Bank of England

November 2024

Monetary Policy Report: Sefton Economic Forum

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Thursday 14th November 2024

What do the Bank's Agents do?

In a nutshell

12 agencies across the UK

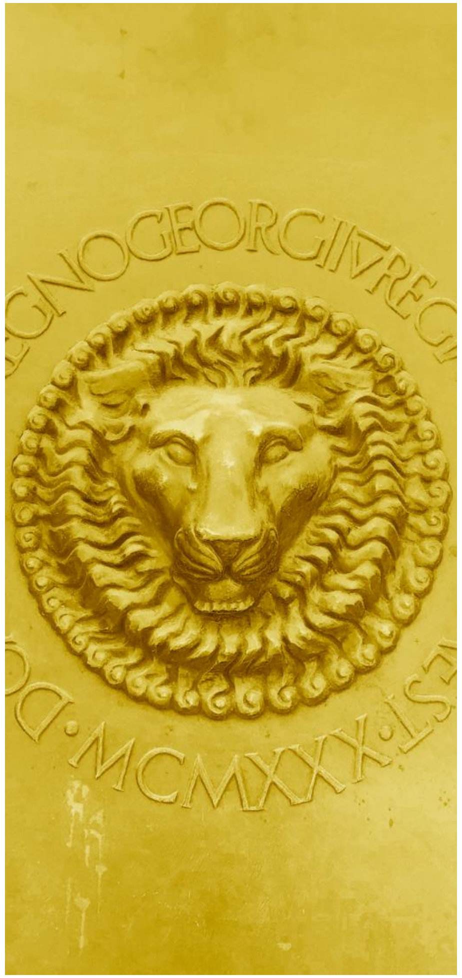
600 presentations a year

9000 discussions with contacts

60 visits by policy makers

- Provide intelligence on economic and financial conditions around the country
- Inform MPC/FPC/Bank policymaking
- Connect policymakers with what is happening on the ground
- Score business conditions and publish the results

Plan for the session



- Headlines
- Near Term Inflation Outlook
- Current Economic & Financial Conditions
- The Growth Outlook
- The Medium Term Inflation Outlook
- MPC Perspective and Policy
- Q&A

Headlines

Main points

- CPI inflation back below 2%. Will rise a little from here as energy effects fade, revealing some persistent domestic pressures remaining.
- These pressures are moderating as expected – labour market continuing to loosen; wage growth and services inflation falling back.
- That gave MPC confidence to cut Bank Rate again on 7/11.

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- CPI inflation back below 2%. Will rise a little from here as energy effects fade, revealing some persistent domestic pressures remaining.
- These pressures are moderating as expected – labour market continuing to loosen; wage growth and services inflation falling back.
- That gave MPC confidence to cut Bank Rate again on 7/11.
- Growth outlook next year is stronger on the back of the Budget, which will also affect inflation and the labour market. Inflation likely to peak around 2¾%.
- In the MPC’s forecast, spare capacity opens up later than before, but still by enough to act against second round effects and return inflation to target

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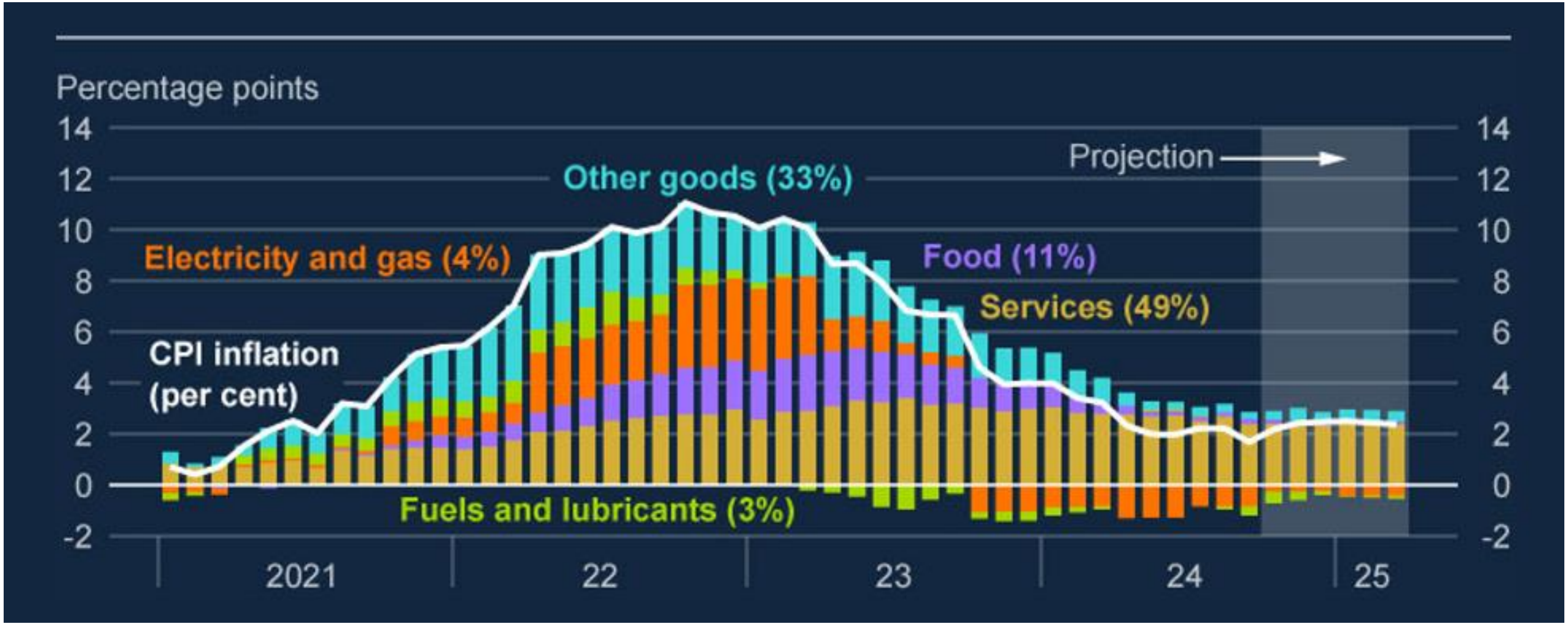
- These pressures are moderating as expected – labour market continuing to loosen; wage growth and services inflation falling back.
- That gave MPC confidence to cut Bank Rate again on 7/11.
- Growth outlook next year is stronger on the back of the Budget, which will also affect inflation and the labour market. Inflation likely to peak around 2¾%.
- In the MPC's forecast, spare capacity opens up later than before, but still by enough to act against second round effects and return inflation to target
- MPC thinks a gradual approach to removing policy restraint remains appropriate.
- But how quickly persistent inflationary pressures fade, and what path for policy will be needed to deal with them, remains the key judgement.

Near-term inflation outlook

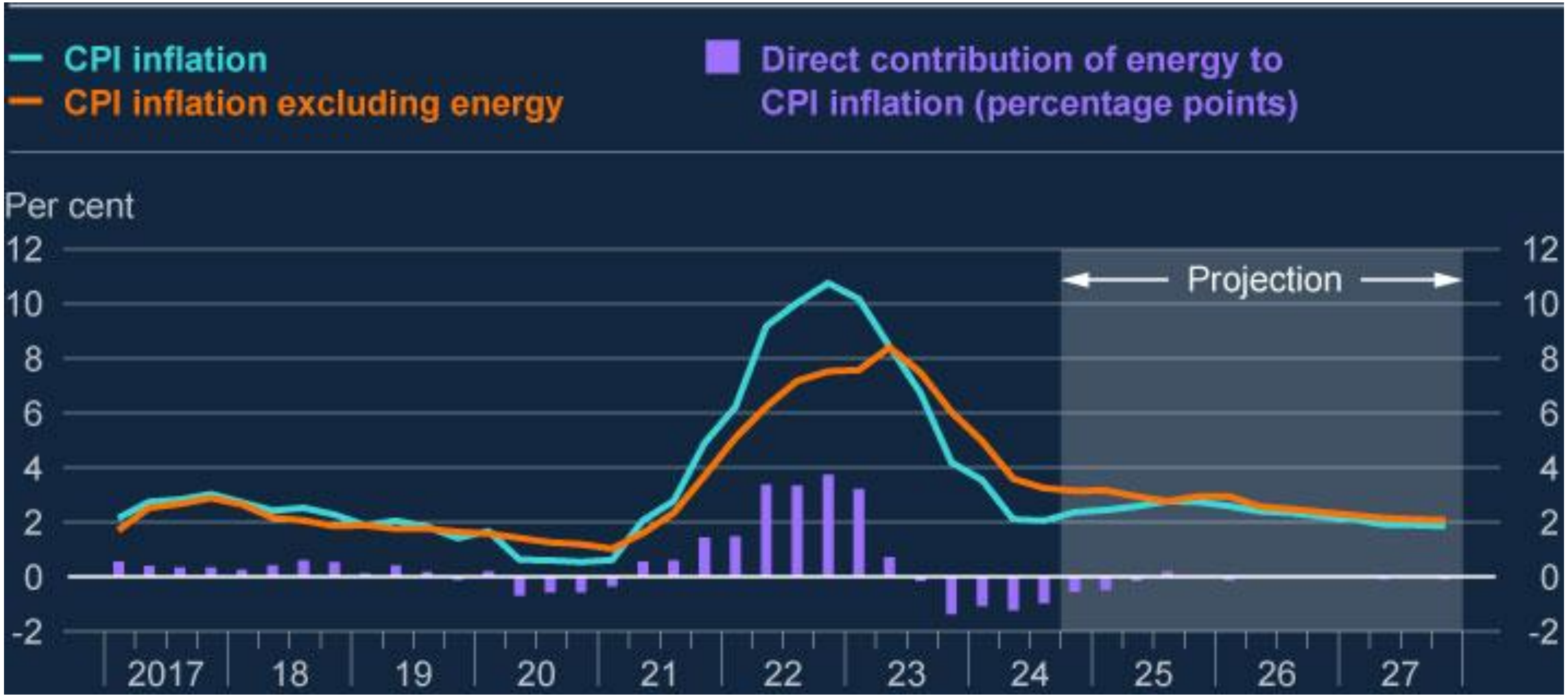
Chart 2.22: CPI inflation fell to 1.7% in September, but it is expected to rise again before the end of the year

Contributions to CPI inflation [(a)]



- CPI inflation fell to 1.7% in September, a bit lower than MPC had expected
- September is likely to be the trough, as energy effects drop out (orange bars get smaller)
- Probably around 2½% across the winter.

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



- Stripping out the effects of energy prices, CPI inflation has fallen by less so far and is still above target
- So still some remaining persistence left in the domestic components of inflation.

Chart 2.23: Core goods inflation weak, but services inflation remains elevated

Annual inflation rates for components of CPI [(a)]

- Looking at goods and services individually, goods price inflation has been very weak, but likely to pick up a little to more normal rates. Risks to global goods prices in both directions
- Services inflation was 4.9% in Sep, a little lower than expected. Likely to hover around this rate.

