BANK OF ENGLAND

News release

Press Office
Threadneedle Street
London EC2R 8AH
T 020 7601 4411
F 020 7601 5460
press@bankofengland.co.uk
www.bankofengland.co.uk

1 December 2005

Monetary Policy: Significant Issues of Today - Speech by Sir Andrew Large

Speaking to West London Business this afternoon, Sir Andrew Large gives his last public speech as Deputy Governor of the Bank of England. In his speech, he draws attention to four significant issues that have been of particular interest to him while on the Monetary Policy Committee: oil, debt, the labour market, and pensions and longevity.

Reflecting on the recent increases in the price of oil, Sir Andrew notes the possibility of inflationary pressures. He says: "I think it is still too early to relax in relation to inflation expectations, and I think that the subject of oil will feature as a significant issue for some time to come in the monetary policy arena."

Discussing the potential impact on consumption of changes in household debt, he noted: "As far as debt levels are concerned, for me the key issue for monetary policy is that the more capital gearing or leverage increases the greater the vulnerability to shocks and the consequent adjustment to consumption behaviour. In my experience as leverage increases, so the level of debt ceases to be a mere residual and becomes more of a determinant of behaviour in its own right, and hence becomes of real consequence for monetary policy." He asks whether borrowers are becoming more cautious in the light of already high debt-to-income ratios and whether there are changes in the attitudes of lenders which might reduce the supply of lending. Sir Andrew asks: "…has the stabilisation in house prices led homeowners to become more conservative or precautionary in their borrowing habits, realising that they can no longer assume that their debt will be offset by significant increases in house prices? Secondly, could the attitude of lenders have contributed to the downturn, through the withdrawal of credit?"

He notes the need to consider the labour market in a global context, because in assessing the size of the market we can no longer think of it being constrained by the UK as a geographic entity. Commenting on the increase in supply of labour from migrant workers, Sir Andrew says: "So if we have already allowed for this increase in migrant workers, a key question is whether the rate of influx will continue and, if it does, what will the net effect be on demand and supply in the economy?"

Turning to pensions, he raises the question of whether there will be significant changes in consumption as people save more for their retirement. "For monetary policy the key issue is how and over what timeframe

will these changes impact on savings, which at a domestic level are likely to have to increase to provide adequate income in retirement…And the question is whether these changes will be smooth trends, or whether there will be more sudden, and perhaps unpredictable shifts or discontinuities in behaviour. And if the latter, will they be of sufficient magnitude to be relevant to shorter-term monetary policy?"

Finally, in describing his own voting record, Sir Andrew says: "I am very conscious that I have collected the description of being a 'hawk': of erring on the side of rate rises. Certainly my willingness to allow thoughts about insurance to influence decisions at the margin, has meant that on the occasions when I have voted with the minority it has been on the upside for rates. But equally the longer term issues, such as those of labour supply and pensions saving, are more likely to manifest themselves on the downside. I am certainly very conscious of these factors too…."

Note to Editors

As already announced, Sir Andrew is to leave the Bank shortly after the MPC meeting in January.

Key Resources

Monetary Policy: Significant Issues of Today
Speech by Sir Andrew Large, Deputy Governor, to West London Business on 1 December 2005
http://www.bankofengland.co.uk/archive/Documents/historicpubs/speeches/2005/speech262.pdf