BANK OF ENGLAND

MEETING OF THE MONETARY POLICY COMMITTEE
March 2015

A meeting of the Monetary Policy Committee was held on Thursday 5 March 2015. The following members of the Committee were present:

Mark Carney, Governor
Ben Broadbent, Deputy Governor, Monetary Policy
Jon Cunliffe, Deputy Governor, Financial Stability
Nemat Shafik, Deputy Governor, Markets and Banking
Kristin Forbes, External Member
Andrew Haldane, Chief Economist
Ian McCafferty, External Member
David Miles, External Member
Martin Weale, External Member

Dave Ramsden was present as the Treasury representative

Anthony Habgood was present as an observer in his role as a member of the Oversight Committee of Court

The following members of staff were present:

Gareth Ramsay, Director, Monetary Analysis
James Bell, MPC Secretariat
James Talbot, MPC Secretariat
Garry Young, MPC Secretariat
Matthew Tong, Deputy Editor of Inflation Report

Transcript of the Monetary Policy Committee Meeting on

Thursday 5 March 2015

Governor Carney. Good morning everyone, I would like to formally call this meeting to order. The first thing I would like to do is to turn to Andy to ask him for an update on any significant developments overnight on pre-released data.

> **Andrew Haldane.** No new domestic data out since yesterday, Governor. There have been a clutch of PMIs internationally, covering China, the euro area, the US and globally. Overall, taken together, I would say they are all up and on the positive side of neutral, consistent I think with the message from yesterday.

Governor Carney. Thank you. OK starting off with Ben and then I'm going to go to Ian after that. So Ben.

> **Ben Broadbent**. Thank you Governor and good morning everybody.
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> Let me begin, as ever, with a summary of some of the key international news over the past month, starting with developments in the euro area. As Jon explained yesterday, these were generally positive, if only at the margin. On Greece, the recent Eurogroup deal gives a little more breathing space to agree a more permanent settlement, including a new IMF programme in June. And although there is still plenty that could still go wrong in the meantime, we are probably in a better place than we feared we might be one month ago. The tolerance of the Commission regarding fiscal deficits was less of a surprise, and it's not clear how much of a constraint that body provides anyway. But the acceptance of a longer period of adjustment for France was welcome. And there were also some small positives in the economic data from Europe. Inflation was a little less negative than expected, albeit thanks to stronger non-core contributions; activity surveys, and those for credit supply, were a little firmer. The same goes for credit itself: in the three months to January, it rose 1½%, the highest quarterly growth rate since the Lehman default in 2008. After a long period of decline in bank lending this is a straw in the wind. But, taken together, the economic numbers have been on a gently improving trend in the euro area since late last year. The index of data surprises, unweighted, has been rising since November.
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> In the US, we had another strong employment release for January. For the first time in eighteen years, the increase over a rolling three-month period topped one million, 0.6% of the active workforce. The unemployment rate was flat. This partly reflects a weaker reading for employment in the household survey. There has also been firmer growth of the active workforce, including a slight uptick in the participation rate. If that creates an offset to the strength of employment, as far as US monetary policy is concerned, then so too do low inflation readings and recent softness in breakeven rates of inflation in bond markets. On the other hand, average earnings also bounced back very strongly in the United States in January and might provide some reassurance, after a dip in December, that nominal pay growth is not, as yet, following downwards headline inflation.
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> Elsewhere, there was less news – less UK-weighted news, at least: growth in some oil-consuming emerging economies looked a little better in the fourth quarter of last year; Chinese indicators were a little softer and the PBOC cut its main policy rate again. The currency peg, and the strengthening of the US dollar, will have tightened monetary conditions in China. The PBOC has not yet taken the step of widening the bands within which its currency can move.
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> Nor was there that much news, relative to the norm at least, in domestic economic data. Headline UK growth was unrevised, for the fourth quarter of last year, at 0.5%. The first cut of the expenditure breakdown showed weak business investment and a strong contribution from net trade. The drop in investment looks to have been driven mainly by cuts by North Sea companies. This would make sense. But the expenditure data are in general volatile and, particularly in the case of business investment, subject to significant revision. Surveys of investment intentions still point to positive growth. Surveys of output, on which we rely for our near-term GDP forecasts, are also firm. They point to a slight uptick in growth in the first quarter of the year, consistent with the central projection in the February Inflation Report.
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> The labour market data for the fourth quarter also came in much as expected. Wage growth was stronger; but this was due entirely to bonuses, which are volatile and also – arguably – backward

looking: contractually, at least, bonuses are not a marginal cost of ongoing employment. Unit wage costs have accelerated and, with unemployment set to fall further in the near term the staff's statistical models point to a figure of 5.3% for the second quarter of this year. We might expect these costs to accelerate further through this year. But they still need to do so, all else equal, if inflation is to return to target within two years.

With few big surprises in the economic data the more striking events this month, for me, were in financial markets. Typically, and to generalise somewhat, the following things are true about day-to-day movements in the main equity and bond markets in Europe and the US. First, there is a lot of co-movement, particularly in prices of longer-term assets. Second, in response to positive news in the euro area, bund yields tend to rise, relative to those in the US, and the euro exchange rate tends to strengthen. Third, to the extent euro and dollar markets diverge, prices of UK assets, bonds and equities alike, tend to follow those in Europe more than those in the US (though both regions matter). Consistent with this, on days on which the dollar strengthens against the euro, sterling does the same, but only by a little. Though the average move is small, sterling's trade-weighted index tends on those days tends to fall.

The past month has confounded all these trends. Ten-year Treasury yields have risen sharply, by over 30 basis points; despite better economic news Eurozone yields have failed to rise and the euro has weakened further. That has resulted in the sharpest widening in the Treasury-Bund spread since 2010, when the news about the euro area was clearly worse. And, rather than being pulled more in the direction of Europe, UK markets actually went the other way: 10-year gilts yields rose by over 40 basis points – you have to go back to March 1994 to find a bigger monthly increase in the spread between gilt and bund yields – and sterling strengthened not only against the euro but the dollar as well. The trade-weighted index is up 2½% on the month and 5% since last August, when expectations of ECB asset purchases began to grow.

As far as the exchange rate is concerned, and taking the past few months together, it seems likely that a good part of sterling's appreciation is due to ECB policy. Between August and the end of January, days on which there was significant news about QE – and that news was almost always in a positive direction – saw cumulative rises in sterling's exchange rate of almost 4%. The causes of February's sharp moves, in bond markets as well as currency markets, are less easily identifiable. They post-date the announcement of QE and there's been little news about ECB policy since then – yet may well reflect a lagged response to that same announcement.

If asset purchases lead to stronger growth in the euro area, and more confidence about its sustainability, this can only be good for our own economy. Equally, the rise in sterling interest rates and the exchange rate will, all else equal, have something of a depressive effect. Simple ready reckoners suggest that the 2½% appreciation since the last Inflation Report will knock around 0.3% off GDP growth over the next year, 15 basis points off inflation in each of the next two years. That is something we will have to assess properly in the next forecast round. In the meantime I am happy to vote for no change in Bank rate and no change in the stock of purchased assets.

