

# IMF Working Paper

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## Central Bank Credit to the Government: What Can We Learn from International Practices?

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## **IMF Working Paper**

Monetary and Capital Markets Department

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#### **Abstract**

Using a central bank legislation database, this paper documents and analyzes worldwide institutional arrangements for central bank lending to the government and identifies international practices. Key findings are: (i) in most advanced countries, central banks do not finance government expenditure; (ii) in a large number of emerging and developing countries, short-term financing is allowed in order to smooth out tax revenue fluctuations; (iii) in most countries, the terms and conditions of these loans are typically established by law, such that the amount is capped at a small proportion of annual government revenues, loans are priced at market interest rates, and their maturity falls within the same fiscal year; and (iv) in the vast majority of countries, financing other areas of the state, such as provincial governments and public enterprises, is not allowed. The paper does not address central banks' financial support during financial crises.

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## I. INTRODUCTION, KEY FINDINGS, AND RECOMMENDATIONS

During the last two decades, many countries have reformed their central bank legislation with the objective of defeating inflation. One of the pillars of this reform was restricting central bank financing of the government, as this was considered a chronic source of inflation. Limiting such financing was also considered critical for building central bank credibility, a key ingredient for achieving monetary policy effectiveness.<sup>2</sup>

This paper documents and analyzes worldwide institutional arrangements governing central bank lending to the government in order to identify practices and provide policy recommendations. Using a new database of central bank laws, we review central bank legislation covering more than 150 countries, focusing exclusively on central bank laws and relevant excerpts from constitutions. The analysis is conducted from a central bank perspective and does not address fiscal policy considerations. Nor does it address any form of unconventional monetary policy that involves purchasing government bonds. These transactions aim, for example, at reducing the cost of private sector funding during periods of financial distress, or at avoiding a sharp decline in the price of government debt that may hamper financial institutions' balance sheets in the midst of a financial crisis. These policies, although highly relevant, are beyond the scope of this paper.

While interest in discussing central bank lending to the government is not new, little or no attention has been devoted recently to this issue in the literature (see Box). This paper contributes to filling this gap. Its findings and recommendations are intended to be a useful tool for Fund staff advice and for country authorities interested in revisiting policies for central bank financing of the government. The interest in central bank lending to the government has increased recently during the “great recession,” since a number of governments have turned to central banks for money as government liabilities increased, tax revenues declined, and financing for fiscal imbalances from domestic and international capital markets was expensive or unavailable.<sup>3</sup> Our analysis is based on *de jure* information and does not incorporate *de facto* practices that divert from legal provisions, which are typically observed in countries with weak institutional foundations.

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<sup>2</sup> In this paper we use the word “government” in a broad sense to refer to the state, including entities such as local governments and public enterprises. Similarly, the term “fiscal deficit” refers to the public sector deficit.

<sup>3</sup> For instance, countries approved legislation requiring central banks to temporarily grant credit to the government or public enterprises (for example, Bolivia granted credit to finance the oil-producing enterprise) or used extraordinary legal provisions to finance a government's payments of external debt (Jamaica and Zambia) or simply to finance government spending (Tanzania). In other countries, central banks started monetizing balance of payments loans received from multilateral institutions (Georgia and Ukraine, among others) to finance government expenditure.

### Box 1. Review of the Literature

Central bank lending to the government has received little attention in the literature, particularly since the early 1990s. At that time, the studies addressed central bank financing to the government across countries and its macroeconomic and institutional implications. Leone (1991) surveyed legal restrictions on central bank lending to the government in more than 100 countries and explored its macroeconomic consequences in a group of 44 industrial and developing countries. Other studies examined the institutional basis for central bank lending to the government and its impact on the independence of central banks. For instance, Cottarelli (1993) examined the appropriate model for constraining central bank lending to the government at the time of the drafting of the legislation which created the ECB and which restrained its ability to provide credit to the government. From a more academic perspective, Grilli et al. (1991) and Cukierman (1992) incorporated restrictions on central bank lending to the government into their respective indices of central bank independence. These indices have been widely used to measure how central bank independence affects inflation across countries.

Recently, the rules governing central bank lending to the government have been revisited as part of the design of good practices for the governance of central banks (Bank of International Settlements, 2009). The basic recommendation is to establish explicit restrictions to central bank financing to the government in order to avoid disrupting central banks' objective of preserving price stability.

Key findings are the following: (i) about two-thirds of the countries in the sample either prohibit central bank lending to the government or restrict it to short-term loans; (ii) most advanced countries and a large number of countries with flexible exchange rate regimes feature strong restrictions on government financing by the central bank; and (iii) when short-term loans are permitted, in most cases market interest rates are charged, the amount is limited to a small proportion of government revenues, and only the national government benefits from this financing. Yet, there is room for improvement in a large number of countries. With governments relying extensively on central bank money to finance public expenditure, central banks' political and operational autonomy is inevitably undermined for the fulfillment of their policy objective of preserving price stability.

Based on these international practices, we lay out below key recommendations for the design of the institutional foundations underlying central bank credit to the government.

- As a first best, central banks should **not** finance government expenditure. The central bank may be allowed to purchase government securities in the secondary market for monetary policy purposes. Restrictions to monetizing the fiscal deficit are even more compelling when countries feature fixed or quasi-fixed exchange regimes to avoid fueling a possible traumatic exit from the peg.
- As a second best, financing to the government may be allowed on a temporary basis. In particular, central bank lending to the government is warranted to smooth out tax revenue fluctuations until either a tax reform permits a stable stream of revenues over

time or markets are deep enough to smooth out revenue fluctuations. Financing other areas of the state, such as provincial governments and public enterprises, should not be allowed.

- The terms and conditions of short-term loans should be established by law. Central bank financing should be capped at a small proportion of annual government revenues (on a case-by-case basis), priced at market interest rates, and paid back within the same fiscal year. Communication between the government and the central bank for the disbursement and cancellation of these loans is necessary to facilitate the central bank's systemic liquidity management.
- As a good transparency practice, transactions that involve central bank financing to the government should be disclosed on a regular basis, including the amount and financial conditions applied to these loans.

The rest of the paper is structured as follows: Section II describes the data and the method of analysis, including the various criteria used to evaluate central banks' government financing; Section III takes stock of these legal provisions across the world, in a sample of 152 countries, and takes a preliminary look at the association between central bank financing to the government and key economic variables, in particular, inflation; Section IV summarizes the main findings of the paper and lays out good practices that should be adopted when governments borrow from central banks. Our analysis focuses exclusively on the monetary aspects of central banks' financing of the government and does not address fiscal considerations.

## II. CHARACTERIZING CENTRAL BANK LENDING TO THE GOVERNMENT

Defining the relationship between the government and the central bank is a key component of central bank charters. This relationship has many dimensions, such as central bank ownership, political autonomy (including restrictions on taking instructions from the government and rules for the resolution of conflicts with the government on policy matters), central bank capital and distribution of its profits, and central bank credit to the government.<sup>4</sup> This paper focuses on the latter, specifically on its monetary implications.<sup>5</sup> From an institutional perspective, provisions for central bank lending to the government, particularly when they involve large and long-term lending, may undermine central banks' autonomy and/or credibility. From an operational perspective, central bank loans to the government

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<sup>4</sup> See BIS (2009) for an extended discussion of these and other aspects of the governance of central banks in advanced economies and emerging markets.

<sup>5</sup> Government borrowing from the central bank also has important fiscal implications. Depending on how restrictive existing legal provisions are, the management of public finances may vary as governments may or may not have access to this source of financing.

may, if implemented in a disorderly manner, become a source of distortion for monetary operations and for central banks' liquidity management.

In this section, we characterize the different modalities of central bank lending to the government as they are provisioned for in the legislation of our sample of countries. We then identify the main parameters for central bank financing of the government.

### A. Modalities of Lending

This paper differentiates between the various levels of restrictions on central bank financing to the government. In particular, it clusters legal provisions into five groups according to the following ad hoc, criteria:

- *Full prohibition.* In many countries, central banks are prohibited from financing government expenditures in the primary market or providing unsecuritized loans. Some of them are even restricted in regard to their purchases of government securities in the secondary market, as they are considered a form of indirect financing of the government. Such restrictions include the establishment of a cap on the relative amount of government paper that the central bank can hold in its balance sheet. Countries where legislation permits central bank financing of the government under extraordinary circumstances, for example, during war or natural disasters, are also included in this category.
- *Short-term access to central bank financing, or advances.* Somewhat less restrictive provisions allow governments to obtain funds from the central bank on a temporary basis. Normally, this lending consists of advances or overdrafts on the government account at the central bank, and aims at compensating for seasonal shortfalls in government revenues. Legislation typically puts a ceiling on the amount of the loan and requires the government to pay it back within the same fiscal year. The ceiling may be an absolute cash value, a small percentage of government revenues/expenditures in previous years, or a proportion of a central bank liability. Interest rates charged may or may not be defined explicitly in the law.
- *Long-term financing or credit in the primary market.* This category includes legislation that allows central banks to lend directly to the government at more than one-year maturity, or to purchase securities in the primary market, regardless of whether the central bank is also empowered to extend advances.<sup>6</sup> Legislation may or may not include either the financial conditions of the loans as well as the limitations

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<sup>6</sup> We do not include in this category the institutional arrangements that allow central banks to purchase government bonds in the primary market for monetary policy purposes, like in Brazil, where the central bank is empowered to buy government securities in the primary market, but only to roll over its portfolio.

to the amount of lending. Countries with provisions that empower the central bank to pay foreign debt on behalf of the government or provide financing for this purpose, as well as legislation that requires the central bank to transfer funds to the government—for instance international reserves—are also included here.

- *No legislation on central bank lending to the government.* In a handful of countries, there are no legal provisions that prohibit central bank lending to the government.
- *Other forms of central bank financing.* A final category includes countries with legislation that allows other forms of central bank financing of the government, such as lending to specific economic activities where the state is involved, or financing the government or state-owned deposit insurance institutions to tackle financial crises. Legislation authorizing central banks to transfer to the government unrealized profits—associated with changes in exchange rate adjustments among the currencies in the international reserves—is also included in this category.

This analysis does not include central bank purchases of government securities in the secondary market. We have treated these transactions as part of the central bank's regular conduct of monetary operations, although we are mindful that they may become an indirect form of government financing if the volumes involved in these transactions are sufficiently large—for example, when they deviate from historical trends. The paper does not address conditions for central bank financing to private corporations or for development purposes.

## **B. Parameters for Lending**

Where central banks are vested with powers to provide loans to the government, it is worth identifying the main criteria underlying these transactions. An examination of these criteria is relevant because they may also have adverse effects on the central bank's autonomy and its ability to execute monetary policy. The following criteria in the legislation of our sample of countries are examined:

- *The maximum amount for loans or advances permitted in the law.* Specifically, we documented if the law prescribes a cap on central bank loans to the government. We also verified whether this cap is expressed in terms of cash or relative to base money or another central bank liability, or if the ceiling is defined as a ratio of total government revenues or expenditures in a given period.
- *The authority responsible for deciding the conditions of the loans, in particular, the interest rate.* Legislation may prescribe that the central bank board is in charge of setting these conditions, may empower the government to decide, or may leave room for negotiations between the two parties. The key parameter at stake is the interest rate. The government may be required to pay market interest rates or it may receive preferential treatment and pay below-market rates on central bank loans. Legislation

may call central banks and governments to negotiate interest rates, or the law may be silent in this regard, thereby leaving room for central banks and governments to agree on the cost of the loans.

- *The beneficiaries of central bank lending.* On this topic, we ascertain whether the law empowers the central bank to extend credit only to the central government, or if other public institutions are also entitled to borrow from the central bank, namely local governments and public enterprises.
- *The maximum maturity of central bank loans to the government.* The threshold for these operations is one year. Shorter maturities are consistent with the financing of government liquidity shortages, whereas longer maturities generally fund structural government deficits.

