Central Bank Independence

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1. An Idea Whose Time Has Come

Until a relatively few years ago, Central Banks were regarded as an integral part of

modelled on those of the Bundesbank, historically the most independent of all Central Banks. And other European Community nations cannot participate in the final stages of European Monetary Union and join the European System of Central Banks until these Central Banks have been made independent of their executive Governments, no longer subservient and indeed even statutorily prevented from taking any instructions from Government. Hence all the major European countries are moving towards the degree of constitutional independence already enjoyed by Germany and Switzerland.

Why has this surge of support for the concept of an independent Central Bank now occurred? The purpose of the exercise is to improve economic performance, and, as might therefore be expected, the basic ideas which have driven the case for independence have been provided by economic theory. The first of these goes by the somewhat unfortunate name of the vertical Phillips curve. Bill Phillips, a New Zealand economist working at LSE, had earlier discovered in the 1950s that, using historical British data, when unemployment was high, the pressure of demand in an economy being low, then wage and price inflation had also been lower. This suggested that the authorities might be able to choose an optimal combination, or trade -off, between inflation and unemployment. And this is exactly what governments sought to do in the 1950s and 1960s. But by the 1970s, the rate of inflation consistent with a given level of unemployment kept on rising; we ran into stagflation.

Milton Friedman then explained that the problem was that the short run Phillips curve had depended on the existing state of inflationary expectations. If the supposedly `optimal' level of inflation that the authorities wanted was above that which had been expected by the public, then the public's real wage and profit outcomes, which they had sought to achieve by their price setting agreements, would have been systematically inflated away. They would subsequently revise their inflationary expectations up, and at any given

level of unemployment would demand higher wage, or price, increases. In short, if the authorities tried to keep the level of unemployment below the natural rate, which is, broadly, the rate that causes workers to seek that rate of real wage increase that their own productivity increases make available, then inflation will not be constant, but will rise without limit; in economists' jargon, in the longer term the Phillips curve is vertical. There is no trade-off in the medium, and longer, term between inflation on the one hand, and output, growth and unemployment on the other.

During the immediate post-war decades when economists and governments had worked on the basis of such an assumed trade-off, the choice of the `optimal' balance between employment and inflation objectives was seen, and rightly so, as an essentially political matter. Consequently, instruments of demand management, monetary and fiscal policies, needed to be coordinated and managed to achieve that balanced outcome. Once, however, the concept of the medium-term vertical Phillips curve was absorbed, it became apparent that one both could, and should, use monetary policy to control inflation in the medium, and longer, term without losing any benefits in the way of growth or employment over that same horizon.

But what that suggested was that governments should use monetary policy as a medium term instrument to control inflation, while, perhaps, using (quasi-automatic) fiscal stabilizers, or supply side measures, to moderate shorter terms shocks and cycles, not that the monetary policy instrument should be removed altogether from the hands of Ministers. And this is broadly what happened. Governments in the 1970s and early 1980s embraced monetary targets, and medium-term financial strategies, for bringing down inflation,and moved to `supply side' measures to encourage growth.

This strategy had a mixed success. When sufficiently tough Central Bankers and

Treasurers were in charge, at the Bundesbank, Paul Volcker at the Fed, Geoffrey Howe and Nigel Lawson in the UK, inflation was brought down, but often at a severe short-term cost in terms of higher unemployment. These costs were attributed, in large part, to a lack of credibility that the authorities would achieve, and then maintain, a regime of stable prices, of zero inflation. And this in turn was attributed to the short-time-horizons of politicians, especially in advance of elections. Even though in the longer term expansionary monetary and fiscal policies, lowering taxes and raising expenditures, would do no good to output and employment, and just raise inflation, in the short run, with expectations given, they would raise employment, induce a feel-good factor, and raise the probability of re-election. Economists incorporated all this into another jargon-rich model of behaviour, termed time-inconsistency, whereby a government's rhetoric would always be that its counter-inflationary determination was absolute, but its actual actions, whenever short-term pressures really mounted, or an election loomed, would be to accommodate, even to encourage, monetary expansion as a short-term palliative. However, the public, not being entirely mugs, would soon appreciate this and would therefore largely ignore and disdain the government's counter-inflationary rhetoric. The medium-term result would be higher inflation, no more growth, and a thoroughly cynical set of politicians and electorates.

