Bank of England

Monetary Policy Summary and minutes of the Monetary Policy Committee meeting ending on 4 May 2022

5 May 2022

These are the minutes of the Monetary Policy Committee meeting ending on 4 May 2022.

They are available at **https://www.bankofengland.co.uk/monetary-policy-summary-and-minutes/2022/may-2022**.

The Bank of England Act 1998 gives the Bank of England operational responsibility for setting monetary policy to meet the Government's inflation target. Operational decisions are taken by the Bank's Monetary Policy Committee. The minutes of the Committee meeting ending on 15 June will be published on 16 June 2022.

Monetary Policy Summary, May 2022

The MPC sets monetary policy to meet the 2% inflation target, and in a way that helps to sustain growth and employment. At its meeting ending on 4 May 2022, the MPC voted by a majority of 6-3 to increase Bank Rate by 0.25 percentage points, to 1%. Those members in the minority preferred to increase Bank Rate by 0.5 percentage points, to 1.25%.

Global inflationary pressures have intensified sharply following Russia's invasion of Ukraine. This has led to a material deterioration in the outlook for world and UK growth. These developments have exacerbated greatly the combination of adverse supply shocks that the United Kingdom and other countries continue to face. Concerns about further supply chain disruption have also risen, both due to Russia's invasion of Ukraine and to Covid-19 developments in China.

UK GDP is estimated to have risen by 0.9% in 2022 Q1, stronger than expected in the February Monetary Policy Report. The unemployment rate fell to 3.8% in the three months to February, and is likely to fall slightly further in coming months, consistent with a continuing tightening in the labour market and with a margin of excess demand at present. Surveys of business activity have generally remained strong. There have, however, been signs from indicators of retail spending and consumer confidence that the squeeze on real disposable incomes is starting to weigh on the household sector. The level of GDP is expected to be broadly unchanged in Q2.

Twelve-month CPI inflation rose to 7.0% in March, around 1 percentage point higher than expected in the February Report. The strength of inflation relative to the 2% target mainly reflects previous large increases in global energy and tradable goods prices, the latter of which is due to the shift in global demand towards durable goods and to supply chain disruptions.

The Committee's updated central projections for activity and inflation are set out in the accompanying May Monetary Policy Report. The projections are conditioned on a market-implied path for Bank Rate that rises to around 2½% by mid-2023, before falling to 2% at the end of the forecast period. Fiscal policy is assumed to evolve in line with announced Government policies. Wholesale energy prices are assumed to follow their respective futures curves for the first six months of the projections and remain constant beyond that, in contrast to futures curves, which are downward sloping over coming years. There are material risks around this assumption.

In the May Report central projection, CPI inflation is expected to rise further over the remainder of the year, to just over 9% in 2022 Q2 and averaging slightly over 10% at its

peak in 2022 Q4. The majority of that further increase reflects higher household energy prices following the large rise in the Ofgem price cap in April and projected additional large increase in October. The price cap mechanism means that it takes some time for increases in wholesale gas and electricity prices, and their respective futures curves, to be reflected in retail energy prices. Given the operation of the price cap, consumer price inflation is likely to peak later in the United Kingdom than in many other economies, and may therefore fall back later. The expected rise in CPI inflation also reflects higher food, core goods and services prices.

Underlying nominal earnings growth has risen by more than projected in the February Report and is expected to strengthen in coming months, given the further tightening of the labour market and some upward pressure from higher price inflation. Companies generally expect to increase their selling prices strongly in the near term, following the sharp rises in their costs, with many reporting confidence that they will be able to rebuild at least some of their margins.

Nonetheless, in the May Report central projection, UK GDP growth is expected to slow sharply over the first half of the forecast period. That predominantly reflects the significant adverse impact of the sharp rises in global energy and tradable goods prices on most UK households' real incomes and many UK companies' profit margins. Although the unemployment rate is likely to fall slightly further in the near term, it is expected to rise to 5½% in three years' time given the sharp slowdown in demand growth. Excess supply builds to 2¼% by the end of the forecast period.

With monetary policy acting to ensure that longer-term inflation expectations are anchored at the 2% target, upward pressure on CPI inflation is expected to dissipate over time. Global commodity prices are assumed to rise no further in the central projection, global bottlenecks ease over time, and the weakening in demand growth and building excess supply lead domestic inflationary pressures to subside.

Conditioned on the rising market-implied path for Bank Rate and the MPC's current forecasting convention for future energy prices, CPI inflation is projected to fall to a little above the 2% target in two years' time, largely reflecting the waning influence of external factors, and to 1.3% in three years, well below the target and mainly reflecting weaker domestic pressures. The risks to the inflation projection are judged to be skewed to the upside at these points, given the risks of more persistent strength in nominal wage growth and domestic price setting than assumed.

