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# ECONOMIC POLICIES AND PRACTICES

PAPER NO. 1

## COMPARATIVE FEATURES OF CENTRAL BANKS IN SELECTED FOREIGN COUNTRIES

MATERIALS PREPARED FOR THE
JOINT ECONOMIC COMMITTEE
CONGRESS OF THE UNITED STATES

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## LETTER OF TRANSMITTAL

OCTOBER 15, 1963.

*To Members of the Joint Economic Committee:*

Transmitted herewith are materials comparing features of central banks in selected countries of Western Europe, Canada, and Japan. This is one of a series of brief studies being planned as aids to an increased understanding of economic policies and institutions in the various industrial countries. While no precise pattern will be followed in releasing this series, I believe that, by making data on various national policies and practices more readily available, members of the committee, other Members of Congress, and the U.S. reader in general, will be aided in understanding our international economic problems within the framework of the enterprise and free market "rules of the game" as practiced in the leading industrial nations.

The summary outlines and country memorandum have been prepared at the Joint Economic Committee's request by the staff of the Board of Governors of the Federal Reserve System, particularly its Division of International Finance. A somewhat similar compilation was prepared by the Division of International Finance for this committee in connection with our 1958 studies on economic policy in Western Europe. The present compilation adds data on additional countries and brings up to date this earlier material. The cooperation of the Board of Governors and its staff is much appreciated.

Faithfully,

PAUL H. DOUGLAS, *Chairman.*

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# COMPARATIVE FEATURES OF SELECTED FOREIGN CENTRAL BANKS

## OWNERSHIP

| | |
|---|---|
| Belgium | 50 percent Government owned since 1948 (remaining shares freely traded on stock exchange). |
| Canada | 100 percent Government owned since 1938. |
| France | 100 percent Government owned since 1946. |
| Germany | 100 percent Government owned since incorporation in 1957. |
| Italy | Majority of shares is held by savings banks, and remainder by several large commercial banks, insurance companies, and social security institutions. |
| Japan | Since the Bank's establishment in 1882, the Government has always owned at least half of the stock. As of March 1962, ownership was divided as follows: Minister of Finance, 55 percent; financial institutions, 3.9 percent; and others, 41.1 percent. |
| Netherlands | 100 percent Government owned since 1948. |
| Sweden | 100 percent Government owned since 1668. |
| Switzerland | Joint stock company; 55 percent owned by cantons and cantonal banks, remainder by a large number of private shareholders. |
| United Kingdom | The entire capital stock of the Bank has been held by the Treasury since Mar. 1, 1946. |

## SELECTION OF GOVERNOR

| | |
|---|---|
| Belgium | Appointed by Crown for 5-year term. |
| Canada | Appointed by Board of Directors, with approval of Government. |
| France | Appointed by Government decree for an indefinite term. |
| Germany | Appointed by the President of the Republic after consultation with the bank's council of directors. |
| Italy | After being approved by the Government (in practice the Ministry of the Treasury), the governor, general manager, and vice manager are appointed by the superior council, which is composed of the governor and the 12 elected directors from the bank's 12 main branches. |
| Japan | The Governor and Vice Governor are appointed by the Cabinet, each for a term of 5 years. |
| Netherlands | Appointed by the Crown for a 7-year term on nomination at a joint meeting of governing board (appointed by Crown) and the Board of Commissaries (appointed by Minister of Finance). |
| Sweden | Elected by the Board of Directors from among its seven members. However, chairman of Board of Directors, rather than Governor, appears to be policy head. |
| Switzerland | A board of 3 directors appointed by the Cabinet on recommendation of Bank Council is responsible authority for operation of Bank. |
| United Kingdom | The Governor and the Deputy Governor are appointed by the Crown upon recommendation of the Prime Minister for 5-year renewable terms. |

## SELECTION OF BOARD

| | |
|---|---|
| Belgium | Appointed by Minister of Finance based on nomination and selection by Bank's council of regents made up of industrialists, professors, trade unionists, and other nonbankers. |
| Canada | Appointed by Government. |
| France | 4 ex officio heads of principal Government financial institutions, 7 appointed by Minister of Finance to represent various economic interests, and 1 representative of the Bank's staff. |
| Germany | Same as governor. |
| Italy | The 12 directors are elected by the stockholders. |
| Japan | Direction of the Bank of Japan is entrusted to 2 executive bodies, the policy board and the board of directors. 4 members of the policy board are appointed by the Cabinet with the consent of both Houses of the Diet; 2 nonvoting members are selected by the Government, 1 from the Ministry of Finance and 1 from the economic planning agency. Members of the board of directors (a minimum of 3, but in practice 7) are appointed by the competent Minister (generally the Minister of Finance) from among persons recommended by the Governor. |
| Netherlands | The Governing Board is appointed by the Crown for a term of 7 years and is responsible for the day-to-day operation of the Bank. The Board of Commissaries supervises the administration of the Bank. |
| Sweden | Board of directors consists of 7 members; chairman is appointed by Cabinet, other 6 directors are chosen by Parliament. |
| Switzerland | A Bank Council of 40 members, 15 elected by stockholders and 25 by the Cabinet, results in considerable governmental influence in decisions and management of Bank. |
| United Kingdom | A Court of Directors of 16 members is appointed by the Crown upon recommendation of the Prime Minister for 4-year renewable terms. The terms of 4 Directors expire each year on Mar. 1. No more than 4 Directors at any time may be employed by the Bank of England. |



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## DISPOSITION OF PROFITS

| | |
|---|---|
| Belgium | Stockholders receive an annual dividend of 6 percent of capital stock. Any remainder is divided 4 ways and allocated to the Government, the stockholders, the Bank's personnel, and the Bank's reserves. |
| Canada | Since reserves ("rest fund") reached statutory limit in 1956, all profits are remitted to Receiver-General of Canada. |
| France | Committed to amortization of advances made by the bank to the Treasury in 1957. |
| Germany | 20 percent to legal reserve until it amounts to 5 percent of note circulation; 10 percent to other reserves up to amount of original capital; 40,000,000 deutsche marks (approxiately $9,500,000) for purchase of certain Federal indebtedness; any remainder transferred to Federal Government. |
| Italy | After allocation of not more than 20 percent of profits to the ordinary reserve, an annual dividend is paid of not more than 6 percent of capital stock. Additional profits may be allocated to the extraordinary reserve (in an amount not to exceed 20 percent of profits) and used to pay a supplementary dividend of not more than 4 percent of capital stock. All remaining profits revert to the Government. |
| Japan | After deductions from surplus for prescribed reserve funds and dividends, the remainder is paid to the Government. |
| Netherlands | All profits transferred to the Government. |
| Sweden | Distribution of net profit determined by Parliament. In recent years, annual net profit has been divided between the Treasury and the Bank's foreign exchange adjustment account. |
| Switzerland | A portion of the gross profit not exceeding 2 percent of the capital stock is paid into the Bank's reserves. A dividend amounting to a maximum of 6 percent of the capital stock is distributed amongst the shareholders. The remainder of the profit is then divided as follows: the cantons receive 80 centimes (22 U.S. cents) per inhabitant; any remaining profit is divided up between the Confederation and the cantons, the Federal Government receiving one-third and the cantons receiving two-thirds. |
| United Kingdom | Paid to the Treasury, to be used exclusively for making interest payments on the national debt. |

RELATION TO FINANCE MINISTRY

| | |
|---|---|
| Belgium | Minister of Finance has right to control all operations of bank, and a Government-chosen commissioner supervises operations to insure that they are conducted in the public interest. Strong personalities in the governor's chair have on occasion demonstrated considerable independence and even influenced trends in Government finance. |
| Canada | Deputy Minister of Finance sits as non-voting member of Board of Directors and its Executive Committee. |
| France | In practice the Government in power influences monetary policy through the National Credit Council of 43 members, including its president, who is a Minister designated by the Government, and its vice president, the Governor of the Bank of France. 17 members represent Government departments or public financial institutions and the remaining 24 are appointed by the Minister of Finance on basis of nominations by economic interest groups. Although formal powers of council are advisory, it effectively determines broad lines of policy. |
| Germany | By law the Bundesbank is "independent of instructions of the Federal Government" although bound "to give due consideration to the general economic policy of the Federal Government and to support such policy within the scope of its tasks." |
| Italy | Subject to Treasury control insofar as Treasury approves appointment of Governor. |
| Japan | The Bank is subject to the central government's authority as exercised through the Ministry of Finance. The Minister of Finance is legally empowered to issue orders to the banks, although this power has not been exercised; and certain matters, such as a change in commercial bank reserve requirements, require his approval. |
| Netherlands | The Minister of Finance is empowered to issue directives to the Netherlands Bank but the Bank has the right to appeal to the Crown in case of disagreement. This would lead to a further careful consideration of the issue by the Government as a whole. |

| | |
|---|---|
| Sweden | Legally responsible to the Swedish Parliament, Bank operates under legislation which expressly prohibits the Bank's directors from receiving instructions from anyone except the Parliament and its Banking Committee. For example, Minister of Finance may meet with directors of the Bank but no decisions may be taken in his presence. However, Bank's formal independence of the executive branch of Government is probably not of great practical significance. The Bank's operational independence has increased greatly in recent years; but its role is that of a participant in the Government's coordinated fiscal, monetary and related economic policies. |
| Switzerland | Influence of Government is considerable and from time to time the Cabinet has prescribed monetary policies for the Bank to follow. |
| United Kingdom | Treasury has authority "from time to time to give such directions to the Bank as, after consultation with the Governor of the Bank, they think necessary in the public interest." |

