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(Updates with industrial production in seventh paragraph.)

By Jennifer Ryan

May 10 (Bloomberg) -- Bank of England Governor Mervyn King is about to make the policy decision that may define his final year in office.

The central bank's nine-member Monetary Policy Committee will today halt bond purchases at 325 billion pounds ($524 billion), ending a second round of stimulus, according to 43 of 51 economists in a Bloomberg News survey. The remainder see an increase of at least 25 billion pounds in the biggest split on the direction of policy since October, when the bank unexpectedly restarted quantitative easing.

King must navigate competing arguments on what's best for an economy trying to shake off its first double-dip recession since 1975 while enduring faster-than-forecast inflation. The risk is that getting it wrong may worsen the slump or entrench price gains, complicating the task facing his successor, who will take charge in little more than a year.

"It's a very difficult backdrop and this isn't the final year he'd like from the point of view of policy," said David Tinsley, an economist at BNP Paribas SA and former Bank of England official. "The risks of more QE are around 40 percent, it's a pretty fine line. Inevitably he'll be charged with a policy error."

The MPC will make its decision with new quarterly economic forecasts to be published next week. King, whose second term ends in June 2013, will defend the actions at a press conference May 16 and face questions from lawmakers in the coming weeks.

Europe Threats

The central bank will announce the decision at noon in London. In February 2010, the bank released a statement when it decided not to expand stimulus after finishing its first round of bond purchases.

Industrial production fell 0.3 percent in March from the previous month, in line with economists' forecasts, data today showed. In the first quarter, production dropped 0.4 percent.

Reports last week indicated manufacturing and services weakened last month after the economy shrank 0.2 percent in the first quarter. J Sainsbury Plc, the U.K.'s third-largest supermarket company, said yesterday that the "wider economic situation remains uncertain."

In Europe, Britain's biggest trading partner, Spain is struggling to contain speculation it will need a bailout, while political stalemate in Greece after elections has raised concerns the country may leave the currency bloc.

Gilts Gain

The risks in the region have pushed the euro to its weakest in 3 1/2 years against the pound. Gilts have risen as investors sought the relative safety of U.K. government debt, pushing the 10-year gilt yield to a record low. The yield was at 1.917 percent as of 8:42 a.m. in London, after dropping to 1.881 yesterday, the lowest since Bloomberg began compiling the data in 1989.

"The background for the BOE's decision is a euro crisis which is looking even more of a downside risk, and a U.K.
economy in recession," said Victoria Cadman, an economist at Investec Securities in London. "Even an inflation hawk would be fairly worried about that."

Consumer-price growth accelerated to 3.5 percent in March, remaining above the Bank of England's 2 percent target for a 28th month, and inflation concerns are mounting.

Deputy Governor Paul Tucker said April 18 the "uncomfortably above target" rate could hold above 3 percent into the second half of the year. Policy maker Adam Posen ended a push for further stimulus last month and minutes of that meeting said there was a risk that inflation may "fall less rapidly" than projected.

Inflation Overshoot

"The concerns on inflation make it inappropriate to expand stimulus at this time," said Brian Hilliard, an economist at Societe Generale SA in London and a former central bank official. "The bank has been somewhat wounded by the continual criticism about the overshoot of the inflation numbers."

Minutes of today's decision will be published May 23 and may reveal a split among policy makers. David Miles, the only MPC member to vote for more stimulus last month, has since said that decision looks vindicated, while Martin Weale said data showing the U.K. slipped back into recession strengthened the argument for more QE.

Today's announcement comes as King is already facing criticism for his handling of the financial crisis and for lending political support to the Conservative-led government. He drew fire from the opposition Labour Party for describing the government's fiscal squeeze as a "textbook response" to the turmoil in a BBC radio interview on the day of municipal elections last week.

'Slow Recovery'

King also said that despite a "patchy picture," the U.K.
should "start to see a steady, slow recovery coming during the course of the year." To support the recovery, interest rates are likely to remain low "for the time being," he said. All 61 economists in a survey see the MPC holding the benchmark rate at a record low of 0.5 percent today.

Even if the bank pauses today, the stimulus program may yet be revived. National Australia Bank Ltd., owner of Britain's Clydesdale Bank, said April 30 it will cut more than 1,400 jobs in the U.K. after the deteriorating local economy torpedoed plans to sell the unprofitable business. William Morrison Supermarkets Plc said May 3 that the economic background will "remain challenging for the consumer."

"If they get the kind of news they hope for on inflation in a few months' time, then they will reconsider," Hilliard said. "A debate about QE is going to be seriously back on the table between three and six months."

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