The MPC's remit is clear that the inflation target applies at all times, reflecting the primacy of price stability in the UK monetary policy framework. The framework also recognises that there will be occasions when inflation will depart from the target as a result of shocks and disturbances. The economy has recently been subject to a

succession of very large shocks. Russia's invasion of Ukraine is another such shock. In particular, should recent movements prove persistent as the central projections assume, the very elevated levels of global energy and tradable goods prices, of which the United Kingdom is a net importer, will necessarily weigh further on most UK households' real incomes and many UK companies' profit margins. This is something monetary policy is unable to prevent. The role of monetary policy is to ensure that, as this real economic adjustment occurs, it does so in a manner consistent with achieving the 2% inflation target sustainably in the medium term, while minimising undesirable volatility in output.

Recent developments have exacerbated materially both the near-term peak in CPI inflation, and the prospective negative impact on activity and medium-term inflationary pressures. Nevertheless, given the current tightness of the labour market, continuing signs of robust domestic cost and price pressures, and the risk that those pressures will persist, the Committee voted to increase Bank Rate by 0.25 percentage points at this meeting.

Based on their updated assessment of the economic outlook, most members of the Committee judge that some degree of further tightening in monetary policy may still be appropriate in the coming months. There are risks on both sides of that judgement and a range of views among these members on the balance of risks. The MPC will continue to review developments in the light of incoming data and their implications for medium-term inflation.

The Committee reaffirms its preference in most circumstances to use Bank Rate as its active policy tool when adjusting the stance of monetary policy. As Bank Rate is now being increased to 1%, and consistent with the MPC's previous guidance, the Committee will consider beginning the process of selling UK government bonds held in the Asset Purchase Facility. The Committee reaffirms that the decision to commence sales will depend on economic circumstances including market conditions at the time, and that sales would be expected to be conducted in a gradual and predictable manner so as not to disrupt the functioning of financial markets. The Committee recognises the benefits of providing market participants with clarity on the framework for any potential sales programme. The Committee has therefore asked Bank staff to work on a strategy for UK government bond sales, and will provide an update at its August meeting. This will allow the Committee to make a decision at a subsequent meeting on whether to commence sales.

Minutes of the Monetary Policy Committee meeting ending on 4 May 2022

1. Before turning to its immediate policy decision, and against the backdrop of its latest economic projections, the Committee discussed: the international economy; monetary and financial conditions; demand and output; and supply, costs and prices.

The international economy

2. The economic consequences of the Russian invasion of Ukraine had started to be felt globally. From already elevated levels, increases in the prices of energy and other commodities since the start of the war had put further upward pressure on producer and consumer price inflation, weighing on real incomes. Concerns around supply chain bottlenecks had also risen, owing both to the war in Ukraine and to Covid-19 (Covid) developments in China. These developments were consistent with a deterioration in the outlook for global growth. UK-weighted global GDP was expected to grow only slightly in 2022 Q2, materially slower than had been anticipated at the time of the February Monetary Policy Report.

3. European economies were expected to be particularly affected by the war in Ukraine given their dependence on energy imports. Euro-area GDP was expected to grow only a little in 2022 Q2, at a rate significantly lower than had been anticipated in the February Report, following growth of 0.2% in Q1 according to the preliminary flash release. In the first quarter, the economic impact of the Omicron variant had been somewhat less than had been anticipated in the February Report, and indicators suggested that services activity had continued to expand into the second quarter as Covid restrictions had eased. Nonetheless, the war in Ukraine had weighed on growth prospects, particularly in the manufacturing sector, with output PMIs declining in April. Forward-looking indicators of business expectations and consumer confidence had also weakened significantly since the invasion. The outlook for Central and Eastern European countries had worsened, and their currencies had depreciated relative to the US dollar since the MPC’s last meeting, partly reflecting the strength of their trade linkages with Russia. Ukraine’s economic output was expected to decline materially as a direct consequence of the war. The Russian economy was also expected to contract significantly this year.

4. According to the advance estimate, US GDP had contracted by 0.4% in 2022 Q1, driven primarily by a widening of the trade deficit and weak inventory investment. Although this was weaker than had been anticipated in the February Report, underlying

demand, namely personal consumption and gross private fixed investment, had remained strong in the first quarter, and spending had continued to rotate back towards services from goods. As a net exporter of oil and with retail gas prices having not risen by as much in absolute terms as in Europe, the US economy was expected to be relatively less affected by developments in commodity prices, albeit not fully shielded, and GDP was expected to expand reasonably strongly in the second quarter. The US labour market had remained tight, with the unemployment rate falling to 3.6% in March, close to pre-Covid levels. Wage growth had continued to rise, according to the Federal Reserve Bank of Atlanta's measure.

5. China had been experiencing a significant outbreak of Covid cases, against an already challenging economic backdrop, including stresses in the property sector. The authorities had imposed lockdowns in a number of large cities, including Shanghai, in late March. As a result of these developments, China's GDP was expected to grow more slowly in 2022 Q2 than had been anticipated in the February Report, by 0.8%. This would also be weaker than in Q1, when GDP had grown by 1.3%. Consistent with the Chinese authorities' approach to supporting manufacturing during Covid outbreaks, for example through closed-loop production systems in which workers remained on factory sites, industrial production growth had fallen by less than retail sales growth in March. Some ports in affected cities had experienced congestion and there had been widespread reports of delays to road freight, adding to global supply chain pressures. Although delays had started to ease, further disruptions were possible over the coming months.

