FRBSF Economic Letter

2025-02 | January 13, 2025

Research from the Federal Reserve Bank of San Francisco

Ben Bernanke: Solving a Crisis, Changing the Fed

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Ben Bernanke's contributions to economic thinking have been vast, from his extensive study of the Great Depression to groundbreaking research on the interplay of finance and the macroeconomy and the usefulness of unconventional monetary policy tools. His research helped guide his tenure as Federal Reserve Chair and his role in putting the U.S. economy on a path to the longest expansion in its history. Through that role, he also built a better and more transparent Fed for the future. The following remarks are adapted from a presentation by the Federal Reserve Bank of San Francisco president, who joined Christina Romer (University of California-Berkeley), Mark Gertler (New York University), Emi Nakamura (University of California-Berkeley), and Peter Rousseau (Vanderbilt University) to discuss Bernanke's legacy at the American Economic Association Annual Meeting in San Francisco on January 5.

It's an honor to be part of this esteemed panel celebrating Ben Bernanke's contributions to economics. I will discuss Ben's time as Chair of the Federal Reserve.

Let me begin by taking you back to March 2009. We were deep into a financial crisis that many feared would turn into another Great Depression. Jobs were vanishing by the millions, foreclosures were devastating neighborhoods, and the country was teetering, consumed by uncertainty and fear. Trust in institutions was fragile. Hope felt distant.

And then something remarkable happened. Ben Bernanke, Chair of the Federal Reserve, stepped away from policy meetings, discussions with financial markets, CEOs, and global leaders, and sat for an interview with 60 Minutes. The interview was double-length, largely unscripted, and reached 13 million viewers (Bauder 2009).

For many watching, it was their first encounter with the person at the center of the Federal Reserve's response to the crisis. The Chair explained the actions the Fed had taken and why they were critical for preserving jobs, homes, businesses, and communities. Why they mattered for Main Street, not just Wall Street.

What people saw that evening, was a calm, competent, and steady voice working to restore economic stability and prosperity for the nation. They saw Ben Bernanke: A real person working for real people.

Early days

Now, the thing that we know as economists and students of the Fed is that the words Ben spoke that evening to inform a frightened nation flowed from a foundation of research he had been doing for years.

Ben had long been a student of the Great Depression and how the Fed could use its tools more effectively to ensure economic and financial stability. He had also been a prominent proponent of greater openness from the Federal Open Market Committee (FOMC), arguing that more direct and transparent Fed communications would improve policy effectiveness, and be more consistent with the democratic principles of our nation.

So, when he became the Chair in February 2006, he immediately put some of these ideas into practice.

One of the first changes he made was in the speaking order at the FOMC meetings. Chairman Greenspan used to begin the FOMC policy discussion by telling participants what he was thinking. Committee members would then follow and share their views.

Ben flipped the script. He asked participants to go first, and then he shared his views, generally preceded by a summary of what he had just heard from his colleagues (see FOMC Meeting Transcript, March 27-28, 2006 and Bernanke 2016).

Now this may sound insignificant, but for an organization steeped in hierarchy it was a sea change. It invited more interactive discussions, laid the groundwork for competing ideas, and fostered more vigorous debate. Most importantly, it built a practice, a commitment to collaboration and reasoned disagreement.

It changed the culture.

By his second meeting, Ben had momentum, and he made another change. He announced that Governor Don Kohn would lead the Federal Reserve's first subcommittee on FOMC communications. The committee would be tasked with considering ways to increase the transparency and clarity of FOMC decisions and intentions.

As the meeting transcripts reveal, under Ben's leadership this committee discussed adopting an explicit inflation target, improving FOMC post-meeting statements, and putting out more regular participant forecasts. Each of these ideas, raised in the early months of Ben's tenure, was eventually adopted and continue to serve us well.

Thinking back on those early days when Chairman Bernanke first took office, what I remember most is a new sense of camaraderie. That everyone could offer their best thinking and ideas, debate them to the fullest, and find a solution that served the nation and our mission.

In other words, long before we had a financial crisis, Ben was changing the Fed.

Crisis management

We all know what happened next. By Ben's second year as Chairman, cracks in the subprime mortgage market started to emerge and spill over to the broader economy. In the summer of 2007, several investment firms suspended withdrawals from their subprime mortgage funds, noting that the assets could no longer be valued.

Markets panicked.

Ben called two emergency meetings of the FOMC. The committee first pledged liquidity to facilitate the orderly functioning of financial markets (Board of Governors 2007b, c). They then issued a statement noting that the financial and economic situation had worsened and began lowering the federal funds rate at the next meeting. By the end of the year, the Fed had opened the first of many lending facilities, and a currency swap line with other central banks (Board of Governors 2007a).

The actions taken in 2007 were well within the normal course of business for the Fed. Providing liquidity to depository institutions with good collateral, facilitating dollar liquidity internationally, and easing monetary policy to support the economy.

But as the crisis unfolded, it wasn't enough. And Ben knew it. Years of research helped him recognize the risks to the financial system and the economy. He could see the perilous situation we were in.

