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How Credit Policy Ends: Central Bankers and the Rise and Fall of Credit Controls in Italy, 1973–1983

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Since 2008, growing scepticism about the ability of market forces to ensure financial stability and environmental sustainability has revived interest in credit controls. Credit controls were common in Europe before the 'neoliberal turn' of the 1980s. However, the decline in support for these policies in the 1970s is not well understood. This article examines Italy's shift away from credit controls, focusing on the role of central bank economists and the Bank of Italy's monetary policy ideas. By analysing the discourse and research of central bankers from 1973 to 1983, the article shows that persistent fiscal deficits were the main driving force behind both the introduction and the subsequent abolition of credit controls. It also highlights the influence of a new generation of economists, such as Tommaso Padoa-Schioppa and Mario Monti, on Italian economic policy, providing a case study that contextualises the economic ideas shaping policy making in the European Monetary Union.

Introduction

In the 1970s, the reform of national credit policies became a central focus for central banks.[1] However, the implications of the decline of these policies for the history of European monetary integration have only been partially explored.[2] The delegitimisation of these policies significantly impacted the convergence of central banks and financial systems leading up to the establishment of the European Monetary Union (EMU). To fully understand the EMU's formation in the early 1990s, it is crucial to examine both the end of credit policy and the shift of central banks towards a 'market-based' regime.[3] Despite the renewed interest in credit policy within contemporary academic and policy debates,[4] few studies have investigated why the 'ideational consensus' on credit policy broke down in the 1970s. This consensus, characterised by broad agreement on the need for direct government intervention and strict financial regulation, as advocated by Keynesian economics, was an integral part of post-war economic strategies.[5]

[1] The term 'credit policy' has been used in a variety of ways, revealing a conceptual ambiguity. It is usually understood as the central bank's (or government's) ability to directly intervene in credit allocation by favouring specific sectors or institutions. Cf. section entitled 'The Multiple Meanings and History of Credit Controls'.

[2] D.R. Hodgman, *National Monetary Policies and International Monetary Cooperation* (Boston: Little, Brown & Co., 1974); Eric Monnet, *Controlling Credit: Central Banking and the Planned Economy in Post War France, 1948–1973* (Cambridge: Cambridge University Press, 2018).

[3] Monnet, *Controlling Credit*, 26.

[4] Dirk Bezemer, Josh Ryan-Collins, Frank van Lerven and Lu Zhang, 'Credit Policy and the "Debt Shift" in Advanced Economies', *Socio-Economic Review* 21, no. 1 (2023): 437–78; Eric Monnet and Jens van t Klooster, 'Using Green Credit Policy to Bring Down Inflation: What Central Bankers Can Learn from History', *The INSPIRE Sustainable Central Banking Toolbox, Policy Briefing Paper* 13 (2023).

[5] Stephen A. Marglin and Juliet B. Schor, eds., *The Golden Age of Capitalism: Reinterpreting the Post-War Experience* (Oxford: Oxford University Press, 1991).

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How can we explain the decline of credit policy? Was European monetary integration the primary driver of this change? In this article, I focus on Italy, highlighting the significance of the Bank of Italy's monetary policy ideas and their reappraisal by key economists. This intellectual shift played a crucial role in how Italy phased out credit controls and prepared for monetary convergence. The move to introduce and then dismantle these controls was driven mainly by domestic factors related to monetary and fiscal policy in a changing international environment, rather than by passive adaptation to European regulations. Central bankers' concerns about rising fiscal deficits, coupled with their 'policy learning' about the negative impact of controls on the allocative efficiency of the domestic credit system, were decisive in promoting financial innovation and deregulation.

In general, the end of the 'non-market' approach to monetary policy has often been neglected and treated only as part of the broader convergence process towards financial liberalisation. An extensive literature in economics has examined the consequences of financial liberalisation for economic growth, but the causes of financial reforms have usually received less attention.[6] The spontaneous emergence of increasingly unregulated and competitive financial markets due to the 'shock of the global' is often believed to have put pressure on post-war national financial systems, forcing them into global and regional processes of harmonisation, innovation and convergence.[7] For most European countries, financial deregulation is usually seen as a 'by-product' of this international trend. However, historical studies have pointed out that the 'market-driven' hypothesis fails to capture the nuances of different national paths and the 'agency' of domestic elites in shaping these processes, thus revealing a much more complex adjustment process.[8] In particular, some scholars have emphasised the role of central bankers, both at the domestic and international level, as pivotal actors or 'policy entrepreneurs' in actively pushing for financial and monetary reforms.[9] For example, the rise of the 'Eurodollar market' since the 1950s has been seen both as an attempt to circumvent existing financial restrictions and as a process actively encouraged by national monetary authorities.[10] The end of the system of credit controls reflects this complex and 'chaotic' process, characterised by a multiplicity of institutional paths in different countries.[11]

In the case of Italy, the political science literature has often considered the 'top-down' effects of globalisation and 'Europeanisation' processes as the main explanatory factor for various domestic changes.[12] However, in the long process of European integration, Italy was not only subjected to

[6] Robert G. King and Ross Levine, 'Finance and Growth: Schumpeter Might be Right', *The Quarterly Journal of Economics* 108, no. 3 (1993): 717–37; On the causes of financial reforms cf. Abdul Abiad and Ashoka Mody, 'Financial Reform: What Shakes It? What Shapes It?', *American Economic Review* 95, no. 1 (2005): 66–88.

[7] Beth A. Simmons, and Zachary Elkins, 'The Globalization of Liberalization: Policy Diffusion in the International Political Economy', *American Political Science Review* 98, no. 1 (2004): 171–89; Niall Ferguson, Charles S. Maier, Erez Manela and Daniel J. Sargent, eds., *The Shock of the Global: The 1970s in Perspective* (Cambridge, MA: Harvard University Press, 2010).

[8] R. Abdelal, *Capital Rules: The Construction of Global Finance* (Cambridge, MA: Harvard University Press, 2007); Michael M. Loriaux, *Capital Ungoverned: Liberalizing Finance in Interventionist States* (Ithaca, NY: Cornell University Press, 1997); Laurent Warlouzet, *Governing Europe in a Globalizing World: Neoliberalism and its Alternatives following the 1973 Oil Crisis* (London: Routledge, 2017); Alexis Drach and Youssef Cassis, eds., *Financial Deregulation: A Historical Perspective* (Oxford: Oxford University Press, 2021).

[9] Emmanuel Mourlon-Druol, *A Europe Made of Money: The Emergence of the European Monetary System* (Ithaca, NY: Cornell University Press, 2013); Eric Helleiner, *States and the Re-Emergence of Global Finance: From Bretton Woods to the 1990s* (Ithaca, NY: Cornell University Press, 1996); Ethan Barnaby Kapstein, 'Between Power and Purpose: Central Bankers and the Politics of Regulatory Convergence', *International Organization* 46, no. 1 (1992): 265–87.

[10] Jeremy Green, 'Anglo-American Development, the Euromarkets, and the Deeper Origins of Neoliberal Deregulation', *Review of International Studies* 42, no. 3 (2016): 425–49; Benjamin Braun, Arie Krampf and Steffen Murau, 'Financial Globalization as Positive Integration: Monetary Technocrats and the Eurodollar Market in the 1970s', *Review of International Political Economy* 28, no. 4 (2021): 794–819; Ioan A. Balaban, 'Banking and Eurodollars in Italy in the 1950s', *Enterprise & Society* 24, no. 3 (2023): 759–83.

[11] Eric Monnet, 'The Diversity in National Monetary and Credit Policies in Western Europe under Bretton Woods', *Central Banks and the Nation State in Europe, XIXth–XXth Centuries* (Paris: Presses de Sciences Po, 2012).