6. Supply chain constraints had also arisen due to Russia's invasion of Ukraine, intensifying global cost pressures. Russia and Ukraine were major producers of many inputs, ranging from metals and food to fertilisers, as well as oil and natural gas. The war had led to broad increases in commodity prices, although some had fallen back from their peaks over recent weeks. The spot price of Brent crude oil had increased by around 25% to $106 per barrel since the February Report.

7. European gas prices had risen sharply following the invasion, before moderating. Russia's decision to cease gas flows to Poland and Bulgaria in late April had led to a short-lived increase in the Dutch Title Transfer Facility (TTF) spot price, which now stood at around €100 per MWh, broadly the same level as at the MPC's March meeting and around 20% higher than at the time of the February Report. The TTF futures curve remained at around this level for just under a year before declining notably. A wedge had opened up between the TTF and UK spot gas prices, with UK contracts trading at a lower level of around €65 per MWh, or 160 pence per therm. This was due to large liquefied natural gas (LNG) shipments to the United Kingdom, alongside a rebound in output from Norwegian gas fields and seasonally warmer weather. This wedge

persisted in the futures curve for about six months, at which point the UK futures price rose to the TTF futures price as LNG shipments to the UK were expected to be more in line with capacity to re-export to the European Union.

8. Over recent weeks, metals prices had fallen to levels a little above those at the time of the February Report in aggregate, although the prices of some metals such as nickel and zinc had remained elevated. Food prices, including wheat and corn, had remained substantially higher than at the time of the February Report.

9. Against this backdrop of strong commodity prices, global consumer price inflation had continued to rise. In the euro area, annual HICP inflation had increased to 7.5% in April, with core inflation at 3.5%. In the United States, annual CPI inflation had risen to 8.5% in March, with core inflation at 6.5%, while headline PCE inflation had increased to 6.6%. Much of the increase in US CPI inflation had been due to higher contributions from energy prices, but core goods and services components had continued to make the largest contributions to the inflation rate. In the euro area, energy prices had been the main contributor to inflation, although core inflation had risen sharply in April. Measures of inflation expectations had generally increased in advanced economies, in particular at shorter horizons.

10. The Committee discussed the risks around the global inflation outlook, and the implications for growth. There was an upside risk to the future path for energy prices, particularly gas prices, for example if flows of Russian gas to large euro-area countries slowed significantly. Under such a scenario, European gas prices would be likely to increase sharply and gas quantities could be rationed going into next winter as EU gas stocks might run low. There was also an upside risk to inflation from further price pressures related to global supply chain disruptions. Additional constraints affecting transportation capacity, inputs to industrial processes and agricultural production were possible, both owing to the war in Ukraine and if there were further severe Covid outbreaks in China. Set against the backdrop of continuing strong US consumer demand, this could generate further increases in core goods prices, although lower demand from China could reduce commodity prices at the margin. Finally, there was a risk that tight labour markets and strong wage growth, coupled with higher inflation expectations, could lead to further inflationary pressures in advanced economies. Additional price pressures could lead to a further deterioration in the global growth outlook as real incomes were squeezed, reducing consumer spending and exacerbating the policy challenges facing central banks around the world.

Monetary and financial conditions

11. Since the MPC's previous meeting, advanced-economy government bond yields had risen significantly and by more in the United States and in the euro area than in the

United Kingdom. Ten-year yields had increased by around 80 basis points in the United States, 65 basis points in the euro area and 35 basis points in the United Kingdom.

12. The near-term path for market-implied policy rates in the United States had risen significantly since the MPC's previous meeting. At its March meeting, the Federal Open Market Committee had increased the target range for the federal funds rate to 0.25-0.50% and had given an indication that the Committee was well placed to begin the process of reducing the size of the Federal Reserve's balance sheet as early as May and at a quicker pace than during the 2017-19 episode of balance sheet reduction. The market-implied policy rate in the United States reached 2.8% by end-2022 and peaked at around 3.4% in 2023. In the euro area, the near-term market-implied path for policy rates had also risen since the MPC's previous meeting. At its meeting on 14 April, the ECB Governing Council had left its key policy interest rates unchanged and had noted that recent data had reinforced its expectation that net asset purchases should be concluded in the third quarter of 2022.

13. In the United Kingdom, market pricing was consistent with an increase in Bank Rate of 0.25 percentage points, to 1% at this MPC meeting, and market-implied expectations for the path of Bank Rate had risen further out. The May Monetary Policy Report was conditioned on a market-implied path for Bank Rate, based on the 15-working day average to 26 April, that rose to around 2% by end-2022, peaked at 2.6% in 2023 and then fell back to around 2% in three years' time. The results of the Bank of England's Market Participants Survey had indicated broadly similar expectations for Bank Rate in the near term, with almost all respondents expecting a 0.25 percentage point increase at this meeting. Respondents expected a much lower central path for Bank Rate than the market-implied path further ahead, albeit a significant number of respondents viewed the balance of risks around that path as being skewed to the upside rather than to the downside over the next two years, reconciling at least in part the difference with market-implied expectations.