### C. Data

Based on the categorization outlined above, we conduct our analysis using the information available from the IMF's Central Bank Legislation Database (CBLD). The CBLD is a unique database that comprises central bank laws and the relevant excerpts from the constitutions of 152 countries, including those belonging to 4 currency unions.<sup>7</sup> The CBLD is more than just a collection of laws; it classifies central banks' legislation into more than 100 categories that mirror the structure of most central bank laws enacted during the last two decades.<sup>8</sup>

The sample of countries in this paper has a broad regional coverage (38 countries from Africa, 19 from Asia and the Pacific, 41 from Europe, 25 from the Middle East and Central Asia, and 29 from the Western Hemisphere). This allows us to conduct an analysis from a geographical perspective following the regional classification of countries used by the IMF. The sample also allows for an analysis based on the level of development (industrial, emerging markets, and developing countries) and exchange rate regime. We used the IMF's World Economic Outlook to identify advanced countries and the Standard and Poor's Emerging Market Database to identify emerging countries. We labeled the remainder as developing countries. In turn, to group countries by exchange rate regime, we used the information from the IMF's 2010 Annual Report on Exchange Arrangements and Exchange Restrictions (AREAER).

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<sup>7</sup> These currency unions are the Eurosystem, the Central African Monetary Union, the West African Monetary Union, and the Eastern Caribbean Currency Union.

<sup>8</sup> These categories were elaborated by a team of experts in the IMF's Monetary and Capital Markets Department, and include *inter alia* provisions that pertain to central banks' objectives and functions, policy autonomy and governance structure, operational autonomy, and accountability and transparency. The CBLD also provides the capability to search the text of legislation according to a country's exchange rate regime and monetary union. The classification of the central bank legislation encoded in the CBLD has benefited from comments and suggestions provided by the participating central banks.

### **III. CENTRAL BANK LENDING TO THE GOVERNMENT: THE FACTS**

This section takes stock of central bank constraints on lending to the government as established in central bank legislation in our sample of countries. It analyzes and highlights patterns of government borrowing from the central bank from three different angles. First, we compare and contrast the legal provisions across geographical regions, levels of development, and exchange rate regimes. Second, since a large number of countries' central banks provide credit to the government, we also review their legislation to ascertain the conditions under which central bank financing is granted, as described in section II. Specifically, we focus on the size, maturity, beneficiaries, and nature of the interest rate charged on these loans. Finally, we investigate further the pattern of central bank financing to the government across levels of development using a quantitative indicator and examine whether central bank financing of the government correlates with specific macroeconomic variables. To conduct this analysis, we construct a comparative measure across countries of the restrictiveness of the legal provisions for central bank lending to the government. Specifically, we build a "credit to the government" index and calculate it for each country in the sample. The inputs required to feed the index have been obtained from the IMF's CBLD.

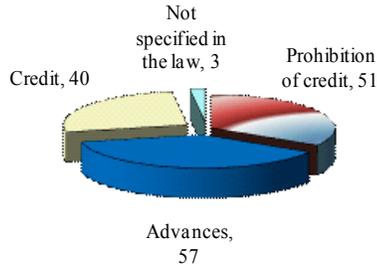
#### **A. Does Geography, Development, or the Exchange Rate Regime Matter?**

##### **Geography**

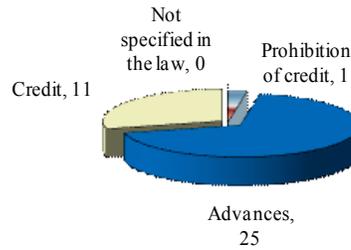
As a first approximation, the data show that, in a worldwide context, restrictions on the provision of central bank credit to the government exist in a large majority of countries. More than two-thirds of the countries in the sample either prohibit central banks from extending credit to governments or only allow them to grant advances to cope with temporary shortages in government revenues (Figure 1).

Figure 1. Legal Provisions for Central Bank Credit to the Government<sup>1/</sup>  
(By Region)

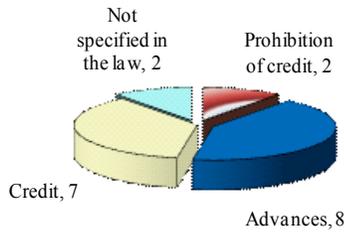
**Total sample of countries (152)**



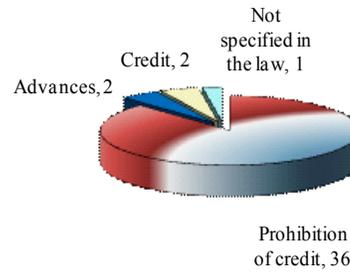
**Africa (38)**



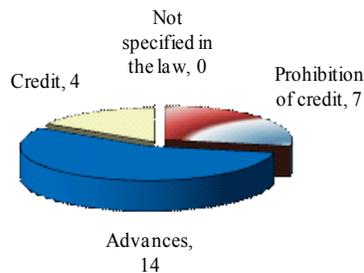
**APD (19)**



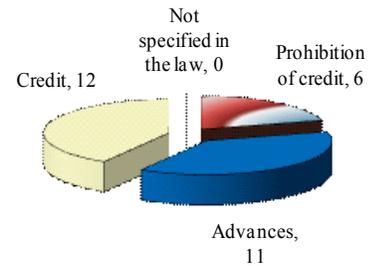
**Europe (41)**



**Middle East and Central Asia (25)**



**Western Hemisphere (29)**



Sources: IMF and Central Bank Legislation Database.

1/ In some countries, the law authorizes central banks to provide both loans and advances to the government. In those cases, to avoid duplication, we only count the provision of loans.

However, this pattern of restrictions is not uniform across regions.<sup>9</sup> Europe exhibits the most restrictive legal provisions, with these restrictions being driven by the limitations imposed by the treaty establishing the European Community (article 101). At the other extreme, countries in Africa and in Asia and the Pacific have more lenient legislation in regard to central bank financing of the government, with almost no countries imposing full prohibitions, and instead empowering most central banks to grant advances and, in some cases, loans. To a great extent, this pattern is also followed by the Middle East and Central Asia and the Western Hemisphere, although in these regions there are a larger number of countries that forbid central bank credit to the government. Within the latter, the Latin American countries, vis-à-vis the Caribbean countries, have more stringent legal restrictions, with some countries banning central bank financing to the government at the constitutional level (for example, Brazil, Chile, Guatemala). The fact that Europe and most of Latin America have the strongest restrictions is probably associated with past episodes of hyperinflation, which were linked to persistent financing of fiscal deficits by central banks.

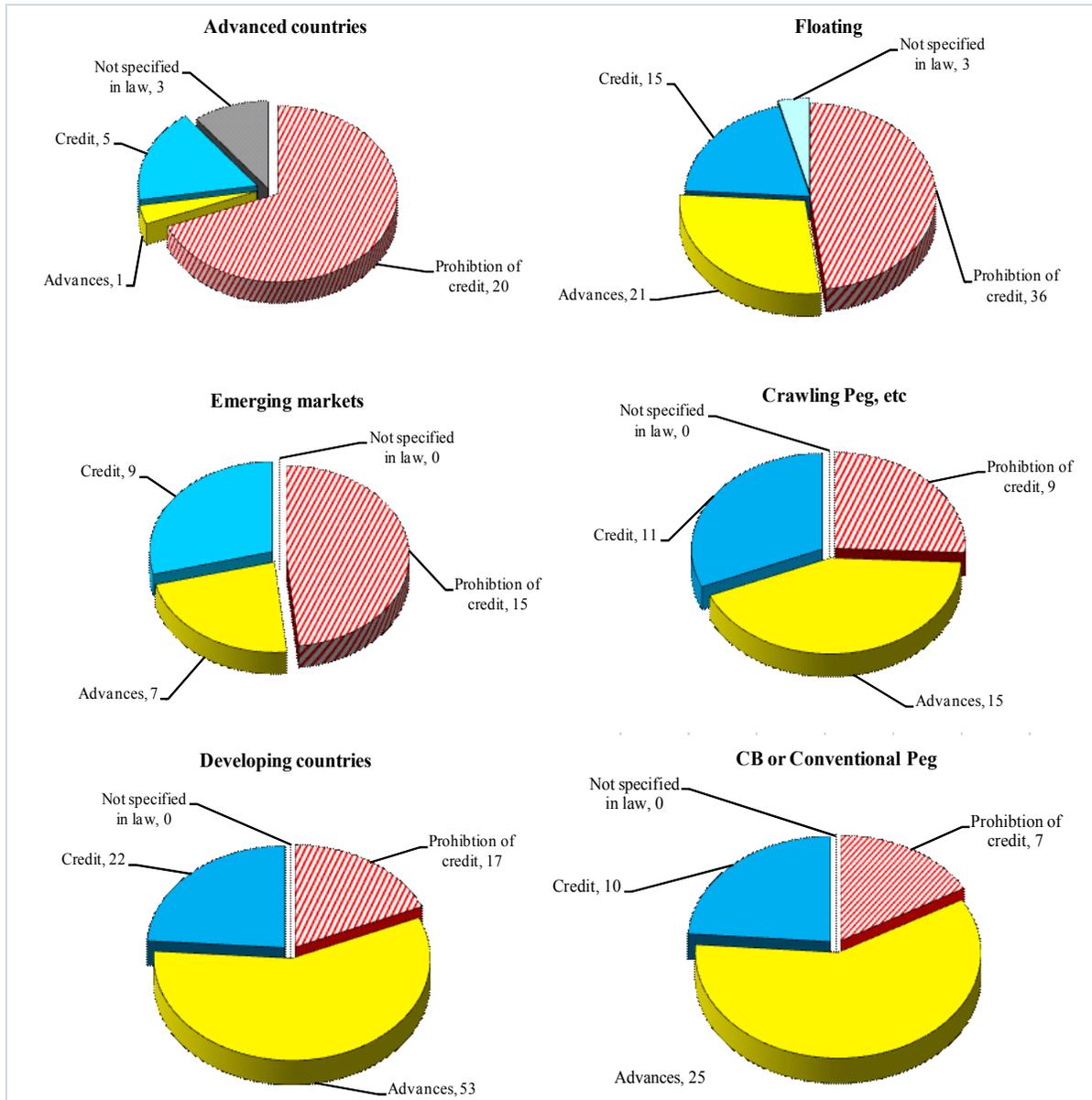
### **Level of Development**

Legal provisions on central bank financing of the government seem to be inversely correlated to the country's level of development. While in two-thirds of the advanced countries, central banks cannot finance the fiscal deficit, this proportion falls to almost one-half in emerging market economies, and to only one-fifth in developing countries. As noted before, the existing restrictions in the European countries drive most of these results in the advanced countries. In turn, allowing the central bank to provide advances to the government is a common feature in more than half of the developing countries (Figure 2, left side). An explanation for this institutional feature is that the tax systems in many developing countries do not generate a stable flow of revenues. Given that capital markets are shallow and governments are unable to obtain financing as needed, short-run central bank credits allow governments to smooth out the seasonal fluctuations in revenues.

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<sup>9</sup> There are three countries where legislation is silent about restrictions on the central bank's provision of credit to the government, namely Australia, New Zealand, and the United Kingdom.

Figure 2: Legal Provisions for Central Bank Credit to the Government<sup>1/</sup>  
(By Level of Development and by Exchange Rate Regime)



Sources: IMF, Central Bank Legislation Database, and Annual Report on Exchange Arrangements and Exchange Restrictions. The list of advanced countries matches the selection made in the IMF's World Economic Outlook, the emerging markets group corresponds to the Standard & Poor's Emerging Market Database, and the developing countries group includes the rest.

<sup>1/</sup> In some countries, the law authorizes central banks to provide both loans and advances to the government. In those cases, to avoid duplication, we only count the provision of loans.

## Exchange rate regime

From another angle, countries featuring flexible exchange rate regimes have the most restrictive provisions for central bank financing of the government. In addition to the European nations, a large number of other countries have adopted inflation targeting regimes. Such regimes are typically supported by institutional arrangements that include strong limitations on central bank financing of fiscal deficits, with the aim of granting central banks political and operational autonomy.<sup>10</sup> On the other hand, almost one-half of the countries that maintain intermediate exchange rate regimes—and a handful of countries with a conventional peg—maintain lax conditions in regard to the financing of government expenditures (Figure 2, right side). This is a potential vulnerability for the stability of the exchange regime and may place an upward bias on interest rates should large central bank lending to the government materialize, although in the case of currency board arrangements, there is an intrinsic limitation on monetizing, including the possibility of financing the fiscal deficit.<sup>11</sup>

### B. If Lending to the Government is Allowed, under what Conditions?

Since many developing countries allow central banks to lend to the government, we review the main conditions underlying this financing. While the specifics vary from one country to another, there are some clear trends across countries. To better present this information, we first focus on the possible beneficiaries of central bank financing. Second, we ascertain who decides about the interest rates charged on these loans. Third, we examine what limits are imposed on the amount of this financing. And fourth, we find out the maximum maturity of central bank loans to the government.

