MPC MEMBERS

COPIES OF THE APRIL 2015 PRE-MPC MEETING PRESENTATIONS

In advance of the MPC meeting, please find attached copies of all presentations given at the April 2015 Pre-MPC meeting.

Monetary Policy COO Division (TS-02)
2nd April 2015

Financial Markets

April 2015 Pre-MPC
FED, MFAD & SMD

Plan

- Interest rates and monetary policy
  - Euro area
  - US
  - UK
- Sterling
- What are equity markets telling us about the growth outlook?

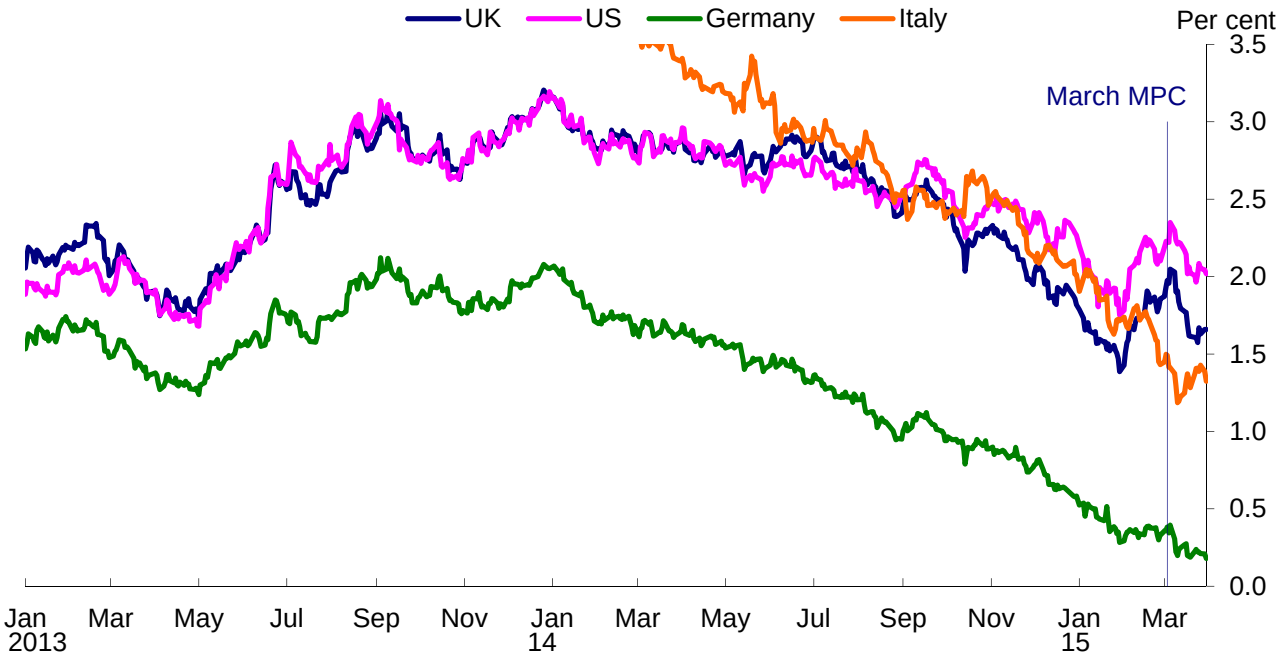
Summary table

	Feb IR 15-day average (4/2/15)	March MPC (4/3/15)	Latest (31/3/15)	Changes since Feb IR	Changes since March MPC
UK 3y spot OIS (%)	0.73	1.01	0.78	5 bps	-24 bps
UK 10y spot (%)	1.53	1.98	1.66	13 bps	-31 bps
US 10y spot (%)	1.88	2.23	2.02	14 bps	-21 bps
German 10y spot (%)	0.38	0.38	0.18	-20 bps	-20 bps
£ ERI	88.3	91.1	90.0	1.9 %	-1.2 %
FTSE All Share	3620	3727	3664	1.2 %	-1.7 %

Interest rates and monetary policy

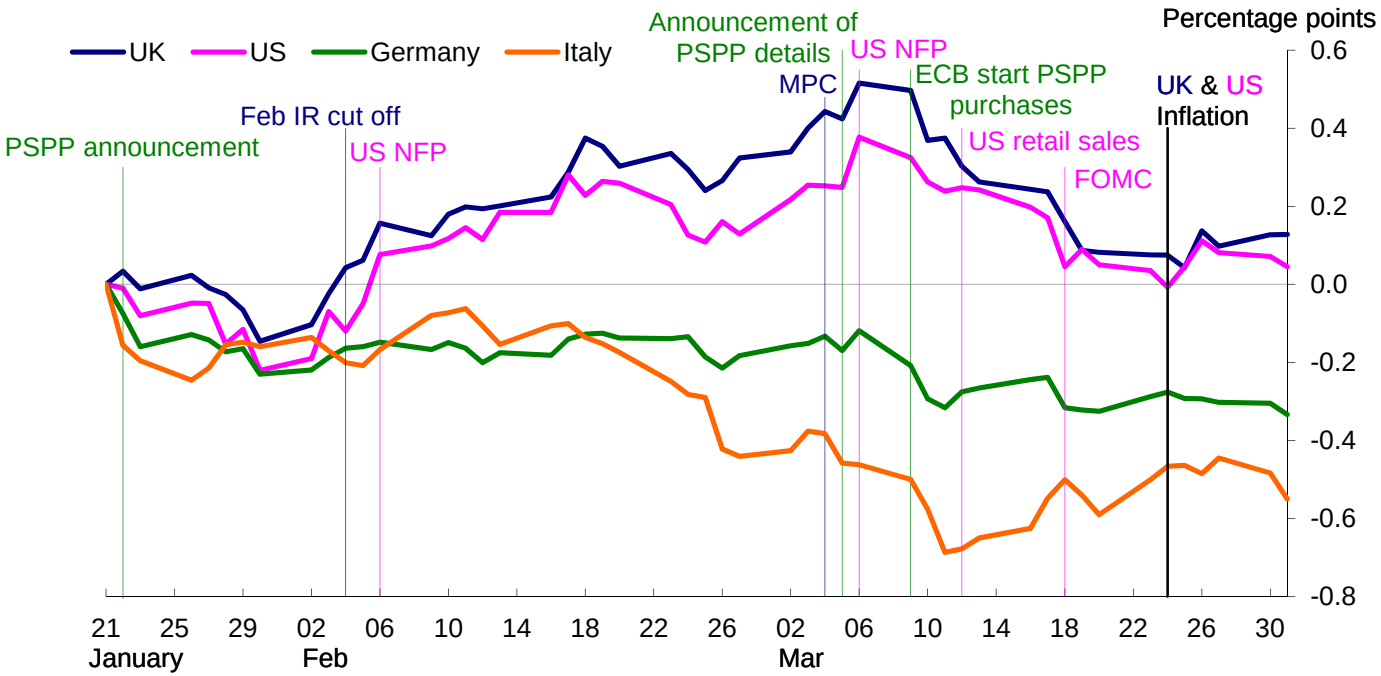
Euro area

10-year spot government bond yields



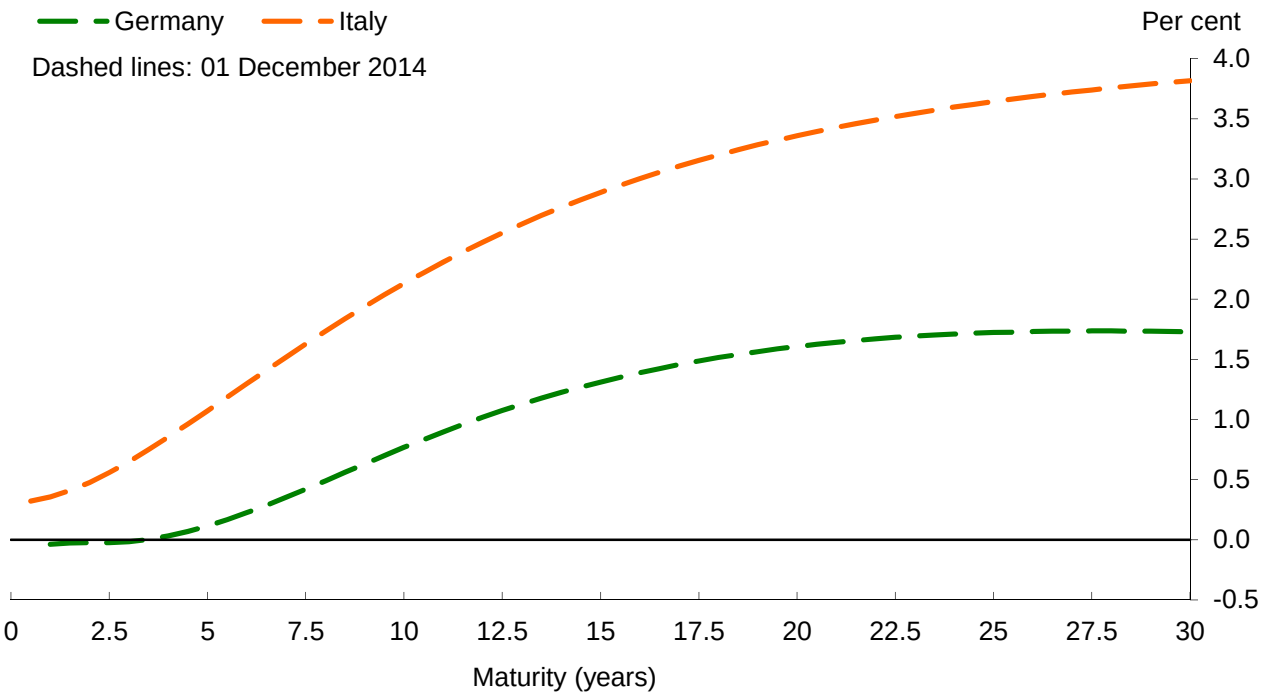
- 10-year yields have fallen since March MPC.

Change in 10-year spot yields since 21 January

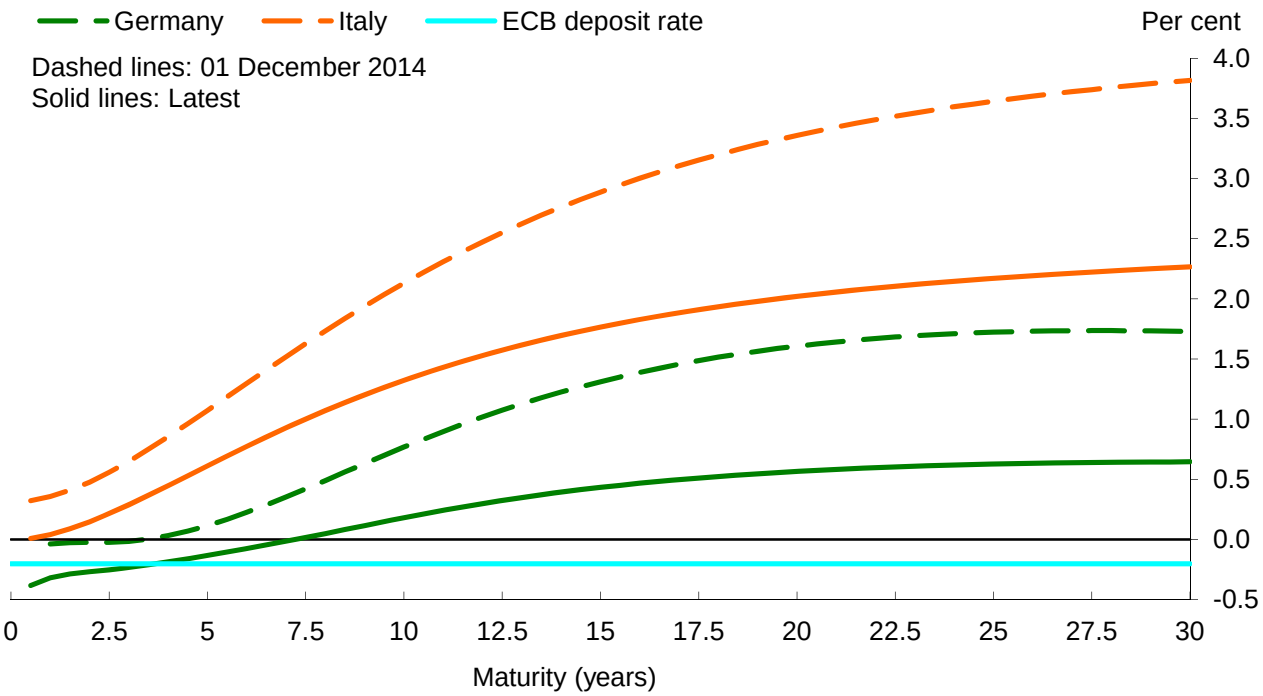


- German and Italian yields fell following the ECB's PSPP announcement on 22 January, and again after the start of purchases on 9 March.
- MI: small reallocations out of euro area bonds and into Gilts and USTs. But more evidence of investors putting maturing funds or new inflows into £ and $ assets rather than €s.

German and Italian spot yield curves

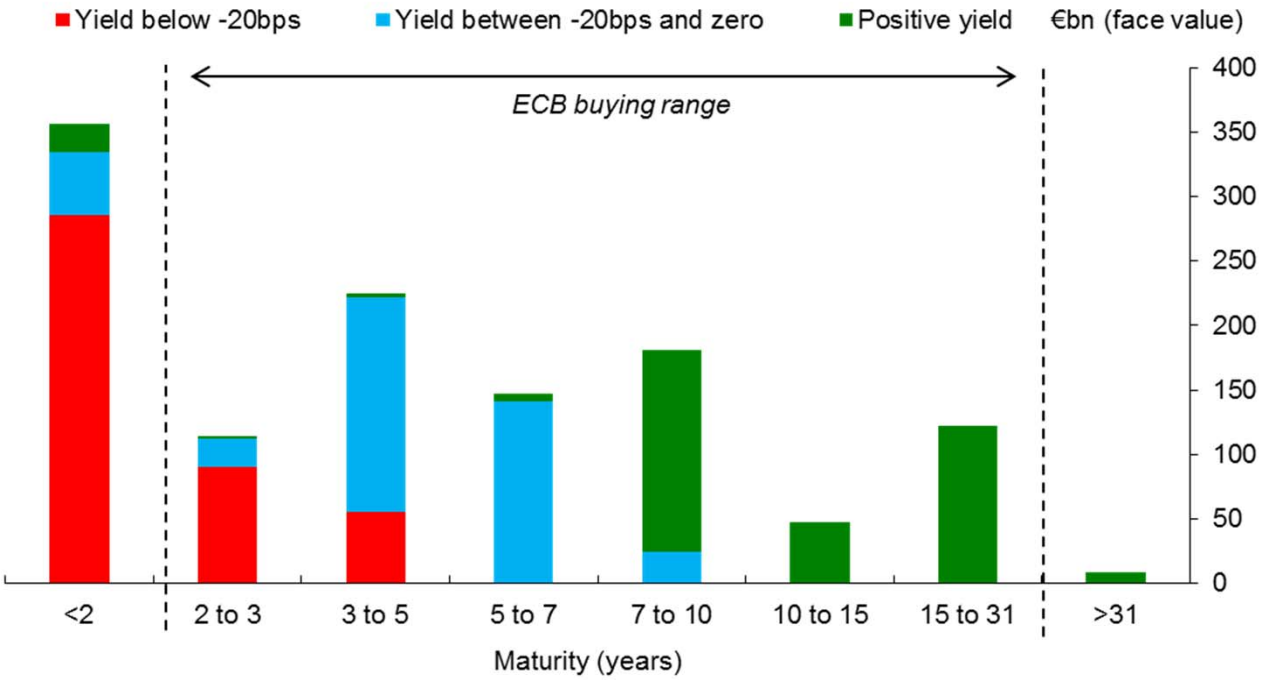


German and Italian spot yield curves



- German and Italian spot yield curves are lower and flatter than in early December.
- The German yield curve is now negative out to around 7 years, and is below the ECB's deposit rate out to nearly 4 years.

Amount of German government bonds by maturity (face value)



- ECB not buying bonds yielding below -20bps means that, as yields fall, more shorter maturity bonds are excluded, so longer maturity bonds need to be bought, lowering yields further.

European bond yields

Positive | Negative

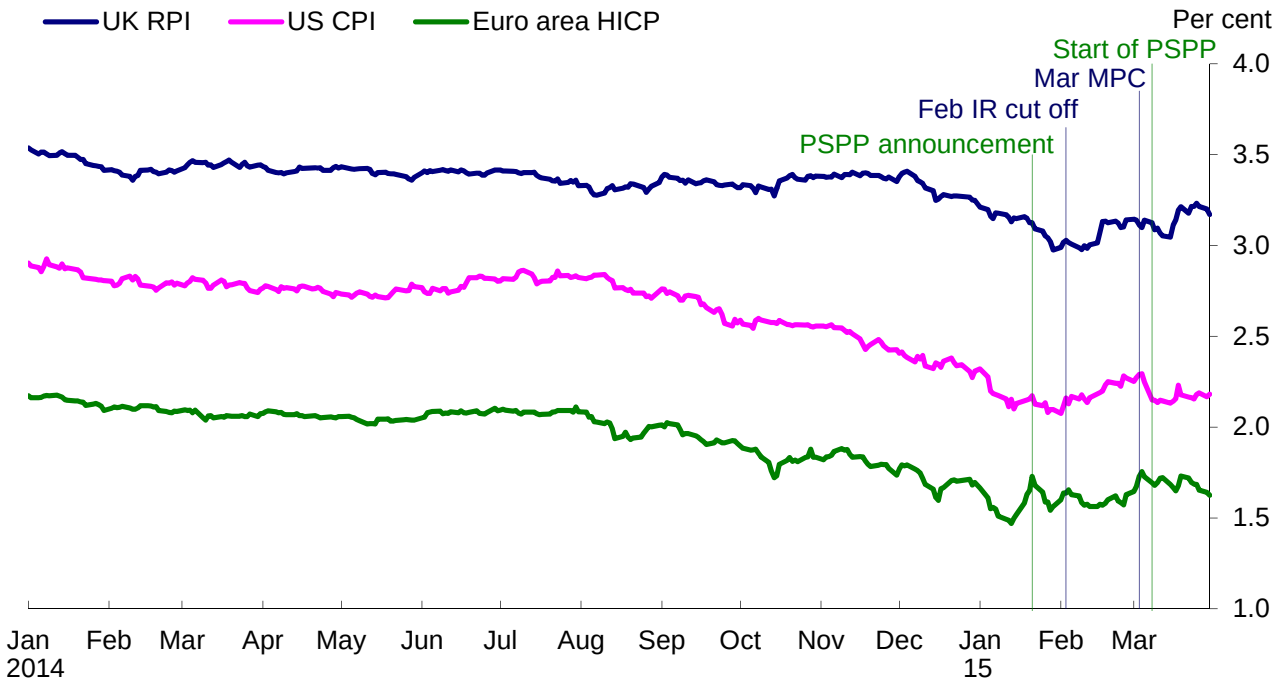
(%)	Policy Rates	Maturity (years) 1	2	3	4	5	6	7	8	9	10
Switzerland	-0.75*	-0.89	-0.86	-0.80	-0.60	-0.40	-0.30	-0.24	-0.20	-0.13	-0.07
Germany	0.05	-0.32	-0.27	-0.23	-0.19	-0.13	-0.08	-0.01	0.05	0.12	0.18
Denmark	-0.75**	-0.70	-0.48			-0.26	-0.01		0.13		0.26
Finland	0.05	-0.22	-0.22	-0.13	-0.07	-0.02	0.00	0.03	0.15	0.18	0.25
Netherlands	0.05		-0.20	-0.15	-0.11	-0.05	0.04	0.12	0.20	0.26	0.34
Austria	0.05	-0.17	-0.18	-0.16	-0.09	-0.02	0.01	0.07	0.17	0.24	0.32
Sweden	-0.25	-0.29	-0.32		-0.16	0.03		0.19	0.31		0.41
France	0.05	-0.19	-0.18	-0.13	-0.06	0.03	0.12	0.21	0.30	0.39	0.47
Belgium	0.05	-0.18	-0.17	-0.11	-0.03	0.01	0.08	0.19	0.27	0.35	0.44
Spain	0.05	0.01	0.04	0.19	0.33	0.53	0.74	0.85	0.99	1.14	1.21
Italy	0.05	0.04	0.15	0.29	0.45	0.61	0.77	0.93	1.07	1.20	1.32
Norway	1.25	0.83	0.83		0.99		1.21		1.36	1.39	1.46
UK	0.50	0.30	0.43	0.67	0.89	1.09	1.24	1.37	1.48	1.58	1.66

*centre of target range **deposit rate

Bloomberg and Bank calculations

- Low yields have encouraged some EA sovereigns to increase the maturity of their issuance.
- There has been strong issuance of €-denominated investment grade corporate bonds, including an unusually large proportion from non-EA issuers.

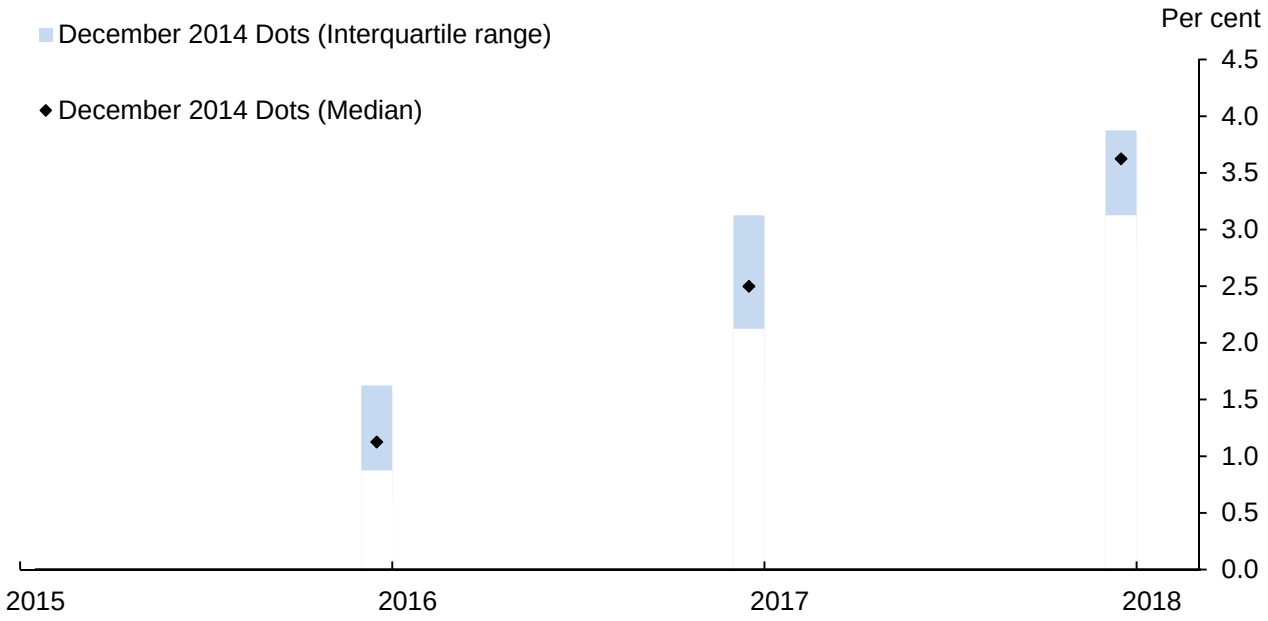
5-year, 5 years forward inflation swap rates



- 5-year, 5 years forward inflation swaps have fallen in the euro area and US since March MPC, but have risen slightly in the UK.

US

FOMC Summary of Economic Projections: path of Fed Funds Rate



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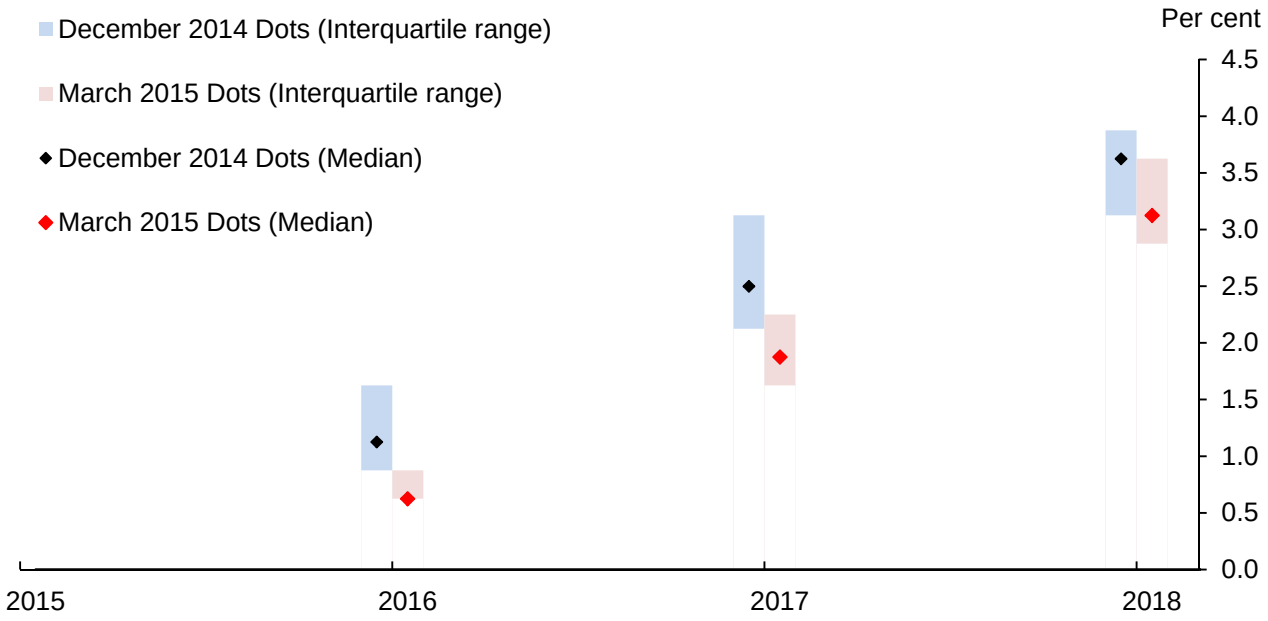
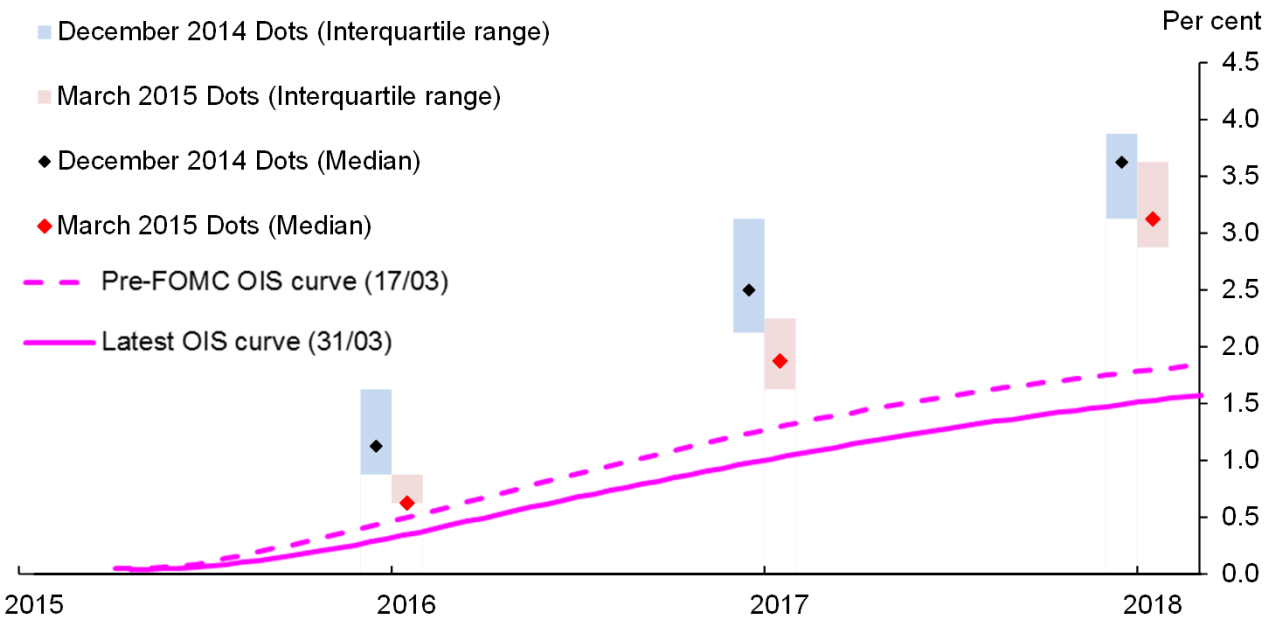


- Path of the Fed Funds Rate was shifted down at the March FOMC meeting.

FOMC Summary of Economic Projections: path of Fed Funds Rate, and US OIS forward curves

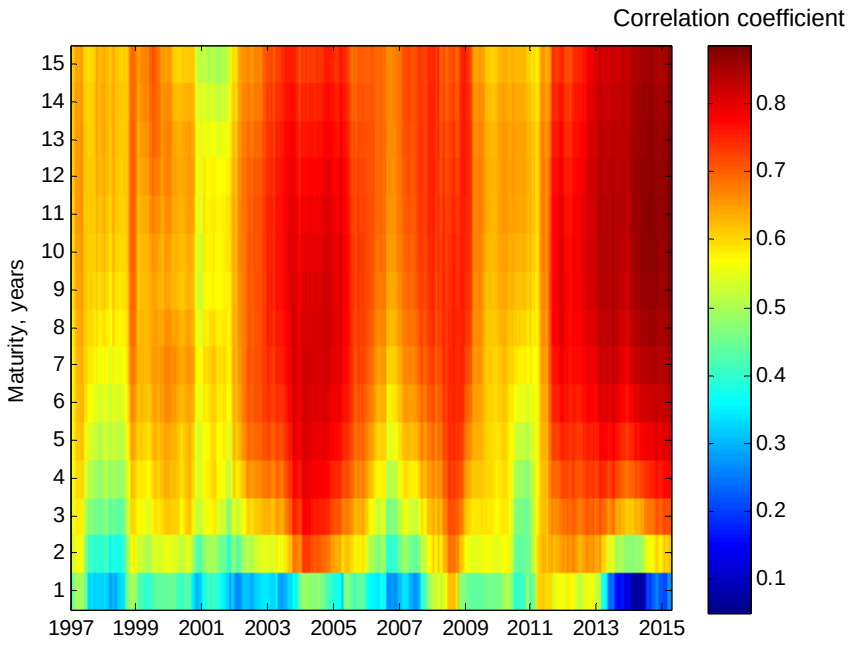


- Although the market-implied timing of lift-off (Q4) is broadly in line with the FOMC dots, the market-implied pace is much slower than the dots imply.

FOMC Chair Yellen (27 March 2015)

- “It is sobering to note that many market participants appear to assess the risks to the outlook quite differently… the generally low level of yields in advanced economies suggests that investors place considerable odds on adverse scenarios that would necessitate a lower and flatter trajectory of the federal funds than envisioned in participants’ modal SEP projections.”

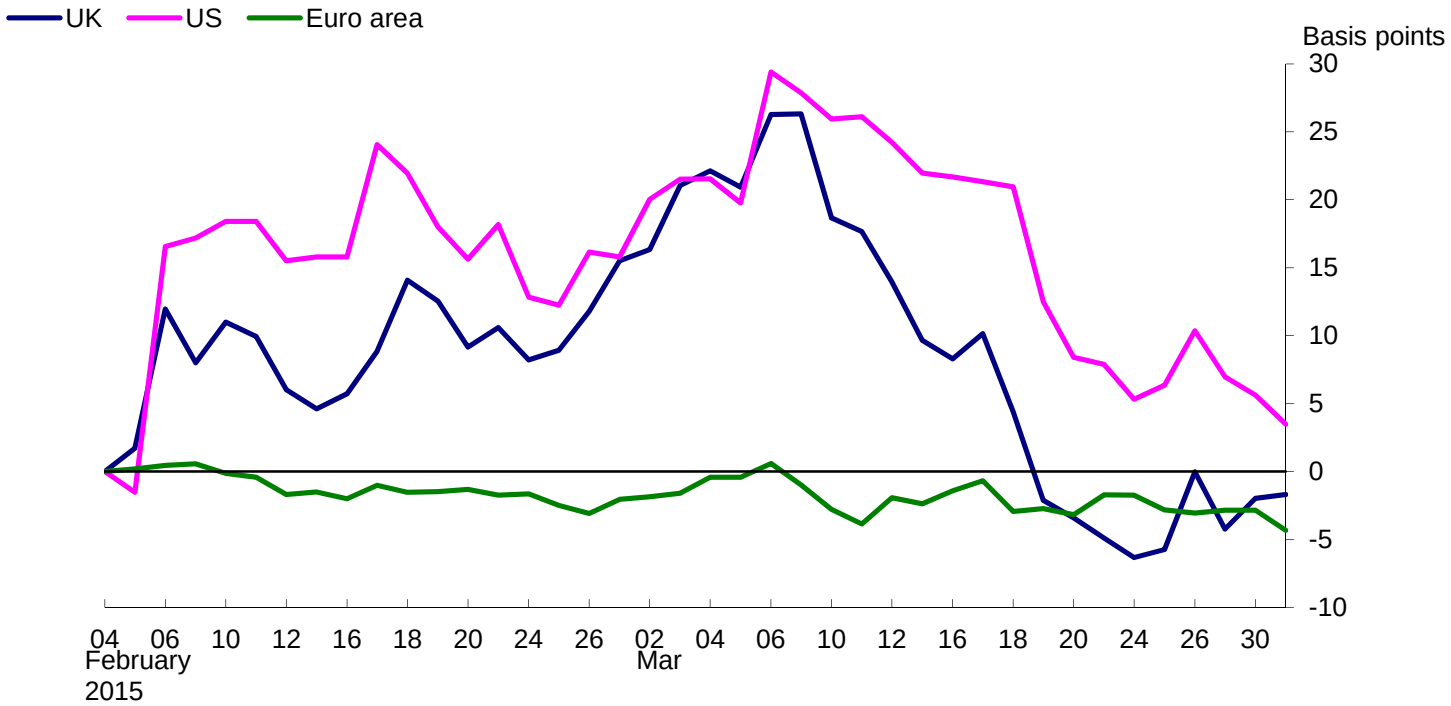
Correlation of changes in UK and US spot yields (2 year rolling correlation of weekly changes)



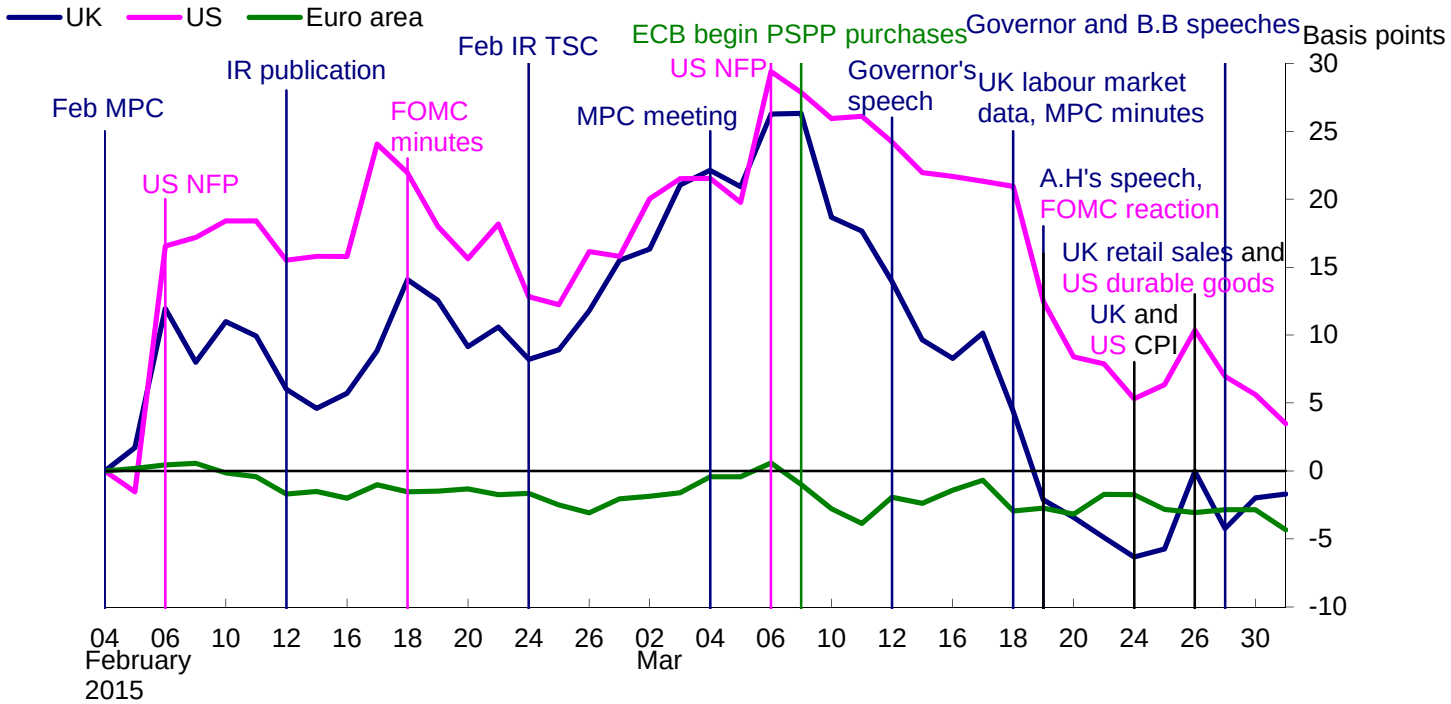
- MFAD Research Awayday: ,
  (23 April), forecast round and GSID special topics meeting in May.

UK

Cumulative change in UK, US and euro area 3-year spot OIS rates since February MPC

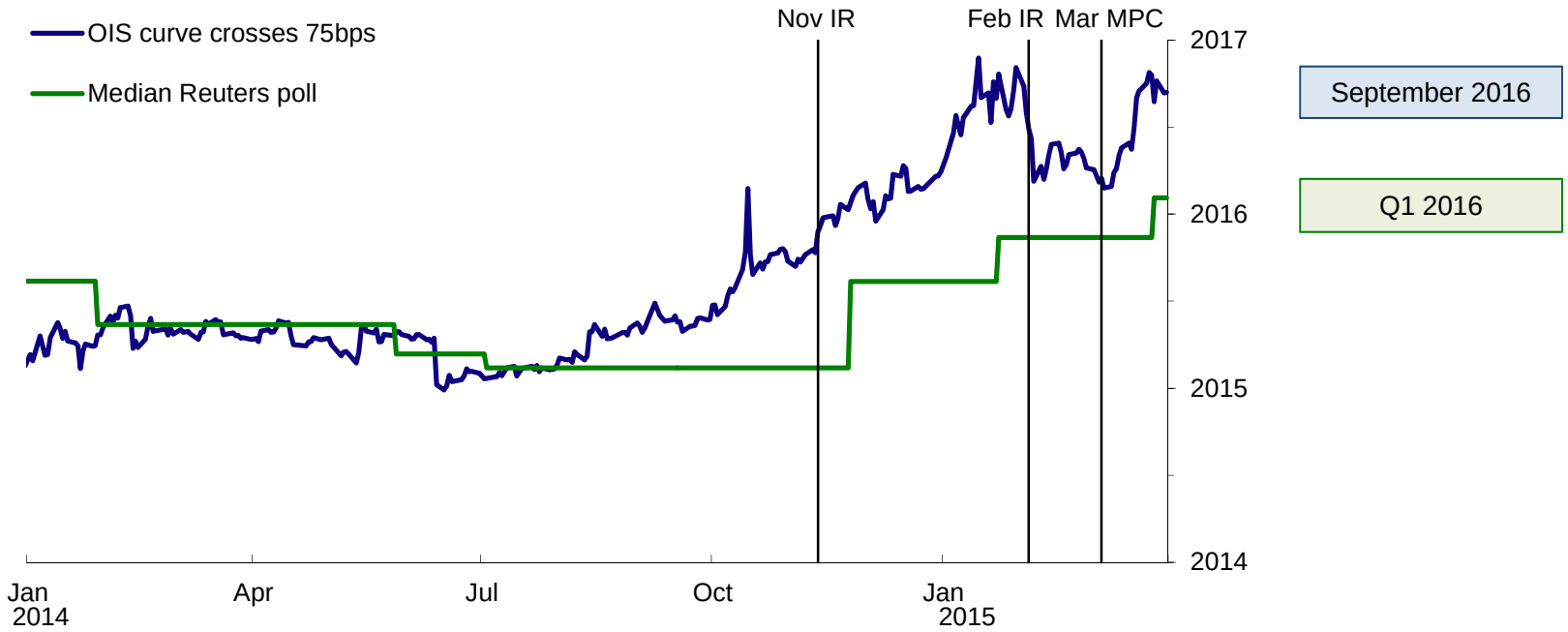


Cumulative change in UK, US and euro area 3-year spot OIS rates since February MPC



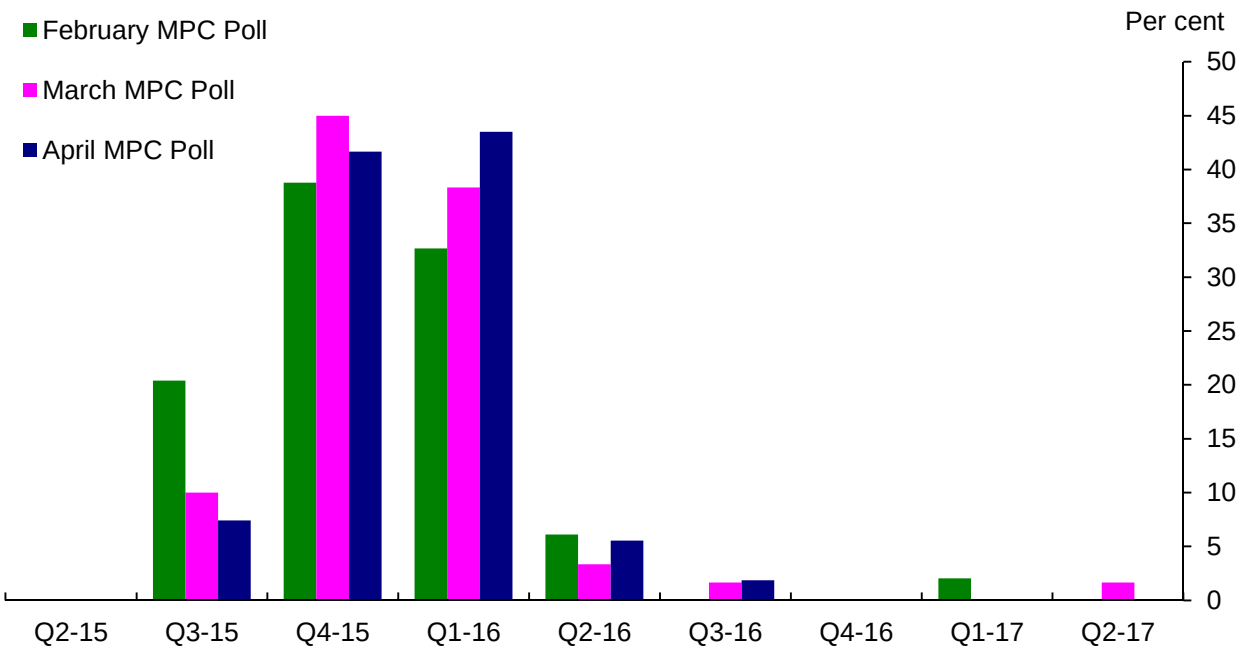
- UK short rates have fallen on the month, reflecting a combination of policy and data news from the US and euro area, as well as the UK (Minutes and labour market data).

Economists' expectations for timing of first rate rise and date at which OIS rates reach 0.75%



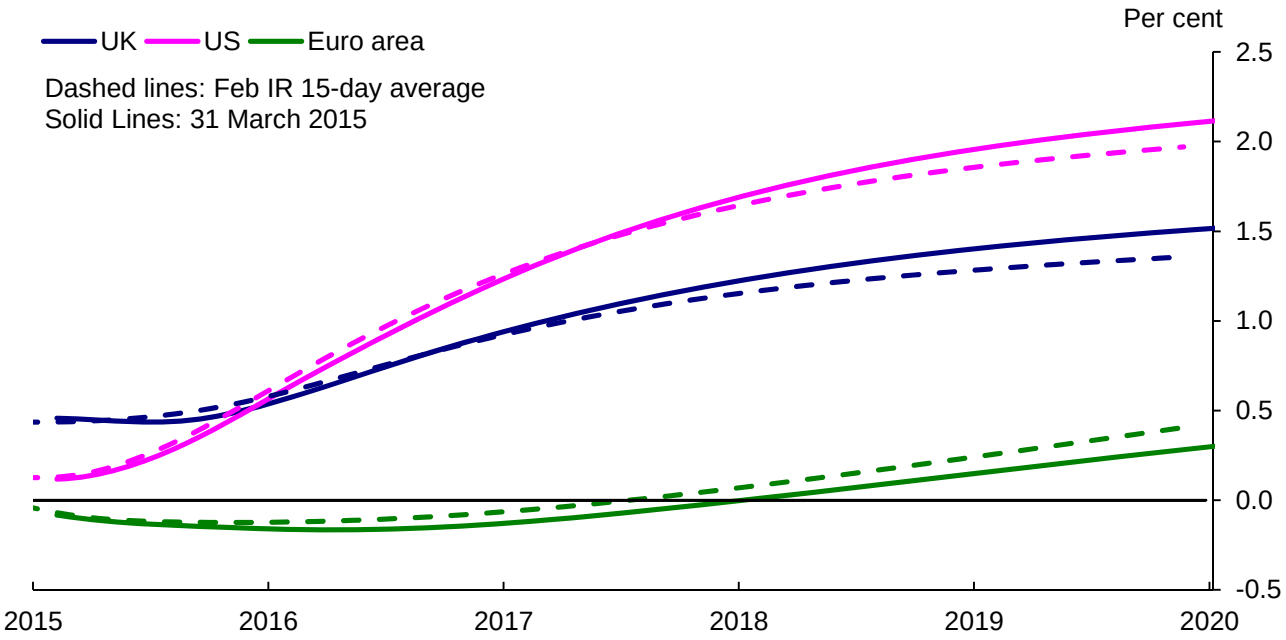
- The OIS forward curve now crosses 0.75% in September 2016, five months later than at March MPC.
-

Reuters survey: expected timing of first increase in Bank Rate



- The distribution of expectations is little changed from last month, with most respondents expecting a rate rise in either Q4 2015 or Q1 2016.
- None of the respondents expect the next MPC policy move to be a Bank Rate cut.

International forward OIS curves



- The UK OIS forward curve is little different to the February IR 15-day average.

Summary

- ECB PSPP purchases led to further fall in yields; -20bp constraint may be contributing to flattening of yield curve; low and negative yields persist in euro area, encouraging corporate issuance.
- FOMC lowered its ‘dots’ but they remain above US curve; bigger gap not timing of liftoff but subsequent pace.
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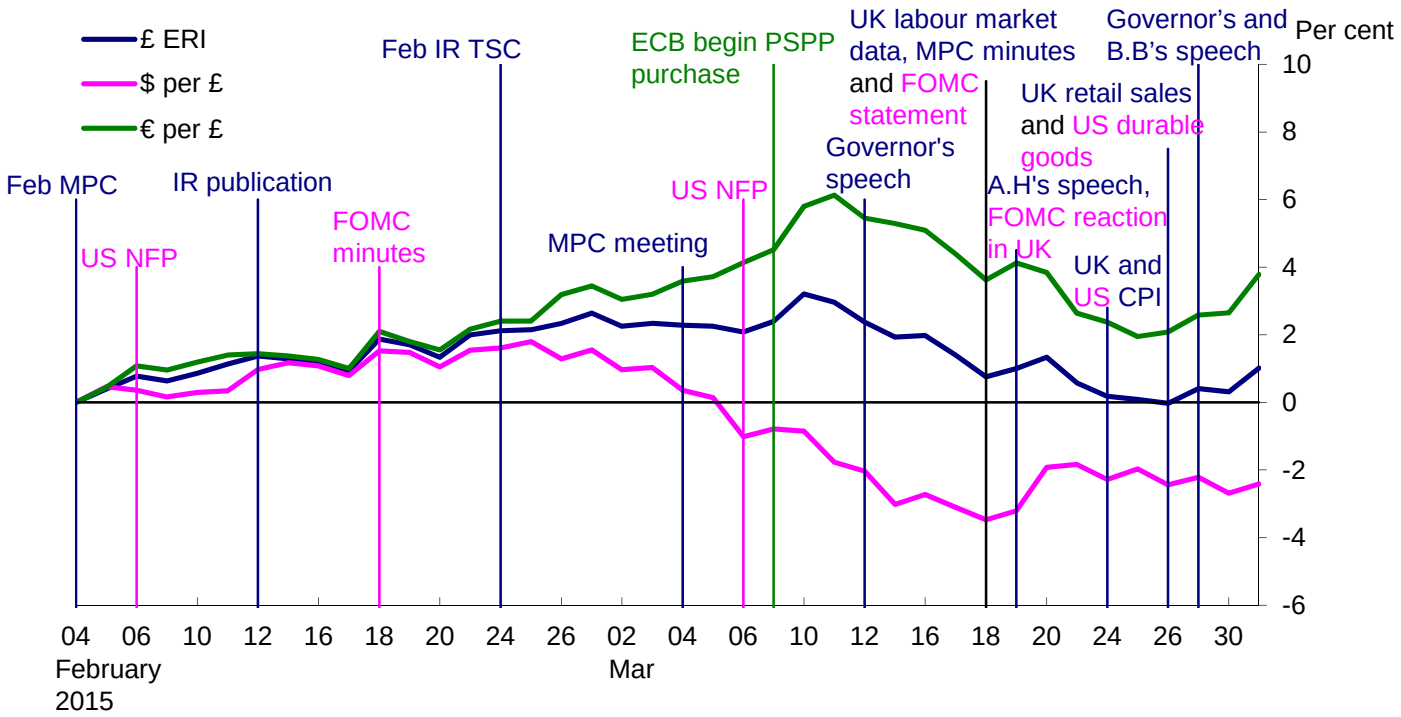
Sterling

Cumulative change in sterling ERI and bilateral exchange rates since February MPC



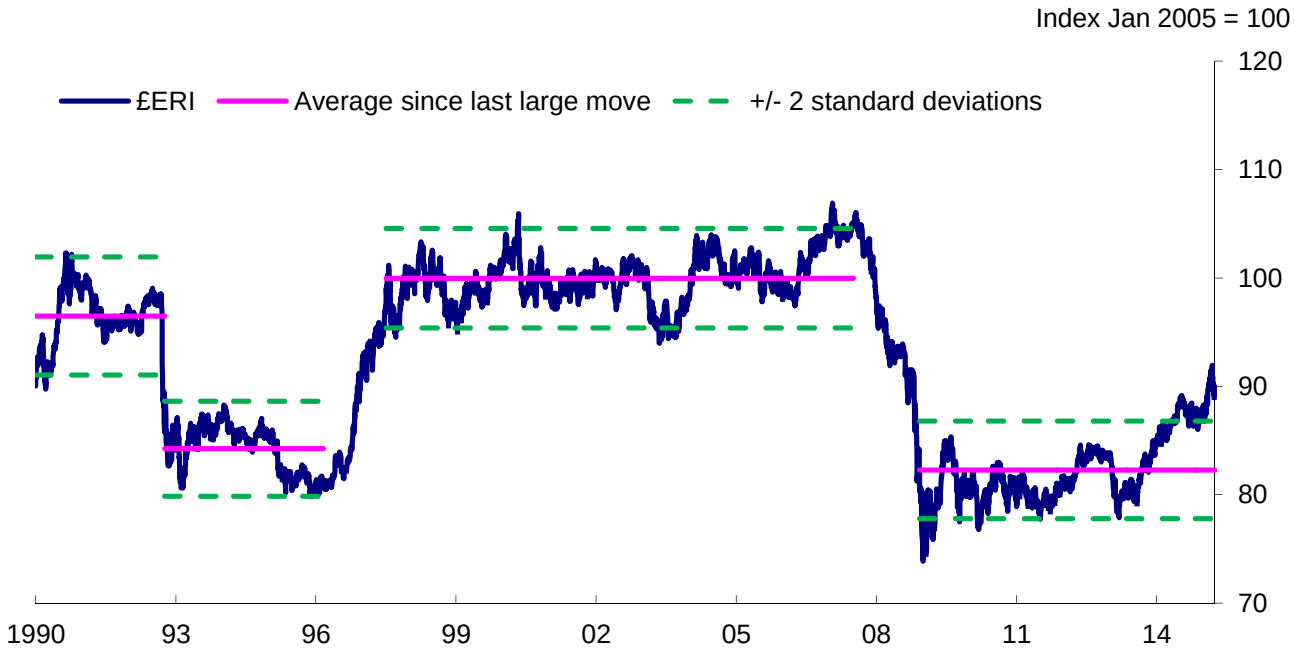
- Sterling is down 1% since March MPC, and up 2% from the February IR 15-day average.

MPC Minutes word clouds (from State Street Global Markets)

February 2015

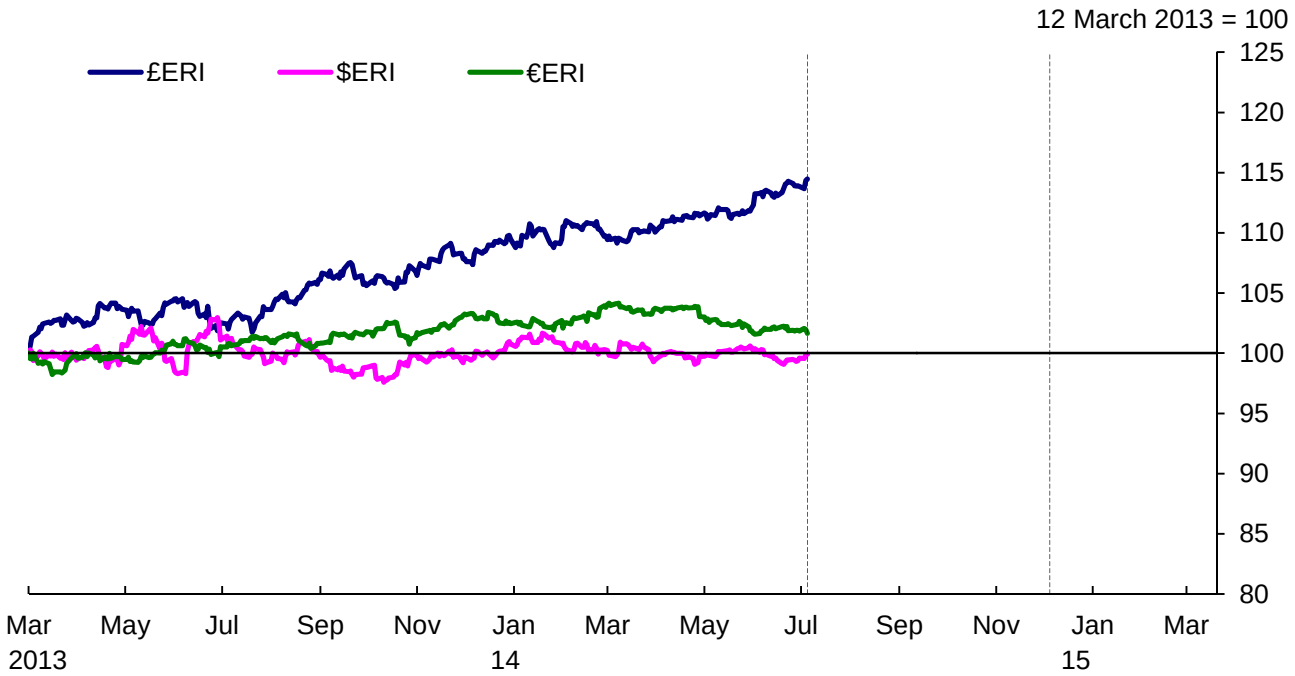
March 2015

Sterling ERI, from January 1990



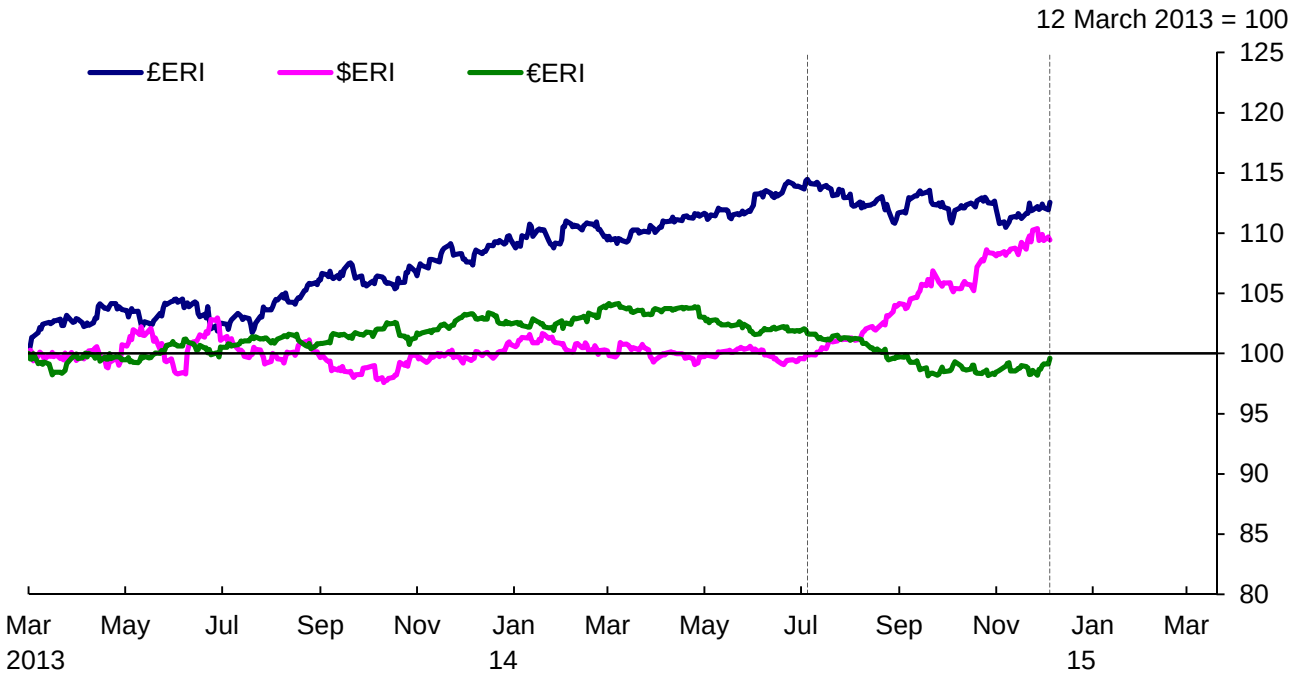
- Sterling is 16% higher than its trough in March 2013.

Phases of sterling since 2013 trough



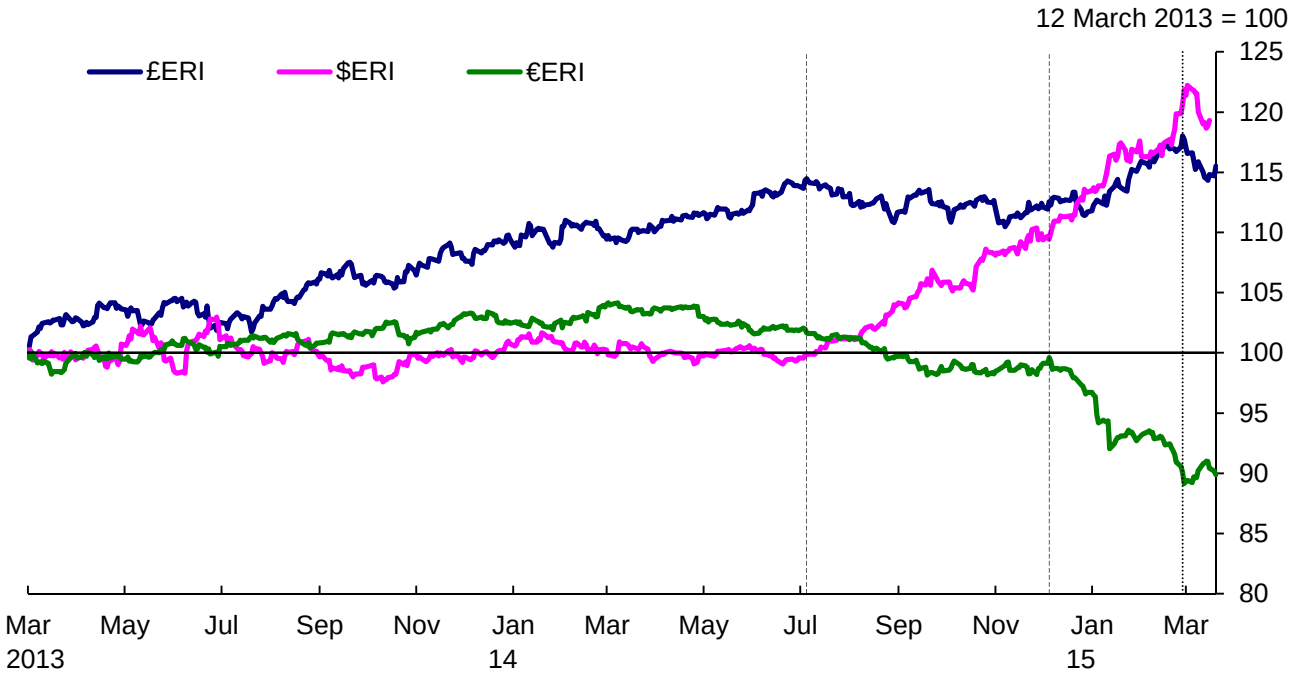
- March 2013 to July 2014: UK-specific factors behind sterling appreciation, as UK outlook improved relative to our major trading partners.

Phases of sterling since 2013 trough



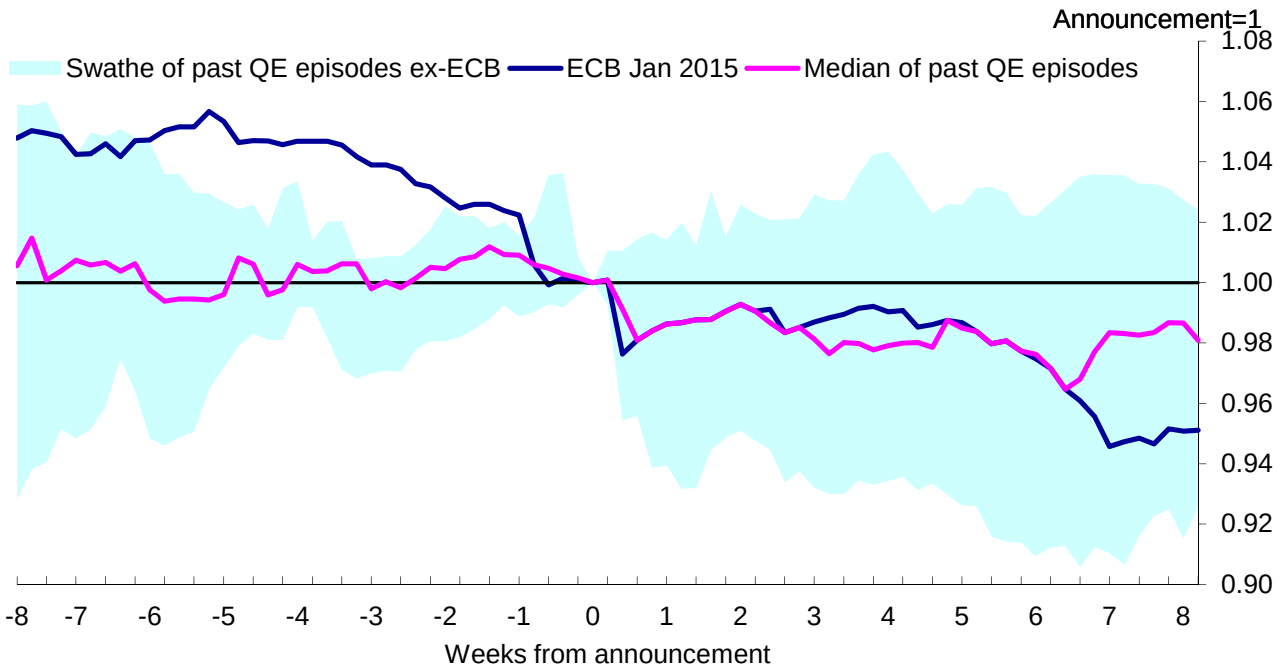
- July 2014 to December 2014: sterling remained relatively stable, as the dollar appreciated significantly and the euro fell slightly.

Phases of sterling since 2013 trough



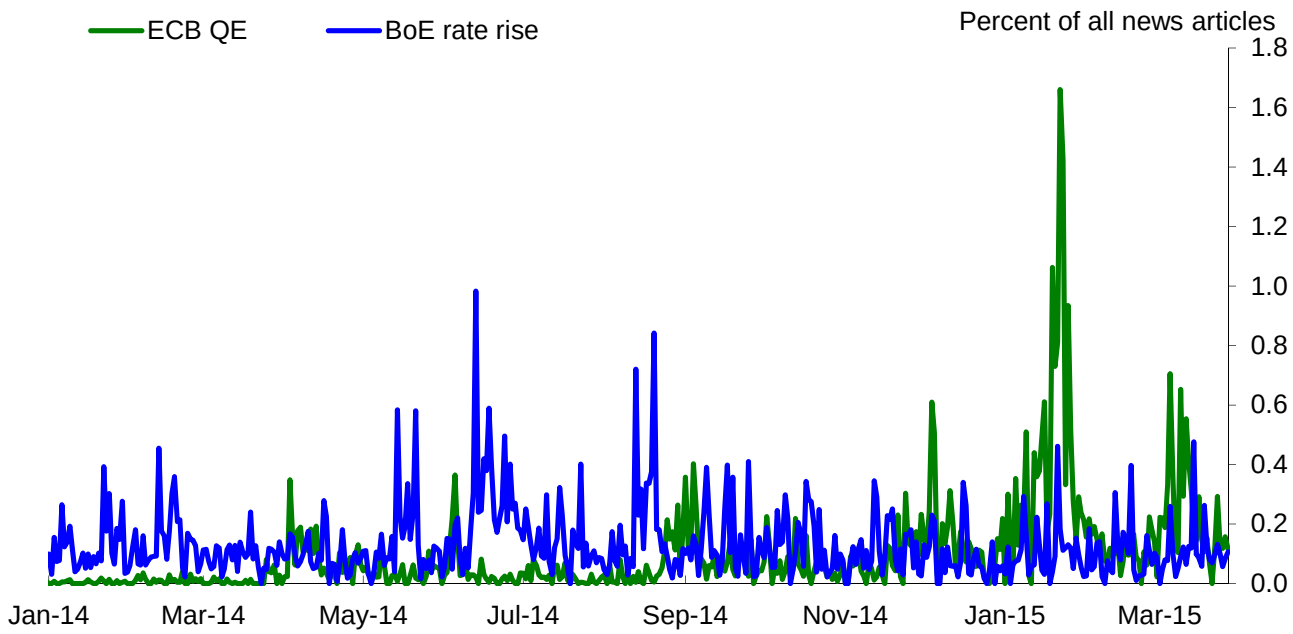
- From December 2014: the dollar continued to appreciate, but sterling rose in effective terms because the euro fell sharply. Now entering a new phase?

