THE LIFE CYCLES OF COMPETING POLICY NORMS
Localizing European and Developmental Central Banking Ideas

Arie Krampf

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The Life Cycles of Competing Policy Norms

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Arie Krampf

Abstract

During the 20th century, the institution called central bank was diffused globally. However, central banking practices differed significantly between European market-based economies and developing economies. This paper traces the ideas and norms that shaped and legitimized central banking practices in the two areas. The paper argues that during the period from the 1940s to the 1970s two central banking policy norms existed: the liberal norm, which emerged in Europe, and the developmental central banking norm, which emerged in Latin America and diffused to East Asia. The paper seeks to trace the life cycles of the two norms: to specify the ideational content of each norm and to identify the actors and networks that produced, promoted and diffused them. The paper makes two contributions. First, theoretically, on the basis of Finnemore and Sikkink's theory of international norms' dynamics, it introduces a mechanism that explains the emergence and internationalization of an alternative international norm in the periphery that challenges the standard international norm. Second, it contributes to the literature on comparative regionalism by historicizing the liberal/European standard of central banking practices and by identifying the existence of an alternative standard for central banking practices in developing countries. The paper covers the period from the 1940s to the 1970s.

The Author

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1. Introduction

During the 20th century, the institution called central bank was diffused globally (Marcussen 2005). At the outbreak of the First World War (WWI), 22 central banks existed; by the year 2000, more than 170 central banks operated around the world (Table 1). Ostensibly, this is a remarkable case of diffusion coupled with global convergence: An institution that emerged among a small number of European countries (Broz 1998) evolved into a universal organ that every state had to adopt.

However, whereas all countries were exposed to the normative pressure to establish a central bank, the literature shows that in the postwar period up until the 1980s, central banks differed in the practices they employed. Variations were most strongly noted between central banks in developed European countries that used indirect (arm’s length) instruments to control the demand for credit, and central banks in developing countries that used administrative instruments to control the banking system and the allocation of credit (Sayers 1956; Sen 1956; Fousek 1957; Basu 1967; Brimmer 1971; Khatkhate/Villanueva 1978; Coats/Khatkhate 1984; Haggard et al. 1993).

Economists have portrayed the deviant central banking practices in developing countries as politicized institutions that served as an arm of the government (Fry 1982, 1997; Fry et al. 1996). This view was rooted in liberal theories of central banking assuming that central banks are part of the institutional and legal infrastructure of market economies as they regulated the supply of money and prevented governments from abusing their power (North/Weingast 1989). The liberal theory of central banking, therefore, was primarily based on the European experience and history of central banking (Sayers 1976; Capie et al. 1994; Broz 1998).

However, the use of the liberal theory as a yardstick for evaluating central banking in developing countries creates a bias that prevents us from understanding the role of central banks in very different institutional environments, such as in developed market-based economies, on the one hand, and in developing countries, on the other. It portrays central banks in market-based economies as apolitical actors, thereby obscuring the political base of these institutions, while concurrently calling central banks in developing economies politicized actors, thereby obscuring the economic function of these institutions in developing countries.

In order to lay out the economic rationale of central banks in developing countries, my aim is to trace the type of the ideas that have been shaping and legitimizing the behavior of central banks there. On the basis of previous research, I assume that in the period from the 1940s to the 1970s, there were two competing sets of ideas regarding the role of central banks, their objectives, instruments and institutional design: the liberal norm of central banking and the developmental norm of central banking (Krampf 2012, forthcoming a, b). This paper traces the life cycle of each of the two norms, their origin, the actors that promoted them and the networks that enabled the continuity of these norms over time and their transfer over space.

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1 This paper was written during my stay as an Associate Researcher at the Kolleg-Forscherguppe “The Transformative Power of Europe” in the academic year 2012-2013. During my stay, I had numerous discussions about the topic with Tanja Börzel and Thomas Risse, for which I would like to thank them. I would also like to thank Barbara Fritz and David Levi-Faur for valuable insights, as well as my colleagues Ali Arbia, Andrea Bianculli, Isik Özel, Dani Berliner, Majda Ruge and Elin Hellquist for their valuable comments. The research is based on material I collected during a field trip to the IMF archive that was funded by the KFG “The Transformative Power of Europe”.
Table 1: Four Global Phases of Central Bank Establishment

<table>
<thead>
<tr>
<th></th>
<th>Emergence Period</th>
<th>Gold standard</th>
<th>Interwar Period</th>
<th>Bretton Woods</th>
<th>Liberalization</th>
<th>Total Sum</th>
</tr>
</thead>
<tbody>
<tr>
<td>Central &amp; Western Europe</td>
<td>10</td>
<td>2</td>
<td>2</td>
<td>3</td>
<td>2</td>
<td>19</td>
</tr>
<tr>
<td>East Europe &amp; Central Asia</td>
<td>0</td>
<td>3</td>
<td>6</td>
<td>1</td>
<td>19</td>
<td>29</td>
</tr>
<tr>
<td>Latin America &amp; Caribbean</td>
<td>1</td>
<td>3</td>
<td>9</td>
<td>15</td>
<td>6</td>
<td>34</td>
</tr>
<tr>
<td>Sub-Saharan Africa</td>
<td>0</td>
<td>0</td>
<td>1</td>
<td>26</td>
<td>8</td>
<td>35</td>
</tr>
<tr>
<td>Middle East &amp; North Africa</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>18</td>
<td>2</td>
<td>20</td>
</tr>
<tr>
<td>East Asia &amp; Pacific</td>
<td>0</td>
<td>1</td>
<td>4</td>
<td>13</td>
<td>6</td>
<td>24</td>
</tr>
<tr>
<td>South Asia</td>
<td>0</td>
<td>0</td>
<td>2</td>
<td>4</td>
<td>2</td>
<td>8</td>
</tr>
<tr>
<td>Oceania</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>2</td>
<td>2</td>
</tr>
<tr>
<td>North America</td>
<td>0</td>
<td>1</td>
<td>1</td>
<td>0</td>
<td>0</td>
<td>2</td>
</tr>
<tr>
<td>Totals:</td>
<td>11</td>
<td>11</td>
<td>26</td>
<td>80</td>
<td>45</td>
<td>173</td>
</tr>
</tbody>
</table>

Source of central bank inception dates: Author’s Database

This paper makes two contributions. First, it contributes to the literature on diffusion of international norms. It applies Finnemore and Sikkink’s conceptualization of international norm life cycles and Acharya’s conceptualization of regional norms and localization. It employs a theoretical framework explaining the emergence of an alternative international norm that challenges the standard international norm in the same policy area. This insight is significant and instructive in helping us understand the diffusion of ideas, norms and practices in a heterogeneous world system. In that sense, the framework connects the diffusion literature and insights from the literature on developmentalism.

