

Report to the Treasury Select Committee

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I am nearing the end of my first year of service on the Monetary Policy Committee and have benefitted throughout from the excellent analysis and insights brought to me by my own research team as well as the wider Bank staff who support the entire committee in its deliberations and decision making. Our collective analysis on many dimensions has been particularly important in a period of extreme uncertainty, with the UK economic situation and near-term future clouded by multiple factors.

In the last twelve months we have confronted the fading after-effects of the inflation spike three years ago, the continuing unreliability of key economic data, the introduction of new trade barriers, the arrival of new price shocks at the start of this year, against a backdrop of weak and weakening economic indicators at home.

This being my first written report, I will set out in some detail my views on economic developments in 2024 and the first half of 2025. I will discuss how that backdrop explains my outlook for the next couple of years and what I see as key issues for monetary policy. I will have to base this on the most likely course of events going forward, which as of now is especially unpredictable, notably at the global level.

In this introduction, let me frame my view within an overarching set of economic themes that seem highly relevant at this time, as we find ourselves at a point in the cycle where underlying inflation is nearing target, the economy is slowing, but short-term factors have triggered a bump in headline inflation. In this kind of situation, a delicate balance is required of policy makers to achieve a "soft landing" – bringing inflation under control after an overshoot without over-braking and triggering a severe recession, where the latter would risk creating the opposite set of problems down the road: inflation below target and economic activity below potential with adverse longer-run consequences.

First, there is the biggest set of uncertainties, the global trade disruptions and attendant downside risks. The new US tariffs look to be settling at an average level around 20%, a level not seen since the Smoot-Hawley tariffs of the 1930s. Much else was going wrong with the world economy and policymaking in the interwar years, and the trade war was more serious back then given that most countries escalated trade barriers. Whereas in the present trade conflict, tariff retaliation is, thus far, more limited. Even so, we should not shrug off this shock and be complacent about it.

While it seems like the astronomic tariffs feared at first may not actually happen, which reduces the risk of a tail event that breaks global supply chains, there will be very high frictions on trade with the US. For exporters, this means a general incentive to divert trade to other countries. And for the UK and the EU (our neighbour and main trading partner), this could mean an influx of additional exports, probably from Asia, in the main goods that can no longer enter the US market given the barriers erected.

In addition, policy uncertainty will linger, weighing on demand everywhere, as firms pause investments until the new global architecture becomes clear and 'deals' become firm. It is less likely to be a sudden crisis, more likely to be a slow-burn package of disinflation and slow growth for a country like ours, and for most of our trading partners.

Second, there is the domestic problem of the weakness of our own economy, which has deteriorated markedly since early 2024. Real GDP growth has been sluggish, with monthly readings often near zero or negative. Vacancies have fallen and unemployment has seen a drift steadily higher, which is clear even in noisy Labour Force Survey data. Bank staff judge there to be growing slack in the economy, whether measured in terms of labour market indicators or estimates of the current output gap. Personally, I strongly believe the current output gap is underplayed in our baseline forecast.

Very little of this slowdown is explicable by the supply side: If it were, underlying inflation would have risen not fallen for the last 18 months. But both wage growth and core inflation measures (e.g., services price inflation excluding administered prices and taxes) have been slowing alongside the real deterioration, the classic signs of a demand retrenchment. High household savings and depressed investment levels corroborate that view.

A large chunk of headline inflation right now is being driven by an unusual combination of increases in regulated and administered prices as well as payroll taxes, alongside food inflation, itself concentrated in a small number of key commodities. These shocks affect the reported headline number but are not manifestations of supply and demand imbalances in the wider economy. Instead, they reflect the wisdom of regulators or, in the case of selected food items, idiosyncratic disturbances in the supply chain of some commodities.

These types of shocks can obscure the underlying disinflationary trend and make it challenging for the MPC to correctly interpret the true state of inflationary pressures, but it is very important that we see through the noise and focus on the deeper signal.

