Bank of England

Edinburgh Speech - Press Conference
29th January 2014

Nils Blythe: So good afternoon, everyone, and welcome to this short press conference. If you could just say who you are and where you're from before asking a question - as you can see, lots of you here, so just a single question. And who would like to ask the first one. Jim?

Jim Naughtie, BBC: The Scottish government's Fiscal Commission said that it envisaged a framework which would allow full flexibility on fiscal policy for an independent Scottish government. What you said seems to indicate that you don't believe that would be possible if a currency union were to work. Can you just take on that question of full fiscal flexibility?

Mark Carney, Governor: Well, I don't think it's appropriate for me to comment directly on anything that the Scottish government has said or anyone from Westminster has said related to these issues. And you can appreciate, what I was looking to do - and hopefully accomplished - was to set out what the core issues were, not just at a high level, but also buttress them with some empirical and certainly theoretical grounding, so others can then delve into them and focus on them.

It is - so I'll make two general points in that context. Obviously - and I'm specifically not commenting on the - where you directed me. Every government - wherever they exist, anywhere in the world - has constraints on their fiscal policy - constraints from markets, constraints from just budgetary realities; and they have to take those into account.

As part of the currency union, which is the issue I was trying to address today, there are additional considerations which may come into play, and on the fiscal side I pointed specifically to this issue around moral hazard - I won't redefine it, it's defined in the speech - and also the role of fiscal policy in smoothing adjustments to shocks, and how that might be best done and has been approached in other instances. But those are judgements for governments to make.

Andy Bell, Channel 5 News: Governor, in a currency union would the Bank of England be the lender of last resort for an independent Scotland?

Mark Carney, Governor: Well, that is one of the issues, Andy, which would need to be determined. And just to be absolutely clear, you know, we are a technocratic institution. We have delegated responsibilities from parliament; we fulfil those remits against those responsibilities and we're accountable to parliament.

We don't make the decisions about those remits; we don't make the decisions about the arrangements in the current union - currency union - in the United Kingdom. We discharge against those decisions to the best of our ability. And so whatever arrangements were put in place, whatever changes were to happen, we would fulfil them.

So the short answer is I can't answer your question, because it's not for us to say.

Faisal Islam, Channel 4 News: Governor, there's Table 4 in the back of your speech compares the Scottish banking system's size to randomly chosen countries - Cyprus, Spain, Iceland and Ireland. Is it the case that you feel that an independent Scotland would be too small to host giant universal banks like RBS?

Mark Carney, Governor: That's clearly not what we said - or I said - in the speech. The sizing of … there is a financial system here which is substantially larger than Scottish GDP, as I mentioned in the speech, and a banking system specifically which is the case. And it brings back the importance of having in place - first and foremost, as you know, which is a point of broader application, Faisal, which is that we - whether Scotland, the United Kingdom, Europe, the US, Canada - we have to end *too big to fail* and we have to finish these various reforms that are being worked through the FSB and the G20 this year. So we have to do that in any regard.

However, even with doing that, there are residual calls on the balance sheet, the national balance sheet, through the central bank, but also an indirect link that becomes very much a direct link because banks tend to hold the debt of their home country, at least in substantial portion. And that needs to be taken into consideration.

Others will judge about the sustainability of that. And I'm not going to provide you with a conclusion on that issue.

Cameron Brooks, Press and Journal: I'm just wondering if you could break down into simple, basic terms what you mean by some ceding of national sovereignty?

Mark Carney, Governor: As used in the speech - well I gave examples of what that would mean. So for example, if as part of a currency union there's an agreement to fiscal rules - let's take the example of the United States - US states balance budget requirements, that is a ceding of state sovereignty, if you will, that is consistent in their system. It's not a requirement, that wouldn't have to be a requirement in all cases, but in their system that's consistent with reinforcing the viability of the currency union in the US. So that would be one example.

Another example would be if there's any pooling of fiscal capacity - so joint backstops for a deposit guarantee scheme, as is being contemplated in Europe.

The bigger question, and I believe that sentence linked, or at least was close to a discussion in the euro area - and this is a big issue for the United Kingdom and a big issue for global financial stability - is that ultimately, in our opinion, there will have to be significant ceding of fiscal sovereignty within the eurozone, in order to make the eurozone a viable currency area. And that's something that is recognised in some circles in Europe, but there's very slow progress at this stage towards that.

Ed Conway, Sky News: It's really following up a couple of these other questions which is to ask that - if you are the central bank and you're issuing the currency which your member countries are using, is it economically preferable in a positive economic sense to be the lender of last resort to those economies, I mean from an economic sense?

Mark Carney, Governor: If the - all countries to a greater or lesser extent have some of their currency used outside of their borders, and so one doesn't want - you know that's not an absolute point. So for example, the Federal Reserve doesn't need to be lender of last resort to the global financial system. It did find itself in a position, however, given - I apologise for the jargon, but it's true - given the sort of currency mismatch position of major banks in funding markets, it did find itself in a position where it was very much in the interests of the United States to effectively, via other central banks, provide close to lender of last resort type facility. It wasn't strictly lender of last resort, but it was sort of extreme liquidity provision over the course of a few years.