## ROLE IN GOVERNMENT FINANCE

| | |
|---|---|
| Belgium | Makes funds available to Treasury within a limit of $200,000,000 equivalent. |
| Canada | Bank may buy and sell Government of Canada and Provincial securities. |
| France | Makes loans and advances to Treasury on the basis of special agreements between the Treasury and the Bank placing ceilings on Bank's credit to Treasury. |
| Germany | May make direct advances to a limited extent and, without limit, buy and sell in the open market Federal bonds and bills. |
| Italy | Obligated to make advances for current Treasury requirements up to a limit of 15 percent of budget expenditures. In practice, Government indebtedness to the Bank has been far below legal limit, and has been reduced since 1955. |
| Japan | The Bank of Japan law permits the bank to make unsecured advances to the Government or to subscribe to, or take up, Government debt issues. Because the relatively low yield on short-term Government securities is unattractive to the private financial community, most of this debt is held by the Bank of Japan or various Government agencies. The bank has also held a substantial portion of the Government's other security issues, although the amount has fluctuated sharply in some years. The bank, at present, does not take up, or extend, long-term loans to the Government. |
| Netherlands | Obligated to make advances on current account to the State each time Minister of Finance considers it necessary. Such advances are noninterest bearing but limited to 15,000,000 florins (approximately $4,000,000). Bank holds in addition more or less static book debt of Government growing out of German occupation. |
| Sweden | Performs ordinary fiscal agency functions. The central bank law makes no provision for direct advances to the Government. |
| Switzerland | The Swiss National Bank performs ordinary fiscal agency functions. The Bank has purchased Federal securities for temporary investment of funds and "cooperates" in the placing of new Federal and cantonal funds. |
| United Kingdom | The Bank of England may make direct short-term loans to the Government to cover current budget spending requirements ("ways and means" advances). |

# CENTRAL BANKING IN BELGIUM

## 1. Historical Setting

From the fall of the French Empire (in 1815) until 1830, Belgium was part of Holland. To promote the establishment and use of fiduciary money in Belgium, King William of Holland created at Brussels, in 1822, the "General Society for the Promotion of National Industry," with a limited right of note issue; and for 3 years after Belgium became independent of Holland, in 1830, the Société Générale remained the only bank of issue in Belgium. Owing to difficulties between it and the Belgian Government, the latter, in 1833, estabtablished the Bank of Belgium, with the right of issuing notes to the amount of its capital. Competition between the two banks became intense. The combination of excessive lending by both, and the run on banks caused by the French Revolution of 1848, produced crises for both institutions in that year.

The need for a change became evident, and the National Bank of Belgium was created by law on May 5, 1850, with a capital of 25 million Belgian francs ($5 million), and a 25-year franchise. The law did not endow the bank with a monopoly of note issue, but the privilege was never subsequently given to any other bank, and that of the National Bank of Belgium was successively renewed. In participating in the capital of the National Bank the Société Générale and the Bank of Belgium agreed to withdraw their notes from circulation.

On the whole, the formal status of the National Bank was little changed until 1948. There was, however, a gradual evolution—speeded up in the 1930's—both in the Bank's conception of its task, and in public awareness of the important role of the central bank in economic stabilization.

## 2. Ownership and Control of the Central Banking Institution

From 1850 until 1948, the National Bank of Belgium was privately owned. The law of July 28, 1948, which strengthened the Government's control over the Bank, provided, inter alia, for an increase in the Bank's capital from 200 million (a figure to which it had been gradually increased from its initial capital of 25 million in 1850) to 400 million Belgian francs, of which half would be subscribed by the Government.

The change in ownership, together with certain other changes in the 1948 legislation, clearly strengthened the Government's control of the Bank; it has been said that under the 1948 legislation the Bank was "seminationalized." However, the Government has always had strong influence over the Bank. Since its inception, the Governor has been appointed by the Crown (for a 5-year term), and a Government commissioner supervised operations to insure that they were conducted in the public interest. Article 29 of the pre-1948 statute, which remained unchanged in the 1948 law, provided that "The Minister of Finance has the right to control all operations of the Bank. He can oppose the execution of any measure which would be contrary to law, to the statutes (of the Bank), or to the interests of the state."

### 3. Relation of the Central Bank to the Government

The Government-Central Bank relationship in Belgium has normally been one of harmonious and effective cooperation. The general view appears to be that the Government has seldom abused its control over the Bank; and the latter has spoken out or acted vigorously on many occasions, including several since 1948. One example was the Bank's unsuccessful fight in 1950 to have the "profit" on revaluation of the gold reserve used to reduce Treasury debt to the Bank rather than for new expenditure. Another example was the Bank's adroit handling of the situation which arose in October 1957 when the Government overdrew its account. The Bank secured repayment of the excess in the next few months, and also appears to have used the occasion to force through a reform of certain weaknesses in the capital market and in the banking system which were directly related to Government finance. However, these examples do not prove that the Government's veto power has never been abused, or that its mere existence has not inhibited independence of Bank action. The two examples cited evidence mainly the fact that since 1945 the Bank has had strong personalities in the Governor's chair.

### 4. Relation of the Central Bank to the Commercial Banks

The National Bank of Belgium is empowered to discount, buy, and sell commercial paper, to discount, buy, sell, or make advances against short-term and medium-term Government or Government-guaranteed paper, and to buy and sell long-term Government securities quoted on the stock exchange. While the organic law of the Bank does not require that its activities along these lines be confined to dealings with credit institutions and Government agencies, its operations are largely with such institutions and agencies. Discounts by credit institutions at the National Bank are subject to ceilings established by the Bank.

### 5. Power of the Central Bank Over the Instruments of Monetary Policy

The National Bank's main instruments of monetary policy have been changes in the discount rate and moral suasion. It has not been necessary to use changes in rediscount ceilings as a means of affecting overall bank lending. Bank reserve requirements are established by the Banking Commission. To contain credit expansion, in 1946 the banks were required to keep a high proportion of their deposits in cash and Treasury bills. To increase the ability of the banks to finance the private sector, these requirements were relaxed and modified at the beginning of 1962 and again at the beginning of 1963. Since the beginning of 1962 the Banking Commission has been empowered to impose compulsory cash reserve requirements for banks upon the proposal of the National Bank of Belgium; so far, this power has not been implemented.

Open-market operations in Belgium are carried out by the Securities Stabilization Fund (Fonds des Rentes), which obtains part of its resources via advances from the National Bank. The scope of the Fund's activities was greatly enlarged in 1957 when it was allowed to issue its own certificates and to deal in short- as well as long-term Government obligations. The National Bank nominates three of the six members of the governing body of the Fund; the other three are nominated by the Finance Minister. Any disputes are referred to Parliament.

### 6. Channels or Sources Supplying Business Capital

As in most other European countries, reinvestment of profits is an important source of business capital in Belgium. Another very important source is (or has been) the banks; close connections between banks and industrial enterprises were very highly developed in Belgium, this system tracing back to the early activities of the Société Générale, which was also the first bank of issue in Belgium. During the 1920's and the early 1930's, there was a rapid concentration of Belgian banks, and an intensification of business and banking affiliation, with the result that bank portfolios became heavily loaded with industrial securities. A strong movement toward reform of the banking system culminated in adoption of the banking reform law of 1935, the main purpose of which was do do away with "mixed banking," generally defined as the holding of industrial securities by banking organizations. In substance, and with few and limited exceptions, the reform law of 1935 made it unlawful for any banking corporation to own stocks or bonds issued by other corporations. However, the separation of banking and industry achieved under the 1935 law appears to have been more apparent than real.

