

Reflections of a Freshman CEO

**Remarks by Cathy E. Minehan,
President and Chief Executive Officer,
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**UMASS Pre-Commencement Dinner
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It has now been over a year since I moved from being chief operating officer to chief executive officer at the Boston Fed. While there is only one word different in the two titles, the difference between "operating" and "executive" has been quite dramatic. Today, I would like to share with you some of my reflections on that transition, reflections both on the professional aspects of the change and on the personal. After all, this is the time of year for transitions, and tomorrow is a very important transition in the lives of the UMASS Boston graduates who will be honored.

A central part of the shift from COO to CEO at the Fed means becoming a member of the Federal Open Market Committee--the group that meets every six weeks to set interest rate policy. In March of last year, I attended my first FOMC meeting. While I had certainly worked in the Reserve System for a long time, I had never attended a Committee meeting. My predecessor Dick Syron never had the good grace to be away at the time of a meeting, and I never was a "back

bencher", so it was all new territory. Prior to the meeting I read two years worth of minutes (honestly, I did) and then sought help-- both from old friends in New York and from my new staff. Where do I sit? What really happens? How do I know when to talk? What do I talk about? And mostly, I thought about two questions: First, how could I, with a background largely in making things in the Federal Reserve System work rather than in monetary policy formation, contribute to this most fundamental task of the central bank? And, second, especially after I became President, what particular role does the President of a regional Reserve Bank play in monetary policy making? I'd like to focus the first part of this talk on the answers to these two questions.

As most of you know, my formative years at the Federal Reserve Bank of New York were spent largely in the area of payment systems, and related supporting activities like doing budgets, running computers, accounting and the like. In the seventies, these areas were a good definition of the backwaters of a Reserve Bank, but by the eighties, given changes in technology, the volumes and values of payments being transferred, and the periodic crises involving payment system risk, knowing how things actually work, and being able to make them

work in a problem situation became a powerful adjunct to policy-making. Thus, it was a great time to be in those areas. We in operations became the close allies of policy makers in a crisis, and important players on the team when it came time to figure out how to handle things better the next time. This was an extraordinary time to learn, and I've found the lessons of this period very powerful in establishing the framework within which I make my decisions regarding monetary policy. What are those lessons?

- o That in addition to price stability the country's, if not the world's, financial stability is the overriding responsibility of the U.S. central bank;
- o That a central bank's credibility is essential to its ability to step into a crisis as a trusted intermediary and promote stability; and
- o That credibility comes in large measure from the expertise it develops over the years and, most importantly, the control the central bank exerts on inflation, since low and stable rates of inflation produce incentives throughout the economy that work in the direction of encouraging productive growth rather than excessive speculation.

So, to cut to the question reporters like to ask: does this make me a hawk or a dove? Neither, I think, since I believe the essence of monetary policy formation is much more subtle than the simplistic hawk/dove dichotomy. However, the lessons of the 80's have made me a staunch defender of the course monetary policy has been following. I believe the focus on containing inflation begun in the early part of that decade has resulted in longer periods of cyclical economic growth, lower interest rates at cycle peaks, and, at the same time, lower unemployment rates, at cycle troughs. It hasn't been perfect, but it has laid the groundwork for the United States regaining its position as one of, if not the, most productive and competitive world economies. That, I think, is the very definition of success for a central bank.

With this perspective, I have approached this first year at FOMC meetings, and now as a voting member, with the old physician's oath in mind "Do no harm." In 1994, the strength of the economy kept exceeding most forecasts while inflation remained well controlled; in anticipation of price problems given tight labor markets and high use of productive resources in general we at the Fed raised short-term interest rates seven times. Now in 1995 things are getting especially

challenging as most indicators suggest the slowdown we were aiming for seems well underway.

But will it be enough? Is what we're seeing now that long sought-after "soft landing"--or what might be better characterized as a levelling-off while still in flight--accompanied by a short cyclical blip in inflation? Is it the beginning of a downturn and higher inflation, a recurrence of the dreaded period of "stagflation" of the late 70's, albeit in single-digit rather than double-digit inflation? Or is it a mere pause in spending both by consumers and businesses that, given lower long-term interest rates and a better competitive picture in international markets, will be over by the end of the year with a substantial pick-up in growth and in inflationary pressures? I think you could find support for any of these arguments right now, making this an especially difficult and interesting time for monetary policy makers.

