

4.5 The Panel Sessions

The conference began with a panel session, **Pioneering Central bankers Remember** in which two former central bank governors, on whose watch the Great inflation was vanquished reflected on their experiences. **Donald Brash**, Governor of the Reserve Bank of New Zealand from 1988 to 2002, the first country to adopt inflation targeting, described the experience of New Zealand in the Great Inflation era and the events that led to formal inflation targeting. New Zealand had the worst inflation experience from 1970 to 1984 in the OECD. A series of policy moves were attempted with limited success in reducing inflation including draconic wage price controls in 1982. A major sea change in the economic policy framework occurred in 1984 with the election of the Labour party which deregulated much of the economy including the financial sector, reduced tariffs and tax rates, floated the exchange rate and gave the central bank independence with a mandate to reduce inflation. Inflation declined from double digits to well below 10% by the late 1980s.

In 1989 the Government introduced radical legislation which gave the central bank de jure independence and a clear mandate to produce price stability(defined as an inflation rate of two per cent or less) as its sole target. The Governor of the RBNZ was made accountable to the government in achieving its inflation objective. By 1991 inflation was below 2%.

John Crow, Governor of the Bank of Canada from 1987 to 1994, describes the background of inflation in Canada and the events that led to the adoption of formal inflation targeting in 1991. Canada was the second country to follow such a path. Canada's inflation experience in the 1970s and 1980s clearly followed that of the U.S. As in the U.S. monetary(M1) aggregate targeting was followed in the 1970s in an attempt to gradually reduce the inflation rate. As in the U.S. financial innovation weakened the connection between M1 growth and inflation and the Bank abandoned the strategy in 1982. The Bank then followed an implicit exchange rate target which implied a close shadowing of U.S. monetary developments. By 1987, inflation was down to 4%.

Upon becoming Governor, John Crow was convinced of the need for the Bank to attach the highest priority to maintaining price stability(which he originally defined as zero per cent inflation) and he forcefully presented his views in a series of speeches,. In 1991 the Government of Canada took the initiative in having the Bank of Canada adopt an inflation target. The Bank was made the agent responsible for hitting the inflation target and for the design of the targets, with the Department of Finance's approval. The target was set at 2 per cent in 1993. As in New Zealand inflation quickly dropped below 2 per cent.

The conference ended with Panel Session II **Lessons from History** involving Federal Reserve Vice Chairman, **Donald Kohn** and **Harold James** of Princeton University. Kohn emphasized the lessons that central banks need to learn after experiences like the Great Inflation. The first lesson is that central banks need to focus on price stability as its most important long-run objective. The second lesson is the importance of inflationary expectations for the control of inflation. The third lesson is the importance of

vigorous debate inside central banks as well as the input by outside experts to safeguard against serious policy errors. The fourth lesson is that once inflation becomes embedded in inflationary expectations that monetary policy should be vigorous and unswerving in eradicating it. His final lesson is for central banks to be humble about what they know.

Harold James discussed the nonmonetary aspects of great inflations in the past—of inflation as a way to buy social peace in a politically precarious environment. Viewing inflation as a monetary phenomenon was key to its resolution both in Germany in the 1920s and in the Great Inflation of the 1970s. The development of inflation targeting is the culmination of this process. James warns of the difficulties of measuring inflation, especially of the role of asset price booms.