House of Commons

Treasury Committee

Oral evidence: Appointment of Dr Catherine Mann to the Monetary Policy Committee, HC 572

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Watch the meeting

Members present: Mel Stride (Chair); Rushanara Ali; Anthony Browne; Felicity Buchan; Emma Hardy; Siobhain McDonagh.

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Witness

I: Dr Catherine Mann, External Member of the Monetary Policy Committee, Bank of England.

Written evidence from witnesses:

Dr Catherine Mann's appointment questionnaire

Dr Catherine Mann's CV

Examination of witness

Witness: Dr Catherine Mann.

Q1 **Chair:** We now turn to Catherine Mann, appointed as an external member of the Monetary Policy Committee. Welcome to the Treasury Committee. Could you very briefly introduce yourself, please?

Dr Mann: Thank you very much for the opportunity to come and chat with you today about becoming an external member of the Monetary Policy Committee of the Bank of England. I am an international economist; it is the lens through which I have done quite a few different things over the course of my career. I have worked in policy at the Federal Reserve board of governors; that is where I started my career, and ultimately I was assistant director of the international finance division in Washington. I have also worked in policy more recently as the chief economist, head of the economics department and G20 finance deputy at the OECD.

In the interim between those two jobs, I had a stint at think-tanks and as a university professor with the Peterson Institute for International Economics in Washington, and then as the Rosenberg professor of global finance and director of the Rosenberg Institute of Global Finance at Brandeis University. That is my academic pillar, so I have a policy pillar and an academic pillar.

The job that I have just resigned is as the chief economist of Citibank—in other words, a private sector pillar, understanding the role of the financial sector in achieving the objectives of the real economy. So I have three pillars, policy, academic and now private, and I bring those three pillars together in service of the Monetary Policy Committee at the Bank of England.

Q2 **Chair:** Catherine, thank you very much and welcome. You have three pillars and a lot of roles. Out of interest, what did you find the most interesting in all those things, and what was it that you have done that you have learned the most from that is relevant to this role you are moving into now?

Dr Mann: From the standpoint of the three pillars, the essential ingredient is that in order to achieve better living standards for citizens, which I see as the objective of policy makers in general, the three pillars have to be working in conjunction and in a complementary fashion. We have to have policy makers on the fiscal side as well as the monetary side working in conjunction with policy makers who are focused on the regulatory climate. In other words, monetary policy, fiscal policy and structural policies have to be complementary in order to achieve the ultimate objectives of policy makers.

The ultimate objective of policy makers is also what is going to be most stable and successful for private sector investors. There is no conflict between achieving the objectives of policy makers for rising living standards of citizens and somehow making money in the financial sector. Ultimately, those two have to be complements, because if they are not, there will be some difficulties.

Q3 **Chair:** My question was which role you enjoyed the most and from which role you learned the most that is relevant to the post that you are taking up now?

Dr Mann: In all three posts, I am a professor; it is just that the clients or the audience are different, so the approach that you take as somebody who is trying to teach and to advocate for particular policy directions is what I did in all these positions.

In understanding the role of the financial sector in achieving the objectives of the Bank of England's monetary policy remit—price stability, sustainable growth and, I would argue, financial stability—and particularly how that changed over the last 10 years, I learned the most by going outside of my comfort zone of being an economist and explicitly into a private sector financial institution, bringing that knowledge of the role that the financial sector plays as the intermediary for monetary policy to achieve the objectives of inflation, growth and financial stability. More very important learning came from my three years there in understanding that intermediary role and its objectives.

Q4 **Chair:** You mentioned inflation and price stability. In the questionnaire that you very kindly completed for us—thank you for that—you focus to some degree on the possibility of weak growth and, therefore, downward pressure on inflation, but not so much on the risks of inflation taking off and becoming embedded. Could you talk us through that? Andy Haldane is preaching great caution and concern here, with a suggestion that the genie might get back out of the bottle and that a wage-price spiral is going on et cetera. Why do you think that that really is not going to happen, or is there a bit of you that does think there is a risk?

Dr Mann: When I think about the understanding of the inflation process, I really look at four elements and a lot of data associated with them. The first piece of the inflation process is understanding inflation expectations. We can look at data for businesses, financial markets and consumers, in both the near and the medium term. We can look at that and at how that is evolving over time.