Governor Carney. Thank you very much Ben. So Ian and then Andy please.

Ian McCafferty. Thank you. Good morning everyone.

It is never prudent to place too much weight on the news in a single month, but I have to confess to being quite encouraged by recent developments. It is not only that most of the news is "good", in terms of the outlook. It is also starting to provide some evidence to help resolve the central policy conundrum with which we have been grappling recently – that is, how to balance the upside risk to our forecast in terms of slack, the labour market and wages with the downside risk of persistently low inflation were inflation expectations to become de-anchored.

As far as the financial markets are concerned, I agree with the hypothesis that Minouche advanced yesterday, that recent moves are a reaction to the over-pessimism of late last year. In my view, there is a growing realisation that the oil price shock will be more beneficial to advanced economy consumers than initial estimates, including our own February Inflation Report forecast, were prepared to allow. There may well be further upside from this source to come, if my reading of the oil market plays out.

Spot prices have risen sharply over the last month, as the market has reacted to the sharp fall in rig counts, but less appreciated is the trajectory of supply, and the level of oil inventories, that we still face, even with lower rig counts. Crude supply is still likely to exceed demand for much of this year, so inventory levels will continue to rise, particularly once we are through the seasonal peak in demand. By the late spring, physical shortages of on-shore storage capacity are likely, requiring oil to be stored in tankers.

However, at current tanker rates, the existing contango in the oil forward curve is nowhere near sufficient to make tanker storage economic, so that as conventional storage becomes scarcer, the contango will have to steepen. This could, of course, be realised through a sharp rise in the forward price, but more likely in my view, given the abundance of supply, is a drop at the front end, and hence further weakness in spot oil prices in coming months.

In the Eurozone, the recent consumer sector data is also encouraging. The rise in consumer sentiment in recent months suggests that the recent strength of consumption might be more than simply an earlier-than-expected response to falling oil prices; we may also be seeing a more fundamental increase in confidence of the sort that helped kick off the UK recovery in early 2013. Of course, significant downside risks remain, in the Ukraine, in Greece, and in European politics more broadly, so this will have to be tested in coming months, but, together, firmer consumer spending driven by improving confidence and rising real wages and improving export competitiveness from the weaker euro would represent a marked upside to our current forecast.

In terms of UK domestic demand, I think it premature to place too much emphasis on the weaker readings contained in the Q4 National Accounts. The average absolute historical revisions to the early data vintages for both consumption and investment is material, and for neither component is the slowing in demand in Q4 fully consistent with survey and higher frequency data. If there has been a slowdown in demand, it is likely to be no more than temporary. On business investment, although the Q4 data will have reflected cutbacks in the oil and gas sector, which can be actioned relatively quickly, I am reminded of the conundrum we faced this time last year, when faced with an inexplicable weakening of investment in the second half of 2013, which was later revised away.

In terms of the risks around our current forecast for domestic demand:

- on consumption, the expected sharp increase in quarterly demand growth looks achievable, given that both nominal and real wages are growing at or even slightly ahead of expectations, we have a conservative judgement on the marginal propensity to consume and there is scope for further falls in the saving ratio.
- on investment, I do worry about a drag from rising pension fund deficits driven by the very low levels of bond yields, but corporate profit growth remains healthy, and credit conditions are a minor constraint. More critical will be first, prospects for future demand, and second business confidence when faced with political uncertainty.

So, in sum, I think for now, our February growth forecasts look well secured, but for me we are starting to be some potential upside risks emerging.

But what of the two key issues that have been central to our discussions in recent months?
In terms of the labour market, I continue to worry about the effective level and pace of absorption of slack, and the risks to medium term wage growth. The incremental news on employment and unemployment this month may have been small, but further falls in labour availability in both CIPS and REC surveys, a rise in job churn, and a vacancy ratio now only just below its 2001-07 average indicate that the labour market is tightening significantly. As a result, wages are continuing to grow at the upper end of our expectations.

Staff projections suggest that unemployment will have fallen from the current 5.7% to 5.3% by the end of the second quarter. Even if U* is lower than our previous estimate of 5½% as a result of the numbers of the newly employed coming from long term unemployment, we will have reached effective full employment before the end of year, and will be increasingly reliant on rising participation and additional hours for any remaining slack.

What of inflation expectations, and the risk of a change in either wage determination or spending intentions as a result of de-anchoring? Here, it is still early days.

But, in spite of the further cooling of the expectations heat map, I found the latest readings from financial markets and the surveys reassuring, as was the latest Bank/NOP survey. This showed the highest proportion of respondents either very or fairly confident that inflation would be close to 2% in 2-3 years since the survey began, in 2011. One reason for this may well be because they are no longer worried about persistent overshooting of the target, but neither do they appear to think that low inflation will be more than temporary.

Other survey data also belie any sense of concern amongst consumers about persistent low inflation: the GfK questions about purchases of large ticket durable items show an increasing keenness to buy, and consumer confidence generally continues to increase.

If we were to see any sign of de-anchored expectations affecting wage and spending behaviour, I would have expected it to appear in the Eurozone. But the confidence and spending data of the last month, combined with the signal from the IG Metall settlement, also show little signs of deflationary mentality.

However, we have yet to reach the low point in annual CPI inflation, and will need to assess whether its persistence over several months at around zero might yet have an impact, so I am not yet in a position to be able to dismiss the downside risk of de-anchoring. If the recent appreciation of sterling persists, it will act to further depress the rate of inflation, such that the period over which annual CPI is very close to zero would be further prolonged.

To summarise, I am increasingly concerned by the evidence of the tightening of the labour market, but still feel it too early to fully dismiss the downside risk of the impact of persistent low inflation. As a result, the immediate policy decision remains finely balanced. But today I vote for no change in Bank Rate and no change in the level of asset purchases.

Governor Carney. Thank you very much Ian. So Andy and then Martin please.

Andrew Haldane. Thank you Governor and good morning.

It has not been an especially news-heavy month. Such as it is, that news has tended to corroborate the picture of a pretty robust real-side of the UK economy, alongside a still-weak nominal side.

Starting on the real side, the single most significant piece of international news over the month I think came from the euro area and, within that, from Germany where a number of surveys and indicators have turned up.

Truth be told, we never quite got to the bottom of why Germany experienced a dip in activity last year. But the stories told then – spillovers from Russia/Ukraine, a slowing in China as a key export destination – seem very unlikely to have reversed sign over the course of the past few months. More likely explanations for the turn in German fortunes are the combined effects of a lower euro and lower energy prices, boosting real incomes, exports and confidence.

Outside of Germany, there are also enough snippets to suggest the economic fortunes of other core euro-area countries might be turning too.

These channels were embodied in our February Inflation Report forecasts. But their impact may well be coming through more quickly than expected, perhaps given a tailwind by the ECB's announcements at the end of last year.

In the UK, the pattern has not been greatly dissimilar. Indicators for the first few months of this year suggest a buoyant consumer, with confidence and spending both strong helped by lower energy and food prices and easier credit conditions.

