



BANK OF ENGLAND

Monetary Policy Summary and minutes of the Monetary Policy Committee meeting ending on 1 November 2017

Publication date: 2 November 2017

These are the minutes of the Monetary Policy Committee meeting ending on 1 November 2017.

They are available at <http://www.bankofengland.co.uk/publications/Pages/news/2017/007.aspx>.

The Bank of England Act 1998 gives the Bank of England operational responsibility for setting monetary policy to meet the Government's inflation target. Operational decisions are taken by the Bank's Monetary Policy Committee. The minutes of the Committee meeting ending on 13 December 2017 will be published on 14 December 2017.

Monetary Policy Summary, November 2017

The Bank of England's Monetary Policy Committee (MPC) sets monetary policy to meet the 2% inflation target, and in a way that helps to sustain growth and employment. At its meeting ending on 1 November 2017, the MPC voted by a majority of 7-2 to increase Bank Rate by 0.25 percentage points, to 0.5%. The Committee voted unanimously to maintain the stock of sterling non-financial investment-grade corporate bond purchases, financed by the issuance of central bank reserves, at £10 billion. The Committee also voted unanimously to maintain the stock of UK government bond purchases, financed by the issuance of central bank reserves, at £435 billion.

The MPC's outlook for inflation and activity in the November *Inflation Report* is broadly similar to its projections in August. In the MPC's central forecast, conditioned on the gently rising path of Bank Rate implied by current market yields, GDP grows modestly over the next few years at a pace just above its reduced rate of potential. Consumption growth remains sluggish in the near term before rising, in line with household incomes. Net trade is bolstered by the strong global expansion and the past depreciation of sterling. Business investment is being affected by uncertainties around Brexit, but it continues to grow at a moderate pace, supported by strong global demand, high rates of profitability, the low cost of capital and limited spare capacity.

CPI inflation rose to 3.0% in September. The MPC still expects inflation to peak above 3.0% in October, as the past depreciation of sterling and recent increases in energy prices continue to pass through to consumer prices. The effects of rising import prices on inflation diminish over the next few years, and domestic inflationary pressures gradually pick up as spare capacity is absorbed and wage growth recovers. On balance, inflation is expected to fall back over the next year and, conditioned on the gently rising path of Bank Rate implied by current market yields, to approach the 2% target by the end of the forecast period.

As in previous *Reports*, the MPC's projections are conditioned on the average of a range of possible outcomes for the United Kingdom's eventual trading relationship with the European Union. The projections also assume that, in the interim, households and companies base their decisions on the expectation of a smooth adjustment to that new trading relationship.

The decision to leave the European Union is having a noticeable impact on the economic outlook. The overshoot of inflation throughout the forecast predominantly reflects the effects on import prices of the referendum-related fall in sterling. Uncertainties associated with Brexit are weighing on domestic activity, which has slowed even as global growth has risen significantly. And Brexit-related constraints on investment and labour supply appear to be reinforcing the marked slowdown that has been increasingly evident in recent years in the rate at which the economy can grow without generating inflationary pressures.

Monetary policy cannot prevent either the necessary real adjustment as the United Kingdom moves towards its new international trading arrangements or the weaker real income growth that is likely to accompany that adjustment over the next few years. It can, however, support the economy during the adjustment process. The MPC's remit specifies that, in such exceptional circumstances, the Committee must balance any trade-off between the speed at which it intends to return inflation sustainably to the target and the support that monetary policy provides to jobs and activity.

The steady erosion of slack has reduced the degree to which it is appropriate for the MPC to accommodate an extended period of inflation above the target. Unemployment has fallen to a 42-year low and the MPC judges that the level of remaining slack is limited. The global economy is growing strongly, domestic financial conditions are highly accommodative and consumer confidence has remained resilient. In line with the framework set out at the time of the referendum, the MPC now judges it appropriate to tighten modestly the stance of monetary policy in order to return inflation sustainably to the target. Accordingly, the Committee voted by 7-2 to raise Bank Rate by 0.25 percentage points, to 0.5%. Monetary policy continues to provide significant support to jobs and activity in the current exceptional circumstances. All members agree that any future increases in Bank Rate would be expected to be at a gradual pace and to a limited extent.

