Bank of England

Monetary Policy Report

Monetary Policy Committee
February 2025

Monetary policy at the Bank of England

The objectives of monetary policy

The Bank's Monetary Policy Committee (MPC) sets monetary policy to keep inflation low and stable, which supports growth and jobs. Subject to maintaining price stability, the MPC is also required to support the Government's economic policy.

The Government has set the MPC a target for the 12-month increase in the Consumer Prices Index of 2%.

The 2% inflation target is symmetric and applies at all times.

The MPC's **remit** recognises, however, that the actual inflation rate will depart from its target as a result of shocks and disturbances, and that attempts to keep inflation at target in these circumstances may cause undesirable volatility in output. In exceptional circumstances, the appropriate horizon for returning inflation to target can vary. The MPC will communicate how and when it intends to return inflation to the target.

The instruments of monetary policy

The MPC currently uses two main monetary policy tools. First, we set the interest rate that banks and building societies earn on deposits, or 'reserves', placed with the Bank of England – this is Bank Rate. Second, we can buy government and corporate bonds, financed by the issuance of central bank reserves – this is asset purchases or quantitative easing.

The Monetary Policy Report

The MPC is committed to clear, transparent communication. The Monetary Policy Report (MPR) is a key part of that. It allows the MPC to share its thinking and explain the reasons for its decisions.

The Report is produced quarterly by Bank staff under the guidance of the members of the MPC.

This Report has been prepared and published by the Bank of England in accordance with section 18 of the Bank of England Act 1998.

The Monetary Policy Committee

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- Sarah Breeden
- Swati Dhingra
- Megan Greene
- Clare Lombardelli
- Catherine L Mann
- Huw Pill
- Dave Ramsden
- Alan Taylor

PowerPoint™ versions of the Monetary Policy Report charts and Excel spreadsheets of the data underlying most of them are available at **www.bankofengland.co.uk/monetary-policy-report/2025/february-2025**.

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Monetary Policy Summary

The Monetary Policy Committee (MPC) sets monetary policy to meet the 2% inflation target, and in a way that helps to sustain growth and employment. The MPC adopts a medium-term and forward-looking approach to determine the monetary stance required to achieve the inflation target sustainably.

At its meeting ending on 5 February 2025, the MPC voted by a majority of 7–2 to reduce Bank Rate by 0.25 percentage points, to 4.5%. Two members preferred to reduce Bank Rate by 0.5 percentage points, to 4.25%.

There has been substantial progress on disinflation over the past two years, as previous external shocks have receded, and as the restrictive stance of monetary policy has curbed second-round effects and stabilised longer-term inflation expectations. That progress has allowed the MPC to withdraw gradually some degree of policy restraint, while maintaining Bank Rate in restrictive territory so as to continue to squeeze out persistent inflationary pressures.

CPI inflation was 2.5% in 2024 Q4. Domestic inflationary pressures are moderating, but they remain somewhat elevated, and some indicators have eased more slowly than expected. Higher global energy costs and regulated price changes are expected to push up headline CPI inflation to 3.7% in 2025 Q3, even as underlying domestic inflationary pressures are expected to wane further. While CPI inflation is expected to fall back to around the 2% target thereafter, the Committee will pay close attention to any consequent signs of more lasting inflationary pressures.

GDP growth has been weaker than expected at the time of the November Monetary Policy Report, and indicators of business and consumer confidence have declined. GDP growth is expected to pick up from the middle of this year. The labour market has continued to ease and is judged to be broadly in balance. Productivity growth has been weaker than previously estimated, and the Committee judges that growth in the supply capacity of the economy has weakened. As a result, the recent slowdown in demand is judged to have led to only a small margin of slack opening up.

In support of returning inflation sustainably to the 2% target, the Committee judges that there has been sufficient progress on disinflation in domestic prices and wages to reduce Bank Rate to 4.5% at this meeting.

Based on the Committee’s evolving view of the medium-term outlook for inflation, a gradual and careful approach to the further withdrawal of monetary policy restraint is appropriate.

In addition to the risks around inflation persistence, there are also uncertainties around the trajectories of both demand and supply in the economy that could have implications for monetary policy. Should there be greater or longer-lasting weakness in demand relative to supply, this could push down on inflationary pressures, warranting a less restrictive path of Bank Rate. If there were to be more constrained supply relative to demand, this could sustain domestic price and wage pressures, consistent with a relatively tighter monetary policy path.

The Committee will continue to monitor closely the risks of inflation persistence and what the evolving evidence may reveal about the balance between aggregate supply and demand in the economy. Monetary policy will need to continue to remain restrictive for sufficiently long until the risks to inflation returning sustainably to the 2% target in the medium term have dissipated further. The Committee will decide the appropriate degree of monetary policy restrictiveness at each meeting.

1: The economic outlook

Progress on disinflation in domestic price and wage pressures has generally continued. In support of returning CPI inflation sustainably to the 2% target, the Committee is maintaining its focus on the persistence of inflationary pressures in the medium term. It also notes the significant uncertainties around the current and prospective balance of demand and supply in the economy.

CPI inflation was 2.5% in 2024 Q4, close to expectations at the time of the November Report. CPI inflation excluding energy has continued to decline over the past year reaching around 3¼% in the second half of 2024 compared with its peak of nearly 8½% in mid-2023 (Chart 1.1). In large part reflecting recent developments in global energy costs and regulated prices, headline CPI inflation is expected to rise quite sharply in the near term, to 3.7% in 2025 Q3. But the MPC judges that this pickup in headline inflation will not lead to additional second-round effects on underlying domestic inflationary pressures in the forecast (Key judgement 1).

The recent slowdown in demand is judged to have led to only a small margin of slack opening up, as growth in the supply capacity of the economy appears to have been weakening over the past year. Within potential supply, labour supply growth has been strong and potential productivity appears to have been very weak. The MPC considers that the labour market is broadly in balance.

In the February forecast, the margin of excess supply is expected to widen over the next couple of years, to around ¾% of potential GDP, before narrowing slightly by the end of the forecast period (Key judgement 2). The unemployment rate is projected to rise gradually to around 4¾%. Annual potential supply growth is projected to rise to around 1½% in the medium term, which supports GDP growth picking up from the middle of this year, to over 1½% by the end of the forecast period.

There are considerable risks around the path of excess supply in the economy. The Committee has considered carefully the impact of alternative assumptions for the degree to which recent developments in activity may reflect greater weakness in demand relative to supply. It has also considered the more material risk that weakness in the labour market and other uncertainties in the global and UK economies could push down on demand in a longer-lasting way over the forecast period. In the other direction, if there were to be more constrained supply relative to demand, this could sustain domestic price and wage pressures.

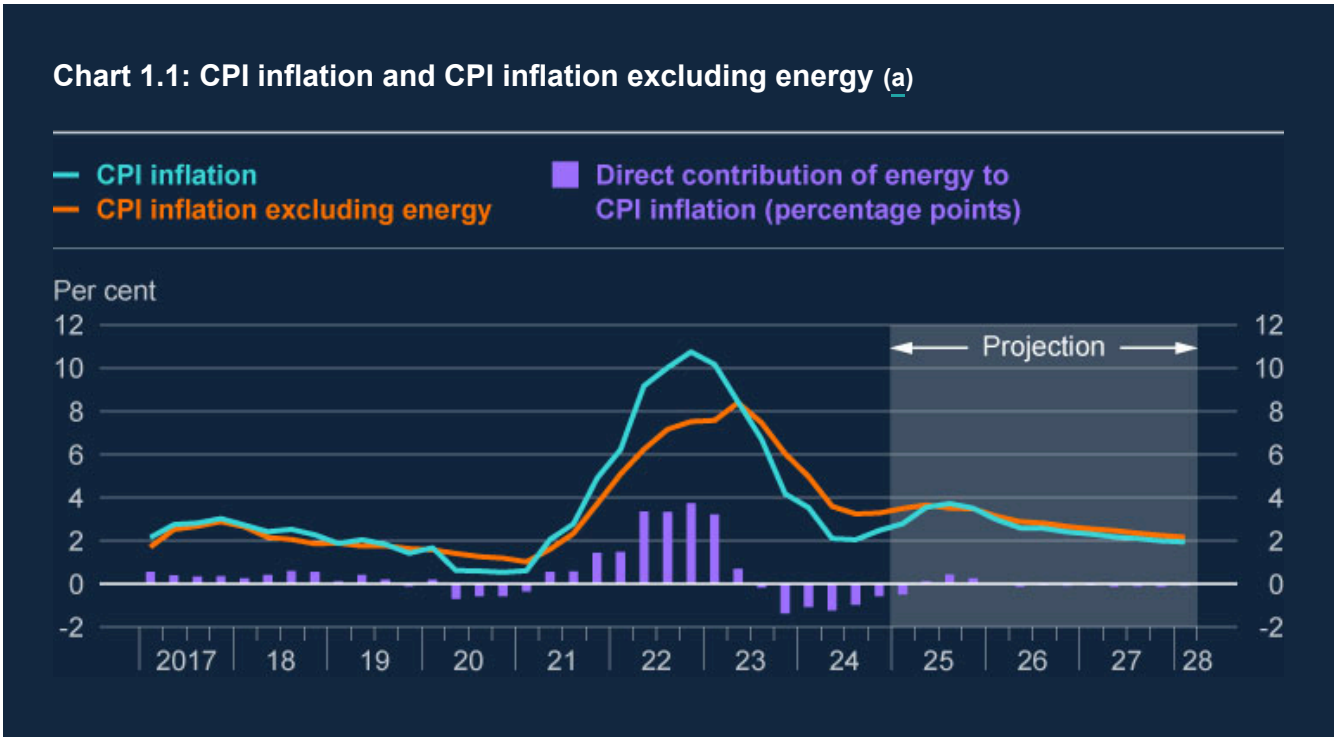
Overall, the Committee judges that, while there have been important developments since November, the forecast remains consistent with the second case that it has identified previously regarding the evolution of the remaining persistent inflationary pressures. That is, conditioned on the market path of interest rates, the emerging margin of slack in the economy acts against some continuing second-round effects in domestic prices and wages in order for CPI inflation to fall back to around the 2% target in the medium term (Key judgement 3).

Table 1.A: Forecast summary (a) (b)

	2025 Q1	2026 Q1	2027 Q1	2028 Q1
GDP (c)	0.4 (1.4)	1.5 (1.6)	1.3 (1.1)	1.8
CPI inflation (d)	2.8 (2.4)	3 (2.6)	2.3 (2.1)	1.9
Unemployment rate (e)	4.5 (4.1)	4.5 (4.2)	4.8 (4.3)	4.8
Excess supply/**Excess demand** (f)	-¼ (0)	-½ (-¼)	-¾ (-½)	-¼
Bank Rate (g)	4.6 (4.4)	4.2 (3.7)	4.1 (3.6)	4

(a) Figures in parentheses show the corresponding projections in the November 2024 Monetary Policy Report.
(b) The numbers shown in this table are conditioned on the assumptions described in Section 1.1.
(c) Four-quarter growth in real GDP.
(d) Four-quarter inflation rate.
(e) International Labour Organization (ILO) definition of unemployment. Although LFS unemployment data have been reinstated by the ONS, they are badged as official statistics in development and the LFS continues to suffer from very low response rates, which can introduce volatility and potentially non-response bias (see Box D in the **May 2024 Monetary Policy Report**).
(f) Per cent of potential GDP. A negative figure implies output is below potential and a positive that it is above.
(g) Per cent. The path for Bank Rate implied by forward market interest rates. The curves are based on overnight index swap rates.

Chart 1.1: CPI inflation and CPI inflation excluding energy (a)



Sources: Bloomberg Finance L.P., ONS and Bank calculations.

(a) Energy prices include fuels and lubricants, electricity, gas and other fuels.

1.1: The conditioning assumptions underlying the MPC's projections

As set out in Table 1.B, the MPC's February projections are conditioned on:

- The paths for policy rates in advanced economies implied by financial markets, as captured in the 15 working day averages of forward interest rates to 28 January (Chart 2.6). The market-implied path for Bank Rate underpinning the February projections declines to around 4% by the end of the forecast period, higher than in the November Report.
- A path for the sterling effective exchange rate index that is around 2¼% lower compared with the November Report. The exchange rate depreciates slightly over the forecast period, reflecting the role of expected interest rate differentials in the Committee's conditioning assumption.
- Wholesale energy prices that follow their respective futures curves over the forecast period. Since November, gas futures have increased materially (Chart 2.4). Significant uncertainty remains around the outlook for wholesale energy prices.
- UK household energy prices that move in line with Bank staff estimates of the Ofgem price cap implied by the paths of wholesale gas and electricity prices (Section 2.5).
- Fiscal policy that evolves in line with UK government policies to date, as announced in Autumn Budget 2024.

- The growth in the size and composition of the 16+ population implied by the ONS's 2022-based interim national population projections published on 28 January, which reflects international migration up to mid-2024.

Table 1.B: Conditioning assumptions (a) (b)

	Average 1998–2007	Average 2010–19	2023	2024	2025	2026	2027
Bank Rate (c)	5.0	0.5	5.3 (5.3)	4.9 (4.8)	4.2 (3.7)	4.1 (3.7)	4.0 (3.6)
Sterling effective exchange rate (d)	100	82	81 (81)	85 (85)	82 (84)	82 (84)	81 (83)
Oil prices (e)	39	77	84 (84)	75 (75)	74 (73)	71 (71)	70 (71)
Gas prices (f)	29	52	101 (101)	107 (101)	115 (101)	97 (87)	82 (78)
Nominal government expenditure (g)	7¼	2¼	7¾ (7)	5¾ (6)	7 (6¾)	3½ (3½)	3¼ (3¼)

Sources: Bank of England, Bloomberg Finance L.P., LSEG Workspace, Office for Budget Responsibility (OBR), ONS and Bank calculations.

(a) The table shows the projections for financial market prices, wholesale energy prices and government spending projections that are used as conditioning assumptions for the MPC's projections for CPI inflation, GDP growth and the unemployment rate. Figures in parentheses show the corresponding projections in the November 2024 Monetary Policy Report.
(b) Financial market data are based on averages in the 15 working days to 28 January 2025. Figures show the average level in Q4 of each year, unless otherwise stated.
(c) Per cent. The path for Bank Rate implied by forward market interest rates. The curves are based on overnight index swap rates.
(d) Index: January 2005 = 100. The convention is that the sterling exchange rate follows a path that is halfway between the starting level of the sterling ERI and a path implied by interest rate differentials.
(e) Dollars per barrel. Projection based on monthly Brent futures prices.
(f) Pence per therm. Projection based on monthly natural gas futures prices.
(g) Annual average growth rate. Nominal general government consumption and investment. Projections are based on the OBR's October 2024 Economic and Fiscal Outlook. Historical data based on NMRP+D7QK.

1.2: Key judgements and risks

1.2: Key judgement 1

Progress on disinflation in domestic price and wage pressures has generally continued. In large part reflecting recent developments in global energy costs and regulated prices, headline CPI inflation is expected to rise quite sharply in the near

term, to 3.7% in 2025 Q3. But the MPC judges that this pickup in headline inflation will not lead to additional second-round effects on underlying domestic inflationary pressures in the forecast.

CPI inflation peaked at around 11% at the end of 2022, following the succession of very large external cost shocks that occurred in 2021–22. Inflation fell back quite rapidly in 2023, to around 4%, and progress on disinflation has been continuing since then. This has allowed the MPC to reduce gradually the degree of monetary policy restrictiveness.

CPI inflation was 2.5% in December and also in 2024 Q4, close to expectations at the time of the November Report (Section 2.5). That was higher than in Q3 when inflation was at the MPC's 2% target on average. The increase was primarily due to a smaller drag on annual inflation from domestic energy bills. CPI inflation excluding energy has continued to decline over the past year, albeit by less than headline inflation has since its peak, reaching around 3¼% in 2024 H2 compared with its peak of nearly 8½% in mid-2023 (Chart 1.1).

The latest evidence suggests progress on disinflation in domestic price and wage pressures has generally continued, supported by the restrictive stance of monetary policy.

Services consumer price inflation fell by more than expected in December, to 4.4%, but that in large part reflected volatility in airfares that may unwind in the new year. Higher frequency measures of underlying services inflation have been more stable but consistent with some further moderation in annual rates of inflation.

Annual private sector regular Average Weekly Earnings (AWE) growth increased to 6.0% in the three months to November, which was materially higher than the expectations in the November Report, although most other measures of pay growth have not risen over recent months (Chart 2.23). Pay growth is expected to slow significantly by the end of 2025, to around 3¾%.

That is consistent with the steer from the Agents' annual pay survey, in which companies expected the average settlement this year to be 3.7%, towards the top of the 2%–4% range that had been suggested by Agency intelligence at the time of the November Report (Box F). This compares with 5.4% in the equivalent survey at this time last year and the 5.3% that contacts have reported for their actual 2024 settlements. More generally, this survey has tended to have a good track record of matching broad trends in aggregate pay growth. The latest evidence from the DMP Survey is also consistent with a decline in aggregate wage growth, to around 4% over the year ahead.

The November Report projection was for CPI inflation to increase further in the near term, to around 2¾% by the second half of 2025. Headline inflation is now expected to rise more sharply, to 3.7% in 2025 Q3, in large part reflecting recent developments in global energy

costs and regulated prices.

The direct energy price contribution to 12-month CPI inflation is expected to increase from -0.6 to a positive contribution of 0.4 percentage points in 2025 Q3 (Chart 1.1). This reflects the increases since the November Report in wholesale gas futures and oil prices, and therefore household energy bills, on which the MPC's forecast is conditioned. CPI inflation is also expected to rise in the near term due to regulated price changes and the impact of government policies announced in Autumn Budget 2024 (Chart 2.19).

The Committee judges that this near-term pickup in headline inflation will not lead to additional second-round effects on underlying domestic inflationary pressures in the forecast, and it has not changed its judgement on the speed with which overall excess domestic inflationary pressures are expected to dissipate. This in part reflects a looser labour market than at the time of the succession of very large external cost shocks. The impact of recent developments on headline inflation is also expected to be much smaller than in 2021–22. This suggests that some of the dynamics in the inflation generating process that were observed following the previous large shocks are unlikely to reoccur. Nevertheless, given the recent extended period over which inflation remained above the 2% target, the threshold for second-round effects may now be somewhat lower.

There also remain some continuing second-round effects in the forecast related to the previous very large shocks. And there remains uncertainty around how quickly such persistent inflationary pressures will dissipate in the medium term and the extent to which these risks may interact with current economic conditions (Key judgement 3). The speed at which persistent pressures fall back will depend importantly on the evolution of slack in the economy (Key judgement 2).

1.2: Key judgement 2

The recent slowdown in demand is judged to have led to only a small margin of slack opening up, as growth in the supply capacity of the economy appears to have been weakening over the past year. The margin of excess supply is expected to widen over the next couple of years, to around ¾% of potential GDP, before narrowing slightly by the end of the forecast period. The MPC continues to recognise the significant uncertainty around estimates of slack in the economy.

Global GDP growth is expected to be slightly weaker than in the November Report, primarily reflecting near-term developments in the euro area (Section 2.1). Four-quarter UK-weighted world GDP growth is projected to rise back to around 2% in 2026 and beyond.

Over recent days, the US administration has announced new tariffs on imports from some countries, and has indicated that it may impose tariffs on other trading partners as well. This news came after the MPC finalised its February Report projections, and so the forecast is not conditioned on any change in global tariffs and does not include any explicit impact from higher trade policy uncertainty. In any case, it also remains unclear what form such policies may ultimately take, and what other economies may announce in response. As discussed in Box C, while the impact on global growth is likely to be negative if such policies are implemented by the United States or by other countries in response, there is significant uncertainty around the size and the direction of any net effect on UK inflation.

UK GDP growth is estimated to have been zero in 2024 Q3, 0.2 percentage points below the projection in the November Report (Section 2.3). GDP is projected to have fallen by 0.1% in Q4 and to rise by 0.1% in 2025 Q1, also weaker than the 0.3% and 0.4% rates expected in November. The level of GDP is estimated to have been broadly flat since March 2024, and a range of recent data suggests that the labour market is continuing to loosen (Section 2.4). Business survey indicators of output growth have deteriorated over recent months, as have broader metrics of business and consumer confidence, which would be consistent with a recent slowdown in demand.

The Committee has completed its regular review of the determinants of the short to medium-term supply capacity of the economy ahead of the February forecast round. As set out in Box E, the level of potential labour supply is judged to have been materially higher over recent years following the latest revisions to the Labour Force Survey (LFS) to reflect updated population estimates. As this has not been accompanied by similar revisions to GDP, this suggests that potential productivity has been much weaker than estimated previously. Potential productivity is also now weaker than can be explained by previously identified factors such as the impacts of past shocks from Brexit and the pandemic. Some of the weakness could reflect increases in employment in health-related activities over recent years that have not been matched by a similar increase in measured output.

Based on the latest LFS data, potential productivity growth appears to have been particularly weak over the past year, and growth in the supply capacity of the economy appears to have been weakening more generally. For example, the forecast incorporates a slowdown in four-quarter potential supply growth from around 1½% at the start of 2024 to around ¾% at the start of this year. This could reflect a continuation of the structural factors that have been weighing on potential productivity, but also the possibility that additional shocks with supply-like characteristics have been affecting the economy.

The MPC continues to recognise the significant uncertainty around estimates of slack in the economy, particularly at a time when the precise factors accounting for weaker activity are not clear. That weakness could be accounted for by lower supply, or by lower demand relative to

supply and hence greater slack, or more likely by a combination of both.

In the February forecast, as growth in the supply capacity of the economy appears to have been weakening over the past year, much of the current weakness in GDP growth is judged to reflect developments in supply. Given that the levels of demand and supply are still judged to have been broadly in balance throughout most of last year, this means that the recent slowdown in demand is assumed to have led to only a small margin of slack opening up. As the MPC judges that the labour market is starting the forecast period broadly in balance, this is consistent with capacity utilisation within companies being only slightly below its normal level (Chart 2.17).

The Committee has also considered carefully the impact on its projections of alternative assumptions for the degree to which recent developments in activity may reflect greater weakness in demand relative to supply. All else equal, changes in this judgement on the starting level of slack in the economy do not tend to have very large implications for the inflation forecast as long as any additional weakness in demand is assumed to unwind quickly over the forecast period. As set out below, however, there is a more material downside risk to medium-term inflationary pressures if demand were to remain enduringly weak over the forecast period.

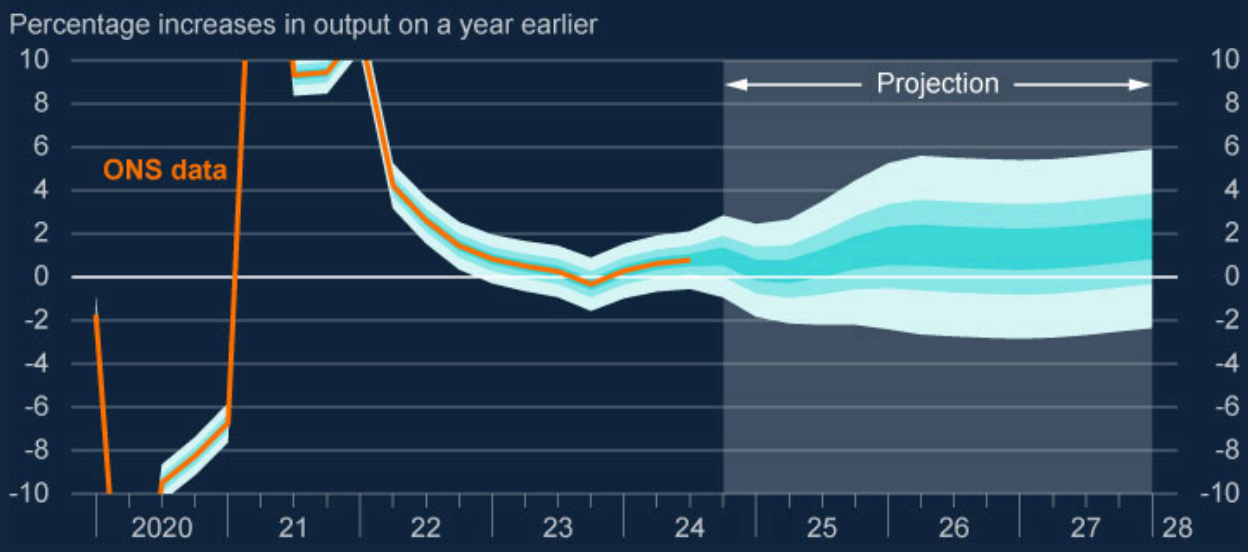
In the February Report forecast, annual potential supply growth is projected to pick up to around 1½% in the medium term (Chart C in Box E). Within that, and reflecting the latest interim national population projections, potential labour supply growth is around ¾% per annum in the medium term. Potential productivity recovers some of its recent weakness and settles at annual growth rates of around ¾%. There could, however, be a downside risk to future potential productivity growth if there are further downward revisions to past trends in productivity, as is suggested by the latest population data that have not yet been incorporated into the LFS.

Four-quarter GDP growth is projected to pick up from the middle of this year, to over 1½% by the end of the forecast period (Chart 1.2). GDP growth in 2025 is much weaker than in the November Report, reflecting recent data developments. Quarterly growth rates are similar to in November beyond the start of this year, however. Household spending growth picks up slightly over the forecast period, supported by a declining saving ratio that in turn reflects the impact of the downward-sloping assumed path of interest rates. Business investment growth slows somewhat in the medium term.

Reflecting these paths of GDP and potential supply, the margin of excess supply is expected to widen further over the next couple of years in the February forecast, to around ¾% of potential GDP. That in part reflects the overall tightening in the stance of fiscal policy that is still assumed to occur following the Budget, and also the continuing restrictive stance of monetary policy. The margin of slack is then projected to narrow slightly by the end of the

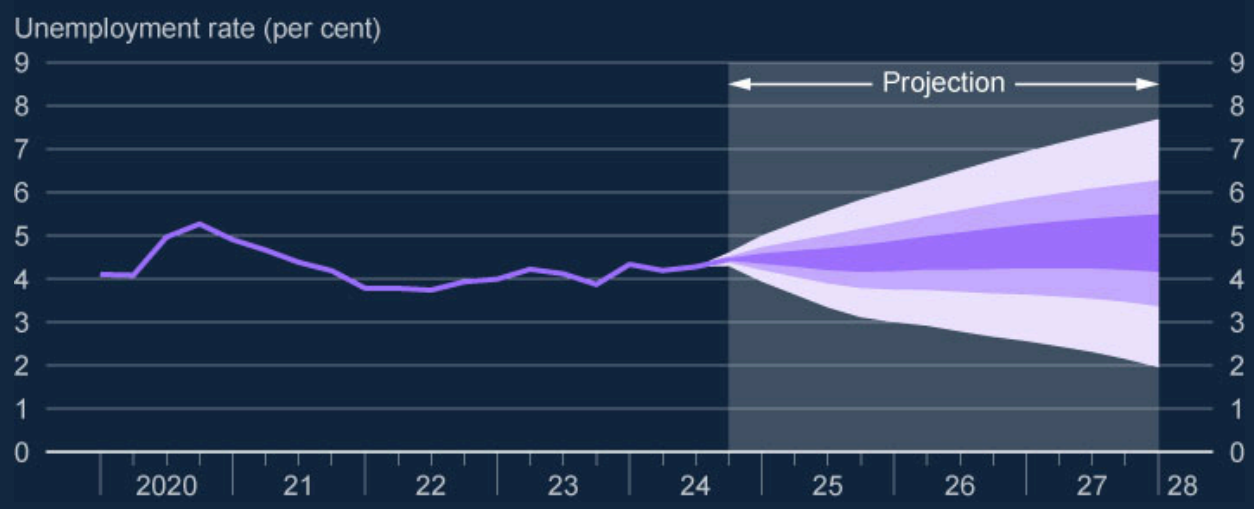
forecast period. Relative to the November Report projection, there is expected to be a somewhat greater margin of excess supply throughout the forecast period, reflecting the weaker starting point and the medium-term impact on slack from a higher market path of interest rates. The unemployment rate is projected to rise gradually to around 4¾% (Chart 1.3), above its assumed medium-term equilibrium rate of around 4½%. Unemployment is somewhat higher than in the November Report.

