



Economic Affairs Committee

Corrected oral evidence: Bank of England: how is independence working?

Tuesday 27 June 2023

3 pm

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Members present: Lord Bridges of Headley (The Chair); Lord Blackwell; Lord Davies of Brixton; Lord Griffiths of Fforestfach; Lord King of Lothbury; Baroness Kramer; Lord Layard; Baroness Liddell of Coatdyke; Lord Londesborough; Lord Rooker; Lord Turnbull.

Evidence Session No. 12

Heard in Public

Questions 196 - 220

Witnesses

I: Lord Macpherson of Earl's Court, Former Permanent Secretary to the Treasury; Sir John Parker, Former Chair of the Court of Directors, Bank of England.

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Examination of witnesses

Lord Macpherson of Earl's Court and Sir John Parker.

Q196 **The Chair:** Welcome to this hearing of the Economic Affairs Committee and our inquiry into the Bank of England. We have two excellent witnesses this afternoon. Would you like to introduce yourselves for the record?

Sir John Parker: Thank you for the unexpected invitation to appear before the committee, unexpected in the sense that my five years at the Bank were between 2004 to 2009, which is 14 to 19 years ago, so I trust you will be tolerant should I not recall those times with perfection.

I should also underline to this committee that I am not an economist; I am a naval architect and engineer. Therefore, I am particularly happy that I share this table with Lord Macpherson, who will cover all those issues for me quite handily, I hope, being the former Permanent Secretary to the Treasury and a man I had a very positive relationship and communication with during my time at the Bank, and with his predecessor, Gus O'Donnell. Thank you.

The Chair: Thank you for joining us.

Lord Macpherson of Earl's Court: I was Permanent Secretary to the Treasury from 2005 to 2016. I should declare an interest as chairman of Hoare's bank, which opposed the setting up of the Bank of England in 1694.

Q197 **The Chair:** That is a very good way to kick off my first question, which does not go back to 1694 but only to 1997-98. Heeding what you say, Sir John, I completely understand.

I ask all our witnesses a scene-setter question. How do you think operational independence is working, and what do you make of the Bank's performance, particularly in light of what we have seen in recent months? I would not say there has been a complete collapse, but it has seen a considerable lack of public confidence in what the Bank is doing to control inflation. Lord Macpherson, could you start by giving us your views overall on the last 20 years or so?

Lord Macpherson of Earl's Court: I think independence has been a success, by which I mean that, since the Bank of England became operationally independent, the outcomes have been better than if the Bank had not been independent. I should briefly point out that my theory of the Bank of England is that we get overly obsessed with legislation and particular Acts of Parliament. It is better to look at the long-term evolution of the institution, and it has been very evolutionary; a lot of the building blocks for independence were put in place when we left the ERM in 1993.

Coming back to the last 25 years, it has generally gone very well. As the then governor described, there was first the nice decade when everything basically went very smoothly, helped by globalisation and the entry of

China into the world economy, but also by the real success of the Bank, supported by the Treasury, in changing inflationary expectations in this country. There was a minor blip during the financial crisis. It is fair to say that the Treasury and the Bank of England did not quite understand each other in autumn 2007, but the good news was that, by autumn 2008, when it really mattered, we had a very good understanding of one another.

The only potential black mark I would put on the period of independence has been what has happened recently. The problems that the Bank has been grappling with are global. Every country in the developed world has been dealing with higher inflation. Britain has its own particular issues, which may or may not be adding to inflation. I think it is fair to say that all central banks perhaps loosened policy too much, for fear that we were going into a period of deflation. We are now dealing with the consequences, which largely arise, in my view, from supply side shocks. However, I would argue that excessively loose monetary policy kept in place for too long has probably facilitated higher inflation than there would otherwise have been across the western world.

Sir John Parker: I do not differ too much from Lord Macpherson's remarks. I looked at it from the point of view of outturns, which as a businessman you generally do. Twenty-six years is quite a long period of time. As far as I can make out from the numbers, the Bank rate in 1997, when Gordon Brown granted independence, was 6.5%; today it is 5%. The average through that period has been around 2.86% for the 26 years, June to June. Inflation in 1997 was 2.2%; today, the average over the 26 years of 2.5% has peaked recently at 11% and is now 8.7%. Based on outturns, I suspect Gordon Brown would probably have brought this 26-year outturn on day one of independence. Looking back, I would say that this has been a very significant success for the country overall.

It is the current deviations that are of concern and the focus of criticism. However, rather than fuel a blame game with critical comments, what is needed is a fundamental root-cause analysis. An industry—if there was a major accident, for example—would immediately swing into action with a root-cause analysis, which would attempt to isolate the contributing factors, ensure learning from the experience, and establish corrective action to avoid repeats. I think that would be my approach if I was asked how I would get a better understanding of what is happening.

As a non-economist, it seems to me that, quite apart from war-induced high energy prices, which most countries have been dealing with, unlike others the UK is wrestling with the fallout from Brexit, which is impacting business. Of course, we are not here to discuss the merits of Brexit—that is a decision already made—but to understand and admit the reality of what business is dealing with in the fallout.

There seems to me to be a unique range of factors that are contributing to forecasting challenges. First, there has been the drop in sterling, which is still fuelling import costs. A second factor, and I know this from industry, is the large number of skilled people who went back to Europe.

Now there is a scramble to replace them at much higher wage rates than what we were paying. Thirdly, there is the negative impact on our exports to Europe, but the increased friction in imports is depressing productivity in some instances and certainly increasing costs.

There are other serious non-headline events happening. I will give you facts and figures in a moment, but a range of suppliers are, arbitrarily and opportunistically, increasing prices by multiple times inflation. I will give you a very small business example from close to my home in Devon, a small specialised bakery. It is closing down, so they gave me the figures for their input costs: flour—plus 104%; margarine—plus 82%; butter—plus 89%. The champion was mayonnaise—plus 123%. These are staggering numbers for a small business, so there are opportunistic drivers going on that must be quite difficult to identify.

Take the construction industry, which represents 9% of employment in the UK. Steel reinforcing bars have gone up by 39% since 2021. Gravel and sand, believe it or not, have gone up by 21%. Plastic doors have gone up by 25%. Wages, catching up with the loss of some skills, are running as high as 14%. We have a lot of underground forces at work that are very difficult and very challenging to pick up in the forecasting.

There is one other point, perhaps, which I can make now or later, which raises a question in my mind. One thing that deeply impressed me when I was at the Bank was the rigour applied to the Monetary Policy Committee processes. As board members, we were fortunate enough to be able to go to the briefing and presentation meetings to members of the MPC in advance of their monthly meeting. It was the sheer rigour and discipline of the process and the fact that the very best economists in the Bank were used in that process. There was the opportunity for the MPC to challenge openly and so on.

Is that same rigour still in place? If I were to suggest a way to plumb the depths of that, it would be to invite a previous highly respected member—who would be a heavyweight economist from the past, from that period—to quickly assess: has something fundamentally changed?

Q198 The Chair: That sets up some very good questions, which we will come on to. Lord Macpherson, when you look back over your period up to now, do you feel that now is the first time the structures around operational independence have been tested? If it is not just now, when else have they been tested and how has that test manifested itself?

Lord Macpherson of Earl's Court: Quantitative easing inevitably created challenges in the way it was going to be conducted because of the relationship between monetary and fiscal policy. It came in in early 2009, I think. That was handled very well, because it appeared to be a temporary measure in extreme circumstances.