#### Beneficiaries

In the vast majority of countries in the sample, legal provisions for central bank financing exclusively benefit the central government (Table 1). However, some countries have expanded these facilities to public corporations (for instance, Bahamas, Bahrain, Bangladesh, Barbados, Fiji, Haiti, Jordan, Nicaragua, Pakistan, and Yemen) and to local or provincial governments (like Canada, Costa Rica, India, Iran, Mauritania, and Uganda). Restricting central bank financing to benefit exclusively the central government not only increases the chances of limiting broad monetization but also facilitates systemic liquidity management by the central bank.

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<sup>10</sup> See Roger (2009).

<sup>11</sup> This is because, typically, currency board arrangements restrict central banks' issuance of money for any purpose to the amount backed by the international reserves.

### **Interest rate decisions**

Less uniform provisions are found when it comes to decision-making about the interest rate on this financing, with some regions having a number of countries where governments have a say (Table 2). For instance, in the Western Hemisphere and Africa, the large majority of central banks are empowered to set the interest rate on loans provided to the government, or legislation links the rate to market conditions. Exceptions include some Caribbean countries and some African countries, notably Angola, Kenya, Madagascar, and Namibia, where there is room for negotiation between the central bank and the government. In Asia and the Pacific, there are some important countries (namely, India, Japan, and Malaysia), where the interest rate is negotiated between the central bank and the government. In most of the Middle East and Central Asia, interest rates are negotiated between the two parties. The same happens in Israel—one of the few European countries where monetizing fiscal deficits is allowed—where the minister of finance negotiates interest rates with the central bank. Sprinkled across the regions, there are some countries, such as Jamaica, Jordan, Mozambique, Syria, Uganda, and United Arab Emirates, where central banks can provide advances to the government at no cost.

Involving the government in setting the interest rate is a subject of concern, in particular for countries with weak institutions, as these negotiations would probably tilt the balance in favor of governments. In general, assigning the government an active role in deciding the interest rate on central bank loans to the government hinders the central bank's autonomy and credibility, and encourages governments to use central bank financing rather than raise money from the markets, internally or abroad.

### **Amount of financing**

Legal provisions governing the amount of central bank lending to the government vary and do not feature any regional pattern (Table 3). Legislation limits the amount of central bank credit to the government based on relative measures, most commonly a ratio with respect to government revenues. In most countries, advances and loans cannot exceed 10 percent of government revenues of the previous fiscal year or an average of the last three fiscal years, although in Africa this proportion is sometimes higher. A small number of countries use alternative relative measures to limit this financing; for instance, a proportion of government expenditures (5 percent in Costa Rica), of the national budget (25 percent in Bahrain), of some central bank liability (12 percent of money base in Argentina), of its capital and reserves (three times this amount in Serbia), or some combination of the last two (central bank capital and reserves plus one-third of its liabilities in South Africa). The maximum amount that can be lent is left open to negotiations between the central bank and the minister of finance in a few countries, either explicitly (Barbados) or implicitly (the Central African Monetary Union); it can depend on congress approval (Korea), or be fixed by law in nominal terms (Papua New Guinea). Although the criterion varies, there is consensus that central banks should only be allowed to provide a limited amount of credit to the government to avoid undermining their operational autonomy.

**Table 1. Central Bank Advances/Loans to the Government—Beneficiaries**

	Central government	Plus other local governments	Plus public enterprises
Africa	25	10	2
Asia & the Pacific	8	2	5
Europe	4		
Middle East & Central Asia	12	2	4
Western Hemisphere	11	1	11

**Table 2. Central Bank Advances/Loans to the Government—Who Sets Interest Rates?**

	The central bank or at market rates	Central bank/government negotiate or not in law	Below market rates
Africa	28	8	1
Asia & the Pacific	9	5	1
Europe	1	3	
Middle East & Central Asia	7	7	4
Western Hemisphere	7	15	1

**Table 3. Central Bank Advances/Loans to the Government—Limits on the Amount (with Respect to Government Revenues)**

	Up to 10%	> 10% up to 20%	> 20% up to 30%	> 30%	Other criteria or not in law
Africa	11	16	2		8
Asia & the Pacific	2	3	2		8
Europe	3				1
Middle East & Central Asia	8	4	2		4
Western Hemisphere	7	8	1	1	6

**Table 4. Central Bank Advances/Loans to the Government—Maturity of Central Bank Loans**

	Up to 90 days	> 90 up to 180 days	> 180 up to 1 year	> 1 year	Not defined in the law
Africa	2	5	24	3	3
Asia & the Pacific	3	5	1		6
Europe		1			3
Middle East & Central Asia	1	4	7	3	3
Western Hemisphere	1	4	4	9	5

Sources: IMF Central Bank Legislation Database.

### **Maturity of the loans**

A similar landscape is found in relation to the maturity of lending operations (Table 4). The maturity of central bank loans and, in particular, advances to the government tend to be concentrated on periods that go up to 180 days; however, in some countries the maturity of central bank loans to the government is not defined in the law, and in some African countries and in the Caribbean it is up to a year.

The information summarized above suggests that there is room for improvement because in a large number of countries public expenditures still rely openly on central bank money. Under these conditions, governments have no incentive to optimize cash management from taxation and from the proceeds of public debt issuance because they can always resort to central bank resources. Thus, countries should address this problem by approving reforms that legally require that (i) governments borrow from central banks at market interest rates, and (ii) loans be paid back within the same fiscal year.

### **C. Basic Empirical Regularities**

In the analysis that follows, we identify patterns across regions about the institutional arrangements governing central bank financing of the government. To facilitate the comparison, we construct a quantitative indicator of the limitations imposed by law on central bank financing of the government. We then examine whether basic empirical regularities exist between our quantitative indicator and key macroeconomic variables, such as inflation and GDP per capita.

The quantitative indicator is based on similar criteria to those used in the relevant part of the well-known Cukierman, Webb, and Neyapti (CWN) index of central bank independence.<sup>12</sup> Specifically, we perform small adjustments to the lending to the government portion of the CWN index, narrowing down the number of criteria from eight to six. These six criteria refer to the following legal provisions: (i) the limitations on the amount of advances to the government; (ii) the limitations on the amount of credit to the government; (iii) who decides the conditions of the loans; (iv) the beneficiaries of central bank credit; (v) the maturity of the loans; and (vi) the interest rate charged on central bank loans. Each criterion was then assigned different weights between zero and one—which mirrored the valuations used in the CWN index—depending on the stringency or leniency of the legal provisions that govern central bank lending to the government. The total value of the index fluctuates on a continuous scale from zero to six, such that higher values indicate greater restrictions on central bank financing of the government, and vice versa (see Appendix I for details).

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<sup>12</sup> See Cukierman (1992).

Using this metric, summary statistics confirm that the institutional restrictions for central bank financing of the government are positively associated with a country's level of development (Table 5). Three important factors contribute to explain this outcome. First, the European Central Bank (ECB), which covers a large number of advanced countries, is not empowered to finance its member governments. Second, most emerging market countries have adopted inflation targeting, which typically precludes any form of fiscal dominance, including central bank lending to the government. And third, many developing countries either have legislation that opens the door for fiscal dominance, or allow short-term advances to the government to smooth out seasonal fluctuations of fiscal revenues.

**Table 5. Summary Statistics**

	Credit to government index				
	Mean	Median	Stand. Dev.	Min	Max
Full sample of countries	4.52	4.5	1.33	1.5	6
Advanced countries	5.41	6	1.15	2.5	6
Emerging market countries	4.51	4.84	1.68	1.5	6
Developing countries	4.29	4.17	1.14	1.83	6

Source: The list of advanced countries was obtained from the IMF's World Economic Outlook, whereas the emerging markets list corresponds to the Standard & Poor's Emerging Market Database.

From a macroeconomic perspective, our credit to the government index is negatively correlated with the level of inflation, which means that lower central bank credit to the government is associated with lower inflation as well. This happens for both the full sample of countries (upper triangle) and the sub-sample of emerging and developing countries (lower triangle) in Table 6 with significant levels for the null hypothesis of zero correlation. The results also show that our index of credit to the government is positively correlated with real GDP growth in the developing and emerging market countries, but not for the advanced countries.

**Table 6. Pair-wise Correlations between Selected Variables**

	Inflation	Credit to govern. index	Real GDP growth
Inflation		-0.239 (0.005)	0.485 0.000
Credit to government index	-0.186 (0.092)		-0.074 (0.375)
Real GDP growth	0.367 (0.001)	0.211 (0.045)	

Source: Authors calculations.

Note: Correlations in the upper triangle correspond to the full sample of countries and in the lower triangle to developing and emerging market countries. Significance levels for the null of zero correlation appear in parenthesis. A larger credit to the government index implies greater restrictions on central bank financing of the fiscal deficit.

The results obtained from expanding the analysis to a multivariate dimension confirm that tighter rules for central bank lending to the government may be associated with lower inflation in developing and emerging market countries. Although conducting a rigorous empirical analysis is beyond the scope of this paper, we provide here preliminary empirical evidence in support of the notion that restraining central bank lending to the government is associated with lower levels of inflation. Running cross-sectional regressions on inflation and after controlling for a number of macroeconomic and institutional variables, we obtained a statistically significant negative coefficient for the credit to the government index in the sub-sample of developing and emerging market economies (see Appendix II).

#### IV. FINAL REMARKS

Conventional wisdom favors the notion that limited central bank lending to the government is conducive to lower inflation and this, if sustained over the long run, promotes higher rates of economic growth. Against this premise, we have taken in this paper a worldwide snapshot of legal constraints to government borrowing from the central bank. Based upon this information, we now lay out general principles for the design of an appropriate framework to govern central bank lending to the government. These institutional arrangements will help to bolster the autonomy of central banks with the aim of preserving countries' price stability.

- As a key general principle, this paper underscores that central banks should refrain from lending to the government, although this may not always be possible depending on the country's level of development. Governments in industrial countries and emerging market economies should have no access to central bank money because they can raise money to finance fiscal deficits from domestic and international capital markets. In practice, a full prohibition of central bank financing to the government is in place in most industrial countries, most notably in Europe, whereas in emerging markets, a number of countries still allow the central bank to lend to the government, albeit at short-term maturity.
- In developing countries, central bank financing to the government may be warranted in the short run. In these countries, government revenues exhibit seasonal fluctuations and capital markets are shallow, thus making the case for allowing central bank financing in the short run—via overdrafts or through advances—to smooth out seasonal revenue fluctuations. As tax administration improves and money and capital markets deepen, governments should be able to smooth out the seasonality of fiscal revenues. In our sample of developing countries, total prohibition of central bank lending to the government is found only by exception.
- The design of a good institutional arrangement for government borrowing from the central bank is not independent of the country's exchange rate regime. While banning central bank lending to the government is as critical as an anti-inflation policy stance, economies with conventional pegs and intermediate exchange rate regimes (exchange

rate bands) should be even more compelled to endorse this principle. Exchange rate targeting countries are particularly vulnerable to a large financing of fiscal deficits, as the increasing money supply can drain central bank international reserves, which, eventually, may lead to a costly Krugman-type balance of payment crisis. In this regard, a number of countries (20 in our sample) should consider adopting a more restrictive legislation to limit central banks from monetizing fiscal deficits—although in the case of currency boards, there is an intrinsic limitation on monetization, including the provision of loans to the government.

- Central banks may purchase government securities in the secondary market exclusively for monetary policy purposes. Limiting the amounts of these transactions would restrict quantitative easing policies and, hence, this should be done only in extreme circumstances—as the United States and the United Kingdom did in the wake of the recent financial crisis—and under clear and transparent rules. Disclosure of stock and flows of these purchases, vis-à-vis a pre-specified rule or program, is advisable to allow market participants to monitor that these transactions are made exclusively for the purposes of monetary operations. In countries where the central bank lacks credibility, legislators should consider limiting the amount of government securities that the central bank can hold at any one time to avoid any indirect government financing. The limit could be either the amount of banknotes in circulation or a proportion of some other central bank liability.

