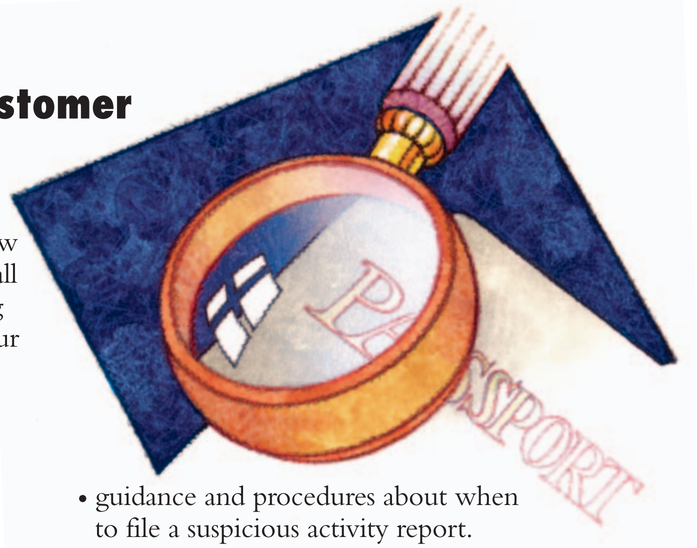
THE FEDERAL RESERVE BANK of ST. LOUIS

Central Banker

WINTER 2004

News and Views for Eighth District Bankers

Regulators Create Exam Procedures for Reviewing Customer Identification Programs



Federal banking agencies have issued Bank Secrecy Act examination procedures to review customer identification programs (CIPs) for all accounts opened on or after Oct. 1, 2003. During each examination, examiners will be reviewing your institution's CIP to ensure that it:

- is appropriate for your bank's size, location and risk profile;
- meets certain minimum standards; and
- provides adequate internal controls and compliance with applicable regulations.

The new exam procedures cover audit and training programs to ensure that your institution has adequately incorporated a CIP. Your CIP must contain:

- detailed account-opening procedures that verify each customer's identity and that notify the customer of the verification process;
- review procedures to ensure your institution complies with record-keeping requirements;
- review procedures that check new accounts against federal government lists of known or suspected terrorists; and
- guidance and procedures about when to file a suspicious activity report.

Examiners also will review a sample of new accounts to test internal controls and compliance with regulations. If your institution relies on a third party for part of the CIP, examiners will review the relationship between the third party and your institution to ensure that it is reliable and contains appropriate internal controls and review procedures.

A copy of the CIP examination procedures is available at www.federalreserve.gov/boarddocs/SRLETTERS/2004/sr0413.htm. For more information, contact Jeff Bock at 1-800-333-0810, ext. 44-8835. ■

Federal Reserve Announces New Deposit Guidelines for Non-Imageable Check Items

As of Oct. 28, non-imageable items must be deposited in a separately sorted forward or return cash letter. Failure to do so will result in the depositor's assuming all liabilities for losses that result from an incorrect deposit.

Non-imageable items include the following: items in carrier documents, including forward items, return items and savings bonds; photocopies in lieu; notices in lieu of return; and foreign and mutilated items.

Follow these deposit guidelines for non-imageable items:

- Deposit forward items in carrier documents, savings bonds in carrier documents and photocopies in lieu of originals in a single cash letter.
- Deposit return items in carrier documents along with notices in lieu of return in a single returns cash letter.

There is no change in the deposit guidelines for forward or return non-machineable items, Canadian items or other foreign items.

Deadlines and availability for submitting non-imageable cash letters remain the same. Pricing of non-imageable items will be at the Mixed cash letter fee for forward items and at the Mixed Qualified Return fee for returns. You can find standard cash letter forms under the forward and return items sections at www.frbservices.org/StandardForms/index.html.

If you have any questions or need additional information concerning these new deposit guidelines, please contact Andy Lueckenhoff, the Eighth District's Check 21 and image specialist, at 1-800-333-0810, ext. 44-8647. ■

Feditorial

Interactive Features on Our Web Site Enhance Two-Way Communication

By Bill Poole, President of the Federal Reserve Bank of St. Louis

Before I became president of the St. Louis Fed, I spent many years in academia. I loved the exchange of ideas and the various debates I had with my colleagues and students.

