



President Cathy Minehan and First Vice President Paul Connolly view plans for the New England Economic Adventure, the Bank's new interactive learning center for economics, opening in 2003.

## letter from the president

*Change, Challenge, Uncertainty, Commitment.* These four words characterize 2002 for all of us here at the Federal Reserve Bank of Boston.

2002 was a year of major change. It saw the intensification of a number of efforts initiated with other Reserve Banks to improve the products and processes that deliver financial services to the nation. These activities engage about 40 percent of our staff in Boston and Windsor Locks. For some time now, the consolidation of the nation's banking system, advances in technology, and our own ongoing commitment to improving our efficiency in providing these services have driven increased standardization, centralization, and specialization among the Banks. In this process, the Boston Fed has become a System resource in several areas, such as Internet firewall management, check image services, and operational support for Fedwire funds and securities transfers. At the same time, other Reserve Banks have also taken on roles that support operations Systemwide. These have included developing a new standard platform for processing checks, which, as 2003 opened, staff in Boston were busy implementing for the 4 million checks we process each night.

In 2002, we also learned through new Federal Reserve research that the use of checks is declining faster than we had anticipated, while the use of electronic payments is growing rapidly. That new information prompted swift action at all of the Reserve Banks, including the Boston Fed, to prepare our check operations for the future. In this new environment, developing and honing our own unique competencies, while outsourcing other activities, has become even more important. In the meantime, we must meet the simultaneous challenges of making a

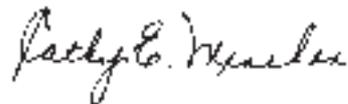
major operational conversion while reducing costs, meeting our efficiency goals, and sizing our operations to the new realities of check. The old paper world of financial services is disappearing rapidly. This change is good for the U.S. economy, but it requires major adjustments on our part as well.

Challenge, uncertainty — the economy has also faced a great deal of both over the past year. The ongoing overhang of the spending excesses of the late 1990s, combined with corporate governance problems and geopolitical concerns, exacerbated market volatility, weakened confidence, postponed spending decisions, and diminished confidence about the future. After a mild recession the previous year, 2002 provided a bumpy start to the recovery, with no job growth and unusual caution on the part of investors and businesses. Since much of the world remains dependent on a U.S.-led recovery, growth in our major trading partners also turned lackluster. With the weather and the situation in Iraq improving, we now look for signs of a more vigorous and sustainable recovery.

The New England economy faces even more challenges and uncertainties than the nation as a whole. Since the beginning of 2001, employment has dropped by nearly 5 percent in Massachusetts, the largest decline in any state. Employment in other New England states has fared somewhat better, but everywhere the hardest-hit sectors were those linked to the boom times of the late 1990s — that is, computers, software, and other high tech manufacturing. Now an upturn in the region depends on improvements in capital spending in the rest of the country. An investment recovery will occur; the question remains when.

Here at the Bank, commitment provided an anchor in the midst of these many changes, challenges, and uncertainties. As always, we remain committed to providing the highest quality financial services, bank supervision, and research for our constituents. As one example, the Bank and its staff have been involved in the challenges facing public education in New England for many years. Last summer our economic conference focused on some of those challenges, exploring educational change in the twenty-first century in this country and around the world. This year's annual report essay focuses on education here in the region, tackling the nature of reforms taking place and assessing progress. Later this year, we plan to open our New England Economic Adventure and Resource Center. This technically advanced facility will demonstrate yet again our continuing commitment to education in general and to economic education in particular.

The Bank is most fortunate to have the assistance of many talented and committed people from around the region who participate on our various advisory boards and work with us in other ways. We owe them our thanks. The members of our board of directors, in particular, play an important role in providing oversight and direction to Bank management. One director retired from the board this year. William O. Taylor, Chairman Emeritus, *The Boston Globe*, served as a director for six years and as the Bank's chairman in 2002. We greatly appreciate Bill's insightful leadership and counsel and wish him all the very best.



Cathy E. Minehan  
President and Chief Executive Officer