The second element to the inflation process that is important to keep a handle on is to look at energy prices, or at commodities in general. Again, there is a spot price and a futures price, and looking at the dynamics of those two, as well as forecasts, is an important ingredient.

The third is understanding the labour markets, not only from the standpoint of unemployment rates and so forth, but understanding the wage-setting process and the extent to which what we see in that process is something that is systematic to have a boost, or whether there are other dimensions that are potentially putting some limitations on the ability of labour to get spiralling wage increases.

The fourth, and in some sense the most critical, question is looking at product markets. Do firms have pricing power—not just one-off but systematically increasing ability to raise their prices? Ultimately, inflation in the real economy comes from firms having pricing power to push through price increases. The systematic increase over time—one-off, one-off and one-off—is what we really have to look at.

Those are the four buckets of data that I look at. Within each bucket, we have to look at what the price level is. For example, there is a lot of concern about price increases right now in, say, aviation, used cars or hospitality, but if you look at the price level in comparison to two years ago, it is still well below where it was. There is inflation in terms of delta—the prices have increased—but the price level is still below where it was two years ago. We have to look at the price level, and at the delta or the rate of price increase from the base last year to where we are now. There are still a lot of base effects. In other words, the prices were very low last year, and so, even with normal price increases, you would end up looking very high this year.

We also have to look at a third dimension, which is something that financial markets in particular look at, and that is price momentum. We are looking at the rate of change of the price increases. For some of the most significant sectors or areas of price increase that people have been mentioning—again, I could use used cars as an example, but also some of the other price increases, even in housing—the momentum of price increases has come off the top, so that the underlying price trend, rather than being a spiral "up, up, up", has started to taper off. We see this coming through on some of the energy prices as well.

When I try to evaluate prospects for price increases and whether it becomes a spiral, which is what we would be really concerned about, I have a lot of information that is very disaggregated that I bring to the analysis. It looks at lots of different parts of the market to evaluate whether we are looking at something that would represent an inflation spiral to which it would be appropriate for monetary policy to react, or whether we are looking at something that represents a transitory change in some prices, but one that is not representing an inflation spiral.

In my remarks, I noted—and you brought them up in particular—that most inflation forecasts for 2023 and 2024 show a dramatic decline in the rate of inflation, as all these Covid-related aspects start to diminish. That is an important feature of those forecasts. Maybe they are all wrong, but we can also look at forward-looking expectations for price increases—this is to the question about having anchored price expectations. That can give us some important guidance for what consumers, business and markets think about this surge in inflation that we have seen, and that we expected, frankly. I was forecasting it every month in my previous job. We were talking about spikes in inflation months ago, and now we have them.

When we look at whether there is going to be a diminution or a disinflationary period over the next six months, and then off into 2023 and 2024, we have to look at what we think is going to be happen to labour markets. Most economies' forecasts do not see a labour market tightness commensurate with what we see in GDP growth. When we look at the pricing power of firms, the issue that is most important to consider is how much inflation there is in the global economy. We do not see a lot of inflation in the global economy being passed through to provide an umbrella under which domestic firms can raise their prices.

That is, essentially, why what we are looking at right now is a major surge. I have a lot of ways of evaluating whether that surge appears to be continuing or transitory, or whether it becomes a spiral. I am on the lookout for it, but I do not see it becoming a spiral.

Q5 **Chair:** On that point, if you get it wrong, if you have your four buckets of data that you look at and if it does end up in a wage-price spiral, where do you think you might end up getting it wrong? What is the most likely area where something might turn out rather differently from what you expect?

Dr Mann: The key question is whether firms systematically have the capacity to raise their prices and whether consumers will accept them. You look at what consumers' expectations are for prices on a three-year horizon. If all consumers are saying, "Prices are going to be super-high in three years," that is almost a signal to firms to raise their prices: "Consumers are already expecting it, so why not? I am going to do it."

If there is not competition from abroad in order to discipline domestic prices, you have the potential for ratification of higher prices between consumers accepting it and businesses taking advantage of it, and they have no external discipline coming from global markets.

Chair: I would love to talk further about all of this, but thank you very much.