Belgium has a number of specialized institutions for assisting in the provision of business capital. Important among these are the Institute for Rediscount and Guaranty, which can discount banking assets not eligible for rediscount with the central bank (which, however, may rediscount bills guaranteed by the IRG); the National Industrial Credit Company (SNCI), which assists in financing new industries, new products, and modernization programs, as well as credit margins in bilateral payments agreements. There is also a National Fund for Credit to Trade and Industry (to provide special credit for small- and medium-sized enterprises), a fund to provide Government guarantees for exports (i.e., guarantees of convertibility of foreign exchange proceeds), a fund for agriculture, and a fund for the provision of mortgage for low credit-cost housing.

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# CENTRAL BANKING IN CANADA

## 1. Historical Setting

The Bank of Canada, established by statute enacted in 1934, was the fourth central bank to be set up in the British oversea dominions, being preceded by South Africa (1920), Australia (1924), and New Zealand (1933). Although the event occurred in the depths of the great depression, it was not motivated by any immediate banking crisis or so much as a single bank failure. Instead, it reflected the rising official involvement in economic affairs, for the Bank was specifically charged from its beginning to "regulate credit and currency in the best interests of the economic life of the nation, to control and protect the external value of the national monetary unit and to mitigate by its influence fluctuations in the general level of production, trade, prices and employment."

## 2. Ownership and Control

Originally founded as a privately owned corporation, ownership passed in two stages to the Government of Canada and since 1938 the Minister of Finance has held the entire $5 million of share capital. The 12 Directors, appointed for 3-year terms by the Minister with the approval of the Governor-General in Council, in turn appoint the Governor and Deputy Governor of the Bank for 7-year terms. The Deputy Minister of Finance sits as a nonvoting member of the Board and its Executive Committee.

## 3. Relation of the Central Bank to the Government

In its capacity as fiscal agent, the Bank of Canada operates the Government's deposit account through which flow virtually all Government receipts and expenditures. Responsibility for debt management policy rests with the Government, but the Bank arranges for the sale of new Government securities and manages all work connected with the outstanding public debt. Similarly, in the field of foreign exchange, the Minister of Finance carries responsibility for policy but the Bank handles the Government's foreign-exchange business, including the transactions of the exchange fund account. Through Board contact with the Deputy Minister of Finance as well as less formal relationships, the Bank is well placed for close and continuous consultation with the Government in the interest of maintaining suitable and properly coordinated monetary, fiscal, and debt-management policies, while maintaining its preeminent responsibility in monetary affairs.

Following a recent period of strained relations between the Bank and the Government, the newly appointed Governor of the Bank issued a clarifying statement on his view of their respective areas of authority. In the day-to-day conduct of monetary policy, the Bank must be sufficiently independent to withstand pressures from any source. But "if there should develop a serious and persistent conflict between the views of the Government and the views of the central bank with regard to monetary policy which, after prolonged and conscientious efforts on both sides, cannot be resolved," the Government's view would have to prevail and the Governor, if he could not in good conscience carry out the Government's directives, would be under obligation to resign.

### 4. Relation With Commercial Banks and Power Over Instruments of Monetary Policy

Pivotal to monetary control are the reserve requirements imposed upon commercial banks. By statute, the chartered banks must maintain cash reserves (Bank of Canada notes or deposits) equal to 8 to 12 percent of the bank's Canadian dollar deposit liabilities on a monthly average basis; by agreement with the Bank of Canada in 1956, the chartered banks also maintain liquid assets (cash, day-to-day loans, and Treasury bills) at a ratio of 15 percent to their deposit liabilities. These reserve ratios are rarely altered. Prior to June 1962 the bank rate at which the central bank makes temporary advances to chartered banks (and to money market dealers under securities purchase and resale agreements) floated at one-fourth of 1 percent above the latest weekly average tender rate for 91-day Treasury bills. Within this framework, changes in the Bank of Canada's holdings of Government of Canada securities, through their effect on the cash reserves of the banking system, provided the chief instrument by which the central bank sought to ease or tighten monetary conditions. As part of the austerity program announced on June 24, 1962, the Treasury bill yield ceased to be linked with the bank rate and the latter has assumed an independent role in monetary policy. Moreover, in a banking system where three chartered banks account for 70 percent of total bank deposits, "moral suasion" has a larger role to play than under U.S. conditions.

### 5. Channels or Sources Supplying Business Capital

Exceptions to the longstanding rule against lending upon security of real property, incorporated in the Bank Act in 1944 and 1954, allow the Canadian chartered banks to participate in Government-guaranteed loans to farmers and fishermen, for housing constructed under the National Housing Act, and to lend to oil companies on the security of oil "in, under, or upon the ground" and production equipment. Provision of working capital to business enterprises has been a traditional function.

The Industrial Development Bank, established in 1944 as a subsidiary of the Bank of Canada, may extend financial assistance to industrial enterprises, in the form of loans, guarantees, etc., in instances where credit or other financial resources would not otherwise be available on reasonable terms and conditions. Loans and investments are also extended through a complex of private financial institutions, including loan and trust companies and insurance enterprises.

## CENTRAL BANKING IN FRANCE

### 1. Historical Setting

The Bank of France was organized by Napoleon in 1800 as a privately owned company engaged in general banking business. In 1803 it was given a monopoly of note issue in the Paris area, and in 1848 that monopoly was extended to all of France. In 1806 a General Council consisting of a Governor and 2 Vice Governors appointed by the chief of state, and 15 regents, and 3 examiners elected by the 200 largest stockholders, was established as the chief governing agency of the Bank. This formal organizational structure of the Bank of France did not change for the next 130 years, but in the course of time actual power swung from the Government at the time of Napoleon to private interests as represented by the regents in the early 1930's. In 1936, following the victory at the polls of the "Popular Front," which had made the power of the "200 families" a major political issue, legislation was passed which gave the Government the dominant position in the management of the Bank, mainly by reducing the number of members of the General Council elected by the stockholders from 18 out of 21 to 2 out of 20. Effective January 1, 1946, the Bank of France was nationalized, the shareholders receiving negotiable Government securities in exchange for their stock.

### 2. Ownership and Control of the Central Banking Institution

The General Council of the Bank of France consists of the Governor, the two Vice Governors, four ex officio members who head the principal Government financial institutions, seven members appointed by the Minister of Finance to represent various economic interests, one representative of the Bank's staff, and two examiners without vote on policy matters. The eight members representing economic interests and the Bank's staff are appointed for 4-year terms, which are staggered. The Governor and Vice Governors are appointed by Government decree, and have indefinite tenure.

The capital stock of the Bank is owned entirely by the state. The profits of the Bank are committed for a long and indefinite period to amortize advances made by the Bank to the Treasury in 1957.

### 3. Relation of the Central Bank to the Government

Because the Bank of France is nationalized and because its Governor does not have tenure for a specified period, the Government has strong ultimate power over monetary policy. In practice the government in office influences monetary policy through the National Credit Council, which is the primary authority for framing credit policy and banking controls. The National Credit Council was established in December 1945 by the same law that nationalized the Bank of France. The

Council has 43 members, including its President, who is a Minister designated by the Government, and its Vice President, the Governor of the Bank of France. Seventeen members of the Council represent Government departments concerned with economic problems, or are heads of public or semipublic financial institutions. The remaining 24 members represent various economic and financial interests, and are appointed by the Minister of Finance or the Minister of National Economy on the basis of nominations by organizations representing those interests, such as chambers of commerce and labor federations. The policies of the government in office are presented to the National Credit Council by the Director of the Treasury who, though not a voting member, is required by law to attend all meetings of the National Credit Council and its committees. The President of the Council, who is usually the Minister of Finance, rarely attends its meetings, and the presiding officer is normally the Governor of the Bank of France.

The National Credit Council has extensive power to regulate the operations of all classes of banks, this power being exercised through the agency of the Bank of France. In matters of monetary and credit policy the Council formally has power only to advise the Government and the Bank of France. In practice, however, it appears that the broad lines of monetary policy are laid down in the National Credit Council, although it is important to bear in mind that the Governor of the Bank of France has a key position in that body.

### 4. Relation of the Central Bank to the Commercial Banks

The Bank of France is empowered to discount commercial paper and Government securities for private individuals and enterprises, all classes of banks, and public and semipublic financial institutions provided that maturities do not exceed 3 months and the commercial paper bears three signatures. The Bank rediscounts short-term paper for the commercial banks and buys from them limited amounts of money market paper. It rediscounts medium-term (2 to 5 years) paper for public and semipublic credit institutions; in most instances, these latter institutions have previously rediscounted such paper for banks. Transactions with individuals and business enterprises have nearly disappeared. Paper exceeding 3 months' maturity is divided into a series of 90-day instruments before being rediscounted by the Bank of France.