There remain considerable risks to the outlook, which include the response of households, businesses and financial markets to developments related to the process of EU withdrawal. The MPC will respond to developments as they occur insofar as they affect the behaviour of households and businesses, and the outlook for inflation. The Committee will monitor closely the incoming evidence on these and other developments, including the impact of today's increase in Bank Rate, and stands ready to respond to changes in the economic outlook as they unfold to ensure a sustainable return of inflation to the 2% target.

Minutes of the Monetary Policy Committee meeting ending on 1 November 2017

1 Before turning to its immediate policy decision, and against the backdrop of its latest projections for output, inflation and unemployment, the Committee discussed financial market developments; the international economy; money, credit, demand and output; and supply, costs and prices.

Financial markets

2 UK short-term interest rates had increased significantly compared with the conditioning path underpinning the August 2017 *Inflation Report* projections. That movement had in large part occurred following the release of the minutes of the September MPC meeting and subsequent public comments by some Committee members. Market intelligence suggested that these communications had led some investors to reassess their view of interest rate prospects.

3 In the run-up to the November MPC meeting, a 25 basis point increase in Bank Rate had been almost fully priced in by market participants and the interest rate curve underlying the November *Inflation Report* projections now reached 1% by the end of the three-year forecast period. That was a higher path than the median response to the latest Reuters poll of economists. Having been unusually compressed following the August *Inflation Report*, option-implied volatility around the future path of short-term interest rates had increased following the September MPC meeting, although it had remained below the levels prevailing prior to last year's referendum on EU membership. Longer-maturity yields had risen since the MPC's September meeting. The sterling effective exchange rate index had been broadly unchanged between *Inflation Reports*, although it had nevertheless remained sensitive to developments regarding the United Kingdom's ongoing negotiations with the European Union.

4 In the United States, the FOMC had confirmed at its September meeting that it would initiate the balance sheet normalisation programme described in its June 2017 Addendum. Short and longer-maturity Treasury yields had risen slightly following the September meeting and to a greater degree following recent stronger-than-expected economic data releases. Most financial market participants expected an increase in the federal funds rate at the December FOMC meeting although, further out, the market curve had remained below the median projected appropriate policy path published in the latest FOMC *Summary of Economic Projections*.

5 At its October meeting, the ECB Governing Council had announced an extension to its Asset Purchase Programme until at least the end of September 2018, with the pace of net asset purchases halving beyond the end of this year. Short-term interest rate expectations had not changed materially since the August *Inflation Report* and most market participants did not expect the ECB to raise interest rates until 2019. German long-term interest rates had fallen slightly since August and government bond spreads in most other euro-area countries had remained broadly stable.

6 There had been signs of a further improvement in global risk sentiment. International equity prices had risen since the August *Inflation Report* and particularly since the Committee's September meeting, while

measures of implied volatilities in equity markets had fallen back to historically low levels recently. The strength of equity prices had been less evident in the UK, however, with the share prices of domestically focused companies within the FTSE All-Share index having generally underperformed.

The international economy

7 The near-term outlook for the global economy had remained strong. The preliminary estimate of euro-area GDP growth in 2017 Q3 had been 0.6%, a little stronger than expected at the time of the MPC's September meeting. Growth had been broad-based across countries and sectors. Industrial production had increased by 1.4% in August relative to the previous month, and business and consumer confidence indicators had remained well above historical averages. High-frequency indicators had suggested that growth would be maintained at a similar rate in Q4. Despite the strength of activity, the flash estimate of core HICP inflation had fallen again in October, to 0.9%, while headline inflation had fallen slightly, to 1.4%.

