Report to the Treasury Select Committee

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Voting Record

Between joining the Committee for its meeting in August 2010 and December of the same year, I voted for no change in either asset purchases or in Bank Rate. Late last year, I became increasingly concerned about the rising rate of inflation and the implications of this for the Committee's ability to deliver its target. In January I therefore voted for a quarter point increase in Bank Rate.

A substantial part of the rise in inflation in January of this year was due to the increase in VAT announced in last year's budget. I felt comfortable with the principle that, because the effect of this would drop out of the inflation rate after about twelve months it would not be appropriate for policy to adjust in direct response to this. There was nevertheless a risk that the resulting increase in prices would have knock-on effects to wage demands; Britain's past history suggested that this risk was a very real one.

Inflation was also elevated because of rising commodity prices and as a result of continuing upward pressure in the aftermath of sterling's depreciation in 2008 and there was a risk that these influences could also have knock-on effects on wages. There is always considerable uncertainty about the future path of commodity prices and also about the full extent one might expect prices to rise in the aftermath of the depreciation. The Committee has a target for consumer prices and not for domestic costs. This means that it should attempt to offset continuing effects of such influences on the inflation rate. At the same time it does not have an effective means of offsetting the short-term consequences of such movements.

There were two factors which lay behind my vote. First of all, the Inflation Reports produced in February and May showed that, if interest rates followed the profile implied by the profile of term interest rates in the money markets, then inflation was expected to be above its target at the two to three year horizon at which the Committee aims to bring the inflation rate to its target. To me, this pointed to a need for a Bank Rate path higher than the market was then expecting.

Secondly, even if the market profile had been adequate to bring inflation to target over a two to three year horizon, it seemed to me that there were benefits in increasing Bank Rate earlier rather than later. An earlier tightening would reduce the need for tightening later on. And it would give extra benefits in terms of credibility at a time when the Committee's reputation was affected by rising inflation.

The economy was weaker in the first half of this year than I had hoped, and by the summer my concerns about developments in the euro area had increased. At the same time weakening commodity prices meant that some of sources of inflationary pressure which had worried me were less acute. Putting these factors together and bearing in mind, in particular, the risk of an intensifying financial crisis, I voted for no change in policy in August and September. Had Bank Rate been increased earlier in the year I would have voted to reduce it. By October it was clear that the crisis in the euro area was having more marked effects on activity at home and I therefore joined my colleagues in voting for an additional £75bn of asset purchases. In November I voted to maintain the asset purchase programme on that scale.

The Outlook for the UK Economy and Inflation

The short-term outlook for the economy is that little growth can be expected either in the current quarter or in the first half of next year. Beyond this, while the outlook is as always uncertain, there is no reason to expect growth at rate below the historical trend. In the long term growth may resume at its trend rate or perhaps somewhat faster. The major source of short-term uncertainty the economy faces stems from the continuing crisis in the euro area. It is clear that the current situation cannot continue indefinitely. But there are a number of different ways in which it could be resolved. Some would be highly disruptive to the international economy and others less so. It is possible that the removal of the current uncertainty, following an orderly resolution of the crisis, would be a positive rather than a negative shock to the economy.

I mentioned above the inflationary risks which concerned me earlier in the year and it is clear that at least some of these have not materialised. With commodity prices having stabilised and the VAT rate dropping out of the calculation, the rate of inflation must be expected to fall fairly sharply in the first part of next year. Weak economic growth is likely to exert its own additional influence in bringing down inflation.

On the face of it there is a strong case for further asset purchases. Increasing the rate at which the Bank makes asset purchases runs the risk of disrupting the smooth running of the gilts market. But if neither economic prospects improve sharply nor inflation prospects worsen, relative to the way they appear at the moment, then I think there will be a strong case for extending the asset purchase scheme when the current purchases of £75bn have been completed and when it is clear that inflation is falling as we have forecast.

Activities

Having voted in a minority in the first half of the year and then changed my vote in August before supporting more asset purchases in October, I have thought it particularly important that I should be prepared to explain my views. Since joining the Committee I have:

- Made four public speeches discussing economic circumstances and commenting on structural issues, in one the focus was my thoughts on the presentation of uncertainty.
- Undertaken nine regional visits.
- Made thirty-four visits to companies as a part of these.
- Talked to sixteen business groups.
- Given interviews to *The Times*, *Handelsblatt*, *The Financial Times*, Sky News, Radio 4 and Reuters as well as regional newspapers and local radio stations.
- Published an article in *The Guardian.*