MPC MEMBERS

COPIES OF THE NOVEMBER 2015 PRE-MPC MEETING PRESENTATIONS

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

Monetary Policy COO Division (TS-B)
28th October 2015

1: Financial Markets

Financial Markets

November 2015 Pre-MPC Markets & MFAD

Plan

- International monetary policy developments
- Short-term interest rates
- Long rates and inflation expectations
- Exchange rates and risky assets

Summary table of moves since August IR and October MPC

	Meeting-to-meeting		
	October MPC (5 October)	Latest (26 October)	**Change**
UK 1-year instantaneous OIS rate	0.60	0.61	**1 bps**
UK 3-year instantaneous OIS rate	1.26	1.26	**0 bps**
UK 10-year gilt yield	1.81	1.85	**4 bps**
£ ERI	90.9	92.6	**1.9%**
FTSE All Share	3457	3512	**1.6%**

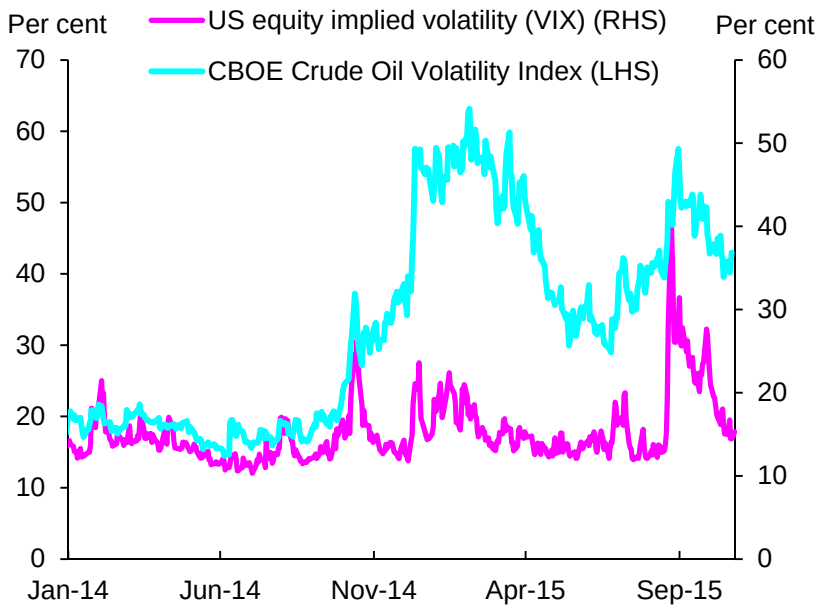
- Risky-asset prices have risen on the month, along with sterling
- Short rates remain materially lower than at the time of the August IR

Summary table of moves since August IR and October MPC

	Meeting-to-meeting			*Inflation Report* 15-day averages		
	October MPC (5 October)	Latest (26 October)	**Change**	August	November (13-day average)	**Change**
UK 1-year instantaneous OIS rate	0.60	0.61	**1 bps**	0.84	0.62	**-22 bps**
UK 3-year instantaneous OIS rate	1.26	1.26	**0 bps**	1.73	1.27	**-46 bps**
UK 10-year gilt yield	1.81	1.85	**4 bps**	2.17	1.84	**-33 bps**
£ ERI	90.9	92.6	**1.9%**	93.5	91.6	**-2.0%**
FTSE All Share	3457	3512	**1.6%**	3643	3484	**-4.4%**

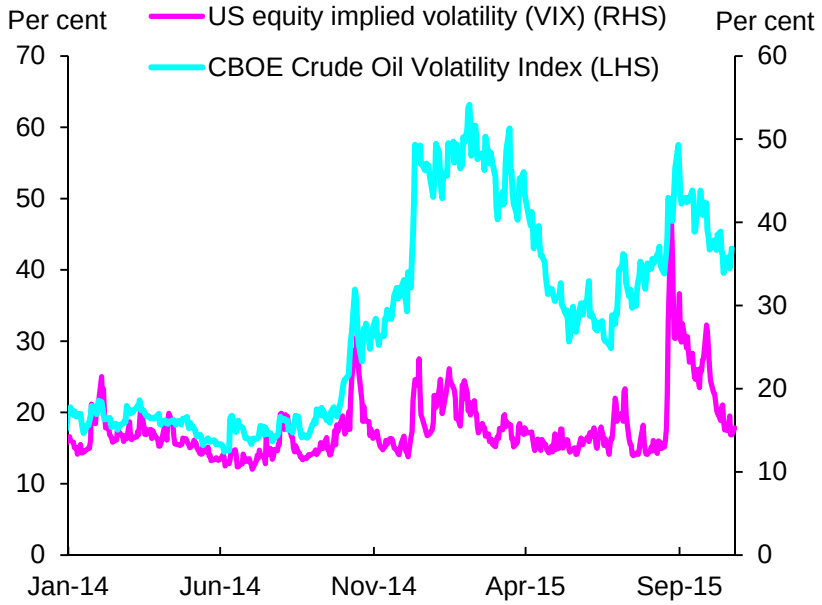
- Risky-asset prices have risen on the month, along with sterling
- Short rates remain materially lower than at the time of the August IR

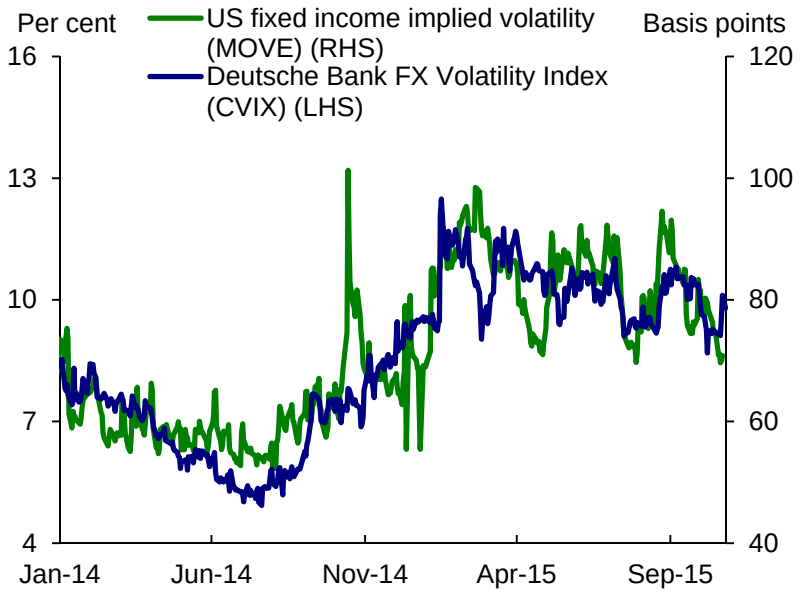
Implied volatilities



- Equity implied vol back to around its recent lows, and commodity vol has declined a little too

Implied volatilities

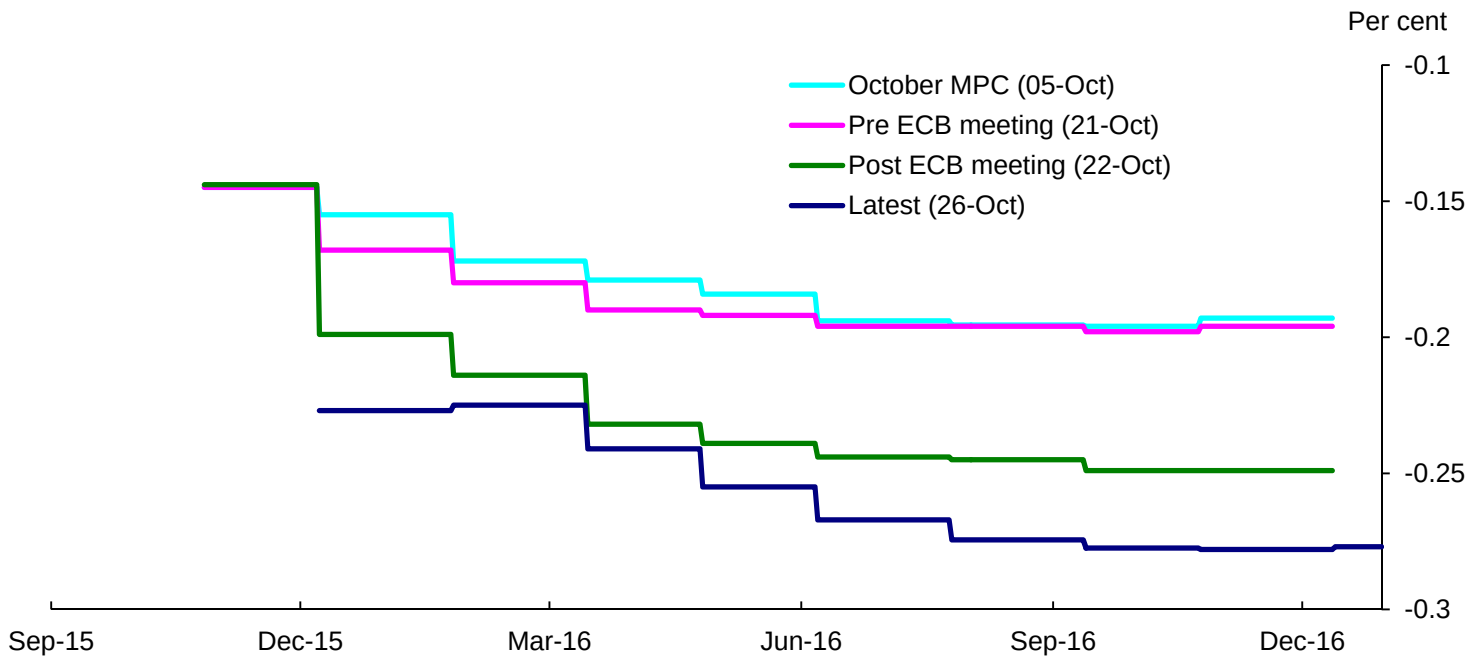




- Equity implied vol back to around its recent lows, and commodity vol has declined a little too
- Volatility in G10 FX and fixed income markets has fallen, but remains rather higher than last year

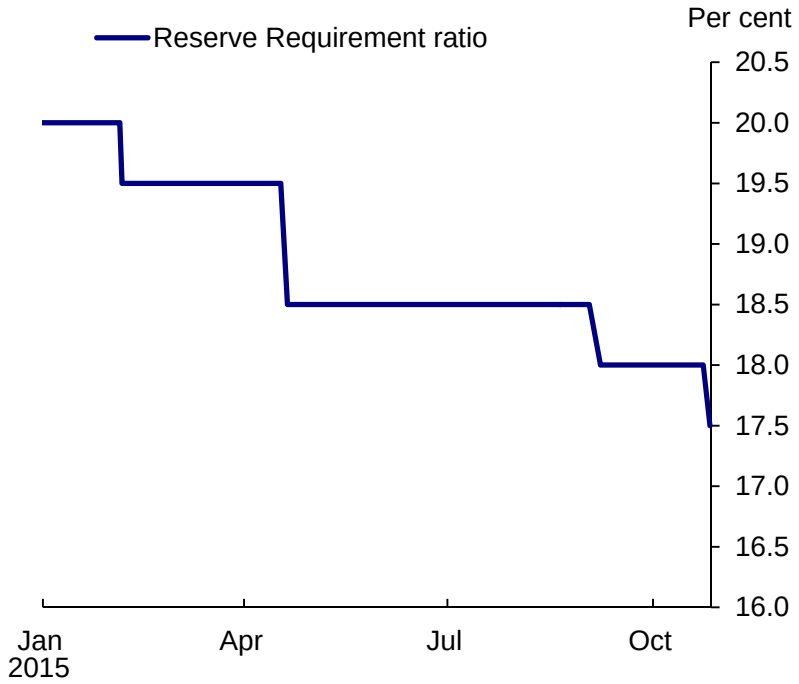
International monetary policy developments

EONIA meeting-to-meeting swaps



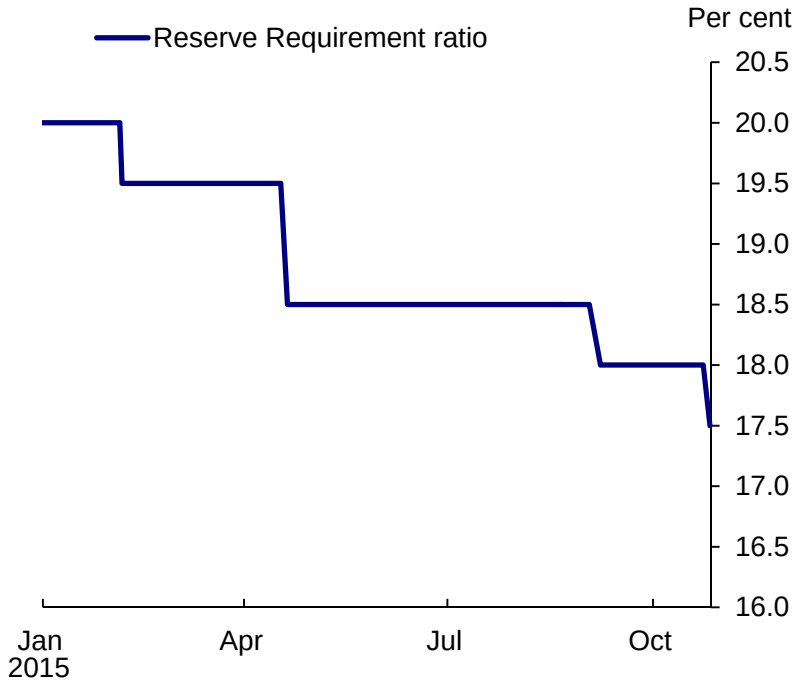
- EONIA meeting-to-meeting swaps curve has fallen materially over the course of the month, in anticipation of a shift towards further policy loosening

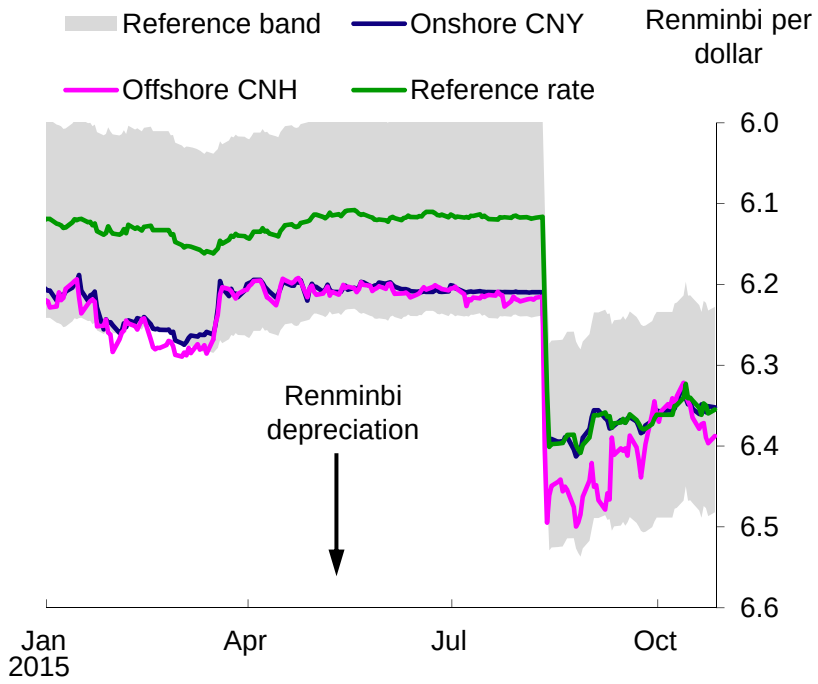
PBoC reserve requirement ratio and Renminbi versus the dollar



- PBoC cut the reserve requirement ratio again
- MI suggests that intervention in the exchange rate has abated in recent weeks

PBoC reserve requirement ratio and Renminbi versus the dollar





- PBoC cut the reserve requirement ratio again
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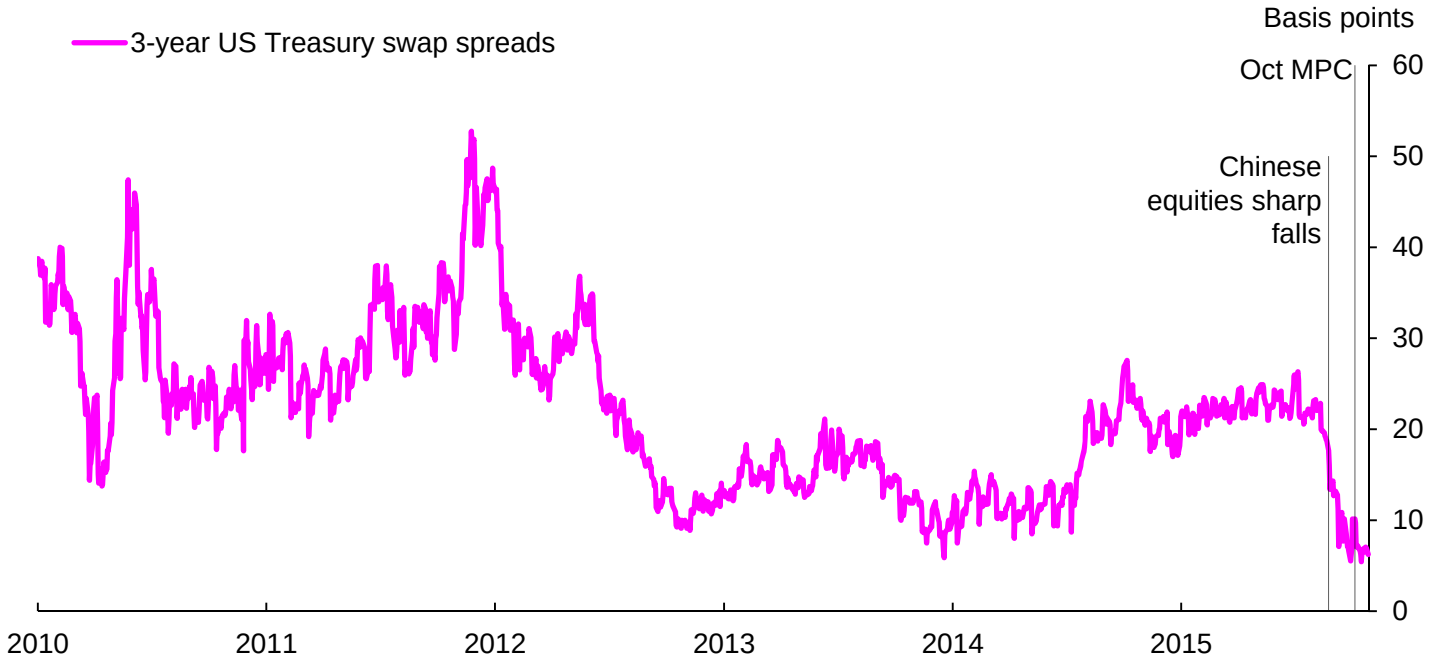
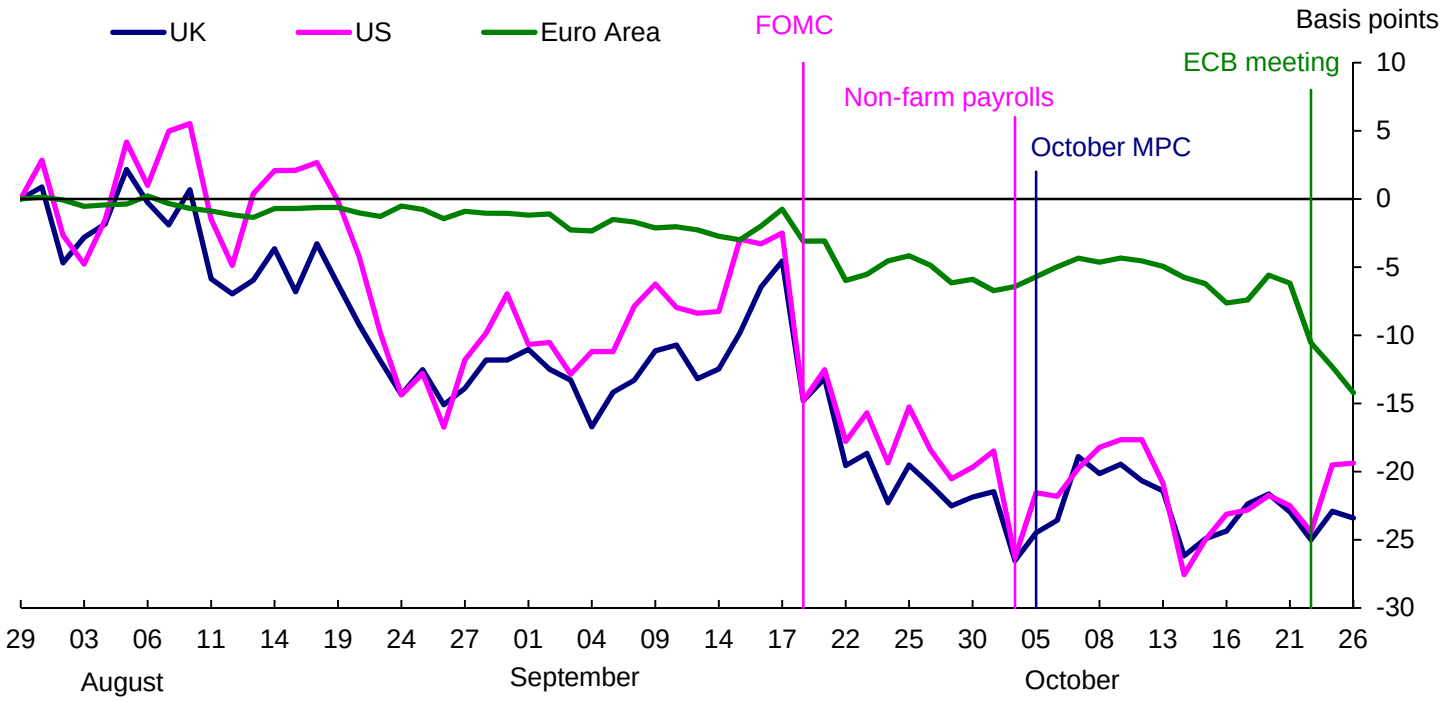
Spreads of US interest rate swaps over Treasury yields



- US Treasury yields have risen relative to comparable maturity interest rate swaps
- Perhaps indicative of EM central bank selling of US Treasuries

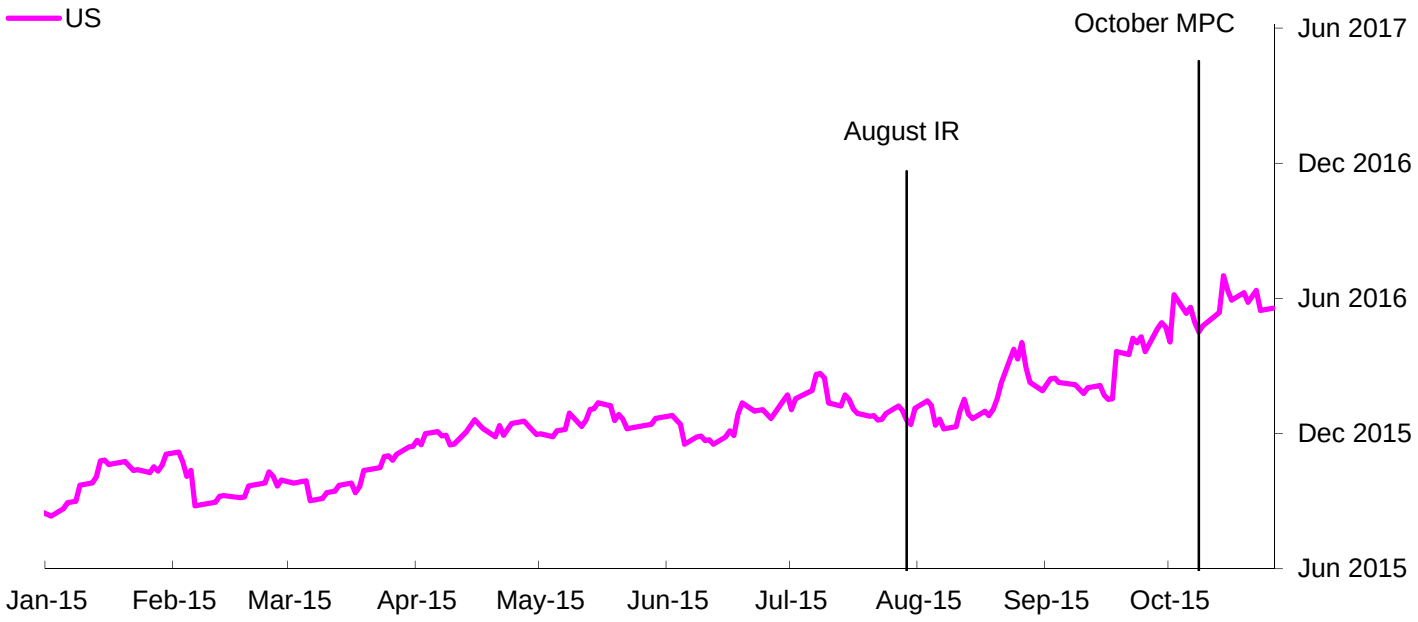
Short-term interest rates

Cumulative change in 1-year instantaneous forward OIS rates



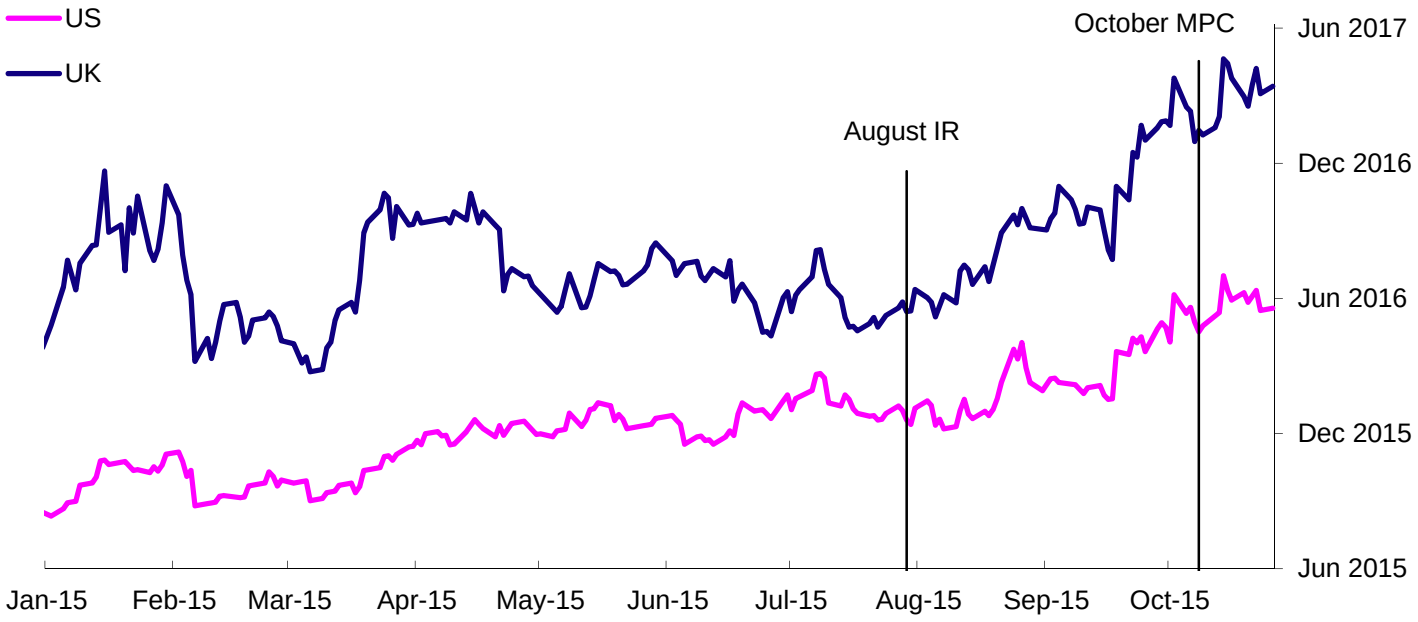
- Not much change on the month in US and UK
- Material fall in short rates since the August IR

Expected timing of first rate rise in US and UK



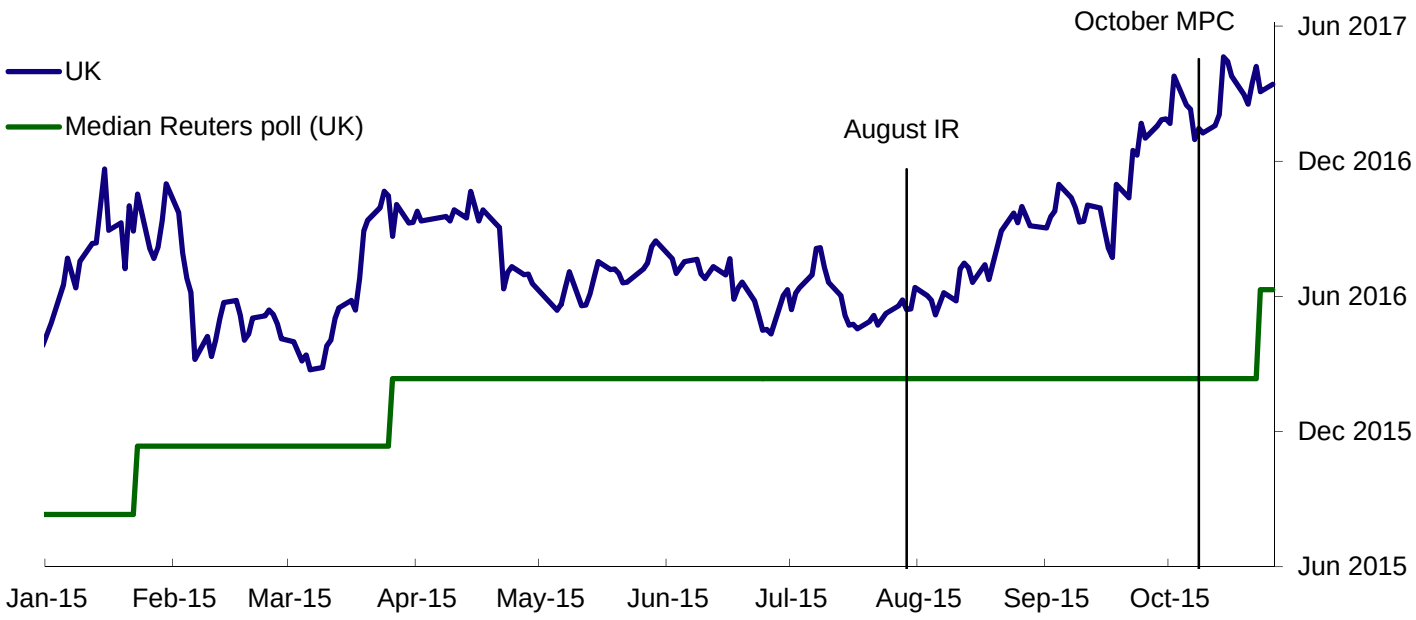
- Timing of lift-off in the US has been pushed out to around May of next year

Expected timing of first rate rise in US and UK



- Market-implied timing of lift-off in the US has been pushed out to around May of next year
- Market curve points to March 2017 in the UK

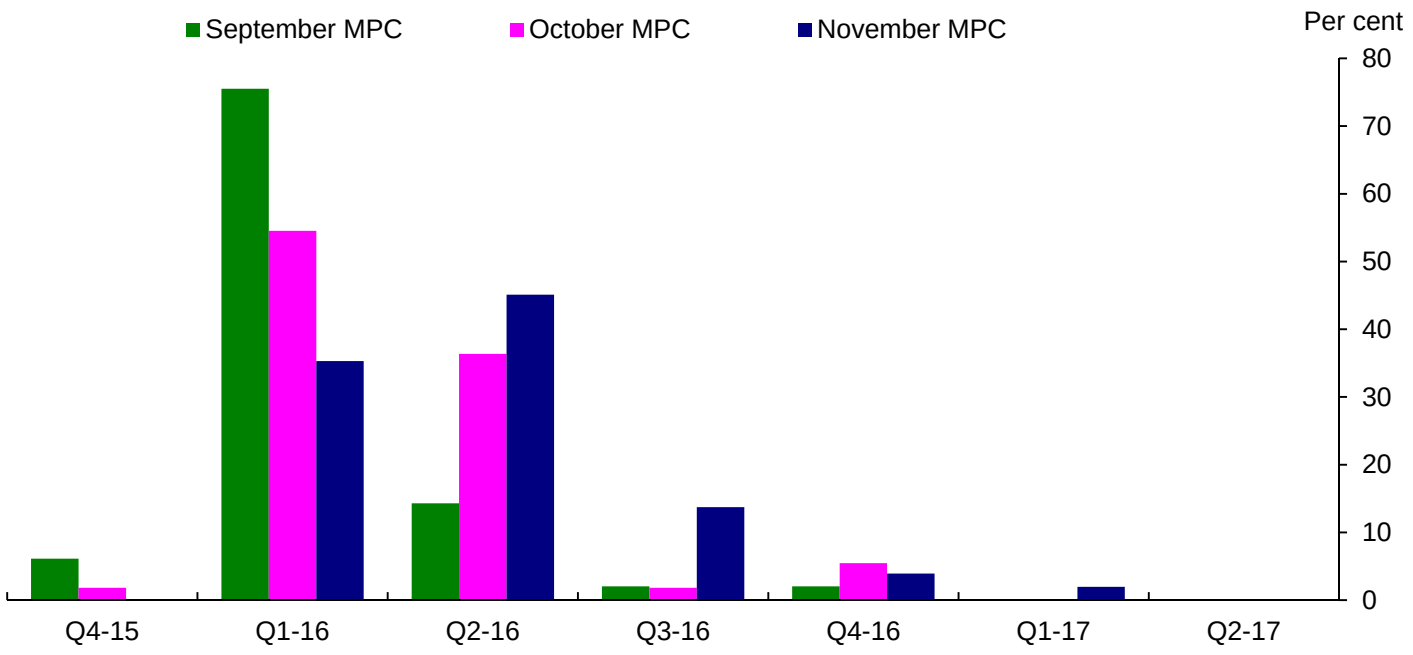
Expected timing of first rate rise in US and UK



	Latest	Last MPC
UK	Mar 2017	Jan 2017
Median Reuters poll (UK)	Q2 2016	Q1 2016

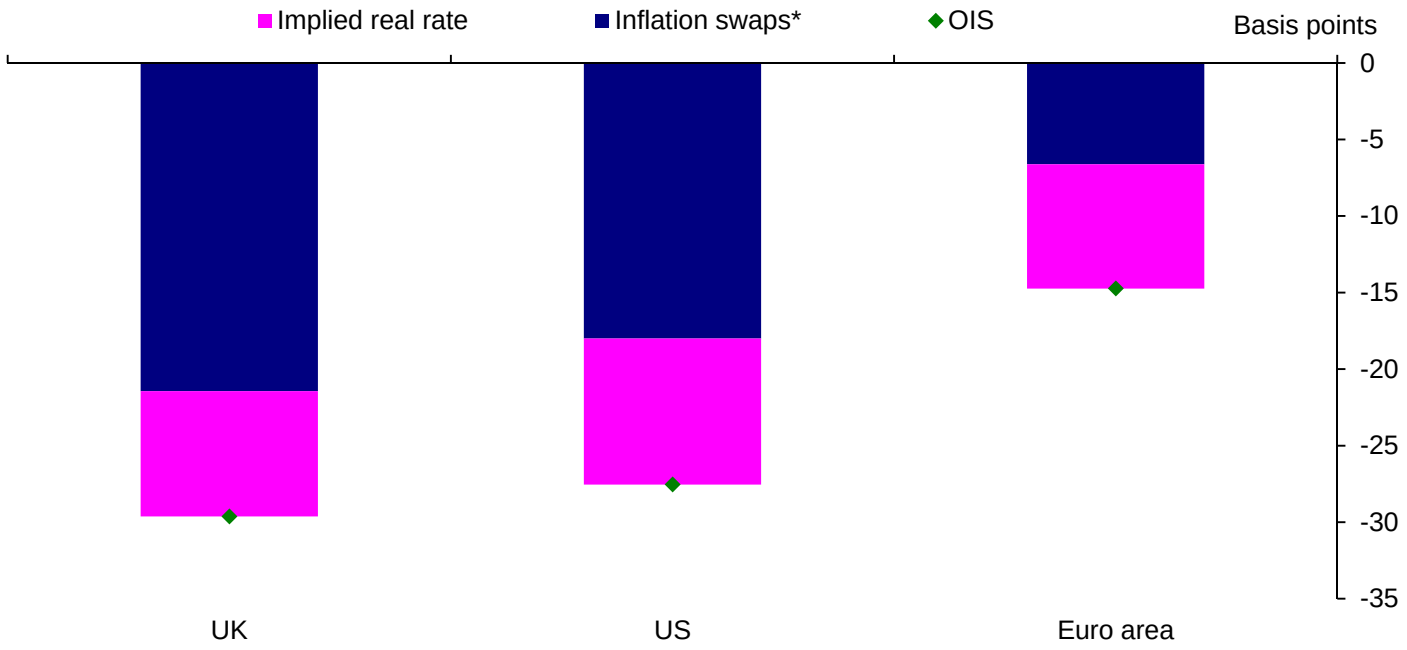
- Market-implied timing of lift-off in the US has been pushed out to around May of next year
- Market curve points to March 2017 in the UK
- Reuters poll has moved out to 2016 Q2

Reuters poll: timing of the first rise in Bank Rate



- Fairly wide distribution of expectations among economists surveyed by Reuters

Decomposition of fall in 3-year spot OIS rate since August IR



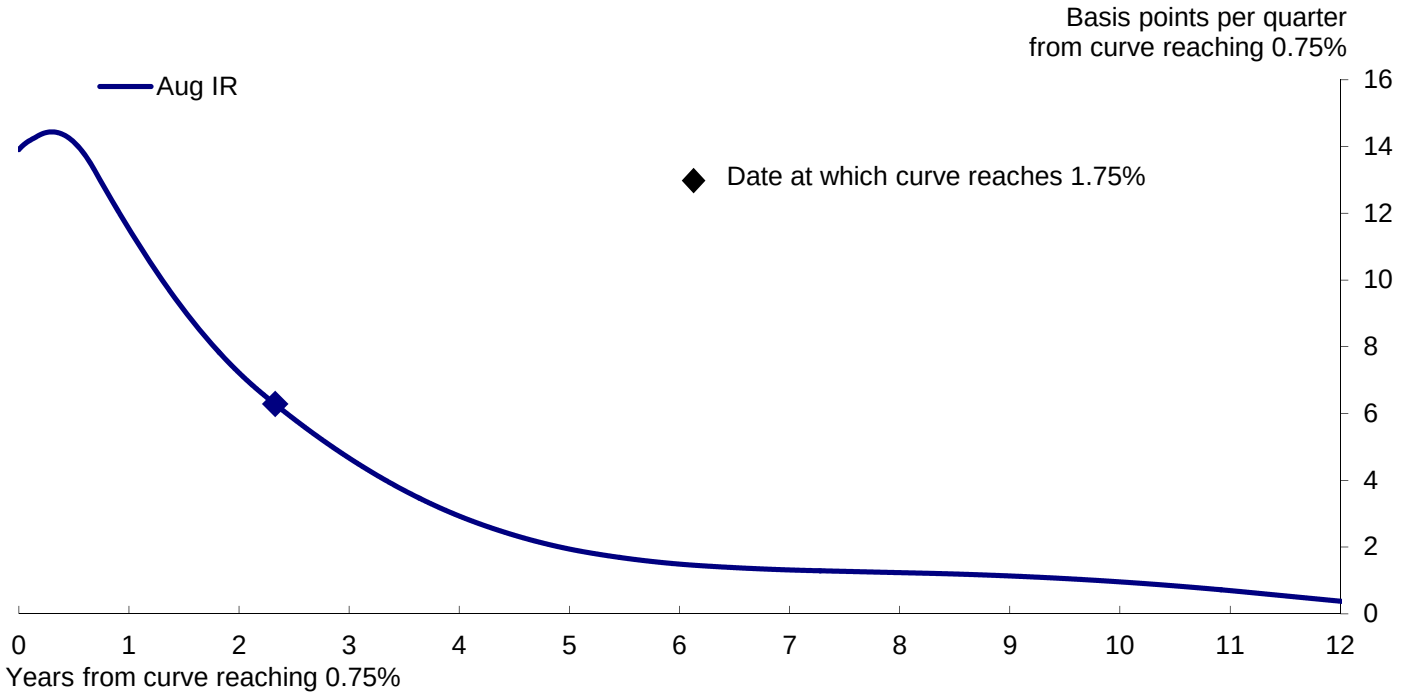
*UK (RPI inflation), US (CPI inflation), EA (HICP inflation)

- Fall in UK and US short-term interest rates driven by international factors and largely reflects lower inflation compensation
- Lower short rates may reflect both a fall in future policy rate expectations and lower term premia

MI on drivers of decline in short-term interest rates

- Change in market expectations for UK policy rates, in particular following the spike in volatility in August and the September FOMC
- Contacts also emphasised that domestic data had become less strong than earlier in the year, including wage growth
- Markets focused on dovish MPC communications
- Positioning in sterling markets is light, with some evidence of trades that would benefit from a rate cut

UK pace of tightening



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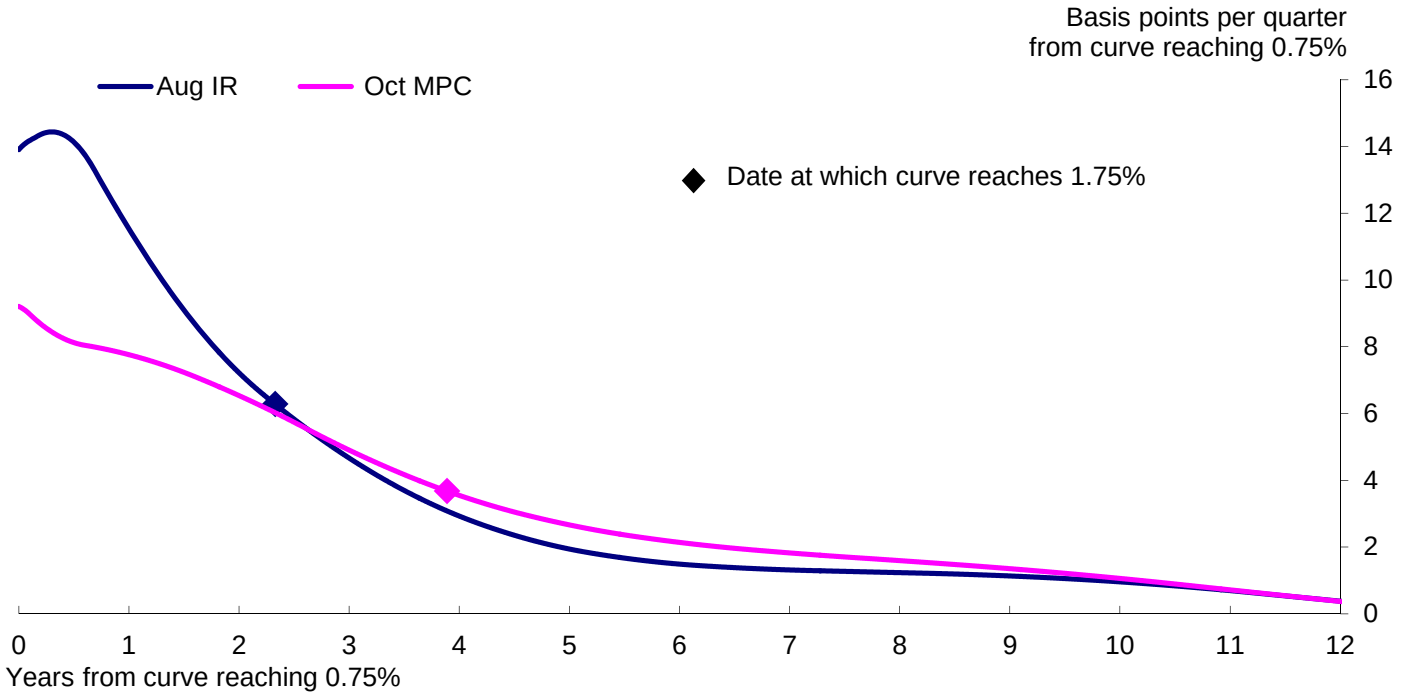
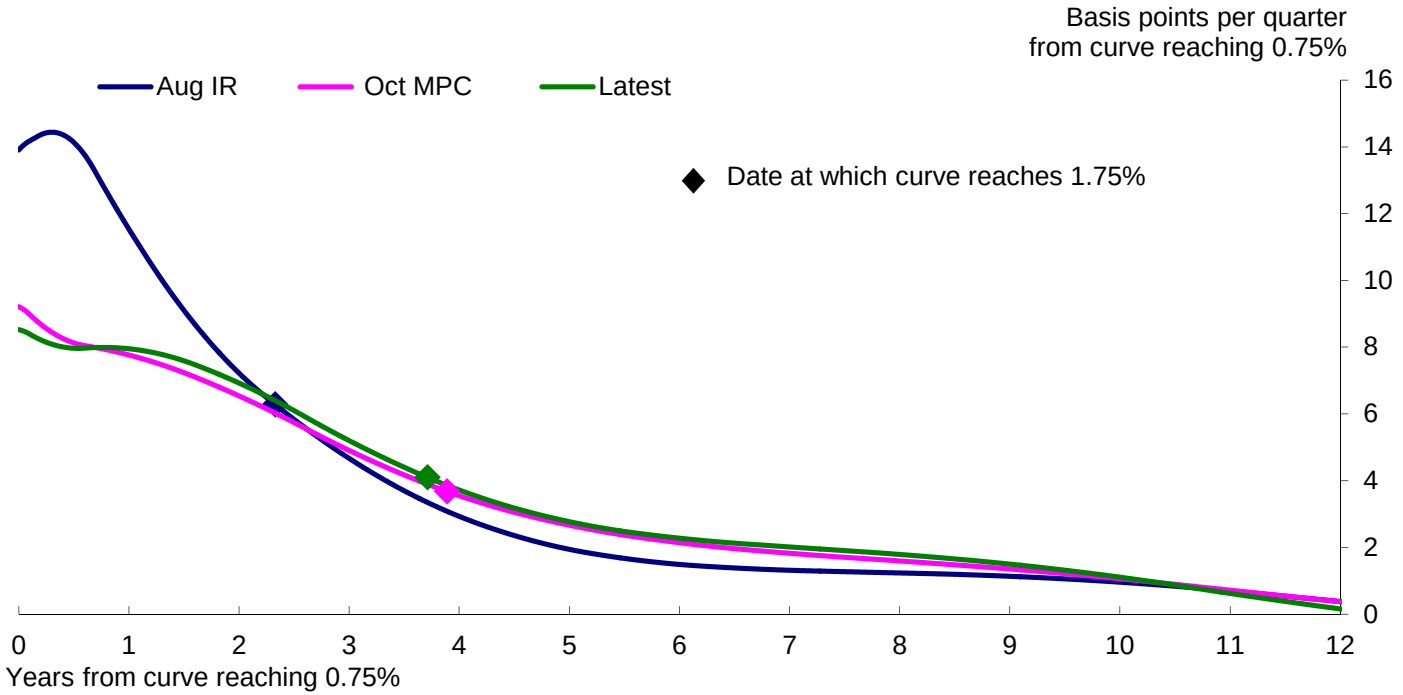


