

Challenges to the Federal Reserve's Political Independence, 2009-2012

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Fed's Independence Threatened

- The Fed's unconventional policy actions have been controversial in the U.S. Congress
- Congress—the Fed's “principal”—has moved to reign in the Fed's political independence
- I examine the coalitions that stand on either side of this issue
- I find evidence of an *ideological reversal*: the Right is now attacking the Fed's independence while the Left is defending it

World turned upside-down?

- Previous literature (Hibbs 1977, Alesina, Roubini & Cohen 1997) has the Right supporting CBI and the Left opposing it
 - CBI yields low inflation, which benefits the Right's wealthy constituents, while the Left prefers more employment, which benefits the working class
- So, why the reversal?

Argument

- CBI requires a political “support coalition”
- Members of the CBI support coalition vary with the mandate the CB is pursuing: stable prices or full employment
- During the Great Recession, the Fed focused on reviving employment, which made it a natural ally of the Left
- The Right, by contrast, frets about future inflation, but its opposition to the Fed also reflects its anti-globalization position

Congressional Threats to CBI

- Title XI of the Dodd-Frank Act (2009) resulted in:
 - A GAO audit of the Fed’s emergency activities during the crisis
 - A GAO audit of Fed governance
 - disclosure of details on the identities of borrowers and the terms of their loans
- This challenge was pushed by the Right—Ron Paul (R-TX) in particular—and opposed by Bernanke, Geithner, the Obama administration, and many Democrats

Federal Reserve Transparency Act of 2012

aka "Audit the Fed"

- Removes all restrictions on GAO audits:
 - Removes ban on audits of the Fed's transactions with foreign central banks
 - Removes ban on auditing the ***deliberations, decisions, and open market actions on monetary policy matters***
- Pushed by the Right (Ron Paul sponsored it) and opposed by the Fed, Obama, and Democrats
- Bernanke called this bill a "nightmare" for Fed independence

Fate of “Audit the Fed”

- On July 25, 2012, the House passed the Federal Reserve Transparency Act by a vote of 327-98 (77% support)
- All but one Republican voted for it, but *Democrats were split 89-97* (I exploit this)
- The bill stalled in the Senate where Majority Leader Harry Reid (D-NV) said he would prevent it from coming to a vote

Analysis of Democrats' vote choice on “Audit the Fed”

- Legislator characteristics
 - **Ideology** (DW-Nominate), seniority, committee assignment
- Special interests
 - **Campaign contributions** from big banks
- Congressional District characteristics
 - foreclosure rate, social security recipients, bank HQ

