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MINUTES OF MONETARY POLICY COMMITTEE MEETING

3 and 4 June 1998

These are the minutes of the Monetary Policy Committee meeting held on 3 and 4 June 1998.

They are also available on the Internet (<http://www.bankofengland.co.uk/mpc9806.pdf>).

The Bank of England Act 1998 gives the Bank of England operational responsibility for setting interest rates to meet the Government's inflation target. Operational decisions are taken by the Bank's Monetary Policy Committee. The Committee meets on a regular monthly basis and minutes of its meetings are released no later than 6 weeks after each meeting. Accordingly, the minutes of the Committee meeting held on 8 and 9 July will be published on 12 August 1998.



MINUTES OF THE MONETARY POLICY COMMITTEE MEETING ON 3-4 JUNE 1998

1 At the start of the meeting on 4th June, the Committee formally acknowledged receipt of a letter from the Chancellor (attached as an annex) setting out the inflation target at which the Committee should aim in accordance with Section 12 of the Bank of England Act 1998.

2 Before considering the implications of the latest data for its immediate policy decision, the Committee discussed the external environment and the exchange rate; evidence on the pace of growth in domestic demand and activity; asset prices and monetary developments; and indicators of price and cost pressures, particularly in the labour market.

The world economy and the exchange rate

3 The Committee examined recent developments in the world economy. For the UK's major export markets, there appeared to be little evidence to change the central projection of external demand embodied in the *May Inflation Report*. The outlook for Japan had probably deteriorated further but there was continuing evidence of a recovery in the major continental European economies, while recent data for GDP growth in the United States had been revised upwards. While a number of countries in the world were facing financial and other economic difficulties those countries, even in aggregate, were not directly very important for UK exports.

4 Macroeconomic conditions in Japan remained adverse, but there were signs that difficult policy and reform decisions were being addressed. The situation elsewhere in Asia also remained unsettled, particularly in Indonesia. There had been a growing recognition that the necessary structural reforms in Asian countries would take a long time to implement and have the desired effects, but the immediate situation was not obviously deteriorating.

5 The situation in Russia was discussed. The pressures on the Rouble appeared mostly to have reflected domestic concerns, in particular the difficulty of raising government revenue, rather than contagion from other countries. The Russian economy was relatively small (around 2% of world GDP) and relatively closed. In 1996, only 1.1% of EU exports and 0.6% of UK exports went to Russia. Nevertheless it was possible that adverse developments in Russia could have knock-on effects elsewhere in the world. The main consequences for Western Europe would probably come indirectly via those East European countries with a large share of exports going to Russia: the Baltic States, Belarus and the Ukraine were the most exposed.

6 Taking these developments together the Committee concluded that the outlook for the world economy as a whole might be marginally worse than a month earlier and the downside risks to external demand had increased. These risks were reflected in some of the scenario analysis in the newly published OECD Economic Outlook. The most significant risk was of a more widespread financial and exchange rate crisis, but that could not be anticipated; policy would need to react if and when such a crisis were to occur.

7 In conjunction with external developments, the Committee considered movements in the sterling exchange rate. The effective rate had fallen by around 2% a few days before the May meeting of the Committee and had since fallen slightly further. It stood at 103.6 at close of business on the first day of the June meeting compared with 104.4 on the first day of the May meeting. The sustained lower rate had implications for the central projection of inflation published in the May *Inflation Report*, which had been based on a starting rate of 106.2: the 15-day average prior to the Committee's May meeting. Taken in isolation and applied mechanically, the step down in the exchange rate would be enough to raise the central projection back to around the level published in the February *Inflation Report*.

8 The external trade data for the first quarter of 1998 had shown the largest deficit since 1990, making a contribution of -0.6 percentage points to GDP growth, a negative contribution for the third successive quarter. In aggregate this was in line with the May central projection, but the geographical composition remained puzzling. It was not clear why net exports to the EU countries remained stronger than net exports to the non-EU countries. It was also somewhat surprising that import growth had been weak in the first quarter, given the apparent strength of both final demand and stockbuilding. However, the breakdown of imports by commodity suggested that growth in imports of consumption goods remained strong. Since a considerable proportion of other imports were subsequently embodied in exports, it was possible that weaker imports in part simply reflected weaker exports.

9 Taking the world economy and the exchange rate together, one view was that the net change in the external environment compared with the May *Inflation Report* assumptions was adverse for UK inflation, with the effects of the sustained lower exchange rate more than offsetting developments in the world economy, although the downside risks to world demand had increased. An alternative view placed more emphasis on the deterioration of the external environment, and noted that the magnitude of the exchange rate depreciation since the latest *Inflation Report* was commensurate with the magnitude of the exchange rate appreciation in the month following previous *Inflation Reports*.

The pace of domestic demand and output growth

10 The May *Inflation Report* had projected strong demand growth in the first quarter of the year, with a slowdown in subsequent quarters. Domestic demand growth had subsequently been estimated at 1.5% in the first quarter, but this included a large contribution from stockbuilding. Excluding stockbuilding, final domestic demand growth had been estimated at 0.8% in the first quarter, (and growth of 4.0% since 1997Q1) and was in line with the May central projection. Within the expenditure total, consumption growth of 1.0% had been marginally stronger than expected and investment growth of 1.3% had been weaker.

11 As yet there were few data to confirm or contradict the Committee's projection that demand growth would slow in the second quarter. The retail sales data for the three months to April did show a significant slowdown: to the slowest three-month growth rate (0.2%) since November 1995. However, it was possible that the April figure had been depressed by unusually wet weather and the March figure might have been affected by the timing of Easter. The Confederation of British Industry (CBI) Distributive Trades survey for May confirmed a weakening over the previous three months, but both the reported and expected balances had picked up slightly since a low point in March and were now at similar levels to August and September 1997. The reports of the Bank's regional Agents had been mixed, but with a majority indicating some weakening in sales growth. In contrast, survey data showed increasing consumer confidence, with consumers indicating strongly that this remained a good time to make a major purchase.

12 Other indicators of personal sector demand were also mixed. The Halifax and Nationwide measures of house price inflation were still divergent (5.0% and 11.9% respectively in the twelve months to May), although both showed signs of moderating. The Department of the Environment, Transport and the Regions (DETR) produced a quarterly series which estimated house price inflation of 9.1% in the year to Q1. The DETR figure seemed consistent with earlier Bank estimates based on Land Registry data, showing an inflation rate roughly midway between the Halifax and Nationwide estimates. Some activity measures of the housing market were slowing but net mortgage lending had risen in April. The rate of consumer credit growth remained high and personal sector money growth was still robust.