- Significant slowing in the pace of tightening between August IR and time of the October policy meeting

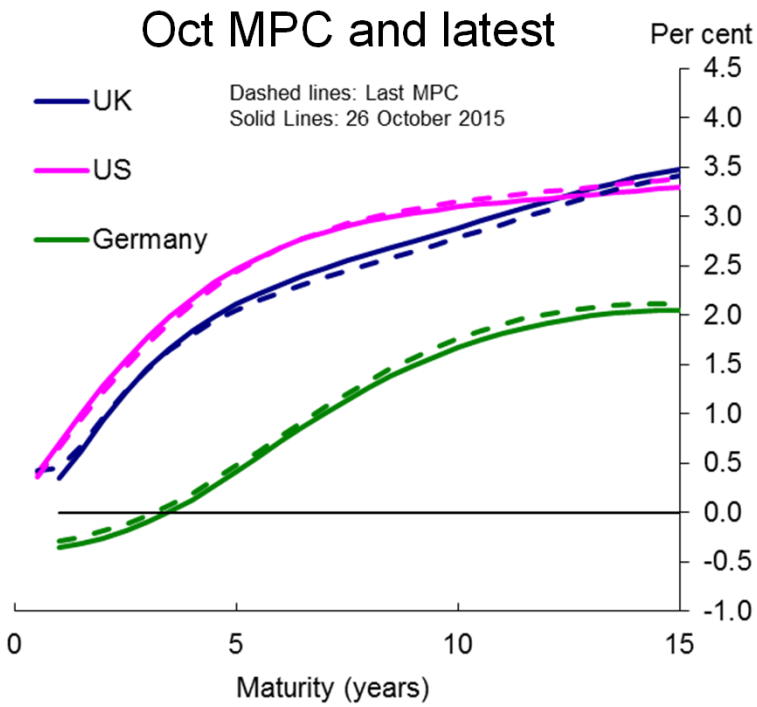
UK pace of tightening

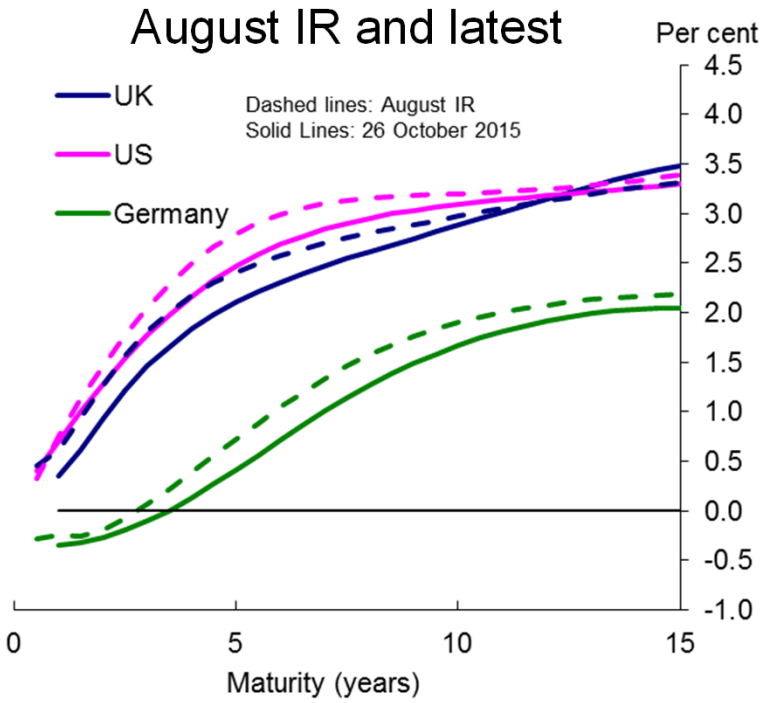


- Significant slowing in the pace of tightening between August IR and time of the October policy meeting
- Pace broadly unchanged compared with October meeting

Long rates

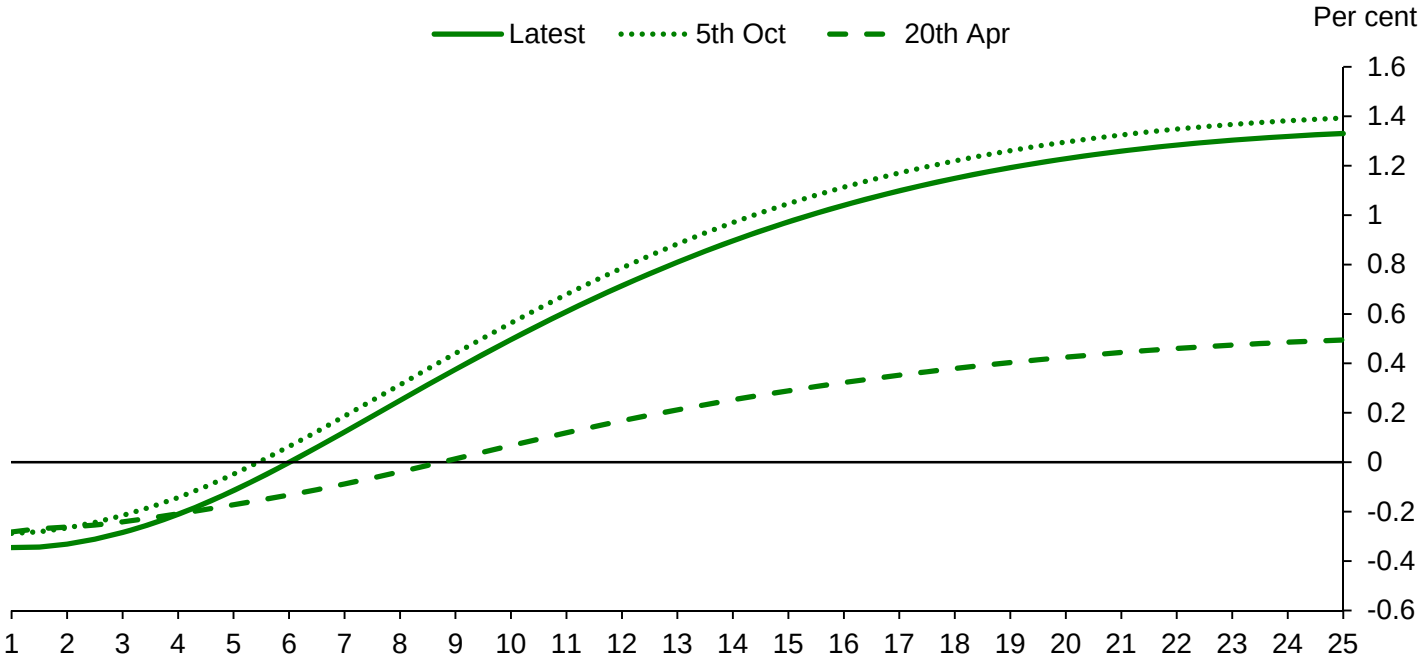
International instantaneous forward yield curves





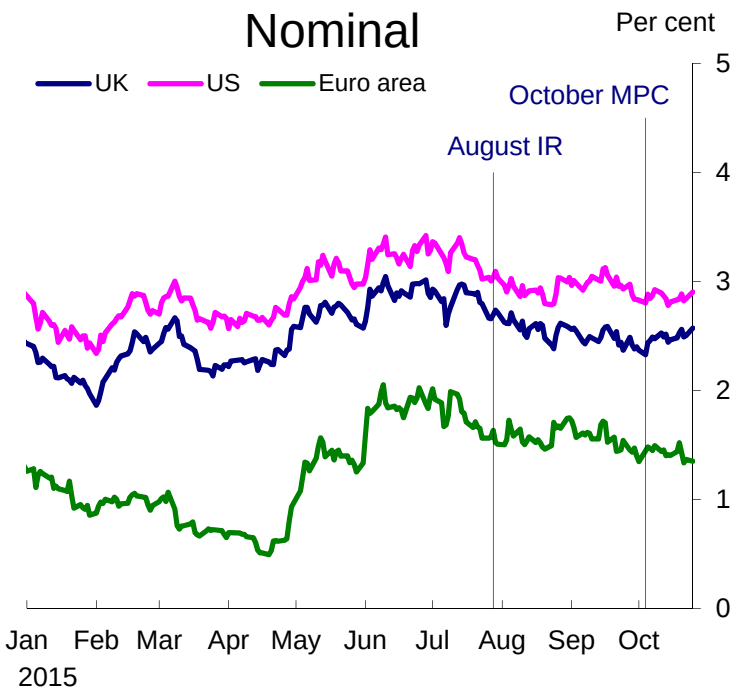
- Little news in long rates on the month
- Long rates somewhat lower than at the time of the August IR

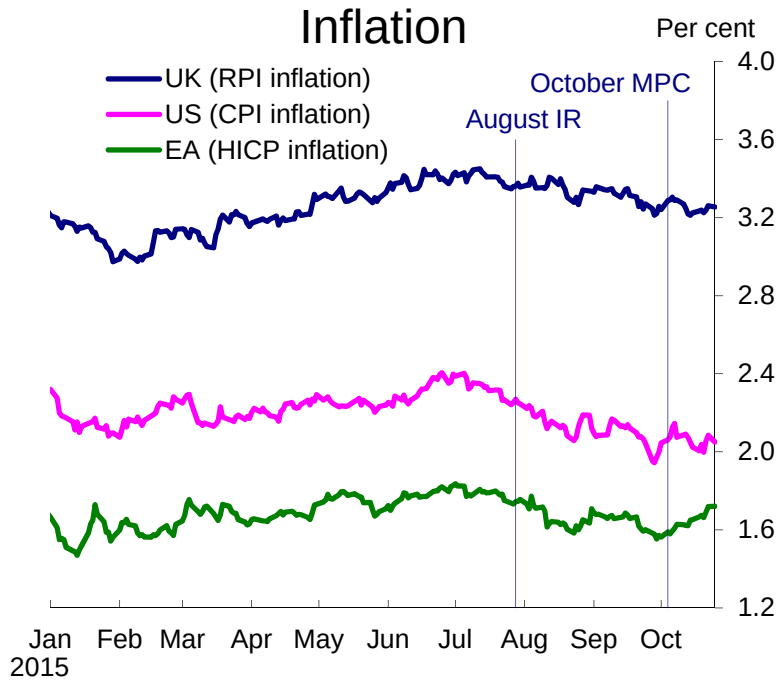
Nominal bund spot yield curve



- Fall in the bund yield curve over the month, leaving more bunds PSPP ineligible
- Curve remains much steeper than observed before the volatile period in the spring

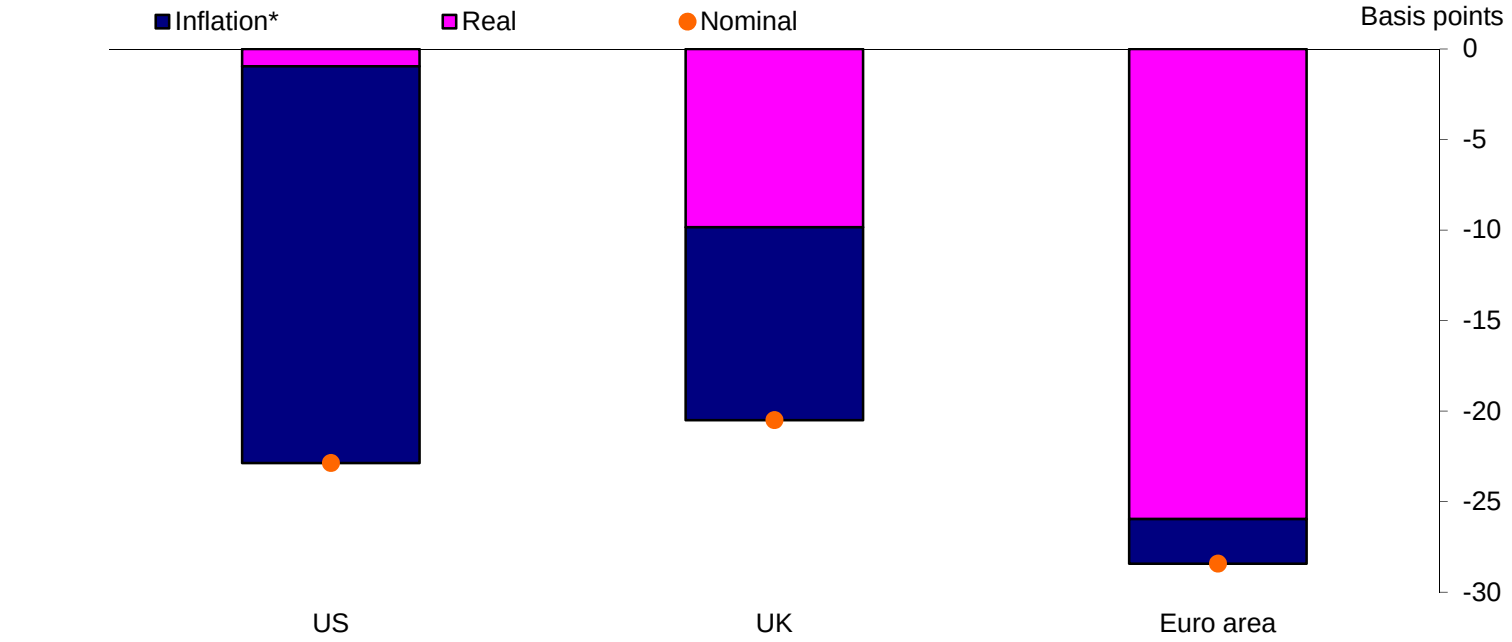
5-year, 5-year forward rates





- 5-year, 5-year rates broadly flat since October policy meeting
- Noteworthy tick up in euro area inflation breakeven

Changes in 5-year, 5-year forward rates since August IR

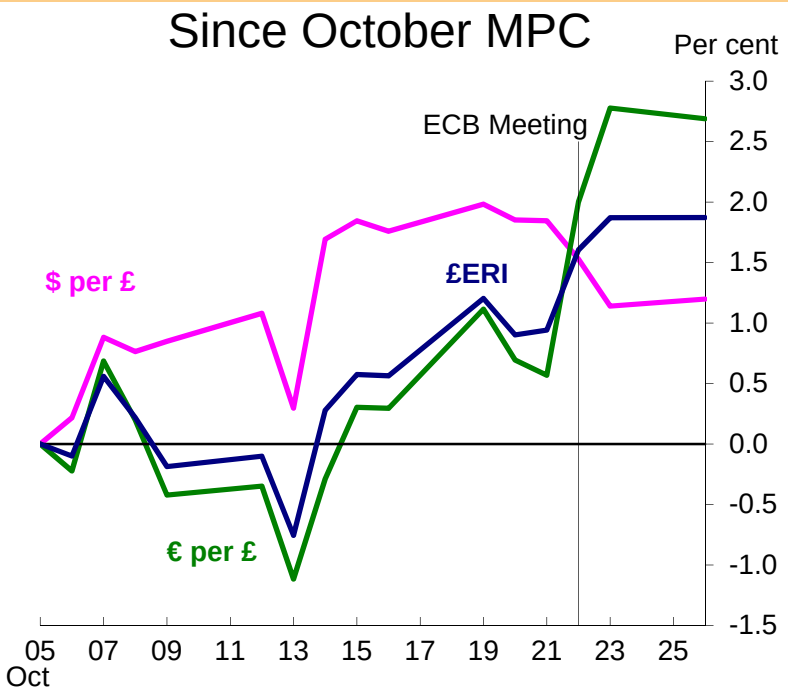


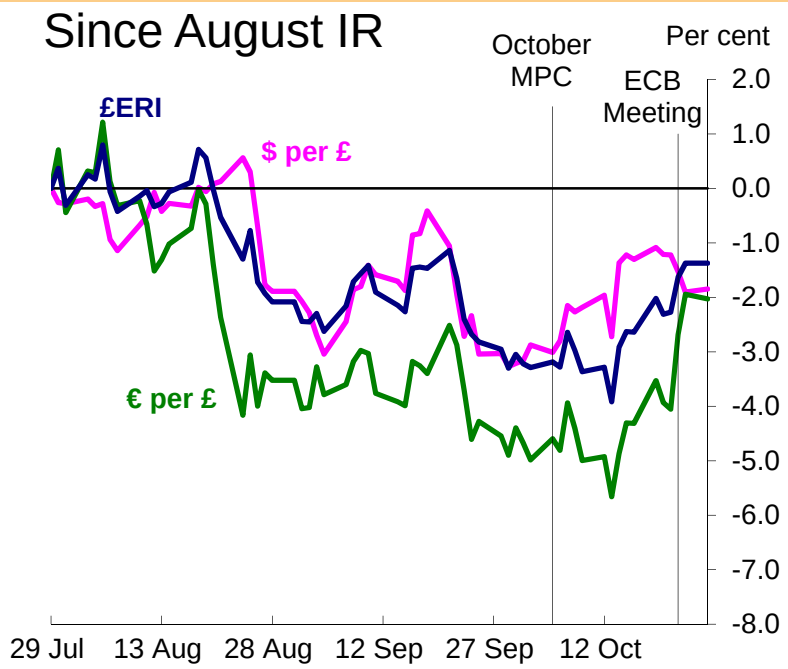
* UK (RPI inflation), US (CPI inflation), Euro area (HICP inflation)

- Fall in euro real rate since August

Exchange rates and risky assets

Cumulative changes in sterling since Aug IR cut off

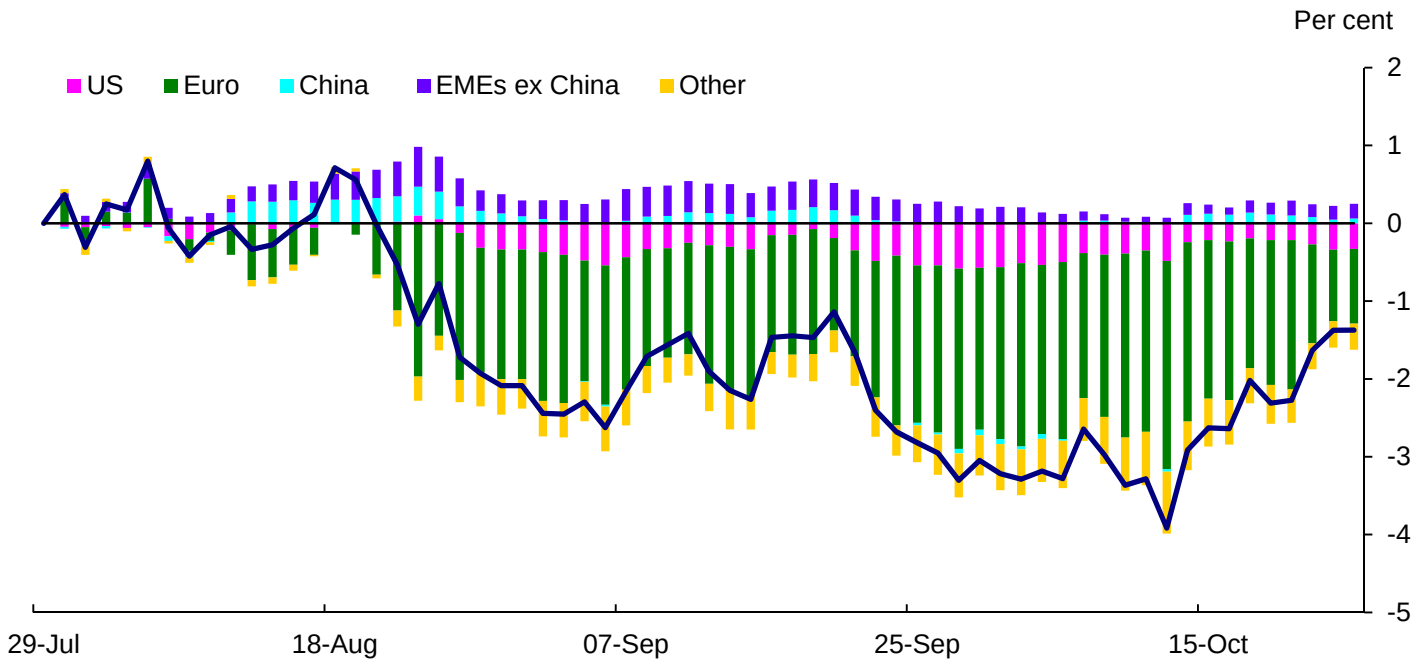




- Sterling ERI has risen by nearly two percent on the month, but 1.4% lower than in August IR

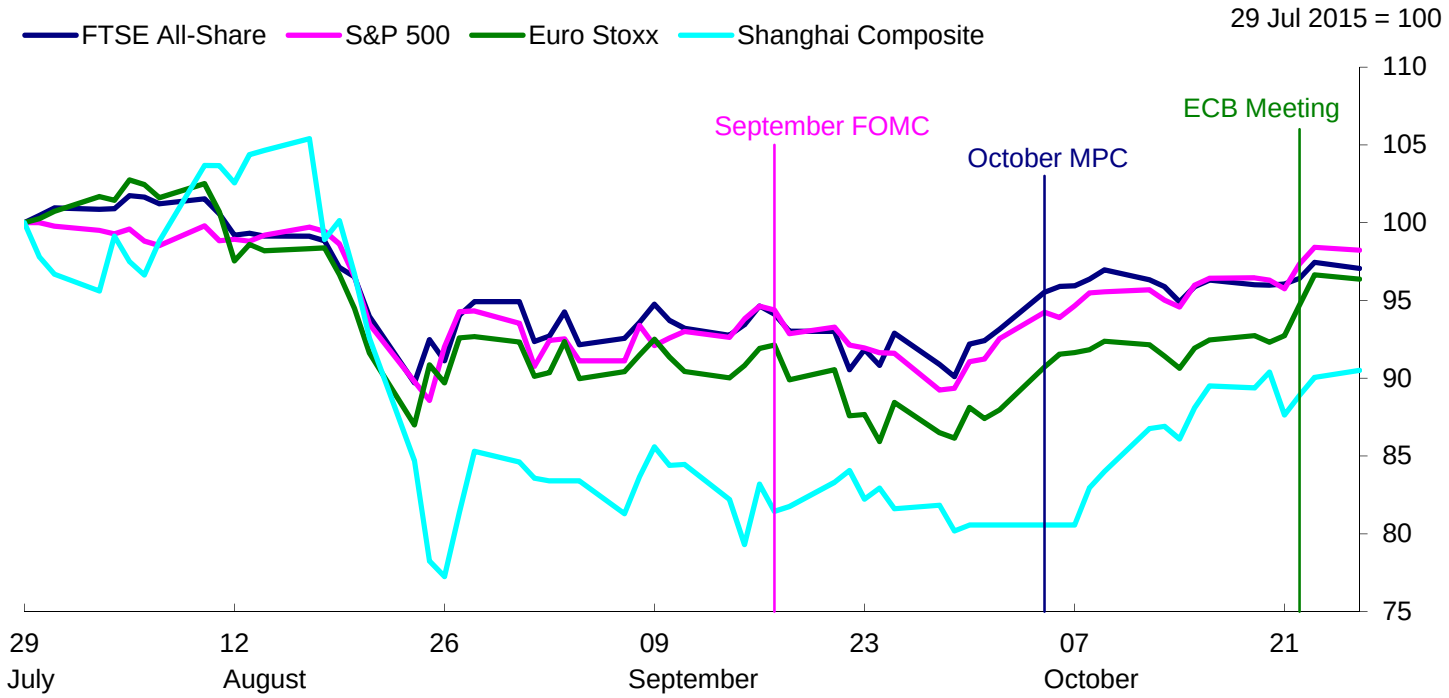
Latest quarterly FX strategy round-up to be circulated later today

Cumulative change in sterling ERI since August IR cut-off



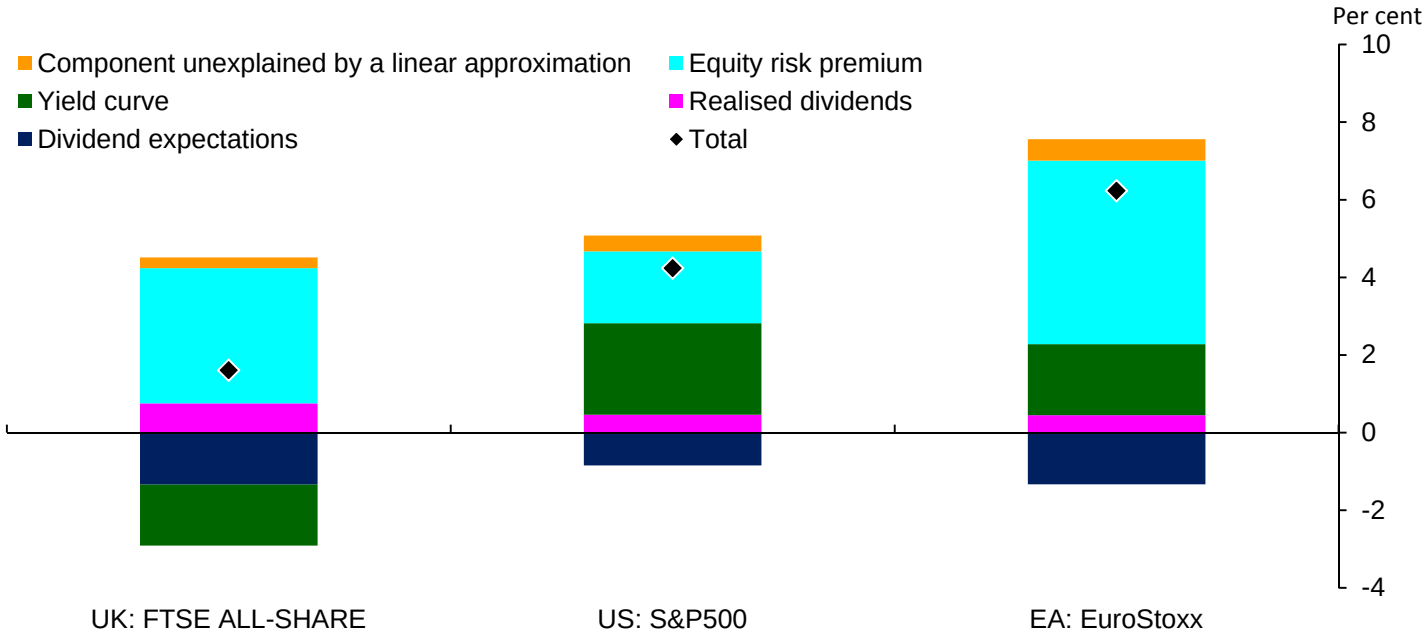
- Fall in sterling since August still largely against the euro

Benchmark equity indices since August IR



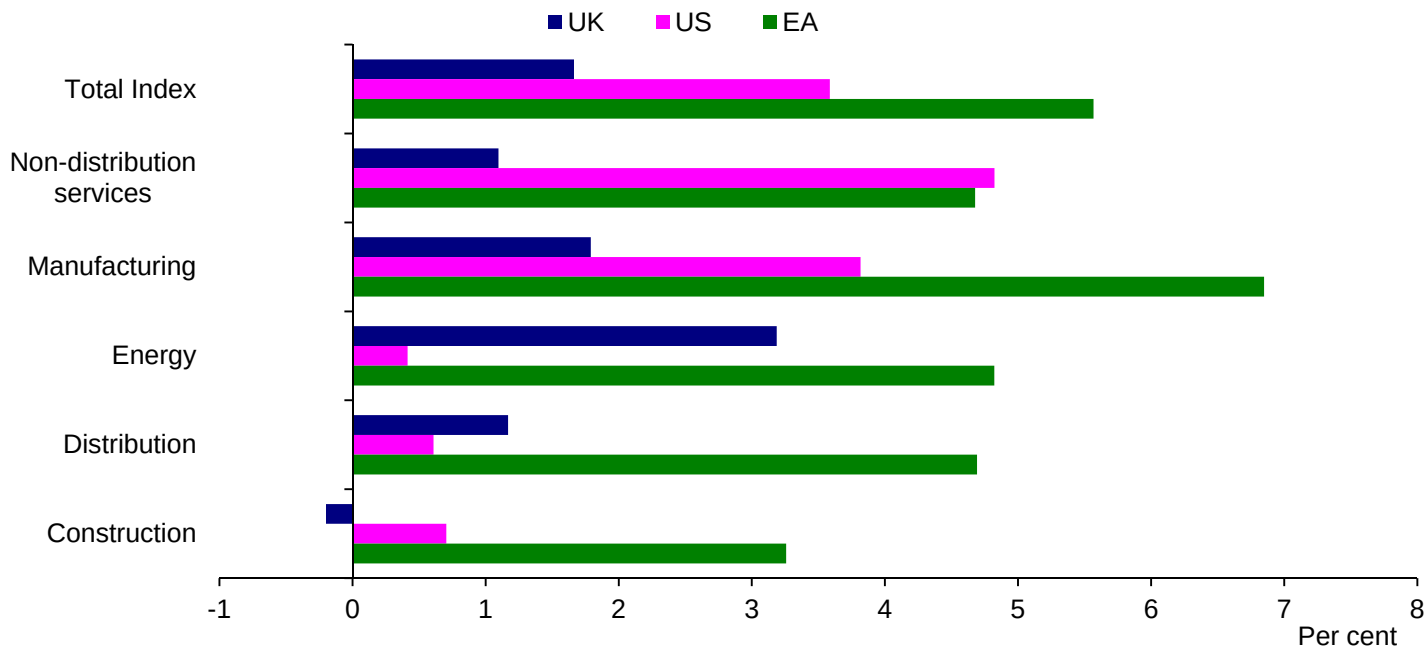
- FTSE All-share down about 3% since August IR
- Much of the decline seen during the volatile period in August has reversed

DDM decomposition of changes in equity prices since Oct MPC



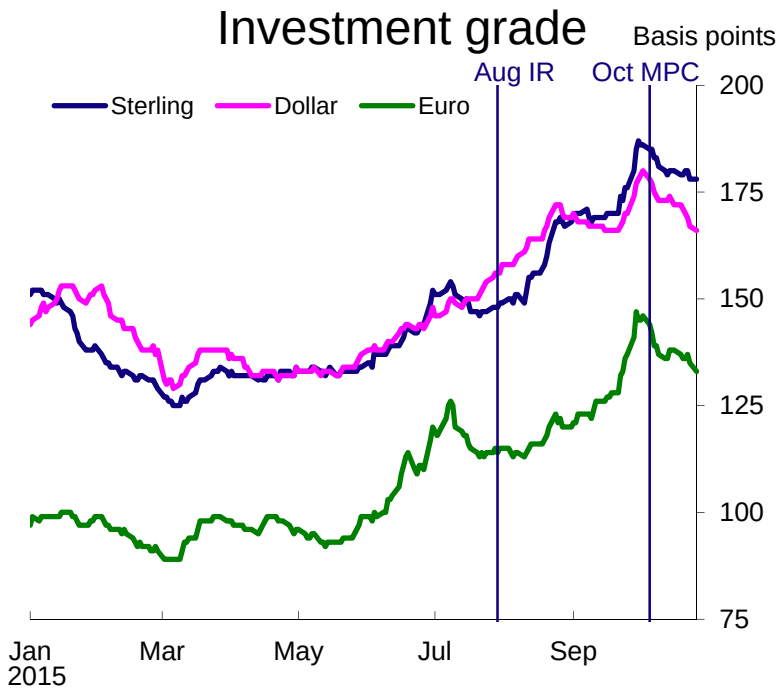
- Recent gains in equities have been driven largely by a fall in the equity risk premium, consistent with improving market sentiment

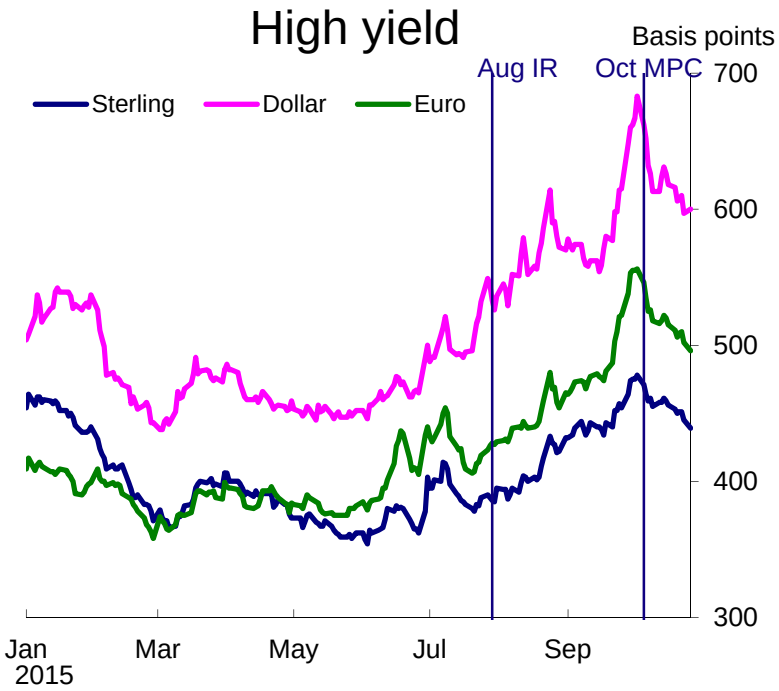
International sector indices since October MPC



- Energy sector has outperformed in the UK compared with elsewhere

Corporate bond spreads





- Narrowing in corporate bond spreads since October MPC
- Spreads remain significantly higher than at the time of the August IR

Key points

- Growing expectation for further central bank loosening
- Materially lower short-term interest rates since August IR
- Appreciation of sterling following latest ECB meeting
- Some recovery in risky asset prices over the past month

2: Global Environment

Bank of England
International Directorate

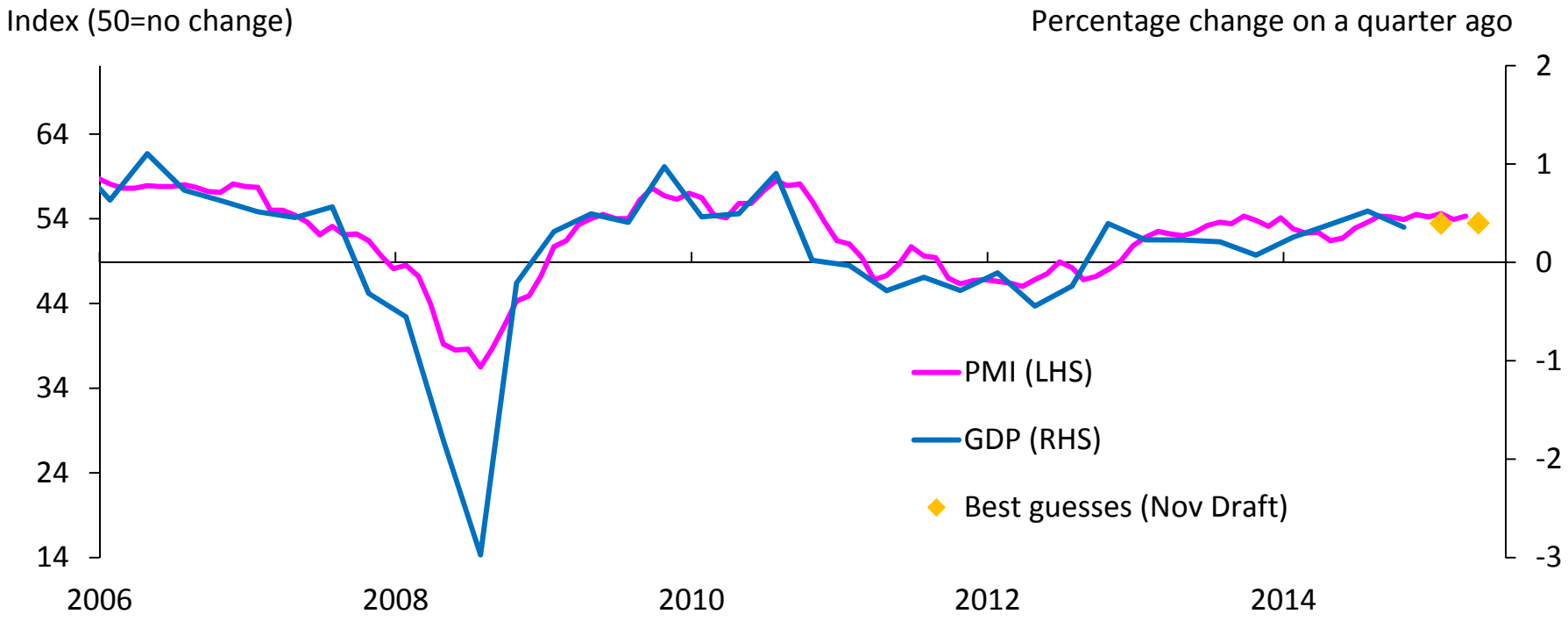
Global Environment and Risks
November 2015

Plan

- Update on developments
  - Euro area
  - US
  - Japan
  - China
- Draft forecast

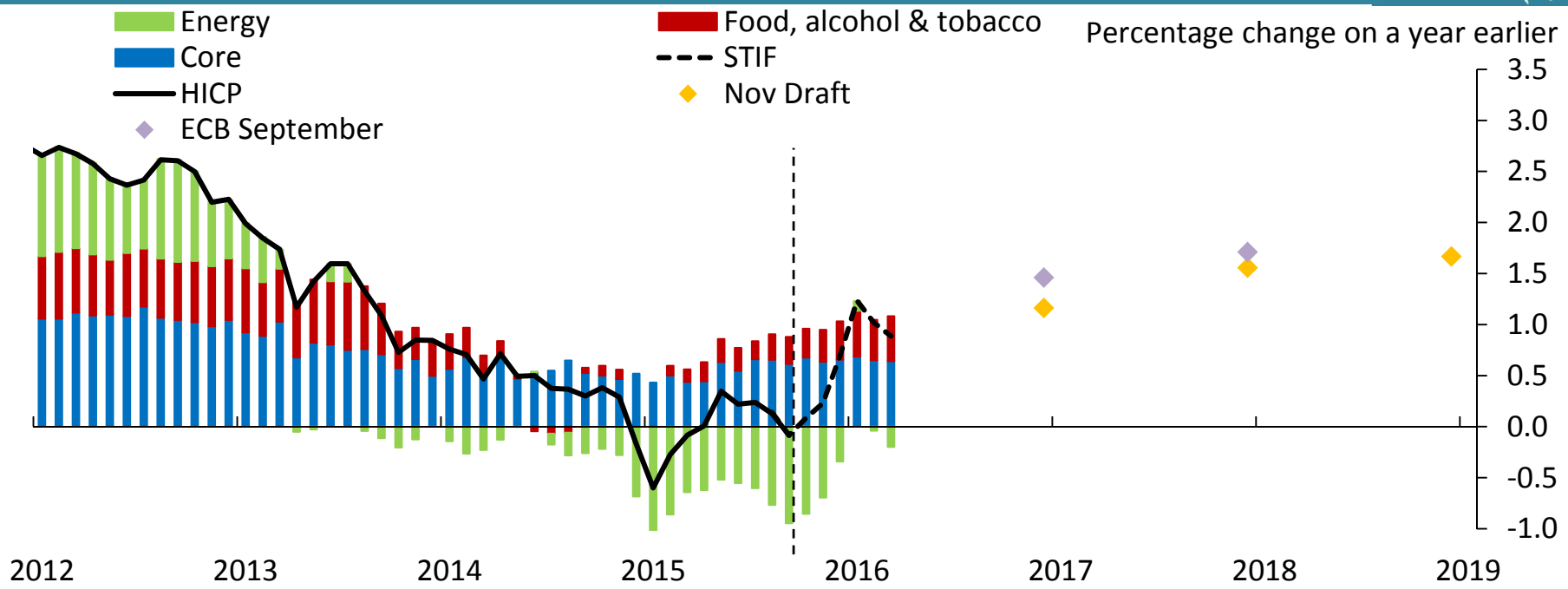
Euro Area

Euro area PMI and GDP



- We still expect 0.4% GDP growth in Q3 and Q4.
- Draft forecast has growth of 1.5% in 2015, 1.7% in 2016 and 2017, and 1.5% 2018

HICP



- Headline inflation for September came in lower than expected at -0.1%. We now expect 0.1% for October.
- Draft forecast has HICP inflation at 1.2% end-2016, 1.6% end-2017 and 1.7% end-2018

ECB policy announcement

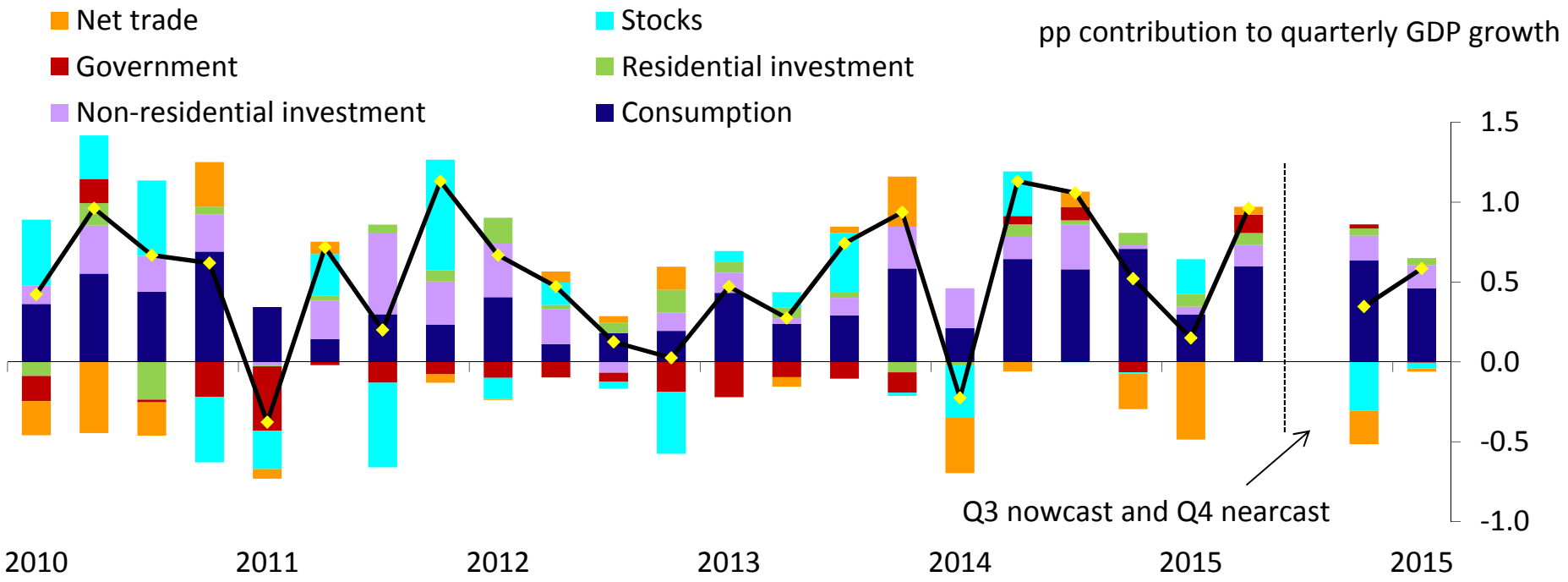
- Last Thursday's ECB press conference was quite dovish.
- President Draghi stressed that all policy tools will be considered, raising a possibility not only of more QE but also rate cuts.
- The Governing Council will reassess policy at their December meeting.
- More QE would be an upside risk to the EA Draft forecast.
- Since the press conference the euro ERI has fallen by almost 2%.

