

## **SPEECH ON THE BICENTENARY OF THE BANK OF FINLAND, 6 MAY 2011<sup>1</sup>**

Mr. Governor - Erkki, Fellow Governors, Hyvät Naiset ja Herrat, Mina Damer och Herrar, Ladies and Gentlemen,

Bicentenaries are special occasions. In my lifetime, we have experienced the bicentenaries of American Independence and the French Revolution. In comparison with those two events, you might think that the founding of the Bank of Finland would be a less significant event. You would be wrong. In fact, the Bank of Finland is a remarkable institution. Created by the reforming spirit of Tsar Alexander I, making it the fourth oldest central bank in the world, the Bank of Finland started life representing only one part of a larger Russian state, issuing first kopecks and then its own markka notes, and is now part of a European monetary union with a single currency. Much happened along the way, as Erkki Liikanen explained yesterday and as is admirably described in the superb history of the Bank by Antti Kuusterä and Juha Tarkka.

As that book makes clear, the history of the Bank of Finland is one of continuous involvement with the international economic scene. Founded at a time of monetary disarray in Europe, shepherding its nation towards independence at a time of turmoil in the Great War, dealing with the challenges of the gold standard and its subsequent breakdown in the interwar period, and finally preserving national independence and subsequent integration into European monetary union, the Bank of Finland has shown the way to its bigger brothers on more than one occasion.

The importance of the Bank of Finland in the political and economic life of this country was evident when I first visited the Bank more than forty years ago – long before I visited the Bank of England for the first time. Several members of the Board of Directors of the Bank of Finland were apparently on leave as Prime Minister and Finance Minister. To a young academic, this was most impressive, as was the state of the art seminar room. I could feel the special role of the Bank in Finnish academic, economic and political life. So it is a real privilege to share this occasion with some old friends and new colleagues.

Much of the academic discussion of monetary policy over the past twenty years has focused on central bank independence. But the wider role of a central bank in the constitution of its country is often overlooked. That is strange from both an historical and a contemporary perspective. In Britain, the creation of the Bank of England was one of a series of constitutional innovations that followed the Glorious Revolution of 1688. The Bank of France came into being following the French Revolution. And today the constitutional implications of monetary union are at the heart of the debate within the euro area.

The Bank of Finland was central to the development of an independent state of Finland. It introduced a new currency, the Finnish Markka, in 1860, long before independence of the nation in 1917. Indeed, the period leading up to independence has been described as ‘from paper rouble to gold markka’.<sup>2</sup>

But it was in the period between the two World Wars that the Bank of Finland faced its most difficult challenge. And the story is one of a relationship between two remarkable men: Risto Ryti and Montagu Norman, the two most famous governors of their central banks who held office through much of this period. Ryti was Governor from 1924 to 1939, and Norman from 1920 to 1944. As anyone who has studied the period, or read the book *Lords of Finance*, or seen his portrait in the Committee Room of the Bank of England, Montagu Norman was a complex, enigmatic and unusual personality, with a taste for the mysterious. He believed strongly in the need for central banks to be free from political interference. In order to pursue his commitment to central bank cooperation, Norman put unusual weight on links with other smaller central banks. He was very influential in the creation of the Bank for International Settlements and its ethos as a place where central bankers can talk with each other out of the glare of publicity. But in Finland, he met his match. For Finland had found a young man from the countryside who preferred books to farming. Risto Ryti was appointed Governor at the age of 34, having already served as Finance Minister. He was the equal of Norman in terms of power of personality and perseverance,

and his better in terms of intellect. This might seem surprising since no fewer than three Governors of the Bank of England have studied at King's College, Cambridge – Montagu Norman, Cameron Cobbold and myself. Sadly, only one completed his degree; it was not Montagu Norman.

From its creation, much of the Bank of Finland's strategy had been to promote the integration of the Finnish economy into the international trading system by linking the markka to a stable exchange standard. But after the First World War, Ryti, exceptionally, could see **both** the attractions of a regime of fixed exchange rates – at that time the gold standard – and the necessity to avoid returning to the gold standard at the pre-War parity. The credibility provided by belonging to a stable regime was actually enhanced by returning to the gold standard at a parity that reflected the truly extraordinary shocks that resulted from the Great War. This was a policy judgement that showed Ryti in a more favourable light than his British and other Nordic counterparts.

