

## **ANNEX: SUMMARY OF DATA PRESENTED BY BANK STAFF**

A1 This Annex summarises the analysis presented by Bank staff to the Monetary Policy Committee on 3 February 2005, in advance of its meeting on 9-10 February. At the start of the Committee meeting itself, members were made aware of the information that had subsequently become available, and that information is included in this Annex.

### **I Financial markets**

A2 Since the Committee's previous meeting, short-term sterling interest rates had risen, but euro and US dollar rates had been broadly unchanged. Interest rates implied by December 2005 short-sterling futures contracts had risen by 24 basis points. The most significant rises in sterling short-term interest rates had followed the UK CPI release for December and the stronger-than-expected UK Q4 GDP preliminary release. The sterling forward curve, implied by overnight interest rate swaps, had been almost completely flat, consistent with market participants expecting official rates to remain unchanged in the near term. The Reuters survey of economists had indicated that none of the 50 economists surveyed had expected a change in rates at the Committee's February meeting.

A3 Over the month, long-term sterling nominal forward interest rates implied by government bonds had fallen by an average of 17 basis points at horizons from three years out to twenty-five years. Long-term nominal forward interest rates had also fallen in the United States and the euro area by, on average, 52 and 43 basis points respectively, over the same period. Falls in long-term sterling nominal interest rates reflected falls in both real forward rates and inflation forward rates. The Consensus Economics survey had suggested that CPI inflation was expected to average 1.7% in 2005, and the HM Treasury survey of forecasters had suggested an average annual rate of CPI inflation of 1.8% in 2005 Q4, broadly unchanged since the Committee's previous meeting.

A4 The sterling effective exchange rate (ERI) had risen by 1.3%, to 103.1, since the Committee's previous meeting. Sterling had appreciated by 1.9% against the euro and by 1.3% against the yen, but had depreciated by 1.9% against the dollar. Market commentary had related some of the sterling appreciation to stronger-than-expected UK data releases, such as the CPI release for December and indicators of activity in the UK housing market. The US dollar ERI had appreciated by 3.6%, following stronger-than-expected US data releases. Over the month, uncertainty surrounding

exchange rates, as inferred from options prices, had fallen for dollar-sterling, dollar-euro and sterling-euro bilateral exchange rates.

A5 The major equity indices had risen over the month, with the FTSE All-Share, S&P 500, Eurostoxx and Topix having risen by 4.5%, 0.4%, 4.5% and 0.7% respectively, in local currency terms. Market views on uncertainty surrounding movements in the main equity indices, as inferred from three-month implied volatility of options prices, had fallen over the period. Sterling and euro-denominated investment-grade corporate bond spreads had narrowed slightly, while dollar-denominated investment-grade spreads had been unchanged.

## **II The international environment**

A6 According to the advance estimate, US GDP had risen by 0.8% in 2004 Q4, following a rise of 1.0% in 2004 Q3. Compared with a year earlier, GDP had risen by 3.7%. US final domestic demand had increased by 1.1% in 2004 Q4. Within this, private consumption had expanded by 1.1% on the quarter and private fixed investment had risen by 1.6%, reflecting a rise of 2.5% in non-residential investment and a rise of 0.1% in residential investment. Government spending had increased by 0.2% in Q4. Net trade had made a -0.4 percentage point contribution and stock building had contributed 0.1 percentage points to quarterly GDP growth in 2004 Q4.

A7 US non-farm payrolls had increased by 146,000 in January, following a 133,000 increase in December, a downward revision from the estimate of 157,000 in the previous release. The unemployment rate had fallen to 5.2% in January, from 5.4% in December.

A8 US industrial production had risen by 0.8% in December, following an increase of 0.2% in November. Retail sales had increased by 1.2% in December, following a 0.1% rise in November. Consumption had grown by 0.9% in December compared with a month earlier, after a 0.2% rise in November (upwardly revised). Saving as a percentage of nominal personal disposable income had increased to 3.4% in December, from 0.3% in November; this rise reflected a special dividend payment by the Microsoft Corporation. The University of Michigan consumer confidence measure had fallen to 95.5 in January, from 97.1 in December. The Conference Board consumer confidence measure had increased to 103.4 in January, from 102.7 in December (revised up from 102.3). The Institute for Supply Management (ISM) manufacturing index had fallen to 56.4 in January, from

57.3 in December. The ISM non-manufacturing business activity index had fallen to 59.2 in January, from 63.9 in December.

A9 US producer prices for finished goods had increased by 4.1% in the year to December. The US headline consumer price index (CPI) had risen by 3.3% in the year to December, compared with a 3.5% rise in November. Annual core CPI, which excludes energy and food prices, had increased by 2.2% in December, unchanged from the annual rate in November. The price index of core personal consumption expenditures had increased by 1.6% in the year to 2004 Q4, up from 1.5% in 2004 Q3. Employment costs had risen by 0.7% in 2004 Q4 compared with a quarter earlier.

