Dear readers,

I hope you are well and found the previous issue of Chimera's Bane *interesting. This one presents a brief argument (yet to be extended and more fully articulated) about what central bank independence is and where it came from. By explaining why I see central bank independence as a rhetorical device and what purpose this device has served for the economic orthodoxy, I am trying to develop a more complete understanding of central bank independence from a heterodox point of view. Do let me know what you think. I count on my readers to help me improve and your feedback is always welcome!*

Sincerely,

Daniyal Khan

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A RHETORICAL DEVICE

The economic orthodoxy of the late twentieth century constructed and used central bank independence as a rhetorical device, even a sleight of hand, to reconcile two otherwise irreconcilable propositions. The first proposition is that the economy should remain apolitical and should not be actively managed by the government except perhaps on the margins. The second proposition is that the price mechanism is a central and essential allocative mechanism of a market economy and should be actively managed by a public entity. These propositions were otherwise irreconcilable and created a political problem that needed to be addressed: how to manage prices (and interest rates) as a productive and distributional economic force without exposing economists to legitimate allegations of being political and pro-economic management. As long as economists held onto their commitment to a free market, an institution as powerful as a central bank could not be allowed to manage the price level. So what could be done? The problem was addressed using the doctrine of central bank independence as a rhetorical construction. As long as a central bank could be legitimately said to be independent of politics and the government, it allowed economic orthodoxy to have a public economic institution legitimately manage the price mechanism while also maintaining the illusion of an apolitical economy and an apolitical economics.

The problem emerged from the unravelling of the Keynesian revolution, the end of Keynesian managed capitalism and the return of the first proposition which had been suppressed during the years of the postwar "golden age" of capitalism. To be more precise,

the problem *re-emerged* with the end of Keynesian management of capitalism. The tension between the two propositions is a long-standing issue in capitalist history. For example, you see this tension expressed in the argument over rules versus discretion in the bullionist debates and in the debate between the Currency School and the Banking School in the 19th century. This tension needed to be managed once again after decades of being submerged under the weight of the series of problems and crises which emerged after the end of Pax Britannica in 1914 and the alchemical transformation of these problems into Pax Americana at the end of the second World War. The ruins of Pax Britannica were beaten into gold by the force of American hegemony. The tension resurfaced at the beginning of the end of Pax Americana as the global gold peg was abandoned by the United States and the system started to come under the repeated pressures of what Wolfgang Streeck has called the crises of democratic capitalism. Thus, this tension may even be seen as one aspect of the tension between democratic legitimacy and the capitalist pursuit of profit.

The argument is more persuasive if we are open to seeing economics as ideology (as in Heilbroner) and as rhetoric (as in McCloskey). As economics is an exercise in storytelling about economic enterprise, so it is also an exercise in persuasion. Central bank independence as an economic theory has been used to actively persuade people that while public management of prices is something that interferes with efficient functioning of the economic system, it is just fine as long as it is done by an institution which is made independent from the government and from politics. The illusion or sleight of hand is in persuading the public that central banks can be and are independent. Central bank independence remains as much of a myth as free markets. Neither has ever truly existed. Central banks are, as Eric Monnet says in *Balance of Power*, pillars of the welfare state. But the history of the rise of central bank independence in the neoliberal period is troubling: this pillar of the welfare state has been defanged and retooled, with the doctrine of central bank independence giving cover to the central bank's pro-capitalist management of the price mechanism.

My argument is also grounded in a fundamentally political view of the economy and of the price mechanism as a productive and distributive mechanism. In fact, I contend that evading the political character of the economy and hence of economic policy in general (though in this case what is of interest is price stability through monetary policy) while also taking politically consequential decisions and committing to politically meaningful and consequential lines of action remains a significant preoccupation in economics as a discipline and as a profession. Hence the emergence of the doctrine of central bank independence as a rhetorical device in the late 20th century takes place in the context of this professional preoccupation.

The rhetorical structure of central bank independence was founded on three different sub-devices or sub-constructs. First, the development of central bank independence indices

and the application of econometric techniques to a political issue played a key part in supporting central bank independence, as it did with other propositions. Second, mistrust in governments and states was actively cultivated by right-wing figures like Thatcher and Raegan at the start of a new global era marked by the fall of the Berlin Wall, the fall of the USSR, and the seeming victory of capitalism and the "end of history." This of course led to New Labour in the UK, which pushed the Labour Party onto a path at the end of which the party is pretty much indistinguishable from the Conservatives, who are themselves at risk of being completely replaced by Reform UK. It also led to the deregulation of the 1990s under Clinton in the United States, leading to the Great Financial Crisis. Thus this was an era in which even heterodox economists like Heilbroner asked whether socialism was possible. Finally, the social costs of the Volcker shock being blamed on a lack of central bank credibility, as in Manuela Moschella's account of the infamous monetary policy episode in *Unexpected Revolutionaries* (p. 42), can be thought of as the *primitive persuasion* which helped establish central bank independence as the key rhetorical and doctrinal touchstone of monetary thinking since the end of capitalism's so-called golden age.

In the past half century, the rhetorical, doctrinal and political character of central banks and generally of capitalist institutions (which is what central banks are) was hidden behind this three-part wall of central bank independence. But central bank independence itself has only been one part of the fortress of the rules-based order which has loomed large over the global political economy since World War II. A fuller understanding of the historical development and use of central bank independence as a rhetorical device requires understanding its role in maintaining the postwar order.