FEDERAL RESERVE BANK *of* NEW YORK *Serving the Second District and the Nation*

Remarks by

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I am delighted to be here this morning to address such a distinguished group of Long Islanders. The many strengths of the New York metropolitan area as a financial and business center, and as a desirable place to live and work, are of great importance to me and my institution. The Federal Reserve Bank of New York employs far more workers than any other Federal Reserve Bank -- some 3,500 at our headquarters in Manhattan and our operations center in East Rutherford, New Jersey -- and thus has a large stake in the economic and social well-being of the New York metropolitan area. In that context, my Bank takes very seriously its responsibility to be an active, contributing corporate citizen.

Today, I would like to begin my remarks with some comments about the performance of the national and regional economies. I also will discuss with you a major challenge that I believe must be addressed head on by the business and professional community of the New York region, in partnership with state and local governments.

Let me start with a few words about the economic picture for the country as a whole. The national economic expansion, already one of the longest of the post-World War II era, is entering its sixth year and shows few, if any, signs of coming to a halt. In fact, I am quite encouraged in many ways by the recent performance of most of the key indicators.

One of the most positive features of the ongoing expansion is the continued good news about inflation. Consumer price inflation, while up slightly during the first quarter of this year, gives no indication that it will accelerate persistently over the months ahead. If that turns out to be the case, one could say that "the beat goes on." As you may recall, the CPI increased by about 3 percent or less in each of the last five years, a record unequaled since the 1960s.

I think it's fair to say that at least some credit for the nation's favorable inflation performance belongs to the forward-looking policies set by the Federal Open Market Committee. The FOMC's policy of monetary restraint, which began in February 1994, brought about a much needed slowing of aggregate demand, which had started to run well ahead of the economy's productive capacity. That move was not without its critics, coming as it did well before most analysts and economists had seen an uptick in the rate of inflation. The Fed's pre-emptive strike against the threat of inflation was necessary, however, because monetary policy works with long and uncertain lags. Although most of the effects of monetary policy on output take place within one to two years, its effects on inflation take even longer -- on the order of three years. Thus, it was clear to us in 1994, and it's just as clear today, that the failure to contain inflation at its earliest, incipient stages only makes it costlier and more time-consuming to bring it under control later.

Although actions by the FOMC play a major role in containing inflation and weakening inflationary expectations, monetary policy, in and of itself, cannot serve as the wellspring of real long-term economic growth. Real growth over time results from increases in the quality, productivity and supply of labor and capital, and from innovations in the way these factors of production are used.

What monetary policy can do is raise or lower the rate of money supply and credit growth, and help to move interest rates to levels consistent with the goal of economic growth with price stability. In the process, the Fed's actions and pronouncements can influence the expectations and confidence of consumers and businesses and, thereby, what they do in the various economic and financial marketplaces. Only by the Fed muting both inflation and inflationary expectations can households, businesses and governments make the decisions and take the steps that create jobs, profits and the steady rise in output from which everyone in our society benefits. Thus, monetary policy can best help to foster economic growth by ensuring the continuation of a stable price environment.

Over the last five years, economic growth has come more grudgingly to our region than it has to the nation as a whole. The 1990-1991 recession hit the New York City metropolitan area earlier -- and hung around longer -- than was the case in most of the rest of the country. Although the region has gained back some of the employment lost in the previous cycle, the recovery here has not been nearly as vigorous as the national recovery and subsequent expansion. Large-scale restructuring in the financial services sector, continued downsizing in manufacturing and defense-related industries, and the bursting of the bubble in real estate values all have contributed to the region's plodding advance. More recently, sharp cuts in state and local government spending, and the resulting loss of thousands of government jobs, have been major impediments to the region's vigorous overall recovery in employment.

