RESEARCH PAPER 03/80
30 OCTOBER 2003

The Monetary Policy Committee: decisions & performance.

This Paper looks at the history of the first six years of the Monetary Policy Committee. It examines the reasons given for its establishment, describes its actions and assesses its impact. It updates Research Paper 01/59 produced in June 2001.

Grahame Allen

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ISSN 1368-8456

Summary of main points

This Paper reviews the first six years' experience of the Monetary Policy Committee (MPC). Established soon after the 1997 General Election, first informally and then later by the *Bank of England Act 1998*, the MPC is responsible for the determination of interest rates, and hence is highly influential in the setting of the overall monetary stance in the economy.

Its membership is drawn from Members of the Bank of England and from outside academics in roughly equal measure. Members' voting records are published as part of the minutes to the meetings. This allows an analysis of the different attitudes and inclinations of the individual members of the MPC. Attitudes have been characterised as being between the 'hawks'- members that are consistently more in favour of higher interest rates than others, and the 'doves' – those who favour a more relaxed policy. The analysis reveals that the Bank representatives have formed into a relatively homogenous group with Mervyn King (the Governor) emerging as the chief 'hawk'. By contrast the outside representatives are far more likely to disagree with the majority view with one, Dr Sushil Wadhwani, emerging as the chief 'dove'.

Inferences about the rationale behind the MPC's decisions can be drawn from the published minutes. A number of issues have been highlighted by the MPC when determining their decisions. These have included concerns about the need to balance nominal demand and the supply potential of the economy (the output gap), and traditional concerns over the state of the labour market.

While it may be too soon to determine the long-term influence of the MPC, certain developments are already worth comment. The Committee appears to have conducted its business in an open and harmonious manner, avoiding the disharmony evident in previous experiments of consensual economic policy-making.

The UK's inflation performance over the period is broadly in line with, or better than, the economic forecasts that were made before the MPC was created. Growth has remained relatively constant and employment has risen.

However, these conclusions have to be seen in the light of other economic factors, most of which have been conducive to low inflation. For example; UK growth rates at or below trend rates, slow growth in Europe, the US and Japan, a high external value of the pound and until recently low world commodity prices.

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I Introduction

One of the first economic policy decisions taken by the incoming Labour Government in May 1997 was to announce the 'independence' of the Bank of England.[1] The idea of a new role for the Bank had appeared in the Party's 1997 general election manifesto:

> We will reform the Bank of England to ensure that decision-making on monetary policy is more effective, open, accountable and free from short-term political manipulation.

The Chancellor made his announcement even before the House had reconvened and extracts from his press statement of 6 May 1997 are shown below:

> The enemy of growth, and the investment necessary for it, is the instability of short periodic bursts of high growth followed by recession.
>
> So we must break from the short termism of the past - the economic instability that has characterised the British economy not just in recent years but for most of the century. That is why I want British economic success to be built on the solid rock of prudent and consistent economic management, not the shifting sands of boom and bust. Now is the time for long-termism. This is the time to set the British economy on a new long-term course that will deliver high levels of growth and employment through lasting stability.
>
> Price stability is, as I have said, an essential precondition for the Government's objectives of high and sustainable levels of growth and employment. The question is how to achieve the long-term stability that we seek?
>
> I have also made clear that reform is required to put monetary policy on a stable, long-term footing. In a speech in May 1995 and subsequently in our 1995 policy document, A New Economic Future for Britain, I set out my view of the proper roles of the Government and the Bank of England in economic policy. Government has a responsibility to the public in setting the objectives of economic policy and that means that the Government rather than the Bank of England must set the targets for monetary policy.
>
> However, as I have repeatedly made clear since 1995, we will only build a fully credible framework for monetary policy if the long-term needs of the economy, not short-term political considerations, guide monetary decision-making. We must remove the suspicion that short-term party political considerations are influencing the setting of interest rates.

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[1] *The Bank of England Act 1998,* which gave the Bank that responsibility, came into force on 1 June 1998.

> I am now satisfied that we can put in place, with immediate effect, reforms of the Bank of England to ensure that it can discharge responsibilities for setting interest rates in an effective, open and accountable way.
>
> This is the time to take the tough decisions we need for the long-term interests and prosperity of the country. I will not shrink from the tough decisions needed to deliver stability for long-term growth. I have therefore decided to give the Bank of England operational responsibility for setting interest rates, with immediate effect. The Government will continue to set the inflation target and the Bank will have responsibility for setting interest rates to meet the target. The Government's policy is set out in a letter I sent to the Governor yesterday, the text of which I am releasing now.
>
> But there is, as I have suggested today, a more long-term context. In the last century, Britain was industrially pre-eminent. The history of this century has been one of economic decline, not least because of short termism and the pursuit of stop-go economics. I am determined that we make the right preparations for long term national economic success, as we look to the century that lies ahead, so that we can move forward again economically. I am therefore setting in place a long-term policy for long-term prosperity. The ultimate judgement of the success of this measure will not come next week , or indeed in the next year but in the long- term. I am convinced that this radical reform, together with measures we will announce to equip our economy for the challenges ahead, creates the platform of stability upon which Britain can build

The outcome of this announcement, confirmed later in a statement to the House[2] was the creation of a new organisation, one that would be responsible for the setting of monetary policy: the Monetary Policy Committee (MPC).

It may be too soon to test the contribution of the MPC to the long-term objectives outlined above with a degree of statistical confidence. However, one can gain an impression of how the MPC works, analyse what influences it recognises, the degree that its membership hold convergent views and to what extent it has met its objectives in the last six years.

II The Monetary Policy Committee (MPC) in action

A. The MPC: organisation and remit

The MPC is accountable to the Government for its remit, to its Court of Directors for its procedures and to Parliament for all aspects of its operations through regular reports and evidence given to the Treasury Committee and the Lords Select Committee on the Monetary Policy Committee.[3]

2 HC Deb 20 May 1997 vol 294 cc 507 - 11
3 Treasury Committee, Ninth Report, 28 March 2001, HC 42 2000-2001, vii, para 3

The relevant provisions of the *Bank of England Act 1998*[4] formally set out the role and constitution of the MPC. Section 11 states that:

> In relation to monetary policy, the objectives of the Bank of England shall be –
>
> (a) to maintain price stability, and
>
> (b) subject to that, to support the economic policy of Her Majesty's Government, including its objectives for growth and employment.

The Government reviews and announces the inflation target at least once in every twelve-month period beginning on the anniversary of the day the 1998 Act came into force. The target the MPC has been given by the Chancellor since 1997 has been a 2.5% increase, over the previous twelve months, in the retail prices index excluding mortgage interest payments - RPI(X). Mortgage interest payments are excluded since they 'confuse' the underlying trend of prices. A direct consequence of a rise in interest rates is to increase mortgage costs and these feed through into the rate of inflation. Thus the very thing that the decision of the MPC tries to prevent automatically happens if mortgage costs are included in the index. After being given the inflation target by the Chancellor the MPC has operational freedom as to how it meets that target.

Decisions on what actions need to be taken to achieve the target are taken by the MPC, on the basis of a majority vote. The membership of the Committee is set out under Section 13 of the Act. It includes the Governor and the two Deputy Governors of the Bank, two members appointed by the Governor after consultation with the Chancellor and four outside 'expert' members appointed by the Chancellor. The MPC has a two-day meeting on a monthly basis and all decisions on interest rates are announced immediately after the last day. The proceedings of the meetings, including votes, are now published within two weeks.[5]

The Chancellor is to change the MPC's target at the time of the 2003 Pre-Budget Report. The new target will be a symmetric inflation target as measured by the Harmonised Index of Consumer Prices (HICP) although the actual value of the target is yet to be announced. Information on this new measure can be found in the Library Research Paper; *Economic Trends*, RP 03/57, 1 July 2003.

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[4] Chapter 11

[5] Minutes of each MPC meeting are available on the Bank of England website as at 21 October 2003: www.bankofengland.co.uk/mpc/minutes.htm

B. Membership of the MPC

Since its inception, twenty individuals have served on the MPC. Brief biographical details of the current membership are shown below.

1. Bank of England Representatives

Mervyn King

Mervyn King is Governor of the Bank of England and the Chairman of the MPC.

Professor Charles Bean

Charles Bean has been Professor of Economics and Head of Department at the London School of Economics. He succeeded John Vickers on 1 October 2000 as Chief Economist and Executive Director at the Bank and is responsible for monetary analysis and statistics. He has been a member and former chairman of the Treasury's Academic Panel, a consultant to the Treasury's Macroeconomic Policy and Prospects division and a former adviser to the Treasury Committee.

Sir Andrew Large

Sir Andrew Large is Deputy Governor for Financial Stability. His main responsibilities are the stability of the financial system and the day to day operation of the Bank. Sir Andrew joined the MPC in September 2002 following the departure of a previous Deputy Governor, David Clemanti. He was previously Deputy Chairman of Barclays, Chairman of Euroclear and of the Securities and Investments Board, now the FSA.

