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# What a Bank Governor should understand [1]

Written by **Dr Madsen Pirie** [2] | Tuesday 20 November 2012

I had a letter published in the Business section of Monday's Telegraph. It had to be abbreviated for lack of space, but I think the full text is worth repeating here because it explains what it is that the incoming Governor should understand.

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*Dear Sir,*

*Next month a new Governor of the Bank of England will be appointed to replace Sir Mervyn King. A suitable candidate must not only possess rare qualities, but should also understand the causes of the financial crisis in order that they might make a recurrence unlikely. They should understand that the low interest rate policy pursued by governments and central banks to smooth the down side of the business cycle produced cheap money and easy credit that fuelled a housing bubble. This was intensified by implicit government guarantees in the US to support loans to borrowers with a high default risk.*

*This was exacerbated by rules that required banks to take more mortgage debt, done in the name of prudence, but in fact compounding regulatory error. Added to this was the fact that the artificially low interest rates drove fund managers into riskier investments because of the low returns on the safer ones.*

*If the person to be chosen as Governor understands this, they are unlikely to countenance future intervention designed to secure a politically acceptable outcome rather than an economically wise one. They will be unlikely, too, to punish by a regulatory stranglehold a financial sector that was far less culpable than the politicians who tried to make it serve their interests.*

*Yours etc.*

*Madsen Pirie*

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Anyone who thought it was all down to greedy bankers taking reckless risks and thinks that tighter regulation is the answer is lacking in the insight and understanding we are entitled to expect from the next Governor.

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[4] http://disqus.com