

# TEN

FEDERAL RESERVE BANK OF KANSAS CITY

Fall 2005

Inside:

Developing  
Bricktown

Rural Education

Mortgage Lending

Data Security

**THE  
GREENSPAN  
ERA** Lessons for  
the Future



# On The Cover:



# TEN

FALL 2005

## **THE GREENSPAN ERA LESSONS FOR THE FUTURE..... 18**

During his years at the helm of the Federal Reserve System, Chairman Alan Greenspan has been at the center of discussions on monetary policy ideas and issues. This year the Federal Reserve Bank of Kansas City's 29th economic policy symposium focused on lessons of his tenure and how they can guide central bankers for years to come.

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## The Jackson Hole Symposium

The Federal Reserve Bank of Kansas City hosted its 29th annual economic policy symposium in late August. Once again, our Bank was honored to host in the Tenth Federal Reserve District a distinguished gathering of central bankers, policymakers and economists.

Over the years, we believe the symposium has provided a valuable forum for the exchange of ideas on important public policy issues of interest to central banks around the world. The symposium's continuing success is due to the contributions of all those who participate, including authors of the papers presented during the symposium, discussants, panelists and audience members.

Generally, the symposium does not focus on the immediate issues facing policymakers. Instead, we look to create a discussion about the broad issues that monetary policymakers around the world will face in the months and years to come. Symposium topics in recent years have ranged from the economic impacts and policy challenges of global demographic change, to economic policy for the information economy.

This year's event, "The Greenspan Era: Lessons for the Future," was attended by leaders from 28 of the world's central banks, a group literally spanning the globe from Argentina to China and including a number of U.S. Federal Reserve Bank presidents, governors and economists.

The origin of our economic symposium dates back to 1978 when the Bank hosted "World Agricultural Trade: The Potential for Growth" in Kansas City.

The symposium would retain its agricultural focus for the next three years until the initial monetary policy symposium was held in 1982.

"Monetary Policy Issues in the 1980s" was the first step toward the symposium's current structure. Held for the first time at our now-traditional location of Jackson Hole, Wyo., the 1982 symposium was the first to be attended by a Federal Reserve chairman, then Paul Volcker, and the first to include international central bankers, with presentations by representatives from the Bank of Canada and the Deutsche Bundesbank, the German central bank, which, in 1982, had the distinct address of West Germany.

In 1990, the symposium provided policymakers with a unique opportunity months after the world witnessed the fall of the Berlin Wall. "Central Banking Issues in Emerging Market-Oriented Economies" included presentations by seven Eastern European central bankers and the chairman of the board of the State Bank of the U.S.S.R. that focused on economic reform programs underway in each of those nations. Presentations from Western economists were focused on possible solutions to the problems identified by the central bankers. At a unique juncture in world history, the 1990 symposium helped to further the dialogue between policymakers in the East and West.

Policymakers were again offered a unique opportunity during our 1997 symposium, "Maintaining Financial Stability in a Global Economy." Although the symposium had been

—continued on page 2



## President's message cont.



Jackson Hole, Wyo., home to the Federal Reserve Bank of Kansas City's economic symposium.

—continued from page 1

in the planning for nearly a year, the event was held only a month after the devaluation of Thailand's currency—the starting point of what would become known as the Asian currency crisis. Against this backdrop, the presentations at our 1997 event, including those by central bankers from Argentina, Japan and Sweden that focused on previous financial crises in each of those nations, were especially significant.

You can read the full proceedings from the 1997 symposium, as well as proceedings from each of our symposiums since 1995, on the Bank's website: [www.KansasCityFed.org](http://www.KansasCityFed.org). We are currently converting the proceedings from symposiums prior to 1995 into an electronic format and will be making them available on our website within the next few months. Meanwhile, you can read about this year's event in this issue of TEN.

THOMAS M. HOENIG, PRESIDENT  
FEDERAL RESERVE BANK OF KANSAS CITY

## Federal Reserve Bank of Kansas City Symposium Series

- 1978 World Agricultural Trade: The Potential for Growth (Kansas City)
- 1979 Western Water Resources: Coming Problems and the Policy Alternatives (Denver, Colo.)
- 1980 Future Sources of Loanable Funds for Agricultural Banks (Kansas City)
- 1981 Modeling Agriculture for Policy Analysis in the 1980s (Vail, Colo.)
- 1982 Monetary Policy Issues in the 1980s (Jackson Hole, Wyo.)\*
- 1983 Industrial Change and Public Policy
- 1984 Price Stability and Public Policy
- 1985 The U.S. Dollar—Recent Developments, Outlook and Policy Options
- 1985 Competing in the World Marketplace: The Challenge for American Agriculture (Kansas City)
- 1986 Debt, Financial Stability and Public Policy
- 1987 Restructuring the Financial System
- 1988 Financial Market Volatility
- 1989 Monetary Policy Issues in the 1990s
- 1990 Central Banking Issues in Emerging Market-Oriented Economies
- 1991 Policy Implications of Trade and Currency Zones
- 1992 Policies for Long-Run Economic Growth
- 1993 Changing Capital Markets: Implications for Monetary Policy
- 1994 Reducing Unemployment: Current Issues and Policy Options
- 1995 Budget Deficits and Debt: Issues and Options
- 1996 Achieving Price Stability
- 1997 Maintaining Financial Stability in a Global Economy
- 1998 Income Inequality: Issues and Policy Options
- 1999 New Challenges for Monetary Policy
- 2000 Global Economic Integration: Opportunities and Challenges
- 2001 Economic Policy for the Information Economy
- 2002 Rethinking Stabilization Policy
- 2003 Monetary Policy and Uncertainty: Adapting to a Changing Economy
- 2004 Global Demographic Change: Economic Impacts and Policy Challenges
- 2005 The Greenspan Era: Lessons for the Future

\*After 1982 symposium, all events held in Jackson Hole except the second 1985 event held in Kansas City.



# Research on the Web

LOOK **ONLINE** FOR THESE PUBLICATIONS FROM THE FEDERAL RESERVE BANK OF KANSAS CITY

## ECONOMIC REVIEW

[www.KansasCityFed.org/EconomicReview](http://www.KansasCityFed.org/EconomicReview)

A quarterly research publication focusing on economic issues of relevance to the Federal Reserve, including macroeconomics and monetary policy, financial markets, regional and international economics, and rural economic studies.

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## MAIN STREET ECONOMIST

[www.KansasCityFed.org/MSE](http://www.KansasCityFed.org/MSE)

A monthly publication from the Bank's Center for the Study of Rural America focuses on issues facing rural America, its agricultural economy, and regional development.

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## FINANCIAL INDUSTRY PERSPECTIVES

[www.KansasCityFed.org/Perspectives](http://www.KansasCityFed.org/Perspectives)

An online periodical from the Supervision and Risk Management Division containing articles reporting on a variety of banking issues and topics.

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## PAYMENTS SYSTEM RESEARCH BRIEFING

[www.KansasCityFed.org/PSR-Briefing](http://www.KansasCityFed.org/PSR-Briefing)

Produced three times annually, the publication focuses on a range of payments topics, including methods of payments, developments in payments networks, and various participants' roles in the payments system.

**www.KansasCityFed.org**

# CLOSING THE GAP

COMMUNITY COLLEGES EMERGE AS ADVANTAGE FOR RURAL LEARNING

BY TONI LAPP, SENIOR WRITER

**J**onathan Fletchall of Pittsburg, Kan., is learning about motorcycle mechanics. Tyler Van Meter of Cheyenne, Okla., is learning about global positioning system technology used in tractors. Benson Begay of Gallup, N.M., is learning to advocate for victims in the Navajo Nation legal system.

While these rural students are pursuing diverse careers, what they have in common is their choice of educational institution: community colleges.

At these institutions, students can earn associate in applied science degrees, which confer very specific training tailored to an industry or avocation.

This route to gainful employment is being touted by some as the key to giving rural areas a competitive edge again. Jason Henderson and Stephan Weiler of the Center for the Study of Rural America at the Federal Reserve Bank of Kansas City report on the emerging trend in a research paper, "Rural America's New Path to Workforce Skills," summarized in the July 2005 *Main Street Economist*.

"Community colleges play a big role in economic development," says Weiler, assistant vice

president and economist with the Bank. "They provide precisely the skill-based degrees and certifications that fit the demand of employers."

Rural areas fight an incorrect perception that their residents are not as educated as urbanites, says Henderson, senior economist. On the contrary, rural residents are increasing their educational attainment, and they're doing so by learning skills that are practical in today's job market.

"If you only look at bachelor degrees, you're not seeing the whole picture," says Henderson. "Rural residents are increasingly ramping up their job skills with associate degrees."

In fact, if one looks at the percentages of the population obtaining associate degrees, the figure is higher for people from rural areas than for their metro counterparts.

In 1995, percentages of rural and metropolitan residents holding associate degrees were roughly the same: 8 percent for nonmetro residents versus 7.8 percent for metro residents. By 2004, the percentage acquiring associate or technical degrees had shot up 40 percent for nonmetro residents, compared with 14 percent for metro residents.

Perhaps one reason rural residents are discovering the value of two-year degrees is because that's where the action is.

In his research studying trends in U.S. job structure, Chad Wilkerson, a policy economist with the Federal Reserve Bank of Kansas City, says he was surprised to find that, according to

**THE HARLEY-DAVIDSON** training program of Fort Scott Community College is the only publicly offered program of its kind, says its director, Steve Vergara.





**HARLEY-DAVIDSON**  
Program director Steve Vergara and second-year student Patrick Dineen work on a motorcycle during class at Fort Scott Community College.

the latest projections by the U.S. Labor Department, jobs requiring an associate degree or vocational award are expected to grow slightly faster through 2012 than jobs requiring a bachelor degree.

“Having the right amount and right kind of education is important for success,” says Wilkerson. “We generally give the message that more education is always better, but the current demands of employers are causing us to rethink that message.”

His research can be found in the second quarter 2005 *Economic Review*.

### **An educational evolution**

Community colleges have evolved considerably since the first junior college was found-

ed in 1901. Then, the institutions were two-year liberal art schools that taught curriculum intended to transfer to baccalaureate degrees.

The term “junior college” fell out of favor as the colleges changed their missions to

## Top Five Fields of Study at Community Colleges

1. APPLIED HEALTH

2. SKILLED TRADES-INDUSTRIAL

3. PUBLIC SERVICES

4. INFORMATION TECHNOLOGIES

5. BUSINESS

SOURCE: American Association of Community Colleges

focus more on local economies and community development.

Today, most community colleges and technical schools offer a broad spectrum of academic and training programs including remedial education, traditional courses for degree-

seeking students on a budget and contract training customized for individual employers.

“Some of the evolution (of community colleges), like evolution in general, is borne of environmental necessity,” says Bill Scaggs, executive director of the Rural Community College Alliance in Meridian, Miss. “It’s difficult to operate a thriving institution in a declining community.”

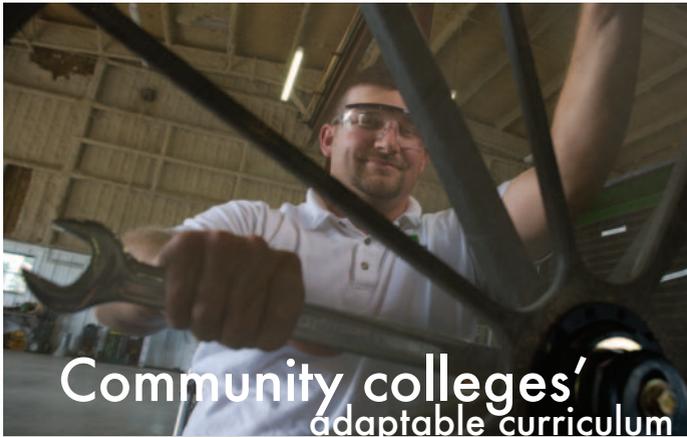
As technology becomes more sophisticated, high school graduates are no longer sufficiently prepared to enter the workforce, says Stuart Rosenfeld of Regional Technical Strategies, Inc. (RTS), a nonprofit organization in Carrboro, N.C. that does policy research analysis into workforce and economic development. Community colleges are

adept at teaching technical skills that employers need, he says.

RTS was founded with a mission to improve the economic vitality of the rural areas that were losing their industry, says Rosenfeld. Community colleges emerged as an underappreciated asset. Some had created “advanced technology centers” that worked with machine builders and software designers and offered training for small- and medium-sized businesses from expert faculty.

Community colleges were well-positioned for this kind of training because they are less research oriented and more accessible than universities, says Rosenfeld.

One strategy RTS has employed in invigorating areas is building business “clusters.” The idea is that businesses, suppliers, professional associations and educational institutions congregate in one area, creating synergy. Examples abound—Detroit and automobiles, North Carolina and furniture, Wichita and aerospace, to name a few.



