

# Lessons from Europe on the Limits of Central Bank Independence

*Mandate, Tools, and Accountability in Practice*

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Hoover Monetary Policy Conference  
Stanford, May 2026

# Independence requires a package

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Cochrane (2026):

- a limited **mandate**
- limited **tools**
- meaningful **accountability**

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The ECB has the narrow mandate, the strong independence, and the treaty-level prohibition on monetary financing the “Hoover view” (Tooze, May 2026) has advocated.

# Three ways independence leaks

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## I. Fiscal dominance

Yield management becomes  
monetary policy

## II. Financial dominance

Emergency tools become  
permanent

## III. Climate dominance

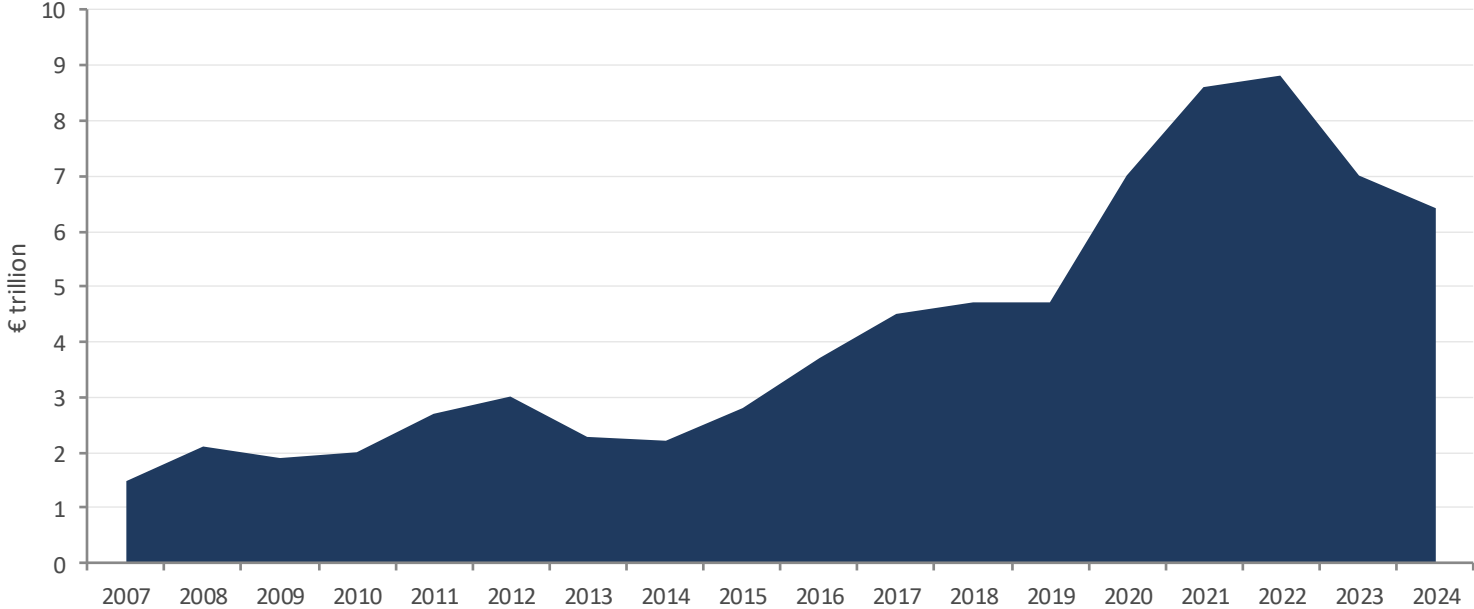
Transmission channels turn  
into mandates