Changes in ERIs around US, UK, Japanese and euro area QE announcements since 2008



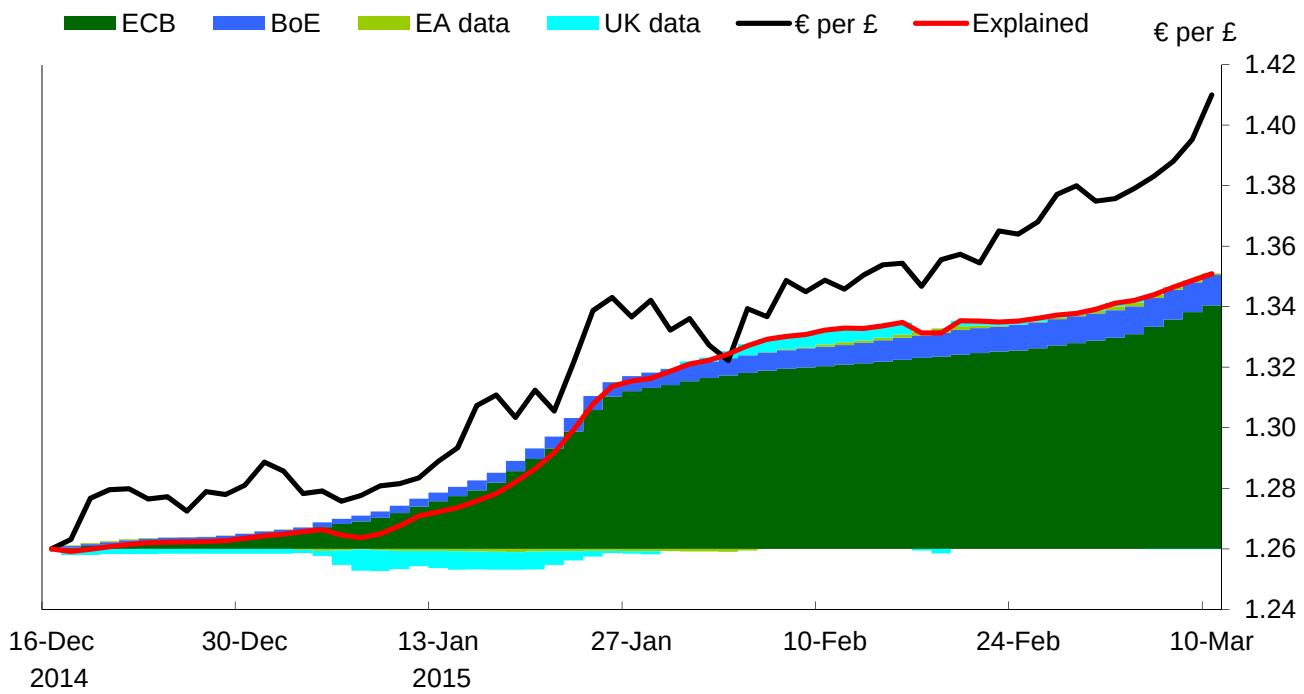
- There was a large anticipation effect ahead of the ECB's January announcement, and a depreciation of the euro over a 2-day window on the announcement. The euro fell further just before and after the ECB started its purchases in March.
-

Share of Bloomberg articles that contain ECB and BoE monetary policy terms



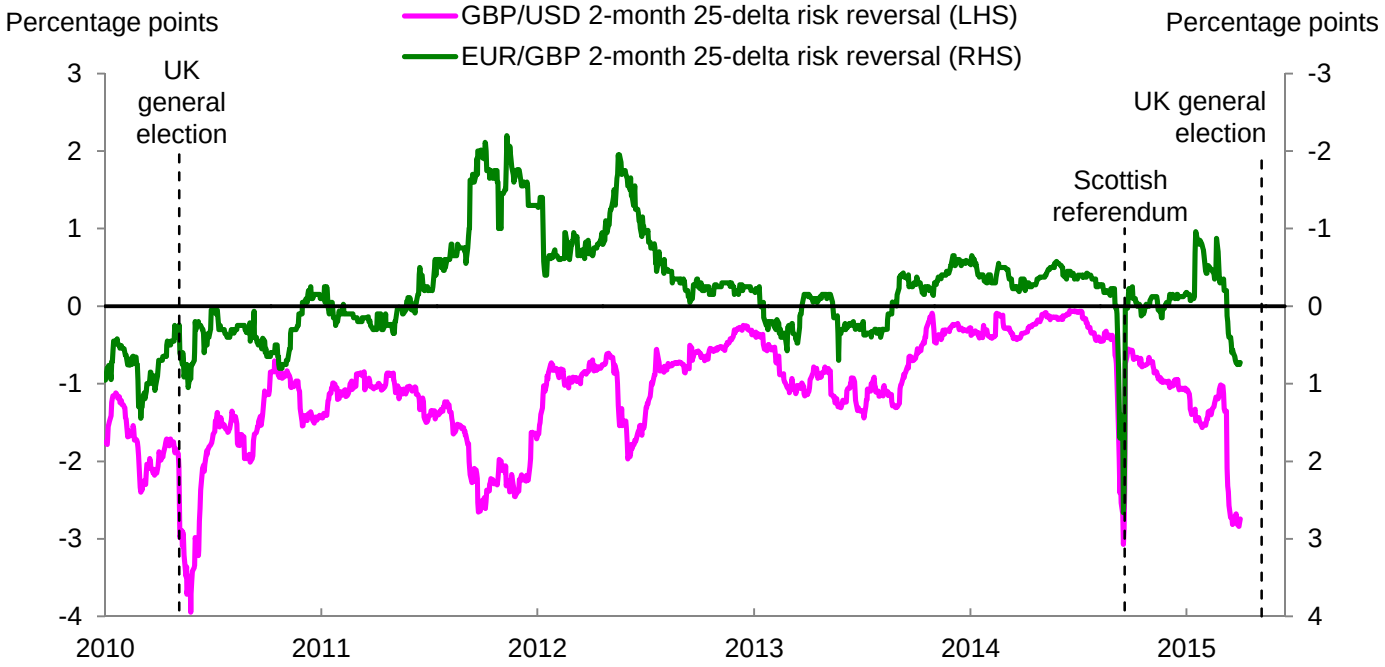
- This approach uses Bloomberg news articles that contain ECB QE as a proxy for market attention on a particular day, and similar searches for news about MPC rate increases.
- And in the regression we also use economic surprise indices for both economies.

Cumulative contributions of policy news and data surprises to sterling's exchange rate against the euro



- This approach suggests the rise in sterling against the euro between December and the recent peak in the £ERI largely reflects news about euro area policy.

2-month, 25-delta 'risk reversal' in sterling against the dollar and euro



- FX option markets pricing in some downside risk to sterling, broadly similar magnitude to the 2010 General Election and the Scottish Referendum, but much earlier.
-

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- UK short rates fell on the month but are little changed since Feb IR 15-day average; forward curve crosses 0.75% in September 2016.
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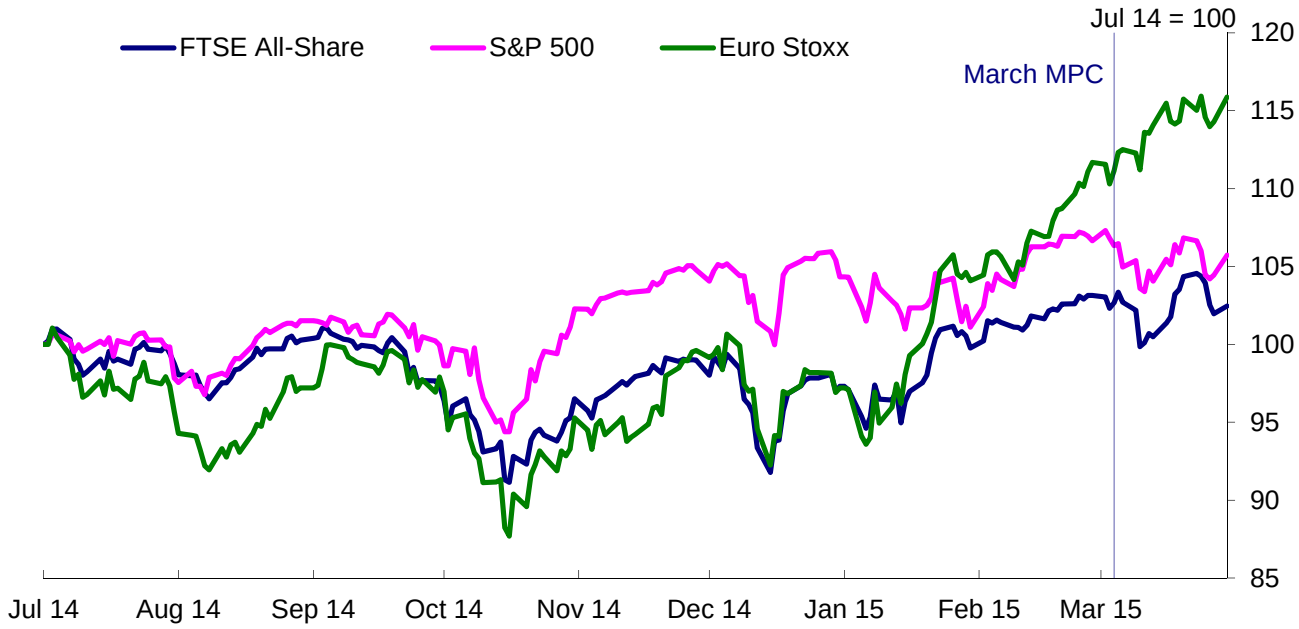
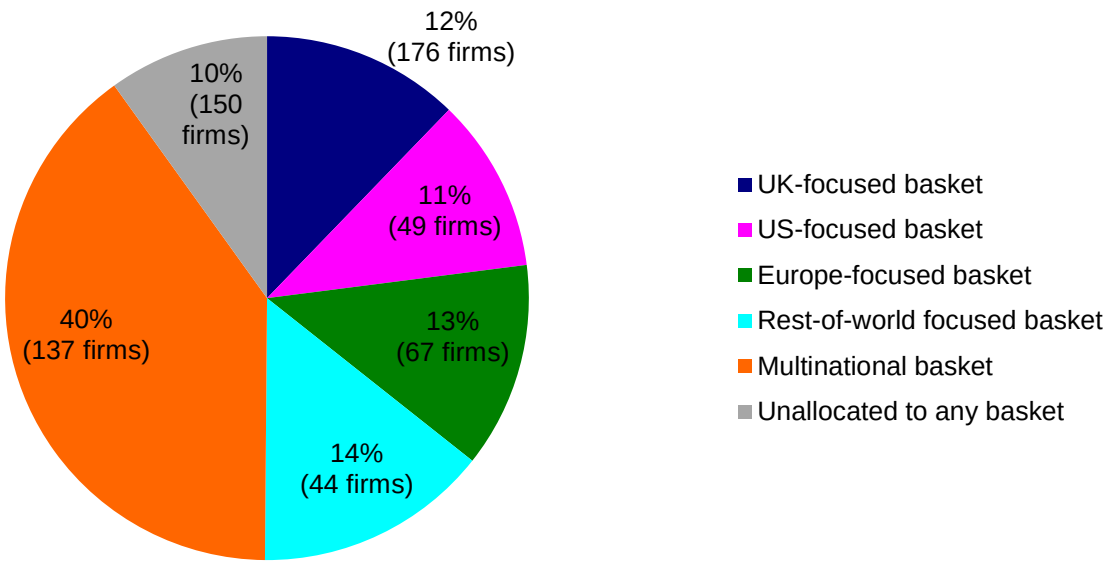
What are equity markets telling us about the growth outlook?

Equity indices since July 2014, local currency



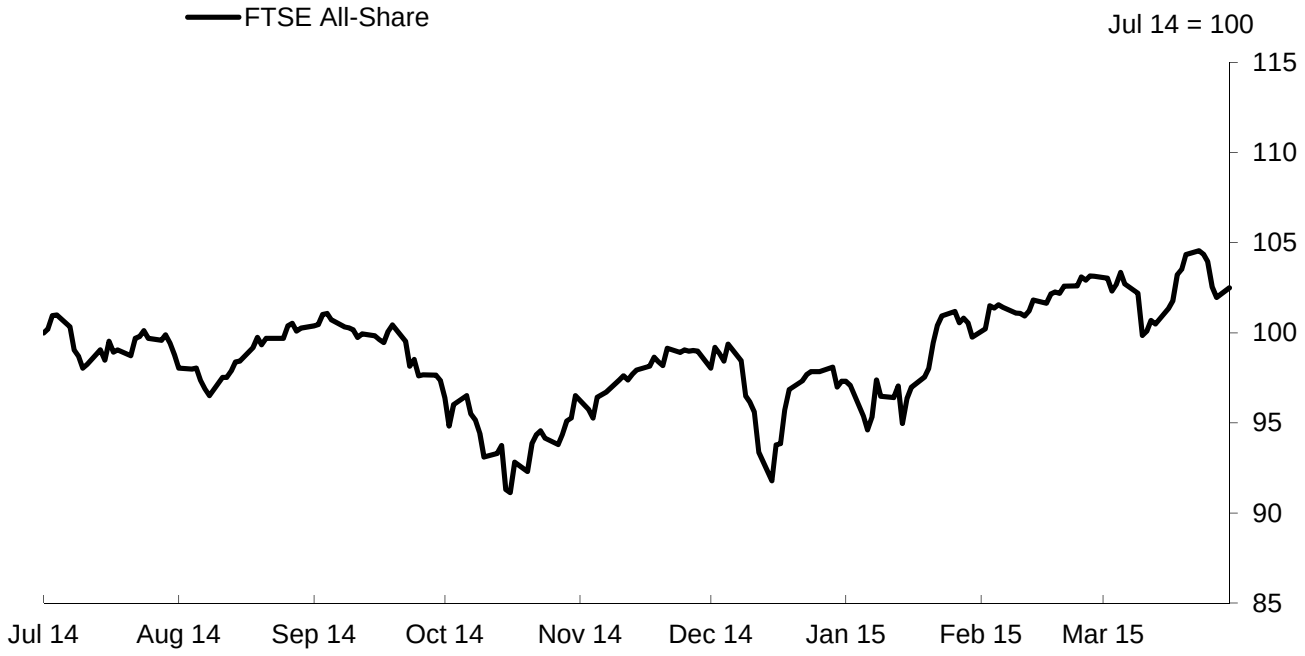
- Eurostoxx up 18% since start of year. EPFR data: net inflows to Western Europe were +$41bn in the year to 18 March compared to +$13bn in 2014.
- FTSE is up 4% since start of year.

FTSE market capitalisation, split into geographic baskets by primary revenue source

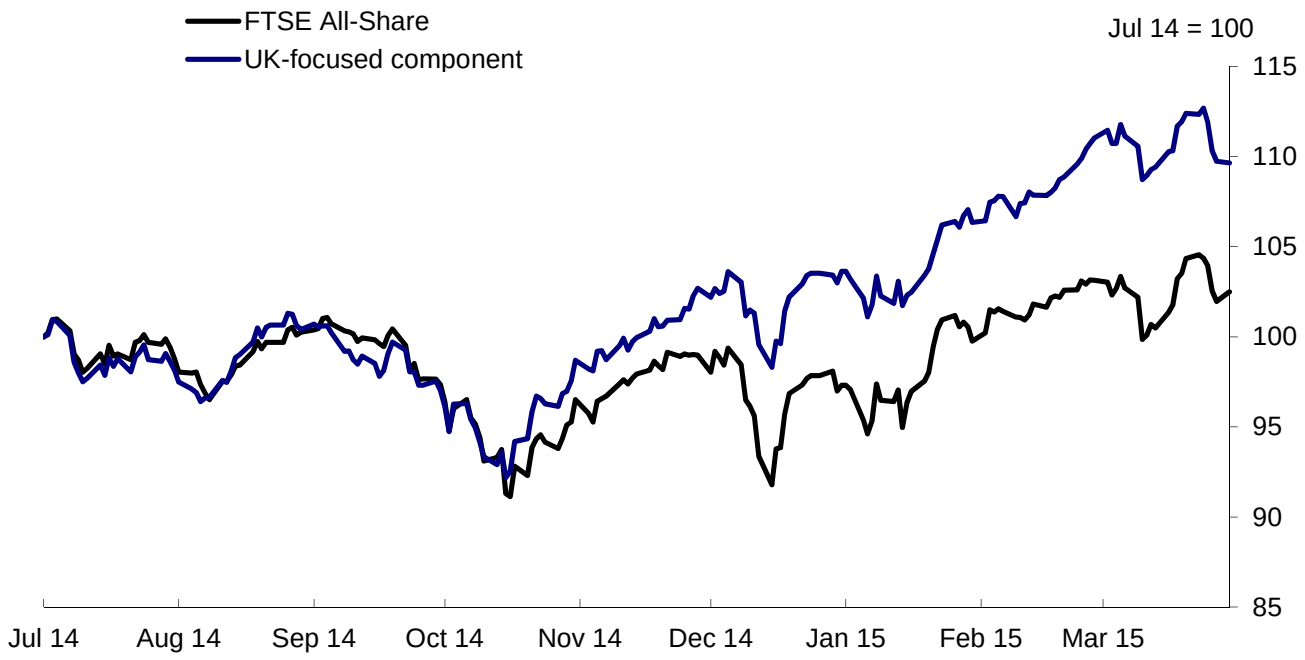


- Using company accounts data, we have decomposed the FTSE All-Share into baskets based on each listed company's primary geographic revenue source.

FTSE All-Share

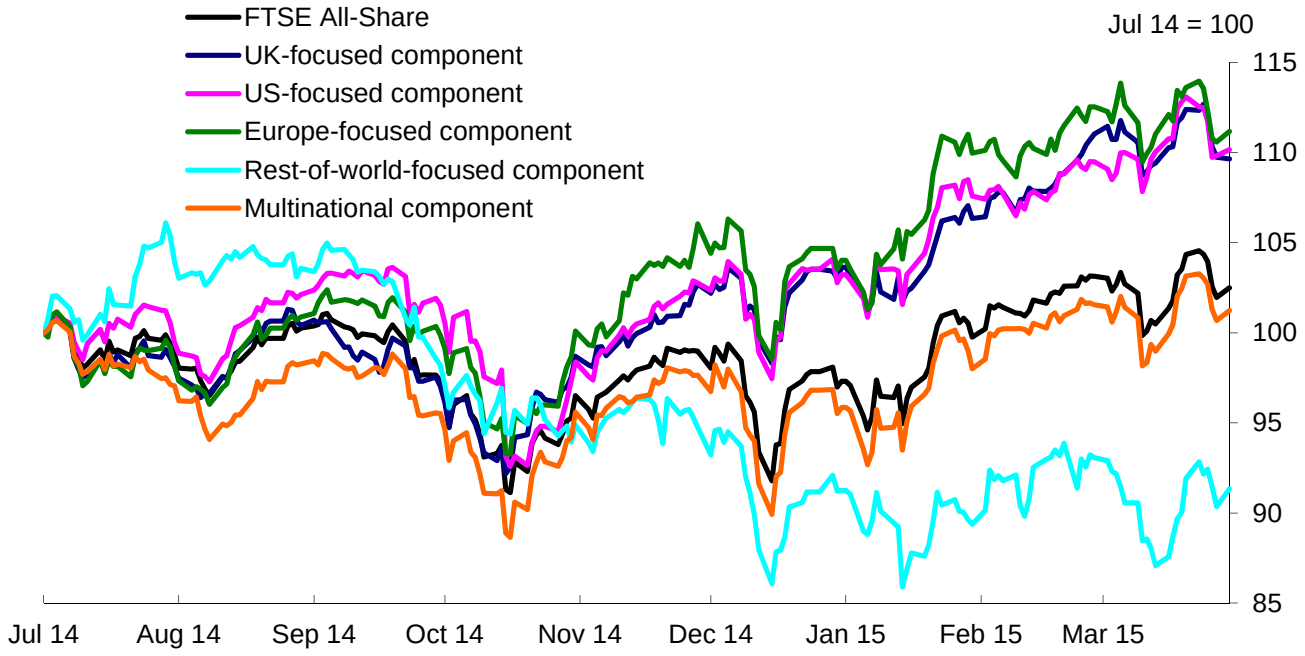


FTSE All-Share and UK-focused component



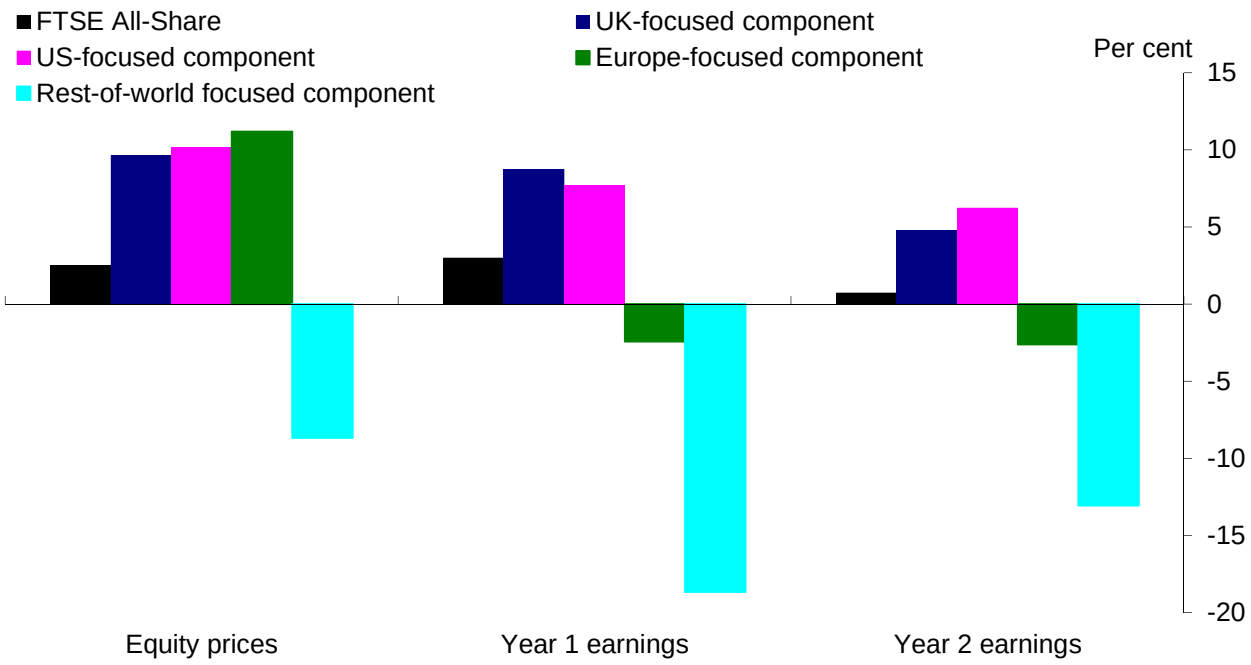
- The price index for the basket of UK-focused FTSE companies has outperformed the wider index.

Geographically-focused components of the FTSE



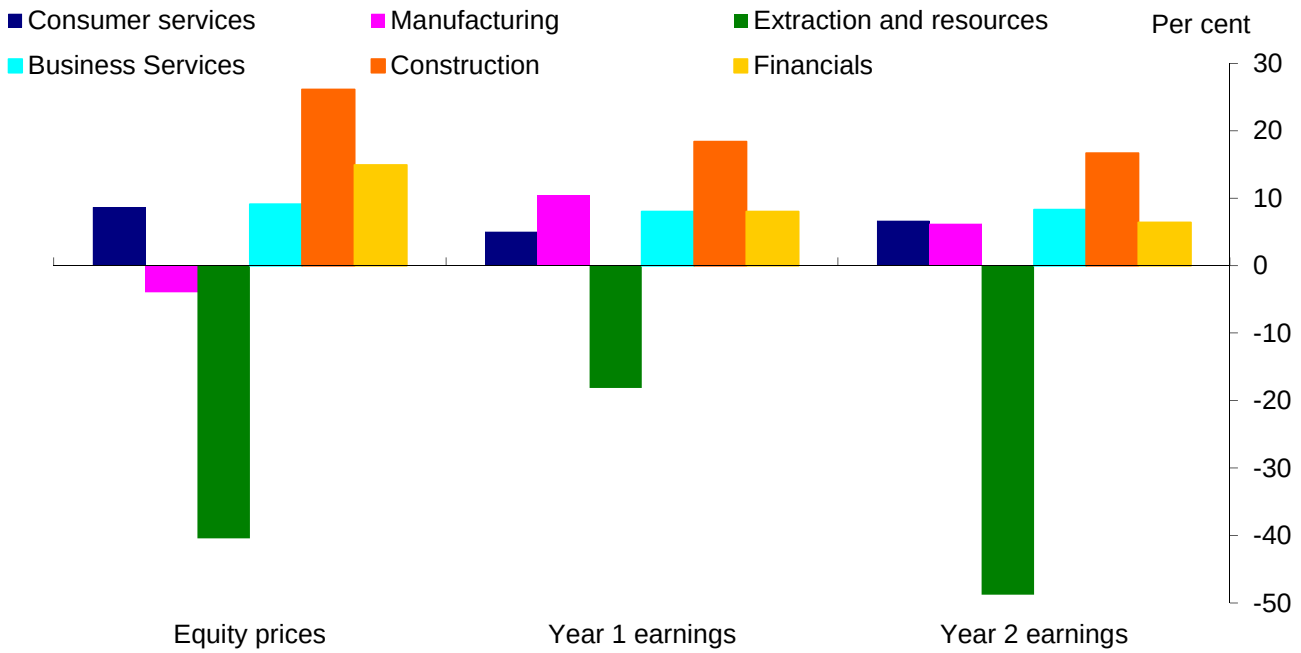
- US and Europe-focused components of the FTSE have also strengthened.
- But the FTSE has been dragged down by weakness in the equity prices of companies generating their revenues elsewhere in the world.

Change in geographically focused components of the FTSE since July 2014



- We also have a new, rich dataset of equity analysts' company-level earnings forecasts.
- Earnings forecasts for FTSE companies on average have been revised up a little since July, but earnings forecasts for UK-exposed companies have been revised up more.

Change in ONS sector components of UK-exposed firms in the FTSE since July 2014



- The strength of UK-focused companies is reasonably broad based across sectors, with the exception of the ‘extraction and resources’ sector, which contains oil and mining companies.
- Earnings revisions consistent with more oil-intensive sectors benefiting more from oil price fall.
- See ‘FMIF14: What are equity markets signaling about the economic outlook?’

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- Policy news from the euro area has been an important factor in sterling’s appreciation; £ERI has fallen since March MPC, but is 2% higher than in the Feb IR; General Election uncertainty seen as downside risk to £.
- UK-focused companies’ equity prices and earnings outlook are stronger than the FTSE-All Share; strength broadly based across ONS output sectors, except extraction.

MONEY, CREDIT AND NOMINAL TRENDS April 2015

Prepared by:
MA, SRDD, FSSR, Agents

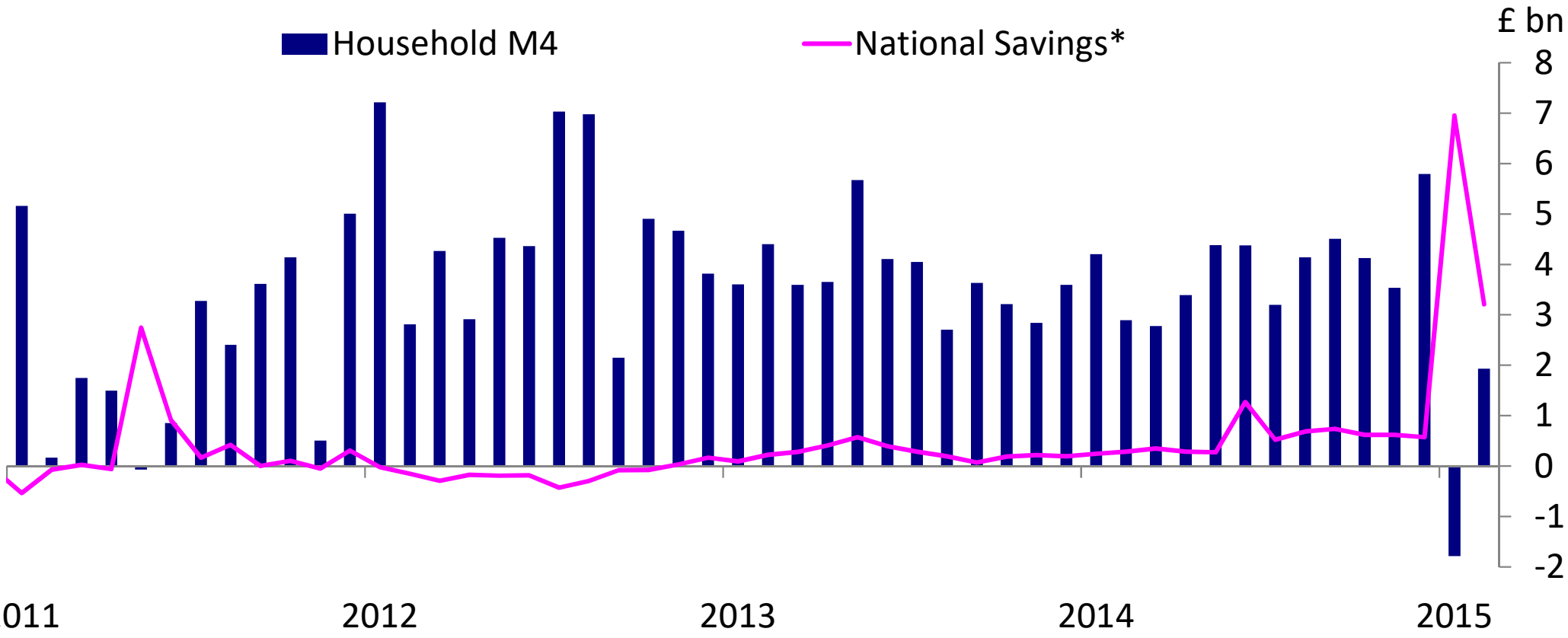
Agenda

- **Bank funding update**
- **Latest housing market forecasts**
- **Update on corporate credit conditions**
- **Inflation expectations stocktake**

See ‘Key points from 2015H1 meetings with the major lenders’,

Flows from M4 to pensioner bonds continue

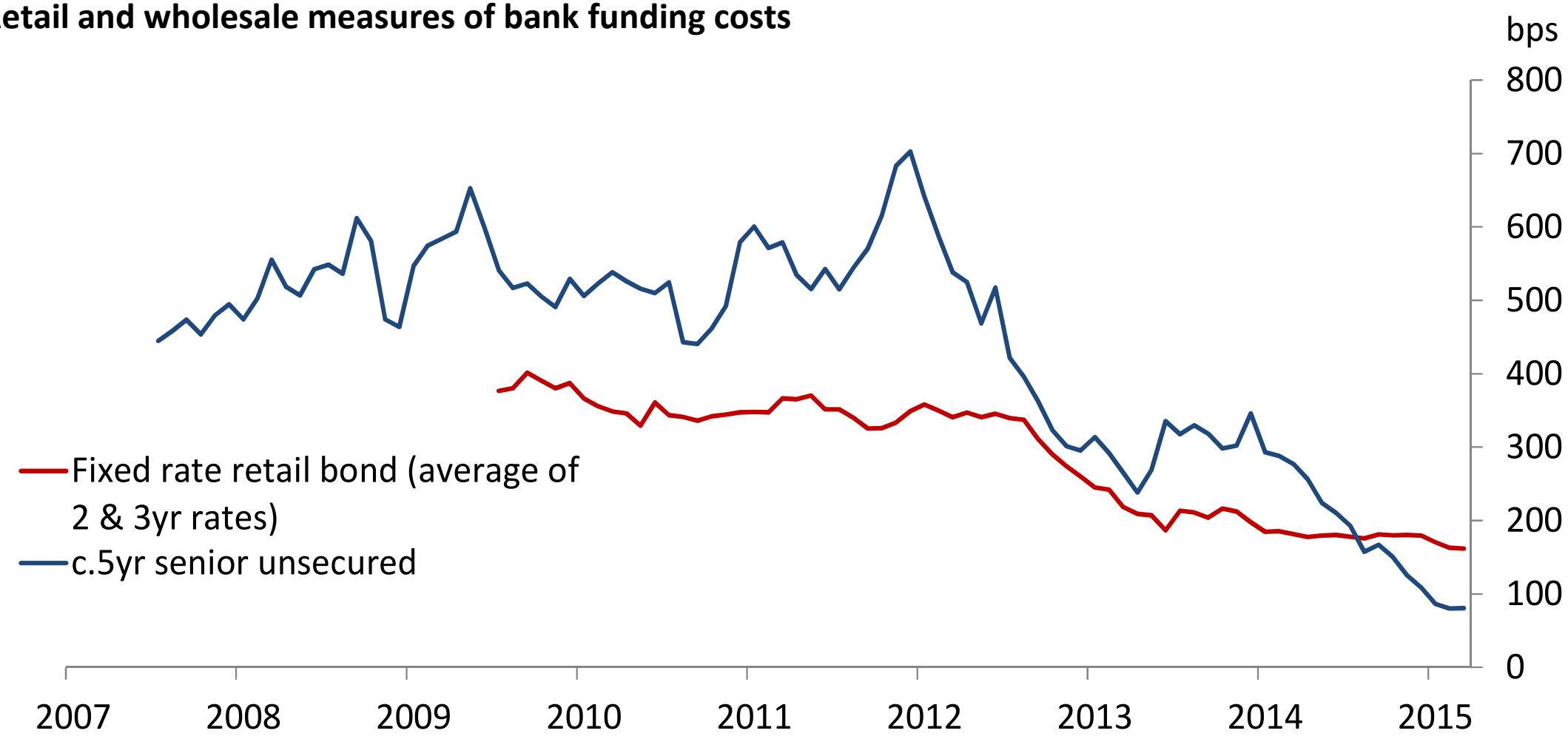
Flows into selected household liquid assets



*Internal estimates based on NS&I data, seasonally adjusted by Bank staff

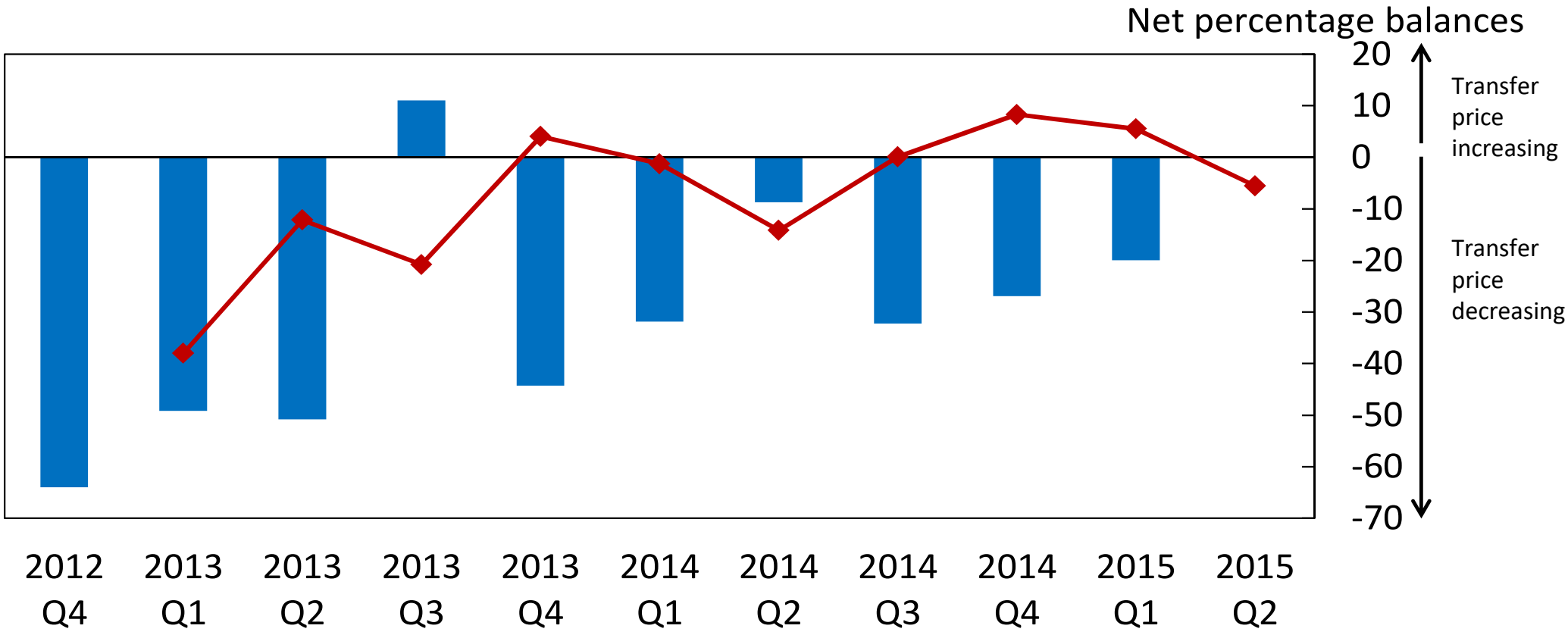
Bank funding costs at new lows…

Retail and wholesale measures of bank funding costs



… driving transfer prices down

Bank Liabilities Survey: 'how has your transfer price changed over the past three months?'



Blue bars show the responses over the previous 3 months, red diamonds expectations for next 3 months.

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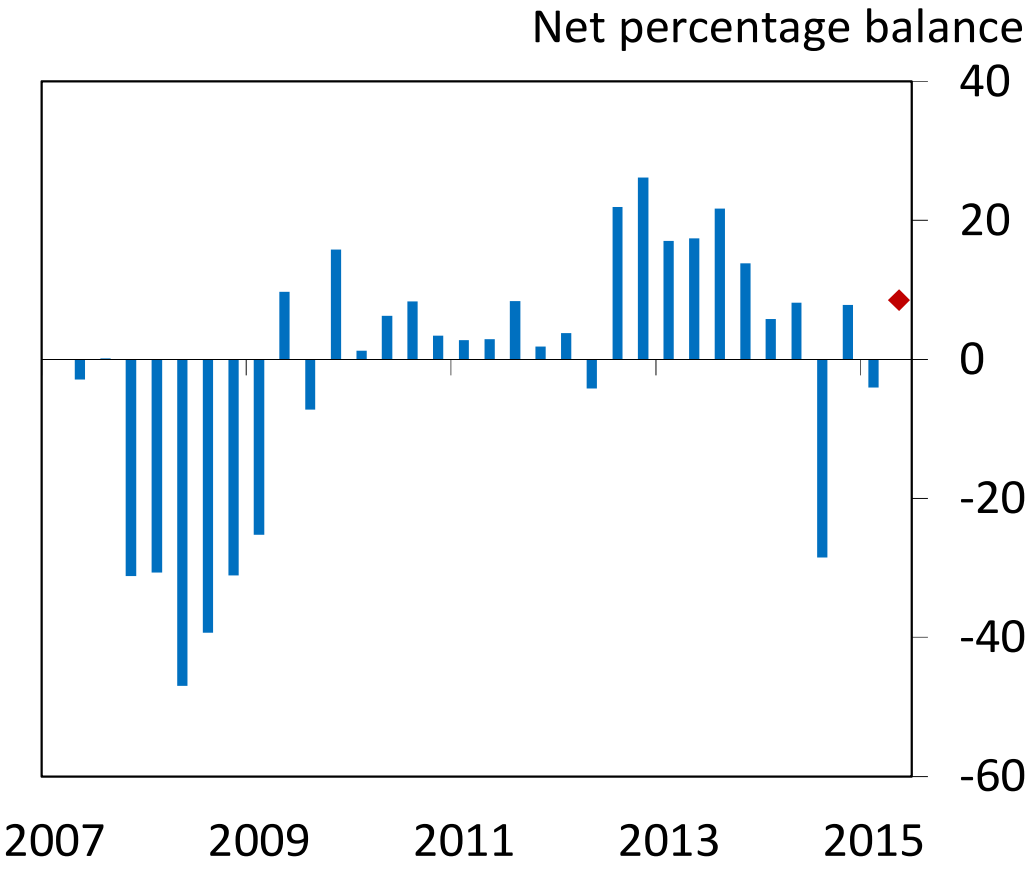
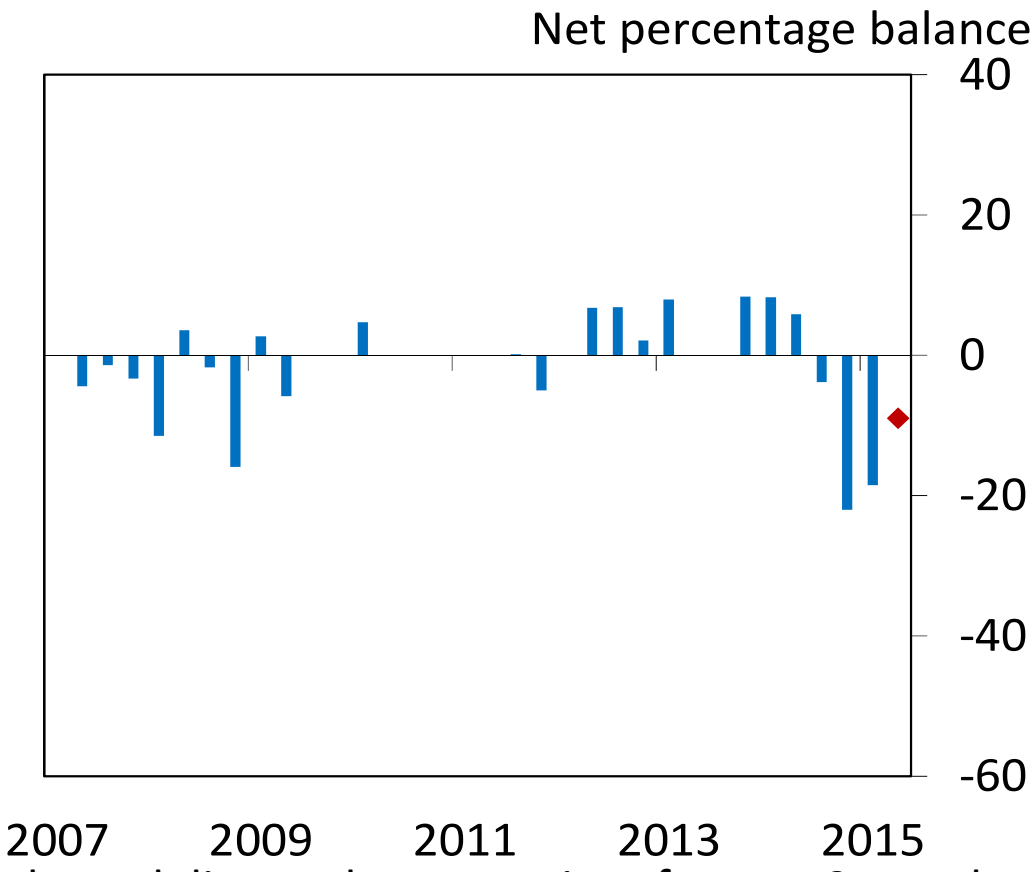
Mortgage availability falling in certain market segments…

CCS – change in availability of secured lending



CCS – change in maximum LTIs



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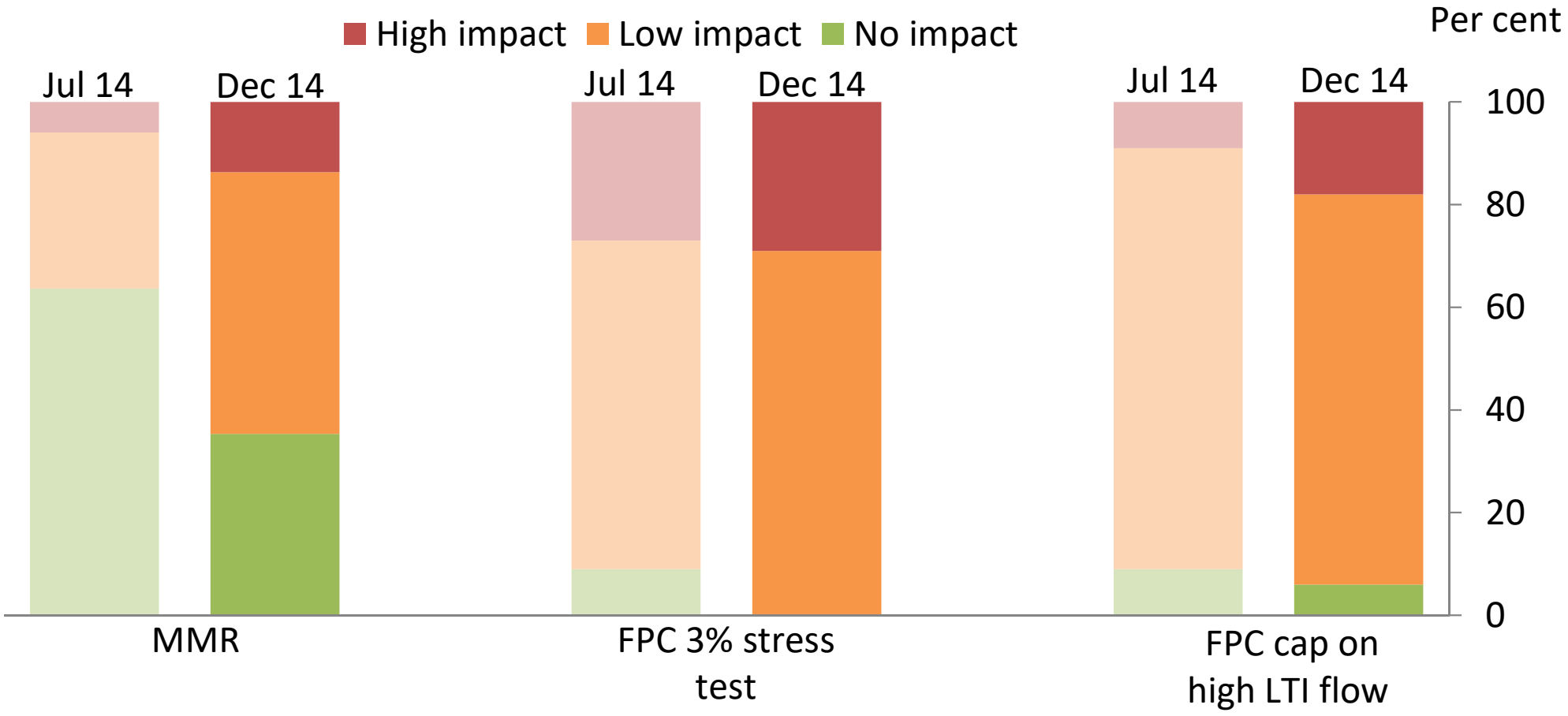
… in response to recent regulatory changes

- The ‘general equilibrium’ effect of the FPC LTI recommendation
- Impact of MMR larger than expected
- FPC interest rate stress test recommendation affecting some lenders
- <u>Individually small, but potentially significant when added together</u>

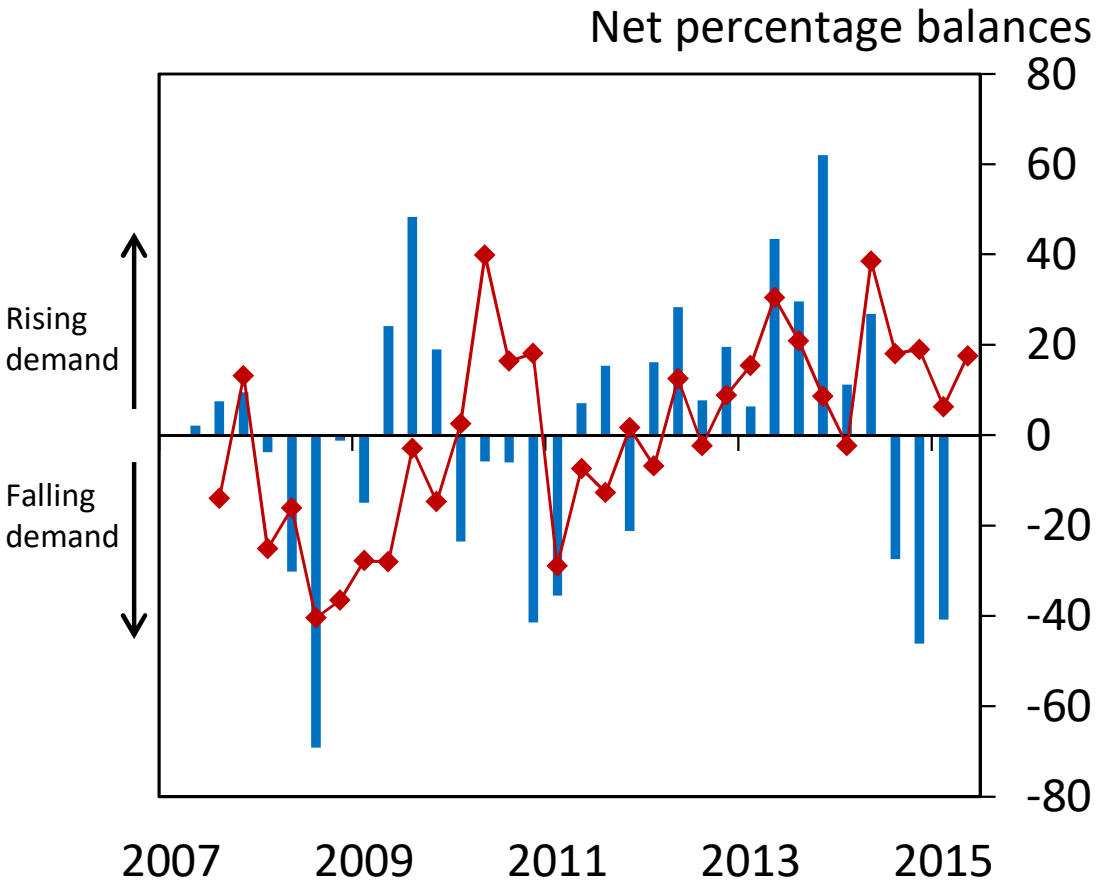
IMLA survey of lenders supports B6 intelligence

Intermediary Mortgage Lenders Association survey of mortgage lenders

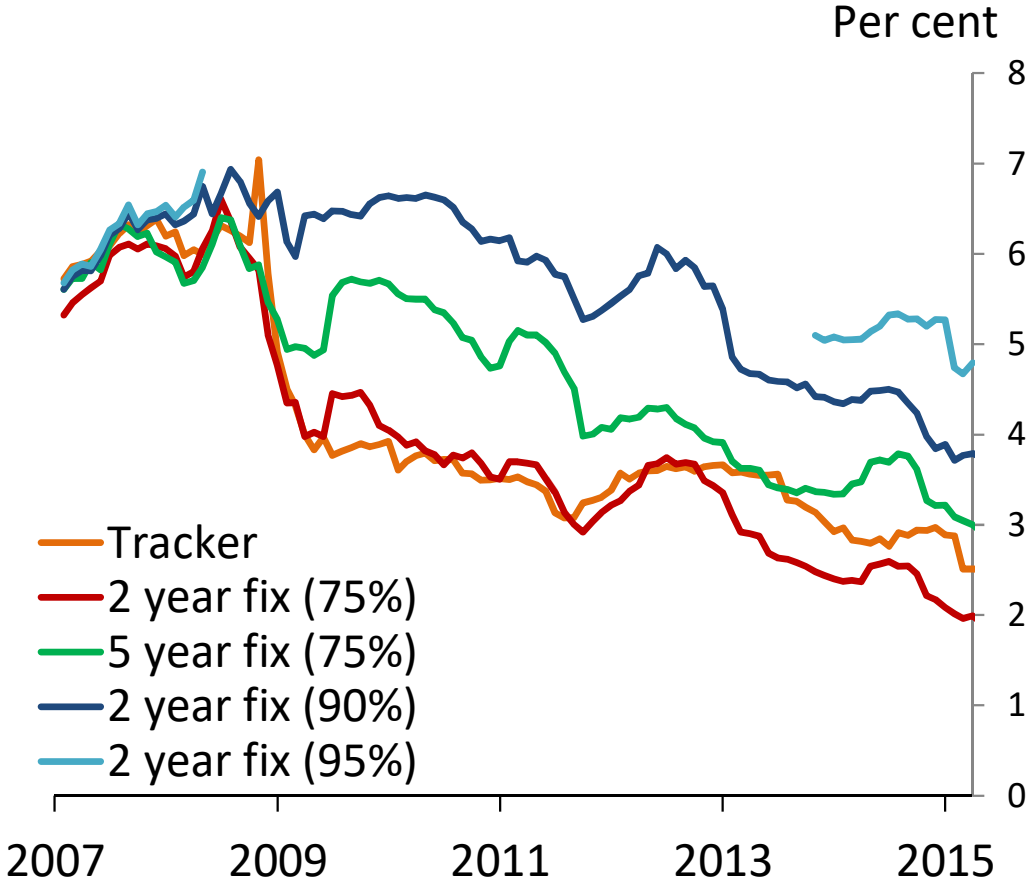


Mortgage demand weak despite low rates

CCS balance - demand for secured credit



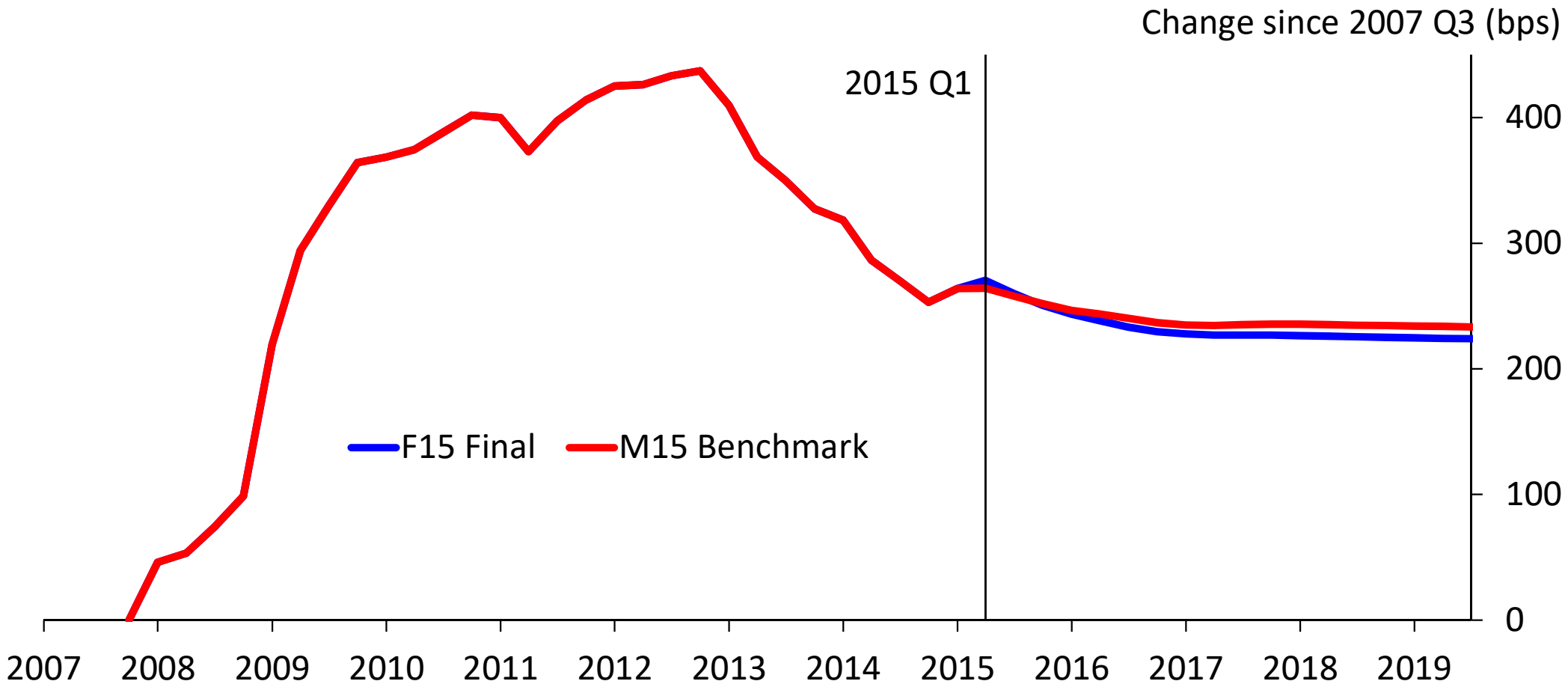
Quoted mortgage rates



Why is mortgage demand so weak?

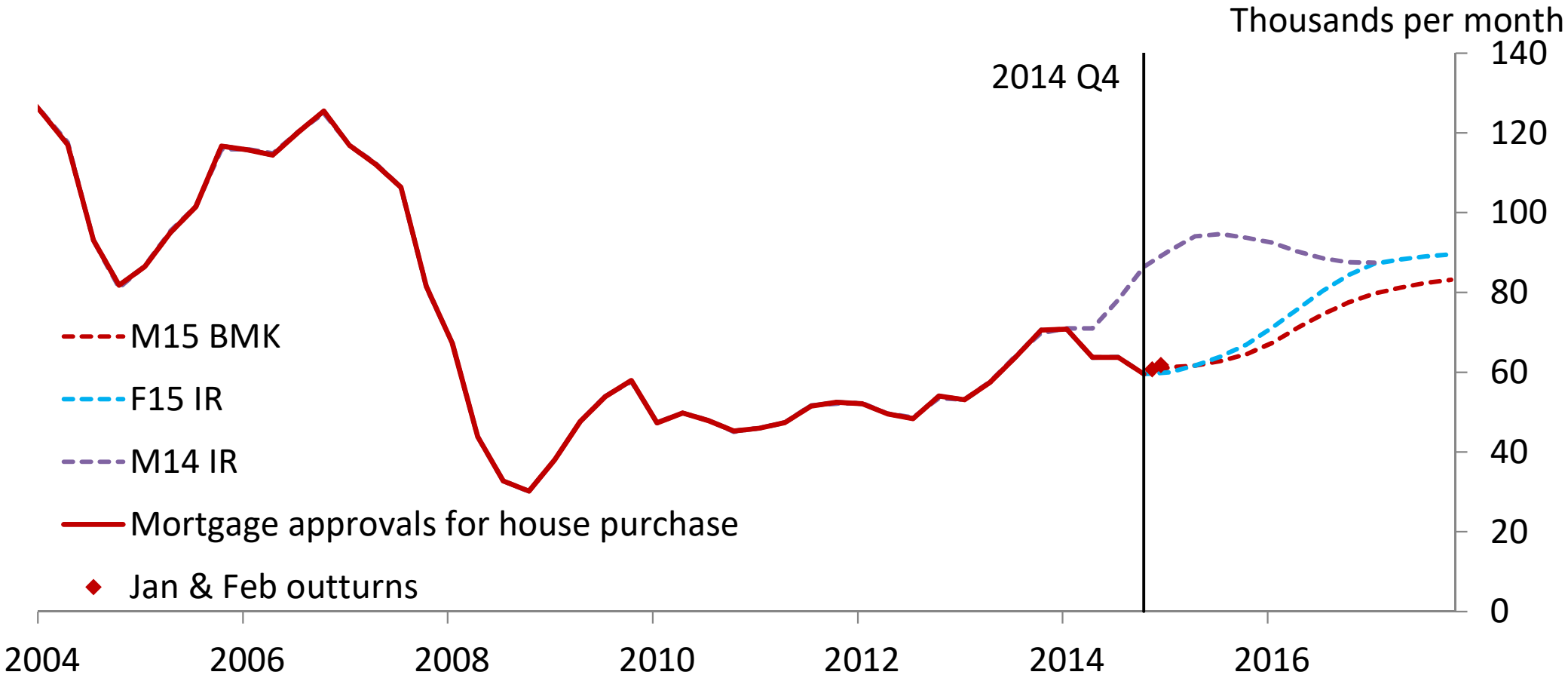
- Weak affordability, particularly in the South East
- Effect of MMR on demand as well as supply
- Possible election uncertainty
- Increased trend towards broker-intermediated business?

May BMK household CSA largely unchanged…



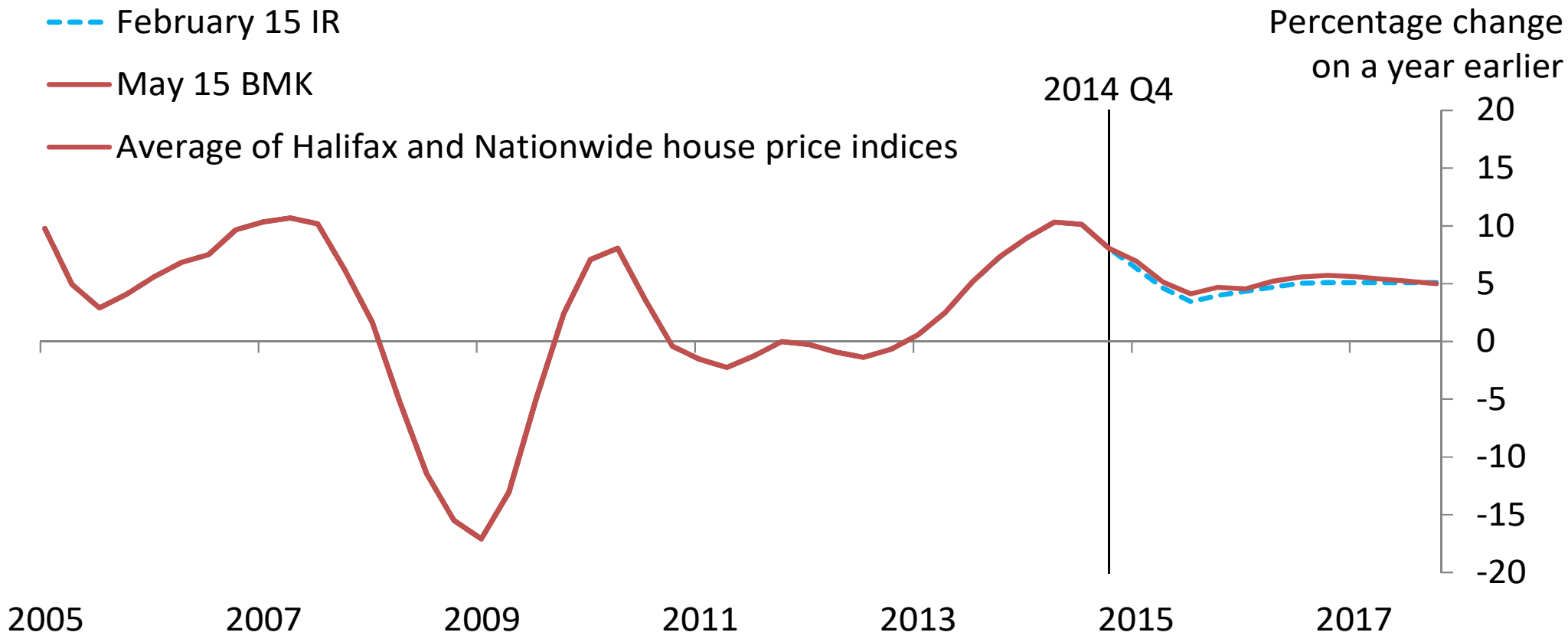
… approvals forecast is a little weaker…

Mortgage approvals for house purchase, SA



… but house price forecast little changed

House price inflation



See "Recent developments in, and prospects for, the housing market"

Housing market: conclusions

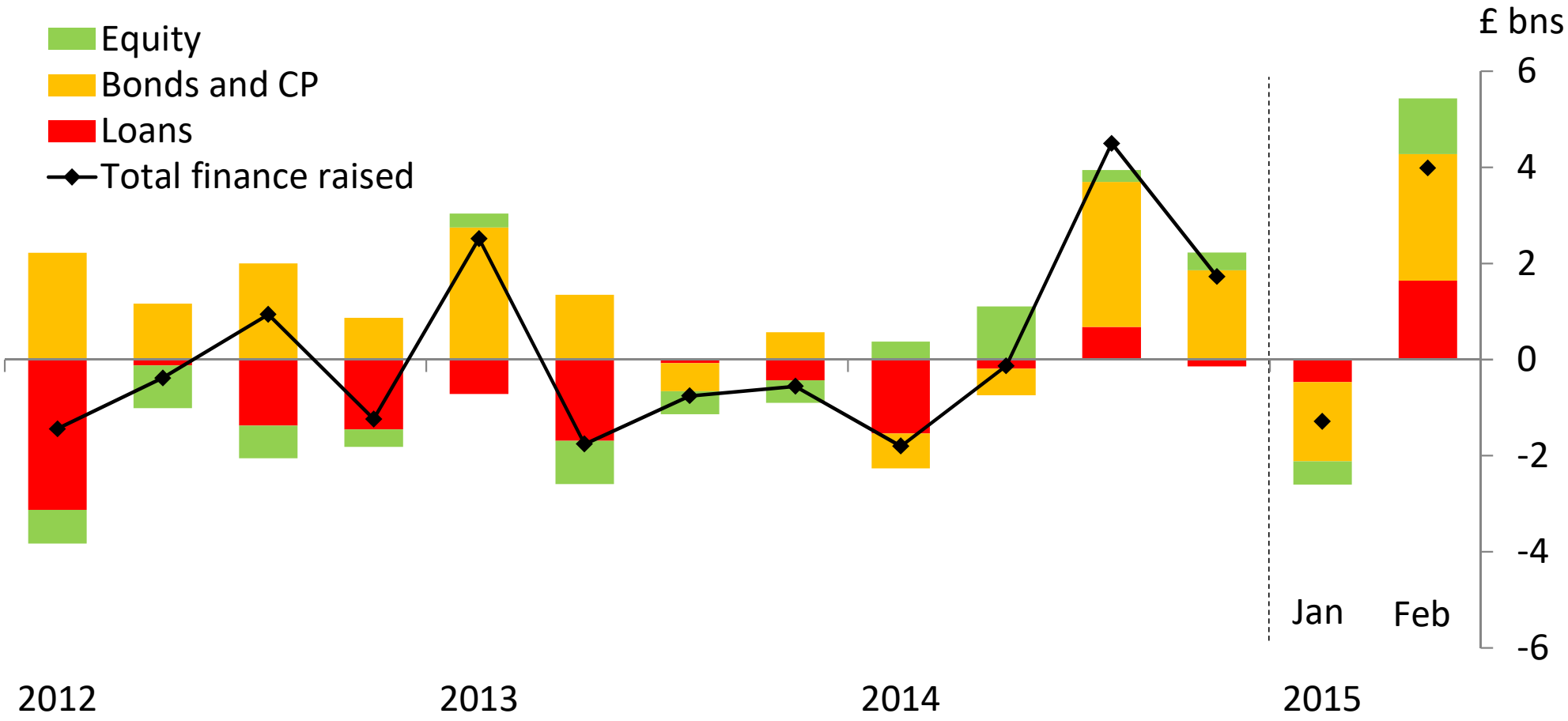
- Mortgage activity in line with February IR forecast so far
- But some risk that the new steady state level of activity will be lower
- House prices continue to be broadly in line with our forecast, but risks are probably to the upside further out

Agenda

- Bank funding update
- Latest housing market forecasts
- **Update on corporate credit conditions**
- Inflation expectations stocktake

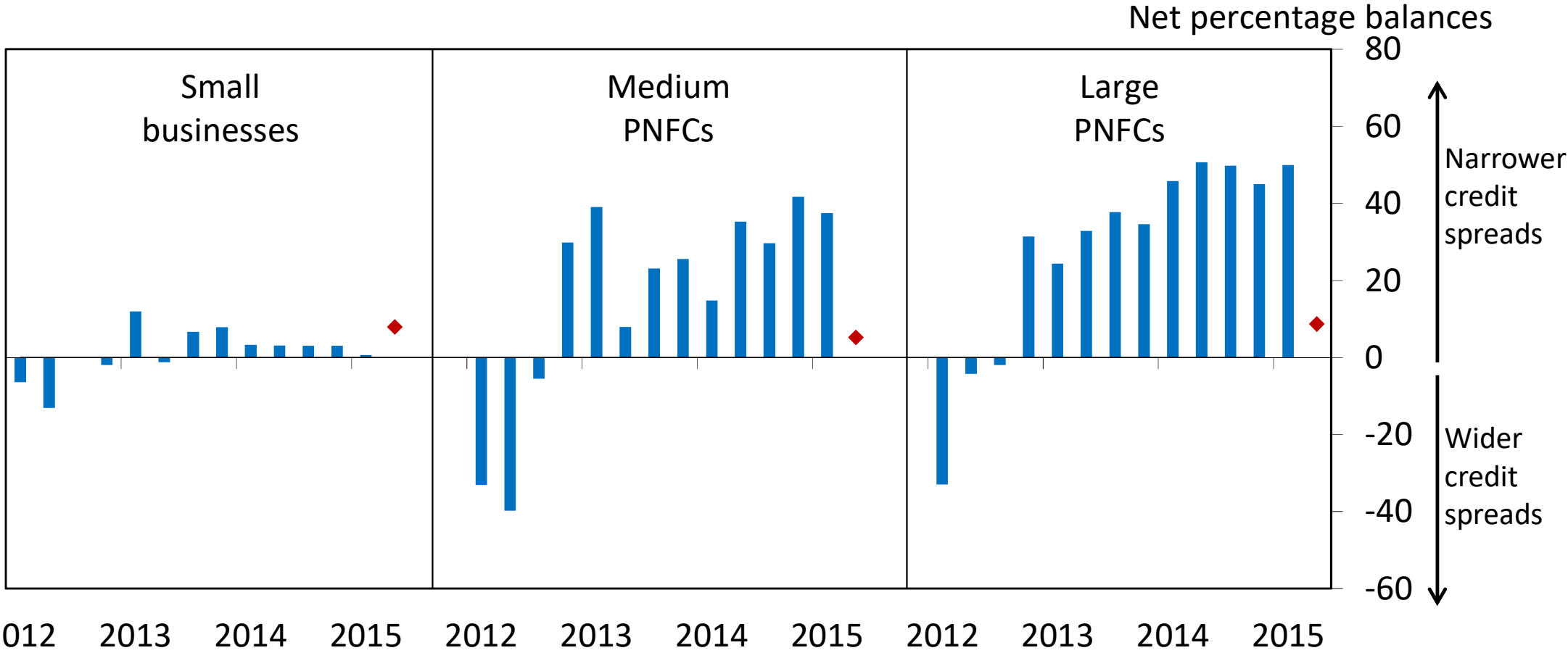
… and net finance raised was also strong on the month

Net finance raised by UK businesses (monthly averages)



Spreads continue to narrow, particularly for larger firms…

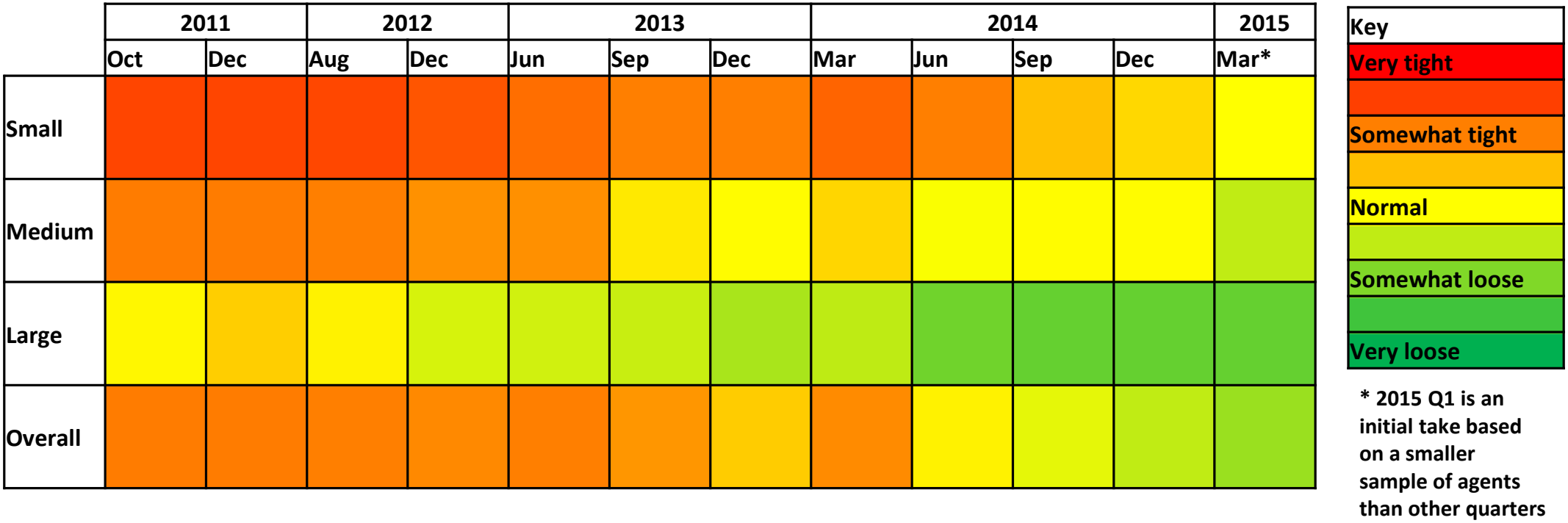
Credit Conditions Survey - credit spreads by firm size



Blue bars show the responses over the previous 3 months, red diamonds expectations for next 3 months.