Meanwhile, the problem of credibility had been made worse by the collapse in the stability of the relationships between monetary growth and inflation, the increasing unpredictability of velocity. Previously governments could publicly pre-commit themselves to a series of monetary targets, which would, it was hoped, lead straight through to lower nominal incomes and inflation. But these monetary relationships progressively collapsed during the 1980s in almost all countries. Currently, for example, some monetarists have been accusing the Fed of excessively expansionary monetary policy on the evidence of a

rapid growth of M1, while others have been blaming it for being too deflationary on the evidence of the sluggish growth M2. Hence operations to achieve stable prices reverted from being a matter of sticking to publicly announced monetary target rules back to the more discretionary use of monetary instruments for that purpose; in many countries interest rates are varied now to try to bring inflation back to its desired, say zero, rate several quarters, perhaps a year or more hence, when the interest rate adjustment would have had its full effect on expenditures and prices. This exercise requires technical expertise, good models of the economy, discretion, patience and long horizons, none of which government ministers as a collective, irrespective of personality, party or country, have been renowned for possessing. There is no doubt but that the popularity of the idea of an independent Central Bank has, as its flip side, a generalized distrust of politicians of all shapes and sizes.

Arguments about the appropriate instruments, indicators and intermediate targets (if any) for monetary policy have neither been resolved, nor stilled. There remains discussion in many quarters, for example, whether interest rates, or reserve base aggregates, make the best short-term operational targets. Yet the collapse of monetary targetry has taken much of the heat out of that discussion. There is some willingness to give the Central Bank clear statutory responsibility for the achievement of price stability, and to reckon that, so long as the incentives on its behaviour are properly designed, it can be trusted to work out the best technical operational mechanisms for itself.

Thus, the theory ran, if there is a need for a credible medium-term counter-inflationary policy, a solution would be for the government to delegate the objective of achieving price stability to a separate institution, an autonomous Central Bank, which should have both the requisite longer time-horizon and technical expertise to achieve that objective. Note in particular that the Central Bank is <u>not</u> independent with respect to

the objectives that it should fulfill; indeed it may often, as in the case of New Zealand, be tied down rather rigidly to the achievement of a defined outcome. In that sense the Central Bank is autonomous with respect to the powers used to achieve its statutorily defined objective, but not independent to choose its objectives. By the same token an autonomous Central Bank can be more democratically accountable than a subservient Central Bank.

But the move towards an independent, or autonomous, (and I prefer the latter adjective) Central Bank was not only a matter of theory. A whole series of econometric/ statistical tests have shown that countries with more independent Central Banks have had generally lower inflation rates, led by Germany and the Bundesbank. Recently countries that have adopted independent Central Banks, such as Chile and New Zealand, have moved from bottom of their class towards being best performers. Finally, but very important, the Germans are so enamoured of their independent Central Bank that they refused to counternance a move towards the European System of Central Banks and European Economic and Monetary Union, EMU, until all the other Community participants, and the European Central Bank, had installed independence along Germanic lines in their own Central Banks.

2. Some Qualifications

In the opening Section I have tried to explain why the entPCTw (CT T96 se-0.0015 -0.0015-0.0015-nc

benefit of an independent Central Bank, to cohorts of aspiring young undergraduates and graduates. When there is such widespread enthusiasm for a new idea, perhaps especially in economics, it is as well to be wary.