The picture for UK companies remains somewhat more mixed, both across surveys and across sectors. But, nonetheless, most indicators and surveys point towards at or above trends rates of growth, actually and in expectation. As a further diagnostic on that, the rate of hiring by companies remains strong, as it has been over the past 18 months, pushing unemployment down further.

The National Accounts data for the second half of last year could cause us to pause in this positive assessment, with the level of final private domestic demand over 1% lower in Q4 than assumed at

the time of the February Inflation Report. And of course our punchy GDP forecast for 2015 stands or falls on a further strengthening in domestic demand.

Nonetheless, given the scope for future revisions to that data, to consumption but in particular to investment, it is probably reasonable to aim off from taking too strong a steer, not least given the strength of survey evidence.

The emerging pattern, then, seems to be some near-term strength in activity, led by the consumer and fed by lower good prices, easier credit conditions and perhaps, as Minouche said yesterday, simply the start of a new year. This is not just what the doctor ordered; it is also just what the Bank itself forecast in its February Inflation Report.

The key question, as we have found in previous years, is whether this bounce will persist – whether the dawn of the New Year is a bright one or a false one. Only time will tell. All three of the near-term positive effects – lower goods prices, easier credit, the New Year – will dissipate with time. And that will leave momentum in the economy dependent on future growth in wages, productivity and external demand. The uncertainties around all three, needless to say, remain as great as ever.

Of course, even if the real economy were to continue growing at or around trend, that by itself does not guarantee the nominal side of the economy will deliver inflation on target.

Despite being cautiously optimistic about developments in the real economy, when it comes to nominal trends I am cautious without quite as much optimism. In fact, I think I'd go as far as to say I find it hard to think of single nominal indicator at present that gives me cause for concern that UK inflation will significantly overshoot its target in the foreseeable future, whereas a number do concern me on the downside.

In financial markets, international yield curves remain, by any metric, astonishingly low. Despite some upwards correction over the month, UK rates are still expected to be below 2% out to four years ahead, and around 3% out to 25 years ahead.

The nominal component of yields has accounted for a larger share of those falls over the past six months. And five-year five-year inflation swaps, while up a bit on the month, remain around 30 basis points lower than in the middle of last year. As staff analysis shows, these would not have to fall too much further before beginning to call into question the Inflation Report judgement that they are "broadly consistent" with the inflation target.

Household measures of inflation expectations cooled further on the month. They have now fallen by 80 to 100 basis points and 40 to 60 basis points respectively, at short and longer-term horizons, over the past six months. According to staff analysis, that means they may already be below the levels consistent with the inflation target.

Core measures of UK inflation are now fairly tightly grouped at around 1.5% – below the inflation target. Despite having picked up from its low point, whole economy pay growth remains at around 2% year-on-year, below the levels consistent with the inflation target. There is little sign so far of upward pressure on settlements – they appear to be coming in similar to last year at around 2.5% on average. And with inflation set to fall further, there must be at least a possibility of settlements, if anything, weakening in the period ahead.

The Bank's latest NOP survey of households put year-on-year earnings growth at little more than 1%. To return inflation to target, wage growth needs to keep going through the gears to 3.5% by the end of this year and 4% next. That's certainly possible if the Phillips curve of old reasserts itself adroitly. But the string of persistent downward surprises to wage growth over the past 18 months suggests to me a flatter – perhaps much flatter – new-style Phillips curve could be at work. If so, that puts the risks to wages to the downside.

A further factor others have mentioned is the further 3% appreciation of sterling since the February Inflation Report which as Ben said, mechanically by itself would lower inflation at our preferred two-year horizon by around another 0.1 or 0.2 percentage points. It would be a brave man, or woman, who predicted this appreciation would continue. But if nominal and real trends in other countries continue to be weak, then pressures to export deflation through laxer policy could intensify. Indeed, it is this which presumably explains why 25 central banks have already eased policy so far this year.

The UK is currently one of the world's tallest pygmies in interest rates and growth net terms, which increases the risk it will face a still-stronger exchange rate and become a further importer of deflation in the period ahead, or at least that is where I would place the balance of risks.

None of this suggests to me the nominal side of the economy is, at present, grossly misaligned with the inflation target. Rather the risks to that target lie for me somewhat asymmetrically to the downside, on a somewhat greater scale and for a longer duration than embodied in our Inflation Report projections.

The MPC's mandate gives primacy to nominal trends over real ones.

Outside forecasters are unanimous in thinking the next rise in rates will be upwards. Financial market participants are less sure, assigning roughly a 20% probability to rates falling over the next 12 months, versus 40% for a rise.

My personal odds are slightly more evenly balanced between rate rises and cuts over that horizon.

But for today my decision is to hold rates at 0.5% and the stock of purchased assets at £375 billion. Thank you.

Governor Carney. Thank you Andy. So Martin and then Jon please.

Martin Weale. Thank you Governor.

Inflation fell to 0.3% in January and the ONS estimate of Q4 growth remains at 0.5%. The first expenditure breakdown of GDP showed weaker consumption and investment growth than we had expected, offset by appreciably less de-stocking. None of the high-frequency indicators for this year suggest that that change has followed through into weaker GDP growth this year. Past experience suggests that the expenditure mix shown early in the data cycle is subject to substantial revision; the most informative data are probably the consumption data. It seems to me that we are unlikely to see sustained weakness in consumption. Real incomes have risen fairly rapidly over the last year and, even though the STIF shows prices turning upwards, the growth in real consumption seems likely to continue.[1] Thus, while I can accept that consumption growth was weak in Q4, these data have not changed my view of the prospect for GDP growth over the last year.

During the last month my sense is that the prospects for cost pressures presaged by a tightening of the labour market have become more marked. Unemployment continues to fall at a rate of 0.3%[2] per quarter. The claimant count, down 0.1%[3] in January, shows no evidence of slackening. Indeed, in absolute numbers, the decline is at its fastest since the early summer of last year. For the rate of decline in unemployment to slow markedly, we need the improvement in the rate of productivity growth to move from our forecast into the economy. The ONS figures show scant productivity growth over the last year; it may be right to assume that this will be revised up slightly. Turning to vacancies, the average number of unemployed people per vacancy is down to 2.6, only just above its pre-crisis average of 2.5. As a percentage of the labour force, vacancies stand at 2.2%, compared with the pre-crisis average of 2.1%.

As to the wage data, of course the annualised rate of growth of total private sector pay of 5.2% provided the headlines. The annualised three month-on-three month rate of growth of private sector regular pay computed from the ONS spreadsheet was 3.7%, although I think this is likely to ease further in next month's figures. Nevertheless, as the labour market continues to tighten, most logic would suggest that these wage pressures are likely to increase, although of course an improvement in productivity growth will offset them. Staff's work on compositional effects suggests that these are pulling down by about 1%[4] on annual wage growth and, with the production function in Compass,

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[1] MPC Secretariat clarification: the STIF is the Bank staff's short term inflation forecast.

[2] MPC Secretariat clarification: the speaker was referring to a 0.3 percentage point fall in the unemployment rate.

