MONETARY POLICY PRESS CONFERENCE

Thursday 8 May 2025

Opening remarks by Andrew Bailey, Governor

The disinflation process in the UK economy has continued. UK inflation was 2.6% in the latest data for March. That is above our 2% target. But it is a little lower than expected. With the progress we have made, we can take another step in making monetary policy less restrictive.

So today, we have we cut Bank Rate by 0.25 percentage points, to 4.25%.

As the past few weeks demonstrate, the global economic environment remains an uncertain one. Interest rates are not on autopilot. They cannot be. Instead, the MPC must continue to respond carefully to the evolving economic circumstances and the outlook for inflation in the UK. Whatever happens, the MPC will continue to set Bank Rate to ensure that inflation returns sustainably to the 2% target in the medium term.

I will return to the global economy shortly. But I will start with – and spend most of my time on – what is happening in the UK economy. That is ultimately what matters for UK inflation and monetary policy. I will have four key messages, reflecting our four key judgements on the outlook, before concluding with the uncertainties we face and the implications for monetary policy.

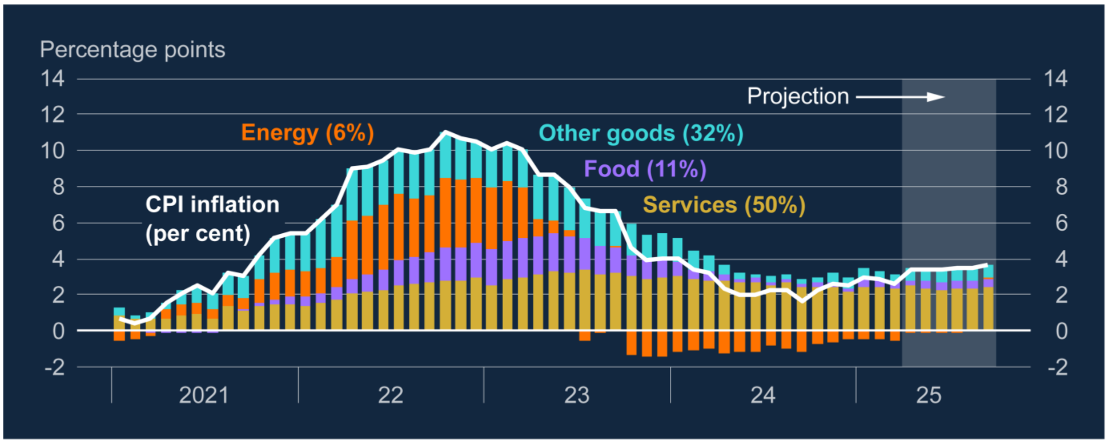
My first key message is that disinflation in domestic price and wage pressures is continuing. While headline inflation is expected to rise in the near term, we do not expect it to persist.

Chart 1 shows the development of twelve-month consumer price inflation since 2021 (white line) along with its components. As the Chart shows, headline inflation has been around the 2% target over the past year, albeit slightly above it on average. In the shaded area, the Chart shows how we expect headline inflation to rise to about 3½% in the coming months.

This is a little less than we projected in February. And we expect the increase to be temporary.

