

ANNEX: SUMMARY OF DATA PRESENTED BY BANK STAFF

A1 This Annex summarises the analysis presented by Bank staff to the Monetary Policy Committee on 30 September 2005, in advance of its meeting on 5-6 October. 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 Oil prices

A2 Since the Committee's previous meeting, the spot price of Brent crude oil had fallen by \$4.19 to \$59.37 per barrel, a decrease of 6.6%, and the sterling spot price of Brent crude oil had fallen by 2.4%, to £33.71 per barrel. Over the same period, the price of the December 2006 Brent crude oil futures contract had fallen by 3.4%, to \$62.30.

A3 World oil consumption growth in 2004 had been the strongest since 1978, according to the *BP Statistical Review of World Energy June 2005*. The IMF's *World Economic Outlook September 2005* had recorded world GDP growth in 2004 as the strongest seen since the 1970s. In its September *Short-Term Energy Outlook (STEO)*, the US Energy Information Administration (EIA) had estimated the spare production capacity of OPEC to lie between 0.9 and 1.4 million barrels per day in August 2005. In every year between 1998 and 2002, annual average spare production capacity had been estimated to be above 3.0 million barrels per day.

A4 In its September *Monthly Oil Market Report (MOMR)*, the International Energy Agency (IEA) had forecast that world oil consumption would increase by 1.6% in 2005 and by 2.1% in 2006, compared with estimated growth of 3.7% in 2004. In its *STEO*, the EIA had forecast 2.1% growth of world oil consumption for both 2005 and 2006, compared with estimated growth of 3.2% in 2004. Forecasts for 2005 had incorporated data for the first half of this year, which had shown a slowdown in oil consumption growth in the United States and China.

A5 In its *MOMR*, the IEA had forecast that non-OPEC oil production would increase by 1.0% in 2005 and by 2.8% in 2006, following estimated growth of 2.2% in 2004. In its *STEO*, the EIA had forecast 0.6% growth of non-OPEC oil production in 2005 and 2.2% in 2006, following

estimated growth of 2.4% in 2004. At this time, information on the timing and size of possible additions to OPEC production capacity had been limited.

A6 In the monthly Consensus survey carried out around 12 September 2005, the mean forecast for the West Texas Intermediate (WTI) crude oil spot price at the end of September 2006 had been \$57.20; the lowest forecast included in that survey had been \$44.70 per barrel, while the highest had been \$75 per barrel. On the same day, the price of the September 2006 WTI crude oil futures contract had been \$65.25 per barrel. In its *STEO*, published on 7 September 2005, the EIA had forecast the average WTI oil price in 2006 to be \$63.46 per barrel.

A7 Looking back over a longer period, the sterling spot price of Brent crude oil had risen by around 100% between 2004 Q1 and 2005 Q3. Between 2004 Q1 and August 2005 the real Brent crude oil price (sterling oil price deflated by RPI) had increased by 96%. Manufacturing input prices in the United Kingdom had risen by 12.7% in the year to August 2005, and had mainly been driven by increases in the prices of oil, gas and electricity. Over the same period, manufacturing output prices excluding duties (PPIY) in the United Kingdom had increased by 3.3%, and increases in the prices of petroleum products had contributed around half of that rise. Annual CPI inflation had been 2.4% in August 2005, 1.1 percentage points higher than a year earlier, and petrol, utilities and transport services inflation had accounted for around 40% of that pickup.

A8 The real ratio of oil consumption to value added in the United Kingdom had generally been trending downward since the 1970s. The value of oil inputs as a share of gross output had been relatively flat since the end of the 1980s, at around 1.6% in 2003. Estimated values for 2004 and 2005 based on profits data had suggested a slight rise in that ratio.

II Financial markets

A9 Since the Committee's September meeting, short-term sterling interest rates implied by March 2006 futures contracts had risen by 6 basis points. In the Reuters poll of economists published on 29 September, the proportion of respondents expecting the Bank's repo rate to remain at 4.50% until at least the end of 2005 had risen to 76% from 64% in the previous survey. Euro interest rates implied by March 2006 futures contracts had risen by 19 basis points. Dollar interest rates implied by similarly dated futures contracts had risen by 39 basis points, and had been above the level prevailing immediately prior to the impact of Hurricane Katrina. Uncertainty surrounding

short-term dollar interest rates, implied by option prices, had declined over the month, after rising sharply following Hurricane Katrina.

