



The Case for Low Interest Rates

Background

Since being made independent the core remit of the Bank of England, as determined by the Chancellor, is to meet inflation targets. The secondary requirement is to maximise economic growth and employment. The argument being that a stable low inflation economy will provide the business environment to ensure the secondary requirements.

The Monetary Policy Committee (MPC) of the Bank of England will decide to increase interest rates in periods of economic growth when there is a danger of 'demand pull' inflation (when demand for goods & services is exceeding the supply, assuming the economy is at full capacity). Increases in interest rates, in these periods, will slow down consumer spending.

Requirement to Increase Economic Growth

If the UK economy fails to reach the top end of the Treasury target for growth there will be an increase in unemployment.

Current Thinking on Interest Rates

On the 5th October 2006 the Bank of England MPC decided to maintain interest rates at 4.75%. It is not insignificant that this decision was welcomed by both the TUC and the CBI.

There are perceived pressures in the economy which some commentators argue should lead to an increase in interest rates in November. Indeed, it is the case that the Government's measure of inflation – the Consumer Price Index (CPI) – has been consistently above its target of 2% for the last six months.

However Adam Lent, TUC Head of Economic and Social Affairs, warns, "The Bank rightly held its nerve and kept rates steady this month but the relief for employees and business will be short lived if borrowing costs increase in November. While there are clear pressures for a rate rise the Bank must consider that growth for 2007 is expected to slow below current expectations. An increase could also jeopardise recent improvements for UK manufacturing."