

# Remarks Before the 6th Annual YMCA Key Leaders Lunch

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*The views expressed are my own and do not necessarily reflect official positions of the Federal Reserve System.*

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I was tempted to title this speech “A Trip to Egypt,” for just as there are myths and suppositions about ancient Egypt, all too often, the business of the Federal Reserve has been viewed as a riddle wrapped inside a mystery inside an enigma. This afternoon, I would like to take some of my time with you to unlock that mystery—to take a peek into the inner sanctum. I’ll then end with a word about our economic future in this great region of this great state.

Despite the general mystique that traditionally surrounds central banking, I would bet that at least some of the folks in this room are familiar with William McChesney Martin—the man who served as Chairman of the Federal Reserve Board longer than anyone else in the institution’s history.

While some of you might recall that Bill Martin was a longtime chairman of the Fed, far fewer of you are likely familiar with his failed bid—and I use the word “bid” very generously—for the presidency. Let me explain. Once a year, a group called the Alfalfa Club—one of the great institutions in Washington, D.C.—holds a dinner devoted solely to poking fun at the political pretensions of the day. Tongue firmly in cheek, the club nominates a candidate to run for the presidency on the Alfalfa Party ticket. Of course, none of them ever win. Nominees are thenceforth known as members of the Stassen Society, named for Harold Stassen, who lost his bid for the presidency nine times before running and subsequently losing a tenth time on the Alfalfa ticket. The group’s motto is “Veni, Vidi, Defici,” a phrase loosely taken from the Latin for “I came, I saw, I lost.”

In 1966, while serving as Fed chairman under his fourth president, Bill Martin was nominated to run for the American presidency on the Alfalfa Party ticket. In his acceptance speech, he announced in jest that, given his proclivities as a central banker, he would take his cues from the German philosopher Goethe, “who said that people could endure anything except continual prosperity.” Therefore, Martin continued, he would adopt a platform to “make life endurable again, by stamping out prosperity.”

“I shall conduct the administration of the country,” he said, “exactly as I have so successfully conducted the affairs of the Federal Reserve. To that end, I shall assemble the best brains that can be found...ask their advice on all matters...and completely confound them by following all their conflicting counsel.”

Martin gave his Alfalfa Club speech some 52 years after Congress passed the Federal Reserve Act and President Woodrow Wilson signed it into law so as to encourage, not stamp out, economic prosperity. One of the more successful and brilliant aspects of this legislation was the creation of the 12 regional banks. The Fed could have been set up solely in Washington, like so many other institutions of the central government. Having representatives from all parts of the country, however, brings a deeper, more diverse perspective (and occasional “conflicting counsel”!), unfettered by politics or political imperatives, to the policy debate at the meetings of

the Open Market Committee when we collectively determine monetary policy, giving a clearer view of what is really happening in the U.S. economy. The regional banks maintain branch offices in cities within their district to stay in touch with local economic conditions and business leaders. In the case of the Dallas Fed, we maintain branches in Houston, San Antonio and El Paso.

If you truly wish to unlock the mysteries of the Fed—to take a peek into the inner sanctum—you should start by learning a little about the businesses we operate in Dallas as a part of the central bank of the United States.

When I was a student at Oxford, the great insurance magnate of that time, Clement Stone, came to speak at the Oxford Union. A student asked him to kindly share with the audience what he considered the key to success. He looked out at the audience, curled up his Ronald Coleman mustache and said: “In one word: cash.” So let’s start there. One of the duties of the 12 Federal Reserve Banks and their branches and depots is to provide to the banks in their districts what Clement Stone considered the key to success: cash.