Chart 1.2: GDP growth projection based on market interest rate expectations, other policy measures as announced



The fan chart depicts the probability of various outcomes for GDP growth. It has been conditioned on Bank Rate following a path implied by market yields, but allows the Committee's judgement on the risks around the other conditioning assumptions set out in Section 1.1, including wholesale energy prices, to affect the calibration of the fan chart skew. To the left of the shaded area, the distribution reflects uncertainty around revisions to the data over the past. To the right of the shaded area, the distribution reflects uncertainty over the evolution of GDP growth in the future. If economic circumstances identical to today's were to prevail on 100 occasions, the MPC's judgement is that the mature estimate of GDP growth would lie within the darkest central band on only 30 of those occasions. The fan chart is constructed so that outturns are also expected to lie within each pair of the lighter aqua areas on 30 occasions. In any particular quarter of the forecast period, GDP growth is therefore expected to lie somewhere within the fan on 90 out of 100 occasions. And on the remaining 10 out of 100 occasions GDP growth can fall anywhere outside the aqua area of the fan chart. Over the forecast period, this has been depicted by the grey background. See the Box on page 39 of the **November 2007 Inflation Report** for a fuller description of the fan chart and what it represents. The y-axis of the chart has been truncated to illustrate more clearly the current uncertainty around the path of GDP growth, as otherwise this would be obscured by the volatility of GDP growth during the pandemic.

Chart 1.3: Unemployment rate projection based on market interest rate expectations, other policy measures as announced



The fan chart depicts the probability of various future outcomes for the ILO definition of unemployment and begins in 2024 Q4. Although LFS unemployment data have recently been reinstated by the ONS, they are badged as official statistics in development and the LFS continues to suffer from very low response rates, which can introduce volatility and potentially non-response bias (see Box D in the **May 2024 Monetary Policy Report**). The fan chart has been conditioned on Bank Rate following a path implied by market yields, but allows the Committee's judgement on the risks around the other conditioning assumptions set out in Section 1.1, including wholesale energy prices, to affect the calibration of the fan chart skew. The coloured bands have the same interpretation as in Chart 1.2 and portray 90% of the probability distribution. A significant proportion of this distribution lies below Bank staff's current estimate of the long-term equilibrium unemployment rate. There is therefore uncertainty about the precise calibration of this fan chart.

There are considerable risks around the future path of excess supply in the economy.

Although the MPC judges that the current stance of monetary policy is restrictive, there remain uncertainties around the impact of monetary policy on demand and hence the margin of slack in the economy (as discussed in Box C in the **August 2024 Report**). Box A in this Report provides a range of estimates for the evolution of the long-run equilibrium real interest rate (R*) since 2018. While cyclical developments in the economy will play a significant role in determining the restrictiveness of the monetary stance at policy-relevant horizons, R* could also play a role in that assessment as a long-term anchor for the policy rate, albeit not as a direct guide for setting policy.

As set out in Box B in the November Report, the combined effects of the measures in the Autumn Budget are expected to boost the level of GDP by around ¾% at their peak, as the stronger, and relatively front-loaded, paths for government consumption and investment more than offset the impact on growth of higher taxes. The increase in employer National Insurance contributions (NICs) was the largest change to taxation in the Autumn Budget. The Committee

has reviewed the latest analysis of the impact of this change (Box D), and has not made material changes to the assumptions in the forecast on the ways in which the NICs increase is likely to be transmitted into higher prices, lower wages and employment, or otherwise absorbed into profit margins. There is a risk that a greater part of the adjustment to the increase in employer NICs comes through lower employment.

That risk sits alongside other current uncertainties in the UK and global economies that could push down on demand and hence on inflationary pressures in the medium term relative to the February forecast. These effects could be magnified if some businesses are already facing cash-flow constraints. In the other direction, if there were to be more constrained supply relative to demand, this could sustain domestic price and wage pressures.

1.2: Key judgement 3

The Committee judges that, while there have been important developments since November, the forecast remains consistent with the second case that it has identified previously regarding the evolution of the remaining persistent inflationary pressures. That is, conditioned on the market path of interest rates, the emerging margin of slack in the economy acts against some continuing second-round effects in domestic prices and wages in order for CPI inflation to fall back to around the 2% target in the medium term.

As set out in Box A in the November Report, the Committee's recent policy deliberations have been supported by the consideration of three cases that impact the evolution of inflation persistence. The February forecast continues to be consistent with the second case, in which a period of economic slack is required in order for pay and price-setting dynamics to normalise fully. The continuing second-round effects in this forecast relate to the unwind of the succession of very large external cost shocks in 2021–22, rather than additional second-round effects from the near-term pickup in headline inflation that is now expected (Key judgement 1). Overall in this projection, the Committee has not changed its judgement on the speed with which excess domestic inflationary pressures are expected to dissipate, with no excess persistence remaining by the end of the forecast period.

In the projection conditioned on the market-implied path of interest rates in the 15 working days to 28 January, CPI inflation falls back gradually from around 3¾% in the middle of this year to around the 2% target in the medium term (Chart 1.4 and Table 1.C). This reflects the continuing restrictive stance of monetary policy and the emerging margin of slack in the economy (Key judgement 2). The February CPI projection is broadly similar to the profile in November from the middle of 2026 onwards, as downward pressure from a somewhat wider margin of slack throughout the forecast period is offset by the impact of higher near-term import price inflation owing in part to the recent depreciation of the sterling exchange rate.

Private sector regular AWE growth is expected to fall from 3¾% at the end of this year to just under 3% in the medium term, similar to the November Report from the middle of 2026 onwards (Table 1.D). Private sector unit wage cost growth is also projected to fall from 3¾% at the end of 2025 to 2¼% at the end of 2026 and to 1¾% at the end of 2027.

There remains considerable uncertainty around the calibration of the Committee's judgement on the path of second-round effects in domestic prices and wages (as set out in Box A in the November Report). Taking recent developments together, the Committee is now placing greater weight on the second and third cases that it has been considering.

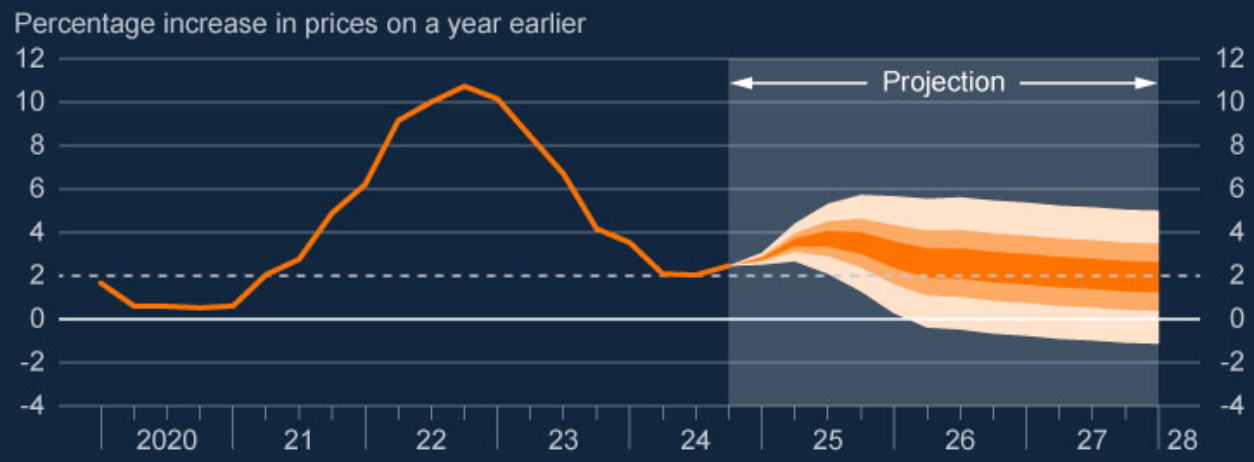
In the third case, there is a risk that the economy has been subject to lasting changes in wage and price-setting behaviour following the major supply shocks experienced over previous years. It remains possible that the path for the medium-term equilibrium rate of unemployment is higher than has been assumed in the forecast, including owing to greater costs of employment, which would be consistent with greater persistence in wage growth. The Committee is also continuing to monitor closely developments in inflation expectations, including the impact from more salient items of the CPI basket such as energy and food prices (Section 2.6).

In the first case that the Committee has considered, the unwinding of the succession of very large past global shocks would continue to feed through to weaker pay and price-setting dynamics, without the need for a period of economic slack. To the extent that this precise case relies on a continuation of weak external cost pressures and lower CPI inflation, it could be somewhat less likely than at the time of the November Report, given recent developments in global energy prices and the near-term pickup in headline inflation. Nevertheless, domestic inflationary pressures could be weaker than in the forecast for other reasons, including the possibility that more of the recent weakness in activity reflects lower demand (Key judgement 2) and that this demand weakness persists such that wages pressures are lower and companies have less pricing power going forward.

The Committee will continue to monitor the accumulation of evidence from a broad range of indicators of inflation persistence.

There also remain risks in both directions around world export price, and hence UK import price inflation. This includes the possibility of increased trade restrictions and greater trade fragmentation (Box C), although there is significant uncertainty around the size and the direction of any net effect on UK inflation.

Chart 1.4: CPI inflation projection based on market interest rate expectations, other policy measures as announced



The fan chart depicts the probability of various future outcomes for CPI inflation and begins in 2025 Q1. It has been conditioned on Bank Rate following a path implied by market yields, but allows the Committee's judgement on the risks around the other conditioning assumptions set out in Section 1.1, including wholesale energy prices, to affect the calibration of the fan chart skew. If economic circumstances identical to today's were to prevail on 100 occasions, the MPC's judgement is that inflation in any particular quarter would lie within the darkest central band on only 30 of those occasions. The fan chart is constructed so that outturns of inflation are also expected to lie within each pair of the lighter orange areas on 30 occasions. In any particular quarter of the forecast period, inflation is therefore expected to lie somewhere within the fans on 90 out of 100 occasions. And on the remaining 10 out of 100 occasions inflation can fall anywhere outside the orange area of the fan chart. Over the forecast period, this has been depicted by the grey background. See the Box on pages 48–49 of the **May 2002 Inflation Report** for a fuller description of the fan chart and what it represents.

Table 1.C: The quarterly projection for CPI inflation based on market rate expectations (a)

	2025 Q1	2025 Q2	2025 Q3	2025 Q4	
CPI inflation	2.8	3.5	3.7	3.5	
	2026 Q1	**2026 Q2**	**2026 Q3**	**2026 Q4**	
CPI inflation	3.0	2.6	2.6	2.4	
	2027 Q1	**2027 Q2**	**2027 Q3**	**2027 Q4**	**2028 Q1**
CPI inflation	2.3	2.2	2.1	2.0	1.9

(a) Four-quarter inflation rate.

Table 1.D: Indicative projections consistent with the MPC's forecast (a) (b)

	Average 1998–2007	Average 2010–19	2023	2024	2025	2026	2027
World GDP (UK-weighted) (c)	**3**	**2½**	**1¾ (2)**	**2 (2)**	**1¾ (2)**	**2 (2¼)**	**2 (2¼)**
World GDP (PPP-weighted) (d)	4	3¾	3¼ (3¼)	3¼ (3)	3 (3)	3 (3¼)	3 (3)
Euro-area GDP (e)	2½	1½	½ (½)	¾ (¾)	¾ (1¼)	1½ (1¾)	1½ (1¾)
US GDP (f)	3	2½	3 (3)	2¾ (2¾)	2¼ (2)	1¾ (2)	1¾ (2)
Emerging market GDP (PPP-weighted) (g)	5½	5	4¼ (4½)	4¼ (4)	3¾ (4)	4 (4)	4 (4)
of which, China GDP (h)	10	7¾	5½ (5¼)	5 (4¾)	4¾ (4½)	4¼ (4)	4 (4)
UK GDP (i)	**2¾**	**2**	**½ (¼)**	**¾ (1)**	**¾ (1½)**	**1½ (1¼)**	**1½ (1¼)**
Household consumption (j)	3¼	2	½ (¾)	1 (¾)	1½ (1¾)	1¾ (2)	1½ (1½)
Business investment (k)	3	4¼	4½ (2¾)	3 (1½)	3 (3¼)	1¾ (2¾)	1½ (2¼)
Housing investment (l)	3¼	4	-7¼ (-7)	0 (-½)	½ (3½)	2¾ (2½)	2¾ (1½)
Exports (m)	4½	3½	-3¼ (-2¼)	-2½ (-¾)	-¾ (2¼)	2½ (1¾)	2½ (2)
Imports (n)	6	4	-4½ (-3½)	1¾ (2½)	3½ (4¼)	3 (3¾)	2¾ (2¾)
Contribution of net trade to GDP (o)	-¼	-¼	½ (½)	-1½ (-1)	-1½ (-¾)	-¼ (-¾)	-¼ (-¼)
Real post-tax labour income (p)	3¼	1½	1 (1½)	4½ (4¼)	1¼ (1½)	¼ (¼)	¼ (¾)
Household saving ratio (q)	7¼	7¾	7¼ (7¼)	10 (10)	9¼ (10¼)	8½ (9)	7¾ (8½)

Credit spreads (r)	¾	2½	1 (¾)	1 (1)	1¼ (1¼)	1¼ (1½)	1¼ (1½)
Excess supply/**Excess demand** (s)	0	-1¾	**¾ (¾)**	0 (0)	-¼ (0)	-½ (-¼)	-½ (-½)
Labour productivity (output per worker) (t)	1¾	¾	-¾ (-¼)	0 (¾)	-½ (½)	¾ (¾)	¾ (½)
Employment (u)	1	1¼	¾ (¼)	1¼ (¾)	¾ (½)	¾ (½)	¾ (¾)
Working-age (16+) population (v)	¾	¾	1¼ (¾)	1¼ (¾)	1¼ (1)	1 (1)	1 (¾)
Unemployment rate (w)	5¼	6	3¾ (3¾)	4½ (4¼)	4½ (4¼)	4¾ (4¼)	4¾ (4½)
Participation rate (x)	63	63½	62¾ (62¾)	63¼ (63)	63 (62¾)	63 (62½)	63 (62½)
CPI inflation (y)	**1½**	**2¼**	**4¼ (4¼)**	**2½ (2¼)**	**3½ (2¾)**	**2½ (2¼)**	**2 (1¾)**
UK import prices (z)	-¼	1¼	1 (1¼)	-1 (-1¼)	1½ (0)	¾ (¾)	½ (½)
Energy prices – direct contribution to CPI inflation (aa)	¼	¼	-1¼ (-1¼)	-½ (-½)	¼ (0)	0 (0)	0 (0)
Private sector regular average weekly earnings (ab)	4	2¼	6¼ (6¼)	6¼ (5)	3¾ (3¼)	3 (3¼)	3 (3)
Private sector regular pay-based unit wage costs (ac)	2	1¾	7¼ (6¾)	7 (4)	3¾ (2¼)	2¼ (2¾)	1¾ (2)

Sources: Bank of England, Bloomberg Finance L.P., Department for Energy Security and Net Zero, Eurostat, IMF World Economic Outlook, National Bureau of Statistics of China, ONS, US Bureau of Economic Analysis and Bank calculations.

(a) The profiles in this table should be viewed as broadly consistent with the MPC's projections for GDP growth, CPI inflation and unemployment (as presented in the fan charts).
(b) Figures show annual average growth rates unless otherwise stated. Figures in parentheses show the corresponding projections in the November 2024 Monetary Policy Report. Calculations for back data based on ONS data are shown using ONS series identifiers.
(c) Chained-volume measure. Constructed using real GDP growth rates of 188 countries weighted according to their shares in UK exports.
(d) Chained-volume measure. Constructed using real GDP growth rates of 189 countries weighted according to their shares in world GDP using the IMF's purchasing power parity (PPP) weights.
(e) Chained-volume measure. The forecast was finalised before the release of the preliminary flash estimate of euro-area GDP for Q4, so that has not been incorporated.

(f) Chained-volume measure. The forecast was finalised before the release of the advance estimate of US GDP for Q4, so that has not been incorporated.
(g) Chained-volume measure. Constructed using real GDP growth rates of 155 emerging market economies, weighted according to their relative shares in world GDP using the IMF's PPP weights.
(h) Chained-volume measure.
(i) Chained-volume measure.
(j) Chained-volume measure. Includes non-profit institutions serving households. Based on ABJR+HAYO.
(k) Chained-volume measure. Based on GAN8.
(l) Chained-volume measure. Whole-economy measure. Includes new dwellings, improvements and spending on services associated with the sale and purchase of property. Based on DFEG+L635+L637.
(m) Chained-volume measure. The historical data exclude the impact of missing trader intra-community (MTIC) fraud. Since 1998 based on IKBK-OFNN/(BOKH/BQKO). Prior to 1998 based on IKBK.
(n) Chained-volume measure. The historical data exclude the impact of MTIC fraud. Since 1998 based on IKBL-OFNN/(BOKH/BQKO). Prior to 1998 based on IKBL.
(o) Chained-volume measure. Exports less imports.
(p) Wages and salaries plus mixed income and general government benefits less income taxes and employees' National Insurance contributions, deflated by the consumer expenditure deflator. Based on [ROYJ+ROYH-(RPHS+AIIV-CUCT)+GZVX]/[(ABJQ+HAYE)/(ABJR+HAYO)]. The backdata for this series are available at **Monetary Policy Report – Download chart slides and data – February 2025**.
(q) Annual average. Percentage of total available household resources. Based on NRJS.
(r) Level in Q4. Percentage point spread over reference rates. Based on a weighted average of household and corporate loan and deposit spreads over appropriate risk-free rates. Indexed to equal zero in 2007 Q3.
(s) Annual average. Per cent of potential GDP. A negative figure implies output is below potential and a positive figure that it is above.
(t) Real GDP (ABMI) divided by total 16+ employment (MGRZ). Although LFS employment data have been reinstated by the ONS, they are badged as official statistics in development and the LFS continues to suffer from very low response rates, which can introduce volatility and potentially non-response bias (see Box D in the **May 2024 Monetary Policy Report**).
(u) Four-quarter growth in the ILO definition of employment in Q4 (MGRZ). Although LFS employment data have been reinstated by the ONS, they are badged as official statistics in development and the LFS continues to suffer from very low response rates, which can introduce volatility and potentially non-response bias (see Box D in the May 2024 Monetary Policy Report).
(v) Four-quarter growth in Q4. LFS household population, all aged 16 and over (MGSL). Growth rates are interpolated between the LFS and ONS National population projections: 2022-based interim within the forecast period.
(w) ILO definition of unemployment rate in Q4 (MGSX). Although LFS unemployment data have been reinstated by the ONS, they are badged as official statistics in development and the LFS continues to suffer from very low response rates, which can introduce volatility and potentially non-response bias (see Box D in the May 2024 Monetary Policy Report).
(x) ILO definition of labour force participation in Q4 as a percentage of the 16+ population (MGWG). Although LFS participation data have been reinstated by the ONS, they are badged as official statistics in development and the LFS continues to suffer from very low response rates, which can introduce volatility and potentially non-response bias (see Box D in the May 2024 Monetary Policy Report).
(y) Four-quarter inflation rate in Q4.
(z) Four-quarter inflation rate in Q4 excluding fuel and the impact of MTIC fraud.
(aa) Contribution of fuels and lubricants and gas and electricity prices to four-quarter CPI inflation in Q4.
(ab) Four-quarter growth in Q4. Private sector AWE excluding bonuses and arrears of pay (KAJ2).
(ac) Four-quarter growth in private sector regular pay-based unit wage costs in Q4. Private sector wage costs divided by private sector output at constant prices. Private sector wage costs are AWE (excluding bonuses) multiplied by private sector employment.

Box A: The long-run equilibrium interest rate

The MPC sets monetary policy to meet the 2% inflation target, and in a way that helps sustain growth and employment. The interest rate required to achieve these objectives can vary significantly over time for both cyclical and structural reasons. The **August 2018 Inflation Report** set out analysis of the equilibrium interest rate, which pointed to it being in the 2%–3% range in nominal terms in the long run. This estimate reflected structural influences such as demographic trends and slower productivity growth, which were expected to keep Bank Rate below its historical average of around 5%.

This box provides a range of estimates for the evolution of the long-run equilibrium real interest rate (R*) since 2018 and discusses recent and potential future developments in its structural drivers. Overall, the evidence suggests that R* is likely to have increased modestly, but that there is significant uncertainty around the range of estimates at any point and the extent of any increase. As a result, while Bank Rate may be reduced further as inflationary pressures fade, absent new disinflationary shocks it is unlikely to fall back to its pre-pandemic lows.

> **In the long run, the equilibrium real interest rate is anchored by slow-moving global structural factors.**

R* is the real interest rate that prevails in the long run when all cyclical disturbances to the economy have subsided, unemployment has returned to its equilibrium level and inflation is at target. While R* is unaffected by cyclical shocks, it can be affected by permanent shocks that have lasting effects on the desired levels of savings and investment. Because R* is a theoretical concept and cannot be directly observed, it is not used by the MPC as a direct guide to setting policy. But to the extent that it can be estimated, it may help to explain the evolution of interest rates over the past and provide some indication of the outlook for interest rates over coming years.

For a small open economy like the UK, R* will ultimately be determined by global forces. That is because frictions that impede the free international movement of capital are weaker over the long run, and free capital movement will tend to equalise capital returns across countries (**Bailey et al (2022)**). At the global level, R* can be thought of as the interest rate that brings the desired stock of savings into balance with the desired level of capital in the long run. The amount of savings individuals want to hold tends to increase as real interest rates rise, since a higher real interest rate implies a greater return on saving. In contrast, the demand for capital tends to fall with the level of interest rates: as the quantity of capital rises, its marginal product falls and so each

extra unit of savings will earn a lower return. The level of R* is thus driven by slow-moving structural factors that affect the global balance between the demand for capital and the stock of savings available to finance it.

Most estimates suggest that R* has fallen over the past few decades across advanced economies.

One of the most important factors for explaining the decline in R* over recent decades is the increasing average age of the global population. An ageing population means, for a given real interest rate, that there is an increase in the quantity of savings individuals wish to hold. In addition, trend productivity growth has slowed across major advanced economies. This reduces businesses' demand for capital and lowers households' expected future income and hence increases their desired savings. Combined, these developments have reduced the long-run real interest rate required to bring actual stocks of savings and capital into line.

Recent empirical evidence suggests that R* has increased modestly since the MPC's assessment in 2018.

Three different empirical approaches to estimating R* all point towards an increase since 2018. Macroeconomic models monitored by Bank staff suggest a modest increase in R* of around 25 to 75 basis points relative to the estimates published in the August 2018 Inflation Report. Financial market-based measures and some survey measures point towards a larger rise, but it is unclear to what extent they accurately reflect perceptions of the long-run equilibrium real interest rate rather than shorter-run developments.

Bank staff monitor developments in R* using a range of macroeconomic models. The common premise of these models is that R* can be identified by decomposing trends and cycles in macroeconomic dynamics. These models point to a modest increase in R* since the MPC's assessment in 2018, though estimates have diverged to some extent since the pandemic. For example, a macrofinance model with two trend factors based on **Davis et al (2024)** finds only a small increase in R* in recent years of around 25 basis points, while a semi-structural model based on **Del Negro et al (2019)** points to a larger increase of around 75 basis points.

Financial market-based measures suggest that R* may have increased to a greater extent, by over 90 basis points since 2018. These measures are based on 10-year UK forward expected real interest rates, which can be extracted from nominal bond yields adjusted for survey measures of inflation expectations. As any cyclical shocks should have dissipated over the 10-year horizon, this should correspond to a measure of R*. However, financial market-based measures may overstate the true increase in R*

because long-term yields have historically been oversensitive to short-term yields. Further, long-term yields reflect both expectations of future interest rates and a term premium, and estimates of term premia are uncertain.

Survey-based measures of equilibrium interest rates also point to an increase in R*. For example, the Bank of England's Market Participants Survey asks respondents for views on the level of Bank Rate at which monetary policy is neither expansionary nor contractionary. This measure has increased by 150 basis points in recent years. However, it is difficult to judge the extent to which these responses reflect perceptions of long-run R*. That is because the question asked does not clearly distinguish between the long-term equilibrium real rate and shorter-term concepts affected by cyclical factors. Meanwhile, 6 to 10 year ahead forecasts for 10-year yields and inflation based on Consensus Economics' survey of professional forecasters imply that expectations of the long-term real interest rate in the UK may have picked up by less than 25 basis points since 2018.

> **Changes in some key drivers of R* are likely to have pushed the equilibrium real interest rate in different directions since 2018.**

Given the uncertainty around a potential change in R*, Bank staff have continued to explore what changes in the global economy may justify an increase. Building on the framework provided by **Cesa-Bianchi et al (2022**) as well as drawing on other studies including **Eggertsson et al (2019)**, **Del Negro et al (2019)** and **Rachel and Summers (2019)**, Table 1 considers how a number of potential drivers may have affected R* since 2018 and could affect it in the future. While some drivers are likely to weigh on R* to a greater degree than previously, others could push up somewhat on R*.

Table 1: Potential drivers of a change in R* since 2018

Potential driver	Likely directional impact on R*
Demographic trends	
Global trade fragmentation	
Higher risk	
Global financial fragmentation	
Expansionary global fiscal policy	
Artificial intelligence (AI)	
Climate change	

Demographic trends, global trade fragmentation and higher risk weigh on R*.

The increasing average age of the global population has weighed significantly on R* over recent decades (**Carvalho et al (2016)** and **Lisack et al (2021)**). According to the **2024 UN population projections**, global population ageing is expected to continue over the coming decades. As the higher desired saving by those approaching retirement is expected be larger than the modest dissaving of retirees over coming decades (**Auclert et al (2021)** and **Vlieghe (2021)**), an ageing population continues to imply a higher desired stock of savings to fund longer retirements. Demographic trends are thus expected to continue to weigh on R*. This reflects a continuation of pre-existing trends as well as a further acceleration of the decline in global fertility rates reported in the UN population projections.

Potential global trade fragmentation and increased trade restrictions could also weigh on R* relative to 2018. Trade openness fosters knowledge spillovers and increases competition, both of which tend to raise productivity growth (**April 2018 World Economic Outlook**). Putting that process into reverse could act as a persistent

negative supply shock for the global economy (Box C). In the longer term, lower potential growth would reduce the return on capital and so reduce R*, other things equal.

Higher risk, as well as higher perceptions of risk and higher risk aversion, could weigh on R*. For example, the experience of the pandemic may have alerted households to the possibility of unprecedented adverse shocks, which could incentivise greater precautionary savings (**Malmendier and Nagel (2011)** and **Jorda et al (2022)**). Meanwhile, greater geopolitical risks as well as risks associated with global trade fragmentation could disincentivise business investment.

> **But financial fragmentation, global fiscal policy, AI and climate change could raise R*.**

While trade fragmentation and higher global risk are likely to weigh on R*, global financial fragmentation is a risk that could push in the opposite direction. In recent decades, global capital market integration has allowed advanced economies to benefit from low borrowing costs, as savings from emerging markets have increasingly flowed to advanced economies. Should this process reverse due to global financial fragmentation, R* would be likely to increase in advanced economies and decrease in emerging markets (**April 2023 World Economic Outlook**).

