Minutes of the meeting of 13 January 2026 at the Institute of Economic Affairs (IEA) (hybrid meeting)

Attendance: Roger Bootle, Juan Castaneda (online), Tim Congdon**,** John Greenwood (online)**, Julian Jessop (online), Graeme Leach,** Andrew Lilico (online), Kent Matthews (Secretary - online), Trevor Williams (Chair), Peter Warburton (online). David Frost (DG – IEA, Observer)

Apologies: None

Chairman's comments: Trevor Williams was late arriving, and Andrew Lilico took the chair to start the meeting. He welcomed David Frost, the new Director-General of the IEA, to the meeting. David Frost asked the committee to consider whether there might be any additional ways the IEA could help publicise the SMPC activities that are not already being done. Andrew Lilico thanked David Frost and asked Graeme Leach to make his presentation to the Committee.

Global Economic Backdrop

Global economic outlook subdued

Graeme Leach began his presentation by referring to the first slide, which showed the consensus forecasts for the developed economies. He said that the latest global consensus forecast for growth in 2025 and 2026 was about 3%, with the US around 2% in both years. He said that there were some outliers, ranging from upside risk on the US front to sclerotic growth elsewhere, with continual variation in the Eurozone between high and low, or medium and low, growth performances. But the growth and inflation outlook is subdued, with some exceptions on the inflation front.

Graeme Leach said that broad money growth in the US and Eurozone are quite muted at 4%, with the UK at 5%, and Japan around 2%, and that no alarm bells are being set off. He said that there are no screaming inflation threats from this end. He said that what is going to emerge in the second half of this decade, over the next 18 to 24 months or so, is the effects of what he called the great race. The great race is the opportunity to reap the benefits of technology and its impact on growth before the impact of demographics and statism. By the latter, he meant the trend toward tax-and-spend policies and public debt that were undermining growth.

AI related investment boost to productivity.

He said that AI-related investment is booming and the AI capex cycle is now bigger than the oil exploration cycle in the 2010s and the telecoms cycle at the turn of the century. This is what underlies the forecast for growth: a boost to capital deepening and a return to productivity in the longer term. He repeated that the downside of the great race is the part played by statism and demographics. He said that there is about to be a change in the bond market attitude toward the USA. He saw a parallel with the roaring twenties in the USA and the 1930s crash. The Roaring Twenties began with a pandemic, but thereafter, with technological change and transition, there was an acceleration in economic growth and, paradoxically, a slight acceleration in US GDP growth attributable to tariffs.

Yield curve inversion.

He said the downside is a 1930s-style crash following an overvalued Wall Street, and the risk is that something similar could happen in China. So, both upside and downside risks to the consensus view are very substantial. Graeme Leach showed a chart of PE ratios and suggested that these indicated overvaluation. Looking at the yield curve spread in the US, he said that a recession normally comes about not during the inversion, but after the un-inversion. Normally, this coincides with rising unemployment that triggers the recession. But in the US, the rising unemployment in the wake of the latest cycle of inversion and un-inversion is far more muted. What all this means for expectations of central bank interest rates is that they are going down in the US and the UK, down slightly in the eurozone, and up in Japan.

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UK Economic Environment

Money growth subdued and easing of inflation

Turning to the UK monetary conditions, Graeme Leach said that M4x growth is subdued at just under 5%. On the inflation front, the bank rate has come down, but the 10-year gilt rate is a tad higher than what it reached in the Liz Truss period. This led to the summary of December monetary policy as a 5-4 vote to reduce the bank rate to 3.75 per cent – a 150 bps reduction since August 2024. Although above the target, inflation is expected to fall quickly towards it. Subdued economic growth and slack in the labour market, along with easing pay growth and services inflation, point to a moderation in overall inflation. Fiscal effects over the next few years are expected to widen the output gap by about 1% of GDP.

Earnings edging downwards – unemployment edging upwards.

