

# Central Banks are not independent and often get it wrong

Please see below the slides from my lecture at All Souls College, Oxford, titled 'There is no Independent Central Bank':

## **Slide 1 – Three common propositions**

The main Central Banks are independent.

They are staffed and led by experts in economies and markets which means they will get it right.

Were the politicians and government departments to have more of a role in the conduct of monetary policy it would be badly run.

The last 30 years experience demonstrates all three of these propositions are false.

## **Slide 2 – Policy changes affecting the Bank of England**

1997 – The Bank of England is said to be made independent. It loses control of regulation of individual major banks to the FCA. It ceases to issue UK government debt which is given to the Treasury.

1998 – new Bank of England Act to confirm changes and keep Bank of England under Parliamentary control and supervision.

2003 – Chancellor of the Exchequer changes target for inflation from RPI at 2.5% to CPI at 2%, a looser target.

2008 – Chancellor of Exchequer overrides Bank of England interest rate setting, ordering a reduction in rates as part of a concerted G7 action to rescue collapsing markets.

2012 – New government legislates again through the Financial Service Act, confirming Treasury powers of direction over the Bank in Part 4.

Chancellor signs off successive programmes of Quantitative easing which are under joint control.

Treasury guarantees Bank of England balance sheet risks in bond portfolio.

## **Slide 3**

The government plays politics with the Bank and the Bank plays politics for the government.

The government exercises its right to select a new Governor of the Bank when needed and uses the appointment process to employ someone compatible with their aims.

The Bank usually keeps its economic forecasts close to those of the Office of Budget Responsibility and Treasury, despite these often being wrong.

The Bank backed Remain heavily in the referendum campaign, producing forecasts that were so one sided it lost a lot of support from the majority Leave side.

#### **Slide 4**

The Fed has a dual mandate to support employment and keep inflation below target.

The Fed Chairman has to report regularly to Congress and is therefore under pressure to respond to their priorities.

The Administration appoints the Board members, subject to ratification by Congress.

The Biden Administration is busily appointing Board members that reflect Democrat priorities.

President Trump took the Fed on in public and forced a change of policy from monetary tightening to promotion of growth.

#### **Slide 5**

The ECB does not have a single country sovereign to report to, which could make it more independent.

However in practice it is very conscious that it is a major driver of European Union and therefore has to be very political to assist integration.

ECB President Draghi's ''Do whatever it takes'' saved the Euro and Eurozone.

The ECB's development of the Target 2 balances system has allowed the big cash transfers needed within the Eurozone without them going through a much bigger EU budget.

#### **Slide 6**

The Bank of Japan works closely with the Japanese government.

Its long standing QE programme and low rates has been part of the government's 3 arrows policy to boost the economy.

It has continuously failed to get inflation up to 2%.

#### **Slide 7**

The Peoples Bank of China makes clear in all its policy statements it is an arm of government

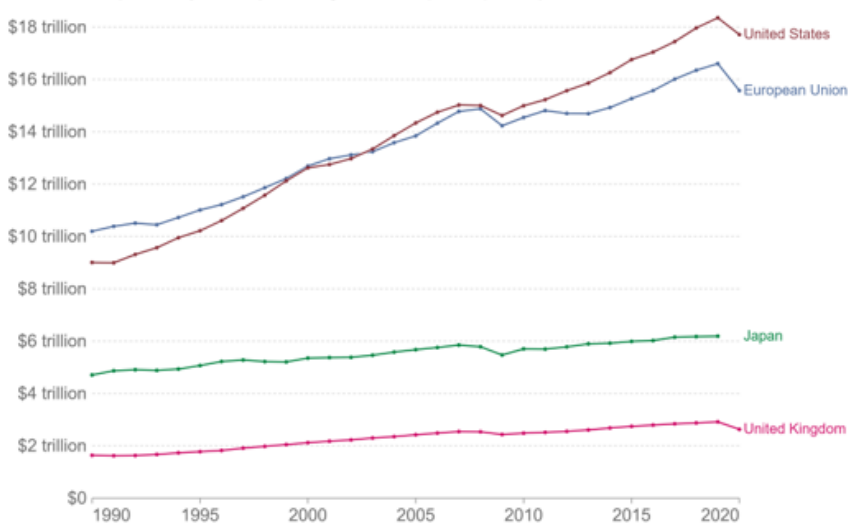
It openly supports the thought and policies of President Xi

It takes direction from the Communist party representative on its Board and fits into the successive government Plans.