The American Association of Community Colleges (AACC) tracks the popularity of programs offered by its member institutions. Not surprisingly, health care, designated by the Bureau of Labor Statistics as having great growth potential, led the field, says Sara McPhee, research associate.

Following health care, skilled trades programs were the next-hottest fields of study, she says. As such, these programs—in construction, agriculture and manufacturing—were among the most commonly added to the offerings of community colleges. But interestingly, these programs were also the most frequently discontinued, according to AACC. How can this be?

“This demonstrates the way in which community colleges respond to the needs of local communities,” says McPhee. “As a manufacturing plant in one community closes down, a manufacturing plant may be opening in another community. The residents in the first community no longer need their community college to offer a manufacturing program, whereas the company opening the plant in the second community wants the local college to open a program as soon as possible.”

This is a concept that rural areas can also employ, say the economists from the Center for the Study of Rural America.

“Community colleges can be vital cogs to evolving clusters by ratcheting the existing skill base of a local area,” says Weiler.

## Think locally

John Deere began partnering with community colleges in 1989, after dealerships—largely in rural areas—gave corporate officers feedback on the need for a quality workforce.

“Our dealers were telling us they needed a good resource for well-trained technicians,” says Kenneth Buell, manager of college partnerships for the tractor manufacturer. The first site for the two-year program was Southeast Community College in Milford, Neb. The program has been so successful that the company now sponsors sites at 16 community colleges in the United States. John Deere provides tools, equipment and instructor training to the schools.

Technical training is compulsory for anyone wanting to work on the tractors, many of which are equipped with GPS technology, Windows-based computer programs and remote capabilities. But the company also wanted its technicians to have a well-rounded education, hence the partnership with community colleges. Students are required to complete coursework in technical writing, personal finance and communications.

“We want our graduates to have a good career path,” says Buell. “It gives local people the chance to go back to their hometown and build a career.”

This is what appealed to Tyler Van Meter. The 21-year-old attended a four-year university for a year with the goal of earning a bachelor’s degree in industrial technology and someday teaching a high school shop class. But he began to rethink his plan after a summer job at a John Deere dealership close to home, where he learned about the program. The curriculum suited him, he says.

“It’s more hands-on than anything,” he says. “I like working with my hands more than sitting at a desk.”

But most important: “This way I get to stay close to home.”



**JOHN DEERE** began partnering with community colleges in 1989, after dealerships—largely in rural areas—gave corporate officers feedback on the need for a quality workforce.

## Targeting niches

While community colleges excel by targeting the needs of the region, not all the programs are technical in nature.

The Tribal Court Advocate Program taught at the University of New Mexico at Gallup, an institution that includes two-year and four-year programs, is emblematic of this. The associate degree program fills a very specialized need in that region: graduates are qualified to represent clients in the nearby Navajo Nation court.

Benson Begay, 40, a paralegal who is in the final semester of the program, says it fills a niche in the community. He speaks fluent Navajo and will be able to use his education to do what he does best: “I like to help people, and these are people who need help, who don’t understand laws and procedures (of the court),” he says. “I feel this is my way of giving back to the community.”

Community colleges often are seen as a more welcoming environment for nontraditional students.

Like Begay, Jonathan Fletchall is older than the traditional university student. Fletchall, 25, a former high school dropout who is married and has two children, says he felt he was languishing in a job as a fork-lift operator when he found out about Harley-Davidson’s pilot program at Fort Scott Community College in Frontenac, Kan. He recently spent the summer interning at a dealership, where he finished the assembly of bikes out of the box. The experience confirmed that he was on the right career path, he says.

“As my kids are getting older, I want to set a good example,” he explains. “Judging by the toys the mechanics here have, this will be a good job.”

Fort Scott program director Steve Vergara says his program is the only publicly offered one of its kind. As corporate sponsor, Harley-Davidson provides diagnostic equipment, motorcycles, parts and accessories, training manuals, and instructor training. The motorcycle giant was interested in a program that would give graduates “soft skills” for dealing with the increasingly affluent Harley owners, says Vergara. Graduates have the potential to follow a management career path with Harley-Davidson or work at dealerships. Some participants have aspirations to open repair shops back in their hometowns, so the program stresses entrepreneurship, he says.

This type of return on investment is what community colleges are all about. Says Henderson: “By helping local people invest in themselves, community colleges can be catalysts for rural regions seeking new economic opportunities in a globalizing economy.”

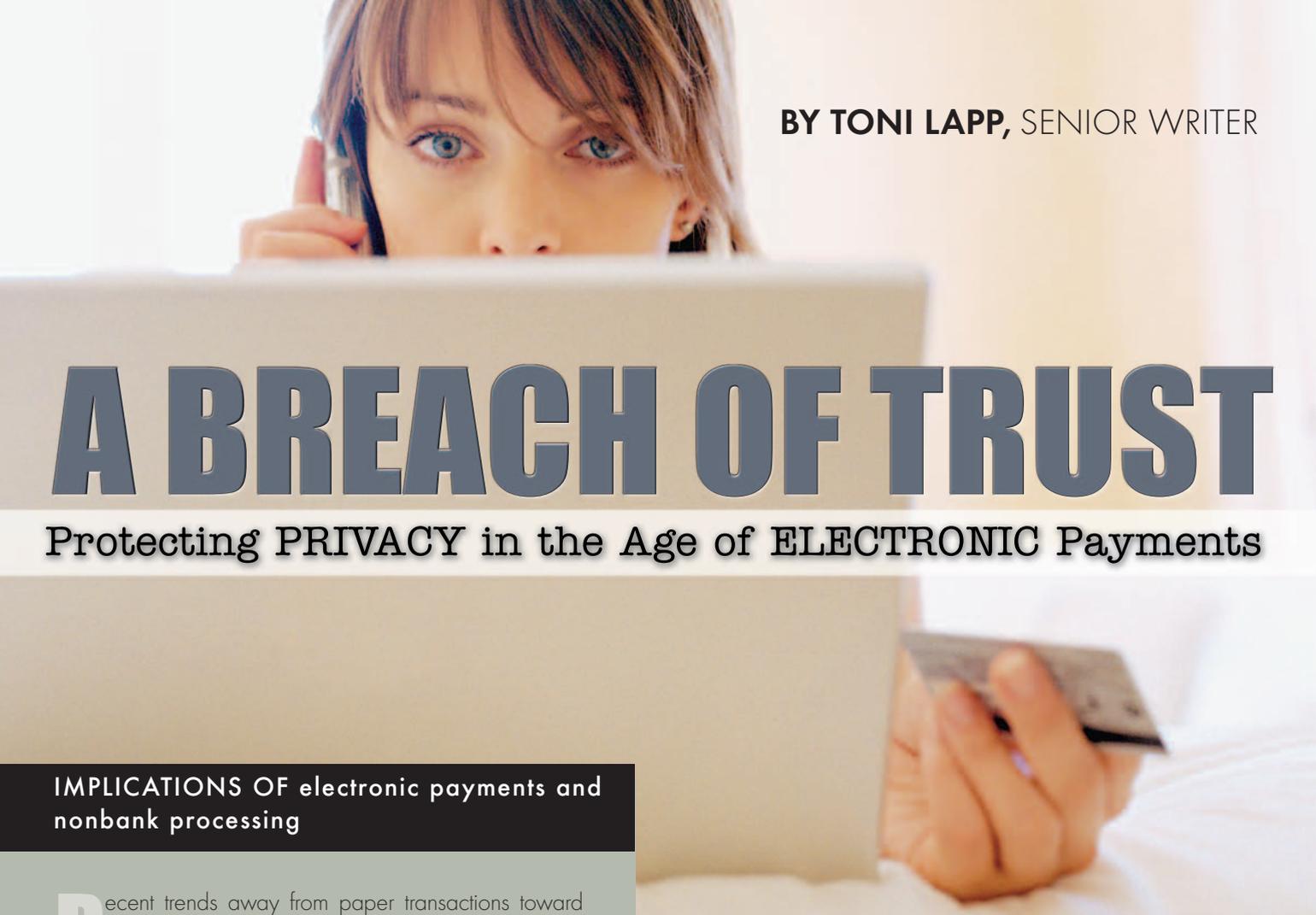
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## FURTHER RESOURCES

FOR FURTHER READING ON THE ROLE OF COMMUNITY COLLEGES IN RURAL ECONOMIC DEVELOPMENT GO TO:

[www.KansasCityFed.org/TEN](http://www.KansasCityFed.org/TEN)

**COMMENTS/QUESTIONS** are welcome and should be sent to [teneditors@kc.frb.org](mailto:teneditors@kc.frb.org).



BY TONI LAPP, SENIOR WRITER

# A BREACH OF TRUST

Protecting PRIVACY in the Age of ELECTRONIC Payments

## IMPLICATIONS OF electronic payments and nonbank processing

Recent trends away from paper transactions toward electronic payments and nonbank processing of retail payments are brought about by the desire to increase efficiency by exploiting economies of scale in payment processing, argues **Senior Economist Richard Sullivan** in his working paper **"The Supervisory Framework Surrounding Nonbank Participation in the U.S. Retail Payments System: An Overview."**

There are many implications to the increased reliance on electronic payment networks. The scale of operations and the interdependencies among elements of the network increase the potential for widespread disruptions.

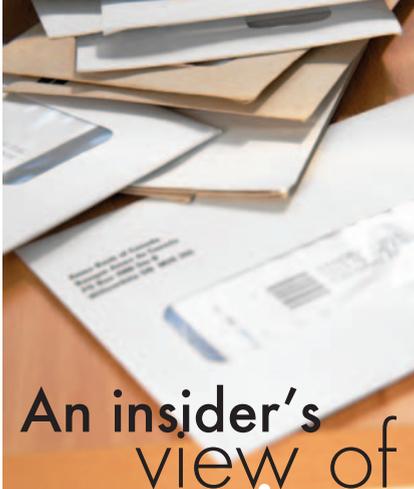
Sullivan's paper describes the supervisory structure over nonbank participants in the U.S. payments system and reviews how policy tools such as standards setting, disclosure, clarifying legal responsibilities, and supervision can each play a role in improving control of payments system risk.

TO ACCESS A PDF VERSION of the full document, published by the Payments System Research Department of the Federal Reserve Bank of Kansas City, go to [www.KansasCityFed.org/TEN](http://www.KansasCityFed.org/TEN).

The letter from the retailer was generic but polite, explaining that the company was investigating the theft of customer data that included credit card and debit card numbers. Midway through, the real purpose of the correspondence emerged: to notify the Designer Shoe Warehouse (DSW) customer that her account information was among the data stolen months before.

The same letter was sent to 1.4 million other customers who made purchases with charge cards or checks, including Federal Trade Commission chairwoman Deborah Platt Majoras.

Clearly, no one is exempt from the threat of breached data.



## An insider's view of security proposals

Joshua Peirez, senior vice president and associate general counsel at MasterCard International, was at the Federal Reserve Bank of Kansas City recently to address officials involved in supervision, research and operations at the Bank. Peirez, who has testified before Congress on the issue, spoke largely about risk in the payments system in the wake of recent data breaches.

### WHAT IS HIS VIEW OF PROPOSED LEGISLATION?

**THE PUNISHMENT NEEDS TO MATCH THE CRIME.** "It is critical that criminal penalties are increased to fit the magnitude of these crimes and that the crimes themselves are easy for law enforcement and prosecutors to prove," says Peirez.

**THE GRAMM-LEACH-BLILEY ACT**, with its requirements for storing sensitive data, should be expanded beyond defined "financial institutions," says Peirez. Any entity-retailers, marketers and payments processor that stores, transmits or uses sensitive consumer data also should have clear obligations to safeguard this data.

**HAVING A UNIFORM NOTIFICATION LAW** that provides consumers with notice both when they reasonably need it and in a way that they can make use of the information makes sense, says Peirez. It is important to work to find the right balance so that consumers are not overnotified or undernotified. It isn't easy to accomplish, but it is important, says Peirez.

The question of how to protect consumers' privacy has been around for years, long before a number of breaches this year resulted in millions of consumers' personal data being exposed.

When the issue came up in Congress, U.S. financial institutions favored an "opt-out" system that was put into law by the Gramm-Leach-Bliley Act in 1999. In other words, consumers who don't want their personal information to be shared must opt out in writing, a scheme that favors businesses who want to sell their customers' information. The law, known as GLBA, also established that financial institutions have a responsibility to protect "nonpublic" information such as account numbers and Social Security numbers.

As a result, some observers think GLBA has become a double-edged sword. Financial institutions asked for freedom to use the information, and now they have to bear the responsibility to protect it.

According to a recent working paper by Richard Sullivan, senior economist in the Payments System Research Department at the Federal Reserve Bank of Kansas City, data breaches are examples of operational risk in payments. Sullivan's paper discusses risk control in the U.S. retail payments system in light of the proliferation of electronic payments.

So how well are companies doing?

