Bank of England

Inflation Report Q&A
4th February 2016

Ed Conway, Sky News: Governor, the markets are now pricing in the possibility - about a 30% possibility - of there being a rate cut rather than a hike in the next year. You've said repeatedly that you feel that the next move is likely to be up rather than down. Do you still stand by that?

Mark Carney: Absolutely. The whole MPC stands by that. We've just released our forecast which, as I mentioned in my opening remarks, is conditioned on a market path of interest rates - and as I think you know, Ed, we use - as a convention, we use a 15-day average. So we didn't use last night's market path; we used the 15-day average up to finalising the forecast. And that 15-day average of the path of rates is rates sustained at current levels for a little while longer, and then gradually increasing father out over the horizon.

And in using that market forecast, based on our central view of the economy, we actually don't achieve our objective. Let me put it a different way. Inflation gets back to target, but then it rises above it. So there's not quite enough tightening in that market path that we used in order to do what the MPC is very clear - has been very clear about - is its objective, which is to return inflation to target in around two years and to keep it there - not to have an overshoot.

And the reason why that's particularly important is - right now we have this circumstance, which we've been going through for most of the past year - a little more than the past year - where we have these disinflationary or deflationary pressures coming in from abroad, and we have a gradual build in domestic costs. Eventually those disinflationary pressures from abroad will wane; the domestic cost pressures are likely to sustain, if not build, and we need to time this and balance the two to not just bring inflation back to target, but to do so sustainably.

So as I said, again, and we said in the Minutes and in the Monetary Policy Summary, and was clear in the letter to the Chancellor, the view is that more likely than not, the next move in rates is up, and that is consistent with the forecast, yes.

Joel Hills, ITV News: Governor, you've made attempts in the past to manage expectations to the likely path of interest rates. I wonder the degree to which you feel that perhaps your credibility has been damaged. When you give guidance on interest rates now, do you think the British public takes your guidance as serious as perhaps it did?

Mark Carney: Well I think - a couple of things. First, in terms of the guidance that we've given over the course of the last two and a half years, the first thing we did was to give guidance to help secure the recovery. And we've always given guidance that's state contingent, not time contingent. So we haven't given pre-set timetables for rate changes; we've said that these certain circumstances are either necessary conditions to even think about moving rates in order to achieve the inflation target.

So we gave guidance to help secure the recovery initially contingent that we wouldn't even begin to think about moving rates until unemployment had fallen to a certain level. That had an effect. We know that from surveys and we know that from the performance of the economy. The worst that can be said about that guidance is that more people came into work sooner than they might otherwise have done. So I don't know that we're going to make any apologies for that.

Secondly, we gave guidance in terms of the overall shape of the likely path of interest rates once they began to rise, and that's guidance we gave about two years ago - that rates, when they were increased, when the time came, would likely to rise to a limited extent and at a gradual pace. That guidance is now so familiar; it's part of the furniture. But it's helpful because we know from going around the country and talking to businesses and me with households, that people understand both that the likely orientation of rates is rates are going to increase as the expansion progresses, but they're not going to rocket as they had to do in the past, and that we'll manage this process appropriately.

We have given more guidance which is maybe of more interest to investors, guidance around the asset purchase facility and when - how we would use our various instruments of monetary policy. And that's useful guidance for those who have to worry about those things.

And then what we've been clear on, and I think I've been clear on - others have slight different weighting on different factors - are what are the broad indicators that influence me in terms of determining the stance of policy? And so when it was last summer where I set out a range of indicators around domestic costs, around core inflation, around momentum in the economy relative to the capacity of the economy. Those are the indicators that help inform when - at least in my opinion - it would become the right time to raise interest rates.

And by setting out those conditions - again, those conditions about the state of the economy, not about the calendar - conditions about the state of the economy, people can form a view on whether or not we're going to move policy. And what you saw, for example, over the course of the fall, as the global conditions deteriorated, as wage pressure grew a little less rapidly than previously and as core inflation picked up a little less rapidly - it picked up, but a little less rapidly than expected - market participants and others, yourself, began to push out the date of when we might raise interest rates.