Long Island, which leads the state in economic growth, has been a welcome exception to this general trend. In 1995, payroll employment in Long Island rose 1.7 percent, twice the rate in New York State, following comparable gains in 1994. In terms of numbers of jobs, Long Island's gain of 20,000 new jobs in 1995 represented one-third of total job growth in New York State. As of the first quarter of 1996, Long Island's unemployment rate of 4.8 percent was well below the State's rate of 6.2 percent.

During the first quarter of this year, Long Island gained another 9,000 jobs on a year-over-year basis. Wholesale and retail establishments have expanded at a moderate pace. Demand for business and consumer services has added to job growth. Although the overall manufacturing sector continues to contract, reflecting the wind-down in defense spending, here too there are signs of growth. Sectors such as pharmaceuticals, bakeries, and apparel are developing niche markets and expanding their workforce.

In addition, the housing market has picked up. Although housing starts remain weak, the large, established market for existing homes has strengthened and prices are rising following moderate losses last year.

In this connection, let me say a few words about a project the New York Fed has recently initiated in partnership with the Long Island Association and a number of other co-sponsors in the area. Entitled the Long Island Home Purchase Process Initiative, the project is designed to identify barriers in the home purchase process, bringing together real-estate and related industry professionals. Our goal is to produce positive and lasting results in ensuring access to home mortgage credit throughout Nassau and Suffolk. Three other Reserve Banks are testing this approach as well -- San Francisco, St. Louis, and Boston.

The Long Island project is unique in that it is the only suburban site among the Reserve Bank initiatives. Issues of access to home ownership can occur in any number of points and we believe the key is to open discussion among all of the players involved in the process. More equal access to housing means economic opportunity for Long Island and the surrounding region. Opportunities for low, moderate and middle income home buyers and minorities mean opportunity for real-estate and related professionals, appraisers, real-estate lawyers, realtors, property insurers, banks, title and mortgage companies.

I am very pleased with this initiative. Moreover, I am encouraged by the fact that it will be implemented in an economic environment for the New York region as a whole that seems to be experiencing at least a gradual comeback. The news on inflation provides still further hope that the New York area can gain competitive strengths. In the real estate markets, rental costs at commercial properties are now at competitive levels, vacancy rates are generally declining, and housing has become more affordable. In addition, tourism is way up, generating revenues for hotels, restaurants and the area's entertainment attractions.

These advances complement the region's already strong structural characteristics to make the long-term economic outlook positive. Our region has a highly educated work force in which 26 percent of the adult population hold college degrees, compared with 20 percent in the nation overall. The region also is the center of a rich array of research and development firms, communications and computer companies, and leading universities and cultural institutions.

Yet any truly comprehensive prospective view of the region's economy must recognize the seriousness of the risks faced by the City and its suburbs as the region experiences fundamental industrial restructuring. As a native Chicagoan, I observed first hand the pain and uncertainty brought about by cyclical downturns and structural dislocations, particularly in the 1970s and 1980s. Well, look at that "rust belt" now! Entire cities have changed their character and the great core of manufacturing, now much smaller and more specialized, has gained unprecedented prosperity.

Instead of buckling under to global competition, the management of firms in the former "rust belt" made tough decisions, rethought their strategies, reshaped their companies and began to take advantage of the new markets opening around the world. Cities like Pittsburgh, Cleveland, Cincinnati, Columbus, and many others that had been written off by many observers as dinosaurs from a bygone age of manufacturing have been transformed by service industries into more diversified, less vulnerable centers of economic and financial activity -- and there's still some manufacturing being done there, too.

For the first time in the 20th century, the New York region's largely service-based economy has been experiencing sustained restructuring and downsizing in the very industries that formed the core of our industrial mix and held up so well during the period of restructuring elsewhere in the country. Spurred mainly by advances in information processing and telecommunications, the region's largest employers have been able to produce more output with a smaller workforce, as high value-added workers -- in the most productive facilities -- have displaced many thousands of their colleagues.