When central bank lending to the government is warranted to smooth out tax revenue fluctuations, and until a fiscal reform smoothes out seasonal fluctuations or deeper capital markets compensate for the fluctuations, the operational arrangements in place should follow key principles with the aim of limiting market distortions. These principles are the following:

- Loans should be provided at short-run maturity. Governments should pay back within a short period of time, and certainly before the end of the fiscal year in which the loan is granted. Establishing a more specific term to pay back central bank loans should be determined, identifying seasonal fluctuations of government revenues and how to better smooth them out using short-term central bank money.
- The cost of central bank lending to the government should be established by law and be based on market interest rates. Using market criteria is critical in order to reduce government incentives to use central bank money as a source of financing as a first alternative rather than as a last resort. If the interest rate is not *a priori* defined in legislation, the central bank will generally need to negotiate the rate with the government, which creates an opportunity for government interference in monetary policy implementation.
- Central bank loans to the government should have an upper bound. This limit should typically be expressed in terms of a proportion of tax revenues, although other

relative measures could also be used, i.e., with respect to a central bank liability. This proportion should be set on a case-by-case basis. In practice, most countries limit credit, overdrafts, or advances to 10–20 percent of government revenues in the previous fiscal year. Establishing limits in terms of government expenditures is not recommended as it tends to be accommodative of an expansionary fiscal policy.

- The law should protect the central bank against the event that the government does not pay its obligation on time. The central bank should be empowered to debit the government account it holds, or to issue marketable securities on behalf of the government for a value equal to the loan plus interest in arrears. The latter is particularly relevant when it comes to government overdrafts at the central bank. In addition, the government should not be allowed to borrow again from the central bank while it is in arrears.
- Only the central government should be entitled to borrow from the central bank. Providing financing to local governments and public enterprises multiplies central bank financing and poses risks of adverse macroeconomic effects.
- The conditions under which the central bank lends to the government should be disclosed as a good transparency practice. The central bank should establish in the law the conditions governing lending operations to the government, and disclose them on a timely basis, including the amount, interest rate, and maturity of the loans, such that markets can internalize any potential impact on systemic liquidity.

## Appendix I. Credit Index

1. Rules for advances	
–Advances to government prohibited	1
–Limited by small percentage of government revenues or expenditures or by the monetary program	0.67
–Allowed under lax limits (more than 15 percent of government revenues)	0.33
–Allowed without limits	0
2. Credit to the Government	
–Not Allowed	1
–Indirect lending to pay government debt abroad	0.67
–In the primary market with limits (< 15 percent)	0.33
–In the primary market with lax limits (> 15 percent)	0
3. Who decides conditions of the loans	
–Central Bank defines terms and conditions or under market conditions	1
–Defined by law	0.67
–No specification or the law allows negotiations between Government and Central Bank	0.33
–Executive branch decides independently	0
4. Beneficiaries of Central Bank lending	
–Only the government	1
–Government plus local government	0.67
–All of the above plus public enterprises	0.33
–All of the above and to the non-financial private sector	0
5. Maturity of loans or advances	
–Limited to a maximum of 6 months	1
–Limited to a maximum of 1 year	0.67
–Limited to a maximum of more than one year	0.33
–No legal upper bounds specified	0
6. Interest rates for advances or loans	
–At market rate or defined by the central bank	1
–Interest rates not specified in law (negotiable)	0.50
–At below market rates	0

## Appendix II. Preliminary Regression Analysis

To complement the statistical analysis conducted in section III, we tested in a multivariate dimension whether restricting central bank lending to the government has any explanatory power on inflation performance. A set of cross-sectional regressions of average inflation on our measure of central bank credit to the government was executed. The regressions were performed on the full sample of countries and the sub-sample of developing and emerging market countries for the period 2004–2008. Inflation was computed as  $\log(1 + p_i)$  to cope with possible heteroscedasticity. We controlled for several variables, including real GDP growth and the exchange rate regime—using a dummy variable—to control for the anchor effect on inflation exercised by currency boards and conventional pegs as classified by the IMF's AREAER. The GDP series were averaged over a five-year span with a one-year lag (2003–2007) to capture the usual delayed impact on inflation, but as a robustness check, similar regressions were run with two- and three-year lags and the outcomes did not show major changes.<sup>13</sup> We also included in the regressions the real credit growth as another explanatory variable, but the estimated coefficients were not statistically significant (not reported). In addition, despite the short period of time on which the analysis focuses, we controlled for the fiscal deficit, measured through the increase in the public debt, as an alternative to avoid using fiscal deficit data, which are not always comparable across countries. The results generally rendered coefficients with the opposite sign and/or nonstatistically significant (not reported).

Table 7 below presents the results of cross-sectional regressions. For both samples, all the parameters had the expected sign, and the estimated coefficients for the explanatory variables were statistically significant throughout.<sup>14</sup> An interesting result is that the credit to the government index has stronger explanatory power for the sample of developing and emerging market countries, both in terms of the statistical significance and the size of the estimated coefficient (column 4 versus column 3). As regards the latter, we found that raising the restrictions to central bank lending to the government by one additional point in the credit to the government index would cause a decrease of approximately 1.1 percent in inflation in the developing world, which is larger than the gain of 0.8 percent in the full sample of countries. While these numbers are not aimed at providing exact results, they give a rough idea, or an order of magnitude, that illustrates the potential benefit that developing countries could enjoy as they tighten conditions for central bank lending to the government.

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<sup>13</sup> The lack of any meaningful association between the fiscal deficit and inflation is consistent with most evidence in the empirical literature, except for high inflation episodes (see, for example, Fischer and others, 2002).

<sup>14</sup> In both groups of experiments the outcome was the same. When we increased the lag for average GDP growth and when we extended the period of analysis backwards, the basic results remained the same, although the level of statistical significance weakened over time.

**Table 7. Ordinary Least Squares Regressions of Inflation on Credit Restrictions to the Government**

	Full Sample	Full Sample	Full Sample	Developing Countries	Full Sample	Developing Countries	Full Sample	Developing Countries
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Intercept	10.10*** (1.51)	11.57*** (1.63)	6.90*** (1.87)	11.66*** (1.78)	5.01*** (1.47)	9.23*** (1.50)	6.52*** (1.94)	11.70*** (1.91)
Credit to government index	-0.78** (0.30)	-0.92*** (0.32)	-0.76** (0.30)	-1.09*** (0.33)			-0.45 (0.34)	-0.82** (0.32)
Dummy: Peg		-2.85*** (0.69)	-2.39*** (0.65)	-4.83*** (0.68)	-2.09*** (0.69)	-4.61*** (0.71)	-2.22*** (0.68)	-4.70*** (0.71)
Real GDP growth			0.69*** (0.16)	0.42** (0.17)	0.74*** (0.17)	0.39** (0.18)	0.73*** (0.16)	0.45** (0.17)
Central banks' political independence					-3.58*** (1.19)	-4.61*** (1.63)	-2.47* (1.31)	-3.01* (1.66)
Number of observations	138	138	138	83	135	80	135	80
R <sup>2</sup>	0.06	0.14	0.33	0.49	0.36	0.50	0.37	0.53

Source: Authors calculations.

Robust standard errors in parenthesis.

\*Significant at 10 percent; \*\* significant at 5 percent; \*\*\* significant at 1 percent.

Note: The developing countries group includes emerging markets. The dependent variable is average inflation from 2004 to 2008 scaled as  $\log(1 + p_t)$ . Control variables include: a Dummy Peg, which equals one in countries with conventional pegs or currency boards and zero otherwise—according to the classification in the IMF's AREAER—real GDP growth, averaged over the 2003–2007 period; and an index of central banks' political independence, based on Arnone and others' (2009) index of central bank independence.

To reduce the effect of possible missing variables, we also controlled for the influence on inflation of the political independence of central banks. The empirical literature of the last decade has largely documented that central banks' independence has been a key factor for explaining inflation performance.<sup>15</sup> Since the legal restrictions for central bank credit to the government are a large component of indexes of central bank independence, we also controlled for the political independence of central banks, which is another critical component of such indexes. This allowed us to reject the possibility that the effect on inflation of the credit to the government index may simply be capturing the impact of a more general index of central bank independence. To this end, we borrowed from Arnone and

<sup>15</sup> See for example, Cukierman and others (2002) on transition economies, Jácome and Vázquez (2008) on the Latin American and the Caribbean countries and, more generally, and Crowe and Meade (2007) and Arnone and others (2009) for a worldwide sample of countries.

others' index of central bank independence and its database, which has worldwide coverage, and extracted the political independence component.<sup>16</sup> Simple cross-sections show that central banks' political independence is significant for the full sample and for the developing country sub-sample (columns 5 and 6). Then, when we ran the regressions with both indices, our credit to the government index became insignificant in the full sample but remained strongly significant in the developing country sub-sample (columns 7 and 8). These results indicate that our central bank credit to the government index preserves the same size and its explanatory power on inflation performance after controlling for the effect of the political independence of central banks. It may also be seen as constituting a significant element of central banks' independence in developing and emerging market countries, as relating to the control of inflation.

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<sup>16</sup> See Arnone and others (2009). Their index of central bank independence consists of a political and an economic component. We excluded the economic component which is largely related to credit to the government.

### Appendix III. Central Bank Regulations on Credit to the Government—Sample of Countries

Africa	Relevant Legislation
South Africa	<p><b>Title: South African Reserve Bank Act 90 of 1989</b>  <b>Last Amendment: Exchange Control Amnesty and Amendment of Taxation Law Act 12 of 2003</b>  <b>10 Powers and duties of Bank</b>  <b>(1) The Bank may, subject to the provisions of section 13</b>  <b>(f) grant loans and advances: Provided that unsecured loans and advances may be granted only in the following cases, namely:</b>            (i) an unsecured loan to the Government of the Republic or to a company referred to in paragraph (b) or, with the approval of the Board, to any company in which the Bank has acquired shares in accordance with the provisions of paragraph (d);            (g) buy, sell, discount or re-discount bills of exchange drawn or promissory notes issued for commercial, industrial or agricultural purposes, or exchequer bills of the Government of the Republic or of the government of any other country, or securities of a local authority in the Republic;</p> <p><b>13 Prohibited business</b>            The Bank may not            (f) hold in stocks of the Government of the Republic which have been acquired directly from the Treasury by subscription to new issues, the conversion of existing issues or otherwise, a sum exceeding its paid-up capital and reserve fund plus one-third of its liabilities to the public in the Republic.</p>
Uganda	<p><b>Title: The Bank of Uganda Statute, 1993</b>  <b>Part VI-Bank Relationship with Government</b>  <b>34. Temporary advances</b>            (1) The Bank may make temporary advances to the Government and local governments in respect of temporary deficiencies of recurrent revenue.            (2) The Treasury shall, at the beginning of each financial year identify and submit to the Bank all its requirements for temporary advances for that year and the Bank shall, subject to subsection (3) operate within that requirement.            (3) The total amount of advances made under subsection (1) shall not at any time exceed eighteen percentum of the recurrent revenue of the Government.            (4) The Bank shall charge market rates of interest on any advance to the Government or local government unless the Board determines otherwise.</p> <p><b>35. Report on advances</b>            (1) Where in the opinion of the Bank the limitations on Bank credit prescribed under subsection (3) of section 34 or the holding of securities is exceeded, the Bank shall make a report on the Bank's outstanding advances or holding of securities in terms of those sections, and the causes that have led to the breach of the limitations, together with any recommendation or remedy; and the Bank shall make further reports and recommendations to the Minister at intervals not exceeding six months until the situation has been rectified.            (2) At any time when the limitations on Bank Credits or the submitted requirement is exceeded, the powers of the Bank to grant additional financing shall cease until the situation has been rectified.</p>

