
August 2011

SUMMARY MINUTES OF THE MONETARY POLICY COMMITTEE MEETING

Held on the 3rd & 4th August 2011

PAYdata

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Financial markets

- Markets had been unsettled during the month, and had become particularly stressed in the days immediately preceding the Committee's meeting.
- That partly reflected market participants' concerns about the challenges faced by a number of euro-area countries.
- Implied market expectations of the point at which Bank Rate would begin to rise had been pushed further into the future, as it also had in the US and the euro area.
- As financial market strains had intensified, the Swiss franc and Japanese yen had appreciated markedly.
- Equity markets had been volatile - having fallen early in the month, and then risen following the euro-area statement, they had ended the month substantially lower.
- Primary capital markets had experienced relatively low levels of activity.

The international economy

- A key question remained the extent to which the slowing in the pace of global activity was temporary or more prolonged.
- Both the backward and forward-looking data released during the month had continued to point towards a broadly based slowing relative to earlier in the year.
- US GDP was estimated to have grown by 0.3% in Q2. There had been substantial downwards revisions to the data for previous quarters.
- Indicators of activity in the euro area had suggested some slowing in Q2. Survey measures of euro-area business confidence had fallen.
- Whilst the measures announced in July had alleviated the immediate financing pressures on Greece, structural adjustment was likely to weigh on euro-area demand.
- Chinese GDP was estimated to have grown by 9.5% in the year to Q2. This is broadly unchanged from the rate of growth in the year to the first quarter.

Money, credit, demand and output

- According to the ONS's preliminary estimate, GDP had risen by 0.2% during the Q2 of 2011.
- Underlying growth was, however, likely to have been somewhat stronger.
- Construction sector output, which had been more volatile than other indicators of construction activity in recent quarters, had risen by 0.5%.
- Weak growth in the remainder of the economy had reflected a pickup in service sector growth partially offset by a decline in manufacturing sector output.
- Business surveys had suggested that this pattern of growth had continued into the third quarter, although with some slowing in the pace of underlying expansion.
- The most recent indicators remained consistent with a subdued pace of consumption growth in the near term.
- In the judgement of the MPC, after some slowing in the near term, a gradual recovery in the pace of activity was expected over the medium term.

Supply, costs and prices

- The Governor informed the MPC that producer input prices had increased by 0.6% in July and producer output prices had risen by 0.2%.
- Twelve-month CPI inflation had fallen to 4.2% in June, from 4.5% in May. The most significant contribution had come from the prices of recreation and culture.
- The most likely near-term path of inflation was for a temporary rise to a peak of around 5% as increases in utility bills further raised the contribution of energy prices.
- There remained little evidence to suggest that above-target CPI inflation had begun to feed through into wages. Earnings growth remained subdued.
- The outlook for inflation remained sensitive to movements in commodity and energy prices.
- The degree of inflationary pressure associated with the path of demand would depend, crucially, on the evolution of productivity.
- The Labour Force Survey measure of employment had risen by 50,000 in the 3 months to May – a slower pace of expansion than earlier in the year.
- The slowing in the labour market was consistent with an upturn in productivity growth; or it might have reflected an anticipation of weaker demand.

The August GDP growth and inflation projections

- The Committee reached its policy decision in the light of its projections, published in the August Inflation Report.
- GDP growth had slowed over the past year and was projected to remain weak in the near term, reflecting the continuing squeeze on households' real incomes.
- There were substantial uncertainties around the outlook for output growth. The most significant risks to demand stemmed from abroad.
- The MPC's best judgement was that growth was likely to pick up gradually, so that by 2014 it was a little more likely to be above its historical average than below it.
- GDP was likely to remain significantly below the level corresponding to a continuation of its pre-recession trend.
- There remained significant uncertainties around the outlook for inflation. It was judged likely to reach 5% later in 2011, then fall back through 2012.
- The MPC's best judgement was that the chances of inflation being above or below the target were roughly equal in the medium term.

The Governor invited the Committee to vote on the propositions that:

- The MPC's central view remained that inflation was likely to fall back in the medium term. There were risks to that view, to the upside and the downside.
- The key upside risk continued to be that inflation would be elevated for longer than the Committee expected.
- The key risk to the downside remained that demand growth would not be sufficiently strong to absorb the pool of spare capacity in the economy.
- In the UK, it was likely that underlying growth in Q2 had been stronger than suggested by the headline number for GDP, but indicators of the evolution of activity in the near term had been subdued.
- The greatest risk to the downside stemmed from the euro area.
- There remained substantial risks to inflation in the medium term in both directions. But overall the news on the month had increased the downside risks.
- Most members judged that it was appropriate to maintain the current stance of monetary policy at this meeting.

- The Governor proposed that Bank Rate should be maintained at 0.5% and that the stock of asset purchases should be maintained at £200 billion.
- Regarding Bank Rate, the Committee voted unanimously in favour of the proposition.
- Regarding the stock of asset purchases, 8 members of the Committee voted in favour of the proposition. One voted against, preferring to increase by £50 billion.

Link to full minutes: <http://www.paydata.co.uk/mpc-minutes-august-2011>

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