Second, the analysis presented in this paper contributes to the literature on comparative regionalism. As Börzel and Risse argue, the literature on comparative regionalism has thus far adopted the European model as a standard for other processes of regional integration (Börzel/Risse 2012). Taking the European model as a standard implies that any deviation is interpreted as resistance, distortion or decoupling. These terms portray peripheral actors as passive (receivers or rejecters) and peripheral norms as deficient. In order to overcome this bias of the comparative regionalism literature, one has to historicize the liberal standard and to study its emergence according to the same methodology used for studying the emergence of the alternative. As articulated by Börzel, one has to account for the supply side of regional models in other regions.
(Börzel/Risse 2009; Börzel 2011). The paper contributes to this endeavor by juxtaposing the life cycles of two central banking norms — the liberal and the developmental — from the interwar period to the 1970s and by tracing the intellectual origins of the two norms as two co-existent standards by which central banks practices were legitimized and evaluated.

The paper spans four decades in order to demonstrate the long-term evolution of these two norms. This approach poses a methodological challenge. Therefore, rather than presenting a linear and continuous evolution of the two norms, the paper focuses on specific milestones and key actors to present an outline of the two life cycles. Moreover, it focuses on the ideational content of each norm and the networks that distributed them.

The analysis presented raises questions regarding the political economic aspects of the consolidation process of the two regional norms: Why did local actors in the periphery reject the liberal/European norm of central banking and why did certain global actors participate in the promotion of the alternative developmental central banking norm in the periphery? Due to the lack of space in this article, I focus on establishing a link between certain types of ideas and certain types of actors. The descriptive analysis cannot make reference to the motivations of actors on the basis of their own discourse. However, the research design does not aim at establishing a causal explanation.

2. The Life Cycle of an Alternative Policy Norm

An international norm is defined as a “set of standards for the appropriate behavior of states” (Finnemore/Sikkink 1998: 893). Thus, the existence of an international norm does not necessarily imply that all actors actually follow the norm, but rather that local actors employ the norm as a standard to evaluate their behavior. In that sense, a policy norm can be understood as an international policy fashion, an informal imperative to act in a certain way that is considered appropriate. The norm functions as a regulative ideal that sets the standard for behavior.

The life cycle of an international norm has three stages: emergence, cascade and internationalization (Finnemore/Sikkink 1998). The norm emerges among norm makers, in most cases dominant countries at the center. Then norm entrepreneurs promote the norm at the international level, which is then adopted by other countries. Finally, the norm gains a taken for granted status when it is institutionalized internationally as a standard. Therefore, the implication of Finnemore and Sikkink’s theory of international norms’ dynamics is that the center (the developed countries, the global North or the First World) creates norms and the periphery (the developing countries, the global South or the Third World) experiences the pressure to follow them. The periphery — the norm takers — does not necessarily actually adopt the norm. Peripheral actors may reject or translate them. Yet, the theory tacitly assumes that peripheral actors do not create their own norms.

However, in fact, the mechanism that explains the life cycle of an international standard norm can, with some minor alterations, be used to explain an alternative scenario, according to which an alternative norm
emerges in the periphery. While the life cycle of an alternative norm consists of similar stages compared to the standard international norm, the process of norm emergence and its outcome are different.

In the periphery, an alternative norm emerges due to a process of localization or translation of a standard norm. The literature on norm diffusion has shown the incongruity between global standards and domestic norms for many cases (Risse-Kappen 1994; Cortell/Davis 2005). One possible outcome is that local actors in the periphery localize and translate global norms, making them congruent with local norms (Djelic 1998). Amitav Acharya addresses cases in which peripheral countries do not adopt the international standard but rather create a regional norm through localization. He defines localization as “a complex process and outcome by which norm-takers build congruence between transnational norms (including norms previously institutionalized in a region) and local beliefs and practices. In this process, foreign norms, which may not initially cohere with the latter, are incorporated into local norms” (Acharya 2004: 241, my emphasis).

The concept of an alternative or regional norm raises a set of fundamental questions. First, if we restrict the discussion to the economic policy domain, international standard norms consist most likely of liberal and market-based economic ideas that prescribe the adoption of market-oriented practices. As such, the localization of market-based ideas involves not only a potential clash with local cultural norms but also with competing local views regarding the effectiveness of the liberal policy prescriptions in developing countries. Therefore, discussing the transfer of policy norms from the global North to the global South, one cannot neglect the issue of effectiveness of liberal practices and institutions in a developmental institutional environment (Marsh/Sharman 2009).

In the second and third stages, two processes take place simultaneously: The norm cascades to other “similar” (developing) countries and those countries promote the alternative norm internationally. By definition, norm entrepreneurs in the periphery have fewer resources than norm entrepreneurs in the center to create, promote and internationalize norms. As Finnemore and Sikkink point out, norm entrepreneurs require organizational platforms in order to promote a norm internationally (Finnemore/Sikkink 1998). Peripheral actors have only limited access to these platforms.

However, peripheral actors can overcome this weakness via two possible strategies. First, they may collaborate with international actors in order to promote the alternative norm. In other words, they may create transnational policy networks comprising both local-peripheral and international actors. Through such networks, participants “can build alliances, share discourses and construct the consensual knowledge that defines an international policy community”. The transnational structure of the network “enable[s] actors to operate beyond their domestic context, and networks are the means by which organizations individually and in coalition can project their ideas into policy thinking across states and within global or regional forums” (Stone 2004: 560).

The assumption that peripheral and international actors collaborate in promoting alternative norms implies that norm entrepreneurs do not necessarily promote ideas that reflect the interest of their territorial institutions: American economists, for example, may promote norms that do not reflect US interests. Norm entrepreneurs do not simply (and always) represent interests of states, sectors or international organizations. In many cases, they are driven by a so-called “ideational commitment” (Finnemore/Sikkink 1998).
This notion implies that the content of norms promoted by norm entrepreneurs cannot be fully explained on the basis of geopolitical interests.