Now on paper, the monetary policy decision process looks unwieldy--some might even say messy. Nineteen participants--some appointed with Congressional approval, others selected by private Boards of Directors with agreement by Washington. Of these nineteen, twelve members who vote at any point in time, eight on a permanent basis and the others with votes rotating based on an

arcane system that at times seems inspired by astrologers. Some members are based in Washington, others in cities across the country, the location of which reflect the population and political centers of the early 1900's. It's hard to believe that such an arrangement would work well, let alone produce a coherent monetary policy. Nonetheless, external appearances notwithstanding, I would argue that this arrangement, this awkward-appearing system of checks and balances, this blend of public and private inputs, has worked well for many years and, as I noted earlier, has worked particularly well recently.

Undoubtedly, much of our success has to do with the good fortune we have had in the men who have served as Chairman. Both Alan Greenspan and Paul Volcker deserve much of the credit for our success. But as great as their contributions have been, some of the credit also goes to this seemingly ungainly federal committee system in which not all of the input to decisions comes from Washington, D.C. (or even the combination of Washington, D.C. and New York City) but some portions come from provincial outposts like St. Louis, Richmond, and yes, even Boston. Specifically, I believe that the contribution from outside the Beltway has been a major factor in making the Federal Open Market Committee an effective institution.

Economics, as some of you are probably already aware, is NOT an exact science. This applies fully, if not doubly, to monetary policy, which, as you know, works only with a lag. Like it or not, forecasts and reasoned, experienced judgements about future economic prospects, and about the variety of financial market reactions are an integral part of monetary policy because of this lag in its impact. Such judgements and forecasts form a place to start but they necessarily are surrounded by a cloud of uncertainty.

Recognizing this, it is important to have a wide-ranging, active debate about the assumptions that underlie the starting point. Where are the risks to this "best guess?" Are these risks evenly balanced, or asymmetric to one side or the other? And what the prospects are for whatever policy is ultimately adopted? This debate means that more than one perspective, more than one school of thought, more than one econometric model can make a valuable contribution. And I also think it means that there's a lot of room for the contributions of those of us with less mathematical, but more experienced-based senses of both the tenor of economic growth and the feel of the markets. Ultimately, monetary policy formation ends up being a process of exercising judgement, with very few clear-cut rights or

wrongs. The Committee has to make a call, and to do so we all have to learn from each other, even from those with whom we ultimately may disagree.

One of the contributions the "salt water" economists in Boston have made over the years is to focus FOMC attention squarely on the fact that while controlling inflation is the key objective of monetary policy, inflation works through the product and factor markets of the economy. If you want to understand and predict what inflation will be, you have to look beyond just money growth or just interest rates or even Wall Street, to the nonfinancial parts of economic activity. The 1987 stock market crash was a dramatic event, but it hardly put a dent in the pace of economic activity and ultimately in the upward creep of inflation. After several false signals from gold and commodity prices, it has ultimately been the increased pressure of the "real economy" on our productive capacity that has provided me with the justification for the Federal Reserve's tighter policy since February 1994. And it will be signals from that real economy first, as well as reflections on all the other market factors, that will provide the justification for easier policy when that is needed.

In addition to providing a forum for different schools of economic

thought to flourish and interact, the decentralized system also provides insight into economic conditions in each region. A region's economic experience can differ quite markedly from the national average and these differences can provide an "early warning" of developments that could affect the nation as a whole. A case in point is the New England experience during the 80's. I am told that Frank Morris, then President of the Boston Fed, was a voice in the wilderness regarding the problems inherent in the excess of real estate lending in the mid-80's. This fueled a sizeable economic boom in New England, but the recession that followed was much deeper than the national downturn. The combination of a declining economy and a collapsing real estate market led to severe problems at the region's banks. As banks struggled to survive, they cut back their lending, which further exacerbated the regional recession.

New England's problems were later echoed elsewhere; but because of New England's earlier experience, the FOMC was already sensitized to the contractionary effect of disruptions to the availability of bank credit. This was one of the headwinds to which Chairman Greenspan referred frequently during the early stages of the national recovery and served as impetus to the monetary policy actions taken

to counter those headwinds. This experience is testimony, I think, to the value of the federal committee system, and to the importance of the regional Reserve Banks in setting national policy. Representing this District, in some senses representing all of you in this room, is a part of this job I take very seriously.

