

**Bank of England**

# Recent developments in UK monetary policy

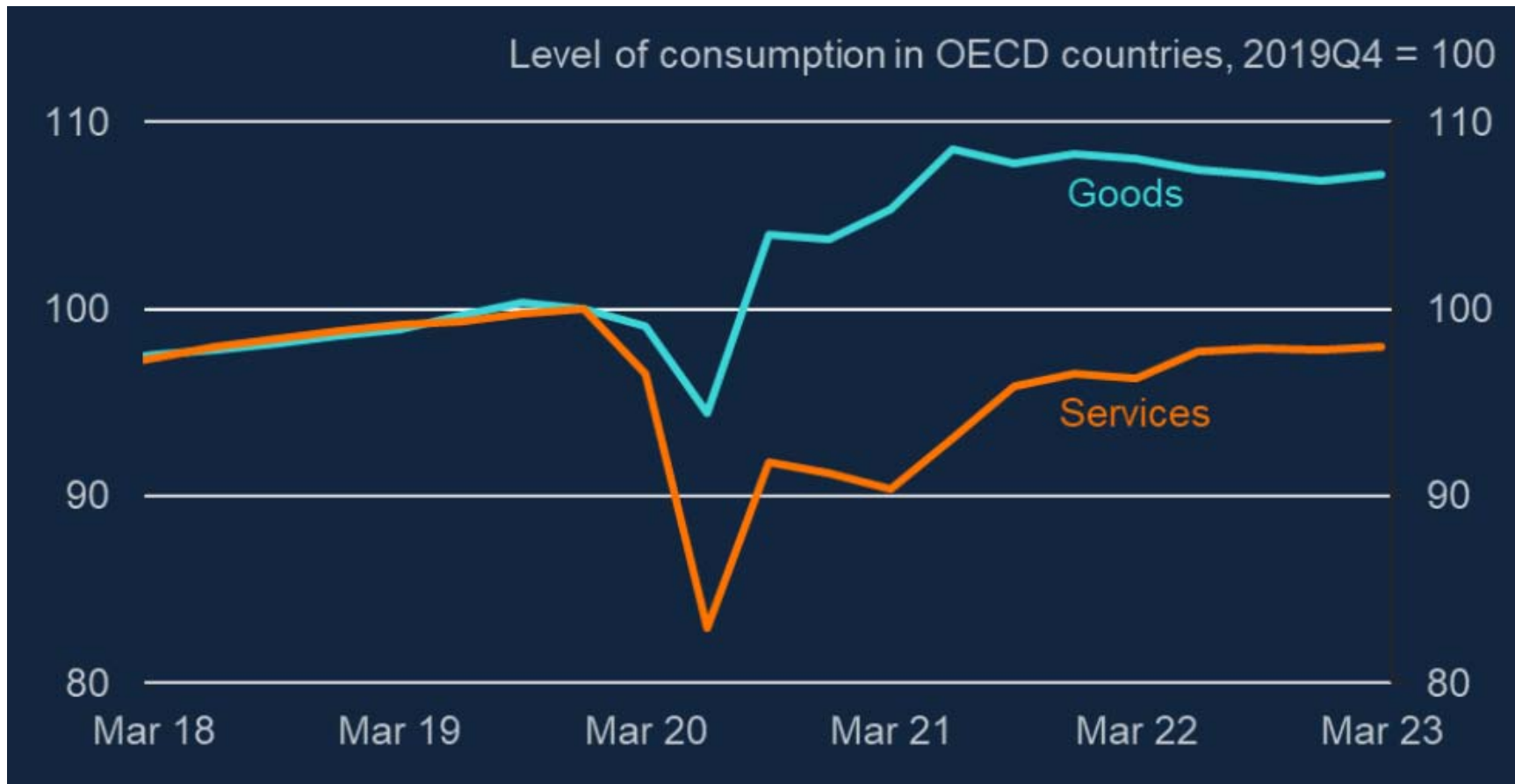
South African Reserve Bank Biennial Conference  
Cape Town, South Africa

**Huw Pill**

31 August 2023

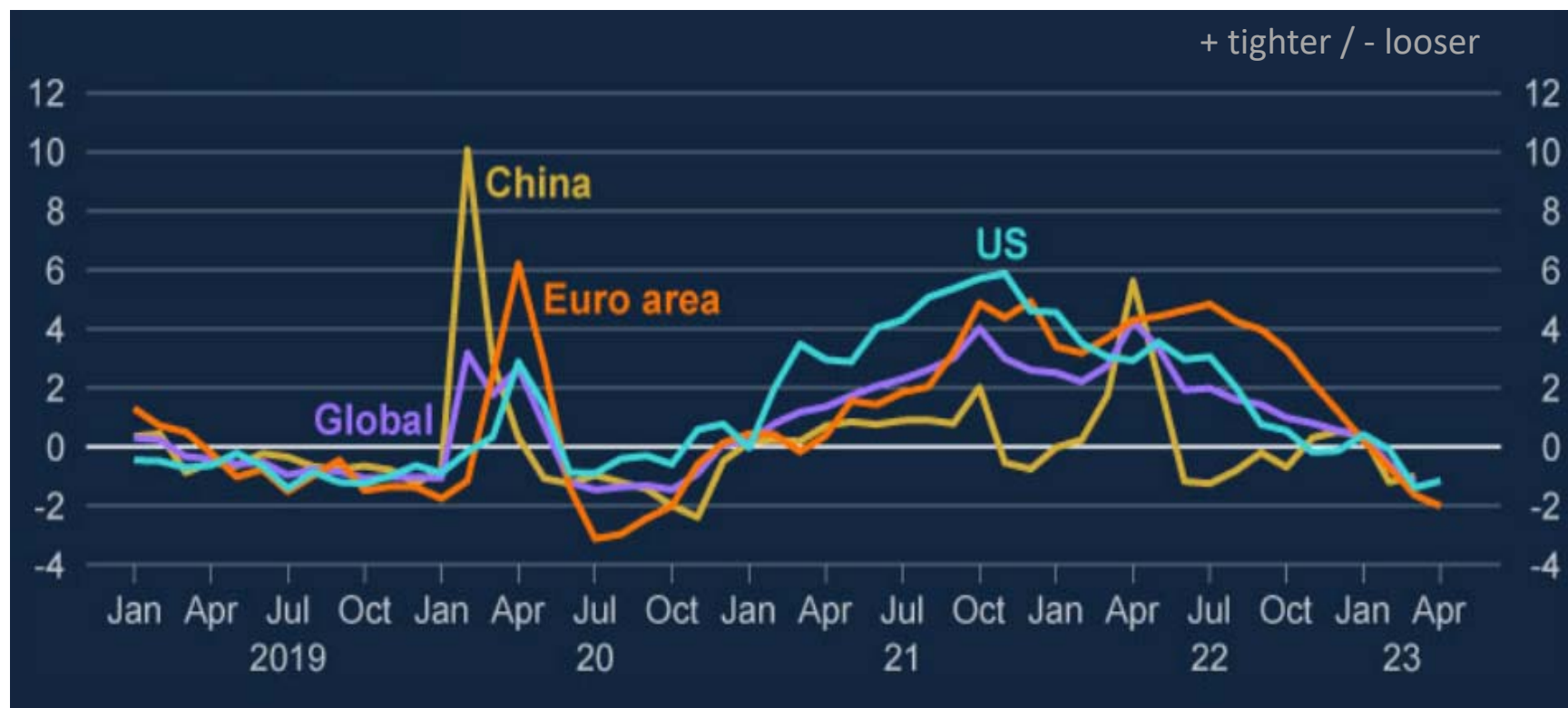


## Pandemic altered patterns of global demand ...



Sources: OECD Quarterly National Accounts, IMF World Economic Outlook and Bank of England calculations

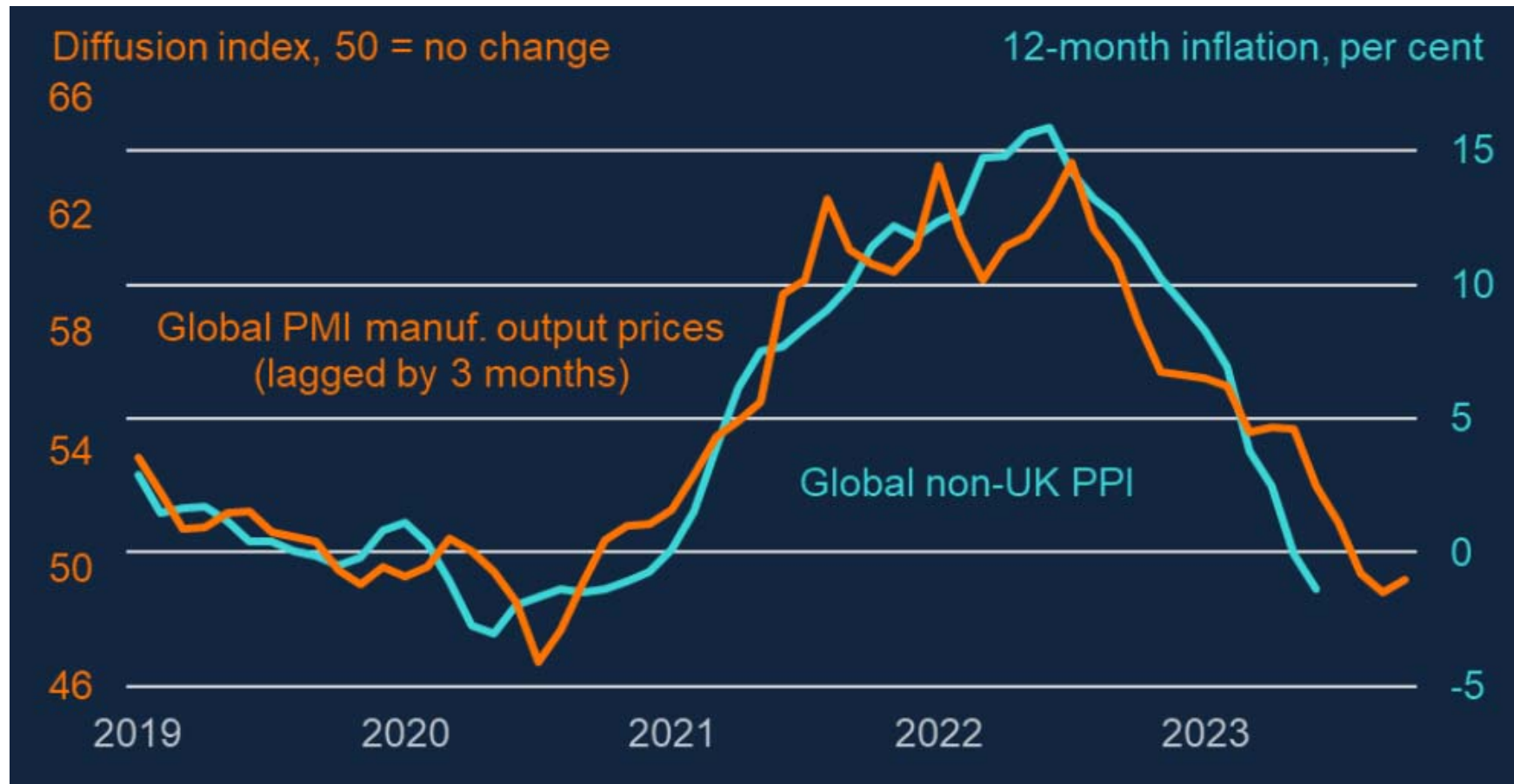
... as well as constraining global supply, particularly for goods