<p><b>Tanzania</b></p>	<p><b>Title: The Bank of Tanzania Act, 2006 (8th June 2006)</b>  <b>Part IV: Other Operations of the Bank</b>  <b>34. Direct advances and other short term credit to the Governments, etc.</b>  (1) Subject to the provisions of this section, the Bank may  (a) make direct advances to the Governments for the purposes of offsetting fluctuations between receipts from the budgeted revenues and payment of the Governments; and  (b) purchase, hold and sell Treasury bills issued by the Governments which mature not later than 12 months from the date of issue.  (2) Each advance made to the Governments under this section shall—  (a) be made solely for the purpose of providing temporary accommodation to the Governments and shall, accordingly, be repayable within one hundred and eighty days; and  (b) bear interest at market rates as determined by the Bank.</p> <p><b>35. Operation in Government securities, etc.</b>  (1) Subject to the provisions of this section, the Bank may, for the purpose of offsetting fluctuations between receipts from the budgeted revenues and payment of the Governments, purchase, hold and sell negotiable stocks, bonds or similar debt obligations or other securities issued by the Governments which shall bear interest at such market rate as determined by the Bank and which mature not later than 12 months from the date of issue.  (2) The total amount outstanding at any time of advances made and the Treasury bills and other securities held by the Bank under this section and section 34 shall not exceed one-eighth of the average budgeted revenues of each of Governments as defined in section 36.</p> <p><b>36. Meaning of annual budgeted revenue.</b>  (1) For the purposes of section 35 the average budgeted revenues of the Governments shall be the average of the actual collected revenues of the previous three fiscal years.  (2) Collected revenues shall include taxes, levies, duties, fees, profits and income from any investment or undertaking and any contribution to the revenue of the Governments from any political sub-division of the United Republic, excluding loans, grants and other forms of economic aid and all borrowing whether of short or long term.</p> <p><b>37. Prohibition of other credit to Governments, etc.</b>  Except as provided in sections 34 and 35, the Bank shall not extend any credit directly or indirectly to the Governments or any public authority.</p> <p><b>43. Bank may purchase, hold and sell securities.</b>  (1) For monetary policy purposes, the Bank may purchase, hold and sell securities issued by any of the Governments or by any authority for a political sub-division of the United Republic, but such purchases shall not be made to finance any Government budget deficit of either of the Governments and shall be made on the secondary market at market rates.</p>
<p><b>Zambia</b></p>	<p><b>Title: The Bank of Zambia Act No. 43 of 1996</b>  <b>Part VII Relations with Government</b>  <b>49. Advances to Government</b>  The Bank shall not advance funds to the Government except in special circumstances and on such terms and conditions as may be agreed upon between the Bank and the Minister.</p> <p><b>50. Limitations on Lending to Government</b>  (1) Except as provided in section 49 and in subsection (4), the Bank shall not directly or indirectly, at any time, give credit to the Government by way of short term advances, purchases or securities in a primary issue, or any other form or extension of credit that exceeds 15 percent of the ordinary</p>

	<p>revenue of Government in the previous financial year.</p> <p>(2) If in the opinion of the Bank the limitation provided for in subsection (1), is likely to be exceeded, the Bank shall submit to the Minister a report stating-</p> <p>(a) the details of the amounts then outstanding of the funds advanced and credit facilities extended by the Bank and the Bank's holding of securities referred to in subsection (1);</p> <p>(b) the causes which are likely to lead to such limitation being exceeded; and</p> <p>(c) its recommendation to forestall or otherwise remedy the situation.</p> <p>(3) The Bank shall continue to make further reports and recommendations on the matters referred to in subsection (2), at intervals of not more than six months until such time as, in its opinion, the situation has been rectified.</p> <p>(4) Where the limitation provided for in subsection (1) is exceeded, the Bank shall forthwith advise the Minister of that fact and shall not allow any further increase, whether directly or indirectly, in the aggregate amount of the funds advanced and credit facilities extended by the Bank and the Bank's holding of securities referred to in subsection (1).</p> <p><b>52. Transactions with Government Securities</b> The Bank may underwrite, purchase, sell, or deal in securities issued or guaranteed by the Government which form part of a public issue.</p>
<b>Asia</b>	
<b>Cambodia</b>	<p><b>Title: Law on the Organization and Functioning of the National Bank of Cambodia - Kram dated January 26, 1996</b></p> <p><b>Title VI: Financial Relations with Public Entity</b></p> <p><b>Article 24</b> The Central Bank shall not directly or indirectly extend to the Royal Government, including by the purchase in a primary issue of securities issued or guaranteed by the government or by public entities, except in accordance with the provisions of this Title.</p> <p><b>Article 25</b> The Central Bank may temporarily extend credit to the National Treasury at the refinancing rate and a maturity not exceeding three months.</p> <p>1. For each extension of credit, there shall be a credit agreement between the Central Bank and the borrower, which shall specify the amount of the credit, its maturity, and the interest rate.</p> <p>2. Such extensions of credit shall be certificated by negotiable government securities delivered to the Central Bank.</p> <p>3. The aggregate amount of the outstanding extensions of credit and holdings of securities described under Article 24 for each financial year shall not exceed 10% (ten percent) of the ordinary domestic budget revenues, excluding grants and proceeds from the sale of assets, for the previous financial year.</p> <p><b>Article 27</b> The Royal Government shall consult the Central Bank every year before the budget is finalized with a view to establishing the total amount of credit which the Royal Government and public entities may seek to secure from the Central Bank within the limits prescribed by Article 25.</p> <p><b>Title XI: Miscellaneous Provisions</b></p> <p><b>Article 63</b> The limitation on credit in subparagraph 3 of Article 25 of this law shall apply to credit extended after the effective date of this law.</p>

<p><b>China</b></p>	<p><b>Title: Law of the People's Republic of China on the People's Bank of China, December 27, 2003</b>  <b>Last Amendment: December 27, 2003</b>  <b>Chapter IV: Business Operations</b>  <b>Article 29</b>  The People's Bank of China shall not provide overdraft for government or directly subscribe to or underwrite treasury bonds and other government securities.  <b>Article 30</b>  The People's Bank of China shall not lend to local governments and government agencies at various levels, or to nonbank financial institutions, other organizations and individuals. However, in exceptional cases, it may lend to non-bank financial institutions deemed eligible by the State Council for such lending.  The People's Bank of China shall not provide guarantee for any institutions or individuals.</p> <p><b>Chapter VII : Legal Liabilities</b>  <b>Article 48</b>  <b><i>If the People's Bank of China commits any of the following acts, the managers and other persons directly responsible for the misconduct shall be subject to administrative sanctions according to law, whereas the case constitutes a crime, the offenders shall be investigated for criminal responsibility according to law:</i></b>  (1) Providing lending in violation of the provisions in the first paragraph of Article 30;  (2) Providing guarantee for an institution or individual; and  <b>Article 49</b>  If a local government, a government department at any level, a public organization or an individual forces the People's Bank of China or its employees to provide a loan or a guarantee in violation of the provisions in Article 30, the managers and other persons directly responsible for the misconduct shall be subject to administrative sanctions in accordance with the law. If the case constitutes a crime, the offenders shall be investigated for criminal responsibility according to law. If losses are incurred, the offenders shall be liable to partial or full compensation of the losses.</p>
<p><b>India</b></p>	<p><b>Title: The Reserve Bank of India Act, 1934 (Act No. 2 of 1934)</b>  <b>Last Amendment: 12 June 2006</b>  <b>Chapter II: Incorporation, Capital Management, and Business</b>  <b>17. Business which the Bank may transact.</b>  <b><i>The Bank shall be authorized to carry on and transact the several kinds of business hereinafter specified, namely:</i></b>  (5) the making to the Central Government and State Governments of advances repayable in each case not later than three months from the date of the making of the advance;  (8) the purchase and sale of securities of the Central Government or a State Government of any maturity or of such securities of a local authority as may be specified in this behalf by the Central Government on the recommendation of the Central Board:  Provided that securities fully guaranteed as to principal and interest by any such Government or authority shall be deemed for the purposes of this clause to be securities of such Government or authority;  [(12AA) lending or borrowing of securities of the Central Government or a State Government or of such securities of a local authority as may be specified in this behalf by the Central Government or foreign securities;  (12AB) dealing in repo or reverse repo:  Provided that lending or borrowing of funds by way of repo or reverse repo shall not be subject to any limitation contained in this section.  Explanation.—For the purposes of this clause:  (a) “repo” means an instrument for borrowing funds by selling securities of the Central</p>

	<p>Government or a State Government or of such securities of a local authority as may be specified in this behalf by the Central Government or foreign securities, with an agreement to repurchase the said securities on a mutually agreed future date at an agreed price which includes interest for the funds borrowed;</p> <p>(b) “reverse repo” means an instrument for lending funds by purchasing securities of the Central Government or a State Government or of such securities of a local authority as may be specified in this behalf by the Central Government or foreign securities, with an agreement to resell the said securities on a mutually agreed future date at an agreed price which includes interest for the funds lent;]</p>
<b>Indonesia</b>	<p><b><i>Title: Act of the Republic of Indonesia Number 23 of 1999 concerning Bank Indonesia Chapter VIII Relationship with the Government</i></b></p> <p><b><i>Article 56</i></b></p> <p>(1) Bank Indonesia shall not provide any credit to the Government.</p> <p>(2) In the event that Bank Indonesia violate the provision as referred to in paragraph (1), the agreement to extend credit to the Government shall be null and void.</p> <p><b><i>Article 76</i></b></p> <p>(1) The provision which prohibits Bank Indonesia to purchase for itself the state debt securities as referred to in Article 55 paragraph (4) shall be effective at latest January 1, 2000, except for the financing of banking restructuring.</p> <p>(2) Bank Indonesia may, for any claims on the state debt securities which have been directly purchased by Bank Indonesia and still have not reached the maturity period, extend the term of the claims at a maximum of 10 (ten) years since the maturity date if it is deemed necessary by the Government upon the approval of the House of Representatives.</p> <p>(3) The Government shall, in the event that the term of the claims has to be extended, propose the application of the term extension of such claims at the latest 30 (thirty) days prior to the due date of such claims.</p> <p><b><i>Title: Act of the Republic of Indonesia Number 3 of 2004 concerning amendment to Act of the Republic of Indonesia</i></b></p> <p><b><i>Source: Text in English from central bank website</i></b></p> <p><b><i>Article 55</i></b></p> <p>(1) In the event that the Government intends to issue government securities, the Government shall hold prior consultations with Bank Indonesia.</p> <p>(2) Prior to the issuance of government securities as referred to in paragraph (1), the Government shall be required to hold consultations with the House of Representatives.</p> <p>(3) Bank Indonesia may provide assistance in the issuance of government securities issued by the Government as referred to in paragraph (1).</p> <p>(4) Bank Indonesia is prohibited from buying government securities as referred to in paragraph (1) on the primary market for its own account, except in the case of short-term government securities needed by Bank Indonesia for monetary control operations;</p> <p>(5) Bank Indonesia may buy government securities on the primary market as part of the provision of the emergency financing facility as referred to in Article 11 paragraph (4).</p>
<b>Japan</b>	<p><b><i>Chapter IV Business</i></b></p> <p><b><i>Article 33 (Regular Business)</i></b></p> <p><b><i>(1) In order to achieve the purpose prescribed in Article 1, the Bank of Japan may conduct the following business:</i></b></p> <p>(iii) Buying and selling of commercial bills and other negotiable instruments (including those drawn by the Bank of Japan in this item), national government securities and other bonds, or electronically recorded claims;</p> <p><b><i>Article 34 (Loans, etc. to the National Government)</i></b></p>

