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Statement of
Alan Greenspan
before the
Committee on Banking, Housing, and Urban Affairs
United States Senate
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I want to begin my remarks today by expressing my gratitude to President Clinton for his confidence in me, and to you, Mr. Chairman and members of the Committee, for holding hearings on my renomination for a fourth term as Chairman of the Board of Governors of the Federal Reserve System. The Federal Reserve has had a close and productive relationship with this Committee over the years. If you and your Senate colleagues afford me the opportunity, I look forward to working with you in the years ahead to build a framework to enable the American people to enjoy the fruits of a sound and efficient financial system, in an economy that is delivering the greatest possible sustained increases in standards of living.

We at the Federal Reserve face considerable challenges in carrying out our responsibilities for both the financial system and the overall economy. In many respects, these challenges relate to discerning, and keeping up with the implications of, the accelerating pace of technological change in our society. The Congress took a major step last year in passing legislation that will help the citizens of the United States realize the benefits of the rapid evolution of technology in the delivery of financial services.

The Federal Reserve's challenge now, working with our fellow regulators, is not only to implement the new law, but more broadly to design supervisory and regulatory policies that can deal effectively with the changing financial structure. Effective oversight must balance a number of possibly conflicting criteria. It must enable our financial sector to evolve in a way that allows competition and technological change so that financial services are delivered in the least costly, most efficient way possible to the highest possible number of our citizens. It must at the same time foster the fundamental soundness of our financial system and put in place safeguards to protect against the remote possibility that unsound behavior in the financial sector is transmitted

beyond the firms involved to the economy more generally. And, it must accomplish the latter with minimal use of the government safety net and of implicit or explicit guarantees that tend to reduce accountability and market discipline and foster excessive and destabilizing risk-taking.

For the economy overall, the marked pickup in technological innovation has accelerated productivity and raised standards of living for many--though regrettably, not all--Americans. Our challenge in monetary policy is to foster, as best we can, the financial conditions that will allow this economic expansion and technological revolution to continue as long, and as vigorously, as possible. Experience has demonstrated that an essential ingredient in this prosperity, and an ingredient for which the central bank has ultimate responsibility over the long run, is low and stable inflation. Effective price stability removes a major source of uncertainty and distortion that would otherwise interfere with the spending and saving decisions of households and businesses. Maintaining price stability also reduces the likelihood that imbalances could develop that would ultimately undermine economic expansion.

We have also learned that the Federal Reserve's potential contributions to financial and economic stability should not end with making policy decisions. We also need to explain to the public what we are doing and why. Importantly, in our democratic system our explanations provide the members of this Committee, your Congressional colleagues, and the people you serve with the information necessary to evaluate our actions and to hold us accountable for them. As you know, we have made considerable efforts in recent years to improve the communication of our decisions, our expectations, and their rationales to the public consistent with our mandate to deliver effective monetary policy. This has not always been a straightforward process, in which the consequences of each step could be readily predicted, but it is one that must continue.

Thus the challenges and the opportunities are substantial in a number of the areas in which Congress has given the Federal Reserve important responsibilities. But in the Federal Reserve, the Congress also has created an institutional structure extraordinarily well-suited to address these issues. The combination of a Board of Governors, firmly tied to the national democratic process and providing overall leadership to the System, and regional Reserve Banks, deeply rooted in their local communities, enables us to bring a unique perspective to the consideration of policy issues.

Our Reserve Banks supply real-time information about developments in their regions, and ongoing observation of, and familiarity with, the financial institutions headquartered there. This information enhances our ability not only to conduct monetary policy, but also to supervise financial institutions and deal with emerging problems in the financial sector, and to play a constructive role in regional economic developments. Board members and Reserve Bank presidents can employ these observations, along with their knowledge of the national and international economic and financial situations, to carry out our legislated mandates.

This structure and these responsibilities have attracted to the Federal Reserve System men and women of high intellectual capabilities and deep knowledge of the relevant subjects. Naturally, and fortunately, these people often disagree. Disagreements, however, are largely over evidence and analysis, not goals and objectives. To be sure, Federal Reserve decisions often emerge as a broad consensus of policymakers. But forming that consensus involves considerable give and take, with many people influencing the outcome.

Policymakers are in turn supported by outstanding staff at the Board and the Reserve Banks. Many, perhaps most, of the policymakers and staff could be making substantially more

income in the private sector, but, attracted by the character of their colleagues, the nature and importance of issues they deal with, and the atmosphere in which those issues are addressed, they chose to exercise their considerable talents within the Federal Reserve.

The strength of the institutions and structures of the Federal Reserve is perhaps most visible in the work of the Federal Open Market Committee. There, the ability of Reserve Bank presidents to draw on local contacts can reveal significant developments in the economy before they are visible in the national data, and can help in understanding the forces behind important economic trends. The Committee is an extraordinary collection of individuals. Among the 17 people gathered around that table, 13 have Ph.D.s. The others have the experience, skills, and common sense to prevent the Committee from becoming paralyzed with a surfeit of two-handed economists.

But monetary policy is not the only area in which this unique blend of skills and perspectives is brought to bear. We utilize committees of Board members and Reserve Bank presidents to deal with such responsibilities as our oversight of the payments system and the implications for supervision and regulation of the growing size and complexity of financial institutions.

What success the Federal Reserve has had in carrying out its legislated responsibilities in recent decades derives from many sources. Certainly, we have enjoyed good fortune--dealing with the challenges of a pickup in innovation and productivity is decidedly more enjoyable than the task faced by our predecessors in the 1970s when productivity slowed and stagflation held sway. I believe we have also learned from our past mistakes, and I hope that we will recognize the new misjudgments we will inevitably make quickly enough to prevent them from becoming

too serious and disruptive. And we have had help and support from various Congresses and administrations seeking, like us, to promote sound public policies. But our ability to meet the legislative mandates of the Congress rests ultimately on the strength of the institutions of the Federal Reserve and the people who inhabit them.

It has been an extraordinary privilege to be able to serve my country at the Federal Reserve, and I would be honored if the Senate saw fit to enable me to continue this association for another four years.