Given the current underlying downward momentum in inflation and activity, braking from monetary policy needs to be withdrawn at an appropriate speed to avoid falling behind the curve, with a hard landing as the result. The moment is particularly dangerous now and in the coming months, I fear. Once recessionary dynamics kick in, history shows that a slow loosening of the labour market can suddenly turn into a rapid deterioration that is much harder to arrest.

I therefore see a constellation of downside risk channels and all of them have seen warning signals rising in intensity over the course of the last 12 months. We do not need all of these risks to materialise to get a bad outcome, even one or two could push us off track. The risk of a downside scenario is now non-trivial, and in addition to missing our inflation target, it would also bring short-term losses in economic activity and a risk of longer-term damage, via hysteresis, pushing the path of productivity down to an even lower level.

State of the economy and voting record

I will briefly summarise the key developments evident in the hard data. Last year, 2024, started with inflation falling from a high level and a healthy rate of real GDP growth, with the economy still operating with excess demand and tight labour markets. An extended period of monetary policy restrictiveness had weighed on inflationary pressures, and both wage and price dynamics were starting to cool. The outlook was not too bad then.

By September 2024, as I joined the committee, monthly CPI inflation had hit 1.7% and the economy was closer to balance, with slack about to appear. By January, backward-looking wage growth was near 6%, but the Bank's agents had survey evidence pointing to wage growth of 3.7% in 2025. After being near the 2% target, a new inflation bump appeared in early 2025, as described above, but this is expected to abate in early 2026, as administered price and tax increases drop out of the annual comparison, and as food prices stabilise. The very latest readings for wage settlements in late 2025 are just starting to come in and they are averaging near 3%, sometimes lower, and advance readings for 2026 are also near 3%.

I interpret these and other data from the recent past as describing an economy suffering more from downward demand shocks than downward supply shocks. The soft data also confirm this trend and suggest it may get even worse, with both household and firm sentiment readings falling over time, for example the latest August Recruitment and Employment Confederation report. Levels of sentiment weaker than current levels are scarcely seen, excluding brief periods right after the 2008 financial crisis or during the pandemic. Again, these worsening sentiment signals were only emerging in mid-2024, and have become stronger over the last 12 months.

Consistent with the evolution of my reading of the data, I began my tenure on the MPC voting with the majority of the committee for a gradual pace of cuts, and then, as I saw a worsening outlook and downside risks emerge more clearly, voting more often in the minority for a faster withdrawal of monetary restriction.

At my first meeting in September 2024, I joined the majority of the committee in voting to hold Bank Rate steady at 5%. The real economy appeared to be growing at a healthy pace (albeit with pockets of weakness) and labour market quantities to be in balance. On the nominal side of things, core inflation was coming down but still well above target-consistent

levels, driven by services prices and buffeted by stronger-than-sustainable wage growth. Therefore, I felt it appropriate to hold Bank Rate steady and wait for the results of new forecasting exercise in November which would also be able to take into account any announcements made at the Autumn budget.

At that meeting in November, I voted to reduce Bank Rate by a quarter point to 4.75%. The greatest inter-meeting news had been the Autumn budget of the new Government which saw the announcement of a mix of both higher-than-expected spending in the near term (and in the past) and higher payroll taxes. The net effect of these announcements were thought to be mildly expansionary and inflationary but that aggregate fiscal multipliers were small. To me, the main risks to this outlook were to the downside, e.g. if the rise in NICs were to have a greater negative impact on the labour market, or if households would save instead of consuming any spending increase in anticipation of future tax rises.

I voted in the minority to reduce Bank Rate by another quarter point to 4.5% in December. As the world outside and staff as well as MPC members inside the Bank were further digesting the fiscal announcements, I judged that their effect would in fact be disinflationary in the medium term. While payroll tax increases would mechanically raise inflation in the near term, their adverse effects on the labour market would, in my view, almost surely weigh on employment. Also, the future stance of fiscal policy turned out to be tighter than initially anticipated, which, alongside a monetary policy stance which would still be firmly restrictive for a while, led me to prefer another cut at this meeting. Trade uncertainty was also rising as a new US administration prepared to take office, buttressing the case for insurance.

