W A Wijewardena: Central banking nearly six decades after John Exter

Speech by Mr W A Wijewardena, Deputy Governor of the Central Bank of Sri Lanka, Colombo, 20 August 2007.

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Nearly six decades have elapsed since John Exter, founding Governor of the Central Bank of Sri Lanka (then, Ceylon), enunciated his wisdom on and philosophy of central banking. He did so in a report titled ***"Report on the Establishment of a Central Bank for Ceylon"*** which he completed in 1949 as one-man commission on the request of the Government of Ceylon. His ideas on central banking could also be found in his speeches and press conferences during the formative years of the Central Bank. The Report, also known as the Exter Report was published by the Government as a Sessional Paper in November, 1949. The case for a central bank for Sri Lanka has been presented succinctly and cogently in this report. As a mark of appreciation of his work and in recognition of the need for placing a competent skipper on the newly formed organization, Exter was invited by the Government to form the new central bank as its first Governor. Exter is reported to have accepted this offer only for a limited period. True to his word, he resigned from the post of Governor in 1953 and returned to the States.

The Exter Report consists of two parts. Part I presents a lucid summary of the significance of a central banking system for Ceylon. It is in this part that he argued the case for a central bank for the country in preference to a currency board. Part II is a draft bill for the establishment of the Central Bank of Ceylon with explanatory comments. These comments have helped to guide generations of central bankers, in the past, what was exactly meant by each section or clause of the bill. It will continue to do so in the future as well. The commentaries presented were succinct, precise and to the point. They testify to the vast knowledge which Exter had about the functioning of an economy, his reading of the status and the direction of the country's economy, the functioning of a monetary system both in domestic and global economies and how a central bank should be organized and operated. Hence, to understand Exter Philosophy of Central Banking, there is no better document than the Exter Report.

Nearly six decades after John Exter completed the Exter Report, it would be useful to re-visit the report and assess his philosophy of central banking in the context of the body of knowledge of central banking today and identify its relevance to central bankers as guidance. This paper is an attempt at this exercise.

The choice between a central bank and a currency board

Prior to the establishment of a central bank, Sri Lanka was operating under a currency board system in which the country's currency had been backed by 100 percent in foreign reserves maintained with the Reserve Bank of India. Hence, the first choice which Exter had to make was whether to retain the currency board system or go for a central banking system. In a way, he did not have much choice in this regard, because his mandate was ***"to report on the organization and the functions of a Reserve Bank for Ceylon…."*** If he preferred a currency board, he should not have accepted the assignment.

However, like a true professional, he compared and contrasted the two systems before he made his recommendation in favor of a central bank. The report demonstrates that his recommendation was out of conviction rather than the performance of a mere duty.

His choice of a central bank for Ceylon in preference to the continuation of even a reformed currency board system was made on the basis of strong economic arguments.

1. **The higher credit needs of a growing economy**: Currency boards which are restrained by the need for maintaining a 100 % foreign reserve backing for the currency cannot supply enough liquidity to meet trade and other requirements unless the country continues to experience a huge balance of payments surplus year after year. Exter argued that it was not only impossible, but also undesirable to have such a surplus. Impossible because a country cannot continue to maintain a competitive edge over its competitors. Undesirable because freezing foreign reserves does not help the country to attain higher growth or welfare.

2. **Inappropriate reserve maintenance**: A currency board has to maintain its reserves in sterling or in Indian rupee because of the long economic relationship with those countries or economic dependence on them. But, both currencies at that time were not convertible, due to exchange controls imposed in the UK and India in the post-war period.

3. **Adjustment for the future**: Ceylon had at that time applied for the membership of the IMF and one of the requirements to be met once the country gained the membership was to express the value of currency in gold or in a gold-convertible currency. Both sterling and Indian rupee were not gold-convertible.

4. **Limited activities of a currency board:** Currency boards do only the issue of currency. Hence, they cannot supervise banks or take action for the development or the stability of the financial system.

5. **Inability to cope with a wider definition of money:** Demand deposits have become an important part of money supply. Currency boards do not have any instrument to control demand deposits, while a central bank could do so through statutory reserve systems.

6. **Meeting the needs of financial institutions:** Financial institutions need liquidity, reserves and clearing and settlement facilities. Currency boards cannot meet them.

7. **Inability to tackle crisis situations:** Currency boards are “fair-weather” systems and not geared to tackle serious domestic or international crises. For instance, if a crisis demands an expansion of liquidity as its solution, currency boards cannot act in such situations.