The latest panel of independent forecasts from the Treasury expects growth of 1.4% in 2025, falling to 1.1% in 2026. UK consumer price inflation figures are still higher than abroad, but the CPI is clearly on a downward path. Looking at services inflation, there is clearly quite a divergence. UK inflation is a little bit sticky, but no longer ringing alarm bells, given the rates of monetary growth. Labour market indicators show that unemployment is unlikely to impact on wage growth. Earnings are edging downwards, and unemployment is edging upwards. He said that an exception is public sector earnings growth, but some of that is a base effect from pay settlements made earlier and recorded, resulting in higher growth compared with the initial base. But overall, it's rising in the public sector. He said that the overall story is captured by the S&P Global UK services PMI, which is very subdued, and there is nothing in the employment growth that raises any alarm bells.

Scope for reduction in savings ratio through lower interest rate.

The trends in business confidence confirm the picture of subdued activity from the CBR industrial trends or GfK consumer confidence figures. He said that there is slack in the household savings ratio, which, if confidence were to pick up in the household sector, from further reductions in base rates, then there is scope for the savings ratio, which is around 10%, compared to the long-term average, to go down to 6%. Lower interest rates could boost activity by reducing debt-servicing costs.

Upside, consensus, and downside.

In summary, Graeme Leach said that the central scenario is the consensus forecast, with upside from AI and technology feeding through into productivity-boosted growth in the second half of this decade. This would be most apparent in the US, but that he would argue given the UK probably ranks third in the world for AI, there could be some positive spillover effects for the UK as well which could raise growth compared to the consensus forecast. Equally, if inflation remains subdued, interest rates can fall faster than expected, and that could boost consumer confidence. On the downside, again, from the US, a yield curve inversion finally feeds through into the US labour market, and that begins to untangle the US economy.

Trevor Williams thanked Graeme Leach for his presentation and invited questions from the committee, starting with the US-global scene and then the UK.

Discussion and Vote

AI data centres absorb huge energy, and the US has cheap energy but not the UK

Roger Bootle asked if there is a difference between the sort of aspects of AI in which the UK is very good at, as number 3 in the world, and the stuff that requires large capital expenditure? He said that these large service centres consume enormous amounts of energy, and, interestingly, America has cheap energy. So, the question is, can we hope for the same sort of boost to real expenditure from AI? He said that his suspicion is that the UK's AI pre-eminence is of a different sort.

Graeme Leach said he did not know, but that the potential in the projected numbers of $700-800 billion up to $1.3 trillion is partly predicated on declining US energy costs, whereas Mr Miliband's intention is to move the curve in the other direction. He said that he thought it would be marginal for the UK.

Trevor Williams said that he had a related question. Regarding AI, he asked what sort of AI spending he was referring to. He said that if it is predominantly in data centres, it is not only about energy, even though industrial energy prices in the UK are the most expensive of any industrialised country due to net-zero policies. The question is also about water use, and a global water crisis is looming, which will add to the hidden costs of these plants as they raise process costs and increase local resistance. The issue is that a large data centre typically uses 5,000,000 gallons of water a day, which is equivalent to 50,000 to 100,000 households. So, if you build lots of data centres, then where's the water coming from when we already have a water crisis in the UK? Moreover, as these centres serve global markets, the local economic benefits are hard to see, as the employment required to run them as built is relatively small, including security guards and technical maintenance crews.

Graeme Leach said this was another reason he thought the effect on the UK would be marginal, and that the more substantial effect would be in the US.

Andrew Lilico said that AI investment in the UK is focused on adoption infrastructure rather than on research and early-stage research. Whereas the big U.S. investment is more in the data centres and that kind of thing. So, there are different characteristics, but he also expected a considerable boost in AI investment in the UK.

US broad money figures misleading

Tim Congdon said that he had a comment about US monetary trends. He said that the broad money figures for M2 are misleading. He said that, with the vast budget deficit, the US Treasury is taking the view that it can shorten the debt without any inflationary consequences by selling large amounts of debt with less than a year to maturity to money market mutual funds. The MMFs in the 2020s have been around double digits most of the time, and now they are about 20% up on a year ago. If MMFs are regarded as broad money, and there are different views on that, then the rate of broad money growth in the USA is about 6-7%. He said that his view is that, combined with the buoyancy of the markets and at least trend growth when the economy is rather stretched, they are not going to get inflation back down to 2% on a sustained basis.

