

Central Bank Governance

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Basic Economic Theory

- Individuals spending other people's money usually do not so do judiciously unless they are subjected to an efficient system of CONTROLS
- These include:

- Efficient competitors (markets)
- Voting with your feet (local governments)
- Checks and balances
- Transparency and accountability
- Tight budget constraints (government agencies)

Which of these apply to central banks?

- One could argue: NONE!
- Still economists say central banks should be independent??
- Incoherence ?
- Capture ?

- The case for independence rests (solely ?) on the «inflation bias» of the political decision process
- Central banks perform many different functions.
- For all functions other than controlling the money supply they should be submitted to the same governance rules as other bureaucracies?

Three dimensions of Governance

- Internal governance: The employees should do what the directors want.
- Transparency: Information about what the central bank does should be correct and **informative**
- External governance: The central bank should do what the public (government?) wants it to do and should do so **efficiently**.

- « The question is whether the oversight exercised by the audit committee should be different (both in scope and in breadth) to that of a commercial corporation. » (p. 12)
- The answer is **yes**.

Reason

- The budget constraint of central banks is very soft (seignorage profits).

- « Recent public sector reforms in industrialized countries were directed toward the internal control function..... how efficiently resources are allocated »
p.10

These reforms never made it to the central banks

- Soft budget constraints of central banks.
- **Indicators**
- (The pension benefits and offices of civil servants versus central bank employees)

- Wage bill of the Canton de Vaud
1995-2005:
 - **+18%**
- Wage bill of the Swiss National Bank
1995-2005
 - **+55%**

- « Effective disclosure and assurances of integrity are at the forefront of the governance debate in central banks striving to balance autonomy and accountability. » (p.11)
- Question:
Do central banks strive to balance autonomy and accountability
or do they want to maximise autonomy?

- One could argue that Mr. Fazio (Central Bank of Italy) liked autonomy more than accountability.
- In Switzerland the Central Bank did not want the salaries of their Directors to be controlled by the central government.

The argument: that would reduce their independence

Question for the future.

- Under the fixed exchange rate regimes central banks got used to hoarding important amounts of foreign currency (and gold) to « intervene on foreign exchange markets ».
- Should central banks keep holding such huge amounts of financial assets?
- What assets should they hold?