



CAGE Brussels Podium

Designing a Central Bank for The 21st Century Eurozone

On Monday 10th February CAGE hosted a debate at the University of Warwick Brussels Office on 'Designing a Central Bank for The 21st Century Eurozone'.

The ongoing financial crisis in the Eurozone has focused attention on designing central banking institutions that promote sustainable economic growth, high employment, stable public finances, and financial stability.

However, debates over the direction of monetary policy and responses to sovereign debt and banking crises point to the challenges of balancing national interests with pan European or

Eurozone objectives. Recent research on institutional design sheds new light on these trade-offs and provides lessons for how European monetary policymaking and bank supervision might look in the twenty-first century.

CAGE researchers, Professor Kris Mitchener and Dr Michael McMahon, discussed the issues around a European Banking Union in the Eurozone in front of an audience of European policy makers.

Professor Mitchener discusses the tensions that are built into the emerging European banking union and how other countries have confronted similar challenges in the past.

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Professor Mitchener



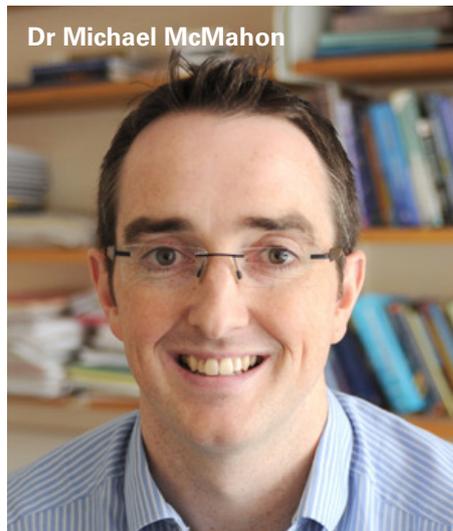
Lessons from History for the European Banking Union

In the context of recent announcements about a banking union in the Eurozone, what does history have to tell us about creating bank supervisory institutions in response to crises? The experience of the United States provides a reasonable historical analogy for understanding how economic states gradually ceded control of supervisory institutions to union-wide agencies. Much as in Europe, each American state had initially developed its own regulatory and supervisory system with the legal right to charter banks.

A survey of the facts suggests Europe's accelerated approach differs from the US case. It took more than a century for modern supervisory institutions focused on systemic stability and depositor welfare to emerge in the U.S., and close to 150 years for two of the pillars (a common supervisory agency and deposit insurance) to emerge at the federal level. In the U.S., institution building at the federal level moved slower than present-day Europe for several reasons: (1) capital markets were less integrated and cross-border banking was limited and (2) banks were initially note issuing entities rather than deposit taking. By contrast, what Dirk Schoenmaker and Sander Osterloo call the "financial trilemma" – the incompatibility between national bank regulation and supervision, capital market integration, and financial stability – presented itself sooner in Europe, creating pressure to reform.

There are several lessons Europe can take from the U.S. experience:

- Maintaining a fragmented supervisory system was unsuccessful
- Federal deposit insurance had a calming effect on the immediate situation
- Winding up banks does not imply a "standing fund"
- Design stress tests to avoid market stigma of recapitalisation funding
- Agency specialisation allows for speedy resolution
- Backstops can be designed to adjust to the size of future crises
- Common resolution was not instantaneous



Dr Michael McMahon

Dr Michael McMahon explains how the size and composition of central banks' policy committees influences the performance of monetary policy and how the relative "transparency" of committee decision making improves the preparation of participants.

The Who and the How of Monetary Policy Institutions

Expert committees within independent central banks are the dominant institution for setting monetary policy throughout the world. By 2000, 79 of 88 central banks surveyed by the Bank of England used committees to decide interest rates. For example, committees are used at the European Central Banks (ECB), United States Federal Reserve (Fed) and the Bank of England (BoE). But different central banks make use of different committee structures. Although there is a broad consensus on the merits of monetary policymaking by independent committee rather than by politicians, many questions of central bank design remain.

Committees outperform individuals because they pool the views of lots of individual experts on the state of the economy, allowing the committee decision to better reflect economic conditions.

By appointing sufficiently expert committee members, the research finds, the committee does not need to be that large; a committee of between 5 and 7 is typically large enough to reap the gains of pooling information while avoiding the costs of deliberation and communication that come in larger committees.

There is little evidence to support the appointment of external experts (as used by the BoE).