Sources: Refinitiv Eikon from LSEG, S&P Global/CIPS and Bank of England calculations

Notes: Indicators are estimated by Bank staff using principal component analysis on a range of PMIs for supply constraints in the manufacturing sector (supplier delivery times, stocks of purchases, stocks of finished goods, input prices and backlogs of work). Before principal components are estimated, these indicators are regressed on the new orders PMI to control for movements in demand. Latest data for the Global and China series are for March 2023, and April 2023 for the US and the euro-area series

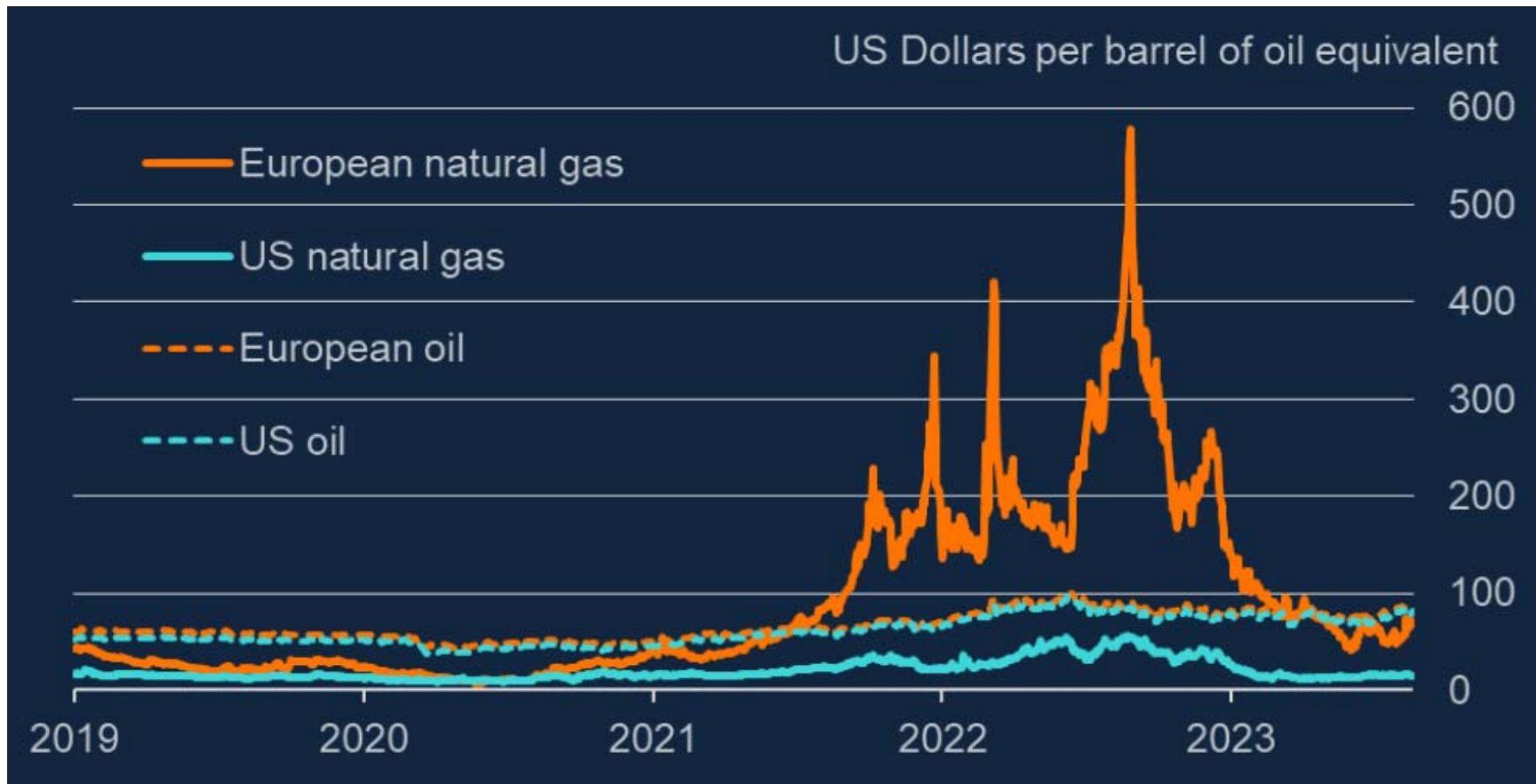
## Global goods inflation rose owing to bottlenecks



Source: Refinitiv Eikon Datastream, JPM Global PMI index and Bank of England calculations

Notes: 'Global non-UK PPI' is the average of PPIs from the Euro area (manufacturing PPI), US, China, Switzerland, India, Poland, Japan, Hong Kong, Sweden, Canada, South Africa, Denmark, South Korea and Singapore, weighted by their shares of UK imports. These economies account for over 90% of UK imports

## Significant shock to European wholesale natural gas prices

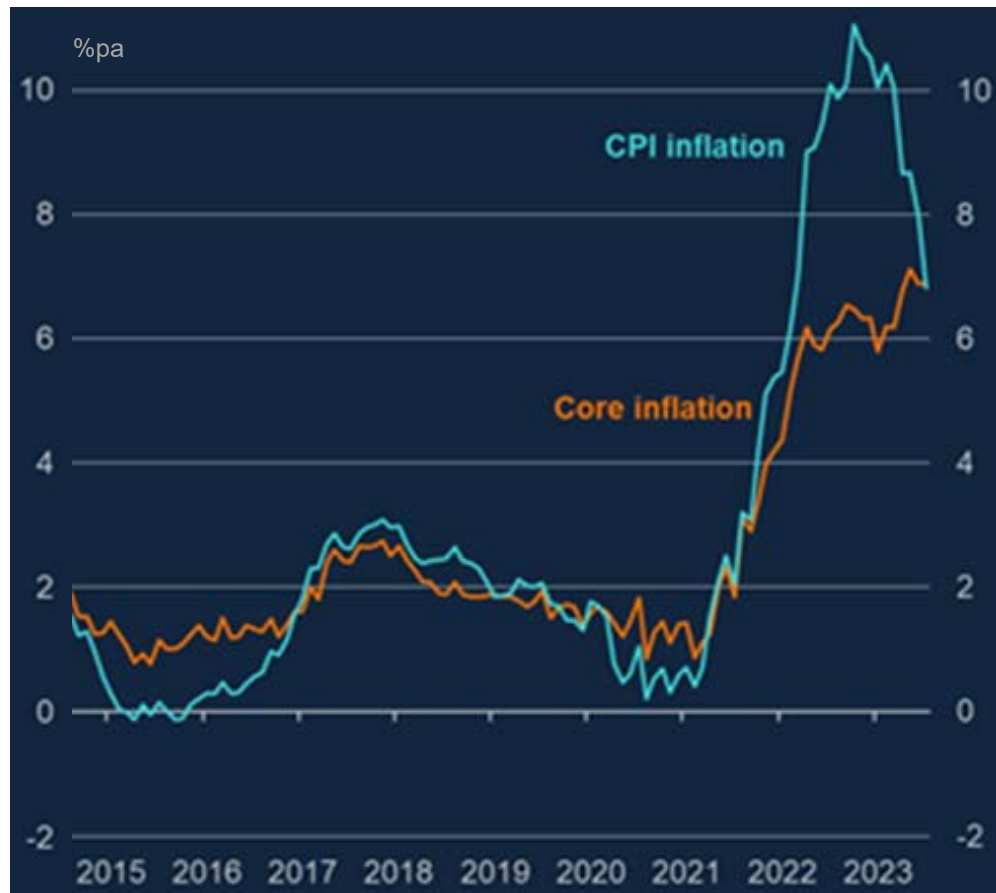


Sources: Bloomberg Finance L.P. and Bank of England calculations.

Notes: US gas is Henry Hub natural gas; European gas is Dutch TTF natural gas. US oil is West Texas Intermediate crude; European oil is Brent crude

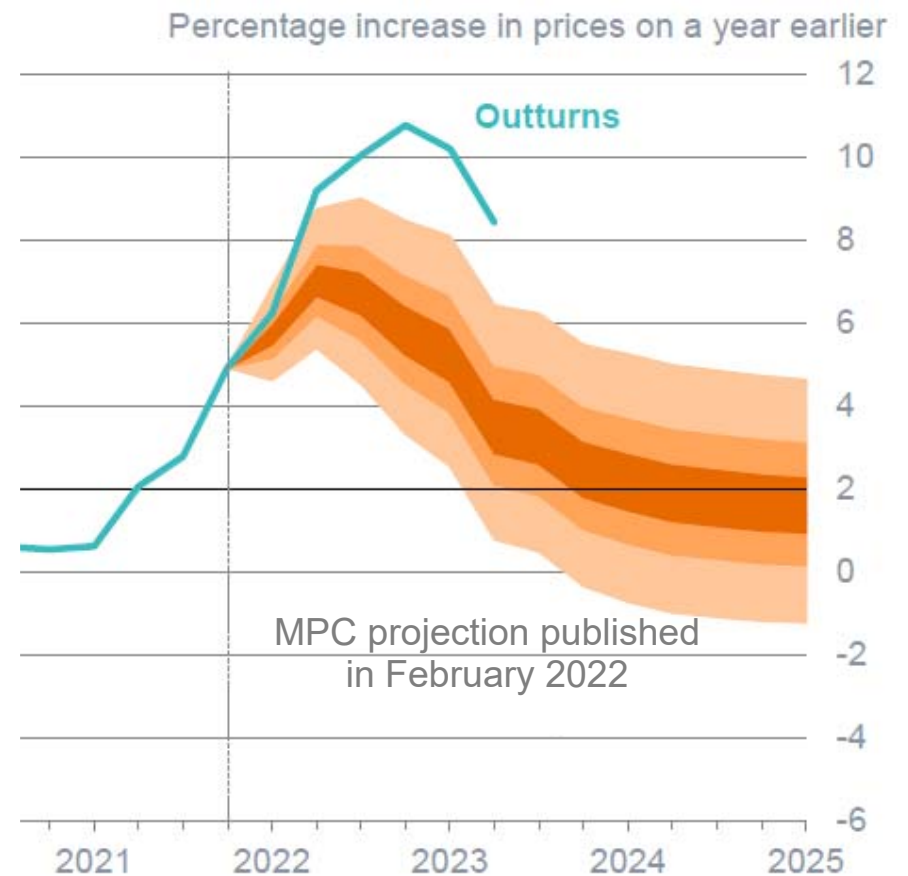


## UK CPI inflation overshoots target – how persistently?



Sources: ONS and Bank of England calculations.

