MPC MEMBERS

COPIES OF THE OCTOBER 2015 PRE-MPC MEETING(S) PRESENTATIONS

In advance of the MPC meeting, please find attached copies of all presentations given at the October 2015 Pre-MPC briefing meeting(s).

This includes the Demand & Output "Blue Book 2015" presented separately on the afternoon of the October Pre-MPC meeting (30th September).

Monetary Policy COO Division (TS-G)
30th September 2015

1: Financial Markets

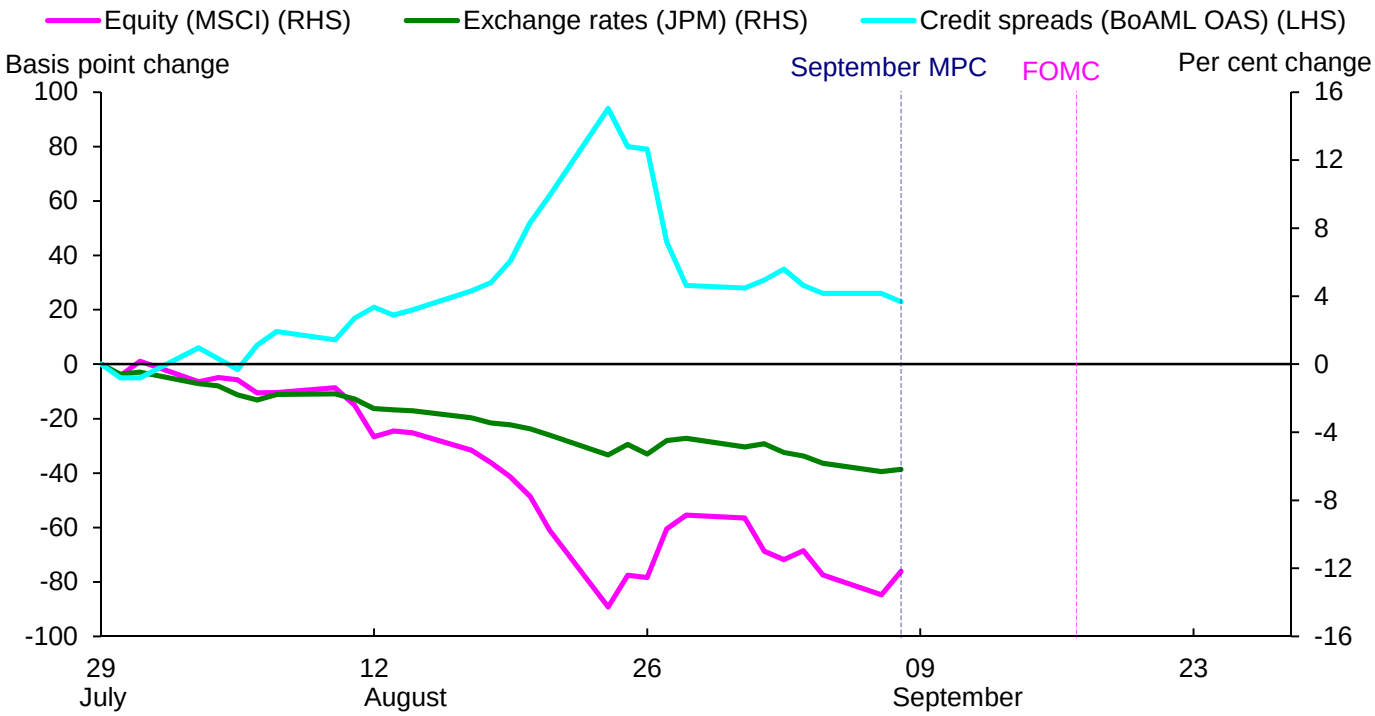
Financial Markets

October 2015 Pre-MPC
FED, MFAD & SMD

Plan

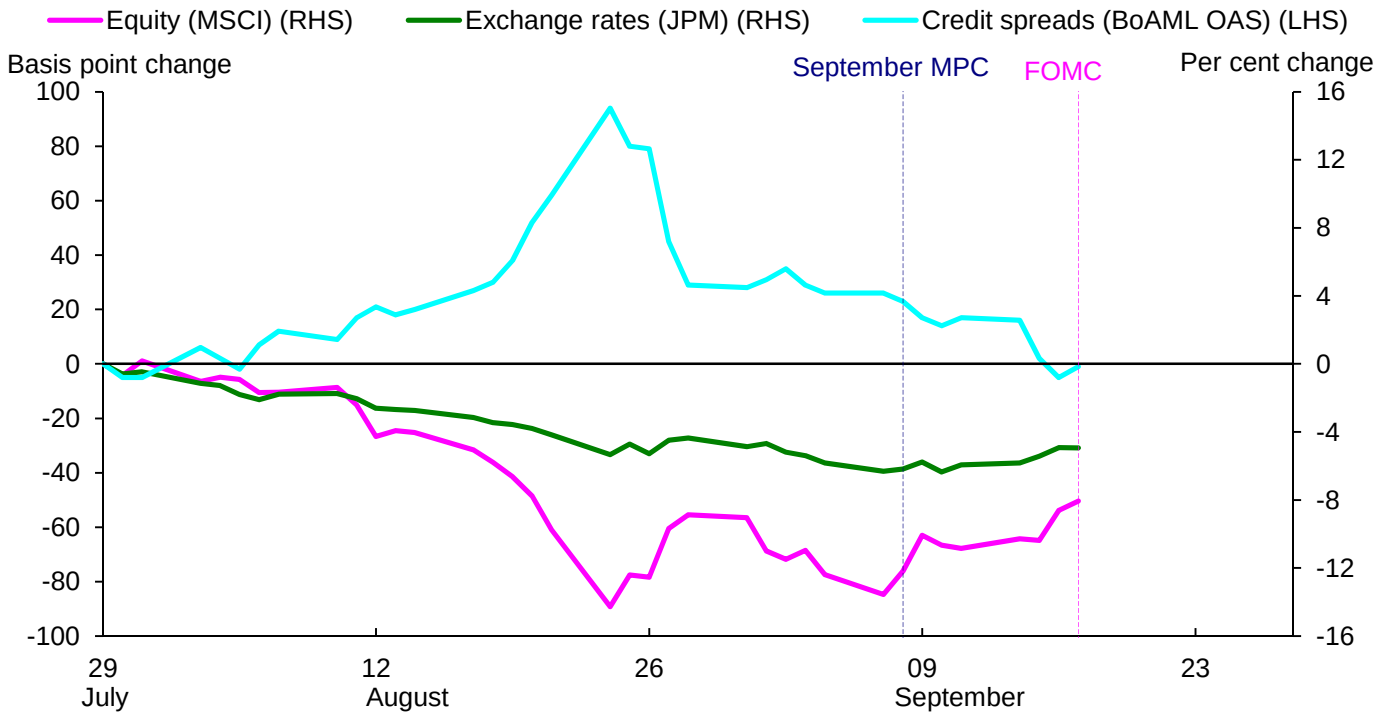
- Update since September MPC
  - Emerging markets
  - FOMC market response
  - UK interest rates
  - Sterling
  - Other central banks
- Equity markets
  - Decomposing moves in the FTSE
  - Chinese economic outlook

Emerging market asset price moves since August IR cut-off



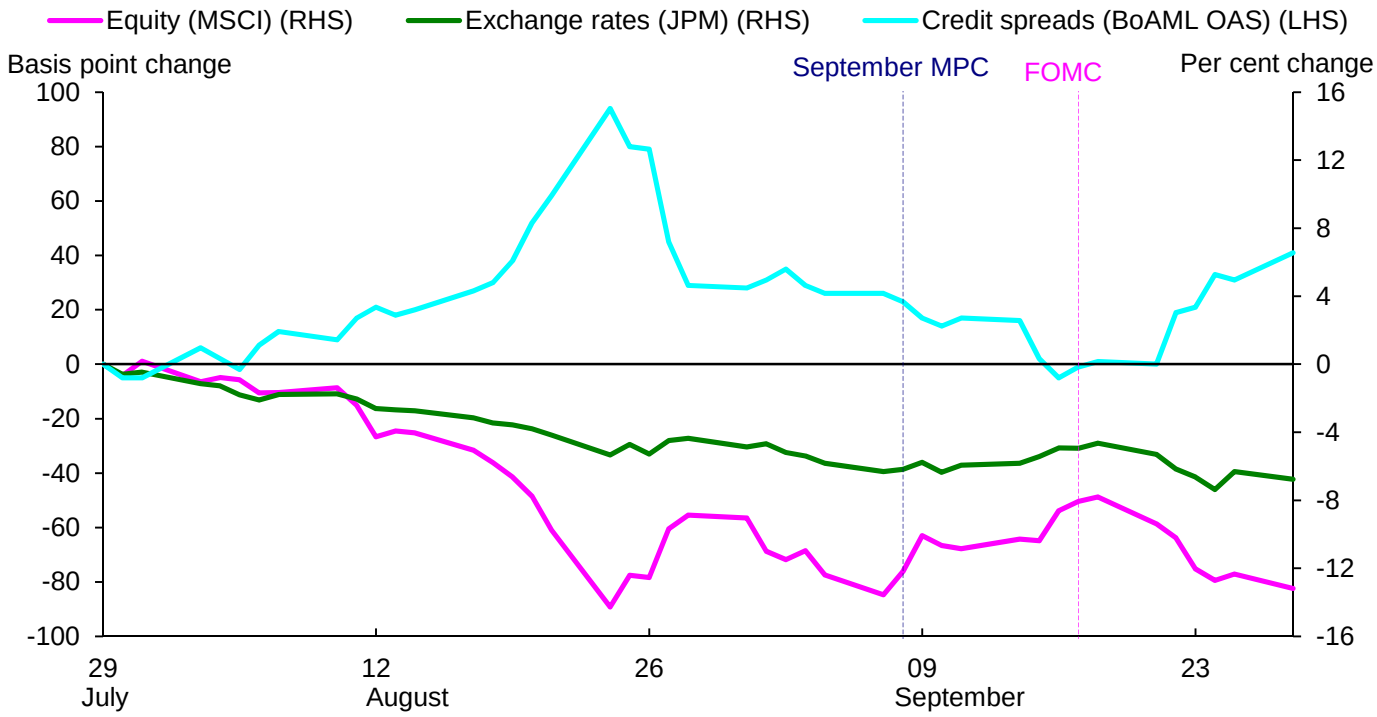
- During August, fears about the outlook for China and other EMEs unsettled financial markets.

Emerging market asset price moves since August IR cut-off



- In September, initially these markets recovered a little…

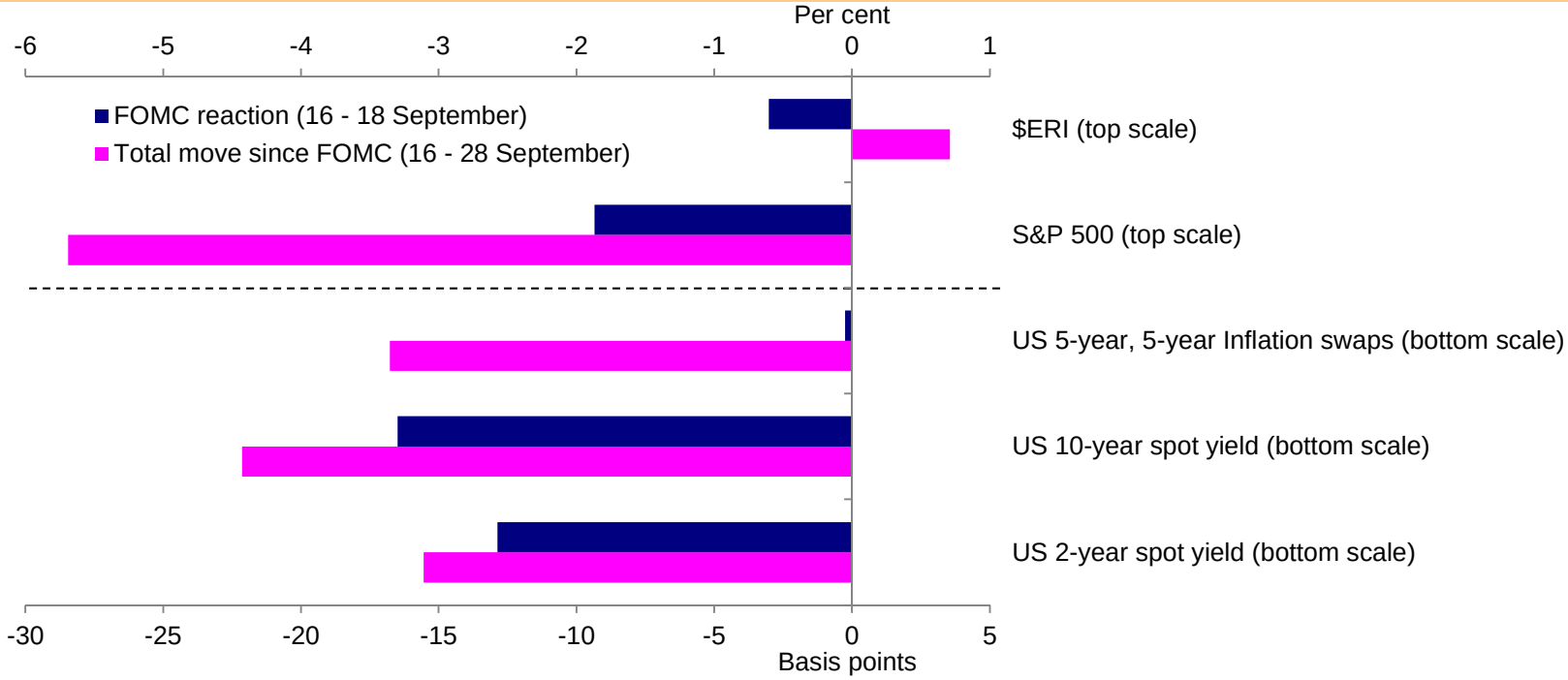
Emerging market asset price moves since August IR cut-off



- … but deteriorated again after the FOMC meeting.

FOMC market response

Asset price moves since September FOMC

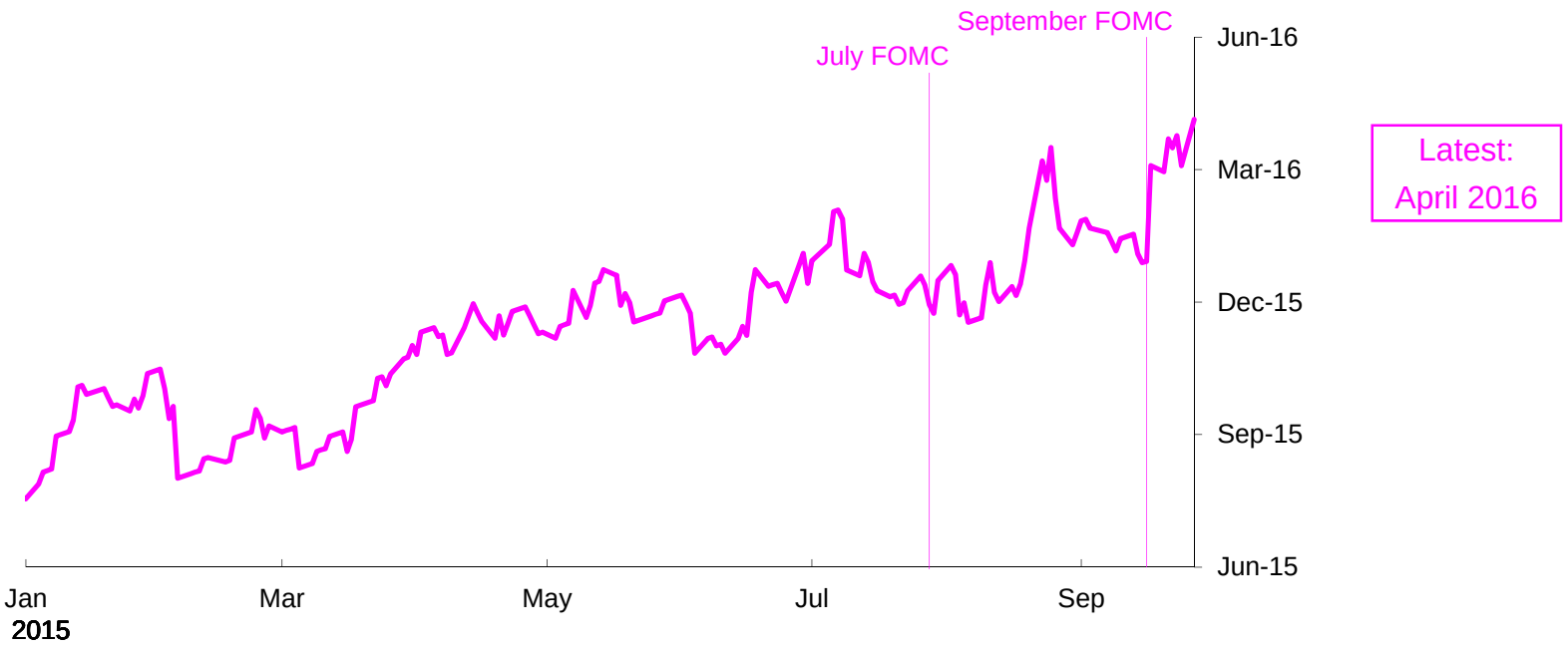


- Yields fell after the FOMC did not hike . . . but so did equities and later inflation swap rates.

Chair Yellen's FOMC Press Conference

"The outlook abroad appears to have become more uncertain of late, and heightened concerns about growth in China and other emerging market economies have led to notable volatility in financial markets."

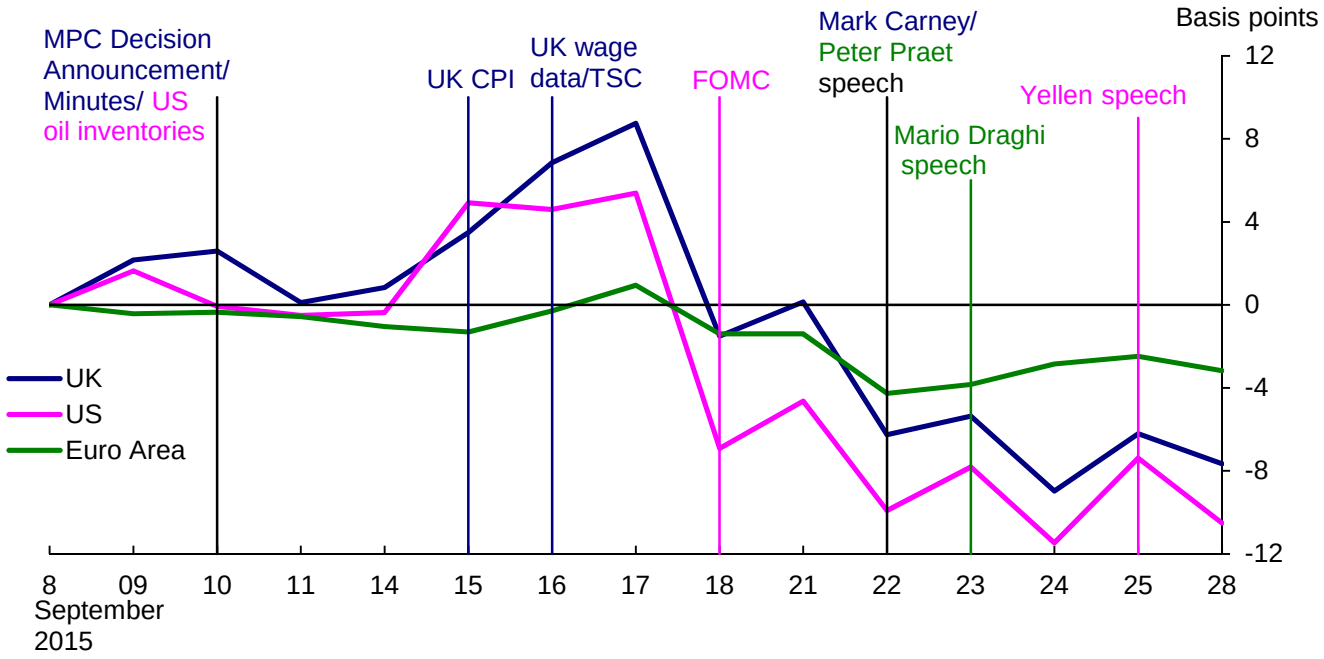
Date at which the US OIS forward curve reaches 0.35%



- The OIS forward curve now reaches 35bp in April 2016.

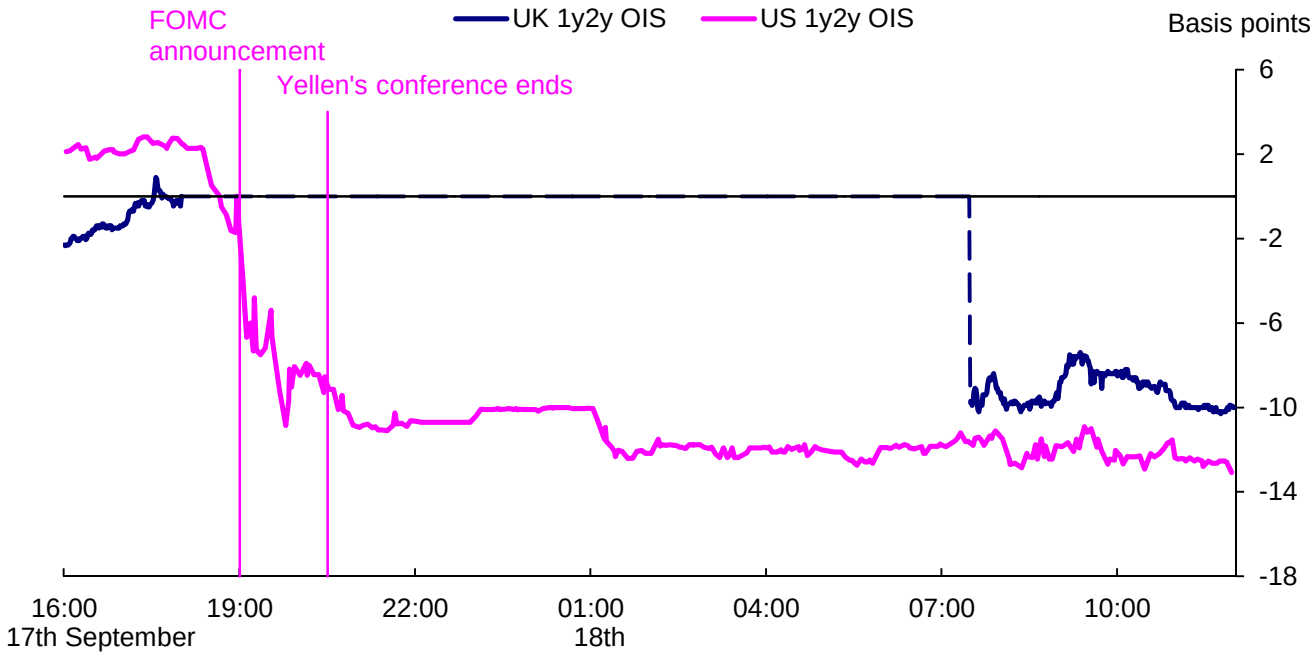
UK interest rates

Cumulative changes in 1-year instantaneous forward OIS rates



- Sterling OIS rates rose on labour market data but then fell following FOMC.

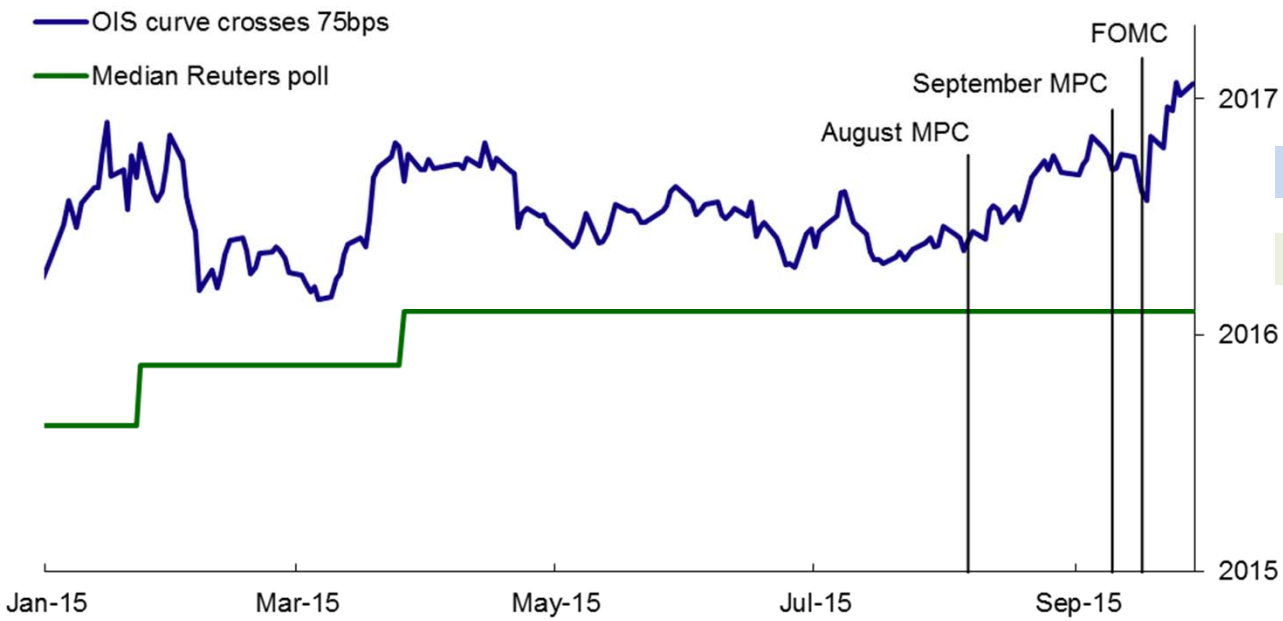
17 and 18 September: Reaction to FOMC (1y2y OIS)



Source: Bloomberg Benchmark Bonds

- UK rates followed the fall in US rates after the FOMC.

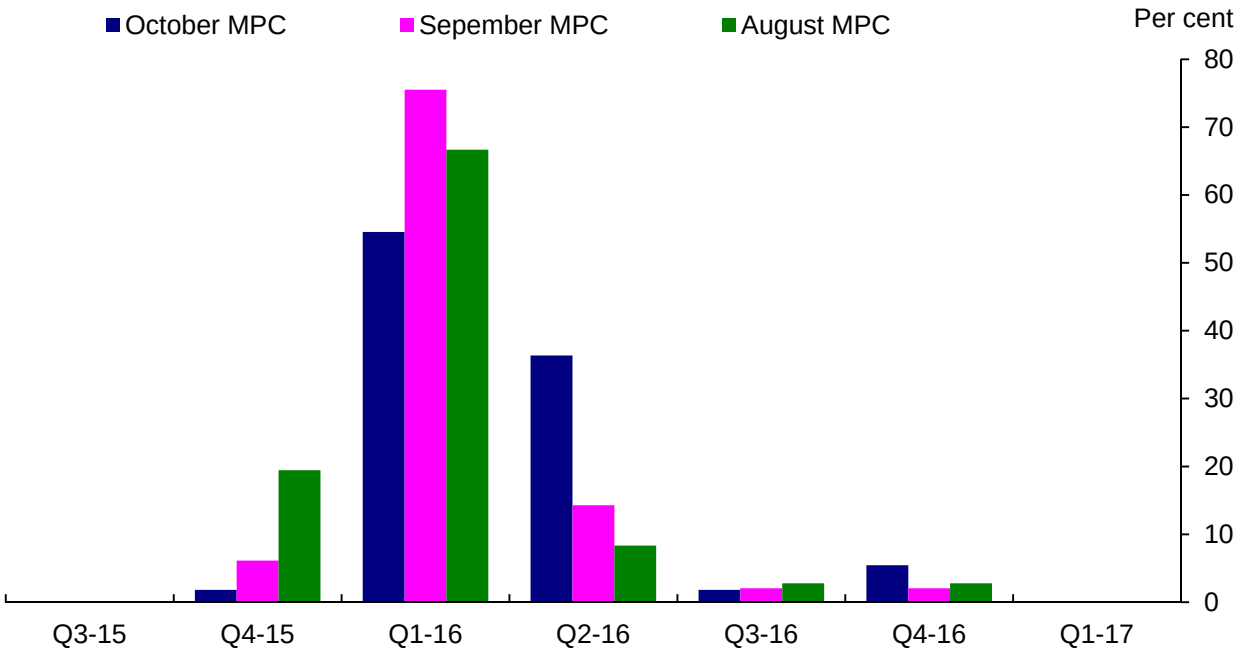
Date which UK OIS rate reaches 0.75% and Reuters poll



	Latest	Last MPC
OIS curve crosses 75bps	Jan 2017	Oct 2016
Median Reuters poll	Q1 2016	Q1 2016

- The date the OIS curve crosses 0.75% has moved back to January 2017 from May 2016 at the IR cut-off; the 3-year point on the instantaneous forward OIS curve has fallen 40bp since then.

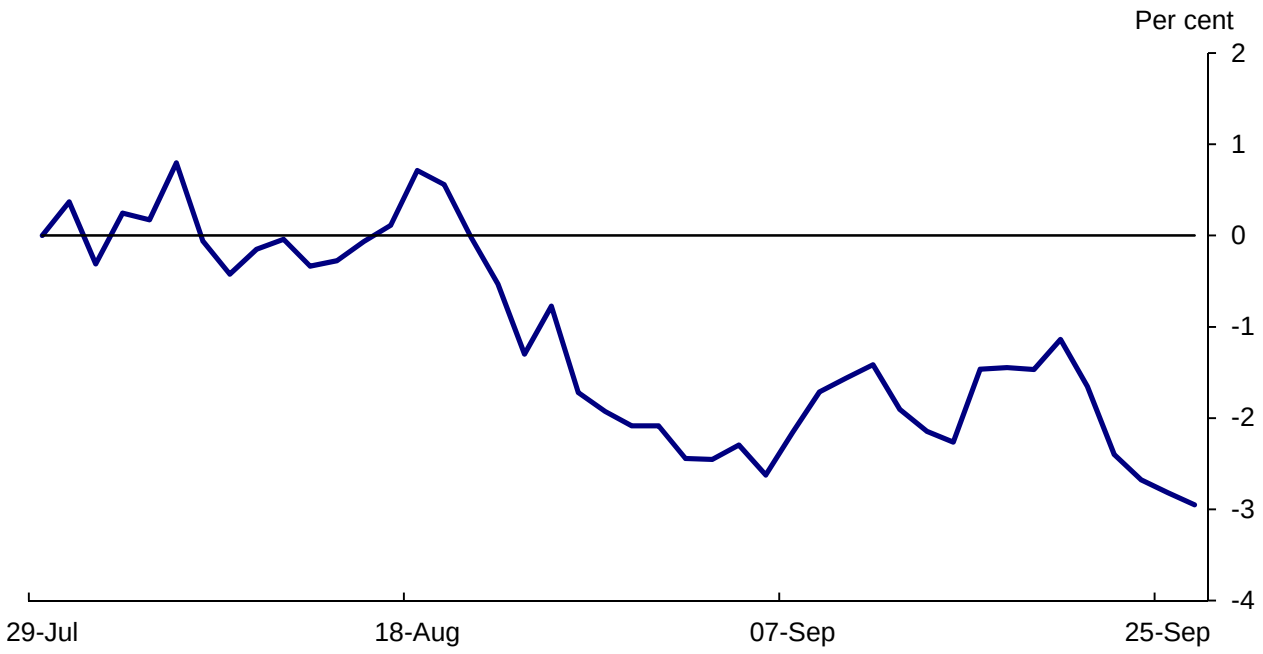
Reuters poll: timing of the first rise in Bank Rate



- Median of economists still expects Q1 2016, but a large minority have moved to Q2.

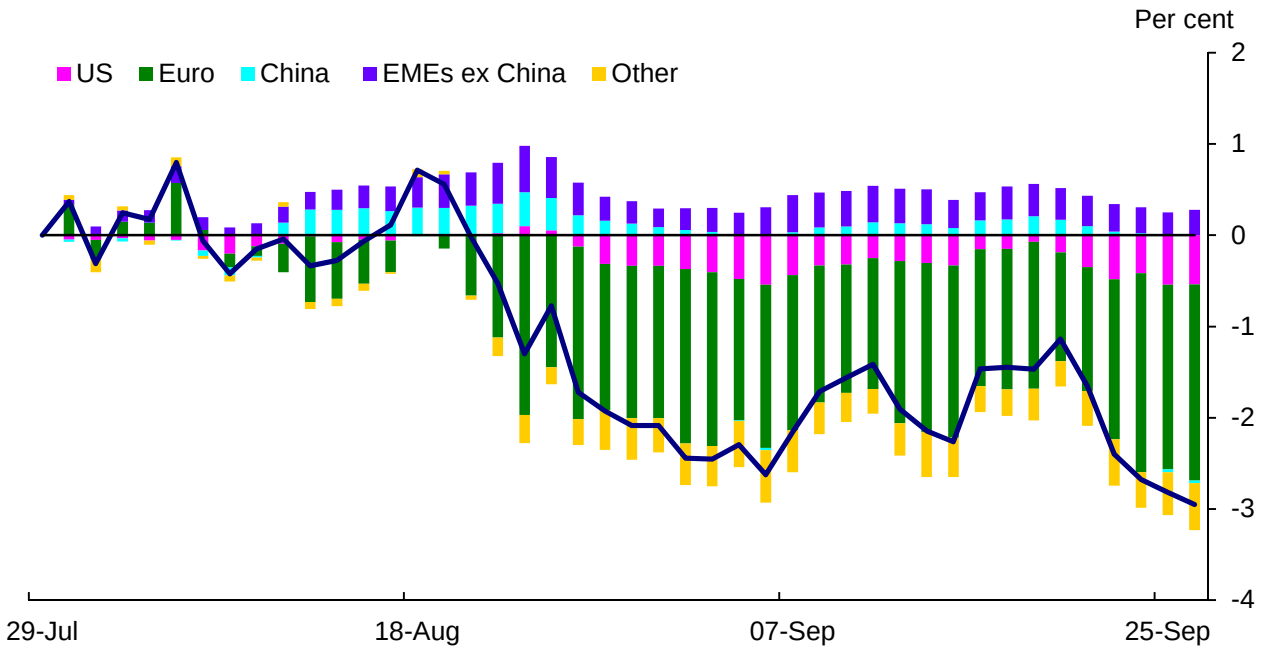
Sterling

Cumulative change in sterling ERI since August IR cut-off



- Since the August IR cut-off, sterling has fallen by 3% (by 2.5% relative to the 15-day average).

Cumulative change in sterling ERI since August IR cut-off



- Sterling has fallen mainly against the euro, offset a little by emerging market currencies.

Other central banks

Other central banks

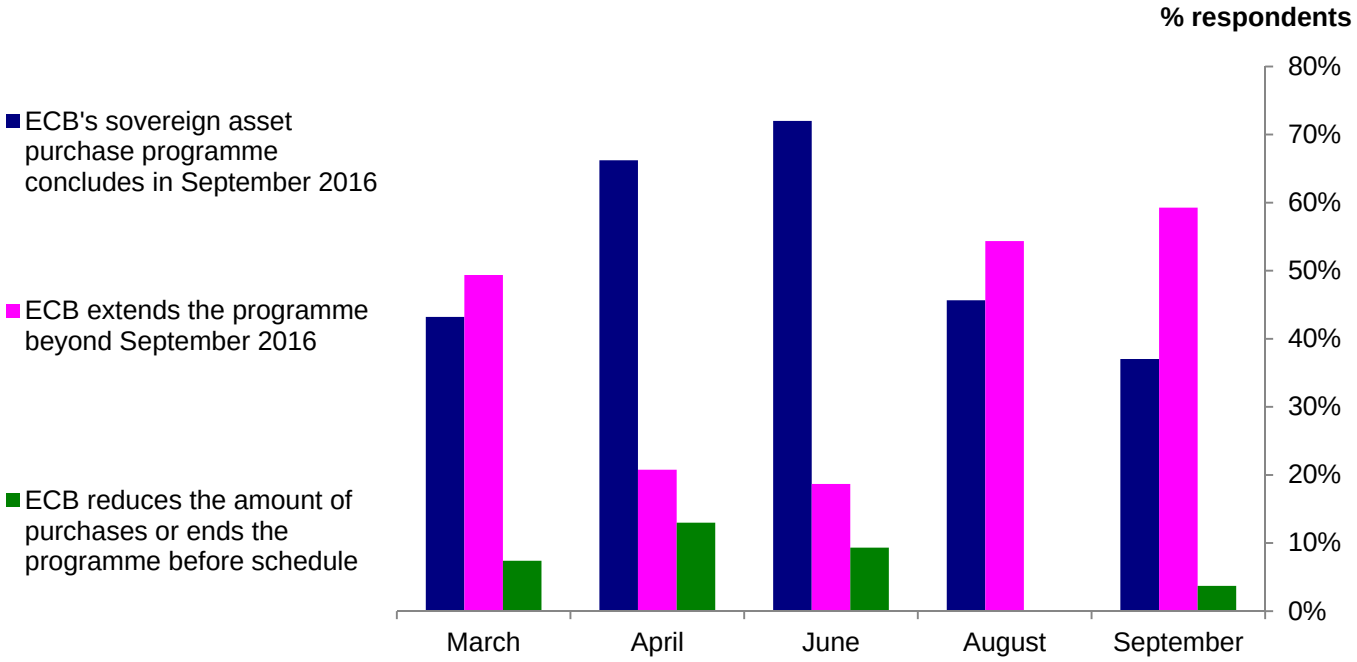
have cut rates…

• Norway	-25 bp	**citing oil prices**
• Hungary	-25 bp	to discourage use of deposit facility
• India	-50 bp	**citing global growth**
• Taiwan	-12.5 bp	**citing growth slowdown**
• Ukraine	-500 bp	after debt restructuring

and

BoJ: increase in expectations of further loosening of monetary policy.

Reuters poll: ECB QE expectations



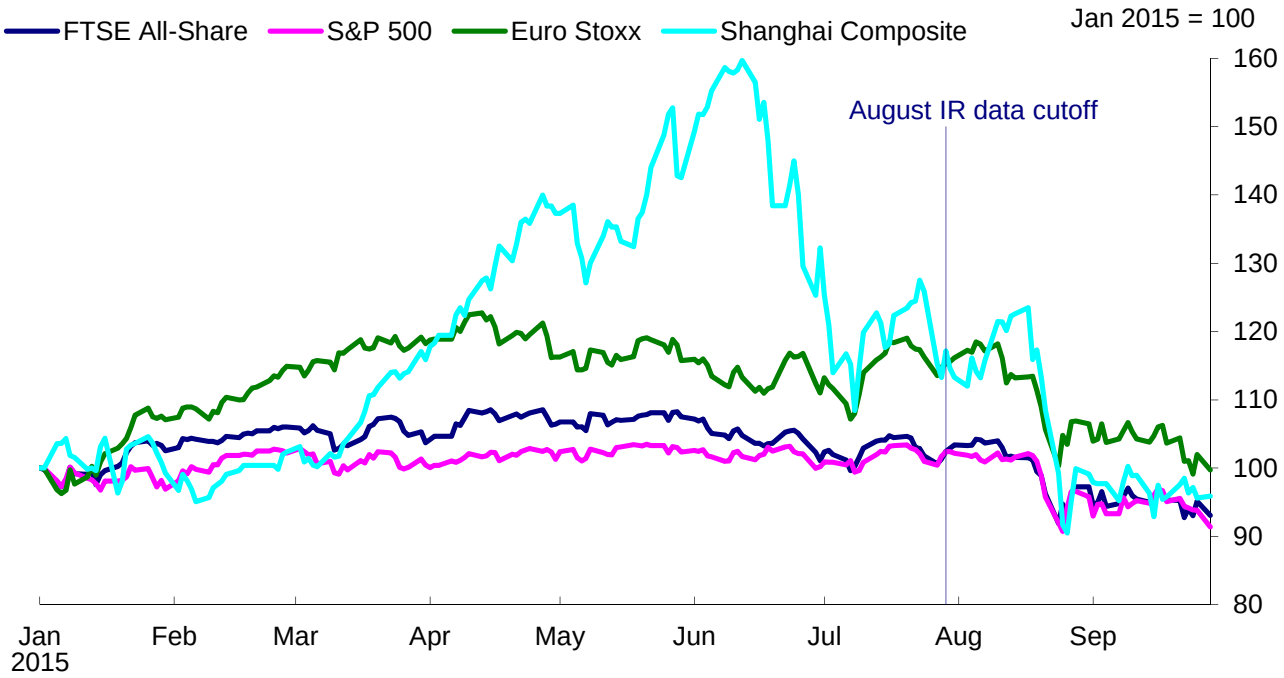
- Expectations that the ECB will extend QE.

Summary

- Renewed concern about emerging market economies, heightened by the FOMC.
- UK rates rose on labour market data but then fell following FOMC.
- Sterling down on the month, weakness against euro offset a little by strength against EME currencies.

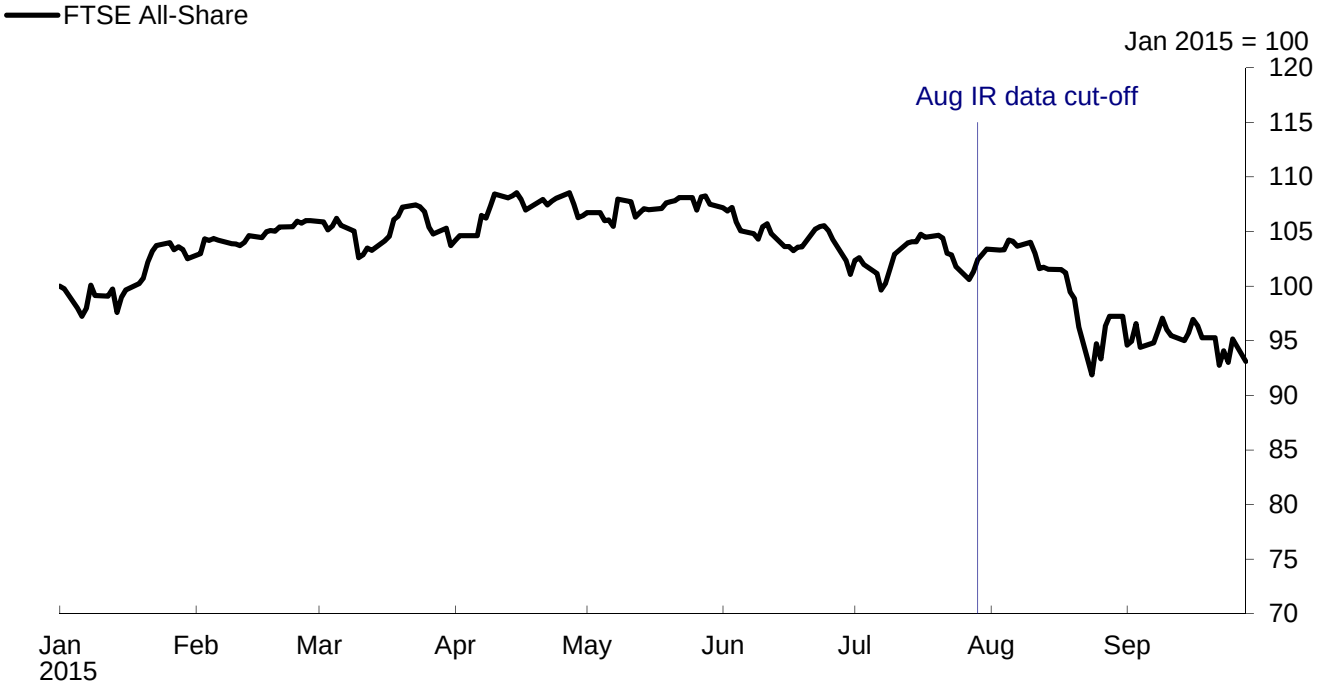
Equities

Benchmark equity indices

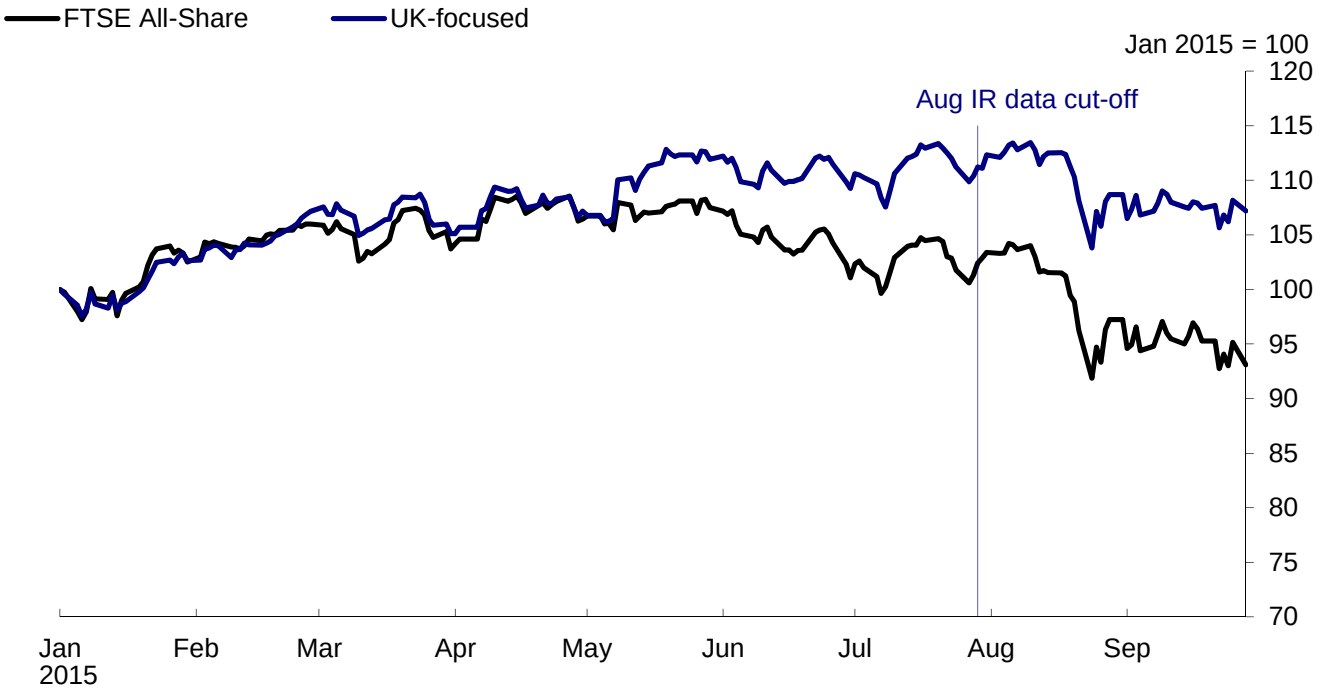


- August volatility in advanced economy equity markets was associated with sharp falls in Chinese equity prices.

Geographically focused components of the FTSE All-Share

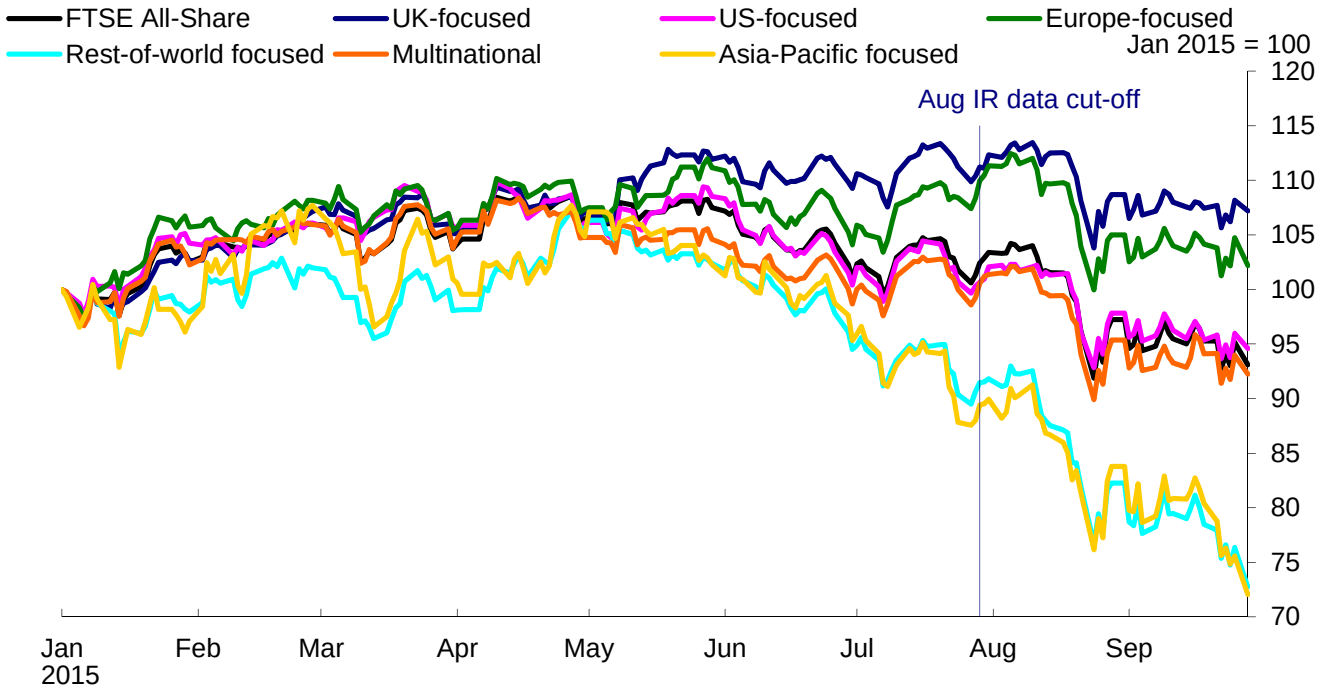


Geographically focused components of the FTSE All-Share



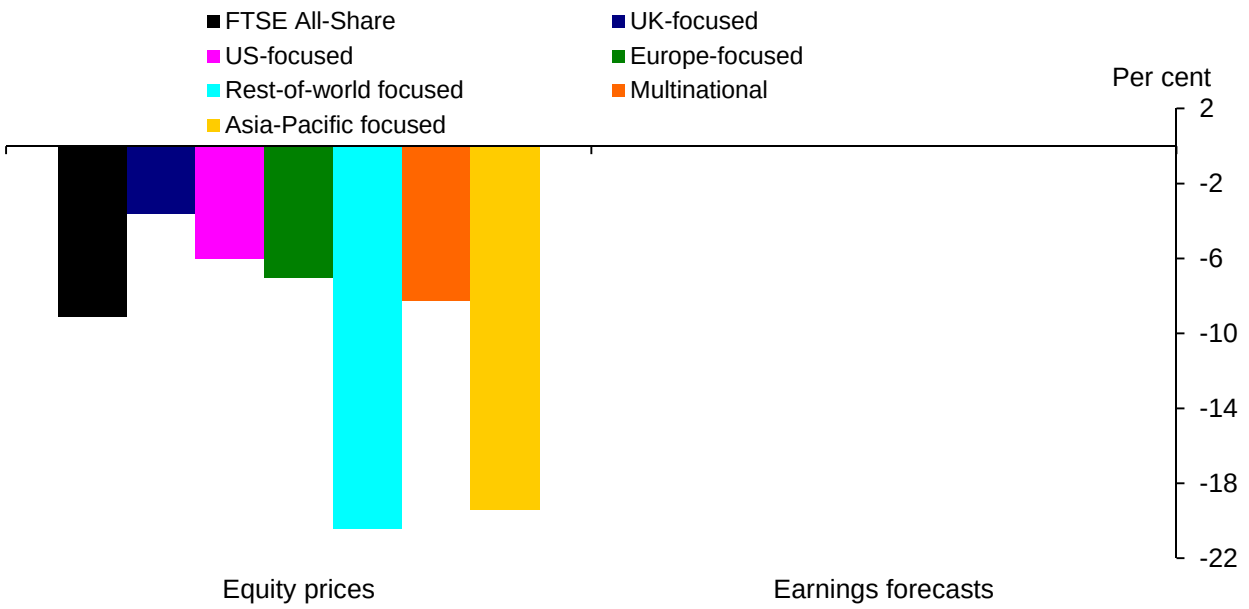
- UK domestically focussed index has outperformed FTSE All-Share

Geographically focused components of the FTSE All-Share



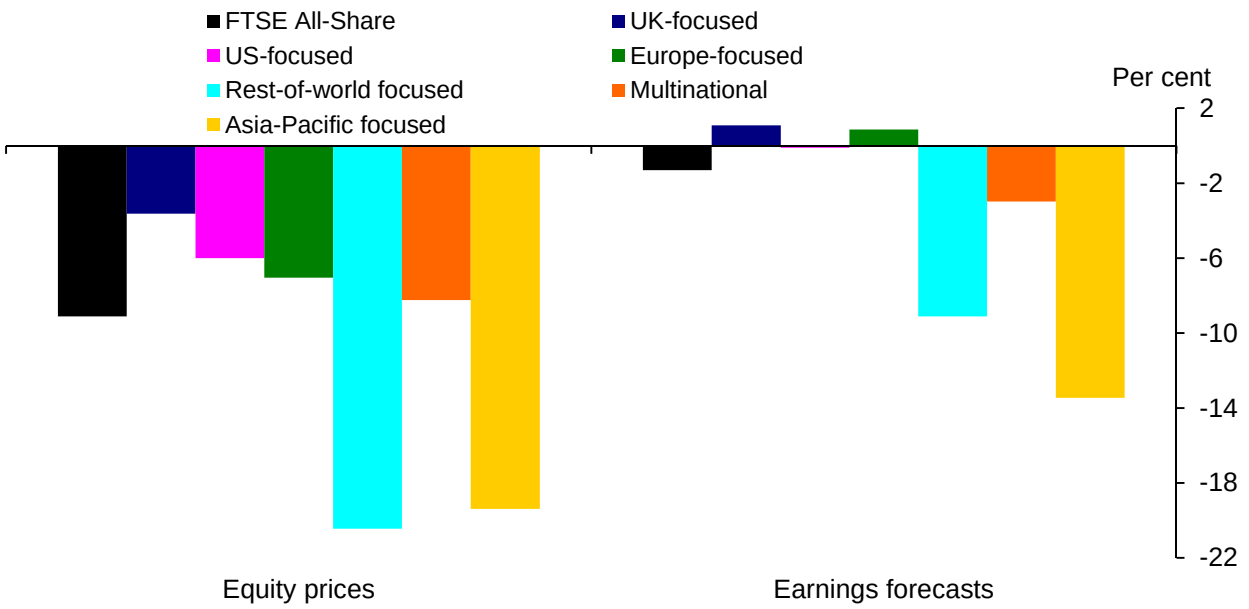
- FTSE All-Share has been dragged down by the weakness of companies generating their revenues elsewhere, in particular the rest-of-world component.

Changes in equity prices and earnings forecasts for FTSE components since August IR



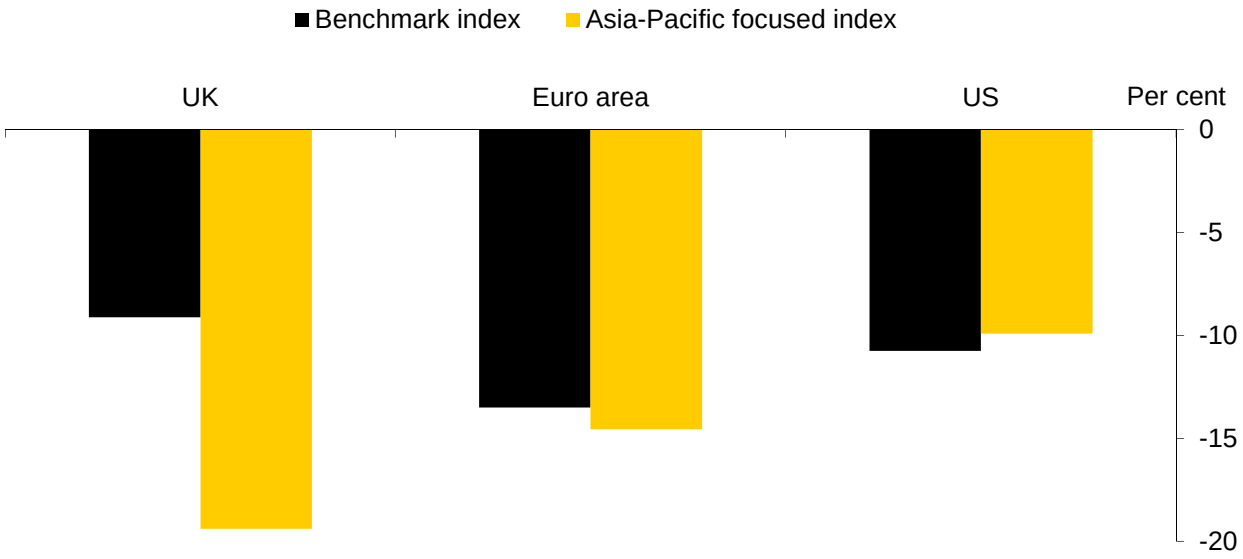
- Companies exposed to the UK – and other advanced economies – have fallen by less than firms exposed to other parts of the world.

Changes in equity prices and earnings forecasts for FTSE components since August IR



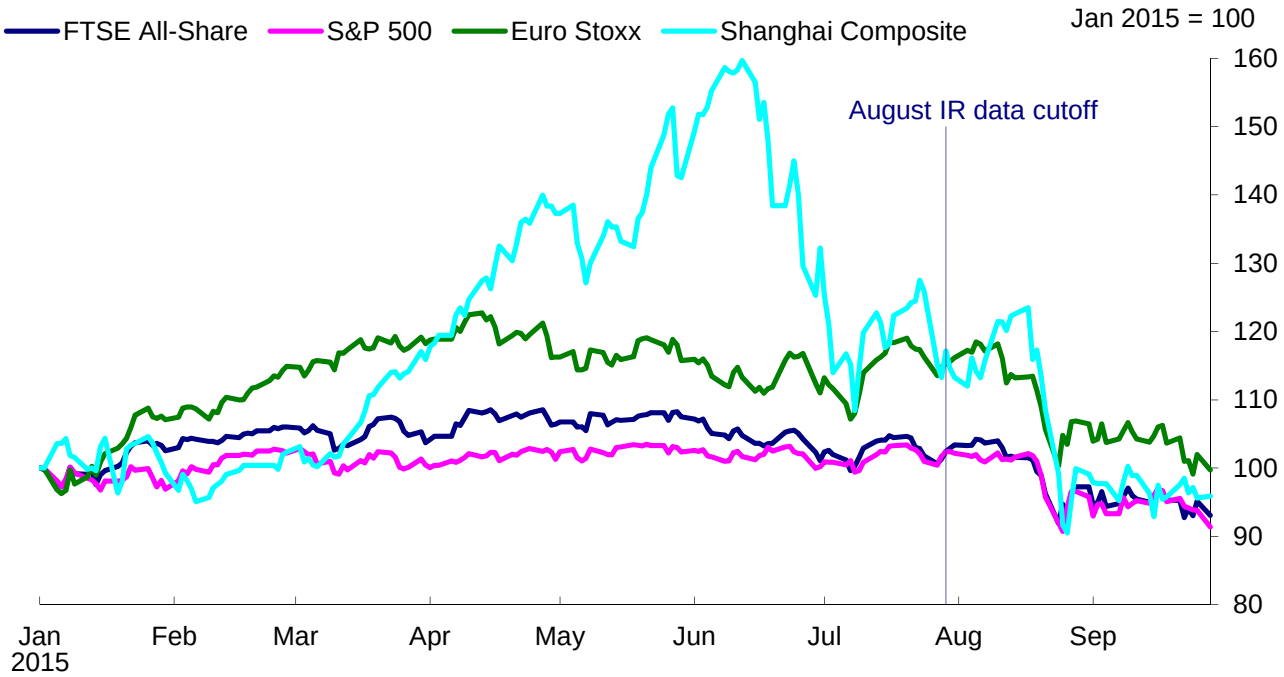
- Earnings forecasts for firms exposed primarily to the UK and other advanced economies are unchanged, or even revised up slightly. But earnings forecasts revised down for firms generating their revenues elsewhere.

Changes in advanced-economy equity indices since August IR



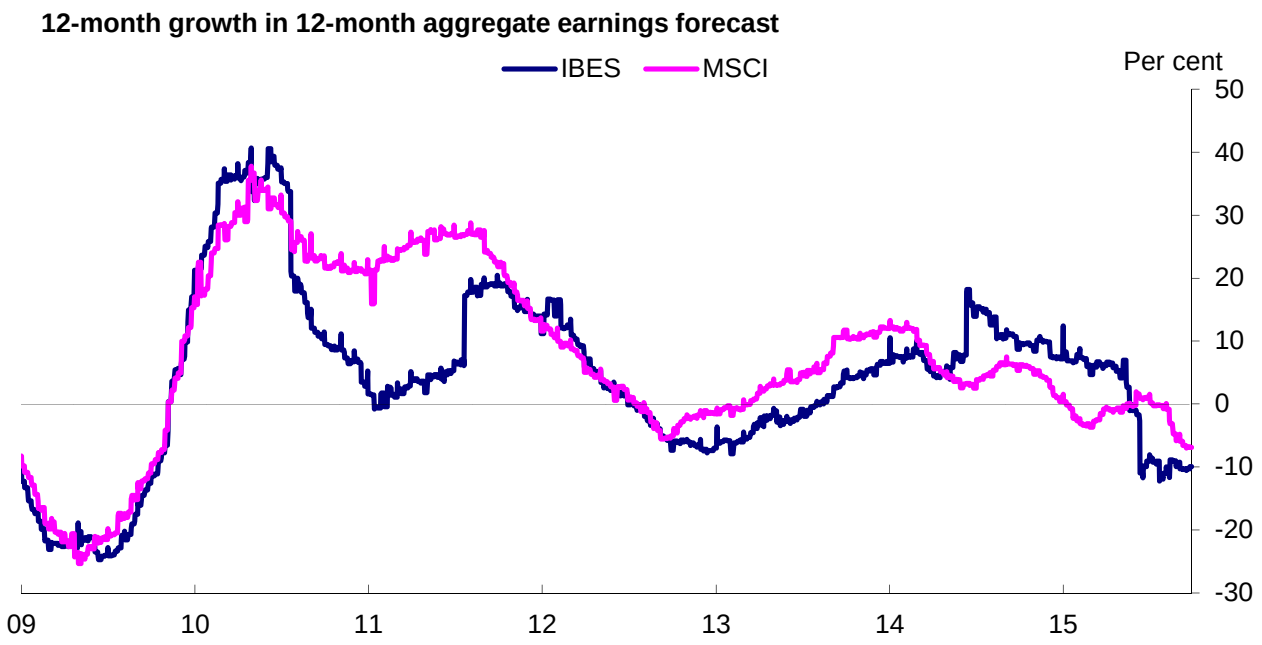
- Larger difference between Benchmark index and Asia-Pacific index in UK (commodities) than in EA, US.