Rachel Lomax

Rachel Lomax became Deputy Governor on 1 July 2003 succeeding Ian Plenderleith. She has specific responsibility within the Bank for monetary policy, including monetary assessment and money market operations. Ms Lomax's career has been in the civil service, mostly in the Treasury but more recently as Permanent Secretary at the Welsh Office, the Department of Work and Pensions, and the Department of Transport.

Paul Tucker

Paul Tucker was appointed as Executive Director of the Bank on 1 June 2002. He is the Executive with responsibility for the Bank's implementation of monetary policy via open market operations, the Bank's foreign exchange market operations, including management of the Government's foreign currency reserves, and for market intelligence and analysis, supporting the Bank's monetary and financial stability core purposes. He is also a member of the Governor's Committee, the Bank's executive management committee and of the Bank's Asset and Liability Committee.

2. Outside representatives

Professor Stephen Nickell

Professor Stephen Nickell is School Professor of Economics at the LSE (part-time), President of the Royal Economic Society and a Fellow of the British Academy and of the Econometric Society. He has acted as academic consultant for various government bodies including HM Treasury, the Manpower Services Commission and the DHSS.

Kate Barker

Kate Barker joined the MPC on 1 June 2001 taking the place of Dr DeAnne Julius who did not seek reappointment. Ms Barker was Chief Economist at the Confederation of British Industry between 1994 and 2001 and was a member of the Institute for Public Policy Research's Commission on Public Private Partnerships. She has previously been Chief Economist at Ford Europe and a Member of HM Treasury Panel of Independent Forecasters.

Marian Bell

Marian Bell was appointed as a member of the MPC from 1 June 2002 taking over from Dr Sushil Wadhwani. Prior to her appointment, Ms Bell ran her own economics consultancy. Between 1987 and 2000 she was Head of Research, Treasury and Capital Markets at the Royal Bank of Scotland. Her previous appointments also include Economic Adviser at the Treasury and Senior Economist at the Royal Bank of Scotland.

Richard Lambert

Richard Lambert joined the MPC on 1 June 2003, following the departure of Christopher Allsopp. He retired as editor of the Financial Times in 2001, where he had worked since 1966. He is chair of Visiting Arts and a Trustee of the British Museum. He is currently undertaking a review on behalf of the Government of the relations between business and universities in the UK.

C. Decisions taken by the MPC

The policy instrument controlled by the MPC is a key money market interest rate now referred to as the repo rate. Up to October 2003, the MPC had taken seventy eight interest rate decisions and of these twenty four changed the rate. On nine occasions the rate was raised, and it has been reduced fifteen times. On twenty occasions the change was a 0.25% change and four times it has been a 0.5% change. The history of rate changes is shown in more detail in the table on the next page:

MPC Decisions **Base/Repo Rate**

	Date of announcement	Decision	Revised rate
1997	Jun 6	$^{1}/_{4}$ % increase	6.50
	Jul 10	$^{1}/_{4}$ % increase	6.75
	Aug 7	$^{1}/_{4}$ % increase	7.00
	Nov 6	$^{1}/_{4}$ % increase	7.25
1998	Jun 4	$^{1}/_{4}$ % increase	7.50
	Oct 8	$^{1}/_{4}$ % decrease	7.25
	Nov 5	$^{1}/_{2}$ % decrease	6.75
	Dec 10	$^{1}/_{2}$ % decrease	6.25
1999	Jan 7	$^{1}/_{4}$ % decrease	6.00
	Feb 4	$^{1}/_{2}$ % decrease	5.50
	Apr 8	$^{1}/_{4}$ % decrease	5.25
	June 10	$^{1}/_{4}$ % decrease	5.00
	Sept 8	$^{1}/_{4}$ % increase	5.25
	Nov 4	$^{1}/_{4}$ % increase	5.50
2000	Jan 13	$^{1}/_{4}$ % increase	5.75
	Feb 10	$^{1}/_{4}$ % increase	6.00
2001	Feb 8	$^{1}/_{4}$ % decrease	5.75
	Apr 5	$^{1}/_{4}$ % decrease	5.50
	May 10	$^{1}/_{4}$ % decrease	5.25
	Aug 2	$^{1}/_{4}$ % decrease	5.00
	Sept 18	$^{1}/_{4}$ % decrease	4.75
	Oct 4	$^{1}/_{4}$ % decrease	4.50
	Nov 8	$^{1}/_{2}$ % decrease	4.00
2003	Feb 6	$^{1}/_{4}$ % decrease	3.75
	July 10	$^{1}/_{4}$ % decrease	3.50

Source: Bank of England

D. 'Hawks' & 'Doves'

As the voting record of the membership is published as part of the minutes to the meetings there has been some interest in the voting record of the individual members of the MPC. From this we can see if some members are consistently more in favour of higher interest rates than others who favour a more relaxed policy, so called 'hawks' and 'doves' respectively.

The full voting record since the last version of this Paper is displayed in a stylised way in the Membership Voting Record table on the following pages (pages 13 and 14).[6] Each recorded vote is given a 'score'. A vote for the majority view is given a score of one. A

6 The full voting record from the previous MPC Paper is displayed in Appendix I

vote for a rate of interest higher than the majority view has a score of two and a vote for a rate of interest lower than the majority view has a score of zero. Hence a 'hawk' will have a number of 'twos', whereas a 'dove' will have some zeroes.

Monetary Policy Committee

Membership Voting Record, Bank Representatives, July 2001- October 2003

Date of announcement		Decision	Sir Edward George	Mervyn King	David Clemanti	Ian Plenderleith	Charles Bean	Rachel Lomax	Sir Andrew Large	Paul Tucker
2001	July 5	no change	1	1	1	1	1	na	na	na
	Aug 2	1/4 % decrease	1	2	2	2	1	na	na	na
	Sept 6	no change	1	1	1	1	1	na	na	na
	Sept 18	1/4 % decrease	1	1	1	1	1	na	na	na
	Oct 4	1/4 % decrease	1	1	1	1	1	na	na	na
	Nov 8	1/2 % decrease	1	1	1	2	1	na	na	na
	Dec 5	no change	1	1	1	1	1	na	na	na
2002	Jan 10	no change	1	1	1	1	1	na	na	na
	Feb 8	no change	1	1	1	1	1	na	na	na
	Mar 7	no change	1	1	1	1	1	na	na	na
	Apr 4	no change	1	1	1	1	1	na	na	na
	May 9	no change	1	1	1	1	1	na	na	na
	June 6	no change	1	2	1	na	1	na	na	1
	July 4	no change	1	2	1	na	1	na	na	1
	Aug 1	no change	1	1	1	na	1	na	na	1
	Sept 4	no change	1	1	na	na	1	na	1	1
	Oct 10	no change	1	1	na	na	1	na	1	1
	Nov 7	no change	1	1	na	na	1	na	1	1
	Dec 5	no change	1	1	na	na	1	na	1	1
2003	Jan 9	no change	1	1	na	na	1	na	1	1
	Feb 6	1/4 % decrease	1	1	na	na	1	na	2	2
	Mar 6	no change	1	1	na	na	1	na	1	1
	Apr 10	no change	1	1	na	na	1	na	1	1
	May 8	no change	1	1	na	na	1	na	1	1
	June 5	no change	1	1	na	na	1	na	1	1
	July 10	1/4 % decrease	na	1	na	na	1	2	1	1
	Aug 7	no change	na	1	na	na	1	1	1	1
	Sept 4	no change	na	1	na	na	1	1	1	1
	Oct 9	no change	na	1	na	na	1	1	2	2

Notes: 1 - vote was in accordance with majority view
2 - vote was for a rate of interest higher than the majority view
0 - vote was for a rate of interest lower than the majority view
* - attended as Treasury observer - no vot na - did not attend, not appointed or had left at that date

Source: MPC *Monthly minutes*, various months

Monetary Policy Committee

Membership Voting Record, Outside Representatives, July 2001- October 2003

Date of announcement		Decision	Dr Sushil Wadhwani	Professor Stephen Nickell	Christopher Allsopp	Kate Barker	Marian Bell	Richard Lambert
2001	July 5	no change	0	1	1	1	na	na
	Aug 2	$^{1}/_{4}$ % decrease	1	1	1	1	na	na
	Sept 6	no change	0	1	1	1	na	na
	Sept 18	$^{1}/_{4}$ % decrease	0	1	0	1	na	na
	Oct 4	$^{1}/_{4}$ % decrease	0	1	1	1	na	na
	Nov 8	$^{1}/_{2}$ % decrease	1	1	1	1	na	na
	Dec 5	no change	0	1	0	1	na	na
2002	Jan 10	no change	1	1	1	1	na	na
	Feb 8	no change	0	1	0	1	na	na
	Mar 7	no change	1	1	1	1	na	na
	Apr 4	no change	1	1	1	1	na	na
	May 9	no change	1	1	1	1	na	na
	June 6	no change	na	1	1	1	na	na
	July 4	no change	na	1	1	1	1	na
	Aug 1	no change	na	1	1	1	1	na
	Sept 4	no change	na	1	1	1	1	na
	Oct 10	no change	na	0	0	0	1	na
	Nov 7	no change	na	0	0	1	1	na
	Dec 5	no change	na	0	0	1	1	na
2003	Jan 9	no change	na	0	0	1	1	na
	Feb 6	$^{1}/_{4}$ % decrease	na	1	1	1	1	na
	Mar 6	no change	na	1	0	1	1	na
	Apr 10	no change	na	1	0	1	0	na
	May 8	no change	na	0	0	0	0	na
	June 5	no change	na	0	na	0	0	1
	July 10	$^{1}/_{4}$ % decrease	na	1	na	1	1	1
	Aug 7	no change	na	1	na	1	1	1
	Sept 4	no change	na	1	na	1	1	1
	Oct 9	no change	na	2	na	2	1	1

