

Central Banks have plenty of options

The Bank of England has uniquely amongst the larger Central Banks of the world set its policy against promoting growth. The rest of the world's leading Central Banks have been loosening policy this year to prevent the global slowdown becoming a recession. How are they doing this? What are the Bank of England's options?

Some have simply been cutting interest rates. Some have lowered reserve asset ratio requirements, which is a way of allowing commercial banks to lend more for the same amount of capital they hold. Some have made available cheap facilities for commercial banks to borrow if they will lend more to the real economy they serve. Some have undertaken full Quantitative easing, creating money to buy bonds and ETFs to drive asset prices up and keep interest rates low. Some have injected more money in through the money markets.

I am not proposing a resumption of Quantitative easing in the UK. Nor does the Bank have to cut interest rates, though taking 25 basis points off the 0.75% interest rate would send a signal. Better would be to relaunch Funding for lending, a scheme to provide more money for commercial banks to support investment and larger consumer purchases in the economy. The Bank should also cancel or defer its recently announced doubling of the counter cyclical capital buffer.

There will be those who object that the Bank is independent, so the rest of us should not discuss these matters. How wrong they are. In a democracy the Central Bank, owned by taxpayers, has to be answerable to Parliament and people. The government has just appointed a new Governor, so presumably they have discussed with their preferred candidate how they see the task ahead. The Labour government legislated to make big changes to the functioning of the Bank, taking away substantial powers it needed to regulate and guide commercial banks and money markets. The Coalition government legislated to put those powers back. Government and Parliament settle the aims of Bank policy and can change those if they wish. There has to be continuous dialogue between Central Bank and Treasury as they are both having influence over the same economy. It helps if they are both trying to achieve the same purpose.

The Governor is accountable to Parliament and comes to give evidence of progress. The Bank works closely with the Treasury, particularly at budget time. The two institutions do not usually diverge much in their forecasts. The new Governor has to understand there has been a big change of economic policy with the change of government. The target of reducing state debt as the main aim of policy has gone. The promotion of growth now lies at the heart of the new fiscal framework. It must also inform the Bank's work. The Bank of course has to keep to the inflation remit but needs to understand the shift of its parallel aim of helping promote growth and good levels of employment. Currently there is no inflation threat in the advanced world and no inflation problem in the UK.

Let's hope others join in the call for a change of approach at the Bank of

England. They have fought inflation successfully. They now need to join the mainstream of world Central Banks and fight against slowdown.