First Difference in Dems' Voting

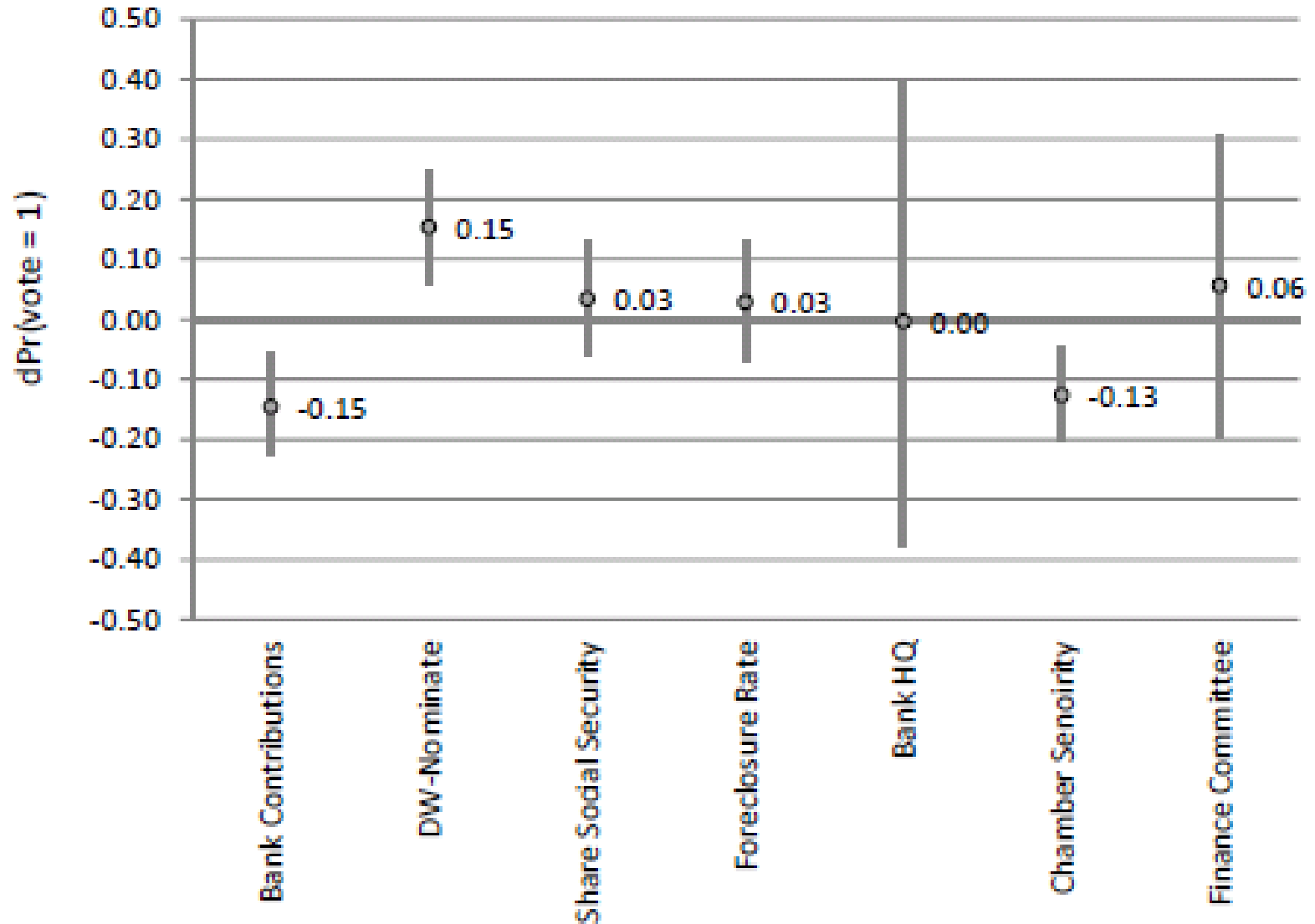
