The Economic Club of New York

103rd Year

407th Meeting

Thursday, January 14, 2010

The Grand Hyatt

New York City

Program

GUEST OF HONOR

THE HONORABLE PAUL A. VOLCKER

Chairman, The President's Economic Recovery Advisory Board

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Introductions

GLENN HUBBARD: …the 407th meeting of the Economic Club of New York, in our 103rd year. I'm Glenn Hubbard, Chairman of the club. The Economic Club of New York is the nation's leading non-partisan forum for talks on the economy and business and finance and more than a thousand distinguished speakers have appeared before the club over many, many years. We have established a strong record of excellence in speaking, as you will, of course, hear today.

Before we begin, I did also want to recognize collectively the members of our Centennial Society. During the centennial year of the club, several dedicated club members made a personal contribution to insure the financial stability of the club in its second century. One hundred and thirty club members are Centennial Society members, and their names are in your program. We are, of course, honored today to hear from Paul Volcker, who is the Chairman of the President's Economic Recovery Advisory Board, and, of course, well known to all of us as former Chairman of the Federal Reserve System. He was appointed to his present position by President Obama and was appointed Chairman of the Federal Reserve by President Carter in 1979 and reappointed by President Reagan in 1983 and served as Fed Chairman until 1987. Paul Volcker worked in the Federal Government for 30 years under five presidents of the United States in a number of capacities. Before becoming Chairman of the Fed, he was President of the Federal Reserve Bank here in New York. After leaving government, Paul became Chairman of the Wall Street firm, James D. Wolfensohn, Inc. and remained there until its merger with Bankers Trust. More recently, he served as Chairman of the Board of Trustees of the International Accounting Standards Committee and chaired a very famous investigation of the U.N.'s Oil for Food Program.

Chairman Volcker last spoke to us two years on our occasional to honor him on his 80th birthday. His remarks that day were so provocative that then New York Fed President Tim Geithner asked if he could respond in a follow on address which favor we granted. Well, we look forward to the Chairman's perspective today. I can think of no one better positioned to speak of busts, bankers and bumbling hearings than the Chairman. After his remarks, we will have two distinguished club members ask questions. Mr. Chairman, Paul, welcome home to New York. The floor is yours.

PAUL A. VOLCKER: Well, thank you, Glenn and members of the Economic Club and guests. It was indeed 20 months ago that I last addressed the Economic Club of New York. The sudden demise of Bear Stearns that happened only a few days before. So that event and market turbulence that accompanied it had already justified, what I then labeled, the mother of all crises. Now the events of the fall of 2008 drove the point home. For a few weeks, the whole financial world seemed to be tottering on the edge of a nervous breakdown. Only aggressive intervention by the Treasury and the Federal Reserve in this country and similar initiatives in the UK and other parts of Europe restored even a precarious sense of stability. Those actions by the national authorities went far beyond the established role of central banks as lenders of last resort. Several trillion dollars in large budgetary funds were spent in the United States to support markets and financial institutions – bank and non-bank. In effect, institutions and markets that had been proud and profitable exemplars of modern finance became wards of the state. De facto if not de jure. In some, the world of finance was turned upside down.

But now there are signs of a return to more normal conditions. The economy seems to be growing, if slowly. Large banks emerging from government support and benefiting from the flood of liquidity are reporting large operating profits. Real progress is being made in restoring capital ratios even as loan losses continue. Risk premia seem more normal. Funds are flowing if not yet in all markets that needed volume.

Now under the circumstances, some market participants just possibly including some in this room, seem to be suggesting that the events of the past couple of years are like a bad dream. A truly unsettling bad dream, but nonetheless something that in the cold light of day need not require a really substantial change in the structure of markets or in corporate lifestyles. Better board oversight, the tightening of institutional risk management practices, more adequate capital and equity standards, better informed and able regulators, a review of credit rating practices, certainly more sensible than uniform accounting standards, the sort of things I characterize as reform lite should be adequate to do the job.

