PREVIEW: BoE rate decision, MPR and minutes due Thursday 4th August 2022

- **BoE rate decision & minutes & MPR due Thursday 4th August 2022 at 12:00BST/07:00EDT, press conference at 12:30BST/07:30EDT**
- **Expectations are for the MPC to lift rates by 50bps, but analysts are far from unanimous**
- **Focus will be on how committed the MPC is to further tightening**

OVERVIEW: The overall consensus looks for a 50bps increase with 46/65 expecting such an outcome vs. 19/65 looking for a 25bps hike. Markets have a higher level of conviction with a 50bps increase priced in via a circa 82% probability; this is in part a by-product of larger increases by other major global central banks such as the ECB and Fed. Looking further ahead, markets anticipate around 135bps of tightening by year-end. The partial ambiguity in the analyst community stems from the lack of clear guidance from MPC officials with Governor Bailey noting that a 50bps increase will be amongst the choices for the meeting (which is not a surprise given recent hawkish dissent), but cautioning against betting on such an outcome. From a data perspective, the June Y/Y CPI print rose to 9.4% from 9.1% and therefore exceeded the MPC's forecast of 9.1%. However, survey metrics in July declined from prior levels with S&P Global noting that "UK economic growth slowed to a crawl in July". Furthermore, the latest jobs data suggests that the labour market is no longer tightening. As well as the decision itself, markets will be looking for any adjustments to the Bank's current guidance that states "the Committee will be particularly alert to indications of more persistent inflationary pressures, and will if necessary act forcefully in response". Elsewhere, traders will be eyeing any details around the Bank's plans for selling Gilts held in the APF.

PRIOR MEETING: As expected, the MPC opted to raise rates by 25bps, taking the Bank rate to 1.25% via a unanimous decision. The decision to tighten further was unanimous, but there was disagreement over the necessary magnitude with three dissenters (Haskel, Mann and Saunders) preferring a 50bps increase. Policymakers opted to continue with their rate hiking cycle on the basis that CPI inflation is expected to print over 9% during the next few months and to rise to slightly above 11% in October. Furthermore, the MPC judged that indicators remain consistent with a tight labour market. From a growth perspective, Q2 GDP was expected to contract by 0.3%, which would be a worse outturn than expected at the time of the May MPR. Elsewhere in the statement, the MPC opted to remove prior guidance which noted that some degree of further tightening in monetary policy may still be appropriate in the coming months. This was replaced with language noting that "the Committee will be particularly alert to indications of more persistent inflationary pressures, and will if necessary act forcefully in response". Some have suggested that this could pave the way for a 50bps increase in August.

RECENT DATA: June's inflation metrics saw Y/Y CPI climb to 9.4% from 9.3% and therefore exceed the BoE's projection of 9.1% as food and energy prices continued to rise. The core reading pulled back to 5.8% from 5.9%, prompting some desks to posit that core inflation might have peaked. On the growth front, M/M GDP in May printed at 0.5% vs. a 0.2% contraction in April with May's outturn supported by positive contributions from all the main sectors. That said, survey data for July saw the composite PMI decline to 52.8 from 53.7 with S&P Global noting that "UK economic growth slowed to a crawl in July...Although not yet in decline...the PMI is now at a level consistent with just 0.2% GDP growth". On the jobs front, the labour market remains tight, but is no longer "actively tightening", according to ING with the unemployment rate holding steady at 3.8% in the three months to May. Furthermore, Pantheon Macroeconomics highlights the decline in the July employment PMI to its lowest level since March 2021. On the wages front, June's XpertHR survey reported that the median pay settlement remained unchanged at 4% for a third successive month, according to Oxford Economics. Retail sales continue to remain a source of concern with June's report marking a sixth contraction in eight months.

RHETORIC: Governor Bailey (19th July) at his Mansion House speech noted that a 50bp increase will be among the choices for the upcoming meeting. However, 50bp is not locked in and therefore "anyone who predicts this is doing so based on their own view". Bailey also reiterated the MPC's guidance that if we see signs of a greater persistence of inflation, and price and wage setting would be such signs, we will have to act forcefully". The Governor also provided some commentary on the MPC's proposed Gilt sale agenda (discussed in the "Gilts" section below). Elsewhere, Deputy Governor Ramsden (14th July) stated that "rates are very likely to have to go up further" and "we're not going to let high inflation become sustained and get out of control like it did in the '70s and '80s." Chief Economist Pill (6th July) stated that current guidance reflects his "willingness to adopt a faster pace of tightening than implemented thus far in this tightening cycle". Deputy Governor Cunliffe (6th July) stated that the MPC will act to ensure the inflation shock does not become embedded, whilst noting that are signs the economy is slowing. External member (and hawkish dissenter)

Saunders (18th July) refrained from revealing how he would vote at the upcoming meeting, but noted that he believes that the tightening cycle has "some way to go". External member Mann (7th July) said uncertainty about the inflation process strengthens the argument for front-loading rate rises. Finally, external member Tenreyro (5th July) says she would expect the QE unwind to have no material impact on the UK economy and experience so far supports that.