Our main cash vault in Dallas is the size of a five-story building. That vault holds lots of Federal Reserve banknotes—what you might know as dollar bills. Through the third quarter of this year, we distributed and received 4.2 billion circulating banknotes, worth nearly \$76 billion at face value. That’s almost \$490 million in cash passing through our Pearl Street vaults every day. This is a thing of beauty to watch. Our mammoth machines scan the cash at an average rate just shy of 100,000 bills per hour. They cull about 780 counterfeit bills each month. They pluck out almost 39 million worn bills each month—valued at \$538 million—and we then shred them and send them off to Money Heaven. The life span of a typical \$1 bill, incidentally, is just 21 months. A \$20 bill lasts 2 years, and a \$100 bill—the largest denomination of currency in circulation since 1969—lasts nearly seven and a half years.

We also process checks. From January through September of 2009, the Dallas Fed processed 69.2 million checks, worth about \$58.4 billion. Over the same period, we’ve handled a daily average of 364,000 paper checks—although that business has been, and will continue to be, on a substantial decline. Due to advances in technology, many banks now send us checks electronically in a digital format. We received and processed an average of 543,000 electronic images each day through the first three quarters of this year.

Another important function of the Dallas Fed is to provide liquidity to District depository institutions through our discount window operations—to be what some have called a banker’s bank. The lending programs that make up our discount window help relieve liquidity strains by providing a source of short-term funding, which must be fully secured, to depository institutions in times of need. In 2008, we made 273 loans approximating \$30 billion. I chair our credit committee and personally review the loans we make every evening. Some of them are very large (a billion or more) and some very small (as little as \$10,000), depending on the needs of the borrowing bank, for overnight purposes or, during the recent financial crisis, up to 84 days so that they might conduct uninterrupted business on behalf of their customers.

Among our other responsibilities is supervising the banking industry within our respective district. We conduct on-site audits of our member banks and monitor bank performance and stability measures using electronic surveillance technologies.

This supervisory role is important. I began my private-sector career at the bank of Brown Brothers Harriman & Co., where my superiors instilled in me one overarching principle—one I'm sure the bankers in this room know quite well: Know your customer. Well, we at the Fed rely upon our regulatory relationship to better “know our customers,” actively monitoring our constituents’ needs and services on the front-line of the commercial banking industry.

The Dallas Fed has also launched public education programs designed to raise financial and economic literacy in our community. We frequently host public events and conferences on significant activities within our economy.

We also do serious economic research, designed to provide the intellectual heft for informed monetary policymaking. Our Research Department employs a crack team of economists and analysts who study the local, national and international economies. Their work is top-notch. Few of you might know, for example, that Finn Kydland, an associate of our research team here in Dallas for the past 15 years, won the Nobel Prize in economics in 2004.

Like many of our other operations, our research function is spread among our branches. In addition to tracking trends across Texas, our economists in San Antonio and Houston and El Paso maintain a keen interest in subjects like the U.S.–Mexico border economy and energy markets.

The Dallas Fed has also taken upon itself the job of contemplating how globalization impacts the execution of monetary policy with the formation of the Globalization and Monetary Policy Institute. While still in its nascent stages, this group has produced a hefty volume of original work and collaborated with top minds around the world to devise new theories and models to understand this oft-overlooked economic link. This Institute is privileged to have on its board the central bank governors of Japan, Singapore and Mexico; the Deputy Governor of the Bank of England; the former deputy of the European Central Bank and other notables that help bring an informed global perspective to our work and, I might add, help us showcase Dallas to the world.

While currency processing, banking supervision and research efforts are an important part of the Fed’s job, they are certainly not the part of central banking that garners the most public attention. The sexier bits of what I do—to the extent anything in central banking is considered “sexy”—deal with monetary policy.

As president of one of the 12 regional banks I described earlier, I have the privilege of serving on the Federal Open Market Committee: the Fed’s central policymaking body. Together with the five Board governors (two shy of normal, thanks to a hold-up in the nomination and confirmation process), we meet every six weeks to discuss the current trajectory of the economy and craft the appropriate policy response.

Our statement, released like clockwork at 2:15 Eastern time, outlines the committee’s thoughts and subsequent policy actions. Parenthetically, I might note that the Federal Open Market Committee is one of the few decisionmaking bodies in the world where members can come together and, in the span of only a few hours, present their positions vociferously, agree to a course of action, craft a statement for public release and, most importantly, break in time for lunch.