Since my arrival at the St. Louis Fed in 1998, I've had the opportunity to continue discussing economic issues not only with monetary policy-makers across the globe, but also with you, our Eighth District bankers. You know what I think because my speeches have always appeared on our web site. Now it's your turn to take an active role in these discussions.

Over the years, I've personally answered letters commenting on my speeches and *Regional Economist* articles. To extend the dialog, we began publishing letters to the *Regional Economist* editor earlier this year. Economists love a good debate; so, we publish as many letters as we can even if they do not agree with our position. We do not censor. But when we publish opposing views, we also provide a clear explanation for why we advocate our particular view by clarifying the rationale for our position.

As we complete this calendar year, I am pleased to announce that we will be introducing two other interactive features to our web site: simple polls and online chat.

Although our polls will not be scientific, they will serve more than entertainment purposes. We want to gather your thoughts about the current economic issues and trends we write about in our publications. Here's an example of a poll we might create. All of us are aware of the recent increase in oil prices. In an article on the economics of oil consumption or mass-transit usage, we could place a poll asking you how the increase in retail gasoline prices is affecting your budgets or travel plans.

We also plan to introduce some form of online chat during 2005. Our plan is to sponsor invitation-only chat sessions at which our staff will discuss various regulatory issues, new products and services, and other topics of interest.

These are just a few of the ways we are facilitating two-way communication via our web site. To view or send a letter to the *Regional Economist* editor, visit www.stlouisfed.org/publications/re/letters/default.html. To view or participate in our polls, visit www.stlouisfed.org/publications/. We'd love to know what you think. ■

St. Louis Fed Establishes Fuel Surcharges for Cash Letters

The recent rising cost of fuel products has had a significant impact on business operations at the Federal Reserve. Specifically, because the contracts we have with vendors include fuel-increase clauses, we have seen aviation fuel prices for transporting checks increase substantially. The St. Louis Fed expects significant increases in transportation costs; therefore, we must offset this increase by establishing the following surcharges:

Cash Letters: A surcharge of $0.50 per cash letter will be assessed on all forward and return cash letters that contain Other Fed items. This will include all Mixed and Other Fed items.

Check Relay Network: A surcharge of $0.001 will be assessed for each consolidated item shipped via the Check Relay network.

Private Vendors: We will continue our practice of *not* assessing a surcharge for direct send cash letters sent via private vendors.

These surcharges became effective Dec. 1 and are expected to remain in effect through the first quarter of 2005. The St. Louis Fed will continue to monitor how the cost of fuel affects its business operations and review these surcharges within 120 days. If you have any questions, please contact your account executive. ■

U.S. Treasury's New Investment Option Offers Multiple Benefits

After piloting cash-investment auctions as an additional cash management tool, the U.S. Treasury announced in October 2003 the permanent addition of the Term Investment Option (TIO) to the Treasury Tax & Loan (TT&L) program. Since the program began, the Treasury has conducted monthly TIO auctions and, as of the end of September 2004, has invested $250 billion through 34 auctions.

Everyone who participates in TIO receives a benefit. The Treasury receives additional investment capacity and a greater rate of return on the funds invested. For participating depository institutions, TIO also provides greater flexibility and more certainty.

Terms and Conditions

To qualify for TIO, participants must be TT&L depository institutions in sound financial condition. Like other TT&L investment options, TIO requires that all invested funds be secured with collateral throughout the term of the investment. The Treasury provides a list of acceptable collateral for any given TIO auction in the initial announcement.

The TIO is built on a competitive bidding process whereby participating institutions submit bids for fixed-term investments offered by the Treasury through a secure web site called TERMLink™. TIO participants can bid at any auction. If an institution chooses to bid, it can submit bids in the amount desired—a $10 million minimum bid amount is required—and at the rate(s) it is willing to pay.

