



BANK OF ENGLAND

News release

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Bank of England Reduces Bank Rate by 1.5 Percentage Points to 3%

The Bank of England's Monetary Policy Committee today voted to reduce the official Bank Rate paid on commercial bank reserves by 1.5 percentage points to 3%.

The past two months have seen a substantial downward shift in the prospects for inflation in the United Kingdom. There has been a very marked deterioration in the outlook for economic activity at home and abroad. Moreover, commodity prices have fallen sharply.

Since mid-September, the global banking system has experienced its most serious disruption for almost a century. While the measures taken on bank capital, funding and liquidity in several countries, including our own, have begun to ease the situation, the availability of credit to households and businesses is likely to remain restricted for some time. As a consequence, money and credit conditions have tightened sharply. Equity prices have fallen substantially in many countries.

In the United Kingdom, output fell sharply in the third quarter. Business surveys and reports by the Bank's regional Agents point to continued severe contraction in the near term. Consumer spending has faltered in the face of a squeeze on household budgets and tighter credit. Residential investment has fallen sharply and the prospects for business investment have weakened. Economic conditions have also deteriorated in the UK's main export markets.

CPI inflation rose to 5.2% in September. The substantial rise since the beginning of the year largely reflects the impact of higher energy and food prices. But commodity prices have fallen sharply since mid-summer, with oil prices down by more than a half. Inflation should consequently soon drop back sharply, as the contribution from retail energy and food prices declines, notwithstanding the fall in sterling. Pay growth has remained subdued. And measures of inflation expectations have fallen back.

Since the beginning of the year, the Committee has set Bank Rate to balance two risks to the inflation outlook. The downside risk was that a sharp slowdown in the economy, associated with weak real income growth and the tightening in the supply of credit, pulled inflation materially below the target. The upside risk was that above-target inflation persisted for a sustained period because of elevated inflation expectations. In recent weeks, the risks to inflation have shifted decisively to the downside. As a consequence, the

Committee has revised down its projected outlook for inflation which, at prevailing market interest rates, contains a substantial risk of undershooting the inflation target. At its November meeting, the Committee therefore judged that a significant reduction in Bank Rate was necessary now in order to meet the 2% target for CPI inflation in the medium term, and accordingly lowered Bank Rate by 1.5 percentage points to 3.0%.

The Committee's latest inflation and output projections will appear in the Inflation Report to be published on Wednesday 12 November.

The minutes of the meeting will be published at 9.30am on Wednesday 19 November.

Notes to Editors

The previous change in Bank Rate was a reduction of 0.5 percentage points to 4.5% on 8 October 2008.