### 5. Power of the Central Bank Over the Instruments of Monetary Policy

Within the policy framework established in the National Credit Council, the General Council of the Bank of France makes the important decisions of the Bank. The twin pillars of French credit controls are (1) the terms applied to rediscounts of short-term commercial paper, and (2) the minimum liquidity coefficient of the banks. The Bank places ceilings on rediscounts of short-term commercial paper, and penalty rates higher than the basic discount rate are applied to rediscounts in excess of the ceilings. Changes in both the rates and the ceilings have been frequent. There are no ceilings on rediscounts of export paper or medium-term paper. The liquidity coefficient, first introduced in early 1961, is the relationship between deposit liabilities and certain assets, mainly cash and equivalents, Treasury bills, medium-term paper, and export paper. A subsidiary requirement of the banks, dating from 1948, stipulates a minimum ratio of deposits to holdings of Treasury bills alone.

The Bank of France's open-market operations are of marginal importance and are totally different in character from those known in the United States. Under this head the Bank of France stands ready to buy from banks, up to fixed limits, Treasury bills, bankers' acceptances, and other types of money market paper. It also intervenes in the market on its own initiative but only to smooth out daily fluctuations.

## 6. Channels or Sources Supplying Business Capital

Apart from banks, the securities market and retained earnings, there are three important sources of medium- and long-term business capital in France. One of these is the Bank of France, which since World War II has rediscounted medium-term paper for the public and semipublic credit institutions. Most of this paper originates with the banks, which rediscount it with the aforementioned credit institutions.

Second, the public and semipublic credit institutions extend large amounts of financing with their own resources as well. The Crédit Foncier de France and its subsidiary, the Sous-Comptoir des Entrepreneurs, extend credits almost entirely for construction. The Crédit National makes equipment loans to industry, and the Caisse Nationale de Crédit Agricole is concerned with agricultural credit. The Caisse des Dépôts et Consignations extends credit for housing and industrial equipment and also rediscounts a large amount of credits initially granted by the other public and semipublic institutions. This organization is the repository of all the funds deposited in French savings banks; besides making loans to business and rediscounting it also makes funds available to the local authorities and the Treasury. In addition to savings deposits, the main sources of funds for the public and semipublic credit institutions are contributions from the budget, public bond issues, and retained earnings.

Finally, the Treasury itself is a very large lender of funds for housing and the equipment needs of industry.

# CENTRAL BANKING IN GERMANY

## 1. Historical Setting

The Reichsbank, Germany's first central bank, was established in 1876, but because Federalist forces in Germany insisted upon the right of other banks to continue to issue bank notes it was not until 1935 that the Reichsbank obtained the note issue monopoly. Following the First World War, the Reichsbank was reorganized under the auspices of the Dawes Committee, largely to make it more independent of the Government, and it continued to operate, as reorganized, until 1948. In 1948, the Bank deutscher Laender was set up as an interim bank, pending the founding of a new German state. The Bank deutscher Laender maintained no branches and the Landeszentralbanken, the central banks of the individual German Laender (States), carried out its functions, including that of note issue. It was not until August 1957 that the current German central bank, the Deutsche Bundesbank, was established. The Bank deutscher Laender then ceased to exist and the Landeszentralbanken became branches of the Deutsche Bundesbank.

## 2. Ownership and Control of the Central Banking Institution

The capital stock of the Bundesbank totals DM290 million and is owned entirely by the Federal Government.

The main organs of the Bundesbank are the Central Bank Council, the Directorate, and the Boards of Management of its branches, the Landeszentralbanken. The Board of Management of each Landeszentralbank directs all transactions and administrative business of the Bank in its area. The Directorate of the Bundesbank is composed of the President, the Vice President and no more than eight additional members possessing special professional qualifications, all of whom are appointed by the President of the Federal Republic after consultation with the Central Bank Council. The Directorate is responsible for the implementation of the decisions taken by the Central Bank Council and generally administers the Bundesbank. The Central Bank Council, which consists of all the members of the Directorate and the presidents of the Landeszentralbanken, determines the monetary and credit policies of the Bundesbank.

## 3. Relation of the Central Bank to the Government

The Bundesbank is legally an autonomous Federal institution. The law states that the Bank "insofar as is consistent with its functions, shall be bound to support the general economic policy of the Federal Government," but that in the exercise of its legal powers it "shall be independent of instructions of the Federal Government." Members of the Federal Government are entitled to participate in the deliberations of the Central Bank Council. They have no vote but they may introduce motions and force the delay of a decision, but for not more than 2 weeks.

It is the duty of the Bundesbank to advise the Federal Government on all matters of importance in the area of monetary policy and to furnish information to the Government upon request. Furthermore, the law which established the Bundesbank states that the Federal Government must include the President of the Bundesbank in its deliberations on matters of importance in the field of monetary policy.

The Bundesbank must limit the amount of credit which it extends to the Federal and Laender Governments and to the Federal Government's special funds.

### 4. Relation of the Central Bank to the Commercial Banks

The Bundesbank does not normally deal directly with the general public but only with credit institutions and certain public agencies in Germany as well as various international institutions.

### 5. Power of the Central Bank Over the Instruments of Monetary Policy

The Bundesbank has at its disposal a number of instruments which it can use to control the availability of credit and the liquidity of the banking system.

The Bundesbank has the power to set and to change the discount rate and the rate it charges for advances on eligible paper. Furthermore, the quantity of open-market paper which the Bundesbank stands ready to rediscount is subject to definite limits which, although not published, is believed to be three times the liable capital plus the reserves of any given institutions.

The Bundesbank may establish minimum reserve requirements for credit institutions at any level up to a maximum of 30 percent for sight liabilities, 20 percent for time liabilities, and 10 percent for savings liabilities. Credit institutions which fail to meet reserve requirements are subject to a penalty surcharge which usually stands 3 percent above the rate charged by the Bundesbank on advances.

The Bundesbank may engage in open-market operations and may use for this purpose bills of exchange meeting certain requirements stipulated by law, Treasury bills and bonds, and other bonds admitted to the official stock exchange.

Relatively recently, the Bundesbank developed a new technique which increases its scope for influencing the liquidity of the banking system. By making it more expensive or less expensive for German commercial banks to make covered investments on the foreign exchange markets, the Bundesbank can discourage or encourage the placement of banking funds abroad, thereby increasing or decreasing the supply of funds available to the domestic money market.

### 6. Channels or Sources Supplying Business Capital

The Bundesbank does not and legally cannot finance the capital development of business. Two Government institutions, the Kreditanstalt fuer Wiederaufbau (Reconstruction Finance Corporation) and the Industrie Kreditbank (a semiofficial agency utilizing both public and private funds) engage in this kind of operation. A rough division of the source of funds for the financing of small business would be one-third internally financed, one-third from the big commercial banks or the institutions mentioned, and one-third from the local county or municipal banks.

# CENTRAL BANKING IN ITALY

## 1. Historical Setting

The central bank of Italy, the Banca d'Italia (Bank of Italy), was founded in 1893 as a result of a financial crisis, and was created by the merger of three joint stock banks. Over the next half century it evolved gradually into a true central bank. It initially shared the right of note issue with the Banco di Napoli and the Banco di Sicilia, but was made the sole bank of issue in 1926. As a private stock bank, the Bank of Italy engaged in a substantial private banking business until the reform of 1936. In that year it was made a bank of "public law" and its shares were redistributed among savings banks and other financial institutions. As of that time also the Bank limited its discount operations to rediscounting only for other banks. It financed the Treasury on a heavy scale in World War I and in the years 1936–47, and has administered exchange controls since 1935. By manipulation of its lending rates the Bank very early acted as a regulator of the money market, but its control over credit creation has been greatly increased since World War II.

## 2. Ownership and Control of the Central Banking Institution

Since 1936 the capital of the Bank of Italy has been held by savings banks (which hold most of the shares), the larger commercial banks, insurance companies, and social security institutions. The management of the Bank is conducted by the Superior Council, composed of the Governor and 12 directors who are elected by the shareholders for renewable 3-year terms. The Governor, General Manager, and Vice General Manager are appointed or dismissed by the Superior Council, with the approval of the Government.

Net profits are used for transfer to reserves (20 to 40 percent of profits) and to pay dividends (6 to 10 percent of paid-up capital). Remaining profits go to the Treasury.

## 3. Relation of the Central Bank to the Government

Although its three highest officers must be approved by the Government, the Bank of Italy is not a subservient institution. The Governor of the Bank, by virtue of his membership in the Interministerial Committee for Credit and Savings—the Government body which determines the basic direction of monetary policy—and in part because of the high caliber of the men who have held the governorship, is able to exert great influence on monetary conditions. The Governor has been instrumental in the formulation of policies which halted the postwar inflation and subsequently maintained a high degree of financial stability in most years. These policies have permitted a buildup of gold and foreign exchange reserves and promoted the high level of savings required to finance Italy's rapid postwar economic growth.

