



Central bank cooperation and the BIS: An insider's perspective*

by

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Objectives of the paper

- Provide a bird's eye view of the history of CB cooperation as reflected in BIS's 75 years of existence
- Answer 3 questions:
 - How did the international monetary and financial environment shape the targets and tools of CB coop?
 - Under what conditions can CB cooperation be effective?
 - Did the BIS make a difference?



Methodological choices

- DO NOT discuss the desirability of CB coop
 - focus on processes
 - positive rather than normative perspective
- Define coop broadly to comprise:
 - purposeful exchange of information (“low-key coop”)
 - joint decisions and implementation (“high-profile coop”)



Outline of remarks

- No time to go over history of the BIS
 - Origin linked to German reparations (1930)
 - Retreat into survival mode following vain attempts to help save the Gold Standard (GS)
 - Resurrection under Bretton Woods (BW), when facilitated operations to keep system afloat
 - Multifaceted support of European journey towards EMU
 - Shift in balance of activities towards financial stability in the post-BW era
 - Gradual transformation into a global institution
- Just focus on the 3 questions



First question

- How did the international monetary and financial environment shape the targets and tools of CB coop?



Our answer

- Targets: consistently monetary and financial stability (MS & FS)
- But the monetary and financial regimes (MR & FR) have deeply affected
 - conception of the tasks
 - balance in the targets
 - tools
- We think of
 - MS as price/exchange rate stability
 - FS as impaired if risk of widespread defaults exists (eg banking/sovereign crises)
- Consider 3 phases
 - Gold Standard
 - Bretton Woods
 - Post-Bretton Woods



1. The Gold Standard

- MR: gold convertibility as ultimate constraint on individual countries and system as a whole
- FR: liberalised financial markets, little regulation and supervision
- MS & FS: perceived as largely coincident concepts for practical purposes
 - MS identified with gold convertibility
 - threats to FS would threaten convertibility
- Target: maintaining gold convertibility
- Tool: mainly regulation of supply and price of liquidity



2. Bretton Woods

- MR: fixed but adjustable rate; gold as (soft) constraint on overall system
- FR: financial repression through administrative controls
- MS: more firmly identified with price stability
- FS: controls kept overt financial instability in check
- In contrast to GS, apparent decoupling between MS & FS
 - exchange-rate from debt & banking crises
 - fixing the exchange rate no longer ensures MS
- Targets
 - re-establish conditions for current account convertibility
 - keep BW afloat
- Tools
 - emergency liquidity lending
 - gold pool



3. Post-Bretton Woods

- MR: unrestricted fiat money
- FR: progressive liberalisation
- MS: after Great Inflation, pursuit of price stability overriding goal
- FS: re-emergence of financial instability with international ramifications
- Targets
 - control of inflation primarily a domestic affair
 - global vs regional (Europe) experience
 - preserving financial stability gains ground (ex ante and ex post)
- Tools
 - sporadic and increasingly less frequent FX concerted intervention
 - emergency international lending
 - codes and standards: eg,
 - prudential regulation and supervision (BCBS)
 - payment and settlement systems (CPSS)
 - improving market information (ECSC/CGFS)



Second question

- Under what conditions can CB coop be effective?



Our answer

- We highlight 3 factors
 - state of international relations
 - standing of CBs and their relationship with governments
 - specific technical nature of the tasks



1. International relations

- International financial diplomacy is a government prerogative
 - CB diplomacy is inevitably influenced by this
- Whole range of conditions over the period
 - very inimical: strained relations in 1930s
 - very favourable: post-war US-led multilateralism



2. The standing of CBs

- Standing influences the degree of legitimacy and support
 - very low: in wake of Great Depression
 - regained: post-war reconstruction
 - very high: after successful fight against inflation
- Degree of CB independence plays a subtle role
 - not much relevant if unity of purpose with government
 - eg, buttressing of BW
 - can be inimical to coop
 - eg, sometimes on global FX issues
 - can be supportive, eg
 - reduction of inflation in Europe
 - development of prudential standards



3. The technical nature of the tasks

- Coop more effective if nature of the tasks puts a premium on CB know-how: eg
 - Lord Norman: managing the GS was a sophisticated affair
 - ditto for the operations to buttress BWs
 - indispensable in prudential regulation, in payment & settlement systems and in market functioning issues



Third question

- Did the BIS make a difference?



Our answer

- On balance, it made a material difference, when circumstances allowed
- The evidence?
 - a priori reasoning
 - revealed preferences
 - specific instances



1. A priori reasoning

An institutionalised setting:

- Provides a neutral and independent secretariat
- Provides greater continuity and depth
- Fosters mutual understanding, helps to build consensus and longer-term personal relationships
- Given a functional banking infrastructure, facilitates speedier decisions at times of need

⇒ low-key coop is the foundation for high-profile coop



2. Revealed preferences

- Regular participation of governors and senior officials
- Efforts to preserve BIS's viability and existence
 - even against governments' opposition (eg WWII)



3. Specific instances

- 1931: Spain turns to Basel, not London and Paris
- 1950s: BIS ideally placed to support EPU
- 1960s: Basel, not Brussels, as location for Committee of EEC Governors
- 1960s-1990s: speed with which international emergency lending was put together
- 1970s-: global prudential regulation originates in Basel
- throughout: resiliency of institution, eg outreach in 1990s



Bottom line

- We are NOT arguing that CB coop would not have occurred without BIS...
 - it predates it, if essentially on bilateral and more ad hoc basis
- ...we are saying that its presence likely facilitated and deepened coop
 - ensuring a degree of continuity and effectiveness otherwise harder to attain