"Monetary Policy Lessons from the Global Crisis"
International Journal of Central Banking Conference
hosted by the Bank of Japan

Welcome and Opening Remarks

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(Welcome)

Good morning. On behalf of the Bank of Japan, I am delighted to welcome you to our conference, which is organized jointly with the International Journal of Central Banking.

The International Journal of Central Banking, or IJCB, was established in July 2004 at the initiative of BIS, G10 central banks, and ECB. Chairman Ben Bernanke, at that time Governor, was the first managing editor. John Taylor of Stanford University succeeded to the position in September 2005. Frank Smets of ECB has served as managing editor since January 2008. By coincidence, both John and Frank happen to be frequent visitors to the Bank of Japan, and John is a former honorary adviser of our Institute for Monetary and Economic Studies at the Bank of Japan. I am grateful for their immense contributions both to the IJCB and to the Bank of Japan, and I am delighted to welcome them to this conference.

The IJCB serves as a forum for discussing central bank theory and practice. It seeks to disseminate applied and policy-relevant research on central banking issues and promote communication among researchers inside and outside central banks.

Starting last year, the IJCB continued to work toward its goals by hosting biannual conferences. Spring conferences focus on issues related to financial stability. Fall conferences, including this one, seek to draw monetary policy implications from a primarily macroeconomic perspective. This conference marks the fourth from last year.

(Classical Question Regarding Competition and Regulation)

The title of this conference is “Monetary Policy Lessons from the Global Crisis.” This is a difficult but extremely important topic. Today and tomorrow, during the two days of the conference, I expect to learn much from the stimulating discussions.

I will ask you for a few minutes to set forth what I believe is a fundamental question bearing on the topic of the lesson of the Global financial crisis. To digress a little bit, this relates to the classic question of competition vs. regulation, which has gathered renewed attention since the recent crisis.

On one side, measures to strengthen competition have been called for over the past two decades. Competition harnesses market mechanisms, which helps find optimal market prices, leading to efficient resource allocation. The resulting policies have promoted competition, global competition in particular. Trade barriers and capital controls have been leveled or weakened. China and other emerging economies entered the global market following the fall of the Berlin Wall. In the financial markets and the financial system, money flows globally this way and that way, searching for the yield or liquidity.

Similarly, macroeconomists have moved in the same direction, assuming that markets in general function effectively. They have developed analytical frameworks, incorporating agents’ expectations and inter-temporal decisions. It resolves the Lucas critique and helps draw many useful implications for monetary policy including the Taylor rule, time-inconsistency, and history dependence.

However, since the crisis, market failures and externalities have been often emphasized as factors contributing to the crisis. To prevent the potential for future crises, stronger financial regulations are now under discussion.

Interestingly enough, the issue of trade-offs between competition and regulation has not been isolated to economics. Other fields of research have also somewhat tracked the shift from regulation to competition over the last two decades and, in the wake of the recent financial crisis, the countertrend from competition to regulation.

At the Institute for Monetary and Economic Studies, which I currently head, our staff pursues research on central banking from a wide range of areas, including economics, financial engineering, law, accounting, information technology, history, and so forth. Such wide coverage is perhaps unique to our Institute among the research institutes at the various central banks.

I have noted similar movements in other fields. In the field of law, we have seen a series of reforms in corporate and financial laws over the past two decades. In accounting, market value accounting has been granted precedence over book value accounting. In general, those reforms have sought to apply market mechanisms and promote competition.

Now following the recent financial crisis, those fields are swinging back from competition to regulation. One study argues that the U.S. bankruptcy reforms of 2005 exacerbated mortgage defaults.[1] In accounting, in light of the destabilizing effects of market value accounting, discussions have tilted toward permitting assessments of certain assets by book value accounting.

Nevertheless, I continue to believe that competition is needed to harness market mechanisms and thereby encourage innovations. Innovations will be a crucial factor driving long-term economic growth.

Regarding regulation, I point to two types: ex ante and ex post regulation. Ex post

[1] Li, W. "Did Bankruptcy Reform Cause Mortgage Default to Rise?" NBER WP 15969, 2010.

regulation focuses on schemes after problems have emerged. For example, it maps orderly bailout schemes for troubled institutions. Japan's orderly liquidation and bankruptcy schemes were finally established in the early 2000s, nearly a decade after the bursting of the bubble. Those schemes played an important backstop role in the recent crisis in reducing uncertainty. I believe that such ex post regulation does better than ex ante regulation to promote competition.

A good framework for analyzing competition vs. regulation will require coordination and integration between economic intuition and intuition based in law, accounting, and other fields. Of course, this is a difficult and perhaps overambitious challenge, but Macroeconomic research on banks' oligopolies would be one promising approach. This is because banks' oligopolies matter for the issue of competition vs. regulation and have useful implications for not just economics but law and accounting.

(Conclusion)

The IJCB also provides an excellent opportunity for identifying clues to the difficult challenges that lie ahead.

Six papers presented in the two-day conference today and tomorrow will recount our recent bitter experience with the global financial crisis. Three renowned economists provide commentary, and five distinguished economists and policymakers exchange their views in a panel session. I am convinced that their deep insights will stimulate discussions and help draw implications for the future of central banking.

Thank you.