



## St. Louis plays big role in Federal Reserve

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SPECIAL TO THE POST-DISPATCH

Friday, Feb. 06 2009

Why is there a Federal Reserve bank in St. Louis?

At the time the Federal Reserve System was set up (by Congress in 1913), it was obvious there would be a Federal Reserve bank here because St. Louis was the fourth-largest city in the nation. It was going to be New York for sure, Philadelphia for sure, St. Louis for sure and after that, it was a scramble. Missouri has two federal reserve banks. It made sense at the time for Kansas City to have one.

I've heard the St. Louis Fed was a bastion of conservatism. Is that still true?

Conservative, I don't know. Years ago it was a place where monetarists' ideas had a lot of sway and power.

Within the 12-district federal reserve system?

This bank began collecting statistics on monetary aggregates in the '60s when the rest of the system did not do that. That has carried forward to today. We have the most active data-provision service on the Web.

Just for the Eighth District?

No, that's national and even international data. Also regional data.

You have leeway to follow things that interest you and the staff?

I think that's a great advantage of the Federal Reserve system. It's a team that works together, but there's enough independence that you get different viewpoints.

It's the federalist concept James Madison liked?

Absolutely. The idea was to keep some of the power outside of Washington.

You're on the Federal Open Market Committee, which means you cast a vote on setting interest rates. What's your bias?

At the last meeting, we lowered our target rate essentially to zero. Monetary policy is about supplying money to the economy, and you can supply money regardless where interest rates are. Going forward, I think we'll be talking more about monetary policy.

How can we have so much stimulus from the federal government and not run the risk of inflation?

We are very concerned about it.

How do you counter inflationary tendencies?

The reserves in the banking system are way up. Money supply numbers are up. Usually inflation is a monetary phenomenon. Also, the government is doing a lot of deficit spending. Usually that's considered inflationary. These are concerns.

What people are saying, which I agree with in part, is that a lot of the reserves that are in the system can be taken back out once the crisis is over. The way central banks and the Federal Reserve have handled financial crises in the past, such as 9/11, you put a lot of reserves in the system during the period of the crisis, then you take them back out shortly thereafter. That doesn't cause inflation and works pretty well.

The big question is, are you going to be able to unwind and take all of this liquidity out of the system? I think basically you can, but there are starting to be some issues about that.

Aren't we putting a lot of money into the system in the next year or two?

The capital purchase program, which is coming out of the Treasury, is \$700 billion. That's used to buy bank assets. You can sell that off at a profit someday if things go well. That's a bit different than your ordinary government expenditure. You do have something of value that you can sell.

What do you think about taxes at this time?

Normally, you wouldn't want to raise taxes when the economy is down like this. That's probably a bad idea. It will be helpful if we can get through this recession and the financial crisis without creating a burdensome federal presence.

You've said this is not the Great Depression.

This is a different scale entirely. But it's turning out to be a pretty sharp downturn.

When will it be over?

I'd be hopeful for the last half of 2009.

What are the leading indicators that will tell us we're coming out of this?

Overall GDP (gross domestic product) growth.

Housing?

I'm still hoping housing will stabilize in the first half of the year. It's been at such a low level I think we can get some stabilization in housing starts. We've been saying that for a while.

Consumer confidence is very low.

It's hard to know why people are as hesitant as they are. They are as pessimistic as they were in the early '80s, when unemployment hit 10.8 percent. We are only above 7 percent now. We have nearly three and a half percentage points to get to that situation now. Why people should be as depressed as they

were in '80s I don't know.

Have we journalists portrayed this incorrectly?

I think the media talks to people, and people are pretty pessimistic.

What do hear when you speak to groups around the Eighth District?

In 2008, that uncertainty about the economy really bloomed up. When uncertainty gets very high, people tend to pull back. This crisis woke people up that probably haven't thought about the economy in the last five years. They were going along and all of a sudden, it's: "What's this? I should put off expenditures, and I shouldn't replace my car." Car sales are way too low, considering normal replacement.

Are the people you meet particularly concerned about any particular sector — agriculture, manufacturing, retail?

Earlier in 2008, you could talk to people about some sectors, like technology. My contacts said things were fine. Now everybody's affected. That's a defining feature of a recession, when things cut across many sectors. In normal times, there might be a particular sector that's not doing that well. In a recession, everybody's doing badly.

Will the recession and the new Congress and new president have an effect on globalization?

One thing about globalization is people were thinking there was this de-coupling going on. The U.S. is a big economy. The European Union is big. Japan is smaller, but has a large per-capita basis. The rest of the world is catching up. The idea was that some of these economies were very dependent on the Western countries as far as their own economies go. Now they have got big enough that that is no longer true.

So the U.S. economy is still the economic engine of the world?

Yeah. You guys were a little premature in saying this de-coupling (from the

U.S.) was going on. As soon as the U.S. and Europe went down, everybody had a lot of trouble. It tells you it's still very important that the large industrialized economies are healthy.

Do you worry about a retrenching and growing protectionism?

I haven't heard as much as I might have expected. In times of prosperity, like in 1998, people start talking about trade restrictions. Why? I don't know.

I read that one issue President Obama may consider is renegotiating the North American Free Trade Agreement (NAFTA).

He has chosen his policy advisers, (Lawrence) Summers in particular, who, as far as I know, have expressed broad support for free trade.

Do you like his economic team?

I do. Tim Geithner (the Secretary of the Treasury), of course, was my counterpart from New York.

Nothing too radical?

I think they'll be centrist.