Benchmark equity indices



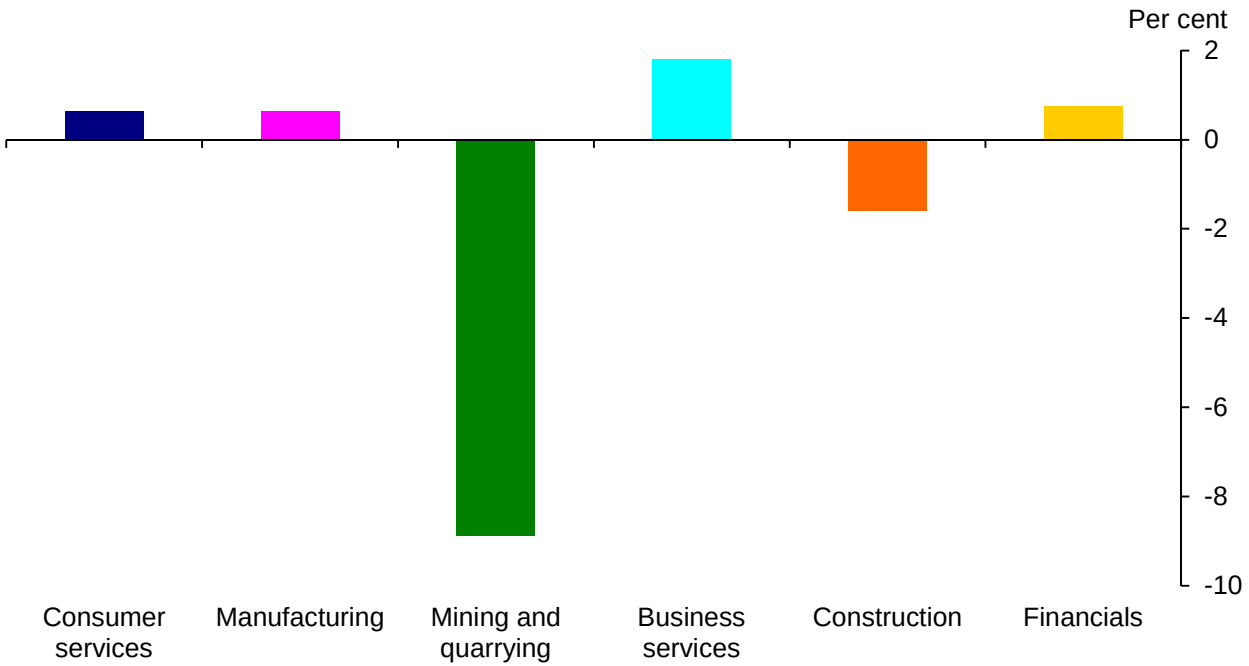
- Chinese equity prices have fallen by around 40% since their June peak. But this doesn't give us a clean read on the Chinese economy.

Earnings forecasts for Chinese equity-issuing firms



- Evidence of a sharp weakening in the Chinese economic outlook.
- But is the slowdown broad based?

Changes in Chinese sectoral earnings forecasts since Aug IR



- Weakness focused in mining and quarrying, and construction.
- But other sectoral earnings forecasts revised up, including business services.

Summary

- Renewed concern about emerging market economies, heightened by the FOMC.
- UK rates rose on labour market data but then fell following FOMC.
- Sterling down on the month, weakness against euro offset a little by strength against EMEs.

- Equity prices and earnings forecasts for UK domestically focused firms more positive than FTSE All-Share.
- Forecasts for Chinese equity-issuing firms' earnings have fallen…
- … but differentiation across sectors of the Chinese economy.

2: Global Environment

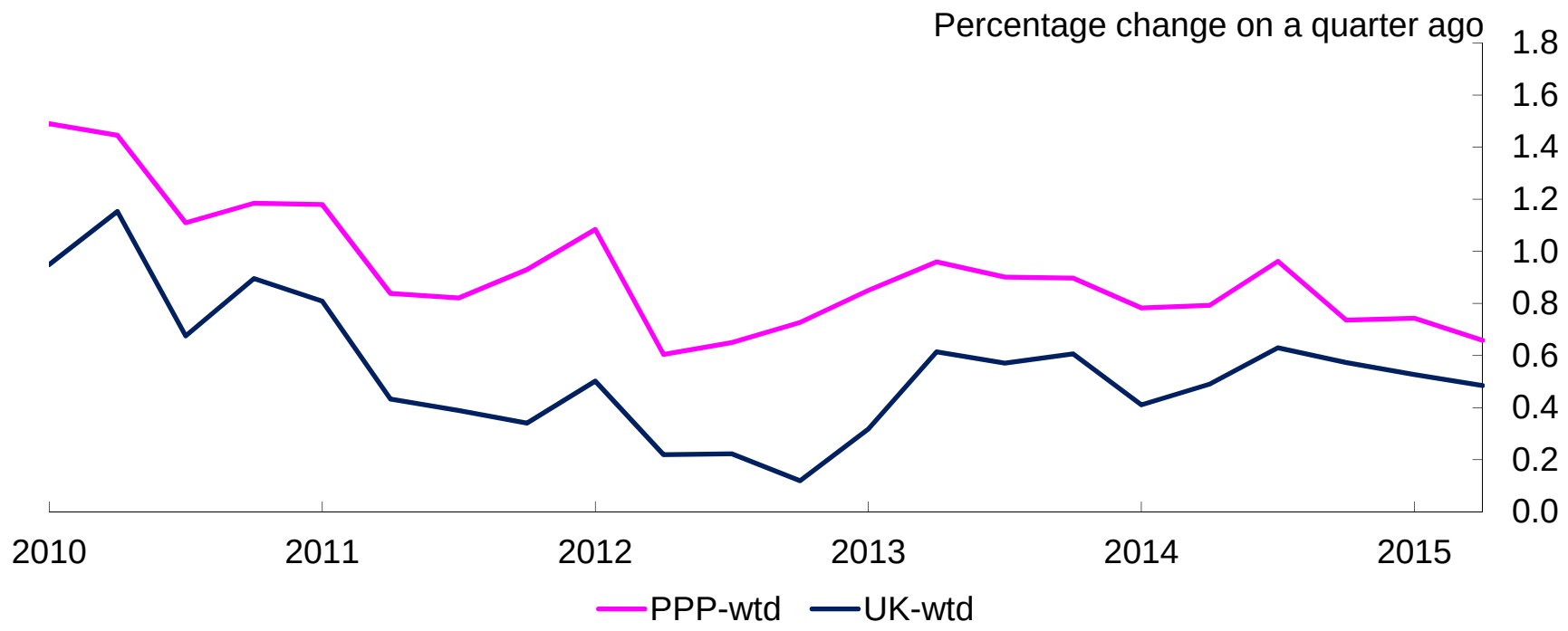
Bank of England
International Directorate

Global Environment and Risks
October 2015

Is the world economy continuing to slow?

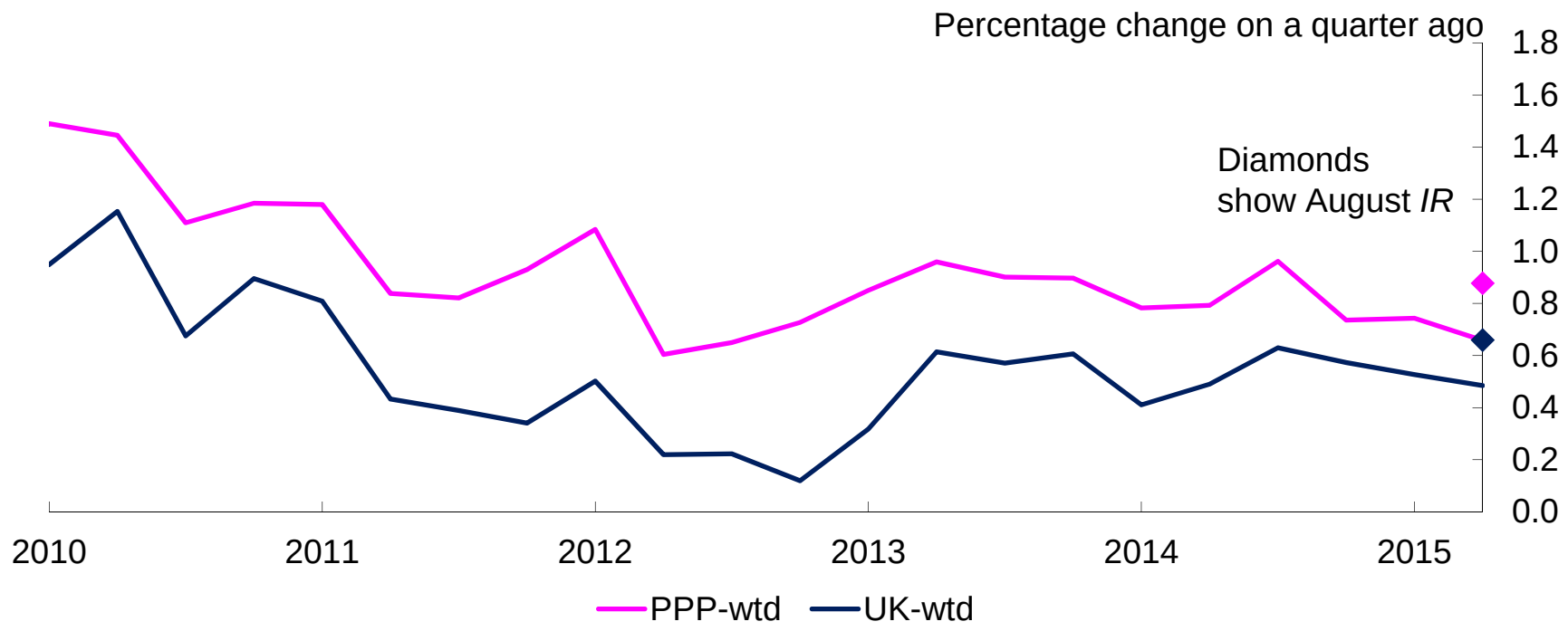
IEM October 2015: How worrying are prospects for the world economy?

World GDP



- Q2 growth ticked down on both measures (to 0.7% PPP-wtd and 0.5% UK-wtd).

World GDP



- Latest GDP outturns disappointed relative to August *IR*

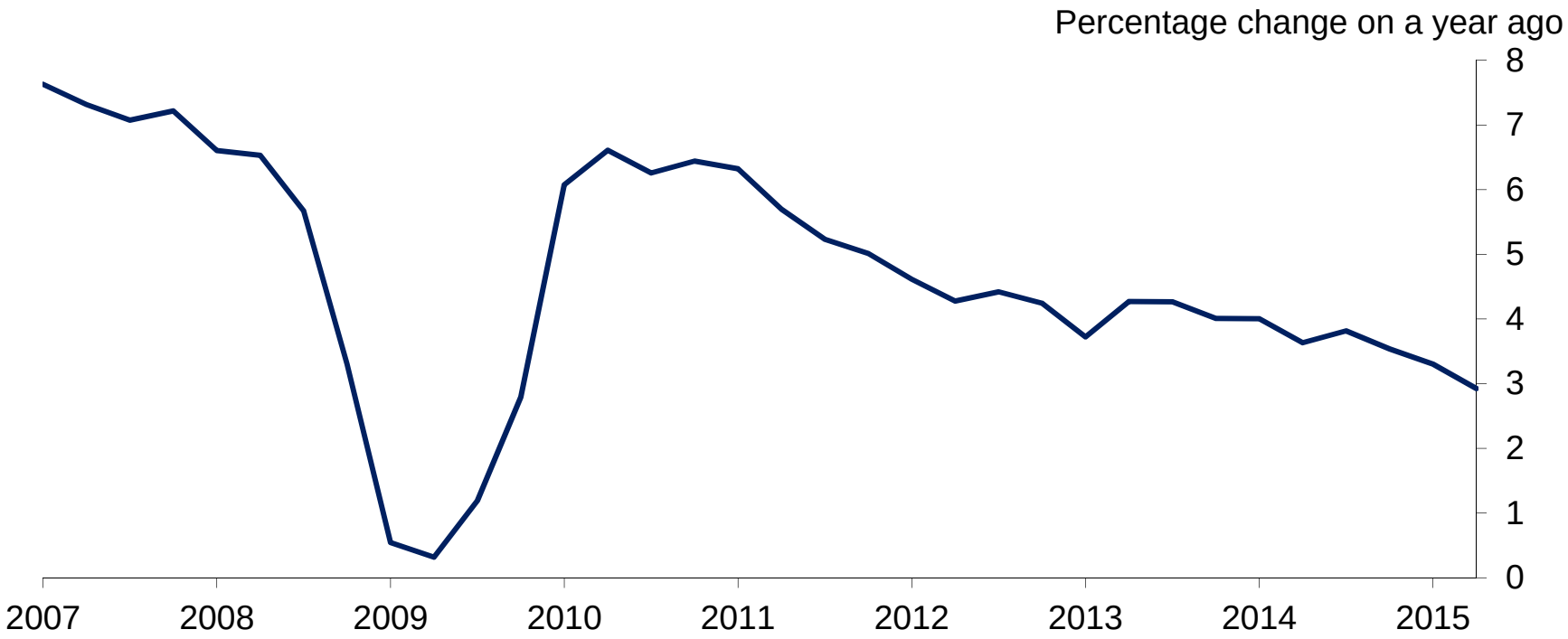
Plan

Is the world economy continuing to slow?

- Emerging markets (excluding China)
- China
- United States
- Euro Area
- Global indicators and world trade

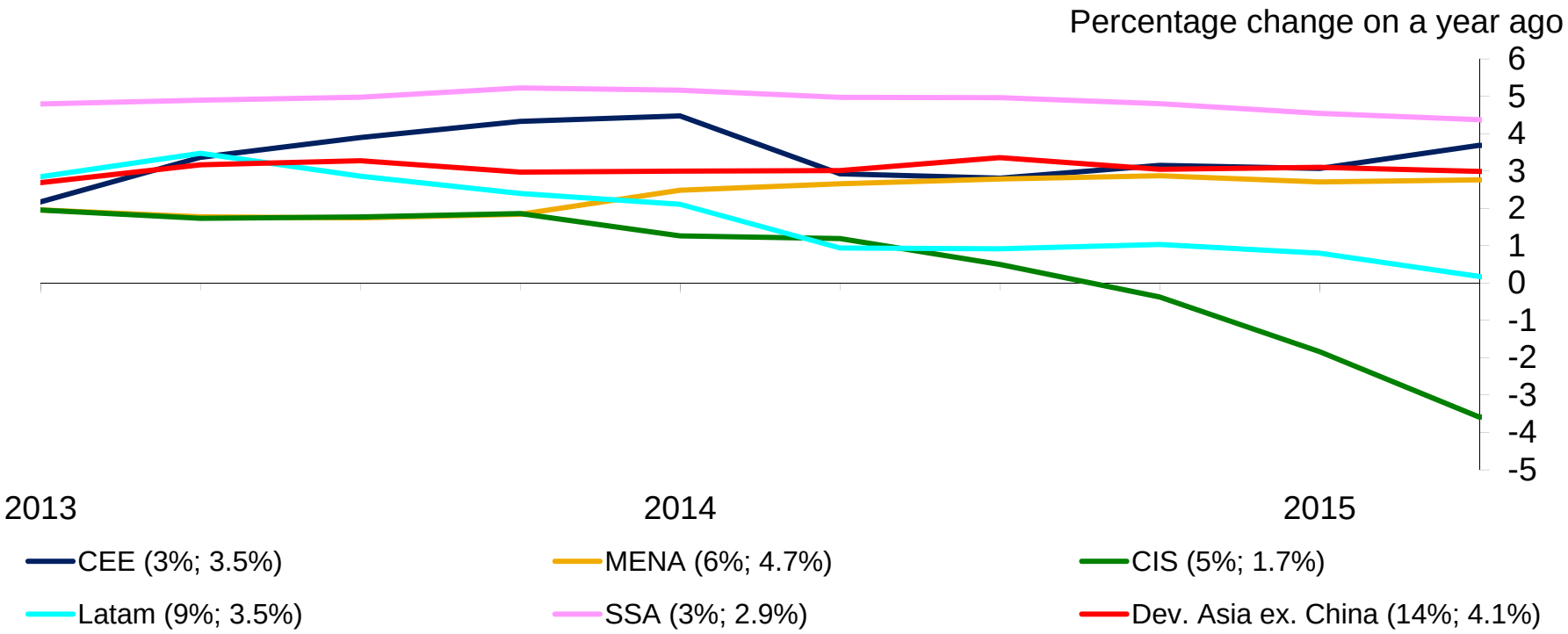
EMEs (excluding China)

EME GDP (excluding China)



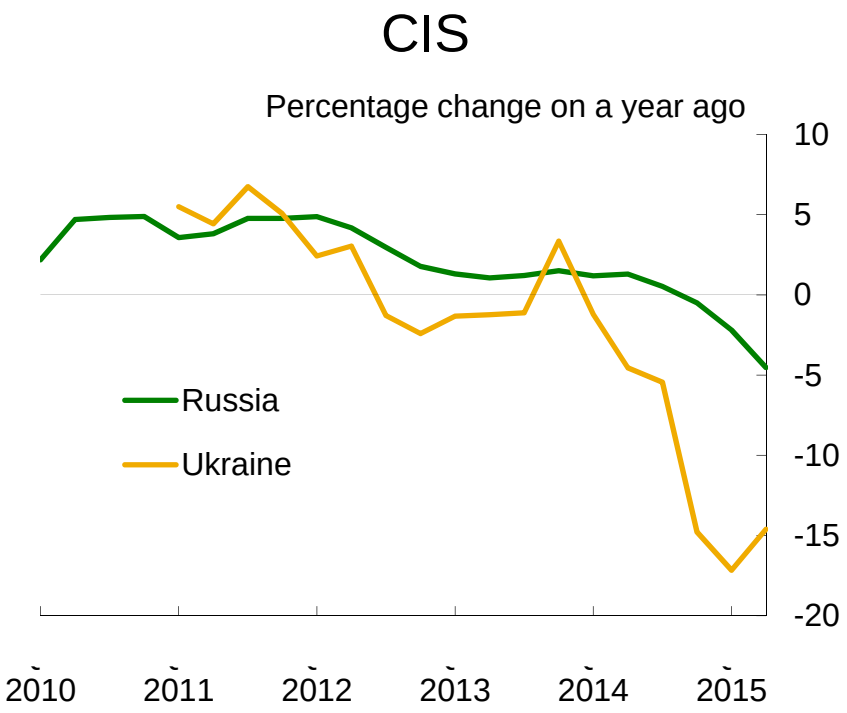
- Steady slowing in EME (ex. China) growth since the financial crisis.

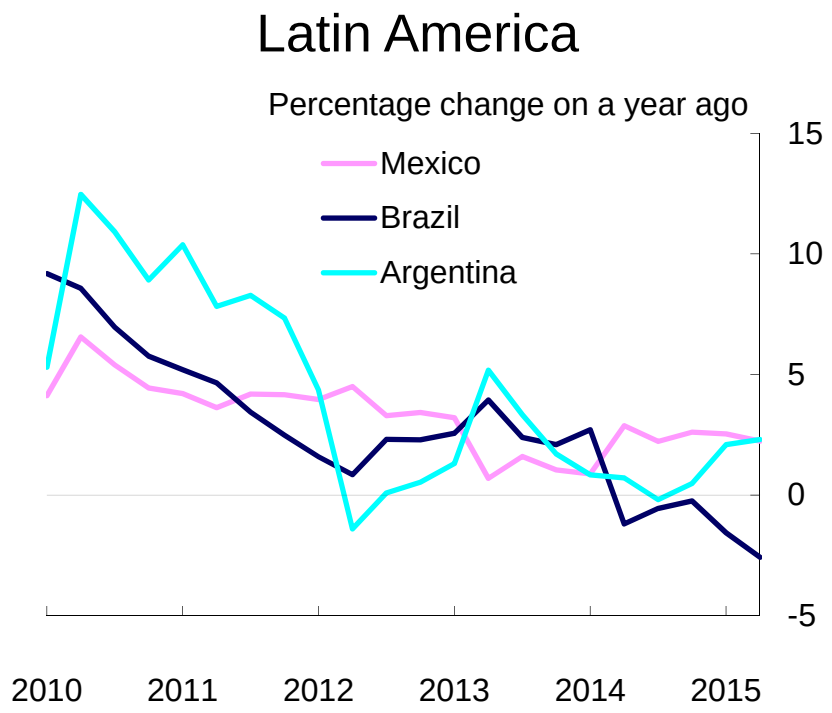
EME GDP



The numbers in brackets indicate respective area weights in PPP-weighted world GDP first and UK export weights second

GDP in selected EMEs



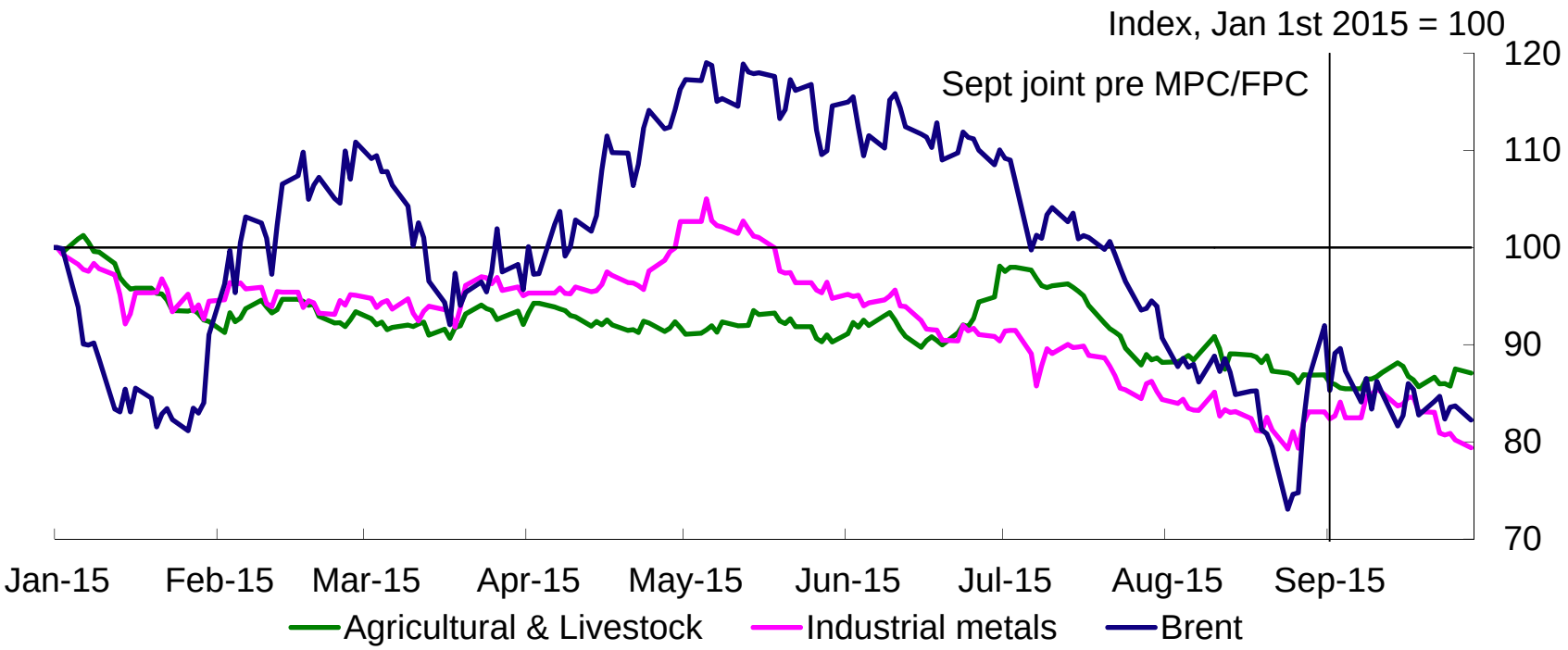


- **International View: Latin America.**

Prospects for EMEs

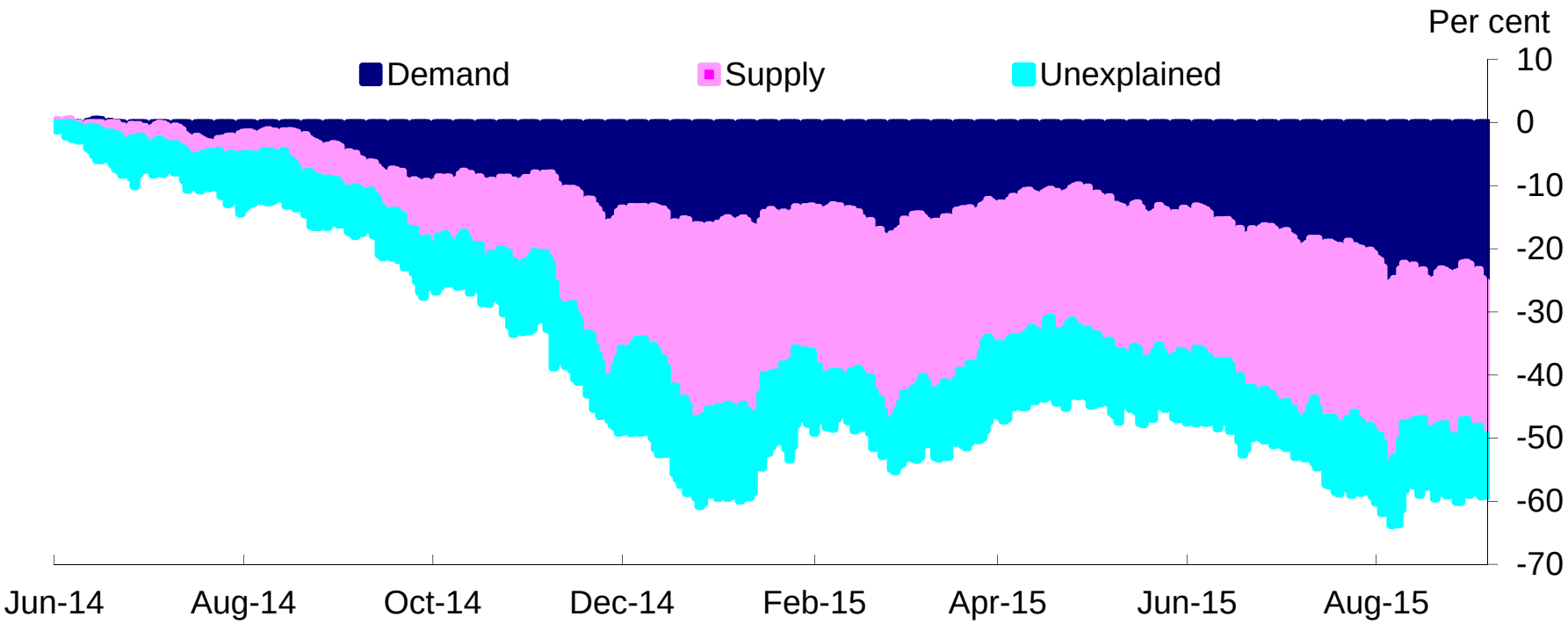
- Little hard evidence beyond Q2.
- Commodity prices fallen further.

Commodity prices



- On the month, both oil and metals prices are down about 3.5%.

Oil price decomposition

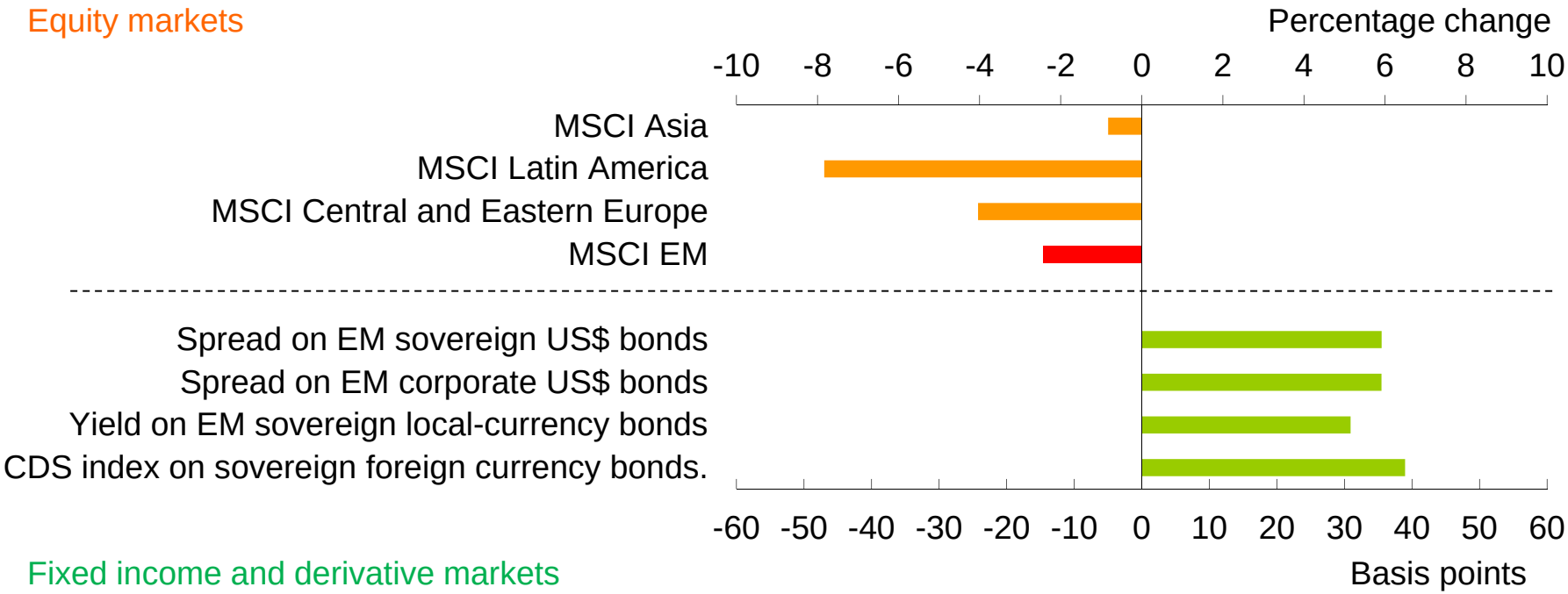


- Oil price falls since May have been more demand-driven than previous falls.

Prospects for EMEs

- Little hard evidence beyond Q2.
- Commodity prices fallen further, although not necessarily bad for all EMEs.
- Tighter financial conditions – equity prices down and bond spreads up.

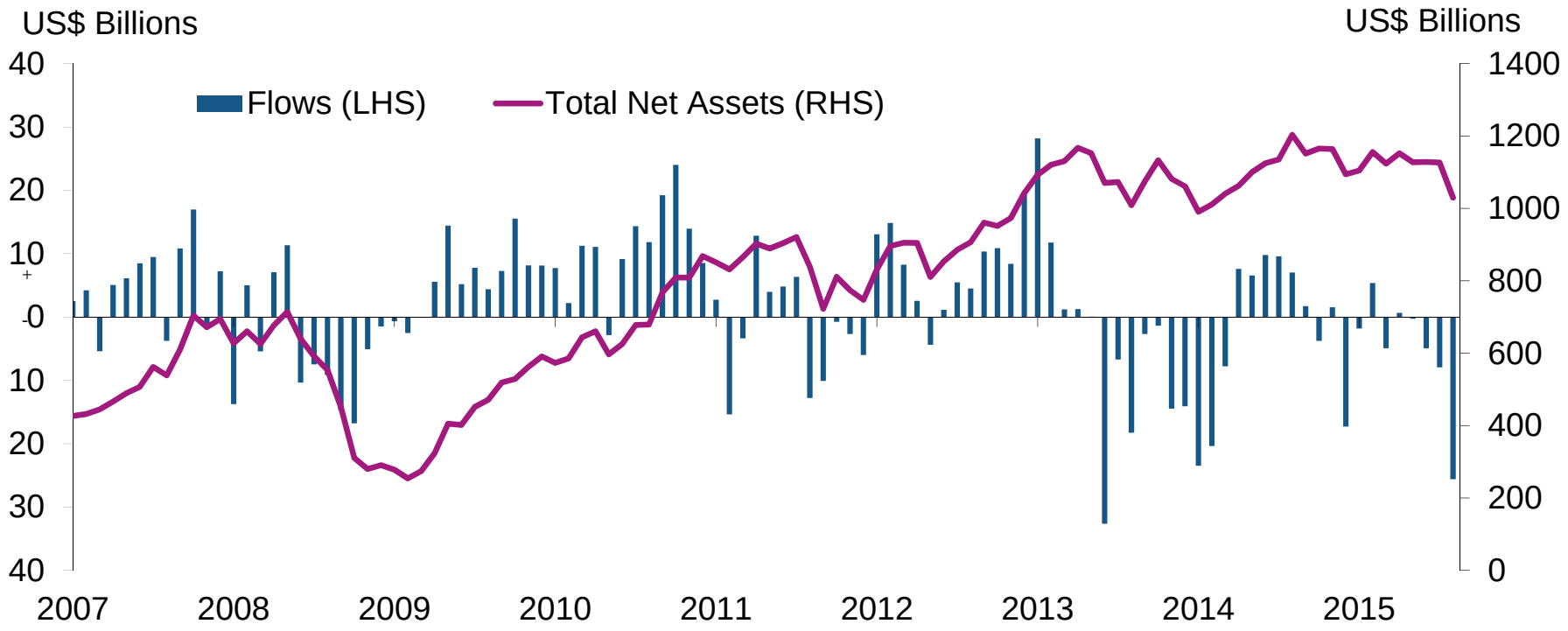
Change in EM asset prices over the past month



Prospects for EMEs

- Little hard evidence beyond Q2.
- Commodity prices fallen further, although not necessarily bad for all EMEs.
- Tighter financial conditions – equity prices down and bond spreads up.
- Some capital outflows have intensified.

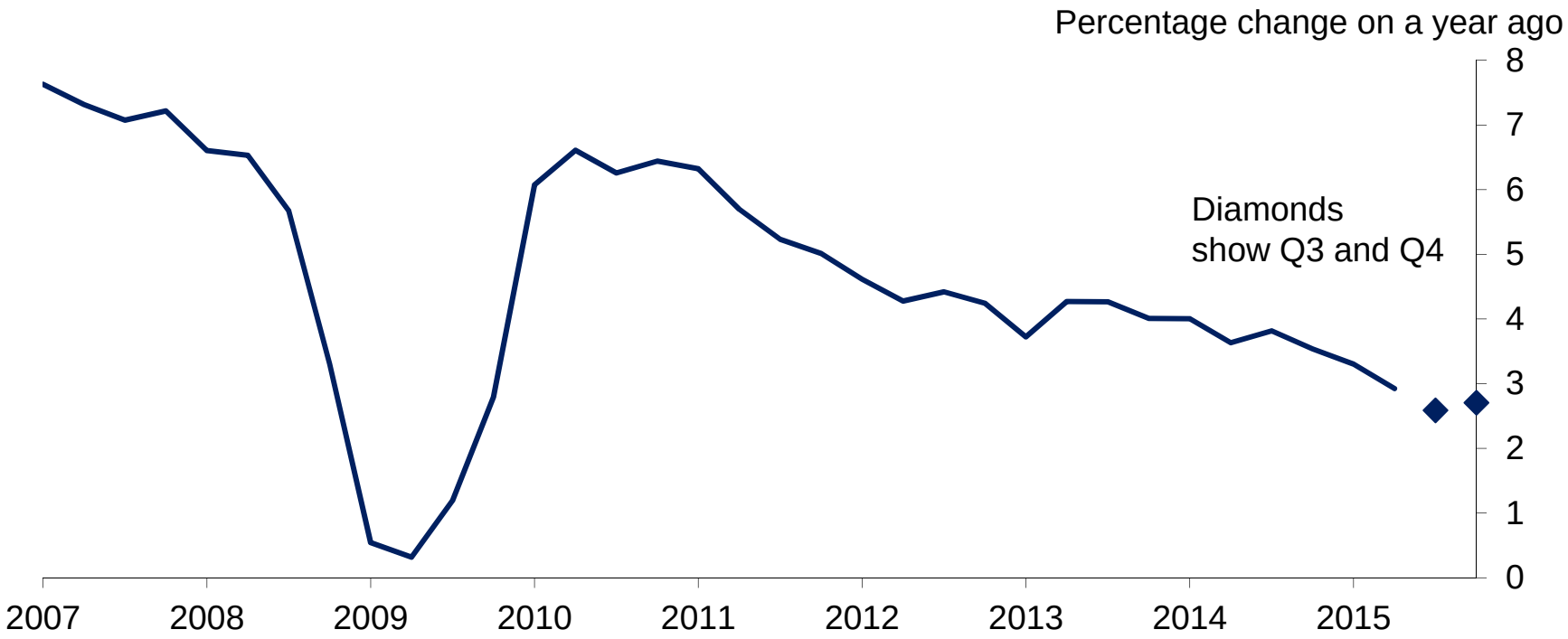
Flows to EM-dedicated (ex. China) equity and debt funds



Prospects for EMEs

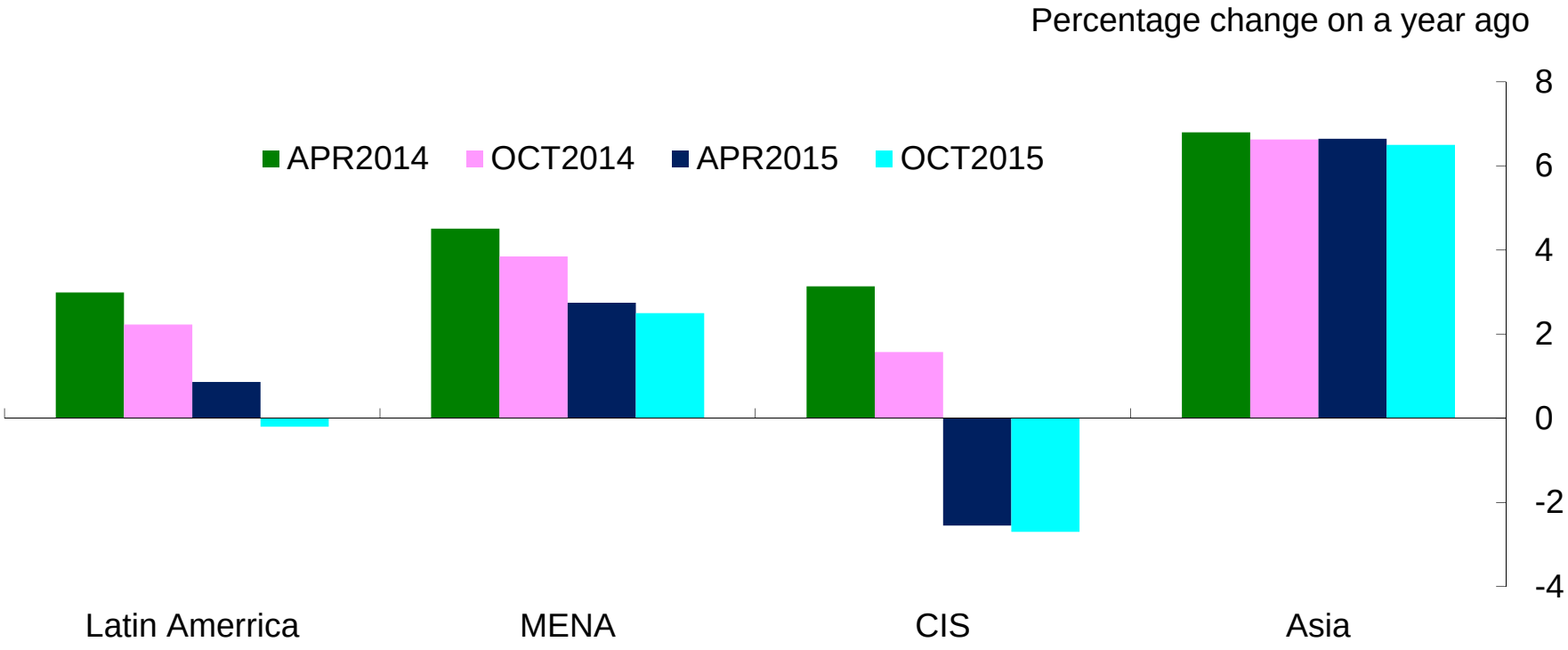
- Little hard evidence beyond Q2.
- Commodity prices fallen further, although not necessarily bad for all EMEs.
- Tighter financial conditions – equity prices down and bond spreads up.
- Some capital outflows have intensified.
- Based on IMF October WEO forecasts, we expect a stabilisation in EME (excluding China) growth in 2015 H2.

EME GDP (excluding China)



- IMF October WEO implies a stabilisation in growth in 2015 H2.

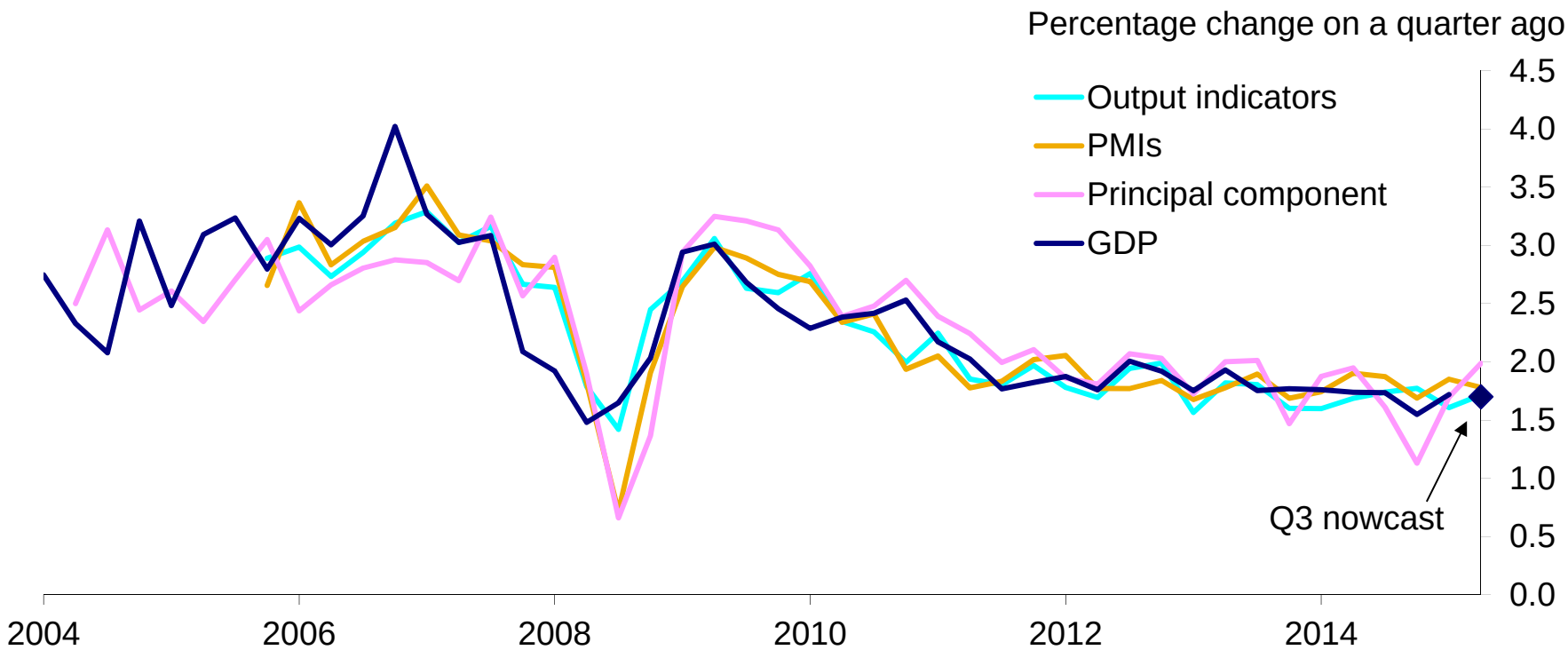
IMF WEO forecasts for 2015



- IMF forecasts for EME growth in 2015 have been repeatedly revised down.

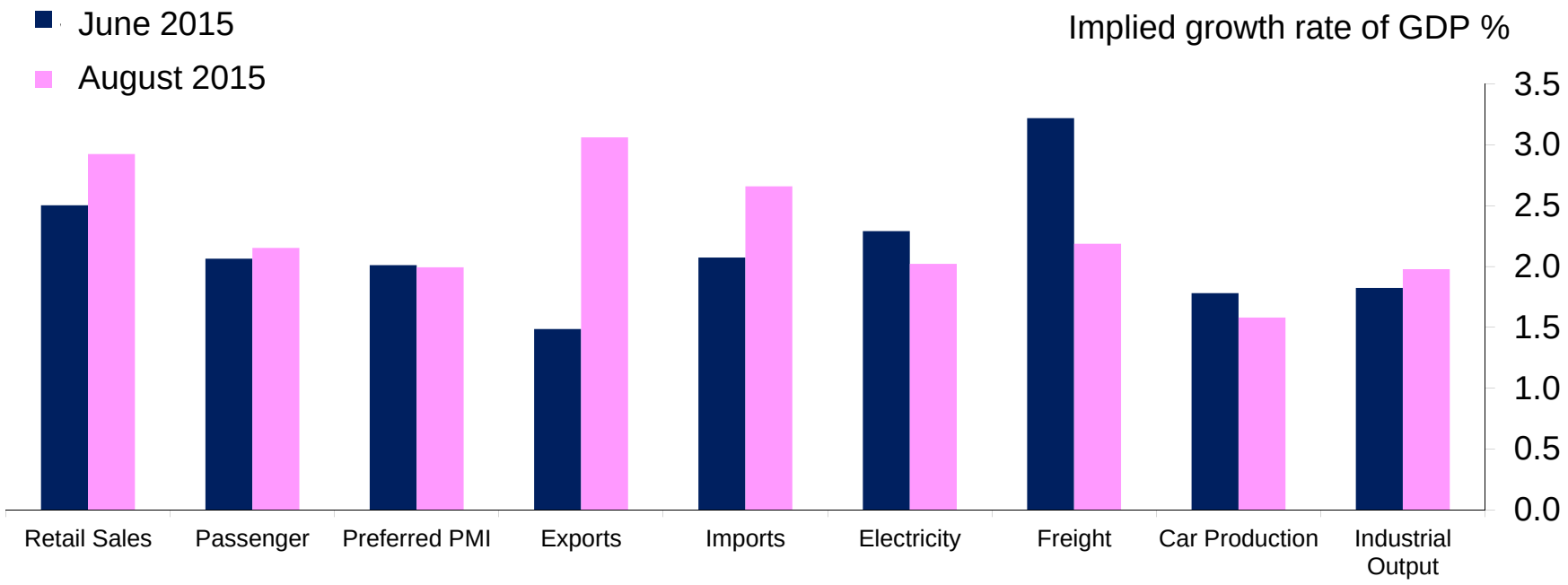
China

Chinese GDP and activity indicators



Principal component measure contains a range of mainly industrial indicators.

Chinese activity indicators



- Little sign of a downturn in Chinese activity so far.

China GDP growth

	Q3	Q4	2015
Nov *BMK*	1.7%	1.6%	6.8%
Aug *IR*	1.6%	1.6%	6.7%

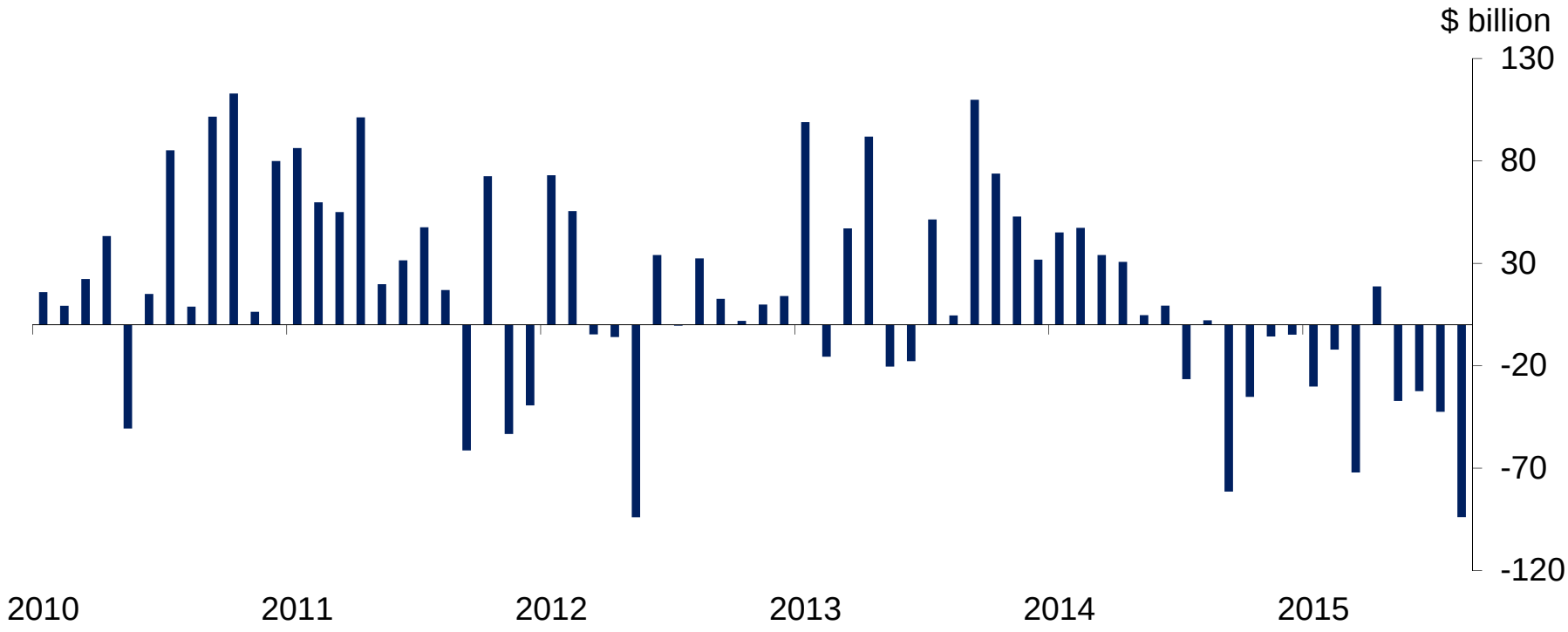
Memo - Q1: 1.4% oqa; Q2: 1.7% oqa

Policy actions in China

- Benchmark rates cut by 50bp since June.

- Fiscal and financial reform measures including:
  - Additional support for home buyers by relaxing restrictions on down-payments.
  - Establishment of a SME Development Fund to support SME growth.
  - Further infrastructure spending to be supported via policy banks.
  - A higher local government debt limit.

Monthly changes in China's FX reserves

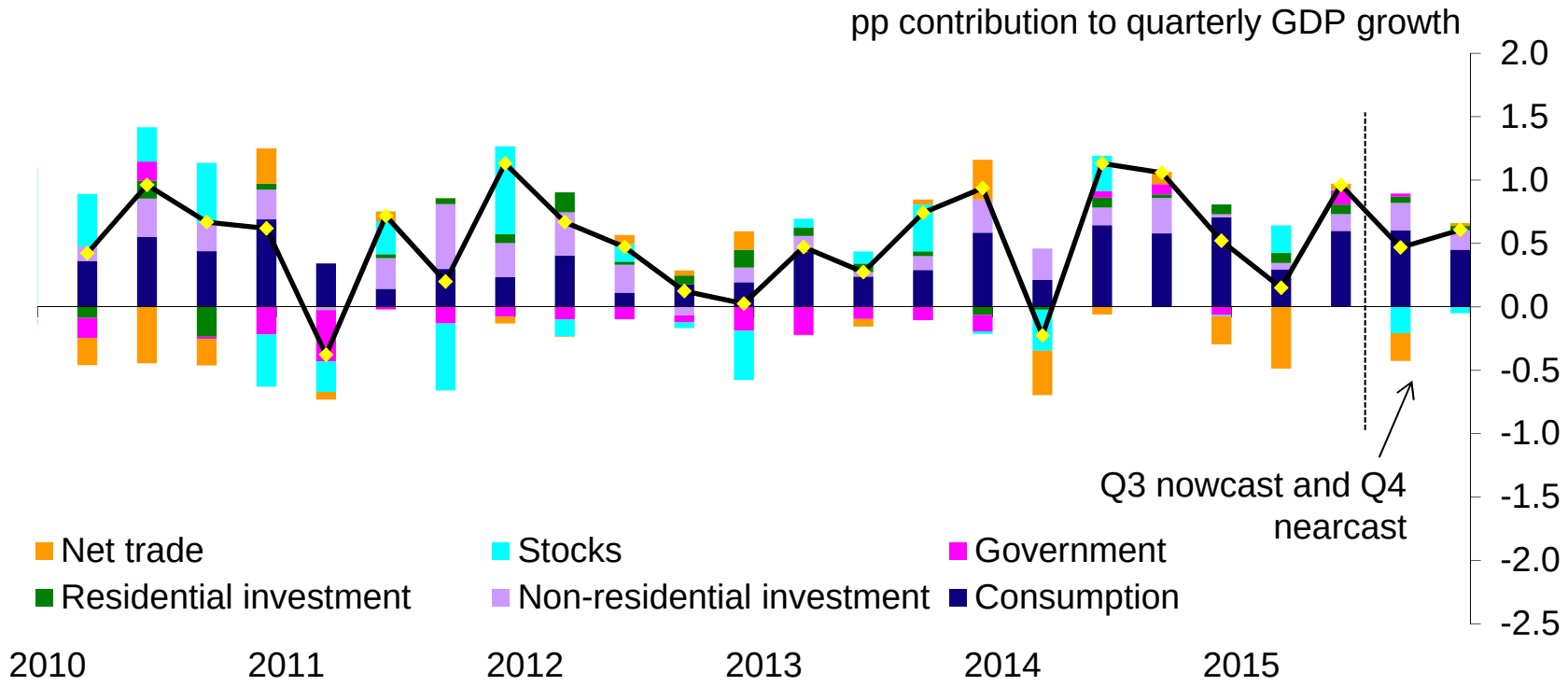


Factors determining further private outflows

- Spread between US and Chinese rates;
- Expectations of further depreciation;
- Fiscal policy action to improve the growth outlook;
- Exchange controls.

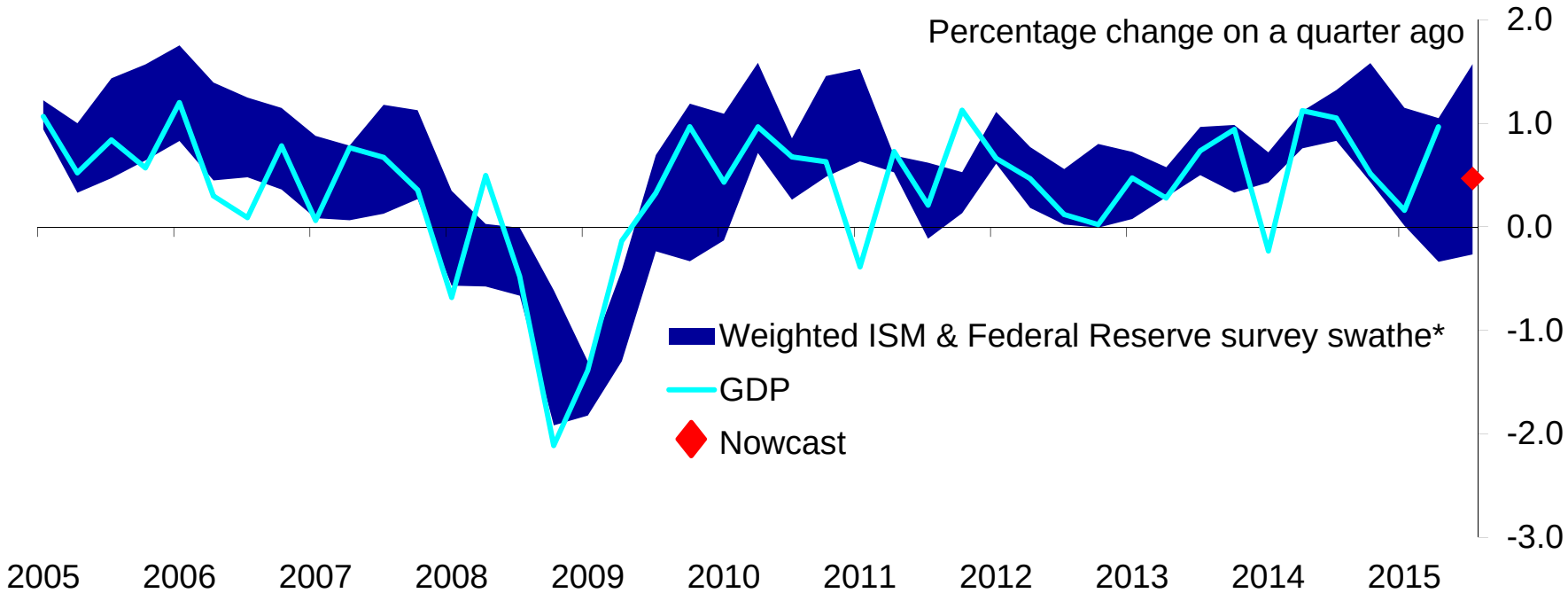
United States

US GDP



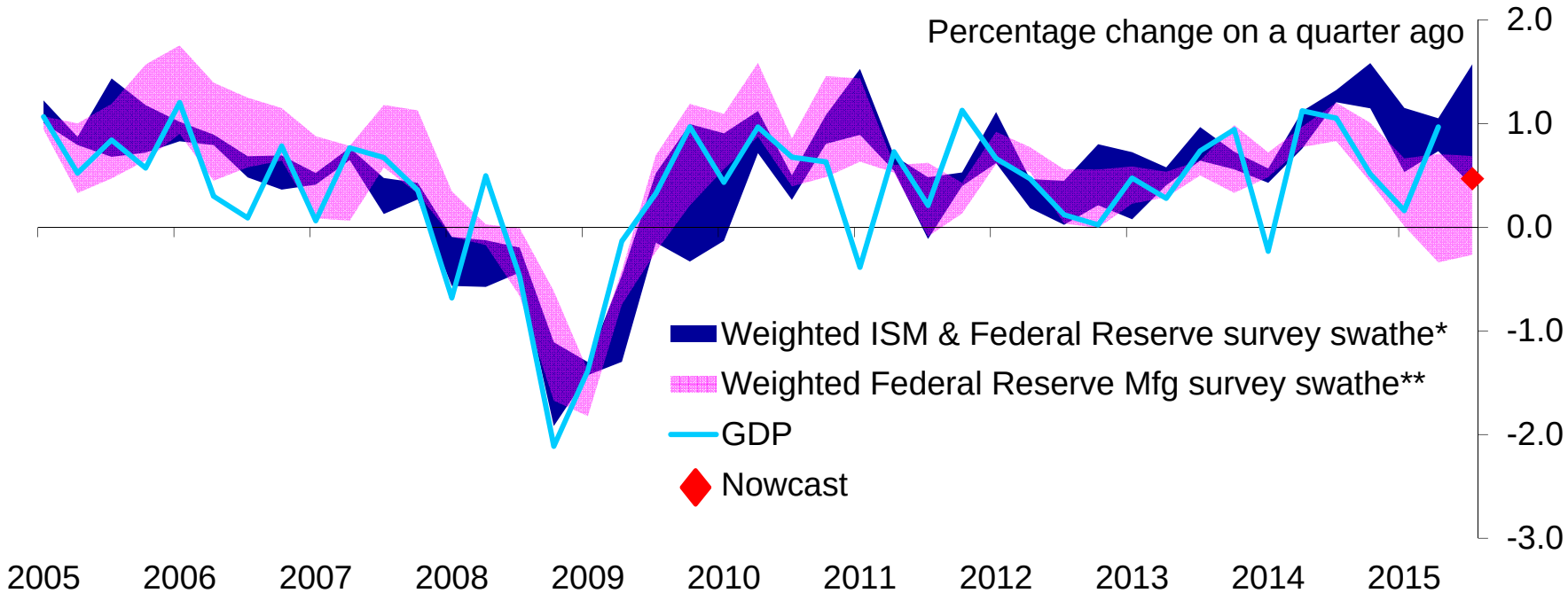
- Q2 GDP growth was revised up to 1.0%, a touch stronger than the August IR.

