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Abstract

This paper analyses the role of capital in Central Banks (CBs), the implications for the effectiveness of economic policy objectives, and the strategies employed to preserve capital levels. Based on a review of literature and cases of CBs that have presented scenarios of considerable losses and capital impairment, the evidence suggests that the financial soundness of CBs may be a necessary condition for achieving their policy objectives, as it can impact their various transmission channels, through agents' expectations and public confidence. In this sense, a negative shock on these channels can compromise CBs' credibility and financial autonomy. However, there are cases of CBs that, despite having negative capital levels, have managed to be effective in implementing their policies, given that they have mitigating factors such as government fiscal support, solid legal and institutional frameworks, and stable financial systems.

In this regard, the case of the Banco de la República is analyzed. It was found that it has a legal framework that grants it financial, technical, and administrative autonomy, and that it also has mechanisms or strategies that have allowed it to maintain a solid financial position and preserve its capital levels. These mechanisms include the mandate to distribute profits/losses with the government, the possibility of establishing reserves in equity, and institutional strength, among others.

> ***The financial soundness of Central Banks (CBs) may be a necessary condition for achieving their objectives. Banco de la República (the Central Bank of Colombia) has a legal framework that grants it administrative, equity, and technical autonomy, as well as mechanisms that help preserve its capital levels, which has contributed to market credibility and confidence in the fulfillment of its functions***