In the first half of 2005, 50 million accounts had been breached in a variety of incidents. More disturbing is that the issue has

moved beyond financial institutions and even their vendors, as the DSW case illustrates. The shortcomings of GLBA have been clear in many of these cases; the legislation, as currently written, only applies to financial institutions that deal directly with consumers.

"What's troubling me is a lot of the data that's a target for hackers is your account information; that's where the money is. And more of that information is in a more readily accessible form in financial and nonfinancial institutions as well as at retailers," said Sullivan.

### The weakest link

Identity fraud is actually on the decline. A 2005 study by a credit industry consultant found that in a year's time, 9.3 million American adults were victims of identity fraud, a 7.9 percent drop from a study in 2003.

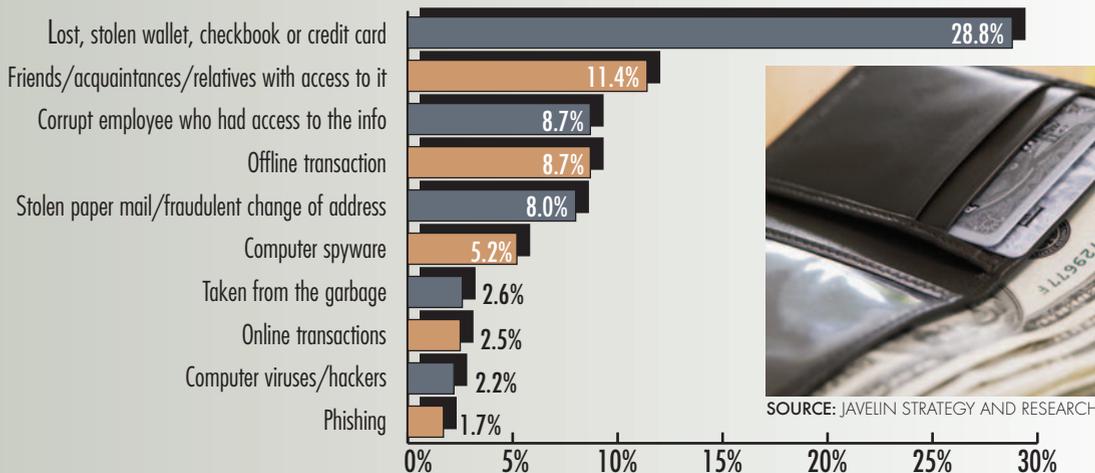
However, the mean cost of each theft increased 12 percent. Thieves are stealing more from their victims. The average out-of-pocket cost to the victim was \$652, and the time spent to resolve ensuing problems averaged 28 hours. Clearly, identity fraud is

costly, consuming money and time.

Thieves are going where the access is: the Internet. While identity theft in general is declining, attacks on Internet users appear to be increasing, based on a seven-year study by the Financial Crimes Enforcement Network. Reports of suspicious activity tied to Internet or online banking were on the rise by 2002.

A lot of publicity has been given to the

# Primary Methods of Identity Theft (From Known-Cause Cases)



risks posed by electronic payment methods; however, most thieves obtained personal information using “offline” methods—billfolds were lost or stolen, acquaintances or family members abused their access or mailboxes were compromised.

That said, a number of means for information to fall into the wrong hands exists in the world of electronic payments. The chart above shows the most common methods criminals use to access sensitive information.

processor, which acts as an intermediary between merchants and credit card issuers like MasterCard and Visa.

What of the protections mandated by GLBA? The law only applies to financial institutions providing services to consumers.

Because of the need for advanced technology in the era of electronics payments processing, outsourcers such as CardSystems have sprung up in recent years. The danger is that outsourcers add another step in the move-

**“ We have little systematic evidence on whether data breaches are occurring more or less in bank or nonbank organizations. ”**

With the growing complexity of technology and the increasing innovations in payment methods, it’s a reasonable public policy question to ask what rules regulators are creating to address changing security risks.

When national media reported earlier this year that 40 million credit cards stored by a technology service provider had been breached, it shed light on the potential for fraud when a customer makes a purchase with a charge card.

After all, such purchases involve a labyrinth of steps during which a weak link can be exploited by a thief.

The company responsible for the breach, CardSystems Solutions Inc., is a payment

ment of money, another place in a network for people to tap into.

As the number of outsourcers increases, so will the risk to the payments system.

So who’s watching for weak links?

In his paper, Sullivan describes the supervisory structure over providers of technology services to banks, which is administered by a little-known agency named the Federal Financial Institutions Examination Council, or FFIEC. FFIEC comprises members of all the federal agencies responsible for regulation and supervision of U.S. depository institutions, including the Federal Reserve System. The FFIEC assesses risk in providers of technology services to

# Modus Operandi

banks and coordinates examinations of the riskiest providers.

Typically, the team that reviews the firm comprises examiners from member agencies, such as the Federal Reserve, the Federal Deposit Insurance Corporation and the Office of Comptroller of the Currency. This ensures that the firm only undergoes one exam, but that all agencies are kept apprised of developments. This program reduces regulatory burden on a firm and improves supervisory efficiency.

Nonbank providers of payment processing services are part of the supervision program. The FFIEC risk assessment would likely place the largest payments processors in the supervision program, but due to limited information, resources and jurisdiction, only 125 payment processors are supervised, Sullivan notes in his paper.

CardSystems Solutions was one of about 500 payments processors; clearly many of these firms go unsupervised. Whether this poses much risk to payments is uncertain.

“We have little systematic evidence on whether data breaches are occurring more or less in bank or nonbank organizations or among supervised or unsupervised technology service providers,” says Sullivan.

## Public policy

Who should bear the costs of security breaches? When credit cards are used fraudulently for online purchases, merchants pay for the fraud, not the card issuer. Some argue that this gives little incentive for card issuers to implement anti-fraud measures. Similarly, cardholders may not have incentive to exercise vigilance when they are protected by loss limits.

To protect the payments system, analysts have proposed legal reform and regulation to rationalize liability and responsibility for risk in contracting relationships for payment processing. Lawmakers are considering more severe consequences for mishandling sensitive information.

It is likely that public disclosure will be addressed by future legislation. The CardSystems Solutions breach was discovered by Australian bank officials in late 2004, yet it wasn't report-

There are a number of methods  
**the criminally minded can employ ONLINE**  
to do harm:

**1 SPYWARE:** These are programs that, when installed on a computer, can change settings, display advertising, track Internet behavior and report information back to a central database. Spyware may be installed unintentionally by users, and can be very difficult to remove. This type of breach was responsible for 5.2 percent of cases of identity theft, the single most common online breach.

**2 PHISHING:** In this type of attack, an e-mail that appears to come from a legitimate company (for instance, eBay) is sent to recipients, who are asked to go to a site to update records and verify username and password. The site is actually a place to collect that information and steal identities, money, records and more. Phishing was cited in a recent study in 1.7 percent of identity theft cases.

**3 HACKING:** Many types of malfeasance—computer worms, Trojan horses and more—fall under this moniker. Hackers, a term used to describe criminals who subvert computer security without authorization, were responsible for about 2.5 percent of known cases of identity theft. CardSystems Solutions was victim to hacking.

ed in the United States until June 2005. Officials have declined to say when the FBI was notified.

What frustrates researchers trying to study the issue is the lack of cold, hard data. Out of millions of data exposures occurring this year, it is unknown how many resulted in actual losses to individuals.

The letter to the DSW customer intimidated as much: “We cannot know if your credit card or debit card will or will not be used by the thieves to commit fraud,” it said.

Sullivan says getting better information on these crimes should be a priority: “As a society we will have to deal with these things as they come along. You can't fix security problems until you know what they are and how bad they are.”

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**COMMENTS/QUESTIONS** are welcome and should be sent to [teneditors@kc.frb.org](mailto:teneditors@kc.frb.org).

# BRICKTOWN

BALLPARK





# ‘If you build it, they will come’

Entrepreneurship and community development

**BY TONI LAPP, SENIOR WRITER**

**I**t's a warm summer evening in Oklahoma City, and Mark Carmouche, a flamboyant water taxi driver, is telling his boatful of passengers about the downtown river walk they are traversing.

“This used to be a slum in here, a salvage operation,” the silver-haired captain says as he gestures to the buildings on both sides of the concrete banks. “But Oklahoma City got rid of all that and built this canal. Oklahoma City is a leader in downtown renewal.”

He queries to see what out-of-state visitors are on his boat and enthusiastically responds, “Yee haw,” when he learns there is a group of five from Brazil.

He goes on to tell the passengers about his city's Metropolitan Area

Projects plan—or MAPs, an acronym that most residents already know.

“We have no natural landmarks. No Rocky Mountains, no Atlantic Ocean and no Pacific Ocean. But this is Oklahoma City, and if you build it, they will come,” he declares. “It must be working; Brazil's here after all.”

Such optimism is typical in Oklahoma City's Bricktown neighborhood. It is a model that other communities could learn from, says an economist at the Federal Reserve Bank of Kansas City.

“Traditionally, communities have sought after large firms in developing their local economies, but research shows that this is not likely to be a successful policy,” says Kelly Edmiston of the



Community Affairs Department. “We have found that large firms ultimately do not bring as many jobs and benefits as expected when they relocate or open a new location. You have to consider what might have happened in the absence of the firm. Moreover, aggressive recruitment policies often set off bidding wars that leave everyone worse off. A better option is to create an environment conducive to entrepreneurship and home-grow your own economic success.”

Edmiston has written recently about his research on community development strategies in a paper titled “The Role of Small Businesses in Economic Development.” An entertainment district such as Bricktown offers just such an example of an environment conducive to entrepreneurs. The positive effect is felt in terms of both job creation and tax impact—by attracting a number of small businesses and creating a vibrant community in which people want to live and work.

A twist of fate gave impetus to Oklahoma City’s Bricktown District. In 1991, the city, then reeling from the 1980s oil bust, had put together a financial package in a bid for a United Airlines maintenance facility. City leaders had lobbied residents to pass a 33-month, one-cent sales tax to offer incentives to the airline.

Needless to say, officials were disappointed when they learned that the airline would build its facility in Indianapolis instead.

Then-Mayor Ron Norick was motivated



to tour downtown Indianapolis to see what it had that Oklahoma City didn’t.

“There were people downtown, restaurants, hotels—lots of activity, whereas Oklahoma City was struggling,” he said.

A seed of an idea was planted: Rather than wait for a company to come to the rescue of its blighted downtown, Oklahoma City would rebuild itself.

“We rolled the dice in an up or down proposal,” says Norick. “It was a gamble, but our people supported it. Every church group, neighborhood group, civic group got behind it. The thought was, ‘We’re doing it for our kids. We’re not doing it for jobs, but for ourselves.’”

In 1993, voters approved a sales tax increase that paid to build a baseball park, canal and performing arts center, upgrade the convention center and more—nine projects in all. Many more projects that followed were private.

“My plan was to put as much as we were going to spend on the aircraft plant into the downtown area,” says Norick. “To get hotels



and restaurants, we needed lots of activities in one area.”

## Mapping a future

Jim Cowan was one of the few entrepreneurs who gambled on Bricktown before anyone else did. Many people scoffed at his business plan for Bricktown Brewery, a micro-brewery and restaurant in the warehouse district, he said.

“This wasn’t a proven location, but there was excitement about what there could be,” he said. The hardwood floors, brick walls, open ductwork and exposed pipes of the turn-of-the-century building—once a candy factory—provided the atmosphere that Cowan wanted for his business. He opened in October 1992, the year before MAPs went to voters.

Business was lackluster, and rumblings about improving the area occurred in fits and starts. MAPs jump-started the movement.

“It didn’t happen fast enough for some of us,” says Cowan.

To be fair, Oklahoma City wasn’t starting from scratch. There was already a convention center downtown. Nearby, there were a lot of vacant brick buildings already owned by the city. Much thought was put into the projects MAPs would undertake. The SBC Bricktown Ballpark was the first project.

“Naturally, restaurants and clubs followed, because they’re going to go where the people are,” says Norick.

The theory that private investment follows public investment is proven time and again throughout the area, says Frank Sims, executive director of the Bricktown Association. Sims counts off on his fingers some of the other public projects that have figured into the



taxpayers’\$350 million contribution: the Ford Center Arena, a reconstruction of the Civic Center Music Hall and a public library. But get him to tally the litany of private investments that have followed and he runs out of fingers: two new hotels, an apartment complex, a Bass Pro Shops sporting goods store and country music star Toby Keith’s restaurant and nightclub, just to name a few.

The challenge as Bricktown continues to grow is to improve the mix of retail and residential to the abundance of nightclubs and restaurants, says Sims.

There is a sense that Bricktown is reaching critical mass.

One of the newest tenants is Nonna’s, a

# BRICKTOWN

## A lesson in community development

**B**ricktown might offer an example for other communities interested in fostering jobs and revenue.

The entertainment district came about in the aftermath of disappointment over the lost United Airlines contract. The money that was used to build Bricktown would not have been available had the city instead used the money to create financial incentives for the airline, says Ron Norick, the former mayor.

