FEDERAL RESERVE BANK OF ST. LOUIS

FALL 2007

Central Banker

News and Views for Eighth District Bankers

Watch for Fed Communications on Check Consolidations

By now, you're undoubtedly aware of the pending System-wide changes in the Federal Reserve's check operations. The long-term strategy for restructuring check and check adjustment operations will reduce the number of check processing sites from 22 nationwide locations to four regional sites: Philadelphia, Cleveland, Atlanta and Dallas.

In the Eighth District, the Memphis and St. Louis offices will no longer provide the full range of check processing services once all transitions are completed. Memphis' volume will move to the Atlanta Fed in the third quarter of 2008. St. Louis' volume will move to Atlanta in the first quarter of 2011.

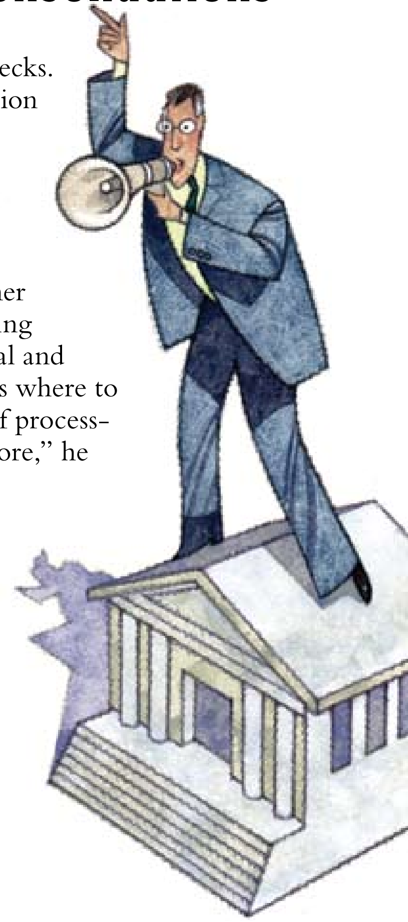
But what does this mean for you, the Eighth District banker?

"We are still a full-service shop until the consolidation," says Bill Little, assistant vice president of Check Processing Management in St. Louis. "We're still continuing to offer the transparent and full level of customer service that bankers expect."

The Eighth District will also continue to process U.S. Postal Service money orders and U.S. Treasury checks, including Philadelphia's volume starting in mid-2008, making St. Louis the only Fed that processes Treasury checks.

The most important action bankers can take, Little explains, is to watch for communications from the Fed about what will happen and when. "Be on the lookout for customer communications concerning impending changes at local and other Bank offices, such as where to send checks, availability of processing, transportation and more," he says. "Communications usually arrive well in advance—approximately 120 days out."

For more information, read the Fed's announcement at www.federalreserve.gov/boarddocs/press/other/2007/20070626/default.htm. ■



Go Direct Converts More Than 1 Million Accounts to Direct Deposit

The *Go Direct* campaign has converted more than 1 million federal benefit checks to direct deposit since the U.S. Treasury created the program in the fall of 2005. The millionth conversion came in June. More than 60,000 of these conversions came from the Eighth District alone.

Go Direct is designed to protect recipients of Social Security and other federal benefits from fraud and identity theft and give them greater control over their money by switching them from paper checks to direct deposit. The program relies heavily on partnerships with community organizations, including banks, credit unions and other financial institutions.

Memphis, which served as the sole Eighth District pilot location before the program went national, has several local organizations involved. Visit www.godirect.org to learn all about the program and www.godirect.org/partners/partners_localRegional.cfm to view a list of local and regional organizations. If you are interested in having your bank or institution become a partner, call *Go Direct* at 952-346-6055 or click the Partners link on the web site. ■

Feditorial

Innovation Conference Showcases Fed's Outreach Efforts

By David A. Sapenaro, first vice president of the Federal Reserve Bank of St. Louis

Some time ago, the Federal Reserve Bank of St. Louis began focusing on greatly enhancing our outreach efforts throughout the Eighth District. The goal was—and is—to be a vital resource in community development, economic and financial education, and more. Since then, our District-wide presence has flourished and continues to do so.

