To Our Readers:

In honor of the 75th anniversary of the Federal Reserve Bank of New York, this special issue of the *Quarterly Review* reprints a selection of speeches by the seven chief executive officers of the Bank. Generally, we have chosen one speech for each chief executive. In the case of our first Governor, Benjamin Strong, we have included a speech dating from the middle of his term as well as selections from a 1915 talk describing the earliest days of the Bank.

Taken as a whole, the speeches contained in this volume portray a noteworthy—but perhaps not surprising—consistency of philosophy among the Bank's chief executive officers. One powerful reason for that consistency is to be found in the writings of Benjamin Strong, whose lasting imprint on the Federal Reserve Bank of New York is readily apparent. Strong's 1915 description of the early days at the Federal Reserve is fascinating in both pragmatic and philosophical terms; his mastery of the details of both commercial and central banking is unmistakable.

From the very beginning, Strong saw credit policy as "the heart of the system upon which . . . every other part depends." In 1922, he captured in a single paragraph a description of the Federal Reserve which, in its simplicity and its insight, probably spells out the essence of the Federal Reserve as well as it has ever been said in a few words. He wrote,

> The Federal Reserve System has always impressed me as being essentially a social institution. It is not a supergovernment, it is simply the creature of Congress, brought into being in response to a public demand. It was not created only to serve the banker, the farmer, the manufacturer, the merchant, or the Treasury of the United States. It was brought into being to serve them all. Its guiding influence is not profit. Practically all its receipts over expenses go to the government. For some the service it performs is direct, for others it is indirect, but is not less definite nor any less important. It needs and asks that it be given the benefit of intelligent study and enlightened criticism. Its future depends upon its own good behavior and upon its success in winning and holding the confidence of the public.

In the case of George Harrison, the second chief executive officer of the Bank, we were able to locate only one full-length address over his term of office. We have included in the publication a letter written by Harrison which explains why he chose to avoid making public statements.

Harrison's 1936 speech is of note not just because it apparently is the only formal speech he delivered during the 12 years of his presidency but also because of the setting in which it was written. It is very apparent that the depths of the recession, the banking crisis of March 1933, and the gathering storm of World War II were all prominent in Harrison's thinking. When he speaks of "short-term funds washing about money markets of the world in defiance of all the ordinary rules except the rule of fear," one cannot help but conjure up a sense of how difficult that period must have been.

Yet, despite the turmoil of the day, Harrison's speech is most memorable for its insights on domestic and international monetary policy. He makes the case that economic nationalism can only result in lower, not higher, standards of living. He obviously is sensitive to the limitations of monetary policy, including his belief that "no central banking system can be made a substitute for a sound commercial banking system." He is skeptical about "rules" in monetary policy but his insight and his pragmatism are perhaps most evident in his comments about alternative exchange rate regimes. Specifically, he writes,

> Now, the increasing rigidity which we have witnessed has been cited by some as proof that an international monetary standard is no longer workable. That seems to me the shallow and short-sighted conclusion. It ignores the great dangers and hazards of fluctuating exchanges as well as the competition in defensive measures to which they lead. Financial armaments, like military armaments, are expensive and unsatisfactory. Moreover, there is implied in this whole view the fallacious notion that nothing more is involved than a mere act of choice; that we are entirely free to choose between domestic monetary stability and international monetary stability. It would be nearer the truth, in my judgment,

to say that neither is possible without the other. Unless each country is literally to build a wall around itself, our economic problem will always be one of interplay between internal and external forces, and no amount of choosing between fixed or flexible exchanges will get around that fact.

Allan Sproul's "Reflections of a Central Banker" was written only six months before he retired as the third chief executive of the Federal Reserve Bank of New York. Sproul's remarks, coming after 14 years of service as the Bank's president, are noteworthy in several respects. One is his spirited defense of the structure of the Federal Reserve, with particular emphasis on the role of the Federal Open Market Committee, the regional character of the Federal Reserve, and the role of the Reserve Bank Presidents as members of the Federal Open Market Committee. Sproul notes with an obvious sense of concern,

I have spoken of this matter of organization at some length because I think it is vital to the preservation of a Federal Reserve System which retains regional vigor in a national setting, and because attempts to destroy the Federal Open Market Committee, as presently constituted, have been made from time to time. In fact, a bill has been resting in a Congressional committee for the past year which would abolish the Federal Open Market Committee and transfer its functions to an enlarged Board of Governors of the Federal Reserve System. That way lies a revolution in the organization of our credit control machinery. I believe that this is a question which goes well beyond the mere mechanics of organization and which needs and deserves your closest scrutiny as citizens, as well as economists and men of finance.

In the remainder of the speech Sproul presents a masterful portrait of the art of central banking, including the great difficulty of winning support for policies that are designed to prevent an outbreak of inflation, in contrast to policies aimed at correcting inflation once it has already occurred. He says,

When we mention inflation as a reason for trying to restrain a boom which shows signs of temporarily exhausting physical capacity to increase the supply of goods and services, ... we are apt to be charged with crying wolf when there is no wolf, to be denounced as apostles of deflation. And if actual inflation does not develop, perhaps because we have done our job of helping to curb its development, the accusation against us seems to gain validity.