Notes: Core inflation excludes the energy, food and non-alcoholic beverage prices



## Changes in price setting behaviour for goods?

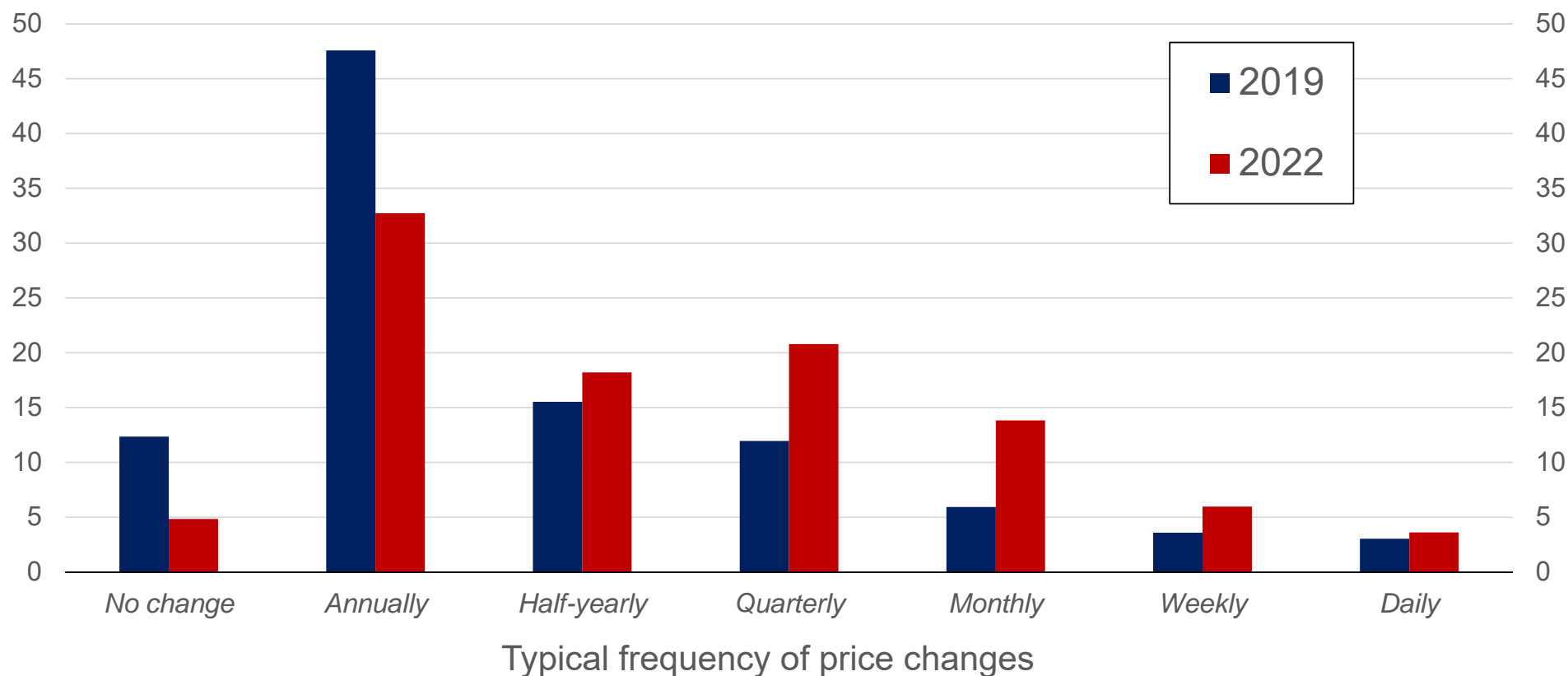


Sources: ONS and Bank of England calculations

Notes: Core output PPI is for manufactured products excluding non-core items

# Survey evidence on frequency of firm pricing decisions

Percentage of businesses, %

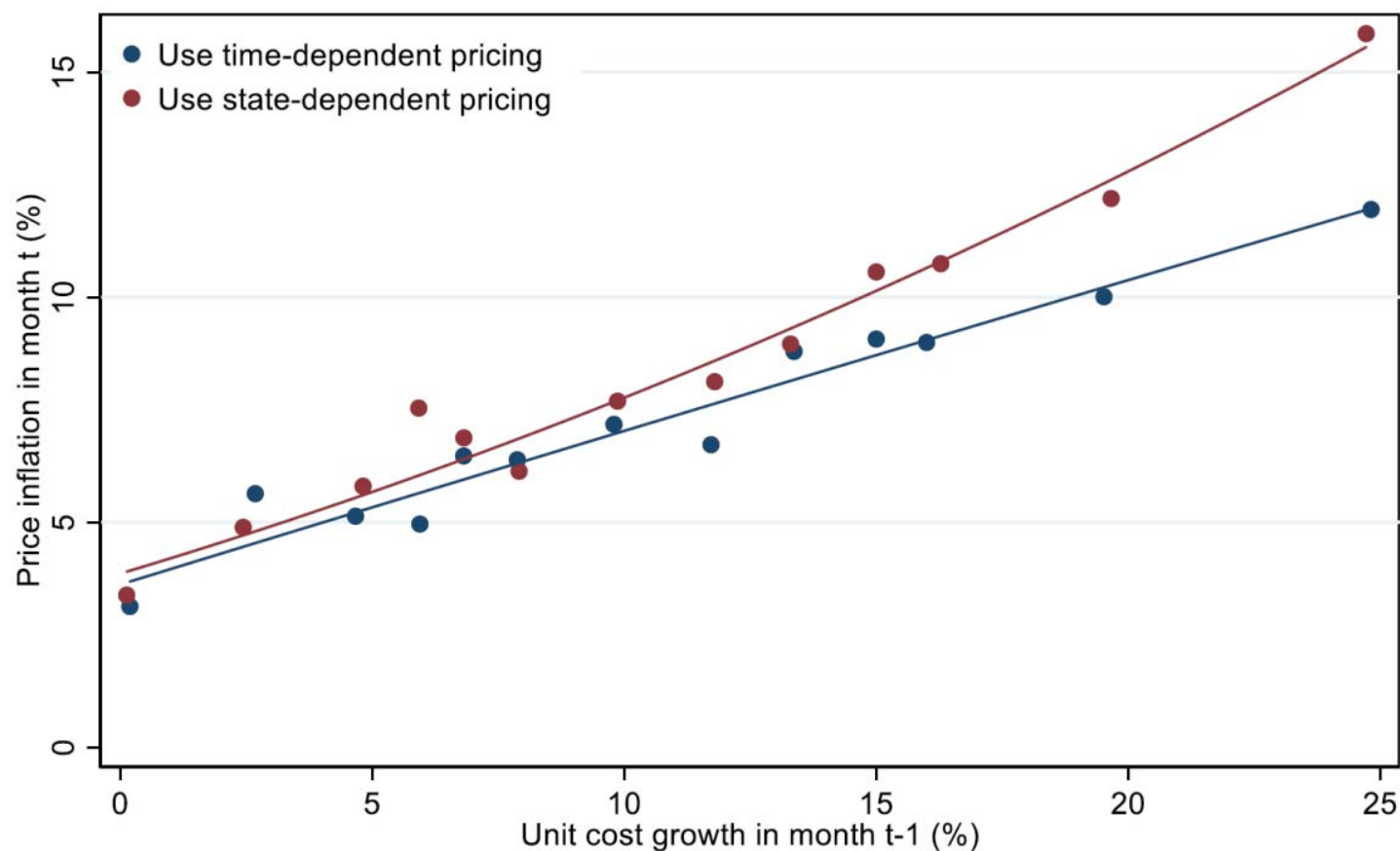


Sources: Decision Maker Panel survey and Bank of England calculations

Notes: The latest data are from the May 2023 Survey. The results on frequency of price changes are based on the question: 'Approximately how often did your prices change in each of the following years?'. Respondents were then asked to choose one of the following options for both year 2019 and 2022: daily, weekly, monthly, quarterly, half-yearly, annually, and prices did not change.