13 Given the mixed data, there was no clear confirmation yet as to whether personal sector demand growth was slowing as the Committee had projected, although the data could be interpreted as being broadly consistent with that projection.

14 The investment data for Q1 were weaker than assumed in the May *Inflation Report* central projection, but this appeared to be accounted for by weaker-than-expected public sector investment (government consumption had been stronger than expected). Evidence from the Bank's regional Agents suggested that strong borrowing figures for Industrial and Commercial Companies reflected a variety of reasons including some need for working capital and continuing

strong investment programmes, with little evidence of borrowing because of financial distress. However, in the agricultural sector, the Agents' inquiries about borrowing confirmed output and income data in showing severe difficulties.

15 In April, the public sector debt repayment had again been larger than generally expected, reflecting both higher revenues and lower outlays. Some of this was simply a timing effect but it now appeared more likely that self-assessment of income tax had generated a higher level of tax receipts which would carry forward. It seemed possible that the strong tax receipts in the 1997/98 financial year would cause the Office for National Statistics (ONS) to revise upwards the level of income for that period.

16 GDP growth for Q1 had been revised up slightly to 0.5%, in line with the *May Inflation Report* projection. The official data suggested that manufacturing output remained weak, with a small fall in the level of output in Q1. Looking backwards, staff estimates based on survey data suggested that the true level of manufacturing output could be higher than officially recorded. It was unclear what implications this would have for inflation without knowing what had happened to trend growth, but it would help explain the unusual weakness in recorded manufacturing productivity growth, and the high rate of increase in manufacturing unit labour costs.

17 Looking ahead, surveys of manufacturing output continued to show a deterioration in output and orders, with the CBI survey much more pessimistic than the Chartered Institute of Purchasing and Supply (CIPS) survey. The former showed a declining total orders balance (down to -17 in May) whereas the latter showed new orders close to flat (an index level of 49.0, just below the neutral 50 level). The Bank's regional Agents reported a broadly flat level of manufacturing output overall.

Monetary developments and asset prices

18 The Committee noted that, having fallen from growth rates of 11%-12% in the summer of 1997, aggregate broad money growth had since remained stubbornly robust, growing at a rate of 10.2% in the twelve months to April. Retail and personal sector M4 growth had both increased on a twelve-month basis but three- and six-month annualised rates were showing slower growth.

Credit growth was stronger, largely on account of a rising rate of ICCs' borrowing. In contrast, narrow money growth was weakening slightly, perhaps in line with weaker retail sales growth.

19 The already inverted yield curve had steepened further; its level and shape contrasted sharply with that of other countries. For some time, markets had been expecting domestic interest rates to fall over the next two years, but the timing of the expected fall was being pushed slowly further out, most recently in response to the earnings data.

20 The FT-SE 100 index of equity prices had fallen slightly during May, although the FT-SE 250 index had continued to rise. Movements in the FT-SE 100 were likely to have been influenced by international factors, given that multi-national companies were some of the largest in the index.

21 These financial indicators were slightly weaker overall than envisaged in the *May Inflation Report*, but neither they, nor the latest developments in the monetary data, were sufficient in the Committee's view to alter the outlook for inflation.

Prices and earnings

22 Price indicators for commodities, imports, manufacturing inputs and outputs all continued to show remarkably benign conditions for retail goods price inflation. And Bank estimates of retail margins in the first quarter of 1998 had fallen back to their 10-year average. These downwards pressures on retail price inflation had been offset by rising service sector price inflation, perhaps reflecting strong domestically generated inflation. This was most clearly seen in the stable level of RPIY inflation (the Retail Prices Index excluding mortgage interest payments and indirect taxes).

23 The labour market data released the week after the Committee's May meeting had confirmed that unemployment was still falling, but at a slower rate than in 1997. The main news had been a significant rise in headline earnings growth in the three months centred on February to an aggregate figure of 4.9% higher than the same period a year earlier (from an upwardly revised 4.6% in the three months centred on January). Surprisingly, the rise was bigger in manufacturing (to 5.3%, from a revised 4.7%) than in services (to 5% from 4.8%). Actual earnings growth in the twelve months to March was even stronger: 6.1% in manufacturing and 5.4% in services. The strength was almost entirely in the private sector for which the headline rate reached 5.6% in the three months centred on February (6.5% in the twelve months to March.) A potential pick-up in earnings growth had been signalled previously by some industrial contacts; on one view it was surprising that it had not happened sooner.

24 The Committee considered the impact and implications of bonus payments on the latest earnings data. The ONS had produced estimates of the impact of bonuses based on a survey

question about whether bonuses, performance-related or profit-related pay had been a significant element of the total pay bill that month. There was no direct evidence on the size of bonuses paid by all firms. The ONS had confirmed that there might also be an upward bias induced by the box-ticking survey procedure on the size of the effect. Despite these doubts about the magnitude, it was clear that there was an upward effect on average earnings growth which was likely to boost the headline rate for at least another two months before dropping out of the calculation. After that point earnings growth was likely to fall back. But it was misleading to focus on earnings growth excluding bonuses. Bonus payments might be backward looking, reflecting earlier profits, but on the other hand they could be an indication of a tightening labour market. Total wage drift - the difference between earnings and settlements - did not seem historically high.

25 Not wishing to place too much weight on the latest numbers, the Committee considered the underlying trend in the labour market over the previous two years. Private sector earnings growth had been drifting up over that period to reach a rate that was disturbing in relation to the inflation target. Notwithstanding the problems of measuring and interpreting bonus payments, the earnings data suggested that it was more likely that unemployment was below the rate compatible with stable inflation. In that case, it was probable that unemployment would have to rise to hit the inflation target on a sustainable basis.

26 The prospects for a significant fall-back in earnings growth were not particularly encouraging: the rise in inflation on the headline Retail Prices Index to 4% pa - reflecting higher taxes and last year's interest rate increases - could have the effect of increasing pay demands and possibly settlements. And the low rate of public sector earnings growth was not considered to be especially comforting, as it was unlikely to be sustainable indefinitely if the labour market remained tight.

27 The Government had not yet announced its decision on the rates and coverage of the National Minimum Wage. The Committee would consider the minimum wage in due course, in conjunction with the Government's other policies on the New Deal.

