Federal Reserve Board Oral History Project

Interview with

Charles J. Siegman

Former Senior Associate Director, Division of International Finance

Date: September 11, 2006

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Interviewers: David H. Small and Dale Henderson

Federal Reserve Board Oral History Project

In connection with the centennial anniversary of the Federal Reserve in 2013, the Board undertook an oral history project to collect personal recollections of a range of former Governors and senior staff members, including their background and education before working at the Board; important economic, monetary policy, and regulatory developments during their careers; and impressions of the institution's culture.

Following the interview, each participant was given the opportunity to edit and revise the transcript. In some cases, the Board staff also removed confidential FOMC and Board material in accordance with records retention and disposition schedules covering FOMC and Board records that were approved by the National Archives and Records Administration.

Note that the views of the participants and interviewers are their own and are not in any way approved or endorsed by the Board of Governors of the Federal Reserve System. Because the conversations are based on personal recollections, they may include misstatements and errors.

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MR. SMALL. Today is Monday, September 11, 2006. This interview is part of the preparation by the Board of Governors of the Federal Reserve System for the celebration of its centennial. I am David H. Small from the Federal Open Market Committee (FOMC) Secretariat in the Division of Monetary Affairs. I am joined by Dale Henderson of the Board staff. Today we will be interviewing Charles J. Siegman, formerly a senior associate director in the Division of International Finance (IF) at the Board of Governors. Mr. Siegman worked at the Board from 1967 to 1998. Mr. Siegman, I want to thank you for participating in our Oral History Project.

I thought we'd start with general background about who you are, where you grew up, where you went to college and graduate school, and any early influences in your life toward academics or economics.

Education and Professional Background

MR. SIEGMAN. I was born in the Netherlands and came to the United States in 1946. I was raised in the New York area and attended the City College of New York and Columbia University School of Graduate Studies. With my international background, I was exposed to world issues through family and friends and in New York. Being sort of a world citizen made me interested in world economics. I majored in economics at City College. I had some very good economics professors there and at Columbia. I remember very fondly Ragnar Nurkse at Columbia. He was well known in the field of international economics. I also had Arthur F. Burns as a professor at Columbia. My interest in economics started formally in undergraduate school and in graduate school. Subsequently, I taught for four years in the Department of Economics at City University and then five years at Swarthmore College. Besides introductory economics, my regular teaching load included international economics, monetary economics, and comparative economic systems. So when I came to the Board, I was not just a fresh graduate—I had experience as an academic.

MR. SMALL. What was international economics like at the time?

MR. SIEGMAN. The discipline was in transition. There was clearly an interest in comparative economics because of the Soviet Union and its satellites. Running a planned economic system was different than running a market-oriented economic system in a Western society. That was one of the reasons I became involved in comparative economic systems both as a student and as a faculty lecturer. The recovery of Europe in particular was on the policy forefront when I was a graduate student and subsequently when I taught economics.

There were discussions about protectionism and the exchange rate regime. In those years, the exchange rate regime was based on the U.S. dollar, the dollar being the dominant currency, and countries were eager to build up their dollar reserves. One of my professors at City College, Elliott Zupnick, had written a book about the dollar problem, and four or five books were published at that time about the potential problem of a dollar shortage.

The political scene in the United States at that time dealt mostly with national issues. International issues were not the primary focus of elections except those related to the Soviet Union and the associated Cold War. But the world economy was not a major topic of discussion. People and the media periodically discussed the role of gold in the international financial system, and sometimes politicians said the wrong thing about gold, which shot up the price of gold. But gold was typically not a critical policy variable. The threat of protectionism and the pros and cons of comparative economic systems dominated the discussion of international-related economic issues.

MR. SMALL. When people think of Arthur Burns in his academic role, they think of business cycles, probably with a focus on domestic. Did he have much influence on you in your international aspects?

MR. SIEGMAN. Not much. There were two faculty members at Columbia named Arthur Burns—one was Arthur F. Burns and the other was Arthur R. Burns. This caused confusion both for students registering for classes and in referring to one of the two; so one professor was called Arthur "Fluctuations" Burns and the other Arthur "Research" Burns. The latter was British and the former American.

At Columbia, Arthur F. Burns [future Chairman of the Federal Reserve] was not international oriented. At that time, he had already made his imprint at the National Bureau of Economic Research with his study on business fluctuations. We read his and Wesley C. Mitchell's and John Clark's published works as part of the assignments. Burns's focus at that time was on the risks and evils of inflation. He wrote a long essay on inflation for an American Assembly publication, and he published a booklet on the causes and dangers of inflation.

MR. SMALL. What time period is this?

MR. SIEGMAN. This was in the late 1950s and early 1960s. When Arthur Burns came to the Board in 1970, he had the reputation as an inflation fighter, but not from a monetary policy angle. It was more about the costs of inflation—inefficiencies in the functioning of the financial system, frictions, inequities, and business cycle movements resulting from the policy responses to curb inflation. When Arthur Burns came to the Board, he was not what one would call a monetary economist.

Early Years Working in the Division of International Finance

MR. SMALL. When you came to the Board, can you explain how IF was structured in units, which unit you started in, and what your initial job was?

MR. SIEGMAN. When I came to the Board for my interview, I was interviewed for positions in different sections in IF. In part because of my academic background, I wasn't viewed as a narrow country or subject specialist but rather as a generalist, which was in my favor. I was interviewed by different section chiefs, some section staff members, and certain officers: Arthur B. Hersey, John E. Reynolds, Reed J. Irvine, and Samuel I. Katz. Robert "Bob" Solomon was the division director then; he organized the interviews. It was then that I met Ralph C. Bryant for the first time. He was a young assistant to Bob Solomon. I got a flavor of the division, and they got some sense of who I was as well.

Eventually they offered me a position in two or three of the sections. One position was in the industrial countries section. At that time, it was called the Europe, Commonwealth, and Japan Section—a strange name. I selected that section. It dealt with studying what was happening in individual countries: the United Kingdom, Germany, France, Canada, a few smaller European countries, and Japan. Bob Solomon asked me whether I was interested in handling "emerging Europe and the Common Market" as a unit, which was forward-thinking, because nobody at that time was looking at Europe as an entity. I took that on. That's how I began my specialization in integration, cooperation, and dealing with the larger picture of the international economy rather than looking at the performance and policies of individual countries.

MR. SMALL. So that started your work on cross-country meetings?

MR. SIEGMAN. Well, there was a need for cross-country work in the division and a focus on cross-country interrelationships because there were six separate countries in the Common Market, and there were issues of how to analyze what was happening in the Common Market as a whole. Does one treat the European Economic Community (EEC) as one entity, with a central organization, or does one treat and analyze what was happening in the EEC in terms of six individual countries? This was only the first stage. Initially, I viewed and analyzed the EEC as a group of individual countries, but subsequently I increasingly started to treat and analyze the EEC from a "one entity" perspective and to follow the economic and financial integration process that was evolving in Europe.

MR. HENDERSON. Can you comment on the potential tension between focusing on countries and focusing on subjects across countries?

MR. SIEGMAN. Yes. As a generalist without a particular country assignment, I was looked at as a partial outsider in that section because everyone else had their country and certain routine assignments. At that time, there were 12 FOMC meetings a year, and meetings were held every three or four weeks. Staff lived a sort of FOMC-cycle life, preoccupied from FOMC meeting to FOMC meeting with preparing Greenbooks, Board briefings, and country updates. While efforts were made to have country specialists focus on cross-country subjects, staff had very little breathing space and time to do so if they were following a particular country or a few smaller countries. They were busy monitoring and reporting on individual countries and mining the information about them.

I didn't have direct country responsibility, although, oddly enough, I had to keep up with what was happening in all of the members of the EEC without being a specialist on any of them. Because of my assignment, over time I was given different tasks. I was an open slot for some cross-country subjects. So I was lucky. I was drawn in when European Common Market issues came up. I was called upon to analyze some cross-country issues and periodically give briefings on these and EEC-related matters to the Board.

MR. HENDERSON. How did the division between country specialists and subject specialists evolve over the years?

MR. SIEGMAN. Well, the workload shifted, because people had more time as the Board moved to fewer FOMC meetings and as the division hired more macro and monetary policy–trained economists. There was a lot of cross-country fertilization in the division. If someone followed Germany and something significant, particularly in policy, happened over there, he was entitled and encouraged to do a cross-country analysis of the issue that was relevant to Germany either on his own or in cooperation with other country specialists. The rest of the division also was covering many functional subject areas, and staff from different sections were encouraged and given time to do cross-section research in depth in diverse subject areas of relevance to the work of the division at large and of interest to the Board.

I came to the Board in the middle of an ongoing evolution of the division. It was noticeable that more and more of the newly hired staff were trained in, and exposed to, more rigorous analytic and empirical methods compared with the existing staff. The latter may have had similar graduate degrees, but they examined issues more from an institutional economics rather than from an analytical perspective. So there was both more need and more scope to utilize highly trained staff for subject matter issues.

Role of the Board in International Relations beginning in Post–World War II

MR. SMALL. In those early years, I can understand why the Federal Reserve would want to monitor many countries because of the effects, or the lack thereof, on the U.S. economy.

What was the role of the Fed in international relations and bringing about agreements? Was it a central player? Was it just a passive one of carrying out agreements?

MR. SIEGMAN. I wasn't at the Board immediately after World War II, so I did not know exactly who the key players were at the Board. But in dealing with those who were at the Board after the War—if I recall correctly—quite a few people from the Federal Reserve were advisers for the reconstruction of Western Europe and Japan following the war, dealing with hyperinflation problems and reestablishing a banking system or a central bank. Arthur Hersey dealt with Japan, and other Federal Reserve staff dealt with the reestablishment of an orderly economic system in Europe and Japan. They provided expertise.

The regional organization at the time, the Organisation for European Economic Co-operation (OEEC)—which evolved into the Organisation for Economic Co-operation and Development (OECD)—was the financial arm of the Marshall Plan to distribute money and provide assistance for the reconstruction.

Besides attending meetings, Federal Reserve personnel were involved periodically in providing analysis and policy guidance on issues the OEEC, and subsequently the OECD, started delving into. Many of those issues involved cross-country matters. The international monetary system had broken down, and the use of national currencies was typically limited to national markets, thereby inhibiting international trade and international investment and lending. In that setting, European currencies were not convertible—i.e., the currencies of one country could not be exchanged for the currencies of other countries—and European countries imposed all sorts of trade and capital controls to maintain currency inconvertibility. Initial attempts by some countries to make their currencies convertible failed and led to foreign exchange market turmoil.

Reintroducing convertibility in Western Europe and making their national currencies useable and acceptable throughout the region—as a means of facilitating intercountry trade and reducing and eliminating trade restrictions—required international cooperation. The OEEC (and subsequently the OECD) in Paris was the forum where these international efforts were discussed and formulated. The effort to restore convertibility included providing financial support (balance of payments support) to countries that were restoring convertibility of their currencies in case these countries were to face pressure on their currencies as a result of doing so. Senior Federal Reserve officials participated in these initiatives, and their knowledge of, and experience with, financial issues proved valuable both to the U.S. Treasury (which typically headed the U.S. delegation to these meetings) and the OEEC/OECD. IF provided the staff support in these efforts.

The OECD had a special committee, Working Party Three (WP3), represented by senior finance/treasury and central bank officials, which was the primary discussion group for consistency of policies appropriate, given the circumstances at the time. Whenever there was a balance of payments problem for a country with the fixed exchange rate, in order to sustain the rate, the country needed more reserves—more dollars in most cases, since the dollar was the preferred fully convertible currency. Financial packages were arranged on the sidelines of WP3 meetings to support countries facing balance of payment and exchange rate pressure problems. During this period, a Governor and a senior IF officer—Bob Solomon at the time—represented the Federal Reserve at WP3. Although the Treasury was the principal spokesperson for the United States at WP3 meetings, the Federal Reserve was very active in formalizing the parameters of the packages, including the terms and the size, and mobilizing the participants.

Quite often, WP3 meetings were the most important international meetings for staff preparation and follow up.