Such actions are not just a cyclical response by businesses and governments to a sluggish economic recovery. Instead, they represent reasoned approaches toward making the best use of available technologies, adapting to changing domestic and international competitive conditions, and responding to the tougher demands of shareholders or the public. Consolidation among banks, the closing of hospitals, shrinkage in the business service fields, and layoffs by the state and local governments are making the New York regional economy a different entity than it was even a decade ago. Eventually, most other cities will face some sort of restructuring and dislocation of workers along these lines. For now, however, it is incumbent upon the leadership in this region -- in both the public and private sectors -- to recognize the situation, measure the risks, and take the steps that will enable all sectors and groups to prosper in the decades ahead. The former "rust belt" did that, and now we must, too.

One risk too frequently given only glancing attention by leaders in the region is the threat to the social fabric caused by disparities in the distribution of wealth and income. Over the last twenty years or so, growth and prosperity have not been shared widely enough, and the less educated and poorer segments of society have lost ground. One cannot be sanguine about this widening gap. Over the long term, I am convinced, strong economic growth can be sustained only if the benefits of the economic pie -- more and better jobs, higher incomes, improved housing and a higher standard of living -- are shared by all parts of society, rich and poor, skilled and less skilled. This is true everywhere in the world. Our region is no exception.

What could we in this room do to help narrow the disparity in income and wealth without sacrificing the well-being of the institutions we represent? Admittedly, this is an enormous and complicated challenge.

I believe that the business community and civic leaders in particular can most directly promote economic well-being by taking active, participatory roles in the education and training of our region's youths and workers. It would be easy to stand before you and preach the gospel of education, and tell you what you already know -- that such a pursuit is important and right. Who could ever disagree? Instead, my message today is that our focused attention on education and training is urgently needed and indispensable now. By not taking an active role in the development of this region's human capital, we risk facing a serious, and permanent, mismatch between the skills we need to run our businesses and those possessed by the pool of available workers. Our school systems are doing what they can and should have our total support, but they can no longer do enough by themselves.

While the need to match the skills of workers to the list of available jobs may sound like an evergreen issue, it has new dimensions in the 1990s that, in my opinion, expand our current challenge to unprecedented proportions. The same forces that continue to reshape the region's economy -- industrial restructuring, global competition, and rapid, persistent technological change -- are the ones that have put enormous strains on much of our work force and the educational establishments. Students nowadays require an array of skills far beyond the three R's that shaped most of us here today. Telecommunications, computers, the information superhighway, and even television have made obsolete the standard curricula that guided education for decades, and they have changed the mix of knowledge, skills, and experiences students and workers must develop in order to function well today.

In addition, the service-based economy, which, like its manufacturing counterpart has grown very capital intensive, also requires keyboard, reasoning, customer service, and communication skills more complex and advanced than those of previous generations. These challenges arose with great suddenness, at a time when school budgets have been stretched as never before. Our failure to help schools now will mean that our businesses won't be able to hire the kinds of workers they need to benefit fully from the business opportunities opening up to us. It also will mean that income and wealth disparities among groups will widen still further and the social fabric of the region and, indeed, the nation will become badly frayed.

Every one of our organizations can and must do more to bolster the readiness for work of all who are entering, and others who have been, in the region's labor force. The investment will be meaningful, and it doesn't have to be very expensive. Whether we run large enterprises with thousands of employees, or small establishments with but a few, we have to use our doors as entrances to the world of work rather than barriers. Educators tell us that individuals learn best by doing, by participating actively in tasks, and by experiencing those tasks in new environments. We can do something about that.

Many of us can do something about it by increasing the number and variety of internships we offer, and by expanding the work-study and school-to-career programs we offer so that learning comes from doing, and not just by sitting in classrooms. In fact, our own State has begun to change its venerable Regents examinations away from pen and paper marathons to ones in which the student's grade is based on the ability to do something. This so-called "performance-based assessment" recognizes that the end result of training must be the ability to perform; this realization, however, puts an enormous burden on school administrators, teachers and students alike to gain practical experiences. Those of us in the business community can provide exactly what they need.

