IEA Shadow Monetary Policy Committee: August 2009

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Hold Bank Rate, extend Quantitative Easing (QE), and beware adverse credit 'events' states IEA's Shadow Monetary Policy Committee

Following its latest quarterly gathering on 21st July, the Shadow Monetary Policy Committee (SMPC) voted to leave Bank Rate at 0.5% when the Bank of England's rate setters meet on 6th August. The unanimous SMPC vote reflected the belief that there was no immediate case for a rate increase – although one member thought that Bank Rate could be safely raised to 2% within the next six months - combined with the view that Quantitative Easing (QE) was the most effective monetary policy instrument available. Some SMPC members believed that an additional £100bn to £300bn of debt re-purchases was required once the current programme had run its course. This represented a more enthusiastic view of the case for QE than the greater agnosticism revealed in the July Bank of England minutes, which were published the day after the SMPC gathering.

The SMPC poll was carried out before the UK Office for National Statistics (ONS) announced a very weak second quarter GDP figure, on 24th July. This seemed to confirm the view expressed at the SMPC gathering that the green shoots of recovery might be wilting. However, subsequent e-mail correspondence revealed that some SMPC members thought that the ONS data were too weak to be valid, possibly because of excessive price deflation. A noteworthy aspect of the 21st July meeting was the amount of time devoted to discussing the risks of sovereign default or another major collapse in the international financial sector. Some members feared that the possibility of another adverse credit-market 'event' this autumn should not be ruled out.

The SMPC itself is a group of independent monetary economists who have assembled quarterly at the Institute of Economic Affairs (IEA) in Westminster ever since July 1997. That it is by far the longest established such body in Britain, and meets physically to discuss the issues involved, distinguishes the SMPC from the similar exercises now carried out by several publications. The document that follows reproduces the Minutes of the 21st July gathering followed by the individual votes. The material appears with the permission of the original authors. The final SMPC gathering of 2009 will take place on Tuesday 20th October and its minutes will be published on Sunday 4th October. The SMPC's next monthly e-mail polls will appear on the Sundays of 6th September and 4th October, respectively.

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Minutes of the Meeting of 21st July 2009

Attendance: Philip Booth, Tim Congdon, Ruth Lea, Andrew Lilico, Hiroshi Oka (Embassy of Japan observer), David Brian Smith (Chair), David Henry Smith (*Sunday Times* observer), Peter Warburton (Acting Secretary), Trevor Williams, Hajime Yoshimoto (Embassy of Japan observer).

Apologies: Roger Bootle, John Greenwood, Kent Matthews, Patrick Minford, Gordon Pepper, Peter Spencer, Mike Wickens.

Chairman's comments

October meeting

The timing of the next meetings was discussed and the suggested timing is Tuesday 20st October at 6pm. The chairman then invited Trevor Williams to present the monetary situation.

The Monetary and Economic Background

Stark realities

Despite some encouraging signs of stabilisation in recent months, the stark reality is that global economic growth has fallen sharply and the downturns in advanced, emerging and developing economies are synchronised. For advanced economies a GDP decline of 4% is probable for 2009, while emerging and developing countries may experience mildly positive growth of the order of 2%. The UK has experienced its first recession in sixteen years with the slowdown led by the corporate sector. A sharp inventory correction has been achieved through the reduction in manufacturing output to levels more than 10% below a year earlier. However, signs of recovery have appeared in recent months, lifting the construction sector Purchasing Managers Index (PMI) from sub-30 readings to the mid-40s; manufacturing PMIs from around 35 to 47 and services PMI from 40 to 52. UK manufacturing output is no longer falling and CBI output expectations have risen markedly in the past three months. As yet, measures of business and consumer confidence have recorded slender gains from the early-year lows.

