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06/08/2015

United Kingdom

Dovish Bank of England stymies chance of 2015 rate rise

- **Lone dissenter votes for 25bp rate rise, but markets had been expecting more hawks to appear**
- **Downgrading of 2015 inflation outlook reduces chances of near-term rate rise**

The latest Bank of England Monetary Policy Committee meeting saw one policymaker break ranks and vote for higher interest rates. But the tone of the meeting was more dovish than many were anticipating, meaning the first rate rise is unlikely to be seen until 2016, at the earliest. Most policymakers consider the recent fall in oil prices and the strong pound as likely to lead to a slower than previously thought upturn in inflation in the medium term.

Ian McCafferty was the sole MPC member voting for a 0.25% rise in borrowing costs, which is itself (somewhat paradoxically) a dovish-surprise, as the minutes from the prior meeting had built expectations that two or even three policymakers were starting to lean towards tightening policy.

Today's meeting therefore represents a more dovish than expected policy stance from the MPC as a whole, effectively removing the risk of rates rising in 2015. Bank Governor Mark Carney has stated that rates are likely to start rising around the turn of the year, and today's news will cement expectations that it's more likely to be after the New Year rather than before. Economists and the markets have been generally looking at rates rising in February, alongside the publication of the Inflation Report that month.

Inflation lower, growth stronger

The Bank believes the economy is on a firm recovery trend over the three-year forecast period and that inflationary pressures will build gradually alongside the steady erosion of spare capacity. Growth is now expected to reach 2.8% this year instead of a prior 2.5% forecast (though a slight slowing of growth in July suggests this may be somewhat optimistic, based on the GDP data available so far.)

The Bank's latest projection is for inflation to hit the 2% target within two years, based on the market expectations of rates starting to rise early next year. However, the outlook for inflation this year has been scaled back from 0.6% to 0.3%. The minutes also indicate that most members appear to consider the inflation outlook as having become more benign due to sterling's appreciation, which will reduce import costs, and the recent renewed fall in oil prices.

A minority of members continue to fear upside risks to the Bank's inflation outlook, and that consumer-driven growth could stoke higher-than-anticipated inflation, reinforced by a commensurate upturn in pay growth as unemployment continues to fall.

McCafferty in particular is concerned that delaying interest rate hikes will only lead to rates having to rise higher in the longer term.

However, the 'hawks' clearly remain vastly outnumbered by the 'doves', and the mass of information pushed out by the Bank today suggests that doves will continue to rule the roost at the Bank of England until at least early next year.

August was the first month in which the MPC meetings were published alongside the interest rate announcement.

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