Greece update

- **31 Oct: AQR and stress test of Greek banks published**
  - Increasing likelihood of private sector involvement
- **15 Nov: deadline for second tranche of ESM recapitalisation funds (€15bn) to be released**
  - Unlikely to be a hard deadline
- **Nov/Dec: First review of ESM programme expected**
  - Pushed back due to reform implementation delays
- **31 Dec: Target date for bank recapitalisation**
  - As of 1 Jan 2016, BRRD comes into force, meaning depositor bail-in

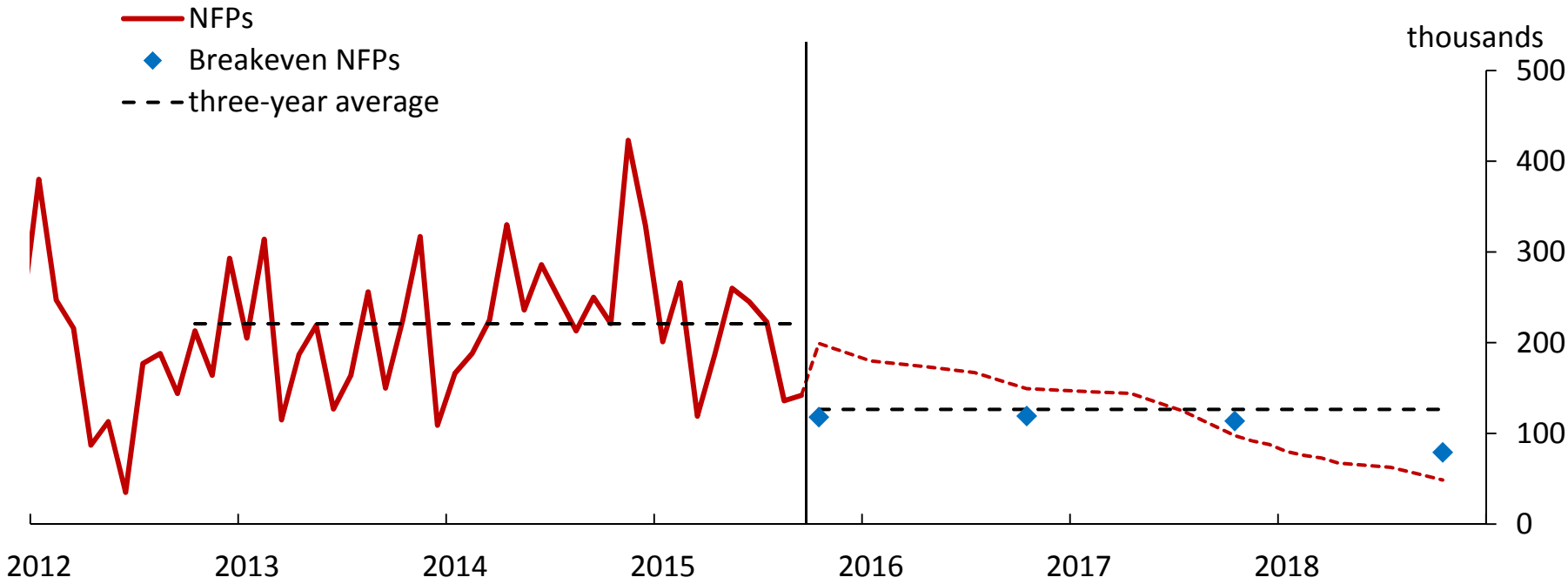
United States

US GDP



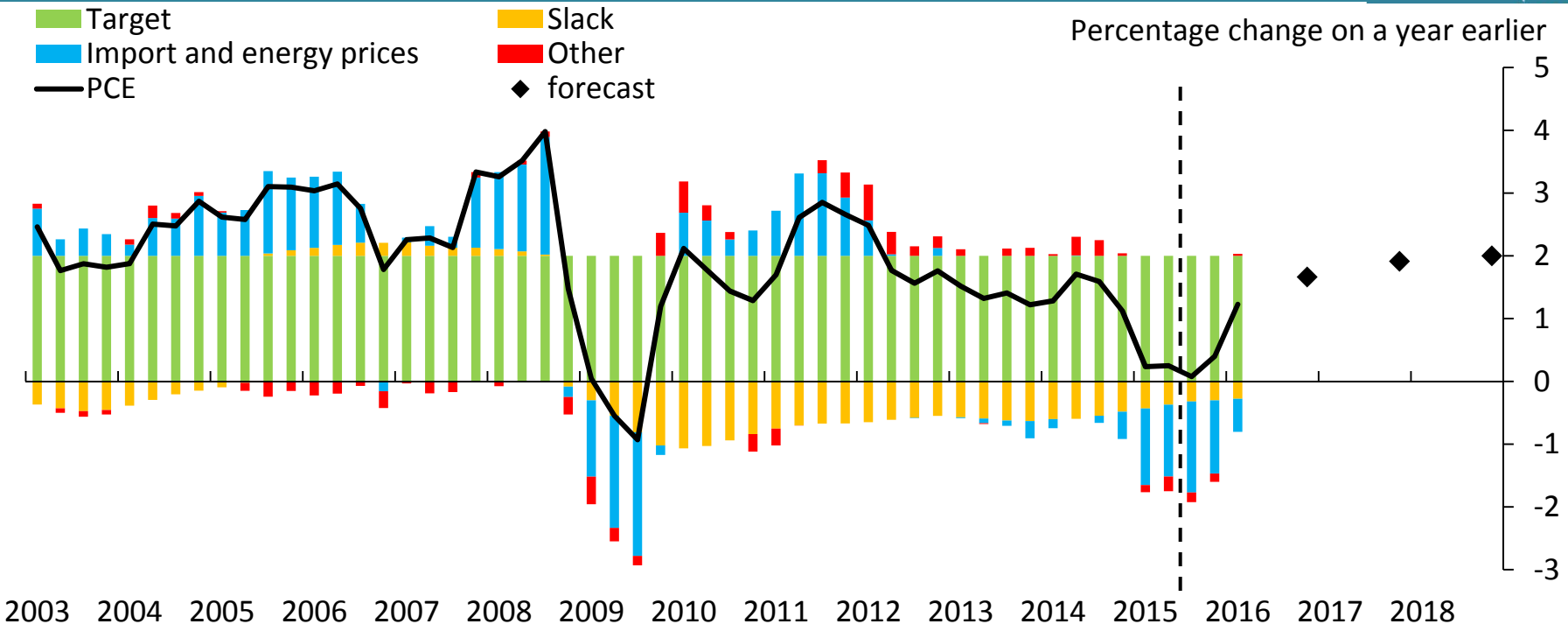
- Growth has been volatile through this year. We expect 0.3% in Q3 and 0.6% in Q4.
- Draft forecast has growth of 2.5% in 2015, 2.4% 2016, 2.2% 2017 and 2.0% 2018.

US Non-Farm Payrolls



- Employment growth expected to average 125k over the forecast: weaker than the average of 220k over past 3 years.
- Estimate of breakeven NFPs over next year is 120k - in the range of fed officials' estimates (70-150k).

US PCE Inflation



- Headline PCE Inflation was 0.3% in August, and core PCE Inflation was 1.3% in August.
- Forecast is for headline PCE Inflation to increase to 1.7% by end-2016, and to hit target of 2.0% in 2018.

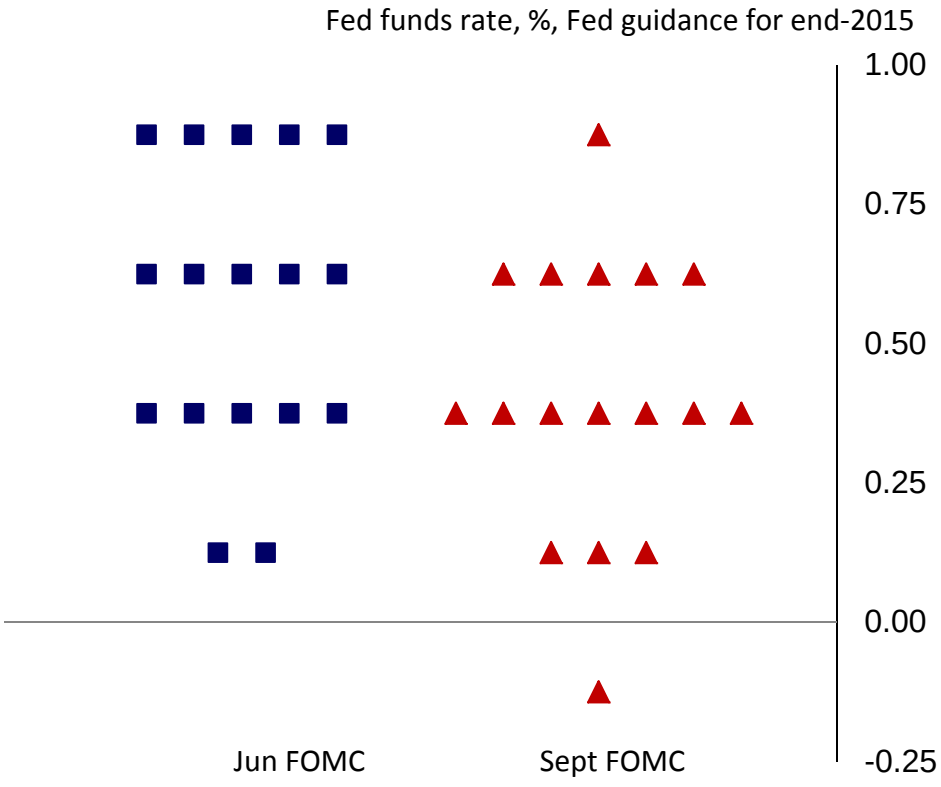
UK & US Inflation Breakdown

UK			
Contribution to yoy inflation	97-07 average*	Sept-15	Difference (Sept vs 97-07)
Services	1.6	1.1	-0.4
Energy, food and other goods	0.4	-1.3	-1.7
CPI	2	-0.1	-2.1

US			
Contribution to yoy inflation	99-07 average*	Aug-15	Difference (Sept vs 99-07)
Services	1.6	1	-0.6
Energy, food and other goods	0.6	-0.7	-1.3
PCE	2.2	0.3	-1.9

- Energy, food and other goods account for 4/5^{ths} of UK inflation weakness and 2/3^{rds} of US weakness.

Disagreements on FOMC



"I anticipate that it will likely be appropriate to raise the target range for the federal funds rate sometime later this year."
– Janet Yellen, 24 Sept.

"I believe the economy remains on a satisfactory track, and…I see a lift-off decision later this year at the October or December FOMC meetings as likely appropriate."
– Dennis Lockhart, 9 Oct.

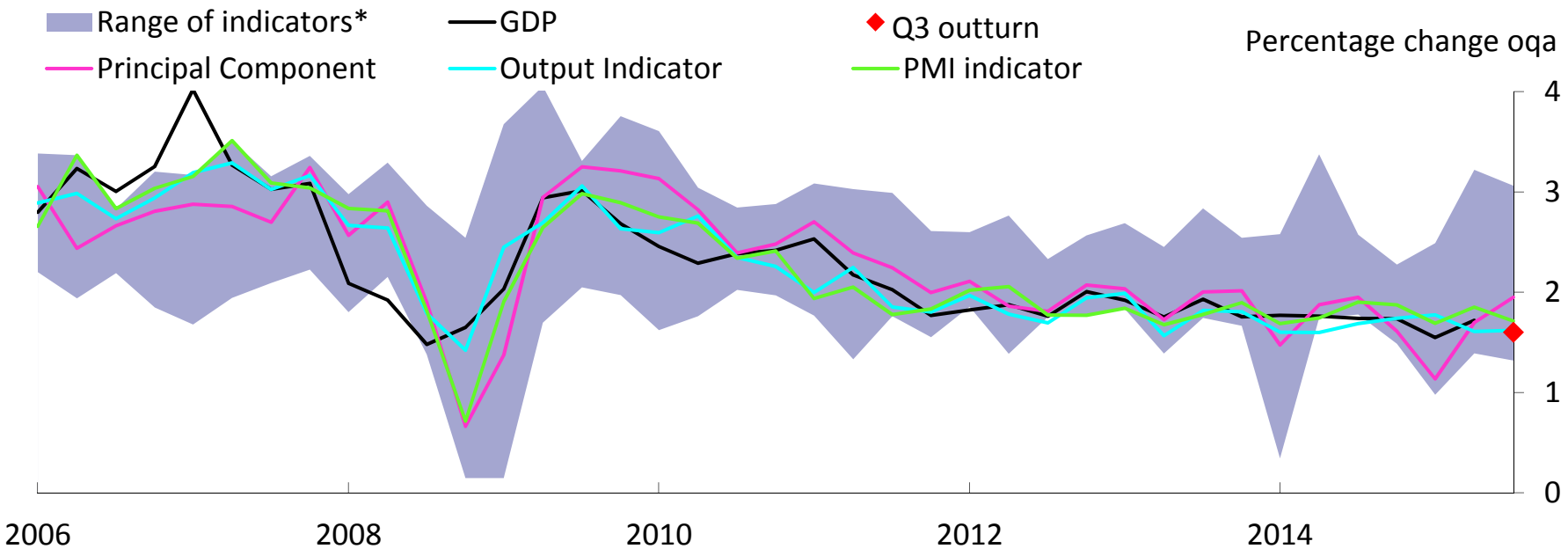
"Based on my forecasts, yes, I am." (responding to question if he is in the camp that thinks a rate hike in 2015 is likely)
– William Dudley, 9 Oct.

"Risk-management considerations counsel a stance of waiting to see if the risks to the outlook diminish."
- Lael Brainard, 12 Oct.

"Right now my expectation is—given where I think the economy would go—I wouldn't expect it would be appropriate to raise rates [this year]."
- Daniel Tarullo, 13 Oct.

China

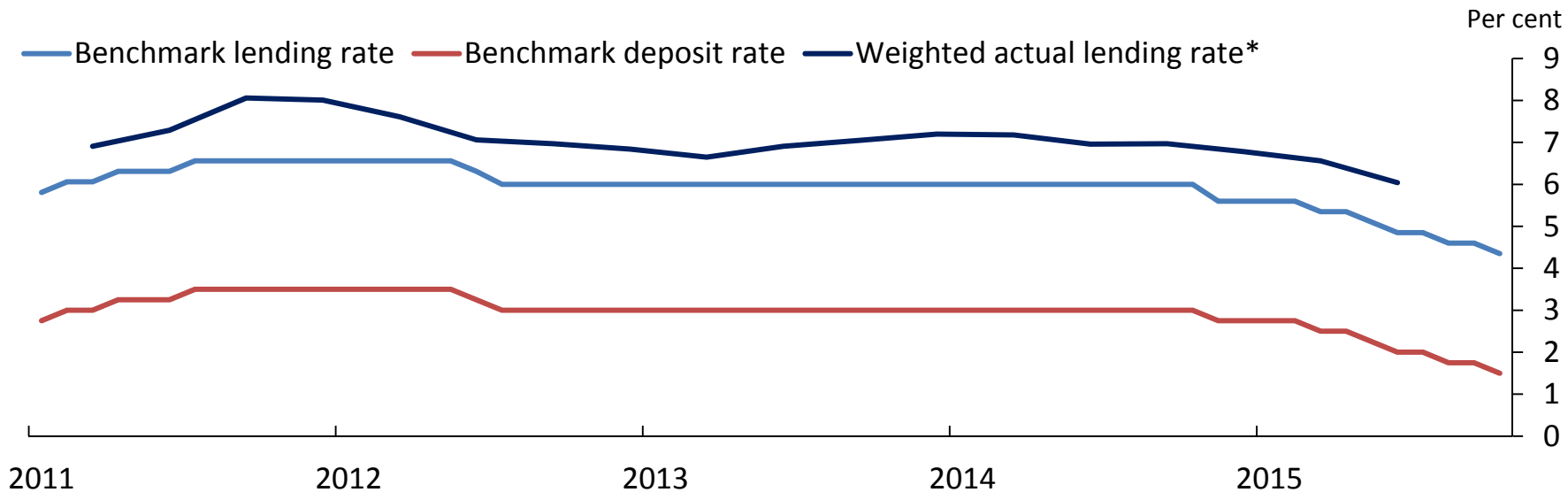
Q3 GDP and indicators



- Official Q3 GDP 1.8% oqa (0.1pp higher than market expectations). OECD Q3 GDP 1.6% oqa (same as Nowcast)
- Mixed indicators: IP fell to 5.7% oya in September; retail sales picked up slightly to 10.9%.
- 5th Plenum 26-29 October: we expect 2016 growth target of 6.5% or a range 6-7% to be announced
- Draft forecast: 6.7% 2015; 6.3% 2016; 6.0 in 2017 and 2018.

Policy

Benchmark rates



- Benchmark interest rates cut by a further 25bp.
- Deposit rate ceiling has now been removed, liberalising domestic interest rates.

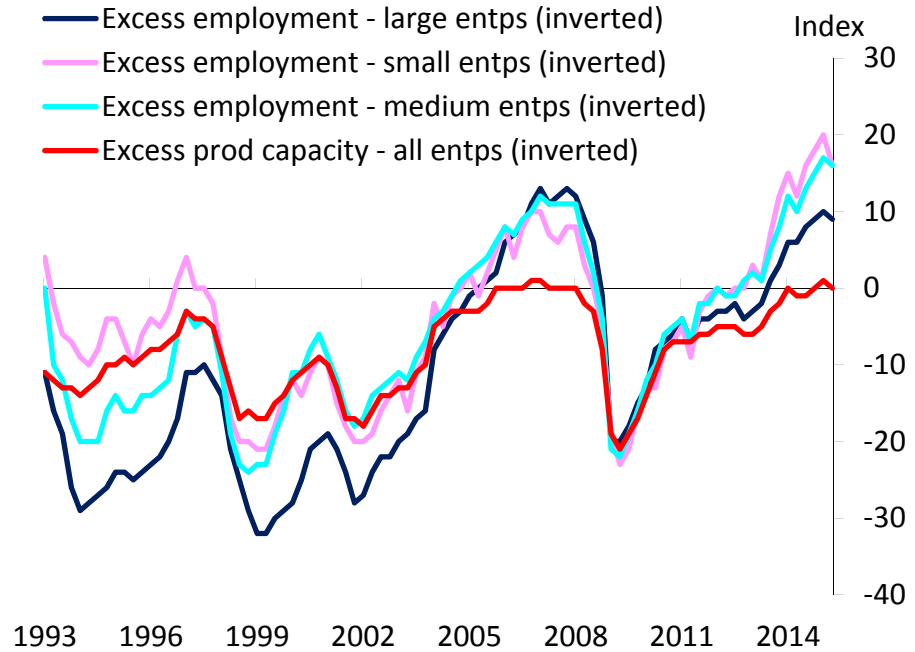
For more information

Japan

Slack has been eroding, but some remains…

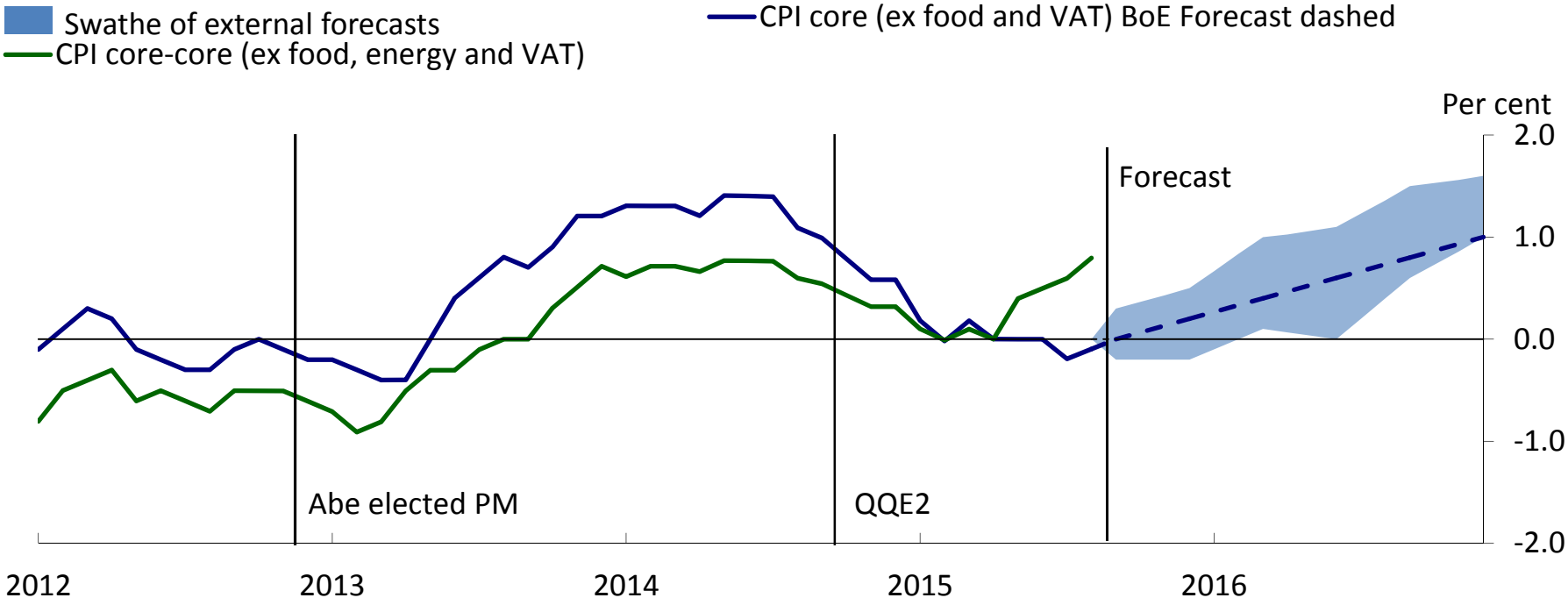
Labour market

Tankan excess capacity vs employment



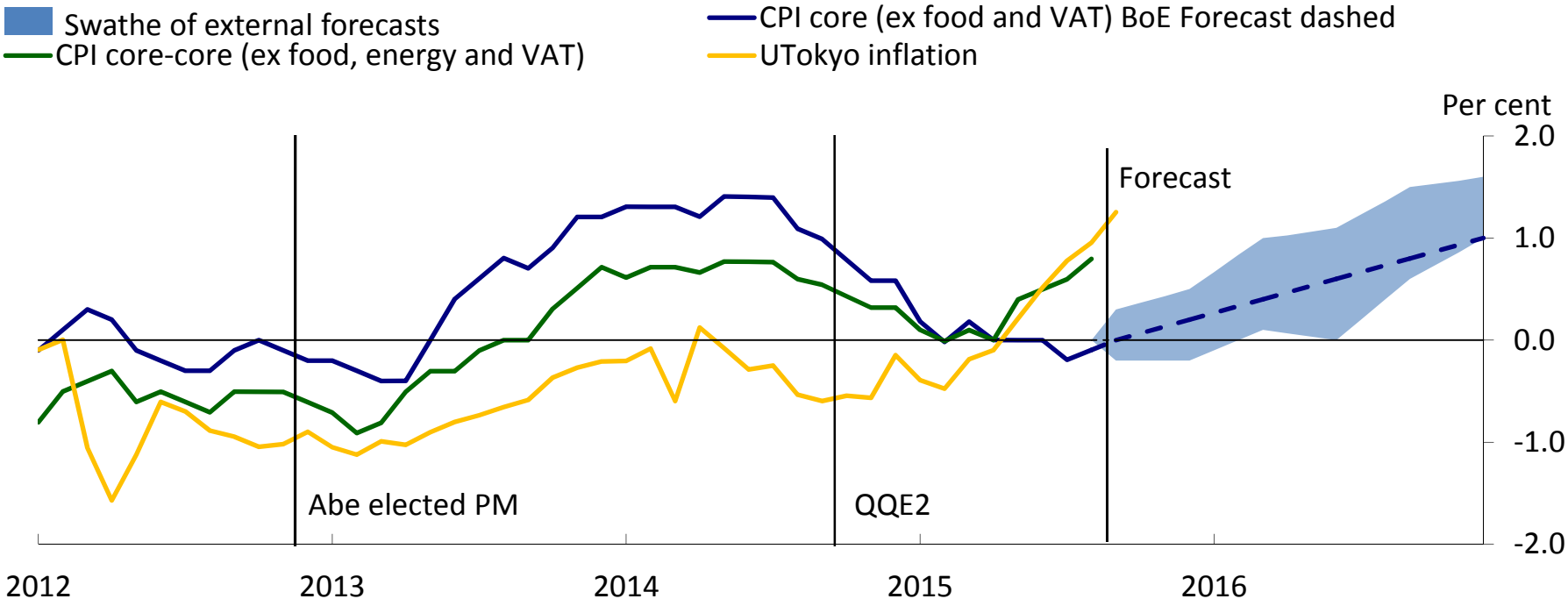
- Unemployment has fallen steadily over past 5 years and sits at 3.4% .
- Tankan survey suggests labour shortages and no slack within firms.

Core inflation measures risen sharply



- Striking rise in 'core' inflation metrics (ex. food and energy).
- Inflation forecast to rise to 1%, but likely to fall short of 2% target.

Core inflation measures risen sharply



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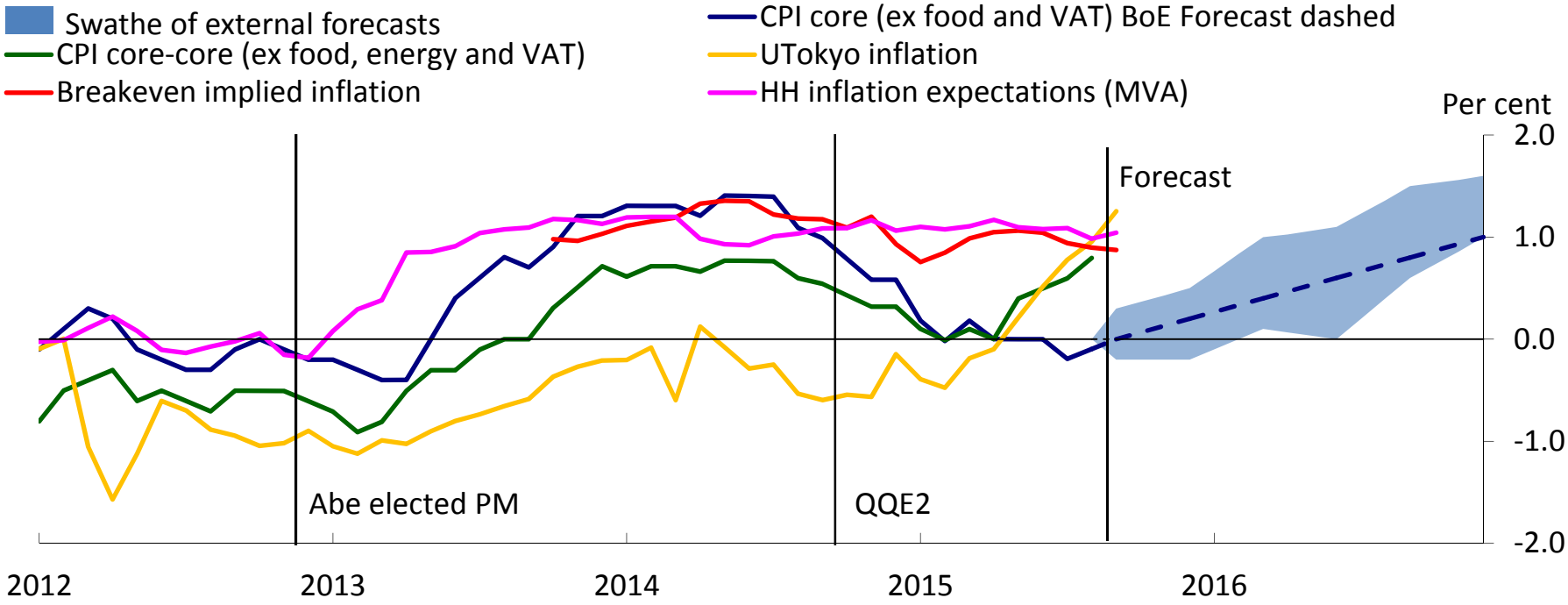
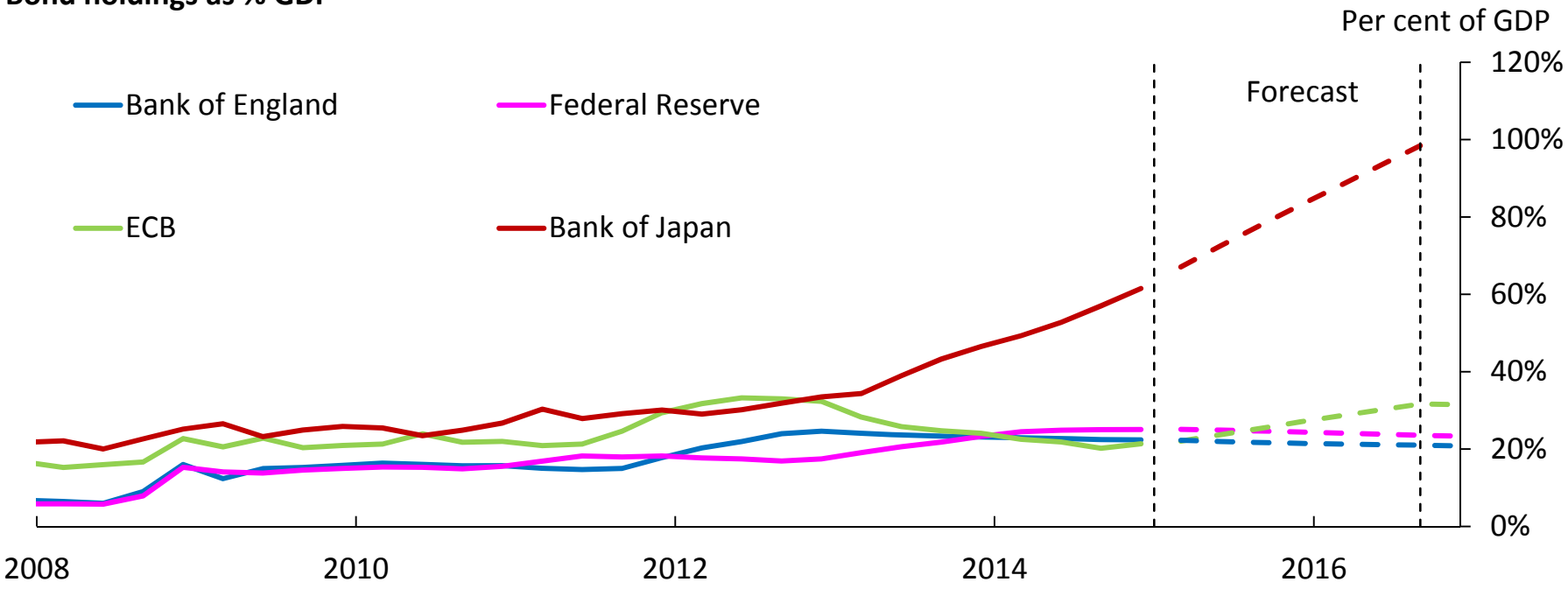


- Striking rise in 'core' inflation metrics (ex. food and energy).
- Inflation forecast to rise to 1%, but likely to fall short of 2% target.

“Shock & awe” from the BoJ

Bond holdings as % GDP

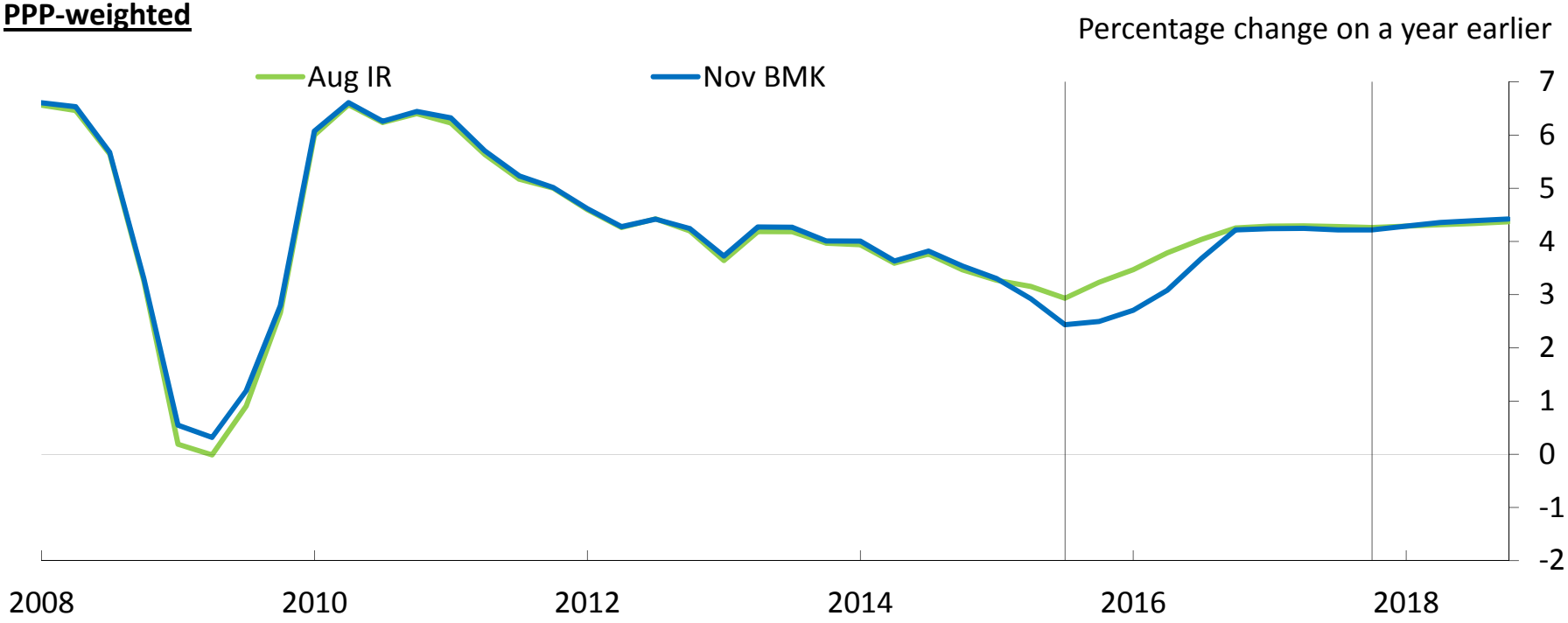


- QQE is more than double the size of US QE3 relative to size of economy.
- Not clear that even this is enough: Bloomberg survey showed half expected Oct move.

Draft Forecast

Non-China EM GDP growth forecast

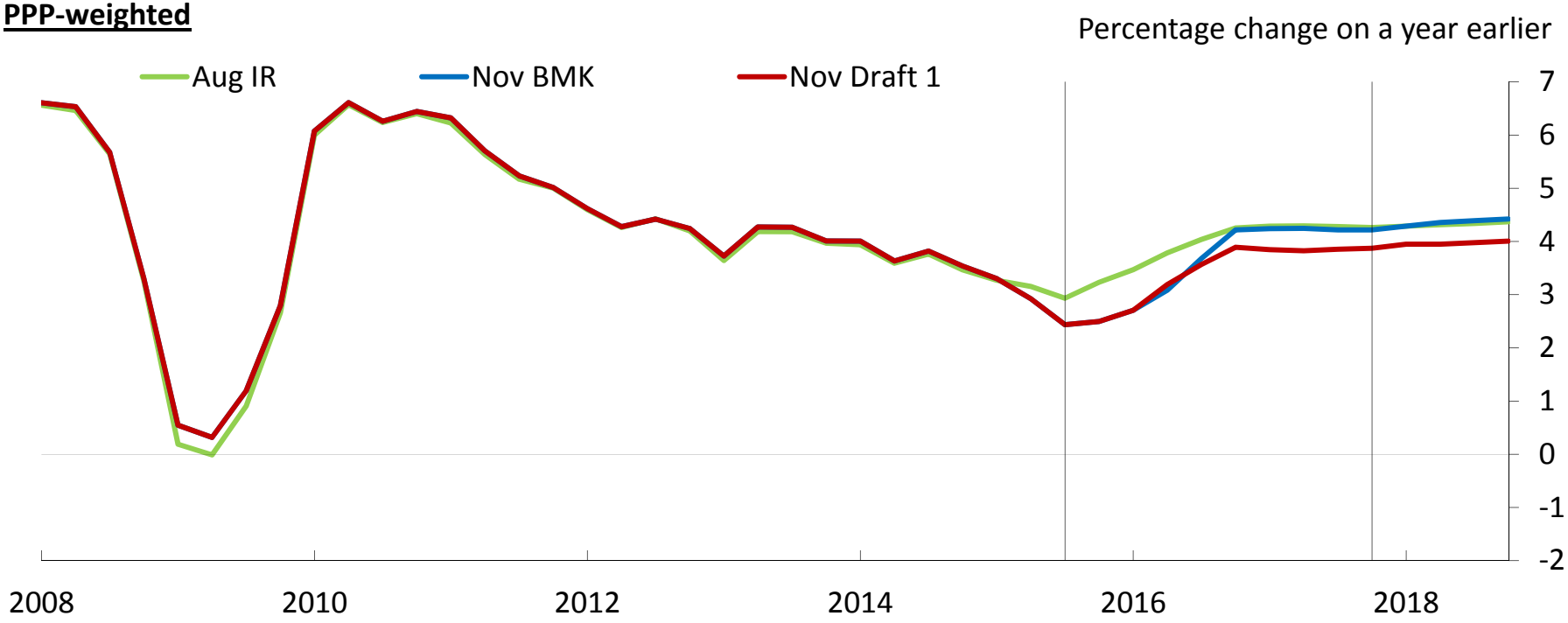
PPP-weighted



- Benchmark revised down to reflect weaker near-term prospects for non-China Ems.

Non-China EM GDP growth forecast

PPP-weighted



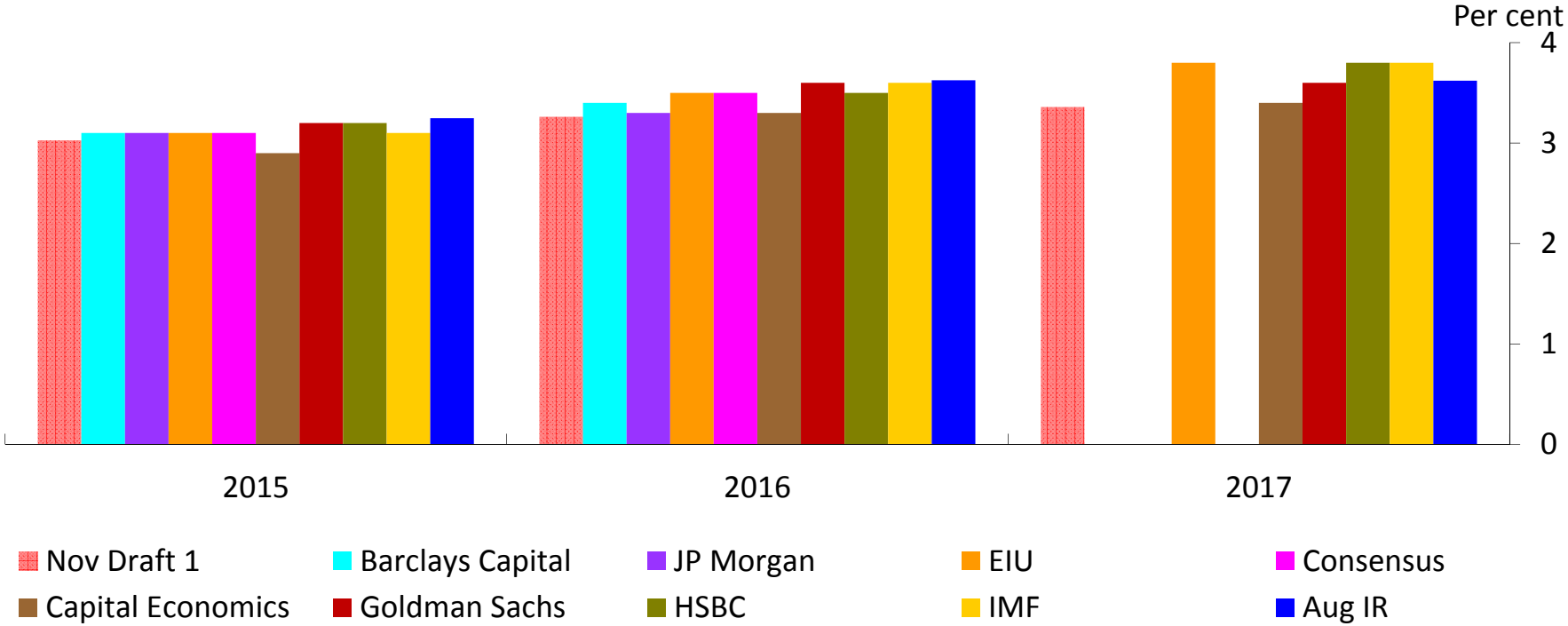
- Following Key Issues we have also revised down medium-term prospects.

Draft forecast

	98-07	2015	2016	2017	2018
World GDP (UK-weighted)	3	2¼ (2¼)	2½ (2¾)	2½ (2¾)	2¼
World GDP (PPP-weighted)	4	3 (3¼)	3¼ (3¾)	3¼ (3½)	3¼
Euro-area GDP	2¼	1½ (1½)	1¾ (1¾)	1¾ (1¾)	1½
US GDP	3	2½ (2½)	2½ (2¾)	2¼ (2¼)	2
EMEs ex. China GDP (PPP-weighted)	4 ½	2¾ (3 ¼)	3 ¼ (4)	3¾ (4¼)	4
Chinese GDP	9¾	6¾ (6¾)	6¼ (6¼)	6 (6¼)	6

**August IR in brackets*

PPP-weighted world GDP growth



- Draft forecast is weaker than externals.

Summary

- US and euro-area growth continues in the face of deteriorating EM prospects.
- Inflation is expected to pick up around the turn of the year.
- The FOMC, the ECB and the BoJ are poised to act.

- China looks set to hit its target of ‘around 7%’ this year…
- …and continues to offer stimulus and reform.

- Draft forecast is for subdued global growth, with all regions weaker than August *IR* and weaker than the IMF.

