Mark Carney (MC) interview with Robert Peston (RP) BBC 13th January 2015

RP: Inflation at 0.5% we have only seen it as low as that once actually since they started calculating CPI. Is 0.5% inflation good news or bad news for Britain?

MC: Well, it depends why inflation is at that level, but actually I would say by and large these figures are good news in the short term for British households. It’s largely caused by lower petrol prices and a lower food prices, that means your pound is going to stretch farther – lower prices at the pump and in the shops. The issue is to make sure that this doesn’t become more generalised and that we don’t see low and falling prices more generally, because a little bit of inflation is good for the economy, it greases the wheels of the economy. The other good news, I’m just giving you good news today, is we have the means at the Bank of England, and the will and the responsibility by Parliament to bring inflation back up to the 2% target level that Parliament has given to us and we generally do that within a two year horizon and we are certainly going to do that with the current outlook.

RP: Was this a bit lower, 0.5%, than you expected?

MC: Well, it is a bit lower than we had expected in November, but given the continued movements in commodity prices; most notably the oil market as you have seen and reported has moved substantially all the way through December and in fact it is down another 25% relative to where it was in December. We have been updating our forecast so when it actually came out this is what we had expected.

RP: So would you expect inflation to fall even further given what has been happening to oil prices?

MC: Well, there are always events, but given what has happened and what is in the pipe line, so to speak with oil prices, the petrol price you can expect to fall further in fact it was 117p on average for unleaded in December and was 109p this morning at the pump, we would expect it to fall further and for CPI to continue to drift down in coming months

RP: What would you be looking at or looking for as signs that what you might call benign low inflation is becoming pernicious deflation?

MC: Well a couple of things. First, we look at all prices and see if this is becoming more generalised but we also look very closely at household inflation expectations, expectations in markets and crucially those expectations over the horizon that we as the MPC of the Bank can affect inflation and that tend to be about a year and a half to two years out and as I said we have the ability to bring this low inflation back up to that 2% target so that the economy can continue to function as is.

RP: Can you tell us right now whether you think the balance of risks has shifted towards deflation?

MC: Well, I think in terms of our horizon it is a little softer but let me be clear what we are talking about in terms of bringing back to that target is still an environment in which interest rates increase in the UK. So it’s a question of the pace of those interest rate increases and the degree. Relative to a year ago it’s probably a little more gradual and a little more limited than it was then, largely because of factors outside our shores, there are these disinflationary or low inflation pressures globally. But we are still in a world where we would expect to start to what we call normalise policy, raise interest rates, over that horizon.
RP: So just to be absolutely clear you are not seeing anything which would suggest to you that we need to follow what is going on, for example in Eurozone, they are expected to do a bit of quantitative easing – we don’t need to do any more quantitative easing here?

MC: The Eurozone is in a very different place. They don’t have wage growth; they have record unemployment in many places. We have grown a half a million jobs, we are seeing wages start to turn, we are seeing solid growth across the economy and we are in an environment where you can expect that interest rates will increase, likely at a gradual and limited pace, so we are in a different spot. The Eurozone, they have been very clear, President Draghi has been very clear, other members of the ECB have been clear that we can expect considerable asset purchases, quantitative easing, in the months to come and they need that in order to fulfil their remit. We have a very different orientation of monetary policy here.

RP: But for the absence of doubt, obviously I understand are never definite, what we might see here is interest rates here lower for longer?

MC: Well it all depends relative to when. If we were sitting down a year ago relative to my expectations at that time yes lower than I would have expected. But I think it is important people understand the direction; we have got good news in terms of temporary falls in some of the goods we buy every single day but we have that ability to bring inflation back to target and it will be an environment, most likely, that interest rates start to increase and move up over the course of the next couple of years.

RP: Governor, many thanks.

MC: Thank you Robert.

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