That's exactly what we want to happen, because that's exactly the way we treat policy. We're not going to tie our hands ever to raise or adjust - raise interest rates or adjust policy in any way, shape or form, to a certain date. But we are trying to inform the markets - and most importantly, households and businesses - in this country what's likely to happen on rates.

And, I'll finish with this - in a situation where we have had - and we alternate with the United States here - but where we have had the strongest recovery in the advanced world now over the course of the last three years, and where we've been steadily - you know, people have been steadily finding work and the job market has been tightening - all in an environment of great global uncertainty and difficulty - in that environment, it is helpful, in my opinion, for households and businesses to recognise that it's more likely than not that rates are going to go up and to plan their affairs accordingly. Particularly since, while there's been tremendous progress, British households have done a great job in paying down debt, they are still relatively indebted, and we want to make sure that, the collective, we do not repeat the mistakes of the past of getting too indebted and then getting shocked - shocked - by movements on rates.

So, no, I don' think we have anything to explain on that front.

Ben Chu, The Independent: Governor, you and the MPC both make the point that low headline inflation seems to have been putting some downward pressure on wage growth, because people have moderated their wage demands. And you also talk about being watchful of the risk of second round effects. You don't use the D word in your remarks, but these are precisely the kind of deflationary dynamics that some have feared - domestically generated deflationary dynamics that some have pointed to in the past.

Although it's clearly not your central case, is it fair to say that these risks now loom a little larger in the Bank's calculations than they did previously?

Mark Carney: Well, I think what has changed - we're watchful for these issues, as we should be all the time and you're right to raise them. What has changed is that we've incorporated some of these dynamics into the forecast and so you do see a more modest pick-up in wages than previously, but still a notable pick-up in wages. And that's a product of the fact that we have a tight labour market, unemployment at 5.1%, more people employed as a proportion of the population since records began to be held, and many other signs of normalisation in the labour market. So we have a tight labour market and we think we have productivity growth starting to pick up which should support those wage gains.

But we have incorporated more persistence of - a slower pick-up, I should say - in terms of wages because of some of these effects.

Now, in terms of our watching, it's not just a question of looking at observed wages and running econometrics and adjusting the forecasts mechanically, we also go out and we use our agency network and talk to businesses across this country. And we precisely ask this question about the impact of low inflation on the wage-setting process. The answer from the agents and from the businesses and, you know, collectively and individually as we meet with them is - it's affecting them a bit, but it's not dominating. So I think we've got a balanced approach to this. It clearly is something we're watching and will continue to watch.

And I'll finish with this - we have to be conscious though that there are other factors that could be causing wages to pick up a little more slowly than expected. The composition of employment is one example. It's possible as well - open to the possibility, it's not our central view - it's possible there's a little more slack in the labour market than we think because the natural rate of unemployment could be lower; that's another possibility. And it could be just the lagged effects of slower productivity growth feeding through on wages.

So we're aware of all those things. You know as much as we do about the labour market. That's the point of bringing all these issues to the surface. Thanks.

David Smith, Sunday Times: Could I just follow up on that? Two things about wages. One is - do you expect the national living wage to have any impact on earnings growth in the coming months? And secondly, just to elaborate slightly on - when does watchfulness turn into monetary policy action? If wages were weak enough, might that bring a monetary policy response?

Mark Carney: Okay. On the first - in terms of the national living wage, we see - and our treatment of this has been not just to look at those who are directly affected by the national living wage, but also those who are close to those wages. In other words, our expectation is that businesses wouldn't just - I mean obviously they've got to abide by the national living wage, but if that bumps somebody from one pay grade up against somebody of the next pay grade, that there would also be some increase there as well.

Going across the numbers of people who are directly affected, indirectly affected by this, you get into the orders of magnitude of probably five or six million workers across this country, including the indirect effect, the second effect.

Overall, we see the net impact of this on wages and inflation of about 10 basis points, ultimately per annum, moving through the forecast. So it's something, but it's not - it's something and it's incorporated into the forecast.

I should say - I should recognise, and as you would know David, that there are certain sectors for which this is a much bigger issue, given the proportion of people who are paid at or around the minimum wage. And we do recognise that, so there will be some distributional things there.

