

## Contents

<i>List of Tables, Figures, and Appendices</i>	page xii
<i>List of Contributors</i>	xv
<i>Preface</i>	xvii
1 The State of Play in Central Banking and the Challenges to Come <i>Pierre L. Siklos, Martin T. Bohl, and Mark E. Wohar</i>	1
1.1 Introduction	1
1.2 Part I: Past, Present, and Future in the Conduct of Monetary Policy	2
1.3 Part II: The Scope of Central Banking Operations and Central Bank Independence	6
1.4 Part III: Transparency and Governance in Central Banking	11
<b>PART I PAST, PRESENT, AND FUTURE IN THE CONDUCT OF MONETARY POLICY</b>	
2 Is the Time Ripe for Price-Level Path Stability? <i>Vitor Gaspar, Frank Smets, and David Vestin</i>	21
2.1 Introduction	22
2.2 The Case for Price-Level Stability	27
2.2.1 The Optimality of Price-Level Stability in the New Keynesian Model	27
2.2.2 Price-Level Stability, Zero Lower Bound, and Deflationary Spirals	34
2.2.3 Going Beyond the Basic New Keynesian Model	36
2.3 Two Objections to PLPS	39
2.3.1 Unrealistic Reliance on Credibility	40
2.3.2 Uncertainty and Price-Level Stability	45
2.4 Conclusions	46

3	The Principal-Agent Approach to Monetary Policy Delegation <i>Georgios E. Chortareas and Stephen M. Miller</i>	52
3.1	Introduction	52
3.2	Background, History, and Context	55
3.3	Time Inconsistency, Discretion, and Central Banker Contracts	57
3.3.1	Commitment and Optimal Policy	58
3.3.2	Consistent Policy	59
3.3.3	Explicit Contracts as a Remedy for Time Inconsistency	59
3.3.4	Contracts and the Selfish Central Banker	62
3.4	Selected Literature Review	63
3.4.1	Solutions to Inconsistency of Optimal Plans	63
3.4.2	Monetary Policy under Contracts and Incomplete Information	69
3.5	Conclusion	75
4	Implementing Monetary Policy in the 2000s: Operating Procedures in Asia and Beyond <i>Corrinne Ho</i>	83
4.1	Introduction	83
4.2	The Institutional Aspects of Monetary Policy Decisions	86
4.3	The Operational Objectives of Monetary Policy Implementation	92
4.4	Demand for Reserves	98
4.5	Supply of Reserves	104
4.5.1	Standing Facilities: Evolving Roles	104
4.5.2	Discretionary Operations	109
4.5.3	Putting the Pieces Together	113
4.6	Concluding Remarks: And the Evolution Continues	114
<b>PART II THE SCOPE OF CENTRAL BANKING OPERATIONS AND CENTRAL BANK INDEPENDENCE</b>		
5	Analysis of Financial Stability <i>Charles A. E. Goodhart and Dimitri P. Tsomocos</i>	121
5.1	Introduction: The Financial Stability Role of Central Banks	121
5.2	Historical Development of the Financial Stability Role of Central Banks	122
5.3	The Functions of a Central Bank in the Provision of Financial Stability	127

