BANK OF ENGLAND

Monetary Policy Summary and minutes of the Monetary Policy Committee meeting ending on 17 June 2020

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These are the minutes of the Monetary Policy Committee meeting ending on 17 June 2020.

They are available at https://www.bankofengland.co.uk/monetary-policy-summary-and-minutes/2020/june-2020.

The Bank of England Act 1998 gives the Bank of England operational responsibility for setting monetary policy to meet the Government's inflation target. Operational decisions are taken by the Bank's Monetary Policy Committee. The minutes of the Committee meeting ending on 5 August will be published on 6 August 2020.

Monetary Policy Summary, June 2020

The Bank of England's Monetary Policy Committee (MPC) sets monetary policy to meet the 2% inflation target, and in a way that helps to sustain growth and employment. In that context, its challenge at present is to respond to the severe economic and financial disruption caused by the spread of Covid-19. At its meeting ending on 17 June 2020, the MPC voted unanimously to maintain Bank Rate at 0.1%. The Committee voted unanimously for the Bank of England to continue with the existing programme of £200 billion of UK government bond and sterling non-financial investment-grade corporate bond purchases, financed by the issuance of central bank reserves. The Committee voted by a majority of 8-1 for the Bank of England to increase the target stock of purchased UK government bonds, financed by the issuance of central bank reserves, by an additional £100 billion, to take the total stock of asset purchases to £745 billion.

Risky asset prices have recovered further from their March lows, although they have remained sensitive to news on the evolution of the pandemic. Recent data outturns suggest that the fall in global GDP in 2020 Q2 will be less severe than expected at the time of the May *Monetary Policy Report*. There are signs of consumer spending and services output picking up, following the easing of Covid-related restrictions on economic activity. Recent additional announcements of easier monetary and fiscal policy will help to support the recovery. Downside risks to the global outlook remain, however, including from the spread of Covid-19 within emerging market economies and from a return to a higher rate of infection in advanced economies.

UK GDP contracted by around 20% in April, following a 6% fall in March. Evidence from more timely indicators suggests that GDP started to recover thereafter. Payments data are consistent with a recovery in consumer spending in May and June, and housing activity has started to pick up recently. The LFS unemployment rate was unchanged at 3.9% in the three months to April. But other and more timely indications from the claimant count, HMRC payrolls data and job vacancies suggest that the labour market has weakened materially. Following stronger than expected take-up of the Coronavirus Job Retention Scheme, a greater number of workers are likely to be furloughed in the second quarter. Evidence from business surveys and the Bank's Agents is consistent with a weak outlook for employment in coming quarters. Some households are also worried about their job security.

Twelve-month CPI inflation declined from 1.5% in March to 0.8% in April, triggering the explanatory letter from the Governor to the Chancellor published alongside this monetary policy announcement. CPI inflation fell further in May, to 0.5%. Current below-target rates of CPI inflation can in large part be accounted for by the effects of the pandemic. The collapse in global oil prices has had direct effects on inflation, via the prices of motor fuels, and indirect effects by reducing input costs in other sectors of the economy. The sharp drop in domestic activity is also adding to downward pressure on inflation through increased spare capacity in most sectors of the economy.

The unprecedented situation means that the outlook for the UK and global economies is unusually uncertain. It will depend critically on the evolution of the pandemic, measures taken to protect public health, and how governments, households and businesses respond to these factors.

The emerging evidence suggests that the fall in global and UK GDP in 2020 Q2 will be less severe than set out in the May *Report*. Although stronger than expected, it is difficult to make a clear inference from that about the recovery thereafter. There is a risk of higher and more persistent unemployment in the United Kingdom. Even with the relaxation of some Covid-related restrictions on economic activity, a degree of precautionary behaviour by households and businesses is likely to persist. The economy, and especially the labour market, will therefore take some time to recover towards its previous path. CPI inflation is well below the 2% target and is expected to fall further below it in coming quarters, largely reflecting the weakness of demand.

At this meeting, the MPC judges that a further easing of monetary policy is warranted to meet its statutory objectives. The Committee agreed to increase the target stock of purchased UK government bonds by an additional £100 billion in order to meet the inflation target in the medium term. The Committee expects that programme to be completed, and the total stock of asset purchases to reach £745 billion, around the turn of the year.

The MPC will continue to monitor the situation closely and, consistent with its remit, stands ready to take further action as necessary to support the economy and ensure a sustained return of inflation to the 2% target. The Committee will keep the asset purchase programme under review.

Minutes of the Monetary Policy Committee meeting ending on 17 June 2020

1 Before turning to its immediate policy decision, the Committee discussed: the international economy; financial markets; credit conditions and monetary developments; demand and output; and supply, costs and prices.

The international economy

2 Recent data outturns suggested that the fall in global GDP in 2020 Q2 would be less severe than had been expected at the time of the May *Monetary Policy Report*. This in part reflected an earlier end to lockdowns than had been assumed. There were signs that consumer spending and services output were now picking up, following the earlier recovery of manufacturing indicators. Recent additional fiscal policy announcements would help to support the recovery. Downside risks to the global outlook remained, however, including from the spread of Covid-19 within emerging market economies and from a return to a higher rate of infection in advanced economies.

