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*Commemoration of Guido Carli
on the tenth anniversary of his death*

Guido Carli
Governor of the Bank of Italy

Address by Antonio Fazio

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Guido Carli was one of the protagonists of Italian history in the second half of the last century.

His work was always inspired by a comprehensive view of the general interest, by the goal of modernizing Italy's economy, institutions and legal system and by his knowledge of the international framework. In principle, he did not oppose correct forms of public intervention but saw the State as a regulator. He advocated greater competition in the banking system as well as other sectors, but put stability first.

He was a servant of the State, as Governor of the Bank of Italy but also in the many positions he held before and after his Governorship, as an Executive Director of the International Monetary Fund, Head of the European Payments Union, Chairman of Mediocredito Centrale, Minister for Foreign Trade, Chairman of Confindustria, Senator and Minister of the Treasury.

Piero Barucci has given an extensive account of Carli's career and above all of his thinking. I shall recall some aspects of the contribution he made as Governor of the Bank of Italy to the country's economic, political and social development. As Paolo Baffi put it, during the time he held that position "he won the highest regard as he wholeheartedly dedicated his remarkable energies to solving the increasingly grave problems that political and economic developments posed for the monetary authorities." He contributed powerfully to Italy's financial credibility by strengthening "the international community's willingness to support the efforts Italy has made and must continue to make in order to overcome its difficulties".

On another occasion that we are planning, we shall recall Carli's work as an economist in the monetary and financial fields.

Monetary management is a complex art; it demands a good knowledge of economics, experience and the prudent assessment of every decision. Guido Carli possessed this rare combination of gifts. His decision-making ability was extraordinary; he would arrive at a decision after meeting with his collaborators to analyze the causes of the problem and the possible consequences of the alternatives.

The first econometric model of the Italian economy was completed in 1964. It was constructed primarily in response to Carli's calls for data on the performance of the main economic variables and how they related to monetary policy.

He was satisfied with the results and used the model on several occasions to explain the Bank of Italy's policy.

The model is Keynesian in structure. It is updated regularly by the Bank's Economic Research Department and is used to prepare forecasts and to simulate the effects of monetary and fiscal policy measures. The structure has been adjusted to take account of the new institutional order in which policy is implemented by the European System of Central Banks.

Carli took the helm of the Bank of Italy at a difficult time. In 1947 Einaudi and Menichella had tamed the postwar inflation, stabilized the lira and laid the foundations for the "economic miracle". In the 1950s the expansion of the economy and the introduction of more advanced forms of production organization brought considerable gains in productivity in industry and growth in employment.

The growth continued in the 1960s.

In 1959 the lira had won the "currency Oscar". In the early 1960s Carli began to fear that the path of firms' advance was narrowing as a consequence of the expansion of the system of state holdings and the demands for wage increases in excess of the rise in productivity. He called the nationalization of the electricity industry "the first example of the intention of the political class to occupy the economy".

After a long period of cost and price stability, which had brought Italy gains in competitiveness, stimulated growth and spread welfare more widely, new political equilibria fostered a major redistribution of income in favour of payroll employment; there was the risk that profits would come under pressure and investment be reduced.

In the summer of 1963 Carli imposed a credit squeeze in order to limit domestic demand and curb inflation. He did not react to the fierce criticisms of leading political figures; this was his constant policy. Since then the Bank has always responded with the facts and detailed accounts of the reasons for and effects of its actions.

The balance of payments came rapidly back into balance. Carli warned, however, that a restrictive monetary policy was not sufficient, that it was necessary to adapt the structure of supply to the changed composition of demand and achieve gains in competitiveness once more. The discretion attributed to the central bank in its action was based on the assumption that its objective could not be limited to monetary stability; beyond the short term the stability and growth of the economy also had to be ensured.

It was in this period that monetary policy's putative role as stand-in for the other forms of economic policy and its possible economic and institutional effects began to be debated.

In 1969 large increases in prices on international markets led to the adoption of restrictive policies in many countries. In Italy the surge in the budget deficit caused the external accounts to deteriorate. The "hot autumn" of labour conflict caused a fall in industrial production and led to wage rises again outpacing productivity.