US GDP and activity indicators



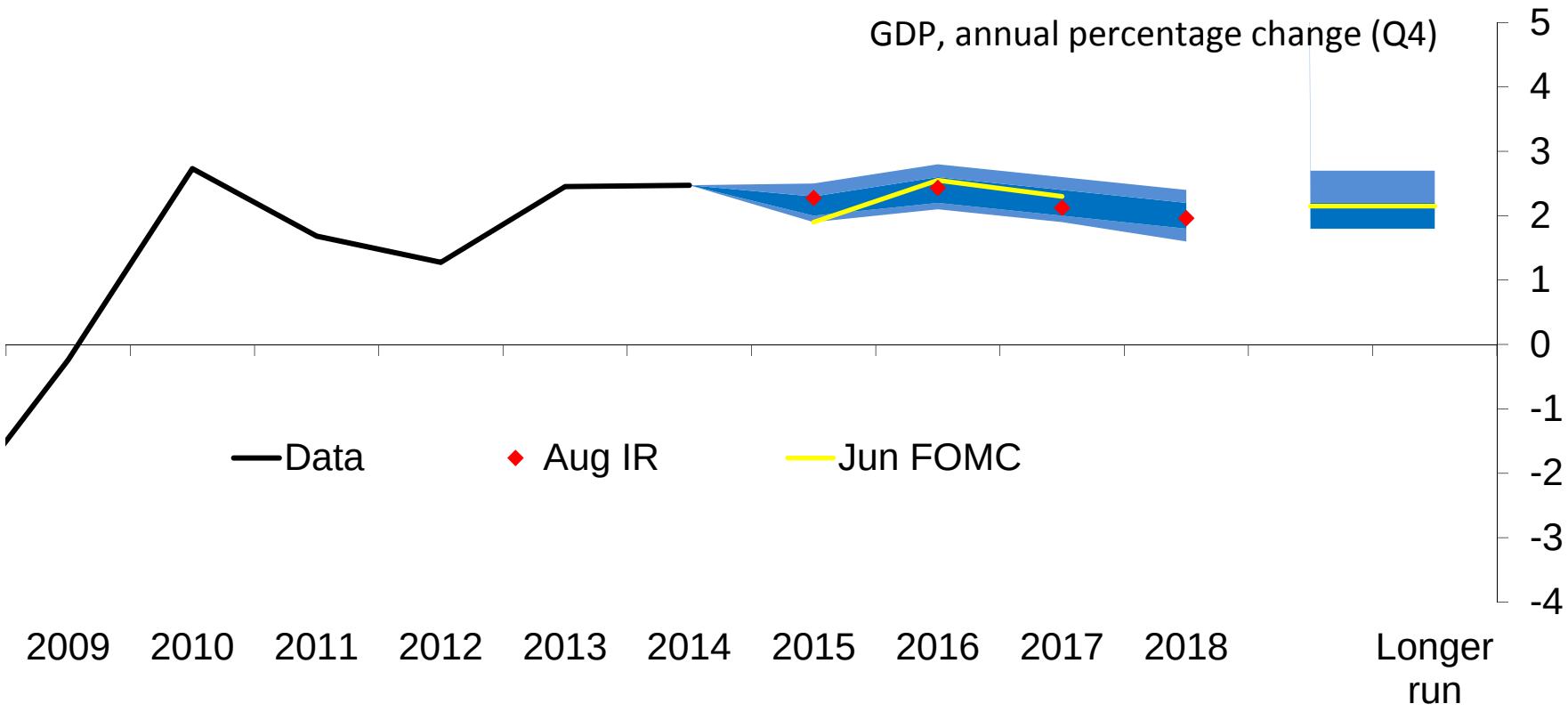
*Federal Reserve surveys: New York Empire State Manufacturing, Philadelphia Fed Business Outlook survey, Weighted Richmond Fed Manufacturing & Services surveys, Weighted ISM, Richmond Fed Manufacturing, Dallas Fed Manufacturing. Data up to August & September.

US GDP and activity indicators

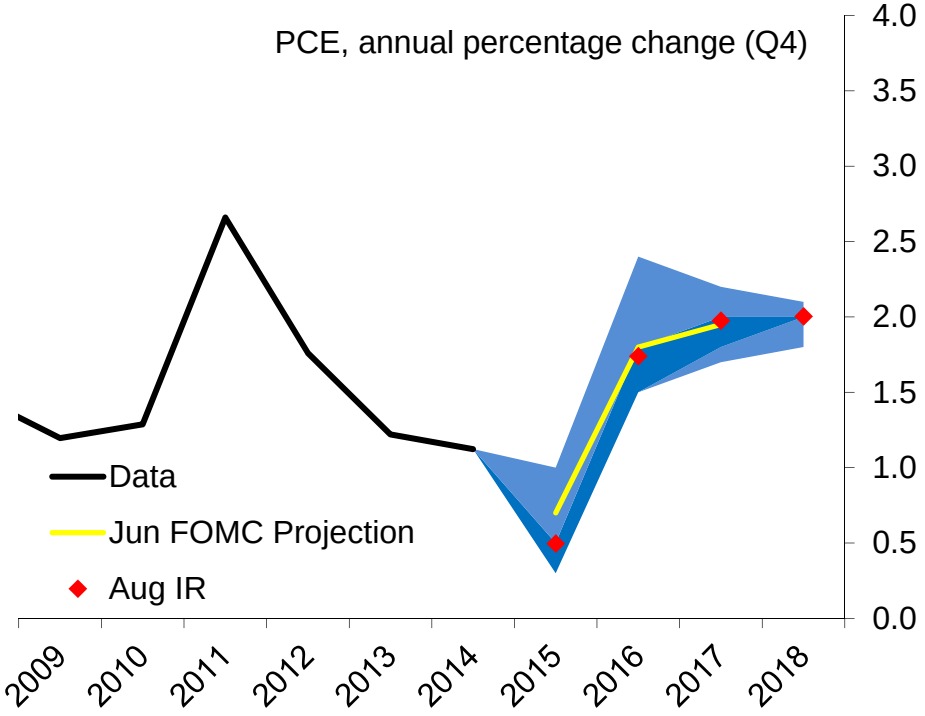


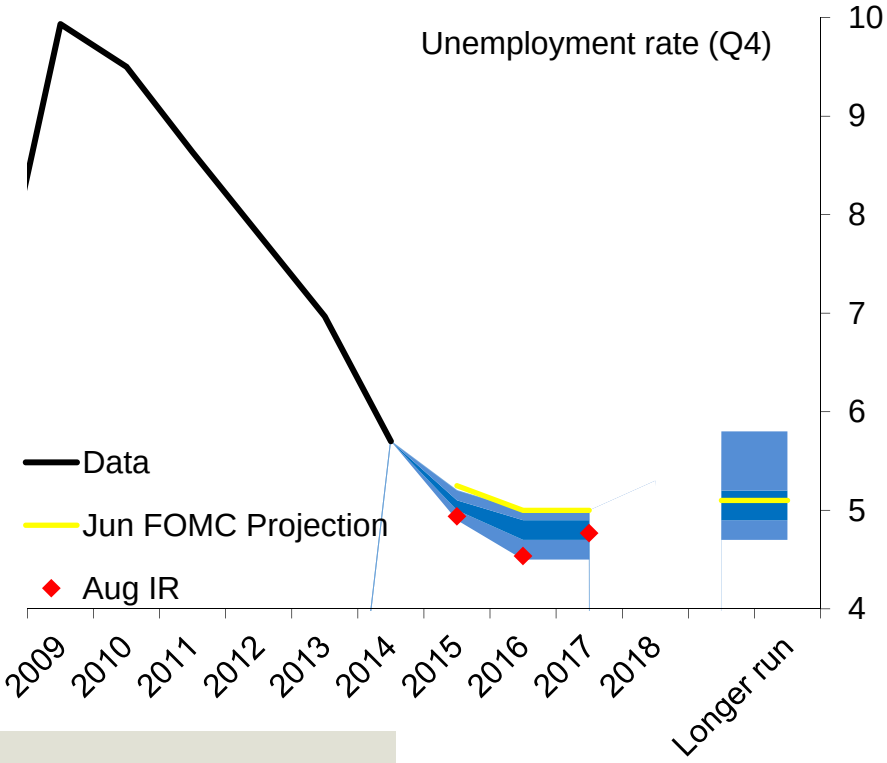
*Weighted ISM & Federal Reserve surveys: Philadelphia Fed Business Outlook survey, Weighted Richmond Fed Manufacturing & Services surveys, Weighted ISM.
**Federal Reserve Mfg surveys: New York Empire State Manufacturing, Richmond Fed Manufacturing, Dallas Fed Manufacturing.
Data up to August & September.

FOMC Macroeconomic Projections



FOMC macroeconomic projections





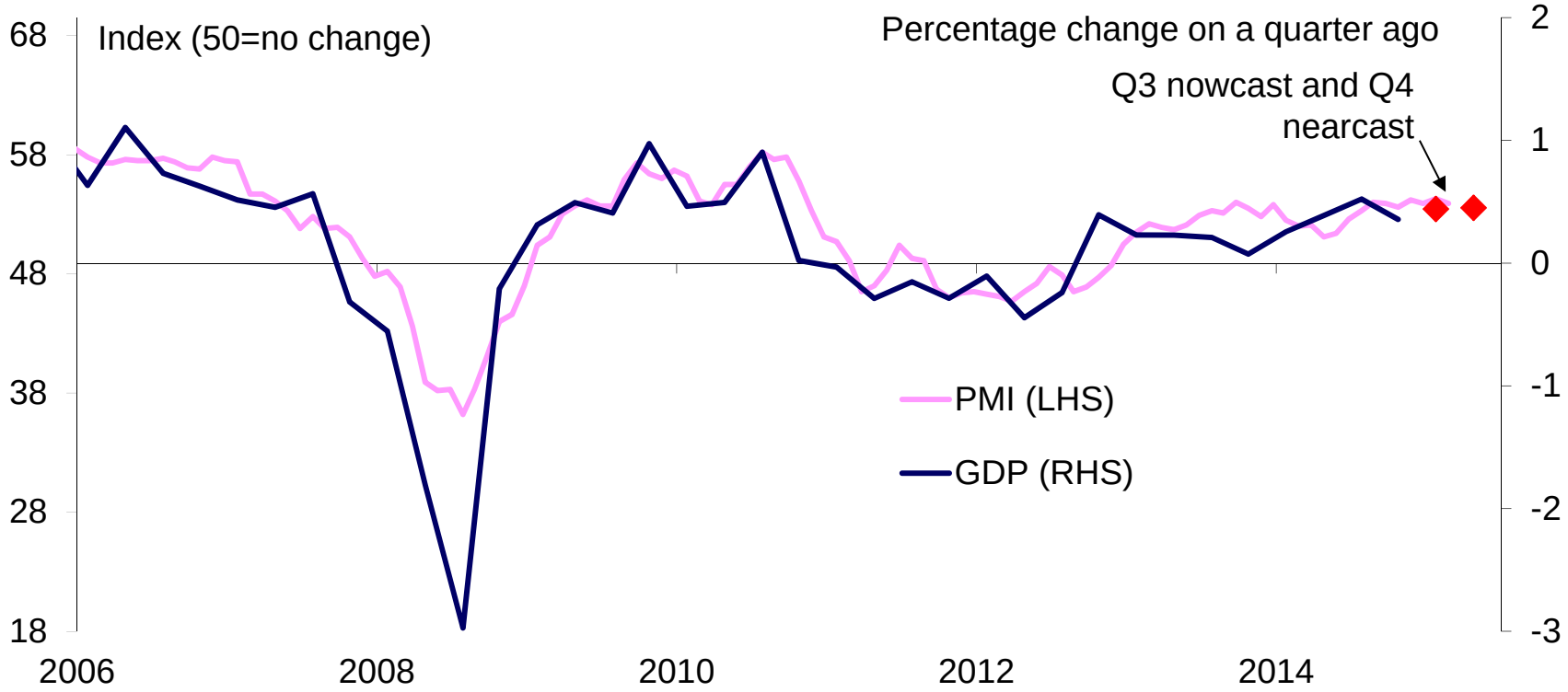
Possible US government shutdown

- The deadline for congress to pass legislation to avoid another government shutdown expires at **midnight tonight**.

- The Senate has advanced a **short-term Continuing Resolution to extend funding until December**. With the bill expected to be approved by the House, albeit very close to the midnight deadline, a **government shutdown is now unlikely**.

Euro Area

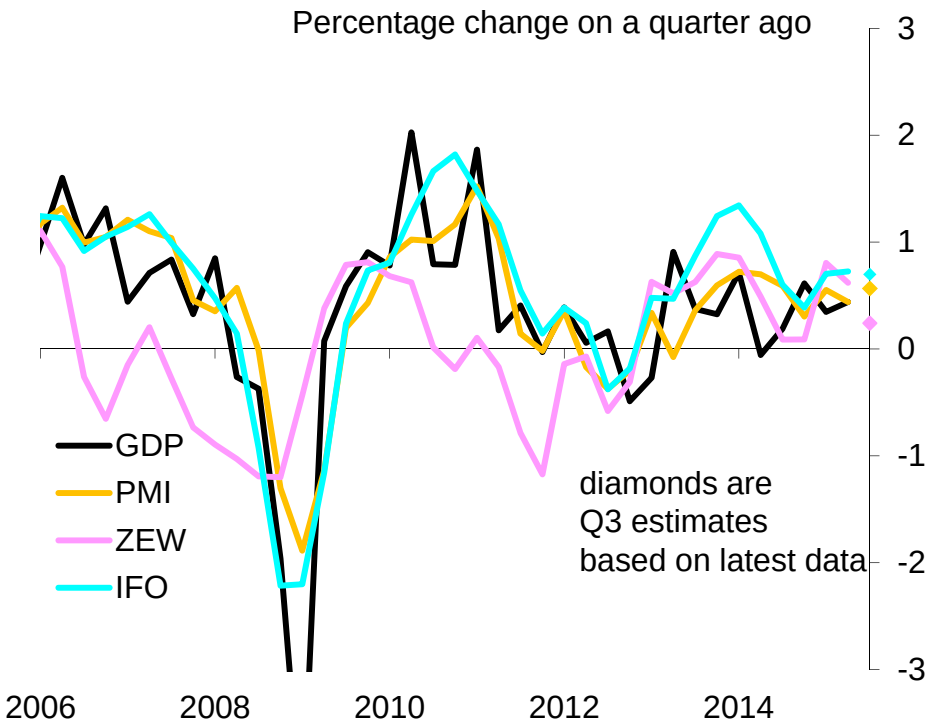
Euro-area PMIs and GDP growth



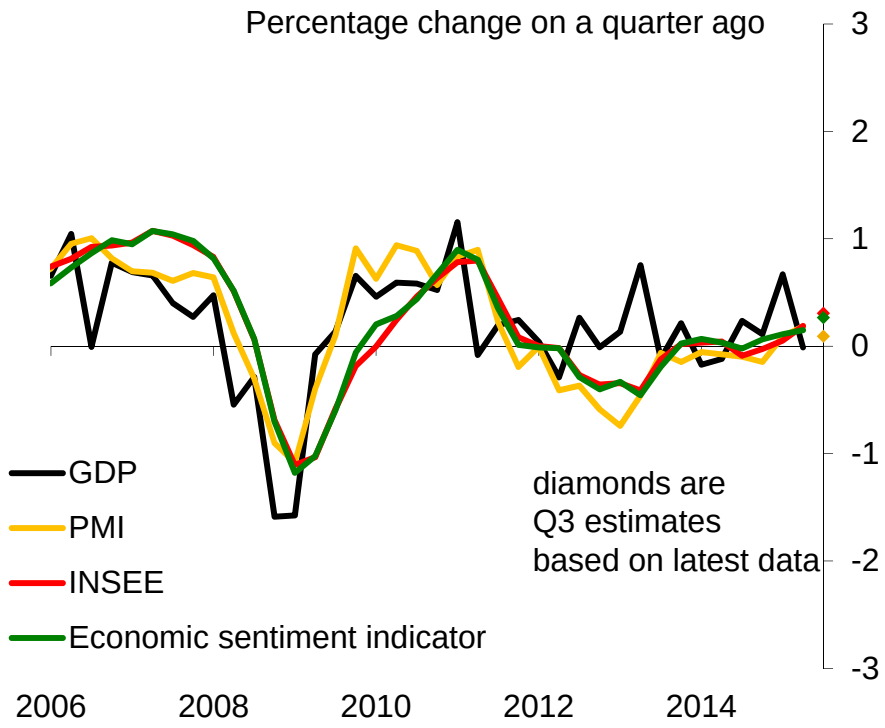
- Q2 GDP growth was revised up to 0.4%, in line with the August IR.

Outlook for Germany and France

Germany

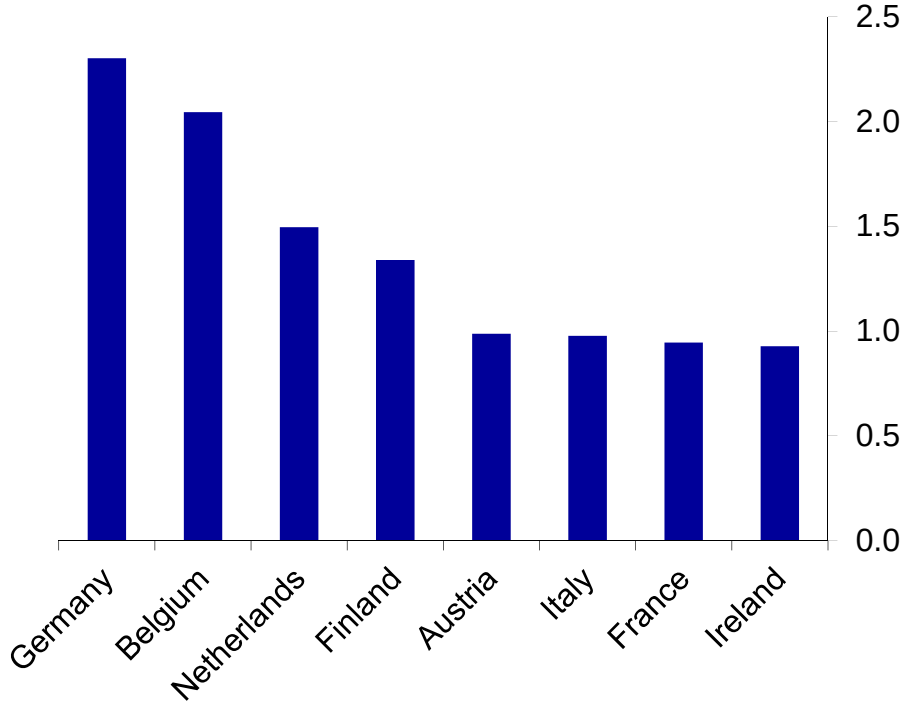


France

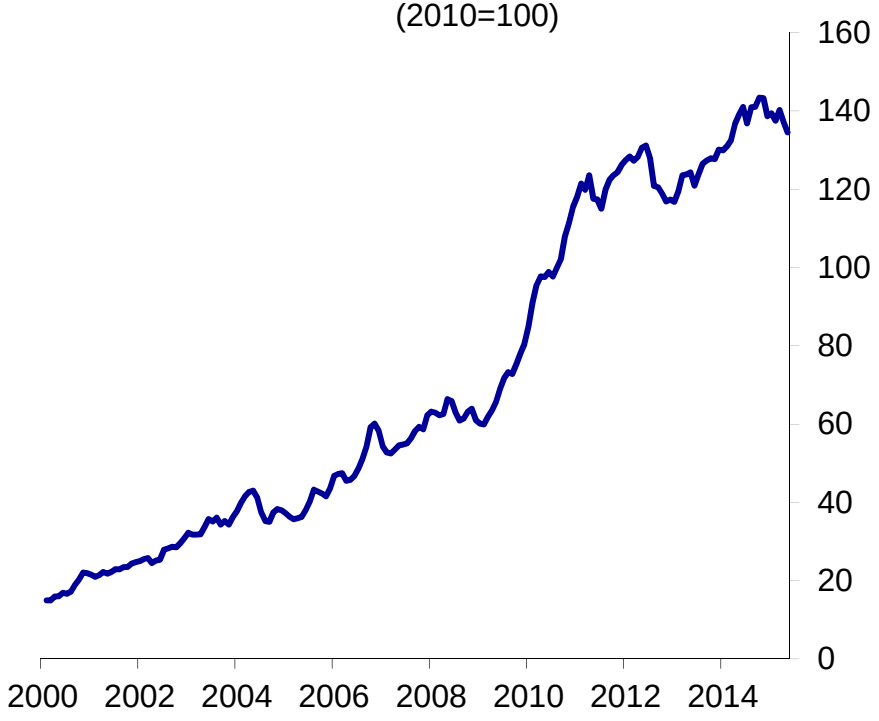


German exports to China

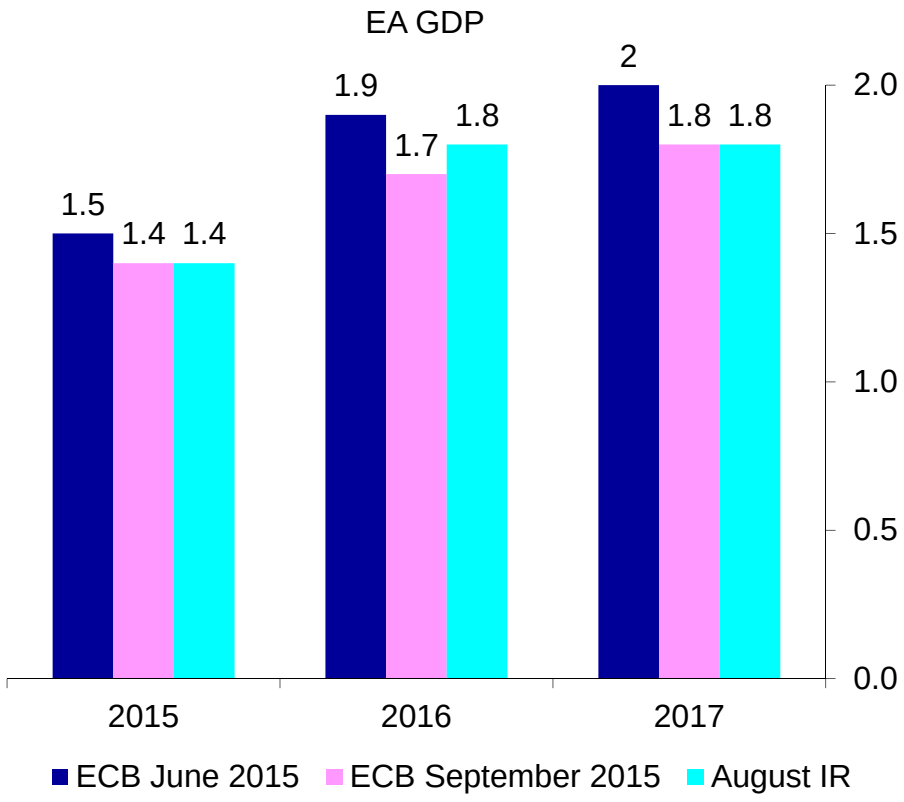
Nominal value of goods exports to China as a % of GDP (2014)

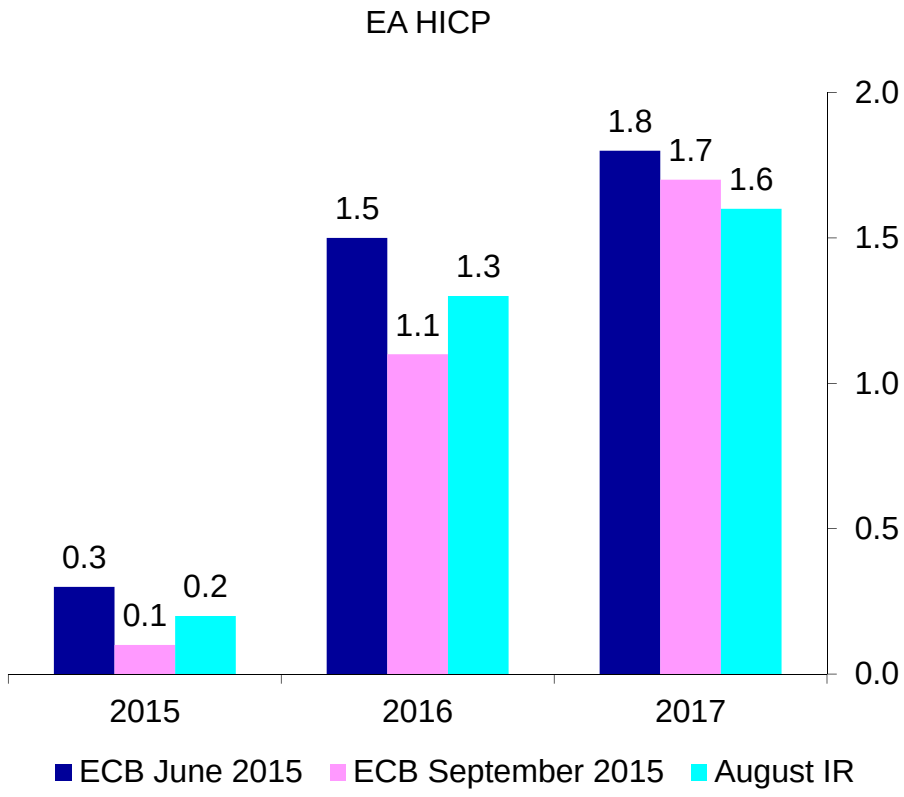


German export values to China, 3m average, €, SA (2010=100)



ECB staff forecasts





Political risks in Europe

Greece

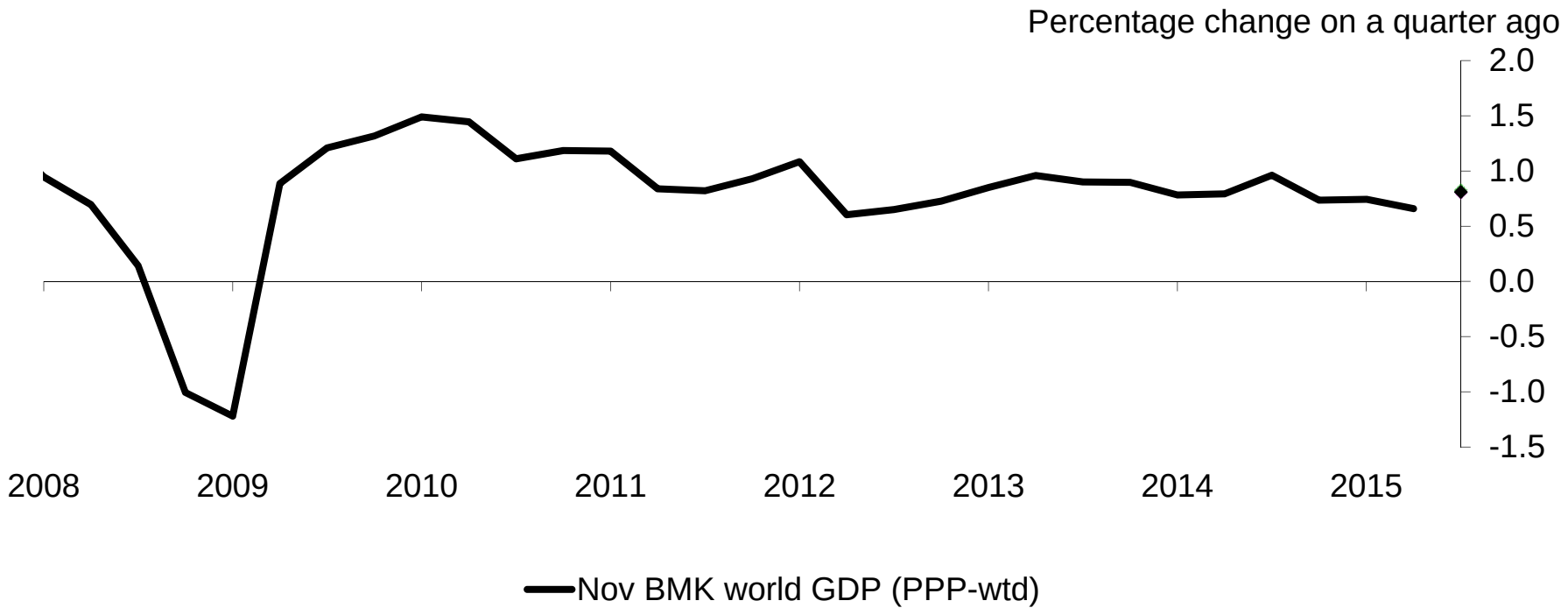
- Election results don't change our assessment of medium-term risks
- Next key milestone is results of AQR and stress tests in mid to late October; first ESM programme review at a similar time; debt talks thereafter

Spain

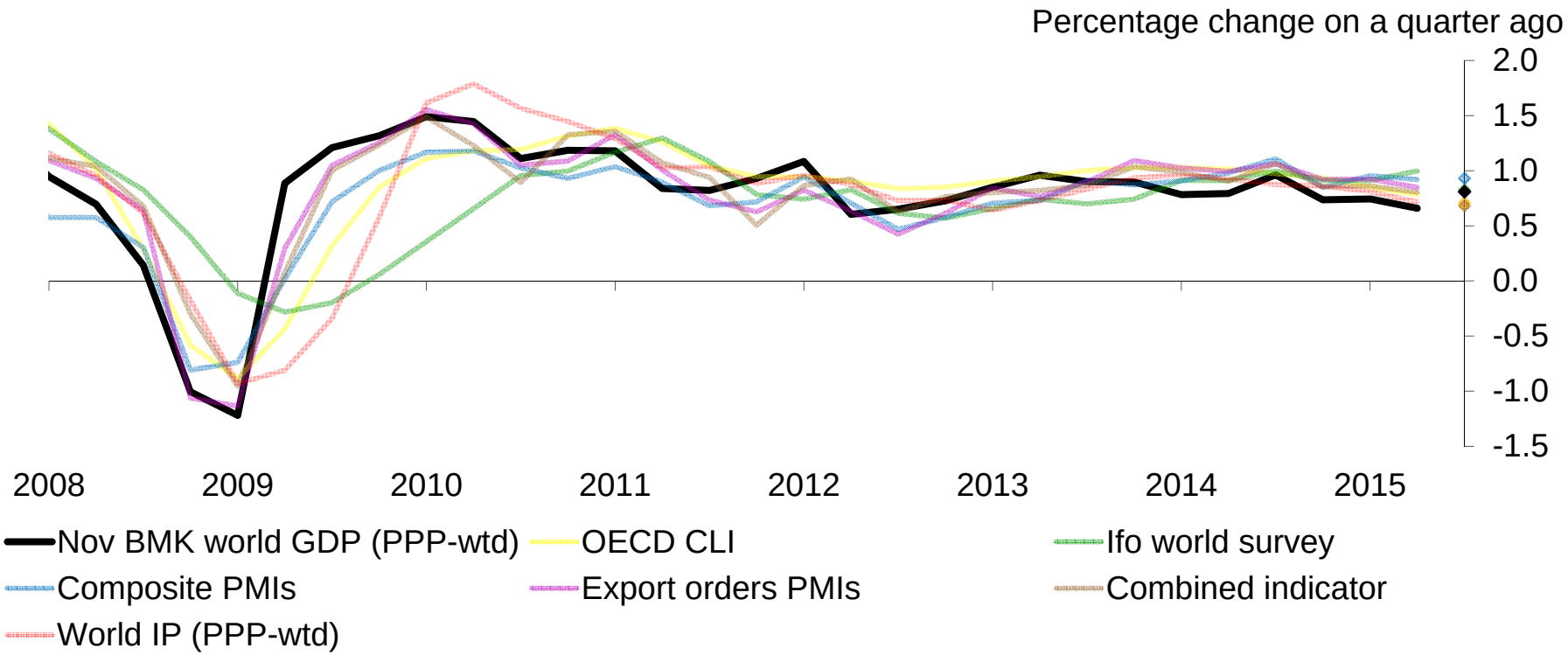
- Strong support for pro-independence parties, but less than the 50% of votes that would be needed in a referendum, and a little less than at the last vote. Next steps are coalition talks and a dialogue with the national government.

World outlook

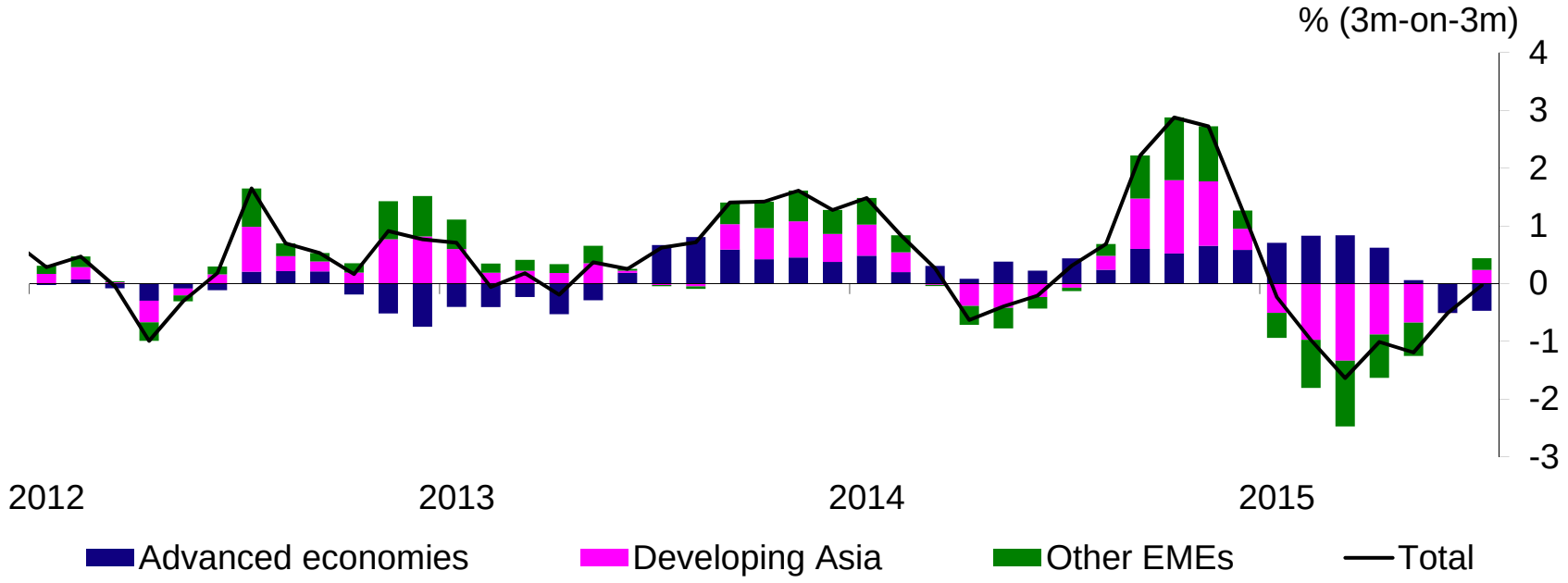
Indicators of global activity



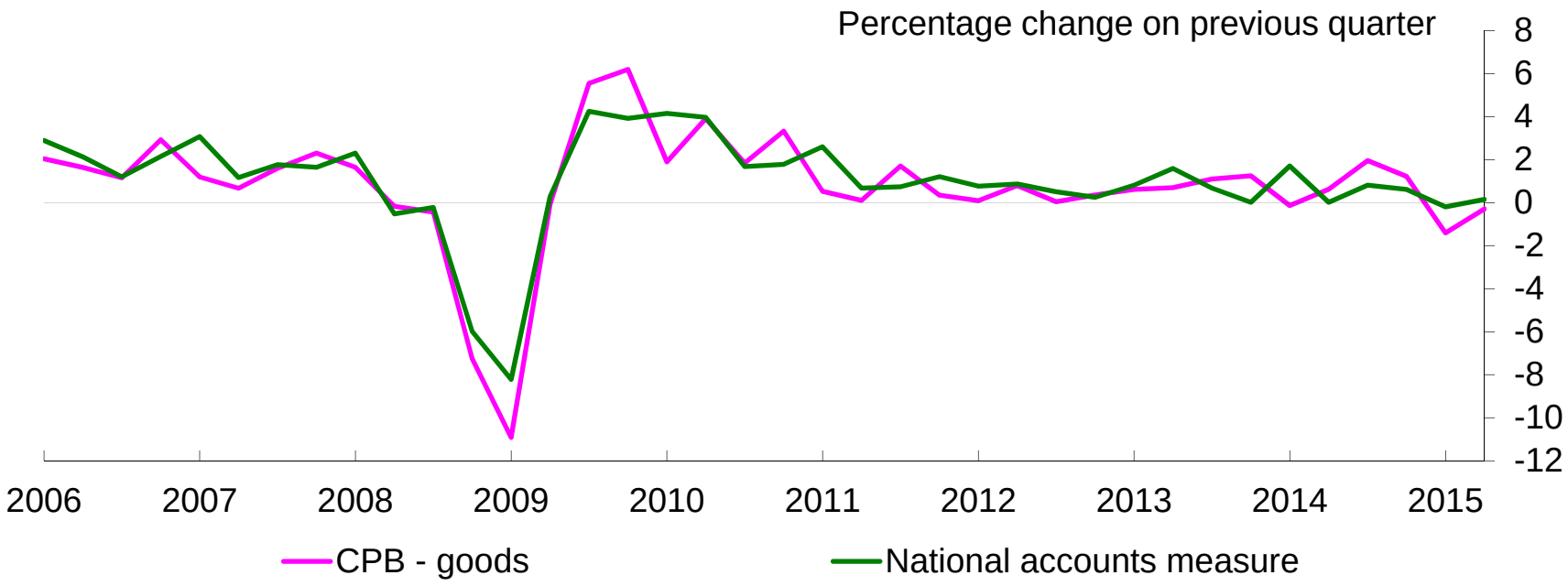
Indicators of global activity



CPB world trade in goods



Measures of world trade



Key messages

- Our central view is that world growth will pick up a little in 2015 H2.
- But we have little evidence beyond August, so remain very uncertain about Q4 growth.

Summary

- IMF Oct. WEO points to a pick-up in EME (ex. China) growth in 2015 H2, but prospects do appear to have deteriorated;
- Chinese GDP growth expected to pick up a little in Q3; FX reserves appear sufficient to offset continued capital outflows;
- US and EA growth expected to be fairly stable in 2015 H2;
- Global indicators point to a pick up in growth in Q3, although have tended to over-predict recently;
- Trade weakness seems to be unwinding and is consistent with observed rates of global growth.

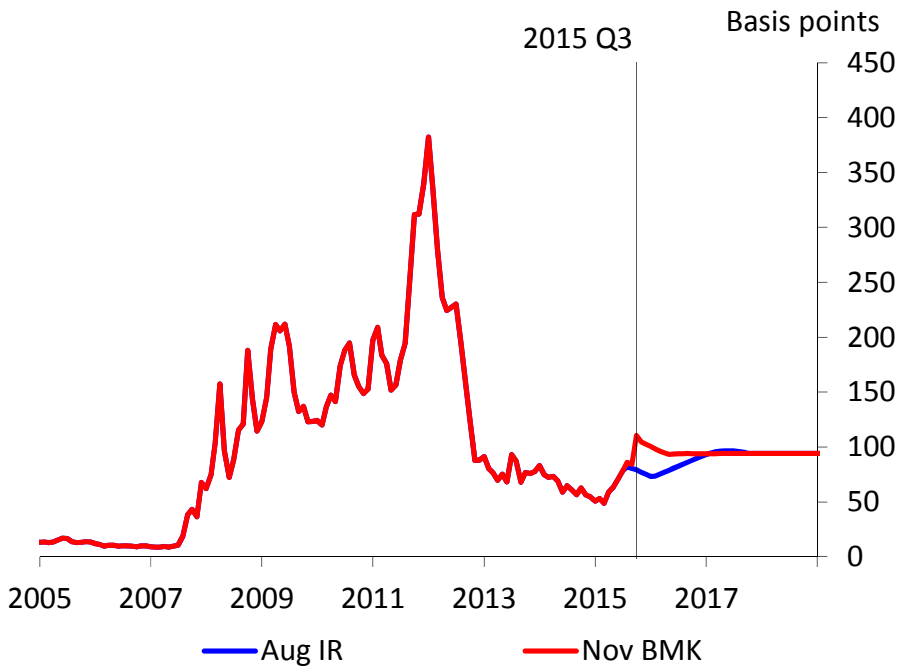
End

3: Money, Credit and Nominal Trends

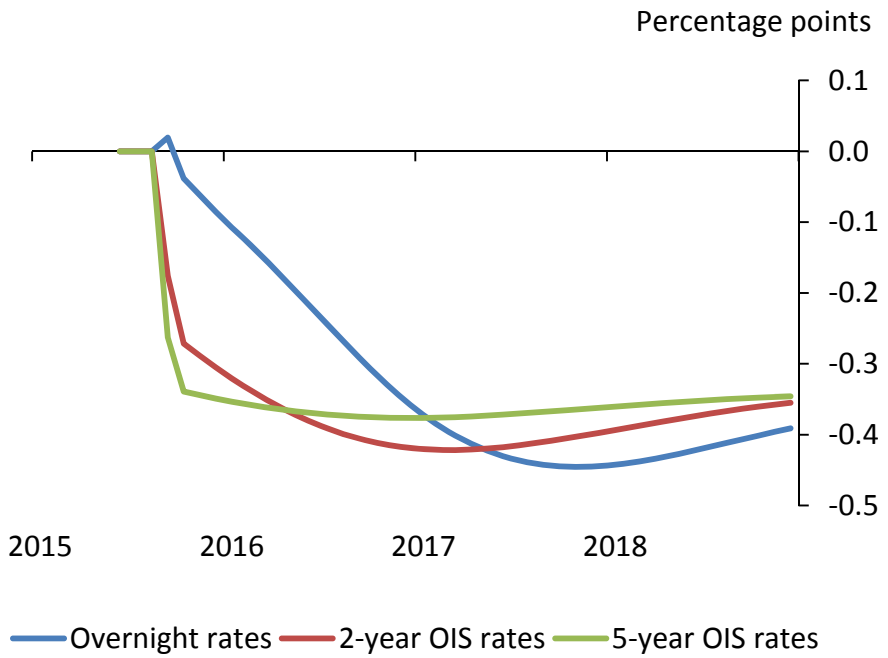
MONEY, CREDIT AND NOMINAL TRENDS
October 2015

- Outlook for the UK mortgage market
- Corporate credit conditions
- Update on inflation expectations

UK banks' all-in funding spreads

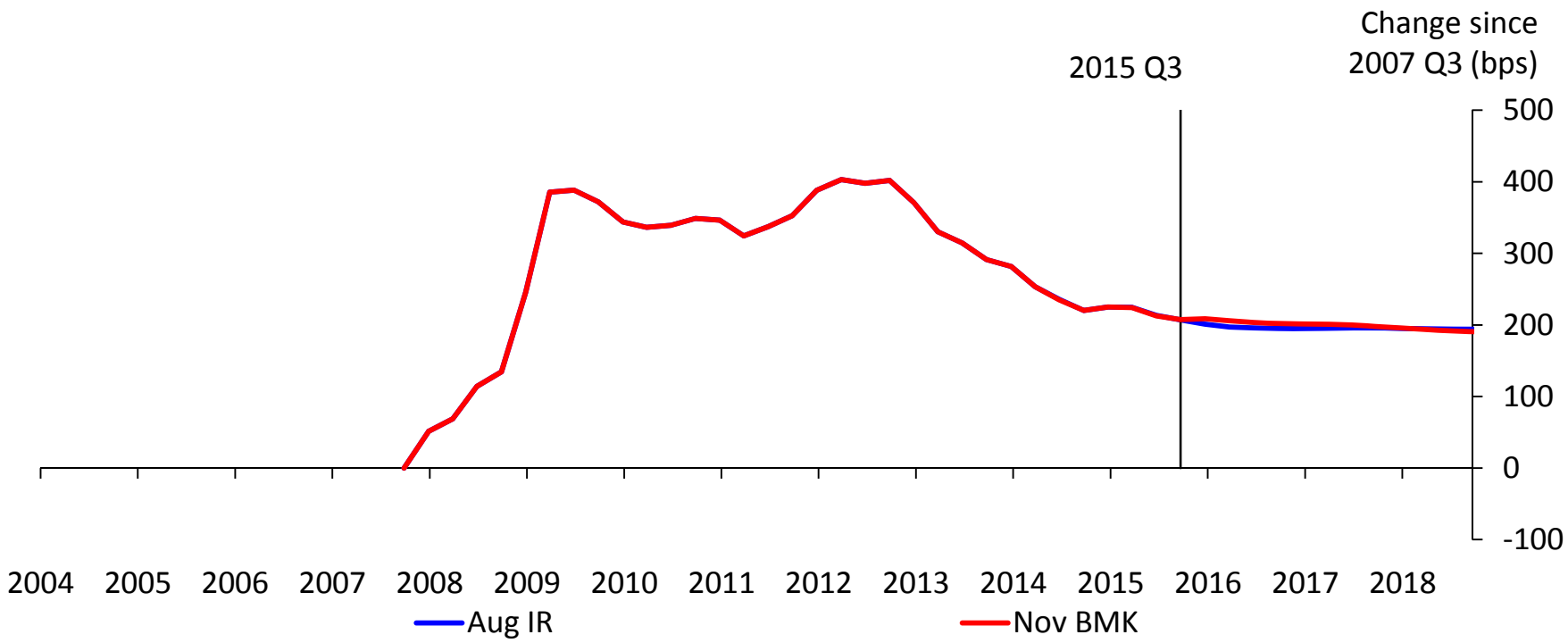


Change in forward OIS curves since Aug *IR*



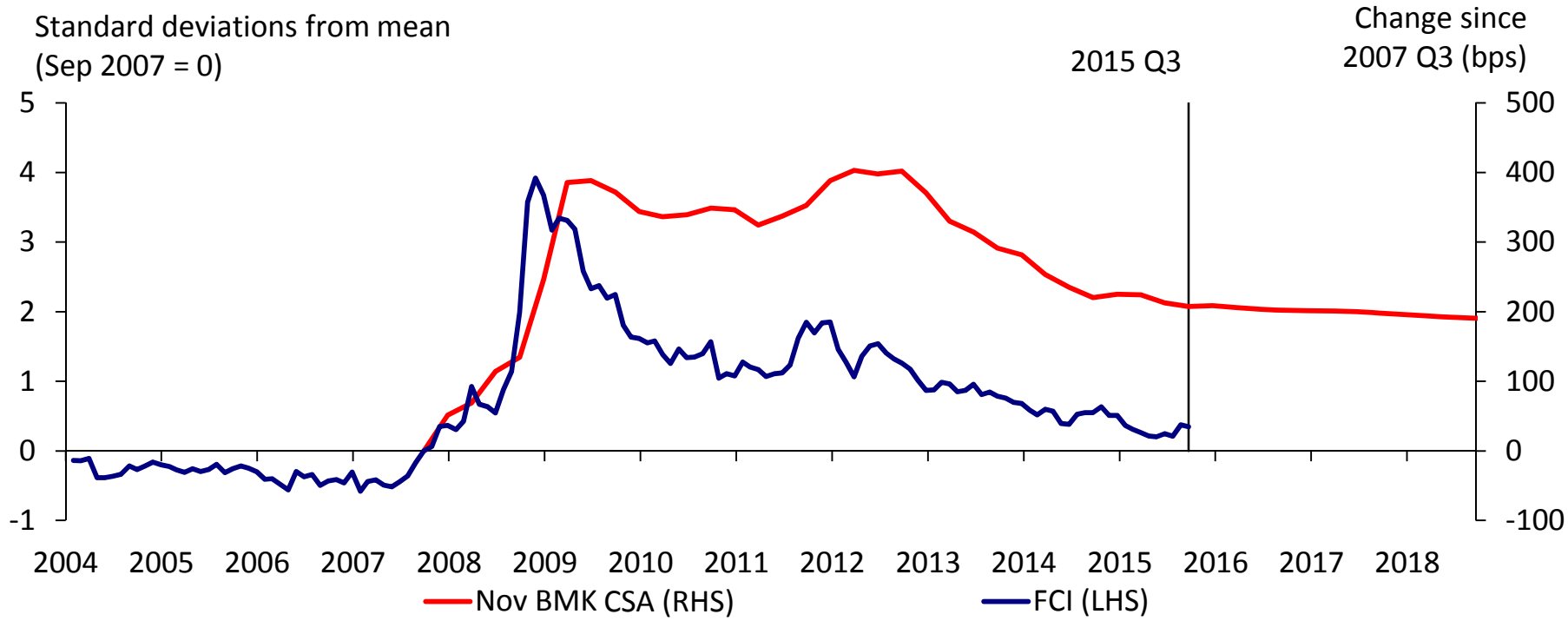
- UK banks' all-in funding spreads have increased around 20bps since we closed the August *IR* forecast, over half of which reflects higher unsecured debt spreads

Aggregate Credit Spread Adjustment (CSA)



- Outlook for bank lending conditions facing the UK real economy overall broadly unchanged from Aug *IR*

Aggregate Credit Spread Adjustment (CSA) and Kapetanios, Price & Young Financial Conditions Index (FCI)



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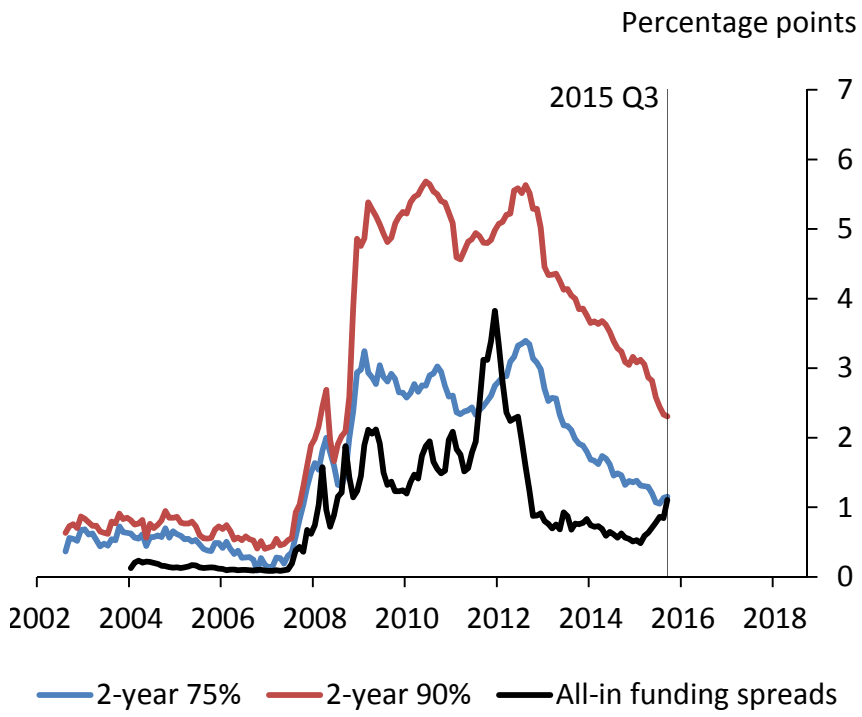
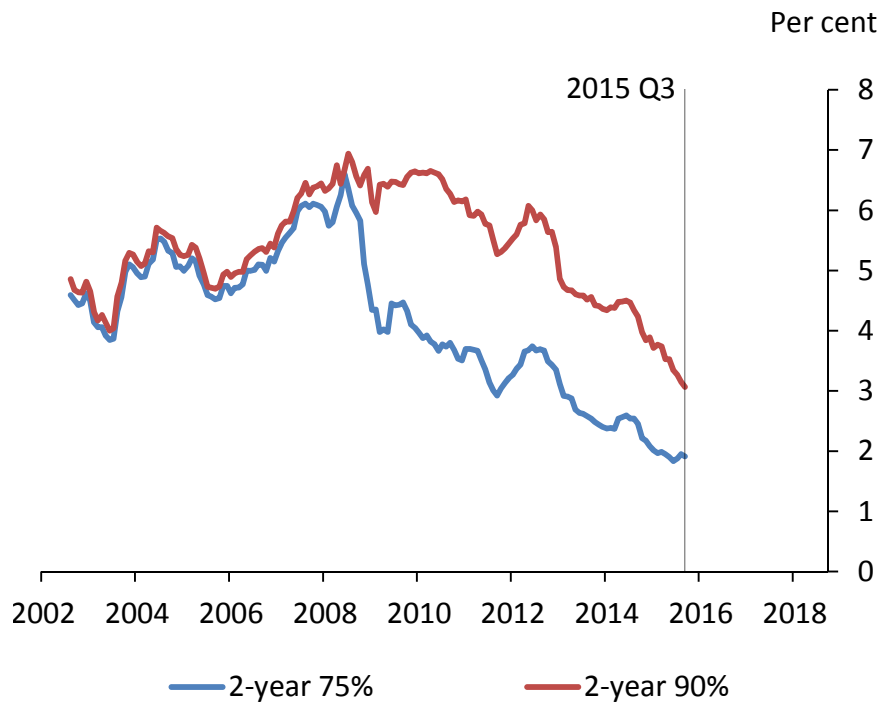
- **Outlook for the UK mortgage market**
- Corporate credit conditions
- Update on inflation expectations

High and low LTV mortgage spreads over OIS

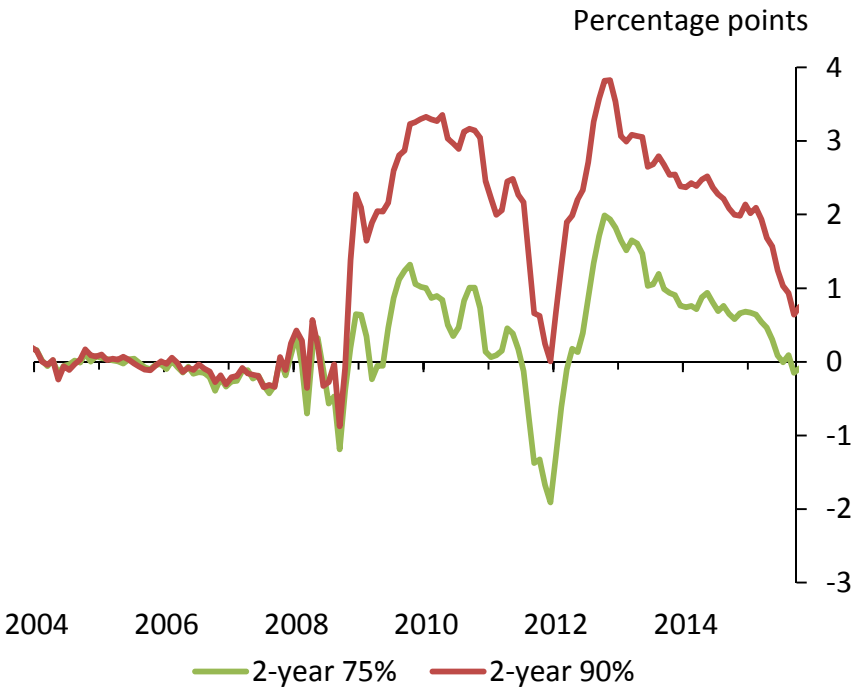


High and low LTV mortgage rates



- Agents cite intense competition, with PRA colleagues perceiving some intensification from spring 2015.
- Lenders share this sense, and attribute it in part to the growing role of broker intermediation.
- A plausible central case is thought to involve only a limited further compression of low LTV spreads, with competition spilling over into higher margin segments.
-
-

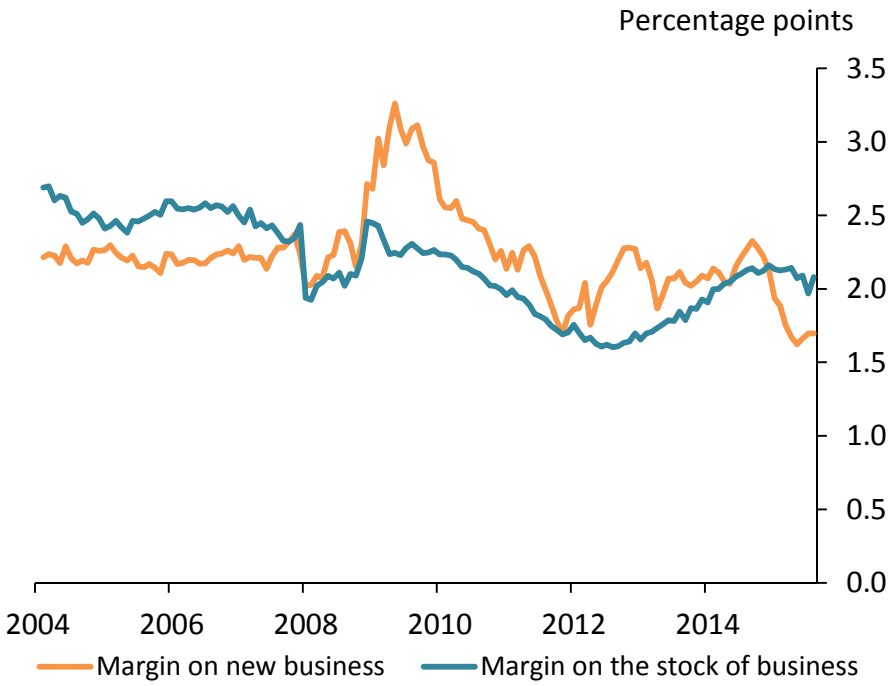
Margins on new 2-year mortgages relative to 2004-05 average (CSA)*



*Quoted mortgage rate minus funding costs, expected losses and capital costs

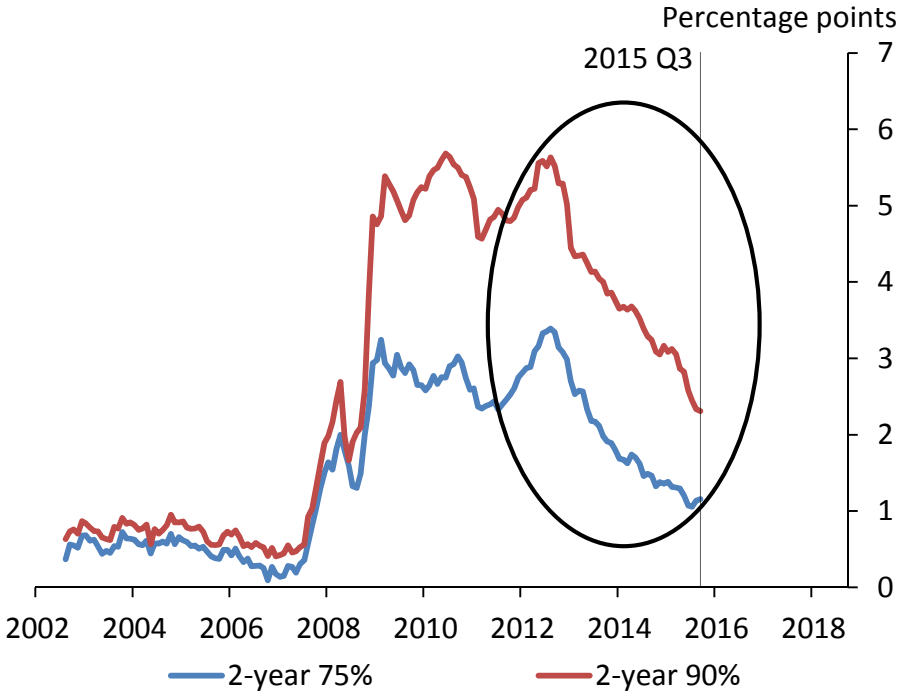
Effective margins on B6 new mortgages and stock **

Individual Institutions Data

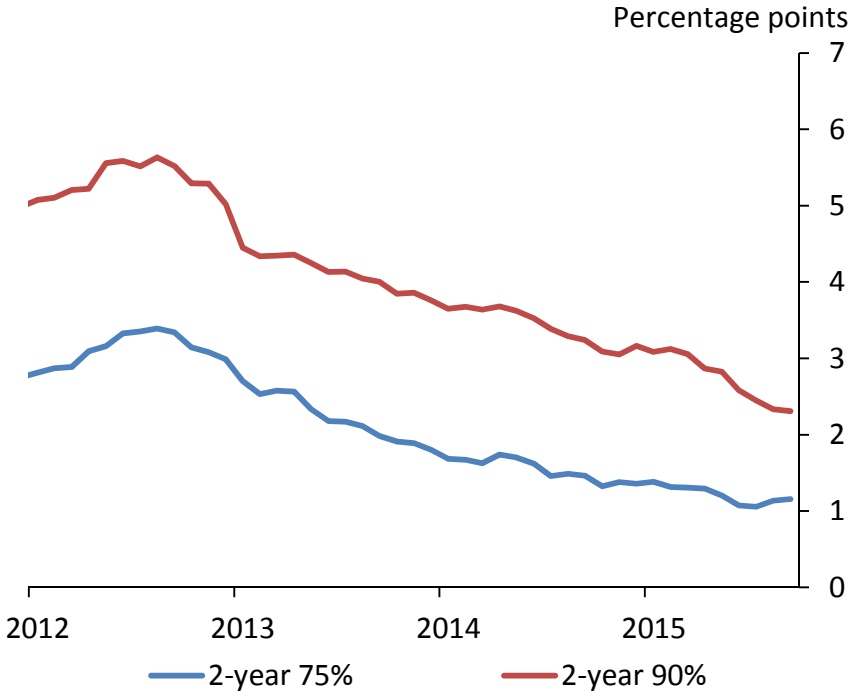


** Effective mortgage rate minus effective deposit rate

High and low LTV mortgage spreads over OIS



High and low LTV mortgage spreads over OIS



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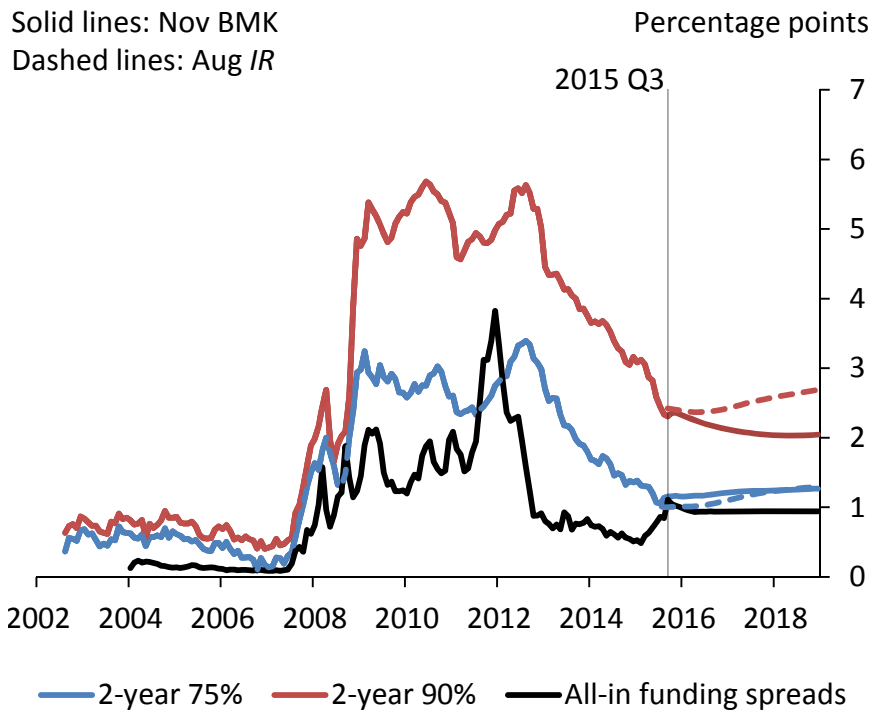
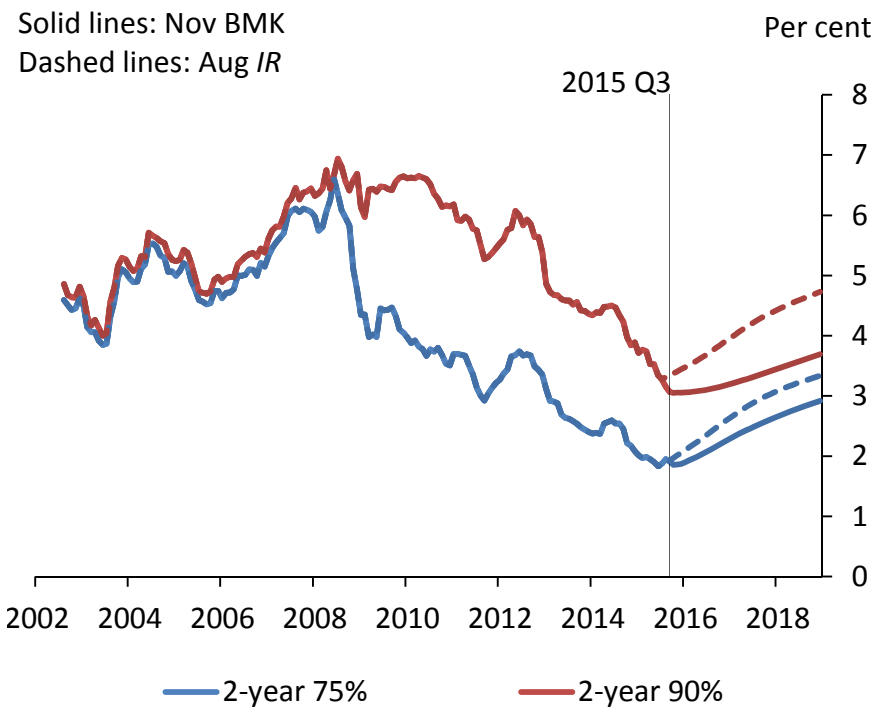
High and low LTV mortgage spreads over OIS swaps



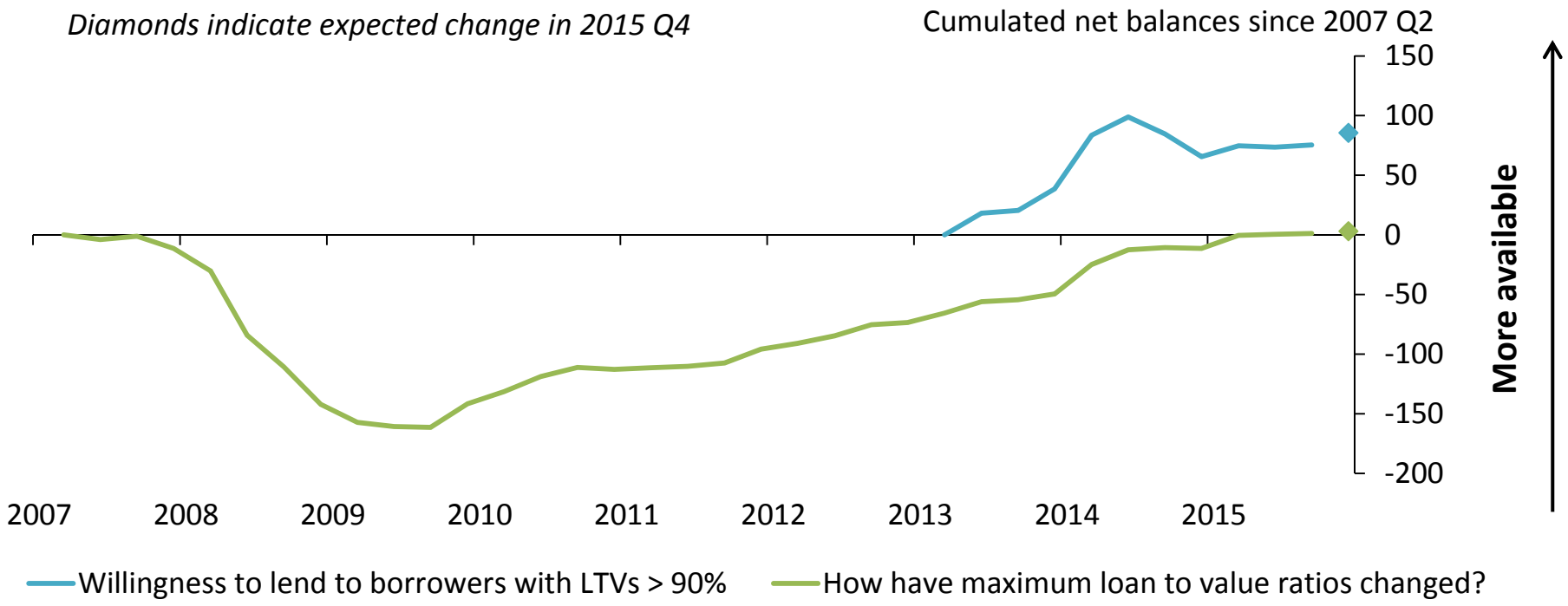
High and low LTV mortgage rates



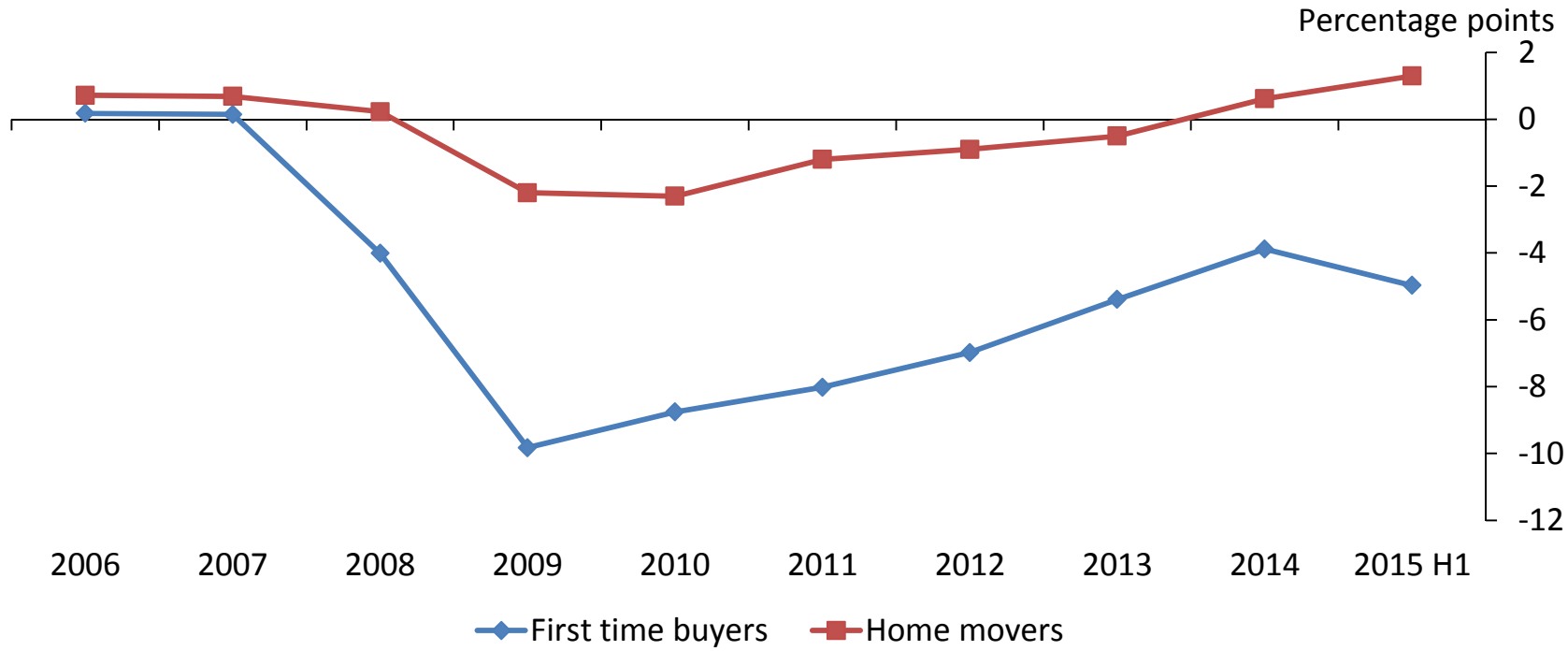
[redacted]

- We do not expect spreads on low LTV mortgages to fall much further, though they plausibly could, as competition spills over into higher margin products.
- Spreads on high LTV products expected to fall further.
- A key question is what further falls in high LTV spreads might mean for the availability and volume of secured lending.

