Report to Treasury Select Committee

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Voting record

Along with a majority of the MPC I voted in November for a 25bp rise in Bank Rate. The reasons were laid out clearly in the minutes and Inflation Report at that time and I'll begin with a brief summary.

Though slow by historical standards, economic growth has been sufficiently above the pace of supply growth that the rate of unemployment has fallen further and the economy's degree of spare capacity has shrunk. This limits the degree of the MPC's tolerance for above-target inflation. It is also likely to lead to some firming of domestic inflationary pressures. In recent months this is evident in signs of a rise in wage growth. So although the effects of sterling's depreciation on CPI inflation are likely to fade over time, that will be partially offset by faster growth of domestic costs. In the MPC's central forecast that means inflation settles marginally above the 2% target and it's against this backdrop that I felt it right to vote for a quarter-point rise in Bank Rate.

Let me add some detail, starting with a reminder of our objectives. The MPC's remit says that, in exceptional economic circumstances, the Committee must balance any trade-off between the speed at which it intends to return inflation sustainably to the target and the support that monetary policy provides to jobs and activity. The steep fall in sterling's exchange rate in 2016, associated with the EU referendum, qualified as such a circumstance. It pushed up significantly the cost of imports and the overall rate of inflation. But it did so at a time when there was still spare capacity in the economy and when uncertainties surrounding the UK's withdrawal from the EU have affected investment spending. In this environment the MPC can tolerate a degree of above-target inflation and aim to bring it back to 2% over a longer period than usual. It also means that, as spare capacity is absorbed, that tolerance is reduced and the period over which one should seek to return inflation to target becomes less extended.

A year ago, the MPC's central forecast was that GDP would grow by 1.6% through 2017 (in the year to Q4), slightly slower than in 2016 but significantly faster than other forecasters were predicting. The consensus forecast was 1.1%. We also thought that the composition of demand growth would shift away from household consumption and towards net trade and business investment.

In these respects the economy behaved as we'd expected. The economy grew by only marginally less than that central prediction (the current estimate is 1.5%). As regards the composition of demand, the predicted rotation has occurred: consumption growth has fallen, investment and net trade have improved.

However, there are two important qualifications. First, the slowdown in UK growth has occurred despite an acceleration in global activity that's been even faster than expected. World GDP grew by 3.7% through the course of last year, stronger than at any time since 2011, with a particularly marked pick-up in the euro area. As a small open economy, the UK is sensitive to economic developments among its trading partners, with business investment particularly well correlated internationally. So the fact that the UK economy has slowed as others have picked up, and that investment growth has been much weaker than elsewhere, is suggestive of a UK-specific drag on the economy. The evidence, including the Bank's Decision Maker Panel survey, suggests the impact of Brexit-related uncertainty on firms' investment decisions is one important factor.

Second, even if growth of demand turned out broadly in line with the MPC's expectations, growth of productivity and overall supply have been notably weaker. Instead of rising slightly, unemployment has fallen further over the past year, and there are signs that the resulting tightness in the labour market is beginning to push up wage growth. In the latest six month period, between May and November last year, regular average private-sector earnings grew at an annualised rate of 3.1%, up from 1.9% over the previous six months.

The outlook

In its latest forecasts, in the February Inflation Report, the MPC has said it expects another strong year for the global economy in 2018. This will continue to support economic activity in the UK and we expect further improvements in net trade and business investment this year. Consumption growth is likely to remain relatively subdued, though the squeeze on households' real incomes is past its worst. Wage growth looks to be picking up, and although the rise in import costs will continue to feed through to retail prices for some time yet, the rate at which it does so is probably around its peak right now.

As regards inflation, therefore, there are two offsetting effects over the forecast period. The external influences are likely to moderate over time but, with only very limited spare capacity in the economy at present, and potential growth notably lower than in the pre-crisis period, domestic cost growth is expected to pick up. On balance the first of these is expected to dominate – inflation is projected gradually to decline – but, at least on the market-path of interest rates on which the forecasts are conditioned, inflation is still likely to be marginally above the 2% target in two to three years' time. This means further rises in interest rates to above 0.50% are likely to be required, though we still believe those are likely to be gradual and limited in extent.

As ever these are expectations not promises and there are considerable risks and uncertainties surrounding the forecasts. The Brexit process is one of those. The MPC's forecasts are based on the average of a range of possible outcomes for the eventual agreed trading arrangements between the UK and other countries and also on the assumption that households and businesses plan on the basis of a smooth adjustment to those arrangements. But there's a long way to go and conditions could always change. More generally, no point forecast will ever be precisely correct, which is why the MPC has always published its growth and inflation forecasts as "fan charts", with probability ranges, rather than individual lines.

Whatever these developments the Committee stands ready to respond as they unfold to ensure a sustainable return of inflation to the 2% target.

Explaining monetary policy

Since May 2016 I have given five on-the-record speeches on various monetary policy issues:

- 15.11.2017 Brexit and interest rates
- 11.07.2017 Winners from globalisation
- 23.03.2017 Brexit and the pound
- 18.11.2016 The distributional implications of low structural interest rates and some remarks about monetary policy trade-offs
- 05.10.2016 Uncertain times

On the day of each Inflation Report, in addition to answering questions alongside the Governor at the televised press conference, I host a briefing meeting at the Bank for private sector economists. I chaired a session of the Bank's Monetary Policy Roundtable, a forum to discuss various issues with external economists.

I made seven regional visits (to Wales, North East, South East, North West, Northern Ireland, Scotland, and West Midlands). These have involved meetings and roundtables with local businesses and events at which I have presented, and taken questions on, the Inflation Report. I have also attended two Future Forums in the Midlands and Liverpool.

I have given several interviews, including to Sunday Times, BBC Radio 4, Wall Street Journal, Bloomberg, Reuters, The Times, Derby Telegraph, and BBC 5 Live. I have attended a variety of meetings and events with journalists, City economists and market participants. Finally, as Deputy Governor for Monetary Policy, I have represented the Bank's views in international settings, including Jackson Hole, ECB, Bellagio, OECD Working Party No3, and the G7.