End

3: Money, Credit and Nominal Trends

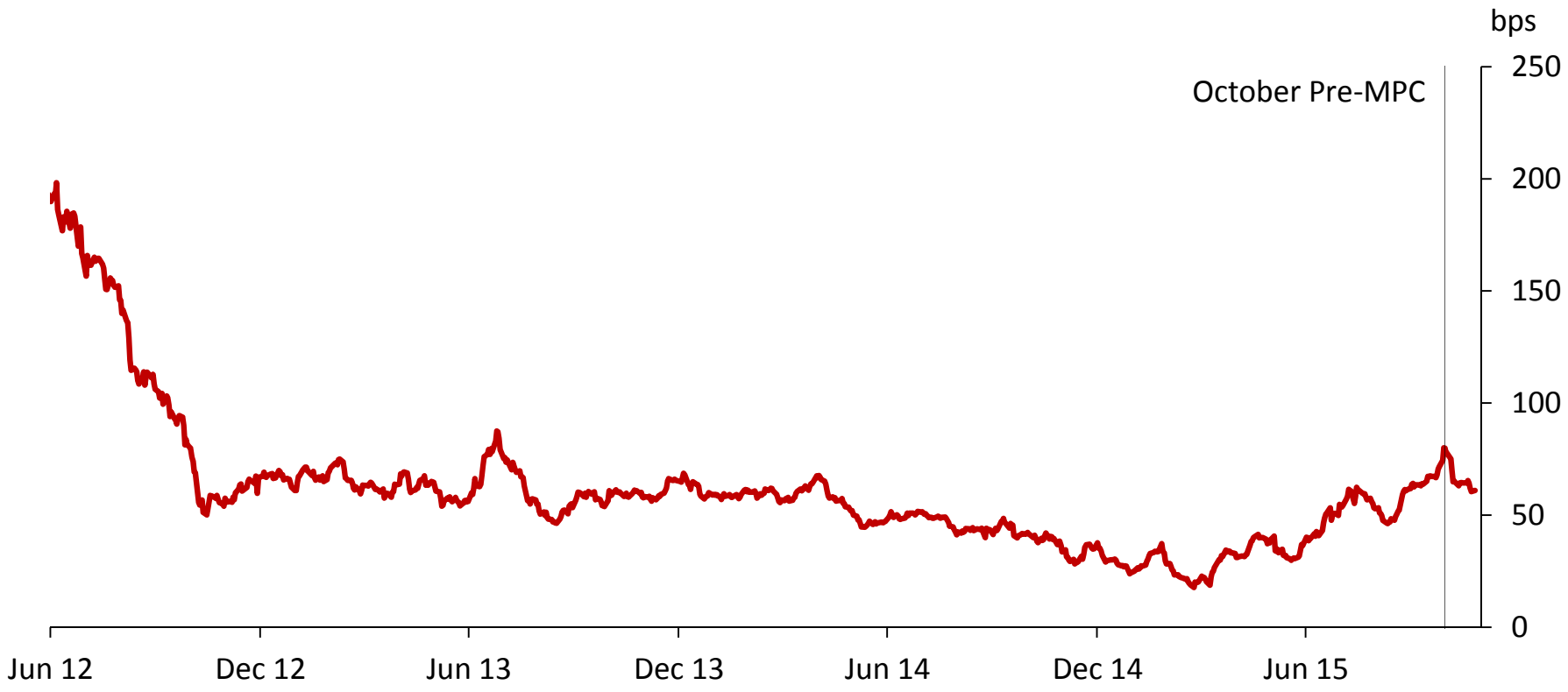
MONEY, CREDIT AND NOMINAL TRENDS November 2015

Agenda

- Bank funding
- Housing market and household debt update
- Corporate deleveraging – transatlantic divergence
- Inflation expectations

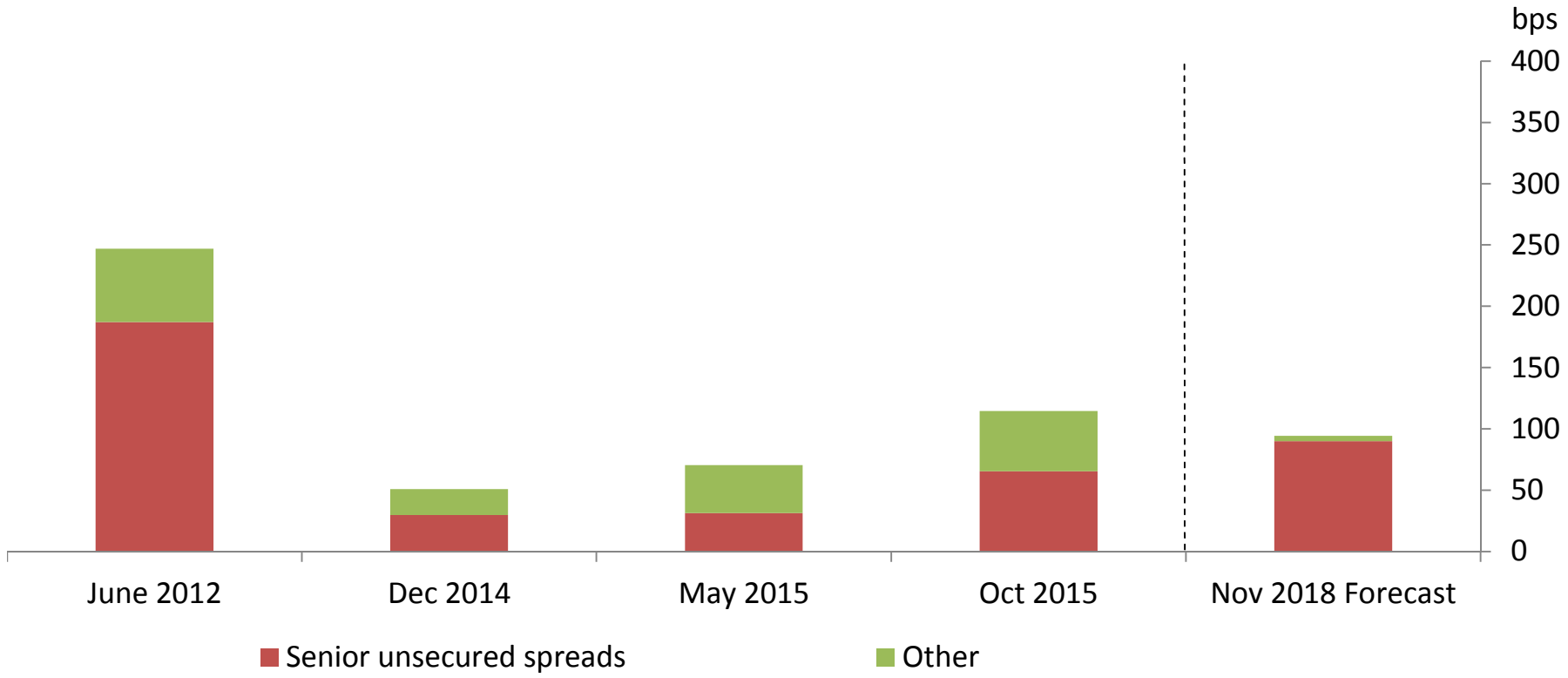
Funding spreads have fallen on the month

Indicative measure of UK banks' 5-year senior unsecured spreads



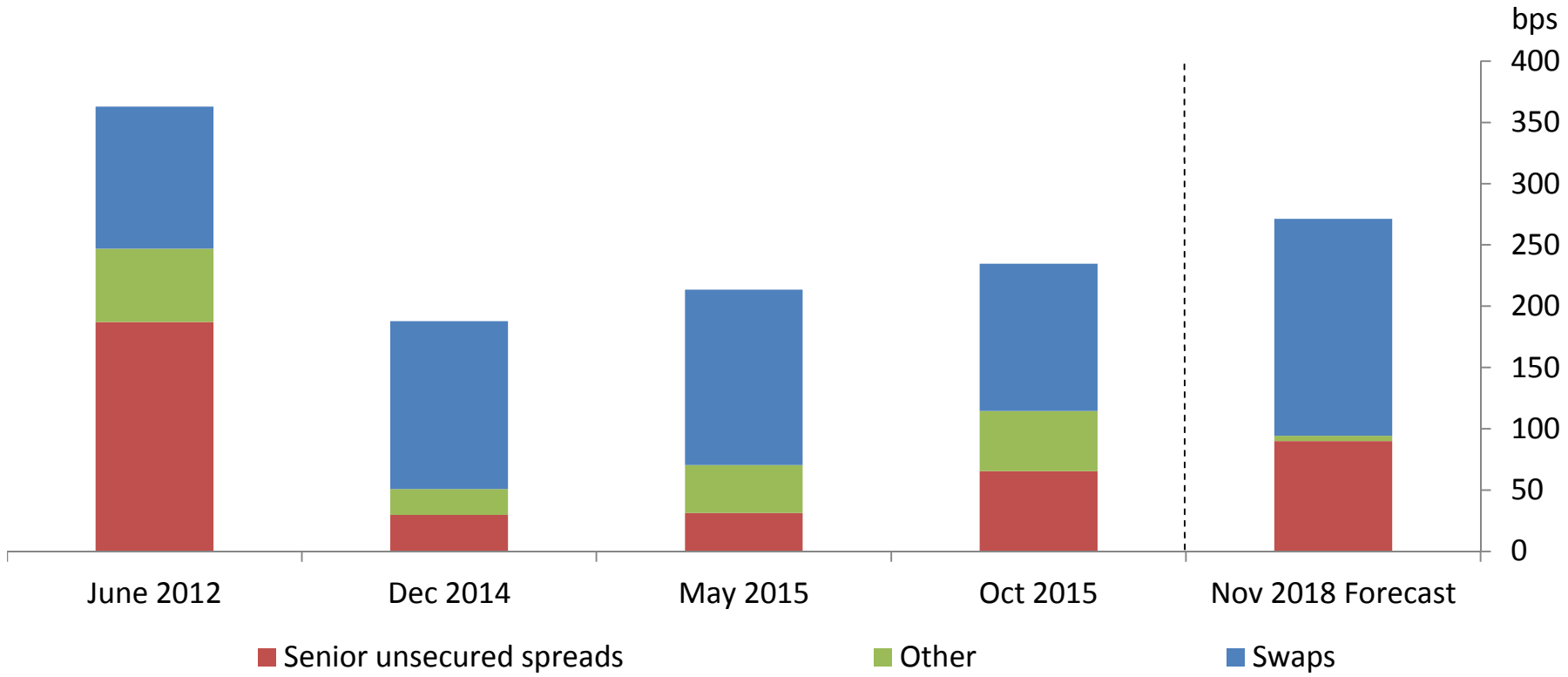
All-in spreads remain elevated relative to H1

Implied measure of UK banks' all-in funding costs



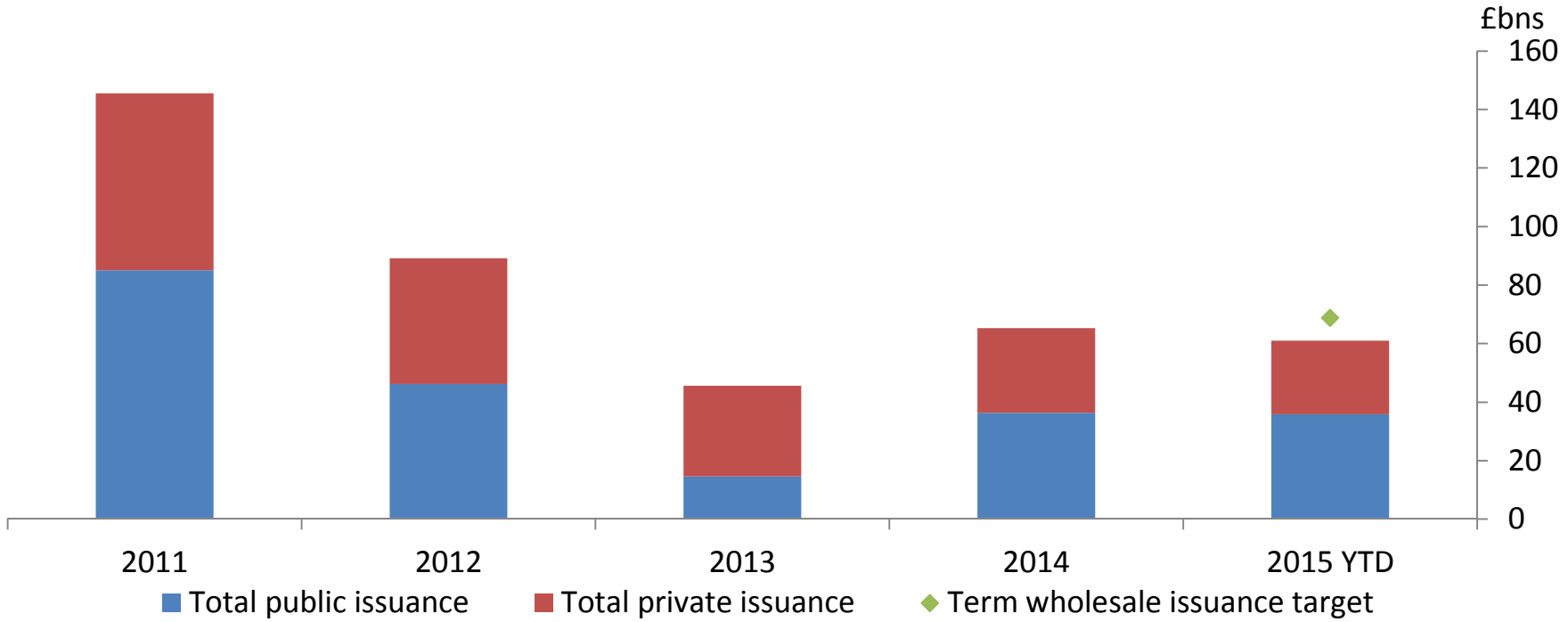
Although the fall in risk-free rates partially offsets that

Implied measure of UK banks' all-in funding costs



Issuance remains on track to meet banks' target

Long-term wholesale issuance* by major UK banks

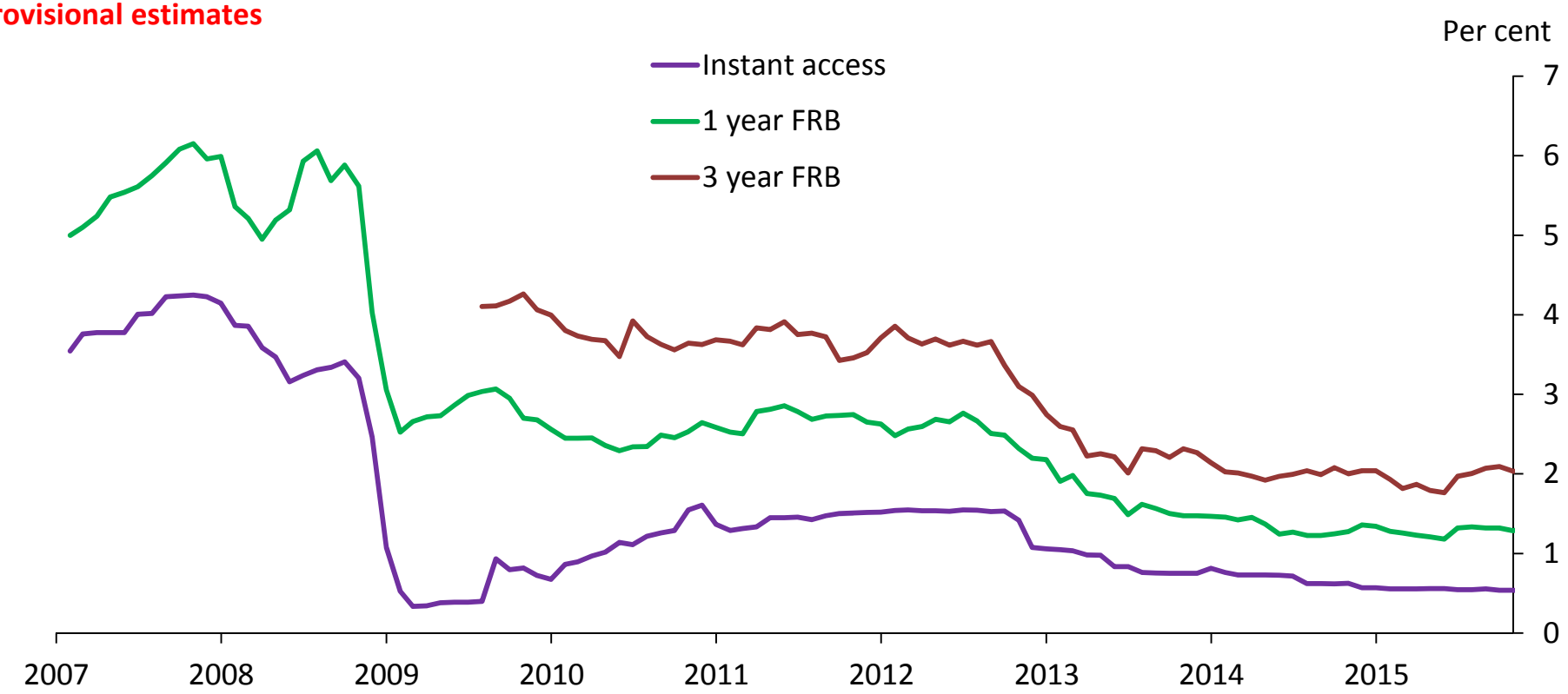


*Bars show secured, senior unsecured and subordinated aggregate issuance, issued both publicly (blue) and privately (red), by major UK banks. Green diamond shows aggregate issuance target provided by banks in Feb 2015.

Deposit rates have remained broadly stable

Quoted deposit rates

Provisional estimates



Reforms to bank taxes do not change ELB

- Nature of bank corporation tax surcharge means our conclusions about the effective lower bound (ELB) for Bank Rate are unchanged
- The reduction in profits due to the tax is very small relative to the impact of the cut in Bank Rate itself

Summary on bank funding

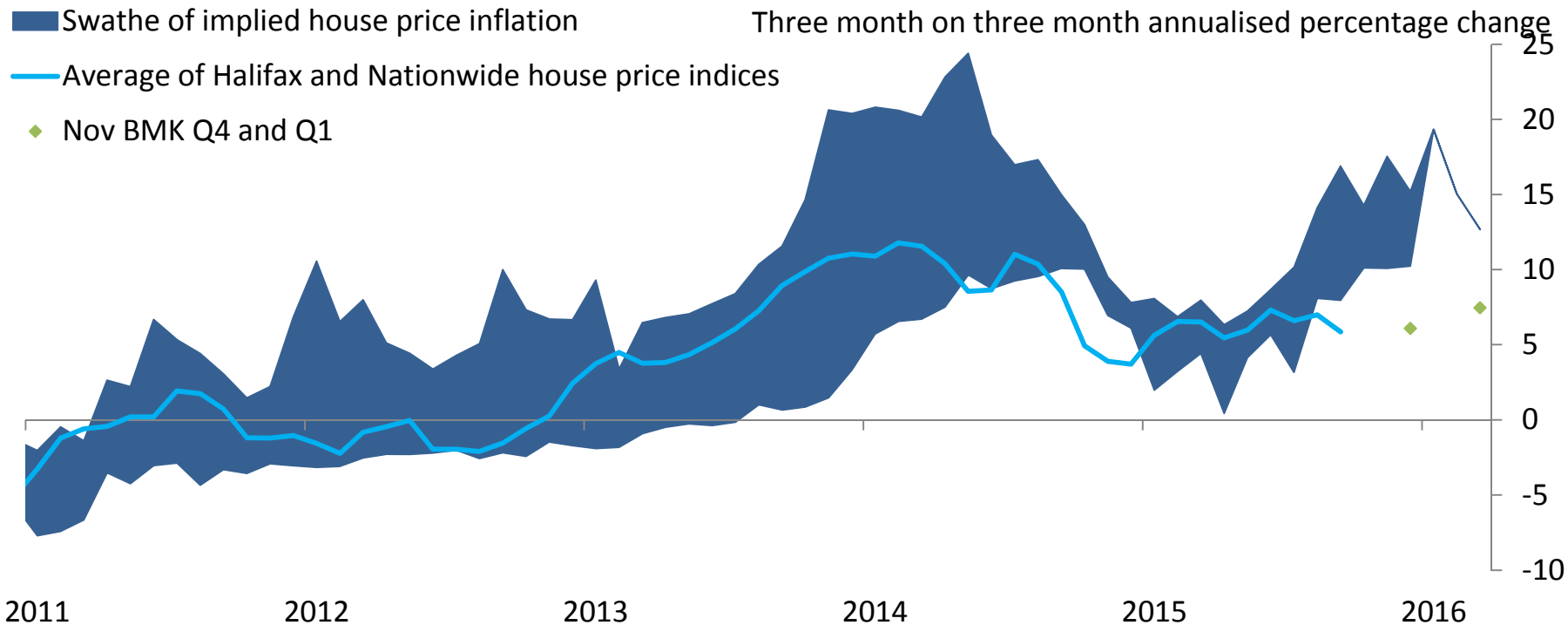
- Wholesale spreads have fallen a little over the month, but remain higher than before the summer
- Total funding costs have increased by less
- We do not think Budget bank tax changes affect the effective lower bound

Agenda

- Bank funding
- **Housing market and household debt update**
- Corporate deleveraging – transatlantic divergence
- Inflation expectations

House prices fell a little in September

Measures and indicators of house price inflation

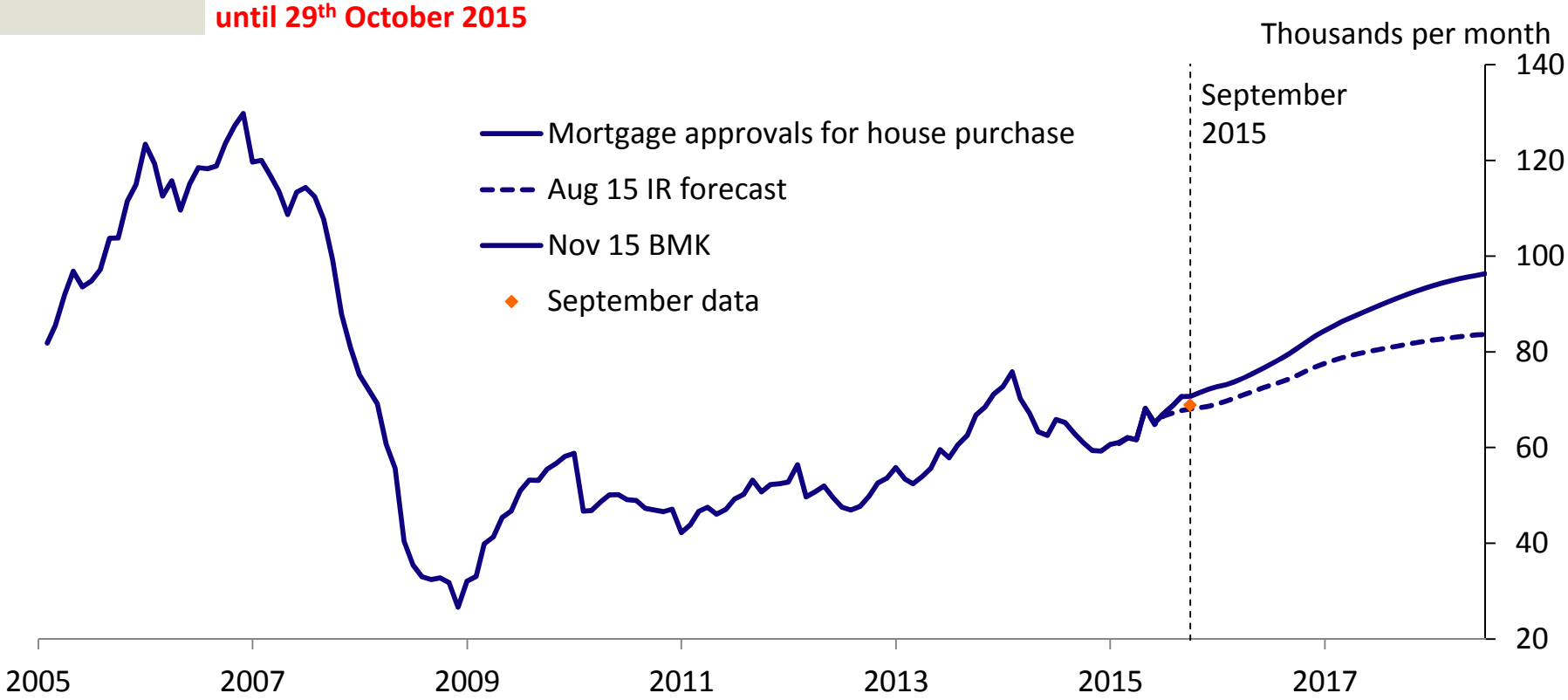


Swathe includes RICS new buyer enquiries less instructions to sell (lagged 6 months); RICS three month ahead price expectations (lagged 3 months); RICS sales to stock ratio (lagged 3 months); and a principal component of house prices.

Approvals in September were a little lower than expected

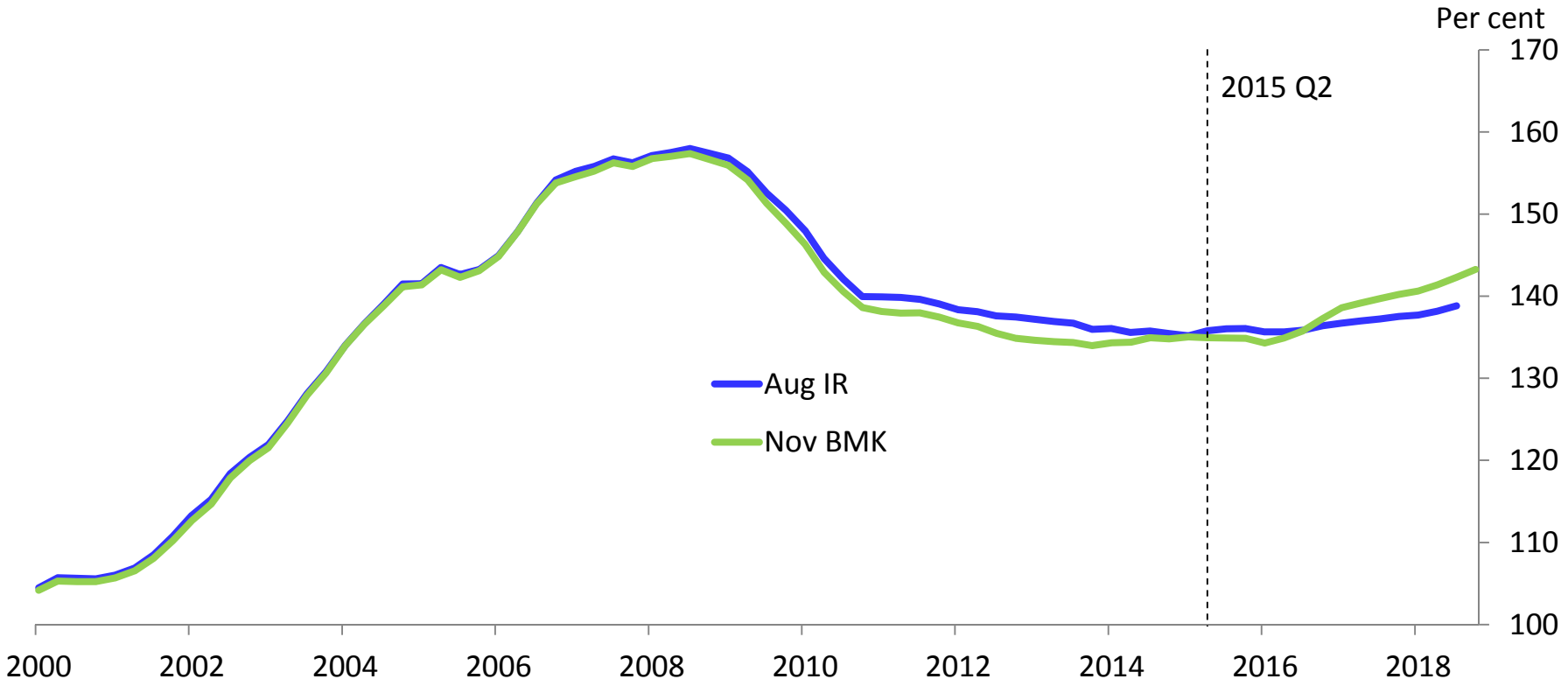
Approvals for house purchase

until 29th October 2015



Household debt-to-income projected to increase

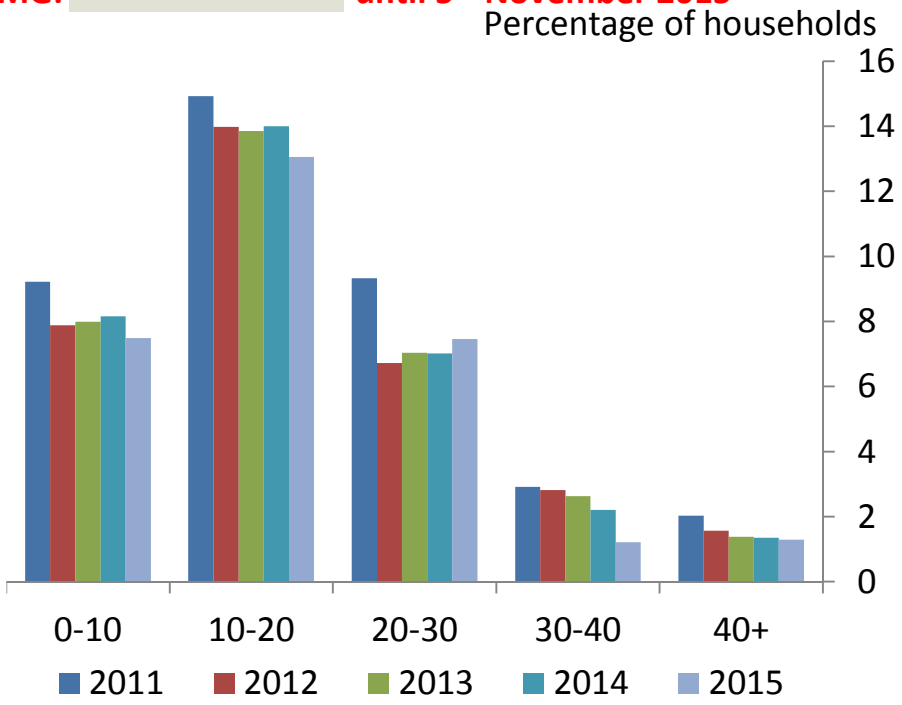
Household debt-to-income ratio



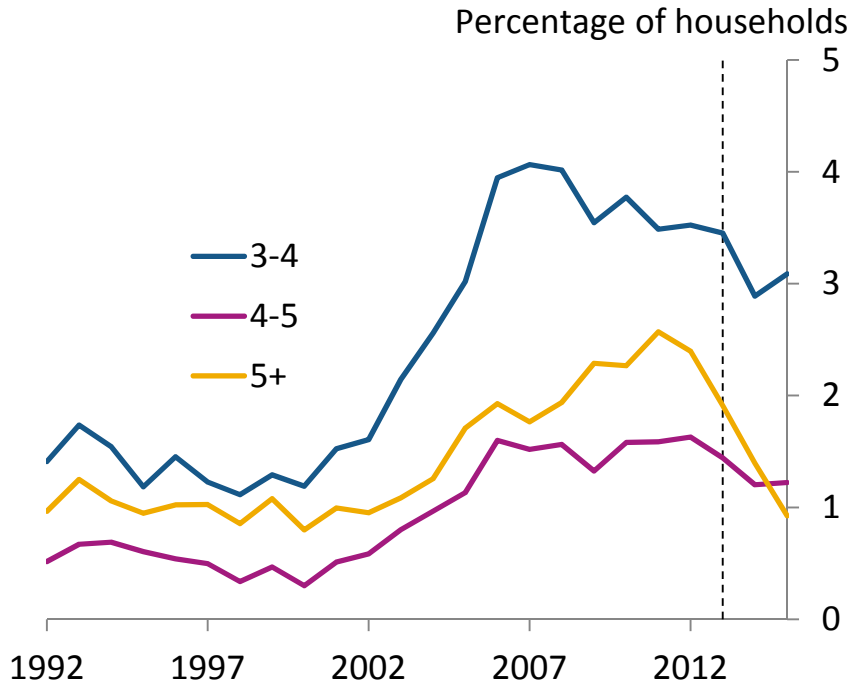
Distribution of debt may have improved a little

Distribution of mortgage debt service ratios (per cent), NMG

NMG: until 5th November 2015



Distribution of mortgage debt to income ratios*



*Data up to 2013 are based on responses to Living Costs and Food (LCF) survey. Data for 2014 and 2015 are based on responses to the NMG Consulting survey and have been spliced onto the earlier LCF survey data series.

Summary on household debt

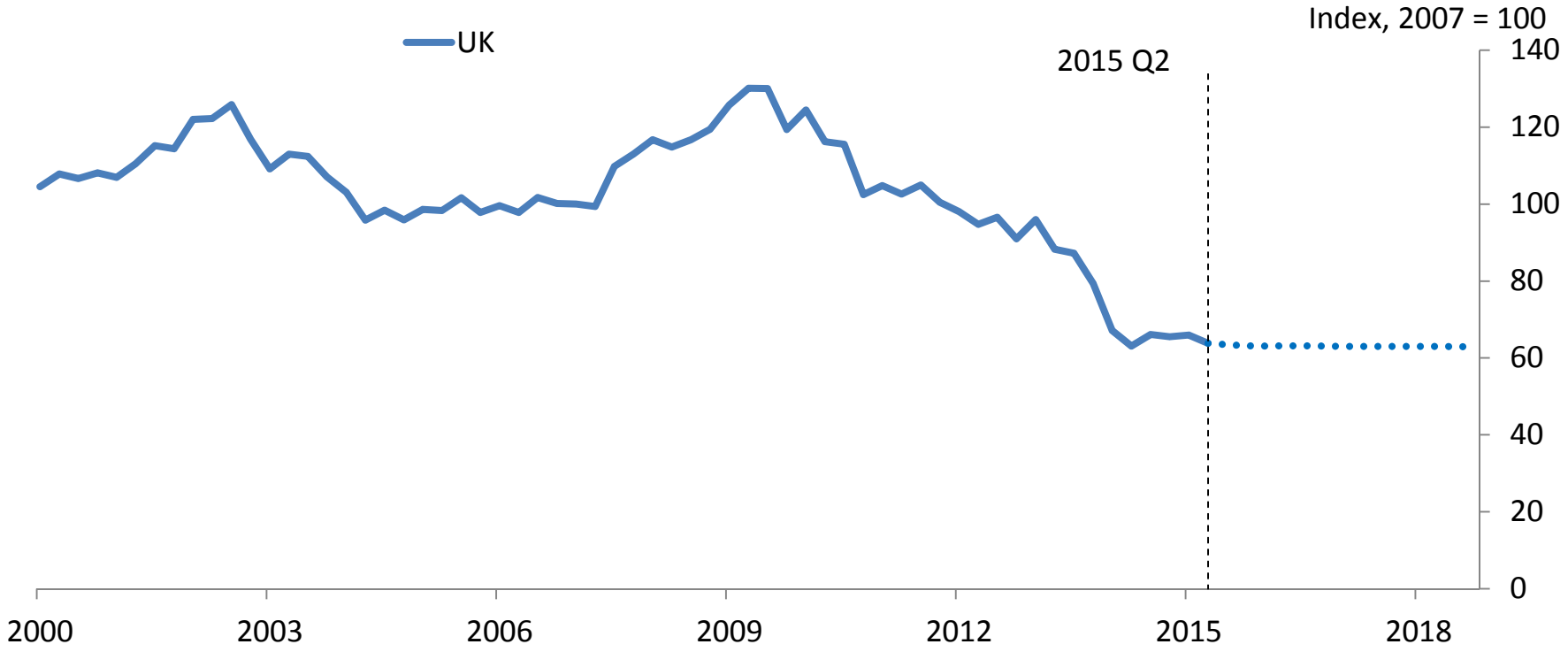
- There has been some small downside data news on the housing market over the month
- Household debt is projected to be higher over the next few years than in August, given lower lending rates
- Although the tail of vulnerable households appears to have shrunk slightly over the past year

Agenda

- Bank funding
- Housing market and household debt update
- **Corporate deleveraging – transatlantic divergence**
- Inflation expectations

UK PNFC net debt has fallen relative to nominal GDP

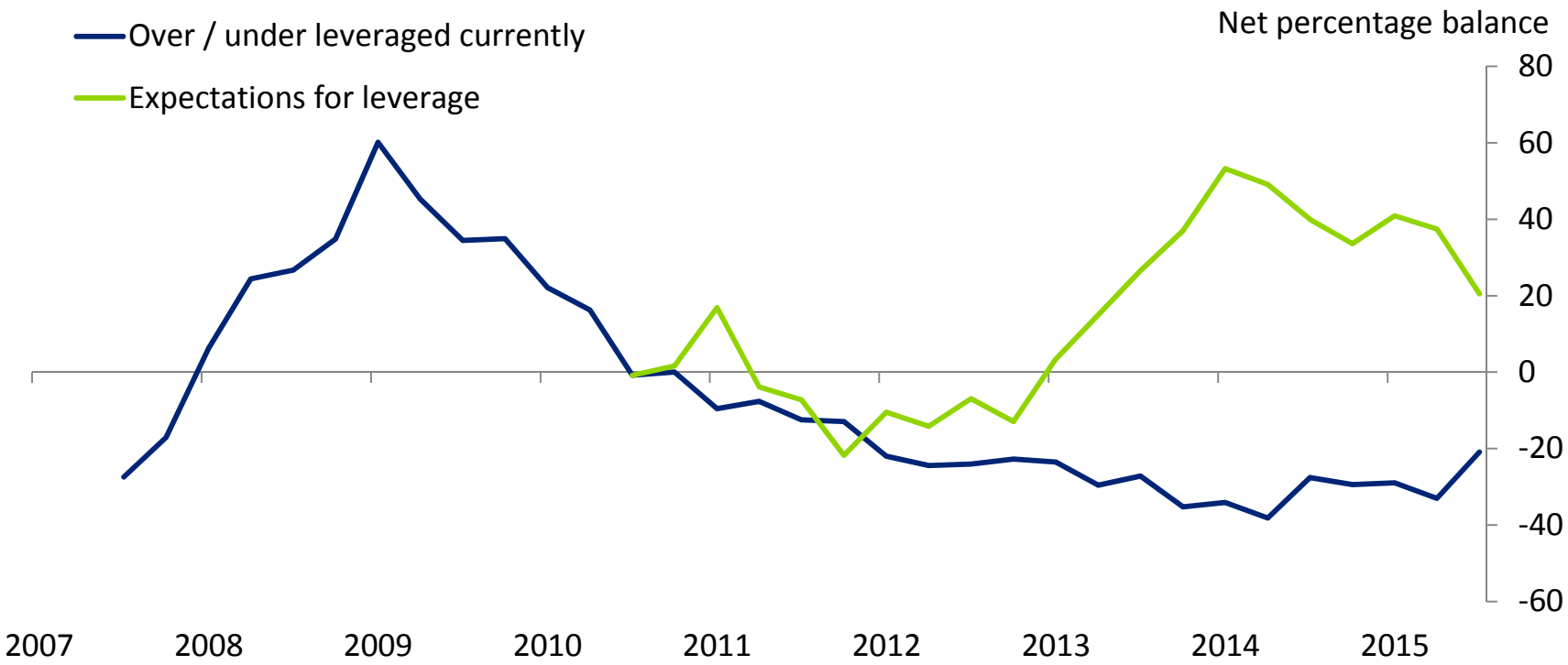
PNFC net debt / NGDP



- Dotted line represents the November 15 BMK forecast

Large firms report that they are underleveraged

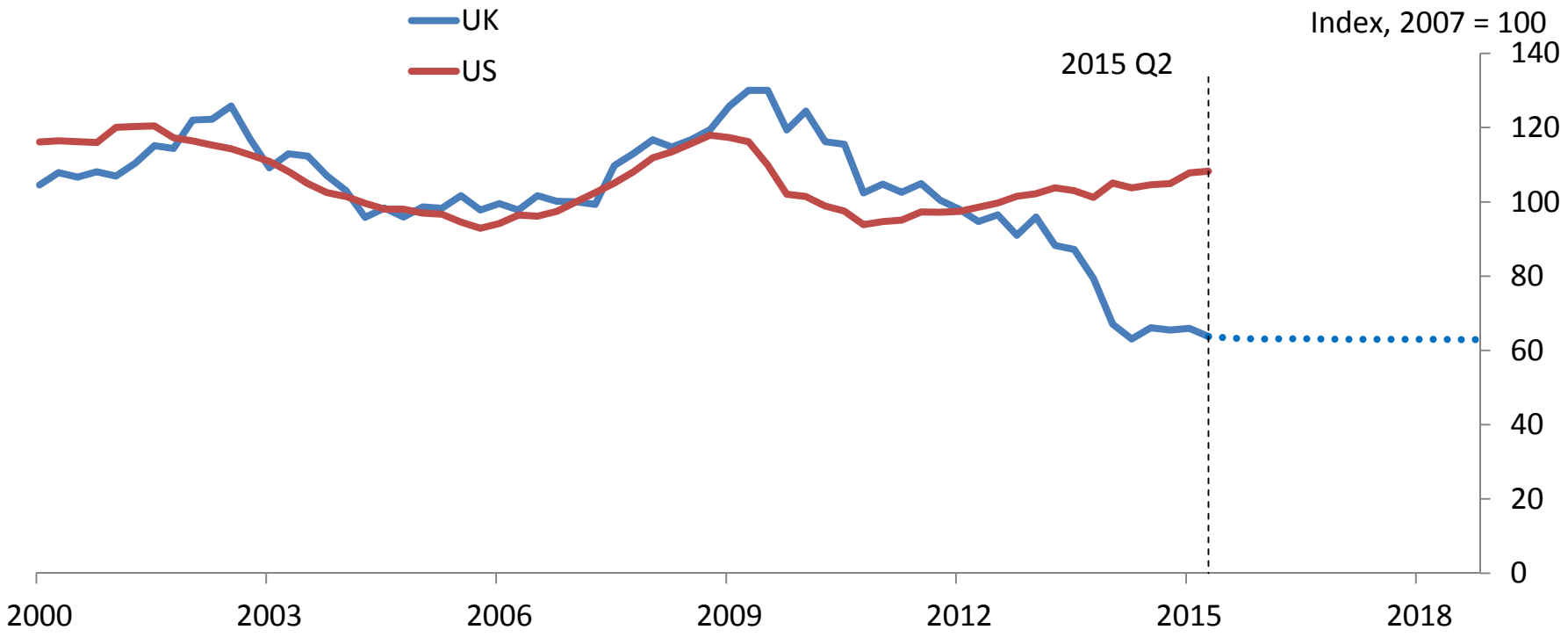
Deloitte CFO survey questions on leverage



A positive net percentage balance indicates that companies are overleveraged or expect to increase their leverage.