Research does find evidence consistent with reputation signalling. Inherently more hawkish MPC members are less affected by such signalling. Nonetheless, signalling does not change the hawkish ranking of members.

While many people argue that transparency of decision making is necessary for reasons of democratic accountability, the concern is that it stifles discussion and deliberation. McMahon's research finds that transparent discussion improves incentives for committee members to accumulate information before they meet. While they are also somewhat less dynamic in their discussions, the added information effect likely dominates.

This is a summary of the event on 10th February. The presentations were followed by a lively debate with: Mr Olivier Debande – Senior Economist, European Investment Bank, Mr Philippe Legrain – Principal Adviser, Head of the BEPA Analysis Team, European Commission, and Mr John Berrigan – Director of Financial Stability and Monetary Affairs, DG Economic Development, European Commission.

To learn more about the event and the research it showcased please visit the [CAGE website](#).

Welcome to...

Media Fellow:

Lindsay Whipp, Global Economy News Editor at The Financial Times, will visit CAGE in March. Previously Lindsay worked on the world desk focusing on online coverage and before that she was Technology, Media and Telecoms News Editor. Between 2008 and 2012 she was Tokyo Correspondent covering markets, and also economy, and was on the ground covering the earthquake and tsunami in the north of the country during and in the aftermath of the disaster. Lindsay has also worked at Bloomberg where she was based in Tokyo covering economy, policy, automakers and the trading companies. Lindsay has a B.A. in Social Anthropology from the University of Manchester and a Masters degree in gender and development from Ochanomizu University in Tokyo.

Policy Fellows:

Stevan Lee is Senior Economic Adviser and Team Leader on Growth Research in The Department for International Development's (DfID) Research Division. Stevan will visit CAGE in March as a Policy Fellow. He has an economics PhD and has worked for 20 years in the development field, mostly in DfID but also with HM Treasury and The World Bank. He has extensive overseas experience especially in East Africa, but also in fragile states like Sierra Leone and Iraq. His current focus is research on urbanisation and development; on institutions and the political economy of development; in the conditions for and conditions of firms in developing countries; and in the skills-labour market nexus in African countries.

Loga Gnanasambanthan, will also visit CAGE in March as a Policy Fellow. Loga is a development economist with more than 15 years' experience, including working on DfID country programmes (Iraq, Rwanda and India) and as an ODI Fellow in the Solomon Islands. She currently works on World Bank issues, including the recent IDA 17 negotiations. Over the coming year her focus will be on the new World Bank Strategy, in particular the Bank's financial and risk management and the long term vision for the World Bank and its concessional finance arm, IDA. She has a Masters in Development Economics from the University of East Anglia and Bachelor's degree in Philosophy, Politics and Economics from Oxford University.

Congratulations to:



Arthur Blouin, one of our PhD students, on obtaining an Assistant Professorship at the University of Toronto. This is an excellent placement for Arthur and he deserves our hearty congratulations.



Sanchari Roy, Postdoctoral Fellow at CAGE, who has been appointed Assistant Professor of Economics at the University of Sussex.



Sascha O. Becker who has been appointed to the Economic Policy (Journal) panel for the next two years.



Dennis Novy, who has received the 2013 Best Article Award from Economic Inquiry magazine for 'Gravity redux: Measuring International trade costs with panel data'.

Lottery winners research makes global headlines



February saw a global media frenzy around **Andrew Oswald** and **Nick Powdthavee's** new research into UK lottery winners' political fickleness. The study, which found that British lottery winners tended to switch their political support to a more right-wing party and become less egalitarian, made headlines around the world,

being featured online, on air and in print in Australia, Russia and the US as well as in the UK. The research paper 'Does Money Make People Right-Wing and Inegalitarian? A Longitudinal Study of Lottery Winners' by Nattavudh Powdthavee and Andrew J. Oswald is available on the CAGE website.



As good as it gets?



Eugenio Proto and Aldo Rustichini's new research into national happiness sparked a whirlwind of media interest with the study making headlines around the world, and Eugenio making an appearance on a number

of radio channels, including BBC Radio 4 and BBC Radio 5 Live.

The study findings show that there is a 'sweet spot' of satisfaction at £22k GDP per capita (as per the UK), beyond which point happiness levels begin to dip as aspiration kicks in. Dr Proto said: "As countries get richer, higher levels of GDP lead to higher aspiration. There is a sense of keeping up with the Joneses as people see wealth and opportunity all around them and aspire to having more. But this aspiration gap – the difference between actual income and the income we would like – eats away at life satisfaction levels. In other words, what we aspire to becomes a moving

target and one which moves away faster in the richest countries, causing the dip in happiness we see in our analysis."