But surely the need is more fundamental. This latest crisis has been cited as a once in a century phenomenon, but do not forget it is only the latest in a string of crises over the past 30 years that seem to be growing in both frequency and intensity. Even more significant today, the forceful official responses were necessarily undertaken in the white heat of crisis without the luxury of time or the benefit of established emergency procedures and financial resources. So we're left with a residue. A residue of really fundamental questions about the appropriate role of government in rescuing failing institutions and markets. The old questions colloquially described as too big to fail loom larger than ever on the agenda.

I don't think in the light of all that's happened we can escape dealing more clearly with the question of moral hazard. That's the elephant in the room. Or perhaps I should say in the halls of Congress. It's not going to go away unless we can develop a reasonable, well understood approach that all those other reforms, all those potential useful efforts to improve financial housekeeping won't provide the reassurance and the safeguards that we need. My sense is that the administration, the Congress and other national authorities have a common interest in achieving an intellectually satisfying workable consensus. But given the inherent complexity and the different national and private interests at stake as well as competing Congressional priorities, the fact is the process has taken time. That may be understandable, but it's important that we get it done. And get it done right. All the interest, refusing to recognize the need for real change must not hold sway.

I have not been restraining myself in recent weeks and months in setting out my own view of what I perceive to be one key element in strengthening the financial structure. My starting point is that for all the innervations in the market, commercial banking organizations are still the indispensable backbone of the financial system and surely that was demonstrated in the crisis. Today they comprise almost all the institutions of truly systemic importance. In recognition of that fact, I do not think the United States or other countries should or will eliminate the basic safety net for commercial banks. Deposit insurance, access to the lender of last resort all balanced by appropriate regulation and close supervision. But I also believe we ought to recognize in some areas of finance, as well as ownership ties with commercial firms, are inappropriate for banking. I have cited in particular hedge funds, private equity funds and proprietary trading in that respect. The point is those activities present added risk and I think as

we've seen recently, virtually unmanageable conflicts of interest with more essential customer relationships. Those market oriented activities are appropriate for our broader capital markets, but they should not implicitly or explicitly be provided safety net support.

I also believe that very few of the capital market institutions engaged in those activities are systemically important. Instead of bringing those activities within the safety net, a special new resolution authority should be created, a point the administration has itself consistently advocated. That authority should be empowered to take control of financial institutions that are approaching failure arranging as appropriate either an orderly liquidation or merger. In no case, should that amount to a rescue in the sense of protecting either management or stockholders. Creditors would be at risk as well if assets, in fact, ultimately prove to fall short of liabilities. I would take a medical analogy of what we're talking about. We're talking about DNA. Do not resuscitate. Not life support.

This afternoon I rather want to spend my time in a closely related area of reform that is of critical importance that surprisingly to me has become highly controversial. What has been particularly disturbing is the position of some that the Federal Reserve should be largely or even completely shorn of its regulatory and supervisory responsibilities. You won't be at all surprised to say that I reject that view. What seems to me beyond dispute, given recent events, is that monetary policy and the structure and condition of the banking and financial system are irretrievably intertwined. Those reciprocal influences and the interdependence make a compelling case that central banks should have a strong voice and authority in regulatory and supervisory matters.

Now I don't want to deny that there are other legitimate public interests and regulatory policies, not least of the finance industry. Ways and means can be found to bring a variety of points of view to bear, but I would insist that neither monetary policy nor the financial system will be well served if a central bank loses interest in or influence over the structure and performance of the financial system. Now the clear challenge for central banks and their colleagues and the regulatory process over the next few years will have to reinforce confidence in the banking system while weaning in a way from excessive reliance and official support.

Now I have to tell you I just read two paragraphs that were the easiest for me to put on paper. In fact, they were lifted word for word from a lecture I gave 20 years ago. What I do want this morning or this afternoon is to place those old words in today's context.