8. **Lack of instruments to control an inflationary situation:** If there is a continuous surplus in the balance of payments, a currency board has to necessarily monetize the surplus at the cost of building inflationary pressures. But it does not have instruments to contain it and is reduced to the status of a passive spectator.

In view of the above shortcomings of a currency board system, Exter recommended that Ceylon should establish a central bank with wide powers.

Exter could not be faulted for making this recommendation, since this was the accepted wisdom at that time. The frustration of the newly independent nations regarding their colonial past, the desire to attain economic independence soon to match the political independence and the obvious inflexibility of currency board systems to supply liquidity in a growing trade and payment era would have contributed to the popular belief at that time that the Currency board should be replaced by a central bank.

However, about two and a half decades later when Singapore had to make the same choice, “Dr Goh and the Cabinet chose the path of prudence for Singapore and sought to preserve the Currency Board System for its in-built financial discipline” (***Prudence at the Helm,*** 1992, p 15). Many nations since then, after devastating experiences with undisciplined monetary management, chose for currency board systems to institutionalize monetary discipline by legal means. Ironically, this virtue of a currency board system had not been dealt with in the Exter Report, possibly it would not have been foreseen at that time. However, to the credit of Exter, many safeguards, checks and balances were added to the law establishing the central bank to prevent such undisciplined monetary management by the new central bank. The absence of even a single episode of hyper-inflation or crises of monetary nature during the past 57 years of existence of the central bank is testimony to the efficacy of these measures added to the law.

The role of the new central bank

The mandate given to Exter was, inter alia, to "report on the organization and functions of a Reserve Bank with a view to ensuring, within the limits of monetary action, full employment of the economic resources of the country, and, if need be, on the promotion of supplemental credit institutions in furtherance of this policy…". The mandate itself had recognized that the central bank should facilitate economic development "***within the limits of monetary action".*** This meant that, though short-term economic stimuli could be provided by raising money and credit, the bank should not do that, since it leads to the abandonment of price stability. Any stimulus to be provided by the central bank should, therefore, be practised cautiously and with due regard to its impact on price stability. While emphasizing on the importance of money and credit on an economy, Exter referred to this as **"stable money** which is essential to performance under contracts and to the equitable liquidation of debt".

Within that limitation, the Exter Report has highlighted that ***"the greatest significance of the introduction of a Central Bank lies in the power of the bank consciously to influence the supply, availability and cost of money in Ceylon"***. While this conscious action constitutes monetary policy, it differs from what a currency board does and even from a central bank's creation of money through similar action by foreign exchange operations. Foreign exchange operations are compulsory and a central bank has no choice in that. When commercial banks offer foreign exchange to the central bank, it has to buy that exchange and issue local currency. But, a central bank's credit creation through domestic operations is **discretionary and voluntary.** So, a central bank is in a position to regulate such money creation depending on the situation and the credit requirements of the economy. Hence, Exter did not expect the new central bank to have an open policy of creating money to finance the domestic operations. He wanted such operations to be conducted at the sole discretion of the bank.

Exter also empowered the central bank to examine and supervise commercial banks in order to strengthen the banking system. Such powers would prevent banks from engaging in unsound practices, protect the depositors against bank failures and, with "lender of last resort" facility, provide liquidity in times of crises. Up to the establishment of the central bank, there was no any attempt at regulating commercial banks in Sri Lanka. Hence, Exter was successful in realizing two objectives in a single operation: price stability and banking system stability. While the broad objective of price stability remained unchanged over the years, the banking system stability was expanded to cover the entire financial system and, therefore, today, the central bank has been charged with the responsibility for maintaining financial system stability.

Exter's wish was that the new central bank would consolidate, under one umbrella, all financial operations which had been widely scattered at that time. Thus, the central bank was expected to encourage the public to make greater use of banks to keep their deposits and channel funds to the government securities market by building confidence in same.

While submitting the draft bill on the central bank, Exter remarked that "good central banking is less good law than good practice". What he meant by this is that a central bank should not rely solely on the legal powers given to it. The strict application of such legal powers sometimes leads to the destruction of sound market relationships. To make central bank policy more effective, it has to make its presence felt by others. Exter advised that it should be done ***"through the development of day-to-day relations of confidence and understanding between itself and various banking institutions than through the exercise of all of the powers given it"*** under the law. In other words, he suggested that practicing "moral suasion" would pay more dividends to a central bank than seeking cover under the law.