Notes: 1 - vote was in accordance with majority view
2 - vote was for a rate of interest higher than the majority view
0 - vote was for a rate of interest lower than the majority view
* - attended as Treasury observer - no vote

Source: MPC *Monthly minutes*, various months

The tables reveal a few interesting features. As might be expected the Bank representatives formed into a relatively homogenous group[7] although, on twelve occasions Mervyn King has voted for higher interest rates than the other Bank representatives. By contrast the outside representatives are far more likely to disagree with the majority view.[8] On three occasions, May and August 1998 and January 1999, votes have been recorded for all three options, i.e. raising interest rates more and less than

[7] 92% of Bank representative's votes have been in accordance with the majority view, while 1% and 7% have been votes for a rate of interest lower and higher, respectively, than the majority view.

[8] 74% of outside representative's votes have been in accordance with the majority view, while 19% and 7% have been votes for a rate of interest lower and higher, respectively, than the majority view.

the majority view. This may confirm the popular perception of the propensity of economists to disagree amongst themselves.

Constructed in this way the full voting table can be used to determine a ‘hawk/dove’ index. In the table below the Committee Members’ average score is determined.

MPC
'Hawk' Index June 1997- September 2003

Member	Number of votes taken	Average 'score'
Bank Representatives		
Rachel Lomax	4	1.3
John Vickers	28	1.2
Mervyn King	78	1.2
Andrew Large	14	1.1
Paul Tucker	17	1.1
David Clemanti	62	1.0
Ian Plenderleith	61	1.0
Sir Edward George	74	1.0
Howard Davies	1	1.0
Charles Bean	38	1.0
Outside Representatives		
Sir Alan Budd	18	1.2
Professor Charles Goodhart	36	1.1
Professor Willem Buiter	36	1.0
Richard Lambert	5	1.0
Professor Stephen Nickell	42	1.0
Kate Barker	30	0.9
Marian Bell	16	0.8
Christopher Allsopp	37	0.7
Dr Deanne Julius	45	0.7
Dr Sushil Wadhwani	37	0.6

Source: MPC *Monthly Minutes,* various months

The results are not very surprising with the Bank representatives’ scores relatively close to one, although with average scores all above one this suggests a preference amongst the Bank representatives for a tighter monetary stance. The outside representatives vary from the most hawkish of all outside members – Sir Alan Budd to the least – Dr Sushil Wadhwani.

Within these overall averages one might note that Professor Buiter has the fewest scores of one. Of the thirty-six decisions he took part in, on seventeen (47%) occasions he voted for different rates of interest than the majority, nine times (25%) for rates of interest higher and eight times (22%) for interest rates below those proposed by the majority.

III What determines the MPC's decisions?

A. Introduction

This section looks at thinking behind the decisions taken by the MPC. It will be recalled that the policy outlined in the1997 Labour Party manifesto was:

> We will reform the Bank of England to ensure that decision-making on monetary policy is more effective, open, accountable and free from short-term political influence.

Part of the commitment to openness has been the timely publication of the minutes, now published within two weeks of the MPC meetings. From these it is possible to gain an impression of the importance attached to various economic factors that determine the Committee's final decision.

B. The decisions

Extracts from the Bank's press releases issued when interest rates were changed are shown below together with various contextual comments. Comments in bold are the author's emphasis.

Date: June 1997.
Decision: Interest rates raised by 0.25% to 6.50%.

> The Bank's Monetary Policy Committee has reviewed the latest monetary and economic data. It concluded that the latest evidence is consistent with the outlook described in the Bank's Inflation Report published on 13 May. Notwithstanding the strength of the exchange rate, which is expected to restrain retail price inflation temporarily in the near term, the Report concluded that "the central projection for inflation, and the risks surrounding it, suggests that, on the present evidence, there is still likely to be a need for some further moderate tightening of policy in the months ahead."

This tells us little other than the fact that, in the Banks' view, inflationary pressures were building in the economy at the time of the 1997 General Election.

Date: 10 July 1997
Decision: Interest rates raised by 0.25% to 6.75%

> The combination of rapid expansion of domestic demand led by consumption and the further appreciation of sterling has sharpened the dilemma for monetary policy. **The Monetary Policy Committee's task is to aim to balance nominal demand and the supply potential of the economy, in order to meet the inflation target and create the conditions for sustained growth of output and employment.** Continued growth of output at well above trend rates would be unsustainable.

> The Committee reviewed the latest monetary and economic data against the background of the Bank's Inflation Report published on 13 May and the 0.25% rise in official interest rates announced on 6 June. It concluded that the latest month's evidence - notably the upward revision of estimated output growth in the fourth quarter of 1996 and recent developments in monetary growth and retail sales - indicated that a further tightening of monetary policy was necessary, notwithstanding the further appreciation of the exchange rate and the contractionary effects of the recent Budget.

If there is one persuasive factor in this analysis it is the position of the UK economy above its trend growth pattern. The Committee clearly held a view that whatever other influences were coming into play the most important factor was the growth rate of the economy.

Date: 7 August 1997
Decision: Interest rates raised by 0.25% to 7.0%

> The Committee recognised that the appreciation of the exchange rate over the past year is putting severe pressure on businesses exposed to international competition.
>
> Nevertheless, in the light of the prospect for domestic demand and on the basis of all the evidence currently available, the Committee judges that today's rise is necessary to put the economy on track for achieving the inflation target of 2½% looking two years ahead. Although the present strength of sterling reflects in large part factors outside the influence of UK monetary policy, upward pressures on the exchange rate should be reduced by the perception that interest rates have reached a level consistent with the inflation target.

Perhaps the most important feature of this notice is the subsidiary influence (despite the laboured – and subsequently inaccurate hint to the markets at the end of the notice) of the exchange rate at a time when sterling was at its highest level for almost a decade.

Date: 6 November 1997
Decision: Interest rates raised by 0.25% to 7.25%

> Inflation has not moderated as much as expected in the light of sterling's appreciation since the autumn of 1996. Domestic demand has remained robust, and the expected impact on external trade, lowering export volumes and raising import volumes, has yet to materialise, so that **GDP has continued to grow at an unsustainable rate. The labour market has tightened further, with skill shortages increasingly reported.**
>
> Looking ahead, the economy is expected to slow down next year as both domestic demand and net external trade moderate, under the combined impact of past tightening in monetary and fiscal policy, the strength of sterling, and a smaller impact of windfalls on consumption. This will help to reduce inflationary

> pressures. But, in the Committee's judgement, the balance of risks implies that a modest further increase in interest rates is necessary to meet the inflation target of 2½% in the medium term.

This was the first of several press releases to mention labour market conditions as indicators of inflationary pressure. Again the main issue of concern appears to have been the 'unsustainable' rate of growth in the economy. 'Windfalls' refers to the sums accruing to individuals when, typically, a building society converted into a bank and compensated its previous members with generous payments.

Date: 4 June 1998
Decision: Interest rates raised by 0.25% to 7.25%

> In the May Inflation Report, the Committee said that: "In the central projection, inflation is expected to remain close to its target throughout the forecast period after the temporary increase in the second quarter of this year. But there are major uncertainties which mean that the outlook for monetary policy remains finely balanced."
>
> The central issue for monetary policy remains whether aggregate demand will slow sufficiently quickly to bring down domestically generated inflation before the restraining price effects of the earlier increase in the exchange rate and falls in commodity prices wear off. As the May Inflation Report made clear, **developments in the labour market are a key determinant of domestically generated inflation**. Evidence has emerged over the past month that the cumulative tightening of the labour market has resulted in a rate of private sector earnings growth that jeopardises achievement of the inflation target over the medium run.

This month also saw explicit reference to the labour market as a "key determinant" of the Committee's decision. However, it emerged later that the figures for average earnings produced by the Office of National Statistics were unreliable and publication of the series was suspended, subject to review, soon afterwards.

Date: 8 October 1998
Decision: Interest rates reduced by 0.25% to 7.25%

> The international economic and financial environment has deteriorated since the Committee met in September. In the domestic economy, surveys and reports from the Bank's Regional Agents have indicated a decline in business and consumer confidence. The outlook for demand and output has therefore weakened. Despite continuing tightness in the labour market and the fall in the exchange rate, the Committee judges that the risks of inflation falling below the target of 2.5% have increased and that a reduction in interest rates of 0.25% is now appropriate.