The TIO funds typically are offered to participating depository institutions toward the middle of the month, although auctions can occur at any time depending on the Treasury's cash balances. The investment terms typically range from five to 19 days, and the investments either mature toward the end of that same month or the beginning of the following month.

The Investment Process

The TIO typically follows a three-day investment process whereby the Treasury offers, auctions and places short-term excess cash balances with successful bidders.

Announcement: On the first day, the Treasury announces the details of the TIO offering and provides the:

- offering amount and term,
- acceptable collateral,
- auction cutoff time and
- placement date.

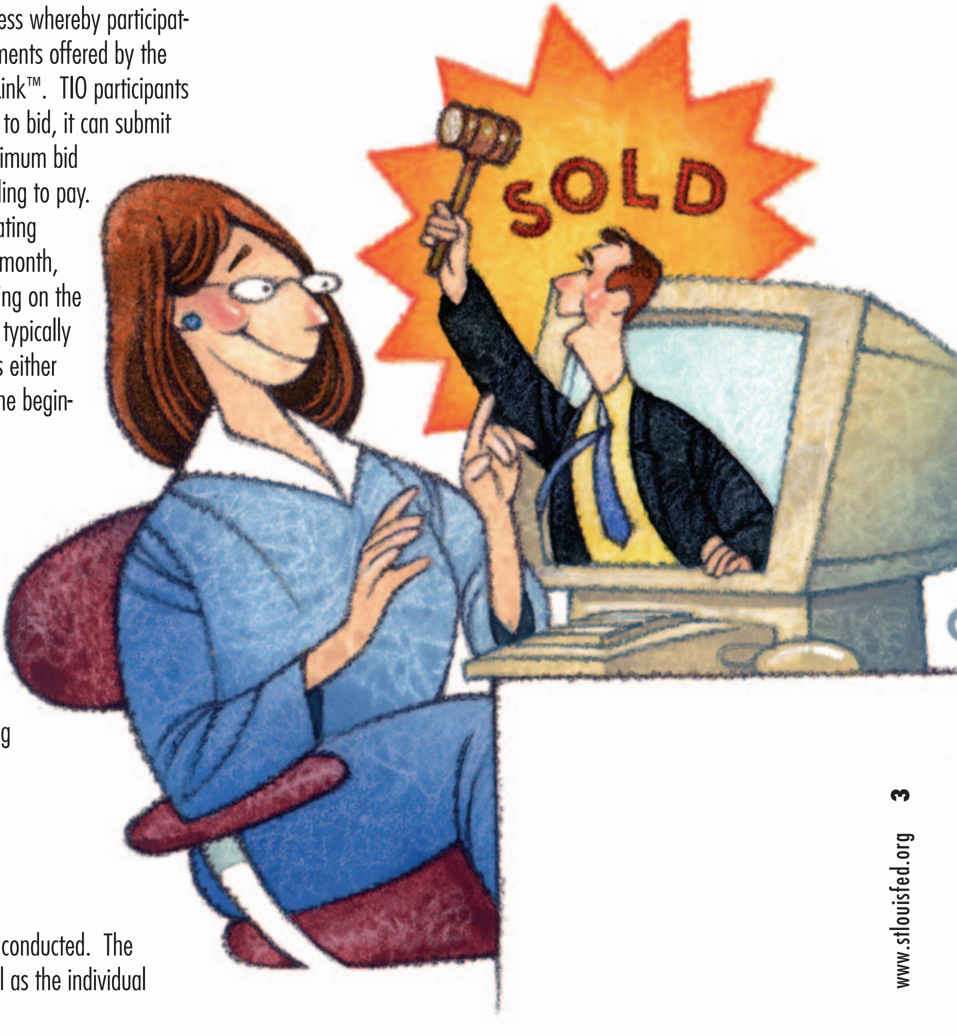
Auction: On the second day, the auction is conducted. The Treasury posts the general auction results as well as the individual award notifications—usually within 30 minutes of the cutoff time—to participating bidders on the secure web site.

Investment: On the third day, the funds are placed. By then, the awarded participants must have pledged sufficient collateral to receive their funds.