[12] Vincent Della Sala, 'The Italian Model of Capitalism: On the Road between Globalization and Europeanization?', *Journal of European Public Policy* 11, no. 6 (2004): 1041–57; Kenneth Dyson and Kevin Featherstone, 'Italy and EMU as a

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external policy decisions but also tried to actively contribute to their formation. Some authors have shown, for example, how pro-European domestic elites have politically reshaped the 'external constraint' to steer domestic policy and favour the process of integration.[13] The Bank of Italy and its network of economists have been considered crucial actors in promoting financial innovation and political change.[14] Italy's experience in the process of European monetary integration thus raises one key puzzle. Despite Italy joining all the arrangements, from the so-called 'snake in the tunnel' (the first currency pegging mechanism agreed in 1972) to the European Monetary System and ultimately the EMU, such an outcome was 'neither obvious, nor preordained, since most of the time the structural context challenged the wisdom of Italian participation'.[15] This observation invites a re-evaluation of the role of ideas and 'agency' of domestic elites in explaining the path of Italy's evolving approach vis-à-vis monetary integration and financial liberalisation.

Italian economic thought has been studied extensively from different perspectives and periods, but central bankers' thinking on credit policy has too often been neglected.[16] Most of the literature on economic ideas and European integration has focused on the dominance of Anglo-Saxon and German ideas (neo-liberalism and ordo-liberalism), emphasising processes of top-down influence and adaptation in more 'peripheral' countries.[17] However, Italian economic ideas and networks can also have a 'boomerang effect', becoming prominent at the EU level.[18]

By analysing the discourses and research activities of central bankers during the 1970s, this article argues that the development of a domestic 'sense-making'[19] or 'policy learning' on credit controls by a group of key reform-oriented economists anticipated, and only subsequently fed into, the discussions on promoting European monetary integration. These economists acquired greater importance during a phase of crisis, widespread theoretical disorientation, and rife social conflict, leading them to became increasingly influential.[20] The central bank was an important 'epistemic hub' due to its autonomy and the unparalleled technical superiority of its research centre (*Servizio Studi*).[21] While the state became increasingly weak during the crisis of the 1970s due to unstable governments and political terrorism, the central bank constituted an 'island of stability and competence'.[22] The 'technostructure of

"Vincolo Esterno": Empowering the Technocrats, Transforming the State', *South European Society and Politics* 1, no. 2 (1996): 272–99.

[13] Giandomenico Piluso, 'Reshaping the External Constraint: Franco Modigliani, Tommaso Padoa-Schioppa and the EMS, 1977–1993', *History of Economic Thought and Policy* 2 (2020): 97–119.

[14] Lucia Quaglia, 'Civil Servants, Economic Policies and Economic Ideas: Lessons from Italy', *Governance* 18, no. 4 (2005): 545–66. Giandomenico Piluso, 'Deregulation, Regulatory Convergence or Escaping from Inefficiency? The Italian Financial System in the 1970s and 1980s', in Drach and Cassis, eds., *Financial Deregulation*, 138–61.

[15] Lucia Quaglia, 'Italy's Policy towards European Monetary Integration: Bringing Ideas Back In?', *Journal of European Public Policy* 11, no. 6 (2004): 2.

[16] Marcello De Cecco, 'Keynes and Italian Economics', in Peter A. Hall (ed.) *The Political Power of Economic Ideas: Keynesianism across Nations* (Princeton, NJ: Princeton University Press, 1989): 195–229; Piero Bini, 'The Italian Economists and the Crisis of the Nineteen-Seventies: The Rise and Fall of the Conflict Paradigm', *History of Economic Thought and Policy: 1, 2013* (2013): 73–101; Fabio Masini, *SMEmorie della lira: gli economisti italiani e l'adesione al sistema monetario europeo* (Milan: FrancoAngeli, 2004).

[17] Roberto Ventresca, 'Neoliberal Thinkers and European Integration in the 1980s and the Early 1990s', *Contemporary European History* 31, no. 1 (2022): 31–47. Cornel Ban, *Ruling Ideas: How Global Neoliberalism Goes Local* (Oxford University Press, 2016).

[18] Oddný Helgadóttir, 'The Bocconi Boys Go to Brussels: Italian Economic Ideas, Professional Networks and European Austerity', *Journal of European Public Policy* 23, no. 3 (2016): 392–409.

[19] Leon Wansleben, 'Growth Models and Central Banking: Dominant Coalitions, Organizational Sense-Making, and Conservative Policy Innovations at the Bundesbank and Fed', *Review of International Political Economy* 31, no. 1 (2024): 124–48.

[20] Franco Ferraresi and Giuseppe Ferrari, 'Italy: Economists in a Weak Political System', *History of Political Economy* 13, no. 3 (1981): 629–55.

[21] Simone Polillo, 'Crisis, Reputation, and the Politics of Expertise: Fictional Performativity at the Bank of Italy', *Review of Social Economy* 81, no. 3 (2023): 342–62; Antonella Rancan, 'Econometric Modelling in Italy: From Economic Planning to Academic Research', *History of Economic Thought and Policy: 1, 2021* (2021): 63–82.

[22] Alberto Predieri, *Il potere della banca centrale: isola o modello?* (Firenze: Passigli, 1996).

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experts'[23] within and beyond the central bank research department included figures such as Paolo Baffi, Beniamino Andreatta, Mario Monti and Tommaso Padoa-Schioppa (TPS), influential and 'hybrid' economists between academia and policy-making who aimed to radically reform the Italian political and financial system.

Among these economists, TPS has been considered in particular a leading figure in the process of European economic and political integration and one of the great 'architects of the euro'.[24] Although his most important contributions to European monetary integration occurred in the late 1980s and 1990s,[25] his work at the national level during the 1970s is equally important, though unfortunately less studied. At that time, his main interests were more domestic and focused on the modernisation of national monetary policy.[26] Since the Werner Report (1970), the harmonisation of national central bank policies and instruments has been considered a crucial step to move forward with the process of monetary integration. During his time at the Bank of Italy, TPS played a key role in leading this modernisation process. However, his role in the intellectual overhaul of Italy's credit system, which was later a prerequisite for joining the EMU in the 1990s, has not been sufficiently emphasised. The same applies to Mario Monti, a Bocconi-trained economist with close ties to the central bank. The article examines how TPS, Monti and other key central bankers and economists contributed to the 'rise and fall' of credit controls in Italy and, in turn, to the transformation of the central bank in line with their growing expectations of the monetary integration process.

The article is structured as follows. After this introduction, a section entitled 'The Multiple Meanings and History of Credit Controls' clarifies the multiple meanings and objectives of credit controls and their difference from 'market-based' instruments. By providing a brief history of these tools, it emphasises the 'agency' of central bankers and their economic ideas as an important variable to look at when analysing the end of credit policy regimes. In the next section, 'The Rise and Fall of Credit Controls in Italy, 1973–1983', the article applies these insights to reconstruct the rise and fall of credit controls in the case of Italy during the 1970s. The section draws on archival documents from the Historical Archives of the Bank of Italy (ASBI) and the Historical Archive of the EU (AHEU), as well as a wide array of economists' research papers and secondary sources. In the final section, I will draw some conclusions.

The Multiple Meanings and History of Credit Controls

The term 'credit policy' has been used in different ways over time and space, revealing a conceptual and functional ambiguity.[27] In its broad sense, it can be defined as 'the set of interventions supported or devised by a central bank (or the government) to promote the development of credit and to influence its allocation, thus replacing free market mechanisms that are deemed insufficient, unfair or flawed'.[28] A credit policy regime thus entails a variety of different tools and regulations,[29] including fiscal and monetary measures, that aim to control the composition and direction of credit to achieve certain social goals. In fact, any kind of credit incentive can be seen as a manifestation of credit policy.[30]

[23] Alfredo Gigliobianco, *Via Nazionale: Banca d'Italia e classe dirigente: cento anni di storia* (Donzelli, 2006).

[24] Fabio Masini, 'Tommaso Padoa-Schioppa: EMU as the Anchor Stone for Building a Federal Europe', in Kenneth Dyson and Ivo Maes (eds) *Architects of the Euro: Intellectuals in the Making of European Monetary Union* (Oxford: Oxford University Press, 2017), 193–211.

[25] As co-rapporteur of the Delors' committee (1988–9) and founding member of the Executive Board of the European Central Bank (1998–2005).