… which is consistent with evidence from the Agents

Agents' assessment of corporate credit availability

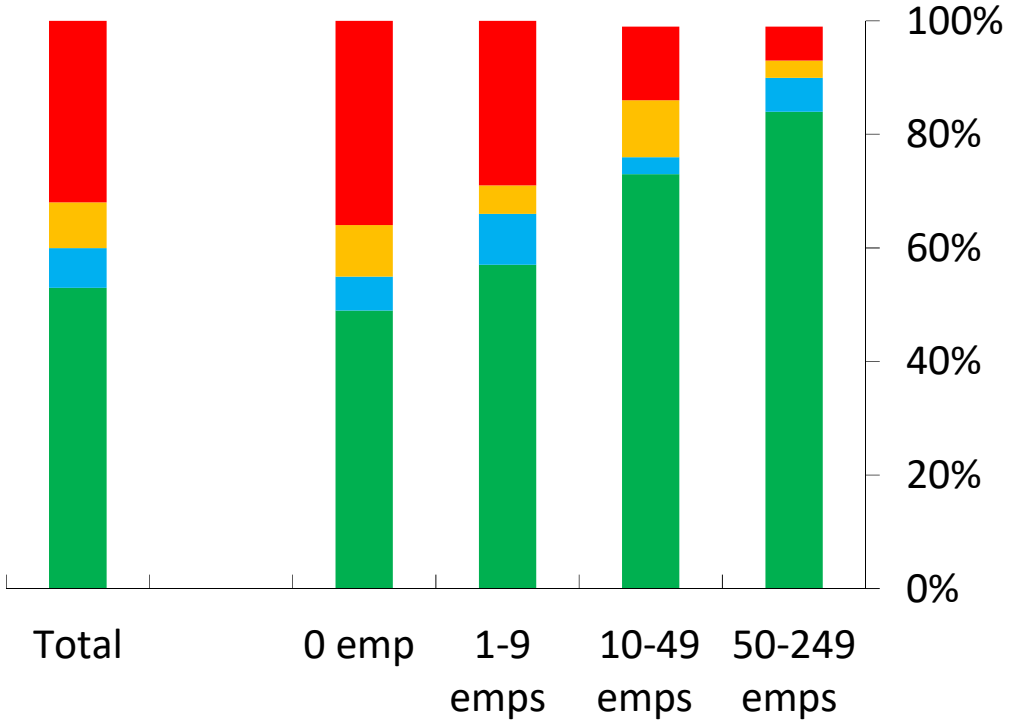


* 2015 Q1 is an initial take based on a smaller sample of agents than other quarters

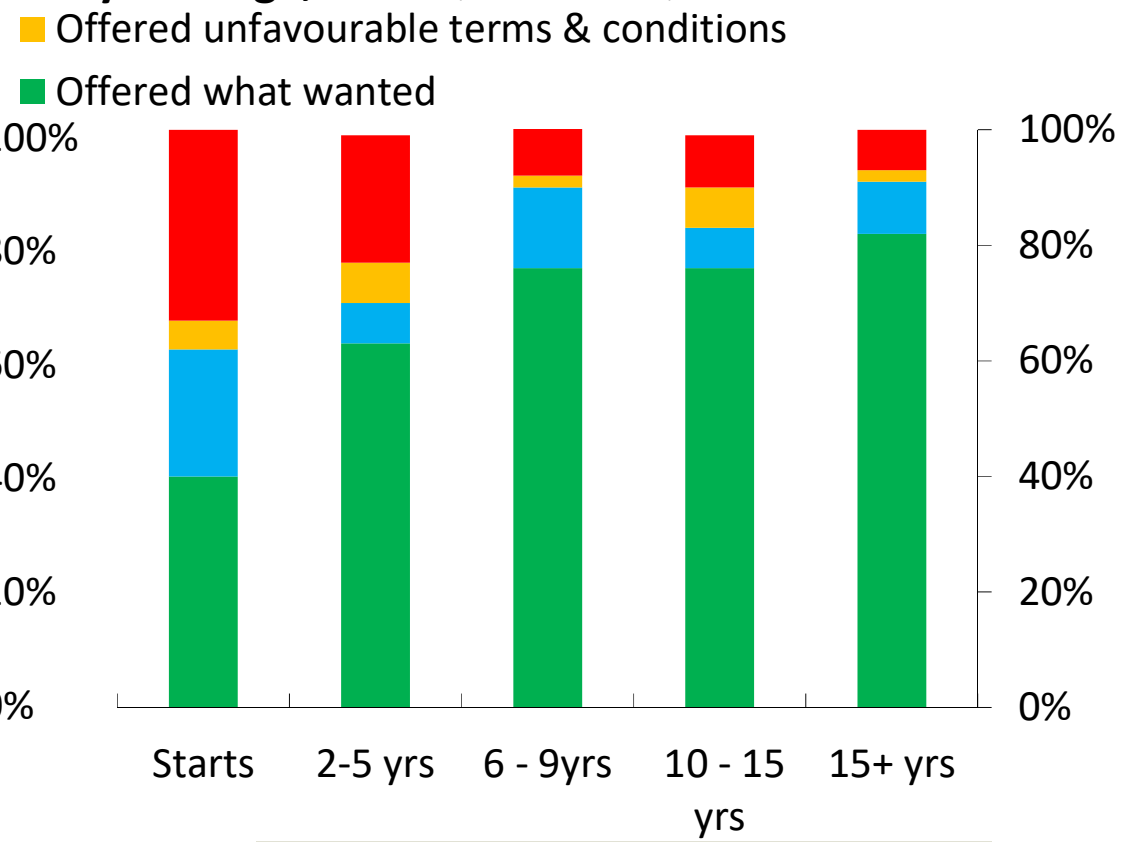
This mapping is based on individual Agencies' assessments of corporate credit availability, weighted by the gross value added of their regions or countries. Firm size defined by number of employees. See Quarterly Bulletin article *The Agencies and 'One Bank'* by England et al (2015Q1).

Acceptance rates lower for smaller and newer businesses…

SME Finance Monitor: acceptance rates on loan applications by size, 2013Q3 – 2014Q4

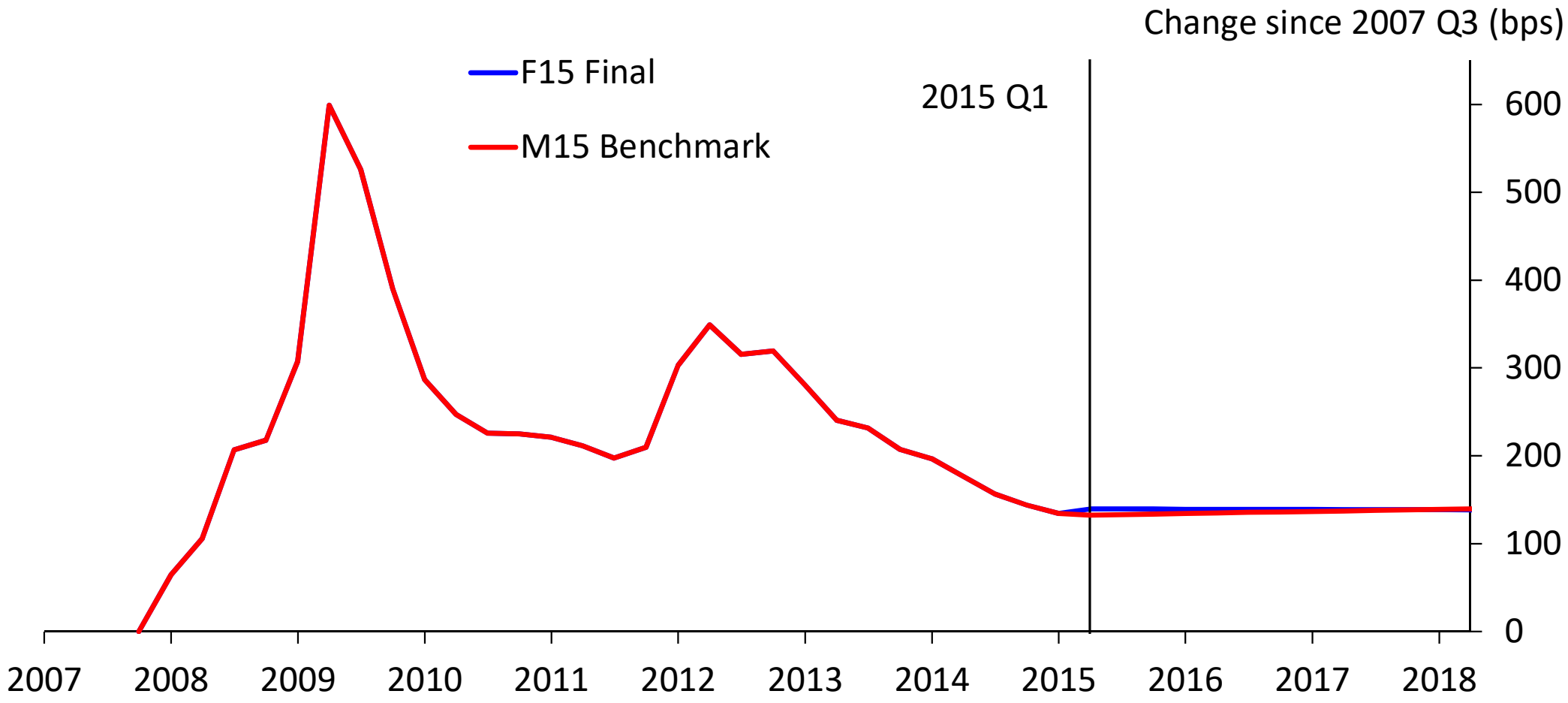


SME FM: acceptance rates on overdraft applications by firm age, 2013Q3 – 2014Q4



For more detail on credit conditions for small & micro firms

… and flat CSA forecast conceals different conditions across firm size

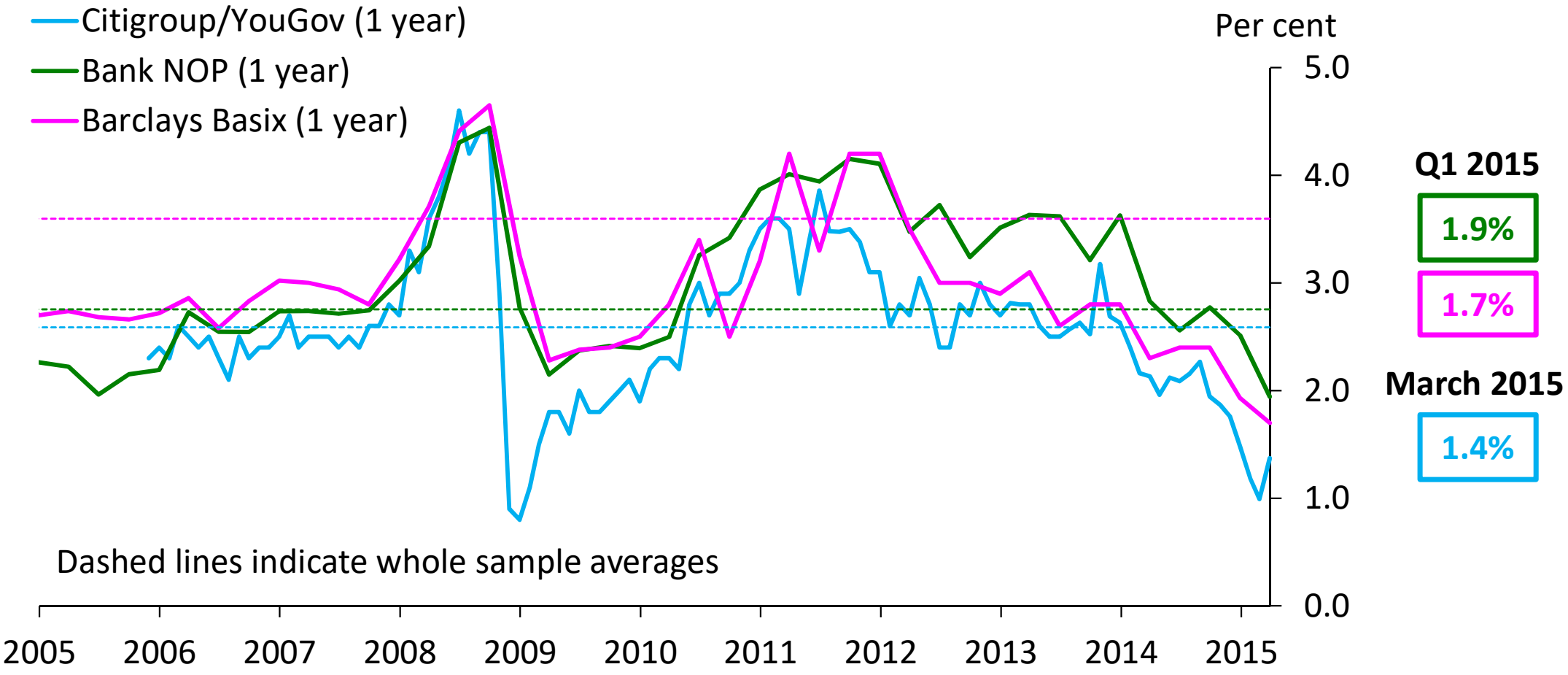


Agenda

- Bank funding update
- Latest housing market forecasts
- Update on corporate credit conditions
- **Inflation expectations stocktake**

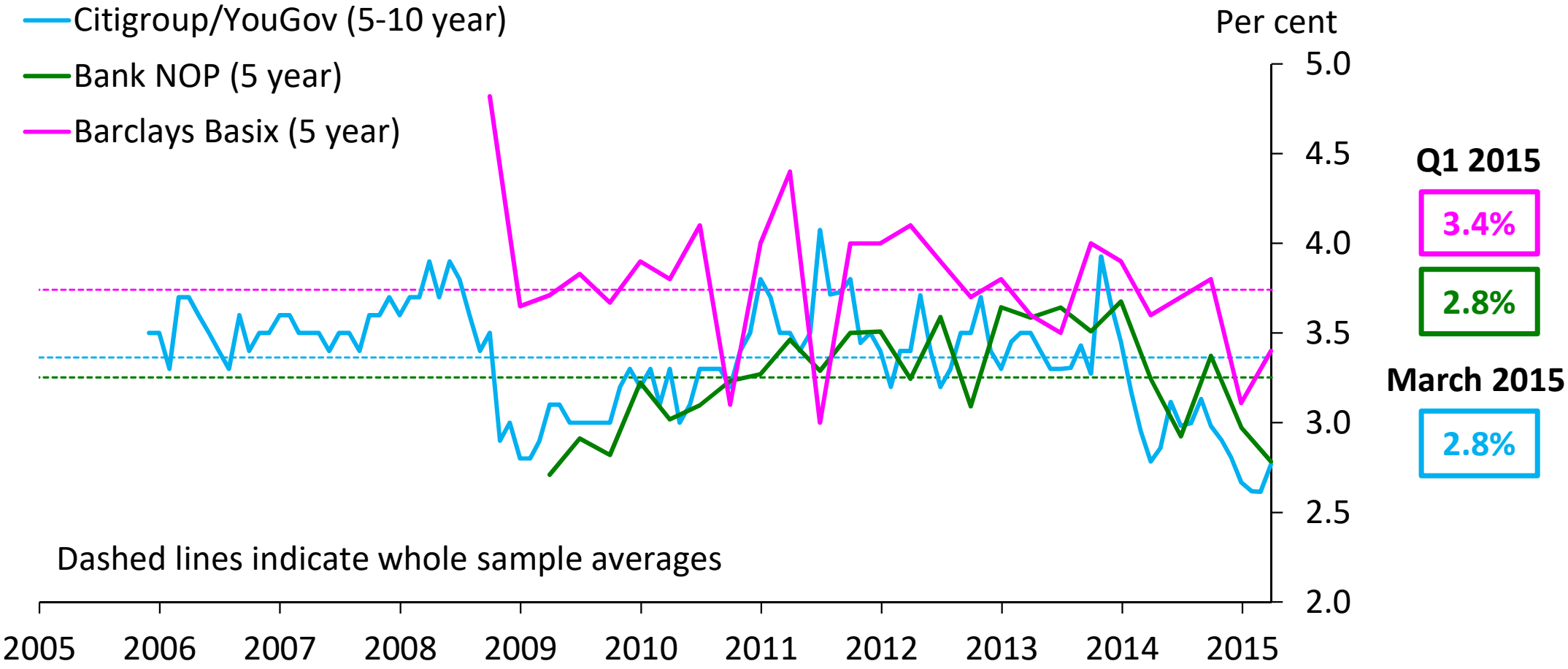
Mixed picture on the month for short-term inflation expectations….

Short-term measures of households' inflation expectations



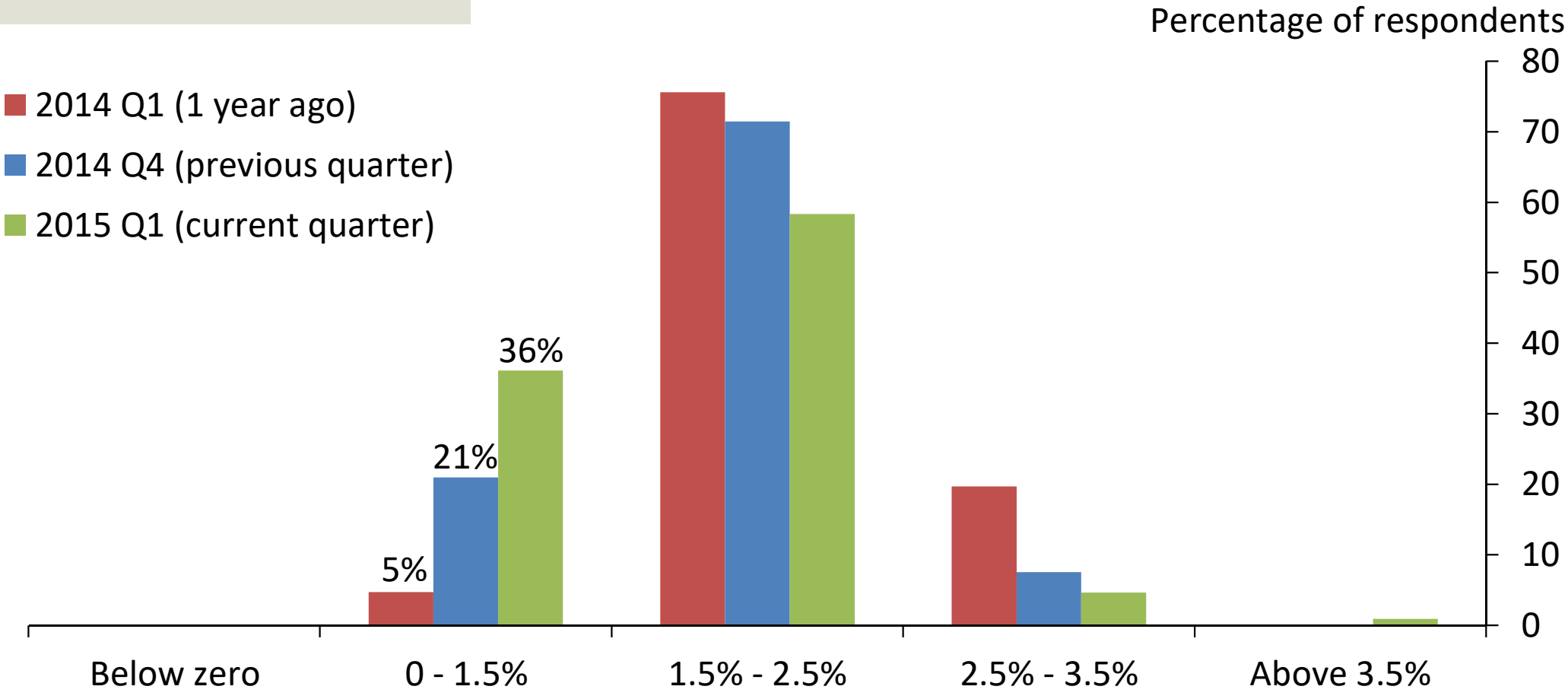
…but households' longer-term inflation expectations have picked up

Long-term measures of households' inflation expectations



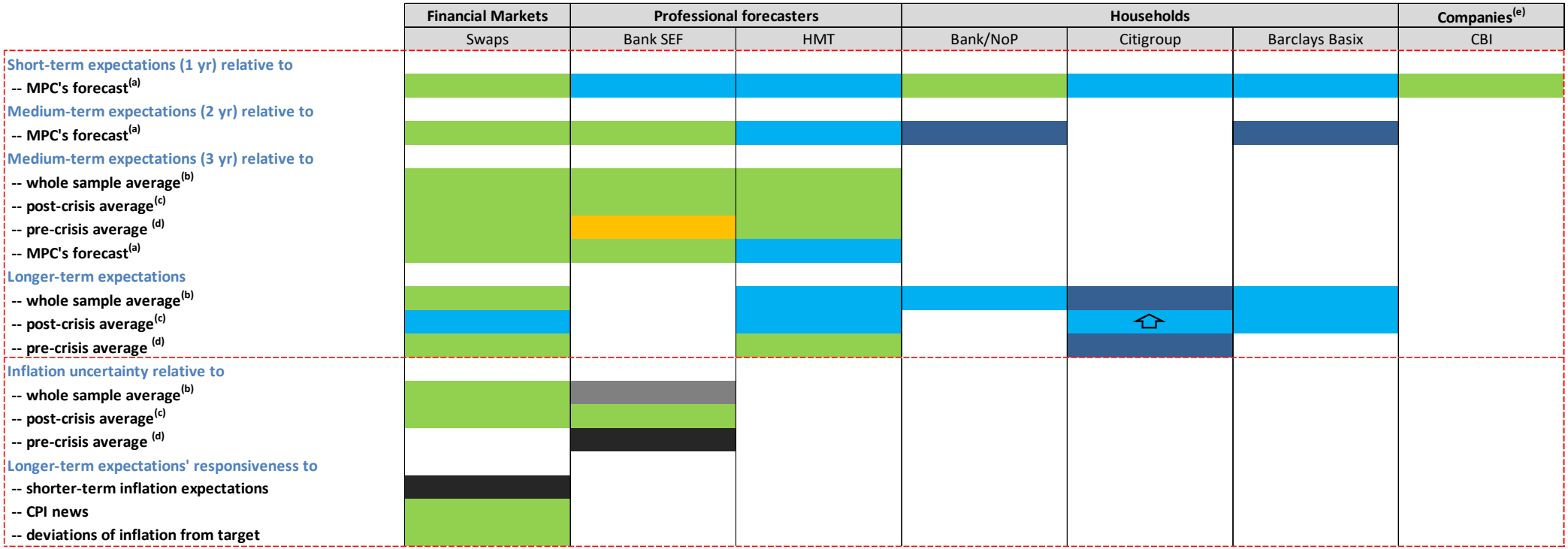
CFOs have lowered their CPI expectations at the 2-year horizon

Deloitte CFO Survey 2015 Q1



Heatmap is little changed on the month

Latest heatmap (April 2015)



Key for π^e levels

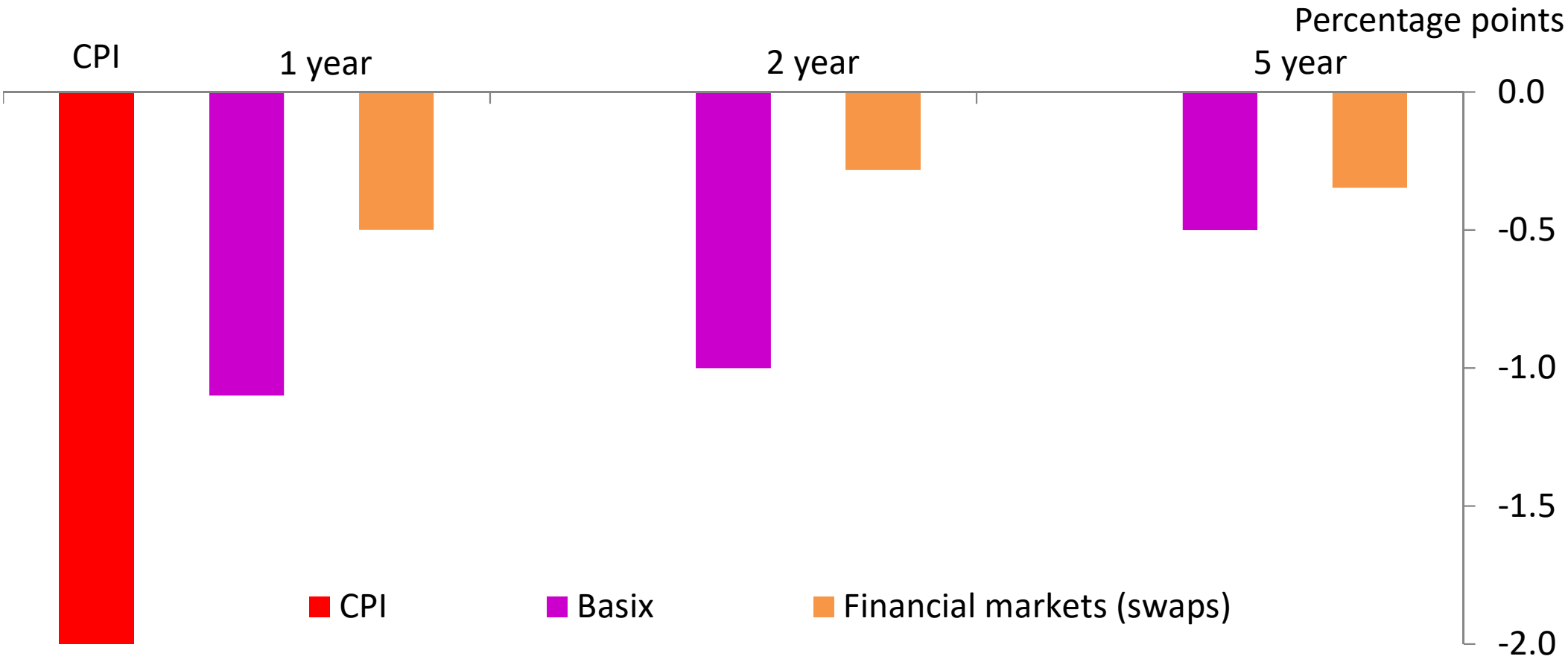
- More than 2 SD above
- More than 1 SD above
- Within 1 SD
- More than 1 SD below
- More than 2 SD below

Key for uncertainty and responsiveness

- Considerably above average
- Somewhat above average
- Around or below average

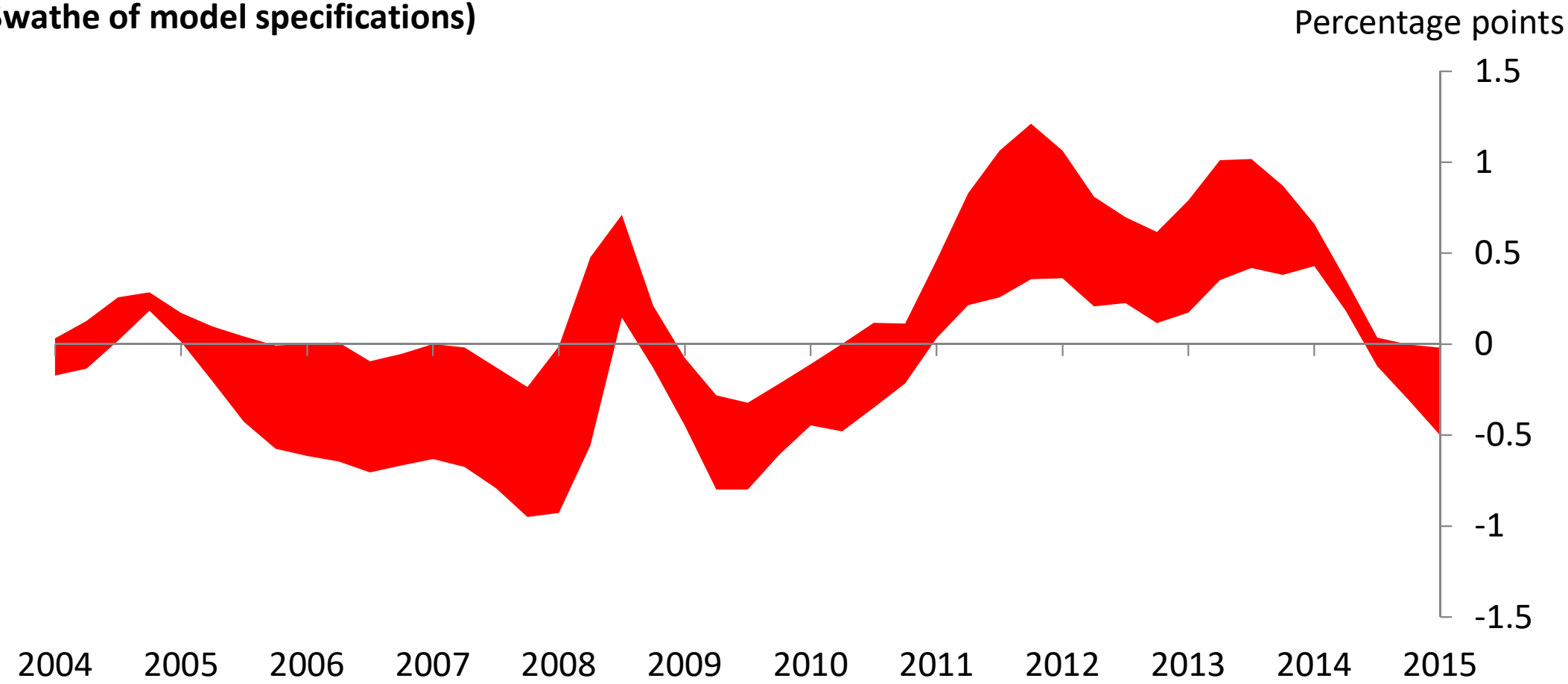
Inflation expectations have fallen at all horizons

Change in inflation expectations since 2013 Q4



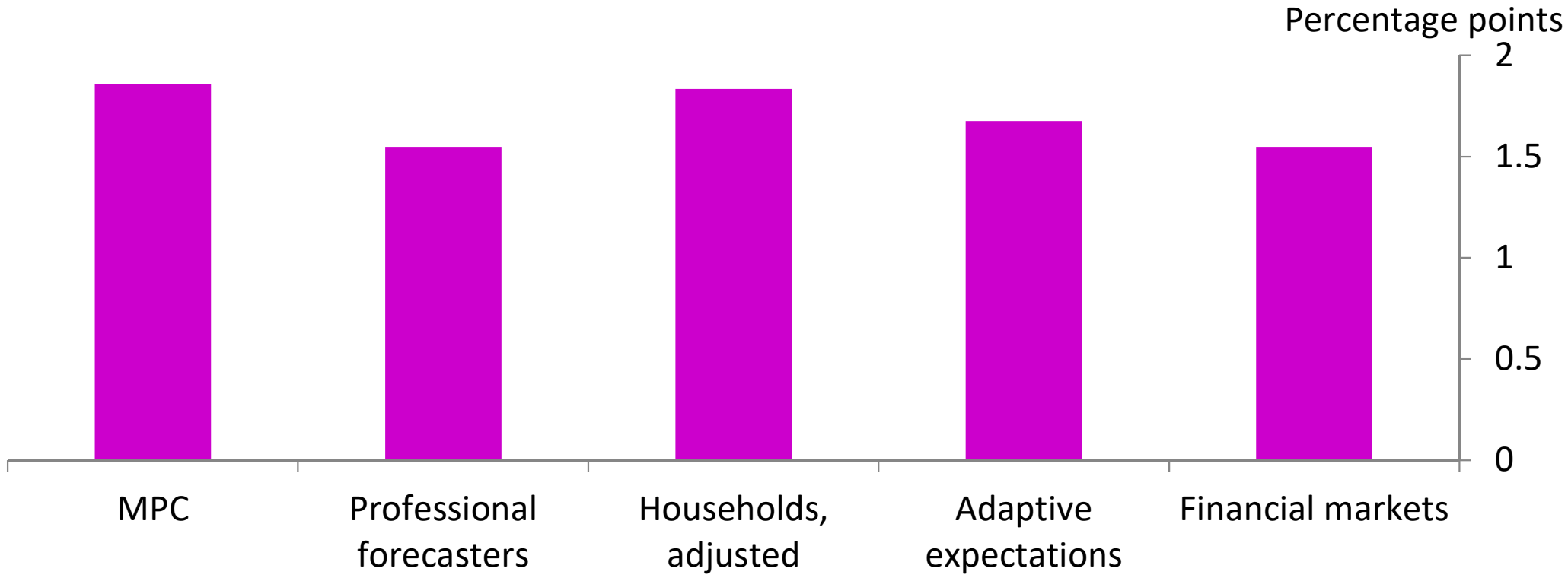
Inflation expectations might have lowered inflation

SVAR model: contribution of inflation expectations shocks to movements in inflation away from trend (Swathe of model specifications)



Households have a similar inflation forecasting track record to others

Root mean squared error of two year ahead inflation forecasts, since 2008 Q1



Professional forecasters' inflation expectations refer to the 2 year expectations in the HMT survey.
Households' expectations refer to the 2 year expectations in the Bank/NOP survey from 2009 Q2, adjusted by 1pp to reflect the average wedge between respondents perceptions of inflation and actual inflation.
Adaptive expectations assume that inflation at the 2 year horizon will be equal to the current inflation rate.
Financial markets expectations refer to the instantaneous 2 year forward rate and its forecast performance is judged relative to RPI outturns.

Jury out on whether inflation expectations affect wages

Recap of February Key Issues:

- Households and financial market expectations significant in *some* wage equation specifications
- Neither can explain the recent weakness of wages
- Risks to wages depend on which matter most now

But…..

- As pointed out last month, changing the estimation period changes the results
- A lack of variability, or a lack of relationship?

Inflation expectations: conclusions

- Medium-term inflation expectations have fallen by more than suggested by simple models
- Households little worse at forecasting inflation than others
- Significance of inflation expectations for wages depends on estimation period
- SVAR points to role for inflation expectations in explaining falls in inflation, but extent depends on specification

Overall Conclusions

- Funding costs remain low
- Mortgage market activity remains subdued, relative to house prices
- Credit conditions continue to ease for most firms, but evidence that conditions are still tough for very small firms
- No further cooling in the inflation expectations heatmap on the month

Bank of England
International Directorate

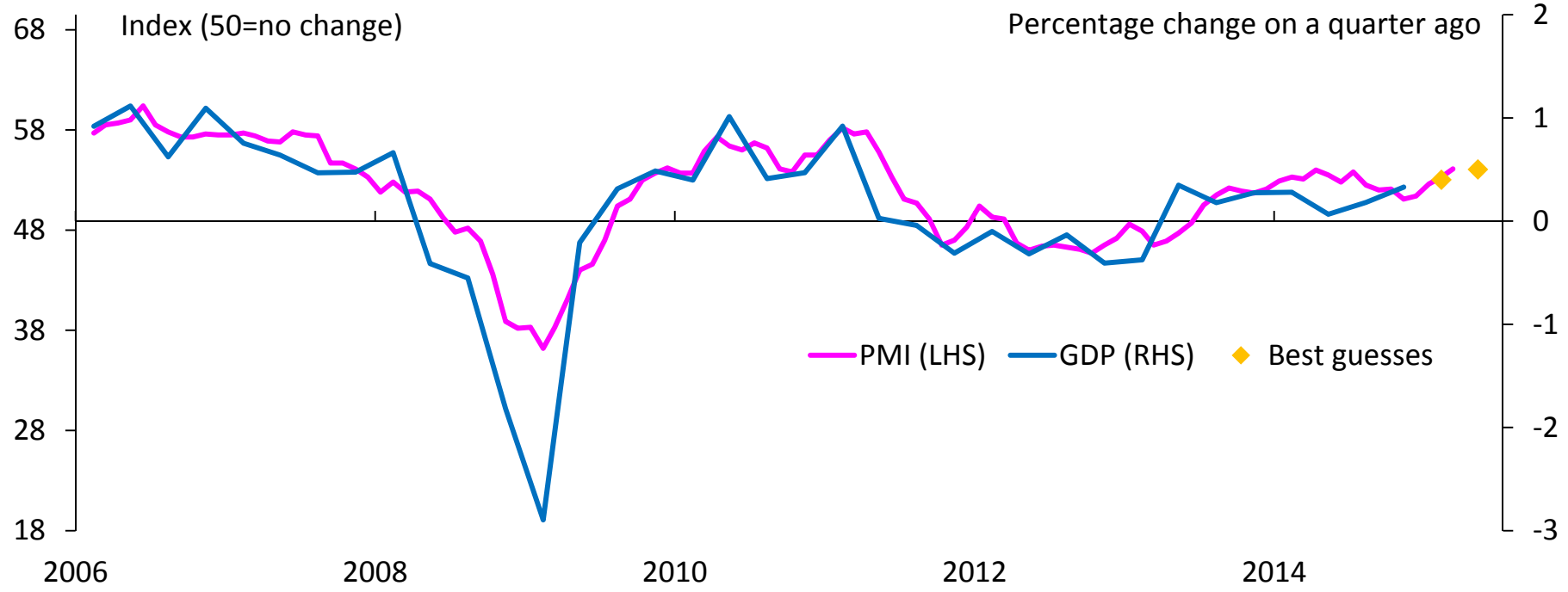
Global Environment
Pre-MPC April 2015

Outline

- Near-term prospects for activity
  - Euro area
  - US
  - China
- Global (dis)inflation
  - Oil and near-term prospects
  - Cross-country trends

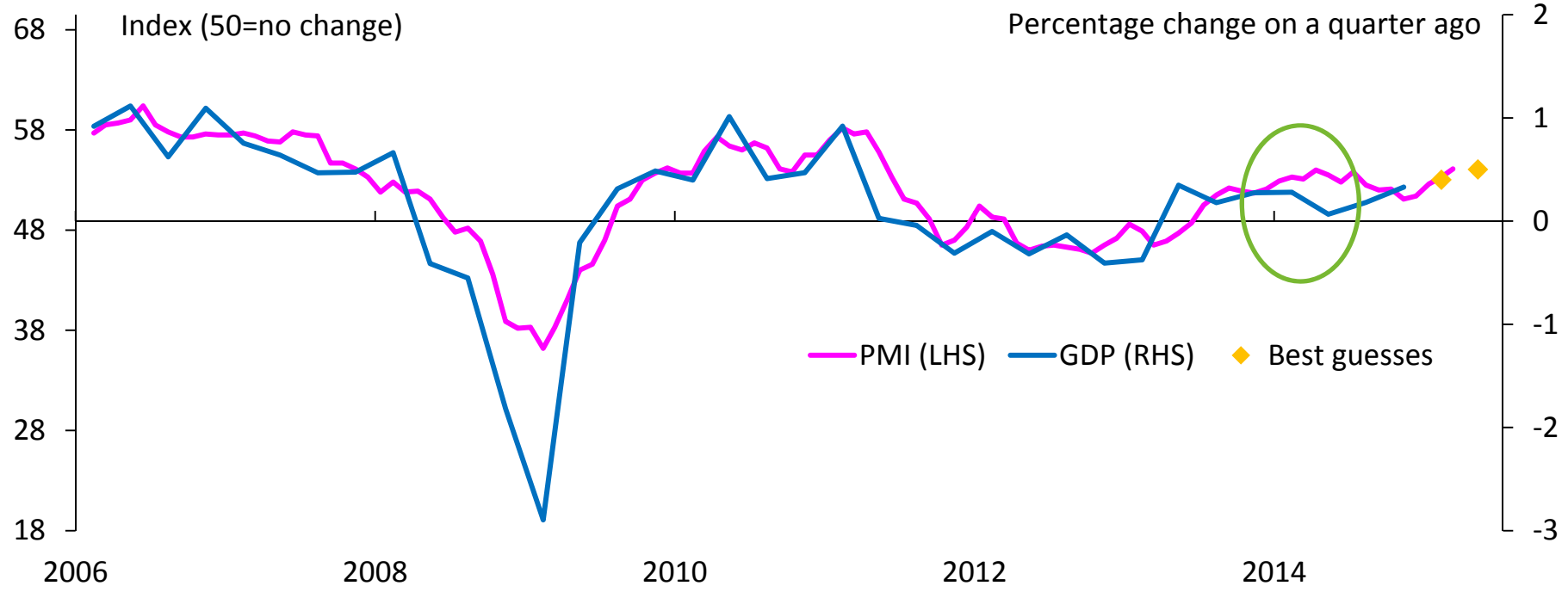
Euro area

Euro-area GDP and PMIs



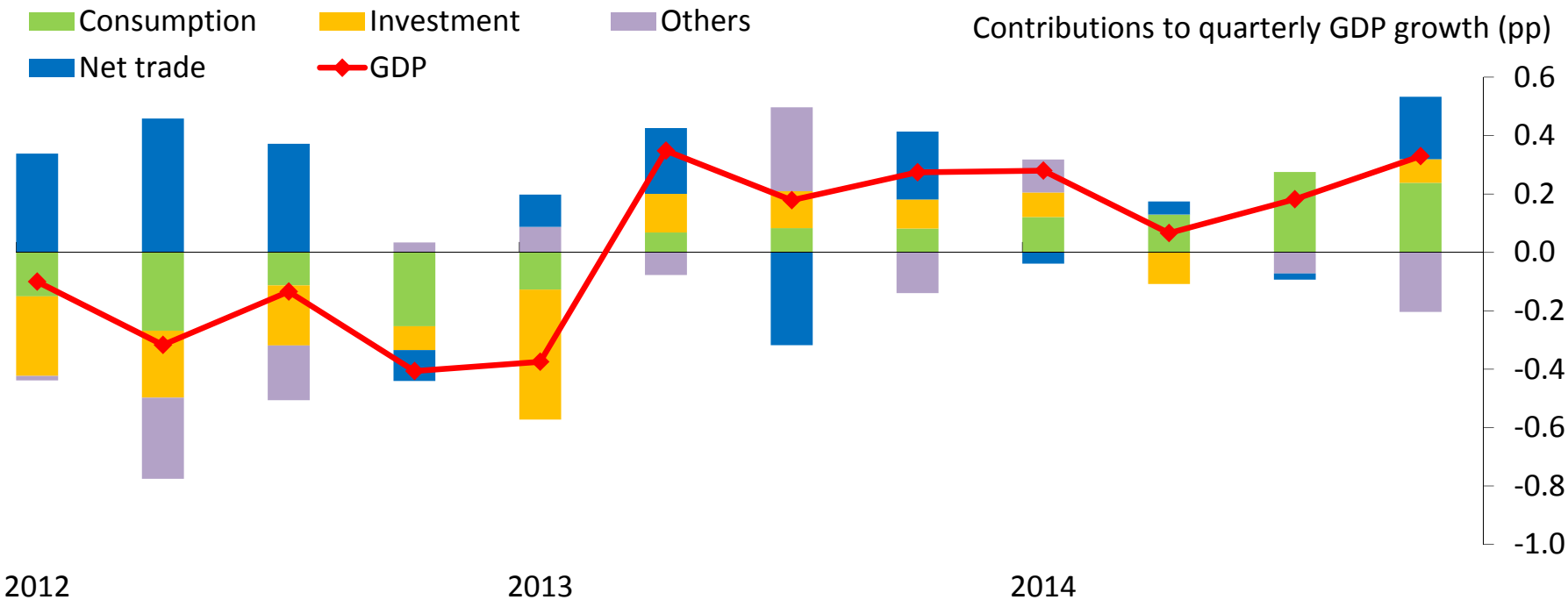
- We've revised up our best guesses for Q1 and Q2 to 0.4 and 0.5% in the May BMK forecast (from 0.3% and 0.4%).

Euro-area GDP and PMIs



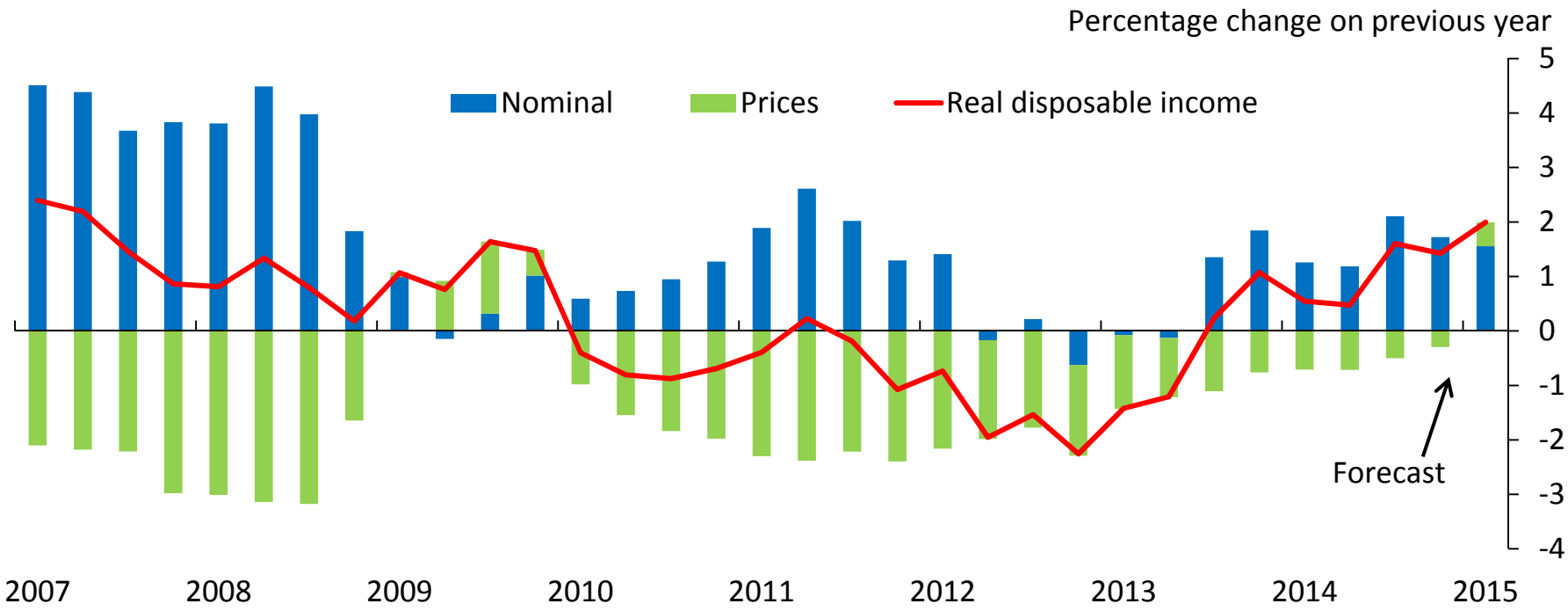
- The March PMI picked up, suggesting activity accelerated further in Q1. But the PMI has proved to be a misleading indicator in the recent past….

EA growth expenditure split



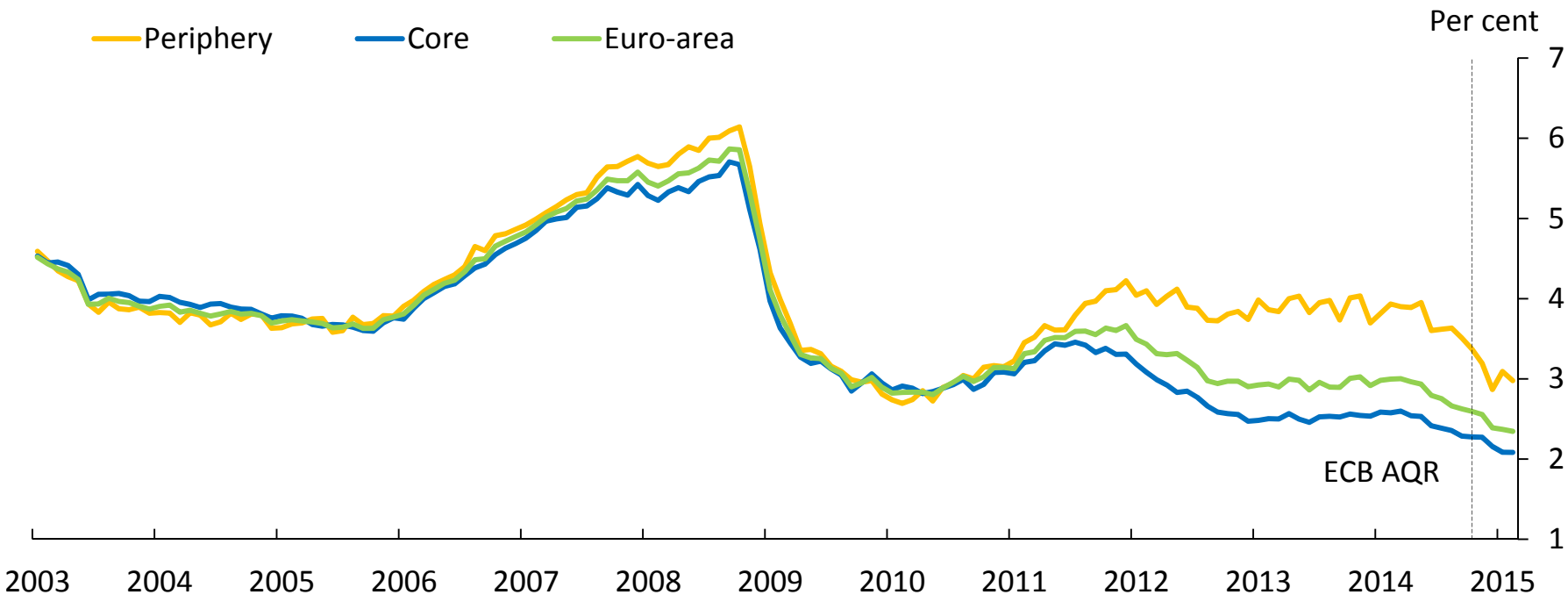
- In 2014 Q4 EA grew by 0.3% (0.1% higher than in the Feb IR), with the pick-up driven by exports, investment and consumption. News to the Feb IR was in consumption and investment.

Household income



- Real income growth is being boosted by lower inflation.

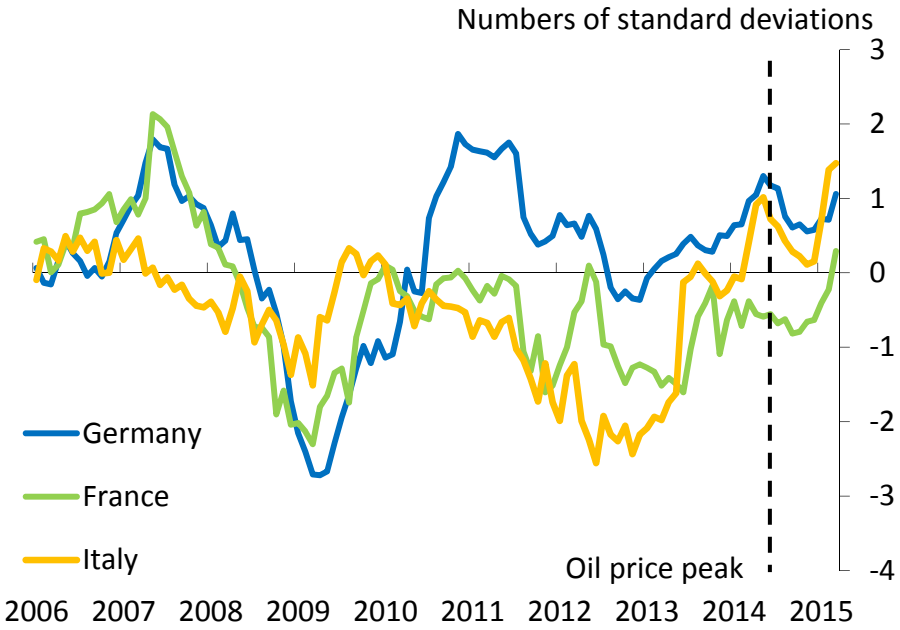
Bank lending rates



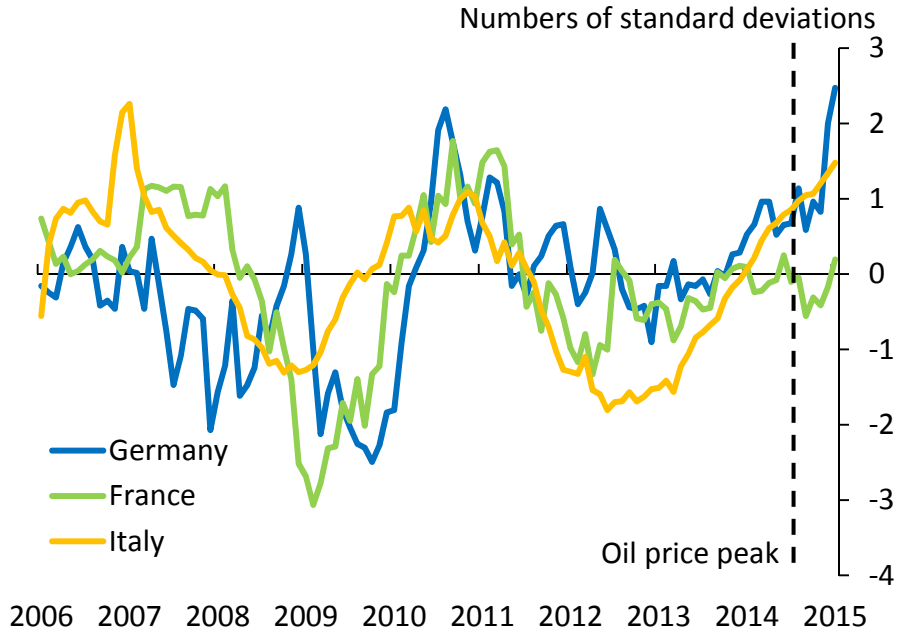
- In the second half of 2014 credit conditions have improved materially, particularly in the EA periphery.

Consumption indicators

Consumer confidence

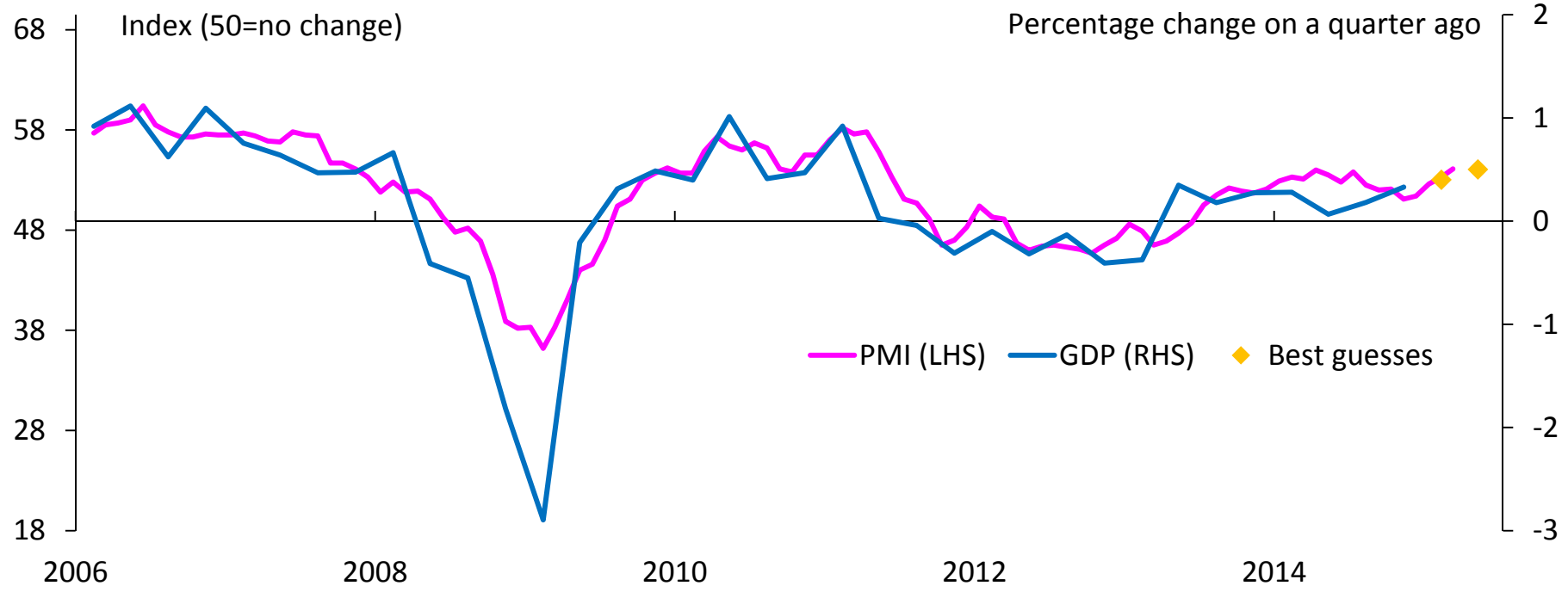


Annual retail sales growth



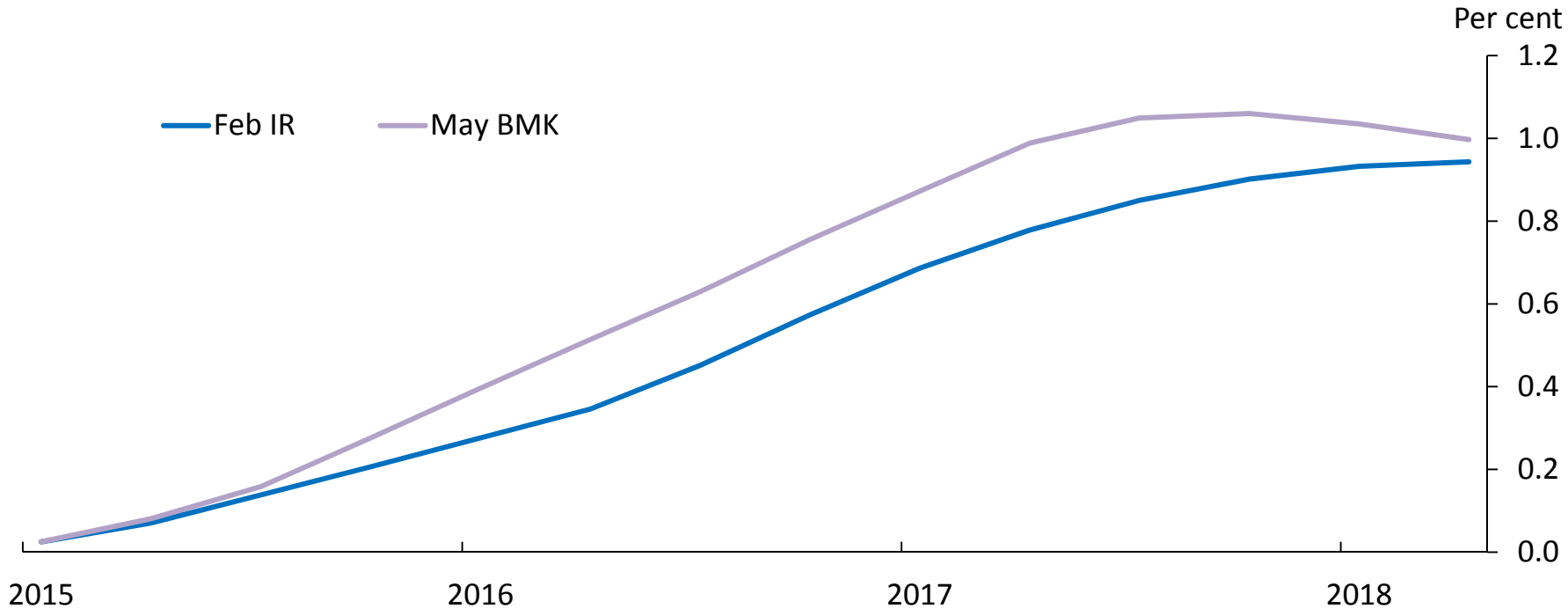
- High frequency indicators point to continued strength of consumption. This might reflect a range of factors, including falling oil prices…

Euro-area GDP and PMIs



- We've revised up our best guesses for Q1 and Q2 to 0.4 and 0.5% in the May BMK forecast (from 0.3% and 0.4%).

Impact of QE (Feb vs May)



- In the May BMK forecast we expect the impact of QE to be a little over 1%.

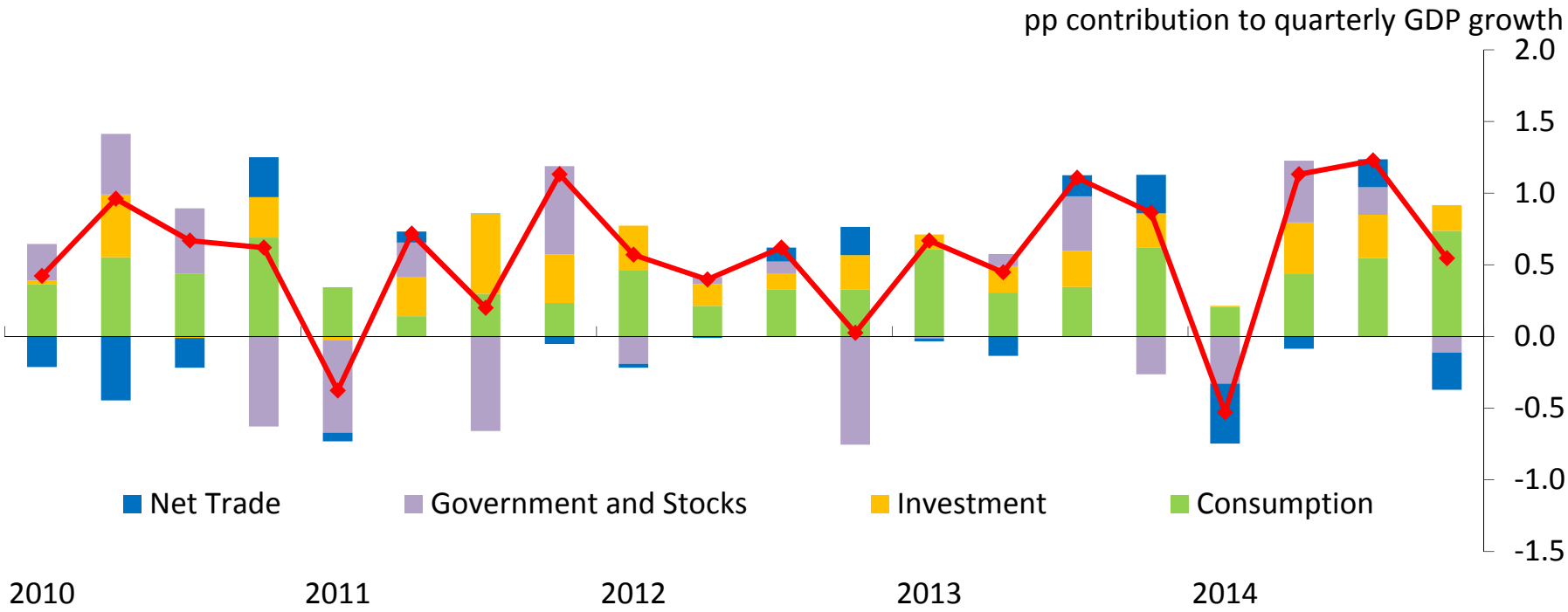
Greece – key events in April

- The government's cash-flow position is critical. There are many potential flashpoints in April.

Date	Event
1 April onwards	Greek authorities and official creditors negotiate detailed list of reforms in exchange for early disbursement of funds
2 April	ECB decides whether to extend ELA access for Greek banks
9 April	IMF repayment of €467m falls due. ECB decides whether to extend ELA access for Greek banks
14 April	T-Bill matures for €1.4bn
16 April	ECB decides whether to extend ELA access for Greek banks
17 April	T-Bill matures for €1.0bn
23 April	ECB decides whether to extend ELA access for Greek banks
End-April	IMF, ECB, Commission and the Eurogroup review progress of proposed structural reforms. This will determine the release of the remaining funds under the current programme (€7.2bn).

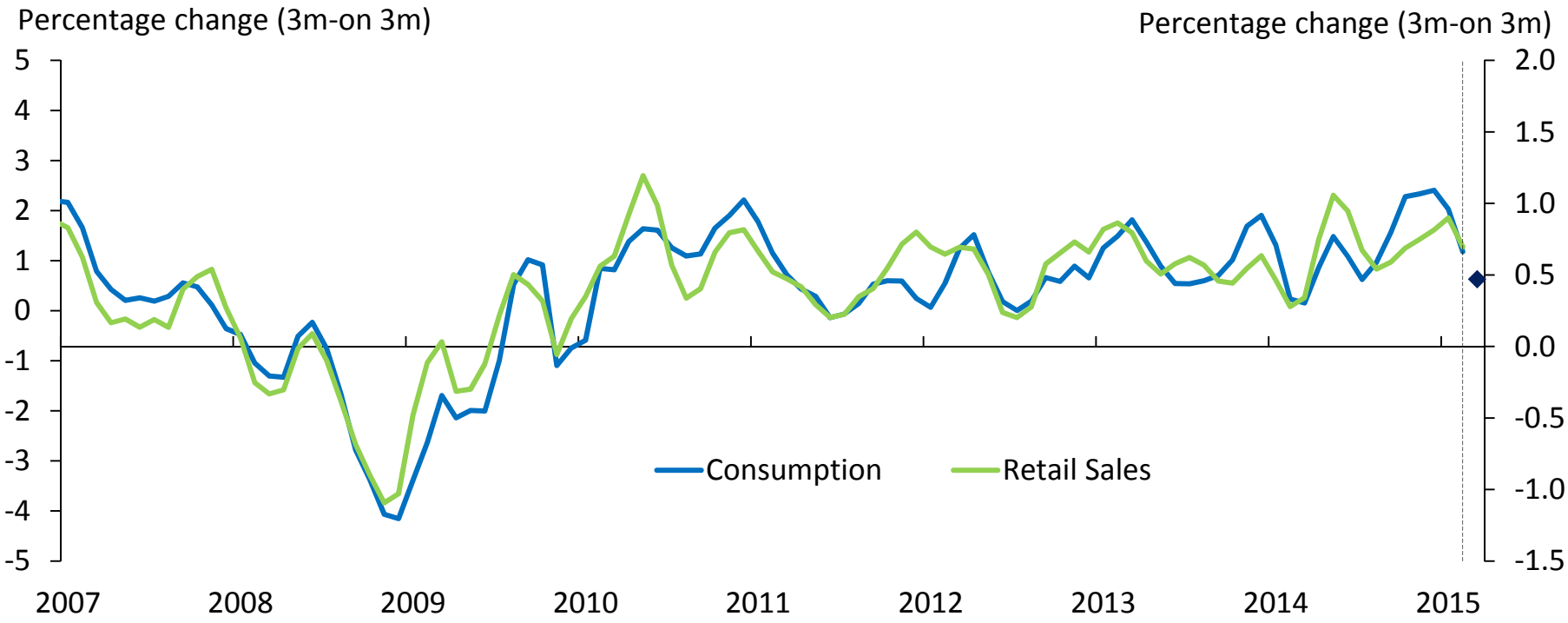
US

US GDP Growth



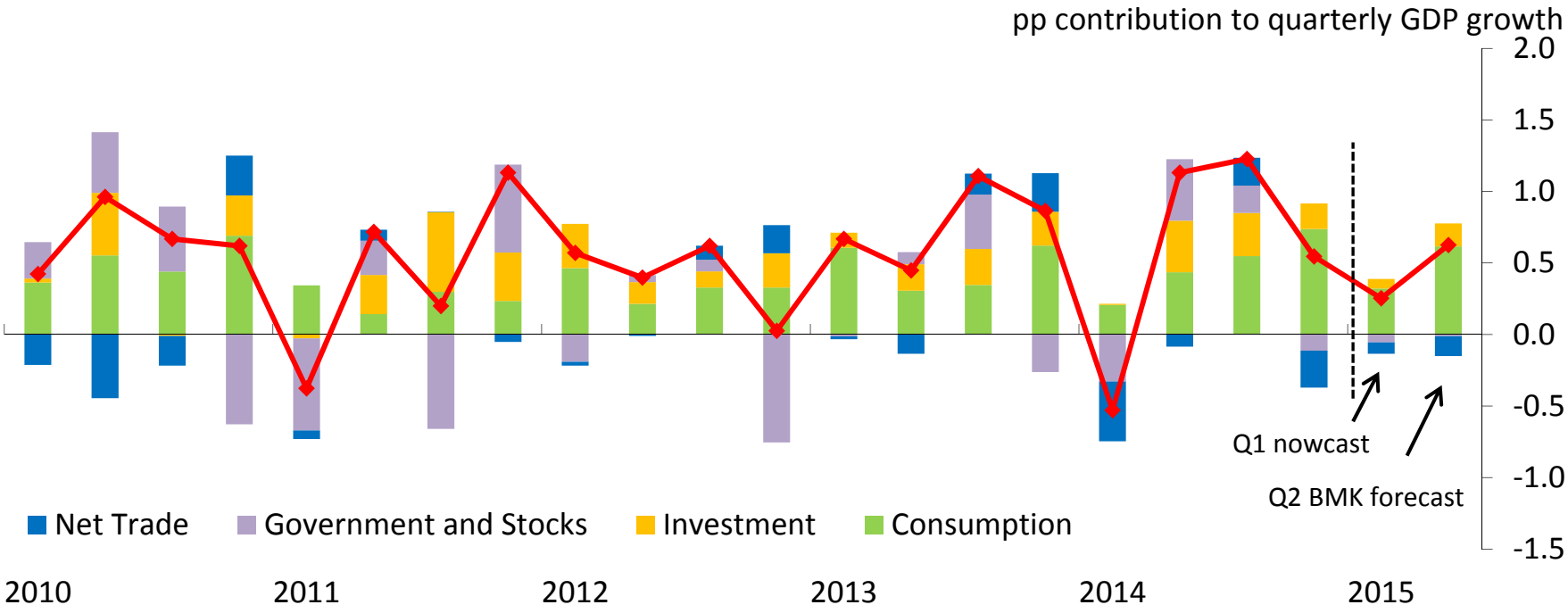
- Headline Q4 GDP unrevised at 0.5%. But consumption strong, contributing 0.7pp to growth.