Now let me turn the remainder of my thoughts for you this evening to some more personal considerations. I noted earlier that two questions had preoccupied my thoughts as I took over the Boston Fed CEO position, and became an Open Market Committee member. There was a third. How important was it that I was the first woman to be president of the Bank, and the only female peer of eleven other white male Reserve Bank Presidents? I think after nearly a year I am inclined to answer that question quite differently than I would have early on.

In progressing through many levels at two Reserve Banks, I had largely focused on doing the best possible job I could at whatever job I had. I never considered my gender as either a plus or a minus. Even when tempted to reflect on a minor setback as perhaps indicative of sexism, I was always convinced that what I was feeling was some doubt on the part of others that I was ready for a new challenge, rather than concern about my ability to meet it simply because I was a

woman. Reaction to my getting the Boston presidency, however, has made me rethink and reshape my perspectives in this area, and reflect a bit on the importance of diversity in the corporate environment, and in society as a whole.

I must say that the overwhelmingly positive reaction by women both in banking and in other professions to both the prospect and the reality of my getting this job has been a pleasant surprise. When Dick left for the American Stock Exchange, I found myself the focus of a network of well-placed women around town who saw my getting the job as an objective of some value. They counseled me, took me to task when necessary, and generally provided the support that's necessary when one is enduring months of a public, nationwide search while also trying to do two jobs--that of the COO and the acting CEO. Those women were incredibly helpful, because they saw, as perhaps I didn't at that point, that my getting this position would have powerful meaning to many other women. And so it has. Women tell me all the time how remarkable it is to see a woman at my level, and how it makes their own progress seem more achievable. They see the diversity that I bring to top levels of the Boston and national financial scene as an important breakthrough that may be the harbinger of a

better gender balance at the top in the future.

This is clearly a benefit of increasing diversity within business--an opening up of new vistas which cannot help but increase the contribution of our increasingly diverse staff. Moreover, just as our employees are more diverse, so too is the marketplace in which we all deal, both here in the U.S. and internationally. To compete in the global arena , increasingly we must have teams that reflect those who will buy our products and services. But diversity in the corporate world and certainly for the larger society itself is far more important than simply a means to compete. Diversity challenges us as individuals to define ourselves and what our personal values are, in the midst of a galaxy of competing cultural and intellectual frameworks. It forces us to recognize who we are and what we are about in a way that a more homogenous world never could. This is not an easy challenge--for many it is incredibly difficult.

For some diversity increases choice. For others it increases competition. For a few, however, it is a scapegoat that can be blamed for one's inability to deal well in the larger society. I think we've seen the uglier side of the threat that our increasingly diverse society can pose in recent months, in a very minor way in the questions raised

about affirmative action goals and in divisive rhetoric both locally and nationally, and in an exponentially more important way in what we've begun to learn about the extremists who have so forcefully commanded the front pages of our newspapers. Diversity demands tolerance, but we as educated people cannot be tolerant of extremes of thought and action brought on by ignorance, frustration or racial hatred. We must work against extremism, and uphold those standards of human discourse that define a just society. We must make it possible to celebrate the next woman who becomes a CEO, the next African-American who becomes a leader, the next gay person who assumes responsibility as a sign of hope for both those minorities amongst us and for all the rest of us as well. And I must say that institutions like UMASS-Boston, with its commitment to both diversity and the best standards of education, stand as shining beacons as we try to find our way to that just society we treasure.

In closing let me say that the past year has been an extraordinary time for me. I've learned a lot about what it takes to be effective in the area of monetary policy formation, and how to go about representing this region. I've also developed a new perspective about the benefits of diversity, and some of the challenges it presents. But

most of all I've been struck by the enormity of the responsibility this job brings with it. After attending FOMC meetings for about nine months, my rotation as a voting member came around this past January. Blithely I thought that the change would make little difference since each FOMC member, voting or not, contributes equally to the discussion. Imagine my shock then when I found myself almost shaking when my name was called for my first vote. Exercise of that responsibility cannot be a rote or mechanical function; the very real human impact is too important. To me this position is the pinnacle of a career spent in public service and the intellectual challenge of it, as well as the ability to make a real impact on the country's economic welfare, make it an incredible opportunity as well.

I appreciate your allowing me to share these thoughts with you tonight. I've enjoyed the chance to reflect and I hope you have as well. Thank you.