# I. Fiscal dominance

*Bank tools leaked into fiscal policy*

# A silent fiscal expansion

From €1.5tn to €8.8tn: the ECB's silent fiscal expansion



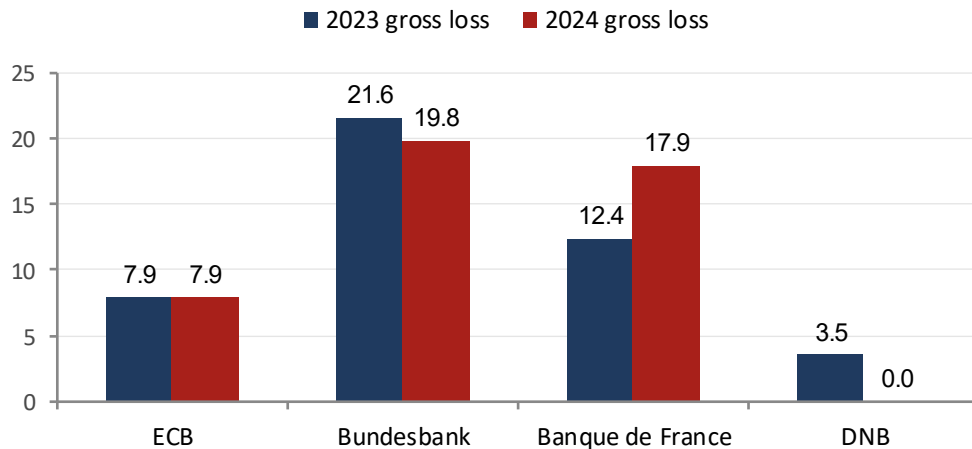
Source: ECB consolidated weekly financial statements. Total Eurosystem assets, end-of-year, € trillion.

# Mechanism: a duration swap on public-sector debt

When the ECB buys a 10-year bond and pays with overnight reserves:

- public-sector liability switches from **10-year fixed** to **overnight floating**
- bondholders sold at peak prices and kept the gain
- taxpayers now pay the policy rate on every reserve euro
- When rates rose from 0% to 4%, the four largest Eurosystem NCBs lost over €90bn combined (2023–2024)

Long-fixed assets meet variable short liabilities (€ billions)



## Fiscal action became redistribution without votes

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ECB fiscal action is also **cross-country redistribution**

- PEPP flexibility (capital-key deviations)
- TPI announced 2022, no exit clause
- ANFA national-asset portfolios
- TARGET2 imbalances

Country	High-spread counterfactual	Approx. 2023-GDP-equivalent € amount
<b>Germany pays</b>	<b>13.2% of GDP</b>	<b>≈ €555bn</b>
<b>Italy receives</b>	<b>8.1% of GDP</b>	<b>≈ €173bn</b>
<b>Spain receives</b>	<b>10.5% of GDP</b>	<b>≈ €158bn</b>

Chien, Jiang, Leombroni & Lustig (2025): the implicit transfers are *large*. A lot of it not to taxpayers, but to local banks.

# The surplus will not arrive

**None of the high-debt sovereigns is delivering surplus needed to stabilize today, and aging will widen the gap.**

*(France 1.3, Italy 2.5, Spain 2.4, Belgium 1.8 of GDP. Germany alone is near balance.)*