Cumulated changes in net balances – *Credit Conditions Survey*

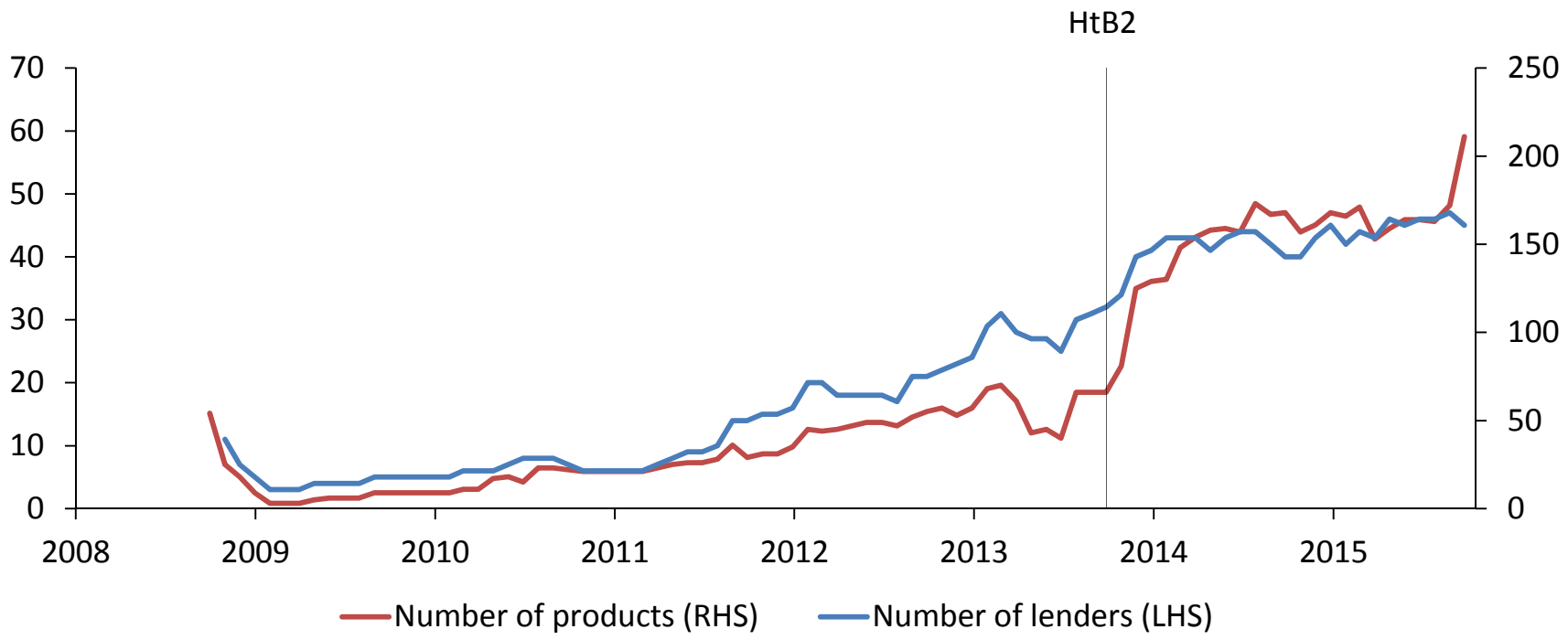


Change in LTV on new mortgages for a given borrower relative to 2005*



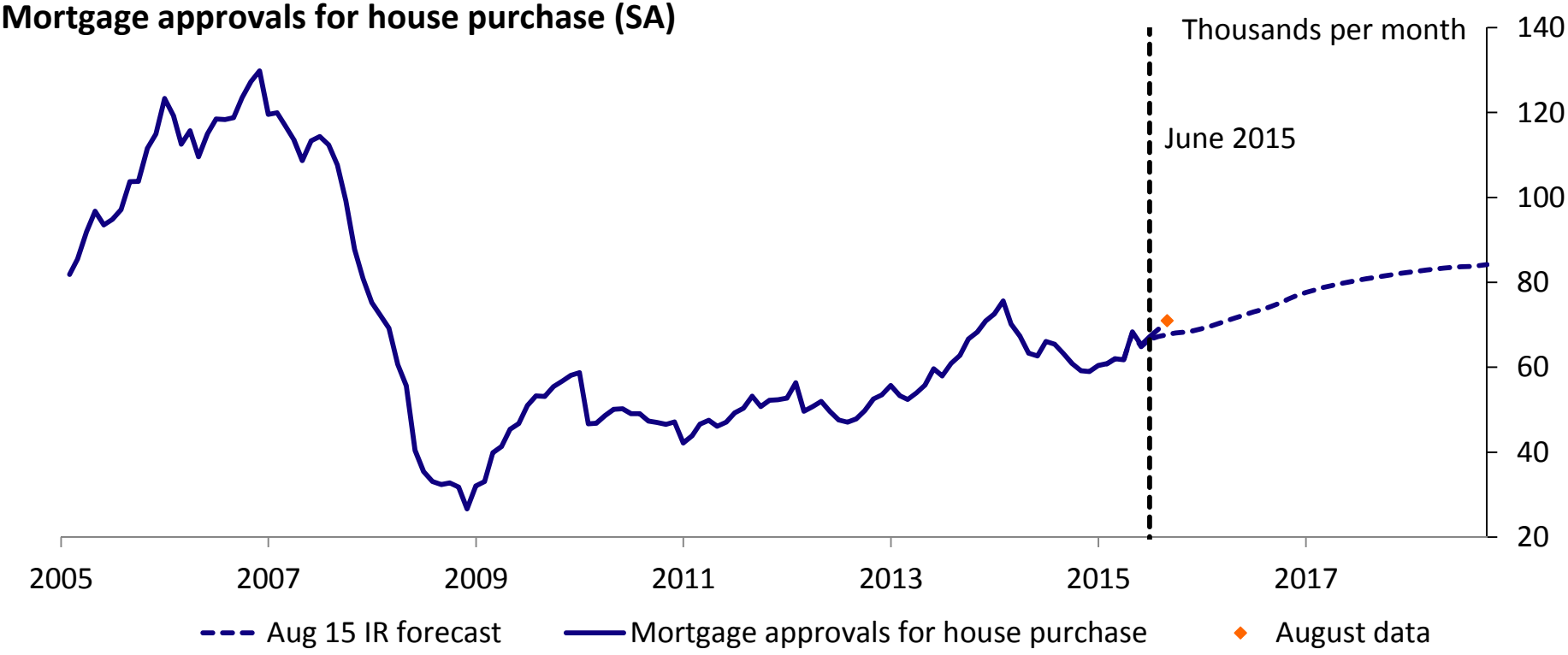
* Controls for gross income, age, property value and region. Uses Product Sales Database.

Number of 95% LTV products and lenders

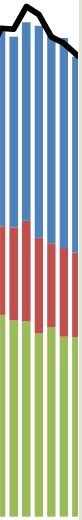


- Nationwide and Santander announced new 95% LTV products outside H2B2

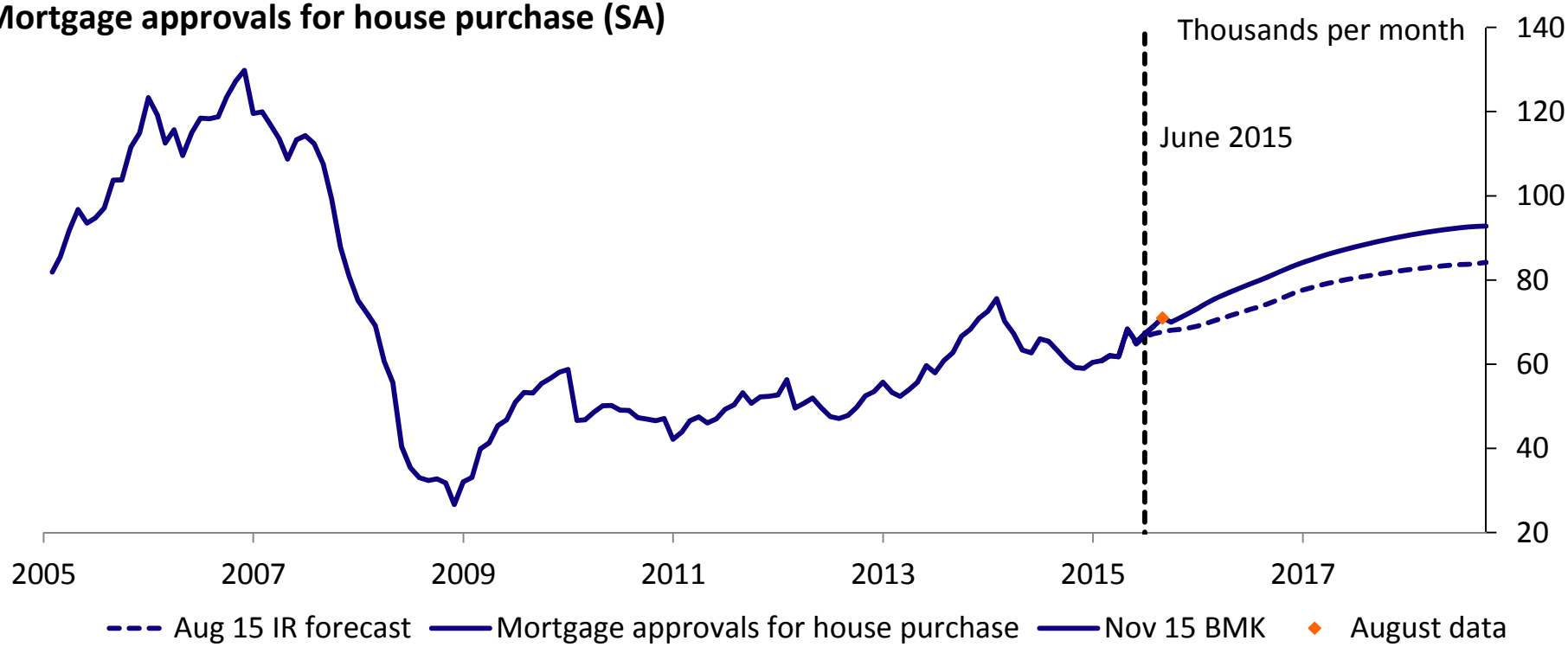
Mortgage approvals for house purchase (SA)



- Mortgage approvals for house purchase were 71,000 in August, up from 69,000 in July.

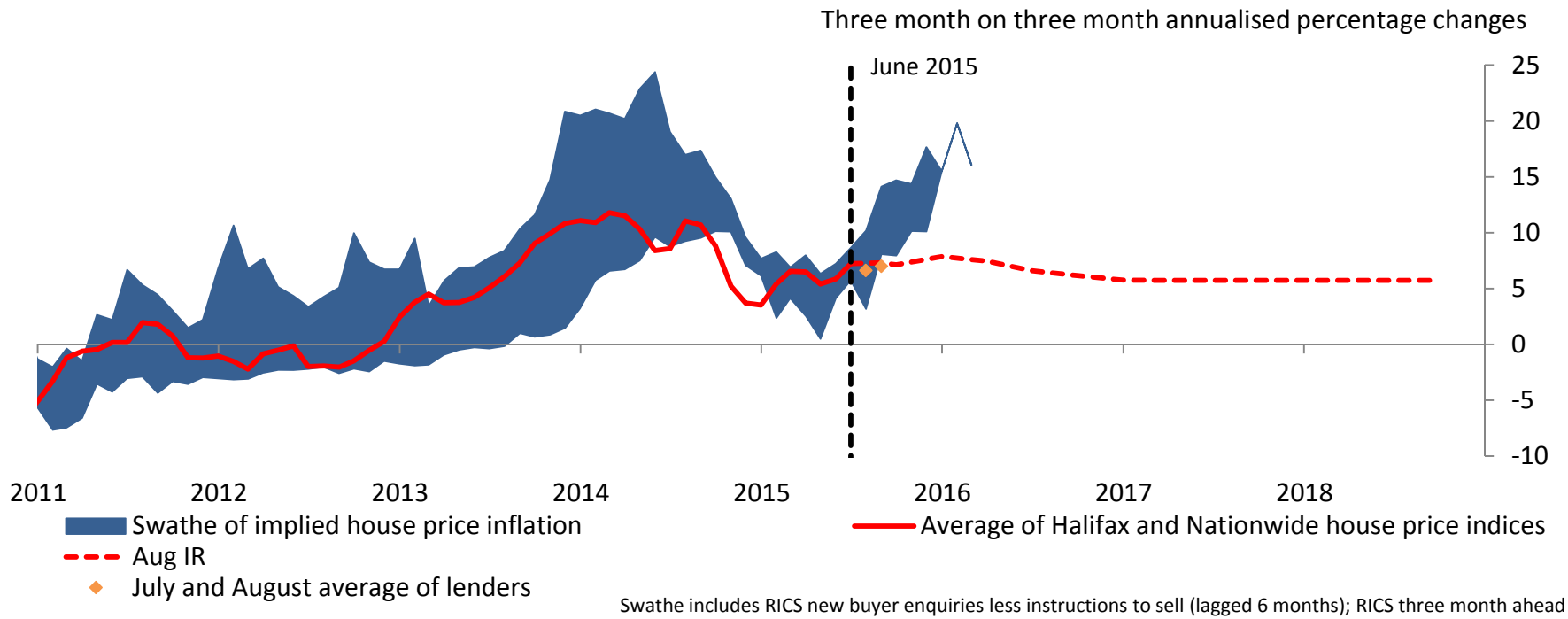


Mortgage approvals for house purchase (SA)



- Approvals still expected to rise gradually in the near-term, and are 6,000 a month higher, on average, over the forecast.

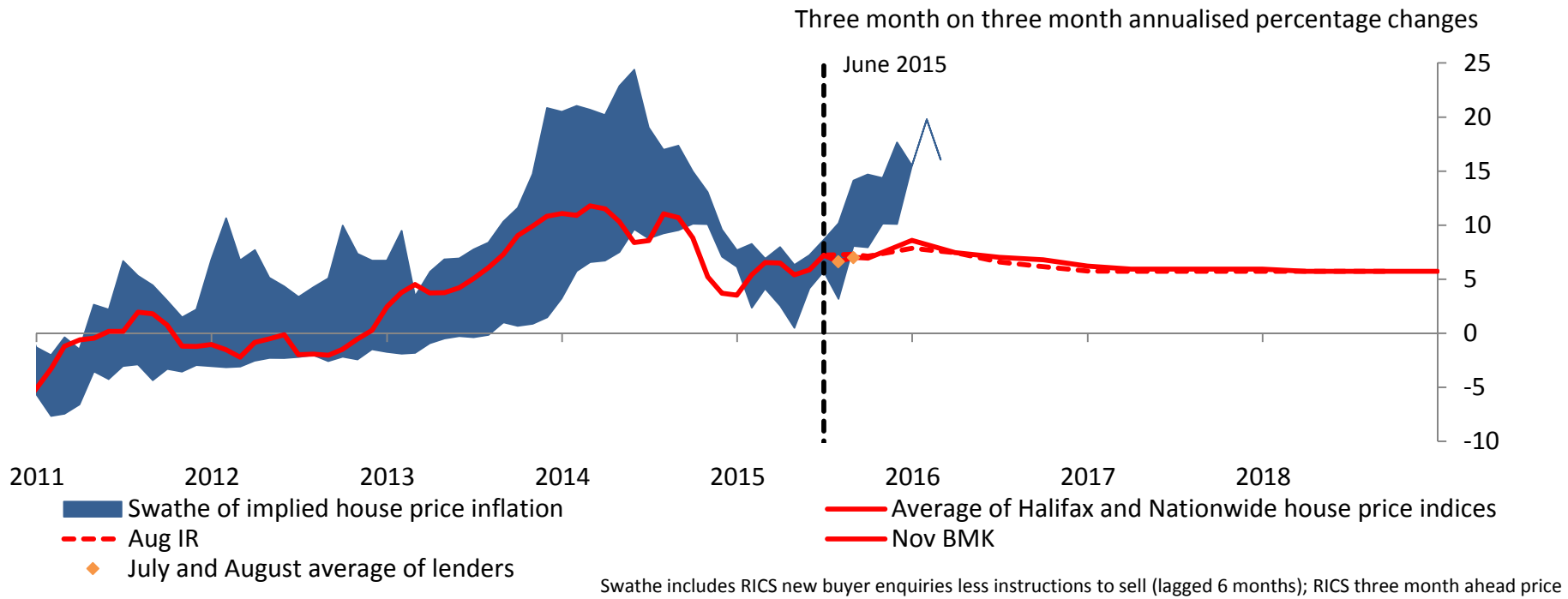
Swathe of leading indicators of house price inflation and house price forecast



Swathe includes RICS new buyer enquiries less instructions to sell (lagged 6 months); RICS three month ahead price expectations (lagged 3 months); RICS sales to stock ratio (lagged 3 months); and a principal component of house prices.

- The average of lenders' indices increased by 1.4% in August, within which Nationwide house price index rose 0.3% and the Halifax index rose 2.7%. The Nationwide index rose by a further 0.5% in September.

Swathe of leading indicators of house price inflation and house price forecast



Swathe includes RICS new buyer enquiries less instructions to sell (lagged 6 months); RICS three month ahead price expectations (lagged 3 months); RICS sales to stock ratio (lagged 3 months); and a principal component of house prices.

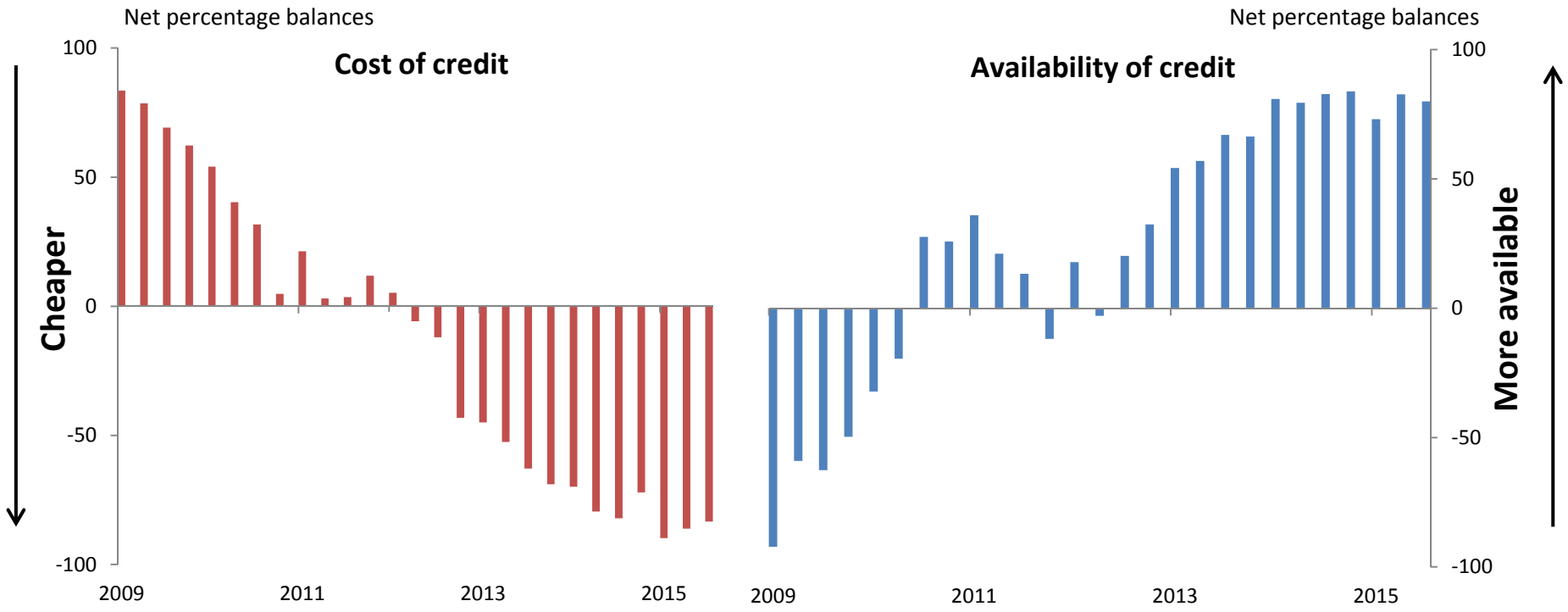
- The level of house prices is around 0.7% higher than the August IR in 2018.

- Outlook for the UK mortgage market
- **Corporate credit conditions**
- Update on inflation expectations

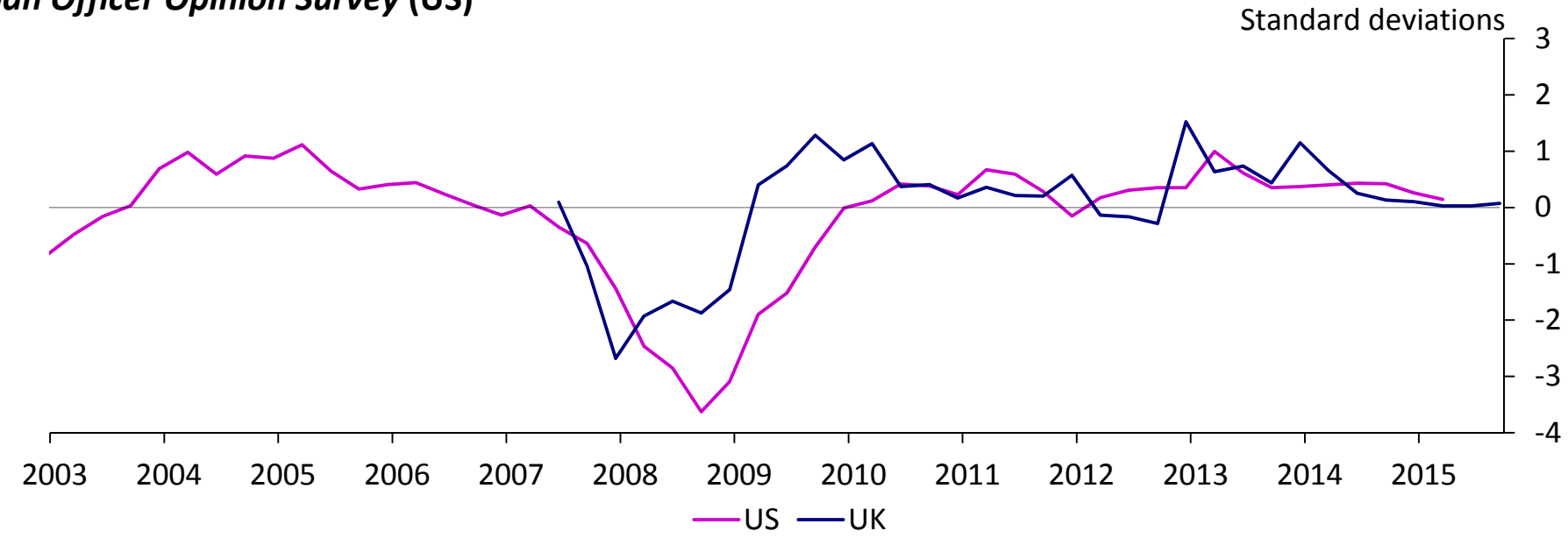
PNFCs net external debt raised as % of nominal GDP, annual average

* 2015 data scaled to be comparable to annual figures

Deloitte CFO survey: cost and availability of credit

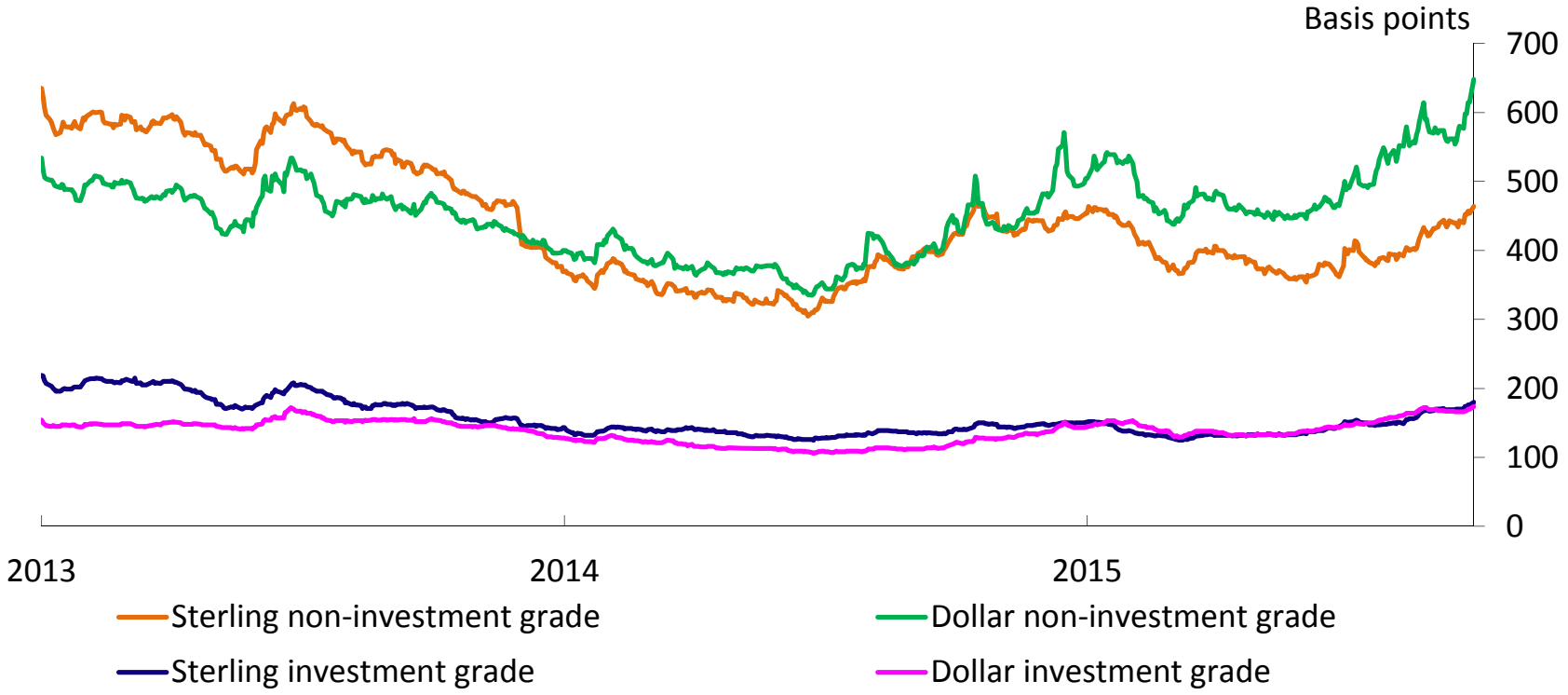


Changes in net balances of corporate credit availability in *Credit Conditions Survey* (UK), *Senior Loan Officer Opinion Survey* (US)



Bank of England *Credit Conditions Survey* asks *'How has the availability of credit provided to the corporate sector overall changed?'*. Federal Reserve *Senior Loan Officer Opinion Survey* asks *'Over the past three months, how have your bank's credit standards for approving applications for C&I loans or credit lines—other than those to be used to finance mergers and acquisitions—to large and middle-market firms and to small firms changed?'*. US data have been inverted so they are comparable to the UK.

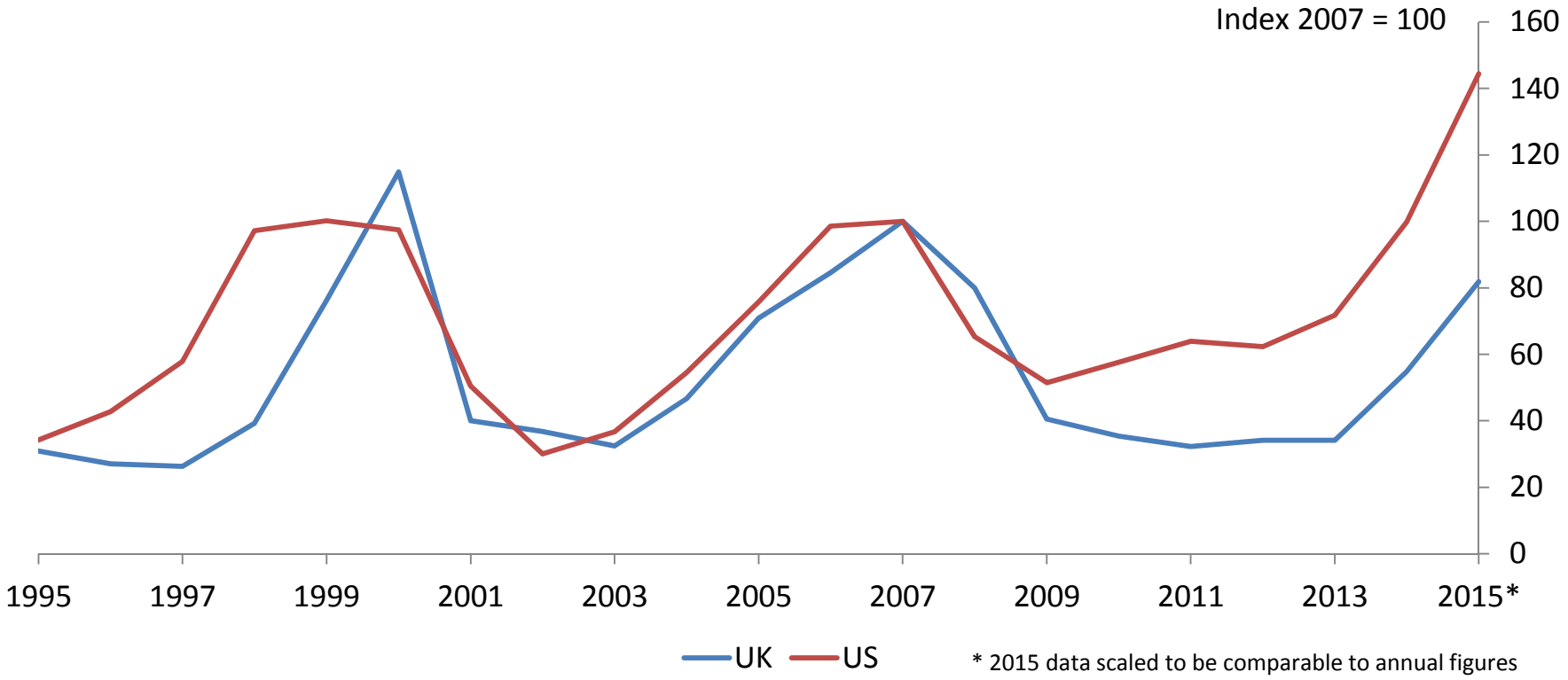
Investment and non-investment grade corporate bond spreads by currency



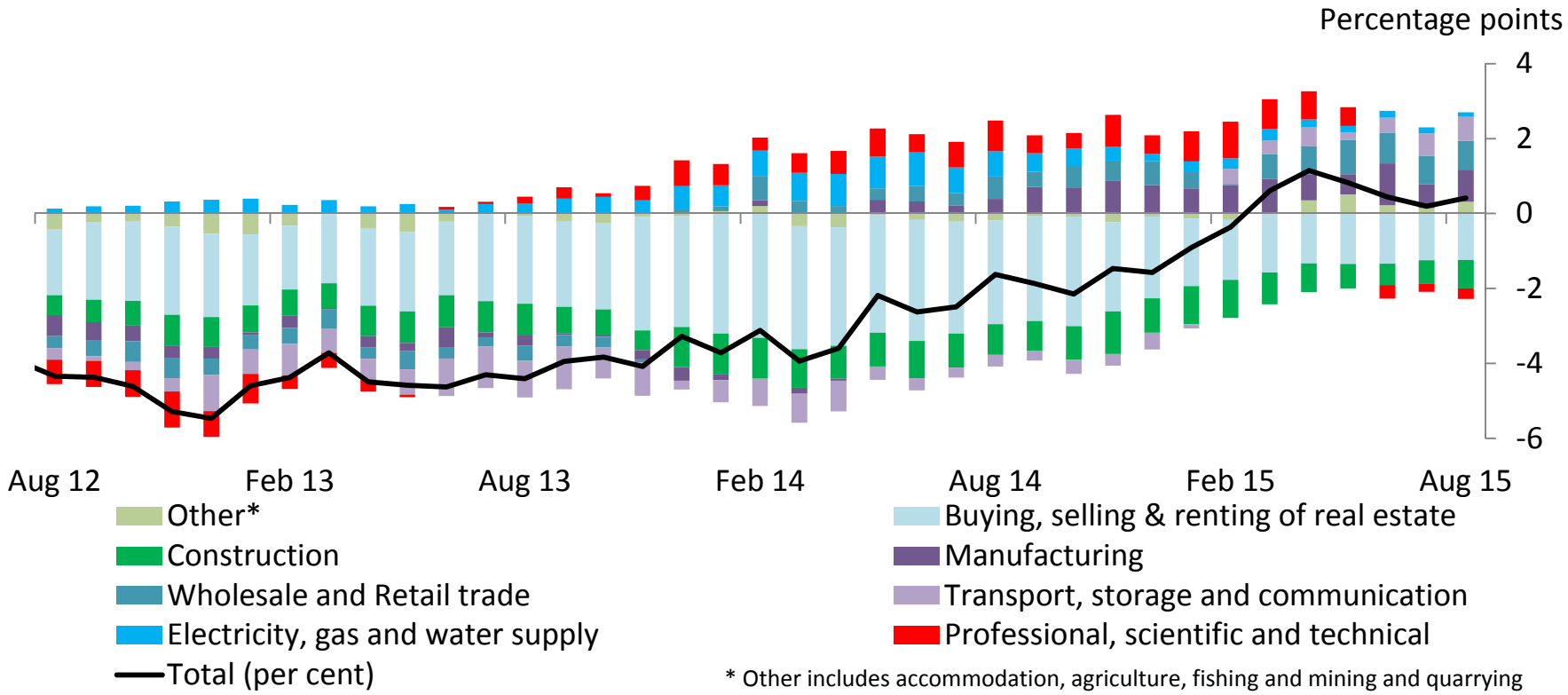
PNFCs net external finance raised as % of nominal GDP, annual average

* 2015 data scaled to be comparable to annual figures

Annual value of Mergers & Acquisition (M&A) activity in the UK and US, Dealogic



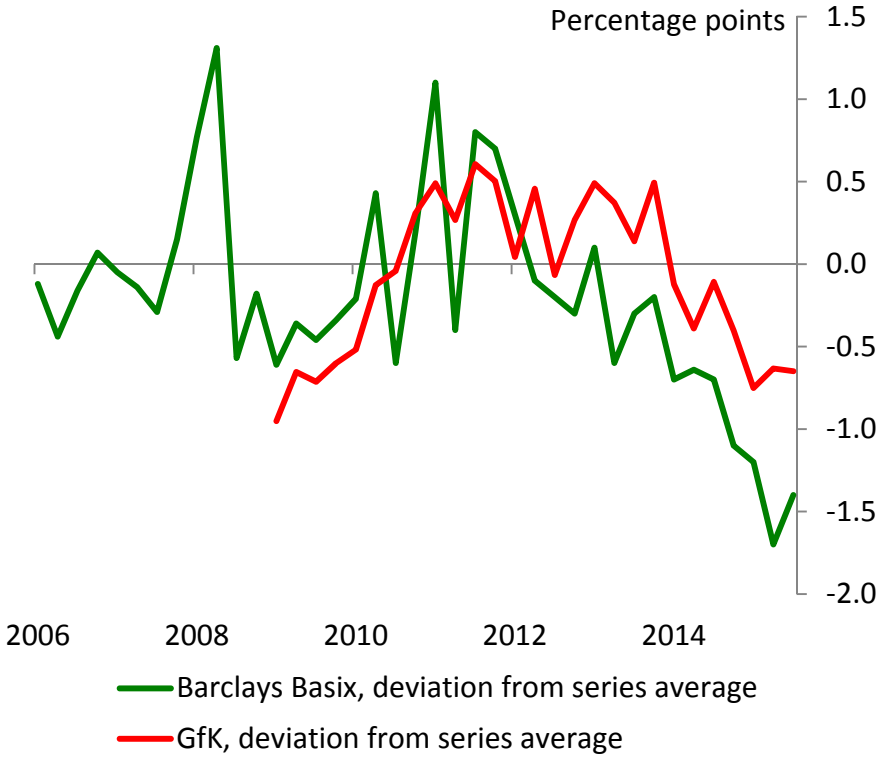
Contributions to 12m growth in lending to businesses, by industry, not seasonally adjusted



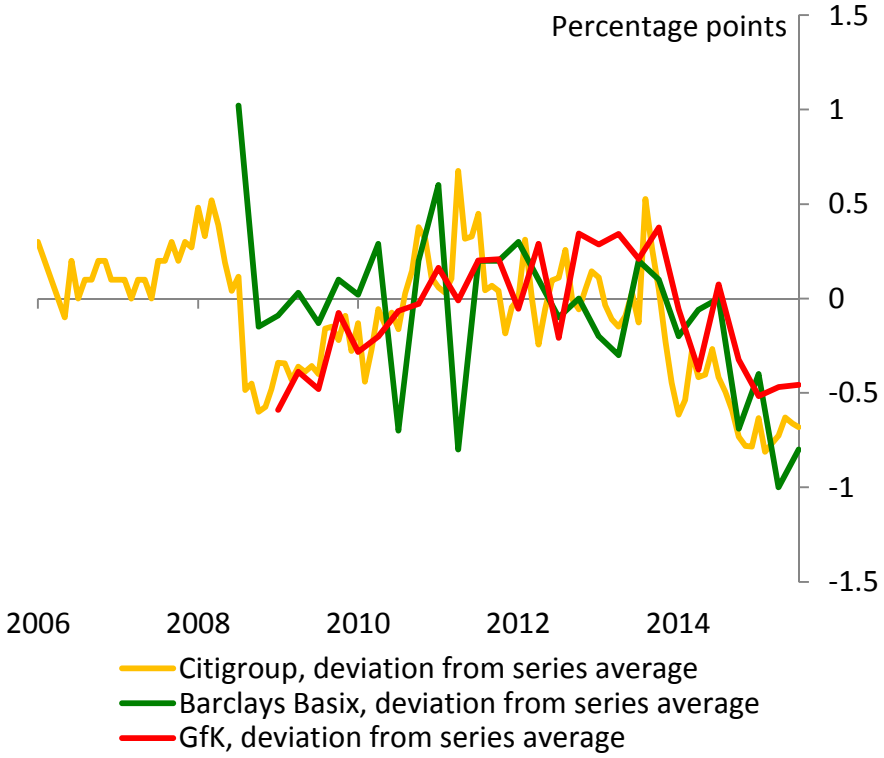
* Other includes accommodation, agriculture, fishing and mining and quarrying

- Outlook for the UK mortgage market
- Corporate credit conditions
- **Update on inflation expectations**

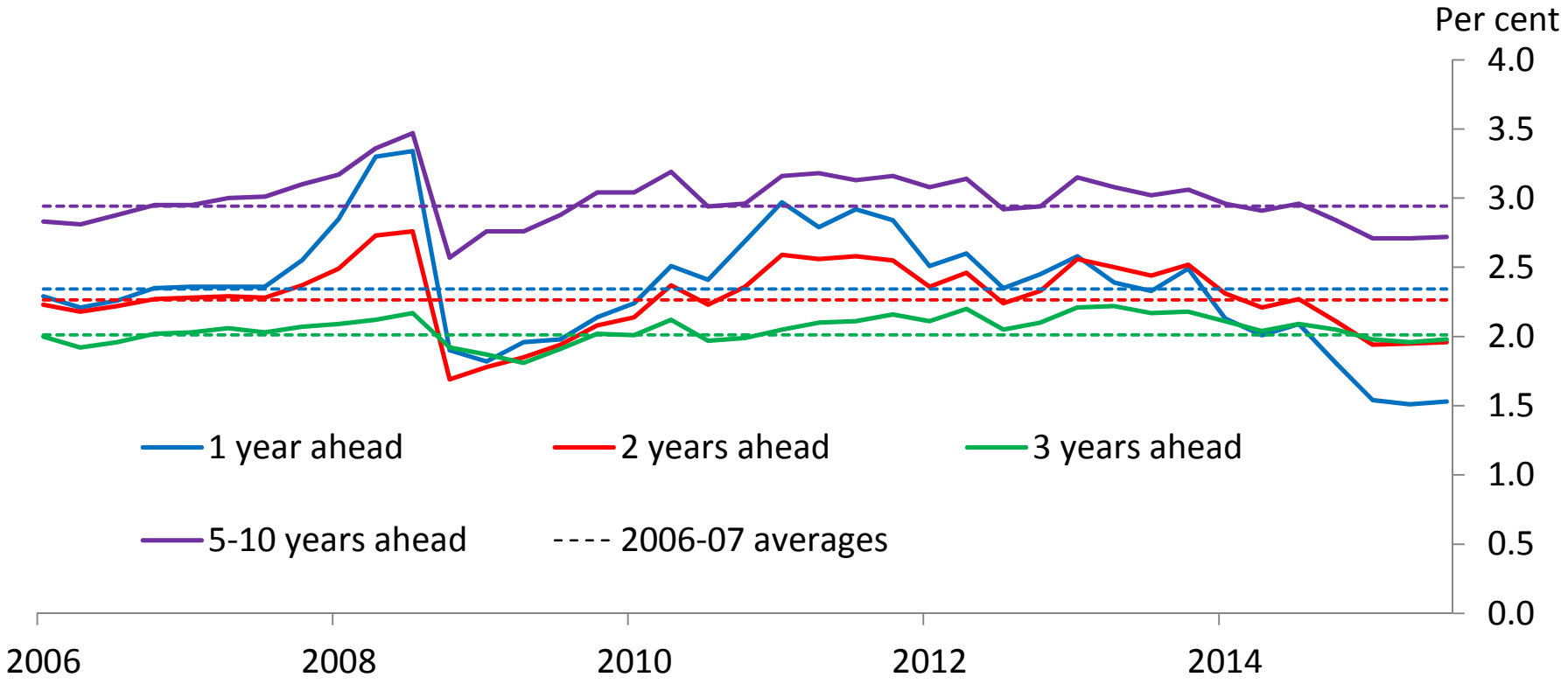
Household inflation expectations 2 years ahead

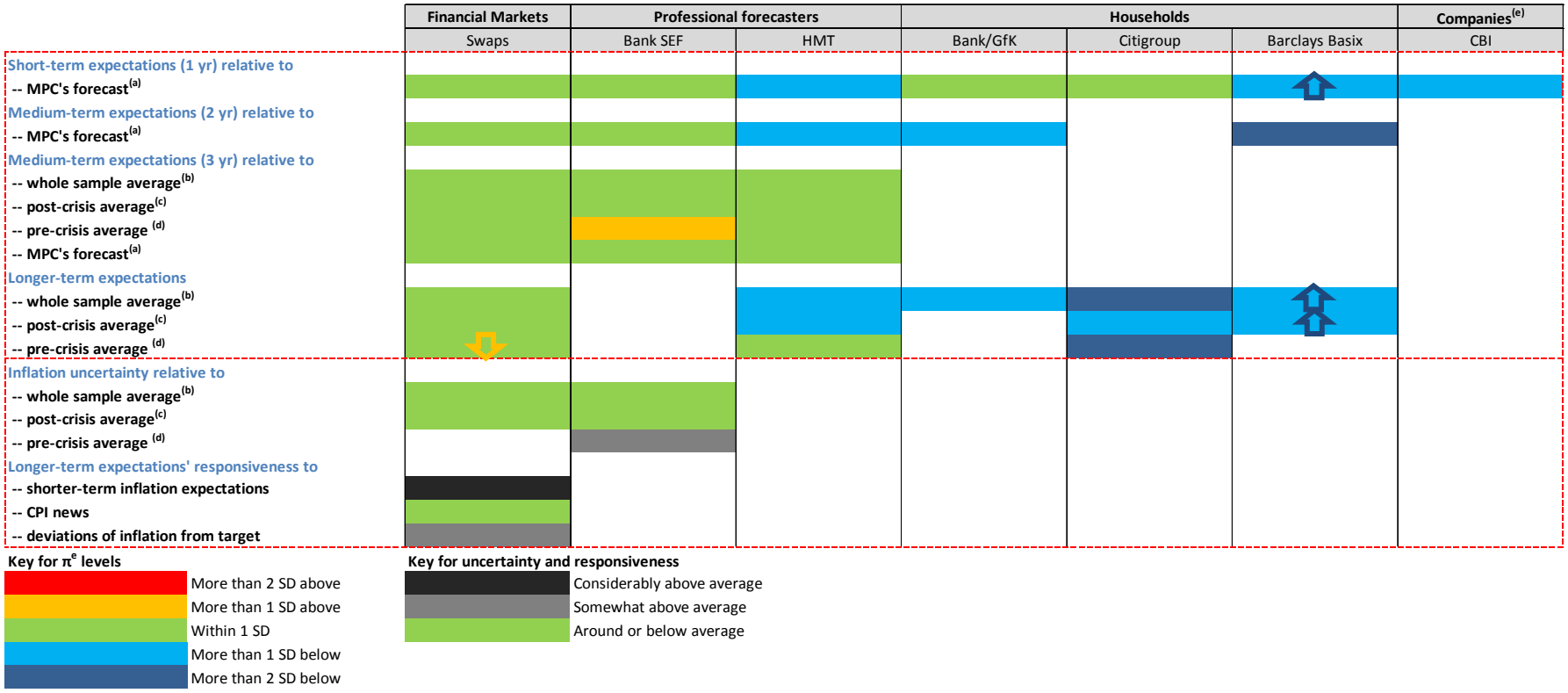


Household inflation expectations 5 years ahead



Inflation expectations summary measure





- Arrows show changes since September MPC

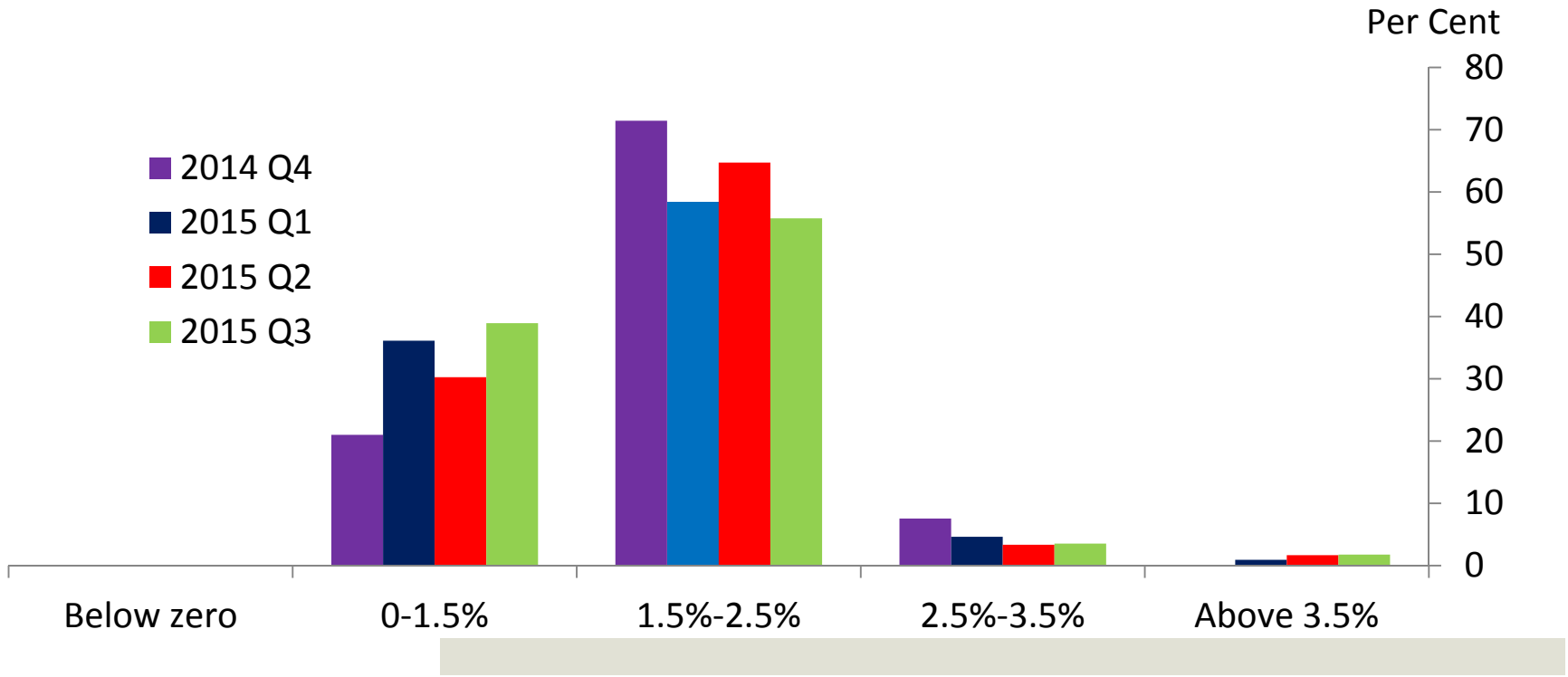
[redacted]

MASD heatmap over time

Sector	2008		2009				2010				2011				2012				2013				2014				2015		
	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3
Professional Forecasters																													
Households																													
Financial Markets																													
Corporates																													

[redacted]

Deloitte CFO survey, Distribution of respondents' 2 year ahead inflation expectations



- **Competition amongst lenders in UK mortgage market remains intense, but with pricing pressure spreading beyond low LTV products.**
- **Credit conditions for UK companies continue to improve.**
- **‘As you were’ on inflation expectations.**

4: Supply, Costs and Prices

Supply, Costs & Prices

30 September 2015

Structural Economic Analysis Division

Agenda

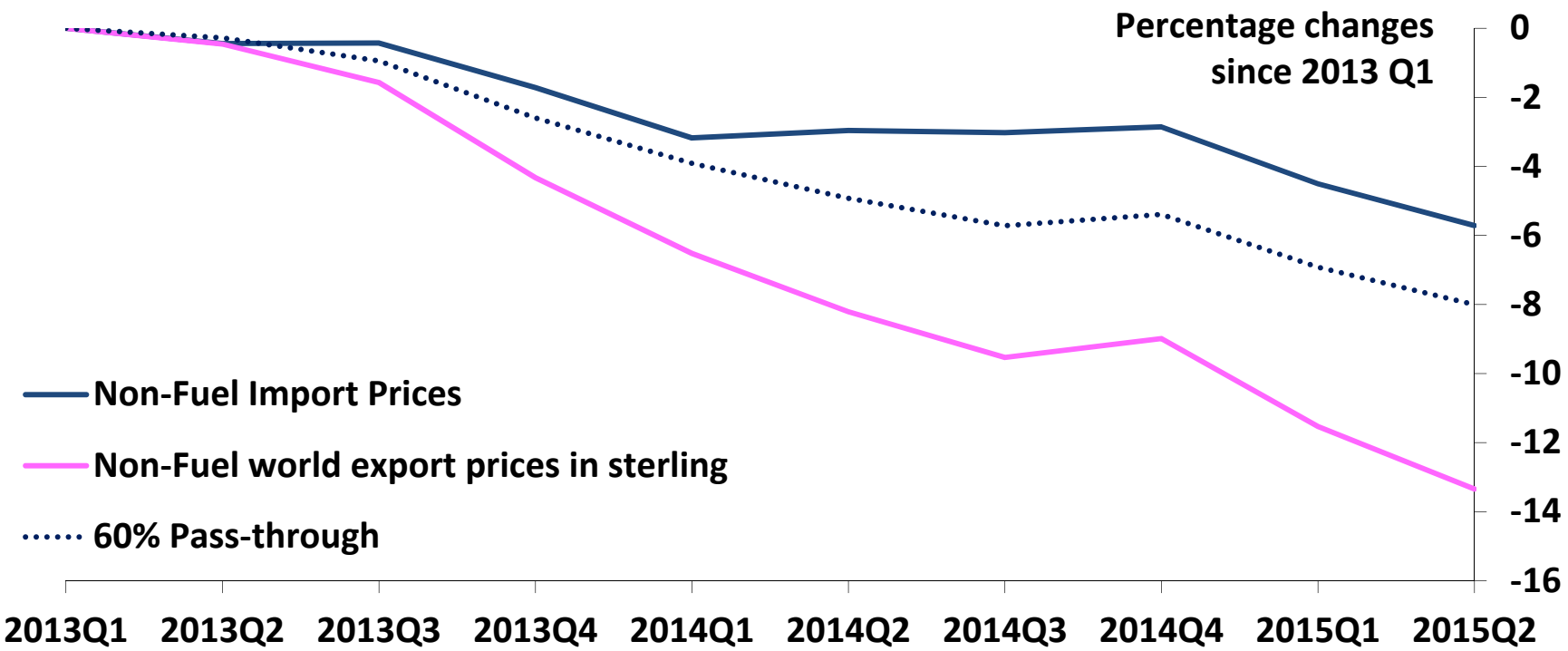
- **What have we learned about exchange rate pass-through?**

- **Where is the balance of risks for our assumptions on equilibrium unemployment?**

Exchange rate pass-through

- for more information.

