

BANCO DE ESPAÑA

FUNCTIONS OF THE BANCO DE ESPAÑA: AN HISTORICAL PERSPECTIVE

Miguel Pellicer

SERVICIO DE ESTUDIOS
Documento de Trabajo nº 9330

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1. INTRODUCTION

The legal provision authorising the nationalisation of the Banco de España was enacted in 1962 ("Ley de Bases de Ordenación de Crédito y de la Banca"). The preamble to this act, commendable in many respects, summarises the Banco de España's previous history: "The central issuing bank's earliest forerunner was the Bank of San Carlos, created in 1782 and subsequently re-named San Fernando following merger with the Bank of Isabel II. It was converted into the Banco de España pursuant to the first General Banking Act of 1856. Since the Decree dated March 19th 1874, the Banco de España has uninterruptedly enjoyed the privilege of issuing banknotes in its joint capacity as State's banker and commercial bank. However, it has not evolved into the bankers' bank, the central regulator of the credit mechanism and the agency responsible for the external value of our currency".

The Banco de España was thus one of the last European central banks to begin to assume many of the functions characterising these institutions. However, since 1962, its transformation into a central bank in the full sense of the term has proceeded apace; indeed, it has assumed functions not habitually performed by its counterparts. For example, it is unusual for a central bank to be involved to the extent the Banco de España is in the fields of supervision (all credit institutions), the organisation of financial markets (the money and government debt markets), payment systems (Money Market Telephone Service), the book-entry system for government debt trading and the National Electronic Clearing System.

To review the functions attributed to the Banco de España it was deemed preferable to address each such function separately rather than follow a principle based on chronological order. This criterion is debatable in view of the strong historical and conceptual relation among almost all the functions. But it was selected as it was considered to offer greater clarity, albeit at the expense of a good deal of repetition.

To classify the various functions, however, a chronological order was chosen, observing the dates at which the Banco de España began to perform such functions rather than discussing them according to their current

significance. This has not prevented greater attention being accorded to those functions of the Banco de España considered most important or specific.

These criteria account for the structure (after the initial brief chronicle in section 2) of most of this paper, which concludes with an overview of how the Banco de España's independence has developed and the ways in which and to whom the bank is accountable.

2. CHRONICLE

- 1782 Creation of the National Bank of San Carlos.
- 1829 Transformation into the Bank of San Fernando.
- 1847 Merger with the Bank of Isabel II, giving rise to the New Spanish Bank of San Fernando.
- 1856 Re-named Banco de España, operating in competition with other issuing banks.
- 1868 The peseta emerges as the basic unit of account in the Spanish monetary system.
- 1874 The Banco de España is accorded the privilege of issuing banknotes.
- 1883 End of the convertibility of banknotes into gold.
- 1898 Decoupling of the maximum amount of banknotes issued from the Banco de España's capital.
- 1913 Banco de España acts as lender of last resort for the first time.
- 1921 First General Banking Act. The Banco de España's conduct in the foreign exchange markets and as the bankers's bank is regulated.

- 1931** Greater public presence in the Banco de España. The setting of interest rates and exchange rate policy become subject to the authority of the Ministry of Finance.
- 1939** End of ratio of metallic reserves to the issue of banknotes.
- 1946** Second General Banking Act. Reinforcement of public presence in the Banco de España and its role as the bankers's bank.
- 1962** Nationalisation of the Banco de España and redefining of its functions, which include banking supervision.
- 1971** Savings banks and credit co-operatives become subject to supervision by the Banco de España.
- 1973** Centralisation of foreign reserves at the Banco de España, which assumes responsibility for the implementation of exchange rate policy.
- 1974** Pursuance for the first time of an active monetary policy, via monetary regulation loans. The interbank deposits market emerges.
- 1976** The Money Market Telephone Service for the dematerialised settlement of large-value transfers and interbank loans is created.
- 1977** Banco de España is authorised to intervene at crisis-ridden entities. Creation of the Deposit Guarantee Funds.
- 1980** Act laying down the Banco de España's status and scope (Ley de Organos Rectores del Banco de España) is passed, strengthening its independence and redefining its functions.
- 1987** Banco de España responsible for regulating the National Electronic Clearing System. Creation of the Book-Entry Government Debt Market, with Banco de España assigned as governing, clearing and settlement agent. The first rules on operating transparency and

banking services are laid down and the Client Claims Service, attached to the Banco de España, is created.

1988 Legislation covering the discipline of, and intervention at, credit institutions is passed, whereby all credit institutions become subject to supervision by the Banco de España.

1990 Open market operations replace monetary regulation loans as the main instrument of monetary intervention.

1993 Draft legislation on the independence of the Banco de España.

3. STATE'S BANKER

Two different fields may be distinguished in a central bank's role as State's banker. The first encompasses financial services and includes the provision of cash management services, i.e. the administration of domestic and external proceeds and payments on the State's behalf, and the servicing of government debt, i.e. services relating to its subscription, conversion, redemption and payment of interest thereon. The second concerns the direct or indirect extension of financing to the State.

The function of State banker is inextricably linked to the history of the Banco de España, from its earliest forerunner to the more recent past. The provision of services, strictly speaking, never caused serious difficulties and was an important source of profits; but State financing is at the root of most of the problems experienced by the Banco de España. To address these, three historical periods can be distinguished:

3.1 First stage (1782-1898): direct financing

The first direct precursor of the Banco de España was the Banco Nacional de San Carlos, which was created in 1782 with share capital totalling 300 million reales.

Pursuant to its functions of "combating usury" and "facilitating trading transactions", it directly entered into business, extended loans and discounted bills. However, the basic reason for its creation was to provide treasury services to the State and to service the latter's reales-denominated certificates, which comprised government debt issued to alleviate the revenue shortfall caused by the discontinuation of precious metal shipments from the American colonies. There was a 4% annual return on these certificates, which were also used as means of payment before the State and in wholesale transactions between individuals.

The endless wars waged during this period led to heavy increases in public indebtedness to the Banco Nacional de San Carlos. Such indebtedness was both direct and, above all, related to the inability of the Treasury to convert into gold the reales-denominated certificates into which the Bank had previously converted holders' money. This led first, to the inoperativeness of the Bank and, subsequently, to its disappearance; as from 1800, virtually all its assets consisted of government debt which was never repaid, and interest thereon was either paid late or not at all.

In exchange for this debt, the shareholders of the Banco Nacional de San Carlos received 40 million reales in 1829 (almost eight times less than the accumulated debt). This amount constituted the effective capital of a new bank: the Banco Español de San Fernando. The regulation and role of this bank saw no significant progress towards a more modern conception of the functions of a central bank.

Although the bitter experience of its predecessor meant an extremely prudent policy was first pursued, the Banco Español de San Fernando was unable to evade the pressure exerted on public borrowing requirements by the Carlist civil war. Once more, the Treasury became the Bank's principal client. This meant that the 1847 crisis scarcely affected it, though it had to bear the problems of the Banco de Isabel II following the unfavourable merger that year, which gave rise to the Nuevo Banco Español de San Fernando.

With difficulties at a height, there was an attempt in 1849 to apply the Peel Act to the new bank by segregating the issue and operations departments, but the experience lasted only a few months. A period of two decades then ensued

in which the role as lender to the State was relatively insignificant: first, because of the Bank's own need to restore its financial health; and further, due to the prosperity enjoyed by the Spanish economy after 1856, when the Banco de España took its current name.

With further civil wars and insurrection by the last American colonies, the financial difficulties of the Treasury resurfaced after 1870. The situation was so serious that, in 1874, the State conferred on the Banco de España the exclusive privilege to issue banknotes in exchange for a loan of 135 million pesetas.

In the historic preamble to the decree-law implementing this measure, the author and subsequent Nobel prize-winner for literature, J. Echegaray, revealed his literary genius: "With credit run down by abuse, taxes depleted by administrative profligacy and amortisation sterilised for the moment, resort must perforce be had to other means to consolidate the floating Debt and to sustain the enormous war expenses which have beset most of our provinces over the past two years. At such a crucial juncture, and yielding to the demands of the present circumstances and to the pressing needs of our struggle, in my capacity as minister, and as resolved by the Council of Ministers, I propose creating under the aegis of the Banco de España and with the help of the provincial Banks a National Bank. This will be a new financial force that will come to the aid of public finances without thereby relinquishing the functions proper to all central banks. The new establishment shall have three main objectives: i) to re-group the immense masses of securities which, as parts broken off the national wealth, are spread asunder and divided as a pledge of multiple operations, and to regenerate them with fresh and sound capital; ii) to take exclusive but discretionary responsibility for the issue of notes and coins, guaranteed at all times by metallic reserves; and iii) to come effectively to the aid of trade, taking the benefits of discounting and issuance first, to the largest possible number of financial centres, and later, as calm is restored nationwide, to all of them. Only through such a concentration of forces may operations be undertaken which, due to their significance, are commensurate with the demands of current circumstances and with the enormity of the expenses involved. And only with the single currency in circulation throughout Spain will an instrument capable of performing such operations be in place. Yet these two major government aims must not overshadow the

ultimate and pivotal mission of all issuing banks, namely the discounting of trade bills".

Thereafter, until the end of the century, meeting public finance needs was once more the main preoccupation of the Banco de España and, therefore, the basic counterbalance of the strong expansion of notes and coins in circulation during that period.

3.2 Second stage (1898-1957): indirect financing of budget deficits

After the end of the American colonial wars in 1898, there was an evident need for a stabilisation plan to contain the monetary growth recorded. The plan, in whose implementation the Banco de España co-operated extensively, was executed rigorously and was a success: the public sector ran surpluses, there was a conversion of government debt from the short to the long term, and unilateral decisions were also taken to defer some redemptions and reduce pacted interest rates. A decade of stability thus ensued, only to be broken first, with the re-emergence of budget deficits in 1908 with the outbreak of the colonial war with Morocco; and further, as a result of the massive gold inflows related to the repatriation of capital from the former colonies and to the trade balance surpluses during the First World War.

The volume of outstanding government debt increased for the first time in 1914, and placement problems arose in the light of the growing rates of inflation. To solve these problems, automatic pledging at the Banco de España at a non-penal interest rate was set in place as from 1917, since the loans extended by the central bank backed by government debt bore a lower interest rate than that on government debt.

The new procedure was a great success both among individuals and, most especially, with banks, which were able comfortably to earn a return on their treasury surpluses with full guarantees of immediate liquidity. As a result, the pledging of public funds increased from PTA 828 million in 1916 to PTA 1,497 million in 1917.

The automatic pledging of government debt at the Banco de España, at the discretion of the holders, would be the means of covering budget deficits over the following forty years, excepting of course the special procedures established during the civil war (1936-1939) by the two Bancos de España which operated separately in this period.

Evidently, the indirect monetisation of government debt prevented any attempt at monetary control by the Banco de España. For this reason, issues with an automatic pledge clause ceased in 1957, as part of the groundwork for the severe 1959 stabilisation plan. This saw the end of the autarchic premises of the post-war years and laid the bases for the following development-oriented decade.

3.3 Re-emergence of budget deficits: 1974-

Following the 1959 stabilisation plan, public finances experienced a period of relative equilibrium. This meant that it was not necessary to issue government debt yielding market interest rates again until 1977.

The limited budget deficits that arose were covered by two procedures. The first was recourse to the Banco de España, since the amount of free advances to the Treasury (confined to 12% of annual budgeted expenditure under the 1962 Decree-Law nationalising the Banco de España) was, instead of being amortised, progressively consolidated at the end of each fiscal year. The second procedure was the issue of government debt at lower-than-market interest rates, particularly via the so-called "certificates of investment", which were placed at banks by virtue of the obligatory investment requirement they had to meet.

The situation changed after 1974 when increasingly bigger budget deficits began to be recorded. Despite the aforementioned resumption in 1977 of government debt issues at market interest rates, the absence of minimally efficient securities markets drastically restricted placements, whereby the financing of much of the rising budget deficits had to be met by the Banco de España.

In an initial stage running to 1983, the Banco de España sought to do this by raising funds from banks at market interest rates via the issue first, of certificates of deposit, and later, of monetary regulation certificates. Financing the Treasury free of charge by raising resources in this way was an unsustainable situation and paved the way for the drastic 1983 measures. In step with the boosting of government debt issues, a special reserve requirement tranche was created bearing lower-than-market interest and amounting to a level of 17% of eligible liabilities⁽¹⁾.

A key factor in normalising this situation was the creation in 1987 of the Book-Entry Government Debt Market. This market allowed the sizable volumes of issues required to finance budget deficits to be absorbed and traded efficiently under market conditions.

With this instrument it was now possible first, to establish in 1989 a timetable for the phasing out of the obligatory Treasury note requirement by end-1992. Second, it was possible in the 1990 Budget to prohibit any increase - measured as of the close of each year- in public recourse to the Banco de España. This constraint enabled the interest-bearing tranche of the reserve requirement to be replaced by Banco de España certificates, with a redemption schedule running to the year 2000⁽²⁾.

Both measures should be seen as preparing the way for compliance with the prohibitions of the Treaty on European Union in the area of public financing by central banks. These have been incorporated in 1993 into the draft legislation addressing the independence of the Banco de España, the wording of which states: "In its relations with the State, other Administrations and Public Agencies, and the entities reporting thereto, the Banco de España shall make no type of advance, allow no overdrafts nor extend any other type of credit facility. The following exceptions shall be made:

⁽¹⁾ In turn, government debt (Treasury notes yielding low interest) became the only asset eligible for the purposes of the obligatory investment requirement on deposit-taking institutions.

⁽²⁾ See Repullo, R., La reforma del coeficiente de caja: una nota técnica. Boletín Económico, April 1990, Banco de España, Madrid.

a) Public-sector credit institutions, which may receive liquidity from the Banco de España under the same conditions as other credit institutions, along -where appropriate- with Deposit Guarantee Funds at credit institutions.

b) Loans and credit extended to international financial agencies of a public nature, such as the International Monetary Fund or the Bank for International Settlements, or managed by these within the framework of international operations.

The Banco de España may not acquire directly from the issuer any form of Government Debt. It may only acquire it in secondary markets for the performance of the functions entrusted to it".

4. ISSUING BANK

There are also three differentiated phases regarding this function.

4.1 Privilege of restricted issue (1782-1856)

From its creation in 1782, the Banco Nacional de San Carlos was authorised to issue banknotes to bearer, although those issued while the Bank remained active had a poor reception among the general public as they were competing (as a means of payment) with the reales-denominated certificates. The latter bore interest of 4% and their price during this phase held at around par. On average, the notes issued by the Bank stood at below 3% of their capital.

The issuing privilege was inherited in 1829 by its successor, the Banco Español de San Fernando. The issuing monopoly referred only to Madrid, but for 15 years no other issuing bank was created⁽¹⁾.

