

## Why the Bank got it wrong

The Sunday Times ran a topical joke." Two members of the Bank's Monetary Policy Committee walk into a bar. You'd think one of them would have seen it". It is not good when the Bank's ability to forecast and to carry out its main task of keeping inflation to 2% is cause for wide ranging ridicule and censorship. Let me try and explain a little more why inflation is so high and who is to blame.

The first thing necessary to have a more adult debate is to understand the very considerable limits on so called Bank independence. When the Bank first starting printing more pounds to buy up more bonds in the policy called Quantitative easing the Chancellor, Mr Darling, insisted on the Treasury agreeing the sums. The Bank wanted an indemnity against losses on the bonds from the Treasury and taxpayers, so the Chancellor demanded the he and his successors signed off the amounts of any such policy. All Chancellors since have done so and continued the indemnity.

The second thing to grasp is that the main reason inflation has set in badly here, in the USA and in the Eurozone is that all three central banks printed too much money. The Chinese and Swiss Central Banks did not do this and their countries have today inflation around 2% despite also experiencing the sky high energy prices and rising food inflation. Countries like Turkey and Argentina which have printed even more have much higher inflation rates.

So we need to ask why did the Bank of England recommend and execute a policy of creating an extra £450bn and buying bonds with it from 2020 to end 2021? They decided that the large contraction in economic output triggered by the wide ranging and long lasting lockdown of the economy from March 2020 required a substantial monetary offset. As rates were already low and they thought they could take only them down to 0.1% they needed to inject large sums of additional cash into markets. They were also conscious alongside the Fed that in March 2020 the fears of the impact of lockdown were causing a financial and banking market collapse which needed large sums in liquidity to offset.

I think their judgement in March 2020 was right and I strongly supported it. I also supported the Treasury action it made possible, of borrowing huge sums to return some income and cash to the many people and firms that were losing income from the shutdowns. The two actions went together. The state could only borrow that amount at a very affordable rate if the Bank printed money to help them. The impact was not inflationary overall as so many activities were stopped or greatly reduced by the controls.

Unfortunately in 2021 the Bank continued to print money and keep interest rates on the floor long after a good recovery in activity had taken hold. The government continued to borrow and spend on huge scale on a series of special programmes where test and trace was the largest. This was bound to be inflationary, though the Bank ignored those of us who warned it to stop printing. The government continued with expensive lockdown style policies for

longer even though vaccines and treatments had greatly reduced death rates from the virus . The economy revealed a number of crucial supply bottlenecks as lockdown measures had damaged UK and global capacity in various areas.

China and Switzerland show that even with sky high energy and dear food it was possible to keep inflation down. The Peoples Bank of China have monetary targets and think controlling the amount of new money is an important part of controlling prices. The Bank of England do not bother to monitor and control the amount of cash . They prefer to believe the unlikely proposition that if you print a load of money and give it to people and businesses they will use it less. That was true in lockdown but they wanted to spend when lockdown tailed off. Maybe the Bank should start to take money growth more seriously.

It was a pity that China who got inflation right was busy trying to correct a credit bubble in property they had allowed. There are many features of the China approach it is better not to follow. The question for Bank of England MPC members is when you saw those piles of cash you were printing, why did you think people would not use them? Or was it you did not see them because you did not bother about the money supply?