Business confidence is improving, but with marked differences between sectors and regions

The latest Lloyds TSB (*Business in Britain*) survey reports a marked recovery in business confidence based on firms' expectations of orders, sales and profits over the next six months. Regionally, the most positive reading is for London and the most negative are for the Midlands and the South East. By sector, the most resilient is business services and the most vulnerable were construction and retail. There was also a clear differentiation of confidence between small and larger businesses. Those with annual turnover of under £5m reported negative balances whilst those with more than £50m turnover showed more positive readings.

Housing and retail sales

There are tentative signs that the UK housing market may have stabilised with a pickup in mortgage approvals. The volume of UK retail sales is lower than a year ago but the CBI retail survey suggests that an improvement is close at hand.

IMF study reveals financial crises protract downturns

There has been considerable interest in the parallels between the current economic downturn and its predecessors. An International Monetary Fund (IMF) study of 122 recessions reveals that downturns linked to financial crises are more protracted and the subsequent recoveries are more gradual than for 'normal' recessions. Examining the experiences of Scandinavia in the early 1990s and Japan from 1997, suggests that lending growth takes three years to return to positive territory. Another factor bearing down on the prospects for economic recovery is the high level of indebtedness of UK households and non-financial corporations. A desire to limit these exposures may make the private sector less willing to borrow.

Liquidity

The latest data show a decline in the pace of OECD monetary growth to around 7% per annum with further declines in prospect. Meanwhile the central banks have created liquidity to varying degrees. Indexing the size of each central

bank's balance sheets to 100 in January 2007, the Bank of England leads the way with 270 followed by the US Federal Reserve at around 230. The European Central Bank (ECB) has risen to 170 while the Bank of Japan scores slightly less than 100. It was observed that headline measures of broad money growth are well in excess of the increase in nominal GDP, suggesting a relaxed stance of monetary policy in all of the four contexts referred to above. There has been considerable discussion regarding the use of an adjusted series for the UK M4 money supply, with the adjustment removing the effect of intermediate other financial institutions (OFI) transactions. This measure is currently showing annual growth of less than 2% as opposed to more than 14% for the headline M4 series.

Loose monetary policy is not a short-term inflation threat, but may be a long-term one

Trevor Williams inferred that loose monetary policy is not a short term threat to inflation but may be a long term threat. Similar inferences were made for the US, the EU and Japan. A disaggregated comparison of trends in bank lending for these countries reveals that lending to non-financial corporations and households has decelerated everywhere apart from Japan. However, there is an anomaly regarding lending to other financial companies where the UK trends are strongly positive but the US, Japanese and EU trends are negative. This was attributed to the severity of the securitisation crisis in the UK. It was observed that the Customer Funding Gap (CFG) remained at a high level of £800bn, of which foreign banks accounted for approximately half. The gradual downsizing of foreign banks' lending activities in the UK has rendered the government's targets for incremental lending superfluous as UK banks cannot readily increase their lending to those borrowers who lose access to a foreign bank. In short, the UK has been borrowing abroad and now that foreign flow has fallen the costs of borrowing have increased and the supply diminished.

Exchange rates

On the basis of relative money supply growth differentials, Trevor Williams observed that Sterling appeared significantly undervalued in relation to the US Dollar; the Yen was overvalued in relation to the US Dollar, and the Euro was significantly overvalued in relation to the US Dollar.

Availability of credit is slightly improved

The Bank of England has recently released a new quarterly survey of trends in lending. The availability of credit to UK borrowers in the form of mortgages has improved since the extreme negative readings of a year ago. A more recent improvement has recently occurred in respect of households' unsecured borrowing and for corporate borrowing. The survey indicates that the availability of credit is expected to improve further in the next three months, especially for corporate borrowers. The default rates on loans remain a serious concern, particularly for mortgage lending. Correspondingly, lending spreads are expected to widen for personal borrowers in the next three months. Net funds raised by UK businesses from all sources have turned positive in the most recent month (May) with equity and bond issues more than offsetting the reduction in bank borrowing.

Discussion

Global banking sector still at risk

Risks of further institutional default and...