Let us, therefore, turn to some of the qualifications, starting with the economic ones. First, the case for an autonomous Central Bank, statutorily committed to price stability, is predicated on the assumption of a natural rate of unemployment, a vertical Phillips curve. Whereas the theoretical underpinnings for that concept seem sound, in practice the natural rate itself does not seem stable, or stationary, either between countries or over time. The unemployment rate consistent with a steady inflation rate appears to differ markedly between Japan, USA and Europe, and has steadily risen in Europe over recent decades from about 2 1/2% in the 1950s to perhaps around 8% now. How far is the `so-called' equilibrium, longer term, level of unemployment a function of the shorter -run path followed in the mean -time; to use another jargon term, does the natural rate exhibit `hysteresis'? There is little evidence of such effects in the USA, but more in Europe. If so, in the European case at least, there may be a longer term trade off between the level of unemployment and the measures taken to reduce inflation, for example its planned rate of change. But such a trade off, if it exists, would once again be a proper subject for political choice, not just a technical matter. Be that as it may, our present inability to understand, or influence, the factors affecting the time -variant (European) natural rate of unemployment should make us cautious about policy proposals that implicitly assume that the natural rate is either constant, or unaffected by the monetary policies adopted in the mean -time.

Keynes remarked that, in the long run, we are all dead. Even in the medium term our tastes change, we may get divorced and change jobs and homes. The short run matters, especially at times of great uncertainly and disturbance, such as political turmoil, civil unrest,

and wars. Some shocks are too massive to refuse any accommodation. Let me evidence German reunification, and the 1973 and 1979 oil shocks. If rules are drawn too tightly, with no let-outs for unforeseen contingencies, they can become unacceptable, and themselves incredible. Thus, there has to be some flexibility in the policy objectives proposed for the autonomous Central Bank. This, for example, is provided for the Bundesbank by carefully refraining from giving any precise definition, either in terms of index, quantification or date, to its objective of price stability. In the case of New Zealand, where the objective is both quantified and date-stamped, the flexibility is provide by the small -print in the contract and by the override procedure. Quite which mechanism for achieving the desired modicum of flexibility is better is a debatable matter. What is clear is that granting autonomy to a Central Bank does not, and should not, mean that complete priority is given to medium term objectives, with no attention to the short run. It involves a significant shift in the balancing of priorities, rather than a total change in regimes.

As noted earlier, [pg. 4], the adoption of monetary targets was intended to make the monetary authorities focus more on the medium term objective of price stability. But that left open the question of whether other instruments of demand, or supply, management, (e.g. fiscal policy), could be used to alleviate shorter -term fluctuations. In practice, a variety of factors, such as the relevant legislative time -frame and the other lags inv olved, make both fiscal policy and supply -side measures unsuitable as short -term stabilisers. By contrast, monetary policy decisions can at least be introduced quickly, and have some (announcement) effects on confidence and asset prices, even if their full effects on expenditures and inflation are slow to take hold. Hence an independent Central Bank cannot focus solely on the longer term, oblivious of current unemployment. There will have to remain some balance between shorter -term real and longer -term inflation objectives,

perhaps reflected in the adoption of a nominal income target, rather than a pure inflation target, in the short run.

Let me go on to some of the more political qualifications. We have in a sense already noted a couple of these. The first is that Central Banks, under this proposal, are not really being given independence; indeed their objectives are in most cases, specifically in the New Zealand case, spelt out and defined much more closely than before. They have autonomy over the powers needed to achieve that objective, notably interest rate adjustment, but no more. Second, even their use of this limited autonomy will be constrained, either specifically by the retention of certain `override' powers by the government, though these are intended to be used only in emergencies, or more generally by the Central Bank's need to retain, if not a political consensus, at least a sufficient degree of political support to maintain their position of `independence.'

