

Governing the Governors

(Frisell, Roszbach and Spagnolo)

Discussion

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Well framed

- A very useful review on a little noticed theme
- Sharp summary of theoretical issues, plus a review of evidence of central bank structure around the world
- Recognizes how standard literature on corporate governance is not too useful for central banks unless properly adapted
- Issue of agency costs arising from multiple tasks
- The argument for multiple tasks is weakening

Main contributions

- The theoretical review highlights how charter tasks for CB are ambiguously stated and conflicting
- Lack of clear measures to assess performance; also, unclear governance procedure
- This creates biased incentives
- The descriptive empirical review shows lack of systematic patterns in CB corporate governance
- It strongly rejects the notion that rules are adapted to the quality of the institutional framework; no real differences between OECD and not OECD
- Calls for more public scrutiny on performance measurement

Ideas from standard corporate governance

- What limits abuse by insider decision makers managing outsiders' money ?
 - Laws: but CB is often protected from political intervention
 - Market for corporate control, product market competition do not apply; the CB usually regulates markets, in any case is a monopoly
 - Charters: this is what seems to bind CB
- But what are the measure of performance against which the CB may be judged ?

Theory: what should be the goals of the Central Bank

1. Price stability; measurable, even if effect of policy is subject to delay
2. Financial stability: measurable only in the medium term; may conflict with 1) in short term (e.g. Schoenmaker 1992)
3. Financial efficiency: measurable only in the medium term
4. Stimulate growth; should result from 1, 2, 3, but can be artificially created by monetary choices
5. Internal efficiency (never named)

Empirical Results:

What are the stated goals of CB ?

- Paper documents overwhelming focus among CB stated objectives on stability
- **Stability:**
 - Monetary and bank stability (named as top priority by 65 %)
 - Reliable payment system (top priority by 6 %)
- Financial efficiency (named by none as top priority; almost never singled out)
- These are conflicting goals, in view of the clear trade off between stability and efficiency

Consequences of multiple tasks

- Critical bias in evaluating performance: Financial instability more visible (e.g. to voters) than lack of competition
- The consequences of a multi task agency problem: more attention to measurable task, even at cost of the other task
- CB governance (eg independence) creates a bias towards easily measurable tasks (e.g. inflation), while at the same time it makes harder to assess more opaque policies (e.g. degree of capture by regulated industry)

Moral hazard in CB

- CB autonomy leads to an excessive focus on stability, at the cost of competition
 - Consistent with incentives aimed at measurable outcomes as defined by charter
 - Increases rents for industry players
 - Enjoys political support
- Yet once reasonable price stability is achieved, growth is best supported by efficiency
- Such choices entrench established financial players, reduce entry and economic renewal

Issues for the future

- The stability bias does not question CB independence, but demands more accountability
- Unclear accountability on regulatory tasks
- Better measures of medium term regulatory quality should be developed to assess performance of Central Banks
- Measures of internal efficiency should also be developed

Suggestions

- Develop some measures of CB performance (sorely needed)
- Relate to empirical literature on corporate governance: look at outcomes (e.g. actual dismissals), not rules
- Be explicit about country specific priorities; e.g. do stable inflation countries focus more on efficiency ?
- Multiple board: be more explicit on the trade off between independence and accountability