Chart 2.25: The share of prices being increased each month has risen sharply since 2022

Share of monthly CPI services price quotes that show price increases or decreases, total services and excluding catering and accommodation (a)

- Standing back, price setting in services is normalising, but still some way to go

Current Economic & Financial Conditions

Chart 2.2: Global GDP growth is projected to remain steady

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

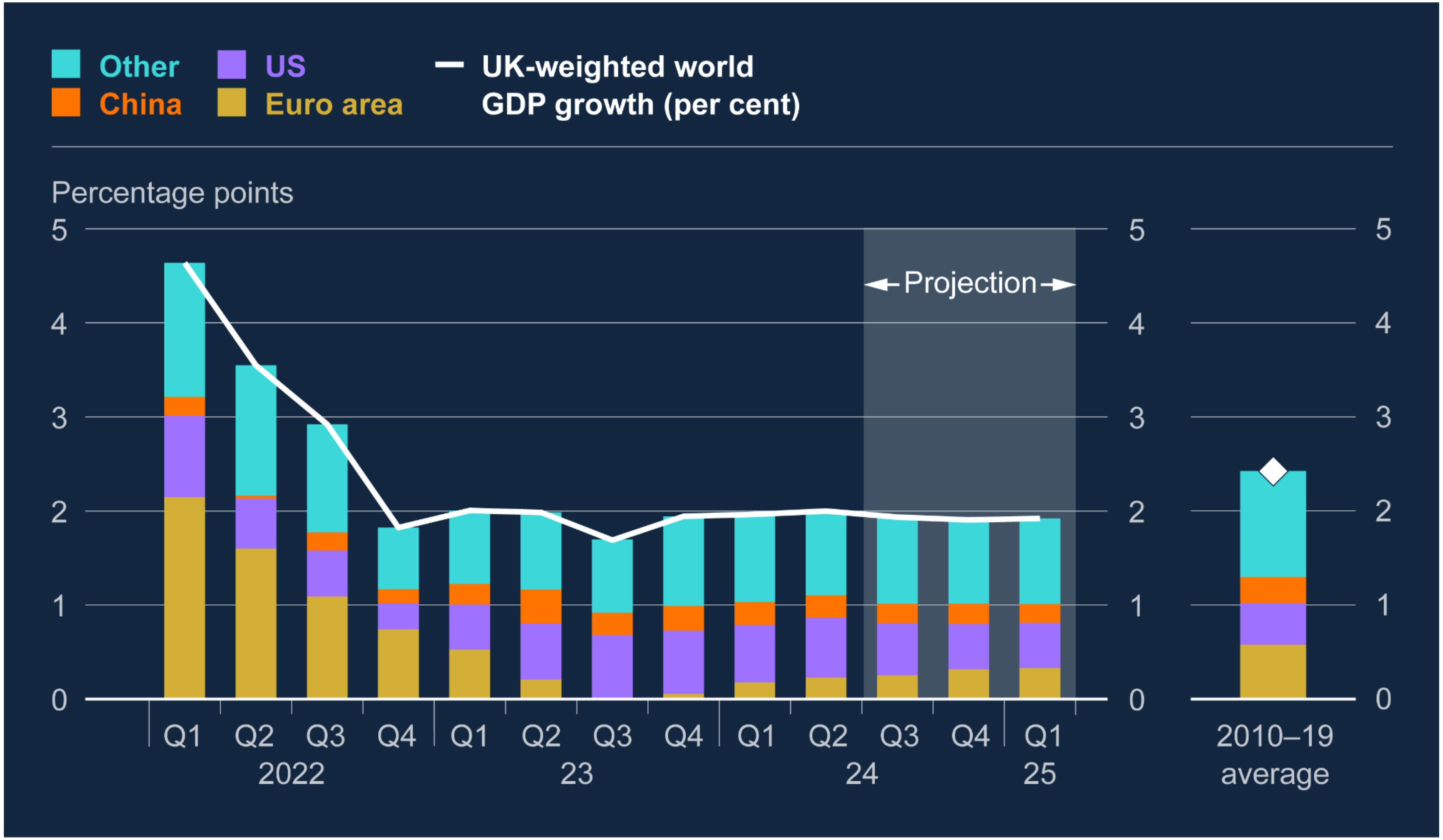


Chart 2.3: Export price inflation has picked up slightly, but remains weak in China

Four-quarter export price inflation across regions[(a)]

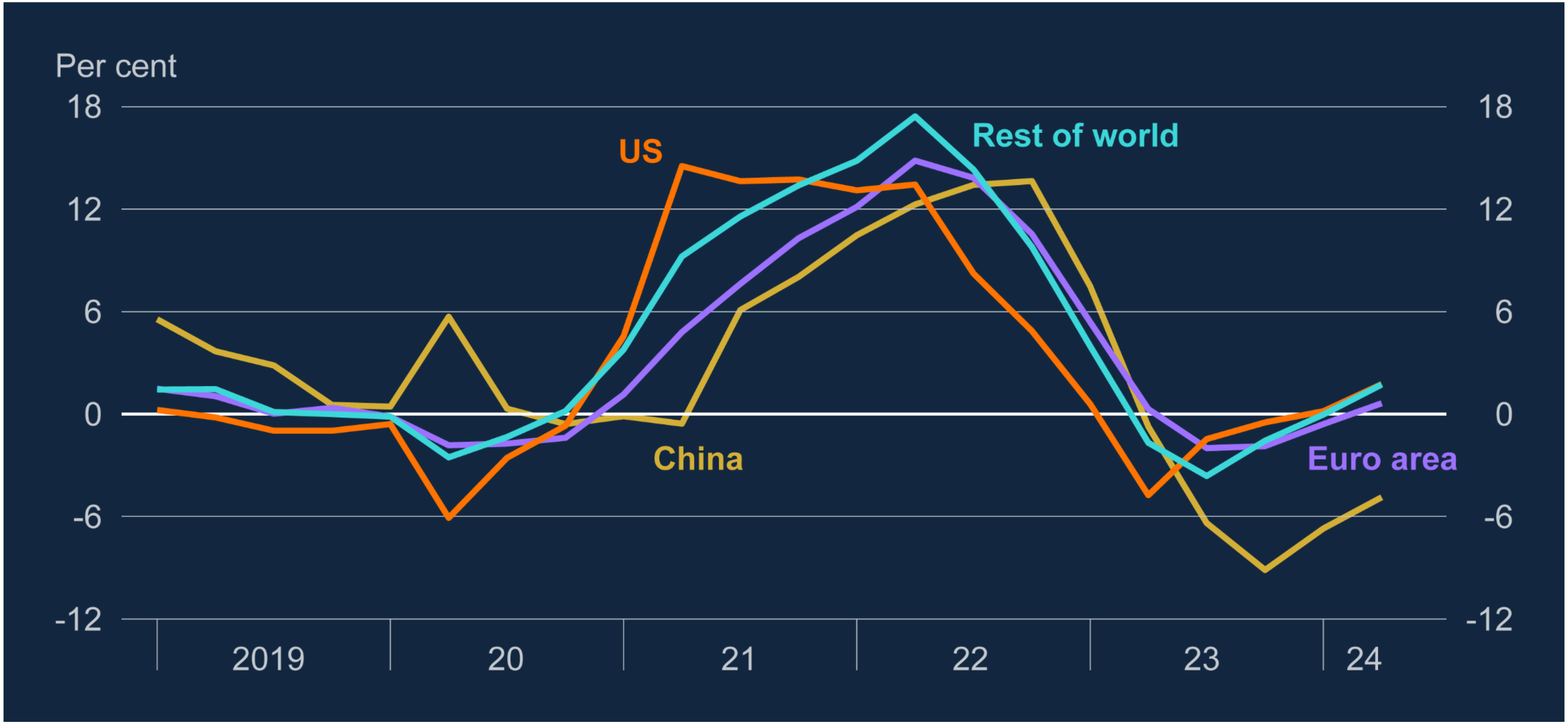


Chart 2.5: Services inflation is moderating across regions

Contributions to annual core services price inflation[(a)]

