

Regional Monetary Policy

Carlos J. Rodríguez-Fuentes

Routledge Studies in the Modern World Economy



Regional Monetary Policy

With the final phase of the European Monetary Union under way concern has been raised over the regional implications of the European Central Bank's (ECB) Monetary Policy. Departing from the standard approach utilized by the ECB, this book provides a comprehensive theoretical framework to explore the ways through which money and monetary policy may affect regions.

Regional Monetary Policy examines the role that the banking system and the liquidity preference of economic agents play in the transmission of central banks' monetary policy decisions to regions within a country or countries within a currency union. This book utilizes a unique framework built upon the basic principles of the Post Keynesian monetary theory which enables the identification of a new way for money and monetary policy to have a regional impact: the behavioural effect.

This book will prove essential reading for all students of economics and politics as well as readers interested in the development of the European Union.

Carlos J. Rodríguez-Fuentes is 'Profesor Titular de Universidad' in the Department of Applied Economics at the University of La Laguna, Canary Islands, Spain.

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This book is dedicated to Sara, Diego and Eva

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Foreword

We are delighted to be invited to write the Foreword to this volume. It brings together and extends Carlos Rodríguez-Fuentes's important and innovative work on regional finance and the differential regional impacts of monetary policy.

The contribution this book makes to our understanding extends beyond the specifically regional field. Carlos makes a much more general contribution by developing fully a Post Keynesian account of money and banking and the mechanism by which monetary policy is transmitted through the banking system. The contrast between the Post Keynesian approach and the more conventional money-macro approach is drawn out in the discussion of monetary policy. The conventional approach assumes that money is under the control of the monetary authorities, while the Post Keynesian approach stresses the active role of the banking system in the creation of money. This challenges the whole idea of thinking of monetary policy in terms of exogenous shocks.

The realism of the analysis is grounded in its application to regional economies, both within and among nations. Until recently, regional economics had been treated as of minor importance within the discipline. But, since the introduction of the euro, regional economics has enjoyed much broader application and has drawn more extensively on monetary and macroeconomic theory.

In the application to the impact of monetary policy on different regions, the role of the banking system becomes even more clear. Banks exercise their power over credit creation differentially, depending on their perceptions of region-specific risk and growth potential. But this power also depends on the stage of development of the banks concerned. Within nations, small firms in particular regions may be dependent on borrowing from local banks with less credit-creating capacity than national banks. Even more clearly, national banking systems may be at different stages of development, as well as having differing conventional behaviours, something which is very apparent within the euro-zone. This translates into a variable regional impact of monetary policy. Until recently, the subject of regional finance has been comparatively underdeveloped. But now the political importance of the euro has prompted a significant research agenda, which has almost exclusively drawn on conventional money-macro theory and competition theory. This book provides an important counterweight to this body of research, opening up another perspective, and one which we feel is both closer to the real operations of the banking system and accordingly more fruitful.

Regional analysis is normally dogged by data availability problems, which impede effective empirical analysis. Carlos's work provides some rare examples of econometric analysis of the regional impact of monetary policy for the euro-zone, Spain and the US, where regional data are less scarce. Again the analysis is all the more effective for being accompanied by a critical analysis of the extensive body of empirical work based on the conventional money-macro approach.

We feel personal pleasure in being involved in Carlos's book in this way, for he is someone we admire as a creative and careful thinker, and value greatly as a colleague and friend.

Sheila Dow and Victoria Chick
Dunblane, 27 November 2004