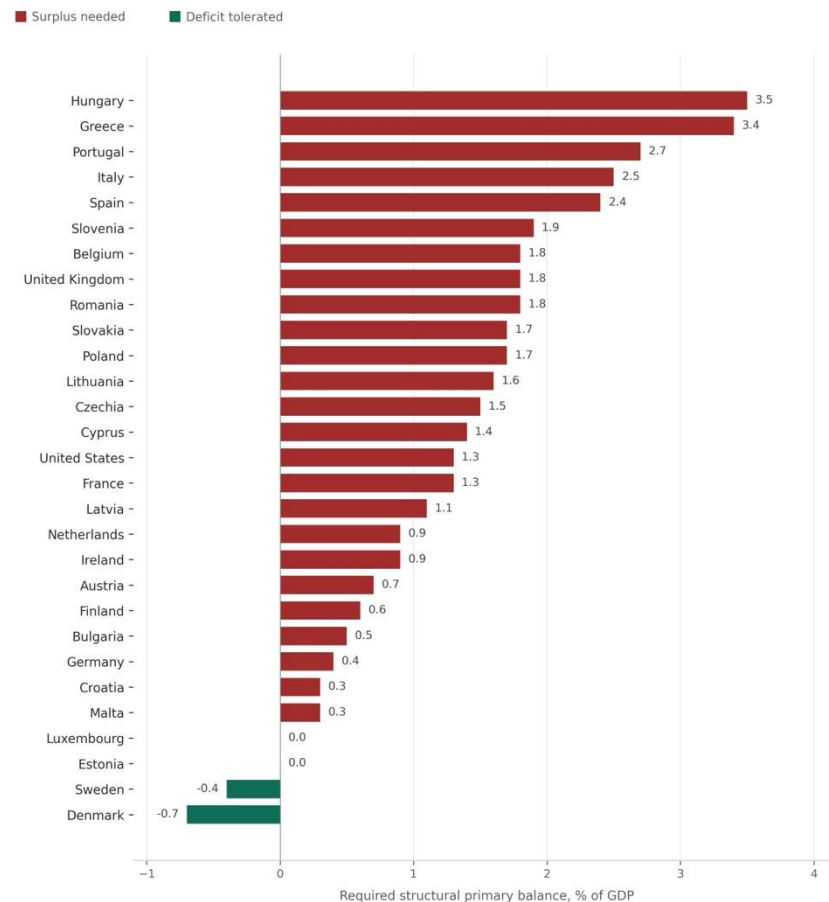
If the surplus does not arrive from fiscal policy, the pressure shifts to the ECB.

Source: Bruegel Working Paper 28/2025, Table 1, column 4 (SPB\*); based on Oct 2025 WEO

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## Structural primary balance required to stabilise debt

Percent of GDP, ranked by size of required surplus



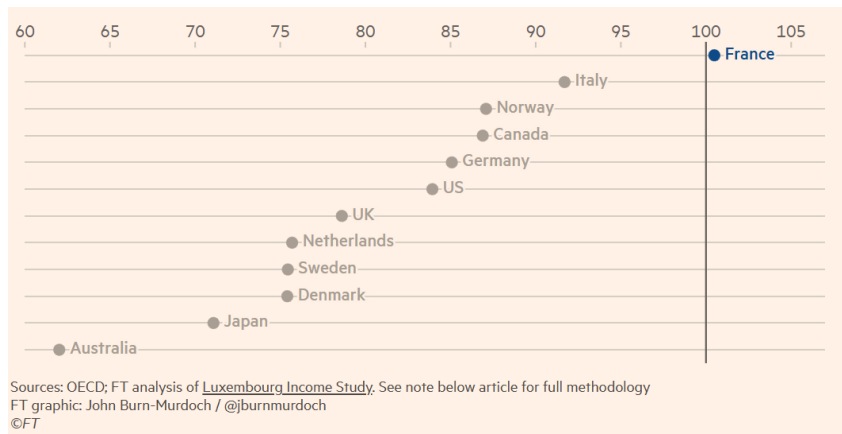
Note: Primary balance that countries would need to achieve by 2031 to stabilise debt within 20 years with a 70 percent probability.

Source: Bruegel Working Paper 28/2025, Table 1, column 4 (SPB\*); based on October 2025 IMF World Economic Outlook data.

# Pension arithmetic

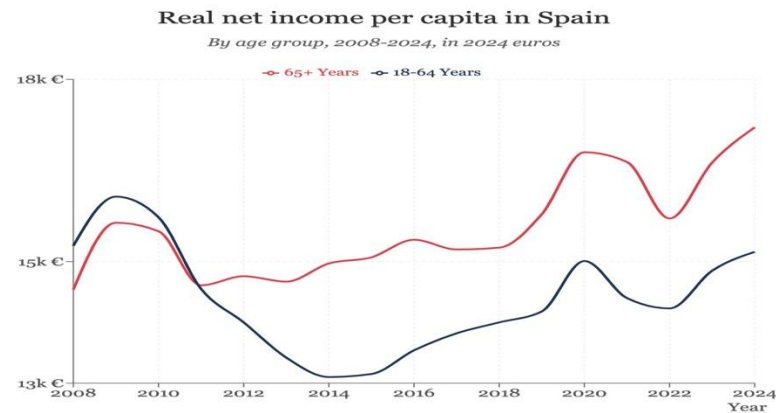
## France: pensioners earn more than working-age adults

Income of those over 65, with median worker = 100.



