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Bernard Corry Memorial Lecture by David Blanchflower: Recent Developments in the UK Economy - the Economics of Walking About

In the Bernard Corry Memorial Lecture given today at Queen Mary, University of London, Professor David Blanchflower, an external member of the Bank's Monetary Policy Committee, discusses five questions about the economy:

- Why have unemployment and inactivity increased recently?
- Why has most of the job growth in recent years been in self-employment?
- What has been happening to capacity within firms?
- Why has wage growth been benign recently?
- Why has inflation failed to respond to higher money growth?

He also highlights the importance of examining data carefully and adopting a more investigative approach, putting the data before the theory, which he refers to as the 'economics of walking about.'

Professor Blanchflower notes there has been a significant improvement in the level of unemployment prevailing in the UK since 1997 and a rise in the number of self-employed. However, there has also been a sharp increase in the number of individuals in the last 10 years who have exited the labour force, and also in the number of 18-24 year olds who are unemployed. He looks at the possible reasons for the growth in self-employment in the last 30 years and the sharp rise in recent months and notes that "It does not appear that the most recent increase in self-employment has been the result of changes in regulation, tax changes, or changes in the minimum wage." Professor Blanchflower says his "reading of the labour data has been that the market has loosened over the past year or so."

Turning to capacity within firms, he says that "survey evidence suggests capacity utilisation is currently above 'normal' levels" but notes it was also unclear "what capacity pressures in services actually means, over and above the skilled labour shortages that have been highlighted by the Bank's Agents in their recent surveys." He believes that spare capacity has fallen in firms over the last year and may be a prelude to price increases but says it is "difficult to interpret what the data are actually telling us about future inflationary pressures at present, although they do seem to point to an upside risk."

Professor Blanchflower observes the benign wage growth recently experienced in the UK at a time when shortages of skilled workers remain apparent. He notes that in any dynamic economy, skilled worker shortages are "a fact of life" and characterises the lack of significant wage inflation as due in part to slack in the labour market and the impact of inward migration. Currently "it appears that wages are the dog that hasn't barked."

He goes on to look at the weakening correlation between the growth of broad money and inflation in the UK, where "fast rates of money growth have occurred alongside remarkably stable and low inflation." Professor Blanchflower cites the role played by deposits from Other Financial Corporations in the pick up in M4 growth and the general rise in the demand for money in the economy. He points out that money supply is a variable that will continue to be monitored and analysed, even though it is not targeted by the Bank.

In conclusion Professor Blanchflower underlines the importance of economists "sniffing the air and putting the data before the theory where this seems warranted." He also explains that the rationale behind his decision to vote for a rate rise this month was "to ensure that inflation expectations remain anchored, given rising food prices, recent further increases in oil prices, more robust world growth, and the March inflation outturn."

<http://www.bankofengland.co.uk/archive/Documents/historicpubs/speeches/2007/speech310.pdf>