**“Aggressive courting of large firms can distort rational behavior, causing a waste of economic resources.”**

—Kelly Edmiston

With Bricktown, Oklahoma City has created an environment conducive to small business growth, says Federal Reserve economist Kelly Edmiston.

“Bricktown is likely to be self-sustaining, while a manufacturing plant in the global economy won’t be,” he said.

Ironically, the winner of the United Airlines contract, Indianapolis, did not realize a great boon from the maintenance facility. The jobs that were created did not reach the number promised by the airline, which filed for bankruptcy in 2002.

Yet, the bidding war for the maintenance facility is a strategy frequently pursued by communities.

“Aggressive courting of large firms can distort rational behavior, causing a waste of economic resources,” says Edmiston in his paper, “The Role of Small Businesses in Economic Development.”

Take the case of two competing regions that are otherwise on a level playing field, so that a

prospective firm is indifferent to locating in either jurisdiction, says Edmiston. Wherever it locates, it will create new jobs and income, but it will also generate additional costs to the region, which must provide roads, sewers and public services such as schools and police.

“Now consider that one of the regions offers to abate the locating firm’s property taxes, and the other region follows suit to stay competitive. The two regions are again on a level playing field.

“Neither region has gained an advantage by its aggressive recruiting, but the winning region will now be faced with increased costs but no property taxes to offset them,” Edmiston writes in his paper.

Like it or not, a relocating business is going to increase costs for the new area. Other businesses that don’t receive tax abatements will be left paying the bill, says Edmiston.

**T**



restaurant and gift store owned by Avis Scaramucci. She says initially she was skeptical about the MAPs plan.

“I was going to vote ‘no,’” says Scaramucci. “But MAPs passed, and lo and behold before our very eyes, things started happening. First the ballpark, then the library and museum. The building began.”

“I got so excited, I began coming down here and poking around. The buildings just caught my imagination.”

She eventually purchased a building near the canal and relocated her establishment from the south side of the city.

The decision was easy, she says.

cus largely on keeping down expenses such as taxes, land and labor. This focus has prompted them to move in large numbers, first to the South and then overseas, to contain costs.

“Now our economy is transitioning into something better,” says Edmiston. “We don’t need to, nor should we try to, keep these businesses from moving.”

Job growth is now in high-tech, high-paying industries. With these employers, the concern is more on finding qualified workers, he says.

“Anymore, businesses with high-skill, high-paying jobs are going to relocate where smart, creative people want to live,” he says.

**“Businesses with high-skill, high-paying jobs are going to relocate where smart, creative people want to live.”**

“How many times in your lifetime do you get to witness a renaissance in your own city?”

But she is not alone. Other entrepreneurs are opening businesses in what she describes as a “conglomeration of people and opportunity.”

“There are so many people down here, different people doing different things, and we come together as a neighborhood.”

### Quality of life

“When I think about Oklahoma City and Bricktown, the thing that impresses me is that the goal here was not to lure companies, but to create a nice place to live,” says Edmiston.

The indirect benefit of improving the quality of life was to make the city more enticing for business. This was demonstrated recently. In 2004, Dell opened a customer service center in Oklahoma City, a move that never would have happened before the downtown redevelopment, says Norick.

Events such as this reflect a shift in strategy in community development. Once upon a time, communities tried to develop a niche industry for themselves. Edmiston envisions something more organic happening—an environment that attracts bright people who bring their own niche ideas.

Traditionally, U.S. job growth is centered on manufacturing, he notes. Manufacturers fo-

This being the case, then Dell’s move can be viewed as a vote of confidence for Oklahoma City.

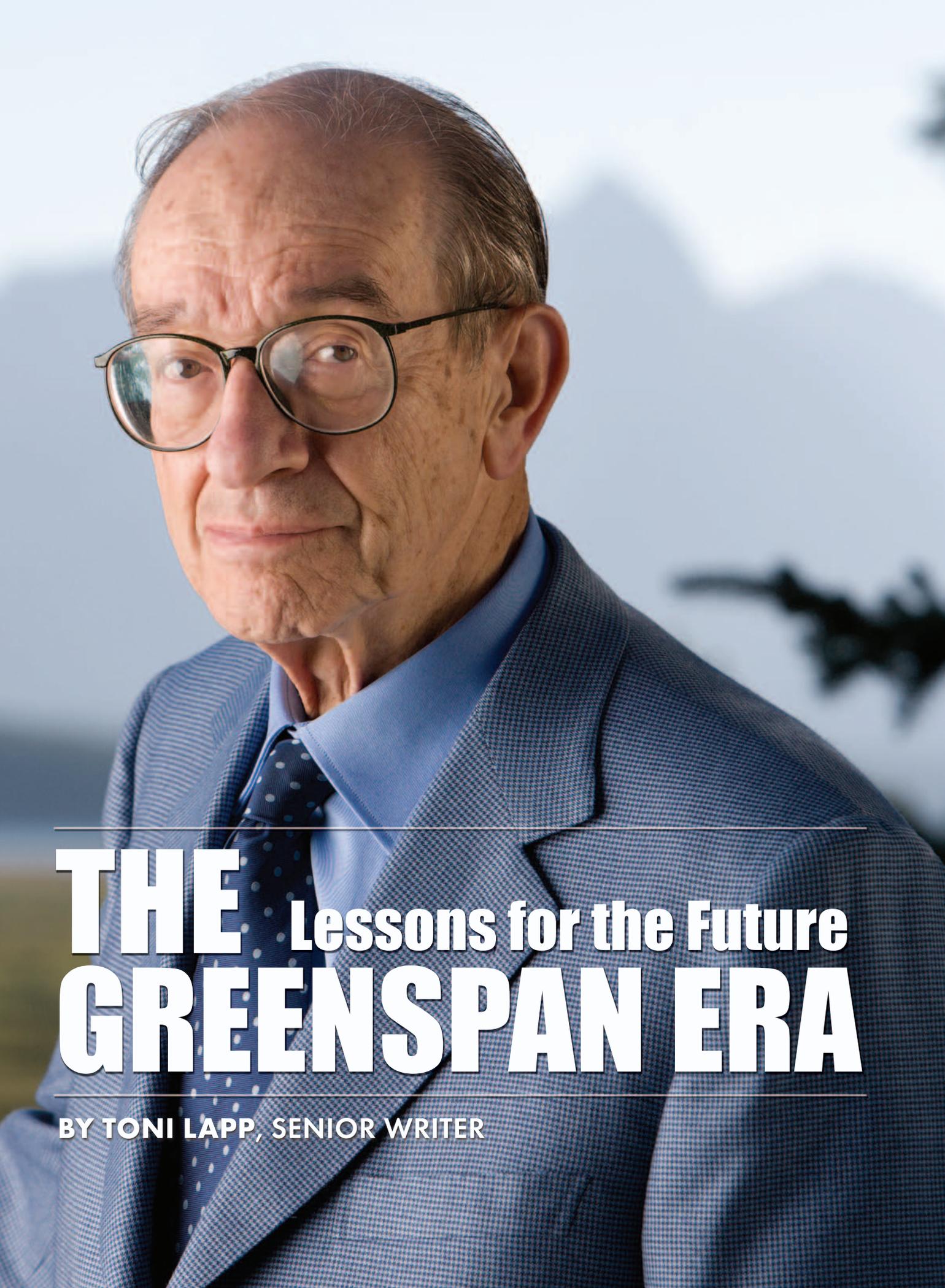
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## FURTHER RESOURCES

**THE ROLE OF SMALL BUSINESSES IN ECONOMIC DEVELOPMENT**

[www.KansasCityFed.org/TEN](http://www.KansasCityFed.org/TEN)

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# **THE** Lessons for the Future **GREENSPAN ERA**

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BY TONI LAPP, SENIOR WRITER

**I**t was a defining event in the history of Alan Greenspan's years as Chairman of the Federal Reserve System, said his peer in the world of central banking.

Mervyn King, governor of the Bank of England, had been invited to speak at the Federal Reserve Bank of Kansas City's annual economic symposium, a storied event among economists, academics and central bankers. The Bank's 29th annual symposium was unique in that it would be Greenspan's last at the helm of the Federal Reserve System. Speakers were asked to examine Greenspan's Chairmanship as a period of time, in a conference titled "The Greenspan Era: Lessons for the Future."

Of all the economic shocks that occurred on Greenspan's watch—the stock market collapse of 1987, international financial crises of the 1990s, the dot-com bubble that burst in 2000, the terror attacks of Sept. 11, 2001—one salient example of the Greenspan Fed's ability to steer the U.S. economy was much more subtle.

In the mid 1990s, the U.S. economy experienced a productivity acceleration. The trend wasn't proved by data until the late 1990s, but Greenspan was taking note of the changing conditions as early as 1995.

"Chairman Greenspan did not wait until 1998 to conclude that the underlying rate of productivity growth might be increasing," said King. "The key reason was that he talked with and listened to people who work in business."

Given the economic conditions of the day, conventional wisdom would have led any other economist to support belt-tightening in the form of higher interest rates, especially when the unemployment rate dipped, a risk factor for inflation. Greenspan had to convince the Federal Open Market Committee, which he chaired, not to raise rates.

“If they had, we might not have gotten the growth that we got,” noted Craig Hakkio, senior vice president and director of research for the Federal Reserve Bank of Kansas City.

The United States’ underlying rate of productivity growth increased from about 1.5 percent to about 2.5 percent in the mid and late ‘90s. Such an increase in productivity growth means an increase in the growth rate of output per worker, thereby boosting a nation’s standard of living.

## Symposium

Each year, the Federal Reserve Bank of Kansas City invites a select group of experts from around the globe to discuss economic issues at its August symposium in the Grand Tetons. Topics are selected with an eye on relevance to current economic policy issues; discussions follow in a free-flowing exchange of ideas.

This year’s symposium was marked by buzz that was beginning to build around who would succeed Greenspan as Chairman, and

participants pondered his extraordinary career and what lessons could be learned from his tenure. Greenspan, the second-longest serving Federal Reserve Chairman, is due to step down at the end of January.

Perhaps the guest list this year reflected the sense of history surrounding the event. In addition to King, participants included Xiaochuan Zhou, governor of China’s central bank, attending for the first time; Jean-Claude Trichet, president of the European Central Bank, who recalled his experiences with Greenspan at G7 meetings; and Robert Rubin, former Treasury secretary, who discussed his interactions with the Chairman, particularly during the global financial crises that marked the 1990s.

Greenspan’s remarks at the meeting were general; he recalled his 18 years at the Federal Reserve, and discussed various indicators used to guide monetary policy. The discussion led to his philosophy of risk management—that is, assessing the many risks to the economy and the consequences of each and then taking precautions against those most likely to create significant damage.

Participants discussed the ramifications of this policy, including the Federal Reserve’s move in 2003 to cut the federal funds rate to 1 percent—a historically low level—to prevent the unlikely but potentially dangerous risk of deflation.

## Eyes on the price

Alluding to the housing boom, Greenspan commented on the recent rise in asset prices and cautioned that many investors had grown complacent in their expectations of continued price appreciation and in requiring less compensation for taking on risk: “History has not dealt kindly with the aftermath of protracted periods of low risk premiums,” he warned.

It was an innocuous comment in context, but one that was seized on by media and repeated ominously on news programs, some of which were broadcasting from the hotel’s lawn. The Federal Reserve, after all, has traditionally focused on growth, inflation and employment numbers. Speculation that the central bank



PHOTO BY MARK WILSON/GETTY IMAGES

**AS FEDERAL RESERVE CHAIRMAN**, Alan Greenspan attends Group of Seven, or G7, meetings along with other world financial leaders, including European Central Bank President Jean-Claude Trichet (left) and Bank of England Governor Mervyn King (right). Both men attended the economic symposium in Jackson Hole, Wyo., where lessons from Greenspan’s tenure was the theme of the conference.

productivity growth well before the data proved it.

### 'Irrational exuberance'

Symposium participants noted that one of the biggest financial shocks of contemporary times—the stock market bubble of the late 1990s—occurred during Greenspan's watch. Remember the "irrational exuberance" speech?

This leads to a discussion of one of Greenspan's philosophies—that it is easier to "mop up" after bubbles than it is to try to prevent them from forming in the first place. Some would have suggested the Federal Reserve should have raised interest rates to cool down the economy as asset prices escalated, particularly during the stock market boom of the late 1990s. Instead Greenspan adopted a policy of cutting interest rates in the aftermath.

Presumably, this philosophy holds, whether the asset in question is stocks or housing.

Which leads to another lesson that King says can be learned from Greenspan. That is, a consistent policy framework will sustain a market economy over the long term.

His counterpart from the European Central Bank agreed.

"A well-designed institutional framework, which undisputedly assigns the central bank the primary objective of price stability, and the adoption of a clear monetary policy strategy, which quantitatively defines price stability and does not pretend to fine-tune directly the business cycle, can make the latter type of policy activism unnecessary in many circumstances," said European Central Bank President, Jean-Claude Trichet, echoing that ever-important concept of price stability.

