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Central Bank Institute Conference
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The Origins and Evolution of Central Banking

Opening Remarks by

Jerry L. Jordan
President and Chief Executive Officer
Federal Reserve Bank of Cleveland

Federal Reserve Bank of Cleveland
P.O. Box 6387
Cleveland, OH 44101

It is my pleasure to welcome you to this conference on "The Origins and Evolution of Central Banking" hosted by the Central Bank Institute of the Federal Reserve Bank of Cleveland.

The Cleveland Fed has a tradition of sponsoring scholarly research on topics that are core to the mission and responsibilities of central banks. Conferences such as this one have been a visible part of that tradition, but this gathering is especially notable as it is the inaugural event for the Bank's newly founded Central Bank Institute.

The Institute represents an attempt on our part to focus some of our resources on the study of central banking, and to leverage our efforts in ways that will encourage other central banks and researchers to pay more attention to what might be called "best practices" in central banking. We will do some research here, and we will promote a network of scholars who can help one another to do better work. We plan to be a source of creativity, inspiration, and information about central banking.

Central banks are worthy of such attention because of their social and economic importance. One way or another, societies will find ways of accomplishing the objectives that are currently assigned to their central banks, even if they are performed by other entities (public and/or private).

Before nations created central banks as we know them today, we relied on private institutions to manage the government's funds and to provide payments services. Price stability was provided through a commodity standard, although that was frequently thwarted by sovereign debasement. Banking supervision was, as it is today in many places, performed by a myriad of governmental organizations exclusive of central banks: state banking agencies, federal banking regulators, SEC-type agencies, insurance commissioners, and the like.

The point is, governments have choices in organizational design and responsibility. In the U.S., the Federal Reserve was preceded by the First and Second Banks of the United States; both ceased to exist after only twenty years. The Federal Reserve Banks are 87 years old this month, and are very different from the original design. No doubt, they will evolve further as they approach their 100th anniversary in 2014.

What we know is that in the future paper will be no more important in the payments system than are metal coins today. Electronically initiated debits and credits will be the way people pay for things. The challenge of keeping down the forgeries and counterfeits will still be there, but, how its done will be very different from a world dominated by paper currency and paper checks.

Collecting deposits and making loans will continue to diminish as the generic business of banking. But, the task of assuring that financial intermediaries are reasonably sound, free of fraud and embezzlement, and not politicized, will still be assigned to someone.

Defining "best practices" for a central bank might seem a daunting task, but the world's central banks, including the Federal Reserve System, have some understanding of what failure looks like. Certainly failure includes circumstances such as periods of inflation and/or deflation that destabilize economic activity and undermine standards of living.

Failure includes financial instability of such proportions that intermediation and risk-bearing services do not facilitate economic growth. Failure includes capital flight and the inability to promote sufficient investment to support economic growth. Failure includes unreliable payment clearing and settlement systems. Failure includes corrupt or politicized financial systems. In recent decades it would not have been very safe to walk down the streets of many places on this earth carrying a sign reading, "I work for the central bank".

When a central bank is perceived as successful in its core missions, it is important to resist the acceptance of assignments that might diminish the likelihood of future success. Central banks could become stretched too thin, or become distracted, the same as any other organization. Throughout the history of central banking nations have differed on the appropriate missions of their central bank. Differing views exist today and will continue to evolve. Governments and central banks appear willing to experiment.

The Federal Reserve System is unusual in taking a three-pronged approach to central banking. At a time when many other central banks are specializing as monetary policy authorities, our mission requires that we perform that job as well as promote an efficient payments infrastructure, and be an effective supervisor of financial institutions and markets. However, the Federal Reserve does not have an explicit price stability target, while many others do. Which approaches will prove to be the better remains to be seen.

Some nations are now closing their central banks, or at least greatly curtailing their activities. A growing list of nations now unilaterally chooses to import their monetary policy from somewhere else. Are there important long-run implications for the exporting central bank? When other nations explicitly or implicitly adopt the U.S. dollar, are they intending to import other parts of the Federal Reserve's domestic mission as well, or will they attempt to achieve those objectives by some other means? We still have much to learn about the institutional design of central banks so that we can see which features of central banking might be complementary, as the borders of nation states become increasingly less relevant to national commerce.

With so many nations experimenting with the purposes and functions of their central banks, the time seems right to establish our Central Bank Institute, initiated by this conference. Among the authors, discussants, and participants are researchers from eminent universities, but also representatives across the Federal Reserve System, from the Central Bank of Chile, the European Central Bank, the Bank of Japan, the Bank of Spain, and the Swedish Riksbank. This opportunity for the cross-fertilization of perspectives on topics of common and vital interest is what the Central Bank Institute is all about.

I should note that this year we have appointed three Institute Scholars-respected researchers who are assisting our Research Department to develop programs and agendas affiliated with the Central Bank Institute. Larry Christiano from Northwestern University and Randy Wright from the University of Pennsylvania are currently serving in these positions. The third Institute scholar is Bruce Smith, who was a driving force behind this conference. On behalf of the Bank, I offer my congratulations and thanks to Bruce for organizing a meeting that so well captures the Institute's vision.

Welcome again to Cleveland. I'm sure this will be a stimulating and useful two days, and I hope you will all join us in future endeavors of the Federal Reserve Bank and the Central Bank Institute.

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