From time to time, the Bank has been under legal obligation to make advances to the Treasury, but late in 1947, when the "defense of the lira" policy went into effect, the outstanding amount of advances was frozen; and since that time the Treasury indebtedness to the Bank has been reduced. The Bank of Italy has no legal obligation to purchase Treasury paper, but it is obligated by law to make advances to the Government up to a limit of 15 percent of budget expenditure. This ceiling is high, and it could be abused; but the Treasury has in practice kept its indebtedness to the Bank far below the legal limit.

The central bank finances the Foreign Exchange Office (the Governor of the Bank of Italy is chairman of the Board of Directors of the Foreign Exchange Office) by means of advances, and it in effect administers the foreign exchange market in accordance with market requirements and monetary policy.

### 4. Relation of the Central Bank to Commercial Banks

The Bank of Italy has wide discretionary power to intervene directly and indirectly in the management and administration of banks. The Inspectorate of the Bank carries out detailed audits and investigations of banks. The Bank's consent is required for many individual loans by banks to their customers, and in 1962 the Bank was empowered to determine banks' investment portfolios. The principal transactions of the central bank with commercial banks have been advances against Government securities, rediscounts (mainly of bills to finance the Government-sponsored pooling system for certain crops), and the holding of banks' compulsory reserves of cash and Treasury bills.

The Bank of Italy also extends short-term credit to the medium- and long-term credit institutions. Its advances to private customers have dwindled to almost nothing.

### 5. Power of the Central Bank Over the Instruments of Monetary Policy

The initial establishment of compulsory bank reserves in cash and Treasury bills in 1947 was a cornerstone of the program that halted the postwar inflation, but the level of the requirement remained unchanged until it was lowered in early 1962. While rediscounts of crop pooling bills must be granted automatically, advances and other rediscounts are granted at the discretion of the Bank. Changes in the Bank's rates on advances and rediscounts have been very infrequent. There is as yet no developed money market in Italy, and open-market operations have not been used to govern bank liquidity.

The main continuing instruments of monetary policy in Italy have been moral suasion and the determination every 4 months of the size of banks' lines of credit with the Bank of Italy. Since 1959 the Bank has also influenced internal credit expansion by actions affecting the foreign borrowing and lending of Italian banks (which is centered on the Euro-dollar market). This has been accomplished mainly through

(1) regulations concerning the amount of net foreign borrowing which banks are allowed to engage in, and (2) short-term swaps of lire for dollars between the central bank and the commercial banks.

## 6. Channels or Sources Supplying Business Capital

The Bank of Italy does not directly finance business, but it does extend short-term accommodation to banks and to the many official and semi-official institutions which supply medium- and long-term credit to business. The latter (known as special credit institutes) have resources equaling about one-third of those of the commercial and savings banks. The institutes extending industrial credits are the Istituto Mobiliare Italiano (IMI), Mediobanca, Efibanca, and Mediocredito (which also rediscounts paper for regional medium-term credit institutes). Others of these institutes specialize in real estate credit, agricultural credit, and the financing of electric power plants. About one-half of the resources of the special credit institutes are obtained by bond issues; the other sources include state funds, short-term bank credit, capital stock, and foreign loans to IMI.

# CENTRAL BANKING IN JAPAN

## 1. Historical Setting

The Bank of Japan was established during the era of the Meiji government (1868–1912) when the country was transformed from a feudal to a modern industrial state. Excessive issues of inconvertible bank notes by the Government and later by a system of American-type national banks threatened the nation's monetary stability in the 1870's and 1880's. It was primarily with the aim of retiring these notes and issuing new convertible ones that the Bank of Japan was established in Tokyo on October 10, 1882. Other objectives included nationwide regulation of money and banking, supply of funds to financial institutions to meet temporary shortages, lowering of interest rates, handling of Government funds, and rediscounting of foreign exchange bills. Given the exclusive power of note issue, the Bank of Japan began to issue new convertible bank notes in May of 1885 and by 1899 the task of retiring the earlier inconvertible notes was completed.

The 1882 Bank of Japan Act was patterned after the 1850 law establishing the National Bank of Belgium. This was because the Japanese believed the Belgian system, which was established later than the British and French, benefited from a study of the merits and defects of other earlier central banking systems. Except for a provision allowing the Government to share in the Bank's profits after June 1932, no substantial changes were made in the 1882 law until 1942 when wartime pressures prompted fundamental revisions in the organization and functions of the Bank. The net effect of a new Bank of Japan law enacted in that year, and patterned after Nazi Germany's Reichsbank law, was to make the bank more subservient to the Government and to expand sharply the field of its business activities. A further substantial change occurred in June of 1949 when a new Policy Board was established as the supreme policy-making organ of the Bank.

In addition to the head office in Tokyo, the Bank of Japan has branch offices in 30 major cities in Japan, and 14 minor offices in other cities. The bank also maintains about 1,680 agencies throughout the country for handling Treasury funds or Government bond transactions, and a permanent representative in New York and London.

## 2. Ownership and Control of the Central Banking Institution

The Bank of Japan was established as a quasi-joint stock company with initial capital stock of 10 million yen. Half of this was subscribed by the Government and the other half by the private sector. The Bank's authorized capital was increased subsequently in 1887, 1895, 1910, and 1942. In 1942 the Bank was converted from a joint stock company to a special corporation with a total capitalization of 100 million yen. The Government committed itself to subscribing

55 million yen (which was later paid in on April 24, 1948) and the private shareholders provided 45 million yen, the paid-up capital of the bank at the time. The new Bank of Japan law in 1942 deprived shareholders of their right to vote and they thereby became merely subscribers. Currently there has been no real participation by the private sector in the Bank's activities even though the ownership of the Bank's stock in March of 1962 was divided as follows: Minister of Finance, 55 percent; financial institutions, 3.9 percent; and others, 41.1 percent.

Since 1942, dividends on stock subscriptions have been limited to a maximum of 5 percent per annum. Bank profits after dividends and appropriate allocation to reserve funds are transferred to the Government.

From the beginning of the Bank's establishment the management has been appointed by the Government. In the 1942 reorganization, the Assembly of Officers was deprived of its vote privileges and complete authority was vested in the Governor of the Bank. During the early postwar years, the Bank's management was vested with the Governor, Vice Governor, and the eight members of the Board of Directors. In 1949 the present system involving a seven-man Policy Board was established to decide the operational and monetary policies of the Bank as well as to regulate the nation's money and credit. This Board is composed of the Governor of the Bank of Japan serving ex officio, four members appointed by the Cabinet with the consent of both Houses of the Diet from men experienced in banking, industry, commerce, or agriculture, one nonvoting representative from the Ministry of Finance, and one nonvoting representative from the Economic Planning Agency. Although the law does not require it, the Governor of the Bank of Japan has thus far always been elected Chairman of the Policy Board. Under the new arrangement, the previous management has become an executive board, carrying out the policies determined by the Policy Board.

### 3. Relation of the Central Bank to the Government

Since its establishment the Bank of Japan has always served as fiscal agent for the Government. Besides providing the Government with deposit and lending facilities, it has assumed over the years a wide range of activities including the handling of public receipts and payments, Government debt, Treasury accounts, and the buying and selling of foreign exchange. In order to carry out its extensive operations in this field, the Bank was maintaining at the end of 1961, 531 Treasury agents, 5,113 revenue agents (to receive revenue payments only), 1,412 debt agents and also oversea fiscal agents for the servicing of foreign loans.

Throughout its history the Bank has advanced funds to the Government, particularly in times of emergency such as the great earthquake and fire of 1923 and the financial disturbances in 1927. After the Second World War the Bank of Japan helped finance postwar reconstruction by accepting large amounts of short-term debentures issued by the Reconstruction Finance Bank.

The Bank of Japan law allows the Bank to subscribe to, or take up, Government debt issues. Most short-term Government securities, although issued through public offerings, are held either by the

Bank of Japan or the Government since the private financial community has found the low, Government-established interest rate on these securities unattractive. They consist primarily of short-term bills for financing the Government's foreign exchange fund and foodstuff control account. Various laws, including the Finance Law of 1947, restrict the Government as to the amount and type of long-term borrowing in which it may engage, however, the Bank of Japan does buy and sell long-term Government securities in the market. Since the early postwar years, the Bank has held a substantial volume of both short- and long-term Government securities, although the amount has fluctuated sharply over short periods of a few months.