The Chairman thanked Trevor Williams for his thought-provoking and thorough presentation and then threw the meeting open for discussion. In response, Andrew Lilico stated that he was concerned that there might be a repeat of the credit market difficulties of last September. He wondered whether refinancing problems could trigger another major failure in the financial system. He observed that such an event would cast extreme doubts on the usefulness of bank stress tests and illustrated his concerns by the example of Ireland. Trevor Williams agreed that this was conceivable and suggested that the risks were evenly balanced. Peter Warburton thought that a repeat credit market 'event' was rather less likely on the basis that the declaration of losses in the global banking system had evolved to the point where approximately 70% of potential losses

had occurred. The greater visibility of banking sector problems, notwithstanding the lack of transparency in the European banking system, has reduced the likelihood of a major credit shock. Tim Congdon commented that the widening of net interest margins is allowing banks to rebuild their capital. As asset values recover, this would also allow banks to write back some of the loan loss provisions that they have made.

...even sovereign default in the EU fringe

Andrew Lilico then raised the issue of prime defaulting in the US or European contexts, should deflationary forces persist. Tim Congdon drew the distinction between internal and external debts. Internal (e.g. between local residents and government) debts were easier to deal with through the reflation of the asset collateral. He acknowledged that external debt presented a more significant problem, citing the predicaments of Latvia, Lithuania and Ireland which lack the ability to reflate away external currency debt. Andrew Lilico suggested that a bout of wage deflation could trigger a default crisis in Ireland. Tim Congdon agreed that banking losses were often associated with a declining standard of living - for example Iceland's banking losses represent between 50% to 100% of GDP - and an implied reduction in living standards over an extended period unless there is a dramatic easing of policy. Trevor Williams wondered whether the Irish banks would be supported by foreign parents or whether the losses would be absorbed by the Irish government. The discussion was broadened to consider the implications of default in Eastern Europe where much of the debt was denominated in foreign currencies. Tim Congdon noted that if governments assume the debts of the banking sector then they may risk sovereign default, as almost happened in South Korea in 1997.

Germany could bail out its smaller neighbours, but its voters do not want to do so

David Brian Smith suggested that there was a difference in kind between the very small EU members who could be bailed out by their larger neighbours without too much trouble and the larger ex-communist nations where this would not be practical. Ultimately, this depended on the political decisions of Germany. German politicians would not want trouble in their own backyard but almost three quarters of the country's electorate appeared to oppose bailing out other countries according to recent polls. He then said that the dilemma from a forecasting perspective was that there was a strong risk of OECD deflation in the short term, based on an output-gap analysis, but the excessive growth of broad money in relation to trend output implied an inflationary outlook in the medium term. He added that the shortfall of OECD industrial output about its trend in the first quarter of 2009 was twice as large as in any previous recession since the early 1960s. At the same time, OECD broad monetary growth in the year to April was a reasonably robust 7.7% - or 7.4% if high inflation countries were excluded. A 'P-Star' calculation for the OECD area as a whole suggested that the region's broad money growth was currently funding trend inflation somewhere in the 4% to 5¼% range.

Measurement problems with the UK monetary aggregates

Tim Congdon countered that the growth of broad money is not rapid in the UK once interbank transactions have been netted out. Following the implementation of Quantitative Easing (QE) he believed that the underlying growth of M4 was about ½% a month. David Brian Smith commented that there were inconsistencies in the Bank of England's monetary data that clouded their interpretation. We were now in the unfortunate position of using QE to stabilise a monetary aggregate, M4 less Other Intermediate Other Financial Corporation (OIOFC) Deposits, where the monthly figures differed from the quarterly data and the levels data were inconsistent with the published changes. He had discussed the matter with the Bank's data compilers. The conclusion seemed to be that the best way of putting a consistent broad money series together was to subtract the Bank's estimate of OIOFC deposits from the break-adjusted M4 series available on the Bank's statistical data base. He hoped to carry out statistical research using this measure in the near future. Tim Congdon then questioned the accuracy of the adjusted M4 growth series in Trevor's

presentation, which had used the Bank's estimates, arguing that there had been a distinct monetary acceleration in 2006-07, driven by corporate sector deposits.

