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## MESSAGE FROM THE PRESIDENT

During 2006, we experienced both challenges and achievements as the way the Federal Reserve carries out some of its essential roles continued to evolve. These changes have been most visible in the financial services we offer to financial institutions, which have been dramatically impacted by technology and other market forces. In response, the Federal Reserve has centralized many operations and designated certain Reserve Banks in leadership roles to oversee the strategic and operational direction of key financial services.

In 2001, our Bank assumed leadership over the Federal Reserve's national Cash Product Office, which directs the central bank's essential role putting new paper bills, or Federal Reserve notes as they're called, into circulation. This year's report examines the life cycle of a Federal Reserve note and the Product Office's role in this area.

Although technology and other factors have influenced how the Federal Reserve's currency business is carried out, cash continues to count—as you'll read in this report. The report provides some interesting statistics about the amount of U.S. currency in circulation and delves into the impact of new technology and banking legislation on the Federal Reserve's vast currency business. The report also describes some

initiatives the Product Office spearheaded in 2006 to address this impact and position the Federal Reserve for the future. Additionally, the report highlights key partnerships with external groups that provide important channels in the currency distribution process.

Our Bank's leadership guiding the Federal Reserve's Cash Product Office is an achievement by any measure, and a range of additional successes and major business milestones are featured in the Highlights of 2006 section of this report.

Our other major operational area, check services, experienced another strong year in spite of considerable change to the operation as a result of the recent Check 21 legislation. In addition to that challenge, we learned early in the year that the San Francisco check processing and adjustments operation had been selected for consolidation in 2007 as part of the Federal Reserve's ongoing national check consolidation effort. This was a necessary decision, but it also was a very difficult one, as it affects a number of employees who have put in many years of dedicated, excellent service. Indeed, their contributions to the success of the District's check function are reflected in our achieving the rank of first place for productivity in check processing for the entire System in 2005 and second place in 2006.

## Message from The President

I recognize that transitions like this are difficult, and in response, the Conference of Presidents of the Reserve Banks extended the involuntary separation program implemented in support of the Federal Reserve's check restructuring.

I also know that accomplishing the Bank's goals in the midst of ongoing change is a challenge for all employees. I would like to take this opportunity to thank them for their commitment and service to this organization and the public.

Turning to the conduct of monetary policy, the year 2006 started off with the fourteenth consecutive quarter-point increase in the federal funds rate, as the Federal Open Market Committee continued its removal of policy accommodation. By August, however, growth appeared to be moderating and the prospects for inflation seemed also to tend toward moderation. Therefore, the Committee voted to pause, leaving the funds rate at 5-1/4 percent, where it ended the year.

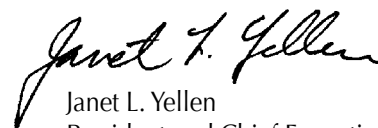
In reaching these decisions, I, like my colleagues around the System, depend on insights from the members of our boards of directors. Their independent assessment of economic and financial conditions throughout our nine western states plays an invaluable role in the formulation of monetary policy, and I thank them for their many contributions.

In particular, I want to acknowledge Barbara L. Wilson, consultant and regional vice president (retired), Qwest Corporation, Boise, Idaho, who completed six years of service on the San Francisco Board of this Reserve Bank, following three years of service on its Salt Lake City Branch Board, of which the final two years were as Branch Board chairman.

In addition, I would like to express my sincere

thanks and appreciation to the other directors and Economic Advisory Council members who concluded their terms of service at the end of 2006:

- *on the San Francisco Board:* Charles H. Smith, former president and chief executive officer, AT&T West, San Ramon, California;
- *on the Los Angeles Branch Board:* Karen B. Caplan, president and chief executive officer, Frieda's, Inc., Los Alamitos, California; and D. Linn Wiley, president and chief executive officer, Citizens Business Bank, Ontario, California;
- *on the Portland Branch Board:* Peter O. Kohler, M.D., president emeritus, Oregon Health and Science University, Portland, Oregon;
- *on the Salt Lake City Branch Board:* William C. Glynn, president, Intermountain Industries, Inc., Boise, Idaho, who served as chairman of the Salt Lake City Branch Board this past year; and Annette K. Herman, vice president, Strategic Initiatives, Uniprise, UnitedHealth Group, Salt Lake City, Utah;
- *on the Seattle Branch Board:* David W. Wyckoff, chairman and chief executive officer, Wyckoff Farms, Inc., Grandview, Washington; and
- *on the Twelfth District Economic Advisory Council:* Thomas E. Cleveland, chairman and chief executive officer, Access Business Finance, Bellevue, Washington, who served as chairman of the council this past year, preceded by three years as its vice chairman; Roberto E. Barragan, president, Valley Economic Development Center, Inc., Van Nuys, California; and Manuel Cunha Jr., president, Nisei Farmers League, Fresno, California.



Janet L. Yellen  
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