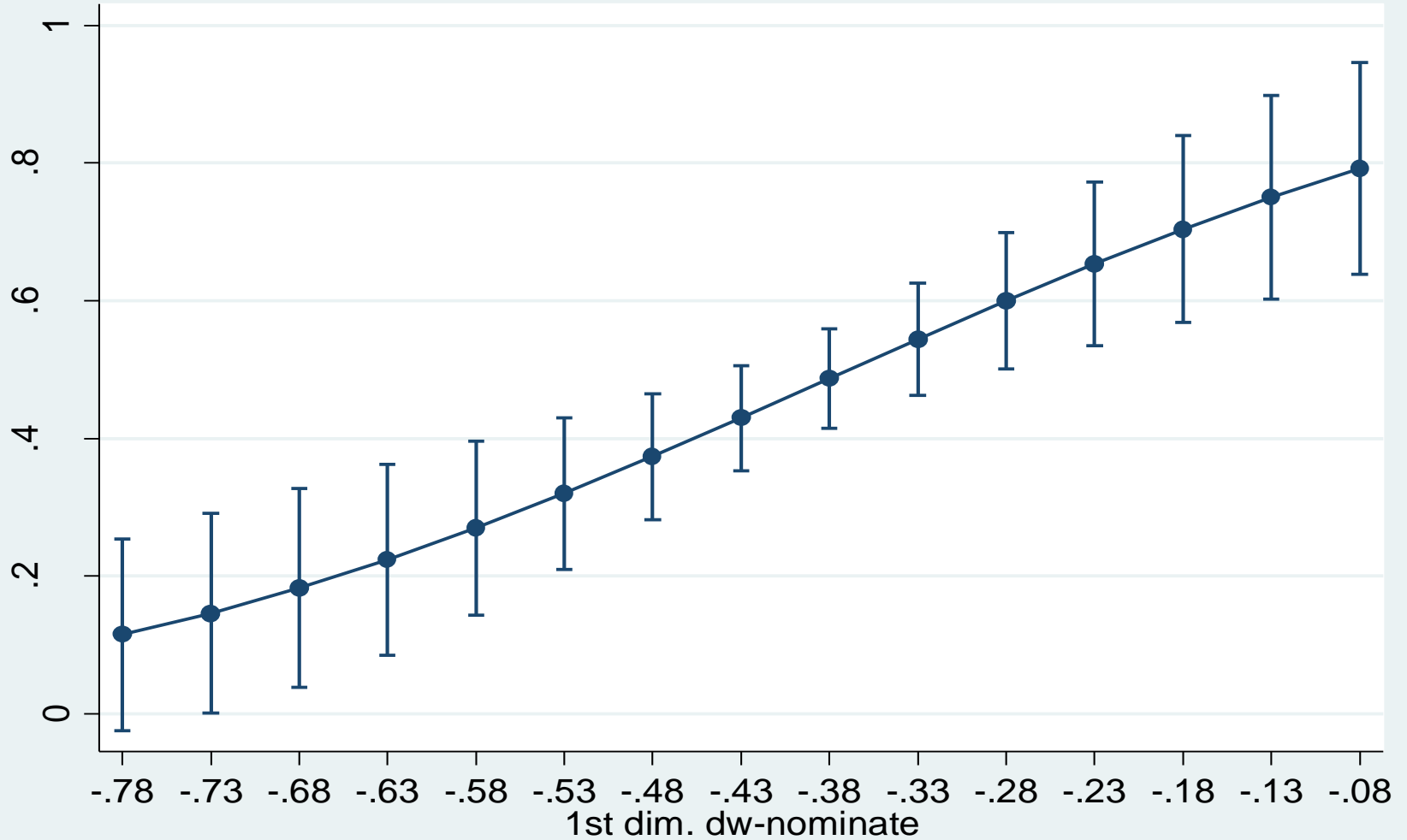


