but below that which would prevail under "normal" market conditions. Unlike the Federal Reserve's previous asset purchase programs, purchases to address market dysfunction could be billed as a temporary program with the explicit commitment that any securities acquired would be sold in a timely manner once market conditions had normalized.[16]

As discussed in Alexander et al. (2023), many technical aspects of such a program would need to be ironed out in advance, particularly on the precise mechanisms that would be used to identify securities to be purchased and the methodology that would be employed to establish a price at which the Fed would be willing to purchase the security in question. Ideally, the pricing would be set in a way that provides market support during a period of dysfunction while also facilitating the Fed's exit strategy as market conditions normalize. For an explicitly temporary program of this type, the FOMC would likely wish to issue some form of statement or other document describing its principles and plans for conducting such operations. And there could be detailed questions as well such as whether the securities acquired would be reported separately each week on the Fed's H.4.1 release. There might also be questions about whether the securities purchased under such a program would be recorded at par value following the Fed's usual accounting conventions or, alternatively, recorded at fair value given the stated intention to sell the securities once market conditions recover.

[16] See Hauser and Logan (2022), Hauser (2023) and Logan (2023) for a discussion of some of the issues associated with programs of this type.

Asset Purchases and Other Balance Sheet Adjustments: In concert with any program to acquire assets, the Federal Reserve would make explicit or implicit decisions about the corresponding adjustments for other items on the balance sheet. In many respects, the most natural balance sheet adjustment associated with asset purchases would be an increase in the quantity of reserves in the banking system. This could push reserves well above "ample" levels but would not impair the Fed's ability to manage the level of short-term interest rates. Reserves would return to ample levels when assets purchased under a temporary purchase program were sold.

If the increase in reserves were judged to be too large for the banking system to manage efficiently, the Fed could narrow the spread between the interest on reserve balances (IORB) rate and that offered on overnight reverse repurchase (ONRRP) agreements. As in the past, that move could result in a shift in the composition of the Fed's liabilities from reserves to overnight repos with counterparties at the ONRRP facility. Alternatively, if the Fed wished to limit the expansion of its balance sheet, it could "make room" for purchases of Treasury securities by selling agency MBS. Selling agency MBS, though, could prove problematic; in all likelihood, a significant disruption in the Treasury market would spill over to significant disruptions in agency securities markets as well; the Fed would presumably not want to be selling agency MBS in stressed market conditions. And sales of agency MBS might also result in significant realized losses for the Fed. The Fed could also sell some of its holdings of Treasury bills and other short-dated securities assuming that the demand for these instruments remained strong.[17]

Other Types of Tools

The Federal Reserve may be able to utilize other types of tools or take other actions in combination with those discussed above importantly including providing temporary regulatory relief or considering structural changes for some of its key operations.

Regulatory Actions: In concert with other regulators, policymakers could take steps to relax regulatory restrictions that could be impeding intermediation by financial institutions. For example, during the COVID period, reserves and Treasury securities were temporarily excluded from assets for the purpose of calculating the leverage ratio. Recently, the Board and other regulators revised the enhanced supplementary leverage ratio (eSLR) applied for Global Systemically Important Banks (GSIBs). The leverage ratio is intended to be a backstop capital requirement that does not bind in normal circumstances. The recent adjustment was intended to address cases in which the leverage ratio may have become binding. In relaxing the eSLR, regulators have noted positive effects in supporting effective functioning of the Treasury market

[17] According to Table 2 of the Fed's H.4.1 release, the Fed's Treasury security holdings include about $500 billion of securities with remaining maturity of 90 days or less.

(see Bowman 2026). In a period of severe stress in Treasury markets, some banks may experience sizable deposit inflows that temporarily affect their capital and liquidity ratios. Temporary regulatory adjustments in light of such effects might be a way of accommodating these types of balance sheet fluctuations.

Central Clearing: From time to time, the FOMC has discussed the possibility of taking steps that would allow central clearing for the Fed's standing repo operations.[18] Central clearing would allow an institution to net repo borrowing in the Fed's standing repo operations against the institution's repo lending. The netting would allow a Fed repo counterparty to borrow in standing repo operations and lend to other counterparties without expanding its balance sheet and incurring the associated capital charges. Implementing central clearing for standing repo operations would likely require the Fed to become a member of the Fixed Income Clearing Corporation—a step that could entail some policy issues as well as legal and operational complications.

Some Common Policy Issues in Deploying Various Tools

A number of policy issues often arise in deploying various contingency facilities and much depends on the circumstances and exact nature of the facility being developed. Nonetheless, some common issues include appropriate design features to limit the real or perceived "Fed Put," tensions that can arise in connection with extending contingency programs to entities not subject to federal regulation, levels of advance preparedness, and the challenges in bolstering public confidence.

The "Fed Put" Versus Run Risks: A tension that often arises in deploying various contingency tools is the desire to address a serious specific issue without also creating adverse incentives. On the one hand, establishing contingency tools may help to mitigate run risks and other forms of knock-on effects in financial markets that can spark contagion and negative externalities. On the other hand, absent any other guardrails, Federal Reserve contingency programs can operate as a so-called "Fed Put" by providing free insurance against a range of possible risks faced by market participants. In doing so, market participants may be incented to limit their own efforts to avoid certain types of risks. For example, a standing program to purchase long-term securities at a fixed price limits the downside risks to market participants in investing in those securities and may provide an incentive for private firms to engage in risky practices—like funding long-term securities with short-term debt—to a greater extent than would otherwise be the case. Central banks recognize these issues and attempt to mitigate these types of effects through effective design of any contingency programs. Often, the design involves a form of pricing that would be

[18] See the brief mention of this possibility in the minutes of the July 2025 FOMC meeting.

costly in normal times but provides an incentive for participation when markets are severely disrupted.[19]

Federal Safety Net and the Regulatory Perimeter: Another common issue that arises in connection with contingency programs is the extent to which liquidity support may be provided to entities over which the central bank has little or no supervisory or regulatory oversight. In the most extreme circumstances, this type of issue often arises in lending to nonbank institutions under the Fed's 13(3) emergency lending authority. But the issue arises as well even with more plain vanilla programs such as the Federal Reserve's standing repo operations. There are no statutory restrictions on the counterparties for open market operations. Temporarily expanding access to standing repo operations to a broader range of Treasury market participants could be helpful in addressing a crisis; on the other hand, if those new counterparties are not subject to federal oversight in some way, it could also be seen as an implicit extension of the federal safety net.

