

Central Banks and The Joy of Accountability* .

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15 October 1998

When EMU starts officially, at the beginning of 1999, Wim Duisenberg, President of the European Central Bank, joins Alan Greenspan, Chairman of the US Federal Reserve Board and Mr. Masaru Hayami, Governor of the Bank of Japan, as a member of the select club of heads of central banks whose decisions have global economic significance. The actions of the ECB, and the procedures it adopts, will affect all of us. The success of the EMU project is therefore a central concern for all concerned with national and world-wide economic stability, and not just for supporters of EMU and for long-standing European Federalists like myself.

A necessary condition for EMU to succeed, is for its institutions to acquire political legitimacy. Monetary policy is entrusted to independent central banks as a safeguard against opportunistic behaviour by elected politicians. An independent central bank is a commitment device to ensure that the flexible and powerful monetary stabilisation instrument is not used in the pursuit of short-term electoral or other party-political advantage. The objectives of low inflation, financial stability and sustained growth and employment are best served by removing the interest rate instrument from the rough and tumble of partisan politics. By establishing an independent central bank, executive responsibilities are delegated by the elected political authorities to an unelected body. In a democratic society, such decision making by technocrats is only acceptable and viable if the institution to which these decision are delegated is accountable to the public at large and to its elected representatives.

To be accountable means having to explain and justify your actions. This requires transparent procedures and maximal openness. The Bank of England Act and the evolving procedures established by its Monetary Policy Committee, represents the boldest attempt in central banking history to combine operational independence and accountability. In contrast, the Treaties of Maastricht and Amsterdam, establishing the ECB, and the procedures the ECB appears to be evolving, risk delivering the worst of all possible worlds: a lack of accountability and a framework in which threats to and infringements of independence cannot be identified and neutralised effectively.

The Bank of England has *operational* independence only. Our objectives are set by the elected political authorities, as they ought to be. Monetary policy should not be a partisan political issue. It is, however, the technical, expert pursuit of politically mandated, long-term objectives. The Bank of England is mandated to maintain price

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stability and, subject to that objective, to support the government's economic policy, including its objectives for growth and employment. The operational definition of price stability is also determined by the government. Since the MPC started functioning in June 1997, this objective has been an annual rate of inflation of the Retail Price Index excluding mortgage interest (RPIX), of 2.5 percent. This inflation objective is symmetric: inflation should be neither above it, nor below it.

The ECB also has a price stability mandate, laid down in the Treaties. Unlike the Bank of England, however, the ECB itself decides the operational meaning of price stability. It has recently decided to define price stability as a year-on-year increase in the harmonised index of consumer prices, HICP, of 2 percent or less. This is an *asymmetric* inflation target: inflation should not be above two percent, but it is allowed to be below two percent. In addition, the ECB will have a 'reference value' for a broad measure of annual monetary growth. It will also use a number of other indicators, including an inflation forecast and estimates of output gaps. These will only be used internally and will not be published.

The Bank of England's procedures and decision-making process are highly transparent. The contrast with what the ECB proposes to do is stark.

Should the MPC fail to achieve the inflation target by more than 1 percent in either direction, the Governor, on behalf of the MPC, has to write an open letter to the Chancellor, explaining why the overshoot or undershoot occurred, what measures will be taken to correct it, and how long we believe it will be before we are out of the danger zone. There is no counterpart to this 'open letter' procedure in the arrangements for the ECB.

The Minutes of the MPC, including the voting record of all members, are published. We have recently decided to shorten the publication lag to 2 weeks. The Minutes are a substantive and fair summary of the discussions held by the MPC, but does not contain individually attributed opinions. The reason for this concession to opacity is that if individual opinions were to be attributed, the free and frank exchange of views that now characterises our meetings would be fatally damaged. Members would turn up at the meetings with prepared statements and read these into the Minutes. The real discussion would move to non-audited, informal settings. Once the Minutes are published, however, individual members can be questioned by the Treasury Select Committee about their views. The ECB is proposing not to release the individual voting records for seventeen years. It will publish quarterly reports on the activities of the European System of Central Banks (the ECB and the 11 national central banks of the EMU member states) and an annual report. While it is proposed that the decisions of the ECB Council will be explained to the public, there appears to be no plan to publish the kind of non-attributed minutes released by the MPC.

The Treasury Select Committee can call any member of the MPC at any time to be questioned about the conduct of monetary policy. Not only is the MPC collectively responsible and accountable, its members are individually responsible and accountable. In the case of the ECB, parliamentary control will be exercised through the competent committees of the European Parliament, which can call the ECB President and the other 5 Executive Board members of the ECB. Of course, without knowledge of the individual voting records, Parliamentary scrutiny is likely to be

ineffective. In addition, there are no plans for the European Parliament to question the 11 national central bank governors, who make of the rest of the ECB's Governing Council. Since national political pressures are most likely to be brought to bear on the national governors, this further weakens Parliamentary oversight.

The procedures of the MPC are reviewed by the Non-Executive Directors of the Court of the Bank of England. Their Report will be published in the Bank's Annual Report.

The MPC publishes a quarterly Inflation Report and Inflation Forecast. This publication is one of the key instruments for explaining the MPC's thinking about the monetary policy transmission mechanism and its views on the evolving economic environment. It is also an essential source of information if government, Parliament and the public are to be able to vet the competence of the MPC and its individual members. The ECB plans not to release its inflation forecast.

Of all the transparency issues, the most important is the early publication of the individual votes. In a recent article in the Financial times, Dr. Otmar Issing, a member of the ECB Executive Board, gives his view on this issue, a view shared by Mr. Duisenberg. His key point concerns the multi-national make-up of the ECB Council : "Making individual member's voting behaviour public would encourage undesirable scrutiny of members' voting patterns. This, in turn, would encourage external pressures on the Council members, arising from local interests. Independence, granted by the Treaty, would be at risk.

I share Dr Issing's concerns about external pressures. I reach exactly the opposite conclusion about the implication for the publication of individual voting records. National political authorities and other interested parties *will* try to put pressure on 'their' nationals serving on the ECB Board as well as on 'their' national central bank governors. Although this violates the spirit and letter of the Treaties, it will surely happen. The question is how the ECB Council members can be shielded from such pressures.

Under the procedures the ECB is proposing, the national heads of government will know the individual voting records within five minutes of a vote being taken, regardless of their formal confidentiality. Six Executive Board members, eleven national governors, countless staff and possibly a member of the Commission and the President of the Council, will be present at the ECB Council meetings.

Leaks and other breaches of confidentiality will be the rule rather than the exception. Selective leaking and briefing of the media by individual Council members, behaviour characteristic of a number of continental European central banks in the past, are poor substitutes for proper accountability. The information required to bring effective pressure to bear on individual ECB Council members will be available, *de facto*, to the national pressure groups. That information will not however, be formally available to the European Parliament. Council members will be able to hide behind the formal cloak of confidentiality, thus avoiding having to justify or defend yielding to local political pressures. The inappropriate exercise of pressure is deterred not by secrecy and confidentiality, but only by openness. Smoke-filled rooms and confidentiality are more likely to allow the ECB's independence to be perverted by national political pressures than openness and the occasional short-term

embarrassment that this entails. There can be no effective accountability if the individual votes are not in the public domain.

The ECB has a unique opportunity to break with a long tradition of central bank secrecy and lack of accountability. The European citizen will not put up with the defensive opaqueness that appears to be on offer.