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from the
Boardroom

This year's report focuses on innovation and U.S. productivity. This seems especially appropriate for a number of reasons. The remarkable performance of U.S. productivity in recent years is proving to be an enduring story—one that is important to all of us. For the Federal Reserve, understanding the sources of the current productivity boom is central to monetary policy because the potential growth of the economy, something we look at in setting a course for policy, depends directly on productivity growth.

The prevalence of high technology firms in the Twelfth District makes the current episode of productivity growth especially relevant for our region, given that the information technology (IT) producing sectors account for a major part of the current surge. Because productivity is so important, we have devoted a significant amount of effort at the Federal Reserve Bank of San Francisco over the past several years to build our expertise in the areas of innovation, technology, and productivity. This led to the launch in 2003 of the Center for the Study of Innovation and Productivity within our Economic Research department. Their efforts have focused on IT as well as other innovations affecting U.S. productivity such as the way businesses are organized and how they implement the use of IT equipment in the workplace. The center also is looking at the relationship of research and development to productivity in different industries and how productivity gains are reflected in prices, wages, and profits.

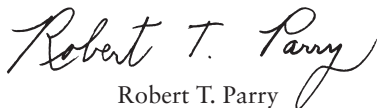
The center's research provides the foundation for our report's main essay, which examines in detail how innovation and productivity are fundamental forces shaping the economy and our standard of living. The essay also looks at the current boom in light of past historical episodes. With the clothing manufacturing and agricultural industries experiencing many of the productivity enhancements shaping businesses today, the report showcases Karen Kane, Inc. and Stahlbush Island Farms, two companies led by former and current members of our boards of directors. The report also looks inside our own doors where new business processes combined with technology and other workplace innovations are shaping how we work at the Federal Reserve Bank of San Francisco.

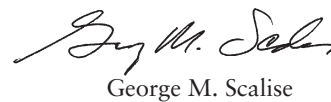
The year 2003 continued to be one of major challenges for our organization as we grappled with ongoing changes in the financial services industry. Facing dramatic declines in check volumes in our District and across the entire Federal Reserve System, we, like other Reserve Banks, focused our attention on cost recovery, revenue generation, and operational improvements. Our employees were asked to meet challenging cost recovery targets, unlike any our District has experienced to date. Despite the difficult circumstances, they met the challenge head on—embracing new approaches to work and bringing forth ideas of their own to surpass our goals for the year. We would like to thank them for their significant efforts.

We also would like to extend our thanks and appreciation to our Twelfth District directors for their invaluable counsel during 2003. The directors' independent assessment of economic and financial conditions throughout our nine western states is critical to the formulation of monetary policy. In particular, we acknowledge the many contributions of Nelson C. Rising (Chairman and Chief Executive Officer, Catellus Development Corporation, San Francisco, California) who stepped down after serving this Reserve Bank in various capacities for more than five years, the last two and a half as Chairman of the Board.

In addition, we would like to express our sincere thanks and appreciation to the other directors and advisory council members who concluded their terms of service during 2003:

- on the Los Angeles Branch Board: Lonnie Kane (President, Karen Kane, Inc., Los Angeles, California) who served as chairman of the Los Angeles Branch Board during two years of his term; Linda Griego (Managing Partner, Engine Co. No. 28, Los Angeles, California)
- on the Portland Branch Board: Patrick Borunda (Principal, The Navigator Group, Yacolt, Washington)
- on the Salt Lake City Branch Board: Peggy Stock (President Emeritus, Westminster College, Salt Lake City, Utah)
- on the Seattle Branch Board: Betsy Lawer (Vice Chair and Chief Operating Officer, First National Bank Alaska, Anchorage, Alaska)
- on the Twelfth District Advisory Council: Richard S. Walden (Chairman, President and Chief Executive Officer, Farmers Investment Company, Sahuarita, Arizona)


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