14. Short-term financial market inflation compensation measures in the United Kingdom had increased since the MPC's previous meeting, in part reflecting the continued impact of Russia's invasion of Ukraine on gas and other energy prices. At the same time, medium-term inflation compensation measures in the United Kingdom had fallen modestly, but they had remained above their levels at the time of the February Report and above their average levels of the past decade. Intelligence gathered from market contacts, suggested that higher inflation expectations and greater perceived upside risks to inflation might have in part accounted for these above-average levels of medium-term inflation compensation measures, alongside other factors.

15. The US dollar effective exchange rate had appreciated by around 2% since the MPC's March meeting, as interest rate differentials had widened. The sterling effective

exchange rate had depreciated by around 1%, while the euro effective exchange rate had remained broadly unchanged.

16. US and euro-area equity prices had been broadly unchanged since the MPC's previous meeting. The FTSE All-Share index had increased to levels seen prior to the invasion of Ukraine, but the UK-focussed FTSE index, which had been less supported by the rise in energy prices, had remained below levels seen prior to the invasion. There had been less adjustment in the corporate bond market.

17. UK bank lending rates on mortgages with loan-to-value (LTV) ratios at or below 75% had risen further since the MPC's previous meeting. This was broadly consistent with a lagged response to the increases in risk-free rates since the autumn of 2021. Lending rates on higher LTV mortgages and sight deposit rates had also started to increase. The further increases in risk-free rates that had occurred since the March MPC meeting would be expected to feed through to mortgage rates in due course. Interest rates on unsecured household borrowing, such as credit cards and personal loans had, as usual, been less sensitive to changes in reference rates.

Demand and output

18. Starting with the most immediate quarter with a complete dataset, UK real GDP growth in 2021 Q4 had been revised up slightly, from 1.0% to 1.3%, with the level of GDP estimated to have been almost identical to that in 2019 Q4 prior to the pandemic. Within the expenditure components, household consumption had risen by 0.5% on the quarter and the saving ratio had fallen to 6.5%, its lowest level since the onset of the pandemic though still higher than during the pre-Covid period. Business investment had increased by 1.0% in Q4, leaving it around 8½% below its pre-pandemic level. Government spending had risen by 1.2%, to almost 9% above its pre-Covid level.

19. Turning to the latest available monthly data, GDP had increased by 0.1% in February, following 0.8% growth in January. The output of consumer-facing services had risen strongly in February, particularly in the accommodation and foods, and arts and recreation sectors, as the economic impact of the Omicron variant had unwound. Government services output had fallen back, as spending on NHS Test and Trace and the vaccination programme had declined. Manufacturing and construction output had fallen slightly on the month.

20. For the first quarter as a whole, Bank staff now expected GDP growth of 0.9%, stronger than the flat quarterly outturn that had been incorporated in the February Monetary Policy Report projection. That upward revision largely reflected higher-than-expected market-sector output.

21. There had been increasing signs that the squeeze on real disposable incomes was starting to weigh on the household sector. Retail sales volumes had fallen by 1.4% in March, following a 0.5% decline in February, with weakness in fuel, food store and non-store retailing. Nominal retail sales values had remained broadly stable, such that weaker sales volumes had been the counterpart to recent further increases in the sales deflator. GfK consumer confidence had declined sharply in April, to close to the previous low point for the series recorded in mid-2008. All five backward and forward looking sub-balances feeding into the headline confidence indicator had fallen on the month. Indicators of house prices and housing activity had remained robust, however.

22. Although some activity indicators from business surveys had weakened, they had remained notably stronger than their household survey counterparts. The S&P Global/CIPS flash composite output index had fallen from 60.9 in March to 57.6 in April, but had remained above its long-run average level. The composite new orders and output expectations series had fallen to around their long-run averages. According to contacts of the Bank's Agents, output was growing at a solid pace overall, with business services reporting strong growth. But growth had continued to be held back by shortages of labour and goods, with the latter worsening and becoming more widespread since the invasion of Ukraine and the increase in Covid-related restrictions in China. Investment intentions reported to the Agents had remained strong despite increasing uncertainty, although current investment spending was being held back by cost pressures and shortages of materials, goods and labour. Expected sales growth over the year between 2021 Q4 and 2022 Q4 had remained strong in the April Decision Maker Panel results.

23. In the May Report central projection, GDP was expected to increase by 0.1% in 2022 Q2, as the real income squeeze weighed on household spending and there were some adverse effects from the renewed disruption of supply chains. Covid-related government spending was also projected to decline further. The timing of the additional Platinum Jubilee Bank Holiday was expected to reduce growth temporarily by a ¼ percentage point, with an equivalent boost expected in 2022 Q3. As a result, excluding the temporary impact of the extra Bank Holiday, market-sector output was projected to grow in Q2, but at only about half of the pace expected in the first quarter.