Only ten days or so ago, Chairman Bernanke made the relevant point. If we're concerned about identifying and dealing with financial bubbles – and I think we should be – we need both the ability to identify the danger points and have the instruments to deal with them. We might debate the extent to which the blunt instrument of monetary policy kind of should be brought to bear. But to be timely, to be effective, to act with anything approaching surgical skill, supervisory and regulatory tools are relevant. And as appropriate, those tools would need to be coordinated with decisions with respect to monetary policy. Now the practical fact is that the Federal Reserve, in executing all the market operations and acting as treasury agent, is in the financial markets day by day. It is inescapably dependent upon – whatever the next page says – it's inescapable dependent upon the efficient functioning of those markets. In acting as lender of last resort, it must know its counterparties and know them well. At times of crisis, those

relationships will be intensified. We've just been witness to extreme examples of that. A related point is that the Federal Reserve both oversees and participates in the basic payment system. Large value payments, domestic and international routinely pass through its books. Now what other official institution has the knowledge, the expertise, the experience to identify and evaluate market conditions, to judge the risks, protect its own position and to act on short notice overnight if necessary.

Now the basic structure of the Federal Reserve System is also relevant. I know from my experience, it's an elaborate, in some ways, cumbersome organization. It was deliberately designed so. It is designed to protect its independence with incumbent and to assure an element of regional participation and to maintain contact with financial, commercial and agricultural interests. The fact that that has remained pretty much intact for close to a century itself suggests the genius of the founders.

Now the truth these days bestselling books remind us that challenges to that structure and particularly to the Feds insulation from political oppression arise from time to time. The intense anger about the amounts of funds required to bail out institutions and market is palpable. But that truly exceptional response to financial crisis drawing on long dormant emergency powers of the Fed was, after all, a properly coordinated decision with the administration, not a misuse of independent authority. A more limited critique is that authorities responsible for maintaining the safety and soundness of particular banks and financial institutions should not be distracted – if that's the right word – by potentially competing objectives of monetary policy.

Well, conversely you hear the Federal Reserve preoccupied with monetary policy will consciously or unconsciously not give enough attention to supervisory responsibilities. I believe neither point can be maintained. There simply are times when supervisory or monetary policies must work in harmony. It simply doesn't make sense as then Fed Chairman Marriner Eccles long ago complained that the efforts of the Federal Reserve to ease money be, to some degree, frustrated by overzealous banking regulators determined to restore bank capital and assure strong lending standards. Nor would it help on the other hand if banking regulators are reluctant to tighten capital or other supervisory standards of particular institutions at the time of incipient excesses in banking and financial markets more generally.

None of this, to my mind, is an argument for exclusive regulatory and supervisory authority to rely on the Federal Reserve. To contrary, there's merit and some division of responsibilities. The FDIC, for instance, brings to the table a…examiner staff with an immense amount of experience in dealing with troubled banks. Clearly, we do not want competition and laxity among a number of regulators aligned with particular constituencies, but equally there is a danger that a single regulator may be excessively rigid and insensitive.

So there's more than one suitable model for the United States or for other countries. I do insist, however, that whatever the particular model that emerges from the present revision, the central bank should maintain a robust presence with real authority and regulatory and supervisory matters – a point of view strongly supported by the present administration. Recall what the original Federal Reserve Act almost 100 years ago – I was reminded walking in here today that the Federal Reserve is almost as old as the Economic Club of New York, but not quite. But we

both have a function to perform. The original Federal Reserve Act almost 100 years ago set out in its own preamble as one of its main purposes a more effective supervision of banking. In those days, of course, commercial banks, for all practical purpose, were the financial system.

As soon as bank holding companies became significant, Federal Reserve responsibility was extended to bank affiliates. In practice, those responsibilities have been shared with the controller of the currency, the FDIC, state agencies, the SEC and more specialized organizations. But plainly some consolidation is called for. In considering that needed reorganization, I would remind you that it is the Federal Reserve to which the Congress, excessive administrations, the general public, and not least, foreign institutions themselves have looked to in times of trouble.