This was the first release to make specific mention of regional influences. The Bank's Regional Agents are a historical throwback to the days when the Bank had a regional branch network to deal with the failures of local note-issuing banks. Over time, and after several initiatives and reorganisations, the agents developed an industrial liaison role. Their work was described in an article from the Bank of England Quarterly Bulletin as being:

> To maintain contact with industry and commerce and to report on the economy as seen by those based in the area. The Agencies play an important part in enabling the Bank to collect 'proper regional and sectoral information for the purpose of monetary policy formation' (as required by the Chancellor's letter to the Governor of the 6 May 1997).[9]

Date: 5 November 1998
Decision: Interest rates reduced by 0.5% to 6.75%

> Since the August Inflation Report was published, news about the international environment and the prospects for domestic activity have led the Committee to moderate its forecast for growth next year and to revise downwards its projection for inflation over the next two years. As a result, the Committee concluded that a reduction in interest rates of 0.5% was appropriate in order to maintain a path for inflation consistent with the target.

References to the international environment appear to refer to the collapse of the Russian economy, following the floating of the rouble in August, along with a deepening of the recession in Japan and substantial falls in equity markets around the world: the FTSE 100 fell by 24% between March and September 1998.[10]

Date: 10 December 1998
Decision: Interest rates reduced by 0.5% to 6.25%

> Since the November Inflation Report, the prospect for global activity appears to have weakened and commodity prices have fallen further. In the UK, GDP growth in the third quarter was revised down, and surveys of activity have continued to indicate deterioration across the economy, although the labour market is still tight and monetary and financial indicators remain relatively strong. The Monetary Policy Committee judged that the downside risks to both activity and inflation have increased, and therefore reduced interest rates by 0.50% to keep prospective inflation on track to meet the 2.5% target.

Date: 7 January 1999
Decision: Interest rates reduced by 0.25% to 6.00%

> Since the Committee's December meeting, **domestic data and survey evidence have, on balance, shown a continuing slowdown in the UK economy**. The labour market remains tight but it seems to have reached a turning point.

9 Bank of England, *Quarterly Bulletin*, November 1997, p 424
10 National Statistics, *Financial Statistics*, October 1999, table 7.1G

> Evidence from wage settlements and the Bank's regional Agents suggest an easing of upward pressures on growth in pay. The risks from the international environment remain clearly on the downside. In these circumstances the Committee judged that a further reduction in interest rates of 0.25% to 6.0% was appropriate in order to maintain a path for inflation consistent with the target.

Date: 4 February 1999
Decision: Interest rates reduced by 0.5% to 5.50%

> Taking account, in particular, of the prospects for international activity and prices, domestic costs and consumer demand, the Committee's latest inflation projections implied that a further reduction in interest rates was necessary to keep inflation on a path consistent with the target of 2 ½%.

The Bank reduced interest rates for the fifth successive month in an attempt to stop an economic slowdown turning into a full-scale recession.

Date: 8 April 1999
Decision: Interest rates reduced by 0.25% to 5.25%

> No Statement released

The Bank offered no explanation for its decision, unlike the previous reductions that had been accompanied by a short statement.

At the time, some City economists suggested this might have meant a split decision among the MPC members[11] but as can be seen from the tables in Appendix 1, only Professor Buiter's decision was against that of the majority. The decision of the MPC may have been influenced by the weakness of inflationary wages and by the resilience of sterling - which remained at around the same level with relation to the German mark as when this round of interest rate cuts began in October 1998.

Date: 10 June 1999
Decision: Interest rates reduced by 0.25% to 5.00%

> The Committee considered recent economic developments against the background of the May Inflation Report. Taking into account all the evidence on the inflation outlook, the Committee judged that it is now more likely that inflation will undershoot the 2 ½% target.

The 0.25% cut in interest rates to 5.00% reduced them to their lowest level since October 1977.[12]

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[11] *MPC brevity taken as hint of a split* The Guardian, 9 April 1999
[12] Minimum Lending Rate reduced by 0.5% at 17 October 1977.

Date: 8 September 1999
Decision: Interest rates raised by 0.25% to 5.25%

> The Committee reviewed developments since its last meeting, including **world demand, the strength of consumption and the housing market, and continuing tight conditions in the labour market**. Although inflation is expected to remain below the target of 2½% in the short term, the Committee concluded that a rise in interest rates was necessary to keep inflation on track further ahead, and that an early move could lower the level at which interest rates might otherwise need to be set.

In the second quarter of 1999, household spending grew by 1.4% and was up by 4.0% on a year earlier. Investment was also up strongly, by 6.7% as an annual rate. Growth forecasts for 1999, clustered around 0.75% in the spring, were revised to 1.5%, the top end of the range laid out in the March 1999 budget. Consumer demand was expanding more quickly than the Chancellor expected, while the current account was also looking worse than predicted.

Date: 4 November 1999
Decision: Interest rates raised by 0.25% to 5.50%

> No Statement released

Date: 13 January 2000
Decision: Interest rates raised by 0.25% to 5.75%

> The Committee reviewed monetary and economic developments since its previous meeting. **The outlook for world economic activity has strengthened. Prospective growth in domestic demand remains strong: increases in wealth, labour income and household borrowing all suggest that consumer spending will continue to grow robustly**. Inflation is currently below the 2½% target and is expected to remain so for a while, but it is likely to rise above target further ahead, reflecting developing pressures in the labour market and on productive capacity. Accordingly the Committee concluded that an increase in interest rates of 0.25% to 5.75% was needed to meet the inflation target in the medium term.

House prices were still rising after the two previous rises in interest rates. At the time the Halifax reported that house prices rose by 3.4% in the final quarter of 1999 and by 11.5% for the year as a whole.[13]

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[13] *No time for half measures* The Guardian, 14 January 2000.

Date: 10 February 2000
Decision: Interest rates raised by 0.25% to 6.00%

No Statement released

Date: 8 February 2001
Decision: Interest rates reduced by 0.25% to 5.75%

No Statement released

The MPC's decision to reduce the interest rate by 0.25% was the first change in twelve-months and followed reduced expectations of GDP growth and falls in equity prices both in the UK and internationally.

Preliminary estimates suggested that the quarter on quarter UK GDP growth rate had eased to 0.3% in 2000 Q4 from 0.7% in 2000 Q3, although the average of new forecasts for UK GDP growth in 2001 remained constant at 2.6% between December 2000 and January 2001.[14] International Consensus forecasts of GDP growth in the US for 2001 fell from 3.0% to 2.6%, from 2.0% to 1.8% for Japan and from 3.0% to 2.9% for the Euro zone.[15]

A reduction in the share price of high technology companies lead to a fall in the FTSE from September 2000 to January 2001 of over 11%.[16] Share prices had also fallen in other major markets over the same period; the US S&P 500, Japan Nikkei 225 and Germany DAX indices fell by approximately 13%, 19% and 13% respectively.[17]

Date: 5 April 2001
Decision: Interest rates reduced by 0.25% to 5.5%

> **While growth in final domestic demand has remained firm, there are downside risks to UK activity from the slowdown in the global economy, the recent fall in equity markets and, in the short run, from foot and mouth disease.** These developments could already have affected demand and output growth and may continue to do so, in particular through their impact on business and consumer confidence. Inflation is currently somewhat below target, and is expected to remain so for a while. Price and cost pressures continue to be subdued. There is little sign of any easing yet in the labour market but, despite its tightness, settlements and earnings growth have so far remained moderate. In addition, the strength of sterling continues to exert a dampening effect on inflation.

14 HM Treasury, *Forecasts for the UK economy: A comparison of independent forecasts*, various months
15 Bank of England, *Minutes of MPC Meeting 7 and 8 February 2001*, 21 February 2001
16 *Financial Statistics*, National Statistics, May 2001, table 7.1G
17 Financial Times Market Watch web site, www.ftmarketwatch.com as at 10 June 2001

The move triggered an immediate response from banks and building societies reducing mortgage rates to their lowest level for 36 years.

Date: 10 May 2001
Decision: Interest rates reduced by 0.25% to 5.25%

> The world economic prospect has on balance continued to weaken. The extent and duration of the slowdown remain uncertain. In the UK, final domestic demand has so far remained firm, but **output growth in Q1 was slower than expected and there has been some weakening in business confidence**. The labour market remains tight. While the latest data showed faster earnings growth, this was largely the result of temporary factors, and settlements remain broadly stable. More generally, price and cost pressures are subdued. As the Committee noted a month ago, inflation is currently somewhat below target, and is expected to remain so for a while.