As time has gone on, with quantitative easing expanding and with a slightly asymmetric approach to quantitative easing, which potentially reached its peak at the beginning of the Covid crisis, you have a greater

tension, which you see playing out with people who argue that the Bank of England is losing lots of money as a result of quantitative easing and the Treasury will have to put taxpayers' money into the Bank. What that quite neatly forgets is that in the early stages it made the Treasury a lot of money. Originally the plan was to keep this money ring-fenced, but the Treasury had the odd fiscal problem, I think in the Osborne era, where we had to meet a target and it became convenient for the money to be transferred into the Treasury.

I do not think this problem has gone away. My guess is that there will be further losses as a result of QE, and it would only take a very populist Government to say, "Hang on, we're not going to use taxpayers' money to prop up the banking system", to potentially undermine the operational independence of monetary policy. It is much more in that space than, say, in the financial stability space that the threat to independence resides.

Q199 Lord Griffiths of Fforestfach: I was very interested, Lord Macpherson, when you said, regarding 2017-18, that the Bank and the Treasury had a good understanding of each other. You said that in 2007 it was not so good, but that in 2008 it was. The Treasury was in charge of fiscal policy and the Bank was in charge of monetary policy. Could you tell us what a good understanding between them really means?

Lord Macpherson of Earl's Court: I was talking very much in the context of financial stability. I do not think we had remotely a problem on monetary policy in 2007-08; we were very happy to let the MPC take the lead.

The problem I would identify was that we were faced with a banking crisis. Some of us had been involved in the Barings collapse, but this was on a different scale, and it was the first retail run, I think—the previous governor will put me right—since 1914. It was something new. We had not anticipated it. I could talk at length on that, but it would be going over old issues.

The new Labour Government were a quite sensitive Government and not in the business of nationalising banks. That was quite a big hurdle to cross. It was obvious to me, and it was almost certainly obvious to Lord King, that Northern Rock was going to be nationalised, and we knew that from late September 2007. Funnily enough, had it been a Tory Government, this would have been less problematic, but new Labour was not in the business of nationalising banks.

Once we passed the necessary legislation, it all became very easy and we could. Inevitably there was a tension over that period, and in these situations the FSA inevitably thinks it is a liquidity problem, the Bank is likely to think it is a capital problem, and the Treasury just wants the whole problem to go away. But we dealt with it. The Treasury was interested, because there was a fiscal consequence to all this, but I do not think it was a classic problem of monetary fiscal interdependence.

Lord Griffiths of Fforestfach: Thank you. That is a very clear explanation.

Q200 **Lord King of Lothbury:** I would like to ask you about your reflections on the structure of the monetary policy framework. Lord Macpherson, you said that we should not focus too much on legislation but on how the system has evolved. One level of the framework looks very simple: the Bank of England is told to achieve price stability, and the Government, through Parliament, tell the Bank that that means always aiming at a 2% inflation rate—we will not hit it precisely, but there will be movements up and down and, with a bit of luck, over a long period of time it will average 2%, which it did right up to 2020.

You both had very special perspectives on this, because those of us who were on the Monetary Policy Committee were involved in making decisions month by month. Sir John, as Chair of Court, and Lord Macpherson, as Permanent Secretary, you had responsibilities for thinking about how the whole framework operated: appointments to committees, scrutinising whether members of the committees had adequate resources, and things of that kind.

Looking back now over the period, is there any issue about the governance side of the framework or the way in which it operated that you think was very successful or unsuccessful and maybe needs amending?

Sir John Parker: One of the tasks I had was to interview every member of the MPC annually to check that they had complete freedom to express their views—there was no coercion involved—and had sufficient research resources, and whether anything else was pinching their heels. Generally, they were extremely happy.

The one question I remember asking MPC member Stephen Nickell was, “Do you feel able to act independently?” He said, “Our great strength is that we don’t do consensus”. I was very heartened by that from a governance point of view: that here was a group of people who could individually do and speak as they felt. That freedom, to me, represented good governance.

Lord Macpherson of Earl’s Court: I would endorse that. I think the principle of one person, one vote strengthened the process. It created transparency—transparency is important for a wider understanding of what is going on—and the fact that the independent members had access to reasonable resources, with time, also helped. The process definitely improved in the early years, and I witnessed that first-hand. There was a problem with appointments because the process for appointments was not as transparent as it might have been.

One of the reforms that Alistair Darling introduced when he was appointed Chancellor, or shortly after, was having a process whereby MPC jobs were advertised, and you had a proper field. Obviously you could ask individuals to apply. When it started, you could attract not necessarily the best but very high-class people. There is always a

problem with conflicts of interest, which increases the probability of appointing academics to the committee, because for them the salary offered by the Bank of England to be a member of the MPC is quite attractive. If you are working in the City or in industry, it might be less so. You need those conflicts to be managed. I do not see a ready answer. I think it has worked.

I worry about a seriously populist Government wanting, in a sense, to manage the Bank of England in a way that has a slight—I do not want to single out Turkey, but let us say Turkish disposition. The terms for members of the MPC are quite short—three years—so with time you could pack the committee. The Bank ultimately appoints the governor and the deputy governors. We have quite a lot of deputy governors nowadays. There is that potential, which is why we rely on Parliament, on the Treasury Committee. However, if you had a deeply populist Government, they might pack the Treasury Committee, and we rely on the Court to cry foul if it feels that the Bank of England is being given a lot of people who are not up to the job.

That is a risk. I have not witnessed it. I have been generally pretty impressed by who Governments have appointed to the committee, but the potential is there.

Q201 Lord King of Lothbury: Sir John, could you comment on the question of conflicts of interest? The Court took responsibility for being in charge of this, because it did not want the executive of the Bank to feel that it had some power over the part-time members of the MPC. In your experience, did you ever have difficulties with conflicts of interest?

Sir John Parker: Not a single issue officially came before me.

Lord King of Lothbury: The Federal Reserve has obviously had embarrassing conflicts in recent years, but it was not an issue in your time.

Sir John Parker: It was not an issue in my five years at that time.

Lord King of Lothbury: Would either of you want to change the length of appointment or way in which the appointments process is made?

Sir John Parker: As you will be aware, Lord King, we certainly we had serious discussions between us in the wider Court after I started to chair the Bank for a period of time, and it was all about its effectiveness. One issue was very clear: that 16 non-executives was much too large a number to govern effectively, plus two deputy governors and the governor, so we had 19 people around the table plus a number of executives attending. To me, that was certainly not an efficient machine.

Secondly, the non-executives had a random skill set. In a plc, I spend a lot of time creating effective boards by ensuring the widest possible skill set and experience I can find in order to deal with any issue that might walk through the boardroom door. This was not the case in the Bank and, in discussion with the governor, we agreed that we would raise this with

Gus O'Donnell at the time. Another important point is that we had no part in defining the skill sets we needed or in taking part in any of the interviews. We had hand-me-downs, if you like.

We had very fruitful discussions with the Treasury. It was agreed that the governor and I would specify their skill sets when a vacancy occurred on the Court and that, in turn, I would take part in the interview process—shortlisting and being in the recruitment interviews. I did that alongside the Second Permanent Secretary, who at the time was Jon Cunliffe. That was a very fruitful process, because gradually you could see the shape and skill set of the Court changing from the arbitrary skill set that we had.

In the recruitment processes for all these areas—I know we may raise this issue later, and Lord Macpherson has already touched on it—when it comes to deputy governors, for example, there should be a proper process that is well defined. What are the criteria? What is the process by which we will go about interviewing, and what are the processes by which we will make the final interview and the appointments?