[3] MPC Secretariat clarification: the speaker was referring to a 0.1 percentage point fall in the claimant count rate.

[4] MPC Secretariat clarification: the speaker was referring to a 1 percentage point effect on wage growth.

about 0.9%[5] on productivity growth. Undoing these will not have much effect on unit labour cost growth while labour market tightening will.

We have talked at some length about the role of expectations in previous meetings; I hope you will excuse me for adding some further observations. First of all, our short-term measures in the heat map are relative to the MPC's inflation forecast. This means that if we raise our forecast, as we did in February, while expectations remain unchanged the reported gap in the heat-map appears to widen. Secondly, staff presented us with an analysis of the effects of different measures of inflation expectations on wage growth. Their models were estimated from 1986 to 2014. If I look at 1993 to 2014 or 1997 to 2014 then I find that neither of the two best-performing measures of expectations, household expectations two years ahead, and the five-year spot break-even inflation rates are significant. Ben has, if I remember correctly, shown that if he adjusts annual wage growth for expected price increases, then the resulting measure of real wage adjustment works well in a Phillips curve. That is a different matter from showing that any of these measures of expectations of inflation has had an influence on pay bargaining since the MPC was set up. Despite these results on expectations, which make me less worried that they will be a source of persistent very low inflation, like Ian I cannot avoid mentioning that, according to the NOP survey, the proportion of people who are fairly or very confident that inflation will be between 1% and 3% in two to three years' time is, at 49%, at its highest for the period since 2011; 35% are not confident and the remainder don't know.

Overall the prospects for GDP on the continent seem more favourable than we had built into our February forecast. German retail sales rose sharply over the last three months and are now 5% up on a year ago. In France household consumption of goods by volume has risen sharply over the last two months and is now 2.6% higher than a year ago. On the other hand, the IFO indicator rose only slightly and the INSEE business climate indicator has not risen since November. The IG-Metall settlement suggests that pay pressures are building in Germany; at the same time it is worth noting that there was a similar rise two years ago. For me the most interesting issue is whether the buoyancy in the euro area might just be spending brought forward, so that faster growth now is followed by slower growth later. If we have correctly estimated the supply path in the euro area, then the buoyancy could only be spending brought forward, while if our view of supply has been excessively coloured by the experience of the past few years, that might not be the case. In the short term though, the buoyancy in the euro area is good news for UK growth.

I have noted previously that there may be a tendency to find a sequence of shocks all affecting inflation in the same direction and that this purely statistical observation leads to a risk that low inflation will persist for longer than our forecast shows. That was certainly what happened the other way round between 2010 and 2012. If the oil price has been one negative shock to inflation, perhaps the exchange rate is providing another. The effective rate has risen by 5% in the February average compared with a year earlier, with about half of that increase coming since January. Staff's post Pre-MPC note suggested that the first-round effects of exchange rate changes might affect inflation in more than two years' time. Depending on our views on pass-through we might not want fully look through the first-round effects of any further exchange rate movement when setting policy.

At present, however, there remains a fine balance between the pressures building from the tightening labour market and the risks that very low inflation will persist, notwithstanding that I am less concerned about expectational effects than previously. This month I once again see that fine balance in favour of no change to Bank Rate. I am also voting for no change to our stock of assets purchased.

Governor Carney. Thank you very much Martin. So Jon and then Kristin please.

Jon Cunliffe. Thank you very much.

Not a huge amount of news on the month, but some straws in the wind on the international economy; Q4 output; the labour market and perhaps inflation expectations. Putting it all together, the positive pieces of news probably outweigh the negative.

[5] MPC Secretariat clarification: the speaker was referring to a 0.9 percentage point effect on productivity growth.

Some of the gloom seems to have lifted in financial markets, which are now pricing in the first rate rise for May 2016 – this is a month or so earlier than last month but I have to say it still seems a long way off to me and the longer end of yield curve looks very low.

On the international economy there is likely to be a continued boost to growth from ECB QE in the euro area and from the fall in oil prices, as in our forecast. In addition to that the underlying prospects for the euro area are probably a little brighter than they were: Q4 growth in the euro area was stronger than expected; fiscal constraints have been loosened somewhat; credit conditions have eased; and the crisis related to Greece has been averted in the very short term at least.

We may also have gained a better understanding of the reaction function of the new Greek government. They backed down and claimed victory and improved their ratings. They did not even flirt with the idea of leaving the euro. That said, there are still material downside risks because as yet there is no lasting solution to the Greece problem and plenty of possible flashpoints.

On the domestic side, UK Q4 2014 output growth was unrevised at 0.5% but the bigger news was in the composition of output with signs of softening in consumption and business investment growth. Consumption growth was surprisingly weak (0.3% versus our expectation of 0.8%) as was business investment (it fell by 1.4% versus our expectation of growth of 2.5%).

Andy and others are right to say that these numbers are subject to material revision with business investment notoriously volatile, but they are hard to set aside entirely: [the][6] growth forecast is driven almost completely by business investment and consumption.

The weakness in consumption in Q4 I think can be explained largely by the non-profit sector which is a volatile component of consumption. Other indicators of consumption have held up, for example, the GfK consumer confidence balance rose to its highest level since 2002 this month, and looking ahead staff still expect growth of 0.7% in Q1.

On business investment, surveys of investment intentions remain strong. The fall in business investment was driven largely by the oil and gas extraction sector but it would have been below our expectations even without the weakness in oil and gas extraction. And this is the second consecutive quarter that growth in business investment has been negative.

I flagged last month a concern that uncertainty created by events in the euro area and/or the forthcoming UK election could create a headwind for business investment in the UK. Given that the euro area looks marginally brighter than last month and that the election is now only a couple of months away, this risk has receded somewhat in my view.

Overall, I think the news on output is a reason to feel a little less confident.

On the labour market, that continued to strengthen. Unemployment fell to 5.7% in Q4 from 6% in the previous quarter, representing a fall of 1.5 percentage points on a year ago. Staff unemployment models point to a Q2 unemployment rate of 5.3%, 0.2 percentage points below the February Inflation Report. Whole economy total pay growth was stronger than our expectations in the three months to December at 2.1% (versus our expectation of 1.7%), though this was largely driven by bonus payments which can be erratic. Private sector pay growth rose to 2.5%.

Unit labour costs grew by 1.3% over 2014, more than we had thought, I think there is news in this given that it was mainly due to lower productivity than we had expected. Unit labour cost growth is moving towards the 2% rate of growth we typically think of as being consistent with inflation at target. But to the extent that productivity growth remains weak over a longer period, there may at some point be less scope for non-inflationary pay growth. We are, I think, a long way from that point. But it is something that I for one will be watching closely further out.

And finally on net migration. We have seen an increase in net migration over the year to Q3 2014 very significantly in excess (by around 130,000) of the forecast by the ONS which we use in our forecast. It is not clear how this affects labour market slack. I'd like to look at this in more detail when we review in May our assumptions about the equilibrium rates for labour market variables.

[6] MPC Secretariat clarification.

