An Historical Perspective on the Quest for Financial Stability and the Monetary Policy Regime

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Introduction

- I focus on the historical evolution in the past two centuries on the connection between the monetary regime (exchange rate regime, monetary policy regime) and financial stability.

- Macroeconomic and financial stability are important for economic growth and development
- These public goods are provided by the macroeconomic policy regime
- Macroeconomic stability encompasses – price stability and stability of the real economy
- Financial Stability traditionally meant preventing and managing financial (banking) crises
- Recently viewed as heading off systemic risk – especially credit driven asset price booms

Introduction

- Exchange Rate Regimes set the basic framework
  1. Specie Standard (bimetallism and gold)
  2. Gold Exchange Standard
  3. Bretton Woods adjustable peg
  4. Managed Float (fiat)

Introduction

- Within the E Regime monetary authorities (central banks) followed a monetary policy regime
- The relationship between monetary policy tools and goals
- Tools: policy interest rate, M aggregates, qualitative and quantitative controls
- Objectives : Pre WWI E convertibility; Post WWI : P stability, y stability, low unemployment , financial stability

Introduction

- Central Banks (CBs) evolved from 1667 (Riksbank) and 1694 (Bank of England)
- From government finance to a bankers bank to LLR, to managing the gold standard (convertibility) to providing macro stability
- The learning process to establishing macro stability was long and painful and non linear
- It followed a pendulum process-- success to failure to success (Bordo and Siklos 2014)
- The Great Moderation (1985 to 2005) viewed as the pinnacle of success

Introduction

- The learning process to provide financial stability was also long and painful
- The pace of learning to be a LLR differed across countries
- After the adoption of the financial safety net in the 1930s banking panics resolved by LLR evolved into expensive fiscally resolved banking crises
- Supervision and Regulation policy also went through a lengthy learning process (Toniolo and White 2016)

Introduction

- Four key principles emerged from the historical evolution of CBs before the Global Financial Crisis of 2007-2008
  1. The importance of maintaining credibility for price stability (low inflation)
  2. Maintaining real macro stability
  3. Providing a credible rules based LLR
  4. Having a sound banking structure and effective supervision and regulation of the banking system

Introduction

- The GFC 2007-2008 changed perceptions considerably on the connection between the monetary policy regime and financial stability.
- Before the GFC CBs were advised not to prevent AP booms and busts but to clean up later (cleaning)
- Since GFC many argue that credit driven AP booms were the key cause of the crisis
- Hence CBs should use monetary policy to head off imbalances in advance (leaning against the wind (LAW))
- Also CBs should use tools of macro prudential policy (eg loan to value ratios and capital requirements) to prevent imbalances from becoming serious
- But others say following such a strategy would conflict with main goals of macro stability
- And encroach on CB credibility and independence

Introduction

- The relationship between monetary policy and financial stability is at the forefront of policy debate
- The lessons from economic history are important to resolve this debate

Introduction: Roadmap

1. I survey the historical evolution of monetary policy and financial stability
2. I survey the empirical evidence on the incidence, costs and determinants of financial crises
3. I provide a narrative on some famous financial crises from history
4. I explore the relationship between credit booms, asset price booms and serious financial (banking) crises

Introduction: Main Takeaways

- Our exploration suggests that financial crises have many causes including credit driven asset price booms
- Which have become more prevalent in recent decades
- In general FCs are very heterogeneous and hard to classify
- Two key historical episodes stand out in the record of serious FCs which were linked to credit driven AP booms/busts
- The 1920s and 1930s and the GFC 2007-2008
- The question arises whether these two perfect storms should be grounds for permanent changes in the monetary and financial environment
- I raise some doubts
- There are important lessons from history for policy makers and historians on the crucial subject of financial crises

Historical Evolution of Monetary and Financial Stability

- CB evolution over 4 Exchange Rate Regimes involved learning
- Both with respect to macroeconomic policy and financial stability policy

A. The Classical Gold Standard 1880-1914

- Credible gold convertibility rule (Bordo and Kydland 1995)
- Bagehots's Rule for LLR
- It was a relatively successful experience with great differences across countries

Historical Evolution of Policy

B. Interwar Gold Exchange Standard

WWI disrupted the domestic and international monetary order –high inflation

- Less credible standard reflecting changed political economy (Eichengreen 1992)
- Fatal flaws : adjustment, liquidity, confidence– propped up by CB cooperation
- Beginning of dual mandate
- Wall Street boom
- Policy mistake by the Fed based on real bills doctrine
- The Great Contraction 1929-33
- Fed failed to act as LLR to prevent 4 banking panics
- GE standard spread contraction abroad via fixed e and golden fetters

Historical Evolution of Policy

C. Bretton Woods 1945 to 1973

- BWS compromise between fixed E of gold standard and domestic macro control of floating E
- Good macroeconomic Performance
- Dejà-vu to the problems of the IW with the gold dollar standard
- Eventual collapse after 1965 because of US inflation policies
- Great Depression blamed on banks and CBs -- led to extensive external and domestic controls and subservience of the CB to the Treasury
- Got Financial Stability but also Financial Repression

Historical Evolution of Policy

D. Managed Float 1973 to 2006

- Great Inflation: causes
  - Release from gold constraint
  - Flawed doctrine : Phillips curve and fiscal dominance
  - Loss of CB credibility
- Volcker shock 1979 led to return to rule like policies and credibility for low inflation
- Great Moderation—good macro performance
- Return of financial instability and banking crises
- Interaction between inflation and controls (reg Q); liberalization driven by financial innovation ; end of capital controls
- With financial safety net banking panics morphed into banking crises with fiscal resolution
- TBTF and moral hazard

Historical Evolution of Policy

E. Global Financial Crisis 2007-2008

- Key causes:
  - US housing policy—begins in 1930s (Rajan 2010)
  - Loose Fed policy 2002-2005 (Taylor(2007)
  - Lax Supervision and Regulation– failure to monitor financial innovation and increased leverage (Calomiris 2017)
- Fuels Credit driven house price boom and bust and global FC
- Successful LLR reflecting learning from 1929-33
- But unorthodox policies threated CB credibility and independence
- Post GFC increased financial regulation (Dodd Frank 2010 and Basel III)
- Based on belief that GFC caused by financial sector imbalances leading to credit driven AP booms
- Return to Financial Repression?

