Pound falls as Bank chief talks of rate cut

Philip Aldrick Economics Editor

Sterling suffered its biggest one-day fall against the dollar in five years yesterday after the Bank of England's chief economist raised the prospect of an interest rate cut.

Andy Haldane warned that inflation may miss the Bank's 2 per cent target and claimed that "the chances of a rate rise or cut are broadly evenly balanced".

He said his personal opinion was that "risks are skewed to the downside".

The comments revealed Mr Haldane as the mystery policymaker who floated the idea of a rate cut for the first time in six years at the February meeting of the Bank's monetary policy committee.

Markets reacted swiftly to the comments despite Mr Haldane's insistence that the views were his own and not those of the MPC.

In London the pound fell 2.4 cents against the dollar to $1.4716, a 1.73 per cent drop, its largest one-day decline since May 2010. Sterling has fallen 5.5 per cent against the dollar this year.

Andy Scott, an associate director at HiFX currency specialists, said: "While he said the remarks represent his own view, rather than that of the MPC as a whole, they carry additional significance in light of the fact that several central banks have cut rates recently due to falling inflation."

The pound's fall was exaggerated by a recovery in the dollar after its sharpest slide against sterling in five and a half years on Wednesday, when the Federal Reserve issued more cautious guidance on interest rates than expected.

Mr Haldane's comments, in a speech

at a business club in Rutland, reinforce his reputation for unorthodox thinking.

The Bank stopped cutting interest rates at 0.5 per cent in March 2009 after deciding that building societies would be at risk if they were any lower.

However, Mr Haldane said that the financial sector was "now stronger" and there "may be greater scope to cut rates below 0.5 per cent".

His calculations showed that having the option of a rate cut halved the risk of deflation to 10 per cent, he added.

While insisting he did "not currently see an immediate case for a policy change in either direction", he laid out a series of reasons why inflation may not return to its 2 per cent target within two years and why a rate cut might be more effective than other responses, such as quantitative easing.

Mr Haldane's position puts him at odds with Mark Carney, the Bank's governor, who told the House of Lords last week that it would be "extremely foolish" to cut rates now.

Mr Haldane cited persistently weak wage growth, falling inflation expectations and the stronger pound as deflationary forces that may need to be addressed.

Falling unemployment should drive up wages but there has been little sign of it, which could signal a more fundamental change.

The Bank was accused this week of joining in the global currency wars by signalling that the pound may be too strong.

Although it fell against the dollar yesterday, sterling was 0.41 per cent stronger against the euro at €1.3842.