

## **LACKER: BANKING AND COMMUNITIES — A CLASSIC**

'Tis the season. We Americans do it every year.

This month, millions of us will gather around our television sets, settle into armchairs or sofas, curl up under blankets ... and learn a little bit about banking.

We seem to take an interest in it each December.

Of course, it might have something to do with the fact that this primer on banking is a movie classic called "It's a Wonderful Life."

Basic banking is the foundation of our economy, but it's based on a potentially fragile business model. Banks use the money their customers deposit into savings and checking accounts to make loans to other customers. While depositors can rightfully demand their money from the banks at any time, banks generally can't do the same to their borrowers or can do so only at considerable cost. And because banks lend out their depositors' money, they don't have a lot of cash lying around, which means that, in a crisis, when all of their depositors show up at once demanding all the money in their accounts, banks are stuck.

"It's a Wonderful Life" depicts this when George Bailey has to explain to the panicked depositors of the Bailey Building and Loan Association that their money isn't available for immediate withdrawal. When they got shares in the Building and Loan, their money was instead invested in their neighbors' homes.

"You're thinking of this place all wrong," George explains to the gathered crowd. "As if I had the money back in a safe. The money's not here. Your money's in Joe's house ... that's right next to yours. And in the Kennedy House, and Mrs. Macklin's house, and, and a hundred others."

When this happens to one depository institution, like a bank or the Building and Loan, it's a run. When it happens to many at once, it's a panic. The Building and Loan survives this particular panic because George remains committed to his depositors. He understands the community they share, and he knows that their survival depends on stable growth over the long run. George's connections to the community allow him to convince his depositors that, although the Building and Loan is short of cash at the moment, it's still fundamentally sound.

This kind of connection to community bolsters banks. As the president of a Federal Reserve Bank, I think about this a lot because connection to community is what makes Reserve Banks unique.

Discussions about what a Reserve Bank is often get muddled because of widespread misconceptions of the Federal Reserve. When most people think of the Fed, they probably think of a government agency run from the nation's capital. In the Fed's case, they'd be half right; the Board of Governors is indeed an independent federal agency in Washington.

There's a second half to the Fed, however: the 12 Federal Reserve Banks, independent corporations created to serve the public and located in cities far removed from Washington. Reserve Banks coordinate and cooperate with one another to help manage the nation's payments systems and its supply of currency and coin. Reserve Bank employees, who aren't government workers, conduct important research and keep an eye on the activities of many of our nation's banking organizations.

Reserve Bank leaders like me are appointed not by politicians in Washington, but by Reserve Bank directors who in their day jobs are regional industry and community leaders. Each Reserve Bank board has nine members, but only six participate in this appointment process, and by law those six represent the public and aren't allowed to be employed by banks.

These regional roots keep Reserve Banks focused on and attuned to the needs of Main Street — and not just the banks on Main Street. Reserve Banks work closely with businesses, local governments and community groups in their respective regions to help solve economic problems.

In response to the foreclosure crisis, for example, each Reserve Bank launched its own, tailored online Foreclosure Resource Center to help keep more homeowners in their homes and promote neighborhood stabilization. Meanwhile, as small businesses have struggled to obtain credit, Reserve Banks have regularly brought together community leaders, lenders and business owners to help come up with potential solutions to the problem.

Reserve Banks are also an important bridge between local communities and national economic policymaking. Each month, the Federal Reserve Bank of Richmond, where I work, conducts surveys of manufacturing firms, service-sector companies and agricultural lenders from Maryland to South Carolina. Other Reserve Banks conduct similar surveys of their regions.

Just like George Bailey pays close attention to the economic conditions facing the Joes, Toms and Charlies of Bedford Falls, Reserve Bank leaders, through these surveys, get a picture of real businesses in their communities facing real economic conditions. As they prepare for meetings of the Federal Open Market Committee, the group within the Fed that sets important benchmark interest rates, Reserve Bank presidents rely on these surveys for important insights into the Main Street economy.

By the movie's close, angel Clarence has gotten his wings, and "It's a Wonderful Life" has offered its audience a gentle lesson on the importance of banking to communities and vice versa. It's a lesson that I and my colleagues take to heart every day.

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