MR. HENDERSON. Did the Treasury and the Fed see eye-to-eye on these packages and assistance, or were they at odds?

MR. SIEGMAN. I was not intimately involved in these early years. But my understanding was that there was dialogue between the two parties if there were differences of views. There was a consensus on the need to sustain the fixed exchange rate system and thus the need to bolster it with financial support where necessary. If a balance of payments problem was emerging for a particular country, then there was a need to find some way to make it sustainable.

The United States was regarded as a strong economy. The United States had to lead both in organizing these financial arrangements and in putting up a major portion of the money when necessary. The International Monetary Fund (IMF) was not involved at that stage in arranging balance of payments assistance programs for industrial countries.

MR. HENDERSON. What role did the Bank for International Settlements (BIS) play?

MR. SIEGMAN. At that time, the BIS was primarily a meeting place for central bankers and was not a major participant in balance of payments assistance deliberations. It did not play a role in the financing arrangements until later as these packages evolved. In later years, given that the BIS had a lot of money from deposits from central banks, it was an active participant in international balance of payments assistance arrangements (in effect, representing the contribution to these packages from some central banks) and in the formulation of the financial assistance responses to various international debt crises.

MR. HENDERSON. Was the Federal Reserve active in organizing the swap network?

MR. SIEGMAN. That started in the 1960s. In an effort to shore up the fixed exchange rate system, the central banks of the major industrial countries (the Group of Ten, also known as the G-10) and of Mexico negotiated bilateral lines of credit, with prearranged terms. Access to these lines was not automatic; they had to be requested, approved, and activated and, in practice, were drawn upon infrequently by most of the participants in the swap network. There were also a few swap lines that the U.S. Treasury had with a few of its counterparts, but they were the exception rather than the rule.

The existence of the swap network gave the Federal Reserve some leeway and influence in the arrangements of balance of payments support packages. The swap network was a Federal Reserve domain item, activated sometimes at the behest of the Treasury. The swap lines were supposed to be used for shorter periods than the financing arrangements of the negotiated balance of payments support packages. They were a sort of first line of defense to tide a country over until the negotiations for longer-term financial support were completed.

The activation of a bilateral swap line was intended to provide a signal to the market that the country experiencing exchange rate pressure was about to receive international support. You're not going to give a country short-term credit and not give it long-term credit if it was needed. To that extent, the activation of the swap network was supposed to reassure markets. On the other hand, in activating the swap network, there was the risk that if the market becomes aware of the activation, it could be misinterpreted that the recipient country was facing a serious balance of payments problem, thereby intensifying pressure on that country's exchange rate.

To your question about the Treasury and the Federal Reserve seeing eye-to-eye on providing financial support to countries facing balance of payments/exchange rate pressure, my impression was that there was consensus on the basic principle of the need for these packages.

At times, Treasury and Federal Reserve officials had different views on the timing and size of the financial support arrangements under discussion, and different countries sometimes had different views. But I think disagreements between the Treasury and the Federal Reserve about a particular loan package were resolved before the meetings and discussed very professionally, very civilly. It was not a "them versus us" situation.

MR. SMALL. Did the Chairman have a powerful role in setting the tone of the debate, in setting the standards for loans?

MR. SIEGMAN. I did not work closely with Chairman William McChesney Martin, Jr., during my early years at the Federal Reserve. I only observed him. I also heard about him from Bob Solomon and others, and I read his speeches and testimonies. He was less of a hands-on Chairman on day-to-day issues than later Chairmen. He focused more on big picture issues.

The senior staff—Bob Solomon on international and his counterpart on domestic matters—kept the Chairman well informed. He basically nodded when something made sense and people went on to do their thing. On the big picture issues, he raised his voice formally, making his position heard, and he represented the System. But on routine matters, he was not noticeably in the forefront. He didn't make many public declarations, and his speeches on international subjects were few and far between. There was one prominent speech about intervention in gold markets. People repeatedly cited it because there were so few other speeches on international matters by him. His testimony focused more on U.S. issues.

By the time Arthur Burns became Chairman in 1970, with the financial problems of the world changing—problems becoming more frequent and bigger—and with systemic issues emerging, the Chairman's role in the financial assistance program deliberations became more active, with different Chairmen at times taking strong positions.

MR. SMALL. Ultimately, the United States left the gold standard. Who at the Board foresaw that development early on? Who had insights into the problems behind that development for which the Board had to deal?

MR. SIEGMAN. The pressure on the gold standard erupted periodically, in part because it was a dollar–gold standard, and the dollar and gold were interlinked. Whenever there was pressure on the dollar, that pressure was reflected on the gold market.

In March 1968, there was a major gold crisis meeting at the BIS, resulting in the modification of some of the limits of the gold points at the margin. The United States needed the consent of other central bankers for this modification. I was in Basel on detail at the BIS at that time. I had been working at the Board only a few months. I arrived at the Board in July 1967, and, in October, Bob Solomon asked if I would like to go to Basel on detail. I didn't know if it was a compliment or a way to get rid of me after a few months! [Laughter]

I went, and it was an interesting experience. I was the U.S. person on the premises, a Federal Reserve mascot of sorts. Chairman Martin and Bob Solomon came for this very hush-hush meeting on gold. The Europeans were much more gold oriented in philosophy than the United States. The United States was gold oriented more by systemic requirements, but the Europeans took the role of gold more doctrinally serious. Thus, to budge the Europeans to make an adjustment in the way the gold standard was operating at that time was difficult. Looking now at this small particular adjustment agreed to at that March 1968 meeting at the BIS, one would think that it was a nonevent. But with that adjustment, the role of gold in the international monetary system started to unravel and, subsequently, to diminish significantly. It was one of the last salvage operations to maintain the post–World War II exchange rate system.

There were previous episodes with strong pressure on the dollar. In 1961, this was resolved by the revaluation of the DM (deutsche mark) and the Dutch guilder. There is a strange thing about exchange rate relationships: A 5 percent depreciation of the dollar is equivalent to a 5 percent appreciation of a lot of other currencies. And if one deals with only a few major currencies, if an exchange rate adjustment is necessary, it makes no difference if a few of the major currencies appreciate versus the other countries or if the other few major countries depreciate. It's a seesaw relationship. But policymakers prefer that the weak party facing downward pressure on its currency—I guess because it is the country that needs the adjustment—takes the exchange rate adjustment action, leaving the strong party to be the passive recipient.

But the United States, being not just at that time probably the weak party because the pressure was on the dollar, given its role and status and for other reasons, decided that it would be better for Germany and Holland, or other countries that had upward pressure, to appreciate. Germany and the Netherlands did appreciate their currencies to remove the pressure off the dollar. The appreciations happened before I arrived at the Board, but they were often cited in IF as an example of the success in maintaining the post–World War II fixed exchange rate regime.

In reality, these efforts to maintain the prevailing exchange rate arrangements were only patchworks. The frequency of recurring foreign exchange and gold market crises suggested that there were fundamental flaws with the fixed exchange rate system. From the time I arrived at the Board in mid-1967, the IF staff became increasingly involved in analyzing the recurring periodic pressures on key currencies and on gold. The sterling devaluation took place soon after I arrived, in the fall of 1967. The fixed exchange rate system was slowly eroding, and patchwork solutions were adopted, including balance of payments assistance packages arranged on the sidelines of

WP3 meetings. Except for those who carried a deep-seated, ideological view of the role of gold in the international monetary system, the gold standard issue was not really the focus of the discussion—it was the sustainability of the fixed exchange rate regime of which the gold standard was an anchor.

The United States was much less committed to having gold play a central role in the operation of the international system. That's why, in the 1960 elections, when President John F. Kennedy said something about gold in some off-the-cuff remark, all hell broke loose in financial markets, because many market participants were still viewing the world from a gold standard perspective. In the United States, gold was not a major public policy issue because U.S. citizens weren't allowed to hold gold. Thus, for the United States, the role of gold became more of an academic issue. Nevertheless, gold price pressures were reflected on exchange rates and vice versa.

MR. SMALL. Did the dominant pressure against the dollar simply come from U.S. domestic inflation, or was it more involved?

MR. SIEGMAN. It was more involved, because the reconstruction of Western Europe and Japan after World War II made these countries initially import heavily, resulting in large trade deficits primarily vis-à-vis the United States. When these countries were on a buying spree, they did not have enough dollars to cover their import expenditures. As part of the Marshall Plan, the United States provided financial assistance to Western Europe and Japan to help them cover their trade deficits. After a while, the reconstruction effort restored these countries' production and export capacity, and these countries became more competitive. As a result, the shift in the structure of these economies became more normal. But the post–World War II international monetary system had a bias, in some sense, for a dollar-based system, which was perhaps appropriate in the immediate years following the war, but less so in an increasingly more competitive world.

Interest rate and inflation differentials are also important in affecting exchange rate relationships. At that time, the inflation differentials were not huge. It was not one country having an annual inflation rate of 2 to 3 percent and another country a rate of 8 percent, which would show up quickly in countries' competitiveness. We were talking about a 1 to 2 percent a year differential. Such differentials take time to show up as pressure on exchange rates, but, cumulatively, they do.

MR. SMALL. You mentioned briefly the actual going off the dollar and allowing public holdings of gold—I think going off gold in those types of holdings.

MR. SIEGMAN. The collapse of the fixed exchange rate regime, leading up to the Smithsonian Agreement, was preceded by a series of foreign exchange market crises.[1] There were a number of financial crises in industrial countries and financial markets, resulting in the closure of markets and the suspension of foreign exchange trading. Closures of markets are one of the worst things for a financial system to deal with. Disruption of commerce, problems with commercial contracts, stranded tourists, and closed financial markets paralyzed the functioning of economies and world trade. One couldn't get dollars, couldn't get marks, couldn't buy anything if one were abroad and did not have local currency.

In most instances, the financial crisis ended temporarily with some changes in exchange rate relationships. Recurring crises, however, led to speculation about which currency would be next on line to face market pressure. Market speculators then tested whether the currency under

[1] The Smithsonian Agreement of 1971 ended the fixed exchange rates established at the Bretton Woods Conference of 1944. At that conference, an international fixed exchange rate regime was established in which currencies were pegged to the U.S. dollar, which was based on the gold standard.

attack could withstand the pressure on its exchange rate, and rumors of a pending exchange rate adjustment became self-fulfilling. It was not only the dollar that faced exchange rates pressures. Markets were focusing on interest rate and inflation differentials, and certain countries were more vulnerable than others because of political problems.

In 1968, while I was on detail in Basel, we lived right at the border of France. People were coming through our backyard, effectively, with satchels of currency, and perhaps gold, asking us where a particular bank in Basel was located. At that time, France had riots and weak economic indicators, so people were very eager to find ways to protect their assets. Market uncertainties became part of life challenges at that time.

The American public, being less internationally oriented even on the industrial and trade side, was much more relaxed than Europeans about the recurring crises, except if one happened to be a tourist or made a major foreign trade contract at that time. The exchange rate problems were not immediately reflected on American markets and in American behavior; at times, the problem wasn't even highlighted in newspapers. In contrast, being more exposed to foreign trade, all over Europe the concerns about exchange rate uncertainties were evident.

Those were the environment and financial conditions people had to contend with in 1968, 1969, and 1970. When these financial crises recurred more often, the system became increasingly unsustainable. All of this led to major collective realignment of currencies under the Smithsonian Agreement, and the fixed exchange rate regime was formally abandoned.

Relationship between the Federal Reserve Bank of New York and the Board on International Matters

MR. HENDERSON. Can you comment on the relationship between the Federal Reserve Bank of New York and the Board on international matters?

MR. SIEGMAN. The relationship between the Federal Reserve Board and the Federal Reserve Bank of New York (FRBNY) changed significantly in the 1960s, reflecting the shift of power between states and the federal government that manifested itself in the United States. After World War II, more key policy decisions dealing with world relationships were channeled to Washington. State governments became focused on local issues.

Before World War II, the FRBNY was a powerful player and voice in domestic and international financial policy. Before World War II, the FRBNY was probably either equal to or more powerful and influential than the Board in international financial matters by default (with the Board often assuming a sideline role) or as a result of the FRBNY's operational activities (for example, handling gold accounts of foreign central banks). The FRBNY was often the main spokesman for the Federal Reserve at BIS meetings. It set the tone and had ongoing dealings with other central banks.

