A History of Central Banking in Great Britain and the United States

Central banks in Great Britain and the United States arose early in the financial revolution. The Bank of England was created in 1694, whereas the first banks of the United States appeared during 1791–1811 and 1816–36 and were followed by the Independent Treasury, formed from 1846 to 1914. These institutions, together with the Suffolk Bank and the New York Clearing House, exercised important central banking functions before the creation of the Federal Reserve System in 1913. Significant monetary changes in the lives of these British and American institutions are examined within a framework that deals with the knowledge and behavior of central bankers and their interactions with economists and politicians. Central bankers' behavior has shown considerable continuity in the influence of incentives and their interest in the stability of the financial markets. For example, the Federal Reserve's behavior during the Great Depression and the periods of low inflation of the 1990s and its resurgence the next decade follow from its structure and from government pressures rather than from accidents of personnel.

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To Norma, as always

Whoever, then, possessed the power of regulating the quantity of money could always govern its value. But the currency . . . was left entirely under the management and control of a company of merchants – individuals, he was most ready to admit, of the best character, and actuated by the best intentions; but who, nevertheless, . . . did not acknowledge the true principles of the currency, and who, in fact, in his opinion, did not know anything about it.

David Ricardo, House of Commons, June 12, 1822

[N]o semblance of acquisitiveness prompts [the Federal Reserve Board's] operations; no banking interest is behind, and no financial interest can pervert or control it. It is an altruistic institution, a part of the Government itself, representing the American people, with powers such as no man would dare misuse.

Carter Glass, House of Representatives, September 10, 1913

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Preface

I have been involved in monetary policy only remotely in groups briefing Federal Reserve Bank presidents for Federal Open Market Committee meetings, but I have had numerous opportunities to observe policymakers and their close advisors: as a graduate student at the Federal Reserve Bank of Chicago, an economist at the Federal Reserve Board, and visitor at the Federal Reserve Banks of Philadelphia, Dallas, and Chicago. It has always been clear to me – at first very disapprovingly, then less so – that central bankers do not see the world like economists. Examinations of the statements and actions of earlier central bankers in Great Britain as well as the United States convinced me that this has always been so.

I do not touch on the questions of whether central banks have been more harmful than beneficial or whether they ought to exist, but rather on understanding them. I hope the study will come across as a sympathetic inquiry by an economist into the knowledge and behavior of central bankers – into what makes them tick. I give them no grades, but I hope that a better understanding of the continuity of their behavior, while at the same time recognizing that they are not immune to ideas, may promote a more useful interaction between them and economists.

Much of the research and writing of this book took place at Clare Hall, Cambridge, with its access to the University and Marshall Libraries, and at the American Institute for Economic Research, Great Barrington, Massachusetts. I am grateful to these institutions and to the above-the-call-of-duty editorial guidance and advice of Michael Bordo, Robert Hetzel, and Anna Schwartz. Most of my other debts are revealed in the citations to the many excellent studies of central banking of which I am one of the fortunate inheritors.