Lord King of Lothbury: Lord Macpherson, any further comment?

Lord Macpherson of Earl's Court: Focusing on the MPC, you can make a case for the appointments being longer, with four-year terms. There is an age-old debate about the length of the governor's and the deputy governors' term. I do not feel strongly. It is a pity if you have a good governor but they can only do eight years. Sometimes it is good to get 10 years out of people, but these are difficult issues.

The problem always arises when it comes to reappointment, which can become quite a difficult issue. I can understand why the coalition Government introduced an eight-year term for the governor, but I do not feel strongly about it.

The Chair: Would you change that?

Lord Macpherson of Earl's Court: There is no right answer to this question.

Q202 **Lord Davies of Brixton:** This bears directly on what you have just said about the skill set, but it raises broader points. It has been suggested by a number of people that there are too many ex-Treasury officials as deputy governors. Does this affect the independence of the Bank, which is the real master? Also, it has been suggested—I will not say by whom—that the Treasury is acting as a prep school for the Bank. Can you comment on these suggestions?

Sir John Parker: To some extent, I have almost dealt with it but, first, let me say that in my time there we had only two deputy governors. I think there are four now. At one stage, we had two from the Treasury, but we also had a period when there was one external and one from the Treasury. I think that was how it ended. I felt that the balance of having

external versus Treasury was good, because having diversity of thinking is very important.

There is a lot of talent out there, but I accept Lord Macpherson's view that conflicts are difficult to manage in some cases. The sheer attraction of salary is also an issue. That cannot be ignored. We need a proper process. The Bank should have a formal nominations committee, if it does not already have one, that has clear procedures laid down for the Court, for members of the MPC and for the deputy governors—and, indeed, for the governor. That may be a difficult one.

I do think we are in an era now of much better governors in corporate life, and certainly for all boardroom positions there are very clear processes now in all well-run companies.

Lord Macpherson of Earl's Court: We should not be totally surprised if the Treasury ends up populating some of the Bank. We only have two big economic policy institutions in this country: one is the Bank of England, the other is the Treasury. You only have to look at France. Jean-Claude Trichet was head of the French Treasury. He went on to run the French Central Bank and then the European Central Bank. My old friend Dr Carney was the senior official at the Canadian Finance Ministry. I reiterate that I do not think the Bank needs so many deputy governors. In having so many, I think they have slightly diluted the importance of these roles.

I would also make a prediction, not least because of this committee's work, that the next deputy governors are unlikely to be from the Treasury because, like in other fora, the Treasury is running out of people to put into the Bank, not least because it has fired perhaps one of the best equipped to do a senior job at the Bank of England.

Lord Davies of Brixton: That is clear and helpful. Neither of you has responded to the question: how does this affect the independence of the Bank?

Lord Macpherson of Earl's Court: I do not think it impacts very much. I do not think that someone like Jon Cunliffe or Rachel Lomax would come back to the Treasury and take instructions. Actually, Treasury officials tend to go native even more quickly than people from any other institution.

It is something to monitor. It comes back to my point about Governments potentially packing the Bank's committees, but it can be overemphasised. I can remember Ben Broadbent leaving the Treasury over 30 years ago. He is far more of a Goldman Sachs man than a Treasury man. You could talk about Goldman Sachs colonising the central bank, but it is the equivalent of saying that I am some creature of the CBI, which I worked for 40 years ago, although I should probably be embarrassed to mention that now.

Sir John Parker: I do not disagree with Lord Macpherson's analysis. I think you should keep these ranks as tight in numbers as you can and make them the pinnacles that people can aim for. That includes the good economists in the Bank. To me, offering a career that takes someone from university into a deputy governor role should be kept at the forefront of mind. Internal development and internal promotion are a healthy thing in any organisation.

The Chair: That is a neat segue into Lord Griffiths' question.

Q203 **Lord Griffiths of Fforestfach:** Do you think there is groupthink in the Bank? From one point of view, you have made it very clear that there is no groupthink on the MPC. People express different views and vote differently. Fine. On the other hand, the Fed, the ECB and the Bank of England all got their forecasting wrong. They all used this new Keynesian model. Even on the MPC you get the feeling that the one thing there is groupthink on is that money does not matter. You get the feeling that it is not discussed that much at MPC meetings. At least, the record does not suggest that it is discussed that much. If you felt that, should there be some way of ensuring that there is intellectual diversity, particularly on the MPC?

Sir John Parker: I think that is an economist question.

Lord Macpherson of Earl's Court: Let me have a go. I think the problem with groupthink has been across all central banks. Central banks tend to meet down in Basel and violently agree with each other about the way forward. I am not a monetarist; I do not believe that there is some inevitable link between some measure of the money supply and inflation. However, money does matter. If you print enough of it you will get inflation.

I was always worried not about the first batch of quantitative easing but about the second and third. I cannot remember if there is a fourth, although there almost certainly was. I once compared it to heroin. The economy gets addicted to it and needs bigger and bigger fixes for it to have an impact. However, once long-term interest rates are down to some absurdly low rate, whether it is 1% or whatever, QE will not make any difference, but it does leave money floating around, which I do not think caused inflation but did enable it to take root.

It is important to have a diversity of views, but one of the problems, and we saw this with financial stability, comes after a long period of low inflation and stability. I have a theory that it takes two generations to repeat an outrageous policy error, and probably one generation just to repeat a common or garden error. We had low inflation for so long that central banks just deluded themselves that it was bound to come back to target.

In a previous evidence session, I think Lord King posed a question—I cannot remember who answered—about the Bank of England's models, which always seem to have inflation coming back to 2% within two years.

The Treasury historically has some slightly strange model of the economy to do with the output gap, whereby you always return to trend in the long run. These are useful devices to check your thinking, but they certainly should not drive your thinking. Therefore, having economists on the MPC who have sufficient intellectual confidence to challenge some of the assumptions is important.

Sir John Parker: I think the groupthink is a challenge for most boardrooms. To me, the only way to address it is to come back to the point I made earlier: that you try to recruit the widest possible skill set, including a number of people who have domain knowledge applicable to your business and who understand your business and go about understanding your business over time. That is one.

The second is to have diversity of gender, including ethnic diversity. In my experience, both change the dynamics in a boardroom and you have people coming at issues from different angles. You then set up a situation where there is likely to be more challenge in debates than there is when it is all male and pale sitting around the table.

Q204 **Lord Turnbull:** Sir John, you quoted with approval Steve Nickell's maxim that there is no pressure for consensus. I wonder whether in the end we got too much of it. Particularly in the period 2019 to 2021, were there enough people expressing different views. Looking at the voting records, by and large there was not much difference in how people voted until quite late on. At that point, we could have done with a bit less consensus.

Sir John Parker: I am obviously not a student of that particular period, but I understand what you are saying. I said earlier that there were significant challenges in this period. You are talking about 2021 to 2023.

Lord Turnbull: I was talking about slightly earlier—2021.

Sir John Parker: Obviously there is a lot of debate about whether the Bank should have acted earlier. However, I can see that, certainly from 2021 onwards, there were a number of real issues that may well have been exceptionally difficult for a forecaster to pick up. I am not trying to make excuses, but I think that is the reality.

Lord Griffiths of Fforestfach: Who would you suggest arguably carried the can for ensuring that there was this intellectual diversity? Where does the buck stop?

Lord Macpherson of Earl's Court: It partly stops with government.

Lord Griffiths of Fforestfach: Do you mean the Chancellor, the Permanent Secretary—?

