PREVIEW: BoE rate decision, minutes and MPR due Thursday 2nd February 2023

- **BoE rate decision, minutes and MPR due Thursday 2nd February 2023 at 12:00GMT/07:00EST, press conference due at 12:30GMT/07:30EST**
- **The MPC is expected to deliver another 50bps hike; will likely be subject to dissent**
- **Focus will be on how committed the MPC is to further tightening**

OVERVIEW: Analysts surveyed by Reuters and market pricing look for a 50bps hike in the Bank Rate to 4%. The decision to hike rates is expected at 7-2 with Mann and Tenreyro set to remain in the unchanged camp. Within the remaining seven, there is likely to be a split of views, the extent to which is hard to judge given the lack of comms from the MPC since December. HSBC has attempted to form a base case scenario with an out-of-consensus call for a 25bps hike in which Bailey, Cunliffe, Broadbent and Pill go for 25bps, whilst Mann, Haskell and Ramsden back a 50bps move. However, such a step down in the cadence of rate hikes would likely need to be accompanied by guidance that rates will still have further to run given developments in the labour market. Looking beyond February, a 25bps hike in March is priced at around 80% with markets split on whether a further 25bps would follow in Q2 to take the terminal rate to 4.5%. In terms of the accompanying forecasts, HSBC expects that the impact of the stronger GBP and softer energy prices will likely outweigh the impact from stronger growth and lower rates, which should therefore lead to a downward revision to the MPC's Q4 2023 inflation forecast to 6.9% from 7.9%.

PRIOR MEETING: As expected, the MPC opted to step down the pace of its rate hiking cycle to 50bps from 75bps, taking the Base Rate to 3.5%. The decision to move on rates was not a unanimous one with dovish dissent from Dhingra and Tenreyro who voted for no change. They framed their decisions on the viewpoint that the current setting of the Bank Rate was more than sufficient to bring inflation back to target, before falling below target in the medium term. At the hawkish end of the spectrum, external member Mann backed a 75bps hike on the basis that it would reinforce the tightening cycle and lean against an inflation psychology that was embedded in wage settlements and inflation expectations. Elsewhere, the statement noted that further increases in the Bank Rate may be required; according to a "majority" of the Committee. Additionally, the statement did not repeat the November line that rates are unlikely to reach the peak implied by the market.

RECENT DATA: Headline Y/Y CPI in December fell to 10.5% from 10.7% (MPC Nov exp. was 10.9%), whilst the core metric held steady at 6.3%; note attention in the aftermath of the release was on the jump in core services CPI to 6.8%. The Citi/YouGov inflation expectations survey for December saw the 12-month ahead metric fall to 5.7% from 6.1%. Note, the latest Decision Maker Panel survey will be released on the morning of the policy announcement. On the growth front, GDP data for November was not as bad as feared, coming in at 0.1% M/M and followed on from the 0.5% expansion in October. As such, GDP for December would need to contract by 0.4% M/M to nudge Q4 into negative territory on a Q/Q basis. More timely PMI data revealed an uptick in the manufacturing PMI and slip in the services component, leaving the composite lower M/M for January and comfortably below the neutral 50 mark at 47.8. The accompanying report noted "Industrial disputes, staff shortages, export losses, the rising cost of living and higher interest rates all meant the rate of economic decline gathered pace again at the start of the year." In the labour market, the unemployment rate held steady in the three months to November, whilst wage metrics were firmer than expected and in proximity to record highs. Retail sales for December fell short of expectations, showing a 1% M/M and 5.8% Y/Y contraction as the cost-of-living crisis continued to squeeze the consumer. Public sector net borrowing (ex-banks) jumped to a record GBP 27.4bln from GBP 19.64bln and was around GBP 10bln higher than forecast by the OBR.

RHETORIC: Since the prior meeting, Governor Bailey has stated that the major risk to BoE's central case for inflation coming down is a UK labour shortage. In a subsequent speech, Bailey stated that the MPC does not target a particular peak in rates, adding that inflation is tracking to fall sharply, whilst there are signs that wages/pay are rising, but some of the forward-looking surveys of earnings don't appear to be as strong. Chief Economist Pill said that the “the longer that firms try to maintain real profit margins and employees try to maintain real wages at pre-energy price shock levels, the more likely it is that domestically- generated inflation will achieve its own self-sustaining momentum even as the external impulse to UK inflation recedes”. External member Mann has remarked that the UK inflation dynamic looks pretty robust, adding that households and firms see inflation at 4% in the years ahead. When asked about over-tightening Mann said "we are not there yet". Elsewhere, comments from other members of the MPC have been minimal.

RATES: 29/42 surveyed analysts by Reuters look for a 50bps hike in the Bank Rate to 4%, with the remaining 13 looking for a more modest 25bps adjustment. Market pricing agrees with consensus as 50bps is priced at around 82%. The decision to move on rates is expected via 7-2 vote with dissent again from Tenreyro and Mann who opted for unchanged in December. Within those backing a hike, there is the possibility of a split in views, the extent to which is particularly hard to judge given the lack of comms from the MPC since December. HSBC has attempted to form a base case with an out-of-consensus call for a 25bps hike in which Bailey, Cunliffe, Broadbent and Pill for 25bps, whilst Mann, Haskell and Ramsden back a 50bps move. Such an outcome is plausible on the basis that 25bps could be favoured by some MPC members as a middle-ground between the hawks and the doves. However, such a stepdown in the cadence of rate hikes would likely need to be accompanied by guidance that rates will still have further to run given developments in the labour market. As it stands, guidance notes that a "majority" of the Committee judges that further increases in Bank Rate may be required for a sustainable return of inflation to target. HSBC speculates that most of this wording will likely be retained, however, there is a risk that "majority" could be switched to "some". Elsewhere, Natwest Markets suggests a dovish tweak to the statement which could see the removal of the word "forcefully" from the following sentence "the Committee continues to judge that, if the outlook suggests more persistent inflationary pressures, it will respond forcefully, as necessary". Looking beyond February, a 25bps hike in March is priced at around 80% with markets split on whether a further 25bps would follow in Q2 to take the terminal rate to 4.5%.

FORECASTS: On the inflation front, HSBC expects that the impact of the stronger GBP and softer energy prices will likely outweigh the impact from stronger growth and lower rates, which should therefore lead to a downward revision to the MPC's Q4 2023 inflation forecast to 6.9% from 7.9%. Analysts at ING suggest keeping "an eye on the so-called ‘constant rate’ inflation forecasts, where the Bank assumes the Bank rate will remain unchanged from now on. If these show inflation at, or very close to, 2% in a couple of years' time, then that would be a sure-fire sign that policymakers think we’re close to the peak for Bank Rate". From a growth perspective, HSBC expects GDP to be revised higher due to near-term fiscal policy and the lower rates profile. HSBC expects 2023 growth to be revised higher to -1% from -1.5% and 2024 to -0.5% from -1%.

Current forecasts

Inflation: 2022 10.75%, 2023 5.25%, 2024 1.5%, 2025 0% Growth: 2022 4.25%, 2023 -1.5%, 2024 -1%, 2025 0.5%