19 September 2024

Bank of England Review

Gradual easing cycle supports GBP

- **At today's monetary policy meeting the BoE left the Bank Rate unchanged at 5.00% as widely expected.**
- **The BoE delivered a hawkish twist to its guidance emphasising their gradual approach to reducing the restrictiveness of monetary policy. We think this supports our base case of the next cut in November and a pause in December.**
- **Gilt yields tracked higher and EUR/GBP moved lower on the hawkish vote split and communication.**

As expected, the Bank of England (BoE) decided to keep the Bank Rate unchanged at 5.00%. The vote split was 8-1 with the majority of members voting for an unchanged decision and dove Dhingra voting for a 25bp cut.

The BoE retained much of its previous guidance noting that "*monetary policy will need to continue to remain restrictive for sufficiently long until the risks to inflation returning sustainably to the 2% target in the medium term have dissipated further*" but added that "*In the absence of material developments, a gradual approach to removing policy restraint remains appropriate*". Combined with the vote split, this delivered a slight hawkish twist pushing back on market expectations of a cut at every meeting. While data on balance has been slightly better than expected compared to the August MPR, the BoE noted upside risks to pay growth. Likewise, the BoE noted that "*Bank staff expected services inflation to ease slightly further in Q4*", which at 5.6% y/y in August remains uncomfortably elevated.

We think the communication today further supports our call of a more gradual approach to a cutting cycle. We expect the next 25bp cut in November with the Bank Rate ending the year at 4.75%.

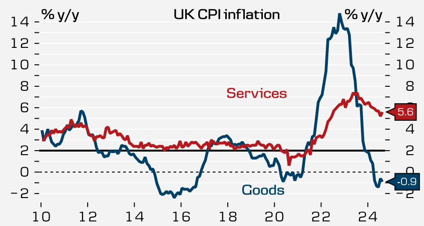
On QT, the MPC announced another GBP 100bn of quantitative tightening for the coming year starting October. Given the maturity profile, the largest part will stem from maturities (GBP 87bn) and to a much lesser extent from sales (GBP 13bn).

Rates. 2Y Gilt yields moved higher on the statement but overall, the reaction in rates markets was muted. Markets price 28bp for November and 14bp in December. We see it as more likely that the BoE will pause in December.

FX. EUR/GBP moved lower on the announcement following the slightly hawkish vote split and notion of a gradual cutting cycle. The guidance delivered today highlights the more cautious approach of the BoE, which supports our case of a continued move lower in EUR/GBP. This is further amplified by UK economic outperformance and tight credit spreads. The key risk is policy action from the BoE. We stay long GBP/CHF.

Our call. We expect the BoE to deliver the next 25bp cut in November and this to be the final cut this year, making it less than markets expect (42bp by YE 2024). In 2025, we expect cuts at every meeting starting in February and until H2 2025 where we expect a step down to a quarterly pace. This leaves the Bank Rate at 3.25% by YE 2025.

Chart 1. Elevated service inflation argues for a gradual cutting cycle.



Source: ONS, Macrobond Financial

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Expected updates

None

Date of first publication

See the front page of this research report for the date of first publication.

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