But as the rest of the U.S. government became more centralized, the Federal Reserve Board asserted its role, and it became much more appropriate for the Federal Reserve Board to represent the United States in international fora and to be the spokesman for the Federal Reserve. When the United States started becoming involved in arranging financial packages, for example, it had to deal with other foreign governments. It's not appropriate for a regional bank, even if it is the most important regional bank, to represent the United States in meetings or negotiations with finance ministries and central banks of Germany, France, or the United Kingdom. So the Federal Reserve Board became the counterpart for the Treasury, as was the case for other countries.

In the early years of this transition from having the Federal Reserve Board regaining and assuming its prominence in the System vis-à-vis the FRBNY, in some areas the FRBNY continued to lead. For example, the swap network was negotiated by Charles A. Coombs, who was a senior vice president for foreign exchange markets at the FRBNY. Coombs represented the Federal Reserve when he negotiated the swap network in the BIS setting and was very effective. Eventually, the representation role for the Federal Reserve shifted to the Chairman or to the Governor attending BIS meetings, supported by a senior Board official (Bob Solomon when he was the IF division director and adviser to the Board and, subsequently, by the IF director or other IF senior officers). This shift from the FRBNY to the Board led to some tension, because someone's role was being diminished and someone else assumed the role of being the lead representative of the Federal Reserve System and its spokesman. So, for a while, there was dual Federal Reserve representation at the BIS. The Chairman of the Federal Reserve Board and the president of the FRBNY, or their representatives, both sat at the table in the seat designated for the United States. It was unique; it was the only country that had two seats. By the time I retired in 1998, there were still two seats at the table for the Federal Reserve for some of the BIS meetings and BIS committees.

On other international matters, especially those that involved coordination with the U.S. Treasury (for example, foreign exchange intervention, reform of the international monetary system, international debt problems, and supervision of international banking), over time a division of labor evolved, with the Board setting policy and the FRBNY handling the operational implementation as appropriate.

Progression toward Flexible Exchange Rates

MR. SMALL. I'm curious about this progression toward flexible exchange rates. At the Board, new economists were coming out of graduate schools with new theories, some research sections were conducting purely abstract research, and new Governors were coming in with new ideas. Was there an old guard/new guard dimension? Was there a modernist Keynesian?

MR. SIEGMAN. Around the time that the exchange rate regime was moving from fixed exchange rates to managed floating or floating rates, it was fortuitous that the composition of the IF staff was changing, with an influx of staff with strong analytic training and the retirement of a number of staff with considerably less formal (modern) economics training. Had the changes in the exchange rate regime occurred 10 years before it actually happened, there would have been much more staff resistance to analyzing both sides of the issue or even leaning toward accepting managed floating and, eventually, floating exchange rates, because the staff's whole professional career had been in an environment of fixed exchange rates. Given the changes in the backgrounds of the division staff, the shift in the division of analyzing exchange rate relationships from a system of fixed rates to that of floating rates went rather smoothly. The division, thus, was well positioned to handle the change in the exchange rate regime.

To be fair to the people who we've labeled as "old guard," either out of practicality or out of intellectual honesty and acceptance of the new reality, nearly all of the senior staff members were eventually forceful spokesmen and advocates of floating exchange rates. Some staff [members] who had argued on behalf of maintaining the fixed exchange rate eventually understood and accepted that the world was changing, and they were catching up with that intellectually as well.

The more recent staff arrivals were younger and much more intellectually prepared to analyze the world economy operating with floating exchange rates and to make the case for the move to managed floating rates. The Chairman and Board members were provided with analysis and briefings on floating exchange rates, thereby allowing them to make informed policy judgments in the new world of floating exchange rates. While the old mentality of some Board members and some of the older staff was being undermined by the changes in the exchange rate system, the realization that the old system was not working, plus the quality of the analysis of the new regime by a number of the staff members, led to a better understanding of the issues that made the Board and the division as a whole reasonably accepting of the new regime.

MR. HENDERSON. Was Bob Solomon an example of someone in the old guard who favored floating rates?

MR. SIEGMAN. Yes, definitely. He made that shift operationally within the Board and in representing the Board. There was no friction or resistance to the changes in the system as the issues evolved. As the breakdown of the Bretton Woods system was being discussed and analyzed, there were legitimate debates on how the system should be dissolved, the design of the new replacement system, what elements should be tossed out, and how much baggage would be left once you have cleaned house. There were all sorts of internal discussions at the Board about the new system being proposed and discussions with the U.S. Treasury and among central banks. The IMF started assuming an active coordinating role in these discussions.

Being a participant in the intellectual ferment of the issues associated with the changes being proposed in the international monetary [system] was quite exciting. One was not labeled if one made arguments for maintaining the fixed exchange rate system or favoring only limited and managed exchange rate flexibility. There was never a dividing line between fixed‒exchange rate staff and flexible‒exchange rate staff. There was a lot of younger staff who had already been exposed in graduate school to the analytic debate about exchange rate system options. IF had very few staff [members] from the Chicago school of economics that advocated allowing markets to determine exchange rate relationships, but there were definitely free floating exchange rate–type people in the division. Most of the Yalies, who had the reputation of being post-Keynesians and saw the virtues of flexible exchange rates, also recognized that, under the circumstances, the move to such an exchange rate system had to be done thoughtfully in order to gain wide acceptance by the markets and the public.

In the intellectual debates on the appropriate exchange rate system, there were some at the Board and in academia who maintained that perhaps the exchange rate problems that the world economy was experiencing were just transitory. They contended that, because the system was not working, it was necessary to suspend temporarily operating under the fixed exchange rate rules. Once exchange rates were stabilized, they argued, countries could/should go back to more fixed exchange rate arrangements. Those who advocated those positions proposed target rates and a type of regime that doesn't allow large exchange rate fluctuations and volatility.

I am not going to make any judgments whether those who favored going back to some form of fixed exchange rates were those who were inherently fixed exchange rate people or not. I don't want to attach motives or intellectual roots to their position. But very respectable economists made arguments at the time that it would be desirable to avoid or minimize fluctuations in exchange rates that flexible exchange rates could generate, and, therefore, they advocated adopting an exchange rate system that had elements of the previous fixed exchange rate system but also some built-in flexibility when necessary—for example, moving-target rates and the like.

MR. SMALL. Was there a development in the research function within IF or the modeling section or other functions that played into this? Did it support both sides of the argument or have any impact at all?

MR. SIEGMAN. In general, the research function in IF was impressive. When I came to the Board, given that I'd been in academia for a number of years and regarded myself as a continuing academic, I needed a break from academic work, because I was getting potentially in a groove. You could wake me up in the middle of the night and I could comfortably tell you my lecture on certain issues like flexible exchange rates and fixed exchange rates and the jokes/anecdotes about them. In the early years of college teaching, for my personal professional growth, I mastered, absorbed, integrated, and transmitted the professional literature—in particular, in the field of international economics. But after a while, I usually read one or two new articles in preparation for class lectures or seminars.

I was interested to see how the policy world works. I would have discussions with friends about either taking a leave of absence and going to the Board or the IMF for a year or actually becoming a staff member. I was advised to become a staff member, because that allows one to assume some responsibility and to work on the inside. If you are a visiting faculty member on leave, you arrive in September and leave sometime during the following summer. If midway of your leave you are working on a project, you are unlikely to be asked to work on another significant assignment, since you are not likely to finish the new project.

So, when I came to the Board in 1967, I made a mental commitment to stay for one or two years. I was fortunate that the issues being addressed at the Board when I arrived were very interesting. Had I come four or five years earlier, hardly anything of significance was happening in the international economy except the 5 percent revaluation by Germany and the Netherlands that I mentioned earlier. But when I came to the Board, year after year, major developments in international economics were taking place that merited detailed discussion and analysis in international economics books being written in that period. Now most of these developments have receded in importance and have been relegated to paragraphs or footnotes in the professional literature.

One of the significant international economic issues of the time was the exchange rate item mentioned earlier. There was extensive academic literature about floating versus fixed exchange rates—Milton Friedman versus Henry Wallich and others who made the case for floating or fixed exchange rates. In one of my seminars at Swarthmore, I had the students write papers. One topic was the case for floating exchange rates versus the case for fixed exchange rates. This is going back now to 1963 or 1964, less than 10 years before the Smithsonian Agreement. I remember vividly these nice young undergraduates. One presented the arguments for fixed exchange rates under certain conditions and assumptions, and another presented the case for flexible rates under different conditions and assumptions. Had they switched the conditions and assumptions, they would have had to accept the other side's arguments. If there are stable market conditions and low inflation, it makes little difference if you have fixed exchange rates or flexible exchange rates.

When I came to the Board, a lot of thinking on the exchange rate issue and other important international economics issues was taking place in IF. Many of the staff had been exposed to the academic debate on these policy issues and had read the professional literature. A number of staff members had made substantive contributions in their published research on these subjects and by their attendance at outside conferences and Board seminars given by outside experts and IF staff members. So there was an air of intellectual excitement about these issues among the staff. The discussion on the foreign exchange issue was on a higher level than just that there is a balance of payments problem the United States is facing and what should/can be done about it. Having to view and analyze the functioning or nonfunctioning of the prevailing exchange rate system at the Board made the academic literature that I had been teaching come alive for me.

Move to Elevate Staff Research

MR. SMALL. Do you think there was an explicit decision to bring in more outsiders, elevate the level or amount of research, or make the analysis more formal? Was there a sense that the staff's formal analysis presented to the Board needed to be strengthened to help this debate?

MR. SIEGMAN. IF had a very effective recruiting process. The division would look for people to fill gaps or to complement people who were in need of certain analytic skills or background. The division did not hire foreign exchange specialists to work on how a fixed exchange rate system might work better or how it operates. Instead, it typically looked for well-trained international economics, monetary policy, and macroeconomics economists with analytic or empirical skills and knowledge.

The Board had academic consultants come in three times a year. Periodically, the academic consultants focused on international topics, with the functioning of an exchange rate system being one of the topics. Many staff members had good contacts in academia, some who were leading figures in the economics profession, from graduate school or from the institutions where they had taught. They thus were able to bounce ideas [off of] their contacts on topics they were working on or send them drafts of their research work.

MR. HENDERSON. But wasn't an intent to give more weight to doing research evident in elevating Ralph Bryant to division director?

MR. SIEGMAN. Yes. When Ralph Bryant became the division director, a general generation shift was already under way. Because Bob Solomon had a rich intellectual mind, he was groping with some of the issues being addressed in the division from his own analytic framework and drawing upon staff who had a more formal, analytic approach to these issues. He worked very closely with Ralph Bryant. He gave Ralph a lot of exposure and responsibility and more or less groomed him.

When Ralph became the division director, given that he was younger and more research oriented and he wanted to keep his credentials and intellectual capital intact, the division made a large jump into encouraging more academic research than before. It came at the right time, because when analyzing the impact of changes on trade, activity, and prices resulting from changes in exchange rates in the new floating exchange rate system, it could get a little dizzying if one is trying to measure the impact of the changes in these variables on the global economy and getting a netting effect both for your country and for other countries. So having an integrated international model was very helpful.

A model was less called for after World War II, since the conditions prevailing were quite obvious. There was a weak, war-torn set of countries that needed to reconstruct and that needed financial assistance to do so. The Marshall Plan was established to provide and allocate the assistance in an organized manner. Production needed to be restored, and financial systems needed to be reestablished functionally. A multicountry model would not have told one much because the coefficients were shifting right in front of you.

When I arrived at the Board, I was impressed by the research being done in IF, and it became substantially richer and of a different quality over time. The research function of IF became more defined. When new staff members were hired, they wanted to know up front what time they would have to do research. Once new hires were given a specific proportion of their work assignment to do research. For equity purposes, others on the staff were given equal research opportunity as well. The enhanced focus on research made the division become intellectually more alive. In addition, the good research environment in the division was helpful in attracting highly qualified young economists, including those who wanted to come to the Board for X number of years and then return to academia, since the environment was conducive for young economists keeping their academic credentials.

