

Returning to Normal?

Interest Rates & Money Creation



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February 2014

Quantitative Easing

- UK - £375bn programme ended
- US – QE3 \$85bn a month

Tapering now at \$10bn a month

- Japan - \$1.4tn (£923bn)
Yen 7tn of bonds bought each month (£46bn)
- ECB – No QE

Other Monetary Measures

Bank of England

- Funding for lending
- Help to buy

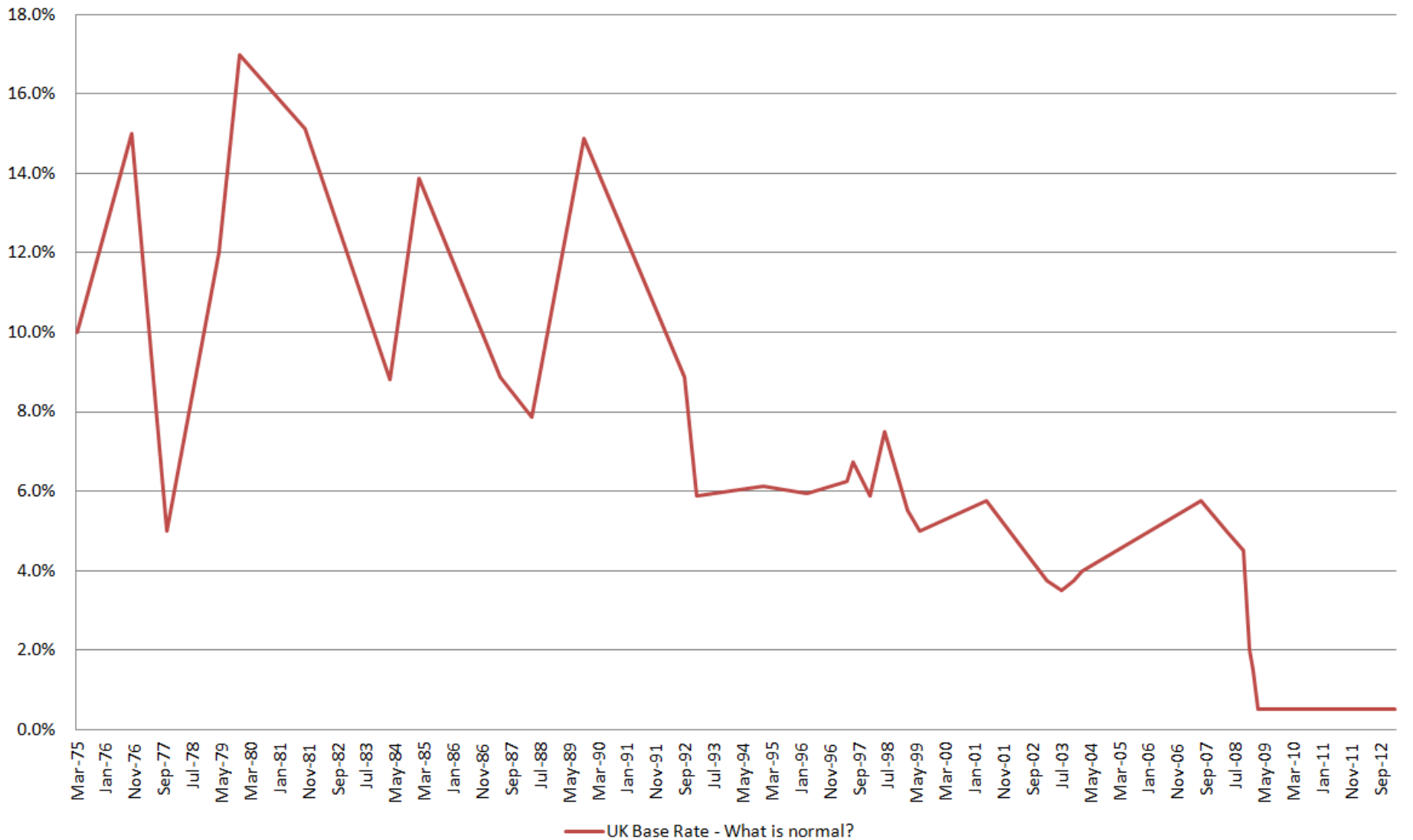
European Central Bank

- LTRO – Longer Term Refinancing Operations

US

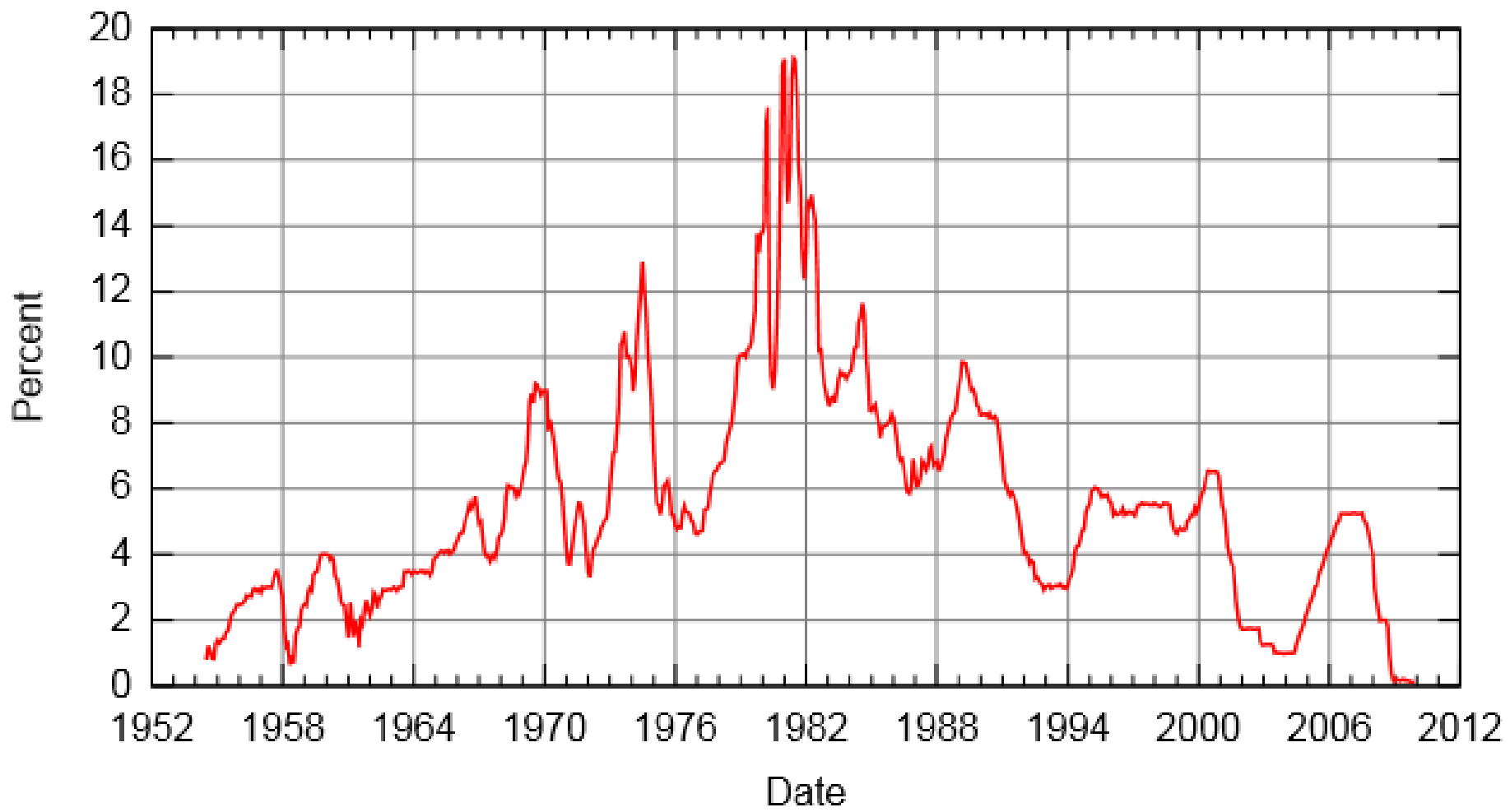
- Twist – September 2011: Fed sold short term bonds and bought long term bonds

UK Base Rate - What is normal?



