

# Bank of England

Lord Bridges of Headley MBE  
Economic Affairs Committee  
House of Lords  
London  
SW1A 0PW

**Andrew Bailey**  
Governor

26 January 2024

Dear George,

## **Economic Affairs Committee report**

I wish to thank you for the Economic Affairs Committee's report on the operational independence of the Bank of England. The Bank welcomes the report and the conclusion within it that the Bank's operational independence for monetary policy has bolstered economic confidence and provides a strong foundation for low and stable inflation.

As you know, the Monetary Policy Committee conducts monetary policy in line with its statutory objectives and the remit given to it by the Government. In performing these duties, we answer to Parliament. A number of your recommendations are therefore naturally directed to the Government, or indeed to Parliament itself. However, I would like to address those issues that fall within the Bank's responsibilities.

## **The MPC's remit (recommendations 1-3 and 7-8)**

The Bank of England Act makes it clear that it is for the Government to define "what price stability is to be taken to consist of". The Chancellor re-confirmed the 2% target for annual consumer price inflation in the MPC's remit issued in November 2023. He also confirmed that this Government will not change the definition of price stability. The MPC remains absolutely committed to the 2% target.



A key strength of the United Kingdom's macroeconomic framework, and in which it remains an international leader, is the strong macroprudential policy pillar we have built since the global financial crisis. Within this framework, the Financial Policy Committee plays a crucial role in identifying and monitoring systemic risks in the financial system as well as in acting to counter them. This allows the MPC to focus on its primary objective of maintaining price stability. The primary objectives for both committees are very clear, and secondary objectives are only considered subject to achieving the primary objectives.

Similarly, as you note, the framework has a well-established separation of responsibilities for monetary and fiscal policies. This is embedded in our institutions and underpinned by legislation.

The increase in the Bank's responsibilities, including for prudential policies and supervision, reflect the lessons learnt during the global financial crisis. The Bank's management structure with four Deputy Governors, each responsible for separate policy areas with a number of expert Executive Directors, allows the Bank to deliver across all of its policy areas and support its policy committees in their important work, including the MPC.

#### **Quantitative easing and public debt management (recommendations 4-6)**

Decisions on the stock of assets held for monetary policy purposes in the Bank's Asset Purchase Facility are taken independently by the MPC. The APF is indemnified by HM Treasury to ensure that the MPC can take its decisions in this way in line with its statutory objectives and the remit given to it by the Government. Public debt management is the sole responsibility of HMT and the Debt Management Office. Existing arrangements ensure that debt management policies are consistent with the framework for monetary policy, and that changes to the stock of assets in the APF do not interfere with the DMO's issuance programme. As these arrangements are set out in public documents, it is not clear that a memorandum of understanding would add further information not already in the public domain.<sup>1</sup>

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<sup>1</sup> See [Chancellor letter to the Governor \(3 March 2009\)](#), [Exchange of letters between the Governor and the Chancellor on the Asset Purchase Facility \(3 February 2022\)](#), and [Provisional Market Notice \(4 August 2022\)](#).

The Bank has studied the impact of quantitative easing extensively over recent years, including potentially adverse effects of a large central bank balance sheet.<sup>2</sup> When designing its strategy for quantitative tightening, the MPC also noted that reducing the size of the APF has the important benefit of reducing the risk of a ratchet upwards in the size of the Bank's balance sheet over time if successive policy cycles encounter the effective lower bound on interest rates. The Bank is currently undertaking extensive analysis on the future steady state level of central bank reserves needed to maintain price and financial stability. Decisions on the size and shape of our future balance sheet will be made in close consultation with relevant stakeholders.<sup>3</sup>

### **A Central Bank Digital Currency (recommendation 9)**

Trust in money is at the core of the Bank's mission and is the foundation for the safe and effective functioning of the UK economy and financial system. In the context of a rapidly evolving UK and international payments landscape, it is therefore imperative that we consider how best to guarantee that the future payments landscape continues to provide money that is trusted and meets the needs of households and businesses. Our work on the potential role for a retail CBDC in the United Kingdom, a 'digital pound', is therefore very much in accordance with the Bank's objectives and forms part of wider work on the evolving payments landscape.

We have always recognised that the wide range of public policy issues around CBDC, including privacy, financial inclusion and competition, go beyond the Bank's remit. For that reason, exploration of a digital pound has been executed as a joint Bank-HMT project since 2021 and overseen by a joint Taskforce. The current 'design phase' of the digital pound project will explore the feasibility of a digital pound and potential design choices. It aims to develop a robust evidence base to inform a decision later this decade as to whether or not to proceed to a 'build phase'.

### **Diversity of views and challenge (recommendations 10-13)**

The appointment process and criteria for appointing MPC members is a matter for the Government, with the exception of the Chief Economist who is appointed by the Governor after consultation with the Chancellor. The MPC benefits from the diverse expertise of external as well as internal members, and from support and challenge from the Bank's excellent staff. I can assure you that discussions on the MPC are open, frank and forensic, often with dissenting views as the votes indicate.

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<sup>2</sup> I discussed this work in a [speech given at the Jackson Hole Economic Policy Symposium in 2020](#). The Bank provided a comprehensive update on its thinking on QE its [2022 Q1 Quarterly Bulletin](#).

<sup>3</sup> This is discussed in more detail in a recent [speech by Andrew Hauser, Executive Director for Markets](#).

The Bank runs open recruitment processes for its staff at all levels of the organisation. It actively strives to ensure that there is a range of candidates from a diverse set of backgrounds.

The Monetary Policy Report provides an extensive summary of the MPC's key forecast judgements along with an assessment of the current outlook for the UK economy and inflation. This includes discussions of data for money and credit. As described in the minutes of several recent MPC meetings, these discussions form part of the Committees' assessment of monetary and financial conditions. The MPC will continue to monitor monetary aggregates along with other data and consider the implications of latest developments for its assessment of the outlook for consumer price inflation.

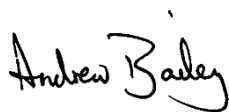
The purpose of the review currently undertaken by Dr Ben Bernanke is to develop and strengthen the Bank's processes in support of the MPC's forward-looking approach to the formulation of monetary policy, especially in times of high uncertainty. Dr Bernanke is approaching this review with the rigour that one would expect of a world-leading expert of his calibre. He is working independently, and I am sure that he will be happy to appear before the EAC to discuss his recommendations in due course.

#### **The Bank's Court of Directors (recommendation 14)**

Finally, it is important to emphasise that the Bank of England Act gives the responsibility for formulating monetary policy to the MPC. The Act specifies that Court plays no role in relation to the formulation of monetary policy. The role of Court is to keep under review the Bank's performance in relation to its objectives, the exercise of the Bank's statutory functions and the processes of the policy committees. The Chair of Court acts to ensure that Court operates to the highest standards, which includes keeping a keen eye on the role of the non-executive directors, individually and collectively, to ensure that they are as effective as possible. The so-called Oversight Committee you refer to was abolished to streamline the governance structure and create a unitary governing body in line with good practice.

I look forward to our next hearing.

Yours sincerely,

A handwritten signature in black ink that reads "Andrew Bailey". The signature is written in a cursive, slightly slanted style.