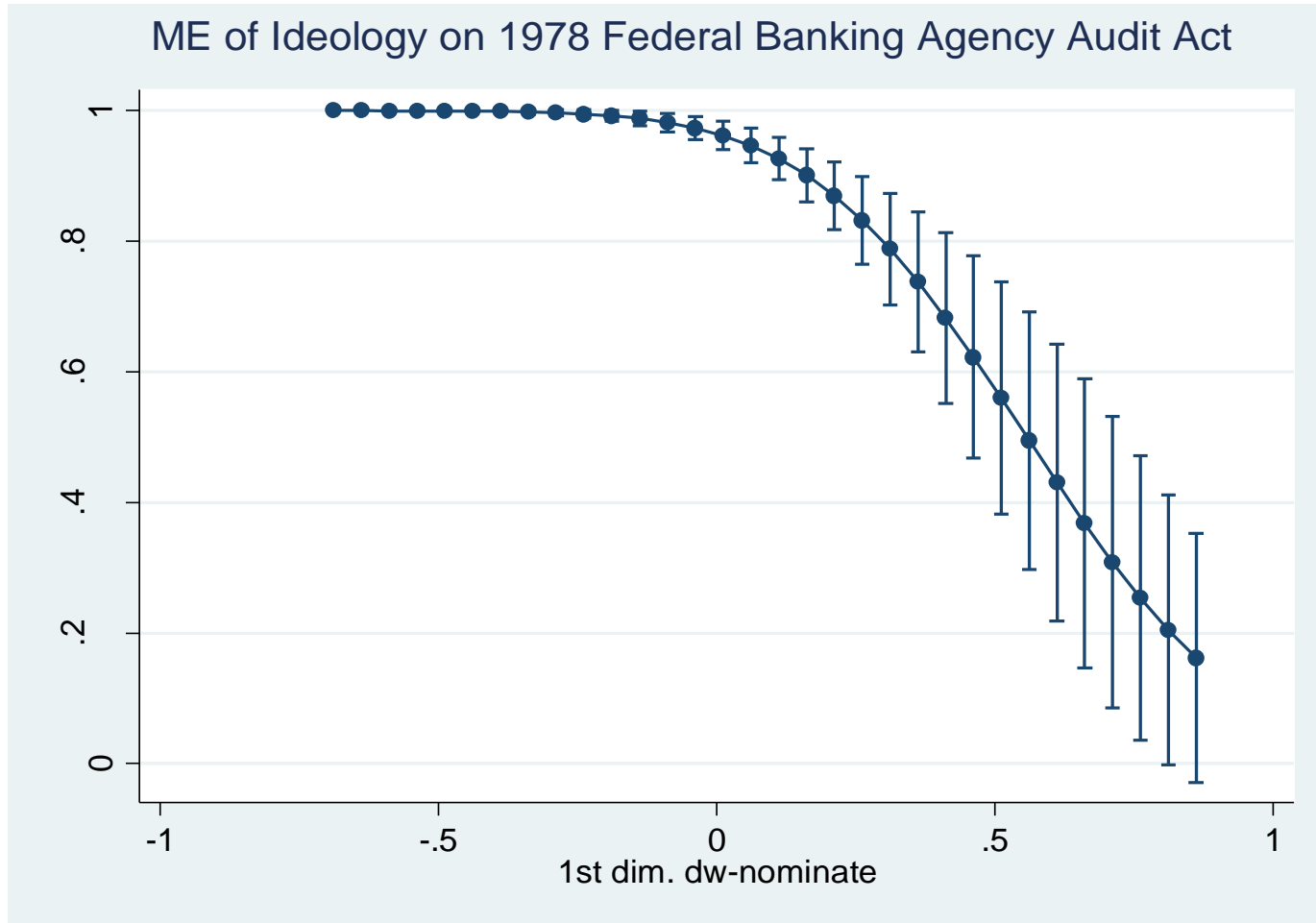
Figure 7: Marginal Effects of Dem's Ideology on "Audit the Fed" Voting



