Bank of England speeches

A short summary of speeches made by Bank personnel since publication of the previous *Bulletin* are listed below.

The repertoire of official sector interventions in the financial system: last resort lending, market-making, and capital

Paul Tucker, Deputy Governor, May 2009.

www.bankofengland.co.uk/publications/speeches/2009/speech390.pdf

In this speech Paul Tucker discussed the role the authorities can play in providing crisis support to the financial system. The current crisis has underlined how problems of funding liquidity, asset-market liquidity and solvency are intertwined. And those dimensions of a systemic crisis map into the authorities' capability, in principle, to be a lender of last resort; a market maker of last resort (MMLR); and a provider of capital of last resort. In relation to central bank liquidity insurance to banks, he explains the thinking behind the Bank of England's new permanent facilities: the discount window facility and wider-collateral long-term repos. Their design reflects the Bank's objective in this area: to reduce the cost of disruptions to the liquidity and payments services supplied by commercial banks by balancing the provision of liquidity insurance against the costs of creating incentives for banks to take greater risks, and subject to the need to avoid taking risk onto its balance sheet. The authorities also need to set the right regulatory framework for banks' management of their liquidity. He argued that regulators should define the 'liquidity buffer' to comprise high-quality securities that can reliably be traded or exchanged in liquid markets, including in stressed circumstances. In practice, that would mean focusing on government bonds in many economies.

In relation to the debate about MMLR operations, he outlined for debate six possible principles, stressing the need for a central bank to perform a catalytic role, helping ideally to kick-start markets rather than replace them. He argued that there was also a need for principles and policies for what might be called 'capital of last resort' given the recurrence through history of episodes when governments have ended up bailing out banks. In that connection, he also suggested for debate that one possible approach would in future be to build on the example of deposit insurance schemes by putting more of the cost of banking system failures on shareholders in the banking system generally rather than the general taxpayer.

Deputy Governor's speech given at Cutlers' Feast, Cutlers' Hall, Sheffield

Charles Bean, Deputy Governor, May 2009.

www.bankofengland.co.uk/publications/speeches/2009/speech389.pdf

In this speech, Charles Bean described how a crisis that had begun in the financial sector triggered a much wider global recession. A collapse in confidence and a sharp contraction in the availability of credit following the failure of Lehman Brothers bank caused a global downturn in demand which was then propagated through the stock cycle. He noted that the nature of this recession was different from previous ones because it was not the result of the need to reduce inflation due to excess demand growth for goods and services, but arose out of excess demand for financial and real assets. The banking system was at the heart of the problem and was therefore where a number of policy initiatives had been focused. He explained the Monetary Policy Committee's decision to cut Bank Rate to 0.5% and the programme of asset purchases intended to increase the growth of nominal spending. He noted that there are were some encouraging signs on the economy and that growth should resume towards the end of the year although the pickup is likely to take place relatively slowly. He emphasised that the MPC's remit is to target CPI inflation and set out the tools the Bank would use to withdraw its monetary stimulus if inflation risks increased. He explained that it would not be necessary to unwind the asset purchases before raising Bank Rate. And if the Bank needed to drain reserves quickly it could issue Bank of England bills in order to be able to stagger the sales of gilts.

Containing system-wide liquidity risks: some issues and challenges

Nigel Jenkinson, Adviser to the Governor, May 2009.

www.bankofengland.co.uk/publications/speeches/2009/speech388.pdf

In his speech, Nigel Jenkinson set out a number of high-level objectives that should help guide future research and analysis on the development and design of a framework to strengthen the regulation of system-wide liquidity risks. He reviewed the origins of the present financial crisis, noting that defences against a rise in system-wide liquidity pressure were clearly inadequate and that attempts by banks to use defences designed to address idiosyncratic liquidity problems severely compounded system-wide stress. He noted that reducing the likelihood and impact of future episodes of system-wide liquidity risk was high on the policy agenda. He welcomed the initiatives being taken by the Basel Committee and Committee of European Banking Supervisors to strengthen the management and supervision of liquidity risk by individual firms, but believes future financial regulation needs to take stronger account of system-wide implications. He gave a preliminary assessment of some of the issues and challenges in meeting five high-level objectives that should influence the future design of a new framework. He thought good progress has already been made in some of the areas but in others, research is only just beginning. He concluded that any new framework must balance the containment of system-wide liquidity risks against the benefits the financial system provides through maturity transformation and the taking of liquidity risk.

Rethinking the financial network

Andrew Haldane, Executive Director for Financial Stability, April 2009.

www.bankofengland.co.uk/publications/speeches/2009/speech386.pdf

In this speech, Andrew Haldane applied lessons from other disciplines, including ecology, epidemiology and engineering, to consider the financial system as a complex adaptive network. Using network theory, he outlined how the emergence of complexity and homogeneity in the financial network over the past decade had resulted in sharp discontinuities in the financial system. He then went on to suggest three broad areas for improvement in the robustness of the financial network. First, improvements in data are needed, in terms of better data collection, better analysis of the data, and better communication of the results to the public. Second, regulation of the network is needed to ensure appropriate control of the damaging network consequences of the failure of large, interconnected institutions — systemic regulation. Finally, the financial network should be structured so as to reduce the chances of future systemic collapse. Central counterparties, netting-off gross claims within the financial system, and public authority intervention against undesirable structural developments, are possible solutions.

