Annual report to the Treasury Select Committee

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Overview

Macroeconomic conditions have changed materially over the past year. A year ago, underlying inflationary pressure was easing alongside subdued activity and a loosening labour market. By the February 2026 Monetary Policy Report (MPR), CPI inflation was expected to return to around the 2% target from spring. The outbreak of conflict in the Middle East in late February significantly changed that outlook as disruption to global energy supplies pushed up energy prices and the near-term path for inflation. As the conflict has persisted, there is an increasing risk that further policy action may be needed in response to higher and more volatile energy prices to prevent direct effects becoming embedded in domestic wage and price-setting.

I voted to hold Bank Rate throughout this period until November when I voted, with most of the Committee, to increase Bank Rate by 25bps to 4%. The considerations underpinning these decisions have evolved. At the end of last year, the key question for me was how quickly restriction could safely be withdrawn as disinflation continued. That cautious withdrawal of policy restriction has given way to a focus on whether policy needs to tighten to prevent a prolonged external energy shock from becoming embedded in domestic inflation.

In September the MPC also set out a multi-year strategy for quantitative tightening. This sets a clear path to fully unwind gilt holdings for monetary policy purposes, alongside wider changes in the balance sheet made by the Bank Executive. The strategy reduces uncertainty for markets and reinforces the credibility of QE as a temporary monetary policy tool.

As Deputy Governor for Monetary Policy, I remain focused on leading the Bank's programme to transform monetary policy in response to the Bernanke Review of forecasting and communication. We have made substantive changes to improve our policy process and published communications. These are now embedded in how we work. The new tools developed have played a central role in the Committee's response to the Middle East conflict and the reforms to our communications have increased transparency around the majority view and individual judgements of the Committee. The focus is now on completing the multi-year reforms to strengthen our underlying data, modelling and analytical infrastructure.

Voting record

My policy decisions over the past year have reflected the changing nature of the risks to inflation. These have evolved from uncertainty about the extent to which earlier shocks would continue to propagate through domestic wage- and price-setting to increasing concern about the cumulative effects of renewed and repeated disruption particularly to energy supply.

By the **November 2025** policy meeting, the UK economy was on a disinflationary path and Bank Rate had been progressively reduced from its previous peak of 5.25% in August 2023. The question at the time was how quickly the remaining degree of monetary policy restriction should be removed. While I expected headline inflation to continue to fall, I remained concerned that underlying inflationary pressures could prove more persistent because of the risk of structural shifts in wage- and price-setting. Given uncertainties around the degree of policy restriction in the level of Bank Rate, I voted to maintain Bank Rate at 4%.

At the **December 2025** meeting, headline inflation had fallen further and the near-term outlook had improved. This was welcome news but I did not judge it sufficient to resolve my concerns about inflation persistence. Some of the improvement reflected mechanical effects from administered prices, while underlying inflation remained above target-consistent rates. Forward-looking indicators from the Decision Maker Panel survey and the Bank's Agents pointed to little further disinflation in wage growth over the following year despite a weakening labour market. I saw a risk that this combination of data reflected structural changes that could sustain inflation persistence and remained uncertain about the degree of policy restriction. Given those risks, I voted to maintain Bank Rate at 4% and dissented from the majority decision to reduce it to 3.75%.

Following the reduction in Bank Rate in December, I voted to maintain the new rate of 3.75% at the **February 2026** meeting. The disinflation process had continued and the near-term inflation outlook had improved further, with CPI inflation now expected to return to around target from April. This reduced some of the upside risks I had previously identified, but wage growth and underlying inflation remained above target-consistent rates. At the same time, the labour market had loosened materially and activity remained weak, leaving risks on both sides of the outlook. With policy closer to neutral, the case for further easing had become a closer call. I judged that a more prolonged period of restriction was warranted while evidence accumulated on underlying inflation and the balance between demand and supply.

By the **March 2026** meeting, the outlook had changed materially following the outbreak of conflict in the Middle East and the resulting sharp rise in global energy prices. Uncertainty over the size and duration of the energy price shock and how it would propagate through the UK economy was extremely high in the early days of the conflict. The shock was expected both to raise inflation and reduce output, creating a difficult trade-off for monetary policy. At that stage, we had limited information on how persistent the disruption would prove or on the scale of any second-round effects through expectations, wages and prices. I therefore voted

with the rest of the Committee to maintain Bank Rate at 3.75%, while making clear that I was prepared to act as needed to address any persistent inflationary effects as the evidence emerged.