⁽¹⁾ Further to the 1829 Commercial Code, banks could be created on the same footing as any other limited liability company; however, royal authorisation was required to issue currency.

In view of the complaints about the scant issuing activity of the Banco Español de San Fernando at a time of economic recovery, the creation of two new issuing banks was authorised: the Banco de Barcelona and the Banco de Isabel II. The latter was headquartered in Madrid, and the active competition it posed shook Banco Español de San Fernando out of its lethargy⁽¹⁾.

After the merger of both these competitors into the Nuevo Banco Español de San Fernando, two other issuing banks were operating in Spain: the Banco de Barcelona and the Banco de Cádiz, a former branch of the now-defunct Banco de Isabel II. In 1849, the Nuevo Banco's issuing privilege was extended to the whole of Spain, with the exception of Barcelona and Cádiz.

4.2 Numerous issuing banks (1856-1874)

The situation changed radically in 1856 when a new phase of economic prosperity coincided with the liberal government of the so-called "progressive biennium". Under the legislation passed in this period, the Nuevo Banco Español de San Fernando was re-named Banco de España. Moreover, throughout the country numerous banks of two sorts were created: a) issuing banks, one per provincial capital (at one point there were 25), which also discounted bills and extended short-term credit; b) credit companies and deposit and loan institutions specialised in promoting industrial and railway companies, of which at one point there were 35⁽²⁾.

When the meagre return on the railway network became evident in 1864, crisis struck extremely harshly. In the following years the number of issuing banks was cut by half and only two major credit companies managed (precariously) to survive. At this time, in 1868 to be exact, the peseta was adopted as the basic unit of the Spanish monetary system.

⁽¹⁾ Since the "notes-to-bearer" issuing monopoly in Madrid in favour of the Banco Español de San Fernando remained in force, the Banco de Isabel II was issuing "certificates to bearer" with identical features in clear breach of the law.

⁽²⁾ Until the 1867 crisis there were, moreover, so-called draft and banking companies, which could not accept deposits or issue short-term securities.

4.3 Issuing monopoly: 1874-

The Banco de España was finally accorded the issuing monopoly in 1874 as a result first, of the critical financial situation of many of the surviving issuing banks; and further, of the chronic inadequacy of the Treasury, exacerbated by the insurrection in the last American colonies and the fresh outbreak in the Carlist civil war.

Public borrowing requirements reached such a level that José de Echegaray (a liberal and firm advocate of the presence of numerous issuing banks) was obliged in 1874 to grant the Banco de España the national note-issue monopoly in exchange for a loan of PTA 125 million to the State coffers⁽¹⁾. The rest of the former issuing banks were given the option of operating as normal banks or being absorbed by the Banco de España, becoming branches of the central bank. The generally adverse situation meant that only four entities opted for the first alternative.

Regarding note issue, mention should be made of the key dates in the evolution towards a purely fiduciary monetary standard. The first was 1883, which saw the end of the convertibility into gold of the notes issued by the Banco de España.

The other two dates mark the lifting of the previous ceilings on note issue, ceilings which were habitually far from being reached⁽²⁾. The first ceiling, a ratio of the overall amount of notes issued to the Bank's capital, had the following legal values: in 1849, 0.5; in 1851, 1; in 1856, 3; in 1874, 5; in 1891, 10; and in 1898, 16.66. Thereafter, this ceiling disappeared in practice.

The second ceiling, a ratio of the banknotes in circulation to the metallic reserves held by the issuing bank, was set in 1856 with a maximum level equal

⁽¹⁾ The issuing privilege was renewed pursuant to contracts in 1891 and 1921.

⁽²⁾ In addition to these variable ceilings, there was always an absolute ceiling set by the Government which, specific periods aside (the First World War for instance), was also far from being overstepped. The limits, in millions of pesetas, were as follows: in 1874, 750; in 1891, 1,500; in 1898, 2,500; in 1899, 2,000; in 1914, 2,500; in 1917, 3,000; in 1918, 3,500; in 1919, 4,000; in 1920, 5,000; and in 1921, 6,000.

to 3. The system was amended in 1891, establishing a procedure which, with slight changes, would last for decades. Hereunder, the Bank's liabilities (banknotes, current accounts and deposits) could not exceed the amount of its most liquid assets (metallic reserves, secured short-term loans and discounted bills at less than 90 days). The effectiveness of this second ceiling was limited, and the average value of the banknotes/metallic reserves ratio was as follows: 1856-1873, 1.88; 1884-1898, 2.63; 1899-1920, 1.48; and 1921-1931, 1.37.

This ceiling was legally phased out in 1939 as a result of the depletion of the Banco de España's gold in financing the civil war. Hence, when the 1921 contract regulating the issuing privilege expired in 1946 it was not renewed, and the State acquired direct control of note issue. In this respect, the preamble to the 1946 General Banking Act indicated that "the issuing privilege, in all circumstances and all the more so if the granting thereof entails the capacity to create money that is legal tender, without the counterbalance of metallic reserves, should not be subject to a contract with the State. It is for the State, which confers the status of legal tender on the money in circulation, to impose, in the exercise of sovereignty, conditions on, and regulate the concession and use of, the aforementioned privilege".

This, then, led after the nationalisation of the Banco de España in 1962 to the current situation regarding note issue. As an historical remnant the ceiling on the issue of banknotes continues to be set by the Government, but this is a mere formality set in motion by the Ministry of Economy and Finance at the proposal of the Banco de España. Moreover, the Banco de España is responsible for the withdrawal and exchange of banknotes, but not for printing them.

The issue of coins is undertaken directly by the Treasury, which delivers them to the Banco de España for their placement in circulation. Only upon such placement does the Banco de España credit the related amount to the Treasury's current account.

5. BANKERS'S BANK AND LENDER OF LAST RESORT

The conduct of the Banco de España's predecessors as State bankers largely accounts for their balance sheets during the early part of their

existence. With a viewpoint constantly and essentially that of a private bank, credit to the private sector, including other banks, generally played a compensating role; it grew relatively during phases in which the public finances were in equilibrium, such phases logically being marked by general economic prosperity.

The situation was exactly this as from 1898. This year marked the start of a period in which the growth of credit from the Banco de España to trade and industry ran at sustained rates among the highest recorded. Also, thanks to the repatriation of colonial capital and the surpluses posted in the wake of the First World War, and in parallel with the development of a strong inflationary process, private banks grew extraordinarily, acquiring the basic features that characterise them today.

Although the Banco de España's conduct vis-à-vis private banks was not even mentioned in its regulations, this phase -1913-1914 to be specific- saw its first role as a lender of last resort in connection with the problems faced by two entities in Madrid and Bilbao.

These factors, along with the external instability of the peseta, explain the substance of the 1921 General Banking Act. This legislation was promulgated on the expiry of the 1891 contract regulating the issuing privilege.

The Act segregated, for the first time, the regulation of the Banco de España's conduct as a private bank and as a central bank. In this connection the Act mentions the Bank's functions as the main organ of monetary policy, in particular, its external realm of operations (the responsibility for which is assumed by the Government) and its role as the bankers's bank.

The only form of conduct envisaged as the bankers's bank was the creation of the rediscount, applying discounted interest rates to banks forming part of the Banking Supervisory Council, a voluntary, corporative body for private banks also created under the 1921 Act. Although the effectiveness of rediscounting for monetary policy was much diminished because of the sizable and automatically pledgeable government debt portfolios held at banks, it did

serve to reduce the Banco de España's direct operations with the private sector⁽¹⁾.

In the following decade, with episodes of widespread instability, many banks faced problems. These were primarily to do with liquidity, and then solvency, as a result in certain cases of speculative foreign exchange operations. In none of these instances did the Banco de España provide assistance, whereby it may be said that its role as lender of last resort backtracked.

This was perhaps why the 1946 General Banking Act, promulgated anew when the contract regulating the issuing privilege expired, acknowledged in its preamble that "it is for the issuing institution to act as a guide and source of assistance for private banks, particularly in the event of transitory difficulties". Article 18 of this Act, which remains in force, stipulates that the Banco de España "shall also take it upon itself, when general interests so advise, to offer all possible assistance within its scope of action that is compatible with the security of its operations to those credit institutions which, having acted in accordance with sound banking practices, face treasury difficulties due to a general crisis or to other circumstances".

Despite these rules, the preamble to the 1962 Act nationalising the Banco de España has to acknowledge that, hitherto, the Bank has always been the "State's banker and also a commercial bank, but it has not yet become the bankers's bank, the regulator of the credit mechanism and the agency entrusted with the external value of our currency". Like the remaining functions mentioned, that of bankers's bank was only assumed in practice, after the nationalisation, essentially as a result of the growing importance of rediscounting. However, neither the decree-law which regulated it nor the 1980 legislation (Ley de Organos Rectores del Banco de España) defining its status and scope, and which re-defined its functions, contributed in any significant way to regulating this function.

⁽¹⁾ The Banco de España's operations with individuals continued, on an ever-lessening scale, until its nationalisation in 1962.

Currently, the lender-of-last-resort function is performed essentially via second-window operations undertaken discretionally by the Banco de España at penal interest rates. These infrequent operations usually take place when interbank markets have already closed. They are undertaken solely with entities free from solvency problems and their purpose is twofold: to prevent overdrafts in the treasury accounts used by the entities for settlement⁽¹⁾. procedures; and to facilitate compliance with the reserve requirement.

6. SUPERVISOR OF THE CREDIT SYSTEM

Until a sufficiently consistent private banking system was set in place in the early 20th century, supervisory rules in the strictest sense could not really be said to exist. The only noteworthy forerunner was the presence of a royal commissioner at each of the issuing banks that existed at different times, including at the Banco de España and its predecessors.

6.1 Self-regulation as a starting point

The primary governing bodies in the sector, notwithstanding the generic rules of the Code of Commerce, were the Banking Supervisory Council and the Banking Commissariat, which came into being further to the 1921 General Banking Act. The former was a purely corporative and voluntary body, although an incentive to membership existed in the form of the "favourable" rediscount at the Banco de España and due to tax benefits related to cheque clearing.

The Banking Commissariat was an official agency, representing the State in the Banking Supervisory Council. It was entrusted with the official register of banks and bankers, on which only members of the Banking Supervisory Council could be listed.

⁽¹⁾ The Banco de España does not extend credit assistance to entities with solvency problems. Where appropriate, such assistance is provided by the deposit guarantee funds, under the terms discussed in section 10.1.

In principle, the regulations governing banking activity decreed by the above-mentioned Council only affected its members. However, the Banking Commissariat presiding it could make these rules extensive to all banks operating in Spain⁽¹⁾.

The supervision of banks was entrusted to the Banco de España by the 1921 Act. It was argued that "among private banks there can be no mysteries and no reservations with regard to the Banco de España; no bank should consider itself offended or its professional secrecy breached on placing its most confidential operations at the disposal of the Central Bank"⁽²⁾.

Despite these arguments, the incongruity of a private bank inspecting its competitors was excessively blatant, and the Banco de España never actually began to perform its supervisory tasks. Nonetheless, in order to be able to assess "sound banking practices" as required of it as the bankers's bank and as lender of last resort, the Banco de España received all banks' balance sheets monthly and their profit and loss accounts annually. The exiguity of the forms established -both for public statements (standardised since 1922) and for the first confidential statements (as from 1955)- explains why there was no incongruity between the receipt of these documents and the fact that the Banco de España should have been operating as a private bank.

The supervisory vacuum was partly filled by the self-regulating activity which arose in connection with the Banking Supervisory Council and the so-called Local Banking Boards. The latter emerged in 1930 to supervise compliance with the banking regulations dictated by the Banking Supervisory Council and declared as compulsory by the Banking Commissariat.

In 1938, at the height of the civil war, the Banking Supervisory Council was dissolved. Its private-banking supervisory functions were transferred to the Banking and Stock Market Directorate-General of the Ministry of Finance, which undertook them in conjunction with the Local Banking Boards, which by

⁽¹⁾ As from 1927 the Banking Commissariat could sanction failure to comply with these rules.

⁽²⁾ Parliamentary speech by the Finance Minister F. Cambó.

that time had been converted into a peripheral associated body⁽¹⁾. This Directorate-General merged in 1957 with its Insurance counterpart, and was re-named Banking, Stock Market and Investment. It also took up the supervision of savings banks, which had previously reported to the Ministry of Labour, and of insurance companies⁽²⁾. As a result, the aforementioned Directorate-General became the system's major supervisory centre, since only the official credit institutions, which reported to the Medium- and Long-Term Credit Committee since being reorganised in 1958, lay beyond its range of powers⁽³⁾.

6.2 Situation following the 1962 Nationalisation Act

Financial supervision arrangements changed radically after the nationalisation of the Banco de España in 1962 (see figure 1).

Despite its apparent complexity, the core of the system -as far as financial intermediaries are concerned- remained attached to the Ministry of Finance through the Banco de España, which was entrusted with the control and supervision of the bulk of financial intermediaries -i.e. private banks- and whose governor presided the Savings Banks Credit Institute, responsible for supervising savings banks, and the Institute of Medium- and Long-Term Credit (ICMLP), charged with official credit -which was also nationalised in 1962- and the remaining intermediaries, except co-operative credit⁽⁴⁾. Co-operative credit, due perhaps to its triple ministerial ascription and scant significance, was not subject in practice to any specifically financial supervision during this period, not even when it was ascribed exclusively to the Ministry of Finance following the 1967 regulation of the sector.