Global fiscal policy has been expansionary following the pandemic, and global government debt to GDP ratios are projected to continue to rise. Higher public sector spending can reduce the amount of capital available for private investment, putting upward pressure on the equilibrium interest rate. At the same time, a higher supply of safe assets could also put some upward pressure on R*.

Developments in AI have the potential to boost global trend productivity growth, which would lead to an increase in capital demand and hence an increase in R*. But the size of this effect is highly uncertain. While some estimates suggest that global trend growth could be around 1½ percentage points higher due to AI over the coming decade (**Goldman Sachs (2023)**), others point to much smaller effects (**Acemoğlu and Johnson (2023)**).

Climate change and associated mitigation policies are likely to have offsetting effects on R*. Productivity growth is likely to be lower than it would have been in the absence of climate change, both due to the direct physical effects of climate change and because mitigation policies will require investment to be focused on greening the capital stock rather than improving it in other ways. But at the same time, higher government spending on climate change mitigation is expected to put upward pressure

on R*. Staff analysis based on the **NGFS Phase IV scenarios** suggests that the net effect may be a small increase in the equilibrium interest rate, but uncertainty around both the size and the direction of the net effect on R* is large.

There are large uncertainties around the extent of any increase in R*.

Overall, R* is likely to have risen since the August 2018 Inflation Report. However, uncertainty around these estimates is high. In addition to estimation uncertainty, there is significant conceptual uncertainty about how the models used to estimate R* should be defined and constructed, since it is an unobservable variable. As a result, different models tend to vary in how the data are decomposed into cyclical and structural changes, especially towards the endpoint of the sample and given the volatility in inflation and interest rates in recent years.

By acting as a long-term anchor for the policy rate, R* plays a role in assessments of the restrictiveness of monetary policy.

Bank staff assess the restrictiveness of the monetary policy stance on a continuing basis, using a range of tools such as financial conditions indices, the measures of restrictiveness discussed in Box C of the **February 2024 Report** and the analysis of household savings reported in Box E of the **November 2024 Report**. While cyclical developments in the economy will play a significant role in determining the restrictiveness of the monetary stance at policy-relevant horizons, R* could also play a role in that assessment as a long-term anchor for the policy rate, albeit not as a direct guide for setting policy. That R* appears to have risen since 2018 suggests that, absent further shocks, rates are unlikely to go back to pre-Covid lows.

Box B: Monetary policy since the November 2024 Report

At its meeting ending on 18 December 2024, the MPC voted by a majority of 6–3 to maintain Bank Rate at 4.75%. Three members preferred to reduce Bank Rate by 0.25 percentage points, to 4.5%.

Since the MPC's November 2024 meeting, 12-month CPI inflation had increased to 2.6% in November from 1.7% in September. This was slightly higher than previous expectations, owing in large part to stronger inflation in core goods and food. Services consumer price inflation remained elevated. Headline CPI inflation was expected to continue to rise slightly in the near term. Although household inflation expectations had largely normalised, some indicators had increased.

Most indicators of UK near-term activity had declined. Bank staff expected GDP growth to have been weaker at the end of the year than had been projected in the **November 2024 Report**. The Committee judged that the labour market was broadly in balance. Annual private sector regular average weekly earnings growth had picked up quite sharply in the three months to October, but had tended to be more volatile than other wage indicators. The latest Agents' intelligence suggested that average pay settlements in 2025 would be within a range of 3% to 4%. There remained significant uncertainty around developments in the labour market.

Monetary policy had been guided by the need to squeeze remaining inflationary pressures out of the economy to achieve the 2% target both in a timely manner and on a lasting basis. Over recent quarters there had been progress in disinflation, particularly as previous external shocks have abated, although remaining domestic inflationary pressures were resolving more slowly.

The Committee continued to consider a range of cases for how the past global shocks that drove up inflation may unwind, and therefore how persistent domestic inflationary pressures may be. The MPC was also monitoring the impact on growth and inflationary pressures from the measures announced in Autumn Budget 2024, and from geopolitical tensions and trade policy uncertainty. These developments had generated additional uncertainties around the economic outlook.

The Committee continued to monitor closely the risks of inflation persistence and would assess the extent to which the evolving evidence is consistent with more constrained supply, which could sustain inflationary pressures, or with weaker demand, which could lead to the emergence of spare capacity in the economy and push down inflation. A gradual approach to removing monetary policy restraint remained

appropriate. Monetary policy would need to continue to remain restrictive for sufficiently long until the risks to inflation returning sustainably to the 2% target in the medium term had dissipated further. The Committee would decide the appropriate degree of monetary policy restrictiveness at each meeting.

2: Current economic conditions

CPI inflation was 2.5% in December, slightly above the MPC's 2% target but broadly in line with expectations in the November Report. Rising goods and energy price inflation have accounted for the recent rise in headline inflation, while services inflation has fallen. Some indicators of households' inflation expectations have risen in recent months. Headline CPI inflation is projected to pick up further this year, reaching 3.7% in 2025 Q3. That rise in large part reflects further increases in energy prices, alongside other regulatory price increases.

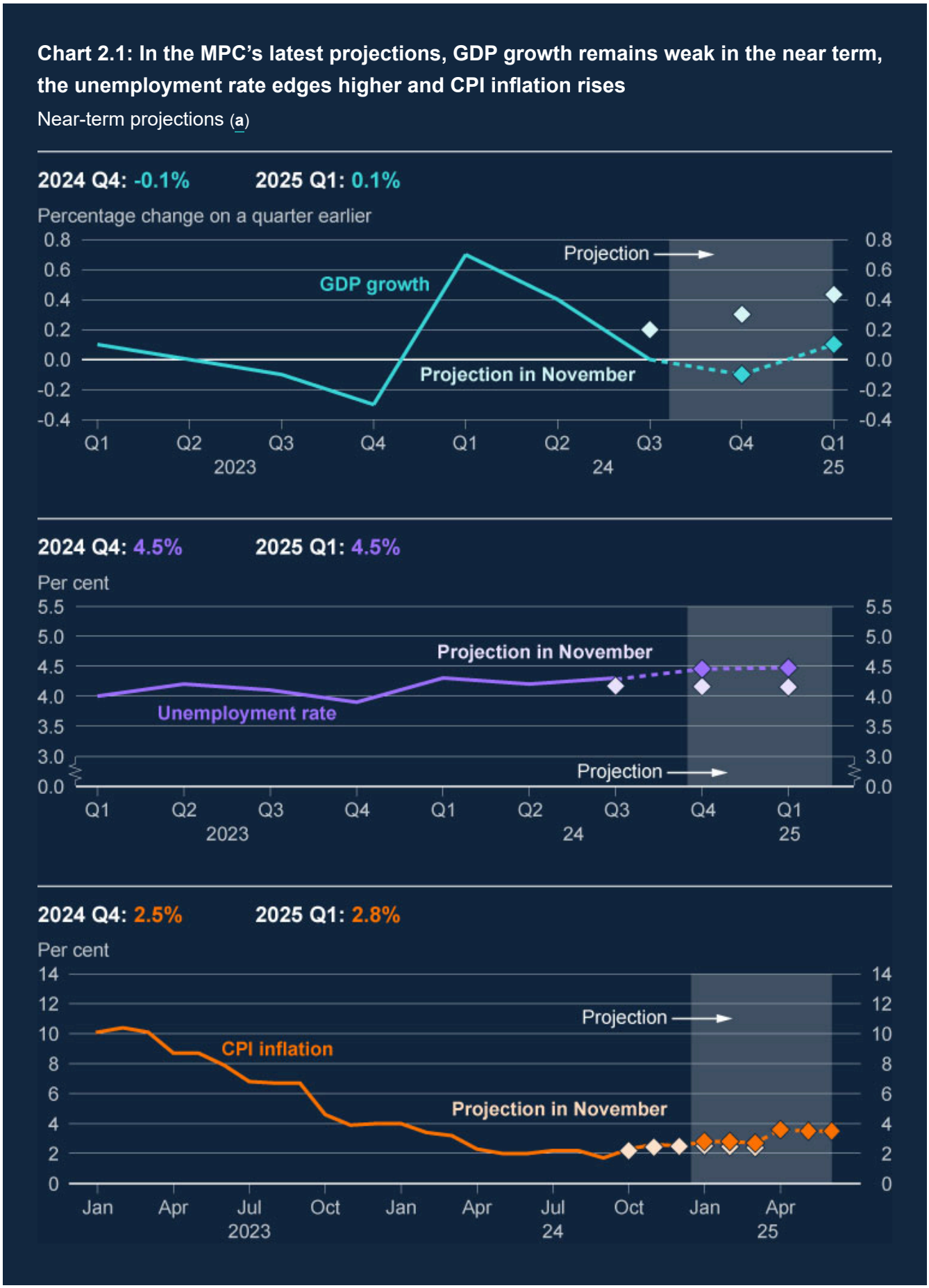
Measures of underlying pressures in services price inflation have continued to ease but remain elevated. They are expected to continue to moderate, including as labour cost pressures fall back somewhat. The labour market has continued to loosen and appears to be broadly in balance. Annual private sector regular average weekly earnings (AWE) growth was 6.0% in the three months to November, higher than expected in the November Report, but an indicator-based model of underlying pay growth was little changed on the quarter. Pay growth is projected to slow over 2025 to around 3¾%, in line with the Agents' annual pay survey.

UK GDP was flat in 2024 Q3 and is expected to decline by 0.1% in the final quarter of the year, reflecting in part a broad-based downturn in business confidence. This is weaker than projected in the November Report. Employment growth has also slowed and surveys suggest a risk of a further weakening. There are significant uncertainties around the current and prospective balance of demand and supply in the economy. In the central assessment, levels of demand and supply are judged to have been broadly in balance throughout most of last year, and so the recent slowdown in demand is assumed to have led to only a small margin of slack opening up.

Global GDP growth is expected to slow slightly into 2025. Trade policy uncertainty has risen, and the US administration has announced new tariffs on some of its trading partners, posing downside risks to global activity. Wholesale gas futures prices have risen notably since November. Headline inflation rates in many economies are now expected to average slightly above central banks' targets this year. Market-implied policy rates had risen since November but have since fallen back lower, while yields on longer-term government bonds are higher in advanced economies. Sterling has weakened somewhat.

Chart 2.1: In the MPC's latest projections, GDP growth remains weak in the near term, the unemployment rate edges higher and CPI inflation rises

Near-term projections (a)



Sources: ONS and Bank calculations.

(a) The lighter diamonds show Bank staff's projections at the time of the November Report. The darker diamonds show Bank staff's current projections. Projections for GDP growth and the unemployment rate are quarterly and show 2024 Q4 and 2025 Q1 (November projections show 2024 Q3 to 2025 Q1). Projections for CPI inflation are monthly and show January to June 2025 (November projections show October 2024 to March 2025). The GDP growth and unemployment rate projections for 2024 Q4 are based on official data to November 2024, while the CPI inflation figures over the same quarter are outturns. Although LFS unemployment data have been re-instated by the ONS, they are badged as official statistics in development and the LFS continues to suffer from very low response rates, which can introduce volatility and potentially non-response bias (Box D of the **May 2024 Report**).

2.1: Global economy and financial markets

> **Global GDP growth is expected to slow slightly into 2025. Elevated trade policy uncertainty could depress growth further and there are downside risks from increases in tariffs.**

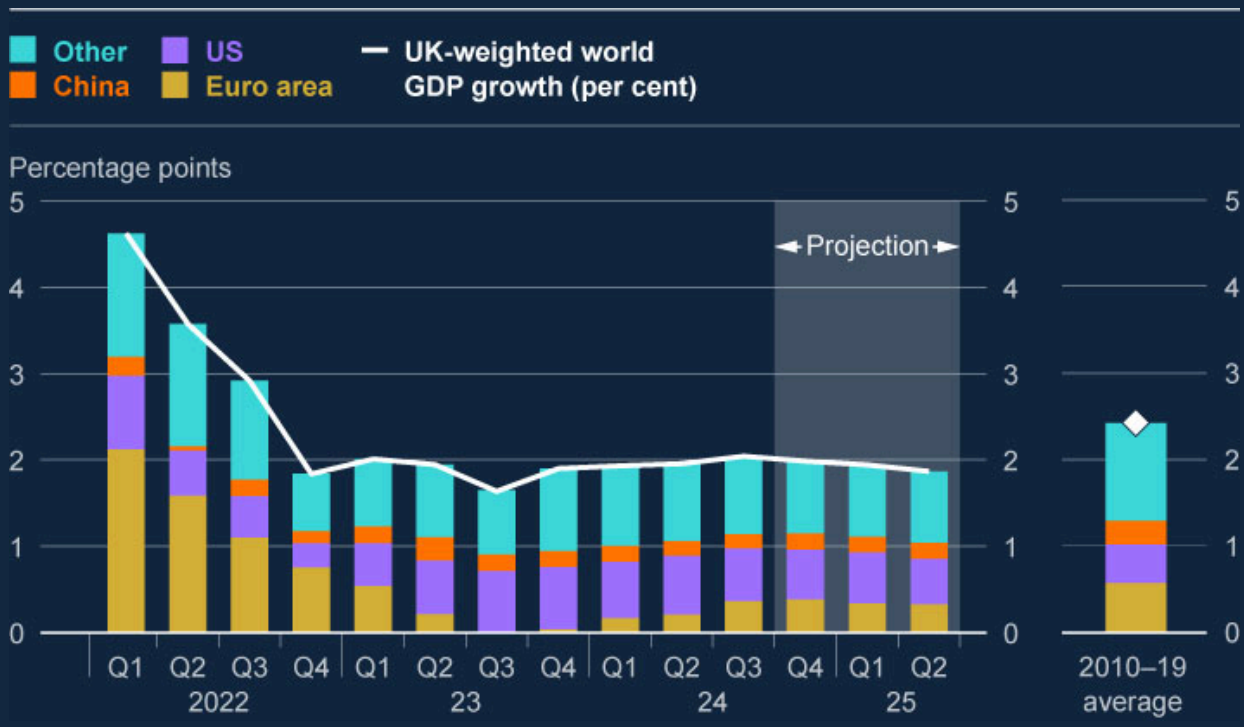
UK-weighted world GDP is projected to have grown by 0.5% in 2024 Q4, the same rate as in 2024 Q3. Global growth is expected to slow slightly in the first half of 2025 (Chart 2.2), partly reflecting a weaker outlook in the euro area.

The US administration has introduced new tariffs on imports of traded goods from China and has indicated that it may also impose tariffs on other trading partners. China has announced some retaliatory tariffs on US goods imports and tariffs might also increase in other countries if they choose to respond to any US measures. Greater global protectionism would be likely to have a negative impact on world economic activity in the medium term, and lead to increased trade fragmentation (Box C).

Measures of global trade policy uncertainty have risen significantly since the US presidential election (Chart 2.3). Rising uncertainty may lead businesses to delay investment spending and hiring decisions until there is greater clarity over trade policy and the economic outlook (**Haddow et al (2013)**), which would negatively impact economic activity.

Chart 2.2: Global GDP growth is expected to slow slightly in the first half of 2025

Four-quarter UK-weighted world GDP growth with contributions by region (a)

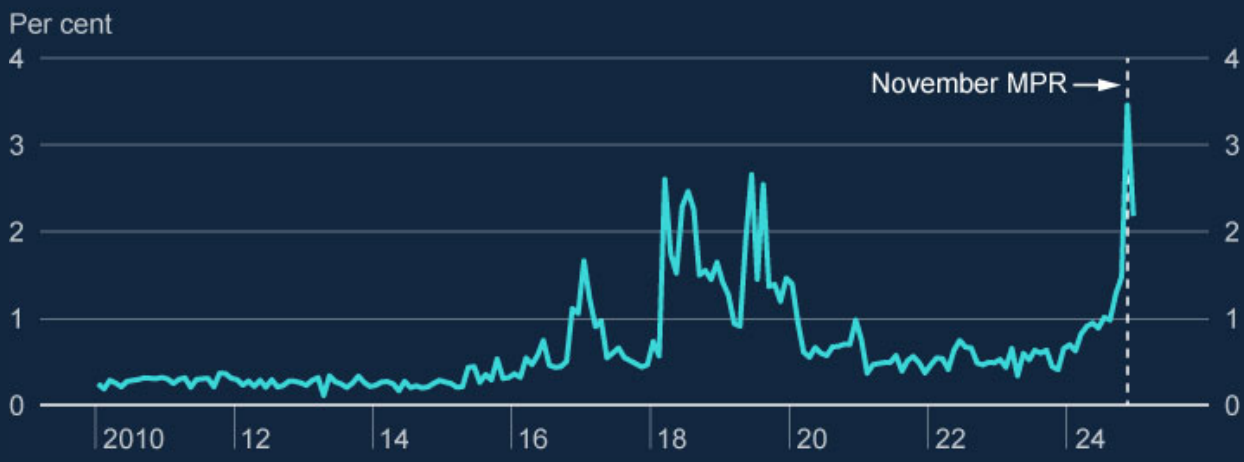


Sources: LSEG Workspace and Bank calculations.

(a) See footnote (c) of Table 1.D for definition. Figures for 2024 Q4 to 2025 Q2 are Bank staff projections. These projections do not include the Advance Estimate of US GDP in 2024 Q4 or the preliminary flash estimate of euro-area GDP for the same quarter, as the data were published after the cut off for incorporation into the forecast.

Chart 2.3: Trade policy uncertainty has reached record highs since the US presidential election

Share of articles in selected publications discussing trade policy uncertainty (a)



Sources: Caldara et al (2019) and Bank calculations.

(a) The trade policy uncertainty index reflects automated text search results of the electronic archives of seven newspapers discussing trade policy uncertainty: Boston Globe, Chicago Tribune, Guardian, Los Angeles Times, New York Times, Wall Street Journal, and Washington Post. Data are monthly. The final data point is for December 2024.

Global export price inflation is expected to have picked up to around its pre-Covid average over the second half of last year.

Global export prices and the sterling exchange rate are key determinants of the level of UK import prices, which in turn are an important influence on UK consumer price inflation (Box D of the **November 2024 Report**). Global export prices, excluding oil, fell in 2023, following a period of sharp increases in 2021 and 2022. Since mid-2024, non-oil global export price inflation has stabilised, and is estimated to have averaged 1.1% on a year earlier over the second half of 2024. This was broadly in line with its pre-Covid average. Global export price inflation is expected to remain close to its pre-Covid average rate over the first half of 2025.

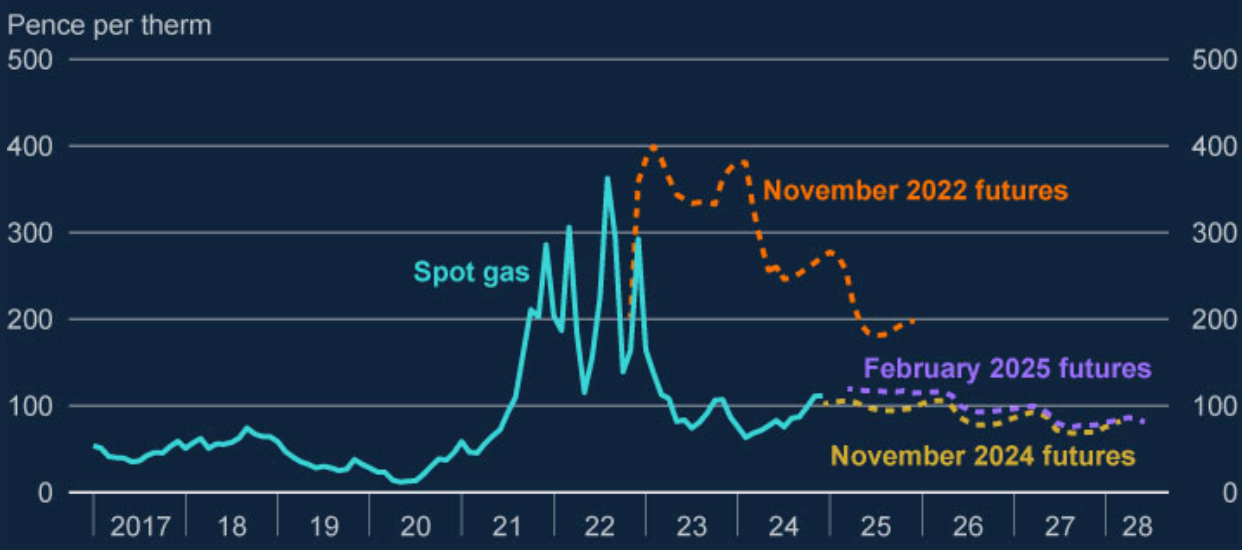
Wholesale gas futures prices have risen notably since November but remain significantly lower than in 2022.

Near-term natural gas futures prices have risen by around 20% since the November Report. However, gas futures prices have changed by less further out (Chart 2.4). Changes in wholesale gas prices feed into the Ofgem energy price cap for household bills (Section 2.5). Demand for natural gas has risen due to a colder-than-expected winter in Europe, leading to lower storage levels in both the UK and Europe than in previous years. Additional demand to replenish gas stores ahead of next winter is likely to maintain upwards pressure on near-term

futures prices. Supply of gas has remained tight recently due to continued restrictions on Russian gas flows into Europe, along with some unplanned temporary pipeline outages. Risks to natural gas prices are judged by Bank staff to be skewed moderately to the upside in the near term, with the balance of demand and supply expected to remain tight.

Chart 2.4: Gas futures prices are notably higher than in November but remain well below their 2022 levels

Wholesale UK natural gas spot price and selected futures curves (a)



Sources: Bloomberg Finance L.P. and Bank calculations.

(a) Spot gas prices are monthly averages of Bloomberg UK NBP Natural Gas Forward Day prices. Dashed lines refer to respective futures curves using one-month forward prices based on the seven-day average to 25 October 2022, and the 15-day averages to 29 October 2024, and 28 January 2025. The final data point shown is the futures price for March 2028.

Moves in oil prices have been smaller than those in gas since November, while wholesale agricultural prices are generally little changed.

Spot Brent crude oil prices have moved slightly higher since the November Report, to US$80 per barrel. Some of this increase reflects new sanctions on Russian oil producers, which may lead to tighter supply. However, supply from non-OPEC+ producers is expected to increase this year, so prices have remained relatively suppressed. Geopolitical tensions have eased since November, particularly following the ceasefire agreement between Israel and Hamas. But direct disruption to oil supply remains an upside risk to prices.

Wholesale agricultural prices are generally little changed since the November Report, although the prices of certain commodities, such as cocoa and coffee, have risen. Changes in wholesale agricultural prices tend to feed through to consumer food price inflation with lags. Wholesale prices have been relatively stable for several months, and UK food input producer prices have fallen recently, suggesting that other factors have driven the recent increase in UK consumer food price inflation rates (Section 2.5).

GDP growth in the US is expected to remain stronger than in other major advanced economies in the near term.

According to the Advance Estimate, US GDP grew by 0.6% in 2024 Q4, following growth of 0.8% in 2024 Q3. US GDP growth is projected to slow to 0.5% in 2025 Q1, although this is likely to be stronger than growth in other major advanced economies. Risks to the US growth outlook in 2025 are two-sided and are highly dependent on the size and timing of the new US administration's trade, fiscal and migration policies.

According to the preliminary flash release, euro-area GDP was flat in 2024 Q4. This followed growth of 0.4% in 2024 Q3, which was supported by strong consumption. The near-term outlook for euro-area activity is relatively weak. Bank staff expect euro-area GDP to expand by 0.2% in 2025 Q1. Growth in the euro area is expected to recover in the second half of 2025 as monetary policy eases, although risks are skewed to the downside due to uncertainty around global protectionist measures and the potential for renewed geopolitical tensions.

While China accounts for only a small share of UK exports, its prominent role in global manufacturing lends it an important influence in commodities and globally traded goods markets. Chinese GDP expanded by 1.6% in 2024 Q4, representing a modest acceleration from earlier quarters. Monetary and fiscal stimulus packages introduced in September and October are likely to be having some positive impact on activity, while export growth has remained strong. Since the November Report, the Chinese authorities have announced a debt-swap programme for local governments, which should provide a small boost to growth over the next few years. Chinese GDP is projected to grow by 1.1% in 2025 Q1. Further monetary and fiscal stimulus trailed by the Chinese authorities may result in some upside news to activity, but underlying domestic demand in China remains weak, and overall, risks to activity growth are skewed to the downside, particularly given recent and potential further tariff increases.

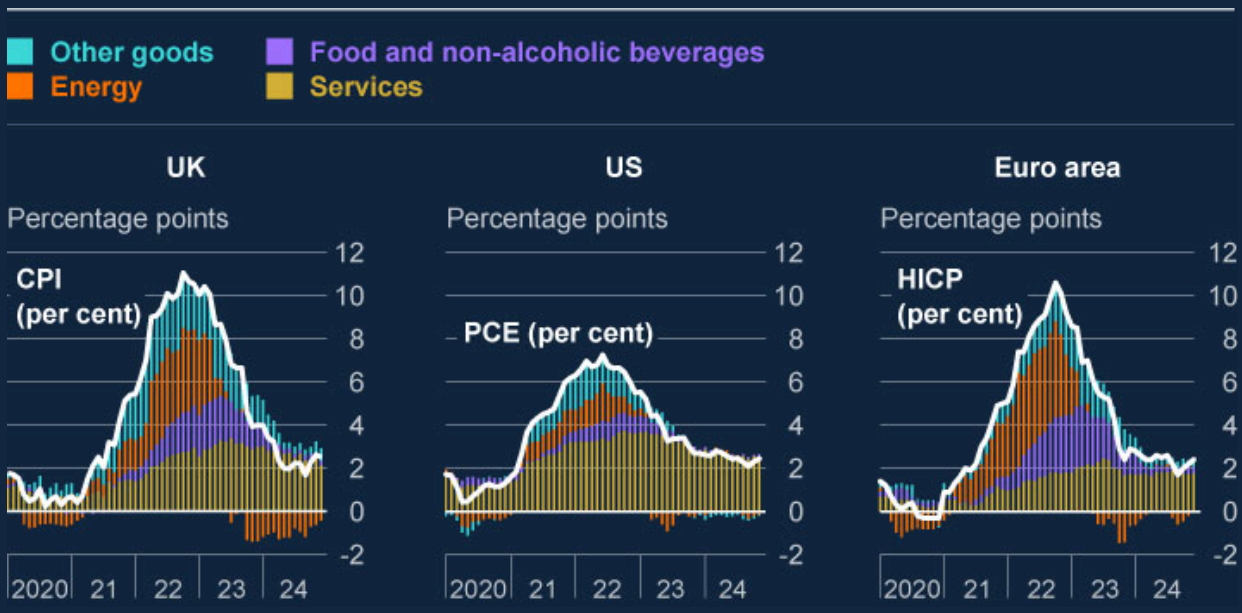
Headline consumer price inflation is projected to remain slightly above target in the US and euro area over 2025.

US PCE inflation, the Federal Reserve's preferred measure, edged up to 2.6% in December, the highest rate in several months (Chart 2.5). PCE inflation is now expected by Bank staff to remain above target throughout 2025. Services inflation excluding energy and housing, which was 3.5% in December, continues to be the major component of headline PCE inflation.

According to the preliminary flash release, annual HICP inflation in the euro area rose to 2.5% in January, while core inflation remained at 2.7%. Bank staff expect that the pass-through of higher wholesale gas prices will also keep headline inflation in the euro area slightly above 2% this year.

Chart 2.5: Headline inflation has moved slightly above central banks' targets in the UK, US and euro area

Contributions to annual headline consumer price inflation in the UK, US and euro area (a)



Sources: Eurostat, ONS, US Bureau of Economic Analysis and Bank calculations.

