

Operational Highlights

Payments Services Providing innovative and cost-effective services to the financial services industry, the public, and the U.S. Treasury is a primary goal of the Cleveland Reserve Bank. Cleveland's check processing function ranked second among the 12 Reserve Banks in the aggregate cross-sectional unit-cost index, which compares efficiency Systemwide. The same index ranked Cleveland second in the retail payments function. The cash function continued to lead the System in currency processing productivity. All financial services—automated clearinghouse operations, cash services, check processing, funds transfer, and book-entry securities transfer—ranked in the top quartile for lowest unit cost.

The Bank's largest priced service, check processing, achieved a cost-revenue match and met local net revenue targets, which are critical to the Federal Reserve System's ability to meet national-level cost recovery targets. All other priced services met their targets for local net revenue, with the exception of wholesale payments. While the book entry area met its local net revenue target and achieved full cost recovery, the funds transfer area fell short of its target and did not match costs with revenue. All other priced services succeeded in achieving a cost-revenue match; coin wrapping was the exception, due in part to a decision to exit the business.

The Cleveland Reserve Bank assumed a leadership role as the first Reserve Bank to implement the Enterprise-Wide Adjustment (EWA) check processing system. Nationwide use of this standardized check-adjustment processing software will improve service efficiencies across the System, streamline cross-District adjustments processing, accelerate error resolution, and enhance customer service.

The Bank assumed a leadership role in the System to pilot a new cash-ordering application with several depository institutions in the Fourth District. This Web-based application—FedLine® Cash Web—will be instrumental in meeting financial institutions' demand for coin and currency more effectively and improving the efficiency of cash operations.

The Cleveland Reserve Bank implemented a new software package, FedEDI, to make the automated clearinghouse (ACH) a more attractive payment option for a much broader spectrum of banking customers. Through ACH, institutions, firms, and consumers can make direct deposits and payments electronically. However, many banks lack the software to translate electronic invoices into plain English for their corporate customers; the FedEDI software provides the solution by translating this information.

In partnership with the Federal Reserve Bank of Atlanta, the Cleveland Fed continued leadership of the Retail Product Office (RPO), which manages check processing and automated clearinghouse operations for the Federal Reserve System. The RPO played a key role in Y2K compliance for System check processing operations, as well as contingency and event planning. Significant accomplishments were made in national check product development, including standardization of electronic products across all Reserve Banks and progress toward a national check business strategy. The RPO also participated in the check modernization project to standardize check-processing software on an IBM platform.

The Federal Reserve System named Cleveland as its FedLine® for Windows Installation Center. This facility will provide the implementation and security components for all installations of the FedLine® for Windows software across the country.

The Bank was selected as the Federal Reserve System's software application development site for the U.S. Treasury's Savings Bond Architecture Project. This project will equip the System's five savings bond processing sites with heightened capability and flexibility to provide consistent products and customer service.

The Bank forged partnerships with 20 major local utility companies and established collaborative agreements with the San Francisco, Richmond, and Kansas City Reserve Banks to use the automated clearinghouse network as the cornerstone for delivering consumer bills electronically. The Bank developed marketing and operating roles for this new electronic billing and payments opportunity.

The Pittsburgh Office of the Cleveland Bank ranked first in unit cost among the five Federal Reserve savings bond processing sites. A new tracking and control system, which will result in improved quality for the operation, was successfully initiated. In addition, the Bank completed installation of the Regional Delivery System for the five savings bonds sites; this technology, which electronically scans savings bond applications, greatly improves application-processing efficiencies.

Monetary Policy/Research The Bank's staff of research economists advanced its core research areas by contributing original research, sponsoring and promoting research by other economic professionals, and disseminating knowledge to nonacademic stakeholders.

Economic research articles appearing in Bank publications and other scholarly outlets built on strengths in the areas of inflation and inflation-expectations measurement, labor market productivity, and the nexus between the monetary policy, regulatory, and payments systems elements of central banking. These efforts advanced the Bank's goal of becoming a respected contributor to strategic thinking about System policy issues and promoting constructive discourse on those issues in the public domain.

