John H. Wood, *A History of Central Banking in Great Britain and the United States* (Cambridge and New York: Cambridge University Press, 2005) pp. 439, xv, $90, ISBN 0-521-85013-4

With *A History of Central Banking in Great Britain and the United States*, John Wood has set himself an ambitious objective. While several authors have written on central banking, most of them have focused on one country or on a specific time period. Wood, on the contrary, offers a history of central banking in the United Kingdom and the United States, from their origins to the present day. Wood clearly states his objective: "this is the first attempt to tie the threads across three centuries within a unified framework that is made up not only of monetary theory but of the situations of central bankers in the financial markets" (pp. 1–2).

Wood did not go into new archival research. His book is based on the existing literature and he quotes abundantly from it (also, at moments very extensively, from autobiographies, which leaves me somewhat uneasy). He offers very much a history of economic thought perspective, focusing on the ideas on central banking, not only of "theorists," but also of the central bankers themselves. Sometimes I have the impression that the title as "A History of Economic Thought on Central Banking in Great Britain and the United States" would have been more appropriate.

Wood starts his book with an introduction, "Understanding central bankers and monetary policy." Thereafter follow four chapters on the United Kingdom, covering the period from the creation of the Bank of England to the outbreak of World War I. The next four chapters cover central banking in the United States from 1790 to the 1960s, followed by a chapter on the Bank of England from 1914 to the 1960s. The last three chapters discuss the most recent period, covering both Great-Britain and the United States. The last pages of the book offer some concluding thoughts.

Wood traces the evolution of central banking. In the eighteenth century, the Bank of England focused on profits and convertibility, the latter requiring the payment of gold on demand for its notes. The nineteenth century saw the progress of the Bank's acceptance of a wider responsibility for financial stability, although convertibility remained crucial. The United States had no institution that could be called a central bank—except two short-lived Banks of the United States between 1791 and 1836—before the establishment of the Federal Reserve in 1913. Nevertheless, the federal Treasury Department, central money markets, and clearinghouses performed central banking functions that were governed by the same ideas that prevailed across the Atlantic, that is, profits for private institutions and seigniorage for the government, subject to currency convertibility and with attention to financial stability.

Central bankers failed to cope with the disruptions of World War I and the Great Depression of the 1930s and tended to make matters worse as the old system collapsed. Monetary theory and practice since that time have, to a large extent, been quests for an adequate replacement of the pre-1914 system. The dollar-exchange system that was agreed to at Bretton Woods in 1944 proved inconsistent with national economic policies, and its breakdown in the early 1970s presaged an agonizing period of accelerating inflation and unemployment. The anti-inflationary monetarist policies associated with Federal Reserve Chairman Paul Volcker and Prime Minister Margaret Thatcher may be understood as reactions to inflations that had failed to bring the

https://doi.org/10.1017/S1053837200009652 Published online by Cambridge University Press

promised benefits. Monetary debates since 1979 have led to a consensus on price stability as the objective of monetary policy.

One of the key messages of Wood is that "central bankers do not see the world like economists" (p. xv). Wood stresses that central bankers are, and think very much, as bankers. They are very much concerned about the "stability" of the financial markets. More academic economists have been "critical of central bankers' attention to the financial markets at the expense of their macroeconomic responsibilities" (p. 4). Famous is David Ricardo's speech, when he criticized the Bank of England:

> 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 (Speech in the House of Commons, June 12, 1822. Wood uses this as his opening quotation of the book, p. viii).

Wood naturally acknowledges that central bankers' understanding of their role in monetary policy has grown (for example, p. 4). However, he argues that these tensions continued: "We will encounter more instances of this difference in viewpoint, but jumping ahead to 1998, we see that the conflict between the career central bankers and economists on the Bank's Monetary Policy Committee (MPC) was similar to that between the Bank and the economists on the 1810 Bullion Committee" (p. 4). Now, I have to admit that, in my opinion, Wood is doing some overkill here. The Bullionist controversy was naturally much more fundamental, with Ricardo reproaching the Bank of England for not understanding the functioning of the monetary system. While I certainly agree that central bankers pay attention to stability in the financial markets (and that is a reason why a clear communication policy is important), other factors, like the assessment of the economic situation and more "Keynesian" or "Monetarist" orientations of policymakers or academic economists, are also important.

So, Wood emphasizes the importance central bankers attach to financial stability. He very much defines this as "smoothing the financial markets." However, he considers, at least, three kinds of smoothing: (1) central bankers who keep interest rates stable, not understanding the macroeconomic impact, cf. the David Ricardo quotation. (2) Interest rate smoothing, gradual movements of interest rates as big changes might upset financial markets, something which economists have "found it difficult to rationalize," (p. 5). And (3) being a lender of last resort in crisis situations, "such as when the Federal Reserve supplied liquidity after the 1987 stock market crash, during the run-up to the millennium, and after 9/11" (p. 7). These are clearly quite different concepts of "smoothing the financial markets." However, Wood does not elaborate very much on the concept of financial stability and does not explore the implications of it.

Given Wood's emphasis on the attention of central banks to financial stability, I'm rather surprised that he gives almost no attention to the role of the Federal Reserve and the Bank of England in the prudential supervision of financial institutions. For instance, as far as I could see, the transfer of responsibility for financial supervision from the Bank of England to the Financial Services Authority, a very fundamental change for the Bank of England, is not even mentioned. Related to this, there is almost no attention in this book to the organization of the payments systems, a core function of a central bank and closely connected with financial stability. Also, the

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organization of the Fed and the Bank of England (for example, number and role of the branches and their evolution in time, number of staff) is not much discussed. Nevertheless, these are certainly important aspects of central banking (cf., Buyst, Maes and Pluym 2005).

Sometimes, I would have liked Wood to be more didactic. For instance, he quickly makes comparisons between ideas in the past-and-present day theories. For instance, he presents Mill's distinction of a temporary or permanent inflation. He continues, "Mill's point is relevant to recent discussions that assume because central bankers do not recognize these distinctions they must commit either to an interest or money rule (p. 83). In a footnote, he refers to William Poole's 1970 article on the choice of monetary policy instruments in a simple stochastic model without much further explanation. At moments he is also a little bit sloppy. On page 96, for example, Wood discusses the balance sheet of the Bank of England, but using different descriptions than the ones used in the balance sheet itself, so that the reader has to make some calculations to see which are the exact posts of the balance sheet he discusses.

Writing a comparative history of central banking in Great Britain and the United States was certainly a broad and ambitious project. However, I cannot say that I was really charmed by this volume.

Ivo Maes
National Bank of Belgium

REFERENCE

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https://doi.org/10.1017/S1053837200009652 Published online by Cambridge University Press