

Willem F Duisenberg: Why price stability?

Welcome speech by Dr Willem F Duisenberg, President of the European Central Bank, at the first ECB Central Banking Conference, held in Frankfurt, 2-3 November 2000.

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Ladies and Gentlemen,

It is with great pleasure that I welcome you to Frankfurt on the occasion of the first ECB Central Banking Conference entitled “Why price stability?”.

This new series of conferences that starts today and will be organised every second year is the ECB’s contribution to a process of open interaction between economists concerned by central banking issues. The conference series should serve as a vehicle for signalling the role of the ECB as a key player in central banking, by bringing together researchers from leading academic and international institutions, including the European Parliament, and economists from ministries of finance, central banks in the ESCB, accession countries and also from non-European central banks. One of its main purposes is to launch a process of exchanging views and information on topics that are highly relevant for the policy objectives of the ECB. The topic chosen for this first conference - *Why price stability?* - is particularly relevant for the policy objective of the ECB. This is because price stability in the euro area is a fundamental obligation assigned to the ECB by the Maastricht Treaty. Moreover, by maintaining price stability, monetary policy makes its best possible contribution to the achievement of a high level of growth and employment in the long term.

An important feature of this conference series is that it welcomes the presence of the press. Participation by journalists in this type of conference should provide them with additional background information on monetary policy issues. This should serve to enhance the public’s knowledge of policy-making at the ECB, as well as to further consolidate the ECB’s openness, transparency and accountability.

Last, but not least, the ECB conference series should make a contribution to economic literature through the publication of the conference proceedings in a book. It is also intended to publish even more extensive proceedings on the ECB’s website.

Less than a year ago we organised, together with the Centre of Financial Studies at the University of Frankfurt, the first large, open conference of the ECB on “Monetary policy-making under uncertainty”. On that occasion, I had the opportunity to signal clearly our commitment to a continuous and active exchange of information between the ECB and the academic world. Today, with a track record of almost two years of monetary policy-making at the ECB, I am pleased to note that the collaboration between the ECB and the academic world is becoming closer and more productive every day. In addition to hosting large, open conferences, like the one we are attending today, where academics and policymakers have an excellent opportunity to enrich each other’s views, our economists participate regularly in the leading academic conferences where they contribute their research and participate in highly relevant policy panels. In the summer of 1999, we started our very active Graduate Research Programme through which graduate students spend three months at our headquarters pursuing their dissertation and interacting with our economists. Visitors from the academic world come on a regular basis to discuss their latest work, to present surveys of what is happening on the research front or to directly collaborate with ECB staff as co-authors of research papers.

Overall, the solid bridges that link the ECB with universities and research centres play a key role in the continuous upgrading of our intellectual capabilities and in the deepening of our knowledge of relevant subjects. These interactions are therefore fundamental for the fulfilment of our strong commitment to excellence in economic analysis and research at the ECB, which is reflected in our

series of Working Papers and periodic bulletins. The close collaboration between the ECB and the academic world mirrors what is occurring more broadly between academia and the new knowledge-based industries. It facilitates the continuous elaboration and improvement of a large set of tools that are of utmost importance for decision-making at the ECB, ranging from models for forecasting and policy evaluation to analytical frameworks for monitoring monetary and credit developments.

I wish to stress that such an exchange becomes particularly important and mutually beneficial in the context of the European System of Central Banks. This is because we at the ECB face considerable and historically unique challenges in carrying out our responsibilities. If, in general, a monetary policy strategy that is successful in maintaining price stability is, in the words of Alan Blinder, *“the result of a wise combination of art and science”*, then for us, in the context of the large-scale institutional innovation brought about by EMU, both the art and the science of monetary policy have to perform at their best.

Over the past ten years, the single most important achievement of monetary policy has been the attainment of price stability. Through an admirable and sustained effort of monetary discipline, central banks in both the United States and Europe have overcome the regrettable “Great Inflation” of the 1970s and the early 1980s. But, at the present juncture, the question we should be asking ourselves is not so much “why have we returned to price stability?”, but rather “how did we lose it in the 1970s?”. One element of the explanation that comes immediately to mind is the misconception that there is a permanent trade-off between inflation and output. We are indebted to academic research for showing that the attempts to exploit a trade-off between inflation and unemployment eventually only lead to higher inflation. It thus re-established a firm basis for the concept of the long-term neutrality of money. Indeed, this is a perfect example of an academic insight that has become a deep-seated principle of central banking.

I have mainly spoken to you about the important input that economic research provides in central banking. Let me briefly touch upon the other leg of this exchange, from policy to science, which is by no means less important than the previous one. By facing the challenge of decision-making in real time and in the real world, policymakers continuously uncover a wealth of new intellectual problems that had not been foreseen by science. Moreover, policymakers have a better knowledge of the institutional constraints affecting policy and are therefore able to transmit a sense of realism to economists who analyse monetary policy issues. An additional, less obvious, but very important aspect of this exchange is that policy-making introduces a form of discipline in the science of monetary policy by placing a premium on analytical results that prove to be robust across different approaches. A central bank needs to be very cautious about “jumping on the bandwagon” of any new but untested paradigm that academic researchers, or other observers, may provide. Here I follow Friedrich Hayek and *“confess that I prefer true but imperfect knowledge, even if it leaves much undetermined and unpredictable, to a pretence of exact knowledge that is likely to be false”*.

Let us now engage in the fascinating and fruitful synergy between academics and central bankers. I wish you a very interesting and stimulating discussion and I look forward to witnessing the results.