Secondly, peripheral actors can compensate for their weakness in resources by promoting the alternative norm collectively with other actors from the periphery. That is, peripheral countries have a strong incentive to collectivize their endeavor to construct an alternative to the global standard. Whereas dominant actors, i.e., the US or the EU, may construct and promote a global norm unilaterally, peripheral countries with similar interests in promoting the alternative norm must do it collectively.

Promoting the alternative norm at the international level enables peripheral countries to shape the international policy discourse and boost the legitimacy of deviant behavior. Namely, in order to reconcile the quest for international recognition, on the one hand, and the domestic pressure to adopt non-standard policy measures, on the other, peripheral countries may promote an alternative norm to improve the legitimacy of deviant practices and reduce the costs of rejecting the global norm. As Acharya puts it, peripheral countries can “create rules with a view to preserve their autonomy from dominance, neglect, violation, or abuse by more powerful central actors” (Acharya 2011: 97). Therefore, the construction of a regional policy norm is a discursive strategy by which local-peripheral actors protect their domestic discretion (Langenhove 2011: 73). The success of such an endeavor enables local actors “to take greater control of financial affairs at the regional level than previously” (Breslin et al. 2002; see also Figure 1).

The concept of an alternative international norm contributes to the discussion by shifting attention from the attempt to understand convergence to the attempt to understand patterns of variations. It implies that patterns of variation may not only be the product of local factors, but also the product of alternative and competing international norms that provide alternative scripts of behavior for local actors.
3. Competing Central Banking Norms

The idea that central banks operate according to norms might seem inconceivable to orthodox economists who assume that central bankers operate according to theory, rule or experience. The concept of policy norms rejects the notion that central bankers shape their behavior on the basis of theory, assuming instead that theory is only part of a specific central banking norm. The framework employed here assumes that central bankers are an epistemic community that shares causal and principled beliefs, which are considered theoretically valid and useful (Haas 1992; Stone 2004). The concept of a central banking norm seeks to capture the socio-political and historical fact that central bankers at different times and places had different views regarding best practices of central banking.

On the basis of previous studies, I identify two central banking norms that prevail in the 20th century: the liberal norm of central banking and the developmental norm. The liberal norm assumes that the key resource of a central bank is its independence from governments and political influence. Independence is required in order to maintain the stability of purchasing power of the currency. However, the idea of independent central banking was only one element of the norm. This element was embedded in an institutional environment of liberalized domestic financial sectors and liberalized international financial markets (free flow of capital) (Table 2).
The Life Cycles of Competing Policy Norms

Table 2: Domestic and International Monetary Arrangements

<table>
<thead>
<tr>
<th></th>
<th>Domestic</th>
<th>International/Regional</th>
<th>Central banking</th>
</tr>
</thead>
<tbody>
<tr>
<td>Liberal/European</td>
<td>• Liberalized financial systems</td>
<td>• Free flow of capital</td>
<td>• Price-stability seeking independent central banking</td>
</tr>
<tr>
<td></td>
<td>• Independent central banks</td>
<td>• Full convertibility</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Reducing capital control</td>
<td></td>
</tr>
<tr>
<td>Developmental</td>
<td>• Preferential credit policies</td>
<td>• Managed exchange rates</td>
<td>• Extensive administrative instruments</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Capital controls</td>
<td></td>
</tr>
</tbody>
</table>

Source: Author’s Illustration.

The notion that central banks have to be independent from governments is justified by the neo-institutional theory, which argues that independent institutions are necessary to protect the market from governments (North/Weingast 1989). Central banks, according to this literature, are part of the legal infrastructure which is required for the performance of an efficient and just market economy. This theory was demonstrated on the basis of European experience and history.

However, in developing countries, financial systems were underdeveloped and market forces led to outcomes that were incongruent with national preferences. Thus, many economists believed that central banks should not protect the private sectors, but rather intervene in the allocation of resources. The literature identifies two key financial policy problems that were unique to peripheral developing countries and that justified a different type of central banking practice. Domestically, due to the underdeveloped banking system, the saving level was very low in comparison to developed countries and also compared to the demand for developmental credit. Therefore, many economists believed that governments should intervene in the allocation of resources according to national preferences (Sayers 1956; Sen 1956; Fousek 1957; Basu 1967; Brimmer 1971; Khatkhate/Villanueva 1978; Coats/Khatkhate 1979, 1980; Haggard et al. 1993).

Externally, peripheral countries had stronger incentives to protect themselves from international financial shocks and speculative financial flows. As small peripheral economies, they were exposed to high risks of speculative capital flows. Within the gold standard regime, changes of interest rates in the global financial centers ignited massive capital in- and out flows that destabilized small economies lacking the capacity to absorb them. The devastating consequences of capital flows were one of the lessons for developing countries from the gold standard period (Lindert 1969). In the postwar period, due to the gap between domestic savings and investment, peripheral countries relied heavily on imports of capital to finance investment. The external debt exposed them to a high risk of exchange rate volatility which arose from the fact that a country’s public debt is denominated in a foreign currency (Love 1995: 405–408; Eichengreen/Hausmann 1999; Fritz/Mühlich 2010).
The developmental norm of central banking prescribed the provision of central banks with extensive discretion and administrative instruments to control the banking and the allocation of resources. This approach was justified on the basis of the assumption that the liberal model of central banking, which was based on arm’s length control or indirect monetary instruments, was ineffective in developing countries. Rather than defending the private sector, the developmental central bank used its capacities to improve the capacity of governments to confront private actors and/or mobilize them.

4. Methodology

In this article, my aim is to capture the ideas that shaped central banking practices in certain regional contexts. The theoretical framework predicts the existence of institutional and ideational continuities over time within European institutions and discourses. This prediction implies that we are likely to be able to identify regional actors (transnational or hegemonic) that promoted the liberal central banking norm. Identifying such continuities — despite the change of the international regime and the consolidation of the Bretton Woods regime (Ruggie 1982; Ikenberry 1992) — would support the claim of the European origin of the liberal central banking norm.