[26] F. Masini, 'Tommaso Padoa-Schioppa: EMU as the Anchor Stone for Building a Federal Europe', in Dyson and Maes (eds) *Architects of the Euro*, 195.

[27] Claire Andrieu, 'A la recherche de la politique du crédit, 1946–1973', *Revue historique* 271, no. Fasc. 2 (550) (1984): 377–417.

[28] Monnet, *Controlling Credit*, 3.

[29] For a summary of credit policy tools cf. Bezemer et al. (2021: 10).

[30] Development banks also perform credit policy functions. Cf. Daniel Mertens and Matthias Thiemann, 'Building a Hidden Investment State? The European Investment Bank, National Development Banks and European Economic Governance', *Journal of European Public Policy* 26, no. 1 (2019): 23–43.

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In the past, credit policy was sometimes used as a synonym for 'monetary policy', although the term is now generally used in a much broader sense to include other types of policies designed to achieve objectives beyond the control of money and inflation, such as industrial and development policies.[31] This can have clear implications for the degree of central bank autonomy, as the central bank becomes even more explicitly involved in allocative decisions. In short, a credit policy regime contributes to blurring the boundaries between the central bank and the government, as well as between the state and the economy.[32] In recent times, its historical significance has been 'rediscovered', following a trend towards expanding state interventions and central bank mandates aiming at supporting key sectors, ensuring financial stability and facilitating the climate transition.[33]

From the end of the Second World War until the early 1980s, during the 'golden age' of Western capitalism, many economies experienced a high degree of interventionism in credit allocation.[34] Developing countries, but also many advanced economies, introduced various forms of credit controls and 'selective' credit policies. Governments adopted these measures to support priority sectors (such as exports), to promote industrial development and to minimise the consequences of inflation and balance of payments difficulties.[35] The terms 'credit controls', 'direct quantitative controls' or 'selective credit controls' were widely used as synonyms for credit policy.[36] Credit controls are not to be confused with capital controls, even though they both belong to the credit policy regime.[37] 'Selective' credit controls aim specifically at influencing the distribution of bank lending so as to achieve a different distribution than if banks were free to act according to their own criteria, with the aim of encouraging or discouraging certain categories of investment and consumption. In short, under a credit control regime, there is a close relationship between the monetary authorities and financial intermediaries.

During the 1970s, many central banks emphasised 'credit' rather than 'money' as the main transmission mechanism of monetary policy.[38] Economists generally considered the classical indirect instruments, such as the interest rate and open market operations, to be ineffective in influencing real variables without jeopardising economic growth. In particular, the discount rate manoeuvre proved ineffective in transmitting restrictive impulses to a highly segmented financial system and often had counterproductive effects. The control of credit flows by central banks thus adjusted and exploited the characteristics of domestic 'bank-based' financial systems, in which the financing of firms mostly rely on bank credit. A credit restriction could therefore take place without necessarily raising interest rates. Monetary policy was mostly conceived as transmitted by 'quantities' rather than 'prices'.[39]

Credit controls have varied considerably from one country to another, mainly because of the diversity of the financial systems in which they have been implemented.[40] Italy is a case where monetary

[31] Gerald Epstein, 'Developmental Central Banking: Winning the Future by Updating a Page from the Past', in Gerald Epstein, *The Political Economy of Central Banking* (Cheltenham: Edward Elgar, 2019), 426–40.

[32] Nathan Coombs and Matthias Thiemann, 'Recentering Central Banks: Theorizing State-Economy Boundaries as Central Bank Effects', *Economy and Society* 51, no. 4 (2022): 535–58.

[33] Monnet and van t Klooster, 'Using Green Credit Policy'.

[34] Marglin and Schor, eds., *The Golden Age of Capitalism.*

[35] I.G. Patel, 'Selective Credit Controls in Underdeveloped Economies', in Warren L. Coats, Jr. and Deena R. Khatkhate, eds., *Money and Monetary Policy in Less Developed Countries* (Oxford: Pergamon, 1980), 561–69; Donald R. Hodgman, 'Credit Controls in Western Europe: An Evaluative Review', *The Federal Reserve Bank of Boston, Credit Allocation Techniques and Monetary Policy* (1973): 137–61.

[36] Such policies took on different names in different countries, such as '*encadrement du credit*' in France and '*madoguchi shido*' in Japan. In this article, I will mainly use the term 'credit controls' for the Italian case.

[37] Capital controls played a role in making credit controls effective. Monnet, *Controlling Credit*, 139.

[38] On the debate between the 'money view' and the 'credit view' cf. Christina D. Romer, and David H. Romer, 'Credit Channel or Credit Actions? An Interpretation of the Post-War Transmission Mechanism', NBER Working Papers 4485, National Bureau of Economic Research, Inc. (1993).

[39] Monnet, *Controlling Credit.*

[40] John Zysman, *Governments, Markets, and Growth: Financial Systems and the Politics of Industrial Change* (Ithaca, NY: Cornell University Press, 1983).

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policy has historically been 'credit-oriented', and where the central bank has traditionally played a key role in regulating the credit system.[41] This was also made clear by Franco Modigliani when he observed that the Bank of Italy had an 'investment-maximising' approach to monetary policy, as was evident during Carli's governorship.[42] The role in credit policy was linked to the peculiarities of Italian capitalism, which suffered from a chronic shortage of risk capital and underdeveloped financial markets, in particular the absence of a modern and efficient money market. Italy, together with France and Belgium,[43] has historically shown a constant concern for the management of credit and its allocation, before shifting, as in other cases, to a more 'financialised' and less interventionist version of monetary policy.

During the 1970s, credit policy regimes in Europe began to lose legitimacy and were gradually dismantled. Economists and central bankers began to debate more critically the effectiveness of credit controls. They increasingly saw these controls as inherently distorting the efficient allocation of resources and as strictly 'emergency' instruments with detrimental side effects for an increasingly open and internationalised financial system.[44] An 'aggregative'[45] and indirect approach to monetary policy gradually regained its centrality and central banks increasingly aimed to be 'neutral' with respect to the allocation of credit in the market.[46] However, the 'chronology' of the end of this financially regulated economy, centred on credit intermediation, was not linear.

In Italy, the authorities first introduced direct credit controls in June–July 1973, just a few months before the first 'oil shock', and gradually phased them out in the early 1980s.[47] The controls were active under three different central bank governors: Carli, Baffi and Ciampi. Their introduction, revision and demise coincided with the 'peak' of the crisis of Italian capitalism during the 1970s and important steps of European integration, such as joining the European Monetary System (EMS). Central bankers and economists played a leading role in shaping the history of credit controls. As the new context of inflation and social conflict in the 1970s increasingly demanded new solutions for the conduct of monetary and financial policy, they had the chance to show their influence and expertise.[48] Many economists became involved in research and analysis aimed at re-thinking the structures and mechanisms of the Italian financial system and the transmission channel of monetary policy. This 'learning process', characterised by moments of acceleration and moments of stasis, provided the 'template' for the slow and gradual transformation of the Italian financial system that continued during the 1980s and 1990s.

The Rise and Fall of Credit Controls in Italy, 1973–1983

In the post-war period, Italy was among the most interventionist countries in terms of credit policy.[49] Historically, the Italian financial system was characterised by underdeveloped capital markets and a

[41] 'The heart of the Italian system of control over lending and investment is the central bank.' Cf. Andrew Shonfield, *Modern Capitalism: The Changing Balance of Public & Private Power* (Oxford: Oxford University Press, 1965), 180.

[42] Guido M. Rey and Paolo Peluffo, *Dialogo tra un professore e la Banca d'Italia* (Firenze: Vallecchi, 1995).

[43] Jens van't Klooster, 'The Case for a European Credit Council: Historical and Constitutional Fine-Tuning', *Accounting, Economics, and Law: A Convivium* (2023); F. Petrini, 'Stabilization through Integration: The European Rescue of Italian Capitalism', *European Review of History/Revue Européenne d'Histoire* 26, no. 4 (2019): 573–99.

