BOOK REVIEWS

Unelected Power: The Quest for Legitimacy in Central Banking and the Regulatory State

by Paul Tucker. Princeton University Press (2018), 642 pp. ISBN: 978-0691176734 (hb, £27.00); 978-1400889518 (Kindle edn, £17.61).

Paul Tucker was a central banker at the Bank of England for over 30 years. Readers of this book would therefore expect it to deal with central banks and what is known as their independence as well as with their legitimacy. They would not be disappointed, but the book ranges much more widely, dealing from various angles with the tendency of the modern state to delegate tasks to agencies which are to some degree distant and insulated from political pressures. It is a fascinating and thoughtful book, and well and clearly written.

The book has an admirable introduction, laying out clearly and succinctly the contents of the following four sections. Indeed, the introduction is so clear that it would be easy for readers in a hurry, or with narrow interests, to turn to the section of most interest for them and ignore the rest. Though possible, that would not be sensible, not only because there are interesting ideas throughout, but also because there are interconnections, each section being symbiotic with the others. But, to summarise despite that warning, the four sections that follow the introduction deal with the development of an 'administrative state' which delegates to independent agencies, the democratic legitimacy of independent agencies, incentives under different constitutional forms (and very important, the limits on what good design of agencies can achieve), some practical problems for such agencies, and finally central banks. All are interesting, enjoyable, and instructive.

Nevertheless, with a book so substantial in the physical as well as the intellectual sense, a reviewer must choose his focus. My choice is first to consider what prompted the book, then to turn to what Tucker writes on central banking. I conclude with a brief consideration of whether some of the problems he identifies are capable of being avoided completely and do not actually need solution.

The preface starts with a quotation: 'Of course, if the Bank were ever given monetary independence, you would need to lose bank supervision in case you became an over-mighty citizen.' Tucker quotes these words from Terry Burns to Robin Leigh Pemberton (then Governor of the Bank), and I have no doubt about their accuracy, because, unlike most such quotations, the author was there when these words were spoken, and taking notes in his capacity as private secretary to the Governor. Since then, the Bank has become independent for monetary policy, lost supervision, and gained it again. Throughout these events, Tucker writes, the Bank wanted to avoid becoming an 'over-mighty citizen'. This was to help the Bank to 'enjoy legitimacy'. That is a sensible objective. But if we think about the origins of the concept of an 'over-mighty citizen', we are led to another way of achieving the Bank's desired legitimacy.

The term is used for a problem which developed in the late feudal period. 'Over-mighty citizens' were lords whose wealth and military strength let them ignore and even possibly overthrow the monarch. That was manifestly destabilising to the state. There is no question of the Bank doing that. But allowing it to accrue great powers presents a problem at least as serious but, so to speak, in the opposite direction.

When central banks emerged – the Bank of England in 1694, with many others following in the nineteenth century – they were charged with raising funds for the state. (This is when they were government banks rather than central banks.) But they soon developed a form of what may be called customary independence. So long as they behaved according to a well understood set of rules the state did not interfere. These rules were the gold standard, to maintain monetary stability (stable prices over the medium term) and financial stability, by acting as lender of last resort to the banking system. The carrying out of these two tasks is what defines the archetypal central bank. But the responsibilities given to central banks in recent years have stretched the meaning of maintaining financial stability so far that central banks are potentially back under the control of government at any point.

Avoiding that situation was a concern of the Bundesbank's from soon after its foundation. That was why it carefully preserved the appearance of distance from the German Federal Banking Supervisory Office – because it feared that if a bank under its direct supervision failed, as banks surely would, that would damage the Bundesbank's reputation for competence, and thus weaken it in arguments over monetary expansion and inflationary finance. To that well justified fear others have been added. The definition of financial stability has been broadened well beyond what can be achieved by the traditional lending in a crisis to any bank which brings in suitable collateral. For example, one definition (from a senior central banker) is: '.. . financial instability could be defined as any deviation from the optimal saving–investment plan of the economy that is due to imperfections in the financial sector' (A. Haldane et al., 'Financial Stability and Macroeconomic Models', *Bank of England Financial Stability Review* 16, 2004, pp. 80–8). A totally non-operational definition. What is the optimal plan? How big a deviation? What are imperfections in financial markets? How do we recognise them? The central bank is bound to fail, for it cannot know what the task is. We have seen the rescuing of individual banks by providing them with capital. As central banks seldom have the capital for this, they had to ask their owner, almost invariably the government (the major exception is the Fed) for some. We now have resolution regimes and ring-fencing designed to allow big banks to be closed in an orderly fashion. Let us see if governments hold their nerve when it comes to using these devices. Central banks have engaged in actions which involve them deciding who to assist and who not. For example, it was reported recently that the Bank of England had urged a large financial institution to choose an auditor other than the one it wanted, on the grounds that the proposed one did not have the resources for the job.

Central banks have been drawn into a morass. They are involved in taking decisions which, if they are to be taken other than by those directly involved, are properly for elected politicians. They are perpetually at risk of being dependent on governments for forgiveness. They may from time to time need to call on them for capital. Such a situation of dependency, as the Bundesbank knew over 50 years ago, is not a recipe for monetary stability.

This is a good book. But it would have been a better one had it included a substantial and critical analysis of the current design of mandates for independent agencies. That is admittedly a slightly odd complaint from a reviewer who noted the book's already considerable size. I hope, therefore, that its author has a second book in progress.

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