## Spain: all the growth goes to retirees

Real net income per capita, by age group, 2008–2024.



When the pension equals the salary, the pension system absorbs not only every cyclical surplus, but **every productivity gain** the working economy generates.

Sources: FT, John Burn-Murdoch (Sept 2025), drawing on OECD and Luxembourg Income Study; Spain: Pieter Garicano, Silicon Continent, drawing on INE.

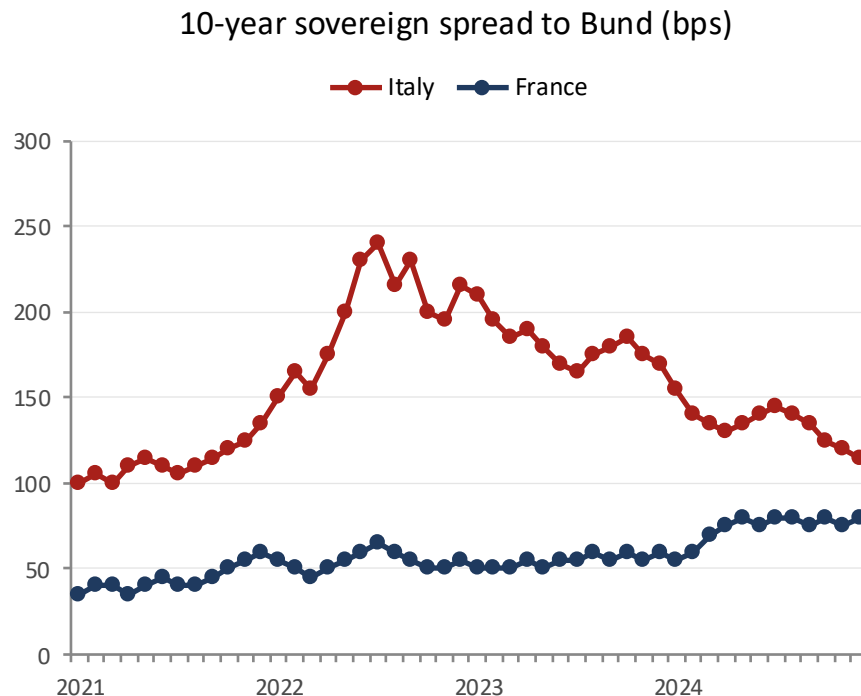
# France: pension reform reversed, November 2025

## What happened

- 12 November 2025: Assembly suspends the 2023 reform.
- National Rally and the left voted together to block budget
- Retirement age moves back from 64 to 62. Funding gap returns.

## What the market did

- Market knows the spread is bounded.
- **ECB acts in the shadow**. TPI does not need to be triggered to discipline pricing.



Source: Bloomberg, 10-year sovereign yields. Italy: €220bn Superbonus (12% of GDP). France: 6.1% deficit. TPI announced July 2022

# The political taboo is gone

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## From the left (Mélenchon, France)

Drop the 3% deficit and 60% debt rules.

Have the ECB lend to states for “sustainable” activities.

Cancel Covid debt for the social and ecological transition.

## From the right (Bardella, France)

French debt near 116% of GDP — ECB discussion unavoidable.

Pairs the demand with a 5-year growth plan, claiming stability not crisis.

His warning: *“If the French economy breaks, the entire euro area breaks.”*



***Both wings now treat ECB action on sovereign debt as a permitted tool, not a taboo.***

Sources: Melenchon2022.fr; The Economist (5 November 2025).

# ECB has no good option

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Demographics, pension promises, and political reversal converge: the required surpluses will not be delivered. Two options remain, neither good.