[44] Edward Kane, 'Good Intentions and Unintended Evil: The Case against Selective Credit Allocation', *Journal of Money, Credit and Banking* 9, no. 1 (1977): 55–69; Marvin Goodfriend and Robert G. King, 'Financial Deregulation, Monetary Policy, and Central Banking', *Federal Reserve Bank of Richmond Working Paper* 88-1 (1988).

[45] Cf. Isabella Weber, Jesus Lara Jauregui, Lucas Teixeira, and Luiza Nassif Pires, 'Inflation in Times of Overlapping Emergencies: Systemically Significant Prices from an Input–Output Perspective', *Industrial and Corporate Change* 33, no. 2 (2024): 297–341.

[46] Jens Van't Klooster and Clément Fontan, 'The Myth of Market Neutrality: A Comparative Study of the European Central Bank's and the Swiss National Bank's Corporate Security Purchases', *New Political Economy* 25, no. 6 (2020): 865–79.

[47] Before 1973, credit ceilings had been introduced in France, the United Kingdom, Belgium, Spain, Switzerland, Japan and the Netherlands and had not been used in the United States, Canada, Germany and Italy.

[48] Ferraresi and Ferrari, *Economists in a Weak Political System*.

[49] Mauro Rota, 'Credit and Growth: Reconsidering Italian Industrial Policy during the Golden Age', *European Review of Economic History* 17, no. 4 (2013): 431–51.

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high degree of banking intermediation. Consequently, the state effectively assumed the role of both entrepreneur and banker, stepping in to address the chronic shortage of risk capital.[50] Banca d'Italia emerged as the central institution in this framework, exerting significant control over lending and investment. Since the beginning of post-war reconstruction, the central bank has considered it as its responsibility to inject liquidity into the system, ensuring the continuity of growth and industrialisation.[51] Although credit policy was legally overseen by an Inter-ministerial Committee for Credit and Savings (*Comitato Interministeriale per il Credito e il Risparmio*; CICR), created by law in 1947, the central bank held *de facto* operational authority due to the extensive powers granted by the 1936 Banking Law.[52]

The central bank was fully integrated into a credit policy regime, in which the interest rate was not the main instrument and a direct relationship with the banking system was considered key to the transmission of monetary policy. However, before the first 'oil shock' in 1973, the control of credit flows was not through the imposition of direct controls, but through the traditional manoeuvring of the monetary base.[53] The absence of a modern money market prevented the central bank from pursuing an interest-rate based policy and the banking system from avoiding the effects of a monetary manoeuvre due to the impossibility of liquidating securities. Since the mid-1960s, the Bank of Italy has pursued a policy of stabilising long-term interest rates by facilitating the placement of bonds with banks and savers, acting as a residual buyer.[54] This helped to strengthen the degree of banking intermediation. Before 1973, there were examples of credit policy instruments, such as the central bank's power to authorise the issue of securities and the system of subsidised loans, but they were mostly indirect.[55]

Although the boundaries between monetary and credit policy were blurred, the Bank of Italy enjoyed a very high degree of autonomy and influence in the decision-making process, due to its good reputation and technical expertise.[56] For example, the central bank was interested in economic planning, but it was strongly opposed to the politicisation of credit policy as pursued by the centre-left coalition government, which it perceived as a threat to its autonomy and powers in the financial sector.[57] In order to increase the bank's technical and planning capacity and to defend its autonomy, Guido Carli invested heavily in economic research and staff training. This process also led to the formulation of the Bank of Italy's first econometric model under the supervision of Franco Modigliani.[58] From the 1960s onwards, many of the bank's young economists, including TPS, Mario Draghi, Ezio Tarantelli and Antonio Fazio, underwent rigorous training in the United States, particularly at the Massachusetts Institute of Technology (MIT). They returned in the 1970s to take up important roles in central banking, academia and public institutions.

[50] Giuseppe Conti and Olivier Feiertag, 'Due banche centrali e due mercantilismi monetari per regolare il sistema finanziario (1880–1980)', in *Credito e nazione in Francia e in Italia (XIX–XX secolo)* (Vol. 1) (Pisa: Pisa University Press, 2009), 25–68.

[51] Giuseppe Mastromatteo and Lorenzo Esposito, 'Il ruolo della Banca d'Italia dalla ricostruzione post-bellica alla fine degli anni Settanta: una nota', *Moneta e Credito* 76, no. 301 (2023): 77–93.

[52] Mattia Lupi, 'A European Credit Council? Lessons from the History of Italian Central Banking after World War II', *Accounting, Economics, and Law: A Convivium* (2022).

[53] Bank of Italy, Annual Report for 1968, 364–65: Cf. Giancarlo Bertocco, 'Il governo della moneta e del credito in Italia. Un'analisi del meccanismo di trasmissione della politica monetaria nel periodo 1960–95', *Politica economica* 13, no. 3 (1997): 309–44.

[54] Banca d'Italia, Considerazioni Finali, 1969, 399; Battilossi 1998, 414.

[55] T. Padoa-Schioppa, 'Il controllo qualitativo del credito: considerazioni sulla recente esperienza italiana', *Moneta e credito* 27, no. 108 (1974).

[56] Giangiacomo Nardozzi, 'A Central Bank between the Government and the Credit System: The Bank of Italy after World War II', *Central Banks' Independence in Historical Perspective* (1988): 161–96.

[57] Paolo Peluffo and Federico Carli, 'Introduzione: "Il cavallo non beve." Dibattiti negli anni Sessanta su politica monetaria e programmazione economica', *Guido Carli, Scritti scelti* (2000), v–liv.

[58] Giandomenico Piluso, 'Blurring Boundaries: The Economists at the Bank of Italy and the Making of the European Monetary System, 1975–1990', *Cahiers d'Economie Politique/Political Economy Papers* 81 (2022): 231–61.

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In the early 1970s, President Nixon's decision to abandon gold parity ushered in a new phase characterised by international monetary disequilibrium and the emergence of a system of flexible exchange rates. The countries of the EEC initially tried to respond by trying to keep their currencies pegged through the institution of the 'snake'.[59] As early as 1970, the Werner Plan aimed to lay the foundations for the creation of a monetary union, but this was never realised. In the plan, the need to promote the harmonisation of monetary policies at the national level was recognised, but there was no explicit plan to reform credit policies.[60] The end of the Bretton Woods system of fixed exchange rates put a strain on European economies. As early as 1969, the Bank of Italy began to anticipate the need for greater exchange rate flexibility.[61] In February 1973, Italy finally abandoned the snake, starting the first process of devaluation of the lira since the dramatic one of 1947.[62]

The international monetary turmoil coincided in Italy with the start of an unprecedented period of trade union struggle, inaugurated by the so-called 'hot autumn' of 1969.[63] The new international context of rising interest rates and rising domestic labour costs led to a severe balance of payments crisis. The Bank of Italy introduced a policy of credit restriction, including an increase in the discount rate and an obligation on banks to reduce their net foreign position. The discount rate was raised to 5.5 per cent for the first time since 1958, when it had been stuck at 3.5 per cent[64] to bring it more in line with international levels and to prevent capital flight. However, unlike the previous credit squeeze of 1963–4, this time the restriction was not as effective.[65] The traditional monetary base manoeuvre was proving ineffective in transmitting restrictive impulses to the system without jeopardising support for long-term investment.

