Bank of England (BoE) maintains status quo

In line with market expectation, the Monetary Policy Committee (MPC) voted unanimously in favour of maintaining status-quo in its policy decision today, keeping the official policy rate unchanged at 0.25%, and voting by a majority of 7-1. Kristin-Forbes (hawk) was the sole member to vote for a hike by 25bps.

On asset purchase plan, the Committee voted unanimously to continue with the programme of Sterling non-financial investment-grade corporate bond purchases totalling GBP 10bn. The programme of GBP60 bn of UK government bond purchases is also being continued to take the total stock of these purchases to GBP435bn.

Highlights of the policy statement

Following were the highlights of the statement.

- **GDP growth broadly in line with February projections**: While the committee lowered its 2017 growth forecast to 1.9% from earlier 2.0%, 2018 and 2019 forecasts were raised to 1.7% and 1.8% respectively from earlier estimate of 1.6% and 1.7% respectively. In the near term, the committee expects a little more inflation with prices rising faster than wages in 2017, intensifying the squeeze on household incomes, but consumption weakness is expected to improve during 2018 as inflation falls back and wages rise, leading to better slightly better growth projections in 2018 and 2019. The BoE said that its latest forecasts assumed "that the adjustment to the United Kingdom's new relationship with the European Union was smooth".

- **Inflation expected to remain higher on account of Sterling depreciation**: The committee expects inflation to peak in Q4'17 around 2.82% on account of sharp Sterling depreciation post Brexit and then fall slightly while still remaining above BoE’s threshold level of 2% for next three years. 2017 inflation forecast was raised to 2.7% from earlier 2.4% whereas 2019 was lowered to 2.2% from earlier projection of 2.5%. The committee said that it expects the squeeze on household incomes from higher inflation to ease later in the year and a recovery to be aided by higher business investment and exports.

- **Higher inflation or growth trigger for policy tightening**: While the committee's current inflation projections account for fall in Sterling, and modest wage growth consistent with the committee's assessment of slack in labour market, any significant sharp uptick in growth or inflation may prompt MPC members to consider towards reducing policy accommodation. It further added that if the conditioning assumptions underpinning May inflation report remain broadly on track, then Monetary policy could be tightened by a somewhat greater extent over the forecast period than the very gently rising path implied by the market yield curve.

Future course of monetary policy

While the committee is still balancing downside risks to growth and upside risks to inflation, we think that it’s still too early to decide about BoE’s future policy accommodation or normalization. Recently released data (GDP growth, retail sales, and industrial production) were mostly below expectations and consequently we would like to await further data print to decide on future direction of BoE’s policy decision. Currently, we expect the central bank to maintain status-quo in 2017.
Sterling expected to remain range-bound
Post the announcement of snap elections by UK Prime Minister Theresa May, we changed our stance on Sterling from bearish to neutral on account of Conservative party gaining significant majority in elections, giving May the power to get a better deal while negotiating with EU. The announcement also increases the chances of “smooth Brexit”. Consequently, we maintain neutral stance on Sterling, expecting it to trade in the range of 1.25-1.30 against US Dollar in the near future.
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