# Sensitivity of firm pricing decisions to cost shocks

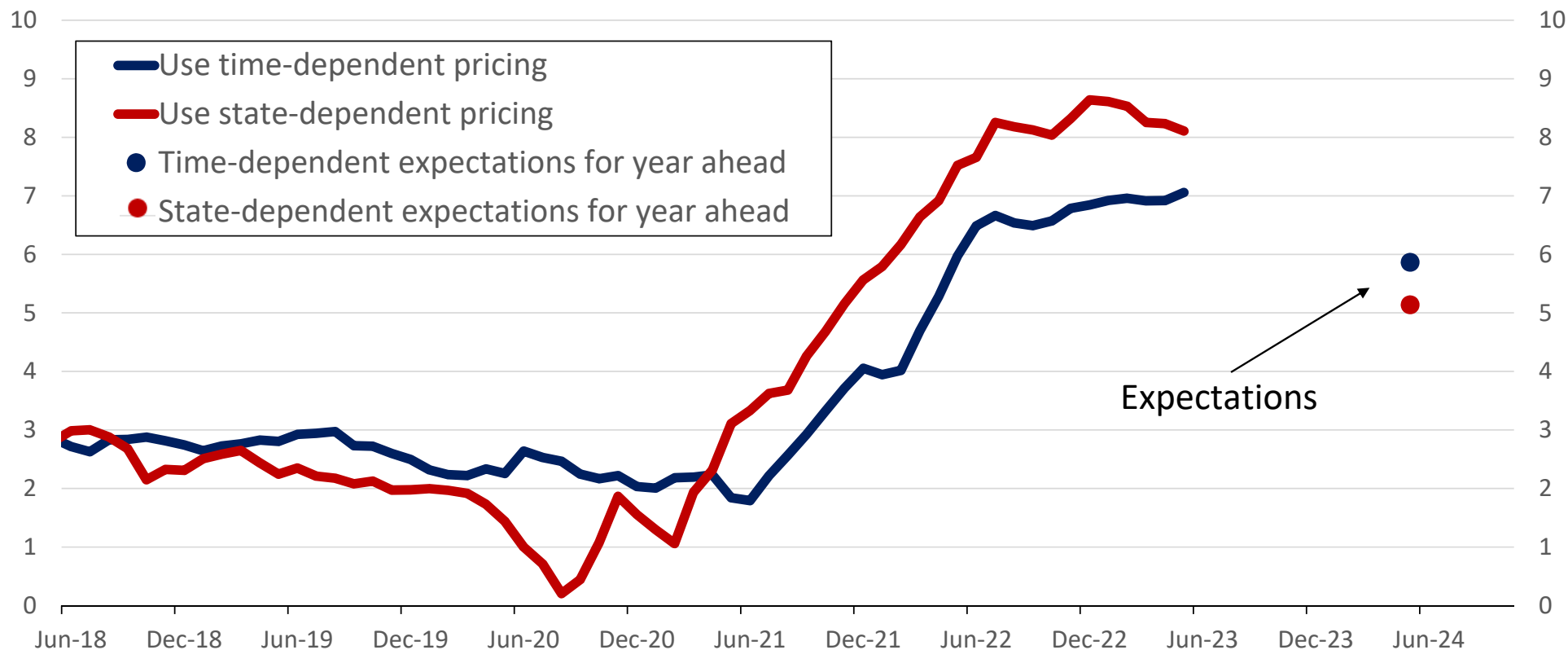


Sources: Decision Maker Panel survey and Bank of England calculations

Notes: The latest data are from the May 2023 Survey. Question wording – ‘Which of the following best describes how your business usually sets prices?’; (i) ‘Mostly change prices in response to specific events (e.g. changes in costs or demand)’ (= state-dependent pricing); (ii) ‘Mostly change prices at fixed intervals (e.g. once a year or once a quarter, etc.)’ (= time-dependent pricing)

# Survey evidence points to change in firm pricing expectations

Per cent, %



Sources: Decision Maker Panel survey and Bank of England calculations.

Notes: Three-month moving averages. Realised price growth (lines) are responses to the question: 'Looking back, from 12 months ago to now, what was the approximate % change in the average price you charge, considering all products and services?'. The latest data are from the May 2023 Survey. Expected price growth (diamonds) are responses to the question: 'Looking ahead, from now to 12 months from now, what approximate % change in your average price would you expect in each of the following scenarios: lowest, low, middle, high and highest?', and respondents are asked to assign a probability to each scenario which is used to create a weighted average expectation of price growth..

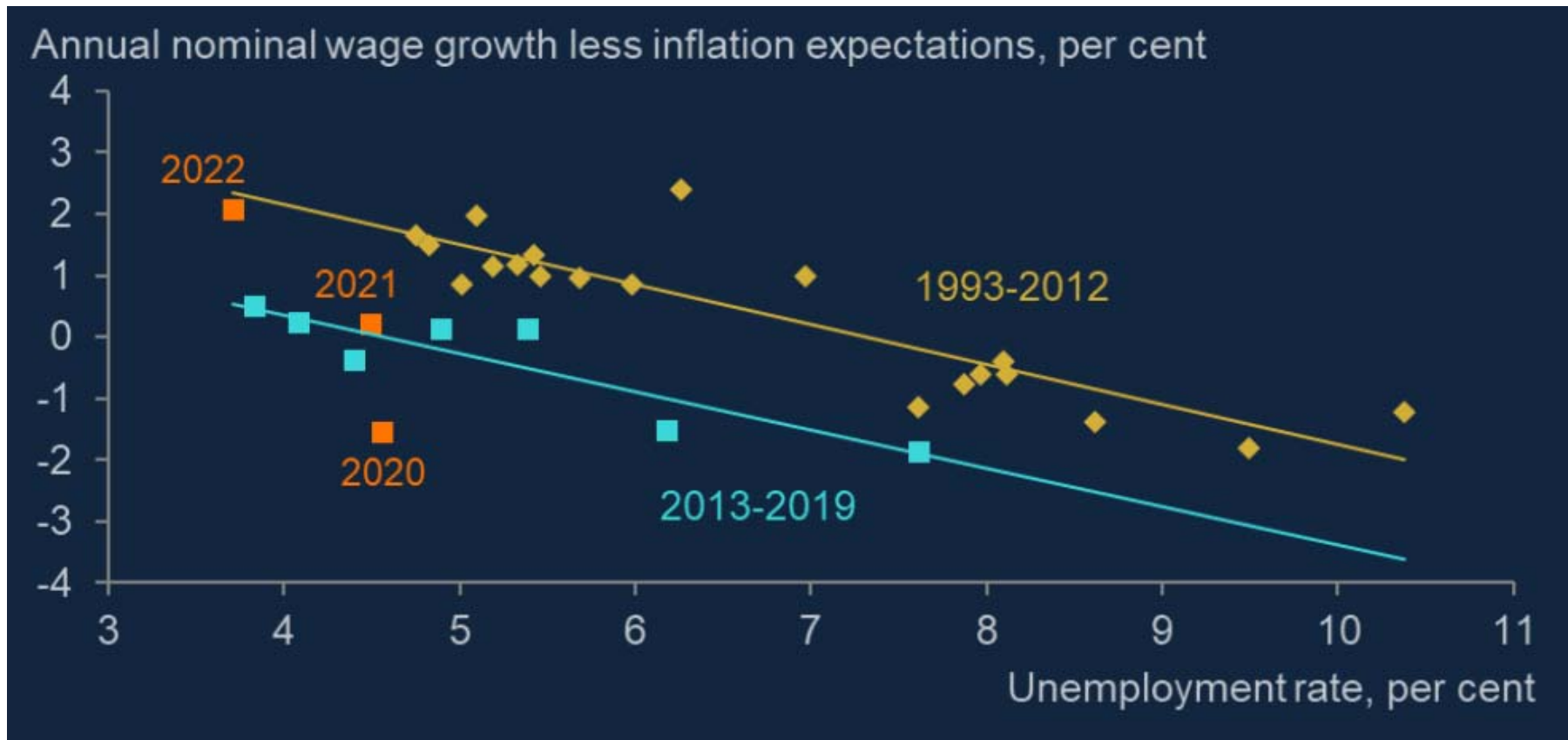
## Changes in wage setting / pricing behaviour for services?



Sources: ONS, Recruitment and Employment Confederation (REC) and Bank of England calculations

Notes: Wages are Average Weekly Earnings (AWE) private sector regular pay; 'underlying' measure removes pandemic-related compositional effects. REC indicator of staff permanent staff salaries is mean-variance adjusted to match wage growth over 2002-19. REC indicator 12-month lag gives best correlation with 12-month wage growth over 2002-19

## Changing slope of the wage Phillips curve



Sources: ONS and Bank of England calculations

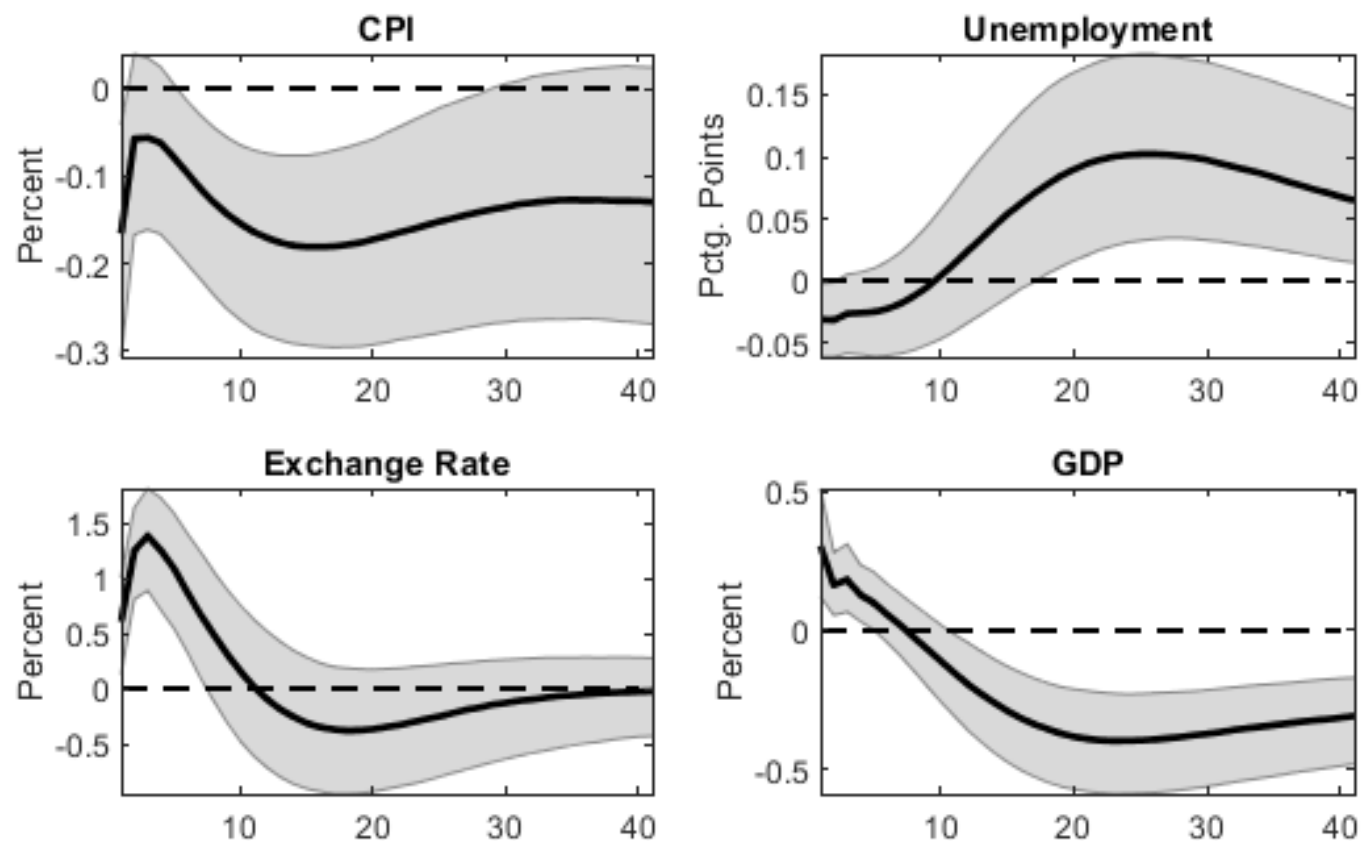
Notes: Wage growth is Average Employee Income (AEI) until 2010 and Average Weekly Earnings (AWE) since. Inflation expectations are implied by the indexed gilt market.