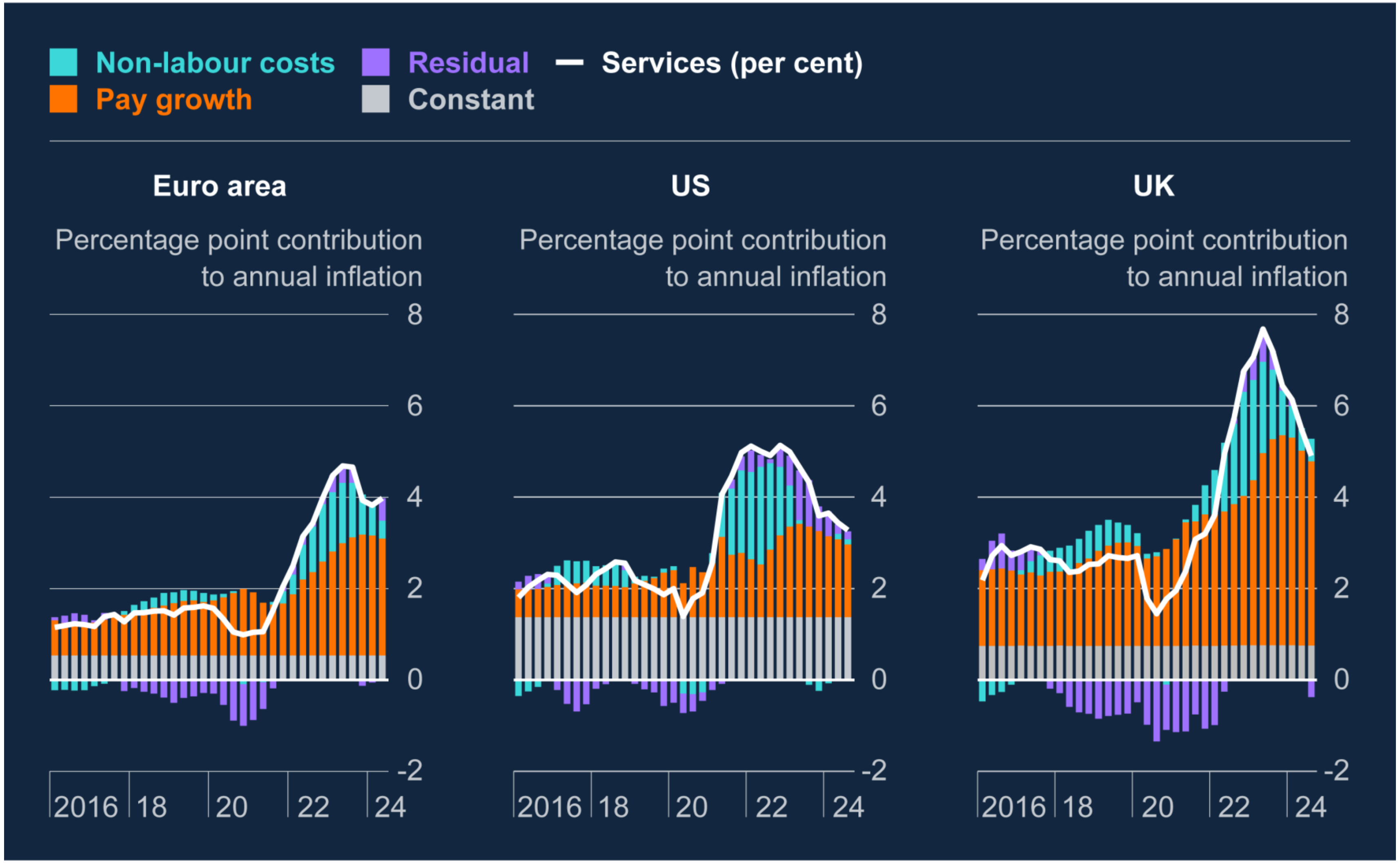
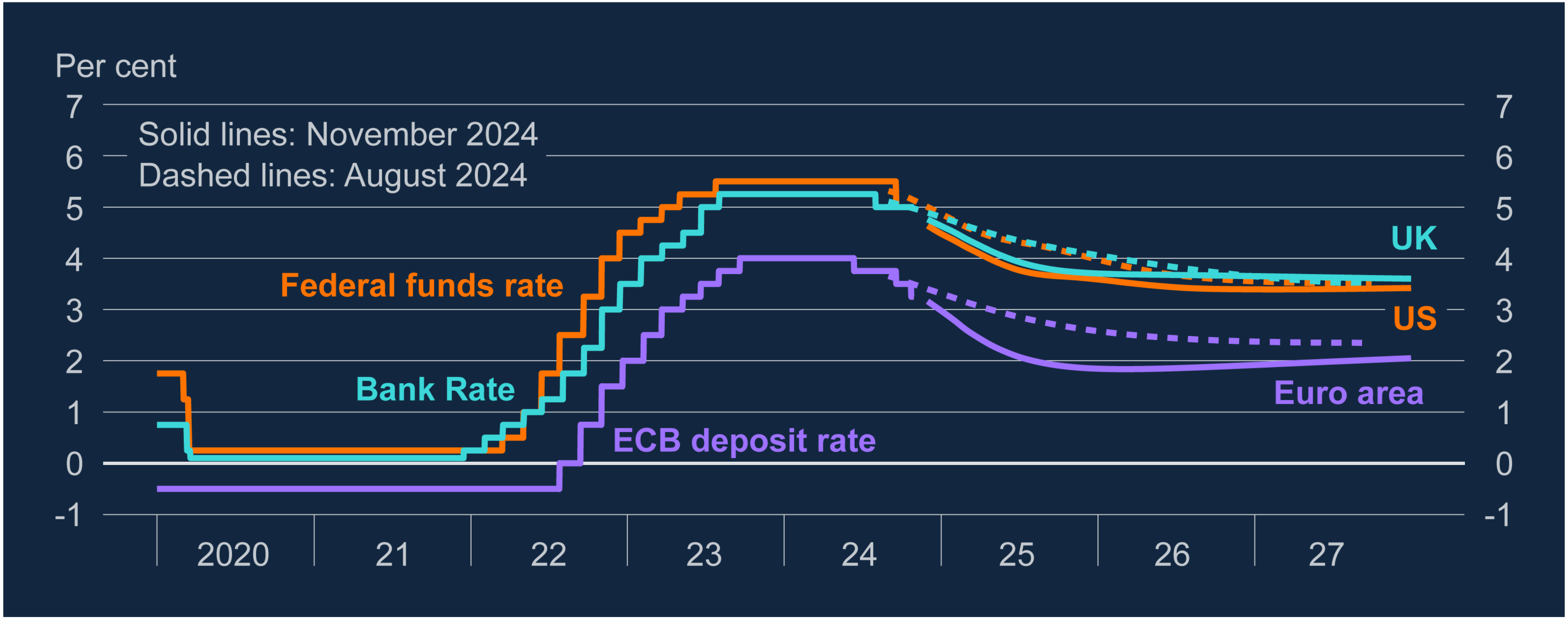


Chart 2.6: Policy rate expectations have shifted down since the August Report

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



However the UK curve rose materially in the wake of the Budget

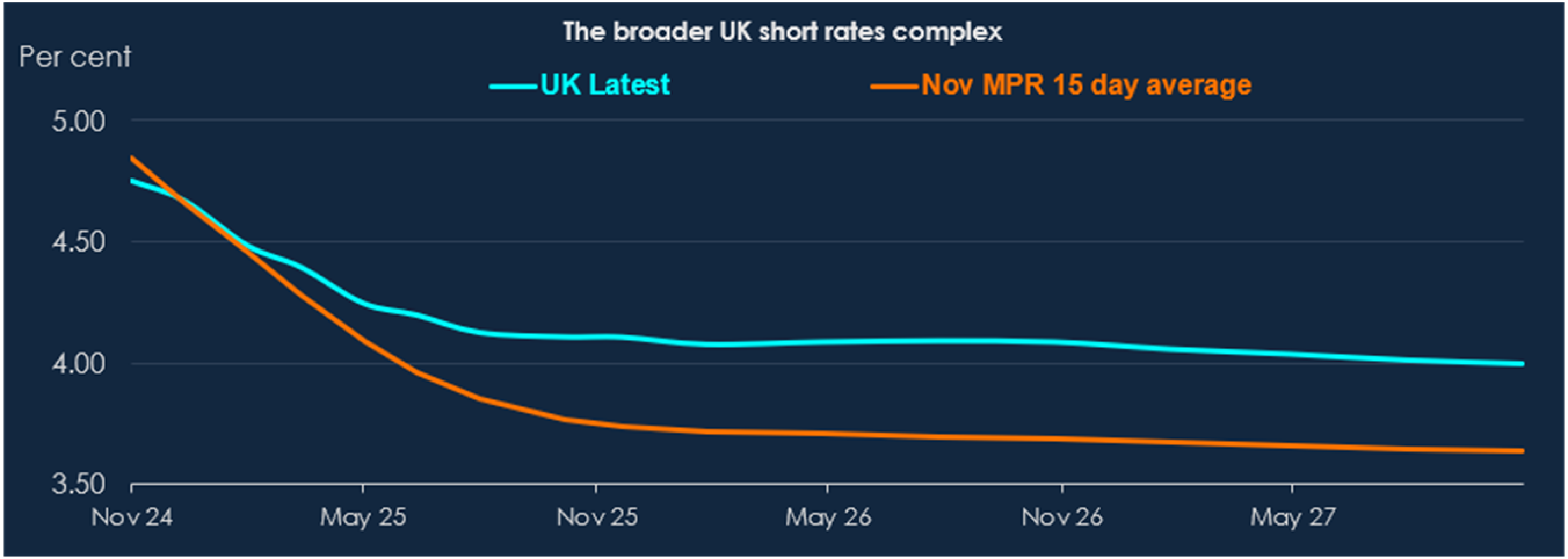
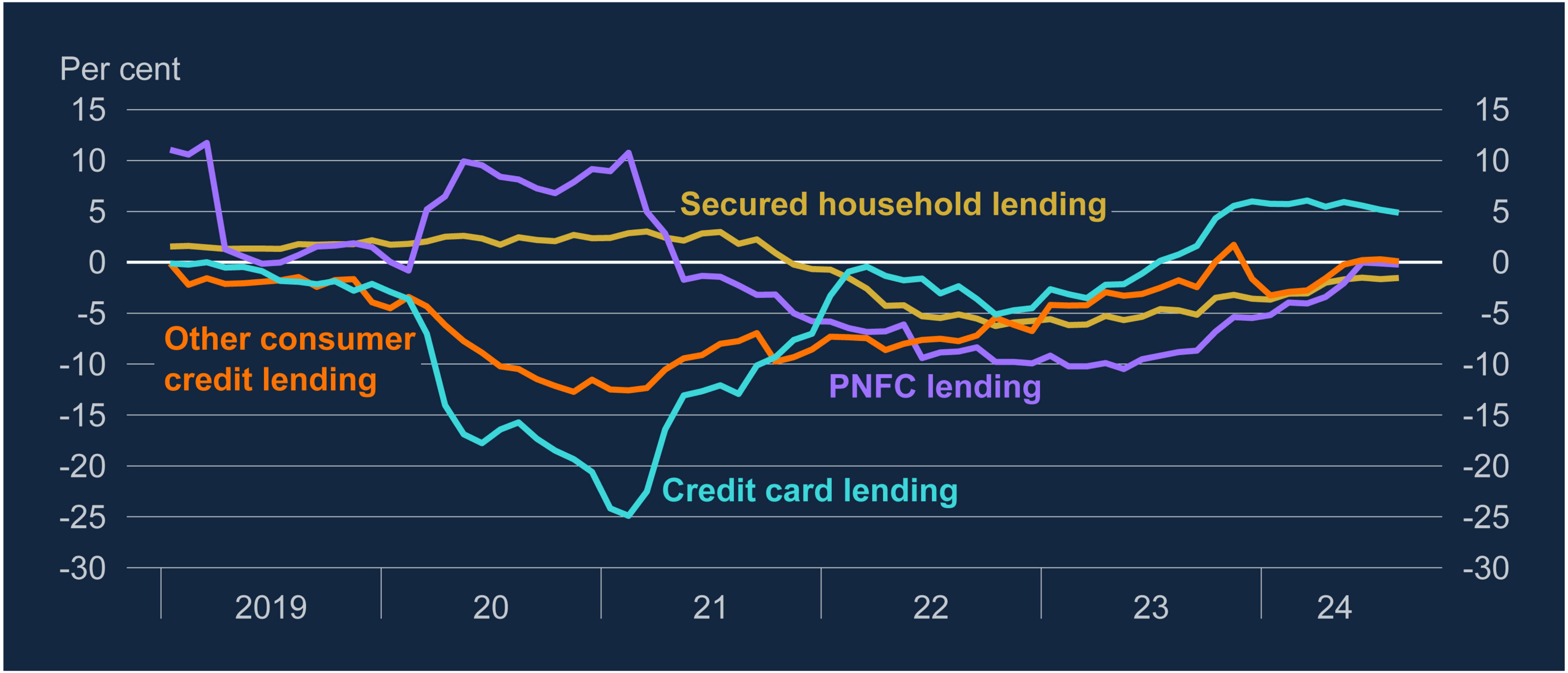