Financial Crises in Historical Perspective: Empirical Dimensions

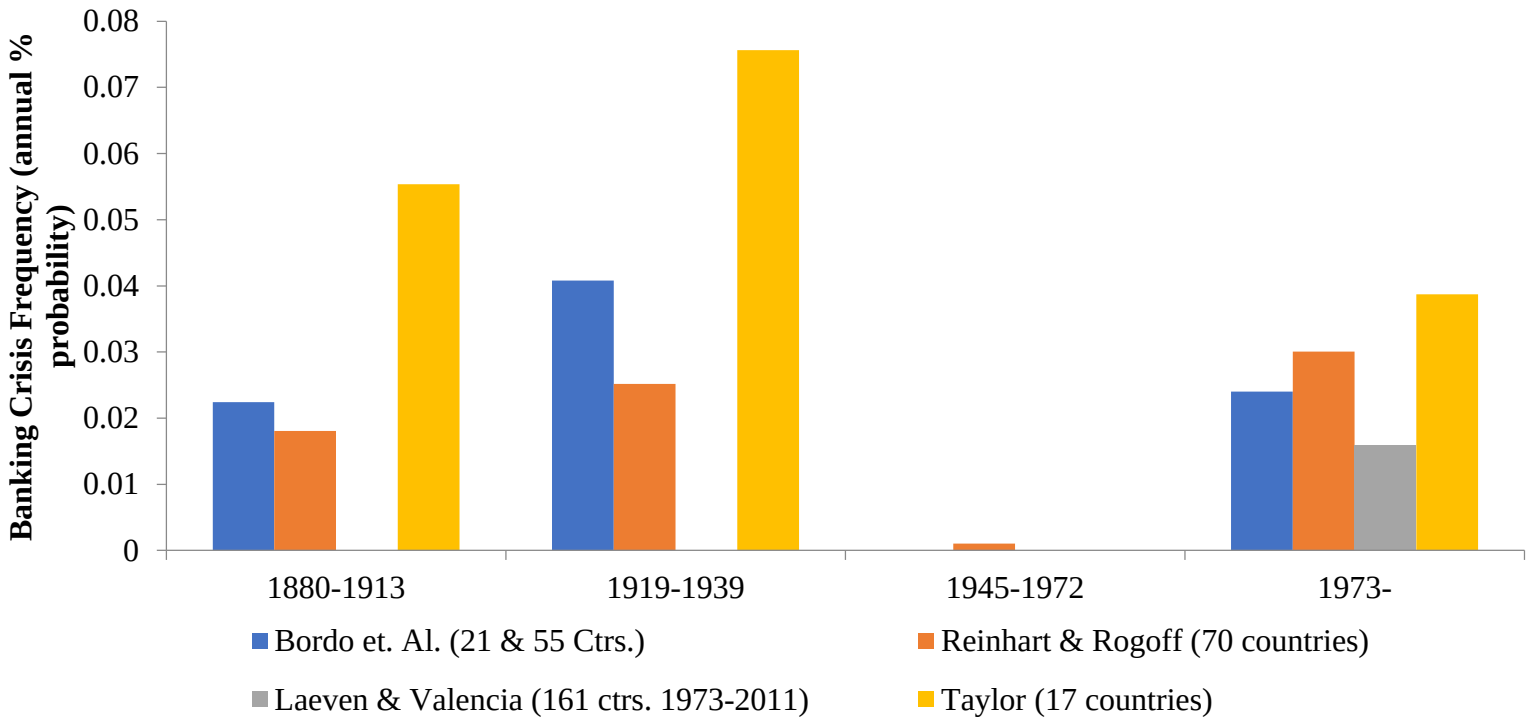
- To understand clearly the link between the monetary and financial policy regimes and financial stability it is crucial to understand the record of the most extreme form of financial instability—financial crises
- Not only has the FC problem returned with a vengeance in the second era of globalization since 1973 to rival its presence in the first era of globalization pre 1914
- But the output losses have been rising in recent years closer to those of the IW
- This explains why the emphasis on financial stability has become so prominent

Financial Crises in Historical Perspective: Measurement

A. The Incidence of FCs (banking crises)

- Figure 1 shows the incidence of banking crises across 4 historical regimes using the most recent data bases (Bordo and Meissner 2016)
- We are" back to the future" the incidence of FCs (banking) since 1973 is close to pre 1914
- There were no banking crises under BWS and the incidence was highest in the IW

Financial Crises in Historical Perspective: Measurement – Figure 1



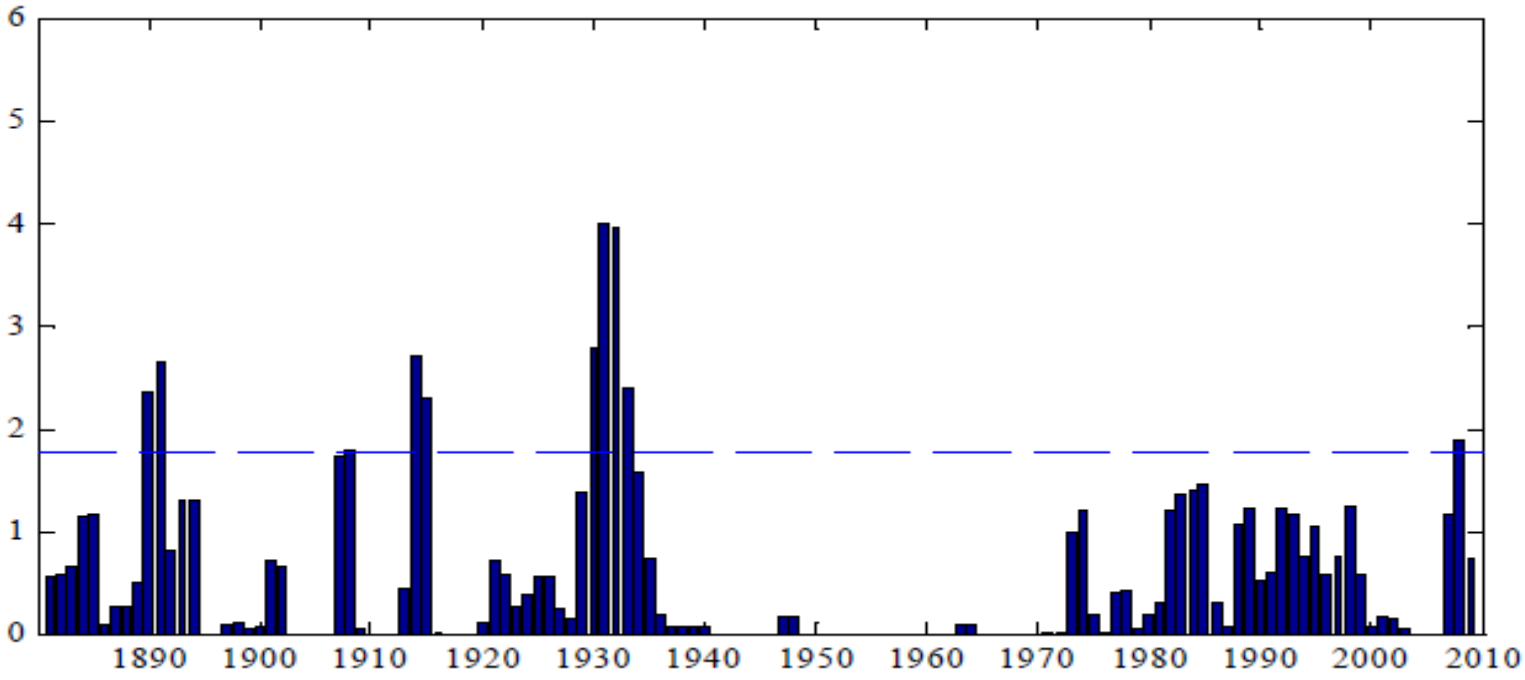
Source: Bordo and Meissner (2016)

Financial Crises in Historical Perspective: Measurement

B. Global Financial Crises

- Global FCs occurred in many countries across continents
- See Figure 2
- Bordo and Landon Lane (2010) identified 5 global banking crises: 1890-91, 1907-08, 1913-1914, 1931-32, 2007-2008
- See Table 1 for the countries involved
- In terms of severity (output losses) 2007-2008 was on a par with 1907-08 and much less than 1931-31

Financial Crises in Historical Perspective: Measurement – Figure 2



Source: Bordo and Landon-Lane (2010)