A10 In the euro area, the estimate of quarterly GDP growth in 2004 Q3 had been unrevised at 0.3% in the second release, although there were offsetting changes to estimated components and revisions to past data. Export growth had been 1.5% compared with the previous quarter, revised up from 1.2% previously. Import growth had also been revised up, to 3.5%, from 3.2% in the first release. Net trade had contributed -0.7 percentage points to quarterly GDP growth, unrevised from the first release. The contribution from stock building had also been unrevised. Private consumption growth had been revised downwards to 0.1%, from 0.2% in the first release. Estimates of investment growth had been revised up slightly in most quarters from 2003 Q2.

A11 The euro-area purchasing managers' index (PMI) for manufacturing had risen to 51.9 in January, from 51.4 in December. The euro-area PMI index for services had risen to 53.4 in January, from 52.7 in December. Industrial production in the euro area had fallen by 0.3% in November compared with a month earlier, after falling by 0.6% in October. The European Commission measures of industrial and consumer confidence had been -5 and -13 respectively in January. Industrial confidence had fallen from -4 in December, with a reported weakening in recent production and order books; consumer confidence had been unchanged. The German IFO index had risen to 96.4 in January, from 96.2 in December.

A12 According to Eurostat, euro-area retail sales had increased by 0.2% in December, following a decline of 0.1% in November (downwardly revised). Broad money in the euro area had increased by 6.4% in the year to December.

A13 Annual euro-area inflation, as measured by the harmonised index of consumer prices (HICP), had increased to 2.4% in December, from 2.2% in November. But the Eurostat flash estimate for

annual euro-area inflation in January had fallen to 2.1%. Annual core HICP inflation, which excludes energy, food, alcohol and tobacco prices, had been 1.9% in December. Annual producer price inflation (excluding construction) had fallen to 3.6% in December, from 3.7% in November.

A14 In Japan, industrial production had fallen by 1.2% on the month in December, following a rise of 1.7% in November. Export volumes had risen by 2.8% in December compared with a year earlier, after increasing by 5.4% in the year to November. Import volume growth had slowed to 2.7% in December compared with a year earlier, from 14.6% in November.

A15 GDP in China was estimated to have grown by 9.5% in the year to 2004 Q4, following a rise of 9.1% in the year to 2004 Q3. Annual consumer price inflation had fallen to 2.4% in December, from 2.8% in November.

A16 Since the Committee's previous meeting, the spot price of Brent crude oil had fallen by 0.2% per barrel, to US \$43.11, but had risen by 1.7% in sterling terms. *The Economist* dollar non-oil commodity price index had risen by 0.9%. The index for metals had risen by 1.7%. The index for food had fallen by 0.1%, while the index for non-food agricultural products had risen by 4.4%.

### **III Money and credit**

A17 The twelve-month growth rate of notes and coin, adjusted for special factors, had risen to 5.8% in January, from 5.5% in December. The three-month annualised growth rate had risen to 5.7% in January, up from 3.9% in December. The annual growth rate of aggregate M4 deposits had decreased to 8.6% in December, from 8.8% in November. The annual growth rate of M4 lending (excluding the effects of securitisations) had edged upwards by 0.1 percentage points, to 12.5% in December. Excluding other financial corporations, annual M4 deposit growth had fallen to 8.0% in December, from 8.5% in November, while annual M4 lending growth (excluding the effects of securitisations) had risen to 11.2%, from 11.0% in November.

A18 The annual growth rate of households' M4 had decreased by 0.3 percentage points, to 8.2% in December. The annual growth rate of total net lending to individuals (a wider measure than M4 lending that includes lending by a broader set of institutions than just banks and building societies) had fallen by 0.3 percentage points, to 12.8% in December. The annual growth rate of secured lending to individuals had fallen to 13.0% in December, from 13.4% in November, while the annual growth

rate of unsecured lending to individuals had increased to 12.1% in December, from 11.7% in November. Within unsecured lending, the annual growth rate of credit card lending had increased by 0.5 percentage points, to 17.4% in December, while the annual growth rate of other unsecured lending had increased to 9.7% in December, from 9.3% in November.

A19 The average standard variable rate on mortgages quoted for existing customers had been unchanged in January, while the average two-year fixed rate on mortgages had fallen slightly. The effective mortgage rate had risen slightly to 5.57% in December. According to the latest data from the Council of Mortgage Lenders, the share of new mortgages (by volume) with fixed rates had risen to 41% in December, from 40% in November. The average quoted interest rate on postal and telephone deposits, and deposit rates for time and instant access accounts had remained broadly unchanged. The average quoted interest rate on credit card borrowing had increased in January; the effective rate for a personal loan had edged upwards to 8.94% in December.

