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

16 September 2021

Lord Forsyth of Drumlean
Chairman, Economic Affairs Committee
House of Lords
London
SW1A 0PW

Dear Lord Forsyth,

I am writing to respond to the Committee's inquiry into Quantitative Easing (QE). I am grateful to the Committee for its report.

The issues you raise in the report are complex and tackle a wide range of issues relating to QE and your recommendations have been acknowledged and carefully considered. This letter responds to recommendations 8, 12, 16, 17, 22 and 25, and the Bank of England are responding to the remainder.

Distributional Outcomes

Your report stated that there was limited understanding of how QE interacts with fiscal policy, and that your research shows that QE has had adverse impacts on wealth inequalities, through raising asset prices, that can only be mitigated using fiscal policy. You invite HM Treasury to reply to any research that the Bank produces on the distributional effects of QE.

All public policy, including monetary policy, has distributional impacts. The Bank's remit requires it to support the economic policy of HM Government, including its objective for strong, sustainable, and balanced growth. Government considers a wide range of research and consults a wide range of stakeholders when making policies to ensure decisions are made using a robust evidence base. The Bank's research forms part of this evidence base.

Bank of England Mandate

Your report notes the updated remit that reflects the Government's environmentally sustainable, net zero growth strategy, noting some of the challenges involved with this. You ask me to write to the Governor to clarify expectations.

The MPC's primary objective of maintaining price stability is unchanged. It is for the MPC to judge how it can support the Government's green and other economic objectives while achieving its primary objective of price stability. It would not be appropriate for Government to instruct the MPC on how to do this as it may interfere with the operational independence of the Bank.

Debt Management

Your report asks HM Treasury to clarify whether they will stop paying interest on reserves and whether this is a decision for the Bank or for HM Treasury, noting that this would constitute fiscal policy. You also ask HM Treasury to publish the Deed of Indemnity.
As noted in my response to the Committee's letters, HM Treasury is not considering a policy of ceasing paying interest on reserves. Additionally, the decision not to publish the Indemnity has been carefully considered and is consistent with the approach taken since the inception of the Asset Purchase Facility.

Uncertainties

Your report notes that the impact of QE on inflation and output is uncertain and recommends that HM Treasury should do more to acknowledge this and understand the effects of QE. I note the Committee's recommendations.

Risks to the Bank remit

You state that HM Treasury has not helped to clarify its relationship with the Bank, and that adding additional objectives for the Bank risks the MPC losing its focus on price stability. I reaffirmed the remit for the MPC at the Budget on 03 March 2021, re-confirming the inflation target for the MPC as 2 per cent as measured by the 12-month increase in the Consumer Prices Index. This reflects the primacy of price stability and the forward-looking inflation target in the UK monetary policy framework. The Government's commitment to price stability remains absolute. Independent monetary policy has been successful in delivering low and stable inflation. In the 20 years prior to independence, inflation fluctuated between 1% to 22%, while over the past 20 years inflation has averaged around 2% and never risen above 5.2%. Inflation expectations have remained well anchored since Bank independence in 1997.

I would like to thank you again for your Committee's work into QE and monetary policy.

Best wishes,

RISHI SUNAK