The immediate policy decision

28 The Committee discussed its immediate policy decision in the context of the balance between external and domestic pressures on inflation. On the one hand, output and prices were both being depressed by the earlier appreciation of the exchange rate, falls in world commodity prices and the weakening of the Asian economies. The restraining effects of these influences on inflation were expected to be temporary - prices, exports and imports would eventually adjust to new levels. On the other hand, domestic demand had been growing significantly faster than trend and would need to slow down if the inflation target was to be achieved. The issue was whether domestic demand

would slow sufficiently quickly to bring down domestically generated inflation before the temporary restraining effects of external pressures on inflation wore off.

29 Committee members agreed that the demand and output indicators for recent months showed the economy to be broadly on track with the *May Inflation Report* central projection. A range of views was discussed as to whether domestic demand might be slowing slightly more than expected or slightly less: the data were not convincing in either direction.

30 Committee members agreed that although the latest news did not obviously warrant a change to the assumption for growth in UK export markets made in the May central projection, the downside risks to the world economy had become greater since the May meeting. The most significant risk, though with a low probability attached, was of a more widespread financial crisis. As it had discussed at previous meetings, the Committee agreed that policy should not anticipate such a development.

31 One view was that the increased downside risks to inflation from the external environment were more than offset by the fact that the exchange rate fall had been sustained so that, other things being equal, the central projection for inflation published in the *May Inflation Report* was too low. An alternative view was that the exchange rate movement since last month should not be assumed to be permanent and, in any case, was unlikely to dominate the effects from weakening world demand, especially given the long lags in price effects from the exchange rate.

32 Members agreed that the recent earnings data heightened concern about inflationary pressures in the labour market. The trend in earnings over the previous two years had been clearly upwards and the latest release had to be interpreted in the context of a cumulative tightening of the labour market. The earnings data showed that domestic inflationary pressures were stronger than previously thought and so the need for domestic demand growth to slow down became more pressing.

33 On one view it was necessary for interest rates to rise in order to bring this about and to curb rising domestically generated inflationary pressures. The data over the past month meant that it would be imprudent to delay and that rates should therefore rise immediately. The question was

raised as to whether a quarter point rise in rates would prove sufficient, particularly if the spike in headline RPI inflation fed through to earnings growth. But no member of the Committee wished to press that case this month.

34 On another view, although the earnings data were worrying, they did not outweigh the other evidence on the domestic economy: sharply falling orders for manufacturing output, slowing retail sales growth, falling import volumes, rising inventories and a more steeply inverted yield curve. And to the extent that the recent earnings data reflected bonuses stemming from earlier profits growth, they were a misleading signal of current and future inflationary pressure. Quantity measures of the labour market suggested that it was no longer tightening. The peak of the economic growth cycle was now six months past and the international environment was fragile. Yet real short-term interest rates remained high and the yield curve signalled a tight monetary stance. On this view, a modest cut in interest rates towards a more neutral stance was still the prudent and appropriate move consistent with achievement of the inflation target.

35 The Committee discussed the possible market impact of an immediate change in rates, given that markets and commentators generally appeared to be expecting no further rise in rates and indeed, a gradual decline over the next two years. It seemed likely that the markets would raise their expected short-run path of official rates. It was judged unlikely that a 25 basis point move would, in itself, have a major impact on the equity market. It was possible that there would be an exchange rate reaction, but the upward pressure on sterling appeared to have moderated recently. Some Committee members felt that raising rates against such a background ran fewer risks than in previous months of exacerbating the imbalances in the economy.

36 The Governor invited members of the Committee to vote on the proposition that the Bank's repo rate be increased by 25 basis points, the change to be announced immediately. Eight Committee members (The Governor, Mervyn King, David Clementi, Alan Budd, Willem Buiter, Charles Goodhart, Ian Plenderleith and John Vickers) voted for the proposition. One member (DeAnne Julius) voted against, preferring an immediate cut.

37 The following members of the Committee were present:

Eddie George, Governor

Mervyn King, Deputy Governor responsible for monetary policy

David Clementi, Deputy Governor responsible for financial stability

Alan Budd

Willem Buiter

Charles Goodhart

DeAnne Julius

Ian Plenderleith

John Vickers

Gus O'Donnell was also present as the Treasury representative.

ANNEX: SUMMARY OF DATA PRESENTED BY BANK STAFF

A1 This Annex summarises the analysis presented by Bank staff to the Monetary Policy Committee on 29 May 1998, in advance of its meeting. At the start of the Committee meeting itself, members were made aware of information that had subsequently become available, and that information is included in the Annex.

I Monetary conditions

A2 Growth in the very narrow measures of money had continued to fall. Notes and coin rose by 0.4% in May. Annual growth fell to 6.2%, from 6.7% at the start of the year; and the three- and six-month annualised rates were 5.0% and 5.8%.

A3 Growth in the non-interest-bearing component of retail deposits had remained low. Average monthly flows into non-interest-bearing money (including notes and coin) had been £0.2 billion during 1998 so far, in comparison with an average monthly flow of £0.5 billion during 1997. Current account deposits might have been used to finance PEP purchases by persons, which had again been strong in April.

A4 Both retail and personal sector M4 rose more strongly in April, by 0.8% and 1.0% respectively, than in March, having been depressed in the first quarter by inter alia, higher self-assessment tax payments.

A5 ICCs' M4 rose by only 0.1% in April, with annual growth falling to 6.3%. The pattern of ICCs' deposits remained volatile month to month, but the underlying picture suggested a gradual slowing in annual growth to around 5%-6%. By contrast, OFIs' M4 remained buoyant, rising by 1.2% in April, with annual and period growth rates all around 22%-23%.

A6 Aggregate M4 rose by a robust 0.9% in April. Annual growth in April had nudged back above 10%, in part because of weak M4 growth in April 1997.

A7 Looking at the counterparts to M4, overfunding of the public sector deficit might, in an accounting sense, have reduced M4 by as much as £8.5 billion during FY1997/98. This negative influence on M4 had continued during April (£1.3 billion). However, it was likely that the true effect on M4 was smaller than this, because of offsetting movements in the other M4 counterparts. For example, although higher tax payments by ICCs and persons at the end of the financial year might have been financed by running down

deposits, these payments could, alternatively, have been financed by higher borrowing, leaving M4 unaffected.

A8 Aggregate M4 lending rose strongly in April, by 0.9%. Annual growth picked up to 8.8%, with period rates at or above 10%.