A10 Medium to long-term nominal forward rates implied by government bonds had changed relatively little over the month in the United Kingdom and the euro area. Despite a small rise on the month, inflation forward rates in the United Kingdom had still appeared broadly consistent with the inflation target. In the United States, five-year nominal forward rates had risen by around 20 basis points but ten-year rates had changed relatively little. US real forward rates had risen by between 15 and 25 basis points across medium to long-term horizons. The rise at long horizons had been small in the context of the downward trend over recent months.

A11 The sterling effective exchange rate index (ERI) had fallen by 1.5%, to 99.9, since the Committee's previous meeting. This had largely reflected a 4.3% sterling depreciation against the US dollar, although sterling also depreciated by 1.0% against the yen and by 0.3% against the euro. For much of the month, the direction of dollar-sterling exchange rate movements had been consistent with relative changes in UK and US interest rates. Over the month, the US dollar ERI had risen by 2.8%; the dollar had appreciated by 4.1% against the euro and by 3.4% against the yen. Market commentary had related some of the dollar appreciation to the repatriation of overseas earnings by US corporates under the Homeland Investment Act. The euro ERI had fallen by 1.1% over the period. There had been little change in uncertainty surrounding exchange rates, as implied by options prices.

A12 Since the Committee's previous meeting, the FTSE All-Share and Euro Stoxx equity indices had increased by 1.0% and 2.3% respectively in domestic currency terms, while the S&P 500 had fallen by 3.2%. These three indices had all experienced strong increases since the trough in March 2003: the FTSE All-Share, S&P 500 and Euro Stoxx had increased by 71%, 49% and 90% respectively. Since the previous MPC meeting, uncertainty, as inferred from the three-month implied volatility of option prices on the FTSE 100, had increased in the near term but had fallen one year out. Sterling, dollar and euro-denominated investment-grade corporate bond spreads had been relatively unchanged.

III The international environment

A13 According to the final estimate, US GDP had risen by 0.8% in 2005 Q2, the same as in the preliminary estimate. Within this, the growth rates of the expenditure components of GDP were little changed between the preliminary and final releases. The US current account deficit had narrowed to 6.3% of GDP in 2005 Q2, from 6.5% in the previous quarter. Goods export volumes had been flat on the month in July, following growth of 1.2% in June; goods import volumes had fallen by 1.7% in July, following a rise of 2.0% in June.

A14 Real private consumption in the United States had fallen by 1.0% on the month in August, following an increase of 0.9% in July. The saving rate had increased to -0.7% of disposable income in August, from a downwardly revised -1.1% in July. The Conference Board measure of consumer confidence had fallen to 86.6 in September, from 105.5 in August. In the final release, the University of Michigan measure of consumer confidence had fallen to 76.9 in September, from 89.1 in August.

A15 US industrial production had risen by 0.1% in August compared with the previous month, following a rise of 0.1% in July. The Institute for Supply Management (ISM) manufacturing index had increased to 59.4 in September, from 53.6 in August. The ISM non-manufacturing business activity index had fallen to 53.3 in September, from 65.0 in August.

A16 US producer prices for finished goods had increased by 5.1% in the year to August, compared with a 4.6% rise in the year to July. The US headline consumer price index (CPI) had risen by 3.6% in the year to August, compared with 3.2% in July. The core CPI, which excludes food and energy prices, had risen by 2.1% in the year to August, the same rate of increase as in July.

A17 According to the second estimate, French GDP had increased by 0.1% in 2005 Q2, unrevised from the previous release. Italian GDP had increased by 0.7% in 2005 Q2, unchanged from the flash estimate. Fixed investment had grown by 1.5% on the quarter, while consumption had increased by 0.6% and government expenditure had increased by 0.3%. Exports had increased by 5.5% while imports had risen by 4.8% on the quarter.