	<p>As the central bank of Japan, the Bank of Japan may, in addition to the business prescribed in paragraph 1 of the preceding Article, conduct the following business with the national government:</p> <ul style="list-style-type: none"> <li>(i) Making uncollateralized loans within the limit decided by the Diet as prescribed in the proviso of Article 5 of the Fiscal Act (Act No. 34 of 1947);</li> <li>(ii) Making uncollateralized loans for the national government's temporary borrowing permitted under the Fiscal Act or other acts concerning the national government's accounting;</li> <li>(iii) Subscribing or underwriting national government securities within the limit decided by the Diet as prescribed in the proviso of Article 5 of the Fiscal Act;</li> <li>(iv) Subscribing or underwriting financing bills and other financing securities;</li> <li>(v) Taking safe custody of precious metals and other articles.</li> </ul>
Korea	<p><b><i>Title: The Bank of Korea Act, Law No. 138 promulgated on May 5, 1950</i></b>  <b><i>Last Amendment: Law 8863, promulgated on February 29, 2008</i></b></p> <p><b><i>Chapter II. The Monetary Policy Committee</i></b>  <b><i>Section 3. Powers of the Monetary Policy Committee</i></b>  <b><i>Article 28 (Decisions on Monetary and Credit Policies)</i></b>  <b><i>The Monetary Policy Committee shall deliberate and decide on matters involving the following Clauses on monetary and credit policies:</i></b></p> <p>6. Basic matters concerning the purchase and sale of Government bonds, securities guaranteed by the Government, and so forth in the open market;</p> <p><b><i>Chapter IV. Operations of the Bank of Korea</i></b>  <b><i>Section 5. Business with the Government and Government Agencies</i></b>  <b><i>Article 75 (Credit to the Government, etc.)</i></b></p> <p>(1) The Bank of Korea may render credit to the Government on overdrafts or in other forms, and may directly subscribe to Government bond issues.</p> <p>(2) The aggregate of all loans and direct subscriptions to Government bonds specified in Paragraph (1) shall not exceed the amount of the indebtedness which, together with any borrowing by the Government from other banking institutions and the public, has been authorized by the National Assembly.</p> <p>(3) The interest rates and other terms of the credit as provided for in Paragraph (1) shall be determined by the Monetary Policy Committee.</p> <p><b><i>Article 76 (Direct Subscription to Securities Guaranteed by the Government)</i></b></p> <p>(1) The Bank of Korea may directly subscribe to securities whose redemption in full and interest payments are guaranteed by the Government.</p> <p>(2) The interest rates and other terms of the subscription to such securities as specified in Paragraph (1) shall be determined by the Monetary Policy Committee.</p> <p><b><i>Article 77 (Deposits from and Loans to Government Agencies)</i></b></p> <p>(1) The Bank of Korea may accept deposits from, and make loans to, government agencies.</p> <p>(2) The term “government agencies” as used in Paragraph (1) shall be defined as juridical persons which are designated by the Government to execute on its behalf projects or functions of a public character in the fields of production, purchase, sale or distribution.</p> <p>(3) The redemption in full and interest payments of the loans stipulated in Paragraph (1) shall be guaranteed by the Government.</p> <p>(4) The Monetary Policy Committee shall determine the interest rates and other terms of loans by the Bank of Korea to government agencies.</p> <p><b><i>Article 78 (Restrictions on Credit to Government Agencies)</i></b>  The Bank of Korea shall, in periods of monetary expansion, endeavor to restrict its credit to government agencies and to contract the outstanding volume of such credit.</p>

	<p><b>Title: Enforcement Decree of the Bank of Korea Act , May 23, 1950</b>  <b>Last Amendment: Presidential Decree No. 18169, December 30, 2003</b>  <b>Source: Text in English from central bank website</b>  <b>Article 15 (Designation of Government Agencies)</b></p> <p>(1) The government agencies prescribed in Article 77 of the Act shall be designated by the Minister of Finance and Economy after consultation with the ministers concerned, subject to the approval of the President of the Republic of Korea upon deliberation by the State Council.</p> <p>(2) The Minister of Finance and Economy may, after consultation with the ministers concerned, rescind the designation of the government agencies, subject to the approval of the President of the Republic of Korea upon deliberation by the State Council.</p>
<b>Europe</b>	
France	<p><b>Title: Treaty Establishing the European Community, December 29, 2006</b>  <b>Article 101</b></p> <p>1. Overdraft facilities or any other type of credit facility with the ECB or with the central banks of the Member States (hereinafter referred to as ‘national central banks’) in favor of Community institutions or bodies, central governments, regional, local or other public authorities, other bodies governed by public law, or public undertakings of Member States shall be prohibited, as shall the purchase directly from them by the ECB or national central banks of debt instruments.</p> <p>2. Paragraph 1 shall not apply to publicly owned credit institutions which, in the context of the supply of reserves by central banks, shall be given the same treatment by national central banks and the ECB as private credit institutions.</p> <p><b>Title: Protocol (No. 18) on the Statute of the European System of Central banks (ESCB) and of the ECB (1992)</b>  <b>Chapter IV. Monetary Functions and Operations of the ESCB</b>  <b>Article 21. Operations with public entities</b></p> <p>21.1. In accordance with Article 101 of this Treaty, overdrafts or any other type of credit facility with the ECB or with the national central banks in favor of Community institutions or bodies, central governments, regional, local or other public authorities, other bodies governed by public law, or public undertakings of Member States shall be prohibited, as shall the purchase directly from them by the ECB or national central banks of debt instruments.</p> <p>21.3. The provisions of this Article shall not apply to publicly owned credit institutions which, in the context of the supply of reserves by central banks, shall be given the same treatment by national central banks and the ECB as private credit institutions.</p> <p><b>Title: Statute of the Bank of France. Monetary and Financial Code</b>  <b>Last Amendment: August 2008, following the law No. 2008–776 of August 4, 2008</b>  <b>Chapter I Task</b>  <b>1.1. Part Main tasks</b>  <b>Article L141-3</b></p> <p>The Bank of France is prohibited from authorizing overdrafts or granting any other type of credit to the Treasury or to any other public body or undertaking. The direct acquisition of their debt instruments by the Bank of France is also prohibited.</p> <p>The agreements entered into between the Government and the Bank of France determine, when necessary, the terms of repayment of the advances granted to the Treasury by the Bank of France prior to January 1, 1994.</p> <p>The provisions of the first paragraph do not apply to public credit institutions which enjoy the same treatment as private credit institutions in regard to the provision of liquid assets by the Bank of France.</p>

Germany	<p><b>Title: Treaty Establishing the European Community, December 29, 2006</b>  <b>Article 101</b>  1. Overdraft facilities or any other type of credit facility with the ECB or with the central banks of the Member States (hereinafter referred to as ‘national central banks’) in favor of Community institutions or bodies, central governments, regional, local or other public authorities, other bodies governed by public law, or public undertakings of Member States shall be prohibited, as shall the purchase directly from them by the ECB or national central banks of debt instruments.  2. Paragraph 1 shall not apply to publicly owned credit institutions which, in the context of the supply of reserves by central banks, shall be given the same treatment by national central banks and the ECB as private credit institutions.</p> <p><b>Title: Protocol (No. 18) on the Statute of the ESCBs and of the ECB (1992)</b>  <b>Chapter IV. Monetary Functions and Operations of the ESCB</b>  <b>Article 21. Operations with public entities</b>  21.1. In accordance with Article 101 of this Treaty, overdrafts or any other type of credit facility with the ECB or with the national central banks in favor of Community institutions or bodies, central governments, regional, local or other public authorities, other bodies governed by public law, or public undertakings of Member States shall be prohibited, as shall the purchase directly from them by the ECB or national central banks of debt instruments.  21.3. The provisions of this Article shall not apply to publicly owned credit institutions which, in the context of the supply of reserves by central banks, shall be given the same treatment by national central banks and the ECB as private credit institutions.</p> <p><b>Title: Bundesbank Act, August 2007</b>  <b>Last Amendment: 21 December 2007 (Federal Law Gazette I, page 3089)</b>  <b>Part V: Scope of business</b>  <b>20 Transactions with public authorities</b>  The Deutsche Bundesbank shall be entitled to conduct the transactions specified in section 19, numbers 2 to 7, with the Federal Republic of Germany, the Federal special funds, the federal states (Länder) and other public authorities; for this purpose, the Bank may grant intraday credit. With regard to such transactions the Bank may not charge the Federal Republic of Germany, Federal special funds or the federal states for any expenses incurred or levy any fees.</p>
Israel	<p><b>Title: Bank of Israel Law, 5714-1954</b>  <b>Chapter Seven: Foreign Exchange Operations</b>  <b>38. Power to borrow and guarantee</b>  (a) The Bank may, with the approval of the Government, borrow from a foreign government, a banking or financial institution outside Israel or an international financial institution (all these hereinafter are referred to as foreign institutions) and to pledge assets held by the Bank as security for the repayment of the loan. The Government may, with the approval of the Finance Committee of the Knesset, guarantee on behalf of the State a loan as aforesaid.  (b) The Bank may, with the approval of the Government, lend money to a foreign institution.  (c) The Bank may, with the approval of the Government, guarantee a loan granted to the State or any person in Israel by a foreign institution if, in the opinion of the Governor, such loan is in the public interest.</p> <p><b>Chapter Eight: Credit Operations of the Bank</b>  <b>45. Loans to Government</b>  (a) The Bank shall not make a loan to the Government to finance its expenditure.  (b) Notwithstanding the provision of subsection (a), the Bank may make to the Government, at its request</p>

	<p>(1) a provisional advance to bridge temporary gaps in the Government's cash flow in the implementation of the budget (hereinafter: provisional advance), provided that the total of the provisional advance shall not exceed, at any time, 1.6 percent of the total ordinary annual budget at that time; however, during two periods of the Government's choice in the course of the fiscal year, neither of which shall last longer than 30 days, the total provisional advance may reach 3.2 percent of the total ordinary annual budget at that time;</p> <p>(2) a loan by way of acquiring bonds issued by the Government to finance the excess of its expenditure in foreign currency over its revenue in foreign currency;</p> <p>(3) a loan for the purpose of paying debts incurred by it to the Bank under law, other than debts under paragraph (1); the conditions of the loan and the times for its repayment shall be fixed by agreement between the Minister of Finance and the Governor.</p> <p>(c) Bonds which the Government shall sell to the Bank in accordance with subsection (b)(2) shall be of one of the negotiable categories sold to the public under the State Loan Law 5739–1979, as the Minister of Finance shall determine in consultation with the Governor, and the provisions of the said Law shall apply to them; however, the restriction on the balance of the loan in section 1 there shall not apply; the bonds shall be sold at market price as will be agreed by the Minister of Finance and the Governor.</p> <p>(d) The Minister of Finance may prescribe, in consultation with the Governor, additional provisions, and conditions for the implementations of subsection (c).</p>
Italy	<p><b><i>Title: Treaty Establishing the European Community, December 29, 2006</i></b>  <b><i>Article 101</i></b></p> <p>1. Overdraft facilities or any other type of credit facility with the ECB or with the central banks of the Member States (hereinafter referred to as ‘national central banks’) in favor of Community institutions or bodies, central governments, regional, local or other public authorities, other bodies governed by public law, or public undertakings of Member States shall be prohibited, as shall the purchase directly from them by the ECB or national central banks of debt instruments.</p> <p>2. Paragraph 1 shall not apply to publicly owned credit institutions which, in the context of the supply of reserves by central banks, shall be given the same treatment by national central banks and the ECB as private credit institutions.</p> <p><b><i>Title: Protocol (No. 18) on the Statute of the European System of Central banks and of the European Central Bank (1992)</i></b>  <b><i>Chapter IV. Monetary Functions and Operations of the ESCB</i></b>  <b><i>Article 21. Operations with public entities</i></b></p> <p>21.1. In accordance with Article 101 of this Treaty, overdrafts or any other type of credit facility with the ECB or with the national central banks in favor of Community institutions or bodies, central governments, regional, local or other public authorities, other bodies governed by public law, or public undertakings of Member States shall be prohibited, as shall the purchase directly from them by the ECB or national central banks of debt instruments.</p> <p>21.3. The provisions of this Article shall not apply to publicly owned credit institutions which, in the context of the supply of reserves by central banks, shall be given the same treatment by national central banks and the ECB as private credit institutions.</p>
Netherlands	<p><b><i>Title: Treaty Establishing the European Community, December 29, 2006</i></b>  <b><i>Article 101</i></b></p> <p>1. Overdraft facilities or any other type of credit facility with the ECB or with the central banks of the Member States (hereinafter referred to as ‘national central banks’) in favor of Community institutions or bodies, central governments, regional, local or other public authorities, other bodies governed by public law, or public undertakings of Member States shall be prohibited, as shall the purchase directly from them by the ECB or national central banks of debt instruments.</p> <p>2. Paragraph 1 shall not apply to publicly owned credit institutions which, in the context of the</p>

