The Economic Club of New York

The Honorable Richard W. Fisher

President and Chief Executive Officer

Federal Reserve Bank of Dallas

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Introduction

William C. Dudley

Good morning everybody. If you could take your seat please. Good morning everybody. I'm Bill Dudley. I am the vice chairman of the Economic Club of New York and I'm also the president of the Federal Reserve Bank of New York. Today is a little brighter than yesterday. It's my great pleasure today to introduce my good friend, Richard Fisher, to speak. Richard has been the president of the Federal Reserve Bank of Dallas since 2005. He's had a distinguished career in both the public and private sector. He began his career at Brown Brothers Harriman. In 1987 he created two firms, Fisher Capital and Fisher Ewing Partners. He was the deputy trade representative between 1997 and 2001 where he worked on the implementation of NAFTA. And he was also the vice chairman of Kissinger McLarty. Richard, as you all know, has great insight and especially great wit. Whenever he speaks, I always perk up. Some of the memorable phrases that he's introduced to the financial market lexicon just this year, remember the lines like "wild turkey to cold turkey." And my favorite, "the feral hogs of the financial markets." So the financial markets are now viewed in a slightly different light than they ever were before. Richard and I sometimes disagree, but we always engage. We always listen very carefully to what each other has to say. And I think that really makes for better policymaking. So without further ado, Richard Fisher.

The Honorable Richard W. Fisher

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Thank you Bill. And before we get started I am so honored that the man I consider to be the Moses of central banking, Paul Volcker, is sitting next to me this morning. I am honored that Paul is here. And Paul, we thank you for your great service to our country and your example. As to Bill, it is a pleasure to be introduced by my colleague from the New York Fed. Bill is a friend as well as a colleague. Though it is our custom at the Federal Reserve to only speak for ourselves and not for others, or any other member of the Federal Open Market Committee, I think I can safely say that all 11 of Bill's fellow Reserve Bank presidents and every governor on the Board of Governors is grateful for his service, and indeed his total devotion to our mission. By the way, he's a great human being. He's a hopeless golfer. But I do want to take this opportunity in front of this room to formally thank him for his service to our country. So, Bill, thank you very much.

It is a very special honor for me to speak to the Economic Club of New York. My very first job after graduating from Stanford Business School was to work at Brown Brothers Harriman as the policy assistant to Robert Roosa. Bob Roosa was the proud chairman of this club from 1970 to 1971. And he used to regale me with its history, of how anybody who was of consequence had spoken to this group. He used to mention Presidents Wilson and Eisenhower and Kennedy, Winston Churchill, Indira Ghandi, Zhu Rongji, and so many others, and so many others since.

So I mentioned this to my wife Nancy before flying up here. And without much humility, I asked her very proudly, "In your wildest dreams did you ever think that your husband would follow in the footsteps of the world's great leaders and speak to the Economic Club of New York?" You know what her answer was? "Richard, we have been married for 40 years. You don't appear in my wildest dreams." That's sort of puts you right in your place.

Well, I came to speak to you this morning not of pleasant dreams but of the nightmare of fiscal indecision and political chicanery that emanates from Washington, the risk it poses for the reputation of our nation, and the limits it imposes on monetary policy.

I did not come to speak of whether or not we should or we might taper our asset purchases at the next meeting of the FOMC or thereafter. Or how Janet Yellen will lead the committee when she succeeds Ben Bernanke. Or how I might vote when I rotate into a voter's slot next year at the FOMC. I promise you this, I would be happy to avoid answering any questions you have on those matters after my speech.

The iconic actor Errol Flynn, who to the very best of my knowledge was not a member of the Economic Club of New York, is reported to have quipped that his legendary financial problems lay in "reconciling my gross habits with my net income." That is the most concise description that I can marshall to explain the problem plaguing our nation's fiscal authorities. And it has not changed with the 11th-hour temporary agreement reached last night by the leaders of the

Congress and the president. Kicking the can down the road for a few months will not solve the pathology of fiscal misfeasance that undermines our economy and threatens our children's future.

I have no doubt that we will go on indefinitely increasing the debt ceiling, be it in a regular or a herky-jerky, last minute manner. For no president or no congressional leader dares risk being recorded in history as having consciously presided over default and the destruction of the full faith and credit of the United States. Republican or Democrat, all know full well that your fellow New Yorker, Felix Rohatyn, was spot-on some 37 years ago during New York's great fiscal crisis when he likened default and I quote him here, to "someone stepping into a tepid bath and slashing his wrists– you might not feel yourself dying but that's what would happen." But there is, I believe, a limit of tolerance for our government's fiscal counter-productivity, counterproductive Errol Flynn-like ways. I believe that razor in hand, we are stepping towards Rohatyn's tepid bath and that the full faith and credit of the United States is, in fact, at risk.

