Markit Economic Research

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United Kingdom

Bank of England still sees little need for rate hikes before spring 2015

- **Bank of England hints economy edging closer to rate hikes**
- **Inflation and growth forecasts largely unchanged**
- **Improved job market outlook**

There were no big surprises in the Bank of England's updated outlook for the UK economy. The Bank's latest quarterly Inflation Report suggested that interest rates will not rise until the spring of 2015. Bank Governor Mark Carney noted that the economy was 'moving closer' to a rate increase, suggesting a rise in the first quarter may be on the cards instead of the second quarter. However, the Bank continues to believe that rates will most likely rise only gradually and remain 'low compared to historic rates'. Quite how low remained unspecified.

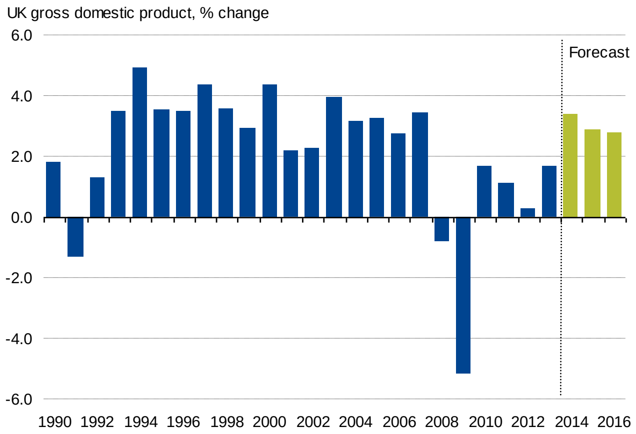
The only major change to the Bank's outlook was in respect to unemployment, which it expects to fall faster than in its February outlook and paints an even gloomier picture of ongoing disappointing productivity growth. Whereas in February it expected the jobless rate to be 6.4% in two years time, it now expects a decline to 5.9%. However, the Bank also indicates that it now believes unemployment can fall lower than previously thought (down to 5.25-5.75%) without generating inflationary pressures. Today's weak pay data alongside a further drop in unemployment supports this view. The forecast for consumer prices was unchanged, with the rate of inflation expected to be 1.9% in two year's time, just below the Bank's 2.0% target.

As for economic growth, the Bank is pencilling in a 0.8% GDP increase in the second quarter, which should help generate 3.4% growth for 2014 as a whole. The pace of expansion is then expected to weaken, albeit only modestly, to 2.9% in 2015 (a little higher than the 2.7% prior forecast) and 2.8% in 2016.

The report contained little reference to the housing market, and Carney reiterated that the recent rise in house prices was an issue to be dealt with by the Financial Policy Committee, all of which indicates that house prices will not affect the interest rate decision but that the FPC will use macro-prudential tools to cool the housing market and ensure financial stability. Carney went as far as to say that interest rates would be a 'last resort' in calming the housing market.

Alarm bells will ring for some as the Bank accepts that policy is being dictated by estimates of the amount of slack in the economy, which is notoriously difficult to measure, and that the Bank will 'learn as we go along'. With the Office for National Statistics set to completely rewrite economic history in wide-raging national accounts revisions in the autumn, the degree of uncertainty under which policymakers are operating should not be underestimated.

Bank of England GDP outlook



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