

Bank of England: Crib Sheet for May meeting

Expect the Bank of England to buy itself more time as it keeps a watchful eye on the cracks appearing in the retail sector

No hike this month but an August rate rise looks likely

It's been a bit of a rollercoaster ride for UK rate hike expectations over the past couple of months. But in the end, we think the Bank of England will err on the side of caution and keep rates unchanged when it meets on Thursday. After all, a rate hike now could be one headwind too many for the faltering consumer-facing sectors.

But assuming the situation in retail doesn't get any worse between now and August, we think a rate hike over the summer still looks likely. With wage growth continuing to accelerate and global growth still (largely) heading in the right direction, we think policymakers are unlikely to have changed their minds when it comes to the prospect of further tightening. The Bank will also be conscious that Brexit noise could make it complicated to hike rates later in the autumn.

Markets are currently pricing a 50:50 chance of an August move, and there is a possibility that the Bank tries to subtly boost expectations. While we doubt we'll see any direct comments about the curve being too low this time, watch out for what the Bank has to say on growth, Brexit and wages, for signs that it is gearing up for further tightening in the months ahead.

Here's what we expect from the May meeting.

Four Bank of England scenarios for the May meeting

Bank of England view/comments						Market impact
No. of rate hike votes	Growth	Inflation/Wages	Brexit progress	Rate hike path		
① No rate hike Big rethink	0 Hike votes	Big outlook reassessment. Global growth slowing, consumer caution to persist	Core inflation set to fall more sharply; wage growth could be slower	Reintroduces language that there are "considerable risks" to the outlook	Removes signal that "ongoing tightening" required over "forecast period"	EUR/GBP +1.25% GBP/USD -1.75%
ING base case						
② No rate hike Buying more time	2 Hike votes	Lower near-term growth forecast. Partly snow, but also lower consumer/Eurozone growth	Lowers inflation forecasts a touch, but still looking for strong wage growth this year	Notes recent transition agreement, but restates Brexit is a "significant" uncertainty	Reiterates that "gradual" rate hikes are needed, but offers nothing more specific	EUR/GBP -0.25% GBP/USD +0.75%
③ Rate hike Stick to the plan	7 Hike votes	Factors driving weakness largely temporary. Risk of upward revision to 1Q GDP	Still expects 3% wage growth, cites evidence from Agents of sharper pay rises	Transition period "reduces likelihood" of disorderly Brexit, should "support" confidence	Hints could hike more than once in 2018. Doesn't say explicitly that market pricing is too low	EUR/GBP -1.75% GBP/USD +2.00%
④ Rate hike Full speed ahead	9 Hike votes	Factors driving 1Q weakness were all temporary (e.g. snow). Expects full rebound	Upside risks to wage growth. Sees risk of persistently above-target inflation	Upgrades medium-term growth profile following transition agreement	Tightening to be greater & earlier. Rates need to rise faster than markets expect	EUR/GBP -2.00% GBP/USD +2.25%

Source: ING, GBP forecasts from our FX Strategy team

Cracks appearing in consumer-facing sectors give reason for pause

As the Bank of England prepares to meet next week, it'll be well aware that hiking in the aftermath of the weakest quarterly growth reading since 2012 would be a tough sell. Admittedly some of the causes of the slowdown were temporary – multiple bouts of snow saw construction activity make an unusually large negative contribution to first quarter GDP. It's possible some of this gets revised up – and it'll be interesting to see if the Bank agrees on Thursday.

But the cracks appearing in consumer-facing sectors look more concerning. The perfect storm of weaker demand, higher business rates and rising minimum wage costs resulted in one of the worst quarters for retail since the financial crisis. A rate hike now might prove to be one headwind too many for retailers, many of whom have become highly leveraged in the post-crisis years. And things aren't set to get much better immediately – real incomes remain pressured by higher fuel and food costs (albeit the worst of the household squeeze has passed).

Alarmingly, consumer credit growth appears to have collapsed in recent months, with banks reportedly scaling back loan availability significantly. This may prove to be a blip, but we suspect the Bank will want to buy time until the underlying drivers of this rapid downfall become clearer.

Unlikely the Bank's pause this month will turn into a permanent hiatus

Away from the activity story, the major drivers underpinning the Bank's recent tightening bias have remained largely on track. The prospects for global growth still look relatively bright, despite the recent moderation in Eurozone activity. Similarly, wage growth has continued to outperform over the last few months, giving policymakers greater confidence that skill shortages in the jobs market are boosting pay. Bank agents have indicated that this could be the best year for pay settlements since the crisis.

Policymakers will also be acutely aware that their window to hike rates could close soon. If the build-up to the December and March EU leader's meetings is any guide, the months leading up to the October summit could see negotiations get increasingly noisy. At the same time, we expect to see core inflation fall back to target over the summer, given that prices have now virtually adjusted to the new value of the pound. This has seen inflation fall noticeably faster than the Bank of England was forecasting back in February.

These two factors could complicate efforts to hike rates as we get later into the year, and we think the Bank will be keen to capitalise while they can. Assuming that the faltering consumer sector doesn't deteriorate further, we think there's still a good chance the Bank will hike again in August.

[Find out why we still think the longer-term direction for sterling is up](#)

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