8 In the United States, the near-term outlook for activity also looked healthy. GDP growth in 2017 Q3 had been 0.7%, in line with Bank staff's expectations at the time of the MPC's previous meeting. After some weakness in August, activity indicators for September had rebounded strongly, in particular auto and retail sales. Non-farm payrolls had fallen by 33,000 in September, the first decline since September 2010, although this had been influenced by the hurricane season. The unemployment rate, which did not appear to have been affected, fell to 4.2%, its lowest level since February 2001. High-frequency indicators had suggested that growth would be maintained at a similar rate in Q4. As in the euro area, strong activity had not as yet translated into higher inflation. Core CPI inflation had remained flat at 1.7% in September for a fifth month in a row, and core PCE inflation had remained subdued, at 1.3% in September.

9 According to the official Q3 estimate, GDP in China had grown by 6.8% on a year ago, a touch lower than in the previous quarter, but remaining above the authorities' growth target for 2017 of around 6.5%. Activity indicators for September had been mixed, though overall fairly robust. Growth in industrial production and retail sales had picked up again, while fixed-asset investment had continued to slow; growth in infrastructure and real estate investment had held up, and credit growth had eased slightly.

10 Elsewhere, high-frequency activity indicators in Japan had shown continued strength, and Bank staff estimated that GDP in Q3 had been around 1.7% higher than a year earlier. That would imply a seventh consecutive quarter of positive growth, which had not been seen since 2001. In emerging markets other than China, high-frequency indicators for Q3 had in general suggested a slight slowdown in growth relative to the second quarter, albeit still at fairly solid rates.

11 Spot oil prices had increased by 13% since the MPC's September meeting, and by 27% relative to the 15-day average incorporated in the August *Inflation Report*. The increase in the spot price appeared to have reflected both upside news on demand and downside news on supply. However, the futures curve had been in sustained backwardation for the first time since July 2014, such that, on average over the forecast period, the curve was only 6% higher than at the time of the September meeting.

Money, credit, demand and output

12 The ONS had reported a preliminary estimate of GDP growth of 0.4% in 2017 Q3, slightly stronger than that expected by Bank staff immediately prior to the release and in the August *Inflation Report*. The outturn was also slightly stronger than the latest Q2 GDP growth estimate of 0.3%. That pick-up in growth could be entirely accounted for by a rebound in the manufacturing sector, bringing the official output data closer into line with the stronger growth implied by most business surveys. Total services growth had remained steady between Q2 and Q3, but growth had rotated away from consumer-facing, and towards business-facing, activities. Construction output had fallen in both quarters, although these data had a tendency to be revised up, on average, over time.

13 In the MPC's central projection, GDP growth was maintained at its recent modest pace. In the near term, that was consistent with the average projection for Q4 across Bank staff's nowcasting models. It remained too early in the data cycle, however, to obtain precise estimates, and individual models had suggested a range of possible outturns, reflecting the varying weights placed on different business surveys and other data sources.

14 Consistent with the MPC's key judgement in the November *Inflation Report*, recent revisions to the Quarterly National Accounts had suggested a more subdued path for household consumption growth over the past year, while business investment and net trade were judged to have contributed to GDP growth to a greater extent than previously estimated. Taken at face value, the latest monthly ONS trade data had pointed to some weakness in net trade in Q3, but survey indicators of goods export orders had remained strong. Companies' investment intentions had been broadly stable, on balance, and pointed to continued, albeit moderate, growth in business investment. A survey conducted by the Bank's Agents had suggested that investment growth would be maintained over the next year at a similar pace to that seen over the previous year, although contacts' expectations were somewhat less positive over the following two years. Over the next twelve months, respondents had judged that economic uncertainty was the factor likely to exert the largest negative influence on their investment plans.

15 Recent indicators of consumption had been mixed. Retail sales volumes had fallen in September but had risen over Q3 as a whole. The October CBI Distributive Trades survey had reported a sharp fall in sales within the retail sector, although that had followed a particularly strong outturn in the previous month. GfK/EC consumer confidence had risen slightly in October, on a seasonally adjusted basis. House price inflation as measured by an average of lenders' indices had risen in Q3 by more than had been assumed in the August *Inflation Report*. In contrast, the September RICS survey had suggested that estate agents expected prices to fall over the next three months, with expectations at their weakest in London.