In the case of the developmental norm, the theoretical framework predicts the existence of transnational linkages between peripheral and international actors (from the center) through which ideas were exchanged, uploaded, downloaded and diffused. Moreover, the framework predicts that these actors promote alternative central banking ideas that challenge the liberal market-based premises.

In both cases, the analysis is based on published and unpublished documents produced by technocrats, central bankers and economists that were employed by central banks or academic economists. The analysis is also based on extensive literature from the 1950s and 1960s about central banking in developing countries.

5. The European Regional Norm Internationalized

The literature on the history of international regimes underlines the ideational break between the gold standard and the post-WWII monetary regime that was associated with the rise of Keynesianism and the regime of embedded liberalism (Ruggie 1982; Weir 1989; Ikenberry 1993; Helleiner 1996). However, a closer examination reveals that the ideational legacy of the gold standard had never been fully abandoned in the European context. The regional actor that kept the gold standard legacy alive was the Bank for International Settlements (BIS).

The BIS was established in 1930 to handle the imbalances that arose from the reparation agreement. It was established by the governments of Germany, Belgium, France, the United Kingdom (UK), Ireland, Italy, Japan and Switzerland. It became a transnational organization that served as a club of central bankers.
From 1930 until the collapse of the gold exchange standard in 1933, the BIS played a central role in the effort to save the gold standard. In the words of Toniolo, the gold standard “was embedded in the very DNA of the BIS” (Toniolo 2005: 131). Following the collapse of the gold standard, the BIS, with the leadership of the Bank of England, used conditionality pressures on European crisis-affected countries and forced them to establish independent central banks following the model of the Bank of England (Toniolo 2005: 24–60).

After the Second World War the BIS collaborated with the US in implementing the Marshall Plan. Both actors shared the agenda of promoting liberal financial reforms in crisis-stricken European countries. The institutional linkage between the BIS and the Marshall Plan was manifested by the role of Per Jacobsson, who was present in both institutions. Per Jacobsson, a Swedish economist who was a key figure at the BIS during the 1930s, was employed by the Organization for European Economic Co-operation (OEEC, established in 1948; from 1961 on it became the OECD), which oversaw the implementation of the Marshall Plan, and by the European Payments Union (EPU, established in 1950), which promoted multilateralism, price stability and convertibility among European currencies. Both institutions played a role in the maintenance and diffusion of ideas regarding the desirability of independent central banks and liberalization of financial systems.

Jacobsson believed that the establishment of independent central banks in European countries was a condition for European regional as well as for international stability. An independent central bank, he argued, was the only institution that was “strong enough to do the fighting” against governments to secure currency convertibility and the free flow of capital (Jacobsson 1958: 268–67).

Obviously, the Marshall Plan’s capacity to enforce the norm on all European countries was limited. The countries that experienced the strongest pressure to comply were those on the losing side and in need of financial assistance (James 2003: 84). The Bundesbank is a case in point. The high level of the Bundesbank’s independence and its adherence to price stability is often explained on the basis of the German ordoliberal tradition (Ptak 2009) and the U.S. preference for a multilateral liberal regime (Holtfrerich/Reis 1999). The Central Bank Act stipulated that “the bank is not subject to instructions from any political body or public office, with the exception of the courts”. The Act set only one goal for the Bundesbank: “safeguarding the currency” (quoted in Neumann 1999, 276–77). As an advisor to the EPU, Jacobsson’s key aim was “to restore equilibrium in the balance of payments” (Jacobsson 1979: 241). He believed that “external [international] equilibrium” would be achieved through “internal [domestic] equilibrium”, which in turn would be achieved through full convertibility and the free flow of capital (Jacobsson 1958: 268-67; see also James 2003: 82). In 1959, the International Monetary Fund (IMF) was actively involved in Spain’s financial reform. Jacobsson was personally involved in this process that was deemed very successful (Calvo-Gonzalez 2006). The reform was portrayed as a decision to adjust the Spanish economy “in line with the countries of the Western world, and to free it from the interventions inherited from the past which do not correspond to the needs of the present situation” (James 2003: 84, 85).

The IMF also participated in enforcing liberal reforms in European countries during the 1947-49 crisis (Block 1977: 37). Fred Block goes so far as to argue that during the Truman administration, the IMF became “another means to impose the deflationary discipline of the gold standard” (Block 1977: 37). According to him, the Marshall Plan had a deep and long-lasting effect on European policies. Immediately following the war,
many Western European countries adopted the paradigm of national capitalism — namely, exchange controls, capital controls, bilateral and state trading arrangements — after the 1947-1949 financial crisis, while “it became [a] central aim of United States foreign policy to prevent the emergence of national capitalist experiments” (Block 1977: 9).

A significant indicator for the uploading of the liberal/European norm of central banking to the international level was the nomination of Jacobsson to the Director of the IMF in 1956, a position he held until his death in 1963. Jacobsson was key in shaping the IMF’s approach to central banking in this period. But he was not alone. Edward Bernstein, the Director of the Research Department at the IMF, shared Jacobsson’s view regarding the proper role of central banks, specifically opposing the idea of central banks being involved in allocating “credit for productive purposes” because of its inflationary effect (Bernstein/Patel 1952: 373–74).

The historical record shows that the gold standard tradition has never been fully relinquished within the European central banking discourse and also in the discourse of the IMF. Indeed, in the 1950s, Europe went through a process of reconstruction and the government’s involvement in the economy was far-reaching. Specifically, countries such as France, Italy and Belgium used selective credit instruments quite extensively. On the other hand, Germany, Austria, the UK and the Netherlands were quite close to the liberal ideal type. Moreover, the BIS continued to promote the liberal model.

Under Jacobsson’s directorship, the IMF also promoted the liberal model of central banking. However, it focused its efforts on European countries. Until the Central Banking Service was established in 1963, the IMF did not invest much effort in shaping central banking practices in developing countries. For instance, in 1955, Brazil requested the advice of Edward Bernstein, but the IMF board did not permit Bernstein to offer advice on behalf of the Fund. The Board eventually conceded, after the Brazilian government had insisted on covering the costs of Bernstein’s visit to Brazil. When Vietnam requested advice in 1956, the Board again demanded that the Vietnamese government assume the costs and responsibility (Horsefield 1969: 391-394). Therefore, developing countries did not operate under the pressure to adopt the liberal standard of central banking.