A18 Euro-area retail sales had increased by 0.9% in August compared with the previous month, following a fall of 0.5% in July. The European Commission's consumer confidence indicator for

the euro area had been -15 in September, unchanged from August. The euro-area seasonally adjusted unemployment rate had increased to 8.6% in August, from a downwardly revised 8.5% in July.

A19 Industrial production (excluding construction) in the euro area had increased by 0.2% on the month in July, following an increase of 0.4% in June. The European Commission's industrial confidence indicator for the euro area had increased to -7 in September, from -8 in August. The euro-area purchasing managers' index (PMI) for manufacturing had risen to 51.7 in September, from 50.4 in August. The euro-area PMI for services had increased to 54.7 in September, from 53.4 in August. The German IFO index had increased to 96.0 in September, from 94.6 in August.

A20 Annual inflation in the euro area, as measured by the harmonised index of consumer prices (HICP), had been 2.2% in August, unchanged from July. Annual core inflation, which excludes energy, food, alcohol and tobacco prices, had been 1.3% in August, unchanged from July. According to the Eurostat flash estimate, euro-area annual HICP inflation had risen to 2.5% in September. Annual producer price inflation (excluding construction) had been 4.0% in August, compared with 4.1% in July.

A21 According to the second estimate, Japanese GDP had grown by 0.8% in 2005 Q2, revised up from growth of 0.3% in the previous release. Within this, private consumption had increased by 0.6%; business investment had increased by 3.6%; and government spending had fallen by 0.3% on the quarter. Net trade had contributed 0.2 percentage points to quarterly GDP growth while stocks had detracted 0.2 percentage points.

A22 Japanese industrial production had risen by 1.2% on the month in August, after falling by 1.2% in July. Annual growth in export volumes had been 2.0% in August, up from -0.8% in July. Annual growth in import volumes had been 9.2% in August, up from -0.6% in July. The all-activity index had fallen by 0.8% on the month in July, following a rise of 1.2% in June. According to the Bank of Japan's Tankan survey for September, the large manufacturers' business conditions diffusion index had increased by 1 point, to 19, and the large non-manufacturers' business conditions diffusion index had been constant at 15.

A23 Since the Committee's previous meeting, *The Economist* dollar non-oil commodity price index had fallen by 1.8%.

IV Money, credit and nominal trends

A24 The twelve-month growth rate of notes and coin, adjusted for special factors, had fallen to 3.8% in September, from 4.9% in August. On a three-month annualised basis, growth had declined to 4.4%, from 5.5%. The annual growth rates of aggregate M4 and M4 lending (excluding the effects of securitisations) had fallen to 10.0% and 11.4% respectively in August, from 11.0% and 12.1% in July. Excluding other financial corporations, annual M4 growth had fallen by 0.6 percentage points, to 8.4%, while annual M4 lending growth (excluding the effects of securitisations) had fallen by 0.2 percentage points, to 11.4%.

A25 The annual growth rate of households' M4 had fallen to 8.3% in August, from 8.7% in July. Annual growth of total net lending to individuals, which includes lending by a broader set of institutions than just banks and building societies (and is therefore a wider measure than M4 lending), had eased by 0.2 percentage points, to 10.5%, in August. The annual growth rate of secured lending to individuals had edged downwards by 0.1 percentage points, to 10.3%, while the annual growth rate of unsecured lending to individuals had fallen to 11.4% in August, from 12.1% in July. Within unsecured lending, the annual growth rate of credit card lending had fallen to 15.4%, from 16.6% in July, while the annual growth rate of other unsecured lending had fallen to 9.8%, from 10.3%.

A26 The average standard variable rate on mortgages quoted for existing customers had fallen by 22 basis points since August to 6.39% in September. Two-year fixed rates on mortgages had fallen by 1 basis point, to 4.59%. Effective mortgage rates had fallen in August by 2 basis points, to 5.52%. According to the latest Council of Mortgage Lenders data, the share of new mortgages (by number) with fixed rates had increased to 54% in August, from 50% in July.

A27 The average quoted interest rate on postal and telephone deposits had fallen in September by 8 basis points, to 3.70%, while the quoted rate on time deposits had fallen by 9 basis points, to 2.98%. The quoted rate on instant access deposits had decreased by 7 basis points, to 1.85%. The quoted rate on credit card lending had been unchanged in September, while the average effective

rate on all credit card lending had risen in August by 6 basis points, to 11.11%, while the corresponding rate for personal loans had fallen by 1 basis point, to 8.81%.