In terms of watchfulness to action, I mean, the action part is determined by all the factors that affect inflation. And so we have to put that into the context of that. We are conscious - our basic expectation, as you've seen - and it's taking a little longer, but it's directionally happening - our basic expectation is that domestic costs are going to continue to grow, to pick up, consistent with that inflation target and that that will be the dominant factor determining inflation in the medium term.

This is the point where I have to say - of course there will be other shocks that happen from time to time, and we'll have to react to those shocks when they do come. I do have to say that, and that is reality. But - so I wouldn't isolate this as - it's important that we surface it, it's important that we've incorporated it into our forecast, but I wouldn't give it a sort of totemic status that it is the determinant of the path of policy. That would be overweighting both what's happened and the reality of the inflation process, which is - there are many factors that determine inflation.

Emily Cadman, Financial Times: Governor, turning to credit growth and household expectations, if households take your guidance that rates are staying where they are for a considerable amount of time and start to pile into credit, would you be worried and, if so, at what level would you start to get worried?

Mark Carney: Well, first thing is the guidance is - I mean, we have a forecast based on a certain set of dynamics. We have guidance around certain indicators that would potentially shift the stance of policy - I won't go through them again. That's the guidance. It's not - you used the time - it's not what the guidance is, okay. So, just - I feel I have to reinforce that.

In terms of credit growth, from the MPC's perspective, we're obviously focused on the strength of domestic consumption; it is the core, as is almost always the case, the core driver of growth in the economy. We do see the savings rate coming down over the - as our expectation, the savings rate would come down over the course of the forecast, that there would be credit growth in aggregate that is around or slightly above the pace of nominal GDP growth. But that's in aggregate. You have much sharper consumer credit growth, which is principally being driven by growth in auto sales, hire purchase arrangements for autos at present.

In terms of - so, we're interested in it, but we're interested in it in the round in terms of the impact on the balance of supply and demand and the outlook for inflation. More broadly, at the Bank, obviously The FPC takes a direct interest in this to ensure that risks to financial stability aren't increasing.

And just - I'll finish with this - one of the things we do is we meet from time to time, the MPC and the FPC, on issues of mutual interest. This is one of them, and in fact the box in the Inflation Report, which we can talk about, goes through some of these dynamics. And that is something which captures the discussion which the FPC and the MPC had. The assignment of responsibility starts with the FPC, though, in terms of the vulnerabilities with monetary policy being the last line of defence, if we felt there were an issue.

But I think, as you would have seen in the last Financial Stability Report of the FPC in December, in terms of the top issues, this is not the top issue - one of the top issues for the FPC.

Kamal Ahmed, BBC: Governor, it now looks clear that the government is very keen on a referendum on Britain remaining in or leaving the European Union this year. How is that playing into the MPC's considerations about the trajectory of growth for the UK economy? And in particular, could you give us the thoughts of the MPC and yourself about the strength or otherwise of sterling or the impact of sterling if Britain were to leave the European Union?

Mark Carney: Well, in terms of the way we conduct our forecast around political events - major political events - whether it's a general election or a Scottish Referendum or the EU Referendum, we assume the status quo. And you wouldn't expect us to speculate on outcomes or alternative projections associated with different outcomes.

Now, that doesn't mean that these political events don't affect the forecast. But the way they affect the forecast is through how they affect asset prices including in the exchange rate, and how they affect household and business confidence.

So what we do in the forecast obviously is we take asset prices where they are and we take those confidence indicators, which at present for the latter - there's not yet a big risk premium built into business and household confidence around the Referendum. We do see in the exchange rate market, and it's observed in the Report, that there has been some minor protection, if you will, around the Referendum. You see it in the skews in options markets around sterling and particularly around cable, that have moved notably since December, consistent with the existence of a Referendum.

We don't have a forecast for sterling - period. And we certainly don't have a forecast for sterling in the event of a political event on which we're not conditioning our forecast. So, I'll leave it at that.

Larry Elliott, The Guardian: Governor, earlier you alluded to your Lincoln speech where you said that the Rate decision would come into sharper focus around the turn of the year, clearly the picture's got a bit blurred around the turn of the year. I just wondered when you now think the Rate decision's going to come back into sharper focus again. Because if guidance is going to mean anything, people have to have some idea about what the Bank's thinking is.