16 The Committee discussed recent developments in the cost and availability of household credit. In the mortgage market, the interest rates charged by banks on new lending were significantly lower than they had been 18 months ago, reflecting: the pass-through of lower Bank Rate and falls in swap rates; reductions in bank funding spreads; and greater competition among lenders. The cost of fixed-rate mortgages at lower loan

to value ratios had risen slightly in the most recent data, however, consistent with the increase in swap rates observed since the Committee's previous MPC meeting.

17 Price and non-price terms in consumer credit markets had loosened over much of the past 18 months, primarily as a result of greater competitive pressures. There were now some signs that credit conditions had started to tighten. Lenders responding to the Bank's *Credit Conditions Survey* had reported a further decline in the availability of unsecured credit in Q3. The average length of 0% balance transfer offers on credit cards had shortened slightly between March and September. Recent regulatory statements and actions by the PRA, FPC and FCA might also have led to a tightening of credit conditions for some borrowers, although it was too early to judge how pronounced this would prove to be.

18 The Committee's November *Inflation Report* projections were conditioned on a path for household credit conditions that reflected the pass-through to household lending rates of the prevailing market curve for Bank Rate and swap rates, and a modest rise in spreads relative to those reference rates. Credit conditions were expected to continue to support growth, but to a lesser extent than hitherto.

Supply, costs and prices

19 Twelve-month CPI inflation had risen to 3.0% in September, from 2.9% in August. The September outturn had contained some downside news relative to Bank staff's expectation immediately prior to the release. However, the inflation rate in 2017 Q3 had been 2.8%, 0.1 percentage points higher than had been expected at the time of the August *Inflation Report*, reflecting upside news in petrol and clothing and footwear prices. The near-term forecast for inflation was consequently higher than in August. Inflation was expected to rise above 3.0% in October, before declining thereafter. Indicators of medium-term inflation expectations had remained consistent with the 2% target.

20 Imported inflation, prompted by the fall in sterling since late November 2015, had been by far the dominant factor driving CPI inflation above the target. The lagged pass-through from import prices to consumer prices meant that some upward pressure was expected to persist throughout the forecast period. Part of that process had been evident in the rebuilding of consumer-facing firms' profit margins, following the squeeze from imported costs in the latter part of last year, and this was expected to continue.

21 Measures of domestically generated inflation had generally remained subdued. However, revised official data had suggested that unit labour costs had grown more rapidly in the recent past than previously thought. The upward revisions to growth had related primarily to non-wage costs and wage costs in the public sector, which were not expected to be persistent. Looking ahead, the MPC's forecast for CPI inflation depended critically on its judgement that wage growth would pick up to a greater extent than productivity growth over the forecast period.

22 There had been little news in the recent outturns for regular pay growth. The MPC's central projection was therefore similar to that in August, with whole-economy total pay growth projected to rise from a little over

2% at present to 3% in a year's time, levelling out at around 3¼% in the medium term. The Committee discussed the risks around this expected pickup.

23 The wage projection rested on a sustained rise in pay growth to levels that were somewhat above the average seen since the global financial crisis. In the near term, there were good reasons to expect the pace of annual wage growth to strengthen. Some of the softness in recent pay outturns had related to the composition of employment, with the number of low-paid jobs growing disproportionately. Such effects had proved transitory in the past. Also, annual pay growth in the near term was likely to increase as the weak growth rates seen around the turn of last year dropped out of the calculation.

24 More fundamentally, the latest indicators had suggested that the labour market had again tightened by a little more than expected. The unemployment rate was estimated to have fallen to 4.3% in 2017 Q3, compared with an expectation of 4.4% at the time of the *August Inflation Report*. Near-term indicators, such as elevated vacancies, suggested it might fall further in the coming months. There was some uncertainty surrounding the precise degree of labour market tightness, and also around the relationship between this and wage growth. Nevertheless, such a low rate of unemployment seemed likely to encourage wage pressures to build. Pay rates were also likely to respond to the greater number of workers that were moving between jobs, a metric that had weakened markedly in the aftermath of the global financial crisis but had returned to close to pre-crisis rates.