(a) Data are not seasonally adjusted. Energy includes fuel and household energy bills. Other goods is the difference between headline inflation and the other contributions identified on the chart, and therefore includes alcohol and tobacco. The latest data are November 2024 outturns for US PCE inflation and the associated contributions, and December 2024 outturns for UK CPI and euro-area HICP inflation.

Unemployment remains low in the US and euro area, while pay growth is expected to continue to ease.

Unemployment in the euro area remained close to record lows at 6.3% in December. The job vacancy rate has continued to trend lower, suggesting that excess demand for labour is easing. Annual growth in compensation per employee remained elevated at 4.4% in 2024 Q3 but is expected to moderate over 2025 as the euro-area labour market continues to loosen. The US unemployment rate also remains low, having fallen back to 4.1% in December.

Employment payrolls data generally eased in 2024 but have been stronger since November. Annual pay growth continues to normalise, falling to 3.8% in 2024 Q4, although this remains above the long-run average level.

The market-implied paths for policy rates had risen since November, particularly in the UK and US, but have since fallen back.

Since the November Report, central banks in the US and euro area have continued to reduce their respective policy rates (Chart 2.6). The Federal Reserve's Federal Open Market Committee reduced the target range for the federal funds rate by 25 basis points to 4.25%–4.5% in December, and the ECB Governing Council announced a cut to its deposit facility rate by 25 basis points to 2.75% in January. Market-implied paths for advanced economy policy rates are consistent with some further reductions this year. However, the expected pace and extent of these reductions has continued to diverge since November, with markets anticipating more loosening over 2025 in the euro area than in the UK and US.

The market-implied path for US policy rates, based on the 15 days to 28 January on which the February forecast is conditioned, had shifted up by around 55 basis points on average over the next three years, relative to the November forecast conditioning path. But US market-implied policy rates have since fallen back lower. At its December meeting, the Federal Open Market Committee suggested a slower approach to reducing policy rates in 2025 and signalled higher expectations for core and headline PCE inflation this year. Market intelligence suggests that anticipated policies by the new US administration could lead to additional inflationary pressures, although there has been growing focus on the potential impact on GDP growth of trade and immigration policies.

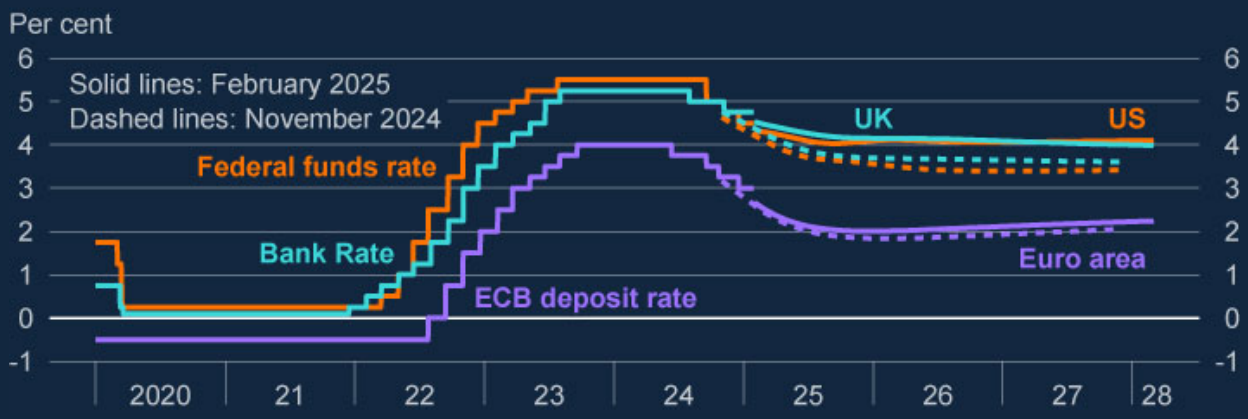
Market-implied policy rates in the euro area had moved by less than those in the US but were around 15 basis points higher than their November 15-day average. Expectations for stickier inflation across advanced economies have been partially offset by the relatively weaker growth outlook in the euro area. The ECB has signalled the risk of below target inflation if policy rates stay elevated for too long.

Movements in the market-implied path for the UK policy rate have been closer to those in the US curve since the November Report, having risen before falling back. On average, the forecast conditioning path for Bank Rate was expected to be around 40 basis points higher over the next three years than was the case in the November forecast conditioning path.

Based on their 15-day averages to 28 January, policy rates were expected to stand at 4.0% in the UK, 4.1% in the US, and 2.2% in the euro area in three years' time. That was around 40 basis points, 65 basis points and 15 basis points higher than expected in the November Report for the UK, US, and euro area respectively.

Chart 2.6: The market-implied advanced economy policy rates on which the February forecast was conditioned had risen since the November Report

Policy rates and instantaneous forward curves for the UK, US and euro area (a)



Sources: Bloomberg Finance L.P. and Bank calculations.

(a) All data as of 28 January 2025. The November 2024 curves are estimated based on the 15 UK working days to 29 October 2024. The February 2025 curves are estimated using the 15 UK working days to 28 January 2025. The federal funds rate is the upper bound of the announced target range. The ECB deposit rate is based on the date from which changes in policy rates are effective. The final data points are forward rates for March 2028.

Yields on longer-term government bonds have risen across advanced economies since November.

Yields on long-term government bonds have moved higher across advanced economies since the November Report and are close to their highest levels since the 2008–09 global financial crisis in the UK and US (Chart 2.7). Rising real term premia have been the most significant driver of the moves since November.

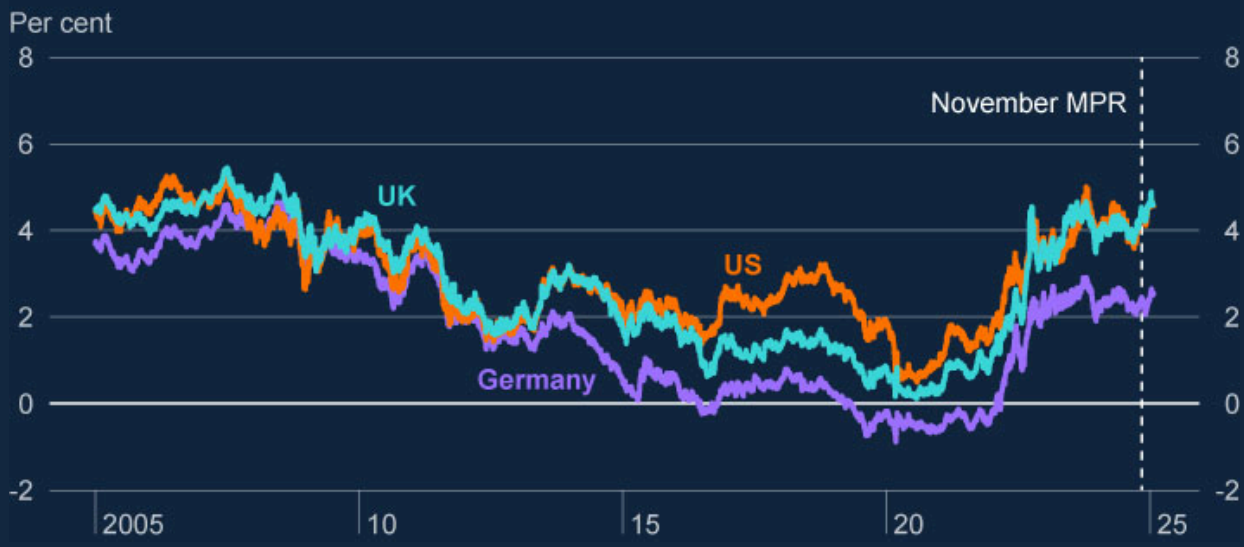
The focus on fiscal policy in advanced economies has prompted some of the increases in long-term rates. Government borrowing is expected to be elevated across advanced economies in 2025 and coming years. Announced gilt issuance in the October Autumn Budget had been towards the upper end of market expectations, while markets are anticipating a further fiscal expansion under the new US administration. Political developments in the euro area have led to greater uncertainty around near-term fiscal consolidation.

Based on the 15-day averages to 28 January, US 10-year government bond yields were around 50 basis points higher since the November Report, while yields in the euro area had risen by around 30 basis points on average. In the UK, 10-year government bond yields had increased by around 55 basis points, although some of the move higher has since retraced.

Market intelligence suggests that the repricing of gilts has been orderly, and bid-ask spreads have remained around historical averages. One model estimated by Bank staff, that decomposes movements in 10-year gilt yields, suggests that the moves since November have been primarily driven by spillovers from global shocks, with UK-specific factors playing a smaller role (Chart 2.8).

Chart 2.7: Long-term government bond yields in the UK and US are around their highs reached during the global financial crisis

Ten-year nominal government bond yields in the UK, US and Germany (a)



Sources: Bloomberg Finance L.P., Tradeweb FTSE Gilt Closing Data and Bank calculations.

(a) The final data points are yields for 28 January 2025.

Chart 2.8: Recent moves in long-term UK rates have been mainly driven by spillovers from global shocks

Decomposition of the cumulative change in 10-year UK nominal government bond yield since 31 October 2024 (a)

Sources: Bloomberg Finance L.P., Tradeweb FTSE Gilt Closing Data and Bank calculations.

(a) Methodology based on Rigobon (2003). Identification of the country-specific origins of shocks is based on asset price volatility over time. Global bars combine identified shocks from the euro area, Japan and US. Data are weekly and the latest data point is for the week to 23 January 2025.

The US dollar has appreciated significantly since the November Report, while sterling has depreciated somewhat. Equity prices have edged higher in advanced economies.

The US dollar has appreciated significantly against other major currencies since the November Report. Recent trade policy developments and broader market expectations around US tariffs have been partly responsible for this dollar strength, while widening interest rate differentials, particularly with the euro area, have also played a role. The sterling effective exchange rate has depreciated by around 2½% since November, primarily driven by weakness against the US dollar.

Advanced economy equity prices are a little higher since November. US share prices rose following the US presidential election result, as market contacts initially focused on the expected positive near-term growth impact from planned policies by the new US administration. US equity prices have been slightly more volatile recently, partly due to developments in the artificial intelligence sector and news around global trade policy. The increases in UK and euro-area equity prices have been smaller than those in the US since November. Investment-grade corporate bond spreads remain low across advanced economies, while wholesale bank funding spreads are little changed since the November Report.

2.2: Domestic credit conditions

The reductions in Bank Rate since August, and the associated falls in market interest rates, have been feeding through to most household lending products as expected.

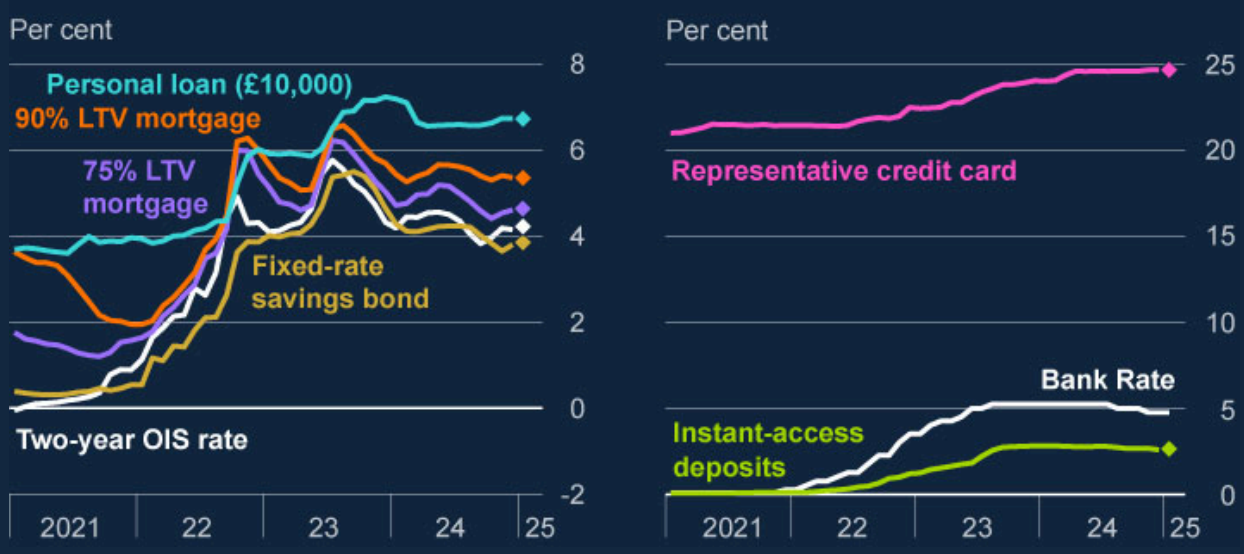
The MPC has reduced Bank Rate since August 2024. The market-implied path for interest rates two-years ahead has fallen since its recent peak of 4.6% in May 2024, although it has risen somewhat since the November Report. The fall in reference rates since their peak has been feeding through to the rates offered on household loans and deposits (Chart 2.9).

Pass-through to household loans appears to be progressing in line with historical experience with, as expected, interest rates for some products taking longer to fall than others. Average quoted rates on two-year fixed-rate mortgages with a loan to value (LTV) ratio of 75%, for example, have fallen by 55 basis points since May 2024 (Chart 2.9). Since the November Report, average quoted rates on some fixed-term mortgages have increased slightly, reflecting the pick-up in the relevant OIS rates since September (Chart 2.9).

Rates on unsecured lending products tend to respond to changes in reference rates more slowly. Quoted rates on representative credit cards, for which Bank Rate is the main reference rate, have risen around 7 basis points since May 2024. Quoted rates on personal loans have also edged up since May 2024.

Chart 2.9: The declines in Bank Rate since August 2024, and the associated falls in the market-implied path of future Bank Rate, have been feeding through to most household deposit and lending rates

Average interest rates on selected household products and their respective reference rates (a)



Sources: Bank of England, Bloomberg Finance L.P. and Bank calculations.

(a) The Bank's **quoted rates series** are weighted monthly average rates advertised by all UK banks and building societies with products meeting the specific criteria. Series are not seasonally adjusted. January 2025 data, shown in diamonds, represent the average of daily quoted rates using data to 28 January and were provisional. The 75% and 90% LTV mortgage rates and savings bond rates are for two-year fixed-rate products. Series shown in white on each panel represent the respective reference rates for the products shown. OIS rate shows monthly averages, while Bank Rate shows month-end numbers. The OIS diamond shows the average of daily rates to 28 January.

Past increases in mortgage rates are expected to result in higher interest rates for some mortgagors rolling off existing fixed-rate mortgages.

Most UK mortgages are held on a fixed-rate basis, with around two thirds of the stock of mortgages currently at a five-year fixed-rate period from origination. Around a third of those on fixed-rate mortgages have not re-fixed since rates started to rise in mid-2021, so the full impact of higher interest rates since then has not yet been passed through to all mortgagors. Bank staff estimates, informed by the FCA Product Sales Data, suggest that just under half of mortgages are likely to see payment increases between December 2024 and 2028 Q1.

Interest rates for those on variable rate mortgages have fallen back from their peaks. A growing number of those who are already paying higher rates may be able to refinance at a lower rate over the next two years. Just over a quarter of mortgage accounts are expected to see monthly payments decrease between December 2024 and 2028 Q1.

Pass-through of Bank Rate changes to household instant-access deposit rates has continued to be lower and slower than historically.

Quoted instant-access deposit rates, for which Bank Rate is the main reference rate, have fallen by 15 basis points on average since May 2024 (Chart 2.9). Pass-through from recent cuts in Bank Rate has been partial and slow when compared to previous cuts when Bank Rate had been at a similar level. That may be partially a consequence of relatively low pass-through during the most recent Bank Rate tightening cycle.

Interest rates on term deposit products, such as those for two-year fixed-rate bonds, have been evolving as expected following movements in the two-year OIS rate (Chart 2.9).

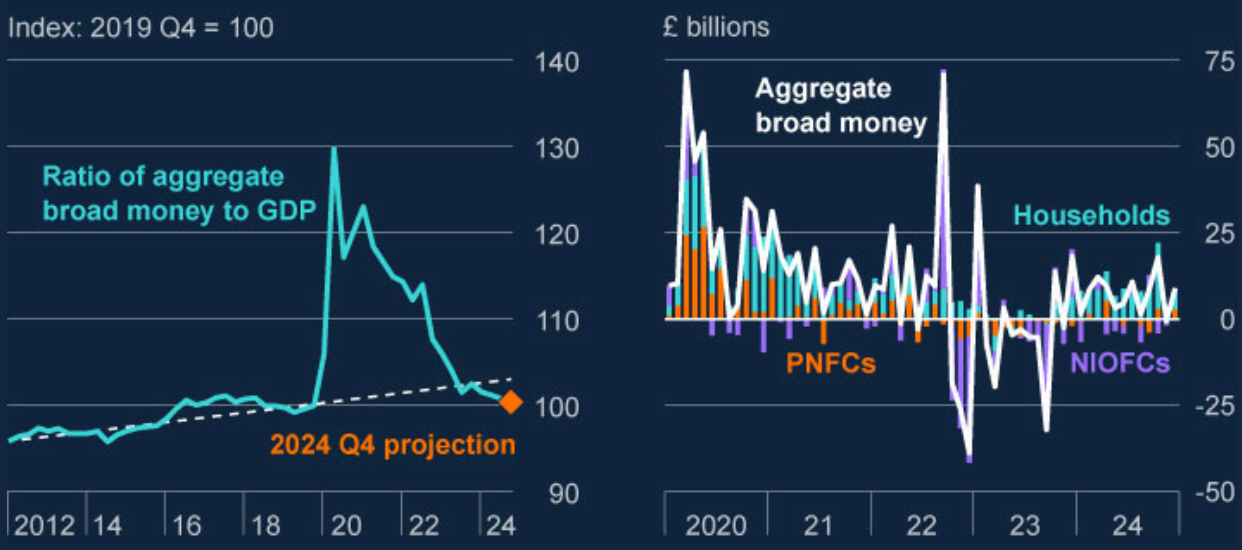
Money growth has been normalising since its post-pandemic weakness.

Aggregate broad money growth has been normalising since its post-pandemic weakness. Broad money holdings increased markedly during the pandemic, reflecting a combination of resilient bank lending growth and the effects of quantitative easing (Box B in the **May 2024 Report**). This was followed by a period of notably weak money growth over 2022 and 2023 and an erosion of the money overhang that had emerged during the pandemic. The ratio of aggregate money to GDP has returned to close to its pre-pandemic trend (left panel of Chart 2.10).

Within the sectoral breakdown, flows into household broad money were notably strong in October 2024 at around £20 billion (right panel of Chart 2.10). Market intelligence suggests those flows were the result of a pick-up in the sale of investments by some households in October. The strength appears to have been temporary, however, with household money flows close to their 2012–19 average in December.

Chart 2.10: Household deposit flows were particularly strong in October 2024, but have since normalised

Ratio of aggregate broad money to nominal GDP and sectoral broad money flows (a) (b)



Sources: Bank of England, ONS and Bank calculations.

(a) Data for the left panel are quarterly. Aggregate broad money captures M4 excluding the deposits of intermediate other financial corporations and is break-adjusted. The dashed line in the left panel shows the 2012–19 trend in the ratio of aggregate broad money to nominal GDP, projected forward. The final data points shown on left panel are for 2024 Q3. The diamond represents a provisional estimate for 2024 Q4, using the latest Bank staff projection for nominal GDP.
(b) Data for the right panel are monthly. Aggregate broad money captures M4 excluding the deposits of intermediate other financial corporations. PNFCs shows broad money flows for private non-financial corporations and NIOFCs shows broad money flows for non-intermediate other financial corporations. For more detail on what is captured within each sector, see **Further details about sectoral analysis of M4 and M4 lending data**. As the sectoral components are seasonally adjusted separately, they may not sum to the total. Latest data shown on right panel are for December 2024.

Consumer credit growth has moderated slightly and is now in line with its pre-pandemic average.

Annual consumer credit growth had been strong since mid-2022. That in part reflected some recovery from the weakness observed during the pandemic. This strength was driven by growth in credit card lending, with some households possibly borrowing to smooth their consumption in response to recent high inflation (**StepChange (2024)**). Consumer credit growth has moderated somewhat in recent months, to 6.5% in December, and is now broadly in line with its 2012–19 average.

There are signs that housing market activity is picking up.

Monthly mortgage approvals for house purchase have risen notably since the start of 2023 and are now slightly above their 2012–2019 average. The recovery, in part, reflects declines in the average rate paid on new mortgages since quoted rates peaked in mid-2023. Banks responding to the 2024 Q4 **Credit Conditions Survey** also reported increased availability of secured lending to households, which was expected to continue into 2025 Q1.

In line with the recovery in housing market activity, nominal house prices have continued to pick up. The official ONS UK HPI measure rose by 3.0% in the three months to November compared with the same period a year ago. The recovery in house prices partly reflects past interest rate rises providing less of a drag.

Corporate lending volumes have been increasing, with some cautious signs of recovery in lending to SMEs.

Corporate lending volumes were weak following the pandemic, particularly for SMEs, reflecting the fact that many businesses had borrowed through the various pandemic-era government loan schemes. Corporate lending growth has since recovered somewhat, reaching 1.9% in the 12 months to December, notwithstanding the downturn in indicators of broader business sentiment (Section 2.3). In addition, there are some cautious signs of that recovery in lending extending to SMEs, with a positive monthly flow of lending to SMEs since October. Banks responding to the 2024 Q4 **Credit Conditions Survey** reported an increase in both availability and demand for corporate lending from smaller businesses and a slight increase from medium and large firms.

2.3: Domestic activity

GDP growth slowed in the second half of 2024.

Having grown solidly in the first half of the year, GDP growth was flat in 2024 Q3, 0.2 percentage points below the projection in the November Report. Household consumption grew by around ½% on the quarter, as did government spending, and business investment grew strongly at nearly 2%. Growth in these expenditure components was offset by a decline in housing investment and a negative contribution from net trade excluding precious metals.

Weak growth continued into the final quarter of last year. On a monthly basis, GDP is estimated to have been flat in the three months to November, which leaves the level of GDP broadly unchanged since March. Weakness has been more pronounced in the market sector, in which output has recorded little growth over the past year while activity in predominantly public sectors has been rising strongly. Bank staff now expect GDP to have fallen by 0.1% in 2024 Q4, lower than the 0.3% quarterly growth projected at the time of the November Report.

Chart 2.11: GDP has been flat since early 2024

Change in measures of activity since 2022 Q4 (a)

Sources: ONS and Bank calculations.

(a) Public sector output includes public administration and defence, education, and human health and social work activities. Market sector output equals total GDP excluding public sector output.

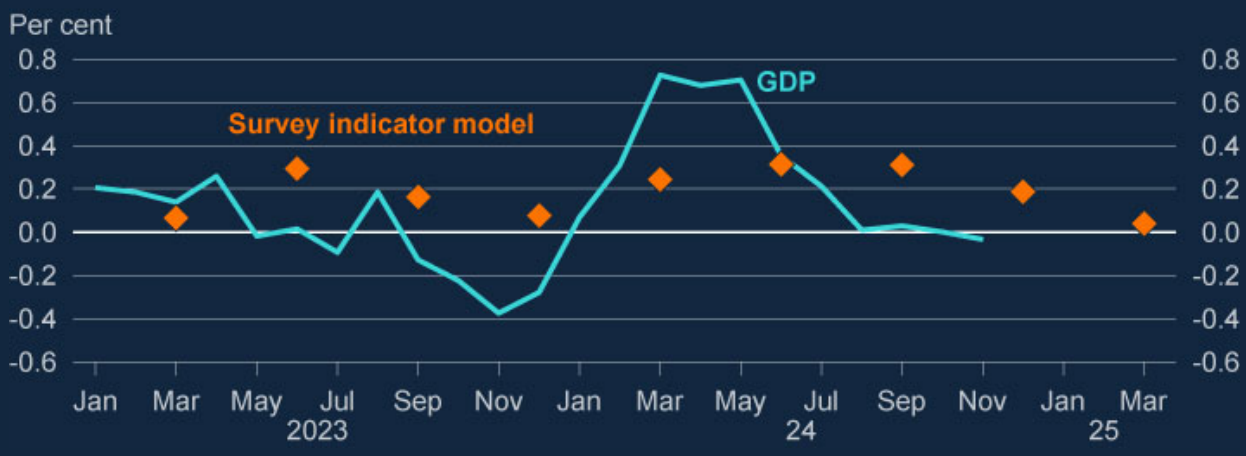
Although GDP growth has been more volatile than suggested by business surveys, underlying growth appears to have slowed since the middle of last year.

Business surveys have suggested a smoother path for GDP growth in recent quarters. GDP growth was above the steer from surveys of businesses' activity in the first half of last year but then slowed to a rate below what these surveys implied in Q3. The S&P Global UK composite output PMI has fallen sharply since last summer and remained below its historic average at 50.6 in the January release. Both the services and manufacturing output balances have fallen since last summer, with respondents primarily linking this to domestic factors, although global factors were also often cited.

The collective steer from surveys now points to a further slowdown in underlying growth at the end of 2024 and into the start of this year (Chart 2.12). GDP growth is projected to pick up to 0.1% in 2025 Q1, 0.3 percentage points weaker than expected at the time of the November Report. Contacts of the Bank's Agents also report that activity has remained subdued around the turn of the year, although they expect some pickup in 2025 as whole. As a result, underlying growth is currently weaker than expected at the time of the November Report.

Chart 2.12: GDP growth has slowed over the course of 2024

Three-month on three-month growth in GDP and quarterly GDP growth implied by business surveys (a)



Sources: British Chambers of Commerce (BCC), CBI, Lloyds Business Barometer, ONS, S&P Global and Bank calculations.

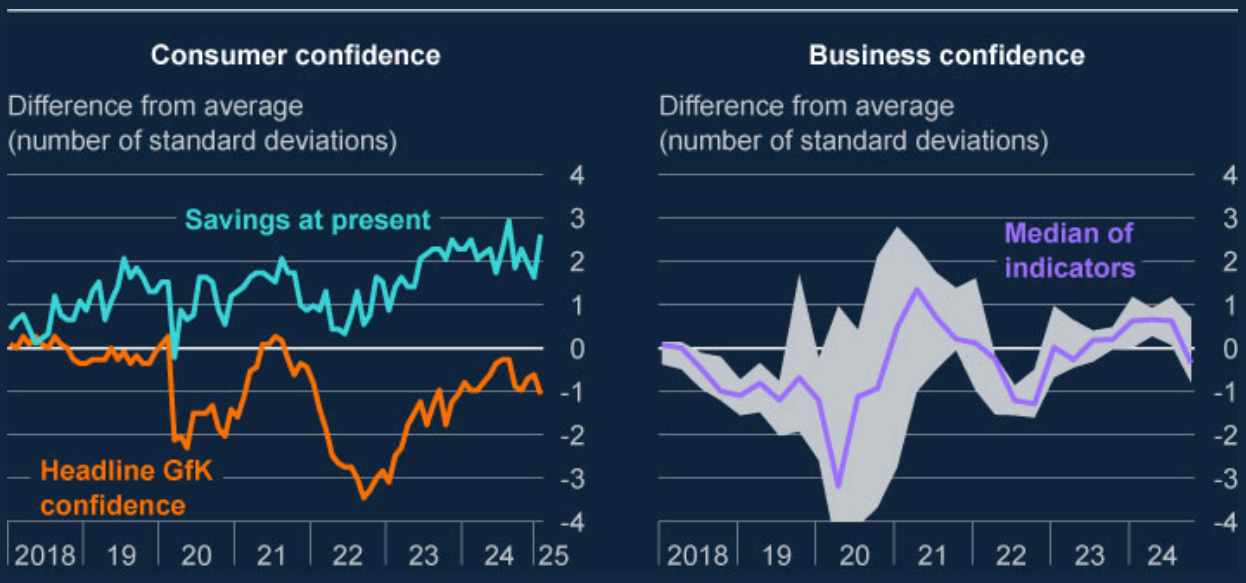
(a) The final data points are for the three months to November 2024. The diamonds to Q3 show in-sample fitted values of the survey indicator model and diamonds for 2024 Q4 and 2025 Q1 show out of sample projections.