Financial Crises in Historical Perspective: Measurement – Table 1

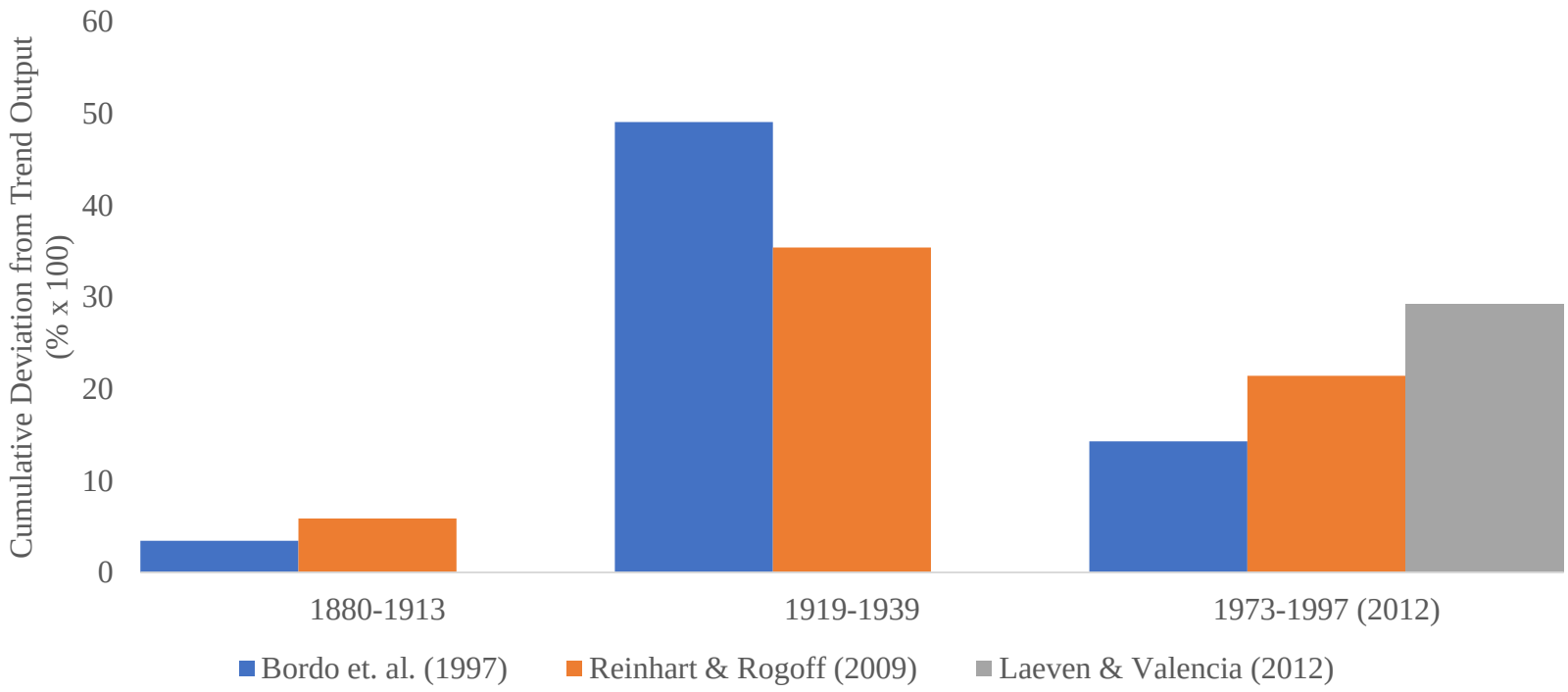
Period	Countries Involved
1890-1891	Argentina, Brazil, Chile, Germany, Italy, New Zealand, Paraguay, Portugal, South Africa, UK, USA
1907-1908	Chile, Denmark, Egypt, France, Italy, Japan, Mexico, Sweden, USA
1913-1914	Argentina, Belgium, Brazil, France, India, Italy, Japan, Mexico, Netherlands, Norway, UK, Uruguay, USA
1931-1932	Argentina, Austria, Belgium, Brazil, China, Denmark, Finland, France, Germany, Greece, Italy, Norway, Portugal, Spain, Sweden, Switzerland, Turkey, USA
2007-2008	Austria, Belgium, Denmark, France, Germany, Greece, Ireland, Netherlands, Portugal, Russia, Spain, Sweden, Switzerland, UK, USA.

Source: Bordo and Landon-Lane (2010)

Financial Crises in Historical Perspective: Output Losses

- A key reason that FCs are deemed so important is that they lead to large output losses
- Figure 3 shows this evidence
- The losses comparing the two eras of financial globalization reflect “back to the future” but recently they are getting worse moving in the direction of the interwar (Bordo and Meissner 2016)

Financial Crises in Historical Perspective: Output Losses – Figure 3



Source: Bordo and Meissner (2016)

Financial Crises in Historical Perspective : Determinants

- A meta study of the literature on the determinants of financial crises suggests that no one factor is dominant (Bordo and Meissner 2016)
- Dominant factors are:
  1. absence of LLR
  2. poor supervision and regulation
  3. weak bank structure
  4. financial sector liberalization
  5. credit booms
- Credit booms are more important in studies focusing on recent decades while absence of LLR dominates pre WWII

Financial Crises in Historical Perspective : Narratives from 12 famous FCs.

- I present narratives on 12 very important and serious FCs in the past two centuries
- UK 1825, 1847, 1866, 1890;
- US 1873, 1893, 1907, 1929-33, 2007-2008, Australia 1893, Japan 1990, Nordics 1990

Financial Crises in Historical Perspective: narratives from 12 famous FCs

- Table 2 shows key characteristics of serious FCs (real GDP declines by 5%):
  - whether part of a global FC
  - the E regime in place
  - whether it was a twin crisis (banking and currency)
  - whether it was associated with a credit boom
  - whether a CB was in place
  - whether it was allayed by a LLR
  - whether it was fiscally resolved
  - the type of banking structure in place (unit, branching, universal)

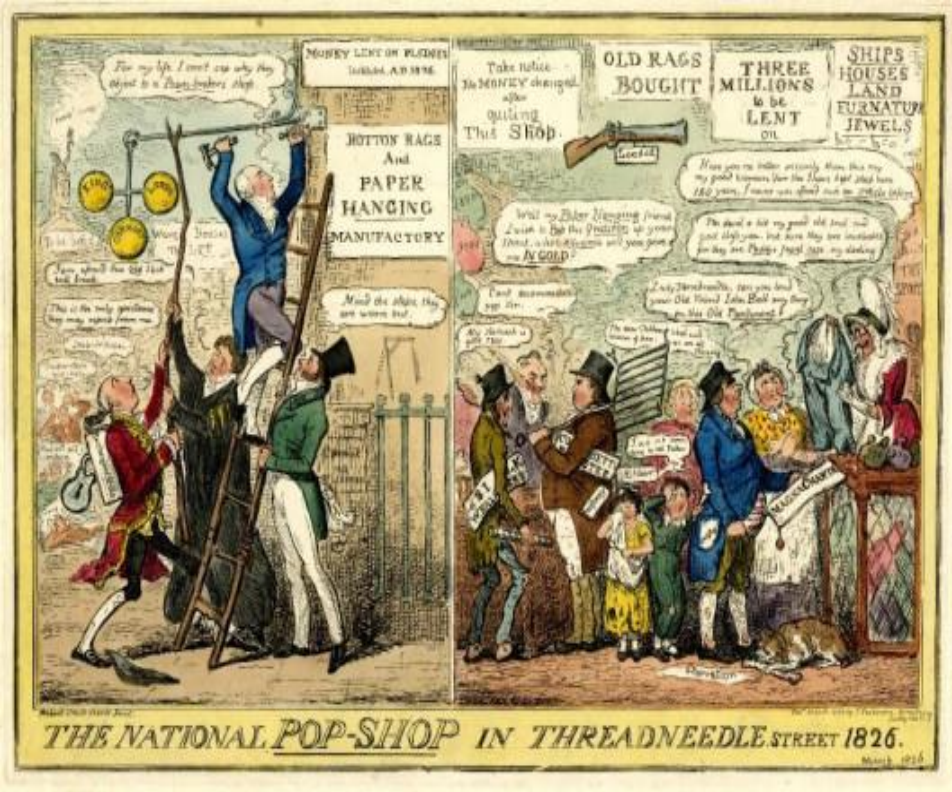
Financial Crises in Historical Perspective: narratives from 12 famous FCs – Table 2