The establishment of the Central Ban k's independence is generally done by a legislative Act, an Act of Parliament or Congress. What one Congress, or Parliament, has enacted, another can repeal. The independence of the Federal Reserve System is constantly under scrutiny, and sometimes under threat, from Congress. For example in the last few months Congressman Gonzales of the House Banking Committee has sought to reopen the question of how the regional Federal Reserve Presidents are to be appointed. The independence of the Bundesbank is not part of the German constitution, but derives from an Act of the Bundestag. The independence of the Banque de France and, perhaps, of the Bank of England would not, could not, be absolute, but would be subject to the continuing pleasure of the legislature. In some respects the prospective independence of the European System of Central Banks is more profound since that will be based on the inter-governmental Treaty of Maastricht. Treaties can also be amended, or rescinded; it just

takes rather longer.

Moreover, there is one key aspect of monetary affairs that Governments have never been willing to delegate to their Central Bank, whether formally independent or not, and this is the right to take the strategic decisions on the exchange rate regime. Despite the vaunted independence of the Bundesbank, the decisions on establishing the Exchange Rate Mechanism (ERM) of the European monetary system, on the exchange rate for changing ostmarks into Deutschemarks, and on conditions for European monetary union, were all taken by the German politicians, in several of these cases against the clear advice and wishes of the Bundesbank. In the US, exchange rate decisions are a matter for the Secretary of the Treasury, not the Chairman of the FRB. Despite awarding an unusual degree of independence to the ESCB, the framers of the Maastricht Treaty kept exchange rate decisions in the hands of the politicians (Article 109). This can cause problems and frictions. Central Banks only have one major instrument, their ability to vary interest rates, (which, of course, has as its dual the ability to control the reserve base of banking system). As a generality this cannot be used to hit two objectives simultaneously, e.g. an external objective for the exchange rate and an internal objective for price stability, except by a fluke. In some cases, e.g. of small, open countries, or countries where domestic control may have been problematical (e.g. Luxembourg, Hong Kong, Argentina, Estonia), Central Banks have transformed their operations, into a currency board format, specifically to achieve an external rather than an internal objective. In other cases, the latitude allowed to a Central Bank to use its powers to achieve domestic price stability may prove to be conditional on the effects of that on the country's exchange rate. Alternatively, a Central Bank, whether formally independent or not, may find that its politicians have agreed to the establishment of an exchange rate regime that restricts its own freedom to act to meet its domestic

objectives. Again, its only recourse would be to the court of public opinion, to persuade the wider public that the exchange rate regime change proposed by the politicians would be counter-productive.

In such an appeal to public opinion, the Central Bank has a reasonably good chance of succeeding. This is partly because of the wide -spread cynicism and distrust of politicians, whereas Central Bankers are, I believe, seen as relatively more disinterested technicians. Indeed, it is this cynicism about politicians, embodied for example in time -inconsistency theory, that is largely responsible for much of the enthusiasm for taking the levers of monetary control from them. In my view this cynicism has been exaggerated. It has been shown, for example, that the existence of a political business cycle, whereby the incumbent government pumps up the economy before the election, only to reverse engines once safely re-elected, is largely mythical. As Lincoln said, "you cannot fool all of the people, all of the time."

The rationale for granting independence to Central Banks derives largely from the view that the continuance of inflation is due largely, if not entirely, to the self -interested short-termism of politicians. This is a very seductive concept, particularly since we like to think ill of those in power over us. But it is not necessarily true. I can certainly remember instances when the politicians in the UK were pressing the Bank of England to lower interest rates, but there have also been cases, e.g. in 1981 and 1982, when the Bank might have adopted, on its own, a more expansionary path than the politicians had chosen. On balance, I do accept that politicians usually have a somewhat shorter time horizon, and feel a greater need to respond rapidly to immediate distress, at a potential cost in longer -term stability, but the differences in priorities, and probably in performance, may not be nearly as great as the enthusiasts for Central Bank independence may believe.