Business confidence has also deteriorated in recent months.

The weakening in economic activity has been associated with a deterioration in business confidence, as evidenced across a range of measures (right panel, Chart 2.13). The British Chambers of Commerce and ICAEW measures of business confidence both declined sharply in 2024 Q4. Similarly, the Lloyds Business Barometer overall business confidence measure ticked down for the fifth month in a row in January. The ONS BICS net balance of firms' performance expectations over the coming 12 months declined for the fifth consecutive month in December, to its lowest level since the end of 2022. Across the range of surveys, various factors have been cited as reasons for the deterioration in business confidence. These include geopolitical and trade uncertainty, but also the impact of recent changes to taxation. Surveys of business confidence are often more volatile than businesses' reported output. However, if this weak sentiment persists, it presents some downside risks to the projection for GDP growth.

Chart 2.13: Survey measures of consumer confidence remain subdued and business confidence has declined in recent months

Consumer and business confidence indicators (a)



Sources: BCC, Deloitte CFO survey, GfK, Lloyds Business Barometer, S&P Global/CIPS and Bank calculations.

(a) The swathe in the right panel is comprised of the BCC confidence in turnover over the next 12 months, PMI future output indicator, Deloitte net balance for optimism about financial prospects and Lloyds net balance for firms' trading prospects over coming year. Values in both panels shown as standard deviations from their mean values since 2000 Q1.

Firms' investment intentions have also softened. Investment intentions indicators from the PMI and DMP Surveys have fallen over 2024 Q4, and intelligence from the Bank's Agents points to rising uncertainty, squeezed cash flow and higher borrowing costs deterring capital investments. Business investment growth has been strong recently, expanding by 1.9% in 2024 Q3 and having grown by nearly 1% per quarter on average over the past two years. The weakening in business sentiment suggests slowing business investment growth. Bank staff expect quarterly growth of 0.4% and 0.6% in 2024 Q4 and 2025 Q1, respectively.

Indicators of household spending have also weakened in recent months but consumption growth is expected to pick up again in 2025.

Having grown steadily in the first three quarters of 2024, more recent indicators of household spending have weakened. Retail sales fell by 0.8% in 2024 Q4. Alongside that, consumer confidence has been weak around the turn of the year. The headline GfK measure fell sharply in January (left panel, Chart 2.13), to its lowest level since December 2023, while the S&P UK Consumer Sentiment Index also fell notably. Savings intentions, according to the GfK survey, remain very elevated. However, surveys of consumer confidence are not always reliable predictors of household consumption.

Household consumption growth is expected to be flat in 2024 Q4 before picking up slightly to 0.2% in 2025 Q1. That is weaker than expected at the time of the November Report and broadly consistent with intelligence from the Bank's Agents network where consumer-facing firms also report subdued levels of demand. Beyond that, consumption growth is expected to pick up further over this year, supported by a declining saving ratio and a reduced drag from past interest rate rises.

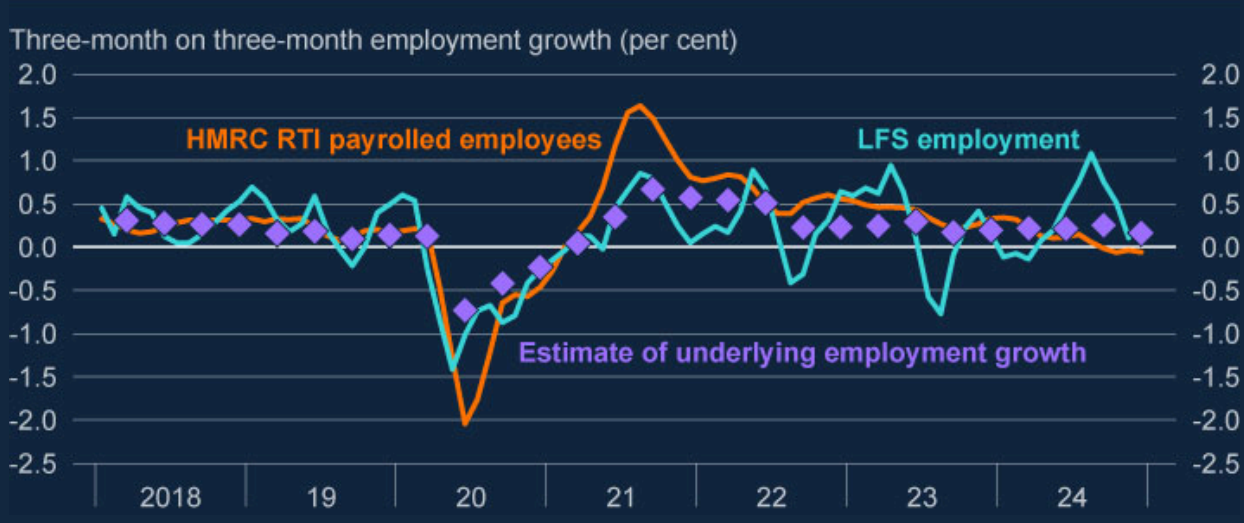
2.4: The labour market and slack

> **Employment growth appears to have softened in recent months and there are downside risks in the near term.**

Staff judge that underlying employment growth has been stable at around 0.2% over much of 2024 (Chart 2.14), although recent data point to a slowing in the pace of growth towards the end of the year. The latest LFS data suggest that employment grew by 0.1% in the three months to November, down from quarterly growth of around 1% in the summer of 2024. Alternative indicators suggest a weaker picture. HMRC RTI payrolls employee data declined for a second consecutive month in December, implying a fall in payroll employment of 0.1% in 2024 Q4 (Chart 2.14). However, early vintages of the payrolls data are subject to frequent and sizeable revisions. More broadly, during 2024 payrolled employment has been supported by strong growth in the public sector while private sector payrolls have been declining.

Chart 2.14: Employment growth appears to have softened though the steer from employment indicators is mixed

Measures of employment growth (a)



Sources: Bank of England Agents, HM Revenue and Customs, KPMG/REC/S&P Global UK Report on Jobs, Lloyds Business Barometer, S&P Global, ONS and Bank calculations.

(a) Bank staff's indicator-based models of near-term employment growth use mixed-data sampling (MIDAS) techniques (**Daniell and Moreira (2023)**). Latest data are three months to November for LFS employment and December for HMRC RTI employment. Quarterly estimates of underlying employment growth extend to 2024 Q4.

Bank staff judge that LFS employment growth was 0.2% in the final quarter of 2024 and will fall slightly to 0.1% in 2025 Q1. However, there are downside risks to the outlook for employment in the near term. Some survey-based employment indicators have weakened notably since the November Report. The composite PMI employment balance fell sharply in December and was little changed on the month in the January reading, at around its lowest level since January 2021. Other survey measures of employment, such as those from the REC and DMP surveys have also weakened, with the increase in employer National Insurance contributions being cited as a key reason by firms (Box D).

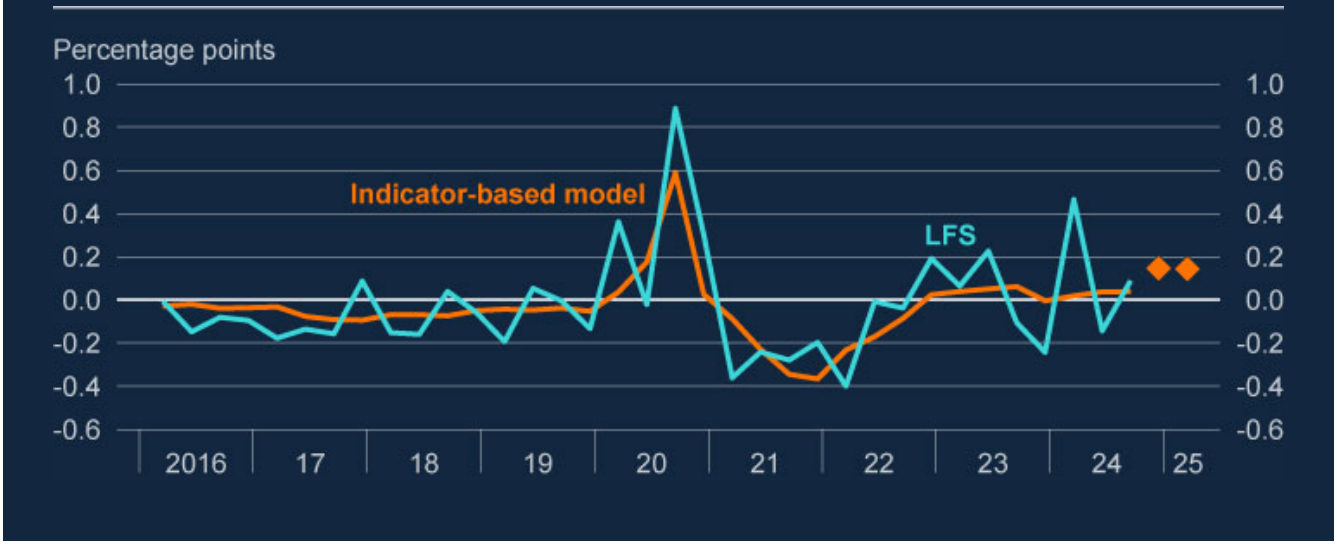
The unemployment rate is judged to have risen only slightly over 2024.

The latest LFS data suggest that the unemployment rate ticked up to 4.4% in the three months to November, having been between 4.1%–4.4% since the start of 2024. Staff estimates of the underlying unemployment rate, which utilise additional data such as the claimant count and measures of recruitment difficulties, also point to a broadly stable rate of unemployment in recent quarters (Chart 2.15). Looking ahead, measures of redundancy intentions point to little change in the path for unemployment, though this differs somewhat to

the weaker steer from surveys of employment. Bank staff expect the rate of unemployment to be around 4.4% in 2024 Q4, rising to 4.5% in 2025 Q1 where it remains over the remainder of 2025.

Chart 2.15: The underlying unemployment rate has been stable in recent quarters

Quarterly change in the unemployment rate (a)



Sources: Bank of England Agents, Google Trends, S&P Global, KPMG/REC UK Report on Jobs, ONS and Bank calculations.

(a) Bank staff's indicator-based models of near-term unemployment use mixed-data sampling (MIDAS) techniques (**Daniell and Moreira (2023)**). Latest data are to 2024 Q3 and the diamonds show the model implied values for 2024 Q4 and 2025 Q1.

The official labour market data have undergone significant revisions but low response rates remain an issue.

In December the ONS revised the LFS data to reflect updated population estimates, which are used to weight the responses to the survey. The ONS has incorporated upward revisions to the estimated population of around half a million people. These revisions have raised the rate of participation and employment implied over the recent past, although the unemployment rate is broadly unchanged (Box E).

While the recent LFS reweighting helps to begin to reconcile different measures of employment, it does not address the continuing issues caused by low response rates (see **Box D, May 2024 Report**). The ONS continues to recommend caution when interpreting the latest LFS data. The MPC continues to employ a wide range of data to inform its understanding of the labour market and the uncertainties surrounding LFS data underscore the importance of this approach.

Demand for workers has continued to ease and the labour market is now judged to be broadly in balance.

Vacancies have continued to decline at a similar pace to recent quarters, falling by around 24,000 in the three months to December. This leaves the ratio of vacancies to unemployment – a measure of labour market tightness – close to pre-pandemic levels.

Analysis by Bank staff supports the MPC's judgement that the labour market has returned to a broadly balanced position. This analysis examines the difference between the observed ratio of vacancies to unemployment and an estimate of its equilibrium. This equilibrium takes account of factors including the lower cost of posting vacancies over time and is informative as observed labour market tightness has exhibited an upward trend over time. The estimate for the equilibrium V/U ratio (aqua line in Chart 2.16) has moved higher from 2014 onwards before flattening off around the time of the pandemic. The observed V/U ratio (orange line in Chart 2.16) moved upwards towards its estimated equilibrium before the pandemic. Since the pandemic, the labour market has been exceptionally tight, before starting to gradually rebalance over the last two years. The latest data show the V/U ratio is back to around its estimated equilibrium. This assessment is consistent with the steer from other indicators of labour market slack, such as the Agents' measure of recruitment difficulties and those in the REC survey.

Chart 2.16: Tightness in the labour market has continued to ease and the market is judged to be broadly in balance

Vacancies to unemployment ratio and estimated equilibrium values (a)

Sources: AA/WARC Expenditure Report, ONS and Bank calculations.

(a) The equilibrium V/U ratio is estimated using an error-correction model over the period 1982–2023. The real cost of vacancy posting and hourly labour productivity are included as long-run determinants for the level of vacancies. The model also includes controls for short-term movements in these variables. Further technical details will be available in a Bank Underground post (Stelmach et al (forthcoming)). The final data points for both series in the chart are 2024 Q3.

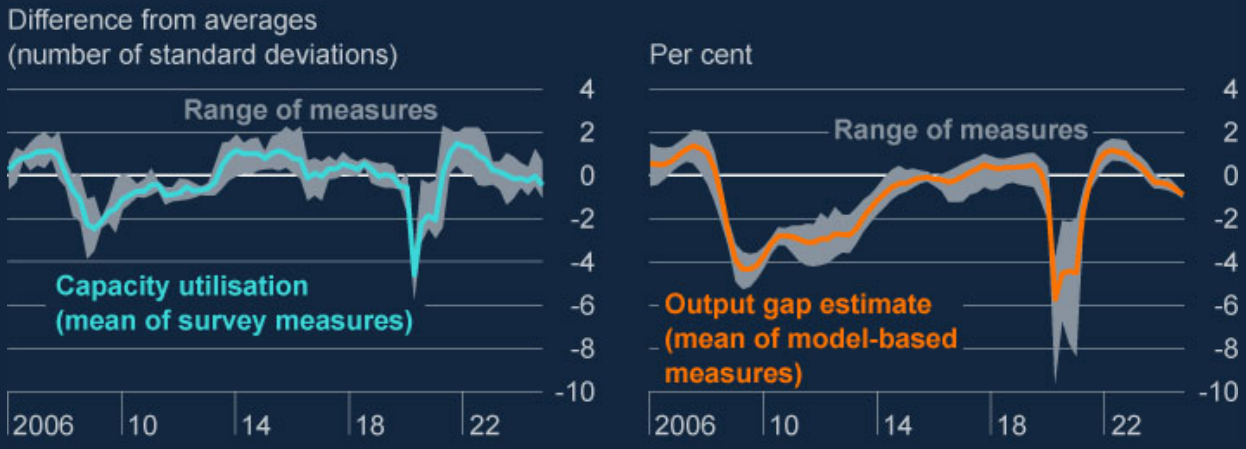
A small margin of economic slack is now judged to have opened up at the end of 2024, though demand and supply remain close to balance.

While GDP growth has weakened noticeably, this has not been reflected to the same extent in estimates of spare capacity across the economy. Alongside the analysis above that suggests there is little excess tightness in the labour market, survey measures of capacity utilisation also point to only a small degree of spare capacity within firms (left panel, Chart 2.17). Meanwhile, top-down estimates of the output gap based on statistical techniques point to it having widened a little over the course of 2024 (right panel, Chart 2.17). Each of these approaches to judging spare capacity are considerably uncertain.

In light of the relative stability in measures of spare capacity compared to those of activity, the current weakness in GDP is judged to reflect not only a slowdown in demand but also a degree of weakening in supply growth over the past year (Section 1 and Box E). There is now estimated to be a small margin of economic slack around the turn of the year compared to the broadly balanced position expected at the time of the November Report (Section 1), but not as large as implied by the weakening in activity on its own. The MPC expects that the margin of slack will open up further, and to a slightly greater extent than in the November Report (Section 1), before narrowing slightly by the end of the forecast period.

Chart 2.17: Measures of capacity utilisation are close to historical averages and output gap models signal a modest widening of economic slack

Survey indicators of capacity utilisation and model-based estimates of output gap (a) (b)



Sources: Bank of England Agents, BCC, CBI, ONS, S&P Global/CIPS and Bank calculations.

(a) Standard deviations from averages between 2000–19. The measures included in the swathe are from the Bank's Agents, the BCC (non-services and services), the CBI (manufacturing (capacity); financial services, business/consumer/professional services and distributive trade (business relative to normal)) and CIPS (manufacturing (backlogs); services (outstanding business)). Sectors are weighted using shares in gross value added. The BCC data are not seasonally adjusted. The data are shown to 2024 Q4.
(b) The model-based estimates of the output gap are based on a variety of multivariate filters whose mean values are standardised to the MPC's estimate of the output gap. The final data point in the chart is 2024 Q4.

2.5: Inflation and wages

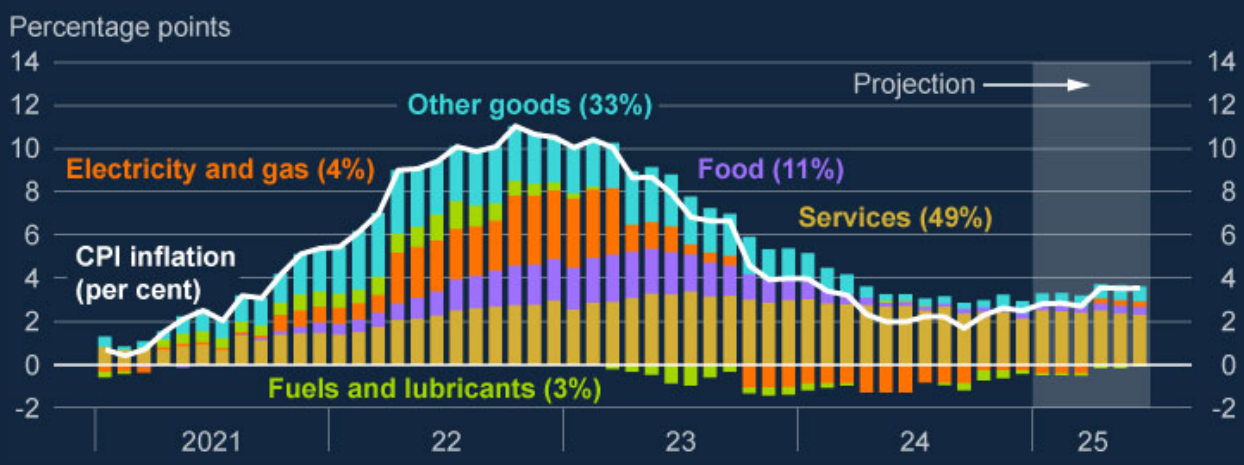
Headline CPI inflation rose to 2.5% in December, above the MPC's 2% target.

Twelve-month CPI inflation was 2.5% in December, up from 1.7% in September (Chart 2.18). The rise in headline CPI inflation over 2024 Q4 was primarily due to a smaller drag on annual inflation from domestic energy bills. Core CPI inflation, which excludes energy, food, beverages and tobacco, fell in December, to 3.2%, a little below the expectation in the November Report but still historically elevated.

The increase in headline CPI inflation over Q4 was broadly in line with the expectation at the time of the November Report. However, within that, stronger-than-expected food and core goods price inflation was offset by weaker-than-expected services inflation, particularly in airfares.

Chart 2.18: CPI inflation was 2.5% in December, and is expected to rise over the first half of 2025

Contributions to CPI inflation (a)



Sources: Bloomberg Finance L.P., Department for Energy Security and Net Zero, ONS and Bank calculations.

(a) Figures in parentheses are CPI basket weights in 2024. Data are shown to December 2024. Component-level Bank staff projections are shown from January to June 2025. The food component is defined as food and non-alcoholic beverages. Fuels and lubricants estimates use Department for Energy Security and Net Zero petrol price data for January 2025 and are then projected based on the sterling oil futures curve.

CPI inflation is projected to rise further in the near term, reaching 3.7% in 2025 Q3, mainly driven by higher energy prices.

Headline CPI inflation is expected to continue to rise in the near term, reaching 3.5% by June (Chart 2.18). Consistent with the expected rise in near-term inflation, the latest S&P Global UK composite input and output price indices have both picked up since October 2024.

The single largest driver of the further pickup in inflation is household energy bills and fuel prices (Chart 2.19). The Ofgem energy price cap for the typical household has risen from £1,568 in July 2024 to £1,738 in January 2025 and is expected to rise somewhat further in April. As previous large falls in domestic energy bills have also fallen out of the annual inflation calculation, household energy is expected to contribute around ½ of a percentage point to the rise in headline inflation between December 2024 and June 2025. This is a larger rise than expected at the time of the November Report, due to the observed increases in wholesale energy costs (Section 2.1), which underpin the Ofgem energy price cap.

Regulated price changes and the impact of government policies announced in Autumn Budget 2024 are also expected to contribute to the near-term increase in inflation. Collectively these are projected to add around ½ of a percentage point to headline inflation by 2025 Q2

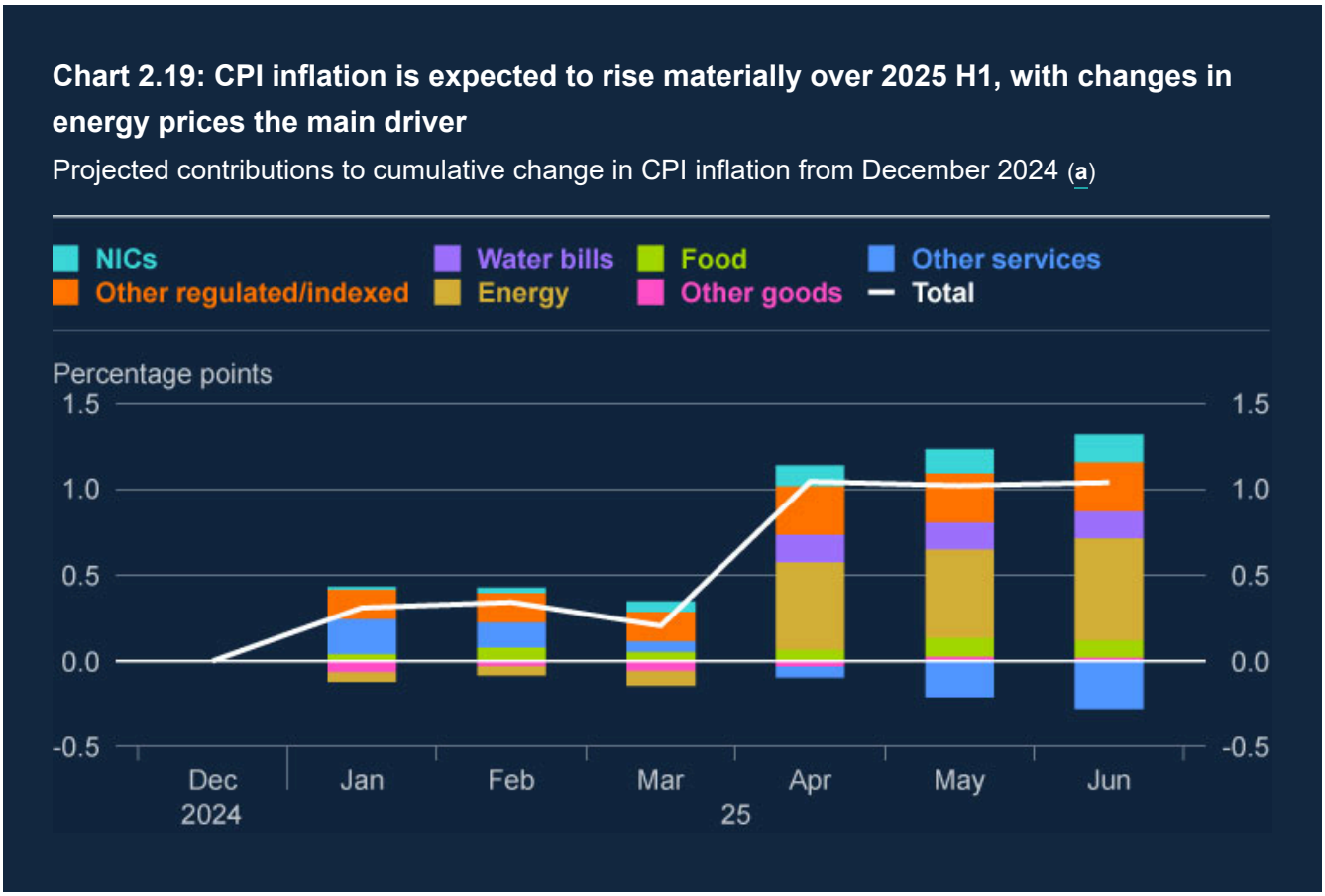
(Chart 2.19). This is made up of a rise in the cap on bus fares and the introduction of VAT on private school fees, which push up on services inflation from January, along with an increase in water bills taking effect from April. The increase in employer NICs is also assumed to have a small upward impact on inflation as firms pass on higher costs to their prices.

Bank staff judge that the recent weaker-than-expected airfares outturn is likely to unwind, which is also expected to push up on services inflation from January, though services inflation is expected to slow again in June (azure bars in Chart 2.19). In addition, as set out below, non-energy goods price inflation is expected to be slightly higher than projected in the November Report.

CPI inflation is expected to rise a little further to 3.7% in 2025 Q3, mainly on account of further pass through of recent developments in global energy costs, before beginning to ease again from the final quarter of the year (Section 1).

Chart 2.19: CPI inflation is expected to rise materially over 2025 H1, with changes in energy prices the main driver

Projected contributions to cumulative change in CPI inflation from December 2024 (a)



Sources: Bloomberg Finance L.P., Department for Energy Security and Net Zero, ONS and Bank calculations.

(a) Data to December 2024. Component-level Bank staff projections from January to June 2025. The energy component includes fuels and lubricants and electricity and gas. The NICs bars show Bank staff estimates of the pass-through of the increases in employer NICs announced in Autumn Budget 2024 to headline CPI inflation. The other regulated/indexed component includes education, other transport services, other services for personal transport equipment and communication services. The water bills component includes water supply and sewerage collection. The food component is defined as food and non-alcoholic beverages excluding the estimated impact of the changes to employer NICs. The other goods component is defined as goods excluding energy, food and non-alcoholic beverages, water supply and the estimated impact of the changes to employer NICs on goods inflation. The other services component is defined as services excluding education, other transport services, other services for personal transport equipment, communication services, sewerage collection and the estimated impact of the changes to employer NICs on services inflation.

Core goods and food price inflation rose in 2024 Q4 and are expected to rise further above their pre-Covid averages in the near term.

Core goods and food CPI inflation fell materially over 2023 and early 2024 (Chart 2.20), following declines in the prices of key inputs such as energy and other externally driven cost pressures.

Both core goods and food price inflation measures have begun to pick up more recently. Annual core goods inflation was 1.2% in December, above its pre-Covid average rate and 0.5 percentage points higher than expected in the November Report (Chart 2.20). Alongside that,

the rate of annual food and non-alcoholic beverage inflation was 2.0% in December, around 1 percentage point higher than expected in the November Report projection.

Recent increases in core goods and food price inflation are likely in part to reflect rising labour cost pressures. Intelligence from the Bank's Agents suggests labour costs are playing an increasing role in these sectors, given recent NLW increases and the upcoming increase in employer NICs.