## Option A: hold the line on inflation

Raise rates as needed to hit 2%.

Risk: aging sovereigns cannot service debt at the resulting yields.

## Option B: keep yields manageable

TPI, asset purchases, or implicit yield management.

Cost: price stability gives way whenever a member state is fiscally stressed.

**Fiscal dominance without monetary financing — limited tools failed.**

## II. Financial dominance

*Financial stability is the same pattern: emergency tools survive because the political architecture cannot absorb losses.*

# TLTRO: crisis subsidy becomes standing instrument

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Targeted Long-Term Refinancing Operations: emergency loans to banks, justified during the 2011–2014 sovereign crisis.

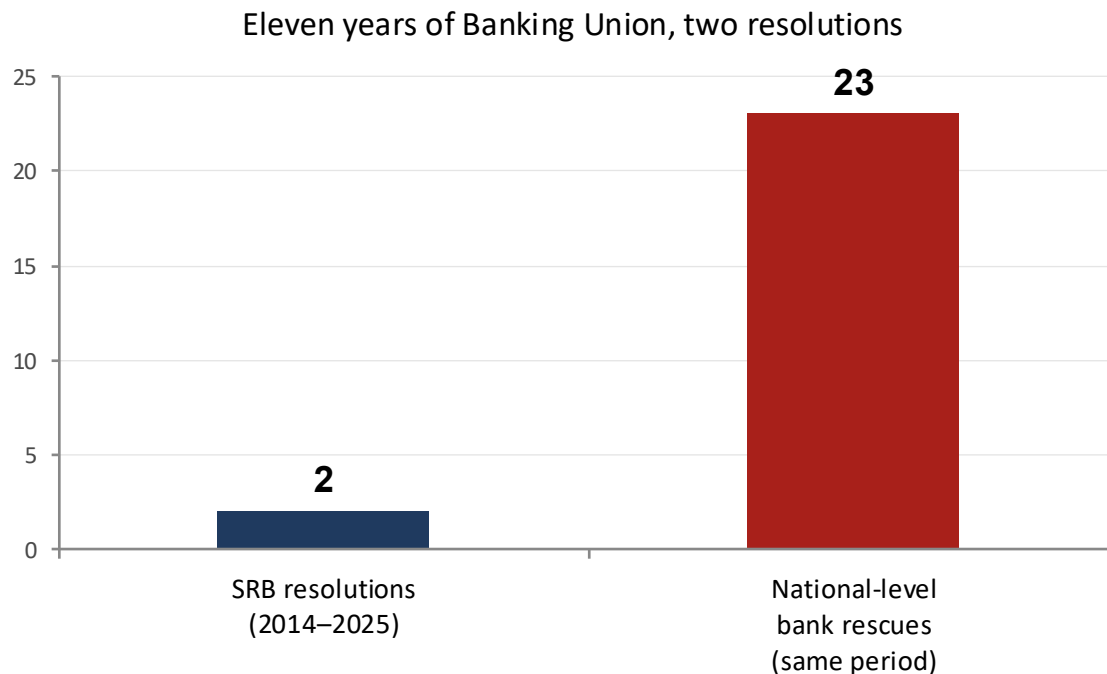
Continued for a decade. At one point, banks could borrow from the ECB at  $-1\%$  and redeposit the same money at the ECB at  $-0.5\%$ : **a risk-free 50bp carry.**

*“The issue is not whether there is a subsidy or not; there is a subsidy. The issue is whether the TLTRO fulfils monetary policy objectives.”*

— Mario Draghi, ECB press conference, March 2019

# Resolution: formal architecture exists but is not used

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Sources: SRB resolution decisions database; national resolution authorities; author's count. National column includes MPS, Veneto banks, NordLB, Greensill, Sberbank Europe national arms.