2 The Belgian central bank used selective credit policies to channel credits to domestic investment (Dorrance and Villanueva 1971). While Italy and France used selective credit controls extensively, these instruments were not implemented by central banks, but by networks of state institutions in which central banks were not the most important institutions (McCarthy 1973; Hodgman 1973; Capie et al. 1994, 134).

3 The German central bank used instruments of direct control only in cases of crisis (McCarthy 1971). In Austria, capital controls were abolished in 1962. This move prevented the central bank from keeping interest rates at lower rates than abroad and therefore the use of selective credit policies was impossible (Khathkate 1970). In the Netherlands, credit control was primarily used to control the volume of credit rather than its allocation (Dorrance and Khathkate 1972; Hodgman 1973: 141).
6. The Latin American Origin of the Developmental Norm of Central Banking

During the 1920s, the Bank of England made extensive efforts to save the gold standard. Among other measures, it promoted the establishment of independent central banks in the periphery according to the liberal model (Drake 1989). With the collapse of the gold standard in 1933, the conditionality pressure ceased and peripheral countries had the capacity to experiment with central banking practices that deviated from the liberal model.

In 1935, Raúl Prebisch redesigned the Bank of Argentina in a way that differed from the Bank of England’s model in two key respects. First, the Bank of Argentina was endowed with extensive supervisory powers. The supervisory authority — or the banking department — was combined with the monetary authority — the issue department. The supervisory powers of the bank overshadowed its traditional monetary authority. In contrast, the Bank of England had a strong and independent issue department responsible for monetary policy and a relatively weak banking department responsible for supervision (Triffin 1944; Andreades 1966; Bordo 1984). In fact, the Bank of Argentina used supervisory administrative powers to achieve goals that were far beyond the stability of banking institutions.

Second, the Bank of England was a joint stock company that had a special contract with the government and its board of governors comprised bankers (Sayers 1976). In contrast, the Bank of Argentina was a state agency and its board comprised of representatives of all economic sectors (Triffin 1944: 100). Hence, it represented the interests of economic sectors and had the legitimacy to confront the financial sector, whereas the Bank of England was much more closely linked with the financial sector (Love 1995: 405–408).

The two institutional features of the Bank of Argentina — extensive discretion in the use of administrative instruments and the sectorial composition of its board of directors — turned the central bank into a powerful institution, in order to allocate credits and implement developmental policies. However, from the perspective of liberal market-based economic ideas, the Argentinean central bank was considered to be politicized as it represented domestic sectors.

6.1 Uploading the Latin American Norm

When Robert Triffin, an American economist who was employed by the Federal Reserve System, was sent to Latin America as economic adviser, he was deeply impressed by the Argentinean central bank. The Argentinean central bank, he wrote, forces us to look “in new directions as yet untried in traditional central banking practices”. Triffin approved the extensive power of the Bank, saying that “it is all the more necessary to endow the monetary authorities with adequate weapons of control” (Triffin 1944: 109). The Federal Reserve board of directors embraced Triffin’s view and confirmed that it “should be considered as a path-breaking innovation in this field.” The board expressed the hope that “this new adventure might influence thinking in the field of central banking both at home and abroad” (Federal Reserve Bank Board of Governors, quoted in Helleiner 2009a: 14).
Triffin’s enthusiasm regarding the unique Argentinean central banking model raises questions regarding the different positions on best central banking practices of the BIS economist Jacobsson and the Fed economist Triffin. Eric Helleiner suggests that the Fed’s approach was consistent with the US’ interests in Latin America and its Good Neighbor policy (Helleiner 2009a, 2009b). However, it is unlikely that an economic expert would shape his views only on the basis of national interests; in many cases, economists and central bankers opposed quite bluntly the views of governments.

Finnemore and Sikkink suggest an alternative explanation according to which norm entrepreneurs are driven by ideational commitment (Finnemore/Sikkink 1998). This explanation implies that Triffin was committed to a different ideational legacy than Jacobsson. A brief survey of the type of ideas regarding central banking that prevailed at the Fed in the 1930s and the 1940s supports this hypothesis.

Whereas European central bankers believed that the Great Depression was caused by state intervention, Alvin Hansen — an influential economist and adviser to the State Department and the Federal Reserve System after the Depression — believed in a more active role of central banks in managing the economy (Mehrling 2010). Thus, the US administration responded to the Great Depression with the Glass-Steagall Act of 1933 and the Banking Act of 1935, which provided the Federal Reserve System with new and unprecedented power to regulate the banking system (Sproul 1951: 315–16; Friedman/Schwartz 1963: 447). Rather than liberalizing, the US administration increased regulation.

Another important figure in this regard was John H. Williams, the Vice President of the Federal Reserve Bank of New York (1936-47) and for many years an advisor to the Fed (1933-56). He was also Triffin’s supervisor at Harvard University. Williams is known for his opposition to the Bretton Woods agreement (Block 1977: 52) and he was reputed to be an advocate of free trade, convertibility and a return to a semi gold-exchange system (Best 2005: 66). However, this reputation obscures the fact that Williams criticized both the gold standard and the Bretton Woods regime for ignoring the geographical aspects of the international money regimes. He argued that the gold standard put a “double burden of adjustment upon countries not similarly equipped with free reserves” (Williams 1947a: 184) and that the Bretton Woods agreement provided only a partial solution. The agreement, he argued, was not equipped to deal with the “divided state of national attitudes and circumstances” (Williams 1947b: 59). Back in the 1930s, he had already argued that “different kinds of countries require different kinds of monetary systems” (Williams 1937: 164; see also Cohen 1998; Asso/Fiorino 2009: 183).

Hence, the intellectual atmosphere in the US in general and within the Fed in particular was very different from the one in the BIS, the OEEC and the IMF. It created a condition for a different type of ideational commitment among Fed experts that explains the engagement in diffusing the Argentinean model of central banking.
6.2 Downloading to the Asian Region

Over the next couple of years, Triffin and his colleagues used the Argentinean model as a blueprint in their technical aid to other central banks in developing countries. Triffin in person advised Costa Rica, the Philippines and the DR Congo. Other Fed experts participated in missions to Paraguay, Guatemala, the Dominican Republic, Cuba and Honduras. In the period from 1946 to 1955, 23 new central banks were established or reformed. Fed experts were involved in the establishment of 15 of the 23, including 5 of the 8 central banks in East Asia and all 8 central banks established during this period in Latin America (Table 3).