What constitutes price stability? Former Chairman Paul Volcker defined, and Greenspan embraced, price stability as an environment in which inflation is so low and stable over time that it does not materially

enter into the decisions of households and firms.

In other words, a healthy economic environment is one in which inflation is such a non-issue that people don't talk about it, said King. Perhaps this can be applied to a number of issues—taxes or property rights for instance, he said.

### Future challenges

Whoever becomes the next Chairman of the Federal Reserve System will have to deal with many issues—the effects and risks posed by technological innovation, and the aging of the U.S. workforce, to name a couple.



PHOTO BY KARIN COOPER/GETTY IMAGES

**FEDERAL RESERVE CHAIRMAN Alan Greenspan regularly testifies before lawmakers on the state of the economy. Here, he presents a July 1998 midyear report on monetary policy to the Senate Committee on Banking, Housing and Urban Affairs.**

But perhaps the repercussions of the trade imbalance loom largest. Never before has a country of the United States' size and advancement run such a large current account deficit—the difference between what a country spends on imports and what it spends on exports. The U.S. current account has moved from being nearly balanced in the early 1990s to posting a record deficit of over \$600 billion in early 2005.

This topic received much discussion at the economic symposium. In the view of many

## GREENSPAN TIMELINE

Key events during the Chairman's tenure

### AUGUST 1987

Greenspan sworn in as Chairman of Federal Reserve System.

Dow Industrials at a record: 2,747.

### OCTOBER 1987

Black Monday stock market crash—22.6 percent loss is the steepest dive ever in percentage terms.

### 1989

Savings and Loan crisis of 1980s culminated in cleanup plan by government estimated to have cost from \$500 billion to \$1 trillion.

### JULY 1990 - MARCH 1991—RECESSION

### 1995

Productivity boom. Greenspan identified this phenomenon, even though most economists, basing their assessments strictly on statistical data, disagreed.

### 1994-95

Mexican peso crisis. The Fed, under Greenspan's direction, provided standby liquidity and encouraged corrective action on part of others.

### DECEMBER 1996

Greenspan speech questions whether "irrational exuberance" has unduly escalated asset values.

### 1997-98

Asian and Brazilian financial crises;  
Greenspan's Fed increased liquidity.

### 1998

Russia defaults on debt. Fed lowers rates.

### MARCH 1999

Dow Industrials reaches 10,000 milestone.

### JANUARY 2000

Dow Industrials peaks at all-time high: 11,722.

### FEBRUARY 2000

U.S. expansion reaches 107th month—the longest on record.

### SPRING 2000

Dot-com bubble bursts.

### MARCH - NOVEMBER 2001—RECESSION

### 2001

Terrorism attacks; Fed provided liquidity, guaranteed discount window would be open.

### JUNE 2003

Fed funds rate cut to 1 percent in response to deflation risk.

### SEPTEMBER 2005

FOMC raises Fed funds rate to 3.75 percent with an 11th consecutive quarter-point increase.

his seat behind the Chairman's desk and opens the top drawer in search of Alan Greenspan's magic formula, he will be sorely disappointed," said Alan Blinder, who was appointed by President Bill Clinton to serve as Federal Reserve Vice Chairman under Greenspan in the 1990s and is now an economics professor at Princeton University.

Nevertheless, King, governor of the Bank of England, cited three lessons he learned from his counterpart:

"The key is to recognize that economics tells you how to think, not what to think," he began.

Accordingly, policymakers should be skeptical that any economic model accurately describes how the economy responds to policy. Many observers say Greenspan's ability to not be constrained by specific models or theories made his term successful.

"Monetary policy under Greenspan has been remarkably flexible and adaptable to changing circumstances—a point he has frequently emphasized," said Blinder.

Responding to the 1998 world financial crisis by cutting interest rates three times "was not in the books," Blinder said.

"That was very much ad hoc. One could argue that it was not appropriate for the U.S. (to cut interest rates). This could never have been prescribed by a rule," said Blinder, noting that members of the FOMC were urging Greenspan to tighten.

The next lesson that King cited related to Greenspan's information gathering. While many economists are content to rely on econometric models and official data, it is important to use information from a range of sources. Tapping business leaders for their observations is essential, said King, referring to Greenspan's ability to detect the upturn in trend

would target asset prices was enough to momentarily move markets.

Why should the central bank concern itself with asset prices?

Because the phenomenon of a bubble forming and then bursting creates and destroys wealth, distorting resource allocation. In essence, this affects the Federal Reserve's target variables—inflation and output. The Federal Reserve is interested in asset prices in that they are another piece of information that indicates the health of the economy, measured by growth and inflation.

Greenspan alluded to as much at the symposium.

“The configuration of asset prices is already an integral part of our evaluation of the large array of forces that influence financial stability and economic growth,” he said.

However, this does not mean the Federal Reserve will attempt to pre-empt unsustainable increases in asset prices, largely because it is difficult to discern a bubble until the bubble has burst.

Not yet, anyway.

“I certainly do not rule out that future work could improve our understanding of asset price behavior, and with it, the conduct of monetary policy,” said Greenspan.

## Data, details and discretion

Greenspan, a former jazz musician, was a known quantity when President Ronald Reagan appointed him Chairman of the Federal Reserve in 1987. He had previously served as Chairman of the Council of Economic Advisers for the Ford administration and had demonstrated a mastery of data and numbers.

Some have likened leading the Federal Reserve to driving a car. The governing body makes decisions regarding inflation and the federal funds rate target and exerts control to speed up or slow down the economy as appropriate.

During the Greenspan era, the nation experienced only two mild recessions. It's been a relatively smooth ride; during his tenure, inflation fell gradually from roughly 4 percent to 2 percent—achieving the Federal Reserve's mission of price stability.

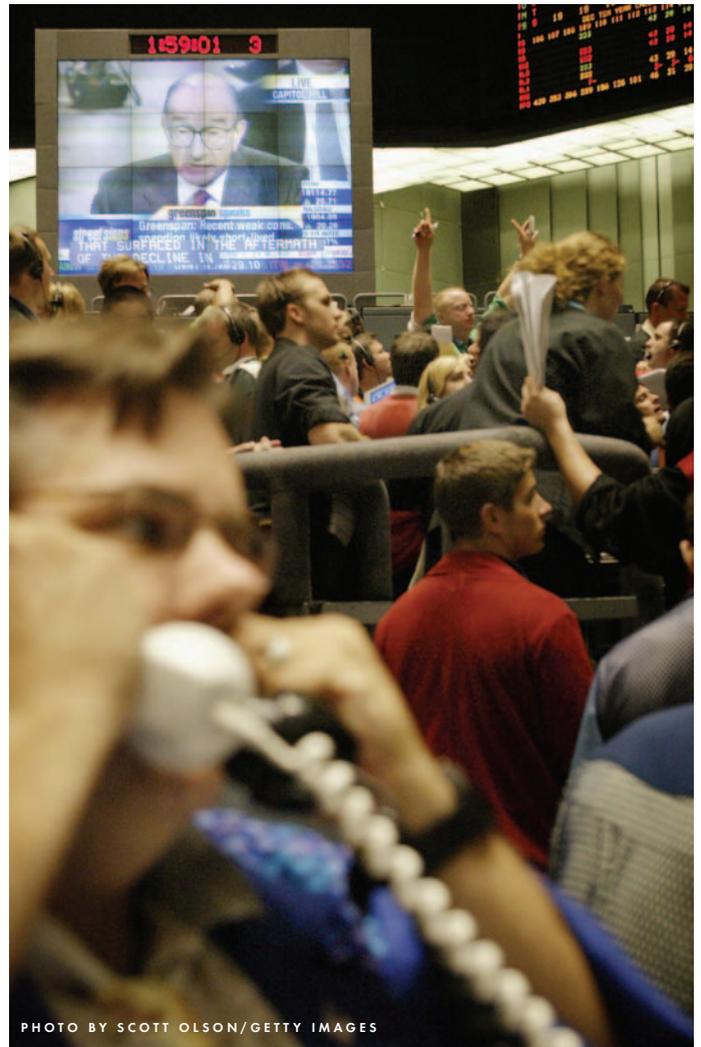


PHOTO BY SCOTT OLSON/GETTY IMAGES

**FINANCIAL MARKETS MOVE** in response to events of the day, prompting traders such as these in Chicago to listen to Federal Reserve Chairman Alan Greenspan for any hint that the central bank may raise interest rates.

To accomplish this, he watched an array of economic statistics such as employment, inventories, orders and shipments.

Given the weighty challenges the next Chairman will face, there is keen interest in learning the keys to the Greenspan Fed's success.

## Monetary Policy 101

Is monetary policy a strategy involving statistics and analysis, or intuition and human instinct? Or both?

“When the next leader of the Fed takes

# Toward a more transparent Federal Reserve

BY TONI LAPP, SENIOR WRITER

One significant change to come out of Alan Greenspan's Federal Reserve was a movement to a more open organization.

During Greenspan's tenure, the Federal Open Market Committee—or FOMC—began releasing interest-rate decisions immediately following its meetings. The first such communication was to announce a rate hike in February 1994. Concerned that the increase—the first such hike in 17 months—would shake up markets, Greenspan told the FOMC they needed to “make certain that there is no ambiguity about our move.”

Before then, such decisions weren't announced for at least six weeks. Fed watchers on Wall Street had to study measures of the money supply to determine if any tightening or easing had occurred as a result of the meetings.

Greenspan acknowledged the changing approach in communications at the symposium.

“We have moved toward greater transparency at a measured pace, in part because we were concerned about potential feedback on the policy process and about being misinterpreted, as indeed we were from time to time,” he said.

The movement toward greater transparency continued in May 1999, when the Federal Reserve began to issue a statement after every FOMC meeting whether or not the funds rate had been changed.

In 2003, the Fed ventured further. In May, the FOMC became concerned about the potential risk of deflation, and the committee's postmeeting press release began to include statements about this outlook. In June the FOMC lowered the funds rate to a decades-low 1 percent and by August it began to make statements about the future funds rate operating target. This was a significant change; the Federal Reserve went from making forward-looking statements about economic outlook to making forward-looking statements about possible future policy actions.

Some economists at the symposium suggested the Federal Reserve should consider further steps toward openness.

Michael Woodford, professor of economics at

Columbia University, presented a paper titled “Central Bank Communication and Policy Effectiveness,” at the symposium. He says that what the FOMC has done to date is not enough.

“The public's understanding, not only of what the central bank is currently doing, but of what it can be expected to do in the future, is critical for the effectiveness of policy,” he said.

There appeared to be momentum to the idea of more open communication. Other speakers also voiced support for the idea.

“Long-term interest rates matter more than the federal funds rate, and expectations are better managed if the market can better anticipate what the central bank will do in the future,” said Alan Blinder, former vice chairman.

Woodford suggested that having inflation targets would enable central banks to better explain interest rate decisions, he said.

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**“The public's understanding, not only of what the central bank is currently doing, but of what it can be expected to do in the future, is critical for the effectiveness of policy.”**

—Michael Woodford

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While a number of countries' central banks set inflation targets, the United States' Federal Reserve has stopped short of announcing an explicit numerical inflation objective.

However, a future chairman may believe that publicizing inflation targets could be a useful communication tool and policy strategy.

What does Greenspan think of such an approach? He touched on the topic at the symposium.

“To date, we have chosen not to formulate explicit inflation targets, in part, out of concern that they could inhibit effective pursuit of our goal.”

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participants, erasing the trade deficit will be painful. Large current account deficits are financed through the inflow of capital from foreign investors purchasing U.S. securities. If the flow of capital were to stop suddenly, the dollar could depreciate and inflationary pressures might build. This could lead the Federal Reserve to raise short-term interest rates which, in turn, could slow economic growth in the United States and possibly the rest of the world.

While there are no modern historical precedents for a country as large as the United States running very large and persistent current account deficits, there are numerous examples of current account reversals among smaller countries in both the industrial and developing world. And the experience of these countries

Whether the decline will be orderly or abrupt will depend on maintaining, if not increasing, the flexibility of economic institutions in the United States and abroad, he said.

## Farewell, Chairman

About 150 participants attended the 2005 symposium, and while some proclaimed the guest of honor to be possibly the greatest central banker ever, others stopped short of such heroic terms. In the end, only the passing of years will determine Greenspan's legacy.

Over the course of two days, Greenspan sat near the back of the conference hall and took it all in. Although he might have raised his profile by injecting himself into the discus-

**“Monetary policy under Greenspan has been remarkably flexible and adaptable to changing circumstances.”**

does not bode well for the United States. Previous episodes of current account rebalancing in both industrial and developing countries have been associated with a depreciation of the exchange rate and a temporary reduction in real GDP growth. Effects on inflation and interest rates vary depending on the size of the country and whether it is industrialized, noted Sebastian Edwards, professor at the University of California-Los Angeles.

