Review Essay

The Authorized Version: The Recent Installment in the History of the Bank of England

Making a Modern Central Bank: The Bank of England, 1979–2003. By *Harold James*. Cambridge: Cambridge University Press, 2020. 350 pp. Paperback, $39.99. ISBN: 978-1-108-79949-2.

Reviewed by Ranald Michie

This book is a worthy successor to those commissioned by the Bank of England that cover its history from its foundation in 1694. It is written by an expert, is thoroughly researched, and provides a wealth of evidence to support the judicious conclusions that are drawn. The discussion ranges from the highly technical to the narrative, indicating the command that Harold James has over his subject. For the period it covers it will become the authorized version of what the Bank of England did and why, covering the details of how it operated as a complex organization and the decisions it made that affected both the domestic and international financial systems. What emerges is how difficult decision making was after the 1970s, following the breakdown of the postwar certainties of the 1950s and 1960s. Though the title suggests that the coverage of the book extends to 2003, it largely ends in 1997. The years that followed are treated with much less depth. That is understandable, as the elephant in the room for any recent history of the Bank of England is the banking crisis of 2007–2008. As it is, the dates chosen are those between which Eddie George, governor of the Bank of England between 1993 and 2003, exerted his greatest influence, having joined in 1962. Increasingly after 1997 Mervyn King took a leading role, becoming deputy governor in 1998 and then governor in 2003. We will have to wait for another commissioned history to discover what part the Bank of England played in the first major banking crisis to hit Britain since that of Overend and Gurney in 1866. Judging from a comment made in this book (p. 432) it is possible that a full understanding of those years will never emerge. When the Monetary Policy Committee, located in the Bank of England, was set up in 1997 it was agreed that the meetings would be recorded and a full transcript of the discussion made. Subsequently, it was decided to delete the recording and

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destroy the transcript, leaving only the published official record of what took place. This mirrors the Bank of England's destruction of the papers relating to its role in the secondary banking crisis of 1974.

The 1980s and 1990s were the years when the Bank of England gradually reinvented itself before being subjected to the radical restructuring imposed in 1997 by the Labour government that came to power that year. Under the plan masterminded by Gordon Brown and Ed Balls, the Bank of England lost a number of the roles it had undertaken since its foundation in 1694, such as managing government debt, as well as others that had grown over the previous 150 years, including the supervision of the banking system. In their place the Bank of England became, in practice, a monetary policy institute with responsibility for ensuring monetary stability, whether of prices or the value of the pound sterling. It is made clear in this book that King, unlike George, had little interest in either the working of banks or financial stability; his focus was on monetary policy, and that was the prime, even sole, function of a central bank. Hence the title of the book, *Making a Modern Central Bank*. However, at the very end of this long and detailed book James questions that focus, in light of the global financial crisis of 2007–2008. With the recognition that financial stability was not an inevitable product of monetary stability but needed to be addressed as a separate issue, the restructuring of 1997 was unpicked and the Bank of England was given back a number of the functions that had been discarded either then or subsequently. A new Bank of England emerged that had many of the features of the one that had been evolving before 1997. There are hints in this book, but no more, that the restructuring that took place in 1997—and then the subsequent direction followed over the next ten years—left the British financial system ill prepared to cope with the crisis that took place in 2007. The Bank of England must bear a degree of responsibility for that; as James makes clear, it was aware of the issues but took no action.

However, the post-1997 years are for another historian to tackle. The focus of this book is the 1980s and 1990s as the Bank of England struggled to cope with its monetary, financial, and economic responsibilities at a time when its ability to influence, let alone control, the behavior of banks and financial markets was steadily waning. These struggles are carefully documented, including the blind alleys and dead ends it met as decisions were made based on the available evidence and in response to pressures from different directions. This was the reality of the world of central banking at the time that hindsight glosses over and mathematical models cannot cope with. The early chapters set the scene for this, describing the environment within which the bank operated and emphasizing the extent to which its ability to influence domestic financial markets was lost with the ending of exchange controls in 1979. In the absence of the ability to impose controls on the domestic financial system, the Bank of England experimented with different policy measures and there is a detailed account of these. The rise and fall of monetarism between 1979 and 1985, for example, is documented as are the various attempts to stabilize the exchange rate. These reveal something of a "treasury-bank divide" as well as differences within the Bank of England itself. The strongest parts of the book are those dealing with monetary policy at both the domestic and international levels. The Bank of England was much keener on European cooperation than the governments it worked with. That included membership of a single European currency and a European Central Bank, as a way of providing itself with the tools required to manage monetary policy in an increasingly integrated global economy. However, that was not to be as long as the Conservatives were in power, especially after the U.K. pound sterling was forced out of the Exchange Rate Mechanism in the early 1990s. The Labour government elected in 1997 was also not sympathetic to Britain adopting the euro, which left the Bank of England as an observer when it came to European monetary integration.

The book is weaker on banking supervision and the wider financial system. This probably reflects the changing priorities of the Bank of England itself, with monetary policy becoming its main focus. However, this weakness was also a product of the difficulties of supervising banking when international barriers were disappearing and the domestic compartmentalization of the past financial system no longer existed. The type of rescue mission attempted in 1974, at the time of the secondary banking crisis, which involved the close cooperation of the major retail banks, could not be carried on in the early 1990s when a similar problem arose. By then the Bank of England had statutory responsibility for the banking system and so could no longer ignore large elements of it. The Bank of England also found it impossible to stop the Hong Kong and Shanghai Bank (HSBC) from entering British retail banking, fearing that its extensive operations in Asia left it vulnerable to a crisis there that would destabilize any bank it owned in the United Kingdom. It had prevented HSBC taking over the Royal Bank of Scotland (RBS) in 1981 and then only reluctantly agreed to its takeover of the Midland Bank in 1992, despite that bank being in financial difficulty. Ironically it was RBS that needed to be rescued in 2008, after having been allowed to take over NatWest in 2000, while the Midland, now owned by HSBC, did not require support.

The impression generated in the book was that the Bank of England was only interested in the financial system, including banking, when either major change was taking place or individual banks were in difficulty. It was relaxed about the changes taking place at the London Stock Exchange and the foreign takeover of British merchant banks. When it did intervene, it was to prevent the collapse of banks that might threaten monetary stability, suggesting that this was already the priority before the restructuring of 1997. Throughout the 1980s and 1990s the Bank of England appeared to be searching for a regulatory model that would allow it to cope with the growing complexities it faced in a world of opaque and uncontrolled financial flows and the emergence of global banks. In this world even its ability to act as lender of last resort was becoming problematic. The solution found was to copy U.S. practice, which was favored by the increasingly influential economic advisors it employed, which meant greater reliance on the authority of the government and international cooperation with other central banks, leading to the 1988 Basel Agreement. One consequence of the changes that took place, reinforced by the 1997 restructuring, was that the Bank of England lost its day-to-day contact with the banks and financial markets. All this is well documented in the book.

In many ways this is an excellent book. It provides an account of what happened in and to the Bank of England between the ending of exchange controls in 1979 and the radical restructuring that took place in 1997. The problem is that the story does not end there. The Bank of England was a major player in what happened to British banking between 1997 and the financial crisis that began to emerge in 2007. In the aftermath of that crisis the Bank of England was then subjected to another major restructuring and only time will tell whether that possesses the resilience required of it.

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