INFLATION REPORT PRESS CONFERENCE

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Opening Remarks by the Governor

Remember, remember, the fifth of November. What is memorable about today's *Inflation Report*?

The headlines are familiar. Inflation remains close to zero. I have written another open letter to the Chancellor explaining why and what we intend to do about it. The MPC has voted again by a majority of 8-1 to maintain Bank Rate at 0.5% and by 9-0 to maintain the stock of purchased assets at £375 billion. And once again, as it has since February of last year, we have reaffirmed our expectation that, when Bank Rate rises occur, they can be expected to be limited and gradual.

More fundamentally, monetary policy must continue to balance two fundamental forces – domestic strength and foreign weakness – in order to return inflation to target in a sustainable manner.

So, despite significant market volatility at times, developments since August have left our broad narrative intact. However, recent events have also highlighted some nuances around this story. Let me begin with the global picture, where the most important developments lie.

Global outlook

The outlook for global growth has weakened since August. Many emerging market economies have slowed markedly this year, and the Committee has downgraded its assessment of their medium-term growth prospects. While growth in advanced economies has continued and broadened, particularly in the euro area, the Committee nonetheless expects the overall pace of UK-weighted global growth to be more modest than had been expected in August.

There remain downside risks to our global outlook, including a more abrupt slowdown in China as authorities attempt to rebalance demand, and in emerging economies more broadly, given high levels of debt and vulnerability to capital outflows. A crystallisation of these risks would slow UK growth – both through trade channels and through the effects on domestic spending of lower asset prices and depressed sentiment.

Reflecting concerns about the global outlook, risky asset prices have fallen since August, and there have also been sizeable declines in the yields on safe assets. These have had opposing effects on the forecast. In part, that reflects genuinely lower expectations for the future path of Bank Rate. But in part it also likely reflects a greater preference among investors to hold safe assets, hedging the possibility of more extreme outcomes.

Domestic outlook

In contrast to the global picture, private domestic demand remains resilient, despite ongoing fiscal consolidation. Consumer confidence is firm, real income growth is expected to be the strongest since the crisis, and firms' investment intentions remain robust.

Although it has moderated recently to around trend rates, economic growth is projected to pick up a little towards the middle of next year as a tighter labour market and stronger productivity support real incomes and consumption. Accommodative credit conditions are expected to encourage strong investment and a pick-up in the housing market.

As usual, there are risks around the expected path for domestic activity. To the downside, domestic demand could grow less strongly if households and firms build precautionary savings in the light of greater global uncertainty. To the upside, firms' investment spending could grow more quickly given the shortfall of capital spending during the crisis, or household consumption could grow even more rapidly given supportive borrowing rates. Taken together, the Committee judges the risks to domestic demand to be broadly balanced.

Inflation outlook

The outlook for inflation reflects the balance between persistent drags from factors such as sterling and world export prices, and prospective further increases in domestic cost growth.

Those external factors are dominant in the September CPI data, in which inflation stood at -0.1%, slightly over two percentage points below the inflation target. As set out in my letter to the Chancellor published today alongside our *Report*, around fourfifths of the deviation from the target reflects falls in energy, food and other imported goods prices, with the remainder reflecting subdued domestic cost growth.

The combined weakness in domestic costs and imported goods prices is evident in subdued measures of core inflation, which at around 1%, are rising at similar rates as at the time of our August *Report*.

A number of factors are dampening inflation. These include the effects of sterling's past appreciation and foreign disinflation. The prospects for inflation reflect the balance of the drag from these persistent factors with prospective further increases in domestic cost growth.

The unemployment rate has fallen by three percentage points since its peak, and now stands at around 5 ½ per cent. Robust private domestic demand is expected to produce sufficient momentum to eliminate the margin of spare capacity that remains over the next year. Domestic cost pressures are expected to build as a result of a pick-up in wage growth relative to productivity growth. CPI inflation is nonetheless likely to remain below 1% until the second half of next year, reflecting the continuing drag from commodity and other imported goods prices.

Beyond that, the dampening influence of sterling's past appreciation on inflation is expected to persist, with it likely still affecting inflation in two years' time. A summary of the extensive analysis underlying this judgement is set out in today's *Report*.

Policy outlook

The MPC's objective is to return inflation to target sustainably; that is, without overshooting the target once persistent disinflationary forces ultimately wane. Given these considerations, the MPC intends to set monetary policy to ensure that growth is sufficient to absorb remaining spare capacity in a manner that returns inflation to the target in around two years – and keeps it there in the absence of further shocks.

In the Committee's judgement, the lower path for Bank Rate implied by market yields would provide more than adequate support to domestic demand to bring inflation to target even in the face of global weakness. Were Bank Rate to follow that very gradually rising path, the MPC's best collective judgement is that inflation would slightly exceed the 2% target in two years and then rise a little further above it, reflecting modest excess demand.

The risks to this projection lie slightly to the downside in the first two years, reflecting global factors. That is consistent with a market view that may assign some risk to a sharper deterioration in global conditions.

Underlying those projections are significant judgements in a number of areas, as described in the November *Inflation Report*. In any one 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. Reflecting that, there is a range of views among MPC members about the balance of risks to inflation relative to the best collective judgement presented in the November *Report*.

All members agree that, given the likely persistence of the headwinds weighing on the economy, when Bank Rate does begin to rise, it is expected to do so more gradually and to a lower level than in recent cycles. This guidance is an expectation, not a promise. The actual path Bank Rate will follow over the next few years will depend on the economic circumstances.

Finally, given the prospects for future increases in Bank Rate, today the Committee is giving further guidance about the future path for the stock of assets held by the Bank under the Asset Purchase Facility. As described in the *Inflation Report*, the MPC's preference is to use Bank Rate as the active marginal instrument for monetary policy, and expects to maintain the stock of purchased assets at £375 billion until Bank Rate has reached a level from which it can be cut materially. The MPC currently judges that such a level of Bank Rate is around 2%. This further supplements the Committee's forward guidance framework, which has included general guidance on the APF, since it was originally announced in August 2013.

With that, we look forward to your questions.