# Greater dispersion across firms' pricing and wage setting



Sources: Decision Maker Panel (DMP) survey and Bank of England calculations

# Monetary policy transmission in the UK

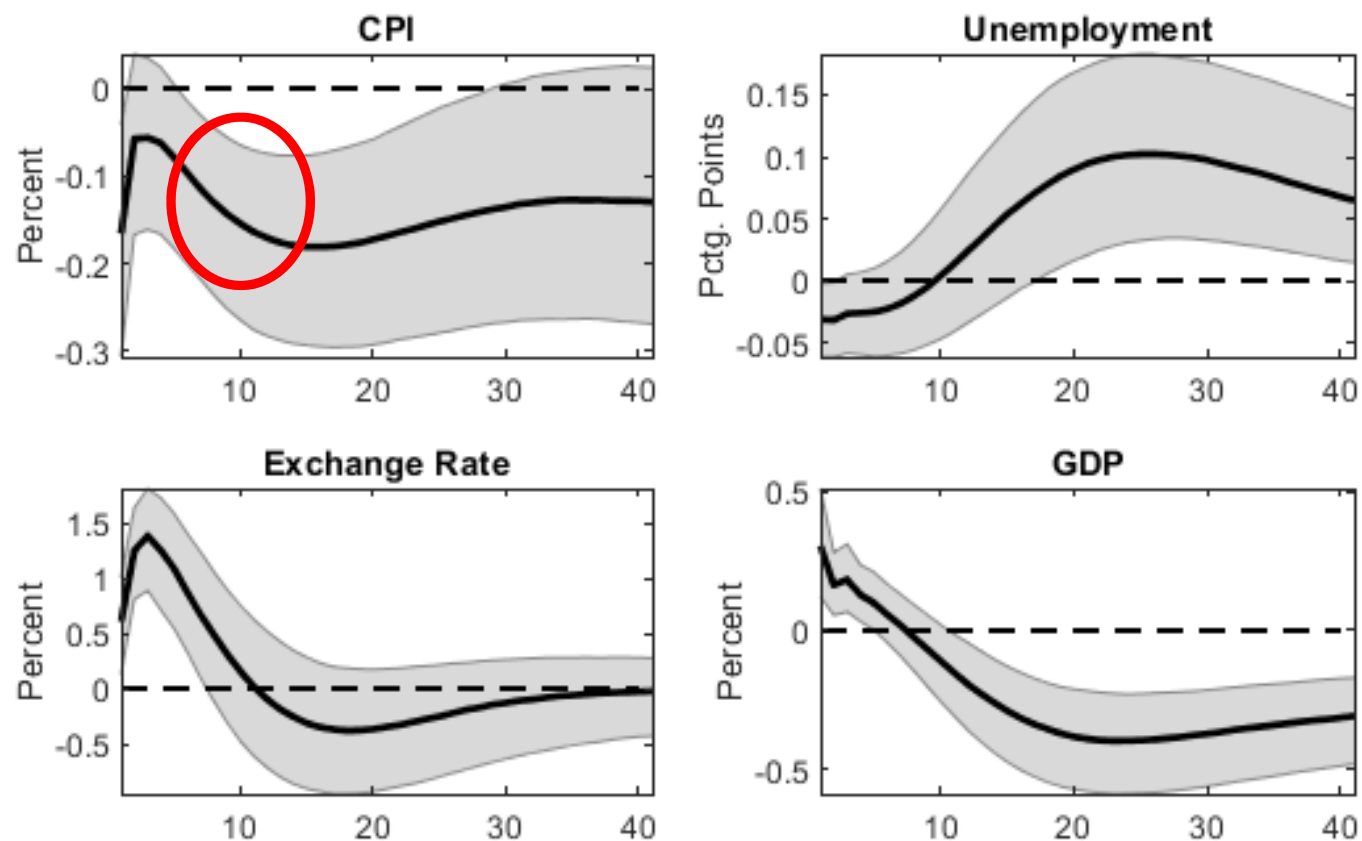


Sources: Cesa-Bianchi, Thwaites and Vicondoa (2020) and Bank of England calculations

Notes: Thanks to Mauricio Salgado Moreno for his work in updating these estimates and comparing across different sample periods. The estimates shown here are derived from a sample period until end-2019. The charts show local projections of monetary policy shocks identified using the innovation in the second short-term interest rate future in a narrow window around the announcement of monetary policy decisions. The model is estimated in levels using monthly data



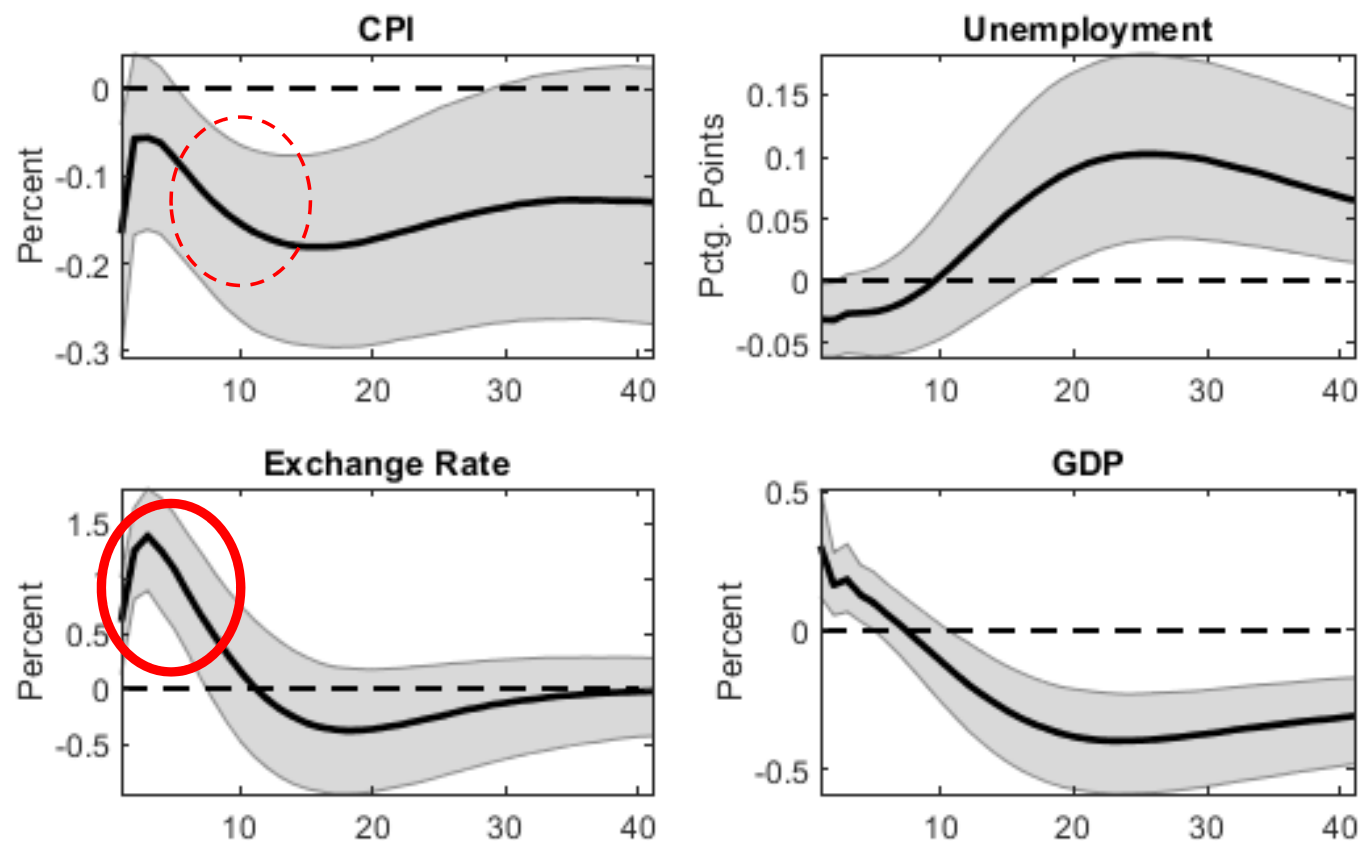
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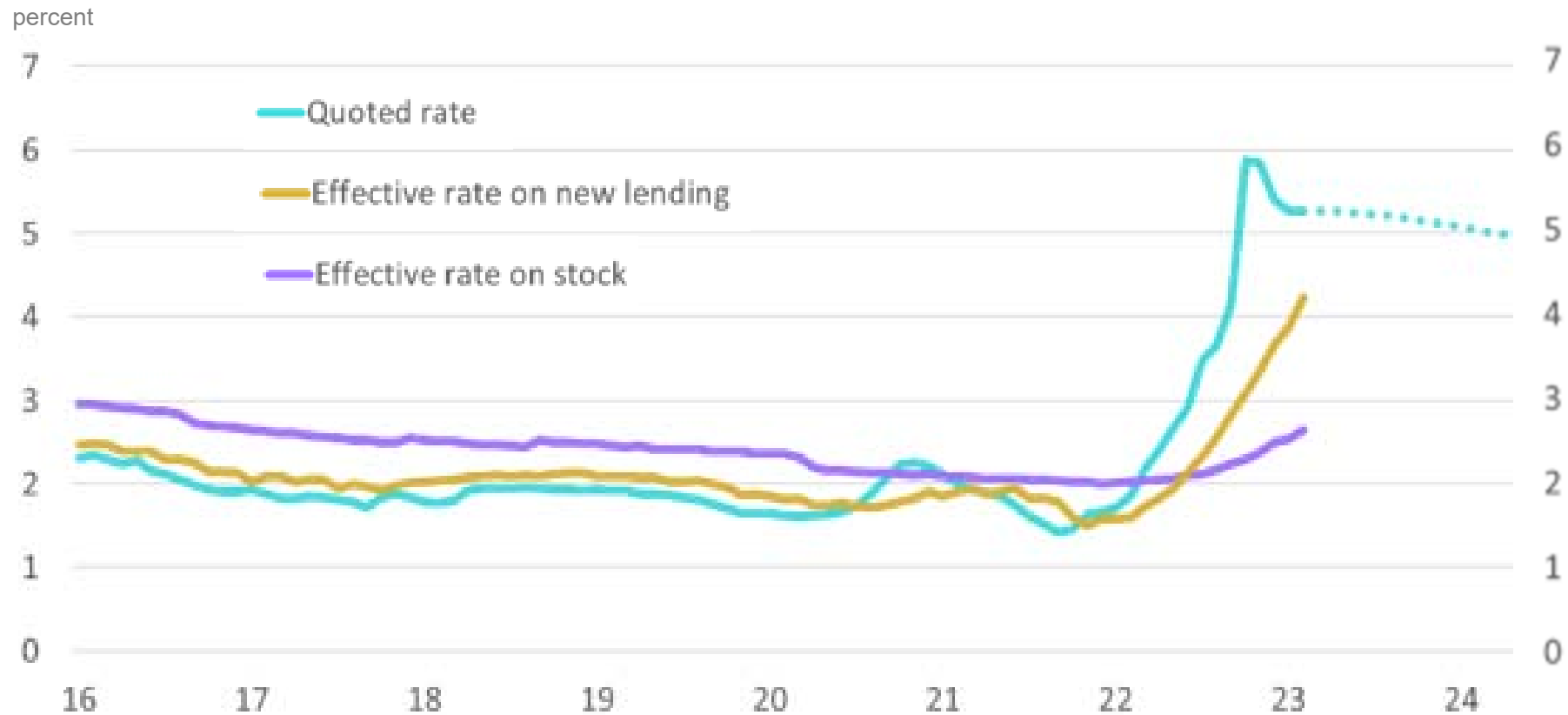
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## Changing structure of UK mortgage market (1)