## Slide 8

### Gross Domestic Product, 1990 to 2020

Gross domestic product adjusted for price changes over time (inflation) and expressed in US-Dollars.

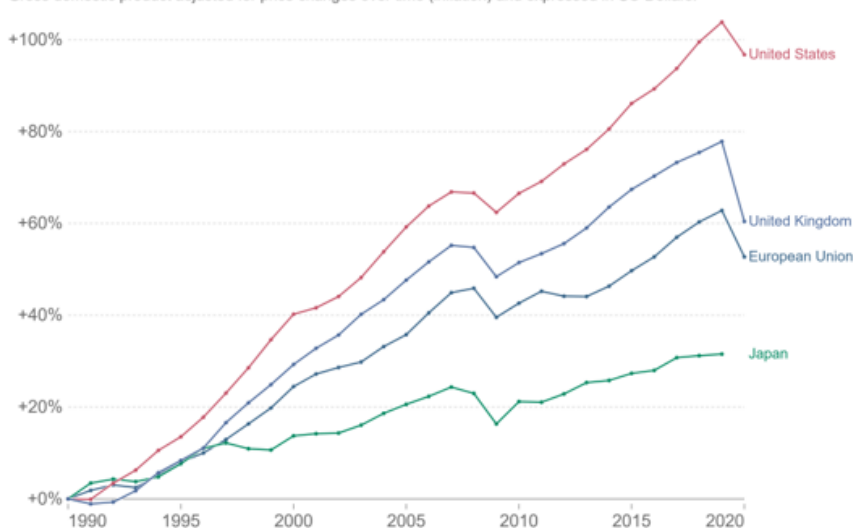


Source: World Bank and OECD

OurWorldInData.org/economic-growth • CC BY

### Change in gross Domestic Product, 1990 to 2020

Gross domestic product adjusted for price changes over time (inflation) and expressed in US-Dollars.



Source: World Bank and OECD

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## Slide 9 – Current inflation rate against 2% target

USA – 7.5%

Eurozone – 5.8%

UK – 5.5%

Japan – 0.5%

## Slide 10 – Three major economic disasters inspired by Central Bank advice and thinking 1990-2021

- a) The Exchange Rate Mechanism collapse 1992
- b) The Great Depression and banking collapse 2007-9
- c) The Euro crises 2011-14

And now the Big inflation 2021-3

### **Slide 11**

The consequences of political intervention have been mixed. Clearly Turkish override of the Central Bank and changes of Head have led directly to currency collapse and rapid inflation. Governments have debauched currencies in countries like Venezuela, Argentina, Zimbabwe where central Banks have not been able to exert more control.

In western societies the political intervention in the 2008 banking crash turned round the disastrous situation the Central Banks had created by deflating their bubble too quickly

President Trump was probably right that Quantitative tightening was too tough when he talked the Fed into a more neutral policy

Governments were right to encourage Central Banks to be very accommodative as an offset to lockdowns during the intense period of the pandemic

It is clearly true that governments are more likely to intervene helpfully when Central Banks are being too tough than when they are being too easy and risking too much inflation.

### **Slide 12 – Why do Central Banks often get it wrong?**

The Western Banks base their work on a model of output and capacity. These concepts are flawed and difficult to measure in a complex globalised economy.

The Banks are too influenced by the consensus. The consensus rarely spots turning points.

The people on Bank Committees rarely have superior insights into markets.

Seeking judgements by Committees rarely gets it right, as Committees tend to an average or blended view. Often in markets you need to choose between two more extreme options to get it right.

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## **Responding to the war in Europe**

Dear Constituent

Many of you will be sharing my horror at events in Ukraine. The daily scenes of death and destruction, of mass movements of people fleeing the violence are harrowing. They are a constant reminder of why war is wrong. They are what happens when politics and negotiation fail.

