

My Telegraph article on Central Banks

Jerome Powell, the leader of the world's most important and powerful Central Bank has made a strong case for limited independence within a democratic framework. Warning against a Central bank widening its remit and scope too far, he spoke out against Central Banks taking on roles to put us on the road to net zero and other social objectives. He argued that "addressing climate change seems likely to require policies that would have significant distributional and other effects on companies, industries, regions, and nations. Decisions about policies to directly address climate change should be made by the elected branches of government and thus reflect the public's will as expressed through elections" . If you give an independent body one or two targets and aims it is possible to monitor success and demand improvements or changes where needed. If you introduce a range of targets the Bank is distracted, making compromises where the aims are in conflict. It also opens itself up to more political criticism. There is no serious body of opinion in the US or UK wanting banking instability or high inflation so setting targets for these does not politicise the Bank. The ways to net zero, the speed of transition and the desirability of its various policies remain much disputed, and are far outside the powers of a Central Bank to deliver. The Bank of England and the European Central Bank should consider this advice carefully.

Jerome Powell wisely recognised a Central bank needs to justify its independent power to raise or lower interest rates. He said " the Fed must continuously earn that independence by... achieving our assigned goals of maximum employment and price stability, and by providing transparency to facilitate effective oversight by the public andCongress." He did not consider how it came to pass that with this independence the Fed kept rates very low, created trillions of dollars and ended up with inflation five times its 2% target. The Fed was free to buy bonds on a huge scale and did so. The Bank of England adopting a similar policy was not independent over money creation and bond buying. Under the agreement first entered into by the Labour government at the time of the great banking crash, all the money created and bonds bought in the UK required the written consent of the Chancellor who answered directly to Parliament. Labour, the Coalition and the Conservative governments all provided a complete taxpayer indemnity for the Bank against losses on the bonds. The Fed is just going to take the losses and record the fact on its balance sheet without taxpayer payments. I agree that keeping rate setting out of the hands of politicians makes sense, but also think the elected bodies that appoint the Governors and question them need to do a better job at finding out why inflation got away. The leading Central Banks should take more interest in monitoring and responding to excessive money and credit creation. There needs to be a proper debate about how they can avoid another big inflationary upsurge – or banking crash – in future.

The Fed Chairman went on to say we should "stick to our knitting and not wander off to pursue perceived social benefits that are not tightly linked to our statutory goals and authorities. In a well-functioning democracy,

important public policy decisions should be made, in almost all cases, by the elected branches of government. Grants of independence to agencies should be exceedingly rare, explicit, tightly circumscribed, and limited to those issues that clearly warrant protection from short-term political considerations.”

This is very good advice. As the Fed, ECB and Bank of England have just shown it is easy for Central Banks to make major errors in their prime task of counter inflation policy, just as they all have questions to answer about their role in the banking crash in the previous decade. Taking on additional roles impedes focus on the central tasks of low inflation and banking stability which must be their rationale.

It is no surprise that Mr Powell should chose to make this intervention into the political debate as he faces a recently elected Republican led House of Representatives who have very different views on fossil fuels and net zero transition to their Democrat opponents who lost the majority. It shows his customary political sensitivity that he at this moment rules out some of the favourite Democrat themes from the core message of the Fed. The Bank of England also needs to concentrate on the knitting after a bad period over inflation. The Bank needs to balance pressure down on inflation without creating a needless deep and long downturn. That is the part of the Fed remit that makes great sense, to worry about employment as well as inflation within the context of an overriding target to keep inflation down to 2%. It is the job of elected governments to decide energy policy, food policy, transport policy and housing policies that are all involved in current ambitious plans to decarbonise.