Overall, the labour market news is probably positive for the outlook. But again, I wouldn't place too much weight on it yet. Pay growth is still only around 2011 to 12 rates and around half its pre-crisis rate.

The final development I want to touch on is inflation expectations where household inflation expectations fell a bit further on the month. For example, inflation expectations fell across all horizons in the latest quarterly Bank/NOP survey – the two-year ahead measure fell from 2.5% to 2.1% (its lowest value in five years). But inflation expectations inferred from financial markets remain stable at a level that staff estimate is consistent with inflation at target. And interestingly the moves on the month have mirrored similar moves in US, with break-even rates getting a little bit higher.

So putting this together I think expectations do not seem out of line with inflation at target.

Broadly the economy seems to be evolving in line with the projections we set out in the February Inflation Report. I don't see greater than expected inflationary pressures building in the pipeline that would merit a tightening of policy.

As always, you could point to signs that go the other way. As I said last month, the case for tightening to me seems to rest largely on us underestimating the amount of slack in the labour market and therefore the speed with which wages and prices will pick up (combined with policy lags).[7] But I don't currently see strong evidence for this proposition.

On the other hand the strongest case for loosening policy would in my view be to take out insurance against the risk of inflation expectations falling further. But I haven't seen enough evidence to suggest that inflation expectations have become materially de-anchored, or are likely to become so in the near future.

So overall, I don't see a strong case to change my view on the appropriate stance of monetary policy. I vote for no change in Bank Rate and no change in the stock of purchased assets.

I'd like to finish by standing back a bit and noting an issue I'd like us to examine in future. I am concerned about the potential interaction between ECB QE on the one hand, and the UK's current account deficit which is now at 6%, on the other. There are very strong reasons to believe that the deficit is broadly sustainable because it is very largely driven by lower income on investments abroad and because the UK is funding it by running down a small amount of a very large stock of foreign assets. We do not yet seem to have a very large net capital inflow. There are positive impacts of ECB QE for the UK but we should look closely at how that policy might impact the UK current account. The effects do not go only in one direction but given the current starting position I would like to understand them better.

Governor Carney. Thank you very much Jon. So Kristin and then Minouche please.

Kristin Forbes. Thank you.

The big news last month was the storms that started abroad but had substantial effects at home. In Boston it was the series of blizzards; in the UK it was oil prices and a series of monetary and exchange rate actions—especially on the European continent. The news this month is how these externally-generated storms are playing out domestically. In both cases, my interpretation of the data is that their effects are largely as expected. In the UK, these external forces have provided a moderate boost to the economy. In Boston, the effects were not nearly as positive. But today let me focus on how recent data indicates that the UK has transitioned from recession, to fragile recovery, to a solid and sustainable (albeit not spectacular) expansion. There are risks—as always—but a continuation of this solid and sustainable expansion has important implications for monetary policy.

The latest data confirm that these external events are providing some support to the UK recovery. Over the five years from 2008 through end-2012, GDP growth averaged a flat 0.0%, while average inflation was well above target at 3.3%. Over the next two years, as the recovery began, GDP

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[7] MPC Secretariat clarification: Mr Cunliffe had meant to say that the case for tightening rested on the Committee overestimating the amount of slack in the economy.

growth averaged 2.4% through 2014. All signs are that growth this year and next should be even stronger. Granted, there are tentative signs that the current forecast for 3.0% annual GDP growth at the start of this year may prove high—such as the recent weakness in investment and consumption. But, even if this weakness outlasts data revisions, this could just support our discussion last month of a potential stall at year-end that was arrested by external events. More recent data indicates underlying strength, and when combined with the real effects of lower oil prices and stronger growth abroad that are only starting to be felt domestically, this should solidify and strengthen the recovery.

Recent labour market data provide further confirmation that the solid recovery is continuing and, if anything, strengthening. Not only has unemployment continued to fall faster than expected, the labour-market recovery is rounding out. More of the jobs being created are permanent and full-time, allowing the part-time and self-employed to shift to better paying jobs. With the short-term unemployment rate at 2.8% (below its pre-crisis average of 3.2%), more of the long-term unemployed are finding jobs. Vacancies are at a record high, so that when combined with the fall in unemployment, the vacancy-unemployment rate has recovered quickly to over 90% of its pre-crisis average. Wage growth has continued its upward trend—and although still below its pre-crisis average on a year-over-year rate—this is even stronger than the headline suggests due to compositional effects—which could be pulling down wage growth by about 1.0 percentage point. Even though it is difficult to assess where "equilibrium" is in this labour market, it is showing strong signs of being close to normalisation.

There are obviously risks to a continuation of this solid and sustainable recovery. Downside risks include the long list of geopolitical concerns and issues in the euro area. Deflationary expectations could slow wage growth, or become engrained and affect consumer and investor behaviour. These effects have not appeared yet--but they could. One new issue on my radar is risks of exchange rate adjustments in currencies linked to the appreciated dollar – specially in Asia – which could generate substantial volatility in forex markets. It is not difficult to outline a number of scenarios leading to further sterling appreciation, which would drag on growth and inflation in the future.

I continue to believe, however, that more of the risks are on the upside. The boost from lower oil prices is only beginning to affect the real economy. Potentially even more powerful, over 20 countries have loosened monetary policy in just the first two months of the year. This will be the "gift that keeps on giving" long after the temporary effects of cheaper oil on inflation have faded. Global growth may exceed expectations this year – possibly even in the euro area. When could we last say that? Stronger demand outside the UK—especially in the euro area – could imply less drag from the current account. Even more important, the broadening strength in the labour market suggests a fundamental shift in which wage growth should continue. Even if inflation falls further in the short term, any of these scenarios I've outlined could cause inflation to accelerate faster than expected in the medium term.

Even if none of these upside risks materialises, the UK appears to be normalising after a severe crisis – except for the current level of Bank Rate. We all appreciate the critical role that near-zero interest rates have played in helping support this recovery. But now that the economy is normalising, keeping rates at such low levels will generate increasing costs. So when will the costs outweigh the benefits? I've been trying to assess a range of these potential costs. Several mentioned concerns are difficult to link directly to low rates. Other potential concerns – such as risks to financial stability and unsustainable sources of demand – could be a concern in the future and merit monitoring, but they don't currently appear to present substantial risks.

A cost of keeping rates at current levels which will likely first become an issue for us is of inflation building faster than expected, putting our intention to raise rates gradually at risk. Granted, inflation is currently well below target at 0.3% and likely to fall lower before picking up. But I am convinced by the analyses which show most of this results from short-term external effects – some mix from movements in oil prices, food and other commodity prices, and sterling. There is not yet evidence that these external effects are dragging down underlying inflation. For example, service inflation and core CPI inflation (excluding food, non-alcoholic beverages, and energy) both ticked up slightly by 0.1 percentage points to 2.4% and 1.4%, respectively. The mean of the seven measures of domestically-generated inflation that I follow have remained in the 1.4% to 1.8% range for the past 1½ years. The SPPI measure ticked down recently, but there will be larger ticks up in wage growth and unit labour costs that aren't even incorporated in those DGI measures yet due to data lags. There could be other factors that drag inflation down—such as if slower wage gains are justified by

low inflation or pass-through from sterling's recent appreciation this year. But given the tightness in the labour market, combined with the continued strength in demand, employees are well-positioned to continue to negotiate at least decent wage gains. This will likely start to boost inflation in the medium term as the effects of external influences fade.

