

Bank of England Review

Not much news in the minutes as we are awaiting the Inflation Report

- As expected, the Bank Rate and the stock of purchased assets were unchanged at 0.50% and GBP375bn, respectively. The rate vote count was unchanged at 8-1.
- There was not much news in the minutes. The lower oil price has lowered the inflation outlook further, growth seems to have slowed down a bit and risk appetite is poor. The weaker GBP pulls somewhat in the other direction.
- The next meeting is due to take place only three weeks from now. At this meeting, we expect focus to be on the updated Inflation Report.
- We think the Bank of England (BoE) will increase the Bank Rate in Q2 16, probably in May, but recognise that it sounds less and less ‘Fed light’.
- We still target EUR/GBP in 0.73 in 3M and 0.71 in 6M.

Voting

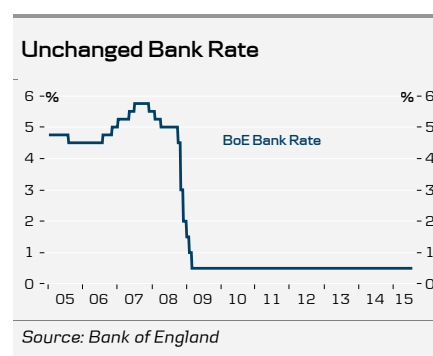
As expected, the Monetary Policy Committee (MPC) kept the Bank Rate and stocks of purchased assets unchanged at 0.50% and GBP375bn, respectively. The vote was once again 8-1, as Ian McCafferty still voted in favour of increasing the Bank Rate by 25bp immediately. Up to the meeting, there had been some discussions among analysts whether McCafferty would change his mind. However, as the labour market has continued to tighten, we do not share this view. The minutes still state that there is a ‘range of views’ among the MPC members.

We now expect BoE to hike in Q2 16, probably in May

The ‘tone’ in the minutes was more or less as expected. The lower oil price since the December meeting has lowered the inflation outlook further, growth seems to have slowed down a bit and risk appetite is poor. The weaker GBP pulls somewhat in the other direction. So, in reality, there was not much news in the minutes. One reason is that the next meeting is due to take place only three weeks from now. In our view, the February meeting is much more important as the updated Inflation Report is due to be released alongside the rate announcement, which should give us more insight into how the recent development has affected the BoE’s outlook for growth, employment and inflation.

We continue to expect the first BoE hike in Q2 16 (probably in May) but recognise that the BoE sounds less and less ‘Fed light’ despite strong developments in the labour market. One explanation is that monetary policy in the UK depends on the oil price and the economic outlook in Europe to a larger extent than Fed policy. We have kept our FX forecasts unchanged.

We target EUR/GBP 0.73 in 3M, 0.71 in 6M and 0.75 in 12M. In the short term, we expect GBP to remain under pressure in a negative risk environment. However, GBP is significantly oversold, according to our short-term financial models, and we still look for a rebound in the coming three to six months, driven by a repricing of the BoE, as we expect the UK economy to continue to grow above trend in 2016.



Pre-conditions for BoE raising rates

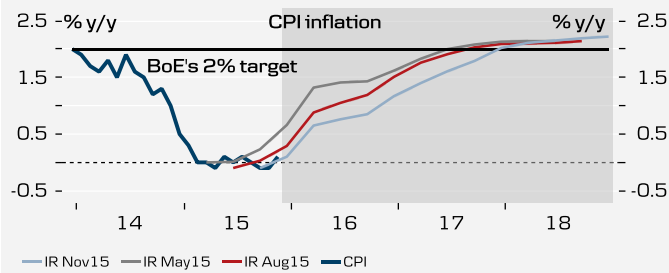
Condition	Status
Unemployment < NAIRU	✓
Wages > 2 %	?
Solid growth outlook (above or at trend 0.5% q/q)	✓
CPI inflation moving higher	✗
Pass-through from stronger GBP	?
No financial stress	✗

Source: Danske Bank Markets

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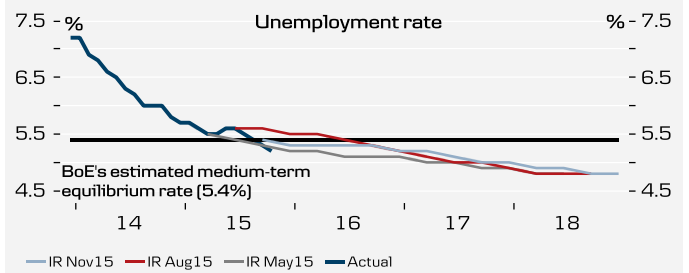
Charts