Levels of Preparedness: Standing, Contingency, or Inside the Four Walls: A fundamental issue in developing contingency plans for facilities that could address a period of severe financial distress revolves around the tension between the desire to be fully prepared for any contingency and the desire to avoid distorting incentives in financial markets. Fully preparing for various market contingencies would likely involve detailed discussion with market participants to develop operational plans including necessary legal documentation. On the other hand, making such detailed arrangements with market participants in advance may undercut incentives for market participants to take steps that would help to avert difficulties in the event of a crisis. This basic tradeoff is discussed in Hauser and Logan (2022) and speeches by policymakers.[20]

Against this backdrop, policymakers could opt for at least three levels of preparedness. The highest level of preparedness might involve creating an "always on" facility—like standing repo operations, FIMA repo operations, or the discount window—that are fully operational and ready to address any unusual funding needs. Apart from putting "foam on the runway" for any impending crisis, some have suggested that the ex-ante availability of such facilities can mitigate crisis pressures by providing certainty in advance about the availability of liquidity support and thereby avoiding market actions that might otherwise tend to exacerbate market strains.

Another approach might be to announce "contingent" facilities. The terms of such facilities could be specified in advance with counterparties identified and enrolled. However, the central bank would determine when the facilities become active. The Bank of England has followed this type

[19] See Alexander et al. (2023) and Hauser and Logan (2022).
[20] See Hauser and Logan (2022), Hauser (2023), and Logan (2023) for further discussion of many of these issues.

of approach in creating two contingency liquidity facilities.[21] Contingent liquidity facilities of this type might overcome many of the operational hurdles in getting a facility up and running quickly while also minimizing to some extent the degree to which the existence of the facility adversely distorts market incentives.

Finally, policymakers could follow an "inside the four walls" approach in developing contingency plans in which the Fed prepares fairly detailed plans for facilities but does not discuss any of the details of those plans with market participants in advance and does not announce anything in advance to the public about the facilities. By preserving "constructive ambiguity," this type of approach may pose the least risk of distorting market incentives. On the other hand, the approach would leave many important operational details to the last moment in a way that could delay implementation of the contingency plan.

The Confidence Factor: A particularly sensitive issue in developing contingency plans involving some sort of public announcement arises in judging whether the plans will provide welcome assurances to market participants and others or, conversely, may be seen as a sign of great concern in the official sector that shakes public confidence. In some cases such as the preparations in advance of Y2K, the potential risks of the event were widely discussed and the Fed's public contingency plans in that episode were viewed as supporting market confidence that liquidity would be available. In contrast, in past debt ceiling episodes, the FOMC has discussed various actions that could be taken but has generally avoided announcing plans in advance, partly because doing so might unsettle markets and also create a false impression that the Fed could do a great deal to address the financial and economic fallout of a government default. In the case of Fed contingency plans aimed at supporting Treasury market functioning during a period of stress, policymakers would likely be very focused on maintaining confidence in the Treasury market among investors and the general public. The views of market participants and others would likely inform the Fed's views about appropriate actions and how best to communicate its plans.

Concluding Comments: Two Overarching Risks

As discussed above, the Fed has a range of tools it could deploy to help to mitigate the effects of a severe disruption in Treasury markets. Developing contingency plans for the use of these tools in a period of market stress would involve a number of policy choices and points on which policymakers would likely debate the pros and cons of various options. On top of these

[21] For details, see discussion of the Contingent Term Repo Facility (CTRF) and the Contingent Non Bank Financial Institution Repo Facility (CNRF). The CNRF opened for enrollment in 2025 and is specifically designed to address periods of dysfunction in the U.K. sovereign debt market by providing repo financing against gilt collateral to entities beyond the BoE's usual counterparties—insurance companies, pension funds, and investment funds.

challenges, the Fed will need to balance two overarching risks in contemplating contingency plans and possible actions.

Over recent decades, the Congress has repeatedly expressed deep concern about the Federal Reserve's actions in financial markets, particularly in the realm of emergency lending. A very forward-leaning contingency posture in which the Federal Reserve announced that it stood ready to provide support to a wide range of entities active in Treasury markets could prompt concerns in some quarters that it was becoming enmeshed in fiscal policy and aligning itself with the interests of large financial firms. Moreover, in some cases, a very forward-leaning posture could create adverse incentives in financial markets to assume greater risks than would otherwise be the case. These types of concerns could erode Federal Reserve independence over time.

On the other hand, being unprepared or ineffective in addressing a period of severe stress in Treasury markets carries risks as well. The repercussions in financial markets and the economy could be severe, threatening the Fed's ability to achieve its long-run objectives of maximum employment and stable prices. The fallout for the Fed stemming from a failure to address a critical liquidity issue in the Treasury market could also undermine the Fed's credibility and independence over time.

So, as is often the case, there's no easy path for the Fed. Given the fiscal outlook, balancing these risks is likely to be a key challenge confronting Fed policymakers for many years to come.

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