At the next meeting in February of this year, the MPC significantly revised its near-term outlook for inflation. Headline inflation in 2025 was going to peak at just under 4% and then fall back to the target. To me there were now indeed risks on both sides: to the upside if the hump were to reinforce more persistent above-target price and wage setting pressures, and to the downside, as economic activity had come in exceptionally weak and sentiment indicators were painting an increasingly gloomy picture. I judged that underlying disinflation was still on track despite the hump and so continued withdrawal of monetary restriction was warranted, and so voted with the majority for a quarter-point cut to 4.5%.

Similar risks and judgements applied when we reconvened in March 2025. The hump in inflation was large and worrying, with salient price rises perhaps leading to some drift in inflation expectations. On the other hand, economic activity was weak and weakening, hiring intentions recessionary, and wage settlements for 2025 were coming in well below backward-looking average weekly earnings growth, a deceleration in line with our Agents' pay survey. Meanwhile, the trade war between the US administration and the world was intensifying which I judged was likely to be contractionary and disinflationary in the UK. But there was a wide range of plausible outcomes for tariffs going forward so, hoping for more clarity by the time of the May forecast, I voted with the majority to hold Bank Rate at 4.5%.

Indeed, clarity came in May but of course not in a way anyone had hoped for with the largest shock to global trade policy in 100 years. Although there still was great uncertainty about the eventual size of tariffs and the size of their effects, directionally, all expert judgement and credible modelling pointed towards disinflationary and contractionary effects for the UK. As such, the monetary policy prescription would be to loosen policy in response. Therefore, I concluded that quickening the pace of cuts was warranted and voted in a minority to reduce Bank Rate by half a percentage point to 4%, a decision supported by my belief that we also had a long way to go to reach a neutral policy rate.

The news between May and June reinforced my view of the continued underlying disinflation in wages and prices and the continued loosening of the labour market. On the trade side, I could detect no real improvement with the deals signed in the interim leaving much to be decided still. It was my view that consumption and investment would remain weak, the labour market would loosen further, and that the stance of monetary policy was still quite restrictive. I worried that monetary policy was over-braking, putting the soft landing at risk. Consistent with this view I again dissented and voted to cut Bank Rate to 4%.

Finally, at the meeting in August 2025, I dissented again on the initial vote and preferred a half-percentage point cut to 3.75%. I thought that the central forecast paths (and the starting point) were becoming more implausible with downside risks to the projected output gap, employment and wage paths, and medium-term inflation firming. For instance, the recent settlements data were pointing to material downside risks to the pay profile.

Macroeconomic Outlook

I have discussed the economic backdrop and recent trends. In that context, my main concern has been to get inflation sustainably back to the 2% target, maintaining monetary policy restrictiveness as long as necessary but no longer, whilst being alert to two dangers.

For me the greater danger is that we get behind the curve, stay too tight in the short-term (or signal a terminal rate too high at the end of the cycle), and thus, by fighting the last war, end up in with the opposite problem: inflation actually undershooting the target and economic activity weak or in recession. This is the downside risk and, in my mind, it has a non-trivial probability that has been rising. Multiple factors are pushing the skew in this direction, principally domestic confidence (weakening sentiment of household and firms, the deteriorating labour market, fiscal rules that imply a marked tightening) and global pressures (economic slowdown in general, and trade diversion from tariffs in particular), as I noted above. I have emphasized these multiple downside factors in speeches, interviews, and in my comments in the MPC minutes.

The main offsetting danger is upside risk to inflation. I am cognisant of this risk, and I should address it here. The key economic argument is the potential dislodging of inflation

expectations, and the risk that this then filters into wage and price setting. I see two counterarguments. Firstly, I see a smaller risk of the latter propagation now as labour market slack opens up, as rising unemployment will create a wage setting environment where bargaining power shifts away from workers and smaller settlements become the norm. Second, at the present moment, household inflation expectations indicators are not out of line with recent historical norms (+0.2 to +0.4 standard deviations relative to the mean). The more reliable financial market expectations are quite steady. Thus, I currently see this upside risk as smaller – and it is concentrated on only one channel. That channel needs to be monitored, and it is. If the readings were to change meaningfully and signal a risk, then I would change my view, but I think that is not where we are right now.