3 According to the final estimate, euro-area GDP had fallen by 3.6% in 2020 Q1. GDP in France, Italy and Spain had declined by over 5% on the quarter, while German GDP had fallen by over 2%. Euro-area industrial production and retail sales had recorded double-digit declines on a year earlier in April, and both the manufacturing and services PMIs had remained well below 50 in May. The unemployment rate had remained broadly flat in April, at 7.3%, following the unprecedented uptake of employment support schemes and lower workforce participation. Covid-related restrictions on economic activity had started to be lifted from early May, although at different times and to varying degrees across euro-area economies. Indicators of economic mobility and spending on social consumption had also picked up in recent weeks, with some tentative evidence that the strongest recoveries had been in those economies that had eased lockdown restrictions earlier than others. Overall, the ECB expected euro-area GDP to have fallen by 13% in Q2, less negative than expected in the May *Report*. This was in line with the latest average of a range of Bank staff estimates, although there remained significant uncertainty about the extent of the weakness.

4 The second estimate of US GDP growth in 2020 Q1 had been revised down marginally, to -1.3%. In April, both retail sales and industrial production had declined significantly on a year earlier. There had been a rebound in retail sales in May, although industrial production had remained relatively weak. Following the easing of Covid-related restrictions in most US states, more timely indicators suggested that spending had continued to recover in recent weeks. A range of published regional Federal Reserve nowcasts implied Q2 growth of between -7% and -15% on a quarterly non-annualised basis. These estimates were broadly in line with recent Bank staff estimates though less negative than expected in the May *Report*. Non-farm payrolls had fallen by over 20 million in April but had increased by 2.5 million in May, against expectations of a further decline. As a result, the unemployment rate had declined slightly, to 13.3% from 14.7% in April. The Bureau of

Labour Statistics had noted that these figures probably under-estimated somewhat the official unemployment rate, as some workers affected by Covid-related business closures had been misclassified as employed but absent from work. The wider U-6 measure of workforce underutilisation had also risen, to over 20%. The Paycheck Protection Program was helping to support small businesses and keep their workforces employed.

5 Chinese economic indicators had continued to recover following the Covid-related shock to activity at the beginning of the year. Annual industrial production and, to a lesser degree, retail sales growth had picked up in April and May. Both manufacturing and services PMIs were above 50 in May, and more timely indicators of consumption had also recovered. Export growth had been stronger than anticipated in April and May. GDP growth appeared likely to rebound significantly in the second quarter as a whole, and to a somewhat greater degree than had been assumed in the May *Report*.

6 There had been further supportive news on fiscal policy since the MPC's previous meeting. The European Commission (EC) had announced its proposal for a new recovery instrument, Next Generation EU, totalling €750 billion. This was to be financed by EC bonds, and the majority of a new Recovery and Resilience Facility was to be made available via grants rather than loans. The Italian, German and French governments had also agreed substantial new fiscal packages, and the Chinese government had announced a significant fiscal expansion at the annual meeting of the National People's Congress. In the United States, the Federal Reserve had operationalised a number of new facilities financed by the CARES Act.

7 Covid-19 was now spreading rapidly across emerging market economies, including Brazil, India and Russia, exposing both domestic and external vulnerabilities. There were constraints on the extent to which emerging market economies could ease policy to cushion the impact of lockdowns. The Committee discussed how the United Kingdom would, through a number of trade and financial channels, be affected by these developments. Emerging market economies outside China accounted for around 18% of UK exports, and there could be additional indirect trade effects via disruption to global supply chains. There was also a risk to global financial conditions should there be substantial capital outflows from emerging markets, including from investment funds.

8 Following sharp falls in March and April, oil prices had generally continued to recover over recent weeks. The Brent price was now $40 per barrel compared with around $20 at its trough and around $65 at the beginning of this year. That recovery reflected the somewhat more positive news on economic activity alongside evidence of greater reductions in oil supply than had previously been anticipated.

9 Euro-area twelve-month HICP inflation had declined to 0.1% in May, while core inflation, excluding energy, food, alcohol and tobacco, had been unchanged at 0.9%. In the United States, CPI inflation had also declined to 0.1% in May, while core CPI inflation had fallen to 1.2%. Non-financial market indicators of inflation expectations in the euro area and the United States had been mixed in recent months, with household expectations generally higher but those of the majority of professional forecasters having fallen.

Financial markets

10 In the period since the May *Monetary Policy Report*, risky asset prices had recovered further from their March lows, although they had remained sensitive to Covid-19 developments including the perceived risk of a second wave of the pandemic. The yields on long-term government bonds had been broadly unchanged. Liquidity conditions and functioning in gilt markets had broadly normalised.