24. The Committee discussed the risks around the near-term outlook for GDP. In the May Report central projections, real consumer spending was projected to rise only slightly in 2022 Q2 and during H2, while real household disposable income was expected to decline materially. That reflected a judgement that the household saving ratio would fall to around 5% in Q2 and to 3½% by the end of the year, around 1 percentage point below its 2019 average. There were downside risks to that consumption profile from reduced-form models and from a mechanical pre-Covid

mapping of recent consumer confidence declines to spending growth. Set against that, it was possible that the saving ratio could fall back even further in the near term, or remain lower for longer, than had been projected. Many respondents to the latest Bank/NMG household survey had stated that they would save less or use existing savings if faced with a hypothetical increase in inflation. And recent strength in business-to-business services, manufacturing and construction output could persist for longer than was assumed in the central projection, consistent to some extent with the relative strength in business survey indicators of output.

25. The Chancellor of the Exchequer had presented the Spring Statement to Parliament on 23 March. In addition to the measures in the Energy Bills Rebate package that had been announced in February, the Spring Statement had included an immediate twelve-month reduction in fuel duty. There had also been an announcement of an increase in the annual National Insurance Primary Threshold and the Lower Profits Limit from July 2022 to align with the income tax personal allowance, and a reduction in the basic rate of income tax from 20% to 19% from April 2024. Taken together, Bank staff estimated that these measures were likely to boost GDP by around ½% over coming years.

Supply, costs and prices

26. The Labour Force Survey (LFS) unemployment rate had fallen to 3.8% in the three months to February, consistent with an ongoing tightening in the labour market. The number of inactive people who reported wanting a job had also continued to be historically low. Inactivity had increased in aggregate and LFS employment had been broadly flat in recent months. In contrast, growth in HMRC employee payrolls and survey indicators of employment had remained strong.

27. The Committee discussed the risks to the outlook for labour market activity. The labour market had again been tighter than expected. The Bank’s Agents were reporting that firms’ employment intentions had remained robust, despite increased uncertainty around the broader economic outlook, but that the recent rate of hiring had been hindered by higher than usual staff turnover and recruitment difficulties. The number of vacancies had remained elevated, and survey measures of firms’ employment intentions and households’ sense of their own job security had also continued to be resilient. Nevertheless, the labour market had lagged activity around previous turning points in the economic cycle, and the prospective weakening in output was likely to weigh on labour demand in coming quarters. Consistent with this, in the May Monetary Policy Report forecast, the unemployment rate was projected to fall further in 2022 Q2, before stabilising in the second half of the year and increasing in 2023.

28. Whole-economy Average Weekly Earnings (AWE) growth had increased to 5.4% in the three months to February on a year earlier, more than 1 percentage point above the February Report forecast, reflecting strength in both regular pay and bonuses. Bank staff estimated that underlying private-sector regular pay growth had remained at around 4 to 4½%, once adjusting for the mechanical effects of changes in the composition of the workforce and the Coronavirus Job Retention Scheme. The median pay settlement recorded in the Bank staff's database had risen in the first few months of this year, broadly consistent with the Agents' February pay survey. More recently, some of the Agents' contacts had begun to consider further increases in pay settlements, or one-off bonuses, during the course of the year to retain staff, especially where there was strong demand for particular skills. Underlying pay growth was expected to increase over the remainder of the year, and by more than had been projected in the February Report, consistent with a tight labour market alongside rising inflation.

29. Twelve-month CPI inflation had risen to 7.0% in March, around 1 percentage point above the February Report forecast. The bulk of the upside news had been split evenly across energy and core goods prices. Taken together, energy and core goods components had also accounted for around four-fifths of the overshoot of CPI inflation relative to the 2% target, with the remainder spread across food and services components. Core goods inflation had been somewhat weaker in the euro area than in the United Kingdom and the United States.

30. CPI inflation was expected to rise to around 9% in April, and to increase further in subsequent months, averaging slightly over 10% at its peak in 2022 Q4.

31. The build up to and subsequent Russian invasion of Ukraine had pushed up commodity prices further. Household gas and electricity prices were due to contribute an additional 1½ percentage points to CPI inflation in April as the new energy price caps announced by Ofgem took effect. Further increases in wholesale prices, which had remained elevated even as spot prices had moderated, were likely to result in higher retail energy price caps when they were next reset in October. Around half of the six-month observation window for determining those price caps had now been completed. If sustained, higher gas and electricity futures prices would mean that the price caps could be around 40% higher, adding a further 1½ percentage points to CPI inflation from October. In addition, recent increases in wholesale oil and food commodity prices were being passed through to households.

32. Core CPI inflation, excluding food, beverages, tobacco and energy, was also expected to increase from its rate of 5.7% in March. Survey indicators of cost and price pressures had remained at historically elevated levels, and recent inflation outturns had tended to be above rates implied by their past relationships with those indicators. A

special survey on pricing and profit margins conducted by the Bank's Agents suggested that firms expected significantly more upwards pressure on prices over the next twelve months than the previous twelve months. Higher labour costs, utilities prices, and the costs of shipping and raw materials were frequently cited as factors pushing up on inflation over the next year. Around half of survey respondents considered that it was easier than normal to pass these cost increases through to prices. Close to 40% of companies had described their margins as unsustainably low at present, but three-fifths of those firms had anticipated rebuilding their margins to sustainable levels over the next twelve months.