Major Banking Crises 1825-2008													
Crisis year	Country	Serious (%ΔGDP)	Output loss (%)	Currency crisis	Global crisis	ER Regime	Credit boom	CB in place	LLR	Crisis year	Country	Fiscal resolution	Banking structure
1825	UK	Yes (na)	NA	Yes	Yes	Gold	Yes (Latin America)	Yes	Ineffective	1825	UK	Treasury letter	Unit
1847	UK	Yes (-2.53)	NA	No	No	Gold	Yes (Railroad)	Yes	Ineffective	1847	UK	Treasury letter	Unit
1866	UK	Yes (-1.25)	NA	No	No	Gold	No	Yes	Ineffective	1866	UK	Treasury letter	Branch
1890	UK	No (-4.94)	8.91	No	Yes	Gold	Yes (Argentina)	Yes	Effective	1890	UK	Treasury backstop	Branch
1893	Australia	Yes (-20.5)	90.65	No	Maybe	Gold	Yes (Land)	No	No	1893	Australia	Yes	Branch
1873	US	Yes (-19.33)	NA	No	Yes	Greenback (paper)	Yes (Railroad)	No	No*	1873	US	No	Unit
1893	US	Yes (-11.11)	8.65	Yes	Maybe	Gold	No	No	No*	1893	US	No	Unit
1907	US	Yes (-10.21)	55.65	No	Yes	Gold	No	No	No*	1907	US	No	Unit
1929	US	Yes (-30.76)	101	Yes	Yes	Gold	Yes (Wall Street)	Yes	No	1929	US	No**	Unit
1990-1992	Nordics†	Yes (-3.9)	45.65‡	Yes	No	Fixed	Yes (Real Estate)	Yes	Effective	1990-1992	Nordics	Yes (bailouts)	Universal
1991	Japan	Yes (-0.025)	18.3	No	No	Floating	Yes (Real Estate)	Yes	Ineffective	1991	Japan	Yes (bailouts)	Universal
2007	US	Yes (-5.71)	26.2	No	Yes	Floating	Yes (Real Estate)	Yes	Effective	2007	US	Yes (bailouts)	Universal

Notes: ***† Finland, Norway and Sweden***
‡ Finland and Sweden
**** Clearing houses***
***** Reconstruction Finance Corporation***
Sources: ***Bordo (2003); Bordo and Landon-Lane (2012); Bordo and Meissner (2016)***

Financial Crises: Narratives Pre WWII - UK

- **1825 London:**
  - First global FC, Latin American lending boom, stock market crash, banking panic ineffective LLR
- **1847 London:**
  - railroad driven stock market boom and expansionary monetary policy stock market crash banking panic ineffective LLR



Financial Crises: Narratives Pre WWII - UK

- **1866 Overend Gurney Crisis**
  - Insolvency of major Discount house in London, BOE lets it fail
  - Banking panic, LLR ineffective

Financial Crises: Narratives Pre WWII - UK

- **1890 Barings Crisis London**
  - Insolvent major merchant bank overexposed to Argentine bonds in a real estate boom/bust. BOE arranges life boat rescue.
  - No panic in London (huge crisis in Latin America)

Financial Crises: Narratives - Australia 1893

- **1893**
  - Massive lending boom in Australian land financed by capital inflows from UK via pastoral companies and Australian banks.
  - When TOT fell in late 1880s banks failed, sudden stop of UK capital.
  - massive banking panic, no LLR

Financial Crises: Narratives - US pre WWII

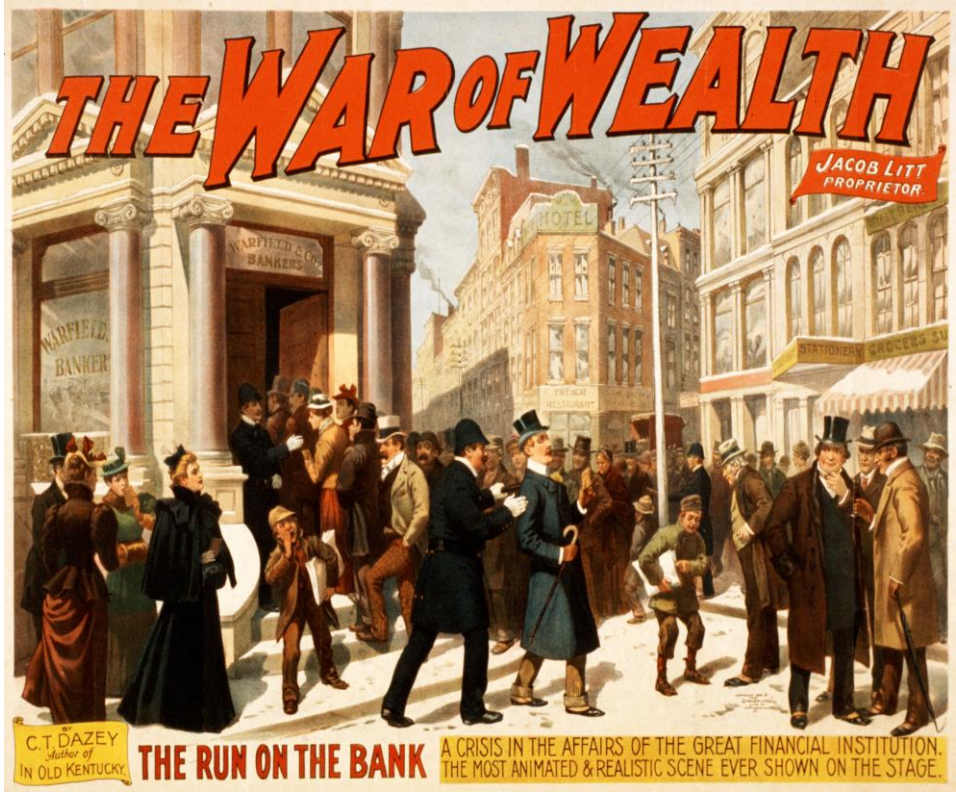
- Pre Civil war period after demise of Second Bank
- State banking regulation , unit banks, inefficient payments system, no LLR,6 banking panics
- Post Civil war National Banking System (NBS).
- Improved payments system but still many crises because of flaws in NBS
- (inverted pyramid of credit and no LLR although clearing house Loan Certificates were an imperfect substitute)

Financial Crises : Narratives - US pre WWII

- **1873**
  - Railroad lending boom financed by UK capital, corporate malfeasance and corruption, sudden stop of K from London, Stock market crash, panic, ineffective LLR