MR. SMALL. Was any of that development driven by the Board members, in that they asked for it, or simply that new Board members could understand the formal analysis better, and therefore they were an appropriate audience?

MR. SIEGMAN. The Board composition in my time was pretty diverse. Excluding the Chairman, some of the Governors came from academia—for example, Governor Henry C. Wallich, Vice Chairman David Mullins, and Vice Chairman Alan Blinder. Some of the Governors had master's degrees, and several were businessmen. Those Governors who were not professional economists, even if one expressed one's memos and briefings in layman's language, had a handicap dealing with arcane matters of monetary policy—the "Ms," the monetary transmission mechanism, and the like. For some, once one starts presenting memos with equations and model results, their eyes glossed over, in part because they didn't fully understand some of the technical matters.

Come budget time and even at Board briefings, there were periodic noises from some Governors that perhaps IF was becoming too academic, too "egghead." In the end, the Chairman and other Board members would endorse the need for the research program, even those Chairmen who did not necessarily appreciate models and sometimes mocked the model results and who preferred judgmental forecasts. Intuitively, both for staff retention and for the reputation of the institution, they felt that research was a necessary ingredient in the division's work program.

At the same time, the Board became a patron of the arts by supporting a considerable amount of research that didn't have a direct or even an indirect relevance to the formation of monetary policy. Some of the topics some of the staff wrote about raised questions about, why is someone in IF working on these issues? What does the Board or the division gain from such research beyond, perhaps, brain sharpening?

The approval of the division's annual proposed research program by division management and the Board was not a foregone conclusion. Some proposed research topics were questioned by division management because, at budget time, when the division director presented the research program to the Board, he/she had to answer why division staff members were writing about some esoteric topic at the Federal Reserve Board. On the whole, however, during the budget process and at other times, the Board was supportive of the division's research program.

Periodically, when certain Board members from academia joined the Board, they asked [the] staff to conduct certain studies of an academic nature on issues with which they had been grappling or were interested to have explored, with some of the research results appearing as coauthored articles in the professional literature.

MR. HENDERSON. Do you think that starting the model in the domestic division, the Division of Research and Statistics (R&S), made it easier to start one in IF?

MR. SIEGMAN. Definitely, even though questions were asked about the justification of the division to devote significant resources to develop a multicountry model. Given that the

Board already had a U.S. model, why doesn't R&S just add the balance of payments and perhaps the exchange rate variable into the U.S. model and leave well enough alone?

One needed quite a bit of breakthrough with the rest of the Board on the idea of developing the multicountry model. I remember that Professor Lawrence R. Klein from the University of Pennsylvania came and made a big pitch for the Board to do this, claiming that the Board's other models were too narrow in scope, and that there was a need to get the interrelationships better formulated. Because a domestic modeling group was already in operation, one had to make a case why IF had to do it. It turned out to be a well-received model in the academic community. They even had a National Science Foundation evaluation of the model that was complimentary.

So the multicountry model was one important area of division research. On the whole, the range of research subject output at the Board, both international and domestic, was impressive.

Impressions of Governors and Board Staff and Changes at the Board over Time

MR. SMALL. Looking back, has the day-to-day feeling of being a staff member changed under the various Chairmen, or were there other factors that affected changes? Are there some instances that reflect how different the Board is now versus in earlier years?

MR. SIEGMAN. It is different now because of all of the security after September 11, 2001. It's very noticeable when one comes to the Board now. The security has inched up over time, but it was never as intensive as it is today. Fortunately, I did not have to experience this. It was a freer environment, in the sense of movement and dealing with people—welcoming visitors and all of that.

When I applied for a job at the Board, I also had interviews at the IMF and the World Bank. Lucky me, I received offers from all three. I have been asked why I chose the Board over the others. Three things made me lean toward the Board over the others. First, going back to 1967, both the IMF and World Bank were very formal compared with the Board. People there were dressed quite formally (dark suit and tie were the norm), ready to attend a wedding or a funeral if necessary at a drop of a hat. I'm perhaps exaggerating, but the point is, the working environment at the IMF and the World Bank at that time was formal and stiff, and it took on a certain lifestyle. There were many Europeans, Asians, Africans, and South Americans at the Fund and the World Bank, with many of the more senior staff having served in high-level positions in their governments. People at the Board dressed properly, but it was less formal. At the Board, many people wore sport jackets. I was used to wearing a sport jacket at Swarthmore. I think the dress code at the Board today is even more casual.

Second, the interview process at the Board was more democratic. At the Board interview, I dealt more with the staff and not just the officers or section chiefs. At the IMF and the World Bank, it was very hierarchal; I was interviewed only by senior staff.

Third, I had the impression that, at the Board, I would have the opportunity to make, overall, fuller use of my academic background. I had the sense that, at the Board, one was able to quote professional articles and to read articles without being "ashamed" of doing so. I was told it was not expected or even appreciated to be too analytic at the IMF (and even more so at the World Bank) except if one was working in the Fund's high-quality research department. The feeling was that the Fund was not meant to serve as an academic institution. I was told by the Fund that, if I would accept a position in one of the Fund's functional departments, I could get a research position once an opening would become available in the Fund's research department.

So when I had to write the letter of acceptance or decline to each of the three offers, I hesitated. Was I making a mistake in choosing the Board? The IMF had a good, but different, reputation than the Federal Reserve. The IMF was more "glamorous" and paid more.

Anyway, I came to the Board, and, in retrospect, I was vindicated personally. I made the right choice for some of the reasons I just mentioned. The Board was different than being in academia. It was a 9-to-5 job, versus a few hours of lectures a day and armchair time otherwise. It took a little getting used to, but the work environment was attractive for a former academic. And, as I mentioned, the issues that came to the forefront, and in which I became involved or was a sideline participant, were interesting. Issues that I used to talk about in the abstract in academia now were happening in front of me.

One of the test questions I used to ask my students in international economics was on the fixed exchange rate: "Pretend you're a minister of finance, and you have to change the exchange rate. Why is it necessary to change the rate, and what percentage devaluation (or appreciation) do you choose—5 percent, 10 percent, 50 percent—and how do you know whether it is enough?" Soon after I started working at the Board in 1967, we had the same questions with the devaluation of the pound sterling and, even more complicated, when the Smithsonian agreement came up in 1971, involving a multilateral realignment of exchange rates. How much exchange rate adjustment was needed in those cases? But here it was not a theoretical question, but of practical significance. In dealing with these exchange rate adjustment questions, I was making use of my intellectual and educational capital and enriching it from different perspectives by having to address practical policy-solving situations. It was a work culture that appealed to me.

My colleagues on the whole were good economists, and some were of exceptionally high professional caliber. The Board is not an institution without warts, without blemishes, or without people who are not necessarily fully professionally qualified for some of the analysis done at the Board. But, over time, this was a pretty stimulating place to be, and I don't regret in the least having come to the Board for a rewarding career of over 30 years.

As I moved up to more responsible positions, I was impressed that the Chairman and the other Board members worked with the staff rather than having executive assistants who ran their offices, who were their preliminary filters of ideas, who assigned work to the Board staff, or who did the work themselves. The Chairman did not have a clerk, like Supreme Court Justices do. He sometimes had an administrative assistant, but that person did not do the work or call the shots. There is contact between the Chairman and the Board members with the staff, through division directors and other senior officers or staff.

The staff having access to Board members, Board members having access to the staff on an individual basis, and [the] staff attending Board briefings is rather unique in executive branch government organizations and in other central banks where it is not common for a wide range of the professional staff to have direct contact with high-level officials or for staff members to sit in at board meetings. Not everyone attends Board meetings, but, on a need to be there, it's pretty open.

And the Chairmen, each in his own way, depending on their own style of how they want to draw upon staff, rely heavily on staff. In the case of IF, the Chairman often calls in the division director or someone else to ask questions, probe, and issue a call for some work to be done. When I was called upon to be directly involved, it was challenging—sometimes too challenging. Not having a layer of staff between the professional institution staff and the Chairman's or Governor's office makes for a positive working atmosphere, but one wants to make sure that the information provided reaches your principals. One has no control over whether or not they read the material provided to them, and quite often they did not read memoranda that staff [members] worked hard on, but very often they did. If Chairmen or Governors did not read material, it was not because some assistant in their offices filtered the material sent to them, deciding that it is not necessary for them to read it, which is very common in other government departments.

Being able to participate at Board briefings and hear the discussion between Governors and the questions that they pose to each other gives one a flavor of what's on their minds, what's missing in their information base, and what would be helpful for them in the future. By having contact with the Chairman and Board members, [the] staff gets the feeling that they are not working in a vacuum. [The] staff should not necessarily cater to the biases of the Chairman or Board members, although sometimes some staff members do. But having contact with the Chairman and Board members or seeing them at Board briefings, one at least gets a sense where one thinks one could offer some enlightenment and broaden their understanding of issues. The staff getting to know the Board members and the Chairman and other Board members getting to know the staff leads to a dialogue and a personal relationship that is rather unique at the Board.

Each Chairman has his own interests. Some need more or want more staff work and are more probing. But, on the whole, most Chairmen and Board members with whom I've dealt work very hard themselves. They receive an incredible amount of material—sometimes perhaps too much material. One shouldn't expect them to read everything. It is impossible for them to read everything that is sent to them, although he or she may have asked for it. I'm very impressed by how much they do read and absorb. This is noteworthy, because some of the Chairmen and Board members, when they come to the Board, did not have a specialization in monetary economics and/or in international economics. They had to learn much from scratch.

As I mentioned earlier, the Governors had diverse backgrounds. Some had very little background in monetary policy or international monetary economics. Some were appointed for political reasons or for their diverse private-sector expertise and experience. To deal with these diverse backgrounds of members of the Board, a number of Governors were assigned staff people to "tutor" them. I and other IF staff [members] used to go to their offices once a week to talk about different issues in order to bring them up to speed. Even those Governors who were outwardly cocky and even arrogant (even at Board briefings) were exceptionally meek in one-on-one sessions. They would ask innocent questions and preface them with, "I really don't know what it's all about. Tell me, what does this technical term mean, or what does this issue really mean?" I think J. Charles Partee, before he was appointed Governor, initiated these information briefings.

Governors were informed that personal briefings were available, and the Governor had to ask for a briefing. For some Governors, we had an outline of issues to be discussed—like a course outline with reading material. Some read selected items for "homework." That this existed was a healthy sign that the Governors, especially new appointees, wanted to come up to speed and make better decisions and participate in the Board or FOMC discussion and debate. That is a very positive work environment culture. Whether it's unique to the Board, I cannot say. But it's not standard, I know that much.

Attending International Meetings

MR. SMALL. Over the years, a large part of your responsibilities involved attending various international meetings. What is your perspective now on whether the functions of those meetings, the structure, and the objectives have changed over time?

MR. SIEGMAN. I participated in quite a few international meetings. I was blessed that Ted Truman, in his capacity as division director, participated and represented the Board in many more meetings than I, because preparing for, attending, and reporting on meetings could be a full-time job. Probably, there is an excess of international meetings taking place at the expense of wear-and-tear of senior policymakers and supporting staff. It was inappropriate for the Board to be represented at these meetings by junior staff. You have to show your face at a similar level to that of other countries!

In my early years at the Board, the major meetings that the Federal Reserve attended were those at the OECD and the BIS. Those organizations had a schedule of meetings for the year. In the 1970s, meetings of the OECD's WP3, attended by relatively senior treasury/finance ministry and central bank officials from the major industrial countries (the Group of Ten countries), often were operational. They dealt with pressing policy problems facing individual countries and didn't just have a discussion or analysis of a "major study"—for example, on the adjustment process under fixed exchange rates. The operational aspect of these meetings was, as noted earlier, to arrange financial support packages for those countries that were experiencing balance of payments/foreign exchange rate pressures. At some of these meetings, discussions were held to enlighten and eventually coax others to adopt better macro policies. The WP3, however, was not a policymaking/decisionmaking group.