Lord Macpherson of Earl's Court: The Chancellor needs to appoint people to the committee who will have both the diversity of thought and the intellectual self-confidence to stand up to any emerging consensus. I can remember attending, as a Treasury observer, meetings of the committee back in 2008, and some members had very different views

from the mainstream. I expect they were slightly infuriating to work with, but they did set out different views, some of which proved to have some insight.

It is also to do with the governor setting the tone of meetings. I can think of one governor who was prepared to be in a minority, because on the face of it, from my perspective, he believed passionately in one person, one vote, and he did not think it undermined the credibility of the institution for him to be in a minority.

Possibly in the last decade, partly because interest rates hardly ever moved, a different culture may have set in, but I have not been privy to recent discussions. I cannot say that with any confidence.

Lord Davies of Brixton: Can I just ask a factual point? You said that you were a Treasury observer. Is that a speaking observer, or did you just sit there and listen?

Lord Macpherson of Earl's Court: I generally listened. I did not think it was my job to try to influence the debate. Far from it. There was the odd occasion when, given what the Government were planning to do either in a forthcoming Budget or in the context of financial stability interventions, it was perfectly reasonable for the Treasury observer to speak up.

Q205 **The Chair:** Lord Macpherson, if you are the Chancellor sitting in No. 11 and you have grave misgivings, or just misgiving, about how the Bank is handling inflation, and you think it has either been too devilish or too hawkish and you want to express the view, how do you express it, or do you just stay completely schtum?

Lord Macpherson of Earl's Court: It is very dangerous for Chancellors to give a running commentary in public. In my experience, that conversation would play out—it did not really play out in public at any point that I can remember—in the context of the regular informal meetings between the Chancellor and the governor. Sometimes it might even involve the Prime Minister. Those meetings tend to take place far more regularly when things are going badly. There is plenty of scope to share views.

Again, I think I was fortunate in that, although occasionally in my time relationships got a bit edgy, those conversations always seem to go reasonably well and you achieved a level of understanding.

The Chair: I ask because, when the Chancellor writes back to the governor on the governor's letter, the Chancellor is often commenting on the governor's assessments. If in private they are saying, "I have misgivings", but in public they are saying, "I stand with you", does that just go with the territory of independence?

Lord Macpherson of Earl's Court: Very much so. Things have to get very bad indeed for a Chancellor to start saying in public that he disagrees with the governor, and that gives the governor a lot of power.

We discussed things like appointments. Governors have a lot of influence on appointments. Chancellors have to accept where the Bank is taking you. We saw only last autumn, when, as I understand it, the incoming Government did quite a lot of briefing ahead of taking office, that it had big consequences in the market. My guess is that Chancellors will be even more cautious in the years and decades ahead.

Q206 **Lord Blackwell:** We have been talking about what Chancellors say—or you have, Lord Macpherson—but from a business perspective, as you know well, Sir John, one is very cautious about what one says in public, particularly about anything that relates to forecasts of future performance. In the Bank—indeed, in all central banks, but maybe particularly the Bank of England—there is not just the governor's but other voices all the time.

Sir John Parker: Yes.

Lord Blackwell: Do you think there is too much communication, or confusing messages?

Sir John Parker: From a business perspective, I have always found the publications of the Bank extremely useful documents, particularly the financial stability quarterly. I loved its fan chart and so on. Over the years, I have always listened to governors' comments at that time. What is not helpful is individual members of the MPC getting themselves involved in commentary through the press. It should be a collective and, unless it is sanctioned by the governor for an independent member to make public statements, it should not happen. I think it can lead to confusion.

Lord Blackwell: The other side of the coin is that, under the last governor, the Bank went for forward guidance. One issue that has been raised with forward guidance is that once the governor has pronounced forward guidance it makes it potentially more difficult to have an open debate about different policy. Do you have any views on that?

Sir John Parker: I think that, if it is made public, it tends to harness the MPC in many ways and you creep away from independence.

Lord Macpherson of Earl's Court: There is a place for forward guidance in the toolkit of central banks, but it needs to be used carefully. More generally, discipline in communication is really important. Clearly, members of the MPC should be allowed and encouraged to make speeches to explain why they think what they think, but they should not be second-guessing the next interest rate increase.

At the apex of the system, it is really important that the governor, and if necessary the chair of the Court, ensures that there is discipline. In my time, some members of the committees and some members of the executive were rather more forthcoming than others when journalists got in touch. Iron discipline is necessary when dealing with something as important as monetary policy.

Q207 **Lord Londesborough:** Just on the subject of talking too much, do you think the Bank's authority and operational independence were compromised when, back in January, the Prime Minister personally pledged to halve the rate of inflation from about 10% to 5%, interestingly at a time when the Bank was forecasting a rate of 3%? It sends out very confusing signals to the market and the public, does it not?

Lord Macpherson of Earl's Court: I was slightly confused by that. The Government sets the remit. It is the job of the Bank of England to deliver it. To be fair to the Prime Minister, I think he thought he was making a pledge that he was very confident he would meet. Theoretically, he has some control over inflation in the short term. He could cut excise duties a huge amount, or whatever. Personally, if I had been there, I would have advised him against, but I am quite sure he would have ignored my advice.

Q208 **Lord Rooker:** I have to say that in 1997 when I went into government, only as a Minister of State, it was a surprise to me that the Government ran themselves by correspondence. The number of times we had to get our letter approved by the planned recipient before we could send it was a bit of a shock to some of us who had not been on the inside before.

I also should say—going back to deputy governors who are ex-Treasury—that, in two of the departments I was in, the Permanent Secretaries were John Grieve and Rachel Lomax, and while they were classed as Treasury they had been out doing other things. I think that is an important point to make.

Back to correspondence and the role of the governor in the formulation of the Chancellor's annual remit letters. Should the governor have a role?

Sir John Parker: If I were Chancellor, which I will never be and have no ambition ever to have been, I would be sitting down with the governor and discussing what role he wanted the Bank to perform, because I think it is good man management. To rely just on a letter arriving on your desk is not quite the full shilling for me. Building the relationship between governor and Chancellor is very important. Then the letter can fly.

Lord Rooker: Lord Macpherson, it would be quite interesting if you could share what your role was at the time in the way the remit letter was constructed and then flowed around the system. That would be very helpful to us.

Lord Macpherson of Earl's Court: I agree. It is surprising how many things are written down and agreed before they are posted, but in this case it is quite important, because this can move markets. Picking up on Sir John's best practice, I think best practice was generally followed. You did not send a letter with a remit without having extensive discussion with the governor. Some Chancellors found discussing technical things quite difficult and they might remit it to someone like me to broker an agreement. In the case of Lord King, the process was usually quite easy, because he was a very reasonable person.

The thing that I would point out, because I have read some of the transcripts of previous discussions, is that the governor is quite influential. If the governor has something that he—because it always has been a “he”—is particularly interested in and wants the Treasury to put in the letter, the Chancellor is only too happy to agree to it.

What you have to understand is that some Chancellors are very political. They know that upsetting the governor could be threatening to their career and so they generally like to keep them happy. I have worked with some Chancellors where, when it comes to the Bank of England, the Treasury has a particular obsession—“This time we are going to tell the Bank to do this”—and when you say that to the Chancellor, the Chancellor just says, “I am not going to do it. I need to keep the governor happy”, because a happy governor is part of how you get re-elected. An unhappy governor, as you approach an election, can be quite difficult.