US consumption



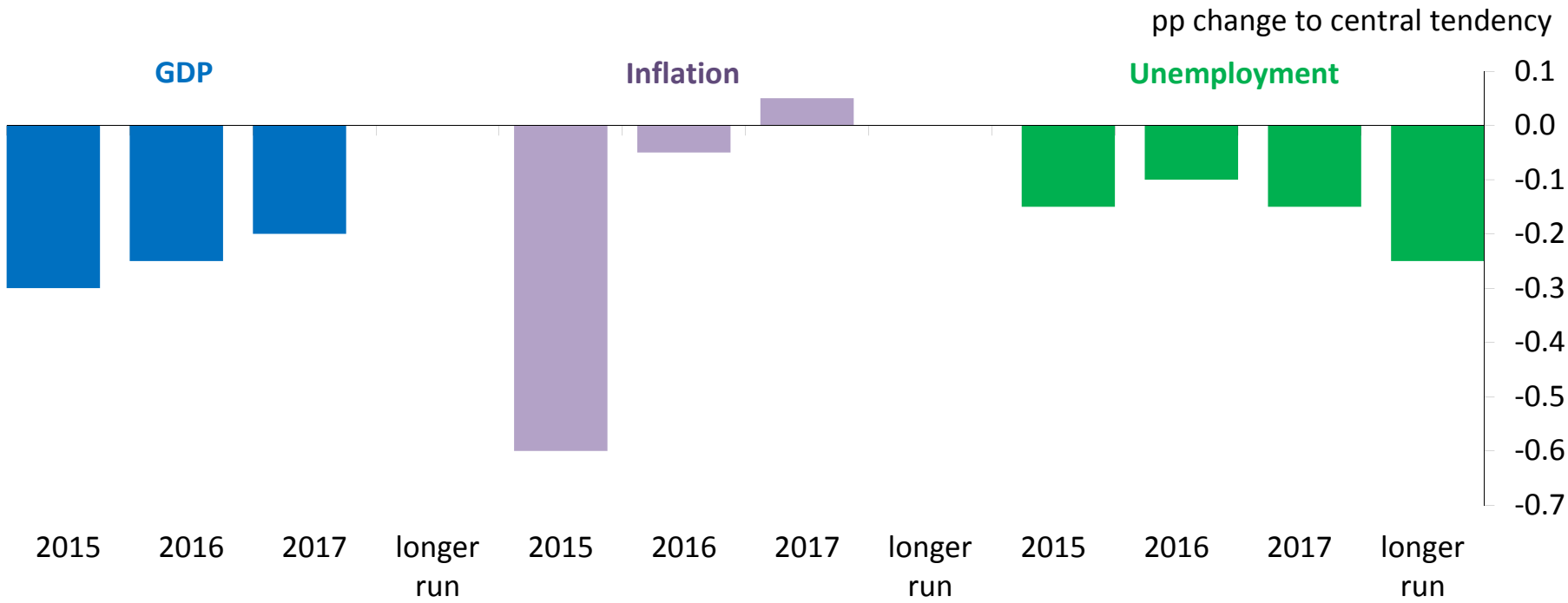
- Consumption indicators look weak in Q1.

US GDP Growth plus H1 forecast



- Q1 nowcast is 0.3%. Q2 forecast is 0.6%.
- Range of external estimates for: Q1 2015 is between 0.2% and 0.5% , and Q2 2015 is between 0.7% and 0.8%.

Summary of March 18th FOMC Meeting



- The FOMC marked down the growth outlook for the next 3 years.
- U* was lowered by slightly more than the unemployment forecast.

Summary of Past US Tightening Schedules

	US Latest
Policy Rate	0.25%
Unemployment Rate (NAIRU)	5.5% (5.5%)
Inflation (core inflation)	0.3% (1.4%)
Wages	2.3%

Summary of Past US Tightening Schedules

	US Latest	US June*	US Sept*
Policy Rate	0.25%		
Unemployment Rate (NAIRU)	5.5% (5.5%)	5.3% (5.4%)	5.1% (5.3%)
Inflation (core inflation)	0.3% (1.4%)	-0.2% (0.8%)	-0.2% (0.9%)
Wages	2.3%	2.7%	3.0%

*M15 BMK Forecast

Summary of Past US Tightening Schedules

Start of tightening cycle	Feb-94	Jun-99	Jun-04	US Latest	US June*	US Sept*
Policy Rate	3.00%	4.75%	1.00%	0.25%		
Unemployment Rate (NAIRU)	6.6% (5.9%)	4.3% (4.9%)	5.6% (5.2%)	5.5% (5.5%)	5.3% (5.4%)	5.1% (5.3%)
Inflation (core inflation)	2.1% (2.3%)	1.4% (1.4%)	2.8% (2.0%)	0.3% (1.4%)	-0.2% (0.8%)	-0.2% (0.9%)
Wages	3.5%	3.1%	3.8%	2.3%	2.7%	3.0%

*M15 BMK Forecast

Summary of Past US Tightening Schedules

Start of tightening cycle	Feb-94	Jun-99	Jun-04	US Latest	US June*	US Sept*
Policy Rate	3.00%	4.75%	1.00%	0.25%		
Unemployment Rate (NAIRU)	6.6% (5.9%)	4.3% (4.9%)	5.6% (5.2%)	5.5% (5.5%)	5.3% (5.4%)	5.1% (5.3%)
Inflation (core inflation)	2.1% (2.3%)	1.4% (1.4%)	2.8% (2.0%)	0.3% (1.4%)	-0.2% (0.8%)	-0.2% (0.9%)
Wages	3.5%	3.1%	3.8%	2.3%	2.7%	3.0%

*M15 BMK Forecast

Summary of Past US Tightening Schedules

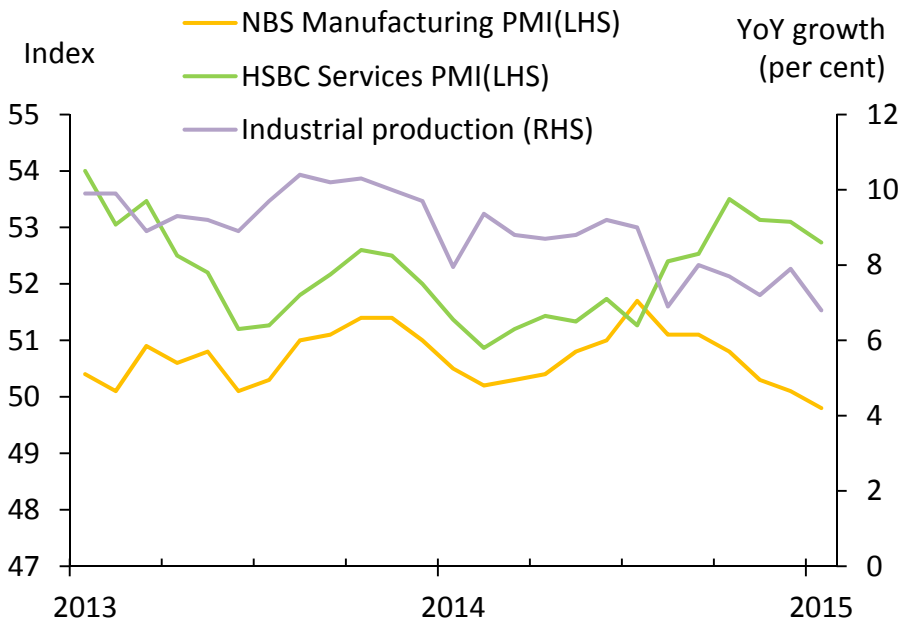
Start of tightening cycle	Feb-94	Jun-99	Jun-04	US Feb	UK Feb
Policy Rate	3.00%	4.75%	1.00%	0.25%	0.50%
Unemployment Rate (NAIRU)	6.6% (5.9%)	4.3% (4.9%)	5.6% (5.2%)	5.5% (5.5%)	5.7%* (5.3%)
Inflation (core inflation)	2.1% (2.3%)	1.4% (1.4%)	2.8% (2.0%)	0.3% (1.4%)	0.0%** (1.2%)
Wages	3.5%	3.1%	3.8%	2.3%	1.8%***

* 3 months to January.
** US inflation series used is February PCE inflation, compared to February CPI inflation for the UK.
*** US wages measure used is Q4 ECI, compared to AWE for the 3 months to January for the UK.

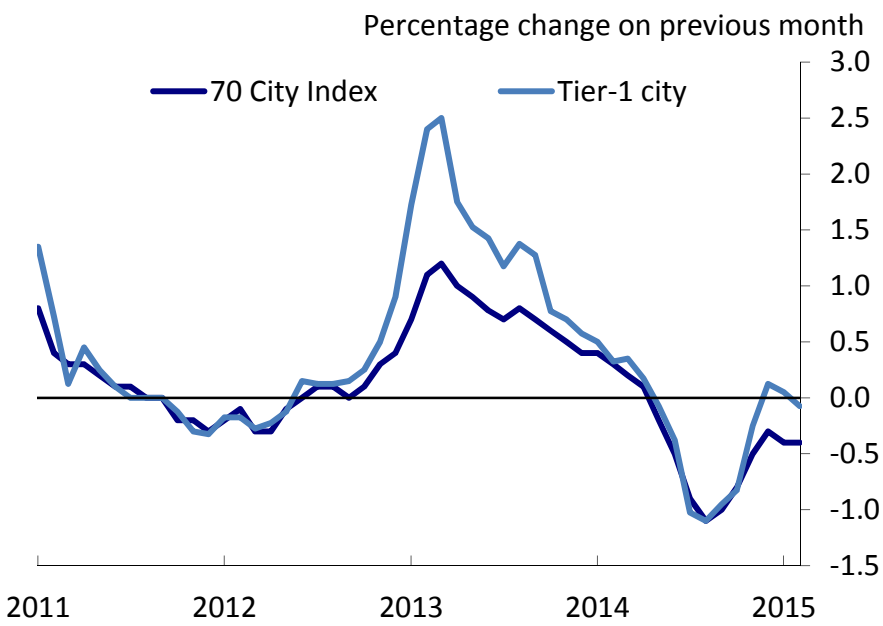
China

China: Activity and property

Activity indicators

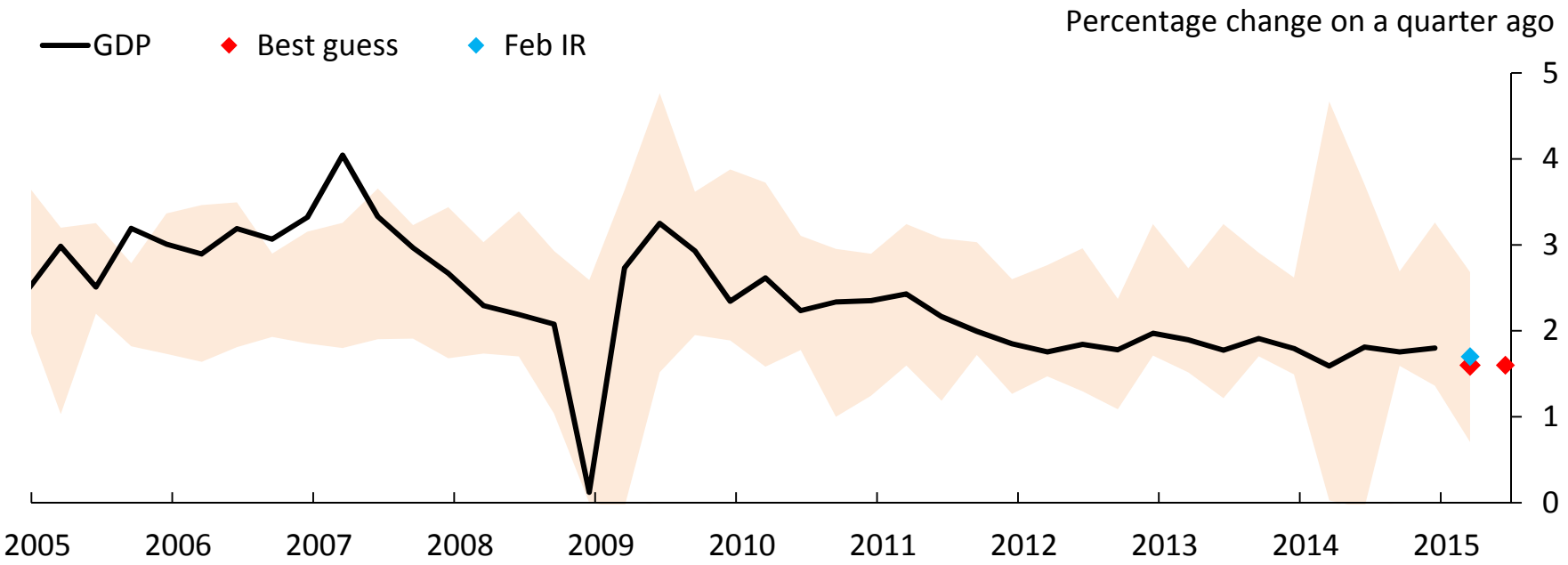


Property prices



- IP has continued to trend downwards, while both manufacturing and services PMIs have also fallen.
- Property market stabilisation is now slightly more in doubt.

China: GDP



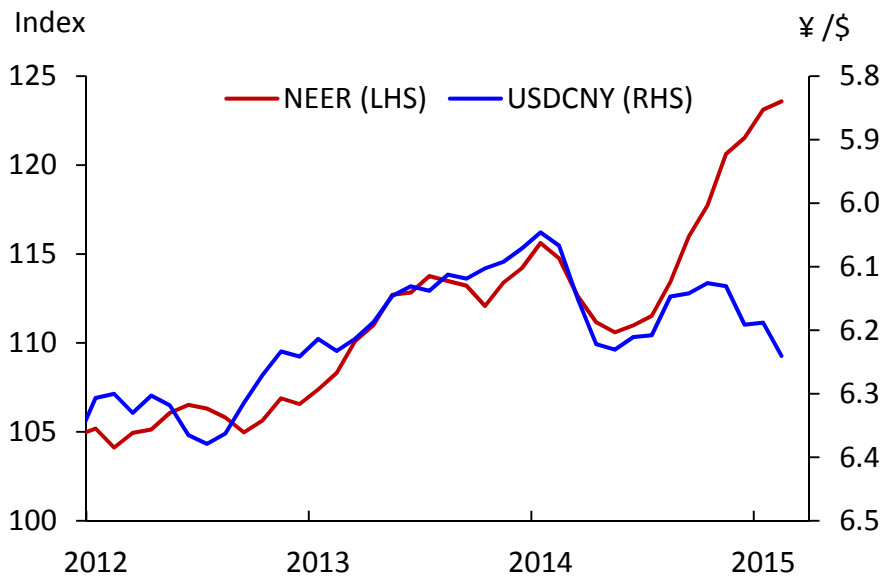
- Near-term indicators are more difficult to interpret due to the New Year effect…
- … but those available have shifted down notably, particularly those we place the most weight on.
- We have revised down Q1 Nowcast to 1.6% and Q2 to 1.6%.

China's NPC and policy stance

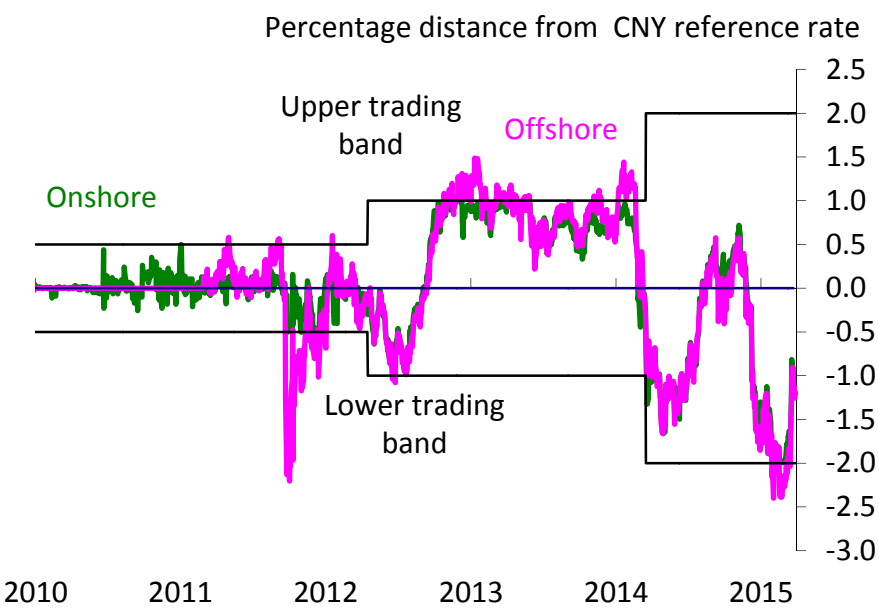
- The **growth target** was lowered to 'about 7.0%' in 2015. And the **inflation target** was lowered to 3%.
- **Fiscal policy:** The government is targeting a budget deficit of 2.3% of GDP, up from last year's 2.1%.
- **Monetary policy:** Since the beginning of 2015, the PBoC has cut both the lending and deposit rates to 5.35% and 2.5%, and cut the RRR by 50bp across the board. We expect further loosening.
- **Property:** The down payment requirement for second homes cut to 40% (-20pp), and capital-gains tax now exempts sellers who have owned their home for as little as two years (previously 5 years).
- **Local government financing** will move away from LGFV to municipal bond issuance this year.
- **Financial reform** appears to be gathering momentum. Deposit insurance will start on 1st May. PBoC Governor Zhou suggested deposit rate liberalisation could happen this year, while the timing of capital account convertibility has likely been brought forward. **FX strategy likely to change only incrementally.**

China FX strategy

Divergence between USD-CNY and NEER



CNY and CNH moves relative to mid-point fix



- The depreciation pressure on USD-CNY and strength of the NEER led to speculation that the PBoC may change FX strategy, for example towards a trade-weighted basket of currencies.
- However, since March, depreciation pressure on USD-CNY has waned.

China FX options

1) Maintain stability of RMB vis-à-vis USD and potentially widen the band

- This is the most likely option: avoids large exchange rate swings and is consistent with inclusion of RMB in SDR and with internationalisation. Any widening likely to be modest.

2) Major policy shift that causes substantial depreciation e.g. moving to a trade weighted basket

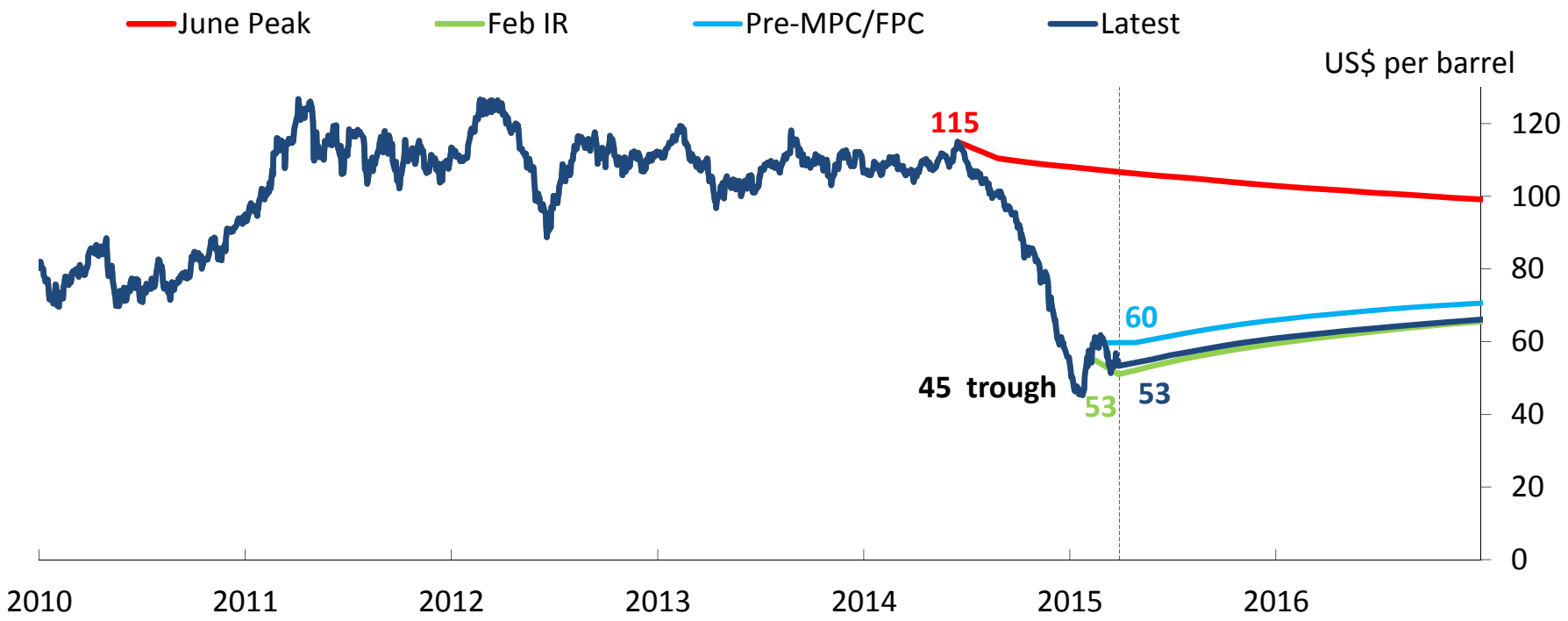
- Would work against internationalisation of the RMB and inclusion within the IMF's SDR.
- But further dollar appreciation and/or China hard landing make this option more likely.

3) A China hard landing including a 10% depreciation is part of the Bank's 2015 stress scenario

- The results will be published alongside the Financial Stability Report in December.

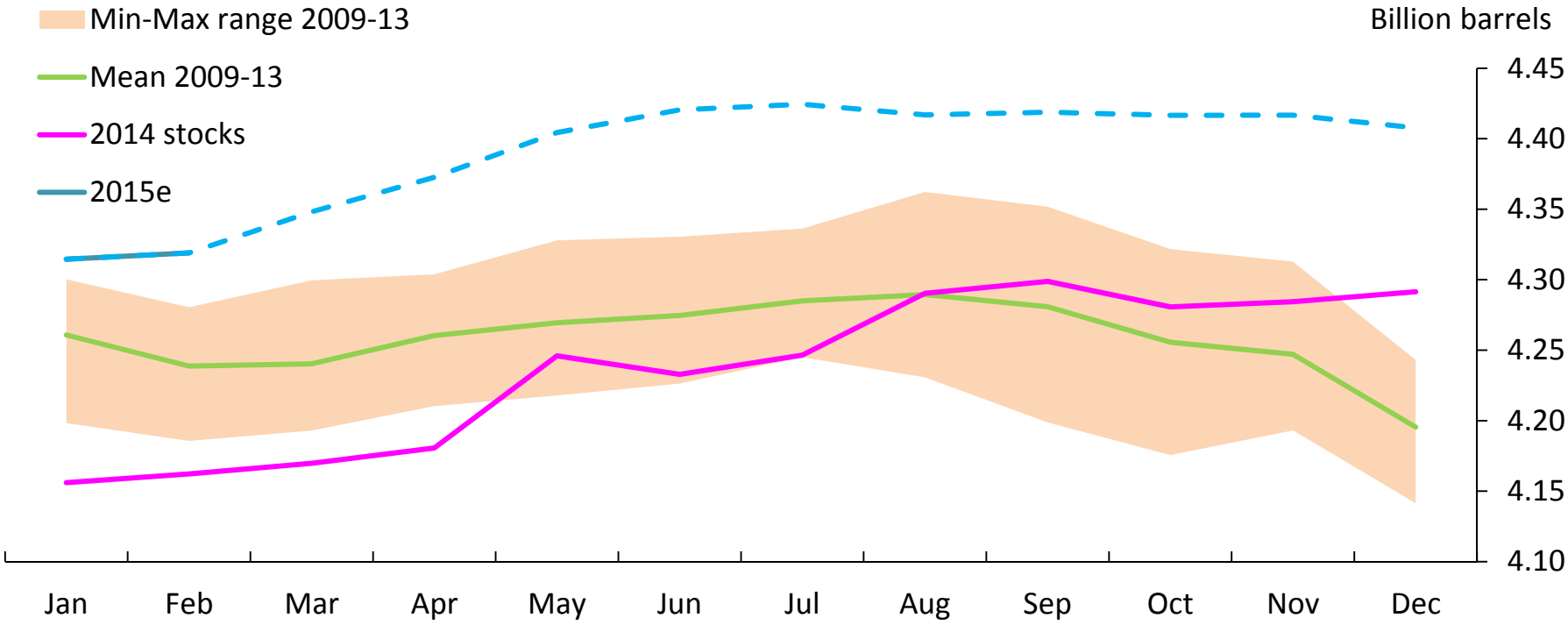
Global (dis)inflation

Oil futures curve



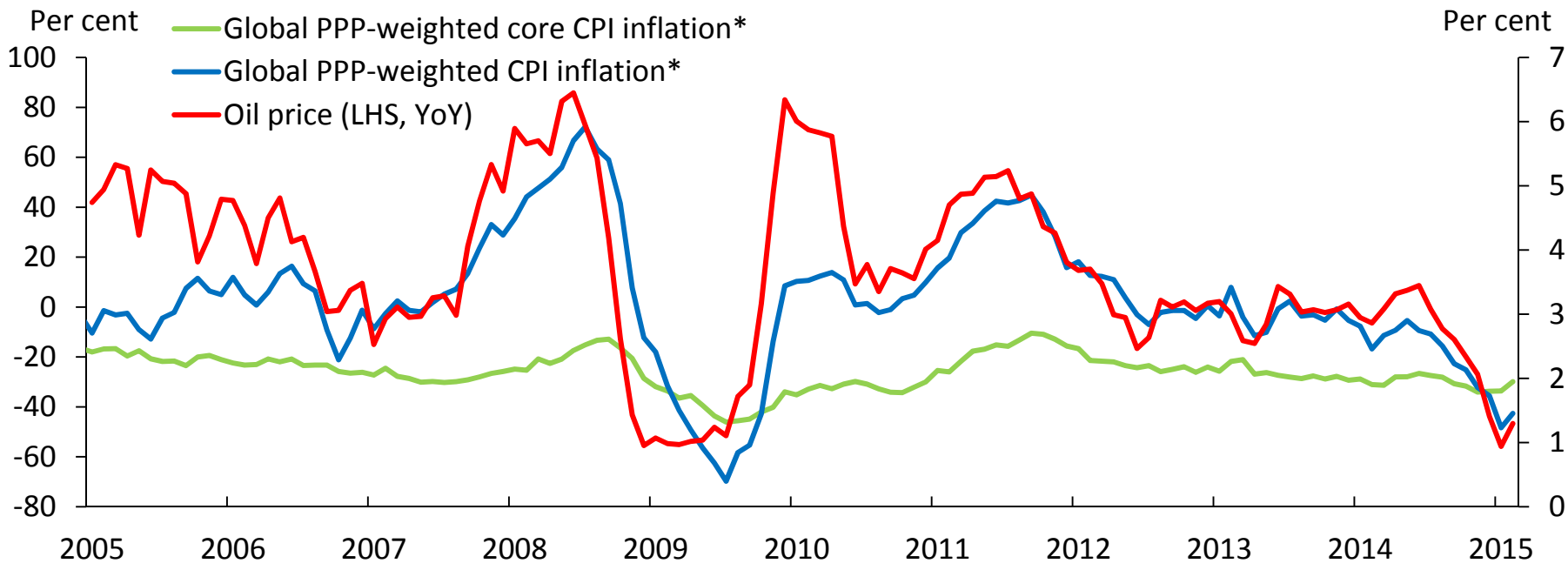
- Oil price fell 10% since pre-MPC/FPC.

OECD oil stock build forecast



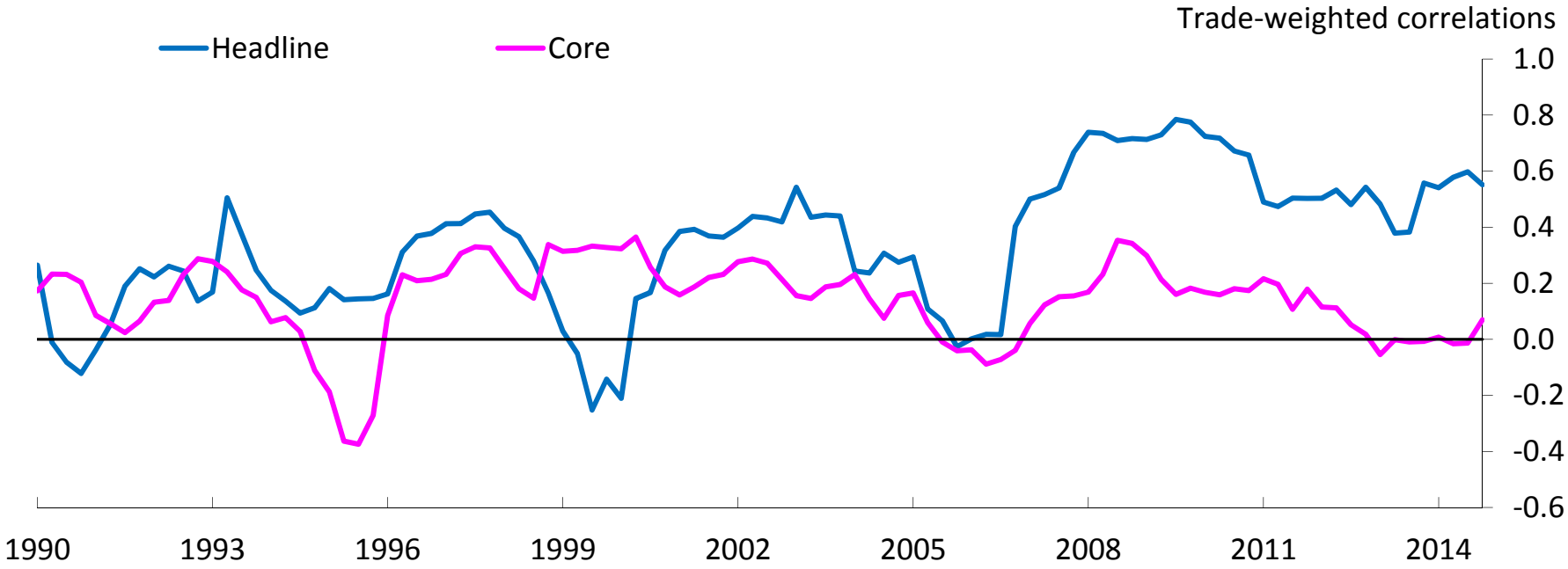
- The OECD oil stock build estimated in 2015 is much higher than the oil stock level over the past 6 years.

Inflation: headline, core and oil



- Average inflation globally ticked up by 0.3pp in Feb, suggesting Jan may have been the trough.
- Inflation remains weak. Indeed, of the 18 central banks with inflation targets, ten now have inflation of less than 1% and five are in deflation.

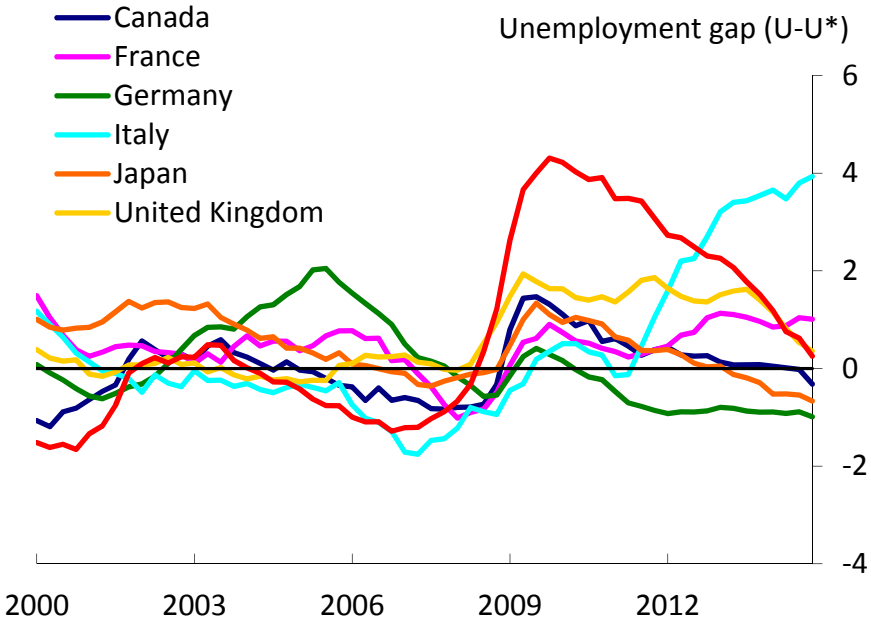
Inflation: correlations of core inflation



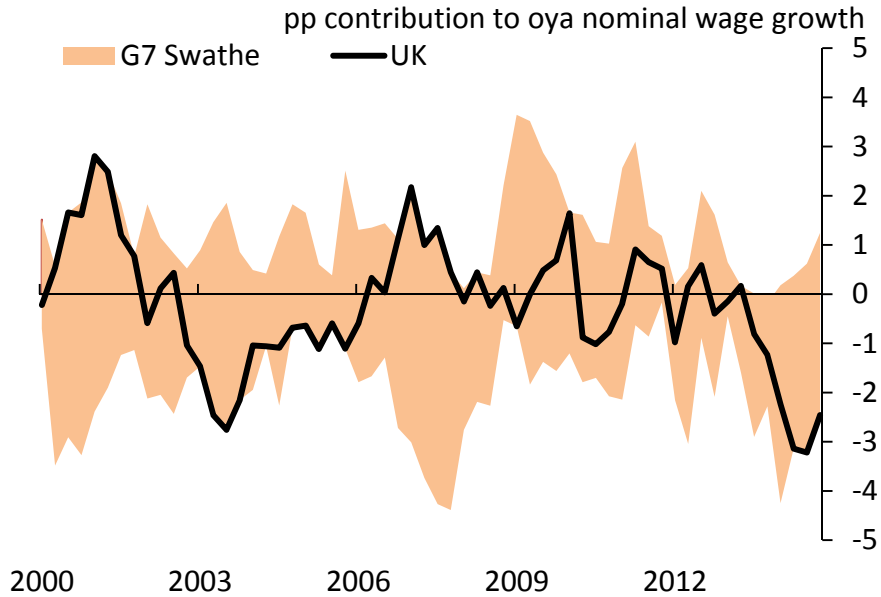
- Correlations of headline inflation rates are high. But these co-movements appear to be predominantly determined by global commodity prices, correlations of core have been getting weaker.
- Core inflation rates may be less synchronised but nonetheless important for UK inflation.

G7 unemployment gaps and wage equations

G7 unemployment gaps



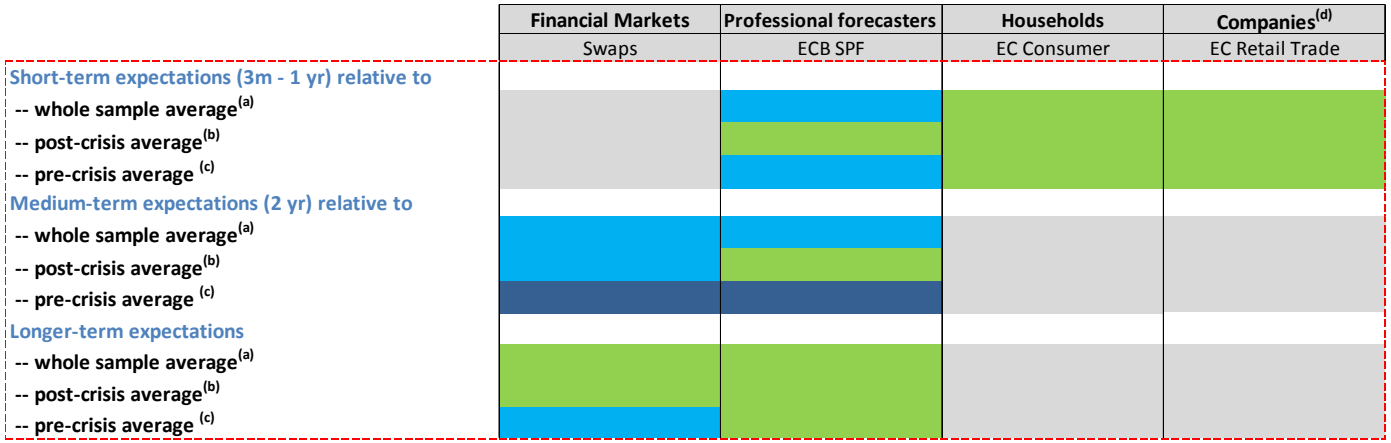
G7 wage equation residuals



- Labour market slack has eroded in several large advanced economies.
- Wage equations attempting to control for labour market slack and other factors, such as productivity, cannot completely account for the current weakness in wage growth in the G7.

Euro-area inflation expectations heatmap

March 2014



Key for π^e levels

- More than 2 SD above
- More than 1 SD above
- Within 1 SD
- More than 1 SD below
- More than 2 SD below

(a) Whole sample average is between the start of each series and 2014Q4

(b) Post-crisis average is between 2009Q1 and 2014Q4

(c) Pre-crisis average is between the start of the series and 2007Q4.

(d) The test for EC inflation expectations is run on the distributive trades series, which should be most closely linked to CPI.

Euro-area inflation expectations heatmap

December 2014

	Financial Markets	Professional forecasters	Households	Companies[d]
	Swaps	ECB SPF	EC Consumer	EC Retail Trade
Short-term expectations (3m - 1 yr) relative to				
-- whole sample average[a]				
-- post-crisis average[b]				
-- pre-crisis average [c]				
Medium-term expectations (2 yr) relative to				
-- whole sample average[a]				
-- post-crisis average[b]				
-- pre-crisis average [c]				
Longer-term expectations				
-- whole sample average[a]				
-- post-crisis average[b]				
-- pre-crisis average [c]				

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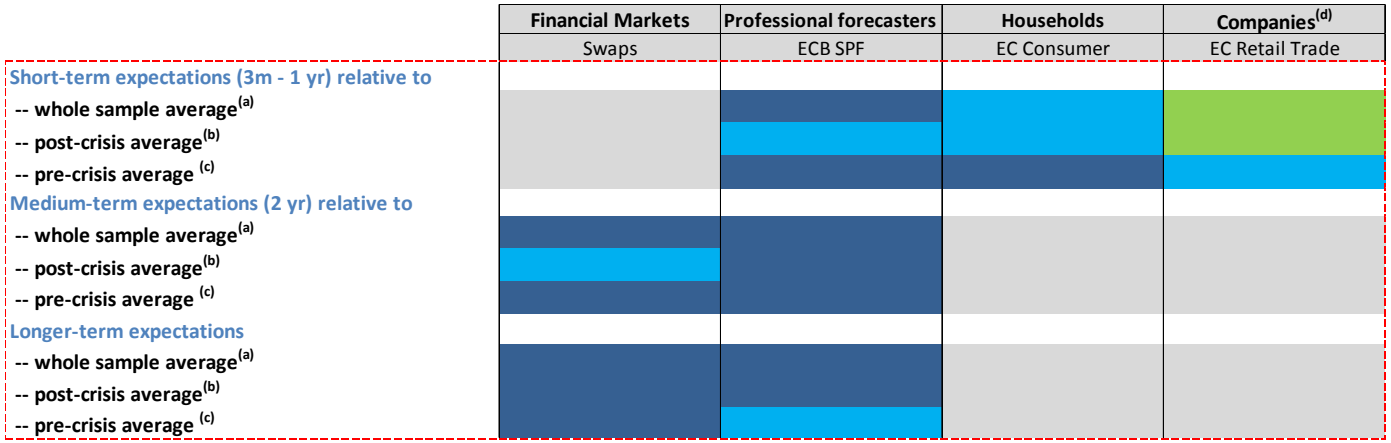
Euro-area inflation expectations heatmap

March 2015



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(c) Pre-crisis average is between the start of the series and 2007Q4.

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US Inflation Expectations Heat Map

March 2014

	Financial Markets	Professional forecasters		Households		Companies	
	Swaps	Professional forecasters survey	Cleveland Fed	Michigan Survey	Conference Board	ISM Mfg	ISM Non-Mfg
Short-term expectations (1 yr) relative to							
-- whole sample average[a]							
-- post-crisis average[b]							
-- pre-crisis average [c]							
Medium-term expectations (3 yr) relative to							
-- whole sample average[a]							
-- post-crisis average[b]							
-- pre-crisis average [c]							
Longer-term expectations							
-- whole sample average[a]							
-- post-crisis average[b]							
-- pre-crisis average [c]							

Key for π^e levels

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(c) Pre-crisis average is between the start of the series and 2007Q4.

US Inflation Expectations Heat Map

March 2015

	Financial Markets	Professional forecasters		Households		Companies	
	Swaps	Professional forecasters survey	Cleveland Fed	Michigan Survey	Conference Board	ISM Mfg	ISM Non-Mfg
Short-term expectations (1 yr) relative to							
-- whole sample average[(a)]							
-- post-crisis average[(b)]							
-- pre-crisis average [(c)]							
Medium-term expectations (3 yr) relative to							
-- whole sample average[(a)]							
-- post-crisis average[(b)]							
-- pre-crisis average [(c)]							
Longer-term expectations							
-- whole sample average[(a)]							
-- post-crisis average[(b)]							
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Key for π^e levels

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(a) Whole sample average is between the start of each series and 2015Q1

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(c) Pre-crisis average is between the start of the series and 2007Q4.

Summary

- **Near-term prospects for activity**
  - Euro area: Q1 and Q2 revised up by 0.1pp: momentum is building
  - US: Q1 revised down by 0.3pp: consumption appears puzzlingly weak
  - China: Q1 and Q2 revised down by 0.1pp: policy support expected
- **Global (dis)inflation**
  - Average inflation across the world remains weak, but may have troughed in Jan
  - Correlations of core inflation rates are very low
  - It is difficult to explain the weakness of wages in the G7
  - Inflation expectations heatmaps look 'cool' in both the EA and US

End

Demand and Output

April 2015

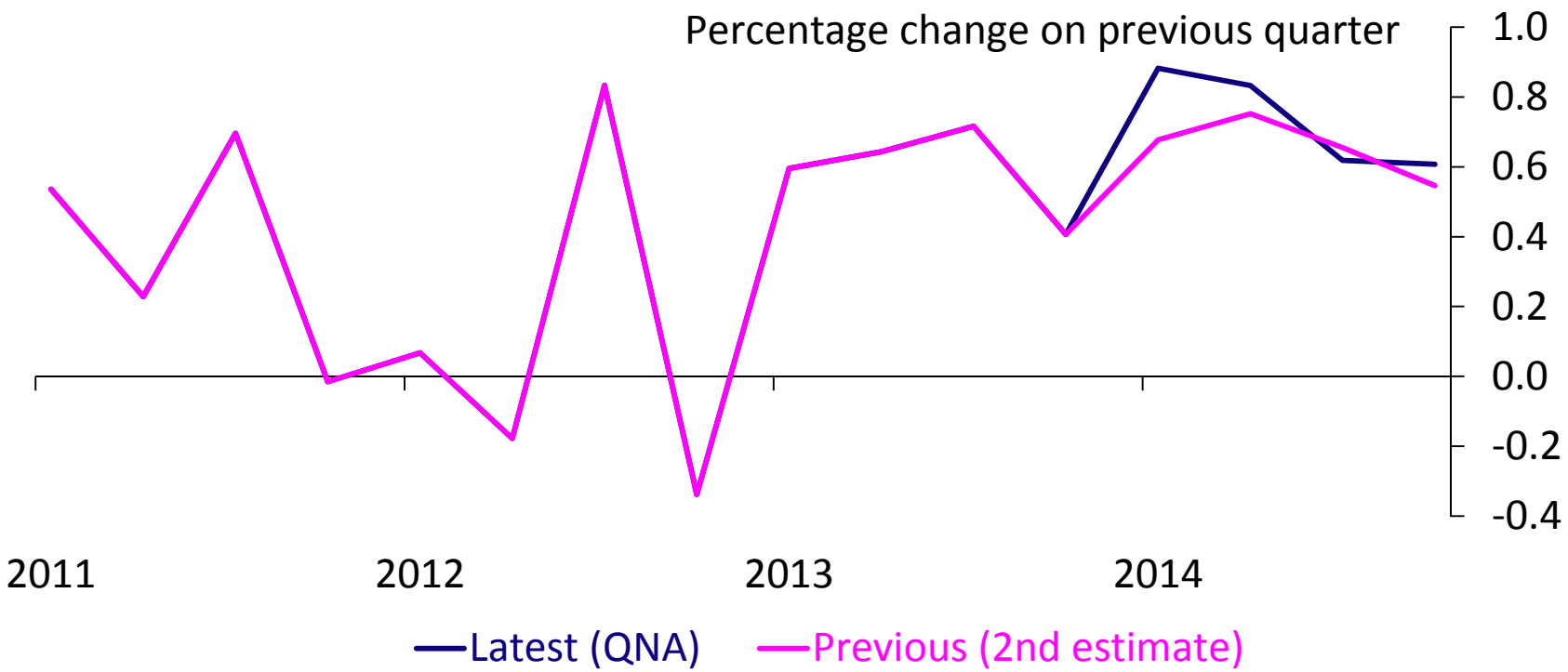
DSI and UK Teams

Outline

1) Update on near term outlook
2) Expenditure news from QNA
3) Prospects for the external sector

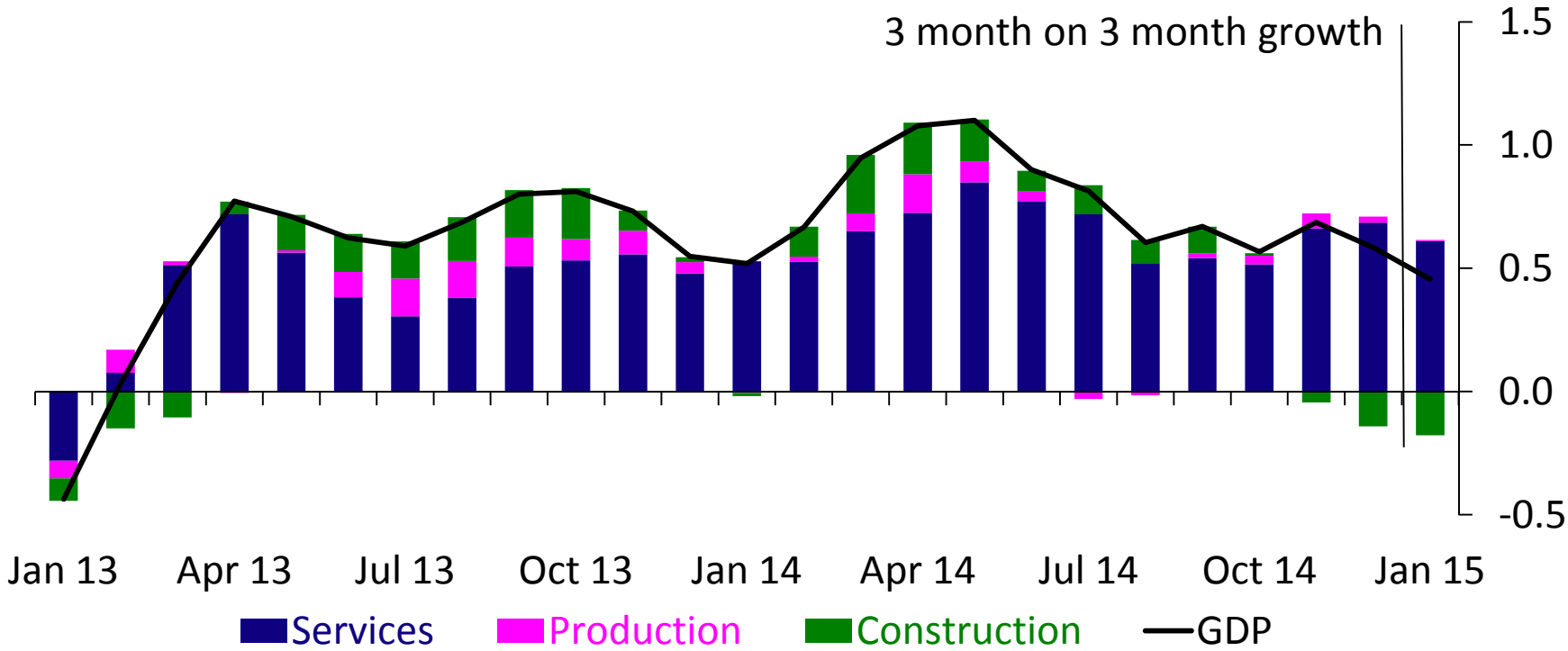
Near term outlook

Real GDP



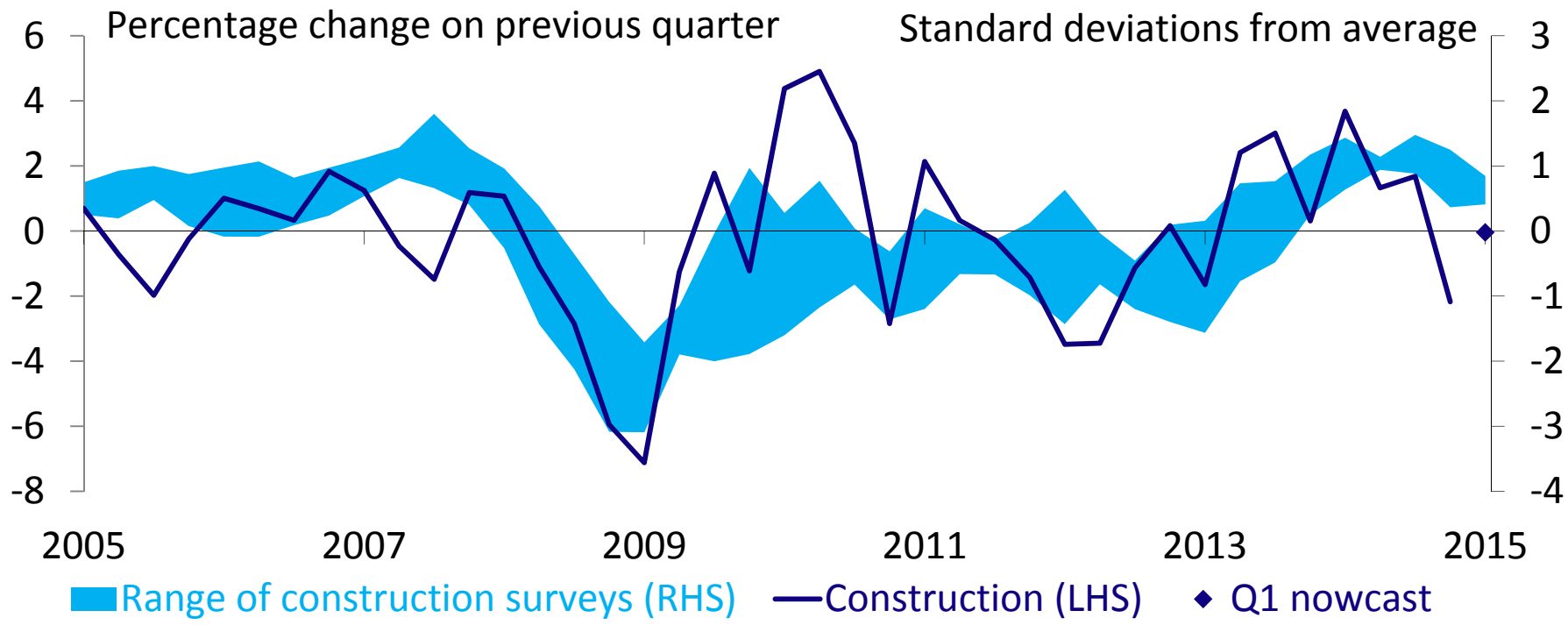
- Data revisions mean calendar year GDP growth in 2014 is now slightly stronger (2.8% vs 2.6%)

Monthly GDP by output



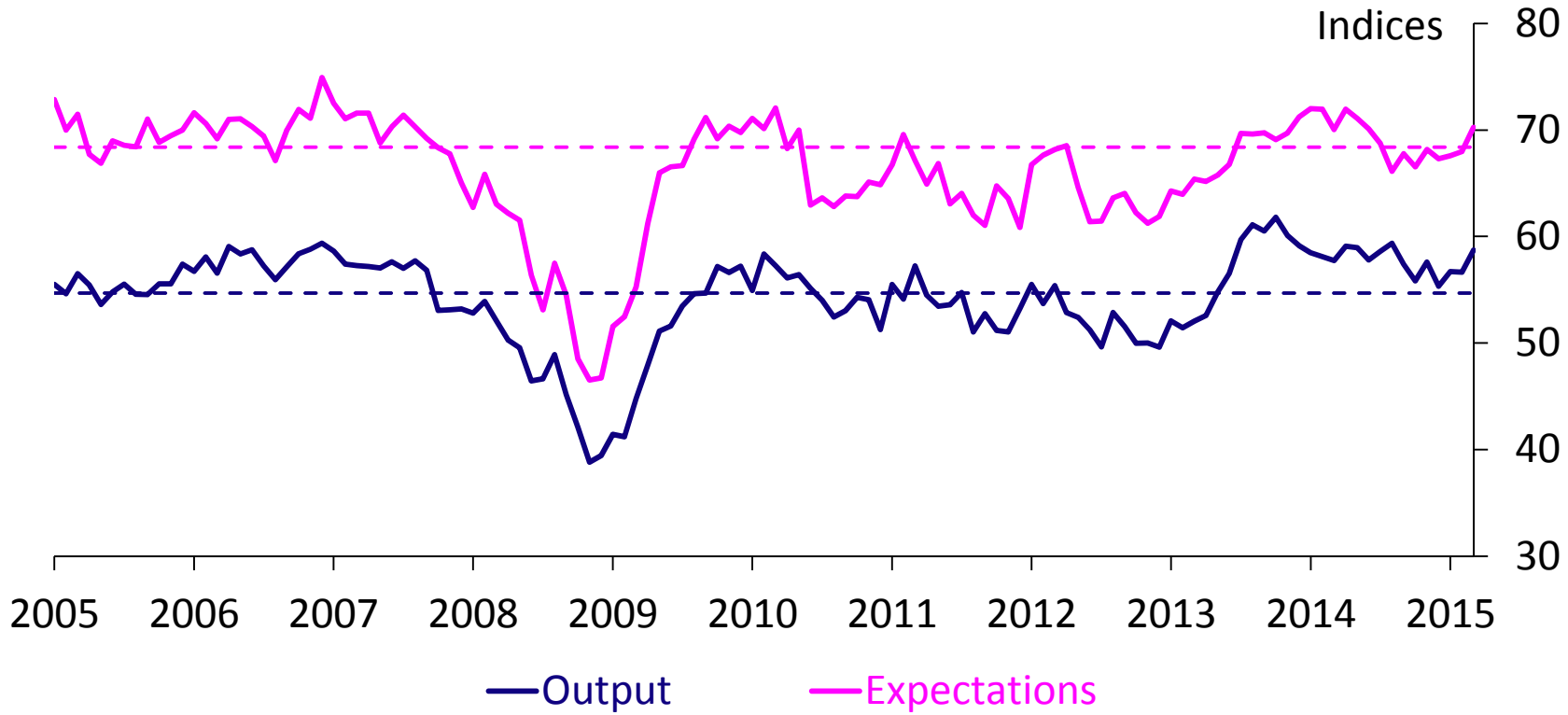
- Service sector output growth slowed in January after strength at the end of 2014

Construction output survey swathe



- The surveys have eased slightly, but have continued to suggest increased activity

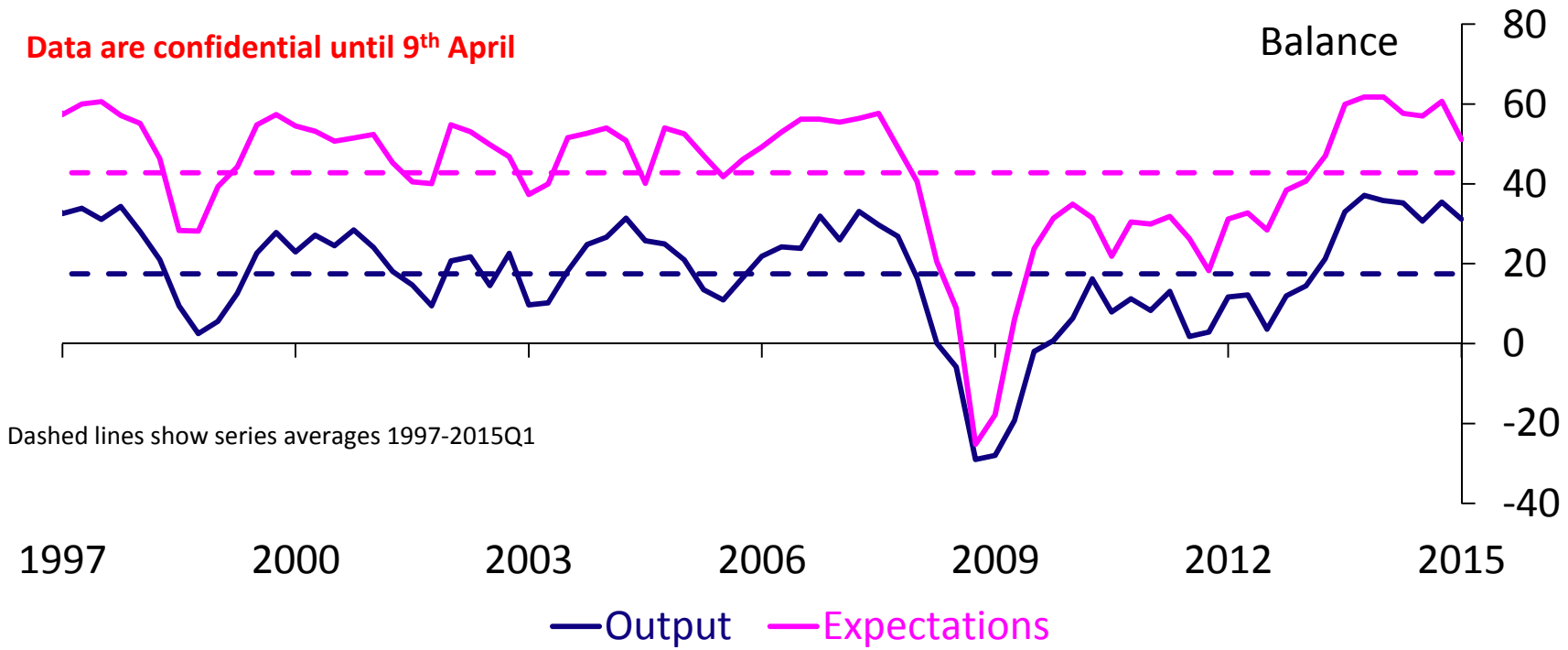
Composite Markit/CIPS output and expectations



Dashed lines show series averages January 1997-Febuary 2015

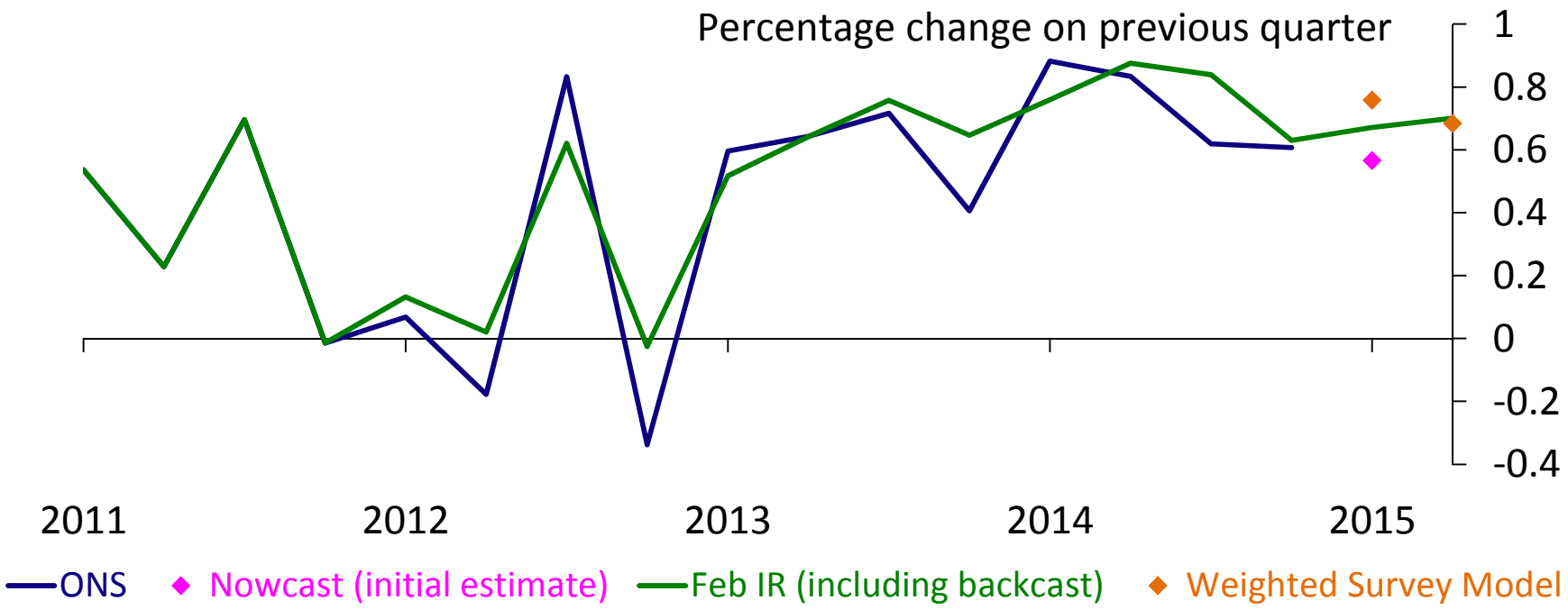
CARE: Confidential and market sensitive. Data are confidential until 9:30am on Tuesday 7th April

BCC composite output and expectations



- Both series fell back in Q4 but are still well above average

Real GDP projections



- Our Q1 nowcast is unchanged since last month, but the weak official January data present downside risks; Q2 still in line with February IR

Expenditure news

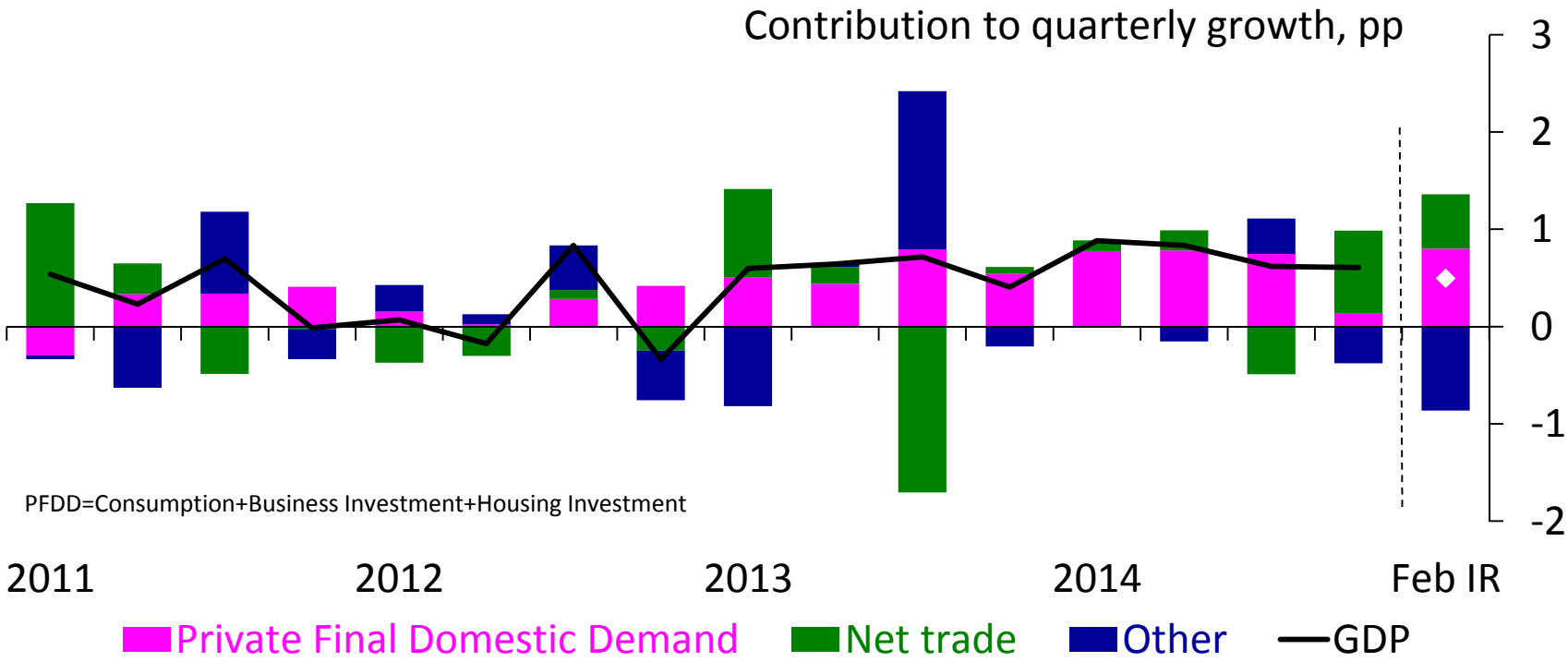
Latest expenditure data (selected components)

Q4 expenditure	Feb IR^	2nd Release	QNA	
	Growth	*Growth*	*Growth*	*Revision*
GDP	0.6	0.5	0.6	0.1
Consumption	0.8	0.3	0.4	0.1*
Investment				
o/w business	2.5	-1.4	-0.9	0.0*
o/w housing	0.6	0.8	-1.1	0.0*
Total stockbuilding*	-0.9	-0.2	-0.5	-0.3
Net trade*	0.6	0.6	0.8	0.2

