



BANK OF ENGLAND

News release

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Court of the Bank of England welcomes three independent reviews

In May 2012, the Court of the Bank of England commissioned a set of three Reviews into areas of the Bank's performance and existing capabilities. Each Review was led by an independent, internationally respected expert. They were completed in October 2012 and the Court of the Bank, including the three Governors, discussed them with the Reviewers at a special meeting on 26 October. The Reviews are published here in full.

The three Reviews cover:

- The provision of Emergency Liquidity Assistance in 2008/9.
- The Bank's framework for providing liquidity to the banking system as a whole.
- The Monetary Policy Committee's forecasting capability.

Publishing the Reviews, the Chairman of Court, Sir David Lees, said:

"The Court of the Bank of England welcomes these three independent Reviews which we are now publishing in full following a recent discussion with the Reviewers by Court. We are most grateful to Ian Plenderleith, Bill Winters and David Stockton for the work they have done and for meeting the agreed target date of October 2012.

When we commissioned the three reviews last May we had two particular objectives in mind. First, to learn practical lessons from past experience. Second, to examine ways in which the Bank may deliver more effectively its increased responsibilities in the future. The Reviewers have provided us with a large number of constructive recommendations and options for further consideration. That meets our original objectives.

Court has asked the Bank's executive, in consultation where appropriate with the Monetary and Financial Policy Committees, to respond to Court on the ideas set out in the Reviews early in 2013 and will follow this up with close interest. A report on progress will be made in the Bank's 2013 Annual Report."

The Governors of the Bank of England, Sir Mervyn King, Charlie Bean and Paul Tucker, said:

“We welcome these three Reviews. The Reviewers have given us an independent perspective on some of the key challenges the Bank has faced in responding to the financial crisis and have given us a great many ideas to consider that could improve the Bank’s performance. We are starting programmes of work to evaluate the recommendations and to plan changes. We will report regularly to Court.

Our initial, high-level, response to the Reviews is set out below.”

Plenderleith Review into the provision of Emergency Liquidity Assistance in 2008/9

The Review highlights many useful operational lessons that will help us to ensure that all future Emergency Liquidity Assistance (ELA) operations are as effective as that in 2008/9, which the Review concludes “can be judged to have achieved its purpose effectively” and was “an essential plank in the structure of official support that was able in the end to return the financial system to a degree of stability.”

The principal objective of many of the recommendations in the Review is to build on that experience to maximise the Bank’s readiness for any future ELA, both in identifying problems early and in the conduct of operations. We share that objective and will use the ideas in the Review to meet it.

The Review recommends that the Bank should have the capacity, if necessary, to extend ELA to non-banks. This is echoed in the Winters Review on the Bank’s framework for providing liquidity to the banking system as a whole, in which it is recommended that the Bank considers making certain liquidity facilities available to non-banks. There is in fact no legal impediment to the Bank providing ELA to non-banks. We will weigh carefully whether or not to go further and to give some non-bank entities access to the Bank’s regular facilities.

The Review makes recommendations for structuring the governance and decision-making around future ELA. This is important. We will develop the Bank’s existing structures, in close consultation with Court and with the Chancellor, who is responsible for any decision involving the use of public funds, including the authorisation of ELA (and any increase in the Bank’s capital, which is recommended in both the Plenderleith and Winters Reviews). We also need to clarify the roles of the FPC and the PRA Board in respect of both general ELA policy and individual cases.

Winters Review into the Bank’s framework for providing liquidity to the banking system

We agree with the finding of the Review that the Sterling Monetary Framework in place before the crisis was insufficient to meet our financial stability objectives. The Review also notes that, following the very extensive changes made during the crisis, the Bank’s framework is now “robust and broadly fit for purpose.”

Nevertheless, we do not wish that process of improvement to stop and this Review offers the Bank a platform for the next stage of development. It offers us a great many options to consider.

Several recommendations are aimed at reducing and ideally removing any reluctance of banks to access the Bank of England's liquidity facilities, particularly the Discount Window Facility (DWF). We share that objective. As the Report argues, we will need to balance that against the need to avoid making it too easy for banks to take excessive liquidity risks. The Review makes helpful suggestions for striking that balance, including the introduction of some form of up-front 'insurance premium', as well as enforced regular usage of liquidity facilities by banks. We will pursue these ideas further.

The Review discusses the role the Bank's framework might play both in providing a backstop to the maturity transformation role of the financial system and in acting as a Market Maker of Last Resort. It suggests that the Bank should be more explicit about its role in these areas. This issue is a challenging one with which many central banks are grappling, and raises fundamental questions about the role of a central bank and the incentives it creates for private institutions to take risk. We need to give it careful thought.