I again voted to maintain Bank Rate at 3.75% at the **April 2026** meeting. Given the exceptional uncertainty around the outlook, instead of a central forecast the MPC set out three scenarios which illustrated different paths for energy prices and their propagation through the economy. I placed most weight on Scenario B, which allowed for both more persistent energy prices and some second-round effects while recognising downside risks to activity. Financial conditions had tightened materially since the outbreak of conflict reflecting the changed balance of risks. I judged that this tightening was warranted and, alongside Bank Rate at 3.75%, provided an appropriate degree of restriction while evidence accumulated on the potential medium-term implications of the shock. Although I did not view the more adverse Scenario C as my central case, I judged it plausible and was prepared to respond more forcefully if stronger inflationary pressures emerged.

The data available at the **June meeting** for the months immediately following the shock told us more about the disinflationary process that had been underway before the Middle East conflict, than about how the energy shock was playing through the UK economy. That data suggested the pre-conflict disinflation had continued, but considerable uncertainty remained about over the inflationary impact of the shock. It remained too early to draw firm conclusions about second-round effects but tighter financial conditions were already leaning against inflationary pressures. Given this combination of data on underlying disinflation and uncertainty over the future propagation of the new shock, I judged that maintaining Bank Rate at 3.75% remained appropriate while further evidence accumulated. I remained prepared to respond more forcefully were there signs that inflation would persist above target.

Incoming data showed underlying disinflation gradually continuing into the **July meeting** and, given the time needed for them to appear, there was still little evidence of material second-round effects from the energy shock. But energy prices remained volatile and above pre-conflict levels with risks skewed to the upside. It was still too early to conclude that more significant second-round effects would not emerge. I judged that monetary policy was restrictive, particularly once the tightening in broader financial conditions was taken into account. That provided sensible insurance against inflation risks and I therefore voted to maintain Bank Rate at 3.75%, continuing to stand ready to adjust policy if necessary.

By **September**, continued volatility and renewed increases in energy prices had become the dominant feature of the inflation outlook. A longer conflict led to oil and gas prices closer to those in the July adverse scenario. Notwithstanding those developments in wholesale energy prices, indirect pass-through to wider consumer prices appeared to be slower than anticipated. There was still little evidence of material second-round effects but the increasing duration of the shock raised the risk that higher energy prices would eventually become embedded in domestic wage and price-setting. Activity and the labour market had also turned

out to be more resilient than expected despite financial conditions and the direct cost impacts of the shock. I therefore voted to maintain Bank Rate at 3.75% but judged that the balance of risks had shifted further to the upside and that the case for raising Bank Rate was building the longer the conflict continued without a lasting resolution.

At the **November 2026** meeting, I voted with the majority of the Committee to increase Bank Rate by 25 basis points to 4%. The conflict had lasted longer than expected, keeping oil, gas and refined product prices elevated and making the inflationary effects of the energy shock larger and more persistent. Cost pressures had remained elevated for long enough to increase the risk of second-round effects becoming embedded in domestic wage and price-setting. Despite this, economic activity had proved more resilient than expected, while recent data suggested that underlying disinflation might have stalled. I recognised downside risks to inflation from a more benign path for energy prices or a slowdown in activity. But, given continuing energy price uncertainty and limited evidence of spare capacity, I judged that the balance of risks to inflation lay to the upside of the central forecast and that an increase in Bank Rate was warranted.

Across these decisions, my approach has sought to use policy to use policy to push down on the risk of inflation persistence as the nature of that risk has evolved. At the end of last year, the question was how quickly policy restriction could safely be withdrawn as disinflation continued. I had advocated for a cautious withdrawal of restriction because I saw upside risks to inflation in the medium term. The outbreak of conflict in the Middle East then created a new policy trade-off. Its medium-term consequences were initially highly uncertain and it was appropriate not to react to the immediate rise in headline inflation. As the year progressed, holding Bank Rate alongside tighter financial conditions provided continued downward pressure on inflation and time to assess how the shock would propagate through the economy. Given the length of time that energy prices have now been high and volatile the balance of risks has shifted in a way that has strengthened the case for tighter policy should those risks continue to build.

Quantitative tightening

As Deputy Governor for Monetary Policy, I oversaw the development of the MPC's multi-year strategy for quantitative tightening (QT) alongside Dave Ramsden, Deputy Governor for Markets and Banking. The strategy replaces annual decisions on the pace of QT with a clear longer-term path to completely end gilt holdings for monetary policy purposes. It combines annual gilt sales with maturing holdings to run the portfolio down to zero. This provides clarity not just about the next year's reduction, but about the intended direction of the portfolio over the years ahead. There are monetary policy benefits of specifying both the destination and the path to it. Alongside the rest of the Committee, I supported the multi-year strategy of £20 billion of annual gilt sales with maturing holdings to deliver an average annual reduction of £46 billion. I judged this pace to be a pragmatic balance between making progress on

reduction at a rate we are confident will be smoothly digested by the market.