	<p>supply of reserves by central banks, shall be given the same treatment by national central banks and the ECB as private credit institutions.</p> <p><b>Title: Protocol (No. 18) on the Statute of the European System of Central banks and of the European Central Bank (1992)</b>  <b>Chapter IV. Monetary Functions and Operations of the ESCB</b>  <b>Article 21. Operations with public entities</b></p> <p>21.1. In accordance with Article 101 of this Treaty, overdrafts or any other type of credit facility with the ECB or with the national central banks in favor of Community institutions or bodies, central governments, regional, local or other public authorities, other bodies governed by public law, or public undertakings of Member States shall be prohibited, as shall the purchase directly from them by the ECB or national central banks of debt instruments.</p> <p>21.3. The provisions of this Article shall not apply to publicly owned credit institutions which, in the context of the supply of reserves by central banks, shall be given the same treatment by national central banks and the ECB as private credit institutions.</p> <p><b>Title: Bank Act 1998</b>  <b>Last Amendment: 2004</b>  <b>Chapter II: Objectives, Tasks, and Activities of the Bank</b>  <b>Division 2. Activities</b>  <b>Section 8</b></p> <p>3. At the request of Our Minister and notwithstanding the provisions of subsection (I), the Bank shall grant the State, whenever Our Minister deems this necessary for the purpose of ensuring the smooth settlement of payments for the account of the State, unsecured overdraft facilities subject to a rate of interest to be agreed between Our Minister and the Bank The State shall be obliged to repay these overdrafts on the same day as that on which they are granted.</p>
Norway	<p><b>Title: The Norges Bank Act, September 9, 1985</b>  <b>Last Amendment: Act No. 11 of March 16, 2007</b>  <b>Chapter IV. Role in the credit market</b>  <b>Section 18. Extension of credit to the government</b></p> <p>The Bank may not extend credit directly to the government.  Amended by Act No. 44 of 20 June 2003 (in force as from January 1, 2005 pursuant to decision No. 1600 of December 19, 2003.)</p>
Spain	<p><b>Title: Consolidated Version of the Treaty Establishing the European Community, December 29, 2006</b>  <b>Article 101</b></p> <p>1. Overdraft facilities or any other type of credit facility with the ECB or with the central banks of the Member States (hereinafter referred to as ‘national central banks’) in favor of Community institutions or bodies, central governments, regional, local or other public authorities, other bodies governed by public law, or public undertakings of Member States shall be prohibited, as shall the purchase directly from them by the ECB or national central banks of debt instruments.</p> <p>2. Paragraph 1 shall not apply to publicly owned credit institutions which, in the context of the supply of reserves by central banks, shall be given the same treatment by national central banks and the ECB as private credit institutions.</p> <p><b>Title: Protocol (No. 18) on the Statute of the European System of Central banks and of the European Central Bank (1992)</b>  <b>Chapter IV. Monetary Functions and Operations of the ESCB</b>  <b>Article 21. Operations with public entities</b></p>

	<p>21.1. In accordance with Article 101 of this Treaty, overdrafts or any other type of credit facility with the ECB or with the national central banks in favor of Community institutions or bodies, central governments, regional, local or other public authorities, other bodies governed by public law, or public undertakings of Member States shall be prohibited, as shall the purchase directly from them by the ECB or national central banks of debt instruments.</p> <p>21.3. The provisions of this Article shall not apply to publicly owned credit institutions which, in the context of the supply of reserves by central banks, shall be given the same treatment by national central banks and the ECB as private credit institutions.</p> <p><b><i>Title: Law of Autonomy of The Banco de Espana - Law 13/1994 of June 1, 1994</i></b>  <b><i>Last Amendment: November 18, 2005</i></b>  <b><i>Chapter II</i></b>  <b><i>Objectives and Functions</i></b>  <b><i>Section 3. Cash Management and Public Debt Services</i></b>  <b><i>Article 13. Cash management services</i></b></p> <p>2. Overdraft facilities or the granting of any other type of credit by the Bank to the central government, Comunidades Autónomas, local authorities or any other of the authorities or entities referred to in article 104 of the Treaty creating the European Community -as amended by the Treaty on European Union of February 7, 1992-are prohibited. The exceptions to the above are as follows:</p> <p>a. Public credit institutions, which may receive liquidity from the Bank on the same terms as other credit institutions, and Deposit Guarantee Funds in credit institutions, when relevant.</p> <p>b. Financing by the Bank of obligations incurred by the government with the International Monetary Fund, or arising from the implementation of the medium-term financial assistance facility of the European Community.</p> <p><b><i>Article 14. Public debt service functions</i></b></p> <p>2. The Bank may not directly acquire from issuers any type of public debt. It may only acquire it in markets, in the exercise of the functions assigned to it.</p> <p><b><i>Second Transitory Provision</i></b></p> <p>Until the agreements mentioned in article 13.1 and 14.1 are approved, the Bank, without prejudice of the terms of article 13.2, shall continue providing to the Treasury and, as relevant, to Comunidades Autónomas, cash management and public debt services as described in current provisions.</p>
Sweden	<p><b><i>Title: Treaty Establishing the European Community, December 29, 2006</i></b>  <b><i>Article 101</i></b></p> <p>1. Overdraft facilities or any other type of credit facility with the ECB or with the central banks of the Member States (hereinafter referred to as 'national central banks') in favor of Community institutions or bodies, central governments, regional, local or other public authorities, other bodies governed by public law, or public undertakings of Member States shall be prohibited, as shall the purchase directly from them by the ECB or national central banks of debt instruments.</p> <p>2. Paragraph 1 shall not apply to publicly owned credit institutions which, in the context of the supply of reserves by central banks, shall be given the same treatment by national central banks and the ECB as private credit institutions.</p> <p><b><i>Title: Treaty Establishing the European Community, December 29, 2006</i></b>  <b><i>Source: Text in English from EU website. 29.12.2006 EN Official Journal of the European Union C321 E/37</i></b>  <b><i>Article 103</i></b></p> <p>2. If necessary, the Council, acting in accordance with the procedure referred to in Article 252, may specify definitions for the application of the prohibition referred to in Article 101 and in this Article.</p>

	<p><b>Title: Protocol (No. 18) on the Statute of the European System of Central banks and of the European Central Bank (1992)</b>  <b>Chapter IV. Monetary Functions and Operations of the ESCB</b>  <b>Article 21. Operations with public entities</b></p> <p>21.1. In accordance with Article 101 of this Treaty, overdrafts or any other type of credit facility with the ECB or with the national central banks in favor of Community institutions or bodies, central governments, regional, local or other public authorities, other bodies governed by public law, or public undertakings of Member States shall be prohibited, as shall the purchase directly from them by the ECB or national central banks of debt instruments.</p> <p>21.3. The provisions of this Article shall not apply to publicly owned credit institutions which, in the context of the supply of reserves by central banks, shall be given the same treatment by national central banks and the ECB as private credit institutions.</p> <p><b>Title: The Sveriges Riksbank Act, 1988</b>  <b>Last Amendment: January 1, 2007</b>  <b>Chapter 8 Other tasks</b>  <b>Art. 1</b> The Riksbank shall not extend credit to or purchase debt instruments directly from the state, another public body, or an institution of the European Union.  The Riksbank may, however, pursuant to Chapter 6, Article 7 paragraph 2, grant intraday credit to the state. Subject to other provisions in this Act, the Riksbank may also grant credit to and purchase debt instruments from financial institutions owned by the state or another public body.</p>
Turkey	<p><b>Title: Law on the Central Bank of the Republic of Turkey. Law No. 1211</b>  <b>Last Amendment: 2008</b>  <b>Part VI: Operations Prohibited for the Bank</b>  <b>Article 56- (As amended by Law No. 4651 of April 25, 2001)</b></p> <p>The Bank shall not, grant advance and extend credit to the Treasury and to public establishments and institutions, and shall not purchase debt instruments issued by the Treasury and public establishments and institutions in the primary market.</p> <p>The Bank shall not extend credits and grant advances except for the operations authorized by this Law, and the credit to be extended and the advance to be granted shall not be unsecured or without cover, and in any manner whatsoever the Bank shall not, be a guarantor or provide security other than its own direct transactions.</p>
<b>Middle East</b>	
Azerbaijan	<p><b>Title: The Law of the Republic of Azerbaijan on the National Bank of the Republic of Azerbaijan</b>  <b>Chapter III. Relations of the National Bank with Government Authorities</b>  <b>Article 16. National Bank's Loans to the State</b></p> <p>16.1. The National Bank shall not loan to the state directly for the purposes of funding the state budget deficit.</p> <p>16.2. In the event of a short-term liquidity shortfall in the state budget, the National Bank may extend a six-month loan to the government under an agreement with the appropriate executive power against collateral of interest-bearing government securities and on condition of repayment by the state budget for the current year. The total amount of the loans issued and of their unpaid part cannot be higher than 3 percent of state budget average revenues for the past three years.</p> <p>16.3. The purchase of securities issued by the Azerbaijan government by the National Bank is considered as an issue of credits to the state, unless they are under the condition of Article 49-1-2. Such transactions can be made in the secondary market only and conditions of Article 16.2 of this law shall be applicable to them.</p> <p>16.4. In cases relating to the implementation of monetary policy, the provisions of Article 16.2 of this Law shall not apply, provided that government securities trading activities are carried out in the secondary market.</p>

	<p>49-1-2. In the event of necessity to cover debt commitment on the targeted loan through state guarantee and in the event of full or partial coverage of this commitment through debt securities issued by the State, at the consent of the central bank, the central bank may acquire the securities in the primary market in compliance of the terms of issuance.</p>
Morocco	<p><b>Title: Statutes of Bank Al-Maghrib. Dahir No. 1-05-38 of chaoual 1426 (November 23, 2005) promulgating Law No. 76-03 on the statutes of Bank Al-Maghrib</b>  <b>Source: Text in French from central bank website. IMF unofficial translation.</b>  <b>Chapter III. Operations of the Bank</b>  <b>Section III. Monetary policy operations</b>  <b>Article 27</b>  The Bank may only grant financial assistance to the State, or guarantee commitments entered into by the State, in the form of the overdraft facility contemplated in paragraph 2 of this Article. The overdraft facility is limited to five per cent of the fiscal revenue of the preceding fiscal year. The total duration of use of this facility may not exceed 120 days, whether consecutive or not, in any one fiscal year. The amounts actually used under this facility shall pay interest at the base rate for banks refinancing with the Bank.  The Bank may suspend use of this facility when it deems that the state of the money market so warrants.  The Bank may not grant financial assistance of any kind to any public enterprise or agency, nor may it guarantee commitments entered into by them. However, these provisions do not apply to public lending institutions licensed to operate as banks in respect of their refinancing operations with the Bank.</p> <p><b>Chapter X. Transitory provisions</b>  <b>Article 62</b>  An agreement to be entered into by the State and the Bank by no later than three months after the entry into force of this law will establish the remuneration, duration and procedures for repayment of all assistance granted to the State as at that date.</p>
Saudi Arabia	<p><b>Title: Charter of the Saudi Arabian Monetary Agency Issued by Royal Decree No. 23 dated 23-5-1377, December 15, 1957</b>  <b>Article 6</b>  <b>The Agency shall not undertake any of the following functions:</b>  c. Making advances to the Government or private parties;</p>
<b>Western Hemisphere</b>	
Bahamas	<p><b>Title: Central Bank of The Bahamas Act, 2000</b>  <b>Part VII: Relations with the Government</b>  <b>28. Advances to the Government</b>  (1) Subject to the provisions of this section, the Bank may make temporary advances to the Government on such terms and conditions as may be agreed between the Minister and the Bank.  (2) Every such advance made by the Bank to the Government shall be repaid by the Government as soon as possible.  (3) The amount of any such advances by the Bank to the Government which may be outstanding at any one time shall not exceed ten per centum of the average ordinary revenue of the Government or ten per centum of the estimated ordinary revenue of the Government, whichever is the less.  (4) In sub-section (3):  "ordinary revenue" means all income or contributions to Government revenue not being loans, capital grants or other receipts of a capital nature;</p>