In practice, the differences in priorities and performance between an independent Central Bank and a Chancellor/Treasurer cannot be all that great, because both ultimately have got to persuade and satisfy the general public that the policies are good. If not, the Central Bank independence would be repealed, just as the Treasurer would be voted out of office. There is, in some quarters, a view that enacting Central Bank independence would be to take monetary policy issues out of the political arena. This is absolutely wrong. What such enactment does is to put the Central Bank squarely into the political arena. Subservient Central Banks can always hide their advice and involvement behind the front of the responsible Minister, and claim that they offer only technical advice on which the government and Ministers put a political gloss. When they become independent, Central Banks have to justify their actions to a much greater extent, and that will involve the full gamut of political and presentational skills.

Indeed, sensible Central Bankers know that they have to forge, and maintain, a widely-based political consensus for the main thrust of their (counter-inflationary) policies. This is central to their success. If a major political party, likely to be elected shortly, campaigns on the basis of rescinding the independence of its Central Bank, what medium term credibility will the latter still have? It was the fact that the Reserve Bank of New Zealand Act was, and is, supported by both the main parties there, that has enabled the newly independent Bank there to start so well. Equally it is the fact that none of the main parties in Germany would want, or dare, to try to compromise the independence of the Bundesbank that gives it its real strength. Even so, there are limits to the extent that even the most independent Central Bank can push its opposition to the policies of the elected government. Every Central Bank Governor knows that the Prime Minister, or President, was elected, whereas he was not. So, in cases of serious conflict, the Governor will resign.

Some may regard Pohl's resignation from the Bundesbank as a case in point.

What this means is that an independent Central Bank will only retain credibility so long as it can maintain a broadly based political coalition of support for giving priority to using monetary policy for the medium term control of inflation, despite the shorter-term pains that such a policy may, at times, involve. But there is something of a paradox here. If there is such a widely-based political coalition for giving priority to medium-term price stability, then you do not need an independent Central Bank, since the politicians would deliver much the same result, unaided. While if there is no such general support for counter-inflationary policies, granting a Central Bank independence probably will not work either. It is for this reason that one should take the historical correlations between Central Bank independence and low inflation with several grains of salt. The true underlying correlations may be between the underlying priorities of the electorate and the economic outturn. Both the independence of the Bundesbank and low German inflation may be symptoms of the abhorrence of Germans for inflation. It is quite possible, therefore, that Germany would have had relatively low inflation in recent decades whatever the status of its Central Bank. It is, perhaps, worth recalling that the German hyperinflation in the 1920s took place at a time when the Reichsbank was statutorily independent of the executive, as was also the Russian Central Bank, at least until Yeltsin destroyed the legislature. It is at least arguable that the constitutional status of the Central Bank is of second-order importance.

The argument, advanced here, is that what really matters in a democratic state are the priorities, perceptions and beliefs of the general public. If so, the passage of an Act to grant the Central Bank independence may achieve little unless it influences those same priorities and perceptions.

3. An Assessment

Although it is, I believe, fair to argue, as I have just done in Section II, that the basic determinants of inflation reside, in a democratic state, in the general public's priorities and preferences, it is not valid to treat these as exogenously fixed, or independent of the institutional framework. The establishment of an independent Central Bank, with a mandate to achieve stable prices, provides a public protagonist for longer-term counter-inflationary policies. Politicians want simultaneously to provide higher real incomes (for their potential supporters) and stable prices (for all). Each party will tend to claim that its own policies can provide both; there is likely to be some self-deception in such claims, but, with all the political parties making somewhat similar claims, the electorate is likely to become confused. The addition of a player into the public arena, the Central Bank, with a more narrowly focused mandate, should help to improve the public's understanding of the true alternatives. Even so, the Central Bank's ability to enter the public arena to help educate the public will be limited. If its advice appears to have a regular bias in favour of one, or another, political party's programmes, then it risks breaking the necessary wide consensus, and thus, perhaps, losing its own independence.