# Why the architecture cannot be used: no deposit insurance

## The political-economy story:

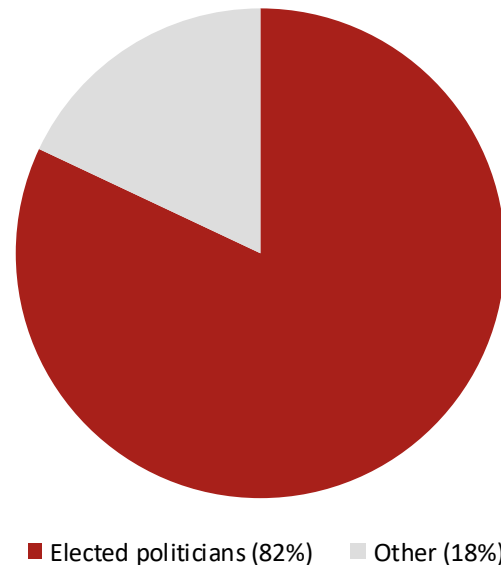
Germany's 359 Sparkassen control €2.5tn in assets.

**82%** of board chairs are elected officials (Véron & Markgraf 2024).

In NRW, Sparkassen fees average **12% of total income** for the politicians who chair them.

*Banking Union failed not because Frankfurt lacked authority, but because Berlin protects banks run by its own politicians.*

Who chairs Germany's 359 Sparkassen?



Source: Véron & Markgraf (2024).

# III. Climate dominance: the mandate is elastic

*A single primary mandate is not protective if the institution defines its own transmission channel*

# Two doors

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Concrete ECB climate measures (July 2021 action plan; July 2022 detailed package):

- Tilt of corporate bond holdings towards better-rated climate issuers (Oct 2022; intensified Feb 2023)
- Climate factor in the collateral framework
- Climate-related disclosure requirements for collateral issuers
- Climate risk stress tests (Banking Supervision, 2022)

## **Door 1: “secondary objectives”**

Article 127(1) TFEU: “without prejudice to price stability,” the ECB shall support the general economic policies of the Union.

## **Door 2: “transmission channel”**

Climate risks affect financial stability, financial stability affects transmission, transmission affects the policy stance.

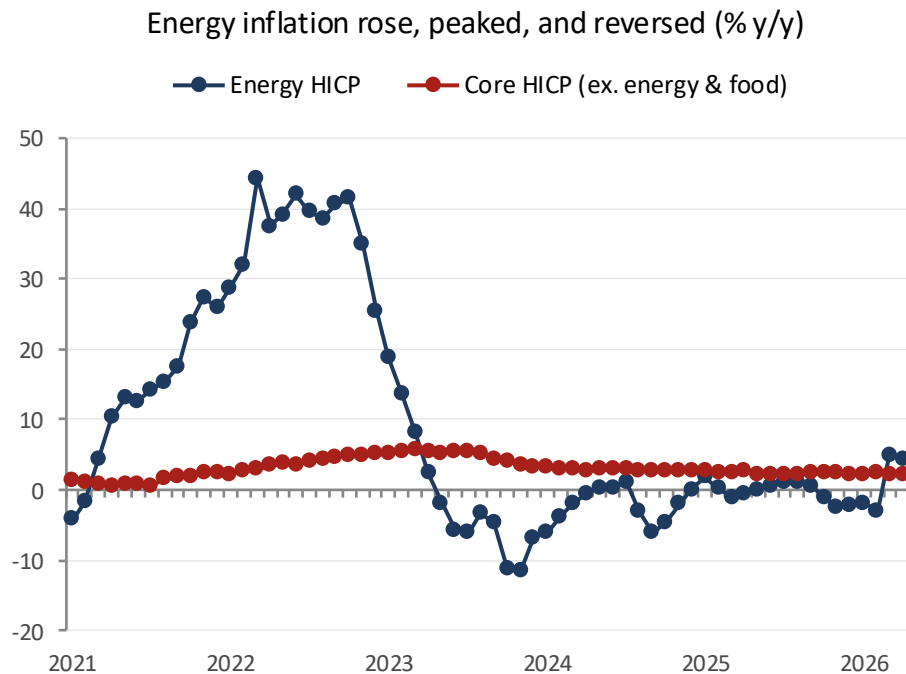
# The rhetoric for the additional (climate) mandate

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Elderson, ECB Blog, April 2026:

- The 2021–2022 inflation surge was “fossilflation”
- Imported fossil fuels were the principal vector
- Energy peaked at +44% y/y in March 2022; headline at 10.6% in October
- A faster clean-energy transition would weaken the link between domestic prices and global energy markets
- “From a central banking perspective, the answer is clear”

# The 2022–2024 disinflation tests the mechanism



## ECB:

A faster transition would still have helped: it lowers the variance of future shocks and the depth of the next peak.