Chart 1: Inflation has been close to target but is expected to rise in April

Contributions to CPI inflation

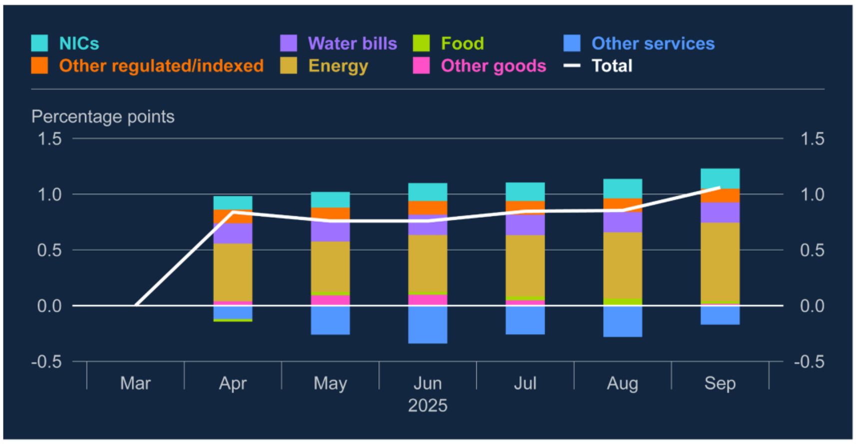


Sources: Bloomberg Finance L.P., Department for Energy Security and Net Zero, ONS and Bank calculations

Chart 2 illustrates why. It shows that the expected increase in inflation is driven mostly by energy prices (now in yellow), and besides that by increases in regulated water bills (purple bars), indexed bills for services such as broadband and mobile phones (orange bars) and higher national insurance contributions (in light blue). These price increases are not directly linked to the underlying cost pressures in the UK economy. We should not expect them to persist. Meanwhile, other services prices (darker blue bars) – those that are more closely linked to activity and cost pressures – are on course to pull down on inflation in the coming months.

Chart 2: Energy and regulated prices will drive up CPI inflation temporarily

Projected contributions to the change in CPI inflation from March 2025



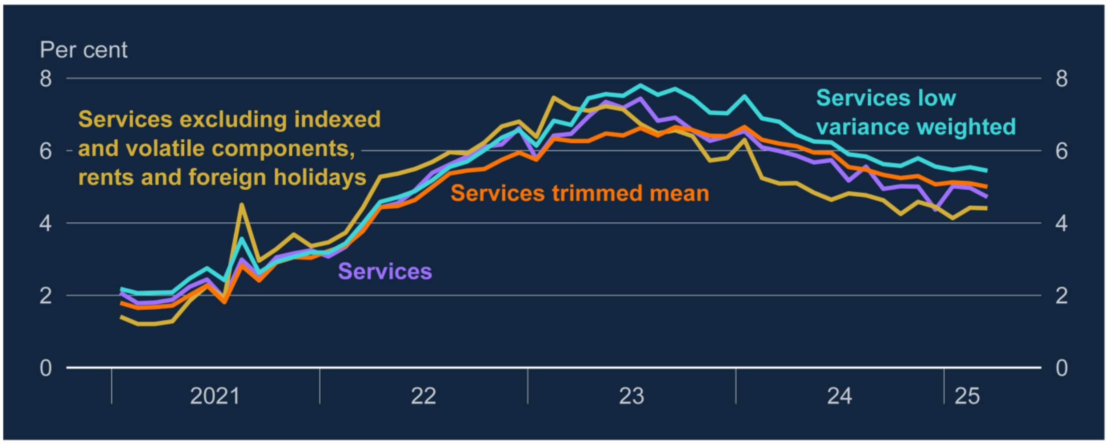
Sources: Bloomberg Finance L.P., Department for Energy Security and Net Zero, ONS and Bank calculations

As the effects of volatile energy prices and indexed and regulated price changes pass through, it is not least the path for these other services prices that will determine headline inflation. And the path for services inflation points to a continued gradual easing of inflationary pressure in the UK economy.

This is shown in **Chart 3**. While their levels remain elevated, measures of underlying services price inflation have continued to diminish. This has happened as pressures from non-labour input costs have faded. So persistence in wage growth is now the main driver of continued high levels of services price inflation.

Chart 3: Underlying services inflation measures have continued to moderate

Measures of annual underlying services price inflation



Sources: ONS and Bank calculations

My second key message is that a small margin of slack has opened up in the UK economy, and we expect it to widen over the next couple of years.

Heightened uncertainty, weak productivity growth and the continued restrictive stance of monetary policy have all been weighing on GDP growth recently. Businesses have been cautious about investing. And while real household incomes have risen quite strongly, consumption has not followed suit.

