Non-Fiction

Who do ‘rock-star’ central bankers answer to?

National banks have become bulwarks against crisis — and in effect gained the power to pick winners and losers

Mark Carney, the governor of the Bank of England © Bloomberg

Desmond King MAY 10, 2018

In *Ashes and Diamonds*, Andrzej Wajda’s film set in war-torn Poland on May 8 1945, the young assassin dispatched to eliminate the party secretary Comrade Szczuka muses to his superior that “everyone’s got to be responsible to somebody”.

Wajda’s observation captures the essence of Paul Tucker’s important reflections in *Unelected Power*. Tucker wonders: to whom are central bankers responsible? How is oversight of their discretionary authority monitored in a democracy? Can central banks remain legitimate as they choose financial winners and losers?

A former deputy governor of the Bank of England, Tucker is well placed to address these urgent questions 10 years after the greatest economic recession since the 1930s threatened to destroy the global financial system. After spending billions of pounds on quantitative easing — the Bank’s purchase of bonds and securities — and on supporting lenders, central bankers have broken free of the traditional limits on their action. They not only use monetary policy to adjust interest rates but through their non-conventional measures impinge on the fiscal policies traditionally controlled by elected politicians. Far from operating on the fringes of everyday life as disinterested experts, central banks now make decisions that affect every household, in effect choosing winners and losers.

Tucker is refreshingly upfront about central bankers’ acquisition of power. He queries “whether and how democratic societies can” cope with the challenges posed by the scale of “unelected power” concentrated in nominally independent central banks. Indeed, such is the scale of monetary intervention that it threatens not only to erode central bank legitimacy but “even that of our democratic system of governance”.

Central bank salience is novel. For decades they were boring and respected institutions. One former chairman of the Federal Reserve famously described central bankers’ job as removing the “punch bowl” once the party got going. All this changed dramatically and irrevocably in September 2008. Citizens and bankers sat transfixed as the financial behemoth Lehman Brothers collapsed, rattling equity and credit markets. Overnight central banks became bulwarks against crisis.

Ten years on from the crisis it is plain that the most affluent recovered faster than the middle class

Financial disaster stirred urgent questions. For some, central bankers are heroic rescuers, for others outfoxed regulators.

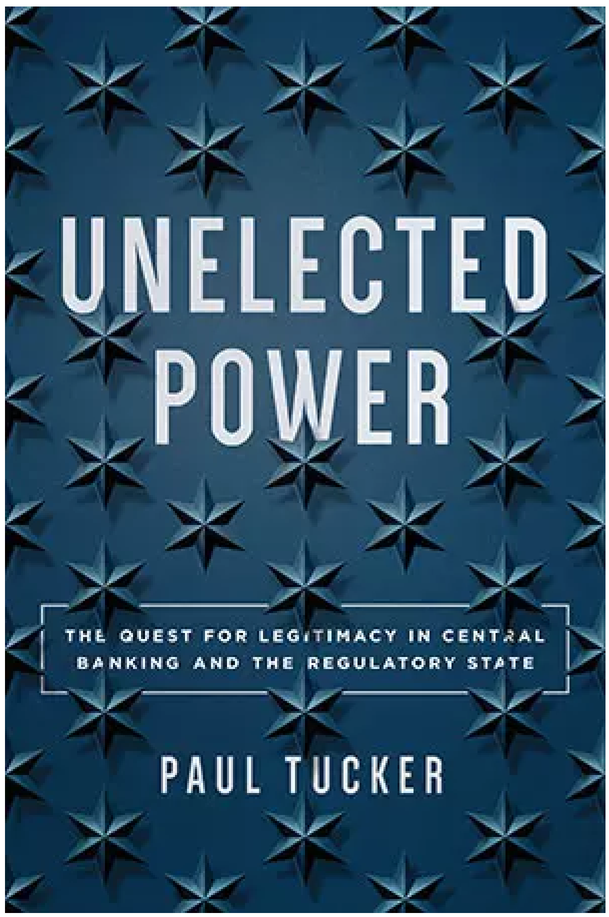
The implications of these and other questions were damped by a sense of relief that central banks stymied a classic run on financial institutions that had the potential to create the second great depression in a century. But a deeper issue could not be ignored as Tucker hints at: central bankers helped everyone by stopping massive job losses and business failure but assisted some more than others. Now that a decade has passed since the 2008 crisis, it is plain that the most affluent members of western democracies recovered faster and to a greater extent than the middle class and certainly far more than the least well-off, who lost more and are still struggling to recover to their pre-2008 levels.