Caution against the excessive creation of money

Exter belonged to the old guard of economists who believed that economic prosperity cannot be attained by printing money. This was indeed going against the popular tides of the late 1930s and 1940s. At that time, Keynesianism had been accepted by the mainstream economists on both sides of the Atlantic as a new religion. It explicitly advocated the desirability of deficit financing as a strategy for attaining full employment. Exter doubted the validity of this claim both in his public speeches and writings. In this respect, Exter was a loner and belonged to the minority of economists of the day. The fact that there were no supporters for his views did not prevent him from making public what he believed to be true. On the very first day of the establishment of the Central Bank of Ceylon, in a press interview he gave as its first Governor, Exter warned against the use of the Bank for things it cannot fulfill.

"Today, we can only be filled with high hopes for the future. It would be a mistake to expect startling results immediately from the establishment of the Central Bank. There is no financial wizardry by which the Bank can suddenly pull out of a hat a higher standard of living for everybody. The Bank's contribution must necessarily be a long-run contribution. The Bank does not itself produce goods and services, but it should, by creating the right monetary conditions enable the country…" to do so.

What Exter repeatedly maintained was the Central Bank was only a necessary condition for future prosperity. That necessary condition was to be created by maintaining price stability so that the economic agents could make economic decisions based on long-run economic prospects. Since the Central bank does not produce goods and services, it cannot directly get involved in economic activities. It is, therefore, the task of the government and the private sector to take appropriate measures to create wealth in the society. The only weapon of the Central Bank is to print money and such money, by changing the price levels, acts only as an illusion. Hence, Exter thought it necessary to warn those who had been advocating the Keynesian type of ideology to raise government expenditure through printed money.

In the Exter Report, he argued that higher income created through money creation would simply stimulate consumption of imported goods and precipitate serious balance of payments difficulties. A similar view has been expressed by Dr Goh Keng Swee, economic architect of Singapore, when he clarified why Singapore chose a currency board system in preference to a central bank. He says that none of his Cabinet colleagues ***"believed that Keynesian economic policies could serve as Singapore's guide to economic well-being"***. Since Singapore's economy was small and open, ***"financing budget deficits through Central Bank credit creation appeared to us as an invitation to disaster"*** (***Prudence at the Helm,*** p 33). About 25 years before Singapore used this wisdom, Exter argued that, given the underlying domestic production capacity, deficit financing would be an efficacious policy in developed countries that were largely dependent on foreign trade. But, it would not be the case with a developing economy. Hence, the Exter Report highlighted that, "***this should serve as a warning to those who might hope that some of the policies growing out of Keynesian economics can be uncritically adapted to Ceylon".*** As a safeguard, a provision was included in the Monetary Law Act prohibiting the Central Bank to engage in trade or otherwise have a direct investment in any commercial, industrial or other undertaking. In Exter's opinion, such interests would lead to money creation, generate conflicts of interest and prevent making investment decisions based on hard-core economic principles. As such, the Central Bank's involvement in economic activities was considered sub-optimal.

It would be useful to examine whether Exter indeed proposed the necessary legal provisions in the draft bill to facilitate the new central bank to carry on business as per the advice given above. In this respect, it is also pertinent to understand that Exter made his recommendations at a time when the whole world had embraced Keynesian type of deficit financing as the sole remedy for unemployment problem and central banking with power to lend to the government or the economy was the rule of the day. Hence, as he had explained in the Exter Report, he had to adopt a pragmatic approach for the issue. He, nevertheless, proposed checks, balances and limitations for the central bank's credit operations with the government or with the economy.

The following are the provisions and limitations he proposed.

1. Provisions have been made in the Monetary Law Act for the Central Bank to grant provisional advances to the government to facilitate the latter to meet any liquidity shortages in its cash flow. Exter has been criticized for making this provision in the Act, because it amounts to printing new money and making it available to the government to finance its operations. Such provisional advances create reserve money and work opposite to the price stability objective of the Bank. Any neutralization of the adverse effect of such advances has to be done by the Bank through its open market operations. But Exter did not propose to offer an open cheque to the government and limited such advances to 10 percent of the estimated government revenue at any time and made them repayable within a period of six months. He justified his limitation arguing that ***"many central banks and national economies have come to grief because governments have had too easy access to central bank credit"***. Hence, he argued that it would be wise to limit such credit just to meet only the very short term cash requirements of the government arising from seasonal requirements of funds. This wisdom of Exter was not followed and, as a result, provisional advances which were meant to be short term credit facilities for six months became permanent credit. As a result, the level continued to increase to a new high level in each successive year with increased estimates of government revenue. It has, therefore, provided permanent free funding to the government, almost similar to the annual profit transfer which the Central Bank makes to the government.