Mark Carney: You know, Larry, I think the point of that turn of phrase, which was part of a speech that laid out a whole framework in terms of the dynamics of the inflation process and those elements of - those indicators of inflation; aside from having a chunk of history about the Magna Carta, but we'll set that to one side - the point of that was to give a sense of how those dynamics would affect inflation and how we would potentially react. And given our forecast at the time - given the Bank's forecast at the time - when those indicators, based on that forecast and the forecast that came out in August, when those indicators would be in the region where that decision would get more difficult - okay - come into sharper relief - become more difficult or become quite easy.

The decision came into sharper relief - from my perspective - came into sharper relief, it was quite an easy decision. The decision is whether or not to raise interest rates; it was an easy decision not to raise interest rates. You know, now is not the time to raise interest rates because we haven't had sufficient, in my judgement, and for various different reasons the judgement of everyone else on the Monetary Policy Committee, we haven't had sufficient build in domestic cost growth. The economy is using up slack, but there's still a bit more to be done there. And core inflation has - while it's picked up - it hasn't picked up quite enough, and that's a product probably of the persistence of exchange rate paths and a few other factors.

But the value of that - the value of that guidance is to give a sense of how we will react to events. Everyone in this room will have a slightly different view, in some cases markedly different view, of the outlook for the economy. To the extent we're telling you what influence, how we would react to those states of the economy, you can form a view on interest rates and we can give a general sense of where things are likely to happen.

We have a view - our forecast today in effect says that we think that if our central view of the outlook for the economy comes to pass, we will need to raise interest rates to a limited degree and at a gradual pace in order to keep inflation - not just get it to target, but to keep it there.

If you have a radically different view of the economy, you can form a different perspective on the path of rates. What we can assure you is that, when it comes time to make each decision, we won't be bound by something we've said in the past; we'll make a decision based on achieving that target. Thanks.

Paul Mason, Channel 4 News: I mean, however you see it, the market sees monetary policy of this institution as Rates, QE plus signalling. And therefore guidance is a kind of euphemism in this sense, isn't it? What has happened during your tenure as the Governor is that you have, through signalling, twice loosened policy. Now that is welcome to those of us who are worried about the downside risk, and in particular the financial market risks outlined in the Inflation Report box that the FPC and the MPC have been concerned about.

But the question becomes then - why not use more signalling because the signalling has been effective? In other words, what is the substance of what you effectively did in that last speech?

Mark Carney: Well, let me say a few things. One is - the substance of what I said in the last speech was to give an accounting of how the economy had performed relative to some criteria that I had set out six months earlier. And you can judge how well it's accounted for, but - and by giving that accounting, I think that updates and reinforces and flushes out, if you will, my reaction function - to use the technical term - how I would be expected to react, depending on how the economy performs.

The second thing is that the package of information we release four times a year in effect provides guidance, provides a perspective, provides more information about the current reaction function of the MPC as a whole, not just myself.

And the third things is - you know, in terms of the overall performance of - if you look at short rates in this economy at a time of great volatility - I mean, it is not an understatement to say there is, you know, tremendous volatility in the global economy, more broadly in financial markets and there is not volatility, but there has been quite a bit of uncertainty in terms of the real economy, particularly around the supply side - a point that Ben Broadbent has made far more eloquently and to much a better grounding than I will. At a time of all that, if you look at the volatility of short sterling, if you look at one year forward volatility, it's half of what it was in the 10 years preceding my arrival at this institution.

It has come down - now you do want volatility, because there are going to be shocks and you don't know. But we have provided guidance, we have provided frameworks, we have provided more information. We are obviously constantly, as a Committee and as individuals, looking for better ways to provide that information. But there has been a movement down. There always will be volatility in financial markets; there always will be events that move around the likely path of monetary policy, whether it's in the UK, the US, the euro area, China. And we have to react to it. All we can do is inform as best as we can, not just the financial markets but in a way that's digestible - very importantly, in my view - for the general public, those who we really serve - all of us really serve - a way that they can understand both likely paths and what can change those paths.

Phil Aldrick, The Times: There seems to be a contradiction in the Inflation Report that I hope you could resolve.