5.4	Recent Challenges to the Financial Stability Role of Central Banks	130
5.5	Is There a Theoretical Basis for the Conduct of Financial Stability?	133
5.6	Conclusions	141
6	National Central Banks in a Multinational System <i>David G. Mayes and Geoffrey E. Wood</i>	146
6.1	Introduction	146
6.2	Monetary Stability	147
6.3	Financial Stability	148
6.4	Failure Through Loss of Liquidity	149
6.5	Internationalization and Classic LOLR	152
6.6	An International LOLR?	156
6.7	Failure Through Loss of Capital	156
6.8	Dealing with Failure	159
6.9	Cross-Border Institutional Structures that Renationalize the Problem	162
6.10	Cross-Border Institutional Structures with Joint Responsibility	165
6.11	Adequate Powers	166
6.12	Preventing Problems	169
6.13	Cross-Border Financial Markets	173
6.14	Some Historical Evidence	175
6.15	Conclusion	176
7	The Complex Relationship between Central Bank Independence and Inflation <i>Bernd Hayo and Carsten Hefeker</i>	179
7.1	Introduction	179
7.2	The Conventional View of Central Bank Independence	181
7.3	Problems with the Conventional View	182
	7.3.1 Independence and Conservatism	182
	7.3.2 Independence and Accountability	188
	7.3.3 Credibility and Removal of Independence	190
7.4	Alternatives to Central Bank Independence	192
	7.4.1 Fixed Exchange Rates, Currency Boards, and Monetary Union	192
	7.4.2 Inflation Contracts and Targets	193
	7.4.3 Labor Market Institutions	195

7.5	Alternative Explanations of Low Inflation	197
7.5.1	Central Bank Independence Is an Endogenous Variable	197
7.5.2	National Inflation Cultures	199
7.5.3	Political Interest Groups	202
7.5.4	Legal System, Political System, and Factual CBI	204
7.6	Conclusion	209
8	Independence and Accountability in Supervision Comparing Central Banks and Financial Authorities <i>Donato Masciandaro, Marc Quintyn, and Michael W. Taylor</i>	218
8.1	Introduction	218
8.2	Designing Supervisory Governance: Hints from the Central Banking Literature on Monetary Policy	221
8.3	Defining Independence and Accountability in Financial Supervision	224
8.4	Governance of Supervisory Function: Main Findings	228
8.4.1	Sample and Methodology	228
8.4.2	Main Findings	229
8.4.3	Impact of the Location and Comparison with Monetary Policy	235
8.5	The Determinants of Supervisory Governance	238
8.5.1	The Econometric Approach	238
8.5.2	The Results	243
8.6	Conclusions	252
<b>PART III TRANSPARENCY AND GOVERNANCE IN CENTRAL BANKING</b>		
9	The Economic Impact of Central Bank Transparency: A Survey <i>Carin van der Cruijssen and Sylvester C. W. Eijffinger</i>	261
9.1	Introduction	261
9.2	Theoretical Findings	265
9.2.1	Cukierman and Meltzer (1986)	266
9.2.2	Coordination	276
9.2.3	Committees	279
9.2.4	Learning	281
9.2.5	Conclusion on Theory	283
9.3	Empirical Evaluations of Transparency	284
9.3.1	Policy Anticipation	284
9.3.2	Synchronization of Forecasts	286

9.3.3	Macroeconomic Variables	286
9.3.4	Credibility, Reputation, and Flexibility	288
9.3.5	Cross-Country Comparisons	289
9.4	Overall Conclusion	290
10	How Central Banks Take Decisions: An Analysis of Monetary Policy Meetings	320
	<i>Philipp Maier</i>	
10.1	Introduction	320
10.2	The Impact of Committees on Decision Making	322
10.2.1	The Benefits of Committee Decision Making	324
10.2.2	The Costs of Committee Decision Making	326
10.2.3	Implications for Committee Design	337
10.3	Monetary Policy Committees in Practice	338
10.3.1	Clear Objectives and Independence	338
10.3.2	The Structure of the Monetary Policy Meeting	339
10.4	Conclusions	352
11	Institutional Rules and the Conduct of Monetary Policy: Does a Central Bank Need Governing Principles?	357
	<i>Pierre L. Siklos</i>	
11.1	Introduction	357
11.2	The “Wisdom of Men” Versus Rules	361
11.2.1	Trustworthiness in the Central Bank and Its Determinants	361
11.2.2	Central Bank Signaling Costs and Trust	364
11.3	Data and Econometric Specification	366
11.4	Empirical Evidence	372
11.5	Conclusions	378
	<i>Index</i>	393