The full paper 'A re-assessment of the Relationship between GDP and Life Satisfaction', by Eugenio Proto and Aldo Rustichini, can be found on the CAGE website.



A Win for Blacks and Whites?

The Economics of the Civil Rights Revolution in the American South

22 January 2014
University of Warwick

CAGE was delighted to welcome Gavin Wright, Professor of American History at Stanford University, who gave a special public lecture on the economics of the US civil rights revolution.

The Civil Rights movement in the American South was a struggle for justice – including economic justice. The famous bus boycotts and lunch counter sit-ins demanded equal access for black southerners; they also raised demands for jobs in the same places where black people were refused service. The Civil Rights Act of 1964 and the Voting Rights Act of 1965 began a period of enforced desegregation, and southern blacks gained dramatic improvements in job opportunities, quality of education, and health care. Yet black advances did not come at the expense of southern whites. The Civil Rights struggle, Wright argues, was that rarest of social revolutions: one that benefitted both sides.

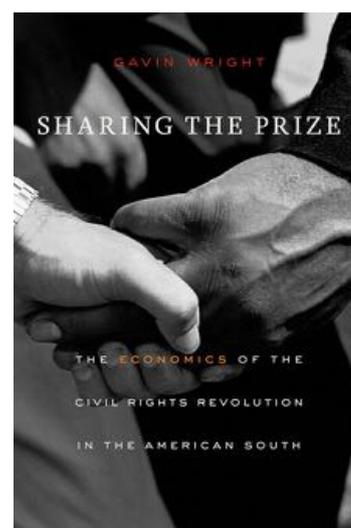
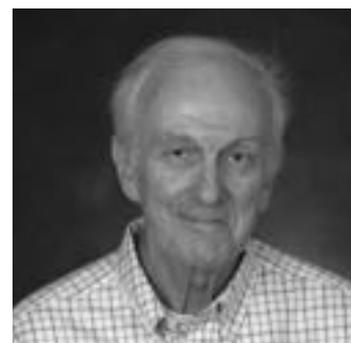
In the lecture Professor Wright shared the findings from his research which undermine beliefs that discrimination was irrational, that government intervention was unnecessary, and that segregation would gradually disappear once the market was allowed to work.

He also explained why white southerners long defended a system that failed to serve their own best interests. Professor Wright's research makes it clear that the material benefits of the civil rights acts of the 1960s are as significant as the moral ones.

Professor Wright's lecture was based on his new book *'Sharing the Prize: The Economics of the Civil Rights Revolution in the American South'*, published by Harvard University Press.

Gavin Wright is William Robertson Coe Professor of American Economic History at Stanford University and a former President of the Economic History Association.

We were pleased to be joined by students and staff from across the University in this lively lecture and question and answer session.



New CAGE-Chatham House Policy Briefings

We have recently added new papers to our policy briefing paper series which is published in partnership with Chatham House. The series aims to advance key policy debate issues of global significance. To see more in the series please visit our website.



The Power of Political Voice: How Women in Politics can Help Tackle Gender Crime

Anandi Mani, March 2014

Dr Mani argues that crime against women is a persistent, even growing, problem in many developing countries. In India, research suggests that having female political representatives can empower women in the battle against gender crime.

Dr Mani shows that that having more female political representatives results in higher rates of documented crimes

against women, but that this reflects the fact that a greater number of gender crimes are being reported, as victims are more willing to come forward because they anticipate they are more likely to be heard. Dr Mani also argues that police responsiveness to documenting and dealing with gender crime is higher in areas with female politicians.



Human Development as Positive Freedom: A World View Since 1870

Leandro Prados de la Escosura, February 2014

In this paper Professor Leandro Prados de la Escosura argues that substantial gains in world human development have been achieved since 1870, but research shows that the main improvement actually occurred between World War I and 1970.

Despite initial successes in lifting human development, the socialist experiments of the 20th century failed to sustain momentum and then (with the exception of Cuba) stagnated and fell behind prior to the socialist model's ultimate demise. Since 1970, while most OECD countries have experienced a second (later life) health transition, all developing regions have fallen behind in this dimension.