Our outreach is designed to help bankers, economists, educators, business owners and others through economic education and information sharing. It's also centered on conducting regional economic research that can be used by policymakers and decision-makers throughout the District. In other words, it's a mutually beneficial outreach, and, so far, it has worked rather well. In fact, strengthening ties throughout the District actually became part of our Bank's mission this year.

We want to make sure that we continue to offer some of the best and most useful opportunities available for information sharing, networking, education and growth. We continue to explore new topics and ideas that will be of interest to you, while continuing to offer the vehicles you've come to value. Our current programs include Economic Forums, the Business and Economic Research Group (BERG), the Center for Regional Economics—8th District (CRE8), various Community Affairs-sponsored workshops and seminars, and much more.

A great example happened earlier this year when we sponsored a gathering called "Exploring Innovation: A Conference on Community Development Finance." It proved to be a mega-hit. With the help of a couple of nationally renowned presenters, our Community Affairs department put together a conference that explored so many different ways of finding and organizing community development financing that most attendees left with a feeling of having really accomplished something. We were still getting praise months after the conference.

Going forward, we will seek to organize similar conferences and programs that bring value to bankers and our other constituents throughout the District. ■

To Our Readers: Summary of *Central Banker* Survey Results

Last year, we surveyed *Central Banker* readers to help determine what readers like and dislike about this publication. The results were flattering, and we thank all of you who answered the survey. Nearly seven percent of our readership responded to the survey.

Almost all who responded said that they read every issue of *Central Banker.* Mostly, they are happy with the publication and its content: The writing is clear, the variety is good and the story length is generally just right. The majority indicated that the articles most often read are the lead story, the Feditorial and the Page 3 feature.

Respondents also indicated that they are interested in hearing more about banking trends, industry changes, and rules, regulations and policies.

One surprise was the lukewarm response to our ideas to expand our online presence. Most indicated they did not read *Central Banker* online; only half said they would read *Central Banker* if it was converted to an entirely electronic publication.

All of the results told us that we should continue to deliver the same high-quality product.

If you have additional comments you'd like to share, please send them in care of Scott Kelly to the address on the back of this issue. Thank you for reading *Central Banker.* ■

Fed Encourages Bankers To Be Innovative in Community Development Financing

When you build a better mousetrap, you're not actually starting from the ground up. You're taking an existing product and making it better.

Likewise when you, as a banker, are looking at community development financing, there's no need to start from scratch. Take the innovative approach by taking advantage of what's already available—and make it better.

That's the continuing message of the St. Louis Fed's Community Affairs department, which sponsored the well-received "Exploring Innovation: A Conference on Community Development Finance," held in May in St. Louis. Community Affairs is using the lessons and resources from that conference to offer ongoing community financing innovation assistance throughout the Eighth District.

"The whole point of the conference was to help attendees realize that they don't have to be the genius who comes up with a new invention," says Matt Ashby, senior community affairs specialist. "Instead, we wanted them to see that innovation can involve bringing together people from different corners of the community."

To help attendees understand the concepts and come away with something useful, the conference was far more than a mere "sit-and-listen" event.

Innovative about Innovation

Glenda Wilson, Community Affairs assistant vice president, explains that other than a few keynote speakers who laid the groundwork for thinking innovatively about community development financing, most of the sessions revolved around facilitated discussions, small breakout sessions, unique note-taking techniques, networking and sharing of experiences. "We sought to create an environment where the learning could flow between our presenters and attendees," says Wilson.

Attendees included bankers, entrepreneurs, venture capitalists, and representatives from numerous community organizations, municipal governments, academia, and more—including some from outside the Eighth District. "We were quite pleased that we were able to help this diverse group come together and see how their individual components could mesh, whether they worked in finance, affordable housing, entrepreneurship or economic development," Wilson says.