Tucker has the courage to question whether central banks can both produce policies that create losers and continue to make claims for independence. He asks how the “legitimacy of delegating power to unelected officials” can be made democratic. This question, which has exercised political philosophers and applied economists for centuries, explains the book’s corpulence as the former banker engages with a vast scholarship on delegation, legitimacy, regulation and accountability to explain why democracies create independent central banks. He proposes Principles for Delegation to include “a clearly articulated regime, simple instruments, principles for the exercise of discretion, transparency that is not deceptive, engagement with multiple audiences, and, most crucially, testimony to legislative committees”. When granted independence in 1997, the Bank of England satisfied these criteria.

Twenty years on events have profoundly changed matters, as *Unelected Power* unflinchingly recognises. Tucker describes how massive central bank activity has become. For instance, until 2010 private banks For instance, until 2010 private banks leaving their money overnight at the

Bank received no interest. In response to the crisis, the Bank, like the Fed, started paying interest on these deposits. This expanded the central bank balance sheets as they tried to boost liquidity. Tucker recounts that when he first suggested such payments “the response of one of my closest colleagues was along the lines of ‘bloody hell’”.

Quantitative easing has been good for those with shares and stocks, boosting their incomes. Many people don’t own shares. Low interest rates are punishing for people with savings. Most people are savers. A recent Bank study describes QE effects as including the largest redistribution of wealth across UK households ever, augmenting the wealthiest 10 per cent to the tune of £350,000 per household. This skewed largesse vividly illustrates Tucker’s claim that central banks no longer exist in a technocratic and neutral “rarefied zone” but are “overmighty citizens”.



Undoubtedly central bankers want to see themselves as neutral experts relying on technocratic tools, leaving tax policy and its effects on household incomes to the ideological clashes of politicians in national legislatures. But under policies such as QE and the undoubtedly pusillanimous inaction of many elected governments, this distinction has faded. In response, Tucker recommends co-ordination with the state when QE-type measures are implemented. It is doubtful that his prudent criteria for such co-ordination will survive in a crisis when these “overmighty citizens” are the centre of the storm.

Unelected Power bristles with ideas and proposals. Tucker appreciates that central banks are losing their legitimacy and becoming a target for opportunistic politicians and unscrupulous populists. He wants a “healthy, legitimate” central bank. Setting aside many turgid debates, Tucker argues that the “most compelling reason” for independence is to “enable governments to save paying an inflation risk premium on their debt”. This disarmingly simple benefit is a major “public interest” effect of the decision to make the Bank independent. Nonetheless, he is candid in doubting central bank independence as a holy grail: “when my friend and former colleague, Bundesbank director Andreas Dombret suggested in the autumn of 2016 that central bank independence is not debatable, my immediate thought was that these institutions are among the last on earth that need ‘safe spaces’ to protect them from criticisms or verbal attack”.

Behind this discussion of status lurks Wajda’s anxiety about responsibility. For Tucker it is governments not bankers who must take responsibility to ensure that prospective losers are “represented at the decision-making table”. This is an audacious and probably unachievable expectation in the world of modern central banking and a huge financial industry where the networks between banker and investor are deep and consequential. This interlayering was exposed in the Libor debacle between Sir Paul and Bob Diamond, chief executive of Barclays bank, in October 2008, when a series of phone calls and memoranda regarding the key lending benchmark descended into comical misunderstandings about “who said what” worthy of an Evelyn Waugh novel. As Tucker later told the Treasury select committee: “we thought [the Libor system] was a malfunctioning market, not a dishonest market.”

And therein is the nub. Just as in the pre-2008 world of Fed policy and subprime mortgages, Sir Paul’s remarks in parliament suggest that the regulators and bankers were either genuinely talking past each other or following distinct priorities of interest-rate setting versus profitmaking. In *Ashes and Diamonds,* Wajda’s anti-hero is immediately held responsible for his action, quickly pursued by a mob minutes after completing his own assassination. The shift to villain is almost seamless. Central bankers, Tucker implies, need to be wary of how exposed their augmented powers render them.

Unelected Power: The Quest for Legitimacy in Central Banking and the Regulatory State, by Paul Tucker, *Princeton, RRP£27.95/$35, 656 pages*

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