On AI, Tim Congdon said that the big thing is supposed to be autonomous vehicles, but so far, it hasn't really got traction. He said that it is a bit like the railway boom of 1844-46, which was then followed by a crash in 1847. He said that we need to be thinking in these terms, maybe not about 2026, but certainly about 2027 and 2028.

Ricardian Equivalence and saving

Andrew Lilico questioned Graeme Leach about the saving ratio. He said that, setting aside the pandemic period, the only other time the saving ratio was as high as in 2025 was in the immediate aftermath of the global financial crisis and at the peak of the Eurozone crisis. He asked what was going on here? Are households putting aside savings in anticipation of big tax rises?

Graeme Leach said that Ricardian Equivalence is a possibility, but that there were demographic effects and evidence of people being more cautious. But there has been some retracement from the peak due to monetary easing, and there could be more with further easing.

Julian Jessop said that the small fall in the saving rate was necessary because real disposable income was even weaker. He said people were starting to pay higher taxes and that inflation was still high. The small fall in the savings rate last year was simply because people were happy to maintain spending even though their incomes were falling short of what they would have liked. Another important factor is rising unemployment and job insecurity.

Inflation, the saving ratio and the 'Pigou effect'.

Kent Matthews said that the saving ratio and inflation are linked, as it was in the 1970s, when high inflation resulted in high savings. Tim Congdon said he agreed, but first, in answer to Julian Jessop, he said that unemployment is really the bottom half of the population, whereas saving is very much the top quarter. What is affecting the savings ratio is tied up with the wealth aspirations of the top quarter, the top 10% of the population. People like to have a stable ratio of financial assets to income. When the inflation rate rises, that means they must save more of their income just to keep that ratio stable.

Trevor Williams said the inflation chart showed the UK had a higher inflation rate than the eurozone, but that it was falling. However, the inflation difference between the UK and Europe is not that large, whereas the interest rate gap is much wider. It means the UK interest rate could drop significantly on the basis that the gap narrows to European levels with inflation

Inflation persistence, broad money growth and expectations

Andrew Lilico said the most recent MPC decision seemed to focus on views on inflation persistence. He asked if Graeme Leach had a view on inflation persistence? Graeme Leach said that he bases his arguments on broad money growth figures, which show that a 4-4.5% rate of growth can accommodate another base rate cut without inflation expectations reacting. Tim Congdon said he disagreed, because 4.5% money growth with trend growth of ¼ or ½% is too much. Graeme Leach said that the problem is that you can't be precise. If there is 1% growth and 2% inflation, and then you've got a velocity shift as well in the short term, exactly what rate of growth are we talking about here in the money supply? While recognising Tim Congdon's argument, he said there was scope for a further cut in the base rate.

Inflation persistence, caused by the monetary overhang.

John Greenwood said that inflation persistence, in part, is due to the continued overhang of excess money from the past. He said that the UK had a much higher rate of money growth over the crisis than the eurozone, not as high as it was in the US, and the economy has not grown nearly as rapidly as the US and therefore there has been less absorption of the excess money. It is just taking longer for the inflation rate to come down.

Trevor Williams invited the Committee to vote.

Votes are recorded in the order made

Comment by John Greenwood

(International Monetary Monitor)
Vote: Cut Base Rate by 25 bps. Maintain the pace of QT.
Bias: No bias.

John Greenwood said that, given where money growth is now, his view is that 4.5 per cent money growth is not going to cause any major problem going forward. Base rate could either stay where it is or be marginally reduced by another 25 basis points. The important thing is to ensure that money growth remains subdued. It is important that, over time, the Bank of England reduces the size of its balance sheet, because the very high level of the balance sheet means the government is effectively transferring a substantial amount of interest to the banks. Correspondingly, banks' deposits are high, and they therefore are substantial income from those deposits

Comment by Juan Castaneda

(Vinson Centre, University of Buckingham)
Vote: To hold Base Rate. Halt QT.
Bias: No bias.

