

Bank of England Review

Dovish outlook suggests more cuts

- The Bank of England kept the Bank Rate unchanged at 3.75%.
- The vote split was 5-4, which was a dovish surprise.
- The new economic outlook for the UK entails less growth and inflation.
- We continue to aim for the next rate cut in April and pencil in another cut in November.

The Bank of England (BoE) kept the Bank Rate unchanged at 3.75% as expected. The decision was taken with a 5-4 vote, which was a closer call than expected and as such the probability of a rate cut in March and of several cuts has increased in our opinion. With two labour market reports and two inflation prints ahead of the March meeting, much can still happen by then.

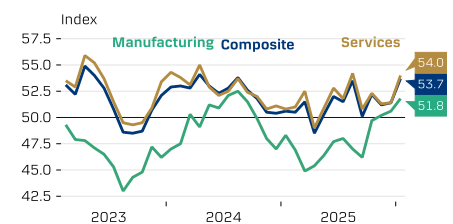
Dissenting to the decision to hold rates were Dhingra, Taylor, Ramsden and Breeden, with the latter two as surprise moves, considering how data, if anything, has come in on the hawkish side since the December meeting. In the MPC member views, they both highlighted new analysis in the monetary policy report as a key reason why upside risks to inflation have diminished. Here BoE staff find that *“structural changes in wage-setting will not keep adding to inflationary pressures”*.

In its monetary policy report, the new BoE outlook has a more dovish tone with both GDP and inflation forecasts lower and unemployment higher compared to November. CPI Inflation is now expected at 1.7% in 2027Q1 vs. 2.2% in the November report, while annual GDP growth has been revised 0.3pp lower to 1.2%. We highlight that recent PMI data had a particularly more hawkish flavour, with composite PMI at its highest level in three years and price indices suggesting more sustained inflation pressures. Upcoming data will judge what to make of this.

BoE call. Once again, the timing of the next rate cut is coming down to Governor Bailey. He clearly looks ready to cut rates further and said he finds the two cuts currently priced by markets as fair. The timing will hinge on incoming data, and we expect the bar for cutting further has been raised as the Bank Rate has closed in on neutral levels. We continue to aim for the next rate cut in April and pencil in another one in November.

Market reaction. EUR/GBP traded a bit higher on announcement, supporting our expectation for a further weakening of GBP. We aim for EUR/GBP at 0.89 levels on a 12M horizon on decreasing rate differentials, relatively weaker growth outlook in the UK and positive correlation to a USD negative environment.

Recent PMIs paint a very different picture than the dovish one set out in the new monetary policy report



Sources: S&P, Macrobond, Danske Bank

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