

# Treasury Committee

## Questionnaire for Charlie Bean

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**For reply by Monday 30 June at 12 noon**

### **Responsibilities as Deputy Governor**

1. Please explain how your experience to date has equipped you to fulfil your responsibilities as Deputy Governor for Monetary Policy. In particular, in what areas of the Bank's work do you believe you will be able to make an immediate contribution and which areas will you have to undertake additional research when in post?

I have spent the past eight years both as a member of the Monetary Policy Committee and as the Bank's Chief Economist and Executive Director for Monetary Analysis and Statistics, the Bank directorate that supports the MPC. Prior to that, I spent 18 years as an academic at the London School of Economics, where much of my research was related to monetary policy and macroeconomics more generally. During that time, I also acted as a policy adviser to various bodies, including the Treasury and to this Committee. So I believe that my past experience leaves me well equipped for this post, and across the full range of responsibilities.

2. To what extent will you require a different approach as Deputy Governor from that required in your previous positions, with regard to the discharge of the duties and responsibilities involved?

As Executive Director for Monetary Analysis and Statistics, I carried the responsibility for day-to-day management of the Bank's activities supporting the Monetary Policy Committee, including the preparation of the *Inflation Report* and the projections contained therein. Those activities absorbed a considerable fraction of my time. My new role is more strategic in nature, and covers both the Monetary Analysis and Statistics, and Markets directorates. In my new role, I expect to have more time to devote to advancing the Bank's communications agenda, both on monetary policy and market operations. I also expect to participate in more international meetings than is the case in my present role. Finally, I expect to play a greater role in the Bank's management, including on financial stability issues.

3. Do you intend to serve out the full term for which you are appointed?

Yes.

4. What are your major objectives in the first six months of your Deputy Governorship?

There is no doubt that the UK economy presently faces the most challenging set of circumstances since at least the early 1990s and possibly earlier. We are faced with two substantial shocks of unknown impact and duration: the de-leveraging that is underway in financial markets and the associated tightening in the availability of credit; and the

relentless rise in oil and other commodity prices. Both these shocks depress activity, but have conflicting effects on inflation. Meeting the Chancellor's inflation target, whilst simultaneously avoiding undue volatility in output, will be no easy task. So ensuring that the MPC gets the best possible analysis and intelligence from both the Monetary Analysis and Statistics, and Markets directorates, will be my number one objective. Ensuring that our aims and strategy in dealing with the challenge is well understood – not only by Parliament, market participants and the media, but also by the broader public – will also take a high priority.

Away from monetary policy, I expect that much of the energies of the Bank's senior management will be directed to preparing for and implementing the Government's planned changes in the financial regulation and stability arena.

5. How do you intend to develop the monetary policy area of the Bank over the next five years?

I am broadly content with the shape of the Monetary Analysis and Statistics Directorate, though it will no doubt continue to evolve over the coming years. In particular, I will expect my nominated successor as Chief Economist, Spencer Dale, to continue to press ahead with the “leaner but smarter” strategy we have been pursuing over the past couple of years. The Markets Directorate is still building its intelligence capability and there is a review presently under way of our market operations to identify necessary changes in the light of the experience of the past year.

6. As Chief Economist, you were more involved with Monetary Analysis than the Markets side of your new brief. How do you intend to familiarise yourself fully with this latter element of your new responsibilities?

The events of the past twelve months have meant that I have already had to come to grips in some detail with what has been happening in financial markets in order to assess their implications for monetary policy. In addition, I am a member of the Bank's Financial Stability Board and participate in the drafting of the *Financial Stability Report*. I am also a member of the group reviewing the Bank's money market operations framework. So I feel that I am already in a fairly good position. Nevertheless, I recognize that I will need to learn more and expect to spend some of my first few months in the post familiarising myself with more material, both internal and external. I also intend extending my circle of personal contacts to include more external market participants.

## Responsibilities as member of the MPC

7. What contributions have you made individually to the conduct of monetary policy on the MPC? What lessons have you learned from your period as a member of the MPC?