A9 Personal sector borrowing rose by 0.6% in April, in line with monthly growth in the past two years. Annual growth remained around 7%. Within this, however, there was a slightly different split of borrowing from in the recent past, with annual growth in secured lending picking up to 5.8%, while annual growth in unsecured lending edged back to 16.2%. But credit card borrowing (around 20%-25% of the stock of unsecured lending and 4% of total personal sector lending) remained strong, rising by more than 20% in the year to April.

A10 OFIs' borrowing rose strongly in April, by 2.2%. Annual growth rate remained high, at 19.3%, with three- and six-month annualised rates above 20%.

A11 ICCs' borrowing rose by 0.5% in April. Three- and six-month annualised growth rates were above the twelve month rate of 5.2%. An industrial breakdown of this borrowing indicated that the pick-up was reasonably widely spread across different industries. For example, growth had recently picked up strongly in the construction and agriculture sectors. However, this probably signalled very different patterns in activity in the two sectors, with construction output growing but the agricultural sector slowing.

A12 In May, the Agents undertook a special survey on the factors behind the rise in ICCs' borrowing. The survey covered 111 firms from the manufacturing, (non financial) services, agricultural and construction sectors, as well as 33 contacts at bank branches. The overall message across the whole economy from both firms and banks was that the reasons for increased borrowing had generally been positive, for example to finance fixed investment or acquisitions. The main exception was the agricultural sector, where there were severe problems, largely on account of sterling's appreciation being reflected in the green pound. In this sector, much borrowing had been in response to a worsening financial situation. Some manufacturers also suggested that lower margins and turnover were factors behind increased borrowing. Typically, these were firms facing intense international competition in home or export markets, such as textiles; a number were fearing for their survival, but would tend to seek alternative solutions to increasing bank debt.

A13 On price developments, there had been little change on the month in bank savings and loan rates. But some building societies had cut rates on fixed rate mortgages (eg, the Nationwide reduced their rate on

five-year mortgages by 20 bp). And more lenders had abolished mortgage indemnity guarantees for mortgages of up to 90% of the purchase price, following a similar move by a number of banks and building societies earlier in the year. This provided what was in effect a discount on the first year of mortgage payments. Overall, it appeared that competition in the mortgage market remains intense.

A14 There was little new survey evidence on inflation expectations during the month. The Merrill Lynch Survey of UK fund managers' inflation expectations for the twelve months to end 1998 and end 1999 had both fallen by 10bp, to 2.9% and 2.7% respectively, while the public's inflation forecast for the next year as implied by the GFK survey had fallen by 20 bp to 3.4%. The Merrill's survey was carried out before the publication of the Inflation Report and recent data, eg, February's average earnings and April's retail sales. The survey period for the GFK survey was 1-14 May.

A15 In the money markets, expected three-month interbank rates implied by sterling futures contracts rose slightly - by around 7 bp - to June 2000, and were broadly unchanged at longer maturities. 15-year forward rates derived from nominal bonds had fallen by 19 bp over the month; this was more than accounted for by a 27 bp fall in the real forward rates derived from index-linked bonds.

A16 The effective exchange rate had depreciated during the month, by 0.8% since the MPC's 6-7 May meeting and by 2.4% compared with the starting point used in the *Inflation Report* projection. Thus the current value of sterling was already significantly below the central projection embodied in the *Report*. A faster depreciation was identified as a specific risk in the *Report*, and the current rate implied by interest rate differentials for sterling in June 2000 lay between the central and mean projections for sterling.

A17 Sterling's effective exchange rate had reached a closing peak on 1 April. During April, movements in yield curves in the United Kingdom and the rest of the G7 were consistent with a depreciation, suggesting that news about monetary policy prospects had initially contributed to sterling's fall. But since the start of May, UK interest rates had risen slightly compared with the rest of the G7. An alternative explanation could be that the required 'excess return' on sterling compared with overseas assets had changed. This excess return can be defined as the difference between the expected depreciation of sterling over a given period and interest rate differentials. By using Consensus survey data of forecasts of sterling's future value, Bank staff had inferred the expected change in sterling (between end 1998 and end 2002) at specific dates over the past two years on the assumption that the surveys reported the expectations of price-setters in the bond market. The surveys suggest that sterling was expected to depreciate by around 2% over that period in June 1996, but by April 1998 the expected depreciation had increased to just over 10%. Conversely, expected interest rate differentials with the M6 for 1998-2002 had not varied much: expected UK rates remained cumulatively about 6-8 pp higher than overseas in the four-year window. This suggested that the

required excess return on sterling in June 1996 was positive, at around 4%, but was negative, at around -5%, in April 1998. The change in required excess return was most obvious for sterling against continental European currencies, rather than the US dollar. Possible explanations included growing uncertainty about the monetary prospects for the EMU area, and a portfolio shift out of prospective 'EMU currencies' into sterling in order to diversify portfolios.

A18 Turning to the more recent fall in sterling's effective rate, shorter-term surveys suggest that the (negative) required excess returns on sterling over the next two years had decreased by around 3pp between mid April and mid May. A possible explanation was that the 'Euro-weekend' on 2-3 May had reduced uncertainties about the prospects for ECB policy.

A19 Despite the uncertainties about its causes, sterling's recent fall was likely to put potential upward pressure on the inflation projection - directly via higher import prices, and indirectly by relieving some of the pressure on net trade from sterling's cumulative appreciation, which was now 24% since August 1996, rather than nearly 30% as at April 1.

II Demand and output

A20 GDP growth in 1998 Q1 had been revised up by 0.1 percentage points to 0.5% on the previous quarter, in line with the *May Inflation Report* forecast. The upward revision had partly been due to higher than previously recorded energy output. The contributions to growth from final domestic demand (domestic demand excluding stockbuilding) and net trade were consistent with the *May Inflation Report* forecast. However, domestic demand growth, at 1.5% on the previous quarter, had been considerably stronger than expected, due primarily to a £1.4 billion rise in stockbuilding. Although the rise in stockbuilding had been widespread, it had included a rise of £450 million in the stock of silver. The factor cost adjustment, which extracts taxes (less subsidies) from GDP at market prices in order to bring the expenditure measure of GDP into line with the income and output measures of GDP, had also been considerably larger than might have been expected given the rest of the expenditure data. The 4.3% rise in the factor cost adjustment between the last quarter of 1997 and the first quarter of 1998 had led to a marked divergence in the recorded rate of growth between GDP at market prices (1.0%) and GDP at factor cost (0.5%). That had reversed the pattern in 1997 Q4, when GDP at market prices had risen by only 0.3%, while GDP at factor cost had risen by 0.6%.