All of that is a long way of saying that generally—and I have not been close to recent remits—the remit reflects a lot of debate. I have here Gordon Brown’s one from 1998, which, because it was from Gordon Brown, was in big, 14-point type, as Baroness Liddell will remember. It is admirably short and to the point and it had an even shorter and to-the-point reply from Eddie George. By the time you get to the present day, it is getting quite a lot longer.

Gordon Brown was rather brief in describing the Government’s economic objectives. Now you have paragraph after paragraph about the Government’s economic objectives, although they are not hugely different from Gordon Brown’s. There has clearly been an evolutionary drafting system, usually based on the last letter, although I see someone very clever discovered a sentence—it was you, was it not?—which had been omitted from a previous letter. I am quite certain that was a mistake by the Treasury.

Sir John Parker: We have not seen the artificial intelligence letter yet.

Q209 **Baroness Kramer:** We are talking about the independence of the Bank of England, but would it not be better to issue a joint statement from the Chancellor and the governor rather than the myth of a letter that is an instruction from the Chancellor to the governor? I am thinking about public perception, public respect and perhaps even the attitude of the markets. “Let us pull the wool over the eyes of those who do not know” strikes me as something very outdated and not advantageous to any of the participants.

Lord Macpherson of Earl’s Court: There is something in what you say but you never know where economic policy in this country will end up. We live in a parliamentary democracy. It is really important, in my view, that a democratically elected Government can determine, in effect, the objectives of the unelected but very capable institution that is the Bank of England.

Personally, I think it is good that the Treasury and Bank of England understand each other at the point the remit is sent, but in the end it has to be owned by the Government. That is our system of independence. I personally prefer that to the alternative, where the institution sets its own objectives, in effect, which I think was true of the Bundesbank and the Fed to a degree.

There will be times when you want the governor and the Chancellor to be on the same platform, reassuring the world that they are on completely the same page, although the fact that they are doing that—it is a bit like football managers and votes of confidence; you generally do that when you are really desperate. Maybe I have been traduced by working with the system for too long but I think it is the least bad way of doing it.

Q210 Baroness Liddell of Coatdyke: It is interesting that you referred, Lord Macpherson, to the length of the letters from Gordon Brown's day onwards, because I am interested in the increase in the scope of the Bank's remit and its balance sheet. When the governor came to see us a few weeks ago he was talking about the fact that the Bank now had to have regard to a number of different issues, a number that started at about 35 and came back down to the mid-20s. I admit that I was a bit taken aback by that.

How do the mechanisms operate to keep the Bank to account and to scrutinise its operation, and are they effective? Climate change appeared in the list and we can argue about whether it should be there or not, but it seemed to have nature as well. That was one of the things that the governor was successful in getting out. If there is going to be this exponential growth in the remit of the Bank, how do you handle it?

Lord Macpherson of Earl's Court: I am a traditionalist. I like to keep things simple and generally have as many instruments as I have objectives—a brief reference to something called Tinbergen's law, which I will not trouble you with.

This is a classic point made by someone who has long since left the game, when it is easy to criticise the regime but what worries me is that at any point in time there is some new fad—not "fad" because it is really important—and it is tempting to add it into the remit. It is a bit like looking at the evolution of the Government's economic policy: you put in something additional about the environment, energy security, net zero or whatever.

I do not want to home in on climate change too much because it could be some other issue, but I do slightly worry. If you want to get to net zero, and you are the Government, why do you not slap on a carbon tax rather than trying to do it through regulation, through an organisation that is at arm's length? With the best will in the world, nothing the Bank of England does in the short run is going to make much difference to climate change.

I did declare my interest at the beginning. As someone who is at the receiving end of some of these requests—if you are a small bank, for example—it imposes a lot of work, most of which is pretty nugatory.

I would be quite cautious on extending remit documents. There is huge scope for culling some of the content. The Government need to be honest about what it is realistic for a central bank to achieve through indirect, regulatory intervention, versus direct measures that the Government are responsible for, which have the potential to have a very quick impact but successive Governments have—I cannot imagine why—steered clear of.

Baroness Liddell of Coatdyke: Is there a mechanism there, though, which ticks the boxes to say, “You have hit that one. You have hit that one. You have not hit that one”?

Lord Macpherson of Earl’s Court: What happens is these things get updated every year and generally there is some new salient issue. For example, this year you have to mention, “As the world deals with the impact of Putin’s war in Ukraine”. That looks like some sort of formulaic epithet that no doubt every letter from the Government starts with.

It is important to the Government because they think lots of people read these documents. Actually, they do not. Very few people read them. I think someone referred to a Christmas tree effect. You get these additions. I am not sure that people take a huge amount of notice of them, especially when they have a primary objective, because a primary objective should trump everything. Price stability is very much there. It gets more difficult with the Financial Policy Committee—I have the document here—and the Prudential Regulation Committee, where it gets really long. I am glad I am not on one of those committees because I would not know how to deal with all these “with regard to”s.

Q211 **Lord King of Lothbury:** One of the governor’s concerns in all this was less about the substance, because you have a primary objective and you may not need to spend too much time worrying about the “have regard”, and more about judicial review. Unless they could demonstrate clearly that they had done a lot of process work to “have regard for”, then the decisions might be subject to judicial review and set aside. That has obviously happened in other government decisions. Is there not a real cost here to piling on “have regard”, when you add on the potential cost of having to demonstrate in public that you have jumped through the thousands of hoops that you need to in order to prove that you did have regard?

Lord Macpherson of Earl’s Court: I accept that if you are serious and take these “have regards” seriously, the logic of the governor’s position is correct.

The Chair: I find this subject intriguing. Maybe, Sir John, you would like to answer. Do you think that the Bank is suffering from mission creep?

Sir John Parker: All organisations, unless you keep discipline from the top, will naturally have a gravitational pull about them and end up not exactly where you necessarily want them. You have to be very careful at the top of any business in ensuring discipline on the strategic priorities. I am with Lord Macpherson: you should try to keep things simple when you

are talking about strategic priorities for any organisation. If you keep it simple, people cannot do the barn dance in front of you to avoid the core responsibilities of their job. If you give them a great, wide scope, they can dance around it. Holding people accountable is possible only if you keep clear definition of priorities.

Lord Macpherson of Earl's Court: Just to add to that, rightly or wrongly, the Bank of England was given far broader and deeper responsibility for both prudential regulation and the macroprudential regime back in 2010. That in itself was a massive expansion of mission, which is a perfectly reasonable thing to have done, but it doesn't half take up a lot of time just meeting the simple aspects of those remits. The problem with any institution that is successful—and you see it a bit with the OBR—is that politicians attempt to give it even more things to do, which sows the seeds of its destruction. To put another thing on the table: for example, if the Bank were to develop a central bank digital currency I could see that potentially bringing the central bank into the private sector banking space.

You have to be careful what you wish for in this space. Keeping a lean, fit central bank that is focused on the things it can control, with the necessary instruments, is, in my view, the most important thing to stick to.

The Chair: Just picking up on your points about accountability, you said that you are not sure that many people even read the letter and I think you are probably right about that. Do you not think that, given the importance of the position that the Bank holds, the letter should be raised in prominence—for example, by there being an annual statement to Parliament and a debate on it—just so everyone here has the opportunity to understand what the Bank is being asked to do and there is an opportunity to hold the Chancellor to account for what he is asking them to do? Would that not be something material we could see happen, or would it make no difference at all?

Lord Macpherson of Earl's Court: It could make some difference. I think in the good times people would just think, "This is a waste of time", and they would not turn up for the debate. In the bad times, they certainly would. It is one thing you could do among many.