The Bank's staff of research economists had 34 articles published or accepted for publication in scholarly journals and collected works. The department continued to publish *Economic Trends*, *Economic Review*, and *Economic Commentary*, which have a national and international circulation.

The Research Department sponsored five conferences, workshops, educational initiatives, and outreach programs on a variety of topics, including Fed Challenge, the System's nationwide high school academic competition. The department, along with the *Journal of Money, Credit, and Banking*, sponsored a conference on the role of central banks in financial markets, bringing Federal Reserve policymakers together with more than 30 eminent economists from U.S. and foreign universities, the World Bank, and the Federal Communications Commission. A workshop sponsored by the department brought together economists from academia, the International Monetary Fund, and the Federal Reserve to discuss the payments system and central banking issues.

The department's outreach efforts play a key role in interpreting monetary policy and explaining the purposes and functions of the Federal Reserve to the public. Staff economists were the featured speakers at regional business association, bank, financial firm, and university meetings.

In partnership with The Ohio State University, the Research Department developed an inflation-expectations survey designed to measure inflation perceptions by family size, homeownership, gender, education, income, and job status. This survey will lay the groundwork for further study and assessment and will contribute to an improved understanding of inflation perceptions and expectations among Ohio residents and businesses.

The Bank established a planning workgroup for a Central Bank Institute and Education Center. This effort will educate students of all ages about the ways the Federal Reserve affects our economy as a supervisor of financial markets, an administrator of monetary policy, and a facilitator of national payments systems.

The economic research staff has the primary responsibility for supporting the Bank president's membership in the Federal Open Market Committee (FOMC). The staff of research economists reorganized the format for the briefings and continued to provide high-quality analytical support and policy advice to the Bank president in preparation for FOMC meetings.

Banking Supervision and Regulation To ensure the Fourth District's readiness for the Year 2000 rollover, the Bank devoted significant resources to preparedness efforts, aggressively monitoring and assessing District institutions by following Year 2000 examination procedures, and met all Federal Financial Institutions Examination Council (FFIEC) and System Y2K examination guidelines. All Fourth District institutions achieved a satisfactory rating by the end of the third quarter.

The Bank continued to advance its risk-focused supervisory examinations, risk monitoring, and surveillance procedures, an approach that takes into account how banks measure and manage risks in their loan and investment portfolios. Supervision staff completed on-site reviews for 81 depository institutions and service providers (exceeding System deadline requirements) and successfully integrated safety-and-soundness and specialty inspections — a process that assesses all risks within an organization simultaneously.

The Bank continued to maximize the use of technology to improve the overall supervision and regulation process. Advances in the area's knowledge management system, SuperLink, and automated scheduling systems allowed staff to plan examinations more effectively, to identify risks proactively, and to implement the primary and internal point-of-contact program more effectively. These initiatives resulted in fewer on-site examinations, thus reducing the regulatory burden on financial institutions and bank holding companies.

The Bank implemented the Federal Reserve System's supervisory program for large, complex banking organizations. To this end, the Bank strengthened specific examiner team assignments for companies over \$10 billion and matched supervisory skill sets with individual financial services companies' risk profiles and business lines.

The Bank continued to facilitate strong working relationships between financial institutions and community development organizations. Consumer affairs supervision staff conducted outreach programs on FFIEC fair lending procedures and made significant strides in developing surveillance and monitoring

guidelines. In partnership with the Cleveland Restoration Society, the Bank hosted a symposium that explored urban planning and reinvestment.

The credit risk management and data services functions implemented cross-District, as-of adjustments processing and increased their interaction with Bank operating areas to enhance risk identification and cross-functional communications.

The Cleveland Fed's banking supervision, credit risk management and data services staff made significant leadership contributions to policymaking in the Federal Reserve System. These included chairing the National Information Center Steering Committee and the Risk Management Systems Task Force.