How TIO Differs from Other Treasury Investment Options

TIO is different from other investment options in the TT&L program in several ways. With TIO, the auction process determines the interest rate, and the rate is stable over the period of the term. In comparison, the Direct Investment, Special Direct Investment and Dynamic Investment options place cash balances based on a pro-rated format that is determined by participants' investment limits. The TT&L TIP Main and SDI Account Balances may be withdrawn at anytime by the Treasury, which announces each morning any investment or withdrawal actions. Also, funds held in these accounts are assessed interest at the TT&L rate, a floating rate based on the average federal funds rate minus 25 basis points over a weekly cycle.

For more information about TIO, call the Term Investment Hotline at 1-800-333-0870 or visit the Treasury's web site for historical auction information, www.fms.treas.gov/tip. ■



St. Louis Fed Expands Its Community Affairs Staff

As part of the District's new Branching Out initiative, the Community Affairs department has hired one new community affairs specialist at each branch. Here are the branch specialists (new hires in italics):

- **Little Rock:** Lyn Haralson (501) 324-8240 and *Amy Simpkins* (501) 324-8268,
- **Louisville:** Faith Weekly (502) 568-9216 and *Lisa Locke* (502) 568-9292, and
- **Memphis:** Ellen Eubank (901) 579-2421 and *Dena Owens* (901) 579-4103.

Additionally, two new economists will join senior economist Tom Garrett in conducting economic research geared toward the local communities in our District. They are:

- Anthony Pennington-Cross, (314) 444-8592, and
- Chris Wheeler, (314) 444-8566.

Look for announcements about new community-development programs and research on our web site, www.stlouisfed.org/community/. ■

Fed Challenge Is Looking for Local Coaches

Have you ever wondered how you could share your knowledge of economic and financial data with your local community? If so, then coaching a Fed Challenge team may be for you.

Fed Challenge is a national competition designed to bring real-world economics into high school classrooms. During the academic year, local coaches mentor high school teachers by helping them gather research and interpret economic data, which helps prepare the teams for competition

Each performance consists of two parts: a 15-minute presentation before a panel of judges in a mock Federal Open Market Committee (FOMC) forum, followed by a 15-minute question-and-answer session. Following the presentation, the judges will question the team about its analysis, forecast, recommendation and the Fed's role in developing and implementing monetary policy.

The team that wins its area competition advances to the district competition. The district winner then receives an all-expense paid trip to Washington, D.C., to compete in the national competition.

If you are interested in becoming a coach for a local high school team, contact:

- Dawn Griffitts, St. Louis, (314) 444-8421
- Billy Britt, Little Rock Branch, (501) 324-8368
- David Ballard, Louisville Branch, (502) 568-9257
- Jeannette Bennett, Memphis Branch, (901) 579-4104

For more information on Fed Challenge, go to www.stlouisfed.org/education/fedchallenge.html.

New Guide Warns Consumers about Internet "Phishing"

Regulatory agencies have published a brochure, *Internet Pirates Are Trying to Steal Your Information*, to assist consumers in identifying and preventing a new type of Internet fraud known as "phishing." With this type of scam, individuals receive fraudulent e-mail messages that appear to be from their financial institution. The messages often appear authentic and may include the institution's logo and marketing slogans.

These messages usually describe a situation that requires immediate attention and state that customers' accounts will be terminated unless they verify their personal information by clicking on a provided web link. The web link then takes the recipients to a screen that asks for confidential information, including:

- account numbers,
- Social Security numbers,
- passwords,
- place of birth or
- other information used to identify them.

Those perpetrating the fraud then use this information to access consumers' accounts or assume their identities.

The brochure advises consumers:

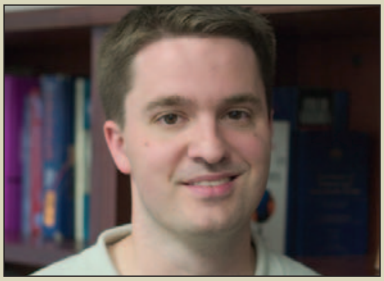
- If you're not sure the e-mail is legitimate, go to the company's site by typing in a web address that you know is authentic.
- If you think the e-mail message might be fraudulent, *do not* click on any embedded link within the e-mail. The link may contain a virus.
- Do not be intimidated by e-mails that warn of dire consequences for not following the sender's instructions.
- If you do you fall victim to a phishing scam, act immediately to protect yourself by alerting your financial institution, placing fraud alerts on your credit files and monitoring your account statements closely.
- Report suspicious e-mails or calls from third parties to the Federal Trade Commission either through the Internet at www.consumer.gov/idtheft or by calling 1-877-IDTHEFT.