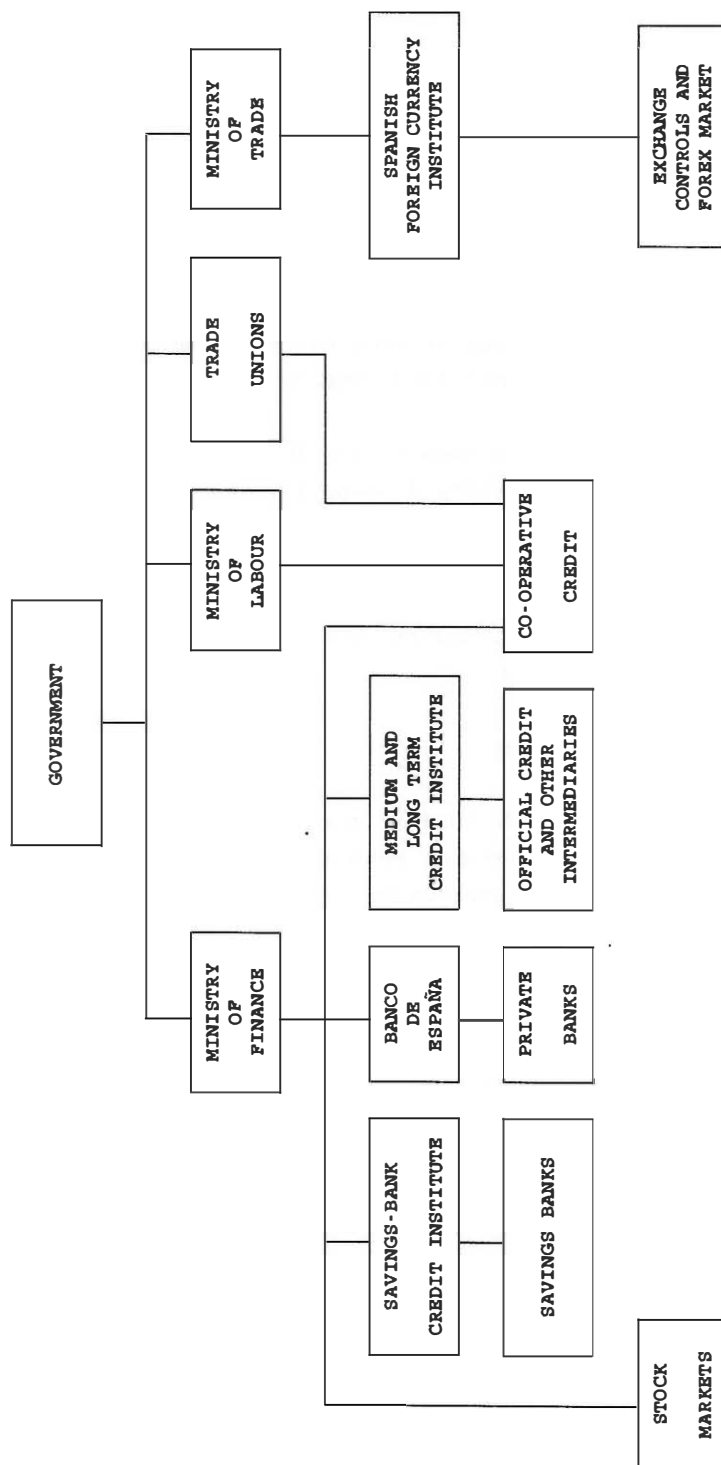
⁽¹⁾ The Banking Supervisory Authority re-emerged in 1946 with merely consultative functions, registration therewith being obligatory.

⁽²⁾ This Directorate-General was also responsible for supervising stock exchanges and investment companies.

⁽³⁾ Supervisory rules and sanctioning capacity were as envisaged in the 1946 General Banking Act. Though drafted for private banks, they were applied analogously to the other entities involved.

⁽⁴⁾ The ICMLP was also entrusted with the administrative authorisation of all issues of medium- and long-term certificates, including those of all types of financial intermediaries.

FIGURE 1
FINANCIAL SUPERVISION ARRANGEMENTS FURTHER TO THE 1962 LEGISLATION



Marginal areas aside, this supervisory structure offered, for the first time, a clear distribution of powers. Coherence was afforded by having the pivotal figure of the Governor of the Banco de España as chairman of the three supervisory centres. These were formally separated from the administrative structures of the State, and had a technical mission which was only partly pursued in practice since the main supervisory advances were in aspects which were more formal and concerned with the defence of public interventionism than they were explicitly financial. It was indeed supervisory problems related to the official credit institutions which triggered the 1971 reform.

Turning to the financial markets, only the Stock Exchanges (which began to report directly to the Ministry of Finance following the disappearance in 1967 of the Directorate-General of Banking, Stock Markets and Investment) and the incipient foreign exchange market were in place. The latter emerged in the wake of the declaration as to the external convertibility of the peseta in 1959, and was stringently controlled by the Ministry of Trade via the Spanish Foreign Currency Institute.

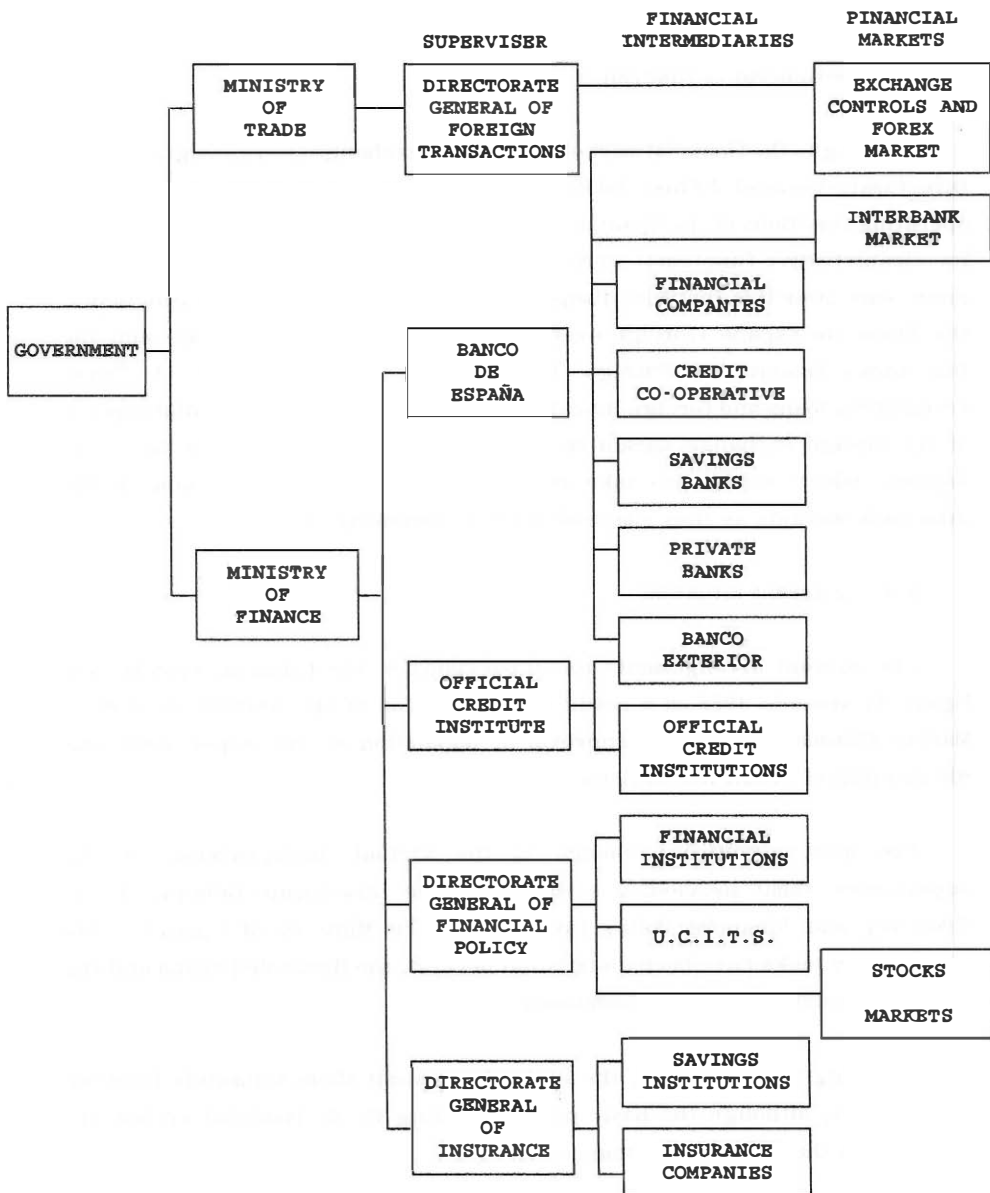
6.3 The 1971 reform

The 1971 reform of the financial system was primarily triggered by the serious working and supervisory flaws uncovered by the Matesa affair. The desire to mask this origin explains why a reform which was to affect the entire financial system was included in a legal provision bearing a much less ambitious name: Law on the organisation and status of official credit.

The structural arrangements for the supervision of the system brought into being by this legislation (see figure 2) remained virtually unchanged for almost two decades. Noteworthy in relation to the previous structure was the disappearance of the Savings Bank Credit Institute, whose supervisory functions were assumed by the Banco de España along with those relating to credit co-operatives and entities specialised in financing instalment sales of capital goods⁽¹⁾. The new Official Credit Institute was given charge exclusively of the financing and supervision of official credit institutions,

⁽¹⁾ These entities, which were created in 1962, operated de facto as specialised banking offices.

FIGURE 2
FINANCIAL SUPERVISION ARRANGEMENTS AFTER THE 1971 REFORM



while its remaining functions were transferred to the Banco de España (those relating to bank issues and to finance companies) and the newly created Directorate General of Financial Policy (all others). The latter agency also began to supervise finance companies, unit and investment trusts and all other financial entities not specifically classified. Insurance companies and capitalisation and savings entities came under the supervisory roof of the Directorate-General of Insurance.

Turning to the financial markets, the stock exchanges were assigned to the Directorate-General of Financial Policy. As to the foreign exchange market, the operating functions of the Spanish Foreign Currency Institute (which retained its administrative functions) were entrusted to the Banco de España in 1969. Four years later this Institute disappeared, and its functions were assigned to the Banco de España (foreign exchange policy and financial loans) and the Directorate-General of Foreign Transactions of the Ministry of Trade (commercial loans and foreign investment). Accordingly, the essential aspects of the foreign exchange market moved in full into the ambit of the Banco de España, which would also take responsibility for the supervision of the interbank markets as they emerged over the following years.

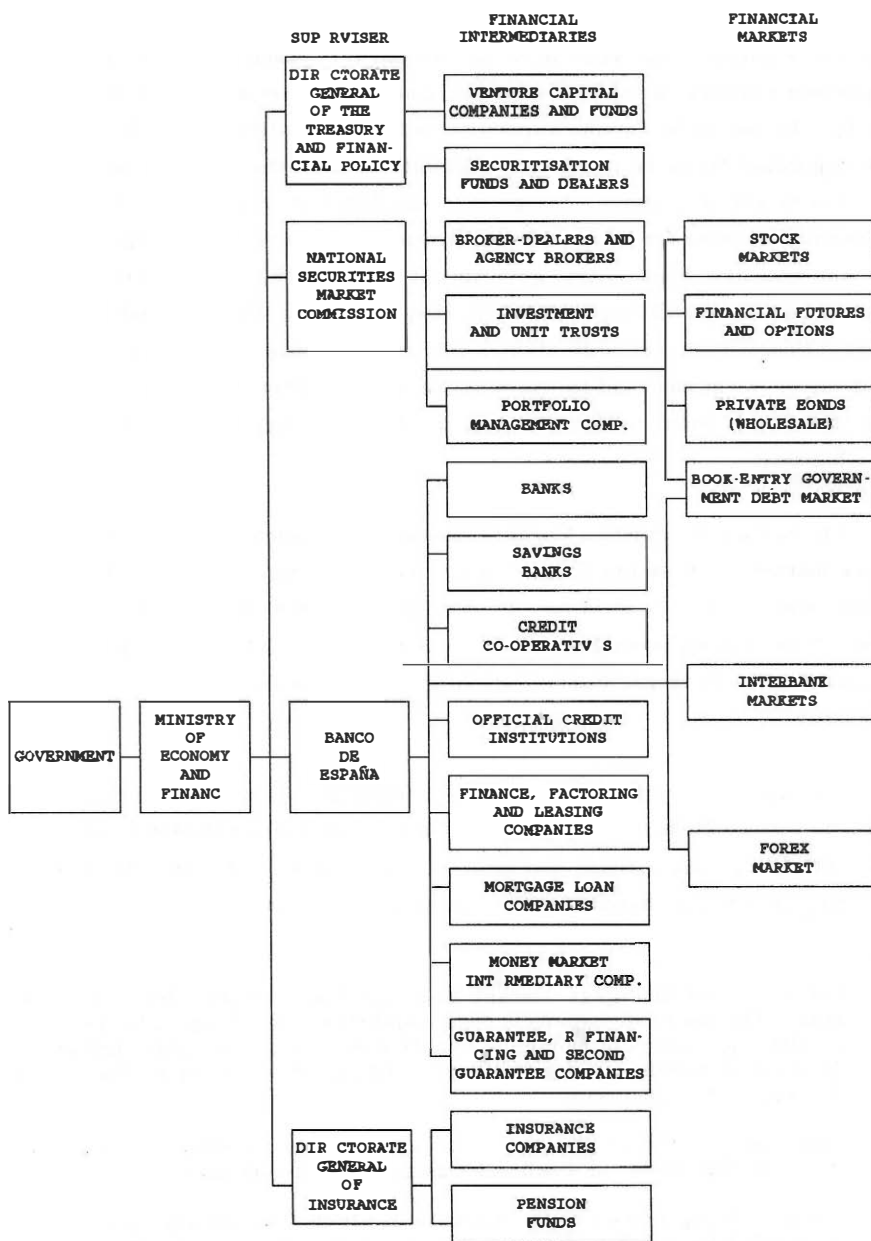
6.4 Current situation

The current arrangements for supervision of the financial system (see figure 3) arose in 1988 as a result of the creation of the National Securities Market Commission and the approval of legislation on the supervision and disciplining of credit institutions.

The most significant change is the virtual disappearance of the supervisory remit previously accorded to the Directorate-General of the Treasury and Financial Policy (attached to the Ministry of Finance). Its supervisory tasks have been distributed between the Banco de España and the National Securities Market Commission.

Following these changes, the supervisory remit stems ultimately from the Government, although the basic powers relating to the financial system are assigned to the Ministry of Finance.

FIGURE 3
CURRENT STRUCTURE OF THE SPANISH FINANCIAL SYSTEM



Four supervisory centres oversee Spanish financial markets and intermediaries. Taking the latter first, the Directorate-General of the Treasury and Financial Policy retains only certain residual tasks in this area; as its name suggests, the Directorate-General of Insurance oversees all insurance entities; the National Securities Market Commission monitors unit and investment trusts, securities brokers/dealers and securitisation funds; and lastly, the Banco de España supervises all credit institutions. The control of the organised financial markets is also entrusted to the two main supervisory centres referred to above. Assigned to the Banco de España's control are the interbank markets for loans and certificates of deposits, the foreign exchange market and the book-entry government debt market. Since the latter is considered as an official market, it also reports to the National Securities Market Commission. Co-ordination is duly attained via a Consultative Committee made up of two members of the National Securities Market Commission, one from the Ministry of Finance and two from the Banco de España, one of whom acts as Chairman⁽¹⁾.

The National Securities Market Commission is primarily responsible for the stock markets. There are four stock exchanges in Spain (Madrid, Barcelona, Bilbao and Valencia). Each has its own Management Company, although more than 90% of trading is conducted via the Stock Market Interconnection System, a continuous electronic market whose governing body is the Stock Markets Company⁽²⁾.

The organised secondary markets for financial futures and options are also considered as official and report to the National Securities Market Commission. As underlying assets these markets use government debt, interbank loans, specific currencies, listed equities and related indices⁽³⁾.