Chart 2.11: Secured household lending growth has risen but remains subdued

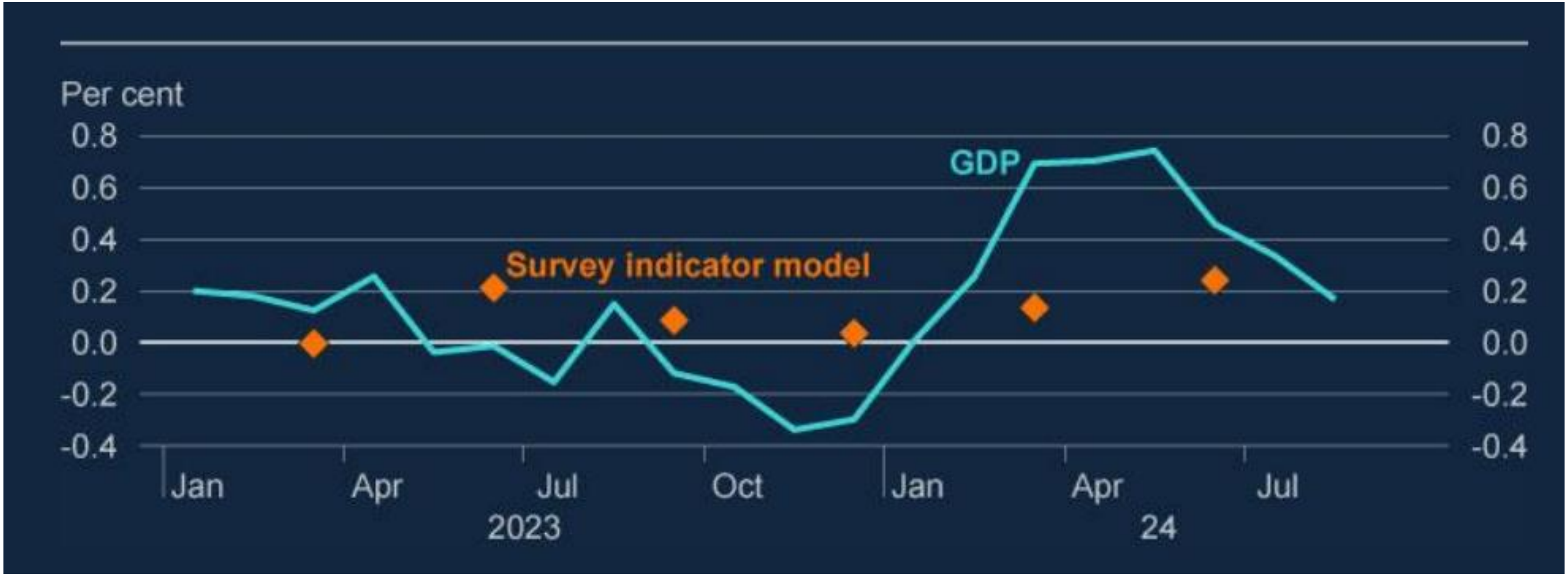
Twelve-month growth rate of M4 lending in real terms, by sector[(a)]



The growth outlook

Chart 2.14: GDP growth was lower than implied by business surveys in 2023 but recovered in 2024

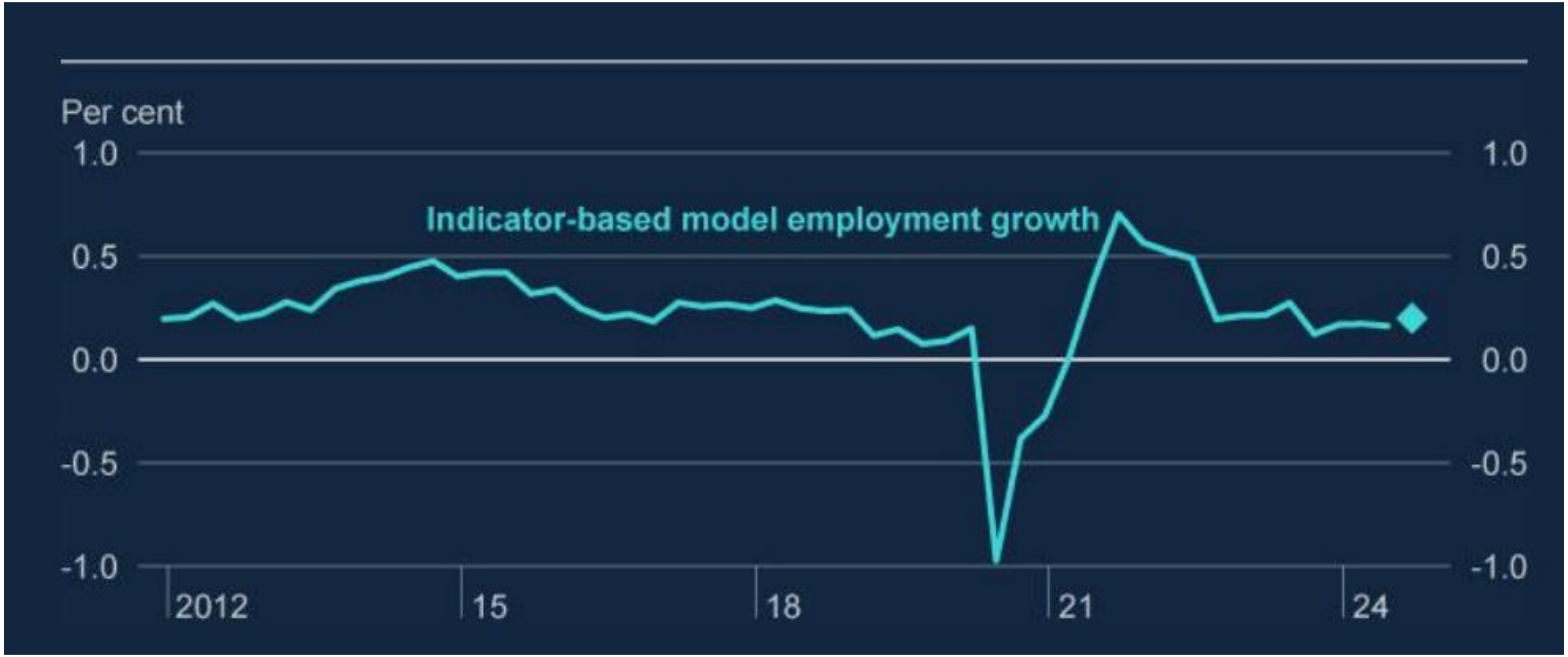
Three-month on three-month growth in GDP and quarterly GDP growth implied by business surveys (a)



- Headline GDP data have been up and down. Surveys suggest a more even pattern of growth over the past year.
- Underlying growth more like 0.3% per quarter and will be close to that in H2.

Chart 2.16: Employment growth is estimated to have been stable

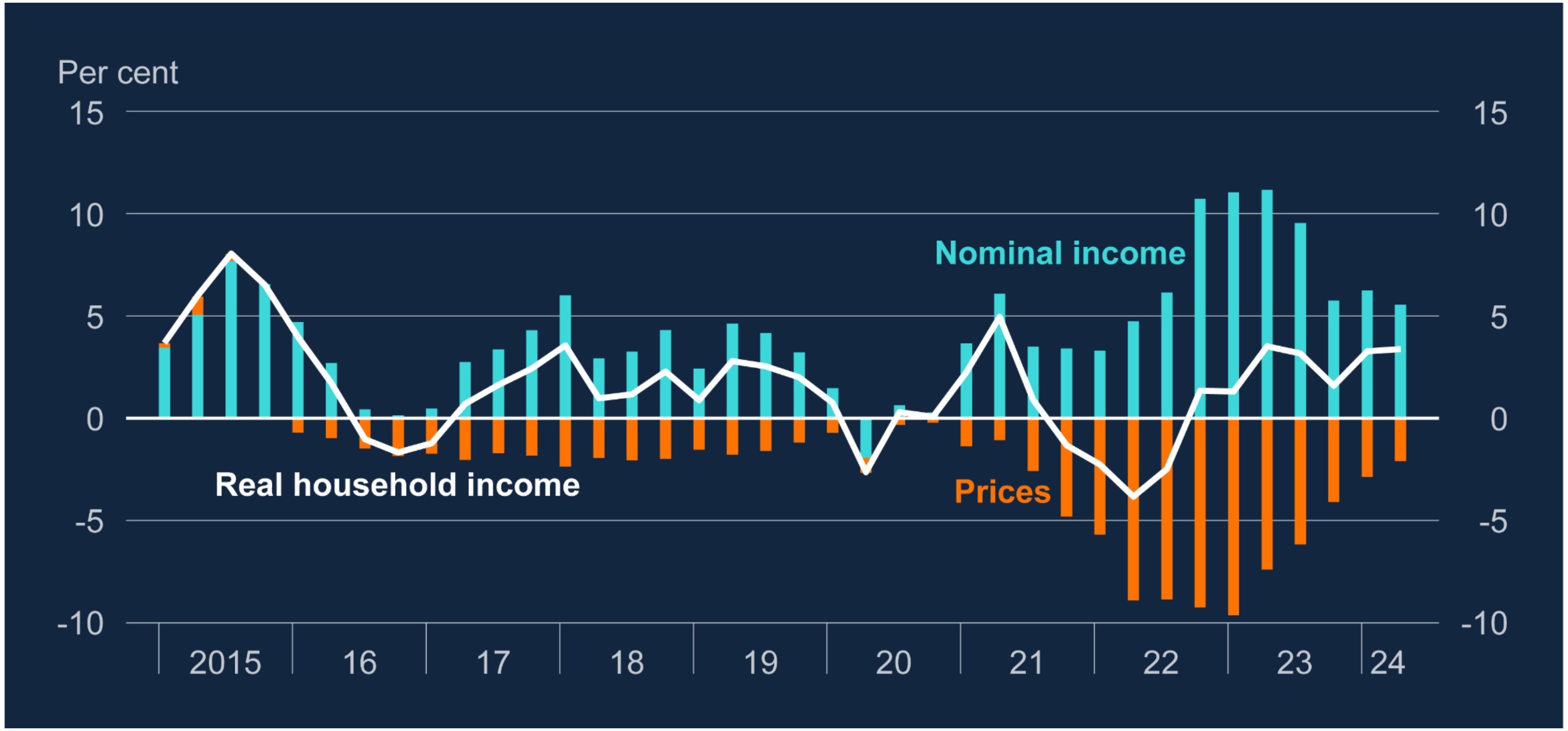
Quarterly employment growth [(a)]



- LFS employment data still hard to read, but looking across a range of indicators also suggests a pretty steady picture of modest employment growth
- Looking forward, need to consider impact of the Budget, but also the position of the consumer

