

BANK OF ENGLAND
LONDON EC2R 8AH

5 July 2012

The Rt Hon George Osborne
Chancellor of the Exchequer
HM Treasury
1 Horse Guards Road
London
SW1A 2HQ

Dear Chancellor,

At its meeting today, the Monetary Policy Committee judged that, in order to keep inflation on track to meet the 2% inflation target over the medium term, its programme of asset purchases should be increased by £50 billion to a total of £375 billion. That would take the scale of the Committee's asset purchase programme financed by the issuance of central bank reserves above the £325 billion authorised in your letter of 9 February 2012.

UK output has barely grown for a year and a half and is estimated to have fallen in both of the past two quarters. The pace of expansion in most of the United Kingdom's main export markets also appears to have slowed. Business indicators point to a continuation of that weakness in the near term, both at home and abroad. In spite of the progress made at the latest European Council, concerns remain about the indebtedness and competitiveness of several euro-area economies, and that is weighing on confidence here. The correspondingly weaker outlook for UK output growth means that the margin of economic slack is likely to be greater and more persistent.

CPI inflation fell to 2.8% in May and is likely to edge down further in the near term. Commodity prices have fallen, which should help to moderate external price pressures. And pay growth remains subdued. Given the continuing drag from economic slack, that should ensure inflation continues to ease into the medium term.

At its meeting today, the Committee agreed that the Funding for Lending Scheme, which would be launched shortly, was a welcome initiative. It also noted recent and prospective actions to ease liquidity constraints within the banking system. Taken together with reduced pressure on

household real incomes, on the back of lower commodity prices, and the continued stimulus from past monetary policy actions, that should sustain a gradual strengthening of output growth.

But against the background of continuing tight credit conditions and fiscal consolidation, the increased drag from the heightened tensions within the euro area meant that, without additional monetary stimulus, it was more likely than not that inflation would undershoot the target in the medium term.

I am therefore requesting the authority to use the Asset Purchase Facility to purchase assets financed by the issuance of central bank reserves totalling £375 billion. The structure and operation of the Asset Purchase Facility would otherwise be unchanged from that described in your predecessor's letter of 3 March 2009.

I am copying this letter to Andrew Tyrie MP, Chair of the Treasury Committee.

Yours sincerely,

A handwritten signature in blue ink, appearing to read 'P. King', is written in a cursive style. The signature is positioned to the left of the typed name 'P. King'.