⁽¹⁾ The so-called mortgage market does not have clearly defined trading ambit. The Banco de España is responsible for controlling and supervising it, although issues of mortgage certificates, bonds and participations, if these are securities, and securitisation funds are overseen by the National Stockmarket Commission.

⁽²⁾ Subsidiary to the stock markets is a secondary market -of very limited size- for the shares of small- and medium-sized companies.

⁽³⁾ The governing bodies of the markets in which the underlying assets are traded have a specific remit for the related derivatives markets.

The AIAF (Spanish Bond Dealers' Association) private fixed-income market, a wholesale market fostered by virtually all financial intermediaries, is likewise recognised as an (unofficial) organised secondary market.

Mention should also be made, under service companies, of appraisal companies, which report to the Banco de España, and of rating agencies, which are overseen by the National Securities Market Commission.

7. MONETARY POLICY

Since its creation and until very recent times, neither the Banco de España nor its predecessors were in a position to exert minimally effective control over the creation of money from the standpoint of the general course of the economy.

7.1 Passive provision of liquidity

Since the outset, the limits on notes in circulation (mentioned in the section on the note-issue privilege) were set by legislation or the Government. Within such limits, the Banco de España, habitually following prudent policies, set its own limits provided that circumstances so permitted.

As private banking operating criteria predominated, with the consequent and legitimate profit-making goal, the general interests of the economy were always in the background or not even present. As a result, the demands for liquidity at times at which the economy was expanding were not always met, thereby prompting various protests and even the creation of rival issuing banks (in 1844 for example). On the contrary, on the few occasions on which the Bank was more go-ahead, the excessive creation of money generated relatively significant inflationary processes (e.g. from 1910 to 1920).

An early change of significance came about further to the stabilisation plan which followed the end of the colonial wars in 1898. A budget surplus actually ensued and both government debt in circulation and indebtedness to the Banco de España declined. When budget deficits reappeared, the indirect monetisation

of government debt was implemented via its automatic pledging at the Banco de España (as described earlier).

Evidently, although the new system was more flexible than the previous one, it entailed no significant headway towards greater control of the creation of money by the Banco de España. The central bank continued to be a passive provider of liquidity, although the initiative for its creation had shifted largely from the Treasury to the holders of automatically pledgeable government debt.

This was the situation when, pursuant to the 1921 General Banking Act, rediscounting favourable to banks was regulated. For 10 years the Banco de España set both individual rediscounting limits and the related (and always favourable) interest rate; however, this monetary policy instrument, the first such modern instrument available to the Banco de España, could do little to counter the large volumes of automatically pledgeable government debt outstanding, held particularly by private banks.

In 1931, during the Second Republic, it was decided that rediscount interest rates should be set by the Ministry of Finance. This decision was ratified in 1938, at the height of the civil war, by what would prove to be the winning side and which remained in power until 1977. With this discretionary power in the Ministry's hands, rediscounting was deprived of any flexibility. And compounding this was the considerable inertia which came to characterise the setting of limits to the amounts rediscountable to each bank, which scarcely moved.

Several significant changes ensued from the 1959 stabilisation plan, aimed at dispelling the autarchic premises underpinning economic policy since the end of the civil war. In the run-up to this plan, specifically in 1957, automatically pledgeable debt ceased to be issued and, three years later, the legal possibility arose of setting in place a reserve requirement "to replace the current procedure of quantitative restrictions on the amount of bank lending operations, which by its very nature is destined solely to cause adverse, rigid and, on occasion, disturbing effects"⁽¹⁾.

⁽¹⁾ Preamble to Decree-Law 22/1960 on monetary control.

The short-term effectiveness of both measures was non-existent. The reserve requirement was initially imposed, in 1963, only on investment banks as a means of restricting their fixed-asset additions, complementing the liquidity ratio⁽¹⁾. For other banks and savings banks, the requirement was set in place in 1971. However, although its use for defining a non-distorting money multiplier required implementation at a homogeneous level for the entire banking system, there was no such homogeneity until 1977 for the different types of banks, and until a year later for savings banks⁽²⁾.

With regard to the uncontrolled creation of liquidity, the automatic pledging of the government debt still outstanding was complemented and then replaced by the special-facility rediscount which emerged in 1960. Hereunder, the documented loans and bills representing financing extended by banks to sectors or activities targeted in development plans as priority areas were automatically rediscountable at the Banco de España under special facilities for unlimited amounts. The Banco de España had no control on the related interest rate and these instruments grew extraordinarily in the following decade.

During this period, in 1962 to be exact, the Banco de España was nationalised. The preamble to the authorising legislation specified the margins of monetary policy independence to be conferred on the central bank: "the Spanish State not accepting the principle of economic neutrality, monetary authority cannot be delegated to the issuing bank but shall be exercised permanently by the Government through the Minister of Finance; in the technical realm, however, it is advisable to entrust the implementing details of the policy pursued to the Banco de España".

This belligerent rationale presided over the design of the arrangements and functions stipulated by the decree-law nationalising the Banco de España. Significantly, on listing its functions, mention was not even made of monetary

⁽¹⁾ From 1966 to 1976 the level of the reserve requirement differed for deposits at less than, and over, one year and for "bonos de caja" (bank bonds with certain tax benefits).

⁽²⁾ Homogeneity has not come about for credit co-operatives, which have had a reserve requirement since 1979.

policy; there was a reference only to "informing and advising the Government on money and credit matters".

However, the same decree-law, in addressing the powers of the Ministry of Finance, stipulated that of "dictating the general rules for the central bank's conduct as executor, within the scope of its remit, of the Government's monetary and credit policy". The only reference to monetary policy implementation, in particular to open market operations, which was not put into practice until twenty years later, provided that the Banco de España may, "acting as a principal, acquire, possess and dispose of securities and bills and operate with this portfolio for the purposes of regulating the money market. It may also receive government debt and Treasury securities for subsequent trading therewith".

In 1963 a new monetary policy instrument -the bank liquidity ratio- was created. As it was very poorly defined, it did not prove effective. Among its eligible assets -in addition to cash, deposits at the Banco de España and automatically pledgeable and unpledged government debt- were documented loans and bills held in bank portfolios but rediscountable on a special-facility basis. The disproportionate growth of the latter made the ratio ineffective.

7.2 Towards an active control of liquidity

It was necessary to wait until 1971 for the disappearance of the automatic channels of liquidity creation. That year saw the replacement of the special rediscounting facilities by the private banks' obligatory investment requirement, "a system which, as experience has proved, obviates squaring the objective of providing sufficient financing for ends deemed by the Government to merit priority with the unavoidable demands of averting an automatic creation of liquidity that hampers the exercise of monetary policy, and of ensuring the ordered working of the banking system"⁽¹⁾.

⁽¹⁾ The ordinary rediscount, which was in fact a semi-autonomous liquidity-creation procedure in view of its high inertia in relation to amounts and interest rates, disappeared in 1979 and was temporarily replaced by special credit facilities, which were closed in 1982.

With the disappearance of the automatic liquidity creation mechanisms, an active, ongoing implementation of monetary policy began at the start of the seventies.

In deciding which model to follow, the first matter raised was whether the results of monetary intervention were to be measured by directly observing the course of the final target (nominal expenditure of the economy) or whether, by contrast, an intermediate target was to be set, which would be indicative of the former and lend itself more readily to monitoring. The delay with which reliable data on the course of the economy's real variables became available and the complementary information an intermediate target could provide led to it being adopted, setting in place a two-step monetary policy framework.

This decision having been taken, the non-existence of freely formed interest rates precluded at that time selecting either the money stock or interest rates as the intermediate target of monetary policy. After opting for the control of the monetary aggregates, the following step was to choose the aggregate evidencing a more stable relationship to aggregate nominal spending. The studies conducted tilted the balance in favour of broad money, the monetary aggregate defined as the sum of cash plus total deposits and bank bonds held by resident sectors.

For the same reasons, the supply of bank reserves was selected as the instrumental target in the short-term implementation of monetary policy.

7.3 Growing importance of interest rates

The advantages of this model, combining the official setting of the reserve requirement with the provision, at market rates, of the liquidity required to meet it, were progressively diluted due to three main factors: first, the growing instability of the demand for bank reserves and for monetary aggregates, owing to financial innovation, disintermediation, taxation, etc.; second, the growing presence of representative interest rates, formed on increasingly integrated markets; and third, the approach and eventual incorporation of the peseta into the exchange rate mechanism of the European Monetary System, against a background of increasingly free capital movements.

As a result, interest rates -particularly short-term rates- increased in importance as the instrumental target of monetary policy. Notwithstanding, regard continued to be had to the course of monetary variables in the very short term and greater direct attention was paid to the rate of inflation.

Logically, these changes in monetary policy design led to significant changes in its implementation, both in the reserve requirement and in the Banco de España's intervention in interbank markets.

7.3.1 Changes in the reserve requirement

Turning first to the reserve requirement, it was earlier noted that, until 1978, its level was not made uniform for the main deposit-taking institutions - banks and savings banks- whose operating possibilities had been homogenised a year earlier. The reserve requirement has since been changed frequently, with regard to its eligible assets (excluding, first, undrawn funds in credit accounts at the Banco de España, and further, cash, until only sight deposits at the Banco de España remain), to how it is calculated (from daily figures to ten-day averages, with a lag between assets and liabilities, counting bank holidays), to its eligible liabilities (ever broader), to the institutions affected (an ever greater number), etc.

Nonetheless, the most significant changes were in its function. First, its role as a money multiplier was overshadowed during the eighties by its significance as what was to all intents and purposes an investment ratio. This was because of a scantily remunerated tranche which came to account for 17% of eligible liabilities and which, in 1990, was replaced by the obligatory purchase of Banco de España certificates. Second, as changes in the intermediate target began to dilute its significance as a multiplier, its eligible assets -sight deposits at the Banco de España- have progressively gained in importance as a support of the payment system. That implies a certain limit on the decline of reserve requirements whilst no reform of the procedures and guarantees relating to the settlement of interbank payments is enacted⁽¹⁾.

⁽¹⁾ The level of the reserve requirement currently stands at 2% of eligible liabilities.

7.3.2 Credit instruments for intervention

The Banco de España's intervention instruments for regulating bank reserves have also been considerably altered. Initially, the fact that all government debt held by the banking system was frozen under obligatory investment requirements meant that the main monetary intervention instrument had to be monetary regulation loans. These emerged in 1974, for banks only, and were allotted on the basis of the resources -initially own and subsequently total- of each entity, at sufficiently low interest rates to ensure the demand therefor. The subsequent redistribution of the overall liquidity thus created, depending on the various banks' particular demand for liquidity, is at the root of the interbank market for deposits. This market was already entrenched when, in 1977, daily auctions became the standard mechanism for assigning loans, to which savings banks already had access⁽¹⁾.

To date, they have been implemented through loans whose ceiling for each entity has had a twin amount: on the one hand, 80% of the entity's own resources and, on the other, the securities provided as a complementary documented guarantee⁽²⁾. As overall intervention needs developed, there were variations in the terms of these loans, which in recent years had been to the following working day and the demand for which had been ensured via changes in the level of the reserve requirement and the use of the liquidity-absorption instruments discussed below⁽³⁾.

7.3.3 Open market operations: background data

Despite the advantages of open market operations discussed below, banks' scant portfolios of unrestricted debt meant, until very recently, that they were

⁽¹⁾ Previously, that same year, the interest rates on all Banco de España operations with the institutions supervised by it had been liberalised.

⁽²⁾ Normally, this guarantee would be made up of securities frozen under obligatory investment requirements (investment certificates, Treasury notes, etc).

⁽³⁾ Exceptionally, second-window operations were made to solve specific liquidity problems at specific entities.

essentially used to withdraw liquidity from the market in such a way that there would be demand for the shorter-dated monetary regulation loans.

Chronologically, the first instrument used in open market operations was Treasury bonds. These were created in 1973, being issued by the Treasury for no specific budgetary purpose, and were transferred to the Banco de España at a fixed rate of interest⁽¹⁾. Their placement with entities was via discount window and at interest rates freely set by the Banco de España. Whereas in the secondary market for these instruments only simple trades were transacted, the bulk of operations was with the Banco de España. With the introduction of sales under repurchase agreement in 1979, operations between entities began to acquire significance.

A year later, in view of the impossibility of meeting liquidity-absorption needs with the limit authorised for Treasury bond issues, the Banco de España certificates of deposit were created. These were issued unrestrictedly by the central bank and only differed from Treasury bonds in that initially banks and savings banks alone were authorised to subscribe them. Authorisation was later extended to the entire system.

Both intervention instruments co-existed until they ceased to be issued in April 1982 as monetary regulation certificates appeared. The short-lived duration of this instrument coincided with the most active stage of market-price fund-raising by the Banco de España. They were issued by the central bank via auctions, essentially of two types: ten-day auctions, open to all entities and at which three-month certificates were placed; and occasional auctions, at which the banking system and money-market intermediaries could buy very-short-dated certificates.

With the disappearance of the monetary regulation certificates in early 1984, a new phase began in which the main liquidity-absorption mechanism was the interest-bearing tranche of the reserve requirement. Open market operations, meanwhile, complementing monetary regulation loans, were undertaken with government debt. Treasury notes were first used and, when

⁽¹⁾ Their balancing item in the Banco de España's balance sheet was a special restricted Treasury account.

they began to be issued at lower-than-market rates in 1985 (since their purchase was guaranteed by ratio requirements), Treasury bills took their place. These were eventually complemented by other forms of public debt at times at which entities' portfolios were too exiguous for intervention requirements.

In summary, the Banco de España's money market intervention procedures in the recent period were the following: 1) ten-day auctions of three-month Treasury bill sales under repurchase agreement open to all entities and which left the system's liquidity slightly below the programmed path⁽¹⁾; 2) daily auctions of monetary regulation loans until the following working day, only for banks and savings banks, which regulated liquidity onto the path of bank reserves programmed for each day; and 3) open market operations with market makers, made throughout the day when interest rate movements threatened to move such rates from their established band.

Broadly, the monetary intervention mechanisms touched on above could be said to work satisfactorily, particularly so after the mutual learning process for both the Banco de España and the entities concerned had helped soften initial rigidities.

7.3.4 Occasional instruments

Evidently, the model described requires the prior selection as a monetary policy intermediate target of either the growth of the monetary magnitudes or changes in interest rates, leaving the alternative not chosen to trend freely.

With the peseta joining the European Monetary System's grid of fixed parities, and despite it being in the so-called wide band, a vicious circle ensued which the aforementioned mechanisms were unable to break: to drain existing liquidity, which threatened to induce an inflationary process that would increase Spain's price differential with the Community, it was necessary to raise interest rates to levels which, by fuelling capital inflows, increased the system's liquidity.

⁽¹⁾ In addition, these auctions served to meet the system's demand for very-short-dated government debt, which the Treasury did not issue.

