PREVIEW: BoE rate decision, MPR and minutes due Thursday 3rd November 2022

- **BoE rate decision & minutes & MPR due Thursday 3rd November 2022 at 12:00GMT/08:00EDT, press conference at 12:30GMT/07:30EDT**
- **Expectations are for the MPC to lift rates by 75bps, but could be subject to a split vote**
- **Focus will be on how committed the MPC is to further tightening**

OVERVIEW: With Y/Y CPI running at an uncomfortably high 10.1% in September and the core metric advancing to 6.5%, policymakers are expected to deliver a “significant” rate hike after the 50bps adjustment in September underwhelmed some in the market. Expectations are for the MPC to hike the Bank Rate by 75bps to 3%, according to 18 /30 analysts surveyed by Reuters. In terms of market pricing, a 75bps hike is 95% priced in as bets for 100bps continue to recede. The decision to hike rates is expected to be unanimous, however, there is expected to be a split in views over the magnitude with Dhingra (voted for a 25bps hike in September) and Tenreyro potential dissenters. Note, the Bank has continued to push back on the aggressive level of market pricing with Deputy Governor Broadbent (20th Oct) noting that it remains to be seen if rates need to rise as much as currently priced in by markets. It’s also worth noting that by the time of the meeting, the Bank’s Gilt sale operation (short and medium-term) will have commenced after pushing back the start date in October. Elsewhere, the accompanying MPR projections will be subject to great uncertainty and potentially of limited use given that they can only factor in stated government policy. Given the fiscal event due on October 31st has now been pushed back to November 17th, the MPC will need to base its forecast on the Energy Price Guarantee being maintained for two years, instead of the shorter timeframe that Chancellor Hunt is expected to officially unveil.

PRIOR MEETING: A unanimous decision to increase the Bank Rate, but three-way dissent on the eventual 50bp hike with Dinghra taking the dovish mantel from Tenreyro and voting for 25bp while known hawks Haskel, Mann and Ramsden supported a 75bp increase. Given the 50bp hike disappointed market pricing for 75bp, a snap dovish-reaction was seen sending Gilts to session highs and pressuring Sterling. However, with reference to the Gilt move, this swiftly reversed to below pre-release levels given numerous bearish factors. Specifically, the BoE confirmed that they were going to reduce their holdings of gov’t bonds by GBP 80bln over the next 12 months. Additionally, the BoE retained its guidance that they will continue to “respond forcefully” as necessary to inflation and while the peak forecast was reduced vs August’s update, it remains elevated and well above target. Finally, the Bank downgraded its view on the UK economy in the near-term, Q3 2022 is expected to see GDP declining by 0.1% (vs August projection of +0.4%); for a second quarter of contraction.

RECENT DATA: Y/Y CPI in September climbed to 10.1% from 9.9%, whilst the core reading advanced to 6.5% from 6.3% with the headline rate bolstered by food inflation which rose to 14.5% and therefore offset declines in motor fuel inflation. On the growth front, August GDP contracted 0.3% on a M/M basis with the ONS noting that monthly GDP is now estimated to be at the same level as it was pre-COVID. On a Q/Q basis, growth stood at -0.5% vs. the MPC expectation of +0.4%. Timelier PMI data for October saw both manufacturing and services delve deeper into negative territory with the composite metric declining to 47.2 from 49.1. S&P Global noted that "GDP looks certain to fall in the fourth quarter after a likely third quarter contraction, meaning the UK is in recession." In the labour market, the unemployment rate in the 3-months to August fell to 3.5% from 3.6%, albeit there are concerns over the increasing number of people classified as long-term sick. Elsewhere, wage growth continued to pick up with headline 3M Y/Y earnings growth at 6.0%. September M/M retail sales saw a contraction of 1.4% as the cost-of-living crisis continued to squeeze the consumer. Pantheon Macroeconomics highlighted that "volumes fell for the ninth time in 11 months, and were 2.1% below their 2019 average level".

