

letter from the president

Thank you for your interest in the work of the Federal Reserve Bank of Boston and the Federal Reserve System. I am happy to share this report on our 2008 activities and to provide some observations on the year—a very challenging one for the U.S. economy.

Financial turmoil and difficulties in credit markets began in 2007 and persisted through 2008. Economic challenges are now taking a toll on many Americans and on companies large and small. Officially in recession since the end of 2007, despite positive GDP growth in the first half of 2008, the United States saw economic conditions deteriorate sharply in the second half of the year as both consumers and businesses retrenched. Consumer wealth was buffeted by declining home values and falling stock prices, and as the year ended the unemployment rate had risen to 7.2 percent in the nation and 6.9 percent in New England.

To help address the ongoing difficulties in financial markets and the weakening economy, the Federal Reserve was very proactive in 2008. We took the federal funds rate target to only slightly above zero—essentially as low as it can go—and created a variety of lending facilities to restore liquidity and help lower the elevated spreads on many interest rates in the marketplace. Well-functioning credit markets are essential to restoring the economy's health, and I believe the measures taken by the Federal Reserve, coupled with fiscal policy, will provide critical support in the year ahead.

Difficult economic times and turbulent financial markets led to several significant initiatives for the Bank in 2008. One was a major foreclosure-prevention workshop that we and the New England Patriots Charitable Foundation held at Gillette Stadium in August. The event brought thousands of troubled borrowers together with their loan servicers. It was just one manifestation of the Bank's broader focus on the problems stemming from subprime mortgages and on finding ways to address rising foreclosures. Another notable initiative was the lending facility that we in Boston set up for the Federal Reserve System. This facility, the AMLF (asset-backed commercial-paper money market mutual fund liquidity facility), helped ease strains experienced by money market mutual funds and "seize-ups" in commercial-paper markets by providing loans to banks enabling them to buy high-quality asset-backed commercial paper from the funds. These and other aspects of our work this year are described in the Bank Highlights section of this report.

The Bank also made strong contributions to our core areas of expertise, including monetary policy, supervisory policy, payments and other services for financial institutions and the U.S. Treasury, economic research, and regional and community initiatives. An important Bank priority is providing high-quality analysis of public policy issues

affecting the New England region—and a particular focus in 2008 involved New England’s future skilled labor force and steps that might help the region retain recent college graduates. Alicia Sasser, a senior economist in our New England Public Policy Center, has contributed an essay on this topic to this annual report, and has helped spark ongoing policy discussions among business leaders, policymakers, and educators that we hope will result in strategies that benefit the region.

The events of 2008 demonstrate that the nation’s financial regulatory framework needs to be reconsidered. Reform of our financial regulatory framework promises to be a major topic for policymakers in 2009, and my hope is that the deliberations will be guided by a few key principles. Specifically, I believe that macroeconomic stability must be a priority of financial regulation, in addition to the safety and soundness of individual institutions. And, because it is central to macroeconomic stability, systemic financial stability needs greater focus (with roles in a crisis more clearly articulated). Liquidity risk, so evident in 2008, similarly deserves greater attention in policy and in regulatory structures. And regulatory coordination (both domestic and international) needs careful thought and attention, as does strengthening market infrastructure (including standardizing securitization contracts and establishing exchanges for more transactions).

In closing, I want to thank the staff of the Bank for their dedicated efforts in a very challenging year. I know they join me in seeking to make a difference in the public’s interest. I also thank our directors and the members of our advisory groups for their commitment and their desire to work with us.

In particular, I want to express the Bank’s appreciation for the service and insights of Kathleen Marcum, President and CEO of Millbury National Bank, who completed three years of service as a member of our Board of Directors in 2008. Kate’s energetic counsel and expert perspective as a lender have been of great benefit to the Bank, and we thank her.

Sincerely,



Eric S. Rosengren
President and Chief Executive Officer