We saw an expression of this last Thursday when Hong Kong Exchange and Clearing Ltd. announced it would apply an increased haircut to its valuation of U.S. securities held as collateral against future trades with Treasuries maturing in less than one year receiving a risk discount of three percent. This was printed on Friday in a highlighted box above the fold of the front page of the *Financial Times.* And opposite was a picture of Chinese Premier Li. And the paper reported had "signaled Beijing's increasing concern at the Asian summit" and then provided a kindly nowonder reminder that China has 60 percent of its $3.5 trillion in assets, in its foreign currency reserves, invested in U.S. dollar bonds.

The *FT* could easily have substituted Premier Li's picture with one of the German chancellor or the British prime minister, or the Mexican president, or any other world leader or business operator or simple observer of events and ascribe to any of them a more explicit but surely pervasively held concern. "What the hell is going on in America?" Has the ship of state, as Maureen Dowd wrote yesterday, turned into a "ship of fools."

My heart bleeds for my country. For no amount of monetary accommodation that Bill and our colleagues and I might come up with, no conceivable amount of large scale asset purchases, no clever new monetary innovation by the Federal Reserve can possibly offset the rot destroying our fiscal house and the blight it spreads over our national economy.

To be clear, the Federal Reserve will take all appropriate measures to preserve monetary and money market functioning and stability in periods of acute distress. I view this as an integral part of our formal dual mandate. Chaotic money markets threaten both price stability and business activity and employment. However, it's not our job to fix the budget impasse. Any initiatives we might have to undertake in the course of our duty as a central bank to prevent serious disruptions of U.S. dollar funding markets should not be executed in a way that might be construed to substitute for fiscal redress. Fundamental, structural imbalances in our economy might be temporarily obscured but cannot be permanently resolved by monetary sleight of hand. Indeed, I argue that the current monetary accommodation policy of purchasing $85 billion a month in Treasuries and MBS, or mortgage-backed securities, risks exacerbating the situation. There is a tipping point where monetary accommodation comes to be viewed not as a pleasant stimulus that levitates the bond and stock markets and the housing markets leading to a felicitous so-called wealth effect, but instead becomes an agent of financial recklessness. None of us really know where that tipping point is. But with each dollar of Treasury and mortgage-backed purchases the FOMC instructs the New York desk to make, we inch closer to it.

For the remainder of Ben Bernanke's leadership and from the very first nanosecond of his successor's, the FOMC will have to astutely maneuver so as to avoid crossing a line that no Nobel laureate, no econometric modeler, no quant-jock or dealer or market operator can identify ex-ante.

I admit to a preoccupation with this concern. Bill knows of my preoccupation with this concern. But this much I know. As long as inflationary expectations are held at bay, we at the Fed can fully open the monetary throttle in an effort to deliver on the mandate Congress gave us to achieve full employment. But it's all for naught as long as the fiscal authorities are slamming on the brakes and leaving everybody in the dark as to how they will cure the fiscal mess that they have wrought.

No rational businesswoman, no rational businessman will or should make a long-term commitment to expanding their workforce or commit their precious capital to significant job-creating projects if they have no idea whatsoever what their taxes will be or how government spending will impact them or their customers or their suppliers. And no manager can plan or budget forward while simultaneously working under the yoke of ever-expanding regulations that render incalculable their cost structure, including the full-in cost of the most important variable in that cost structure – their workforce – as long as the Affordable Care Act remains more of a mystery than a clear, understandable program.

The creative capacity of American businesses for dealing with uncertainty is unparalleled. But doubts caused by fiscal malfunctioning so extreme that the risk-free rate of the world's largest economy and reserve currency is called into question are of a different kind and character than the everyday uncertainties that even the most gifted manager is trained to handle. How does one discount the value of payables and receivables for next year when the world wonders if the U.S. government will validate the full value of Treasury bills?

It is true that unlike the Congress, as Bill mentioned, the FOMC actually makes decisions and most importantly it does so in a civil manner. These are both lost traits in Washington. But it is a myth that we at the Fed have the power on our own to propel our economy forward. We can provide the fuel, but we cannot engage the gears of the engine of employment. Only businesses can do that. And businesses cannot do it when they haven't an inkling of how the fiscal mess that is Washington will be resolved. The simple observation here is that U.S. businesses and households need confidence that fiscal policy will be conducted responsibly, that revenues and expenditures will come into line, at least over time. And until that fog is lifted, do not expect the economy to steam forward at anything but a most cautious pace.

In contemplating the fix that we are in, I thought of a phrase used by Queen Elizabeth in her 1992 speech, marking the 40th anniversary of her accession to the throne. You may recall that was a year when a series of tragedies, including the burning of Windsor Castle, beset her family. And with classic British understatement, she told her subjects: “1992 is not a year on which I shall look back with undiluted pleasure. It has turned out to be an Annus Horribilis – a horrible year.”