*contribution to GDP growth

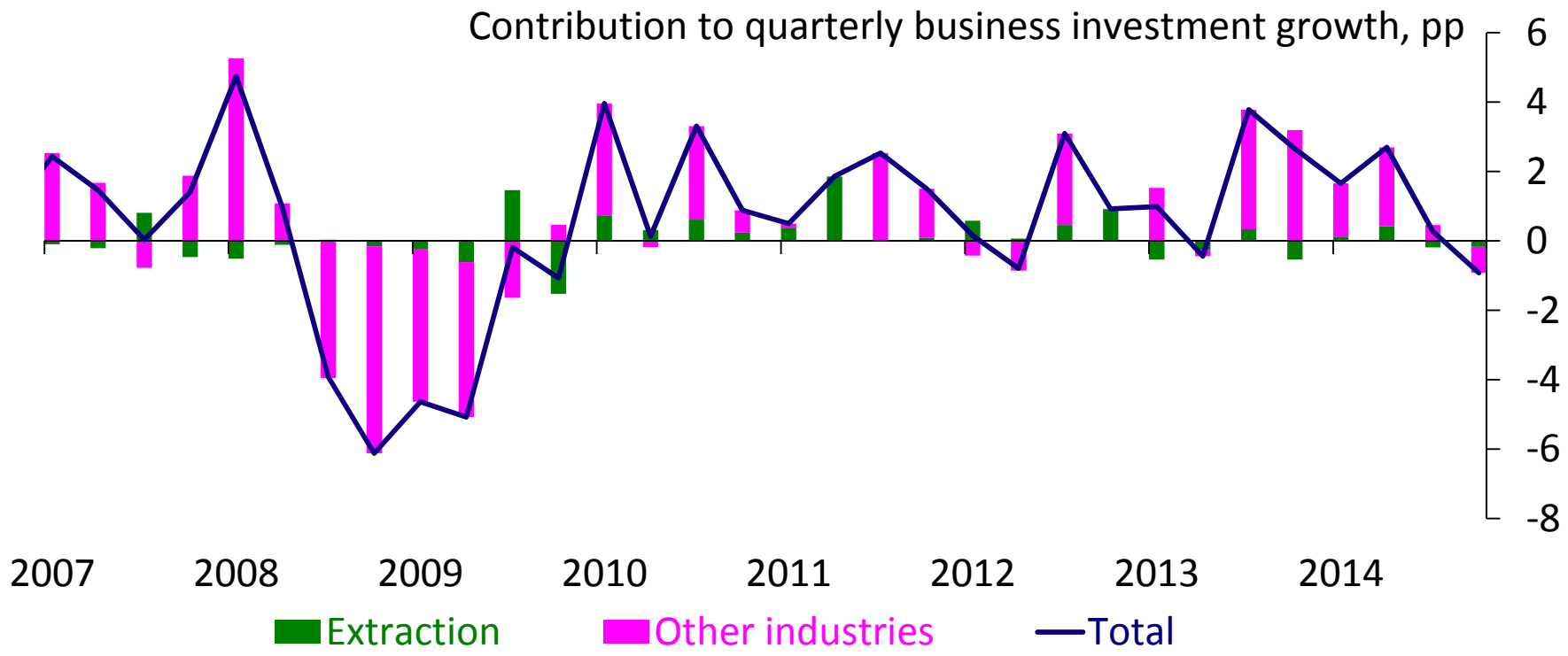
^final estimate

Contributions to quarterly GDP growth



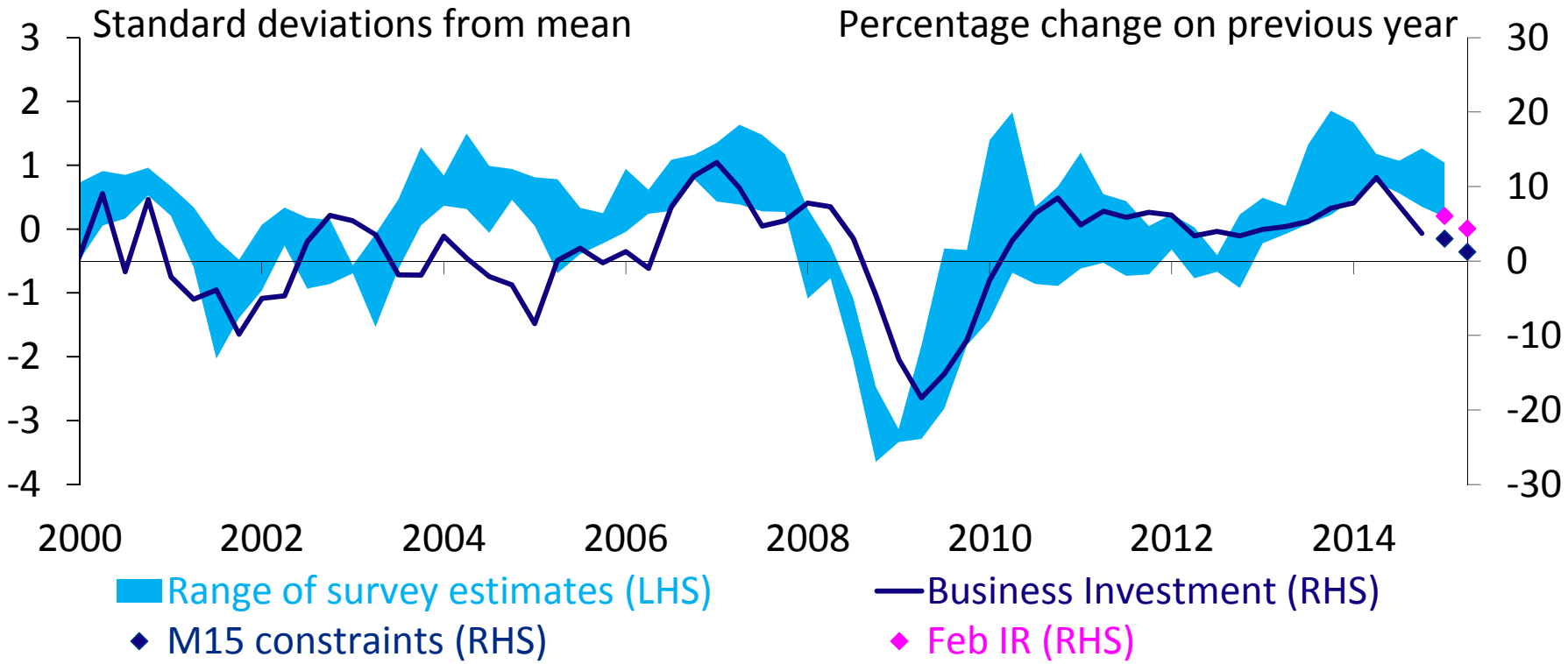
- Significant downside news in Q4 private final domestic demand relative to the Feb IR

Business investment



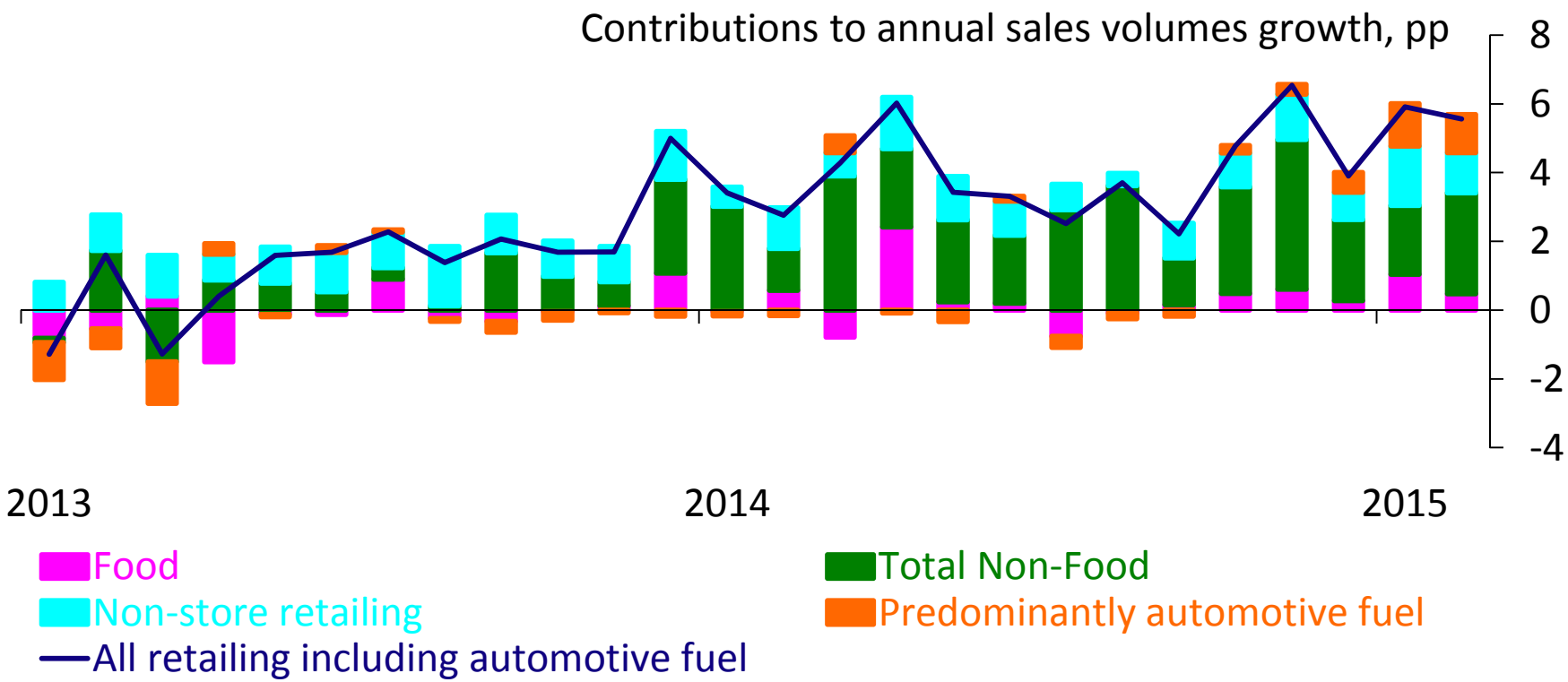
- Revised business investment remains weak in 2014H2 excluding extraction

Business investment and surveys



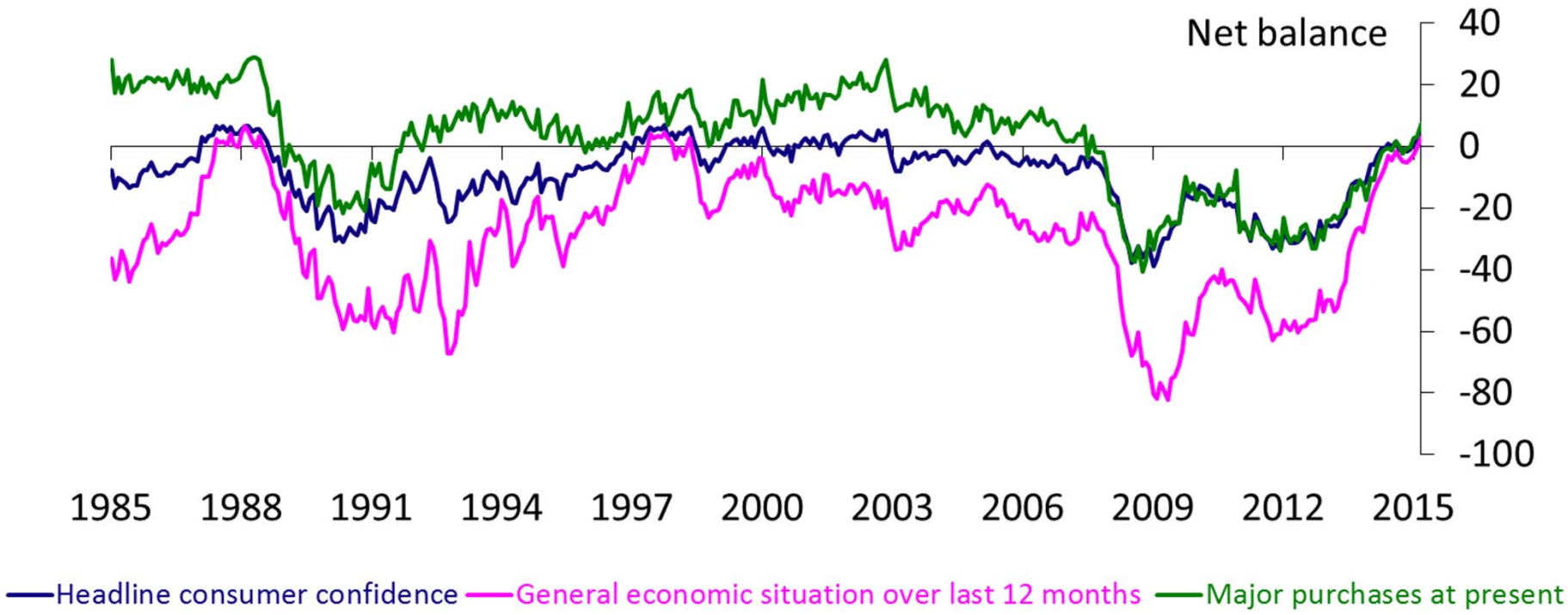
- Latest business investment constraints reflect the weaker official data

Retail sales volumes



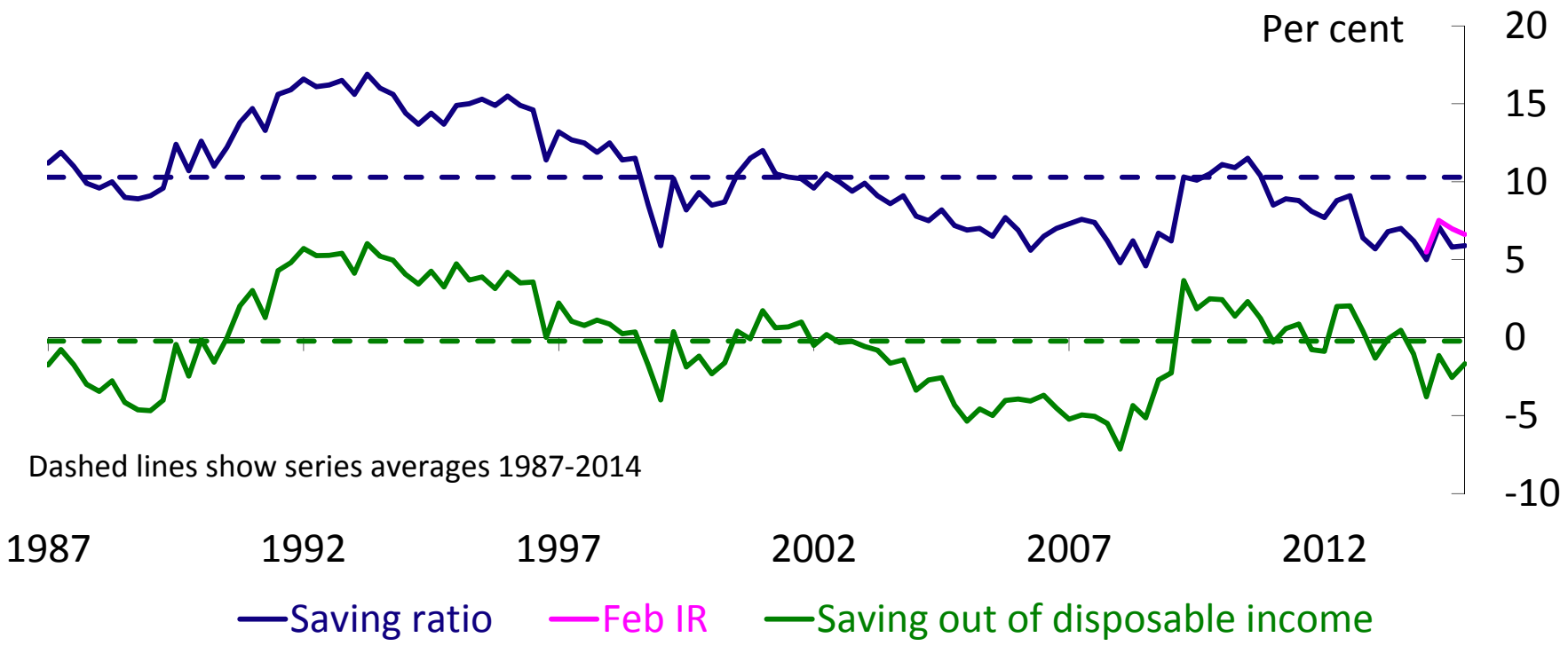
- Strength in retail sales has been broad based

GfK/EC consumer confidence



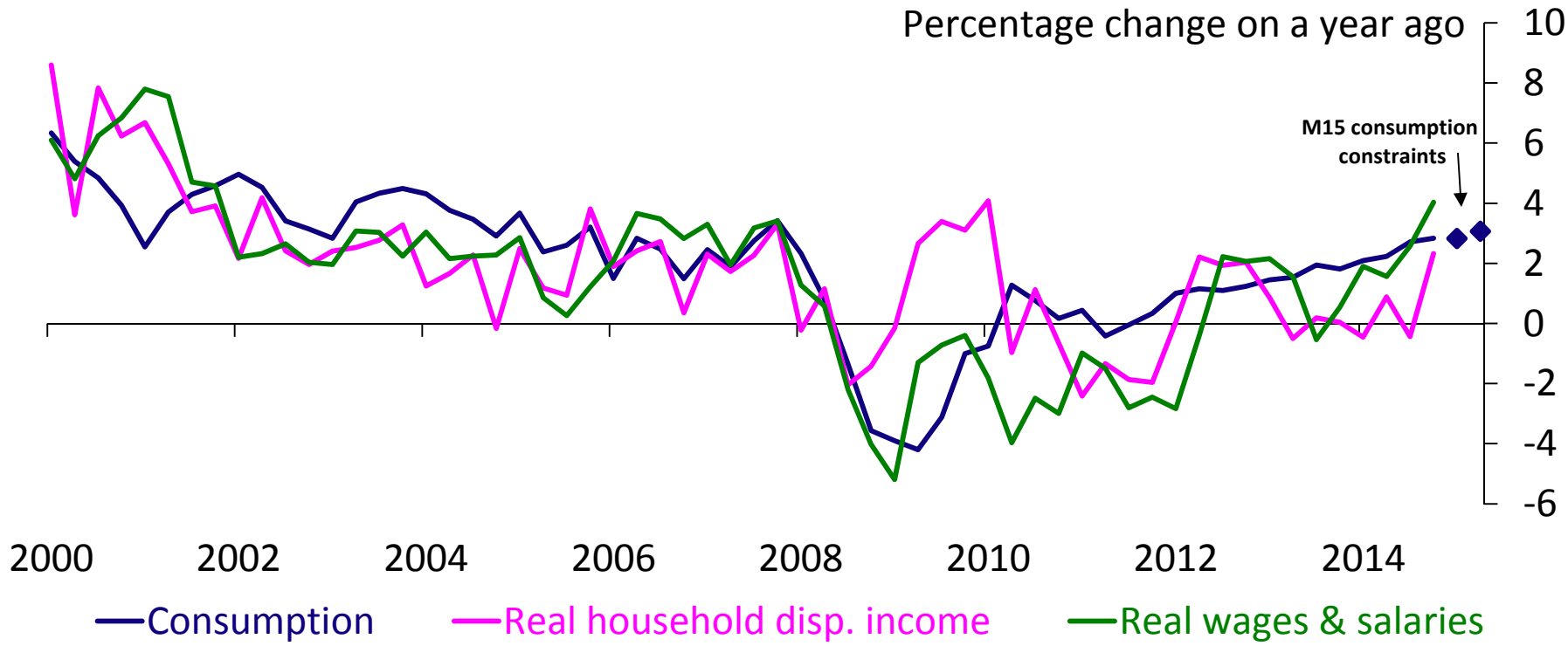
- General economic perceptions are at their highest since late 1997

Household saving



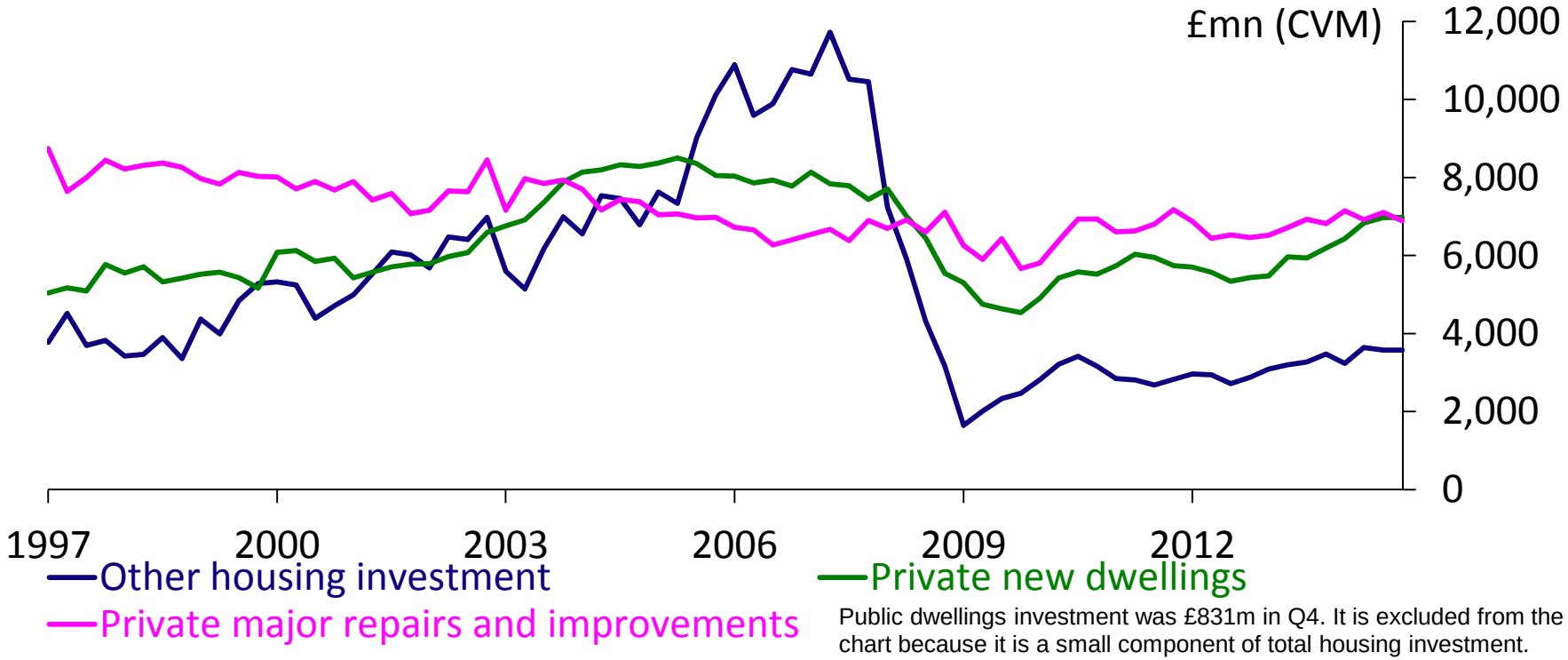
- Both measures of the saving ratio have been broadly flat over the past year

Consumption and real household income



- Real income and consumption growth have been picking up

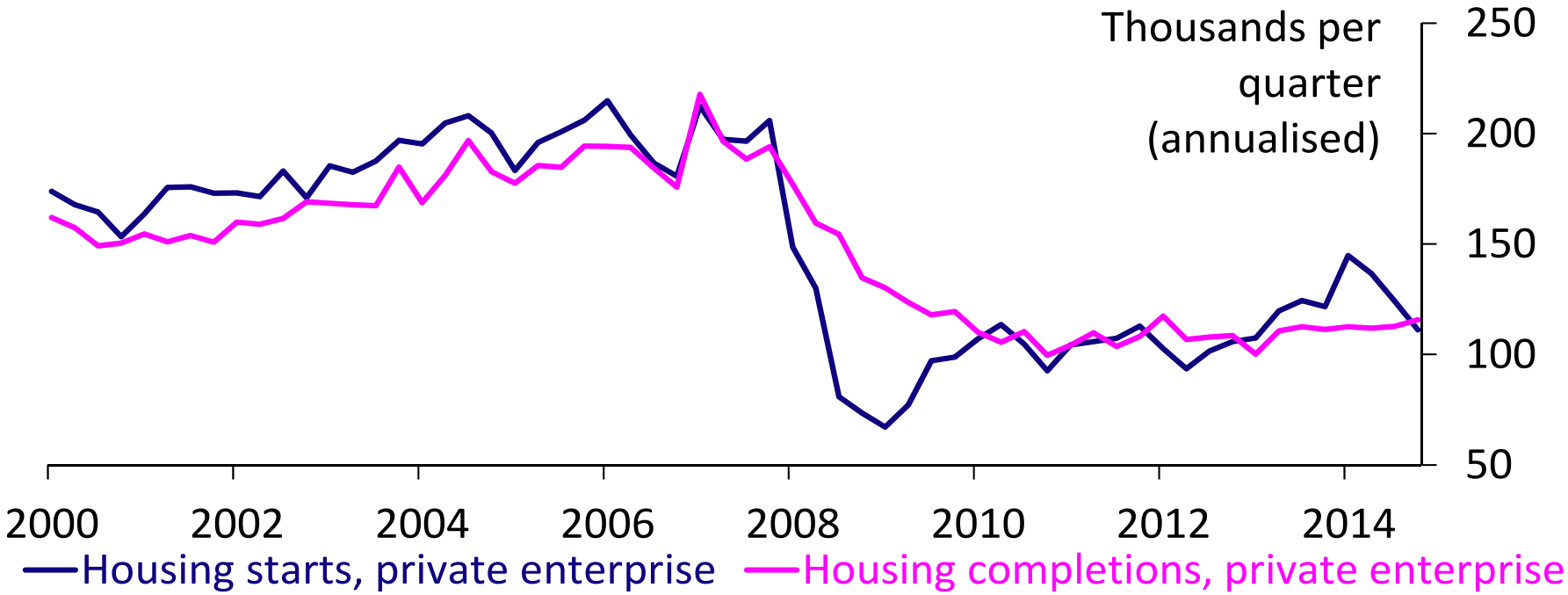
Major housing investment components



Public dwellings investment was £831m in Q4. It is excluded from the chart because it is a small component of total housing investment.

- Private new build investment had been rising strongly until recently

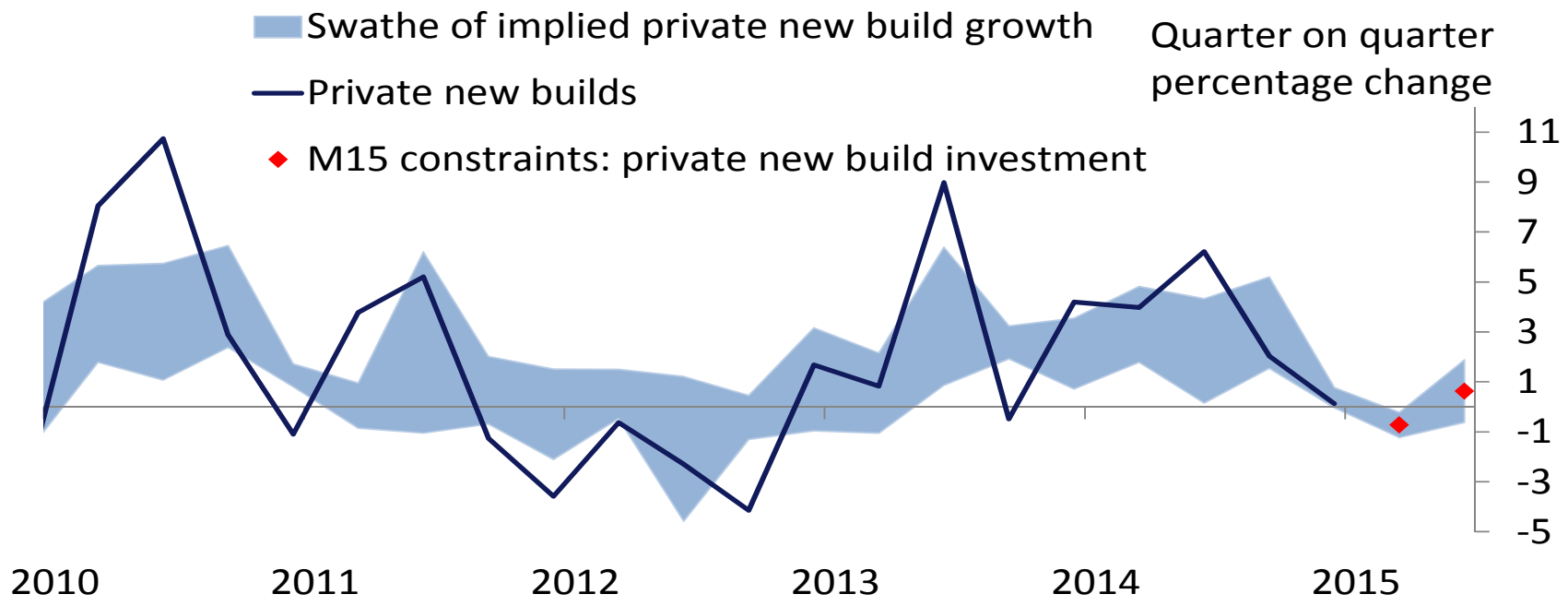
UK private housing starts and completions



Source: DCLG

- Private housing starts have fallen sharply since the beginning of 2014.

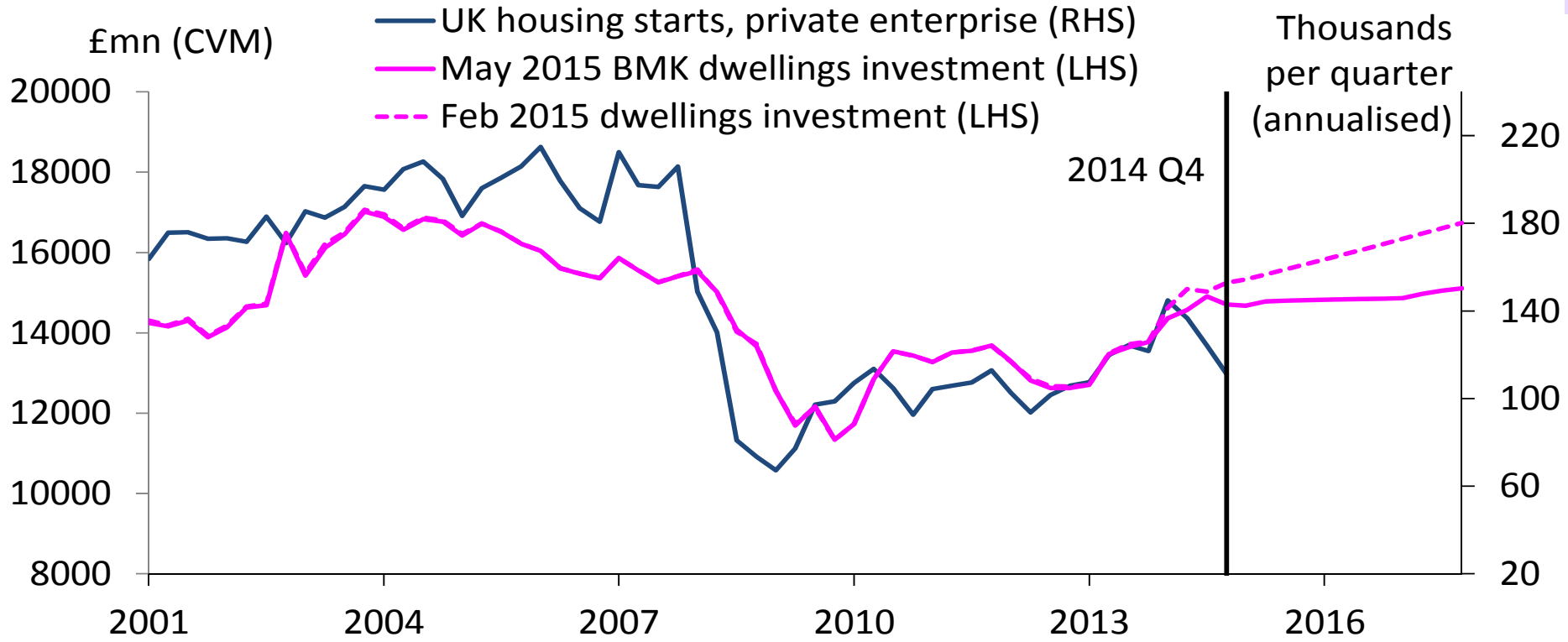
Swathe of private new build investment indicators



The swathe includes private housing starts data, private new construction orders and new housing construction output.

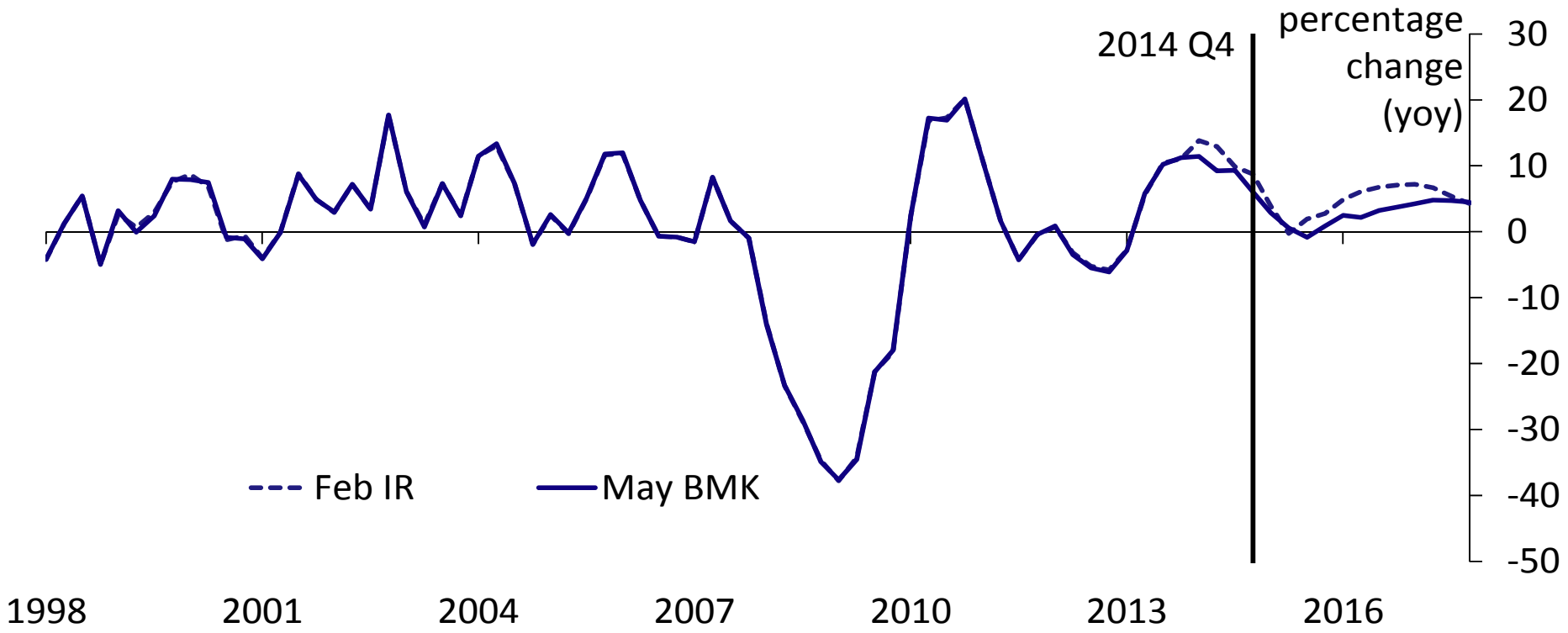
- Lead indicators of private new build investment have been falling.

Dwellings investment and number of new builds



- Our new forecast is consistent with around 150,000 private housing starts by 2018.

Housing investment projections



- Annual growth in housing investment slows over 2015 before picking up to around 4% per year by the end of the forecast.

Monitoring the Key Judgements in the Feb IR

Likely developments in 2015 H1 and 2015 Q3:	Assessment
• Quarterly consumer spending growth of around 1%	Slightly weaker
• Housing investment broadly flat	Slightly weaker
• Average quarterly business investment growth of c1.5%	Slightly weaker

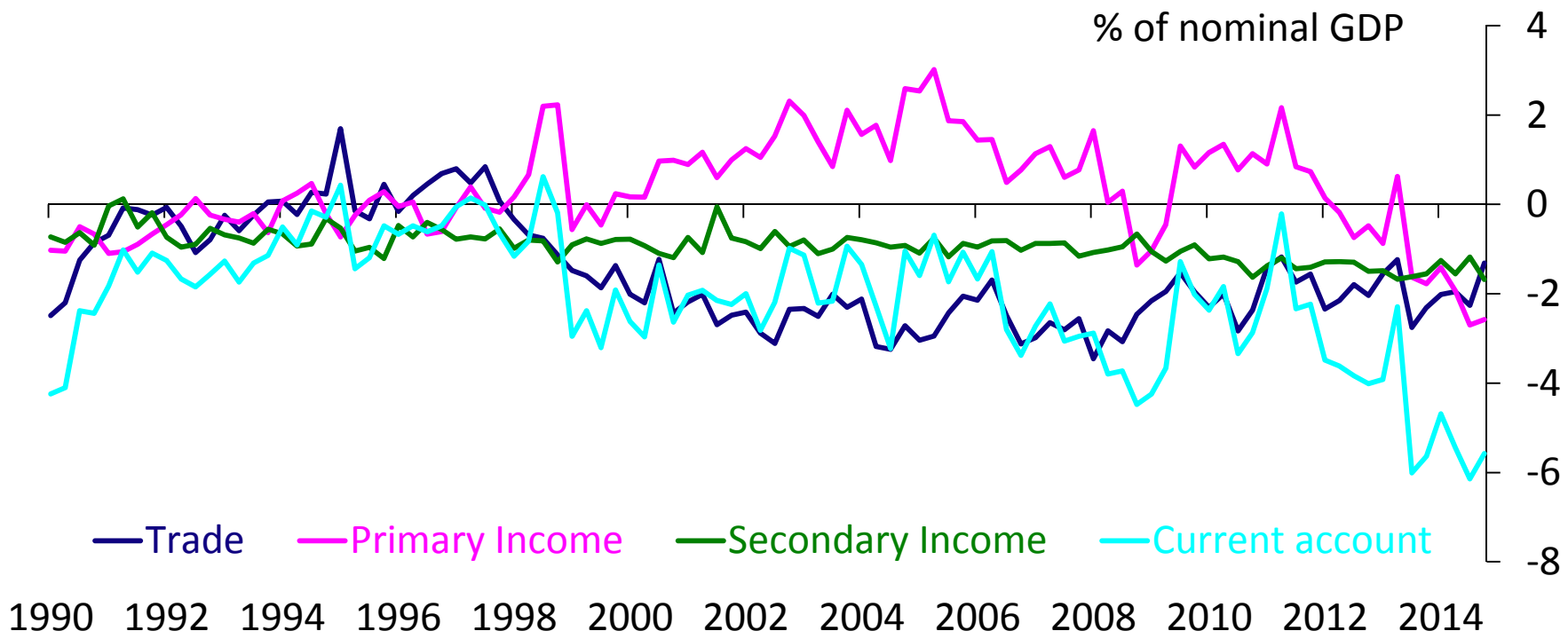
Assessment for consumer spending and business investment only for Q1 and Q2 as estimates for Q3 not available

External sector

External sector key messages

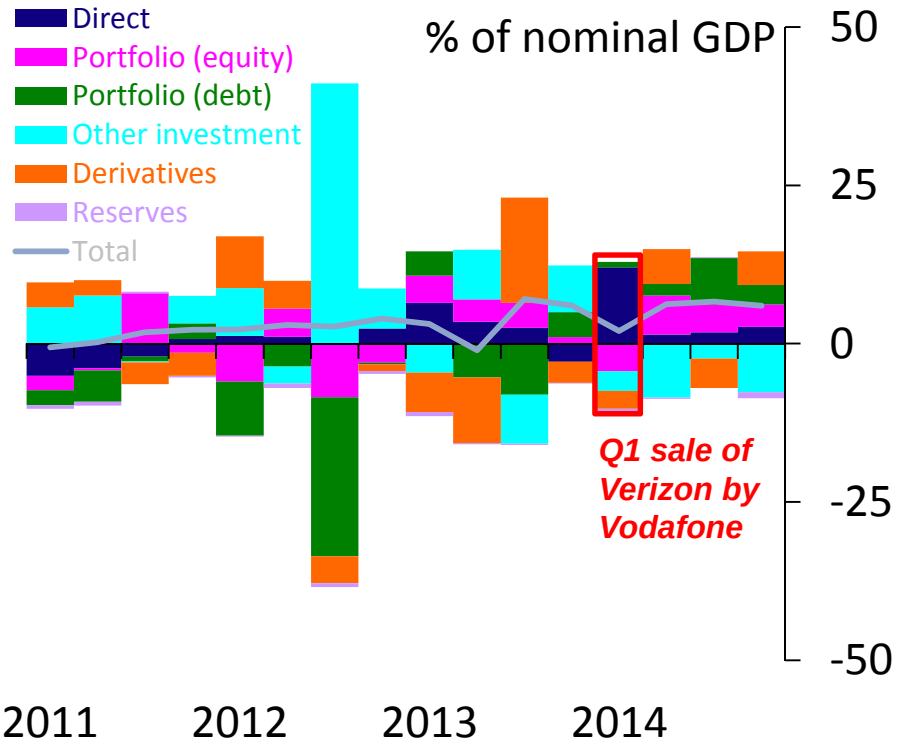
	Key messages
Balance of payments and the real exchange rate	
Latest trade data	
Prospects for exports and net trade	

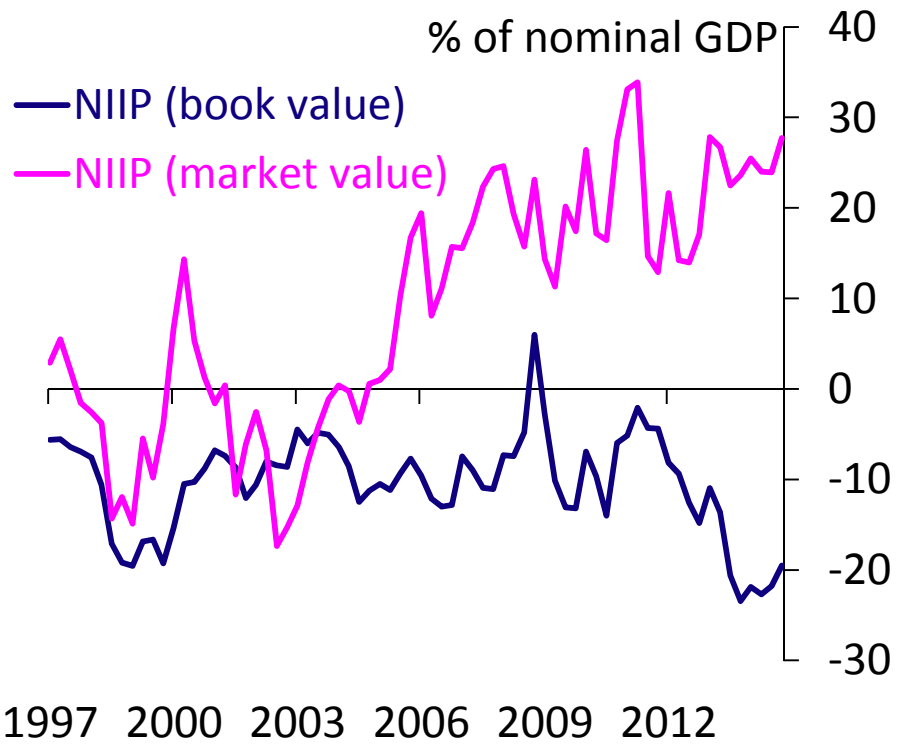
Current account



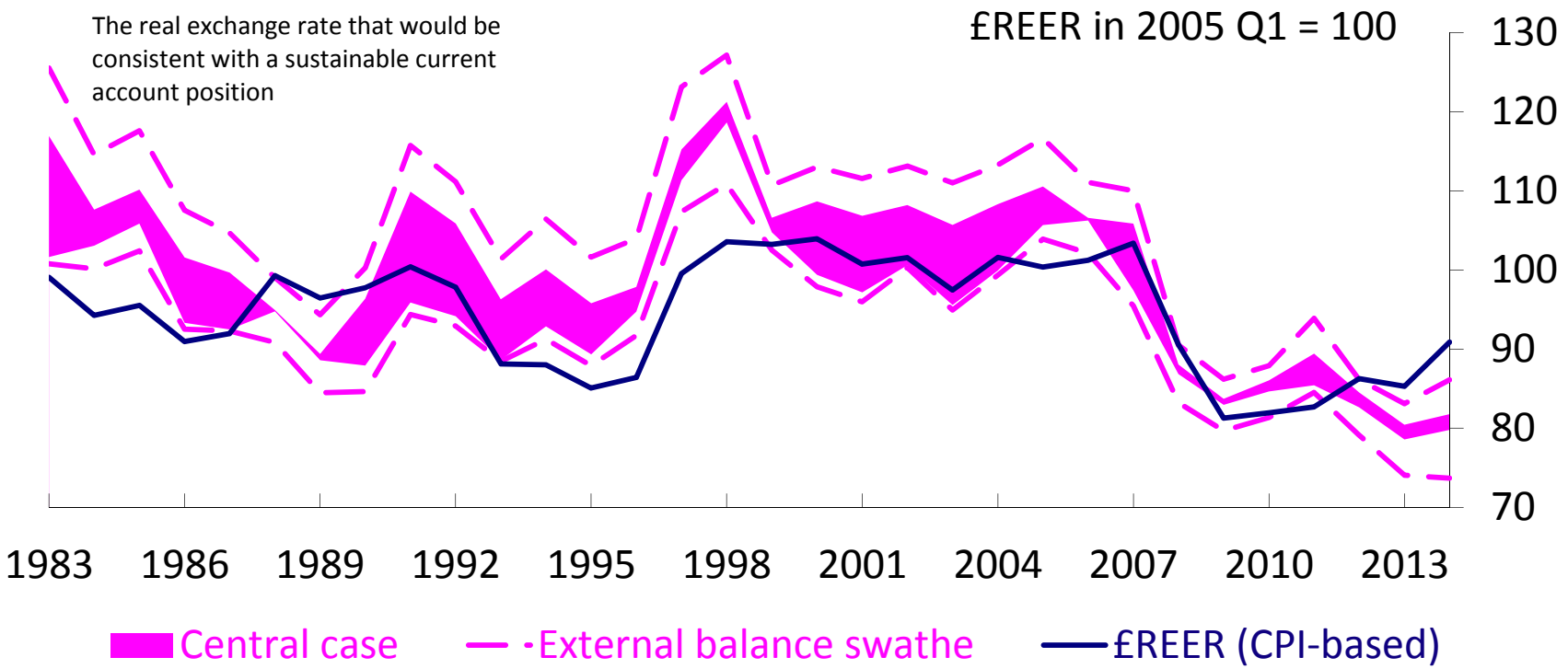
- Current account deficit narrowed slightly in Q4, driven by trade balance rather than primary income

Financial account and external stock position





Equilibrium real exchange rate estimates (£REER)

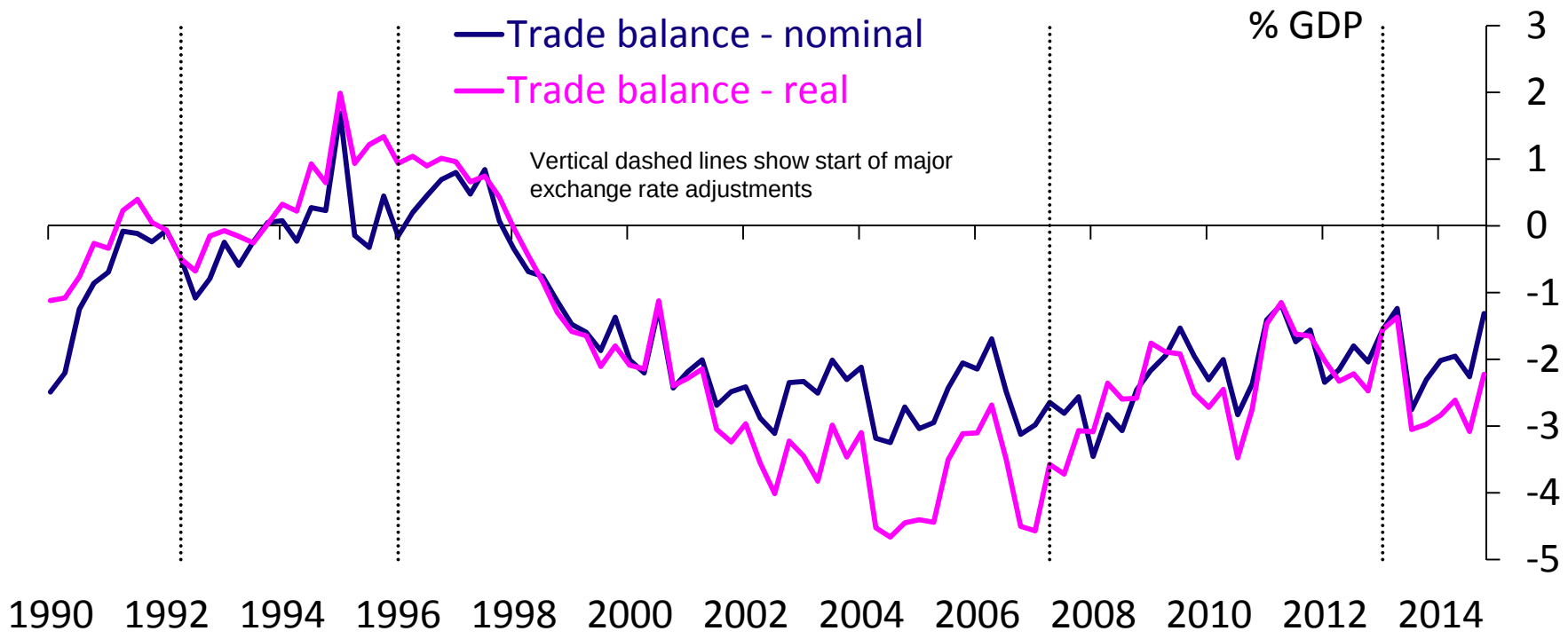


A depreciation in the region of 6% to -23% could be necessary to return the current account to a sustainable position.

External sector key messages (1)

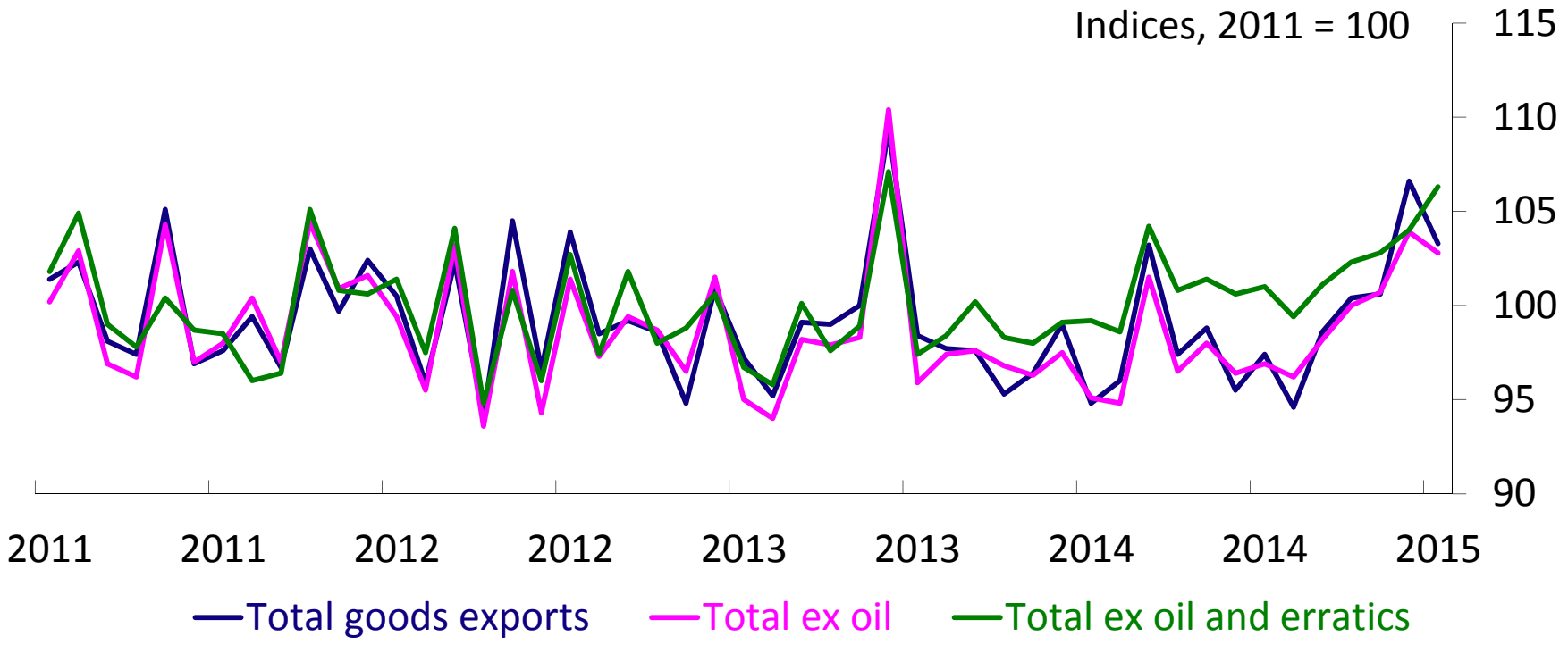
	Key messages
Balance of payments and the real exchange rate	• Slight improvement in the Q4 current account, but no improvement in the primary income balance • Models of the equilibrium real exchange rate suggest sterling could be substantially overvalued

Nominal and real trade balances



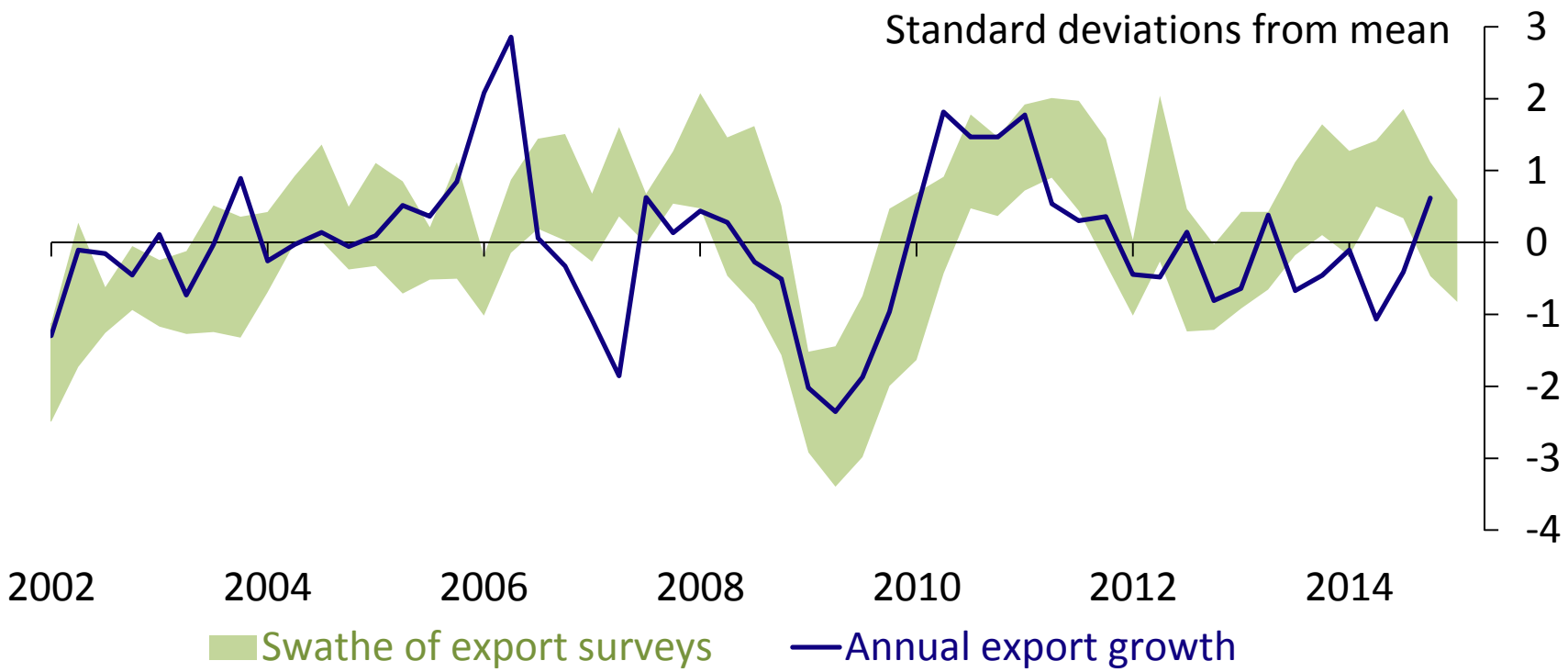
- Some improvement in nominal and real trade balances since 2007 depreciation

Goods export volumes



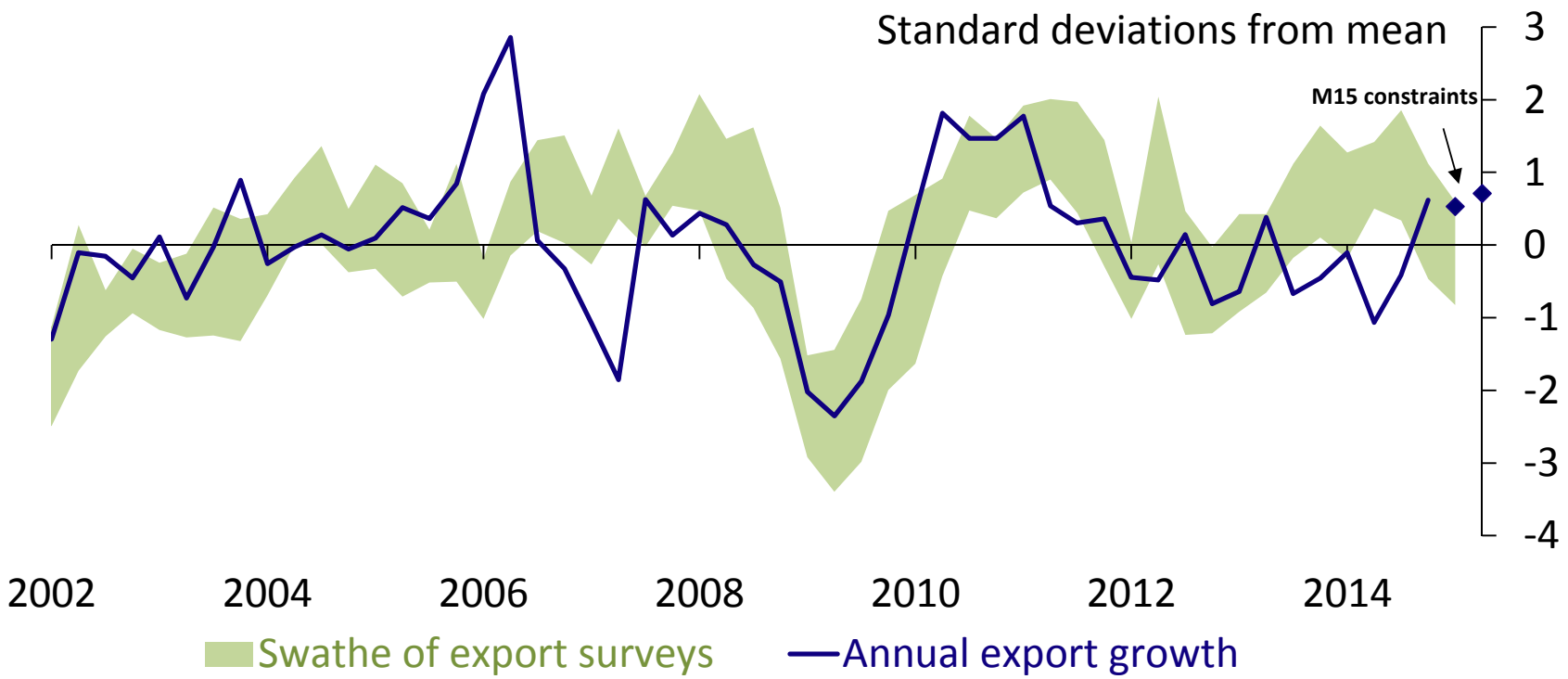
- Strength in monthly goods export volumes most evident excl. oil & erratics

Export goods volume survey swathe



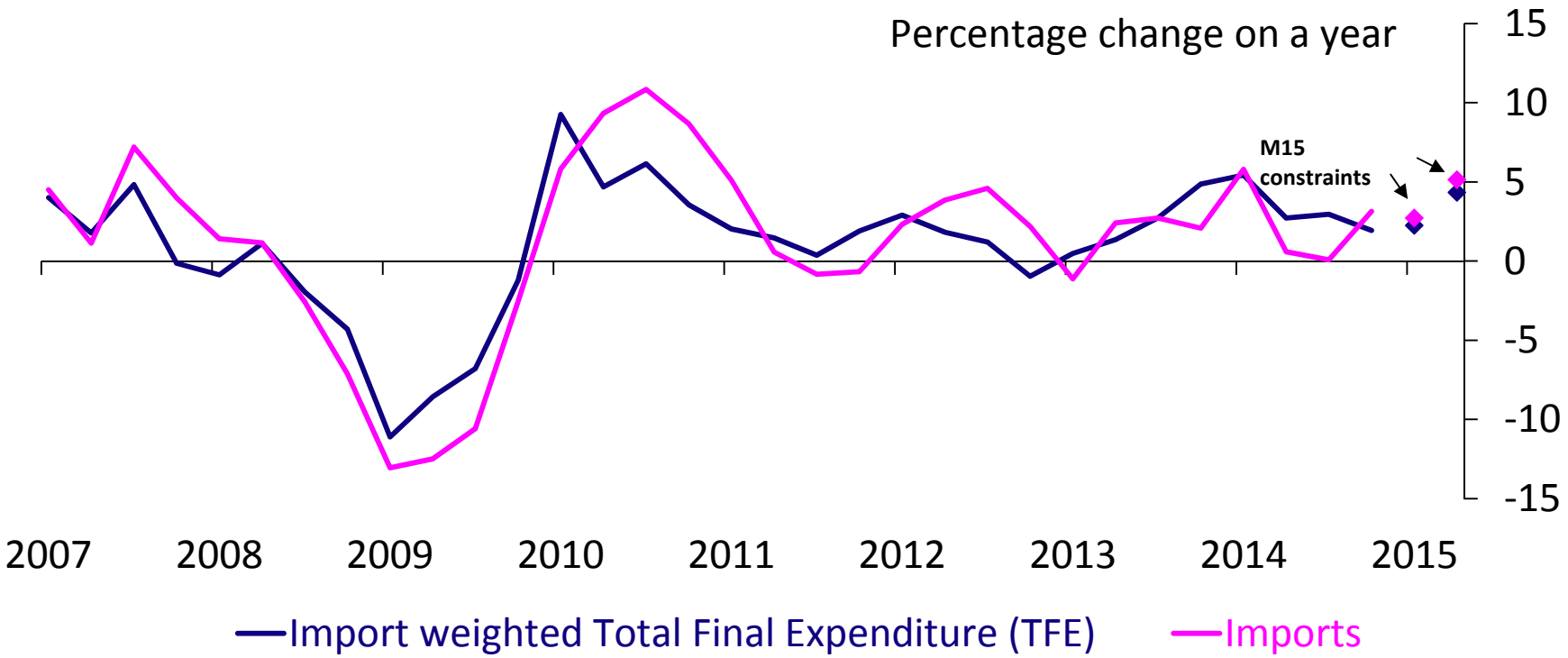
- Official goods export volume growth has strengthened, while surveys have softened

Goods export constraints



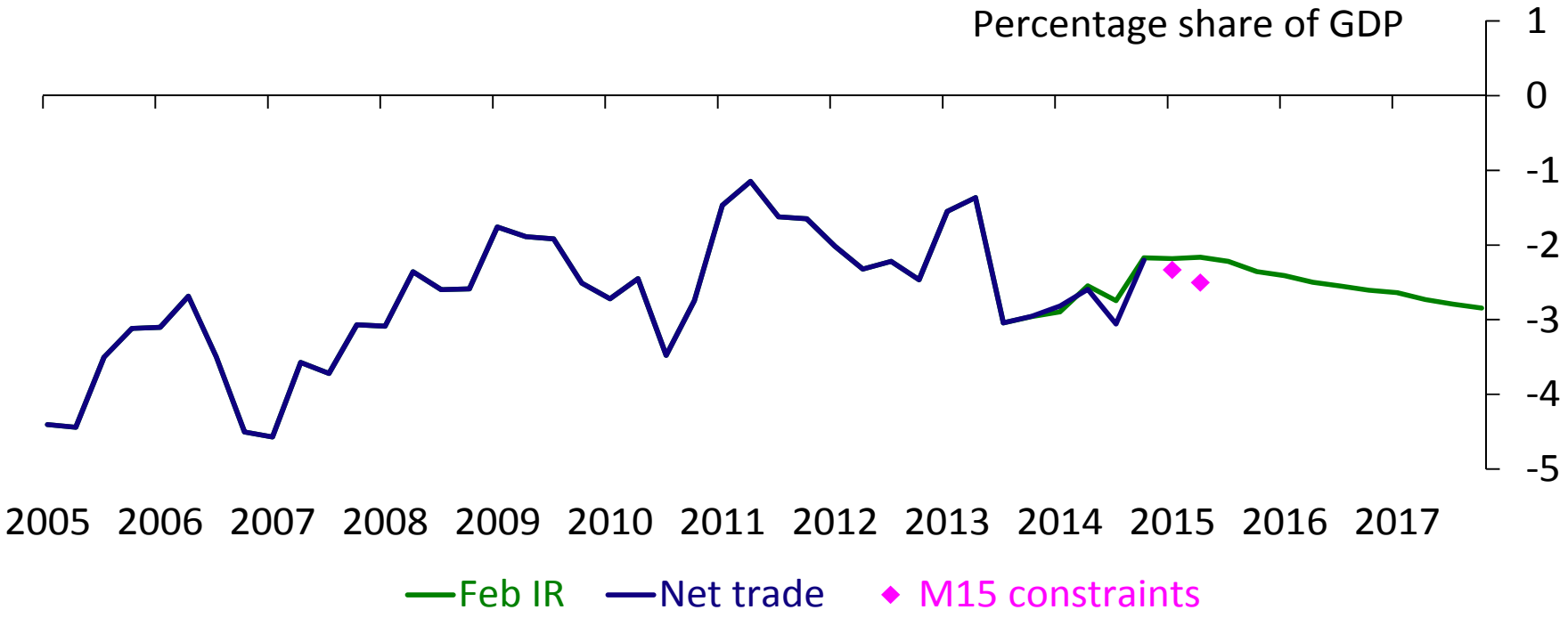
- The surveys pose a downside risk to the goods exports constraints

Import weighted TFE and import volumes



- Imports over 2014 have been puzzlingly weak

Real net trade balance

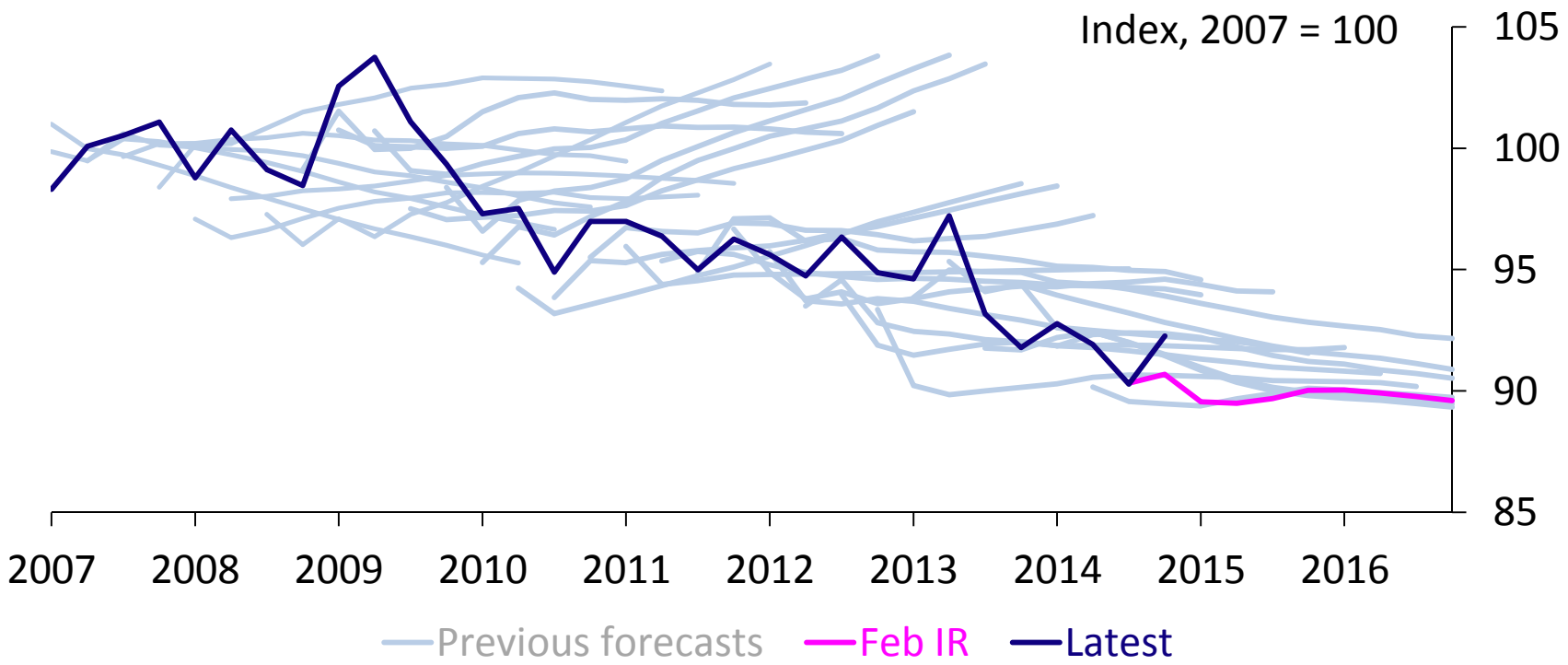


- Net trade broadly in line with February IR as recent strength in exports broadly offset by strong imports