Sproul also was skeptical about monetary rules. On this, he writes, "I do not believe that we can now devise a 'norm' or an equation which will relieve us in any substantial and consistent way of the necessity of exercising human judgment in discharging our responsibility."

When Al Hayes assumed office as the Bank's fourth chief executive officer in 1956, his three predecessors, Strong, Harrison, and Sproul, had, over the relatively short period of about 40 years, created a strong institutional tradition which is to be seen in the writings of the Bank's next three Presidents—Hayes, Volcker, and Solomon. To be sure, each was unique and distinctive in his own right but the influence on them of the first years of the Bank's history is quite evident.

Hayes' late 1974 remarks on the international monetary system should be looked at in the perspective of the time and the man. The setting, of course, was shortly after the collapse of the Bretton Woods system and the first oil shock. The man, like his predecessors, was conservative. He did not resist change but he strongly believed that change—especially major change—had to be approached with care and executed with precision.

In this setting, a number of his comments would prove to be prophetic—for example, his call for "greater emphasis on effective measures to conserve fuel, however unpopular they might be," or even more to the point, his caution that "'recycling'... is a misnomer—or worse" in that "it tends to conceal the basic question of who shall assume the credit risk in lending to the countries beset with economic difficulties."

Perhaps the most important parts of the Hayes speech, however, are the sections "Reflections on Bretton Woods" and "Prospects for the International Monetary System." In looking to the future, he said: "it would not prove possible to agree in advance to a complete new system. Rather, it would be necessary to rebuild gradually on an ad hoc, experimental basis, with various blocks of the new system being put in place as they proved their worth." Finally, his closing strong plea for international economic cooperation speaks for itself.

For those of us who know him well, Paul Volcker's "The Contributions and Limitations of 'Monetary' Analysis" is vintage Volcker. He begins by noting that "sorting out what is true and valid from what is fashionable is never easy." And he ends on this potent note: "My theme today is simple. As we look back over the evolution of thinking about monetary policy and macroeconomic policy generally over the postwar years, we can see the dangers of overly simple and overly confident views of the way the economic world works. Eventually, simple doctrine comes up against complex and harsh reality."

He is plainly skeptical about monetary rules but recognizes that there is a useful element of policy discipline in what he calls "practical monetarism." But even there the emphasis is probably more on the side of "practical" than on the side of "monetarism," for he writes: "I know of no purely mechanical procedure to avoid these risks—to ensure just the right degree of responsiveness to deviations from target. Whether and how much to respond will, I think, always be a difficult matter of judgment and won't be helped much by choice of tactical approach."

Looked at in retrospect, however, the most important part of the Volcker speech is near the end when he worries aloud about an apparent increased tolerance for inflation in the United States. In this context, he says,

> Now, I recognize that it is possible to conceptualize about fully anticipated inflation being equivalent in its real effects to confidence in price stability. But I also question whether our institutions or individuals are in fact fully adjusted, or really can be expected to adjust, to the current rate of price increases or to any sizable rate of inflation. In any case, such an adjustment, once initially made, would not help us to deal with those forces that upset price equilibrium in the past. Indeed I suspect the job of dealing with these forces would be much more difficult, for the difference between a goal of, say, living with 6 percent or a goal of evolving toward stability seems to me profound from a psychological point of view. Willingness to settle for just so much inflation, but no more, would simply lack creditability with the public at large, or indeed, with policy makers themselves. Resistance to increases in the name of short-term advantages could only be weakened, and we would be off again. And I think we have learned enough to see that, in those circumstances, even our employment goals will fall by the wayside.

Tony Solomon's 1984 remarks on what he calls "Unresolved Issues in Monetary Policy" clearly reinforce many of the messages of the five preceding speeches. He warns of serious fiscal imbalances in the United States; he describes efforts to pump up the money supply in those fiscal circumstances as being "nothing short of calamitous"; and he sounds what proved to be an early warning on the effects of financial deregulation and innovation on the monetary policy process. Then, like his predecessors, he says that "we have to pay more attention to the international implications of domestic monetary policy."

Finally, he warns of the deceptions to be found in simple rules of economic behavior and monetary policy. He says,

> The proponents of monetary rules—whether of strict monetary targeting or some mechanical response to changes in the price of gold or some commodity price index—seem to think our problems with inflation are mainly technical. They are not. They are rooted in major structural features of our modern world, both economic and political.

Individually and collectively, these remarks by the Bank's past chief executive officers represent an important insight into the evolution of thinking about monetary policy and monetary matters more generally. Yet, despite that evolution and despite the vastly different circumstances in which each of the speeches was delivered, the commonality of concerns, the blend of vision and pragmatism, and the depth of conviction about the need for financial discipline are what truly stand out. I hope you will enjoy reading these papers as much as I have.

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