We have suffered so much on the financial and economic front in the last few years. And, in fact, since 1976 we’ve had 17 occasions under six of seven presidents where we’ve experienced a federal government disruption, including shutdowns. Since 2010, we have had eight budget conventions and budget committees such as the one created last night to no avail. And we’ve seen several face-offs on the debt ceiling. But the cumulative effect of our government’s fiscal ineptitude and propensity to put off taking action on hard decisions and the frustration that I feel, many of colleagues feel, about the inability of even the most radical monetary policy to work in the absence of long-term fiscal probity has tempted me personally to record 2013 as an annus horribilis, a horrible year. It is certainly at a minimum not shaping up to be a year in which I shall look back with undiluted pleasure.

It need not be so horrible, however. In fact, it may be a year of good fortune if our president and congressional leaders summon the courage to put partisanship, gamesmanship aside and finally craft tax and spending and regulatory policies that encourages businesses to take the cheap and abundant money that the Fed has made possible--the cheapest in 237 years of American history--to take that money and put it to use creating jobs and expanding the wealth of the entire nation, not just that of the rich and the quick financiers and those with the means to speculate and profit from volatility. Getting these incentives right is not an easy task, but it is a crucial one.

One of the most exalted of your club's long history of speakers, Winston Churchill, said, "In finance, everything that is agreeable is unsound and everything that is sound is disagreeable." Continuing down the path of hyper-monetary accommodation is certainly agreeable especially if you are invested in stocks or bonds or have been able to refinance your mortgage and participate in the new housing boom. But carried on for too long, it is surely an unsound way to put our nation back on the path to respectability or to eliminate the markets placing haircuts on the value of U.S. Treasuries. The only way for us to achieve sound footing is for our fiscal leaders to make politically disagreeable decisions. There's no other way for us to regain and maintain our standing as the most prosperous and powerful and accomplished economy in the world.

Now I mentioned Queen Elizabeth's Annus Horribilis speech, but so as not to leave you despondent this morning, and I can see your despondency on your faces, I wish to remind you that the queen's expression was a play on words of a poem written in 1667 by John Dryden. And it was titled, *Annus Mirabilis – the Year of Miracles*. Dryden was writing about the year that spanned 1665 to 1666. It began with the Great Plaque of London, a pandemic that was akin to the bubonic plaque. It ended with the Great Fire that burned London to the ground in five days. So why the title, *Year of Miracles*? Because from that wreckage, London rebuilt itself and arose from the ashes with wide streets and buildings commissioned by Charles II and designed by Christopher Wren that were so solidly built that they stand to this very day.

Our collective task is to turn the current annus horribilis into an opportunity to emerge from the current fiscal wreckage stronger and more resilient than ever. If England can do it in the 17th century, we Americans, who have never, ever flinched from staring down and overcoming adversity, can certainly do it now.

Now I'm tempted to remind you of how Texas arose from the ashes of the 1980s oil bust and savings and loan crisis to lead the nation in job creation for several decades and become our nation's most prosperous state. But I'm not going to do so. I'm tempted to tell you how in the Texas renaissance, as the U.S. job market has seen job destruction in the middle two income quartiles for the past decade, Texas has seen job creation in those same middle income groups and has outperformed the nation in creating jobs also in the highest income quartile. But I won't. I'm tempted to tell you that Texas came off the bottom to become the top exporting state in the United States, but I shan't. Or that our state laws and regulations crafted with the 1980s banking crisis in mind spared Texas the worst of the recent housing crisis. All these factors, of which I won't breathe a word this morning, have resulted in a workforce of some 12.8 million, and in 2006 catapulted the state of Texas to its ranking as the top destination for people who move across states. Americans and immigrants from abroad alike come to my state to seek jobs and opportunity in what continues to be the nation's most dynamic economy. I could tell you about that but I'm going to refrain from doing so this morning.

Instead, let me point to New York as an example of what is possible. Some of you may remember the predicament in which New York found itself in 1975, the year that I came to work on Wall Street at Brown Brothers. It was de facto bankrupt. Garbage piled up on the streets. Crime was rampant. Upper East Side apartments could be had simply for the assumption of maintenance costs. Nothing worked. Everything here was dysfunctional. The outlook was so horrific that Mick Jagger wrote a song called "Shattered" after a cab ride around the city. Let me just read you three of the lyrics. "What a mess. This town's in tatters. I've been shattered. My brain's been battered. Splattered all over Manhattan."

Then, when the markets showed the city the back of its hand, leaders such as Felix Rohatyn and Governor Hugh Carey and others stepped up the plate. They and the people of New York turned something truly horribilis into something truly mirabilis. Very disagreeable but sound decisions were made. And those decisions took a tattered, shattered city and put it on the path to becoming the bright, shiny, miraculous Big Apple that it is today.