As my predecessors and successors have been well aware, when a crisis breaks, it is their telephone that rings. And the ensuing conversations typically have a great sense of urgency. That's been true whether the emergency was the collapse of the silver market or the Latin America Debt Crisis. Early in the 1980s, major bank and thrift institutions failures. Later in that decade the Asian crisis and an overleveraged hedge fund in the 1990s. More recently troubled investment banks and a foundering mortgage market. Now that's not a matter of narrowly defined responsibilities closely dictated by law. Rather it reflects a certain confidence in the central bank as both independent and professionally qualified. It implicitly recognizes the reciprocal influences and interdependencies among institutions and between monetary policy and regulatory concerns that I emphasized earlier. And of course – I don't need to convince this audience – that there's a further and very tangible consideration. It is the central bank that, in the end, has the financial resources immediately available. If more money is needed, well that can

be created. What the current crisis has brought to our attention is concerns about financial stability cannot be confined to a crisis in being. The administration's proposal for regulatory reform, the recent remarks by Chairman Bernanke and the many foreign authorities, the G30 report a year ago and many other private analysts are called for arrangements to provide broad oversight of financial markets and institutions. What I term a systemic overseer.

The point is there's a function of distinction between broad oversight of the system in enforcing regulatory and supervisory authority over particular institutions. It's a concern about the interdependence of those institutions, about trends and leverage and risk management generally. It's about the framework of markets and the significance of new institutions and new innovations for containing, or dare I say, perhaps amplifying risks. The administration appropriately and strongly has set forth that rationale. While affording a strong regulatory role for the Fed, it contemplates that the further oversight role be centered in the Treasury, chairing and staffing a rather large council of regulators.

The alternative, as I see it, is to lodge that responsibility more explicitly in the Federal Reserve. That approach would be consistent with the broad responsibilities of the central bank. Operationally it would build upon its experience, its existing professional staff, its strong regional presence and its tradition of broad consultation with banks and other financial institutions with the business community and the public at large. Whatever the particulars, the close relationship among regulatory authorities encouraged by an advisory council or otherwise would be essential and the new overseer will clearly need adequate authority to collect

information. Consideration needs to be given what elements of regulatory authority beyond the implicitly powerful tool of moral suasion would be needed.

Now let me say the present crisis has clearly exposed weaknesses in existing approaches of all the regulatory agencies and I am acutely aware that that is particularly true of the Federal Reserve itself, which, as I see it, carries the broadest responsibility and has access to the greatest resources. Now the appropriate response for all the reasons I have set out must not be the denude Federal Reserve of supervisory and regulatory responsibilities. Rather there must be legislation and reforms to clarify those responsibilities. We need assurance that the regulatory responsibilities will be consistently respected at the top of the institution by the Board of Governors and by the managements of the regional banks.

Designation of the Federal Reserve is the systemic overseer would itself carry a strong message as to its responsibilities. Within the organization, I do believe there's a clear need for a stronger administrative focus. In that respect, I can only repeat and reinforce the suggestion I made when speaking here more than a year ago that one Board Member be designated as Vice Chairman for Supervision with direct responsibility for managing the effort of the entire Fed system. The position would be subject to Senate confirmation with the requirement for reporting at intervals to the relevant Congressional Committees on the state of the financial system. Consistent with the new framework emphasis on the oversight and supervisory responsibilities of the Federal Reserve Bank President should be emphasized.

Now looking to the composition of the Reserve Board and the Open Market Committee, I do not believe that those bodies should be viewed as the kind of academic conclave to which professional economists have a special entry ticket. Economic training can indeed provide a strong analytic focus and important sense of discipline for central banking. But a profession that has become more and more abstract, obtuse and mathematical also has real limitations in providing insight into human and institutional behavior. The Board and Reserve Banks will always benefit from some officials drawing from business, large and small, from finance generally or banking in particular even from those with experience in public life. Surely the regulatory and supervisory staff must attract some of the nation's best talent certainly professional economics, but also financial engineers, auditors and risk management experts be ready and eager to accept the challenge of participating in public service.

I want to conclude by placing the role of the Federal Reserve in a broader setting. The United States is still the world's largest economy. It's been the exemplar of the benefits of a market system. One hallmark of leadership has been innovative financial markets. The United States is, itself, the home of large active financial institutions internationally. Our influence has been pervasive right around the world. Now it's clear that leadership can no longer be taken for granted as a kind of birthright carried over from the 20th century. In relevant terms, neither are our economy nor our financial system has unquestioned dominance. We are plainly overextended in budgetary terms and in our dependence on foreign capital. We resort these days to the kindness of strangers to meet our deficits. The Great Recession and the collapse of some of our largest and proudest financial institutions carry an ominous message of vulnerability.