A20 The annual growth rate of private non-financial corporations' (PNFCs') holdings of M4 deposits had fallen to 7.2% in December, from 8.7% in November. The annual growth rate of M4 lending to PNFCs (excluding the effects of securitisations) had risen to 7.0% in December, from 5.8% in November. The monthly flow of total finance raised in the United Kingdom by PNFCs had averaged £1.9 billion in Q4, down from a monthly average of £3.5 billion in Q3. Within total finance, the flow of bond, equity and commercial paper issuance (denominated in sterling and foreign currencies) had averaged £0.6 billion a month in Q4, an increase from its Q3 monthly average of £0.2 billion.

#### **IV Demand and output**

A21 In the preliminary GDP release, the ONS had estimated that GDP at market prices had grown by 0.7% in 2004 Q4, following growth of 0.5% in Q3. Annual GDP growth at market prices had fallen to 2.8%, from 3.1% in Q3. Whole-economy gross value added was also estimated to have grown by 0.7% on the quarter in Q4.

A22 In the preliminary GDP release, the output of the service sector had been estimated to have grown by 1.0% in 2004 Q4. The output of the production sector had been estimated to have fallen by 0.5% on the quarter, with a fall of 0.2% in manufacturing output. In December's Index of Production release, the estimate of output of the production sector had subsequently been revised up to -0.1% for

2004 Q4. That revision principally reflected an upward revision to manufacturing output growth, to 0.2%.

A23 Retail sales volumes had fallen by 1.0% in December, accompanied by a 1.2% fall in retail sales values. In Q4 as a whole, retail sales volumes had grown by 0.3%, compared with a 1.0% increase in Q3. The *CBI Distributive Trades* retailers' sales balance had fallen to -3 in January, from +33 in December, and the GfK consumer confidence balance had risen by 4 points in January, to +1.

A24 In terms of indicators at the beginning of the housing market activity chain, the Royal Institution of Chartered Surveyors (RICS) survey balance of new buyer enquiries had risen to -3 in January, from -6 in December. The RICS sales-to-stocks ratio had been unchanged in January, following nine consecutive monthly falls. The monthly balance of net housing reservations reported by the House Builders Federation had decreased to -38.9 in December, from -34.4 in November. The ratio of sales prices to asking prices reported by Hometrack had fallen to 92.7% in January. And further along the chain, mortgage loan approvals had increased to 83,000 in December, from 77,000 in November, the first increase since May 2004.

A25 The Nationwide and Halifax house prices indices had risen by 0.4% and 0.8% respectively in January. The three-month-on-three-month inflation rates of the two indices had risen slightly, to 1.1% and 0.5% respectively in January. Regional data from both the Nationwide and Halifax had suggested that quarterly house price inflation fell across all major regions of the United Kingdom in 2004 Q4.

A26 Some recent surveys had pointed to a modest rise in business confidence in Q4. In the services sector, the British Chambers of Commerce (BCC) survey's balance for confidence regarding profitability had rebounded to +41 in Q4, from +35 in Q3. And the Chartered Institute of Purchasing and Supply (CIPS) *Report on Services* business expectations balance had risen to 77.1 in January, from 73.7 in December. In the manufacturing sector, the BCC survey's balance for confidence regarding profitability had risen to +35 in Q4, from +24 in Q3. However, the *CBI Quarterly Industrial Trends Survey's* business optimism balance in the manufacturing sector had fallen to -22 in Q4, from -10 in Q3.

A27 Surveys of investment intentions had eased back slightly in Q4. The BCC services investment intentions balance had fallen to +15 in Q4, from +17 in Q3. In the manufacturing sector, there had been a decrease in the BCC manufacturing investment intentions balance to +16 in Q4, from +18 in Q3; and a fall in the CBI manufacturing investment intentions balance to -19, from -17, over the same period.

A28 Looking ahead to Q1, the CIPS *Report on Services* business activity index had increased to 55.9 in January, from 54.9 in December. The new orders index had increased to 56.6 in January, from 55.4 in December. The BCC services domestic orders balance had fallen to +21 in Q4, from +23 in Q3.

A29 In the manufacturing sector, the CIPS manufacturing survey output index had fallen to 53.5 in January. The new orders balance had fallen to 51.9, from 54.8 in December. The BCC manufacturing domestic orders balance had been unchanged at +15 in Q4. The CBI total new orders balance had fallen to -4 in Q4, from +4 in Q3.