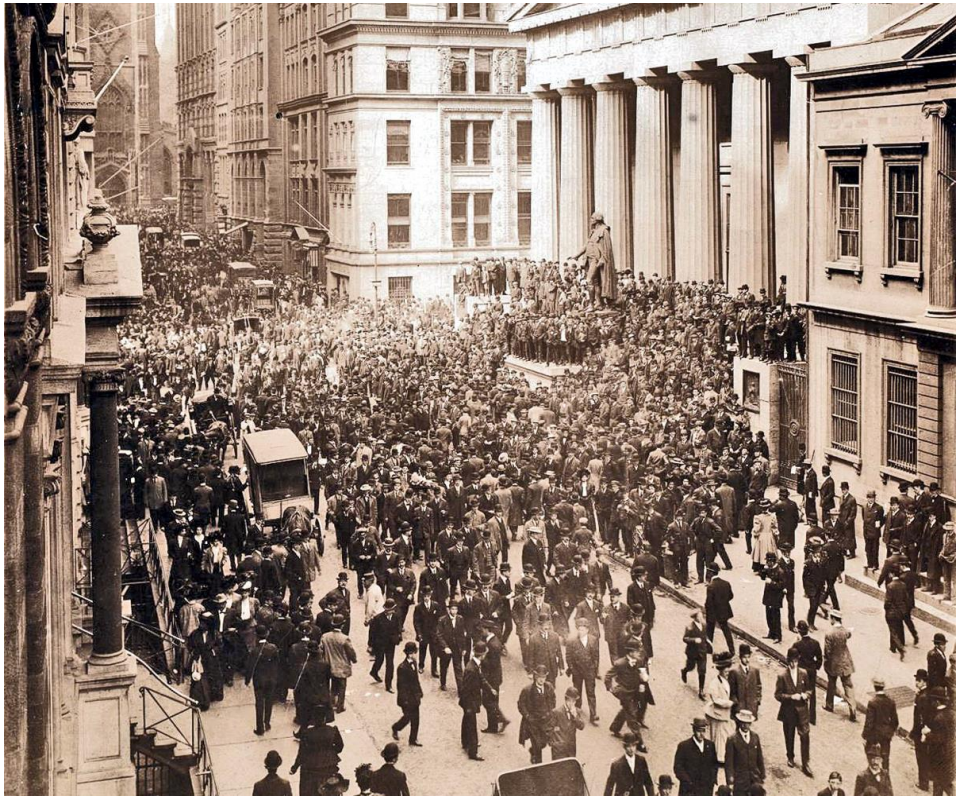
Financial Crises : Narratives - US pre WWII

- **1893**
  - Capital flight driven by political uncertainty from Free Silver Movement leads to stock market crash and 2 banking panics.
  - Ineffective LLR by NYCH and JP Morgan.



Financial Crises : Narratives - US pre WWII

- **1907**
  - Key banking panic pre 1914. Led to establishment of the Federal Reserve
  - Sudden stop of K flows to US after BOE raises Bank rate to stem gold loss due to payout by Brit insurance companies after SF earthquake (Odell and Wiedenmeir 2004)
  - Stock market crash, insolvencies of Trust companies not rescued by NYCH leads to panic.
  - Panic insufficiently allayed by JP Morgan and NYCH loan certificates.



Financial Crises : Narratives - US pre WWII

- **1929-33**
  - Main event is Wall street boom financed by equities and bank credit.
  - Two policy mistakes by the Fed (real bills doctrine): trying to kill the boom; and then failure to allay 4 banking panics 1930-33; led to the Great Contraction

Financial Crises: Narratives - Post WWII

- Post BWS liberalization (removal) of domestic and international controls combined with Great Inflation leads to return of banking crisis problem.
- Aggravated by guarantees and TBTF doctrine
- **Japan 1990**. Real estate and stock price boom in 1980s fueled by easy monetary policy. BOJ pricks boom leads to collapse in AP prices and banking crisis . Forbearance dragged out resolution for a decade
- **Nordics** 1990. Liberalization of domestic financial system and removal of K controls leads to lending booms financing real estate accommodated by loose monetary policy
- Banking crises follow in 1991
- Fiscally resolved at great cost

Financial Crises: Narratives - Post WWII

- **US Subprime Mortgage Crisis 2007-2008**
- Unprecedented housing boom caused by: government housing policy (Rajan 2010), loose monetary policy (Taylor 2007)
- Crisis erupts after Fed tightens monetary policy in 2005-6 and ends housing boom
- Packaging of low quality mortgages in MBS held by shadow banks and commercial banks leads to interbank lending freeze reflecting fears of counterparty insolvencies
- Fed provided LLR and loose M policy fall 2007
- Big policy mistake in September 2008 when Fed lets insolvent Investment bank Lehman Bros go after having bailed out Bear Stearns in similar circumstances in March 2008
- Creates global liquidity panic
- Resolved by unorthodox LLR and credit policies and inter CB policy coordination

Financial Crises: Narratives - Post WWII

- **Eurozone Crisis 2010-2013**
- Fiscal resolution of subprime mortgage related losses in European banks
- Worsened by clean up of several national housing busts led to big run ups in debt in EZ countries which led to a link between banking crises and fiscal crises (Bordo and Meissner 2016)
- Fear of Greek debt default leads to contagion to other EZ countries
- Leads to banking crises in countries whose banks are exposed to sovereign debt
- Resolved by bail outs and bail ins by Troika (ECB, IMF, EU)
- Draghi (2013) “whatever it takes speech”

Financial Crises: Narratives - Summary

- The history of FCs in the past two centuries reveals considerable heterogeneity in the circumstances in which they arose, their causes and how they were resolved
- The key causes involved domestic and external shocks , weak banking structure and supervision and regulation, lending booms and busts, some driven by bank credit others by foreign bond and equity inflows.

Financial Crises: Narratives - Summary

- The key ingredient in how a crisis played out was the presence or absence or failure of the monetary authorities provision of LLR
- In the past two decades the fiscal authorities are a key player
- With the advent of the financial safety net and government guarantees banking panics have morphed into costly fiscal crises
- Credit driven asset price booms , the cause of FCs emphasized since 2008 , were important in a few big crises before WWII but not the majority
- Since the collapse of BWS and the return of financial globalization and domestic liberalization, financial instability has returned

Financial Crises: Narratives - Summary

- Since the 1970s major financial innovation has allowed banks to fund themselves in the financial markets and not have to rely on their deposit base (Schularick and Taylor 2012)
- This has allowed bank credit to grow faster than the money supply, has increased leverage , and may have been a key factor triggering asset price booms and possible financial crises since the 1980s.
- Financial innovation has led to the growth of shadow banks which are outside the traditional supervisory and regulatory networks.
- These innovations have increased both liquidity and leverage in the financial system and has created a new source of systemic risk which can increase financial instability

Credit Booms, Asset Price Booms and Financial Crises

- The GFC led to new perceptions about the causes of FCs – new emphasis on the role of credit driven asset price booms
- And new policy prescriptions
- I ask 3 questions:

1. What is the incidence of credit booms associated with banking crises – do credit booms peak before or coincident with banking crises?
2. What is the incidence of equity boom/busts and housing prices boom/busts associated with banking crises? – do they occur shortly before or coincident with banking crises?
3. What is the relationship between these types of events and serious banking crises associated with deep recessions?