## Evidence:

Headline inflation fell from 10.6% (Oct 2022) to 2.4% (Dec 2024) with no material change in Europe's fossil-fuel share.

Source: Eurostat (HICP, monthly y/y); ECB Data Portal. Energy peaked at +44% (Mar 2022), trough at -12% (Nov 2023). Structural fossil dependence over the same period was broadly unchanged.

## Relevance is not remit

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- Relative-price shocks are not automatically a mandate: price stability is medium-term, and temporary deviations are allowed unless shocks become persistent.
- The ECB's own projections against the claim: March 2026 shows an energy-driven rise, then inflation returning to target in 2027-28.
- Many policies affect prices; few belong to central banks.
  - Clean-energy investment, decarbonisation targets, and ETS design are political choices.

Source: ECB Monetary Policy Strategy (2021); March 2026 ECB staff projections; Elderson, ECB Blog, April 2026.

# Single mandate is not enough

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**Fed: “maximum employment and stable prices”**

Two terms the institution must read against each other.

Each constrains the other.

Expansion requires both to point the same way.

**ECB: “price stability, with secondary objectives”**

One term plus a residual the institution interprets itself.

Nothing constrains the residual.

Expansion requires only that the institution find the door.

# IV. From Europe to the Fed

*Three claims*

# What went wrong

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*Each case fails the same way.*

	<b>Mandate</b>	<b>Tools</b>	<b>Transmission channel</b>
<b>Fiscal dominance</b>	Narrow (price stability)	Broad (QE, TLTRO, TPI)	Self-defined (yield management as monetary policy)
<b>Financial dominance</b>	Narrow (price stability)	Broad (LOLR, supervision, resolution)	Self-defined (financial stability as transmission)
<b>Climate dominance</b>	Narrow (price stability)	Broad (collateral, asset purchases)	Self-defined (climate risk as transmission)

**Narrow mandate + broad tools + self-defined transmission = unbounded scope.**

*Narrowness of the mandate is not a constraint when the institution defines its own channel of action.*

# Three lessons

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## 1. Independence is preserved by narrowness, not by legal status.

The ECB has more legal independence than the Fed and less effective restraint. The Fed's relative weakness on independence is its strength on accountability.

## 2. **Mandate** narrowing without **toolkit** narrowing is meaningless.

Cap the balance sheet outside crises. Sunset every emergency facility. Require explicit congressional authorisation for asset purchases beyond Treasury debt. Otherwise the next QE undoes any mandate revision.

## 3. Threat to independence is lack of **accountability** + unlimited mandate.

Where mandate, tools, and accountability are all unbounded, technocratic discretion produces redistributive choices that no parliament authorised. Each such choice creates a footprint the next political wave will use against the institution.

# Conclusion

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*“Preserving central bank independence rests not only on sound legal foundations, but also on robust fiscal and regulatory frameworks that secure both debt sustainability and financial stability, as well as on a clear commitment by central banks to operate within the boundaries of their mandate.”*

— Isabel Schnabel, 7 May 2026

Legal independence and a narrow written mandate are not enough. The question is who enforces the limits when the central bank discovers new instruments, new emergencies, and new transmission channels.

“The quiet erosion of central bank independence,” Fifth Annual Charles Goodhart Lecture, London.

# References and background

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ECB Annual Accounts; ECB consolidated weekly financial statements; ECB Data Portal; Eurostat HICP; Bundesbank, Banque de France, DNB annual reports; Single Resolution Board; Bloomberg.