The Federal Reserve is limited in its power to make what took place in New York happen for our entire nation. Unless the fiscal authorities get their act together, looking to the Fed to solve the nation's economic ills through ever-expansive monetary policy might well make the situation worse. So I end with a plea for our president and our Congress. The markets are restless. Your peers around the world, Mr. President, are afraid. There is little remaining tolerance for agreeable but unsound decisions. The bond market is beginning to show us the back of its hand. It is time for leadership. Turning something horrible into something miraculous is the American thing to do. Please get on with it. Thank you.

QUESTION AND ANSWER PERIOD

WILLIAM C. DUDLEY: So Richard has kindly agreed, right, to take some questions.

THE HONORABLE RICHARD W. FISHER: And avoid answering them, yes, of course.

WILLIAM C. DUDLEY: So if we could get questions from the floor, if you could identify yourself.

WILLIAM RHODES: Thank you, Richard, for a very interesting and as always provocative speech. And thank you for coming here and the work you do at the Dallas Fed. My name is Bill

Rhodes. I'm a member of the board of the Economic Club. I get all your speeches. You're good enough to send them to me. And you've been very vocal on the subject of "too big to fail." And I know that you don't have time to give another talk on that, but is there anything you'd like to leave...

THE HONORABLE RICHARD W. FISHER: I'd be delighted to do so.

WILLIAM RHODES: I know, but is there anything you'd like to leave us succinctly on that subject because I think it's very important and you certainly have been very outspoken on the subject. Thank you.

THE HONORABLE RICHARD W. FISHER: Well, having mentioned the *FT* and Maureen Dowd's comment in the *New York Times*, just for fair advertising, I brought a copy of the *Wall Street Journal*. And this mentions a specific bank but it absolutely astonishes me. This is from Wednesday, October 9. And it talks about J.P. Morgan's efforts to reform itself. I'm a former banker. I worked for Brown Brothers Harriman. I had beaten into me like a plebe at the Naval Academy the basic principles of banking. And there's one dictum that all bankers, every banker has always hewed to, and that is know your customer. So I was interested to read in the *Wall Street Journal* on page C-1 of that date the following: "Separately J.P. Morgan is conducting a more rigorous analysis called Know Your Customer to ensure it learns as much as possible about its clients." Therein lies the problem. We have banks of scale and scope in which the managers themselves do not even know their customers. I do believe we have banks that are too big to fail. They're now referred to as SIFIs, systemically important financial institutions, which for me sounds save if failure impending would be a better. Or, and besides SIFI sounds like some horrible disease you might contract from risky behavior. So I don't think we've solved the problem. And Bill and I would have disagreements on this, but I have the podium. As much as I love this guy, we've enshrined them. Now just to make it very, very clear what my proposal is and that of the Dallas Fed, I'm not for breaking them up. I'm for making it clear that taxpayer money is only at risk in their commercial banking operations and is only there to protect savers. I don't care what other business they conduct. But every one of those other businesses would be clearly delineated as having no government guarantee. And moreover, if they run those businesses and they run them well, if they increase their positions of risk, they must, like all the rest of us, post margin and be subject to the same rules as any individual or any trading operation in the world. If a hedge fund has to post margin on its derivatives position, then J.P. Morgan should be doing the same on its $80 trillion of outstanding derivatives. No matter how balanced, when they're risking their own book, they should be subject to the same rules. And then thirdly, our proposal just calls for their statements to be more opaque. No analyst I know, no sophisticated hedge-funder I know can really discern what's on those books. The CEOs know the risk that they're taking. If not, they should be gotten rid of. The risk managers, as a former risk manager at one of the largest institutions sitting in this audience who I know and love, they know. If they know, it should be visible to the shareholders. It's a simple proposal. And I think if that were to occur, this isn't taking a government meat axe, it would certainly highlight who is capable and who should get business. And some of them may grow their businesses in those different areas. But the one thing I care about is we never risk another taxpayer penny to bail out bad decision making. That's the essence of our proposal. That would be "breaking up the banks" but it would do so in market-driven manner. And I think the markets would then decide who should be valued at what. The one thing I have noticed is if you take the four most complicated, big, too big to fail, SIFI banks in this country, they do trade at a discount in terms of the multiple book value. The market is telling us something. And I think the market can settle this problem if we just have some clear delineation of where the government is indeed exposed. So those are my proposals. And are we making progress on that front? I would say we are. It is politically attractive on both sides of the aisle. I'm getting great support from the new senator from Massachusetts as well as the extremely liberal senator from Louisiana and others. And I believe we're making progress on that front. It is the one thing that Congress can do that has bipartisan support. And I would like to see them do something and this is something they can act on and I believe they will. Sorry bankers. Yes sir...

David Malpass...

THE HONORABLE RICHARD W. FISHER: David, how are you?

DAVID MALPASS: I'm fine . Thank you for that fabulous speech. I am tempted to ask you when tapering will start, but I won't.

