

Decentralization and the Fed



When people think of the Federal Reserve, many think of the Federal Reserve Board in Washington, D.C., or the Federal Reserve Bank of New York. And with good reason. The Board is ultimately responsible for much of what is done by the Federal Reserve System. And the New York Fed implements monetary policy by conducting open market operations that

move the federal funds rate to the target established by the Federal Open Market Committee (FOMC).

In addition, during the recent economic and financial turbulence, both the Board and the New York Fed have received considerable media attention. They worked closely with large financial institutions, many of which are headquartered in New York, and did much to design and implement the Fed's new lending facilities.

But as the article in this issue of *Region Focus* on the Fed's Beige Book — a survey of economic conditions from around the Federal Reserve's 12 districts — makes clear, the decentralized nature of the Fed is one of its major attributes. It allows each of the Reserve Bank presidents to bring timely, anecdotal information to FOMC meetings, information that may provide insights that official data releases do not yet capture. That can be very important at times, and we are grateful to the many contacts throughout our districts that share this information with us.

But the benefits of a decentralized system do not end there. It promotes information gathering, as I discussed above, while at the same time promoting information dissemination. Reserve Bank officials are able to meet and speak with their constituents about the economy and what the Fed is doing, and hear and address any concerns they may have. For instance, we have held several regional forums throughout the Fifth District since the financial turmoil began, learning the particular issues those areas face. It is hard to imagine how a more centralized system could as effectively engage communities facing disparate economic conditions. In effect, our structure permits us to have deep, ongoing discussions with the diverse economies of our districts.

A good example of this is the issue of foreclosure prevention. Although many communities are suffering from quite high rates of foreclosure, the reasons why those rates have risen often differ quite significantly from community to community. And, hence, the best way to address those

problems also often differs. Staff from the Richmond Fed have provided information and counsel to community leaders active in helping individuals avoid foreclosure, something that I think would have been difficult, if not impossible, if we did not have firsthand, local knowledge of the areas. Former Speaker of the House Tip O'Neill was fond of saying that "all politics is local." In many ways, I think that is true with the economy as well.

In a 1999 article, my former colleague Marvin Goodfriend, now of Carnegie Mellon University, made another point about decentralization that I think deserves special attention. A decentralized system allows Reserve Banks to have different research agendas — to not only focus on certain areas of economic research but also to have unique perspectives on those issues. To put it another way, a Reserve Bank can look at the economy through a particular analytical lens, which can often lead to quite different implications for public policy decisions.

This is useful in many ways, but perhaps the most important is that it increases the quality of debate at FOMC meetings. Prior to each meeting, Bank presidents meet with their research staffs to consider issues that will likely arise when the committee convenes. The input we receive during those sessions — along with the close, ongoing discussions we have virtually every day — enrich our understanding of the key issues facing the economy. The varied perspectives of the different Reserve Banks are brought to the FOMC, where they are advanced firmly but collegially. Ultimately this leads to better policymaking than if research were concentrated solely at the Board of Governors.

I have been at the Fed 20 years now. There are, in my opinion, still many unresolved questions facing central bankers. But one issue that I think can be stated with certainty is that a decentralized system is good for the Federal Reserve and ultimately our nation's economy.

A handwritten signature in black ink, appearing to read "Jeff M Lacker". The signature is stylized and fluid.

JEFFREY M. LACKER
PRESIDENT
FEDERAL RESERVE BANK OF RICHMOND