From June to July 1973, to cope with a situation characterised by growing public deficits, difficulties in controlling the monetary base, soaring inflation and a large balance of payments deficits, the Bank of Italy introduced for the first time 'selective' controls on credit, such as the portfolio constraint[66] (*vincolo di portafoglio*) and the ceiling on bank lending[67] (*massimale sugli impieghi*). In this way the central bank extended its 'dirigiste' powers over the financial system.[68] To reduce the liquidity of the system, to raise interest rates, but at the same time not to deprive the public sector and long-term investment of funding, the bank thus moved from the indirect regulation of the monetary base to an increased emphasis on the volume and allocation of credit. Policy-makers used these instruments with the dual objective of fighting inflation and external imbalances, while influencing the direction of credit, mainly to the public sector.[69] This was done in the belief that the system of restrictions on banks' portfolios would have made it possible to achieve 'more objectives than the monetary base manoeuvre could achieve on its own'.[70]

59 Mourlon-Druol, *A Europe Made of Money*.
60 Monnet, *Controlling Credit*, 275.
61 Daniele Caviglia, *La diplomazia della lira: l'Italia e la crisi del sistema di Bretton Woods (1958–1973)* (Milan: FrancoAngeli, 2013).
62 The Italian lira devalued in 1947, but not so dramatically as British sterling. Cf. Alan Milward, *The Reconstruction of Western Europe* (London: Routledge, 1984).
63 Gerd-Rainer Horn, *The Spirit of '68: Rebellion in Western Europe and North America, 1956–1976* (Oxford: Oxford University Press, 2007). A. Gigliobianco and M. Salvati, *Il maggio francese e l'autunno caldo italiano: la risposta di due borghesie* (1980).
64 Ignazio Visco, *Inflazione e politica monetaria* (Roma-Bari: Laterza, 2023), 16.
65 Antimo Verde, 'La crisi della lira del 1963–64, una crisi senza svalutazione: perché?', *Studi e note di economia* 1 (2002): 75–97.
66 Introduced on 18 June 1973 by the CICR, it required banks to increase their holdings of bonds/fixed-income securities net of investments already made for compulsory reserve purposes, by no less than 6% of the previous year's deposits. An instrument characterised by a primary 'prudential' purpose took on an allocative credit policy function. It was renewed several times, relaxed in 1979 and finally abolished in 1986.
67 Introduced on 26 July 1973 by the Bank of Italy, thanks to its power to determine the maximum limits of the loans to be granted. The measure excluded loans to operators with exposures of less than 500 million, unless they were commercial and financial companies, as the measure was intended to protect them in a restrictive phase. It was abolished in 1983.
68 Tommaso Padoa-Schioppa, 'Selective Credit Policy: Italy's Recent Experience', *PSL Quarterly Review* 28, no. 112 (1975).
69 Cf. Monnet and van t Klooster, 'Using Green Credit Policy'.
70 Banca d'Italia, Relazione annuale sul 1977, 396; see also Banca d'Italia, Relazione sul 1974, 427.

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What contributed to this change in the monetary policy technique in 1973? The interplay between the effects of the new social and economic environment and the attempts by the bank's economists to find new solutions was a decisive factor. The destabilising pressures of labour rigidities and international turmoil had made the use of traditional monetary policy ineffective, slow and imprecise in transmitting impulses to the system. The monetary instrument was clearly inadequate because of its 'insufficiently selective nature and the difficulty of controlling the volume of credit in the short term'. A strengthening of the credit channel therefore seemed necessary to better control destabilising pressures.

One of the key experts behind the study of such monetary techniques was TPS. In 1970, TPS was recruited by the Study Service (*Servizio Studi*), after studying at MIT, where he began a close collaboration with Franco Modigliani. In 1971, TPS went on a mission to Japan to study the Japanese growth model. The Japanese experience was of great interest because of the similarities with Italy, such as the 'dual' economy and the 'bank-based' financial system. In a final report, TPS emphasised the importance of credit control for balance of payments adjustments and the preference for the use of direct quantitative controls over interest rate policy. The reasons for relying on direct controls were that 'the economy was heavily dependent on banks and banks on the central bank […] the authorities did not want to raise interest rates in order to promote growth […] a rapid instrument was needed because of the low level of international reserves'.[71] The role played by banks in Japan's economic growth as a major channel of money supply was of 'outstanding significance' because, as in Italy, capital markets were underdeveloped. In fact, the Bank of Japan did not regulate its credit expansion to the banking system through the price mechanism.

However, in the same report, TPS had already mentioned how the role of banks in facilitating economic growth in Japan was changing due to the rapid growth of 'quasi-banks' such as mutual loans, savings banks, and credit associations. This, according to TPS, was reducing the effect of credit restrictions and called for a 're-examination of monetary policy in the face of new developments such as the issuance of long-term government bonds and the persistent payment surpluses'. The role of banks was shifting from the promotion of growth to the achievement of economic stability, and indications were that soon monetary policy would have shifted its emphasis from direct quantitative controls to indirect controls, giving more importance to the adjustment function of interest rates.[72]

In the same year, TPS and Franco Cotula, another young MIT-trained central bank economist, published a paper on direct credit controls.[73] In the paper, the authors proposed to study the potential impact and application of credit ceilings on bank lending in Italy, asking whether they could be conceived as a substitute or an additional tool for monetary base management. Given the close relationship between the banks and the central bank, they argued that a monetary restriction could be more easily implemented without raising the official discount rate. However, they also concluded that the credit ceilings should have been considered only as a 'temporary instrument' because of their distortionary effects on financial intermediation and inefficiency in the allocation of resources.[74] Another economist, Rainer Masera, shared the same conclusions.[75] In June–July 1973, the Bank of Italy introduced the portfolio constraint and the credit ceiling.

In Europe, the revival of selective credit policies coincided with the rise of monetary targeting. Credit ceilings were 'quantitative' objectives that could be coupled with money targeting while being consistent with the traditional purposes of selective credit policy. In fact, as noted by TPS, direct controls could also be used 'in conjunction with the instrument of monetary base control to speed up the effects of a restrictive policy or to increase its effectiveness and precision in cases where banks may expand credit to an extent not desired by the central bank'. Moreover, they could also be imposed 'as a

[71] HAEU, TPS n. 694.
[72] Ibid.
[73] Franco Cotula and Tommaso Padoa-Schioppa, 'Direct Credit Controls as a Monetary Policy Tool', *PSL Quarterly Review* 24, no. 98 (1971).
[74] Ibid.
[75] Rainer Masera, 'Controllo quantitativo del credito: alcune considerazioni generali', *Moneta e credito* 24, no. 96.

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matter of necessity when international commitments make it necessary to set a strict quantitative limit on total credit expansion'.[76] This was in particular the case of Italy in the context of the *stand-by* agreement with the IMF starting from 1974. During the negotiations with IMF officials, the Bank of Italy committed itself to adopt a new intermediate target, Total Internal Credit (*Credito Totale Interno*; CTI).

The idea behind CTI was to control the amount and direction of financial flows to mitigate the balance of payments constraint and preserve the level of economic activity, thus combining credit selectivity with monetary targeting.[77] The use of CTI was an occasion to boost coordination between fiscal and monetary policies by forcing consistency between financing the public deficit and financing the private sector of the economy.[78] The adoption of CTI did not result from an IMF imposition but from a choice of the central bank itself.[79] This strategy represented a difference from the models traditionally used by the IMF.[80] In the model adopted by the Bank of Italy, the role of 'money' was downgraded, and more emphasis was placed on the demand for total financial assets, which was considered more appropriate in the context of the Italian financial system. This soon opened an internal debate among economists on the degree of monetary tightening implied by this commitment.[81] With the introduction of CTI, monetary policy, while remaining within the formal framework of selectivity, took on the character of a more quantitative control *tout court*. Selectivity and attempts to keep the weaker sectors at bay actually increased credit rationing. The measures launched in June–July 1973 did not lead to a real planning of credit flows. In this respect, the central bank preserved its rather deep-rooted preference for neutrality towards the credit system.[82]

The year 1975 marked a significant moment in the history of credit control. Paolo Baffi, an economist who had previously worked in the Study Service, replaced Carli as governor of the central bank and began a process of delegitimisation. However, his appointment coincided with the most severe crisis of the lira since the post-war period, which occurred in January 1976.[83] The Italian economy faced several challenges that imposed a renewal of credit controls while attempting to mitigate the undesirable effects in terms of allocative efficiency. A major consequence of the credit controls was the so-called double intermediation (*doppia intermediazione*'),[84] which led to the de-responsabilisation of bankers and even a dramatic deterioration in the financial structure of manufacturing firms.[85] Moreover, banks increasingly circumvented both the portfolio constraint and the credit ceiling, which had begun partly to lose their original purpose. The portfolio constraint, which was initially applied uniformly, had different effects on different banks. Some banks increased deposits in order to circumvent the constraint. Thus, the 1975 renewal allowed for an increase in

[76] Padoa-Schioppa, 'Selective Credit Policy', 40.