Left-Wing Dems-----Right-Wing Dems

Moving from most left-wing Dem (Jim McDermott WA) to most right-wing Dem(Heath Shuler NC) increases the odds of voting "yes" by 67 percentage points

Ideology had opposite effect during the inflationary 1970s



- Left supported GAO audits of the Fed and the Right opposed them

Conclusions

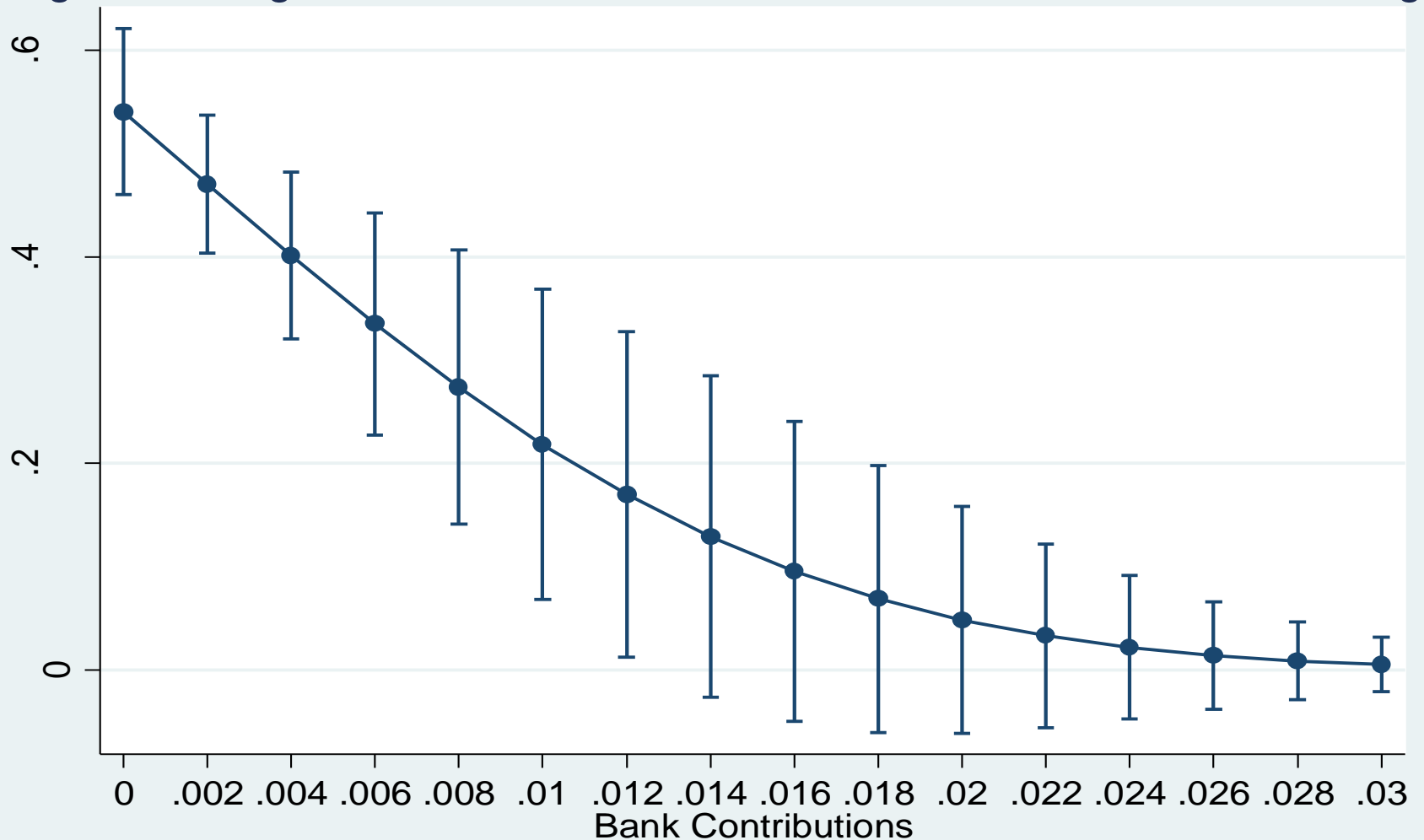
- Ideological positions on the Fed have reversed during the crisis
 - Right is now challenging the Fed to be more transparent, more accountable, and less “global”
 - Left is positioning itself as the Fed’s defender
- Conjecture: The Fed has changed, not the coalitions

Extra Slides

Voting on Audit the Fed (probits)