A reduction in the trade deficit will include simultaneous adjustments in savings and investment in the United States and the rest of the world, along with changes in exchange rates. In addition, to ensure that the adjustment is gradual, most participants felt that policymakers should resist protectionist trade measures and work toward further trade liberalization.

Greenspan himself had some thoughts about the current account deficit, and noted that the correlation between increases in home equity extraction and the current account deficit suggests that the end of the housing boom “could induce a significant rise in the personal saving rate, a decline in imports, and a corresponding improvement in the current account deficit.”

sions that followed the presentations, he quietly observed.

Except for the occasional autograph seeker hanging around outside the meeting hall, he attended the symposium with little fanfare, addressing the participants at the beginning and then at the end. His concluding remarks were met with a standing ovation, as close as you get to hero worship in a crowd of economists, academics and central bankers.

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## FURTHER RESOURCES

### THE GREENSPAN ERA: LESSONS FOR THE FUTURE

Papers presented during the Federal Reserve Bank of Kansas City's annual economic symposium in Jackson Hole, Wyo.

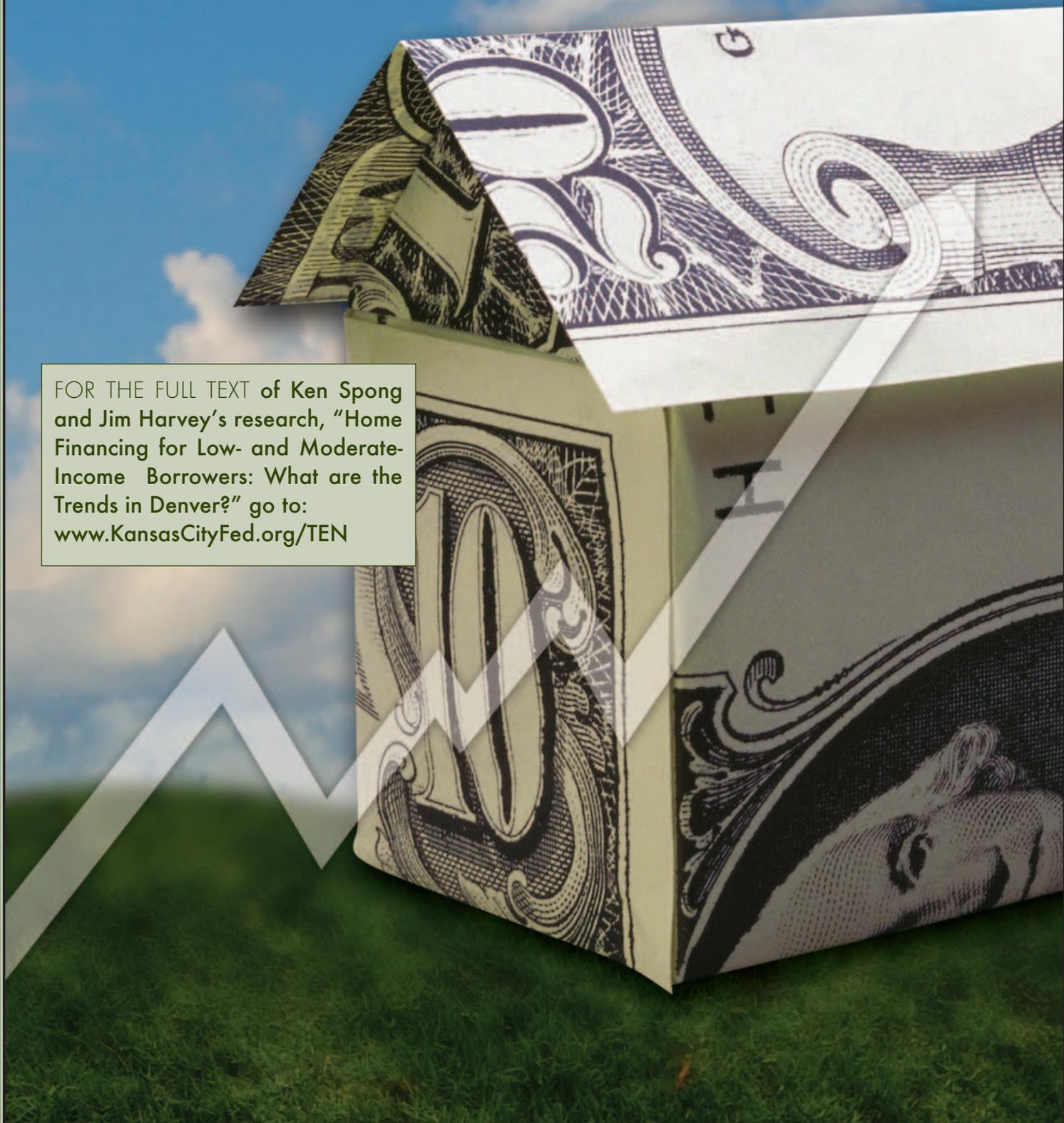
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# House and Home

THE SURGE IN DENVER'S LOW- AND MODERATE-INCOME MORTGAGE LENDING

FOR THE FULL TEXT of Ken Spong and Jim Harvey's research, "Home Financing for Low- and Moderate-Income Borrowers: What are the Trends in Denver?" go to: [www.KansasCityFed.org/TEN](http://www.KansasCityFed.org/TEN)





**BY KEN SPONG**, SENIOR POLICY ECONOMIST  
**AND JIM HARVEY**, POLICY ECONOMIST

**O**ver the last decade, dramatic changes have taken place in home lending and mortgage markets. These changes have been spurred on by a number of factors, including a strong economy, rapid technological innovation and increased public and regulatory scrutiny of fair lending laws and affordable housing programs. An outgrowth of all of these changes is a rapid increase in the volume of home lending across much of the United States.

This trend has been particularly evident in the Denver metropolitan area. The dollar volume of loans extended for home purchases in Denver increased by nearly four-fold between 1992 and 2002, and housing prices appreciated at twice the annual nationwide rate during the 1990s.

These numbers point to a significant increase in home lending and homeownership—71 percent of Denver households now own their homes compared to less than 66 percent in 1995. But how have local families with low and moderate incomes fared in obtaining financing and increasing their rate of homeownership?

### **Changes and developments in home lending**

A number of factors may have improved the flow of credit to low- and moderate-income borrowers in recent years. One factor is a strong economy that has provided one of the most stimulative environments on record for homeownership. The longest period of uninterrupted growth in U.S. history occurred between 1991

and 2001, thus giving many lower-income borrowers a solid employment record and the willingness to undertake the long-term financial commitment required to purchase a home. Declining interest rates are another part of the relatively bright economic picture. The average interest rate on new 30-year, fixed-rate mortgages fell from 10.13 percent in 1990 to 6.54 percent in 2002 and has mostly stayed below 6.0 percent since then.

Another set of factors, technological innovation and improvements in information processing, is helping lenders do a better job of constructing household financial histories and finding data to support the creditworthiness of lower-income borrowers. Moreover, innovations in financial markets, such as the development of mortgage-backed securities, are opening the door for a wider group of investors and thereby contributing to a more even flow of funds into the affordable housing market.

Public policy changes are providing an additional incentive for lending to lower-income groups. The Community Reinvestment Act of

**TABLE 1: HOME PURCHASE LENDING TO LOW- AND MODERATE-INCOME BORROWERS IN THE DENVER METROPOLITAN AREA (average annual amount)**

	1992-1994		1995-1998		1999-2002	
	Amount (\$ Millions)	Share of All Lending	Amount (\$ Millions)	Share of All Lending	Amount (\$ Millions)	Share of All Lending
All Low- and Moderate-Income Borrowers	918.4	21.9%	1,394.8	22.4%	2,419.3	22.7%
Low- and Moderate-Income Borrowers in Low- and Moderate-Income Census Tracts	219.0	5.2%	361.4	5.8%	598.8	5.6%
Low- and Moderate-Income Borrowers in All Other Census Tracts	699.4	16.7%	1,033.4	16.6%	1,820.5	17.1%
All Home Purchase Lending in Denver	4,187.6	100%	6,222.9	100%	10,670.2	100%

1977 (CRA), which focuses on how depository institutions meet the credit needs of the communities in which they maintain deposit-taking offices, was amended in 1990 to provide for public disclosure of supervisors' CRA evaluations. Also, banking agencies implemented a performance-based CRA rating system in 1995 to provide quantitative measures of an institution's low-income lending activities. The Home Mortgage Disclosure Act of 1975

median household income in the Denver metropolitan area—benefit from the generally strong home lending market? This question is of particular importance to lower-income households because financing plays a significant role in their choice of housing and in their financial prosperity. Also, recent housing trends may provide some perspective on which factors and public policies have been most influential in expanding homeownership.

## How have local families with low and moderate incomes fared in obtaining financing and increasing their rate of homeownership?

(HMDA), which requires mortgage lenders to publicly disclose information about their home lending in urban areas, has been amended several times to expand the types of reporting institutions and the information reported (see the sidebar on page 31 for a description of the new loan pricing disclosures HMDA reporters must make). These changes are thus giving community groups and public authorities a better means for comparing institutions' records on lending to lower-income groups.

### Lending to low- and moderate-income borrowers

Did low- and moderate-income households—those with less than 80 percent of the

As shown in Table 1, the dollar volume of home purchase lending to all low- and moderate-income borrowers increased significantly from a yearly average of \$918 million in the 1992-1994 period to a \$2.4 billion average between 1999 and 2002. This growth, moreover, exceeded the rate for all borrowers in Denver, leaving low- and moderate-income borrowers with a slight increase in their share of overall home lending in Denver—from a 21.9 percent share in the 1992-1994 period to a 22.7 percent share in the final period. Given the very rapid growth and price appreciation that occurred in the middle and upper end of the Denver housing market during much of the 1990s, the fact that lower-income borrowers

more than held their own represents a good sign of progress.

Table 1 also indicates that about three-fourths of all home lending to low- and moderate-income borrowers occurs outside of low- and moderate-income areas. As a result, much of this lending is being dispersed into other parts of the Denver metropolitan area—a sign that lower-income borrowers may be finding a range of opportunities in housing, employment and public services.

The total amount of lending in low- and moderate-income neighborhoods is also an important measure determining the stability and future, quality of life, and public services in these areas. Moreover, the CRA stresses the importance of local depository institutions serving lower-income neighborhoods. Within Denver's low- and moderate-income areas, the volume of lending to home purchasers at all income levels rose from a yearly average of \$425 million during the 1992-1994 period to \$1.3 billion between 1999 and 2002. This represents a 226 percent rise compared to a 155 percent increase in home lending across all areas. As a result, low- and moderate-income neighborhoods have experienced a gain in their share of all home purchase lending, but this share is still just a little over one-eighth of all home lending in Denver.

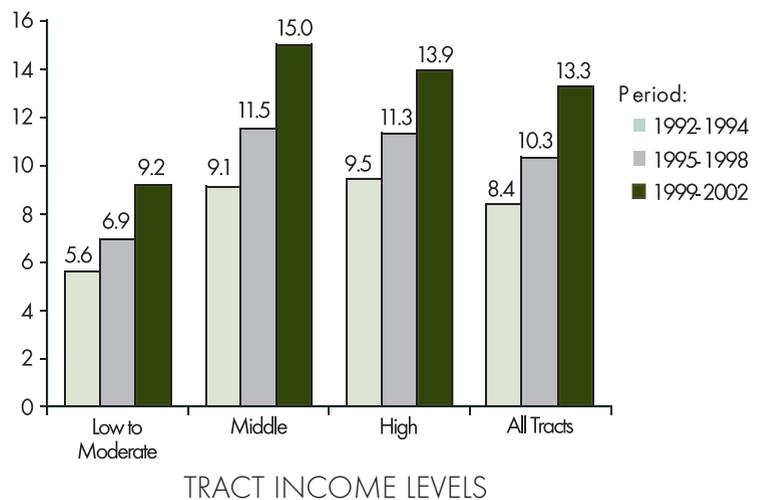
A more detailed way to look at the relative level of lending in low- and moderate-income neighborhoods is to compare the number of home purchase loans to the number of owner-occupied housing units. This comparison helps adjust for housing differences across varying economic levels, especially between neighborhoods composed of mostly rental housing and others where single-family homes and the need for home financing may be more prevalent. As shown in Chart 1, the number of loans in low- and moderate-income neighborhoods has jumped from an annual average of 5.6 loans per every 100 owner-occupied housing units to 9.2 loans. While this trails the 13.3 loans for all

of Denver, there are reasons why a lower rate might occur in lower-income neighborhoods, for example staying in a home longer to take advantage of terms in a special lending program or because the costs of changing homes—such as loan closing costs and real estate sales expenses—are proportionately higher.