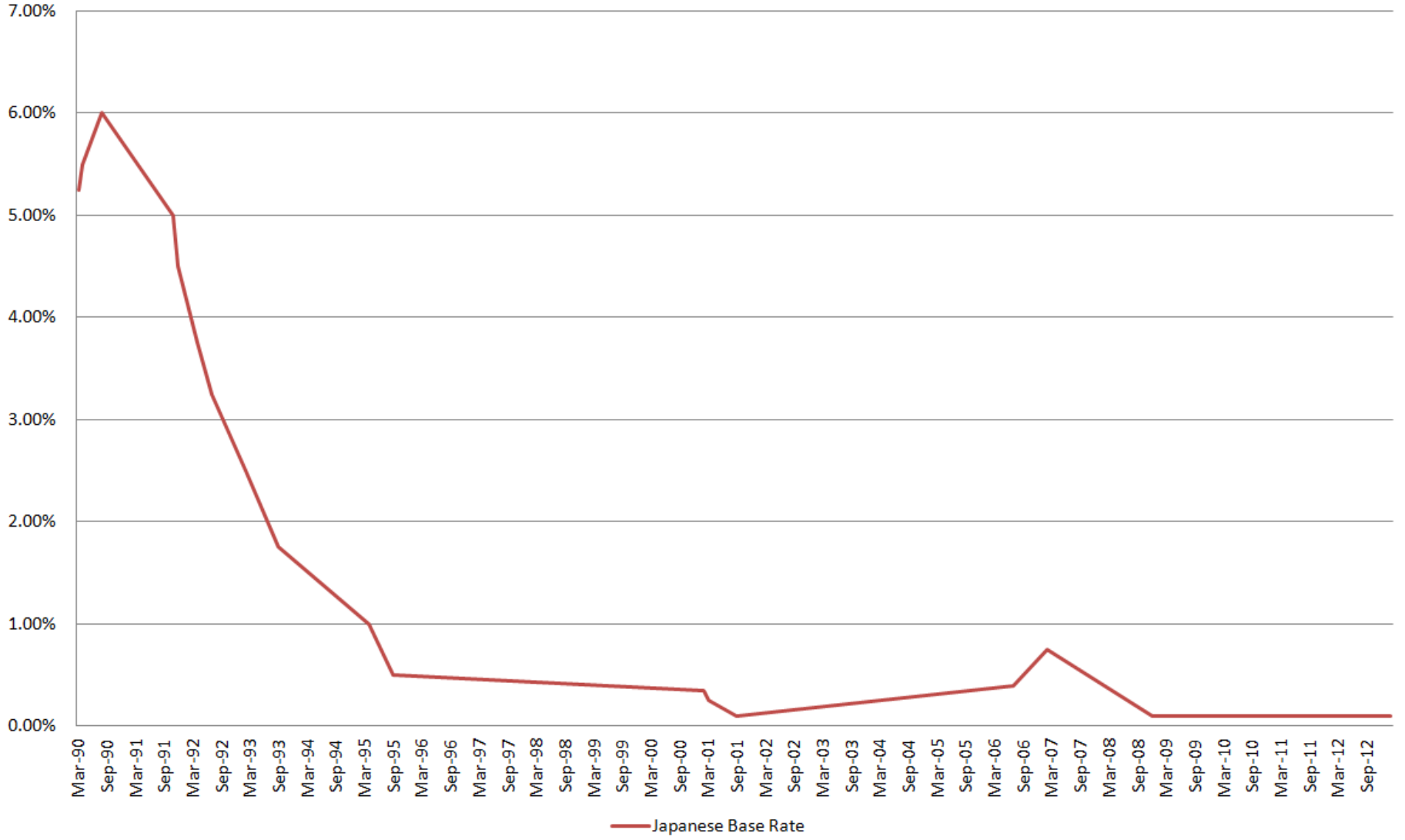
Source: Own Work (Approximate)

Federal Funds Rate (effective) July 1954 to December 2009



Source: Wikipedia Federal Funds Rate 1954-2009

Japanese Base Rate



Source: Own Work (Approximate)

The UK

- The Bank of England has said (February Inflation Report):
- “The date of the first rise in the Bank Rate implied by market interest rates” is Q2 2015
- When the Bank Rate does increase, it is expected to do so gradually
- No run down of QE before the first rise in the Bank Rate
- “Even when the economy has returned to normal levels of capacity and inflation is close to target, the appropriate level of Base Rate is likely to be materially below the 5% level set on average by the MPC prior to the financial crisis.”

The USA

Janet Yellen, February Testimony:

- “The committee will likely reduce the pace of asset purchases in further measured steps at future meetings.”
- “A highly accommodative policy will remain appropriate for a considerable time after asset purchases end.”
- “The current low target range for the Fed funds rate to be appropriate at least as long as the unemployment rate remains above 6½%, inflation is projected to be more than ½% above our 2% longer-run goal...”

ECB – More Monetary adventures?

- “Seriously considering” a negative overnight bank deposit rate
- Karlsruhe Court thinks OMT “exceeds the European Central Bank’s monetary policy mandate and this infringes the powers of the member states... considers it possible that if the OMT decision were interpreted restrictively” it could conform.
- Main refinancing rate 0.25%
- Deposit facility 0%

ECB Statements

- Mr Draghi: “We continue to expect the key ECB interest rates to remain at present or lower levels for an extended period of time.”
- “We remain firmly determined to maintain a high degree of monetary accommodation and take further decisive action if required.”
- “The risks surrounding the economic outlook for the Euro area continue to be on the downside.”