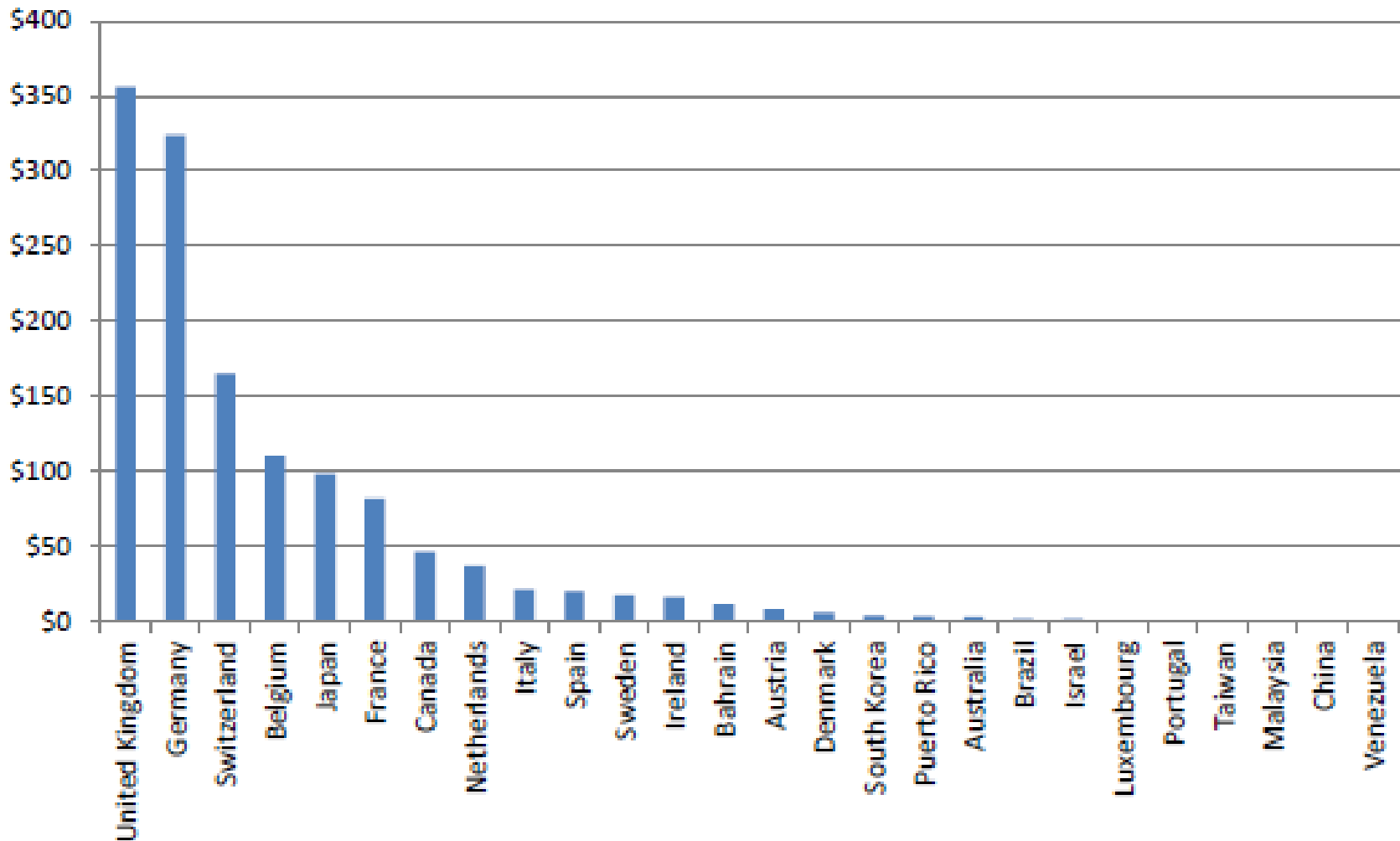
	(1)	(2)	(3)	(4)	(5)
Bank	-71.374***	-98.493***	-94.135***	-100.912***	-95.293***
Contributions	(26.214)	(28.541)	(28.700)	(35.028)	(27.059)
DW-Nominate		3.659*** (0.848)	3.618*** (0.880)	3.108*** (0.935)	3.544*** (0.551)
Social Security			1.683 (2.831)	1.840 (2.976)	1.651 (2.950)
Foreclosure Rate			13.335 (15.613)	12.174 (16.050)	12.332 (16.280)
Bank HQ				-0.046 (0.665)	-0.057 (0.663)
Chamber Seniority				-0.048** (0.021)	-0.045** (0.019)
Finance Committee				0.158 (0.323)	0.152 (0.306)
Obs.	186	185	185	182	416
Pseudo R2	0.025	0.117	0.121	0.143	0.518

Figure 6: Marginal Effects of Bank Contributions on "Audit the Fed" Voting



e.g. Dem that gets 1% of total contributions from banks is 38 percentage points less likely to vote "Yes" than a Dem that gets 0%