And just what *did* they learn? Some of the many financing concepts that presenters and organizers drove home were:

- Use the already-established resources in your community in a collaborative sense.
- Be creative in your approach to find sources of capital, which can include social groups and the government.
- Start thinking in innovative ways to help others outside your immediate circle and draw them into your network. For example, identify business models that nonprofit organizations could use to become self-sustaining; or determine what role your financial institution can play to address a developer's needs to make a project work.

Those examples barely begin to give an idea of what was presented, discussed and mulled over throughout the conference. Innovation presenters also wanted attendees to look inside their organizations, as well. For example, Paul Light, a professor at NYU Wagner, gave four characteristics that innovative organizations share:

- They know the future will change, which helps them stay relevant.
- There are six or fewer layers between the top and bottom, making them agile as organizations.
- Their employees are saturated with information about what is going on and are more likely to offer ideas to generate change.
- They realize that changing things requires knowing the starting point and anticipating where they could end up.

If you want to fully understand what attendees heard and learned, go to www.stlouisfed.org/community/innovation/web/framepages/index.htm and scroll through each day's notes. You'll see the ideas that were presented, as well as the actual notes of those ideas.

To take innovation in community development finance further, Wilson and Ashby recommend using the notes from the conference as both a starting point and an ongoing resource. The conference page is a permanent addition to the Fed's web site.

And in 2008, the Community Affairs staff will kick off the first Exploring Innovation in Community Development Week, with activities planned throughout the District. ■

Regional Roundup

Little Rock Team Takes Top Honors in National Fed Challenge

A team of students from Little Rock (Ark.) Central High School won first place in the spring in the Fed Challenge, a national economics competition sponsored by the Federal Reserve System. The Little Rock team was Shariq Ali, Stuart Shirrell, Cameron Zohoori, Brent Sodman and Hilary Ledwell, with Charles Meyers as an alternate. The coach was teacher George West.

Each of the seven finalist teams made a 15-minute presentation before a panel of judges in a mock Federal Open Market Committee format. Their presentations were based on research of economic conditions and a recommended course of action for monetary policy.

Robert Hopkins, senior executive of the St. Louis Fed's Little Rock Branch, said, "I'm not surprised that the Central High students are national champions. Their willingness to seek constructive criticism, ask questions and dig deeply reflected their commitment. They are a group of smart, talented, hard-working young adults. Their futures are very bright, and we at the Fed wish them well." ■

GeoFRED™ Gets You Connected to Fed Employment Data

The St. Louis Fed's Research division recently added the GeoFRED™ web-based application, which lets users create thematic maps of U.S. economic data by state, county or metropolitan statistical area. Maps can be generated from more than 12,000 regional data series available in the FRED® database, including civilian labor force, residential population and unemployment rate.

Bankers, economists, teachers or anyone else interested in unemployment rates, government employment rates, manufacturing employment rates and other pertinent information can go to GeoFRED and get the numbers.

Previously, these numbers were available only for the Eighth District as part of a downloadable database. Now, users can click on a map and compare unemployment figures in St. Louis County, Mo., with Harris County, Texas, for example. GeoFRED also can sort numbers by state, MSA and more. The data spans from 1990-2006. Find GeoFRED at http://geofred.stlouisfed.org. ■

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Fed Seeks Better Supervision of Subprime Lenders

The Federal Reserve is joining forces with two federal agencies and two associations of state regulators to conduct targeted consumer-protection compliance reviews of selected nondepository lenders with significant subprime mortgage operations.

