PREVIEW: BoE rate decision and minutes due Thursday 17th March 2022

- **BoE rate decision & minutes & due 17th March 2022 at 12:00GMT/08:00EDT**
- **Expectations are for the BoE to raise rates by a further 25bps to 0.75% via a unanimous decision**
- **Hike will be justified by rampant inflation in the UK which will likely be exacerbated by events in Ukraine**

OVERVIEW: After hiking rates by 15bps in December and 25bps in February, the BoE is set to come to market with another 25bps worth of tightening. Recall, the decision to raise rates at the prior confab was unanimous, however, there was a split of views in terms of the magnitude with five policymakers voting for a 25bps increase and the remaining four preferring a 50bps increase. This time around after failing to pull the trigger on a 50bps move, the consensus is firmly towards a 25bps hike. The backdrop to the upcoming meeting is once again characterised by rampant inflation in the UK, and the Russian invasion of Ukraine is likely to further fan the flames of inflation whilst cooling growth. UBS highlights that further advances in inflation will likely increase the MPC's concerns about second-round effects via higher wages with the Bank's Agents report suggesting that there are signs of significant increases in wage growth this year. Looking beyond the upcoming decision, markets currently price in around five additional rate hikes (excluding March) by year-end. UBS, as well as several other desks, suggest that such pricing will likely prove to be too aggressive. UBS expects that after raising the Bank rate to 1% in May, policymakers will hold off from lifting rates further. Note, the upcoming meeting will not be accompanied by economic projections.

PRIOR MEETING: As expected, the MPC opted to follow up the 15bps December hike with a further 25bps of tightening, bringing the Bank Rate to 0.5%. The decision to lift rates was unanimous, however, the magnitude of the rise was subject to a 5-4 vote split with Mann, Saunders, Ramsden and Haskel advocating a 50bps move to 0.75%. Nonetheless, with the rate at 0.5%, the Bank will halt reinvestments under its Asset Purchase Facility. The decision to lift the Bank Rate again was justified by “the current tightness of the labour market and continuing signs of greater persistence in domestic cost and price pressures”. As a guide, inflation was expected to increase further in coming months, to close to 6% in February and March, before peaking at around 7.25% in April. Within the accompanying MPR, the 2022 GDP projection was cut to 3.75% from 5.0% with growth of just 1.25% pencilled in for 2023. The rate path implied a Bank Rate of 1.5% by mid-2023 ahead of the release, however, the MPC cautioned that such a level of interest rates would push inflation well below target in 2024. At the follow-up press conference, Governor Bailey warned that policymakers face a trade-off between weakening growth and inflation, and as such markets should not extrapolate and assume rates are on a long march upwards.

RECENT DATA: CPI metrics for January saw Y/Y CPI climb to 5.5% from 5.4% with the core metric picking up to 4.4% from 4.2%. ING noted that some of the upside was attributable to the annual adjustment to the basket weights with the basket more heavily tilted towards goods spending than pre-pandemic. On the growth front, M/M GDP for January was 0.8% vs. the 0.2% contraction in December (which was above the BoE's expected decline of 0.5%). Note, in the February statement, the BoE cautioned that "beyond the near term, UK GDP growth is expected to slow to subdued rates". Survey data for February saw the composite PMI metric jump to an 8-month high of 59.9 from 54.2 with IHS Markit noting "the ebbing of the Omicron wave of the COVID-19 pandemic contributed to a rebound in growth in the UK service sector in February". In the labour market the unemployment rate in the 3M period to January fell to 3.9% from 4.1% in December. On the wage front, average weekly earnings (inc. bonus) rose to 4.8% in January from 4.3%. Despite the uptick, Pantheon Macroeconomics does not expect wages to soar after observing that " the year-over-year growth rate of the timelier PAYE measure of median pay slowed to 5.1% in February, from 6.1% in January".

RHETORIC: Since the prior meeting, Governor Bailey (Feb 23rd) has noted (in the context of the 5-4 vote split) that it is important not to suggest there is a difference in the view on the MPC about the level that rates need to reach, as opposed to the pace. Bailey also reiterated that the message to markets is not to get carried away by rate rises, adding that moderate rate rises are likely in the coming months. Deputy Governor Broadbent (Feb 23rd) suggested that over the medium term, he thinks the risks to global goods prices are, like those of energy, skewed somewhat to the downside. Deputy Governor Ramsden stated that when it comes to further modest tightening, the word “modest” is significant. Deputy Governor Cunliffe (Mar 2nd) on the Russian invasion of Ukraine stated "the events of the last few days have led to an abrupt shift in our expectations of the future and an increase in uncertainty.” Chief Economist Pill (Feb 9th) suggested that "Restricting ourselves to a 25bp now – albeit with the prospect of more to come in the coming months – is an investment in containing market expectations of aggressive ‘activism’ that I saw as worth making.". External member Mann (Feb 25th) wished to emphasise her focus on inflation expectations and she thought it was important to dampen inflation expectations by voting for a 50bp rate increase. External member Saunders said his vote for a 50bps hike in February does not necessarily imply that he believes that the level of rates one or two years ahead will be higher than the yield curve used for the February MPR. External member Tenreyro (Mar 2nd) noted that the high level of Cos. wage expectations in the BoE agents' survey was a surprise with evidence of a wage-price spiral in the UK not obvious. External member Haskel said that his decision to vote for a 50bps hike in February was a "finely-balanced" one. He also noted that previous MPC estimates of equilibrium interest rates remain valid, but have gone down.

RATES: After hiking rates by 15bps in December and 25bps in February, the BoE is set to come to market with another 25bps worth of tightening at its upcoming meeting. Since the prior meeting, inflation has continued to pick-up pace with the Ukraine conflict stoking further inflationary concerns; Pantheon Macroeconomics now expects inflation to hit 8.7% in April vs. the MPC forecast of 7.25% and suggests that inflation could peak "slightly above" 9% in October when OFGEM raises its energy price cap. UBS also highlights the BoE's Agents report which noted there are signs of significant increases in wage growth this year. Note, the decision to raise rates at the prior confab was unanimous, however, there was a split of views in terms of the magnitude with five policymakers voting for a 25bps increase and the remaining four preferring a 50bps increase to signal the Bank’s inflation-fighting credentials. This time around after failing to pull the trigger on a 50bps move, the consensus is firmly towards a 25bps hike to 0.75% with 44/49 surveyed expecting a hike and just five economists anticipating no change. The 25bps hike is expected to come via a unanimous 9-0 decision. Looking beyond the upcoming decision, markets currently price in around five additional rate hikes (excluding March) by year-end. UBS, as well as several other desks, suggest that such pricing will likely prove to be too aggressive. UBS expects that after raising the Bank rate to 1% in May, policymakers will hold off from lifting rates further given the squeeze on real incomes and demand from rising energy prices. Rabobank even goes as far as suggesting there is an increased risk of rate cuts from 2023 onwards on the basis that the MPC will be raising rates into a looming slowdown and could potentially deepen it.

QE: With rates now at 0.5%, the BoE announced at its prior meeting that it will "cease to reinvest any future maturities falling due from its stock of UK government bond purchases.". As a reminder, current guidance from the BoE suggests that it will actively start selling Gilts when the Bank Rate hits 1%. However, policymakers have stated that selling Gilts when the Bank Rate hits 1% will not be an automatic process. Rabobank expects the MPC to leave this guidance unchanged at the upcoming meeting despite the criteria being on track to be met by May.