A28 The level of house prices, as measured by the Nationwide index, had been unchanged in Q3, having increased by 1.0% in Q2. The Halifax index of house prices had increased by 1.8% in Q3, following a rise of 0.2% in Q2. The number of loan approvals for house purchase had risen to 107,000 in August, from 99,000 in July. The monthly balance of net housing reservations reported by the House Builders Federation (seasonally adjusted by Bank staff) had risen to +2 in August, from -11 in July. Mortgage equity withdrawal as a proportion of disposable income had risen to 4.2% in Q2, from 3.2% in 2005 Q1.

A29 The annual growth rate of private non-financial corporations' (PNFCs') holdings of M4 had fallen to 8.7%, from 10.5% in July. The annual growth rate of M4 lending to PNFCs (excluding the effects of securitisations) had remained unchanged in August, at 14.8%. UK PNFCs' total finance raised (excluding the effects of securitisations) had been £0.5 billion in August, compared with £3.6 billion in July. Within total finance raised, the net flow of bond, equity and commercial paper issuance (denominated in both sterling and foreign currency) had been -£2.3 billion in August, compared to +£0.2 billion in July.

A30 Household capital gearing (defined as net debt as a percentage of total assets, excluding housing wealth) had been unchanged at 37.8% in 2005 Q2. Household income gearing (defined as total interest payments plus regular mortgage principal repayments as a percentage of annual post-tax household income) had fallen to 11.5% in 2005 Q2, from 11.9% in Q1. The household financial balance (as a percentage of total household resources) had fallen by 0.1 percentage points, to -2.9%, in 2005 Q2. The quarterly growth rate of total household financial assets had risen by 1.0 percentage points in Q2, to 2.7%, while the growth rate of household financial liabilities had risen by 0.5 percentage points, to 2.6%.

A31 PNFCs' capital gearing (defined as net debt divided by the market value of the assets of UK-resident firms) had fallen to 30.5% in Q2, from 30.8% in 2005 Q1. PNFCs' income gearing (defined as total interest payments as a percentage of gross operating surplus) had risen by 0.9 percentage points, to 21.3%. PNFCs' financial surplus (excluding the alignment adjustment) had risen to £9.5 billion in 2005 Q2, from £3.7 billion in Q1. The latest estimate had represented the highest surplus since the start of the series in 1987.

A32 The September HM Treasury survey of forecasters had shown an expected average annual rate of CPI inflation of 2.3% in 2005 Q4, compared to an expectation of 2.0% in the August survey. The September Consensus survey had suggested that CPI inflation would average 2.0% in 2005, up 0.1 percentage points from the August survey. The Bank/NOP survey for August had shown that the median expectation for inflation over the next twelve months had increased to 2.2%, from 2.0% in the May survey.

V Demand and output

A33 The *Quarterly National Accounts* for 2005 Q2 had been published on 28 September. Estimated GDP growth in Q2, at both basic and market prices, had been 0.5%, unrevised from the previous release. However, GDP growth had been revised down in previous quarters, such that the level of GDP at market prices in 2005 Q2 had been 0.3% lower than previously estimated.

A34 On the expenditure side of the accounts, quarterly growth in domestic demand had been estimated at -0.1% in 2005 Q2, unrevised from the previous release. Within domestic demand, final domestic demand growth had been estimated at 0.6%. The contribution of stockbuilding (including the quarterly alignment adjustment) to overall growth had been unrevised at -0.7 percentage points.

A35 The estimated growth of households' consumption (including that of non profit-making institutions serving households) had been revised up by 0.2 percentage points, to 0.4% in 2005 Q2. Business investment growth had been estimated at 1.5% in Q2, revised up from 0.5% in the previous release. Whole-economy investment (including acquisitions less disposals of valuables) growth had been revised down to 1.5% in Q2, from 2.0%. Government consumption growth had been estimated at 0.5%.

