New Central Banks*

The desire to help build up a soundly based banking system and develop an active and independent monetary policy has continued to encourage the establishment of central banks, particularly in the newly independent countries. During the last three years alone, fifteen such institutions have opened their doors. Ten of these began operations in 1964: the Bank of Lebanon, the Central Bank of Jordan, the Bank of Sierra Leone, the National Bank of the Congo (Kinshasa), the National Bank of Rwanda, the Bank of the Republic of Burundi, the Reserve Bank of Rhodesia, the Reserve Bank of Malawi, the Bank of Zambia, and the Central Bank of Trinidad and Tobago. In 1965 the list was extended by the opening of the Bank of Guyana and the Central Bank of the Republic of Brazil. The Central Bank of Kenya, the Bank of Tanzania, and the Bank of Uganda were set up in 1966.

These banks are indeed new, in that they are operating under new statutes and have an expanded arsenal of monetary policy instruments at their disposal. But each of them is the successor to one or more institutions that previously exercised some form of monetary authority. Thus, in two of the countries, commercial banks formerly carried out many central banking functions. The Central Bank of the Republic of Brazil has taken over powers hitherto held by the Bank of Brazil, with a new policy-making body —the National Monetary Council—replacing the previous Superintendency of Money and Credit (SUMOC). Lebanon's new central bank has assumed responsibilities formerly discharged by the largely foreign-owned Bank of Syria and Lebanon. Six of the new institutions are derived from former central banks in territories or political units that were subsequently split up: the dissolution of the Federation of Rhodesia and Nyasaland in late 1963 led to the separate central banks of Zambia, Malawi, and Rhodesia,[1] and new central banks have replaced the former Bank of Issue of Rwanda and Burundi and the Congo's temporary Monetary Council (both of which had superseded the Central Bank of the Belgian Congo and Ruanda-Urundi in 1961). The seven other new central banks in the group grew out of currency boards, which issued currency and conducted foreign exchange operations. In this category are the new central banks in Kenya, Tanzania, and Uganda (which replace the East African Currency Board) and those in Guyana, Sierra Leone, Trinidad-Tobago, and Jordan.

The new central banks in Lebanon, the Congo, Rwanda, and Burundi—as well as several others established in 1959-63—have been analyzed in a previous article, and their statutes will not be dealt with here.[2] The functions, powers, and organization of the remaining eleven banks are discussed below.

BACKGROUND

All these new central banks have been established in less developed countries, where overseas trade and foreign capital play a large role in the economy; furthermore, many of them operate in areas where the existing commercial banks are often branch offices or subsidiaries of major banks based elsewhere. However, the financial and monetary environments of these countries differ consider-

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[1] On December 3, 1965, after Rhodesia's unilateral declaration of independence, the United Kingdom dismissed the existing Board of Governors of the Reserve Bank of Rhodesia and named a new Board domiciled in London. The Reserve Bank of Rhodesia continues to operate in that country, however, with a Board appointed locally. In this article, discussion of the bank is confined to a description of its statutory powers as they are set forth in the 1964 law.

[2] See "New Central Banks", this *Review* (July 1964), pages 133-37.

ably in structure and stage of development. Financial dualism—wherein sophisticated and advanced mechanisms are found side by side with the most rudimentary facilities—is a common situation. The wide diversity in the extent to which banking habits have developed is evident in the variation of the ratio of currency to total money supply,[3] which ranges from 70 per cent in Sierra Leone to 20 per cent in Brazil (the current figure for the United States is 22 per cent). Population per banking office, another measure of the development of banking, ranges from 19,000 in Trinidad-Tobago to 45,000 in Jordan and 137,000 in Tanzania (the figure for the United States is 6,400).

The nature of a central bank in any country is, in part, determined by its relationship to the government, both as defined in the statutes and in actual practice. Among the major issues involved in this relationship are the degree of independence the central bank exercises vis-à-vis executive and legislative authority and the extent to which the government is limited in using central bank credit to finance its operations. The nature of the central bank is shaped also by its relationship to the financial community. Here a balance must be struck between the needs to assure the stability of the banking and financial system and to foster the growth of that system—so necessary for the evolution of less developed countries. Finally, there is the problem of external monetary stability, which calls for the maintenance of an orderly exchange market for a country's currency and the attainment of a level of international reserves which is adequate to meet the swings in the country's balance of payments. Because financial institutions and experience vary so greatly among nations, the theory and practice of central banking do not provide a single set of prescriptions which deals with all these issues. Thus, the statutory provisions reviewed here describe a variety of techniques by which the new central banks will endeavor to resolve these and related problems within the context of their own environment.