This weakness in demand has coincided with continued weakness in the potential supply capacity of the UK economy. Productivity growth has been weak. Nevertheless, labour market developments, survey indicators of capacity utilisation and statistical estimates all suggest that weaker demand has led to a small margin of economic slack opening up.

Looking through data volatility, we expect underlying GDP growth to remain subdued in the near term before economic activity starts to pick up later this year as household spending and business investment recover, supported by a downward path for interest rates. We expect housing investment to strengthen too.

Assuming potential productivity recovers some of its recent weakness, that pickup in GDP growth will still probably go hand in hand with a wider margin of slack.

This takes me to my third key message. An emerging margin of slack in the UK economy should act against any remaining persistence in domestic wage and price setting to return inflation to the 2% target sustainably.

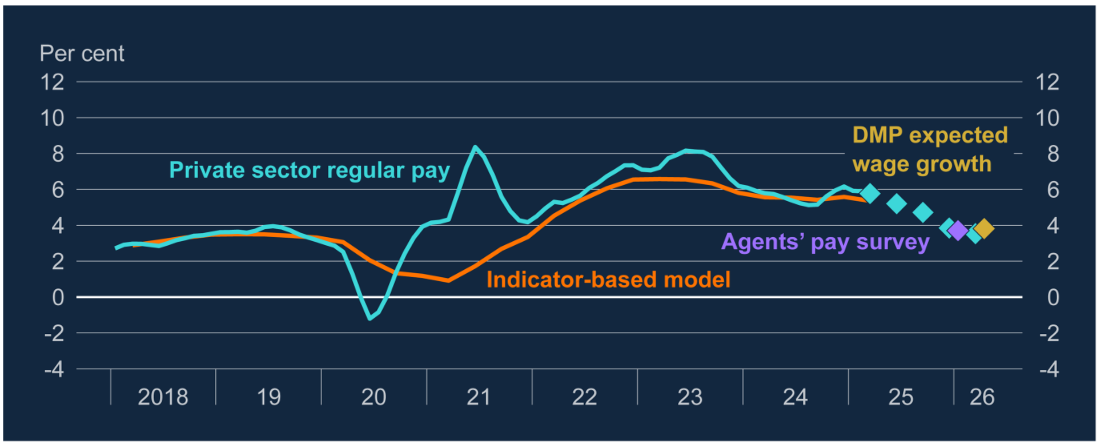
A normalisation in wage growth is particularly important to ensure that services price inflation continues to fall back to levels consistent with the 2% target for headline consumer price inflation.

This process still has some way to go. Annual private sector regular average weekly earnings growth was 5.9% in the three months to February, having risen in the second half of last year.

This was slightly lower than we expected in the February Report, however. As **Chart 4** shows, underlying measures – estimated by Bank staff – have been more stable and point to a slightly lower rate of wage growth. And as we look ahead over the course of this year, we expect wage growth to moderate with a loosening in labour market conditions. This is supported by forward-looking indicators. The Bank's latest Decision Maker Panel survey suggests that wage growth will be about 4% for the year ahead (yellow diamond), and the Bank's Agents point to average pay rises for 2025 between 3½% and 4% (purple diamond).