During the preparations for the return to the gold standard in 1925, and before the collapse of the standard in 1931 after which the markka was pegged to sterling, Ryti and Norman came to know each other well, and Ryti visited London on a number of occasions. During a visit to the Bank of England in September 1926, Governor Ryti explained to Harry Siepmann, Norman's advisor, something about his country and his central bank. According to the minute of that meeting kept in the Bank of England's archives,

“The Bank of Finland never have a dispute with their Government! The Government and country is well disposed to the Bank, partly because it was a Finnish institution, even when the country was under Russia. ... Officials of the Bank are better paid than our Government officials, but received about the same as those in the other banks. ... The Intelligence Section is run by one man and three women.”

Another confidential document, from 1932, provides the Bank of England's assessment of Ryti: he "typifies all the best points of his countrymen, especially grit and determination to overcome difficulty". Perhaps a more revealing letter to be found in the Bank of England archives is from Governor Ryti to Cameron Cobbold, a Bank official and later Governor, dated 18<sup>th</sup> June 1935, which discussed the forthcoming visit of Cobbold and another official, Humphrey Mynors, to Finland. Ryti wrote: "I shall have great pleasure in receiving you and Mr Mynors at the Bank of Finland at which I shall arrive on 4 July at 11:00 a.m. from the country where I spend my summer holidays at that time. Permit me to invite you and Mr Mynors to luncheon at the Bank after your arrival. I propose that we, after having discussed matters of mutual interest, start for a little trip to some nice places in South Finland, where I shall arrange possibilities of fishing or any other summer enjoyment in which you and Mr Mynors might be interested". On the letter is a handwritten comment by Mr Cobbold to Mr Mynors "this sounds like real central banking cooperation! What are your summer sports?" To which Mr Mynors responds by saying "Does this mean taking a mosquito net?"



Those happy and innocent days were soon to end. Once again, Finland found itself caught up in a European war, and isolated between Russia and Germany. When Russia attacked Finland on 30 November 1939, thus starting the Winter War, the promises of aid that Britain had made before the War were abandoned in the face of the logistical difficulty of making them a reality. Ryti became Prime Minister, and then President, in his country's time of need. Given his pro-British sympathies and dislike of Nazism, the tragedy of his later career is so much more poignant. With Russia an enemy, and Britain unable to help, Finland had to reach an accommodation with Germany. Britain even declared war on Finland in December 1941, often cited as the only time two democracies have ever gone to war. When Russia invaded Finland again in 1944, the only place to turn was Germany. So Ryti reached an agreement with von Ribbentrop guaranteeing that Finland would not negotiate peace with the Soviet Union for as long as he was the President. In exchange, Germany delivered weapons which enabled Finland to stop the Russian invasion. The letter was sent after discussions with Marshal Mannerheim and the war cabinet, and was deliberately expressed as Ryti's personal undertaking, thus avoiding the form of a binding

treaty between the governments of Finland and Nazi Germany. That enabled Finland to renege on the agreement later when Ryti resigned after the Russian invasion was halted. Ryti had knowingly sacrificed himself for his country.

Of course, at the end of the War, Finland was in the Russian sphere of influence, and Russia demanded that Ryti and others in the wartime government were put on trial. In March 1945 the British Foreign Office was under pressure from the Russians to have no dealings with ex-President Ryti. The Bank of England, in the person of Harry Siepmann, wrote to the Foreign Office in the following terms:

“This is no business (directly) of ours, and I realise that the Russians have strong views; but I hope I am not precluded from writing to you personally about what we know of Ryti. We have had long experience of him. ... His concern was always to promote general and not particular interests ... his abilities were absolutely first-rate by any standards. He did not sparkle, nor wish to; but he had an extraordinary poise, which made him simple, straightforward, dispassionate and clear in his approach, and quietly balanced in his judgment.

Behind all this, one felt the strong reserves of willpower which he held in readiness, to enforce but not to distort his conclusions. He was a man in a million. It may be – though I doubt it – that we can afford to discard such men. But nobody could be embarrassed or sorry or anything but proud to have been, and to remain, a friend of Ryti's, whatever the Russians may say". Not many politicians get that kind of plaudit from the Bank of England, but then Ryti was a former Governor!

