INSTITUTE OF INTERNATIONAL MONETARY RESEARCH

Monetary Policy Committee meeting, Bank of England, 4th November 2021

Bank of England surprises markets by doing nothing.

On 17th October, Andrew Bailey, the Governor of the Bank of England, stated that in response to the recent surge in energy prices the bank "will have to act and must do so" because of the "risk, particularly to medium-term inflation and medium-term inflation expectations" These comments were widely interpreted as implying that monetary policy was to be tightened at the next meeting of the BoE's Monetary Policy Committee on 4th November. It therefore came as something of a surprise to many that neither a rise in base rates nor a termination of the asset programme were announced. The votes were not unanimous, with two of the nine members of the MPC voting for a rate rise and three members voted to curtail the asset purchases. Mr Bailey said that the decision had been a "close call", but the MPC felt the need to hold back to see how well the labour market responded to the end of furlough. The preference to carry on as before comes in spite of an acknowledgement in the minutes of the meeting that inflation is likely to rise further, breaching 4% in October and rising as high as 5% in April 2022 before subsiding. The minutes acknowledged that inflation expectations were "materially higher than expected in the August report." which makes the MPC's inaction all the more inexplicable.

In the latest Monetary Policy Report which was published the same day as the MPC met, the Bank repeated its well-established opinion that the spike in energy prices and the supply chain disruption would be temporary, but nonetheless stated that "We expect interest rates will need to rise modestly to return inflation to our 2% target", suggesting that rates will rise at some point during 2022. As usual, the Bank's analysis completely ignored any mention of money growth. UK broad money grew at an annualised rate of 5.5% in the three months to September, the second lowest reading since the start of the Coronavirus Pandemic in spring 2020, but still higher than the typical readings in the preceding years. We at the Institute of International Monetary Research very much side with the dissenting minorities in the two MPC votes. Given that the UK economy has now been free of most restrictions for the better part of four months and the Government appears very hesitant to re-impose them, the economy is able to stand on its own two feet without further stimulus. This is not the first time that a Monetary Policy Committee has admitted to being caught out by the scale and duration of above-target inflation. The Fed's FOMC made the same confession recently. The solution to keeping prices under control is simple – slow the growth of broad money. The Bank of England sadly missed out on its opportunity to do so at its meeting on 4th November. It is therefore likely to be caught out again by inflation persisting for longer that it expected.

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