Inflation in UK hits 3.3% mark

Bank of England Governor Mervyn King warned on Tuesday that inflation could climb above 4% this year as oil and energy prices soar.

In an open letter to the Chancellor after official inflation hit 3.3%, Mr King said he had revised previous forecasts upwards due to a 15% rise in oil prices during the past month and the prospect of higher gas and electricity bills.

Mr King's latest forecast puts consumer prices index (CPI) inflation at more than double the Bank's 2% target and raises fears of imminent rate rises.

Chancellor Alistair Darling replied that he and the Prime Minister were 'working across a range of international fora' to tackle price rises and added that inflation was moderate compared with the 1970s and 1980s.

The Governor is forced to write a letter if inflation moves more than 1% above or below the Bank's target. Mr King added that inflation should peak around the end of the year and begin to fall back towards its target 'in the absence of further unexpected increases in oil and commodity prices'.

The Governor said that the course of interest rates needed to meet the 2% target was 'uncertain'. He added that the Bank's monetary policy committee (MPC) would make month-by-month judgments on the course of borrowing costs.

The MPC has faced a balancing act between cutting rates too sharply and adding to inflation risks and keeping rates too high and risking a sharp slowdown of the economy.

Soaring fuel and food prices pushed inflation above 3% in May to its highest reading since records began more than 11 years ago. The Consumer Price Index rose by 0.3 percentage points to 3.3% during May - the highest reading since the measure was first reported in January 1997.

Previous comparable annual inflation readings were last as high in July 1992, the Office for National Statistics said. The cost of living has now risen more than 1% above the Government's 2% target, triggering a public explanation from Mr King about what he will do to bring the measure down.

The underlying rate of Retail Prices Index inflation rose to 4.4% in May from 4% in April, the ONS added.

The Governor highlighted that in the year to May, world agricultural prices rose 60% with UK food retail prices up 8%. Oil prices rose by more than 80% on average while fuel prices in the UK soared 20%. Meanwhile, wholesale gas prices are up 160% and households have faced rises of around 10% in gas and electricity bills.

In contrast to his letter last year to former Chancellor Gordon Brown, Mr King said his letter was likely to be the first in a sequence as inflation remained 'markedly above target' until well into 2009. He said attempts to tackle the short-term spike in the cost of living would cause 'unnecessary volatility in output and employment', although the MPC is concerned about rising prices feeding into demands for higher wages.

The Governor added that a further slowing of the economy was likely this year as higher prices and the credit crunch weighed on household spending. But the MPC remained determined to set rates at the correct level to meet the target and prevent a prolonged period of subdued economic growth, Mr King said.

Meanwhile, Mr Darling said continued pay restraint in the public and private sectors was also needed to help rein in inflation.

'To return now to inflationary pay settlements would undermine rather than raise people's living standards with a damaging circle of wage increases eroded by steadily rising prices,' Mr Darling said.

MasterCard to suspend interchange fees

MasterCard Europe is to suspend a controversial element of its charges for crossborder credit and debit card transactions while it attempts to negotiate arrangements acceptable to Europe's antitrust regulators. Brussels declared that MasterCard's so-called "interchange" fee - that is a fee charged per payment at retail outlets when transactions are processed - to be in breach of competition rules last year. Officials gave the company six months to withdraw the fee or come up with alternative suitable arrangements.

If MasterCard failed to comply with the order, Brussels threatened to levy heavy daily penalties. The six-month deadline is June 21, which is when the fee suspension will come into force. Discussions between the company and competition officials at the European Commission over possible revisions to the existing arrangements are believed to have got under way. The company said that although it believed it had made several proposals to "reduce substantially" cross-border consumer interchange fees, it had not yet "reached an understanding" with the Commission on future steps. It added that the transactions affected accounted for less than 5 per cent of MasterCard Europe's volume and it did not expect any significant financial effect. Neelie Kroes, EU competition commissioner, said: "Irrespective of Master-Card's decision to temporarily repeal fee, the Commission will continue to be open to assess any new proposal from MasterCard."

Reliance Capital plans UK fund foray

India's No 1 fund firm Reliance Capital Asset Management plans to sell its funds in UK from September and launch emerging market and Europe-focussed funds in the country by the next fiscal, a top official said.

The firm, a unit of Reliance Capital Ltd, will also start an asset management business in Singapore in the next two years and expand in Gulf, where its presence is restricted to Dubai so far, Chief Executive Vikrant Gugnani said. "We see a potential for India-dedicated funds not only in UK but also for central and eastern Europe," Gugnani, a former Citibank executive, said in an interview. "UK will start off as advisory office but will gradually upgrade to a full-fledged asset management company," said Gugnani, whose firm's average monthly assets stood at 984 billion rupees in May.

