The Bank of England's November dashboard

Expect the Bank of England to retain an air of caution this week as a highly uncertain election campaign gets underway. Policymakers are still likely to notionally hint at future tightening if Brexit goes smoothly, although amid falling investment and stumbling jobs growth, interest rates are likely to remain on hold for the foreseeable future

Source: Bank of England

The Bank of England's November dashboard

Bank of England view/comments

	No. of rate hike/cut votes	Brexit	Growth	Inflation/Wages	Rate hike path
1 On hold	All agree (9-0)	Steps up warnings about risks of 'no deal' & prolonged uncertainty	Weaker global growth & Brexit uncertainty means more economic slack	Given weaker growth outlook, price pressures could become more muted	Removes tightening bias completely – risk one or two members even vote for rate cut
2 On hold	All agree (9-0)	Explicitly warns that transition period ('til Dec 2020) too short	Sizable downgrade to growth on trade war & Brexit uncertainty	Lowers wage growth forecasts given risk of lower excess demand	Makes tightening bias more nuanced given Brexit risks
ING base case: 3 On hold	All agree (9-0)	Warns of period of "entrenched uncertainty" but notes "good news" of deal being agreed	Modest downgrade to growth on global activity & investment weakness	Retains positive view on wages but says job market no longer tightening	Simply reiterates that "gradual", "limited" tightening may be needed
4 On hold	All agree (9-0)	"Significant increase" in investment if deal ratified	Keeps growth unchanged but hints upgrade possible if Brexit deal ratified	Wage growth to accelerate given large degree of excess demand	Hints that market pricing too dovish – signals rate cut unlikely

More hawkish

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Source: ING

The Bank of England's November meeting comes at another politically awkward moment for policymakers. The UK's general election campaign will, as of Wednesday, be formally underway. And with massive uncertainty surrounding not only the result of the December election, but also the outlook for Brexit and therefore the UK economy in 2020, policymakers are likely to remain cautious this week.

Here are three things to look for from Thursday's announcement...

1 Growth forecasts to be revised down amid investment uncertainty

We're likely to see the Bank of England nudge down its growth forecasts for 2020 this week. That's partly down to weakness in the global economy – the Bank's August projection for 1.5% eurozone growth next year looks particularly optimistic relative to our own forecasts.

But the bigger challenge to the UK outlook in 2020 comes from investment. The BoE already expects capital spending to fall again next year, and it's possible policymakers lower these forecasts further this week.

The key question is what happens if a Brexit deal is approved by Parliament early next year. That's what most believe will happen if the Conservatives gain a majority in December's election. BoE

Governor Mark Carney suggested last month that ratification of the Brexit deal could translate into a “rebound in some” investment.

However we are less convinced. Even if the deal is ratified and the UK leaves the EU by the end of January, focus will quickly shift to the transition period. This standstill phase, where the UK’s trading relationship remains unchanged, will last until the end of 2020. But this almost certainly won’t be long enough – either to agree a new trade agreement with the EU, or to set up the necessary border infrastructure and staffing required to keep shipments flowing.

Prime Minister Boris Johnson will need to sign up to EU budgets beyond 2020 to unlock the extension most believe is necessary, and this will undoubtedly be controversial. That needs to be resolved by the end of June for the transition period to be extended, otherwise the UK (with the exception of Northern Ireland) risks leaving the single market and customs union at the end of next year – a result that for most firms will be fairly indistinguishable from ‘no deal’.

In the meantime, this uncertainty will keep a lid on investment.

2 Jobs market no longer tightening - risks to wage growth?

The persistent Brexit uncertainty is also beginning to take its toll on the jobs market. A lack of investment means new order levels have fallen, including in the service sector where a lower appetite to expand means less demand for things like finance/professional activities. With less capacity required, demand for new hires is slipping.

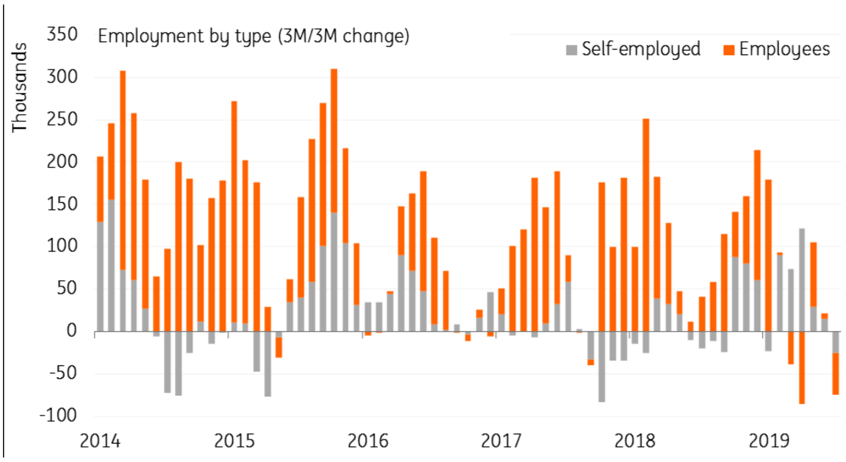
It's still early days, but vacancy levels have declined consistently through 2019, albeit they still remain high by historical standards. Employment growth fell in the three months to August, and what is particularly striking is that the total number of employee jobs has fallen marginally so far this year. In both the manufacturing and service sectors, the recent PMIs suggest firms are actively beginning to make redundancies.