A21 Real consumer expenditure had risen by 1.0% in 1998 Q1 from the previous quarter. Increased spending on durables, and in particular on vehicles, had driven the rise. However, the increase in spending had been more than matched by a 1.7% rise in income from employment (60% of income before tax). The

consumption : labour income ratio had been rising since 1990, and had reached a historical high by the end of 1997. By contrast, the consumption : real personal disposable income ratio was below its historical average and had fallen back since the early 1990s. That implied that the rise in consumer spending in the present recovery has been supported by increases in financial wealth and investment income.

A22 More recent data on retail sales volumes had shown a rise of only 0.1% in April, reducing the three-month growth rate to 0.2% - the lowest rate of growth since November 1995. Moreover, the annual rate of increase in sales volumes had also fallen back in the three months to April, and was expected to continue to do so as the windfall-boosted increases of last year dropped out of the calculation. Nonetheless, the GFK consumer confidence indicator had risen in May for the second successive month, to 6.7%. The balance of respondents saying that it was a good time to make a major purchase had also remained high, at 18%, compared an average balance of 8.5% for the recovery as a whole. It was possible that the optimism regarding major purchases had been related to the recent appreciation of sterling, which had made some imported durable goods cheaper. Private car registrations had been around 20% higher in the first quarter than a year earlier, and import penetration of the UK car market was at a record high.

A23 The gap between the Nationwide and Halifax measures of annual rates of house price inflation had begun to widen again. The Nationwide index rose by 1.2% in May compared with April, though the annual rate of inflation moderated slightly to 11.9%. The Halifax measure of annual inflation had risen to 5.6% in April, but fell back to 5.0% in May, following a monthly rise of only 0.3% in May compared with April. The number of particulars delivered had been falling since mid 1997 and had weakened further in April. But net lending secured on dwellings had risen by £0.5 billion in April to £2.3 billion, suggesting that the rise in approvals in the previous two months had begun to feed through into higher activity.

A24 The PSBR had continued to undershoot expectations in the first month of FY 1998/99. The net repayment of £3.4 billion in April was significantly larger than most commentators had expected. The undershoot had been due to a combination of lower spending, particularly by public corporations, and higher tax receipts. It now seemed likely that the introduction of self-assessment had led to greater compliance.

A25 Total investment had risen by 1.3% on the previous quarter. Business investment had risen by 1.5%, implying a small negative contribution from public sector investment. The rise in business investment had been due to a 13% rise in investment by utilities and oil companies, which had more than offset a 0.5% fall in investment by private service sector firms. Manufacturing investment rose slightly on the quarter. By asset, investment in vehicles, ships and (in particular) aircraft had accounted for around one third of the rise in total investment, in line with the contribution such investment had made during 1997 as a whole. Dwellings investment and investment in plant and machinery had also risen on the quarter.

A26 Industrial and commercial companies (ICCs) had run a financial deficit in 1997, the first since 1992. That implied that further growth in investment would rely more heavily on external finance. However, the prospects for further investment growth still looked positive. ICCs' capital gearing had been falling, and equity market valuations implied that future profit streams were expected to outstrip significantly the level of current debt commitments. And though income gearing had risen in 1997 Q4, at least half of that rise had been due to the introduction of the windfall levy. Survey evidence from the BCC indicated that service sector plant and machinery investment plans had remained positive, and that this was expected to more than offset any weakness in manufacturing investment plans. Continued growth in new construction orders suggested that construction-related investment should also continue to rise.

A27 The real net trade balance in goods and services had deteriorated further in 1998 Q1. The deficit was the largest since 1990 Q3. The deterioration had been less excluding oil and erratics, but net trade excluding these items had made a third consecutive negative contribution to GDP growth. In value terms, the total deficit in trade in goods had narrowed in March, primarily because of a narrowing in the deficit with non-EU countries, which had continued into April. Excluding oil and erratics, there had been little change in the goods trade deficit, but it seemed probable that the trend had remained downwards. The deficit in goods trade with other EU countries had remained surprisingly flat. There had been a similar pattern in the French trade data. The French trade surplus with the rest of the European Union had risen sharply since the beginning of 1997, and despite a 10% real depreciation of the French franc against the dollar, the balance with the rest of the world had slipped into deficit. Underlying UK import volume growth had remained surprisingly weak during the first quarter, though to some extent that had been because of a 6% fall in imports of cars. Imports of finished consumer goods rose by 3% on the previous quarter.

A28 On the output side, 1998 Q1 service sector growth had been revised down by 0.1 percentage point the previous quarter to 0.7%, though the published index numbers had remained unchanged. Growth in the distribution, hotels and catering sector had been revised down by 0.3 percentage points to 0.6%. Manufacturing output had contracted slightly during the quarter, as implied by the preliminary GDP estimate. Overall industrial production output fell by 0.3%, though it remained slightly higher than a year earlier. Construction sector growth, at 1.1% over the quarter, was stronger than had been indicated in the preliminary GDP release.

A29 The weakness in the official manufacturing data, which showed the output of the manufacturing sector falling in two successive quarters, contrasted with the relatively more buoyant survey data. Although recent survey data had weakened, ONS data had shown virtually no increase in the level of manufacturing output since 1995. Using a statistical technique to quantify CBI balances on the volume of output in the

previous four months implied a significantly higher level of manufacturing output. That would fit past sectoral experience better. The official data showed a marked divergence in growth between the output of the manufacturing and service sectors during the current recovery, which was unusual in an historical context and had begun well before the appreciation of sterling.

A30 International comparisons had continued to show UK industrial production declining relative to the other major EU economies. Industrial production in the EU15 had risen by 4.6% in the three months to January compared with the same period a year earlier. That contrasted with growth of only 0.3% in the United Kingdom in 1998 Q1 compared with a year earlier. However, the expected recovery in EU domestic demand had remained patchy, with Germany in particular showing only a gradual recovery to date. US first-quarter GDP had been revised up by 0.2 percentage points to 1.1% on the previous quarter. The upward revision had been due to higher than previously recorded stockbuilding, which had offset a more negative contribution from net trade.

III Labour market

A31 Indicators of labour demand suggested that the pace of growth had slowed in recent months. LFS employment was 39,000 higher in the three months to March 1998 than in the fourth quarter of 1997. This was similar to the rise in the three months to February, but slower than either the rise during Q4 or the average rise in the past twelve months.