Therefore, given all signs that this strong and sustainable recovery will continue, and be boosted by the previous "external storms" from oil and monetary policy, I continue to believe that the next move in rates will not only be up, but most likely before year-end. The downward pressure on inflation from external events, and stability in core and domestic measures of inflation, provides us a bit more time to ensure that the recovery continues and broadens, and especially that it is not derailed by another external storm. As we have learned from Boston, one storm is often quickly followed by another, and another. Also, even if my upside risks play out, inflation would be starting at such a low level, and the drags from external forces will continue, so that even in my more-optimistic scenarios, inflation will likely still take some time before reaching target. Therefore I vote to keep rates unchanged and asset holdings constant.

Governor Carney. Thank you Kristin. Minouche and then David please.

Nemat Shafik. Given that we have just emerged from the rigours of a forecast round and our forecast seems to be holding up against recent data, now seems a good time to stand back and take stock of where we are on the path to normalisation, and what risks lie off that path. I will cover the domestic economy, global activity and inflation.

On the back of Oscar season, this may seem like "The Theory of Everything". Though one suspects that with the benefit of hindsight when these transcripts are published they will be judged to benefit from "The Unexpected Virtue of Ignorance".

Let me start with the domestic real economy. The data on the month contained some mild disappointment in the form of another quarter of shrinking business investment, and a weaker than expected contribution from consumption. But overall I remain of the view that robust private domestic demand will continue in the foreseeable future, and that it will continue to underpin the growth forecast of between 2½% and 3% embedded in the central path.

For households, I expect this to be supported by the boost to real income delivered by falling energy prices. Indeed there is evidence of this beginning to feed through to consumer confidence in the general economic situation which had dipped slightly in the second half of last year. It seems the oil dividend, as the Governor refers to it, is beginning to pay out.

For businesses, in particular non-oil PNFCs, the conditions for investment remain good. In particular we continue to receive reports of improved credit conditions for large and medium-sized companies (who make up the bulk of investment), and the Bank's agents report competition amongst lenders. I see these improved credit conditions as the fruit of all that has been done to improve the resilience of the banking sector, and I expect it to provide sustained support to the real economy as lending growth picks up over the coming years. You could say that the FPC/PRA/FSB dividend is beginning to pay out.

There are of course domestic risks to activity. In particular from the general election, where the worst outcome would be an unclear result. In that event the uncertainty which would accompany prolonged negotiations over coalition-forming or a weakly-mandated minority government would be damaging to households and particularly business confidence. And we have anecdotes from the foreign exchange market that it is certainly looming large on financial markets' assessments of the short-term outlook.

But I remain of the view that the big risks to activity are posed by the world. To be sure, some of the political concerns from the euro area have lessened over the month: an agreement between Greece and the group-formerly-known-as the Troika may buy us some time, and the ECJ's broadly favourable opinion on OMTs would seem to have lessened the political limits on the ECB, and of course implementation of ECB QE is imminent. Our discussion yesterday left us somewhat more optimistic about prospects in Europe.

But while political risks have diminished a little, economic risks remain. The staff estimate that the euro area crisis took an estimated 3% off the level of UK GDP over the course of 2011 to 2012, and should the current nominal weakness begin to feed through to real activity in the euro area through undesirable debt deflation dynamics, I could easily believe the same effect would be repeated. The most obvious channels for spillover would be:

- Through the elevation of funding spreads for our own banks and hence higher interest rates in the real economy.

- Or through continued weakness in investment income from our overseas investments, prolonging the weakness in our current account, and ultimately jeopardising the flow of funds from investors through our capital account. I think there I agree with Jon, we really need to think more carefully about that channel of influence.

The other risk arises from the prospect of normalisation by the FOMC. Reading the tea leaves, it would seem that the ground has been laid for an increase in the target Fed Funds rate. One of the consequences of the "taper tantrum" was that it provided a trigger for market participants and emerging economies to put their houses in order. Nevertheless, I believe the risk from a snap back in US Treasury yields and a further appreciation of the dollar remain real. I would add that this risk is heightened by the revelation from staff that China is no longer adding to its stock of US Treasuries, thus removing one of the buffers which would have otherwise dampened a move higher in yields.

To sum up on activity: our central path for growth seems relatively straight, though the terrain off that path is decidedly rocky.

Let me turn next to inflation. For once it seems that there is little news on the month with inflation turning out broadly as expected. Though that still leaves us with the prospect of inflation falling further to 0.0% in March and April, and a significant chance of year-on-year negative inflation.

The staff have made the case that around two thirds of the weakness in inflation relative to its target is due to factors which will have only a transitory effect, such as the 50% decline in energy prices, and that the remainder is broadly consistent with the remaining degree of slack in the economy. The drag from slack will also prove transitory as the economy returns to normality, allowing inflation to return to target over the next couple of years. I believe this central case.

But I do retain a serious concern about the risk that inflation will persistently undershoot the inflation target. Let me be clear that I am not referring to the "bad deflation" scenario in which consumers postpone their consumption in the anticipation of lower future prices. That particular scenario seems a long way off the central path.

Instead I refer to the scenario in which five years of wage growth averaging 1.7% begins to become embedded in expectations of nominal growth. In such a scenario, it is possible that even when the output gap has been closed, and the economy is growing at potential, headline inflation will linger below target in the 1 to 1½% range. This risk concerns me because: it would be a failure to meet our inflation target; it would slow the adjustment in debt-to-income ratios that we have seen over the past few years; and by feeding through to lower nominal yields, it would limit our ability to lower Bank Rate without hitting the effective lower bound.

So let me sum up. I have said much about the risks, but I don't want them to detract from the most likely path – which is the central case remaining one in which:

- A steady if lacklustre recovery in the world economy neither impedes nor greatly contributes to headline UK GDP growth in line with its historical trend.

- Once the transitory factors currently affecting inflation have passed through, and once the output gap has been closed, inflation will remain around target.

The data we have seen thus far is consistent with that path: in particular the decline of unemployment to 5.7% and the pickup in private sector total pay growth to 2.5%. But the fact that inflation hasn't yet reached its trough means there is still one more bend to come before reaching the path of inflation approaching target. So this month I vote for no change in Bank Rate and no change in the stock of purchased assets.

Governor Carney. Thank you very much Minouche. David

David Miles. Thank you Mark. I will be fairly brief this morning.