Preliminary estimates of UK GDP in 2001 Q1 suggested the quarter on quarter growth of GDP had eased for the third quarter running. The quarter on quarter UK GDP growth rate had eased to 0.3% in 2001 Q1 from a revised 0.4% in 2000 Q4,[18] although the average of new forecasts for UK GDP growth in 2001 remained constant at 2.6%.[19]

Date: 2 August 2001
Decision: Interest rates reduced by 0.25% to 5.00%

> Indicators of **world economic activity have been weaker than expected over the past few months. This and the persistent strength of sterling** are adding to the pressures on the externally exposed sectors of the UK economy, and at the same time there are signs of weakening investment growth. By contrast, retail spending, household borrowing and the housing market are still robust, partly supported by recent reductions in interest rates. On balance, the outlook, although highly uncertain, is for aggregate demand and output growth to be weaker than previously projected.
>
> **Although RPIX inflation has picked up in recent months, that partly reflects erratic factors**, and underlying price and cost pressures are expected to remain subdued. Monetary policy needs to balance the weaker external environment by sustaining domestic demand growth.

Date: 18 September 2001
Decision: Interest rates reduced by 0.25% to 4.75%

> **The Committee considered the reaction of financial markets to the tragic events of last week; it considered the Federal Reserve's decision to reduce**

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[18] National Statistics Press Release *Gross domestic product* 27 April 2001
[19] HM Treasury, *Forecasts for the UK economy: A comparison of independent forecasts*, various months

> **interest rates yesterday, and the responses of other central banks to that move. Falls in stock markets around the world, and the likely impact on confidence, suggest a weaker outlook for global activity than appeared likely at the Committee's meeting earlier this month. It is too early to make an informed judgment about the scale of the impact on the UK economy. But the direction of that impact and the associated risks are clear. The Committee decided that an immediate reduction of interest rates was, therefore, appropriate.**

This was the first and only special meeting of the MPC and followed a collapse in stock market confidence after the attacks in the US on 11 September 2001.

Date: 4 October 2001
Decision: Interest rates reduced by 0.25% to 4.50%

> The Committee reviewed the information about economic and financial developments which had become available since its scheduled meeting on 5-6 September and **the impact of the terrorist attacks in the United States on 11 September**, taking into account its decision at the special meeting on Tuesday 18 September to reduce interest rates by 0.25%.
>
> It now appears that, even before the terrorist attacks, the prospects for global activity were somewhat weaker than projected. **In the United Kingdom, revised data show that consumption and final domestic demand in the first half of this year had been growing faster than previously thought**, and remain stronger than in many other countries. Looking ahead, the consequences of the terrorist attacks for the UK and the world economy are still unclear. Early indications are that the direct impact on the UK economy will be less severe than in the United States. But the weaker world outlook and increased uncertainty have set back UK business and consumer confidence, and may, for a time, restrain business and household spending.

Date: 8 November 2001
Decision: Interest rates reduced by 0.5% to 4.00%

> World economic activity had weakened further, and evidence on the outlook now suggests that the global slowdown may be somewhat deeper and longer than previously thought. World inflationary pressures, including commodity prices, are weaker. In the United Kingdom, growth has so far remained close to trend. But reflecting the changed world outlook, the latest surveys of confidence and business activity have weakened. Meanwhile, cost and price pressures are somewhat more subdued.

Date: 6 February 2003
Decision: Interest rates reduced by 0.25% to 3.75%

> RPIX inflation has, as expected, moved a little above target, but this is the result of temporarily large contributions from petrol prices and from housing

> depreciation. These influences on inflation will persist for some time but are expected to unwind further ahead. **Over the next two years, the prospects for demand, both globally and domestically, are somewhat weaker than previously anticipated**.

This was the first meeting in over fourteen months where a decision to change the interest rate was made.

Date: 10 July 2003
Decision: Interest rates reduced by 0.25% to 3.50%

> The global economic recovery has remained hesitant. Although the preconditions for recovery remain in place, the prospect for external demand for UK output is weaker than previously expected. Output growth in the United Kingdom has recently been below trend. **Slower consumer demand and subdued private investment have so far offset the impact of higher public spending.** Although RPIX inflation is currently above the 2.5% target, this is the result of temporary factors which are expected to unwind in the coming months. Overall pay growth has been muted so far this year**. The fall in the sterling effective exchange rate since the start of this year should help underpin growth, but in recent weeks that fall has been partly reversed, reducing the prospective impact on inflation.** Against that background, and given the possibility of subdued economic activity continuing in the near term, the Committee judged that a reduction in official interest rates to 3.50% was necessary in order to keep inflation on track to meet the target in the medium term.

The 0.25% cut in interest rates to 3.50% reduced them to their lowest level since January 1955. The meeting was also notable for being the first for Mervyn King as Governor of the Bank and Chairman of the MPC.

IV Has the MPC worked?

A. Introduction

It may still be too soon to be able to judge, with any degree of confidence, whether or not the MPC has fulfilled the broad aims set out for it by the Chancellor:

> Now is the time for long-termism. This is the time to set the British economy on a new long-term course that will deliver high levels of growth and employment through lasting stability.
>
> Price stability is, as I have said, an essential precondition for the Government's objectives of high and sustainable levels of growth and employment. The question is how to achieve the long-term stability that we seek?[20]

[20] Chancellor's statement, HM Treasury press release, 6 May 1997

It may take longer than the six years of experience of the MPC we have to date, to see whether we can view its operations as a success or failure because in the international arena the past six years have been a period of relative stability. However, it is still possible to the achievements of the MPC so far.

B. Achievements

1. Conduct of the MPC

Perhaps the first achievement is that the Committee appears to have conducted its business in a harmonious manner. Differences of opinion and emphasis are acknowledged within the minutes of the discussion, however, there has been no obvious sign of public, off-the-record, briefings by disenchanted members or sudden acrimonious resignations. One can contrast this with what happened during the previous attempt at consensual advice giving by a group of economists and government, namely the Treasury's group of 'wise men' who gave advice to the Chancellor on the management of the economy. This group was set up in 1992 in the aftermath of the UK's exit from the ERM. It developed into a body with no coherent view and ended after some highly public rows between some of its members.

No less important in terms of the Committee's prestige and authority was the move taken in October 1997 to reduce the period between the date of the meeting and the publication of the minutes to just two weeks instead of the permitted six weeks delay. This move improved the transparency of the Committee's decisions and makes the job of the market in interpreting it and predicting future moves much simpler.[21]

2. Political consensus

Prior to the 1997 General Election the Conservative Party's manifesto promised to keep an inflation target of 2.5% but contained no references to the independence of the Bank suggesting that the Chancellor would continue to set the interest rate. While the Labour Party's manifesto did not use the word 'independence' it did contain a pledge to:

> reform the Bank of England to ensure that decision making on monetary policy is more effective, open, accountable and free from short-term political manipulation.

and the Liberal Democrats manifesto pledged to:

> turn the Bank of England into a UK Reserve Bank free from political interference.

[21] For an assessment of the impact of interest rate announcements on UK financial markets see *Assessing the impact of Macroeconomic news announcements on securities prices under different monetary policy regimes* Bank of England Working Paper Series, No 125, February 2001

Since independence the apparent success of the MPC in meeting its main objective has lead to political acceptance of Bank independence among the main parties. Almost immediately after his appointment as Shadow Chancellor, in February 2000, Michael Portillo reversed the Conservative Party's opposition to an independent Bank: [22]

> The next Conservative Government will respect the independence of the Bank of England and will legislate to enhance that independence and increase accountability to Parliament.

In setting out the Conservatives' macro-economic policy stance in December 2000 Michael Portillo expanded on their proposals for the terms of the Banks' independence:[23]

> I thoroughly welcome the independence of the monetary policy committee of the Bank of England. But I believe we should enhance that independence as well as better define its accountability to parliament. Again we must be aware that the new arrangements have not been tested in difficult conditions. Now is the time to think about how we can improve on what the government put in place in a hurry and without consultation. The Conservative Party appointed a distinguished commission on the Bank and we will be guided by the findings, which were published earlier this year. It must be made clear that the responsibility for setting the inflation target rests with the Chancellor of the Exchequer, who is responsible to parliament. The MPC is required to make the interest rate decisions necessary to achieve the Chancellor's target. In the event that the target is missed – because of some major systemic shock – in our view it is the Chancellor who should prescribe the path of intermediate inflation targets that must lead back towards the long-term inflation target.
>
> There is little guarantee under present arrangements that the members of the MPC will necessarily be independent or the right people, though I have no complaints about those who have actually taken up positions. For there to be greater confidence in the process, the members should be appointed following a fully transparent procedure… They should report to a special committee of parliament on the manner in which they have carried out their duties.
>
> The MPC should be encouraged, if it sees fit, to comment on whether it would have made different interest rate decisions had the fiscal stance been different; in other words the members should be entirely free to comment on any inconsistency between monetary and fiscal policy. I believe the Chancellor's inflation target of two-and-a-half per cent to be appropriate at present. There is a range around it, and if the MPC goes outside the range it is required to write to the Chancellor to explain how that situation has arisen and how it will be corrected. We think that appropriate too. But if the MPC continues to undershoot

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22 HC Deb 3 February 2000 vol 343 cc1189-91

23 Conservative Party News Release, *Five Disciplines for Macro-economic Policy*, Conservative Party web site as at 7 June 2001: www.conservatives.com/show_news_item.cfm?&obj_id=481&SPEECHES=1

> the inflation target, we will have to consider both whether to lower the target and whether to narrow the range.