A32 Part-time employment accounted for almost all of the recent rise: full-time employment had been flat over the past quarter. By contrast, the LFS series for hours worked increased by 0.8% in Q1 from the previous quarter, and by 2.1% compared with a year earlier. Stronger growth in hours worked than in employment suggested a rise in overtime. But the hours worked data are very volatile, making firm conclusions difficult.

A33 The CIPS survey suggested that manufacturing employment fell for the third consecutive month in May. That was consistent with reports from the Bank's Agents, although less timely ONS data suggested that manufacturing employment rose in 1998 Q1, albeit slowly. The CIPS service sector survey for May indicated continued rapid growth in service sector employment, though some Agents suggested that service sector recruitment was slowing.

A34 A slowdown in the pace of tightening was also apparent from the unemployment data. LFS unemployment fell by 33,000 in the three months to March, to 6.4% of the workforce. That fall was smaller than the 78,000 fall in the previous quarter, and than the average decline during the previous year. It was

also smaller than the fall of 52,000 in the three months to February. Almost all of the recent fall was accounted for by the long-term unemployed (defined as those unemployed for more than one year). In fact, the long-term unemployed accounted for 238,000 of the 275,000 fall in unemployment in the past year. That could reflect either a fall in the inflow to long-term unemployment, or a fall in the average duration of the long-term unemployed. It is difficult to extract flows data from the LFS, but work using claimant count data to measure outflow rates suggested that the average duration fell during 1997.

A35 Continuing falls in the number of long-term unemployed have meant that they account for a declining proportion of total unemployment. This is normal in a recovery: the share of the long-term unemployed among the unemployed has been counter-cyclical since at least 1984. This could indicate that as the labour market tightens, employers extend their recruitment activity more widely, improving the job prospects of the longer-term unemployed. This implies that the long-term unemployed are an imperfect substitute for the short-term unemployed, and a fall in their share of total unemployment is indicative of labour market tightness. Econometric work by Bank staff had provided support for this theory: it suggested that the long-term unemployed do exert downward wage pressure, but less so than the short-term unemployed.

A36 Claimant unemployment fell by 18,000 in April, to 4.8%. That was the largest monthly fall for four months, although it was smaller than all but one of the monthly falls during 1997.

A37 The data on vacancies were mixed. The stock of vacancies edged up in April by 1,500. Bank analysts had adjusted the back data for an overcount in the stock of vacancies. The corrected series showed that the trend in vacancies continued to rise. But the number of notifications of new vacancies fell by 1,500. The number of notifications remained around the average levels of the second half of 1997.

A38 There were few new data on skills shortages. The Reed survey for May suggested that 71% of firms were experiencing shortages of skilled applicants when they recruited. This was in line with February's survey. The Agents suggested that on balance skills shortages had continued to intensify, although at a less rapid pace, with five regions reporting that they had stopped intensifying. One survey pointing in the opposite direction was the construction trends survey, which reported an easing in labour availability in Q1, at odds with the Agents' view of pressures in this sector. The CIPS service sector survey for May indicated that skill shortages in the service sector were pushing up input costs.

A39 Headline underlying annual earnings growth increased to 4.9% in February, up from a revised 4.6% in January. Within that, services earnings growth increased from 4.8% in January to 5% in February, and manufacturing earnings rose from 4.7% to 5.3%. The headline numbers are centred moving averages of

twelve-month growth rates. In March, those monthly growth rates were 5.4% for the whole economy, 6.1% for manufacturing and 5.4% for services.

A40 Bank analysts had tried to identify how far recent earnings data have been affected by bonus payments. The ONS had suggested that bonuses in March 1998 were around 25% larger than a year earlier. But there are a number of problems with using that figure to estimate the contribution of bonuses to earnings growth. Though bonuses may have been particularly concentrated in March this year, these other elements of non-basic pay may well have a continuing effect in the coming months. Second, the ONS had suggested that its method of calculating bonus effects may be biased upwards, for reasons connected with the way firms respond to the earnings questionnaire. Firms ticked a box and gave a figure to indicate 'significant changes' in bonus payments each month. So the answers from those firms that paid bonuses in March each year but considered a payment in one year insignificant and payment in the next significant could result in a spuriously large recorded rise in bonus payments in the twelve months.

A41 The Bank's Kalman filter-adjusted earnings index suggested that there had been a pick-up in bonus-smoothed earnings from 4.74% in February to 4.85% in March. But this number could be revised back down if April's figure for average earnings was much lower.

A42 If bonus payments were especially high in March, then earnings growth in the twelve months to April and subsequent months would be lower. But this did not mean that bonus payments should be discounted. Though bonuses were a more flexible element of total remuneration, if they were paid to encourage recruitment and retention, they would reflect current labour market pressures as much as normal pay did. However, if bonuses were linked to company profits, they might be a backward-looking indicator of rapid economic growth. Either way, they still reflected a cost to firms and income for workers. Any estimate of overall earnings trends needed to smooth identified bonus payments across the year.

A43 Further evidence on the differential between public and private sector pay was presented. According to the ONS, private sector pay had outpaced that in the public sector since 1993. In the year to February 1998, public sector pay grew by 2.6%, while that in the private sector grew by 5.6%. One possibility raised was that special factors were distorting the divergence. DfEE figures suggested that there had been a substantial rise in the number of teachers taking early retirement in the past year, probably linked to early retirement deadlines in 1997/98. If those early-retired teachers had been replaced by 'cheaper' young teachers, then the earnings data could give a misleading impression of the wage rise received by each individual. The staging of many public sector pay awards was also likely to have had a temporary downward influence on public sector earnings. But it was unlikely that those two factors alone could explain the whole of the negative wage drift in the public sector.

A44 Staff presented some analysis on whether public sector pay was likely to catch up with that in the private sector. Work by Elliott and Duffus (1996) suggested that public sector earnings had been trending downwards relative to the private sector over the past twenty years. And the relative fall seemed to have been particularly fast in the past five years. Any signs of a catch-up should be reflected either through public sector labour disputes or through recruitment and retention difficulties. But the number of days lost to industrial action was very low by historical standards. And the DfEE survey of 'hard-to-fill vacancies' showed that although such vacancies were increasing in the public sector, they had risen even more in the private sector. Staff also presented data on schools' teaching vacancies which, although rising, remained much lower than in 1990.