Q6 **Rushanara Ali:** Good afternoon, Dr Mann. I wanted to pursue some further questions on inflation and growth, as well as productivity. You have spoken about your assessment of inflation. Picking up on what you have said to the Chair, what should we fear more: an incomplete recovery that leaves the economy scarred, or an overheated recovery that unleashes inflation? It sounds to me that you are saying that it is not the latter we should be fearful of, but is it the former?

Dr Mann: That is a very good question, and thank you for asking it. There is a lesson that we can take from the period after the global financial crisis. That crisis and the present crisis were different in terms of origin, but there are lessons that we can draw for policy. We remember that, several years after the global financial crisis hit, there was a concern about rising inflation. We remember the days in August 2013 when oil prices were at $150 a barrel—I distinctly remember that—and people were very worried about inflation taking hold. We also remember that time period where there were significant concerns about debt sustainability and, as a result, fiscal policy was put on more of an austere path.

The lesson from that time period is that there was never a recovery of lost GDP to the global economy or to individual economies. There was a return to pre-GFC growth, but there was a loss of about 5% to 7% of global GDP. We never made up losses associated with the GFC, and the losses were borne disproportionately by younger people. They had different wage dynamics and entered jobs with a lower wage profile. It was at the low end of the income distribution and it was a disproportionate loss for those who saved through interesting-bearing instruments as opposed to equities.

The disproportionate losses are ones that we can see in the data. We do not want to repeat that coming out of Covid, so that bears on the need to not be premature in tightening monetary policy. The metaphor has been used—I guess it is appropriate in the current circumstances—that you have to wait until you see the whites of their eyes. We did not wait back after the GFC, and we do not want to be in the situation again, only 10 years later, of permanent losses to a country’s GDP and the living standards of those who are younger or at the lower end of the income distribution, or who are bondholders.

Q7 **Rushanara Ali:** That takes me on to a follow-up question. If the UK and the international community more widely acted in a similar way and acted prematurely, what would be the loss of global GDP? You mentioned 5% to 7% after the global financial crisis. If they approached it in that way and acted prematurely, would you be able to put a number on it?

Secondly, the UK has had 10 years of stagnated wages, and our Government recently could not even bring themselves to give more than a 1% pay rise to NHS workers, which has caused a great deal of outrage. It is not like that there is much going on in terms of wage increases or even impacts from pressure from the public for wage increases where they are clearly deserved. Given that, how should we be approaching this crisis and how much is going to be gained versus lost if we take the approach that you are suggesting?

Dr Mann: We have to recognise the magnitude of the different kinds of fiscal policies that have been implemented by different economies around the world. That is an important consideration for the strategy going forward. Dramatic action has been taken for monetary policy around the world.

One of the challenges that we face right now is the pace of return to pre-Covid GDP and, in fact, doing better than pre-Covid. The whole point is to try to make up the loss from Covid, not just to try to get back to where we were before. Where we were before was not exactly a great growth rate from the standpoint of rising living standards, or in terms of incentivising businesses to undertake real investments or innovations that would enhance of the capacity of the economy to grow, to deliver those living standards and to repay debt. We really need to do better coming out of Covid than just where we were before. The role that monetary policy can play in that is to not be premature in terms of tightening. That is the important ingredient for monetary policy to play, but it is not the only one.

I want to take this opportunity to key a little off of what Sarah Breeden was saying in her remarks with regard to climate. Climate policy is a key ingredient for incentivising private sector innovation and investment, which are critical ingredients for enhancing the capacity of the economy to grow, which also gives monetary policy more space to engage with policy changes.

Q8 **Rushanara Ali:** That is really helpful. Thank you. In that context, on the one hand we have opportunities for innovation and climate, but also the threats that came up in the earlier session. We have the Glasgow summit coming up and so on. We also have a situation where we should expect scarring to have an impact. While it is not as bad as we might have thought a year ago, it is still pretty bad. The MPC is currently assuming that scarring will amount to 1.25% of GDP in the UK. We have the pre-pandemic assessments around how the economy is going to change and the shape of the labour market, with automation and so on.

When you add up all those things, plus this additional shock and the impacts on younger people, women and other groups in terms of scarring, how do we approach those sorts of dynamics for the UK economy? We have not mentioned Brexit. For the last year and a half, the pandemic overtook the concerns around the impact on GDP, but we know, as the Governor of the Bank of England and many others have pointed to, there is going to be a longer-term hit of about 4%, which is going to come to the fore, and we are still processing some of the uncertainties around that. What does all of this mean for the UK and the direction of travel, and what advice you are going to give when you are on the committee?