## Who is lending?

Another interesting aspect of low- and moderate-income lending is who is doing the lending—have the major lenders stayed much the same over time, or are technologies and other factors bringing new players on the scene? Independent mortgage companies were the most common lenders across the Denver metropolitan area and at all income levels. As a group, they increased their lending in lower-income neighborhoods from an average annual rate of 3.06 loans per 100 owner-occupied

**CHART 1: HOME PURCHASE LOANS APPROVED PER 100 OWNER-OCCUPIED UNITS (Denver metropolitan area)**



units in the 1992-1994 period to 4.55 loans in the 1999-2002 period. Some of the greatest gains between these two periods, though, were achieved by thrifts and banking organizations without Denver deposit-taking offices, which tripled and quadrupled the numbers of loans they made in low- and moderate-income neighborhoods.

# Help for Denver's low- and moderate-income homebuyers

**BY ARIEL CISNEROS, SENIOR ADVISOR, COMMUNITY AFFAIRS**

**L**ow interest rates played a major role in the surge of homeownership in Denver, but they are not always enough for low- and moderate-income (LMI) residents to attain homeownership.

Even with low interest rates, some potential homebuyers still have difficulty because they have low credit scores, limited funds for downpayment and closing costs or a lack of available affordable inventory.

To ease the burden on LMI families, various public and private partnerships and collaborations have developed products and services that help prepare potential home buyers and get them into homes. Along with financial education so that potential homeowners can get on the right financial track, there is pre- and post-home buyer education and counseling, downpayment and closing cost assistance, and an ongoing effort to develop a viable inventory of affordable housing.

Many Denver LMI residents have benefited from funds that were passed through to aid organizations by NeighborWorks America, which is part of the NeighborWorks system, a national collaborative effort of businesses, government officials, residents and many other partners. Rocky Mountain Mutual Housing Association, Inc., an affiliate of NeighborWorks America, has been providing home buying opportunities along with homebuyer and financial education for its clients for many years. The organization has developed partnerships with local financial institutions, local government and housing authorities to provide these needed services for potential homebuyers.

Colorado Housing Enterprises, LLC, a part of Colorado Rural Housing Development Corporation, also helps limited-income families with home buying by providing homebuyer education and downpayment assistance.

Assisting on the development side, the Housing Development Project (HDP), a collaboration of the Enterprise Foundation, Denver area banks and corporations, the City and County of Denver seeks to build the capacity of nonprofit community development organizations to develop, manage and preserve affordable housing benefiting LMI people and neighborhoods in metro Denver, says Lisa Goldberg, senior program director for HDP. HDP supported local nonprofit housing developers to accomplish the following from 1993 to

second quarter 2005: Almost 1,200 affordable homeownership units developed, in both new construction and rehabilitation. HDP support provided homeownership counseling to approximately 1,500 families that purchased homes, along with assisting over 1,100 families considering homeownership and needing financial education.

Ray Stranske, executive director and founder of Hope Communities, started Hope Communities, a community development corporation, in 1980, after a task force of citizens concerned with the lack of affordable, comfortable housing for people with low incomes came together. Hope Communities has developed the neighborhood, with over 60 units for sale along with over 700 units of affordable rental housing. Hope has rehabilitated and built new construction, including a mixed use development along the light rail corridor. Hope's office and most of its housing units are located in the diverse Five Points neighborhood, just north of downtown Denver.

For-profit developers are also filling some of the need for affordable housing, or workforce housing, for individuals and families that are 80 percent or below the median income. At Stapleton, the former airport for the city of Denver, and now a redevelopment for housing and commercial space, units of affordable housing, in one development, have a starting sales price of \$99,990 for a one bedroom unit, \$129,990 for a two bedroom and \$159,990 for a three bedroom condominium.

Through inclusionary zoning (IZ), the city of Denver is promoting the development of more units of affordable housing,

requiring developers that develop more than 30 units of housing in a single development to provide 10 percent of the units as affordable for a population earning less than 80 percent of the area median income.

Public and private partnerships involving government, the nonprofit community, and the private sector, including financial institutions, have been developing appropriate and flexible lending tools, financial education, pre- and post homebuyer education and counseling, and developing units of affordable housing that will support safe and decent neighborhoods in a high cost community like Denver.

**Much of this lending is being dispersed into other parts of the Denver metropolitan area — a sign that lower-income borrowers may be finding a range of opportunities in housing, employment and public services.**

**T**

## NEW HMDA LOAN

### Lending progress

During a period of rapid growth in home lending throughout the Denver area, low- and moderate-income borrowers income neighborhoods have thus experienced an increase in their share of all home purchase loans. In addition, the level of lending in relation to the number of owner-occupied housing units has increased significantly in low- and moderate-income neighborhoods. These results suggest that home financing has become more readily available to lower-income households, thus ensuring greater progress toward their homeownership goals.

Some of the factors behind this progress undoubtedly are a strong economy, declining interest rates, and greater regulatory incentives. An additional and very noteworthy development, though, is the increasing role that banking organizations and thrifts without Denver deposit-taking offices are playing in low- and moderate-income home lending in Denver. The fact that these organizations have overcome the lending advantages that local institutions once held suggests that innovations in technology and financial markets are dramatically reshaping our mortgage markets and bringing new competitors into these markets.

From a longer-term perspective, the emergence of such competition should greatly benefit low- and moderate-income borrowers, while providing a sign that lower-income lending can meet the same market tests as other forms of lending. To the extent this is true, a broader range of lenders and investors will develop to serve low- and moderate-income households, and a more

In response to the growth of the subprime mortgage market and concerns about higher-rate loans, the Federal Reserve expanded the HMDA reporting regulations to include selected loan pricing data. For home purchase, refinance or secured home improvement loans, lenders must now report the spread between the annual percentage rate on a loan and the yield on Treasury securities of comparable maturity, provided this spread exceeds three percent on first-lien loans and five percent on subordinate-lien loans. As of March 31, 2005, lenders must disclose their loan pricing data to anyone upon request, and edited, aggregate data was made available on September 13, 2005.

These disclosures will not provide a complete picture of loan pricing practices, since several factors relevant to the pricing of loans will be missing—most notably, loan-to-value ratios, credit scores and histories, and borrower debt-to-income ratios. The pricing data, though, will serve as a starting point for community groups and lenders to discuss loan pricing policies, identify higher-rate markets in need of more competitive entry and obtain better information on where to look for credit.

## PRICING DISCLOSURES

continuous and competitive source of financing will be available to support lower-income neighborhoods.

T

## FURTHER RESOURCES

LOW- AND MODERATE-INCOME HOME FINANCING:  
WHAT ARE THE TRENDS IN KANSAS CITY?

[www.KansasCityFed.org/TEN](http://www.KansasCityFed.org/TEN)

COMMENTS/QUESTIONS are welcome and should be sent to [teneditors@kc.frb.org](mailto:teneditors@kc.frb.org).

## Bank's Community Affairs Department, Kauffman Foundation to host entrepreneurship conference

The Community Affairs Department of the Federal Reserve Bank of Kansas City, in partnership with the Kauffman Foundation, will host a conference exploring opportunities for and challenges facing entrepreneurship in low- and moderate-income (LMI) communities.

The conference, which runs November 3 and 4 in Kansas City, Missouri, will present a number of studies commissioned specifically for this conference, including entrepreneurship's role in reducing problems unique to LMI communities, entrepreneurship's current presence in LMI communities, challenges facing entrepreneurship in LMI communities and accounting for variation in entrepreneurial success. The final session will provide an overview of the findings presented and suggest future studies needed in the area of entrepreneurship in LMI communities.

A compilation of the presented works will be made available shortly after the conference via the main Community Affairs webpage at [www.KansasCityFed.org/comaffirs/caconferences.htm](http://www.KansasCityFed.org/comaffirs/caconferences.htm).

## Special report from the Center for the Study of Rural America now available

"A Review of the Federal Role in Regional Economic Development," a special report prepared by Mark Drabenstott, vice president and director of the Center for the Study of Rural America, is now available.

In 2004, the federal government spent approximately \$17 billion on economic development programs aimed at specific areas and communities. The Center's report examines current fiscal policy with regard to economic regions, and highlights the need for a redesign of economic development grant programs.

The report frames what the federal government's future role could be in regional economic

development. Three steps are essential in framing that role. The first is to define what regional development policy is today. The report provides a comprehensive review of current federal programs and how federal dollars are spent on regional development. It shows that federal programs are highly fragmented today, that programs largely assume that all regions grow the same way and that federal spending is focused heavily on physical infrastructure.

The second step is to identify what makes regional economies grow in the 21st century. The report reviews the economics literature and highlights state-of-the-art thinking on regional growth. It shows that economists believe the drivers to regional growth have changed dramatically over the past decade and that regions now grow when they gain a competitive edge in rapidly changing global markets. Within this new context, a region's capacity to innovate and its ability to grow entrepreneurs are keys to success.

The final step is to consider how federal policy might change to help regions grow in the future. Three shifts in federal policy will be important if the nation wants to help regions hone their competitive edge:

1. Make regional competitiveness the goal of federal regional development policy and align federal development programs accordingly.
2. Design new efforts to help regions seize innovations and grow entrepreneurs.
3. Create an effective delivery system for taking federal programs to regions around the nation.

The full report is available at [www.KansasCityFed.org/TEN](http://www.KansasCityFed.org/TEN) and will be available in hardcover via the Center's main page at [www.KansasCityFed.org/RuralCenter/RuralMain.htm](http://www.KansasCityFed.org/RuralCenter/RuralMain.htm).

## Bank hosts Oklahoma Economic Forums, plans for '06 Forums

The Federal Reserve Bank of Kansas City recently hosted Economic Forums in four Oklahoma locations and officials are currently planning for Forums events in other Tenth Federal Reserve District states in 2006.

In the Economic Forums program, which was created 50 years ago, Bank economists visit local communities where they make presentations on the regional economy and national economic outlook. Through question and answer sessions, as well as informal discussion, the economists are able to gain first-hand insight into the District economy while local residents are able to learn more about the Federal Reserve's perspective on economic issues. As his schedule permits, Bank President Thomas Hoenig speaks to Forums audiences.

The Forums program is on a two-year cycle, meaning that Bank economists and staff visit all regions of the seven-state District at least every two years.

In 2005, Oklahoma Forums in Clinton, McAlester, Oklahoma City and Tulsa during September followed spring Forums in Colorado that were held in Colorado Springs, Denver, Durango, Fort Collins and Grand Junction. In the spring of 2006, the Forums program will visit locations across Kansas and in western Missouri, while in the fall, the program will visit communities in Nebraska, New Mexico and Wyoming.

Invitations to the 2006 Forums will be mailed to bankers, business and community leaders as the events approach. Those interested in ensuring that they will receive an invitation can email: [Teneditors@kc.frb.org](mailto:Teneditors@kc.frb.org). There is no charge for attending Forums events.

## Banks Marking Milestones as Federal Reserve Members

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GUARANTY BANK & TRUST COMPANY Denver, CO.....	1
KAW VALLEY STATE BANK & TRUST COMPANY Wamego, KS.....	1
FIRST STATE BANK, Lincoln, NE.....	1

## FURTHER RESOURCES

Research from the Federal Reserve Bank of Kansas City available at [www.KansasCityFed.org/TEN](http://www.KansasCityFed.org/TEN):

