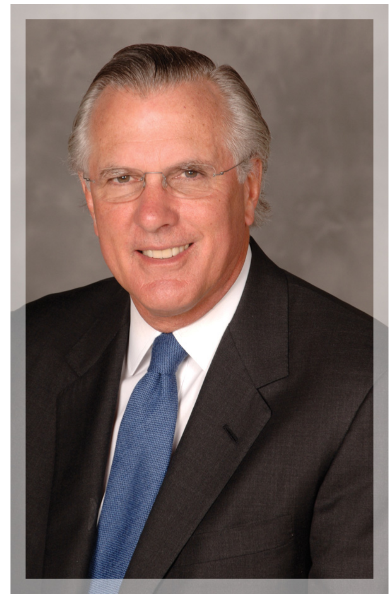
Letter from the President



Nearly four years ago, the Federal Reserve Bank of Dallas took a public stand against what we called the "pathology of 'too big to fail.'" We have worked tirelessly to advance this important issue and keep it at the top of policymakers' to-do lists, advocating an end to too big to fail (TBTF) in speeches, presentations and reports, including the 2011 annual report.

The fact remains, however, that our economy and financial system are saddled with TBTF institutions. Indeed, our financial sector has become ever-more concentrated, with a dozen of the largest banking institutions controlling some 70 percent of industry assets. Five years after the financial crisis unfolded, these behemoth banks continue adversely affecting monetary policy's transmission mechanism and undermining the process of creative destruction, a hallmark of American capitalism that can't fully function among TBTF entities.

It has become increasingly apparent to financial industry practitioners, public policy experts and politicians on both sides of the aisle that the Dodd–Frank Wall Street Reform and Consumer Protection Act—Congress' attempt to combat TBTF—has codified, rather than eradicated, the large banks' TBTF status. The number of rules, regulations and unintended consequences of this presumably all-encompassing law is mind-numbing.

To press the issue further, the Dallas Fed released a special report in January, "Financial Stability: Traditional Banks Pave the Way." The collection of five essays also forms the centerpiece of this year's annual report. The essays outline the virtues of our nation's community banks, as well as the regulatory burden and cost disadvantage the maintenance of TBTF institutions inflicts upon them. We believe our proposed solution would end taxpayer-funded bailouts and level the competitive playing field. I encourage you to read the report in its entirety and spread its message within your respective communities.

The essays and recommendations—and my speech announcing them—have generated significant attention. Interest was so high that public demand temporarily overwhelmed our website. We have received many thought-provoking questions and suggestions. We have drawn on this response to further refine our approach, and accordingly, have added a sixth essay on the Dallas Fed's prescriptions for TBTF and answers to questions that have arisen about our proposal. Both are included in this annual report.

We hope that citizens of the Eleventh District and of this great country can take pride in the Dallas Fed's leadership on this very important issue. We look forward to your thoughts and suggestions as a result of our efforts. We passionately believe that, until we are freed from the stranglehold of TBTF institutions, the American economy cannot reach its highest potential.

Richard W. Fisher
President and CEO
Federal Reserve Bank of Dallas