11 High-yield and investment-grade corporate bond spreads had continued to fall back since the May *Report*. Major global equity indices had risen by around 10%. The FTSE All-Share and Euro Stoxx equity indices had now recovered around half of the falls seen from the peaks in February to the lows in March, while the S&P 500 had recovered around three quarters of its decline over that period.

12 The Committee discussed the drivers of the recovery in risky asset prices. Analysts' expectations had continued to point to persistently lower UK corporate earnings over coming years, and futures prices appeared to reflect expectations of persistently lower dividends. The increase in equity prices since mid-March was instead estimated to have been accounted for mainly by falls in equity risk premia, which had reversed earlier increases. Measures of equity market implied volatility, such as the VIX, had fallen back since March but had remained above historical averages. Market pricing suggested that the VIX was expected to remain at elevated levels over the rest of the year. Options prices suggested that investors continued to demand higher-than-usual compensation for the risk of a sharp fall in equity prices over the next six months.

13 At its meeting on 10 June, the Federal Open Market Committee (FOMC) had left unchanged the target range for the federal funds rate and indicated that it would, having gradually slowed its asset purchases since the May *Report*, maintain at least the current pace in coming months. The ECB Governing Council had left its key policy interest rates unchanged at its 4 June meeting, and had increased the size of its Pandemic Emergency Purchase Programme by €600 billion to €1.35 trillion, slightly more than market contacts had expected, and had also lengthened the purchase window to at least June 2021. Since the May *Report*, euro-area periphery countries' sovereign debt spreads to German Bunds had fallen markedly.

14 Shorter-term market interest rates in the United States, United Kingdom and euro area had fallen since the May *Report*, and market pricing implied that rates were expected to remain at low levels. Most market contacts expected the FOMC to implement some form of cap on the yields of short-duration US Treasuries later this year. In the United Kingdom, three-year instantaneous forward Overnight Index Swap (OIS) rates were around 20 basis points below the May *Report* 15-day average. The OIS curve indicated that market participants now placed some weight on a further reduction in Bank Rate. Market contacts expected the MPC to extend its asset purchase programme at its June meeting.

15 Advanced economy long-term government bond yields had been broadly unchanged since the May *Report.* Market functioning and liquidity conditions in gilt markets had broadly normalised. Indicators of liquidity such as bid-offer spreads and round trip trading costs in cash gilt and gilt future markets had returned to around pre-Covid levels, and overnight gilt repo rates had been close to Bank Rate. UK five-year inflation swap rates, five years forward, had been broadly unchanged since the May *Report*, at around their pre-Covid levels.

16 The sterling exchange rate index had fallen by around 1% since the May *Report*. Sterling risk reversals continued to suggest perceived downside risks to the exchange rate. Market contacts had noted that the outcome of Brexit negotiations had come back into focus for investors. The UK government had formally declined the option to extend the current transition period beyond the end of this year.

17 UK wholesale unsecured bank funding costs had fallen back since the MPC's previous meeting to around their levels at the beginning of March. It was likely that the Bank's TFSME scheme had reduced the need for bank debt issuance. Lending under the scheme had so far reached around £12 billion and was likely to exceed £100 billion over the coming year, based on the provisional plans submitted to the Bank by participating firms.

Credit conditions and monetary developments

18 Sterling money holdings by households, private non-financial corporations (PNFCs) and non-intermediate other financial corporations (NIOFCs) had increased by a further £37 billion in April. Following the £55 billion increase in sterling borrowing from banks in March, which had been driven primarily by large companies drawing down on credit facilities, borrowing had decreased by £3 billion in April. This had reflected weakness in household and NIOFC flows, while PNFC borrowing had remained positive. Broader net finance raised by companies, including capital market issuance, had been £16 billion in April.

19 Corporate credit demand had remained high, according to both the Bank's Agents and business surveys. Companies had sought to borrow to address cash-flow issues and, more recently, to fund plans to re-open their businesses.

20 There were signs that corporate credit conditions had continued to improve. For large firms, conditions in capital markets had improved and investment-grade companies' issuance of bonds in dollars and equities had exceeded previous years' run-rates. In addition, based on data to 17 June, these companies had outstanding drawings of around £18 billion under the Covid Corporate Financing Facility (CCFF). For small firms, as of 14 June, lenders had approved £26 billion of loans under the Bounce Back Loan Scheme (BBLS), which targeted small companies, typically with a turnover of less than £1 million. Accounting for an estimate of the usual repayments, this could be consistent with net lending of around £20 billion in May, significantly more than the annual net lending to such companies over recent years. The high acceptance rate of over 80% for the BBLS suggested that the scheme had made a large contribution to filling the gap between credit demand and credit supply for small firms. For firms with turnover of up to £45 million, over £10 billion had been borrowed under the Coronavirus Business Interruption Loan Scheme (CBILS) and, for mid-tier companies with turnover of over £45 million, £2 billion had been borrowed under the Coronavirus Large Business Interruption Loan Scheme (CLBILS). Intelligence from the Agents had suggested that some mid-tier non-investment grade firms were still facing credit constraints, particularly in consumer-facing sectors such as retail and travel.