Juan Castaneda said he agreed with John's analysis, though not with his policy recommendation, for the same reasons stated by him. The rate of growth of money is very much compatible with a 2% inflation target and the economy growing at roughly 1% on trend. He voted to keep interest rates steady..

Comment by Tim Congdon

(Institute of International Monetary Research, University of Buckingham)
Vote: To HOLD Base rate. QT to be maintained at current pace
Bias: No Bias.

Tim Congdon said that he was in the same camp as Juan and John. He said that, of course, there is another dimension of monetary policy: the Bank of England is still selling off some of its stockpile. The MPC reduced the number of sales, as opposed by Huw Pill said, but it has been reduced. In fact, Huw Pill and his colleagues are looking at broad money. He said they are thinking pretty much the same way we are and don't really want big changes; they want to keep money growth in the 3-5% range. He said that John has flagged up a very important medium-term issue, which could become more of an issue as we get towards 2029, about what happens to this system of paying interest on banks' cash reserves and how that gets changed. We basically want to return to the zero-interest rate on cash reserves that we had in the UK before 2006.

Comment by Graeme Leach

(Macronomics)
Vote: To cut Base Rate by 25bps.
Bias: No bias.

Graeme Leach said that he had made his explanation in the presentation. He voted for a quarter point cut only and maintain money supply growth at current trends.

Comment by Peter Warburton

(Economic Perspectives Ltd)
Vote: To HOLD Base rate. Suspend QT.
Bias: No bias.

Peter Warburton said that there were several points where he diverged from the very interesting presentation that Graham had given. He said that there is a risk of an oil price resurgence in 2026. There is very good chance of disruption and a real chance that we could get an upside surprise in oil prices, which obviously arithmetically would also spoil the benign inflation outlook. He said that we've got one of the opaquest global credit systems particularly in the US. There's a lot of hidden default risk and there's huge fear about continued interest rate normalisation because obviously interest rate normalisation isn't mature from 2022. He said that there are a lot of resets that will only come in after four or five years and a lot of people who are paying 2% interest rates will need to pay 4% or 5% Bessent and Trump are terrified of what will happen if the interest rate reset just matures naturally as it would. The pressure to undermine the Fed and take control of its interest rate decisions comes from a genuine fear about the fragility of the credit system.

With the UK, he said we are sliding into recession and not sure if anything can be done about it. Private sector output is now contracting, company insolvencies are rising sharply at the levels last seen since 2008-09.There are a lot of businesses that have lost their supply to affordable credit and are throwing in the towel. Could we rush interest rates down? He said he wasn’t sure it would do any good and it would also compromise the fight against creeping and persistent inflation as well. He said that fiscal policy must be more contractionary. He voted for a token quarter point rate cut and the immediate suspension of the QT programme.

Comment by Andrew Lilico

(Europe Economics)
Vote: HOLD Base rate. Maintain QT
Bias: no bias

Andrew Lilico said that with inflation still comfortably above target, although it's falling, and with monetary growth sitting at around the level we want, we'd need some good reason to change interest rates, and he didn't really see one. Absent a good reason to move rates in any direction, and with the money growth OK, the inflation is above target, but it's falling. He said that there's some recession risk, but that seems to me to be supply driven. He voted to hold base rate and keep QT where it is.

Comment by Roger Bootle

(Capital Economics)
Vote: Cut Base Rate by 25 bps. Maintain QT
Bias: No bias.

Roger Bootle said that little has been said about the labour market, but this is key. What the government has done to the balance of power between employers and employees is quite shocking and he expects to see quite a lot of job layoffs, a falling back in pay growth, rising unemployment, and the result of all that will be that inflation, which has been persistent is going to come down a fair old bit and that's going to allow us to cut interest rates. He voted for a ¼ point cut now and then see how things go. He said he was very worried about the political situation. The May elections are going to be critical. There is the chance, that we end up with both the Prime Minister and the Chancellor even more left wing. With fiscal policy, we could end up with more tax rises again.