Besides such educational functions, a Central Bank should be able, dependent on the strength and breadth of its political support, to give significantly greater priority in its monetary policy actions to the achievement of longer term price stability; it will have a longer time horizon. Subject to the earlier qualification about hysteresis, that would be advantageous in itself, since in the longer term no output growth is lost and greater price stability is achieved. Moreover, depending on its record, its constitutional position, and its political support, a Central Bank may hope to make its, and the nation's, future adherence to price stability more credible. To the extent that such credibility is achieved, private sector

behaviour may help to make such stability self -fulfilling, (since a rise in prices would then become a signal to sell, not to buy more, before inflation worsens further); it may become possible for the Central Bank to offset short -term shocks to a greater extent without risking its longer-term credibility, and the costs in terms of short -term unemployment and output loss of reverting to price stability may fall. The achievement of credibility is the Holy Grail of this exercise.

It is dubious whether this Holy Grail has yet been attained. Whereas c ountries with independent Central Banks do tend to have lower inflation, I have seen no evidence to indicate that their loss ratio, measured as the number of extra man -years of unemployment necessary to lower inflation by one per cent, has also been significantly or systematically lowered. Even so, there are likely to be some practical differences in credibility between countries, such as Germany and Switzerland, which have a proven reputation for maintaining low inflation,and those countries which may be enacting constitutional independence for their own Central Banks for the first time, in some part in the hopes of improving a relatively poor past inflationary performance. This suggests that the mandate, for the achievement of low inflation, may need to be more tightly drawn, and narrowly focused, for the newly independent Central Banks, as in New Zealand: the longer and better established independent Central Banks, with a stronger counter -inflationary track-record, can afford to be more accommodating to short -term shocks, since this will not immediately endanger their credibility. This was one of the considerations influencing the Roll Committee's judgment in the UK, whether a prospectively independent Bank of England should follow the Bundesbank or the New Zealand model.

In the UK context, with which I am, of course, most familiar, there have been two main arguments put up against independence for the Bank of England, which should be

directly addressed. The first is to query the democratic accountability of an independent Central Bank; the second is to ask whether such independence would preclude a desirable degree of policy co-ordination: (this latter issue is generally raised intra-nationally, but could also be relevant in an inter-national context). Neither criticism is compelling.

The issue of democratic accountability depends on the exact model of the independent Central Bank under consideration. Under the New Zealand model, democratic accountability is clearly enhanced. The government is a party to the specific contract, and maintains an override. The public knows exactly what the Governor's objective is, and the Governor is accountable for that. I would agree that democratic accountability is formally lacking in the Bundesbank model, but that may be because, in the German context, there is such a strong, underlying coherence between the public, the political parties, and the Bundesbank on the appropriate (medium term) objectives that there is less need to formalize them. This suggests two conclusions. First, the question of democratic accountability is model specific. Second, it may be undesirable to seek to impose on other European central banks the German model, since the success of the latter may depend on circumstances and conditions particular to Germany.

The second question, of coordination, has been raised in the UK, not altogether surprisingly, by ex-Treasury officials. There is, however, nothing to stop fiscal policy still being co-ordinated with the given, counter-inflationary monetary policy. The argument is not really about co-ordination, but about which policy instrument should move first and have primacy. Under the Keynesian policy modalities of the 1950s and 1960s, fiscal policy had primacy; the fiscal deficit was decided first, and monetary policy then adjusted to achieve the desired level of interest rates, given the deficit. With an independent Central Bank, monetary policy is aimed at achieving stable prices. The government, and Treasury,

can still vary fiscal policy as they prefer. But in so far as such fiscal measures are assessed by the Central Bank as affecting the future course of inflation, the Central Bank will vary interest rates in a counter-vailing fashion. Essentially the difference is that, without independence, the Treasury can bring about a change in the fiscal stance while ensuring that interest rates remain unchanged. With independence, a change in the fiscal stance is rather likely to induce an offsetting interest rate adjustment. while one can see why Treasury officials and Ministers may prefer the first set-up, it is equally self-evident why the latter is likely to be more consistent with price stability.