2. The Central Bank has been authorized to acquire Treasury bills from the primary issues and it, therefore, constitutes another form of lending to the government. The Bank has been prohibited to subscribe to primary issues of or, underwrite, the other types of government securities, viz., Rupee securities or Treasury bonds. Exter justified this prohibition on the ground of the obvious possibilities of abuse by governments. Even the purpose of investing in Treasury bills was not to finance the government but to acquire the necessary liquidity for conducting smooth open market operations. This was explained by Exter as an injunction familiar to central bankers and commercial bankers alike that a bank should look to the liquidity of its portfolio.

An important principle established by Exter has been that the principal use of OMO was to offset the effects of surpluses and deficits in the balance of payments. Since the surpluses of BOP raises money supply and deficits would do the opposite, it is necessary to counter their effects by an equivalent change in the domestic assets of the Bank. Hence, any OMO to siphon off the additional liquidity created by the Bank by increasing its domestic assets first, i.e., by investing in primary market Treasury bills, is contrary to the wisdom expressed by Exter in his report.

Can Exter be faulted for permitting the Central Bank to lend to the government? Though it is completely contrary to the principles of responsible central banking advocated by him elsewhere in the Report, he should be viewed as a pragmatic person. He argued that ***"if the Government were determined, even in the face of opposition by the Monetary Board to make excessive use of Central Bank credit, legal limitations could be relaxed"*** by the government. In such a situation, ***"the Board being a Government agency would have no***

alternative but to comply". Thus, legal provisions are not of any use if governments do not function responsibly and the civil society is weak in resisting such dangerous moves by the governments. He made this point clear in his Report as follows:

"The danger that a government will make use of the power of a central bank to over-expand credit is a real one and might appear a strong argument against having a central bank at all. But, as already indicated, if a government wishes to engage in the irresponsible creation of money, it can do so without a central bank. Paper money has come to stay. The only real safeguard against its abuse is responsible government".

So the blame should not go to Exter. It is the absence of responsible governments that would erode the value of money through excessive creation of central bank credit. An example for such irresponsibility could be found in a reported statement by Robert Mugabe, President of Zimbabwe that, if money is not found for projects, he would print the same, at a time when inflation was rising at more than 4500 % in his country. (***Time,*** 13 Aug 2007)

Elimination of the seigniorage from the books of accounts

The issue of paper based fiat money at a fractional cost of the face value has enabled sovereigns to earn a substantial profit known as the seigniorage. Since there is no requirement for the issuer to back such money with an equivalent reserve, there is no limit to the issue of money by a sovereign. As a result, central banks which have been mandated by sovereigns to issue currency grow like an inverted pyramid: with a very low base as capital and reserves at the bottom and substantially high level of acquired assets through money creation at the top. This pushes a central bank to a very high risk level, when it is viewed from the point of solvency, since an overgrown central bank may not have sufficient assets to discharge its liabilities in a crisis situation.

Exter, having known this fundamental risk faced by a central bank, made provisions in the Monetary Law Act to automatically hide the seigniorage. In terms of these provisions, the printed currency stock in the vaults of the central bank does not become a part of its assets. When currency is issued, it becomes a part of its liabilities with a corresponding asset created in its books. However, when that asset is liquidated, currency issued earlier comes back to the central bank and such currency is taken out of its books by deducting it from the currency issue. Thus, the accounting system prescribed in the Monetary Law Act does not take into account the profits made by the bank in its currency issue. The cost is simply charged to the income account of the bank and eliminated from the books.

On the currency issued, the Central Bank makes a seigniorage. However, that seigniorage is dispersed among all the assets of the Central Bank and cannot be identified for the purpose of paying out to the government. Instead, what is explicitly recorded in the books of accounts is the interest income which the Bank earns on the assets it has created. All costs of the Bank are charged to this interest income and the net surplus is ascertained. That surplus is not automatically paid to the government, since Exter has made specific provisions regarding the appropriation of the profits of the Bank.

In terms of these provisions, there is an order of priority for the appropriation of profits of the Bank.

First, profits should be applied to pay any outstanding amount carried to a Monetary Adjustment Account on account of (a) extraordinary currency issue (b) expenses and interest payments on the issue of Bank's own securities and (c) any interest paid on commercial bank reserves in that unlikely event of the Bank's raising the statutory reserve ratio to 100 percent to fight a very high inflationary situation.