Dr Mann: That is a fairly broad agenda that you are setting out in terms of what monetary policy can do for the overall UK economy. Let me step back and say that one of the key challenges for the UK economy is to have capital reallocation—in other words, businesses reallocating capital and associated employment towards activities that are going to be appropriate in the new trade environment under Brexit on the one hand, digitalisation on the second, and then in response to coming out of Covid. We are talking about what role monetary policy can play in driving reallocation of capital towards this new set of incentives that are coming out of the three major drivers: Brexit, Covid and climate.

Monetary policy is not alone in having to create the environment for businesses to invest in the new Brexit environment, the new climate environment and the new post-Covid environment. Monetary policy can play a role but it is a much bigger set of issues than just monetary policy. Going back to the framework that I mentioned before, there is a question about which there is a need for more research. We have monetary policy actions, whether they be policy rate, balance sheet or financial stability through the FPC and related authorities. That is the set of policy levers that monetary policy can pull.

Then there is the financial system as an intermediary for those levers to affect the real economy, and particularly this motivation for private sector investment to invest in employment and skills associated with post-Covid, climate and Brexit.

The most important question that we have to address as monetary policy authorities is how much the financial sector is acting as a complement or a partner to the policy levers that we pull for the objectives of achieving higher business investment and higher potential growth in the economy through those channels. Is the financial sector acting to complement the policy instrument and to transmit the policy signals—those levers for the monetary policy authority—or is it acting to absorb those policy levers, rather than transmitting them to get to the real economy, which is reflected in narrow credit spreads, higher asset prices, including housing, and greater financial stability risks?

This is an area for critical research. There has been some research done that I was involved with, looking at levers to the financial sector, but we must look at the extent to which the financial sector transmits the signals from monetary policy to the real economy and how much it absorbs the monetary policy signals. The more it is absorbing rather than transmitting, the greater the challenge it is for monetary policy to achieve the objectives that are in its remit.

Q9 **Rushanara Ali:** On this area, I have one final question and a supplementary. You referred to a 5% to 7% loss in GDP from the global financial crisis. Would you be willing to put a number on what the losses would be, if the global economy reacted in a similar way?

Dr Mann: I did research when I was at Citi that is client proprietary, so I cannot tell you what it is, but there is a number. It is not quite as big as the GFC, but it is a big number.

Q10 **Rushanara Ali:** What is it? Sorry, I missed it.

Dr Mann: It is Citi proprietary, but I could certainly replicate it at the Bank of England.

Q11 **Rushanara Ali:** That would be really helpful, when you are able to. When we get past this appointment hearing, if you could share that with us, that would be really interesting.

Given what you said earlier to the Chair's questions about price levels and increases, you are not seeing a huge amount of pressure. Would you say that policy makers should not be overly concerned about that at this stage? Would you put yourself in the group of thinkers who are much more in the bracket of needing to stimulate the economy and focus on the issues around scarring and getting people back to employment, versus being overly concerned about inflationary pressures?

Dr Mann: As a monetary policy maker, you always have to be concerned about inflation, both on the upside and the downside. Price stability is the principal remit of the monetary policy authority. On the downside as well as on the upside, it is important to be alert and, indeed, concerned. It is our job to be concerned.

What I am saying is that there are multiple ways of evaluating where we are in terms of inflation dynamics. That richness in terms of the way to look at inflation dynamics is very helpful in gauging how concerned how concerned we should be right now about an inflation spiral. By taking a more granular approach—looking at the four buckets that I was talking about in terms of datasets, and the three different types of data within each one, which were price level, price growth rates and momentum of price growth rates—this mosaic of information really allows us to gauge whether it is time to make an adjustment in monetary policy.

To the extent that we can communicate the way in which we are evaluating inflation dynamics, that gives guidance to decision makers out there about what it is that we are looking at to make us either more or less concerned. You are asking me to say whether now is the right time, and I am saying that I need to see the data for the UK.

