Hal Scott – Stigma and the Discount Window

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It is commonly asserted that stigma associated with borrowing from the discount window ("window") potentially limits the effectiveness of the Fed's lender of last resort function. This raises two distinct questions that require further research. First, do banks not borrow from the window because of stigma? And second, even if this is true, does this reluctance increase the probability of a bank-run and financial contagion?

With respect to the first question, factors other than stigma can account for reluctance to borrow at the window — in particular the terms of borrowing at the window compared to alternatives. The two basic alternatives to the window are the interbank federal funds market and advances from the Federal Home Loan Banks ("FHLBs").

Interbank Federal Funds Market

Borrowing in the interbank federal funds market is no longer significant, as daily transaction volume now averages $2-4 billion compared with more than $100 billion before the 2008 Global Financial Crisis ("GFC"), largely due to the existence of ample bank reserves.[1] The window rate is also deliberately set higher than the Federal Open Market Committee's target rate and, therefore, typically exceeds the Fed funds rate.[2]

Although a recent New York Fed staff report found evidence of stigma because certain banks borrow in the federal funds market at rates above the discount window's primary credit rate, this study has important limitations. First, given that the Fed funds rate is generally lower than the window rate, this finding appears to be driven by a narrow subset of idiosyncratic transactions.[3] Second, comparing the federal funds rate directly with the discount window rate is not a like-for-like comparison, because differences between the terms of borrowing may explain a bank's willingness to pay a federal funds rate higher than the window rate for reasons unrelated to stigma. Most notably, discount window loans must be collateralized, whereas federal funds borrowing is unsecured.[4]

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[1] BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM ["FEDERAL RESERVE"], *Bankers' Banks and their Role in the Federal Funds Market* (Jan. 30, 2026), https://www.federalreserve.gov/econres/notes/feds-notes/bankers-banks-and-their-role-in-the-federal-funds-market-20260130.html; FEDERAL RESERVE, *The Recent Evolution of the Federal Funds Market and its Dynamics during Reductions of the Federal Reserve's Balance Sheet* (Jul. 11, 2024), https://www.federalreserve.gov/econres/notes/feds-notes/the-recent-evolution-of-the-federal-funds-market-and-its-dynamics-during-reductions-of-fr-balance-sheet-20240711.html.

[2] Olivier Armantier, et al., *Discount Window Stigma After the Global Financial Crisis*, FEDERAL RESERVE BANK OF NEW YORK Staff Report No. 1137 (2024, revised 2026), https://www.newyorkfed.org/medialibrary/media/research/staff_reports/sr1137.pdf. ("[T]o prevent the DW from becoming a substitute for the market, a penal rate was set at a spread over the Federal Open Market Committee's target rate."].

[3] *Id*. (For example, in the year following the 2023 banking turmoil, 48.6% of the federal funds purchased by banks with less than $50 billion in assets were at rates above the primary credit rate, compared to 1.6% for all banks).

[4] *Compare* FEDERAL RESERVE BANK OF NEW YORK, *Effective Federal Funds Rate*, https://www.newyorkfed.org/markets/reference-rates/effr (last visited Aug. 7, 2026) ("The federal funds market consists of domestic unsecured borrowing…") with FEDERAL RESERVE, *Discount Window Lending* (Jun. 30, 2026),

Federal Home Loan Banks

A more significant source of alternative funding for banks is borrowing from the FHLBs. The volume of FHLB advances typically exceeds that of window borrowing. Total FHLB advances are currently about $463 billion compared to $5.2 billion in current window borrowing.[5] Another point of comparison is March 2023 during the banking crisis when FHLB advances were $804 billion compared to $152 billion in window borrowing.[6]

Numerous non-stigma factors could account for the greater usage of FHLB advances relative to window borrowing. For example, FHLB rates are typically lower than the window.[7] And although borrowing from the FHLBs requires collateral like the window, the eligible collateral, applicable haircuts, and available borrowing maturities may often be more favorable than at the window.[8] Such a comparison would also have to consider that there is one set of terms for window borrowing for all Federal Reserve Banks, whereas different FHLBs have different terms.[9]

No thorough comparison of the terms of window, Fed funds, and FHLB borrowing has been done.

The Role of Stigma During Financial Stress

The possible role of stigma is most important as it relates to a bank's decision to borrow during periods of stressed liquidity or contagion, when banks may fail or are failing, rather than during normal periods. It is the failure of a financial institution (as illustrated by Lehman Brothers in the GFC and SVB during the 2023 bank crisis) that often sets off financial contagion,[10] and the primary function of the window is to prevent and contain such contagion. The question of whether stigma associated with the use of the discount window increases the likelihood of bank failures and contagion needs further examination. Establishing such a relationship would require showing that banks are deterred from borrowing even when doing so is necessary to avert their own failure.

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https://www.federalreserve.gov/regreform/discount-window.htm ("All discount window loans must be collateralized…").

