Caution grows at Bank of England as Brexit risks linger

The Bank of England's language looks increasingly cautious, emphasising that the prospect of fresh tightening looks more distant. That said, the fact that policymakers are still flagging the faint possibility of rate hikes hints that the BoE will remain reluctant to follow the Fed and ECB towards easing in the near future

Source: iStockphoto

The Bank of England has unanimously voted to keep rates on hold but as has been the case for the past couple of meetings, there is an increasing air of caution creeping into the narrative.

The thing that really stands out to us in this latest statement is that the Bank appears to be getting more wary about the outlook for wage growth. Don't forget that this has been a key pillar of the Bank's hawkish rationale over the past couple of years, and came amid increased skills shortages in the jobs market.

But while policymakers continue to emphasise that pay growth has strengthened, they note that the labour market "does not appear to be tightening further". Importantly, policymakers note that "political events" could lead to another prolonged period of "entrenched" uncertainty – and this, in turn, could hurt prospects for inflation.

At the very least, this just signals that Brexit will likely continue to dash any thoughts of policy tightening over coming months.

Admittedly, the perceived risk of 'no deal' appears to have decreased over the past couple of weeks following Parliament's legislative efforts to force a further delay to the Brexit process. However, the path for the UK's EU exit remains considerably uncertain. In our opinion, the chances of a deal being agreed, then approved by the UK Parliament during October, remain relatively low.

An election, coupled with an Article 50 extension, still looks likely. This means that the risk of 'no deal' could easily come back to the fore again, depending on who is in government after voters go to the polls.

In short, while the Bank still notes that rates may need to rise if Brexit goes smoothly, the risks surrounding Brexit, as well as global growth, mean this tightening is increasingly unlikely to materialise.

Having said that, 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.

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