THE HONORABLE RICHARD W. FISHER: I'll let Bill answer that question.

DAVID MALPASS: I have a fiscal question...well, Bill, when will...(Laughter)...a fiscal question and so two parts. The Fed right now is buying down the interest rate by borrowing very short term at very low interest rates and buying the higher coupon bonds. So it has the effect of lowering the fiscal deficit. So my question for you is there's been reluctance in Washington to reduce spending on the idea that it would be contractionary. We all talk about fiscal stimulus. So could you put that in context. Would a reduction in government spending slow the economy? And how does the Fed's buying down of interest rates help provide stimulus or not? Thanks.

THE HONORABLE RICHARD W. FISHER: All right, David, you and I know each other well. That was a good statement disguised as a question. It is true that the cost of government debt has declined. I want to remind you that we've had a 32-year bond market rally. It started when Paul broke the back of inflation and it's been running every since. So, yes, we did intervene and we have twisted the yield curve. We added what I call the crescendo to this great market rally. But it was already well under way and we've driven it now to all-time, as I mentioned, historically low records, the lowest records at least we think in 237 years of American history. And I presume one could say that this has made it easier or less offensive for fiscal authorities. And I think the implication of your question is have we assisted basically in their misfeasance. I've argued that at the table. It's one of the costs that's involved offsetting the benefits of the policy that we, the committee in its wisdom, has ensued. The other question which is would cutting spending or changing, I think it's more, first creating some certainty. I'm not a PhD in economics. I'm very proud of that by the way. I don't have the brain power of most of my colleagues at the table except for Bill's which I far exceed. But the one thing I learned as a Stanford Business School first-year student was what business is, is decision making under conditions of uncertainty. I referred to that in my speech. We have to at least know what's going on. How can you running X, Y, Z company, or a woman running A, B, C company understand and have a sense of confidence going forward which is required to make CapX and to create jobs and hire people. You don't hire people to dispense with them, you hire them to have them on your payroll for a long time to enhance your output. How do you make a decision if you don't know what your taxes are going to be next year? How do you make a decision if you don't know how government spending will impact you, as I said in my speech, or your customers or your suppliers? How could you possible make a decision as to the full-in cost of an employee if you don't know what the blankety-blank, the Affordable Health Care Act is, what it means to you? None of us know. If you knew, you could maneuver around it. So I think that's point number one. Certainty, David, is what we need. Businesswomen and men in America are great at navigating through uncertainty. That's what they're paid to do for a living. You cannot navigate a ship, even with all the instruments, or the rock and roll music behind you, if you're in a complete and utter fog, pea fog. You can't do it. So let's start there. As to the spending and taxing patterns, I'm going to take a moment to answer this. To me our fiscal policy is still Cold War, old-fashioned fiscal policy. I'd like to remind the audience to remember one thing in the same spirit of...New York, we won, we won the Cold War. I grew up, Bill grew up, anybody of our generation, in a nation that was in a constant state of fear of mutually-assured destruction. The wall came down. Mao is dead. Ho Chi Minh is dead. Those old troglodytes, Brezhnev et al, Shcherbitsky in the Ukraine, they're dead. They now want to play the game. We got exactly what we wanted. At the same time, we experienced the IT revolution, which by the way wasn't invented by Al Gore, but it stemmed from the genius of kids that were educated at the greatest institutions of the world, American institutions, American universities. So we got what we wanted. And when I used to travel with President Carter as a kid, we went to the G6. Before that there was a G5. Now there is what I call the G-whiz. There's everybody in the room. So this is exactly what we wanted. We have to shift our entire tax/spend regulatory policy to compete in this world. And I don't understand, Democrat or Republican, why not take advantage of what the Fed has given them, the cheapest money in history. Loads of it. The gas tank is full. Why not say, whether you want union workers or non-union workers, let's put the American people back to work. We have the means to do it. Our businesses have the balance sheets that are the strongest and leanest and meanest and my kids would say, the most ripped ever. Let's focus on this. Because anybody who runs a business, David, you or anybody else, you have an obligation to earn an ROI. If you're publicly held, if you don't, you're fired. And your private creditors are going to demand the same if you're a private company. You can go anywhere in the world now, thanks to us. Thanks to Ronald Reagan. Thanks to his successors. Thanks to Bill Clinton. Thanks to others. We can go anywhere we want with our capital and we should and we must. So our choice is wide open. Why don't we make it more attractive to invest here than anywhere else? Right now, if the descendants of Lee Kuan Yew tell you that you're going to have the following tax treatment for the following years, it's as good as gold. Well, it's as good as gold at $1,900. Here, you don't believe me. So get it straight. And then the spending patterns and so on, I don't think it's a matter of cutting spending. It's a matter of just giving clear signals and we don't do that. So please remember, we were victorious, but now we're losing, we're snatching defeat from the jaws of victory. A phrase never used before, before this group. Other questions? Yes, sir.