Here is how I see things. First off clearly we've got the scope to move monetary policy in either direction. But the case for doing so is not a strong one at all. Over the last few quarters growth has been running a little bit above what's likely to be the cruising speed of the UK economy. Nobody is quite sure how much slack there is but it's pretty clearly been falling. I think there probably is some slack left in the economy but I very much agree with the view that we took in the February Inflation Report that we're likely to use up slack over the next few quarters. I do think that's the most likely outcome. And that's on the assumption that we made - the conditioning assumption in that Inflation Report - that normalisation in policy doesn't begin for several months. So given that, and given that inflation is pretty much at zero at the moment, I think the case to tighten policy today is not a compelling one at all. I do think it is very likely that inflation will move back up towards the target – particularly during the course of next year. And I think that is largely because the big falls in commodity prices clearly will drop out of the year-on-year comparisons toward the second half of this year. And I think the case on the other side for an easing in policy to try and accelerate that process to get inflation back to target even more quickly really isn't a compelling case at all. So I am not at all inclined towards voting for a more expansionary policy today either.

In some ways I think that is just as well because our scope to make policy more expansionary should we need to is pretty limited. There are costs to cutting Bank Rate. I think asset purchases would be effective although I think they could be considerably less effective than when they were undertaken in earlier years when financial markets were somewhat dysfunctional. I think there is a quite strong reason for thinking asset purchases are most effective when financial markets are dysfunctional, and that's not where we are now right now. So I think we have some ammunition that we could use if we need to make monetary policy more expansionary. But I don't think it makes any sense to use that ammunition right now.

Now of course all this could change and the case for easing policy might become stronger, I don't think it's at all a strong case today. One thing that several people have mentioned, and I do have a few observations on this very briefly, is about inflation expectations. My own view is that it's not very likely that inflation expectations will become a trigger to make a more expansionary monetary policy appropriate. My own view is that there is very little evidence at the moment that expectations are inconsistent with the broad thrusts of our central forecast which is that inflation moves back to target over the next couple of years. The most I would say is that household expectations might suggest - but it's only a might even here - they might suggest that some households think it will take longer to get back to the inflation target than in our central forecast. But I wouldn't go much beyond that. Even that is far from clear. And I suspect that even if that were the case, even if it's the case that right now households think it's going to take longer than we think is most likely to get back to 2%, I suspect that itself might be a short-lived phenomenon. I can't help but notice that actually there's been a very large increase in oil prices over the last few weeks. I suspect we're not far off the day when petrol prices for households in the UK actually edge up a little bit. And I suspect things like that have a very powerful impact on people's perceptions of current and future inflation. There is not much else to do when you fill your car up with petrol than watch the dial going round, so people are very sensitive to the petrol price more than probably any other price. And you fill up your car a lot. So I mean it sounds a kind of trivial comment but I suspect that expectations are quite sensitive to these things and we might actually be changing direction in terms of petrol prices more or less as we meet this morning.

I was also struck by the assessment that the Agents made which was presented to us at Pre-MPC a couple of days ago where they said that there's virtually no evidence, their phrase was "minimal evidence" of low inflation spilling over to pay. And as regards outright deflationary expectations – they are strikingly absent. I think on the whole, I would say that there seems a very widespread understanding in the UK right now, a very widespread understanding, that very low inflation rate is largely an oil, other energy price and food price phenomenon that is not likely to last very long. None of this means that there might not be a case for easing monetary policy down the road, but I just think the inflation expectations trigger is not a terribly likely one.

So I remain of the view that the most likely appropriate next move in policy is a tightening or if you prefer a sort of beginning of the gradual process of normalisation. If that's true it may well mean that

the UK is going to be struck in the middle if you like between the rest of Europe where monetary policy might even become easier and the US where policy might become tighter sooner than in the UK, quite possibly within the next few months. I don't think we should worry too much about that. In a way I think it is entirely natural; exactly what you would expect given the relative economic situations in terms of inflation, output growth and the amount of slack in the economy. And obviously with a floating exchange rate we can and should set policy by reference to what is happening in the UK and I don't think be overly influenced by the strategies of the ECB and the Fed. Might this mean nonetheless that there is a significant rise in the value of sterling against some currencies – the euro – and maybe a fall offsetting it to some extent against the dollar? Well maybe. But I am not at all confident in predicting – or expecting – this link. I think the link between differences in monetary policy and movements in exchange rates is not a very reliable one. In fact I would say it is reliably unreliable. In 2008 we had a very big fall in sterling, 25%. For nearly all of that year UK monetary policy was significantly tighter than the Fed's policy. Our Bank Rate was for nearly all of that year from memory 3 percentage points higher than the Fed Funds rate; we were 1 percentage point higher than the ECB, and we get one of the biggest depreciations in modern times.

I don't think any of this means we should be indifferent to a potential rise in the value of the sterling effective exchange rate – I think that would be unwelcome. Obviously we have a very large current account deficit, we've got slack in the economy, inflation is close to zero. An appreciation in the currency is not at all what we need at this point. But I don't think we can depend on some reliable link between movements in the exchange rate index and relative monetary policies. In which case I think moving monetary policy in either direction by more or less because of some expected knock-on effects on sterling is, I think, a bit of a mug's game.

I think we are far better to be guided by our own assessment of the outlook taking as given the exchange rate – much as we implicitly do in the Inflation Report.

Anyway today for me the decision is pretty clear cut, I vote today for no change in Bank Rate or in asset purchases.

Governor Carney. Thank you David, thank you everyone. Let's take as given as introduction that I associate myself with Ben's comments about limited domestic news, relatively significant financial market news, and comments of others which indicate some, on balance, positive news internationally.

I want to go to this question of implications for UK monetary policy of persistently low global inflation. Now we all know the relative statistics that inflation is below target in seventeen of the nineteen major inflation targeting countries, eleven of whom have inflation rates below 1%.[8] We also all know that there is a big element of oil in driving that and all of us have come independently to the conclusion that the most important factor behind the move in the oil price has been movements in actual, and importantly potential, supply of energy, much more so than demand shocks. And I would very much agree with what Ian said - I think it is quite an astute point in terms of the dynamics of storage, particularly floating storage - it may be wrong but it was reinforced by my visit to Saudi and their expectations. So on balance I actually think you might see a little uptick at the petrol pump as the dial moves. (I don't know where the dial moves. In the City Road I know, as Martin tells us, they have actually digital readings.) So we may see an uptick. But on balance there is a decent risk that we are going to see, we will test, new lows. March is an important month actually given refinery shut downs. Broadly a supply story - a net positive for the global economy, the main reason. But core inflation globally has been trending down as well. In the euro area it's running at 0.6%, in the US it's 1.3%. But those rates are down three quarters of a percentage point since 2012 and I just recall that our STIF for core inflation goes down to slightly below 1% in coming months. In that environment, globally there is a risk that persists and some risk, not necessarily going to pertain, that inflation expectations drift downwards further.

In terms of global monetary conditions there's been a flurry of activity, but on some measures global monetary conditions have actually tightened despite the moves by twenty central banks, and again it goes to where you think on inflation expectations but if you just take simple outturns and forecasts of inflation, global real rates have increased 100 basis points since the summer. So there's reasons why central banks are moving but the question is whether they've moved enough.

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[8] MPC Secretariat clarification: it was discovered subsequent to the meeting that inflation was below target in sixteen of the eighteen major inflation targeting countries, rather than in seventeen of the nineteen inflation targeting countries as the Governor had said.