Lower oil price means the inflation profile is likely to be lowered in the updated Inflation Report in February



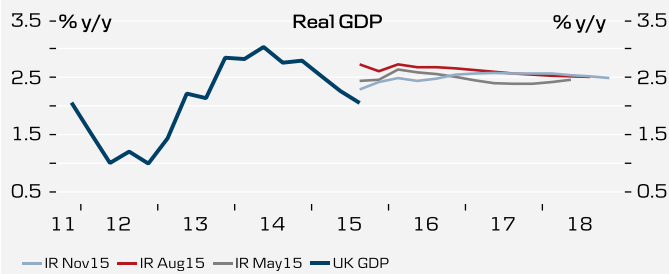
Source: Office for National Statistics, Bank of England

Unemployment is likely to be revised down further as once again it has fallen further than expected



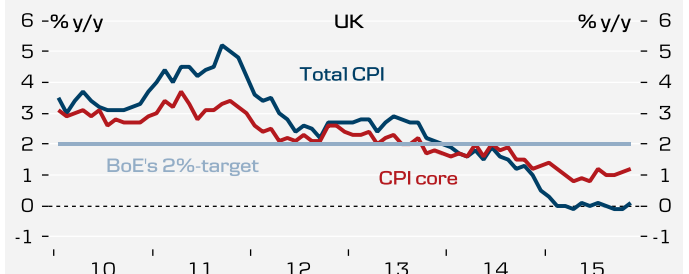
Source: Office for National Statistics, Bank of England

Growth has slowed, Inflation Report will look into this



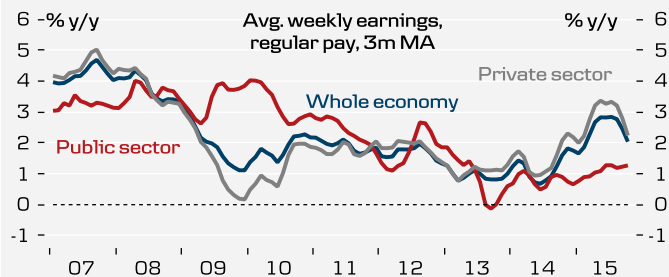
Source: Office for National Statistics, Bank of England

Very low CPI inflation



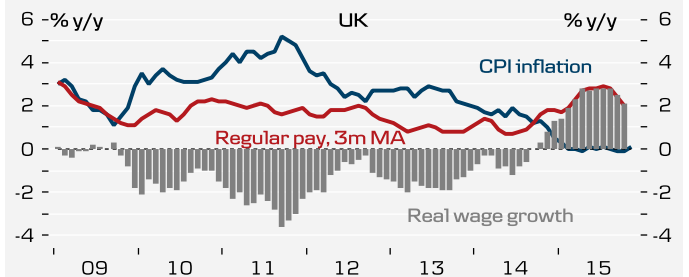
Source: Office for National Statistics

Subdued wage inflation in recent months is a concern



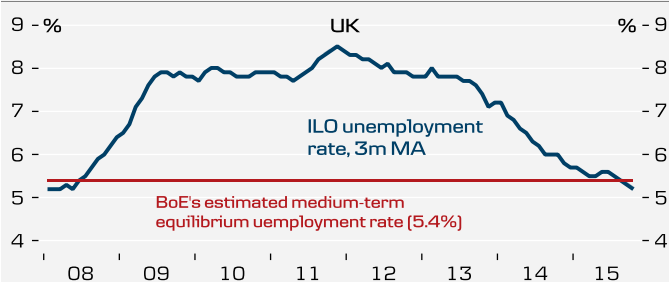
Source: Office for National Statistics

Positive real wage growth supports growth



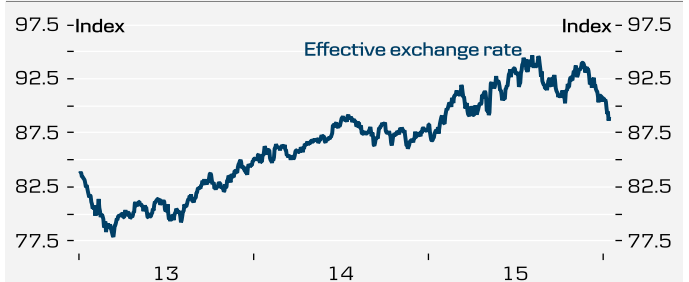
Source: Office for National Statistics

Unemployment rate more or less 'normal'



Source: Office for National Statistics, Bank of England

BoE less worried about GBP as it has weakened in recent months



Source: Bank of England

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