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REMIT FOR THE MONETARY POLICY COMMITTEE

The Bank of England Act (1998) requires that I specify what price stability is taken to consist of and the Government's economic policy objectives at least once in every period of 12 months beginning on the anniversary of the day the Act came into force.

I hereby re-confirm the inflation target as 2 per cent as measured by the 12-month increase in the Consumer Prices Index (CPI). The inflation target of 2 per cent applies at all times. This reflects the primacy of price stability and the inflation target in the UK monetary policy framework.

In accordance with the Act, I also confirm that the economic policy objective of Her Majesty's Government is to achieve strong, sustainable and balanced growth that is more evenly shared across the country and between industries.

The Government's commitment to medium-term price stability remains absolute. It represents an essential pre-requisite for economic prosperity.

Monetary policy is a key element of the Government's macroeconomic strategy, supported by a credible commitment to necessary fiscal consolidation. The Government has ensured that monetary policy can continue to play its role fully by updating the UK's monetary policy framework at Budget 2013.

At Budget 2013, I also asked the Monetary Policy Committee to assess whether it would be appropriate, given the exceptional economic circumstances, to deploy explicit forward guidance in order to meet its objectives more effectively.


I welcomed the Monetary Policy Committee's assessment, "Monetary policy trade-offs and forward guidance", published alongside the August 2013 Inflation Report, and I welcome the further guidance on the setting of monetary policy as the economy recovers included in the February 2014 Inflation Report. As you have noted, forward guidance has provided clarification about the factors

affecting policy decisions, and reassurance that the recovery will not be threatened by a premature withdrawal of monetary stimulus.

The Financial Policy Committee and the Monetary Policy Committee should continue to have regard to each other's actions, to enhance coordination between monetary and macroprudential policy. As also noted in my remit letter to the Financial Policy Committee, I share the Bank's view that the Financial Policy Committee's macroprudential tools, together with the microprudential supervision of the Prudential Regulation Authority and Financial Conduct Authority, are the first line of defence against risks to financial stability.

Finally, I also confirm that the Asset Purchase Facility, created on 29 January 2009, will remain in place for the financial year 2014-15.

A copy of the remit is attached.

A handwritten signature in black ink, appearing to read "George Osborne". The signature is written in a cursive, slightly slanted style.

GEORGE OSBORNE

REMIT FOR THE MONETARY POLICY COMMITTEE

The Bank of England Act came into effect on 1 June 1998. The Act states that in relation to monetary policy, the objectives of the Bank of England shall be:

- a. To maintain price stability; and
- b. Subject to that, to support the economic policy of Her Majesty's Government, including its objectives for growth and employment.

In order to comply with the Act, this remit sets out what price stability shall be taken to consist of and what the economic policy of the Government shall be taken to be.

Price stability

I confirm that the operational target for monetary policy remains an inflation rate of 2 percent, measured by the 12-month increase in the Consumer Prices Index. The inflation target of 2 per cent applies at all times. This reflects the primacy of price stability and the inflation target in the UK monetary policy framework.

The inflation target is forward-looking to ensure inflation expectations are firmly anchored in the medium term. The Government believes that low and stable medium-term inflation is an essential pre-requisite for economic prosperity.

The framework is based on the recognition that the actual inflation rate will on occasion depart from its target as a result of shocks and disturbances. Such factors will typically move inflation away from target temporarily. Attempts to keep inflation at the inflation target in these circumstances may cause undesirable volatility in output due to the short-term trade-offs involved, and the Committee may therefore wish to allow inflation to deviate from the target temporarily.

Circumstances may also arise in which attempts to keep inflation at the inflation target could exacerbate the development of imbalances that the Financial Policy Committee may judge to represent a potential risk to financial stability. The Financial Policy Committee's macroprudential tools are the first line of defence against such risks, but in these circumstances the Committee may wish to allow inflation to deviate from the target temporarily, consistent with its need to have regard to the policy actions of the Financial Policy Committee.

In exceptional circumstances, shocks to the economy may be particularly large or the effects of shocks may persist over an extended period, or both. In such circumstances, the Committee is likely to be faced with more significant trade-offs between the speed with which it aims to bring inflation back to target and the consideration that should be placed on the variability of output.