A45 The teachers' and nurses' pay review bodies had tended to highlight specific areas of recruitment difficulties, and problems recruiting trainee teachers and nurses, rather than generalised problems. Though these were certainly signs of emerging pressure, most settlements for this year had already been agreed, and so there was little evidence to suggest an imminent bounce-back in public sector pay.

A46 On provisional data, the twelve-month employment-weighted mean settlement increased from 3.4% to 3.6%. But the preponderance of public sector settlements led to the three-month mean falling from 3.9% in March to 3.1% in April.

IV Prices

A47 The Bank's commodity price index was provisionally estimated to have increased by 0.2% in April. This largely reflected a rise in oil prices. Excluding oil, commodity prices were unchanged. And they were likely to fall once food price data were included, following the sharp reduction in milk prices announced in April (food prices are assumed to be flat in the provisional estimate). On the provisional basis, the annual rate of deflation in commodity prices had fallen to 10.1% in April from 14.2% in March. But there were no clear signs of a change in the recent trend of flat or falling commodity prices: metal prices had fallen for the eighth consecutive month, and cotton and rubber prices were lower, both possibly reflecting the effects of the East Asia situation. However, the recent depreciation of sterling may be an upward influence on some commodity prices in the next few months. The oil price had risen again in May, by 2.5% in dollar terms. But prices were not expected to rise much more, as supply continued to exceed demand.

A48 Manufacturers' input prices had fallen sharply in April, by 0.9%, despite the rise in oil prices. This fall had been largely due to lower milk prices following the renegotiation of milk supply contracts. Prices of imported foodstuffs and other imported material had also fallen further. Lower material prices had

continued to be a downward influence on manufacturers' output prices. Excluding excise duties, these had fallen by 0.2% in April, taking the annual rate of inflation to -0.2%. Output prices including duties had increased by 0.1% in the month, because of the higher petrol duties announced in the Budget. The CBI Industrial Trends Survey had pointed to continued downward pressure on manufacturers' prices. The May survey recorded a balance of -12 (seasonally adjusted) for price expectations over the next four months. The close correlation between output price inflation and retail goods price inflation in the past suggested continued downward pressure on retail goods price inflation, consistent with the *May Inflation Report* forecast.

A49 Trade prices had fallen further in March. In particular, there had been a 0.9% fall in import prices (0.7% excluding oil prices). After showing signs of moderating in recent months, the annual rate of deflation in import prices increased to 5.4%, from 5.0% in February. Export prices had fallen by 0.3% in March, taking the annual rate to -4.8%. Provisional data for April covering non-EU trade had showed a further fall in import prices of 0.3% (0.5% excluding oil). Export prices to non-EU countries were unchanged in April.

A50 Annual retail price inflation had risen sharply in April on both the RPIX and RPI measures, to 3.0% and 4.0% respectively. The increases had reflected a series of one-off increases in items such as council tax and rents. The reduction in MIRAS announced in the Budget also contributed to the increase in RPI inflation. But the main contribution had come from the increase in petrol duties announced in the March Budget. These had previously been increased in July last year. Until those effects dropped out of the twelve-month calculation this July, RPIX inflation would be temporarily higher than would otherwise have been the case. Consequently, changes in annual RPIY inflation were considered to be more relevant to an assessment of the trend in inflation over the current period. RPIY inflation increased by 0.1pp to 2.2% in April, reflecting a rise in services price inflation. The pattern of falling goods price inflation and high services price inflation continued to be evident: RPIY goods price inflation fell to 0.6% (1.0% in March), compared with RPIY services inflation of 3.5%. The trends evident in goods prices in the first quarter of the year had again been apparent in the April data: leisure goods prices fell, with lower audio-visual goods prices, perhaps reflecting the depreciation of East Asian currencies; and new clothing and footwear lines had been introduced into the shops at lower prices than last year, perhaps reflecting further effects from sterling's appreciation, as demand growth slowed.

A51 Consistent with the picture of falling goods price inflation, retailers' margins were estimated to have fallen further in 1998 Q1 (Bank estimates). This had reflected a fall in the level of goods prices during the quarter, alongside a small rise in total costs. Bank estimates suggested retailers had widened their margins in the last two years. But the recent fall meant that margins were now only 0.3pp above their level in 1997

Q1, and roughly in line with the average level over the last ten years. The rise and subsequent fall in retail margins had been consistent with a lagged response in retail pricing behaviour to sterling's appreciation and lower import prices, particularly as the growth in retail sales had slowed.

A52 A further fall in inflation in the M6 economies had been evident in 1998 Q1. This had been larger than most forecasters had expected, and inflation forecasts for 1998 had subsequently been revised down. But in contrast with the M6 economies, UK inflation had not fallen sharply over this period. The reason for the common fall in inflation across the M6 economies appeared to be related to falling commodity prices, and particularly energy prices.

A53 In the United States, energy and petrol prices had accounted for all the fall in CPI inflation in the recent period, while in the United Kingdom there had only been a small negative contribution to inflation from lower energy prices (fuel and light, petrol). It appeared that UK petrol retailers had not yet passed on all the fall in oil prices to consumers. Petrol prices net of duties (RPIY), which were closely correlated with oil prices, had fallen by much less than the oil price in recent months. Retailers may have widened their margins, perhaps as a result of the earlier petrol price-war. Alternatively, because the oil price is a relatively small proportion of the final retail price in the United Kingdom, retailers may allow margins to fluctuate in the short term in response to movements in oil prices, particularly if these movements are expected to be reversed. If oil prices remained lower, there could be some downward pressure on petrol prices this year, though this was unlikely to influence overall inflation prospects in the medium term.

Foreign exchange

A54 There were three main developments over the month: the fall in sterling; yen weakness; and a strengthening of euro currencies following the ‘euro weekend’ at the beginning of May, though the Deutsche Mark had lost ground towards the end of the month.

A55 The sterling effective exchange rate had fallen by 2.6% since the end of April. Much of this was in the first few days of May, before the May MPC meeting. The fall seemed to be due partly to EMU-related factors, including a move by trading houses to cover short positions in euros now that uncertainty about the start date and membership of EMU and the ECB Executive Board had been resolved. This was consistent with the analysis of excess returns based on Consensus surveys of forecasts reported in “Monetary Conditions” above.