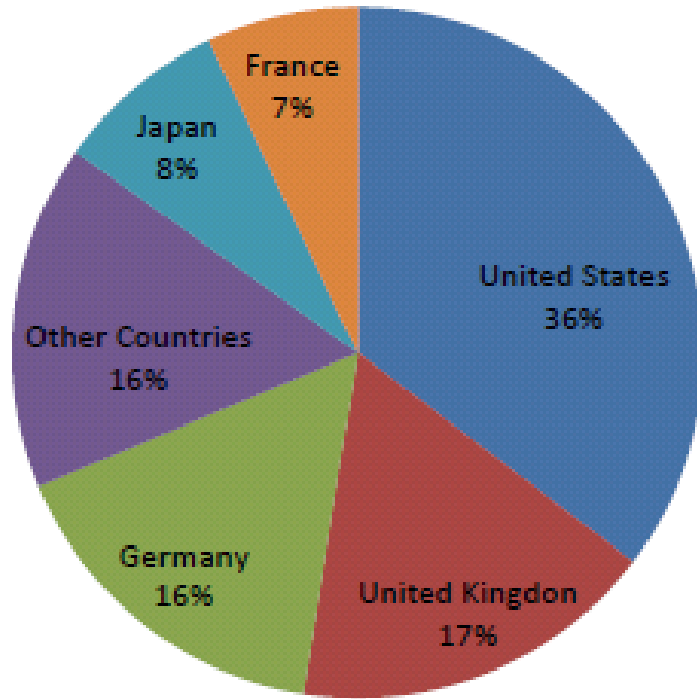
Fed Lending to Foreign Banks, by Country (Billions USD at peak)



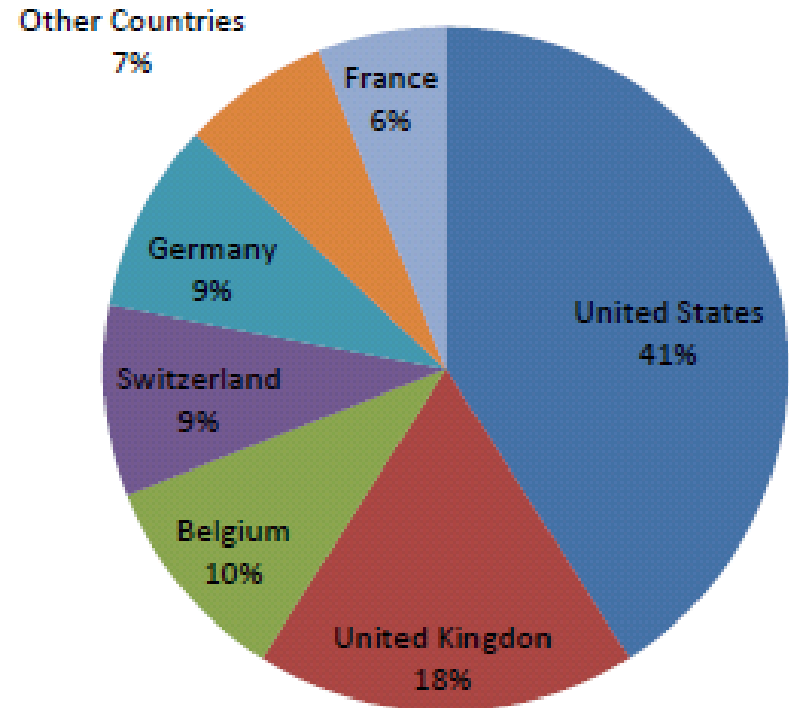
Fed's Dollar Swap Lines with Central Banks

Foreign Central Bank (date announced)	Number of Transactions	Peak Amount (Billions USD)	Peak Trade Date
European Central Bank (12/12/2007)	271	170.93	Oct 15 2008
Bank of England (09/18/2008)	114	76.31	Oct 15 2008
Bank of Japan (09/18/2008)	35	50.17	Oct 21 2008
Swiss National Bank (12/12/2007)	81	13.11	Jan 13 2009
Danmarks Nationalbank (09/24/2008)	19	10.00	Oct 24 2008
Sveriges Riksbank (09/24/2008)	18	10.00	Oct 15 2008
Reserve Bank of Australia (09/24/2008)	10	10.00	Sep 26 2008
Norges Bank (09/24/2008)	8	7.05	Jan 27 2009
Bank of Korea (10/29/2008)	10	4.00	Dec 2 2008
Banco de Mexico (10/29/2008)	3	3.22	Apr 21 2009
Bank of Canada (09/18/2008)	0	0	-
Reserve Bank of New Zealand (10/28/2008)	0	0	-
Banco Central do Brasil (10/29/2008)	0	0	-
Monetary Authority of Singapore (10/29/2008)	0	0	-