Q12 **Rushanara Ali:** I apologise if I am going over old ground, but, in your response to the questionnaire, you said that returning to pre-Covid growth rates should not be considered a sufficient outcome. You have indicated that much more could have been done to avert a 5% to 7% global GDP loss after the financial crisis. Is there a risk that countries, including our own Government, could end up being too reticent about stimulating growth and that we fall into a trap?

Dr Mann: Let me start by noting that the degree of fiscal policy and monetary policy response for Covid was dramatically larger than after the GFC. That is the first thing. At the time, I was writing "Go Big Go Now", because it was critical, and policy makers absolutely stepped up to the plate. In some sense, we were already on a better track to recover GDP in the Covid situation. What I want to say is that the long-term growth rates that we are looking at for advanced economies, including the UK, and for emerging markets are not going to be sufficient to raise living standards.

When we think about what we need to be doing, I hesitate to say more stimulus, because that is not necessarily the way to achieve higher sustainable growth in the long run. There is a difference between the sugar high and the supply-side growth, and so what we really need to be focusing on is not the word "stimulus" but a word that focuses on innovation and private sector investment, which leads to greater employment capabilities and higher long-term growth. We have to be very careful about the language.

Q13 **Rushanara Ali:** Is that the kind of mechanism for increased productivity? You will be aware of the UK's challenges around improving productivity as well.

Dr Mann: You were looking for a number for lost GDP. The OECD had several scenarios that showed GDP losses from the failure to undertake the appropriate policy responses, so I can refer you to those and say that my number was not so different from the OECD's.

With regard to productivity, the key issue is that we have to be looking at the productivity process. What we mean by that is looking at firm-level data, which we have done for the UK. When I was chief economist at the OECD, we undertook this type of analysis for the UK Economic Survey that I headed up in 2017, when I was there. When we look at productivity, every country and sector has leading firms. These are the firms that are the most productive, have the most IT capital, have the most global engagement, being big exporters and importers, and pay the highest wages; they tend to be bigger companies. These are the frontier companies in each sector, so it is not just IT companies; every sector has examples.

What we worry about is that there is very long tail of companies that are laggards. These are companies that tend to be small; they tend to have managers who do not like to change; they have working conditions that are not so great and they do not pay very good wages; they have not engaged in digitalisation. In many countries, those companies survive much longer than they should. They go by the name of zombies. We called them zombies when I was at the OECD and that name has pretty well stuck. I worry that zombification becomes engrained because of the concerns that we cannot get rid of zombies due to the potential employment consequences. That just engrains a low-level productivity and low-wage, bad working conditions environment. That is one concern I have about productivity.

Secondly, there is some concern that even the leading firms, the ones at the frontier that are arguably the most innovative, are becoming less innovative because they are not getting the appropriate incentives of competition at the frontier. This is where we worry about competition at the frontier, whether it comes from abroad or upstarts and new businesses. That is a concern as well in terms of the productivity and the understanding of productivity dynamics.

The UK has examples of the tail and the potential zombification issue, but it also has some issues about how to incentivise the companies at the frontier to keep on pushing out that frontier. This is again where we can get to these issues of what business environment will promote innovation in the context of the post-Brexit and post-Covid environments and the climate challenge.

Q14 **Emma Hardy:** Thank you, that is really interesting. I want to question you a little bit about your views on unconventional monetary policy, by which I mean quantitative easing and negative interest rates. In your questionnaire, you said that the substantial liquidity provided by central banks post-global financial crisis has not motivated private business investment to the expected degree with asset prices responding relatively more. You also warned about the effects of misaligned asset prices. Is it fair to say that you are a sceptic about the effectiveness of quantitative easing? Do you think the costs and side effects outweigh the benefits?

Dr Mann: Quantitative easing has been in place for quite some time, so what I might have said about quantitative easing seven years ago is different from what I say about quantitative easing today. Going into my three years working for Citi, I was already a sceptic about the extent to which quantitative easing was being absorbed by the financial sector in the form of higher asset prices relative to the transmission of quantitative easing through the financial sector to support real-side economic activity.