Chart 2.15: Real income growth has picked up as inflation has slowed

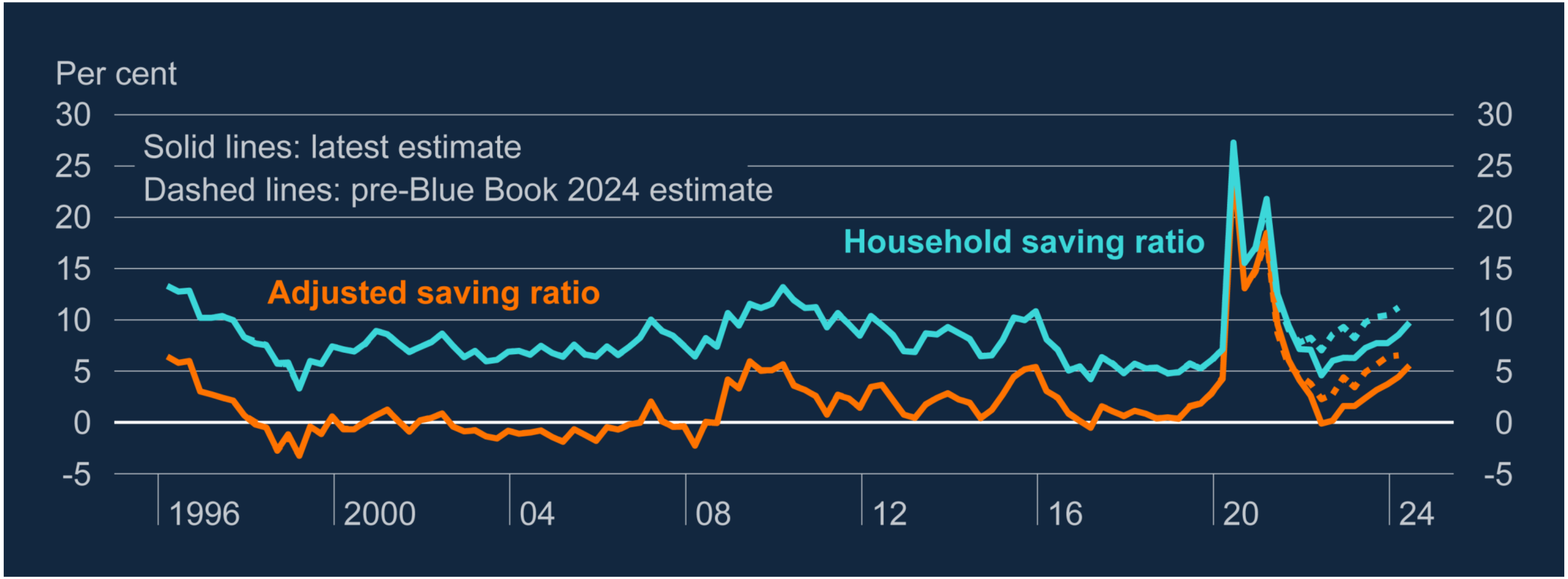
Contributions to four-quarter growth in real household disposable income [(a)]



- Real income growth is currently fairly healthy for households, as they benefit from fading external costs, while wages and remain elevated and the labour market still tight

Chart A: Despite downward revisions in the latest data, the aggregate household saving ratio is higher than pre-pandemic

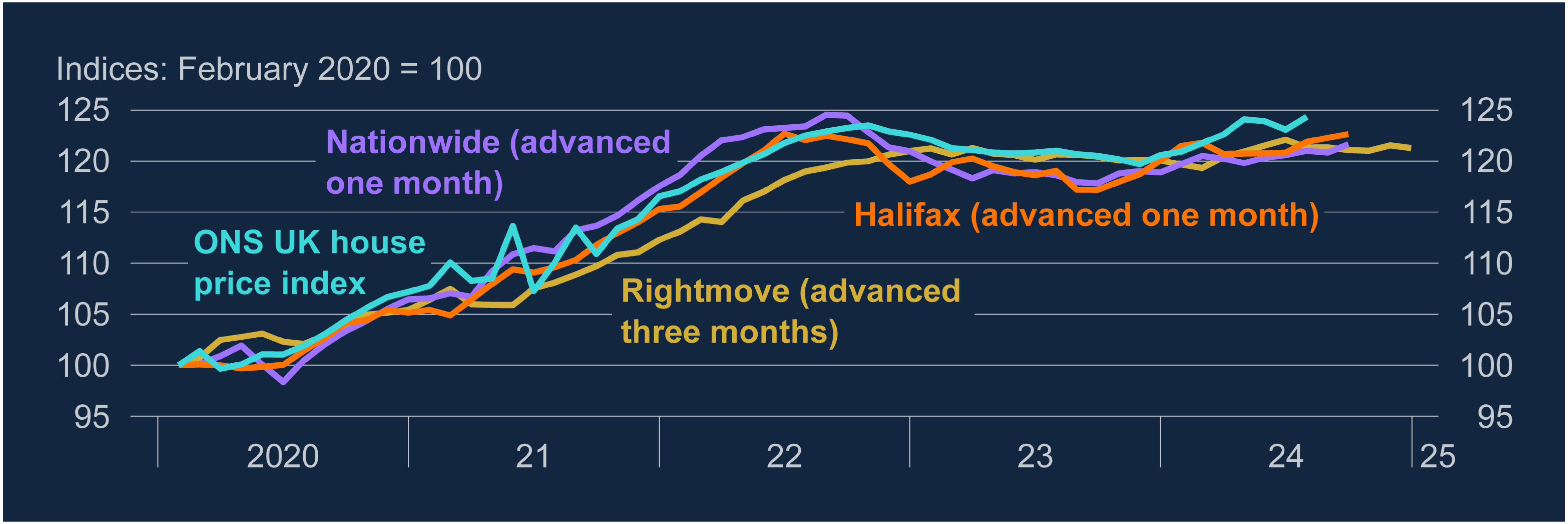
Household saving ratio [(a)]



- Nonetheless household savings rate has picked up steadily over the past couple of years, to around 10%, even if some of the increase was revised away in Blue Book 2024
- In large part that is going to reflect higher interest rates, but this impact should soon be peaking

Chart 2.10: House prices have risen in 2024

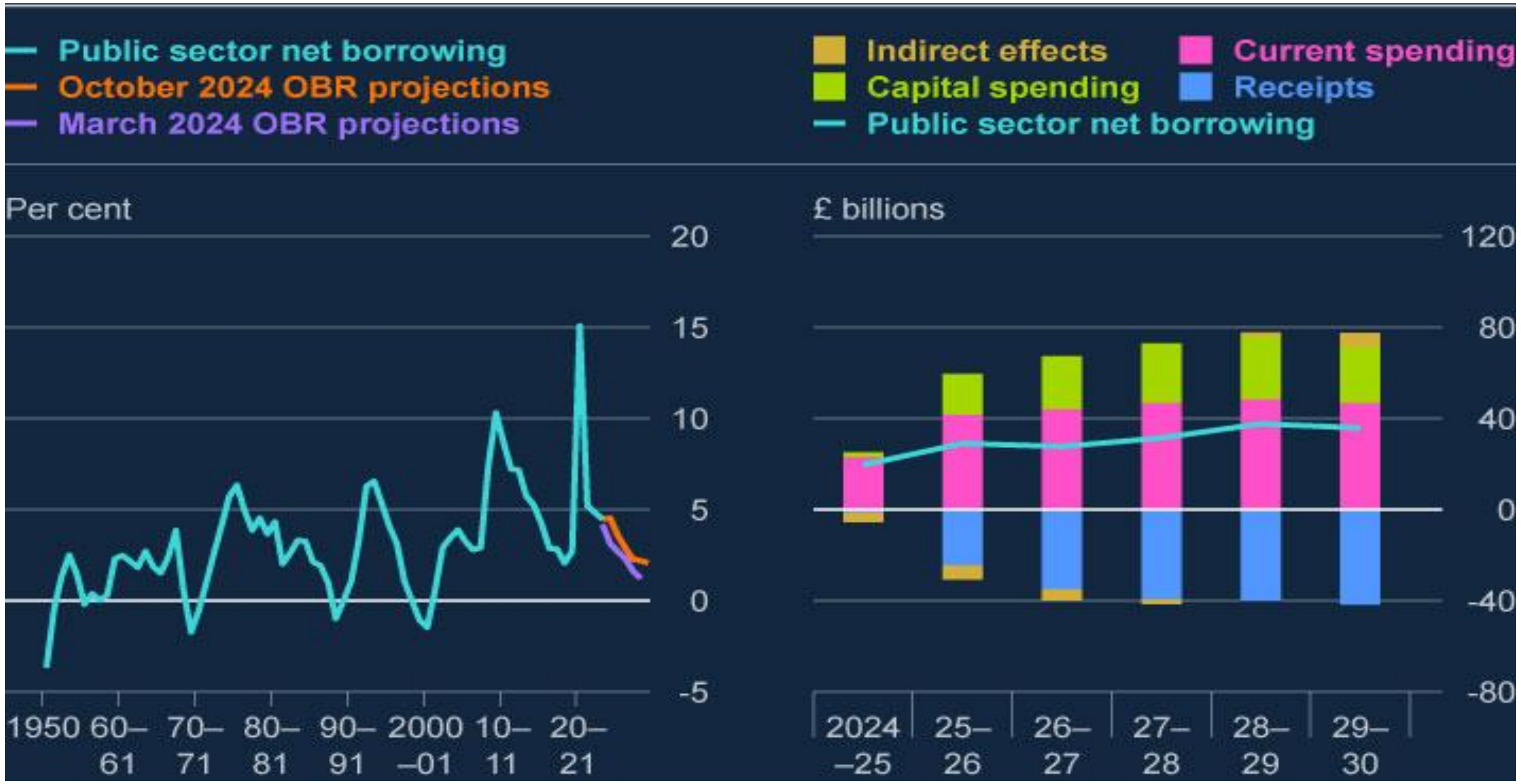
House price indices (a)



- …But early signs of a recovery in the housing market may suggest a broader change in sentiment.
- MPC expect savings rate to fall back from here from 10% to 8%, but timing uncertain

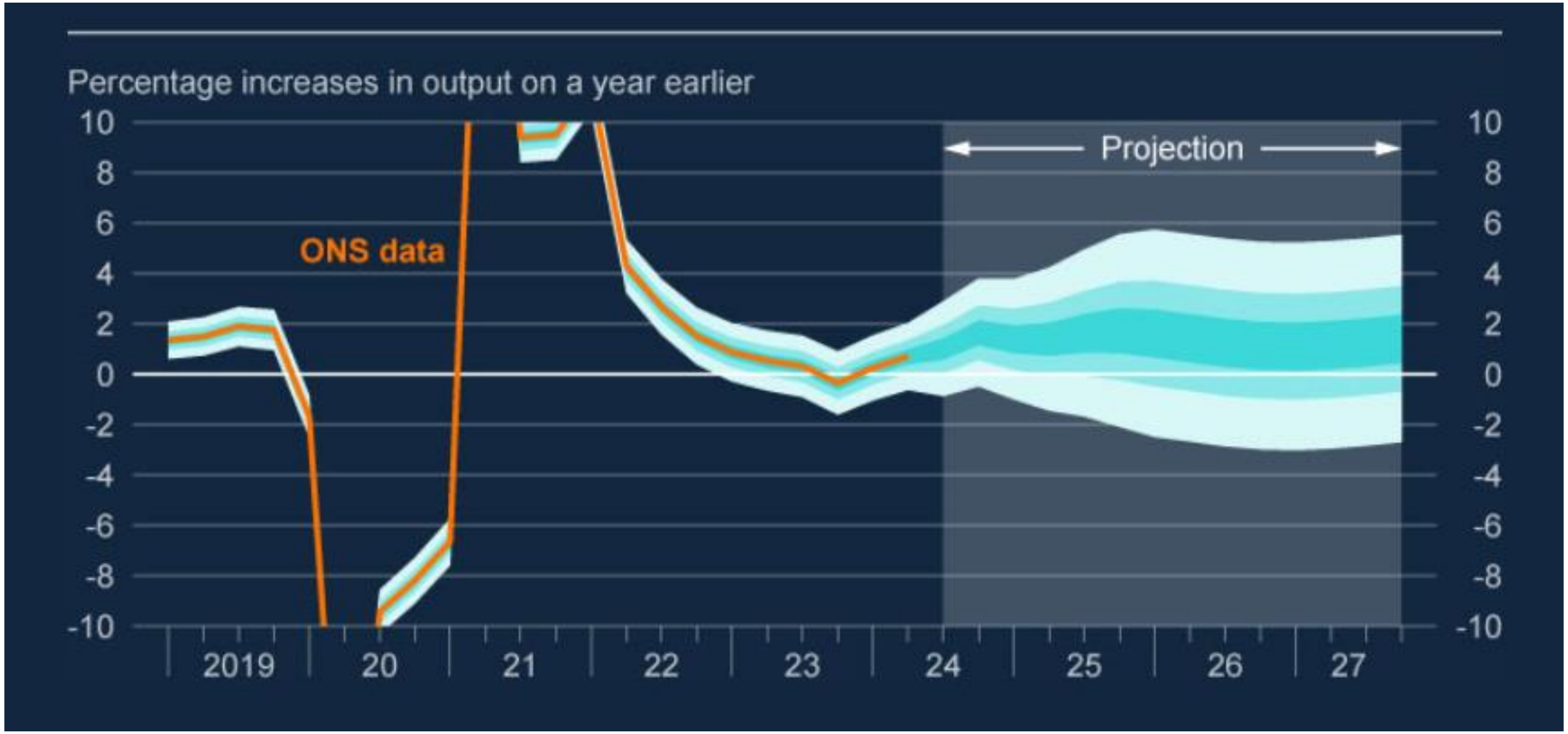
Chart A: Public sector net borrowing is projected to be higher than under the OBR's March projections