Mark Carney: Well I'm sure Dr Broadbent would be very happy to do that.

Phil Aldrick, The Times: Ben, one for you then. But in it you talk about spare capacity being eliminated by the end of this year, and then if you look at the projections off the market yield curve which obviously in the Report isn't as severe as it is today, that seems to suggest that the first lift-off wouldn't be until halfway through 2017 at the earliest. Yet elimination of spare capacity by the end of this year would suggest that you'd get interest rate rises much earlier. So which is it? Should we be looking at spare capacity and ignoring the yield curve?

Mark Carney: No, I am going to pass to Ben, but this is a very welcome question because this is an extremely important point to understand.

Ben Broadbent: Well the main answer is there's absolutely no mechanical link between the level of the output gap and the appropriate level of interest rate. So there is no contradiction at all. And indeed, even to the extent there was a reasonable correlation prior to the financial crisis - even then, it wasn't the only the thing; inflation mattered, obviously, inflation expectations and so forth. But I would say - not just since the financial crisis but even before, there have been big variations, generally declines, in what you might call the neutral rate of interest. And we have to take those into account.

You know, we could have had a zero output gap 20 years ago and the level of interest rates, the appropriate level of interest rates, would have been completely different - indeed it was completely different. So I think it's a mistake to imagine there's some simple mechanical link between a single indicator, whether indeed that's wage growth or the output gap, and interest rates. And if there were then we wouldn't have to write these reports and sit there and think about lots of things, not just one.

Phil Aldrick, The Times: There wasn't fuzzy guidance based on the output gap - that was poor guidance part two because a lot of it was spare capacity anyway.

Ben Broadbent: Not at all. I'll reiterate what the Governor said a moment ago. Read first of all what the guidance actually said okay. It said that the Committee judges that the path of interest rates that is likely to be necessary to meet our objectives will be shallower than it was in the past and end up at a lower level. That's what it said. It said no more than that. It certainly said nothing time specific; it didn't introduce the output gap quotes. The earlier phase had unemployment in it, but that wasn't a sufficient condition for rate changes either, it was just a necessary condition. So I just don't think that's right as a premise.

Hugo Duncan, Daily Mail: Going back to Brexit and the Referendum, if I may, and particularly on business spending and investment intentions. The minutes note that the referendum presents a downside risk in the near term to business spending, yet goes on to say that intentions had not softened significantly thus far. I'm just wondering how real you think this risk is and whether you actually think that possibly, as is the case with the

Scottish Referendum, businesses will just carry on investing through the period to the Referendum and beyond?

Mark Carney: Well we'll have to see, Hugo. And it will be a product of how the campaign unfolds, and we will see. In terms of what we assume, based on the existing surveys and the relationship with those surveys to the path of business investment, and based on some fundamental factors - very high return on capital, the fact that there's relatively little, in our judgement relatively little spare capacity in the economy, we expect, as you've noted, a pretty smart rate of growth of business investment certainly relative to historic growth rates. I think growth rates in the 6% per annum area versus kind of 2.5% per annum historic growth rates.

We'll update that as events transpire, but that is our base case expectation. And as I said earlier to an earlier question, we're not conducting a hypothetical exercise of - we're not predicting an outcome, we're using our straight convention which we use for every major political event, whether it's a general election or Scottish referendum in that example, of just assuming the status quo as the base case, as the only case.

Hugo Duncan, Daily Mail: You don't appear too concerned about business investment taking a major hit between now and a referendum whether -

Mark Carney: Well we haven't picked it up - we're being, if you will, mechanical, not predictive, with respect to this issue because to be otherwise - we don't have a basis to be otherwise but also, let's be honest, to be otherwise would be to potentially wade into a political debate where we don't belong.

Scott Hamilton, Bloomberg News: Governor, the MPC has today emphasised the near term downside risks a lot, which obviously has pushed back the prospect for an interest rate increase, but might the medium term risks, which makes now inflation come back to the target quicker, mean - make later means less gradual, faster rate increases when they do come, especially if these downside risks don't materialise?

Mark Carney: In terms of the path with which we set policy, we look at the mode as opposed to the mean. So we haven't incorporated the downside risks into our central projection. So we're looking at the most likely measured as the mode, as opposed to the mean; we've always done that by convention.