Core goods and food price inflation are expected to rise somewhat further above their pre-Covid averages in the near term (Chart 2.20). For core goods inflation, that in part reflects previous weakness in price rises falling out of the annual inflation calculation. Both components are affected by the impact of tax and regulatory changes in the first half of the year. The food and drinks sector is also expected to be affected by the Extended Producer Responsibility (EPR) regulations, which come into effect from October 2025. These regulations increase the responsibility of some organisations in the supply chain for paying the recycling costs of packaging materials. Some contacts of the Bank's Agents in the sector expect the impact of the EPR for their business could be similar to that of the increases in employer NICs.

Chart 2.20: Core goods and food price inflation are slightly above their pre-Covid averages while services inflation remains elevated

Annual inflation rates for components of CPI (a)

Sources: ONS and Bank calculations.

(a) The core goods component is defined as goods excluding food and non-alcoholic beverages, alcohol, tobacco and energy. The food component is defined as food and non-alcoholic beverages (FNAB). Data are to December 2024. Bank staff projections from January to June 2025. Dashed lines represent the 2010–19 averages, which are 3.0%, 1.6% and 0.8% for services, FNAB and core goods respectively.

Underlying inflationary pressure in services is continuing to moderate. Services inflation is expected to rise again in the near term, however, driven mainly by one-off or volatile factors.

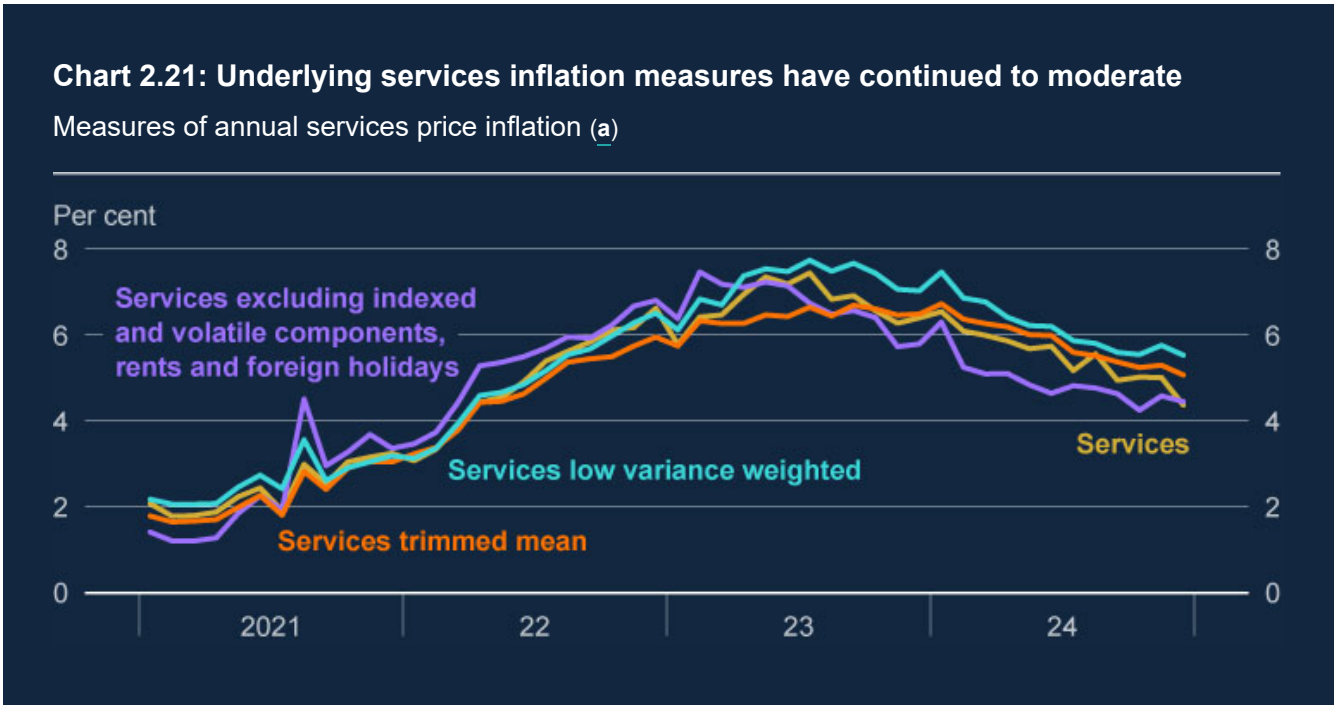
Annual services price inflation has continued to moderate from its peak but remains elevated relative to the rate previously seen as compatible with the achievement of the inflation target (Chart 2.20). Annual services price inflation fell to 4.4% in December, down from 5.0% in November. The December outturn was 0.4 percentage points lower than projected in the November Report, mainly driven by the smaller-than-expected increase in airfares.

Services inflation is expected to rise to just above 5% in January and average around that rate over 2025 H1 (Chart 2.20). That rise is driven in part by volatile factors, including the expected reversal of the weaker-than-expected increase in airfares in December. In addition, the range of regulatory and fiscal measures outlined above – including increases in private school fees, bus fares, Vehicle Excise Duty, sewerage bills and employer NICs – are expected to be adding just under 1 percentage point to headline services inflation in April 2025. Headline services inflation is then expected to fall back a little, to 4.7% in June.

Bank staff judge that, looking through the impacts of regulatory and fiscal measures and other one-off factors, underlying services inflationary pressures will continue to ease slightly over 2025 H1. Measures of underlying services price inflation have been gradually easing, broadly as expected at the time of the November Report, though they remain elevated (Chart 2.21). Consistent with this, there has been an easing in underlying pay pressures since mid-2023, with these expected to abate further over 2025 (Chart 2.22). Intelligence from the Bank's Agents also points to a modest slowing in the pace of services price inflation in the coming year.

Chart 2.21: Underlying services inflation measures have continued to moderate

Measures of annual services price inflation (a)



Sources: ONS and Bank calculations.

(a) The low variance measure is calculated by weighting each component of services inflation by the inverse variance of the change in 12-month inflation of that component from 12 months previously. The maximum adjusted weight is capped at twice its original value. Details on the components which have been included/excluded from the 'Services excluding indexed and volatile components, rents and foreign holidays' measure are included in the accompanying spreadsheet published online. There has been a small definitional change to this series compared with versions shown in previous Reports to remove the passenger transport by bus and coach component. The trimmed mean measure excludes the 10% largest and 10% smallest price changes. The latest data points shown refer to December 2024.

Private sector regular pay growth was stronger than expected towards the end of 2024…

Wage growth remains an important factor behind the remaining persistence in services inflation. Annual growth in private sector regular average weekly earnings (AWE) rose by 6.0% in the three months to November (Chart 2.22), notably higher than anticipated in the

November Report. Bank staff's indicator model of underlying pay growth – based on a statistical combination of signals from a range of pay indicators – points to underlying wage growth being little changed on the quarter at 5.2% in 2024 Q4, however.

Chart 2.22: Official AWE growth has picked up in recent months, but is expected to moderate over the coming year

Measures of annual private sector wage growth (a) (b)

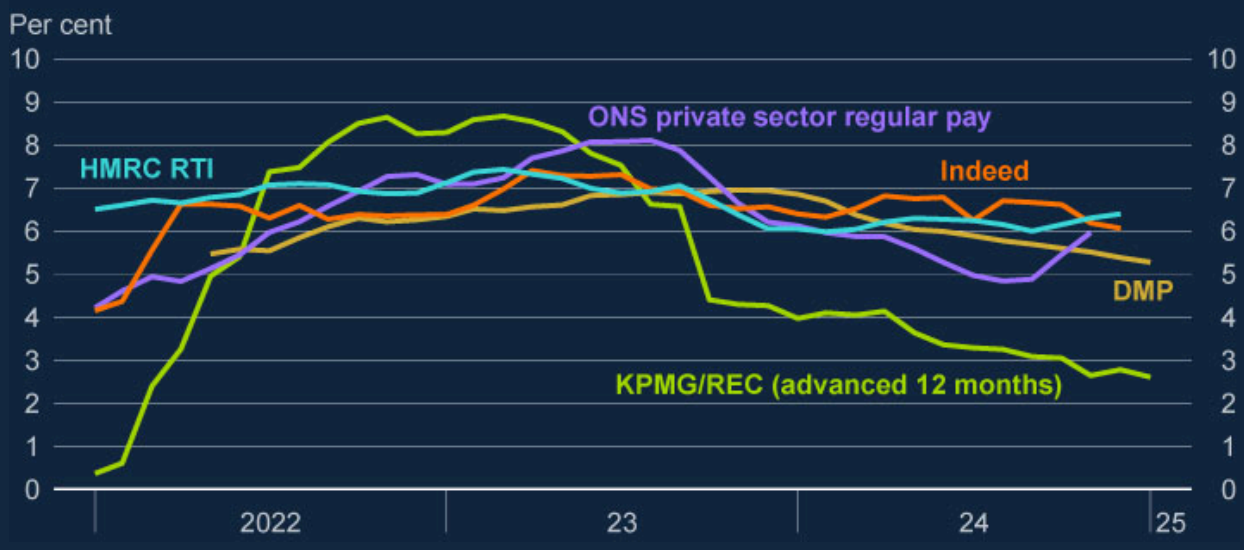
Sources: Bank of England Agents, DMP Survey, HMRC, Indeed, KPMG/REC UK Report on Jobs, Lloyds Business Barometer, ONS and Bank calculations.

(a) Private sector regular pay growth in the aqua line shows the ONS measure of private sector regular average weekly earnings growth (three-month average on same three-month average a year ago). Bank staff's indicator-based model of near-term private sector regular pay growth is quarterly and uses mixed-data sampling (or MIDAS) techniques. A range of indicators inform the model, including series from the Bank of England Agents, the Lloyds Business Barometer, Indeed, ONS/HMRC PAYE payrolls and the KPMG/REC UK Report on Jobs. Indicators are weighted together according to their relative forecast performance in the recent past. Latest data points are for the three months to November 2024 for private sector regular pay and 2024 Q4 for the indicator-based model estimates.
(b) Diamonds indicate projections or expectations for pay growth. Definitions of wage growth vary between each of the measures. The Agents' pay survey diamond shows respondents' expected average pay settlements in 2025, weighted by employment and sector. The DMP diamond shows average expected pay growth one year ahead for respondents to the January 2025 DMP Survey. Pay growth projections are for 2024 Q4 to 2025 Q4.

Within that, some individual indicators are stronger at present. Annual growth in median private sector pay derived from HMRC payrolls data (aqua line Chart 2.23), for example, pointed to pay growth of around 6.4% in the year to December and has shown limited signs of moderation in recent months.

Chart 2.23: Some indicators offer a firmer read for pay growth than others at present

Measures of annual private sector wage growth (a)



Sources: DMP Survey, HMRC, Indeed, KPMG/REC UK Report on Jobs, ONS and Bank calculations.

(a) Definitions of wage growth vary between each of the measures. Private sector regular pay growth is the ONS measure of private sector regular average weekly earnings growth (three-month average on same three-month average a year ago). DMP shows three-month average realised pay growth from the DMP Survey. KPMG/REC shows average starting salaries for permanent staff compared to the previous month. The KPMG/REC index is mean-variance adjusted to ONS private sector regular pay growth over 2002–19 and is advanced by 12 months, which better reflects the leading relationship between the KPMG/REC index and the ONS measure of pay growth. HMRC Real-Time Information (RTI) shows median of private sector employee pay growth. Indeed shows annual average job title matched pay growth for UK job vacancies. Latest data points are the three months to November 2024 for private sector regular pay, December 2024 for Indeed, HMRC RTI and the KPMG/REC index, and January 2025 for the DMP Survey.

…and while it is expected to moderate over 2025, it will remain elevated by historical standards.

Annual private sector wage growth in the MPC's baseline projection is expected to slow to around 3¾% by the end of 2025, as the easing in the labour market and past falls in inflation expectations feed through to lower wage growth (Chart 2.22). That is ½ of a percentage point higher than the November 2024 Report projection.

The higher expected path for pay growth in part reflects the steer from the latest Agent's annual pay survey. This points to some moderation in pay settlements in 2025 relative to 2024, to 3.7% (Chart 2.22 and Box F). This estimate is at the higher end of the range of 2%–4% indicated by the Agents' intelligence at the time of the November Report. Estimates from the Agents' pay survey have historically been a good predictor of realised pay settlements (Chart 2.24).

Chart 2.24: Estimates from the Agents' pay survey have historically been a good predictor of pay settlements

Measures of annual pay settlements (a)

Sources: Bank of England Agents, Incomes Data Research, Incomes Data Services, Industrial Relations Services, Labour Research Department and Bank calculations.

(a) The Agents' pay survey diamonds shows respondents' expected average pay settlements for a given year (as reported on the survey the year prior). Estimates are weighted by employment and sector. Latest diamond in purple shows respondents' expected average pay settlements for 2025. The Bank of England private sector settlements database is informed by intelligence gathered from the Bank's Agents, Incomes Data Research, Incomes Data Services, Industrial Relations Services, and the Labour Research Department. Companies were asked to state their average UK pay settlement for each year and their expected average UK pay settlement for 2025. Private sector pay settlements are a 12-month average based on monthly data.

The latest evidence from the DMP Survey is also consistent with a softening in wage growth across all sectors, to around 4% in aggregate over the year ahead. Expected wage growth in consumer services companies, in particular, remains elevated at around 5%. The latest DMP survey also asked firms about their expected response to the announced increase in employer NICs, with a number reporting they expected it to result in some downward pressure on wage growth. As outlined in Box D, however, there is evidence that suggests the NLW may act as a constraint on that adjustment within some sectors.

> **The outlook for inflation will also be influenced by the extent to which firms pass higher costs into prices in order to maintain or rebuild their profit margins.**

While the evidence is mixed, firms appear not to have passed cost increases fully into prices in recent years (Section 2.5 in the **November 2024 Report**). The extent to which firms pass higher labour costs, from higher wages and increases in employer NICS, into prices in coming quarters will depend in part on the strength of demand in the economy as well as the competitive pressures they face. At present, the scope for such pass-through appears to be

limited. The Bank's Agents' intelligence suggests that firms in consumer-facing industries expect to raise prices in 2025, though many think they will need to do so gradually so as not to disrupt sales. In addition, recent surveys suggest that firms may have to accept lower profit margins in response to the higher rate of employer NICs (Chart B in Box D).

2.6: Inflation expectations

Households' inflation expectations rose somewhat over the second half of 2024…

Inflation expectations can influence CPI inflation through influencing wage and price-setting behaviour. The MPC monitors a range of indicators – including surveys of households and companies as well as those derived from financial market prices – to assess whether inflation expectations remain consistent with meeting the 2% inflation target sustainably in the medium term.

Having fallen significantly since the end of 2022, survey measures of household inflation expectations have risen somewhat in recent months, albeit to varying degrees. The Bank of England/Ipsos Inflation Attitudes Survey measure of median one year ahead inflation expectations rose to 3.0% in November, while the medium-term expectations measure also ticked up (left panel of Chart 2.25). The Citi/YouGov measures of households' short-term and medium-term inflation expectations have risen more materially over recent quarters and were 3.5% and 3.7% respectively in January (right panel of Chart 2.25).

Chart 2.25: Some measures of household inflation expectations have increased over 2024 H2, though remain below their pandemic-era peaks

Measures of household inflation expectations (a) (b)

Sources: Bank/Ipsos Inflation Attitudes Survey, Citigroup, YouGov and Bank calculations.

(a) Left panel shows the median responses from the Bank/Ipsos Inflation Attitudes Survey. Data shown are the one-year and five-year ahead inflation expectations measures. Dashed lines represent the series averages over 2010–19. A methodological break occurred during the Covid-19 pandemic that means a degree of caution should be taken when making long-run comparisons with these data, for more information please see the methodology notes linked in **the latest IAS release for November 2024**. The latest data points are for 2024 Q4.
(b) Right panel shows the monthly Citi/YouGov survey data. Data shown are the one-year and 5–10 year ahead inflation expectations measures. Dashed lines represent the series averages over 2010–19. The latest data points are for January 2025.

…however, household inflation expectations remain broadly in line with their economic drivers.

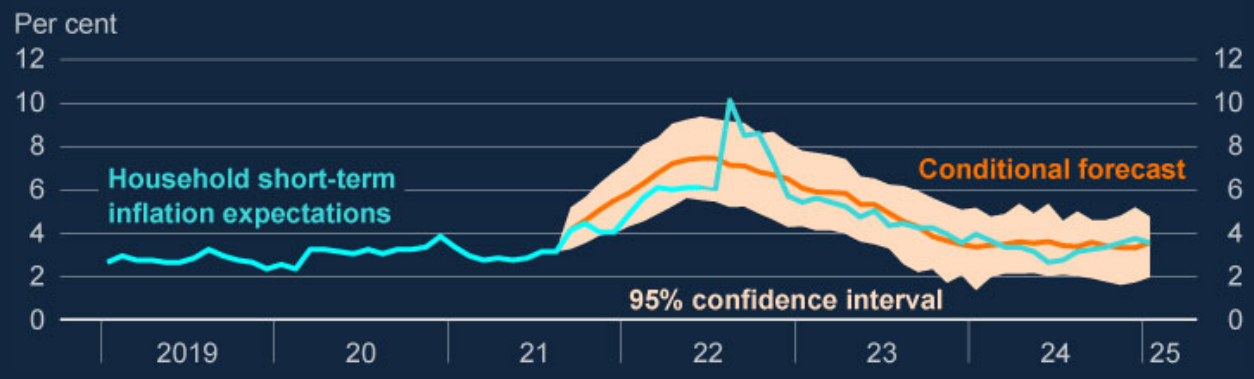
It is possible that following the recent period of high inflation households are more attentive to price rises. Google searches for the term inflation, for example, remain elevated. In addition, studies suggest that households' inflation expectations are particularly influenced by price changes for items that they buy more frequently, such as food and energy (**Anesti et al (2024)**, **D'Acunto et al (2021)** and **Coibion and Gornichenko (2015)**). Given the recent price rises in these components, they may be an important factor in the observed rise in household inflation expectations.

Consistent with that, Bank staff analysis suggests the developments in short-term household inflation expectations are broadly in line with what might be expected given developments in the wider economy. Chart 2.26 shows a comparison between households' average reported expectations for inflation one year ahead and a model-based estimate of how expectations

might have been expected to evolve since August 2021 based on a number of key economic factors affecting inflation expectations (in orange). The recent rises in the Citi/YouGov measure leave it broadly in line with the model-based estimate for end-2024.

Chart 2.26: Short-term household inflation expectations have largely evolved in line with economic factors

One year ahead household inflation expectations and conditional model-based forecast (a)



Sources: Citigroup, ONS, YouGov and Bank calculations.

(a) The orange line shows a forecast for one year ahead household inflation expectations from August 2021 conditional on observed economic outturns since then. The conditional forecast is estimated using a Bayesian vector autoregression (BVAR). The BVAR is conditioned on the evolution of inflation, employment, AWE (private sector regular pay), GDP and exchange rates. The latest data points shown are for January 2025.

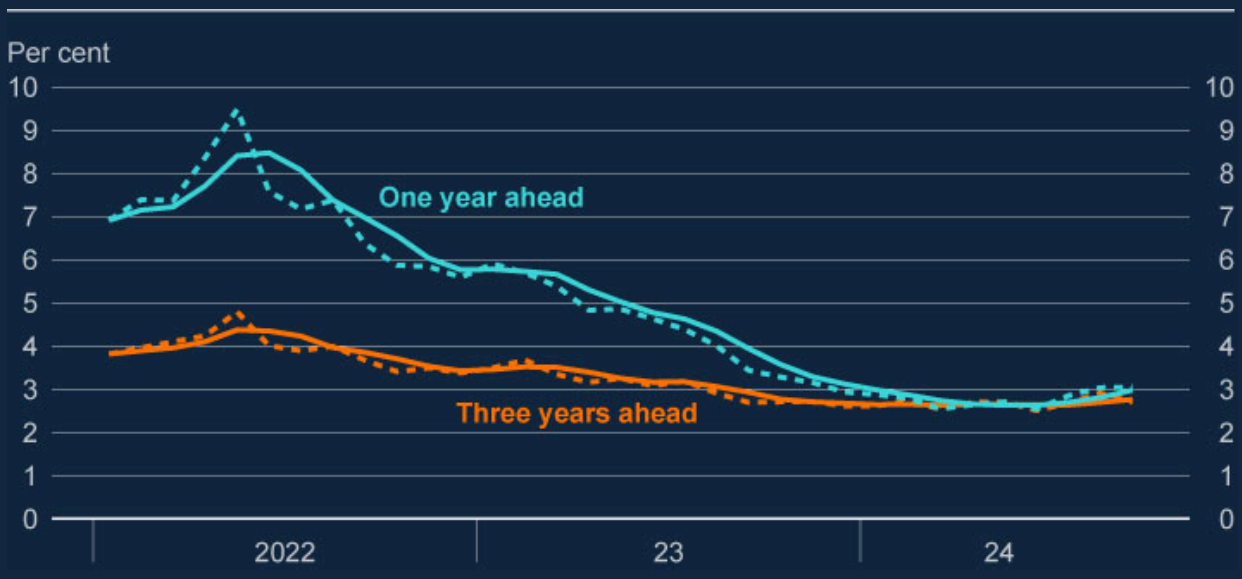
Businesses' medium-term CPI inflation expectations have been broadly stable…

Firms' one year and three year ahead expectations for CPI inflation, as measured by the January DMP Survey, have fallen back from their peaks in 2022. Medium-term CPI inflation expectations have been little changed over 2024 (Chart 2.27). The Deloitte CFO survey measure of two-year CPI expectations was 2.4% in Q4, slightly higher than the 2.3% figure reported in Q3.

DMP Survey respondents' expectation for their own price inflation in a year's time remained elevated at around 4%, however, and has edged up slightly in recent months. This expectation is similar to firms' reported own price inflation for the past year, suggesting that respondents do not expect much moderation in their rate of price inflation in the coming year. Intelligence from the Bank's Agents suggests that a combination of changes to the NLW, employer NICs and the introduction of the EPR may push prices up over the next year – especially for the food and drink, hospitality, leisure and care sectors (Box F).

Chart 2.27: Businesses have reported broadly stable expectations for CPI in three years' time

Firms' short-term and medium-term expectations for CPI inflation (a)



Sources: DMP Survey and Bank calculations.

(a) Solid lines show three-month moving averages and dashed lines show the single-month value. One year and three years ahead CPI inflation expectations are responses to the question: 'What do you think the annual CPI inflation rate will be in the UK, one year from now and three years from now?'. The latest data are for January 2025.

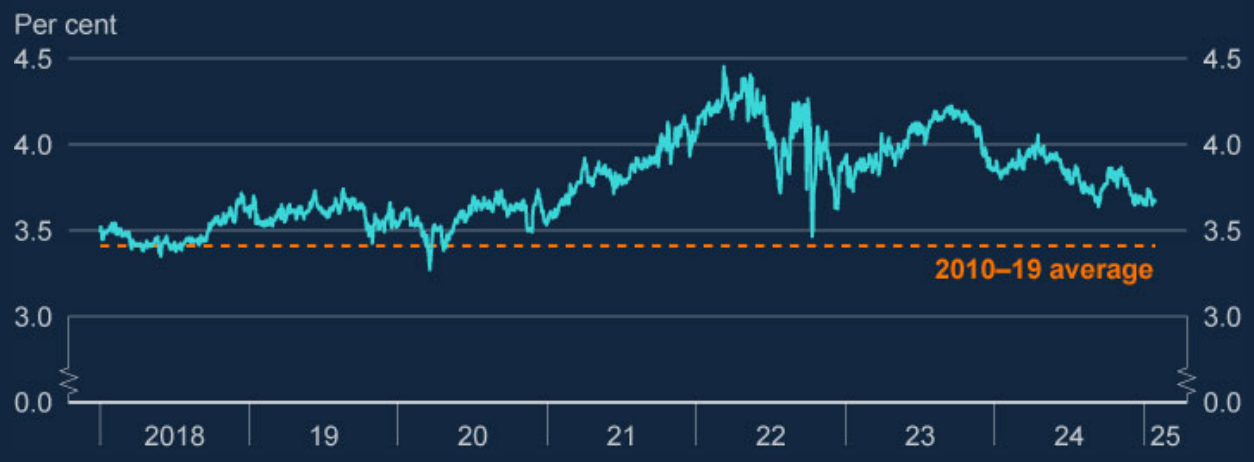
…and an indicator of market-based inflation compensation has trended down over 2024, though it remains above its pre-Covid average.

A measure of medium-term inflation compensation in financial markets has trended downwards over the course of 2024 (Chart 2.28). Some market contacts partly attributed the decline to reduced concerns around inflation persistence and the perceived restrictiveness of monetary policy. The measure remains above its 2010–19 average (Chart 2.28), with intelligence from market contacts suggesting this reflects perceptions of some continuing upside risk from inflation persistence in light of developments in services CPI inflation and pay growth.

The median respondent in the January Market Participants Survey expected CPI inflation of around 2.5% one year ahead, up slightly from 2.4% in December. Median five year ahead expectations were unchanged at 2%, although responses remain skewed to the upside of that estimate.

Chart 2.28: Five year ahead inflation compensation based on swap rates fell over 2024

RPI-reform adjusted measure of five-year, five-year forward inflation compensation (a)



Sources: Bloomberg Finance L.P. and Bank calculations.

(a) Dashed line represent the series average over 2010–19. Market-derived inflation compensation rates for average UK RPI inflation over a five-year period starting five years into the future. It is derived by adjusting the five-year, five-year rate to account for UK RPI reform. From 2030, UK RPI will be aligned with the CPIH measure of consumer prices. At present, the wedge between the current definition of RPI and CPIH affects the unadjusted series. This measure is calculated by adding a scaled market-derived estimate of the impact of RPI reform onto the unadjusted rate. That is calculated as the difference between the closest one-year forward rates before and after the planned RPI reform date (currently the four-year, one-year rate and the six-year, one-year rate) on a three-month daily rolling average basis, and the adjustment is applied to the five-year forward period impacted by the reform. The latest data are for 28 January 2025.

The MPC will continue to monitor closely developments in inflation expectations measures.

As noted in Section 2.5, CPI inflation is expected to rise quite sharply this year, accounted for predominantly by further rises in energy prices alongside a number of other regulatory changes. Although households' inflation expectations appear to be in line with their fundamental economic drivers, there is a risk that higher expectations add to the persistence of inflationary pressures (Key judgement 3 in Section 1).

Box C: The potential effects of trade tariffs on the UK

The US administration has made various announcements on new tariffs on imports from its trading partners, to which some other governments have responded. The MPC's forecast was finalised before these latest US tariffs were announced and it remains unclear what the overall landscape for US and other global tariffs will ultimately look like. This box therefore sets out a framework for how US tariffs on other economies could affect UK output and inflation, discussing the main transmission channels and their likely directional impact. While tariffs are likely to lower UK economic activity, the overall effect on UK inflation is unclear. Both the size and the direction of any net effect on UK inflation, and hence also any appropriate monetary policy response, are sensitive to changes in other countries' trade policies and the relative strength of different economic channels, particularly the impact on exchange rates.

The US is the UK's most important trade partner after the EU.

In 2023, 22% of UK gross exports were sold on the US market, accounting for 7% of UK GDP or about £190 billion. This captures the UK's direct trade links. Given the complex nature of global supply chains, some of the UK's exports to other countries are used as intermediate inputs to goods and services ultimately destined for the US market. Based on value-added trade statistics, this could account for an additional exposure in the region of ⅔% of GDP or about £20 billion.

Almost 70% of the UK's exports to the US are services exports, which would not be directly affected by a potential imposition of US goods tariffs. However, restrictions on services trade are in principle also possible. Moreover, some services exports are contingent on UK goods exports, such as after-sales services for UK goods sold to the US. UK services exports to other countries may also be affected if foreign firms that export to the US reduce their demand for UK services in the event of US tariffs.