Sterling world export prices and UK import prices

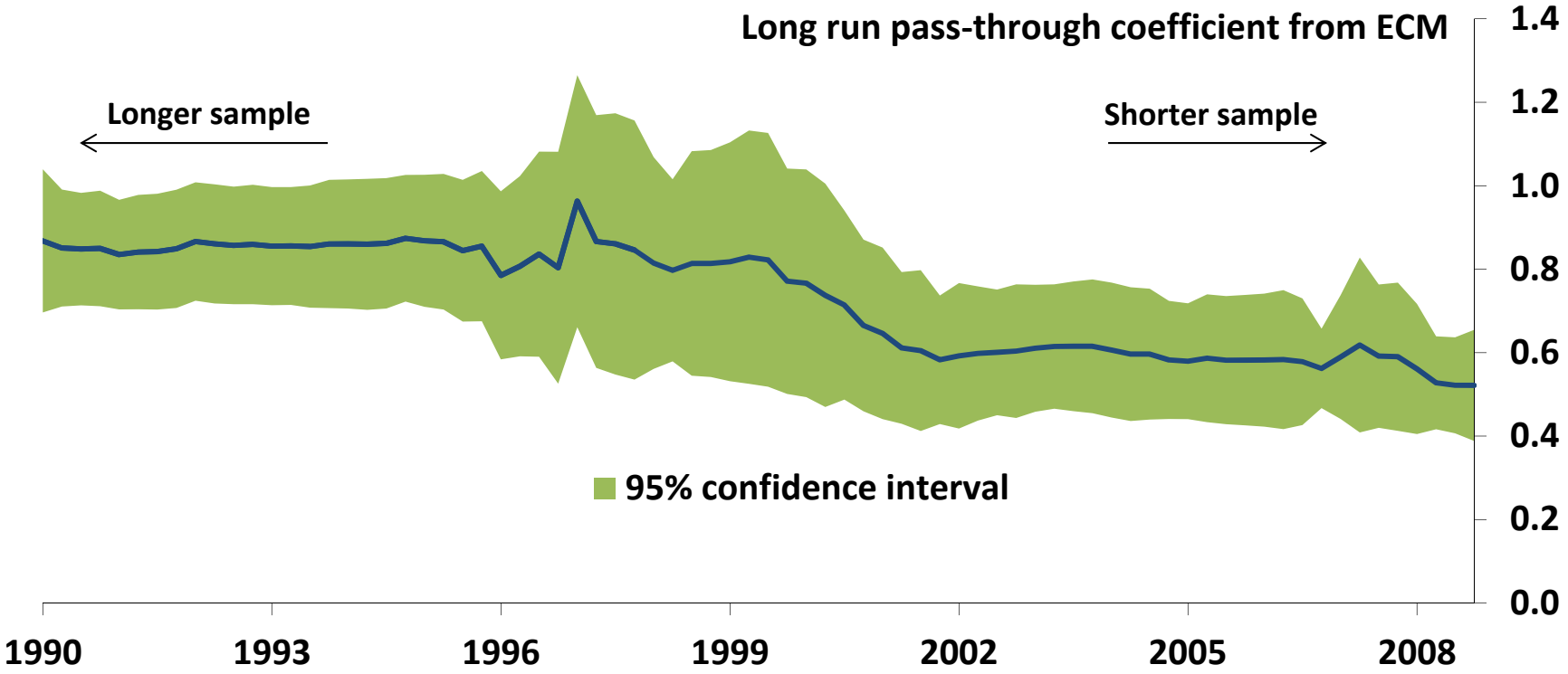


- **Import prices have fallen less than would be expected given the appreciation of sterling.**

Literature on exchange rate pass-through

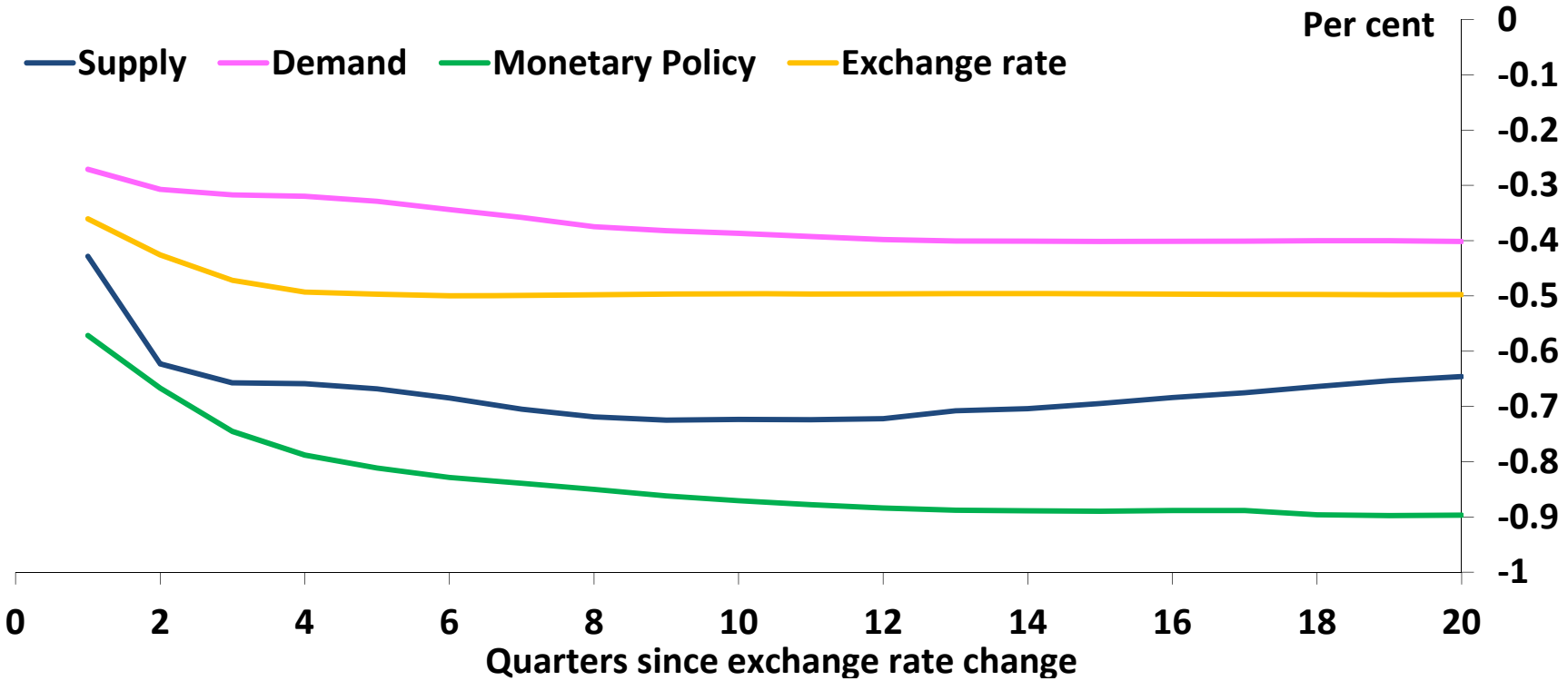
- **Consistent finding of incomplete pass-through to import prices.**
- **Campa & Goldberg (2005) find average pass-through of 64% across 23 advanced economies.**
- **Potential explanations:**
  - **Pricing to market (margins vary to protect market share).**
  - **Distribution costs less affected by exchange rates.**
  - **Offsetting changes in exporters' input costs from exchange rate moves.**
- **for more information.**

Backward recursive estimates of long run pass-through



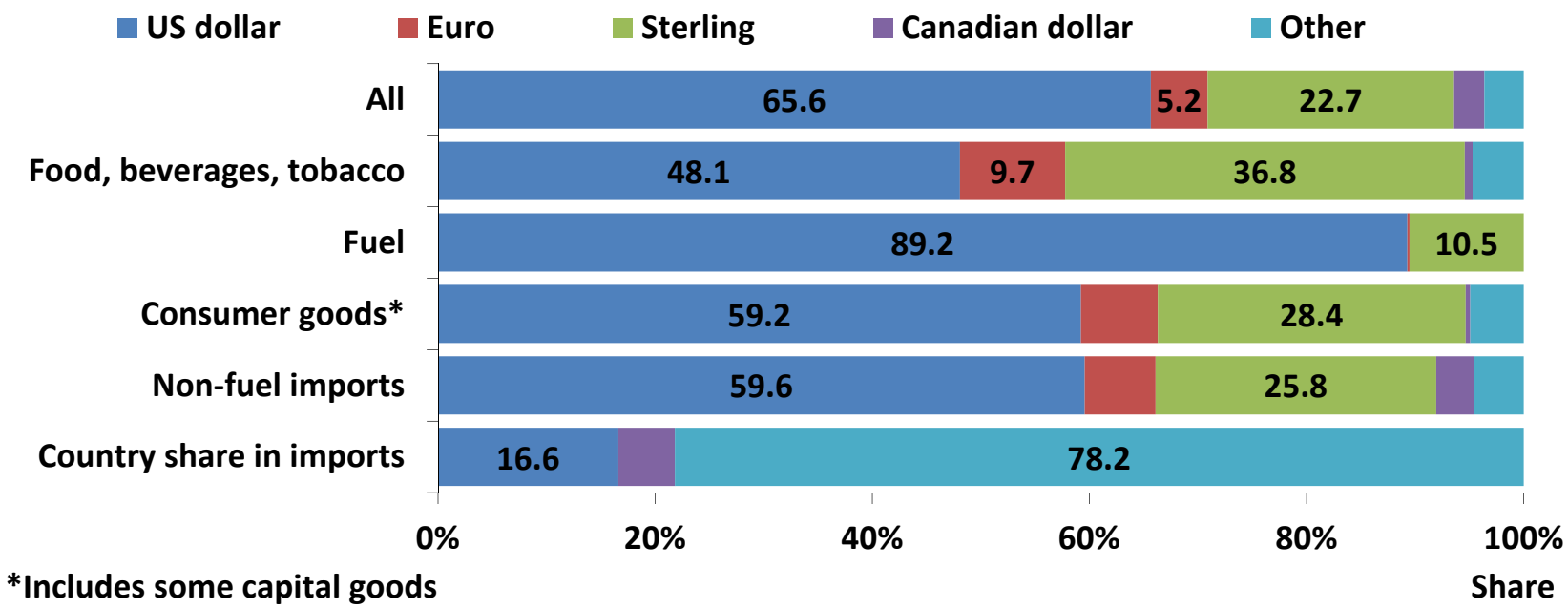
- **Data issues for import prices affect longer sample periods. Post-2001 estimates fairly stable at 0.6.**

Pass-through to import prices in SVAR from 1% appreciation by type of shock



- **The source of the shock to exchange rates is likely to affect pass-through.**

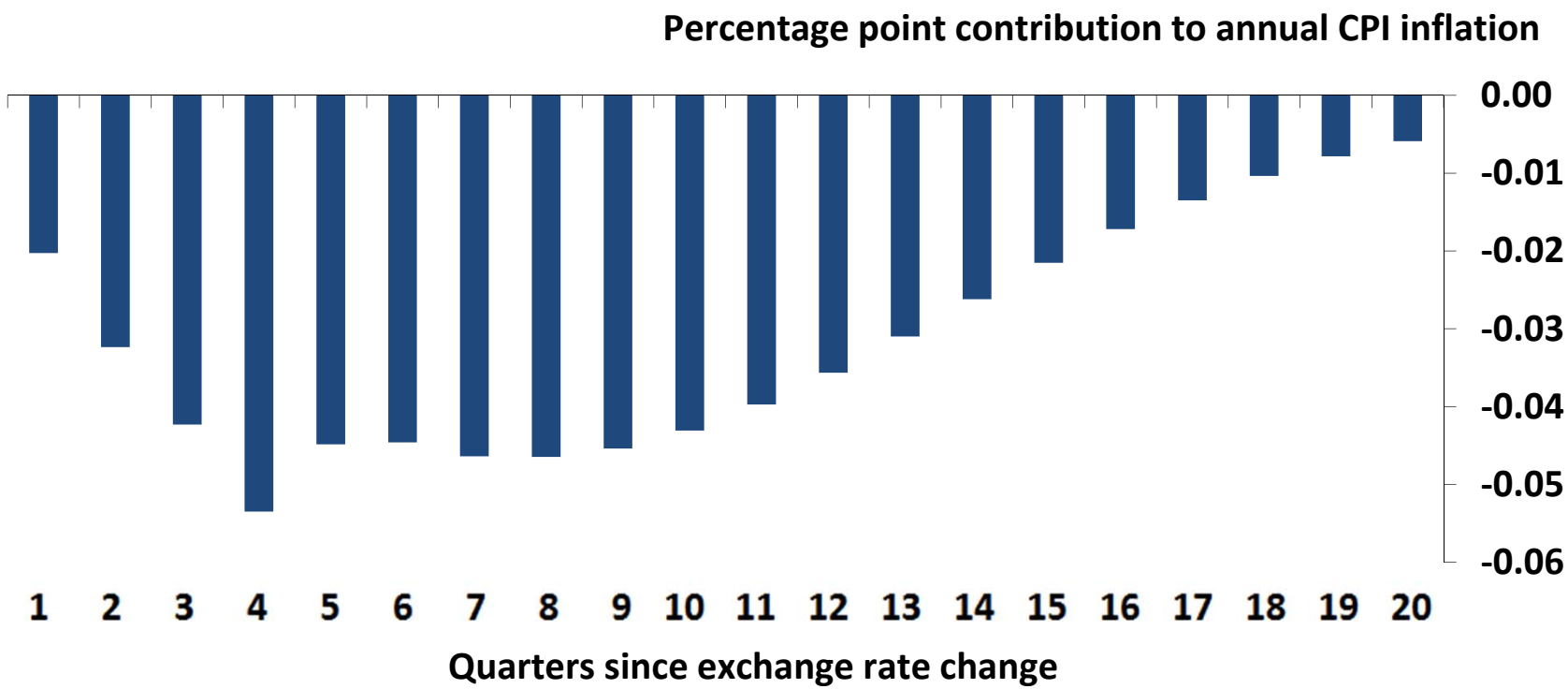
Non EU goods imports currency of invoicing



*Includes some capital goods

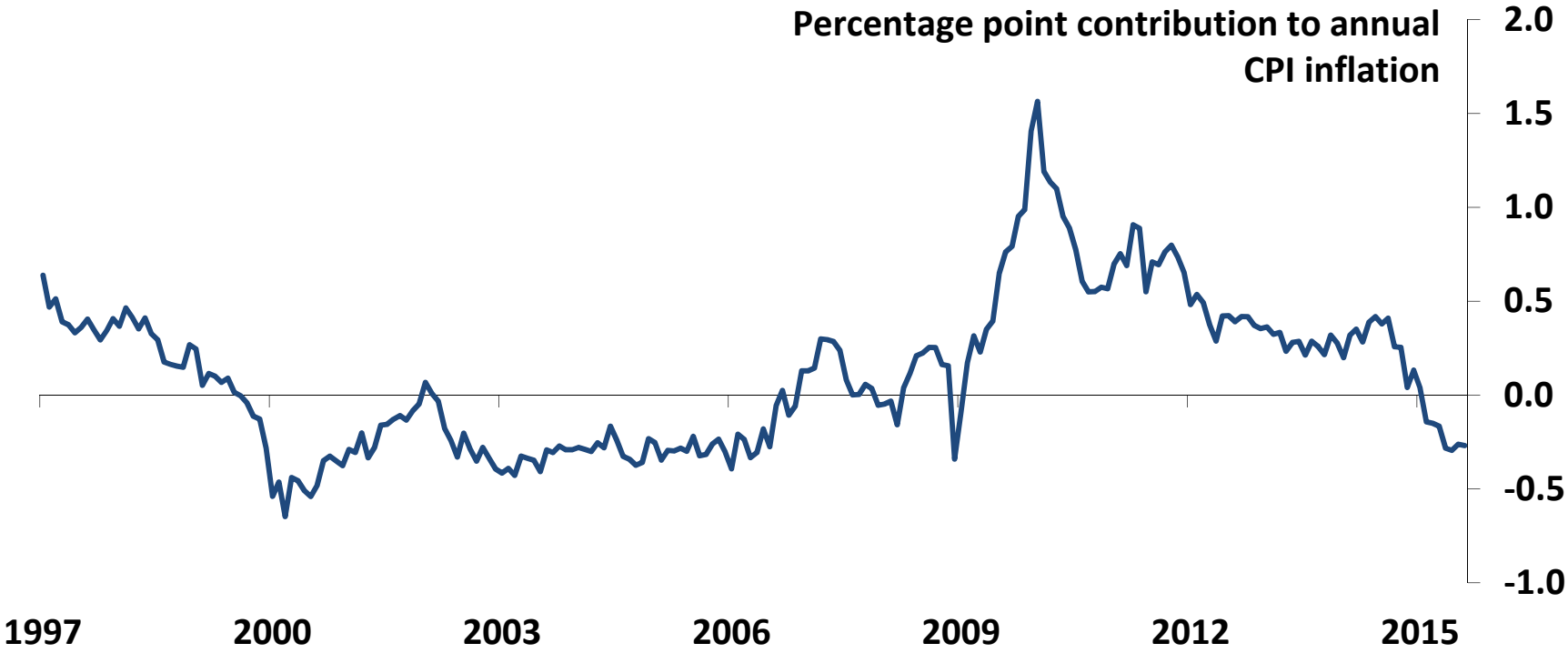
- **The dollar is much more important for pricing of UK imports than the US trade share would suggest.**

Direct effect of 1% appreciation on CPI inflation (ex. energy)



- **Pass-through to CPI assumed to be very gradual.**

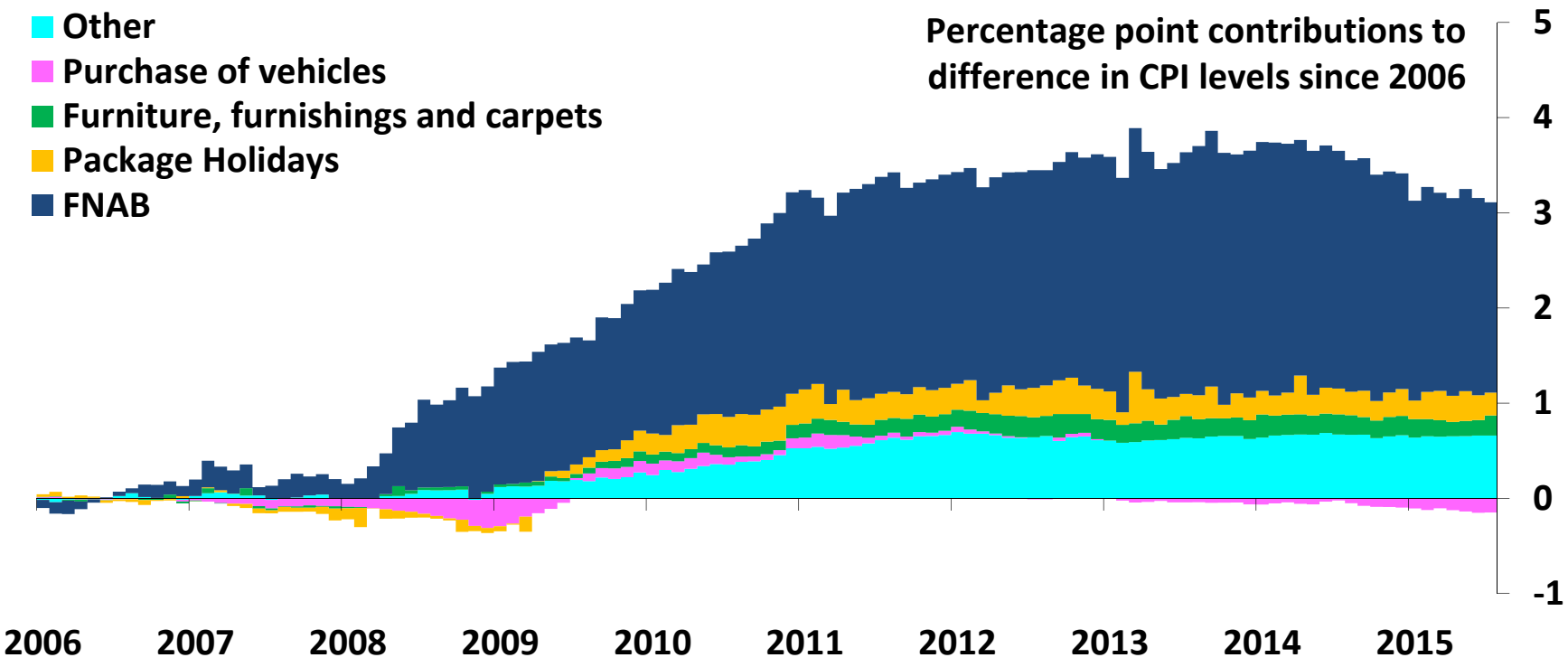
Contribution of core goods to inflation



*Excludes clothing and footwear due to changes in measurement practices in 2010.

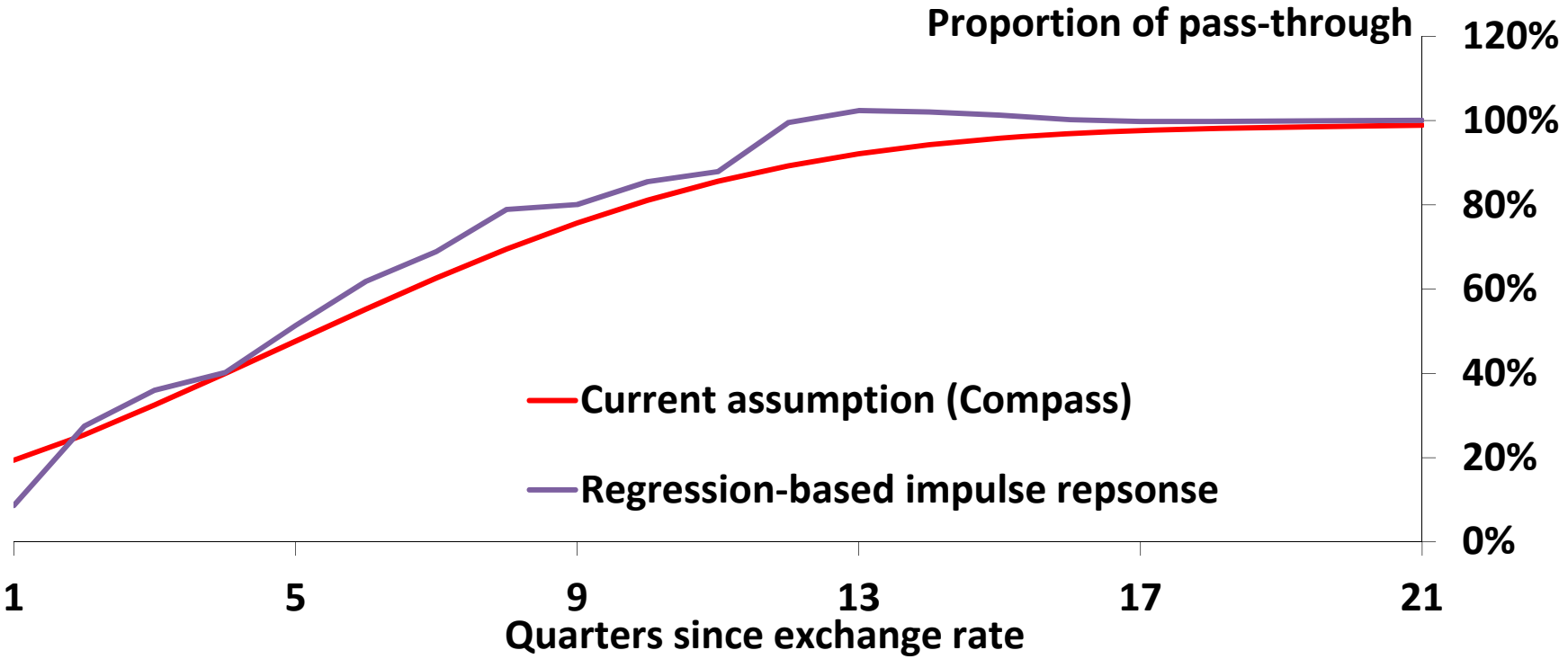
- **Contribution of core goods remained elevated for a long time after sterling depreciation in 2007/08.**

Contributions of import-intensive items to difference between UK & euro area CPI levels



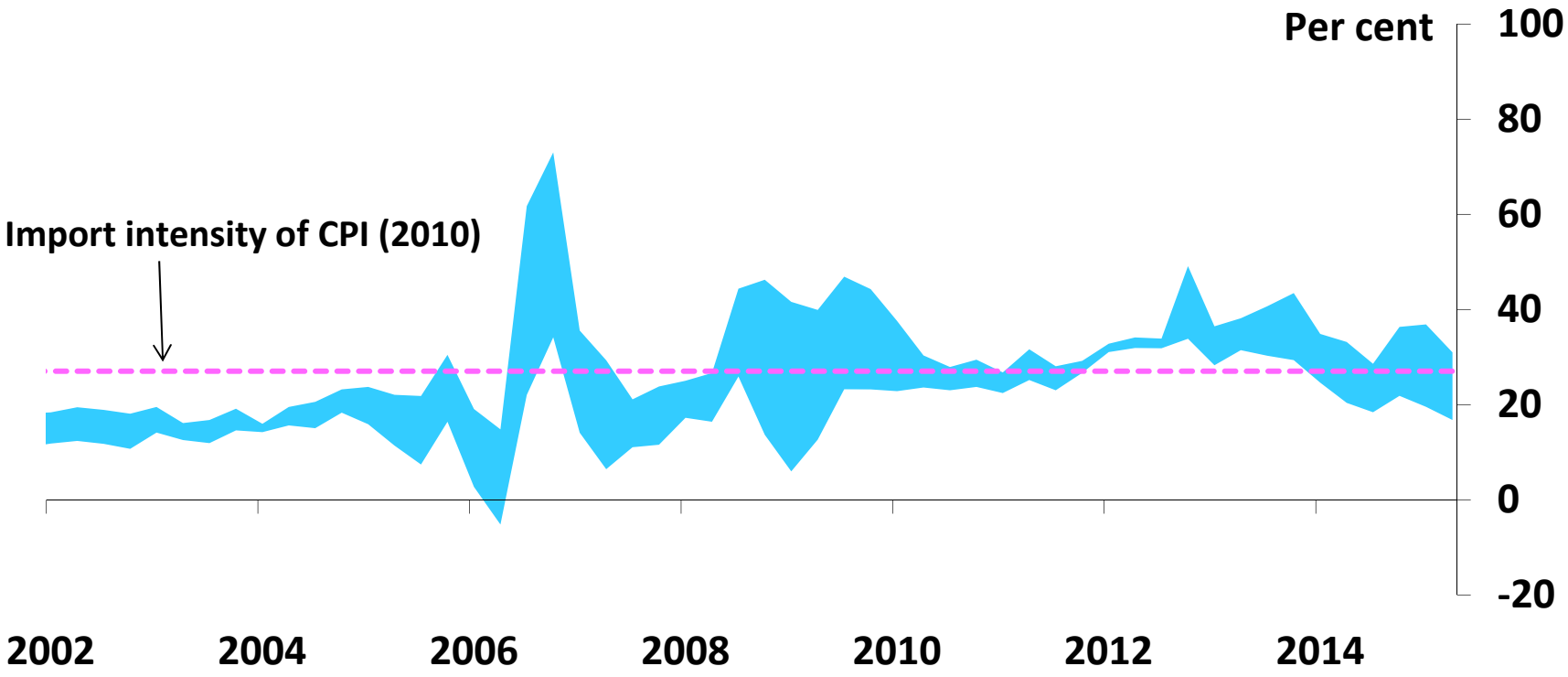
- UK-EA CPI differential built up gradually following depreciation.

Estimates of speed of pass through to CPI inflation



- **Compass and regression-based estimates point to protracted pass-through.**

Rolling regressions of long-run pass-through to CPI



* The swathe reflects variations in the number of lags included.

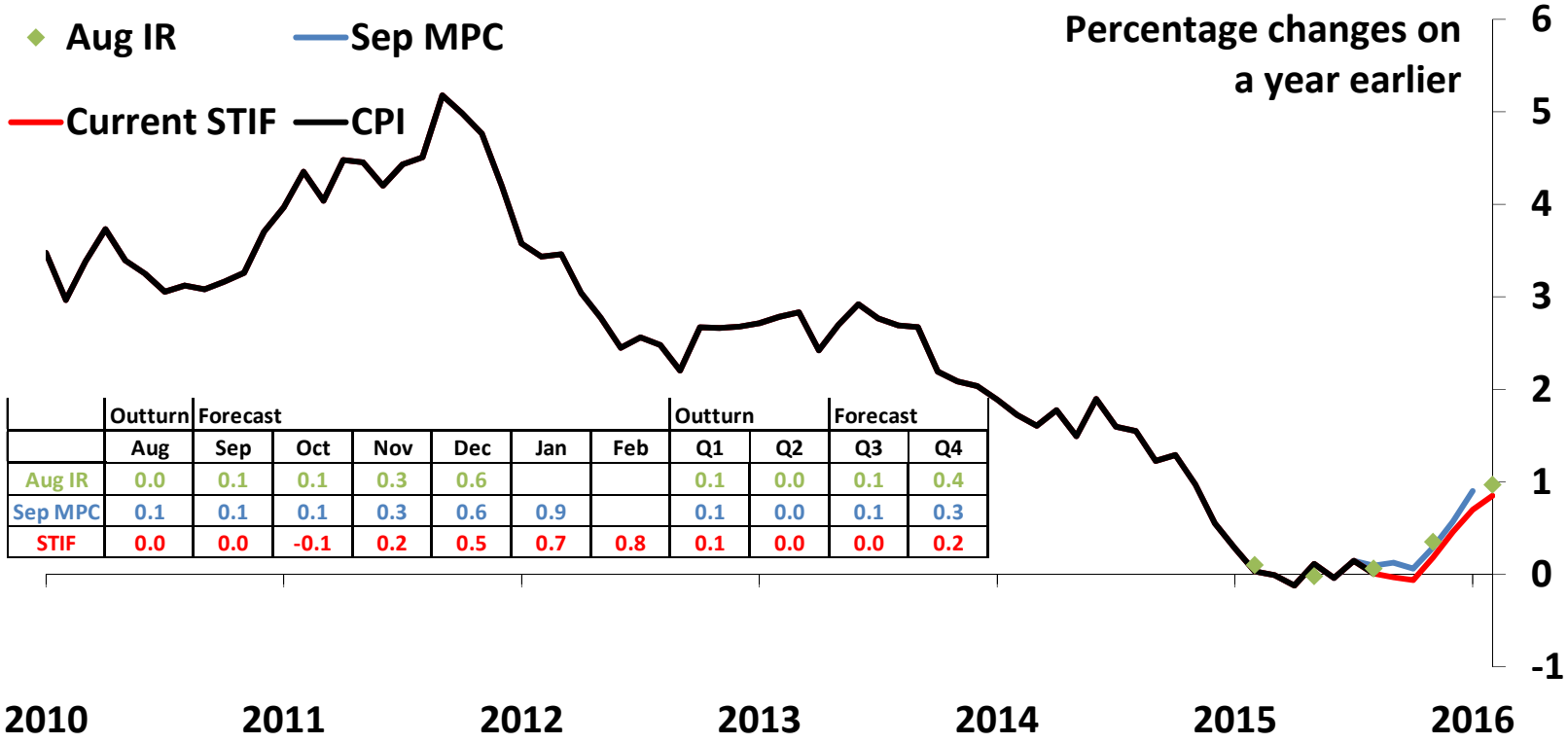
- **Simple regressions point to full long-run pass through to CPI.**

Main messages

- **Exchange rate pass-through**
  - **Further work supportive of August IR assumptions.**
  - **Prevalence of dollar pricing may explain smaller than expected fall in import prices.**
  - **Substantial uncertainty that stretches to policy-relevant horizons.**

Inflation

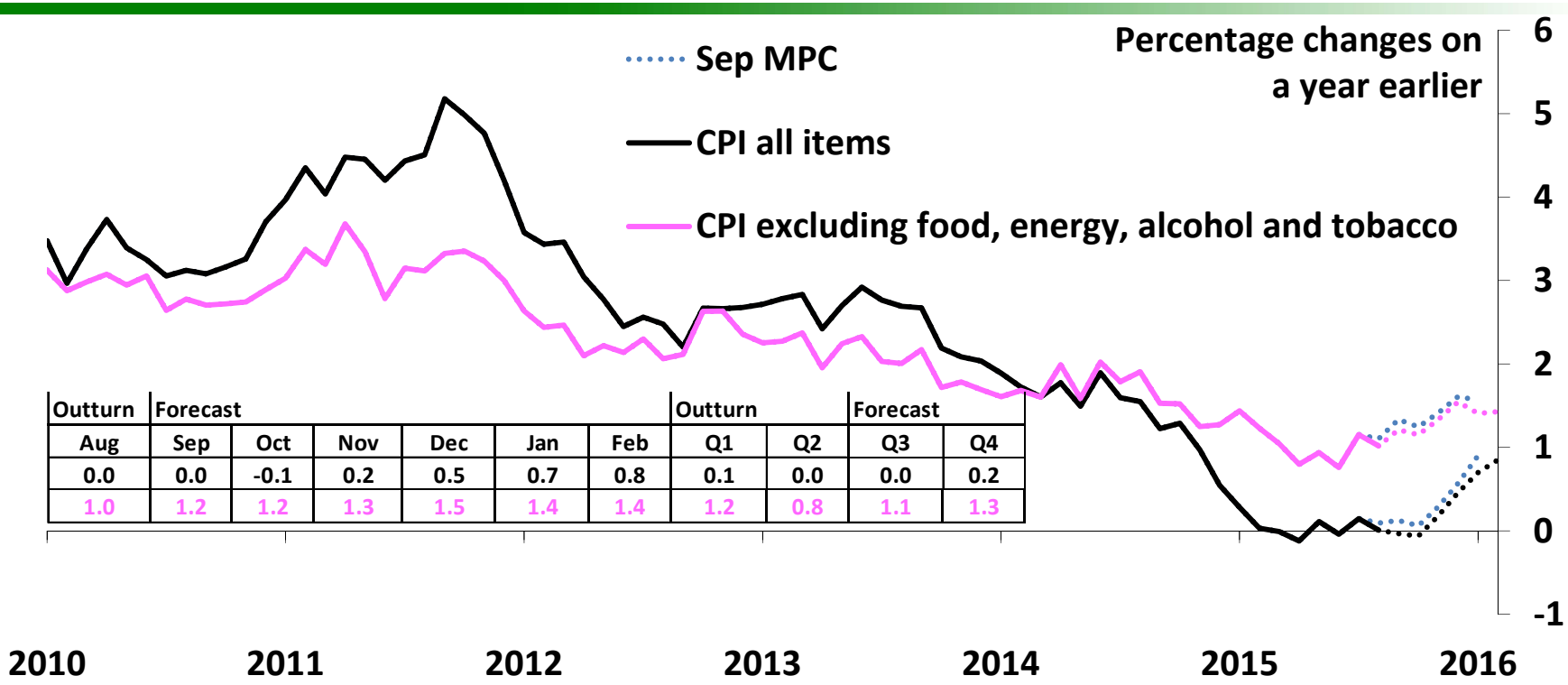
Short-term inflation forecast



	Outturn	Forecast						Outturn		Forecast	
	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Q1	Q2	Q3	Q4
Aug IR	0.0	0.1	0.1	0.3	0.6			0.1	0.0	0.1	0.4
Sep MPC	0.1	0.1	0.1	0.3	0.6	0.9		0.1	0.0	0.1	0.3
STIF	0.0	0.0	-0.1	0.2	0.5	0.7	0.8	0.1	0.0	0.0	0.2

- **Inflation forecast 0.2pp lower than August IR.**

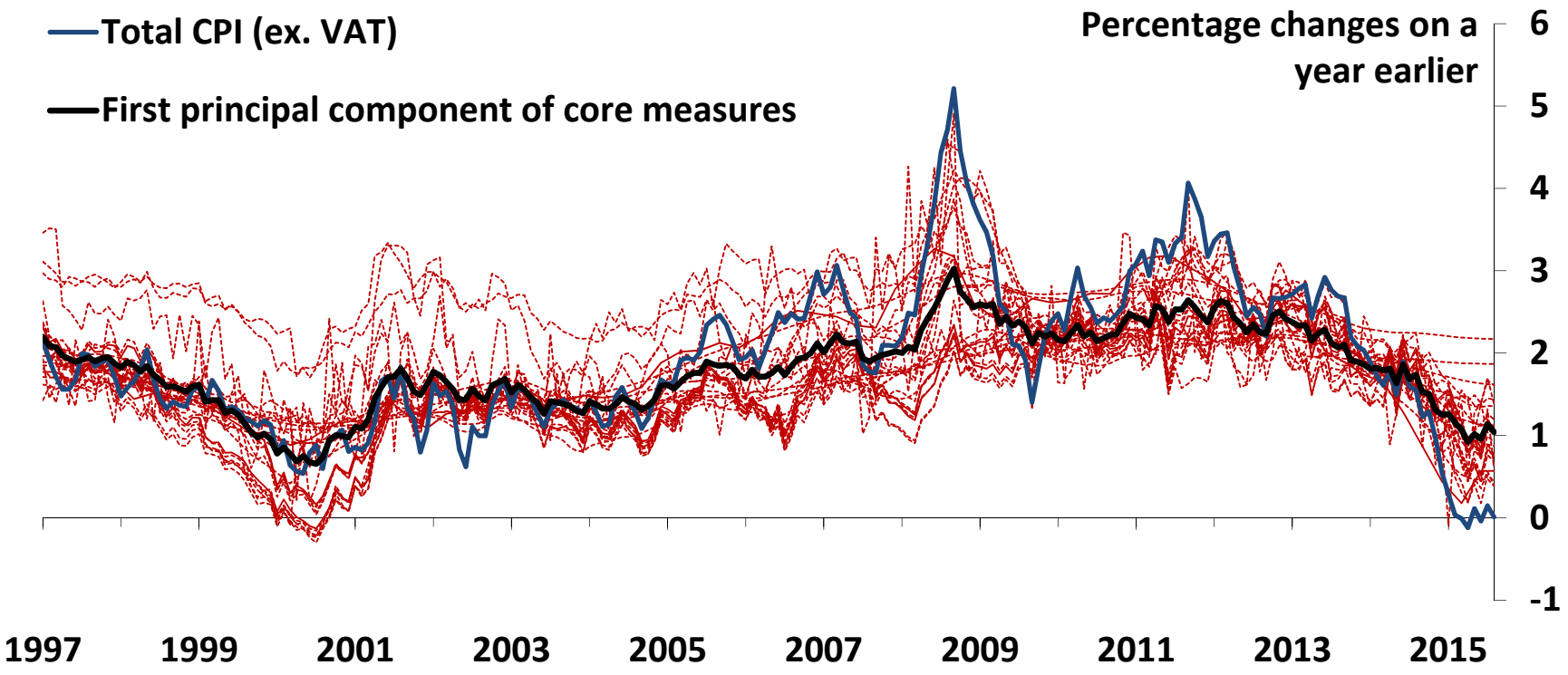
Short-term inflation forecast



Outturn	Forecast						Outturn		Forecast	
Aug	Sep	Oct	Nov	Dec	Jan	Feb	Q1	Q2	Q3	Q4
0.0	0.0	-0.1	0.2	0.5	0.7	0.8	0.1	0.0	0.0	0.2
1.0	1.2	1.2	1.3	1.5	1.4	1.4	1.2	0.8	1.1	1.3

- **The ONS measure of core inflation fell back to 1.0% in August.**

Core inflation measures



- **Our summary indicator of a wide range of core measures also fell back to 1.0%.**

Main messages

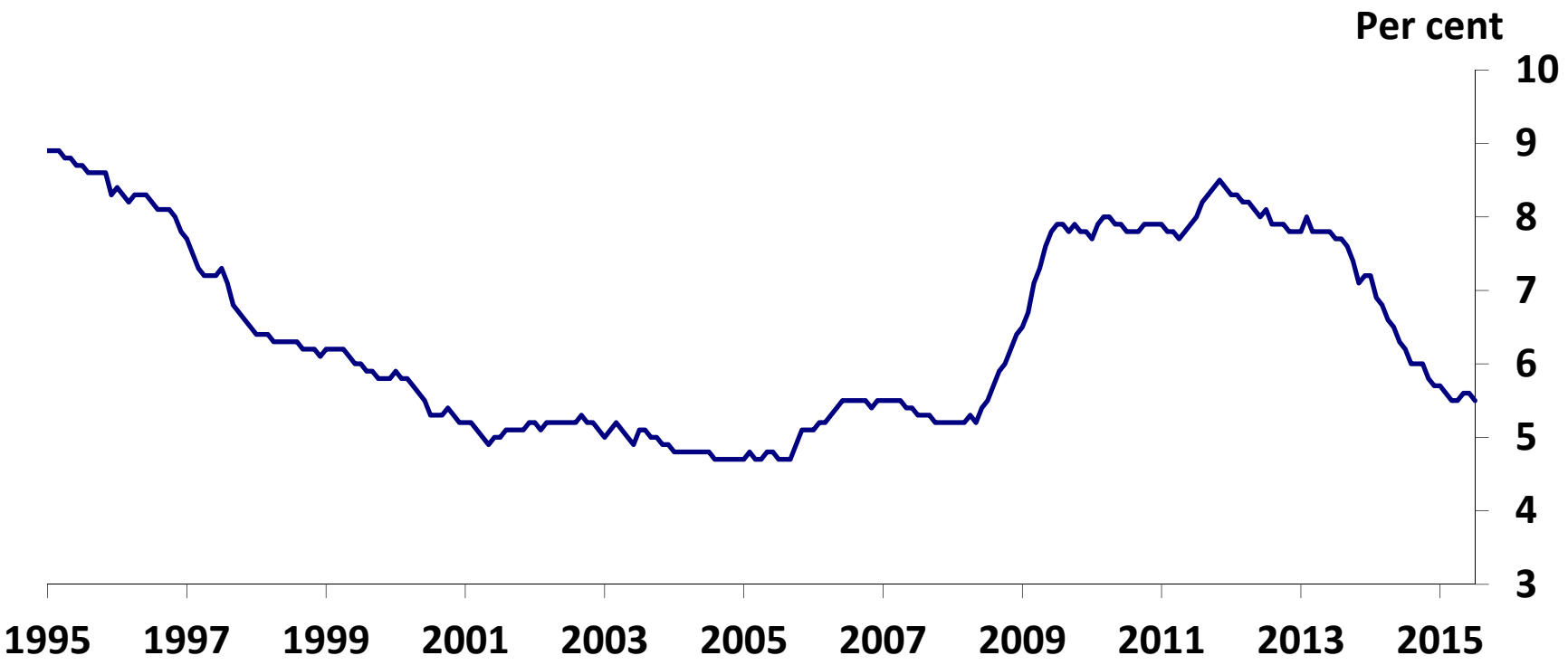
- **Exchange rate pass-through**
  - **Further work supportive of August IR assumptions.**
  - **Prevalence of dollar pricing may explain recent weak pass-through.**
  - **Substantial uncertainty that stretches to policy-relevant horizons.**

- **Inflation outlook lower than August IR mainly due to food and energy.**

Equilibrium unemployment

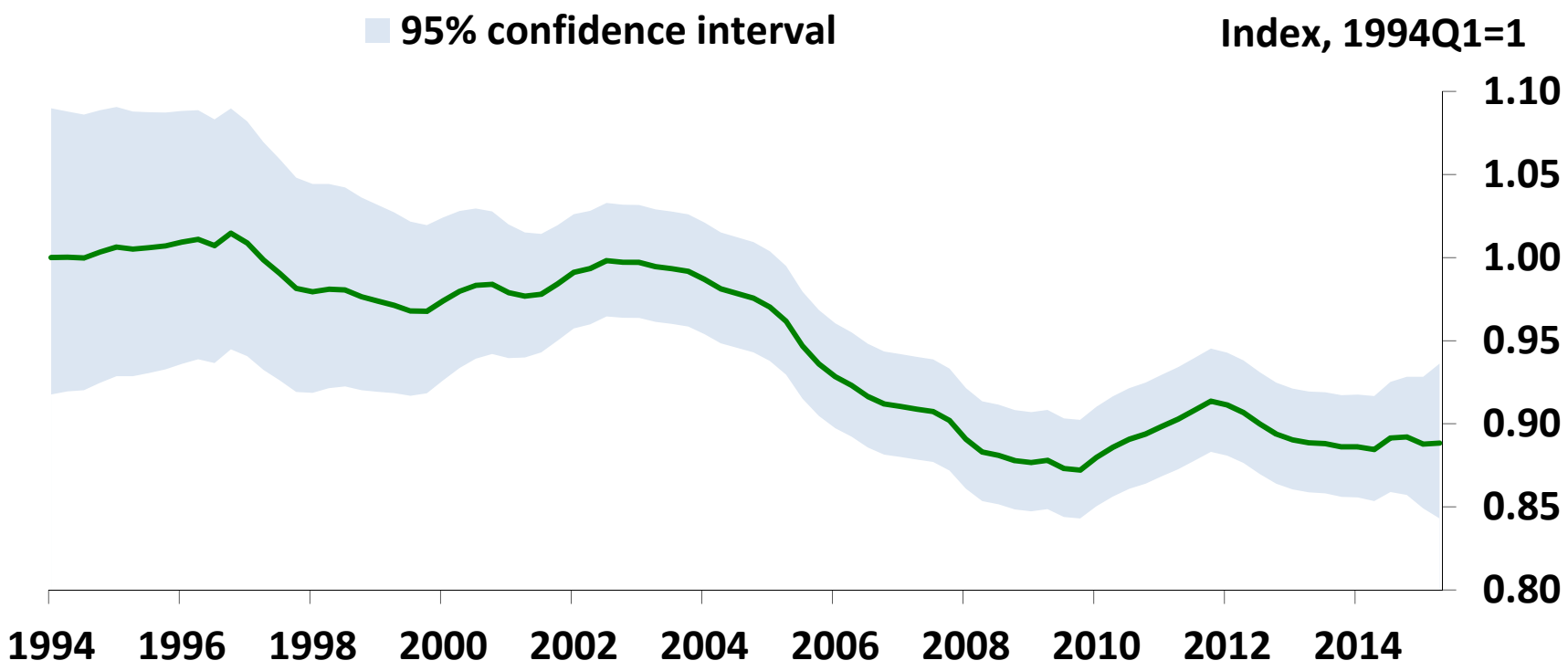
- for more information.

Unemployment rate



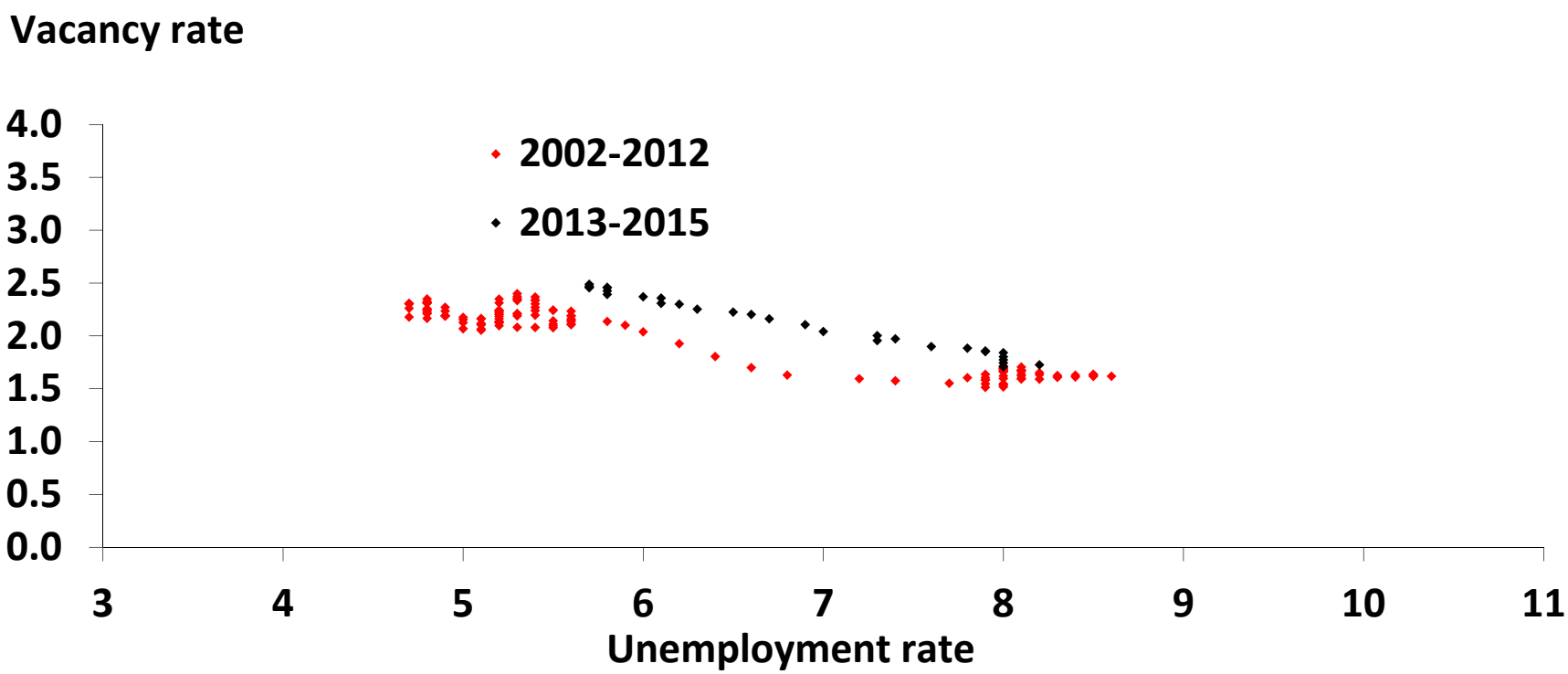
- **Unemployment fairly stable at 5% pre-crisis but picked up to 5.5% just before the financial crisis.**

Time-varying estimate of matching efficiency

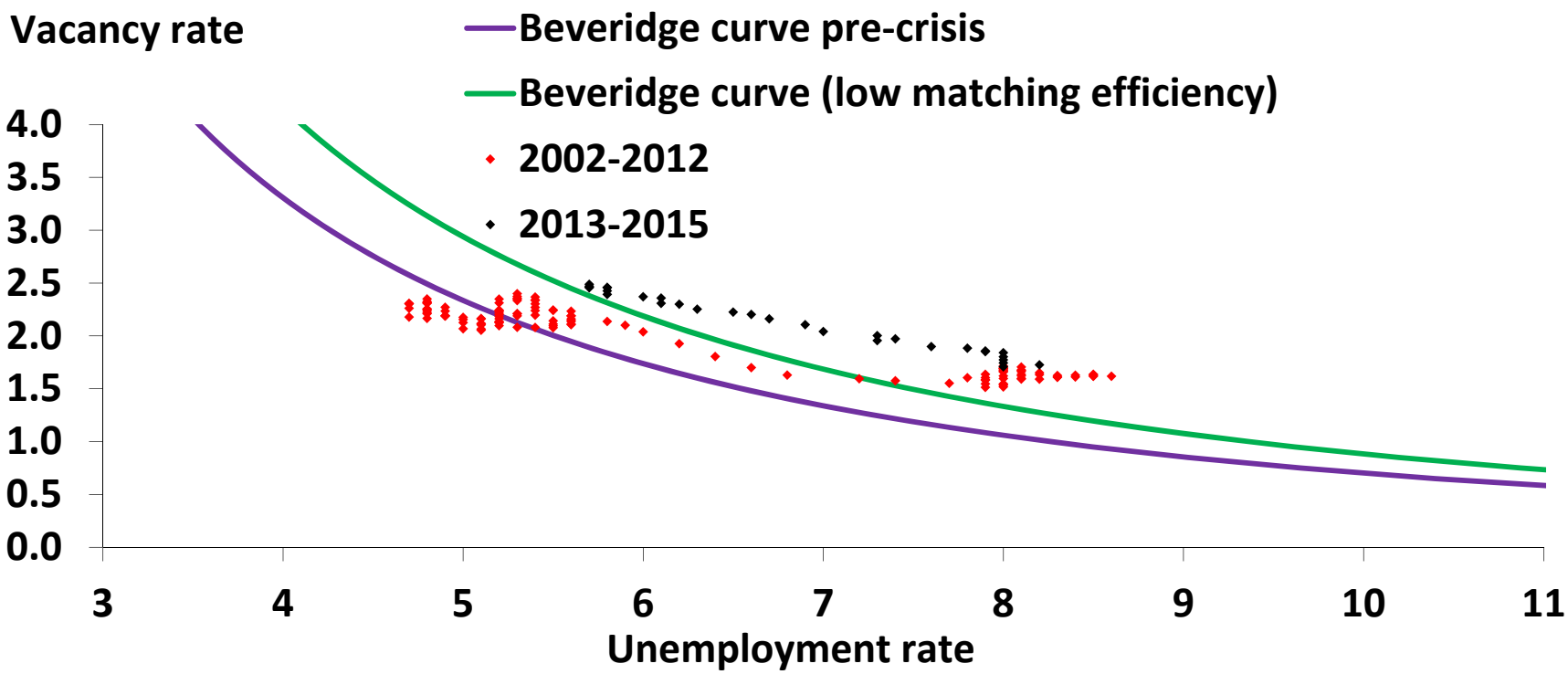


- **Decline in matching efficiency might point to higher equilibrium unemployment.**

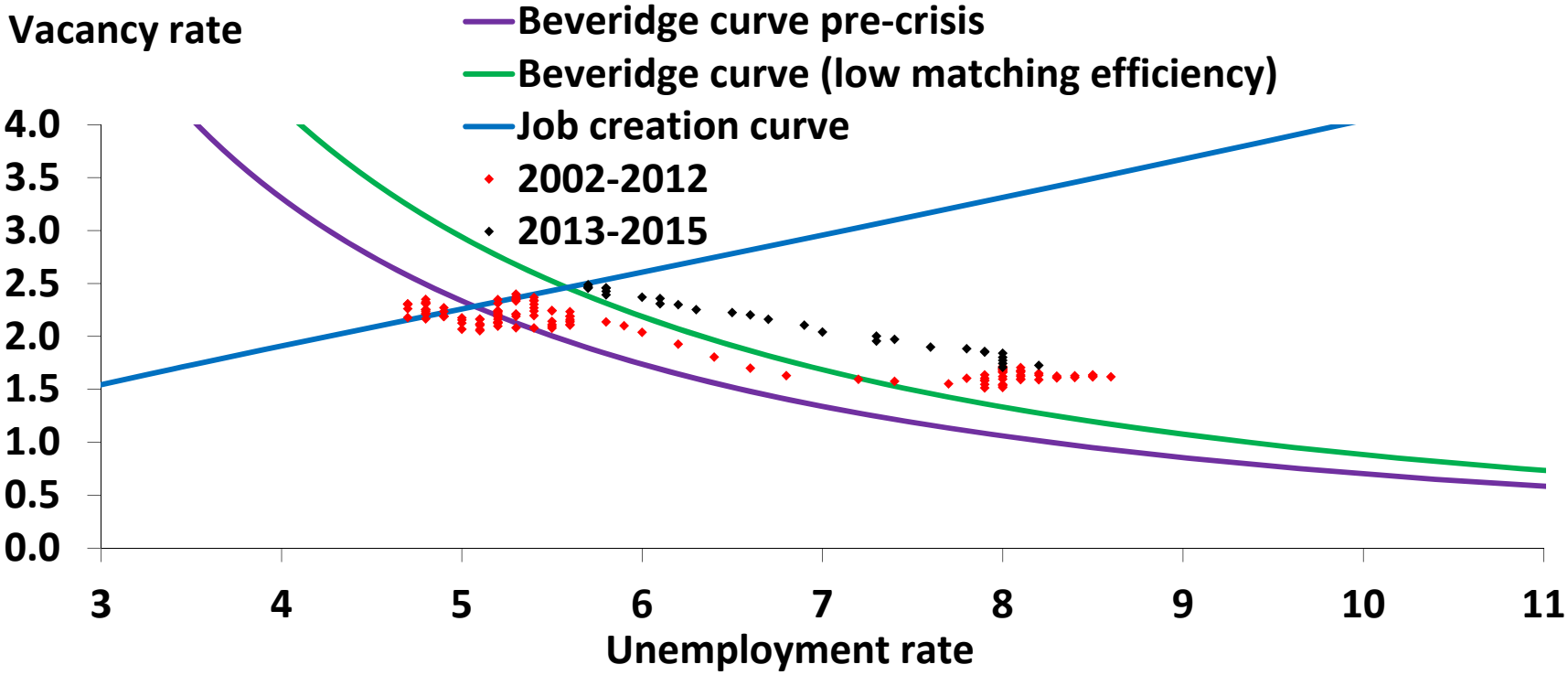
Beveridge curve



Beveridge curve

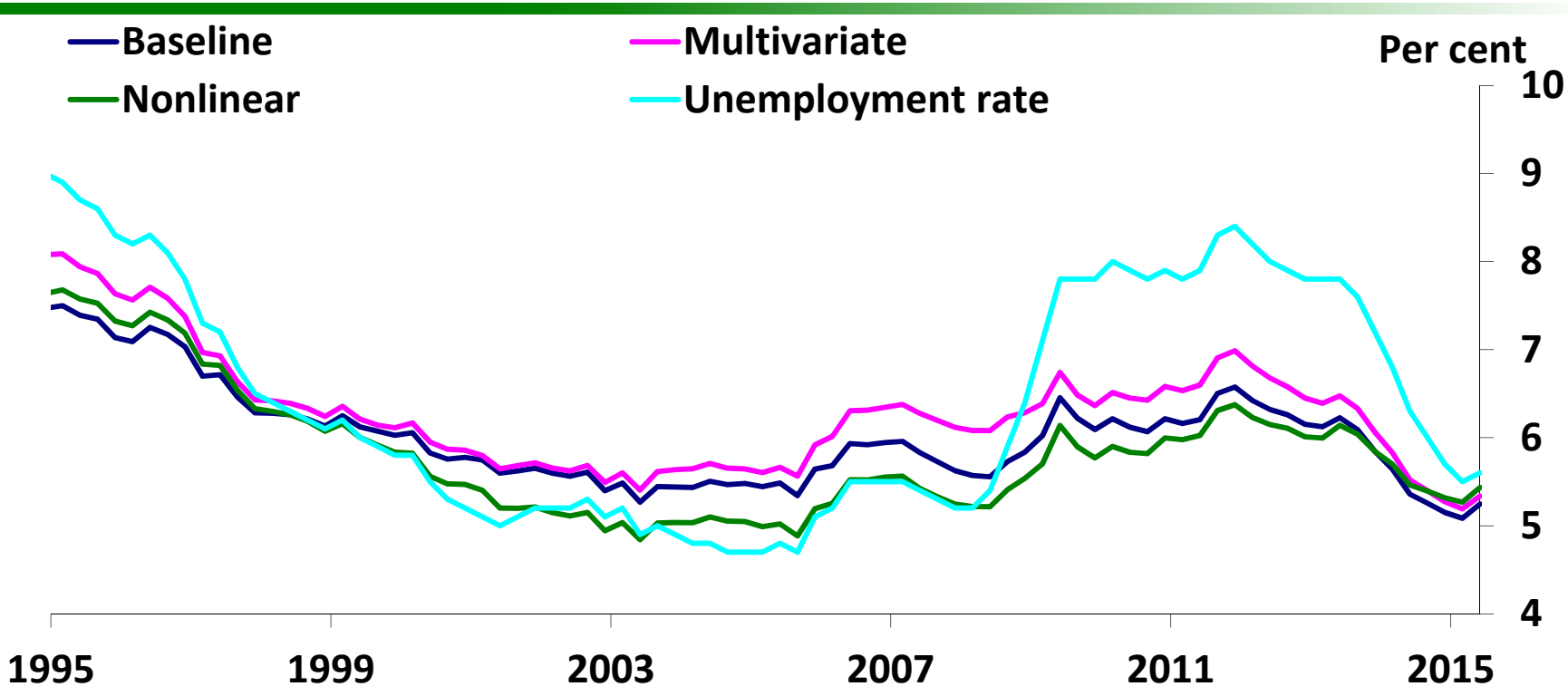


Beveridge curve and job creation curve



- **Shift out in Beveridge curve consistent with an increase in equilibrium from 5% to 5.5% but may be transitory.**

Filter-based estimates using Phillips curve relationship



- **Filter-based estimates consistent with *U** estimate of 5.3% in Q2.**

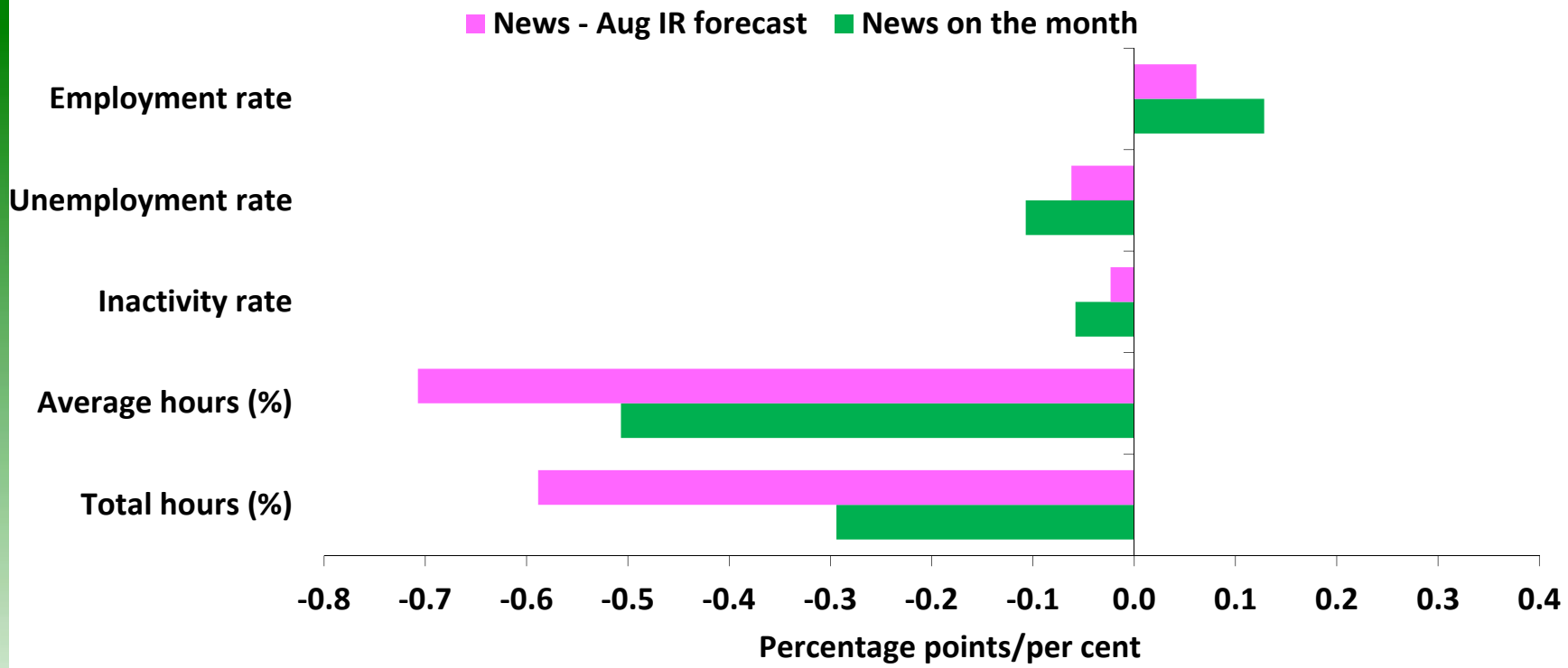
Main messages

- **Exchange rate pass-through**
  - **Further work supportive of August IR assumptions.**
  - **Prevalence of dollar pricing may explain recent weak pass-through.**
  - **Substantial uncertainty that stretches to policy-relevant horizons.**