Analyzing the content of policy advice demonstrates that Fed experts did not follow the same type of central banking ideas promoted among European countries. John Exter was a Fed economist who was sent to Ceylon for a consultancy mission in which he prepared a Central Bank Bill and a Banking Bill. Exter defined the role of a central bank as being responsible for the “administration and regulation of the monetary and banking system of Ceylon” (Exter 1949: 2). The bill proposed by Exter granted the bank authority to administer “productive credit” by rediscounting bills “resulting from transactions related to the production, manufacture or processing of agricultural, animal, mineral, or industrial products” (Exter 1949: 33). The Central Bank Bill included a section on banking supervision. The supervisory department was endowed with powers to demand information from commercial banks and the authority to “take charge of all books, records and assets of the institution.” The supervisory department was also granted the power to suspend the operation of commercial banks (Exter 1949: 11). Arthur Bloomfield, who advised Korea, recommended the transfer of supervisory power from the Bureau of Financial Institutions to the central bank (Bloomfield/Jensen 1951: 55). In Vietnam the Fed’s advisor encountered resistance from the local government that was affiliated to the idea of merging the central bank and supervisory authority to centralize power. The Fed’s expert insisted that the Central Bank Bill would be combined with the Banking Act because, he claimed, a combined structure provides “adequate powers to ensure strict compliance with central bank directives” (Shiff 1958).

There is not much documentation regarding the IMF’s response to the Fed’s mission in the East. Indirect evidence is provided by a letter sent by Bloomfield to Edward Bernstein, in which Bloomfield criticized the IMF’s approach for being “too broad and general, and insufficiently oriented around the Philippines problems as such”. Bernstein was accused of “laying down general rules and principles of monetary policy”, while it was more desirable to use “illustrations drawn from [the] Philippines experience”. The IMF emphasized the “overriding necessity of maintaining internal monetary stability and of avoiding any inflationary financing”, whereas the Fed’s experts believed that the important question was “whether or not a certain amount of inflationary financing of development would be ‘safe’ and what that amount might be” (Bloomfield 1955).

It bears noting that the Bank of Argentina and the Fed were not the only sources of developmental central banking. A dominant central bank in a developing country that employed developmental practices without the Fed’s advice was the Indian Bank. After its nationalization in 1945 (Simha/Deshmukh 1970: 496), the Department of Banking Development was established (1950) to deal with the “financing of medium and small-scale industries and the establishment of State Industrial Finance Corporations”, “the mobilization of rural savings”, and the “extension of rural credit” (Simha/Deshmukh 1970: 502). In 1956, the Reserve Bank
of India Amendment Act provided the Bank for the first time with the authority to use variable reserve ratios as a monetary policy instrument (Roy 1962: 101). The Act “offered the more promising possibility of acquiring an additional instrument, which was both handy and flexible, to control the expansion of bank credit” (Balachandran 1998: 43). In the same year, the Reserve Bank started to use selective credit control (Roy 1962: 124–125; Sen 1967: 189; Balachandran 1998: 70). In later years, as we see below, a senior economist in the Indian central bank would play a key role in the IMF in the promotion of these practices.

### Table 3: Involvement of FRS Experts in the Establishment of New Central Banks

<table>
<thead>
<tr>
<th>Number</th>
<th>East Asia and Pacific</th>
<th>Latin America &amp; Caribbean</th>
<th>Middle East &amp; North Africa</th>
<th>South Asia</th>
<th>Africa</th>
<th>Europe</th>
<th>Sum</th>
</tr>
</thead>
<tbody>
<tr>
<td>Involved</td>
<td>5</td>
<td>7</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>0</td>
<td>15</td>
</tr>
<tr>
<td>Not Inv.</td>
<td>3</td>
<td>0</td>
<td>3</td>
<td>1</td>
<td>0</td>
<td>1</td>
<td>8</td>
</tr>
<tr>
<td>Sum</td>
<td>8</td>
<td>7</td>
<td>4</td>
<td>2</td>
<td>1</td>
<td>1</td>
<td>23</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Countries</th>
<th>Involved</th>
<th>Not Inv.</th>
</tr>
</thead>
<tbody>
<tr>
<td>East Asia and Pacific</td>
<td>Philippines, Korea (S.), Vietnam, Cambodia, Laos</td>
<td>Korea (N.), Myanmar, China</td>
</tr>
<tr>
<td>Latin America &amp; Caribbean</td>
<td>Guatemala, Dominican Republic, Haiti, Costa Rica, Cuba, Honduras, Paraguay</td>
<td>Iraq, Saudi Arabia, Libya, Pakistan, Libya, Germany</td>
</tr>
<tr>
<td>Middle East &amp; North Africa</td>
<td>Israel</td>
<td></td>
</tr>
<tr>
<td>South Asia</td>
<td>Sri Lanka</td>
<td></td>
</tr>
<tr>
<td>Africa</td>
<td>Congo</td>
<td></td>
</tr>
<tr>
<td>Europe</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sum</td>
<td>23</td>
<td></td>
</tr>
</tbody>
</table>

Sources: Triffin 1944: 104; Grove/Exter 1948; Exter 1949; Triffin 1946; Bloomfield/Jensen 1951; Triffin/Wallich 1953; Fousek 1957; Kim 1965: 7; Sen 1967; Helleiner 2003; Helleiner 2009b.

### 7. Internationalization of an Alternative Norm

The individual missions to the East were followed by attempts of economists from the periphery and from the center to legitimize the developmental practices of central banking in the international organizational platforms. Arthur Bloomfield played a significant role in the legitimization of developmental practices. In 1957, he published a paper in the *Journal of Finance* in which he praised the “unusually wide and flexible powers” of the new central banks that were “established since 1945 with the help of Federal Reserve advisers” (Bloomfield 1957: 191). These central banks employed instruments that were “admittedly outside the
The Life Cycles of Competing Policy Norms

In specific, Bloomfield emphasized the role of these central banks in the allocation of credit and their extensive supervisory power. Those practices were not based on sound theory, but rather on experimental practices. Nevertheless, “out of this experimentation”, Bloomfield expressed his hope, “will develop a theory of central banking policy appropriate to the economically backward countries” (Bloomfield 1957: 197, 204). In that same year, a comprehensive survey of central banking practices in developing countries was published by the Federal Reserve Bank of New York, whose president pointed out that

“[c]ountries outside the Iron Curtain have come increasingly to rely upon monetary controls in the effort to limit economic fluctuations and to promote sturdy economic growth. Foreign central banks, often operating within an institutional setting far different from that in the United States, have sought not only to adapt the traditional credit controls to the environment in which they function, but also to introduce new tools, and to use the various individual instruments in new and changing combination” (Fousek 1957: 78).