Funding policy

Andrew Lilico suggested that if the Bank of England drew its QE program to a close that there may be a funding problem for the government. Tim Congdon disagreed, asserting that the government can always borrow directly from the banks. He queried the implementation of QE, whereby the banks accumulate bank reserves at the Bank of England. He asked why the government could not borrow directly from the banks without inflating the Bank of England's balance sheets. He pointed out that monetisation can occur in the presence or absence of a large government deficit; it was not necessary to monetise new borrowing. Andrew Lilico reiterated his concern that public spending might be encouraged by the QE program. David Brian Smith said that the golden era of Open Market Operations (OMOs) in the 1920s occurred because there was a large stock of government debt left over from the Great War, which could be bought or sold according to the needs of the economy by the central bank, at the same time as a credible balanced budget rule and commitment to the gold standard meant that bond holders did not have to fear that expansionary OMOs/QE posed a longer-term inflation threat. The empirical evidence for both the UK and the US suggested that sustained debt sales of 1% of national output eventually raised the real long-term government bond yield by some 0.2 percentage points. The scale of the prospective fiscal imbalances in Britain and the US suggested that real bond yields could rise to the point where increasing debt servicing costs lead to an aggravation of budgetary problems.

Change in market expectations about QE

The *Sunday Times* observer, David Henry Smith then commented that market expectations have changed appreciably since the MPC declined to take up the remaining £25bn of asset purchases at the July meeting. There is a presumption that the MPC would not have paused without good reason and that this will become clear when the August *Inflation Report* is released. Regardless of whether this marks the end of QE, there has been a marked shift of expectation as to its longevity.

Concerns over US exit strategy

Peter Warburton thought it important to consider the US context of QE, where the US$1.75trn programme of asset purchases was approximately half-completed. It seems likely that the Fed's balance sheet will grow materially over the coming months as offsetting factors (the run-off of short-term funding instruments) become less significant. US bank reserves have been falling in the past three months, suggesting that more lucrative uses are being found for the funds. The initial indications are that the seeds of a monetary acceleration have been sown. Parallel concerns over the Fed's exit strategy have prompted Fed chairman, Ben Bernanke, to submit a long explanation in an article in the Wall Street Journal (21st July).

Wilting 'green shoots'

Roger Bootle commented (by an e-mail submission circulated in advance of the meeting) that there are already signs that the "green shoots" of recovery are starting to wilt, with May's drop in industrial production being a prime example. Indeed, there are several reasons to doubt that a strong and sustained recovery is on its way. A severe fiscal consolidation was looming, probably involving both tax rises and public spending cuts. Banks were likely to remain cautious about lending for some time yet, not least because a raft of recession-related bad debts was heading their way. Slowing pay growth was offsetting any boost that falling inflation might have given to households' real incomes. And the real benefit from the lower pound was unlikely to be felt until global demand strengthened significantly. Even if the recovery did turn out to be stronger than he expected, it would take a prolonged period of rapid economic growth to use up the large amount of spare capacity that was building up in the economy – even accounting for the fact that the credit crunch had probably knocked potential output. Accordingly, deflation, not inflation, would remain the big risk for some time.

Votes

Votes are listed alphabetically

The Chairman then asked each member to make a vote on the monetary policy response, apart from Roger Bootle who had submitted his vote earlier (by e-mail). In addition, to Roger Bootle's submission there was a need for a second *vote in absentia*, since only seven SMPC members had been present at the meeting. This was provided shortly after the meeting by Patrick Minford. The votes are listed alphabetically rather than in the order they were cast, since the latter simply reflected the arbitrary seating arrangements at the meeting. The Chairman traditionally votes last.