It is also a place where Texas, like the other states, has a voice at the table of making policy for the most powerful and essential central bank in the world. The President of the United States appoints and the Senate confirms the governors of the Federal Reserve System. The member bankers in Texas and the Eleventh District elect a nine-member board of directors—similar to the other 12 regional banks. Those boards hire and fire the bank presidents.

I was hired by a board led by Ray Hunt. Presently, I serve at the pleasure of a board of directors that includes Herb Kelleher; Mike Ullman, the chairman and CEO of J.C. Penney; Margaret Jordan, the president and CEO of Dallas Medical Resource; and Bob Estrada, who most people in this room know, among others. I mention this to underscore that I and my fellow bank presidents represent Main Street and not the Washington political establishment or Wall Street. And I want you to know that every time I speak or intervene in our policy discussion at the FOMC—which is quite often—I do so very much with that in mind.

Suffice it to say that those who serve alongside me in the hallowed halls of the Federal Reserve spend every waking hour doing their level best to perform their duty. You should take comfort in that fact.

Now, I know, Gordie, that you wanted me to say a few words on the economy. In a word it is *improving*. But slowly. The national economy is trying to work its way out of our [AD LIB]. If you will indulge me, I'd like to wrap up my remarks with a discussion of an issue that I hold near and dear to my heart—one that has a significant effect on this region's future and economic prosperity and is key to our long-term economic success as a city and as a state.

Dallas–Fort Worth is the fourth-most-populous metropolitan area in the country and the sixth-most economically productive. Texas ranks second in the nation in population and productivity, surpassed on both fronts only by California. We produce more economic output in the Lone Star State than India does. Or Mexico. We are a global economic power.

Texas has six major public university systems. The University of Texas System is the granddaddy of them all, with just under 200,000 students in nine universities and six health institutions. The Texas A&M System has eleven universities with 100,000-plus students and a multicampus health science center. The remaining students are spread over the campuses of the Texas State University System, the University of North Texas System, the University of Houston System and the Texas Tech System. Stephen F. Austin, Midwestern State, Texas Southern and Texas Woman's are each independent public universities. Together, these institutions house over 530,000 students.

By contrast, California has more than 650,000 students enrolled at just 33 public campuses. The granddaddy of that state educational system is the University of California, with 220,000 students spread over 10 universities.

How many people in this room think that Berkeley is the only center of excellence in the University of California System? Not one of you. And that is because you know that in addition to Berkeley, the University of California System has UCLA, UC San Diego, UC Irvine, UC Davis and UC Santa Barbara. All that before you take into account Stanford, USC, CalTech and the Claremont Colleges.

Now here is a fact. According to the latest *U.S. News & World Report* survey, Berkeley, UCLA, UC San Diego, UC Davis, UC Santa Barbara and UC Irvine all outranked UT Austin—which placed 47th—for overall educational excellence. And the rest of our universities? Texas A&M was ranked 61st. SMU ranked 68th, Baylor 80th and TCU—despite the high rankings of its powerhouse football club—110th. The shining star in our higher education galaxy is Rice, ranked 17th, behind Johns Hopkins and tied with Vanderbilt and above Berkeley.

Hold that thought: The “overtaxed, over-regulated, left-coast state” of California has within one fleet six universities that are ranked equal to or better than UT Austin, our flagship.

Now let’s broaden our aperture a little by looking at membership in the Association of American Universities, which is regarded by most scholars as the definition of the cream of the crop of research universities. The AAU consists of 60 U.S. and two Canadian universities. These 60 U.S. schools garner about 57 percent of all federal R&D dollars to colleges and universities; they are home to 81 percent of all elected members of the National Academy of Science, the National Academy of Engineering and the Institute of Medicine—the highest recognition in each of those fields. Since 1901, 35 percent of all Nobel Prizes have gone to individuals affiliated with AAU universities. It is fair to say that everyone in this room would like to have our Texas universities included in this prestigious group of 60.