On governance, the Review notes "it is apparent that the Governor regularly consults the Deputy Governors and other senior staff over the Bank's Sterling Monetary Framework", but suggests this appears to be at the discretion of the Governor of the day. We intend to follow the recommendations to put in place mechanisms to formalise this, as well as to formalise the roles of MPC and FPC in this area.

The finding of the Review that less senior staff "have a tendency to filter recommendations" is one to which we, and Court, will give very careful attention. The Review notes too that "less senior staff regularly undertake significant in-depth analysis of a wide range of policy options, and are often willing to challenge the views of their superiors..." Our aim is to follow the recommendations of the Review to ensure that this is embedded in the culture of the Bank.

Stockton Review into the Monetary Policy Committee's forecasting capability

The Review finds that the "forecast process and associated forecasting tools employed by the Bank in support of its monetary policy decisions are sound." Nonetheless, given the challenges experienced by forecasters during the financial crisis, we will consider carefully the ideas for improvement in the Review. The first step in our work programme will be to consult the Monetary Policy Committee.

The Review recommends that the Bank undertakes and presents a fuller analysis of its past forecasting performance. Analysis of past performance is already a part of MPC's forecasting process, but we accept that the Bank should do more in this regard.

The Review calls for more 'entry points' for a range of alternative views into the forecast process, particularly those that diverge from the consensus. We will work up plans for developing the expertise of staff,

engagement with outside experts, and ultimately what the Review summarises as “mechanisms capable of acting as a trigger for a fundamental reassessment of the outlook.”

We agree with the finding of the Review that the financial crisis has demonstrated how important it is that our forecasting process should take even greater account of the potential implications of imbalances - in the financial sector, the wider UK economy, and the world economy.

Several of the recommendations in the Review would tilt the balance of the forecast away from being a ‘best collective judgement’ of the MPC as a whole. The MPC will need to consider this carefully. In contrast to some other central banks, monetary policy decisions are determined by individual votes and not by consensus. The Inflation Report is the only outlet through which the MPC explains its collective view rather than the views of individual members and, as the Review notes, the process of forming a collective forecast brings some notable benefits.

The Review recommends that the MPC should take stock of the information provided in the Inflation Report, in the light of the experiences of other central banks. The MPC will do so, aiming to communicate the right amount of information, with clarity, and in a way that is consistent with forecasts being not a single number but an assessment of the probabilities attached to a whole range of possible outcomes.

Notes for Editors

- The terms of reference for the Reviews were published in May 2012 and are available on the Bank of England website at <http://www.bankofengland.co.uk/publications/Pages/news/2012/049.aspx>

- The Reviews were conducted by Ian Plenderleith, Bill Winters and David Stockton. The Reviewers and their support team had unrestricted access to Bank of England records and were able to speak to both Bank staff and others outside the Bank as they chose.

- Ian Plenderleith CBE is Chairman of BH Macro and a non-executive Director of Morgan Stanley and Co International and of BMCE Bank International in London, and of Sanlam in South Africa. Previously, his main career was at the Bank of England (1965-2002), where he was Executive Director responsible for market operations and a member of the Monetary Policy Committee, and at the South African Reserve Bank in Pretoria (2003-2005), where he was Deputy Governor and a member of the South African Monetary Policy Committee.

- Bill Winters is the Chief Executive Officer and a managing partner of Renshaw Bay. He has 28 years of experience in the investment industry, including 26 years at JP Morgan. He moved to London in 1992 as the Head of European Fixed Income and in 2004 was promoted to Co-CEO of JPMorgan Investment Bank. He played a key role in managing JP Morgan Investment Bank through the 2008 financial crisis, including the

acquisition and management of Bear Stearns. He was a member of the Independent Commission on Banking in the United Kingdom which submitted its report to the Chancellor in September 2011.

- David Stockton is a Senior Adviser at Macroeconomics Advisers LLC and the former Director of the Division of Research and Statistics at the Board of Governors of the Federal Reserve System. In that position, Mr Stockton oversaw the preparation of macroeconomic and financial market analyses and forecasts for the Board of Governors and the Federal Open Market Committee (FOMC) to assist them in decisions related to monetary policy.

Key Resources

<http://www.bankofengland.co.uk/publications/Documents/news/2012/cr1plenderleith.pdf>

Review by Ian Plenderleith

<http://www.bankofengland.co.uk/publications/Documents/news/2012/cr2winters.pdf>

Review by Bill Winters

<http://www.bankofengland.co.uk/publications/Documents/news/2012/cr3stockton.pdf>

Review by David Stockton