33. Measures of businesses' inflation expectations had risen further since the MPC's previous meeting. Respondents to the Decision Maker Panel had increased their expectations for their own price increases over the next twelve months to 6.2% on average in April, and more than three quarters of those responding to the 2022 Q1 Deloitte CFO Survey had anticipated CPI inflation being above 2½% in two years' time. The Citi/YouGov household measures of expectations over the next year and next five-to-ten years had edged down in April, but had remained historically elevated. Professional forecasters had continued to expect inflation to be close to the 2% target in the medium term.

The immediate policy decision

34. The MPC sets monetary policy to meet the 2% inflation target, and in a way that helps to sustain growth and employment.

35. The Committee reviewed recent developments against the backdrop of its updated central projections for activity and inflation as set out in the accompanying May Monetary Policy Report. The projections were conditioned on a market-implied path for Bank Rate that rose to around 2½% by mid-2023, before falling to 2% at the end of the forecast period. Fiscal policy was assumed to evolve in line with announced Government policies. Wholesale energy prices were assumed to follow their respective futures curves for the first six months of the projections and remain constant beyond that, in contrast to futures curves, which were downward sloping over coming years. There were material risks around this assumption.

36. Global inflationary pressures had intensified sharply following Russia's invasion of Ukraine. This had led to a material deterioration in the outlook for world growth. Global GDP was expected to grow only slightly in 2022 Q2. Concerns about further supply chain disruption had risen, both due to Russia's invasion of Ukraine and to Covid-19 developments in China.

37. Market pricing was consistent with an increase in Bank Rate of 0.25 percentage points, to 1% at this MPC meeting, and market-implied expectations for the path of Bank Rate had risen further out. The Bank of England's Market Participants Survey indicated broadly similar expectations for Bank Rate in the near term, although respondents expected a much lower central path for Bank Rate than the market-implied path further ahead.

38. The Chancellor of the Exchequer had presented the Spring Statement to Parliament on 23 March. Taken together with the Energy Bills Rebate package that had been announced in February, Bank staff estimated that the Spring Statement measures were likely to boost GDP by around ½% over coming years.

39. UK GDP was estimated to have risen by 0.9% in 2022 Q1, stronger than had been expected in the February Report. That upward revision largely reflected higher-than-expected market-sector output.

40. The unemployment rate had fallen to 3.8% in the three months to February, and was likely to fall slightly further in coming months, consistent with a continuing tightening in the labour market and with a margin of excess demand at present. Inactivity had increased, however, and LFS employment had been broadly flat in recent months. In contrast, growth in HMRC employee payrolls and survey indicators of employment had remained strong. Firms had continued to report significant recruitment difficulties and elevated levels of vacancies, and most surveys suggested above-average levels of capacity utilisation.

41. Surveys of business activity had generally remained strong. There had, however, been signs from indicators of retail spending and consumer confidence that the squeeze on real disposable incomes was starting to weigh on the household sector. The level of GDP was expected to be broadly unchanged in 2022 Q2. The timing of the additional Platinum Jubilee Bank Holiday was expected to reduce growth temporarily by a ¼ percentage point, with an equivalent boost expected in Q3. Excluding the temporary impact of the extra Bank Holiday, market-sector output was projected to grow in Q2, but at only about half of the pace expected in the first quarter.

42. In the May Report central projection, UK GDP growth was expected to slow sharply over the first half of the forecast period. That predominantly reflected the significant adverse impact of the sharp rises in global energy and tradable goods prices on most UK households' real incomes and many UK companies' profit margins. Total real household disposable income was projected to fall by 1¾% in 2022, which was a greater fall than in the February projection. Four-quarter consumption growth was expected to slow materially over the first half of the forecast period. However, it was expected to slow by much less than income growth and was positive throughout the

projection. The outlook for aggregate consumption would depend on a range of factors including the distribution of the squeeze on incomes across households, and the extent to which they were willing and able to draw on accumulated savings. Overall, four-quarter GDP growth was expected to be broadly flat in 2023.

43. Although the unemployment rate was likely to fall slightly further in the near term, it was expected to rise to 5½% in three years' time given the sharp slowdown in demand growth. The Committee had also revised down its projection for labour force participation following the fall during the pandemic. In the May Report central projection, excess supply in the economy was expected to build to 2¼% by the end of the forecast period.

44. Twelve-month CPI inflation had risen to 7.0% in March, around 1 percentage point higher than had been expected in the February Report. The strength of inflation relative to the MPC's 2% target mainly reflected previous large increases in global energy and tradable goods prices, the latter of which was due to the shift in global demand towards durable goods and to supply chain disruptions. There had also been some increase in the inflation rates of more domestically supplied services.

45. In the May Report central projection, CPI inflation was expected to rise further over the remainder of the year, to just over 9% in 2022 Q2 and averaging slightly over 10% at its peak in 2022 Q4. The majority of that further increase reflected higher household energy prices following the large rise in the Ofgem price cap in April and projected additional large increase in October. The price cap mechanism meant that it took some time for increases in wholesale gas and electricity prices, and their respective futures curves, to be reflected in retail energy prices. Given the operation of the price cap, consumer price inflation was likely to peak later in the United Kingdom than in many other economies, and might therefore fall back later. The expected rise in CPI inflation also reflected higher food, core goods and services prices.