Indeed, one of the advantages of an independent Central Bank is that, once Treasury officials and Ministers lose the power to control short-term monetary policies, fiscal policy itself may become more disciplined. The coordination issue may, in truth, be an argument for, rather than against, Central Bank independence. This upbeat view does, however, depend on Treasury Ministers and officials being prepared to accept the Central Bank's objectives and reaction functions as prior-determined, and then optimising their own fiscal policies in the light of these given variables. It may, however, be the case that fiscal policy is still set without full cognizance of, or coordination with, the independent monetary policy, as appeared to be the case in the USA throughout much of the Reagan era. In such conflict cases, an easy fiscal policy, interacting with a counter-inflationary monetary policy, may lead to high real interest and exchange rates, crowding out of private sector investment, and low growth. But while such instances of policy conflict and coordination failures are sub-optimal, the resolution of this co-ordination failure by easing up on monetary policy, and accommodating the fiscal expansion, would surely have been even worse.

If I may sum up now, I do not think that the enactment of Central Bank independence will make an enormous difference; it will not be a panacea leading directly to

price stability at little, or no, short term cost. The continuing (and perfectly natural and proper) political constraints on even the most independent Central Bank, concerns about the exchange rate, and the very complexity of the inflation process itself, will all serve to lessen the likely effects of such a constitutional measure. If people expect the world to alter greatly for the better immediately after such a change, they are likely to be gravely disappointed.

The adoption of the Ce ntral Bank independence ought, instead, to be seen as an incremental step, leading to somewhat improved policy measures, in both the monetary <u>and</u> fiscal areas, aimed at a longer time -horizon, and to a better public understanding of policy issues. I would stress the latter. An independent Central Bank will fail and be rejected, unless it can establish broadly -based public support for its policies. The educational and presentational skills of an independent Central Bank will be as important as its technical and operational capabilities. To succeed it has to establish a broad constituency.

Will the present government in the UK bring forward a Bill to grant the Bank of England greater autonomy? That remains uncertain. The Roll Report already has proposed (and the) Select Committee (for the Treasury and Civil Service) of the House of Commons is likely to do the same), greater independence for the Bank, probably advocating a modified form of the New Zealand Act. Two past Chancellors, Nigel Lawson and Norman Lamont, have endorsed the idea, but both the Prime Minister, John Major, the present Chancellor, Ken Clarke, and the Leader of the Opposition, John Smith, remain cagey, unwilling to reveal either preferences, or their arguments, in any detail. Mrs. Thatcher was broadly in favour of the idea when in opposition, but turned against it when in power. That is symptomatic of the main, but largely unspoken, reason for political objection, which is that it serves, and is intended, to reduce politician's hands -on power ov er the economy. It is

always hard for a Prime Minister to cede any particle of his, or her, power.

It is the case, of course, that the UK could only participate in EMU if the Bank was to have become independent by the time of entry, but that is not currently a factor enhancing the likelihood of such an Act. After the travails of the ERM, the path to, and achievement of, EMU are seen as problematical. There are, moreover, so many passionate euro-sceptics in the UK that, should independence for the Bank of England be seen as part of the federal European program, it might endanger its chances of obtaining Parliamentary assent. In any case, as already noted, the Select Committee of the House of Commons and the Roll Report are likely to recommend a modified version of the New Zealand model, and that is not exactly consonant with the Maastricht Treaty, which appears to require national Central Banks to adopt, more or less, the Bundesbank model.

Whether this, or a successor, government will introduce such a Bill, therefore remains uncertain. The worst reason for doing so would be to try to bind the hands of a successor from another party, though that may nevertheless be influential. The best reason for doing so would be because it becomes widely accepted that such independence would be beneficial to us all.