EDWARD F. COX: In your speech you emphasized uncertainty in fiscal affairs and its impact on business. The British conservatives came into power on the heels of the Great Recession and went on an austerity budget that should have given certainty to British industry on where government policy would go. That's the benefit of a parliamentary system. And our Macedonian system has been a little bit different and more uncertainty. Could you comment on the impact on the British economy and business vis-a-vis the U.S. government lack of decisions or inability to make decisions, the impact on our economy?

THE HONORABLE RICHARD W. FISHER: Gosh, that's pretty wide-ranging and it takes me back to my student days at Oxford. They're wittier than we are. They have worse teeth than we do. And I do like the fact that the Prime Minister has to go and speak at the box every Thursday. But let's put this in perspective. I love Britain. It's a tiny economy. It doesn't play the role that we play in the world. And again we won. We won a long, long time ago. And we are the beacon for the rest of the world. Our democracy is very different. As you said, theirs is a parliamentary system and you, Mr. Cox, know better than anybody how our system works. They've struggled for a long time with productivity. They had a serious problem with both high unemployment and high inflation. I do think Mr. Carney is one of the luckiest guys in the world. He arrives and a week later, the statistics change suddenly. Amazing what a Canadian can do when they're put in British circumstances. But I'm not sure what good it does to discuss this, to be honest with you. We have the system we have. It's not going to change. It requires different skills of leadership. And with all due respect to our British friends, what we do really, really, really counts. Eighty percent of all the commercial transactions in the world have the dollar on one side or the other. Bill would probably know the answer, but in British pounds I'd say it's probably less than five percent. I don't know. So the importance of what we do has greater weight. The system in which we operate is entirely different. And it's an interesting question, I like to think about it. But I don't want to be rude. I don't think it matters. I don't think there's a whole lot we can draw from them. But suddenly, and I'm not implying causality, the British economy is improving and performing better than it was before. But I do attribute it to having a Canadian at the Central Bank. By the way, I love Mervyn King, mainly because he supported me on "too big to fail." He's a great guy. Smart guy. Yes, sir.

PAUL DAS(?): Governor, thank you for sharing your insights with us. And over the last few weeks, given the debate, and I was, I noticed words that you used like blight. I did go back and look a little bit at our history and it seems to me going back to the 1860s up to now from time to time Mark Twain's words about "news of my death is greatly exaggerated" tends to come to mind when we look at how we deal with our issues. And ultimately in retrospect when we see where we have gotten to from where we started, I'd like to press you a little further. It seems to me from what you are saying is we should take advantage of this unique period in time where money is as cheap as it is, to actually do a lot more of the fundamental investing, whether it is in R&D, whether it is in education, rebuilding the productive capacity of the country, such that for the foreseeable future for a competitive world that you are talking about that we have to compete in the post-Cold War era, we are better prepared. And overall this may augur for us to be spending a little bit more than what we are taking in. Not to say we shouldn't be prudent. So it seems to me from what you are saying, that there is a tilt in favor of that. I will press you a little further for your views on it. Thank you very much.