In 1963, the IMF established the Central Banking Service (CBS), which later changed its name to the Central Banking Department. The aim of the CBS was to provide technical aid to developing countries in the field of banking and central banking. It played a significant role in promoting the developmental norm of central banking and its members engaged in providing it with a solid economic-scientific ground without sharing the views of the IMF’s executive organs.

Deena Khatkhate, the director of the CBS, was an Indian-American economist who was previously the Director of Research at the Reserve Bank of India. Though mindful of the risks involved in the use of selective credit policies, Khatkhate supported them. He rejected the claim that there is an “automatic link between inflation and selective credit controls” and was convinced that selective credit policies “if properly designed and executed, strengthen the process of financial intermediation by improving its allocative aspects”. Therefore, “[o]n balance, selective credit policies have greater chance to succeed in less developed countries than in the developed ones” (Khatkhate/Villanueva 1978: 988).

Within the CBS, the common belief was that structural conditions in developing countries were unique and, therefore, standard economic policies would be ineffective in these countries. Yung Chul Park, a researcher at the CBS who later became the president of the Korean Development Institute, argued that “the differences in structural characteristics and institutional elements between advanced and developing countries are so extensive that any straightforward application of the models of advanced countries to developing countries would be grossly unrealistic” (Park 1980 [1973]: 675). Vinayak Vijayshanker Bhatt, who was an economist in the Research Department of the Federal Reserve Bank of India, a manager at the Industrial Development Bank of India, an economist at the Asian Institute for Economic Development, and finally an economist at the World Bank (Bhatt 2009), argued that “[t]he role of the Central Bank [in developing countries] has to be conceived in the context of evolving a sound financial infrastructure conducive to rapid development, [that is, the] efficient mobilization of savings” and the “allocation of resources consistent with development objectives” (Bhatt 1974: 64).
To be more precise, the developmental and the liberal/European norm did not directly compete. By the 1960s, orthodox economists also acknowledged that developing countries differ greatly from developed countries. However, the orthodox economists believed that the financial problems of developing countries would be best solved by liberalizing financial systems. From the 1950s through the 1970s, a small group of economists promoted the liberalization of financial systems in developing countries. John Gurley, Edward Shaw and Ronald McKinnon were three prolific writers who are quoted in any debate on the matter (Gurley/Shaw 1955, 1956, 1966; Shaw 1973; McKinnon 1973). In later years, Maxwell Fry joined the group (Fry 1978, 1982, 1988).

The key argument promulgated by these economists was that the financial problems of developing countries arose primarily from endogenous rather than exogenous factors. Indeed, developing economies are characterized by unique and underdeveloped financial systems. However, government policy only aggravates these problems rather than solving them. The economists further argued that the only way to solve these problems is by liberalizing domestic financial systems.

In order to evaluate the legitimacy of the two norms, we can compare the journals in which each community of experts published its articles (Table 4). The table shows that a large number of economic journals published articles from both groups and it implies that both norms enjoyed scientific recognition.

<table>
<thead>
<tr>
<th>Orthodox economists</th>
<th>Both orthodox and developmental economists</th>
<th>Developmental economists</th>
</tr>
</thead>
</table>

Source: Author’s Illustration

8. Regional Institutions in Asia

The idea that the central bank should play a significant role in allocating resources was institutionalized not only on the international level, but also in the discourse of regional institutions. In this paper, I focus on the Asian case and examine the adoption of the developmental norm by Asian regional organizations. I discuss three regional organizations: the South East Asian Central Banks (SEACEN), the UN Economic Commission for Asia and the Far East (ECAFE) and the Asian Development Bank (ADB).
In 1967, at the second Annual conference of the ASEAN, the governor of the Philippines’ central bank initiated the establishment of a Regional Center for Monetary Studies, which later turned into the SEACEN that included the central banks of Ceylon, Indonesia, Laos, Malaysia, Nepal, the Philippines, Thailand, Vietnam and Singapore. The idea was inspired by the Latin American Centro de Estudios Monetarios Latinoamericanos (CEMLA). The Research Center served as a training center of central banking personnel and for research about central banking issues unique to the Asian countries. The Director of the SEACEN thus explained it:

“[B]ecause most countries in the region are mainly agro-based economies sharing the developmental goals of balanced economic growth, the training course should include in its scope the role of policy makers in both the public and private sectors at mobilizing and channeling resources towards the objective of balanced economic growth” (Valdepeñas et al. 2007: 26).

Moreover, the SEACEN was a regional forum in which the South East Asian voting groups coordinated their votes in international financial organizations (Valdepeñas et al. 2007: 2). They were thereby able to increase their bargaining power.

Another regional institution that operated in the 1960s was the ECAFE, which was used as a transnational regional forum for coordinating the shift from policies of import-substitute industrialization (ISI) to export-oriented industrialization. To that end, the Asian countries aimed at promoting intra-regional integration (UNECAFE 1964a). While the European model was cited as an inspiration, there was consensus among experts and policymakers that the European model of integration could not be adopted and was ill-suited to the Asian region. Liberalization of the flow of goods and capital did not serve the national purpose of the Asian countries. Therefore, while the Asian policy makers used the term ‘coordination’, the term meant something different than in the European model.