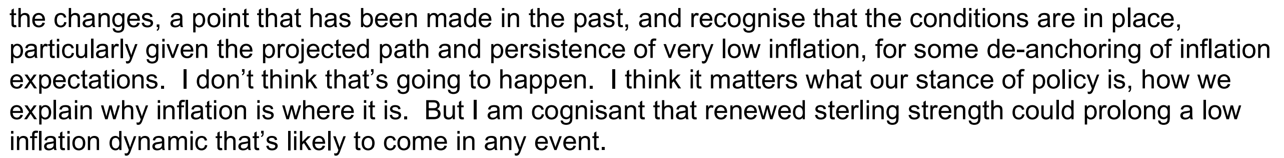
Now global inflation, global dynamics are important but they are not decisive here. There is only a 30% import content to our CPI basket. And co-movement since the advent of inflation targeting between UK inflation and OECD inflation is about 0.3 - various metrics, but that's the order of magnitude. But it is a transmission mechanism. In general, all things being equal, lower global activity leading to lower global inflation, a direct impact in terms of the import component (import channel), indirect impact through lower demand, bigger output gap, lower domestic inflationary pressures. And the standard offset again, all things being equal is easier policy relative to prior path, the exchange rate part of the transmission mechanism. And as we have been discussing yesterday and a number of you have made comments today, the extent to which currencies are trading on something else. Whether it is a certain effect of QE, whether it is some element of safe haven, or whether it is on relative growth prospects. And one of the reasons why having, and a number of us who have lived in currency markets for a long time, my experience of currency markets is they trade on different things at different times.

So in 2008 they were not trading on relative monetary policy, they were trading on financial stability and relative prospects and quite frankly perceptions of the effectiveness of the policy responses in countries and the UK was seen as a laggard at that point. I would suggest right now they are ignoring current account deficits. Monetary policy's interesting but relative growth in an anaemic world is particularly important. Others have detailed the recent strength in sterling in the past month and the 5½% increase since last year. At a time when foreign CPI, as I say, has fallen, this is all reinforcing obviously the deflationary impulse from foreign inflation. And as Martin suggested, and as we have discussed in the past, the fact that we have material pass through in this economy and protracted pass through in this economy, does potentially create this challenge of a persistent drag on domestic CPI which raises the question as to what we do to offset that.

I think we have to ask ourselves the question of what if foreign central banks are unsuccessful, or more unsuccessful than we expect, in returning inflation smartly back to their targets. We have the possibility, I won't use quite Andy's analogy, but basically half a percent is a high-yielding currency so to the extent to which relative yield matters, or relative growth matters, the possibility of further sterling strength as others have mentioned. And as we will be examining in greater detail, not to say that we haven't been examining it, but examining in greater detail in the run up to May, looking more closely at labour flows and again what's the impact of relative growth prospects. We have received large net migration flows since we've started to pick up smartly. A third of the net migration from Ireland (I was struck by this). Two-thirds of the net migration from Ireland went outside the European Union. Everyone else who left that went into the European Union came here. Everyone, nobody went to the Continent. And that is not the historic pattern, I went through those figures with the Irish authorities when I was there. There's different ways to cut it. We talked about one cut yesterday with the 300,000 increase an indication of the relative proportion of that entering the labour market. But since the end of 2012 two-fifths of the increase in overall employment has been accounted for by non-UK born employees. So we have the potential continuation of this dynamic reinforcing the compositional effects that we've seen and dampening the movement in wage growth.

So what's the point of all that. It's a risk, it's a dynamic and I mention it in part because in my assessment at least there's not a lot else that's material going on, but for the record I just reinforce that this puts the premium on generating domestic inflation and in that regard we are on track. The labour market is tightening, growth is sold, I won't repeat the figures. Unit labour costs are starting to grow at rates consistent with core inflation although a lot of that reflects poor productivity. We have a forecast which is heavily reliant on the consumer and the strongest growth in real incomes in a decade. The good news is we are on track for that at the moment and consumer confidence is, as others have mentioned, at a ten year high, retail sales on a strong upward trend, and there is little evidence in fact, I don't think I can find any evidence, of an actual deflationary mind-set setting in amongst consumers. The point David has made exceptionally in the past, now we have a chance to test it and we're not seeing anything on that front. I, like others, am minded to look through the recent measured weakness in investment, partly because some of that should reflect reduction in North Sea investment, but also just because, as Ian says and we had this conversation last year, it's inconsistent with the surveys, it's inconsistent with virtually every business we've talked to, it's inconsistent with credit conditions and the profitability of those firms, so we would expect to see, I would expect to see, that solid investment growth.

We are not seeing evidence yet of more generalised deflation, the proportion of prices that are falling remains consistent with the average over the past decade - that has not changed. We do need to remain vigilant, the main thing I take from the cool map of inflation expectations is not to ignore it but to take note of



the changes, a point that has been made in the past, and recognise that the conditions are in place, particularly given the projected path and persistence of very low inflation, for some de-anchoring of inflation expectations. I don't think that's going to happen. I think it matters what our stance of policy is, how we explain why inflation is where it is. But I am cognisant that renewed sterling strength could prolong a low inflation dynamic that's likely to come in any event.

Now what does it mean for policy? I don't think it's worth, apart from mentioning the risk, I don't think we need to act on it. We have successfully clarified that we could cut Bank Rate if necessary and we successfully did that in a way that didn't lead to market expectations, or agents' expectations, individuals expectations that we are actually were planning on doing so. And in my view, given the firming of consumption demand, the fact that inflation expectations are still consistent with the inflation target, such fine tuning isn't required and could actually run the risk of being counterproductive, undermining confidence and inducing unnecessary volatility in inflation and output. I don't think we need to be pre-emptive either about inflation at this stage. There is no clear and present danger in my view of an inflation overshoot. Wages and unit labour costs have a way to run, corporate margins are fat and global disinflationary pressures will likely persist for some time and could be reinforced by the currency. So I'm still in the camp of limited and gradual increases over the next three years consistent with the last Inflation Report, necessary to hit the inflation target but that today is not the day to begin that process. So I vote as well for no change to Bank Rate, no change to asset purchases.

So what I would like to do is just to confirm what I thought I heard for the record is that we all voted the same, with some nuance which will be reflected in the minutes, but we all voted for no change to Bank Rate, no change to asset purchases at this meeting. So it's 9-0 for that. OK, good.

So what we need to circulate is the draft news release. And it's exciting despite the fact that this is sixth year anniversary of no change to Bank Rate and our vote is consistent with the last few meetings. We have a paragraph which highlights that this is the first fully transcripted meeting and lovers, or haters for that matter, can mark their calendars eight years hence. We'll be able to read every pearl of wisdom and insight that was discharged this morning and then all the other 9,800 words.

[A draft press notice was circulated to MPC members]

If colleagues could just have a brief scan to confirm.

All right, we'll take that as approved, that will go out and we'll meet for minutes. So unless anyone has any other business related to today I will formally adjourn this meeting and for reference the transcript will stop at this point.