	<p>"average ordinary revenue" means the annual average of the ordinary revenue of the Government over the three years (for which accounts have been laid before Parliament) next before the year in which any question under the subsection is raised;</p> <p>"estimated ordinary revenue" means the ordinary revenue, as estimated in the estimates of the Government as laid before Parliament, for that year.</p> <p><b>Part VIII: General Powers of the Bank</b></p> <p><b>29. Powers of the Bank</b></p> <p><b>(1) Subject to the provisions of this Act, the Bank may, in the discharge of its functions:</b></p> <p>(c) buy, hold and sell securities issued or guaranteed by the Government, being securities issued to the public and maturing within twenty years from the date of their acquisition by the Bank, but so that the total amount of any such securities at any time held by the Bank which mature beyond five years after their date of issue (including any such securities held by the Bank as security for any loans or advances) shall not exceed twenty per centum of the demand liabilities of the Bank;</p> <p>(f) make to any commercial bank or any public corporation, on such terms and conditions as may be determined by the Bank, loans or advances on the security of any of the following, that is to say:</p> <p>(i) gold coins or gold bullion;</p> <p>(ii) bills of exchange, promissory notes, other credit instruments, Treasury Bills or securities, being bills of exchange, promissory notes, credit instruments, Treasury Bills or securities of any kind mentioned in paragraph (b) or (c);</p> <p>(iii) warehouse warrants or other documents to goods duly insured and secured by a letter of hypothecation from the owner; or</p> <p>(iv) securities of any kind mentioned in paragraph (d) or (e).</p> <p>(2) Where any loan or advance is made on the security of any instrument mentioned in subsection (1)(f) (ii)</p> <p>(a) the loan or advance shall not extend beyond the maturity date of the instrument itself or ninety-three days, whichever is the longer; and</p> <p>(b) the amount of any such loan or advance shall not exceed eighty-five per centum of the market value of the instrument at the date of its acquisition by the Bank.</p> <p>(3) Subject to the provisions of this Act, the Bank may in the discharge of its functions do any other banking business incidental to or consequential upon the functions of the Bank.</p>
Brazil	<p><b>Title: Constitution of Brazil</b></p> <p><b>Last Amendment: March 8, 2006</b></p> <p><b>Title VI – Taxation and Budget</b></p> <p><b>Chapter II – Public Finances – Section I – General Rules</b></p> <p><b>Article 164</b></p> <p>Paragraph 1 – It is forbidden for the central bank to grant, either directly or indirectly, loans to the National Treasury and to any body or agency which is not a financial institution.</p> <p><b>Title: Law No. 4595 of December 31, 1964.</b></p> <p><b>Last Amendment: 1998</b></p> <p><b>Chapter II: National Monetary Council</b></p> <p><b>Article 4</b></p> <p><b>Pursuant to the guidelines established by the President of the Republic, the National Monetary Council shall:</b></p> <p>XIX. Establish rules to be observed by the Central Bank of Brazil in its transactions in public securities and in securities issued by entities in which the State has a shareholding;</p> <p>XX. Authorize the Central Bank of Brazil and federal public financial institutions to subscribe to, buy, and sell shares and other securities issued or under the responsibility of semipublic enterprises and State enterprises;</p>

	<p><b>Chapter III: Central Bank of Brazil</b>  <b>Article 10</b>  <b>The Central Bank of Brazil shall, on an exclusive basis:</b>  XII. Purchase and sell federal public securities, as an instrument of monetary policy;  <b>Article 12.</b>  The Central Bank of Brazil shall operate solely with public and private financial institutions and is prohibited from engaging in banking operations of any nature with other entities under public or private law except as expressly authorized by law.</p>
Canada	<p><b>Title: Bank of Canada Act</b>  <b>Last Amendment: August 5, 2008</b>  <b>BUSINESS AND POWERS OF THE BANK</b>  <b>Powers and business</b>  <b>18. The Bank may</b>  (i) make loans or advances for periods not exceeding six months to the Government of Canada or the government of a province on taking security in readily marketable securities issued or guaranteed by Canada or any province;  (j) make loans to the Government of Canada or the government of any province, but such loans outstanding at any one time shall not, in the case of the Government of Canada, exceed one-third of the estimated revenue of the Government of Canada for its fiscal year, and shall not, in the case of a provincial government, exceed one-fourth of that government's estimated revenue for its fiscal year, and such loans shall be repaid before the end of the first quarter after the end of the fiscal year of the government that has contracted the loan;</p>
Chile	<p><b>Title: Constitution of the Republic of Chile 1980</b>  <b>Last Amendment: 20.050, September 17, 2005</b>  <b>Chapter XIII. Central Bank</b>  <b>Article 109</b>  The Central Bank may only perform transactions with financial institutions, either public or private. In no way whatsoever may it act as collateral thereof nor secure documents issued by the State, its Bodies, or Enterprises.  No public expenditure or loan may be financed with direct or indirect credits of the Central bank. However, in case of a foreign war or the menace of such a war, as determined by the National security Council, the Central Bank may secure, grant, or finance credits to the State and public or private entities.  The Central Bank may not adopt any agreement which should represent, in a direct or indirect manner, the establishment of different or discriminatory norms or requirements in relation to persons, institutions or entities perform.</p> <p><b>Title: Law 18,840 Basic Constitutional Act of the Central Bank of Chile</b>  <b>Last Amendment: January 2006</b>  <b>Title III: The Authority and the Operations of the Bank</b>  <b>Subtitle One, General Provisions</b>  <b>Section 27</b>  The Bank may grant financing or refinancing to banking entities and financial institutions only. Under no circumstances shall the Bank grant to such entities and institutions its guarantee, nor acquire securities issued by the state, its agencies, or enterprises.  No public expenditure or credit of whatsoever nature may be financed either directly or indirectly with loans granted by the Bank.  However, in the event of foreign war or threat of foreign war, to be qualified by the Council on National Security by means of a secret resolution, the Bank may obtain, confer, or finance credits to the state and to public or private entities.</p>

Honduras	<p><b>Title: Law on the Central Bank of Honduras, Decree 53 of February 3, 1950</b>  <b>Last Amendment: October 7, 2004</b>  <b>Chapter III. Operations</b>  <b>Section IV. Exceptional Credit Operations with the Public Sector</b>  <b>Special Credit to the Public Sector. (Amended by Decree 111-2004 of August 17, 2004). Article 40.</b></p> <p>Without prejudice to the provisions of Article 5 of this Law, the Central Bank of Honduras may only extend loans to the government and to official agencies by buying securities on the secondary market. These loans may not exceed the limits unanimously approved by the Board of Directors. Securities so bought by the Central Bank may be traded with the public and with financial system institutions.</p> <p>The provisions of the foregoing paragraph shall not apply to loans that the BCH extends to the Government in emergency situations and serious government crises. The granting of these loans shall require unanimous approval by the Board of Directors, as well as ratification by Decree issued by the President of the Republic in the Council of Ministers. The National Congress shall be notified immediately of any such Decree.</p> <p>The restrictions in the first paragraph of this Article shall not apply in the case of BCH loans to the government to cover seasonal fluctuations in revenues and expenditures. These loans shall be made on terms of no longer than six (6) months, at market rates, and shall be limited to ten percent (10 percent) of total tax revenues for the prior fiscal year. They must be unanimously approved by the Board of Directors. At all events, the loans referred to in this paragraph shall be repaid in the same fiscal year in which they are applied for.</p>
Mexico	<p><b>Title: Banco De Mexico Law of 1993, December 23, 1993</b>  <b>Last Amendment: January 19, 1999</b>  <b>Chapter III: Operations</b>  <b>Article 7</b>  <b>Banco de México shall be entitled to perform the following activities:</b></p> <p>II. Grant credit to the Federal Government, to credit institutions and to the Institute for Protection of Bank Depositors;  (Modified in the Official Gazette of the Federation published on January 19, 1999).</p> <p><b>Article 9</b></p> <p>Banco de México shall not lend securities to the Federal Government nor purchase securities from it, except when purchases of securities that are payable by the Government comply with one of the two following conditions:</p> <p>I When said purchases are covered by cash deposits, made by the Government in the Bank with the proceeds of the placement of said securities, and which may not be withdrawn before their maturity date; the amounts, terms and yield on these deposits must be equal to the amounts, terms and yield of the securities being traded; or</p> <p>II. When purchases of securities result from bids by the Bank in primary auctions of said securities. The amount of these purchases may under no circumstance exceed the amounts of securities payable by the Government, owned by the Bank and redeemable on the same date of placement of the securities being auctioned.</p> <p><b>Article 10</b></p> <p>Only the Central Bank may act as the Federal Government's agent in issuing, placing, purchasing and selling Government domestic debt securities and, in general, in servicing said debt.</p> <p><b>Article 11</b></p> <p>Banco de México may grant credit to the Federal Government only through the current account the Federal Treasury holds in the Bank, and subject to provisions of Article 12. For the purposes of this Law, securities payable by the Federal Government and owned by the Central Bank are not</p>

	<p>considered as credit.</p> <p><b>Article 12</b>  <b><i>Banco de México shall carry a current account for the Federal Treasury which will be managed according to the terms agreed to by both parties and in all cases according to the following:</i></b></p> <p>II. Banco de México may, without authorization of the Federal Treasurer, charge the account in order to cover the service on the domestic debt of the Federal Government;</p> <p>III. No checks or any other documents payable to third parties may be drawn on this account, and</p> <p>IV. Should the Federal Government's balance in the current account be negative, said balance must never exceed the equivalent of 1.5 percent of the Federal Government's expenses as laid out in the Federal Expense Budget for the corresponding year, not taking outlays destined to amortize the Government's debt into consideration; this provision may be void if, due to extraordinary circumstances, the temporary differences between public revenues and expenses increase considerably.</p> <p>Should the negative balance of the account exceed the aforementioned limit, the Bank must proceed to place securities payable by the Federal Government on the market, on behalf of the Government and for an amount equivalent to the balance in excess of the limit. If necessary or appropriate, the Bank, again on behalf of the Federal Government, shall issue securities payable by the Government and place them on the market. In determining the characteristics of the placement and, if necessary, the issuance, the Bank shall seek the best possible terms for the Government as the market allows. The Bank must place the aforementioned securities within fifteen business days from the date on which the limit is exceeded, and offset the excess credit with the proceeds of the corresponding placement. In exceptional cases, if it helps to prevent disruptions in the financial market, the Board of Governors of the Bank may extend that term, in one or more instances, for a total duration of no longer than three months.</p> <p><b>Chapter VI: Government and Supervision</b>  <b>Article 46</b>  <b><i>The Board of Governors shall be empowered to</i></b></p> <p>IV. Decide on the granting of the Bank's credit to the Federal Government.</p>
United States	<p>Section 14 (b) of the Federal Reserve Act 12 USC Sec.355</p> <p><b>Title 12 – Banks and Banking chapter 3 – Federal Reserve System Subchapter IX- Powers and Duties of Federal Reserve Sec. 355. Purchase and sale of obligations of National, State, and municipal governments; open market operations; purchases and sales from or to United States; maximum aggregate amount of obligations acquired directly from or loaned directly to United States</b></p> <p>Every Federal Reserve bank shall have power:</p> <p>(1) To buy and sell, at home or abroad, bonds and notes of the United States, bonds issued under the provisions of subsection (c) of section 1463 (11) of this title and having maturities from date of purchase of not exceeding six months, and bills, notes, revenue bonds, and warrants with a maturity from date of purchase of not exceeding six months, issued in anticipation of the collection of taxes or in anticipation of the receipt of assured revenues by any State, county, district, political subdivision, or municipality in the continental United States, including irrigation, drainage and reclamation districts, and obligations of, or fully guaranteed as to principal and interest by, a foreign government or agency thereof, such purchases to be made in accordance with rules and regulations prescribed by the Board of Governors of the Federal Reserve System. Notwithstanding any other provision of this chapter, any bonds, notes, or other obligations which are direct obligations of the United States or which are fully guaranteed by the United States as to principal and interest may be</p>

bought and sold without regard to maturities but only in the open market.

(2) To buy and sell in the open market, under the direction and regulations of the Federal Open Market Committee, any obligation which is a direct obligation of, or fully guaranteed as to principal and interest by, any agency of the United States.

**Section 12A of the Federal Reserve Act 12U.S.C.263 (b)**

No Federal Reserve Bank shall engage or decline to engage in open-market operations under Section 14 of this Act except in accordance with the direction of and regulations adopted by the Committee”.

**Title 31 – Money and Finance Subtitle IV – Monetary Transactions Subchapter I – Credit and Monetary Expansion Sec. 5301. Buying obligations of the United States Government**

(a) The President may direct the Secretary of the Treasury to make an agreement with the Federal reserve banks and the Board of Governors of the Federal Reserve System when the President decides that the foreign commerce of the United States is affected adversely because (1) the value of coins and currency of a foreign country compared to the present standard value of gold is depreciating; (2) action is necessary to regulate and maintain the parity of United States coins and currency; (3) an economic emergency requires an expansion of credit; or (4) an expansion of credit is necessary so that the United States Government and the governments of other countries can stabilize the value of coins and currencies of a country.

(b) Under an agreement under subsection (a) of this section, the Board shall permit the banks (and the Board is authorized to permit the banks notwithstanding another law) to agree that the banks will (1) conduct through each entire specified period open market operations in obligations of the United States Government or corporations in which the Government is the majority stockholder; and (2) buy directly and hold an additional \$3,000,000,000 of obligations of the Government for each agreed period, unless the Secretary consents to the sale of the obligations before the end of the period. © With the approval of the Secretary, the Board may require Federal Reserve banks to take action the Secretary and Board consider necessary to prevent unreasonable credit expansion.

Source: Central Bank Legislation Database.

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