Still, I remain optimistic. We cannot eliminate inflation volatility, but we must handle the shocks as well as we can, and economic research confirms the value of independent central banks who are committed to a policy framework to deliver an inflation target. These institutions can achieve disinflations without the very high costs of recessions that we went through in the 1980s, if expectations are anchored and the economy has sufficient flexibility. If not, sacrifice ratios become large, and hard landings are more likely.

One year ago, a soft landing for the UK economy seemed within reach, as was the case in other advanced economies. Despite being buffeted by new shocks, we are getting closer to that soft landing now, but we are also in a fragile moment, and monetary policy will need to be carefully calibrated in the coming months to keep us on track.

Explaining Monetary Policy

Since joining the MPC, I have given three on-the-record speeches to lay out my views about the state of the economy, monetary policy strategy, and the underlying drivers of interest rates.

In January 2025, I delivered my first speech at Leeds University Business School, focusing on the passthrough of recent shocks to inflation, the ongoing disinflation process, and the degree of monetary restrictiveness. I argued that, despite the large shocks that had hit the economy in recent years, from the pandemic to the energy crisis, the transmission across CPI components was going about as expected given the size of the shocks. Much of the observed persistence in headline inflation was due to slower pass-through components which were starting to come down while anchored inflation expectations and central bank credibility were helping to guide inflation back toward target.

My second speech was delivered at the ECB Forum on Central Banking in Sintra on 2 July 2025. I argued that central bank communication regarding the neutral rate is important and useful for coordinating the actions and plans of economic agents, especially during periods of elevated uncertainty and large shocks. I also argued that without a view of the neutral

rate, it is difficult to gauge the degree of monetary policy restrictiveness. As an empirical matter, I showed that model-based estimates of the nominal neutral rate were a better guide to the medium-term level of interest rates than alternative measures such as the market curve. Finally, I pointed out that, in my view, the nominal neutral rate in the UK is around 2.75% to 3%, and that current rates remain restrictive given growing downside risks to inflation and output.

Little thereafter, on 4 July 2025, at a lecture at the London School of Economics, I reflected on the historical forces driving down interest rates over the past eight hundred years, starting from improvements in property rights and the development of financial markets, passing through industrialization, globalization and recently the demographic shift and the global savings glut. I view recent history not as an aberration, but indicative of things to come, since most fundamental drivers of natural rates are unlikely to reverse. This is especially so as aging demographics spread to the whole world and rising incomes support higher propensities to save for retirement, one of the big economic shifts we face in the 21st century. I presented my most recent estimates of neutral rates for several advanced economies, which show that neutral rates remain very low in these economies, and that the main driving forces have not changed materially. This would imply that current UK monetary policy and the market curve is still quite restrictive.

Alongside these major speaking engagements, I have done a number of smaller events, fireside chats, interviews, talks at schools, community forums, and company visits often while visiting different parts of the country with the Bank of England's Agency Network.

I have visited a total of eight Agencies in my first year on the Monetary Policy Committee: to Scotland, Yorkshire and Humber, the South West, the North East, the North West, South East and East Anglia, Central South England, and Northern Ireland. These visits involved a mix of company visits, private roundtables, community forums, and citizens' panels, where I engaged with businesses in a variety of sectors including food production and agriculture, aerospace and engineering, automotive manufacturing, textiles and apparel, logistics and transport, ports and maritime services, technology and software, and education. During these visits I also visited and presented at schools, including: Crofton Academy, Wakefield; New College, Durham; St Anne's Catholic School & Sixth Form, Southampton.

Further, I have participated in numerous speaking engagements other than speeches, such as a fireside chat and Q&A at the Yorkshire Post, citizens' panels in Darlington and Liverpool, and a community forum in Cambridge.

Finally, my media engagements have included my first interview as an MPC member with the Yorkshire Post; a long-form interview with the Financial Times as a part of the "Economists Exchange" series; another interview with the Financial Times to discuss the policy outlook after the start of the trade war and the one-off shocks causing the rise in inflation; and a live television interview with Bloomberg at the ECB Forum.