The solution adopted only in 1989 and 1990 was that the above-mentioned monetary intervention mechanisms should focus basically on keeping the course of interest rates compatible with the exchange rate of the peseta. In parallel, to avoid an excessive growth of the monetary aggregates, an official 10% ceiling was placed on the growth of credit to non-financial firms and households.

As in previous situations where strong restrictions were in force, these measures had to be complemented by the raising of obstacles to foreign capital inflows. Notable in this connection were the obligatory deposit proportionate to 30% of foreign credits and the consideration of convertible-peseta balances and of the net increase in foreign-currency positions as eligible liabilities for reserve requirement purposes.

7.4 Current situation: open market operations

The situation changed again in 1990 when Banco de España certificates emerged further to the reform of the reserve requirement. With the reserve requirement level falling from 17% to 5% of eligible liabilities, the liquidity freed hereby had to be withdrawn from the system so as to avoid the surge in the growth of the monetary aggregates that would have ensued. Accordingly, entities subject to the reserve requirement were obliged to subscribe these certificates to the order of PTA 3.3 trillion.

The Banco de España certificates have a unit face value of PTA 10 million and are instrumented through book entries at the Banco de España. They bear annual interest of 6%, payable in six-monthly coupons, and will be redeemed, in increasing proportions, from March 1993 to September of the year 2000.

As from issue, these certificates are tradeable through repurchase agreements (repos) or reverse repos only with the Banco de España or other entities subject to the reserve requirement. Outright-purchase transactions may be freely undertaken with the Banco de España; however, with the other entities subject to the reserve requirement, they have only been fully

tradeable since 1992⁽¹⁾. Trading is unrestricted within the aforementioned group of entities, but it is not planned to be authorised outside such group.

The Banco de España had advocated for several years the advisability of intervening in money markets via open market operations, especially through repos and reverse repos with government debt⁽²⁾.

Open market operations have three basic advantages in relation to monetary regulation loans: 1) their symmetry, i.e. their capacity both to inject and drain off liquidity; 2) a much more flexible execution of guarantees compared with the freezing of public debt accompanying loans; and 3) they boost the setting up by entities of back-up liquidity facilities made up of highly liquid assets which, acting as a buffer between deposits at the Banco de España and other credit investments, help give flexibility to the structure of balance sheets. The characteristics of this back-up liquidity facility and the high interchangeability of the assets it comprises with the more liquid items of the bank balance sheet give shape, moreover, to an effective mechanism of integration between the money and credit markets.

This intention could never have been put into practice: first, due to the non-existence of government debt issued under market conditions and which, therefore, was not tied to obligatory investment requirements; further, due to the absence of an efficient secondary market; and subsequently, following the creation of the Book-Entry Government Debt System, because of the exiguous bank portfolios of public securities not sold under repurchase agreement to the public, which were totally inadequate for sustaining the liquidity injections required.

With the emergence of the Banco de España certificates, this situation changed radically; entities now have a back-up liquidity facility (the setting

⁽¹⁾ The aim of placing temporary restrictions on outright-purchase transactions was to prevent the impact on corporate income tax, through outright sales of certificates with heavy capital losses (in view of their far-below-par price), from altering the expected return for initial subscribers.

⁽²⁾ Logically, outright transactions are only resorted to when it is considered interventions should be of a permanent nature.

up of which was initially obligatory) whose redemption schedule enables open market operations to be fully consolidated, before their disappearance. This has facilitated the far-reaching change in monetary policy implementation, whereunder loans are only used as last-resort liquidity support and for special circumstances.

The outcome of these developments is the current situation, which may be characterised by: a) intermediate targets focused -in the very short term- on interest rates, without abandoning -in the short term (a month)- the growth path of liquid assets held by the public as a reference and a final consideration of nominal expenditure and the inflation rate; b) a reserve requirement with a level of 2% which may fall when more finely-tuned procedures are established for covering payment-system risks; c) implementation based on two types of open market operation (repos and reverses with Banco de España certificates and with book-entry government debt): c.1) ten-day auctions open to the banking system, which place bank reserves at around the planned level and mark interest rates, c. 2) daily fine-tuning interventions via auctions open only to market-makers, and with last-resort, secured loan operations bearing penal rates, to resolve the liquidity problems of individual entities, such difficulties generally stemming from technical problems arising at the daily close of payment systems.

8. EXCHANGE RATE POLICY

8.1 Background

Until the emancipation of the chief American colonies in the late 19th century, remittances of precious metals were the mainstay of public revenues. Throughout this period the issue of government debt ("reales"-denominated certificates) and recourse to the Banco de España and its predecessors were directly related to interruptions in the shipment to Spain of gold and, especially, silver from the Americas, due to the various wars being waged at that time.

When the Banco de San Carlos was created in 1782, its stated functions included the exclusive execution of the "Royal Draft", i.e. meeting the

Treasury's external payments. Having to meet such payments, at a time the reales certificates were depreciating steeply, led a year later to the Bank being granted the exclusive privilege to export coined money, it being considered that this was the only way a drastic loss in the value of paper money could be avoided, especially abroad.

In principle the monopoly was temporary; but despite the severe criticism voiced by the mercantilists, it was successively renewed until the remittances from the Americas ceased altogether, and it was for long periods the main source of profits for the Bank.

Over what was virtually a century, sustaining the external value of the currency was never a concern for the Bank. However, with the external depreciation of the peseta commencing in 1882 and culminating in 1898, critics once more inveighed against the Banco de España, holding it responsible for what they considered were excessive gold outflows.

Nonetheless, such outflows were not of the Bank's volition. They were due rather to two factors beyond its control. The first, following on from a trade balance chronically in deficit, was the decline in capital inflows triggered by the 1882 international crisis. This fall, exacerbated by the under-valuation of gold in Spanish monetary legislation, led to an outflow of gold which explained the need to discontinue, in 1883, the convertibility into gold of the Banco de España's banknotes and its subsequent loss of international prestige.

Turning to the second factor, there was a reconversion of public debt in 1882 which unilaterally diminished the return thereon, split it into domestic and external parts and guaranteed to the latter the payment in gold of the interest thereon. This sparked massive purchases of external debt by Spanish investors, with the subsequent export of capital. Only in 1889 when measures against this repatriation of external debt were adopted did the value of the peseta cease to fall.

1903 saw a first attempt to create an Exchange Office at the Banco de España (made up of the Minister of Finance, the Director-General of the Treasury and the Governor) responsible for regulating the external performance of the peseta. The Office did not, however, prosper.

After 1905, the price of the peseta began to rise as foreign capital inflows resumed, as capital from the former colonies was repatriated and, a year later, as the payment in gold of the protectionist tariffs in force began to take hold.

Shortly afterwards, a new plan to organise foreign exchange market intervention systematically was unveiled. An Exchange and Currency Fund was created under the joint responsibility of the State and the Banco de España. It was to be headed by a Commission, presided over by the Minister of Finance and made up of delegates from both institutions, and its basic function was to take responsibility for "all banking and mercantile operations related to international exchange, the gradual decline in which will be pursued".

Although this plan did not prosper either, the guidelines for it were once more evident ten years later. This was when the 1921 General Banking Act was drafted, at a time of weakness of the peseta and against a background of speculation by Spanish banks, whose bleak results foreshadowed a series of bankruptcies, which bore particularly heavily on Catalonia.

8.2 Lead role for the Government and inhibition of the Banco de España

The 1921 Act did not establish a defined foreign exchange intervention procedure. It confined itself to stipulating that, in the event of the Government deciding to intervene on the foreign exchange market in defence of the peseta and of it requiring the co-operation of the Banco de España, the latter should participate by the same proportion as the State in the operations to which such policy might give rise. In consideration hereof, the gains or losses obtained would be distributed in equal portions, with the constraint that the losses of the Banco de España should never exceed the balance of a special reserve which by law it was obliged to set aside. The practical consequence of this regulation was that the Banco de España relinquished, for almost fifty years, its vigilance over the external value of the peseta.

During these years the relative high rates of inflation weakened the trade balance, causing a slow slide in the peseta which only ceased in 1925. The next two years saw sizable short-term capital inflows, speculating in favour of the peseta. The sudden withdrawal of these funds in 1928 prompted a heavy fall in the international price of the peseta.

Given the gravity of the situation, the Government made use of the provisions of the 1921 Act and created a Foreign Exchange Intervention Committee, with resources totalling PTA 500 million (provided in equal proportions by the Banco de España and the Treasury). The Committee was active only for a few months, buying pesetas; however, it succeeded only in cushioning the fall of the peseta in the few months in which it acted.

Criticism of its performance, the depletion of the foreign credits used and the Banco de España's fear of a fall in its gold reserves led to the winding up of this Committee. The harshest criticism was from the Gold Standard Committee, created in 1929; while it accepted the need to intervene in the foreign exchange markets, it criticised the Intervention Committee's methods and advocated a diametrically opposite policy, i.e. aimed at preventing the over-valuation of the peseta.

In 1930 the Foreign Exchange Regulating Body was created. It worked within the Banco de España and was entrusted with centralising foreign exchange operations and, in particular, foreign currency purchases. That same year it was replaced by the Official Currency Transaction Centre, formed by the State and the Banco de España. It took charge of intervention operations and set daily the price of the peseta and its maximum fluctuation.

To raise resources holding out against the opinion of the Banco de España, gold was deposited abroad and, using it as a guarantee, credit was negotiated with North American banks. With the onset of the Republic a year later, the North American credit was cancelled and the increase in the notes and coins in circulation, still backed by metallic reserves, prevented fresh gold outflows. As a result, the Centre could not continue operating and stringent exchange controls were set in place the rigidity of which, despite changes thereto, would not slacken over the following forty years.

8.3 From exchange controls to the Spanish Foreign Currency Institute

For exchange control purposes, cross-border dealings were divided into three groups: prohibited operations (speculation or capital flight), operations requiring prior authorisation (which were not of a strictly commercial nature) and unrestricted operations (goods imports and exports). The Official

Currency Transaction Centre began to act as a centralising body for foreign currency reserves: all Spanish residents had to sell to it all the foreign currency they obtained, while those demanding foreign currency had to justify the use thereof.

Into the civil war, the Franco Government set up in 1936 the Foreign Currency Committee, which confined itself to placing the scant resources available at the disposal of war requirements. The Committee initially reported to the State Technical Junta, and later to the National Banking, Currency and Exchange Service. It remained under the control of the Ministry of Finance, which was entrusted with the "supreme management and oversight of foreign currency policy and of changes to official exchange rates".

This hierarchical relationship changed in 1939 when the Committee became the Spanish Foreign Currency Institute, reporting to the Ministry of Trade. As a result, foreign exchange policy was, for 20 years, a trade policy instrument. Based on stringent exchange controls, the Institute's most characteristic measure was to set in place a system of multiple exchange rates for each currency, which could -according to the destination of the foreign currency demanded- vary in the proportion of one to five.

This situation remained essentially unchanged until the 1959 stabilisation plan. The most significant consequence of the plan in this area was the 1961 declaration on the external convertibility of the peseta, i.e. only for non-residents.

8.4 Participation of the Banco de España in foreign exchange policy

In 1962, the legislation from which the nationalisation of the Banco de España ensued stated categorically that "the movement of foreign payments and the centralisation of metallic and foreign currency reserves shall be transferred to the Banco de España". That said, nothing was done for seven years.

In 1969, the purely operative functions of the Spanish Foreign Currency Institute were moved to the Banco de España. The Institute's director-general became the deputy governor of the Banco de España, and an inter-ministerial

commission was designated and entrusted with co-ordinating actions relating to reserves and foreign currency. The supervision of foreign exchange markets -which had only started operating as such a year earlier- also became the responsibility of the Banco de España.

Finally, in 1973, the Spanish Foreign Currency Institute was abolished. Its functions were assigned to the Banco de España (implementation of the foreign exchange policy decided upon by the Government, and all matters pertaining to financial operations with the external sector) and the Directorate General of Foreign Transactions of the Ministry of Trade (commercial loans and foreign investment).

With regard to the regulation of capital movements, the most significant liberalising measures away from the previous, rigid interventionism came about further to the enactment of the 1979 Exchange Controls Act. This regulation remains in force and is basically confined to bringing under its roof all types of operations from which proceeds or payments vis-à-vis the external sector may arise, and to delegating to the Government the specific regulation of each type of operation. In subsequent amendments to the implementing regulations of this act, there began to be a place for generic authorisations whereunder residents could perform an increasingly wider range of foreign transactions. In parallel the Banco de España, in successive circulars, progressively extended the operating scope of entities authorised to operate in the foreign currency markets.

And thus to the current situation. After the Government decision to bring forward the free capital movements originally envisaged for 1993, mention need only be made in connection with exchange controls of the obligation to make all proceeds and payments vis-à-vis the external sector through an authorised bank (this is for statistical and fiscal control purposes). There are no restrictions on banks' operations in foreign currency provided that they do not exceed the risk ceilings imposed for solvency purposes.

To conclude, and although the link to foreign exchange policy is only indirect, it should be mentioned that the Banco de España has been entrusted since 1992 with the legal obligation of preparing the balance of payments (previously the responsibility of the Ministry of Trade).

9. PAYMENT SYSTEMS AND ORGANISATION OF MARKETS

The role played by one of the Banco de España's services, the Money Market Telephone Service, in relation to payment systems and market organisation advises treating these aspects in conjunction.

9.1 Historical background to the payment system

As background data it should be mentioned that, the issue of currency aside, the opening of current accounts at the Banco de España by banks began early this century as soon as the Spanish banking system began to take root. The basic function, however, was not initially related to the payment system but to the undertaking of credit operations, in particular the automatic pledging of government debt, as from 1917, and the rediscounting of bills, from 1921.

A year later, at the behest of the Banking Supervisory Council, the Clearing Houses emerged. These were subject to the Council's authorisation and supervision, and their operating regulations, at the request of the Banking Commissariat, were officially recognised.

In 1946, pursuant to the Second General Banking Act, the currently operating Clearing Houses were already in place: Madrid, Barcelona, Bilbao and Zaragoza. The authorisation to increase this number, the responsibility of the Ministry of Finance, was never used. There were also two Private Clearing Houses, created by the Banco de España in its Valencia and Seville branches. The authorisation to create new private houses, which were to operate under the responsibility of the Banco de España or some private bank, was ceded to the Directorate General of Banking and Stock Markets in 1949, and to the Banco de España in 1962⁽¹⁾.

⁽¹⁾ Savings banks were accorded access to both types of houses in 1971, as were credit co-operatives in 1979.

9.2 The Money Market Telephone Service

The first landmark in the modernisation of the payment system was 1976 when, as support for the incipient interbank market for deposits, the Money Market Telephone Service was created. This Banco de España service was a linchpin both of the subsequent development of the payment system and of the development and entrenchment of money markets in Spain.

