New Central Bank Mandate in Argentina: A Bold Initiative to Restore Central Banks as Agents of Economic Development

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Prevailing ideology has held that the only legitimate task for central banks is to control inflation, which often comes at the expense of broader goals such as employment creation, financial stability or economic growth. Now, in a bold and important move, the government of Argentina has fought against this neo-liberal "conventional wisdom" and broadened the mandate of the Argentine Central Bank to include economic growth and financial stability, and empowered it to use more tools to support credit allocation to promote productive investment and job creation (see Weeks, www.social-europe.eu/2012/04/getting-priorities-right-the-new-central-bank-law-in-argentina/).

In March, 2012, the Argentinean Congress approved new legislation that regulates the functioning of its central bank, and the financial system. This new legislation marked the final formal step in the reorganization of the rules governing Central Bank monetary and credit policy following the disastrous Convertibility Plan that tied the Argentine currency to the U.S. dollar in 1991. This led to economic collapse in 2002 with a debt default and severe economic crisis. The Convertibility Law required that the Central Bank maintain the fixed value of the peso relative to the dollar, and as such, was an extreme version of the neo-liberal monetary policy focused on fighting inflation to the exclusion, and therefore at the expense of, economic growth, job creation and economic development.

The Central Bank reform has instituted a triple mandate, which includes monetary stability, financial stability and economic development with employment creation and income equality. The reform also creates new instruments of monetary and credit policy: it allows the Central Bank to lend directly to the government up to 12% of the monetary base and advance funds that correspond to no more than 10% of the government revenue in the previous 12 months. It also allows for the use of international reserves for the payment of the foreign debt obligations of the national government, eliminating some restrictions that were in place over the use of international reserves. Perhaps most importantly, the reform allows the bank to provide funds for domestic banks and other financial institutions involved in the financing of long-term productive investment.[a]

The new law is already attracting criticism from orthodox critics. *The Economist*, for example, proclaimed that the Argentine Central Bank had become the "piggy bank" of the Argentine government, "losing the last shred of its legal independence" (March 3, 2012, www.economist.com/node/21551507). This, they claimed, would lead to massive inflation and runaway budget deficits.

[a] This description is based on communication from Matias Vernengo, Senior Research Manager at The Central Bank of Argentina.

But as I have argued elsewhere, the new Argentine mandate is quite in line with historical practices of central banks. The historical norm has been for central banks to be integrated into the overall government framework of macroeconomic policy making. This has been true not only in developing countries, but also in many of the currently "developed" countries of Europe and Japan, and also even in the U.S. and the U.K.[b] Central bank coordination with the fiscal authorities and support of credit allocation policies was crucial in the recovery of the Europe and Japan after the Second World War, in the growth and development of major Asian success stories such as South Korea, Taiwan, China and India, and in the United States and the U.K. with respect to specific sectors, including the housing sector following the Great Depression and the Second World War.

Recently, similar policies have been proposed to help generate employment and make the transition to a green economy.[c] To be sure, such policies can be and have been abused. As Alice Amsden pointed out in her seminal book *The Rise of the Rest,* performance requirements for subsidized credit, and close monitoring of credit allocation policies are necessary for success. The same holds true for the relations between central banks and governments. But these tasks are no more complex or fraught than ensuring that so-called independent central banks act in the interests of society as a whole, rather than promoting the interests of a narrow sector of society, usually the financial sector. We have seen the high costs of central banks' coziness with finance in the great economic crisis we are currently experiencing, and in the collapse of the Argentine economy in 2002.

External support for the Argentine Central Bank law is building. Letters of support for the law are coming in from economists in various parts of the world (see **the letter from the U.K.**, [d] **from the U.S. organized by SAFER**,[e] and a letter from Turkish economists, in process). I hope this support builds quickly, as the pressure on the other side is sure to mount. Equally importantly, I hope other countries will look closely at the Argentine experience and be inspired to go down a similar path: to transform their central banks to act less as agents of finance and instability and more as agents of equity promoting economic development.

[b] "Central Banks as Agents of Economic Development," in Ha-Joon Chang, ed. *Institutional Change and Economic Development,* 2007, United Nations University and Anthem Press. www.wider.unu.edu/stc/repec/pdfs/rp2006/rp2006-54.pdf

[c] See, Robert Pollin,*Back to Full Employment* MIT Press, 2012. mitpress.mit.edu/catalog/item/default.asp?ttype=2&tid=12891

[d] http://www.primeeconomics.org/%20?p=1014

[e] http://www.peri.umass.edu/fileadmin/pdf/other_publication_types/SAFERbriefs/Argentina_letter_May22.pdf