THE HONORABLE RICHARD W. FISHER: Well, you gave a great summary of what I tried to say. I think you're right. This is, to me, a moment of great opportunity. Let me just go through a little bit of history here very, very quickly. In 2008, we had an inflationary scare. Running up through August, we had inflation that was beginning to raise its ugly head up to almost the eight percent level on a monthly basis. How do businesswomen and men deal with that? If you can't price what goes out the door at the same rate of what comes in the door, you turn to your cost variables and you tighten. You drive productivity. What's the biggest cost variable in any business? Labor. Particularly in a service-based economy. And so we had already begun to see a tightening of the discipline that surrounds workforce management. Then everything hit the fan, and we had an implosion of final demand. Lehman Brothers failed, Bear Sterns, et al. The system collapsed. And the Fed went to work to patch it up. By the way, successfully, and we didn't lose money on a single transaction. I'm proud of Bill and everybody else for helping us achieve that. But we had an implosion of final demand. It collapsed. What do businesswomen and men do? They drive down their costs even further. If you can't grow your top line, you do have to manage your bottom line always. As a result of those two forces, I do believe that we have in the United States the most well-run, most productive, most tightly managed and able businesses in the world. I fear China to zero degree. And I used to say at the time, and Bill may remember this phrase, when we looked at the mess that was elsewhere, that at least we had the best looking horse in the glue factory. I've changed that opinion. We are now the finest thoroughbred on the track. And again I don't want to be too self-serving here because I've disagreed with the final aspects of this policy and I worry about the risk we are taking at the Fed. And I mentioned that in the text of my speech. But it is well watered and well fed, plenty of oats, and it's ready to roll. Someone has to open the starting gates. We cannot do that. That's not within our powers as a central bank. And the starting gates can only be opened by the fiscal authorities. Let me give you a, I'm sorry to talk about Texas. I promised I wouldn't, but I will. Let me give you an example. Where I come from, I have 27 million people in my district. Ninety-six percent of the output of my district comes from one state, Texas. I have a little piece of Louisiana, what I call the productive parts Louisiana. And then I have for the southern New Mexico economy. So Texas is the core. I know Texas well. We have the same monetary policy as the rest of the United States. Same rate on CNI loans, same mortgage rates, same consumer lending rates. But we outperform the country, and we've done it for 30 years. And employment creation which is an important part of our mandate at the Fed, even though we have a limited ability to impact it, it's not complete, in Texas with the same monetary policy we've outperformed the nation for 30 years in the rate of growth of employment in all four income quartiles by a factor of 2 to 1. Why is it different where I live than it is in Michigan or Illinois, the same monetary policy? Fiscal policy. Under Democrats like Ann Richards or Republicans like George Bush or Governor Perry, the legislature which is bicameral and is also bipartisan has created a set of rules and regulations and laws that attracts businesses rather than detracts from doing business. Now that's at the margin. We're a big and powerful state and we're the eighth, or ninth or tenth largest economy in the world. But imagine if U.S. fiscal policy, which has a much greater impact on how businesses as a whole think, could be as clear and as attractive in bringing business in and would emphasize job creation. I hasten to add that legislatures have to make laws and they should. For example, our state legislature after the debacle of the 1980s limited by law the amount that you could borrow against your home. All forms of financing were limited to 80 percent of the appraised value of your home. And incidentally, the appraised value of a home in Texas is marked down for a Homestead deduction. So that was prudent legislation. And there were people that complained about it but it was a smart thing to do. So if we can do it, why can't the country do it? And in a moment of total indiscretion I said that we needed more Texa-fication of America and less Califor-nication of America. Not central banker's language, but I believe that deeply. I mean there is one difference. Our legislature meets for only 140 days every two years. Two days every 140 years we'd be doing even better.

And we're not going to change, going back to your question, Mr. Cox, the way we are structured as a Congress. But we certainly can learn from the success cases. And I think we have a good laboratory right here at home. Again, same monetary policy, same interest rates, same availability of capital, but we work it. Why do we work it? Because we've created a culture that encourages it. Where does that culture come from? Not just the frontier spirit, that's old-fashioned stuff. We're not cowboy boots and oil anymore. We're microchips and business suits. But because we are encouraged to do so and our legislature has helped us in that regard. So my point is let's Texa-fy the way the American Congress incenses people without adopting the accent. Yes sir.

My name is Charlie Rose, but I'm not the guy on television.

THE HONORABLE RICHARD W. FISHER: That's why you're not standing up.

CHARLIE ROSE: That's right. The question I have for you is that you didn't address to some degree in your speech, which I thought was excellent, you didn't really address some of the components of fiscal irresponsibility and some of those components seem to be surrounding some of the public issues, surrounding entitlement issues. Some of them seem to be tied to the degradation of education. And some of it is obviously related to the two wars that this country has fought in the last several years that have been funded, that have soaked up a lot of capacity. So I'd like some of your insights into some of the issues about fiscal irresponsibility that need to be corrected. Where would you focus on the equation?

THE HONORABLE RICHARD W. FISHER: Well, I hasten to remind you that neither Bill nor I are elected officials of this country. We're central bankers.

CHARLIE ROSE: I understand.

THE HONORABLE RICHARD W. FISHER: And I'm an equal opportunity basher as far as Democrats and Republicans are concerned and fiscal policy is concerned. I don't think it is my job, nor would the people want me, to give specific recommendations. All I pray for, and plea for is clarity because that's the best way to put our accommodative monetary policy to work. I'll only comment on one thing, because I spend a lot of time on this privately, which is education. We live in a high value added society. I quoted Churchill earlier and Churchill used to always speak of the super refined processes. And what he meant by that was high value added. He was a free trader, by the way, as I am. He wasn't when he started out as Minister but he became one. And he used to advocate let other people subsidize production with their people's tax money. We'll take it, add value to it, and we'll make the greatest profit. So if you live in a high value added society, you have to have a high value educational system and our educational system is in the tank. I see this where I live and I see it everywhere I go. And all of my family in one area or another is involved in the education system, creating charter schools, rewarding schools financially for their performance through our charitable giving, and I'm an overseer of Harvard

University. So I see it at every single level. There's nothing more important to our country than preparing people to compete in a high value added world. And we're passing through the stage in which we've brought billions of people into the workforce at the low value added end and they're moving up. So my only comment is that we need to. And a lot of that has to do with the states themselves, not just the federal government. And I personally worry that there may be too much federal interference but again I'm not an elected official, and I don't think it's appropriate for me to comment on your question. Any others? Yes sir...please. And then I'm going to...I have to tell you a true story I just thought of which I hope will let you leave on an upbeat note from this breakfast. Yes sir.