The OECD also had an Economic Policy Committee (EPC), represented by treasury/finance ministry/Council of Economic Adviser and central bank officials of all OECD member countries, which was a talk fest about economic policy and economic conditions in the OECD member countries. The discussion at EPC meetings typically was general and not analytic. A member of the Council of Economic Advisers usually represented the United States at EPC meetings and often was the chair of that committee. The Federal Reserve was represented by a Governor, joined by a staff member, and played a background role at these meetings. The Federal Reserve representative's principal task was to review U.S. monetary policy developments and listen for the rest of the meeting. If the designated Governor was overburdened and had to cancel attendance at the last minute, [a member of the] staff represented the Board at the meeting. That happened more than once.

The EPC meetings were talk fests, because too many countries—22 countries in my time—attended. And each one, even the smaller ones (for example, Finland, Iceland, Ireland), felt obligated to review their country's economic conditions and policies. Many of the presentations were read from prepared texts. Rarely anything of substance was raised that was not already known. Once in a while, the discussion was put into the broader framework—for example, comparing the OECD forecasts with those of the IMF.

As an international institution, the OECD did respectable analytic cross-country and institutional studies, which were helpful in documenting events and comparing and analyzing the performance of different sectors in OECD countries. But the EPC meetings were second-order significance for the Federal Reserve. WP3 was more substantive for quite a while. Lately, I think, they have become less so.

In the early post–World War II years, the OECD played a role to get the Marshall Plan off the ground, and it played a useful role in keeping the fixed exchange rate system in place. Subsequently, it has become more of a discussion forum. Every so often there are discussions to streamline the number of international organizations that deal with macroeconomic policies and issues, and the possibility of disbanding the OECD has been raised, but, in the end, the OECD has been given another lease on life.

The BIS, on the other hand, is an active central bank club meeting forum. It played an increasingly valuable role over time as Europe reconstructed and became an important economic entity as it started moving to a unified and integrated European entity. The BIS—being a European-based institution and heavily weighted by European membership—had a European bias, orientation, and focus. The Federal Reserve, although influential, was, in some sense, a partial outsider, since it was not part of Europe.

Although the Federal Reserve attended the monthly meetings of central bankers and meetings of bank supervisors and payment system experts at the BIS, for a long period the Federal Reserve was not a member of the BIS. The Federal Reserve didn't become a member until 1994 for peculiar reasons. I was involved in working on the BIS membership issue for many years. I inherited the issue of why the Federal Reserve was not a member, whether it should be a member, and how it could become a member. Every four or five years, there was a Board meeting to discuss the BIS membership issue, and each time the decision was to reconsider the issue at a later date. After the case was made that membership was overdue, the Federal Reserve eventually joined in 1994.

The BIS holds 10 monthly meetings of central bank governors of the G-10 countries a year. Because the tenures of central bank governors are much longer than those of treasury officials, there is a rapport and personal relationship among central banks that does not exist among treasury officials. Even though some of the European central bankers were quite formal, given the frequency of personal contact, phoning one's counterpart at a central bank to convince him/her to do something was much more effective than a treasury official calling his/her counterpart who had assumed his/her position a month or so ago and who one had not yet met. The ongoing personal relationships among central bankers was especially valuable when dealing with immediate systemic problems such as exchange market instability or international debt problems, or if there was a bilateral central bank issue when one could smooth things out directly and fairly promptly.

Having this ongoing dialogue among central bankers allows them to resolve issues and reach an understanding on matters that affect them all. Many of the staff members that attended meetings at the BIS and other international meetings representing the central bank had even longer relationships than governors—quite often 20 to 30 years of working together in different positions at their respective central banks. The close working relationships central banks and their staffs have developed are tremendous assets when important issues requiring central bank cooperation arise.

The long tenure of independent central bank heads also served countries with unstable governments. For example, in the early post–World War II years, Italy had one or two new governments every year. Eventually, the governor of the central bank, the Bank of Italy, became the most influential policymaker in Italy because he could represent his country at international meetings with some continuity, compared with a finance minister who had just assumed office and was likely to be out of office within a month or two.

At BIS meetings, the economic and financial situation is reviewed and updated from month to month, thus keeping all attending parties informed, similar to what takes place at FOMC meetings. But, in contrast, the BIS is not a policymaking/decisionmaking institution. Over time, the BIS became the forum for international dialogue on bank supervision matters, payment system issues, and other functional financial system questions where discussion of proposals on how to structure certain financial policies were made—for example, capital adequacy ratios and the like.

While agreement on financial-sector standards and the like aims at developing a consensus, it is not achieved by getting the lowest common denominator but by forging a common denominator without ramming things down people's throats. This is a time-consuming process, sometimes taking years. Although some of the arrangements on payment system or bank supervisory matters are not necessarily perfect, they are improvements over having every country going its own way. In the bank supervision area, for example, one does not want to have nations compete to attract capital inflows or banking business on the basis of leniency of supervision standards.

Originally, the BIS was a forum for getting central bankers under one roof. It benefited much from hosting these meetings very effectively. [The] BIS received a lot of credit as the institution where central bankers meet and where they get things done. Later, some general managers of the BIS took on a more active leadership and visible participatory role. At times, the BIS left the impression that it was coordinating the issues under discussion by central bankers at the BIS. But, in reality, it was central bankers who were coordinating their joint efforts.

Most of the issues discussed and decided upon by central bankers at the BIS were central bank related. They didn't require Treasury approval, but on many issues the Treasury was informed by the Federal Reserve (usually in general terms) [about] what was discussed at BIS meetings. The Treasury, however, was kept out of attending meetings at the BIS. There was one famous case where a U.S. Treasury official appeared in Basel to attend an emerging crisis meeting on the fixed exchange rate, and he politely was told to leave: "You don't belong here. If you have a message, go through your central bank. And if you want to ask us, go through your central bank." The Treasury learned quickly.

Typically, the IF division director accompanied the Chairman or a Governor to the more important international meetings. However, I attended a number of the monthly meetings at the BIS accompanying the Chairman or a Governor. My colleague, Larry Promisel, attended quite a few meetings at the BIS dealing with the operation of facets of financial markets. At the OECD, I attended a number of WP3 meetings; they were considerably more interesting, relatively speaking, than the other OECD committee meetings. But none of them were major policy decisionmaking meetings.

That's one thing about international meetings dealing with economic operations and central bank operations—they are not necessarily addressing a crisis [or a] decisionmaking matter, telling governments or central banks what to do. International cooperation involves dialogue and maybe some arm-twisting through dialogue, but it does not "command" what countries or central banks have to do. The aim of most international meetings is to achieve a consensus. Quite often, there's a communiqué or statement issued at the conclusion of international meetings. Some organizations issue long communiqués, words and words. The less one says publicly about the proceedings of an international meeting, the more one does, and the more one says, the less one does. The BIS typically had no communiqué, unless there was a particular issue on the discussion table where central banks finally agree on common procedures or guidelines to do certain things—then a brief communiqué is issued. Otherwise, central bank officials go to meeting after meeting and conclude that they would meet next month or two months later without issuing a public statement.

With the exception of meetings of central bankers at the BIS, the Federal Reserve had some choice whether to participate in international meetings. At EPC meetings, the Federal Reserve presented an overview of U.S. monetary policy and typically would be quiet for the rest of the meeting. At WP3 meetings, because they dealt more with international policy issues, the Federal Reserve played a more active role.

As the world economy evolved, the IMF started taking a larger role in international cooperation activities, both in surveillance of exchange rates and certain issues on the management and the structure of the international monetary system. The Federal Reserve selected issues for which it felt, or others felt, that the Federal Reserve had expertise or knowledge or that may intrude on monetary policy matters. On those matters, the Federal Reserve took a much more active role voluntarily or by request from the Treasury or sometimes both. On issues that were peripheral to Federal Reserve interests and mandate, although the Federal Reserve had some views, it most often acquiesced to what [the] Treasury decided to do, unless it did something totally stupid or foolish or it raised some fundamental questions. On IMF quota changes, for example, the Federal Reserve was typically passive. Similarly, on the conditions that are appropriate for IMF programs, case by case, the Federal Reserve did not get heavily involved except in cases where the Federal Reserve had strong views. The Federal Reserve let the IMF staff work out the conditionality of its programs, let the executive directors discuss it, and let the Treasury decide whether the conditionality of IMF programs met its criteria for the direction such programs should take. On these IMF matters, the Federal Reserve thus was selective in deciding the extent of its involvement.

On international monetary system issues, the Federal Reserve has been an active partner with [the] Treasury in formulating U.S. policy. Following the Smithsonian Agreement of 1971, the Committee of Twenty was created to develop the blueprint for the international monetary arrangements to supersede the fixed exchange rate system. Chairman Burns, Bob Solomon, and a number of IF staff [members] played very active roles in this exercise. [The] Federal

Reserve's expertise on international monetary system issues continues to be drawn upon to the present.

Throughout the year, the IMF holds several "grand" meetings. The principal meeting used to be that of the Interim Committee and renamed the International Monetary and Financial Committee (IMFC). Twenty-two countries represented at the IMFC meet twice a year. The Secretary of [the] Treasury is the principal U.S. representative. The Federal Reserve Chairman rarely assumes a public role at those meetings. He attends loyally because he represents the Federal Reserve, and, sometimes, if the Secretary of [the] Treasury is not able to be present for parts of the plenary sessions, he represents the United States. The annual meetings of the IMF and the World Bank are limited in substance because all 187 IMF members are represented. There are many general presentations and speeches. The Federal Reserve's main concern at IMFC meetings is what the Secretary of [the] Treasury might say about U.S. monetary policy. What's not said about monetary policy is preferable to what is said. [The] staff prepares documentation for these meetings for the Chairman and offers necessary staff support. The bilateral meetings of the Chairman with foreign officials at the time of these IMF meetings have become the primary meetings for the Chairman.

The annual meetings of the IMF and World Bank and the two IMFC meetings each year are preceded by G-7 and G-10 meetings. The G-7 meeting is attended by finance ministers and central bank governors, not heads of state, of the seven major industrial countries—United States, Japan, Germany; United Kingdom, France, Italy, and Canada—with the ministers of finance and the central bank governors from China and Russia attending parts of the meeting in recent years. The Chairman usually attends the G-7 meetings without staff, but the staff prepares a comprehensive briefing book.

The G-7 typically releases a statement following their meetings. Here, again, a main Federal Reserve concern is to make sure that nothing is said in the public statement about what the Federal Reserve should do, because an underlying objective of the G-7 is to set out the direction [of] macropolicies of key countries and how these policies should be coordinated (with each country eager to see others doing the adjustments!). If there's an issue or an attempt to build a consensus about a functional problem on which the G-7 is focusing at the time—for example, money laundering—the Federal Reserve and Treasury have no problem participating in the formation of a consensus. They are less receptive to being told by the G-7 in its postmeeting public statement what to do on monetary or fiscal policies. The Federal Reserve typically is satisfied if there's no mention of monetary policy in the statement. If it is mentioned, the Federal Reserve would prefer to have U.S. monetary policy described in neutral terms. The Federal Reserve staff involved in drafting the end-of-meeting statement would try to achieve that tone. The staff would also try to make sure that there's some mention in the statement about having sustainable noninflationary growth.

There is also an annual G-7 meeting of heads of state, the G-7 Summit, but the Federal Reserve does not attend. There have been occasions where the Federal Reserve has been asked by the staff preparing the President for the summit to review some of the documentation prepared for the President for these meetings.

The G-7 is important because, in the preliminary meetings of deputies for the formal G-7 meeting, there sometimes is an effort to get a package of agreement on policy changes by the major countries. Country "A" would do so and so, while country "B" would do so and so, et cetera. To the extent that those policy commitments would be addressing issues that should be addressed in any case, getting this imprimatur from the international group sometimes is helpful with legislators. Sometimes it backfires, with legislators arguing that they are not bound by commitments made with foreign officials. So one must be careful not to come back after a meeting and report that the other G-7 countries told us what to do and certainly not make any commitments if such commitments require congressional approval.