All of this, in turn, poses questions for wage growth. Accelerating pay growth has been at the centre of the Bank of England's hawkish rationale over recent years, but that could begin to change if slack continues to emerge in the jobs market.

However it's worth remembering that the recent rise in wage growth has not solely been driven by cyclical factors. Structural constraints are at least partly to blame for the skill shortages in various UK sectors. In some cases, demographics (high rates of retirement) are reducing the pool of available workers. In others, the noticeable reduction in incoming EU citizens citing "work" as their reason for movement, is reportedly leading to staffing problems. Neither of these challenges are likely to disappear imminently.

For now, we expect the Bank of England to retain its constructive view on wage growth, although we may see a greater emphasis on the risks to the jobs market at this week's meeting.

Figure 1: Employment growth has been partially held up by self-employment



Source: Macrobond

3 Tightening bias retained

Having said all of the above, we still expect the Bank to notionally retain a tightening bias – a reminder that if Brexit ultimately goes smoothly, rates still may need to rise.

Realistically, this is unlikely to happen any time soon. But the fact that the BoE is maintaining a tightening bias at all, does hint that policymakers are – and will likely remain - reluctant to follow the Federal Reserve and European Central Bank in the direction of policy easing in the near future.

GBP: Bank of England playing second fiddle to the early election

The BoE meeting should have a fairly limited impact on the pound given that:

1. The outcome of an early election should be the prime GBP driver in coming weeks
2. The BoE's interest rate path is conditional on the outcome of Brexit talks.

As the latter is firmly tied to the former, the BoE meeting and its interest rate path (and the continued signalling of a hike) should have a muted impact on GBP. The signal that monetary policy could eventually tighten is not overly relevant given the Brexit uncertainty.

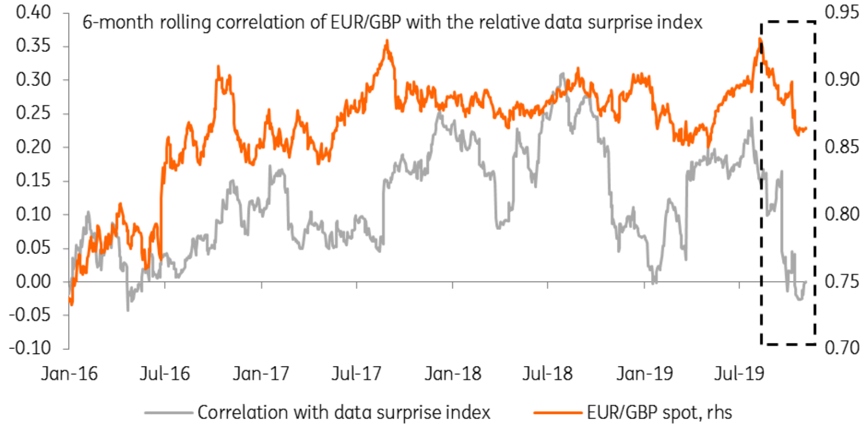
Indeed as Figure 2 shows, the correlation of sterling to economic data surprises is currently non-existent. The sole driver of the GBP rally last month was the changing perceived odds of a 'no deal' Brexit rather than economic data points. This also suggests a limited impact of the BoE's guidance on GBP at this point.

GBP gains have stalled recently and we don't see many catalysts for further upside from here as:

1. The Conservative party election victory is widely expected
2. The passage of the Withdrawal Agreement Bill is not an imminent topic
3. There is inherent uncertainty associated with early elections.

Should the pre-election polls start to show an increasing likelihood of a hung Parliament (the latest ICM voting intention poll shows a narrowing gap between the Conservatives and Labour), EUR/GBP is likely to move closer towards the 0.8800 level.

Figure 2: Non-existent correlation between UK data surprises and GBP moves



Source: Bloomberg, ING

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