
Alexandre Lamfalussy and the monetary policy debates among central bankers at the end of the 1970s

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Résumé

The 1970s, with the end of the Bretton Woods monetary system, the two oil shocks and accelerating inflation were a turbulent period in postwar economic history. The breakdown of Bretton Woods implied that central bankers had to look for new monetary policy strategies, as the exchange rate lost its central role. Moreover, financial stability became a major preoccupation, certainly at the BIS. In this sense, and contrary to the Bundesbank and the Federal Reserve, Alexandre Lamfalussy, the BIS's Economic Adviser at the time, was less concerned about the growth of the money supply and its inherent inflationary risks, than with the expansion of credit and the threat of a debt crisis. The Latin American debt crisis of the early 1980s would confirm his fear.

This paper focused on how central bankers at the BIS responded to the Great Inflation in the developed countries. Monetarist ideas, focused on flexible exchange rates and monetary targeting were already in the ascendancy in the academic world in the 1960s. In the 1970s, with the Great Inflation, monetarism also gained ground in the central banking community, especially in the Bundesbank and in the Federal Reserve System.

The BIS Annual Reports, even before the 1973 oil shock, identified inflation as a major policy problem. However, the analysis, strongly under the influence Milton Gilbert, the BIS Economic Adviser in the early 1970s, focused very much on cost push factors as causes of inflation. From 1976, with Alexandre Lamfalussy as Economic Adviser, the BIS gave much more attention to monetary and financial developments. The high-level BIS Working Party on Domestic Monetary Policy, which was created in early 1978, focused specifically on problems and techniques of monetary management.

During the debates at the end of the 1970s, Lamfalussy, in his early years a Keynesian in favour of discretionary policies, moved to a "conservative Keynesian" position, acknowledging that a medium term orientation and the credibility of monetary policy were important to break inflationary expectations. However, Lamfalussy and the BIS never moved to 'monetarist' positions. Lamfalussy certainly acknowledged that under the right conditions, monetary targets could reinforce the credibility and independence of monetary policy. However, he stressed that also other rules, like an exchange rate target, could play this role. Moreover, he rejected mechanical rules. In the early 1980's, with the rise of financial innovations, Lamfalussy would stress even more the limitations of monetary targeting. In essence he aimed for a middle position: rules applied with a pragmatic sense of discretion. In his

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view, central banking remained an art, not a science.