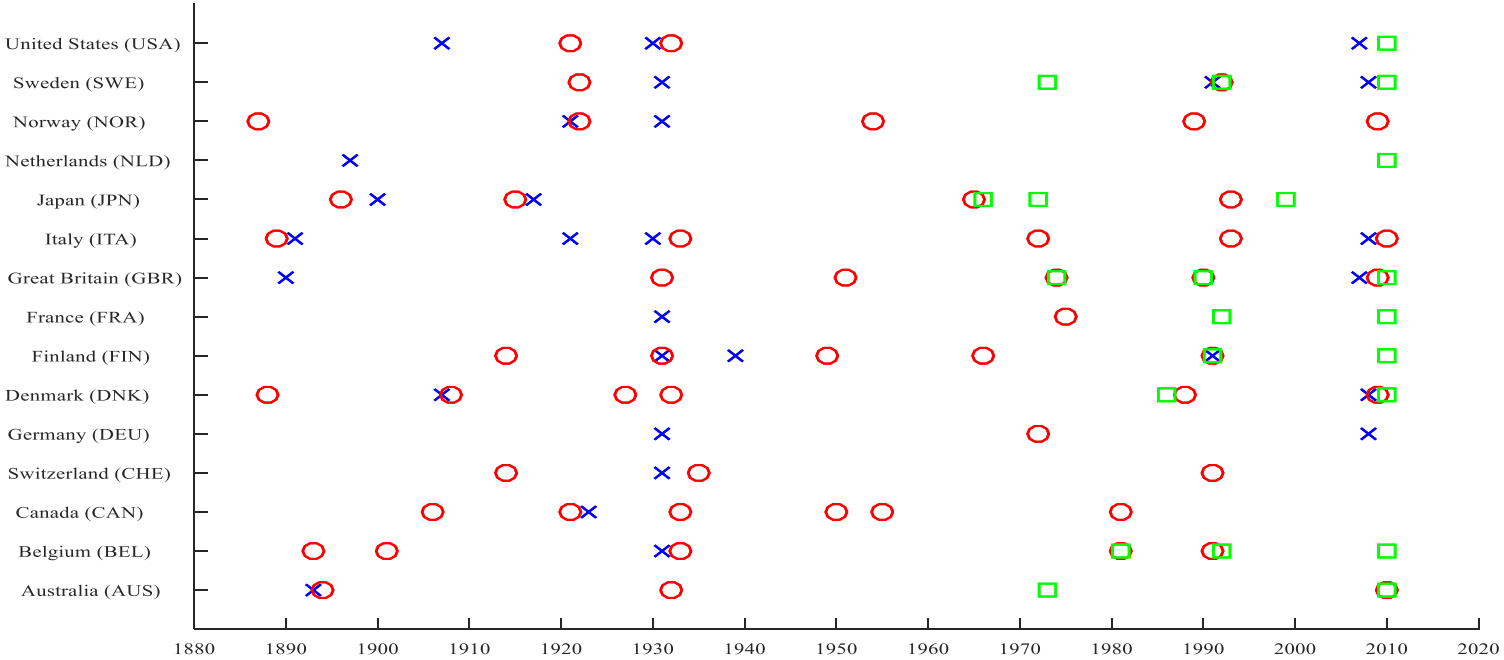
Credit Booms, Asset Price Booms and Financial Crises

- I use business cycle methods to identify credit cycles and AP boom/busts (Bordo and Landon-Lane (2013))
- Credit booms are identified following Gorton and Ordoñez (2016)
- A good credit boom is related to the growth of TFP (eg railroads) in the nineteenth century, the internet today
- A bad credit boom ends in a financial crisis because the TFP fizzled
- Their identification rule is that a credit boom starts with 3 periods of growth averaging more than 5 % per year and ends with 2 periods of negative growth
- Two annual data bases for 15 countries are used to measure credit: a) total loans divided by GDP from Jordà et al. (1880-2010); b) domestic credit to the private sector divided by GDP from the World Bank (1973 to 2010).

Credit Booms and Financial Crises

- Figure 4 compares credit booms to major financial crises associated with recessions with output drops greater than 5% .
- The percentage of credit boom peaks that peaks within 1 year of a financial crisis is 3.75% and the percentage of credit booms that precede or are in the same year is even lower at 2.6%
- These results are quite dramatic. They suggest that credit booms induced big crises like the Great Contraction of 1929-33 are very rare –about once every 50 years.
- It raises the question whether there should be a major financial stability regime change

Credit Booms and Major Financial Crises – Figure 4



Major Banking Crises (blue x's), Credit Boom Peaks (loans) (red circles), Credit Boom Peaks (Gorton) (green squares)

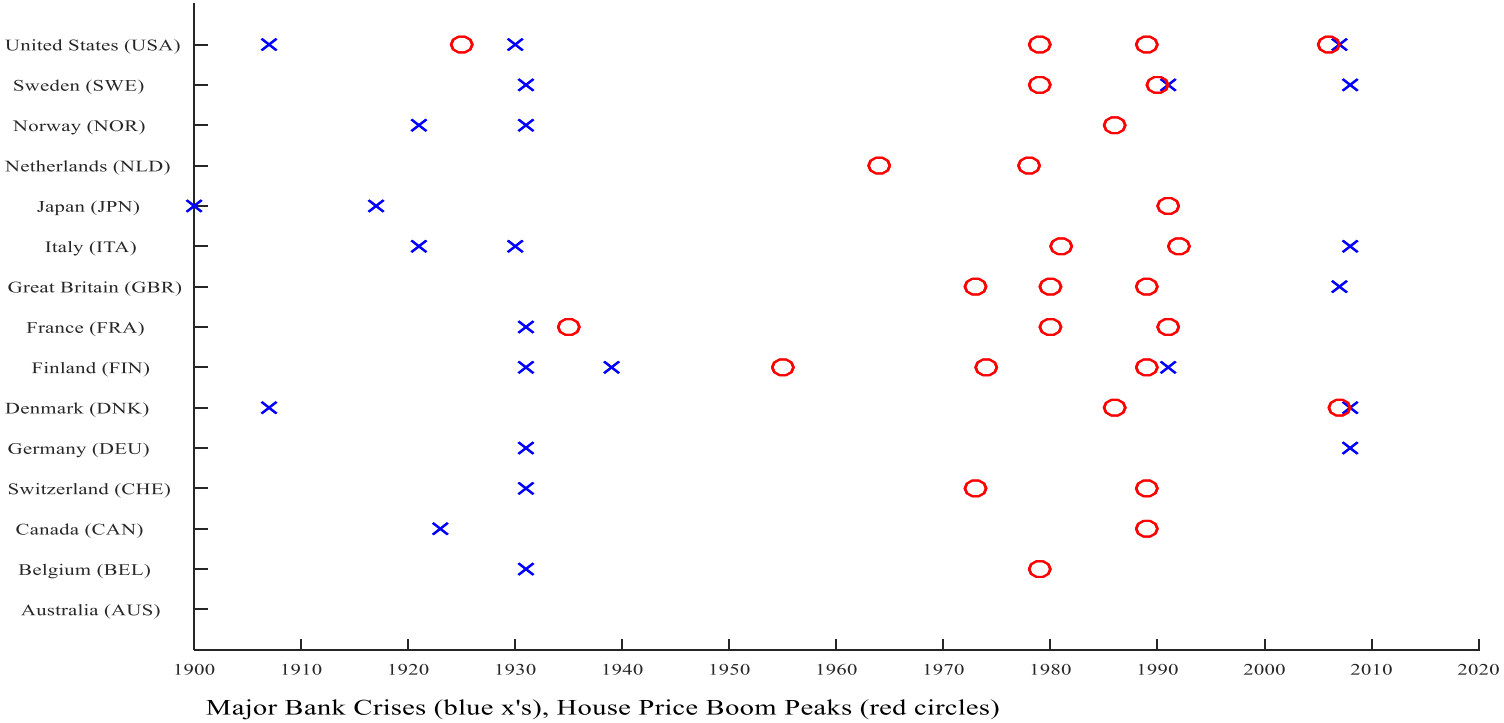
Credit Booms, Asset Price Booms and Financial Crises

- Figure 5 compares housing boom busts with major banking crises.
- 11% of house price booms that peak occur within one year of a banking crisis and 11% occur one year before or coincident with a banking crisis