Are there upside risks to inflation? Yes, there are upside risks to inflation. We talked earlier - and it was useful to have the discussion - but we talked about this assumption that wage growth is shallower, the pickup in wage growth is shallower than we previously had expected because of some sort of - some elements of second round effects, early elements of second round effects. That may not transpire. It is possible there is a variety of scenarios one could have in terms of a better outcome for global growth, more momentum domestically. And any of those, less spare capacity than we currently think, could result in higher cost growth and a tighter path of policy.

Now to go back to the earlier discussion, Larry's and other people's questions, by laying out some of the elements that would influence our reaction to that, if you start to see those things develop, if, you know, labour costs pick up more smartly, if core inflation - if there's less pass through from the past depreciation of sterling, for example, and core inflation rises more rapidly, or just the economy grows more rapidly than we expect, well then all things being equal one would expect that policy would be tighter both in terms of timing and amplitude. But we'll see and we can't do more than that.

Szu Chan, The Telegraph: Just to get back to the flip side of the scenario that you presented and the risk that low inflation becomes entrenched in wage expectations, etc., I know you just said that you can't look at just one data point alone, you look at a range of factors, but when does low inflation start to become a worry for the Committee and what is your message for employees and employers as they start to negotiate the wage round for this year?

Mark Carney: I'll ask Ben to …

Ben Broadbent: Just to reiterate what the Governor has said. What we did in the forecast is make a small adjustment for what we perceive probably as a small effect, negative, but not that big of low rates of inflation on actual pay settlements.

Now the pay data themselves are pretty volatile, there are all sorts of things that influence them so it's not possible to say with certainty this is what's happening. We've made some allowance for it and therefore have a slower rate of growth of wages and unit costs certainly through the course of this year. So I don't think we should overemphasise the risks of this.

Wage growth has picked up; unit cost growth has picked up on any measure. There's a chart I can point you to showing that. Some of the fears, great fears were expressed in this room a year ago about deflation and people deferring consumption, I remember a whole host of questions about that simply haven't come true.

So it is something we watch. We have obviously a responsibility to watch inflation expectations, how they're influencing wages. It's a sort of core part of the job of the monetary policy maker. But I don't think there's any simple level at which it suddenly switches to becoming the overriding concern.

Geoff Cutmore, CNBC: Governor, I wonder if I could ask you to address just the international context a little bit more here. Clearly from the Minutes, the Committee spent a lot of time thinking about the volatility in risky assets at the moment, concerns around the slowing growth in China and emerging markets, the risk of liquidity problems in capital markets particularly secondary bond markets. I wonder to what extent the Committee is taking this into consideration as it shapes policy, rather than the domestic context, given that you've actually said there is quite a lot that's robust in the UK right now? So are you making policy for the international context rather than the domestic at this stage, and if so, what do you fear and what do the markets fear?

Mark Carney: Thanks, Geoff. I mean the first thing I'll say is, as I said at the outset, this is one of the most open economies in the world and it has the leading global financial centre housed in it. So international factors, the trajectory of the global economy, global financial conditions are very important for the UK. And the deterioration in the global outlook has had an impact on our forecast. It's something that we have been concerned about for some time. We've tended to have a lower global forecast than the IMF, for example, and others. We have a lower - that's again the case with this forecast and we do see some downside risk.

I would say that in terms of global dynamics, if you step back in terms of financial market dynamics, at the core of these is a - I believe, we believe, that they stem from concerns about the growth trajectories in China and major emerging markets and the potential amplification of that to advanced economies. And questions in terms of the ability of policy to respond to those concerns.

The distinction we would make is that we have a very different - we're in a very different position - as I tried to do at the outset than we were seven years ago, in terms of both the health of the system, of the financial system, the improvement in balance sheets corporate and personal and the amount of momentum, sustainable momentum, that is there in the economy. So, Geoff, we obviously have to blend the two.

The last point I would make and actually, Minouche, ask you to just amplify on this. In terms of market liquidity, I mean let me cite it for the Monetary Policy Committee first and then Minouche can talk more generally about what's going on there. In terms of influencing monetary policy, we would need to see a persistent shift in market liquidity that would create a permanent wedge or a persistent wedge, if you will, in terms of borrowing costs that flowed through to the United Kingdom. And all things being equal that would influence the stance of monetary policy.