46. The Bank staff's measure of underlying nominal earnings growth had risen by more than had been projected in the February Report and was expected to strengthen in coming months, given the further tightening of the labour market and some upward pressure from higher price inflation. The median pay settlement recorded in the Bank staff's database had risen, broadly consistent with the Agents' February pay survey. More recently, some of the Agents' contacts had begun to consider further increases in pay settlements, or one-off bonuses, during the course of the year. Companies generally expected to increase their selling prices strongly in the near term, following the sharp rises in their costs, with many reporting confidence that they would be able to rebuild at least some of their margins.

47. Since the MPC's previous meeting, UK short-term financial market inflation compensation measures had continued to increase, as had measures of businesses' short to medium-term inflation expectations. Longer-term inflation expectations implied by financial markets and in household surveys had fallen modestly but remained elevated by historic norms. There had been limited news in indicators of professional forecasters' expectations. The Committee would continue to monitor measures of inflation expectations very closely.

48. With monetary policy acting to ensure that longer-term inflation expectations were anchored at the 2% target, upward pressure on CPI inflation was expected to dissipate over time. Global commodity prices were assumed to rise no further in the central projection, global bottlenecks were expected to ease over time, and the weakening in demand growth and building excess supply led domestic inflationary pressures to subside.

49. Conditioned on the rising market-implied path for Bank Rate and the MPC's current forecasting convention for future energy prices, CPI inflation was projected to fall to a little above the 2% target in two years' time, largely reflecting the waning influence of external factors, and to 1.3% in three years, well below the target and mainly reflecting weaker domestic pressures. The risks to the inflation projection were judged to be skewed to the upside at these points, given the risks of more persistent strength in nominal wage growth and domestic price setting than had been assumed. In projections conditioned on the alternative assumption of constant interest rates at 1%, CPI inflation was expected to be 2.9% and 2.2% in two and three years' time respectively.

50. There were downside risks to the assumed paths for energy and other commodity prices if prices fell back to the levels implied by futures curves. In the case of energy prices, the level of GDP would be nearly 1% higher by the end of the forecast period and excess supply and unemployment around ¾ percentage points lower than the central forecast in the May Report. CPI inflation would fall back towards the target more rapidly than in the central projection and would be around ½ and over 1 percentage points below the target in two and three years' time respectively.

51. The Committee turned to its immediate policy decision.

52. The MPC's remit was clear that the inflation target applied at all times, reflecting the primacy of price stability in the UK monetary policy framework. The framework also recognised that there would be occasions when inflation would depart from the target as a result of shocks and disturbances. The economy had recently been subject to a succession of very large shocks. Russia's invasion of Ukraine was another such shock. In particular, should recent movements prove persistent as the central projections

assumed, the very elevated levels of global energy and tradable goods prices, of which the United Kingdom was a net importer, would necessarily weigh further on most UK households' real incomes and many UK companies' profit margins. This was something monetary policy was unable to prevent. The role of monetary policy was to ensure that, as this real economic adjustment occurred, it did so in a manner consistent with achieving the 2% inflation target sustainably in the medium term, while minimising undesirable volatility in output.

53. Recent developments had exacerbated materially both the near-term peak in CPI inflation, and the prospective negative impact on activity and medium-term inflationary pressures. Nevertheless, given the current tightness of the labour market, continuing signs of robust domestic cost and price pressures, and the risk that those pressures would persist, all members of the Committee judged that an increase in Bank Rate was warranted at this meeting.

54. Different members placed different weights on the arguments for whether to increase Bank Rate at this meeting and if so by 0.25 or 0.5 percentage points. Momentum in labour market activity had continued to be both strong and stronger than had been expected. Strength in the labour market had so far been accompanied by a notable resilience in business relative to consumer confidence. While there were signs of weakness in household spending now that the real income squeeze was beginning to bite, the stronger than forecast domestic inflationary pressures since the February Report justified a further increase in Bank Rate. Underlying wage growth had continued to strengthen and, at a time of already high headline inflation, there was the potential for some further second-round effects in domestic wage and price setting. A key question was whether some self-sustaining momentum in domestically generated inflation would remain even as slack in the economy was expected to open up. The greater the delay between the real income squeeze leading to weakness in aggregate demand and to a turn-around in the labour market, the more risk there was that higher inflation expectations would become embedded in the economy.

55. Six members of the Committee judged that a further 0.25 percentage point increase in Bank Rate to 1% was warranted at this meeting. The May Report projections implied that some tightening in monetary policy was required to bring inflation back to the 2% target sustainably in the medium term. But, conditioned on the market path for Bank Rate, the endpoint of the forecast was characterised by a large margin of excess supply and CPI inflation well below target, although the medium-term outlook was particularly uncertain currently.

56. Three members preferred a 0.5 percentage point increase in Bank Rate at this meeting. These members put more weight on continued strength in demand, yielding risks that capacity pressures, especially in the labour market, would be greater over the

forecast period than in the May Report projections. These members also judged that monetary policy should lean strongly against risks that recent trends in pay growth, firms' pricing strategies and inflation expectations in the economy more widely would become more firmly embedded. Faster policy tightening now would help to bring inflation back to the target sustainably in the medium term, and reduce risks of a more extended and costly tightening cycle later.