Now I am confident we can make our way back to a healthy economy and to a strong and stable financial system, a system privately owned and operated, but it's also evident that the simple and essential element of trust is in short supply whether in our country or abroad. We must not shrink away from change, but accept the need for basic financial reform and in undertaking that job, let us also recognize that this is no time to weaken the role of the one economic institution – our central bank – that has long commanded a sense of respect and confidence not only among Americans, but right around the world. Political leaders and market participants alike have looked to the Federal Reserve as a guardian of stability of the financial system in general and the dollar in particular. I do, too. We simply can't afford inadvertently to undermine that sense of trust. If you agree, I urge you to make your voices heard. Thank you very much for your patience this morning. Thank you.

GLENN HUBBARD: Thank you very much, Chairman Volcker. Our two questioners are Alan Blinder. He is a Professor of Economics at Princeton and former Fed Vice Chair and Paul Gigot, who is the editorial page editor of The Wall Street Journal. Alan, the first question goes to you.

ALAN BLINDER: Paul, I agree very much, as you probably know, with the central contention of your speech which is that to play a proper role in guiding the financial markets and avoiding system risks, the Fed has to keep a strong hand in bank supervision. One objection that's been raised to that is that making the Fed the overseer of systemically important financial institutions and markets could and likely would, in the critics' view, draw it into some politically charged decisions such as life and death decisions over individual companies and if that's the

case, that could, by inference, endanger the Feds political independence. What's your response to that criticism?

PAUL A. VOLCKER: Well, you're setting forth one possible approach which is giving the Fed direct responsibility for large presumably systematically sensitive institutions which is what the administration has proposed and I'm not objecting to that. I'm just saying that's not the only way to do it there's pluses and minuses. But so far as involving the Federal Reserve in politically charged areas, let me make a point I didn't make in the speech based upon my own experience. Banking regulations and supervision can be politically charged. There is no doubt about it. You're affecting particular institutions. Those institutions have a voice. They have money. They have lobbyists. They affect Congressmen and so forth and so on.

Now the practical problem, as I see it, is how you get a regulatory and supervisory system that is resistant to that political involvement or pressure that is inevitable? And it does seem to me, and based upon maybe my biased experience, that the Federal Reserve, by its character, by its tradition is more insulated from that pressure than other regulatory institutions. The very life depends upon the regulation of the particular industry. That is not true with the Federal Reserve. So I think that that helps to put the Federal Reserve in a somewhat different and more favorable context in terms of dealing, which inevitably are going to be political pressures.

On the other hand, I do not suggest, and I don't think it would be wise for the Federal Reserve to take over the whole thing, lock, stock and barrel. We need some degree of healthy competition in the area of regulation, but I do think they are better placed for maintaining an even keel – if

that's the right expression – relative to other agencies. I don't think I ever experienced in the time I was Chairman a Congressman coming and complaining about our approach about a particular institution in making a broad regulatory change. Sure, there's comment. But you know I almost had the feeling they knew that was kind of improper – entering the great temple and complaining about treatment of an individual institution. I think that's the way it should be.

PAUL GIGOT: Mr. Chairman, I have a related question about the independence of the Fed and its powers. As you know, the Federal Reserve is ultimately a creature of Congress and Congress's main duty is to deciding how taxpayer money should be spent, the power of the purse, and fiscal policy. You make a very compelling case for Congress to stay out of monetary policy, but when the Fed becomes deeply involving in fiscal policy through committing hundreds of billions of dollars of taxpayer dollars, my question is can the Fed not expect to be more strictly supervised and audited by Congress? And to put it another way, has the Fed, itself, put its own independence at risk by its forays into fiscal policy the last 18 months and were those interventions a mistake?