I would note that for a long time we have been saying as a Committee that one of the many reasons why we expect the neutral interest rate of which Ben spoke to rise to a limited extent is that we expect that wedge to come in as a consequence of a series of changes that have been made. But I wonder, Minouche, if you just want to expand for a minute on some of the drivers of this market liquidity and what we're doing more broadly as a Bank on it, because it's an important issue.

Minouche Shafik: Well I mean, as you well know there are concerns about market liquidity partly attributed to changes in regulation on the leverage ratio, but also around structural changes in the way markets operate, particularly the rise in high frequency trading and the fact that the structure of some of these markets has changed. Now the FPC has an extensive stream of work on various aspects of this, and we are paying quite a lot of attention to changes in market liquidity and how that might affect markets in the UK.

Mario Blascak,
World Business Press Online: Governor we saw you revising down the unemployment forecast below the 5% equilibrium rate. At the same time, how low do you think the unemployment in the UK should fall to put the upward pressure on the closely watched earnings or wages growth? And in what other segments of the labour market do you see the slack remaining?

Mark Carney: We did an assessment of the overall degree of slack in the economy; we just had a periodic so-called supply stock take. And so we looked pretty hard at the labour market as a whole. We made a couple of determinations in that. One is that we took down a bit our expectations around participation, the participation rate in the economy. We had had quite a relatively high level. And we also took a signal from recent behaviour in the labour market in terms of hours worked of individuals because we're seeing a normalisation in patterns. People had been taking less leave than historic or than on offer, and there's been some normalisation of that and to an extent that it mattered.

In both respects there is still some marginal slack there but very limited, as we indicated. In November we felt there was around a half a percentage point of slack. We now think it's less than that, there's a little more than zero but not so much that it can't be eliminated over the course of the year.

And in fact, as you rightly point out, over the course of the forecast we expect on average that the unemployment rate would fall below 5%, below that current estimate of the natural rate.

Now we will be very interested to see, as everyone will, in terms of how wage costs evolve, if this comes to pass, and also how job matching and job churn and other indicators evolve. There are reasonable arguments on both sides of this to suggest that the natural rate or the NAIRU - different concept but similar - has actually fallen in this economy over the course of the last several years because of a series of reforms to labour markets and the nature of work and other factors. We're alive to that possibility. For the purposes of this forecast we've made a judgement to which we all adhere, that we've kept that assumption at 5%. But we do expect that the actual outturn will be below that. We'll see what happens to a variety of other indicators and we'll update as appropriate. Thanks.

Harry Daniels, Live Squawk: Just with regards to your tenure and when it finishes, if we look at the market forecasts at the moment, the first Rate move is seen for mid-2018 now, so I'm pricing up a 30% chance of a Rate cut by the end of your tenure. Are you worried that you could become the first Governor since I think 1944 to 1949, Thomas Catto, to leave rates unchanged for his whole tenure?

Mark Carney: Well no, I think what's important to all of us - and we had a colleague on the MPC, David Miles, who went through two terms on the MPC without raising interest rates. He did a lot of other things - quantitative easing - other range of work and took judgements every single meeting of the right stance of policy. I think the important thing for all of us is that we set policy in a way that maximises the likelihood that we're going to achieve our objectives, and that's how ultimately we're going to be judged.

As whether it's monetary policy, or even more so with respect to financial stability policy or supervisory policy, you can only really be assessed quite some time after your term has finished, so it's not about action for action's sake; it's about the right stance of policy. And with this institution and its broad range of powers, it's a huge suite of policies that we have to, through the various committees in which I participate, to try to get right to ensure in the end what we're delivering is monetary and financial stability, and in that way supporting strong, sustainable and balanced growth in the United Kingdom. And that's how we'll be judged.

Yvonne Esterházy, German Businessweek: A follow up to the EU referendum, it looks increasingly likely that it will happen in a few months' time now, and I was just wondering - apart from forecasts and investments where you don't want to say anything - but could you elaborate a little bit on your plans, your contingency plans within the Bank, for this big event? Clearly the markets are showing some concern and it would be a shock if there were a vote for Brexit.