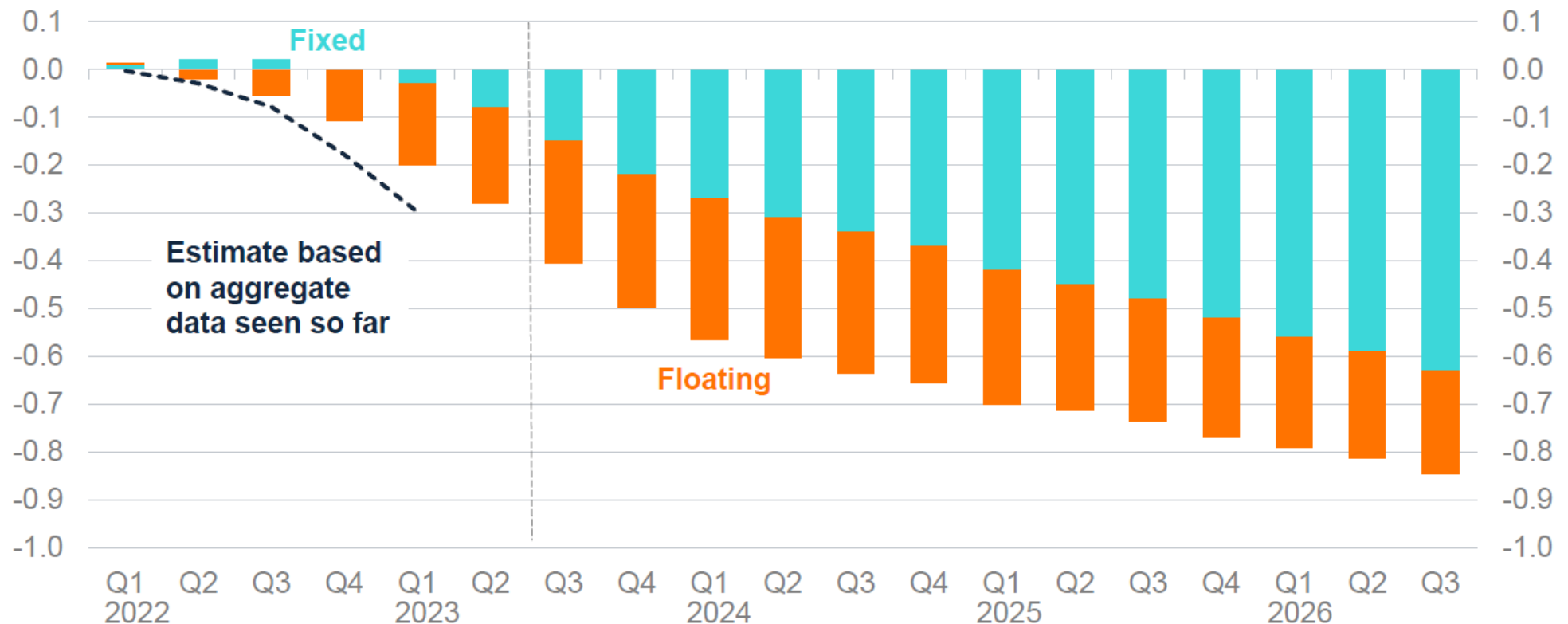


Sources: Bank of England calculations

## Changing structure of UK mortgage market (2)

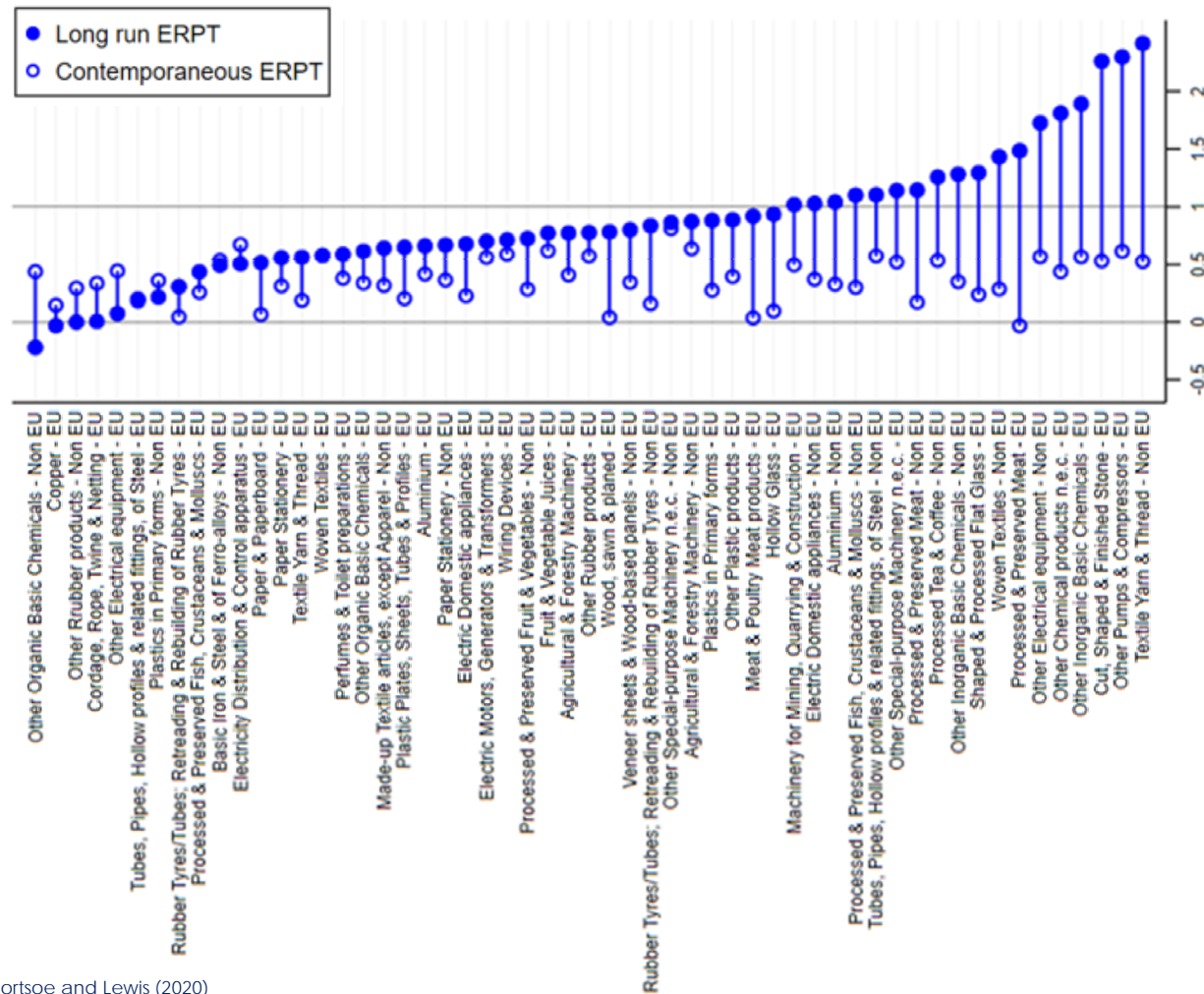
### Impact of change in Bank Rate on mortgage payments, % of consumption