Second, anything remaining after the first appropriation, a reserve should be created to a value of at least 15 percent of the domestic assets of the Bank.

Third, if any profits are left out after the above two appropriations, the remaining profits can be paid to the government.

In terms of the above provisions, the payment of profits to the government is the third and last priority on the scale. Exter argued that that should be the case because of the inflationary or deflationary effects which the payment or the non-payment of profits can have on an economy. For instance, when the profits are transferred to the government, the reserve money will increase, raising both money supply and creating inflationary pressures. Exter argued that such an expansion that would have arisen from the Central Bank's own contribution to inflation by raising its domestic assets should be prevented. Domestic assets of the Bank could go up due to the Bank's lending to the Government or the commercial banks. If these assets have increased too rapidly, the result would be inflation through a similarly rapid increase in money supply. Exter's prioritization of the appropriation of profits intended to prevent the Bank from paying to the government such profits earned by inflating the economy. But, he did not have any objection to the transfer of profits to the government, if such profits have been earned on the Bank's investment of its foreign assets. Since the foreign assets are maintained by the Bank on behalf of the government, the latter have a right to receive its due rate of return. So, Exter concluded that if the domestic assets have not expanded (in other words, if the Central Bank has not inflated the economy), "***there should be no ill-effects from paying out the Central Bank's profits to the Government, especially since in this case the Government could not have been obtaining excessive accommodation from the Central Bank".***

The most important provision relating to the appropriation of profits of the Central Bank is the requirement that the Bank should build reserves out of profits to back its demand liabilities, viz., currency issue and demand deposits maintained by the Bank. Exter's recommendation was that such reserves should be equal at least to 15 percent of the Bank's domestic assets. Such reserves need not be built up against foreign assets, since those claims on the rest of the world would in anyway back the currency and demand liabilities. But, the domestic assets which are created by the Bank at its own discretion have no value in the domestic economy in a severe crisis. Since the build up of the reserves would prevent the transfer of profits to the government, Exter concluded that it would "***prevent them from adding to the expansion of central bank credit".***

Given the ever rising provisional advances granted by the Central Bank to the government and its permanent nature making such advances another form of implicit profit transfer, it is questionable whether the minimum of 15 percent is an adequate backing for the Bank's currency and demand liabilities. For the provisional advances, there is no any collateral placed by the government with the Central Bank. Hence, they are akin to unsecured overdrafts given by a commercial bank to its customers. Since the risk weights given to such unsecured advances exceed even 100 percent, it is necessary for the Central Bank to plan for a higher level of reserves than the minimum 15 percent. The Central Bank management, having taken this prudential requirement into account, has decided, as a part of the Bank's modernization program, to raise the reserve level up to 100 percent of the domestic assets of the Bank. This is being continued by the Bank since 2003 and the reserve level today stands closer to 100 percent. However, it would be prudential to revisit even this percentage today in terms of its adequacy in view of the level of ever rising unsecured provisional advances and Exter's warning that the profits earned by inflating the economy should not be distributed.

The build up of reserves by the Central Bank to be equal to its domestic assets has another monetary dimension. On the liability side of Bank's Balance Sheet, it has liabilities on account of currency issue and demand deposits maintained by commercial banks. These liabilities are known as monetary liabilities, since they constitute the reserve money of the system. All other liabilities, including the capital and reserves, are, therefore, called non-monetary liabilities. When reserves are built-up to be equal to the Bank's domestic liabilities, its monetary liabilities would vary exactly in accordance with the movement of the Bank's net foreign assets. When the Bank raises its net foreign assets, monetary liabilities or the reserve money would increase by an equivalent amount. When the opposite takes place, reserve money would fall. This is similar to the operation of a partial currency board system on a voluntary basis in Sri Lanka.

It is considered a partial currency board system because it backs both the currency issue and the demand deposits of commercial banks by an equal amount of foreign assets. In a currency board system, only the currency issue has to be backed with foreign assets in this manner. Since the system voluntarily practiced by Sri Lanka provides a wider backing than the currency issue, it could be considered as a more prudential system than even a currency board system, provided that net foreign assets always remain a positive number. If they become negative due to the fact that Bank's foreign liabilities are greater than its foreign assets, it poses the bank to a new type of a risk. The risk becomes very much material in a situation where there are continuous balance of payments deficits and if the Bank is required to raise foreign loans to meet the emerging foreign exchange requirements. In this situation, the backing of the monetary liabilities by foreign exchange reserves would sever, making monetary liabilities highly vulnerable to emerging market developments, specifically what would happen to the net domestic assets of the Bank.