OBJECTIVES, FUNCTIONS, AND STRUCTURE

The statutes of the new central banks often specify economic and social goals to be served by the monetary authorities. In line with the trend of central banking legislation since World War II, most of the new banks stress economic growth and development as the primary goal. The statute of the Central Bank of Trinidad and Tobago specifies this goal most concretely, emphasizing the expansion of production, trade, and employment. More conventional objectives are internal monetary stability, set forth in all the new banks' charters, and stable exchange rates, which only Guyana does not specifically include. While all the banks maintain research facilities, the statute of Trinidad-Tobago underscores the role of the central bank in aiding development by requiring continuous economic, financial, and monetary research.

To serve these objectives, the new central banks are given the following powers: the sole right of note issue,[4] authorization to buy and sell gold and foreign exchange, and freedom to engage in open market operations. All the institutions serve as banker and financial adviser to their respective governments and, with the exception of Brazil,[5] act as government fiscal agent. Moreover, to aid in the control of credit and the supervision of commercial banks, the new banks are vested with at least some of the following powers: implementation of minimum reserve requirements; establishment of minimum liquid asset ratios; direct control of the volume, terms, and conditions of commercial bank credit; regulation of interest rates charged or paid by banks; and examination of bank records.

The central banks in this discussion are legally defined as corporate bodies, with authorized capital ranging from $1.4 million equivalent for Malawi to $5.6 million equivalent for Uganda. This capital is fully held by the respective governments, except in Brazil where the central bank owns its equity capital outright. In all cases provision is made for reserve funds, from one to three times the authorized capital, to which a varying percentage of central bank profits is allocated. Beyond the maximum limit of these reserve funds, profits accrue to the governments, except in Brazil, where the central bank keeps all earnings from its operations.

In most cases responsibility for bank policy and administration is vested in a board of governors, ranging in size from five members in Sierra Leone, Malawi, and Guyana, to nine members in Uganda, Zambia, and Rhodesia. The governor and deputy governor are usually appointed by the executive head of government, and serve

[3] The money supply definition used here is that of the International Monetary Fund, which includes currency outside banks and demand deposits; government deposits are excluded.

[4] In Guyana, however, a subsidiary of Barclays Bank Limited retains the right to issue bank notes so long as certain United Kingdom laws continue to apply as part of the banking code of the country.

[5] In that country, the Bank of Brazil continues in its former capacity as fiscal agent of the government.

terms of three to seven years. Exceptions are Jordan, where appointments are made by the government's Council of Ministers, and Tanzania, where the length of term for governor and deputy governor is not specified by statute. In Brazil central bank policy is set by the autonomous National Monetary Council. This body has nine members: the finance minister, who acts as chairman, the presidents of the Bank of Brazil and the National Economic Development Bank, and six Brazilians of financial and banking background. Four of these last six serve as directors, with one acting as president, of the central bank and have the responsibility of implementing decisions of the National Monetary Council.

RELATIONS WITH THE GOVERNMENT

Along with their powers and duties, the new central banks' relations with the government are usually closely defined in the founding statutes. Important sections of these concern the coordination of monetary policy with the government's general economic policies. In Kenya and Tanzania, a Treasury representative is a voting member of the central bank's board of governors. In Tanzania he may postpone any of the board's decisions, and in Kenya he may suspend a vote by the board and refer the matter to the finance minister, whose decision is binding. In Trinidad-Tobago, Zambia, and Guyana, the minister of finance or his representative attends board meetings but does not vote; however, after consulting the central bank's governor he may, except in Guyana, issue general directives that bind the bank to implement government monetary and fiscal policies. Brazil provides for close government supervision through the fact that central bank policy is determined by the National Monetary Council headed by the finance minister.

A number of the statutes require government approval for specific operations by the central bank. Approval of the finance minister is needed by the central banks of Zambia, Malawi, Uganda, Tanzania, Sierre Leone, and Trinidad-Tobago if they wish to hold, sell, or subscribe to shares of any registered corporation.[6] Although the Rhodesian central bank may buy and sell foreign currencies outright, it may borrow them only with the finance minister's consent.