Public sector net borrowing (PSNB), as a per cent of GDP (left panel) and contributions to change in the OBR's PSNB projection between March 2024 and October 2024 (right panel) [(a)]



- Borrowing is expected to be higher over the next few years, as the increase in current spending and planned increase in investment spending is not quite matched by the increase in taxes
- Peak impact of ¾% of GDP, reasonably front-loaded. Consolidation still planned.

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



- Growth picks up next year to 1½% from 1% in 2024. Falling back to 1¼% further out.
- Based on a 15-day average of the yield curve up to 29 October.

The medium term inflation outlook

Monetary policy is working, but uncertainties from here

- Monetary policy has 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.

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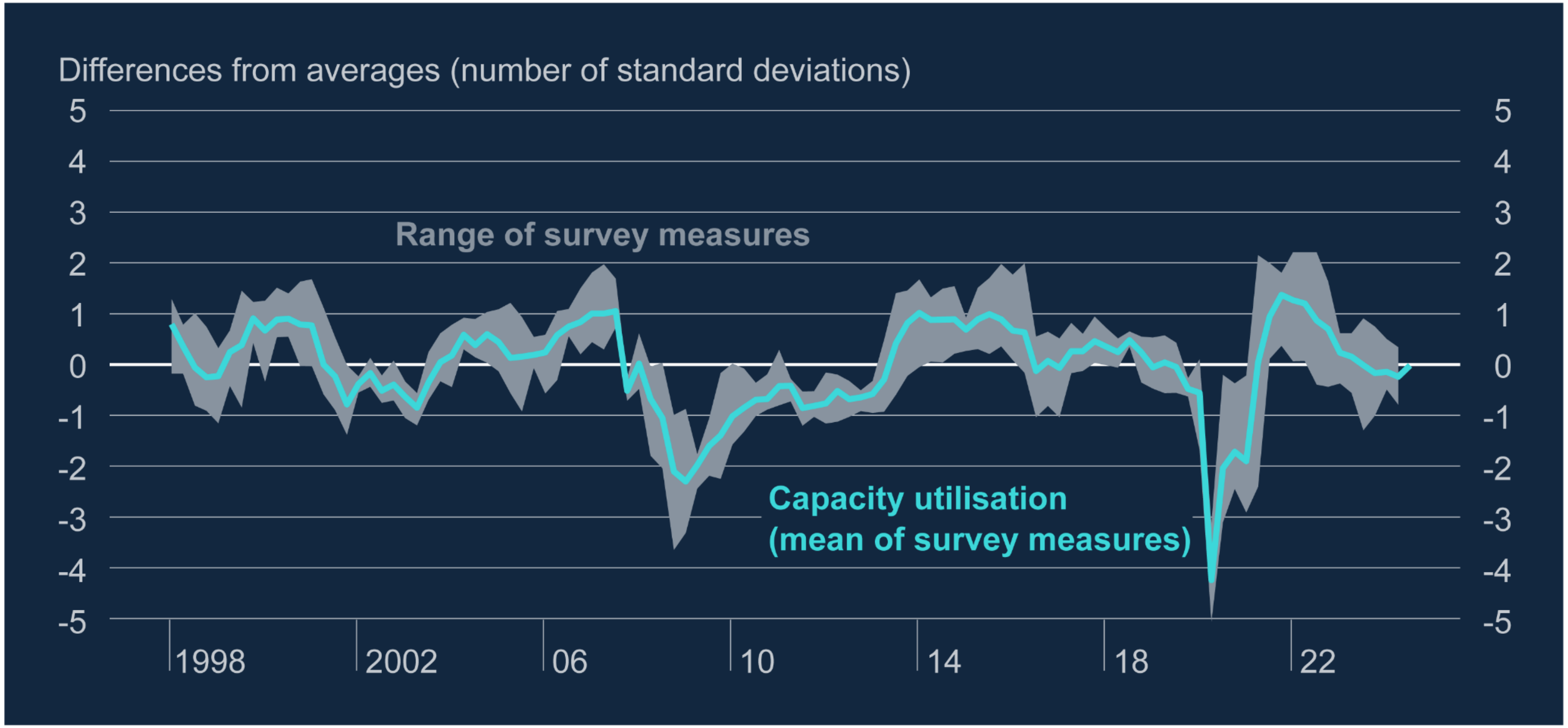
- Monetary policy has been guided by the need to squeeze remaining inflationary pressures out of the economy to achieve the 2% target both in a timely manner and on a lasting basis.

- Evolving evidence encouraging, but is this persistent element of inflation truly on course to decline, and what it will take to make it happen?
  - Case 1 – the decline in persistence now almost baked in as the shocks that drove up inflation continue to unwind. Would be consistent with a less restrictive path for policy
  - Case 2 – it requires a period of economic slack. This is the view underlying the MPC’s forecast.
  - Case 3 – a more permanent change to wage and price setting that requires monetary policy to remain tighter for longer.

Chart 2.21: Measures of capacity utilisation are close to their average levels over the past

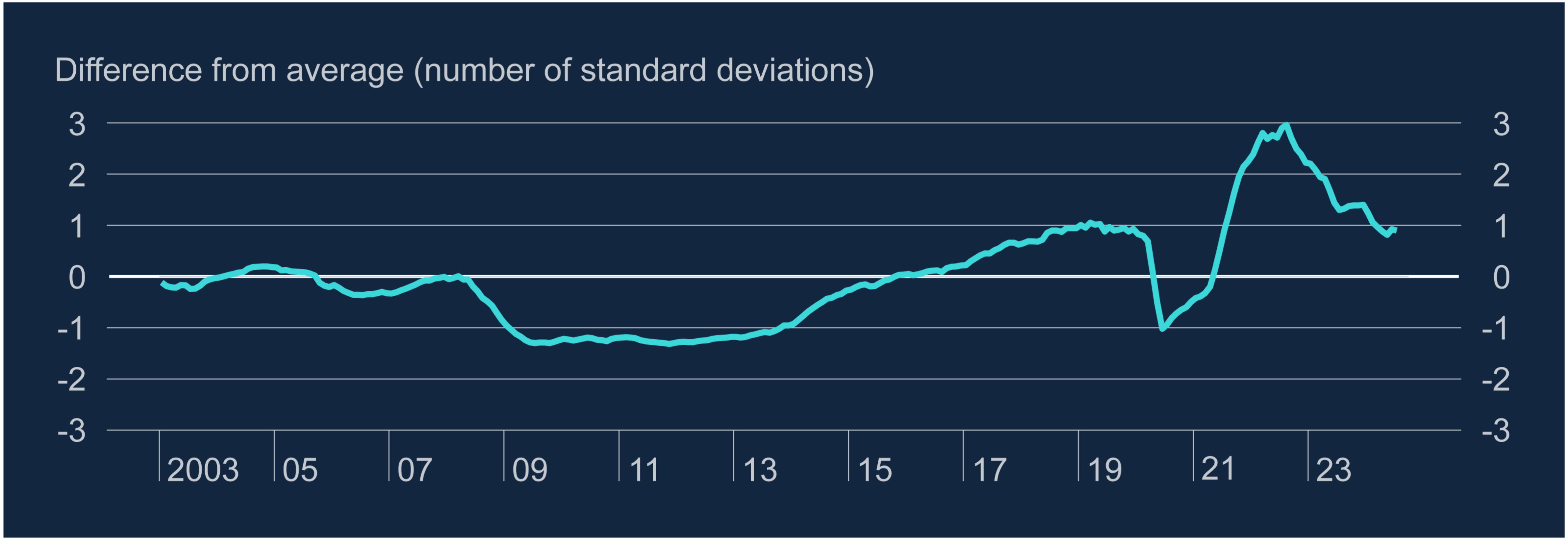
Survey indicators of capacity utilisation [(a)]



- Capacity utilisation indicators are running around long-run averages and the economy seems to be in broad balance at the moment

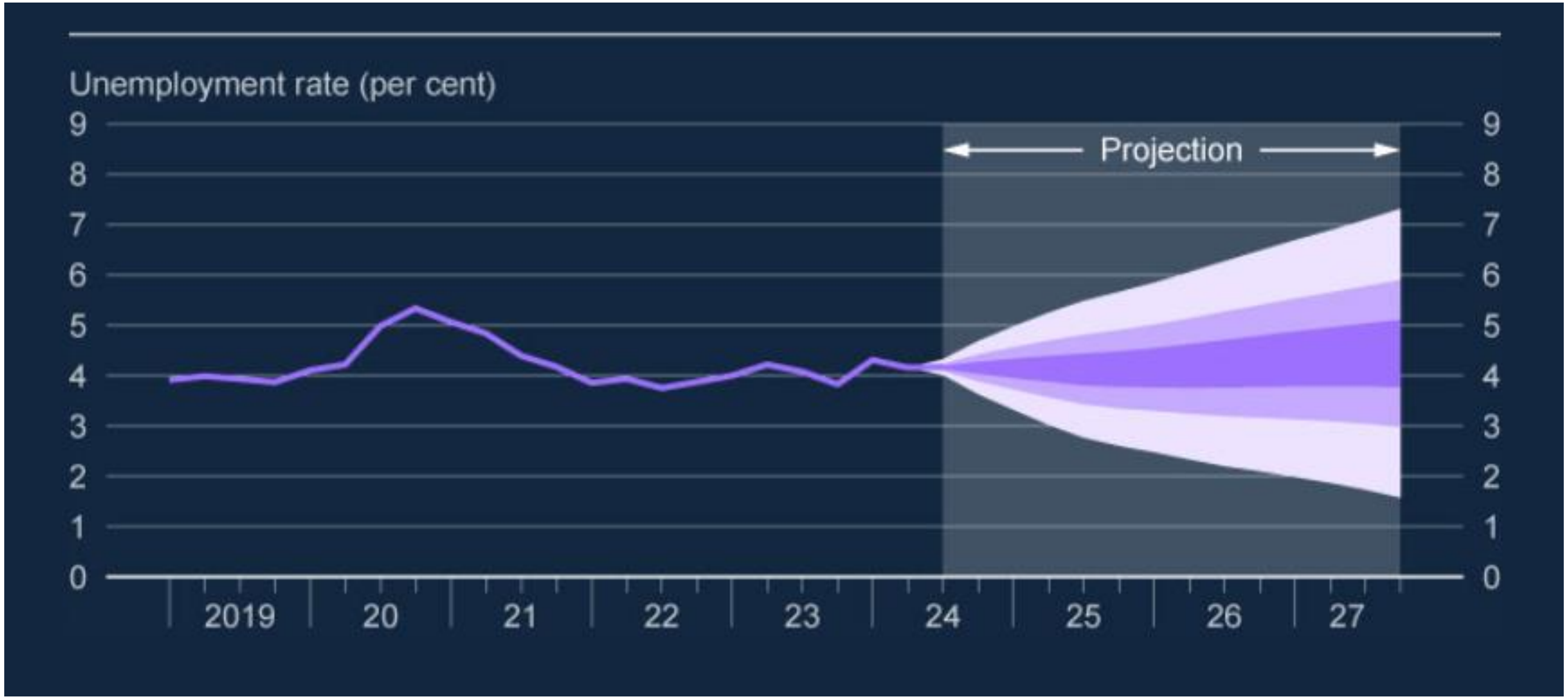
Chart 2.19: Tightness in the labour market continues to ease, although at a slower pace than in 2023