PhD Macroeconomics Workshop: Recent Developments in Money, Macroeconomics and Finance

31st March - 1st April 2014
University of Warwick

Together with colleagues at the University of Warwick and the Bank of England, the Money Macro and Finance group, MMF, are launching an annual workshop for UK-based PhD economists in the broad fields of money, macro and finance.

The main objective of the workshop is to provide advanced PhD economists, about to go on the job market, an opportunity to present

their research to their peers and leading researchers in the field in order to obtain feedback and practice the presentation of their key research ideas. An added bonus is that it allows for some early dissemination of these ideas across the research and policy-making community. As well as senior academics, the conference will be attended by economists from the Bank of England and H M Treasury.



This event is sponsored by the Money, Macro, Finance Group, CAGE, Warwick Business School and the Bank of England.

Education, Human Capital and Labour Market Outcomes

The University of Warwick in Venice,
Palazzo Pesaro Papafava

16th - 17th May 2014

Organised by:
Sascha O. Becker, Mirko Draca,
Victor Lavy and Fabian Waldinger

This CAGE workshop brings together experts on education and labour economics from North America and Europe to discuss their latest research findings on Education, Human Capital and Labour Market Outcomes.

For further details please see our website.



Working Papers

CAGE publishes a series of working papers available online: go.warwick.ac.uk/cage

Recent papers include:

Walk the Line: Conflict, State Capacity and the Political Dynamics of Reform

Authors: Sanjay Jain, Sumon Majumdar and Sharun Mukand
No. 156/2013

This paper develops a dynamic framework to analyse the political sustainability of economic reforms in developing countries. The authors demonstrate that economic reforms that are proceeding successfully may run into a political impasse, with the reform's initial success having a negative impact on its political sustainability. The authors also demonstrate that greater state capacity, to make compensatory transfers to those adversely affected by reform, need not always help the political sustainability of reform, but can also hinder it. Finally, the authors argue that in ethnically divided societies, economic reform may be completed not despite ethnic conflict, but because of it.

Eurozone Sovereign Debt Restructuring: promising legal prospects?

Authors: Marcus Miller, Dania Thomas
No. 144/2013

The Eurozone debt crisis has stimulated lively debate on mechanisms for sovereign debt restructuring. The immediate threat of exit and the breakup of the currency union may have abated but the problem of dealing with significant debt overhang remains. After considering two broad approaches - institutional versus contractual - the authors look at a hybrid solution that combines the best of both. In addition to debt contracts with Collective Action Clauses, this includes a key amendment to the Treaty establishing the European Stability Mechanism, together with innovative state-contingent contracts and a Special Purpose Vehicle to market them.

Believing in Oneself: Can Psychological Training Overcome the Effects of Social Exclusion?

Authors: Sayantan Ghosal, Smarajit Jana, Anandi Mani, Sandip Mitra, Sanchari Roy
No. 152/2013

This paper examines whether psychological empowerment can mitigate mental constraints that impede efforts to overcome the effects of social exclusion. Using a randomised control trial, the authors studied a training program specifically designed to reduce stigma and build self-efficacy among poor and marginalised sex workers in Kolkata, India. They find positive and significant impacts of the training on self-reported measures of efficacy, happiness and self-esteem in the treatment group, both relative to the control group as well as baseline measures and also higher effort towards improving future outcomes as measured by the participants' savings choices and health-seeking behaviour, relative to the control group. These findings highlight the need to account for psychological factors in the design of anti-poverty programmes.

CAGE Seminar Series

CAGE holds a weekly Tuesday seminar in the Department of Economics at the University of Warwick.

External speakers are invited to give a seminar focusing on an applied microeconomics topic.

Seminar speakers for the Spring Term are:

18 February 2014

Johannes Haushofer, MIT. *'Household Response to Income Changes: Evidence from an Unconditional Cash Transfer Program in Kenya'*

25 February 2014

Oriana Bandiera, Professor of Economics, LSE. *'Recruiting for the state: the selection effect of career incentives on performance'*

4 March 2014

Luigi Guiso, Professor of Finance, Einaudi Institute for Economics and Finance. *'Time Varying Risk Aversion'*

11 March 2014

Suresh Naidu, Assistant Professor of Economics and Public Affairs, Columbia University. *'Worker Mobility in a Global Labour Market: Evidence from the United Arab Emirates'*

22 April 2014

Rick Hornbeck, Associate Professor of American History, Department of Economics, Harvard.

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