As fiscal agents to their governments, the central banks (except that of Brazil) have responsibility for administering government accounts, managing the public debt, and acting as depository for government funds. As bankers to their governments, all of them may grant short-term loans or advances to offset temporary deficiencies in budget revenues. Most of the statutes set limitations on these advances in respect to both maturity (usually a maximum of three months) and amount (figured as a percentage of estimated revenues for the current year). Sierra Leone, which limits advances to 5 per cent of current government budget revenues, appears to be the most stringent in this respect; in most of the other countries, the figure is 15 per cent to 20 per cent. The major exception is Brazil, which requires the National Monetary Council to authorize the central bank to cover, by direct purchase of Treasury bills, any portion of the government deficit not financed through other means.

RELATIONS WITH THE BANKING SYSTEM

Each of the new central banks has the power to control the supply of money and credit in its economy. The means for exercising this control include rediscount and open market operations, reserve requirements and minimum liquid-asset ratios, direct controls over commercial bank credit, and licensing, supervision, and inspection of commercial banks.

All the statutes except those of Jordan and Sierra Leone contain authorization to require the commercial banks to maintain a percentage of their deposit liabilities in the form of reserves at the central bank. In some of the countries, this reserve ratio—which must be uniform for all commercial banks—can be freely determined by the central bank, up to a given percentage of the banks' deposit liabilities. In Kenya, Tanzania, Uganda, and Guyana, the maximum is 20 per cent. In Brazil, where the National Monetary Council sets the ratio, it is 25 per cent, of which half may be required in the form of Treasury bills or public debt certificates. Trinidad-Tobago, on the other hand, sets only a minimum reserve requirement (5 per cent). In Zambia, Rhodesia, and Malawi, neither a ceiling nor a floor is established in the statutes. Rhodesia's central bank appears to have statutory authority to impose reserve requirements against the assets of commercial banks.

The bank statutes of Malawi, Jordan, Rhodesia, Guyana, and Zambia allow the central bank to require commercial banks and other financial institutions to maintain minimum liquid-asset ratios. Rhodesia's statute permits these percentage requirements to differ as between banks and acceptance houses.

All the new central banks can buy, sell, discount, and

[6] The Reserve Bank of Rhodesia may also buy and sell shares of registered corporations, but endorsement by the finance minister is not required.

rediscount securities of their governments but, except in Brazil, limitations are placed on the amount of such purchases. Three of the statutes set an absolute limit: those of Kenya and Trinidad-Tobago (both of which apply to total lending to government) and that of Jordan (which applies only to securities). In Uganda, Malawi, Sierra Leone, and Zambia, the limitation on holdings of government securities is a specified percentage of the bank's deposit liabilities; in Rhodesia it is defined as the bank's paid-in capital and general reserve fund plus 20 per cent of its deposit liabilities; and in Tanzania and Guyana it is a specified percentage of average government revenues over the preceding three financial years. In two countries —Brazil and Rhodesia—the central banks also may deal in securities issued by themselves.

All the statutes empower the central banks to purchase, sell, and rediscount credit instruments of commercial banks, generally including bills of exchange and promissory notes for commercial transactions involving the storage and movement of goods and for agricultural and industrial production. A number of the banking laws spell out in detail the permissible maturities for various categories of eligible paper. Instruments for financing agricultural or industrial production are usually acceptable for longer maturities than those covering commercial transactions—a differentiation through which the central banks can encourage the development and financing of certain sectors in their economies, while limiting credit flows to other sectors. Thus, Sierra Leone and Uganda rediscount paper for commercial transactions with maturities of up to 90 days and allow maturities of up to 180 days for paper financing the movement and marketing of agricultural or mineral products. In Jordan, the respective maximum maturities are three and nine months. Kenya, Tanzania, Guyana, and Trinidad-Tobago allow maturities of 180 days for all types of paper, but the first three of these countries provide that the limit may be extended to 270 days for paper financing agricultural or industrial production if it fosters the development of the economy. Brazil does not specify the types of assets that can be rediscounted, bought, or sold by the central bank. The latter has taken over the functions of the rediscount department of the Bank of Brazil, but the policy governing such operations is decided by the National Monetary Council.

All the central bank statutes specify the conditions under which loans and advances, backed by adequate collateral, may be extended to commercial banks. In Uganda, Jordan, Sierra Leone, and Malawi the maximum maturity is three months, while in Kenya, Tanzania, Trinidad-Tobago, and Guyana it is six months. Zambia, Rhodesia, and Brazil set no maximum. In Brazil, policy governing loan operations is established by the National Monetary Council.

