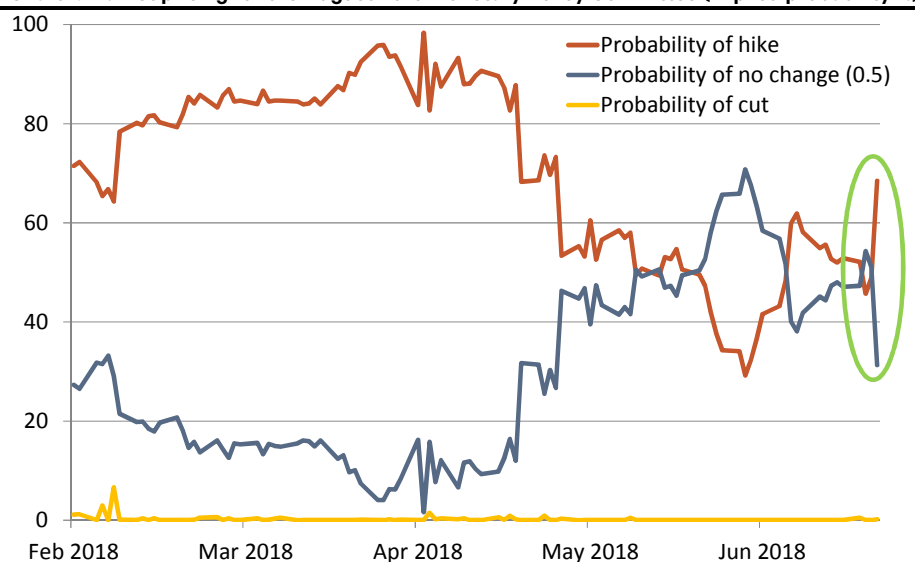


## Next BoE hike in August – Haldane the hawk

**Chart 1: Market pricing for the August 2018 Monetary Policy Committee (implied probability %)**



### Ready for another rate hike soon?

Today's surprise vote for a rate hike by the Bank of England's chief economist Andy Haldane shifts the balance of probability for the next hike to the August meeting. Previously we had called for a November hike, with a risk of a potential move in August already. However, the minutes from the June meeting show that, despite heightened uncertainty about the global economy linked to trade tensions, the Monetary Policy Committee (MPC) is confident that growth has rebounded to around its trend rate in Q2 (co.4% qoq) after a soft patch in Q1.

The MPC sees evidence of growing cost pressures in the labour market. Before today's MPC meeting, the market saw around a 50% chance of a hike in August. Today's minutes have firmed up the market's expectations for a rate hike in August – Chart 1.

### Have we been here before?

The Bank of England (BoE) seems to be re-opening the playbook it used ahead of the November 2017 rate hike. Step one, signal to markets that a hike could come soon. Step two, let a couple of known hawks dissent in a policy vote shortly thereafter. Step three, hike rates. However, the BoE went down this path ahead of the May meeting only to keep rates on hold. This casts some doubt over the probability of an August hike. Nevertheless, it is likely that the MPC had genuinely anticipated hiking in the run-up to the May meeting only to step back at the last minute due to the surprisingly weak Q1 data (0.1% qoq).

As the BoE continued to signal in May that rates would likely rise at some point during 2018, it was just a case of waiting for the MPC to signal when. Today, the addition of Andy Haldane to the group of MPC members voting for a hike – Michael Saunders and Ian McCafferty, both known hawks – is significant, in our view. As chief economist, Mr Haldane has a lot of influence over the bank's overall policy outlook. That he is not known for being especially hawkish strengthens our view that his vote is an early signal of where the rest of the committee will head soon.

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## Key snippets from the June minutes

“A key assumption in the MPC’s May projections was that the dip in output growth in the first quarter would prove temporary, with momentum recovering in the second quarter. This judgement appears broadly on track.”

“A number of indicators of household spending and sentiment have bounced back strongly from what appeared to be erratic weakness in Q1, in part related to the adverse weather. Employment growth has remained solid.”

“Although manufacturing output recorded a decline in April, and this was accompanied by a fall in goods exports, surveys of business activity have been stable and, as a whole, point to growth in the second quarter in line with the Committee’s May projections.”

“Most indicators of pay growth have picked up over the past year and the labour market remains tight, suggesting that domestic cost pressures will continue to firm gradually, as expected.”

“As in May, the best collective judgement of the MPC remained that...an ongoing tightening of monetary policy over the forecast period would be appropriate to return inflation sustainably to its target at a conventional horizon.”

## Of course, an August hike is not a done deal

As the BoE demonstrated in May, if the economy were to soften unexpectedly, it would hold rates in August and simply wait until the data improved. Markets should therefore pay close attention to the UK economic data between now and August and speeches by key MPC members – particularly governor Mark Carney and deputy governor Ben Broadbent.

We think the BoE will need to see three developments for a hike in August: 1) a sustained rebound in real GDP growth to at least the BoE’s estimated potential growth rate of 1.5% annualised yoy; 2) nominal wage growth at close to or above 3% yoy (currently 2.8%); and 3) survey measures that continue to point to rising underlying inflation and falling spare capacity.

## BoE could shrink its balance sheet earlier than projected

The minutes noted that the MPC “intends not to reduce the stock of purchased assets until Bank Rate reaches around 1.5%, compared to the previous guidance of around 2%”. After hiking in August 2018, we expect two further hikes in 2019. This would take the bank rate to 1.25% by the end of 2019. Therefore, in our view, it is likely that the BoE will begin to unwind its QE assets in 2020. We expect more details on the precise strategy next year.

## Summary of the June monetary policy decisions

“The governor invited the Committee to vote on the propositions that:

- Bank Rate should be maintained at 0.5%;
- The Bank of England should maintain the stock of sterling non-financial investment-grade corporate bonds, financed by the issuance of central bank reserves, at £10 billion;
- The Bank of England should maintain the stock of UK government bond purchases, financed by the issuance of central bank reserves, at £435 billion;
- The Committee intends not to reduce the current stock of purchased assets until Bank Rate reaches around 1.5%.

Regarding Bank Rate, six members of the Committee (the Governor, Ben Broadbent, Jon Cunliffe, Dave Ramsden, Silvana Tenreyro and Gertjan Vlieghe) voted in favour of the proposition. Three members (Andrew Haldane, Ian McCafferty and Michael Saunders) voted against the proposition, preferring to increase Bank Rate by 25 basis points. Regarding the stock of purchased assets, the Committee voted unanimously in favour of the second, third and fourth propositions.”

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