21 Effective interest rates on new lending to all PNFCs had fallen by 10 basis points in April, while effective rates on new lending to SMEs had fallen by over 50 basis points. The latter had reflected the commencement of lending under CBILS, for which companies did not pay any interest for the first twelve months.

22 The Committee discussed the outlook for corporate financing and, in particular, the degree of unfulfilled demand for credit. Some very small firms were reluctant to borrow because they had not done so previously. Other companies could meet their cashflow needs by drawing down on their deposit facilities, or were reluctant to take on extra debt. For some of those firms, equity-like solutions might be preferable to additional debt. Looking ahead, UK companies had significant refinancing needs over the next few years, with more than a third of banks' corporate lending books turning over in the next twelve months. In most sectors, trade credit conditions had not tightened materially. The Government's introduction of a guarantee on trade credit insurance would help to prevent that happening, although the market for new business was not currently expected to re-open in a significant way.

23 For households, there had been a sharp drop in mortgage approvals, from 140,000 in February to 57,000 in April, driven by the large fall in demand during the period of official social distancing measures. In particular, approvals for house purchase in April had been less than 25% of the monthly average in the year to February 2020. There had been some signs of a pick-up since the housing market re-opened in mid-May; Zoopla listings of houses for sale and those sold had picked up materially. Some evidence of a reduction in the supply of credit remained, however. For instance, the number of mortgage products available had continued to be much lower than prior to the Covid shock and there was very limited availability of high loan-to-value mortgages for new borrowers. Mortgage payments deferred from the end of March would begin to fall due later this month, although the Financial Conduct Authority had announced recently that borrowers could apply to defer for a further three months and had also extended the application window for new deferrals until the end of October.

24 Consumer credit flows had been very weak in April, consistent with a sharp fall in household spending. Gross consumer lending had dropped from £20 billion in March to £12 billion in April, less than 50% of the monthly average in the year to February 2020. That had been offset partly by lower repayments, as borrowers had taken payment holidays, but repayments had still outpaced new lending by over £7 billion. While weaker credit demand was likely to have been the primary driver, some lenders had tightened credit criteria, for instance by raising the credit score that a prospective borrower needed to obtain credit, and lowering limits on credit cards and overdrafts.

25 The Committee continued to monitor the pass-through of its recent 65 basis point reduction in Bank Rate. Interest rates quoted on household sight deposits had fallen by around 20 basis points, and were only expected to fall a little further in coming months, as they were already close to their assumed lower bound. Interest rates on household fixed-rate term deposits had fallen by around 50 basis points, almost as much as Overnight Index Swap rates of the same maturity. Pass-through of the reductions in Bank Rate to new mortgage rates had been slower than expected to date. That might reflect lags in transmission or other more enduring factors. Effective rates on the stock of standard variable rate and tracker mortgages had fallen by 54 basis points and 57 basis points respectively between February and April.

Demand and output

26 Following the imposition of social distancing measures, monthly GDP data for April had confirmed that the reduction in activity related to the Covid-19 shock would be unprecedented in scale. However, the latest indicators for May and June suggested that the weakening of the UK economy in the second quarter of the year was likely to be less severe than expected at the time of the May *Monetary Policy Report*.

27 GDP was estimated to have fallen by 2% in 2020 Q1, and by 5.8% on the month in March alone. That quarterly decline was slightly smaller than the 2.9% decline expected in the May *Report*. Household consumption had fallen by 1.7% in Q1, compared with a figure of 2.8% in the May *Report*. Social consumption and transport-related spending had been particularly weak.

28 In April, GDP was estimated to have fallen by a record 20% on the month. Services output had declined by 19%, industrial production by 20% and construction output by 40%. The cumulative fall in output of 25% across March and April had been somewhat less severe than expected at the time of the May *Report*. Nevertheless, its composition had been in line with expectations and there were significant uncertainties around the precise estimates. ONS staff had in May briefed the Committee about their approach to data collection during the lockdown.

29 To complement official data and business surveys, Bank staff had continued to use a range of high-frequency indicators to provide a timely read on economic activity. Payments data from CHAPS and other sources suggested that consumer spending had started to recover a little earlier than had been expected at the time of the May *Report*, following a fall of around 30% in expenditure in April. Within those payments data, the sharpest recovery appeared to be spending on delayable goods, a category that included DIY goods, car sales, clothing and household goods. Work-related spending, including on motor fuels, had also risen recently, as had spending on food delivery from restaurants. Online retail sales had risen by 18% in April, and payments data implied a further pickup subsequently. That was consistent with reports from the Agents that companies were expanding and improving their capacity to process sales online. Reports from the Agents and the ONS Business Impact of Covid-19 Survey also suggested that some consumer-facing firms, which had closed temporarily in March and April, had re-opened in recent weeks.

