Old Lady of Threadneedle Street hit by bull

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Another day, another symbolic record high for a stockmarket. Yesterday it was the Dax at 13,000. Today the Dow at 23,000.

One commentator complained on Twitter that he'd only just received his shipment of a "Dow 22,000" hat. Some else was caught wearing one by the media. (They actually exist and no sees the irony of wearing one now.)

But what about Britain? Our stockmarket isn't in the lines. But the country can't get out of them.

The news that inflation in the UK hit 3% was drowned out by the **Bank of England** governor and his new sidekick, the deputy governor Dave Ramsden. Neither seem terribly worried about inflation. They signalled rate hikes are not imminent. Perhaps in a few months.

The narrative goes something like this

Normally, 3% inflation is a bad thing. And so the Bank of England should put up interest rates. Which would make the pound rise. And that fits particularly well given it's the falling pound that's supposedly driving inflation in the first place.

However, the monetary meddleomaniacs see it differently this time. The various risks of **Brexit** make it too dangerous to raise rates. Which made the pound fall, worsening coming inflation.

Secondly, take a look at the justification for not raising interest rates. Central bankers are now Brexit managers, not just inflation, employment, financial stability, bank capital, interest rate, debt and emergency lending managers.

They supposedly know **how the Brexit negotiations will play out**, and what policies will be in place. They know what the consequences of those policies will be too. And, therefore, they can set the appropriate interests rates.

There's nothing these people don't know, can't do and won't meddle in

But by adding Brexit to their list of obsessions, they're spreading themselves thin. I call it juggling mandates. The number of indicators which central bankers look at to guide **monetary policy** is steadily growing. That's called mandate creep, named after the mission creep which the US illustrates the disastrous results of in Afghanistan.

The problem with many mandates is that the variables can go haywire. Unemployment and inflation are supposed to go in opposite directions. But what if you get both at the same time? Or what if wages stagnate while inflation takes off? Then the juggler has a problem.

The second possibility is what's taking shape. Jeremy Warner explained the nature of the problem in The Telegraph:

> *In normal circumstances, there would be no question about what the Bank of England should do. Regrettably, circumstances remain far from normal. Something is missing from the news that inflation is rising at its fastest rate since April 2012; fed by a weak pound, prices are forging a but wages are refusing to follow suit.*
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> *The consequent income squeeze is weighing on consumption, thereby depressing economic activity and undermining the case for higher interest rates.*

So the central bankers have added wages to their list of mandates too now

The divergence between inflation and wages is really just a new version of the problem which gave you the stagflation of the 1970s. Central bankers failed to prioritise inflation as the most important mandate back then too. Employment and **GDP** growth were too weak to raise rates, just as wage growth is now. The rest is history.

It took years to mop up the mess with extraordinarily high interest rates. Economic law has a sense of irony. Central bankers probably didn't have mortgages at the time though.

At this point, it's time to explain the line. An Australian mining genius and **economics** fanatic by the name of Ron Kitching once had a bull he named Inflation. He treasured a picture of the economist Friedrich von Hayek “grabbing Inflation by the balls” on a visit to the farm Down Under.

In case you’ve forgotten, it was Hayek’s books that Lady Thatcher held close while inflation was tamed. It remains unclear whether she resorted to the same methods as Hayek did Down Under.

The Old Lady of Threadneedle Street is a nickname for the Bank of England. I’m trying to read a one-volume history of the Old Lady now, so you don’t have to. More to come on that.

Today’s subject line and title predicts that the Old Lady of Threadneedle Street will be run over by the bull called Inflation. If the Bank of England doesn’t get its hands dirty soon, inflation will run riot.

How Brexit could go wrong

If the Bank of England is betting on a Brexit disaster with its low interest rates, it’s not hard to see how inflation might get out of control.

Perhaps Brexit will be a success, triggering improved economic growth, not a lack of it as Mark Carney assumes. After all, it’s the rest of the world that’s doing well, not Europe. Escaping Europe’s trade barriers could make trade boom.

So far, Brexit has embarrassed its mainstream forecasters constantly. Roger Bootle from Capital Economics pointed out why in a column recently. The forecasters use miserable assumptions, especially about trade, for their base case scenario.

I’m less worried about Brexit than poor domestic policy.

Here’s a good example how to muck things up. In Britain, changes to stamp duty rules are causing an enormous mess. Thousands of people are asking for advice from HMRC about what the rules are supposed to mean. Many say the answers are contradictory. And they take 40 days to arrive.

In Australia, one of the most overpriced housing markets in the world relative to median income, stamp duty reductions helped first-home buyers to a four-year high as a proportion of buyers from a four-year low. It doesn’t solve the underlying problem. But it does show what happens when governments get out of the way.

Until next time,

Nick Hubble
Capital %26 Conflict

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