25 Regarding productivity growth, volatile employment and average hours data had imparted some noise into recent estimates, making it difficult to discern the underlying trend. The MPC continued to expect productivity to grow at a pace that was slightly higher than had been seen in the recent data. Given the serial disappointments in productivity growth since the global financial crisis, there was a risk that it would remain weak. However, to the extent that weaker outturns for productivity were echoed in pay growth, there would not necessarily be major implications for unit labour costs, or therefore inflation.

The immediate policy decision

26 The MPC sets monetary policy to meet the 2% inflation target, and in a way that helps to sustain growth and employment. In pursuing that objective, the main challenges for the Committee had remained to assess the economic implications of the United Kingdom withdrawing from the European Union and to identify the appropriate policy response to that changing outlook, including to the substantial depreciation of sterling that had been associated with the decision. During the negotiation period, those economic implications would be influenced significantly by the expectations of households, firms and financial markets about the United Kingdom's eventual economic relationships with the European Union and other countries, and the transition to them.

27 The decision to leave the European Union was already having a noticeable impact on the economic outlook. The overshoot of inflation throughout the forecast predominantly reflected the effects on import prices of the referendum-related fall in sterling. Uncertainties associated with Brexit were weighing on domestic activity, which had slowed even as global growth had risen significantly. And Brexit-related constraints on

investment and labour supply appeared to have been reinforcing the marked slowdown that had been increasingly evident in recent years in the rate at which the economy could grow without generating inflationary pressures.

28 Monetary policy could not prevent either the necessary real adjustment as the United Kingdom moved towards its new international trading arrangements or the weaker real income growth that was likely to accompany that adjustment over the next few years. It could, however, support the economy during the adjustment process. The MPC's remit specified that, in such exceptional circumstances, the Committee had to balance any trade-off between the speed at which it intended to return inflation sustainably to the target and the support that monetary policy provided to jobs and activity.

29 Growth over the past year had been supported by resilient consumer confidence, the stronger world economy, the small loosening in fiscal policy relative to previous plans and the MPC's comprehensive package of measures in August 2016. Credit conditions facing UK households and companies had eased further, and exporters had also benefited from a lower level of sterling. Unemployment had fallen to a 42-year low and the level of remaining slack was limited. CPI inflation had risen above the MPC's 2% target as expected, as the sharp fall in sterling had begun to pass through into consumer prices.

30 At the same time, it had become increasingly evident that the pace at which the economy could grow without generating inflationary pressure had fallen relative to pre-crisis norms. This reflected persistent weakness in productivity growth and, more recently, the more limited availability of labour. The MPC would consider these aspects in more detail as part of its scheduled reassessment of supply-side conditions in the run-up to the February *Inflation Report*.

31 The MPC's most recent assessment of the outlook for inflation and activity, contained in the November *Inflation Report*, was conditioned on a market path that implied two additional 25 basis point increases in Bank Rate over the three-year forecast period. In the MPC's central forecast, GDP grew modestly over the next few years at a pace just above its reduced rate of potential. Consumption growth remained sluggish in the near term before rising, in line with household incomes. Net trade was bolstered by the strong global expansion and the past depreciation of sterling. Business investment was being affected by uncertainties around Brexit, but it continued to grow at a moderate pace, supported by strong global demand, high rates of profitability, the low cost of capital and limited spare capacity.

32 CPI inflation had risen to 3.0% in September. The MPC still expected inflation to peak above 3.0% in October, as the past depreciation of sterling and recent increases in energy prices continued to pass through to consumer prices. In the November forecast, the effects of rising import prices on inflation diminished over the next few years, and domestic inflationary pressures gradually picked up as spare capacity was absorbed and wage growth recovered. On balance, inflation was expected to fall back over the next year and, conditioned on the gently rising path of Bank Rate implied by current market yields, to approach the 2% target by the end of the forecast period.

33 As in previous *Reports*, the MPC's projections were conditioned on the average of a range of possible outcomes for the United Kingdom's eventual trading relationship with the European Union. The projections also

assumed that, in the interim, households and companies based their decisions on the expectation of a smooth adjustment to that new trading relationship.

