

BANK OF ENGLAND  
LONDON EC2R 8AH

6 August 2009

The Rt Hon Alistair Darling  
Chancellor of the Exchequer  
HM Treasury  
1 Horse Guards Road  
London  
SW1A 2HQ

Dear Chancellor,

We discussed over the past month the possibility that the Monetary Policy Committee would decide at its August meeting that it wished to increase the scale of its asset purchase programme above the £150 billion authorised in your letter of 3 March. At its meeting today, the Committee judged that, in order to keep inflation on track to meet the 2% inflation target over the medium term, the programme of asset purchases should be increased to a total of £175 billion and Bank Rate should be maintained at 0.5%.

The context for that decision can be summarised as follows. The world economy remains in recession, though there have been increasing signs that output in the UK's main export markets is stabilising. Financial market strains have eased and banks' funding conditions have improved a little, although financial conditions remain fragile. Household and business confidence has picked up, albeit from the very low levels experienced in the wake of the financial crisis last autumn.

In the United Kingdom, the recession appears to have been deeper than previously thought. GDP fell further in the second quarter of 2009. But the pace of contraction has moderated and business surveys suggest that the trough in output is close at hand. Underlying broad money growth has picked up since the end of last year but remains weak. And though there are signs that credit conditions may have started to ease, lending to business has fallen and spreads on bank loans remain elevated.

CPI inflation fell back to 1.8% in June, a little below the 2% target. The decline in recent months was mainly accounted for by lower food and energy inflation, though past falls in sterling continued to put upward pressure on inflation. The margin of spare capacity in the economy increased further and pay growth remained weak.

The future evolution of output and inflation will be determined by the balance of two sets of forces. On the one hand, there is a considerable stimulus still working through from the easing in monetary and fiscal policy and the past depreciation of sterling. On the other hand, the need for banks to continue repairing their balance sheets is likely to restrict the availability of credit, and past falls in asset prices and high levels of debt may weigh on spending. While some recovery in output growth is in prospect, the margin of spare capacity in the economy is likely to continue to grow for some while yet, bearing down on inflation in the medium term. But the recession and the restricted availability of credit are also likely to impact adversely on the supply capacity of the economy, moderating the increase in economic slack.

I am therefore requesting the authority to use the Asset Purchase Facility to purchase assets totalling £175 billion. The structure and operation of the Asset Purchase Facility would otherwise be unchanged from that described in your letter of 3 March.

I am copying this letter to The Rt Hon John McFall MP, Chairman of the Treasury Committee.

Yours sincerely

A handwritten signature in black ink, appearing to read 'R. King', is centered on the page. The signature is written in a cursive style with a large, looping initial 'R'.