

The Bank of England fights itself

The Bank of England has two major committees. The Monetary Policy Committee is currently wanting interest rates to climb ever higher and is willing to see mortgage and other longer term rates of interest hiked as well. They regret the big inflation that has taken place, though they blame the European war rather than their own ultra low rates and bond buying in 2021. They forget that inflation was already at 5.5% before the invasion started, 175% above target. They want to start selling the large portfolio of bonds they bought up over the last decade to take big losses on the bonds and drive interest rates higher.

The Financial Policy Committee is responsible for orderly markets and avoiding financial crises. They have had to intervene in the last two weeks to temporarily reverse the MPC's policy of selling bonds and hiking rates. They have warned that rates have risen too far too fast and bonds have been too depressed. This has led to issues for some pension funds and other owners of government bonds that has worried them .

This big split has led to some announcements that seem contradictory. We are told the MPC has great resolve to make money dearer to get rid of inflation, and that the FPC needs rates lower to cut the losses on bonds to ensure stability. In 2021 the Bank was united in wanting rates as low as possible and bond prices as high as possible. In 2021 for a time the Bank was united in wanting to correct its 2021 errors by higher rates and ending bond purchases. More recently we have had the announcement of bond sales, promptly followed by the announcement of bond buying, to be followed by possible bond sales shortly afterwards. No wonder the market is disturbed.

We need stability of policy and clear signalling of intentions. Why not say the Bank has no plans to sell any bonds all the time they are this depressed? They should give early warning of any intent to sell should bonds rise to a more acceptable level. They could do what Japan does and give indications of what they think a sensible level of 10 year interest rates would be. As the Bank owns around one third of all the gilts and is such a major player they can have great influence over the interest rates and bond prices. They need to use this influence for the Goldilocks rate – the rate that brings inflation down without causing a panic or deep recession.