The brochure is on the Office of the Comptroller of the Currency's web site, www.occ.gov/consumer/phishing.htm. ■

Does Inflation Targeting Make a Difference?

By Jeremy Piger, senior economist

This article is based on a cover story written for the April 2004 issue of *Monetary Trends*, another publication from the St. Louis Fed.



Over the past 15 years, an increasing number of central banks have adopted explicit inflation targeting as a framework for conducting monetary policy. Inflation targeting takes many forms, but at its heart are:

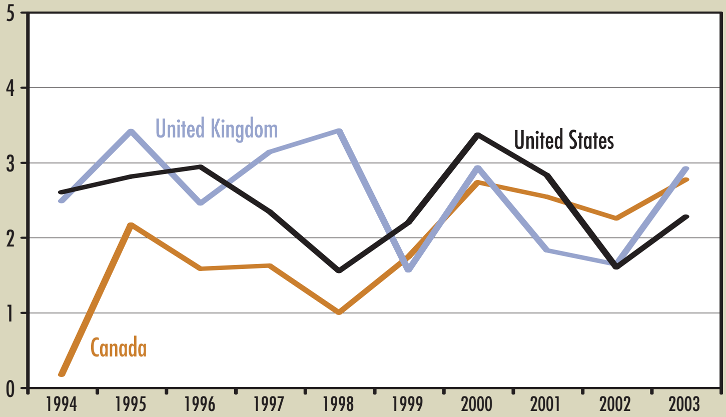
- a statement made by the monetary authority announcing its targeted inflation rate (or range),
- regular communication with the public on the progress being made toward hitting the target and
- mechanisms for holding the monetary authority accountable should it miss its target.

Inflation targeting was adopted by a handful of mainly industrial countries during the early 1990s. Spurred by its perceived success, a large number of countries—including many emerging market economies—have recently adopted inflation targeting.

Despite the popularity of inflation targeting around the world and a general perception that it works, most early research studies found little evidence that the economic performance of non-inflation-targeting countries had suffered because they did not adopt inflation targeting. For example, a landmark study by Ben Bernanke, Thomas Laubach, Frederic Mishkin and Adam Posen found little difference in the macroeconomic performance of inflation targeting vs. non-inflation targeting countries.

The figure shows the inflation rates throughout the past decade in Canada and the United Kingdom—two representative inflation-targeting countries—along with the inflation rate in the United States, the most notable holdout to inflation targeting. At first glance, the figure confirms the notion that inflation targeting does not affect inflation performance because all three countries have experienced relatively low and stable inflation rates.

CPI Inflation Rates in Selected Countries



Digging deeper, however, recent studies have begun to unearth significant performance differences between inflation-targeting and non-inflation-targeting economies. One study by Jeremy Piger, Andrew Levin and Fabio Natalucci found that inflation targeting does affect the public's expectations about inflation. The authors found that the public's expectations about inflation—particularly at longer horizons—under an inflation-targeting regime were "anchored" by the inflation target, that is, the public's expectations about future inflation were less responsive to short-run changes in actual inflation.

The study found that Australia, Canada, New Zealand, Sweden and the United Kingdom—a group of inflation-targeting countries—had a near zero response in their inflation expectations when their countries experienced a real increase in inflation. However, the response from the euro area, Japan and the United States—a group of non-inflation-targeting economies—was much larger and statistically significant.

This is important because the public's expectations also can be self-fulfilling. When people expect higher future inflation, they usually negotiate their expectations into higher pricing schedules and labor contracts. Thus, keeping inflation expectations anchored significantly benefits a country's economy by helping to keep inflation low and stable.