[77] Cf. Salvatore Rossi, *La politica economica italiana dal 1968 a oggi* (Roma-Bari: Laterza, 2007), 20.

[78] C. Caranza and A. Fazio, 'Methods of Monetary Control in Italy', in D. Hodgman (ed.) *The Political Economy of Monetary Policy: National and International Aspects* (Federal Reserve Bank of Boston, Conference Series) 26: 65–88, (1983).

[79] Banca d'Italia, Considerazioni Finali on the year 1974, 41.

[80] The IMF model was based on the Domestic Credit Expansion (DCE). CTI differed from DCE mainly in the inclusion of securities issued by the public sector purchased by the public, loans to the public by special credit institutions and bonds. Cf. Jacques Polak and Victor Argy, 'Credit Policy and the Balance of Payments', *The Monetary Approach to the Balance of Payments* (Washington, DC: International Monetary Fund, 1977).

[81] Giacomo Vaciago, 'Credito totale interno e offerta di moneta', *Rivista internazionale di scienze sociali* 46, no. Fasc. 5/6 (1975): 563–95; Franco Bruni, 'Considerazioni sul calcolo del credito totale interno', *Giornale degli Economisti e Annali di economia* (1976): 43–66.

[82] J.R. Hillman, 'The Mutual Influence of Italian Domestic Politics and the International Monetary Fund', in *The Fletcher Forum* (The Fletcher School of Law and Diplomacy, 1980, Jan.), 1–22.

[83] Antimo Verde, 'La crisi della lira del 1976. Cause, conseguenze e possibili schemi interpretativi', *Studi e note di economia* 2 (2003): 143–83.

[84] 'Double intermediation' refers to the practice whereby a financial intermediary, in addition to lending directly to end-users, finances another intermediary who in turn lends to end-users.

[85] Piluso, 'Deregulation, Regulatory Convergence or Escaping from Inefficiency? The Italian Financial System in the 1970s and 1980s.'

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fixed-income securities of up to 40 per cent of deposit formation. The ceiling lost its 'selective' capacity and directly limited the growth of bank lending. In 1975, the renewal exempted foreign currency lending to reduce the balance of payments deficit.[86]

Meanwhile, the central bank had already begun a process of strengthening market tools. Central bank economists began a 'sense-making' process to understand the nature and effects of the Italian credit system. This ushered in a period of problematic 'co-existence' between credit controls and market tools. The process of strengthening market mechanisms had already begun in the last months of Carli's governorship. During the 1970s, growing public sector deficits emerged as one of the main constraints on the conduct of monetary policy. The central bank actively sought alternative sources of financing for the treasury to avoid inflationary monetary financing. In February 1975, it introduced a new compulsory reserve requirement to establish a more predictable and direct link between the creation of the monetary base and the development of credit and deposits. In March, the reform of the auction mechanism for treasury bills (BOTs) established a 'marriage' between the treasury and the central bank, as the Bank of Italy acquired the right (not the obligation) to buy unsold government bonds. Prior to 1975, there was no real secondary market for government bonds in Italy. In 1976, the new legislation provided that all treasury bills would be issued through market auctions.[87]

The Bank of Italy thus became the main architect of financial innovation, laying the foundations for the creation and development of a modern money market in Italy, the first step towards the abolition of credit controls.[88] In Italy, the abolition of credit controls was closely linked to the issue of public finance and the relationship between the central bank and the treasury. Indeed, the need to regain control over the monetary base and monetary financing increasingly justified their delegitimisation. From this perspective, the 'financialisation' of government bonds can be seen as the result of the economic chaos of the 1970s and the urgent need to create new channels of financing for the treasury.[89] Carli was thus both the main interpreter of the administrative approach to credit and the one who began to lay the foundations for its demise.[90]

In addition to these first reforms, Carli, in agreement with Baffi, helped to promote economic research on the Italian credit system. In 1975–6, he continued to head a joint Bank of Italy-Bocconi University research group inspired by his conviction of the need to reform the outdated 1936 banking law.[91] Mario Monti and TPS co-ordinated the group at the Einaudi Body for Monetary, Banking and Financial Studies (*Ente per gli studi monetari, bancari e finanziari Einaudi*). In a letter to Governor Paolo Baffi (23 January 1976), TPS argued that 'economists could no longer claim that the origins of the crisis were non-economic and that suggesting political measures would be beyond their competence. Instead, they should have taken responsibility and proposed solutions based on economic considerations.'[92] This study was inspired by the conviction that the Italian economy needed 'deeper corrections than those that can be achieved through cyclical manoeuvres'. Carli later noted how the 'Pandolfi Plan' of 1978, the adjustment strategy aimed at solving Italy's macroeconomic and competitiveness problems and ensuring Italy's participation in the European integration process, accepted the approach outlined in this research.[93] The document was largely conceived by TPS and supported by Director General Carlo Azeglio Ciampi.[94]

[86] David Croff, Franco Passacantando, Franco Cotula and Pietro de'Stefani, 'Il controllo diretto del credito', *La politica monetaria in Italia, istituti e strumenti* (Bologna: Il Mulino, 1979).

[87] ASBI, Carte Baffi, Monte Oppio, n. 80, fasc. 4: Tommaso Padoa-Schioppa, Tecniche di Emissione dei Buoni Ordinari del Tesoro, 1975.

[88] Maria Teresa Salvemini, 'Osservazioni sul mercato dei Buoni del Tesoro Ordinari', *Moneta e Credito* 28, no. 111 (1975).

[89] Alexander Nützenadel, 'The Political Economy of Debt Crisis: State, Banks and the Financialization of Public Debt in Italy since the 1970s', *A World of Public Debts: A Political History* (2020): 405–25.

[90] Croff, Passacantando, Cotula and de'Stefani, 'Il controllo diretto del credito', 104.

[91] Seven of the nine Member States were in the process of changing their banking laws. Italy was the exception (along with Luxembourg).

[92] ASBI, Carte Baffi, Monte Oppio, b. 24, fasc. 1.

[93] Guido Carli, *La Struttura del sistema creditizio italiano: elementi per un riesame, Introduzione* (Bologna: Il Mulino, 1978).

[94] Piluso, 'Reshaping the External Constraint'.

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Paolo Baffi played an active and important role in supporting this review process. Within the central bank, economists were increasingly concerned that credit restrictions were inefficient and significantly distorted the allocation of resources. Baffi warned against the loss of autonomy in assessing debtors' creditworthiness due to 'double intermediation'.[95] He drew inspiration from the bank's repertoire of monetary policy ideas. In 1976, Baffi pointed out that the issue of credit controls had already been raised by Carli in 1963. In fact, in 1963 Carli stated that selective credit criteria should be considered as 'emergency instruments and not as a permanent component of credit policy'.[96] In 1975, Baffi rediscovered this argument, noting how 'the ideas put forward in recent years had not invalidate its logic'. On the contrary, it was 'comforting to note that these arguments have been independently taken up by others. […] The recourse to selective measures of short-term credit, made in the 1973–4 emergency, revealed even greater difficulties of application than those envisaged back then.'[97] Carli, however, had been the main architect of the use of administrative measures, a mode of intervention from which Baffi clearly wanted to deviate.[98] In fact, he found the central bank's action in interfering with the autonomy of the banking system and directing credit towards obligatory lines 'deeply unsatisfactory', both in terms of logic and effects. According to Baffi, the effects of credit controls tended to be unstable because of the ability of operators to circumvent them. Moreover, they increasingly conflicted with the intention of the monetary authorities to promote the development of an efficient money market.[99] In short, the bank's objectives of creating alternative funding channels for the treasury and regaining control over the monetary base increasingly clashed with the existence of credit controls. The coexistence of administrative controls and market instruments made monetary policy and efficient resource allocation increasingly ineffective.[100] It was thus necessary to allow a gradual return to less constraining modes of intervention.