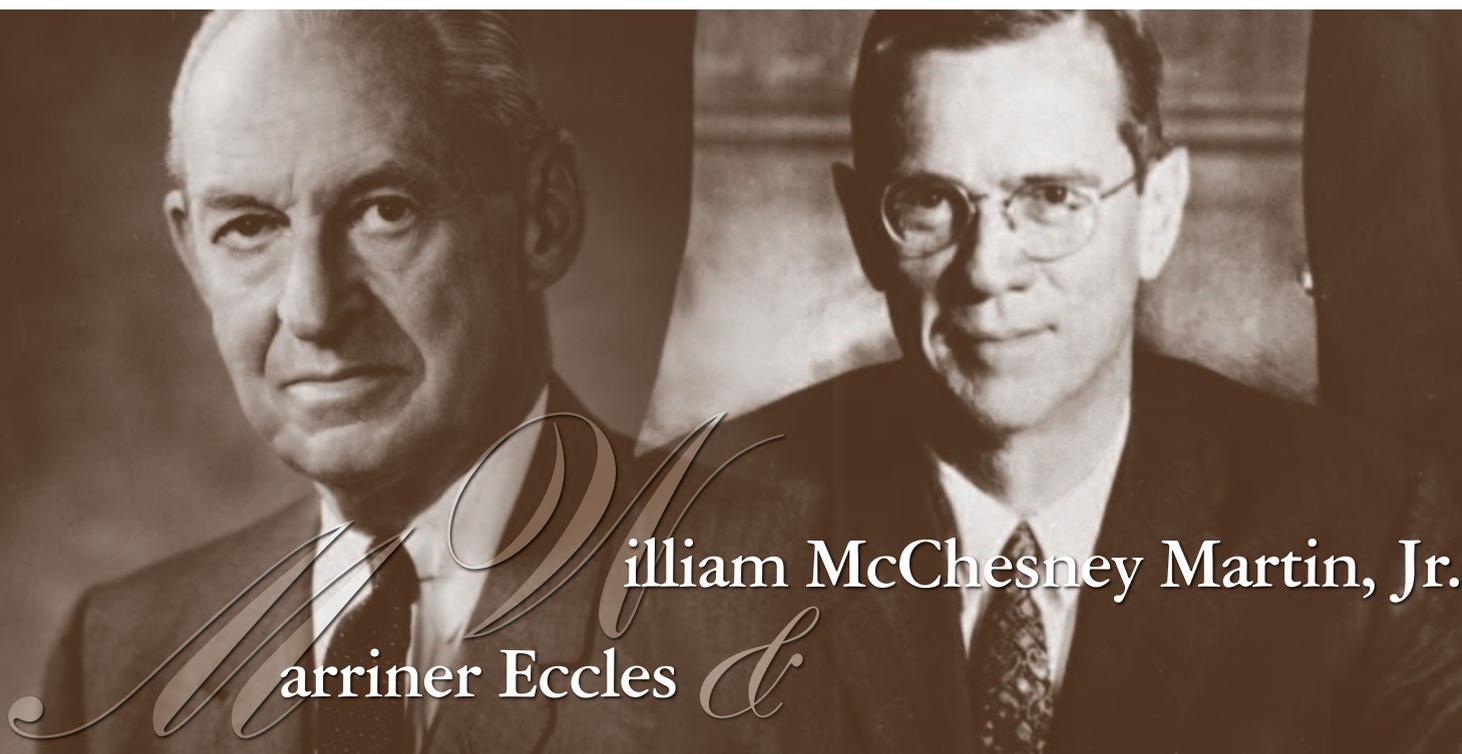
**WHO IS PROCESSING YOUR PAYMENTS? A LOOK AT THE MANY ROLES NONBANKS PLAY IN PAYMENTS ACTIVITIES AND THE OVERSIGHT QUESTIONS THAT ARISE AS A RESULT**

**CREDIT UNION GROWTH IN THE TENTH FEDERAL RESERVE DISTRICT: HOW LEGAL AND REGULATORY CHANGES HAVE AFFECTED CREDIT UNION EXPANSION**

**SMALL BANK LENDING: TAPPING OPPORTUNITIES FOR RURAL GROWTH**

**WHAT CAUSED THE GREAT MODERATION; THE SHARED FORTUNES OF CITIES AND SUBURBS; GAUGING A REGION'S ENTREPRENEURIAL POTENTIAL**

**NEXUS, THROWBACKS, AND THE WEIGHTING GAME**



**F**ederal Reserve Chairman Alan Greenspan is the second-longest serving chairman in the history of the nation's central bank, trailing only William McChesney Martin, Jr.

Greenspan and Martin, who both served more than 18 years, are clearly the exceptions. There is only one other chairman who even begins to approach that length of service: Marriner Eccles, who served as chairman for 13 years.

However, when it comes to total years of service, Eccles nearly equals Greenspan and Martin. His time on the Board of Governors spanned nearly 17 years and encompassed one of the most important periods in the history of the nation's independent central bank.

### **The terms of office**

Because of the way terms of office are structured on the Board of Governors, it is unlikely that a future Federal Reserve chairman will rival Greenspan or Martin for their length of service.

The Federal Reserve has a unique "inde-

pendent within the government" structure. Although the twelve regional Federal Reserve Banks are not government agencies, the Board of Governors of the Federal Reserve System, which has broad oversight responsibility for the operations and activities of the regional Reserve Banks, is a government agency.

As such, Board members are appointed by the president and confirmed by the Senate. Board members serve 14-year terms and are not eligible for reappointment to a second full term. However, governors who are initially appointed to the Board to complete the unexpired portion of a term may be reappointed and, once confirmed by the Senate, can serve a full 14-year term.

It is not uncommon for Board members to resign their positions prior to the completion of their terms. Because of the number of early departures over the years, several governors have been appointed to the Board to complete an unexpired term. It is somewhat uncommon for a member who completes the unfinished term to be reappointed to a second term. Rarer still is the

appointee who then completes that second term.

There are, however, a few notable exceptions.

Greenspan was appointed to the Board as its chairman on Aug. 11, 1987, completing the unexpired term of his predecessor, Paul Volcker.

Regardless of when an appointee begins serving on the Board, the terms of office do not change. The unexpired term that Greenspan was appointed to complete ended on Jan. 31, 1992. He was reappointed to the Board and began serving his full 14-year term the following day. That term will conclude on Jan. 31, 2006.

The term of a chairman is a separate matter.

The president selects a chairman and a vice chairman, whose names are then submitted to the Senate for approval. The nominees for these positions must either be current members of the Board of Governors or, as is usually the case with the chairman's position, simultaneously appointed to a position on the Board of Governors.

Similarly, a departing chairman who resigns that position will usually vacate his seat on the Board of Governors. However, because they are separate terms, it is possible to have a former chairman continuing to serve as a member of the Board.

It has happened once.

## Eccles and Martin

Marriner Eccles was appointed to the Board in 1934, but he is sometimes referred to as the Federal Reserve's first chairman because of sweeping changes in the Board's structure occurring during his tenure.

Under the provisions of the Federal Reserve Act signed by President Woodrow Wilson in 1913, the Federal Reserve Board was comprised of seven members: five appointees along with the comptroller of the Currency and the secretary of the Treasury, who was *ex-officio* chairman.

The Banking Act of 1935 made several changes, including changing the name of the Federal Reserve Board to the Board of Governors of the Federal Reserve System. The Act also changed the Board's composition into seven appointed positions, requiring the secretary of the Treasury and the comptroller of Currency to both leave the Board in 1936. The Act also cre-

ated four-year terms for the offices of chairman and vice chairman—known prior to the 1935 Act as governor and vice governor.

Eccles, a former Utah banker who had held a position in the Treasury prior to his Board appointment, was the chairman. He would complete an unexpired Board term and be reappointed to another term by President Franklin Roosevelt. After his initial appointment to the newly titled chairman's position in 1936, he would be reappointed as chairman by Roosevelt in 1940 and 1944.

In the midst of World War II, it was an interesting period for the Federal Reserve.

Although the secretary of the Treasury had been removed from the Board of Governors by the 1935 Act, there was significant friction between the agencies relating to numerous issues. Chief among them was the expectation that the Federal Reserve would implement policies supporting the prices of long-term government debt, thereby helping to finance government spending.

"The pattern of war finance had been firmly established by the Treasury, the Federal Reserve merely executed Treasury decisions," Eccles writes in his 1951 book, *Beckoning Frontiers: Public and Personal Recollections*.

The arrangement also eventually contributed to increasing inflationary pressures.

In 1948, with President Harry Truman in office, Eccles, who had been an opponent of these Treasury-mandated yield rates, was not reappointed to the chairmanship.

In his book, Eccles relates the conversation where John Steelman, the president's special assistant, informs Eccles that he will not be reappointed:



William McChesney Martin, Jr.

“The [P]resident has given me a very unpleasant assignment. I am to inform you that he is not going to redesignate you as [C]hairman of the Board of Governors. But he told me to be sure you understand that he wants you to stay on as a member of the Board,” Steelman said, according to Eccles’ account of the meeting.

Eccles, who thought he had a strong relationship with Truman, was surprised by the news. After Roosevelt’s death in 1945, Eccles said he offered to step down so Truman could appoint a new chairman “of his own choice.” Eccles said he was told at that time by Truman that such a change was not necessary.

After being told of the president’s decision by Steelman, Eccles requested and was granted a meeting with Truman. In his book, Eccles said

ment’s requirements and, at the same time, to minimize the monetization of the public debt.”

Alan Meltzer explains the significance of the accord in his 2003 book, *A History of the Federal Reserve*.

“For the first time since 1934, the Federal Reserve could look forward to conducting monetary actions without approval of the Treasury,” Meltzer writes. “The accord ended ten years of inflexible rates, following seven years of inactive and inflexible policies.”

McCabe would resign five days later, after reportedly being told by the president that he was no longer needed.

William McChesney Martin, Jr., who had been the Treasury official handling that agency’s side of the accord negotiations, then was ap-

## “ For the first time since 1934, the Federal Reserve could look forward to conducting monetary actions without approval of the Treasury. ”

that, during the meeting, Truman personally asked Eccles to remain on the Board, pleading with him, “Please stay and help me. I need your help.”

Eccles, after consulting with friends, agreed to continue to serve as a member of the Board of Governors even though he would no longer be its chairman.

“I swallowed my pride,” he would later write.

To replace Eccles as the chairman, Truman appointed Thomas B. McCabe, a Pennsylvania banker and businessman who led Scott Paper Company from a relatively small operation into a multinational firm. McCabe would have a brief tenure at the Federal Reserve, serving as chairman for less than three years.

McCabe’s resignation would come only days after the announcement of what is known as the Treasury-Federal Reserve Accord, an agreement to resolve the ongoing disputed issues between the two agencies.

The statement issued March 4, 1951, reads:

“The Treasury and the Federal Reserve System have reached full accord with respect to debt-management and monetary policies to be pursued in furthering their common purpose to assure the successful financing of the [G]overn-

pointed chairman of the Federal Reserve by Truman. Eccles, meanwhile, was still on the Board and would remain there for a few months before resigning.

Although Fed watchers of the day might have expected Martin’s appointment to essentially negate some the independence gained by the Federal Reserve through the accord, that would not be the case. During his tenure, Martin would protect the Federal Reserve’s independence and sometimes today is referred to as the creator of the modern Federal Reserve. Presiding during periods of strong economic growth, Martin is also well-known for making the often-repeated statement that the role of a central bank is to “take away the punch bowl just when the party gets going.”

After finishing the first term, Martin was appointed to serve a full 14-year term. When Martin’s full term expired, he had served as chairman of the Board of Governors for a record 18 years and nine months.

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## Online Resources

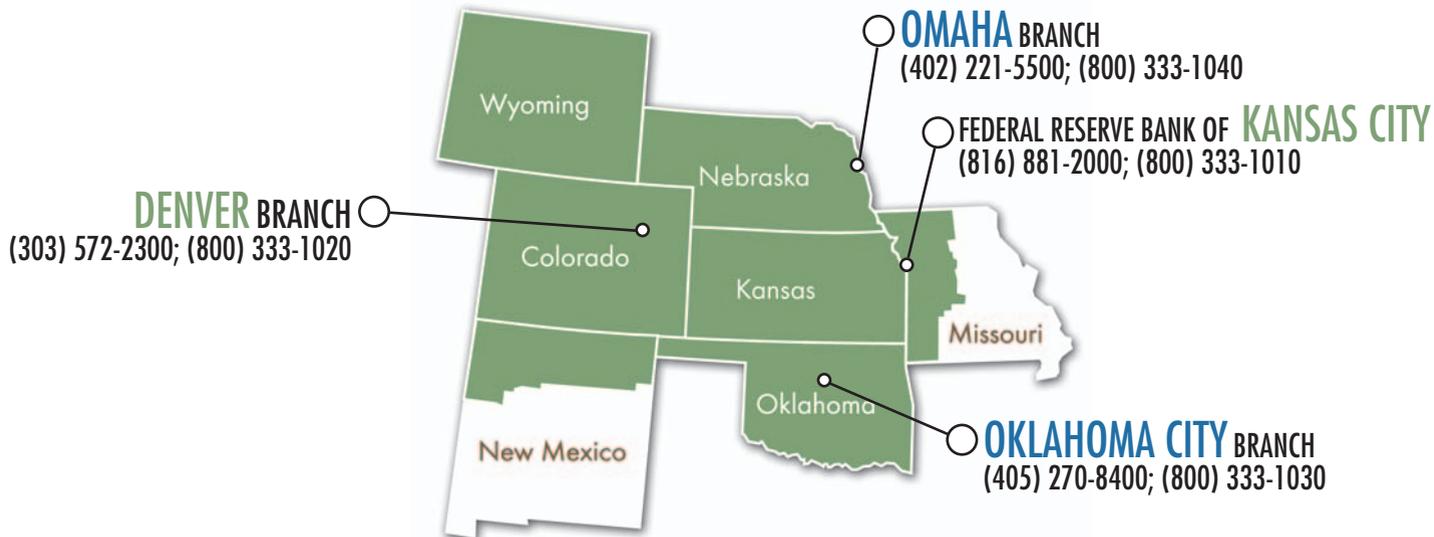
THE BANK HAS A NUMBER OF ONLINE RESOURCES AVAILABLE ON BANKING AND ECONOMIC ISSUES:

BOARD OF GOVERNORS: [www.federalreserve.gov](http://www.federalreserve.gov)

FEDERAL RESERVE PUBLICATIONS: [www.newyorkfed.org/publications](http://www.newyorkfed.org/publications)

EDUCATOR AND STUDENT RESOURCES: [www.FederalReserveEducation.org](http://www.FederalReserveEducation.org)

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