*(based on micro cash-flow analysis)*



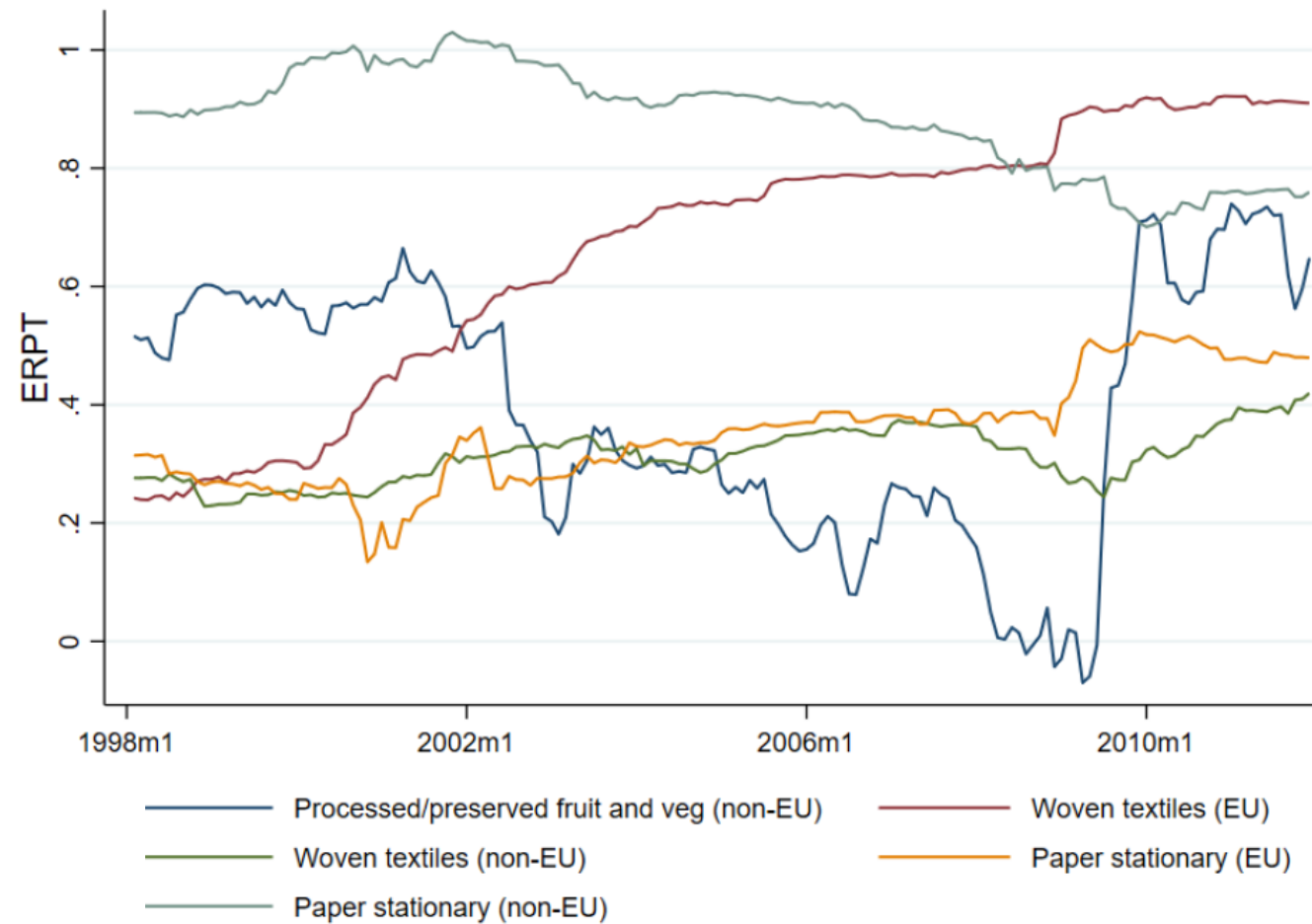
Sources: Bank of England calculations

# Deep dive into FX pass-through sector-by-sector



Source: Hjortsoe and Lewis (2020)

## Time variation in FX pass-through by sector

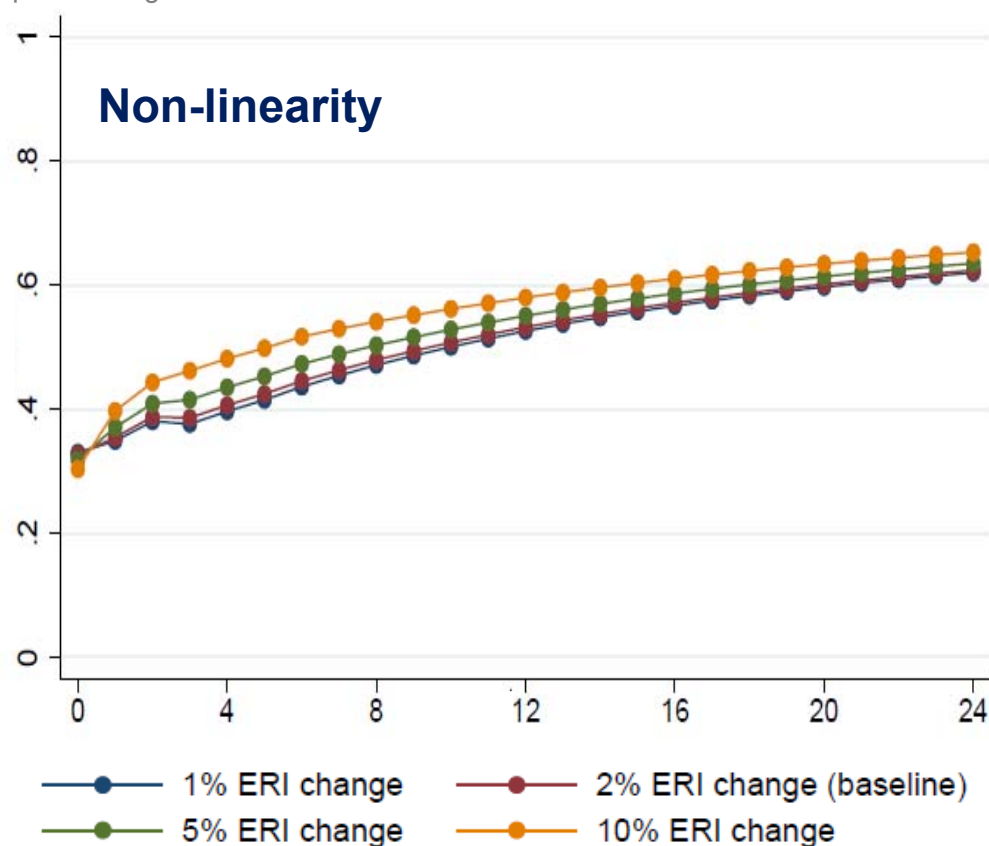


Source: Hjortsoe and Lewis (2020)

