

## Bank of England tapers QE amid recovery optimism

The Bank of England has tapered its QE pace, and the next step will be to offer up clues on how it might reduce its bond holdings alongside future rate hikes. But despite growing optimism about the recovery, we think a more benign inflation story next year is likely to see the Bank hold off on tightening until 2023



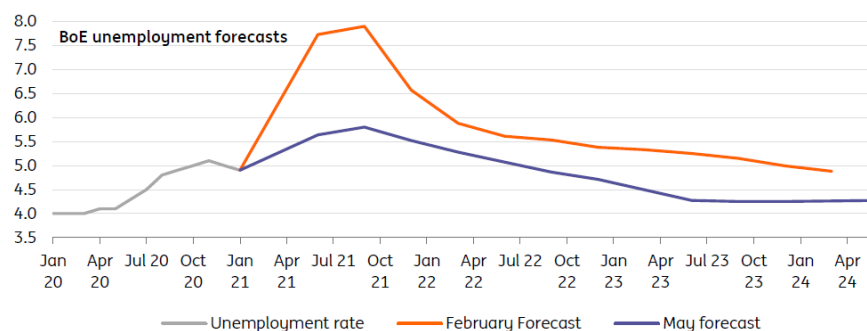
### Growing optimism in the recovery

Amid rising vaccination rates and receding Covid-19 transmission, the Bank of England has upgraded its assessment for the coming months. The Bank was arguably already towards the more optimistic end of the spectrum when it came to forecasts, but the positive news since the February update has given the committee confidence to make some further upgrades.

The Bank of England now expects the economy to meet and possibly exceed its pre-virus level later this year, while the unemployment rate is now expected to rise considerably less than previously thought this year. Like us, the Bank clearly feels that the extension of the furlough scheme until a few months after the formal reopening process is expected to have been completed, should give firms enough time to get back on their feet and bring most employees

back to work. We currently expect the jobless rate to peak around 6%.

## The BoE has significantly reduced its unemployment forecast for this year



Source: Bank of England

## From tapering to tightening

Importantly, this growing confidence in the recovery has enabled the Bank to cut the weekly pace of its asset purchases. This shouldn't come as a huge surprise – the BoE expects its gilt holdings to reach £875bn by year-end and at the recent £4.4bn/week pace, they'd have reached this target months too early. The new £3.4bn/week pace, while a little higher than we'd expected, is more consistent with purchases continuing until later in the year.

With tapering out of the way, the next question is how – and when – the Bank of England will enter a formal tightening cycle. There was a bit of excitement today with Chief Economist Andy Haldane's vote to reduce the asset purchase target, effectively meaning gilt purchases would end in August. It's worth remembering though that Haldane is easily the most hawkish committee member, and he has also recently announced his forthcoming departure from the Bank.

For now, the Bank is taking a leaf out of the Federal Reserve's book, offering a fairly vague signal that tightening won't come until the recovery has made "significant progress". However in the not-too-distant-future, we expect the Bank will offer further details on how it might reduce its gilt holdings alongside future rate hikes.

Governor Andrew Bailey has hinted in the past that this would help to increase space to 'go bold' again in future if a rapid pace of purchases was necessary. As we explained in [more detail this week](#), we think this might initially involve stopping/reducing reinvestments of proceeds from maturing bonds, perhaps by setting an annual 'unwind' target. That approach could enable the Bank to reduce its bold holdings by say £30-40bn per year.

When might this – and rate hikes – come? We doubt it will happen before 2023, partly because we think the inflation story will be less exciting in 2022, once some of the reopening-related price spikes have faded.

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