30 There were also signs of a pickup in activity elsewhere in the economy. Housebuilding indicators had recovered partially, broadly in line with the path of housing investment expected in May. The Bank's Decision Maker Panel had suggested that the negative impact on business investment from Covid-19 had been slightly smaller than previously estimated, but that capital expenditure was still likely to have fallen by around 40% in the second quarter. While it was hard to estimate trade flows accurately even in normal times, monitoring of traffic around ports and airports had suggested that they too had begun to recover, following a fall in both export and import volumes of around 30% between February and April. Taken together with consumer spending, these developments suggested that the level of GDP in the second quarter might be 20% below its level in the final quarter of 2019, rather than the 27% included in the May *Report*.

31 It was not clear how strong a signal to take from the latest data for the outlook. Some of the upside news in 2020 Q2 could reflect a bringing forward of the rise in spending previously projected to occur in Q3. Although

the pace at which the lockdown had been relaxed was broadly in line with the May *Report*, the earlier than expected re-opening in England and Northern Ireland of non-essential retail outlets in mid-June and, prospectively, pubs, restaurants and bars in early July, would provide further impetus to spending. Nevertheless, a survey of households conducted by Ipsos MORI for the Bank had suggested that, as official social distancing measures continued to ease, households expected to re-start social spending only gradually. Around a quarter of respondents had said that they would return to pubs or restaurants 'straight away' and around 40% said that they would ultimately expect to go out to these venues 'at least as often as before'.

32 There was also substantial heterogeneity across households in their experiences of, and responses to, the Covid-19 shock. The 2020 H1 NMG survey, conducted for the Bank between 6 April and 1 May, suggested that households were very pessimistic about the course of spending over the next year. That had coincided with a deterioration in households' expectations about their financial situation and, in particular, a fear of unemployment among currently furloughed workers. There had been little change in the proportion of households who thought that their saving for an emergency was adequate. On the one hand, it was possible that there could be a rise in precautionary savings, including in response to actual or possible unemployment. On the other hand, it was clear that, largely due to constraints on spending during the lockdown, actual saving had risen. While this could provide a boost to spending in the future, increases in savings appeared to have been concentrated within high-income and retired households, who tended to have a lower marginal propensity to consume.

33 A key feature of the Covid-19 shock was that sectors of the economy had been impacted to very different degrees. This sectoral heterogeneity was likely to persist. Over the next year, demand was expected to remain weakest in consumer-facing industries according to the Decision Maker Panel, with sales recovering only gradually. Investment by consumer-facing firms in the DMP was likely to recover even more gradually. Intelligence from the Bank's Agents suggested that insolvencies would rise over the remainder of this year, and again with an uneven impact across sectors.

Supply, costs and prices

34 Administrative data suggested employment had fallen markedly alongside spending, but that was yet to be clearly evident in the Labour Force Survey (LFS). According to HMRC Pay As You Earn (PAYE) Real Time Information (RTI) data the number of employees had declined by a further 163,000 in May, having fallen by 449,000 in April. The comparable LFS data showed a further rise in the number of employees in the three months to April, however, alongside a fall in self-employment. The LFS unemployment rate had been unchanged at 3.9% and inactivity a little higher, at 35.8%, as some individuals had been disincentivised from looking for work, or had been unable to, due to social distancing restrictions. The apparent resilience in the LFS jobless rate might have reflected sampling variability or timing, with LFS employment softening towards the end of April. More timely data, including the RTI, suggested further ongoing weakness. The claimant count had risen by 1½ million up to mid-May, although claims for Universal Credit had slowed to closer to typical levels by

late-May, consistent with a moderation in the rate of newly unemployed. Official and online indicators of the number of vacancies had remained around 60% below their levels earlier in the year.

35 According to the LFS, the number of workers classifying themselves as temporarily away from work had risen by 6¼ million by the end of April, largely reflecting employees being furloughed under the Coronavirus Job Retention Scheme (CJRS). That was only slightly above the six million assumed to be furloughed on average in 2020 Q2 in the May *Report*. CJRS claims had covered around nine million jobs at any point up to mid-June, however. While the two figures were not directly comparable, as some employees had been furloughed from more than one job or only for a part of the quarter, the share of employees covered during Q2 was now thought to be closer to a quarter than the fifth assumed originally. More than half of CJRS claims had related to staff employed in small- and medium-sized businesses. And a third had been concentrated within accommodation and food services, where 60% of employees had been furloughed, and the distribution sector. Take-up of the Self-Employment Income Support Scheme had reached 2½ million. Looking ahead, the schemes would soon close to new claims, with subsequent flexibility to deploy furloughed employees on a part-time basis. Employer national insurance contributions and pension contributions would no longer be paid under the CJRS from August onwards, however, and the proportion of salary covered by the government would be tapered to 70% in September and 60% in October, with employers topping up to 80%.

36 Both total and average hours worked had fallen by 8.7% in the three months to April. Average hours worked were 20% below their 2019 Q4 average in April itself.