RATES: The overall consensus looks for a 50bps hike to the Bank Rate to 1.75%. A Reuters poll taken between the 13th-25th July originally saw analysts split in their views with 29/54 expecting a 25bps increase with the remaining 25 looking for a larger increment of 50bps. Since then, a poll conducted between July 27th and August 1st has seen analysts shift towards expecting a 50bps increase with 46/65 expecting such an outcome vs. 19/65 looking for a 25bps hike. The decision to increase interest rates is expected to be a unanimous one, however, the vote split over the magnitude is less certain. As a reminder, Haskell, Mann and Saunders dissented (hawkishly) at the June meeting and therefore it will require a minimum of two other MPC members to deliver a 50bps hike this time around. As it stands, market pricing has a higher level of conviction than surveyed analysts with a 50bps increase priced in with a circa 82% probability; this is in part a by-product of larger increases by other major global central banks such as the ECB and Fed. Looking further ahead, markets anticipate around 135bps of tightening by year-end. In terms of those looking for a 50bps increase, ING expects such a move not "because the data we've received since June's 25bp hike decision has moved the needle all that much". But, "policymakers hinted back in June that they could act 'forcefully' to get inflation lower. And with a 50bp move more-or-less priced, that's what we expect them to do". Beyond August, ING expects a 25bps hike in September before the MPC pauses its current cycle. Elsewhere, Goldman Sachs also looks for a 50bps increase given "the strong inflation data" and likely sizable upward revision to the BoE's growth forecast". However, GS concedes that given the lack of comms from some of the more dovish members on the MPC in recent weeks, forecasting the vote split will be "more difficult than usual". Of those who are looking for a 25bps increase, Oxford Economics suggests that although the outcome of the meeting is "finely balanced", the consultancy favours a 25bps move given that "the likely increase in the BoE's inflation forecast will be due to factors outside the MPC's control". Furthermore, Oxford Economics sees "scant evidence of second-round effects via higher wage growth, and surveys have shown a retreat in cost pressures". As well as the decision itself, markets will be looking for any adjustments to the Bank's current guidance that states "the Committee will be particularly alert to indications of more persistent inflationary pressures, and will if necessary act forcefully in response".

GILTS: Since the prior meeting, Governor Bailey (19th July) noted that at the upcoming meeting, the MPC will discuss the strategy for selling Gilts held in the APF. Furthermore, details of the strategy will be published alongside the MPR with a potential confirmatory vote by the MPC to follow as early as September and the option to commence sales shortly after. In terms of a potential size, Bailey noted that "we are currently looking at a total reduction in the stock of gilts held by the APF, which covers both sales and gilt redemptions, of something in the region of £50#100bn in the first year". In terms of desk views, Pantheon Macroeconomics expects Gilt sales to commence in Q4 whilst noting that in the 12 months from October, GBP 35bln of Gilts will mature and therefore guidance from Bailey points towards active sales of between GBP 15-65bln over this period. Pantheon expects an amount towards the lower end of this range given that the MPC has expressed a preference in the past to tighten monetary policy primarily by raising the Bank Rate, rather than by shrinking its balance sheet. Furthermore, given the fiscal uncertainty emanating from the Conservative leadership race, the MPC will likely err on the side of caution when it comes to unwinding its balance sheet.

PROJECTIONS: The accompanying projections in the MPR are expected to see an upgrade to the 2022 CPI estimate of 10.25% to around 12% on account of a revision to the BoE's forecast for the October OFGEM price cap, according to Goldman Sachs. Goldman Sachs also looks for a minor downtick to the 2023 projection to 3.25% from 3.5%. Of potentially greater interest will be the medium-term forecasts given that the MPC has continued to warn that the implied market rate path would push inflation materially below the 2% threshold. Goldman Sachs suggests that the 2024 forecast could be nudged up towards 1.75% from 1.5% and therefore indicate that the MPC views current market pricing as "more reasonable", but ultimately pricing would still need to be scaled back further. From a growth perspective, Goldman Sachs expects the 2022 GDP projection to be upgraded to 4% from 3.75% on account of recent activity data and government support measures. Thereafter, 2023 is expected to be revised higher to 0.25% from -0.25% with 2024 held steady at 0.25%.

Previous forecasts:

Inflation: 2022 10.25%, 2023 3.5%, 2024 1.5%

GDP: 2022 3.75%, 2023 -0.25%, 2024 0.25%

Unemployment rate: 2022 3.25%, 2023 4.25%, 2024 5%

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