9.2.1 Previous situation

To appreciate what this Service has entailed, it is useful to recall how the interbank market for deposits operated prior to the Service being created in 1976. The market was poorly developed and devoid of organisation. A significant number of banks still considered it "undignified" to become indebted to other banks outside their own group. Moreover, the traditional flow of funds from savings banks to banks was largely made on the basis of informal ties rather than of market criteria.

By 1974, however, two of the factors that would prove decisive for developing this market had emerged: the obligatory reserve requirement and the monetary regulation loans of the Banco de España. The latter were initially allocated only among banks at a low interest rate in order to ensure the demand therefor and with maximum limits per entity set in terms of a criterion -their own resources- which had little to do with their individual liquidity requirements. Logically, a poor criterion for the distribution of the total volume of liquidity demanded by the system boosted its redistribution in the interbank market.

Such rudimentary organisation matched the limited development of the market and, in turn, hampered its expansion. Over the course of the morning session operations were by telephone, habitually on a direct-search basis between lenders and borrowers, as brokers would not emerge on this market until several years afterwards. As a result, it was a direct-search market which was scarcely transparent and did not generate valid prices or information on amounts exchanged.

At the close of the morning, when no further operations were envisaged, couriers from the entities which had received funds would do the rounds of the central offices of the lending entities in order to collect the cheques with which the operations pacted were to be settled, depositing them in their current account at the Banco de España before the central bank windows closed. On the maturity of the operations, the couriers' rounds would, conversely, involve collecting the banker's cheques evidencing the refund of the principal plus interest. As a result, market security was affected by a whole range of uncertainties: delays, losses, oversights, procedural defects impeding the cheques being deposited, etc. all bore on the settlement of operations.

To make up for the lack of information, the Banco de España had entered into an agreement with a significant group of banks whereunder the latter voluntarily reported the key data of their lending operations (so as to avoid duplications) in the interbank market, both with other banks and with savings banks. Receiving and then processing the statements lengthened the period before information was available to fifteen days, such information being more representative with regard to interest rates than to amounts traded.

The rudimentary organisation described explains some of the specific features of the Money Market Telephone Service as from its creation, which distinguishes it from other interbank payment networks.

9.2.2 Characteristics

Initially, the Service was open only to banks and savings banks and use of it was voluntary and free of charge. It could only be used to arrange debits and credits in the current accounts open at the Banco de España arising from the settlement of fixed-term loan operations transacted on the interbank market for deposits and for initial amounts expressed in round millions⁽¹⁾.

⁽¹⁾ The remaining payment, remittance or fund transfer operations continued to be transacted via the traditional procedures for several years afterwards.

The security, ease and speed these new procedures entailed for the settlement of all types of operations are self-evident; for very-short-dated treasury operations, however, their use was vital.

Certain singularities the Money Market Telephone Service has evidenced since its creation should be highlighted. The main one, from which the others stem, is that the principal data of the operations conducted are notified to it, rather than it arranging only the gross or net transfers resulting from trading, as is the case in other payment networks. Thus, the Service, though it has no responsibility for the successful outcome of the operations, performs a registration function that benefits the market, extending far beyond a simple transfers service, the causal operation of which is unknown.

In addition to greater security, this registration function gave rise to transparency in a market in which incipient brokerage activity was not conducive to the grouping of prices and did not permit disclosure of the terms and amounts negotiated. Since then, all the information amassed by the Service reverts to the participating entities on the same day and in a duly prepared format. The information also provides a basis for the Banco de España's supervisory tasks and for the preparation of its monetary statistics.

Accordingly, the Money Market Telephone Service is much more than an interbank payment network⁽¹⁾. The significant differentiating feature whereby it receives the key data of the operation originating the movement of balances has been the basis, over time, for the Service progressively taking responsibility for execution, clearing and settlement on the main interbank markets, in addition to other functions relating to the payment system.

In theory and in practice, it is important that both functions should be dealt with separately, however much they may be deeply connected, since the principles and procedures used in its management of the wholesale network of interbank payments, for example, need not be applicable to its conduct as the organising and ruling body of interbank markets.

⁽¹⁾ Indeed, interbank transfers could not be arranged through the Telephone Service until years later.

9.2.3 Market registering, clearing and settling functions

Three markets currently execute, clear and settle their operations via the Service: those for interbank deposits, Banco de España certificates and book-entry government debt (between account-holders). Logically, those entities authorised to operate in these markets may avail themselves of the Telephone Service provided they submit an application and offer, in the Banco de España's opinion, sufficient guarantees of solvency and managerial capacity.

To facilitate registration, clearing and settlement, communications relating to operations are currently received by telephone (orally or by fax), they may not be cancelled or modified, and they must be confirmed before the market closes⁽¹⁾. Normally, communication from both parties to each operation is required. But when operating without knowing the counterparty entity, communication is three-sided: from the broker, who assigns a number to the operation and identifies the two parties, and from each of these parties, making a reference to the number of the operation and to the broker. At the close of the morning, each entity receives a summary detailing the operations it has undertaken and the final balances of the cash and securities accounts it holds open at the Banco de España.

When the markets close, payment orders arise from the clearing of disclosed operations. Before these orders are executed, a check is made to assure the balance in the related securities and cash accounts is sufficient. If this is not the case, extraordinary transfers of securities or cash aimed at rectifying existing overdrafts may be authorised. In specific circumstances the Banco de España may, to resolve such overdrafts, also resort to the balances of any of the securities or cash accounts opened at the central bank by the entity concerned. If the overdrafts are not righted, the orders it has not been possible to execute are communicated to the entities concerned. Logically, in selecting these unmet orders, the Money Market Telephone Service seeks out

⁽¹⁾ For the move from telephonic to electronic communication, a trial run involving the direct interconnection of computers was started up some years back. So far this only provides for the direct transmission of transfer orders by entities and the viewing of their balances in the various accounts they have open at the Banco de España.

those that cause fewest upheavals on the market, avoiding as far as possible the formation of series of insolvent operations so as to obviate system risk.

9.2.4 Interbank network of wholesale payments

The Money Market Telephone Service also runs the wholesale interbank network for transfers of cash and government debt. In other words, it is the vehicle for movement in the balances of the treasury and book-entry debt accounts held by authorised entities at the Banco de España. The Service thus facilitates the settlement of the payment orders that each entity builds up against the remaining entities, as a result of its own and its clients' transactions.

Within these payment orders are those resulting from the clearing of cash balances arising from the clearing of operations transacted in the main Spanish financial markets. All these markets, organised to differing degrees, have clearing procedures both for the financial instrument being traded, which will be settled via the related delivery system, and for money, which is settled by the interbank transfer system managed by the Telephone Service.

Among the cash payment orders which, via the Telephone Service, are settled on the treasury accounts opened at the Banco de España are the following: orders from the interbank deposits market, the book-entry government debt market, the currency markets (between Spanish entities), stock markets, the AIAF (Spanish Bond Dealers' Association) fixed-income market, the official futures and options markets, the FRAs markets, the internal transfers of each entity, interbank transfers, operations processed by the clearing houses and by the various sub-systems of the National Electronic Clearing System (cheques, invoices, bills of exchange, etc.), interventions by the Banco de España to regulate liquidity in the currency market, etc. The Money Market Telephone Service clears all these orders and settles them provided that the treasury accounts involved show a sufficient balance at the end of the day.

9.2.5 Other functions

Besides the aforementioned functions, the Money Market Telephone Service performs others such as the channeling of the Banco de España's interventions in the above markets, auctions, etc.

9.3 The payment system at present

9.3.1 Clearing houses

Returning to the evolution of the payment system, there are currently a total of 51 provincial clearing houses. The Banco de España is a member and president of all of them. The banks operating in each province may belong to the respective clearing houses either as associated entities (in which case they are owners of the house) or as delegate entities.

The houses perform the traditional clearing of cheques, invoices, transfers and trade bills in paper form, along with currency market operations between resident entities (only pesetas). The settlement of the cash balances resulting from all of these is performed, after clearing, in the accounts of the respective entities at the Banco de España. In the Madrid and Barcelona clearing houses, operations are settled with the value date of the day following the exchange of documents, which takes place on the same day they are received by the entities. The operating cycle is thus one day. For the other clearing houses this cycle is two days.

As a half-way stage before fully fledged electronic exchange, the clearing houses introduced simplification procedures throughout the past decade in relation to the traditional process. These ranged from the truncation of cheques and trade bills to the replacement at source of specific documents (invoices, transfers, etc.). These operations would converge at the Interbank Co-operation Centre and be settled via the Madrid Clearing House.

9.3.2 National Electronic Clearing System

The main qualitative gain in the mechanisation of exchanges has been the creation of the National Electronic Clearing System in 1987, which started up in March 1990. The main banks and savings banks belong to this system, in which now virtually all clearing of cheques, transfers, trade bills, standing-order debits, credit and charge cards and foreign currency operations is done using electronic procedures via interconnected computers.

The Banco de España promoted and co-ordinated the creation of this System. It also chairs its advisory commission and provides it with its settlement services. Every day at 10 a.m. the settlements of the exchange made the previous night are booked in entities' accounts via the Banco de España-managed National Settlement Service. The operating cycle is thus less than one day.

9.4 The Book-Entry Government Debt Market

With regard to the Banco de España's role as market organiser, the essential features of two of the markets under its responsibility -the interbank deposits market and the market for Banco de España certificates- were mentioned earlier in connection with the current implementation of monetary policy.

But mention has yet to be made of the essential features of the Book-Entry Government Debt Market, created in 1987, and the plan to integrate the FRAs market into the Money Market Telephone Service.

9.4.1 Creation

The book-entry market arose due to the need for a market with the capacity to absorb and trade efficiently the major volumes of government debt required to finance, under market conditions, the heavy budget deficits that had emerged since the mid-70s.

Notwithstanding the obligations deriving from its role servicing the public debt, the Banco de España was entrusted with the management of this market for two reasons. First, because the fixed-income stock market did not exist in Spain. Since the end of the civil war, virtually all issues of public and private fixed-income securities had been placed by virtue of the compulsory investment requirement on banks and savings banks, remaining frozen thereafter until redemption.

Second, the Banco de España had acquired and built up experience in organising interbank markets for securities dematerialised via book entries; since 1979, the various instruments used in open market operations had been traded on these markets.

9.4.2 Functions of the Banco de España

The functions of the Banco de España in relation to the Book-Entry Government Debt Market are in three areas. The first is the keeping of the central book-entry register.

There are two major groups of accounts in the Central Book-Entry Office. The first, called direct accounts, can be opened by whosoever directly subscribes debt at the auctions arranged by the Banco de España and managed by the Treasury. Holders of these accounts must designate a bank account where the Banco de España can credit returns and redemptions. They are essentially designed as a stable means of holding debt for minor and medium-scale investors. If it is wished to sell the debt recorded in these accounts on the secondary market, it must first be transferred to the accounts of clients of a registered dealer.

For the second group of accounts, only market members can be holders. Entities that can only hold in such accounts debt they own are called account-holders, and those that hold in such accounts an overall balance representing the debt owned by their clients are called registered dealers, some of which are

able to house -duly separated- in their accounts both own and clients' book-entry debt⁽¹⁾.

The central bank's second function is as the governing body of the market, in which there are three fields of trading. Turning first to operations between market members acting as principals, pricing is carried out by telephone or via the money-market brokers' trading screens⁽²⁾. Operations are transacted by phone, either directly or with the participation of brokers. The execution, clearing and settlement of this sub-market involves mobilising the related balances of securities and of cash via the Money Market Telephone Service, from where the price and volume statistics are obtained daily.

From the full-capacity registered dealers a group of entities called primary dealers is selected using objective criteria based on market presence. These have direct access to the "anonymous" pricing and trading network serviced by "blind" brokers (inter-dealer brokers). This is the wholesale segment of the market, designed to provide liquidity to the major operators. Trading (outright spot and forward transactions only) is carried out without knowing the entity offering the counterparty, whereby three different communications to the Money Market Telephone Service are necessary for the execution, clearing and settlement of operations: from the two operating entities, which do not know each other's identity, and from the blind broker, which identifies both. Information from this sub-market is obtained daily.

As the market for individuals' operations is a closed one like all official markets, they must operate in it via the registered dealer they have chosen. This dealer operates offering a counterparty to its client, if it has dual capacity, making a market search for such counterparty or confining itself to taking note, i.e. to transferring or entering the securities traded by its client

⁽¹⁾ This overall balance should match exactly the amounts recorded for the individual accounts held open by the registered dealer for its clients. For obvious reasons, the entry relating to the balances held by non-residents evidences some singularities which come to bear on clearing and settlement.

⁽²⁾ Unlike those operating exclusively on the interbank market for deposits (of which there are only three), these brokers should be considered for legal purposes as agency brokers, registered in the National Securities Market Commission.

without its participation. Here, pricing and trading are fully decentralised. Clearing and settlement are carried out at the level of the registered dealers, depending on the type of operation transacted. The overall balances of each registered dealer's clients' accounts resulting from this operating procedure are received daily by the Banco de España so that the central bank can set about assuring orders are matched. However, the full, itemised information on operations in this sub-market is received weekly by the Banco de España on magnetic tapes sent by each registered dealer.

The third function, clearing and settlement of traded transactions, has already been discussed extensively in connection with the Money Market Telephone Service.

9.4.3 Derivatives markets

A further function of the Banco de España related to financial markets is the result of the emergence of sizable government debt portfolios held by both the public and, in particular, the banking system. The latter's holdings have been increasingly financed by shorter-dated sales under repurchase agreement, evidencing the existence of interest rate risks of a considerable scale. The need to provide for hedging operations against this risk accounts for the emergence of the organised derivatives markets for financial futures and options which, initially, used tradeable government debt as the sole underlying asset. The markets were fostered and initially supervised by the Banco de España.

The first to come on stream was the OMIB options market at end-1989, followed in March 1990 by the MEFFSA futures market. Both availed themselves of the specific regulations governing book-entry government debt. Subsequently, at the end of 1990, these markets were made subject to the provisions of the Securities Markets Act, which enabled them to add underlying assets other than government debt: first, interbank deposits; next, foreign currency; and finally, stock market securities and indices. As a result, the National Securities Market Commission assumed responsibility for their supervision.

9.5 FRAs market

The FRAs (forward rate agreements) market has developed spectacularly in Spain. It began to be of some size in 1986 while still fully disorganised. Nonetheless, two years later, the Money Market Commission (presided by the Banco de España and made up of representatives of the most active entities in the interbank markets) established standard arrangements (known as FRACEMM), which normalised a part of operating procedures, the rights and obligations of the buyer and seller and the means of determining the settlement price.