In the near term, higher trade policy uncertainty could weigh on investment.

The prospect of material changes to existing trading arrangements, even before specific policies are announced or implemented, can impact firm behaviour (**Caldara et al (2020)** and **Handley and Limão (2022)**). Since many investments are irreversible, when there is uncertainty about global trade policies firms involved in global supply chains have an incentive to wait and see (**Dixit and Pindyck (1994)**). Indices of trade policy uncertainty have picked up materially since the US election (Section 2.1). Lower business investment could weigh on aggregate demand, reducing economic activity and inflationary pressures.

US tariffs could be inflationary or disinflationary for the UK depending on other countries' trade policies and the relative strength of different transmission channels.

US trade tariffs could affect the UK through several key channels outlined in Table 1. Most of these channels would act to lower UK economic activity. However, some channels are likely to reduce UK inflation while others might push up on it. Whether US tariffs might be inflationary or disinflationary overall for the UK would depend on the relative strength of the different channels outlined in this box, as well as on developments in other countries' trade policies.

Table 1: Potential effects of US tariffs on the UK

Channel	UK activity	UK inflation	Explanation
Expenditure switching			US demand for UK exports weakens.
Weaker global demand due to counter-tariffs			Additional trade distortions weigh on global demand, weakening demand for UK exports.
Supply chain disruptions			Supply chain disruptions due to missing components could lead to short-term price spikes.
Trade diversion			Other countries lower prices of exports previously destined for US.
Exchange rate movements			Sterling could appreciate or depreciate depending on other countries' trade policies and changes in global risk sentiment.
Long-term supply chain reconfiguration			Reorganisation temporarily reduces global supply capacity and increases price pressures.
Lower competition and knowledge transfers			Reduced trade openness weighs on global potential supply growth.

US tariffs are likely to lead to expenditure switching by US consumers and firms, which would reduce demand for UK exports and weigh on UK activity and inflation.

US tariffs on imports from abroad are expected to raise the cost of imports relative to US-produced goods faced by US firms and consumers. However, the magnitude of this effect is uncertain because foreign producers may lower their prices in response to higher tariffs to remain competitive. The large size of the US market makes some degree of margin compression for foreign producers likely, although this would also depend on the extent to which US consumers are able to switch to domestically produced goods.

Higher import costs could lead US firms and households to rebalance their purchases towards domestically produced goods, and away from imports including from the UK. US tariffs on imports from other countries may also lead to a reduction in demand for intermediate inputs from the UK from those countries. In the medium term, US activity is also likely to be weaker because tighter US monetary policy might be required to reduce inflationary pressures due to tariffs, further weighing on global demand. All else equal, lower global demand for UK exports would reduce UK activity and inflationary pressures.

> **Counter-tariffs could weigh on global demand, while supply chain disruptions could lead to price spikes.**

Other countries may respond to US tariffs by imposing a number of trade policies including counter-tariffs on imports from the US. Such additional trade barriers would lead to further distortions in trade flows and prices, which could result in a reduction in global aggregate demand, weighing further on demand for UK exports and hence on UK activity and inflation. At the same time, supply chain disruptions due to rising global trade barriers could lead to price spikes that cascade through production networks, which might push up on global and UK prices.

> **Any new US tariffs are likely to result in trade diversion, which could reduce UK import costs.**

With access to the US market more expensive, exporters in other countries might seek alternative consumers for goods they can no longer sell as profitably in the US. This is likely to require them to lower their export prices, reducing UK inflation. Assuming no change in UK trade policy, falls in UK import costs due to such trade diversion effects would increase real incomes and consumption of UK households. However, lower relative prices for imported goods could reduce demand for domestically produced substitutes, leaving the overall effect on UK activity ambiguous.

Some countries may choose to impose broader defensive trade measures to mitigate a potential reduction in demand for domestically produced goods due to such trade diversion effects. In that scenario, the effects of trade diversion would become more intense for countries that do not impose such measures. This would strengthen the

positive effects on domestic real incomes and disinflationary pressure from trade diversion for those economies. At the same time, it might lead to more intense competition for UK producers of tradable goods.

Sterling might appreciate or depreciate depending on other countries' trade policies and the evolution of global risk sentiment.

Absent any changes in other countries' trade policies, the US dollar is likely to appreciate in response to higher US tariffs. Higher import costs would reduce US demand for foreign goods, resulting in lower US demand for foreign currencies to purchase these goods. That said, the dominant role of the US dollar in international trade is likely to limit the size of this effect. Many internationally traded goods are priced in dollars, and hence the US typically uses dollars rather than foreign currency to purchase imports, limiting any moves in the dollar exchange rate in response to changes in US tariffs. Sterling would be likely to depreciate in this scenario, pushing up on UK import and consumer prices.

If other countries respond by imposing counter-tariffs on imports from the US, the US dollar could depreciate. The counterpart of US dollar depreciation would be an appreciation of sterling alongside other currencies. A higher sterling exchange rate could add to the fall in US demand for UK exports to some extent, while also reducing the cost of UK imports, pushing down on UK inflation. Pass-through to UK import and consumer prices could be relatively strong in this case because the exchange rate would move in response to a global shock, but this would also depend on the size of the exchange rate move (see Box D, **November 2024 Report**).

That said, in the event of a global escalation of trade tariffs, exchange rates may also respond to changes in risk perceptions and risk aversion in global markets. As long as increased trade barriers do not negate the US dollar's role as the dominant currency in international trade and as a safe haven for global investors, the dollar exchange rate may be supported by safe haven inflows. This could partly or fully offset changes in exchange rates due to trade tariffs, leaving significant uncertainty around the sign of exchange rate moves in different trade policy scenarios. The response of the sterling exchange rate is likely to be a key determinant of the overall impact of changes in global trade policies on UK inflation, particularly in the near term.

In the longer term, an escalation that contributed to global trade fragmentation would weigh on potential growth around the world.

A protracted global escalation of tariffs and other trade barriers could result in more significant and persistent disruption. In such a scenario, firms may want to reorganise supply chains, reducing their length and complexity where possible to mitigate

exposure to actual and potential future trade barriers. While a gradual and orderly reconfiguration of global trade relationships might have modest effects on price pressures, a disorderly fragmentation could add to global inflationary pressures.

In the longer term, fragmentation of the global economy is likely to weigh on global potential growth. Openness fosters knowledge spillovers and increases competition, both of which tend to raise productivity growth. Putting that process into reverse could persistently reduce the supply capacity of the global economy.

> **The MPC will continue to monitor developments in global trade policies and their implications for UK growth and inflation.**

The effects of global trade tariffs on the UK economy are complex. Tariffs and other trade barriers would likely have adverse effects on UK activity. However, the net effect on UK inflationary pressures is highly uncertain. Consequently, the direction of any appropriate monetary policy response is unclear without detailed information on the trade policies enacted and analysis of the relative strength of different economic channels. The MPC will continue to monitor developments in global trade policy.

Box D: Monitoring the impacts of changes to National Insurance contributions

The Government set out its tax and spending plans in Autumn Budget 2024. The MPC's provisional assessment was that the combined effects of the new measures would boost the level of GDP by around ¾% and CPI inflation by just under ½ of a percentage point at their peak, relative to the projection in the August 2024 Report (see Box B, **November Report**).

The increase in employer National Insurance contributions (NICs) was the largest change to taxation in the Autumn Budget. From April 2025, the NICs rate that firms pay will increase from 13.8% to 15%, while the earnings threshold at which NICs are levied on employers will be lowered from £9,100 to £5,000. These changes are partly offset by an increase in the Employment Allowance which employers can claim on their NICs liabilities. Around the time of the Autumn Budget, the Government also accepted the recommendation of the Low Pay Commission for a 6.7% increase in the NLW main rate in April 2025. At an aggregate level, Bank staff estimate the expected net effect of the changes to NICs are to increase firms' employment costs by 1.9 percentage points. In addition, the increase in this year's NLW rise is estimated to equate to a further 0.2 percentage point increase in employment costs.

How firms choose to respond to these changes has implications for price and wage-setting dynamics across the economy and therefore the outlook for inflation. Recent survey evidence helps to shed some light on how firms are considering their choices. This box sets out the latest analysis of the impact of the changes to employer NICs and their interaction with the NLW.

> **Economic theory suggests that more of the adjustment to changes in NICs tends to come through real wages than profits.**

Increases in employer NICs represent an increase in the costs of production for businesses. In response, employers may act to absorb the extra costs within their profit margins, pass on the cost increases to consumers through higher prices, or mitigate the impact of cost increases by reducing nominal wages or employment. The combination of lower nominal wages and higher prices reduces real wages.

The extent to which costs ultimately fall on workers and consumers, through lower real wages or employment, or on firms, through lower profits, depends on the relative supply and demand elasticities of labour. These elasticities calculate the responsiveness of labour demand and supply to changes in the wage rate. A more

elastic labour demand indicates that employers will want considerably fewer employees for a small increase in wages, whereas a more elastic labour supply suggests that considerably more employees will exit the labour market for a small decrease in wages.

The academic literature points to a relatively higher elasticity of demand for labour, which would mean more of the adjustment is likely to come through real wages or employment than profits (**Office for Budget Responsibility Economic and fiscal outlook – October 2024**). Empirical estimates of previous changes to NICs provide a wide range of estimates of the degree of pass-through across the possible margins of adjustment (**Melguizo and Gonzalez-Paramo (2013**), **Lehmann et al (2013**), **Saez et al (2019)**), and previous episodes often included a combination of policy changes that differ from the current one. For instance, the 1999 increase in employer NICs in the UK was accompanied by an increase in the earnings threshold at which employers had to pay. The magnitude and speed of these effects is also likely to depend on the cyclical state of the economy as well as recent shocks that may still be having an impact.

> **The interaction of a higher contribution rate with both a Lower Earnings Limit and a higher NLW may affect how firms respond this time.**

There are factors in the current environment that may limit the extent to which firms can push down on nominal wages in response to the employer NICs increase. Given the lowering of the threshold at which NICs are levied on employers, the increase in labour costs will be larger for lower-paid workers. Bank staff estimate that labour costs are increasing by over 5% for the bottom 5th–10th percentiles of the pay distribution, compared with just over 1% for the top 95th–100th percentiles of the distribution (top panel of Chart A). In turn, the NLW is likely to limit the scope for firms to adjust wages for this subset of employees. As a result, firms with more employees paid at or around the NLW may have to make more use of the remaining margins of adjustment. Academic literature (**Popp (2023)**) concludes that the elasticity of demand is greater for low skilled workers, which could further compound the impact at the bottom end of the pay distribution.

Employment may have a more prominent role as a margin of adjustment than otherwise, as the sectors that are most affected by the NICs increase also tend to be more labour intensive. The bottom panel of Chart A suggests that consumer-facing sectors, that typically tend to be more labour intensive, are most affected, with construction being the least affected.

Chart A: The percentage increase in labour costs is higher in the lower end of the pay distribution and for more consumer-facing sectors

Impact on weekly employer labour costs due to the NLW and NICs increase, by percentile of the labour cost distribution and by sector (a)

Sources: Annual Survey of Hours and Earnings (ASHE) and Bank calculations.

(a) This is based on Bank staff analysis of employer returns from the ASHE microdata, along with modelled changes of the impact of the NLW and NICs changes. This work was undertaken in the ONS Secure Research Service using data from ONS and other owners and does not imply the endorsement of the ONS or other data owners. The data used for the analysis are for 2024 and have been uprated to 2025 levels using forecast earnings growth.

Recent survey evidence continues to suggest firms will respond along several margins.

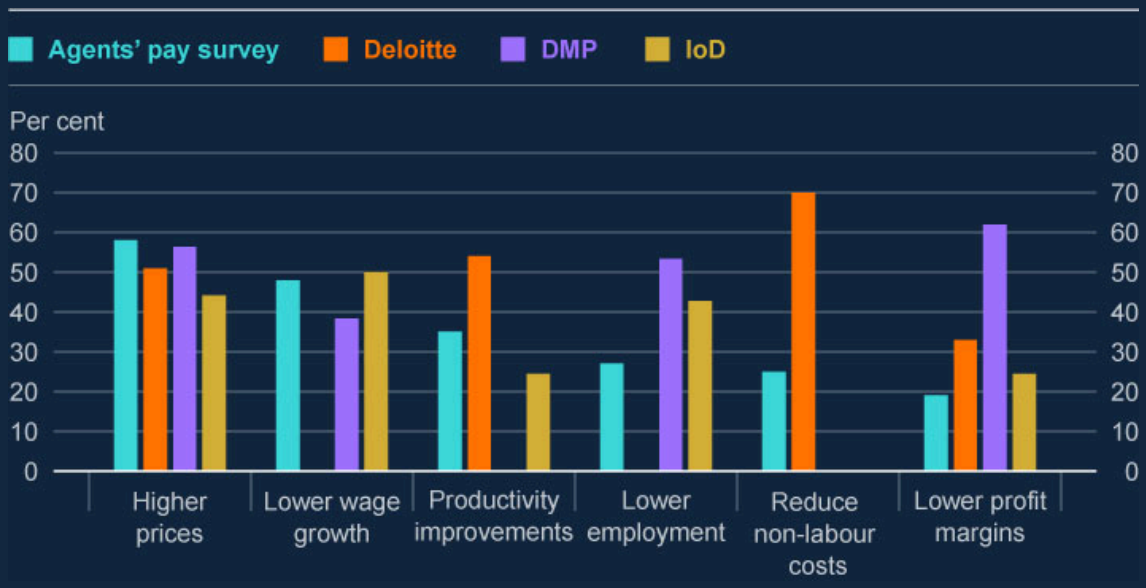
Since the November Report several surveys have asked firms how they plan to respond to the changes to employer NICs, with some also asking about their interaction with the NLW (Chart B).

In the latest DMP Survey, a majority of firms expected to use either two or three different margins of adjustment in combination. The relative ranking of these different margins was similar across sectors. Over half of the firms expect to respond to the

cost increase by lowering profit margins, increasing prices, or lowering the number of employees. Lowering wages is also likely to be a margin of adjustment, reported by around one-third of firms. Bank staff analysis based on the DMP Survey finds that firms more exposed to the NLW are more likely to plan to lower employment and are less likely to lower wages.

Chart B: Firms plan to use a variety of margins of adjustment as a response to the NICs increase

Proportion of firms reporting responses to Autumn Budget policy changes by margin of adjustment (a) (b) (c) (d)



Sources: Agents' pay survey, Deloitte, DMP Survey, IoD and Bank calculations.

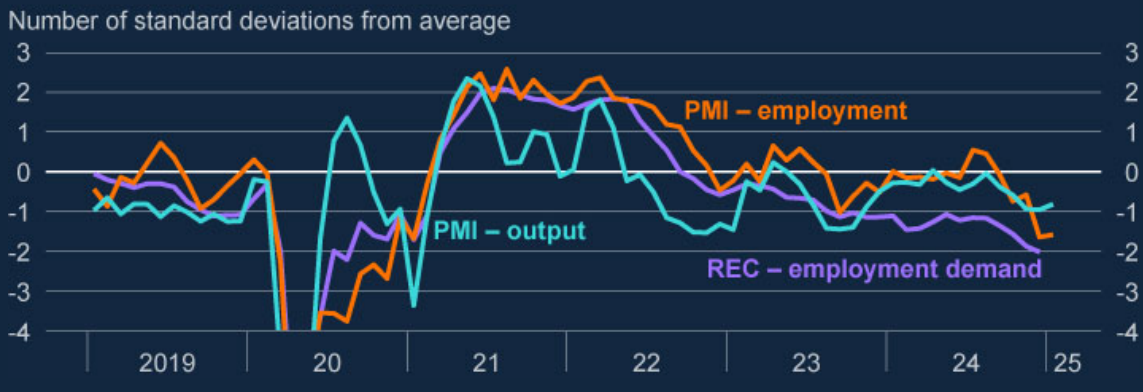
(a) Agents' pay survey results are based on the question: 'In response to the April 2025 increases in employers' National Insurance contributions (NICs) and National Living Wage/National Minimum Wage (NLW), and other changing labour market policies (including proposals in the Employment Rights Bill), what actions do you plan to take (select up to three that are most relevant/significant to you)?'. Firms are allowed to select multiple options, although limited to three options, therefore the percentages do not add up to 100. Responses are weighted by firm industry and size. Responses are for November and December 2024.
(b) Deloitte CFO survey results are based on weighted-average ratings on a scale of 0–100 for how likely chief financial officers are to pursue the following strategies in response to the forthcoming rise in employer National Insurance contributions. Zero stands for not pursuing at all and 100 stands for pursuing to the greatest extent. Latest data are for 2024 Q4.
(c) DMP results are based on the question: 'How do you expect your business to respond to the changes to employer National Insurance contributions announced in the November 2024 Budget?'. Firms are allowed to select multiple options, therefore the percentages do not add up to 100. Responses are weighted by firm industry and employment. Responses are for January 2025.
(d) IoD results are based on responses the question: 'You said the changes will increase your employer National Insurance bill. How do you plan to respond to the resulting higher costs of employment?'. Latest data are for November 2024.

The Agents' annual pay survey (see Box F) also asked firms to consider the impact of changes in employer NICs and the NLW. It reported that firms are planning to respond to these announced policies through a range of margins (Chart B). Pass-through of costs into higher prices and lower wage increases than would otherwise be the case were the most common responses. The Agents' pay survey also suggested that the NLW increase is the most significant factor that is exerting material upwards pressure on pay settlements this year. In the Agents' survey, firms in consumer-facing services and manufacturing sectors are those most likely to report considering reductions in headcount or working hours in response to the changes to NICs and the NLW increase, but few have made final decisions.

Broader surveys of employment intentions have also weakened, with some respondents citing the impact of the upcoming increase in NICs (Chart C). In the PMI survey, respondents report a sharper deterioration in hiring intentions than the weakening in reported output growth. The latest REC survey also highlighted that the Budget had led some firms to limit or halt recruitment activity as they reassessed their staffing needs. Overall, the evidence from surveys since the Budget highlights the risk that more adjustment to the NICs changes might come through lower employment than in the central assessment in the forecast.

Chart C: Business survey measures suggest a recent easing in employment intentions

Survey indicators of UK employment and output (a)



Sources: KPMG/REC UK Report on Jobs, S&P Global/CIPS, and Bank calculations.

(a) Standard deviations from averages between 1998–2019. Latest data for both the composite output and employment PMIs are Flash estimates for January 2025 and for the REC index of staff demand are for December 2024. For ease of viewing the data, the axis has excluded the Covid trough in these measures.

The MPC continues to judge that firms will utilise a number of different margins in response to the change in NICs but with a slightly bigger impact on prices in the near term.

Survey evidence and Bank staff analysis since the November Report continues to support the judgement that firms are likely to use a number of different margins in response to the change in NICs. The MPC has reviewed Bank staff analysis and evidence from the latest surveys, and there have not been material changes to the treatment in the forecast. The increase in NICs is expected to have a marginally larger impact on prices in the near term than at the time of the November Report.

Results from some of the latest surveys, as well as the possibility that the NLW could limit the scope to which certain firms can use nominal wages as a margin of adjustment, highlight the risk that employment may be more affected than in the central assessment in the forecast. There remain considerable uncertainties around how firms will respond, however, which the Committee will continue to monitor.

Box E: The supply side of the economy

An economy's supply capacity, or potential supply, is determined by the amount of labour and capital available, and the efficiency with which these factors can be combined. The supply side of the economy determines the level of output that, in the absence of other shocks, generates neither excess nor insufficient domestic inflationary pressures. It is therefore an important consideration for monetary policy. The economy's supply potential cannot, however, be directly observed. Real-time estimates are inherently uncertain and the data underpinning them prone to revision.

Given the latest data, the uncertainties surrounding them, and what they imply for supply growth in recent years, the MPC has focussed more of its attention in this stocktake on judging the current cyclical position of the economy. This box sets out the MPC's view of current potential output, and how that relates to its assessment of spare capacity and developments over the forecast period.

In light of the latest LFS data, which have been heavily revised due to partially updated population data, the level of potential labour supply is judged to be higher. But as this has not been accompanied by similar upward revisions to GDP this suggests that the level of potential productivity is weaker than previously estimated. A review of the evidence on the factors that the MPC judged to have previously been affecting potential productivity cannot fully account for its recent weakness.

While revised labour market data has resulted in the estimated composition of supply growth being reevaluated over 2024, the growth rate of potential GDP is also thought to have slowed over the past year. This assessment stems from the combination of slowing GDP growth and limited evidence of spare capacity opening up. Four-quarter potential supply growth is estimated to have declined from around 1½% at the start of 2024 to around ¾% by the first quarter of 2025. There are significant uncertainties around this assessment and, therefore, the extent to which recent weakness in GDP growth reflects slower supply or demand growth (Key judgement 2 in Section 1).

> **Employment and hours worked are now higher in the latest data vintage, although ongoing data issues mean estimates remain highly uncertain.**

There remains considerable uncertainty over statistics derived from the Labour Force Survey (LFS), reflecting low survey response rates. As a result, the MPC has reduced confidence in key labour market measures, including levels of employment, participation and average hours worked, as well as the signal implied by these measures for the economy's supply potential.

The ONS continues to revise the LFS data to reflect updated population estimates. In December 2024, the LFS was reweighted to reflect population data based on 2022 mid-year estimates, implying an upward revision to the estimate of the UK's population in the LFS of around half a million people. This update does, however, not account for the most recent estimates of migration published by the ONS in November 2024 or the latest set of ONS National Population Projections (NPPs) published in January 2025 that have not yet been incorporated into the LFS. A simple estimate of the LFS population based on the latest NPP growth rates points to potential upward revisions of around a further ½% by mid-2024, although this figure is subject to several assumptions and a large degree of uncertainty.

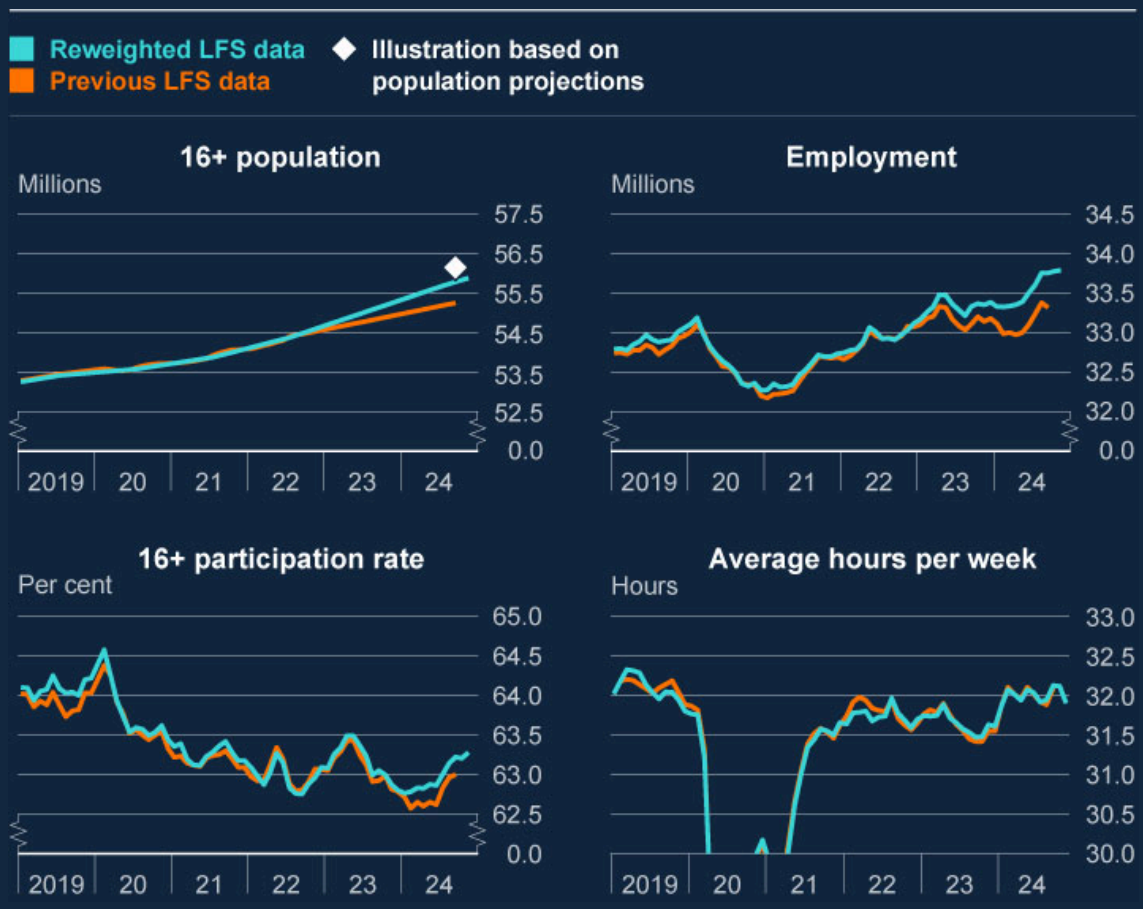
The December 2024 revisions to the LFS population in turn mean that the size of the labour force and the level of employment in the LFS are both higher than previously estimated. The level of employment and the labour force were both revised up by around 1.2%. The reweighting has also led to small upward revisions to the estimated labour force participation rate (bottom left panel, Chart A).

Previously, the level of employment implied by the LFS data had been substantially lower than that implied by alternative measures such as Workforce jobs or HMRC payroll employees. The recent reweighting of the LFS data has closed around half the gap between these measures, aided also by downward revisions to the Workforce jobs employment measure. If LFS employment were to have grown in line with the HMRC payroll or Workforce jobs data since end-2019, it would now be around 1%–3% higher.

In addition to revisions raising the levels of these variables there has also been stronger than previously estimated increases in them over the past year. Quarterly LFS employment growth has been 0.4 percentage points stronger on average than expected at the time of the February 2024 Report. The participation rate has risen by 0.2 percentage points over the year to 2024 Q3 compared with expectations of a 0.2 percentage points decline at the time of the February 2024 report. Although largely unchanged by the recent set of revisions, average hours worked have also grown strongly over the past year. In the four quarters to 2024 Q3, average hours worked picked up sharply to around the level seen immediately before the pandemic.

Chart A: The estimated population, employment and participation are all higher after recent revisions

Revisions to selected labour market variables (a)



Sources: ONS and Bank calculations.

(a) Data labelled as reweighted LFS show the profiles consistent with the latest LFS data which extends to the three months to November. The previous vintage refers to the LFS data prior to reweighting and extends to the three months to September. The illustration of the LFS population consistent with the latest National Population Projections shown in the white diamond is constructed by applying the growth rate in the NPPs since mid-2022 to the LFS population at that time. This exercise embeds an implicit assumption that the ratio of the total population to that used for the LFS's purposes remains fixed and the result is sensitive to this assumption. For example, if this ratio were to fall it would reduce the increase in the LFS population implied by the latest population projections.

> **The MPC judges that these upward revisions, as well as the strength in recent data, reflect stronger potential labour supply as well as demand.**

The MPC's overall assessment of potential labour supply is informed by a range of data including survey indicators of labour market tightness (Section 2.4). Based on these data – as well as recent work by Bank staff comparing labour market tightness to

its estimated equilibrium levels – the MPC judges that the labour market is broadly in balance.

Given this judgement, much of the strength in recent labour market data over the course of 2024, as well as the upward revisions, are deemed to reflect higher potential labour supply rather than excess labour demand. There is a degree of uncertainty around this assessment, however, given the ongoing issues with the LFS data highlighted above.

Potential labour supply growth has been strong but is expected to slow over the forecast period.