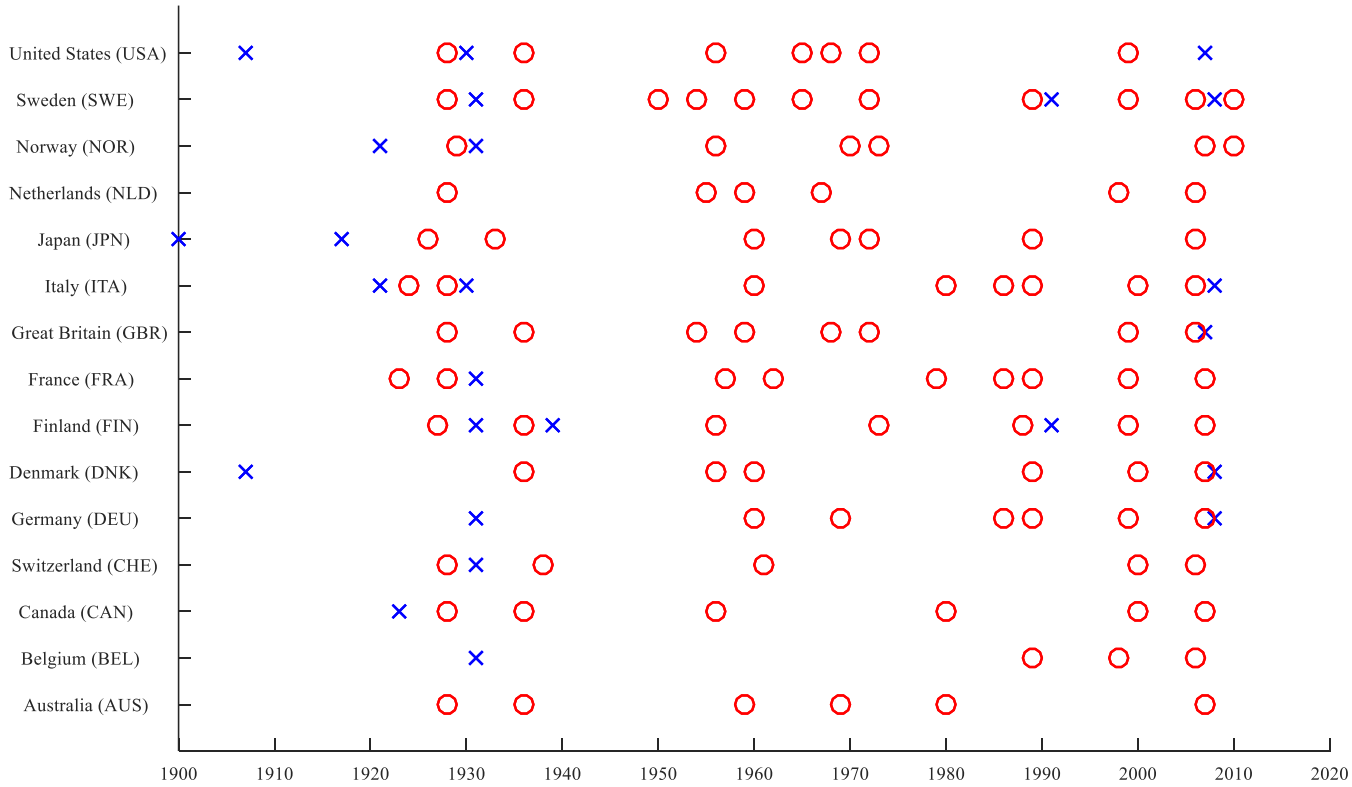
Credit Booms, Asset Price Booms and Financial Crises

- Figure 6 compares stock market booms with major banking crises
- Only 3% of stock market booms occur within one year of a major banking crisis and 3% occur one year before or are coincident with crises
- These results agree with many studies which find housing busts more associated with crises than stock market crashes

House Price Booms and Major Financial Crises – Figure 5



Stock Price Booms and Major Financial Crises– Figure 6



Major Banking Crises (blue x's), Stock Price Boom Peaks (red circles)

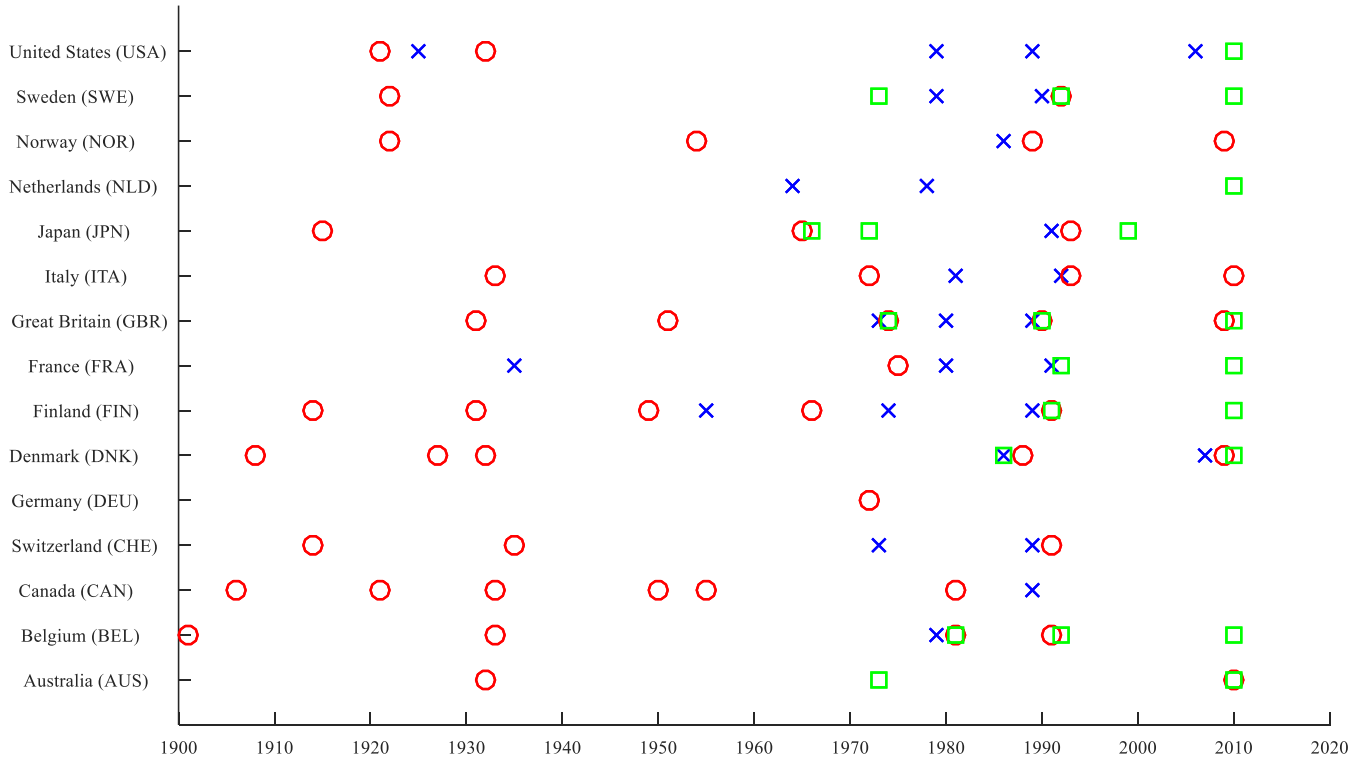
Credit Booms, Asset Price Booms and Financial Crises

- Figure 7 compares house price busts with credit boom peaks
- For loans to GDP 6.3 % of credit booms peak within one year of a housing bust. For total credit it is 7.2%.
- No credit booms occur one year before or coincident with a housing bust for loans while 1.4% is the case for total credit