RHETORIC: Since the prior meeting, commentary from MPC members has been sporadic and in part focused on financial stability given the market turmoil that followed the government's mini-budget in September. Governor Bailey has not made much in the way of direct commentary on monetary policy with comments on October 11th largely centred around volatility in the Gilt market where he warned pension funds that bond purchases of long-dated Gilts would not be extended beyond the October 14th deadline. At the time, Bailey also highlighted that the BoE's role on financial stability and monetary policy were working in opposite directions. Deputy Governor Broadbent (20th Oct) noted that it remains to be seen if rates need to rise as much as currently priced in by markets, which at the time priced in a peak rate of around 5.25%. Furthermore, he added that if government support mitigates the effect of import costs, there will be more at the margin for monetary policy to do. Chief Economist Pill on 12th Oct., said he was inclined at the time to believe that "a significant" monetary policy response would be required to the significant macro and market news of the past few weeks. From a macro perspective, he also noted that employment has stagnated and is showing tentative signs of falling, adding that "the sustained (and reassuring) downward trend in market inflation expectations that emerged from early April appears to have come to an end, at least for now". Deputy Governor Ramsden, flagged that the new energy price guarantee details (on Oct 31st) would have been particularly important for the MPC, however, this fiscal event has now been pushed back to November 17th. Ramsden also noted that PMI data is consistent with the UK economy being in a recession and the MPC will need to take account of the fall in the value of the Pound. External member Mann (3rd Oct) said she voted for a 75bp rate hike in September due to inflation expectations, Sterling depreciation, the impact of the energy cap and other factors.

RATES: Expectations are for the MPC to hike the Bank Rate by 75bps to 3%, according to 18/30 analysts surveyed by Reuters. For the remaining 12 surveyed, 10 expect a 100bps move, one favours 125bps and another looks for 150bps. In terms of market pricing, a 75bps hike is 95% priced in as bets for 100bps move continue to recede. The decision to hike rates is expected to be unanimous, however, there is expected to be a split in views over the magnitude with Dhingra (voted for a 25bps hike in September) and Tenreyro potential dissenters. Market participants will also be on the lookout for clues about further tightening within the policy statement given the recent pushback from Deputy Governor Broadbent. As it stands, looking beyond November, the MPC is expected to hike by a further 50bps in December with the peak rate for the cycle seen around 4.75% in 2023.

GILTS: Following the fallout of the UK's mini-budget which prompted a spike in Gilt yields and instability within the UK bond market, the MPC opted to push back the date of its Gilt sale operations that were due to start on October 3rd. Furthermore, the Bank went into the market and bought longer-dated Gilts between September 28th and October 14th in an attempt to restore order to the distressed pension sector. As it stands, the MPC is to commence its Gilt sale operations (just short and medium term offerings) on November 1st with the annual target of an GBP 80bln stock reduction unaffected and unchanged. With this part of the Bank's operations now seemingly on auto-pilot, greater focus for the release will be on the Bank's rate hike ambitions. That said, the Governor will likely be questioned during the press conference on when the MPC views it will be able to sell long-dated Gilts back into the market and what conditions could prompt the Bank to pause its purchases if market conditions deteriorate.

PROJECTIONS: Given that the fiscal event due on October 31st has now been pushed back to November 17th, the MPC will need to base its forecast on the Energy Price Guarantee being maintained for two years, instead of the shorter timeframe that Chancellor Hunt is expected to officially unveil. Furthermore, the MPC will not be able to factor in the more stringent fiscal package that will be put forward in November. Accordingly, analysts at Pantheon Macroeconomics expect “the MPC’s forecasts likely will show CPI inflation hovering near the 2% target in two-to-three years’ time, despite the big upward shift in markets’ expectations.” Note, that if this is the case, this would not necessarily be an endorsement by the BoE that market pricing is consistent with the MPC reaching its inflation mandate over the medium-term, it would more be a case of the distortions of the mini-budget assumptions which are no longer valid. Accordingly, given the great level of uncertainty underpinning the forecasts, they will likely carry less weight than usual. From a growth perspective, focus will be on how the MPC judges the recessionary outlook, however, again, these forecasts will be dismissed by many given the upcoming fiscal event on November 17th.

Previous forecasts:

- Inflation: 2022 13%, 2023 5.5%, 2024 1.5%
- GDP: 2022 3.5%, 2023 -1.5%, 2024 -0.25%
- Unemployment rate: 2022 3.75%, 2023 4.75%, 2024 5.75%