A commitment to complete the unwind is important for the credibility of QE as a monetary policy tool. QE was first introduced following the 2008 financial crisis and was intended to provide temporary stimulus, rather than to become a permanent feature of the Bank's balance sheet. Confirming the intention to fully unwind holdings for monetary policy purposes improves the credibility of the tool. Should economic conditions require it, monetary policy makers would need optionality to deploy QE in future, recognising there are challenges with the tool, as there are with all economic tools available at the zero lower bound.

A clear multi-year approach to QT also has benefits for financial conditions. Investors need to form a view about the future supply of gilts. Uncertainty about the scale and timing of the Bank's sales can add to the risk premium, separately to the expected volume of those sales. An annual decision-making cycle led to a recurring question about the next stage of the unwind. Setting out the planned path over several years reduces that uncertainty, allowing market participants to incorporate the intended reduction in holdings into their expectations. The effects of QT can be absorbed more predictably.

The best available analysis suggests the effects of QT have been small, but these estimates come with considerable uncertainty. These estimates suggest that QT has made a modest contribution to tighter monetary conditions, with its cumulative impact estimated to have raised ten-year gilt yields by around 20–30 basis points. Assessing these effects involves examining movements in yields around QT announcements, alongside model-based analysis of how changes in the supply of bonds affect the pricing of the interest-rate risk. These estimates are necessarily uncertain: QT has often been anticipated, so its effects need not occur on announcement dates, and the relatively short experience of QT makes it difficult to separate its contribution from other influences on yields. Its impact can also vary with market conditions and investor demand. So these estimates give us a sense of scale of the likely effects and provide confidence that those effects have not been significantly larger.

The MPC's strategy is distinct from the Bank Executive's decisions about implementation and balance-sheet management. As the Executive, we decided to retain £120 billion of the longest-dated gilts in the Asset Purchase Facility (APF), holding them to maturity to back current and future banknote issuance indirectly. Their retention is consistent with the full monetary policy unwind because they will no longer be held for monetary policy purposes. The Executive also announced its intention, subject to agreement with HM Treasury, to sell gilts to the Government rather than directly to the market, restoring a single public sector supplier of gilts. These arrangements concern how the unwind is delivered; the MPC remains responsible for the monetary policy decision. The distinction is important: retaining assets for a separate balance-sheet purpose does not dilute the commitment to exit the existing QE portfolio for monetary policy purposes.

Reforming our monetary policy processes and communications

One of my areas of responsibility is the implementation of the 2024 Bernanke Review of forecasting for monetary policymaking and communication. Our response to the Bernanke Review has moved forward significantly over the last year. Many of the reforms are now embedded in the MPC's regular work and communication. The final phase will build on these changes and complete the investment in infrastructure, tools and skills needed to sustain these improvements. The attached Annex sets out the progress we have made to date and what the final stage of the programme will include.

The experience of the past year has provided an important test of how those reforms can be applied in practice. The conflict in the Middle East has led to a highly uncertain policy making environment. Our new tools, developed through the implementation of the Bernanke Review have proved useful in helping us understand the implications of that uncertainty and improving our monetary policy communication through this period.

One important change has been to move away from relying too heavily on a single model or central forecast to organise the policy debate. We are bringing a wider range of models and analytical approaches into policy discussions, with an emphasis on considering alternative paths for the economy and challenging consensus views. The central projection remains an important organising device, but it now sits alongside a wider range of models and analytical tools designed to understand different features of the economy. We also now evaluate our forecasts more systematically and learn from our errors. And we are communicating more clearly the assessments underlying individual MPC members' votes and how that sits with the Committee's collective assessment. We have used scenarios to structure our internal policy discussion around the major areas of uncertainty, in particular the uncertainty around energy prices and their propagation through the economy.

We have deployed enhanced energy modelling. In particular, we have upgraded COMPASS, our core DSGE model used in the forecast to feature a more sophisticated treatment of how energy affects the economy. We have also used separate models to capture inflation mechanisms which are not fully captured in COMPASS. We applied the approach by Bernanke-Blanchard to quantify our assessment of second-round effects and the extent to which higher inflation expectations feed through to wage and price setting.

We are developing our use of AI to bring faster analysis of a richer set of data sources into the policy process. For example, better processing information gathered through the Bank's Agents which are a particularly helpful source of insight at times of shocks and uncertainty as they give us a timely read on how businesses are thinking about and responding.