Vacancies to unemployment ratio [(a)]



- In the labour market, the vacancy-to-unemployment ratio is back to pre-Covid levels, but there's probably still a bit of tightness remaining

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



- The stimulus in the Budget will push out the point at which spare capacity is likely to open up
- But a fiscal consolidation is still planned, growth will probably be slowing, monetary policy is still restrictive. Unemployment rises to 4½% by the end of the forecast

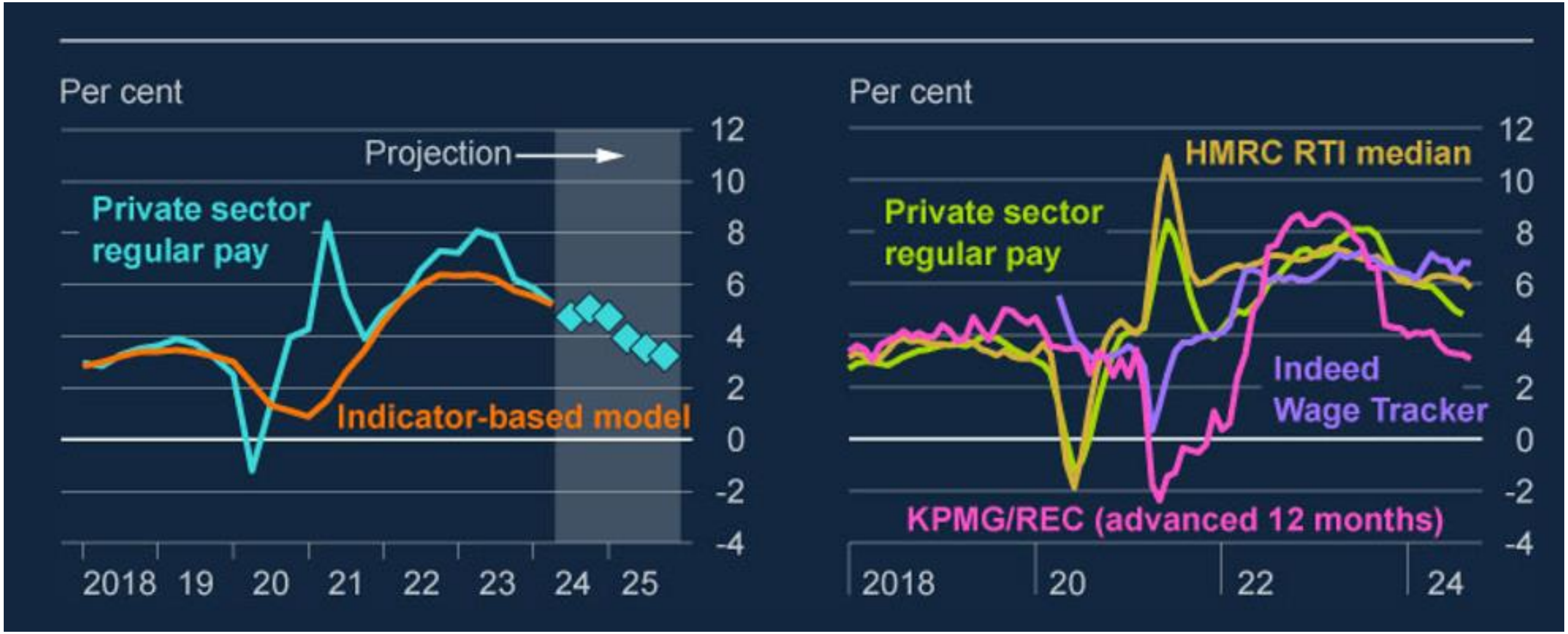
Chart B: Policies included in the Budget are expected to raise CPI inflation by just under ½ of a percentage point at their peak

Impact of Budget on CPI inflation forecast (a)

- As well as affecting inflation through stronger demand, some measures in the Budget will affect inflation directly (eg NICS, fuel duty, VAT on private schools etc)
- NICS impact particularly uncertain – implications for prices, wages, employment and margins

Chart 2.29: Most indicators of wage growth have moderated in recent quarters

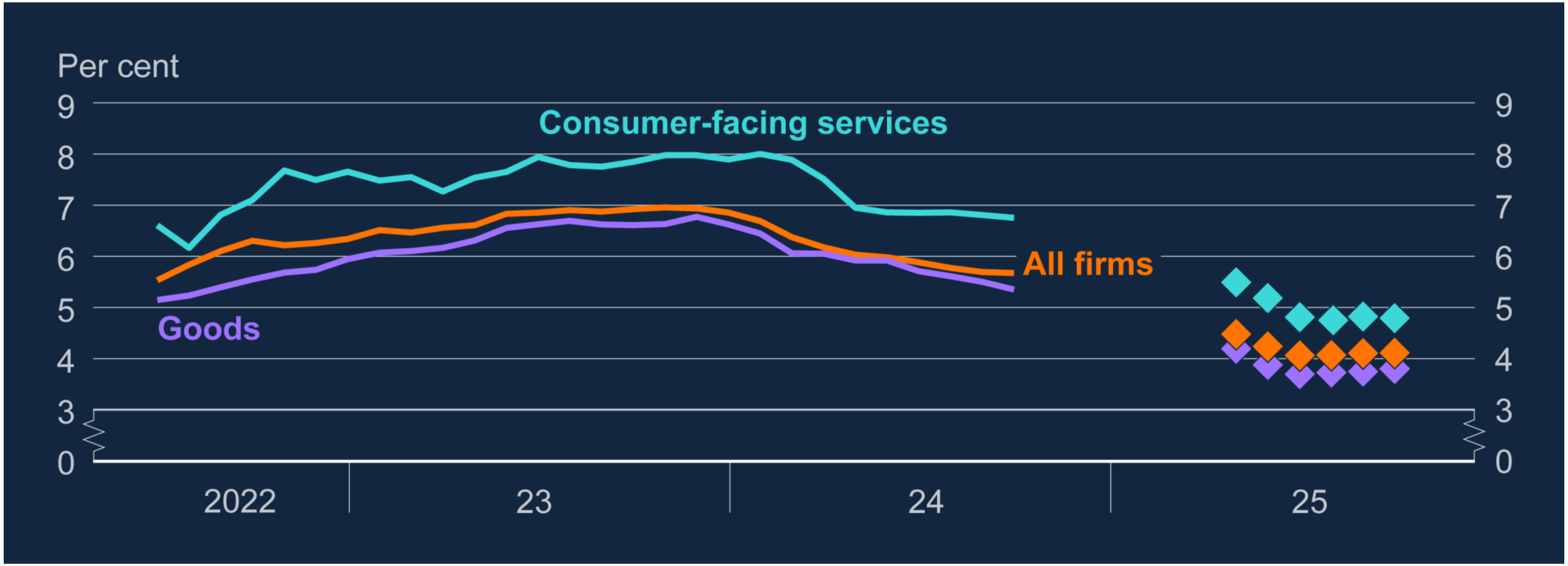
Measures of annual private sector wage growth [(a)]



- Wage growth on most measures is continuing to ease off but still elevated. 4.8% in August
- Will probably hover around current rates over the rest of the year, but likely to ease off.

Chart 2.31: DMP Survey respondents expect wage growth to decline, but those expectations appear to have stabilised at elevated levels

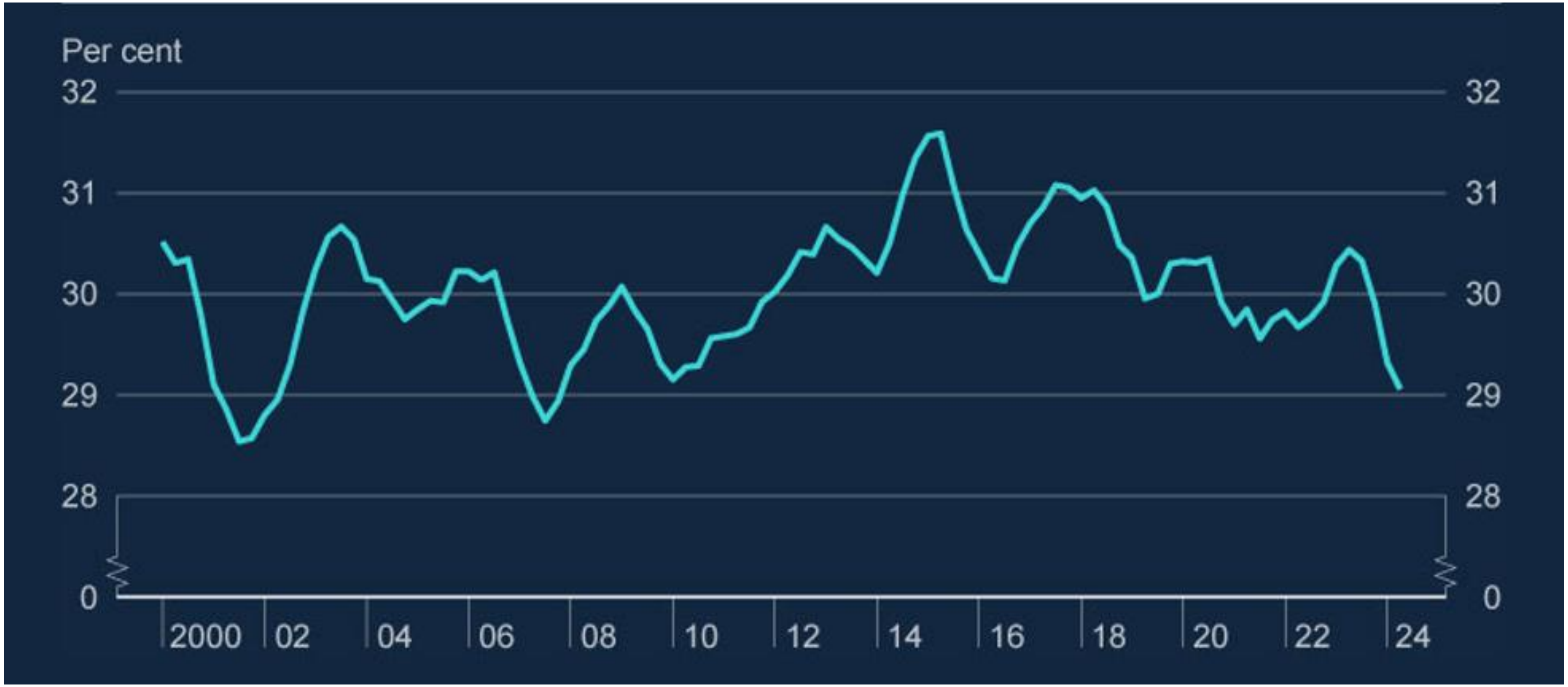
Realised annual wage growth and 12-month ahead expectations (a)



- Early intelligence from our Agency Network suggests settlements next year in the 2-4% range.
- Lots of factors will play into that, and they'll play out in different ways across sectors
- DMP respondents (taken prior to Budget) are closer to 4%, higher in consumer-facing services.