Credit Booms, Asset Price Booms and Financial Crises

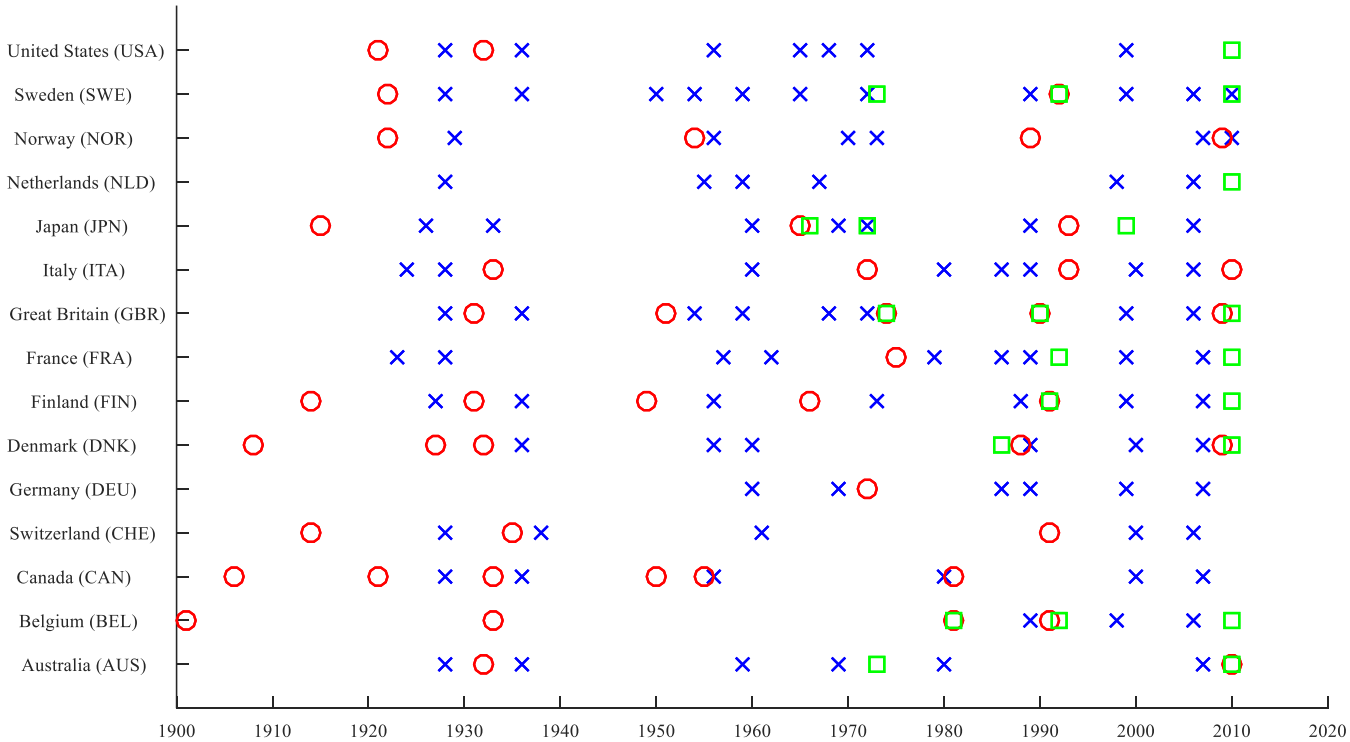
- Figure 8 shows the connection between credit boom peaks and stock market crashes
- The results are not too different from housing busts
- This suggests that credit booms only have a very limited connection with asset price booms/busts

House Price Booms and Credit Booms – Figure 7



House price peaks (blue x's), Credit Peaks (Loans) (red circles), Credit Peaks (Gorton) (green squares)

Stock Price Booms and Credit Booms – Figure 8



Stock price peaks (blue x's), Credit peaks (loans) (red circles), Credit Peaks (Gorton) (green squares)

Credit Booms, Asset Price Booms and Financial Crises : Summary

- The evidence suggests that the coincidence between credit boom peaks and serious financial crises are quite rare
- It also suggests that the coincidence between credit boom peaks are not very closely connected to asset price busts
- Most of the coincidence occurs across all of the figures in two perfect storm episodes ; The Great Contraction 1929-33 and the GFC

Credit Booms, Asset Price Booms and Financial Crises : Summary

- This leads to the question whether such rare events should lead to a sea change in monetary policy and financial stability policy
- After the Great Contraction the worlds' monetary authorities believed it should and it led to 40 years of financial repression
- That strategy led to unintended consequences driven by the dynamics of financial innovation and may in turn have set the seeds for the GFC 80 years later

Credit Booms, Asset Price Booms and Financial Crises

- The current obsession with financial stability and especially the increased use of the tools of macro prudential policy and LAW raises the risks of repeating the mistakes of the 1930s
- And creating a new regime of financial repression which will most likely have unintended consequences
- It will likely head off a few minor financial crises in the next few decades but much later down the road precipitate an even bigger FC than 2007-2008

Credit Booms, Asset Price Booms and Financial Crises

- There is an analogy with policies to prevent natural disasters
- Scholes (2009) gives the analogy between firefighters putting out every small fire in Yellowstone Park, leading to the growth of underbrush and setting the stage for multiple lightning strikes to cause fires leading to much greater devastation
- Financial Regulators do the same thing when they dampen volatility
- It leads to greater risk-taking and the risk of a major FC

Lessons from History

- The survey of the record on the link between monetary regimes and financial stability in advanced countries in the past two centuries shows a varying evolution between monetary stability and financial stability
- It involved a slow learning process by the CBs

Lessons from History

- A key lesson from the historical record through the Great Moderation period was that if four key principles are followed a stable monetary policy regime can be compatible with financial stability
  1. Credibility for price stability (low inflation)
  2. Real macro stability
  3. a credible rules based LLR
  4. sound financial supervision and regulation and banking structure
- Canada has avoided banking crises altogether by pretty closely following these principles
- A key difference between Canada and the US has been sound banking structure and prudent financial regulation

Lessons from History

- The GFC of 2007-2008 like the 1930s was blamed on the banks and the financial system
- This led to the creation of a new regime of financial regulation and the elevation of the financial stability mandate to primary importance
- And to the current case for elevation of the financial stability mandate to paramount importance and encouraging CBs to use their policy tools to head off credit driven asset price booms
- It is based on the assumption that serious FCs are largely caused by credit driven AP booms and the failure of monetary and financial regulatory authorities to head them off

Lessons from History

- Our empirical evidence casts doubt on this assumption
- FCs are very heterogeneous.
- Moreover serious FCs with credit booms are very rare

Lessons from History

- The recent GFC may have been a rare one off event , a perfect storm (with multiple causes)
- Like 1929-33
- This raises the question whether such rare events should lead to a sea change in monetary policy and financial stability policy as occurred after the Great Contraction
- That strategy created an environment of financial repression which did provide financial stability but which also set in place forces which led to unforeseen and eventually serious threats to financial stability
- And may have sown the seeds for the GFC 80 years later

Lessons from History

- The current obsession with financial stability risks recreating some of the mistakes of the 1930s, 40s, 50s, and 60s
- In addition to financial repression the adoption of many of the tools of macro prudential regulation that have been proposed may recreate many of the problems with the use of these tools in the past
- Many of these macro prudential policies were credit or fiscal policies which greatly involved the MA in inefficiently picking winners and losers and influencing the allocation of resources.
- They also impinged on CB independence
- The pursuit of such an enhanced financial stability strategy may head off a few minor crises in the next few decades
- But much later precipitate an even bigger crisis than we saw a decade ago

Lessons from History

- My survey of the historical record on the connection between the monetary regime and financial stability teaches us that a knowledge of history matters
- Basing important regime changing decisions on the record of the last crisis ignores the heterogeneity of the crisis problem.
- History teaches us the importance of relearning the details of the events of the past which often contain important and long forgotten clues to aid in understanding of the “crise du jour”.