In forming and communicating its judgements the Committee should promote understanding of the trade-offs inherent in setting monetary policy to meet a forward-looking inflation target while giving due consideration to output volatility. It should set out in its communication:

- The outlook for inflation and, if relevant, the reasons why inflation has moved away from the target or is expected to move away from the target;
- The policy action the Committee is taking in response;

- The horizon over which the Committee judges it is appropriate to return inflation to the target;
- The trade-off that has been made with regard to inflation and output variability in determining the scale and duration of any expected deviation of inflation from the target; and
- How this approach meets the Government's monetary policy objectives.

If inflation moves away from the target by more than 1 percentage point in either direction, I shall expect you to send an open letter to me, alongside the minutes of the Monetary Policy Committee meeting that followed the publication of the CPI data and referring as necessary to the Bank's latest Inflation Report and forecasts, covering the same considerations set out above. The reason for publishing this letter alongside the minutes is to allow the Committee time to form and communicate its strategy towards returning inflation to the target after consideration of the trade-offs.

You would send a further letter after three months, alongside the minutes of the third subsequent Monetary Policy Committee meeting, if inflation remained more than 1 percentage point above or below the target.

In keeping with the principles underpinning the monetary policy framework, and the practice followed in previous inflation open letter exchanges, I suggest that you copy your letters to the Chair of the Treasury Committee.

In responding to your letter and confirming whether an appropriate balance has been struck in the judgements the Committee has made, I shall, of course, have regard to the circumstances prevailing at the time.

The thresholds do not define a target range. Their function is to define the points at which I shall expect an explanatory letter from you because the actual inflation rate is appreciably away from its target.

Unconventional policy instruments

In the event of exceptional shocks that result in the Committee's conventional policy instrument having approached its effective lower bound, as has been the case since March 2009, the Committee may judge it necessary to deploy unconventional policy instruments in order to set monetary policy consistent with the requirements of this remit.

Where those instruments involve unconventional interventions in specific markets or activities, with implications for credit risk or credit allocation, I shall expect the Committee to work with the Government to ensure the appropriate governance arrangements are in place to ensure accountability in the deployment of such instruments. This was the case with the Bank of England and the Treasury in establishing the Asset Purchase Facility in 2009 and the Funding for Lending Scheme in 2012.

The Committee may also judge it to be appropriate to deploy forward guidance in order to influence expectations and thereby meet its objectives more effectively. The Government considers any use of this to be a matter subject to the Committee's operational independence in setting policy.

Government's economic policy objectives

The Government's economic policy objective is to achieve strong, sustainable and balanced growth that is more evenly shared across the country and between industries. This objective recognises that over a number of years preceding the recent financial crisis, economic growth in the UK was driven by unsustainable levels of private sector debt and rising public sector debt. This pattern of unbalanced growth and excessive debt helped to create exceptional economic challenges in the UK.

The Government's economic strategy consists of four key pillars:

- Monetary activism and credit easing, stimulating demand, maintaining price stability and supporting the flow of credit in the economy;
- Deficit reduction, returning the public finances to a sustainable position and ensuring that sound public finances and fiscal credibility underpin low long-term interest rates;
- Reform of the financial system, improving the regulatory framework to reduce risks to the taxpayer and build the resilience of the system; and
- A comprehensive package of structural reforms, rebalancing and strengthening the economy for the future, including a package of measures to support businesses to invest and export.

Accountability

The Monetary Policy Committee is accountable to the Government for the remit set out in this letter. The Committee's performance and procedures will be reviewed by the Oversight Committee of the Court on an ongoing basis (with particular regard to ensuring the Bank is collecting proper regional and sectoral information). The Bank will be accountable to Parliament through regular reports and evidence given to the Treasury Committee. Finally, through the publication of the minutes of the Monetary Policy Committee meetings and the Inflation Report, the Bank will be accountable to the public at large.

Restatement of the Remit

The inflation target will be confirmed in each Budget. There is a value in continuity and I will have proper regard to that, but I will also need to consider that case for a revised target at these times on its merits. Any changes to this remit will be set out in the Budget. The Budget will also contain a statement of the Government's economic policy objectives.

Coordination between monetary policy and macroprudential policy

In order to foster coordination between monetary and macroprudential policy, there is overlap between the membership of the Monetary Policy Committee and the Financial Policy Committee. To enhance that coordination, where appropriate, the Monetary Policy Committee should reflect, in any statements on its decisions, the minutes of its meetings and its Inflation Reports, how it has had regard to the policy actions of the Financial Policy Committee. In the same way, the Government had also asked the Financial Policy Committee to note in the records of its meetings, its policy statements and its Financial Stability Reports how it has had regard to the policy settings and forecasts of the Monetary Policy Committee.