



# 2006 Bank Highlights:

## Our Role in New England and the Nation





The Bank had the pleasure of welcoming Chairman Ben Bernanke for an extended visit in June. It was in truth a welcome back, since as an economist Bernanke had spent time as a visiting scholar at the Bank in 1989 and 1990. During his visit, Chairman Bernanke met with local business leaders, the Bank's leadership and directors, and staff.

In a lively Bankwide gathering, the Chairman answered questions on a wide variety of topics – ranging from economic policy to payments innovations, and from formative experiences in his career to his typical workday. The Chairman also reflected on the fundamental public-service mission of the Federal Reserve System – the motivating sense, shared by staff throughout the System, that the work of the central bank can make a difference to the welfare of average citizens.



*The Bank focuses its activities in four major areas:*

- *maintaining a safe, efficient, and cost-effective payments system,*
- *conducting economic research to support monetary policy and advance economic understanding,*
- *maintaining a safe and sound banking system, and*
- *sharing our expertise to benefit the public.*

The Federal Reserve Bank of Boston continued to manage significant change in 2006. At the same time, we achieved a variety of successes, passed a number of key milestones, and further refined our view of how the Bank can best serve New England and the nation in the years ahead. Below are Bank highlights of 2006.

## **Payments Services**

### **Check**

- The Bank consolidated its **check processing operations** into one large operation at our Windsor Locks CT office. This successful consolidation provides a highly efficient environment for check processing.
- The transformation from **paper to electronic** check processing accelerated nationally and in New England. By year-end, 34 percent of the Bank's check volume was being deposited in image form or being converted into images for collection. The Bank is a Federal Reserve System leader in Check 21, the national initiative to support electronic check collection.

## Cash

- In a move that improves efficiency, our cash services operations began to implement a **custodial inventory program** with New England banks. The program supports the efforts of banks to recirculate currency to meet their customers' demands. This is a more efficient and cost effective approach for banks and their customers.
- Cash services staff held an **annual customer conference** with presentations on cash usage trends, counterfeit activity, and the custodial inventory program.

## Stored Value Cards

- A team from the Bank spent almost two months in Iraq and Kuwait implementing the **stored value card program** developed by Bank staff for military personnel on duty overseas. The team provided training, bank account set-up, and overall management as well as equipment installation. Military personnel can use stored value cards to pay for goods and services at overseas bases, eliminating the need for the military to keep stores of cash overseas. Stored value card programs supported by the Bank now operate at 34 military bases worldwide.

## Internet Payment Platform

- We conducted some 70 outreach sessions with federal agencies to explain the Internet Payment Platform, a **web-based service** being developed at the Bank to enable federal agencies to process all purchase orders, invoices, and payments information electronically. IPP is on target for implementation in November 2007.

## Emerging Payments Research Group

- The Emerging Payments Research Group, a multi-disciplinary team of payments professionals and economists, enhanced our



understanding of consumer payment behaviors and their impact on the payments system. EPRG conducted a three-day conference on consumer behavior and payment choice; developed a case study of online payment service providers; and identified gaps in industry-led **consumer payments research**.

## Economic Research and Monetary Policy

### Research Department

- The Bank's research economists published a record 26 working papers and public policy discussion papers in 2006, with 20 papers accepted at leading academic journals. Topics of research included the risks posed by **alternative mortgage instruments** in a slowing housing sector; changing estimates of steady-state growth of employment and potential output; and changes in **inflation dynamics**.

- The Bank's June **research conference**, "Global Imbalances as Giants Evolve," examined shifts in the global distribution of labor, capital, and technology, focusing on the recent **emergence of China and India** as important actors in the global economy. The essay in this annual report features this topic and draws on conference presentations.

### Center for Behavioral Economics and Decision-Making

- The Bank's Center for Behavioral Economics and Decision-Making, a unit of the research department, co-sponsored a conference on **life-cycle saving and investing**. The conference examined what optimal saving and investing should be, why people deviate from the optimal, practical models for financial planning, innovative products, the role of government, and possible educational initiatives. Follow-up research is planned.