At present, the main political parties agree to the operational independence of the Bank of England and the MPC. Both the Conservatives, who were initially opposed to the independence of the Bank, and the Liberal Democrats, have suggested that the Bank should become more independent still.

The Conservative Party in their 2001 General Election Manifesto on the economy stated:

> We will maintain the Monetary Policy Committee of the Bank of England, but enhance its independence. We have been investigating how the original independence arrangements […] can be improved.
>
> […] For example, we will ensure that the Committee is able to be robust to political pressure, by making its members' terms last no longer than a parliament. We also intend to ask the MPC to comment on whether its interest rate decisions would have been the same if the fiscal stance had been different.

The Liberal Democrat's present policy stance is given in their briefing document *Investing in Britain's Future Policies on the Economy*:

> We will make members of the Monetary Policy Committee more independent by giving them non-renewable terms and making them more representative of the UK as a whole. We will also make the appointments system more open and transparent.[24]

3. Long-term interest rates

One immediate benefit that followed the establishment of the MPC was a reduction in the long-term interest rate. Investors, it is argued, require a rate of return (interest) that will take into account the expected rate of inflation. If this falls then the rate of interest required by investors also falls. In the case of overseas investors they also consider any relative movement between the value of their domestic currency and the currency that the investment is denominated in. In its May 1997 Inflation report[25] the Bank noted that:

> The immediate reaction of financial markets to the Chancellor's announcement (which was accompanied by a $^1/_4$% rise in official interest rates) was marked (see the table). That was most evident in long-term bond yields, which reflect expectations of inflation, real interest rates and risk premia. Long gilt yields fell by around 30 basis points. And, ten-year nominal forward rates-fell by about 50 basis points. Because real forward rates were broadly constant, this implies a

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24 Liberal Democrat web site as at 17 October 2003: http://www.libdems.org.uk/documents/policies/Policy_Briefings/01_2003_Economy.pdf

25 Bank of England, *Inflation Report*, May 1997.

corresponding fall in measured inflation expectations, the inflation risk premia or both. It seems likely that the changes to the UK monetary framework announced by the Chancellor have, at least for the moment, improved the credibility of monetary policy.

Change in UK financial market measures

	Fri 2 May (a)	Tues 6 May (a)	Change (b)
£ Effective exchange rate	99.71	100.56	0.85%
DM/£	2.80	2.82	0.82%
$/£	1.62	1.64	1.17%
Ten-year nominal forward rate	7.83	7.31	-0.52
Ten-year implied forward inflation rate	4.17	3.70	-0.47
Ten-year zero coupon rate	7.39	7.07	-0.32
Three month Libor (c)	6.53	6.53	0.00
FF-SE 100 index level	4,455.60	4,519.30	1.43%

(a) Close of business.

(b) Percentage points, unless indicated. Data are between close of business on Friday 2 May and close of business on Tuesday 6 May.

(c) 8.30 am rate, following business day.

4. Price stability

On the key point of whether the MPC has actually hit its stated inflation target the news is ambiguous. The inflation target that the MPC is required to meet is a 2.5% increase, over the previous twelve months, in the retail prices index excluding mortgage interest payments. The Governor must write to the Chancellor if the rate moves more than plus or minus 1% from this. Over the period covered by this Paper the following monthly inflation rates, on the stated basis, have been recorded:

RPI(X)
Annual Changes

		per cent	Meets target?	over/under target			per cent	Meets target?	over/under target			per cent	Meets target?	over/under target
1997	June	2.7%	no	0.2%	**1999**	July	2.2%	no	-0.3%	**2001**	Aug	2.6%	no	0.1%
	July	3.0%	no	0.5%		Aug	2.1%	no	-0.4%		Sept	2.3%	no	-0.2%
	Aug	2.8%	no	0.3%		Sept	2.1%	no	-0.4%		Oct	2.3%	no	-0.2%
	Sept	2.7%	no	0.2%		Oct	2.2%	no	-0.3%		Nov	1.8%	no	-0.7%
	Oct	2.8%	no	0.3%		Nov	2.2%	no	-0.3%		Dec	1.9%	no	-0.6%
	Nov	2.8%	no	0.3%		Dec	2.2%	no	-0.3%	**2002**	Jan	2.6%	no	0.1%
	Dec	2.7%	no	0.2%	**2000**	Jan	2.1%	no	-0.4%		Feb	2.2%	no	-0.3%
1998	Jan	2.5%	yes	0.0%		Feb	2.2%	no	-0.3%		Mar	2.3%	no	-0.2%
	Feb	2.6%	no	0.1%		Mar	2.0%	no	-0.5%		Apr	2.3%	no	-0.2%
	Mar	2.6%	no	0.1%		Apr	1.9%	no	-0.6%		May	1.8%	no	-0.7%
	Apr	3.0%	no	0.5%		May	2.0%	no	-0.5%		June	1.5%	no	-1.0%
	May	3.2%	no	0.7%		June	2.2%	no	-0.3%		July	2.0%	no	-0.5%
	June	2.8%	no	0.3%		July	2.2%	no	-0.3%		Aug	1.9%	no	-0.6%
	July	2.6%	no	0.1%		Aug	1.9%	no	-0.6%		Sept	2.1%	no	-0.4%
	Aug	2.5%	no	0.0%		Sept	2.2%	no	-0.3%		Oct	2.3%	no	-0.2%
	Sept	2.5%	yes	0.0%		Oct	2.0%	no	-0.5%		Nov	2.8%	no	0.3%
	Oct	2.5%	yes	0.0%		Nov	2.2%	no	-0.3%		Dec	2.7%	no	0.2%
	Nov	2.5%	yes	0.0%		Dec	2.0%	no	-0.5%	**2003**	Jan	2.7%	no	0.2%
	Dec	2.6%	yes	0.1%	**2001**	Jan	1.8%	no	-0.7%		Feb	3.0%	no	0.5%
1999	Jan	2.6%	no	0.1%		Feb	1.9%	no	-0.6%		Mar	3.0%	no	0.5%
	Feb	2.4%	no	-0.1%		Mar	1.9%	no	-0.6%		Apr	2.9%	no	0.4%
	Mar	2.7%	no	0.2%		Apr	2.0%	no	-0.5%		May	2.8%	no	0.3%
	Apr	2.4%	no	-0.1%		May	2.4%	no	-0.1%		June	2.9%	no	0.4%
	May	2.1%	no	-0.4%		June	2.4%	no	-0.1%		July	2.9%	no	0.4%
	June	2.2%	no	-0.3%		July	2.2%	no	-0.3%		Aug	2.8%	no	0.3%

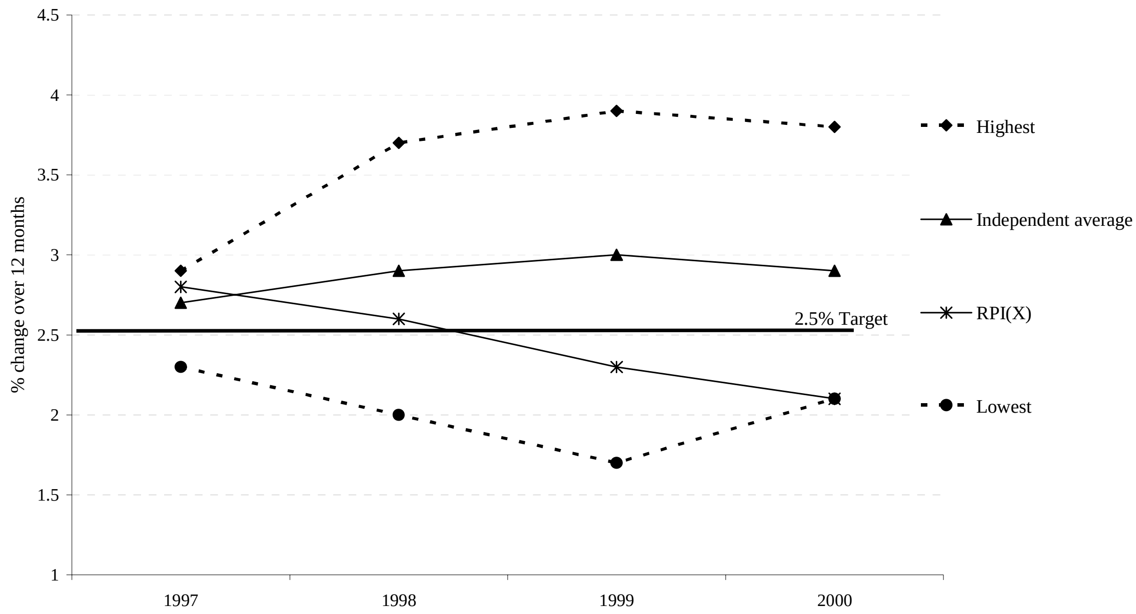
Source: National Statistics First Releases, various dates

Is this good or a bad performance? Only five out of the seventy five rates have met the target exactly but none have been far enough away that the Governor has had to write to the Chancellor with an explanation. Twelve of the last fifty three rates have all undershot the target, suggesting that MPC policy may have been too 'tight'.