PNFC net debt has risen gradually in the US

PNFC net debt / NGDP

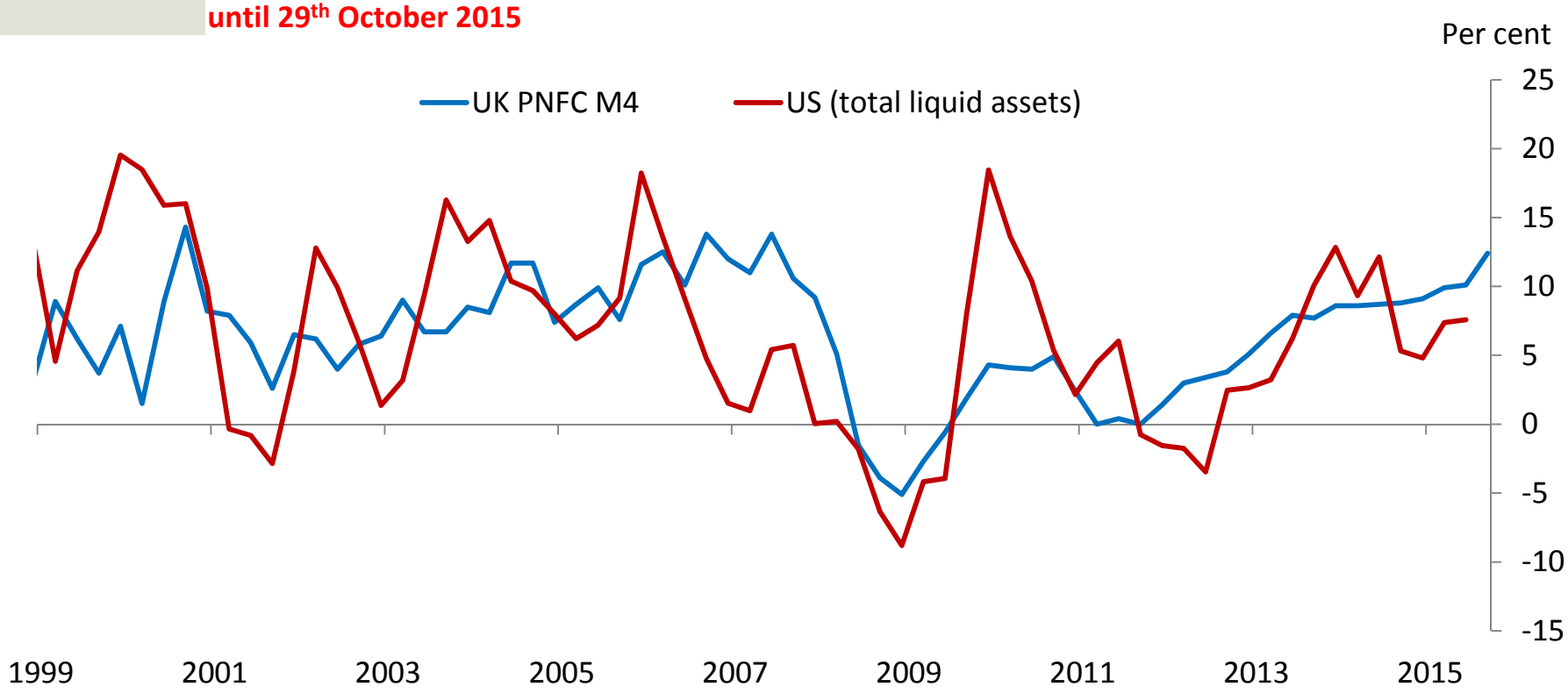


- Dotted line represents the November 15 BMK forecast

The divergence doesn't reflect differences in deposit growth

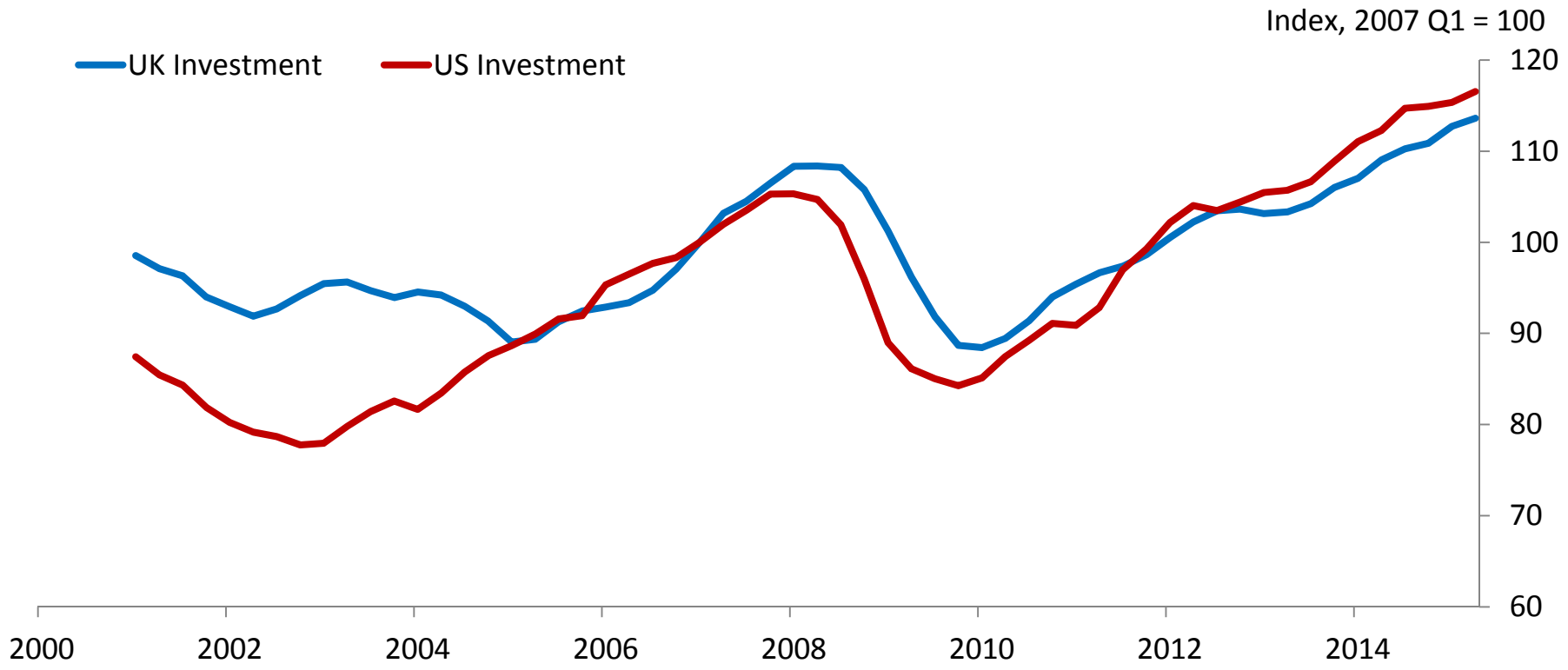
Annual PNFC liquid asset growth

until 29th October 2015



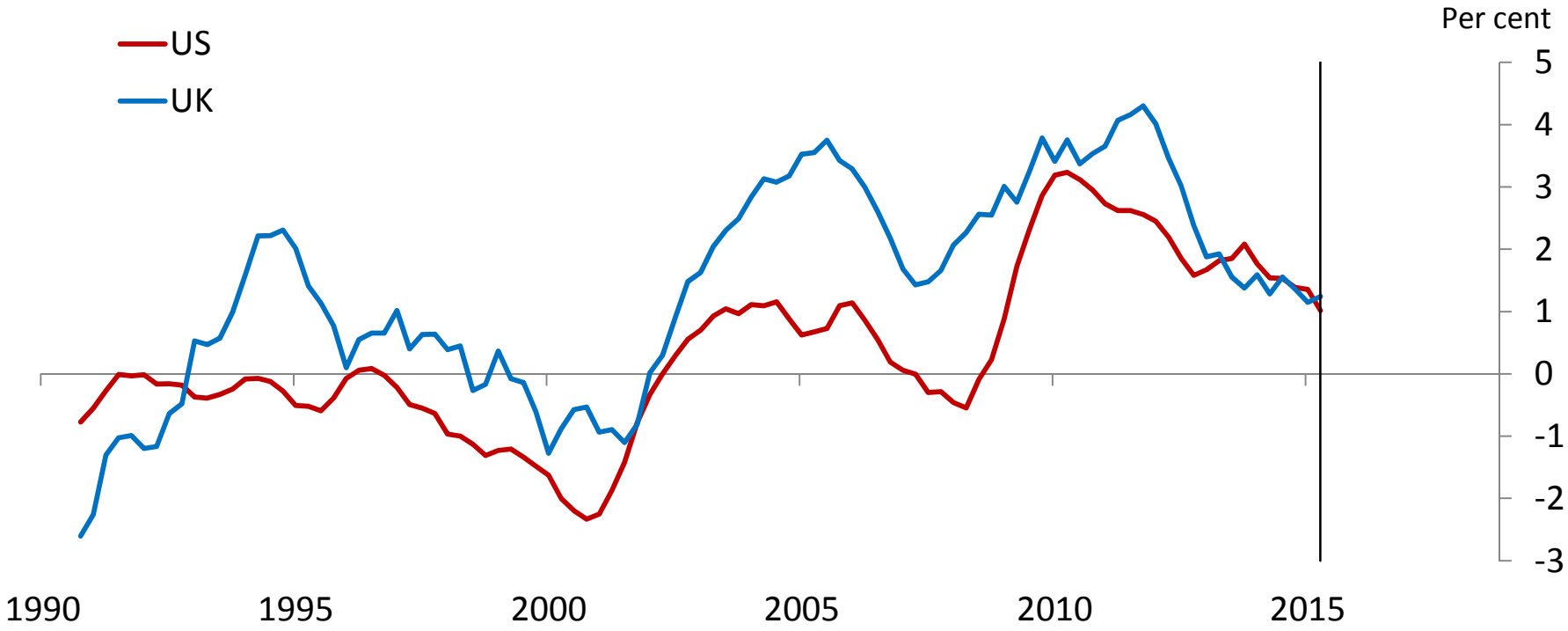
Stronger US investment can explain only a little

Nominal business investment



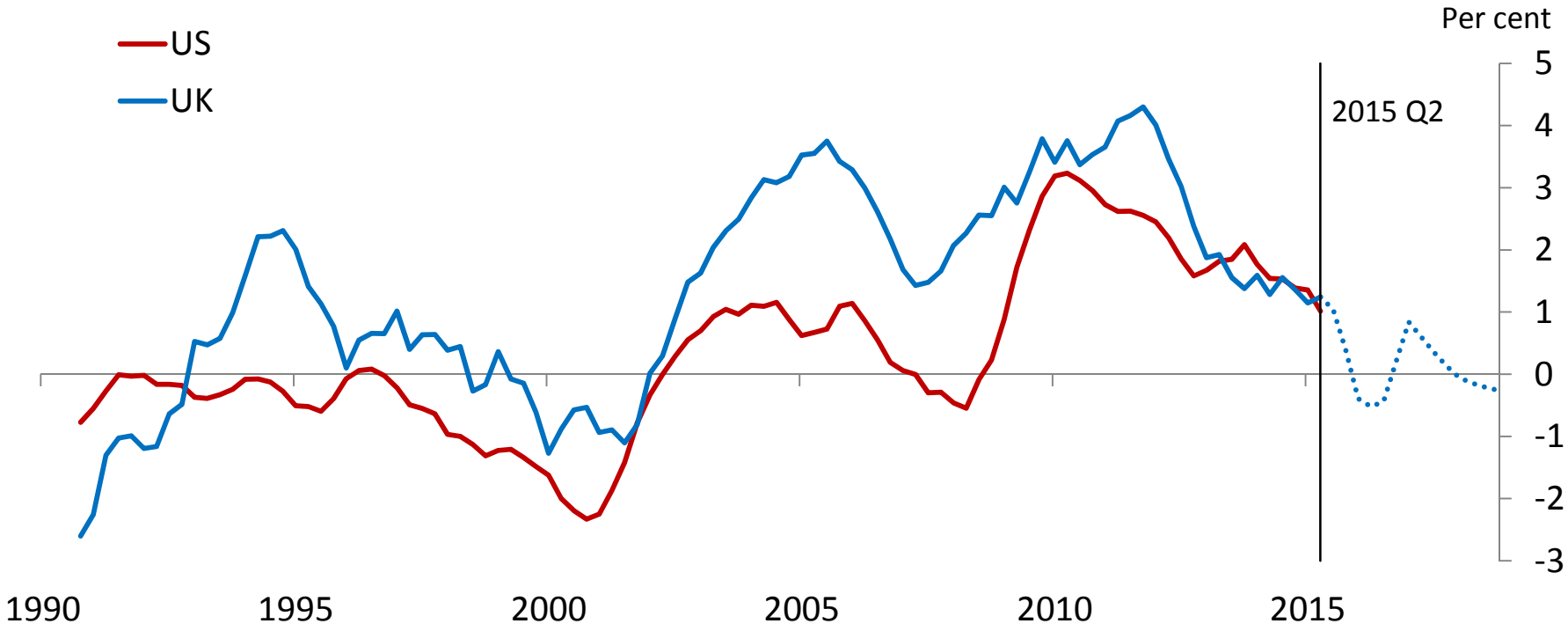
PNFC financial surpluses are currently similar

PNFC financial balance as percentage of GDP, 4Q moving average



UK PNFC financial surplus generally projected to continue

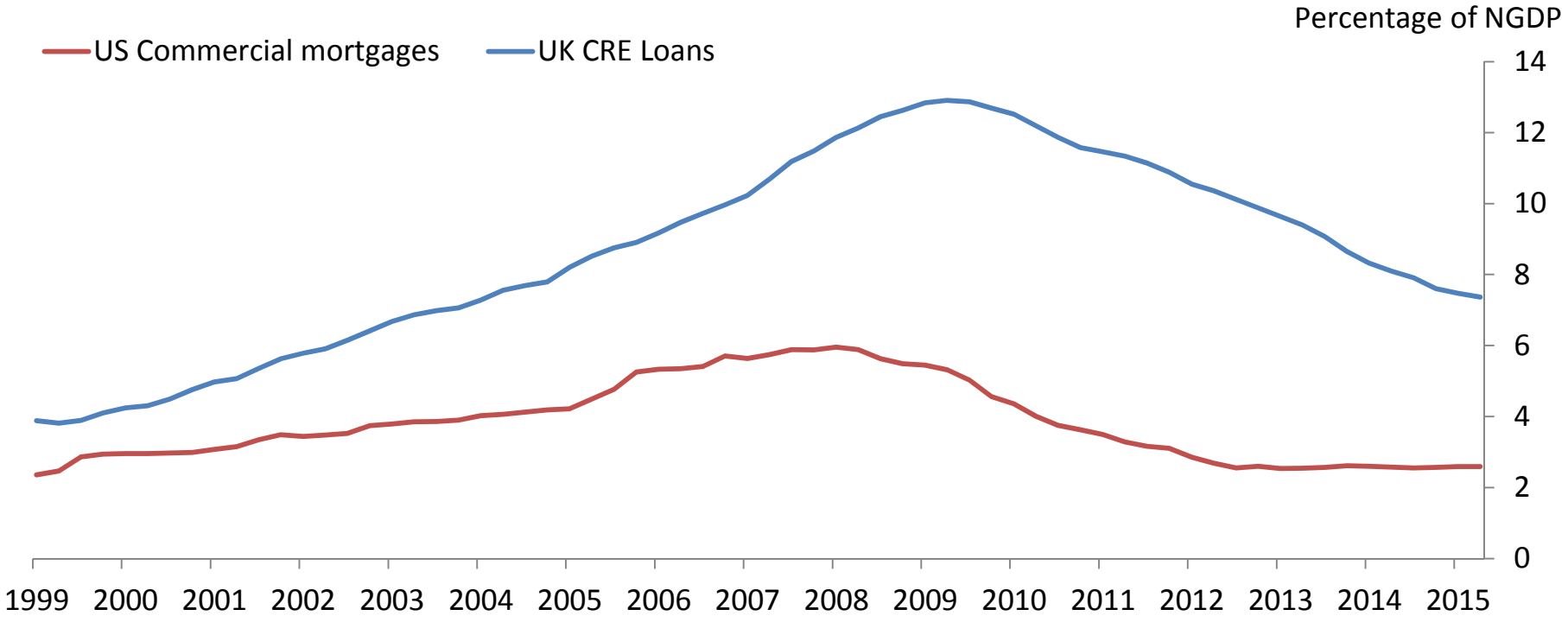
PNFC financial balance as percentage of GDP, 4Q moving average



- Dotted line represents the November 15 BMK forecast

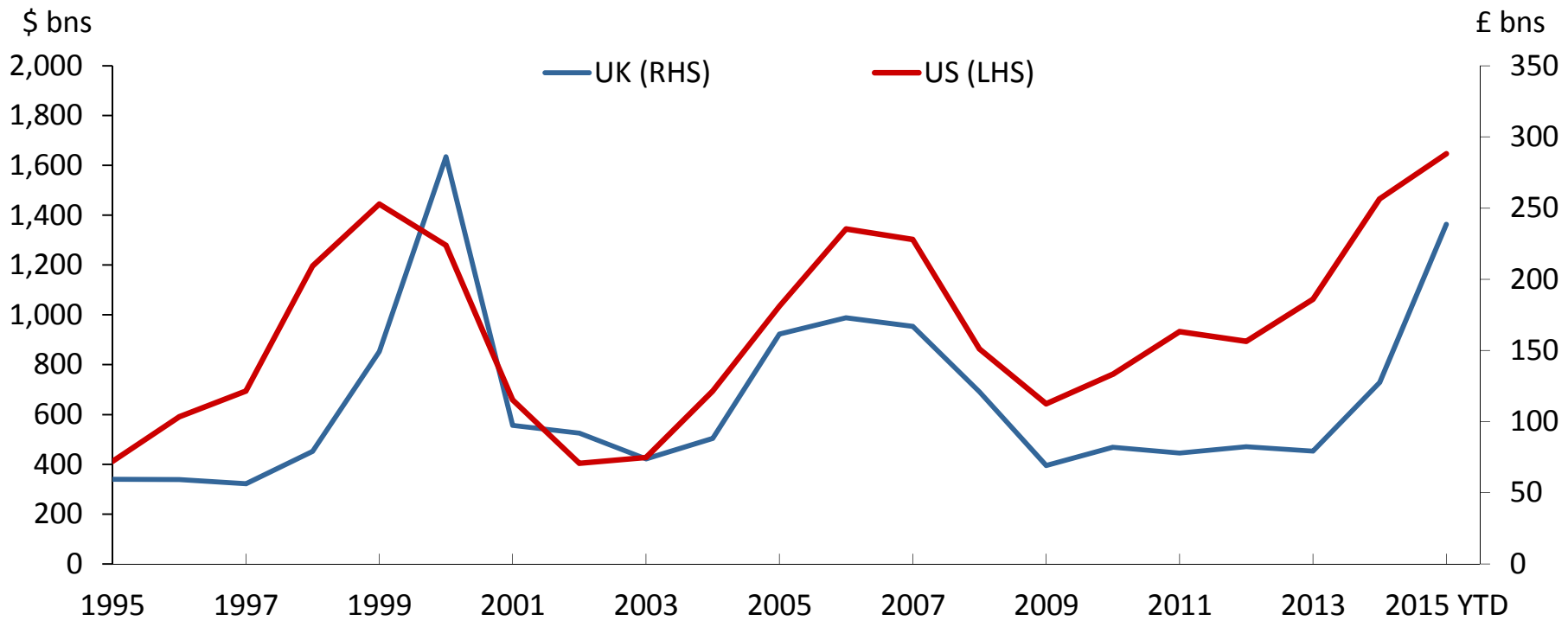
CRE lending has continued to decline in the UK

Lending to real estate, as percentage of NGDP



- UK data are break-adjusted, but include the effect of write-offs

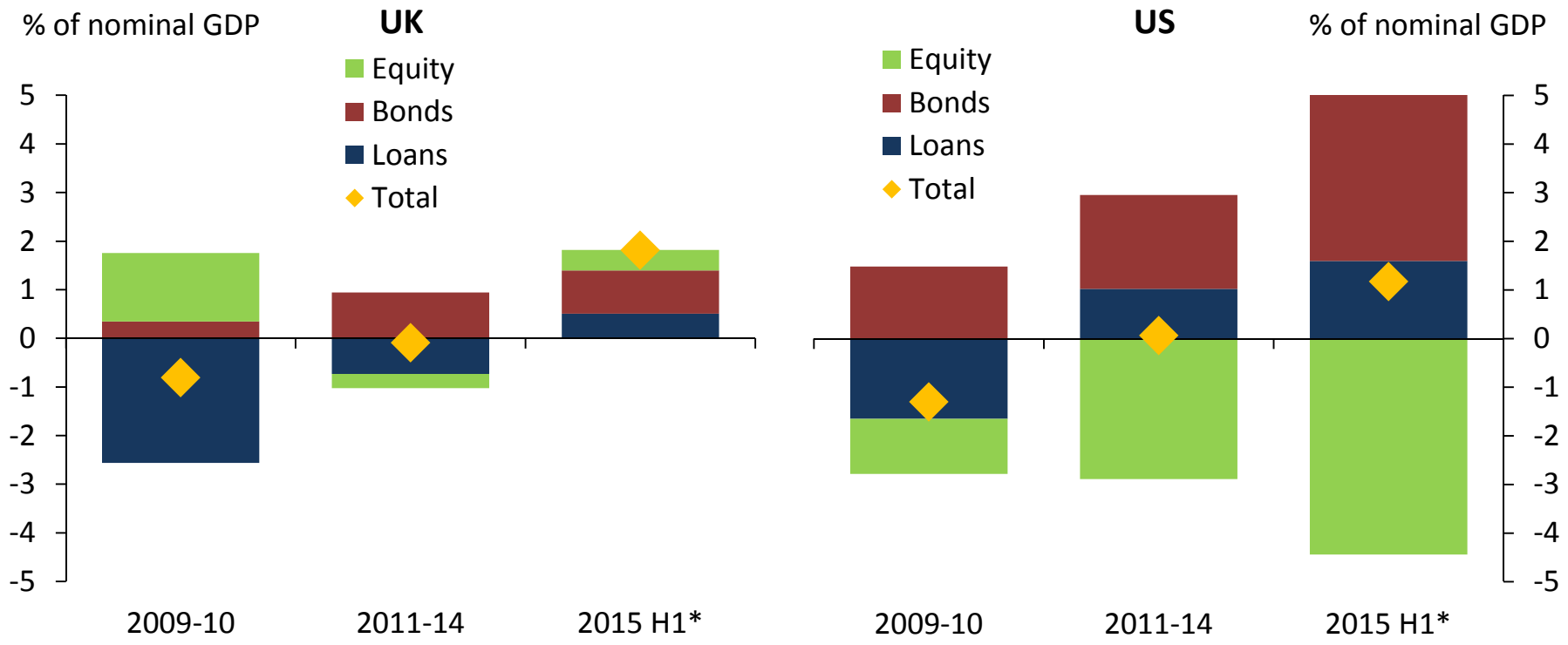
M&A has been stronger in the US until recently



- See 'UK corporate risk assessment 2015 H2' for more on recent M&A deals

Rising US debt partly offset by falling net equity

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



*2015 data scaled to be comparable to annual figures

Hypotheses for the difference between the UK and US

Hypothesis	Summary	Outlook for UK
Business cycle	Investment a little weaker in the UK; financial surpluses similar	UK investment expected to rise; financial balance declines
Credit conditions	Credit conditions similar	Credit conditions not expected to change much
CRE	Has been more of a drag in UK	Some more deleveraging likely in near term
M&A	UK activity slower to pick up, but has recently risen, although not excessively debt-financed	Pickup in UK may persist
Other	Tax incentives boost US companies' demand for debt	Unlikely to change

Summary on corporate debt

- We project net debt to grow broadly in line with nominal GDP over the forecast period
- The risks to that profile are probably weighted to the upside

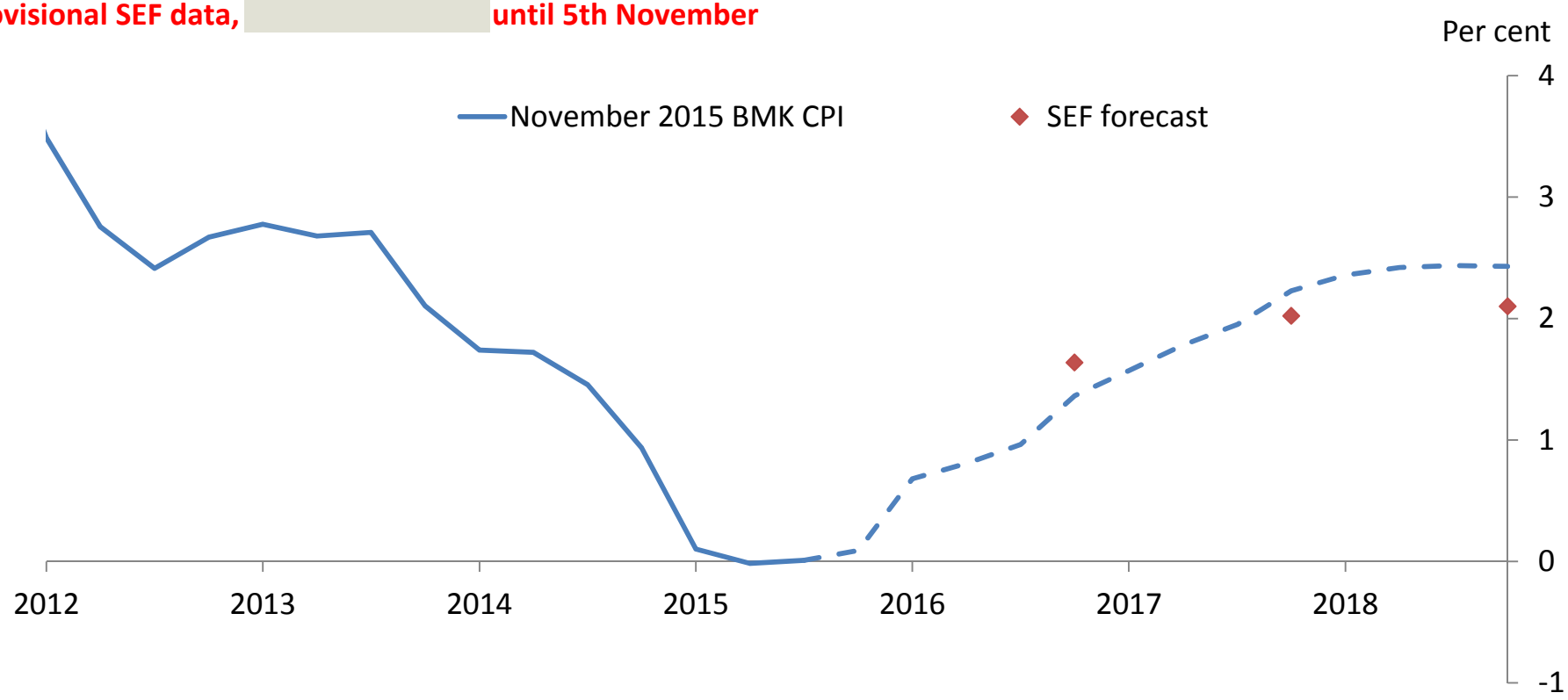
Agenda

- Bank funding
- Housing market and household debt update
- Corporate deleveraging – transatlantic divergence
- **Inflation expectations**

Professional forecasters have lower inflation expectations than Benchmark further out

November 2015 BMK inflation forecast and Survey of External Forecasters' average projection

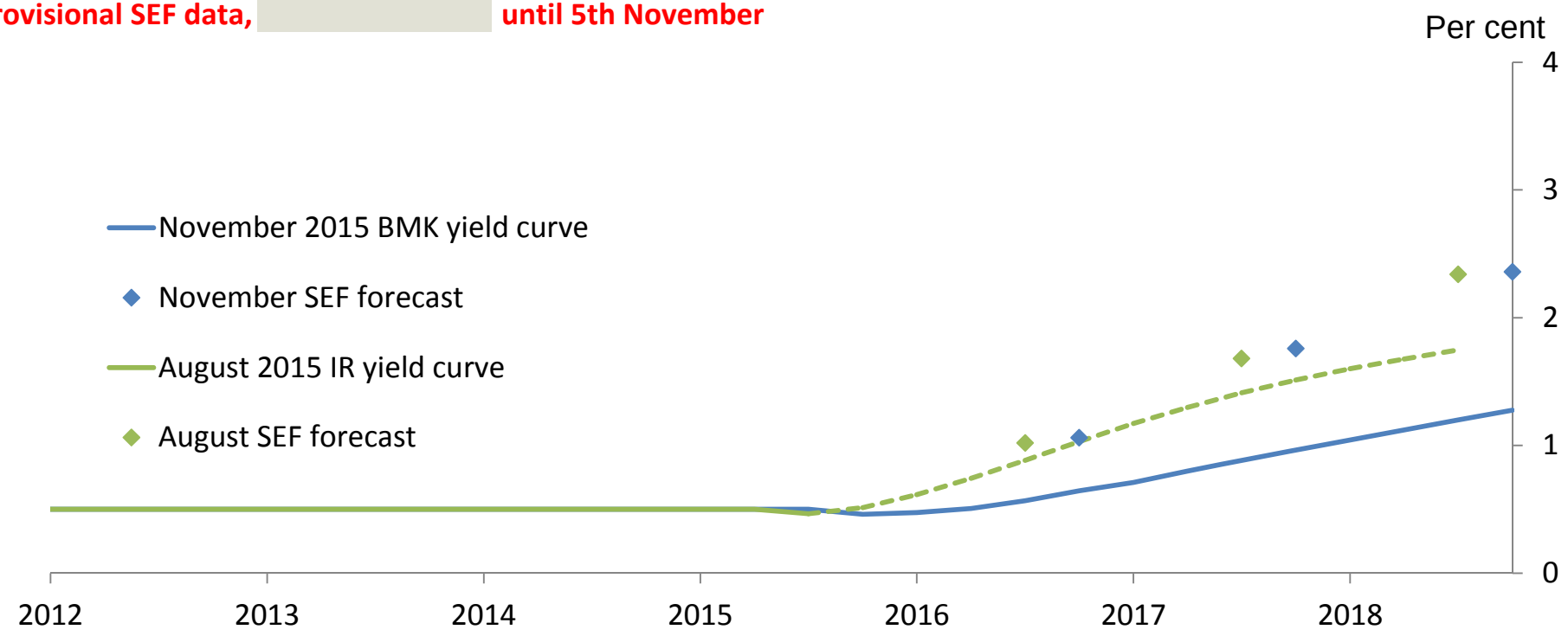
Provisional SEF data, until 5th November



Potentially driven by higher expectations for Bank Rate

Profiles for Bank Rate: market yield curves and Survey of External Forecasters' average projection

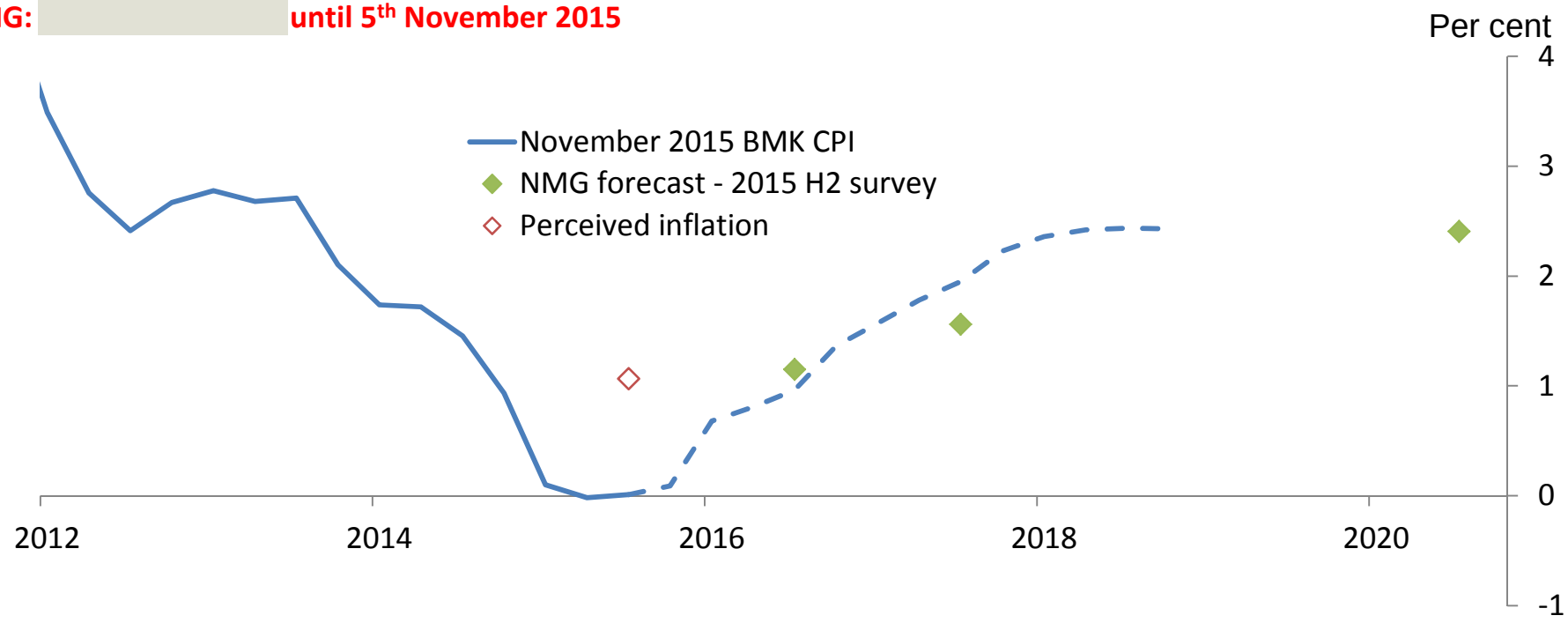
Provisional SEF data, until 5th November



Households expect inflation to get back to target more slowly

NMG 2015 H2 survey median inflation expectations and November 2015 BMK forecast

NMG: until 5th November 2015

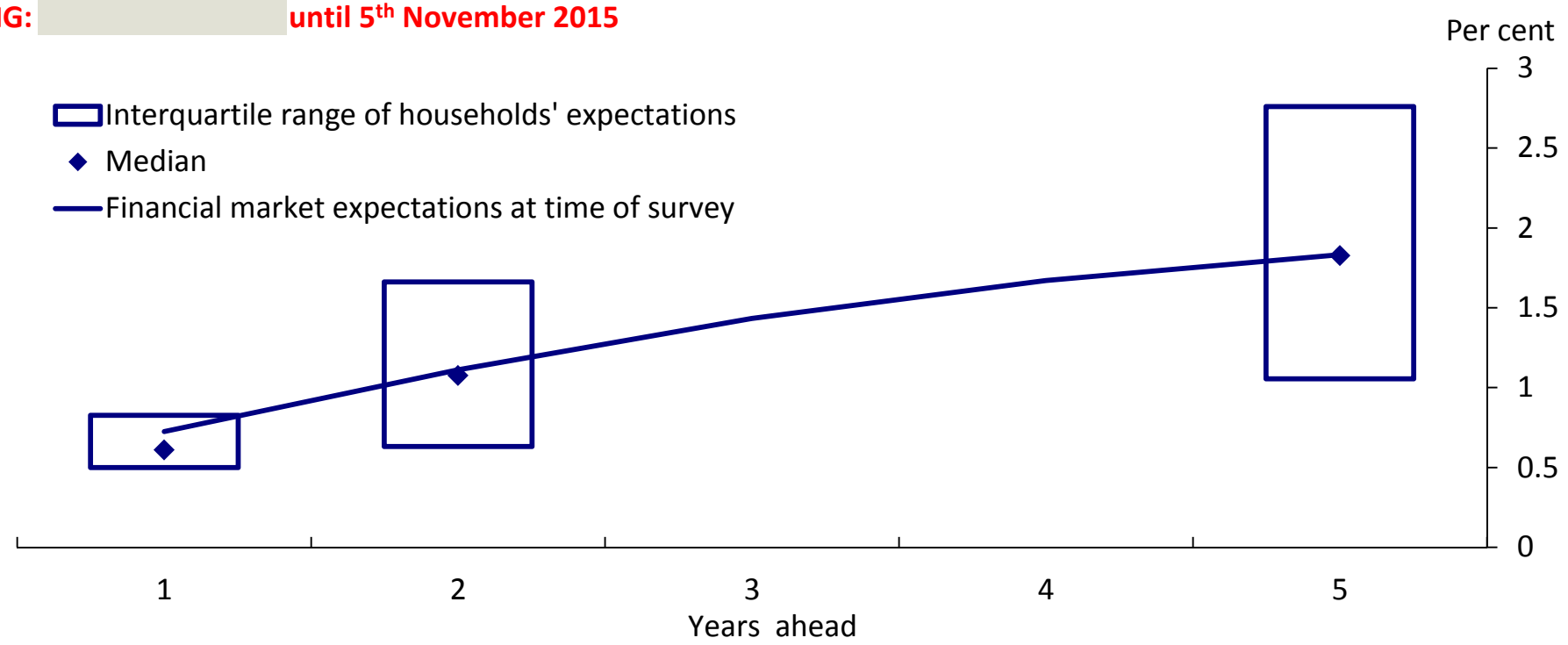


NMG Questions: Perceptions: Which of these options best describes how prices have changed over the last twelve months? Expectations: By how much would you expect prices in the shops generally to change over the next twelve months/12 months after that/over a year in the longer term, say five years time?

Households' Bank Rate expectations in line with yield curve

Median Bank Rate expectations in NMG survey and financial market expectations at time of the survey*

NMG: until 5th November 2015



*Survey conducted between 2nd and 22nd September 2015

NMG Question: The level of interest rates set by the Bank of England (Bank Rate) is currently 0.5%. At what level do you expect that interest rate to be in each of the following time periods? One/Two/Five year(s) from now

Summary on inflation expectations

- Professional forecasters' inflation expectations are below the November Benchmark, although they expect Bank Rate to rise faster than the yield curve

- Households continue to expect inflation to return to target more slowly, while their expectations for Bank Rate are similar to the market profile

Summary

- Although bank funding spreads are higher than in early 2015, overall funding conditions are relatively favorable
- Household debt to income is projected to pick up, although the distribution may have improved a little
- We expect companies' leverage to be broadly flat, although there is a risk it picks up, as it has in the US
- Households continue to expect inflation to return to target more slowly

4: Demand and Output

Demand and Output

November 2015

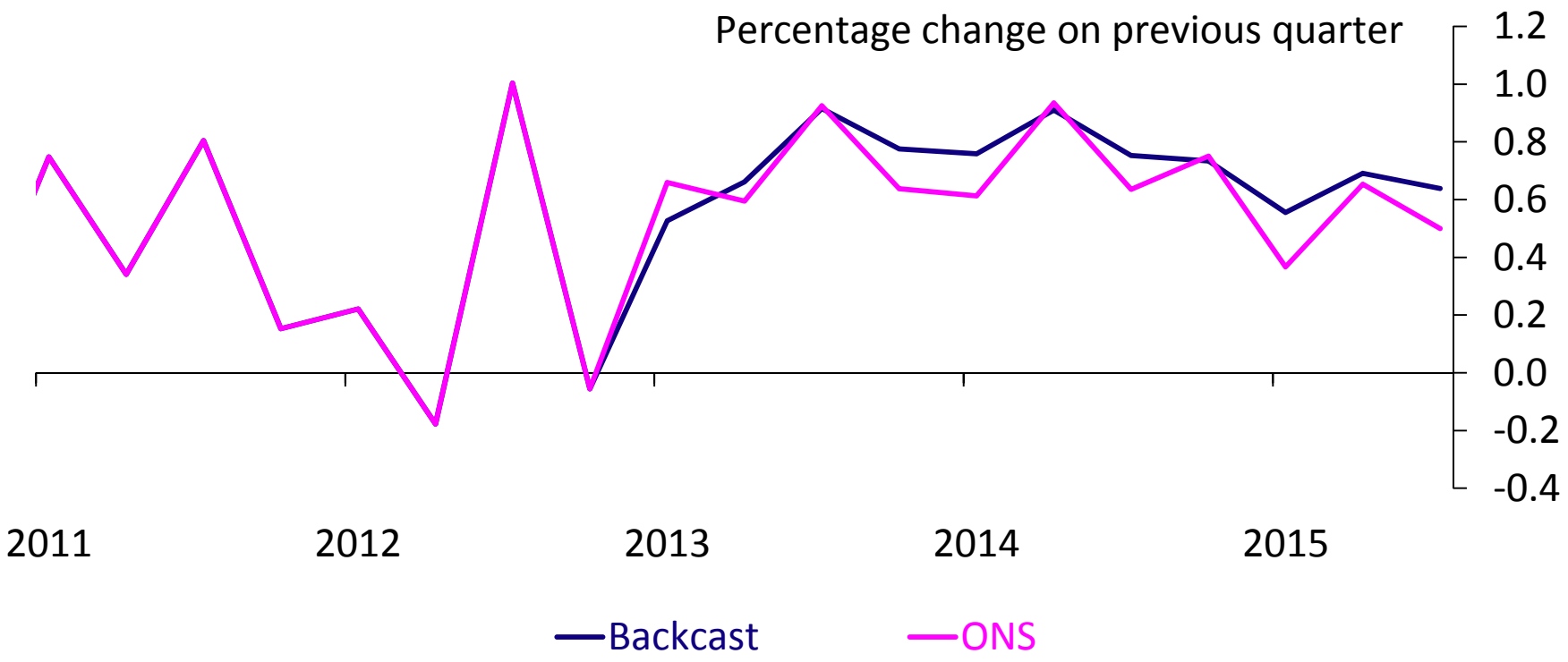
DSI and UK Teams

Outline

1) What is the short-term growth outlook?

2) Update on issues with the trade data

Real GDP growth



- GDP grew by 0.5% in Q3, which we expect to be revised up to 0.6%

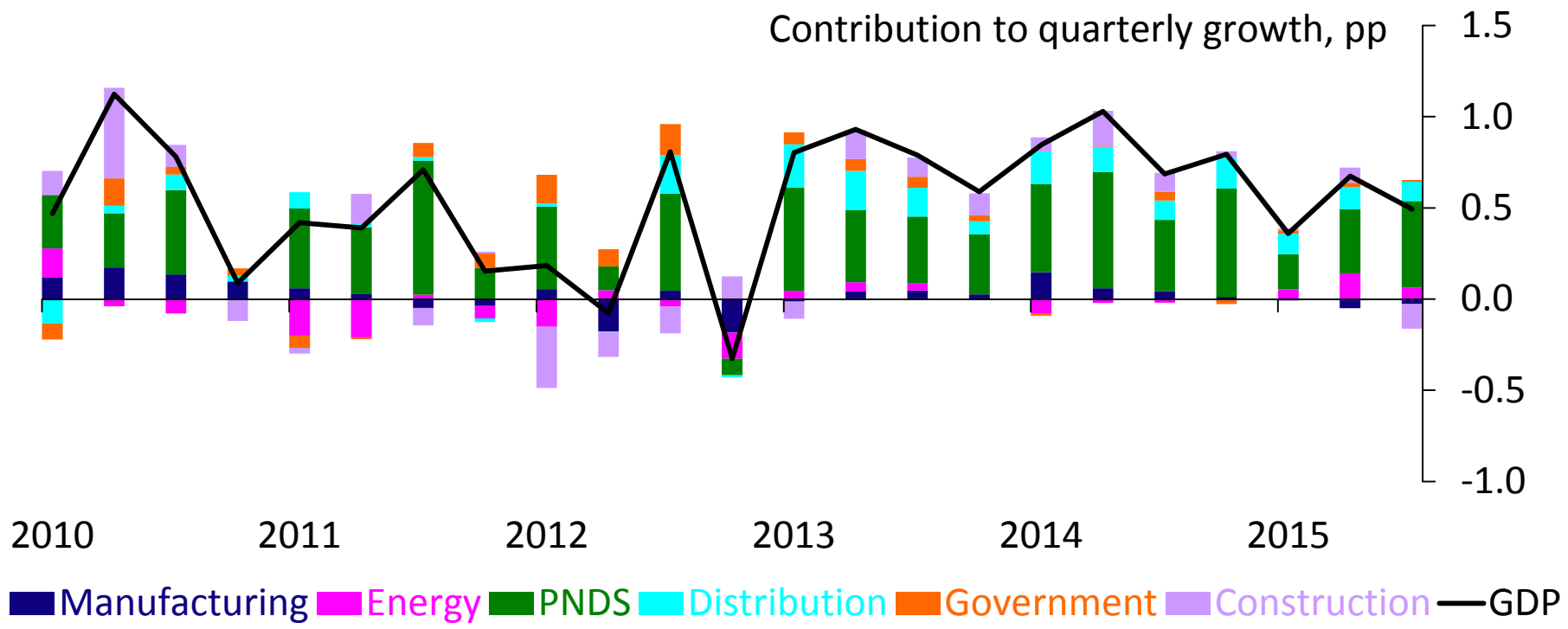
Q3 preliminary GDP estimate

	Expectation for Prelim+	ONS Prelim	Contribution to GDP error (pp)
Services	0.7	0.7	0.0
PNDS	0.9	1.0	0.0
Distribution	1.0	0.9	0.0
Government	-0.1	0.0	0.0
Production	-0.1	0.3	0.1
Manufacturing	-0.6	-0.3	0.0
Energy	1.3	1.5	0.0
Construction	-1.4	-2.2	0.0
GDP	**0.5**	**0.5**	**0.0**

* Contributions do not sum due to rounding

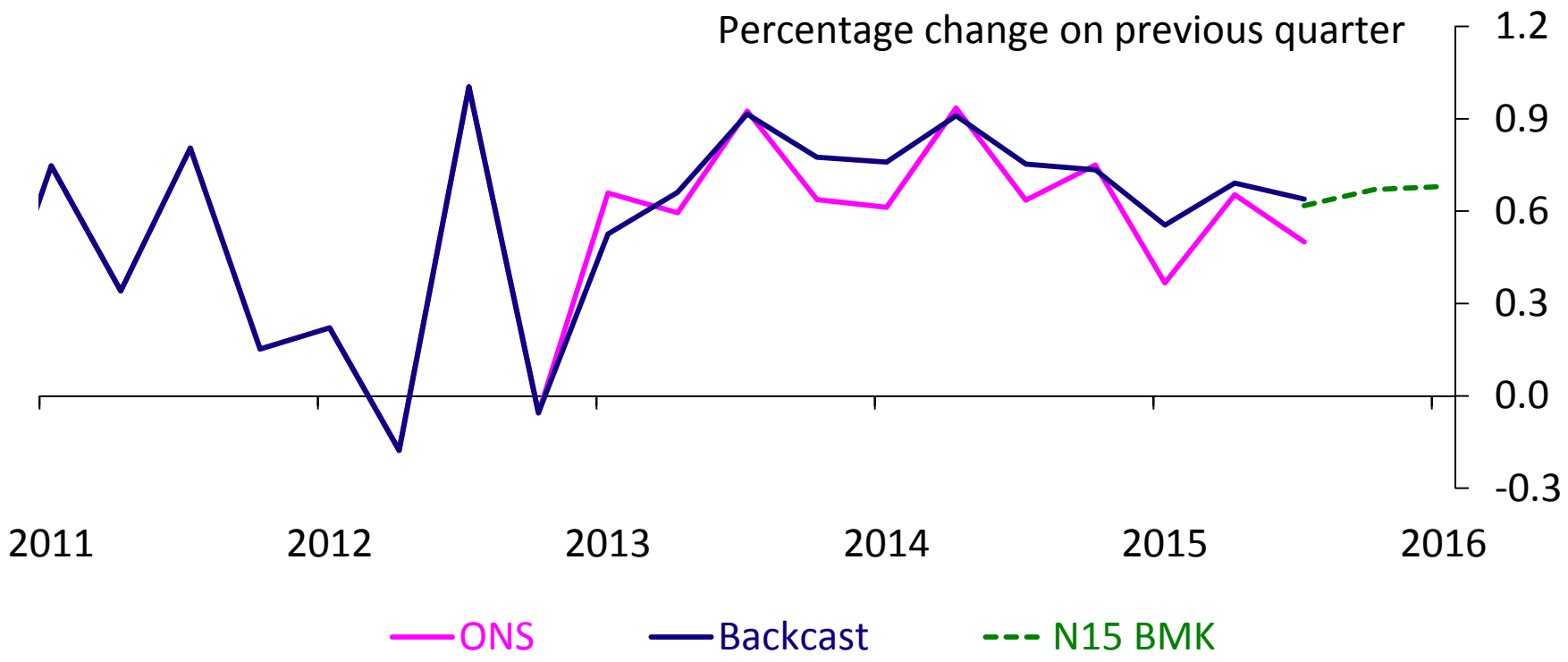
+ Expectations immediately before preliminary release

Quarterly GDP growth



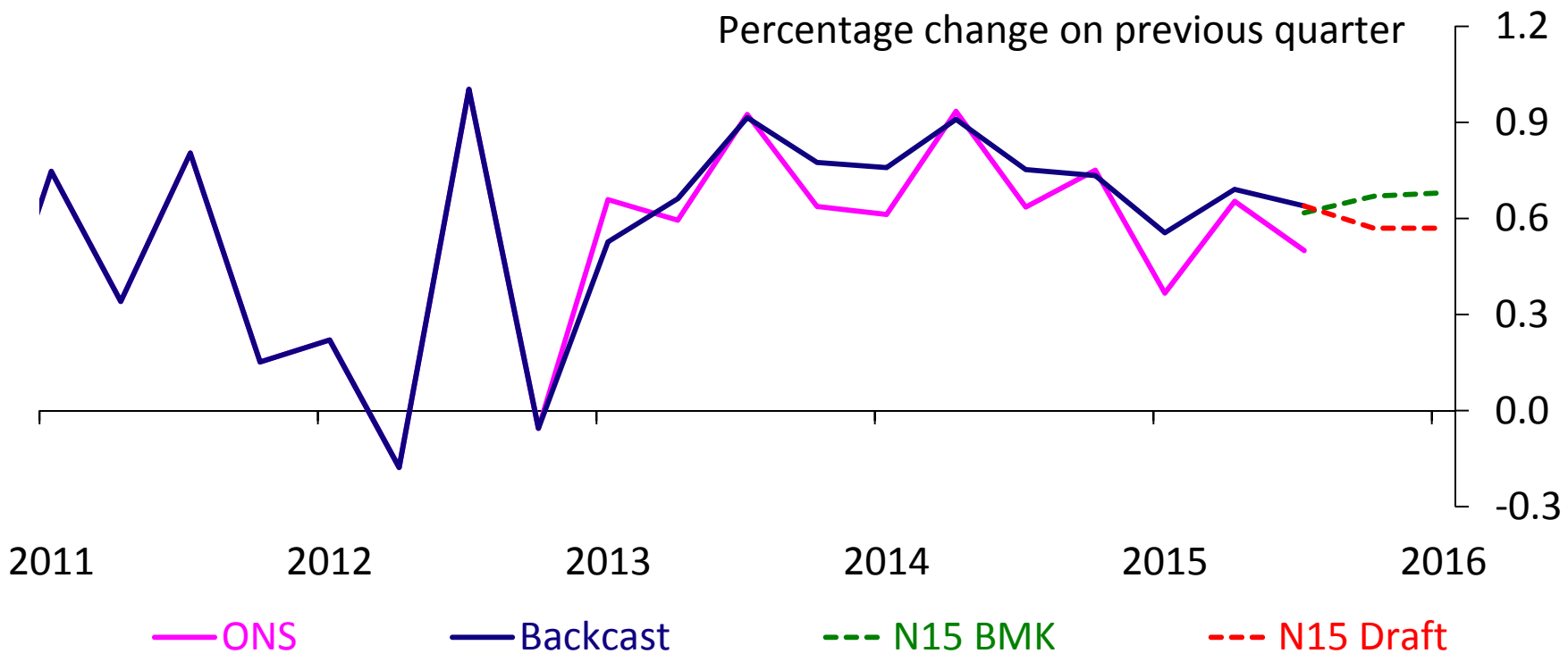
- Construction accounts for all of the 0.2pp slowdown between Q2 and Q3