- **Inflation outlook lower than August IR mainly due to food and energy.**

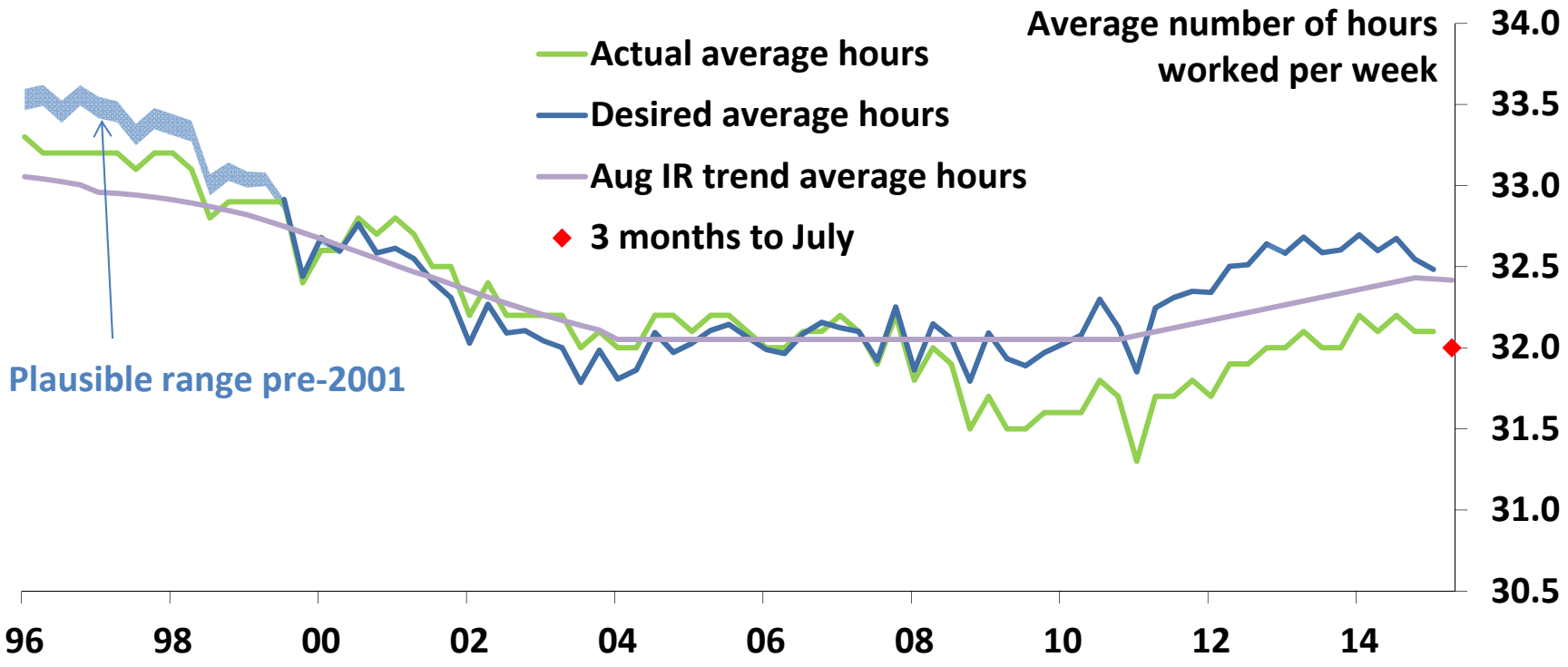
- **Risks around equilibrium unemployment more balanced.**

News in labour market quantities



- **Downside news entirely accounted for by weak average hours.**

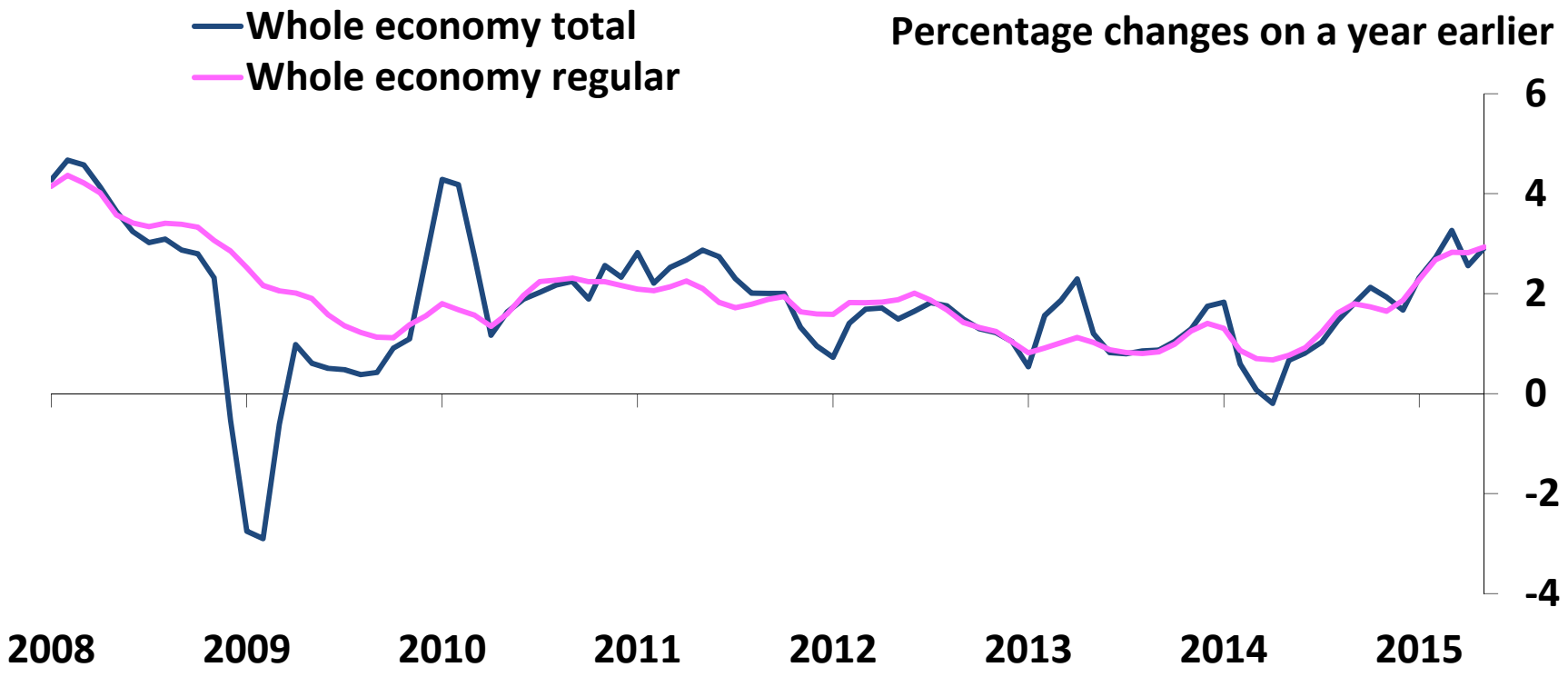
Desired hours



- **Assumed trend for average hours now looking too high.**

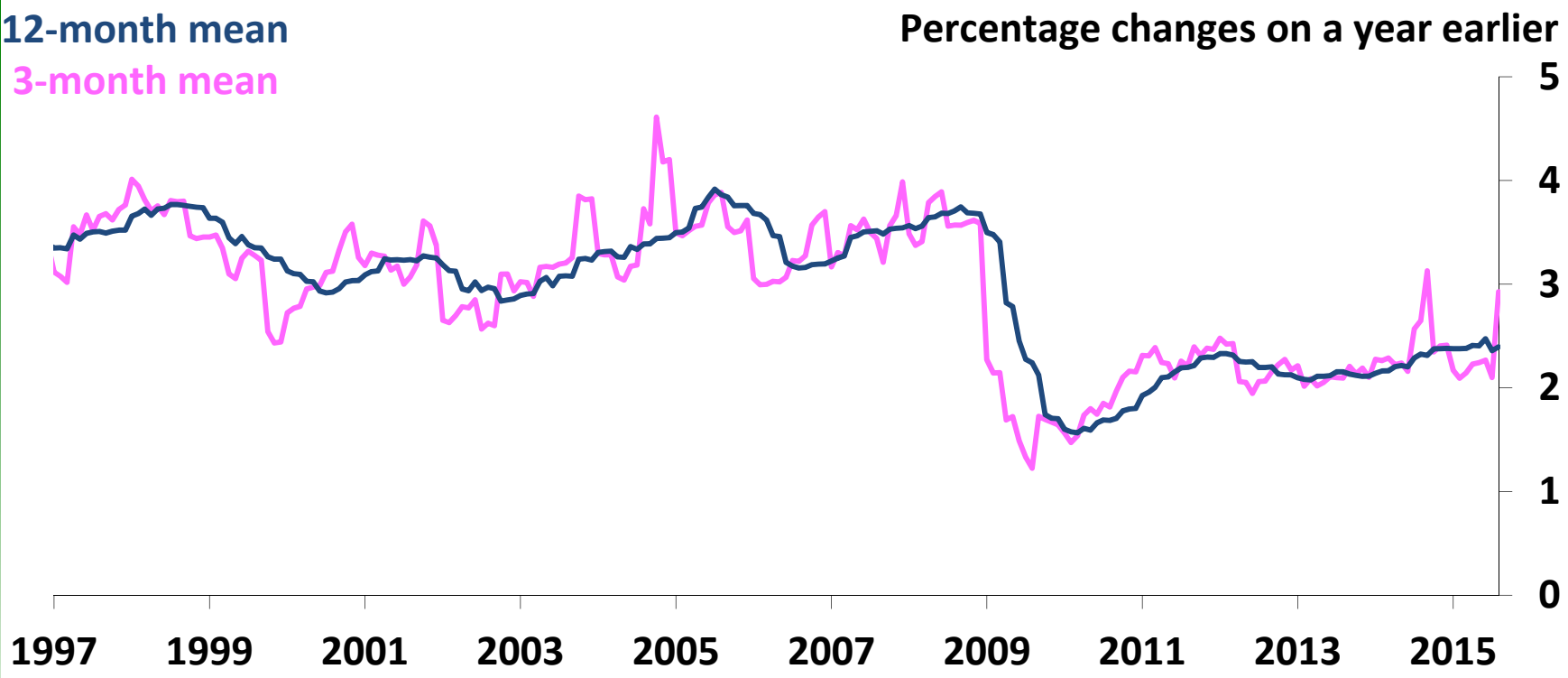
Wages

Whole economy pay



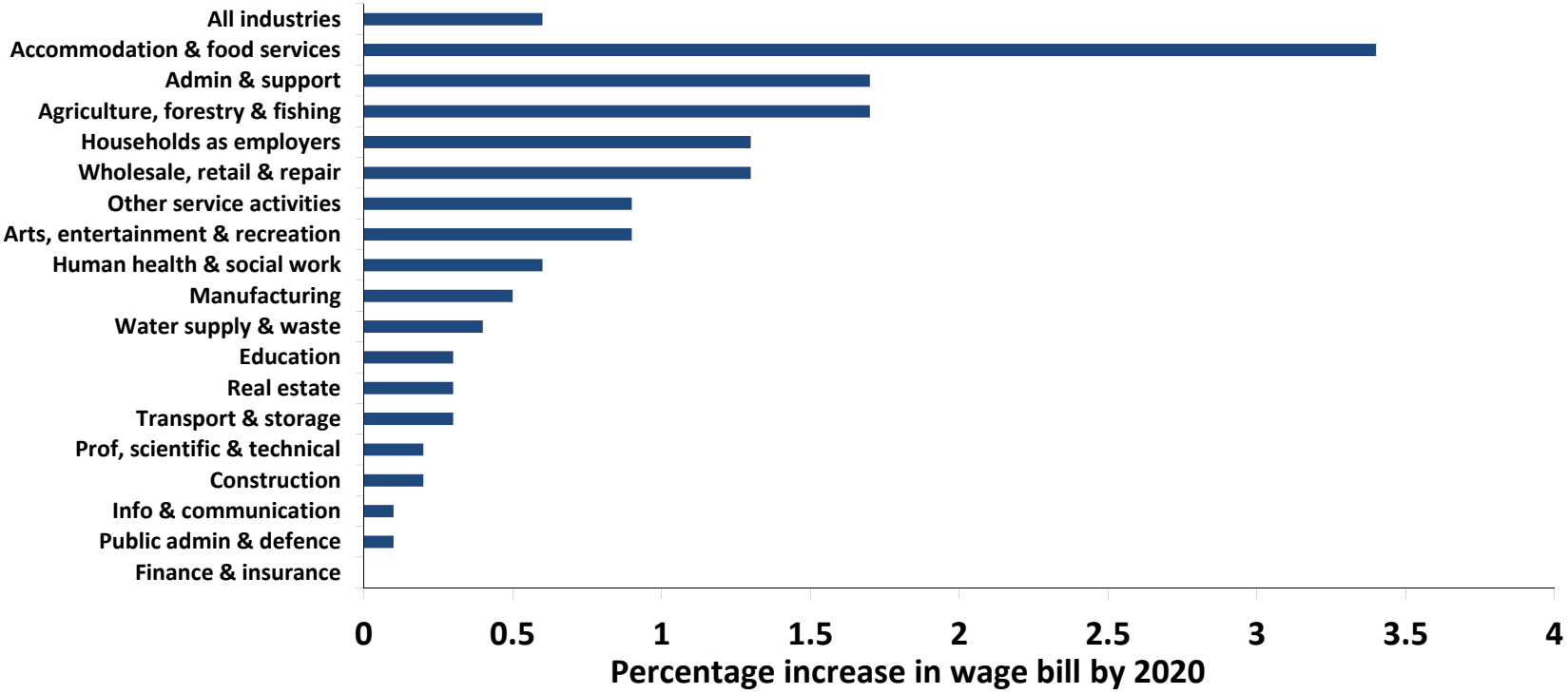
- **Pay growth broadly in line with the August IR.**

Private sector pay settlements



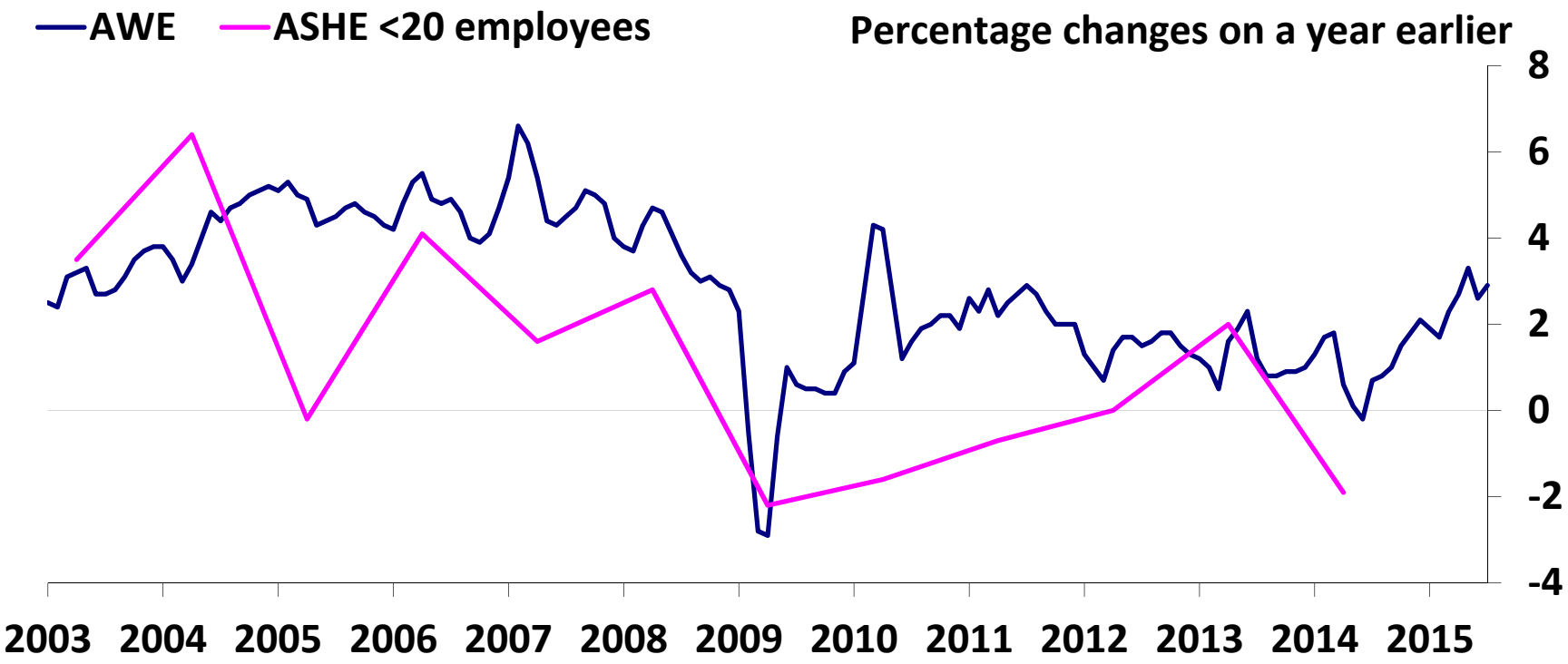
- **Private sector settlements still pretty flat at 2.4%.**

Resolution foundation sectoral impact of NLW



- **Impact of NLW likely to vary significantly across sectors.**

AWE vs ASHE pay growth for small firms



- **Incorporation of 2014 ASHE data on pay in small companies will lead to small downward revisions to AWE.**

Main messages

- **Exchange rate pass-through**
  - **Further work supportive of August IR assumptions.**
  - **Prevalence of dollar pricing may explain recent weak pass-through.**
  - **Substantial uncertainty that stretches to policy-relevant horizons.**
- **Inflation outlook lower than August IR mainly due to food and energy.**
- **Risks around equilibrium unemployment more balanced.**
- **Average hours trend looks too strong.**
- **Pay growth broadly in line with the August IR.**

END

5: Agents’ Special Topic

Agents' Survey

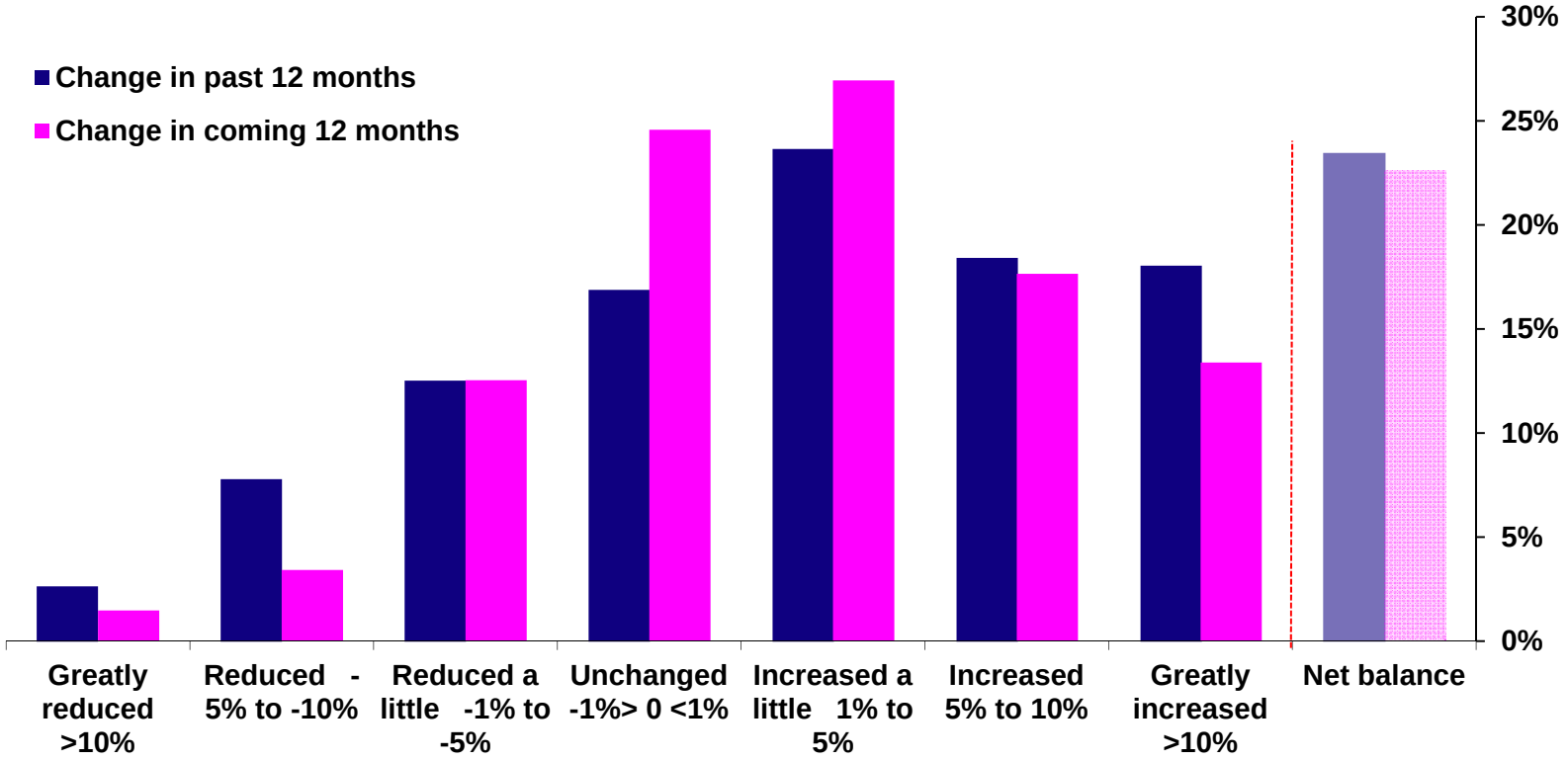
30 September 2015

, Agency for the West Midlands
Inflation Report & Agency Intelligence Division

Prospects for Employment

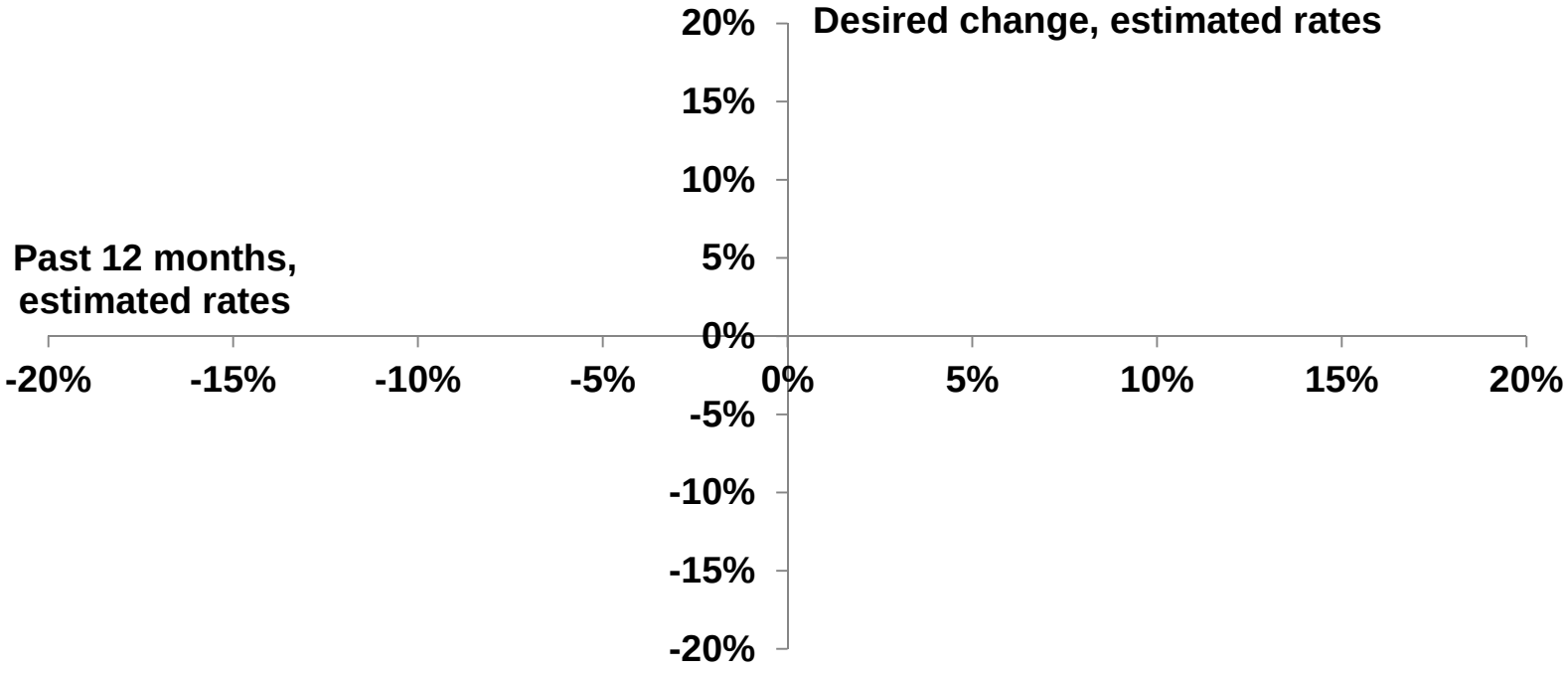
1. Change in size of workforce – past and next 12 months?
2. Change in *desired* size of workforce – past 12 months?
3. Change in vacancies – past 12 months?
4. Difficulty filling vacancies compared to a year ago?
5. Recruitment difficulties binding on workforce growth?
6. Planned responses to recruitment difficulties?

Actual and expected change in employment



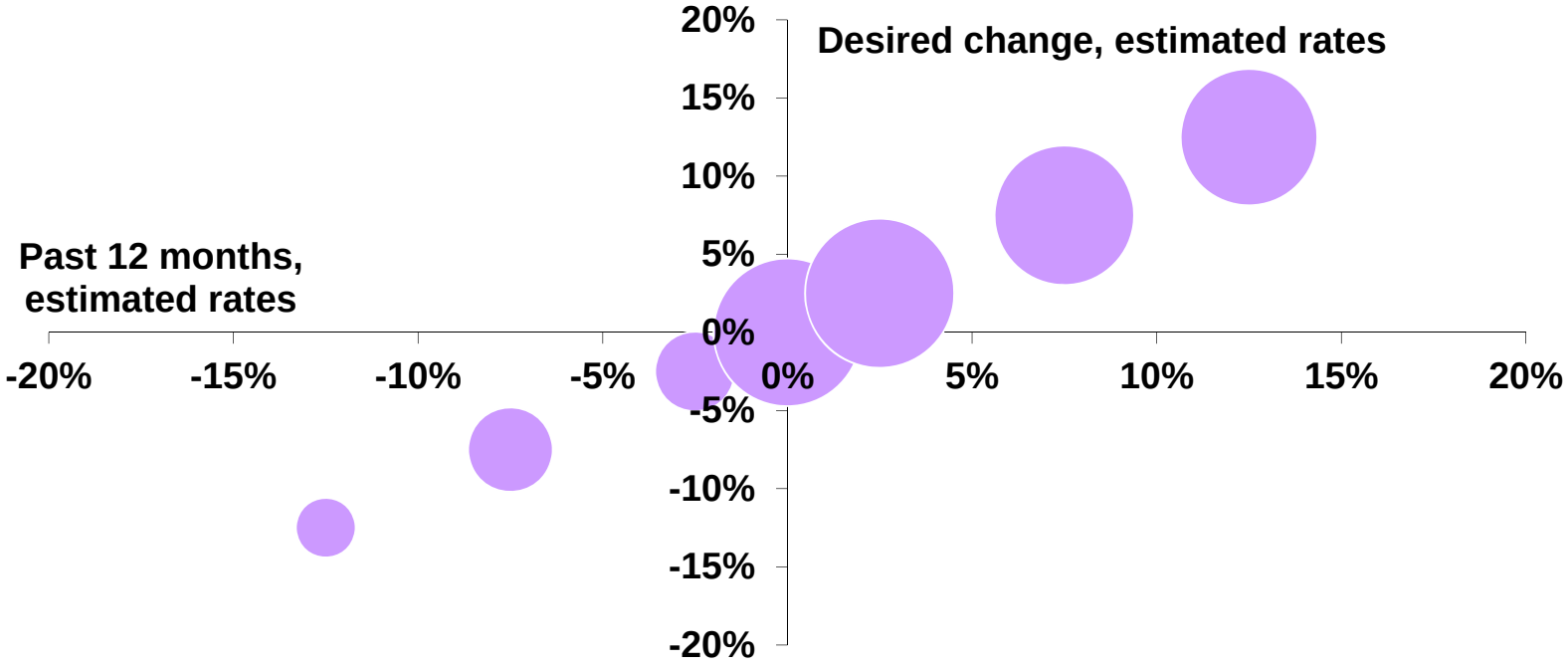
- Employment intentions remain positive

Actual and desired change in employment



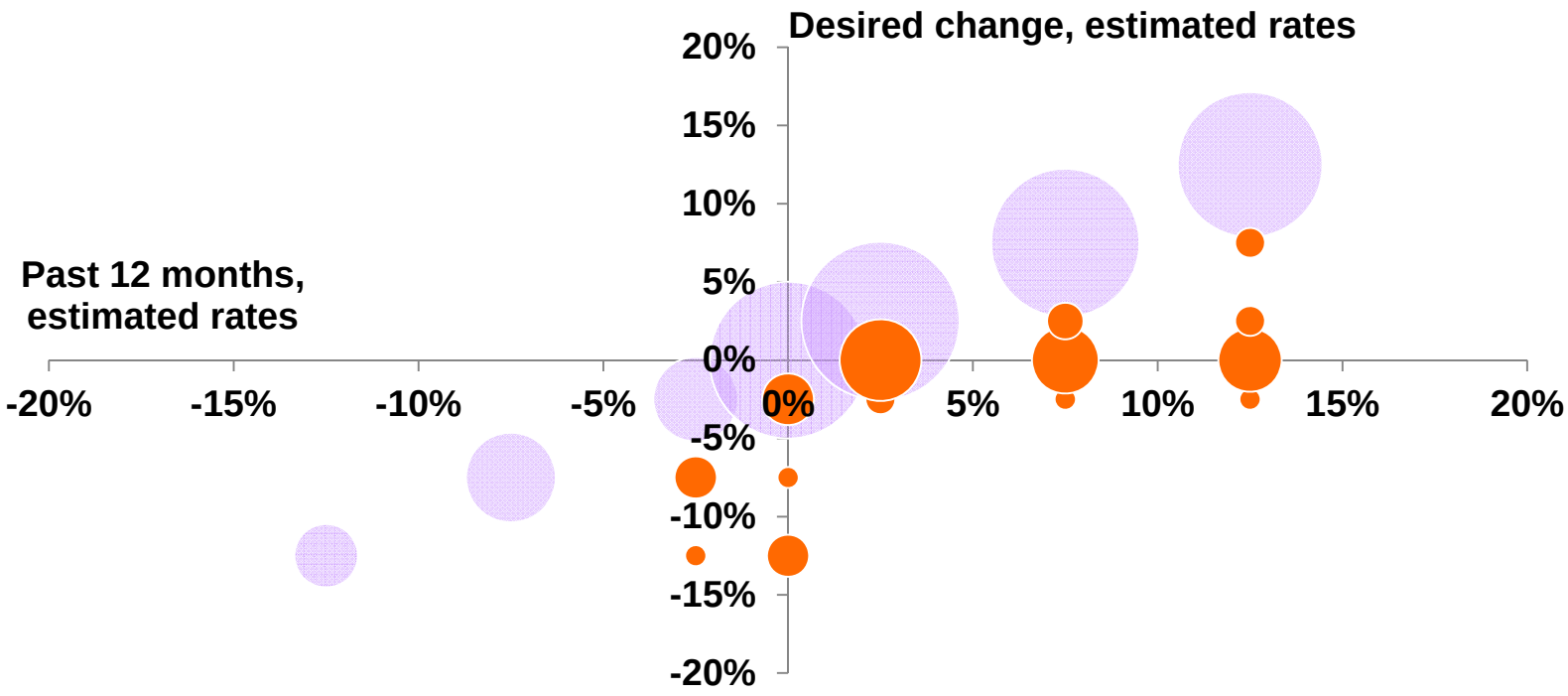
- Was workforce change as desired?

Actual and desired change in employment



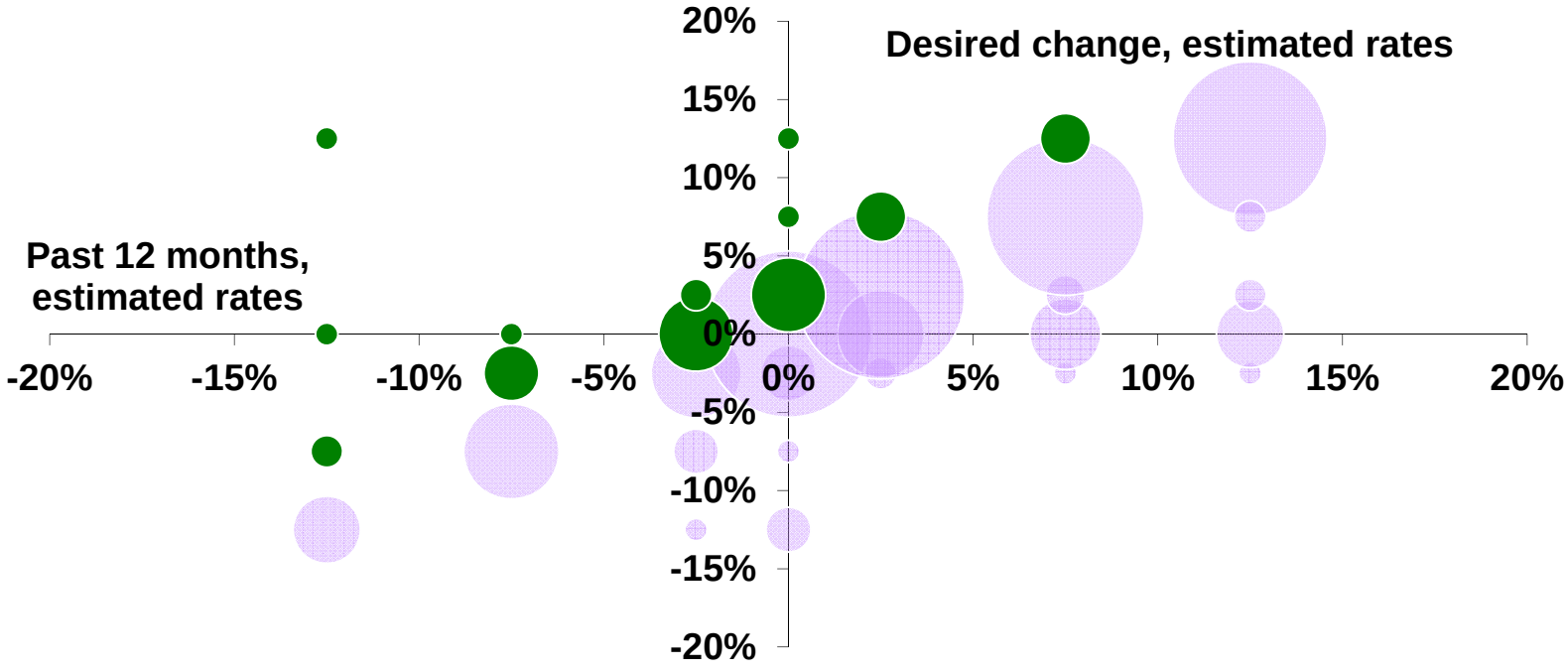
- Most contacts achieved their desired change in workforce

Actual and desired change in employment



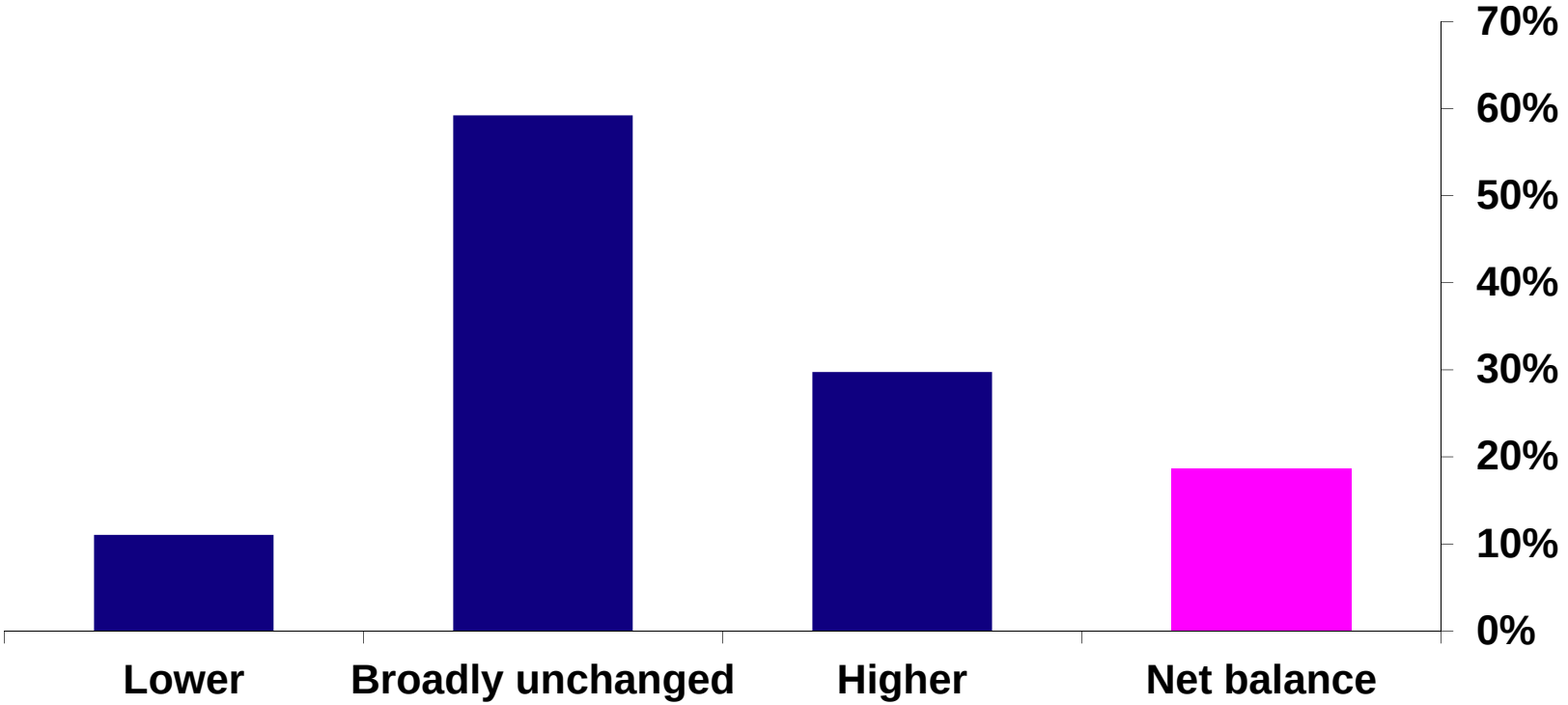
- Some contacts' actual workforce growth was <u>greater</u> than desired

Actual and desired change in employment



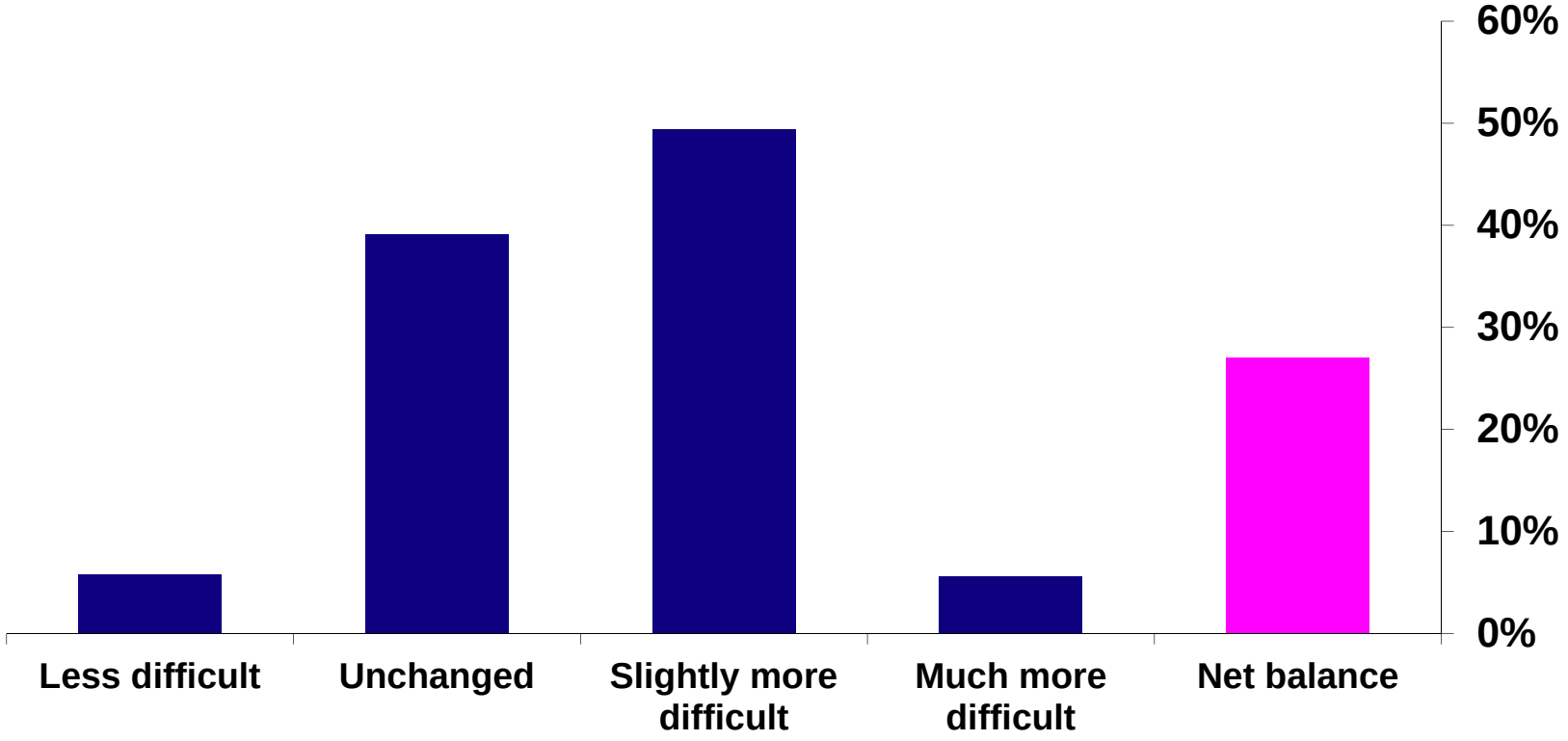
- Some contacts' actual workforce growth was <u>less</u> than desired

Changes in vacancies over the past 12 months



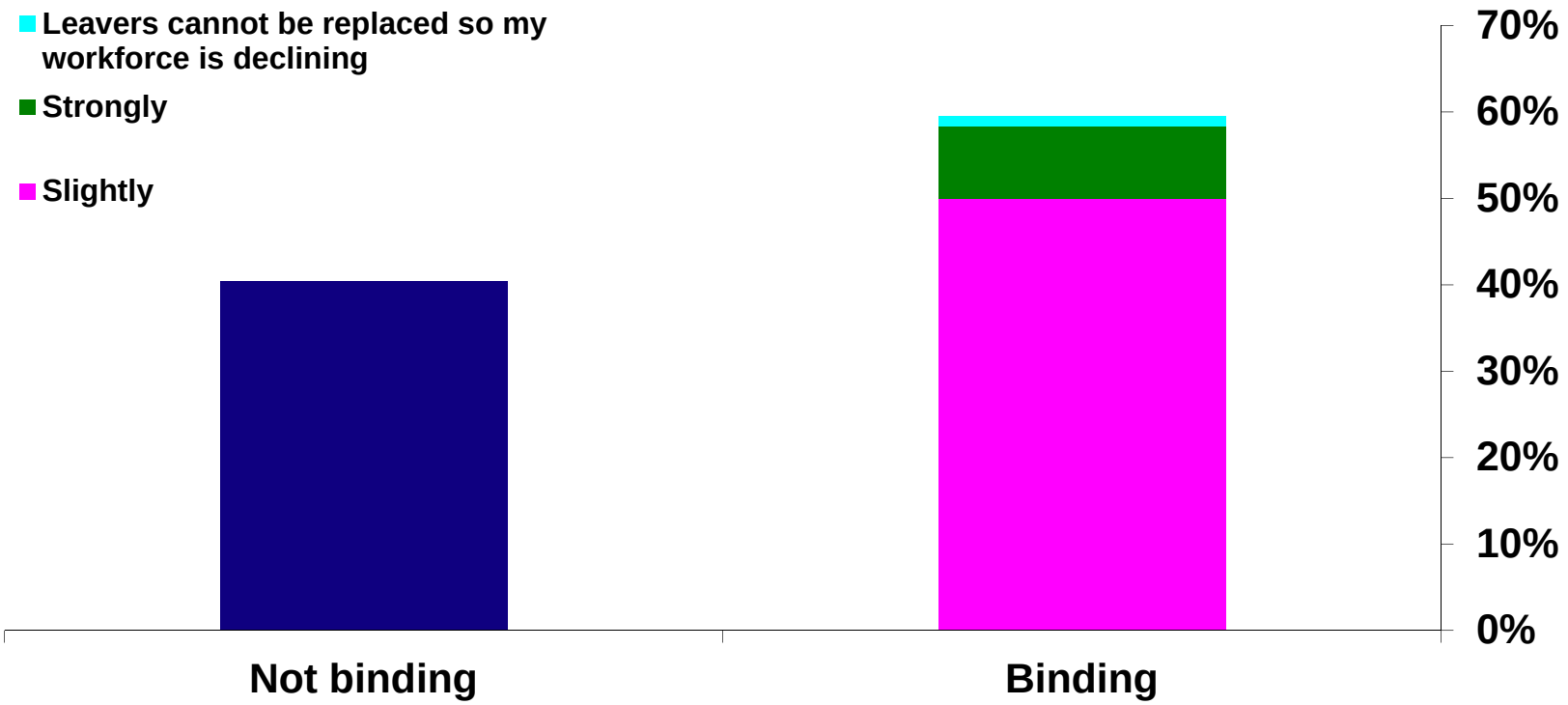
- Vacancies increasing on balance

Difficulty filling vacancies over the past 12 months



- Recruitment Difficulties increasing for all sectors and company sizes

Impact of recruitment difficulties on workforce growth

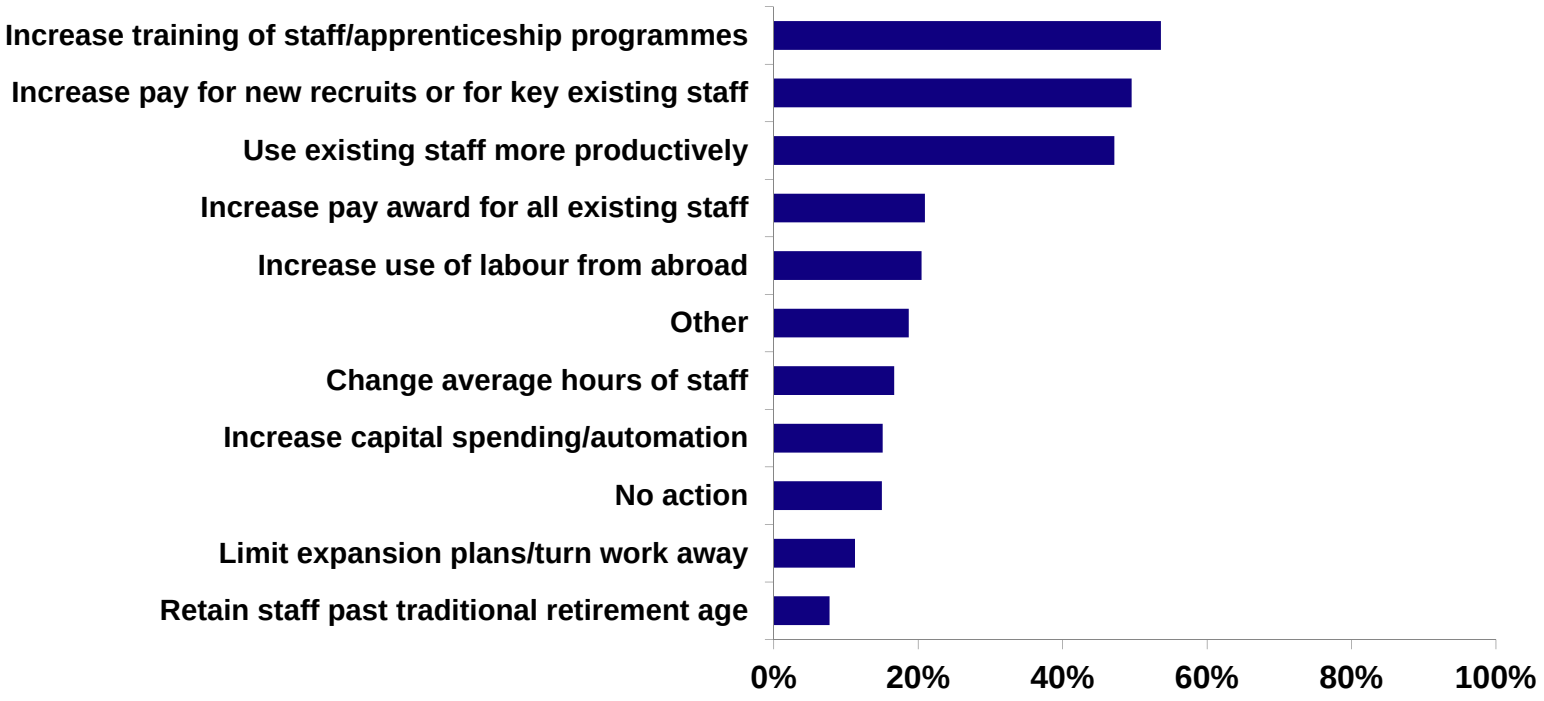


- Majority of contacts report recruitment difficulties binding slightly on workforce growth
- But not reducing the level of employment

Stock Take

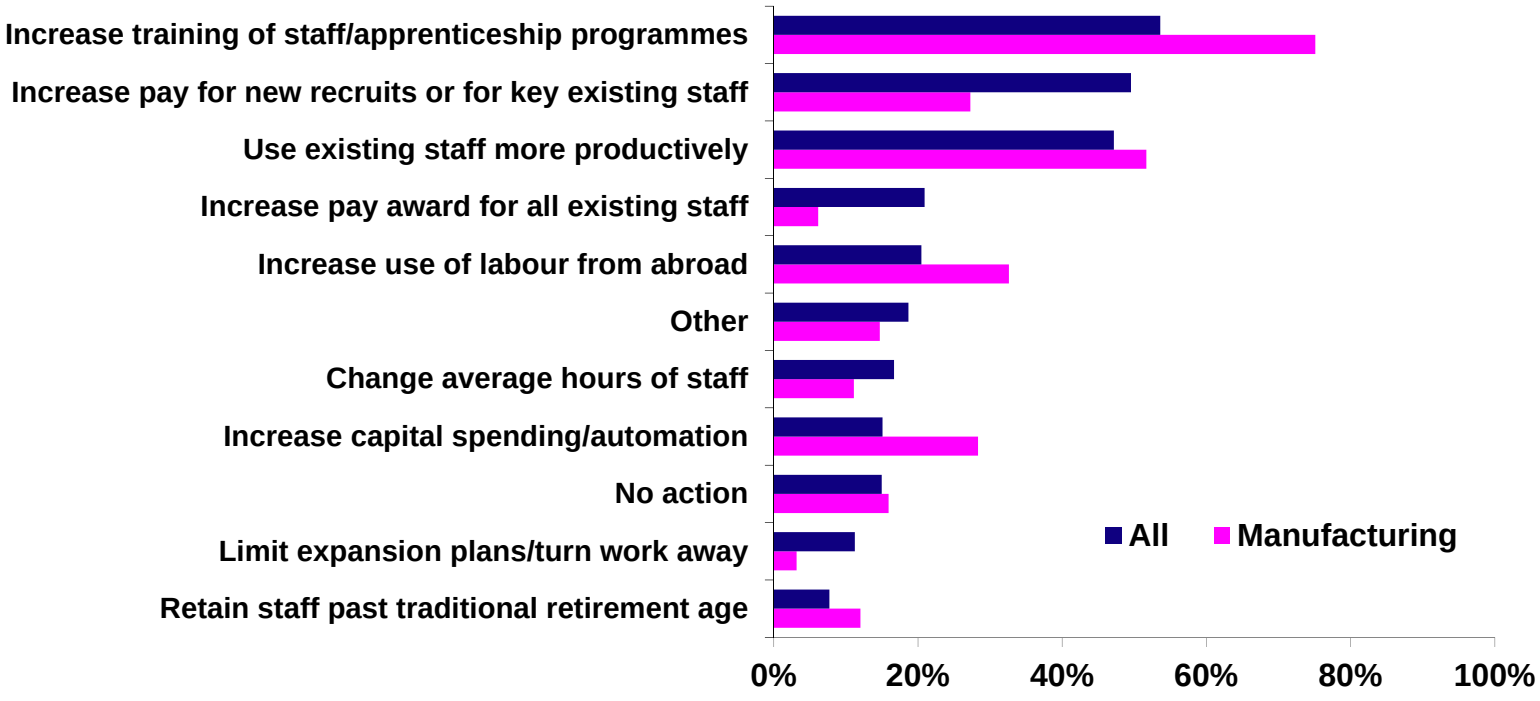
- **Employment intentions remain positive**
- **Vacancies are rising and increasingly difficult to fill**
- **Increasing recruitment difficulties are slightly restraining workforce growth**

Responses to recruitment difficulties



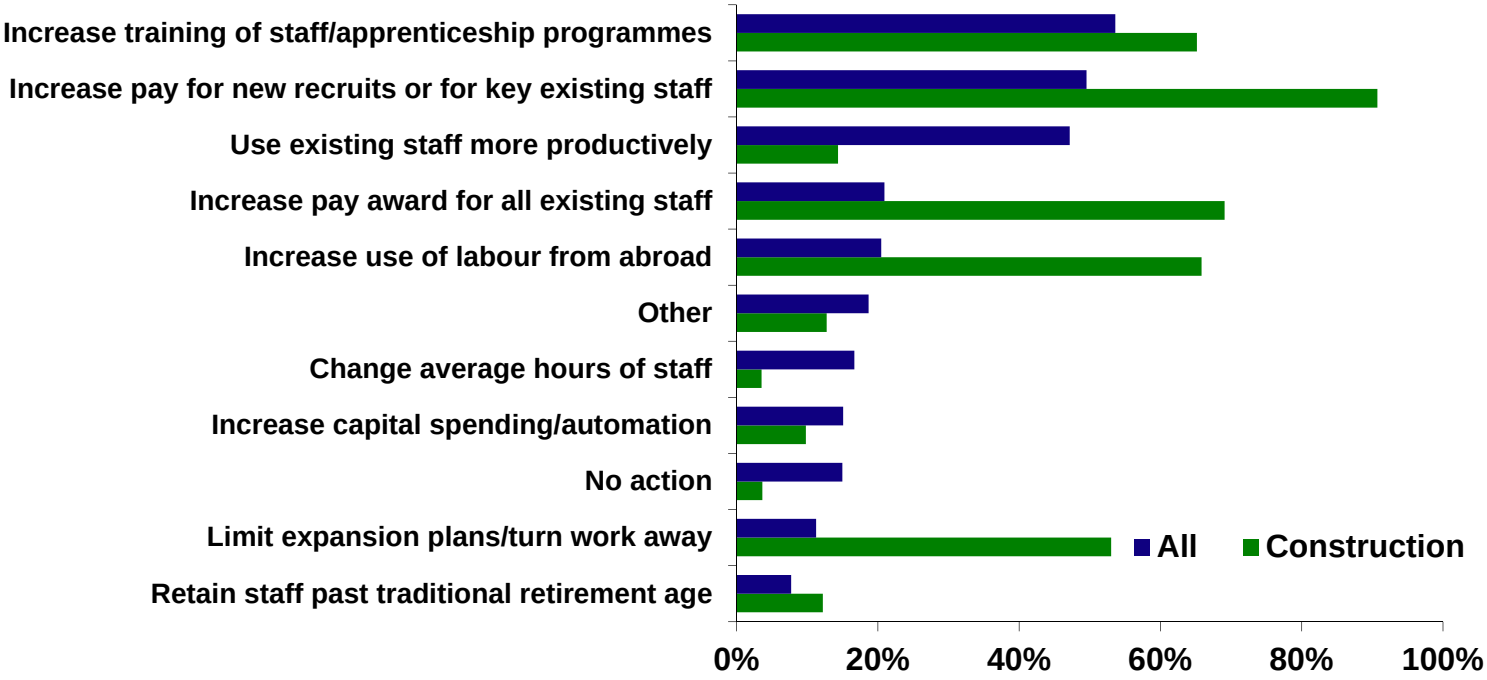
- Improving productivity and training/apprenticeships
- But also upward wage pressure

Manufacturers' responses to recruitment difficulties



- Manufacturers increasing automation and overseas labour – lower wage pressure.
- Strong use of training and apprenticeships

Construction sector responses to recruitment difficulties



- Construction pay pressure high: increasing use made of overseas labour
- Work being turned away and training ramping up

Summary

- **Employment intentions remain positive**
- **Vacancies are rising and increasingly difficult to fill**
- **Increasing recruitment difficulties are slightly restraining workforce growth**
- **Firms are responding by increasing productivity, training and apprenticeships ….**
- **…and targeting pay increases**