All the inflation rates are good by historical standards.[26] However, in the light of the downturn in both the UK and international economies and the general collapse in world commodity prices this has been a period during which background economic conditions have been conducive to low inflation.

Another way to compare the performance of the MPC is to compare inflation over the period with what had been the forecast immediately prior to its establishment. In the chart below, the actual average annual inflation rate RPI (X)[27] is compared to the average and range of forecasts made by independent groups, themselves influenced by their knowledge of the government's inflation target (that at the time was a 1-2.5% target range).[28]

Forecast and actual annual percentage change RPI(X), 1997 to 2000



The chart confirms the view that inflation has been substantially lower than most forecasters predicted in 1997. However, it is still just within the range that economists thought it would be. Of course this type of comparison is as much a test of the predictive abilities of a particular group of economists as it is of the MPC.

26 Long term RPI(X) is shown in chart form in Appendix II
27 National Statistics First Release, 15 May 2001
28 HM Treasury, *Forecasts for the UK economy: A comparison of independent forecasts*, No 121, May 1997

5. Secondary objectives

As set out in the Section 11 of the *Bank of England Act 1998*, subject to maintaining price stability, the secondary objectives of the MPC are;

> to support the economic policy of Her Majesty's Government, including its objectives for growth and employment.[29]

Since the MPC was set up, real gross domestic product (GDP) in the UK has grown by an average of 0.6% per quarter.[30] In the same time period prior to the MPC being set up, real GDP grew by an average of 0.7% per quarter. On its own this would appear to show that growth has fallen since the MPC was created. However, average quarterly UK growth during this period is higher than in Japan, Germany, Italy and the euro zone as a whole.[31] Employment over the period has risen by just over 5.5%[32] while unemployment, depending on the definition, has fallen by between 28% and 40%.[33]

The figures suggest that the MPC has achieved its primary objective of price stability whilst growth has remained relatively constant and employment has risen, thereby also achieving its' secondary objectives.

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29 Long term GDP and employment data are shown in chart form in Appendices III
30 National Statistics database, series YBEZ
31 OECD
32 National Statistics database, series MGRZ
33 ILO Unemployment and Claimant count unemployment respectively, National Statistics database series, MGSC, BCJD

Appendix I: MPC Voting Records June 1997 - 2001

Monetary Policy Committee
Membership Voting Record, Bank Representatives, June 1997- June 2001

Date of announcement		Decision	Sir Edward George	Mervyn King	David Clemanti	Ian Plenderleith	John Vickers	Howard Davies	Charles Bean
1997	Jun 6	$^{1}/_{4}$% increase	1	1	1	1	na	na	na
	Jul 10	$^{1}/_{4}$% increase	1	1	na	1	na	1	na
	Aug 7	$^{1}/_{4}$% increase	1	1	na	1	na	na	na
	Sept 11	no change	1	1	1	1	na	na	na
	Oct 9	no change	1	1	1	1	na	na	na
	Nov 6	$^{1}/_{4}$% increase	1	1	1	1	na	na	na
	Dec 4	no change	1	1	1	1	na	na	na
1998	Jan 8	no change	1	1	1	1	na	na	na
	Feb 5	no change	1	2	1	1	na	na	na
	Mar 5	no change	1	2	1	1	na	na	na
	Apr 9	no change	1	2	1	1	na	na	na
	May 7	no change	1	1	1	1	na	na	na
	Jun 4	$^{1}/_{4}$% increase	1	1	1	1	1	na	na
	Jul 9	no change	1	1	1	1	1	na	na
	Aug 6	no change	1	1	1	1	1	na	na
	Sept 10	no change	1	1	1	1	1	na	na
	Oct 8	$^{1}/_{4}$% decrease	1	1	1	1	1	na	na
	Nov 5	$^{1}/_{2}$% decrease	1	1	1	1	1	na	na
	Dec 10	$^{1}/_{2}$% decrease	1	1	1	1	1	na	na
1999	Jan 7	$^{1}/_{4}$% decrease	1	1	1	2	1	na	na
	Feb 4	$^{1}/_{2}$% decrease	1	1	1	1	1	na	na
	Mar 3	no change	1	1	1	1	1	na	na
	Apr 8	$^{1}/_{4}$% decrease	1	1	1	1	1	na	na
	May 6	no change	1	1	0	0	1	na	na
	June 10	$^{1}/_{4}$% decrease	1	2	1	1	1	na	na
	July 8	no change	1	1	1	1	1	na	na
	Aug 5	no change	1	1	1	1	1	na	na
	Sept 8	$^{1}/_{4}$% increase	1	1	1	1	1	na	na
	Oct 7	no change	1	1	1	1	1	na	na
	Nov 4	$^{1}/_{4}$% increase	1	1	1	1	1	na	na
	Dec 9	no change	1	2	1	1	2	na	na
2000	Jan 13	$^{1}/_{4}$% increase	1	1	1	1	1	na	na
	Feb 10	$^{1}/_{4}$% increase	1	1	1	1	1	na	na
	Mar 9	no change	1	1	1	1	1	na	na
	Apr 6	no change	1	2	1	1	2	na	na
	May 4	no change	1	1	1	1	1	na	na
	June 7	no change	1	2	1	1	2	na	na
	July 6	no change	1	1	1	1	1	na	na
	Aug 3	no change	1	2	2	1	2	na	na
	Sept 7	no change	1	2	2	1	2	na	na
	Oct 5	no change	1	1	1	1	na	na	1
	Nov 9	no change	1	1	1	1	na	na	1
	Dec 7	no change	1	1	1	1	na	na	1
2001	Jan 11	no change	1	1	1	1	na	na	0
	Feb 8	$^{1}/_{4}$% decrease	1	1	1	1	na	na	1
	Mar 8	no change	1	1	1	1	na	na	1
	Apr 4	$^{1}/_{4}$% decrease	1	1	1	0	na	na	1
	May 10	$^{1}/_{4}$% decrease	1	1	1	1	na	na	1
	June 6	no change	1	1	1	1	na	na	1

Notes: 1 - vote was in accordance with majority view
2 - vote was for a rate of interest higher than the majority view
0 - vote was for a rate of interest lower than the majority view
* - attended as Treasury observer - no vote   na - did not attend, not appointed or had left at that date

Source: MPC *Monthly minutes*, various months

Monetary Policy Committee

Membership Voting Record, Outside Representatives, June 1997- June 2001

Date of announcement		Decision	Sir Alan Budd	Professor Willem Buiter	Professor Charles Goodhart	Dr Deanne Julius	Dr Sushil Wadhwani	Professor Stephen Nickell	Christopher Allsopp	Kate Barker
1997	Jun 6	$^{1}/_{4}$% increase	*	1	1	na	na	na	na	na
	Jul 10	$^{1}/_{4}$% increase	*	1	1	na	na	na	na	na
	Aug 7	$^{1}/_{4}$% increase	*	1	1	na	na	na	na	na
	Sept 11	no change	*	1	1	1	na	na	na	na
	Oct 9	no change	*	1	1	1	na	na	na	na
	Nov 6	$^{1}/_{4}$% increase	na	1	1	1	na	na	na	na
	Dec 4	no change	1	1	1	1	na	na	na	na
1998	Jan 8	no change	2	2	2	1	na	na	na	na
	Feb 5	no change	2	2	2	1	na	na	na	na
	Mar 5	no change	2	2	2	1	na	na	na	na
	Apr 9	no change	2	2	1	1	na	na	na	na
	May 7	no change	1	2	1	0	na	na	na	na
	Jun 4	$^{1}/_{4}$% increase	1	1	1	0	na	na	na	na
	Jul 9	no change	1	1	1	1	na	na	na	na
	Aug 6	no change	1	2	1	0	na	na	na	na
	Sept 10	no change	1	0	1	0	na	na	na	na
	Oct 8	$^{1}/_{4}$% decrease	1	0	1	0	na	na	na	na
	Nov 5	$^{1}/_{2}$ % decrease	1	0	1	1	na	na	na	na
	Dec 10	$^{1}/_{2}$ % decrease	1	0	1	1	na	na	na	na
1999	Jan 7	$^{1}/_{4}$% decrease	1	1	1	0	na	na	na	na
	Feb 4	$^{1}/_{2}$ % decrease	1	0	1	1	na	na	na	na
	Mar 3	no change	1	0	1	1	na	na	na	na
	Apr 8	$^{1}/_{4}$% decrease	1	0	1	1	na	na	na	na
	May 6	no change	1	0	1	0	na	na	na	na
	June 10	$^{1}/_{4}$% decrease	na	1	1	1	1	na	na	na
	July 8	no change	na	1	1	1	1	na	na	na
	Aug 5	no change	na	1	1	1	1	na	na	na
	Sept 8	$^{1}/_{4}$% increase	na	1	1	0	0	na	na	na
	Oct 7	no change	na	1	1	1	1	na	na	na
	Nov 4	$^{1}/_{4}$% increase	na	1	1	0	1	na	na	na
	Dec 9	no change	na	2	1	1	1	na	na	na
2000	Jan 13	$^{1}/_{4}$% increase	na	2	1	1	1	na	na	na
	Feb 10	$^{1}/_{4}$% increase	na	1	1	0	1	na	na	na
	Mar 9	no change	na	1	1	1	1	na	na	na
	Apr 6	no change	na	2	1	1	1	na	na	na
	May 4	no change	na	1	1	1	1	na	na	na
	June 7	no change	na	na	na	1	1	2	1	na
	July 6	no change	na	na	na	1	1	1	1	na
	Aug 3	no change	na	na	na	1	1	2	1	na
	Sept 7	no change	na	na	na	1	1	2	1	na
	Oct 5	no change	na	na	na	1	1	1	1	na
	Nov 9	no change	na	na	na	1	1	1	1	na
	Dec 7	no change	na	na	na	0	0	1	1	na
2001	Jan 11	no change	na	na	na	0	0	1	0	na
	Feb 8	$^{1}/_{4}$% decrease	na	na	na	1	1	1	1	na
	Mar 8	no change	na	na	na	0	0	1	1	na
	Apr 4	$^{1}/_{4}$% decrease	na	na	na	0	0	1	1	na
	May 10	$^{1}/_{4}$% decrease	na	na	na	1	0	1	1	na
	June 6	no change	na	na	na	na	0	1	1	1