Several of the new central banks have the power to establish interest ceilings. Those of Kenya, Uganda, Tanzania, and Guyana, and also the National Monetary Council in Brazil, are authorized to limit the interest rate that commercial banks may pay on deposits and other liabilities. With the exception of the central banks in Kenya and Tanzania, these same institutions may set minimum or maximum rates also on bank charges for loans, advances, and other forms of credit, including the establishment of preferential rates to encourage or limit credit to any particular sector of the economy.

Authority for direct controls on the amount and availability of commercial bank credit exists in a number of the statutes. The central banks of Kenya, Tanzania, Uganda, Zambia, Guyana, and also Trinidad-Tobago with the approval of the finance minister, may all prescribe ceilings—either general or selective—on the amount of loans and advances that commercial banks may grant during any period. These same banks, except that of Zambia, may issue instructions specifying the purposes and conditions under which loans, advances, or investments may be made. In Zambia and Rhodesia, it may be required that a specified percentage of any increase in total advances and bills discounted be deposited with the central bank.

Trinidad-Tobago, as well as Zambia with ministerial consent, has statutory provisions whereby the central bank may set a minimum ratio of commercial banks' local assets to their local liabilities, to go into effect six months from official notice. Any variation in this ratio shall not exceed 10 per cent (Trinidad-Tobago) or 5 per cent (Zambia), during a given six-month period. Thus, these two countries could gradually require that foreign banks operating in their territories increase their proportionate holdings of domestic assets.

INTERNATIONAL RESERVES

All the countries hold international reserves as a means of maintaining the exchange value of their monetary units. Thus, the statutes for their new central banks require that a certain part of the banks' assets be held in some internationally acceptable form to constitute these reserves. Gold is listed for this purpose by all the central bank acts and, except in Brazil and Guyana, foreign currencies that are freely convertible into gold are also specifically included. Brazil and Guyana include all types of foreign exchange, convertible or not, as part of their international reserves. Again with the exception of Brazil, holdings of foreign Treasury bills and of securities denominated in convertible currencies qualify as external reserves.[7] A number of the central bank statutes allow inclusion of foreign bills of exchange. Other assets that may qualify are securities of international financial institutions (Trinidad-Tobago, Guyana, Tanzania, and Kenya) and automatic drawing rights at the International Monetary Fund (Guyana and Trinidad-Tobago).

Uganda, Jordan, Sierra Leone, and Malawi set specific limits on the maturities and amounts of the foreign instruments that may be held for international reserve purposes. In general, three-month bills of exchange, six-month Treasury bills, and medium-term securities meet the requirements.

All the countries except Brazil state the level below which these international reserves may not fall, but the level is expressed in varying ways. Most of the countries express it as a percentage of central bank demand liabilities: in Jordan, 100 per cent; in Trinidad-Tobago, Guyana, Sierra Leone, and Malawi, 50 per cent; in Uganda, 40 per cent; and in Rhodesia, 25 per cent. In Zambia the requirement is 50 per cent of total liabilities held in June 1965, when the Bank of Rhodesia and Nyasaland was dissolved, and 25 per cent of all increases in liabilities since that time. Kenya and Tanzania, the two other countries that have central bank reserve requirements, relate the level to balance-of-payments needs: their international reserves may not fall below the value of four months' imports as recorded and averaged for the three preceding years.

Special provision is made in Rhodesia and Zambia for the temporary suspension of these reserve requirements. In those countries, the finance minister may waive the statutory conditions for as long as six months, and even longer if legislative approval is given.

CONCLUSION

In general, the new central banks have been asked to help create an atmosphere conducive to economic development in their respective countries, while at the same time maintaining monetary stability. The majority of these countries lack fully developed financial institutions that could effectively channel available savings into productive investment, and hence the central banks' basic objectives include the responsibility of encouraging the development of such institutions. In fact, rather than being involved primarily with the implementation of monetary policy in the more narrow sense, many of the recently established central banks have come to concern themselves also with the broader goals of economic policy. In particular, some of the new central banks have been conceived as organs for financing—or arranging the finance for—long-term basic economic development, as well as for building up a tightly knit and comprehensive system of banks and related financial institutions. In addition, the new banks should aim to manage foreign financial and monetary relations in such a fashion that the inflow of foreign capital is encouraged and balance-of-payments crises are avoided.

[7] The statutes of Tanzania and Guyana do not specifically require that the securities be issued in convertible currencies.