Report to the Treasury Select Committee
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Voting record

A few months before I joined the Committee, during the early part of 2011, it looked as though the world economy – and, with it, that of the UK – was embarked on a steady (if unspectacular) recovery. Business surveys were consistent with growth at around its trend rate and, with inflation still a long way above the target, any additional monetary stimulus seemed unwarranted. In my view this remained the case through the early part of the summer as signs of weaker growth were, at least in part, attributable to higher energy prices, which was were also pushing up on near-term inflation.

Since then, events have taken a material turn for the worse, particularly in other parts of Europe. In early August, concerns about indebtedness and competitiveness in some parts of the euro area led to a sharp weakening in the price of risky assets, including sovereign debt in the "periphery" countries and, on a wider basis, the debt and equity of European banks. This threatened a renewed round of credit withdrawal across the continent, including in the UK. It also meant that the rise in oil and other commodity prices came to a halt. Along with the rest of the Committee, I therefore voted for an expansion of asset purchases in October and again, following weaker forecasts in both the November and February Inflation Reports, in February 2012.

Along with other policy actions, most notably the two large auctions of ECB liquidity (the "LTROs") announced in December, this helped buoy sentiment going into the New Year and business surveys picked up too. In the UK, near-term indicators of output growth improved and firms continued to take on new employees.

However, it was not clear, even then, that there was sufficient growth in the economy to begin to absorb spare capacity in the UK. And the broader rally in sentiment, both in financial markets and among businesses, in any case proved short-lived. European equity indices peaked in March and the euro area's composite PMI has declined in each of the past five months. This may reflect the limitations of central bank policy in the single currency area. The provision of funds by the central bank is clearly crucial, in times of stress, if the underlying strains in the Euro area are not to be multiplied by a full-blown banking crisis, and the LTROs succeeded in that respect. But this lending does not, in and of itself, solve the underlying problems of indebtedness and competitiveness.

More recently, our own task on the MPC has been complicated by an upward revision to the near-term forecast for inflation (between the February and May Inflation Reports) and I have therefore refrained from voting for a further easing in policy since February. That said, I have been reassured that measures of medium-term inflation expectations in financial markets have, of late, fallen back slightly. It is also notable that the price of crude oil has fallen back materially since its peak in early March.

The outlook

The economy remains in a difficult position. Weak activity over the past year owes something both to the earlier rise in commodity prices, and the resulting squeeze on real domestic income, and also to continued fiscal tightening. These particular pressures are likely to ease in coming months. In the absence of any renewed upward pressure on commodity prices the squeeze on real household incomes will subside, mostly via lower inflation (rather than faster nominal wage growth). As for the fiscal position, the OBR projects a decline of 0.4% of GDP in the government's cyclically adjusted primary balance during the current fiscal year, compared with well over 3% of GDP during the past two years.

In my view, however, a good part of the drag on UK activity relates to the problems of the euro area, and it is much less clear that these are abating. Investors remain nervous about the underlying strains and imbalances within the system and about the authorities' capacity to address them. In the meantime, the risk of a much more extreme outcome is pushing up yields on risky assets throughout the continent. Note that, although this is transmitted (and probably amplified) partly by the banking system, a cost that is then borne by borrowers dependent on bank lending, the past two years have seen a rise in financing costs even for those borrowers (such as large companies) that can, in principle, by-pass the banks.

This tightening in financial conditions has affected demand in the economy and the near-term indicators suggest that, abstracting from the various short-term distortions (the effect of the Golden Jubilee holiday, for example), output is broadly flat in the next quarter or two, as it has been for the past eighteen months.

By impairing its ability to reallocate resources to areas where economic returns are higher, higher financing premia may also have affected the economy's supply capacity. Whatever the reason, it is evident that productivity growth has been much slower than in previous economic recoveries and it is not clear to me, at any rate, that this is purely the result of weak demand. After all, it is not simply that firms have been failing to shed labour: in aggregate, at least, they have been actively hiring new people. This suggests that the weakness of productivity growth reflects something other than the combination of deficient demand and labour hoarding.

All that said, there still looks to be quite a bit of spare capacity, most obviously in the labour market. It therefore seems likely that, controlling for the short-term influence of commodity prices, inflation will continue to drift down, over the medium term, back to the 2% target.

Explaining monetary policy

In my first year on the Committee I have given three public speeches. The first, last September, discussed the relationship between rebalancing, the exchange rate and inflation. The second, in March, argued that levels of debt in the domestic non-financial economy were not as problematic as many suppose. More recently, in May, I explained how the risk of rare but very bad economic outcomes can impair growth in investment and productivity quite independently of the banking system.

I have given nine on-the-record media interviews, three during Agency visits, seven to national outlets (including the FT and BBC Radio 4 and the Independent newspaper). I have also had several off-the-record meetings with journalists.

I have made four Agency visits, one to the North West (along with the rest of the MPC), last October, the others to the West Midlands (November 2011), Northern Ireland (February 2012) and Wales (June 2012). During these I have made numerous visits to individual companies, as well as attending larger meetings with groups of local businesses.