Comment by Philip Booth

(Cass Business School)
Vote: Hold
Bias: Neutral

Unease over operation of QE

Philip Booth expressed unease at the way the policy of QE was operating. He believed that the government should give the Bank of England free rein on the extent of QE, which should be set in order to deliver the appropriate growth of the money supply. The government's role should be to monitor and set limits on the sorts of assets that are bought as a result of QE because the taxpayer ultimately underwrites the risk. Still lacking is a coherent strategy as to the purpose of QE, its predicted effects, its relationship to the inflation target and the framework for deciding when the policy should be reversed.

Comment by Roger Bootle

(Deloitte and Capital Economics)
Vote: Hold
Bias: Neutral on rates but announce £300bn increase in QE

Deflation is immediate risk, not inflation

Roger Bootle believed that deflation, not inflation, will remain the big risk for some time and that interest rates should be kept at their record low level of ½% for a sustained period and that QE should be extended further. The MPC should start by using the last £25bn of the £150bn originally sanctioned by the Chancellor. It should also ask for this upper limit to be raised, given that he thought that it will probably have to do more than £150bn of QE in total. Indeed, in order to convince the market that it is prepared to do whatever it takes, the MPC should ask for a huge amount of extra QE, perhaps well in excess of what it thinks it is likely to do, say £300bn, and then proceed to do QE steadily in £25bn slabs.

Comment by Tim Congdon

(International Monetary Research Ltd.)
Vote: Hold
Bias: Neutral

DMO should be re-integrated into the Bank

The policy of QE should be extended to the full amount agreed (£150bn) and the Bank of England should be given the option to extend by another £50bn by October. The purpose of QE is to achieve a steady positive growth in the quantity of money held by household and non-financial companies. The advent of QE has thrown into serious doubt the relevance of the remit of the Debt Management Office (DMO). It was time to consider transferring the DMO's functions back to the Bank of England, which had successfully managed the gilt-edged market from 1694 to 1997, in order to ensure that official operations in the government bond market were not at cross purposes, as at present, and compatible with the broader needs of monetary policy.

Comment by Ruth Lea

(Arbuthnot Banking Group)
Vote: Hold
Bias: Neutral but extend QE

Deteriorating economic outlook

Ruth Lea's assessment of the economic outlook has grown more pessimistic in recent months due to the lack of visibility of drivers for growth. With unemployment rising, personal balance sheets in disrepair, a prospective increase in VAT from January and higher rate income tax in April next year, her concern was widespread. She had no concerns on the re-emergence of inflation for the foreseeable future and supports the continuation of QE and believed an extension of the policy should be considered.

Comment by Andrew Lilico

(Europe Economics)
Vote: Hold
Bias: Neutral on rates but extend QE by £150bn

Fears of a double-dip recession

In view of the risk of a repeat adverse 'event' in the credit system, and the associated risk of a second dip in economic activity, it was appropriate to carry on with QE and seek permission from the Chancellor for another £150bn of capacity in Andrew Lilico's view. He remained concerned that deflation risk had not been eliminated. During the course of this crisis, the inflation target had lost credibility and his preference was to shift to a price level target for the duration of QE. Andrew Lilico remained concerned at the absence of a coherent exit strategy from QE.

Comment by Patrick Minford

(Cardiff Business School, Cardiff University)
Vote: Hold
Bias: Neutral on rates and continue with QE

Role of policy as worst of crisis is over

Patrick Minford stated in his e-mail submission that, based on the Cardiff model of the economy, we should be observing a turning point after the crisis. Indeed, this is what we were seeing, with the usual variations between regions and countries. Unusually it was China - where QE has been most striking and determined, with state-mandated credit revival - that had lead the recovery. He had argued before that fiscal 'packages' must be seen as essentially credit packages, not conventional fiscal policy 'stimuli' (which were probably quite ineffective normally). In a credit crisis, the only agent able to provide the credit that was unavailable from the banks and the markets was the taxpayer. While central banks provided cash to the markets in exchange for whatever assets the markets could offer – they were permitted to do so because the taxpayer picked up the risk on those assets - governments themselves were providing credit and capital to the banks and the private sector via their greatly increased deficits. These deficits were a form of credit because they had to be paid off in due course through cuts in spending or higher taxation. This overall provision of credit by the government, whether through the central banks or directly, has been vital in staunching the wounds caused by the credit crunch.

