

## The Bank of England's February dashboard

Deteriorating economic data and increasing political uncertainty means we're unlikely to get a Bank of England rate hike any time soon - although the recent strength in wage growth means a move later in 2019 shouldn't be completely ruled out



Source: Bank of England

When the Bank of England announces its latest interest rate decision on Thursday, there will be just 50 days left until the UK is scheduled to leave the EU. With no clarity on whether a deal will be in place by then, or indeed if the 29 March deadline will be pushed back, there is little doubt policymakers will keep policy unchanged this week while likely striking a tone of greater caution.

Economic data is deteriorating, and it is likely growth will continue to stall (or potentially stagnate completely) through the first quarter as business and consumer caution grows.

This means a rate hike in the first half of 2019 looks very unlikely, but further tightening later in the year shouldn't be completely ruled out. With wage growth continuing to perform strongly, we sense that policymakers would like to raise rates again if they can.

Of course, whether they can or not depends almost solely on Brexit - a fact that is increasingly reflected in markets by their lower sensitivity to surprises in UK data.

Most paths now lead to an extension of the Article 50 negotiating period, which would prolong the uncertainty for longer. However if the government does gradually inch towards a cross-party solution on Brexit (for instance committing to a permanent customs union) that ultimately commands a majority for a deal, this would take 'no deal' off the table and allow the transition period to begin.

This scenario would likely see the Bank of England follow with further policy tightening, although admittedly such a solution still seems quite some way off. We very loosely have a rate hike pencilled in for August, although realistically this could easily come much later depending on which Brexit scenario materialises.

## Consumer spending



After a tough Christmas, the outlook for the high street hasn't improved in the new year. Consumer confidence is at the lowest level since 2013, driven by concerns about both the economic situation and personal finances. With the unemployment rate at a 43-year low and wage growth rising at the fastest pace since the crisis, it's hard to attribute this pessimism to anything other than Brexit uncertainty - in particular the impact 'no deal' could have on job security and finances. So while the fundamental backdrop for consumers is a little better, it's hard to see spending recovering markedly over the next few months.

## Wage growth



Wage growth is running at a post-crisis high, making it perhaps the one bright spot in an otherwise bleak economic picture. This emphasises that firms are having to lift pay more quickly in response to skill shortages in certain sectors - particularly in areas such as construction and hospitality. Admittedly, the appetite for firms to hire appears to be falling, which will add to some potential downside to wages over the coming months. For now, though, it seems more likely that pay will continue to perform solidly. This is a key reason why the central bank appears inclined to tighten policy further if it can later in 2019.

## Inflation



2019 looks to be a reasonably benign year for inflation. The impact of the pound's post-Brexit plunge has largely fizzled out of the year-on-year numbers. In the short-run, the headline rate may remain modestly sticky if oil prices continue to increase, as our commodities team forecasts. However one way or another, we expect headline CPI to end the year below 2%. Beyond then, higher wage growth should see core price pressures build, although this relies on corporates having sufficient pricing power to pass these costs on. In the current challenging consumer environment, that may not always be the case.

## Hiring



Job creation has shown a little more energy in the past couple of reports, following a lacklustre summer in 2018. That said, both the most recent manufacturing and services PMIs point to rare falls in employment. This implies that businesses are likely to continue to put new hires on hold, but also that unemployment could gradually rise in some sectors as new orders and backlogs decline. In the short-term, there is a risk that all of this could slip into the consumer mindset, further limiting household spending in the run-up to Brexit.

## Investment/manufacturing



With business optimism in the manufacturing sector at a 30-month low based on the latest PMI, the risk of the sector slipping into a recession looks like an increasing possibility. Order books are deteriorating, partly on Brexit uncertainty, but also on slower global demand growth. While inventory building ahead of Brexit appears to be taking place, a lack of storage capacity in the UK means that firms may have limited ability to stockpile components and goods.

## Author

**James Smith**

Developed Markets Economist

[james.smith@ing.com](mailto:james.smith@ing.com)

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