The Chair: Sorry, what are the other things you could do, if there are many? If there are many, I am interested to—

Lord Macpherson of Earl's Court: Now you are going to talk about accountability and there are all sorts of things around the margins you can do.

The one point I would make is that people do generally understand the inflation target. They might not read the letter but they know there is an inflation target of 2%. Yes, it was originally 2.5% and RPIX. Basically, it has remained unchanged for 25 years and how it is articulated in broad terms has remained unchanged. That is deeply embedded and, until

recently, expectations across the whole economy were consistent with this: that it would come back to 2%.

I may have been unfair about the letters. I read the financial stability letter and the prudential one yesterday for the first time in many years. Those are far more difficult to embed in people's consciousness.

Q212 Lord Turnbull: In the 1998 settlement, it looked very clear and simple: that there was monetary policy and fiscal policy. The Bank did monetary policy and had an instrument, which is the interest rate, and the Treasury had fiscal policy, emphasised by the fact that the management of the debt—this it is how it was funded—was transferred to the Treasury. They each have their domain and they do not get in each other's hair.

Probably even from the start, this was an illusion. Both these things affect demand, although they do it through different transmission mechanisms, and they both have distributional effects. There are winners and losers from how it is done.

Nowadays, we find that this simplicity seems to have crumbled, or maybe realism has come in, helped by the fact that the Bank now owns half the Government's debt. The question of how you co-ordinate monetary policy and fiscal policy has become a lot more complicated. We do not see those processes. They are not public in the way the MPC is. There are no minutes published. How do the two institutions go about making sure that, as far as possible, fiscal and monetary policy work together, or, as in the LDI case, a very special short-term exception is made? How is that co-ordination done?

Lord Macpherson of Earl's Court: For most of the 25-year period, fiscal policy has been set in a medium-term context. It has not been used to increase demand or reduce demand, for the very good reason that trying to use fiscal policy as a way of influencing short-term economic activity is very difficult because the lags are long and variable. When interest rates were well above zero, I think it is fair to say that everybody was very happy to leave it to the Bank to seek to influence short-term demand. Generally, for most of this period, the system has worked very well.

From time to time, the threat to inflation, or most of the time to economic activity, is such that fiscal policy has to be more activist. I can remember being sent by Alistair Darling—I think I took the then chief economic adviser, Dave Ramsden, with me—to talk to the then governor and deputy governor about what a sensible Budget would look like to support what the Bank was doing in late 2008 or early 2009. That was a classic co-ordination problem where we wanted to ensure that the Bank was happy with the sorts of things we were contemplating doing. I can recall having a very sensible conversation and we went away aligned. Latterly, it has become more complicated because of QE. I do not think, operationally, QE is that complicated. The Bank and the Treasury, through the Debt Management Office, have co-ordinated interventions very sensibly so that they do not disrupt the market.

What you have highlighted, in a sense, is: "What are the short-term objectives of fiscal policy and monetary policy? Are they consistent?" and so on. This was after my time. If I could have been a fly on the wall just after the Brexit referendum or just at the point that Covid became a big issue in March 2020, I would be interested to know what conversations took place between the Treasury and the Bank of England, but I recognise that you are in more difficult territory, and the risk at that point is about perception as much as reality.

I remember that, in 2020, the quantum of QE chosen by the Bank was broadly the same as the quantum of fiscal support announced by the Government. In my mind, that set alarm bells ringing, not so much because I thought we were going down some dangerous path of monetary financing, although in one sense we were, but because of the appearance that somehow the Bank were doing the Government's dirty work for them: that is, funding the massive increase in borrowing.

Lord Turnbull: You have a choice. At any time, you could do some more QE and let the total go up, you could just put it into run-off and allow things to mature, or you could start to tighten. You have all sorts of quantum to each of these. Where does that decision get taken? Who first puts forward a proposal: "We think that in the next year we should be doing X"? Does that tend to come from the Bank or the Treasury?

Lord Macpherson of Earl's Court: In my time, the Treasury was very disciplined on this. It did not interfere at all. We agreed, in effect, to support whatever the Bank chose to do. There was an exchange of letters, and I think we gave them a guarantee. There is a debate about why the guarantee has not been published; I do not know why it has not been published, because I do not think it contained anything interesting at all. We had a system and the Bank got on with it. If it wanted to do more, it asked for a further guarantee. We gave it that as a matter of course.

My belief is that that is how it has continued. I do not know what happened in the Kwarteng-Truss period, but I do not think at any point the Treasury has tried to define the quantum or indeed the policy. Sometimes I rather regret that. I always rather favoured a policy of just letting QE run off automatically as debt matured, but that was too imprecise for the Bank of England.

Q213 **Lord Blackwell:** Can I pick up, Lord Macpherson, on this point about co-operation or interchange between the Bank and the Treasury? As Lord Turnbull has said, they are both operating in the same space in terms of aggregate demand, although maybe on different timeframes and with different distributional effects. It would seem common sense that you would want to optimise that by conversations and exchanges of the sort that you describe going on during your period as Permanent Secretary.

You were also Private Secretary to the Chancellor in the period of Ken Clarke, before independence but after the setting of an inflation target, which some people would say has been the real change in this. Is the

nature of the conversations and the co-operation between the Bank and the Treasury any different now than what it was in the 1992 to 1997 period?

Lord Macpherson of Earl's Court: Yes and no. Yes, very different. This is the Bank's decision. In the Ken Clarke era, the governor would advise and the Chancellor would decide. The reality is that the difference between the two was pretty small. Usually there was a quarter of a percent in it, in terms of the difference between the governor's view and the Chancellor's view.

In my view, the clarity achieved by the post-1997 regime created greater credibility. That was observable in the long-term cost of borrowing from that point onwards. It was not that Ken Clarke was wanting to be devious; it was just that there was a perception that he might be devious if he was running up to an election. I attended every monthly monetary meeting over the period the minutes were published, as I expect Mervyn King did in his role as the chief economist, including our last meeting in Nottingham, the then Permanent Secretary refusing to let Ken hold it at Trent Bridge because that was in his constituency.

Q214 **Lord Blackwell:** You have talked about the fact that the Government are a democratically answerable body. The Bank is independent; it is not elected. Yet the Bank's policies can have a profound impact. They can cause a recession. They may well be in the course of causing a recession. Do you think there is sufficient democratic accountability? We have appointed this group of experts who can then claim independence. How do we hold them to account for the vast power they have over the economy?

Lord Macpherson of Earl's Court: That is an important question for every country that has an independent central bank. There are different ways of doing it. I think accountability is reasonably strong in this country, partly because the Government set the remit and appoint the people, and sometimes reappoint them—or not, as the case may be. Most importantly, the Bank leadership is accountable to the Treasury Committee, which regularly meets with them and asks them to account for themselves.

In an ideal world, I would like to see a stronger Treasury Committee that was better resourced to enable it to ask the questions it needs to ask. The appointment of the chairman of the Statistics Authority has to be approved by the relevant committee. That committee has a power of veto over the chairman of the stats authority, and indeed exercised it at one point. You could give the Treasury Committee a power of veto over appointments. Especially since I have become a very minor part of this great Parliament, I am in favour of parliamentary democracy, so I would be inclined to give the committee that power.

Q215 **Lord Blackwell:** Sir John, in your business roles you are very clearly accountable to shareholders. When you were chair of the Court, who did you feel accountable to? Did you feel accountable?