Exit strategies

The issue now was turning to the timing of 'exit strategies'. Patrick Minford's view was that the priority was to consolidate the still highly fragile recovery. Indeed, credit growth was still low or even non-existent in wide swathes of the world. This implied that the creation of money in exchange for a wide variety of assets in short demand (QE) must be continued vigorously. In this respect, he was alarmed by the tepid attitude of the Bank in indicating that QE may not be extended beyond the current limits set by the Treasury. Since the lags in effects from both the credit shock and the response were quite short, a matter of two or three quarters to their peak effect on both output and inflation, it was a mistake

to dwell on exit strategies when we had yet to see through the recovery process. Once the recovery was quite assured there would be plenty of time to put into effect the necessary tightening of money supply that will raise interest rates once more and prevent any inflation resurgence.

Inflation targeting framework means that an exit strategy is already there

It has been said that the lack of an exit strategy threatened a resurgence of inflation. This was true, but there was an explicit exit strategy in the UK and in most major economies: this was inflation targeting according to whose logic money will automatically be tightened to achieve target inflation. There was really no need to do anything other than reiterate that this structure remained in place. Despite the loose talk of how nice it would be to use inflation to soak up rising government debt, there had been no official encouragement of this view. Politically, inflation targets remained popular everywhere. There was no reason to expect governments to sacrifice their popularity by using the 'inflation tax'. He had been struck by debates in Europe and the UK where it had simply been assumed, without explicit discussion, that inflation targeting was in place .As far as fiscal policy was concerned, this was integral to the revival of credit. Here too premature tightening and panic about debt levels was misplaced. Fiscal policy should remain as it was until recovery was assured. There should then be a careful and measured return to fiscal balance, with the debt overhang allowed to be reduced naturally by future cyclical improvements. His conclusion was clear: an exit strategy was there and would be implemented calmly as conditions changed. Meanwhile, it was essential that current policies to restore recovery continued with determination.

The longer-term prospect

However it by no means followed that the recovery would be strong and vigorous or 'V-shaped'. In Patrick Minford's view this was unlikely because of the fundamental reason for the growing problems in 2007 and 2008 that brought the world boom shuddering to a halt and precipitated the financial conditions that brought Lehman down. This reason was the acute and growing shortage of raw materials in the face of the huge growth of China and its satellites. As the world economy recovered this shortage would reappear, indeed that was already visible in rising commodity prices. Unfortunately this shortage was not quickly or easily remedied. It required major technological change that cut the use of raw materials per unit of GDP, as occurred after the oil crises of the 1970s and 1980s. Extra supplies of raw materials may be brought on stream with a lag but the main need was to curb demand. This could take a decade to come to fruition. Hence we should expect growth to be held back until this has happened. Capacity that was viable at the old raw material prices will prove uneconomic at the new ones; cars, aeroplanes, factories etc. will need to be replaced with more resource-efficient ones.

Policy Conclusion

The Cardiff forecasts looked for a resumption of growth but not back to the same path that we were used to in the mid-2000s. It seems likely that there had been a permanent loss of capacity and that there would be slower growth from that lower level. The policy conclusion was that interest rates should be kept on hold with no bias either way. QE should continue at current rates of growth in assets until there was a revival of credit and core M4 growth. Since the exit strategy was already in place: no further discussion of it was required other than to emphasise and explain what inflation targeting already implies.