A36 Excluding the effects of the identified missing trade intra-community (MTIC) fraud, estimated export growth had been 2.9% in 2005 Q2, revised down from 4.3% in the previous release. Estimated import growth (excluding the effects of MTIC fraud) had been 0.4%, revised down from 1.6% in the previous release. Net trade had made an estimated 0.6 percentage point contribution to GDP growth in 2005 Q2, unrevised from the previous release.

A37 On the output side of the National Accounts, the services sector had grown at an estimated 0.6% in Q2, unrevised from the previous release. However, growth in the previous four quarters had been revised down, such that the level of service sector output in 2005 Q2 was 0.5% lower than previously estimated. Manufacturing output had fallen by an estimated -0.2% in Q2, revised up from -0.3% in the previous release.

A38 On the income side of the accounts, households' real post-tax income had risen by 0.9% in 2005 Q2. Nominal household consumption had grown more slowly than income in Q2, so the household saving ratio had risen to 5.0% in Q2 from 4.5% in Q1.

A39 The gross operating surplus of corporations (excluding the quarterly alignment adjustment) had risen by 2.5% in 2005 Q2. Within that, the gross trading profits of oil companies had grown by an estimated 7.7% in Q2, while the gross trading profits of private non-oil, non-financial corporations had grown by an estimated 1.2% in Q2.

A40 Turning to indicators of output in 2005 Q3, industrial production had fallen by an estimated 0.9% in August, following a fall of 0.4% in July. Manufacturing output had fallen by 0.2% in August, while energy output had fallen by 3.8%. The Chartered Institute of Purchasing and Supply (CIPS) manufacturing survey output index had risen to 52.9 in September, from 52.2 in August. The new orders index had also risen to 54.1 in September from 52.3 in August. The expected output balance in the *CBI Monthly Trends Enquiry* had risen to 6 in September from 3 in August and the new orders balance had also risen to -27 from -29. The *CIPS Report on Services* business activity index was broadly unchanged at 55.0 in September. The incoming new business index had fallen, to 55.3 in September from 56.0 in August.

A41 Turning to indicators of expenditure in 2005 Q3, retail sales volumes were unchanged in August, following a fall of 0.6% in July. In the *CBI Distributive Trades Survey*, the balance of retailers reporting positive annual growth in sales volumes had fallen to -24 in September – the lowest level since the survey began in 1983. The *GfK UK Consumer Confidence Survey* headline balance had fallen in September, to -5. According to the Society of Motor Manufacturers and Traders (SMMT), new private car registrations had been 7.7% weaker in the three months to September than in the same period a year earlier.

VI Supply

A42 The annual growth rate of whole-economy labour productivity, measured using numbers employed, had been 0.5% in 2005 Q2, compared with 0.6% in 2005 Q1. The annual growth rate of whole-economy labour productivity measured using hours worked had been 0.3% in 2005 Q2, compared with 0.4% in 2005 Q1. The annual growth of whole-economy unit wage costs had been 3.1% in 2005 Q2, compared with 3.6% in 2005 Q1.

A43 The population of the United Kingdom had been 59.8 million at mid-year 2004, a rise of 0.5% on a year earlier, compared to 0.4% between mid-2002 and mid-2003. About two thirds of the latest increase in the UK population had been due to net international migration. The mid-year population estimates for 2004 had been incorporated into the Labour Force Survey (LFS) estimates.

A44 According to the LFS, employment had increased by 83,000 in the three months to July compared with the three months to April. In the three months to July, the 16+ employment rate had been unchanged compared with the three months to April, and had increased by 0.2 percentage points compared with the same three-month period a year earlier. Average hours worked had been unchanged in the three months to July compared with the previous non-overlapping quarter, at 32.1.

A45 The CIPS/NTC employment index from the Deloitte/REC *Report on Jobs* had pointed to some growth in employment. The overall CIPS employment index for September had been unchanged at 51.0. Within this, while the construction index had showed an increase, the services index had fallen slightly.

A46 LFS unemployment had risen by 12,000 in the three months to July, and had been 3,000 higher than a year earlier. The LFS unemployment rate had been 4.7% in the three months to July, unchanged compared with the previous non-overlapping quarter, and unchanged compared with the same period a year earlier. The claimant count unemployment rate had been unchanged at 2.8% in August compared with July. The level of 16+ inactivity had increased by 6,000 in the three months to July. The 16+ inactivity rate had fallen to 36.9% in the three months to July, down by 0.1 percentage points compared with the previous non-overlapping quarter and down 0.1 percentage points compared with the same period a year earlier.