Our first Forecast Evaluation Report has given us a more systematic way to understand forecast errors and whether they reflect data, models or assumptions. Since publication of the Forecast Evaluation Report, staff have prioritised improvements in the areas where past forecast errors were greatest. These include (i) a better treatment of the effects of energy

shocks on activity and inflation, (ii) an enhanced wage-modelling suite, which reduces post-Covid forecast errors, (iii) a more realistic treatment of the effects of fiscal policy on GDP, and (iv) more regular reviews of developments in potential supply. While uncertainties will always remain, confidence in these areas has been improved following these modelling changes.

That analytical breadth has been valuable this year in considering alternative paths for the economy. We have also encouraged staff-led challenges to the consensus view and have used scenarios to consider alternative outlooks for the economy. Scenarios make alternative assumptions explicit, trace their economic consequences and help identify the judgements and risks that matter most for inflation and policy. The Bank's post-Bernanke capabilities have been used to generate a range of input scenarios through the conflict for the committee to consider and some of those have been published as outputs in April, July and November to help explain how different factors affect the economic outlook and the impacts on policy. For example, showing how different paths for energy prices would change the needed policy.

Scenarios have also provided a framework for learning. By setting out in advance the mechanisms and assumptions associated with different outcomes, scenarios give the MPC a benchmark against which to interpret incoming evidence and reassess which risks are materialising.

By November, energy prices had risen materially further since July, but indirect effects on other prices continued to be smaller than expected and evidence of second-round effects remained limited. Activity had also proved more resilient. Box A of the November MPR updated the monitoring indicators, stressing that limited evidence so far did not rule out stronger effects later. Our scenario analysis has helped us distinguish between the evolution of the energy shock itself, which had become larger, and its transmission through the economy, which had so far been weaker.

The November MPR also considered a weaker demand scenario. It explored how households and businesses becoming less able to absorb the energy shock could weaken activity, increase spare capacity and limit second-round effects. This is a risk we need to monitor. The comparison illustrated why the policy response depends on the economy's reaction to higher energy prices, not just the prices themselves (see Section 3).

External Engagement

Articles

- Global imbalances are back.
- This time it's personal: the rise of dynamic, personalised pricing and what it means for inflation.

On the record speeches

- The Outlook for Inflation, given at the Sixth Biennial Conference on Macroeconomic Policy, Warsaw, 24 September.
- The low-gear labour market, given at the Bank of England Watchers Conference, London, 10 November.

On the record interview

- Young people in UK hit by 'low-gear economy', The Guardian, 10 November.

I have made 9 regional visits since my last annual report. These involve meetings with individual businesses, roundtables, school visits, public meetings and community events.

South West – 23-24 September 2025

Central Southern – 8 October 2025

Wales - 17-18 November 2025

South East & East Anglia - 26 March 2026

Yorkshire - 13-14 May 2026

North West - 29-30 June 2026

North East - 13-14 July 2026

Greater London – 29 September 2026

West Midlands – 7-8 October 2026

Annex: Progress Implementing the Bernanke Review[1]

The Bank has made substantial changes to its analytical and policymaking processes, with more to come

Following the period of above-target inflation, the Bank's Court of Directors commissioned Dr Ben Bernanke to review forecasting for monetary policymaking and communication in times of uncertainty (Bernanke, 2024). His review found that forecast performance had deteriorated across central banks and other forecasters in the face of exceptional shocks, and that the MPC's forecast shortcomings were not materially worse than those of relevant comparators. Nevertheless, the review recommended substantial changes to the Bank's data, models, infrastructure, policy process and communications.

The Bank is implementing those recommendations. Our objective has been not just to improve forecasts, but to help the MPC make well-informed, robust decisions when the outlook is uncertain and to explain those decisions more clearly. As set out in a 2025 Quarterly Bulletin article, a central forecast remains useful but cannot capture every risk that matters for monetary policy. Considering alternative perspectives and challenging assumptions help the MPC assess whether its policy judgements hold up if events unfold differently. Explaining that reasoning also helps Parliament, markets and the public understand and scrutinise the MPC's decisions.

Many of the most externally visible changes to the policy process and communications are now in place. The next phase will focus on embedding these improvements and completing the investment in infrastructure, tools and skills needed to sustain them. Key changes include:

Bringing a wider consideration of uncertainties, risks and challenge into policy discussions.

The MPC is now presented with a wider range of analysis, evidence and perspectives, including alternative scenarios and policy rules alongside the central forecast. This helps the MPC to identify risks that a single model or forecast might miss, and test how sensitive its policy judgements are to different assumptions.

