PREVIEW: BoE rate decision and minutes due Thursday 22nd June 2023

- **BoE rate decision and minutes due Thursday 22nd June 2023 at 12:00BST/07:00EDT**
- **The MPC is expected to deliver another 25bps hike; will likely be subject to dissent**
- **Focus will be on how committed the MPC is to further tightening**

OVERVIEW: 64/64 economists surveyed by Reuters (pre-CPI data) expect the BoE to raise rates by another 25bps, taking the Base Rate to 4.75%. Following the release of the May inflation data, markets price in a 55% chance of a 25bps hike and 45% chance of a larger 50bps move (vs. 75% 25bps pre-release and 25% 50bps). Expectations for a more aggressive move from the BoE ratcheted up after latest CPI data saw the Y/Y headline rate hold steady at 8.7% vs. consensus 8.4% (MPC expected 8.3%), whilst core Y/Y advanced to 7.1% from 6.8%. In the labour market, headline earnings growth in the 3M/YY period in April rose to 6.5% from 6.1%, whilst the unemployment rate unexpectedly fell to 3.8% from 3.9% (consensus was for an increase to 4.0%). Focus will be on any tweaks to the Bank's guidance which notes that "if there were to be evidence of more persistent pressures, then further tightening in monetary policy would be required". In terms of market pricing, a total of 160bps (including June) is currently expected. However, many analysts suggest that this looks a bit aggressive with 50bps further hikes judged to currently be the base case.

PRIOR MEETING: As expected, the MPC delivered a 12th consecutive hike by raising the Bank rate by 25bps to 4.5% via a 7-2 vote split. Once again, Tenreyro and Dhingra voted for an unchanged rate on the basis that they judged prior tightening was yet to make its way into the economy. The MPC also opted to retain guidance that "if there were to be evidence of more persistent pressures, then further tightening in monetary policy would be required". The accompanying MPR projections showed upgrades to the inflation profile with the 2023 projection raised to 5.0% from 4.0%. Crucially, inflation in 2025 is seen materially below the MPC's 2% target at just 1% and therefore indicated that market pricing (upon which the forecasts are based) was too aggressive over the medium-term to be consistent with the BoE's goals. On the growth front, as was expected, 2023-2025 GDP projections were upgraded with the MPC no longer forecasting a UK recession. At the follow-up press conference, Governor Bailey avoided giving markets a "directional steer on rates", stating that policy will be guided by the evidence. Bailey did note however, that the Bank "must stay the course to ensure inflation returns to 2%".

RECENT DATA: The CPI data for May saw the Y/Y headline rate hold steady at 8.7% vs. consensus 8.4% (MPC expected 8.3%), whilst core Y/Y advanced to 7.1% from 6.8%. Pantheon Macro notes that "the pick-up was broad-based across components, and not obviously attributable to any one-offs". The May BoE Decision Maker Panel data saw the 1yr ahead inflation expectation rise to 5.9% from 5.6%, whilst the 3yr ticked higher to 3.5% from 3.4%. In the labour market, the unemployment rate in the three months to April unexpectedly fell to 3.8% from 3.9% vs. Exp. 4.0%, employment rose by 250k over the same timeframe, whilst the more timely HMRC payrolls measure for May showed a 23k M/M increase and headline wage growth advanced to 6.5% from 6.1% 3M/YY in April. On the growth front, M/M GDP for April rose 0.2% vs. the 0.3% contraction seen in the prior month. More timely survey data for May saw the service PMI print fall to 55.2 from 55.9, manufacturing slip to 47.1 from 47.8, leaving the composite at 54.0 vs. prev. 54.9. The accompanying release noted "there were again divergent trends across the UK private sector economy, as rising services activity helped to offset a fall in manufacturing production. Moreover, the latest decline in manufacturing output was the steepest since January". Retail sales in April grew 0.5% on a M/M basis vs. the 1.2% contraction seen in March. The ONS noted that "when compared with their pre-coronavirus (COVID-19) level in February 2020, total retail sales were 16.5% higher in value terms, but volumes were 0.8% lower".

RECENT RHETORIC: In terms of commentary from the MPC, Governor Bailey (13th Jun) has stated that the Bank has put more inflation persistence into its models and food inflation is taking a lot longer to come down than expected. Chief Economist Pill (15th May) stated (before April CPI data) that he liked to think the BoE had done enough and was concerned the UK economy had too much momentum. Deputy Governor Ramsden (18th May) noted that QT has had some effect on the economy, but it is fairly small, adding that there is potential for QT sales numbers to go up but does not see it going down. At the hawkish end of the spectrum, external member Mann (12th June) stated that services inflation is a concern and inflation expectations remain high. In previous comments (23rd May) she also remarked that financial conditions were not tight and could not make judgements about the peak in rates given that such a decision will be data dependent. External member Haskel (12th June) is of the view that it is important the BoE continues to lean against the risks of inflation momentum, adding that further increases in interest rates cannot be ruled out. From a move dovish perspective, dissenter Dhingra (13th June) remarked that there is no doubt that inflation, whilst beginning to ease off its peak last year, is still far too high relative to the 2% target. However, "lags in monetary policy transmission imply that there is little we can do to affect inflation in the immediate future, therefore focus should be on the medium term".

RATES: 64/64 economists surveyed by Reuters (pre-CPI) expect the BoE to raise rates by another 25bps, taking the Base Rate to 4.75%. Following the release of the May inflation data, markets price in a 55% chance of a 25bps hike and 45% chance of a larger 50bps move (vs. 75% 25bps pre-release and 25% 50bps). With a June hike nailed-on, attention will be on any guidance provided by the Bank. As it stands, existing guidance notes that "if there were to be evidence of more persistent pressures, then further tightening in monetary policy would be required". In terms of market pricing, a total of 160ps of tightening is currently expected. However, many analysts suggest that this looks a bit aggressive given the increased strain on UK homeowners remortgaging at higher rates. As such, many desks are of the view that a final 25bps hike in August will put the Bank Rate at terminal. Note, the upcoming release will not be accompanied by a MPR and therefore, the MPC will not have an explicit quantitative means by which they can push back on this pricing. It remains to be seen if the policy statement will object to such an aggressive rate path. As highlighted by ING, it is worth noting that inflation was already seen as being below target for the Bank over the medium term when the assumed rate was 5% and therefore, a projected rate at 6% would likely push any inflation forecast below the Bank's 2% threshold.