A56 Uncertainty about the pound/Deutsche Mark exchange rate, measured by implied volatility on currency options, increased at the one-month horizon around the time of the euro weekend. But longer horizon pound/Deutsche Mark uncertainty had changed little. Implied correlations between the pound and Deutsche Mark showed a fall at the one-month horizon, whereas the implied correlation between the pound and dollar was little changed. An increased prospect of EMU-related news in the short term was consistent with this behaviour, but the lack of a longer-term response did not support the explanation for sterling’s fall being a fundamental reassessment of its ‘safe-haven’ status.

A57 The international foreign exchange background was dominated by yen weakness. The yen had fallen by 4.6% during the month, reaching a seven-year low against the dollar, of 139, on May 29. Yen depreciation reflected the weakness of the domestic economy, and concerns about Indonesia and other parts of Asia. The FOMC’s move to a tightening monetary policy bias, announced on May 21, came as no surprise to the exchange markets. The Deutsche Mark appreciated modestly during the month, its moves moderated by the fact that euro currencies account for 57% of its effective index, but moved down on concerns about Russia later in the month.

Bond and money markets

A58 The main feature of the month was a reappraisal of the market's previous optimism about the prospects for cuts in official UK interest rates next year. Gilt-edged yields were broadly unchanged since the previous MPC, in common with most international markets.

A59 Short-term interest rate expectations drifted up following the euro weekend, accompanying the fall in sterling. Domestically, the most significant impact on short sterling came on May 13. The release of higher-than-expected average earnings data initially had a material impact, while the *May Inflation Report* seemed to have little effect. Short rate expectations rose further as market participants and the press digested the new information and analysis in detail. Later, the retail sales data were seen as soft and some of the rise in expectations was reversed. Despite these movements in short sterling, market participants did not expect a move in the Bank's repo rate for some months. The gap between interbank rates implied by short sterling futures and the repo rate had widened since last summer to around 30 basis points (from 20-25 basis points). So the June 1998 contract, pricing in three-month interbank rates of 7.50%, discounted official rates close to the current 7 ¼% level.

A60 Gilt yields were stable over the month as a whole. They rose at the beginning of May, influenced by weak sterling and then the earnings data and *Inflation Report*. They fell later in the month, supported by the well-covered 30-year gilt auction, the possibility of lower supply after the latest PSBR data and, later, a 'flight to quality' as there were further concerns about Asia and then Russia. Real yields on index-linked bonds fell at the longer end and rose at the short end. But real yields were particularly difficult to interpret this month, because they were affected by the release of the RPI for April. Although the April RPI was broadly in line with market expectations, so that bond prices were little changed on the news, the increase in RPI was much higher than the market's conventional assumption embodied in the calculation of real yields. Real spot yields jumped up on the day of the news and the derived inflation expectation curve jumped down. The movement was particularly sharp at the short end.

Equities

A61 UK and US equity markets had fallen slightly since the last MPC. In the United Kingdom, the FT-SE 250 and small capitalisation indices had risen, in contrast with the FT-SE 100. It had been suggested that renewed concerns about Asia lay behind the recent weakening of the FT-SE 100, though evidence on the stocks with the most direct exposure to Asia did not support this.

A62 Implied volatility of the UK and US equity markets had fallen to levels before the Asian crisis in the fourth quarter of last year. The negative skew in the probabilities attached to future levels of the FT-SE 100 (measured by the gap between mean and mode as a percentage of mode), which had increased after the Asian crisis, had returned to its five-year average.

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3 June 1998

**The Governor
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REMIT FOR THE MONETARY POLICY COMMITTEE

The Bank of England Act came into effect on June 1. The Act states that in relation to monetary policy, the objectives of the Bank of England shall be

- (a) to maintain price stability, and
- (b) subject to that, to support the economic policy of Her Majesty's Government, including its objectives for growth and employment.

In order to comply with the Act, this remit sets out what price stability should be taken to consist of and what the economic policy of the Government should be taken to be.

Price stability

I confirm that the operational target for monetary policy remains an underlying inflation rate (measured by the 12-month increase in the RPI excluding mortgage interest payments) of 2 1/2 per cent. The inflation target is 2 1/2 per cent at all times: that is the rate which the MPC is required to achieve and for which it is accountable.

My intention is to lock into our policy making system a commitment to consistently low inflation in the long term. The real stability that we need will be achieved not when we meet the inflation target one or two months in succession but when we can confidently expect inflation to remain low and stable for a long period of time.

The framework takes into account that any economy at some point can suffer from external events or temporary difficulties, often beyond its control. The framework is based on the recognition that the actual inflation rate will on occasions depart from its target as a result of shocks and disturbances. Attempts to keep inflation at the inflation target in these circumstances may cause undesirable volatility in output.

But if inflation moves away from the target by more than 1 percentage point in either direction I shall expect you to send an open letter to me, following the meeting of the Monetary Policy Committee and referring as necessary to the Bank's Inflation Report, setting out:

- the reasons why inflation has moved away from the target by more than 1 percentage point;
- the policy action which you are taking to deal with it;
- the period within which you expect inflation to return to the target;
- how this approach meets the Government's monetary policy objectives.

You would send a further letter after three months if inflation remained more than 1 percentage point above or below the target. In responding to your letter. I shall, of course, have regard to the circumstances prevailing at the time.

The thresholds *do not* define a target range. Their function is to define the points at which I shall expect an explanatory letter from you because the actual inflation rate is appreciably away from its target.

Government's economic policy objectives

The Government's central economic objective is to achieve high and stable levels of growth and employment. Price stability is a precondition for these high and stable levels of growth and employment, which in turn will help to create the conditions for price stability on a sustainable basis. In the recent past, instability has contributed to the UK's poor growth performance, not least by holding back the long-term investment that is the foundation for a successful economy.

The monetary policy objective of the Bank of England is to maintain price stability and subject to that, to support the Government's economic policy, including its objectives for growth and employment.

Accountability

The Monetary Policy Committee is accountable to the Government for the remit set out in this letter. The Committee's performance and procedures will be reviewed by the Court on an ongoing basis (with particular regard to ensuring the Bank is collecting proper regional and sectoral information). The Bank will be accountable to Parliament through regular reports and evidence given to the Treasury Select Committee. Finally, through the publication of the minutes of the Monetary Policy Committee meetings and the Inflation Report, the Bank will be accountable to the public at large.

Restatement of the Remit

The inflation target will be confirmed in each Budget. There is a value in continuity and I will have proper regard to that. But I will also need to consider the case for a revised target at these times on its merits. Any changes to this remit will be set out in the Budget. The Budget will also contain a statement of the Government's economic policy objectives.

GORDON BROWN