Nowcast summary



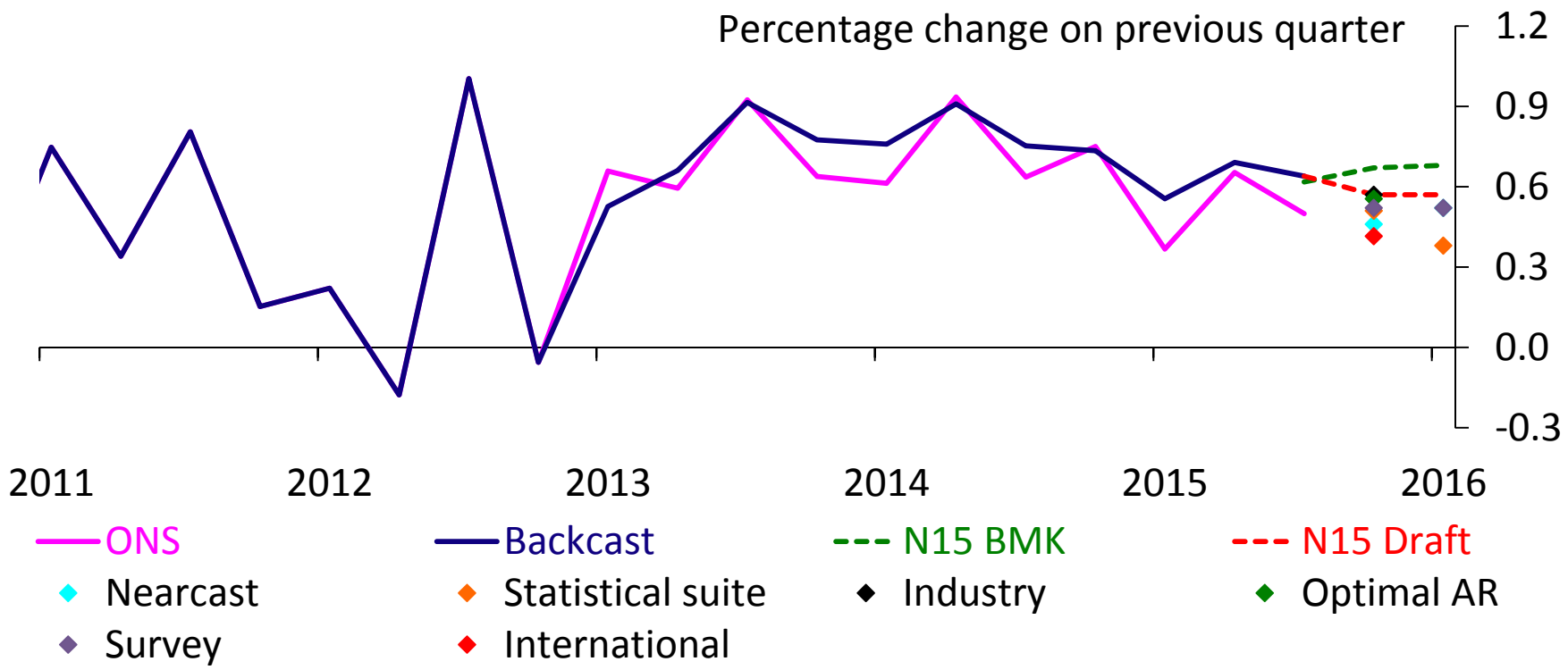
- Growth picked up from 0.6% in Q3 to 0.7% over the rest of the N15 BMK forecast

Nowcast summary



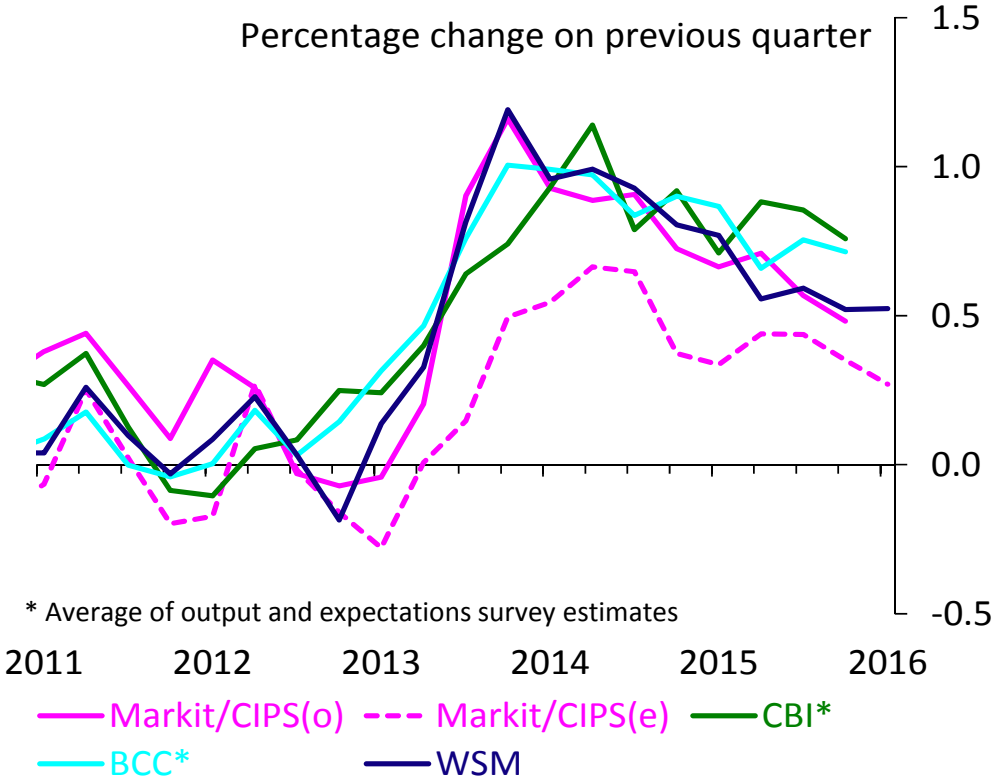
- Near-term growth in Q4 and Q1 has been lowered in the N15 Draft forecast to 0.6%

Nowcast summary



- Nowcast models suggest weaker growth than the N15 BMK forecast

Weighted Survey Model (WSM)



Correlation with latest GDP estimates

	Markit/CIPS^	CBI	BCC
Output composite*	0.72	0.71	0.58
Expectations composite* (t-1)	0.71	0.56	0.63

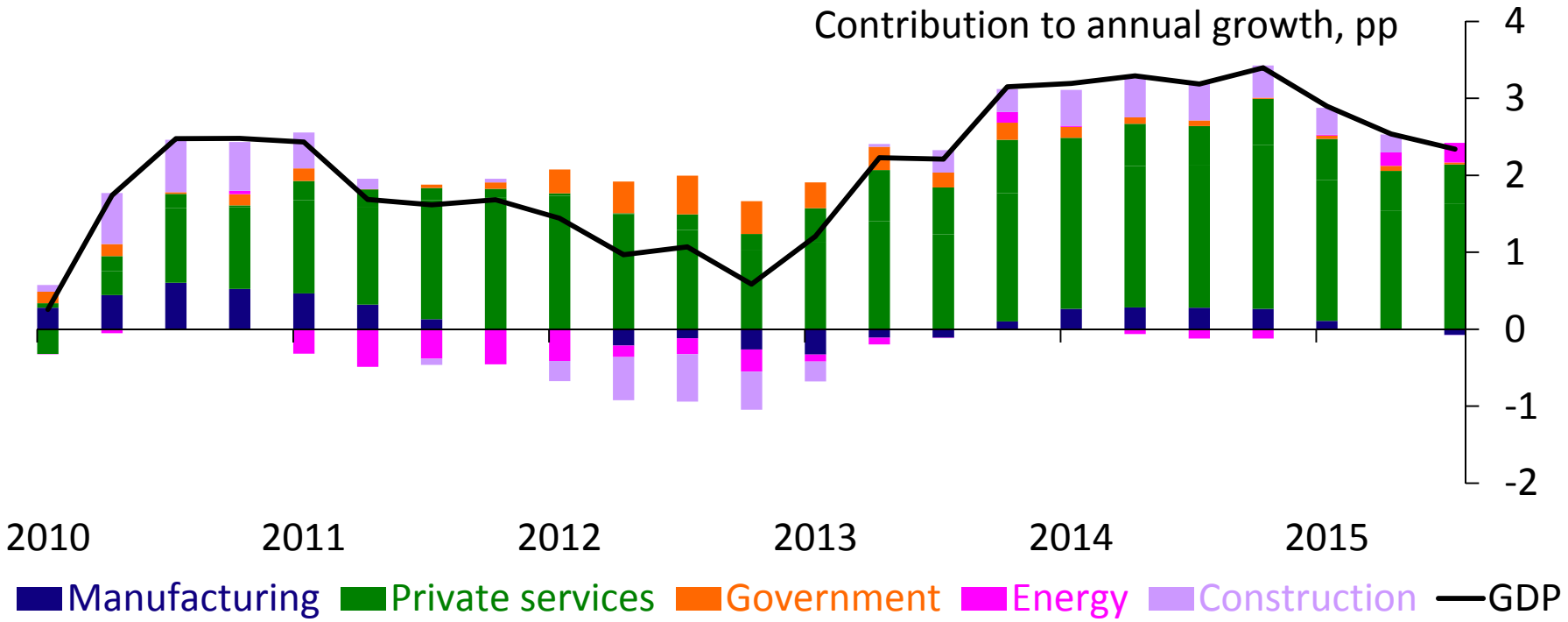
^Quarterly average

*Composites are the weighted industry sector surveys

Sample period is 1999Q1 to 2015Q3

- Markit/CIPS data have the highest correlations with latest GDP growth

GDP growth industry split



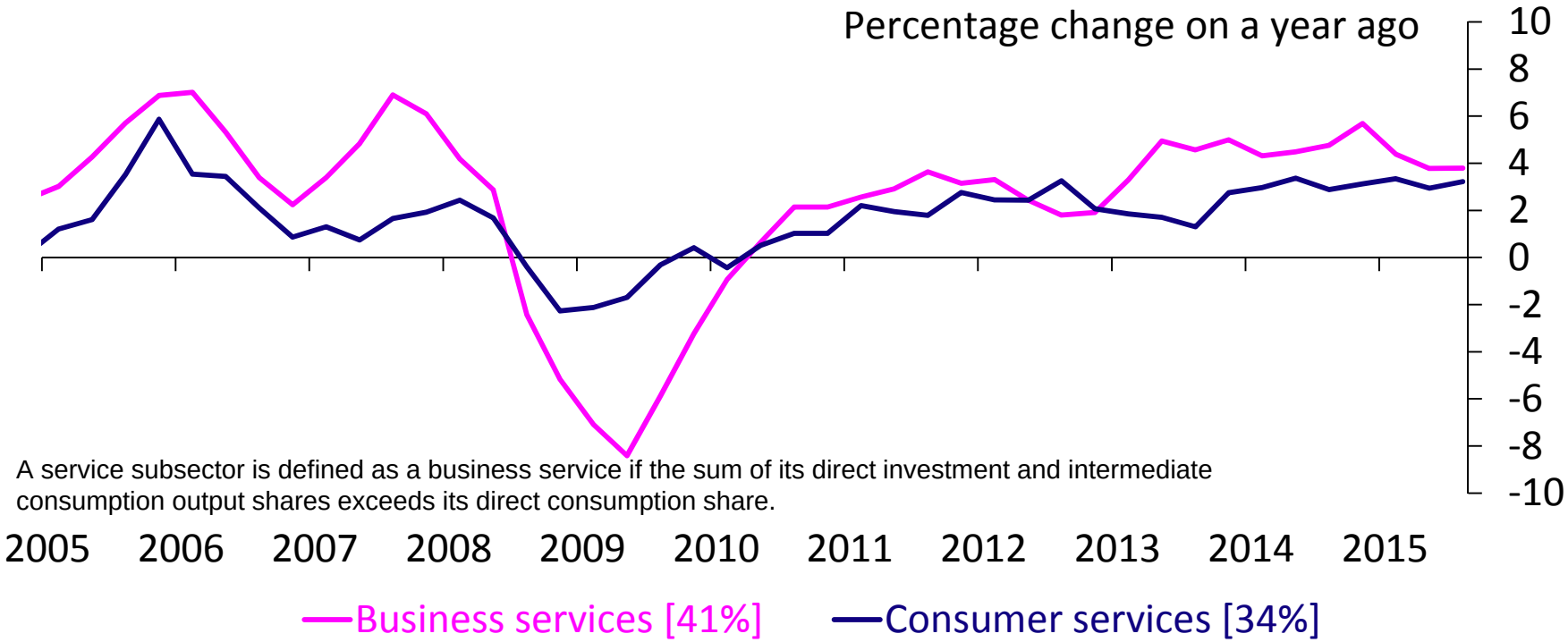
- Slowdown in 4-quarter GDP growth has been broad based

What does the industry mix tell us?

Feature of narrative	Evidence*
Strong domestic demand	
Negative external influences	
Nets to solid GDP growth	

* Green indicates supportive evidence, red the reverse

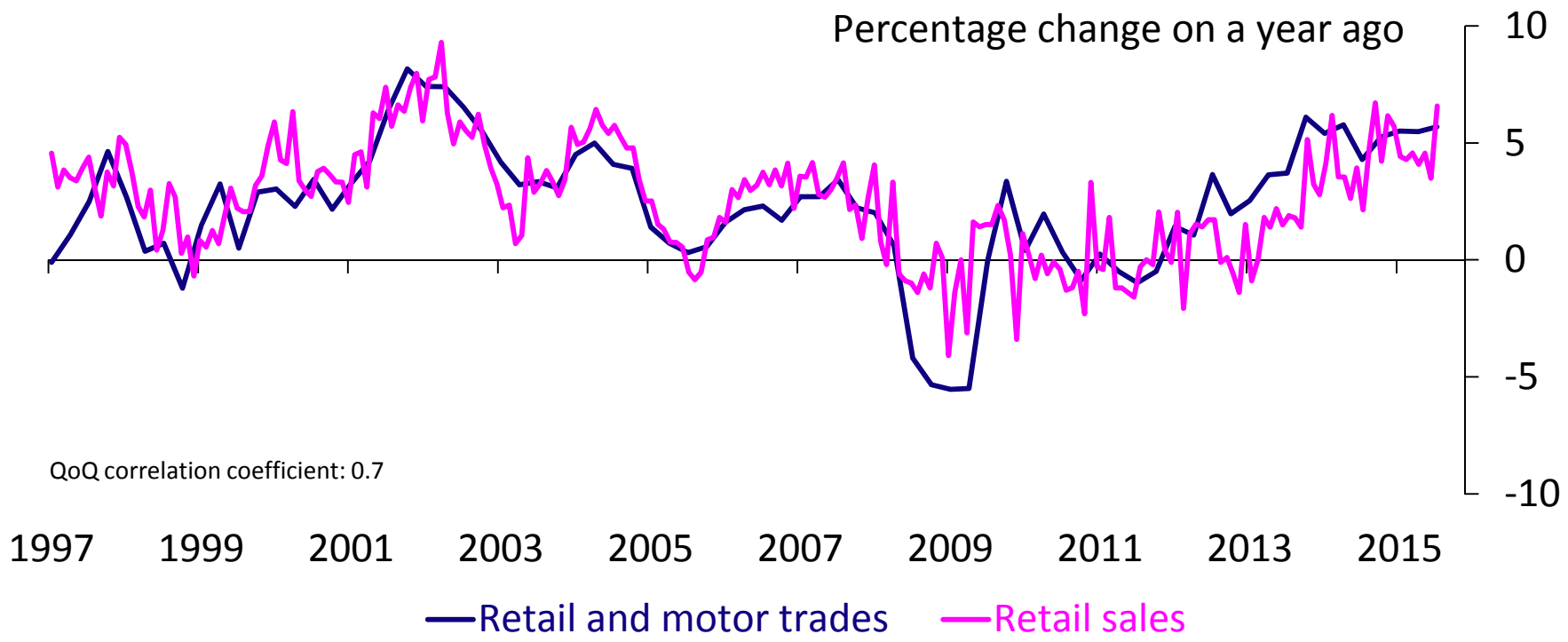
Consumer and business services



A service subsector is defined as a business service if the sum of its direct investment and intermediate consumption output shares exceeds its direct consumption share.

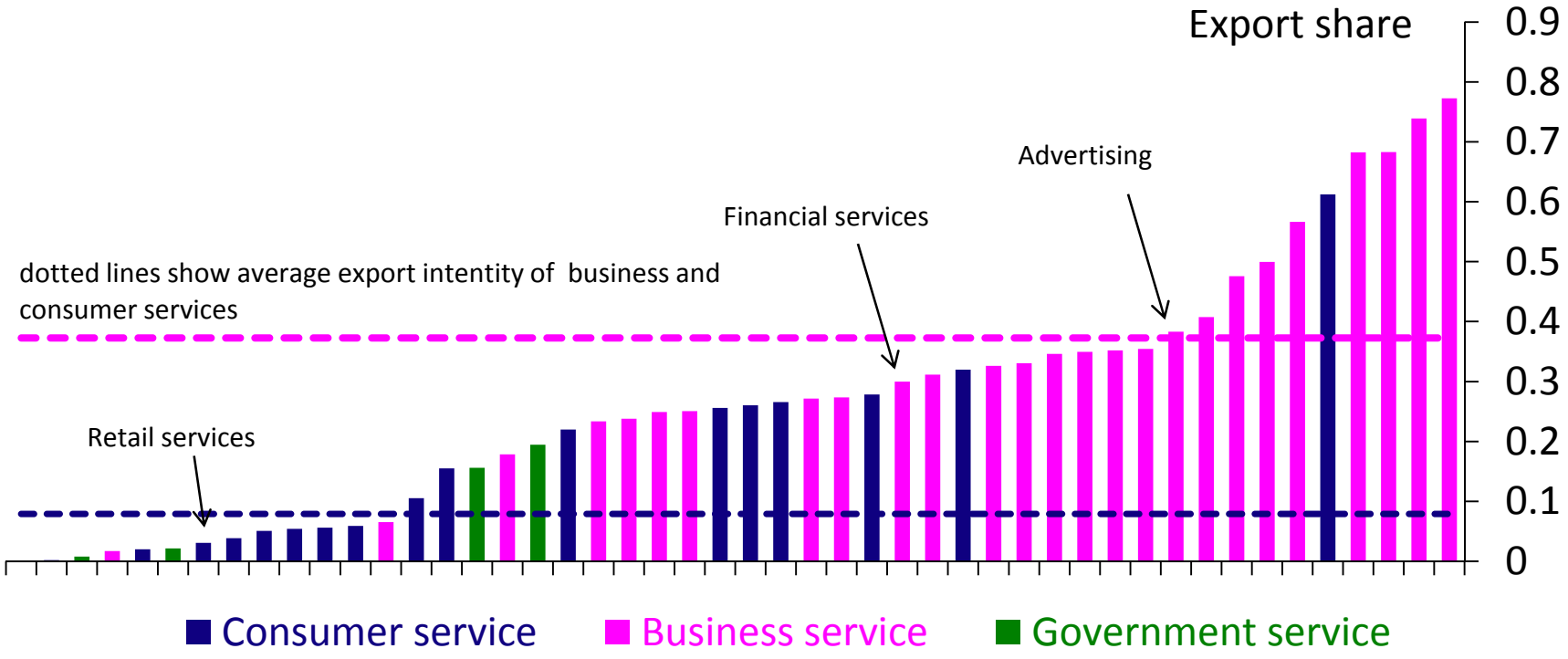
- Consumer services growth has been steady while business services have slowed

Distributive services



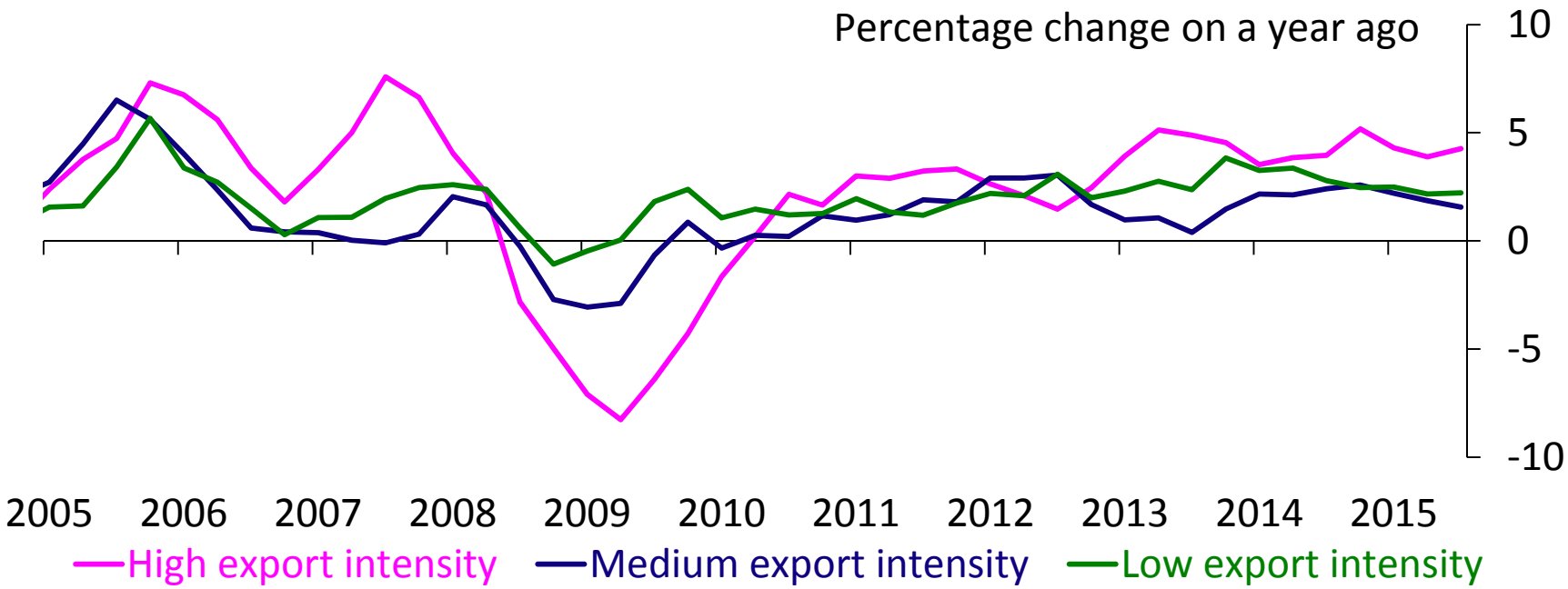
- Retail sales growth remains strong, consistent with robust growth in retail services output

Export orientation of service sectors



- Business services are much more export-oriented than others

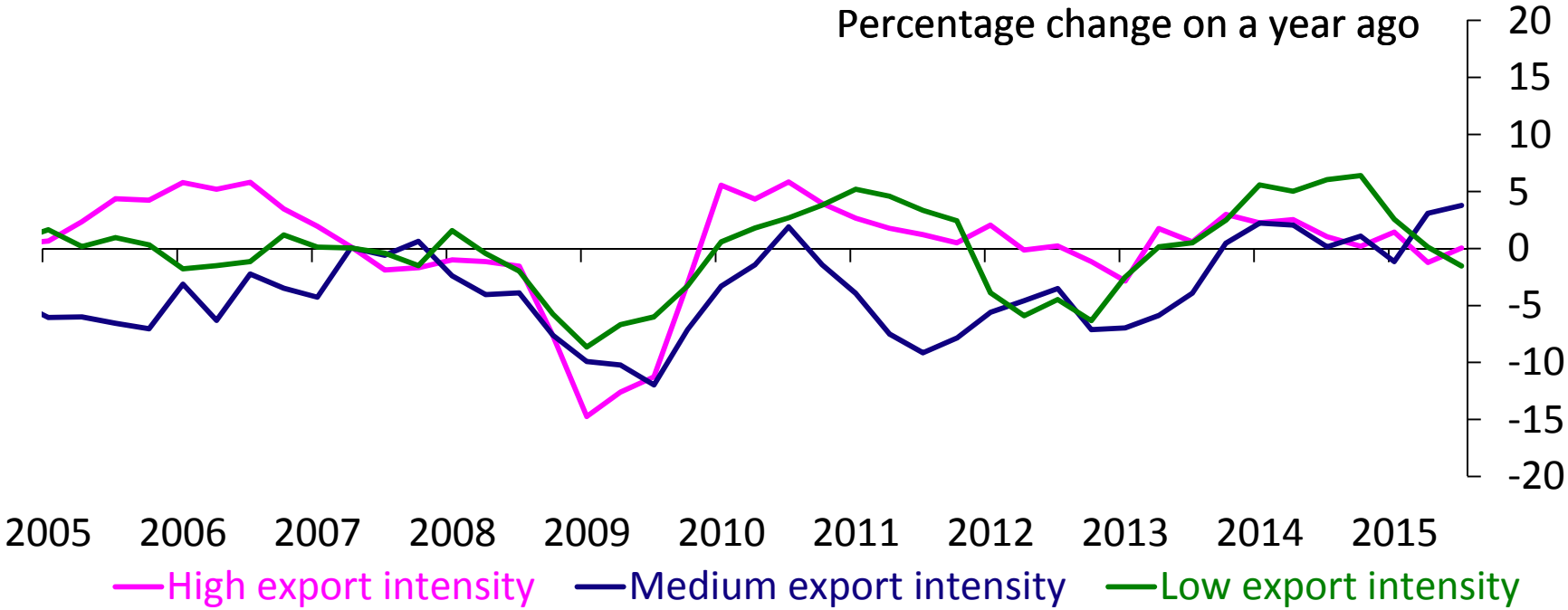
Services by export orientation



Subsectors of total services are grouped into three equally-weighted categories according to their export intensities

- Export intensive service sectors have not slowed more than domestically focused sectors

Manufacturing by export orientation



Subsectors of total manufacturing are grouped into three equally-weighted categories according to their export intensities

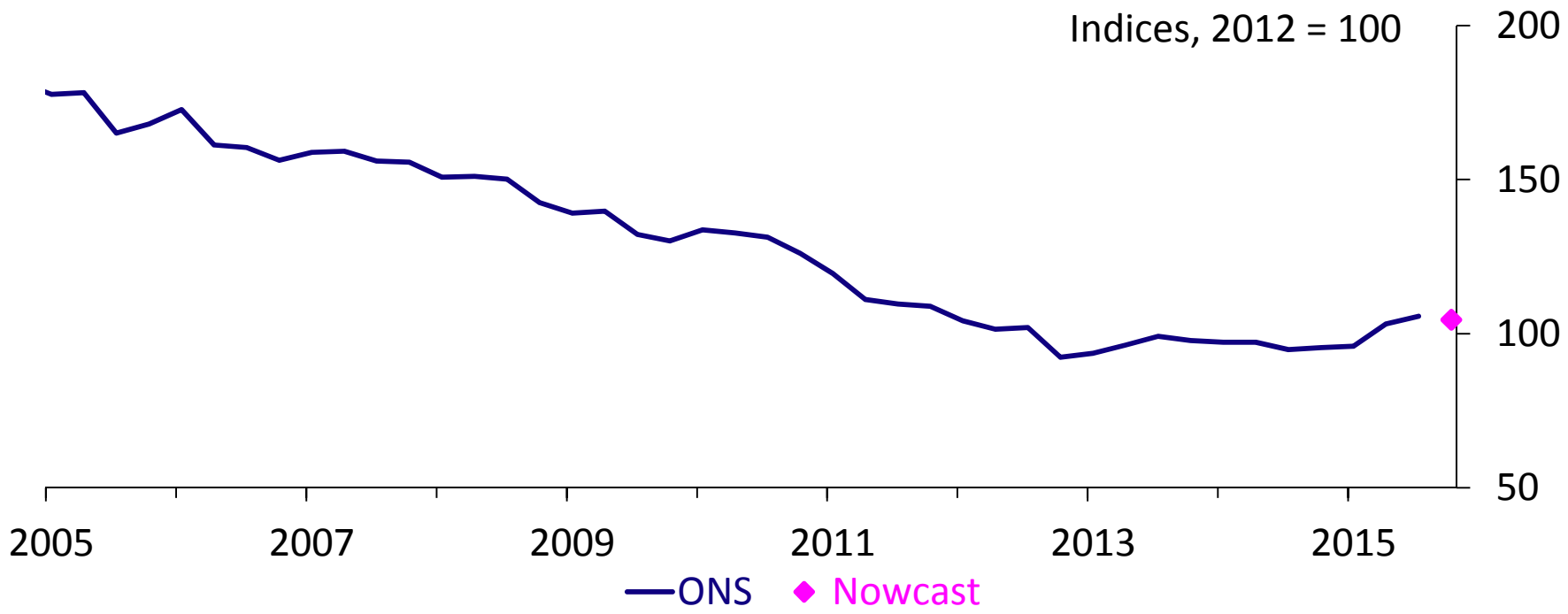
- Recent slowing in manufacturing driven by sectors with lower export intensity

What does the industry mix tell us?

Feature of narrative	Evidence*
Strong domestic demand	• Strong and steady consumer services growth • Solid distributive services, including retailing • Broad-based slowing in manufacturing and business services growth
Negative external influences	• Weak export-focused manufacturing and some evidence on service side
Nets to solid GDP growth	

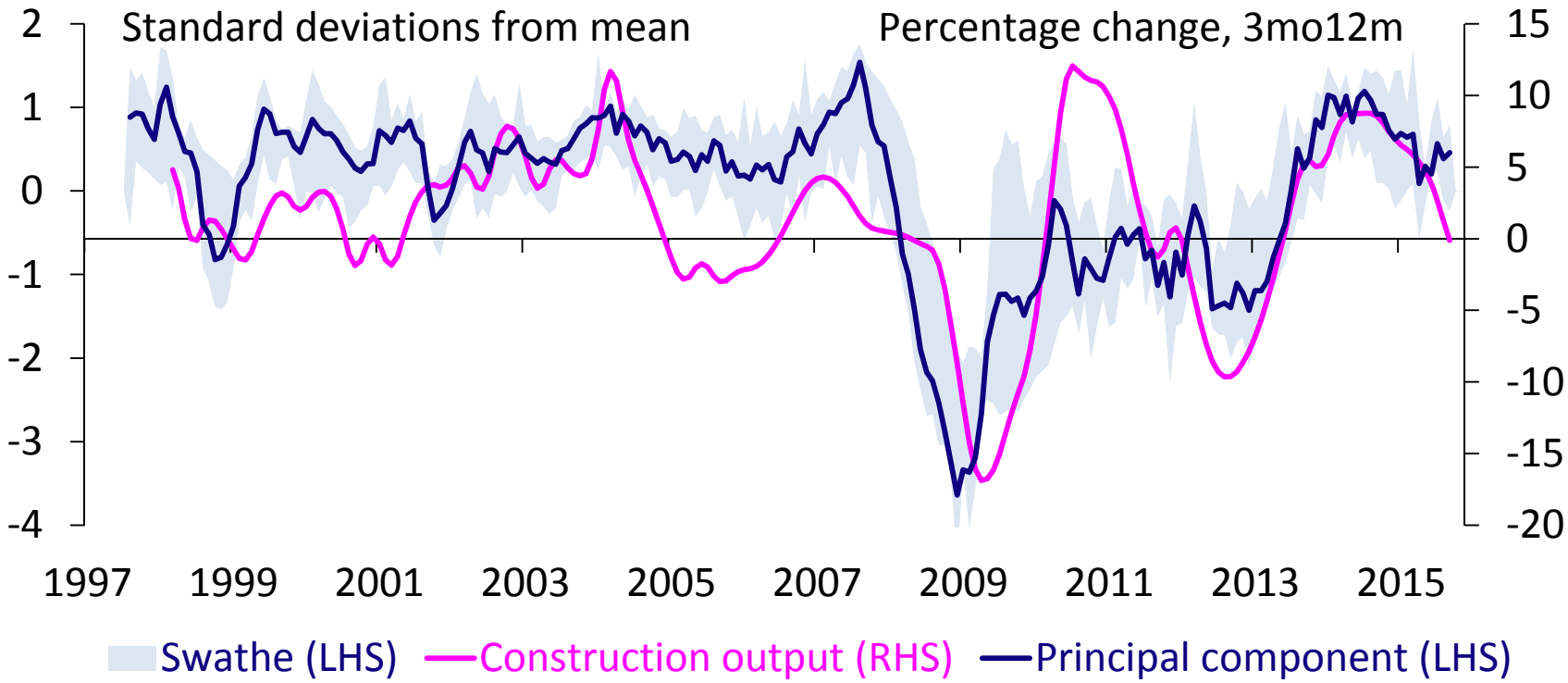
* Green indicates supportive evidence, red the reverse

Extraction output



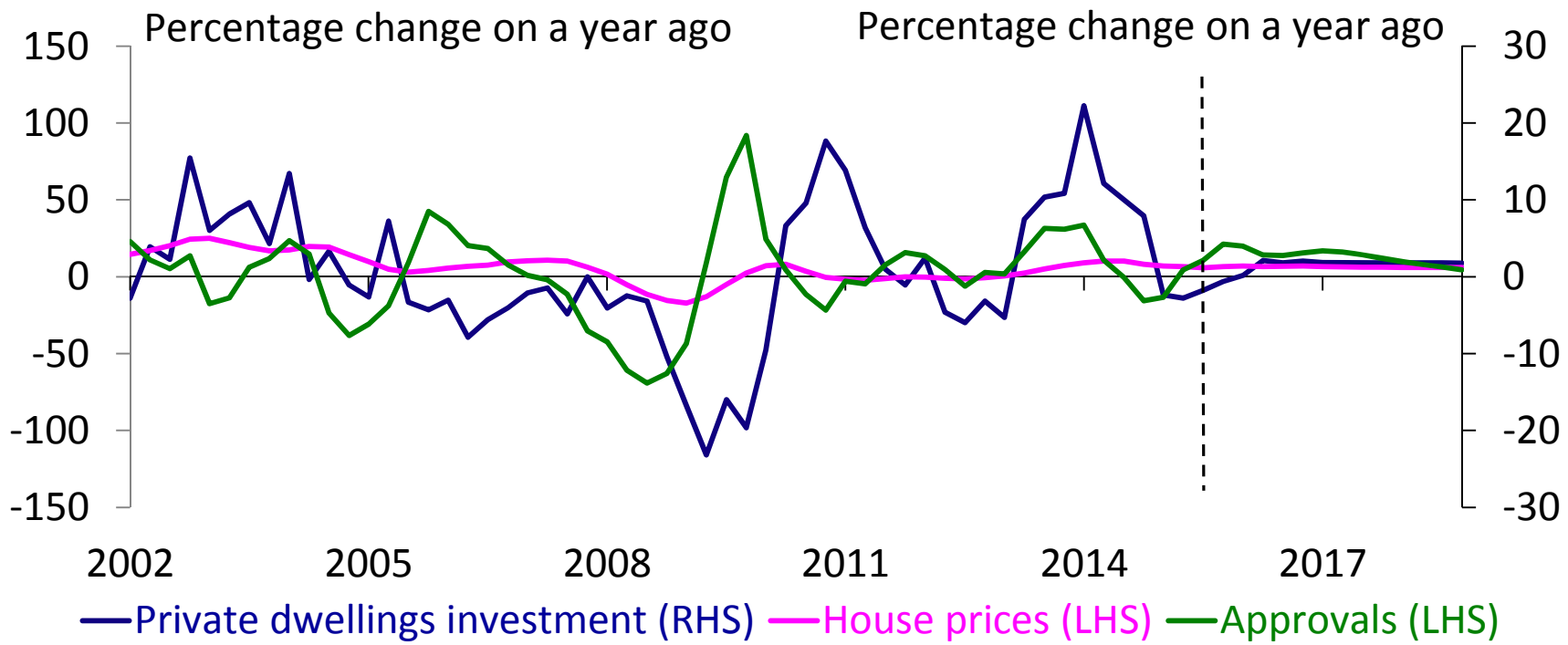
- We expect extraction output to be broadly flat in Q4, after contributing positively to growth in Q2 and Q3

Construction



- Construction output growth has slowed materially

Private dwellings investment



- The expected pick up in approvals and robust house price inflation should support dwellings investment

Government policies on house building

Since 2013

Help to Buy: Equity Loan – accounted for around 2% of housing transactions since April 2013

Announced in the Summer Budget and productivity plan

Reduction in social housing rents (explicitly incorporated in the forecast) - 1% reduction of social housing rents for four years

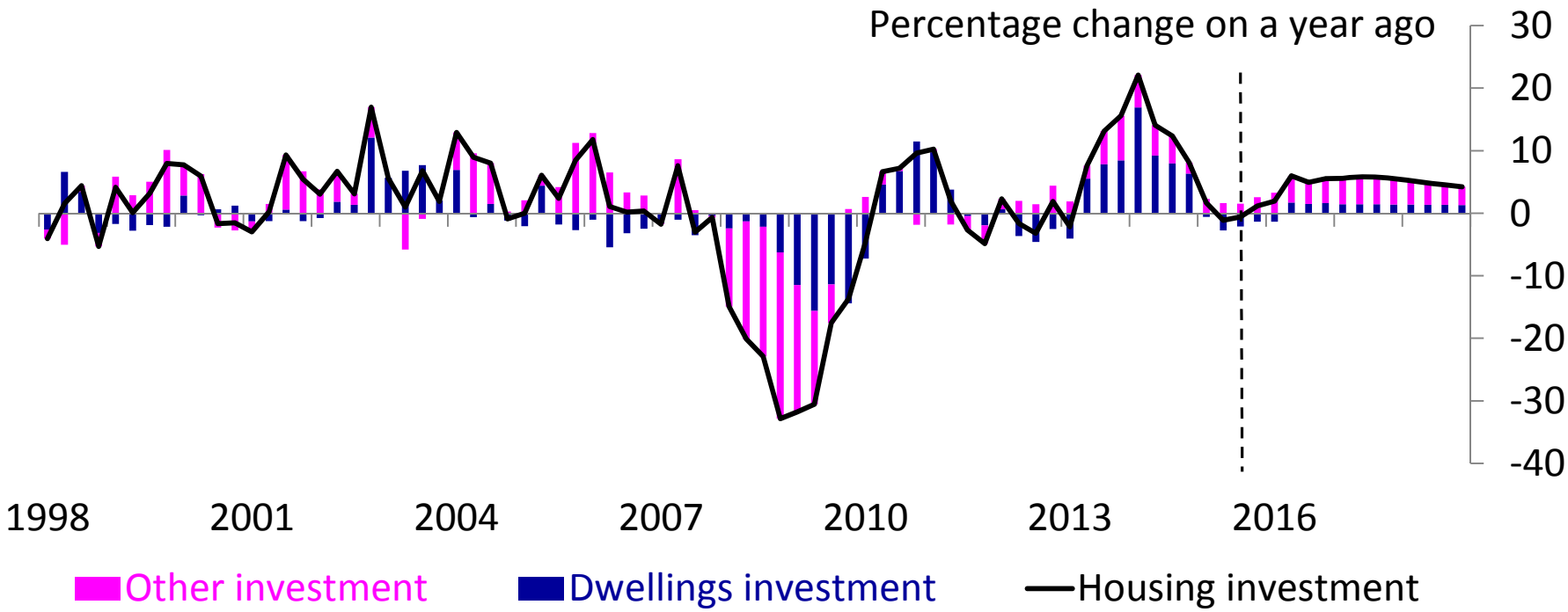
Initiatives announced in the Productivity Plan – for example new zonal system to give effectively automatic permission on some brownfield sites

Right to Buy extension - Extension to tenants of Housing Associations with commitment to replace all homes sold

Revised at the recent Conservative party conference

Starter Homes - Government committed to building 200,000 starter homes , with a change announced at the Conservative party conference that these homes may be built in place of affordable homes for rent under Section 106

Housing investment growth



- Housing investment grows at a little over 4% over the forecast, driven primarily by other housing investment

What does the industry mix tell us?

Feature of narrative	Evidence*
Strong domestic demand	• Strong and steady consumer services growth • Solid distributive services, including retailing • Broad-based slowing in manufacturing and business services growth • Weak construction consistent with low housing investment
Negative external influences	• Weak export-focused manufacturing and some evidence on service side
Nets to solid GDP growth	• Boost from extraction flattering headline picture

* Green indicates supportive evidence, red the reverse

Summary outlook for Q4 & Q1 growth

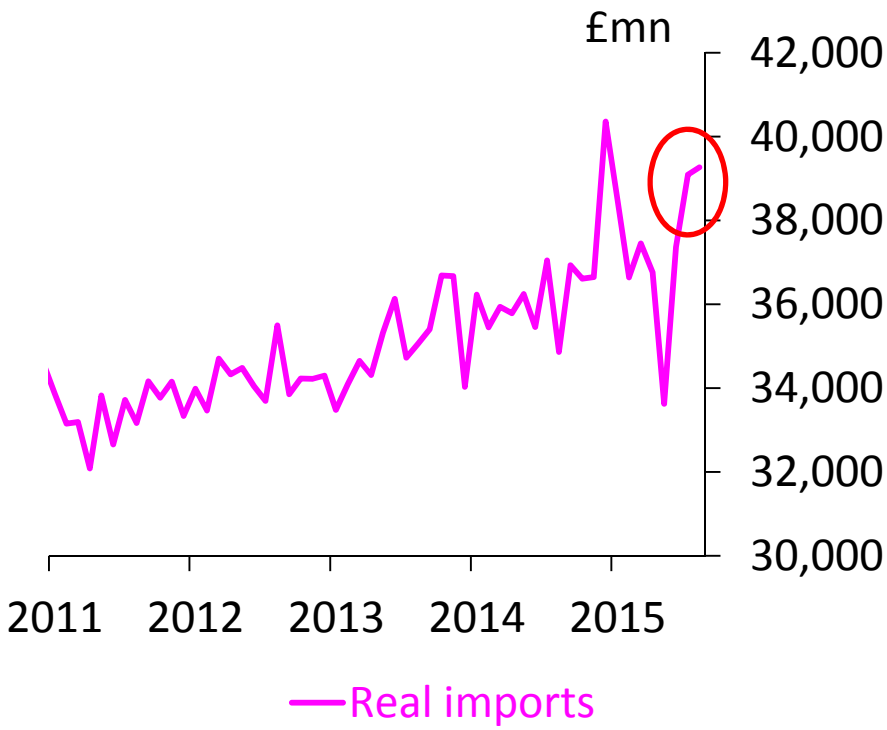
- Little news in Q3 GDP growth, with services output firm, and notable rebound in CIPS data in October
- But range of nowcasting models weaker than the benchmark forecast, at 0.4-0.6% for Q4 and Q1
- Industry data suggests broad-based decline in growth since 2014, rather than just externally-focused
- On balance, we expect growth of 0.6% in both Q4 and Q1, 0.1pp lower than the benchmark forecast

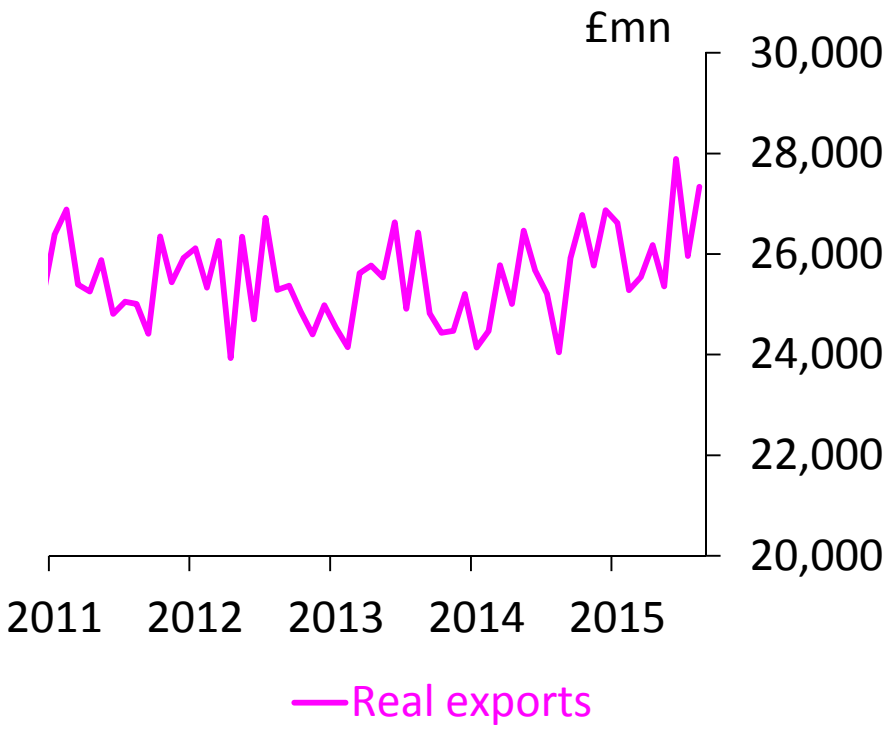
Outline

1) What is the short-term growth outlook?