The pilot project will begin during the fourth quarter of 2007. The review will focus on nondepository subsidiaries of bank and thrift holding companies, as well as mortgage brokers doing business with, or working for, these entities. The states will conduct coordinated examinations of independent state-licensed subprime lenders and their associated mortgage brokers. For more information, see www.federalreserve.gov/boarddocs/press/bcreg/2007/20070717/default.htm. ■

Changes Proposed to Regulation Z's Credit Disclosures

The Federal Reserve Board wants more effective disclosures for consumers from credit-card accounts and other revolving credit plans as part of its sweeping review of open-end credit rules. To that end, the Board has proposed amendments to Regulation Z (Truth in Lending), and you have a chance to comment on the proposal until Oct. 12.

The amendments, based on consumer testing feedback, focus on the rules for open-end credit accounts that are primarily general purpose and retail credit-card plans. In short, the changes are designed to make disclosures and information more understandable for consumers.

The proposal would require changes to the format, timing and content of disclosures for credit-card applications and solicitations. It would also change the information that consumers receive throughout the life of an open-end account, including account-opening and periodic statements.

In addition, disclosures with credit-card applications and solicitations would highlight fees and penalty rates. Creditors would be required to summarize key terms at account opening and a change in terms. Periodic statements would identify costs for interest and fees.

Two alternatives are being considered for the effective or historical annual percentage rate disclosed on periodic statements. The proposal would also increase the circumstances under which consumers receive written notice of changes in terms to their accounts. For more information or to comment, go to www.federalreserve.gov/boarddocs/press/bcreg/2007/20070523/default.htm. ■

Is There an Inflation Disconnect, and Could It Affect Policymaking?

By Riccardo DiCecio

Riccardo DiCecio is an economist at the Federal Reserve Bank of St. Louis.

When you read or hear about inflation measures in the media, you should be aware that economists have noticed a disconnect between different measures of inflation. *Headline inflation* is the percentage change in the price index for a basket of goods and services. *Core inflation* measures the underlying trend in inflation. The most common way to measure core inflation is to exclude food and energy from the set of goods and services. The rationale for excluding food and energy prices is that historically they have been highly volatile and high volatility tends to mask the underlying trend. But why always exclude these two classes of goods while including others?

The difference between headline inflation and the most commonly used measure of core inflation (less food and energy, or XFE) has been increasing since early 2004. The gray line in the chart illustrates this by showing a five-year moving average of the difference between headline consumer price index (CPI) inflation and CPI-XFE inflation. The discrepancy between these two indices reflects the sharp and sustained increase in the price of oil between mid-2004 and mid-2006. The inflation rate of the energy component of the CPI (CPI-E) has been growing much faster than the overall CPI. (The orange line in the chart shows the difference between the two.)

The academic literature is increasingly focused on limited-influence estimators to measure core inflation. The Federal Reserve Bank of Cleveland calculates two such monthly measures of core inflation: the weighted median and the trimmed mean CPI inflation rates. These measures exclude the items facing more extreme price movements in each time period, resulting in a different basket of omitted items each period.[1]

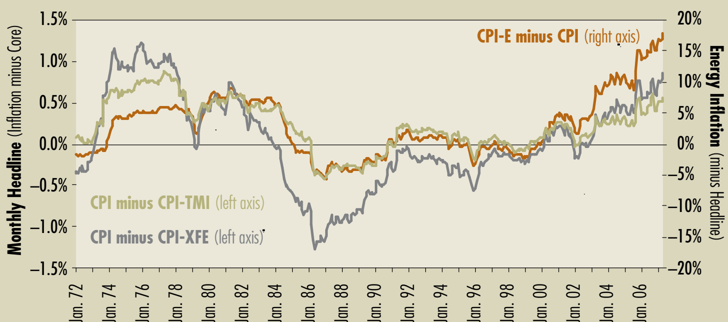
Proponents have argued that limited-influence measures of core inflation have superior statistical properties and, in particular, are better at forecasting headline inflation. The tan line in the chart shows the difference between headline inflation and core inflation, measured by the 16 percent trimmed mean CPI inflation (CPI-TMI). This smaller difference between core and headline inflation suggests that discrepancies between headline and core inflation are partly induced by the way core inflation is defined and measured.