Sir John Parker: It is a very good question. First of all, I felt an accountability to the Treasury at the end of the day because of the relationship with the Permanent Secretary. In a way, it seems strange that the chairman should have an accountability to the chief executive, but because of the special role that the governor played relative to government and the public, and his reporting on behalf of the Bank of England to the Treasury Committee, which I think he attended about 100 times in his role as governor, I felt that I had a duty to perform the task in the operation of the Court in support of him in that role.

There were many things that we were involved in. You may read our annual reports, which involve statements from the governor and me. I read a few of them the other day and I was amazed at the extent of work and reform that we actually did. I used to read in the newspapers that Lord King was not very keen on reform, but that was certainly not the case in practice. I can think of the introduction of the strategic debates in Court on every element of the organisation, setting them strategic targets, holding them to account in due course, and tackling things like the defined pension scheme, which I think government has shied away from. We managed, with a lot of hard work, to change that to a defined contribution scheme, which was not easy. There were big, major issues like that that we did tackle.

When the 2008-09 crisis hit, we had to establish a subcommittee of the Court in order to deal with emergency funding for the institutions that finally got into trouble. I, the governor, two deputy governors and the chair of the other two committees—remuneration and audit—did that job. I remember that on one particular day we were at the Bank, I think, three times. A lot of work was involved, and a lot of reforming work. We also had a third party carry out a board performance assessment three years in, if I remember correctly, which was very new in the Bank of England world.

Q216 Lord Londesborough: Coming back briefly to the subject of QE, what are your thoughts on the view that the levels of QE and the size of the Bank's balance sheet have, first, served to compromise the Bank's independence by blurring the lines between monetary and fiscal policy and, secondly, served to damage the Bank's credibility in its fight against inflation?

Lord Macpherson of Earl's Court: I do not think that QE intrinsically caused those problems. It is more that it has increased the risk of the Bank's independence being compromised.

As I said earlier, I think the first round of QE was really quite effective. I have my doubts about subsequent ones. The point I made at the beginning about the remuneration of reserves held by clearing banks at the Bank of England, I do see as a potential source of conflict in the future. I recall the investigation by this committee about 18 months ago where highly credible commentators suggested that reserves should no longer be remunerated at the prevailing interest rate. If the Treasury was

to stop effectively underwriting the Bank's losses on quantitative tightening, that could create a dangerous period in the Bank's status.

Lord Londesborough: Lord Macpherson, coming back to your analogy between QE and heroin—needing ever-increasing fixes to create a high while negative side-effects increase—you tweeted back in 2017, not that I track all your tweets, that it was time to move on. Well, there were another four years of QE. What were your particular concerns about the side-effects?

Lord Macpherson of Earl's Court: The side-effects—we have seen them—are in asset price inflation. Lord Turnbull earlier raised the issue of distributional effects. It is not the Bank of England's role to worry about distributional effects, it is the Government's, but Governments tend to be a bit pusillanimous when it comes to dealing with gains, especially those that go to the rich.

I just think that we have seen more asset price inflation than has been desirable. I am not claiming there is some great relationship between asset price inflation and the consumer prices index, although I suspect in the long run there is some relationship. I am just worried that QE has given windfall gains to a section of society who, quite frankly, do not need those windfall gains, potentially at the expense of poorer people who have suffered the effects of inflation because they spend more on food, on energy, on rents and so on.

I am not against QE in principle. When you are down to zero interest rates, you need new instruments to affect demand, but I fear that we went too far. Suffice to say, no one took a blind bit of notice of my tweet, but it is very nice that you have picked it up.

The Chair: Do you think there was sufficient accountability and scrutiny of that phase of QE during Covid?

Lord Macpherson of Earl's Court: Yes and no. There was some scrutiny. I am quite certain that the governor appeared before the Treasury Committee. We are definitely applying hindsight here. At the point Covid started, we had no idea where the economy was going to pick up.

The Chair: Sorry, let me rephrase the question. Given what we now know about the impact of QE, how can we improve accountability and scrutiny, were that kind of tool to be used again?

Lord Macpherson of Earl's Court: I think all parliamentary committees need to be very focused on the statement that accompanied the original QE. My recollection is that on both occasions it was presented as an emergency measure. The critical question is: when do you cease to be in an emergency? After the Brexit referendum, the world did not come to an end. The following week after the Brexit vote, life went on much the same as before.

That emergency support could have been framed far more like the intervention last autumn with the LDI. You intervene rapidly to deal with the disruption in the disorderly market and then you withdraw the support. That is the classic central bank role. But dressing it up as QE and then leaving it on the table, not even withdrawing it when the gilts matured, was an asymmetric response.

In terms of accountability, Parliament should have been very focused on this. To be fair, you did a report on QE not long after the event, so clearly it has gone on, but maybe parliamentary committees need to raise the volume.

Lord Layard: You mentioned the House of Lords Committee that did that. Some people have said that the Treasury Committee does not embody enough professional expertise, and somebody has suggested that the parliamentary body to which the Bank should be accountable or to which it reports should be a Joint Committee of the Lords and Commons. Do you have any view on that?

Lord Macpherson of Earl's Court: As a Member of the House of Lords, I should obviously be very much in favour of that. The problem comes back to democratic accountability. It is the House of Commons that is elected, and if it has faults it should sort itself out, and the Government should support the committee system in sorting them out. I fear they will not. It would be fantastic to have a committee that featured the likes of Lords Layard and King, and indeed all the other eminent Lords and Baronesses around this table, but I fear it may be a bridge too far.

Q217 **Lord Layard:** Sir John, could we go back to the role of the Court? I suppose the basic question is: should it have a somewhat wider role? You have made one or two remarks that have suggested that, and perhaps we could pursue it a bit more systematically.

We had evidence from Sir Paul Tucker—I do not know if you have seen it—which covered that issue. He says that “except where powers are conferred by Parliament on particular bodies such as the MPC, FPC and so on, all the Bank’s powers are best viewed as vested in the governor and company. In other words, that is the Court of Directors, which reserves a few things for itself such as signing off on budgets but otherwise delegates everything to the person of the governor”.

That means that it is delegating things such as the role of the Bank as lender of last resort, and so on. He says that instead of it being left to the governor, “It would be far better if there were a formal executive board”. Could you comment on the general issue of roles within the existing system and, separately, the idea of an executive board?

Sir John Parker: If you have an executive board in any organisation, you end up talking to yourselves. The most important point is that it would be at odds absolutely with modern governance in corporate life, where non-executive directors are responsible under the law to the same extent that executive directors are, and carry the same can. That same structure should apply in the Court. Maybe there is a case for examining

what should be under the responsibility of the Court, beyond what is already specified in statute. Perhaps that should be reviewed in the future, given that the shape of things keeps changing in the Bank. That should be considered.

Also touching on Lord Blackwell's earlier point, there is the whole issue that in plc life our shareholders ultimately have the right to sack you as an individual director by voting at an annual general meeting. There is no such mechanism for an individual in the Court. To some extent, we may need to have stronger assessment of performance of the individual directors than we have. They are appointed for a five-year period, and perhaps there is a case, two years in, for reviewing their individual performance.

There are a number of improvements you could introduce in this area to align more with modern governance practices, but certainly I would be opposed to the concept of an executive board. By all means an executive committee, but reporting back to the board as a whole. That did happen in practice, in any event. The governor would report monthly, at that time, on all aspects of the Bank operation, as well as individual executives coming and speaking about their area of the Bank. We had an opportunity to interrogate the executive in the way you would have in a plc.