The Wall Street/Main Street disconnect is a well-known metaphor. That disconnect has only got larger in recent years. At this point, we are in a very difficult transition period where the disconnect between financial markets and the real economy is particularly great. When I was at Citi, I wrote about what I call the central bank dilemma. The central bank faces a dilemma. Its tools are quantitative easing, policy rate, a variety of other macroprudential tools and a set of financial stability tools. Those are its tools; they are what it gets to wield. It has a remit: price stability, sustainable growth and climate for the Bank of England. Those tools work through the financial sector, so the more the financial sector works to absorb those signals—the levers that get pulled—the more challenging it is and the bigger the dilemma is, because ultimately those are the only tools you have. You are trying to get to your remit and the financial sector sits in the middle. As they are absorbed to a greater extent, it is facing the dilemma, "Do I continue to pull these same levers and use these same tools, even though the extent to which they are affecting the things in my remit is decreasing?"

These are the only tools that you have, so the challenge is, "What happens if I stop using those tools or use them in a different way? How much would that have a consequence on financial stability?" Financial stability means not a risk of a financial crisis, but financial volatility, as credit spreads widen, maybe equity markets have a little bit of an adjustment and maybe there is a yield curve effect on different securities—these are all factors that are certainly important and that feed over to the real side through the channel of volatility, the wealth channel, uncertainty, business investment, potential spreads on lending and who can get loans.

It is not an easy decision and it is one about which we do not know enough. How does financial volatility, which might be precipitated by exiting some of the instruments, transmit into my real-side remit? More work needs to be done to understand that linkage.

Q15 **Emma Hardy:** Do you think that quantitative easing has played a role in the rapid rise in house prices that has occurred during the pandemic?

Dr Mann: Asset prices in general have increased, partly because the degree of financial support coming from the fiscal policy side has also been pretty large. There are financial policies being implemented on the monetary policy and fiscal sides, both of which are supportive of asset prices and the underpinning earnings for firms. It is fair to say that, for people, housing is housing services and where they live, but it is also an asset.

For some companies that hold a bank of these houses as rentals—apartment buildings or other things—those are assets. Quantitative easing and other policies to try to stabilise economies after Covid are factors that have tended to increase prices, and housing is an important asset.

Q16 **Emma Hardy:** Thank you. That is really interesting. Do you think that the fact that the Bank owns around half of the national debt under quantitative easing puts monetary policy at risk of Government pressure and fiscal dominance?

Dr Mann: The issue of central bank independence is a very important one. It was brought up as a concern in the most recently released Lords report, but it was also brought up as a concern in the Bank of England's own independent review process in 2019, so it is not as if this is a new concern about the potential for monetary policy independence to be at risk through the magnitude of the holding of Government obligations on the balance sheet.

We have to think about this in terms of not just the Bank of England's holding of obligations but also who else holds the obligations. Foreign participation in the gilt or Government bond market is a very important issue to address and investigate. I did work on that in the United States, and foreign participation in US treasury markets was very important in driving the yield curve, which ultimately is one of the things that would be of greatest concern for the potential interest service on Government obligations.

It is not just the Bank of England holding the debt. It is also who else holds it and how their demands for gilt debt would change over time, if it were the case that the Bank of England altered its quantitative easing programme.

Q17 **Emma Hardy:** I know that in the past you have been a bit critical of negative interest rates. I wonder if you can foresee yourself ever calling for further quantitative easing or voting for a negative bank rate as a member of the MPC.

Dr Mann: It is hard to say never, because it is hard to know what situation might present itself that would require a return to expansionary monetary policy through the channel of these two unconventional monetary policy tools of quantitative easing or negative interest rates. What I can say is that, in terms of the research undertaken collectively with some of my colleagues, negative interest rates tend to be deployed, basically, too late to have the impact that one might want in terms of incentivising lending.

It is also important to go back to the objective of pulling these levers, which is to reduce the cost of capital in order to incentivise businesses to take up loans and invest in new equipment, software, worker training or whatever. Some of the research that my teams did when I was at the OECD showed very clearly that the cost of capital is not the main driver of business investment. It is about the state of the economy. How quickly is it growing? How healthy is the state of the economy? What is the business environment in terms of regulatory climate? What are the incentives, for example, to promote new products and processes for climate change? That is a much more important driver of business investment than the changes in the cost of capital at the margin that we might be talking about.

Q18 **Emma Hardy:** That is really interesting. Given the doubts that you have, are you worried that monetary policy is out of ammunition, to put it one way, as a way to stimulate the economy if it is not using quantitative easing or negative interest rates?