When the net foreign assets are negative, it exerts pressure for domestic assets to increase in a compensatory manner, for otherwise, there would be a huge liquidity crunch in the economy adversely affecting all the economic activities. Such a sudden and rapid increase in domestic assets would reduce the ratio of capital and reserves to the domestic assets to unacceptable levels. The corollary would be that both the foreign assets and reserves would fail to back the Bank's monetary liabilities. To mitigate this risk, it may be necessary to maintain the reserve level greater than the value of the domestic assets of the Bank. In other words, capital and reserves of the Bank should be higher than 100 percent of the domestic assets of the Bank.

The independence of the central bank

Central banks have been created by societies to issue the medium of exchange and preserve its value. The power given to central banks as sole issuers of currency is similar to nationalization of money supply. This is an extraordinary monopoly power vested with a central bank. Hence, there is the possibility that this power can be abused by the masters who have given the power to a central bank. Since the history is full of examples of governments' abuse of this power, the question of the independence of central banks has come to the focus. Noble Laureate, F.A, Hayek, arguing that inflation throughout the history has largely been engineered by the governments, made even the suggestion that the central banks should be dissolved and money supply should be de-nationalized (***Denatinalisation of Money,*** Hobart Paperback No 70, 1978). Some have even cynically referred to central banks as "necessary evils". Against this background, the issue of the independence of central banks is of crucial importance. In this regard, the independence of the Central Bank of Sri Lanka has been raised by many at numerous public fora.

The question of Bank's independence has come to limelight due to the Secretary of Ministry of Finance sitting as a vote carrying member of the Monetary Board, the highest policy making body in the Central Bank. The critics have argued that, since he is a government official, he would steamroll all other members of the Board and get the Central Bank to comply with government wishes.

Many have found fault with Exter for making the Secretary to the Ministry of Finance a member of the Monetary Board. The criticism is that the Secretary, acting in his own self-interest, would get the Central Bank to fund the government budget through money creation, thereby permitting the fiscal policy to override the monetary policy. It has been equated by some critics to the case of permitting a child to put his hand into a cookie jar as many times as he wishes. While these criticisms may have some validity, Exter's wisdom was to create an environment for both the government and the Central Bank to have a peaceful and amicable cohabitation. Exter argued in his report that ***"….there are, however, many important problems of monetary policy, especially those relating to fiscal policy, on which a central bank should work in close harmony with the government".*** Accordingly, a degree of independence has been afforded to the Central Bank unlike other governmental bodies. This independence extends to the budget of the Bank, job security of key central bank officials and power to make monetary policy without consulting the government. The wisdom of Exter was that the Central Bank should as far as possible work in consultation with the government, rather than in isolation. He believed that the true independence of the Central Bank could be preserved only through that consultative process. In the words of Exter, **"*the ideal is….one in which there will be continuous and constructive co-operation between the Monetary Board and the government. The principal instrument for achieving this co-operation should be the Permanent Secretary to the Ministry of Finance whose membership on the Board will ensure at all times that his Minister's views will be known to the other members of the Board".*** However, Exter did not expect this arrangement to be effective at all times. Hence, he made the proviso that ***"it would depend on the men occupying the key positions"*** and not on any legal formula. He argued quite correctly that such complex and delicate relationships cannot be established full-blown by a piece of legislation. It must be the result of years of experience and the slow growth of political conventions.

Exter Report testifies to the fact that the independence of the Central Bank should be attained and maintained by people in both the Central Bank and the Ministry of Finance and working with a "moral consciousness" regarding the well-being of the whole society rather than narrow self-interest objectives.

Conclusions

Six decades is a long period during which a society should necessarily undergo tremendous political, social and economic transformation. The onslaughts of new technology, globalization and advancements in fast communication systems have changed the ideals of the people of all societies throughout the globe. Hence, one may tempt to question whether the ideals expressed by Exter more than a half a century ago are still valid and relevant.

Though the ideals of societies have changed, the core principles that are embodied in the philosophy of central banking have not changed over the time. In fact, they have become much more hardened today than 60 years ago. Nations throughout the world have gone for price stability as a necessary prerequisite for continuous prosperity. Hence, the hands of central bankers have been strengthened much more today in all parts of the world to facilitate central banks to function independently and make appropriate policies for monetary stability. The wave of modernization that has swept over almost all central banks in 1990s and in the new millennium is a testimony to this new trend. Hence, John Exter still lives in the core of the hearts of central bankers throughout the world and will continue to do so in the foreseeable future as well.