NATIONAL INSTITUTE OF ECONOMIC AND SOCIAL RESEARCH:
PRESS CONFERENCE
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Opening remarks by the Director

Good morning. Welcome to the National Institute of Economic and Social Research for the release of our quarterly Economic *Review*. Despite all the talk of uncertainty we can certainly say that we live in interesting times. The country has been through a difficult referendum campaign, with a surprising result, a change of Prime Minister and heightened concerns of an immediate economic slowdown, which may have been militated against by the swift change of government, the delay in the triggering of Article 50 and an easing in monetary conditions. In the Introduction to the articles for this Review, I suggest that we are now in a position to re-consider our democratic institutions and the question facing us is whether the post-referendum climate will prove to be sufficiently fertile to grow the kinds of institutions we need.

It is, of course, somewhat of a truism but the UK has had a difficult relationship with the European Union, and its predecessors the European Economic Community and the European Community, along many dimensions, as long run polling data and both the announcement and result of this year's advisory Referendum confirm. But, despite imminent exit from Union, the UK remains a European nation. So whether the country is a full member of the supranational organisation or ultimately becomes simply an observer, our relationship with Europe will continue to be a hugely significant point of departure for our external trading and political relationships.

The immediate post-Referendum analysis seemed to fall into three broad categories. First, that the referendum was a moment of madness and the result should not be taken too seriously - a grand one night stand. The second was that it was a generalised, perhaps ill-directed, plea from the previously disenfranchised to be heard: that the left-behind should not be ignored. The third was that there are clear socio-cultural factors that explain the result and these will act to constrain political choice in the run up to the triggering of Article 50 and the negotiations that follow. In some senses, the third is the most compelling answer and says that we live in a country that wants to divorce from the EU and we must now locate the best, or second best, form of exit.

The projections presented in this Review suggest that the UK economy will undergo something of a slowdown as the risks identified by NIESR from an exit in May and in August from the European Union start to materialise. One quarter's respite is just that and the longer term prospects continue to be worrying and, I ought to note, that there is significant event risk attached to the triggering of Article 50. Accordingly, the government may be tempted to use fiscal policy to offset any imminent slowdown but caution must be exercised. First the exchange rate has jumped down by some 15% and is providing some considerable impetus to the economy. Secondly, public debt levels are already high and risk premia have been far from eradicated. Third, the Bank of England is already the largest single holder of UK debt and that starts to erode the distinction between monetary and fiscal policy to the point where it is hard to see much of a difference. Indeed it is now common to treat inflation as a joint monetary-fiscal phenomenon.

We thus need to use the opportunity of the Autumn Statement to think about a fiscal framework that explains 'misses' from previously announced plans but promotes a sense of 'timeless' fiscal sustainability. The level of debt, its path and the composition, as well as who holds it, all matter for financial and monetary conditions and we have very little formal guidance on these matters. In pursuit of macroeconomic stability, Bagehot's famous points on the English Constitution may be quite apt in considering the role of a Governor of the Bank of England who has the right to be consulted, the right to encourage and the right to warn. Politicians should, of course, set targets according to some social welfare function but experts must be allowed to pursue policy in the manner they see fit and that might ultimately what we have to do with fiscal policy.

Our fiscal framework is in need of some attention before policy can be asked to allow debt to deviate for long periods from what we may think is normal. If the framework is credible then there will be more latitude for the government to provide a persistent buffer for shocks. The analogous benefit of a credible monetary framework will become apparent when inflation rises to nearly 4%. So much so that it is the unhinging of inflation expectations rather than inflation *per se* that is a major risk to our projections. So when debt is high the Chancellor must explain how it will be reduced. We may wish to consider addressing the problem of fluctuations in refinancing costs by lengthening the maturity of public debt. Even though the average maturity of conventionals is around 16 years at present (excluding the holdings of gilts by the APF) and nearly 25 years for index-linked bonds, there may be some merit in issuing even longer-term bonds and restructuring the maturity of debt to match ever longer-term liabilities faced by financial institutions and perhaps promote longer-term planning horizons by the private sector. Ultimately, rather than a rule for deficits we might need an architecture for managing public debt.

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