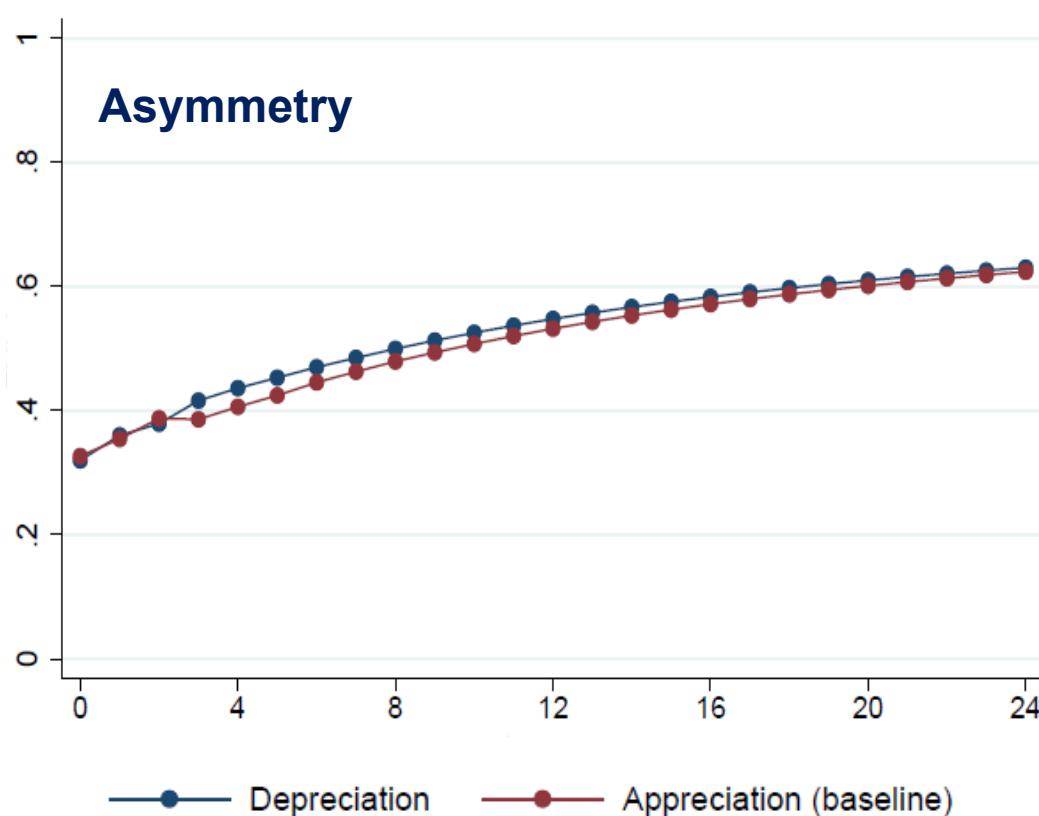


# Non-linearities and asymmetries in FX pass-through in aggregate

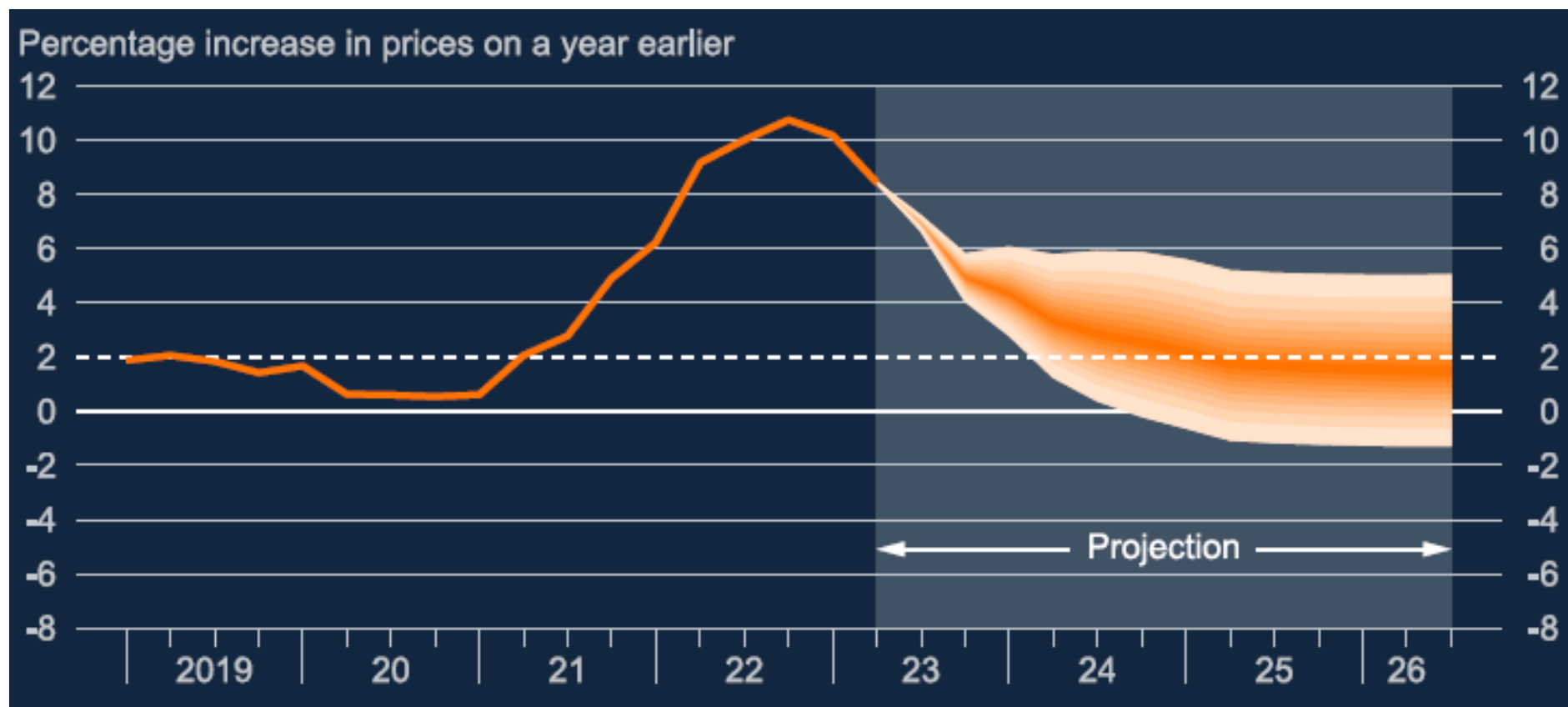
pass-through



pass-through

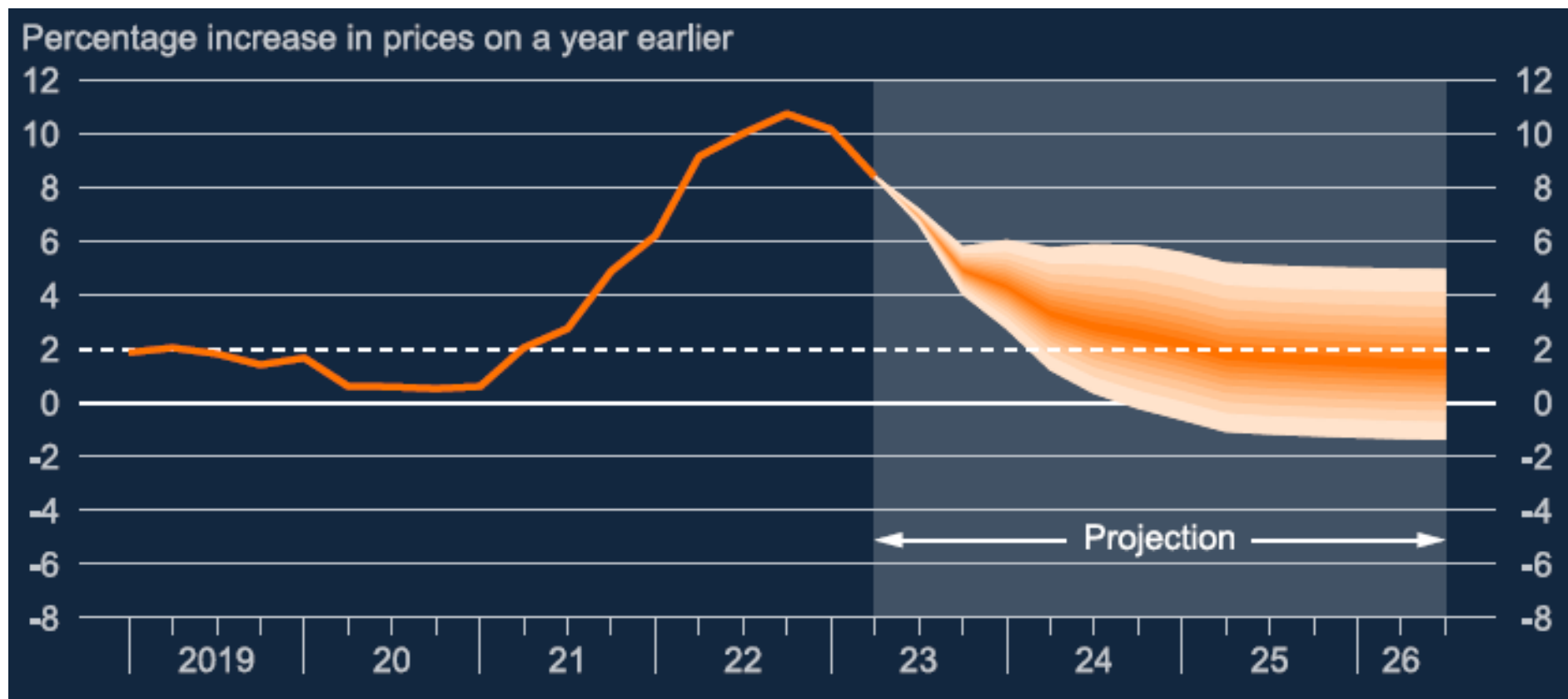


## Inflation outlook under market-implied path for Bank Rate – peaking just above 6% in mid-2024, falling to 4½% in mid-2026



Sources: MPC Monetary Policy Report (August 2023) and Bank of England calculations

## Inflation outlook under constant path of Bank Rate – at 5.25% throughout the forecast period



Sources: MPC Monetary Policy Report (August 2023) and Bank of England calculations



## References

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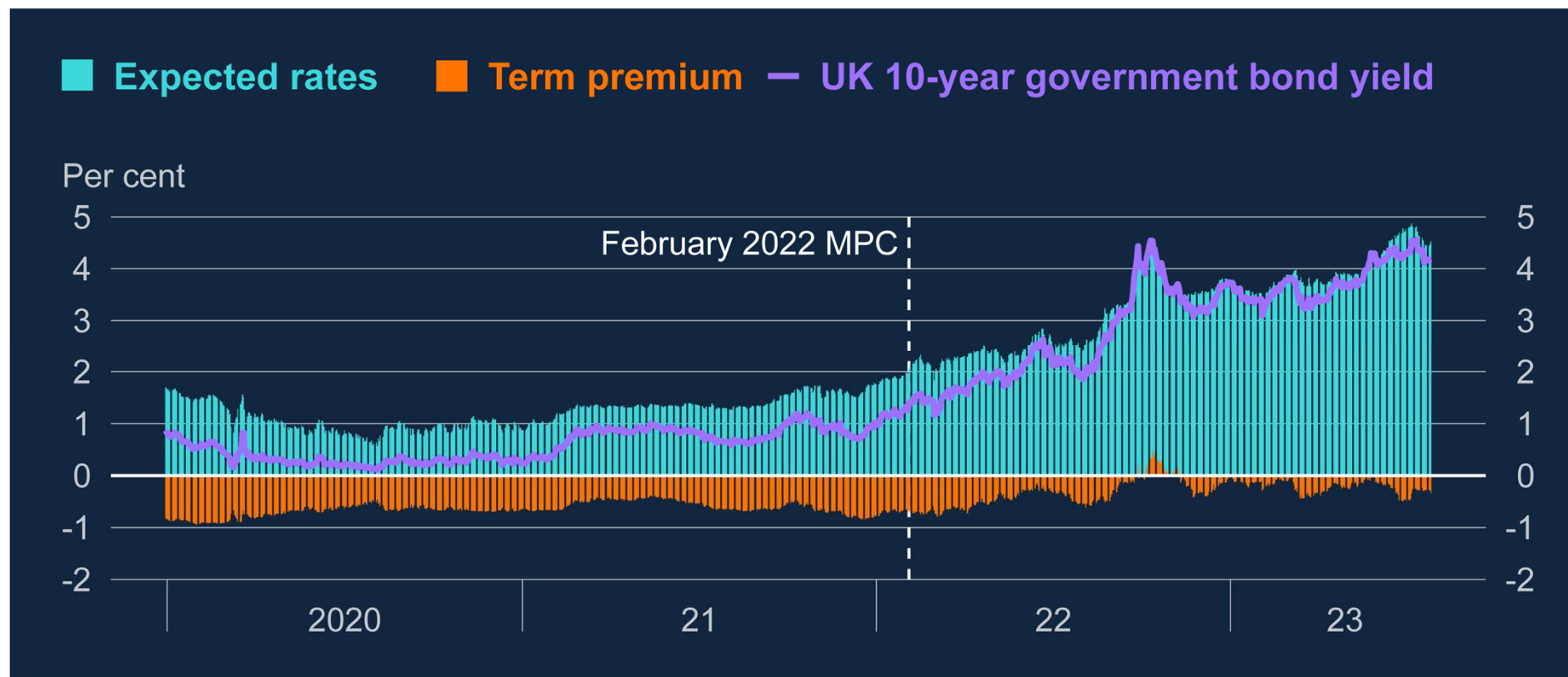
Cesa-Bianchi, A., G. Thwaites and A. Vicendoa (2020). **"Monetary policy transmission in the United Kingdom: A high frequency identification approach"**, *European Economic Review* 123(C).

Hjortsoe, I. and J. Lewis (2020). **"Non-linearities, asymmetries and dollar currency pricing in exchange rate pass-through: Evidence from the sectoral level"**, Bank of England staff working paper no. 868.

Pill, H. (2023a). **"Recent experience with macroeconomic forecasting for UK monetary policy"**, contribution to the conference volume of ECB Sintra forum volume, forthcoming.

Pill, H. (2023b). **"Inflation persistence and monetary policy"**, ICMB Lecture, Graduate Institute, Geneva.

## Annex 1: Decomposition of UK 10-year government bond yield



Sources: Bloomberg Finance L.P. and Bank of England calculations



## Annex 2: Cash flows associated with APF unwind / maturities



Sources: Bloomberg Finance L.P. and Bank of England calculations