

UK finished with rate hikes as inflationary pressures ease

Assuming the encouraging trends on price-setting behaviour persist, we think the Bank of England will opt against a further rate hike in May



Governor of the Bank of England Andrew Bailey arrives at London School Of Economics, ahead of a speech - March 2023

Source: Shutterstock

Inflation is heading in the right direction

Amid the turmoil in global markets, the Bank of England's March meeting was an exercise in keeping its options open. It hiked by 25bp – its smallest hike for some time – and the Bank's Governor, Andrew Bailey, has since insisted further rate rises are possible should the data require them.

For now, the data that matter have as been pointing in the right direction on inflation. Perhaps most importantly, the official wage growth numbers finally look like they've peaked. The Bank's own Decision Maker Panel survey – which polls CFOs across the UK – has been pointing to less aggressive planned price and wage rises over the coming months. Inflation expectations among both businesses and consumers have begun to ease too.

The official inflation numbers have been more mixed, and core services CPI was higher than the Bank would have liked in February (it rose from 5.6% to 6.4%, by our estimates). But we do expect some gradual improvement here in the months ahead, and we think the recent collapse in

wholesale gas prices will alleviate some pressure.

While it's easy to think this is more consequential for goods categories, an official ONS business survey found that 80% of hospitality firms that raised prices in recent months attributed it to higher energy prices, compared to 46% who cited labour costs. With wholesale costs now lower, the same logic probably applies in reverse.

In short, if the recent trends in inflation and wages continue then we think the Bank of England is done with rate hikes.

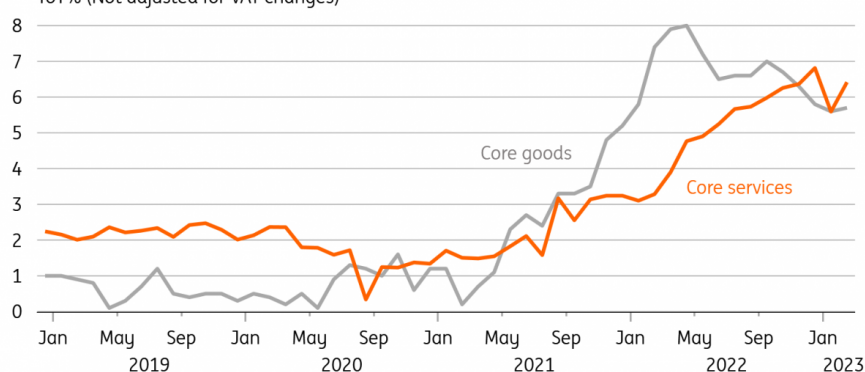
Even before the latest developments in the banking sector, policymakers had been emphasising that much of the impact of past rate hikes was still to come through, which in part is because 90% of UK mortgages are on fixed-rate products.

Policymakers have effectively set a much lower bar for pausing rate hikes over the coming months.

Core services inflation should begin to ease on lower gas prices

UK core inflation measures

YoY% (Not adjusted for VAT changes)



Source: Macrobond, ING calculations

Core services inflation excludes air fares, package holidays and education. Core goods excludes food, energy, alcohol and tobacco. Series vary slightly from BoE estimates, partly due to lack of VAT adjustment

Rate cuts may be some way off (banking crisis dependent)

That's not to say the descent in core inflation is going to be rapid. While wage growth might have peaked, the structural issues in the jobs market – long-term sickness being a major example – haven't gone away. Hiring demand is undoubtedly fading, and recent reports of redundancy notices to the government have picked up. But worker shortages are still likely to remain an issue for many businesses given constraints on labour supply.

Barring a material deterioration in the health of the banking sector, this 'sticky' inflation story suggests we shouldn't expect the first BoE rate cut until 2024.

Author

James Smith

Developed Markets Economist, UK

james.smith@ing.com

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies).* The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit www.ing.com.