During most of its life, and particularly since 1942, the Bank of Japan has been subject to the central government's authority as exercised through the Ministry of Finance. Present statutes permit the Minister of Finance to issue orders to the Bank, although this power has not been exercised, and many matters, such as a change in commercial bank reserve requirements, require his approval.

The Ministry of Finance, in conjunction with the Bank of Japan, also plays an important role in determining the level and structure of interest rates in Japan. The Ministry's authority for this role stems in part from the Temporary Money Rates Adjustment Law of 1947. Although the situation has changed somewhat since then in the direction of more voluntary regulation by the financial community, the Ministry continues to exercise close control over interest rates through powers of moral suasion. Official control is further enhanced by the policy of the Japanese Bankers' Association of automatically raising or lowering the structure of commercial bank lending rates in consonance with changes in the Bank of Japan's basic discount rate.

A difference of opinion regarding the degree of independence that the Bank of Japan should have from the Government was underlined as a result of a study conducted between 1957 and 1960 by a Government research committee on Japan's financial system. One view held that the Government must have the right to give direction to the bank and the other argued for bank independence from the Government. Because the committee's opinion was split on this point, no action has been taken by the Ministry of Finance on a proposed revision of the Bank of Japan law.

### 4. Relation of the Central Bank to the Commercial Banks

The Bank of Japan is empowered to carry out a wide variety of activities with commercial banks and other financial institutions. These include receiving deposits, making loans, discounting bills and notes, and buying and selling bills and securities. Because of the relative scarcity of financial capital in Japan, commercial banks have turned to the central bank, not only for temporary or seasonal needs, but also as a ready source for current funds. Since the passage of a new Bank of Japan law in 1942, the Bank has explicitly been allowed to make loans secured by stocks, shares, and corporation bonds, as well as merchandise. As a result of these conditions, Japanese commercial banks are heavy borrowers from the Bank of Japan, and at the end of 1962, 6.4 percent of their total liabilities consisted of debt to the Bank. Most of this reflected Bank of Japan loans rather than discounts.

Although the amount of commercial bank borrowing from the Bank of Japan is substantial, the Bank has attempted during the past decade to restrain such borrowing in order to foster general monetary stability. A form of moral suasion, usually termed "discount window guidance" by the Bank, has been practiced. This has consisted of monthly meetings with the city bank managers, at which time the banks are given advice and recommendations by the Bank of Japan on their borrowing plans. Since November of 1962 the Bank has increased its reliance on the use of open-market operations and in May of 1963 the Bank announced that it was discontinuing the "window guidance" program.

Supervision and examination of commercial banks in Japan is carried out both by the Ministry of Finance and the Bank of Japan. The Ministry is empowered to require any bank to furnished whatever financial information is necessary in order to provide the Ministry with complete knowledge of the financial condition of the bank. Japanese law requires that banks be examined at least twice in every 2-year period.

## 5. Power of the Central Bank over the Instruments of Monetary Policy

Largely because of the financial structure of the Japanese commercial banks, central bank discount policy has played an important and effective role in maintaining general economic stability. Open-market operations and reserve requirements have been of only minor importance in the past, though recently their importance has been increasing.

Central bank effectiveness in using discount policy can be related to three factors. First, the commercial banks are heavily dependent on credit from the Bank of Japan and the money market to meet their financial needs. A restriction of central bank credit has an immediate and significant impact on commercial bank lending and investing activities. Second, the policy of "window guidance" mentioned earlier has in effect constituted a form of rationing of central bank credit. Although this technique has been used extensively in the postwar period, there has been some debate regarding its effectiveness. While some believe that it has been a key factor in the restoration of economic equilibrium, others, including some officials of the Bank of Japan, have disagreed with this assessment. As noted earlier, the program was discontinued in May of 1963. Third, a system of penalty discount rates for banks borrowing large amounts from the central bank in relation to the quotas established for each bank has also been effective in restraining excessive commercial bank credit expansion. During the three business cycles of the past decade, monetary policy has been used successively in restraining excessive expansion and restoring both domestic and international economic equilibrium.

Until recently, open-market operations have been confined largely to absorbing the excessive seasonal liquidity of local banks and the Central Cooperative Bank of Agriculture and Forestry. In periods of seasonally tight credit, the Bank has also bought from commercial banks moderate amounts of Government-guaranteed debentures. Since November of 1962 the Bank has expanded its buying operations, both in terms of volume and the variety of securities, and at the same time has been reducing its discount operations.

Although Japan had been anxious for many years to establish reserve requirements for commercial banks, the extremely low liquidity of the banks seemed to preclude such a step. These reservations were finally overcome in September of 1959 when relatively low reserve requirements, ranging from 0.25 to 1.5 percent, were established. Since reserve deposits account for only a very small part of total bank deposits and the banks at the same time are heavily in debt to the central bank, the reserve requirements are not yet very effective as an instrument of bank credit regulation. In March of 1963 the reserve requirement system was extended to apply to mutual loan and savings banks, and credit associations.

## 6. Channels or Sources Supplying Business Capital

In recent years in Japan about one-third of new industrial funds have been derived from internal sources (retained earnings) and the other two-thirds from external resources. Both operating and equipment funds have been provided by four types of banks, viz, city, local, trust, and long-term credit banks. The main sources of industrial funds include bank loans and funds from other financial institutions. Of lesser importance are new issues of stocks and debentures. A substantial part of city and local bank credits consist of medium- and long-term business loans. These banks are also an important source of small business financing.

Because of the strong business demands for financial capital from the banking system and the relatively low capitalization of most banks, Japanese banks, particularly the large city banks, at times find themselves in an "overloan position." Although this term has various meanings, it generally refers to a condition where a bank's loans are in excess of its deposits, debenture issues, and capital. The banking system as a whole has not been in an overloan position in the above sense since the early 1950's, but during the 1950–62 period, the large city banks were "overloaned" except in 1955, 1956, 1959, and 1960.

Japan also has a wide variety of other financial institutions for financing a broad range of economic activities. These include six types of financial institutions for financing small business, agriculture, and forestry; insurance companies; call loan and foreign exchange brokers; investment trusts; corporations for financing securities; and some 13-odd Government financial institutions.

# CENTRAL BANKING IN THE NETHERLANDS

## 1. Historical Setting

The Netherlands Bank (De Nederlandsche Bank), was chartered as a joint-stock company in 1814, and retained this form under successive renewals of its charter until the Bank was nationalized in 1948. The Bank's original charter gave it the note issue monopoly for 25 years; and the Government subscribed to part of the Bank's capital stock. The Government disposed of its stock in 1847, while the Bank's note issue monopoly was formally withdrawn in 1863. With successive renewals of its charter, however, the Bank took on added responsibilities as agent for the Government; and as the note issue out privilege was not given to any other institution after 1847, the Netherlands Bank retained a de facto monopoly.

## 2. Ownership and Control of the Central Banking Institution

The capital stock of the Netherlands Bank has been entirely owned by the state since nationalization of the Bank by the act of April 23, 1948. The shareholders received Government securities in exchange for their shares. All of the profits of the Bank are transferred to the Government.

The Governing Board of the Netherlands Bank, which consists of the President, the Secretary, and from three to five Executive Directors, is appointed by the crown for a term of 7 years on the basis of nominations by a joint meeting of the Governing Board and the Board of Commissaries. The Board of Commissaries "supervises the administration of the Bank and approves and adopts the yearly profit and loss account."

## 3. Relation of the Central Bank to the Government

Although the Finance Minister is empowered to issue directives to the Netherlands Bank, the latter has the right to appeal to the Crown in case of disagreement, which would lead to a further careful consideration of the issue by the Government as a whole. Traditionally, the Netherlands Bank does not support the Government long-term bond market, although it is legally empowered to do so.

## 4. Relation of the Central Bank to the Commercial Banks

The act on the supervision of the credit system, passed in January 1952, empowered the Netherlands Bank to issue "general instructions" to credit institutions concerning the maintenance of minimum reserves, maximum extension of credits, maximum size of individual credits, and prohibition of limitation of specific kinds of credits and investment, with the general exception that under no circumstances could a credit institution be compelled to hold Treasury paper. The act also empowered the Bank to require credit institutions to submit periodic statements and such other information as the Bank should deem necessary. Before issuing an instruction the Bank must consult with the representative organizations of the credit institutions, and if their agreement is not obtained, the instruction in question becomes void unless it is approved by the legislature within 3 months of promulgation.

Since 1951, the discount rates of the Netherlands Bank have been higher for private customers than for banks, and this differentiation has tended to reduce the importance of the Bank's private business.