The Executive Secretary of the ECAFE adhered to the belief that developing countries, especially the small ones, would be unable to extract the full benefit of the liberalization of trade “unless they undertake joint efforts to accelerate their economic and industrial development” (UNECAFE 1964a: 11). The Report of the Expert Group asserted that at the outset, experts recognized that “if the full benefit of trade liberalization measures were to be realized, it was important to aim at an increasing measure of co-ordination of investment plans in industry, mining and agriculture”. Rather than eliminating economic planning, the experts recommended that each country “should take into account the development programmes of other countries” (UNECAFE 1964b: 48). As the Japanese delegate stated very clearly, integration and liberalization were not ends in themselves, but rather a means to support import-substitutions and the expansion of export. “The prerequisite for such an achievement is the mutual co-ordination of development plans” (UNECAFE 1964a). The representative of Thailand expressed a more cautious view regarding the success of regional integration of the ECAFE countries. He specifically referred to the “methods of economic co-operation applied in Western Europe” and portrayed them as not being “suitable or relevant to the conditions of the ECAFE region” (UNECAFE 1964a: 42).

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4 The Experts Group that prepared a report for the Conference on Asian Economic Cooperation included the French representative to the European Communities and the Head of the Latin American Commerce Department (UNECAFE 1964b: 73).
Robert Triffin, who was invited to organize the Seminar on Financial Aspects of Trade Expansion in the context of the plans of an Asian Payment Union, reaffirmed the developmental norm: “Free — or even simply freer — trade commitments are [...] not negotiable in practice without supporting [...] financial and internal policy commitments’ (Triffin 1968: 87). Moreover, liberalization and integration “are means to an end, and are justified only when their benefits [...] exceed their cost, i.e., the bridling of the freedom of choice by individuals or groups, and the administrative and political complexities needed to reach and implement joint decisions” in national contexts (Triffin 1968: 87). Therefore, during the postwar period, the developmental norm provided legitimacy for developing countries to use policy practices that deviated from liberal-European practices.

The third regional institution important in this context is the ADB, established in 1966 by the ECAFE members to “foster economic growth and co-operation in the region of Asia and the Far East... and to contribute to the acceleration of the process of economic development”. The ADB agreement defined the bank’s function as promoting “investment in the region of public and private capital for development purposes” and to give priority to “those regional, sub-regional as well as national projects and programmes which will contribute most effectively to the harmonious economic growth of the region as a whole” (ADB 1966).

Hence, the discourse that characterized the three regional organizations suggests that the Asian countries consciously, deliberately and collectively promoted a developmental norm that rejected the liberal/European norm. The Asian countries did not create the developmental norm from scratch. Rather, it was a process of policy translation. Whereas the European model was used as an aspiration, policy makers and central bankers on the regional level believed that the European model was ineffective in the Asian context.

9. The Demise of the Developmental Monetary Norm

So far, the article traced the consolidation of two distinct central banking norms, which I labeled the liberal/European norm and the developmental norm. In the 1980s, due to geopolitical and ideational factors, a process of convergence took place and the liberal/European norm was globalized.

In the late 1970s, the IMF changed its passive attitude towards developing countries and started to promote market-based central banking ideas in the peripheral regions. The doctrine of financial repression promoted by Gurely, Shaw and McKinnon was adopted by IMF economists and became the basic theoretical foundation of policy advice to developing countries. The reports of the Asian Department at the IMF acknowledged that “[a]ll SEACEN central banks have some refinancing program for reallocating credit”. However, the economists of the department argued that the allocation of credit policies were ineffective because credit spilled over to other borrowers and eventually “if controls become all pervasive the financial system becomes distorted and repressed” (Narvekar et al. 1979).

The discursive change regarding central banking norms can be demonstrated by the change within the IMF and specifically at the Central Banking Department. The Department hired economists that acquired
their academic credentials in the US. Warren Coats, who was Milton Friedman’s graduate student at the University of Chicago, came to the Central Banking Department in 1977, where he became active in promoting a move within the Department towards market-based allocation of resources in developing countries. He worked with Deena Khatkhate, who was the director of the Department.5

A milestone in this process was the publication of an edited volume by Coats and Khatkhate (Coats/Khatkhate 1980). This publication represents the transition point from the developmental to the European/liberal approach of the Central Banking Department towards central banking in developing countries. Coats and Khatkhate embraced the financial repression thesis of Gurely, Shaw and McKinnon. The “old and fierce battles between the structuralists and monetarists”, they announced, became “faint memories of a distant past” The new consensus was that developing economies should also liberalize their financial systems (Coats/Khatkhate 1979: 1897). On the basis of “the unsavoury experiences of the ravages of inflation that have afflicted a large number of them [LDC]”, the practice of selective credit policies was abandoned (ibid). Coats and Khatkhate adopted the liberal narrative according to which state intervention was part of the problem rather than part of the solution. The problems of developing countries stem from “the rigidities in the production structure in LDCs, and the imperfections of all markets” (ibid). In the following years, as the debt among developing countries grew, the IMF had a growing leverage to exert conditionality pressure to liberalize the financial system and adopt the liberal norm of central banking (Boughton 2001). Eventually, the Asian financial crisis in the late 1990s provided the IMF with an opportunity or an excuse to enforce liberalization on the East Asian countries.

10. Conclusion

The aim of this paper was to identify and trace two regional central banking norms that prevailed in the period from the 1940s to the 1970s. Each norm was characterized by its content and by the network that secured its continuity and internationalization. The liberal monetary norm prescribed liberalization of financial systems, free flow of capital and independent central banks, which emerged in the European context. It was promoted among European central banks by the Bank of England, the BIS, the Bundesbank, the OEEC (OECD) and the IMF. The paper showed that this norm prevailed within these institutions despite the global trend that was manifested in the Bretton Woods regime.

The developmental central banking norm emerged in Latin America. It was uploaded to the international level by Fed experts, who were more receptive to ideas of banking regulation and more skeptical regarding the stabilizing role of market forces. The Fed’s experts subsequently downloaded the new blueprint to the newly established developing countries in East Asia. The developmental model was embraced by local actors as fitting the type of economic problems they faced, as well as their authoritarian political culture. The developmental norm was concurrently legitimized by American and Asian economists in the American policy discourse in academic venues and international organizations.

This paper identified key milestones in the life cycles of two norms, thereby leaving open questions for further research. Two questions are particularly important for closing the gaps in the arguments presented in this paper. First, to what extent were there intra-regional variations in terms of adoption of each norm? Second, to what extent did the liberalization period eliminate the developmental norm? These questions await further research.
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- Identity and the Public Sphere
- Compliance, Conditionality and Beyond
- Comparative Regionalism and Europe’s External Relations