The small size of the G-7 allows for a direct and somewhat personal dialogue with counterparts. The G-7 discussions rarely take on the form of negotiation. There is more "negotiating" taking place on developing the text of the public statement issued at the conclusion of the meeting than on what are the focus themes of the meetings! But the give-and-take discussions at G-7 meetings sensitize the participants of the policy concerns of their counterparts. If you are a secretary of treasury with a serious aggregate macroeconomic policy problem, you would be most uncomfortable when your counterparts focus critically on your country's problem at an international meeting such as the G-7. If your country in some sense is the cause of a global problem, you squirm and try talking your way out of it by saying that your policies will be improved within six months. Then, if six months pass and the problem is either the same or worse, when you meet your colleagues whom you see over the year in other contexts as well, that's the maximum discomfort you would like to face.

And this may be a reason—and not the only reason—why, when you come home, you will try getting your critics off of your back. No country is going to adjust its macropolicies because of these meetings if it's against their national interest. But, at the margin, these meetings sensitize policymakers to the nature of a problem. If you can't convince your counterparts in March, you may convince them in September/October. You have to face your counterparts on a regular basis. A treasury secretary may be lucky, given the more frequent turnover of treasury/finance ministers, and a treasury secretary who was under intense criticism for his country's macropolicies sometimes would not have to face his counterparts of an earlier meeting because of new elections, with one or more new finance ministers attending the new G-7 meeting. Because central banks have much less turnover, the Board Chairman often faces the same counterparts at G-7 meetings whom he sees at the monthly meetings at the BIS.

The Federal Reserve Chairman, however, is not usually on the "hot seat" and being criticized for the Federal Reserve's monetary policies. Rarely is monetary policy discussed in terms of what should be done. But at times when volatile exchange rate markets are the focus of discussion, the Chairman and the Secretary of [the] Treasury may be asked to intervene in foreign exchange markets in order to calm markets. Heavy intervention, however, could affect the effectiveness of Federal Reserve monetary policy, and the Federal Reserve thus has a preference to weigh the appropriateness of intervention outside the context of G-7 deliberations.

Forecasts Used in G-7 Policy Coordination Process

MR. HENDERSON. There were actual numerical forecasts being used in this G-7 policy coordination process. Do you know why that process was discontinued?

MR. SIEGMAN. First, as an institution, the IMF felt left out of the policy coordination process. The IMF would have liked to be regarded as *the* international policy coordination forum, but it had no formal role at the G-7 meetings. One of the suggested "solutions" adopted was that, before the meeting started, the managing director of the IMF would give a presentation on the world outlook and on some of the major issues in the international economy without preaching about a policy direction. But, otherwise, the managing director wasn't welcome.

The IMF staff was asked to prepare a global forecast and a policy analysis of where the G-7 economies were heading and how the macrovariables were likely to perform. Over time, the IMF prepared an outlook and forecast document for the Interim Committee/IMFC meetings, the

IMF annual report, and for the IMF's World Economic Outlook paper. The IMF outlook presentation at the G-7 meetings couldn't deviate from what had already been published. In the end, the main value of having the IMF outlook forecast was that all governors and finance ministers attending the G-7 meetings had a common outlook document to which they could refer in their discussion.

MR. HENDERSON. I had the impression that some countries had more responsibility for signing off on those reports made for the G-7 than they did for the ordinary forecast. Is that right?

MR. SIEGMAN. Indirectly, G-7 attendees had a little more assumed responsibility for signing off on the IMF outlook forecast unless they wanted to take issue with it, since they were attending the G-7 meeting. But the G-7 meetings, often held at the Blair House, are relatively brief, lasting three or four hours—unless there were contentious issues on the table. Those attendees who had flights scheduled wanted the meetings to end by a certain time. If attendees were to get involved in the nitty-gritty of the forecast, it would be at the expense of the policy dialogue, so discussion of the forecast often was cut short. But given that the IMF forecast served as a common reference point, attendees could readily say, "No, we disagree." The discussion by the FOMC is similarly helped by all the attendees having the Greenbook forecast, thereby allowing everyone to refer to the same forecast.

The IMF also wanted to be *the* international organization to formulate policy consistency and coherence, especially since countries that are not members of the G-7 are affected by what is happening in the world economy, and the Fund represented the larger global economy. The Fund had hoped that its forecast document for the G-7 meetings would give it more influence in the policy debate, but, in the end, the G-7 attendees did not give the IMF forecast document much attention or weight.

G-10 Organization

MR. SIEGMAN. The G-10, composed of the G-7 countries plus Belgium, the Netherlands, Sweden, and Switzerland, was formed in the early 1960s to administer the General Arrangements to Borrow (GAB), a supplementary funding arrangement for the IMF. The basic funding for the IMF comes from IMF member country quotas. Member countries facing balance of payments financing strains are eligible to draw multiples of their quotas. There was a fear that if large countries with large quotas had a need to draw on the IMF, the IMF's resources would be drained, leaving little access to IMF resources for smaller member countries should they face balance of payments problems. To prepare for such a contingency, the GAB, a supplementary line of credit among the major countries, was arranged.

Activating the GAB and renewal of the arrangement requires the approval of the GAB signatories. Instead of only scheduling meetings of the G-10 to activate the GAB and renewing the arrangement, regular meetings of the G-10 have been held since its inception around the time of the Interim Committee/IMFC meetings. The Federal Reserve is represented at G-10 meetings by the Chairman or a Governor and supported by staff. Unless the activation of the GAB is on the agenda, there is not much to discuss at G-10 meetings that is not already covered at G-7 and Interim Committee/IMFC meetings. The G-10 meetings last an hour or so, and there is not much value-added gained from these meetings. Discontinuing the ritual of meetings of the G-10, except for renewing the arrangement or discussing changes in the participants, would save time and effort of those spending too much time already at international meetings.

In order to provide the IMF with additional sources of financing, the New Arrangements to Borrow (NAB) took effect in 1998. Under [the] NAB, additional countries to those that participate in the GAB commit to provide the IMF with funds on a prearranged basis. The initiative for this enlargement originated with the Federal Reserve. It was proposed at the time of the mid-1990s debt crisis, when it became apparent that more funds were needed by the IMF, as it started providing substantially larger stand-by arrangements (loans) by approving drawings of higher multiples of members' quota. Given the increase of participating countries involved in the two arrangements—25 in total—called for an annual meeting of all participants, thereby adding to the travel and international meeting schedule of already busy officials. The Chairman, or another Governor, attends some of these supplementary meetings supported by staff.

The G-7, G-10, IMFC, and the annual meetings of the IMF and World Bank—and, typically, preliminary meetings of deputies to set the stage for these meetings attended by principals—meet sequentially in the spring and fall. As a result, senior treasury/finance ministry and central bank officials could be away from their offices for extended periods attending these meetings. In addition, the major central banks have 10 monthly BIS meetings and the annual meeting of the BIS, which is attended by all central banks that are members of the BIS. The Federal Reserve is fortunate that, for some of the meetings, the Governor designated by the Board to deal with international matters can represent the Board, thereby relieving the Chairman from the burden of attending these scheduled meetings and some supplementary meetings scheduled at times of "crisis."

Financial Stability Forum

MR. SIEGMAN. Financial globalization and the development of new financial instruments and financial firms created new challenges for the operation of the overall international financial system. These developments affect the management of international capital flows, international bank supervision, capital adequacy for banks, payments systems, offshore markets, security markets, terrorism financing, and money laundering.

Most of these specialized financial-sector issues fall outside the traditional macroeconomic policy, balance of payments, [and] foreign exchange rate concerns of treasury/finance ministries and central banks and that are the standard focus of international dialogue at G-7 and IMFC meetings. To deal with these international financial system issues, a new high-level committee, the Financial Stability Forum, was formed.

There's logic to have such a forum, because it provides an avenue to bring bank supervisors, security regulators, those responsible for payment systems, and insurance regulators to the table. It is not very meaningful for finance ministry or the central bank officials to discuss these specialized issues and make recommendations about appropriate policies and standards for them if officials of the relevant institutions that are going to be responsible to administer them are not represented. One would expect that the latter have knowledge of what's feasible or what is appropriate in the analysis of the issues related to their areas of jurisdiction. If policymakers want to do something about hedge funds, for example, it would be appropriate to have representatives of the agencies responsible for security markets (the Securities Exchange Commission for the United States) participate in meetings that discuss this subject.

MR. SMALL. Did the capital standards go through that?

MR. SIEGMAN. No, that went through the Basel Committee on Banking Supervision. But how does one deal with these other financial sectors outside the banking system? Some of the specific financial-sector issues mentioned above sometimes are the responsibility of more than one government agency, and there is a danger than oversight responsibility could fall between the cracks.

I have noted that some of the missions of some international organizations/committees may have outlived their original usefulness. At the same time, in the more complex world of financial globalization, there is a need for new organizational structures. The Financial Stability Forum is one such entity needed to focus in an organized manner on these new—and at times interrelated—aspects of the international financial system.

The Federal Reserve has expertise and interest in some of these financial issues discussed by the Financial Stability Forum, especially since a number of these financial-sector issues affect the stability of the international financial system. Therefore, it is reasonable for the Federal Reserve, both on the Chairman/Governor level and the senior staff of several Board divisions level, to be actively involved in the deliberations of the Financial Stability Forum. And it is not surprising that Vice Chairman Roger Ferguson was selected to chair this forum.

Where monetary policy is discussed or central banks are represented at international meetings, the Federal Reserve is going to be there and be counted upon to provide leadership and expertise. But its role and influence on specialized financial system issues differ from issue to issue.

MR. SMALL. Which crises were the most important in spurring the Financial Stability Forum or the most important in lessons learned by the forum or in looking forward?

MR. SIEGMAN. I think it was the realization that there are gaps in the international financial-sector regulatory environment. The bank that went belly up—BCCI—was one case where those who managed the bank exploited the lack of uniform international banking supervision standards. The collapse in the late 1990s of former Vice Chairman David Mullins's investment group (Long-Term Capital Management)—the exponential hedge fund—was another case where it was necessary for drawing in other financial regulatory institutions to provide comprehensive oversight.[2] These huge financial collapses, as well as the realization that the world's capital markets were massive and fluid, had serious implications for the health of the international financial system. They were the stimulus for the formation of the Financial Stability Forum.

Having representatives from the various regulatory agencies representing banking, securities markets, and insurance (for example, participating in discussions on their areas of responsibility and expertise) allowed policymakers to become better informed about the interrelationships of these financial sectors and thus formulate policies to deal with the problems at hand and design procedures to prevent these sectors from undermining the stability of the international financial system.

Role of Federal Reserve in Other Central Bank Development; Independence and Transparency

MR. SMALL. A hot topic is independence and transparency. Over the last few decades, some central banks, such as the Bank of Japan, have gained independence. And we've had new ones created, such as the ECB, the European Central Bank. Did the Federal Reserve have much influence or have a consulting role in any of these particular developments toward independence?

MR. SIEGMAN. During my tenure at the Board, the Federal Reserve played an important advisory role with the transition economies—the former Soviet Union, the East European countries, and China—on development of the structure and the nature of their financial

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[2] Editor's note: David Mullins was one of 11 partners of Long-Term Capital Management, which was founded in 1993 by John Meriwether.

systems, including the central bank independence. Initially, the focus was on assisting these countries in developing the infrastructure for a modern and effective financial system rather than on the development of independent central banks, because the central bank in these countries was viewed as an important political state institution. These countries had their own concept and history of the role of a central bank, and it took time to convince the authorities to modify the operational objectives and functions of the central bank.

When China reentered the global economy formally in 1979 or so, the Federal Reserve was called upon to offer its expertise in advising China on the operation of the international monetary and financial system, including the role and functioning of a modern central bank. The Federal Reserve provided China with a lot of technical assistance, considerably more than what the Federal Reserve offered other countries. The Federal Reserve was helpful in exposing the Chinese to how the Western financial system functions, but it didn't preach on how China should conduct its monetary and financial affairs. We would describe the merits and limitations of a market-based financial system as well as the benefits and nature of certain financial practices, including banking supervision, organized payments system, and market allocation of funds.