So he did more.

No holds barred

Ben took extraordinary actions to prevent the crisis from turning into another Great Depression. He took these actions against intense public scrutiny and no shortage of critics. It was not the world where he was celebrated. It was the world where he was questioned. He took them while angry at the firms that had irresponsibly dragged the nation into the crisis. (For example, see Bernanke 2015 for discussion of AIG.) And he took them knowing that they were largely untested.

But he took them anyway, recognizing that the cost of doing nothing far outweighed the cost of trying.

The actions fell into three categories: extensive use of the Fed's emergency lending authority, asset purchases or quantitative easing, and forward guidance, a specific type of Fed communication. I will touch on each.

Facilities

Let me start with the emergency facilities. Counterparty risk had spread throughout the economy and paralyzed the financial system, and banks alone were not able to fully facilitate liquidity provision. So, the Fed invoked a rarely used power—Section 13(3) of the Federal Reserve Act—to serve as the lender of last resort to nonbank institutions and nonfinancial borrowers in unusual and exigent circumstances. Over the crisis, the Fed opened six of these facilities, supporting funding needs for primary securities dealers, money market mutual funds, commercial paper markets, and purchasers of securitized loans.

These facilities were lifelines. They provided relief to disrupted markets and ensured that financial frictions didn't spiral into a full-blown collapse.

But some damage had already occurred, and that is where unconventional policies came in.

Quantitative easing

By December 2008, the federal funds rate was essentially at zero. There was no more room for conventional policy easing. But the economy was in great need. Job losses and unemployment were rising, and businesses were closing.

So, the Fed began large-scale asset purchases or quantitative easing (QE). QE allowed the Fed to use its balance sheet as a policy tool.

Although new to the Fed's toolkit, it was not a new concept to Ben. Ben had studied the theoretical and empirical underpinnings of QE as a method of supporting the economy when the policy rate reached its effective lower bound, as in Japan (Bernanke, Reinhart, and Sack 2004). He recognized its theoretical limitations but believed it could be effective in practice. During the course of the financial crisis and its aftermath, the Federal Reserve completed three rounds of QE.

People have different views on how well it worked, but for the millions of Americans who needed the economy to get better, QE was successful.

But as we all know, the job still wasn't done.

Forward guidance

Fully recovering from a financial crisis is challenging and takes a protracted period of monetary policy support. Holding rates lower for longer.

The question was how to ensure that markets and the broader public understood this and set their expectations accordingly. After all, as Ben had long known, expectations play an important role in determining financial conditions and behavior (Bernanke 2004).

The FOMC had already released forward guidance in its December 2008 FOMC statement (Board of Governors 2008). In 2009, policymakers strengthened that language and added long-run forecasts for economic growth, inflation, and the unemployment rate to their public projections (Board of Governors 2009a,b).

In 2012, the FOMC became even bolder. The Committee provided very specific conditions under which it would first consider raising the policy rate. This state-based guidance was very effective in lowering long-

term interest rates and easing financial conditions. It built on the "date-based forward guidance" introduced in August 2011, which explicitly stated how long the policy rate was likely to remain at the zero lower bound.

None of this was easy to do. Policymakers do not like having their hands tied. And many worried that this would undermine credibility and even risk accelerating inflation. But Ben worked with his FOMC colleagues and fashioned a plan that ultimately did its job.

Coming out of the recession, the U.S. economy grew significantly faster than its peers in the eurozone, the United Kingdom or Japan. The expansion that began during Ben's term as Fed Chairman turned into the longest in U.S. history.

Groundwork for a better future

As the crisis abated and the recovery began, Ben continued to lay the groundwork for a better and more transparent Fed.

In April 2011, he conducted the Fed's first ever post-FOMC press conference.

In January 2012, the Fed formalized its 2% inflation goal. It also released its first annual Statement on Longer-Run Goals and Monetary Policy Strategy (Federal Open Market Committee 2024). And it added the now famous "dot plot" to the Summary of Economic Projections.

Individually, these were groundbreaking changes. Together, the new policies and approaches to policymaking that began in 2006 constituted a major shift for a century-old institution.

To the outside world, Ben's legacy is built on financial rescue and the tools that made it possible: Fed facilities, QE, forward guidance, an inflation target, better communications…I could go on. Ben rightfully gets credit for saving the world.

There's another part of his legacy that is worth celebrating. It is his imprint on the Federal Reserve. The practice of good faith debate. The commitment to transparency. The idea that trust is our most important tool, and integrity our most important value.

And more than any one program or policy, Ben imbued the Fed with a sense of dynamism. Of innovation, of agility, of the ability to meet what is in front of us with our best thinking. He changed our institutional DNA, allowing us to move slowly, gradually when it's appropriate. To move swiftly and take smart risks when needed.

In the end, during his tenure as Chair, he solved a financial crisis, he put us on a path toward the longest expansion in our history, and, maybe as importantly, he changed a culture. That is his legacy.

So, Ben, departing from the normal rules of Fed engagement, I will say on behalf of *all* of us at the Federal Reserve, current and former, thank you.

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