PAUL A. VOLCKER: Well, this question of what the Federal Reserve should say about fiscal policy, I find more difficult than the previous question about the pressures they're exposed to and the regulatory sites. In one sense, the fiscal decision, budgeting decisions are the essence of political decision making and the Federal Reserve should and must live with whatever the results of that process are, but when there is a sense that budgetary problems – without getting into particular details about particular programs or taxes – are some indication as to whether that helps or hurts in terms of the Federal Reserve Stabilization Policies, I think you cannot avoid,

under certain circumstances, taking a position on them. And it's very tricky. I remember, frankly, when I became Chairman of the Federal Reserve, a year or two later President Reagan was elected and he had a brand new fiscal program of the sort that you're familiar with which involved big tax cuts and potentially bigger deficits which at first blush anyway didn't seem to make the job of restraint any easier, what do you say? I resorted to saying what I thought was unexceptional. If you're going to have that big tax cut, you better cut expenditures, too. I think that was unsuccessful in that bit of advice, but it's a difficult area.

ALAN BLINDER: If the Fed were to be put in charge of overseeing systemic risk as you proposed, and, as I said before and I agree with, that would certainly add to both its responsibilities and its powers over the financial system and by indirection over the economy. Another criticism that's raised by some is that the Fed's already too powerful with section 13.3 and in a variety of other ways. So do you think that in return for this extension of power, the Fed should give up any of its current powers and responsibilities? And if so, which ones?

PAUL A. VOLCKER: Well, there's a big controversy, as you know, which I didn't touch upon at all as to the Federal Reserve responsibility and others responsibilities in the consumer, protection area which is a very important and sensitive area politically. My sense historically, and I think I'm correct, is that Congress gave the authority that it had over consumer and investor protection because it trusted the Federal Reserve more than it trusted the other agencies. I think it was as blunt as that in the then Senate Committee and Chairman Proxmire. And that's a nice, in a way, accolade for the Federal Reserve but you always wonder whether that is a controversial important area that really is not at the heart of financial stability and monetary policy.

So something's going to be taken away from the Federal Reserve and it looks like it's going to happen. I think that would be an area. I don't know in areas where, you know, its prime responsibility is – monetary policy and regulation – there's really any – there can be a different sharing of the regulatory responsibility, and I didn't lay out anything here that says just how that should be done. It should be reviewed. I think that's fair. Should the Federal Reserve just be big banks? Should it be – retain some contact with small banks? Should it do the holding company and somebody else does the bank? It's all fair game, but I – I think at the end of the day, the Federal Reserve has to be left with robust responsibilities in its main line of activities.

PAUL GIGOT: As we've all heard this morning, the administration is proposing a new tax on financial institutions. Do you think that such a tax is an appropriate way to address excessive risk taking – financial risking taking – and will such a new tax on financial intermediation help to increase bank lending?

PAUL A. VOLCKER: Well, you know, help increase what?

GLENN HUBBARD: Bank lending.

PAUL A. VOLCKER: Bank lending.

PAUL GIGOT: Will such a tax help to increase –

PAUL A. VOLCKER: Yes, yes, I understand. You know, if I knew of a tax that would effectively and equitably cut down on risk and promote bank lending, I would have proposed it this afternoon. I don't know of any such approach. I know the – this country, other countries, are facing a very real and kind of legitimate political problem as to how they deal with the losses involved and the rescue programs that took place. And I know the president's announcing some measures this afternoon or maybe he already announced them this morning, which seem to me are not – not on first glance anyway – not an unreasonable response given the fact that he's got to do something. The law says he has to do something. And has he carved out an approach that minimizes any damage of the sort that you're raising, but responds to very real public anger and the fact that we already have this enormous budget deficit, you've got to do something. And I think it's not unfair to say that these big institutions that have benefited one way or another have got to carry part of that burden and it's just a question how to do it.

ALAN BLINDER: Going back to the first part of your talk, you were expressing concern, as a number of people have, that the financial system looks to be slipping back into business as usual, coming out of a dream, as you put it – before we enact any real regulatory reform rather than after which is an important distinction. What do you think we can do about that and in the process, I think you should – you need to choose what we mean by we. There are a number of we's that could be implied by that. We, citizens. We, people in finance. We, people in government. Your choice. What could we do about it?