34 At the September meeting, a majority of MPC members had judged that, if the economy continued to follow a path broadly consistent with the prospect of a continued erosion of slack and a gradual rise in underlying inflationary pressure, some withdrawal of monetary stimulus was likely to be appropriate over the coming months in order to return inflation sustainably to target. Since then, data outturns had been broadly in line with expectations, or a little stronger. Global momentum had been strong, domestic financial conditions had been highly supportive, and consumer confidence had remained resilient. Spare capacity appeared to have eroded, if anything, a little more rapidly than the Committee had anticipated in its August projections, and the margin of slack in the economy now seemed fairly limited, while underlying domestic inflationary pressures had shown some signs of picking up, in line with expectations. This, in turn, had reduced the degree to which it was appropriate for the MPC to tolerate an extended period of above-target inflation.

35 In light of these developments, and in line with both the framework for managing monetary policy set out by the MPC at the time of the referendum, and with the guidance accompanying its recent meetings, a majority of members judged that a small reduction in stimulus was therefore warranted at this meeting to return inflation sustainably to the target. Monetary policy would continue to provide significant support to jobs and activity in the current exceptional circumstances.

36 Two members, while sharing the framework for managing monetary policy set out by the MPC at the time of the referendum, did not support an increase in Bank Rate. These members felt that there was insufficient evidence so far that domestic costs, in particular wage growth, would pick up in line with the *Inflation Report's* central projection. It was possible that there was a greater degree of slack in the economy than was assumed in the central case, for example, if a larger part of the recent weakness in productivity had been cyclical. In addition, for those members, recent experience suggested that wage growth could continue to be less responsive to falling unemployment than past experience would suggest.

37 In considering the case for an increase in Bank Rate, all members noted the analysis presented in the *Inflation Report* on the sensitivity of households and companies to changes in interest rates, which had suggested that debt servicing costs would remain historically very low, even in the event of a rate rise of 25 basis points.

38 All members agreed that any future increases in Bank Rate would be expected to be at a gradual pace and to a limited extent.

39 There remained considerable risks to the outlook, which included the response of households, businesses and financial markets to developments related to the process of EU withdrawal. The MPC would respond to them as they occurred insofar as they affected the behaviour of households and businesses, and the outlook for inflation. As such, resolution of uncertainty about the nature of, and transition to, the United Kingdom's future relationship with the European Union would prompt a reassessment of the economic outlook. The Committee would continue to monitor closely the incoming evidence on these and other developments, including the impact

of today's increase in Bank Rate, and stood ready to respond to changes in the economic outlook as they unfolded to ensure a sustainable return of inflation to the 2% target.

40 The Governor invited the Committee to vote on the propositions that:

Bank Rate be increased by 25 basis points to 0.5%;

The Bank of England maintain the stock of sterling non-financial investment-grade corporate bond purchases, financed by the issuance of central bank reserves, at £10 billion;

The Bank of England maintain the stock of UK government bond purchases, financed by the issuance of central bank reserves, at £435bn.

Regarding Bank Rate, seven members of the Committee (the Governor, Ben Broadbent, Andrew Haldane, Ian McCafferty, Michael Saunders, Silvana Tenreyro and Gertjan Vlieghe) voted in favour of the proposition. Two members (Jon Cunliffe and Dave Ramsden) voted against the proposition, preferring to maintain Bank Rate at 0.25%.

Regarding the stock of purchased assets, the Committee voted unanimously in favour of the second and third propositions.

41 The following members of the Committee were present:

Mark Carney, Governor
Ben Broadbent, Deputy Governor responsible for monetary policy
Jon Cunliffe, Deputy Governor responsible for financial stability
Dave Ramsden, Deputy Governor responsible for markets and banking
Andrew Haldane
Ian McCafferty
Michael Saunders
Silvana Tenreyro
Gertjan Vlieghe

Clare Lombardelli was present as the Treasury representative.

As permitted under the Bank of England Act 1998, as amended by the Bank of England and Financial Services Act 2016, Anthony Habgood was also present on 26 and 30 October as observer for the purpose of exercising oversight functions in his role as a member of the Bank's Court of Directors.