Comment by Julian Jessop

(Independent Economist)
Vote: Cut in Bank Rate by 25 bps.
Bias: No bias

Julian Jessop said that he votes for a ¼ point cut because he is a bit more confident than others that inflation will fall sharply over the first half of this year. Inflation is on track to hit the 2% target, partly because of mechanical reasons and the base effects and so on for food and energy prices. Interest rates are higher than they need to be now to meet the inflation mandate. The other factor is the near-term outlook for the economy. The economy is on the brink of recession. Confidence is weak across the board. The labour market is particularly fragile.

Comment by Trevor Williams

(TW consultancy, ATFX Connect, University of Derby)
(Vote: Cut Base rate by 50 bps)
Bias: Bias 3%, continue QT

Trevor Williams voted for a 50bps cut to bring the base rate down to 3.5%. He said there is a risk of recession for the reasons already stated, but that he thinks growth will be close to the trend pace of 1¼%. The monetary growth figures suggest that inflation will stabilise over the medium term, but there's a short-term risk that it could drop further. He voted to continue with QT at the new level and to make a ½ cut to get the base rate to 3¼. He said that for struggling households and those with high debt levels, the bank rate is too high in real terms and should be lower. He reiterated his view that with similar economic growth and consumer price inflation to those in the eurozone, yet has a higher bank rate, the UK's monetary policy stance is therefore too tight.

Comment by Kent Matthews

(Cardiff Business School, Cardiff University)
Vote: To HOLD Base rate. To maintain QT.
Bias: No bias.

Kent Matthews said that he votes for a cautious 25 bps cut in base rate. He said that he took the point that money supply growth is about the right rate of growth for a long-term target of 2% inflation. He said that there's a general expectation for inflation to fall over the next quarter or so, but that the inflation expectation is predicated on a further cut in the interest rate. If we were to keep interest rates where they are, then real interest rates would be higher than what the market expects and also what's necessary for an equilibrium growth. He said that he had no strong view on QT but would go with the consensus to maintain it at its current pace

Any other business

There was no other business, and the Chairman called the meeting to a close. By convention, if there are more votes than required, the Committee records the vote but discounts the last member(s) to log in or present themselves at the venue. The last member to log in to the meeting was John Greenwood.

Policy response

1. There was a majority vote that the Base rate should be cut by 25 bps to 3.5%.
2. Five members voted to cut the Base rate by 25 bps.
3. One member voted to cut by 50 bps.
4. Three members voted to hold the base rate at its current position.
5. A majority voted to maintain QT at the current pace.
6. A majority expressed no bias to further cuts in the Base rate.

Date of next meeting

14 April 2026

Note to Editors.

What is the SMPC?

The Shadow Monetary Policy Committee (SMPC) is a group of independent economists drawn from academia, the City and elsewhere, which meets physically for two hours once a quarter at the Institute for Economic Affairs (IEA) in Westminster, to discuss the state of the international and British economies, monitor the Bank of England's interest rate decisions, and to make rate recommendations of its own. The inaugural meeting of the SMPC was held in July 1997, and the Committee has met regularly since then. The present note summarises the results of the latest quarterly meeting held by the SMPC.

Current SMPC membership

The Secretary of the SMPC is Kent Matthews of Cardiff Business School, Cardiff University, and its Rotating Chairman is Andrew Lilico (Europe Economics) and Trevor Williams (TW Consultancy, University of Derby). Other members of the Committee include: Philip Booth (St Mary's University, Twickenham), Roger Bootle (Capital Economics Ltd), Tim Congdon (Institute of International Monetary Research), Jamie Dannhauser (Ruffer LLP), John Greenwood (International Monetary Monitor), Julian Jessop (Independent Economist), Graeme Leach (Macronomics), Patrick Minford (Cardiff Business School, Cardiff University), Peter Warburton (Economic Perspectives Ltd), Juan Castaneda (Vinson Centre, University of Buckingham).