57. Based on their updated assessment of the economic outlook, most members of the Committee judged that some degree of further tightening in monetary policy might still be appropriate in the coming months. There were risks on both sides of that judgement and a range of views among these members on the balance of risks.

58. Some members of the Committee judged that the risks around activity and inflation over the policy horizon were more evenly balanced and that such guidance was not appropriate at this juncture.

59. The MPC would continue to review developments in the light of incoming data and their implications for medium-term inflation.

60. At its February 2022 meeting, consistent with the guidance set out in the August 2021 Report, and given that financial markets were functioning normally, the Committee had agreed to cease to reinvest any future maturities falling due from its stock of UK government bond purchases. This had reflected the MPC's intention to reduce its holdings of government bonds in a gradual and predictable manner. The MPC had also reaffirmed that it would consider beginning the process of selling UK government bonds only once Bank Rate had risen to at least 1%, and depending on economic circumstances at the time.

61. At this MPC meeting, the Committee reaffirmed its preference in most circumstances to use Bank Rate as its active policy tool when adjusting the stance of monetary policy. As Bank Rate was now being increased to 1%, and consistent with the MPC's previous guidance, the Committee would consider beginning the process of selling UK government bonds held in the Asset Purchase Facility. The Committee reaffirmed that the decision to commence sales would depend on economic circumstances including market conditions at the time, and that sales would be expected to be conducted in a gradual and predictable manner so as not to disrupt the functioning of financial markets. The Committee recognised the benefits of providing market participants with clarity on the framework for any potential sales programme. The Committee had therefore asked Bank staff to work on a strategy for UK government bond sales, and would provide an update at its August meeting. This would allow the Committee to make a decision at a subsequent meeting on whether to commence sales.

62. The Chair invited the Committee to vote on the proposition that:

> Bank Rate should be increased by 0.25 percentage points, to 1%.

63. Six members (Andrew Bailey, Ben Broadbent, Jon Cunliffe, Huw Pill, Dave Ramsden and Silvana Tenreyro) voted in favour of the proposition. Three members (Jonathan Haskel, Catherine L Mann and Michael Saunders) voted against the proposition, preferring to increase Bank Rate by 0.5 percentage points, to 1.25%.

Operational considerations

64. As of 4 May 2022, the total stock of assets held in the Asset Purchase Facility (APF) was £867 billion, comprising £847 billion of UK government bond purchases and £19.6 billion of sterling non-financial investment-grade corporate bond purchases.

65. At the February 2022 MPC meeting, the Committee had agreed that the Bank of England should cease to reinvest any maturities falling due from its stock of sterling non-financial investment-grade corporate bond purchases, and that it should initiate a programme of corporate bond sales to be completed no earlier than towards the end of 2023 that should unwind fully the stock of corporate bond purchases. The Committee had also asked Bank staff to design a programme of corporate bond sales, designed so as not to disrupt the functioning of the sterling investment-grade corporate bond market.

66. Consistent with that previous guidance, the Committee had been briefed at this MPC meeting on the Bank of England's plans to commence corporate bond sales in September 2022, and for any corporate bonds held in the portfolio maturing on or before 5 April 2024 to be allowed to mature. Further details were being provided in the high-level Market Notice accompanying these minutes, with a full operational Market Notice to be published at least a month prior to the start of the sales programme. The publication of further information on this programme of corporate bond sales should not be taken as a signal regarding the design or timing of any potential future UK government bond sales programme.

67. As had been agreed in the exchange of letters between the Governor and the Chancellor of the Exchequer in February 2022, as the size of APF holdings declined, the authorised maximum size of the APF should be adjusted to reflect the size of the portfolio every six months. In line with that earlier agreement, and as set out in a further exchange of letters that would be released alongside these minutes, the authorised maximum size of the APF could now be reduced to align with the size of the current holdings. This would be reviewed and confirmed between the Governor and Chancellor again in October.

68. As noted in the Governor's letter to the Chancellor in February 2022, were gilt sales judged to be appropriate in the future, these would be conducted in a predictable manner over a period of time so as not to disrupt the functioning of financial markets. The Bank would liaise with the UK Debt Management Office (DMO) in order to minimise interference with the DMO's own issuance programme and would consider the views of market participants as to how best to minimise disruption in asset markets.

69. The following members of the Committee were present:

Andrew Bailey, Chair
Ben Broadbent
Jon Cunliffe
Jonathan Haskel
Catherine L Mann
Huw Pill
Dave Ramsden
Michael Saunders
Silvana Tenreyro

James Benford was present as the Treasury representative on 27 April and Clare Lombardelli was present as the Treasury representative on 29 April and 4 May.

70. As permitted under the Bank of England Act 1998, as amended by the Bank of England and Financial Services Act 2016, Dido Harding was also present on 27 April and 29 April, as an observer for the purpose of exercising oversight functions in her role as a member of the Bank's Court of Directors.