Lord King of Lothbury: I recall some of Sir John's earlier evidence that the Court did not delegate the power to launch lender of last resort operations to the governor alone. The Court delegated it to a special subcommittee of Court. All lender of last resort operations, because they affect the Bank's balance sheet, have to be approved one way or another by the Court, but since they were happening so frequently the special committee was set up to do it. It was not given to the governor as an individual decision.

Sir John Parker: There was a remarkable amount of accountability between the executive and the Court, way beyond that which is expressed in statute.

Q218 **Baroness Kramer:** The question that is allocated to me, in a sense, picks up some of that theme, because I wanted to ask about the Independent Evaluation Office. Let us set aside the word "independent". I want to explore that in a moment. My understanding is that this was initially set up to provide data resource analysis to the oversight committee made up of the non-executives on the Court so that they could hold the executive more effectively to account and question independently, and that continued until Lord Bridges, in his wisdom, eliminated the oversight committee.

The Chair: Do not let us go there. Let us move on.

Baroness Kramer: That is when we first got to know each other. In 2014, I note that the Independent Evaluation Office did a pretty substantial report on the issues of forecasting and data of the Bank—

exactly the same issues, it would seem, that it is being asked to report on today by the current chair.

One of my questions is: did anybody take a blind bit of notice of the recommendations that it came up with? They do seem to have a rather ghostly echo to them, suggesting that the Bank should learn more from other forecasters and models and more systematically from the past, and that it should challenge conventions more, take more steps to introduce greater challenge to forecast conventions, and so on. If it was not listened to very much then, is anyone is going to listen to it now?

Lord Macpherson of Earl's Court: These changes took place relatively recently. I was still Permanent Secretary when the oversight committee was abolished and this institution produced its report. I should remember it, but the fact that I do not—

Baroness Kramer:—says it all, does it not?

Lord Macpherson of Earl's Court: —suggests that it did not land in quite the way it should have done.

Like Sir John, I am not really in favour of an executive board. I think having a unitary board works relatively well, especially now that it is a smaller board, but a critical role of any board is to ensure that the institution learns the lessons of both successes and failures, the better to help future generations.

I cannot remember why the oversight committee was abolished. I suspect the Bank of England wanted it abolished, so it was an easy win to give for the Treasury. I cannot remember the Treasury having any agenda on the subject. In fact, I was always a rather fan of the oversight committee as a way of very mildly, just occasionally, challenging the executive to understand why things turned out as they had.

I have read the evidence. I am told the people who work for this office are very good. My view is that it should probably be strengthened in some way, because it could genuinely be helpful. Whether it should be detached from the Bank of England and live in some sort of space like the OBR does in relation to the Treasury, I do not have a view on at this stage, but it is definitely worth contemplating. Embedding a culture where you not only learn lessons but are seen to learn lessons, in any institution of this nature, is really important.

Baroness Kramer: Sir John, what are your thoughts on this? Maybe we should then roll in this issue of independence, as Lord Macpherson did, because, as far as I can tell, every member is recruited by the Bank of England and, in fact, most people who staff the office come from the Bank of England. It is resourced by the Bank of England, it is sited within the Bank of England, it carries out tasks that are commissioned by the Bank of England, and yet it stresses that it is independent. I think sometimes outsiders are brought in to join the crew when work is done.

Sir John Parker: It was certainly after my time, so I do not really feel qualified to speak about its effectiveness or otherwise.

Baroness Kramer: Would you have valued something like this as you were carrying through your role? If there was an independent body that could be tasked to provide particular expertise or analysis outside the framework of the Bank itself, would that have strengthened you in your role or perhaps changed a decision?

Sir John Parker: In any company you can always reach for some degree of expertise outside the boardroom, through consultancy or whatever, if you feel the need for that degree of support or analysis work. I always felt that there was sufficient talent in the Court. Having third-party challenge and review of the Court and its effectiveness is the most useful thing you can do in that role, in my view.

There is always a danger that we feel that we need another independent layer somewhere. If you recruit good people, make them responsible, clarify what you expect of them and hold them accountable for delivery, that, to me, is the way to run a modern organisation. Do not have too many fleas upon fleas upon elephants' backs.

Lord Macpherson of Earl's Court: Sir John has identified the trade-off here. In a sensible world, which I think has largely been the case, the Court would commission work on lessons learned, as indeed it did. There were three exercises, I think, in 2010-11 to learn from the crisis. That is one model. I would want the Court to have the power to initiate requests.

In one sense, creating an independent body gives you a bit of heft. If I was some professor of monetary policy at the LSE, working in this organisation or indeed running it might be really exciting and interesting, especially if it was well paid. The trouble about creating new, independent institutions, which are reviewing other independent institutions, is that you just get more bureaucracy. There is a tension there. I could see a case for it, but I am not strongly advocating it. Potentially, the interesting question is that it might blur accountability. I do not know whether this is the right way forward or not.

Giving Parliament the power to commission reports, as well as the Court, would be an interesting form of accountability. It is worth thinking about. As I say, I do not have especially developed views or have a strong position on this, but I think you are on to something that could add to transparency.

Q219 **Lord Turnbull:** Lord Macpherson has got to where I was getting to. What the IEO seems to lack is a customer, someone who really wants to see these reports. If you look at the list, there are not just forecasts but all sorts of issues in the Bank. I doubt that the Treasury Committee has looked at any of them. It is very interested in monetary policy and getting the Bank along, or financial stability. I would have thought that as part of its calendar it should be asking, "What has the IEO produced in the last year that we should be looking at?" I do not think it does. It is a

question of selling it to them as part of Treasury accountability.

Lord Macpherson of Earl's Court: I am quite certain the Court was interested in them, because that is what the Court does. It is very focused on these issues and generally it does a very good job. The problem, probably, in 2014 was that we did not have an inflation problem, and it is in the nature of committees full of politicians that they want to focus on politically salient issues. That is probably why this report did not really surface.

Lord Turnbull: An analogy. The CNAG does not necessarily go around looking for politically attractive subjects. It does its work and then it has a committee to send it to—the PAC. Between them they can get into the work of Whitehall. There does not seem to be anything equivalent for the work of the Bank, where the Treasury Committee could perform for the Bank what the PAC does for government departments.

Lord Macpherson of Earl's Court: As you may not know, some of us, much to the Bank's irritation, were involved in giving the National Audit Office a role in relation to the central bank, although sadly, since it was not allowed to look at policy issues, its role is rather circumscribed. I take your point. Having some arm's-length body that can evaluate policy, which has a higher profile than it currently does, is desirable.

Q220 **The Chair:** Thank you very much. We have covered an enormous amount of ground in one hour and 50 minutes, and we are all incredibly grateful to both of you. As a final question, just to sum up, we have touched on the remit, on accountability, on a whole range of topics. If you had to pick one of them that you would say we should be highlighting to improve the operational performance of the Bank, what would that be?

Sir John Parker: To me, it is a people organisation, and issues as to how you recruit people at every level are crucial. There should be well-defined criteria, and clear processes in who is involved at each stage, including up to the governor. You can define these things well, but really good governance is what should surround it. We want the best possible people in every slot and we want the broadest range of skill sets, from deputy governors right through the organisation.

Lord Macpherson of Earl's Court: I am having real trouble identifying one, but let me go with mission creep and really sharpening up. I think it was Sir John Vickers who described how many words were in the original genome; he said it was 900 words. I think making these remits clearer, with fewer baubles on them, would do the Bank of England a great service.

The Chair: Very good. Thank you both very much indeed. It has been a great session.