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Microprudential, macroprudential and monetary policy: conflict, compromise or co-ordination? - speech by Paul Fisher

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In a speech today at Richmond University, Deputy Head of the Prudential Regulation Authority (PRA), Paul Fisher discusses the conditions under which the Bank of England's three policy committees – the Monetary Policy Committee (MPC), the Financial Policy Committee (FPC) and the PRA Board - can work effectively together to deliver their separate objectives.

In his speech, Paul asks a series of questions designed to examine whether the MPC, FPC and PRA Board have been set the right targets, appropriate policy levers and an appropriate structure to meet those conditions.

Paul explains that there is no inherent conflict to achieving the triple objective of CPI inflation at 2%, financial stability, and safety and soundness of firms at the same time. But coordination is needed. He says "even though the different policy objectives can be achieved simultaneously, that does not mean that each committee can ignore the others". He continues "in practice independence is inevitably partial: each policy tool is likely to affect all the objectives, albeit in different degrees...the choices of one committee will affect the choices of the others". Paul uses the example of the financial stability 'knockout' which was included in the MPC's forward guidance, which acknowledged explicitly that there might be circumstances when monetary policy settings had to reflect the risks to financial stability.

Co-operation and co-ordination is necessary between the committees to achieve all three objectives. One aspect of this co-operation is a common understanding of the economy. This is important as the committees could set inconsistent policies if they had different views about the state of the economy or just used different economic models. The presence in the Bank of a single forecasting function and cross-use of its outputs helps to avoid that particular trap.

Paul also notes that the objectives have to be achieved over the medium term because of policy lags and there are secondary objectives which ensure that the outcomes are consistent with maximum sustainable growth. But that means that 'The MPC should not be inflation nutters'; 'The FPC should not seek the stability of the graveyard'; and the 'The PRA Board should not seek to implement a zero failure regime'.

Paul notes that "coherence doesn't always mean agreement. There will no doubt be disagreements at some point". He highlights that the appointment of independent members to the policy committees is intended to ensure challenge and stop 'group-think'. Paul explains that the likelihood of incoherent policies across committees is mitigated by some common membership and points out that the Bank of England has "a collective institutional need to make the whole framework function in the best interests of the UK economy".

Paul concludes by saying "It is important that we give the new structure time to work…because we will learn a lot" as well as noting that the regulatory reform agenda is still being decided and implemented internationally. Finally, Paul comments that "policy changes take time to have their effect. Indeed, the experience of monetary policy over the past few years demonstrates the need for patience".