California has nine AAU members, with four of those in the greater Los Angeles area alone. New York has seven: Columbia, Cornell, New York University, Syracuse, Stony Brook University, the University of Rochester and the University of Buffalo. You actually should add an eighth by including Rutgers, which is within arm’s reach of New York City.

And Texas? We have three: Rice, UT Austin and Texas A&M.

Think about that. The great state of Texas—the state I love to brag and boast about; a state of over 24 million people that has a glorious history second to none and an economic powerhouse that produces more than India or Mexico—has the same number of AAU member universities as the greater Boston area. And Dallas, our hometown...has none. Think about that: The eighth-largest city in America does not have a single top-ranked academic institution. We do have UT Southwestern, a top-tier medical school, of course. But a medical school standing alone, no matter how good, is not enough in a world that is built on advanced technology and in-depth knowledge across many fields.

Now, how can we expect to navigate our way into the economic future without a single elite university in our city? How can we expect Dallas to excel in the Knowledge Age—the era in which economic prosperity and wealth will be defined by cyberspace, nanotechnology, robotics and biology and mathematics-driven financial expertise—without at least one established fountainhead of advanced knowledge? How can we reasonably expect the youth of Dallas—a group that I know people like Gordie and the good folks in this room care very much about—if we aren’t providing them with top-notch preparation for the economy of tomorrow?

Economists may quibble about a lot of things, but they are united on this: Education pays off. We can see it in wage data provided by the Bureau of Labor Statistics. The U.S. economy today is far different than the one that employed our parents and grandparents in the fields and

factories. Agriculture represents less than 2 percent of our national economy. Oil, gas and mining account for 5 percent. Manufacturing employs nearly 10 percent of our workforce. Roughly 80 percent of American workers are employed in services, a sprawling sector that includes some of the nation's most prestigious and highest-paying jobs. In Texas, average hourly wages in 2008 were \$77.22 for internal medicine doctors, \$42.67 for geological engineers, \$43.50 for computer software engineers and \$29.70 for registered nurses, according to Bureau of Labor Statistics estimates. Those are handsome earnings compared to Texas' overall average hourly rate of \$18.90. We want as many of our people as possible working in those higher income brackets. And the only way to accomplish that is to build our prowess in higher education.

When we leave this luncheon today, I want you to look around Dallas' cityscape. Tell me how many factories you see. You won't see one—at least not any of the old-fashioned kind with smokestacks and loading docks and noisy machines. Instead, you will see glass and steel buildings that house the machines and the capital stock of the modern economy: human brains. Those brains are employed in many of the high-value-added sectors I just described.

The brain is to this Knowledge Age what the motor was to the Industrial Age. And education is the oil, the fuel that drives the knowledge economy forward.

We need more of that brain power, right here in River City. We need thousands upon thousands of the world's best and brightest here in Dallas. We can fuel our economy with graduates from California and Massachusetts and other states and other countries—up to a point. But that is no substitute for Texas- and Dallas-bred intellectual talent, with its roots in the community and its commitment to building Big D and all the benefits it would bring to the arts and civic and educational communities on top of the economic muscle it would add.

I referred to Egypt at the beginning. Here's the punch line. If any of you leave this room today willing to accept the fact that Dallas, Texas, does not have one university ranked in the top 60 by either *U.S. News & World Report* or the Association of American Universities, then you are not the Dallas-ites whom I know and love. If any of you are willing to accept that David Daniel at the University of Texas at Dallas or Gerald Turner at Southern Methodist University or Daniel Podolsky at the University of Texas Southwestern Medical Center or Victor Boschini at Texas Christian University or Jim Spaniolo at the University of Texas at Arlington is fighting with one hand tied behind his back because the powers that be in Texas cannot rise above parochialism and give to this city what California has in San Francisco and Silicon Valley, or Los Angeles or San Diego or Santa Barbara, or what New York has in Manhattan, Rochester or Buffalo, then, well, you, my friends, are, as they say, in Egypt—suffering a serious case of denial.

Thank you.