Over time, the Chinese benefited a lot from Federal Reserve advice and technical assistance. I was the principal staff contact person with the Chinese, and I had a good relationship with them for many years. Following an exchange of official delegation visits, the PBOC (People's Bank of China) and the Bank of China sent many delegations to the United States, and they called us quite often for assistance and guidance in arranging these visits. Upon request from the PBOC, the Federal Reserve sent different teams of specialists from the Board and the regional [Reserve] Banks for a series of visits to China, and the Federal Reserve encouraged other central banks, the IMF, and the BIS to provide assistance to China.

In 1980, the Federal Reserve and China exchanged visiting delegations. I was responsible for arranging both visits. A group of 25 or so Chinese came to the United States as guests of the Federal Reserve. The Federal Reserve covered all the inland expenses for their visit to the United States, something the Federal Reserve did not do for any other emerging country central bank. It was unique. The Federal Reserve paid for their inland expenses because the Chinese claimed that China was short of foreign exchange. How things have changed since then! Eventually, the Federal Reserve had to set limits on meeting the Chinese requests for sending study delegations to the States for exposure and technical assistance on finance-related matters. The Federal Reserve tried to channel the requests by the Chinese to the IMF, other relevant government agencies, regional banks, and sometimes the private sector.

The visit by the Chinese delegation to the United States, headed by President Li of the PBOC and composed of officials from the PBOC, the Bank of China, and the Agricultural Bank of China, was intended to expose the Chinese officials to the basic institutional and operational features of the U.S. financial system about which the delegation had very limited knowledge. In addition to several sessions with Chairman Volcker and Board members and staff presentations on the structure and functions of the Federal Reserve System and the conduct of monetary policy, meetings were arranged with U.S. Treasury, the Council of Economic Advisers, and IMF officials. Several official lunches with Board officials and senior staff, an official dinner with the Board and officials from a number of U.S. government departments and agencies and the IMF, a cultural evening, and a guided-in-Chinese visit to the Air and Space Museum rounded out the intensive program of the delegation in Washington.

The visit to Washington was followed by visits to New York and Chicago (for which I was the official staff escort) and Houston and San Francisco (for which George Henry, my IF division colleague, was the official staff escort). In these cities, the delegation met with Federal Reserve District Bank officials, learning about the role of regional Banks in the Federal Reserve System. They also met with groups of private banks and financial firms and visited landmarks and sights of interest.

The Chinese delegation's visit to the United States was eye opening for the Chinese in many ways. For most members of the delegation, this was the first time that they had been to a Western country and, for some, the first time being outside of China. The substantive meetings on U.S. and world monetary policy issues and financial-sector matters were big learning experiences, since so much of what the Chinese heard was so far removed from what they were accustomed to and familiar with in China. The U.S. road system, communication networks, electric grids, high technology, and airports to which they were exposed left a big impression on them. Even such items as revolving doors and bank credit cards were viewed with amazement—again, being first-time experiences for most members of the delegation.

The six-person Federal Reserve delegation to China was hosted by the PBOC. The delegation included Chairman Paul Volcker, Governor Nancy Teeters, Federal Reserve Bank of San Francisco President John Balles, FRBNY First Vice President Thomas Timlin, Federal Reserve Bank of San Francisco Senior Economist Hanson Cheng, me, and an interpreter engaged by the Federal Reserve.

The Federal Reserve delegation was one of the first official U.S. delegations to visit China following the opening of China to Western official visitors. The delegation thus received special official treatment. In Beijing, the delegation met with a number of senior Chinese Communist Party officials and with PBOC and Bank of China officials. The delegation was given an overview of China's official thinking at the time about China's aspirations in the economic sphere. There was much interest by the Chinese about the Federal Reserve's role in the U.S. government apparatus and about the Federal Reserve's functions and policies. One morning, at the University of Beijing, Chairman Volcker gave an overview lecture on the U.S. economic system, including the role of the Federal Reserve. A descriptive academic catalogue booklet in English presented to the delegation listed a number of required courses for all students on various aspects of Marxism. Tours of Beijing's major sights and several banquets in grandiose halls filled out the program for the delegation's stay in Beijing.

The remaining part of the Federal Reserve delegation's stay in China was heavily focused on showing the delegation what the Chinese regarded as interesting and historically and politically important sights in four cities—Shanghai, Hangzhou, Xian, and Guangzhou. The most spectacular sight was the terra cotta army sculptures in Xian that were being excavated in our presence.

The delegation met with the presidents of the PBOC's provincial or municipal city banks, who were the formal hosts for the delegation and for the official banquets in each city. Given that the presidents of these banks at the time of our visit were Communist Party rather than professional appointees, there was little of substance discussed with these officials. In Shanghai, the delegation had an interesting session with the mayor of Shanghai, which was a major political Communist Party position. He subsequently became prime minister.

Informative substantive discussions on the Chinese economy and on the activities and policies of the PBOC did take place during our travels and stay in China with the official escort from the PBOC's Beijing headquarters, Shang Ming, a longtime senior official of the PBOC who was very knowledgeable in these subjects as well as in Chinese contemporary history. This official, who also was part of the Chinese delegation visit to the United States, in turn raised many questions about the Federal Reserve and the U.S. economy, which gave the delegation an opportunity to enlighten this senior PBOC official on these topics.

The Federal Reserve delegation visit occurred in the early stages of China's reentry into the world economy. What we saw was a country that was still reeling from the Cultural Revolution (the PBOC officials with whom we conversed during our travels in China and on the sidelines of official meetings spoke quite openly about the Cultural Revolution) and was at the start of the transition from being an agricultural society to becoming an industrial economy. At the time, China did not have the infrastructure to support an advanced industrial economy. The economic progress that China has achieved in the 25 years since the Federal Reserve's delegation visit is thus quite remarkable.

The exchange of visits by the PBOC and the Federal Reserve visit met the objective of establishing a personal and institutional relationship with senior Chinese and Federal Reserve officials and with the PBOC and the Federal Reserve. Having a U.S. official of Chairman Volcker's stature spend 10 days in China was a coup for the PBOC. Both the Federal Reserve and the PBOC have built on the relationship established by the visits of the two delegations, with senior Federal [Reserve] officials paying official visits to China and senior PBOC officials visiting the Chairman of the Federal Reserve Board on a regular basis.

A number of the former Soviet satellite states—the East European countries—established contact with the Federal Reserve before the Soviet Union did. They needed functional help to bring their central banks up-to-date rather than starting from scratch to understand how to function in the international financial system. The absence of working in and with financial markets was shorter for East European countries than that of Russia—starting in the 1940s in the case of East European central banks, compared with the 1920s in the case of Russia's central bank. The East European central banks still had some people who served in the pre–World War II central bank, with memories of having worked in foreign exchange, bond, and gold markets. They thus were more receptive intellectually to adopt certain aspects of market forces in the conduct of their affairs. In addition, some of the younger staff members in East European central banks were exposed to conventional financial concepts in their studies and thus were ready to introduce central bank practices and policies pursued by Western European central banks.

The Federal Reserve assisted the East European central banks in selective ways—in particular, in the payment system area, in general financial market operations, and [in] central bank organization matters. The Federal Reserve provided much staff time and expertise and helped arrange contact with other financial experts.

Dealing with the former Soviet Union/Russia was more complicated. Partly, it was psychological. The Russian central bank (the Gosbank) officials thought that Russia was the second most important country in the world. And now they were faced with being advised by the most important country in the world, the United States, that this is the way it is done in Western countries, or that it is advisable to adopt this or that practice. So it was more delicate dealing with Russia on these matters. Also, market concepts were difficult for the Russian officials to absorb, since the mind frame of many of the Russian central bank officials was anti-market, and the old guard Communists were, for the most part, in control of the central bank.

The Federal Reserve was visited by many delegations and by senior officials from the Gosbank. And the Federal Reserve, with the FRBNY playing a major role, provided the Gosbank considerable technical assistance, in particular in the financial market development and payment system areas. Some of the younger staff members were more open minded; they had been exposed somewhere along the way to some of the modern central bank concepts. I don't know what they read, but they knew something about markets.

The Board staff and, certainly, the Chairman, other Governors, and regional [Reserve] Bank officials understood that one can't go around telling Russian officials to do this or to do that if they want to run their economy and financial system smoothly. One had to be much more circumspect in giving advice. Chairman Greenspan made a number of speeches in Russia and in the United States, providing the big picture by contrasting operating the financial system with open markets versus doing so by central direction. Over time, the message filtered down, and Russian central bank officials made changes in the right direction. I think that the Federal Reserve had an impact in the transition of the Gosbank from a narrowly focused central bank, serving the needs of central planning, to a central bank designed to function with markets, both domestic and international.

All these former communist countries had to adjust their thinking and practices from ingrained, ideologically based ways of running their central banks. But once some central bank officials from these countries were exposed to how the central banks in Western countries were organized and operated and became convinced that the Western approach to running a central bank would be appropriate for their central bank, you get an advocate within that central bank who kind of pushes this viewpoint, and you have made inroads.

One of the basic organizational characteristics of modern Western central banks is central bank independence from the political authorities. Many countries don't have central bank independence, but, in recent years, more countries, including some East European ones, have adapted their legislation to grant their central banks operational and policy independence. While the Federal Reserve is a strong advocate of central bank independence, in its contact with the central banks of China and Russia, the Board typically did not highlight this feature of central bank organization for adoption by these central banks because this topic was politically sensitive. The Federal Reserve left this task to the IMF.

Federal Reserve officials and staff were consulted meaningfully and extensively by European officials from central banks, finance ministries, and the European Commission who were exploring how to establish a European central bank, the ECB. Many of these officials thought that the Federal Reserve was the perfect model for a European central bank—if they just were to copy the organizational structure of the Federal Reserve, all their problems would be solved. They had 1 central bank with 12 national banks. The United States has 1 central bank with 12 regional banks.

Board staff—me included—who were involved in long dialogues with these European officials tried to dissuade them of this notion. A convincing argument was telling these officials that, if the Federal Reserve had to be established in the year 2000, it would not have done it the same way as it was done in 1913—the way the Federal Reserve is structured and operates is an accident of history, reflecting the political circumstances of the time. Our European interlocutors were urged not to copy our clumsy system, whereby a discount rate change has to be initiated by the board of directors of a regional Bank and sent to the Board to be ignored, approved, or denied. If approved by the Board, the discount rate change announcement is made from the District that submitted the request for the change. And, lo and behold, in order to have a uniform discount rate in all 12 Federal Reserve Districts, the other 11 Districts submit a request for the same discount rate change approved by the Board for the first submitted request for a discount rate change. That's a Rube Goldberg way of running a discount rate change mechanism.

The European officials went around the world to consult with many central banks to learn what features of those banks would be appropriate to be incorporated in the new ECB, but the frequency of visits by European officials to the United States was based on the notion that the Federal Reserve was the ideal model for organizing the new central bank.

When visiting with the Chairman, some key players on the European scene asked the Chairman and the staff questions about central bank independence. The meetings with the Chairman on this subject were some of the most interesting meetings that I attended. Chairman Greenspan impressed upon these European officials that a complement to central bank independence is central bank accountability. In the U.S. case, the Federal Reserve System is a creation of the Congress. Central bank independence was granted to the Federal Reserve by congressional legislation, and it therefore is appropriate for the Federal Reserve to be accountable to the Congress, an entity that has authority. Technically, the Federal Reserve Board is subject to impeachment.[3] That's the ultimate threat. But as part of day-to-day accountability, the Board has to explain itself. This is done by regular appearances by the Chairman or Governors before congressional committees, submission of reports to the Congress, public addresses, and the release of reports and studies to the public. While central bank independence does not allow the Congress to interfere in the day-to-day conduct of policy or to override decisions by the Federal Reserve Board or the FOMC, sometimes the legislative branch could give broad policy guidelines, which, unless the policy guidelines are part of legislation, the Federal Reserve need not necessarily follow.

