INFLATION REPORT PRESS CONFERENCE

Thursday 6th August 2015

Opening remarks by the Governor

Today marks a new approach to monetary policy communications at the Bank of England.

By releasing simultaneously our *Inflation Report* together with the Minutes of the Committee's deliberations, we are ending the drip feed of information around monetary policy decisions.

Instead, we are setting out our assessment of recent economic developments and future prospects in a comprehensive fashion.

One decision; with the forecast and all the supporting analysis released simultaneously.

At this press conference we will, as usual, present the MPC's best collective judgement and speak for the Committee as a whole.

At its meeting yesterday, the MPC voted by a majority of 8-1 to maintain Bank Rate at 0.5%. The Committee voted unanimously to maintain the stock of purchased assets financed by the issuance of central bank reserves at £375 billion. And it reaffirmed its expectation that when Bank Rate rises occur they can be expected to be limited and gradual.

The most striking development in the UK in the past year has been the fall in CPI inflation, which edged back down to zero in June.

As set out in my latest in an expected sequence of open letters to the Chancellor, around three quarters of the deviation of inflation from the 2% target reflects unusually low contributions from energy, food, and other imported goods prices. The remaining part of the undershoot reflects the past weakness of domestic cost growth, and wages in particular.

The combined weakness in domestic costs and imported goods prices is evident in subdued core inflation, which is currently around 1%.

With some underutilised resources remaining in the economy and with inflation below target, the Committee is setting monetary policy to ensure growth is sufficient to absorb the remaining economic slack and to generate the rise in domestic costs needed to return inflation to the target within two years.

Conditional upon Bank Rate following the gently rising path implied by market yields, the Committee judges that this objective will likely be achieved.

Demand outlook

The Committee projects UK-weighted world demand to expand at a moderate pace – about ¾ of a percentage point below historic averages in this year. The composition of that growth is rotating from emerging to advanced economies. Despite steady global growth, UK exports will still be held back by the strength of sterling.

Risks to global growth are judged to be skewed moderately to the downside reflecting risks to activity in the euro area and China.

At home, private domestic demand growth is robust and expected to remain so. This year, household spending has been supported by the boost to real incomes from lower food and energy prices. More recently, wage growth has begun to pick up as the labour market has tightened and productivity has strengthened. Consumer confidence remains its highest for over a decade, and credit conditions have continued to improve, with historically low mortgage rates boosting activity in the housing market.

Business investment has made a substantial contribution to growth in recent years. Surveys suggest this will continue, thereby helping to return productivity growth towards historical averages.

Inflation outlook

The near-term outlook for inflation is muted and the falls in energy prices over the past few months will continue to bear down on inflation at least until the middle of next year.

Nonetheless, a range of measures suggest that medium-term inflation expectations remain well anchored. There is little evidence in either wage settlements or spending patterns of any deflationary mind set among businesses and households.

Sterling has appreciated by 3½% since May and 20% since its trough in March 2013. The drag on import prices from this appreciation will continue to push down on inflation for some time to come, posing a downside risk to its near-term path in particular.

Set against that, the degree of slack in the economy has diminished substantially over the past two and a half years. The unemployment rate has fallen more than 2 percentage points since the middle of 2013, and the ratio of job vacancies to unemployment has returned from well below to around its pre-crisis average.

Robust private domestic demand is expected to be sufficient to eliminate the remaining margin of spare capacity—judged to be around ½% of GDP—over the next year or so, despite the continuing fiscal consolidation and modest global growth. The closing of the output gap, in turn, should generate the rise in domestic costs necessary to counterbalance the drag on price pressures from sterling, and so return inflation to the target in the medium term.

Policy outlook

The MPC's projections are conditioned on Bank Rate following the gently rising path implied by market yields. Under this assumption, demand growth is expected to be sufficient to return inflation to the target within two years. Inflation then moves slightly above the target in the third year of the forecast period as sustained growth leads to a degree of excess demand.

Underlying those projections are significant judgements in a number of areas, as set out in the *Report*. These include the degree to which risks to global growth are contained, the prospects for private domestic demand, the outlook for wage and productivity growth, and the extent to which the external factors currently weighing on inflation dissipate.

In any of these areas, developments might easily turn out differently than assumed with implications for the outlook for growth and inflation, and therefore for the appropriate stance of monetary policy. The Committee will continue to monitor closely the incoming data in tracking these key judgements and will adjust monetary policy as appropriate in order to meet the 2% target in the medium term.

As the UK expansion progresses, speculation about the precise timing of the first move in Bank Rate is increasing. This is understandable and is another welcome sign of the economy returning to normal.

The likely timing of the first Bank rate increase is drawing closer. However, the exact timing of the first move cannot be predicted in advance; it will be the product of economic developments and prospects. In short, it will be data dependent.

The MPC will monitor developments relative to the forecast in particular wage growth, productivity, core inflation, import prices and risks to the international environment.

The path of rates is much more important than the precise timing of the first increase. Given the likely persistence of the headwinds facing the economy the MPC expects Bank Rate increases, when they come, to be gradual, and to be limited to a level below past averages.

By acting in this manner, the MPC can secure the expansion and build on the hard-won gains of recent years.

With that, we look forward to your questions.