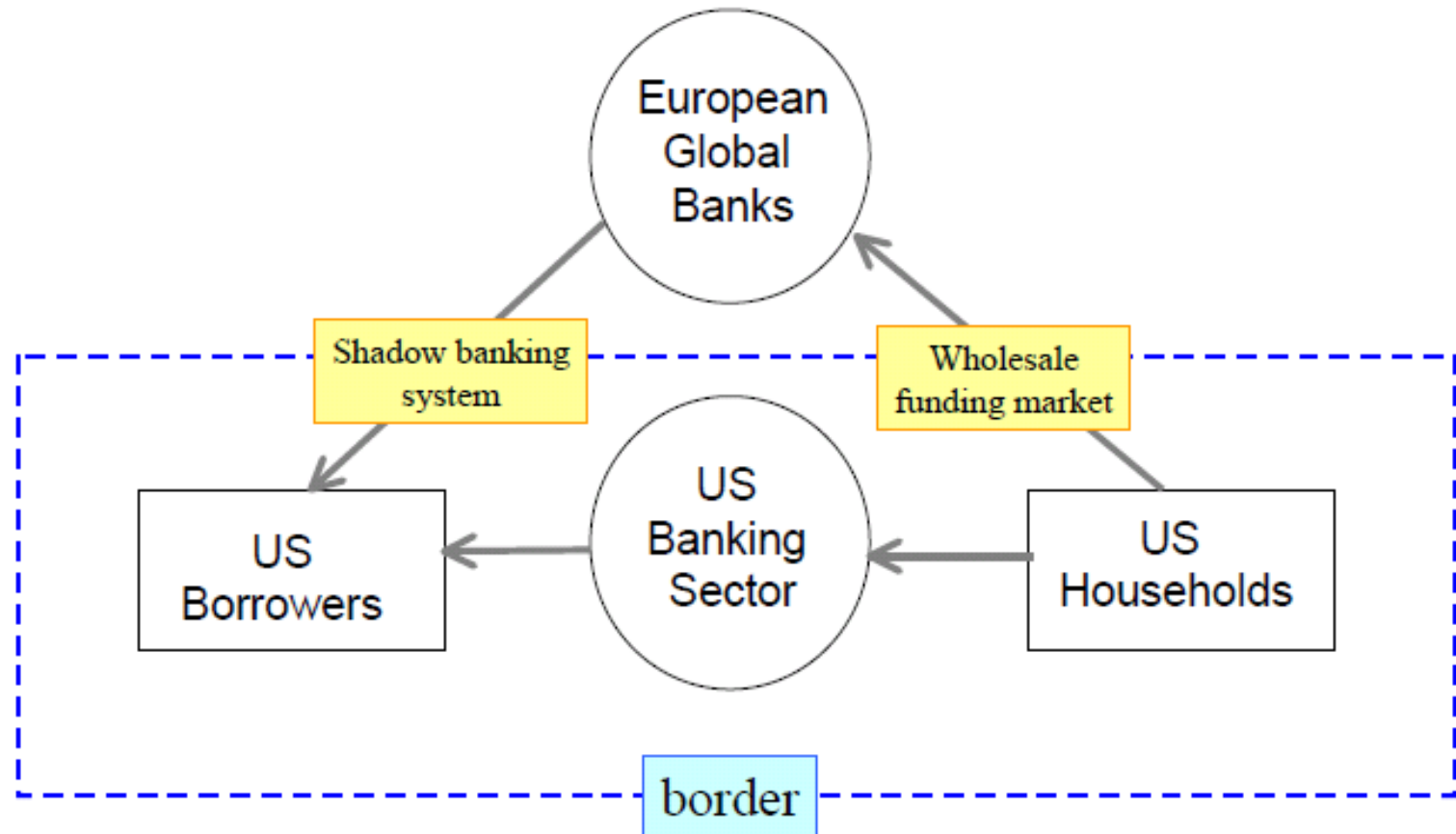
Term Auction Facility (TAF)



Commerical Paper Funding Facility (CPFF)



Why the Fed acted as global LLR



Shin, Hyun Song. 2012. "Global Banking Glut and Loan Risk Premium."