Chart 4: AWE growth has picked up but is expected to moderate

Measures of annual private sector wage growth



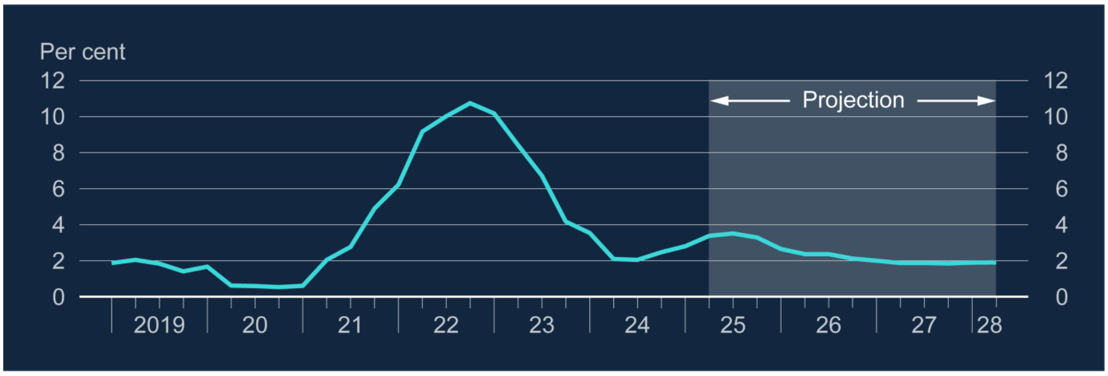
Sources: Agents, DMP Survey, ONS and Bank calculations

With a continued easing in labour as well as non-labour costs, further declines in services price inflation will support a gradual return of headline inflation to the target as we look beyond the near-term increase.

As shown in **Chart 5**, in our baseline projection conditional on the market-implied path for Bank Rate, inflation gradually falls from later this year to reach around the 2% target within two years' time.

Chart 5: CPI inflation is projected to return to target over the medium term

UK CPI inflation and projection



Sources: ONS, Bank calculations

My fourth key message is about the global economy. New tariffs and elevated trade policy uncertainty weigh on global activity. We expect global trade prices to be materially weaker, particularly in China.

The US administration has made a series of announcements with significant changes to tariff polices. Some of its trade partners have responded. Volatility in financial markets has accompanied these announcements.

Slower growth in the global economy is likely to reduce the demand for our exports and impact economic activity here in the UK. That reduction in external demand will also work to reduce inflationary pressures in the economy.

But while the impact of what we have seen so far is likely to push inflation down somewhat, the overall impact on inflation remains uncertain. On the one hand, lower US demand for global exports, particularly from China, could lead to lower global export prices and hence lower prices for the UK, reducing inflationary pressures further. On the other hand, higher costs in the global supply chain – as intermediate inputs are subjected to tariffs or because of disruptions – could push up on prices. While sterling has appreciated in recent weeks, easing inflationary pressures, global exchange rates can shift in response to trade policy news and the evolution of global risk sentiment.

Although they understandably dominate the headlines, it is important to remember that global trade policies, and how they affect the UK economy, is only one source of risk to the outlook for inflation in the UK.

The MPC is alert to a range of risks in both directions. Domestic inflationary pressures could persist for longer than we expect, despite the progress we have made, or they could ease more quickly as the margin of slack widens. The balance between supply and demand in the UK economy, and how it will develop over the forecast horizon, also remains highly uncertain. We need to watch very carefully for any signs that the near-term increase in inflation could lead to additional second-round effects on wage and price-setting, even if that is not our central assumption, but also for any further weakening in demand which would reduce inflationary pressure.

In the Monetary Policy Report, we present two scenarios in addition to a baseline projection for activity and inflation to illustrate some of these risks. In one scenario, there could be weaker supply and more persistence in domestic wages and prices, including from second-round effects related to the near-term increase in headline inflation. In the other scenario, inflationary pressures could ease more quickly owing to greater or longer-lasting weakness in demand relative to supply, in part reflecting uncertainties globally and domestically.

Considering all the risks, we will continue to monitor closely the accumulation of evidence on the outlook for inflation over the medium term and set Bank Rate accordingly to meet the 2% target.

To conclude, our restrictive stance of monetary policy has reduced inflationary pressures in the UK economy. With the progress we have made, we have been able to take another step in making monetary policy a little less restrictive today. A gradual and careful approach to the further withdrawal of monetary policy restraint remains appropriate.

And with that, Clare, Dave and I will be happy to take your questions.