PAUL A. VOLCKER: Well, if you agree, make your voices heard somehow or another. You know, I got a whole bunch of people that support the position I'm taking and a lot of them

are rather more elderly than the average. So we have to have some people, you know, actively in business to take the position, which I think many do. But, you know, there is heavy lobbying and there has been heavy lobbying on the other side. And that has to be overcome by a combination of, I guess, lobbying on the right side and maybe including some money in some cases. But I think it mainly is going to be a public argument. I suggested to the Senate Committee, why don't they reopen up the hearings on this point and we'll have an argument in public and clarify the issues. And I think I'd win that argument if that happens or I wouldn't have suggested it, but I – if I had all of you behind me, that game's over; I win.

I don't think it's – I forget – the kind of thing we're talking about are restrictions on what's called scope these days, literally in the banking world, affect as many institutions as I can count on my hand in a serious way. Now those five institutions probably account for half the financial assets in the country, but it's not a matter that affects very many institutions. Now it will affect a handful. It was interesting. I don't know where it came from. A few weeks ago there was a report I think in the Financial Times, the implication was the Treasury – I don't know if this is true – had I identified the systemically important institutions in the world and there were only 30 of which all but three were commercial banks. There were a couple insurance companies. They only had three non-bank, only one or two insurance companies – I don't know who. I don't what was the foundation of the report, but I presume somebody was playing around with this notion, and I don't think it's far wrong. When you think of non-banking institutions that are really systemically important, there are a couple very obvious ones. But once you get by the very obvious ones, there aren't many.

PAUL GIGOT: You've argued today for a robust Federal Reserve Authority and, fair enough, I remember 18 months ago you had mentioned, however, that you thought that the Fed was perhaps pushing some of the limits of its statutory authority and prudential regulation. As you look over everything that the Fed has done over the last 18 months, are there any specific actions that it's taken that give you particular pause? And I'd like to mention two in particular. One is the direct purchase of treasuries by the Fed and the Mortgage Backed Securities Program, which is about $1.25 trillion, it will go up to that, and does get the Fed involved in the allocation of capital.

PAUL A. VOLCKER: Well, it's interesting you take those two examples. I had a number of things that were done to make me squirm, but that doesn't mean they weren't important. I think they made Mr. Bernanke squirm and others squirm. The two you mentioned, buying treasury securities, Federal Reserve has always bought treasury securities. In fact, when I was a young guy, I'm so old that I remember all these things. When I was in the Federal Reserve Bank in New York and we thought we were responsible people, we argued very vigorously – or my superiors argued very vigorously – that the Federal Reserve ought to be buying long term treasure securities, if not all the time, whenever it seemed appropriate in terms of the monetary policy objectives. And the Board of Governors had taken the view – it was called Bills Only in those days, which became ingrained in behavior. But it's not establishing a new questionable legal authority to buy long term treasury nor Mortgage Backed Securities where this is a particular provision in the law that permits that.

Now earlier they were doing a lot of things for which there is no particular provision in the law, to put it kindly. And I didn't touch upon it in my remarks, but they – I hate the fact that they had to rely on this emergency authority because once you use it, everybody will assume you can use it again and we always try to avoid it. But that's been done, but properly – and I think this could be embedded in the law – it shouldn't be done without the approval of the administration. Now, in fact, it was done without the approval of the administration, but I think that ought to be a legal matter because it does wander rather directly into areas that should not ordinarily concern the central bank. And you might put other limitations on that authority. It seems to me the only justification of that it is they can act in a hurry and you can't go to Congress and get authority for money when the market is collapsing this week or tomorrow. So it provides a kind of bridging authority and that's the way it ought to be looked at.

GLENN HUBBARD: Thank you very much, Chairman Volcker, for those remarks and Allan and Paul for your comments. We do have a modest token of appreciation for you. I can assure you while it's given with great fondness by all of us, it's sufficiently low monetary value that the White House Gift Office will allow you to accept it. Please enjoy your lunch.

(END)