Comment by David B Smith

(University of Derby and Beacon Economic Forecasting)
Vote: Hold
Bias: Neutral

Lessons from the inter-war period

David Brian Smith thought that there were still lessons to be learnt from the successful policy combination operated by the UK in the 1930s and contrasted this with the policy mix today. In the 1930s, the UK abandoned the gold standard early, and combined a tight fiscal stance with a loose monetary policy. This had

the effect of crowding in private sector activity and minimising the economic damage caused by the collapse in overseas demand for UK exports. The undesirable aspect of interwar policy was the state-sponsored cartelisation of the British economy, whose adverse supply-side legacy lasted until the 1970s. David Brian Smith considered that the fiscal-monetary policy mix was less intelligent today but the interventionist instincts are no less prevalent. He expected mildly negative inflation rates in the UK and the OECD over the next three years and was unconcerned about inflationary risks over the next year or so. He was agnostic on the case for an extension to QE and would like to see more research on the transmission mechanism of the policy. He regretted the poor quality of the monetary data which stood in the way of clear analysis. Without better indicators of the underlying monetary stance, he believed that policy was flying blind to an undesirable extent.

Comment by Peter Warburton

(Economic Perspectives Ltd)
Vote: Hold
Bias: To raise Bank Rate over the next six months

An urgent and significant tightening of the fiscal stance is required

During the next six to twelve months, nominal economic activity is likely to be bolstered by the heady combination of low interest rates, QE, credit guarantees, special liquidity provision, accommodative fiscal policy and a weakened exchange rate. A powerful, but temporary, rebound in activity is probable as the UK participates in a global rebuilding of inventories and a partial recovery of industrial output and exports. However, the structural issues have yet to be addressed and de-leveraging is a prospect not a fact. The greatest threat to the UK economy in this interim phase is a further widening of the budget deficit which could undermine sovereign credit perceptions and the willingness of foreigners to hold sterling assets. An urgent and significant tightening of the fiscal stance is required, in the context of the extension of the QE policy for another year. In current circumstances, Bank Rate at ½% confers little benefit to the financial system and could safely be raised towards 2% without jeopardising the economy.

Comment by Trevor Williams

(Lloyds TSB Corporate Markets)
Vote: Hold
Bias: Neutral but expand QE by a further £100bn

Large output gap means that inflation will ease in short term

The remaining £25bn of QE should be used and the scope of QE should be expanded by a further £100bn. In view of the large output gap, inflation should be expected to fall in the short term, reinforced by de-leveraging in the personal and corporate sector. Trevor Williams supported a faster pace of money supply growth in the near term but shared concerns around the practical issues of unwinding QE over the coming years.

Policy response

1. The committee voted unanimously to hold Bank Rate at its current ½%.

2. One member had a bias to raise Bank Rate within the next six months. All the others had a neutral bias, in part because of the uncertainties involved.

3. There was a widespread view that QE needed to be extended, although there was disagreement as to the precise amount involved.

Date of next meeting

Tuesday 20st October 2009

Note to Editors

What is the SMPC?

The Shadow Monetary Policy Committee (SMPC) is a group of independent economists drawn from academia, the City and elsewhere, which meets physically for two hours once a quarter at the Institute for Economic Affairs (IEA) in Westminster, to discuss the state of the international and British economies, monitor the Bank of England's interest rate decisions, and to make rate recommendations of its own. The inaugural meeting of the SMPC was held in July 1997, and the Committee has met regularly since then. The present note summarises the results of the latest monthly poll, conducted by the SMPC in conjunction with the *Sunday Times* newspaper.

SMPC membership

The Secretary of the SMPC is Kent Matthews of Cardiff Business School, Cardiff University, and its Chairman is David B Smith (University of Derby and Beacon Economic Forecasting). Other current members of the Committee include: Roger Bootle (Deloitte and Capital Economics Ltd), Tim Congdon (International Monetary Research Ltd.), John Greenwood (Invesco Asset Management), Ruth Lea (Arbuthnot Banking Group), Andrew Lilico (Europe Economics), Patrick Minford (Cardiff Business School, Cardiff University), Gordon Pepper (Lombard Street Research and Cass Business School), Peter Spencer (University of York), Peter Warburton (Economic Perspectives Ltd.), Mike Wickens (University of York and Cardiff Business School) and Trevor Williams (Lloyds TSB Corporate Markets). Philip Booth (Cass Business School and IEA) is technically a non-voting IEA observer but is awarded a vote on occasion to ensure that nine votes are cast.

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