6: Agents’ Update

Agents' Update

30th September 2015

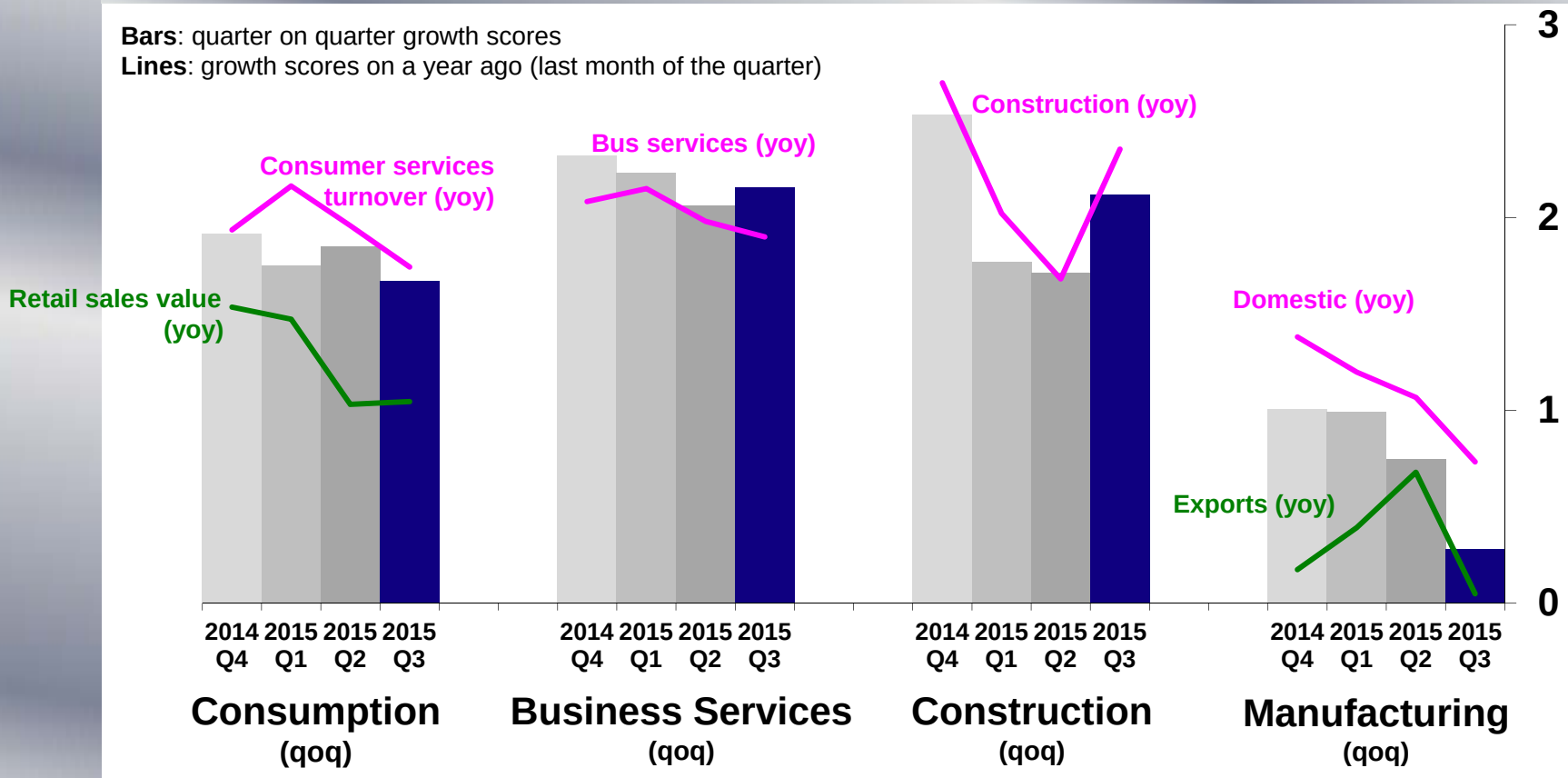
Agency for the South East & East Anglia

Inflation Report & Agency Intelligence Division

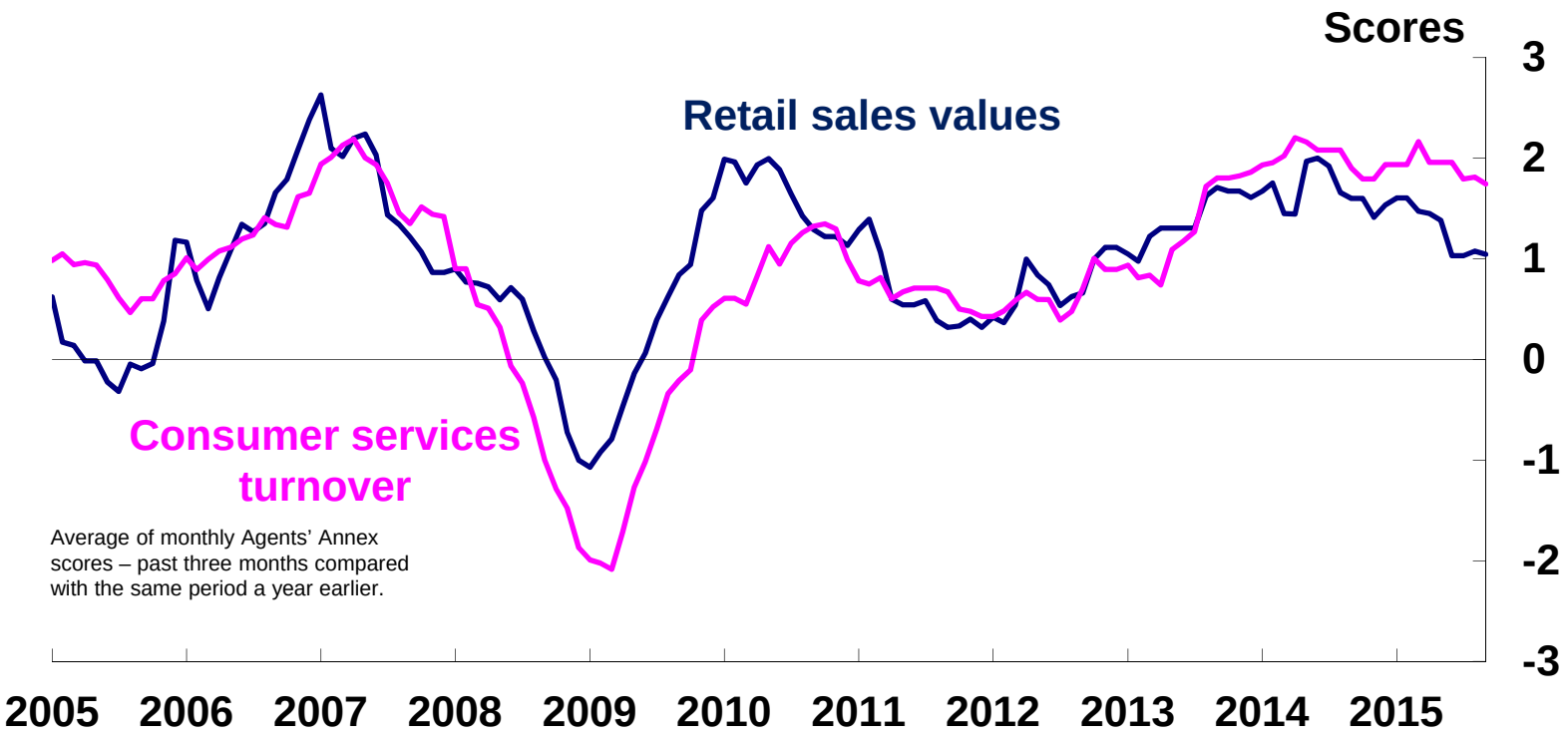
Topics

- **Activity: Quarterly & annual output**
- **Consumption**
- **Labour costs and initial thoughts on the National Living Wage**
- **China**

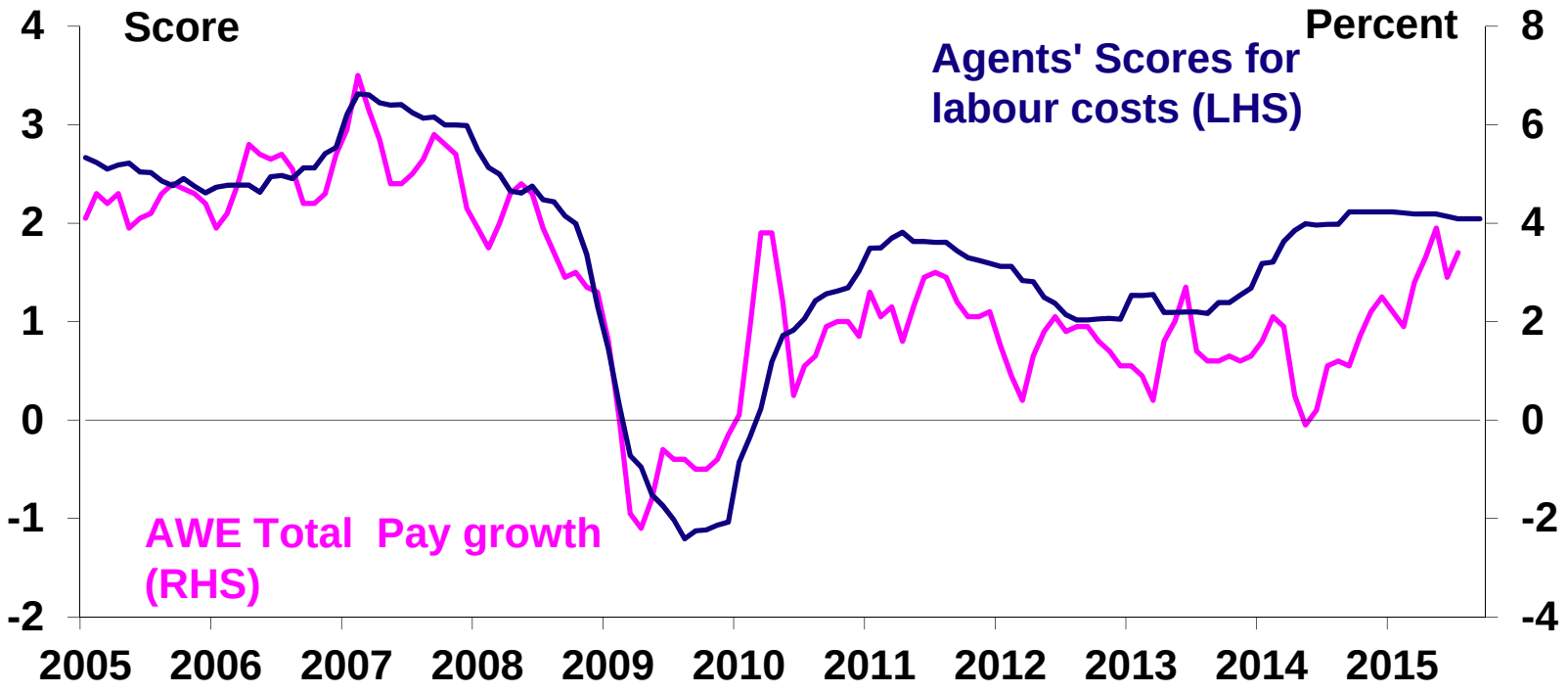
Growth Scores: qoq and yoy



Growth of Consumer Demand



Agents' scores and AWE total pay



National Living Wage (NLW)

- **Contacts report April 2016 increase as manageable with very limited near-term inflationary impact;**

- **Concerns are particularly acute in hospitality, retail and the care sectors;**

- **However, there are deep-seated concerns about the medium-term impacts of:**
  - **Maintaining pay differentials;**
  - **The compound effect of wage increases over time;**

China

- **Growth has been easing in China throughout 2015;**
- **Recent equity adjustments appear to have affected sentiment rather than further depressing activity;**
- **Respite for UK energy intensive producers and commodity consumers;**
- **Concerns about contagion effects persist.**

Summary

- **Q3 output growth broadly in line with Q2;**
- **Consumption volume growth stable;**
- **National Living Wage more of a concern to contacts after next year's wage round;**
- **Chinese concerns pre-date recent equity market adjustments.**

7: External Commentators

8: Demand & Output

Blue Book 2015, Demand and Output

October 2015

CAPD and SEAD

Outline

1) Headline news in the Blue Book: GDP, productivity, slack and inflationary pressure

2) How has the Blue Book affected the composition of growth?

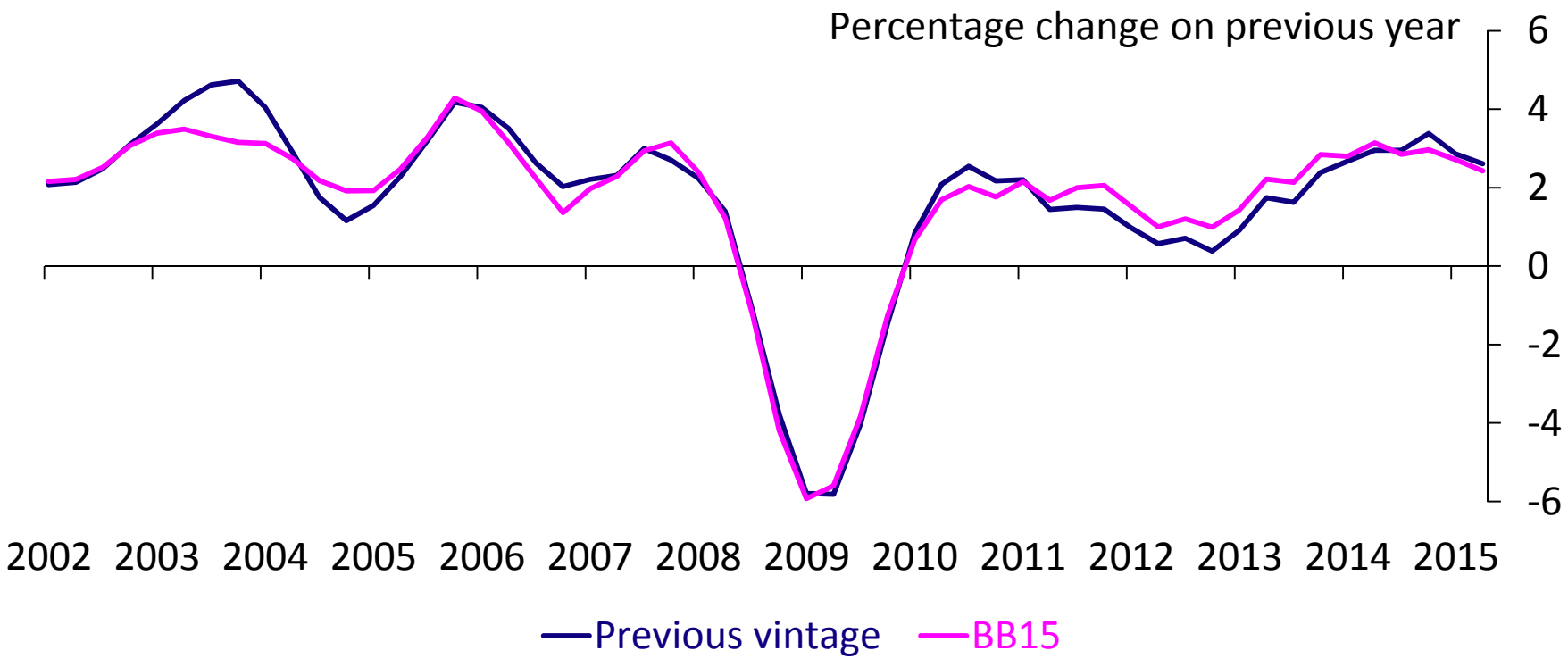
3) Update on the short-term outlook

What is in Blue Book 2015?

	Not that important	Somewhat important	Very important
Affects GDP	-Illegal drugs -Local government pensions -Alcohol and tobacco consumption -CPIH alignment -Consumption of fixed capital on roads -Vehicle registration tax -Smuggling -Non-monetary gold -Reclassifications (e.g. Network Rail, TFL) -Dwellings repair & maintenance -Software investment deflator	-Valuables PYP chain-linking -Insurance industry output -NPISH measurement improvement -R&D investment -Stamp duty	**Exhaustiveness** - undercoverage of small businesses - concealed income
GDP neutral	-Reclassifications (e.g. 3G/4G spectrum sales)	-Cross-border property	NA

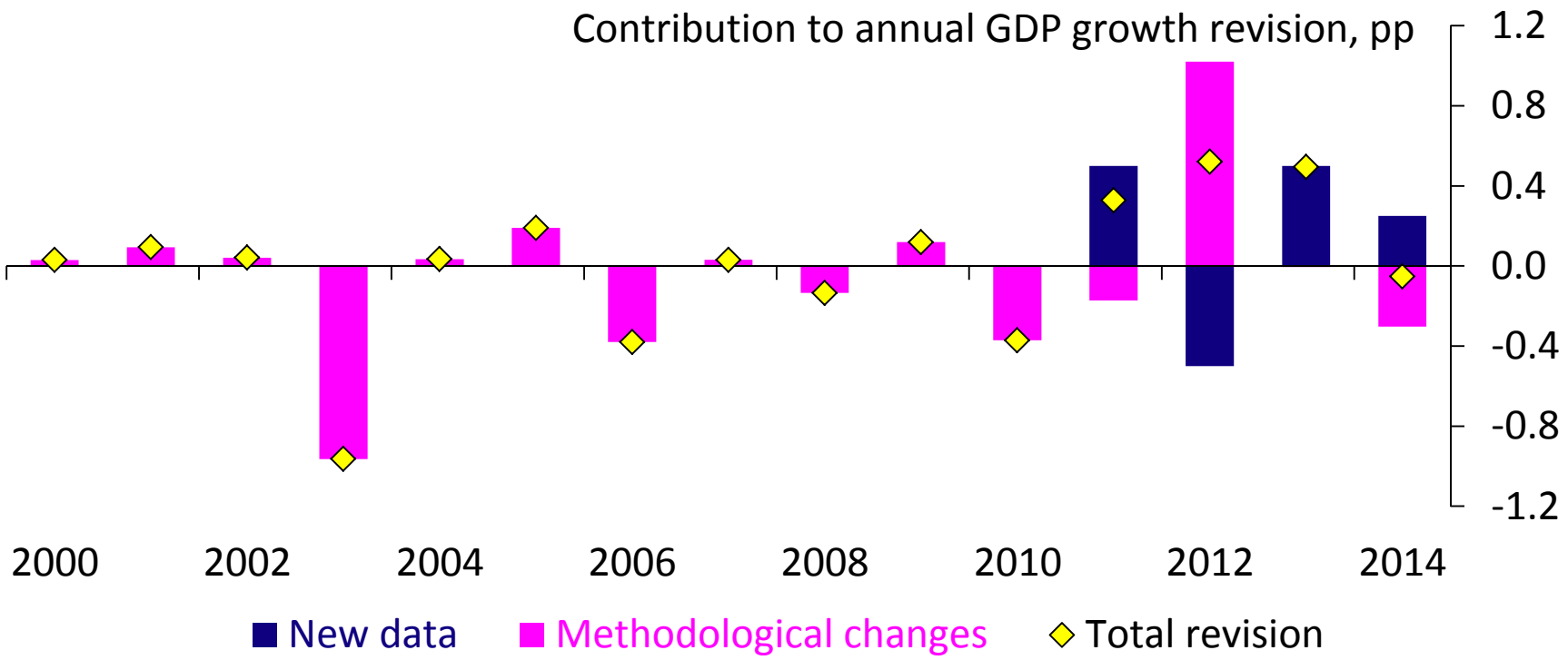
NB This list is not exhaustive

Annual real GDP growth



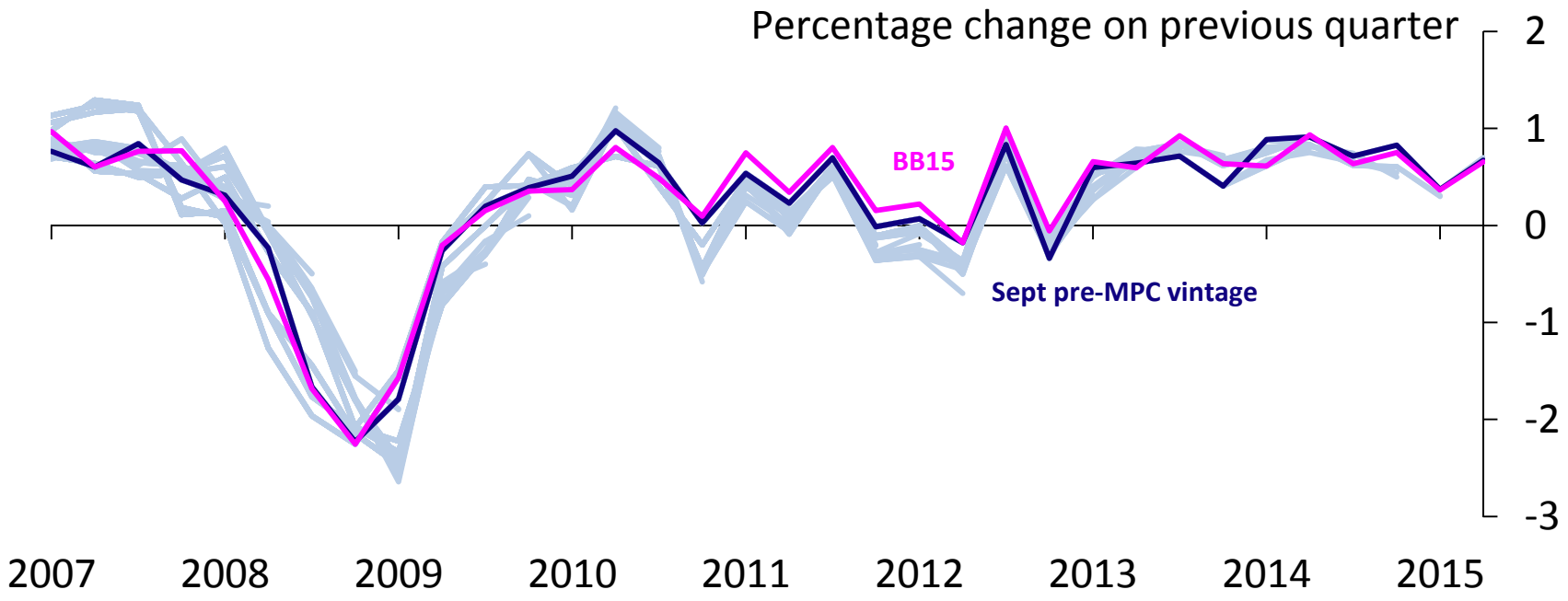
- Growth is stronger over 2011-2013, but little changed in 2015 H1

Indicative source of real GDP growth revisions



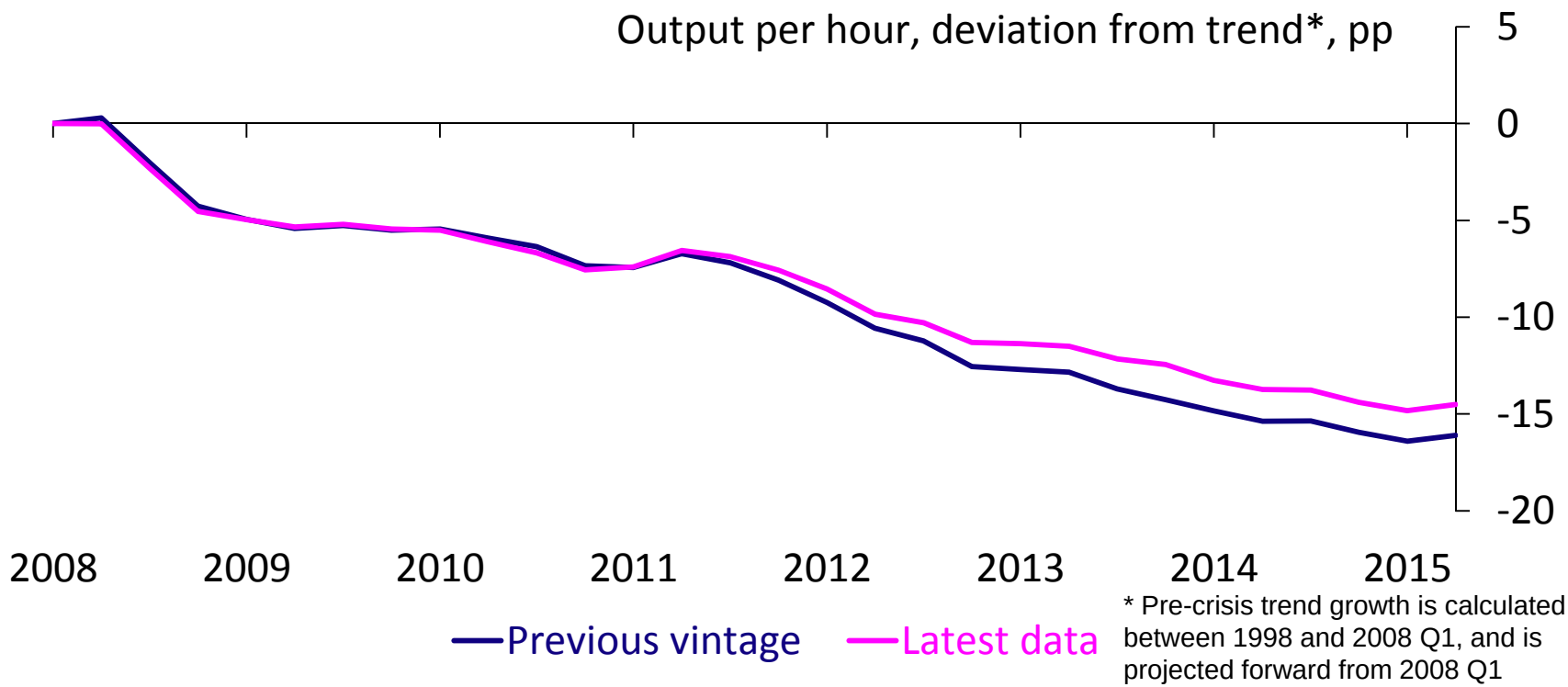
- Although the average revision to annual growth is 0.0pp, the revisions to later years tend to reflect new data or improved exhaustiveness adjustments

Quarterly real GDP growth



- Quarterly GDP growth unrevised in 2015 Q1 and Q2

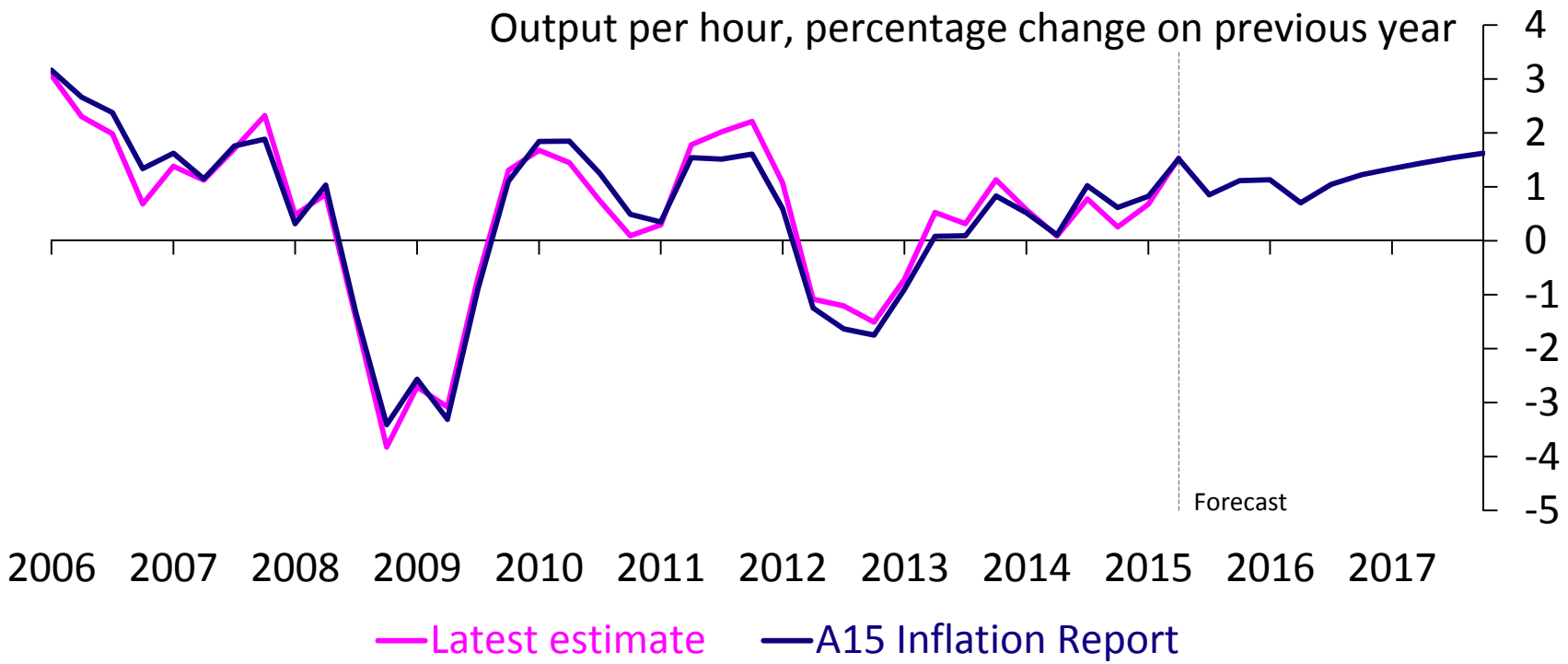
Productivity puzzle



* Pre-crisis trend growth is calculated between 1998 and 2008 Q1, and is projected forward from 2008 Q1

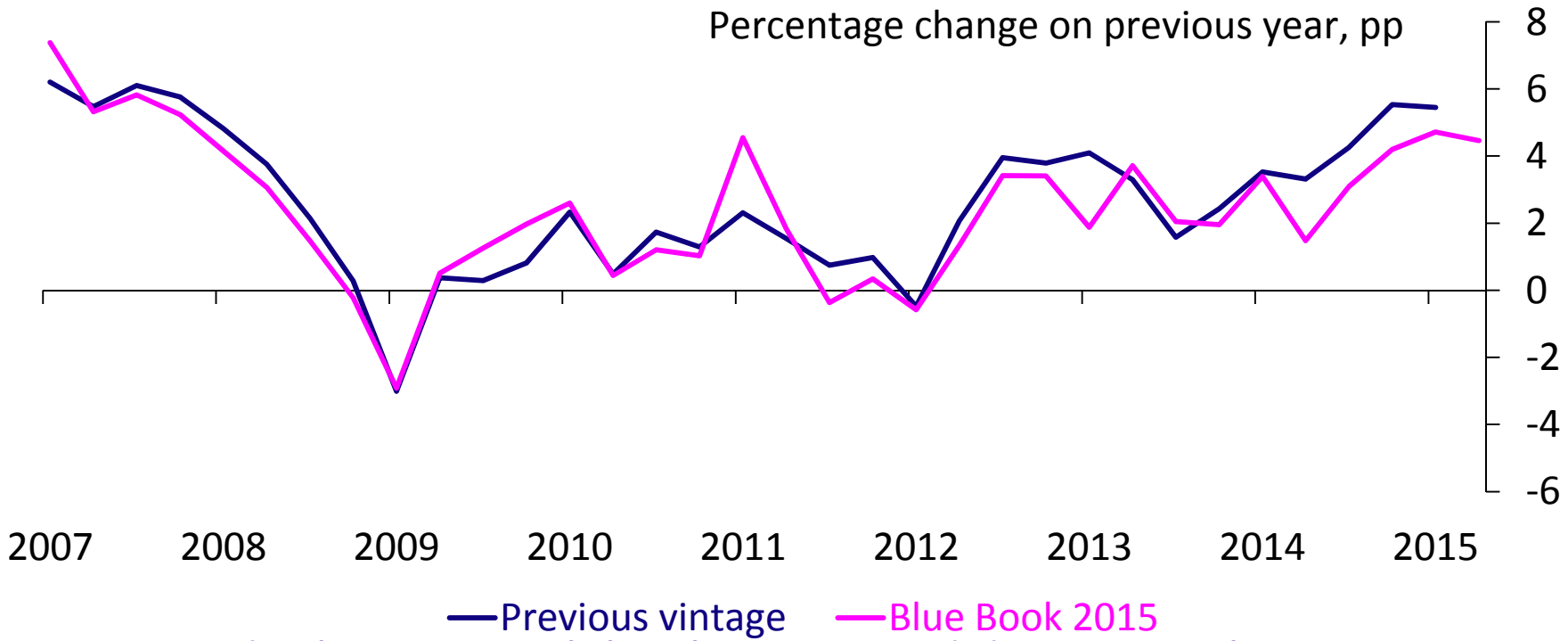
- Productivity remains 15% below the level implied by its pre-crisis trend

Productivity growth



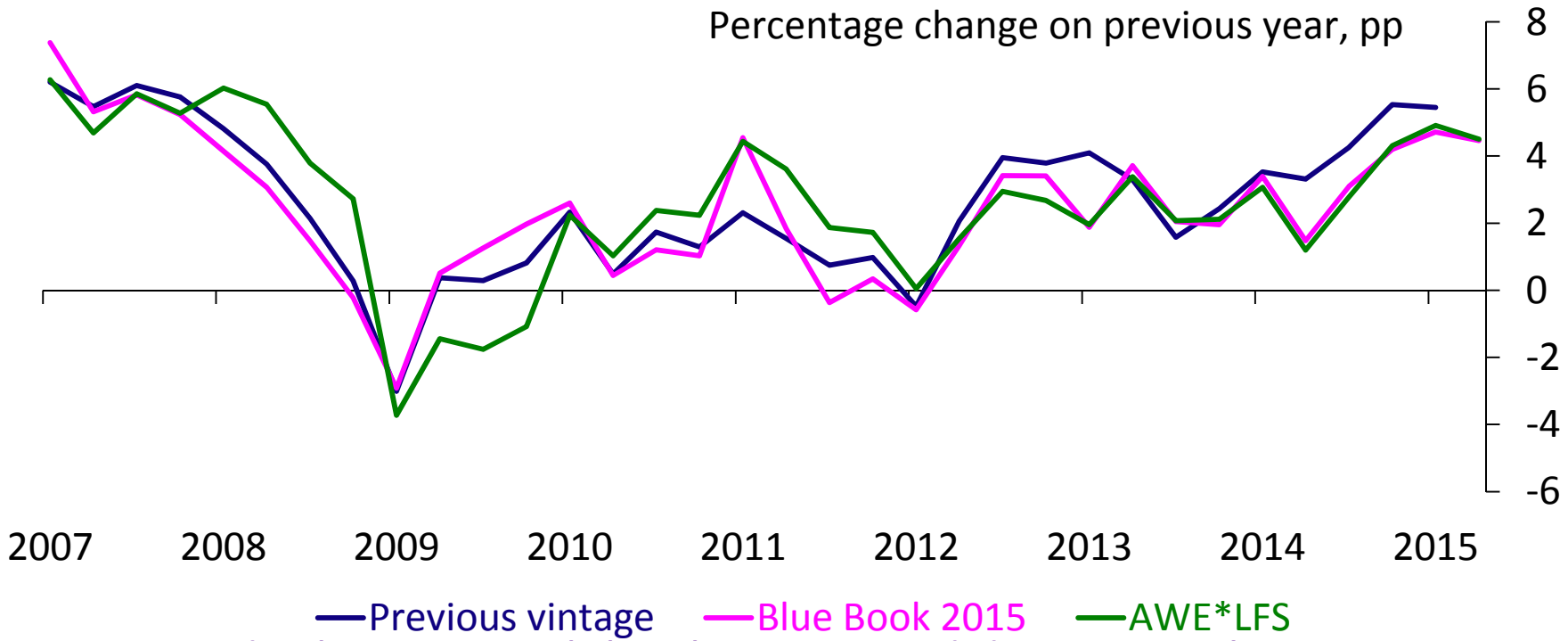
- We estimate annual productivity growth was 1.5% in Q2

Wages and salaries



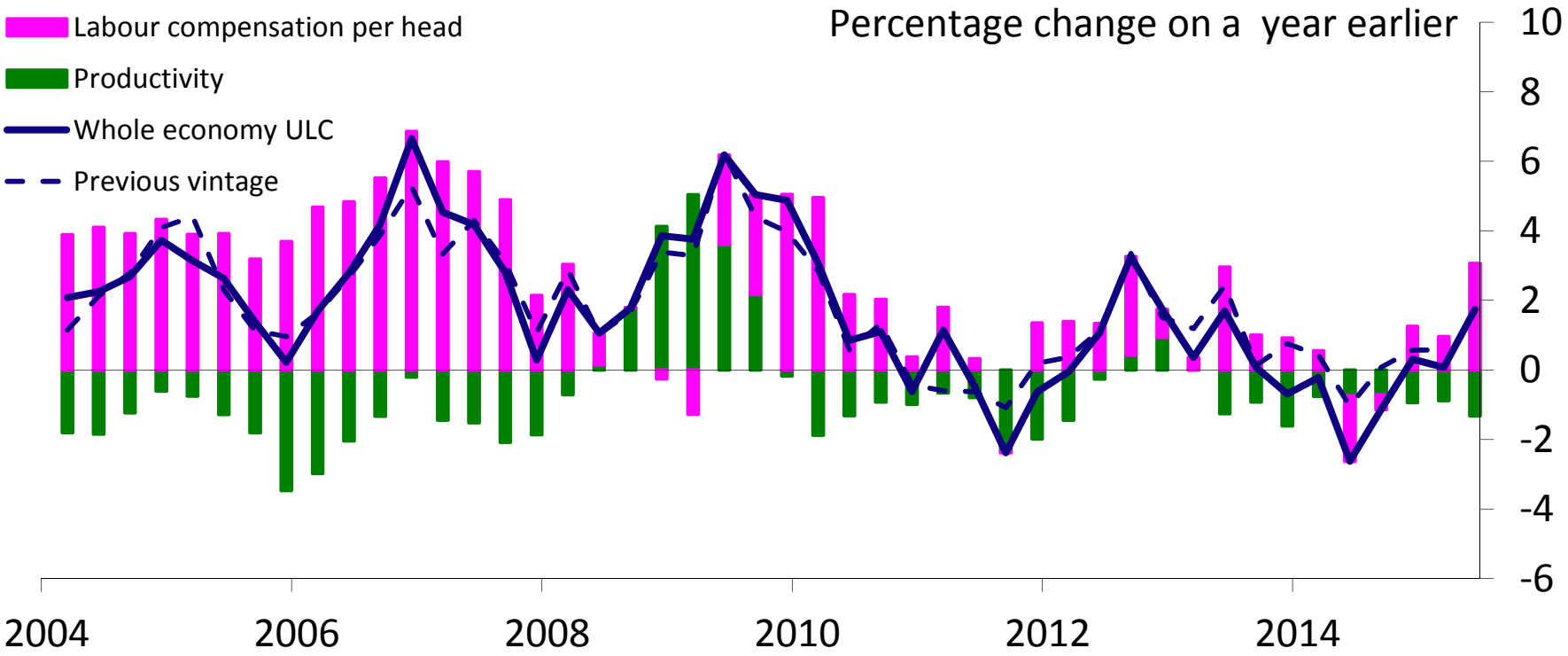
- Wages and salaries growth has been revised down over the past year, and is now in line with an AWE*LFS proxy

Wages and salaries



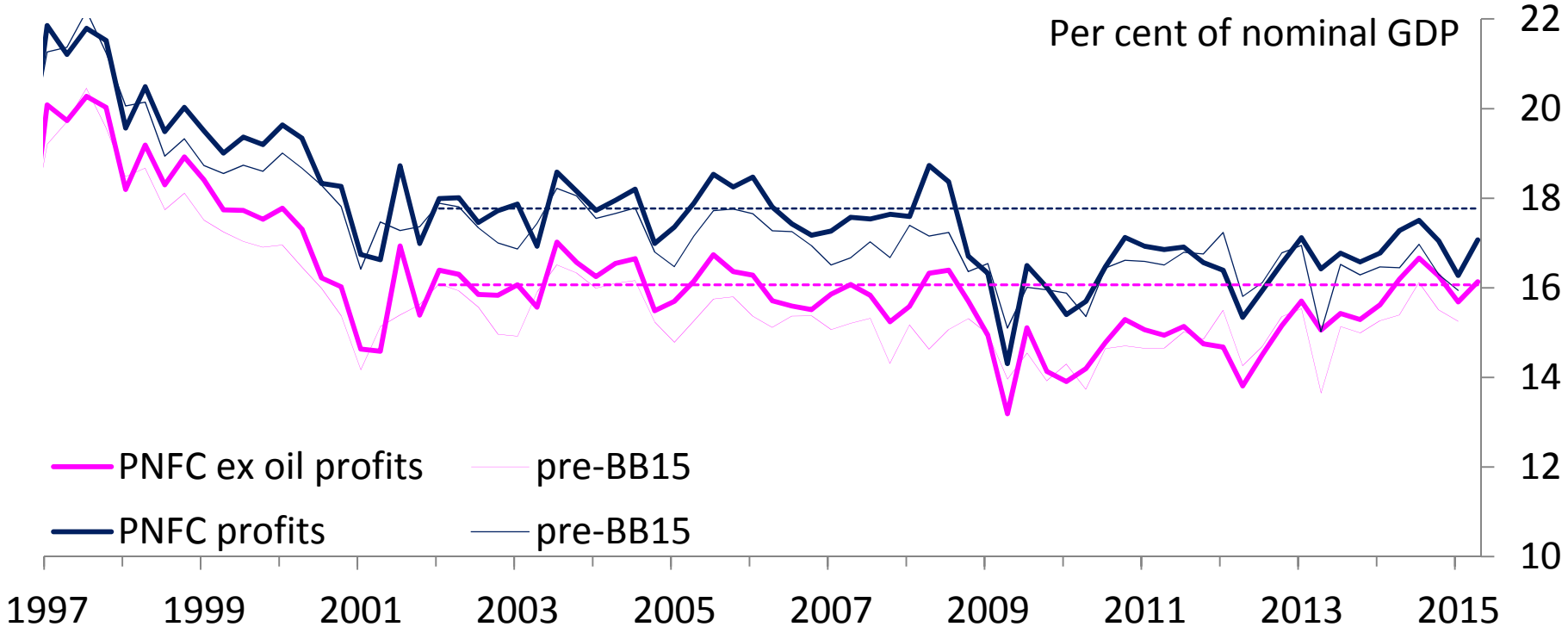
- Wages and salaries growth has been revised down over the past year, and is now in line with an AWE*LFS proxy

Annual growth in whole economy ULCs



- Unit labour cost growth is a little lower over the past two years, largely as a result of the revisions to income growth

PNFC profit shares

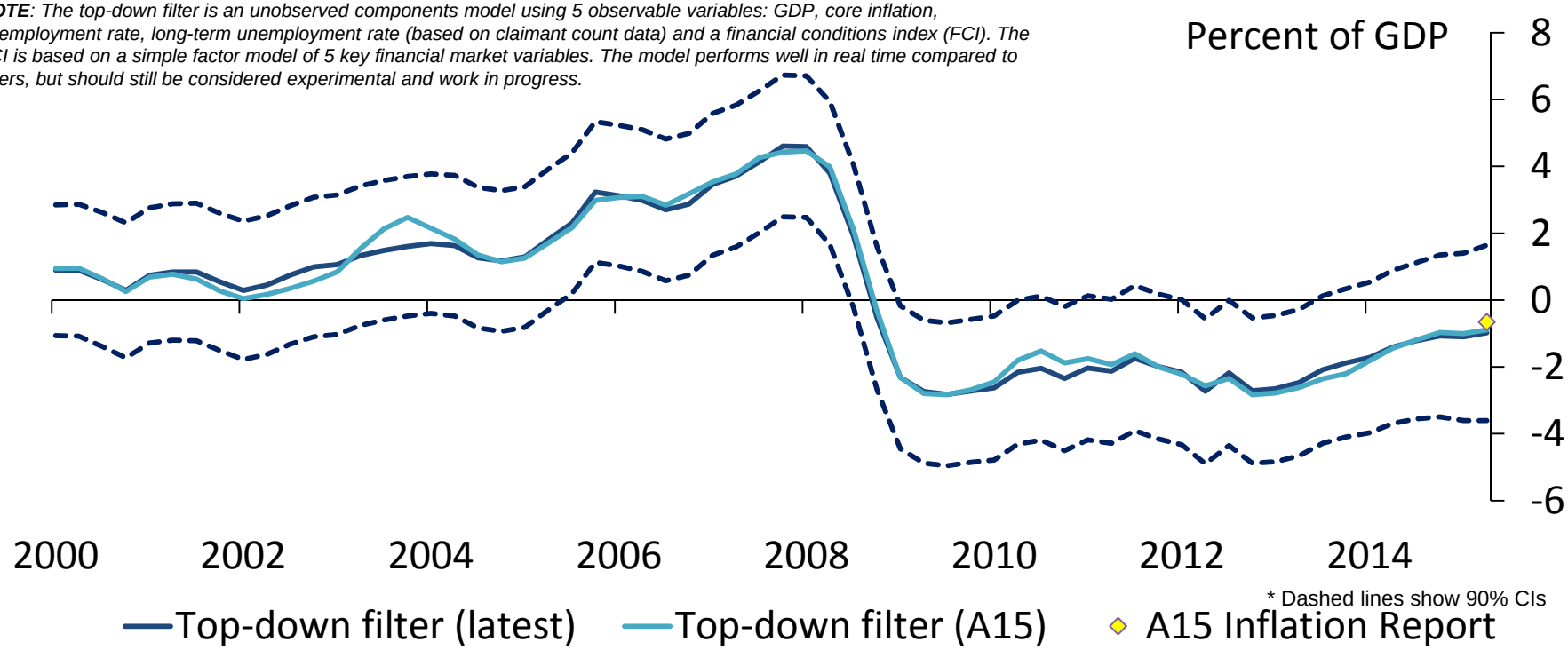


Dashed lines show BB15 pre-crisis averages over the period 2002-2007

- The PNFC ex. oil profit share has been revised up and is now around its 2002-07 average

Filter estimates of output gap

***NOTE**: The top-down filter is an unobserved components model using 5 observable variables: GDP, core inflation, unemployment rate, long-term unemployment rate (based on claimant count data) and a financial conditions index (FCI). The FCI is based on a simple factor model of 5 key financial market variables. The model performs well in real time compared to peers, but should still be considered experimental and work in progress.*

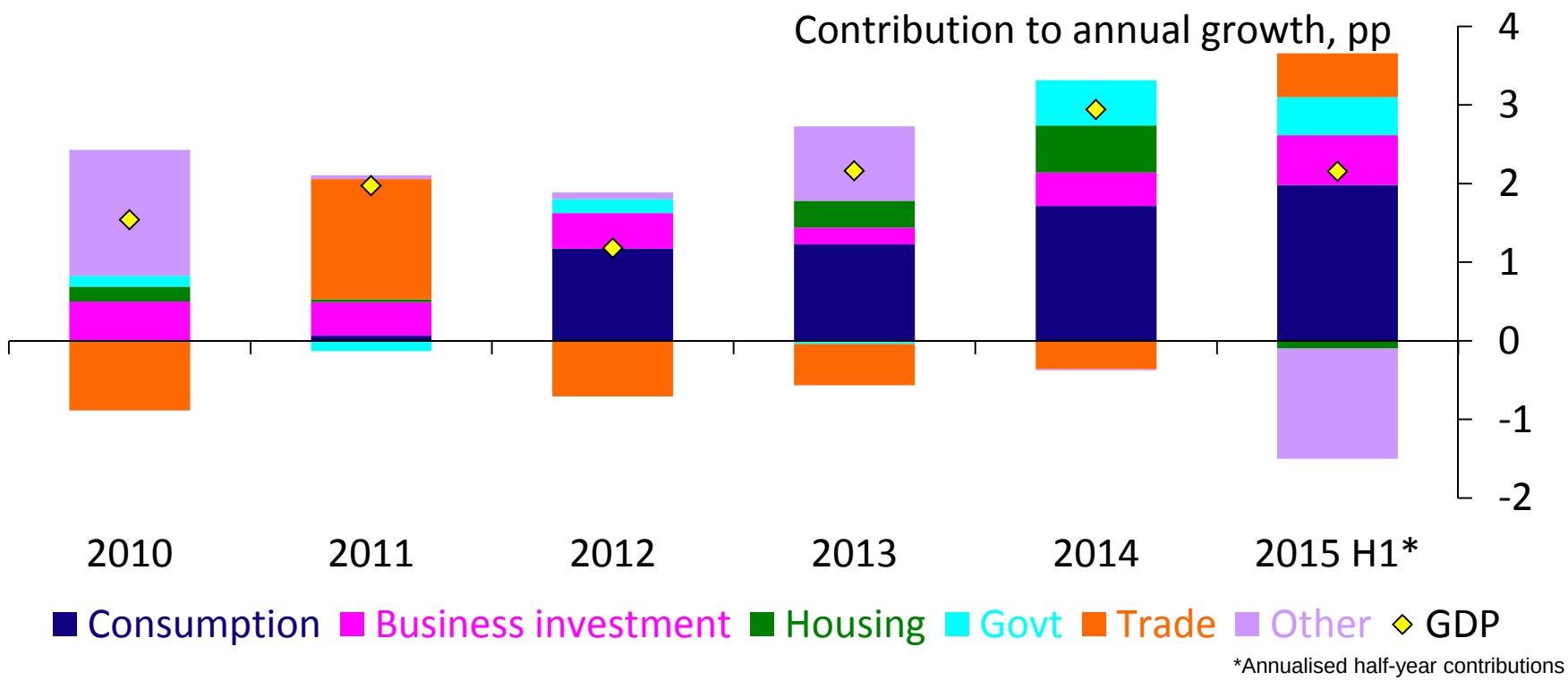


- The latest top-down estimate of the output gap is -1.0%. The 90% confidence interval extends from -4% to 2%.

Outline

1) Headline news in the Blue Book: GDP, productivity, slack and inflationary pressure
   - GDP growth a little stronger over 2011-13, but similar in 2014-15 H1
   - Productivity puzzle slightly smaller, as expected
   - ULC growth weaker, profit share higher
   - Top down output gap -1.0% in Q2

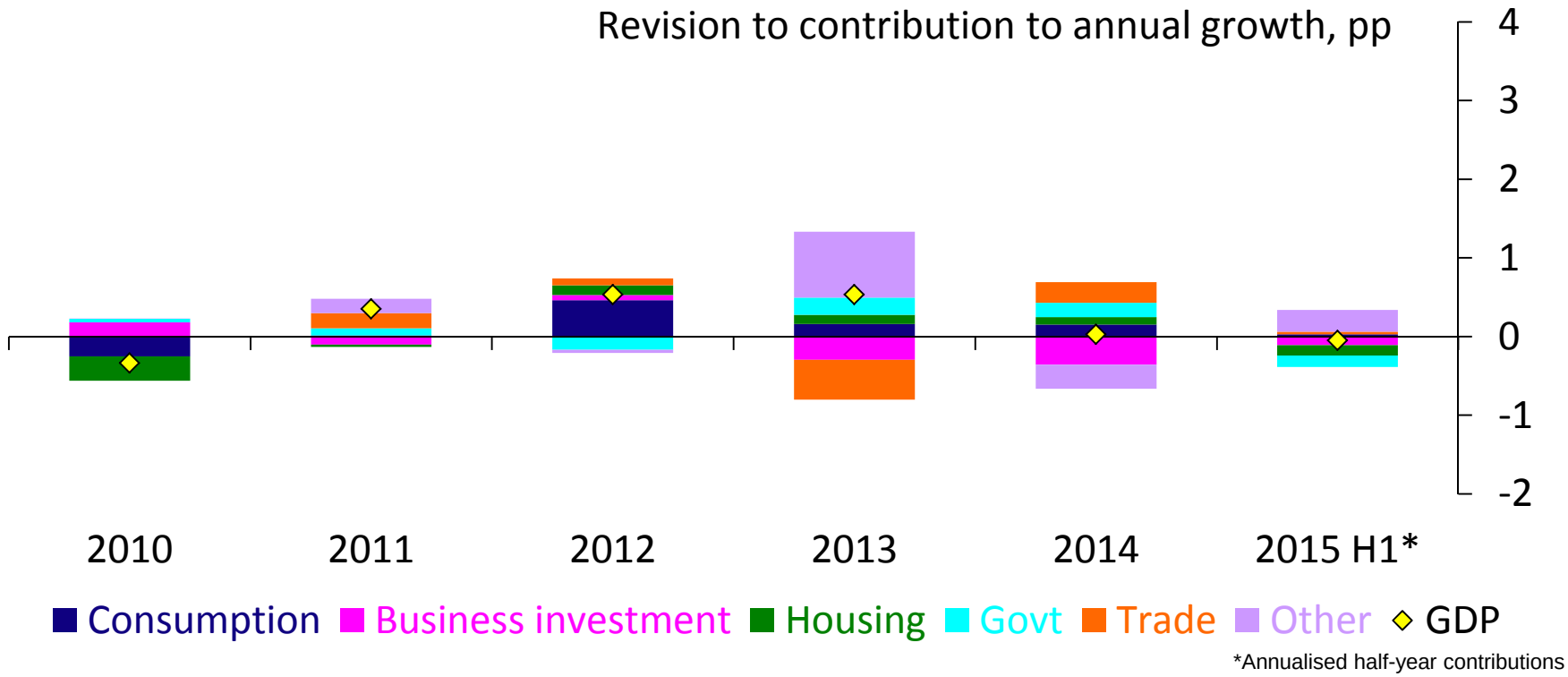
Expenditure composition of GDP



*Annualised half-year contributions

- The recovery from 2013 has been driven by private domestic demand

Revisions to expenditure data



- The composition of GDP growth has not changed significantly

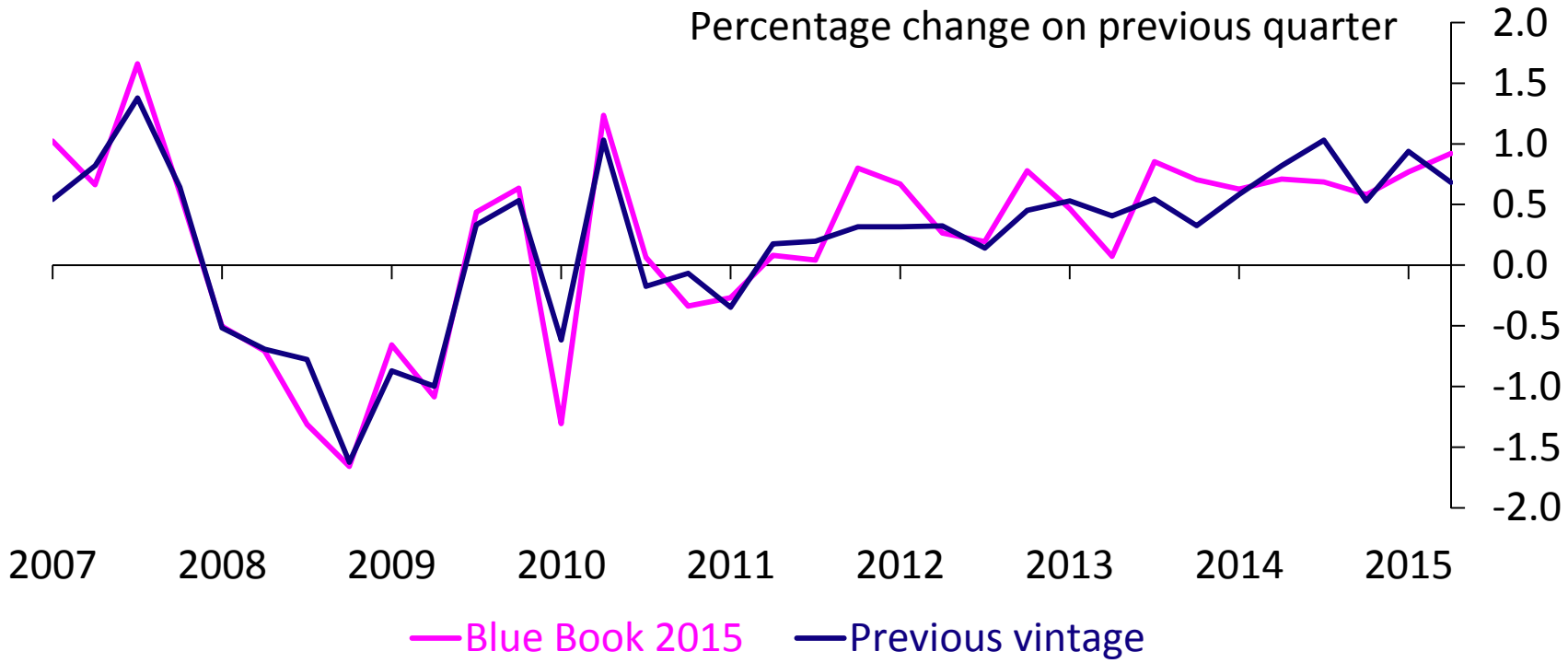
Q2 2015 expenditure split

Q2 expenditure breakdown				
	2nd Release	QNA	Revision	Aug *IR* ^
GDP^	0.7	0.7	0.0	0.7
Consumption	0.7	0.9	0.2	0.9
Government consumption	0.9	0.4	-0.5	0.0
Investment				
o/w business	2.9	1.6	-1.3	0.9
o/w housing	-3.5	-2.7	0.8	1.2
o/w government	0.2	2.7	2.5	0.0
Net trade*	1.0	1.4	0.4	1.1
Stockbuilding (excl AA)*	-1.2	-0.7	0.4	-0.9
AA*	0.0	-0.6	-0.6	-0.1

*contribution to GDP growth

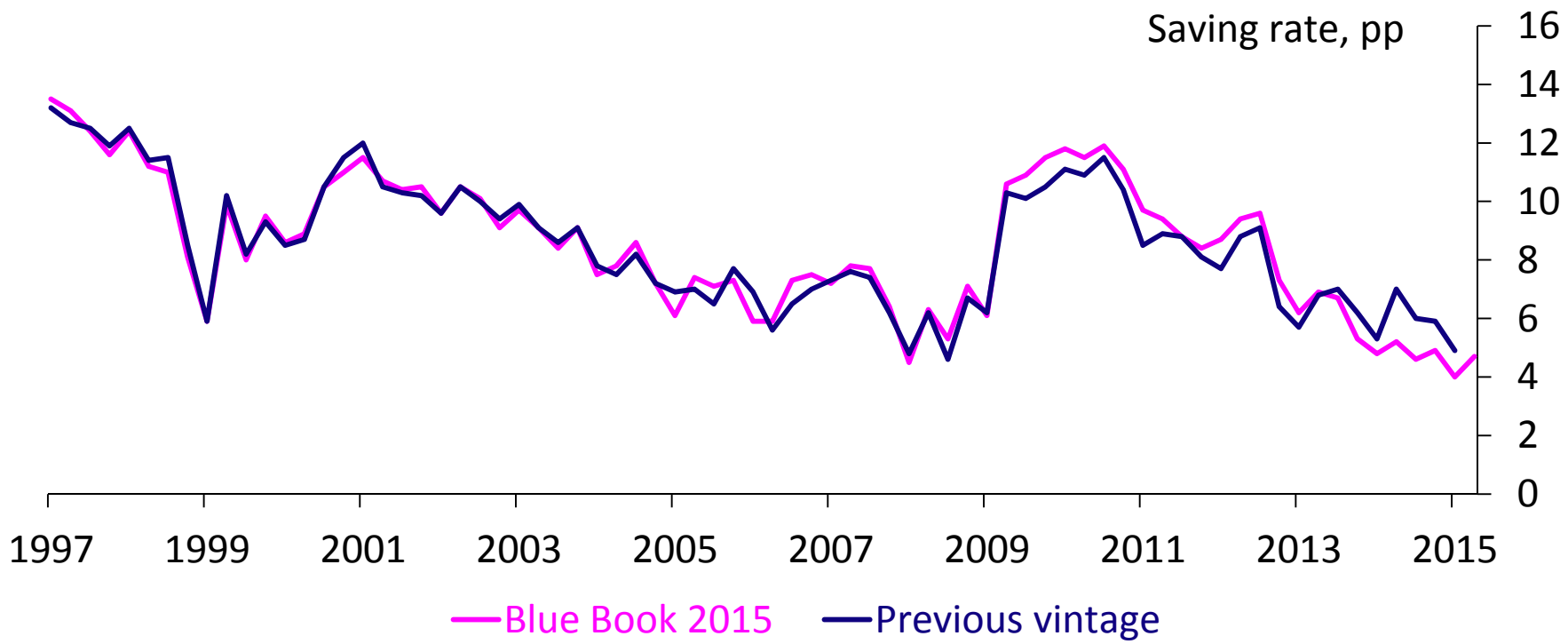
^final estimate

Quarterly consumption growth



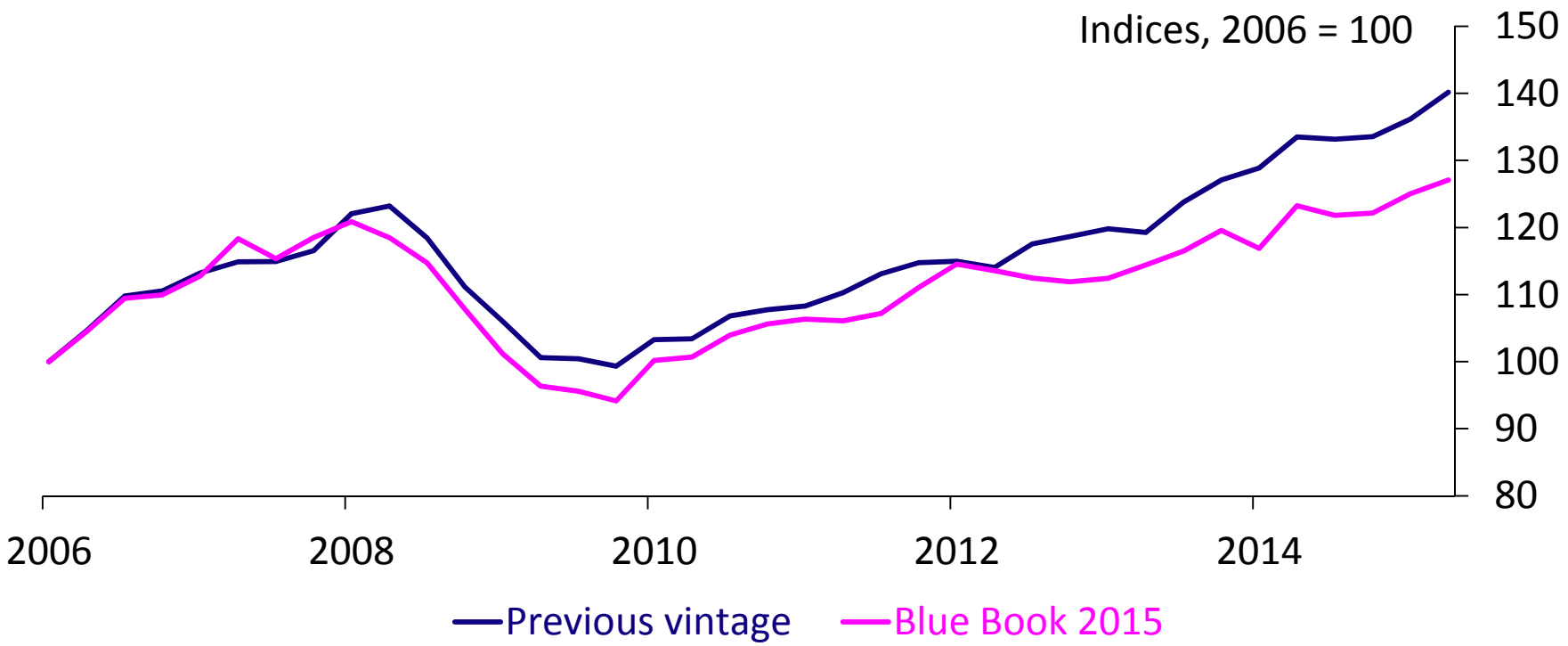
- Consumption growth picked up to 0.9% in Q2 in the latest vintage, in line with the August IR