## **V The labour market, costs and prices**

A30 According to the Labour Force Survey (LFS), employment had increased by 99,000 in the three months to November compared with the three months to August. The 16+ employment rate had risen by 0.1 percentage points in the three months to November, to 60.1%, and had increased by 0.2 percentage points compared with the same period a year earlier. Average weekly hours worked had risen by 0.9% in the three months to November compared with the previous non-overlapping quarter, to 32.1.

A31 Survey balances on employment had generally fallen slightly. The CIPS surveys for January had shown a fall in the employment balances for manufacturing and services, but the construction employment balance had risen. The balances for services and construction had remained above the 'no change' level of 50.

A32 LFS unemployment had increased by 13,000 in the three months to November, but had been 64,000 lower than a year earlier. The LFS unemployment rate had been flat at 4.7% in the three months to November, but had decreased by 0.2 percentage points compared with the same period a

year earlier. The claimant count unemployment rate had remained unchanged, at 2.7% in December. The level of inactivity among those aged 16+ had decreased by 39,000 in the three months to November. The 16+ inactivity rate had fallen to 37.0% in the three months to November compared with the previous non-overlapping quarter, but had been unchanged compared with the same period a year earlier.

A33 According to settlements information available to the Bank, the mean whole-economy average earnings index (AEI-weighted) settlement had been 3.2% in the year to December, unchanged from November. The twelve-month mean settlements in the private sector (AEI-weighted) and public sector (sample-weighted) had been 3.2% and 2.9% respectively.

A34 Annual whole-economy earnings growth had been 4.2% in the three months to November, up 0.1 percentage points on the figure for the three months to October. Private sector pay growth had increased by 0.1 percentage points, to 4.1%. Within this, pay growth in manufacturing had fallen by 0.2 percentage points, to 3.1%, and pay growth in private sector services had increased by 0.1 percentage points, to 4.1%. Public sector pay growth had risen by 0.1 percentage points, to 4.7%, in the three months to November. Whole-economy earnings growth in the year to November had increased by 0.3 percentage points, to 4.5%. Annual earnings growth excluding bonuses had been flat at 4.4% in the three months to November compared with the three months to October.

A35 The Bank's regional agents had conducted an informal survey of around 300 firms with 800,000 employees on the prospects for earnings growth in 2005. Weighted by employment numbers, the balance expecting a higher across-the-board settlement had been +12%. A higher balance, +42%, had expected stronger total pay growth per employee this year compared with last year, and a balance of +50% had expected the growth of total labour costs (a wider definition including non-pay elements such as pension costs) to be higher than in 2004. The inflation outlook had been cited as the most significant factor behind the upward pressure on total labour costs.

A36 UK manufacturing input prices had fallen by 2.3% in December. The annual inflation rate had fallen to 3.4% in December, from 6.0% in November. The fall in the input price index between November and December had mainly reflected a fall in the price of crude oil. The *CIPS Report on Manufacturing* had pointed to a rise in input price inflation in January; the input price balance had risen to 72.5, from 71.7 in December.

A37 Manufacturing output prices excluding duties (PPIY) had fallen by 0.4% in December. The annual PPIY inflation rate had fallen to 3.0% in December, from 3.7% in November. Survey data were mixed: the expected output price balance from the *CBI Quarterly Industrial Trends Survey* had risen to +19 in January, but the output price balance from the *CIPS Report on Manufacturing* had fallen to 56.1 in January, from 56.5 in December.

A38 Annual CPI inflation had risen to 1.6% in December, from 1.5% in November. Within this, annual goods price inflation had risen to -0.1% in December, from -0.4% in November. Annual services price inflation had risen by 0.2 percentage points, to 3.7%, in December. Annual RPIX inflation had risen to 2.5% in December, from 2.2% in November. Annual RPI inflation had increased to 3.5%, from 3.4% in November.

## **VI Reports by the Bank's Agents**

A39 The Bank's regional Agents reported that retail sales volumes had picked up a little in January from the lull the previous month. Taking the two months together, it appeared that the growth of sales had moderated. And many retailers had been nervous concerning the outlook for consumer demand, on account of the effect of households' higher mortgage commitments, falling house prices, higher council tax bills and the cost of utilities. Even so, consumption growth had been expected to slow only gradually, partly because of the underlying strength of spending on some consumer services such as hotels, restaurants and leisure activities.

A40 The annual rate of house price inflation had continued to ease, though there had been some signs that activity and prices were close to a turning point. Turning to investment, contacts reported that investment in information technology had been strong. And investment in commercial property (particularly in the retail sector) had been recovering. Manufacturing investment had not been as strong as it had been at similar points in previous economic cycles, and had been directed at raising productivity rather than expanding capacity. Contacts' investment intentions had been reasonably positive, but had not suggested that capital spending would accelerate this year.