Dr Mann: Right now, I think people are not worried about monetary policy as further stimulating the economy. As I say, I am a little concerned about using the word "stimulus". We ought to be talking about reallocation and how monetary and fiscal policy together, as well as financial stability, are designed to incentivise a change in the environment in order to promote business investment. I come back to my three pillars: fiscal, monetary and structural policies have to be working in complementary fashion in order to achieve higher living standards. Monetary policy clearly has a role to play, but it is not alone in its job to achieve those higher living standards.

Q19 **Emma Hardy:** Finally, and I do have to be quick, I want to press you a tiny bit more. I realise that you cannot say you will never ever support quantitative easing or negative interest rates. Do you see it as unlikely, in the current circumstances, that you would be calling for further quantitative easing or supporting negative bank rates?

Dr Mann: Right now, it is very hard to say that negative interest rates would be the right policy tool. Right now, it seems unlikely that additional quantitative easing would be the right course of action. This is not the environment in which either one of those approaches seems to be appropriate. Where are we going to be in 2023 and 2024? Come back to me and ask me then.

Chair: Thank you very much, Catherine. We might well do; I don't know.

Q20 **Siobhain McDonagh:** Dr Mann, my questions focus on the impact of events abroad, particularly on the prospects of a rapid recovery and inflation risks in the United States, and the ongoing economic impact to of the pandemic continuing worldwide. Should UK policy makers be worried about the rise in inflation in the US to well over 5%? What will be the spill-over to the UK?

Dr Mann: Thank you very much for asking that question. It is a very important one. The issue about spill-overs is one that needs to be elevated in terms of concern and analysis. The UK economy is a small open economy. In other words, it is definitely buffeted—the domestic environment and policy makers are definitely buffeted—by both policies and events abroad. Let me take those two issues separately.

Let me first address the issue about global growth and its potential impact on the UK economy. Many people are looking at global growth rates right now of 6% and thinking, "This is fabulous to have the global economy growing so quickly," but, of course, that is a consequence of coming out of the Covid crisis last year. It is an implication of what your comparison is and the base effect. The growth rate is expected to slow really quite dramatically into 2023 and 2024.

In particular, in the near term, there is a fragility in global growth that is associated with the concerns about new virus mutations as well as difficulties in vaccination deployment in many emerging markets. Of course, emerging markets are very large in terms of their weight of the global economy, so we cannot ignore what is going on with them. There is a fragility underlying that 6% forecast that we have to acknowledge and be concerned about, particularly when looking at some of these emerging markets as new trading partners for the UK in a post-Brexit trading environment. That is one source of concern for the UK economy.

I will turn to your second question on the concerns in the US about high inflation there and very rapid growth in the US as well. For the US, on the inflation front, my analysis of US inflation follows the same strategy as I was putting forth before—looking at whether inflation is well anchored, looking at consumers, businesses and markets. In terms of inflation expectations, I think it still is. I am not worried about anchoring.

I am looking at commodity and energy prices, particularly in light of the recent changes that were agreed between OPEC-plus. It looks as if energy, which is a tailwind right now in terms of prices, will become a headwind as energy prices come off the top next year. That is not a concern for the US and, by the way, it is relevant for the UK as well. Then, on the third and fourth buckets having to do with labour and product markets, yes, there are increases in wages in the United States but, again, from a very low base. For a certain part of the economy, I do not see a wage spiral coming.

I still see labour markets as being loose in the United States. There are a substantial number of workers still on the sidelines, so there are lots of opportunities to bring workers on. Of course, we have to see how things play out in September when some of the programmes run off, which, by the way, is another issue that is important for the UK and its own programmes.

Then the pricing power of firms is a relevant consideration in the US. When we were talking about the pricing power of firms, an important ingredient even in the US is the kind of price discipline that might be coming through globalisation, digitalisation and automation. In the US, yes, we have a 5% inflation rate now, but that is transitory. I see that as coming off the top, so I am not worried about that.

However, the pace of recovery in the United States is faster than any other advanced economy. Therefore, monetary policy authorities in the United States will appropriately be moving sooner to normalise both the balance sheet strategy and the policy rate approach. That will be sooner than other advanced economies such as the UK, the euro area and Japan. I put them in that order because that is probably the order in which they are going to normalise.