I would single out two primary contributions. First, ensuring that Monetary Analysis provides the MPC with high quality and timely analysis of the conjunctural issues facing them, together with delivering the quarterly *Inflation Report*. The annual survey of MPC members, carried out for Court, suggests that they generally rate the quality of the support very highly. Second, leading the economic discussion on the Wednesday afternoon part of the MPC meeting itself. In addition, I hope my speeches (e.g. on asset prices and monetary

policy) have added to the public debate and understanding.

As far as lessons go, it would take a book to cover everything that I have learnt about the economy and about the making of monetary policy since joining the Committee. I have become acutely aware of the difficulties of extracting the signal from what are often conflicting indicators. I have been impressed by the value of the intelligence gained through the Agency network. From an economic perspective, I have learnt much from both the staff and my colleagues on the Committee about the wide variety of economic questions that have faced us. And from a policy-making perspective, I would highlight the value of a robust yet open-minded debate, where each MPC member brings something different to the discussion.

8. What contributions have you made to explaining the work of the MPC and enhancing public confidence in its actions over the last three years? What activities do you intend undertaking in order to add to the public's understanding of the role and decisions of the MPC?

Aside from my appearances before the Treasury Committee, since June 2005 I have made:

- 13 regional visits through our Agency network;
- 10 presentations of the *Inflation Report* (generally to business audiences);
- 21 presentations on what the MPC does (to a variety of audiences);
- 7 public speeches on a variety of economic issues;
- Participated in 12 *Inflation Report* press conferences.

In addition, as Chief Economist, I have had responsibility for overseeing the preparation of the *Inflation Report* each quarter, including the drafting of the Overview, as well as for the preparation of other public documents (such as the Bank's submission to the Treasury Committee's "MPC Ten Years On" enquiry).

## Macroeconomics

9. Over the next three years, what are the major risks you foresee to the MPC meeting the inflation target?

The Committee is presently confronted with two major conflicting risks. On the downside, the dislocation in financial markets probably has further to run, especially if a slowing economy here and abroad generates a second round of write-downs, this time associated with corporate loans. Moreover, the impact of the tightening in the terms of availability of credit could prove greater than is embodied in the central case in our most recent set of projections. That might be so, for instance, if falling house prices have a greater depressing effect on household spending than we currently anticipate. In that case, the slowdown in growth could be even more pronounced and/or be more persistent, leading inflation to undershoot the target in the medium term.

The second risk relates to the prospects for commodity prices, especially oil, and the possibility that the current period of elevated inflation will lead to inflation expectations becoming dislodged and the higher inflation becoming embedded in the economy. Oil prices have systematically surprised to the upside over the past four years, reflecting the combined influence of sustained growth in global oil demand coupled with unresponsive oil supply. Though the price may fall back in the long run as higher prices generate substitution away from oil and new sources of supply come on stream, the near-term

prospect for oil prices (and energy prices more generally) remains particularly uncertain.

As regards the possibility that the current above-target inflation will become embedded through second-round effects onto other prices and pay, we are already seeing more pass-through of higher costs into output prices than had been the case during the first phase of the rise in commodity prices. And while pay growth has so far remained subdued in the face of higher consumer price inflation, there remains the risk that employees will seek to maintain their living standards by seeking higher wages. Past experience suggests that it can be very costly in terms of foregone output and higher unemployment to reduce inflation, once it has become embedded at a high rate.

10. How important do you think the official measures of inflation are in the wage-setting process in the United Kingdom?

RPI rather than CPI remains the dominant reference index in pay discussions, particularly in the private sector. However, empirical studies suggest that the link from RPI outturns to wage settlements and earnings is much weaker now than it was in the 1970s and 80s. This probably reflects: changes in the structure of wage-bargaining; increased competitive pressures in product markets; increased availability of migrant labour; and the increased scope for offshoring production. All four developments mean that employees may struggle to obtain compensation for past and prospective increases in RPI, even though they may request it. Instead, the dominant criteria may be the ability of businesses to pay higher wages and their need to recruit and retain suitable staff. That may help to explain why pay growth has remained subdued, in spite of the pickup in inflation.