2) Update on issues with the trade data

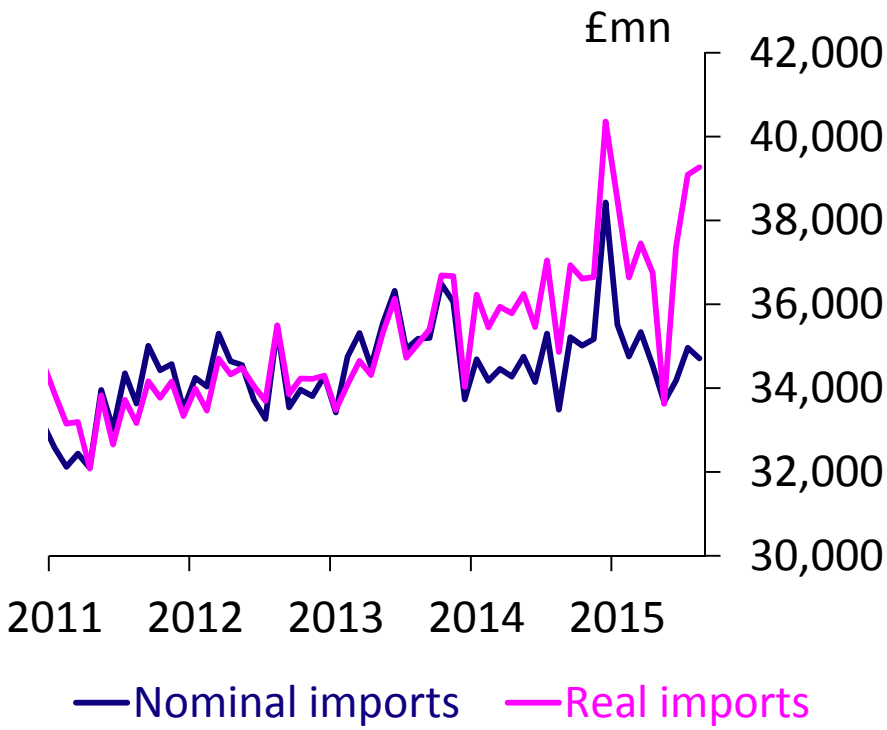
Monthly goods trade

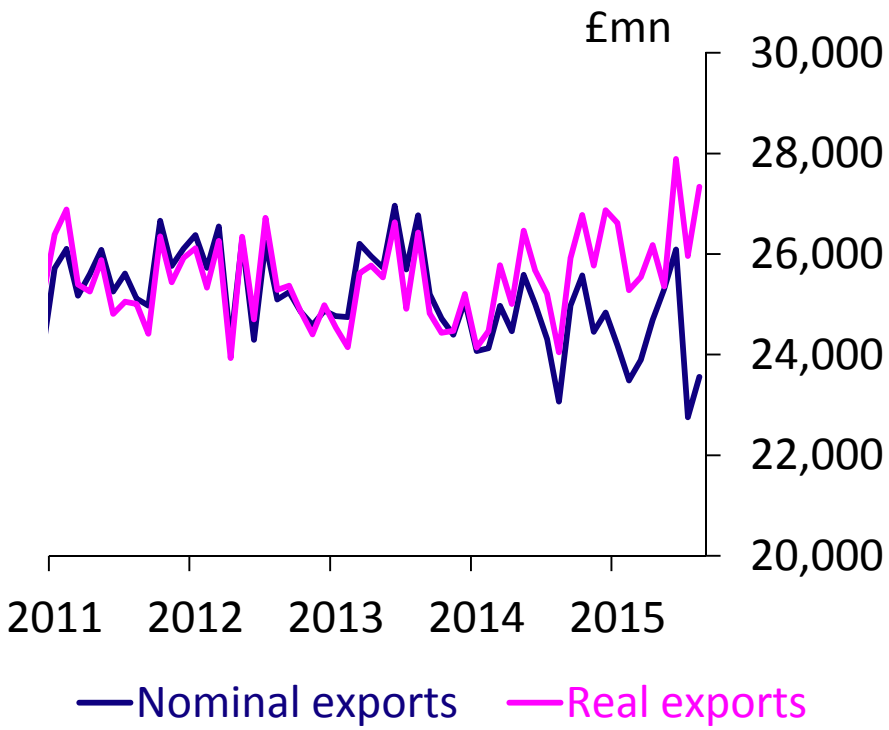




- Weak Q2 real goods imports are unwinding in Q3

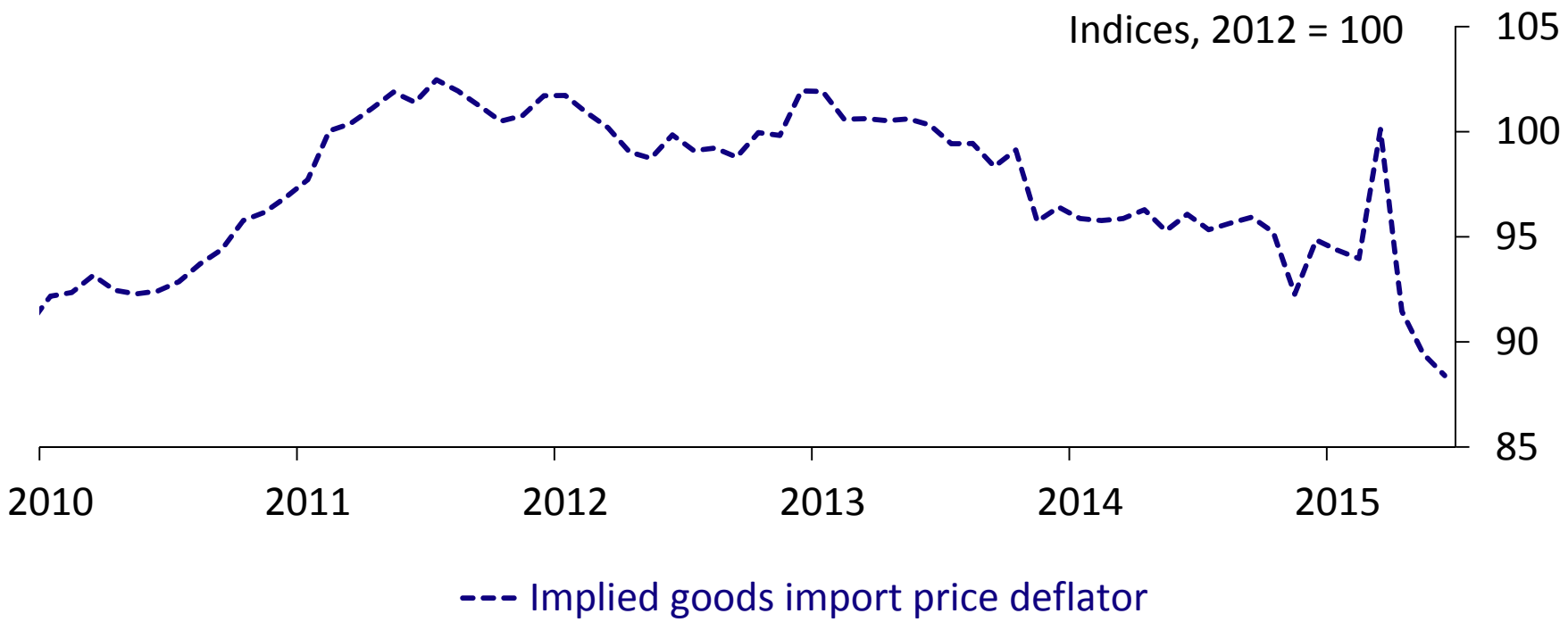
Monthly goods trade





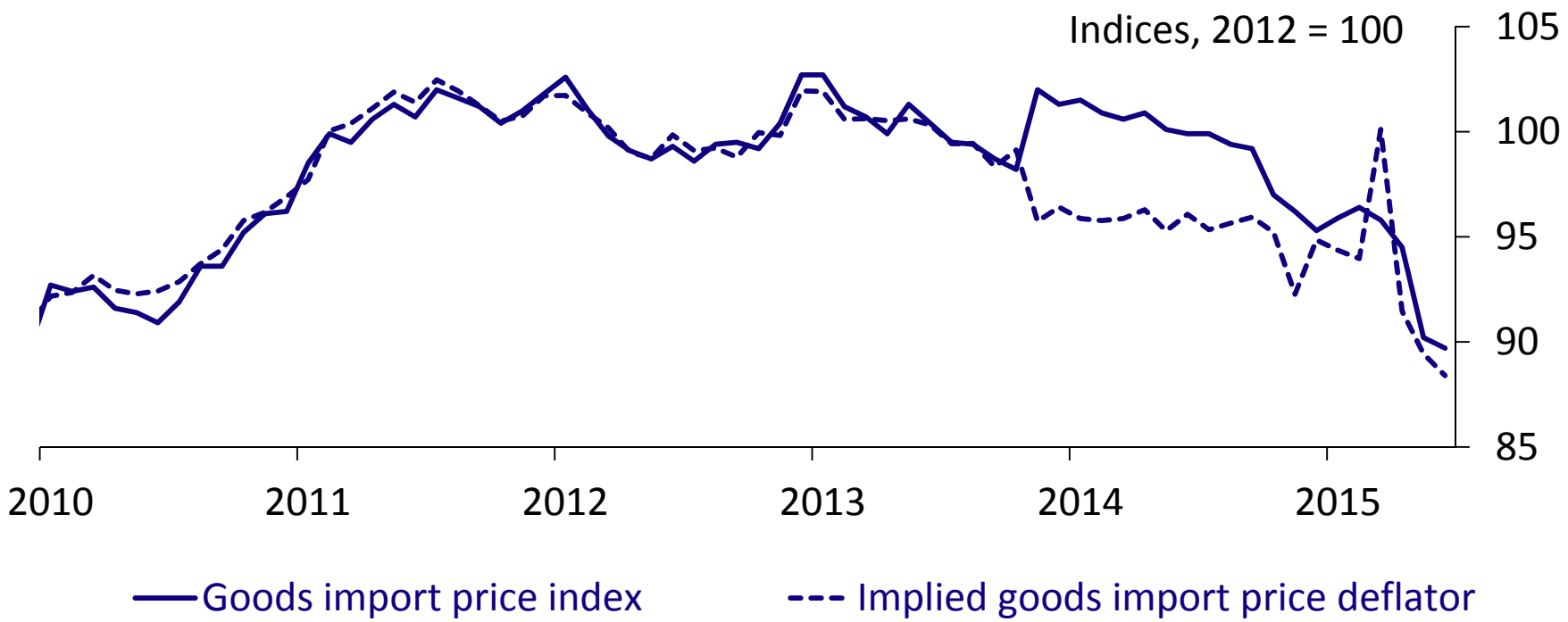
- The real and nominal trade data have diverged since 2014

Monthly goods import prices



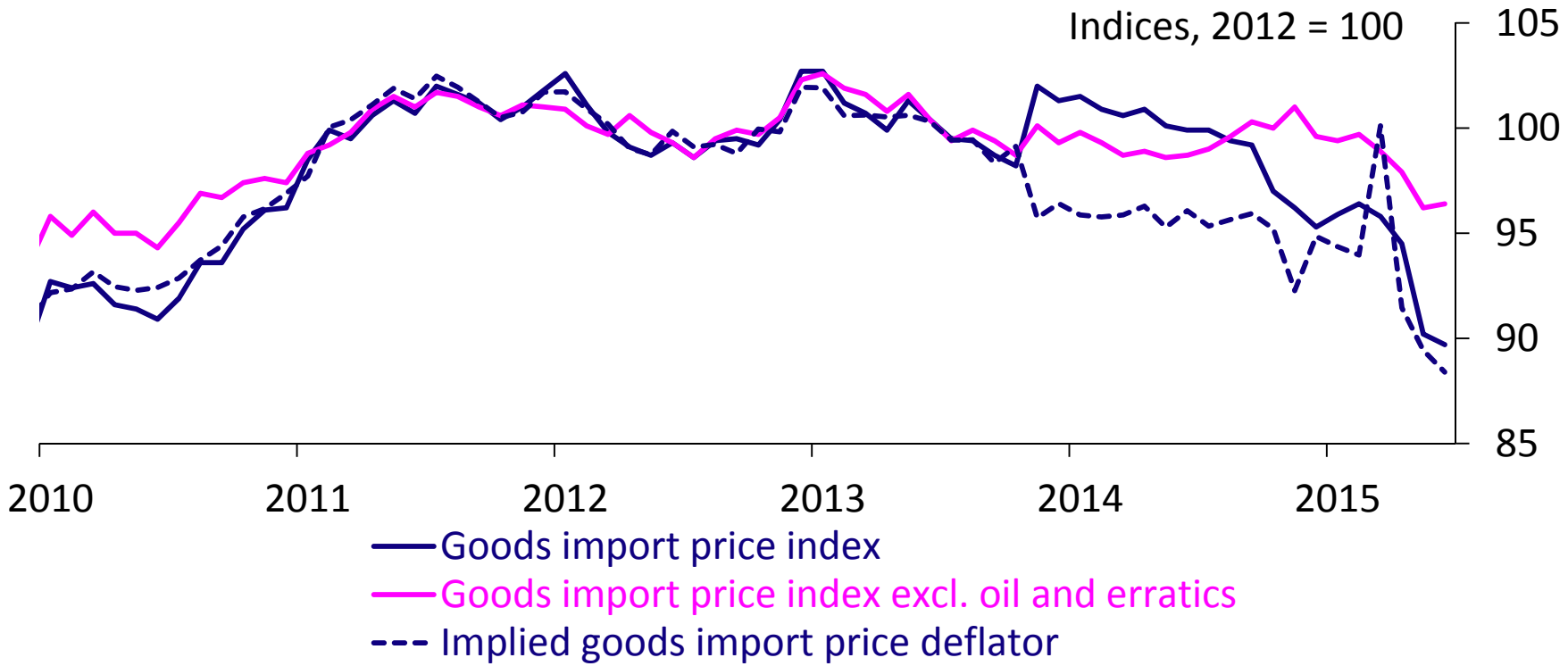
- The implied goods import price deflator is incorrect from 2014 onwards. See for more details.

Monthly goods import prices



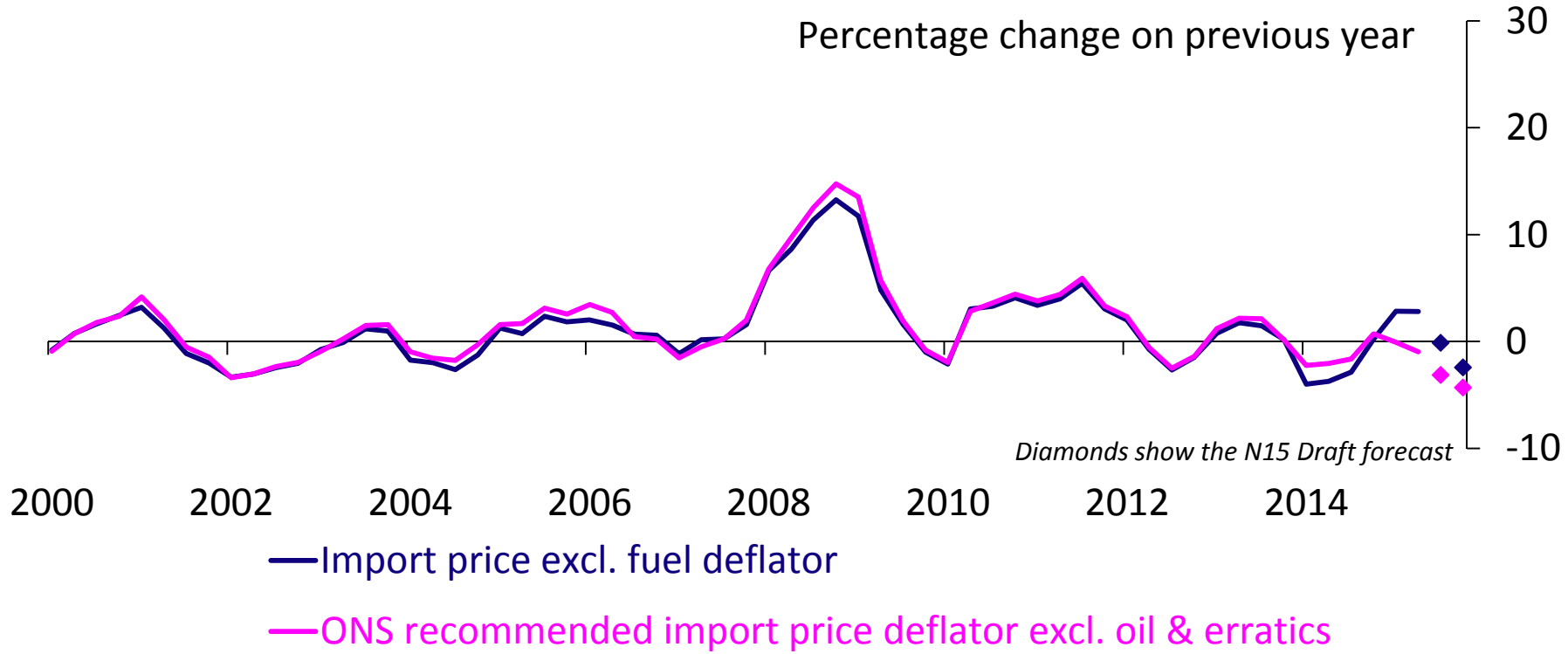
- The goods import price index, largely based on PPIs, gives a better steer on import prices. for more details.

Monthly goods import prices



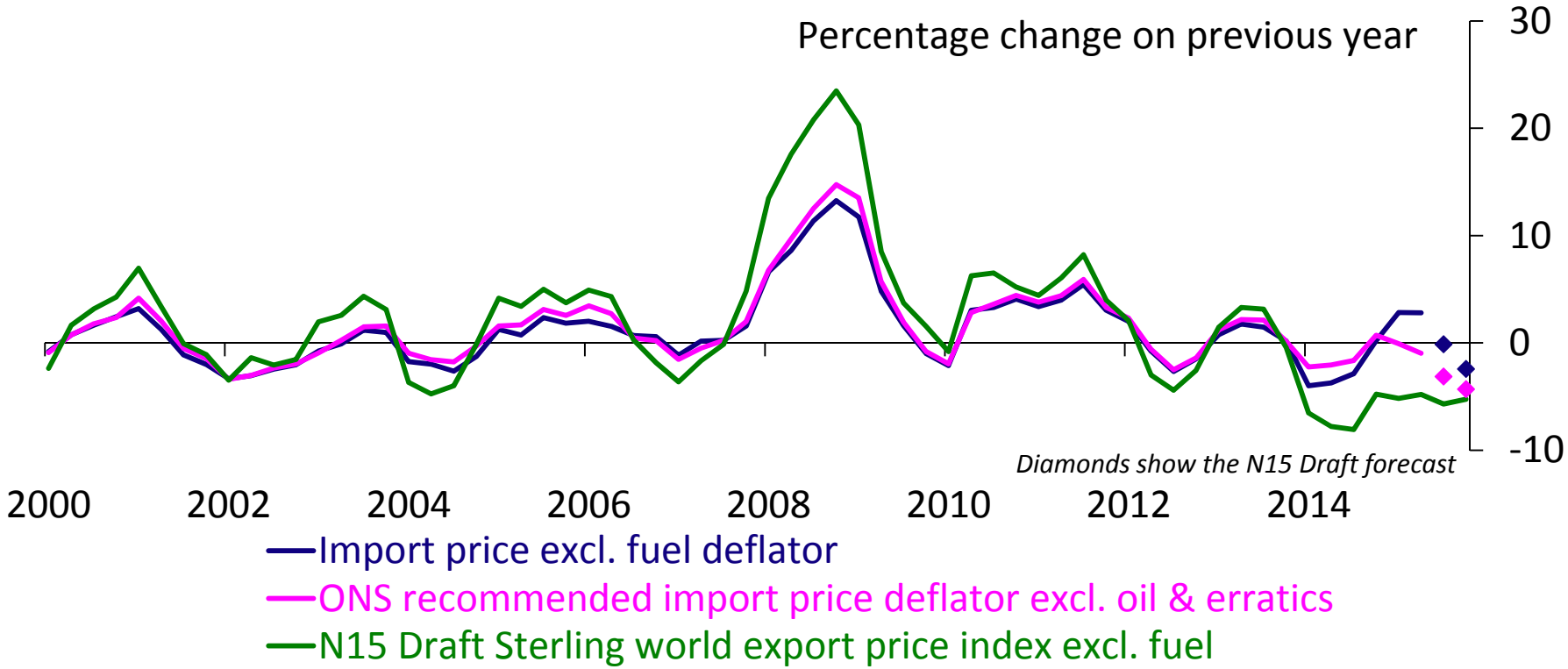
- The goods import price index excl. oil & erratics provides the best measure for our assessment of import price pass-through

Import prices (goods & services) excluding fuel



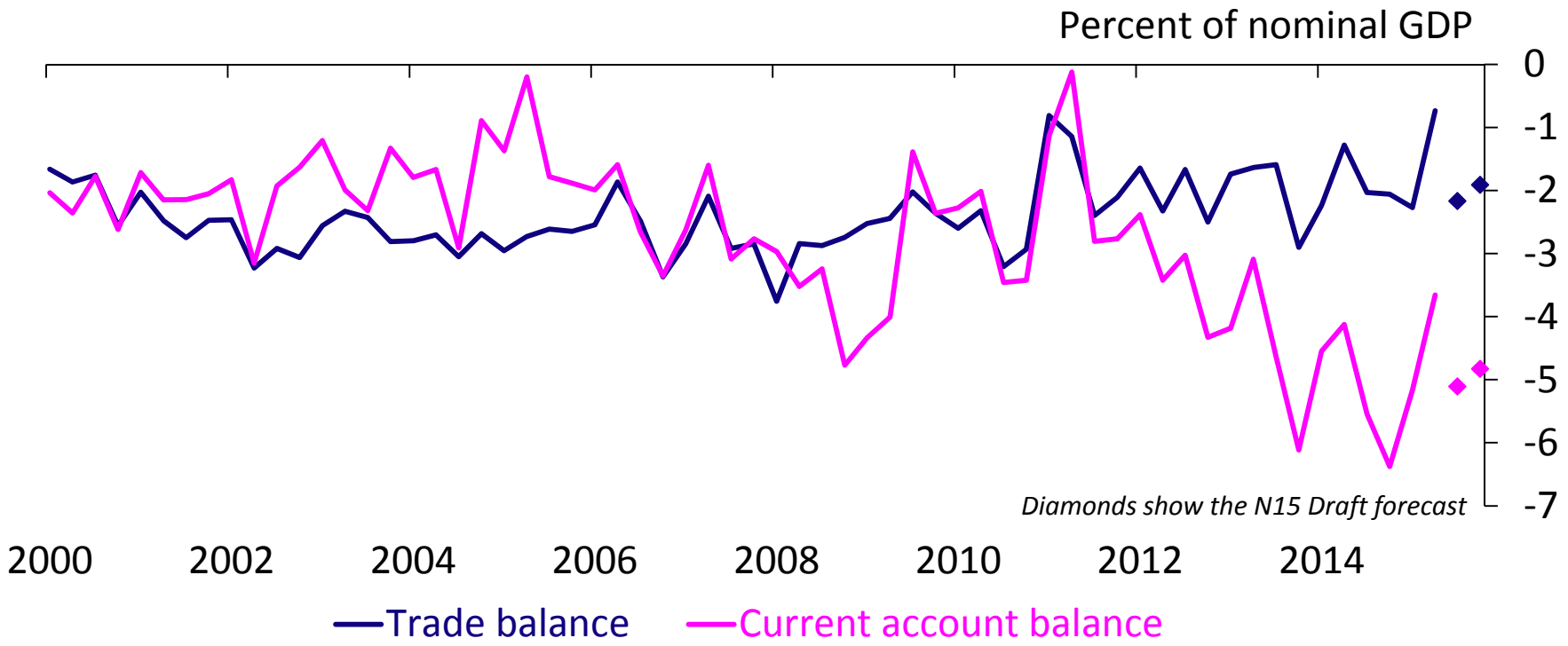
- We will be using the import price series excl. oil & erratics provided to us by the ONS as our main measure of import prices

Import and sterling world export prices



- Preferred import price data consistent with our import pass-through assumption

Trade balance and current account deficit



- The improvement in the nominal trade balance and current account deficit in 2015 Q2 looks to be erratic, and we expect these to unwind

Key messages

- We have revised down Q4 and Q1 a little, to 0.6%
- There is greater than usual uncertainty about the trade data
- But preferred import price data appear consistent with pass-through assumptions
- We think the trade balance and current account probably widened in Q3

END

5: Costs and Prices

Costs & Prices

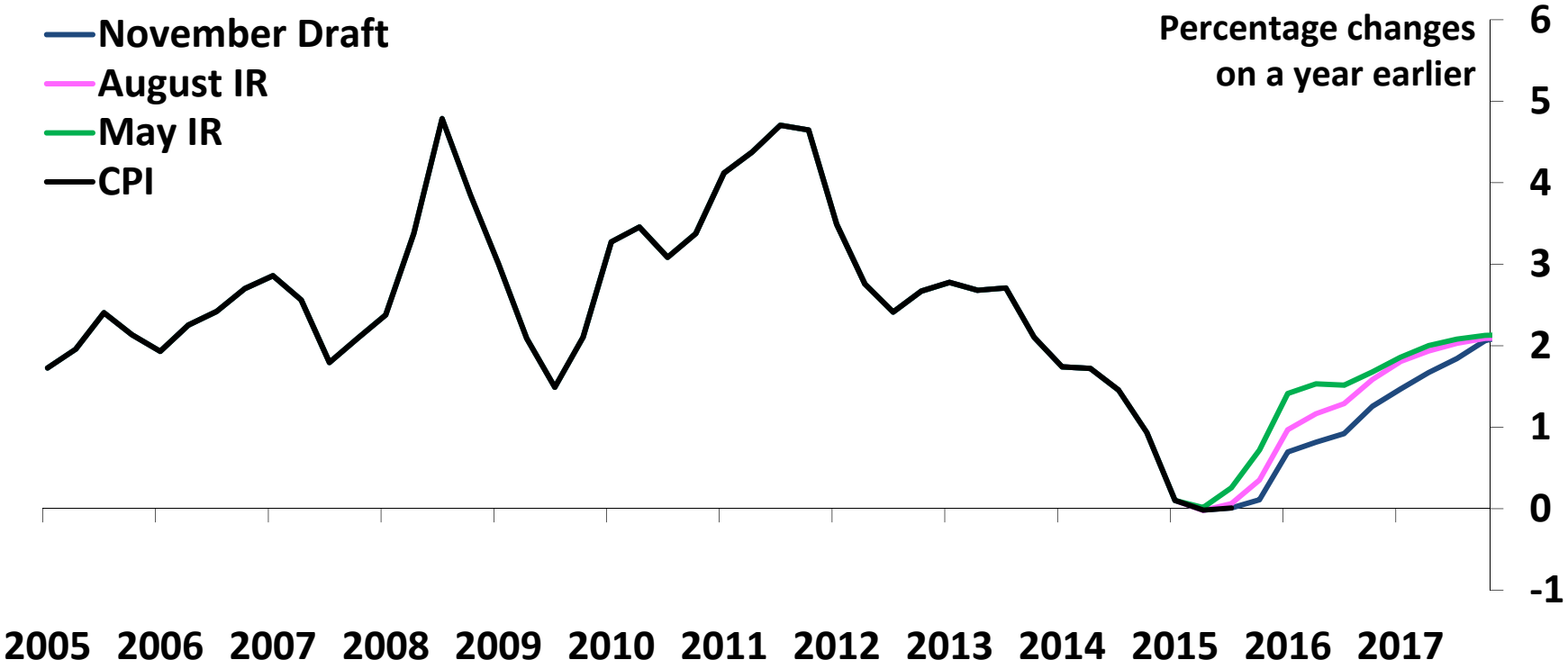
28 October 2015

Structural Economic Analysis Division

Agenda

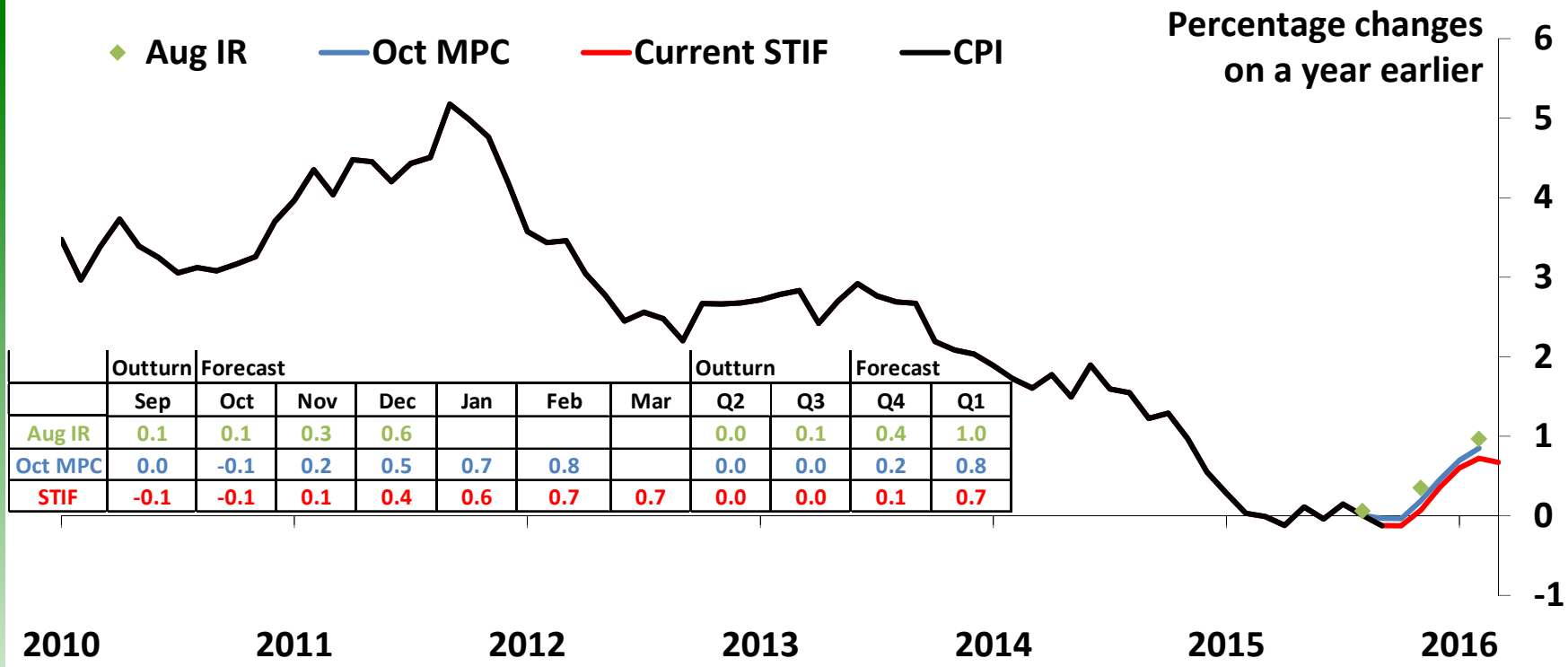
- **How confident can we be in the projected pickup in inflation?**

Inflation forecasts



- **Near-term profile for inflation has been revised down.**

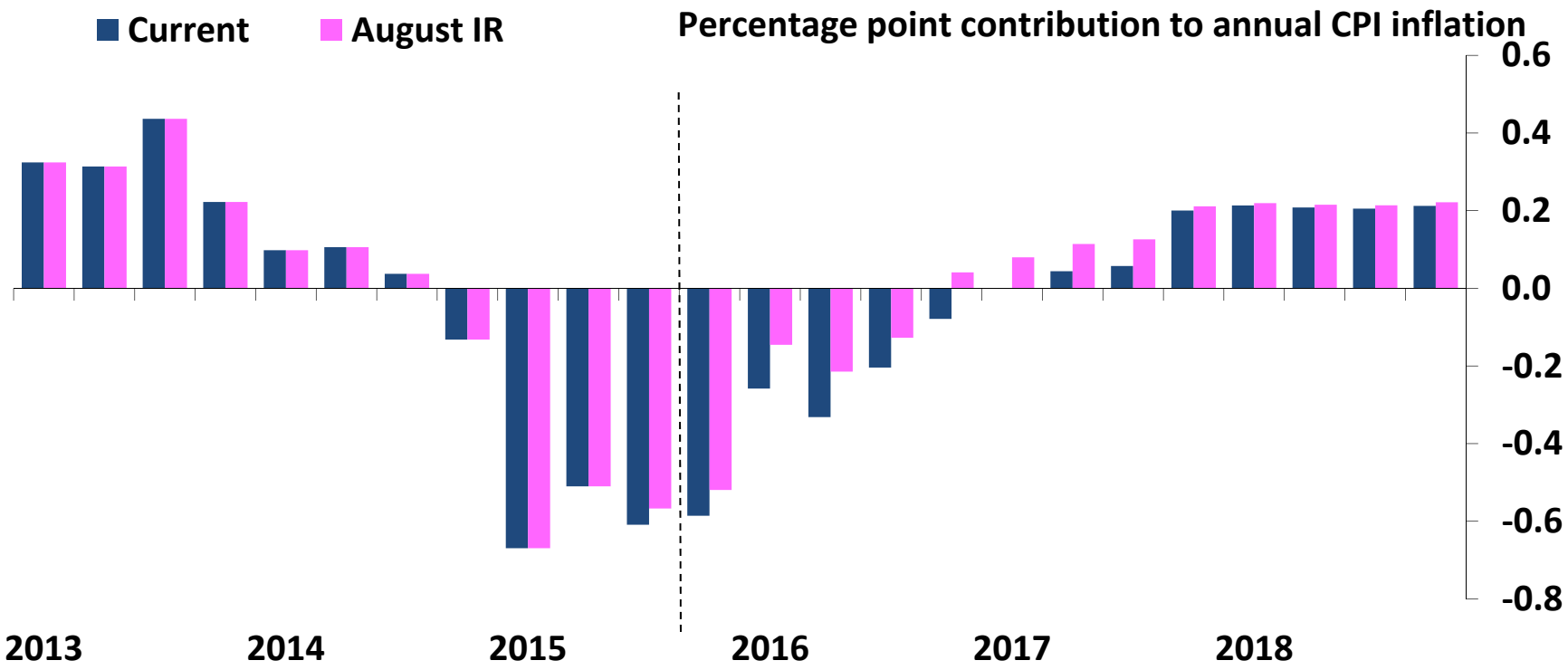
Short-term inflation forecast



	Outturn	Forecast						Outturn		Forecast	
	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Q2	Q3	Q4	Q1
Aug IR	0.1	0.1	0.3	0.6				0.0	0.1	0.4	1.0
Oct MPC	0.0	-0.1	0.2	0.5	0.7	0.8		0.0	0.0	0.2	0.8
STIF	-0.1	-0.1	0.1	0.4	0.6	0.7	0.7	0.0	0.0	0.1	0.7

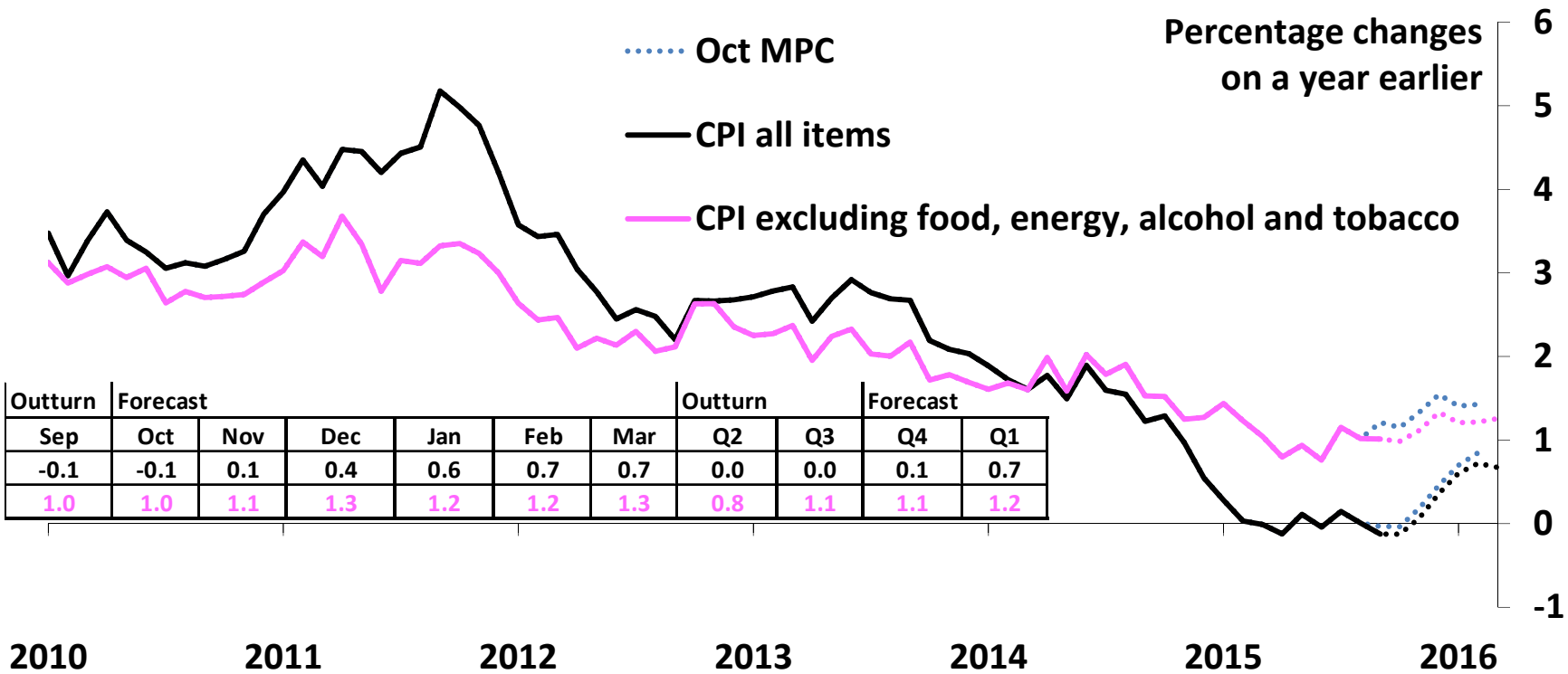
- **Short-term forecast 0.3pp lower than August IR by Q1.**

Contribution of energy to CPI inflation



- **Base effects from <u>food and energy</u> likely to push up on inflation by ½pp over next six months.**

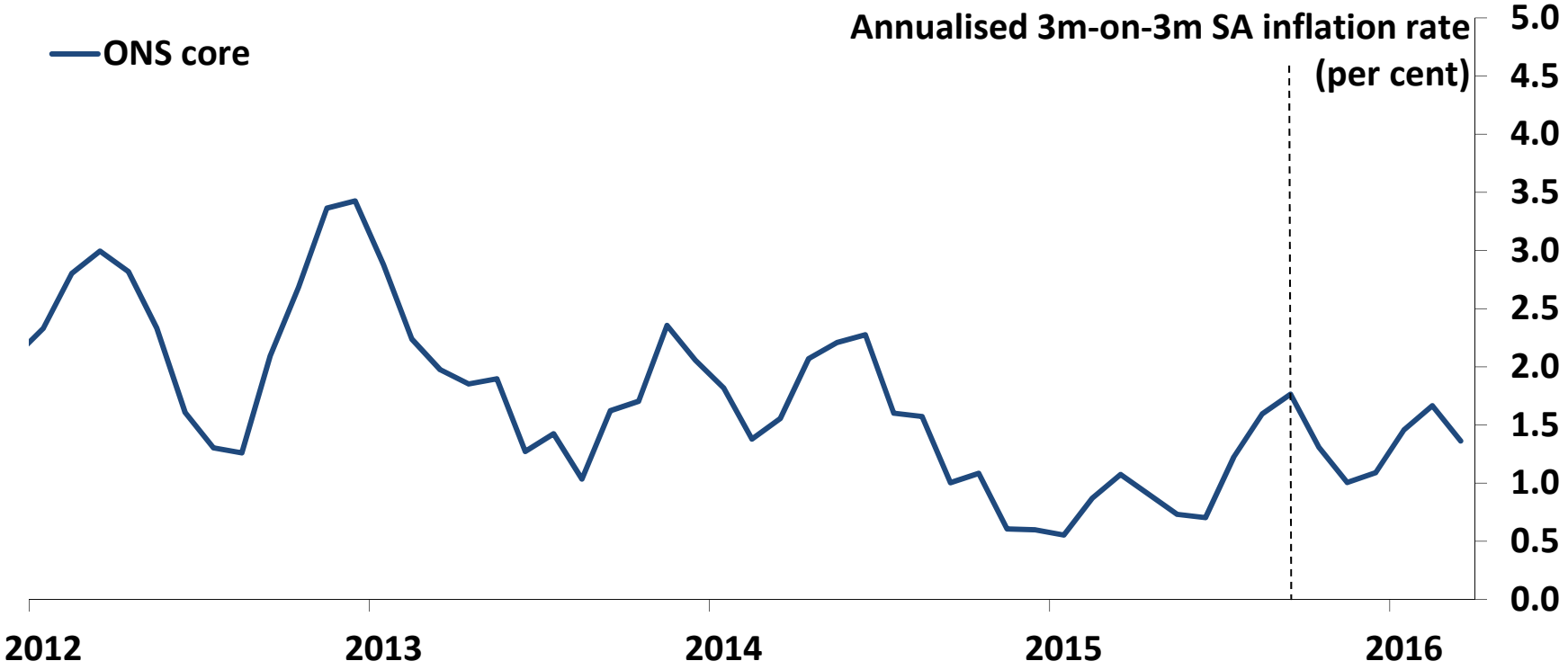
Short-term inflation forecast



Outturn	Forecast						Outturn		Forecast	
Sep	Oct	Nov	Dec	Jan	Feb	Mar	Q2	Q3	Q4	Q1
-0.1	-0.1	0.1	0.4	0.6	0.7	0.7	0.0	0.0	0.1	0.7
1.0	1.0	1.1	1.3	1.2	1.2	1.3	0.8	1.1	1.1	1.2

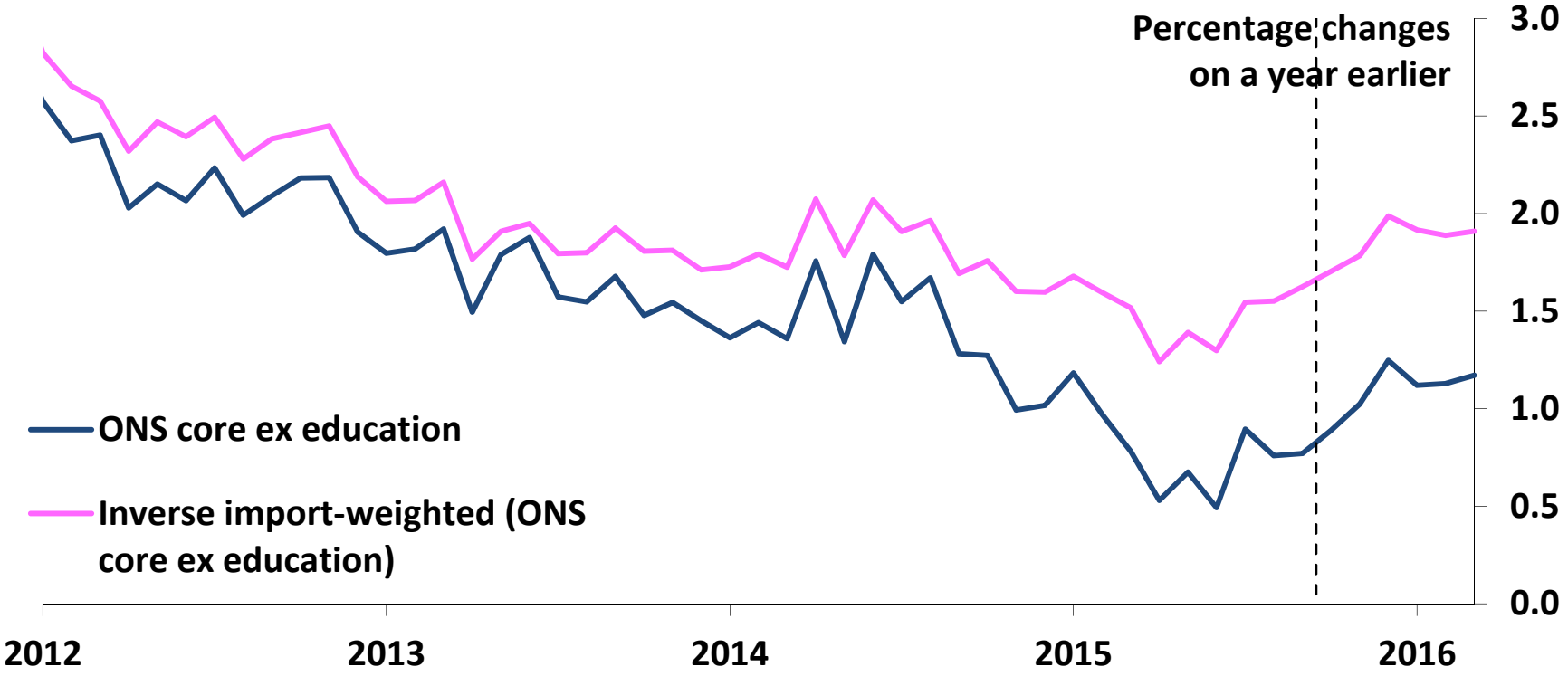
- **ONS core inflation now expected to pick up to 1.3% by March.**