That is a difficult position to be in. The Fed absolutely made the right decisions, but that is a difficult position to be in and it's preferable to avoid being in that situation from a structural-entering into that from a discrete decision as opposed to an evolution of the way the system works.

Richard Edgar, ITV News:	Governor, regardless of whether you think a currency union is a good or a bad idea, your speech seemed to indicate that agreeing one would be very difficult. Can you briefly explain why?
Mark Carney, Governor:	Well I didn't mean to suggest that. I merely meant to underscore what the core issues were. And then I would suggest that it's the responsibility of the parties to outline how they would address those issues …
Richard Edgar, ITV News:	There's an awful lot of them ...
Mark Carney, Governor:	… I don't refute those issues as issues or outline how they - but I'd be surprised if the former strategy were successful, quite frankly - but outline how they would address those issues, and then others can judge whether those proposed arrangements would be successful.
Richard Edgar, ITV News:	It was a long list?
Mark Carney, Governor:	The three most important issues, yes.
Glenn Campbell, BBC Scotland:	Governor, if asked, if required, could you as Governor make a currency union between an independent Scotland and the rest of the UK work?
Mark Carney, Governor:	The Bank of England, which is a financial technocratic institution, would implement whatever monetary arrangements were decided to the best of our ability. We would also, as appropriate, provide technical advice and context to those making those decisions. But once decisions are made, we implement this; we're not the ones who are elected to make decisions, very clearly.

David Clegg, Daily Record: Just to pick up on some of the points made there - the timetable for agreeing a currency union is 18 months from a yes vote for independence, according to the Scottish government's timetable. Does that seem realistic given the issues you've outlined today?

Mark Carney, Governor: For others to judge, that's for others to judge.

Paul Gilbride, Daily Express: Governor Carney, you gave three examples - three main examples - for stable, successful currency unions US, Canada and Australia, and you used them very much as a counterpoint to the eurozone. Is it entirely a happy coincidence that those three examples are nation states? If not, what are the reasons why it’s such a stable currency union in those countries?

Mark Carney, Governor: Well, I won’t make a political judgement. From an economic perspective, I think what’s interesting and the point I was trying to make, using the juxtaposition of the eurozone and those others, is that there's - it’s not just about being similar, it’s about the institutions. And so you can be relatively similar.

Now there are - you can disaggregate the eurozone more and there's greater differences, but it’s more similar than one would think in terms of industrial structure, not in terms of productivity differences and things. So you can be similar and it doesn’t work, and you can be quite different and it can work. And so what matters is the institutional arrangements that are put in place around the mobility of factors of production and goods, around various aspects of a financial union, banking union, and obviously fiscal arrangements.

Now nation states put all of those in place. But you will have an attempt - you have an attempt that is very clearly not yet completed at some risk to the global economy - the European and global economies - you have an attempt with the eurozone to put in place a durable currency union - or I should be more positive, to reinforce the currency union, to reinforce the euro with additional measures which will likely require some ceding of national sovereignty, and that's clearly recognised.

But it doesn't - I'll leave it to the political theorists to determine whether at the end of that the eurozone is a nation state as opposed to nation states that have these arrangements which create a truly viable economic and currency union.

Paul Gilbride, Daily Express: So do you not have any examples of any currency unions which aren't nation states?

Mark Carney, Governor: You only get one question; it's a shame.

Laughter

Phil Aldrick, The Times: I'm just going back to the lender of last resort issue. Would the Bank of England be satisfied that banks like Royal Bank of Scotland and Lloyds would be regulated by a Scottish regulator if you were providing lender of last resort facility, given that the opposite has been happening in the UK with the Financial Services Authority being brought in house, it seems to be a retrograde step?

Mark Carney, Governor: I don't think it's helpful for me to speculate on post-September arrangements, so I won't. I'll make the most general point which is that we're obviously very targeted in our provision of lender of last resort facilities. It is that ultimately we're putting - there are protections that are taken, but we are putting the sovereign balance sheet on the line. So we're disciplined in our provision of that. And then we're quite liberal in the provision of the liquidity for all the reasons you would expect, to this specific institution, because we're trying to address a specific liquidity issue. Leave it there.

Peter McMahon, ITV Border: You spoke of tight fiscal rules. What would - if there were a currency union - what are those rules?

Mark Carney, Governor: Well sorry, Peter, that's for others to decide what would be appropriate. You know, I can point you to different examples. I gave the US example which is one extreme. Obviously within the eurozone there were fiscal rules that have proven ineffectual basically because they weren't respected and there wasn't a credible sanction against them.

In Canada there are not fiscal rules per se, but there is a very active form of fiscal federalism, and very large transfers, and large transfers from the federal government to the provincial governments, and also quite a bit of a stabilising aspect to those transfers as well as to employment insurance transfers which compensate for the absence of fiscal rules.

So when you bring that back, it suggests that there are different approaches that could work, but most cases what one finds is that you can either have the more activist federalist approach, and potentially if you have that you don't need the fiscal rule. But it's been a little less successful just to have the fiscal rule without some other arrangement.

Nils Blythe: I think we're out of time, so thank you all very much indeed for coming today.

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