HM Treasury, 1 Horse Guards Road, London, SW1A 2HQ

10 June 2021

The Rt Hon. Lord Forsyth of Drumlean
Chairman of the Economic Affairs Committee
House of Lords
London
SW1A 0PW

Dear Michael,

ENQUIRY INTO QUANTITATIVE EASING

Thank you for your letters of 26 and 28 May regarding your enquiry into quantitative easing and Dominic Cummings' evidence to Parliament, respectively. I have responded to each of your questions in turn below.

1. In what ways did HM Treasury and the Bank of England ensure their respective policies were consistent and complementary?

The Governor and I have regular meetings to discuss the latest economic data and outlook, and update each other on policy decisions taken by our respective bodies. A representative from HM Treasury also attends Monetary Policy Committee (MPC) meetings and can discuss fiscal policy issues, though is not a member of the MPC and therefore does not vote on monetary policy decisions. On the Financial Policy Committee (FPC), HM Treasury has a non-voting member who attends FPC meetings to ensure coordination with HMG policy, for example, where legislation is required. It's also the case that officials from HM Treasury and the Bank of England meet regularly to discuss and collaborate on issues that are relevant to both institutions, including: the economy, financial stability, and international cooperation to name a few.

2. What assessment have you made of risks to the public finances if the Bank had to raise interest rates in response to sustained inflation?

As set out in the March 2021 Budget (Box 1.D), having rebuilt the strength of the public finances over the previous decade, and underpinned by the UK's strong institutional framework, the government has been able to borrow to provide a comprehensive package of support for the economy. However, increased borrowing leaves the public finances more vulnerable to future shocks. As noted in the March 2021 Budget, a sustained 1 ppt increase in short rates would increase debt interest spending by £11.9bn and a 1ppt increase in RPI inflation would increase spending on debt interest by £6.9bn, in the final year of the forecast (2025-26). The overall impact on the public finances from an increase in interest rates would depend on the source of the shock; if the increase in interest rates reflected higher economic growth, the debt stock could be lower and the primary balance more favourable.

3. Whether you agree that proposals to cease paying interest on reserves constitute fiscal policy and would therefore be a decision for HM Treasury?; and,

4. What assessment you have made of such proposals?

This proposal is not one that is being considered by the Treasury. The governance for any future new policies would be based upon the current split of responsibilities between HM Treasury and the MPC. The independent MPC has sole responsibility for the operation of monetary policy, and the Treasury has responsibility for fiscal policy.

5. Will HM Treasury publish the Deed of Indemnity for the Asset Purchasing Facility?

I would reaffirm the Governor's remarks during his evidence, that the document does not cause the Bank to have to ask for permissions and it sets out the terms of operations of the Asset Purchase Facility and how the Indemnity works.

6. Did HM Treasury provide any guidance or instructions to the Bank of England on how it should interpret and implement the update to the mandate?

The remit of the MPC is set by the Chancellor and is reaffirmed yearly through a letter to the Governor of the Bank of England, as required by the Bank of England Act 1998. As is standard practice, ahead of Budget the draft remit was shared with the Governor and senior Bank staff for comment. The Treasury gave no guidance or instruction to the Bank of England on how it should implement the update to the mandate, as it is for the independent MPC to judge how it can support the Government's green and other economic objectives whilst achieving its primary objective of price stability

7. How do you expect the update to affect the Bank of England's corporate bond purchasing scheme? How should the Bank avoid accusations of 'picking winners'?

Monetary policy, including decisions on Bank Rate and asset purchases, is the responsibility of the independent MPC. Therefore, the Government does not comment on the conduct or effectiveness of monetary policy. The separation of fiscal and monetary policy is a key feature of the UK's economic framework, and essential for the effective delivery of monetary policy.

More details on the potential impact on the Bank's corporate bond purchase scheme of including climate considerations were published by the Bank in a Discussion Paper on 21 May.

8. Did you or HM Treasury officials attend meetings which included discussion on using “emergency powers” to direct the Bank of England during the COVID-19 pandemic?;

9. Which Ministers and/or senior officials, including from the Bank of England, attended any such meetings?;

10. What was the substance of these discussions?; and,

11. What is your assessment of the evidence provided by Mr Cummings?

Neither myself nor HMT officials attended meetings on the potential use of emergency powers to direct the Bank of England during the COVID-19 pandemic.

Best wishes,

RISHI SUNAK