37 The latest business and household surveys suggested upside risks to the path of unemployment. On balance, respondents to the latest Decision Maker Panel had expected employment to fall further, with reductions concentrated within firms that had faced the largest declines in sales to date and had furloughed a relatively higher share of their workforce. A quarter of manufacturing companies responding to the 2020 Q2 Make UK Quarterly Survey had planned to make some redundancies within six months. Among respondents to the NMG household survey, 30% of employees currently furloughed had thought it at least quite likely that they would lose their job, compared to around 20% of other employees. Ultimately, the unemployment profile would be determined by the speed of recovery across different sectors, the extent to which labour could be reallocated between them, and policy support.

38 Annual whole-economy Average Weekly Earnings (AWE) growth had slowed to 1.0% in the three months to April. Recent AWE data had been depressed as a result of lower pay for furloughed employees, despite some companies topping up their pay above the 80% covered by the CJRS. Survey evidence suggested some weakening in the underlying trend. The Bank's Agents had reported that some companies had postponed or cancelled pay rises that would typically take place at this time of the year. Pay indices within the May REC Report for Jobs, applicable to new hires, had also fallen to levels last seen during the financial crisis, when annual pay growth had slowed to around zero.

39 Twelve-month CPI inflation had fallen to 0.8% in April and somewhat further to 0.5% in May, in large part accounted for by the effects of the pandemic. As the inflation rate was below 1%, an exchange of letters between the Governor and the Chancellor of the Exchequer would be published alongside these minutes. A

sharp reduction in economic activity in the United Kingdom, and globally, was reducing UK inflation through a number of channels. Reduced demand had led to a collapse in global oil prices in particular. Coupled with past falls in commodity prices, energy had subtracted three-quarters of a percentage point from CPI inflation in May, as the prices of motor fuels, consumer gas and electricity had all fallen on the year. Rises in spot and future oil prices since the run-up to the May *Report* had pushed the staff's short-term inflation forecast higher by 0.2 percentage points on average. Nevertheless, energy prices were likely to continue to weigh substantially on CPI inflation over the remainder of 2020 and early 2021.

40 Core CPI inflation, excluding energy, food, alcoholic beverages and tobacco, had fallen to 1.4% in April and 1.2% in May, and was likely to fall further in the near term reflecting downward pressure from low demand. It remained too early to assess fully how the Covid-19 shock was affecting consumer prices across different sectors of the economy, but it seemed likely that there would be more sectoral dispersion than usual. Some sectors in which demand was much lower than usual had already experienced weaker inflationary pressures. The ONS Business Impact of Covid-19 Survey also suggested widespread weakness in selling prices across the economy.

41 Despite the recent falls in measured inflation, shorter-term household inflation expectations had been reasonably steady, although there had been contrasting changes across medium-term measures. Two- and five-year ahead household inflation expectations had fallen sharply in the Bank of England/TNS Inflation Attitudes Survey in May, to 1.9% and 2.6% respectively. A discontinuity might have been generated in those series by moving the survey online as opposed to being held face-to-face, however, in particular as the option to not state a view, and reply 'don't know', had become less prominent. Caution in interpreting moves between the latest and previous survey was therefore warranted. Five-to-ten year ahead expectations had remained broadly stable according to the Citi/YouGov household survey for May, which had continued to be run online.

The immediate policy decision

42 The MPC sets monetary policy to meet the 2% inflation target, and in a way that helps to sustain growth and employment. In that context, its challenge at present was to respond to the severe economic and financial disruption caused by the spread of Covid-19.

43 The unprecedented situation meant that the outlook for the UK and global economies was unusually uncertain. It would depend critically on the evolution of the pandemic, measures taken to protect public health, and how governments, households and businesses responded to these factors.

44 The MPC reviewed the news since its previous meeting.

45 Risky asset prices had recovered further from their March lows, although they had remained sensitive to news on the evolution of the pandemic. Recent data outturns suggested that the fall in global GDP in 2020 Q2 would be less severe than expected at the time of the May *Monetary Policy Report*. That would appear to be because Covid-related restrictions on economic activity had eased earlier than assumed, but also because the

effects of the lockdowns on activity that quarter had been less severe. Recent additional announcements of easier monetary and fiscal policy would help to support the recovery. Downside risks to the global outlook remained, however, including from the spread of Covid-19 within emerging market economies and from a return to a higher rate of infection in advanced economies.

46 UK financial conditions had been fairly stable since the previous MPC meeting, but had remained tighter than prior to the Covid shock. That partly reflected widening household credit spreads, with risk-free interest rates having fallen but new household lending rates as a whole having been little changed so far. That in turn might reflect lagged pass-through from the recent reductions in Bank Rate or other more enduring factors.