With this type of FRA, known as "broken date", the market became fully entrenched. Nonetheless, in the search for greater liquidity, "fixed" FRAs emerged shortly afterwards which, moreover, have a standardised commencement date (third Wednesday of March, June September and December) and the term of the theoretical interbank deposit (three months). With both types of FRAs, the market became one of Spain's biggest.

In the quest for greater transparency and legal security, entities were quick to request of the Banco de España that the market be integrated into the Money Market Telephone Service. In this connection the relevant proceedings have commenced and, now the problems raised (particularly that of how the Banco de España should calculate settlement prices, on the basis of firm prices quoted by a randomly selected group of entities) have been resolved, the necessary data processing application has been finalised and is currently at the trial stage. Once trials have been completed, the FRAs market will be integrated into the Money Market Telephone Service.

10. OTHER FUNCTIONS

10.1 Intervention at ailing entities

Throughout its history, the Spanish banking system has faced many critical phases. Among those furthest back are the two years spanning 1847-1848, which gave rise to the merger between the Banco de San Fernando and

that of Isabel II; the ten years from 1864 to 1873, which did away with 15 issuing banks and 22 credit companies; the 1882-1891 decade, which saw 31 banks close; and finally the 1920-1931 period, during which time more than 20 banks fell, mortally impacting the Catalanian banking tradition.

Despite this long series of incidents, when the worst-yet crisis broke in 1977 deposit guarantee funds did not exist and the Banco de España was not authorised to place ailing entities under its official administration. Thereafter, 57 banks, 15 savings banks and 37 credit co-operatives have undergone sufficiently serious crises to merit special treatment extending beyond the Banco de España's acting as lender of last resort.

Given the scale of the crisis, improvisation was necessary on all fronts. In 1978 the Banco de España was authorised -whenever the seriousness of the situation so required- provisionally to designate official administrators at crisis-ridden entities and to suspend temporarily their boards of directors and management.

Although these intervening powers were later refined, the current governing regulations (in the 1988 Act on the supervision and disciplining of credit institutions) still remain insufficient. This is because the procedural flexibility that supervisors of credit institutions require, and the level of discretion that some of their decisions must evidence, are not readily accommodated in Spanish bankruptcy law nor in the rationale underpinning all Spanish legal regulations.

The case of the deposit guarantee funds (which emerged in 1977) was worse, since it was not possible to improvise sufficiently sizable funds to face up to a crisis on such a scale. Accordingly, the Banco de España's participation in solving the crisis -which, although significant, never aroused panic or jeopardised the stability of the system- was especially active in all areas. In particular, considerable advances had to be made to the Deposit Guarantee Fund for Banking Establishments, the worst affected sector. Special aid -for instance, soft credit and exemption from compulsory reserve requirements- had also to be given to entities that took over crisis-ridden banks.

There are currently three deposit guarantee funds: for banks, savings banks and credit co-operatives. Affiliation to the funds is obligatory "de facto". They are overseen by committees presided by the Banco de España and whose representatives form a majority compared with those from the related entities.

In the case of savings banks and credit co-operatives, the habitual financing is from two types of annual contributions: from their affiliates, equal to 1 per mil of deposits, and from the Banco de España, for an equal amount. The current annual contribution by banks is 1.5 per mil, with that by the Banco de España totalling half that amount.

The functions of the three funds are the same and, to perform them, they all act using the same criterion: to help restore an ailing entity to health or to pay insured deposits (PTA 1,500,000 per depositor), selecting the option which proves least expensive for the fund involved.

During 1992, the deposit guarantee fund for banks completed the refund of the special credits received from the Banco de España at the time of the banking crisis. The deposit guarantee fund for credit co-operatives is expected to do likewise in 1994. By then, the general reform of deposit guarantee funds -which is currently under study- will have been finalised.

10.2 Central Credit Register System

The Central Credit Register System originated in 1962 as one of the functions entrusted to the Banco de España under the decree-law that same year nationalising it.

Monthly, all credit institutions supervised by the Banco de España have to send a list of their duly identified accredittees (individuals or companies from the private or public sector) meeting any of the following conditions⁽¹⁾: a) their credit exposure is equal to or more than PTA 4 million; b) their off-

⁽¹⁾ No information need be sent on entities obliged to report to the Central Credit Register System.

balance-sheet exposure is equal to or more than PTA 10 million⁽¹⁾; c) local corporations are involved, irrespective of the amount the risks total; d) the accreditee's position is subject to bankruptcy law (temporary receivership, bankruptcy, moratorium or insolvency).

The information received on the risks assumed is very detailed, including - in addition to amount - type of risk, implementation, currency, term, guarantees, situation (current, past-due, doubtful or non-performing,) etc.

Reporting entities receive information monthly on the total exposure the system as a whole has assumed with each of their accreditees. The Banco de España, meanwhile, uses the Central Credit Register System's data to prepare credit statistics and to analyse the asset quality of the entities supervised by it.

10.3 Statistics and the Central Balance Sheet Office

Homogeneous public balance sheets and profit and loss accounts for banks were first established in the wake of the 1921 General Banking Act. It is currently for the Ministry of Economy and Finance to determine the model these financial statements must follow, while their monthly publication is the responsibility of the Banking Supervisory Council and the Spanish Confederation of Savings Banks⁽²⁾.

The confidential accounting statements that entities must send to the Banco de España were created in 1955, when the Bank was still private. Since then the scope of confidential information has developed to an extraordinary extent; to the point, indeed, where banks and savings banks must now send around 150 different statistical and financial accounting statements at different intervals to the Banco de España. Drawing on these data, and on those obtained in the exercise of its various functions, the Banco de España prepares

⁽¹⁾ Despite the limited scale of these amounts, entities habitually report risks with lower amounts.

⁽²⁾ The Banco de España was made legally responsible for this function in 1973, but in practice this has not occurred.

and publishes the country's monetary and credit statistics, among others. It then incorporates these into the Financial Accounts of the Spanish Economy, for whose preparation it is responsible⁽¹⁾.

Since 1982 the Central Balance Sheet Office has been running at the Banco de España. Non-financial firms voluntarily send their balance sheets and profit and loss accounts in standardised format to this Office in exchange for receiving overall balance sheets -to differing degrees of aggregation- relating to their branch of activity.

10.4 Safeguards for bank customers

The provision of safeguards for bank customers is not explicitly included among the functions entrusted to the Banco de España; but in recent years, on its own initiative and pursuant to various regulations, the central bank has increasingly taken a more prominent role in this connection, acting in three areas.

The first departs from entities' freedom to set interest rates and commissions. Through the regulations in force since 1989, it is sought to ensure transparency in the cost of financial products so that customers are quite clear about which interest rate will be applied to them, the value dates of different transactions and the related commission thereon, this being always understood for financial services actually provided. Before such conditions are applied, therefore, they must be communicated to the Banco de España. Control over the veracity of banking advertising has been regulated since 1949, coming under the Banco de España's remit in 1962.

The second area concerns supervision. Here, along with the usual checks as to "sound banking practices" under regular supervisory inspections, mention should be made of sampling checks aimed specifically at verifying that customer-relations regulations are adhered to.

⁽¹⁾ As earlier stated, since 1992 the Banco de España has also been preparing the balance of payments.

The third area is customer claims. Leaving aside those claims processed directly for court action, the specific procedure in the banking sector involves submitting claims firstly to the customer "ombudsman", a post now existing in every deposit-taking institution. If agreement is not reached, resort may be had to the Banco de España's Customer Claims Service, created in 1988. Having received the related documentation, this Service hears the parties out, studies the case and issues its verdict. The verdict is not a binding one; but if the parties do not accept it, it may be submitted as evidence, substantiated by the Banco de España, in a subsequent appeal by the claimant before the courts.

11. INDEPENDENCE OF THE BANCO DE ESPAÑA

There is an obvious landmark date for addressing the independence of the Banco de España: that of its nationalisation in 1962. Simply expressed, until 1962 the momentum had been increasingly to foment a public presence in the Banco de España, the private status of which was deemed to be one of the causes hampering it from assuming the functions proper to a central bank. After nationalisation and, specifically, in the wake of the stagflation besetting the Spanish economy in the mid-seventies, there were increasing calls for greater independence for the Banco de España in monetary policy decision-making.

11.1 The period to nationalisation

There was actually a public presence in the forerunners to the Banco de España from the very outset, namely the existence of a royal commissioner and the royal appointment of the governor, from a short list of three proposed by the shareholders' meeting. But it was not until the proclamation of the Second Republic that the most significant changes began⁽¹⁾. In 1931, the 1921 General Banking Act was partly amended. The State could now appoint three of its representatives to the General Council of the Banco de España and supervise

⁽¹⁾ Nonetheless, the Treasury's share in the Banco de España's profits was increasingly greater as from 1921.

in-house its accounts via auditors from the Ministry of Finance. This same Ministry took responsibility for setting the rediscount interest rate and for managing foreign exchange market intervention.

The public presence in the Banco de España increased after the civil war when, in 1942, posts for two specialist attachés to the Governor were instituted, thus forming a Government Delegation, with the right to vote on any resolution, and creating a State Inspection Service at the Banco de España. A further step was taken further to the 1946 General Banking Act when the public presence on the Bank's General Council became a majority and the General Shareholders' Meeting was reduced to a body devoid of decision-making powers.

With regard to regulation, in 1938 the competence of the Ministry of Finance to "determine the general rules of credit policy dating from 1931" was ratified. This principle was confirmed by the 1946 General Banking Act - wherein no mention was even made of monetary policy- in the following terms: "The general rules of credit policy shall be dictated by the Ministry of Finance further to the resolution of the Council of Ministers. The Minister of Finance, duly informed by the Banco de España and the Banking Supervisory Council, shall be responsible for:

a) Indicating the maximum interest rate payable on current accounts, deposits and other similar operations;

b) Setting the maximum and minimum interest rates and commissions on lending operations and the conditions of their application. The difference between both interest rates shall, in any event, be set on the basis of the cost of money. Nonetheless, changes may be made to rates and conditions in certain financial centres or for certain sectors or activities of the national economy when special circumstances so advise it (...).

c) Stipulating the form in which the balance sheet and profit and loss account statements of Banks and Bankers operating in Spain shall be prepared;

d) Laying down general binding rules for the distribution of banking dividends".

As a result, the Banco de España's scope for independent conduct was very limited.

11.2 Nationalisation

The nationalisation of the Banco de España came about pursuant to the legislation enacted in 1962. The preamble to this Act established clearly the rationale that would underpin the new regulation of the Banco de España: "The Spanish State not accepting the principle of economic neutrality, monetary authority cannot be delegated to the issuing bank but shall be exercised permanently by the Government through the Minister of Finance; in the technical realm, however, it is advisable to entrust the implementing details of the policy pursued to the Banco de España, providing it with an autonomous organisational structure with the responsibility, independence and authority proper to its eminent mission to co-operate with, inform and advise the Government on monetary and exchange rate policy and on private banking discipline".

To trace the growing independence of the Banco de España after such an inauspicious start, discussion will first focus on how its functions have progressively been defined, with particular reference to monetary policy. A second aspect will address how changes in the regulation of its governing bodies have occurred.

11.3 Definition of the functions of the Banco de España

11.3.1 In 1962

With regard to monetary policy, the aforementioned 1962 Act stated that: "Authority for monetary and credit matters shall rest with the Government which shall, through the Minister of Finance, lay down the guidelines for the Banco de España and the various Credit Agencies to follow at each stage, thus pursuing monetary and credit policy in the manner most suited to the country's interests".

In keeping with these principles, the 1962 decree-law nationalising the Banco de España entrusted it with the following functions:

- a) Issue, status and management of legal tender.
- b) Treasury service to the State and servicing of the national debt.
- c) Bankers' bank.
- d) Supervision and disciplining of private banks.
- e) Preparation of monetary and credit statistics.
- f) Running of the Central Credit Register System, for risks derived from credit institutions' lending operations.
- g) Information and counsel to the government on money and credit matters.

The above listing of these functions evidences the absence of any reference to monetary policy other than the mention of counsel to the Government, which is regulated as follows: "The Banco de España shall act as an advisory body to the Government on money and credit matters and shall report to it, through the Ministry of Finance, both on matters in which its ruling is mandatory and on those in which its particular interpretation is requested. It may, on its own initiative, also convey its opinion to the Government on those matters which, within the scope of its advisory functions, it deems appropriate".

11.3.2 In 1980

The functions of the Banco de España were not re-defined until 1980, when legislation regulating its governing bodies was promulgated. In the span of almost twenty years separating both sets of legislation, and in particular since the outset of the seventies, the Bank gradually gained bigger measures of independence in practice, though the regulatory framework lagged much further behind. Indicatively, the Banco de España was unable to start allocating via auction its monetary regulation loans until 1978, because it could not freely set the interest rates on its credit's operations with the entities under its supervision.

The first article of the 1980 Act stipulated that "The Banco de España is a public corporation with its own legal status and full public and private capacity, which, for compliance with the aims indicated in the third article, shall act independently of the State, within the limits established in this Act".

Undoubtedly, this wording must be considered as a legacy from the early versions of the draft law, in which its functions were regulated; except in relation to monetary policy, the legal text does not stipulate any of the above-mentioned limits⁽¹⁾. Indeed, nor were the "functions" mentioned as such, since they are listed on mention of the "purpose" of the Bank as follows: "The Banco de España shall be entrusted with the placement in circulation of coined money and the issue of banknotes of legal tender, and administer and regulate the circulation of coins and banknotes, in accordance with the requirements of the economy; it shall service free of charge the public debt and manage the State's accounts; it shall act as the bankers' bank; it shall centralise metallic and foreign currency reserves and the movement of foreign proceeds and payments and shall conduct monetary policy both domestically and externally in accordance with the general objectives set by the Government, implementing it as it deems most appropriate for attaining the stated ends, particularly that of safeguarding the value of the currency. The Banco de España shall also perform functions relating to the discipline and supervision of the credit and savings institutions registered with it and whatsoever other functions legally entrusted to it. The Banco de España shall inform and advise the Government on all these matters, taking the initiative, if it so wishes, in the preparation of reports whenever it deems it advisable for the common interest. It shall likewise report to the Parliament on the latter's request, following the channels established in this connection".

Accordingly, the autonomy of the Banco de España in relation to monetary policy is confined to policy development and implementation, strictly as part of the goals set by the Government.

⁽¹⁾ The same Act included an order to the Government to send "a draft law to Parliament updating and finalising the provisions relating to the nature, legal status, functions and conduct of the Banco de España". This order has been met in 1993 with the Draft Act on Autonomy.

11.3.3 Draft Act of Autonomy of the Banco de España

These limits have disappeared in the Draft Act of Autonomy of the Banco de España, which is expected to be approved and come into force in 1994. Briefly, the listing of the Bank's functions contained in it is as follows:

1) The Banco de España shall define and implement monetary policy with the primary aim of attaining price stability.

Notwithstanding this objective, monetary policy shall support the Government's general economic policy.

