Funding the Future

The Governor of the Bank of England is now a threat to ...

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Andrew Bailey proved beyond a shadow of a doubt that he is the wrong Governor for the Bank of England at this (and maybe any other) moment yesterday. Writing in the Financial Times he said:

This is a time of great uncertainty. The Bank of England is doing all it can in this difficult environment to reduce the disruptive consequences for businesses and households and minimise longer-term damage to the economy.

He did not tell the truth when making that opening claim. At the end of his piece he qualified his statement, saying:

The BoE will not hesitate to take all necessary actions both to support British businesses and households through this period of uncertainty and to ensure inflation is consistent with the 2 per cent target in the medium term.

In other words, the Bank will help just so long as the neoliberal thinking that establishes the priority of stable money to preserve the value of debts owing to the wealthy is not prejudiced.

And as if to throw down a direct challenge to the government on who he thinks has control over management of this crisis, he said:

The crucial point is that the MPC remains in full control of how and when that expansion is ultimately unwound. The goal is to ensure that borrowing costs and spending are consistent with achieving the inflation target. If the recent expansion of bond buying appears to threaten that goal, the MPC can react.

In other words, let's ignore the fact that people, including fourteen health workers so far, are dying right now. And let's ignore the fact that it is likely that six million people in the UK will likely really be unemployed by this summer. And let's be wholly indifferent to the fact that getting employment going again is going to require unprecedented liquidity boosts for the economy, without which we face many years of slump. Instead let's worry about the credibility of the old order. And let's worry about the dogma of monetary economics that dictates bankers must be in control to fight an enemy so long ago defeated, which was inflation at something like full employment.

This is callous indifference. It reveals a mindset determined by privilege. It reveals blatant bias, not least when it is clear that bankers will get what they wish. Bailey noted the “recent provision of liquidity to the banking sector and purchase of commercial paper in the new Covid Corporate Financing Facility”. He is apparently entirely happy with this expansion of the Bank’s role.

He did, however, make very clear his objection to direct monetary funding (DMF) of government spending by central banks. As he said:

The MPC controls the level of benchmark interest rates and can vary the quantity of central bank reserves. Central bank reserves are interest-bearing deposit accounts held at the BoE backed by the central bank’s assets, mainly gilts.

Some MPC actions result in the creation of central bank reserves. But these reserves are not being created with the aim of paying for the government deficit, as under monetary financing. They are a consequence of independent central bank policy actions to deliver monetary and financial stability.

In saying this Bailey makes clear that he will not use the power of the Bank to create money to help the government tackle our current crisis.

What is the alternative? Presumably he would want the government to tackle the crisis by taxing more, which would suck money from the economy at the very time it was most needed, and just when deficits should be run, and when underpinning by the Bank is essential.

But he won’t do that. As he put it, he will only go so far:

To that end, the Monetary Policy Committee voted last month to increase the bank’s bond holdings by £200bn to support the needs of the British people. Some external commentators are linking this move to fears that it that it may be using “monetary financing”, a permanent expansion of the central bank balance sheet with the aim of funding the government.

This type of reserve creation has been linked in other countries to runaway inflation. That is because it could undermine a central bank’s ability to control monetary conditions over the medium term. Using monetary financing would damage credibility on controlling inflation by eroding operational independence. It would also ultimately result in an unsustainable central bank balance sheet and is incompatible with the pursuit of an inflation target by an independent central bank.

So we have a choice, which is to maintain the credibility of theoretical monetary policy, which in the era of net-zero inflation rates that we have witnessed for the last decade, has been irrelevant in the UK and much of the rest of the world for the last decade, or we can a government in democratic control of getting us out if this mess. And he even resorts to hints of the Weimar Republic myth to make his supposed case.

Bailey has indicated dogma comes before people as far as he is concerned. By doing so he confirms he is made of the banking mindset that consigned this country, wholly unnecessarily, to the Great Depression of the 1930s.

This country can not afford the likes of Andrew Bailey at any time, but most especially at moments like this. He is a man as out of his depth as Sunak was on Budget Day, indicating by his words that he is dealing with a situation that is far beyond his ability to comprehend. I sincerely hope his tenure is short, or he will seek to impose untold harm on the country.