- Working with Public and Community Affairs staff, the Behavioral Economics Center began a number of research projects related to consumer education and protection, including a study of the **efficacy of credit counseling**. The same team also undertook a cooperative effort with the U.S. Treasury to find ways to increase acceptance





of electronic payments among unbanked persons; and a cooperative effort with the Board of Governors to use behavioral economics to inform the development of regulations.

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## Safe and Sound Banking System

- **New England banks** recorded strong profits in 2006, as was also true for banks nationwide. However, net interest margins continued to narrow, and, in addition, many banks found it more challenging to attract deposits. Deposit growth in New England slowed substantially relative to previous years.
- Bank supervisory staff played a key role in the Federal Reserve System's nationwide program for supervising large financial institutions (LFIs). Staff of the Bank assisted in the development of a governance process involving new models for sharing information, best practices, and risk assessments and helped lead a program of **operational risk assessment** for LFIs.
- Bank staff continued to make important contributions to the System's work on Basel II. "Basel II" is shorthand for a multinational effort to develop international capital standards for large banks. Bank staff prepared two white papers on ways for **quantifying operational risk** with respect to Basel II capital requirements and made numerous presentations on operational risk to national and international audiences.

## Outreach

### Economic Education

- Visits to the Bank's on-site **New England Economic Adventure** were up by 10 percent in 2006, while "virtual visits" in economic education – that is, hits to the educational materials on our public web site – increased by over 400



percent compared with 2005.

- The Bank hosted a “**Reserve Cup**” challenge that pitted high school teams from each New England state against one another to test their knowledge of personal finance, economics, financial literacy, and the Federal Reserve System. The competition was subsequently televised throughout New England.
- Bank staff developed a second interactive educational tool, *Show Business: The Economics of Entertainment*, to join the web-based game, *Peanuts and Crackerjacks*, as a means to engage students in learning economics. The Bank is emphasizing **interactive instruction**, in the belief that making the learning process fun and engaging makes it more effective.
- Some 30 secondary-school teachers from throughout New England attended a three-day **teacher workshop** hosted by Bank on the topic “globalization and international economics.”

#### **New England Public Policy Center**

- The Bank’s New England Public Policy Center, created in 2005 to focus on economic and public policy issues affecting the region, conducted research on a number of topics, including the **lack of affordable housing**, regional energy needs, and **disparities in non-school costs and revenue capacity** among Massachusetts cities and towns.

- Policy Center staff prepared 18 “rapid-response” memos to address questions posed by regional policy makers and held meetings with policy makers, analysts, and researchers in each of the six New England states to gain intelligence about **emerging issues**.
- **Health insurance** was the focus of “Covering the Uninsured: Costs, Benefits, and Policy Alternatives for New England,” a conference sponsored by the Policy Center.

#### **Community and Consumer Affairs**

- The Bank worked with regulators in the region to call attention to the growing numbers of mortgage foreclosures. A brochure highlighting **risks associated with alternative mortgages** was developed and broadly disseminated. It is being used in the City of Boston’s new home buyer and credit counseling courses.
- Through a conference, discussion paper, and articles in publications, Bank staff explored and spotlighted two

emerging community **economic development strategies**: how public sector pension funds can support community development while earning a market rate of return, and how secondary cities can attract venture capital funding.

- The Bank strengthened its **community affairs outreach**, conducting 81 meetings with government officials, nonprofit groups, businesses, and others throughout the region. These meetings solidified relationships and helped clarify important regional trends.

### Community Relations

- Through its FinTech program, the Bank provided **internship opportunities** for 12 Boston students with the objective of enabling and encouraging them to follow careers in financial services. We were pleased to see most participants significantly improve their school grades, and we are now sharing our experience with other major financial services providers.

- Working with the City of Boston, the Bank provided training and volunteer support for the City's **Earned Income Tax Credit campaign** to help eligible working people receive this important benefit. Building on this program, the Bank initiated with the City a consumer **credit repair program** that aims to help consumers make better choices in managing revolving credit.