Chart 2.26: The profit share of income has fallen slightly in recent years

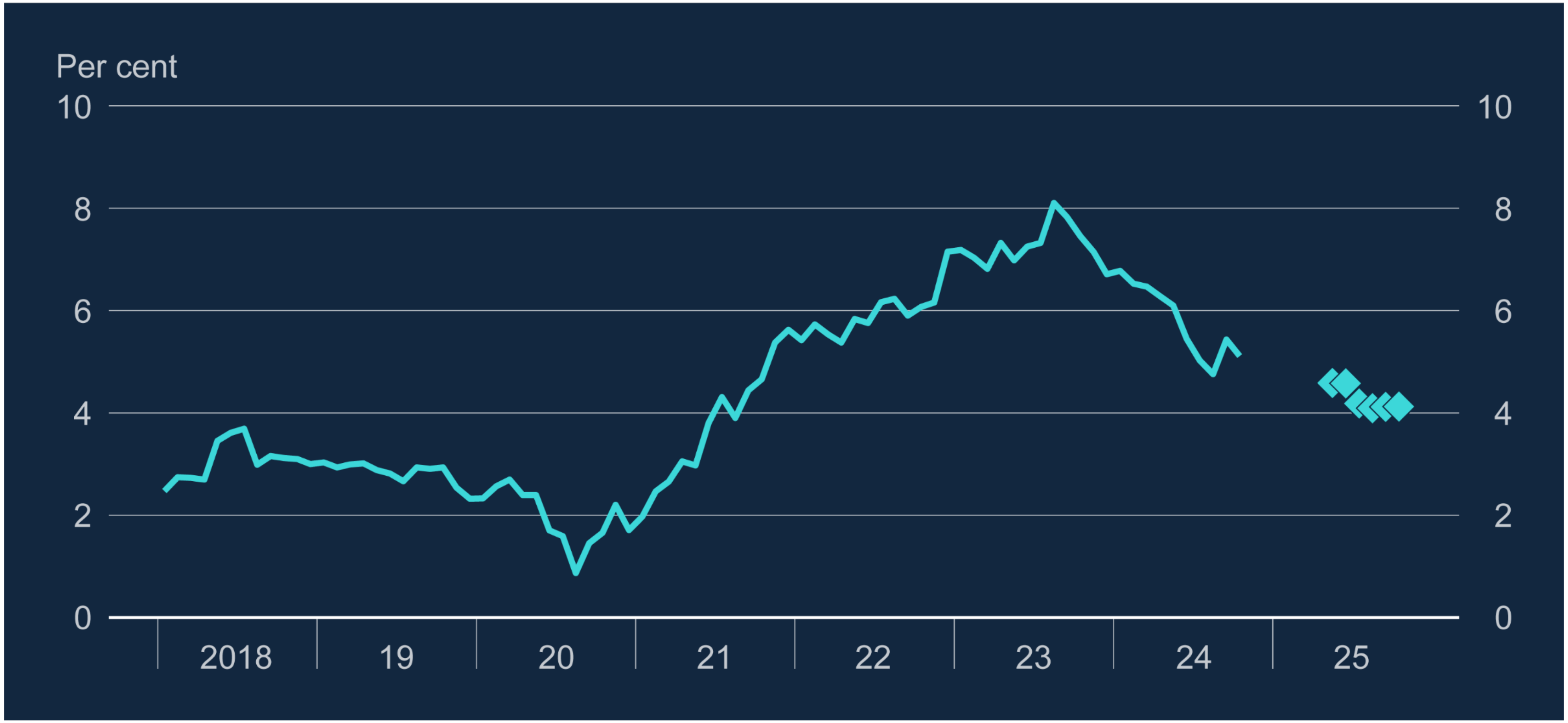
Private sector profit share, four quarter moving average [(a)]



- Flip-side of the pick up in household incomes has been some fall in margins.
- Lots of factors will play into how firms will think about this – strength of demand, tightness of the labour market, other pressures on costs, broader pricing power

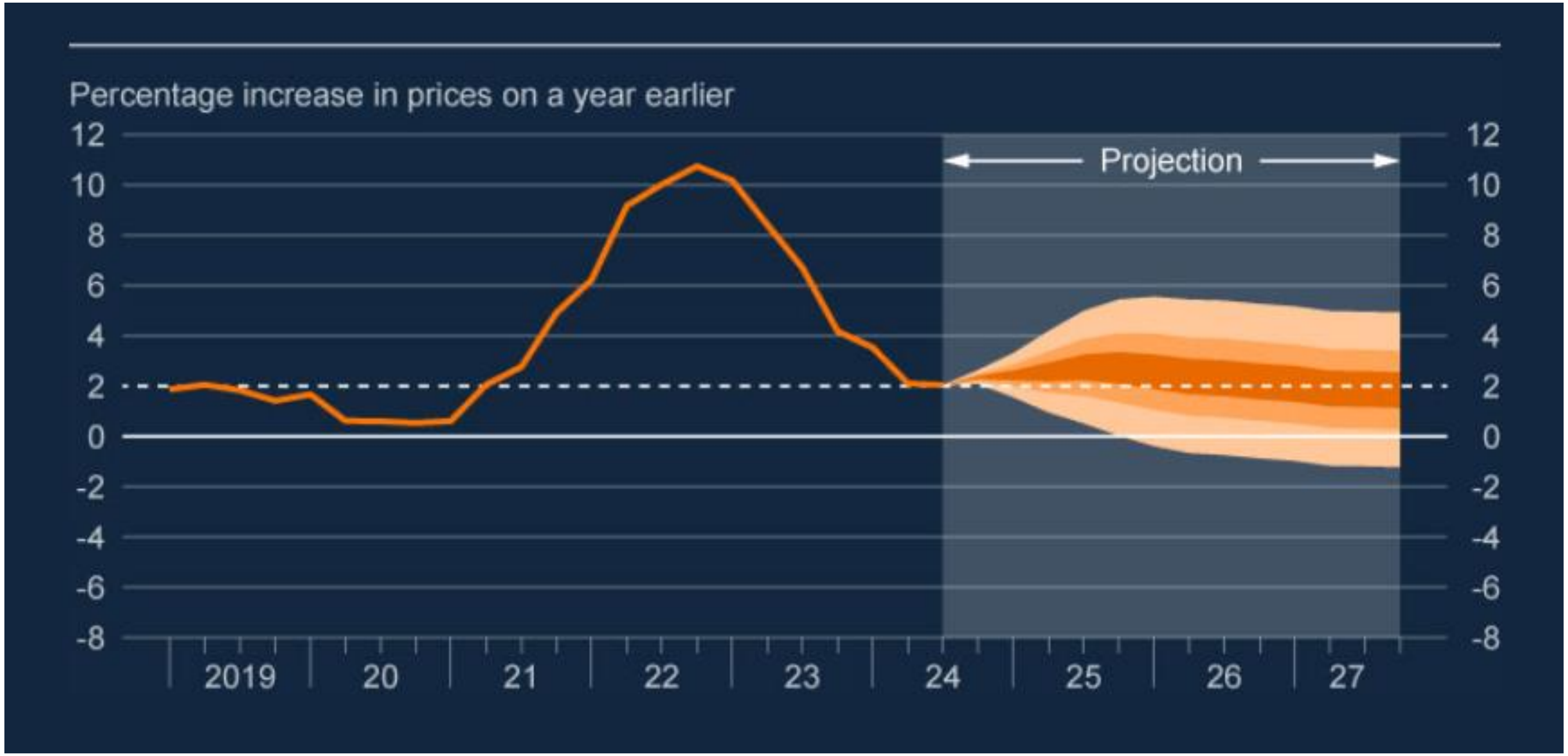
Chart 2.27: Firms responding to the DMP Survey expect further declines in services price inflation

Annual consumer service price inflation, realised and expected [(a)]



- DMP survey asks companies about expectations for their own prices too.
- Aggregating across consumer services firms, this suggests some further modest disinflation.

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



- Inflation in the forecast peaks at around 2¾% next year before falling back.
- Spare capacity opens up later than before, but still by enough to act against second round effects and return inflation to target

Table 1.A: Forecast summary [a] [b]

	2024 Q4	2025 Q4	2026 Q4	2027 Q4
GDP (c)	1.7 (2)	1.7 (0.9)	1.1 (1.5)	1.4
CPI inflation (d)	2.4 (2.7)	2.7 (2.2)	2.2 (1.6)	1.8
Unemployment rate (e)	4.2 (4.4)	4.1 (4.7)	4.3 (4.7)	4.4
Excess supply/**Excess demand** (f)	0 (-¼)	-¼ (-1¼)	-½ (-1)	-¼
Bank Rate (g)	4.8 (4.9)	3.7 (4.1)	3.7 (3.7)	3.6

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)	4.8 (4.9)	3.7 (4.1)	3.7 (3.7)	3.6
Sterling effective exchange rate (d)	100	82	81 (81)	85 (84)	84 (84)	84 (83)	83
Oil prices (e)	39	77	84 (84)	75 (83)	73 (78)	71 (75)	71
Gas prices (f)	29	52	101 (101)	101 (92)	101 (95)	87 (84)	78
Nominal government expenditure (g)	7¼	2¼	7 (7)	6 (2¾)	6¾ (2¼)	3½ (2¾)	3¼

MPC perspective and policy

Main messages from the Monetary Policy Summary

- “At this meeting, the Committee voted to reduce Bank Rate to 4.75%, reflecting the continued progress in disinflation.

- Based on the evolving evidence, a gradual approach to removing policy restraint remains appropriate. 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 continues to monitor closely the risks of inflation persistence and will decide the appropriate degree of monetary policy restrictiveness at each meeting”

Q&A