

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 June 2005, in advance of its meeting on 8-9 June. 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 interest rates had fallen in the United Kingdom, the United States and the euro area. Interest rates implied by December 2005 futures contracts had fallen by 29 basis points in the United Kingdom, by 17 basis points in the United States and by 18 basis points in the euro area. In the United Kingdom, short-term interest rates had fallen markedly following the publication of the *Inflation Report* on 11 May. Market prices had been suggestive of a reduction in official rates during 2005 H2, although many market contacts had continued to expect rates to remain unchanged during 2005. The Reuters survey of economists had indicated that all the respondents had expected rates to remain unchanged at the June MPC meeting. But the mean of economists' expectations for policy rates at the end of 2005 had fallen by 12 basis points to 4.70%; the majority of economists expected the next move in policy rates to be down. UK short-term interest rate uncertainty, implied by options prices, had remained broadly unchanged at shorter horizons, but had risen at longer horizons.

A3 Since the Committee's previous meeting, medium to long-term nominal forward interest rates had fallen internationally. In the United Kingdom and the euro area, these nominal changes had largely been accounted for by lower real rates. However, the falls in nominal forward rates in the United States had been split roughly equally between changes in real rates and implied inflation. The falls over the month had pushed international long-term nominal and real rates back to, or below, the recent lows experienced in 2005 Q1.

A4 The sterling effective exchange rate index (ERI) had fallen slightly by 0.1% to 102.0 since the Committee's previous meeting. Sterling had depreciated by 2.8% against the dollar and by 1.0% against the yen, but had appreciated by 1.2% against the euro. For much of the month, the direction of sterling had been consistent with relative movements in international interest rates. But following the

'no' vote in the French referendum on the European Union Constitutional Treaty on 29 May, the euro had depreciated sharply against other major currencies. Over the month, the euro ERI had fallen by 2.0% and the US dollar ERI had appreciated by 2.3%. Exchange rate uncertainty implied by options prices had remained low.

A5 The FTSE All-Share, S&P 500 and EuroStoxx indices had risen by 2.4%, 2.0% and 3.9% respectively in local currency terms since the Committee's previous meeting. The Topix had fallen by 0.2% in local currency terms. Market participants' near-term uncertainty surrounding equity indices, as inferred from three-month implied volatility of option prices, had fallen. Corporate credit spreads had widened during the first half of the month. This had partly reflected some idiosyncratic factors in the US auto sector. But this widening subsequently reversed; over the month, sterling, dollar and euro-denominated investment-grade corporate bond spreads had narrowed. Profit warnings in the United Kingdom had remained higher than at the same time last year.

II The international environment

A6 According to the preliminary estimate, US GDP had risen by 0.9% in 2005 Q1, revised up from the advance estimate of 0.8%. Within this total, the estimate for private fixed investment growth had been revised up slightly to 1.3%, from 1.2%; and government spending growth had been revised down slightly, to zero from 0.1% in the advance release. The contribution to quarterly GDP growth in Q1 from stockbuilding was revised down to 0.2 percentage points while the net trade contribution had been revised up to -0.2 percentage points from -0.4 percentage points. Non-farm business sector unit labour costs had risen by an upwardly revised 0.8% in Q1, following an upwardly revised rise of 1.9% in Q4.

A7 US industrial production had fallen by 0.2% in April, following a rise of 0.1% in March. New orders for non-defence capital goods had risen by 4.1% in April. The Institute for Supply Management (ISM) manufacturing index had fallen to 51.4 in May, from 53.3 in April, while the ISM non-manufacturing index had fallen to 58.5 in May, from 61.7 in April.

A8 Real US consumption had increased by 0.2% in April, following a rise of 0.4% in March. Real personal disposable income had risen by 0.1% in April, having been flat in March. The saving rate had fallen to 0.4% of disposable income in April, from 0.5% in March. US non-farm payrolls had

increased by 78,000 in May, following an unrevised rise of 274,000 in April. The Conference Board measure of consumer confidence had increased to 102.2 in May, from 97.5 in April, but the University of Michigan headline index of consumer confidence had fallen to 86.9 in May, from 87.7 in April.

A9 US producer prices for finished goods had increased by 4.8% in the year to April. Annual headline consumer price inflation had been 3.5% in April, compared with 3.1% in March. Annual 'core' consumer price inflation (which excludes food and energy prices) had been 2.2% in April, down from 2.3% in March. The 'core' measure of the personal consumption expenditures deflator had increased by 1.6% in Q1 compared with a year earlier.

A10 According to the first release, euro-area GDP had risen by 0.5% in Q1, following an increase of 0.2% in Q4. Within this total, private consumption had grown by 0.3%; investment had fallen by 0.7%; and government consumption had fallen by 0.2%. Net trade had contributed +0.5 percentage points to GDP growth in Q1, while the contribution from stockbuilding was zero.