From this point of view, the rejection of credit selectivity seems to be a constant in the Bank of Italy, reflecting a liberal economic philosophy since Einaudi. Carli had developed alternative ideas that led him to reconsider the value of fiscal measures, selectivity, and other concepts more in line with the advocates of economic planning. The Bank of Italy's attitude thus found a parallel in the distrust of selective controls among economists, who generally considered the allocation of resources by means of large flows operated by quantitative instruments, the apparently more neutral ones, to be preferable. Faced with the difficulty of managing an economic environment characterised by the combined operation of coercive and market instruments, the central bank decided to reform the system of constraints while it was still in force.[101]

Economists, bankers and party experts proposed reforms in line with a collective spirit of reform sparked by the 1976 crisis and clearly articulated in the 'Pandolfi Plan'. The central bank focused on credit as a key issue, aiming to restore the separation between short-term and medium- to long-term credit, while significantly reducing the state's intermediation activities. At the Study Service, TPS systematically analysed many of these proposals between 1977 and 1978.[102] The Bank of Italy suggested a potential revision of the credit control system, which could be implemented in June–July 1978, coinciding with the expiration of both the ceiling and the portfolio constraint. Mario Monti introduced one of the most notable of these proposals known as the 'planchers'. The proposal aimed to shift control from banks' assets to their liabilities and to introduce a system of progressive penalties for those with a

95 Leandro Conte, 'L'azione della Banca d'Italia 1948–1993', in *Storia d'Italia, Annali, La banca*, ed. Salvatore La Francesca (Torino: Einaudi, 2008).

96 Banca d'Italia, Considerazioni finali sul 1963.

97 Banca d'Italia, Considerazioni finali sul 1975, 38.

98 'While the multiplicity and variability of interventions may have satisfied Carli's inclination to test his genius, I believe he sometimes felt nostalgia for simpler approaches.' Banca d'Italia, Considerazioni sul 1975, 7.

99 Ibid., 34.

100 Ibid., 36.

101 Banca d'Italia, Considerazioni finali sul 1975, 38.

102 ASBI, Banca d'Italia, Dir. Padoa-Schioppa n.1.

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higher percentage of deposits.[103] Monti hypothesised that this approach would give banks greater flexibility in managing their assets and allow bankers to demonstrate their real skills, as some had called for. He considered this method to be more adaptable than credit ceilings and believed that it could lead to banking disintermediation.[104]

Starting from the end of 1978, Monti wrote several articles in the *Corriere della Sera*, denouncing the transformation of the state into a 'hidden banker'. Monti argued that the public sector was absorbing increasing shares of total domestic credit, which had a 'crowding-out' effects on firms. The allocation of credit by the state favoured the less successful initiatives, rendering the selective function of the market ineffective. The responsibility for the performance of credit intermediation was thus no longer with the central bank, but with the state. Monti observed how everything became 'confused and grey. Financial intermediation enters the state and in return, bureaucratisation enters the bank.'[105] Other economists outside the central bank begun to be persuaded by Monti's ideas and started to actively call for the abolition of credit controls. One of them noted: 'the abandonment of quantitative constraints require a great deal of courage, but the current internal and external situation seems propitious for this leap'.[106] However, despite the fact that delegitimisation of state intervention in the financial sector intensified, credit controls were renewed due to the uncertain macroeconomic environment, but with changes aimed at mitigating their discriminatory effects.[107] The central bankers' preferred mode slowly returned to indirect control of credit through the monetary base and market mechanisms, after a phase of 'coexistence' with direct instruments. As noted by TPS, only the consolidation of public finances and a slowdown in the inflationary process could have paved the way for a more complete liberalisation of bank credit.

The transition to a 'market-based' monetary policy regime was not linear. The ceiling on bank lending and the portfolio constraints imposed in June 1973 were renewed several times until the early 1980s, although their effects were gradually mitigated. The credit ceiling in particular, was maintained until June 1983.[108] Thus, at the turn of the 1980s, Italy's monetary policy regime was still based on both administrative and market instruments. In 1979, Carlo Azeglio Ciampi replaced Paolo Baffi as Governor of the Banca d'Italia. Ciampi was determined to continue the reforms initiated by his predecessor and had previously worked with his colleague and friend TPS.[109] Baffi had been forced to resign after a controversial political and legal attack. Ciampi, TPS and other members of the bank, including the head of the Study Service, Masera, had been actively pushing for Italy's entry into the EMS since 1978.[110] Their aim was to implement anti-inflationary policies, maintain exchange rate stability and anchor Italy's economic and political future to Europe.[111] At the domestic level, they aimed to establish a 'new monetary constitution' based on public finance discipline, wage restraint, and central bank independence.[112] This latter was formally achieved in agreement with

103 Examples of these constraints with a progressive nature can be found in the United Kingdom. On the so-called 'corset' cf. Duncan Needham, *UK Monetary Policy from Devaluation to Thatcher, 1967–82* (London: Springer, 2014); Charles Goodhart, 'Competition and Credit Control: Some Personal Relections', *Financial History Review* 22, no. 2 (2015): 760–79.

104 Cf. report written by Francesco Cingano, managing director, quoted in Piluso (2021, 152).

105 Mario Monti, *Il banchiere occulto*, Corriere della Sera, 2 Nov. 1978.

106 Giorgio Ragazzi, *Una politica monetaria coraggiosa*, Mondo Economico, 14 Oct. 1978 (own transl.).

107 Tommaso Padoa-Schioppa, Alternative formulations of the portfolio constraint (26 June 1978). ASBI, Banca d'Italia, Dir. Padoa-Schioppa n.1.

108 Franco Cotula and Salvatore Rossi, 'Il controllo amministrativo dei flussi finanziari in Italia', *La politica monetaria in Italia* (1989), 351–77.

109 Between 1979 and 1983, TPS closely collaborated with Jacques Delors at the European Commission, DGII. Cf. Carlo Azeglio Ciampi, 'In Ricordo Di Tommaso Padoa-Schioppa', *Moneta e credito* 64, no. 253 (2011): 3–8.

110 Francesco Petrini, '"La politica antiinflazionistica è la politica europeistica e viceversa." L'adesione italiana al sistema monetario europe', in *Integrazione europea e trasformazioni socio-economiche. Dagli anni Settanta a oggi*, eds. Lorenzo Mechi and Daniele Pasquinucci (Milan: FrancoAngeli, 2017), 53–68.

111 Piluso, 'Reshaping the External Constraint'.

112 Banca d'Italia, Considerazioni finali sul 1980, 38.

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Treasury Minister Beniamino Andreatta, an economist with close ties to the bank, through an institutional 'divorce' in 1981.[113]

In investigating the causes of the end of the credit policy regime, researchers have raised the question of whether the process of European monetary integration was indeed a crucial determinant of change. In many countries, the abandonment of credit controls coincided with the implementation of deflationary policies following entry into the EMS.[114] However, Italy initially stabilised inflation in the early 1980s with the controls still in place. The Werner Plan had failed to include credit controls despite calling for the harmonisation of national monetary policies. Similarly, the first and second European directives on banking legislation in 1973 and 1977 introduced significant innovations in prudential regulation and banking activities in the EEC but did not address credit controls.[115] In 1979, the EEC working group (Bastiaanse) published their second report on the harmonisation of monetary policy instruments. The report recommended a common scheme for analysing financial flows to enable better mutual information on the monetary policies of member countries. However, in the course of the negotiations, it emerged that it was impossible to converge on a single intermediate objective.[116] In 1978, entry into the EMS did not entail the abolition of credit controls, which on the contrary actually served the domestic economies to control financial flows during a delicate economic juncture.[117]

What could explain the abolition of credit controls in Italy if the EEC did not play a major role in this process? The abolition of credit controls in Italy is closely linked to public finance and the relationship between the central bank and the treasury. As early as 1975, the central bank began to discredit credit controls while expanding market instruments as a solution to limit the treasury's reliance on monetary financing. Moreover, central bank economists traditionally viewed credit controls as strictly emergency and temporary measures.[118] However, from 1973 onwards, the increasing lack of control over the monetary base in a context of high inflation forced the central bank to experiment with direct controls in order to achieve two objectives: to transmit restrictive impulses more quickly to the financial system and to guarantee an interest rate structure different from that of the market so as not to jeopardise long-term investments.

