Inflation, money policy and wages

Yesterday came the expected good news that headline inflation is below the 2% target. Core inflation has been below target since June 2018. Meanwhile wage growth is around 3%, so real wages are now rising. People can look forward to having more to spend as their pay goes up.

The Bank of England has been changing its mind about all this. In a past good lecture the Governor argued that there is no longer a simple trade off between lower unemployment and higher inflation. The so called Phillips curve suggested that if unemployment fell wages started to go up faster, leading to price inflation and the need for the authorities to rein things in. Revision to this pointed out that in a modern open trading economy like the UK prices are held down by global competition, and wages by inflows of migrants and by importing labour intensive goods and services from lower wage countries. In his most recent speech the Governor has rowed back a bit on this sensible observation. He claims that there is once again a modest trade off between lower unemployment and higher wages, and that therefore the Bank will need to tighten further to control prices in the months ahead.

I do not agree. It is true wages have been going up faster in the last year, but there is no evidence this is flowing through to prices which remain under the cosh of global competition. In part wages have gone up through the introduction of the Living Wage, in part through cost push pressures in areas of the economy like care homes where recruitment has been difficult. The danger is lifting interest rates too far too fast will plunge us into a downturn. There is too little money and credit about as it is, given the Bank's tightening policy. The Governor does at least acknowledged that he has deliberately tightened policy over the last year.
It is time he said job done. The Fed has been more magnanimous in saying they have tightened enough. The Bank of England should also say this more clearly, and work to ensure a decent supply of credit to households and businesses. As The Governor argued convincingly there is no debt problem in either the public or banking sectors in the UK. With China slowing and the Eurozone stalling we need a positive policy in the UK. With inflation under target now is a good time to promote growth and allow people to buy more cars and invest more in property and business.