In August 1971 the convertibility of the dollar into gold was suspended. The monetary regime created at Bretton Woods was in crisis. In Italy, following the stabilization of 1947, first Menichella and then Carli had ensured an exchange rate of 625 lire against the dollar. Thanks in part to its large balance-of-payments surpluses, Italy had acquired the status of a strong-currency country. Inflation in the 1950s and 1960s was very low by international standards, lower than in Germany.

Carli immediately recognized the importance of the break with the past, giving proof of a lucidity that surprised us youngsters, accustomed to the fixed exchange rate system, and accepted floating rates. I remember the theoretical seminars with the active participation of the members of the Directorate in which Fausto Vicarelli explained the new models for the pursuit of internal and external equilibrium, through public demand and the floating of the exchange rate.

At the end of 1973 the fourfold jump in oil prices intensified the inflationary pressures and threatened the country's financial stability. At the beginning of 1974 inflation exceeded

20 per cent on an annual basis owing to the oil crisis and the enormous balance-of-payments deficit. Carli did not hesitate to impose a tight credit squeeze.

In the absence of an appropriate economic policy strategy, the task of reining in demand fell to the central bank. Recourse was made to supervisory rules and instruments to pursue monetary policy goals.

The dosage of the supply of credit by means of administrative measures, already suggested by Baffi in the second half of 1973 and designed to avoid the rationing of credit to small and medium-sized enterprises, was applied to all bank lending.

Stabilization was achieved in the context of an agreement with the International Monetary Fund concluded on conditions that were the result of extremely tough negotiations. In a letter of intent Italy undertook to meet an intermediate objective defined in terms of total domestic credit. The conditions laid down by the International Monetary Fund, revised in the light of estimates obtained with the econometric model, brought down the government of the day and were only accepted by a new one that was politically committed to the credit restrictions imposed by the Bank of Italy.

The intervention had the desired effect of curbing demand; the deterioration in the balance of payments and the depreciation of the lira were halted. The inflation rate was halved, from more than 20 per cent on an annual basis to around 10 per cent. The stringency of the 1974 credit tightening was second only to that of the squeeze imposed in 1947; the economy and the financial system had risked a crisis that I have no hesitation in defining as potentially disastrous.

During the annual meeting of the International Monetary Fund in October 1974 Carli put forward a proposal for recycling the petrodollars that exceeded the development needs of the Arab OPEC countries — “a sort of Marshall plan on a world scale”, as he called it. In this and other proposals concerning international relations it is possible to discern an “*ante litteram*” vision of the phenomena present in financial globalization.

Faced with the crisis described above, he had deemed that a refusal to finance the State would have been a “seditious act”, even though such funding might distort the market and prolong inflation. This decision should not be interpreted as acquiescence in inflationary policies but as the thinking of a conscientious public servant who, holding one of the key

positions in the institutional order, recognized the ultimate authority of Parliament's sovereign will.

There was concern for a political and institutional setting that lacked stability. Partly owing to those reflections and in a different institutional context, we now have precise statutory rules deriving from the Constitution and Community law.

That it was not a question of surrender can be seen from Guido Carli's influence, strengthened by the international acclaim he enjoyed, on the action of the Government, which, engrossed by the difficulties on the political and labour relations fronts, sometimes risked losing sight of the objective of monetary stability.

In 1975 Carli was succeeded by Paolo Baffi at the start of what Baffi was later to call "five years under fire". The economy deteriorated against a background of social and political strains marked by the outbreak of terrorist violence.

The Bank that Carli left had increased its authority in the country and abroad. It had coped skillfully with serious crises that were overcome through the use of monetary policy. In a delicate period of transition in political and institutional relations, it had consolidated its independence and built up the range of instruments at its disposal; it had constantly drawn attention to the ills of the real economy and the public finances.

The vision that guided Carli was liberal, not laissez-faire, and attentive to solidarity and social cohesion, without this being confused with visions that justified waste or parasitism. At times he was pessimistic, as when the electricity industry was nationalized. He never failed, however, to serve the State loyally, as when he committed the Bank and its branches to a demanding analysis of the issues related to the planning process which the Government of the day intended to introduce and which contrasted sharply with his own ideas.

Carli had entered the Bank as Director General at just 45, and immediately felt himself part of the institution.