Direct controls were initially used to regain control of the monetary base and to selectively channel credit to priority sectors for countercyclical policy. Over time, however, the controls lost their effectiveness and their original 'selective' purpose, partly due to circumvention by banks. Meanwhile, economists embarked on a 'policy learning' process to assess the costs and effectiveness of credit controls, increasingly denouncing their negative effects in terms of 'allocative efficiency' and the autonomy of the banking sector. The period of coexistence between administrative and market instruments was seen as generating further contradictions, as the objective of developing a secondary market for government bonds conflicted with the existence of restrictions. These contradictions included the transformation of credit controls into instruments to facilitate the placement of public debt. In the late 1970s, Monti played a key role in the delegitimisation process based on this argument. From this point of view, 1981 was a crucial year. In an effort to curb the treasury's persistent budget deficits,

[113] Gerald Epstein and Juliet Schor, *The Divorce of the Banca d'Italia and the Italian Treasury: A Case Study of Central Bank Independence* (Cambridge, MA: Harvard Institute of Economic Research, 1986); Giuliano Garavini and Francesco Petrini, 'Il "divorzio" tra Tesoro e Banca d'Italia: il vincolo interno e le origini del problema del debito pubblico italiano', in *Al governo del cambiamento. L'Italia di Craxi tra rinnovamento e obiettivi mancati*, eds. Daniele Caviglia and Silvio Labbate (Soveria Mannelli: Rubbettino, 2014), 39–71.

[114] Monnet, *Controlling Credit*.

[115] Jane Welch, ed., *Regulation of Banks in the Member States of the EEC* (London: Springer Science & Business Media, 2013); Emmanuel Mourlon-Druol, 'Banking Union in Historical Perspective: The Initiative of the European Commission in the 1960s–1970s', *JCMS: Journal of Common Market Studies* 54, no. 4 (2016): 913–27.

[116] ASBI, Banca d'Italia, Dir. Padoa-Schioppa n.1; cf. Monnet, *Controlling Credit*, 280.

[117] Carlo A. Ciampi, 'Tra mercato e controlli: aspetti operativi della politica monetaria', *Banche e Banchieri* (1981): 8.

[118] 'Never must there be less awareness of the risks that a rigid system runs and the willingness to abandon it as soon as the main road of the market becomes broader again' (P. Baffi, Imprenditori del credito, 29 Jan. 1979, own transl.). ASBI, Banca d'Italia, Dir. Padoa-Schioppa n.1.

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Ciampi and Treasury Minister Andreatta initiated the so-called 'divorce' between the treasury and the central bank. With an exchange of letters, they ended the practice, started in 1975, of the central bank buying unsold bonds at auction. The aim of the 1975 reform had been to strengthen the money market and give the treasury more tools to finance deficits. With the 1981 'divorce', however, they sought to 'decouple' the central bank from the obligation to intervene in the market, facilitating a return to market interest rates and helping to rein in government deficits. Central bankers abolished credit controls as part of their efforts to 'discipline' public finances and promote the return of the market as the primary mechanism for resource allocation.[119]

In 1981 Monti made explicit reference to such mechanisms, calling for the abolition of the ceiling on bank lending. He argued that

> the main reason for the survival of the ceiling is that it amounts to an indirect portfolio constraint on banks and the public to hold government bonds. The logical continuation of the 'divorce' with the Bank of Italy is for the Treasury to allow the divorce also to its other current 'forced spouses', the banks and the public. To do this it is necessary to remove the ceiling.[120]

Central bankers' frustration with growing treasury deficits during the 1970s led the bank to build a more efficient money market and thus to become a promoter of financial innovation itself. Credit controls, introduced as an emergency measure in 1973, then became an important part of monetary policy for ten years. Initially, they made it possible to channel resources to the public sector, keep interest rates low and direct credit to priority sectors at a time of high inflation and intense social conflict. From 1976, however, Paolo Baffi and later Ciampi, inspired by the central bank's 'repertoire of ideas', began to pave the way for a return to a more 'neutral' monetary policy regime, considered to be the bank's traditional framework. In the words of Ciampi:

> The model of monetary control that the Bank of Italy has taken as a reference has always been indirect, through the regulation of the monetary base and interest rates. Administrative constraints were conceived as an emergency measure. The fact that they have been maintained uninterruptedly for almost ten years can only be explained by the precarious state of the economy and, above all, of the public finances, and also by the time needed to restore the conditions necessary for indirect control to be effective.[121]

Conclusions

This article examines the causes behind the end of credit controls, with a focus on the Italian case in the 1970s. Credit controls were widespread during the 'golden age' of post-war capitalism, reflecting the distinct characteristics of national financial systems across various countries. These policies were part of a broader framework of state intervention in the economy, rooted in a fundamental distrust of the market and its ability to spontaneously achieve certain social objectives.

From the 1970s onward, global shocks, inflation, and social conflict posed significant challenges, leading to a crisis in state intervention. This resulted in the delegitimisation of the credit control regime and a shift towards a 'modern' or 'neoliberal' approach to central banking. In many European countries, this transition was disorderly and coincided with the process of European monetary integration. The creation of the European Monetary Union (EMU) was premised on the convergence of national monetary policies, with the market becoming the primary mechanism for the

[119] Maria Teresa Salvemini, 'L'indipendenza della Banca centrale e il divorzio tra Banca d'Italia e Tesoro', *il Mulino* 57, no. 5 (2008): 947–58.

[120] Mario Monti, 'La politica monetaria e creditizia italiana nel 1981–1982: aspetti congiunturali e prospettive strutturali', *Rivista Internazionale di Scienze Sociali* 89, no. 4 (1981): 822–30, own transl.

[121] Carlo A. Ciampi, 'Rientro dall'inflazione e politica monetaria: l'esperienza italiana, 1979–1985', *Banca d'Italia. Bollettino Economico* 6 (1985): 38, own transl.

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transmission of monetary policy. As a result, some scholars have questioned whether the European Economic Community (EEC) played a role in driving regulatory changes within national financial systems, ultimately leading to the abandonment of credit controls.

This article demonstrates that both the introduction of credit controls and their subsequent delegitimisation and dismantling were primarily driven by domestic processes related to monetary policy in a shifting international and financial environment. In Italy, the rise and fall of credit controls were closely linked to concerns over public finances and the central bank's efforts to establish an efficient money market. This aimed to expand alternative financing channels for the treasury and reduce dependence on monetary financing during the 1970s. The controls introduced in 1973, which were studied by economists in the bank's research department and inspired by foreign experiences, such as those in Japan, were justified by the difficulty of controlling the creation of base money and the need to transmit restrictive impulses to the system more quickly and more accurately. However, within the central bank's 'repertoire of ideas', credit controls were always considered emergency measures. Their prolonged use, along with the distortions they caused, led economists to reconsider Italy's credit system, ultimately favouring a return to the market as the primary mechanism for resource allocation. Rather than being a direct determinant, the process of monetary integration functioned as an 'ideal framework' that influenced and shaped the mental models of a new generation of economists, both within and outside the central bank, who sought to reform Italy's political and financial systems in accordance with their economic and political aspirations.

The end of credit controls in the 1970s offers valuable lessons for today's debates on the 'return of the state', particularly in understanding how crises and ideological shifts influence policy changes. In Italy, the economic shocks of the 1970s led to a rethinking of state intervention, with central bankers and a new generation of economists advocating a shift towards more market-oriented policies. This historical moment highlights the role of intellectual and ideological frameworks in shaping economic reform. Today, global challenges such as inequality and climate change are prompting a similar reassessment of the balance between state and market forces, with competing ideologies – ranging from (neo)liberalism to more state-centric models – shaping the debate. The experience of the 1970s shows how crises create opportunities for institutional change and policy innovation.

For future research, it would be valuable to explore how credit policy affects the degree of central bank independence, especially in the context of increasing government intervention. Understanding this relationship could provide important insights into the tensions between market dynamics and state control in addressing economic challenges. In addition, investigating the role of intellectual shifts in driving policy transitions could provide a deeper understanding of how different ideologies shape the trajectory of credit policy regimes in other countries.

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