Of course, the case regarding the benefits of inflation targeting is still far from being closed. For example, another recent study by Larry Ball and Niamh Sheridan used an alternative measure of inflation expectations and found smaller differences across inflation targeting and non-inflation targeting countries. There are also potential drawbacks to adopting inflation targeting that might offset any potential benefit from anchored-inflation expectations. For example, some Federal Reserve policy-makers have argued that inflation targeting removes the flexibility needed to respond to changing macroeconomic conditions, as well as unusual events.

Whether the United States would experience a net benefit from adopting inflation targeting is an active topic of debate, both inside and outside of the Federal Reserve. The outcome of this debate will be important in shaping the Federal Reserve's policy framework for the future. ■

FedFacts

FOMC Announces 2005 Meeting Schedule

The Federal Open Market Committee has announced its tentative meeting schedule for 2005:

• Feb. 1-2	• Aug. 9
• March 22	• Sept. 20
• May 3	• Nov. 1
• June 29-30	• Dec. 13

More information can be found at www.federalreserve.gov/boarddocs/press/monetary/2004/.

St. Louis Fed Publishes 2005 Holiday Schedule

The 2005 holiday schedule is as follows:

Monday, Jan. 17	Martin Luther King Jr. Day
Monday, Feb. 21	Presidents Day
Monday, May 30	Memorial Day
Monday, July 4	Independence Day
Monday, Sept. 5	Labor Day
Monday, Oct. 10	Columbus Day
Friday, Nov. 11	Veterans Day
Thursday, Nov. 24	Thanksgiving Day
Monday, Dec. 26	Christmas Day (observed)

Note: New Year's Day does not appear on the 2005 legal holiday schedule because it falls on a Saturday.

Federal Reserve Board Announces Appointments for 2005

The Federal Reserve Board has announced the appointments of the chairmen and deputy chairmen of the 12 Federal Reserve Banks for 2005. In the Eighth District, Walter L. Metcalfe Jr., chairman, Bryan Cave LLP, St. Louis, Mo., was renamed chairman. Gayle P. W. Jackson, managing director, FondElec Clean Energy Group Inc., St. Louis, Mo., was renamed deputy chairman. The list of all appointees can be found at: www.federalreserve.gov/boarddocs/press/other/2004/20041027/default.htm.

New Brochure Explains Overdraft Plans and Fees

The Federal Reserve Board of Governors has published a new consumer brochure called *Protecting Yourself from Overdraft and Bounced-Check Fees.* The brochure explains the different plans financial institutions may offer to help customers when they overdraw their accounts. It also describes the types of fees customers will pay for courtesy overdraft protection, bounce coverage and other such plans. The brochure can be found at www.federalreserve.gov/pubs/bounce/default.htm.

Light-Rail Study Is Available Online

Over the past several decades, cities across America have constructed light-rail systems as a means of reducing traffic congestion and promoting economic development. In his report, *Light-Rail Transit in America: Policy Issues and Prospects for Economic Development,* Fed Senior Economist Tom Garrett discusses whether light rail has lived up to these expectations. The report can be found at www.stlouisfed.org/community/. ■

CalendarEvents

UPCOMING FED-SPONSORED EVENTS FOR EIGHTH DISTRICT DEPOSITORY INSTITUTIONS

Community Development Speaker Series: "Seizing Opportunities for Improving Local Communities"

LITTLE ROCK, ARK.
DEC. 7 AND FEB. 17, 2005

Several well-known experts on revitalizing ailing communities will present the inaugural speeches for the St. Louis Fed's first Community Development Speaker Series. For more information, visit www.stlouisfed.org/community/Speakers_Series.htm or contact Lyn Haralson at (501) 324-8240.

Promises & Pitfalls: As Consumer Finance Options Multiply, Who Is Being Served and at What Cost?

WASHINGTON, D.C.
APRIL 7-8, 2005

The Federal Reserve is hosting its Fourth Community Affairs Research Conference, and the keynote speaker is Alan Greenspan. For more information, visit www.stlouisfed.org/community/. ■

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