The MPC regularly explores scenarios alongside a central forecast, recently examining alternative energy-price paths and their effects following developments in the Middle East. A new semi-structural model, featuring the richer sectoral detail recommended by the Bernanke Review, is being developed to help compile the central forecast in future. The

[1] The material in this annex has also been submitted by the Bank as part of its evidence into the TSC Inquiry into 30 years of monetary policy independence.

current model, COMPASS, is being upgraded and will form part of a more pluralistic modelling approach, which also includes new models to capture important features of the economy (such as energy and labour markets) in greater detail.

New approaches to producing the central projection and scenarios under alternative assumptions about monetary policy have been developed. These tools enable a richer exploration of both the potential policy implications of alternative scenarios and the effects of alternative policy approaches in any given scenario. Considering both aspects informs MPC discussions of the likely robustness of different policy approaches.

We are developing our use of AI to bring faster, deeper analysis of a richer set of data sources to the MPC. For example, our Agency Network is using AI to help summarise business intelligence more quickly and draw out implications from the vast quantity of rich text-based information collected through our interactions with business contacts.

Policy discussions now include staff-led challenges to the prevailing view, helping to bring alternative explanations into the debate. A Monetary Policy Innovation Lab has been created to provide greater capacity for staff to apply new and challenging perspectives to key policy issues.

Looking ahead, we will continue to expand our external engagement efforts (recent examples of which include the June 2026 Chief Economists' Workshop and our biannual Macro Modelling for Monetary Policy forums) to explain our changes and hear outside perspectives.

Explaining policy decisions and uncertainty more clearly.

Clearer explanations of risks, judgements and policy choices give Parliament and the public a better basis for understanding why the MPC has reached its decision, where members disagree and what could affect future decisions. This strengthens transparency and makes it easier to hold the Committee to account.

The Monetary Policy Report (MPR) now gives greater prominence to risks, uncertainty, scenarios and policy strategy. Analysis of these areas complements a central projection that is based on a staff proposal that a majority of the MPC agrees is a reasonable baseline, rather than attempting to capture the MPC's 'best collective judgement'. This approach allows for a broader range of analysis to inform MPC policy decisions.

The MPR's Monetary Policy Overview explains how these inputs fed into the Committee's decision. The Minutes now explain the judgements behind each individual MPC member's vote, alongside the Committee's discussions in reaching its decision.

We will continue to use external feedback to assess how well these changes help audiences understand the MPC's decisions and the uncertainties it faces, and to improve how we present scenarios and policy choices.

Learning from forecast errors and opening up our monetary policy analysis to scrutiny.

The Bank is publishing more of the analysis behind our monetary policy work and has built stronger tools for systematically evaluating forecasts. This helps staff identify where models, assumptions or judgements could be improved.

Publishing the methods and findings allows others to scrutinise that assessment and contribute to improving our approach. The published material includes the **Forecast Evaluation Report**, staff **Macro Technical Paper No. 6** on the Bank's enhanced approach to forecast evaluation, an **open-source Python forecast evaluation toolkit** for others to use and develop, and the forecast evaluation dashboard used for the Report.

We have discussed this work with external researchers including at events with **NIESR and King's College London**, and **Leeds University**, and will continue to do so, to encourage scrutiny, discussion and challenge of our methods and findings.

Strengthening the data, technology and expertise that support policy advice.

Much of the remaining work will focus on continuing to build and embed the foundations needed to sustain these improvements. Embedding and continually improving capabilities across data, technology and people reduces operational risk and supports efficiency over time.

We are moving nearly two million data time series to a new data platform to make them easier to access and use. The new platform will dramatically reduce the time taken to gather, analyse and visualise data, creating more capacity for staff to focus on deeper analysis and research.

We have strengthened senior leadership and expertise in macroeconomic modelling, monetary policy strategy and data science, and brought research closer to policy work. We have also trialled teams that bring together staff from different specialisms to work on priority questions for the MPC. These changes will be finalised under a new operating model to make our ways of working more effective.

We will continue to broaden and upgrade our economic models and data infrastructure, addressing gaps in our ability to analyse developments that matter for policy.
The planned investment is expected to be completed in early 2028. Testing and improving

our tools, analysis and communications will continue beyond that date as part of the Bank's regular work. We will assess how the changes are working, draw on external feedback and publish updates on progress. The aim is to make these improvements—and the capacity to keep adapting—a lasting part of how the Bank conducts monetary policy, rather than something that depends on repeated upgrade programmes.