External sector key messages (2)

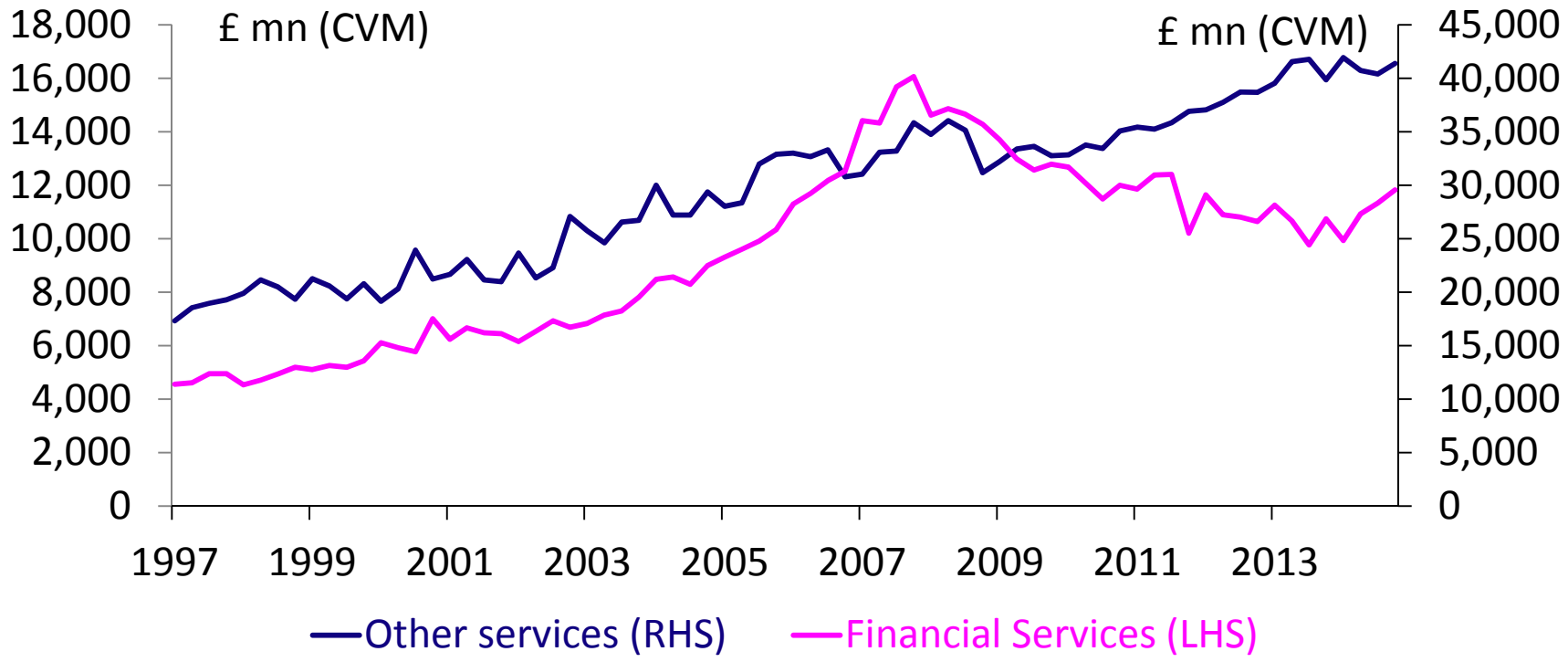
	Key messages
Balance of payments and the real exchange rate	• Slight improvement in the Q4 current account but no improvement in the primary income balance • Models of the equilibrium real exchange rate suggest sterling could be substantially overvalued
Latest trade data	• Recent export data have been surprisingly strong given weakness in business surveys and the likely drag from sterling's appreciation • But imports have also been strong so there is little news for net trade

Successive IR export share forecasts



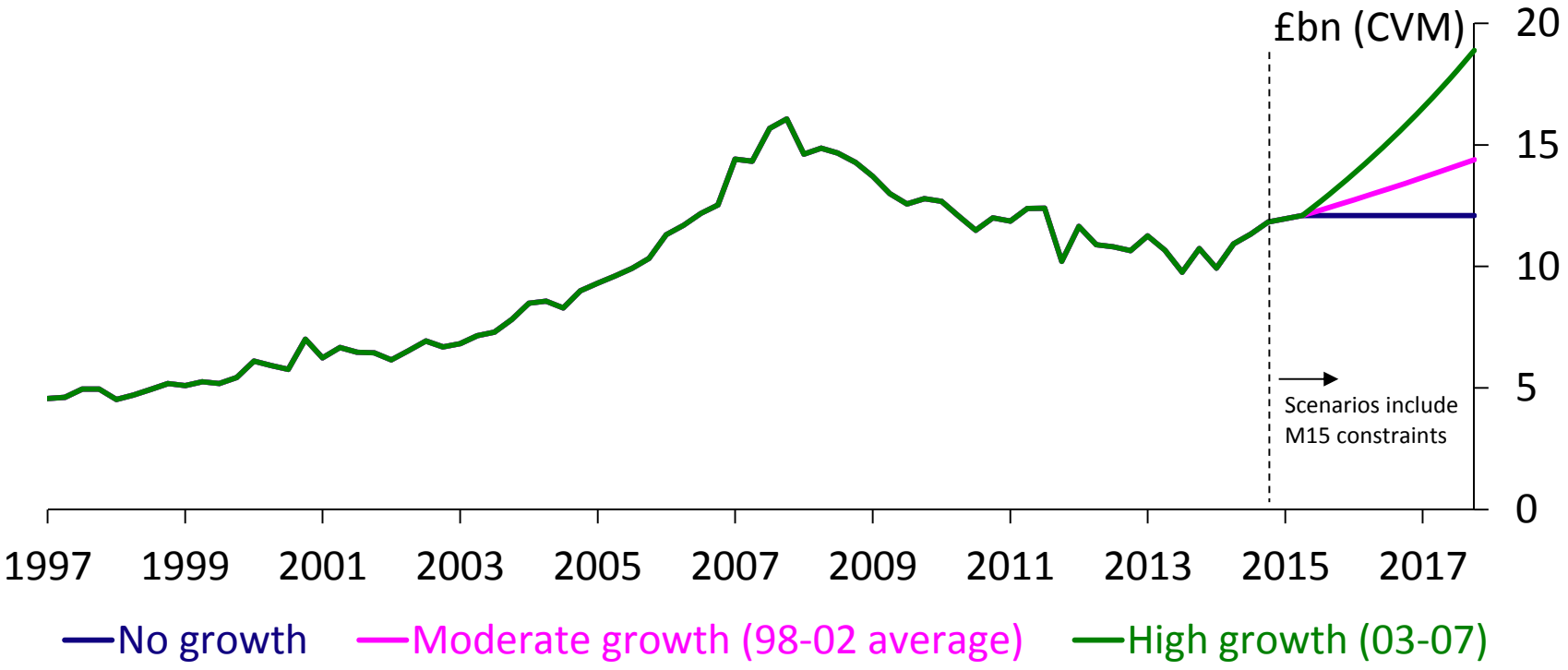
- We repeatedly over-predicted the export share following the depreciation

Services export volumes

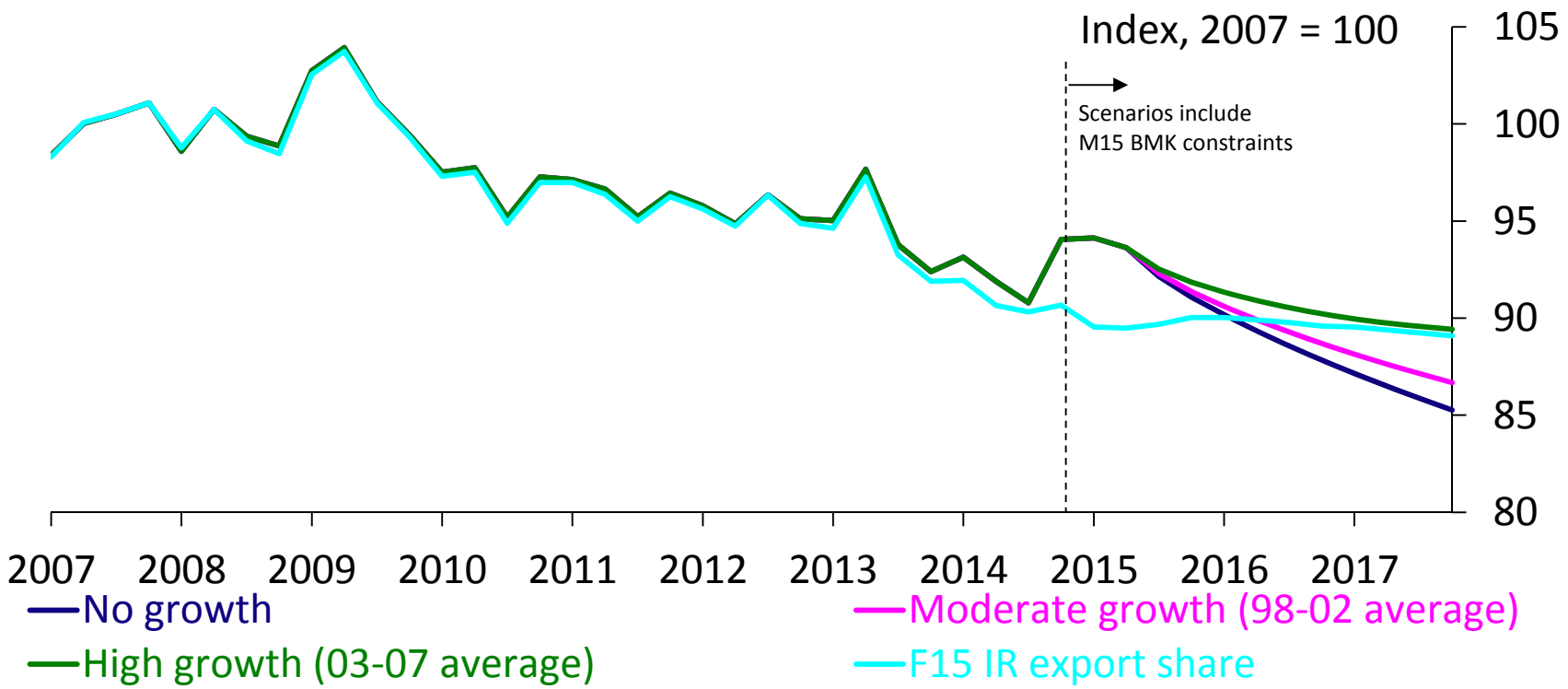


- Most of the deterioration could be attributed to financial services

Scenarios for financial services exports



Scenarios for the total export share



- Only in the 'high growth' financial services scenario does the export share stay as high as in the February *Inflation Report*

External sector key messages (3)

	Key messages
Balance of payments and the real exchange rate	• Slight improvement in the Q4 current account but no improvement in the primary income balance • Models of the equilibrium real exchange rate suggest sterling could be substantially overvalued
Latest trade data	• Recent export data have been surprisingly strong given weakness in business surveys and the likely drag from sterling's appreciation • But imports have also been strong so there is little news for net trade
Prospects for exports and net trade	• The export share forecast implicitly relies on strong growth in financial services exports given sterling's recent further appreciation • Revising down that forecast would have significant implications for GDP growth

Key messages

1) Update on near term outlook

- Forecast for solid and fairly stable growth remains on track

2) Expenditure news from QNA

- Main domestic components slightly weaker than expected in the near term

3) Prospects for the external sector

- Exports and net trade could disappoint in the medium term

END

GDP tables

Excluding revisions:

Current quarterly GDP growth & initial release projections

	Headline GDP#		GDP**^	
	Now	Feb IR	Now	Feb IR
2013 Q1	0.6	0.6	0.7	0.7
Q2	0.6	0.6	0.5	0.5
Q3	0.4	0.7	0.5	0.5
Q4	0.4	0.4	0.5	0.5
2014 Q1	0.9	0.6	0.7	0.5
Q2	0.8	0.8	0.8	0.8
Q3	0.6	0.7	0.6	0.7
Q4	0.6	0.5	0.8	0.7
2015 Q1	0.6	0.6	0.7	0.6
Q2	N/A	N/A	N/A	N/A

market prices

^ basic prices

Including revisions:

Final quarterly GDP growth estimates & projections

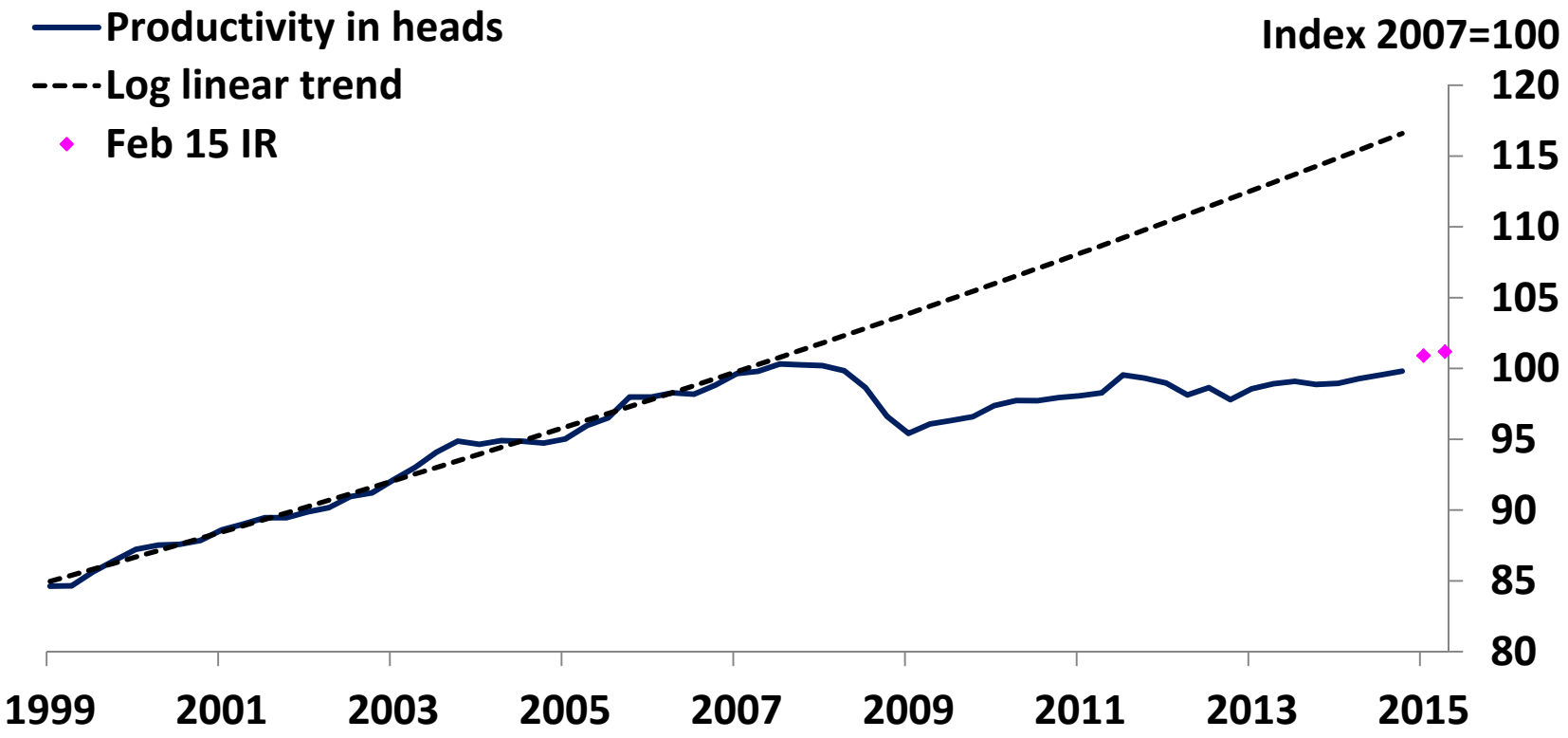
Headline GDP#		GDP**^	
Now	Feb IR	Now	Feb IR
0.5	0.5	0.9	0.6
0.6	0.6	0.5	0.5
0.7	0.8	0.7	0.5
0.7	0.6	0.7	0.7
0.9	0.8	0.9	0.7
0.9	0.9	1.0	0.9
0.7	0.8	0.7	0.9
0.7	0.6	0.9	0.8
0.7	0.7	0.8	0.7
0.7	0.7	N/A	N/A

Supply stocktake

2nd April 2015

Structural Economic Analysis Division

Labour productivity



Part I: Productivity

What happens after severe financial crises?

Evidence from previous episodes:

- **Potential output *level* permanently lower**
- **No permanent effect on trend *growth rate***
- **No evidence of faster growth (i.e. level catch up) immediately after crisis.**

Outline of part I and Key messages:

1) Steady state growth trend

Pre-crisis trend growth attainable with some downward risks

2) Productivity puzzle update

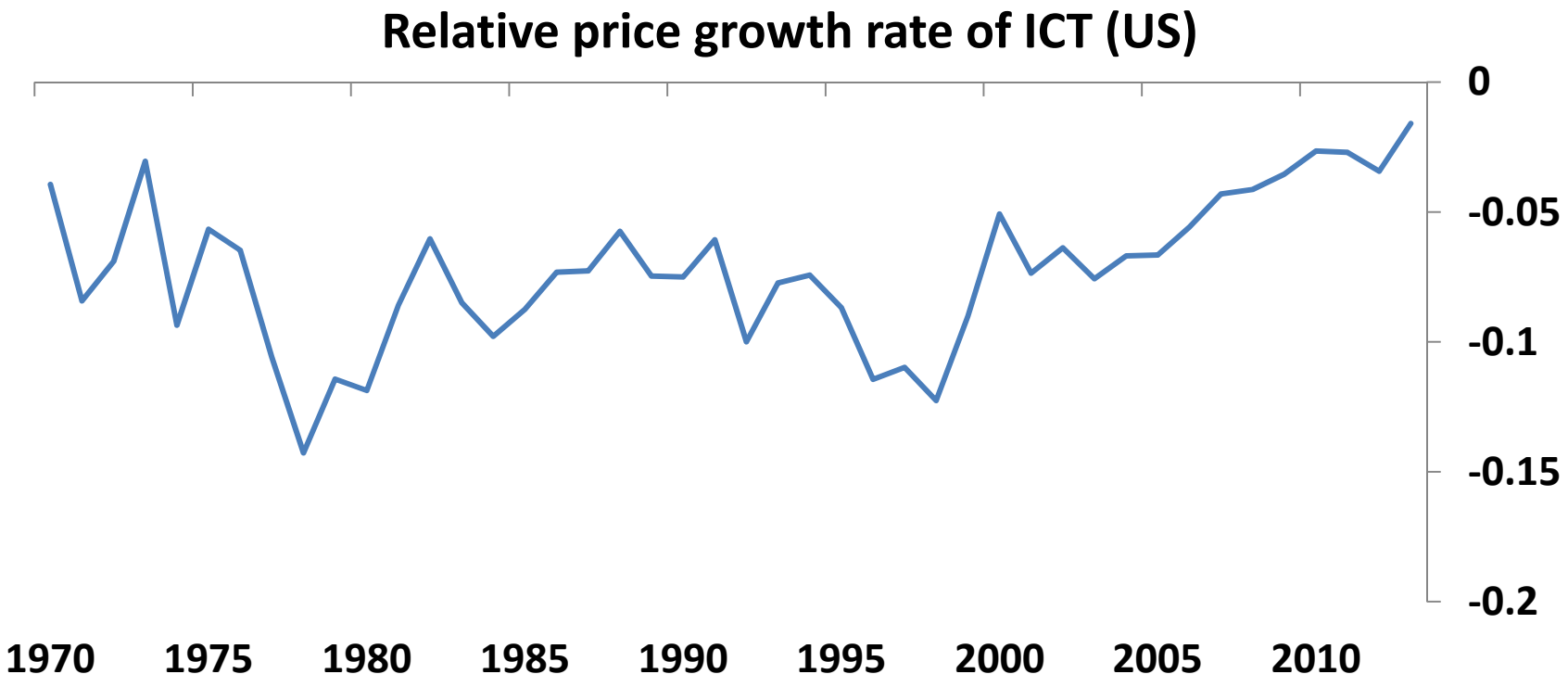
Some indication that resource reallocation is beginning to happen

Steady state growth

Is pre-crisis growth rate attainable?

- Two sector growth models tend to fit the data better than one sector models
- They emphasise the role of a fast growing 'investment' sector
- ICT as the investment sector in the current environment

Downward risks to technology



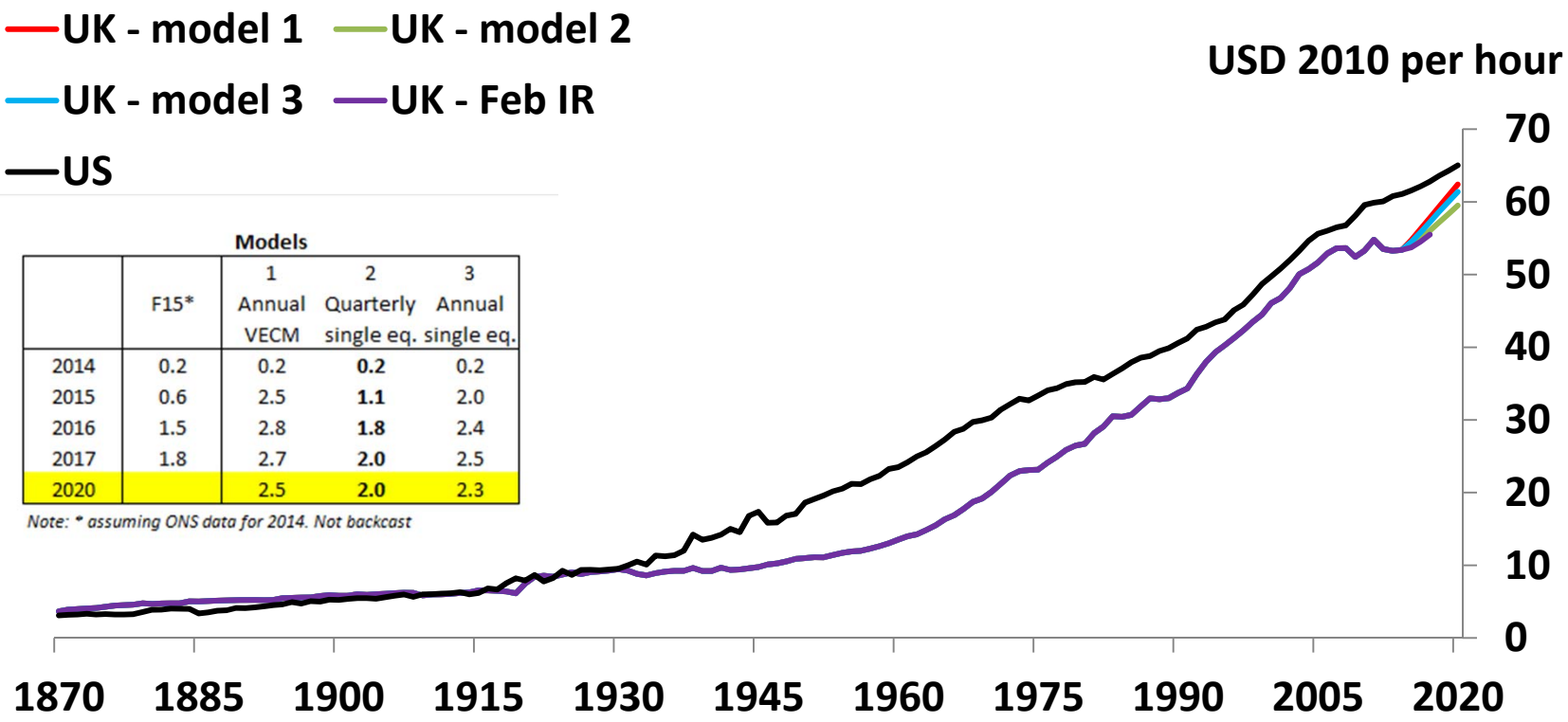
Source: BEA

Technological stagnation

Theme	Pessimists	Optimists
Scale of existing innovations	ICT not as important as electrification or steam (Cowen, 2011, Gordon, 2012)	ICT already had bigger impact on growth than electricity (Craft, 2004)
Impact of existing innovations	ICT revolution has run its course (Gordon, 2012)	ICT revolution has still long to go (Brynjolfsson and McAfee, 2011, Syverson 2013, Byrne et al, 2013)
Source of new innovations	No major innovations on the horizon (Cowen, 2011, Gordon, 2012)	Scientific discovery has accelerated (Mokyr, 2014)
Demographics	Lower population growth means less ideas are created (Gordon, 2014)	Ideas can circulate much faster thanks to new technologies (Jones and Romer, 2010)

-

UK and US productivity



		Models		
	F15*	1 Annual VECM	2 Quarterly single eq.	3 Annual single eq.
2014	0.2	0.2	**0.2**	0.2
2015	0.6	2.5	**1.1**	2.0
2016	1.5	2.8	**1.8**	2.4
2017	1.8	2.7	**2.0**	2.5
2020		2.5	**2.0**	2.3

*Note: * assuming ONS data for 2014. Not backcast*

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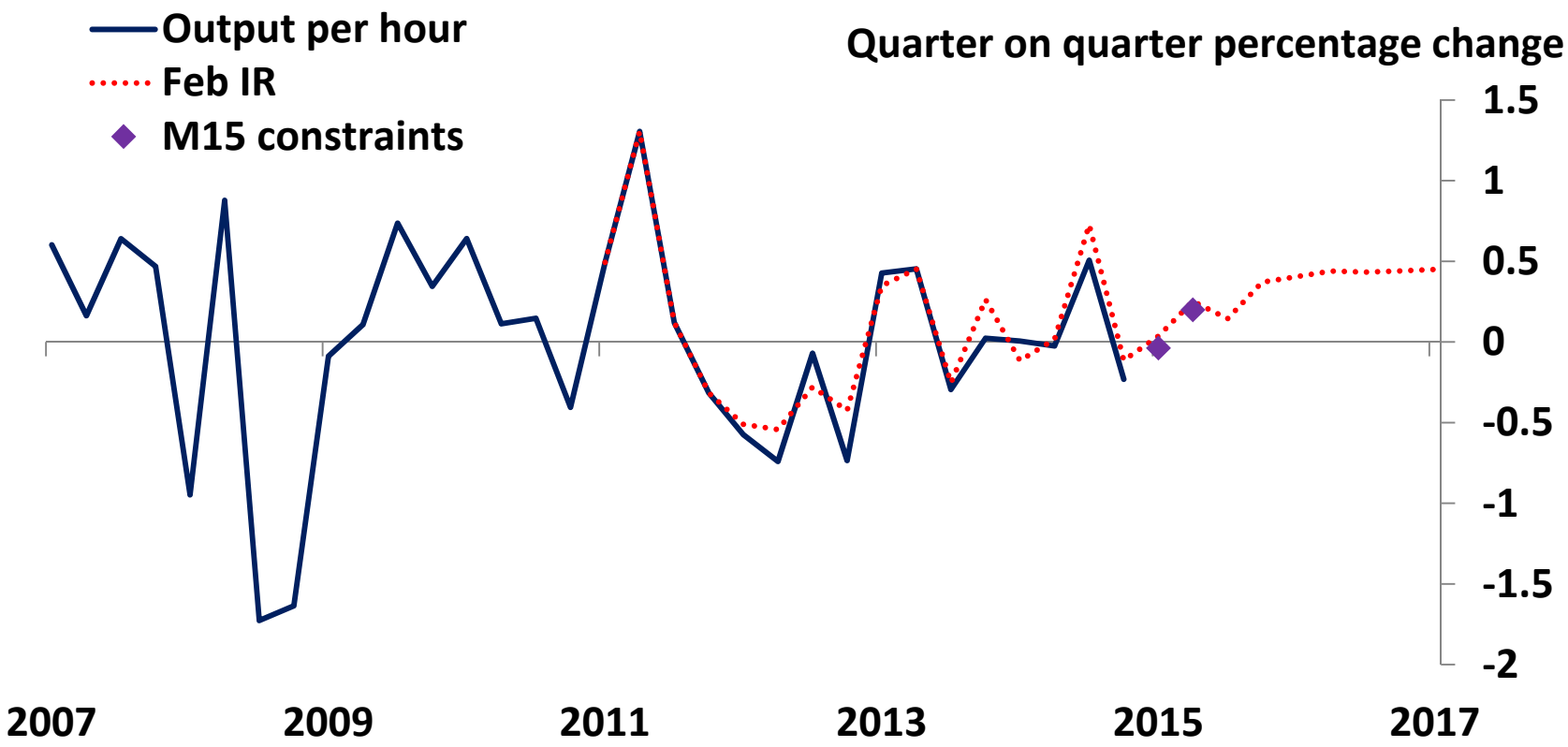
Update on the productivity puzzle

Labour productivity growth

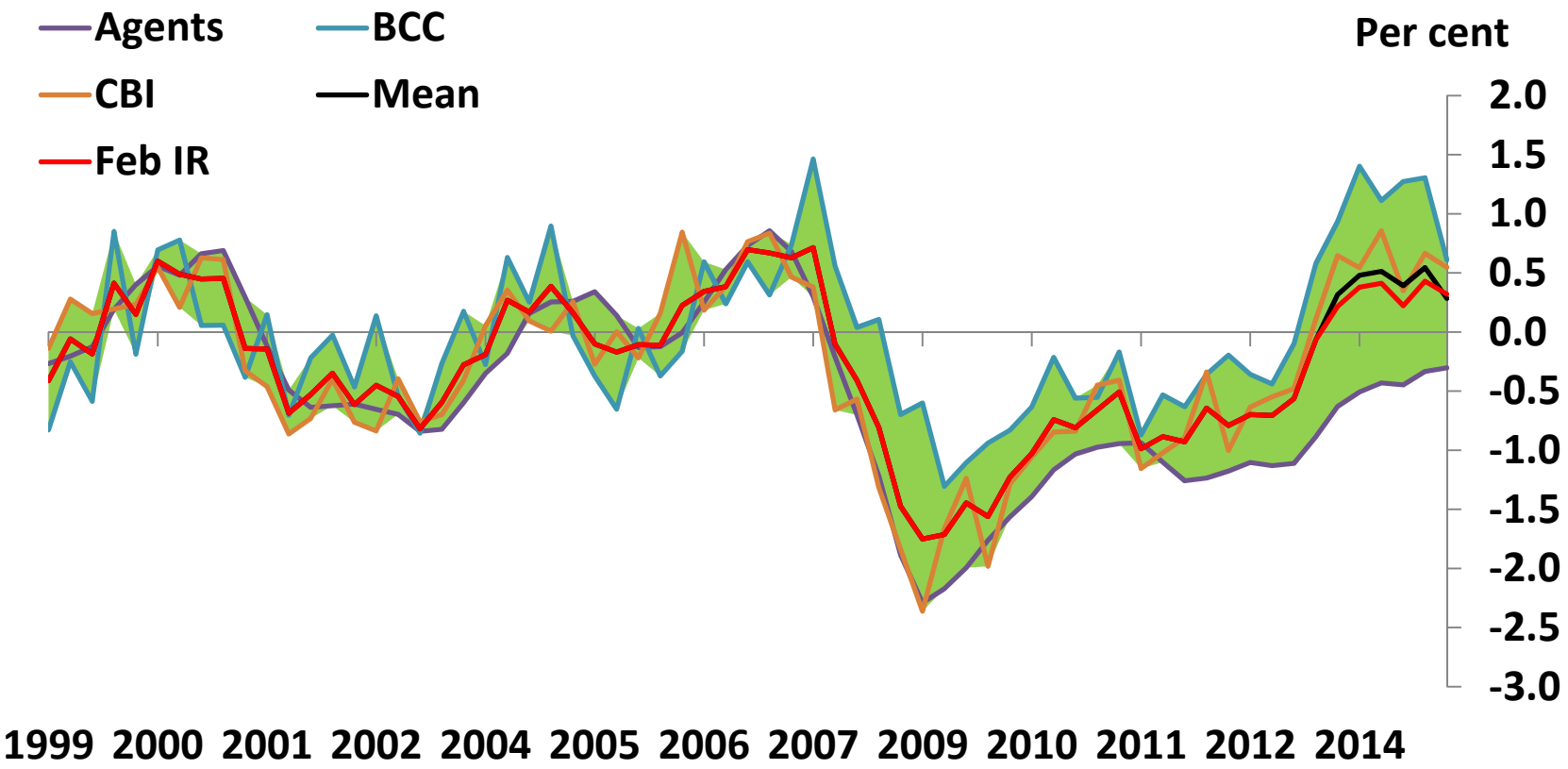


Explanations of the productivity puzzle

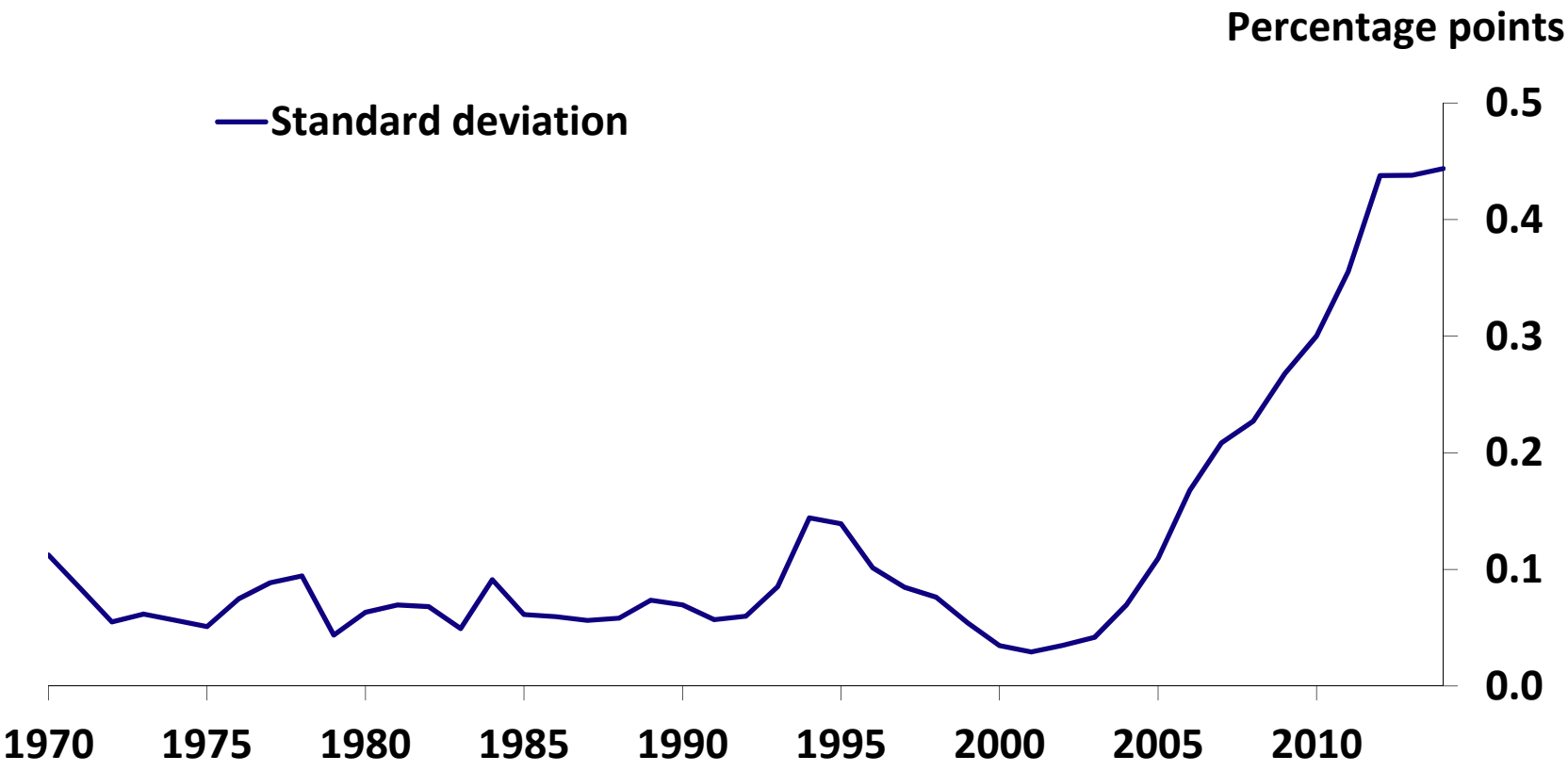
Factors contributing to the weakness in UK labour productivity

(in pp)	2013 Q4 (original vintage)	2013 Q4 (latest vintage)	2014 Q4
Shortfall relative to trend	16	13.5	15
Measurement issues	4	2.5	3
Measurement of output	2	0.5	1
o/w R&D capitalisation	1.5	-	-
Lower trend in some sectors	2	2	2
Actual shortfall to explain	12	11	12
Cyclical	0	0	0
Lower CAPU	0	0	0
Labour hoarding	Uncertain	Uncertain	Uncertain
Persistent	6-9	7-9	7-9
Lower physical and intangible capital	3-4	4	4
Impaired resource allocation & high firm survival rates	3-5	3-5	3-5
Total left unexplained	3-6	2-4	3-5

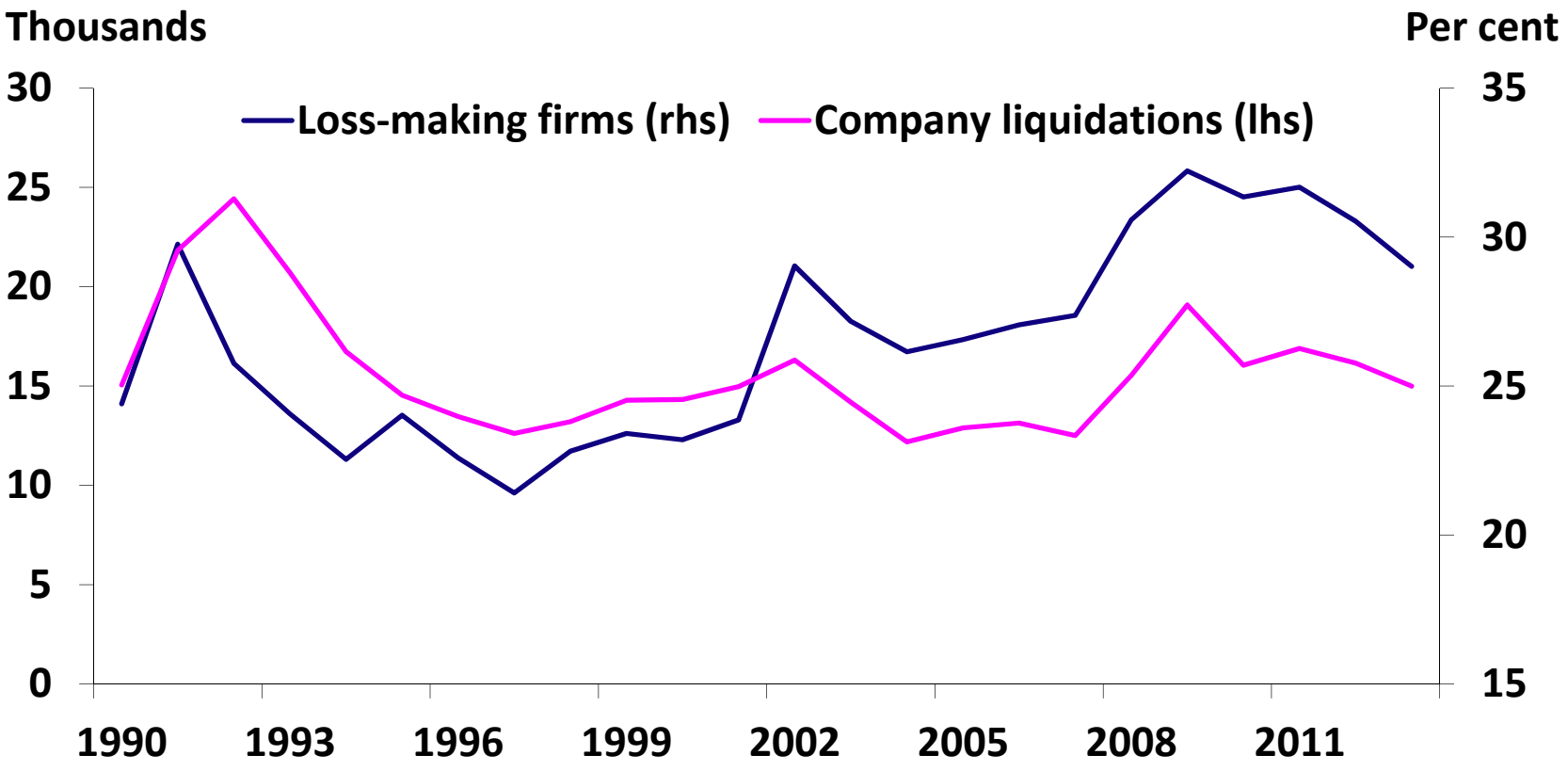
CAPU


Agents
BCC
CBI
Mean
Feb IR
Per cent
2.0
1.5
1.0
0.5
0.0
-0.5
-1.0
-1.5
-2.0
-2.5
-3.0
1999
2000
2001
2002
2004
2005
2006
2007
2009
2010
2011
2012
2014

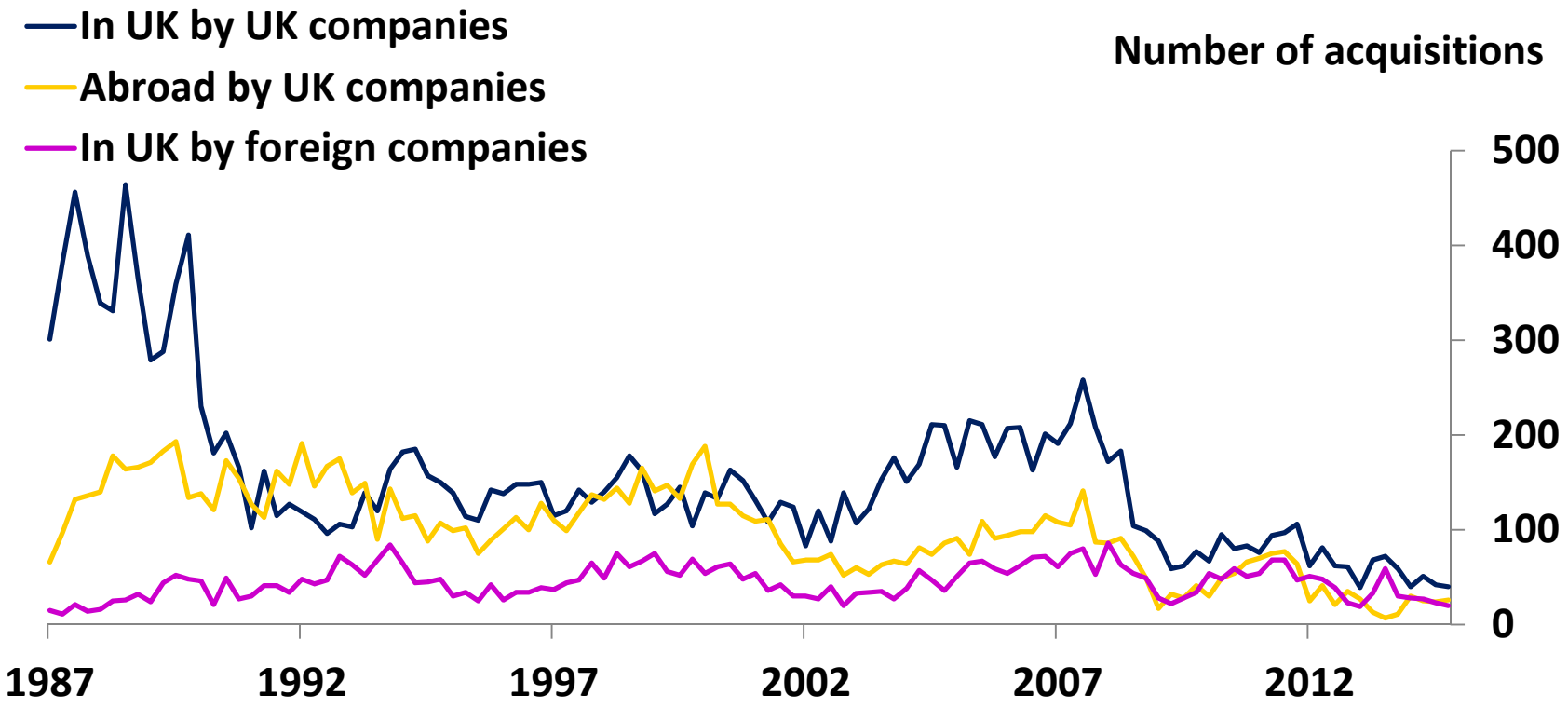
Productivity dispersion across industries



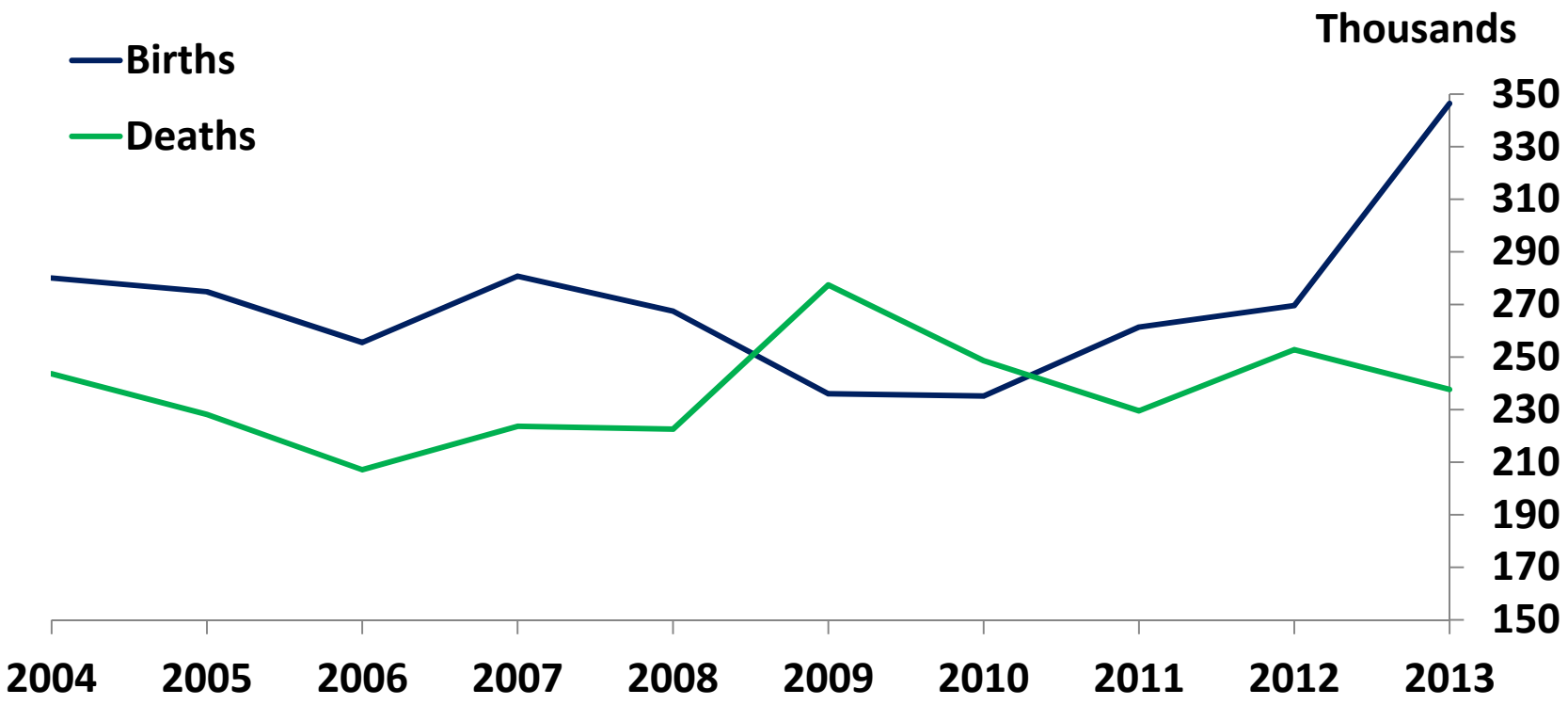
Liquidations and loss making firms



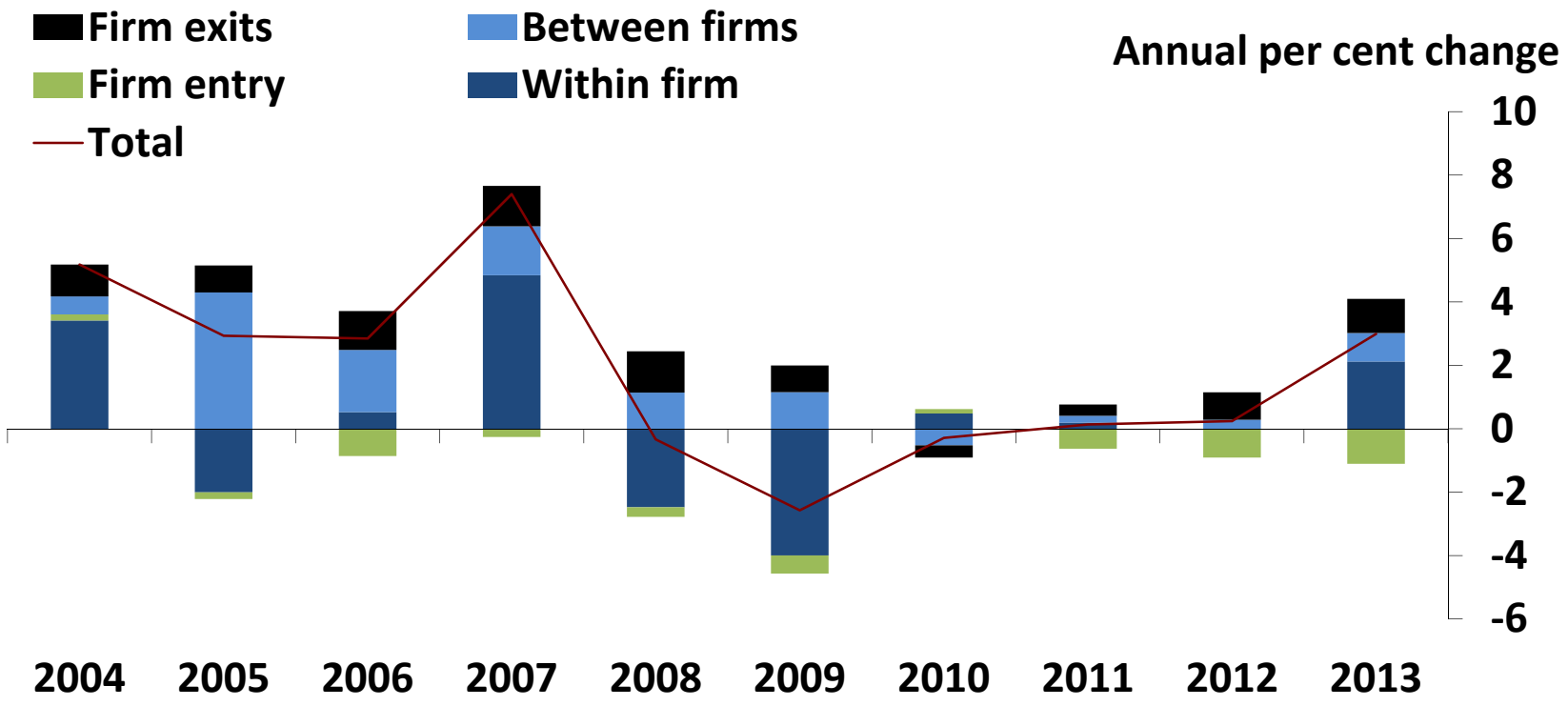
M&A


In UK by UK companies
Abroad by UK companies
In UK by foreign companies
Number of acquisitions
500
400
300
200
100
0
1987
1992
1997
2002
2007
2012

Company births and deaths



Productivity dynamics



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Productivity summary

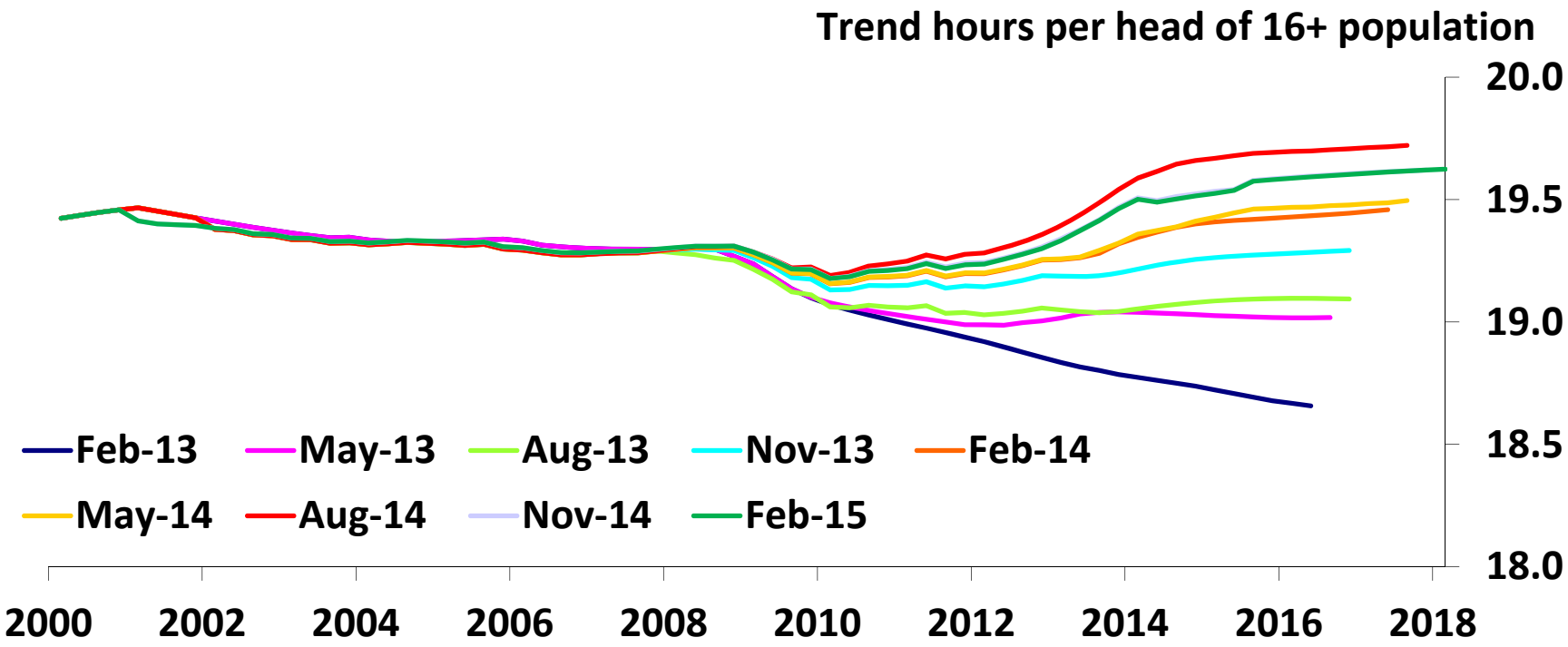
- **A return to historically average productivity growth rates is a good central assumption.**

- **Our diagnosis of the post-crisis productivity puzzle has changed little in the past year. But there are tentative signs of an easing of recourse reallocation constraints.**

- **We can probably no longer rely of the absorption of under-utilised labour resources to support growth in the absence of a productivity growth pickup**.

Part II: labour supply

Vintages of trend labour supply assumptions



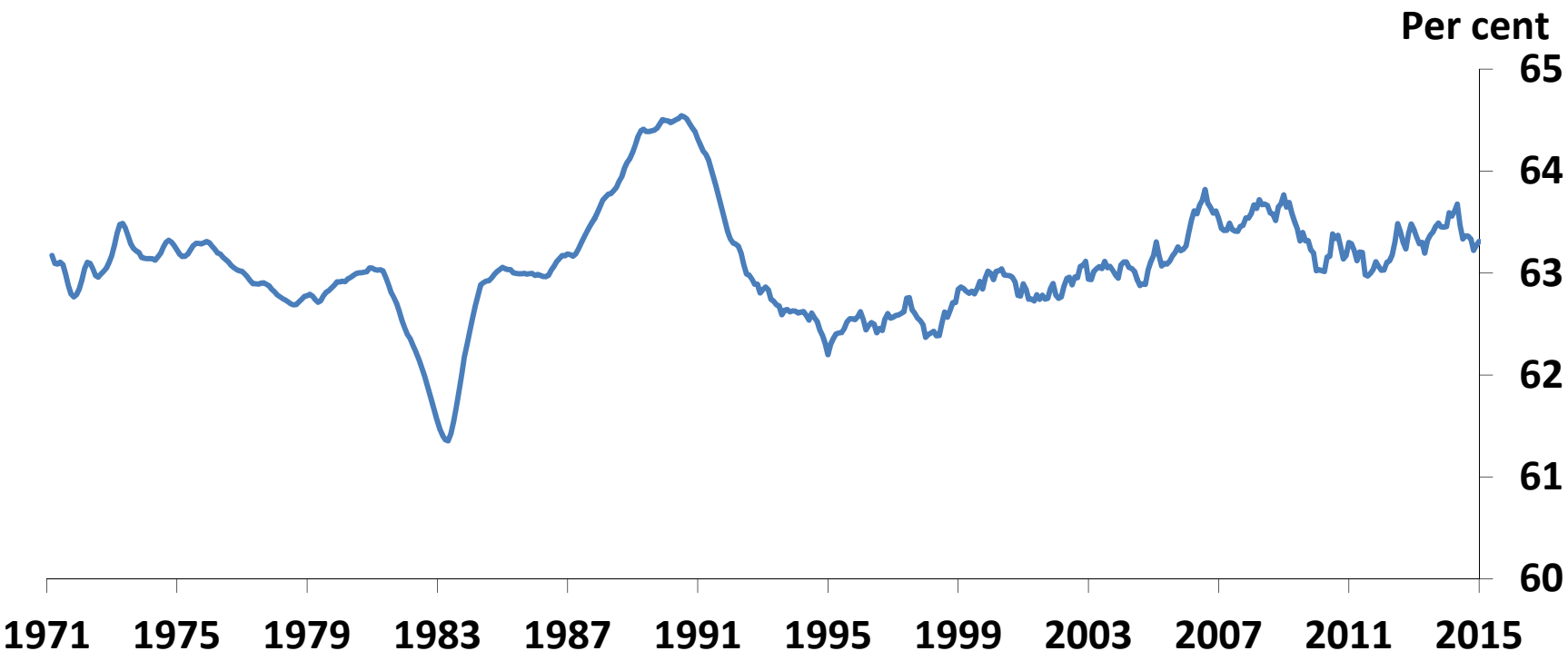
- **Trend labour supply per capita in 2016 had been revised up by 5% since Feb 2013.**

Risks to labour supply

	2015 Q1 gap		Main risks	Balance of risks
	Feb IR	BMK		
Participation				
Average hours				
Unemployment				
Population/ migration				

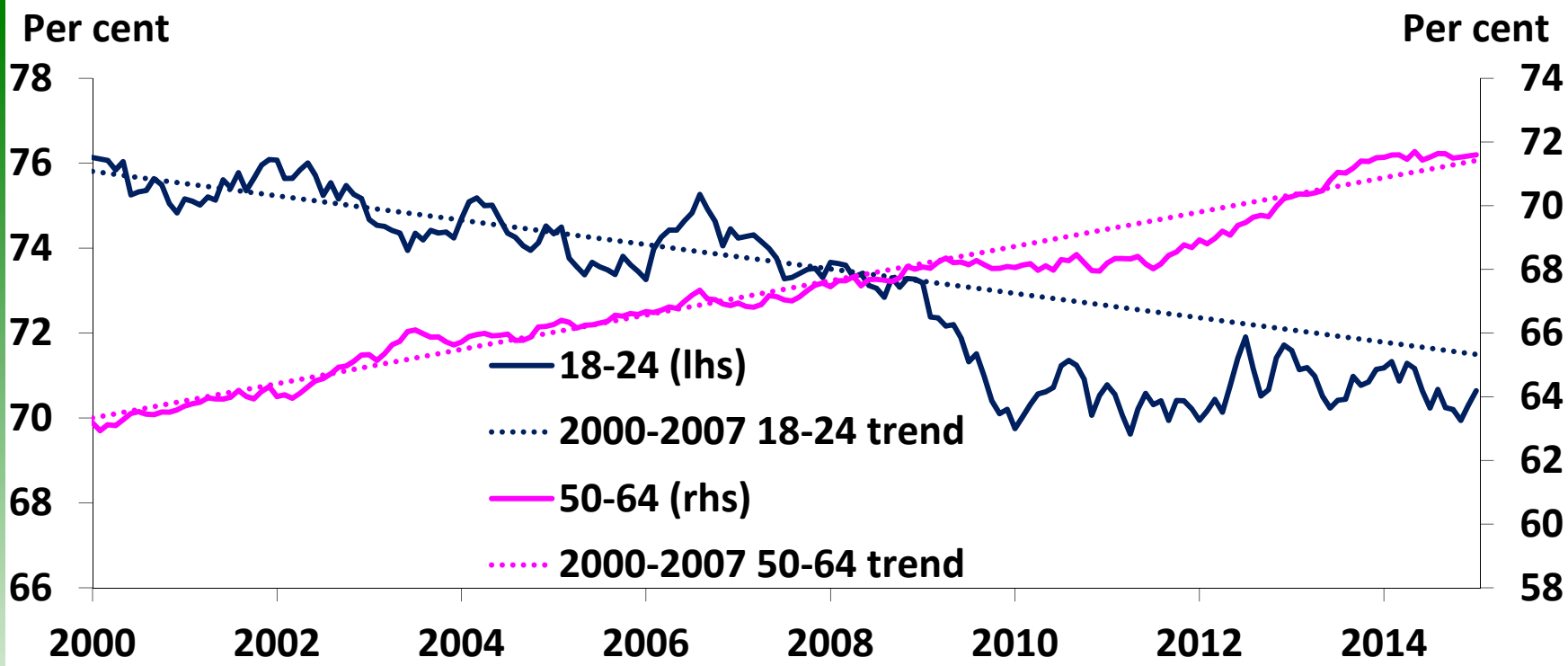
Participation

Participation rate



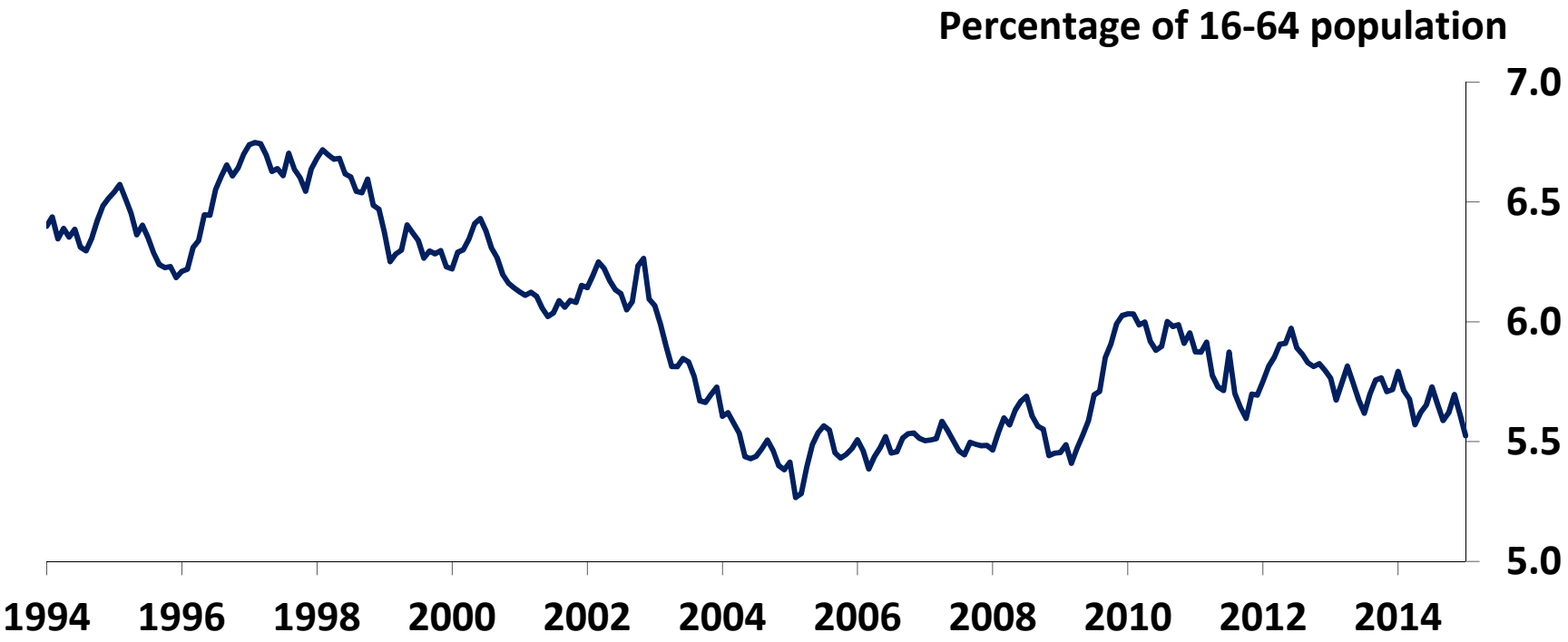
- **Participation fell by ¾ pp following the crisis but has since partly recovered.**

Participation rates for 18-24 and 50-64 year olds



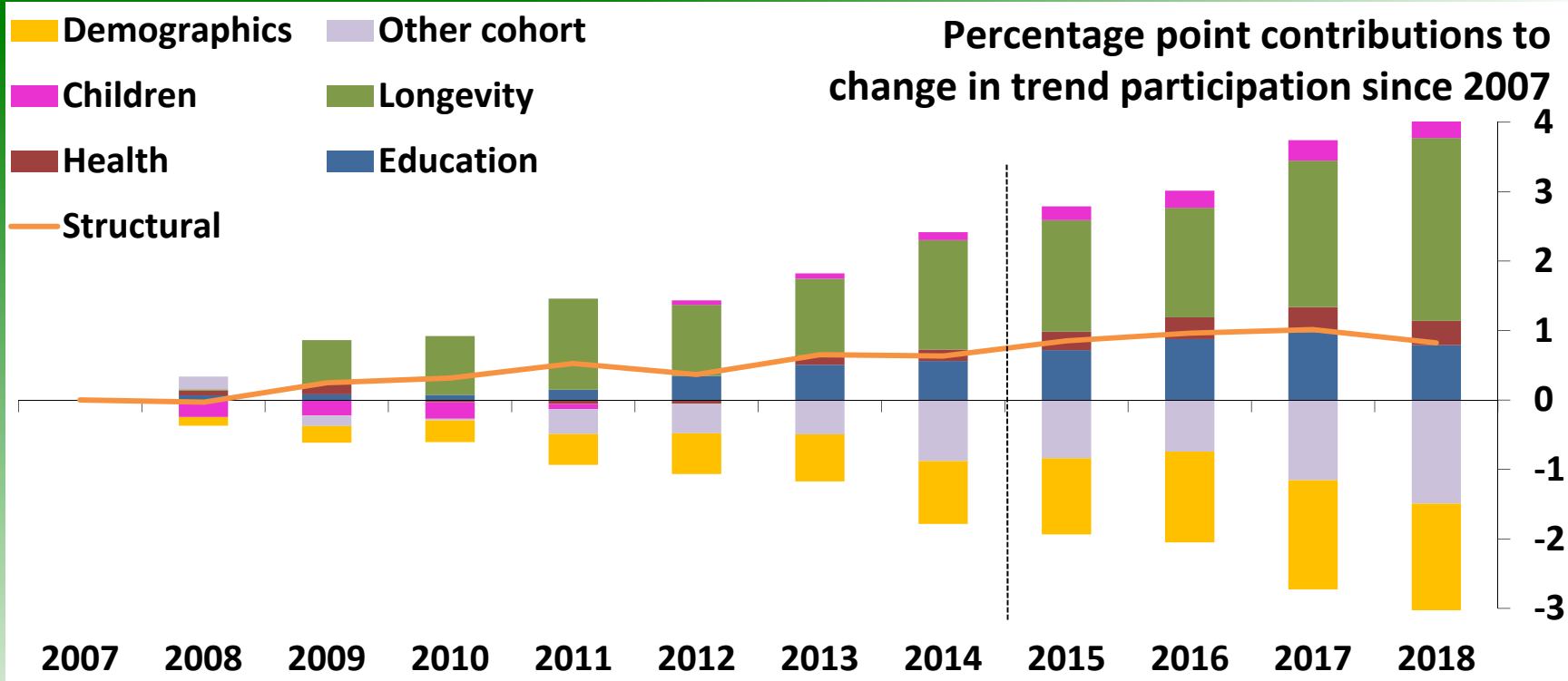
- Cyclical hit to participation for young and those nearing retirement has largely unwound.