Some of you write wanting the U.K. to enforce a no fly zone over Ukraine to stop aerial bombing. This would mean declaring war on Russia, as a no fly zone would require contesting Ukrainian air space with the Russians. Escalating the war in this way would be full of hazards. Nuclear powers taking each other on requires restraint by both sides over first use of nuclear weapons. NATO could of course defeat Russia at likely great cost to life and property but the U.K. alone would be stretched. Our allies led by the USA do not want to take NATO to war with Russia over Ukraine. A successful No fly zone after a bruising set of air battles would not end the ground artillery and missiles raining down on Ukraine unless a victorious NATO airforce went on to bomb Russian forces in difficult urban locations with likely deaths of the very people we wish to help.

Some of you wish to see more rich Russians in the U.K. sanctioned, with confiscation of assets. Ministers are keen to do this to all cronies of Putin who might still have some influence over him, and to those who came by their wealth through crime. They do need to proceed according to the rule of law. Many rich Russians living peacefully in the U.K. are neither Putin supporters nor criminals. The government should sanction those where they have a good legal case against them. This can take time to research and establish.

Some of you want a generous offer to those fleeing the violence. The government is expediting entry to the U.K. to those with family here who wish to come to stay. The needs and wishes of the hundreds of thousands crossing into Poland and Romania is to be housed and fed near to Ukraine with a view to returning to their homes as soon as possible. Many are women and children temporarily separated from their menfolk who have stayed at home to fight. The U.K. is offering substantial financial and practical aid to assist with the temporary camps. The U.K. will keep its support under review as the situation develops as needs and wishes may change.

The U.K. did lead a stronger response from NATO with deliveries of weapons to help defend Ukraine before others and by working with US Intelligence to reveal the true nature of Putin's plans to encourage preparation against the onslaught. The U.K. is striving to do all it can as a good ally short of declaring war to pressurise Russia to end the violence and helping brave Ukrainian defenders hold off the attacks.

Yours sincerely

John Redwood

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# Ukraine Humanitarian Appeal

Constituents have asked how they can donate to the humanitarian effort in Ukraine. I've been informed that the Disasters Emergency Committee (DEC) has launched its Ukraine Humanitarian Appeal. The UK Government will match pound-for-pound the public's first £20 million and look to increase over time.

<https://www.dec.org.uk/appeal/ukraine-humanitarian-appeal>

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## A change of accounting could give us a better energy policy

It is wrong that the U.K. is importing Russian Gas by LNG carrier. It means more CO<sub>2</sub> is generated than burning home produced gas. It means Russia gets huge tax revenues that the U.K. would reap on home gas. It means we miss out on more better paid jobs. It means we finance Russia's thug wars.

It is wrong that the U.K. continues to import wood from North America to burn in the Drax biomass power station. We should growing more of our own timber to stoke the fires at Drax.

It is wrong that we are importing electricity from a European continent short of energy and dependent on Russian gas and coal for some of its generation. We should generate our own using U.K. fuels or renewables.

So why are we undermining our national resilience? Why are we making U.K. consumers pay even higher prices to cover the extreme costs of imports at current spot prices? Why are we creating more global CO<sub>2</sub> with this import based system?

Part of the answer seems to be the civil service and some Ministers' passion to get the U.K. count of CO<sub>2</sub> produced down. The way they count it if we import fossil fuel or products made with fossil fuel is the CO<sub>2</sub> generated counts against the exporting country and does not add to our total. Yet the world ends up with more CO<sub>2</sub>. Time to account for all the CO<sub>2</sub> to weight decisions back in favour of domestic energy and production.

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## What proportion of covid-19 test kits are imported?

**Rt Hon Sir John Redwood (Wokingham) (Con):** To ask the Secretary of State for Health and Social Care, what proportion of covid-19 test kits are imported.

**Maggie Throup, Parliamentary Under Secretary of State for the Department of Health and Social Care:** Currently 90% of lateral flow device tests are imported although we expect this to decrease to approximately 70 to 80%.