3-month on 3-month ONS core inflation



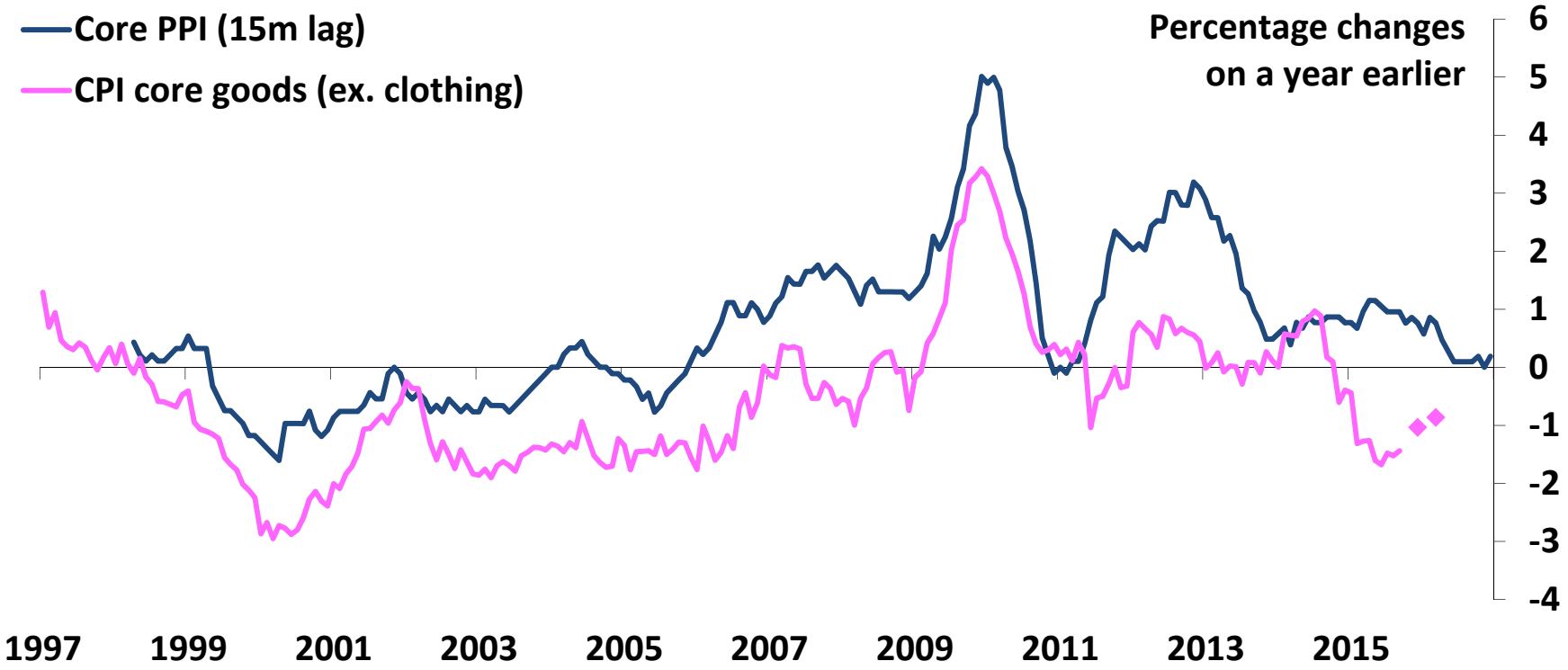
- **Annualised three-month on three-month seasonally-adjusted core at 1.8% in September.**

ONS core & inverse import-weighted core



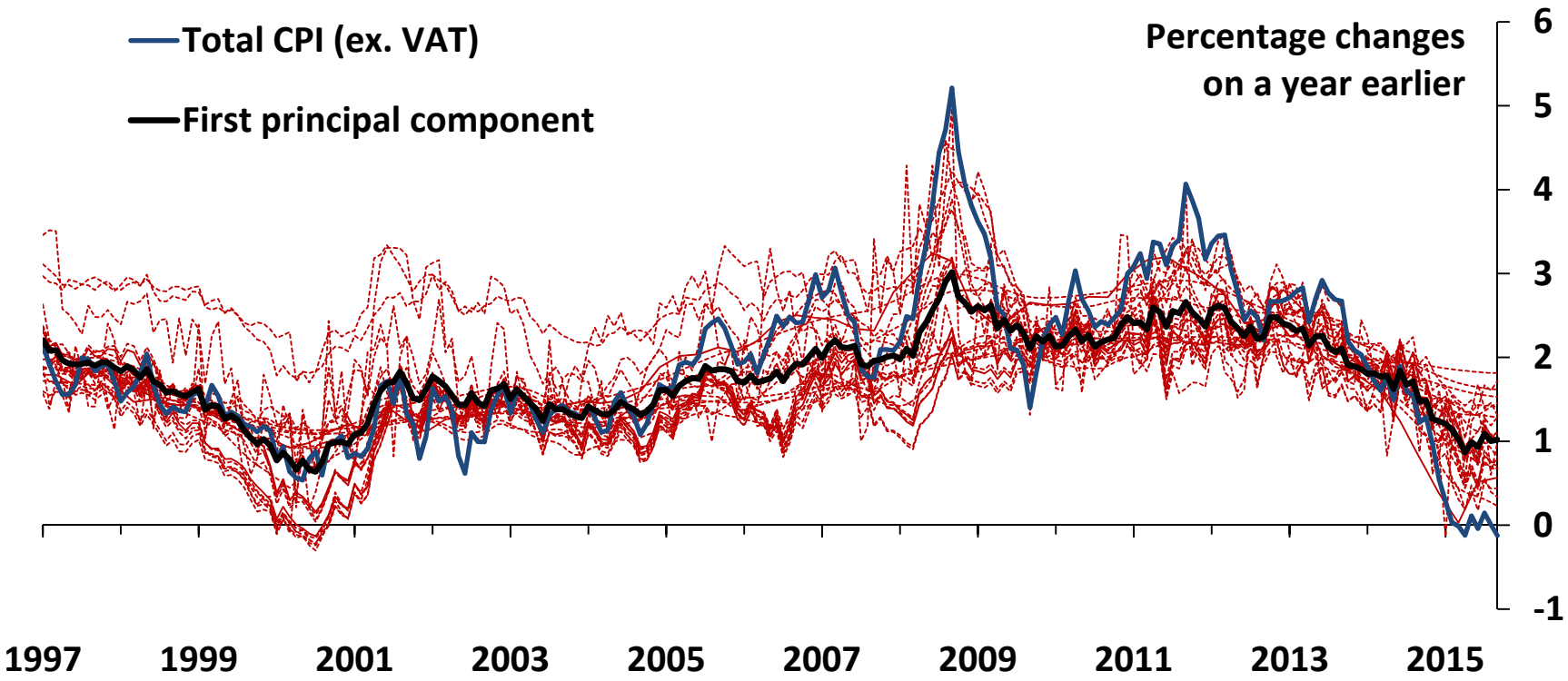
- **Import-intensive items in CPI have dragged down inflation.**

Producer prices and core goods inflation



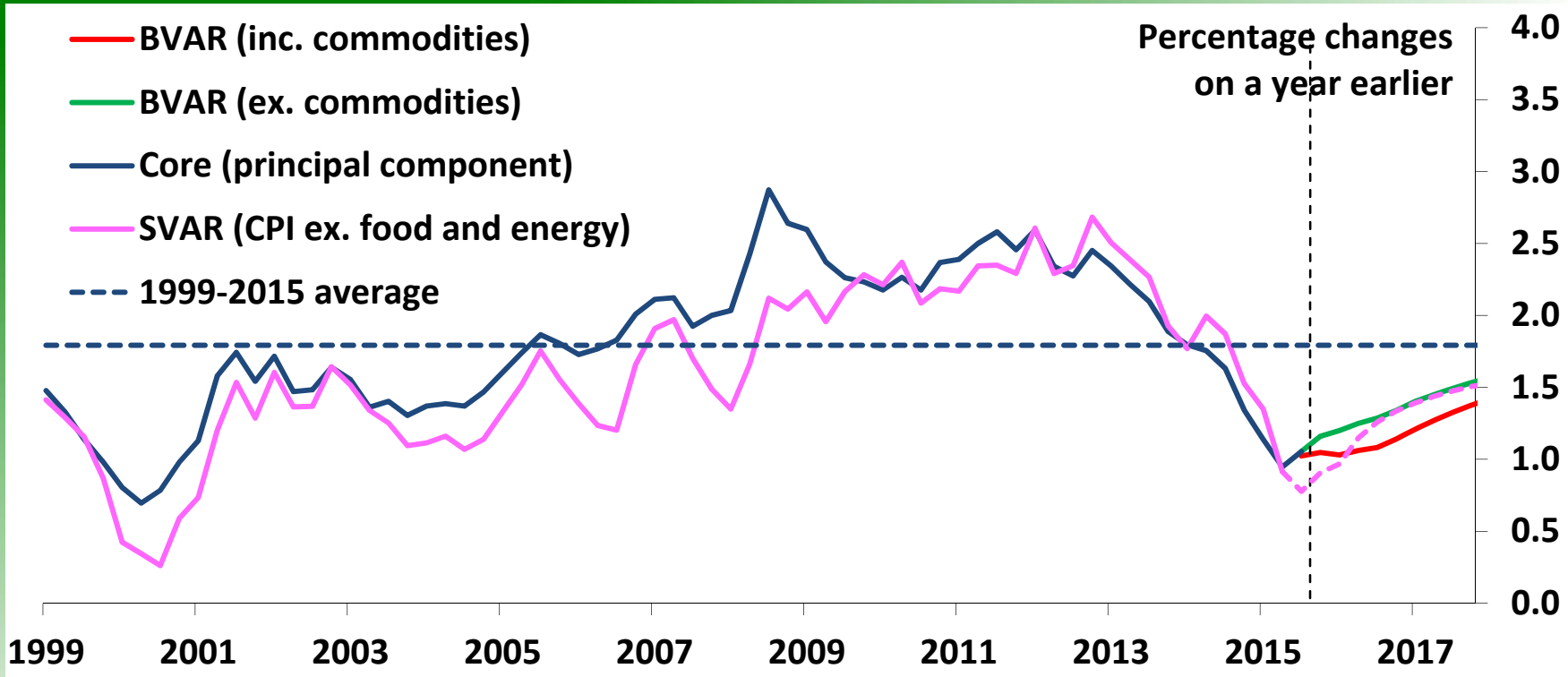
- **Core PPI inflation remained subdued at 0.2% in September.**

Core inflation measures



- **Broader measure of core at 1% in September.**

Forecasts of core inflation

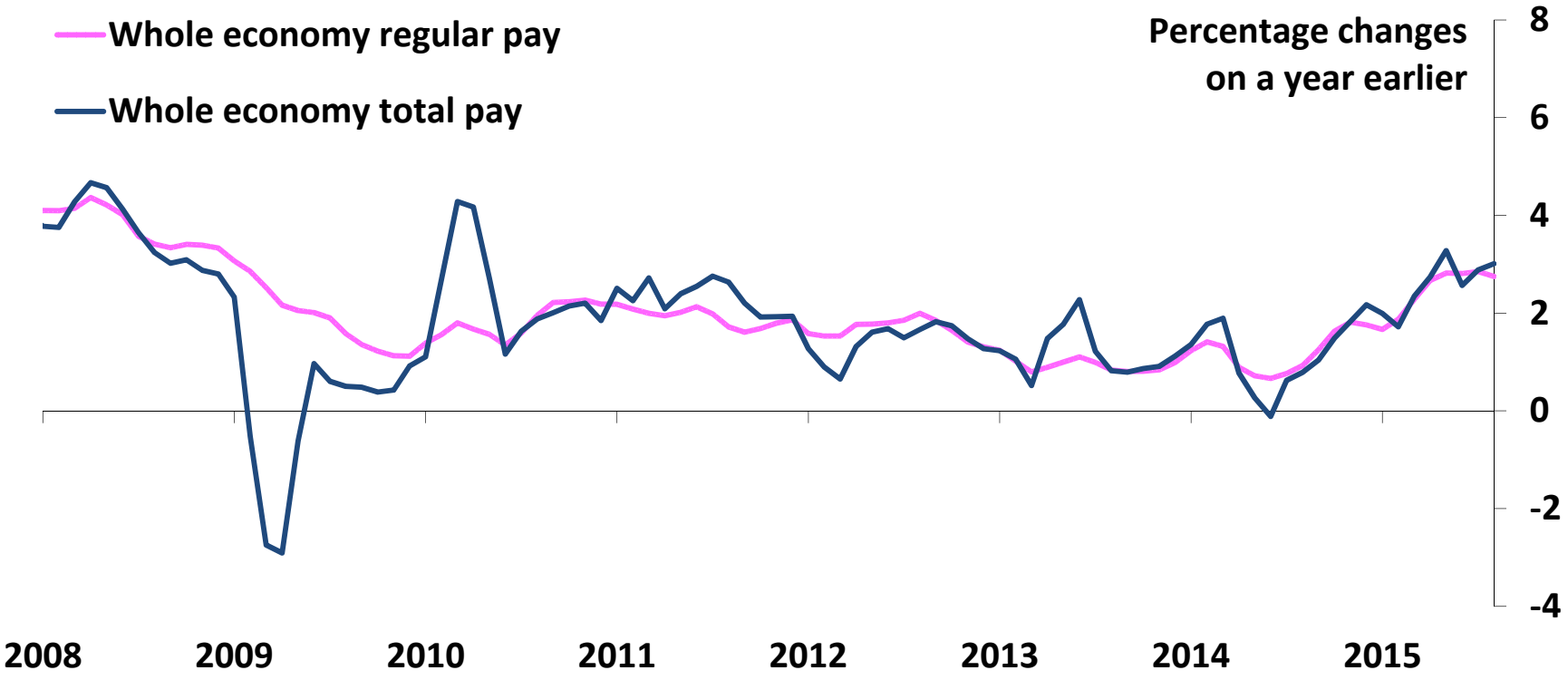


- **Forecasts from BVAR and SVAR models point to a gradual pickup in core inflation.**

Main messages

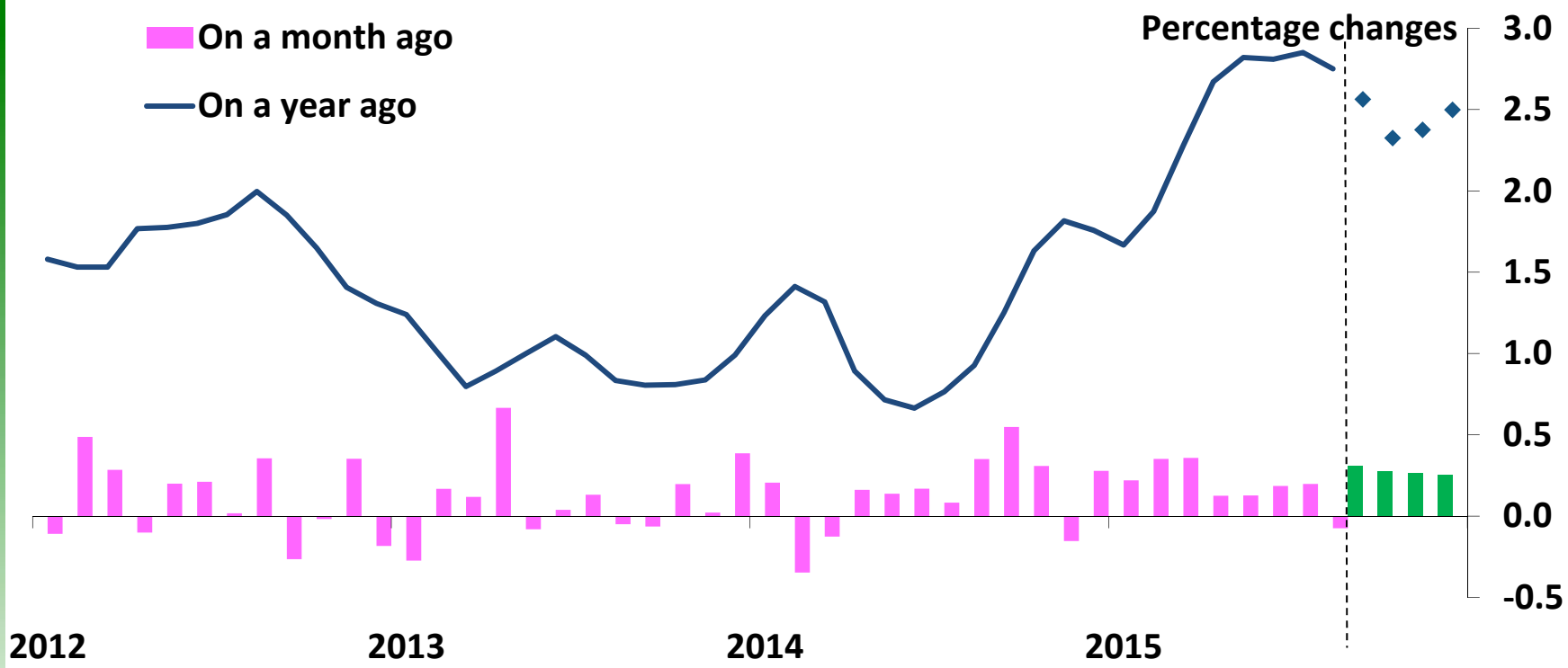
- **How confident can we be in the projected pickup in inflation?**
  - **Base effects from food and energy could add 1pp to inflation over the next year.**
  - **Core inflation projected to pick up only gradually but signs of recent strength.**

Whole economy pay growth



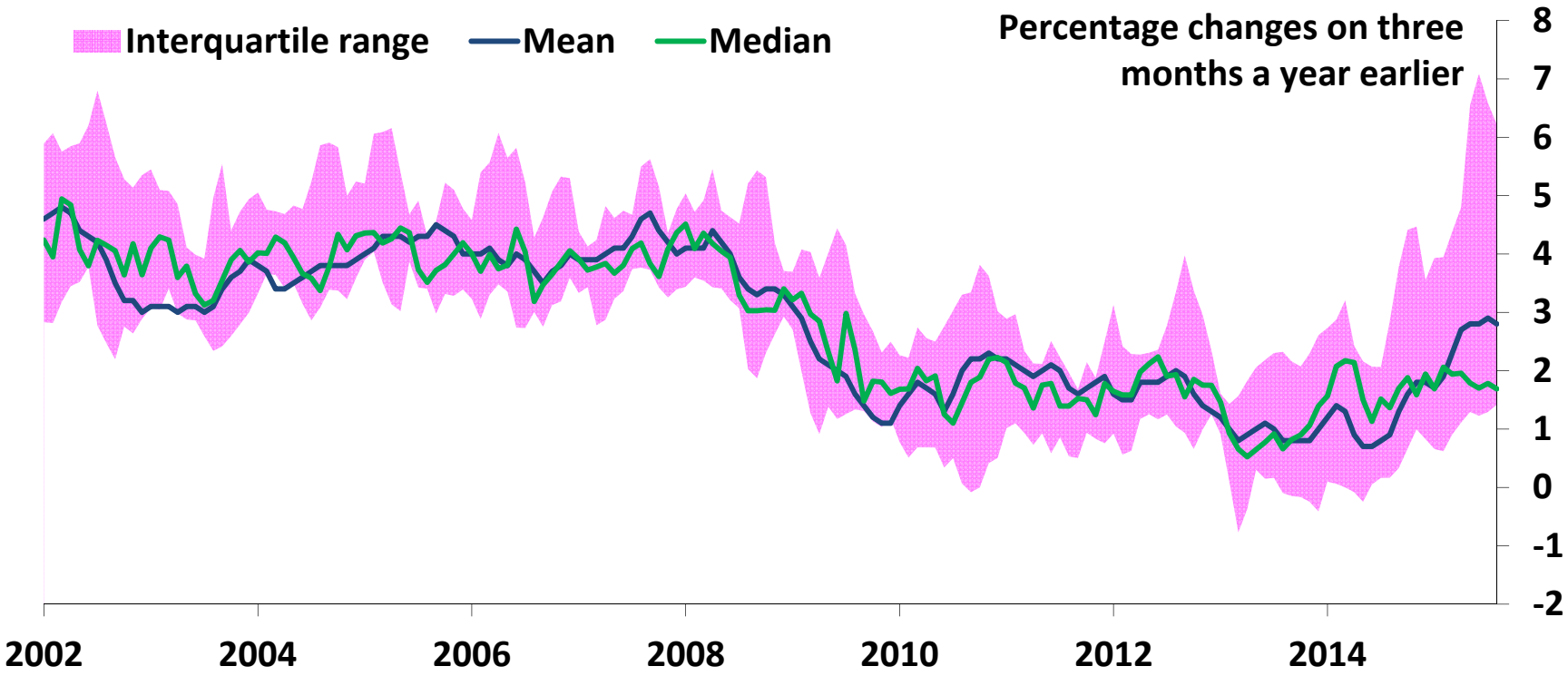
- **Regular pay growth 0.2pp weaker than expected in August.**

Whole economy regular pay growth



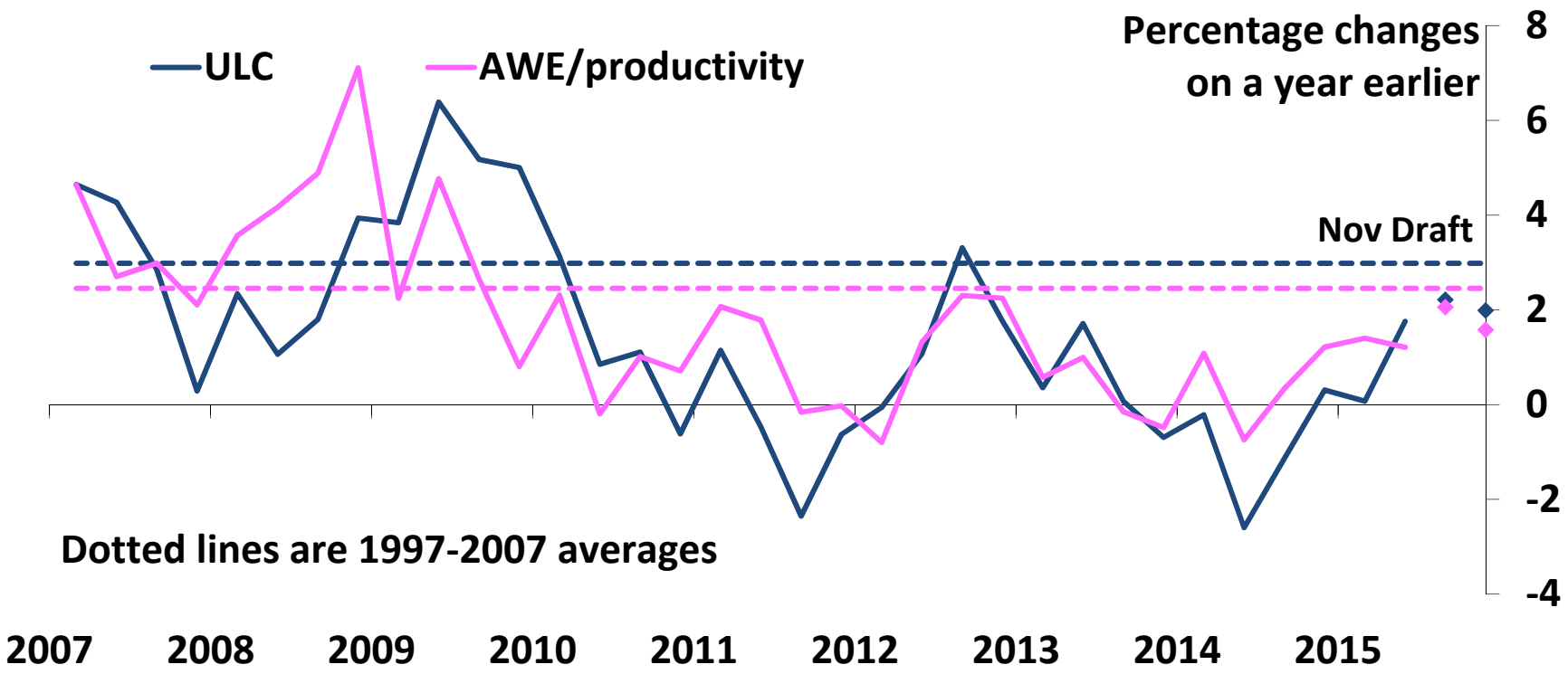
- **Annual regular pay growth has flattened off and is expected to fall a little by the end of the year.**

Distribution of regular pay growth by sector



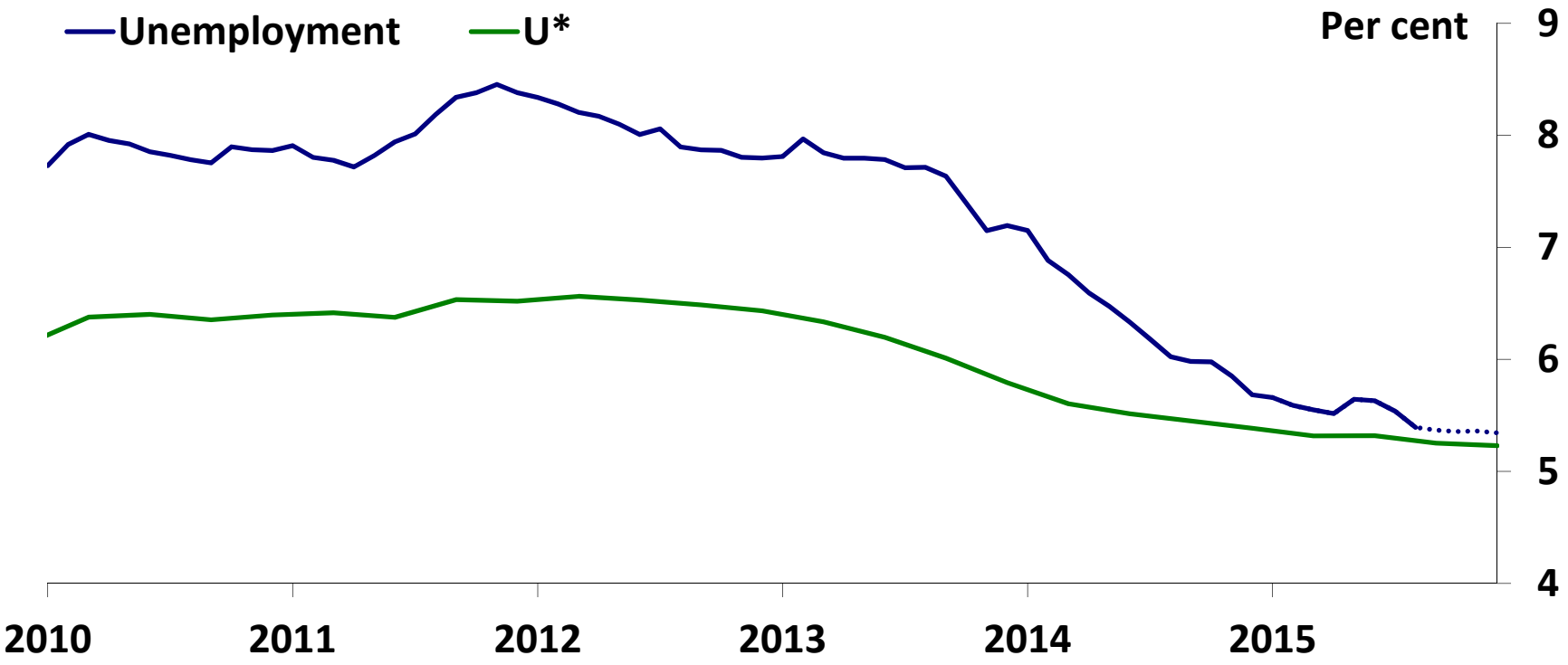
- **Sharp pick-up in regular pay growth in some sectors.**

Whole economy unit labour costs



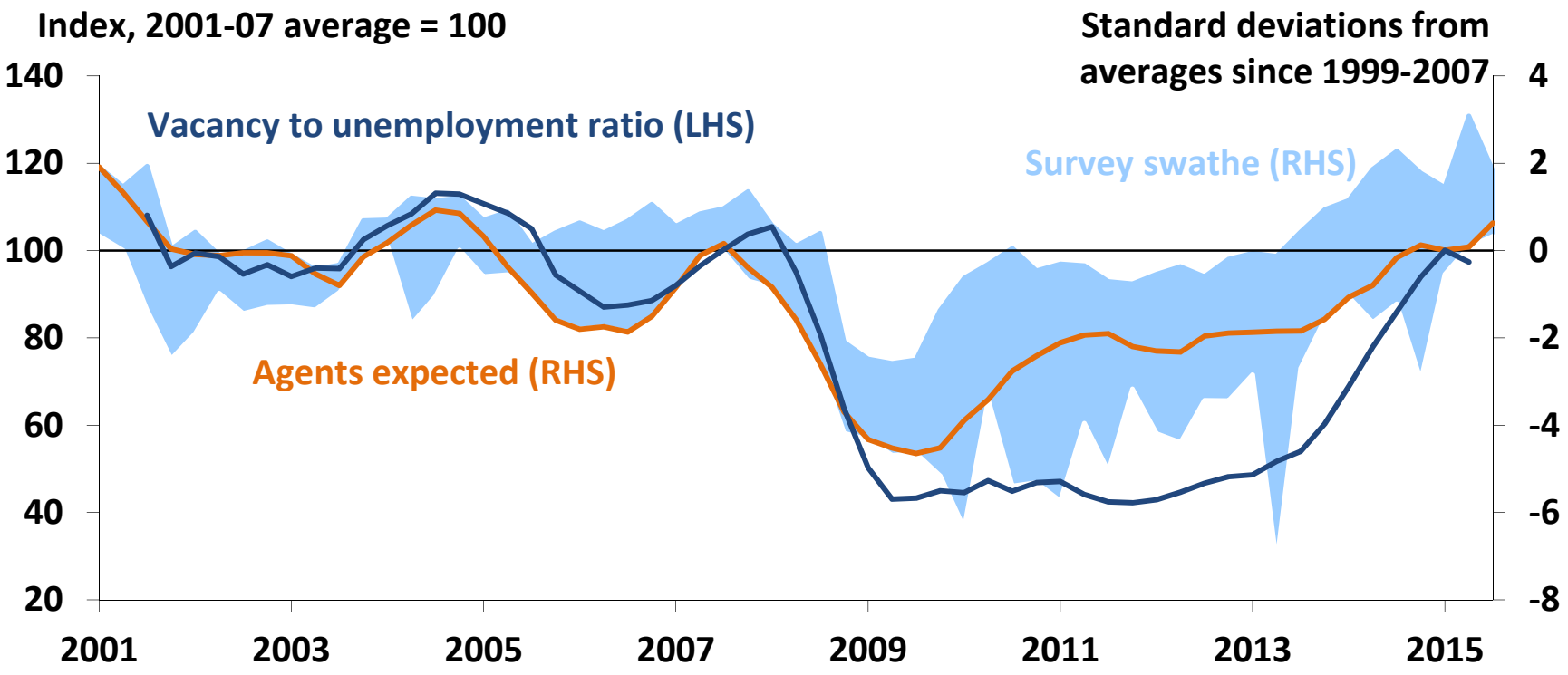
- **Wide dispersion of unit cost measures, but all remain subdued relative to pre-crisis averages.**

Unemployment rate



- **Unemployment down to 5.4%, close to U*.**

Recruitment difficulties



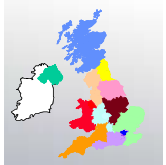
- **Surveys point to a tight labour market.**

Main messages

- **How confident can we be in the projected pickup in inflation?**
  - **Base effects from food and energy could add 1pp to inflation over the next year.**
  - **Core inflation projected to pick up only gradually but signs of recent strength.**
  - **Wage growth has flattened off, but the labour market looks increasingly tight.**

END

6: Agents’ Update



Agents' Update

28th October 2015

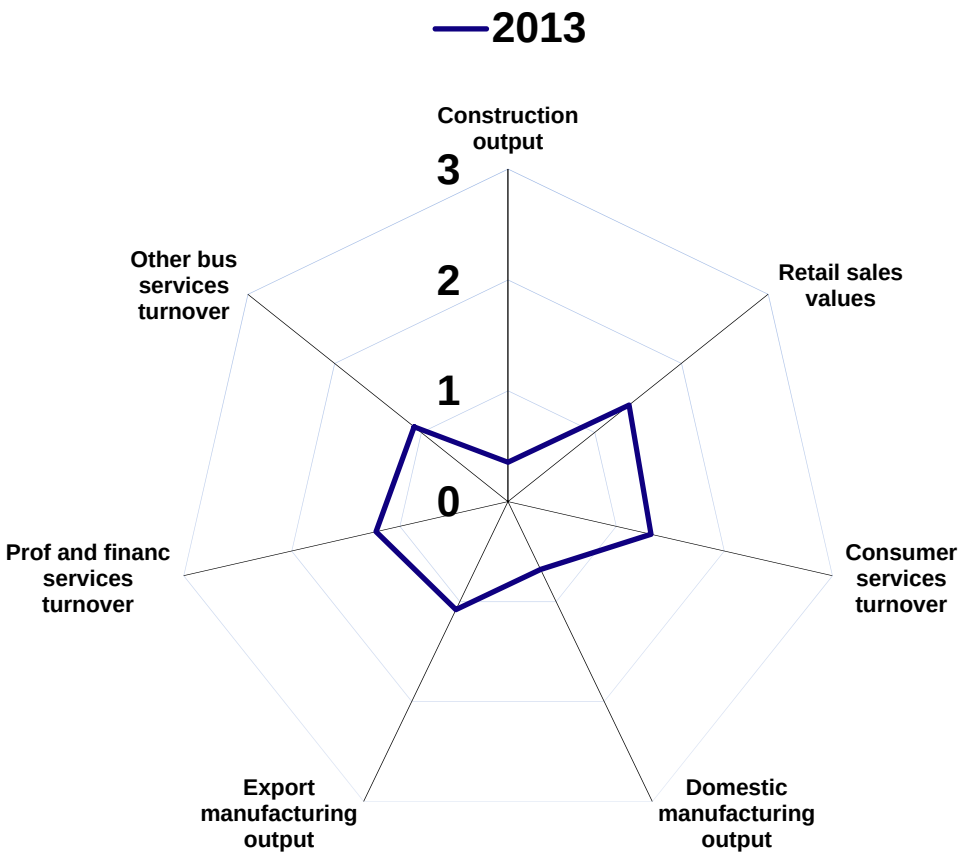
Agency for the North East
Inflation Report & Agency Intelligence Division

Topics

- **Activity**
- **Global demand**
- **Labour costs**

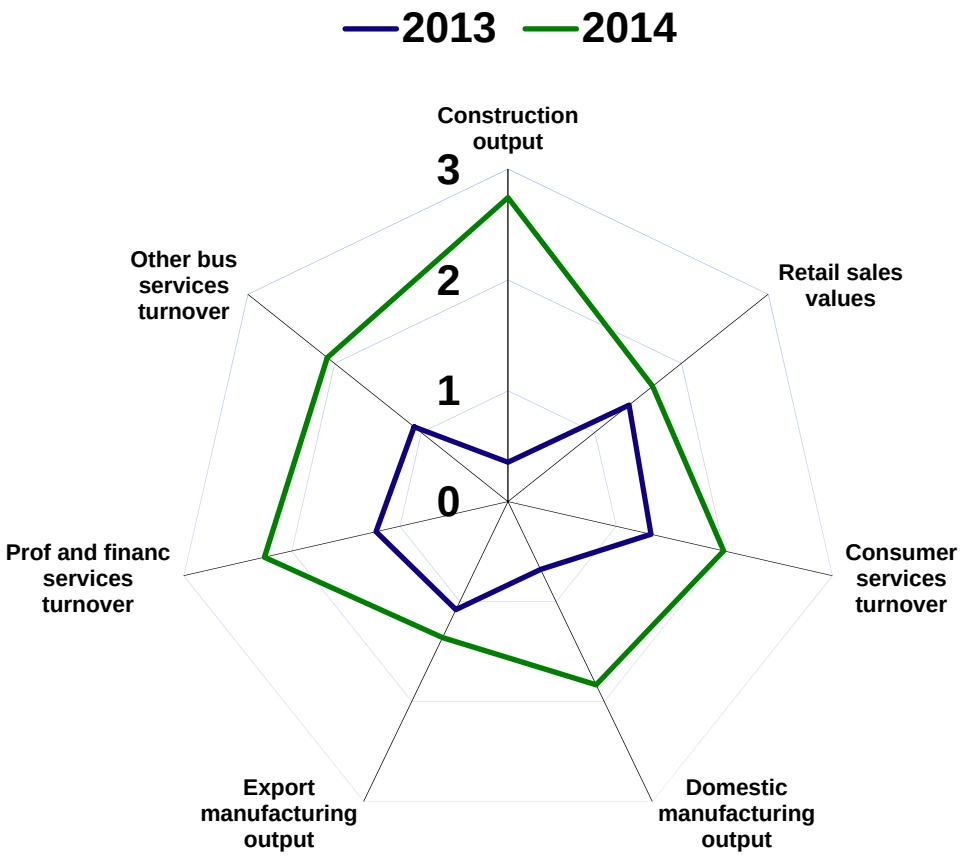
Agents' Growth Scores

Average annual scores



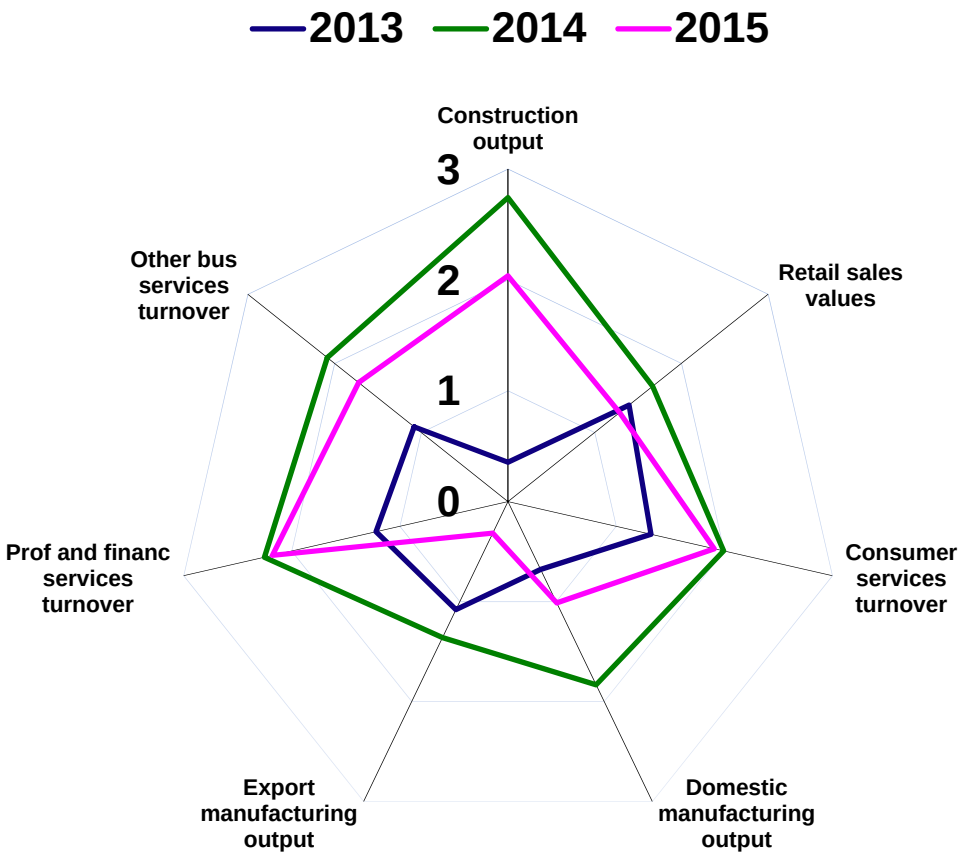
Agents' Growth Scores

Average annual scores



Agents' Growth Scores

Average annual scores



What's happening in manufacturing?

	Weak <- Not a more/less scale ->	Strong <- Not a more/less scale ->
Manufacturers for domestic market	Defence Domestic supply chain of weak exporters	Construction products Food & drink Scientific & medical equipment Automotive & caravans Home furnishings Aerospace & automotive supply chain
Exporters	Oil & gas supply chain Capital goods (for various sectors) Automotive Electronic components Steel	Aerospace & supply chain IT hardware

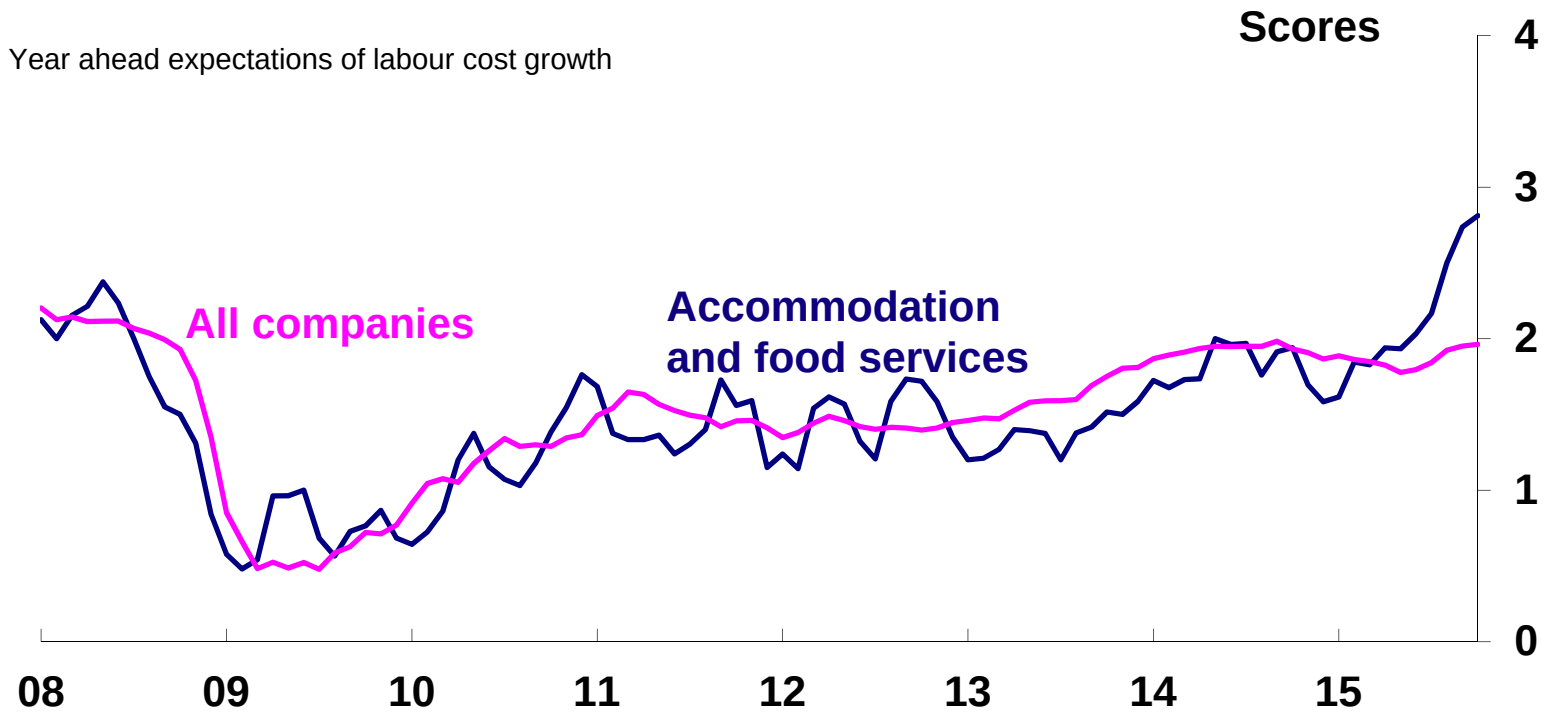
Global demand

- Exchange rate making it harder to compete against € manufacturers, offsetting gentle pickup in € area demand
- Slowdown concentrated in EMEs; BRICs and Middle East…
- …mainly in exports of capital goods related to extraction

Labour costs

- Modal pay settlements in 2-3% range and expected to remain there next year
- Retention and recruitment difficulties key justification for higher settlements
- Increased focus on finding productivity gains
- Early evidence of NLW pushing up *expected* labour cost growth in most exposed sectors

Company Visit Scores: Expected Labour Costs



Summary

- Growth slower in 2015 than 2014
- Export-oriented contacts slowing most (but spreading)
- …driven by subdued world growth and earlier appreciation of sterling
- Apart from NLW, pay increases expected to be little changed over coming year
- But recruitment difficulties indicate upwards pressure in some sectors