Inactive wanting a job (16-64)



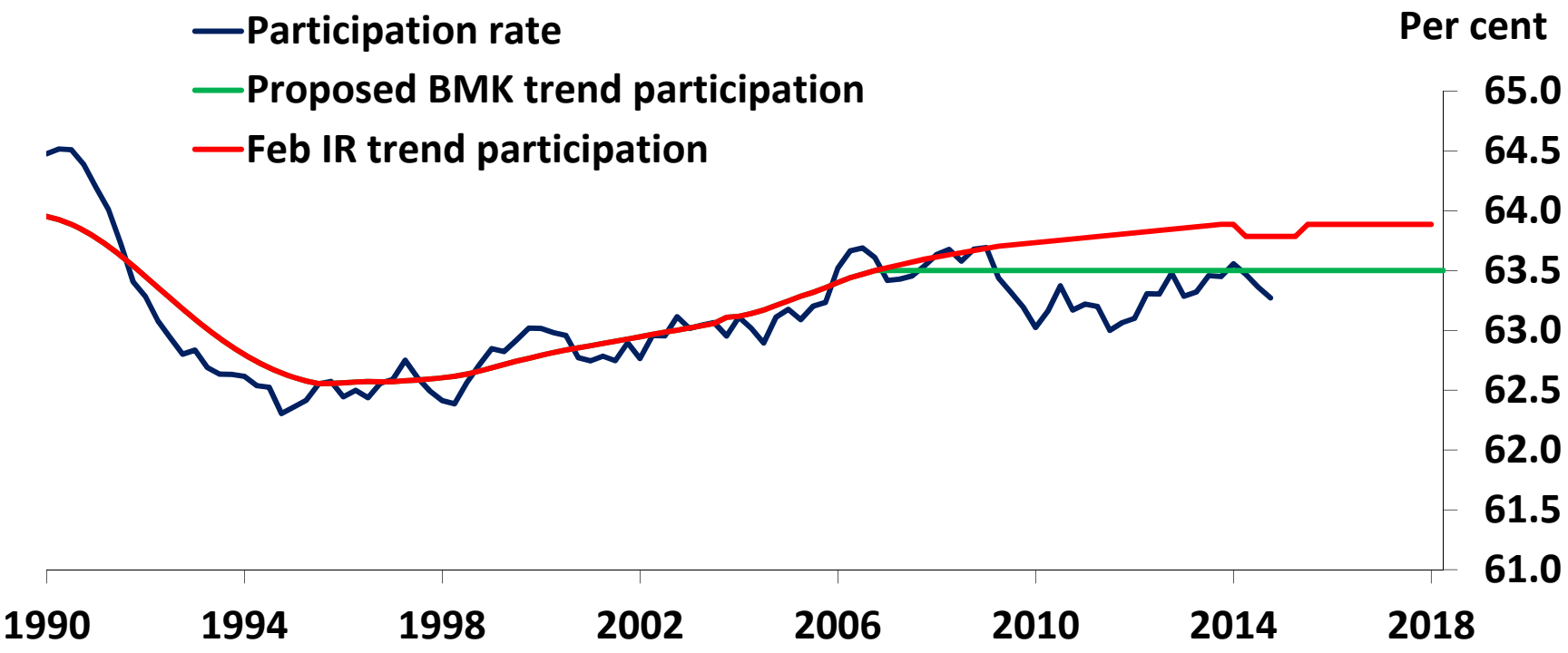
- **Cyclical boost to 'involuntary inactivity' has unwound, suggesting little cyclical gap.**

Cohort model of participation



- Cohort model of participation suggests flat trend over next few years.

Trend participation assumptions



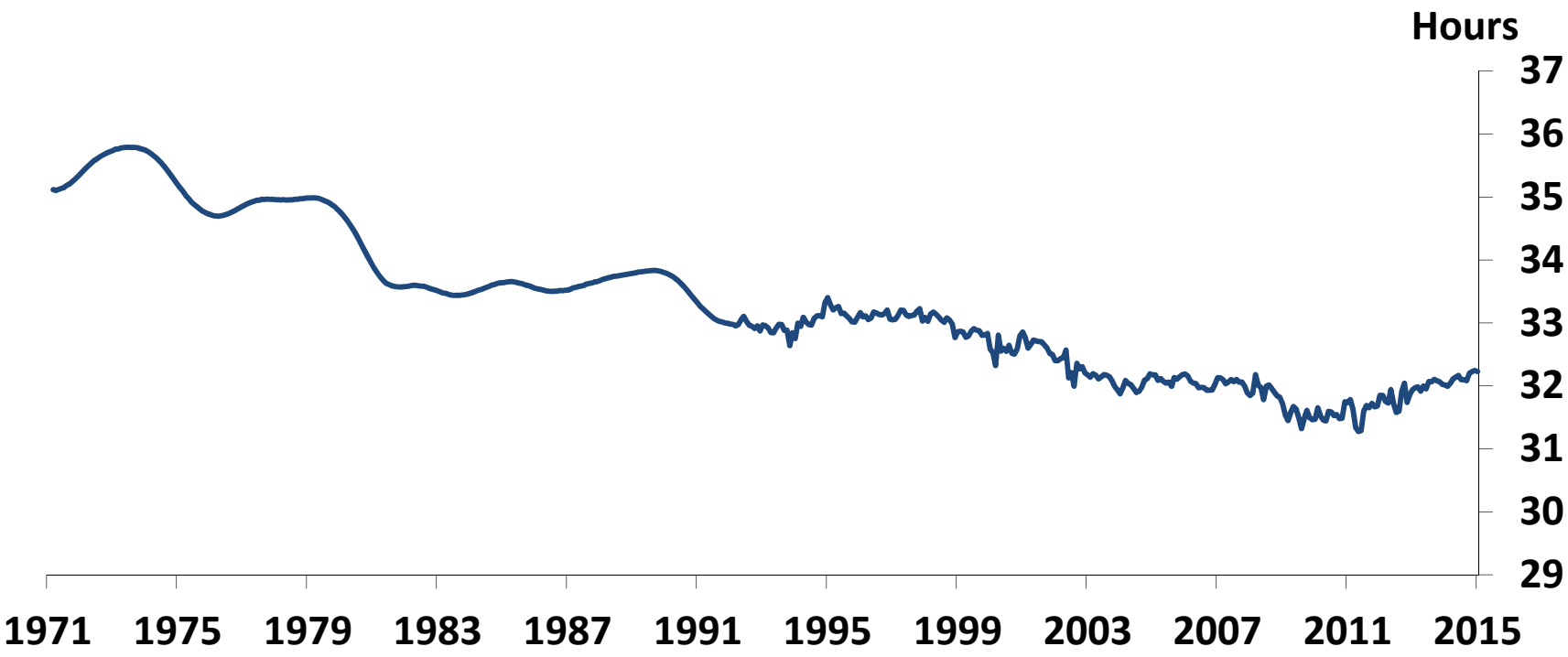
- **Proposed trend 0.4pp lower over the forecast.**

Risks to labour supply

	2015 Q1 gap		Main risks	Balance of risks
	Feb IR	BMK		
Participation	0.5pp	0.2pp	Whether trend increase in older participation or demographic drag from ageing population dominates.	⇔
Average hours				
Unemployment				
Population/ migration				

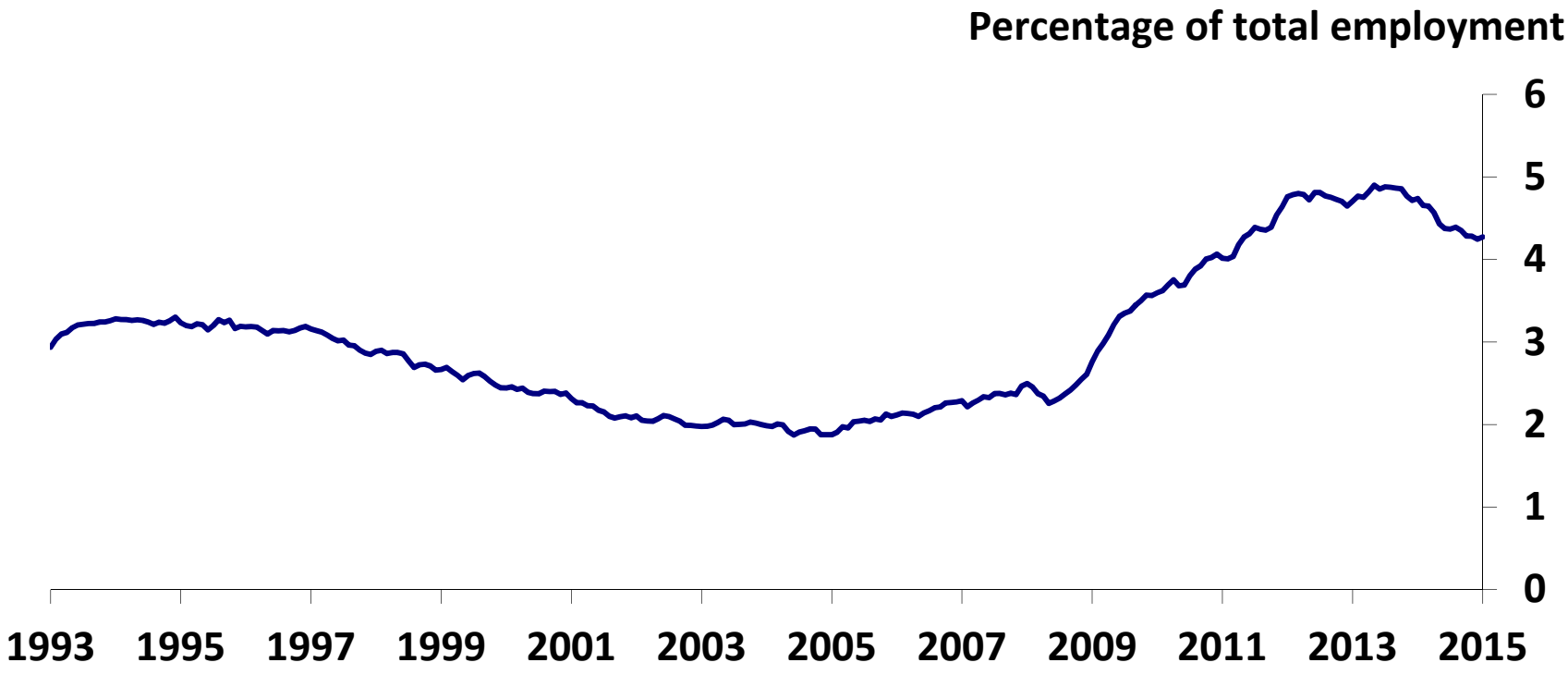
Average hours

Average hours



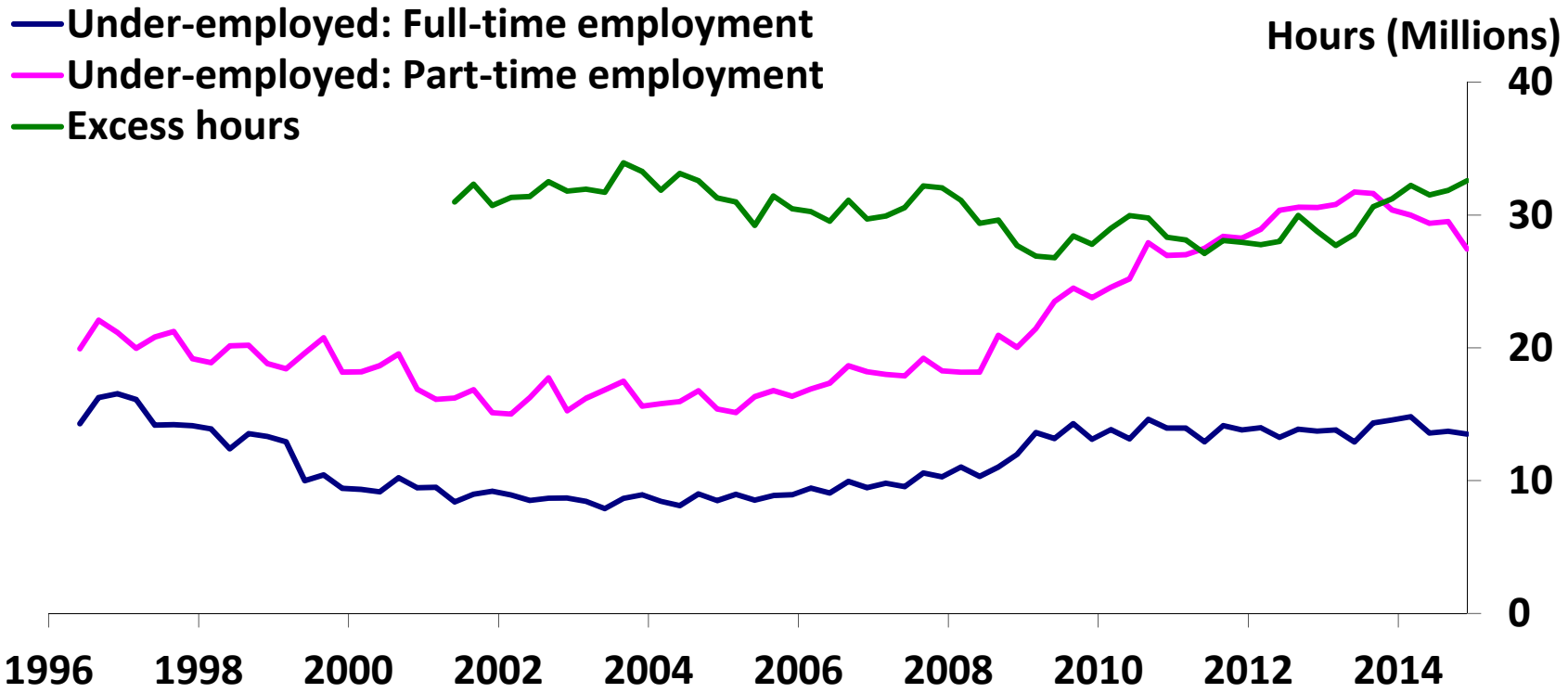
- **Recent strength in average hours in contrast to longer-run downward trend.**

Part-time workers that want a full-time job



- **Involuntary part-time working still elevated.**

Decomposition of desired hours into FT/PT



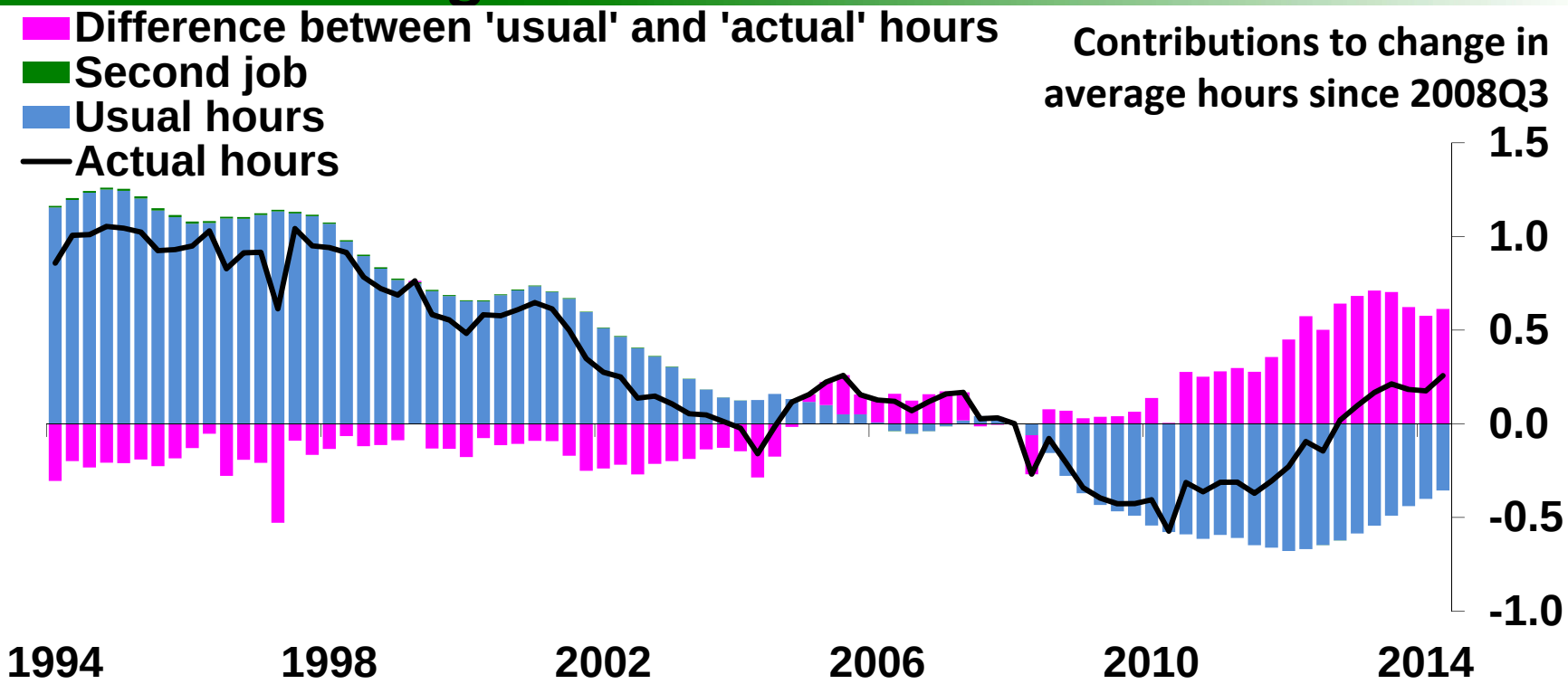
- Most of the increase in desired hours has come from part-timers.

Desired and subsequent actual change in average hours

Current status	Status four quarters ago: All — Under-employed	Fully-employed	Over-employed
Under-employed			
Desired change	13.5		-11.1
Actual change	1.1	-1.8	-9.3
Fully-employed			
Desired change	11.8		-11.7
Actual change	4.8	-0.1	-3.9
Over-employed			
Desired change	10.7		-11.6
Actual change	5.9	1.2	-1.1

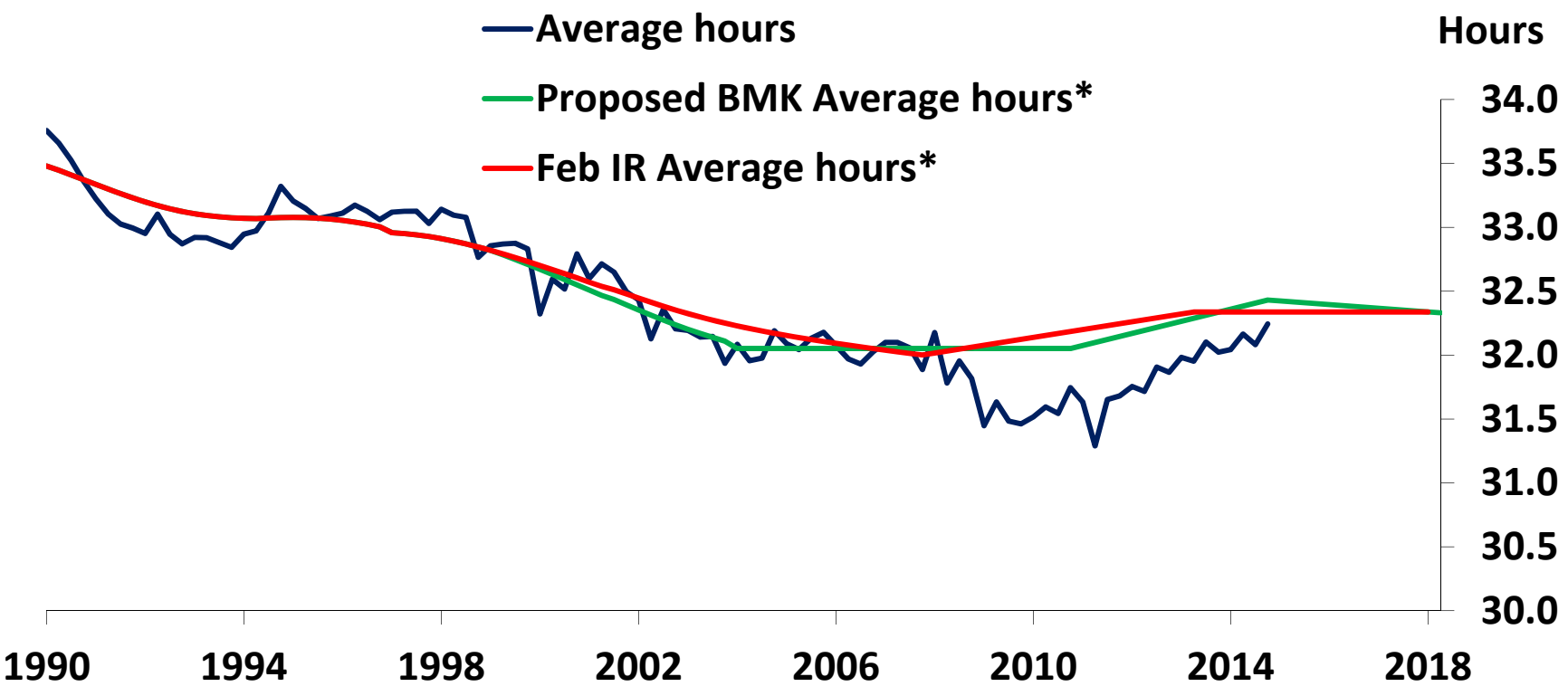
- **Workers happy with fewer hours than they say they want.**

Decomposition of actual average hours into 'usual' hours and wedge



- Usual hours have not picked up as much as actual hours due to people taking less holiday.

Trend average hours assumptions



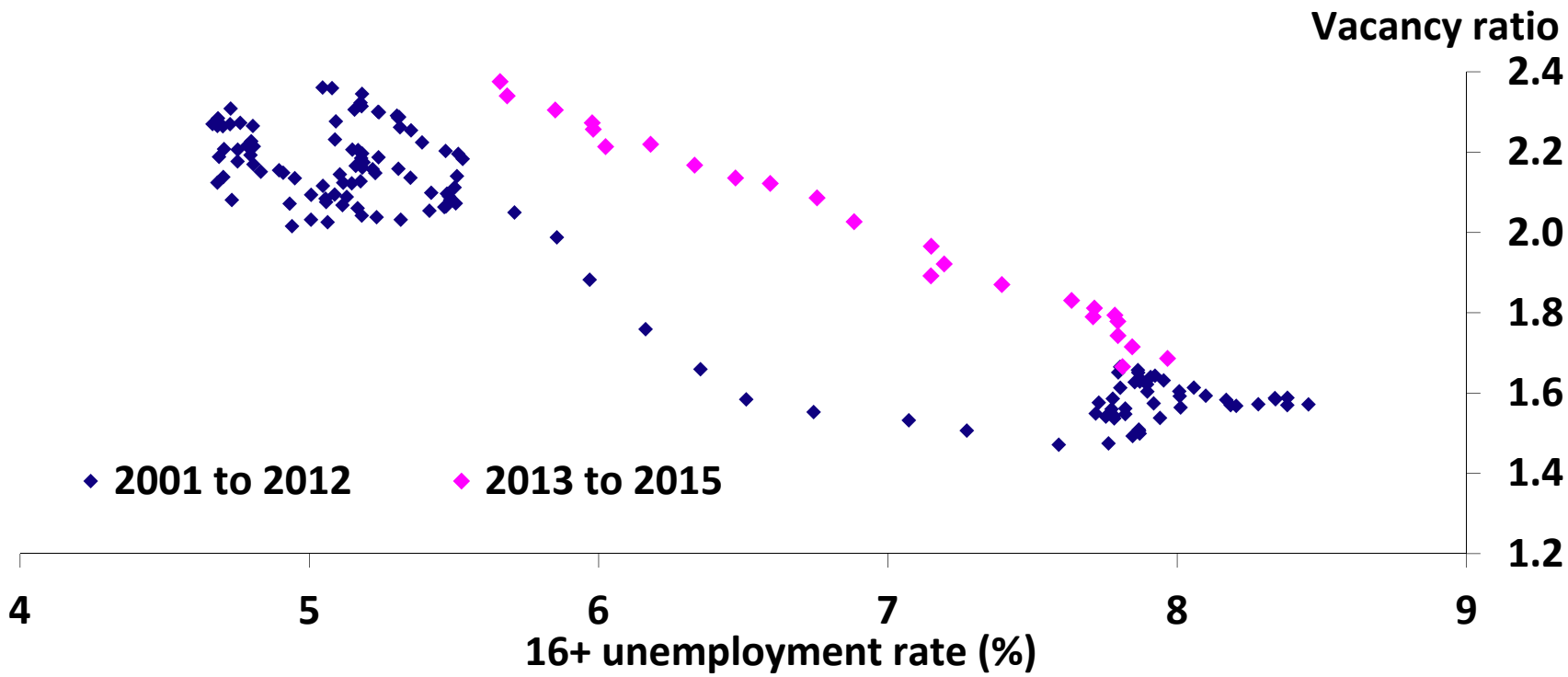
- **Proposed profile for average hours little changed.**

Risks to labour supply

	2015 Q1 gap		Main risks	Balance of risks
	Feb IR	BMK		
Participation	0.5pp	0.2pp	Whether trend increase in older participation or demographic drag from ageing population dominates.	
Average hours	0.1%	0.3%	More of the increase in desired hours could feed through to actual hours. Fall in amount of holiday taken could unwind, or longer-run downward trend could resume.	
Unemployment				
Population/ migration				

Unemployment

Beveridge curve



- Cyclical 'loops' in Beveridge curve make it harder to judge if equilibrium unemployment rate has changed.

Factors affecting the long-run equilibrium rate

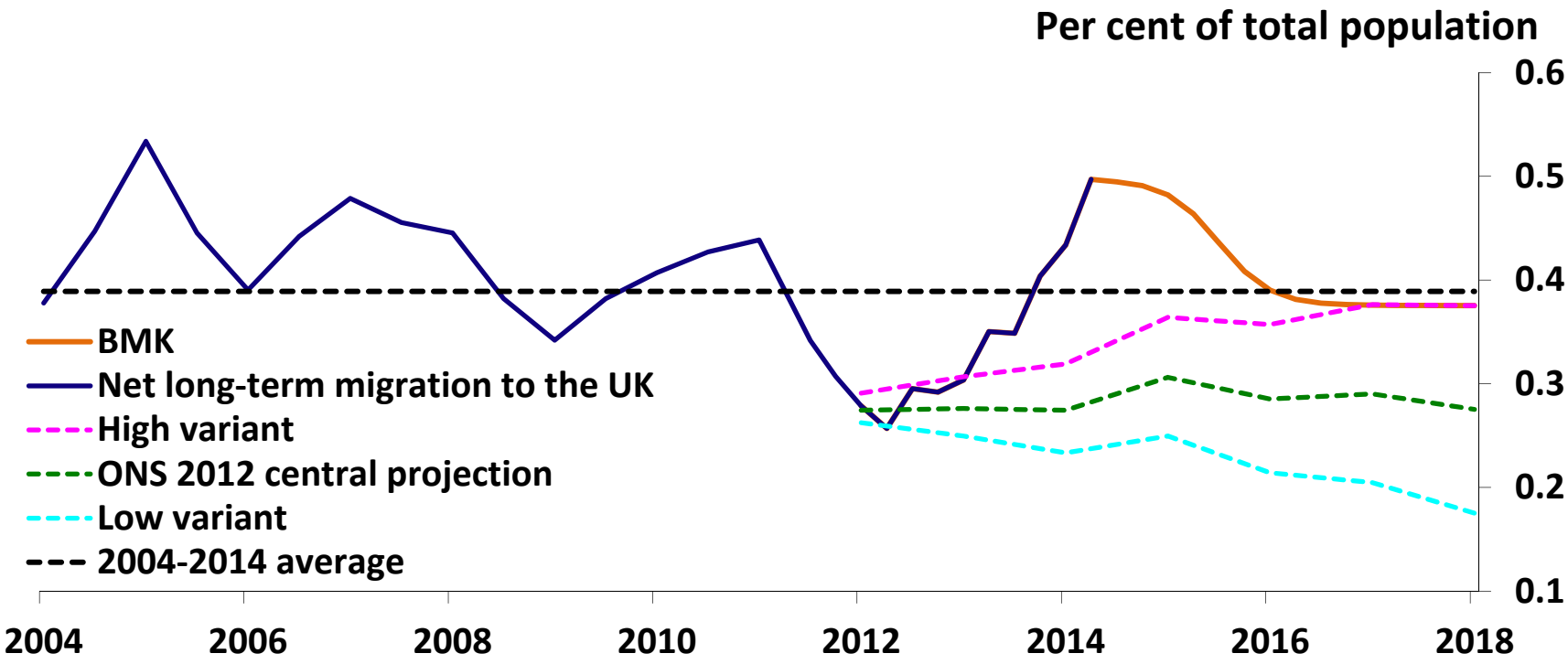
Factor	Risks to equilibrium unemployment
Demographics	↓
Changes to tax and benefit system	↑ ↓
Improved job search technology	↓
Recruitment difficulties/skills mismatch	↑
Regional/sectoral mismatch	↔

Risks to labour supply

	2015 Q1 gap		Main risks	Balance of risks
	Feb IR	BMK		
Participation	0.5pp	0.2pp	Whether trend increase in older participation or demographic drag from ageing population dominates.	⬌
Average hours	0.1%	0.3%	More of the increase in desired hours could feed through to actual hours. Fall in amount of holiday taken could unwind, or longer-run downward trend could resume.	⬌
Unemployment	0.3pp	0.2pp	Structural factors such as demographics and changes to tax and benefit system could reduce equilibrium unemployment. Pickup in recruitment difficulties potentially signals less slack.	⬆ (for labour supply)
Population/ migration				

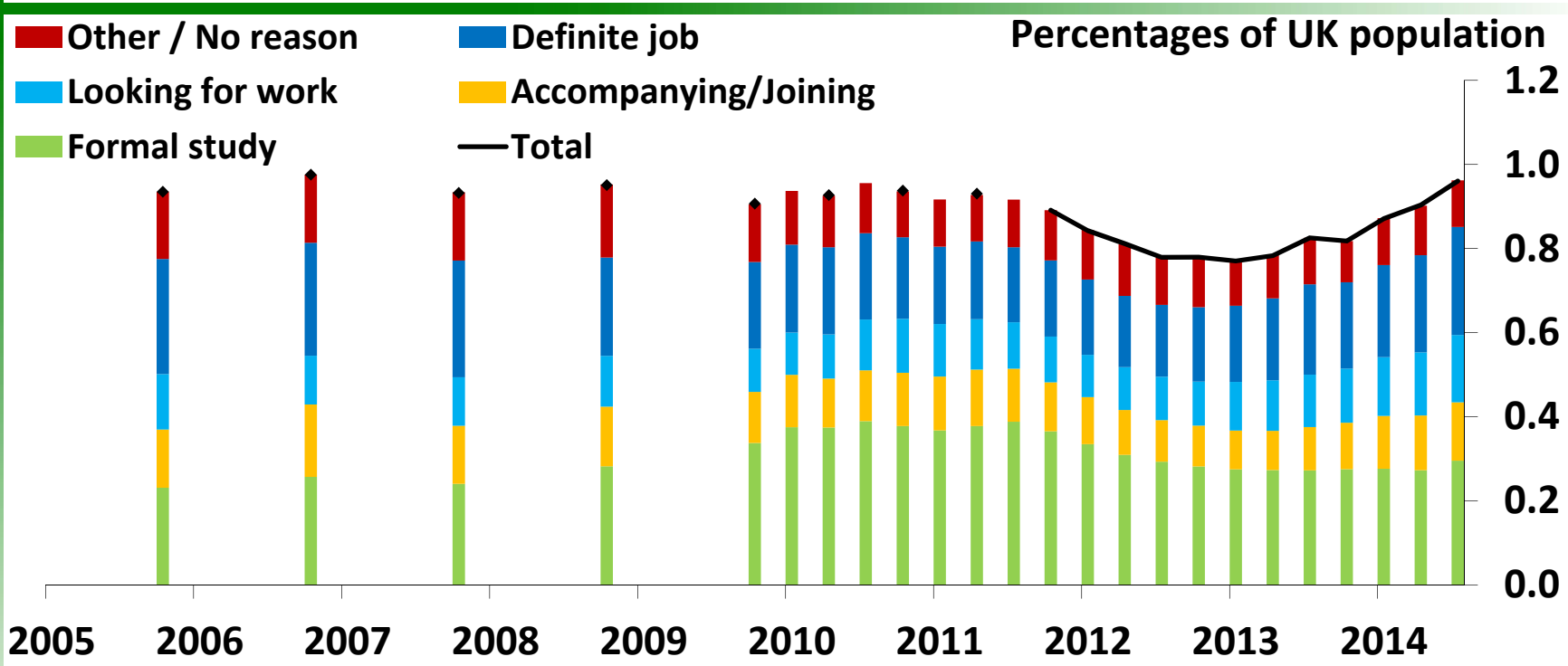
Population

Migration BMK projection



- **Recent strength of migration assumed to push population up by an extra 0.7% by 2018.**

Gross inward migration by reason



- ‘Latent’ slack effects from pool of potential overseas workers may be small.

Risks to labour supply

	2015 Q1 gap		Main risks	Balance of risks
	Feb IR	BMK		
Participation	0.5pp	0.2pp	Whether trend increase in older participation or demographic drag from ageing population dominates.	⇔
Average hours	0.1%	0.3%	More of the increase in desired hours could feed through to actual hours. Fall in amount of holiday taken could unwind, or longer-run downward trend could resume.	⇔
Unemployment	0.3pp	0.2pp	Structural factors such as demographics and changes to tax and benefit system could reduce equilibrium unemployment. Pickup in recruitment difficulties potentially signals less slack.	↑ (for labour supply)
Population/ migration		+0.3%	Migration could remain at high levels or fall back more sharply depending on UK labour market performance relative to those abroad.	⇔

Contributions to the output gap

	Feb IR		May BMK	
	Q1	Q2	Q1	Q2
U gap	-0.2	-0.2	-0.2	-0.1
AVH gap	0.0	0.0	-0.3	-0.2
LP gap	-0.6	-0.5	-0.2	-0.1
CAPU	0.3	0.2	0.2	0.2
Total	**-0.6**	**-0.5**	**-0.4**	**-0.3**

Key messages

- **Expecting a return to historically average productivity growth rates is reasonable.**
- **Productivity just as puzzling as it was a year ago. But some signs of an easing in resource allocation bottlenecks.**
- **Little labour market slack to support growth in the absence of a recovery in productivity (or pickup in wage and price pressures).**
- **Staff estimate of the output gap a bit reduced over the past o/a lower trend participation.**
- **Highlights need to reconsider the outlook for wage growth. (Possible effect from stronger migration but probably not that large.)**

End

Costs and Prices

2 April 2015

Structural Economic Analysis Division

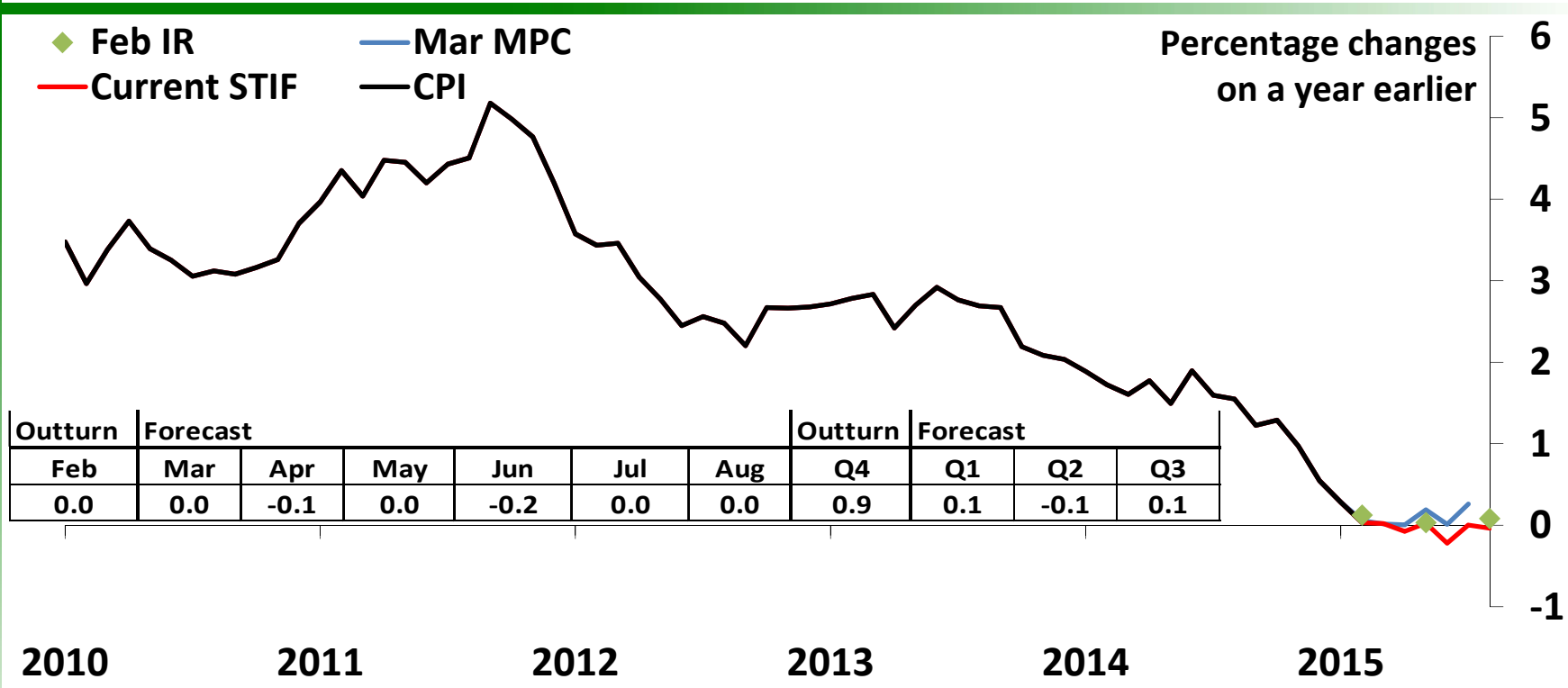
Main messages

- **Inflation is very low, but the recent falls are most likely being driven by external factors that should ultimately prove to be temporary.**

- **Pay growth was a bit lower than expected and we have revised down our near-term forecast slightly. There are many factors that could explain the weakness in pay.**

Inflation

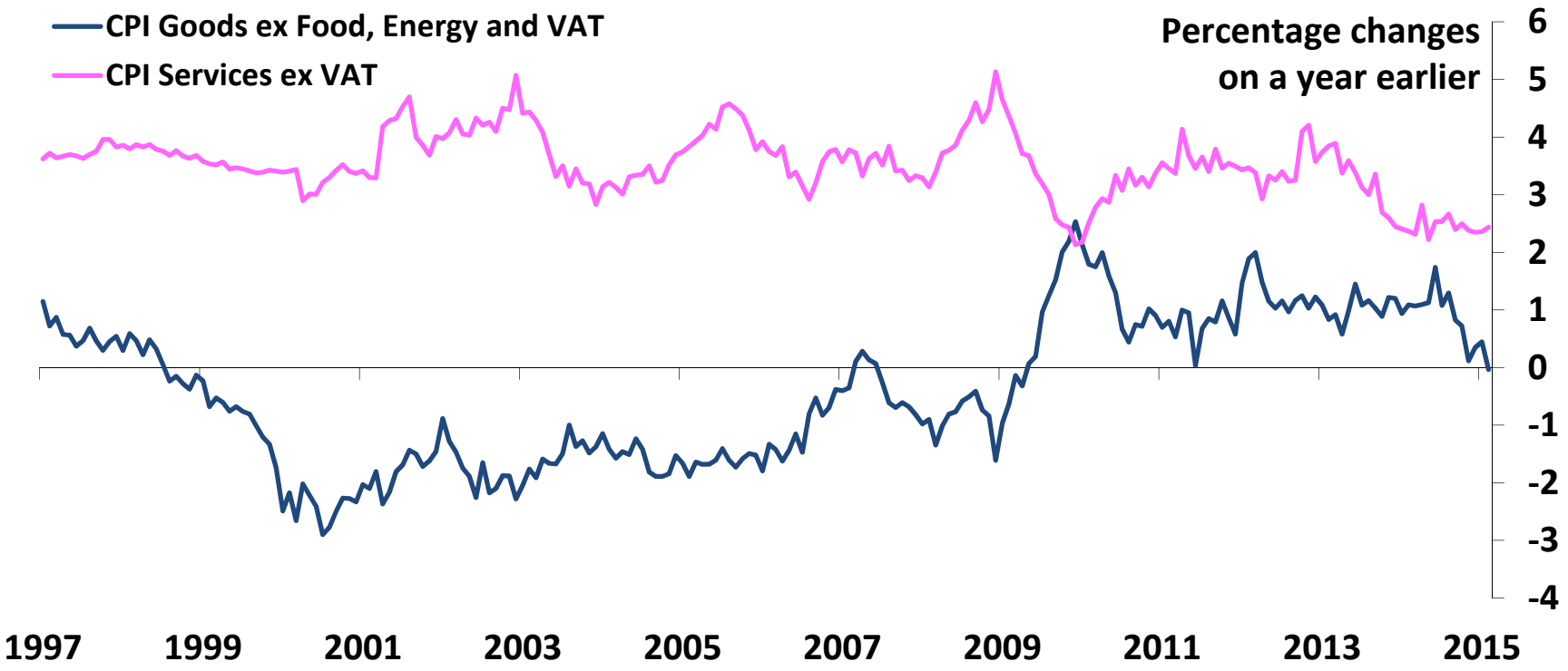
Short-term inflation forecast



Outturn	Forecast						Outturn	Forecast		
Feb	Mar	Apr	May	Jun	Jul	Aug	Q4	Q1	Q2	Q3
0.0	0.0	-0.1	0.0	-0.2	0.0	0.0	0.9	0.1	-0.1	0.1

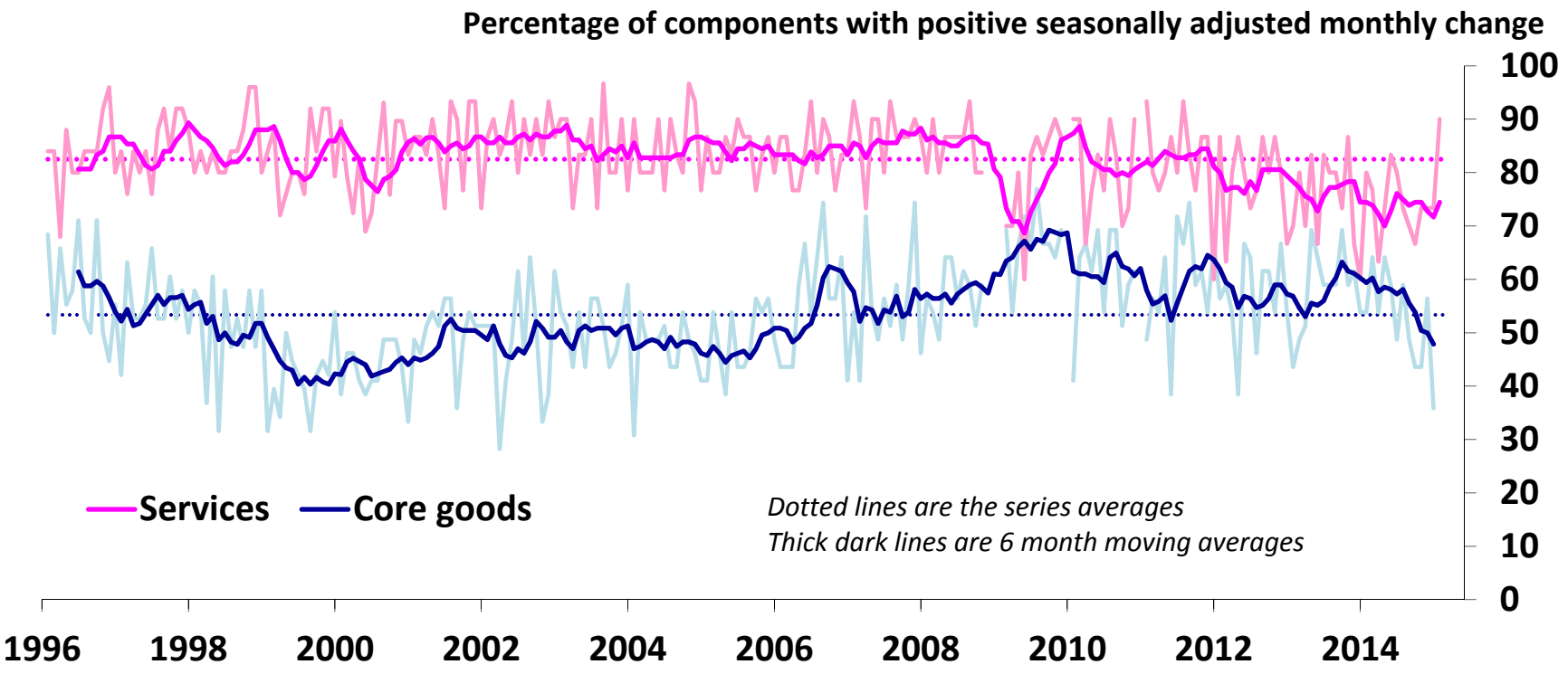
- **Inflation fell to 0% in February. STIF is 0.1pp lower than last month, but the Q3 forecast is in line with the Feb IR.**

Goods and services inflation



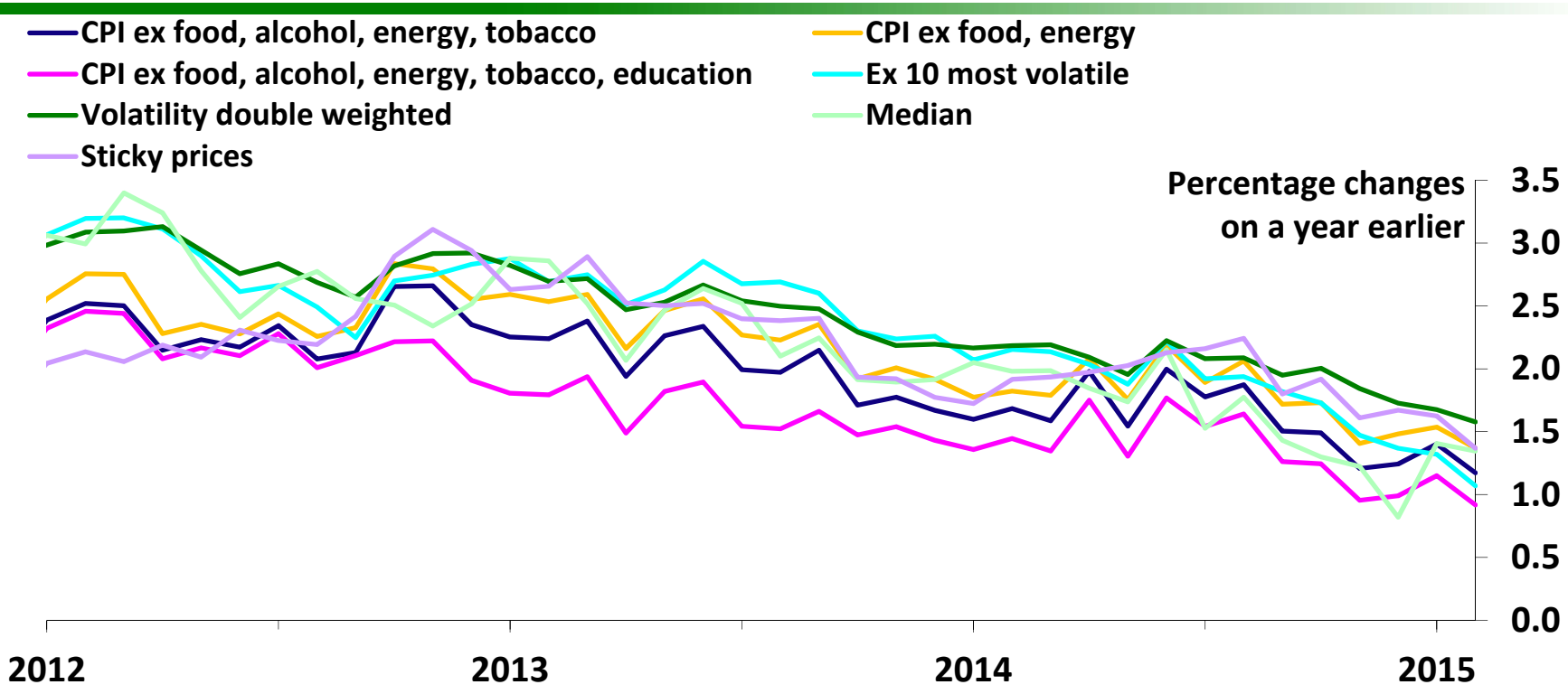
- **Core goods inflation has fallen sharply, which likely reflects sterling's appreciation.**

Diffusion indices



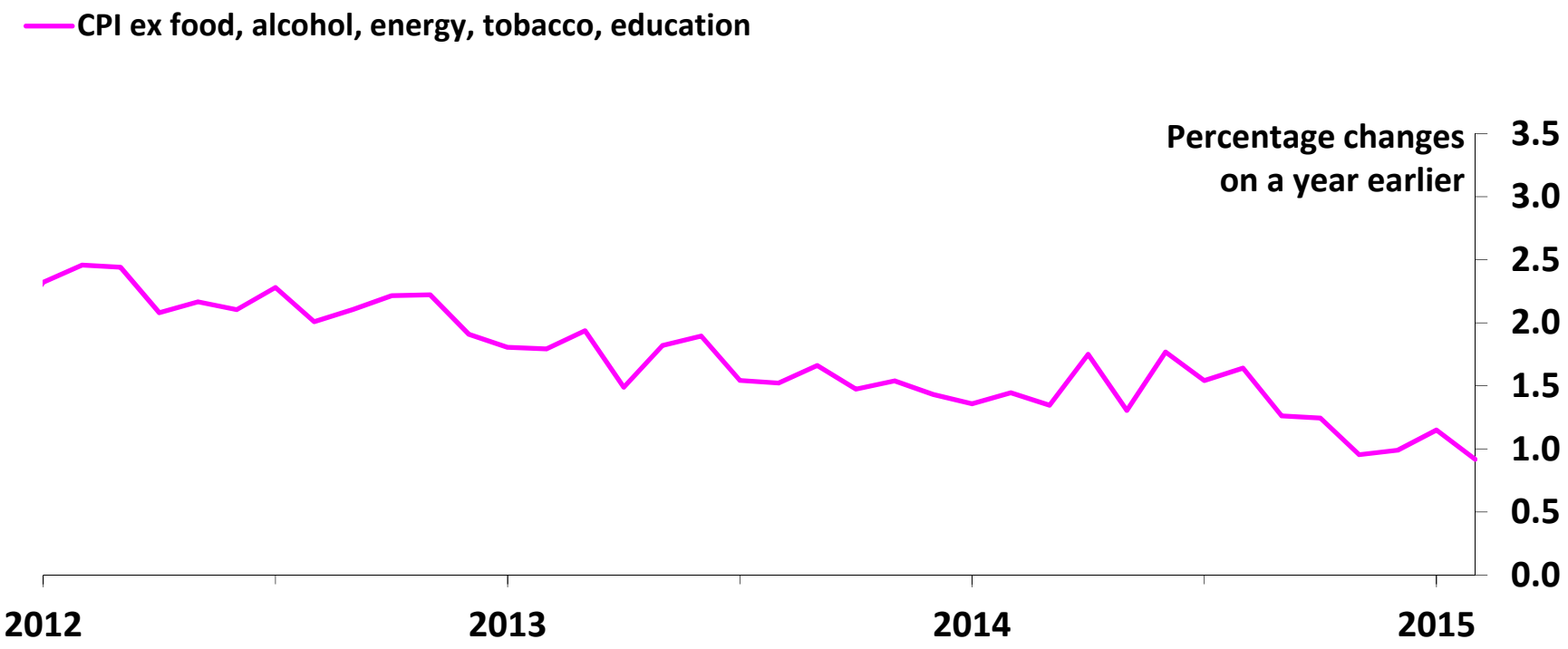
- **The proportion of goods prices that are rising has declined.**

Measures of core inflation



- **Core inflation measures are drifting down, this may reflect lower import prices.**

Measures of core inflation



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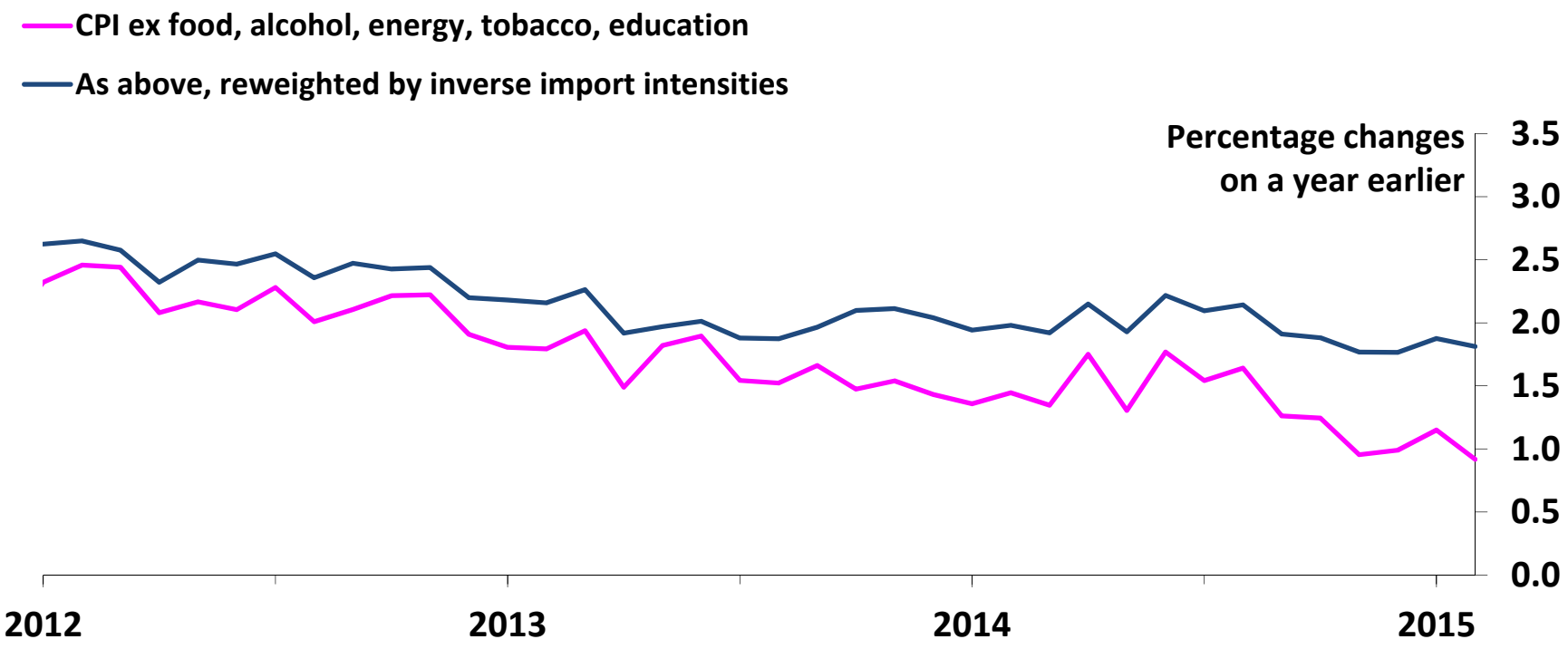
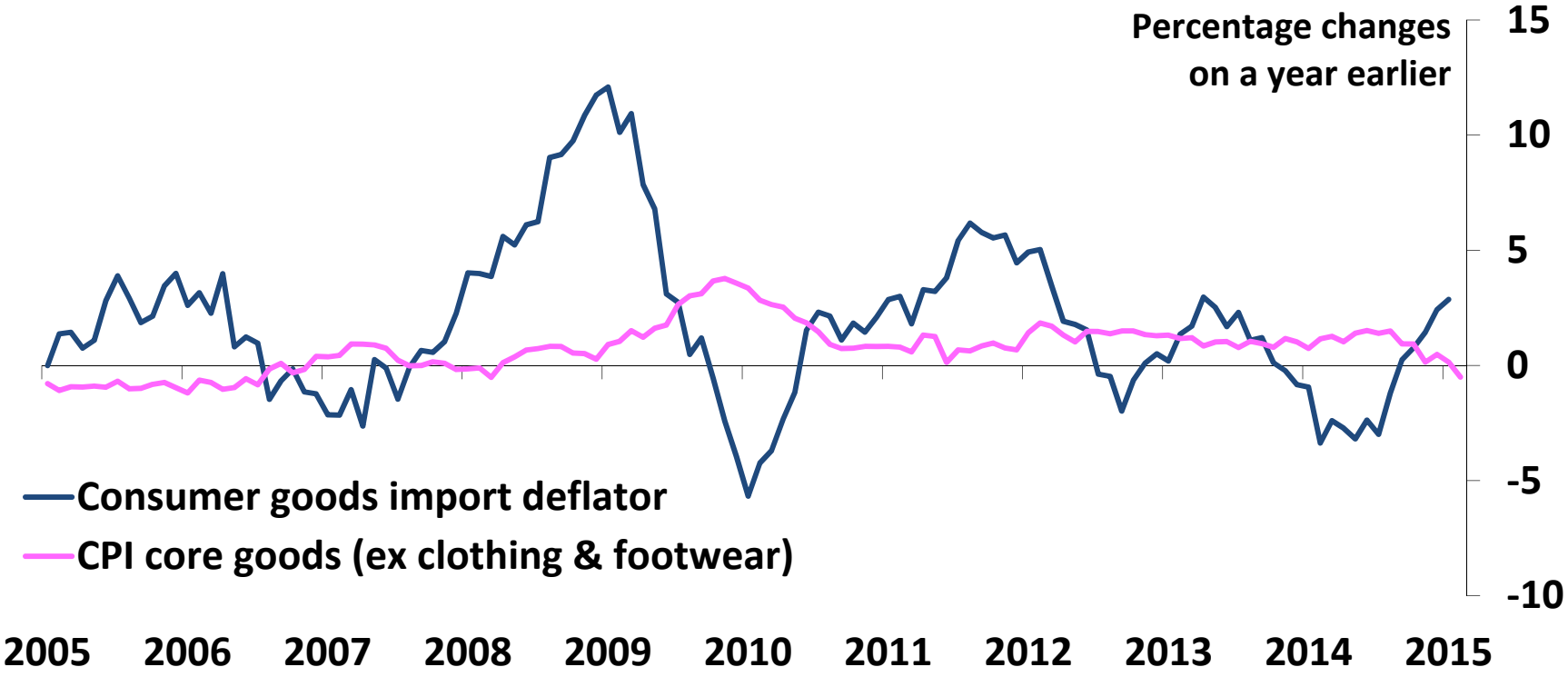
Measures of core inflation



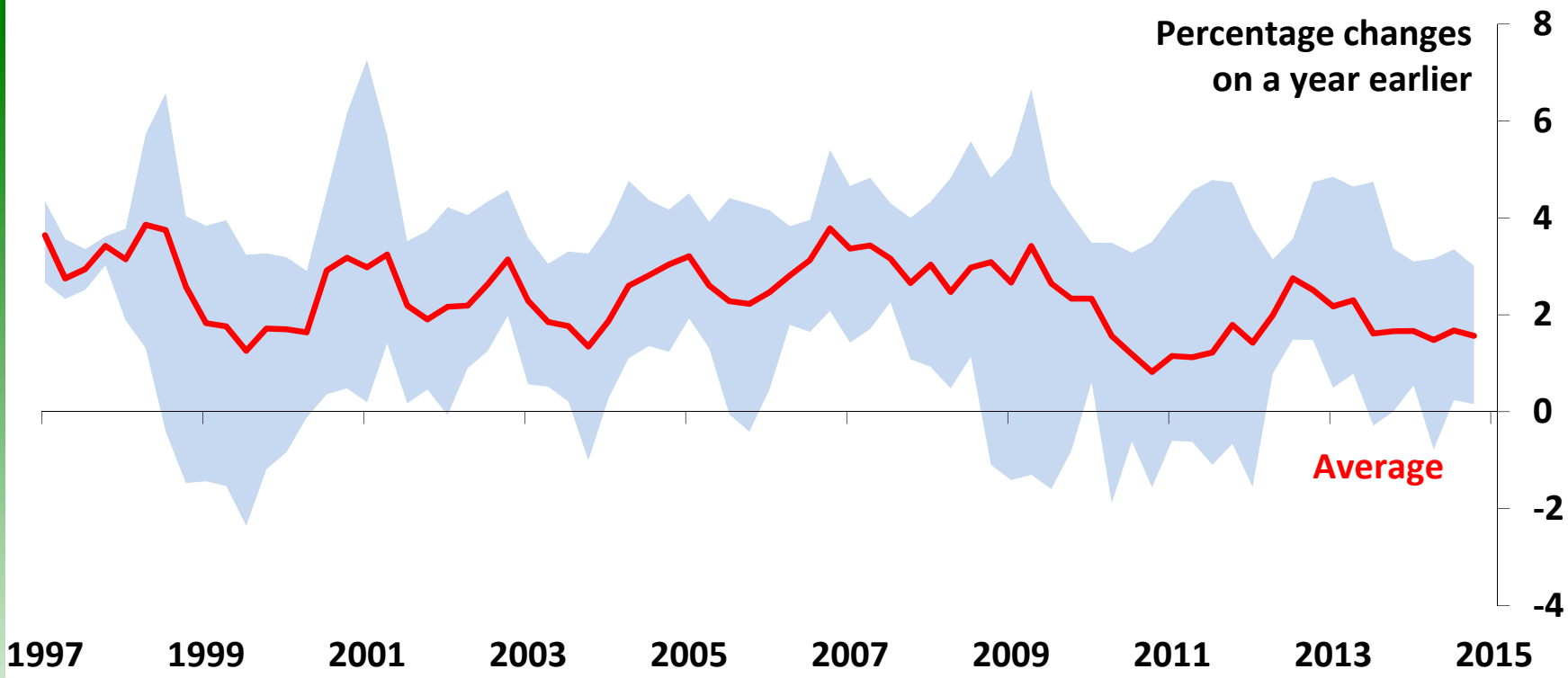
- **A measure of core inflation with a lower weight on imported goods is more stable.**

Core goods



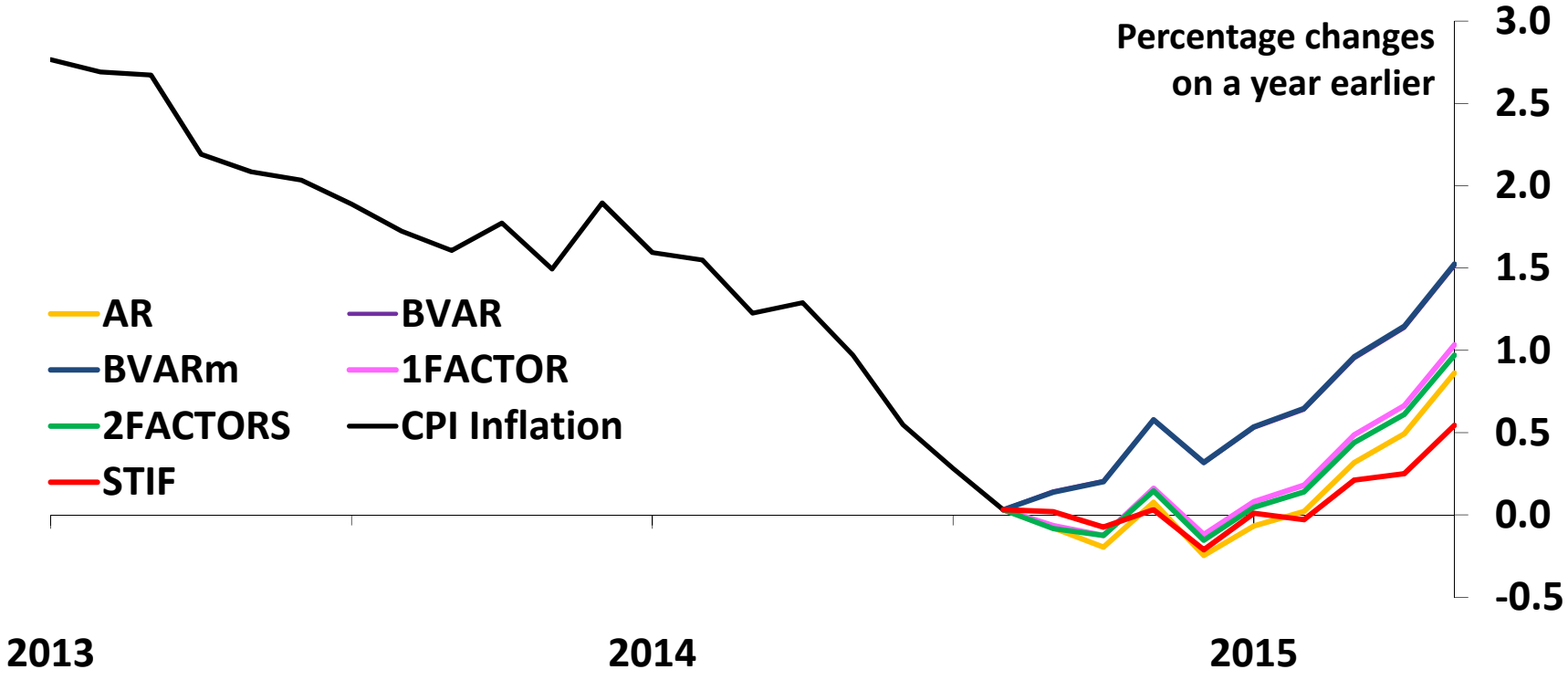
- **Goods inflation was unexpectedly strong, but is now falling back.**

DGI Swathe



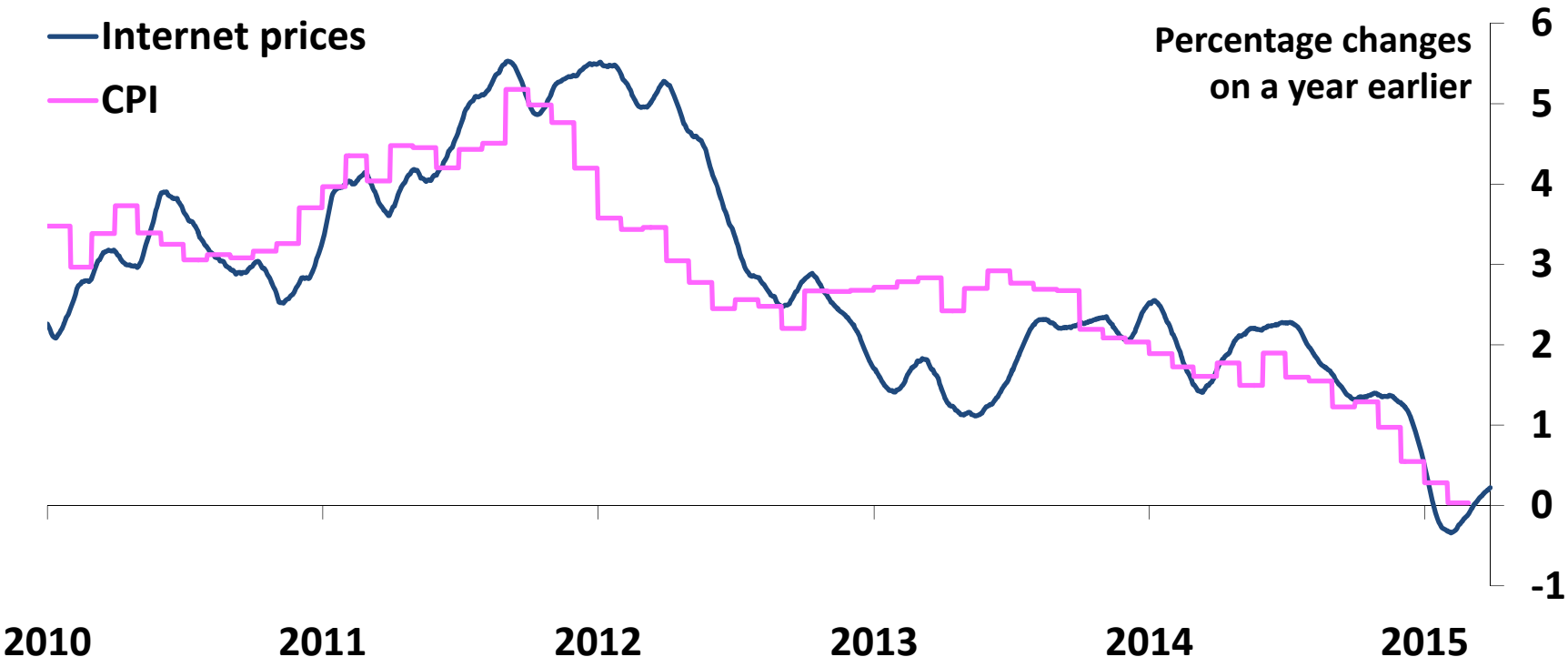
- **Measures of DGI have, on average, been stable.**

Statistical suite of models



- Other models also point to a pick up in inflation.