The MPC now judges that potential labour supply increased by 2.2% in 2024, its fastest rate of growth since at least 1997, aside from the volatile pandemic period (Table 1). This strength is in part due to population growth which has been driven by historically high levels of net migration. Potential labour supply growth in 2024 is judged to be around 1.7 percentage points higher than assumed at the time of the February 2024 report. Of this upwards revision, population revisions and higher trend average hours growth account for 0.7 percentage points and 1.1 percentage points, respectively. Potential labour supply growth is project to slow to 0.5% in 2025, before settling around ¾% per annum in the second and third years of the forecast period.

The latest population projections point to slower growth in coming years.

Population growth is expected to continue to be the largest driver of labour supply growth over the forecast period. As set out above, the latest LFS data do not yet incorporate the national population projections that were released in January 2025, which will only be reflected in the LFS in coming quarters. However, these higher growth rates have been incorporated into the MPC's projection for population growth, which converges to the rate of growth implied by the latest NPPs over the second and third years of the forecast. The MPC's projections are based on annual LFS-relevant population growth slowing from 1.2% in 2024 to around 1% by 2027.

Potential participation is still projected to fall slightly over the forecast horizon.

The potential participation rate has been revised up slightly, to reflect the higher starting point implied by reweighted LFS data. The MPC's assessment of trend participation over the forecast horizon is broadly unchanged, however. As in previous assessments of supply, demographic factors will continue to weigh on the participation rate. In addition, the impacts of the recently increased rates of National Insurance contributions (see Box D), which were incorporated into the November 2024 forecast, are also expected to weigh on participation.

Table 1: Decomposition of estimated potential supply growth (a)

	Average				Projection			
	1997–2007	2010–14	2015–19	2020–23	2024	2025	2026	2027
Potential supply growth (per cent)	**2.9**	**1.4**	**1.8**	**0.7**	**1.5**	**1.0**	**1.7**	**1.5**
of which, potential labour supply growth	0.7	1.3	1.1	0.2	2.2	0.5	0.8	0.8
of which, population	0.7	0.8	0.6	0.8	1.2	1.1	1.1	1.0
of which, participation	0.1	0.0	0.2	-0.4	0.1	0.3	-0.1	-0.1
of which, unemployment (b)	0.2	0.1	0.3	-0.1	0.0	-0.1	0.0	0.0
of which, average hours (c)	-0.3	0.3	0.0	0.0	1.0	-0.8	-0.2	-0.1
of which, potential productivity growth	2.2	0.2	0.7	0.5	-0.7	0.5	0.9	0.7
of which, capital deepening (d)	0.6	-0.3	0.5	0.3	-0.4	0.5	0.4	0.4
of which, total factor productivity (d)	1.6	0.5	0.2	0.2	-0.4	0.0	0.5	0.3

(a) Percentage point contributions unless otherwise stated. Contributions may not sum to the total due to rounding. Data for 2025 onwards are projections consistent with the MPC's forecast.
(b) Positive numbers indicate that a fall in the equilibrium unemployment rate has increased potential labour supply.
(c) Recent strength in average hours worked is expected to unwind such that they decline towards their structural trend which results in negative contributions over the forecast horizon.
(d) The productivity decomposition is based on a growth-accounting framework using a constant returns to scale Cobb-Douglas production function, with the elasticity of output with respect to capital set to 1/3. Total factor productivity is a residual.

What do these judgements imply for potential productivity?

Hourly productivity has been declining in the year to 2024 Q3.

The latest data indicate that output per hour fell by around ½% in the two years to end-2023, after which it began to decline more quickly and has since fallen by 2.4% in the four quarters to 2024 Q3. Mechanically this has resulted from moderate GDP growth of

0.9% being outpaced by much stronger growth in total hours worked. By contrast, productivity per worker, based on the LFS measure of employment, has been more stable. That said, alternative data sources imply stronger employment growth since mid-2021, which would also reduce measured productivity on a per worker basis. In time, this may be reflected in the LFS data as they incorporate the latest National Population Projections.

Potential productivity is judged to have been much weaker than previously estimated.

Since the MPC judges that recent outturns and the revisions to the LFS have increased estimates of potential labour supply, while measured GDP has been more stable, this implies that potential productivity has been much weaker than previously estimated. This weakness has emerged over 2024. Overall, the changes to the level of potential productivity implied by these revisions leave it around 1¾% lower than expected at the time of the February 2024 Report (Chart B) and 1¼% below expectations in the November 2024 Report.

Chart B: Potential productivity is now estimated to have been much weaker 2024

Potential productivity per hour

Source: Bank calculations.

A reassessment of the economic factors likely to be affecting potential productivity cannot account fully for the additional weakness implied by the latest revisions.

In recent years the MPC has identified several factors which are judged to be weighing on potential productivity. A re-examination of the evidence pertaining to these factors does not suggest substantially different effects than previously estimated, and so

cannot explain the additional weakness in productivity implied by the recent data revisions.

The MPC previously judged that the long-run effects of Brexit would leave the level of potential productivity 3¼% lower than otherwise. Having reviewed the latest evidence from trade data, firm-level reporting, and recent research (**Freeman et al (2024)**), the MPC judges that the impact of Brexit on the level of potential productivity is evolving broadly as expected based on its previous assessment (Section 3 of the February 2024 Report).

The latest data published in Blue Book 2024 suggest that the supply-side effects of the pandemic on the market sector have also dissipated as expected. At the time of the February 2024 Report, the evidence suggested that there had been no significant drag on productivity due to the recent energy price shock.[1] Updated analysis continues to support this conclusion.

One contributing factor to weakness in measured productivity may be the increasing share of employment accounted for by areas where the public sector is the predominant employer such as education, health and public administration. Employment in these sectors has risen significantly since 2019, particularly in health-related activities, but these sectors have also seen significant declines in their measured productivity per hour. This means that the shift in the composition of total employment towards these areas will have weighed on total productivity.

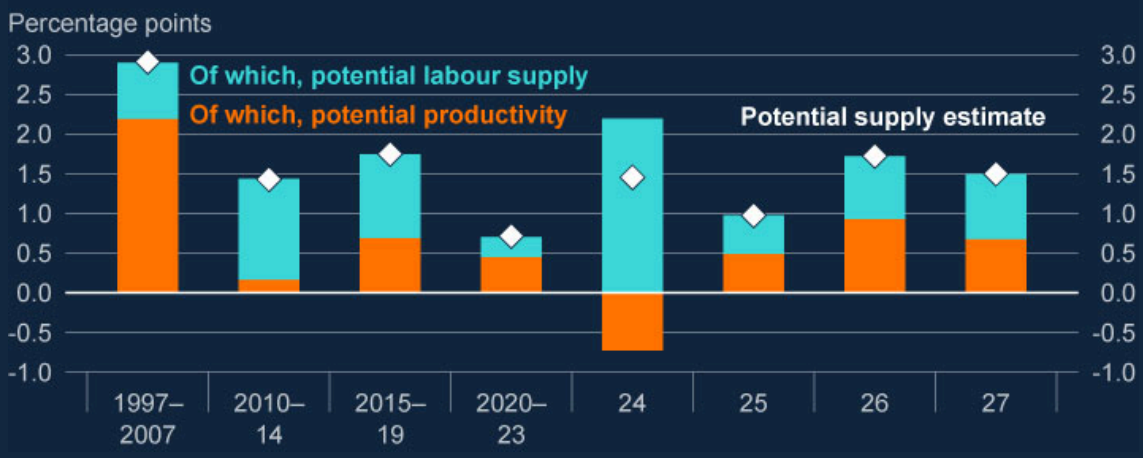
Potential productivity growth is assumed to recover over the forecast horizon.

The MPC has taken the judgement that potential productivity growth is likely to recover somewhat over the forecast. There is however considerable uncertainty around this, reflecting data uncertainty and the extent of unexplained past weakness.

In the second and third years of the forecast period, potential productivity growth is split fairly evenly between growth in total factor productivity and capital deepening. The contribution of capital deepening is expected to be a little below its pre-Covid average (Table 1), reflecting moderate growth in business investment over the forecast. In the long run, higher public investment outlined in Autumn Budget 2024 may crowd-in private investment, though any impact from this channel would be very small over the current forecast period.

Chart C: Potential supply growth is expected to pick up slightly over the forecast horizon

Estimated contributions to potential supply growth (a)



Source: Bank calculations.

(a) Average annual growth rates for periods stated. Estimates for 2024 Q4 onwards are projections consistent with the MPC's forecast. Contributions to estimated potential labour supply growth are approximations calculated as the growth rate of the individual series and so do not exactly sum to the total.

Potential supply in the MPC's forecast

> **The MPC expects potential supply growth to slow in 2025 before picking up again to around 1½% in the final year of the period.**

Annual potential supply growth is judged to have grown by 1.5% in 2024. However, across the year growth appears to have slowed, from a rate of around 1½% at the start of 2024 on a four-quarter basis to around ¾% by the first quarter of 2025.

Annual supply growth in 2025 is projected to be just under 1%. The slowing in potential supply growth reflects a normalisation in labour supply growth after the strength seen in 2024, partially offset by a recovery in potential productivity growth. As potential productivity recovers further beyond 2025, aggregate supply growth rises to 1.7% and 1.5% in the second and third years of the forecast, respectively. Relative to the MPC's assessment in the February 2024 Report, supply growth is 0.2 percentage points lower in 2025 and 0.4 percentage points higher in 2026.

Box F: Agents' update on business conditions

This box presents a summary of the intelligence gathered in the six weeks to early January by the Bank's Agents that was considered by the MPC at its February meeting.

Agents' intelligence suggests that output growth continues to ease in line with previous updates. While expectations are still for activity to pick up in 2025, contacts are revising down expectations of the pace of growth and/or revising out the timing, as sentiment has continued to deteriorate.

Overall employment intentions have softened further and are now broadly flat, in part reflecting companies' response to the forthcoming rise in employers' National Insurance contributions (NICs) and National Living Wage (NLW).

The 2025 Agents' Annual Pay Survey, carried out over November/December 2024, suggests average expected pay settlements in 2025 of 3.7%, at the upper end of the 2%–4% range reported in the **November 2024 MPR**, but down from the average actual settlements of 5.3% in 2024.

Contacts expect further reductions in service price inflation, but at a slower pace, owing to upward pressure on wages from NLW and NICs. Contacts in the food sector now expect food price inflation to be higher in 2025 than they did in the months prior to the Budget. Most other consumer goods contacts expect price increases over 2025 to remain limited.

> **Consumer spending remains subdued across goods and services. Contacts forecast slow volume growth in 2025, as expectations of slower interest rate cuts and companies' potential response to the Budget weigh down on consumer sentiment.**

Volume growth on the same period a year ago appears to have been minimal in the run-up to Christmas as consumers remain price conscious. Consumer goods retailers report consumers are prioritising experiences and holidays over physical goods. Pubs, restaurants, and takeaways report subdued volumes over the past year, though revenue growth has been strong owing to price increases. UK staycation demand is relatively flat after falling back from its pandemic high, while larger hotel chains report modest increases in occupancy. Airports continue to see strong annual growth in passenger numbers, with demand for ancillary airport services also increasing.

Investment intentions have become more subdued this round, with the range of reasons to hold off or pull back widening. Contacts are waiting to see how demand and the investment environment unfold during 2025.

Squeezed cash positions, demand uncertainty, higher working capital requirements, increased costs of capex, higher interest rates, and a reluctance to borrow are all weighing on investment appetite. More contacts mentioned the Budget as a deterrent to investment this round than last, with a few referencing business asset relief, inheritance tax, and NICs.

Intelligence suggests annual services export values growth eased slightly and is now expected to grow at a slightly weaker pace. Goods export volume growth contracted further on a year ago, and expectations for 2025 H1 growth fell back as concerns around potential US tariffs pose a downside risk to the goods' trade outlook.

Within services exports, professional services continue to grow, most notably legal and consulting. Overseas tourist numbers are down on the same time last year, partially driven by the US election. International student numbers are substantially down compared to a year ago.

Consumer goods exports remain weak, particularly in the automotive sector as UK producers face growing competition from cheaper Chinese electric cars. Exports related to construction and chemicals remain lower than a year ago. However, exporters to the defence, marine and aerospace sectors continue to report strong growth.

Business service turnover shows modest growth on a year ago owing to price increases with volumes remaining flat. Contacts expect turnover growth to continue into 2025 H1 as volumes pick up and price inflation moderates.

Professional and financial services continue to see steady revenue growth driven by strong Budget-related activity. Restructuring work continues to pick up on a year ago and there is an increase in companies being sold. Demand for both general consultancy and IT services is lower than a year ago, with clients reluctant to spend. But advice on energy transition, artificial intelligence (AI) and cyber is strong. Recruitment services continue to report revenue falling on a year ago. There is a downside risk from the impact of higher NLW and NICs on clients in the year ahead, increasing uncertainty about the outlook for demand.

Manufacturers' volumes fell slightly at the end of 2024 compared to a year ago and expectations for 2025 Q1 have weakened. Contacts have mixed views about the outlook for 2025, many now expect volume growth will be lower than previously hoped and take longer to emerge.

Defence and aerospace remain the most upbeat sectors with strong forward domestic and overseas order books. Food and soft drink output remains marginally ahead on a year ago, although pub, restaurant and hotel orders were weaker than for retailers. Vehicle output is down owing to weaker demand and some retooling for electric vehicle production. Capital goods and construction-facing output remains subdued.

> **The rate of decline in construction output compared to a year ago continues to ease. Positive output growth is now expected to return during 2025 H2; but weaker confidence following the Budget and supply constraints suggest it will be modest.**

Private housebuilding rates continue to pick up. Repair and maintenance output is up modestly on a year ago, spend on commercial renovations has improved and social housing providers are focusing on improving existing stock, but fewer households are undertaking housing renovations. New commercial development remains down on a year ago.

> **Estate agents reported slightly higher levels of sales in 2024 Q4, but overall confidence in the housing market remains fragile.**

The lower end of the market appears strongest, driven by first-time buyers. Activity is expected to pick up in Q1 ahead of stamp duty increases in April, but few expect a buoyant market throughout 2025. House prices are expected to rise modestly over the course of the next 12 months.

Demand has softened in the rental market and tenants are less willing to accept further increases in rental price. Landlords are more willing to accept lower profits on rental properties to retain desirable tenants ahead of the ban on no-fault evictions.

> **The credit conditions story is little changed. Bank appetite to lend continues to improve gradually, including to sectors previously considered ‘vulnerable’. High interest rates and weak activity continue to supress demand for credit.**

Large firms can typically access credit as normal. Small firms, including start-ups, still find it more difficult than pre-pandemic and find secondary lenders easier to access. Bond and private placement markets remain open for investment grade firms. Contacts feel further interest rate cuts are needed to stimulate new borrowing demand. Many firms are reducing gearing when refinancing. Demand for working capital and acquisition finance remain high, and there may be a flurry of acquisitions ahead of the rise in capital gains tax in April.

Businesses report very few customer defaults and that delayed or late payments are at manageable levels. Banks continue to report low levels of arrears. Cash remains tight for many small firms in hospitality, retail, manufacturing and construction.

Overall employment intentions have softened further and are now – on balance – broadly flat. This softening, at least in part, reflects companies' response to the forthcoming rise in employers' NICs and NLW.

An increasing number of contacts intend to reduce headcount, primarily through attrition. There has also been a slight increase in those expecting to make redundancies. Some firms, mostly in business services, intend to increase headcount on the back of demand growth. In many cases they will do so more cautiously than they otherwise would owing to higher NICs and will look towards automation and technology/AI to improve productivity over hiring additional staff.

Recruitment remains easier than a year ago, but overall conditions are still tighter than contacts would consider normal. Churn is lower, in part reflecting less appetite among higher-skilled staff to move, and fewer firms are holding vacancies.

A small margin of spare capacity has opened up within firms in recent months. This loosening mainly reflects weakening demand and, for some, past investment in plant and machinery.

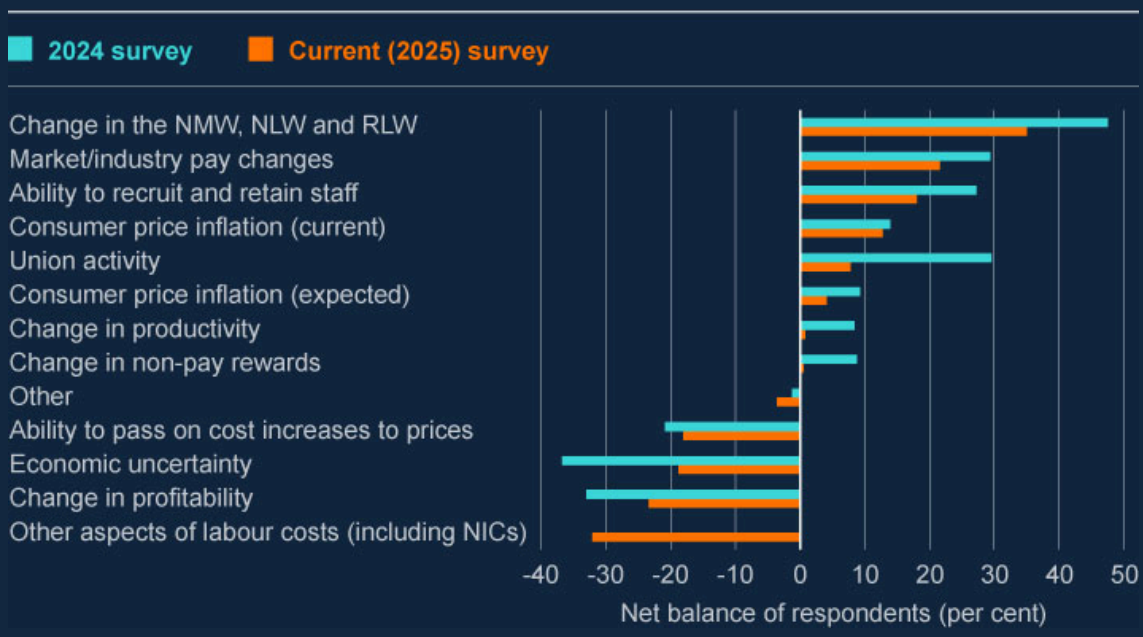
The 2025 Agents' annual pay survey shows an average expectation of 3.7% for pay settlements in 2025, at the upper end of the 2%–4% we reported in the November 2024 MPR, but higher than the 5.3% average of actual settlements in 2024.

As last year, the push factor with the greatest upward influence on pay settlements is the change to the NLW, which was a surprise to many contacts, especially the age-related changes. Some companies note these changes mean it is now too expensive to hire young workers and apprentices relative to the cost of more experienced workers. In contrast, the impact of consumer price inflation, the second-highest push factor on settlements a year ago, is much lower. Although as Chart A shows, the influence of all the push factors on pay settlements have reduced compared to last year.

Chart A shows that the factors that tend to pull down on wage settlements are also expected to exert less pressure than last year. The exception to this is the changes to non-pay labour costs (including the coming increase to NICs) a new category in this year's survey that has emerged as the strongest downward influence, ie firms may look to contain overall labour costs by revising down pay settlements as employer NICs rise. The survey suggests however, that taking such an action is more of an option in sectors where labour market conditions have eased and among firms with limited exposure to NLW.

Chart A: Most factors affecting pay settlements are expected to exert less pressure in 2025

Factors affecting average pay settlements (a)



Source: Bank of England Agents.

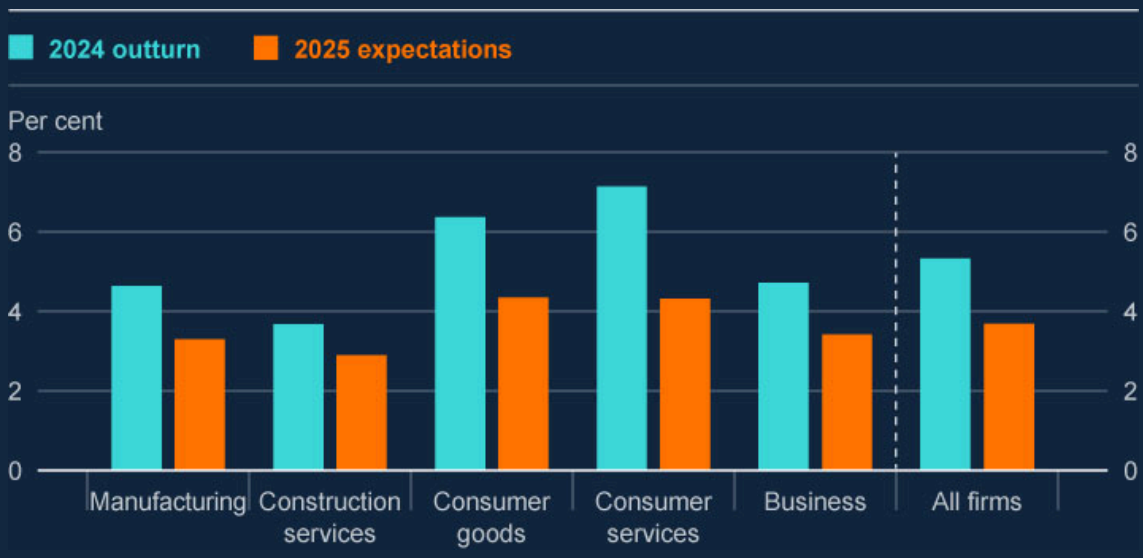
(a) When calculating these balances reports of' 'slight pressure' were given a 50% weight and reports of 'significant pressure' were given 100% weight.

Pay settlements are expected to fall across all sectors. As last year, the consumer-facing firms have the highest expected settlements, around a percentage point higher than the other sectors, though this difference is also smaller than last year (Chart B). At least in part, this is because consumer-facing firms typically employ a high proportion of low-paid workers and therefore face upwards pressure from changes to the NLW.

Many contacts report a material increase in total labour costs owing to increases in NICs. Contacts with higher proportions of part-time or low-paid workers may face labour cost increases between 2% to 4%. Those also affected by NLW, could face a combined cost increase of up to 10%. Respondents to this year's pay survey are taking a range of measures in response. Over half intended to pass through increased labour costs into higher prices, with pursuing lower wage settlements not far behind. Other measures include improving productivity, lowering employment, reducing non-labour costs, and lowering profit margins. Only 10% of firms report they will not make or see changes.

Chart B: Expectations for pay settlements in 2025 are highest in consumer-facing sectors

Average pay settlement growth (per cent)



Source: Bank of England Agents.

> **Contacts expect further reductions in service price inflation, but at a slower pace, owing to upward pressure from NLW and NICs. Expectations for food price inflation have increased.**

Raw materials prices are broadly stable or lower compared to a year ago. Imported goods prices also remain stable on last year. Many manufacturers report weak order books and intense competition for new business and so are wary of increasing prices for fear of potentially losing sales volume.

Most Business service providers report low-to-mid single digit annual inflation, though there are still some hot spots, especially services with a high NLW component such as security and cleaning.

Many consumer services firms, especially in health and care services or accommodation, expect to raise prices in 2025 more than previously anticipated owing to NLW and NICs. However, owing to weak consumer demand many contacts plan to increase prices incrementally so they can assess any impacts on sales. Most contacts intend to search for further efficiency gains though they acknowledge this is increasingly difficult.

Contacts in the food sector now expect food price inflation to be higher in 2025 than they did in the months prior to the Budget. Most other consumer goods contacts expect price increases over 2025 to remain limited.

Annex: Other forecasters' expectations

This annex reports the results of the Bank's most recent survey of external forecasters. Responses were submitted in the two weeks to 26 January and are summarised in Chart A. These are compared with the MPC's projections, which are conditioned on a range of assumptions (Section 1.1) that may differ from those made by external forecasters.

On average, external forecasters expected GDP to rise by 1.5% over the four quarters to 2026 Q1, with four-quarter growth then of 1.3% in 2027 Q1 and 1.4% in 2028 Q1 (left panel of Chart A). The average external forecast is the same as the MPC's projections for 2026 Q1 and 2027 Q1 and below the MPC projection for 2028 Q1 of 1.8%.

External forecasters expected the unemployment rate to be 4.5% in 2026 Q1, the same as the MPC's projection of 4.5% (middle panel of Chart A). They expected the unemployment rate to remain at around 4.5% in 2027 Q1 and 4.4% in 2028 Q1. By comparison, the MPC's projection increases to 4.8% in 2027 Q1 and 2028 Q1.

CPI inflation was expected to be 2.5% in 2026 Q1, below the MPC's projection of 2.9% (right panel of Chart A). The average external forecasts for 2027 Q1 and 2028 Q1 were both 2.2%. The MPC's projections are 2.3% in 2027 Q1 and 1.9% and 2028 Q1.

Chart A: At the three-year horizon, external forecasters expected four-quarter GDP growth to be 1.4%, the unemployment rate to be 4.4%, and CPI inflation to be 2.2%

Projections for GDP, the unemployment rate and CPI inflation

Glossary and other information

Glossary of selected data and instruments

AWE – average weekly earnings.

CPI – consumer prices index.

CPI inflation – inflation measured by the consumer prices index.

CPIH – consumer prices index including owner-occupiers' housing costs.

DMP – Decision Maker Panel.

ERI – exchange rate index.

GDP – gross domestic product.

HICP – harmonised index of consumer prices.

LFS – Labour Force Survey.

M4 – UK non-bank, non-building society private sector's holdings of sterling notes and coin, and their sterling deposits (including certificates of deposit, holdings of commercial paper and other short-term instruments and claims arising from repos) held at UK banks and building societies.

OIS – overnight index swap.

PCE – personal consumption expenditure.

PMI – purchasing managers' index.

RPI – retail prices index.

Abbreviations

AI – artificial intelligence.

ASHE – Annual Survey of Hours and Earnings.

BCC – British Chambers of Commerce.

BICS – Business Insights and Conditions Survey.

BVAR – Bayesian vector autoregression.

CBI – Confederation of British Industry.

CFO – chief financial officer.

CIPS – Chartered Institute of Purchasing and Supply.

DFM – dynamic factor model.

ECB – European Central Bank.

EPR – Extended Producer Responsibility.

FCA – Financial Conduct Authority.

FNAB – food and non-alcoholic beverages.

FTSE – Financial Times Stock Exchange.

GfK – Gesellschaft für Konsumforschung, Great Britain Ltd.

HMRC – His Majesty's Revenue and Customs.

ICAEW – Institute of Chartered Accountants in England and Wales.

ILO – International Labour Organization.

IMF – International Monetary Fund.

IoD – Institute of Directors.

LTV – loan to value.

MIDAS – mixed-data sampling.

MPC – Monetary Policy Committee.

MTIC – missing trader intra-community.

NICs – National Insurance contributions.

NIOFC – non-intermediate other financial corporation.

NLW – National Living Wage.

NPP – National Population Projection.

OBR – Office for Budget Responsibility.

Ofgem – Office of Gas and Electricity Markets.

ONS – Office for National Statistics.

OPEC – Organization of the Petroleum Exporting Countries.

PAYE – Pay As You Earn.

PPP – purchasing power parity.

PNFC – private non-financial corporation.

REC – Recruitment and Employment Confederation.

RLW – real living wage.

RTI – Real-Time Information.

S&P – Standard & Poor's.

SME – small and medium-sized enterprise.

UN – United Nations.

WEO – IMF World Economic Outlook.

Symbols and conventions

Except where otherwise stated, the source of the data used in charts and tables is the Bank of England or the Office for National Statistics (ONS) and all data, apart from financial markets data and results from the Decision Maker Panel (DMP) Survey, are seasonally adjusted.

n.a. = not available.

Because of rounding, the sum of the separate items may sometimes differ from the total shown.

On the horizontal axes of graphs, larger ticks denote the first observation within the relevant period, eg data for the first quarter of the year.

1. Note that this sentence was corrected on 6 March 2025.