Annual Report to the Treasury Select Committee

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Voting record

I last reported to the Committee in June 2009. Since then the MPC has voted to expand its asset purchase programme, by £50bn at the meeting in August 2009, and by a further £25bn in November 2009, taking the total stock of purchases to £200bn. I voted in favour of those decisions. In August, although there were already some signs of the beneficial impact of the asset purchases on risky asset prices, there were few signs that a durable recovery was in prospect. Most notably, GDP fell in the second quarter, and broad money growth was weak. That meant a significant margin of spare capacity was likely to persist over the medium term, pulling down on inflation. In November, I was persuaded by the case for further action: the Q3 activity data had also been surprisingly weak; and it had become increasingly clear that substantive fiscal consolidation would be needed in the UK, which would weigh on demand.

Asset purchases reached £200bn by the time of the February meeting, at which point the MPC agreed to pause further purchases, and to maintain Bank Rate at 0.5%. Choosing the level of asset purchases at which to pause was one of the most complex decisions I have faced so far on the Committee. Some of the medium-term nominal indicators such as money and earnings growth remained consistent with subdued growth and below-target inflation. But set against that, there were upside risks to the medium-term inflation profile from the decline in the exchange rate, and potentially from rising CPI inflation itself. And there were tangible signs that asset purchases were having their desired effect, particularly through the positive impact on asset prices. On balance, I judged that policy should not be loosened further, but that the Committee should stand ready to act if the outlook deteriorated markedly.

Since then, upside risks to inflation have remained, or indeed become more magnified and actual CPI inflation has been higher than we previously expected. At the same time, downside risks to the global recovery have increased. Against that backdrop, I have voted to keep Bank Rate and the level of asset purchases unchanged.

The outlook

I expect the economy to evolve broadly in line with the projections embodied in the May *Inflation Report*. A recovery has been underway since late 2009, and should continue to gather strength, as the effects of the exceptionally large monetary stimulus, the past depreciation of sterling and a prospective recovery in global demand feed through. At the same time, and as I discussed recently in a speech in Liverpool, inflation is likely to continue to fall back, as the temporary upward pressures unwind, and the large margin of spare capacity in the economy bears down on prices. However, there are risks to that profile – recent events serve to highlight that. I would pick out three. First, the strength of the recovery in global demand remains uncertain – indeed the outlook appears to have weakened somewhat, in light of the sovereign debt crisis in the euro area and the associated fiscal consolidation. Second, and related to that, recently financial markets (including bank funding markets) have become more fragile, potentially exacerbating already restricted credit conditions for households and firms. An insufficient supply of credit – especially to support investment by businesses – would be a major drag on the recovery going forward. Third, inflation is likely to continue to be buffeted by temporary factors such as volatile energy and commodity prices and a higher VAT rate. It will be important for the Committee to assess how that affects medium-term pricing behaviour and inflation expectations.

Explaining monetary policy

In these exceptional times, it is more important than ever that the MPC coherently explains the challenges it faces in setting policy. With quantitative easing, the framework for implementing monetary policy has also changed. So as the Bank's Markets' Director, I believe it is important for me personally, to help build confidence amongst the market community and the wider general public about the implementation framework. Over the past year, I have given three on-the-record speeches outlining: how the Bank's Balance Sheet has been used to support monetary policy (and financial stability); the policy motivation and mechanics of corporate asset purchases; and more recently a discussion of why CPI inflation has been so high. And I have been interviewed by the media (both national and regional), as well as undertaken a number of informal background briefings with media contacts over the year. That has been supplemented by several unpublished presentations to a wide range of audiences including trade associations, market economists, business people and financial market contacts.

Since my last report I have made five personal visits to parts of the United Kingdom outside of London: Scotland, Wales, the North West, West and East Midlands regions. That has involved several round-table meetings with groups of business people as well as a number of individual company visits.

The Bank also has an established global network of contacts in banking and capital markets to provide timely and well-informed market intelligence. That network also facilitates two-way conversations - giving the opportunity to explain the Bank's thinking on monetary policy (and financial stability issues). During the past year, I have had hundreds of meetings, phone calls etc, with market participants or their representative bodies including leading formal rounds of visits to various financial communities in the United Kingdom and the United States. Finally, together with the Governor and the Deputy Governor for Financial Stability, I regularly represent the Bank in international meetings at the Bank for International Settlements.