A11 German GDP had increased by 1.0% in Q1, following a contraction of 0.1% in Q4. Within this total, private consumption had fallen by 0.2% in Q1, following a rise of 0.3% in Q4. Investment had fallen by 1.7% in Q1, having increased by 0.3% in Q4. Government consumption had fallen by 0.2%, having risen by 0.1% in Q4. Net trade had added 1.6 percentage points to GDP growth in Q1, while inventories had subtracted 0.1 percentage points. French GDP had increased by 0.2% in Q1, following growth of 0.7% in Q4. Private consumption had risen by 0.7%; total investment had increased by 1.3%; and government consumption had contracted by 0.5%. Net trade had subtracted 0.2 percentage points from GDP growth, while inventories had subtracted 0.1 percentage points. In Q1, Dutch GDP had fallen by 0.1%; Spanish GDP had increased by 0.9%; Greek GDP had increased by 2.5%; Italy's preliminary estimate of GDP had suggested a contraction of 0.5%; and, according to the flash estimate, Belgian GDP had been unchanged.

A12 According to Eurostat, euro-area industrial production had fallen by 0.2% in March, having fallen by 0.6% in February. The European Commission measure of euro-area industrial confidence had fallen to -11 in May, from -9 in April. The consumer confidence indicator had decreased to -15 in May, from -13 in April. The Purchasing Managers' Index for the manufacturing sector in the euro area had fallen to 48.7 in May, from 49.2 in April, and the index for the service sector had increased to 53.5 in May, from 52.8 in April. The German IFO index had fallen to 92.9 in May, from 93.3 in April.

A13 The euro-area unemployment rate had been 8.9% in April, unchanged from March. According to Eurostat, the volume of retail sales in the euro area had fallen by 1.2% in April, following an increase of 0.1% in March.

A14 According to the Eurostat flash estimate, annual inflation in the euro area, as measured by the harmonised index of consumer prices (HICP), had fallen to 2.0% May, from 2.1% in April. Annual ‘core’ inflation (excluding energy, food, alcohol and tobacco prices) had been 1.4% in April, down from 1.6% in March. Annual producer price inflation (excluding construction) had been unchanged at 4.2% in April.

A15 According to the first estimate, Japanese real GDP had increased by 1.3% in Q1, compared with a downwardly revised estimate of zero growth in Q4. Within the total for Q1, private consumption had increased by 1.2%, business investment had increased by 2.0% and government consumption had risen by 0.8%. Net trade had contributed –0.1 percentage points to quarterly GDP growth.

A16 Industrial production in Japan had risen by 2.2% in April, following a fall of 0.2% in March. The workers’ household survey had reported a fall of 3.1% in real spending in the year to April, compared with a rise of 1.7% in the year to March. Annual growth in export volumes had been –1.4% in April, down from 1.1% in March. Annual growth in import volumes had slowed to –0.6% in April, from 1.6% in March. The all-activity index had fallen by 0.5% in March, having fallen by 1.2% in February.

A17 Since the Committee’s previous meeting, the spot price of Brent crude oil had risen by \$1.99 to \$51.88 per barrel. *The Economist* dollar non-oil commodity price index had increased by 1.0% over the same period.

III Money and credit

A18 The twelve-month growth rate of notes and coin, adjusted for special factors, had fallen to 4.3% in May, from 4.8% in April. The three-month annualised growth rate had fallen to 2.1% in May, from 3.2% in April. The annual growth rate of aggregate M4 had risen to 10.5% in April, from 10.4% in March. The annual growth rate of M4 lending (excluding the effects of securitisations) had fallen to 12.0% in April, from 12.6% in March. Excluding other financial corporations, annual M4 growth had

fallen to 8.5% in April, from 8.7% in March, while annual M4 lending growth (excluding the effects of securitisations) had risen to 11.6%, from 11.5% in March.

A19 The annual growth rate of households' M4 had edged upwards by 0.1 percentage point, to 8.6% in April. 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 11.7% in April.

A20 The annual growth rate of secured lending to individuals had decreased to 11.3% in April, from 11.7% in March. At 6.61% in May, the average standard variable rate on mortgages quoted for existing customers had been unchanged since April, while the average two-year fixed rate on mortgages had fallen by 19 basis points, to 5.01% in May. The effective mortgage rate had fallen slightly, to 5.51% in April. According to the latest data from the Council of Mortgage Lenders, the share of new mortgages (by volume) with fixed rates had risen to 42% in April, from 40% in March. The number of loan approvals for house purchase had increased to 95,000 in April, from 92,000 in March. The monthly balance of net housing reservations reported by the House Builders Federation had fallen slightly to -50 in April, from -49 in March. The three-month on three-month rate of inflation of the Nationwide house price index had eased to 0.5% in May, from 0.6% in April. The three-month on three-month rate of inflation of the Halifax index had also fallen, to 0.1% from 0.7%.