Chairman Greenspan pointed out to the European officials that the European Parliament is not like the U.S. Congress. The Congress has authority, whereas the European Parliament

[3] Editor's note: The Federal Reserve Act (section 10(2), 12 U.S.C. 242) says the President may remove a Board member "for cause."

does not. In order for the ECB to have credibility and national public support for its policies, there ought to be a notion of accountability to a responsible authority. The European Community has an independent central bank that is specified in the community's constitution. That itself is a problem, according to Chairman Greenspan, because constitutions are very difficult to change. In contrast, legislation can be changed—as was done by the Congress, for example, when it mandated the Federal Reserve to meet the specific Humphrey-Hawkins requirements in its conduct of monetary policy. The Federal Reserve's mandate and formal responsibility has been changed by legislation since the Federal Reserve was established.

Was the Federal Reserve influential in guiding the establishment of the ECB? Yes—in overall management types of issues focusing on the organization of the new central bank, the Federal Reserve was helpful. I remember giving some of the European officials (who came to the Board for consultations on how the Federal Reserve conducts its affairs) the documentation for FOMC meetings (outdated Greenbooks and Bluebooks and the Beige Book) as an illustration of the staff preparation for FOMC meetings, with all FOMC participants sharing a common forecast and common assumptions. Would the ECB be very different from the current one without the extensive consultations European officials had with Federal Reserve officials and staff? I don't know. But based on the way the ECB is running its affairs, it would appear that the officials who consulted with the Federal Reserve listened to the guidance and information provided by Federal Reserve officials and staff quite a bit—but not on the central bank independence and accountability issues. The ECB is independent by decree—very independent, in fact. But it does not have any real strong accountability feature.

Your other question was on transparency. I have some vested interest in this topic. After I left the Board, I went to the IMF. A few months after I arrived, I was asked to work on developing a code of good transparency practices for monetary and financial policies. The Interim Committee at that time was proposing and mandating the Fund to do this and to do that. Two years earlier, U.K. Chancellor of the Exchequer, Gordon Brown, mandated the IMF to develop a code of transparency for fiscal policy. The IMF developed, and the Interim Committee approved, such a code. In the spring of 1998, the Interim Committee, at the behest of Chancellor Brown, called on the IMF to prepare a similar code for transparency for monetary and financial policies for approval by the Interim Committee.

So the IMF received its marching orders, which were passed on from management to the staff in the department where I was working. Another fellow and I were given the mandate to develop an outline for this code, and, subsequently, I was given primary responsibility to formulate a text for this code. We knew roughly what was meant by the term "monetary policies" in the code's title. We were less clear what the Interim Committee had in mind with the term "financial policies" in the code's title, since it could cover a wide variety of policies. It could mean bank supervision, insurance regulation, or security regulation. Should it also include pension fund management, foreign exchange control, debt bureaus, payment systems, and deposit insurance? We tried talking IMF management out of having the code cover both monetary and financial policies, but our suggestion was rejected. Since Chancellor Brown proposed it, the IMF had to comply. It turned out that, in speaking to his staff, they also didn't know what was intended by the term "financial policies."

Trying to develop in the Fund a code on transparency for monetary and financial policies was no simple matter. All major documents in the Fund go through a thorough review process. Drafts are first circulated in the department that has primary responsibility in drafting it, then in the other departments of the Fund, then to management, and finally they are reviewed by the

IMF executive board for approval and transmittal to the Interim Committee. There thus were many IMF staffers who had a chance to raise objections on the draft, and the draft had to be navigated through some departments that thought that they should be the primary drafters.

In addition, since the transparency code had to be approved by 181 countries represented at the time by the IMF executive board, we had to be sensitive to the diverse and often contradictory views on transparency by the Fund membership. Moreover, it is not easy to prepare a code of good practices that fits all types of economies. In addition, other international organizations and some of the major central banks got real uptight when they learned that the IMF was drafting a transparency code for monetary policies. Who is the IMF to draft a code on monetary policy transparency? The BIS felt that it had more knowledge of monetary policy than the IMF. Some of the major central banks maintained that they did not need an IMF-prepared document to tell them what good transparency practices for monetary policy are and to be bound by the transparency practices enumerated in a code. The G-10 countries and the BIS wanted their input in the draft document early in the drafting process. Also, they wanted to have a say in defining transparency. Eventually, the code was a negotiated document with all the relevant parties—IMF staff and management, executive directors representing the Fund's membership, and international organizations.

The Code for Good Practices on Transparency in Monetary and Financial Policies was approved in 1999 by the IMF executive directors and adopted by the Interim Committee. After that, we prepared a supplementary document to explain each practice. The code is not a bad document. The transparency code is now in operation, but it's not a code for which there are penalties if central banks and financial agencies fail to meet all transparency practices listed on the transparency code. As part of the IMF assessment of countries' adherence to kinds of codes and standards, the IMF periodically assesses central banks and financial agencies on their adherence to the practices of the code, and the assessment document identifies whether and where the central bank or financial agency is deficient on some of the practices.

By now, transparency has taken on a life of its own, and transparency is now regarded as a desirable objective. Part of my activity after I left the Fund was doing some of the assessments of the code and reviewing the assessments of the code done by IMF staff. Central bankers and financial agencies are sensitive on how they are assessed in meeting the terms of the code. They want their central bank to meet the practices of the code and want to get a "Good Housekeeping Seal" for transparency.

Transparency of monetary and financial policies by central banks and financial agencies involves communicating to the public—in a coherent, consistent manner—what the institution is doing. The reason why it is now accepted by most central banks, including the Federal Reserve, that it is desirable to be transparent about its activities and policies is because it is relatively easy to be transparent. It isn't costly to do so, and there appear to be positive payoffs in doing so. In many cases where the assessment of the transparency code takes place, the central bank governor or financial agency head wonders why his institution has not done the things needed to meet the code's transparency standard.

Transparency probably helps build public support for what a central bank or financial agency is doing, if you have a credible policy. Many countries that adopt an inflation target by definition become more transparent, because they have to issue periodic inflation reports. And having a numerical inflation target allows the public to monitor whether the central bank is adhering to it. If the central bank does not meet the announced inflation target, the central bank will have to explain why the inflation target has not been met. That's part of being transparent.

As more countries were moving to inflation targeting, it was natural for them to sign on to the transparency code.

For small central banks, in a world where financial investors look at the attractiveness of financial markets of different countries, if one has a choice of investing in a country that meets various international standards and codes versus investing in a country that does not do so, investors would likely prefer the country that adheres to these standards and codes. A country thus does not want to be labeled as a nonobserving transparent country by the investment community.

But one should not oversell transparency and make it an end-all objective. A central bank that follows all the transparency practices listed in the code is not necessarily a "good" central bank. A central bank that pursues sound monetary and financial policies but has lousy transparency is much to be preferred to a central bank with lousy policies and good transparency.

Over the years that I was at the Federal Reserve, it became more transparent, sometimes with some resistance on the part of some Board members. There periodically is some tension between the Congress and the Federal Reserve on how much of Federal Reserve's decisionmaking should be revealed and how the Federal Reserve reveals its decisionmaking. The reluctance by central banks to be more forthcoming in revealing to the public what and why they are doing something harks back to the time when central banks typically operated in an environment of secrecy, and it was thought that it was desirable for monetary policy to be opaque. The mantra of central bankers used to be: "The more vague and secretive you are, the more power and control you have. Since the public at large does not understand the monetary policy transmission mechanism anyhow, why go through the bother to explain? Let the public rely on our good judgment, our expertise." This attitude was paternalistic, at best. In the first half of my career at the Board, whenever the Congress asked for certain information from the Federal Reserve, there was considerable resistance. The press releases after FOMC meetings contained limited information. There were long lags in the release of FOMC minutes, and they were written in fairly broad generalities. The general view was: The more one reveals, the more one restricts the decisionmaking group's room to maneuver, and one therefore upsets rather than stabilizes markets.

The transparency code explicitly noted that the call for transparency was not intended to require revealing everything about the central bank's or financial agency's decisionmaking. There are good reasons why it would be inappropriate for the central bank or a financial agency to reveal internal debates of monetary or financial policies decisions, or the decisionmaking strategy, or the names of financial institutions that are experiencing serious problems, if such revelations would have adverse financial market repercussions or risk compromising confidentiality. But when policy decisions are made, there is no reason why a central bank or financial agency should not publicly disclose the decision on a timely basis in language that the public understands, with everyone having access to such information at the same time. Transparency implies orderliness in the public disclosure of information and clear communication. If it is the judgment of a central bank that the release of information concerning a policy decision or a market situation is too sensitive at a certain time, it does not justify never releasing such information. There comes a time when such information loses its sensitivity, and, for the record, it merits to be disclosed.

Over time, the Board has become much more communicative. Information that it maintained 10 or 15 years ago that should not be disclosed so as not to upset markets and create instability, the Board does now disclose as a matter of course. Increasingly, there has been more open communication about Board and FOMC decisions. At the time the transparency code at the Fund was being drafted, I periodically consulted the Board on some issues related to the code. The code was met with considerable skepticism and reservations about its appropriateness. Subsequently, articles in the Federal Reserve Bank of St. Louis *Review* and speeches by Chairman Greenspan, Chairman Bernanke, Governors, and regional Bank presidents laud the virtues of transparency and endorse transparency practices that go well beyond what was able to be included in the code document. So one does not need to give up hope for progress or breakthroughs!

Managing International Financial Crises

MR. SIEGMAN. The Federal Reserve has played an important role in managing financial crises. The exchange rate issue is no longer the critical issue in international monetary policy. It still comes up once in a while, but no one is talking about getting back to fixed exchange rates. Policymakers and market participants have gotten used to the floating-rate regime and learned to accept and deal with its consequences.

International debt problems, however, appear to be recurring phenomena. Every few years or so, the same countries or different ones get into debt-servicing difficulties, leading to the fear of defaults that would threaten the stability of the international banking system. There has been a succession of debt and banking crises. It started with a number of Mexican debt crises, then Latin America, then the Asian crisis, and then the Russian debt problem. The fear by policymakers was that the national sovereign indebtedness problem would spill over to international banks, and the international banking system's health would suffer. How does one deal with recurring debt problems? How does one contain and manage these crises? Ideally, these types of debt problems should be prevented from happening by borrowing countries pursuing sound macropolicies, but one cannot count on good policies being followed by all major borrowing countries.

The central banks became involved in dealing with these debt problems because they were concerned to protect the health of the international financial system. The Federal Reserve assumed an active role—sometimes helping to arrange bridge loans through the BIS, but, in general, by participating with central banks, finance ministries, and the IMF in developing and implementing a coherent and coordinated policy approach to the problem. Many foreign central banker and finance ministry officials from indebted countries used to come to the Board to report on how they were trying to deal with the debt problem and to pick the Chairman's and staff's brains.

The reason why the central bank and the finance ministers were concerned about what was happening in a relatively small economy in Latin America was because they wanted to avoid a breakout of commercial contract defaults. If that were to happen, commerce would come to a halt. If a country declares that it can't/won't pay what it owes or disowns its debts, the country's airplanes, ships, and cargo run the risk of being attached by its creditors should the debtor country's planes, ships, or cargo land in a foreign country. Similarly, foreign bank accounts of the indebted country could be attached. The country's creditors could go anywhere in the world to attach the debtor country's assets. What started as a financial problem soon turns into an out-of-control legal problem that could gum up the whole works and spread from one country to the next, affecting commerce and the security of assets all over the world. So it was partly that and the health of the banking system that made the Federal Reserve become actively involved both in the advisory role and in participating in the policy approaches.

Terrorist Attacks on the United States on September 11, 2001 (9/11)

MR. SMALL. This is the fifth anniversary of 9/11. Where were you on that day five years ago?

MR. SIEGMAN. On 9/11, I received a phone call from my son-in-law, who said, "Quickly, turn on the television. You won't believe what you're going to see there." We saw the second tower go down. People were very disturbed that such an attack could happen and that it did happen. And they didn't know whether more was in store, because once you had the sequential terrorism that occurred on that day, more terrorism could take place somewhere else in the world.

I was in Israel at that time. Ironically, some Israelis—who have their own problems and experience with terrorism—advised me not to go home, because the United States was a danger spot! Previously, I also was in Israel at the time of the sniper shootings in Maryland and Virginia, and I met with the same reaction.

MR. SMALL. Thank you for the interview.