47 As outlined in the letter that the Governor had sent to the Chancellor of the Exchequer on 17 March, the MPC would take the size of the Covid Corporate Financing Facility (CCFF) into account when it took its decisions on the appropriate monetary policy stance necessary to fulfil its remit. On 19 May, HM Treasury had published updated terms of the CCFF that set out: that all businesses that wished to draw from the CCFF for a term extending beyond 19 May 2021 would be expected to provide a letter addressed to HM Treasury that committed to showing restraint on the payment of dividends and other capital distributions and on senior pay during the period in which their commercial paper was outstanding; that businesses that had drawn under the CCFF were now able to repay their drawings early if they chose to do so; and that HM Treasury and the Bank had decided to publish the names of businesses that had drawings under the CCFF, as well as the amounts borrowed. Based on data to 17 June, companies had outstanding drawings of around £18 billion under the CCFF.

48 As of 17 June, the total stock of the Asset Purchase Facility had reached £613 billion, an increase of £168 billion as part of the existing programme of asset purchases announced on 19 March. Within that increase, £162 billion of UK government bonds, and £5.8 billion of investment-grade corporate bonds, had been purchased since March. In order to complete the existing programme of asset purchases, the Bank would continue to purchase corporate bonds, such that around £10 billion of these bonds were purchased by the end of the programme, with the remainder of the existing programme comprised of further government bond purchases.

49 Liquidity conditions and functioning in gilt markets had broadly normalised. Indicators of liquidity such as bid-offer spreads and round trip trading costs in cash gilt and gilt future markets had returned to around pre-Covid levels, and overnight gilt repo rates had been close to Bank Rate.

50 UK GDP had contracted by around 20% in April, following a 6% fall in March. Evidence from more timely indicators suggested that GDP had started to recover thereafter. Payments data were consistent with a recovery in consumer spending in May and June, and housing activity had started to pick up recently. Net trade might also provide a small boost to GDP growth in light of the relative news on UK and global demand. Overall, recent developments suggested that the level of GDP in the second quarter might be 20% below its level in the final quarter of 2019, rather than the 27% included in the May *Report*.

51 The LFS unemployment rate had been unchanged at 3.9% in the three months to April. The apparent resilience in this measure might have reflected sampling variability or timing, with LFS employment softening

towards the end of April. The single month figure showed that participation had also fallen in April, possibly because the lockdown had limited the extent to which some people could search for work or be available to work. Other and more timely indications from the claimant count, HMRC payrolls data and job vacancies suggested that the labour market had weakened materially. Following stronger than expected take-up of the Coronavirus Job Retention Scheme (CJRS), a greater number of workers were likely to be furloughed in the second quarter. Average hours worked had fallen significantly in April. Evidence from business surveys and the Bank's Agents was consistent with a weak outlook for employment in coming quarters. Some households were also worried about their job security.

52 Twelve-month CPI inflation had declined from 1.5% in March to 0.8% in April, triggering the explanatory letter from the Governor to the Chancellor published alongside these minutes. CPI inflation had fallen further in May, to 0.5%. Core CPI inflation had been subdued even before the Covid outbreak. Nevertheless, current below-target rates of CPI inflation could in large part be accounted for by the effects of the pandemic. The collapse in global oil prices had had direct effects on inflation, via the prices of motor fuels, and indirect effects by reducing input costs in other sectors of the economy. The sharp drop in domestic activity was also adding to downward pressure on inflation through increased spare capacity in most sectors of the economy. For example, the ONS Business Impact of Covid-19 Survey suggested widespread weakness in selling prices.

53 CPI inflation was expected to fall slightly further in the near term, as the drag from the Covid-related shock built. It was then expected to rise during 2021, as the direct impact of the recent fall in the oil price dropped out of the annual comparison and the downward pressure from domestic factors waned as demand recovered.

54 The MPC was continuing to monitor closely developments in indicators of inflation expectations, including those of households, businesses and financial markets. Overall, the Committee judged that inflation expectations remained well anchored and consistent with inflation close to the 2% target.

55 The Committee turned to its immediate policy decision.

56 Consistent with its remit, monetary policy was aimed at supporting businesses and households through the crisis, and limiting any lasting damage to the economy so as to ensure a sustainable return of inflation to the target.

57 The emerging evidence suggested that the fall in global and UK GDP in 2020 Q2 would be less severe than set out in the May *Report*. Although stronger than expected, it was difficult to make a clear inference from that about the recovery thereafter. There was a risk of higher and more persistent unemployment in the United Kingdom. Even with the relaxation of some Covid-related restrictions on economic activity, a degree of precautionary behaviour by households and businesses was likely to persist. The economy, and especially the labour market, would therefore take some time to recover towards its previous path. CPI inflation was well below the 2% target and was expected to fall further below it in coming quarters, largely reflecting the weakness of demand.

58 Different members placed different weights on the extent to which the recent news on GDP and the labour market had implications for the economic outlook and the risks around it.