## 5. Power of the Central Bank Over the Instruments of Monetary Policy

Subject to the veto power of the Finance Minister and the machinery for appeal mentioned above, the Governing Board of the Bank has full power to set its discount rates and conduct open-market operations. The Bank is empowered to buy and sell bills of exchange, and debenture bonds of the Netherlands Government, or bonds guaranteed by it, provided such bonds are quoted on the Amsterdam Stock Exchange. In practice the maturities of securities traded in open-market operations have been from 1 to 5 years. Since open-market operations were begun in 1952, they have played a significant role in the monetary policy of the Netherlands Bank. For the most part they have been used to offset changes in commercial bank liquidity arising from seasonal fluctuations and changes in the foreign balances, but open-market sales have at times been undertaken with the object of exerting pressure on the money market.

The Netherlands Bank is empowered under the terms of the "gentlemen's agreement" of March 1954 to raise the cash reserve requirements of the commercial banks to 15 percent of total deposits; the ratio has been as low as 4 percent and as high as 10 percent. The Bank has the power, on a "standby" basis, to require minimum liquidity ratios of cash, call loans, and short-term securities to total deposits.

## 6. Channels or Sources Supplying Business Capital

One semipublic institution established in the Netherlands in the postwar period provides long-term financing to business. The Reconstruction Bank (Maatschappij tot Financiering van het Herstel)—commonly referred to as the Herstelbank—was established in 1945 in order to finance reconstruction. The Herstelbank may not supply risk capital but may make loans involving more than normal risk if the loan carries a Government guarantee. The Government holds more than one-half the capital stock of the Herstelbank. The Netherlands Participation Company (Nederlands Participatie Maatschappij) is a subsidiary of the Herstelbank (which holds over 30 percent of its stock) established in 1948 to provide risk capital to small- and medium-sized firms, which it does by investing in shares listed on the stock exchange or by direct participations.

The Nederlandsche Middenstandsbank, an institution originally formed to grant commercial credit to shopkeepers, small craftsmen, and members of the professions—the so-called middle classes, as is implied by the name of the bank—also makes loans for periods up to 10 years when these loans are guaranteed by the Government.

# CENTRAL BANKING IN SWEDEN

## 1. Historical Setting

The Bank of Sweden (Sveriges Riksbank) is the oldest central bank in the world. It was organized in 1668 as a state-owned bank responsible to the Swedish Parliament (Riksdag), after the failure in that year of a predecessor institution, the Bank of Stockholm (Stockholm Banco), chartered as early as 1656 and considered to be the first bank to issue ordinary bank notes. It is noteworthy that the Bank of Stockholm, although a private enterprise, was for many practical purposes regarded as a state institution; and, from its beginnings, important questions pertaining to the Bank were referred to the Swedish Parliament. The tradition that the central banking institution is responsible to the national legislature—a tradition which has been embodied in a formal provision of the Swedish Constitution—is thus of very long standing.

The Bank of Sweden acquired the attributes of a modern central bank only very gradually in the 19th century. It was for a long period a state commercial bank and the leading credit institution in the country. In 1897 the Bank of Sweden was given the note issue monopoly, and the private banks' right to issue notes expired at the end of 1903. Operations of the Bank of Sweden were restricted almost entirely to those of a central banking character by the 1897 legislation, so that the transformation of the Bank of Sweden into a central bank in the modern sense was completed at the turn of the century.

## 2. Ownership, Control, and Relation to the Treasury

The Bank of Sweden is state owned. Legally responsible to the Swedish Parliament, it operates under legislation which expressly prohibits Directors of the Bank from receiving instructions from anyone except the Parliament and its Banking Committee. For example, the Minister of Finance may meet with the Directors of the Bank, but no decisions may be taken in his presence.

The Bank of Sweden is administered by a Board of Directors consisting of seven members, of whom the Chairman is a Government appointee named by the King-in-Council; the other six Directors are chosen by a joint group of electors from both Houses of the Swedish Parliament. Current administration of the Bank of Sweden is handled by a Board of Management consisting of the Governor of the Bank, a Deputy Governor, two Directors, and several Managers. The chief executive officers of the Bank—the Governor and Deputy Governor—are elected by the Board of Directors from among its members.

The operational independence of the Bank of Sweden was seriously impaired during the 1930's, when the ruling Social Democrats subordinated monetary policy, then in disrepute, to the general economic policy of the Government. The subordination of monetary policy continued into much of the postwar period—as it did in many European countries, although this phase was perhaps somewhat more prolonged in Sweden than elsewhere—and the Government continued to pursue cheap money conditions as an integral part of its full employment and social welfare policies. Starting with the resignation of Gov. Ivar Rooth in 1948, three successive Governors of the Bank of Sweden reportedly resigned in part in protest against the monetary policy which the Government continued to enforce into the mid-1950's. Serious conflict between the central bank and the Government last occurred in July 1957, after the Bank of Sweden raised the discount rate without informing the Government in advance. Although the Government forced the resignation of its appointee, the Chairman of the Board of Directors, the higher discount rate was not subsequently altered by Parliament.

### 3. Instruments of Monetary Policy

Throughout most of the postwar period the Swedish economy labored under persistent inflationary pressures, to which successive budget deficits and a large Government-sponsored housing program contributed significantly. For a fairly extended period after the war the Bank of Sweden played an essentially passive role. Until 1955 the Bank pegged the Government bond market—although it did so at progressively higher interest rates toward the end of the period—in order to permit flotation of the large volume of bond issues necessary to finance the budget deficits and the housing program. Because of the consequent impossibility of satisfying the high level of demand for long-term funds, the Bank of Sweden also exercised capital issues control, under which applications to float long-term securities were screened to assure that loans for priority sectors, i.e., the central government and the housing market, received preferential treatment.

Monetary policy began to play a more active role in 1952, when the Bank of Sweden obtained authority to impose effective minimum liquidity ratios on the commercial banks. The liquidity requirements, which are differentiated by size of bank and which have been changed from time to time, have been embodied in voluntary agreements, usually negotiated each year, between the central bank and the commercial lending institutions. At times, the agreements have contained elements of selective credit policy, such as guiding lines for the allocation of credit to designated sectors or recommendations for the restriction of credit for speculative or otherwise undesirable purposes. During one brief period (1955–57), the agreements also included an absolute ceiling on bank advances imposed by the Bank of Sweden. Along with the agreements concluded with the commercial banks, the Bank of Sweden's controls have also extended to the savings banks and insurance companies, in the form of requirements that these institutions reserve specified portions of new money for priority borrowers.

While capital issues control remains in effect, a condition of relative balance has emerged on the Swedish capital market since about 1960. Two factors are responsible for this rather dramatic transformation. The emergence of budget surpluses after a decade of chronic deficits—resulting from the introduction of a national sales tax—has substantially reduced the Government's borrowing needs. The operation since 1960 of the compulsory national pensions scheme has also produced a large increase in savings in the public sector, and a sizable portion of the resources of the new general pension fund has been invested in long-term loans to the business sector. As a result, the traditional queue of long-term borrowing applicants to the Bank of Sweden has been virtually eliminated.

The renaissance of Swedish monetary policy has been accompanied by the evolution of an interesting combination of tax measures, fiscal policy devices, and labor market practices designed to meet the needs for policy instruments which can be fairly quickly adapted to changing economic conditions. This is especially true of the much-publicized system of investment reserves, which is designed to spread private investment activity more evenly over the business cycle. In an expansionary period, business enterprises are encouraged, by tax incentives, to set aside specified portions of gross profits, which are deposited in the central bank; when the authorities later consider that the economic situation requires some stimulus, these reserves may be released at the discretion of the Labor Market Board to finance certain types of business investment.

## 4. Channels or Sources Supplying Business Capital

Traditionally the Swedish commercial banks have engaged in long-term financing of industry; in addition, they act as underwriters for bond issues and hold large portfolios of bonds and housing mortgages. In part this investment behavior reflects the stability of bank deposits and the tendency for a large share of savings to be kept in the form of bank deposits.

The Ship Mortgage Bank is a semiofficial institution which grants long-term loans on the security of ship mortgages. In 1953 the commercial banks founded Svensk Fartygskredit AB for the purpose of financing loans to shipowners. The Industrial Credit Bank was organized in 1934 jointly by the Government and a few leading commercial banks for the purpose of giving medium- and long-term loans to industrial firms which were too small to have ready access to the bond market. The loans of this institution have never reached large proportions.

# CENTRAL BANKING IN SWITZERLAND

## 1. Historical Setting

The Banque Nationale Suisse (Swiss National Bank) was established in 1907 after nearly 20 years of political dispute as to the legal form of the Bank and its location. The Bank was set up as a joint stock company with an authorized capital of 50 million Swiss francs, only half of which has been paid in. As of a recent date, 55 percent of the capital was held by the cantons and the cantonal banks and the remainder was widely distributed among private holders.