Monetary policy in turbulent times

Andrew Sentance, Monetary Policy Committee member, April 2009.

www.bankofengland.co.uk/publications/speeches/2009/speech385.pdf

In this speech, Andrew Sentance explained how the pattern of recession which has unfolded over the past six to nine months, reflected the compound effect of three major global shocks from commodity prices, the 'credit crunch', and the confidence shock following the collapse of Lehman Brothers. The worst-affected economies have not been those which have seen the biggest rises in credit or house prices, but those which are major exporters of manufactured goods. This illustrates how, in an integrated global economy, a country's vulnerability to recession depends on whether its economy is a large producer of the products where global expenditure is falling. Other features of a more highly integrated global economy might be more volatile commodity prices, more synchronised international business cycles and an increased risk of financial cycles. The solution to these potential volatilities should not be to hold back the process of globalisation but to build a regulatory and policy framework capable of attenuating them.

Remarks by Paul Tucker

Paul Tucker, Deputy Governor, March 2009.

www.bankofengland.co.uk/publications/speeches/2009/speech384.pdf

In this speech, Paul Tucker summarised views on a range of policy issues for making the global and domestic financial system more resilient in future. He defined 'financial stability' to a large degree as being about maintaining the value of private sector money (deposits with banks) in terms of central bank money. Alongside low and stable inflation, that is essential for broader monetary stability. He reviewed a few key issues in microprudential regulation: having supervisors prepared to face down bank management where necessary, but act with restraint; avoiding overly large exposures of any kind; and avoiding business structures that are too complex to supervise, a lesson from BCCI. He emphasised that all banks should hold a core liquidity buffer of high-quality government bonds; and that regular capital should essentially comprise equity, as only it can absorb losses. On the debate about macroprudential supervision, he identified five big issues that need to be resolved: whether the objective should be to dampen the credit cycle; whether it is enough to focus on banks; what the instruments should be; whether the policy should be based on rules or discretionary judgements; whether individual national authorities would need to co-operate or co-ordinate in any way. Finally, he stressed that policy to make the banking system and capital market more resilient in the event of a future bubble bursting, were just as important as taming the cycle.

Tough times, unconventional measures

Spencer Dale, Executive Director and Chief Economist, March 2009.

www.bankofengland.co.uk/publications/speeches/2009/speech383.pdf

In this speech, Spencer Dale described the tough times that the UK economy was experiencing. The pace, breadth and spread of the global downturn suggested that tighter credit conditions were not the only force at work — a widespread collapse in confidence had also played a major role. Nevertheless, there was a substantial stimulus in the pipeline — larger than at comparable stages of previous recessions. The degree of stimulus was not the only difference. The causes of the current downturn were unique and the structure of the UK economy had evolved. These changes highlighted a danger of viewing the current recession through the prism of previous ones. He went on to describe the unconventional measures being employed by the MPC. There were encouraging signs that asset purchases might be having the desired effect. He concluded by noting that the Committee's decisions remained focused on the symmetric inflation target. This target was therefore a natural guide to the exit strategy.

The future of monetary policy

David Blanchflower, Monetary Policy Committee member, March 2009.

www.bankofengland.co.uk/publications/speeches/2009/speech382.pdf

In this speech, David Blanchflower considered the future for monetary policy. He explained that the 'one tool one target' approach of using Bank Rate to target CPI inflation had been inadequate. This approach failed to prevent the build-up of imbalances that presaged the crisis and was insufficient in dealing with failing banks and financial market stress as the crisis developed. There was a consensus that new tools were required to regulate the financial sector and prevent such crises in the future. However, the current problem facing policymakers was that banks were risk-averse. As the costs and benefits of tighter regulation were likely to be least favourable in the aftermath of a financial crisis, it would be prudent to take time in deciding on new regulatory structures. In the near term, monetary policy was likely to remain accommodative given the disinflationary pressure evident in the economy.

Finance: a return from risk

Mervyn King, Governor, March 2009

www.bankofengland.co.uk/publications/speeches/2009/speech381.pdf

In this speech, the Governor discussed the nature of risk in the financial system to draw lessons about the policy responses that are required to ensure greater monetary and financial stability in the future. He considered the design of future banking regulation and the more urgent need to recover from the present crisis.

The Governor stated that at the heart of the crisis was an inability to perceive the true nature of the risks involved, which has been a persistent feature of crises over time. He stressed that regulation should be 'simple and robust'. He argued that, 'To correct these types of market failure will require a system of regulation that effectively marries the 'top down' assessment of the risks to the system as a whole to the 'bottom up' supervision of individual institutions.'

He went on to discuss why these measures should not involve monetary policy being diverted from its role of controlling inflation. Instead, he supported the introduction of additional tools. 'What is needed is an additional instrument… to provide the authorities with the ability to control the growth of the financial sector and its interactions with the wider economy.'

He also spelt out the need to address the weaknesses in the international monetary system that allowed global imbalances — one of the underlying causes of the crisis — to grow unchecked.

Stability, instability and monetary policy

Kate Barker, Monetary Policy Committee member, March 2009.

www.bankofengland.co.uk/publications/speeches/2009/speech380.pdf

In this speech, Kate Barker looked back at the history of UK interest rates, compared with other developed countries, over the period from the start of inflation targeting in 1992 to the financial crisis in 2007. It was concluded that the United Kingdom's real short-term interest rate had been a little higher than the average, and suggested that this might be attributed to the United Kingdom's relative economic stability which had tended to reduce domestic precautionary savings. Looking to the present, she also considered the adverse impact of low Bank Rate on savers and on some financial institutions. Although cuts in Bank Rate at low levels might have less positive effect on the economy, the recent reduction to 0.5% and associated announcement of a programme of quantitative easing, were necessary steps to reduce the risks of an even sharper UK recession and potential deflation.