In accordance with his view of the Bank of Italy as an economic authority, embodied in Italy's de facto constitution, Carli strengthened banking supervision, started a process designed to make the regulation of the monetary base less dependent on the Treasury's financing needs, and tenaciously and sagaciously fostered economic and institutional research.

The times were changing. It was necessary to create, under the existing laws, a new framework for the powers and functioning of the supervisory authority, to clarify its aims and to define its relations with both the ordinary and the administrative judicial authorities.

A substantial increase in the number of inspectors was gradually implemented, starting from 60 in 1968. Today, there are 160 working out of the Head Office and the same number again working out of branches. Drawing also on experience in other countries, the methods and instruments for carrying out inspections were revised, binding rules concerning the transparency and disclosure of banks' annual accounts were laid down, including the requirement to disclose hidden reserves, a farsighted choice that also contributed to banks not being involved in the numerous episodes of corruption that came to light in the 1990s.

Decades later, banking supervision has taken on far greater importance than in Carli's times. But the seed sown then has borne abundant fruit. For Carli, intellectual consistency and rigour, together with a clear recognition of the aims, were the prerequisites for earning merit. They are principles which are not undermined by the sporadic virulence of vested interests seeking to appear as the general interest.

The Bank of Italy owes its transformation into a modern central bank to Guido Carli.

Donato Menichella believed in "*fuge rumores*"; he was diffident of any relationship with the press and claimed with dry humour that there was no basis for such relations since one could not recount the truth yet had the moral duty not to tell lies.

However, as Baffi had occasion to remark, "the actions of central banks have left the realm of silence, perhaps never to return; if in the past silence was seen as a guarantee of independence, today independence is achieved by giving explicit account of one's action in ways and at times that do not prejudice its effectiveness".

The innovations in monetary policy, the enhancement of banking supervision and research were also possible because Carli, at the very beginning of his Governorship, launched a major drive to renew and strengthen the Bank's staff and internal organization. Special attention was paid to personnel management, to allow the Bank to attract the best of the new generations and carefully instruct them in its working practices.

He gave greater responsibility to younger members of the staff and involved them directly in the decision-making process.

The Central Credit Register was created in 1962 and the School of Automation for Bank Executives was set up in Perugia in 1968. The Interbank Convention on Automation was established, the department responsible for foreign relations was completely reorganized, forms of "participation" were introduced into relations with the trade unions. Lastly, Via Nazionale-Via Tuscolana was chosen as the axis of expansion of the Bank's main premises.

Carli was a precursor of the direction in which the role of central banks would evolve, especially in Europe. As Treasury Minister of the Government headed by Giulio Andreotti, he signed the Maastricht Treaty.

But these values, today reinforced in the European context, had already become, thanks in significant measure to Guido Carli, a central element in our laws and in the Bank's institutional and organizational tradition.

In 1976 Carli succeeded Giovanni Agnelli as Chairman of Confindustria; in taking on this task, he gave further proof that he was a "practical intellectual". Following his election to the Senate, in 1989 he was appointed Minister of the Treasury. In this new role he explicitly adopted the policy of turning the proposals of the Bank of Italy into Treasury decisions. He completed, in formal terms, the project to make the Bank entirely independent by promoting the law that transferred the power to fix the official discount rate to the Governor.

Italy has made important progress since the years of Carli's Governorship.

The terms of the relationship between banks and firms are no longer the same as those of Carli's proposal to transform bank loans into equity holdings. In several periods after that proposal major restructurings took place in industry and more recently, since the mid-1990s, the banking system has been restored to a sound footing and consolidated.

The question of structural reforms, which can no longer be put off, can also be seen as a development of the analyses and lucid diagnosis of the fragility and limits of the Italian economy that Carli put forward in the 1970s. Innovation, competitiveness, productivity and the role of our productive system in the world economy are issues repeatedly addressed in all the Bank's Annual Reports.

Today it is essential to revive the growth of the economy: strategies and policies in this age of globalization are more complex than they used to be. Carli's writings and work can still help us.

There are moments when we miss Carli, his thinking, his ability to devise projects at a time when we are faced with the need to re-establish equilibria, behaviour and rules among states, so as to foster distension and peaceful cohabitation at the international level. A time when Europe should play a very different role.

We are grateful to Guido Carli for what he did, for what he left us. We are proud of the work he did, of the contribution he made to the international community and to Italy.