A five-year bull run in the local stock market has lured overseas investors, despite a more than 25 per cent decline in 2008, making distribution of India-dedicated funds in the international markets a lucrative business for asset managers. More than 35 India-dedicated offshore funds registered for sale in the UK managed assets worth nearly $16 billion at the end of May, data from Lipper, a Thomson Reuters company, showed.

Global asset managers such as Robeco, part of Dutch Rabobank Group, and Britain's New Star Asset Management are also looking to offer India-dedicated funds.

Reliance Mutual Fund will add at least 84 branches and increase headcount by 40 per cent in FY09 as it looks to attract retail investors from Tier I and Tier II cities to retain its position as India's largest asset manager. The firm is also looking to expand in Gulf Co-operative Council locations such as Kuwait, Muscat, Egypt and Bahrain and evaluating options to start a representative office in the US, Gugnani said.

Pak allows duty free imports of farm equipment

The Pakistan Federal Board of Revenue (FBR) has eased the restrictions, allowed the agriculture sector to import machinery, equipment, horticulture/floriculture machinery, irrigation/draining equipment, harvesting/threshing machinery and greenhouse farming equipment, etc, whether locally manufactured or not, without payment of customs duty and sales tax.

The government is pursuing a consistent policy of supporting agriculture to attract foreign and local investments and to boost per acre yield. Presently, specific machinery and equipment are exempt from customs duty and sales tax provided that the same are not manufactured locally. This condition has the overriding effect in discouraging investment in the sector. The government has already exempted hotels/hospitals, tourism projects, wholesale and retail chain stores from the condition of local manufacture.

The de-linking of duty-free import of agricultural machinery from the local manufacture condition will largely help in improving the grain handling and storage facilities.

Open the Box AND Take the Money

Huge gains for HMRC with recoveries from safety deposit boxes

Noshir J Avari

In a modern and slightly adjusted version of "Take Your Pick" (which will test the memories of many readers) HM Revenue & Customs have hit the jackpot by "opening the box" and "taking the money", many millions of pounds if reports are to be believed.

I have written previously on ground-breaking legal decisions which enabled HMRC to mount a concerted assault on offshore bank accounts. A year ago, this led to their Offshore Disclosure facility which recently ended with the final agreement of HMRC to most of the disclosures made under that so-called amnesty. The department count this exercise as a major success, and there is a follow-up operation in progress where they are directly challenging individuals who failed to take advantage of the opportunity to disclose evaded liabilities linked to offshore bank accounts. I will be writing separately on this issue, but the purpose of this article is to focus on another, radical, new method of attack which has surfaced, to widespread publicity.

Money laundering law has been used to obtain search warrants enabling the Police to open some seven thousand safety deposit boxes in West and Central London. Money and other items found in the boxes has been impounded, with box owners invited to apply for the return of box contents felt to have an innocent origin.

Whilst the ownership of many boxes has been established, in a large number it apparently has not, and a substantial sum has not been claimed or, of course, returned to anyone. Although the supposedly anti-terrorism law was used, it is clear that the owners of many boxes are alleged to have been involved in a wide variety of crime, by way of theft of money and assets, drug trafficking or tax evasion. My concern is the final category, where there are likely to be many people who wonder whether the raids on the strongbox offices are soon going to lead to criminal action against them, with loss of substantial funds.

In advising such individuals, the recommended course of action is likely in general to be similar to that adopted with the Offshore Disclosure brigade. That is, to come clean and disclose full details of any tax irregularities which have given rise to money locked away in strong boxes, well away from the prying eyes of HMRC.

But there are important contrasts with the Offshore Disclosure regime cases, and some vital aspects to be addressed.

First and foremost, there is no amnesty on offer. Any tax due will be subject to penalties at a much higher rate than the 10% offered last year, and since it is likely that some of the raided boxes contain evidence of fraud which is clear-cut and detailed, kept on the assumption that this damning information would never see the light of day, we can expect some possibly high-profile prosecutions.

Second, there is a very definite element of "guilty until proved innocent". This is because the Proceeds of Crime Act basically requires that anyone claiming back money, financial instruments and other valuable assets impounded will have to prove that the items were legitimately acquired. That may not be easy. It may be impossible.

In the case of anyone in business, there is an obvious added factor - HMRC will presume that such funds represent diverted receipts of the business and will wish to investigate the personal and business finances of the box holder, his/her businesses and associates to establish the full extent of undisclosed income and gains. In serious cases this might lead to prosecution, but in any event it is likely to result in a financial settlement with HMRC which will make a serious hole in the funds.

Third, HMRC will also expect that profit or income understatements will extend beyond anything in the box.

In some cases, there will no doubt be offshore bank statements and other documents revealing additional funds and assets held elsewhere, and there is inevitably the question of what further amounts of extracted funds were spent supporting an extravagant lifestyle.

For more information visit: www.avariandassociates.co.uk