At the New York Fed, we have committed substantial effort to the development and implementation of a wide range of participatory instructional programs geared mainly toward easing students' transition from school to career and toward developing a better understanding of business, economics and finance. In addition, we have a strong commitment to the training of educators throughout the Second Federal Reserve

District in a variety of subject areas in which we have expertise. In 1995 alone, the Bank hosted meetings and seminars for teachers of economics, finance, law, social studies, political science, consumer economics, government, and education; we also hosted conferences for administrators, department chairpersons, principals and assistant principals, while working to help shape the New York State secondary schools social studies curriculum. For the educators, the collaboration has provided much needed additional resources, ideas, and training; for the Bank, the time and resources devoted to these efforts helps us to fulfill our community responsibility while raising the readiness for work of thousands of students in the region from whom we, and perhaps you, will draw to meet future human resource needs.

Let me give you an idea of some of the more successful of my Bank's programs: (1) "The Econ Explorers Club" is aimed at elementary and middle school students, ages 9-13. Students receive assignments that require them to gather information, collect and chart data, interview workers in various occupations, and write letters. By filling out a bank account application, for example, they find out what the savings process is all about. Hundreds of students a year participate and the program costs the New York Fed less than $1,000 a year. (2) "In the Shoes of a Fed Policy-maker" is intended to teach high school teachers. The program brings a couple of dozen teachers to the Bank for four days in the summer, which allows them to gain a better understanding of how policy is made and implemented. This hands-on experience is intended to enable the educators to teach other teachers and their students about the monetary policy process much more accurately. Cost to the Bank: a few dollars and a bit of the time of some of our staff. (3) Our most widely joined program, "The Fed Challenge," is a competition among high school students that has earned national recognition, though it's only in its second year. Teams of students from participating schools present an analysis of current economic conditions, a forecast, and a monetary policy prescription before a panel of judges consisting of senior-level New York Fed staff. This year, 40 high schools from the metropolitan area took part and almost 100 schools participated nationwide. Next year we'll have many more.

In addition to "The Fed Challenge" and our other innovative programs, the New York Fed engages in a range of more traditional collaborations with schools, including a Join-a-School partnership, summer internships, a mentoring program and several career days. We also provide intellectual support to Classroom, Inc., a non-profit organization that has created outstanding computer-based simulations of enterprises in various industries.

All of these collaborations have the benefit of improving the preparation of teachers and the performance of students. They also involve staff of the Federal Reserve at all levels, encouraging volunteerism and civic pride, while providing concrete opportunities to participate actively in the achievement of a major objective of our institution. While the specifics of the New York Fed's programs focus on what we do, there is no doubt that everyone in this room has the potential to engage in similar projects in your areas of specialization. It's good business to do so, and it responds to a major civic imperative.

For most of the public, the reputation of the Federal Reserve will continue to be measured mainly by our success in promoting economic growth with price stability, rather than by our interactions with educators and students. Over the months and years ahead, I will continue to advocate a monetary policy that promotes price stability, without which long-term economic growth will not be possible. Such a policy stance would be favorable, not just for the nation but for our region as well. The New York City area, with its many interest rate-sensitive industries, has prospered when decision-makers in the public and private sectors could have confidence that the Federal Reserve was committed to a rigorous set of policies that promoted price stability, in a growth-oriented economic environment. Price stability also promotes innovation and confidence, both of which lead to jobs, and it paves the way for the entrepreneurship that gives hope for the future to the people who live here.

Our monetary policy roles notwithstanding, the New York Fed also must respond to the social needs of our community. In that context, my Bank will continue to work both independently and with community leaders to help make the Second Federal Reserve District a better place to live and work. We firmly believe that our efforts to improve educational opportunities contribute to that mission, though we remain very aware of the challenges that lie ahead to narrow the gap in income and wealth among groups.

I encourage you to join with me and many others in committing our organizations and ourselves more fully to the task of meeting this challenge head on.

Thank you very much.