A Conversation with Gary Richardson

Federal Reserve Historian Seeks to Expand Access to Central Bank Records

Gary Richardson was named historian of the Federal Reserve System in 2012, in advance of the central bank's centennial. An economics scholar specializing in the Great Depression, Richardson discusses his job and how long-secret records can aid policymaking.

Q. What does the Federal Reserve historian do?

Initially, I'm helping with the centennial and working on projects relating to education, public information and research for the centennial. After the centennial will come the second phase: recommending policies regarding the preservation, organization and dissemination of historical materials.

An organization like the Fed needs a historian because it responds to events that are infrequent but very severe. An example would be the financial crisis that began in 2008. The job of the historian is to make sure that after these events occur, you retain the information you need for people to study them. It might take 10, 20, 50 years before you really understand what could have been done, what should have been done and what we should do the next time one of these rare events occurs.

After 2008, we see a big pattern where we've had periods of great success and stability that have ended in big financial crises. We really want to figure out what's going on so the next time we get to a period of great success and great stability, we'll be aware of what the trigger signs are, and we will have a better understanding of how decisions that led to great success could also contribute to the buildup of risk.

Q. What theme from the Fed's first 100 years resonates most with you?

People should recognize how successful the Federal Reserve has been. It's an institution that people don't think about most of the time. That's because it's successful. The payments system works, interest rates are smooth, people can get credit. Financial institutions have plenty of liquidity. Crises come along like 9/11, and the financial system keeps working. This is something people should be amazed by.

The attack on 9/11 was a deliberate attempt by al-Qaida and its leaders to bring down the U.S. financial system. By destroying the World Trade Center, they were hoping to disrupt the operations of financial institutions. The attack failed to have its intended effect in large part because of the courage of the American citizens, the people who lived and worked in New York. It in large part was also through the efforts of the Federal Reserve System and the Federal Reserve Bank of New York, which told people, "We're open, we're operating," and told financial institutions, "We expect you to keep operating. If you have a problem, bring it to us and we'll solve it."

Q. The Fed as an institution is difficult for many people to understand. Its proceedings aren't open to the public. What is the purpose of this opacity, and what challenges does it pose?

The secrecy that we used to think made our policies effective created uncertainty in the long run. And businesses have to react and prepare for that uncertainty. We've learned that by reducing uncertainty in policy, we'll get less volatility, less inflation and better outcomes.

But we still need to keep some things secret. The decisions of the FOMC [the interest rate-setting Federal Open Market Committee] can have a big effect on markets and can redistribute wealth. Financial institutions place big bets—we're talking billion-dollar bets—on the decisions of financial leaders. There's a huge incentive for institutions to get this information. There's a potential for them to earn vast profits; these will be profits that they will be earning at the expense of other financiers. That would really distort the financial system. When we release financial information, we want to do it in a way that creates a level playing field and has the most salient effect on the financial system.

The other side of the Fed is financial regulation and bank supervision. Here opacity is important because we gather information from firms about their financial positions, about their financial strategies and about the state of the economy. This is private information that these firms depend on. To ensure that we get the most accurate information, we have to provide privacy. We have to guarantee that they will not suffer some kind of loss or disadvantage because they provide us with information.

Q. Economist Allan Meltzer's voluminous *A History of the Federal Reserve* is regarded as the definitive work on Fed history. Where do you pick up the story and how do you bring something new?

The Federal Reserve Board of Governors and the System as a whole have over the last 20 years done a great job of opening the archival materials from the

> *"An organization like the Fed needs a historian because it responds to events that are infrequent but very severe. The job is to retain the information you need for people to study them."*

FOMC to researchers. If the goal of the System is just to help Allan Meltzer and other people to do this, then we don't need an economic historian.

You don't have nearly the same amount of historical study of the Federal Reserve Bank of Dallas or the Federal Reserve Bank of San Francisco. This is largely because these Banks have not opened their archives to scholars. The reason that you appoint a historian is that there are important histories that haven't been written, and there are important issues that you want to study more, and the current system isn't allowing those histories to be written.

Q. What are the main contributions of the Federal Reserve Bank of Dallas to the Fed's story? What has distinguished the Dallas Fed from its peers over the last 100 years?

During the 1920s and 30s, there was a lending boom here and in the district to the north, Kansas City, that was focused on agricultural credit. It ended in the 1930s in the Dust Bowl. It seems more relevant today because we did a repeat of this pattern in the 1990s and the 2000s.

Around 1915, the U.S. government began to sponsor quasi-government entities—the Federal Land Bank and the Federal Intermediate Credit Banks. These organizations issued bonds on eastern financial markets to raise funds to make mortgage loans. The mortgage loans were bundled into packages of securities. Mortgage-backed security lending was really big in this district in the 1920s and up until the 1930s, when there was a big collapse.

The Dallas Federal Reserve District also has a unique history in the 1970s and the 1980s. Due to high inflation and interest rate caps imposed by the Federal Reserve Board, a lot of depositors pulled out their money from local banks and sought higher returns elsewhere. Some of this money sloshed up to New England and then, we know, some of it sloshed back down to the Dallas Federal Reserve District. There were big booms here in lending that ended in a big mess in the 1980s. That's really an important issue; we probably should do more short-run studies to understand exactly what happened and how the Fed's policies contributed to the problem and how they ameliorated it.

Q. From the perspective of a historian and economist, how do you think your successors will evaluate policymakers' response to the recent financial crisis?

I'm spending a lot of time reading recent accounts of the financial crisis written by the leading practitioners, critics and scholars. I'm looking at the questions that they are posing and making sure that the System is going to retain the information so that scholars and reporters can answer these questions in the future. Alan Blinder in his book *After the Music Stopped* said there is a key historical question about the financial crisis that historians and economists will argue about for decades: Should the Federal Reserve Board have intervened to prevent Lehman Brothers from failing?

It's not clear how you would answer this question. We see that after Lehman Brothers failed, there was a cascade that swept through its counterparties. There was this massive panic in financial markets. If we had bailed out Lehman Brothers, some other firm could have failed. Or the trigger for the cascade might have been put off a week. It might have been put off a month.

You have to think about all these possible counterfactual scenarios. Decisions were made in a very short period of time in a big pressure cooker and they are all related in very complicated ways.

Q. You've written extensively about the Great Depression. How much of the Fed as an institution reflects that period?

The structure and the powers of the Federal Reserve today strongly reflect amendments to the Federal Reserve Act in the 1930s. You couldn't have had quantitative easing policies without the changes to the structure of the System in the 1930s. You couldn't have had the emergency response in 2008, you couldn't have had a rescue of Bear Stearns, you couldn't have had a rescue of AIG [insurer American International Group] or of Reserve Primary [a money market fund] if you didn't have the reform acts in the 1930s.

Congress gave similar powers to the Federal Reserve that it gives to officers in the armed forces. If you're a general or an admiral, you're under civilian control—you have to follow the rules that the civilian government sets. When we send you out to battle, you're in charge—you have a mission, things are going to happen and your job is to succeed.

When I look at the actions that the Federal Reserve took during the financial crisis, the people who looked really good were decision-makers in the Federal Reserve, the Treasury and other central banks around the world. But I think there was also a lot foresight by the [Depression-era] Congress, which understood how to craft a decision-making structure for the Federal Reserve that could handle crises.

Hear excerpts of the interview at: www.dallasfed.org/research/swe/2014/swe1401c.cfm.