The implication is, from a spill-over perspective, that monetary policy authorities at the Bank of England are going to be very conscious of a tightening spill-over coming from the United States. The front end of the research paper I mentioned before that had reference to negative interest rates looked at these spill-overs in terms of financial conditions. It found a very important global factor, of which the US is a big part, to impact financial conditions in the UK.

Monetary policy authorities in the UK have to be very conscious of a potential early tightening coming from that global factor if, in fact, the Federal Reserve does move towards normalisation sooner, from a calendar perspective, than other authorities do. That does mean, in some sense, less necessity for the Bank of England to tighten.

Q21 **Siobhain McDonagh:** You have already made some reference to my next question. As you say, the United States is expected by some forecasters, including the IMF, to exceed its pre-pandemic growth path in the coming years, supported by fiscal and monetary expansion. Do you think that recovery will be sustainable and will it be positive for other world economies?

Dr Mann: That is a good question. There are two pieces to that: first, whether it is going to be sustainable, and secondly, how beneficial it will be for global economies. There is no question that the rapid growth in the United States has already been supportive of the global economy through the channels of trade. The US current account deficit, trade deficit, is widening, which is a standard situation for the United States. It has returned to being the global locomotive in terms of bringing in imports from other economies.

There are some limitations to how much that global locomotive has been able to chug down the tracks, in part because of supply chain issues but also because of limitations, for example, on cross-border tourism. I can say that many more people would be travelling abroad from the United States this year if there were not the difficulties with Covid lockdowns and international travel concerns. That would be another way in which US expansion would be aiding some economies around the world. That is very much the case.

The question about sustainability really revolves around the nature of the next round of policies that might be promulgated from the current Administration. The next set of policies come underneath the umbrella of infrastructure, both traditional and social infrastructure, and potentially some issues with regard to climate, the sustainability of the US expansion, and the potential for the US to get above 2% growth. The US has been below 2% for a while. If we are talking about a sustainable expansion that is higher than the pre-Covid rate, we have to be talking about an expansion that is north of 2% for the United States.

That depends on the supply side of the economy, potential growth, so that depends on innovation. It depends on business investment being stronger and more sustainable than it has been over the last 10 years. It depends on ensuring that those who are and have been outside the labour force come back into the labour force and participate in employment.

We do not know exactly what the key elements of this next round of infrastructure packages look like yet or the probability that they will be passed. These are very important for driving the supply side of the US economy so that it can grow sustainably at above 2%. I am not talking about 2.5%—I do not know exactly the right number—but above where the US economy was growing over the last 10 years. In that regard, a more robust US economy—yes, of course, it is a big economy—will have sustained benefits for the rest of the world through the trade channels and foreign direct investment channels.

Q22 **Siobhain McDonagh:** You have also touched on this one a bit. The pandemic is far from being under control on a global level and vaccine rates are still low in many emerging economies in particular. What ongoing risks and challenges will the pandemic present to the UK until it is under control worldwide?

Dr Mann: In understanding the challenges and the risks associated with Covid, we had all thought that we were closer to the light at the end of the tunnel, but these additional mutations have really generated some concern. We see the financial markets being concerned that it is not just the delta and the delta-plus but that there is going to be something after that. Some of this is a consequence of the difficulties of achieving vaccines and vaccination rates in emerging markets.

It is a global concern. It does imply lower growth for emerging markets. Again, emerging markets are a very big chunk of the global economy; they are not a second class, so coming up with a more robust co-ordinated effort to ensure that vaccines are available and vaccinations are undertaken in emerging markets is something that all economies should be working together on collaboratively, because they are all benefiting. It is a classic externalities case where a collaborative effort improves the prospects for all the economies, not just for the individuals who are receiving the vaccination and have lower death rates and reduced health risks, but from an economic standpoint with regard to business prospects as well.

Chair: Catherine, thank you very much indeed. That brings us to end of this session. It had been very interesting to spend time with you and thank you very much indeed for appearing before us. We wish you every success in the future. So that viewers are aware of what happens now, this meeting will conclude; then the Committee goes into a private session to discuss both appointments. Shortly after that, we will be issuing a report. Thank you very much indeed.