Internet price growth



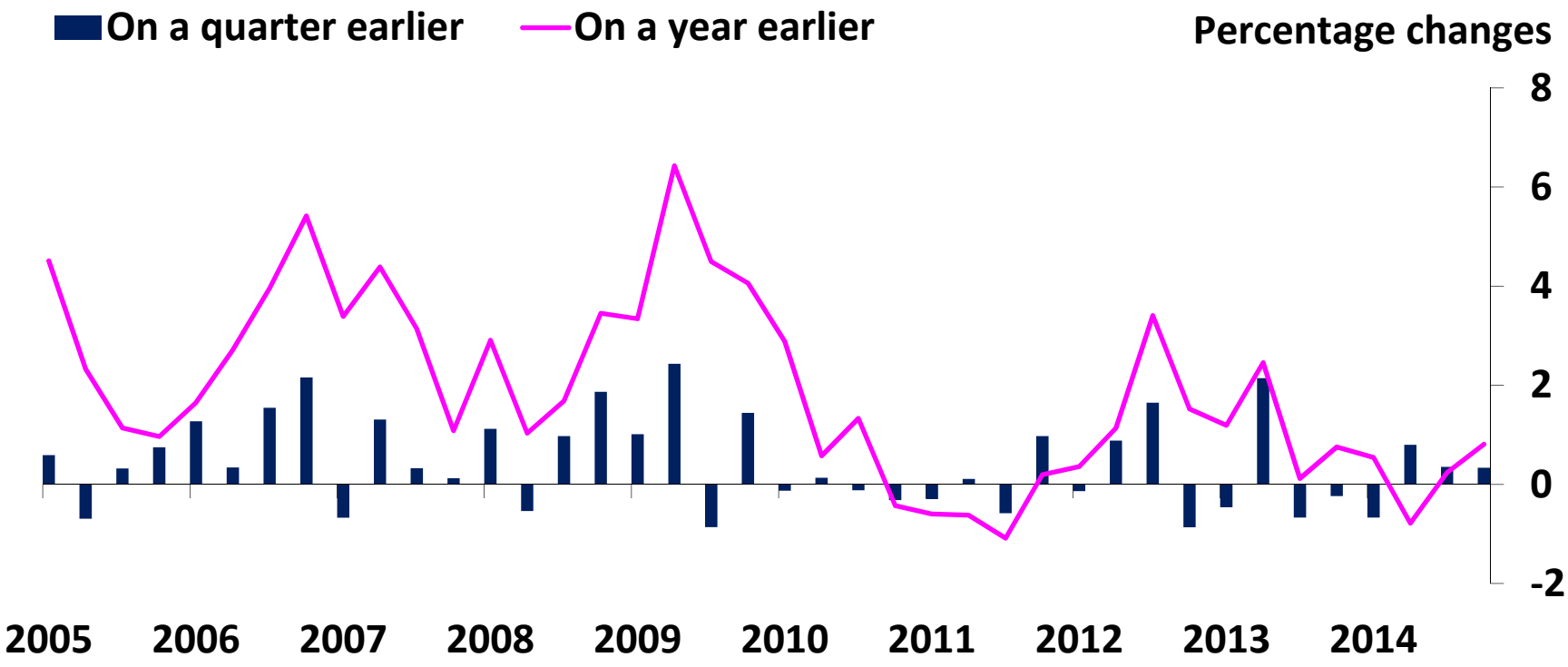
- And data from the Billion Prices Project suggest UK inflation may be bottoming out.

Main messages

- **Inflation is very low, but the recent falls are most likely being driven by external factors that should ultimately prove to be temporary.**

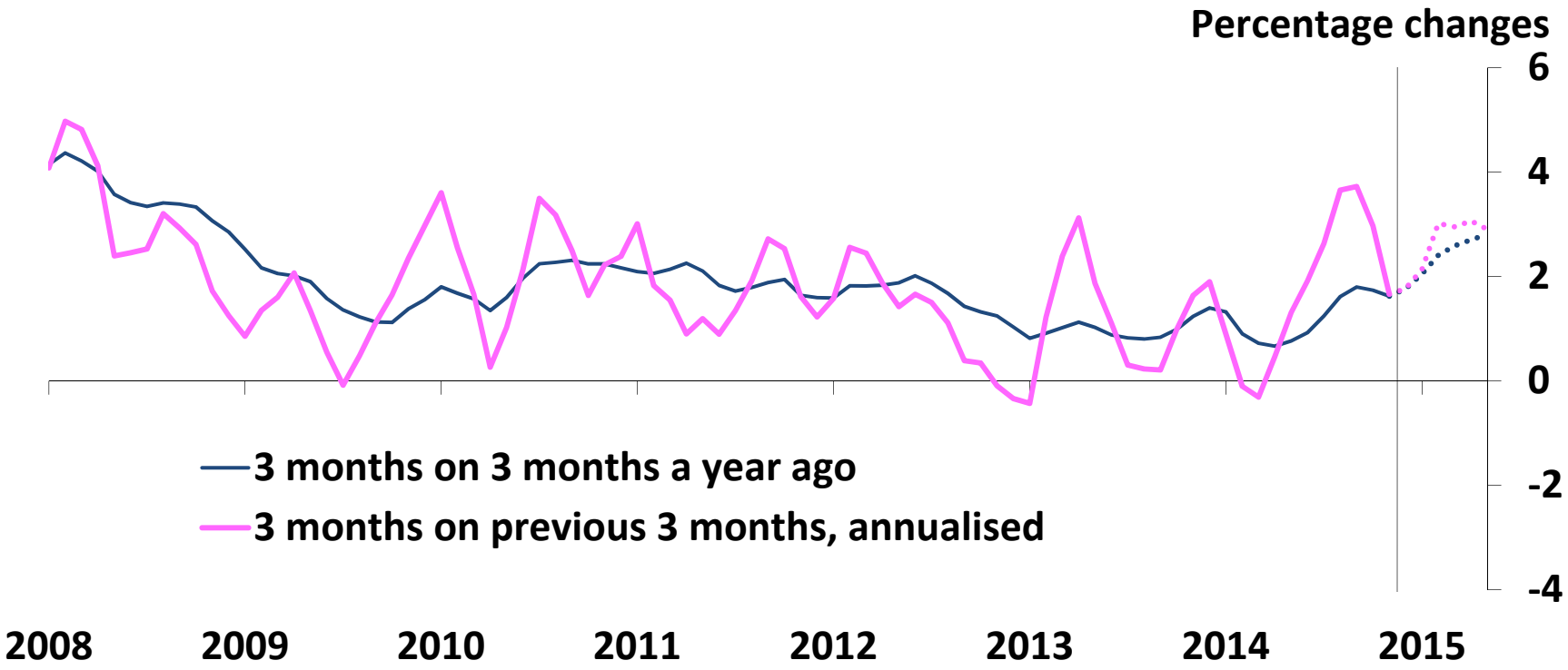
Wages and ULCs

Whole economy unit labour costs



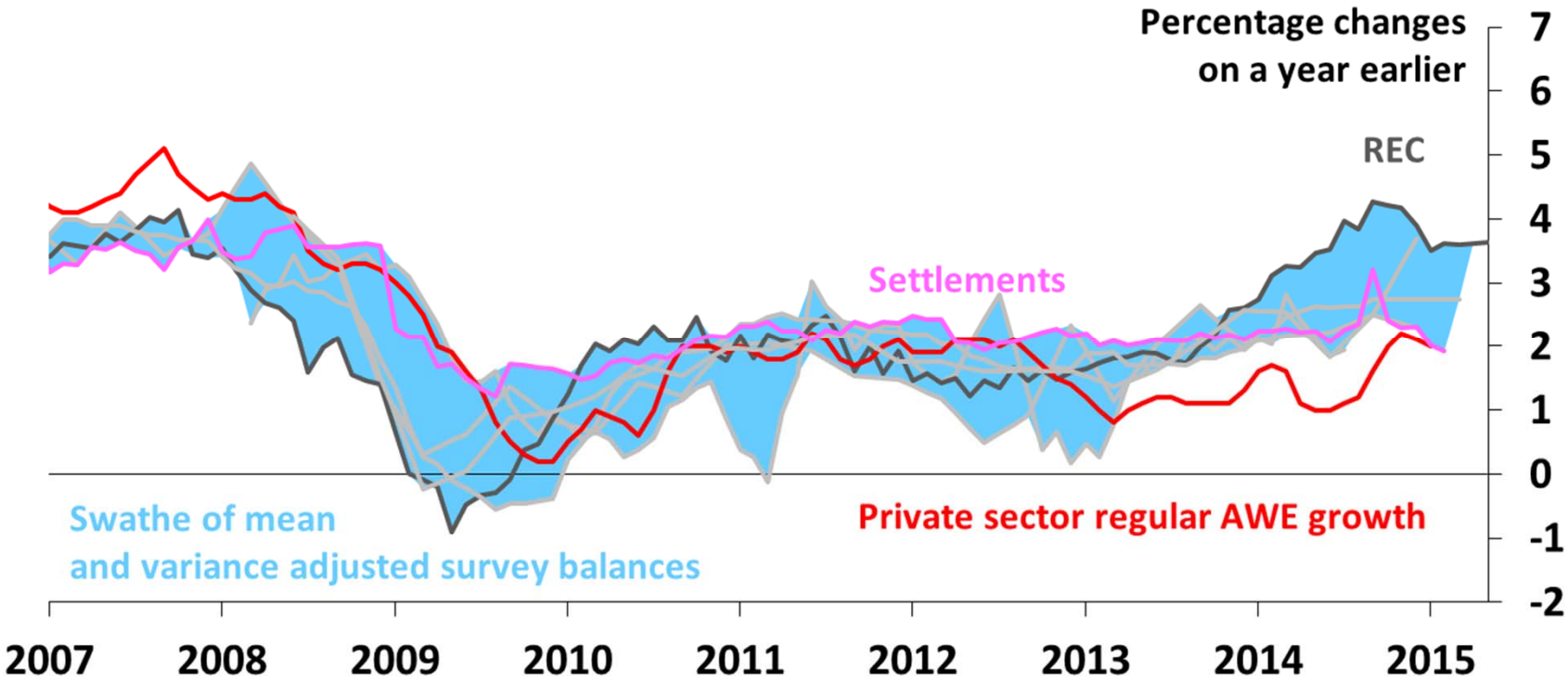
- **Unit labour costs rose 0.3% in Q4 and are up 0.8% on a year ago.**

Whole economy regular pay growth



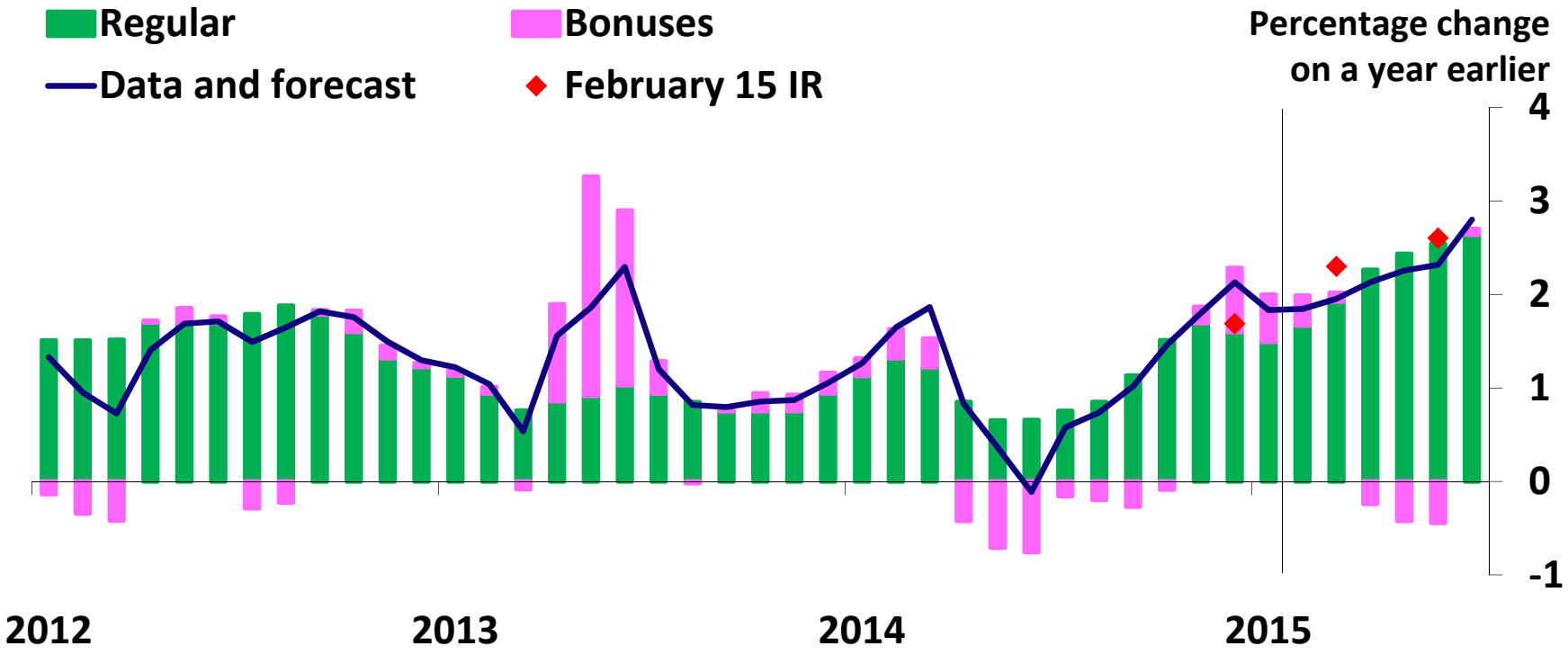
- Annual regular pay growth was 1.6% in the three months to January.

Earnings swathe



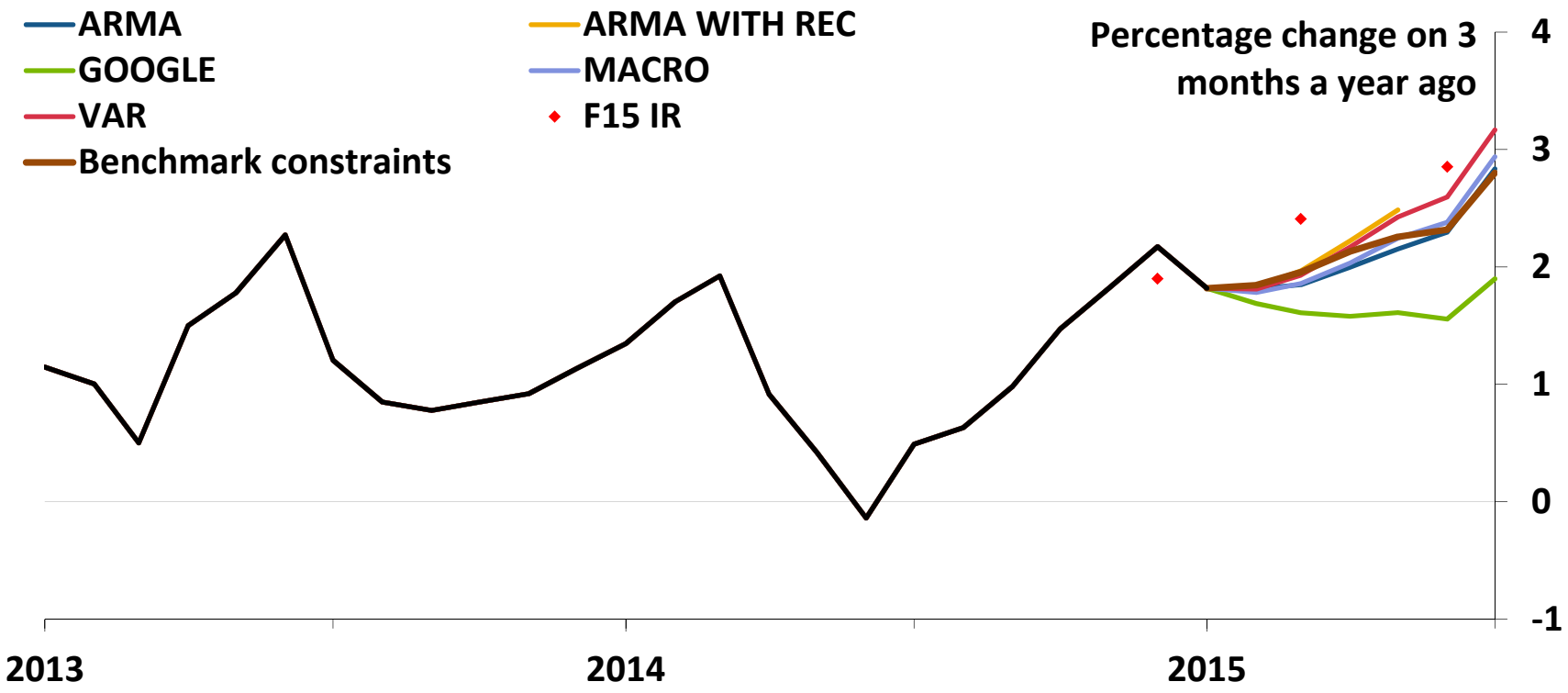
- **Other indicators of pay growth are broadly stable.**

Whole economy total pay growth



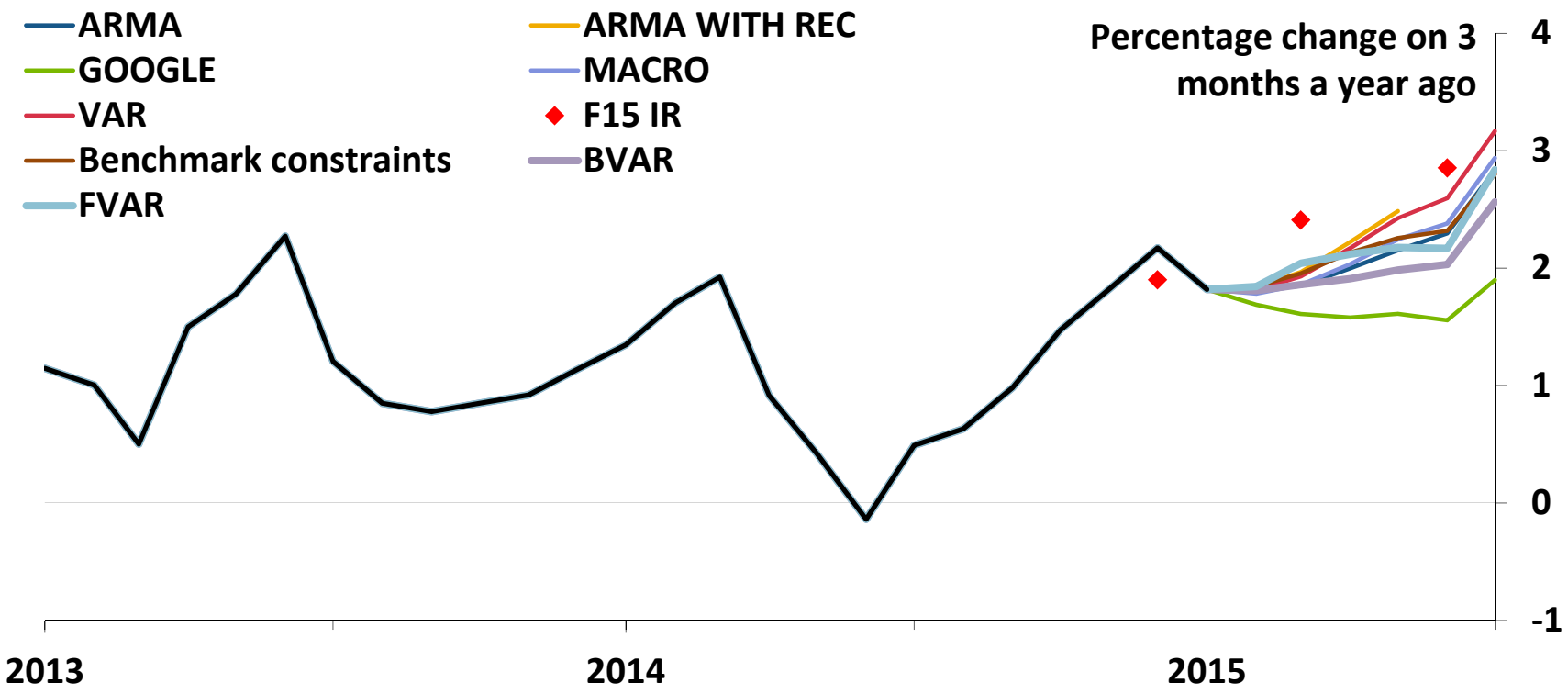
- We've revised down our near-term forecast slightly relative to the Feb IR.

Short-term earnings forecast



- **Our short-term forecasting suite points to a further rise in pay growth.**

Short-term earnings forecast



- And some new models support that picture.

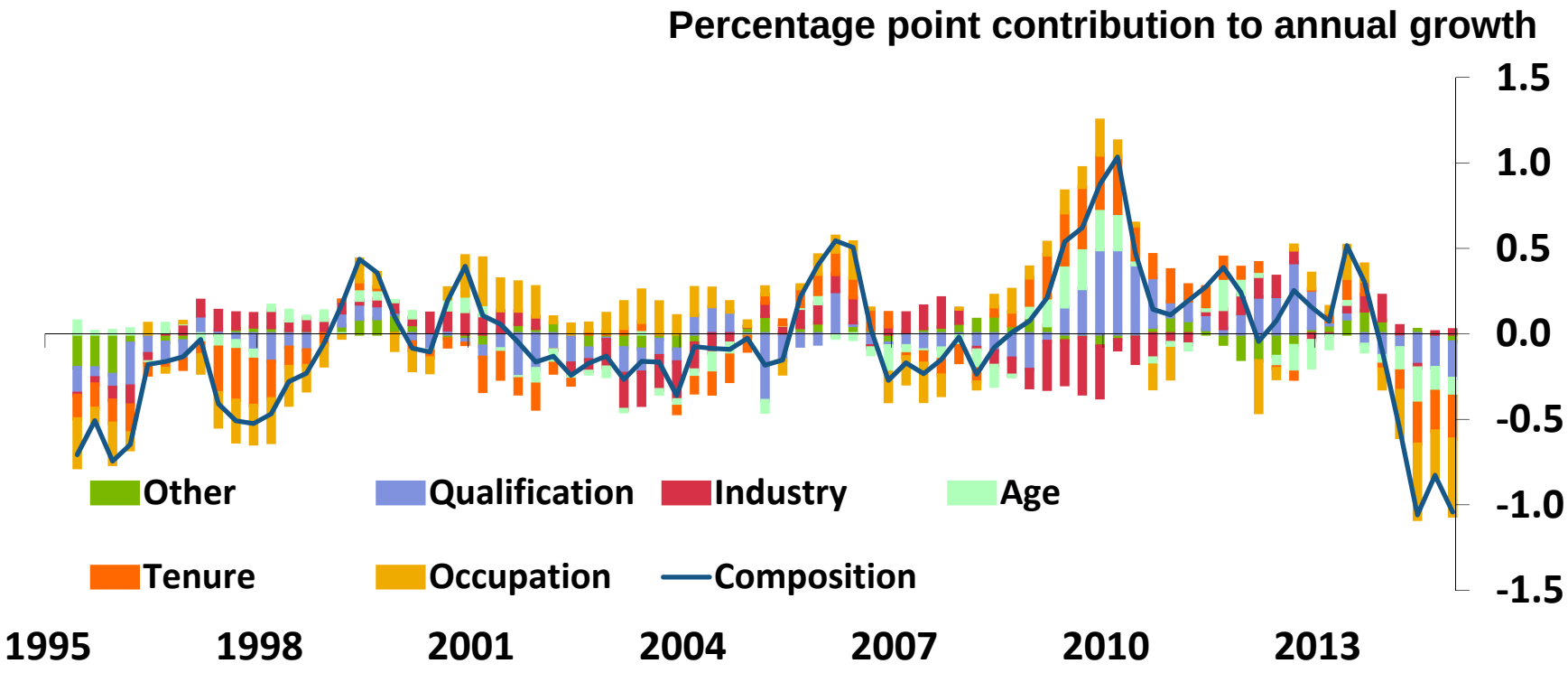
Possible reasons for unexplained weakness in wages

Category	Possible causes
More slack than we've assumed	Incorrectly estimating equilibrium unemployment, participation or average hours, or missing the effect of foreign job searchers
Unusually long lags from slack	Employees not yet bidding for higher pay or changing jobs
Low inflation expectations or more of a drag from expected productivity weakness	Record low CPI inflation, productivity growth remains weak throughout forecast
Wedge effects (real wage resistance)	Import prices, pension costs, and taxes
Structural changes in labour share	Movements in reservation wages, e.g. because of the public sector pay freeze; changes in competition in product markets; international downward trend in labour share
Measurement issues	Mis-measurement of wages or productivity; differences between average and marginal pay; compositional effects
Pent up wage deflation	Lagged effect of nominal wage rigidities that prevented earlier adjustment

Private sector job-to-job flows

- **Job-to-job flows are picking up but remain below normal and may account for slow response of wages to a tightening labour market.**

Compositional effects



- **Compositional effects are still dragging on annual pay growth.**

Possible reasons for unexplained weakness in wages

Category	Possible causes
More slack than we've assumed	Incorrectly estimating equilibrium unemployment, participation or average hours, or missing the effect of foreign job searchers
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Measurement issues	Mis-measurement of wages or productivity; differences between average and marginal pay; compositional effects
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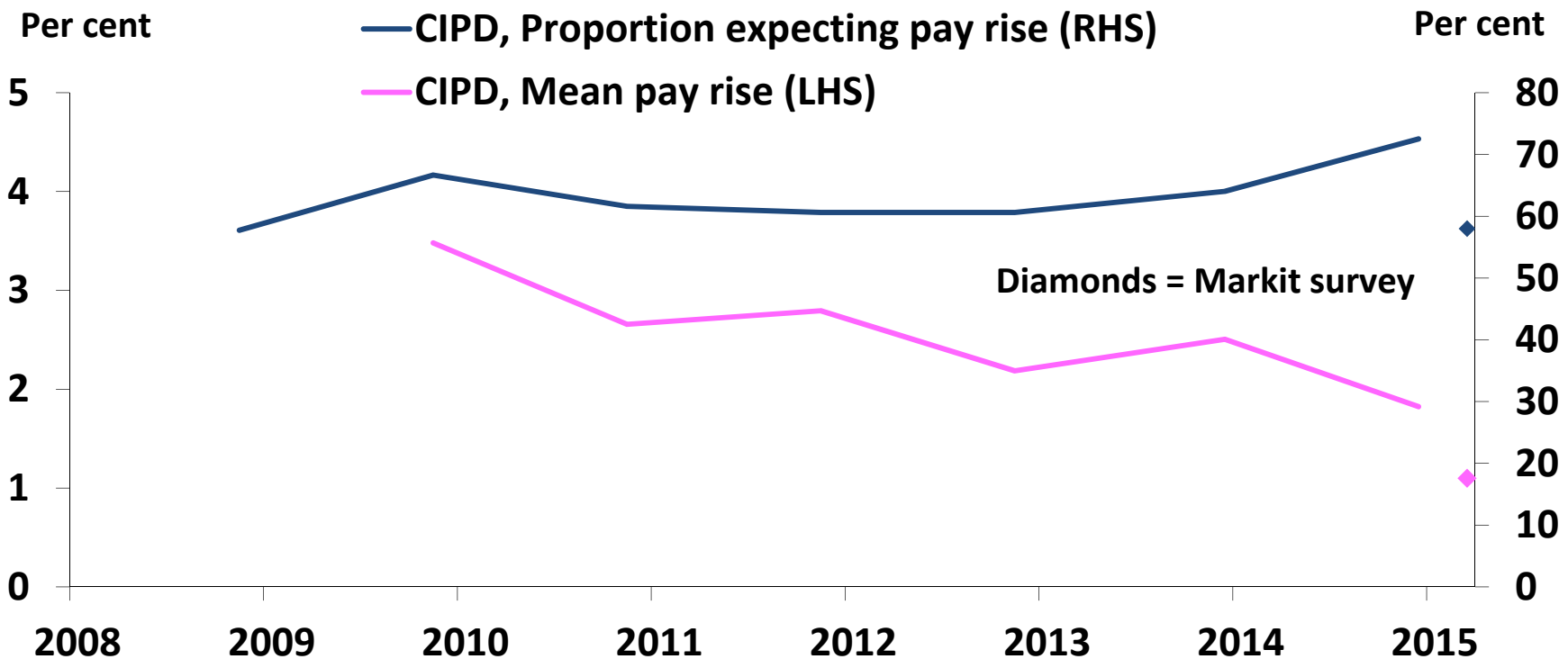
Employee pay expectations



- **Households pay expectations appear to have weakened.**

Main messages

- **Inflation is very low, but the recent falls are most likely being driven by external factors that should ultimately prove to be temporary.**

- **Pay growth was a bit lower than expected and we have revised down our near-term forecast slightly. There are many factors that could explain the weakness in pay.**

THE END

Agents' Corporate Pricing Survey

2 April 2015

Inflation Report & Agency Intelligence Division

UK Corporate Pricing Survey

We asked questions to understand:-

- **Expectations for corporates' UK sales price inflation**
- **The factors influencing price inflation**
- **Current margins compared to 'normal'**
- **The use of hedging for fx and input costs**

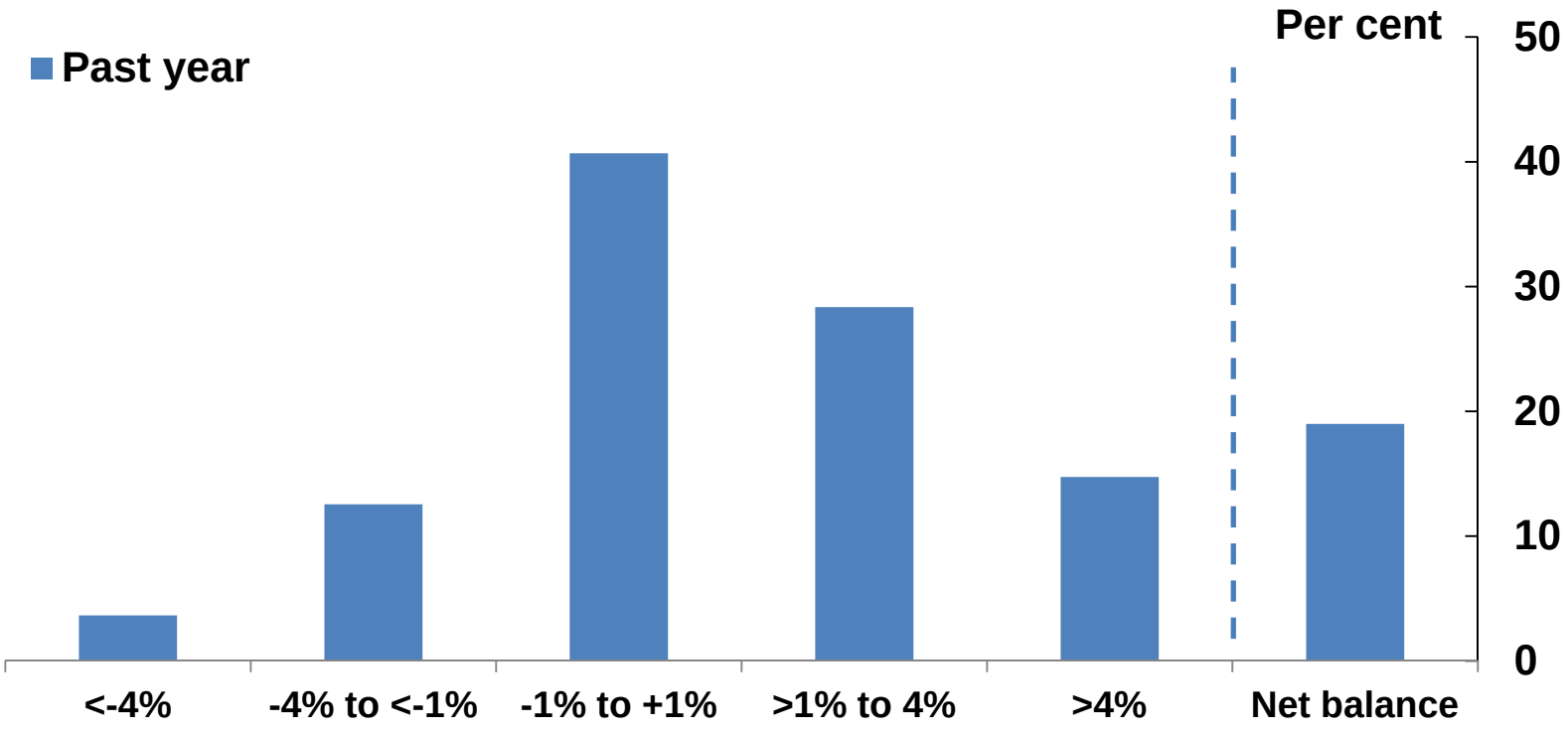
Main messages

- **Pricing expectations remain positive but are a little weaker than price changes made in past year**

- **Most influences were having a dampening effect on price inflation for the year ahead, the exception is where companies want to rebuild margins**

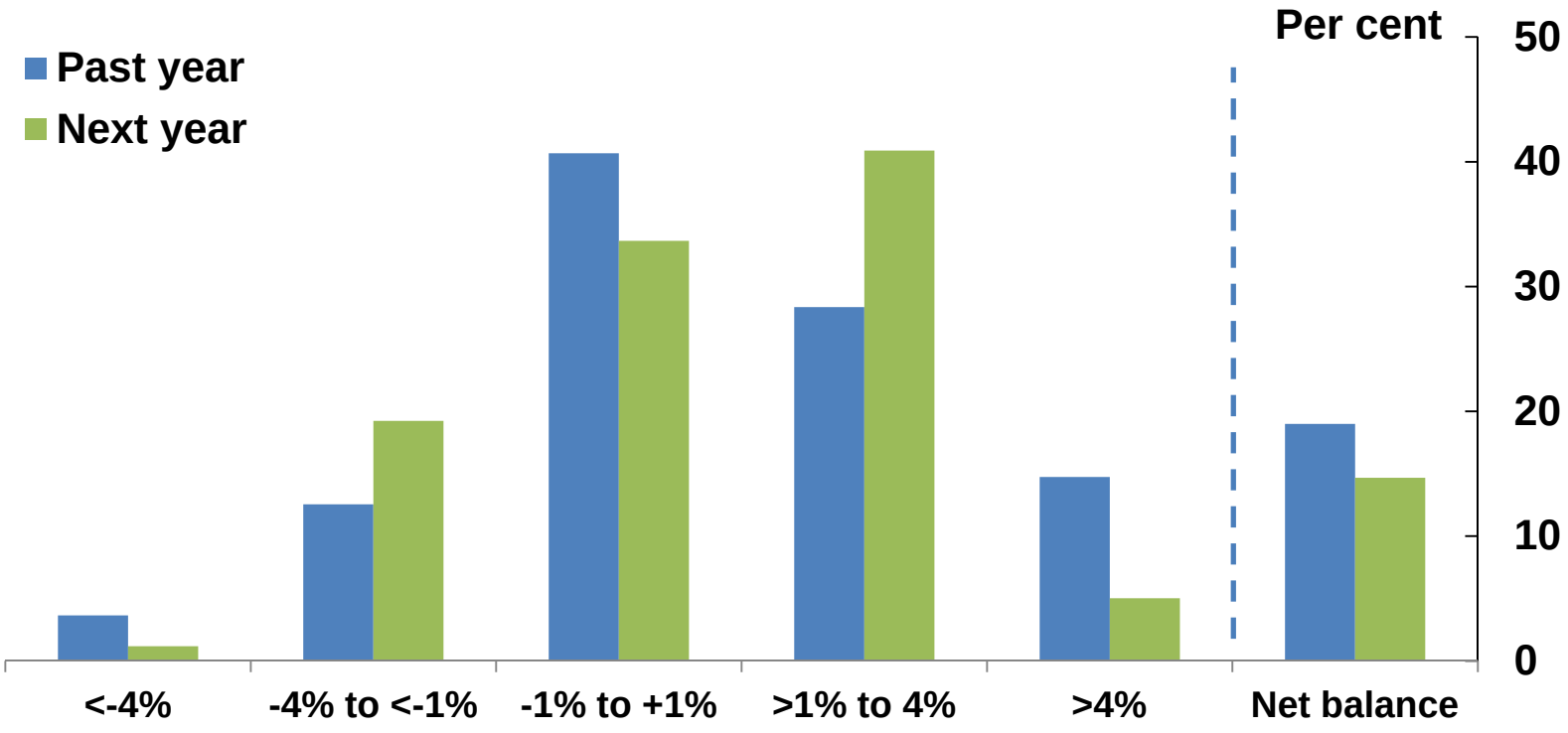
- **A significant minority of companies report margins below normal**

Price changes over last year



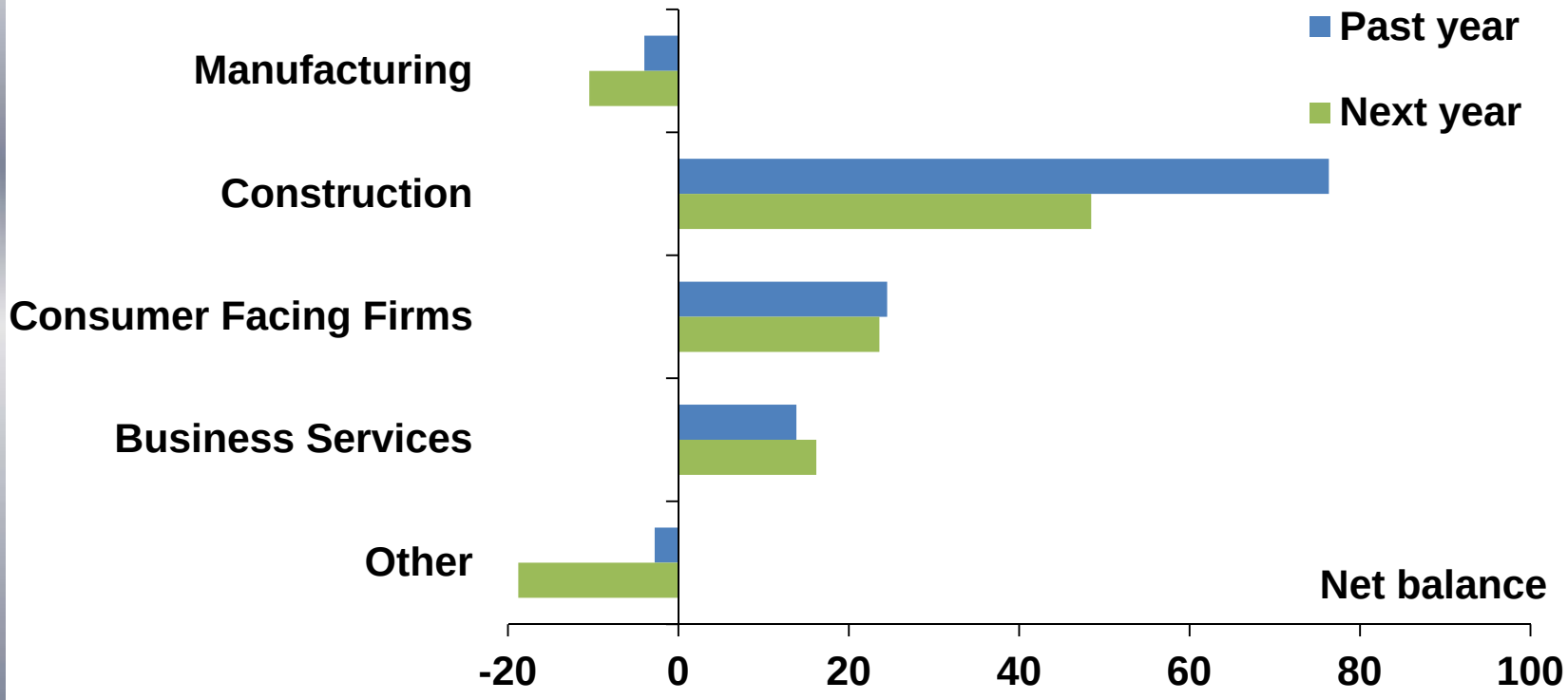
- Steady increase in pricing over past year

Corporates' expectations for their sales price inflation in the year ahead



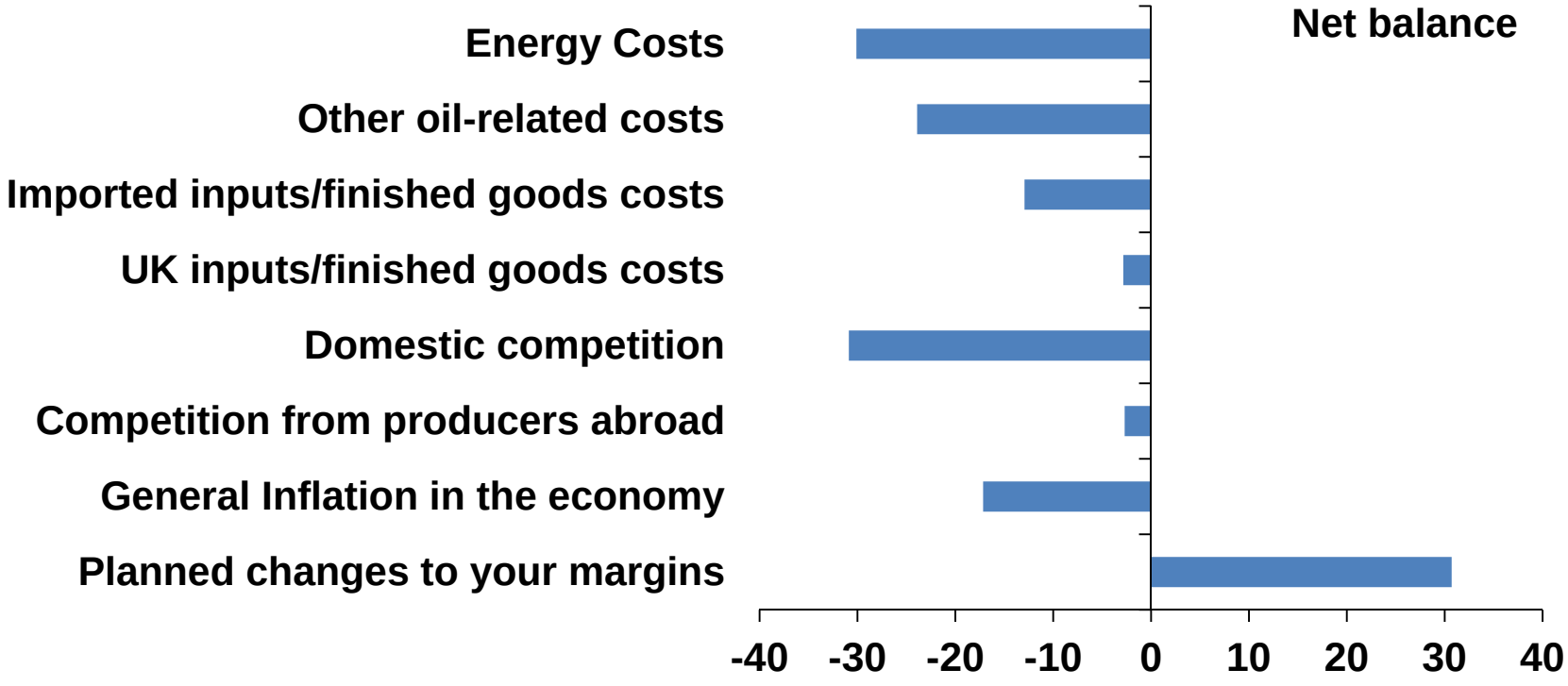
- Price inflation expectations remain positive, but weaker than in the past year

Pricing - net balances by sector



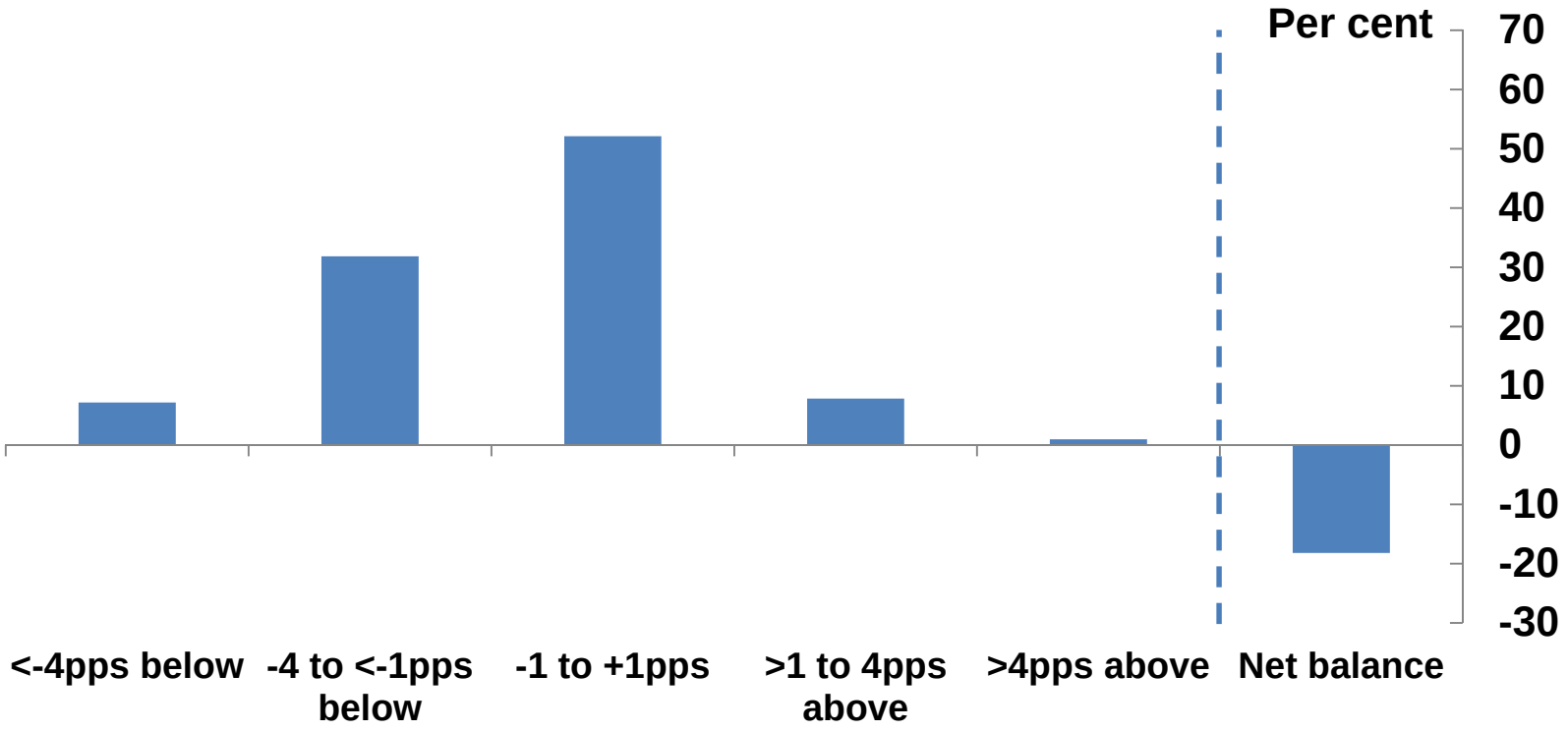
- Construction firms expecting smaller price increases this year

Factors influencing change in output price inflation



- Most influences on price inflation are downwards, improving margins is the exception

How far are margins from ‘normal’?



- Margins are still below normal, but few contacts indicate they are at unsustainable levels

Hedging – currency

Unweighted % of responses	FX Some hedging
Total	21
Manufacturing	37
Construction	0
Consumer Services	19
Business Services	14
Other	38

- Ongoing use of currency hedging by some, mainly larger, corporates

Hedging – currency and input costs

Unweighted % of responses	FX Some hedging	Input Costs Some hedging
Total	21	21
Manufacturing	37	27
Construction	0	15
Consumer Services	19	35
Business Services	14	10
Other	38	50

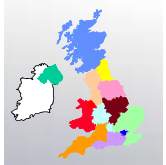
- Construction companies tend to hedge next quarter's input costs, other sectors hedge for longer

Summary

- **Pricing expectations remain positive but are a little weaker than price changes made in past year**

- **Most influences were having a dampening effect on price inflation for the year ahead, the exception is where companies want to rebuild margins**

- **A significant minority of companies report margins below normal**



Agents' Update

02 April 2015

Agency for Greater London
Inflation Report & Agency Intelligence Division

Outline

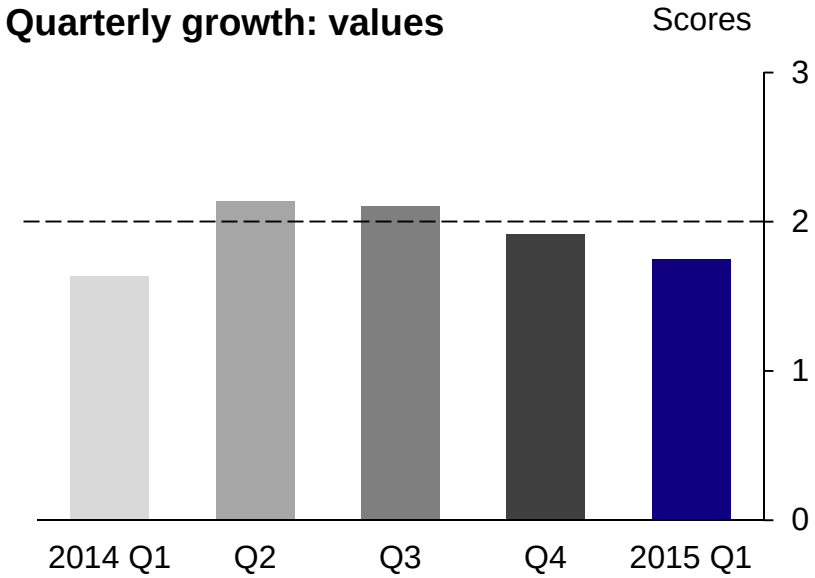
Quarterly estimates of activity

- Growth eases in construction (2015 Q1), subdued in manufacturing (2014 Q4)

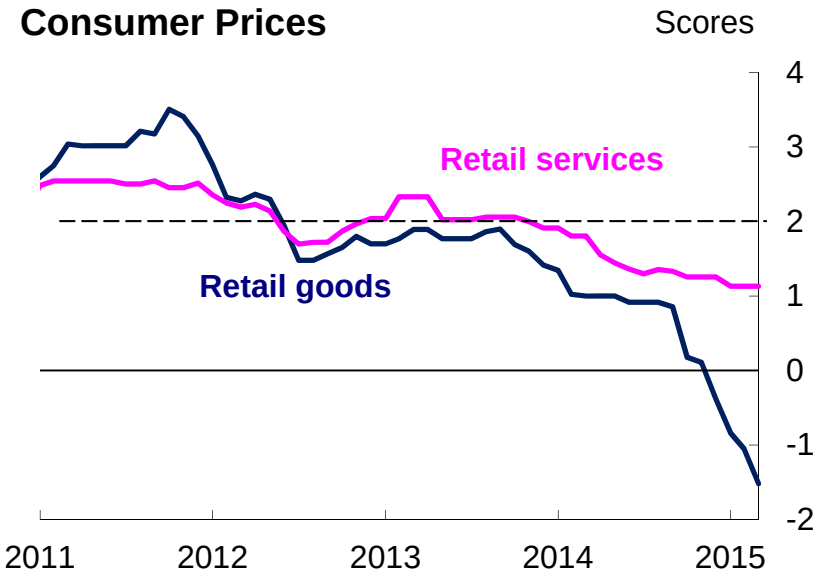
Have lower costs made room for pay increases?

- Company Visit Score evidence: little change expected overall, slight slowing in manufacturing

Consumer services



Agents' quarterly scores, estimating q-o-q growth rates.

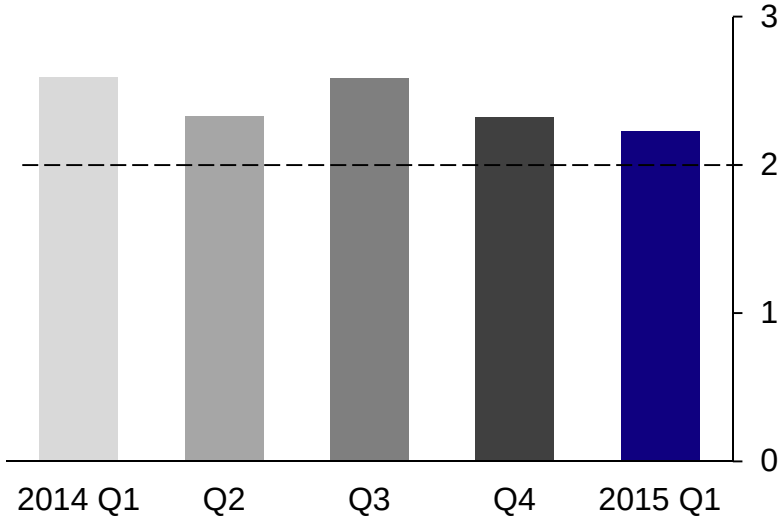


Agents' scores for prices in past 3 months cf same 3 months a year earlier.

- **Turnover growth eases but low inflation implies robust activity growth; rising discretionary expenditure on consumer services**

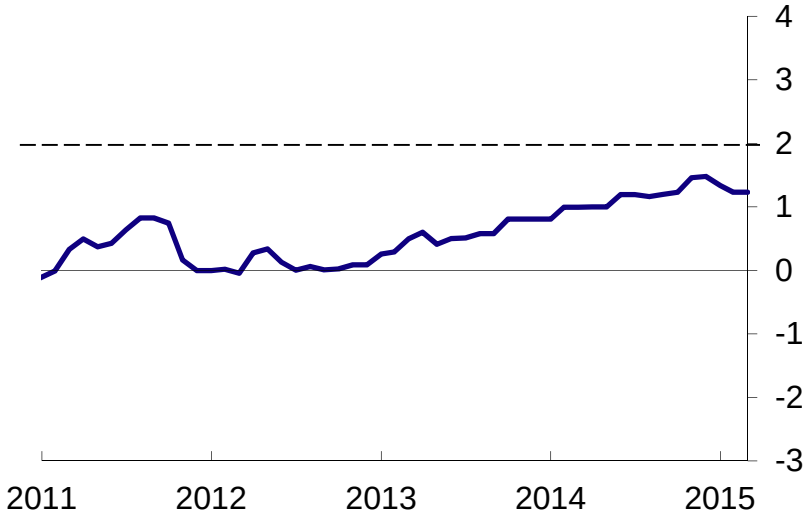
Business services

Quarterly growth: values



Agents' scores for estimates of q-o-q growth rates.

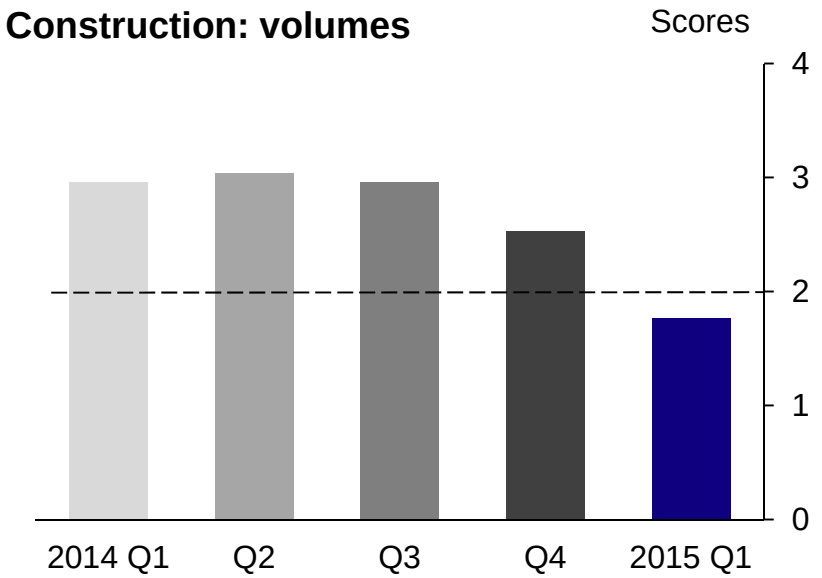
Business to business prices



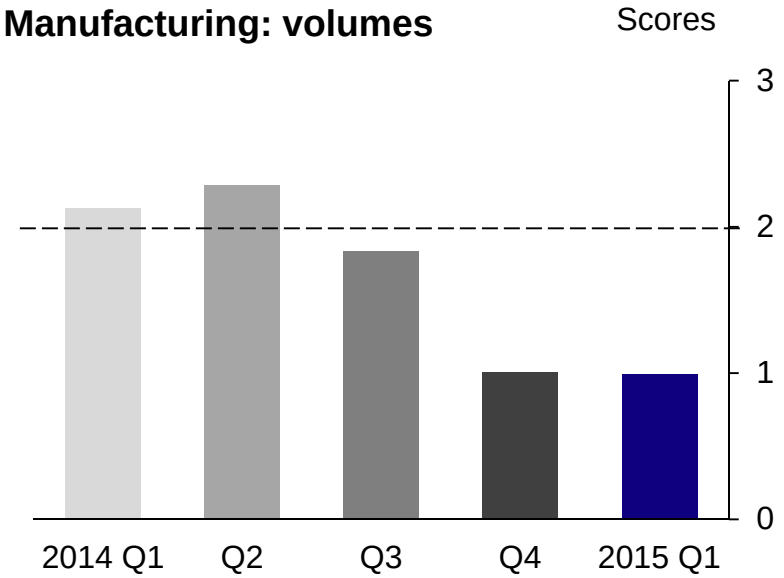
Agents' B2B prices scores: past 3 months cf same 3 months a year earlier.

- **Robust activity growth supported by corporate finance and property transactions**

Construction and Manufacturing



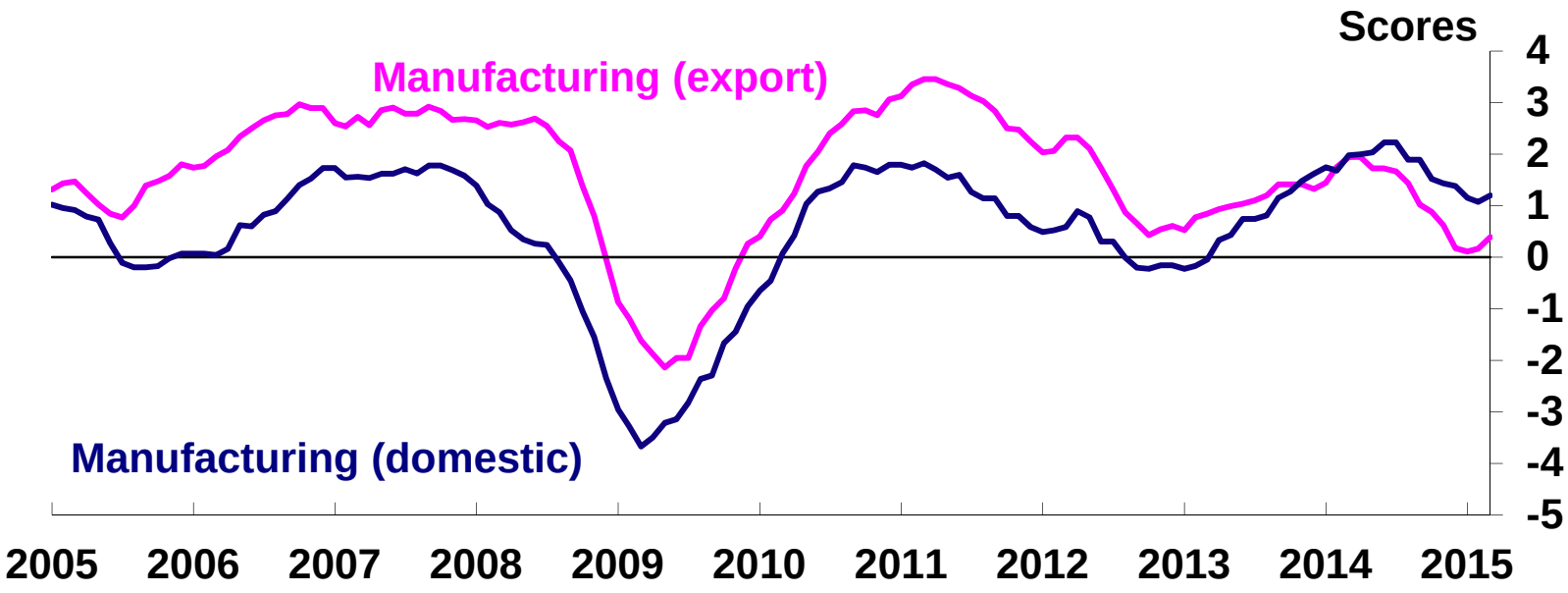
Agents scores for estimates of q-o-q growth rates



Agents scores for estimates of q-o-q growth rates

- **Output growth easing in construction; manufacturing growth flattened in 2015 Q1 after slowing in 2014 Q4**

Manufacturing output



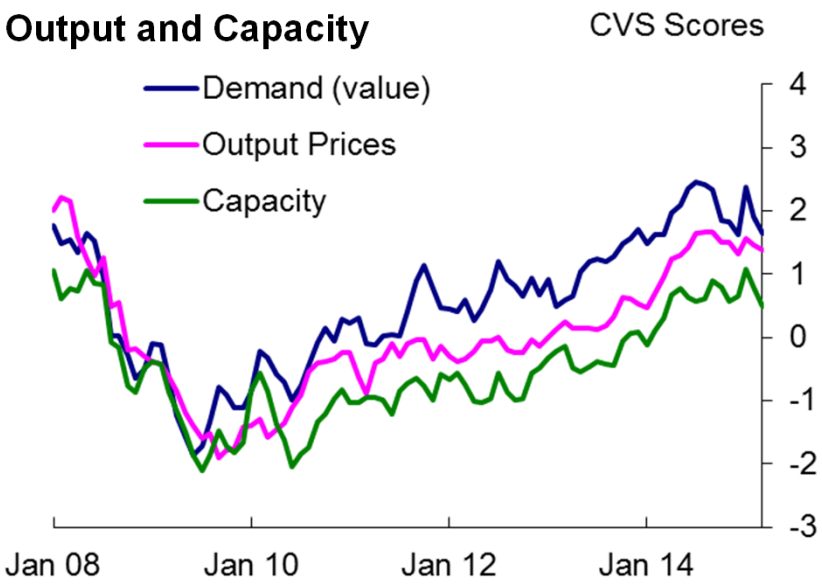
Agents' scores are past three months compared with same 3 months a year earlier.

- Sharper slowdown to foreign than to domestic customers

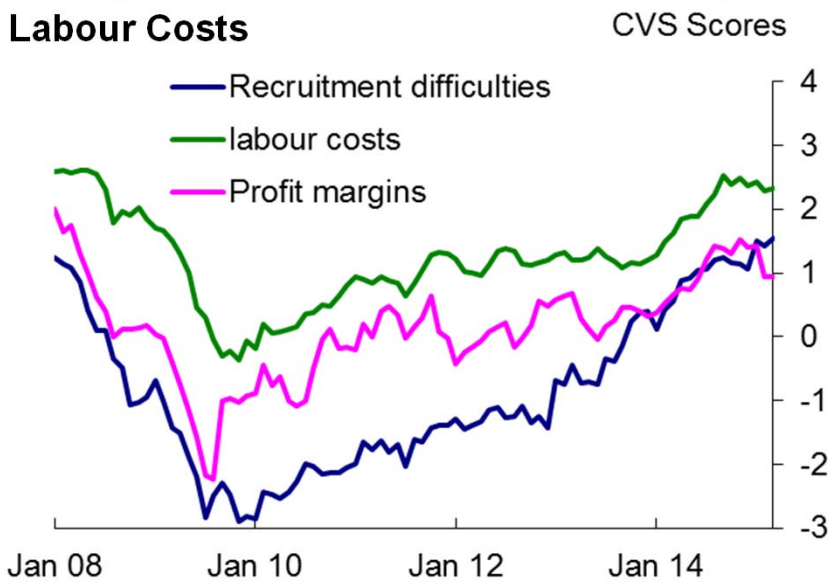
Why is construction growth slowing?

- **Moderation of growth in housebuilding, cf strength in 2014 H1 (NB: HCA grant period ended 2015 Q1)**
- **Skill shortages raising the cost of building relative to returns**
- **Plenty of positives: prime offices, industrial, shopping centres, hotels, higher education, transport infrastructure**
- **Some oil and gas related slowing; occasional mentions of pause in public sector decisions**
- **Collapse of domestic insulation by utilities since Apr 2014 o/a end of incentive; otherwise "trades" expect to be busy**

Construction – output constrained?



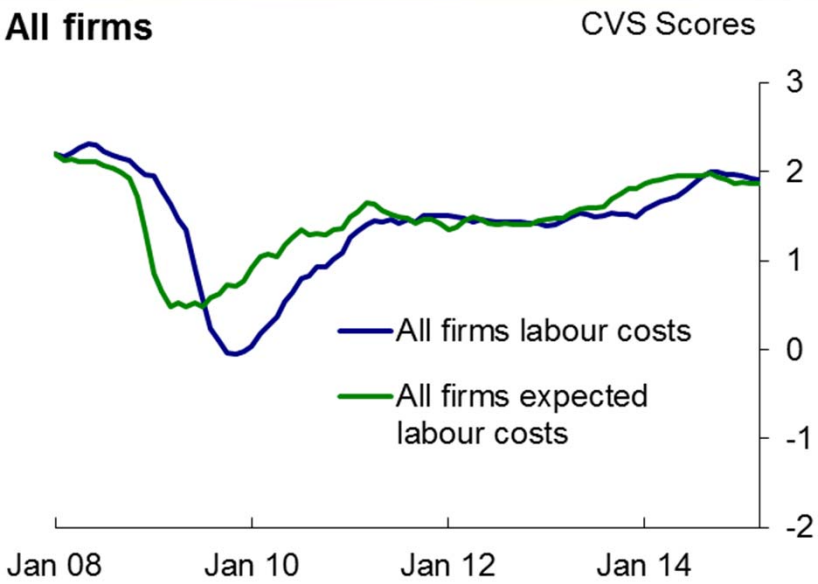
Rolling 3 month averages of Company Visit Scores for construction companies cf a year ago.
Capacity utilisation is scored relative to normal = 0



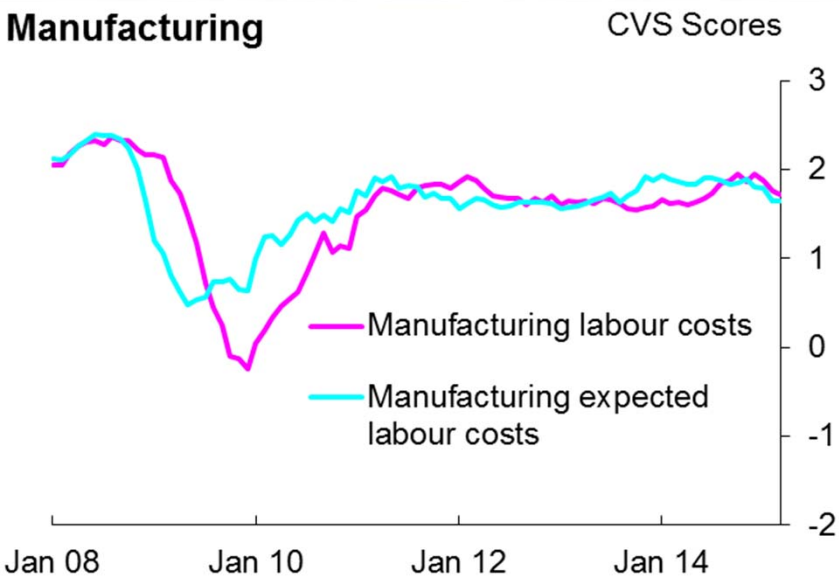
Rolling 3 month averages of Company Visit Scores for construction companies cf a year ago.
Recruitment difficulties scored relative to normal = 0

- **Activity growth in 2013-14 led to tightening capacity; recruitment difficulties led to higher labour costs**

Current and expected labour costs



Rolling 3 month average of CVS – past 3 months cf same 3 months a year earlier, and expectations for same 3 months in a year's time.



Rolling 3 month average of CVS – past 3 months cf same 3 months a year earlier, and expectations for same 3 months in a year's time.

- **Labour cost inflation picked up in 2014; similar rate expected**
- **Tentative signs of easing in manufacturing labour cost growth**

Summary

- **Above average activity growth in consumer and business services; construction and manufacturing growth have eased**
- **Slower manufacturing growth mainly reflects exports; weaker Eurozone growth and competitive pressure**
- **Construction costs rising faster than prices/profits, reflecting capacity/recruitment challenges; may inhibit growth**
- **Labour cost growth picked up after 2013; expected to remain stable; tentative and modest slowdown in manufacturing**

END