A21 The annual growth rate of unsecured lending to individuals had fallen to 13.2% in April, from 13.6% in March. Within unsecured lending, the annual growth rate of credit card lending had decreased by 1.3 percentage points, to 19.6% in April, while the three-month annualised growth rate had fallen to 13.8%, from 20.6% in March. The annual growth rate of other unsecured lending had edged downwards by 0.1 percentage point to 10.6% in April. The effective interest rate on all credit card balances had fallen slightly, to 11.01% in April, from 11.05% in March. The effective rate for a personal loan had also eased slightly, to 8.90% in April, from 8.95% in March.

A22 The annual growth rate of private non-financial corporations' (PNFCs') holdings of M4 had fallen to 8.4% in April, from 9.7% in March. The annual growth rate of M4 lending to PNFCs (excluding the effects of securitisations) had risen to 12.3% in April, from 10.8% in March. Total finance raised (excluding the effects of securitisations) in the United Kingdom by PNFCs had been £2.5 billion in April. This compared with a monthly average of £4.0 billion in 2005 Q1. Within total

finance raised, net issuance of bonds, equity and commercial paper (denominated in sterling and foreign currencies) had been –£0.9 billion in April, compared with a monthly average of –£0.6 billion in Q1.

IV Demand and output

A23 Estimated quarterly growth of GDP at market prices had been revised down in the 2005 Q1 Output, Income and Expenditure release to 0.5%, from 0.6% published in the Preliminary release.

A24 On the output side of the accounts, service sector growth had been estimated at 0.8% in 2005 Q1, unrevised from the previous release. Production sector output had been estimated to have fallen by 0.7% in 2005 Q1, compared with a fall of 0.1% in the previous release. Within the production sector, manufacturing output had fallen by 0.7%, revised down from +0.1% in the previous release. In April's Index of Production release, manufacturing output growth had subsequently been revised down again, to –0.8% in Q1. Construction sector output had been estimated to have grown by 0.6% in 2005 Q1.

A25 On the expenditure side of the accounts, real household consumption (including that of non-profit institutions serving households) was estimated to have risen by 0.3% in 2005 Q1. Real government consumption had risen by 0.7% and whole-economy investment had fallen by 0.4%. Within whole-economy investment, business investment had fallen by 0.1%.

A26 Total exports had fallen by 1.0% in 2005 Q1. Within this, goods exports had decreased by 1.5% and services exports had grown by 0.2%. Total imports had decreased by 1.9%, within which goods imports had decreased by 2.7% while services imports had grown by 0.9%. Overall, the contribution of net trade to quarterly GDP growth in 2005 Q1 had been +0.4 percentage points. Adjusting for the effects of missing trader intra-community (MTIC) VAT fraud, total export and import growth had been estimated at –0.9% and –1.9% respectively. In the ONS trade release for April, goods export growth had subsequently been revised down to –1.1% in Q1, while goods import growth had been revised down to –2.1%.

A27 Turning to indicators of expenditure in 2005 Q2, retail sales volumes had risen by 0.5% in April, following a fall of 0.3% in March. The three-month on three-month growth rate of retail sales had been 0.2% in April, the same as in March. The GfK consumer confidence balance had fallen by 1

point in May, to –1. In the *CBI Distributive Trades Survey*, the balance of retailers reporting positive annual growth in sales volumes had risen to –7 in May, from –14 in April. According to the *BRC-KPMG Retail Sales Monitor*, retail sales values had grown by 1.4% in the twelve months to May. According to the Society of Motor Manufacturers and Traders, new private car registrations (seasonally adjusted) had been 4.5% higher in the three months to May compared with the previous three months.

A28 The Index of Production release had indicated that industrial production had grown by 0.8% in April. Within that, manufacturing output had risen by 0.9% and energy output had increased by 0.8% on the month. The Chartered Institute of Purchasing and Supply (CIPS) *Report on Manufacturing* output index had fallen to 47.9 in May, from 50.7 in April. The new orders index had also fallen in May, to 46.3 from 48.7. The *CBI Monthly Trends Enquiry* total orders balance had risen to –22 in May, from –24 in April, while the expected output balance had fallen, to –1 in May, from +5 in April. The CIPS *Report on Services* business activity and new orders indices had both fallen in May, to 55.1 and 55.4 respectively.