Ryti and seven other former cabinet members were tried in Finland by a special "people's court" and found guilty of leading Finland to war against the Soviet Union. He was sentenced to ten years' imprisonment with hard labour. His health deteriorated and he was released after five years. As Erkki was kind enough to mention, in 2006 I received an honorary doctorate from the University of Helsinki, exactly fifty years after Risto Ryti was belatedly so honoured – he died only a few months later. I talked about the day on 21<sup>st</sup> February 1946 when the sentences were passed down on Ryti and his fellow defendants. Silence fell as the sentences were announced on the wireless, and a sense of anguish and shame were felt keenly, but in that silent Finnish way, across the country. The woman standing next to me in the degree ceremony, also receiving her honorary doctorate and a distinguished Finnish academic, looked at me and said, "My birthday is the 21<sup>st</sup> of February. Until today I never understood why my fifth birthday party was cancelled". Like so much of what happened at the end of the Second World War, only now are we able to see Risto Ryti's role in Finnish history in a truer perspective.

In conclusion, I want to draw three lessons from the example of Risto Ryti's life, one for Finland, a second for Europe, and a third for central banks everywhere.

First, Finland should be proud of the role which the Bank of Finland has played, not just in its administration of monetary affairs, but also in the wider political life of the country.

Monetary matters are often intricately bound up with politics. To some extent this is inevitable – what surer way is there of destroying the existing order than debauching the currency? But in a deeper sense, central banks are part of a country's constitutional arrangements. The Bank of Finland played a crucial role in the emergence of Finland as an independent state, and will surely be just as important in future as the constitutional implications of an enduring monetary union become apparent.

Second, in Europe we must pay more attention to the structure of our banks and the state of their balance sheets, not only for financial stability reasons but also for the conduct of monetary policy. Risto Ryti paid great attention to the details of banking arrangements. Monetary policy operates partly through its effects on the banking system. Economic theory has paid insufficient attention to the way the transmission mechanism of monetary policy depends upon the details of the behaviour of the banking system. As Governor Klaus Waris said in a speech on the 150<sup>th</sup> anniversary of the Bank fifty years ago, “The banks are inclined to be over-optimistic as to their future liquidity; they tend to underestimate their need for rediscounting, and hope to avoid the penalty rates”. When we redesign the liquidity regime for banks in the next phase of the Basel III negotiations let us remember the words of Governor Waris and our own experience in the autumn of 2007.

Third, around the world the tradition of central banks is to think objectively and to respect facts. That was the great quality of Risto Ryti. He looked at the facts and however unpleasant were their implications, he accepted them in deciding what was best for his country. However unpleasant we may feel the present situation to be, the choices we face cannot be compared with the appalling dilemmas faced by Ryti. He believed in openness, transparency and honesty in his political life. So he would have felt completely at home in a modern central bank. And we should be thankful that we face technically difficult but much less fraught problems.

As we meet on this historic Bicentennial, let us recall that we too are all experiencing a period of monetary and economic turbulence following the world's biggest financial crisis. We need to chart our way out of this crisis, and that we can do only together. In these circumstances, no country is an economic island and our salvation must be found in international cooperation. That must be built on national sovereignty. The history of Finland shows that to deny the importance of national sovereignty is dangerous. But for national sovereignty to be successful in an interdependent economic world requires a degree of trust and mutual cooperation. That has not always been present, but is more necessary than ever.



The leading figures of the Bank of Finland have been examples to us all. I have spoken at length about the remarkable Risto Ryti. But that same commitment to serving the interests of his own country while promoting international cooperation have been displayed by the present Governor, Erkki Liikanen, who served as a European Commissioner before becoming Governor, and his predecessor but one, Sirkka Hämäläinen, who was one of the founding Executive Board Members of the European Central Bank. And we remember today with sadness Matti Vanhala who died seven years ago at the early age of 58 and who, in a short time, showed us why Ryti was truly representative of his nation and central bank.

Today we celebrate not only a great past but an exciting, albeit challenging, future. Some of the events that shaped the Bank of Finland occurred many years ago, or, in the phrase used by Governor Waris on the 150<sup>th</sup> anniversary of the Bank, “kun isä lampun osti”, a delightful expression which means “in the days when father bought the lamp”. We have celebrated the past. Now let us drink to the future.

Suomen Pankki – kipsis! Skål! Cheers!

**ENDNOTES**

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<sup>2</sup> by Hugo Pipping