

Faculti Summary

<https://staging.faculti.net/the-political-economy-of-reforms-in-central-bank-design/>

The paper discusses the significant reforms in central banking over the past 50 years, focusing on the relationship between central bank independence (CBI) and macroeconomic variables. The author notes existing literature suggests a negative relationship between CBI and inflation, particularly in advanced economies. However, previous studies often overlooked CBI as an endogenous variable, failing to address the contextual factors driving reforms in central bank institutional design.

The author's research, which involves a dataset covering 154 countries from 1972 to 2017, aims to identify the drivers of these reforms by incorporating a comprehensive analysis of central bank legislations. The methodology includes creating an index of CBI that reflects contemporary developments and characteristics not considered in older indices.

The findings reveal that countries experiencing lower levels of independence are more likely to reform. External pressures, such as IMF programs and convergence requirements for joining monetary unions, significantly influence the likelihood of reform. Interestingly, the study identifies peer effects, where countries lagging behind in CBI are driven to catch up with their peers.

The implications of the research highlight the importance of considering the endogeneity of CBI when analyzing its effects, suggesting that reforms are contingent upon political and economic contexts. The results contribute to the understanding of the political economy of reforms by emphasizing that institutional changes evolve based on dynamic conditions rather than being fixed or exogenous.