2) Safeguarding the aspects provided for in the preceding point, the Banco de España shall perform the following functions:

- a) Hold and manage the foreign currency reserves.
- b) Promote the sound functioning and stability of the financial system and, in particular, the payment system.
- c) Determine the total amount of notes and coins to be issued and place it in circulation, performing on the State's behalf all other functions entrusted to it with regard thereto.
- d) Supervise, pursuant to the provisions in force, credit institutions' solvency, conduct and compliance with specific regulations, along with whatsoever other entities and financial markets whose supervision has been assigned to it.
- e) Provide cash management services and act as financial agent for the public debt under the terms pactured with the Treasury.
- f) Advise the Government, prepare and publish statistics related to its functions, and draft relevant reports and studies.
- g) Perform the remaining tasks attributed to its remit under legislation.

11.4 Governing bodies of the Banco de España

A second indicator of the degree of autonomy attained by a central bank is the composition, appointment and term of office of its governing bodies, and the reasons for departure and dismissal therefrom. The regulation of these matters is detailed in figures 4, 5 and 6, which address the content of the three Acts mentioned when referring to its functions: those of 1962 and 1980 and the draft legislation of 1993.

It may be readily observed that the evolution of the two indicators coincides: from the absolute subordination of the governing bodies of the Banco de España to the Government (through the Ministry of Finance) evident in the 1962 regulations, the 1980 legislation represents a significant advance, although the results are far from satisfactory. Lastly, the regulations envisaged in the draft 1993 Act are fully consistent with the autonomy of the Banco de España in monetary policy matters and with the prohibition on it financing the public sector.

11.5 Accountability of the Banco de España

The current procedures whereunder the Banco de España is made accountable date back to its nationalisation, although the 1980 legislation on its status and scope (Ley de Organos Rectores del Banco de España) made some amendments.

One form of Parliamentary control is exercised via the appearance several times a year of the Governor, in particular before the Parliamentary Committee on Economic Affairs and the Monetary Policy Sub-Committee.

The Banco de España's annual budget is prepared by its Executive Council and approved by its General Council. Its annual accounts (balance sheet and profit and loss account) are also prepared by the Executive Council. The government, at the proposal of the Ministry of Economy and Finance, annually designates a commission drawn from members of the General Council which makes an internal audit of the Central Bank's accounts. Accompanied by this Commission's report, the annual accounts are submitted to the General Council and, once approved, are sent to the Ministry of Economy and Finance and to the Spanish National Audit Authority. This latter body is also responsible for making periodic external audits of the Banco de España.

FIGURE 4

GOVERNING BODIES OF THE BANCO DE ESPAÑA FROM 1962 TO 1980

BODY/POST	APPOINTED BY	TERM OF OFFICE	DISMISSAL FROM OFFICE
GOVERNOR	Government	Unspecified	Unconstrained
DEPUTY GOVERNORS (1)	Government	Three years	Disciplinary reasons
DIRECTORS-GENERAL	Minister of Finance	Unspecified	Disciplinary reasons
EXECUTIVE COUNCIL			
<ul style="list-style-type: none"> • Governor • Deputy Governor • Three council members of the group (*) 	Minister of Finance	Two years	Unconstrained
GENERAL COUNCIL			
<ul style="list-style-type: none"> • Governor • Deputy governors • Five government representatives (*) • Two private banking representatives • One representative from the Medium- and Long-term Credit Institute • One representative from the savings-Bank Credit Institute • Four Trade Union Representatives • One employee representative 	Government Minister of Finance Minister of Finance Minister of Finance Trade Union Minister of Finance	Unspecified Unspecified Unspecified Unspecified Unspecified	Unconstrained Unconstrained Unconstrained Unconstrained Unconstrained Unconstrained

(1) Initially three; after 1967, two.

FIGURE 5.- GOVERNING BODIES OF THE BANCO DE ESPAÑA (Act 30 dated June 21st 1980)

NAME AND COMPOSITION	APPOINTED BY	TERM OF OFFICE	DISMISSAL	REQUIREMENTS	SITUATIONS OF INCOMPATIBILITY	MAIN AREAS OF COMPETENCE
GOVERNOR	HEAD OF STATE (ON GOVERNMENT'S PROPOSAL)	4 YEARS RENEWABLE	-END OF TERM OF OFFICE -RESIGNATION ACCEPTED -REMOVED BY THE GOVERNMENT FURTHER TO PROCEEDINGS INITIATED BY THE MINISTER OF ECONOMY AND FINANCE	-SPANISH NATIONALITY, OF FULL AGE, ACKNOWLEDGED COMPETENCE IN ECONOMIC MATTERS	-ELECTED MEMBER OF PARLIAMENT OR SENATOR -WHATEVER ACTIVITY NOT INHERENT TO THE POST -WORKING IN PRIVATE INSTITUTIONS AND LEASING THEN TWO YEARS AFTER HOLDING POST	-REPRESENTATION OF BANCO DE ESPAÑA -SUPREME AUTHORITY FOR ITS MANAGEMENT -TO DECIDE AND AGREE TO THE EXECUTION OF THE BANK'S OPERATIONS, FURTHER TO AGREEMENT WHERE NECESSARY, OF THE EXECUTIVE COUNCIL -CASTING VOTE WITH REGARD TO VOTING BY GENERAL AND EXECUTIVE COUNCILS
DEPUTY GOVERNOR	GOVERNMENT (ON THE PROPOSAL OF THE MINISTRY OF ECONOMY AND F.)	4 YEARS RENEWABLE	AS FOR GOVERNOR	AS FOR GOVERNOR	AS FOR GOVERNOR	-TO STAND IN FOR THE GOVERNOR -TASKS DELEGATED BY THE GOVERNOR OR ENTRUSTED TO POST BY INTERNAL REGULATIONS
GENERAL COUNCIL -GOVERNOR (CHAIRMAN) -DEPUTY GOVERNOR	BY DECREE					
SIX COUNCIL MEMBERS	GOVERNMENT	3 YEARS RENEWABLE				
ONE COUNCIL MEMBER	BE EMPLOYEES					
DIRECTORS-GENERAL OF THE BE (≤ 4)	GOVERNOR	1 YEAR RENEWABLE	AS FOR GOVERNOR	AS FOR GOVERNOR -10 YEARS OF SERVICE	WORKING IN PRIVATE FINANCIAL INSTITUTIONS	-TO APPROVE THE GUIDELINES FOR THE CONDUCT OF THE BANCO DE ESPAÑA -TO APPROVE THE INTERNAL REGULATIONS AND REPORT ON BANKING RULES -TO APPROVE THE GENERAL ACCOUNTS AND ANNUAL REPORT -TO ADVISE THE GOVERNMENT AND APPROVE THE GENERAL REPORTS SUBMITTED TO IT -TO APPROVE PROPOSALS FOR MAJOR PENALTIES -TO ASSIST THE GOVERNOR -PERIODICITY OF SITTINGS
DIRECTOR-GENERAL OF THE TREASURY AND FINANCIAL POLICY			UPON LOSS OF POST GIVING RISE TO ORIGINAL APPOINTMENT			
DIRECTOR-GENERAL OF THE BUDGET						
NON VOTING MEMBERS: -GENERAL SECRETARY OF THE BANCO DE ESPAÑA -OTHER GENERAL DIRECTORS OF THE BE						-MONTHLY MEETING CONVENED BY THE GOVERNOR -ON THE PROPOSAL OF HALF OF ITS MEMBERS
EXECUTIVE COUNCIL -GOVERNOR -DEPUTY GOVERNOR						
FIFTEEN COUNCIL MEMBERS OF THE SIX APPOINTED BY THE GOVERNMENT	ELECTED BY THE GENERAL COUNCIL			FULL AVAILABILITY AND READINESS FOR COUNCIL DUTIES		-TO IMPLEMENT THE GUIDELINES OF THE GENERAL COUNCIL -TO PREPARE REPORTS TO THE GOVERNMENT -TO PREPARE THE ANNUAL REPORT, GENERAL ACCOUNTS AND ANNUAL REPORT -TO PREPARE INTERNAL REGULATIONS -TO APPOINT THE BANCO DE ESPAÑA'S SENIOR OFFICIALS -TO RESOLVE ADMINISTRATIVE AUTHORISATIONS -TO EXERCISE PENAL JURISDICTION
ONE BANCO DE ESPAÑA DIRECTOR-GENERAL -NON VOTING: GENERAL SECRETARY OF THE BE						

FIGURE 6.- GOVERNING BODIES OF THE BANCO DE ESPAÑA (Draft Autonomy Act)

NAME AND COMPOSITION	APPOINTED BY	TERM OF OFFICE	DISMISSAL	REQUIREMENTS	SITUATIONS OF INCOMPATIBILITY	MAIN AREAS OF COMPETENCE
<u>GOVERNOR</u>	KING (ON THE PROPOSAL OF THE HEAD OF GOVERNMENT)	6 YEARS NON-RENEWABLE	-END OF TERM OF OFFICE -RE-SIGNATION -ON REACHING AGE OF 70 -ON REACHING AGE OF 75 -ON REACHING AGE OF 80 -ON REACHING AGE OF 85 -ON REACHING AGE OF 90 -ON REACHING AGE OF 95 -ON REACHING AGE OF 100 -ON REACHING AGE OF 105 -ON REACHING AGE OF 110 -ON REACHING AGE OF 115 -ON REACHING AGE OF 120 -ON REACHING AGE OF 125 -ON REACHING AGE OF 130 -ON REACHING AGE OF 135 -ON REACHING AGE OF 140 -ON REACHING AGE OF 145 -ON REACHING AGE OF 150 -ON REACHING AGE OF 155 -ON REACHING AGE OF 160 -ON REACHING AGE OF 165 -ON REACHING AGE OF 170 -ON REACHING AGE OF 175 -ON REACHING AGE OF 180 -ON REACHING AGE OF 185 -ON REACHING AGE OF 190 -ON REACHING AGE OF 195 -ON REACHING AGE OF 200	-SPANISH NATIONALITY -COMPETENCE IN THE FIELD OF MONETARY OR BANKING MATTERS	-HIGH-RANKING GOVERNMENT OFFICIAL -ACTIVITY IN THE POST-BUSINESS -SURRENDERING (INCL. DATE FAMILY MEMBERS) IN SUPERVISED ENTITIES OR COMPANIES WORKING IN ANY ACTIVITY RELATED TO CREDIT INSTITUTIONS OR SECURITIES MARKETS AT LESS THAN TWO YEARS AFTER HOLDING POST	-TO LEAD AND MANAGE THE BANCO DE ESPAÑA AND PRESIDE OVER ITS GOVERNING COUNCIL -TO REPRESENT THE BANCO DE ESPAÑA BEFORE THE LEGAL AUTHORITIES AND INSTITUTIONS, AND IN PARTICULAR BEFORE THE EUROPEAN MONETARY INSTITUTE AND THE EUROPEAN SYSTEM OF CENTRAL BANKS
<u>DEPUTY GOVERNOR</u>	GOVERNMENT (ON THE PROPOSAL OF THE GOVERNOR OF THE BANCO DE ESPAÑA)		-PROPOSAL OF THE GOVERNOR OF THE BANCO DE ESPAÑA'S GOVERNING COUNCIL -ON REACHING AGE OF 70 -ON REACHING AGE OF 75 -ON REACHING AGE OF 80 -ON REACHING AGE OF 85 -ON REACHING AGE OF 90 -ON REACHING AGE OF 95 -ON REACHING AGE OF 100 -ON REACHING AGE OF 105 -ON REACHING AGE OF 110 -ON REACHING AGE OF 115 -ON REACHING AGE OF 120 -ON REACHING AGE OF 125 -ON REACHING AGE OF 130 -ON REACHING AGE OF 135 -ON REACHING AGE OF 140 -ON REACHING AGE OF 145 -ON REACHING AGE OF 150 -ON REACHING AGE OF 155 -ON REACHING AGE OF 160 -ON REACHING AGE OF 165 -ON REACHING AGE OF 170 -ON REACHING AGE OF 175 -ON REACHING AGE OF 180 -ON REACHING AGE OF 185 -ON REACHING AGE OF 190 -ON REACHING AGE OF 195 -ON REACHING AGE OF 200			-TO STAFF IN FOR THE GOVERNOR GOVERNOR OR INTERNAL REGULATIONS
<u>GOVERNING COUNCIL</u> -GOVERNOR -DEPUTY GOVERNOR			-INCOMPATIBILITY ARISING DURING TERM OF OFFICE -PROSECUTION	-SPANISH NATIONALITY -COMPETENCE IN ECONOMICS OR LAW		-TO APPROVE GUIDELINES OF CONDUCT AND TO SUPERVISE COMPLIANCE -TO APPROVE REPORTS AND CIRCULARS -TO APPROVE THE BUDGET ACCOUNTS AND PROPOSE THE DISTRIBUTION OF PROFITS -TO APPROVE DISCIPLINARY PENALTIES UNDER THE BANCO DE ESPAÑA'S REMIT BEFORE THE BANK
-SIX COUNCIL MEMBERS	GOVERNMENT (ON THE PROPOSAL OF THE MINISTER OF FINANCE AFTER CONSULTATION WITH THE GOVERNOR OF THE B.E.)	8 YEARS NON-RENEWABLE			-WHATEVER ACTIVITY IMPEDING ON THEIR DUTIES -INTERESTS OR CAUSING CONFLICT OF INTERESTS OR ENABLING PRIVILEGED INFORMATION TO BE USED FOR THE GOVERNOR AND DEPUTY GOVERNOR	
-DIRECTOR-GENERAL OF THE TREASURY AND FINANCIAL POLICY -DEPUTY CHAIRMAN OF THE COUNCIL OF MARKET COMMISSION				-NO VOTE IN MATTERS PERTAINING TO MONETARY POLICY AND NOTE ISSUE		
NON VOTING: -DIRECTORS-GENERAL -GENERAL SECRETARY OF THE BANCO DE ESPAÑA						
<u>EXECUTIVE COMMISSION</u> -GOVERNOR -DEPUTY GOVERNOR						-TO IMPLEMENT MONETARY POLICY -TO RESOLVE ADMINISTRATIVE AUTHORIZATIONS -TO DECIDE UPON THE BANCO DE ESPAÑA'S OPERATIONS -TO SUBMIT PROPOSALS TO THE GOVERNING COUNCIL IN THOSE AREAS OF ITS COMPETENCE -TO ORGANIZE THE BANK AND APPOINT ITS STAFF
-TWO COMMISSION MEMBERS	GOVERNMENT (ON THE PROPOSAL OF THE GOVERNOR OF THE B-DE ESPAÑA)	3 YEARS RENEWABLE				
NON VOTING: -DIRECTORS-GENERAL -GENERAL SECRETARY OF THE BANCO DE ESPAÑA						

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