

Independence of Other Central Banks

- Bank of England is least independent: government makes policy decisions
- European Central Bank: most independent—price stability is its primary goal
- Bank of Canada and of Japan: fair degree of independence, but not all on paper
- trend to greater independence: New Zealand, other European nations

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Explaining Central Bank Behavior

- Theory of bureaucratic behavior
 - is an example of the principal-agent problem
 - bureaucracy often acts in own interest
- Implications for Central Banks:
 - act to preserve independence
 - try to avoid controversy: often plays games
 - seek additional power over banks

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Should the Fed be Independent?

- Case “for”
 - an independent Fed likely has longer-run objectives, politicians don't: evidence is independence produces better policy outcomes
 - avoids political business cycle
 - less likely that deficits will be inflationary
- Case “against”
 - Fed may not be accountable
 - hinders coordination of monetary and fiscal policy
 - Fed has often performed badly

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