59 Recent payments and other high frequency data suggested that consumer spending could already have reached the level that the May scenario had suggested would be reached in the third quarter. There were also signs of a pickup in activity elsewhere in the economy. It was unclear, however, how sustainable those trends would be and to what extent consumers would be willing to return to shopping physically now that some Covid-related restrictions had started to be lifted. Forms of social expenditure were also likely to continue to be held back by social distancing, whether officially mandated or voluntary. If the degree of voluntary social distancing depended on the prevalence of the virus, the recovery in social consumption might be slower in the United Kingdom than in other economies that had experienced a lower number of Covid cases. More generally, there were risks to the recovery from ongoing high uncertainty, weaker balance sheets, particularly in the corporate sector, and increased risk aversion.

60 Risks around the outlook for the labour market appeared to be tilted to the downside, notwithstanding the latest LFS unemployment and employment data. Current indications from business surveys suggested that furloughed employees might not be fully re-absorbed into the workforce as current government support measures started to be withdrawn later in the year. Concerns about job security could also lead to an increase in precautionary saving, further dampening the recovery. That said, although there was the potential for a negative feedback loop to develop from unemployment to spending, there was also the potential for a positive loop from stronger demand to higher employment. It was possible that companies' employment plans would improve as they revised up their sales forecasts to take into account the most recent improvement in activity.

61 At this meeting, a majority of MPC members judged that a further easing of monetary policy was warranted to support the economy and thereby to meet the inflation target in the medium term. While recent demand and output data had not been quite as negative as expected, other indicators suggested greater risks around the potential for longer lasting damage to the economy from the pandemic. The most timely data remained consistent with a significant weakening in the labour market in the second quarter. There was a risk that the path of unemployment would be higher than expected at the time of the May *Report*, particularly if it proved difficult for furloughed workers to be re-absorbed into employment. A persistent margin of spare capacity, in large part reflecting slack in the labour market, would weigh on inflation. Existing fiscal support provided to workers and to companies was likely to continue to play a key role in preventing a larger fall in spending and widespread business failures. Looser monetary policy also had a role to play by supporting cashflows, demand, and financial conditions. In an environment of heightened uncertainty, some members in this group also envisaged a role for monetary policy in seeking to mitigate the potential impact of more adverse economic scenarios, including those in which there were higher rates of Covid-19 infection going forward. Some members noted that risk management considerations favoured a prompt response to downside risks at present in order to ensure a sustained return of inflation to the target.

62 One member preferred to maintain the existing monetary policy stance at this meeting. The recovery in demand and output was occurring sooner and materially faster than had been expected at the time of the previous MPC meeting. If this persisted, cumulative output losses over the policy horizon could plausibly have halved compared with what had been expected at the time of the May *Report*, boosting inflation prospects in the medium term. There were still material downside risks, especially around employment, but these risks were

more evenly balanced than in May. Existing monetary conditions were extremely accommodative and, in the view of this member, supporting a strong recovery sufficient to return inflation to its target.

63 The MPC would continue to monitor the situation closely and, consistent with its remit, stood ready to take further action as necessary to support the economy and ensure a sustained return of inflation to the 2% target. The Committee would keep the asset purchase programme under review.

64 The Chair invited the Committee to vote on the propositions that:

Bank Rate should be maintained at 0.1%;

The Bank of England should continue with the existing programme of £200 billion of UK government bond and sterling non-financial investment-grade corporate bond purchases, financed by the issuance of central bank reserves;

The Bank of England should increase the target stock of purchased UK government bonds, financed by the issuance of central bank reserves, by an additional £100 billion, to take the total stock of asset purchases to £745 billion.

The Committee voted unanimously in favour of the first and second propositions.

Eight members (Andrew Bailey, Ben Broadbent, Jon Cunliffe, Jonathan Haskel, Dave Ramsden, Michael Saunders, Silvana Tenreyro and Gertjan Vlieghe) voted in favour of the third proposition. Andrew Haldane voted against this proposition, preferring to maintain the target for the total stock of asset purchases at £645 billion.

65 As set out in the Market Notice accompanying these minutes, the Committee expected the new asset purchase programme to be completed, and the total stock of purchases to reach £745 billion, around the turn of the year. With liquidity conditions having stabilised, purchases could now be conducted at a slower pace than during the earlier period of dysfunction. Should conditions worsen materially again, however, the Bank stood ready to increase the pace of purchases to ensure the effective transmission of monetary policy.

66 Consistent with the Committee's previous guidance, and as described in the accompanying Market Notice, the Committee agreed to reinvest £6.4 billion of cash flows associated with the redemption of the July 2020 gilt held by the Asset Purchase Facility.

67 The following members of the Committee were present:

Andrew Bailey, Chair
Ben Broadbent
Jon Cunliffe
Andrew Haldane
Jonathan Haskel
Dave Ramsden
Michael Saunders
Silvana Tenreyro
Gertjan Vlieghe

Clare Lombardelli was present as the Treasury representative.

As permitted under the Bank of England Act 1998, as amended by the Bank of England and Financial Services Act 2016, Bradley Fried was present on 11 and 15 June, as an observer for the purpose of exercising oversight functions in his role as a member of the Bank's Court of Directors.