Mark Carney: There's a very long list of things around the EU referendum about which we don't want to say anything. And with respect to contingency plans, of course we have contingency plans around potential market events, potential shocks, both those that we can identify and generic ones. And the EU referendum falls into the camp of an identifiable one.

As always is the case, it serves no one to talk at length about the specifics of those contingency plans in advance, and so we'll adhere to that convention. What we do have a commitment to do though is after events have passed, as appropriate, we do disclose what we had done, and that was the case with the Scottish referendum where we provided a record of the discussions at the Financial Policy Committee around contingency planning for the Scottish referendum, and you can expect something similar.

Sam Nussey, Nikkei: Governor, with the BOJ having joined the ECB Switzerland, Sweden, Denmark, and having used negative rates, do you see negative rates as part of the BOE's arsenal and could you envisage a situation in which they would be used?

Mark Carney: Well let me start that discussion we had as the MPC was whether now was the right time to raise interest rates. And the judgement, as you've seen nine to nil, was that now was not the right time to raise interest rates, but we had a forecast - we have a forecast - which requires some increases in interest rates in order to sustainably achieve the inflation target. That's the first point.

The second point is that we have provided guidance on the use of Bank Rate and where we think the effect of lower bound is on Bank Rate. We updated that guidance in the spring of last year, that we felt that time had moved on from 2009/10 and because of the improvement in the banking system, particularly the building society sector, that we could lower Bank Rate further. So we're not at the effect of lower bound at this stage.

As an institution, we will always review our facilities from time to time and refresh them as appropriate. As the Monetary Policy Committee, we have not had discussions about potentially using those instruments, for the obvious reason of the orientation of policy is in a different direction.

One of the advantages of a day like today - and I know one of the disadvantages of a day like today is you all had to come in at nine in the morning and get locked up in the sub vault and probably treated quite poorly and had to read a bunch of documents, but in those documents are included the Minutes of the Monetary Policy meetings. So you know in real time that we didn't discuss that possibility at the meeting, and the orientation was, as I say, in a different direction. So you will know if that point comes as even a conceptual discussion. Thanks.

Chris Papadopoullos, City AM: Given the compositional things that are impacting productivity and the average weekly earnings figures, why are they being given so much attention? As in why are people so worried that they're low given the compositional effects that are keeping them low?

Mark Carney: I'm going to pass to Ben to speak to this, but I'll just say on a high level - I mean obviously it's important for those who are affected by it, those who are in those positions. And it's important that, if I can put it this way, we're not misled by composite. We have to understand why there are certain dynamics in terms of wages and productivity, and not misinterpret those dynamics, because if it weren't compositional effects, it could be higher slack, it could be this persistent second round effect, it could be other factors that are dampening on wages.

So it's important to understand, because it's a material dynamic in the economy in our view. And as I say, from a policy perspective, a compositional effect is basically awash in terms of the impact on policy, whereas these other effects can influence the path of the policy. But Ben, do you want to …?

Ben Broadbent: Yeah I think this is an important point to remember the number of things that can affect wage growth, even the very sort of concept of what wage growth is. So the AWE does not represent the pay growth of some representative individual. And you're right that if the composition of the workforce changes, indeed if average hours change, that will affect AWE, even if the hourly pay of no single individual changes. And you can see - there's a chart on the top of page 25 where you can see our estimates of those compositional effects; they've been pulling down on wage growth. At other times they were pushing up. Average hours have also been pulling down on AWE growth, at the same time in addition to this.

But as the Governor pointed out, I think one important point to bear in mind is that our broad assessment is that these have similar effects on AWE growth and on per capita productivity growth, and that's one of the reasons we pay quite a lot of attention to unit costs which is the ratio of the two. There's no first order impact on those.

And you know it's worth bearing in mind, although we'll have dipped down a little on the fourth quarter of the year, you look - flip forward to page 29 you can see that unit costs have been accelerating, that growth rate has been picking up. So it is an important point you've made and we certainly do our best to take it into account.

Jenny Scott: That's all we've got time for. Thank you very much everyone.

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