Saving ratio



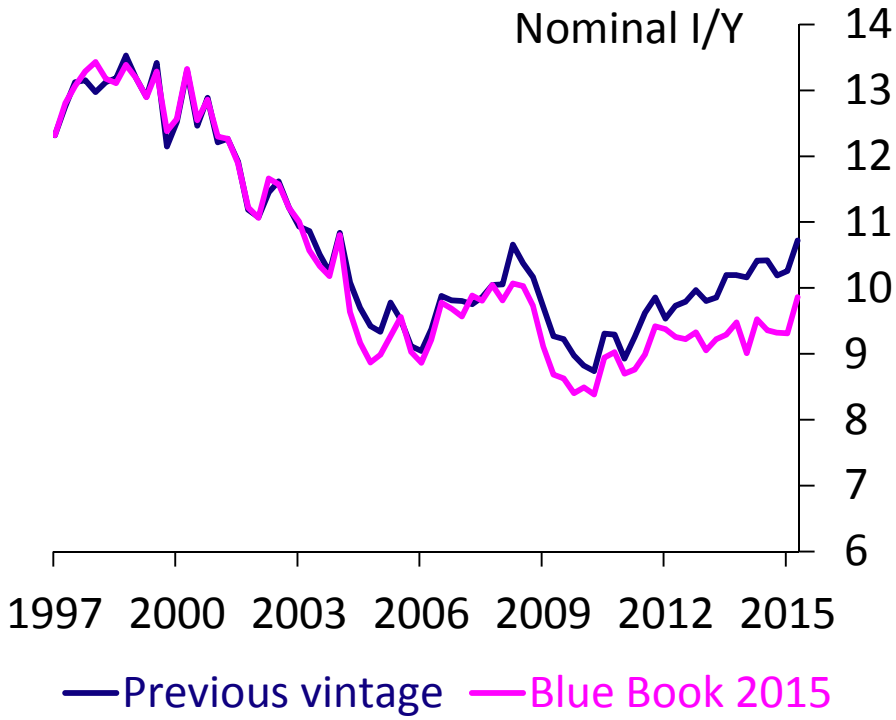
- The saving ratio has been revised down over the past year or so, and was 4.7% in Q2

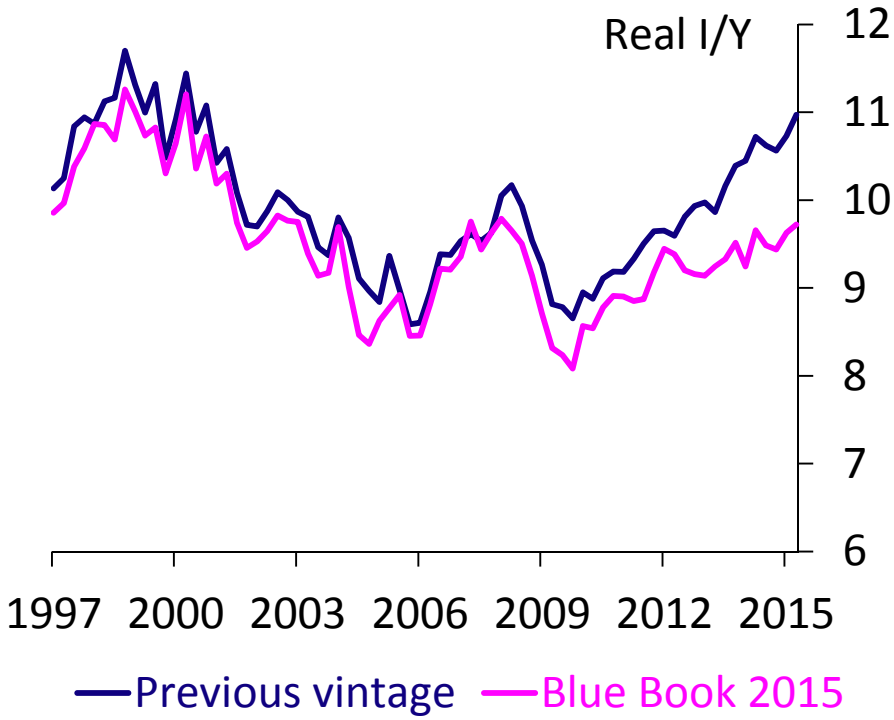
Real business investment



- Quarterly business investment is now estimated to have grown by 35% since 2009 Q4 (previously 41%)

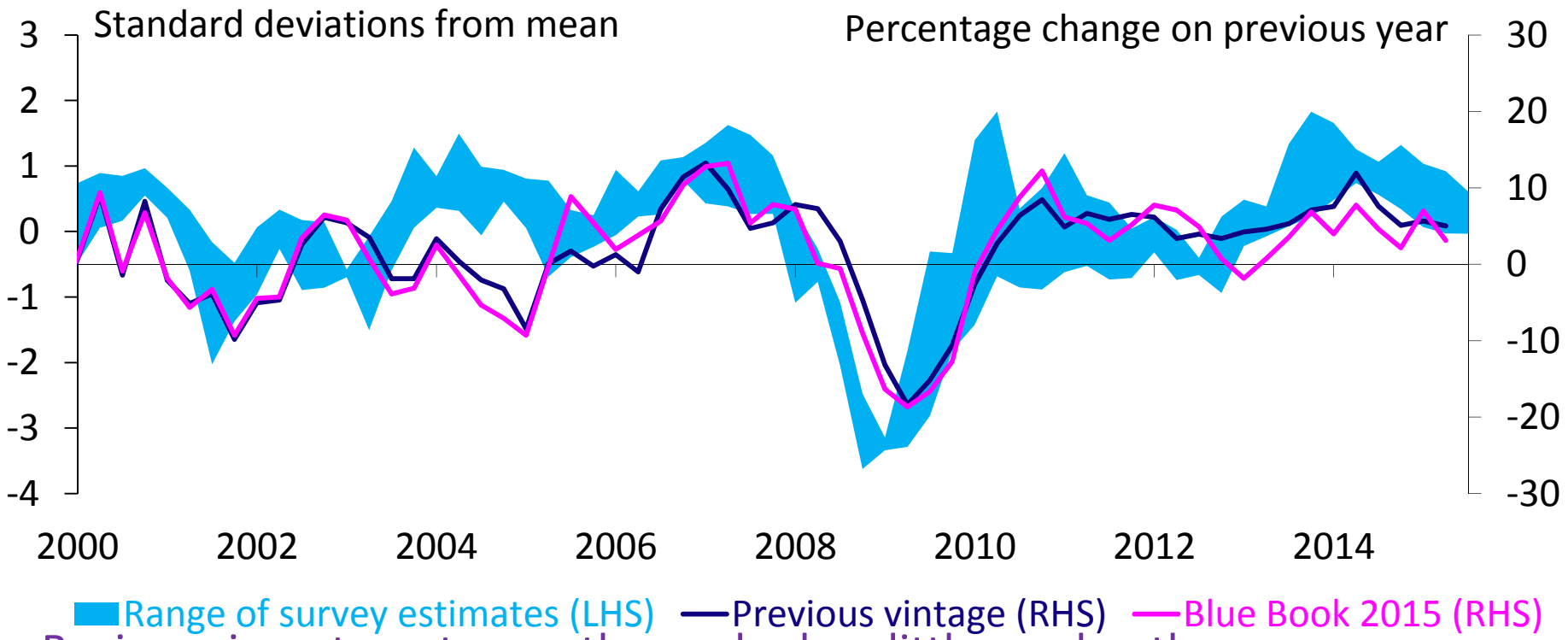
Business investment share of GDP





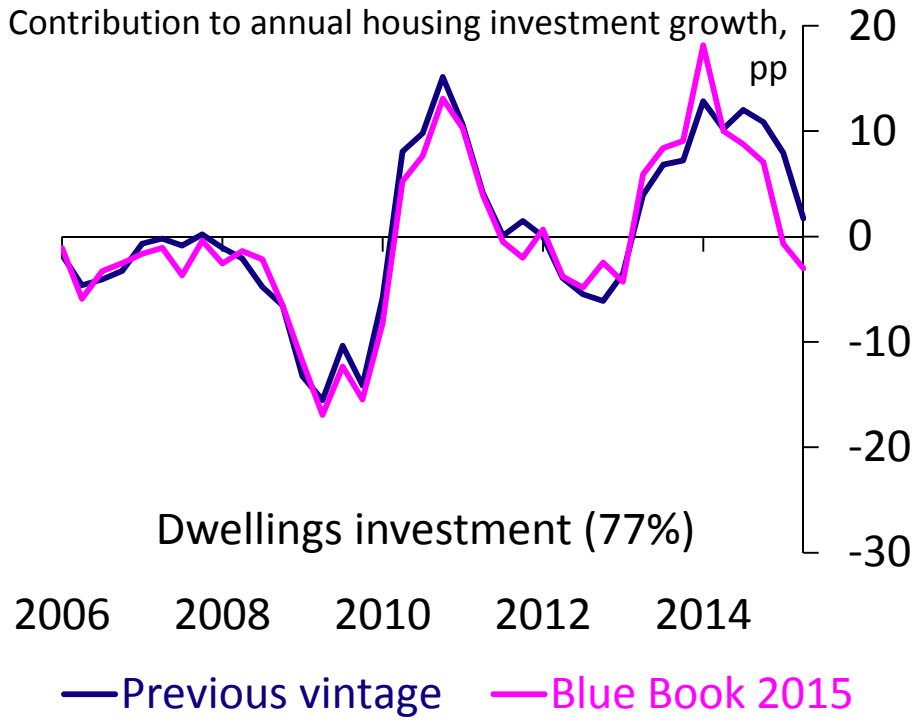
- Ratio of business investment to GDP has been lowered

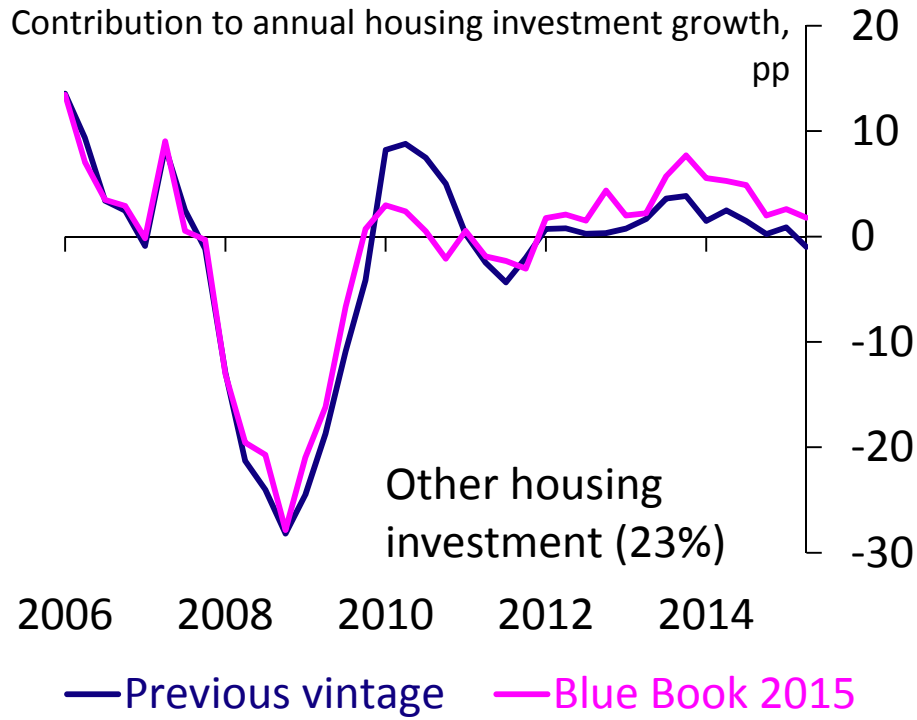
Investment intentions surveys



- Business investment growth now looks a little weaker than our survey indicators over 2013-14

Housing investment

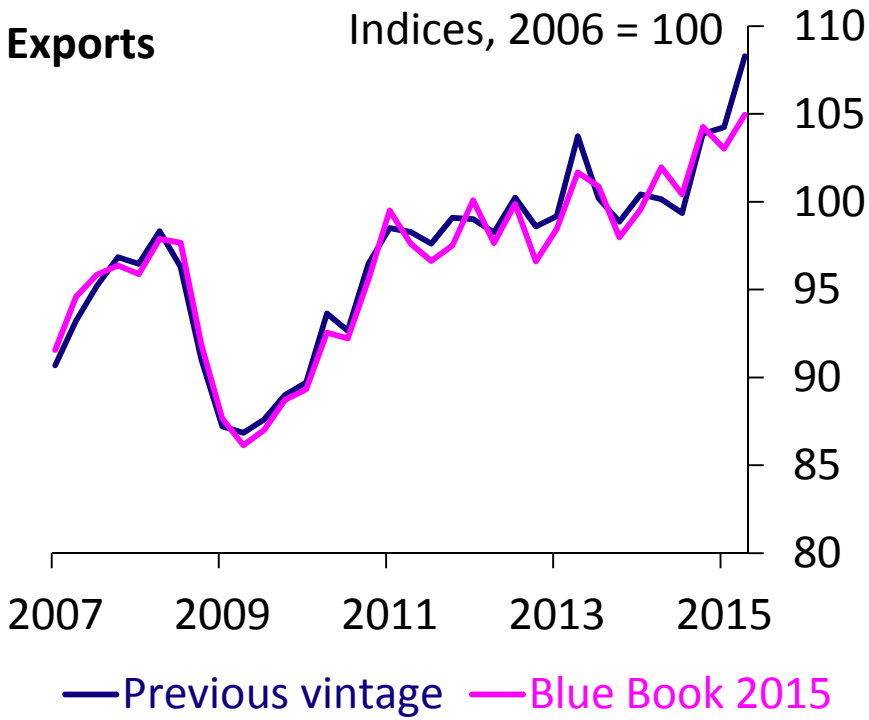


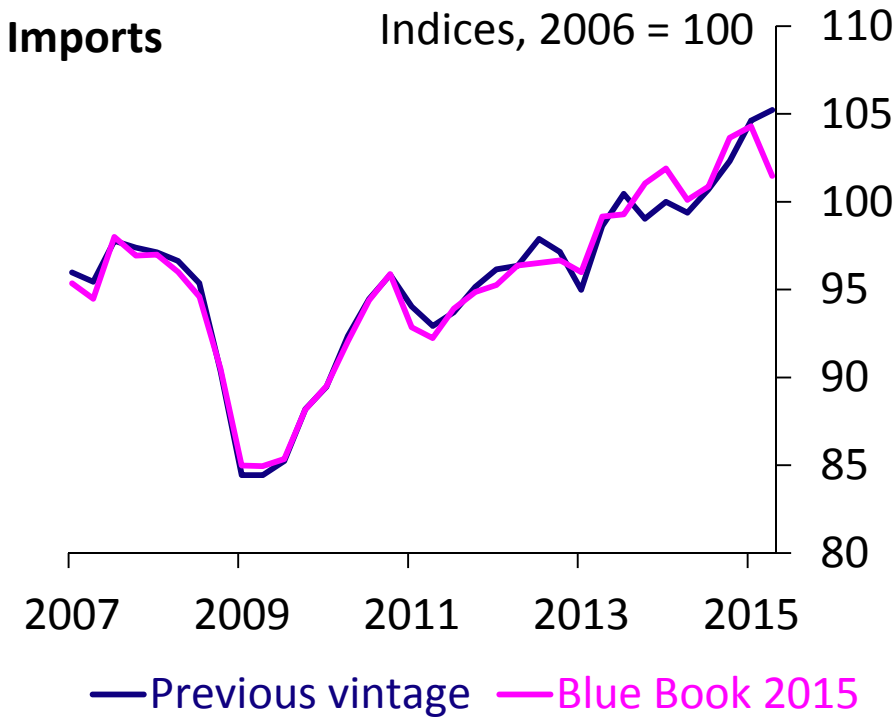


NB Numbers is parentheses are shares of total housing investment in 2014

- Total housing investment growth is little revised, although updated stamp duty data have increased the contribution of 'other housing investment' recently

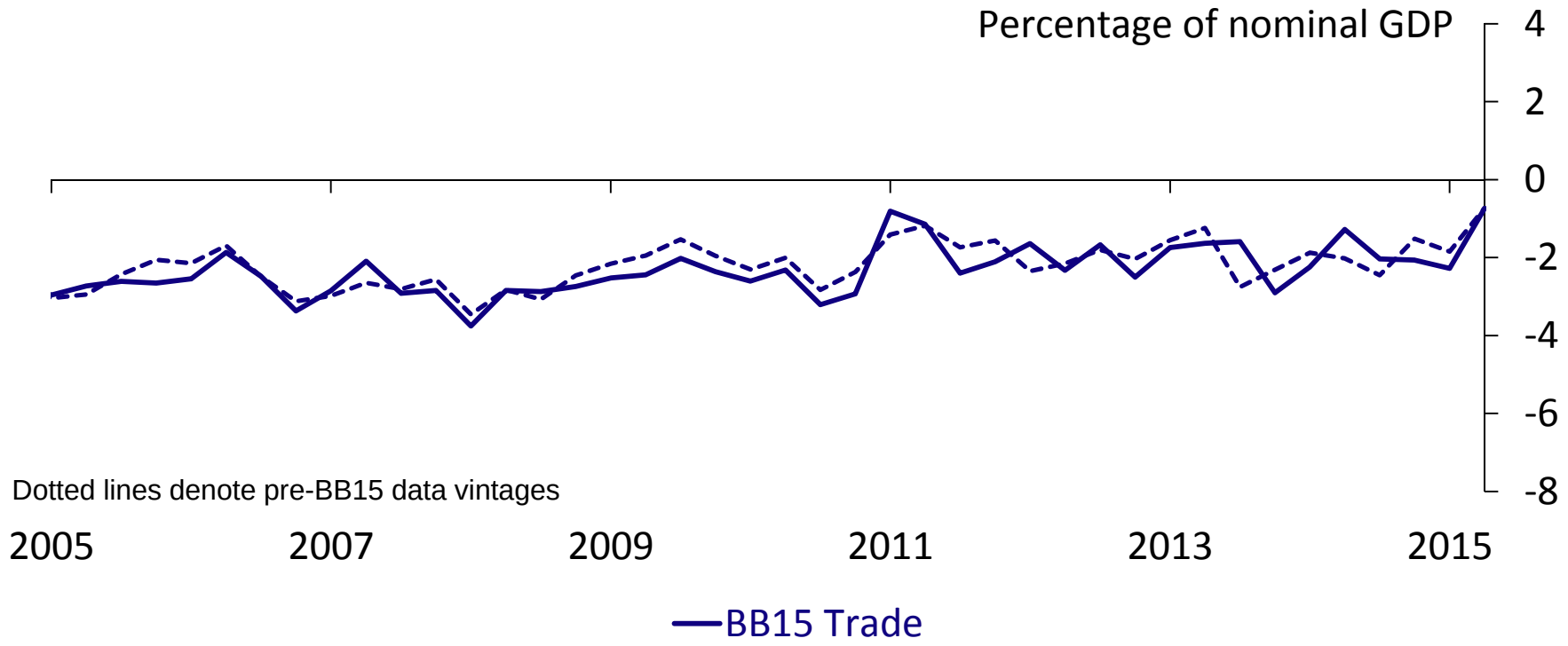
Exports and imports





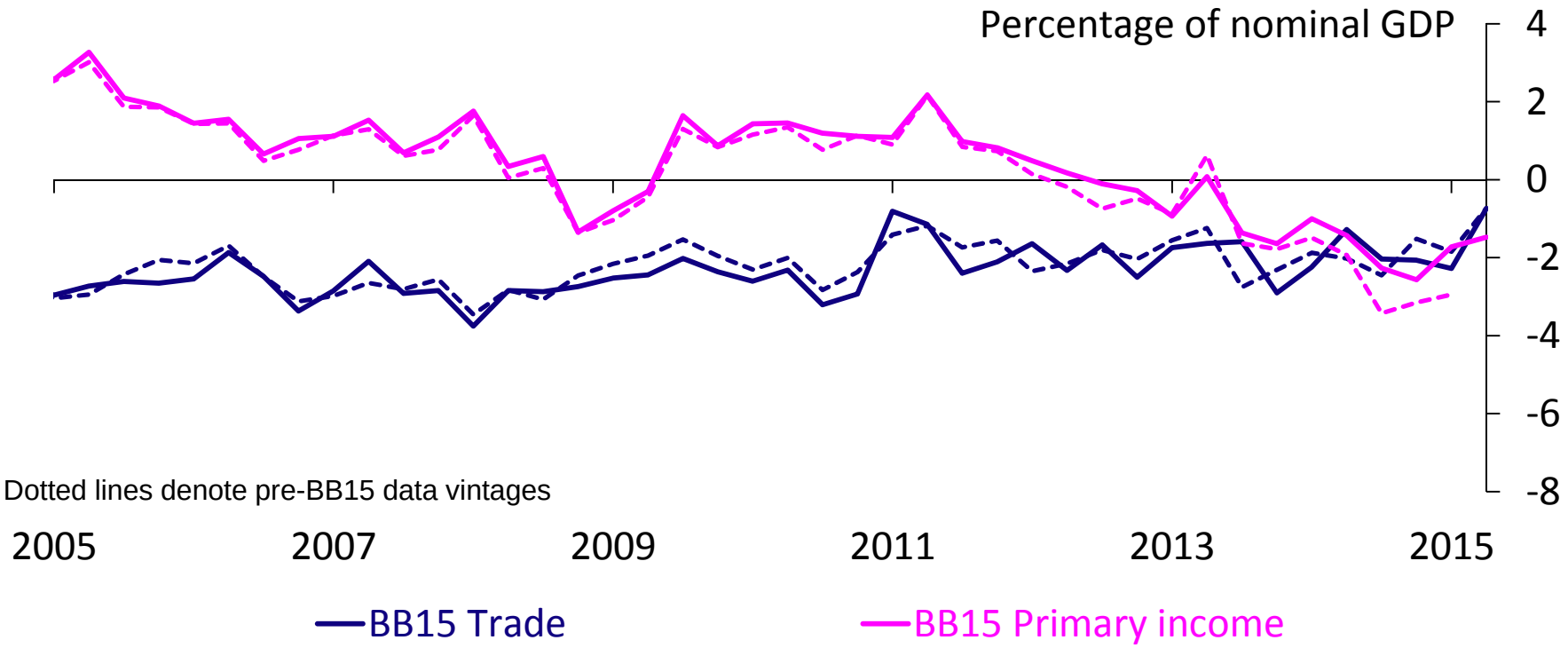
- The level of exports and imports were both revised down in Q2

Current account



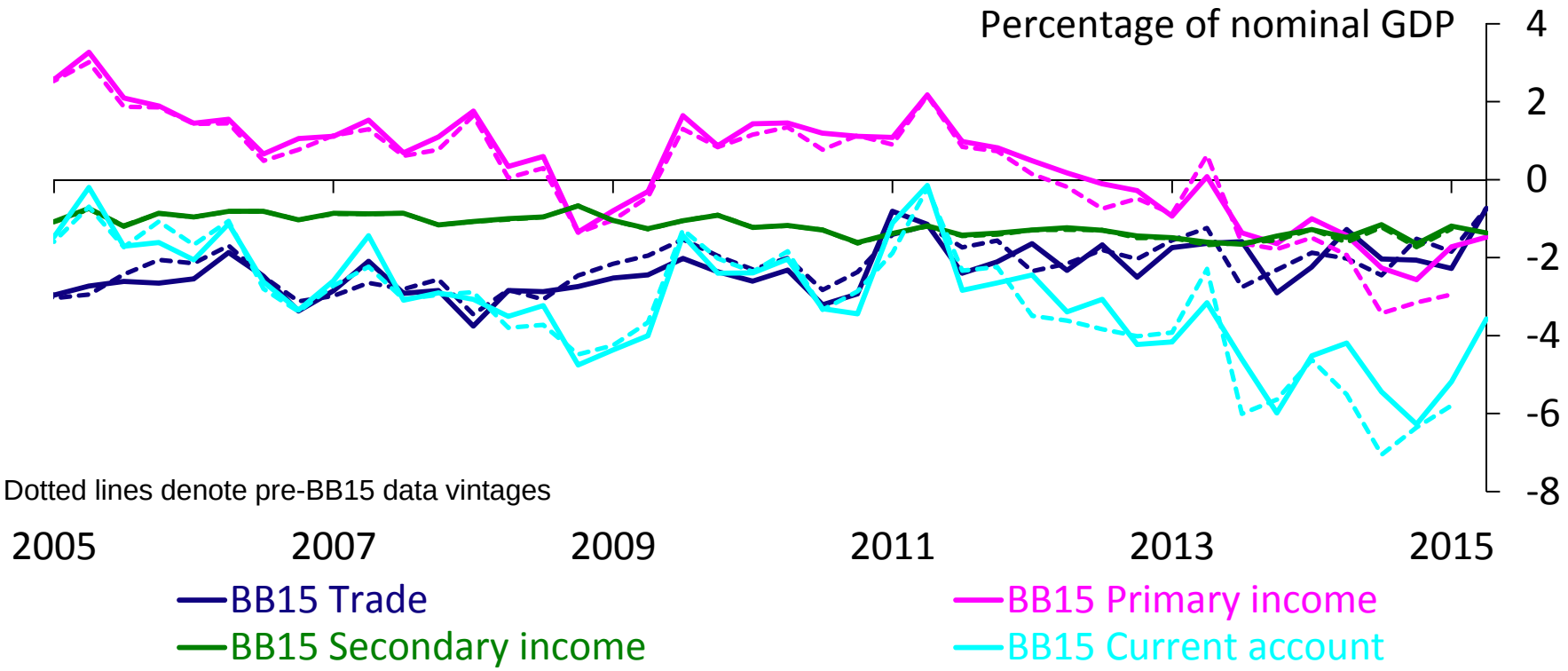
- The nominal trade deficit shrank in Q2 2015

Current account



- The upward revision to primary income largely reflects new FDI data

Current account



- The current account deficit is now 3.6% in Q2 2015

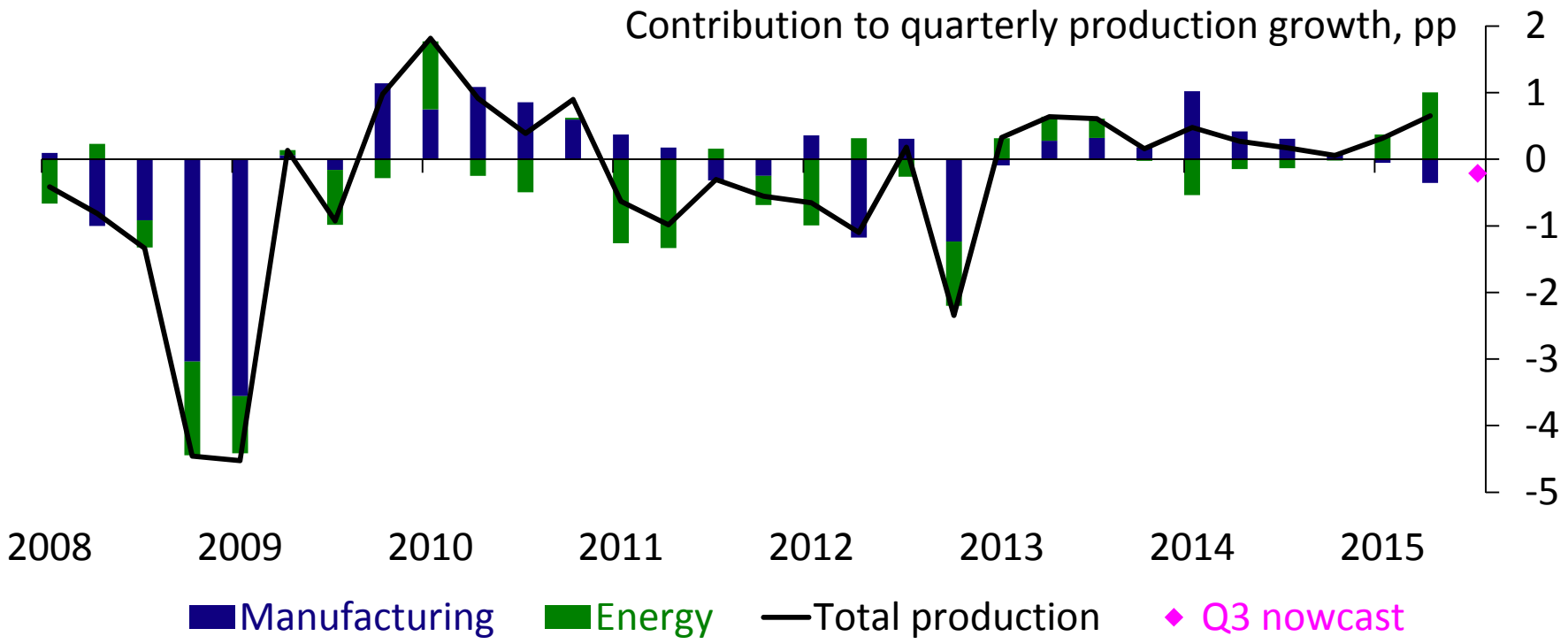
Outline

1) Headline news in the Blue Book: GDP, productivity, slack and inflationary pressure
2) How has the Blue Book affected the composition of growth?
   - Expansion still driven by private domestic demand
   - Firm consumption, lower saving ratio
   - Downward revisions to business investment

Outline

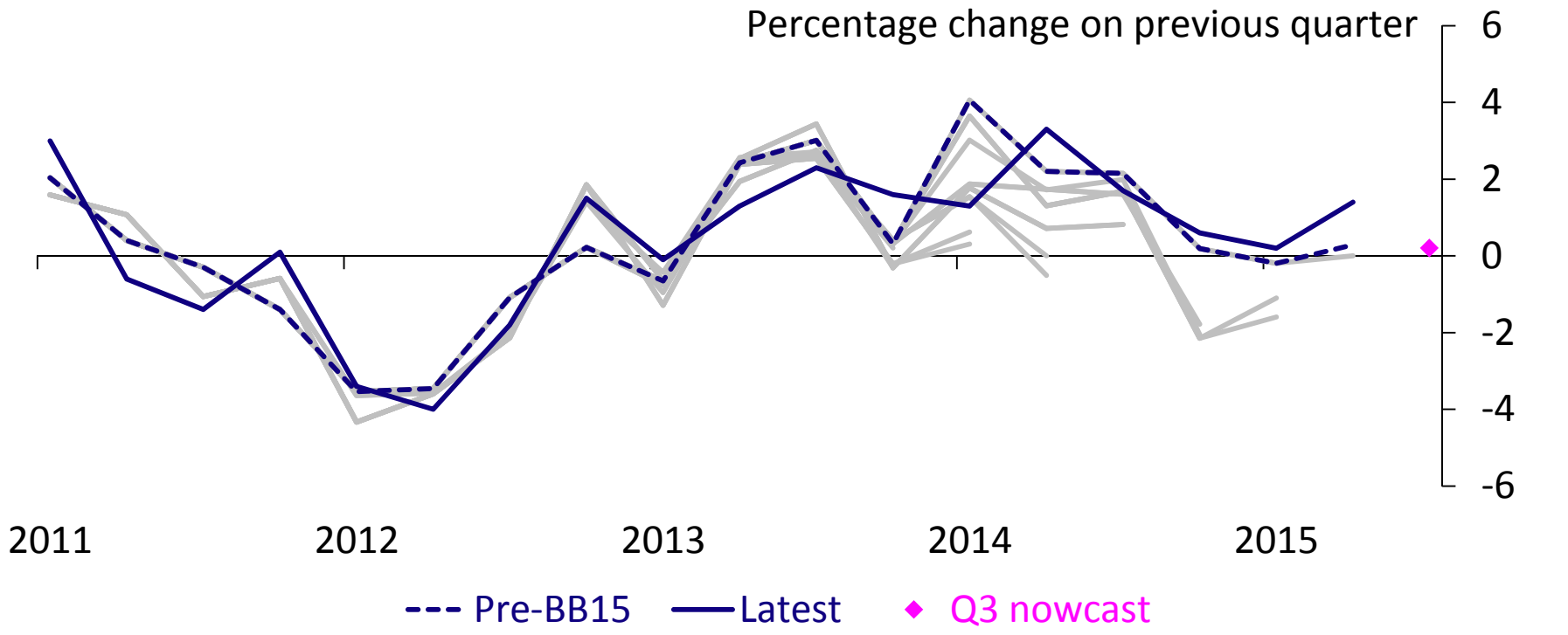
1) Headline news in the Blue Book: GDP, productivity, slack and inflationary pressure
2) How has the Blue Book affected the composition of growth?
3) Update on the short-term outlook
   - Mixed news on the month
   - Maintained Q3 nowcast at 0.6%, 0.1pp lower than Aug IR

Production



- Manufacturing has continued to drag on production activity

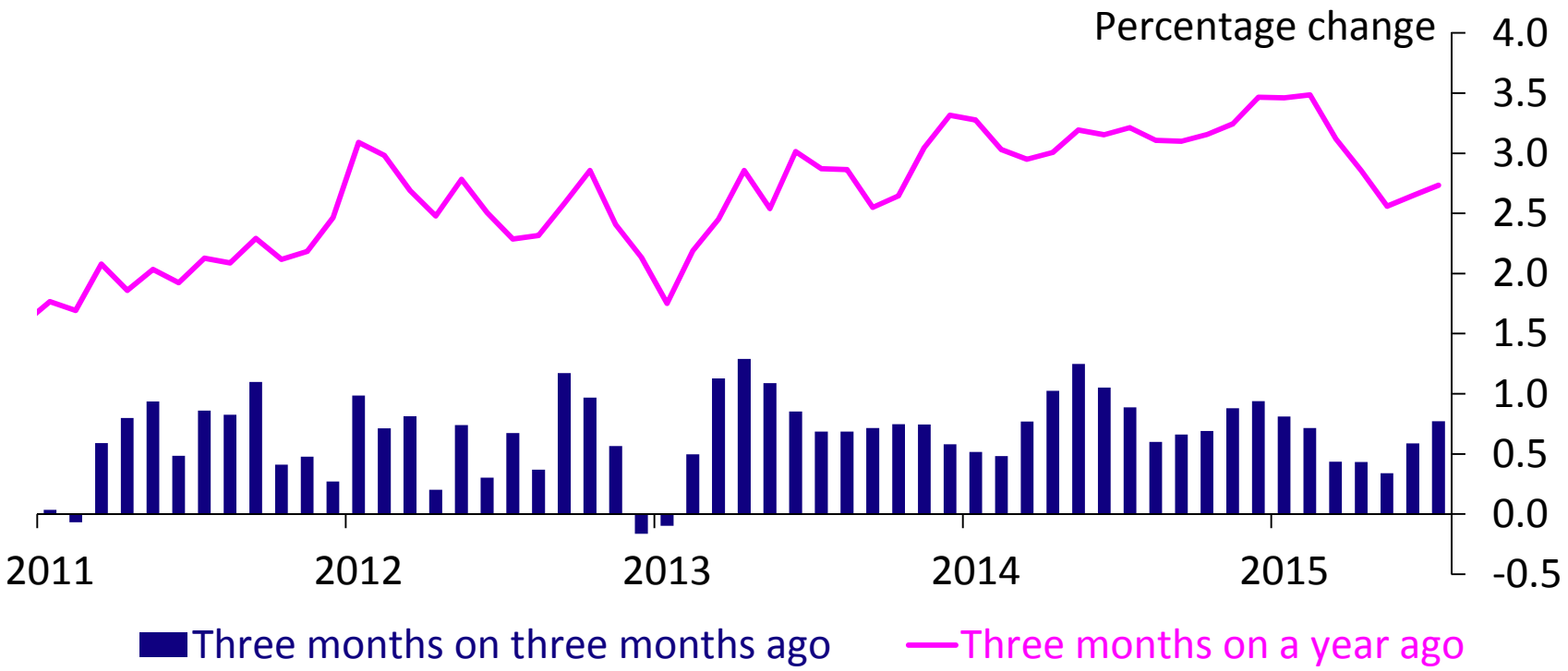
Construction



NB grey lines are real-time data vintages

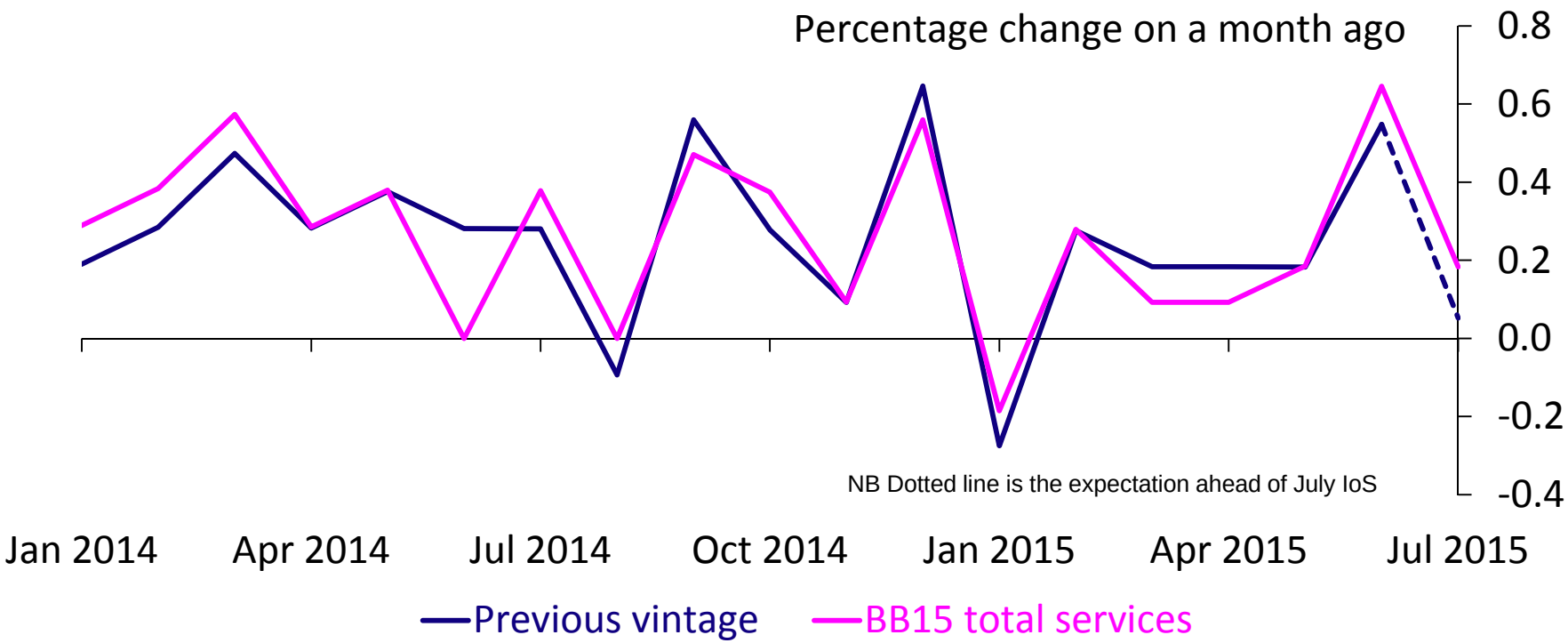
- Construction growth expected to be broadly flat in Q3

Total services



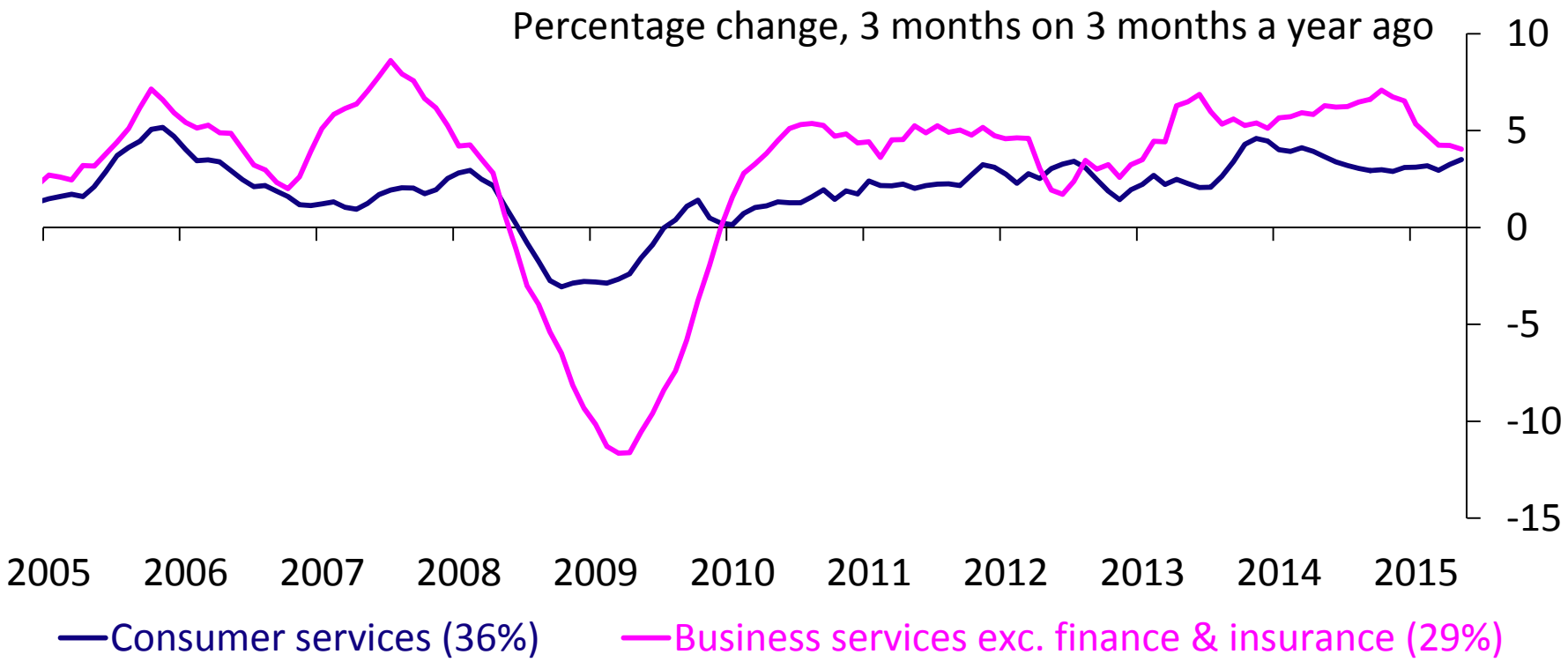
- Total services growth was stronger than expected in July

Total services monthly growth



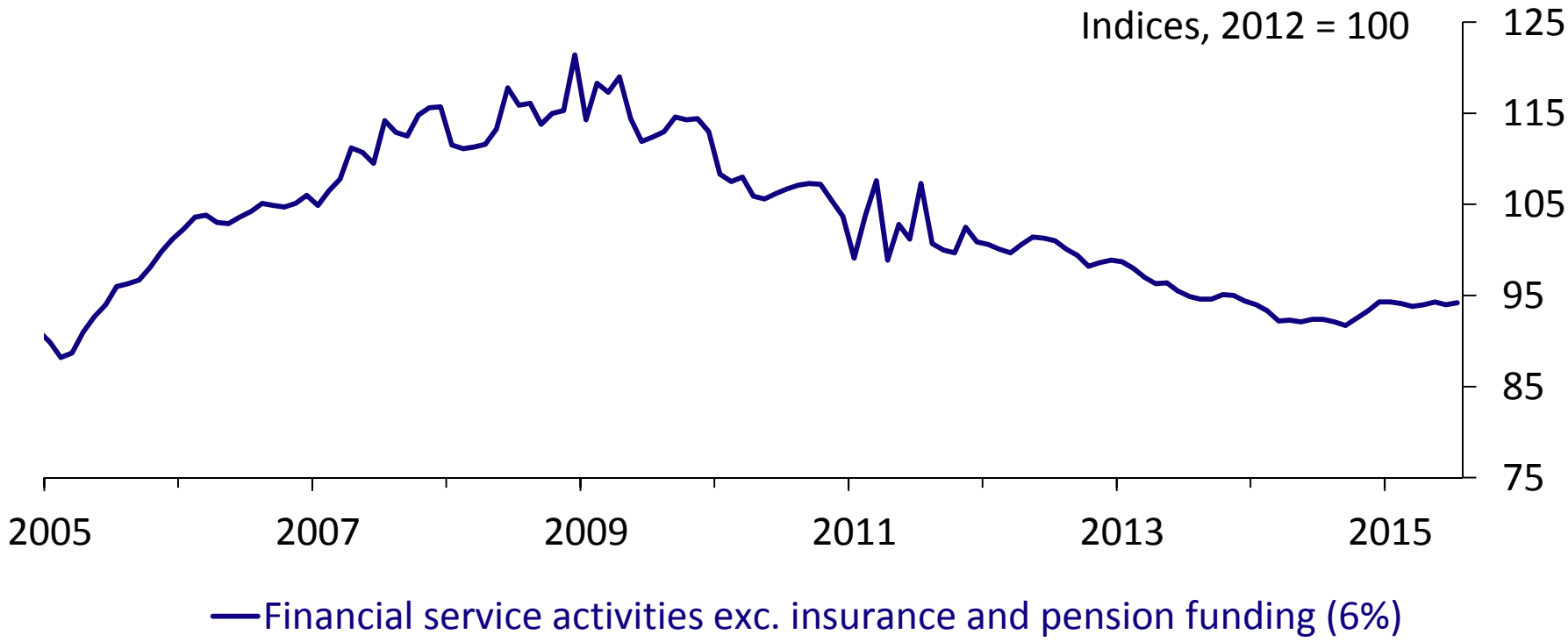
- July services output growth was slightly stronger than expected

Consumer and business services



Consumer services: motor & retail trades; air transport; accommodation and food; media; real estate; recreation; households as employers; other services.
Business services: wholesale trades; transport & warehousing; post; ICT; professional services; administrative activities
NB: Figures in parentheses show share of total services output

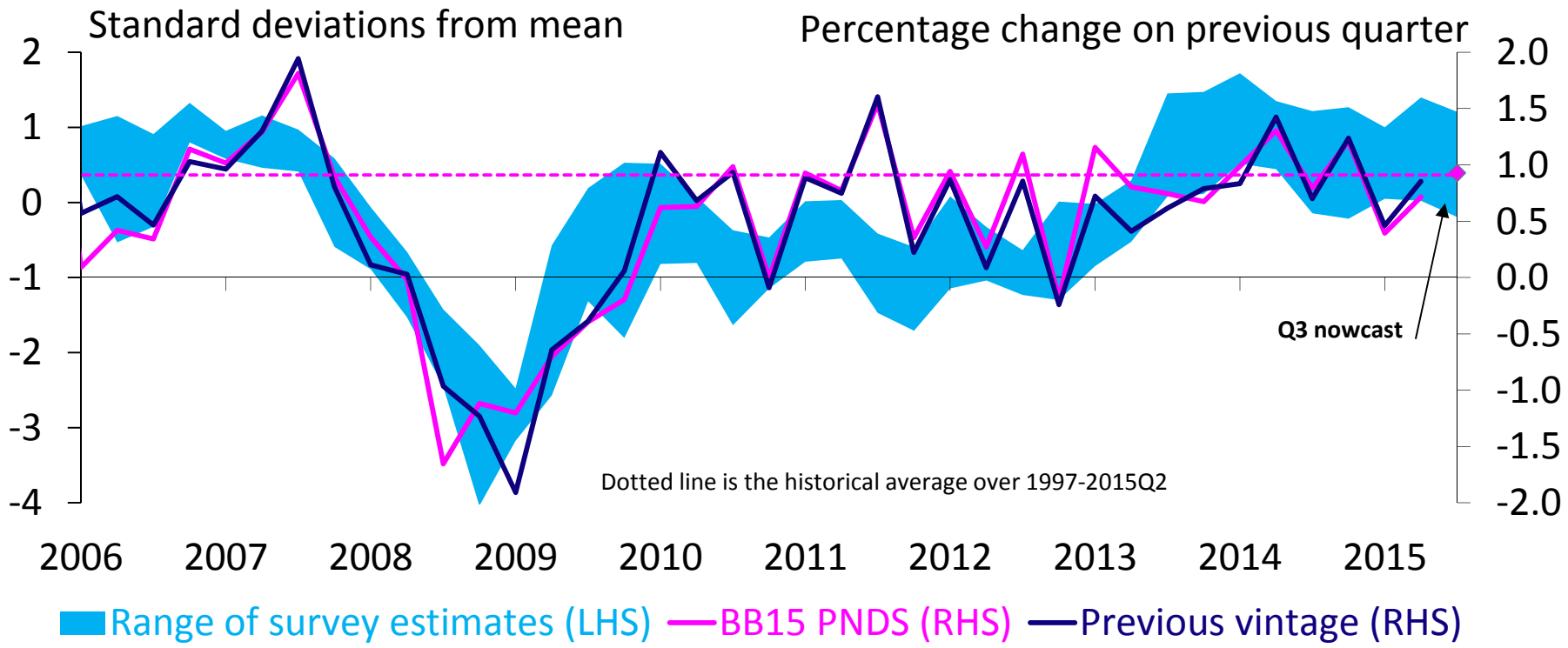
Financial services output



NB: Figures in parentheses show share of total services output

- Financial services output has stabilised

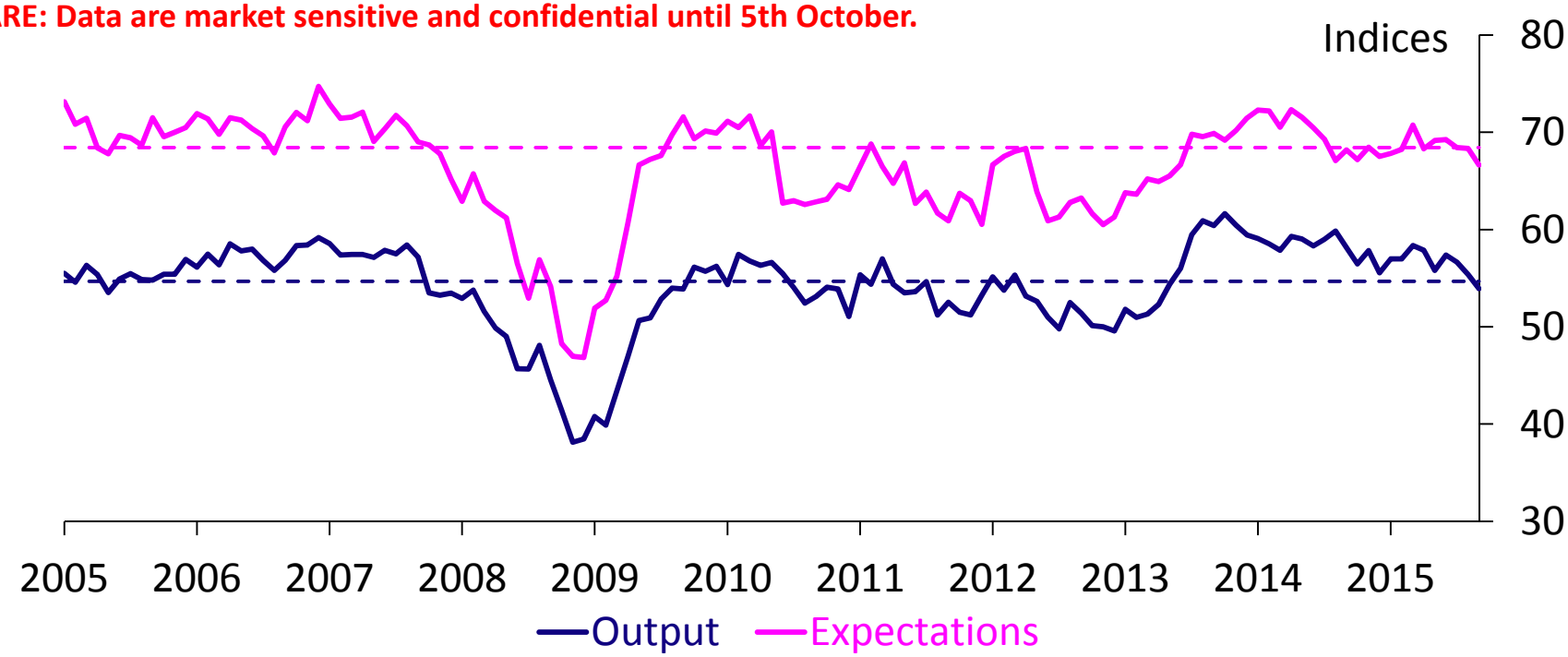
Quarterly PNDS growth vs surveys



- Our Q3 PNDS nowcast is near the middle of the survey swathe

Markit/CIPS output and expectations composite

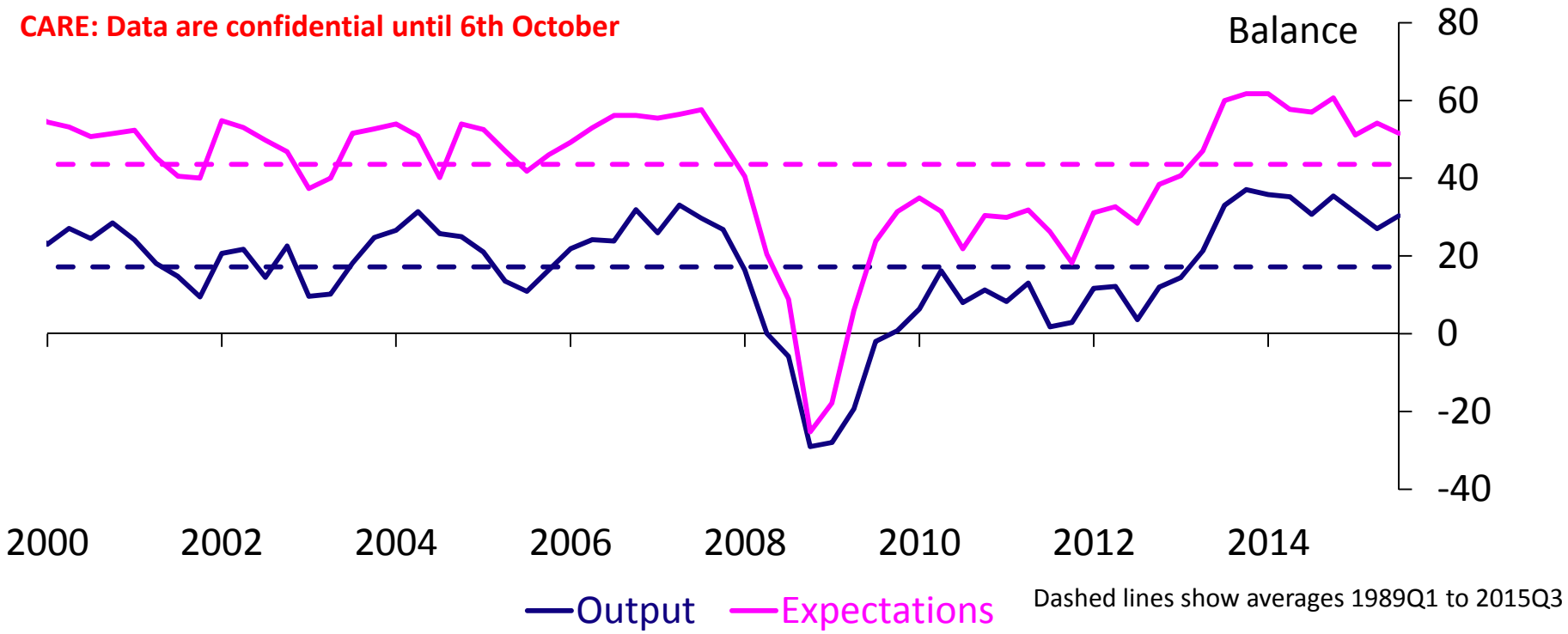
CARE: Data are market sensitive and confidential until 5th October.



Dashed lines show averages January 1997 to September 2015

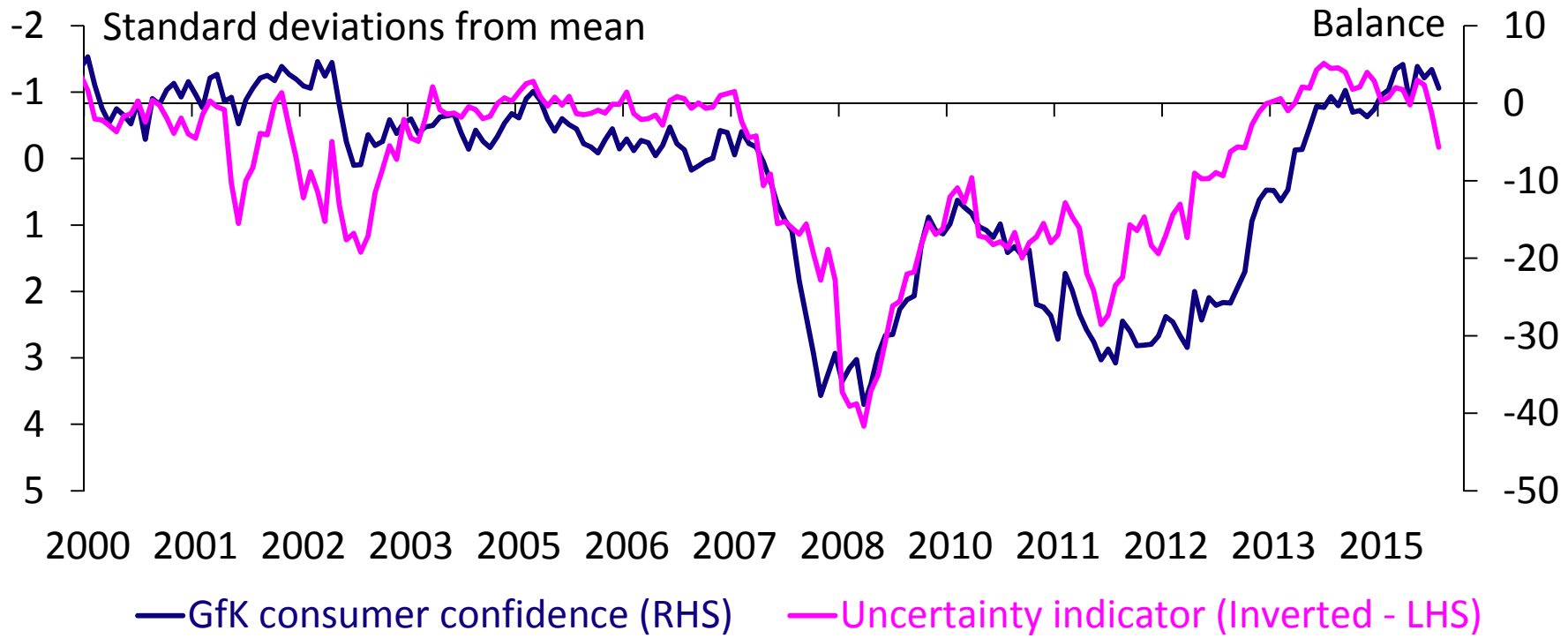
- Both the output and expectations composites fell in September

BCC composite survey



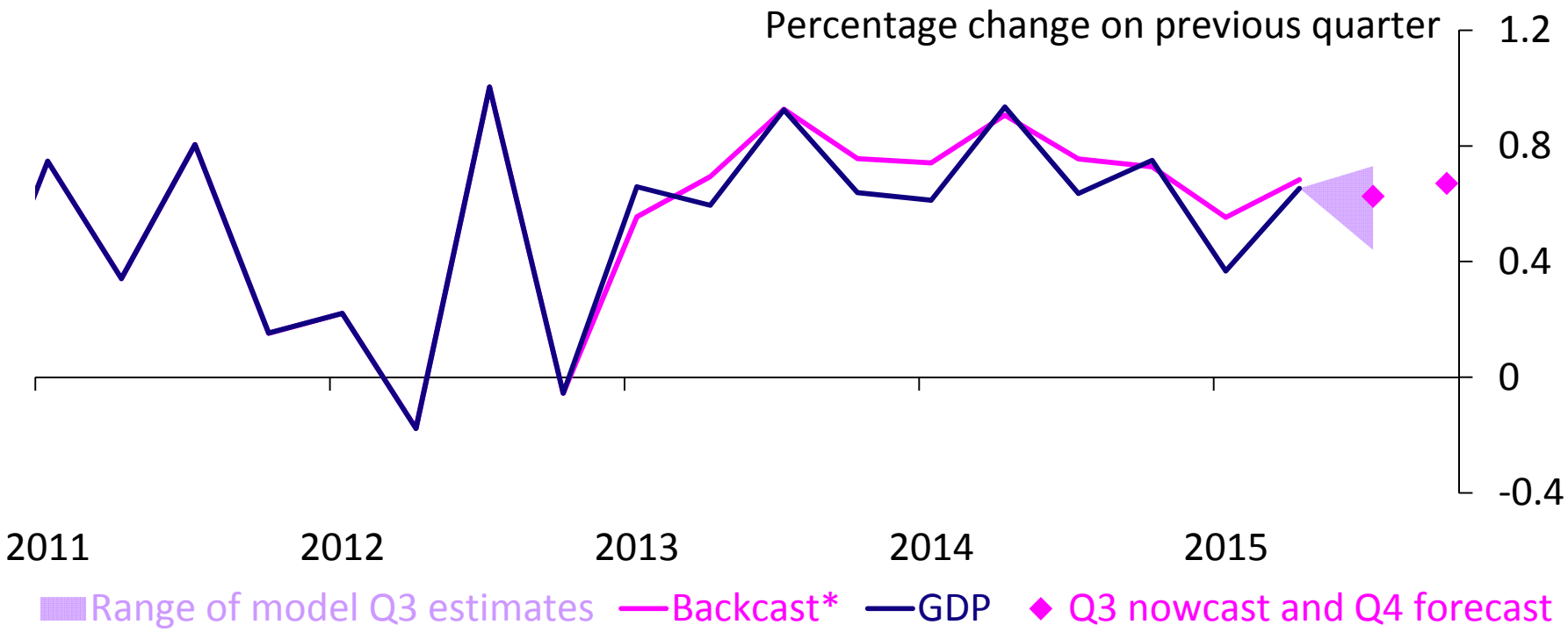
- The output composite ticked down, but expectations remain high

Uncertainty and confidence



- Consumer confidence remained high in September, although uncertainty increased according to our uncertainty principal component

Short-term outlook



*Provisional backcast

- Our Q3 nowcast remains unchanged at 0.6%

Outline

1) Headline news in the Blue Book: GDP, productivity, slack and inflationary pressure
2) How has the Blue Book affected the composition of growth?
3) Update on the short-term outlook
   - Mixed news on the month
   - Maintained Q3 nowcast at 0.6%, 0.1pp lower than Aug IR

Key messages

- Little headline news in the Blue Book
- Expansion remains driven by private domestic demand
- Maintained Q3 nowcast at 0.6%

END