Notes: 1 - vote was in accordance with majority view

2 - vote was for a rate of interest higher than the majority view

0 - vote was for a rate of interest lower than the majority view

* - attended as Treasury observer - no vote

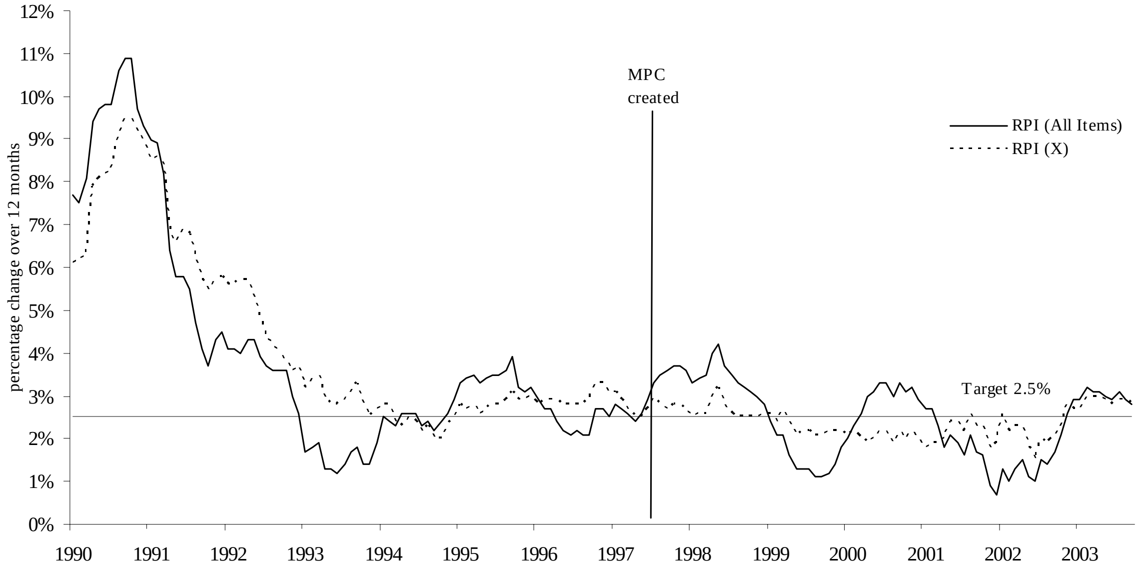
na - did not attend, not appointed or had left at that date

Source: MPC *Monthly minutes*, various months

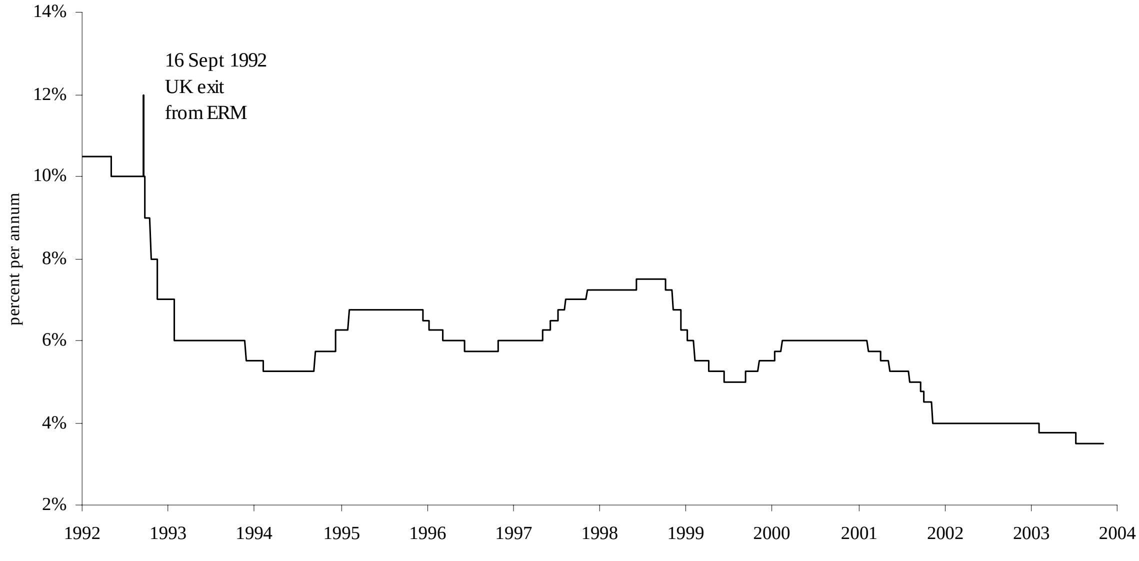
Appendix II: Inflation & Interest Rates

Indicators of inflation and interest rate performance are shown in the charts below:

Retail Prices Index 1990 - 2003



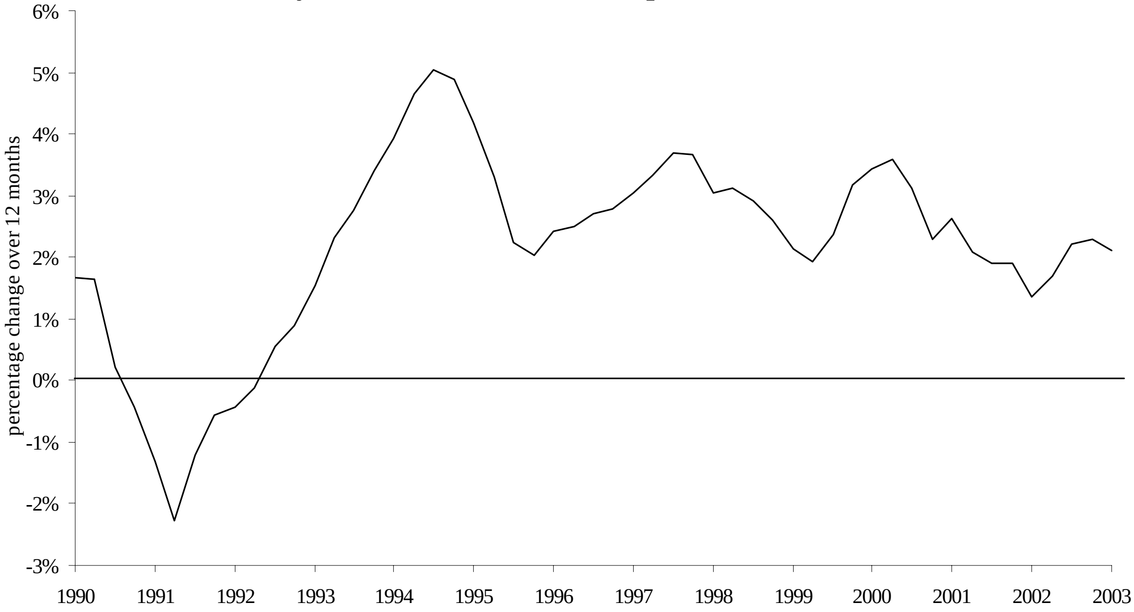
Base / Repo Rates 1992 - 2003



Appendix III: GDP and employment

Indicators of GDP and employment performance are shown in the charts below:

Quarterly GDP at constant market prices 1990Q1 - 2003Q1



Total Employment, January 1995 - 2003