Again thank you very much for your presentation. You comment on the U.S. fiscal problem which I totally agree. Would you care to make a comment about the much worse Japanese fiscal problem, where that's likely to head? And what the implications might then be for the world?

THE HONORABLE RICHARD W. FISHER: Very briefly. I lived in Japan. I worked in Japan. My son played on a Japanese baseball team as a high school boy. None of us really understand how Japan works. I've lived there. I've worked there. I ran my fund out of Nahmuro(?) for a year. And, by the way, I got there the day the market peaked at 39000. But if you're looking for a parallel, and we'll see if they can pull it off, remember that Prime Minister Abe talks about the arrows in his quiver. And, of course, they've run massive stimulative monetary policies. They have a different franchise than Bill and I operate under, and our colleagues. We're only allowed to buy treasuries in government agencies. They can buy anything and they do. They've lived in a deflationary trap for a very long time. My observation when I was on the ground was that they failed in one major thing. They never dealt with "too big to fail." They closed one large bank and that was a political battle between a certain prime minister and a banker he couldn't stand. And they did him great damage. But they never dealt with their banking problem. In addition to that, it's a hyper-inefficient society. President Clinton charged me, working with an assignee from Prime Minister Hashimoto who was the Deputy Foreign Minister, to put together the Commission on Competition and whatever the heck it was, to deal with every single sector. So we went from the retail laws to the electricity distribution system. The treasury on our team handled insurance and finance and so on and so on and so on. They've made great strides there, but therein lies their problem. And he talks about a third arrow. The third arrow is dealing with rig bidding and construction and all the things that we worked on under President Clinton and Prime Minister Hashimoto which have still not been done. So it's the structure of that society and the Prime Minister himself has spoken about it. And monetary policy which is uber-accommodative, we run hyper-accommodative, they run uber-accommodative monetary policy, they've already seen does not do the trick. It has lifted inflationary pressures. It has assisted in a sense, from that small lift, from a constant state of deflation to a slight increase in consumption but not as much as they expected. And unless they have structural change, it won't work. So we need our own third arrow. He's having a hard time pulling it out of his quiver because there's an inherent corruption that exists in the diet, which is their legislature, and in the structure of their economy. It's the same thing in a different culture.

I want to conclude with something. Bill is telling me to wrap it up, so I've got to tell you this story because it's so uplifting. After our last, actually it was two FOMC meetings ago, I rushed out to the airport. Bill knows I leave immediately after the meetings. I just feel better getting home to Texas. And I went, my plane was delayed, so I went up to the Admiral's Club to wait because it's all American Airlines, we're the hub. And there was, at the desk, a little, old man and a little, old lady. And the guy had a ball cap on. And I could hear the woman behind the desk saying, "I'm sorry, sir, you can't come in, you're not a member." And I walked around and looked at the front of his ball cap and it had written on the front, World War II veteran, Korean War veteran, Vietnam War veteran. So I said, "Are you a veteran of three wars?" He said, "Yes, I am." And I turned to the woman at the desk and said, "You have to let this man in, he's a hero." And she said, "Well, I'm sorry, rules are rules." I said, "Okay, well, they're my guests." And as soon as I said that, this little, old, blue-haired lady said, "Does that mean I can drink champagne?" So I said, "You can have all the champagne you want." So I took her to the bar and I got her a whole bottle of champagne. And then the little, old man said, "Well, if my wife drinks champagne, I have to have a few martinis." So I gave him two martinis. And I said, "Are you really a veteran of three wars?" He said, "Yes. At the age of 19 they dropped me behind enemy lines in a glider. They told me I would never come back and I did. And then I flew fighter planes in Korea" which as you all know is slaughter, the Chinese and North Koreans were enormously able in that war. "And then I flew F- whatever they were in Vietnam." And he pulled out one of those old-fashioned wallets with the long pictures and showed me pictures. Absolutely amazing. So I said, "Well, where are you off to?" He said, "Well, me and the little woman are on our honeymoon." I said, "How old are you?" "I'm 92." But he said, "My girl here is 82." And I said, "Well, where are you going on your honeymoon?" He said, "Phoenix, to see her great grandchildren." I said, "How did you, what's the story?" He said, "Well, by the way, just so you...I didn't rush into this. We dated for two years so I wanted to make sure." And then I said, "Well, tell me, seriously, how did you meet, in church or a synagogue or what was it?" He said, "No, no, no. You know how we met? Match.com." And then he concluded with the reason I'm telling you this story. He said, "You never give up, young man." Never give up on America. Thank you very much.

WILLIAM C. DUDLEY: Thank you all for attending. The session is concluded. Thank you, Richard, very much.