A29 The Bank's regional Agents had conducted a special survey of their contacts in the business and financial services sector. According to ONS data, output in that sector had been firm around the turn of the year, consistent with responses to the Agents' survey. Most of the 139 contacts that replied to the survey had reported increasing demand, and the balance of respondents had expected demand to continue to increase over the following six months, although at a slightly weaker pace than the previous six months. Growth had been particularly strong in the business services sector, while financial companies had reported more modest demand growth, especially from households. Demand growth from the government sector had been robust, but that was a relatively small source of demand for business and financial services.

V The labour market, costs and prices

A30 According to the Labour Force Survey (LFS), employment had increased by 87,000 in the three months to March compared with the three months to December. The 16+ employment rate had risen by 0.1 percentage points in 2005 Q1 to 60.2%, but was unchanged relative to the same period a year earlier. Average weekly hours worked had fallen by 0.1% in 2005 Q1 compared to 2004 Q4, to 32.2.

A31 The overall CIPS employment survey for May had fallen to 50.8. Within this, the services and construction balances had both fallen, although the balance for manufacturing had risen slightly.

A32 LFS unemployment had fallen by 15,000 in 2005 Q1, and had been 23,000 lower than a year earlier. The LFS unemployment rate had been 4.7% in 2005 Q1, 0.1 percentage points lower than 2004 Q4. The claimant count unemployment rate had been 2.7% in April, unchanged on the month. The level of 16+ inactivity had increased by 1,000 in 2005 Q1. The 16+ inactivity rate had been 36.9% in 2005 Q1, 0.1 percentage points lower than 2004 Q4, but 0.1 percentage points higher than the same period a year earlier.

A33 According to settlements information available to the Bank, the mean whole-economy twelve-month average earnings index (AEI-weighted) settlement had been 3.5% in the year to April, 0.2 percentage points higher than in the year to March. The twelve-month mean settlement in the private sector (AEI-weighted) had been 3.7%.

A34 Annual growth in whole-economy earnings had been 4.6% in the three months to March, down 0.1 percentage points compared with the three months to February. Private sector pay growth had also fallen by 0.1 percentage points, to 4.6%, within which manufacturing had fallen by 0.1 percentage points, to 3.4%, and private sector services had been unchanged, at 5.0%. Public sector pay growth was 0.1 percentage points lower than in the three months to February, at 4.5%. Whole-economy annual earnings growth, excluding bonuses, had fallen by 0.2 percentage points to 4.1% in the three months to March, compared with the three months to February.

A35 Manufacturing input prices had risen by 0.3% in April. The annual inflation rate had fallen to 10.4% in April, from 11.1% in March. The CIPS *Report on Manufacturing* input price balance had fallen to 52.2 in May, from 60.2 in April.

A36 Manufacturing output prices excluding duties (PPIY) had risen by 0.4% in April. Annual inflation had risen to 3.4% in April, from 3.2% in March. The CIPS manufacturing output price balance had fallen to 48.7 in May, from 51.6 in April. Looking ahead, the balance on expected output prices from the *CBI Monthly Trends Enquiry* had fallen to -3 in May, from +5 in April.

A37 The ONS's experimental corporate services price index (CSPI) had indicated that annual corporate services price inflation (not seasonally adjusted) had risen to 3.2% in Q1, from 2.4% in Q4. The CIPS *Report on Services* prices charged index had fallen to 51.9 in May, from 52.5 in April.

A38 Annual CPI inflation had been unchanged at 1.9% in April. Within this, annual goods price inflation had risen by 0.1 percentage points to 0.2%, while annual services price inflation was unchanged at 4.0%. Annual RPIX inflation had fallen to 2.3% in April, from 2.4% in March. Annual RPI inflation had been unchanged in April, at 3.2%.

VI Reports by the Bank's Agents

A39 The Bank's regional Agents reported that the value of retail sales in May had been broadly flat compared with the previous month. Retailers had reported that sales growth may have stabilised, following previous declines. And the housing market had steadied. By contrast, car sales had remained weak. The slowdown in consumer spending on durable goods had resulted in a build-up in stocks, particularly with distributors, which had resulted in greater discounting to clear the surplus inventory. The build-up in stocks had been expected to depress future orders, which might weaken imports in the months ahead. In consumer services, demand had held up rather better than for retail sales, though recently there had been signs of slightly slower growth.

A40 In the past two years, reports from contacts suggested that export volumes had grown rather more strongly than indicated by the latest official data. Although exports had continued to increase, growth had been weakening steadily in recent months. Contacts reported that trading conditions had been difficult, particularly in European markets, and that they had struggled to maintain market share.

A41 In the past year or so, contacts' investment intentions had generally been rather stronger than suggested by the official data for business investment. With intentions remaining fairly upbeat, this suggested that business investment would continue to grow in the rest of 2005. Investment intentions had been focused on commercial property (with retailers looking to expand despite the recent slowdown in demand) and information technology systems, the latter aimed at raising productivity.