The Swiss National Bank has two main offices. The securities and the foreign exchange departments and the office of the Bank's Board of Directors are located in Zurich, the capital market and foreign exchange trading center of Switzerland. However, the departments concerned with note issue, the Government account, the management of the central bank's gold supply, and the central bookkeeping are located in Berne, the seat of the Federal Government. The Bank has 8 branches and 15 agencies in the major cities and towns of Switzerland.

The Swiss National Bank has the sole right of note issue. Furthermore, according to the revised national bank law of 1953, the central bank is responsible for the supervision of the money circulation, the regulation of currency and credit policies, facilitating domestic payments, and advising the Federal Government on currency matters.

## 2. Control of the Swiss National Bank

A Bank Council of 40 members, 15 elected by the stockholders and 25 by the Federal Council (the Swiss Cabinet), is the organization with general supervisory control of the Bank. The Bank Council is required to have adequate representation of commerce, industry, and agriculture. An Executive Committee of 10 members, elected by the Bank Council, is responsible for the close supervision of the management, and it must meet with the latter group at least once a month. A Board of Directors consisting of three members appointed by the Federal Council, after recommendation by the Bank Council, is the responsible authority for the day-to-day running of the central bank.

## 3. Relation of the Central Bank to the Government

Through its powers of appointment and otherwise, the influence of the Government with the central bank is considerable, and from time to time the Federal Council has prescribed monetary policies for the Bank to follow. The Bank has permissive power to purchase both Federal and cantonal government securities for the temporary investment of funds, and it "cooperates" in the placing of new Federal and cantonal funds. The Bank is required to rediscount acceptances for financing strategic stocks at the minimum applicable rate.

## 4. Relation of the Central Bank to the Commercial Banks

The Swiss National Bank is not prohibited from dealing with financial institutions other than banks of deposit, but virtually all of its business, other than that with the Federal and cantonal governments, is with banks of deposit.

## 5. Power of the Central Bank Over the Instruments of Monetary Policy

Although the central bank has the power to change the rates on rediscounts and advances, the bank has made little use of this power because rediscounting and resort to advances figure little in operations of Swiss commercial banks. Banks rarely go to the Swiss National Bank in order to improve their liquidity positions primarily because of the large sums flowing to them from foreign depositors and speculators. Furthermore, the Swiss National Bank does not have the power to adjust reserve ratios, for such control is held to be unconstitutional. Open-market operations cannot be carried on because the central bank has no portfolio of appropriate securities.

Left without any of the traditional powers of monetary and credit control, the Swiss National Bank has developed two other methods of regulating the degree of liquidity in the Swiss economy that have proven eminently successful. The basis of Swiss monetary control is the traditional willingness of its commercial banks to listen to the urgings of the central bank and to enter into ad hoc arrangements—"gentleman's agreements"—designed to maintain continued sound economic conditions.

Second, the currency swap technique, a relatively new development in the area of Swiss monetary control, is simply a Swiss adaptation of the corresponding practice introduced in the past several years in the area of international payments. On a number of occasions since 1961, the Swiss National Bank has entered into short-term swaps with Swiss commercial banks. By swapping U.S. dollars (or other currencies) with the commercial banks for Swiss francs, the central bank has been able to reduce the liquidity of the banking system by removing francs from circulation. When the central bank has wished to increase liquidity, the process has merely been reversed. In the final analysis, however, the Swiss National Bank could not make use of this method of credit control if the commercial banks were not as cooperative and as open to moral suasion as they have traditionally proven to be.

The Federal banking law does prescribe liquidity requirements for all banks, but the banks are under no penalty if they are temporarily deficient. These requirements are based upon a rather complicated formula involving various ratios of liquid assets to liabilities. The liquidity requirements are supervised by the Banking Commission, a group appointed by the Federal Council, and independent of both the Swiss National Bank and the Treasury.

## 6. Channels or Sources Supplying Business Capital

The Swiss National Bank cannot finance capital development. The commercial banks of Switzerland are "department store" banks, meaning that they engage in all types of banking business. Small businesses which are members of the credit unions (Raiffeisen Banks), a well-developed and wide spread movement in Switzerland, are able to obtain development financing through their local organizations.

# CENTRAL BANKING IN THE UNITED KINGDOM

## 1. Historical Setting

The Bank of England was chartered by act of Parliament in 1694. In 1844 it was given sole right of note issue. By the second half of the 19th century, the public service aspects of the Bank's activities began to eclipse its private banking business. It became the lender of last resort to the money market and the regulator of the great international gold and capital market in London.

## 2. Ownership, Control, and Relation to the Treasury

By 1926, relations between the privately owned Bank of England and the Government were so close that the then Governor, Montagu Norman, noted that the Bank had the right to offer advice but was always subject to the "supreme authority of the Government."

In 1946, the Bank was nationalized by act of Parliament. The Government acquired the entire capital stock of the Bank, and was emplowered to appoint the Governor, Deputy Governor, and Directors of the Bank for fixed terms. The Treasury was empowered to give directions to the Bank, after consultation with the Governor. The Bank in turn was empowered, upon authorization from the Treasury to request information from and give directions to the commercial banks when it thought this necessary in the public interest.

Nationalization of the Bank was generally regarded as primarily codifying by statute an existing relationship between the Bank and the Treasury. Since nationalization, the Bank has continued to operate and to advise the Government in much the same way as before.

## 3. Instruments of Monetary Policy

Monetary control is exercised mainly by a combination of open market operations and discount policy. This is done on the basis of certain institutional arrangements peculiar to the British monetary system. Unlike the Federal Reserve System, the Bank of England does not lend to commercial banks but only to discount houses, whose main business is to underwrite the weekly Treasury bill issue with call loans secured mostly from the London clearing banks. These banks account for 70 percent of the total deposits of the United Kingdom's commercial banks. As a matter of traditional practice, the clearing banks maintain cash reserves (vault cash plus deposits at the Bank of England) equal to 8 percent of gross deposits and, at the same time, liquid assets (cash reserves, call loans, Treasury bills, and commercial bills) equal to 30 percent of gross deposits. In addition to these two reserve requirements, a "special deposit" scheme was announced in July 1958 and was in effect from mid-1961 to mid-1962. Under that scheme, the clearing and Scottish banks could be asked to maintain interest-bearing deposits with the Bank of England up to as much as 3 percent of gross deposits.

The Bank of England restricts credit by selling Treasury bills or Government bonds through its "special buyer" (a discount house) or the "Government broker" (a securities dealer), thus absorbing cash from the banking system. To restore their cash and liquidity positions, the banks can withdraw their call loans from the discount houses; the discount houses in turn may be forced to borrow from the Bank of England at bank rate. In contrast with the Federal Reserve discount rate, bank rate is a penalty rate, being higher than the average yield from the discount houses' earning assets. If the discount houses are forced to borrow heavily from the Bank of England, they tend to lower their bid at the following week's Treasury bill auction. The higher rate of interest on Treasury bills, along with selling pressures generated by the Bank of England itself, tends to force up money-market interest rates generally. A rise in bank rate may then follow.

By longstanding practice, a change in bank rate is followed immediately by corresponding adjustments in commercial bank deposit and lending rates. Recently the Bank of England took a step to obtain more scope to raise London money-market rate (to attract or retain funds of nonresidents) without forcing up domestic banking charges. Reverting to a technique formerly in effect in the 1920's, the Bank on March 19, 1963, made loans to the discount houses at a rate *higher than* bank rate. On that occasion, the Treasury bill rate moved closer toward bank rate, but since bank rate was unchanged, commercial bank loans and deposit rates were not affected.

In contrast to the U.S. banking system, "moral suasion" is a significant instrument of control, as the Governor of the Bank of England meets frequently with the chairmen of the London Clearing Bankers Association and of the London Discount Market Association. Gentlemen's agreements for qualitative controls are relatively easy to establish. For example, from mid-1961 to mid-1962, the banks agreed to give priority to loan requests from export industries and not to make loans for financing personal consumption and real estate developments.

### 4. Channels or Sources Supplying Business Capital

The Bank of England owns 30 percent of the share capital of the Finance Corporation for Industry, Ltd., which was formed in 1946 "for the reequipment and development of major industries with a view to promoting efficiency." The Bank also has a token participation in the Industrial and Commercial Finance Corp., Ltd., also set up in 1945, which has as its main object "the provision of credit and finance by means of loan capital and share capital for industrial and commercial concerns in Great Britain, particularly in cases where the existing facilities provided by banking institutions and the stock exchange are not readily or easily available."

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