Quality Improvements The Cleveland Fed continued to make progress in realizing its strategic vision — to become the best example of a private enterprise serving the public interest. The Bank made substantial advances toward its four corporate goals: efficiency and effectiveness, customer culture, alignment, and leadership. In addition, the Bank advanced its balanced scorecard — the framework for its strategic management system — which ensures that Bank activities and expenditures are aligned with strategic direction and customer needs. The balanced scorecard was enhanced at the corporate and functional levels to track performance against strategic plans.

A cross-functional team was organized to implement customer service initiatives that resulted from transformation efforts and customer surveys. The team assessed recommendations for a formal call-tracking system, certified customer service training, and customer service awards for staff.

The Bank addressed changes in the business environment by undertaking an intensive job-evaluation project intended to align job descriptions and compensation more closely with the marketplace.

The Cleveland Fed contributed to System leadership initiatives in several key areas. The Bank president chaired the Conference of Presidents throughout 1999, and the first vice president served on the System's Information Technology Oversight Committee. The Bank led strategy development for the next generation of

security infrastructure, which will enable the Federal Reserve to conduct business securely over the World Wide Web; made recommendations to revamp the System's cost accounting system; chaired the Executive Development Task Force; and provided leadership resources for the Smartcard for FedLine® project.

The Cleveland Fed spearheaded a workgroup that reviewed contingency plans for all the Reserve Banks' facility and protection functions and assessed the readiness of utility companies across the nation.

Century Date Change Certifying the readiness of internal systems and preparing the U.S. financial system for the Year 2000 were the Bank's highest priorities in 1999. All Federal Reserve System delivery dates and final project milestones were met ahead of System target dates. Staff throughout the Bank participated in comprehensive efforts to ensure that the Bank, the Federal Reserve System, and the banking community were ready for the century date change.

The Bank completed the second and third phases of the supervisory examination process in accordance with established System schedules, and all District institutions were rated satisfactory in their Y2K compliance efforts. Follow-up reviews were completed between August and November, and monthly on-site visits to large bank holding companies took place throughout the fourth quarter. In addition, regular health checks were conducted with banking institutions during the fourth quarter to ensure a successful transition. Examiners were on site at 11 key institutions during the rollover.

Activities in 1999 focused on communication and outreach efforts to ensure banking industry readiness and to strengthen public confidence. Fed representatives conducted seminars for financial institutions in 18 Fourth District cities to provide guidance on Y2K contingency planning, offer updates, explain testing procedures, and answer questions regarding regulatory and readiness issues. A Year 2000 Readiness and Reference Guide was produced to guide banks through test support details, special processing hours, contacts, financial institution responsibilities, and other vital rollover information.

To facilitate century-date-change readiness and public awareness, the Bank maintained high-profile communications with the media to ensure that proper attention and resources were given to Y2K readiness efforts. Further, Cleveland Fed representatives made many appearances before trade associations and community and business groups to help them develop strategies for dealing with the century rollover. Bank staff participated in a series of "Community Conversations" sponsored by the President's Council on Y2K Conversion.

The credit risk management function made significant contributions to the Bank's Y2K efforts by ensuring the liquidity readiness of Fourth District banking institutions. Record numbers of District banking organizations filed the necessary legal documentation to borrow from the Discount Window, in addition to pledging record amounts of borrowing collateral. These readiness efforts gave depository institutions a funding alternative to ensure sufficient transactional liquidity and provided a credit safety net to lessen any potential systemic crisis.

Extensive customer testing confirmed banks' ability to interact electronically with the Federal Reserve in a future-date environment and contributed to the success of the event. More than 540 financial institutions with electronic connections to the Bank scheduled 4,100 century-date-change tests. This high rate of response was a direct result of outreach efforts to institutions that did not conduct testing in 1998.

Internal simulation exercises certified the Bank's readiness and validated communications flows, century-date-change contingency plans, and office automation tools. New guidelines were developed for event management, including local financial institution health checks and problem tracking; proactive customer contact tracking; a skills inventory database; and on-line access to contingency plans. All systems functioned flawlessly throughout the rollover event.