[5] *Compare* FEDERAL RESERVE BANK OF ST. LOUIS, *Balance Sheet: Total Liabilities and Capital: FHLB Advances* (Q1, 2026), https://fred.stlouisfed.org/series/QBPBSTLKFHLB with FEDERAL RESERVE BANK OF ST. LOUIS, *Assets: Liquidity and Credit Facilities: Loans: Primary Credit: Wednesday Level* (Aug. 5, 2026), https://fred.stlouisfed.org/series/WLCFLPCL.

[6] *Compare* FEDERAL RESERVE BANK OF ST. LOUIS, *Balance Sheet: Total Liabilities and Capital: FHLB Advances* (Q1, 2023), https://fred.stlouisfed.org/series/QBPBSTLKFHLB with FEDERAL RESERVE BANK OF ST. LOUIS, *Assets: Liquidity and Credit Facilities: Loans: Primary Credit: Wednesday Level* (Mar. 15, 2026), https://fred.stlouisfed.org/series/WLCFLPCL.

[7] *See* Anil K Kashyap, *Interactions Between the Discount Window and FHLB Contingent Lending* (Oct. 30, 2025), https://www.dallasfed.org/-/media/documents/research/events/2025/25bankfunding/25bankfunding-kashyap.pdf

[8] *Id*. (noting the complex interaction between FHLB and discount window borrowing and raising questions for further analysis).

[9] Darryl E. Getter, *The Federal Home Loan Bank (FHLB) System and Selected Policy Issues*, CONGRESSIONAL RESEARCH SERVICE (Jul. 14, 2026), https://www.congress.gov/crs-product/R46499.

[10] Hal S. Scott, *Connectedness and Contagion: Protecting the Financial System from Panics*, THE MIT PRESS (May 13, 2016).

Existing analyses do not distinguish between stigma deterring routine borrowing and stigma that results in the delay or failure of a bank to seek liquidity needed to avert its failure. In particular, a New York Fed staff report on discount window stigma during the GFC estimates the economic cost of stigma based solely on the additional interest expense some banks incurred to obtain liquidity through the Fed's Term Auction Facility, the asset-backed commercial paper market, and the repo market rather than the window.[11] It does not, however, examine whether these alternative borrowings, even if motivated by avoiding window stigma, were a causal factor in bank failures or exacerbated the broader financial crisis by depriving banks of needed liquidity. Indeed, a 2012 report prepared by Bill Winters at the request of the Court of the Bank of England acknowledges this distinction in its review of the functioning of the Bank of England's liquidity facilities during the GFC, and notes that it is unclear whether stigma-related reluctance to borrow resulted in greater systemic risk.[12] The discussion offers some anecdotal evidence that this may have occurred but does not engage in a systematic analysis of the question.[13]

The 2023 SVB episode suggests that banks may in fact quickly overcome any possible stigma against window borrowing when a liquidity crisis becomes existential. SVB sought to borrow from the window before its failure, and it was operational issues and collateral policies that prevented it from doing so.[14] Moreover, aggregate window borrowing from other banks increased from $4.6 billion on March 9, 2023 (the day before SVB was placed in receivership), to $152 billion as of March 15, 2023, as other banks faced stress.[15] Discount window borrowing only subsided when the Fed established the alternative Bank Term Funding Program ("BTFP") with better terms. The substantial take-up of the BTFP during a period of contagion suggests that borrowing from that facility was not deterred by stigma – even though it was, like the window, a Fed facility.[16] It is more likely that rather than window stigma, borrowing instead shifted to the BTFP due to better terms and collateral policies than were available at the window.

Conclusion

In conclusion, a new study is needed to determine whether stigma specifically deters discount window borrowing, either generally, on the eve of, or during a crisis, and if so whether the reluctance to borrow under any of these three circumstances creates financial instability.

[11] Olivier Armantier et al., *Discount Window Stigma during the 2007-2008 Financial Crisis*, FEDERAL RESERVE BANK OF NEW YORK Staff Report No. 483 (2011, rev. 2015), https://www.newyorkfed.org/medialibrary/media/research/staff_reports/sr483.

[12] Bill Winters, *Review of the Bank of England's Framework for Providing Liquidity to the Banking System*, COURT OF THE BANK OF ENGLAND (2012), https://www.bankofengland.co.uk/-/media/boe/files/news/2012/november/the-banks-framework-for-providing-liquidity-to-the-banking.pdf.

[13] *Id*. at 65 ("It is clear that during the Crisis, banks facing liquidity problems took precisely the actions listed above. [excess self-insurance and pledging assets to lenders at shorter maturities] But it is difficult to distinguish how much was due to reluctance to access central bank facilities.).

[14] Hal Scott and Connor Kortje, *Lender of Last Resort: Lessons from the 2023 Banking Crisis* 30 STAN. J.L. ECON. & BUS. 349, 351 (2025), https://law.stanford.edu/publications/lender-of-last-resort-lessons-from-the-2023-banking-crisis/.

[15] *Id*. at 383.

[16] *Id*.