The reason why this disconnect between measures of headline and core inflation is being discussed is because it could be a concern for policymakers: It may not be reasonable to conclude that monetary policy has been effective in maintaining price stability by looking solely at a core measure of inflation that excludes sustained oil price increases.

However, keep in mind that an increase in energy prices could present monetary policymakers with a trade-off between controlling inflation and stabilizing the output gap, i.e., the difference between actual and potential output of the aggregate real economy, if these price increases affect actual output more than potential.

In sum, price indices provide a snapshot of the dynamics of prices of a basket of goods and services. However, because each core index suppresses a different source of information, each provides a different measure of inflation. Especially in times of substantial relative price movements, all price indices should be considered by policymakers and analysts. ■

CPI Inflation Rates: Headline, Core Measures and Energy
(5-year moving averages of annualized % change)



SOURCE: Bureau of Labor Statistics/Federal Reserve Bank of Cleveland/Haver

ENDNOTE

[1] Mick Silver, "Core Inflation Measures and Statistical Issues in Choosing Among Them," Working Paper No. 06/97, International Monetary Fund, April 2006.

FedFacts

Fed Offers New Online Mortgage Comparison Calculator

The Federal Reserve Board offers an online mortgage comparison calculator to help consumers make informed decisions when they shop for home loans. The calculator lets them compare monthly mortgage payments and equity accumulation for up to six types of mortgages, including 30- and 15-year fixed-rate mortgages, interest-only fixed-rate mortgages, adjustable-rate mortgages (ARMs), interest-only ARMs and payment-option ARMs.

To use the calculator, you need to compare at least one fixed-rate mortgage with at least one adjustable-rate mortgage. The calculator also includes a mortgage shopping worksheet, a glossary of mortgage terms and links to the Board's other consumer education resources on mortgages. The calculator is found at www.federalreserve.gov/apps/mortcalc/. ■

Agencies Offer Illustrations Describing Nontraditional Mortgage Products

As part of an ongoing effort to help educate the public on nontraditional mortgage products, federal bank, thrift and credit union regulatory agencies issued final illustrations earlier this year that explain the risks of those products. The illustrations are part of the 2006 Interagency Guidance on Nontraditional Mortgage Product Risks.

Institutions are not required to use these illustrations, but the representations can help consumers get clear and balanced information about nontraditional mortgages before choosing a product or selecting a payment option for an existing mortgage. Note that these illustrations are not pictures, but rather:

- a narrative explanation of nontraditional mortgage products,
- a chart comparing interest-only and payment option adjustable rate mortgages (ARMs) to a traditional fixed-rate loan, and
- a table that could be included with monthly statements for a payment-option ARM, showing the impact of various payment options on the loan balance.

The illustrations can be downloaded from www.federalreserve.gov/boarddocs/press/bcreg/2007/20070531/attachment.pdf. ■

CalendarEvents

UPCOMING FED-SPONSORED EVENTS FOR EIGHTH DISTRICT DEPOSITORY INSTITUTIONS

Reaching the Unbanked and Underbanked

LITTLE ROCK, ARK.—OCT. 18

This series for financial institutions discusses the unbanked and underbanked. This session will focus on acquiring customers through stored value cards and building loyalty through second-chance checking accounts. The fee is $15. Registration is due Oct. 11 by contacting Julie Kerr of the St. Louis Fed's Little Rock Branch at 501-324-8296 or julie.a.kerr@stls.frb.org.

Meetings and Economic Forums

NOVEMBER

The St. Louis Fed will host a banker meeting and two economic forums in November. St. Louis Fed President Bill Poole will discuss Fed policy and the national economy. Participants may share their observations about local economic conditions, business trends and factors affecting the national economy. Call Jill Dorries at the St. Louis Fed at 314-444-8818 to register.

- Nov. 13—Tupelo, Miss., Economic Forum
- Nov. 28—St. Louis Banker Meeting
- Nov. 29—Mount Vernon, Ill., Economic Forum

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