A47 The annual growth of private sector capital had been broadly unchanged in 2005 Q2, compared with 2005 Q1.

VII Costs and prices

A48 According to settlements information available to the Bank, the mean whole-economy twelve-month average earnings index (AEI) weighted settlement had been 3.7% in the year to August.

A49 Overall whole-economy annual earnings growth had been 4.2% in the three months to July, 0.1 percentage points higher than in the three months to June. Private sector pay growth had increased by 0.1 percentage points, to 3.9% in the three months to July. Public sector pay growth had decreased by 0.1 percentage points, to 5.5% in the three months to July. Whole-economy annual earnings growth excluding bonuses had decreased by 0.1 percentage points to 3.9% in the three months to July, compared with the three months to June.

A50 Manufacturing input prices had risen by 0.2% in August. That meant that the annual inflation rate had fallen to 12.7% in August, from 14.0% in July. The *CIPS Report on Manufacturing* input price balance had risen to 59.3 in September, from 57.9 in August.

A51 Manufacturing output prices excluding duties (PPIY) had risen by 0.3% in August. Annual inflation had risen to 3.3% in August, from 3.2% in July. The balance on expected output prices from the *CBI Monthly Trends Enquiry* had been unchanged at -8 in September, compared with August.

A52 According to the National Accounts, the annual inflation rate of the GDP deflator at market prices had been 2.7% in 2005 Q2, 0.2 percentage points higher than in Q1. Within this, the annual inflation rate of the household consumption deflator had increased to 2.0% in 2005 Q2, from 1.5% in Q1. The annual inflation rate of the government consumption deflator had risen to 5.5% in 2005 Q2, from 5.2% in Q1. The annual inflation rates of the import and export deflators had been 2.7% and 2.3% respectively in 2005 Q2.

A53 Annual CPI inflation had been 2.4% in August, 0.1 percentage points higher than in July. Within this, annual goods price inflation had risen by 0.1 percentage points to 0.6%, and annual services price inflation had been unchanged, at 4.5%. Annual RPIX inflation had been 0.1 percentage points lower in August than in July, at 2.3%. Annual RPI inflation had also been 0.1 percentage points lower in August, at 2.8%.

A54 The Bank's regional Agents had conducted an informal survey on input prices. The survey had covered around 180 companies with a total turnover of over £36 billion. The vast majority of firms had reported that the cost of their raw materials and inputs had risen over the past year. Both service sector firms and manufacturers had faced similar scales of increase. The survey had suggested that smaller firms were the worst affected by the rising costs. The biggest impact of the rises over the past twelve months had been the reduction of profit margins and output price increases; similar effects had been expected over the next twelve months. The past price rises had been expected also to result in lower investment and employment.

VIII Reports by the Bank's Agents

A55 The Bank's regional Agents had reported that the twelve-month growth in retail sales values may have passed its low point. However, there had been no sign of a strong recovery, and reports from retail contacts had been mixed. The deceleration of spending on consumer services had also come to an end; spending growth on services had remained above retail sales growth. Leisure and tourism spending had been reasonably robust in most regions, with the exception of central London: there, hotels and attractions had still been experiencing weaker bookings in the wake of the July bombings.

A56 Investment intentions had softened again in September. The weakening had been most pronounced in manufacturing, as capacity utilisation had fallen further. Higher energy prices had reduced profit margins and increased uncertainty, which had led firms to be more cautious. Investment intentions in the service sector had also weakened, partly because non-food retailers had become more hesitant. However, there was enough work in progress on major shopping centres to support retail investment over the next year.

A57 Agents' contacts had reported continued growth in manufacturing exports. Demand from the Middle East and other oil-producing countries had been strong. That had primarily reflected investment in capital goods to facilitate expansion of the oil industries in those countries. But there had also been reports of increased demand for a wider range of goods as well. Growth in exports to the United States and Asia had also remained robust, but demand had remained flat in the euro area.