



MONTHLY UK ECONOMIC BRIEFING

MAY 2018

KEY POINTS

- The Bank of England’s Monetary Policy Committee (MPC) voted by 7-2 to keep rates on hold at 0.5%, with no change in asset purchases and corporate bond holdings at GBP435bn and GBP10bn respectively.
- This was largely down to the weak preliminary estimate of Q1 2018 GDP growth, which came in at 0.1%, below the consensus of 0.3%.
- The MPC meeting minutes reveal members are keen to see how the data unfolds over the coming months.
- Over the medium term, the inflation forecast is relatively unchanged. As a result there is little change in the Bank’s view, only the tone is slightly softer.
- Despite the MPC emphasising that growth does not need to be that strong for policy to tighten, it is beginning to look as though the window for 2018 rate rises may have closed.



Preliminary estimate of Q1 18 GDP growth

0.1%



In March the RPI rate was

3.3%



Current Bank rate

0.5%



BoE’s annual 2018 GDP growth forecast

1.4%



In March the CPI rate was

2.5%



UK 10-Year Bond yield (April)

1.51%

Sources: ONS, BNP Paribas, BoE and Macrobond

CONTACTS



Damian Cronk
Head of Commercial Markets
damian.cronk@realestate.bnpparibas
+44 (0)20 7318 5065



Sukhdeep Dhillon
Senior Economist
sukhdeep.dhillon@realestate.bnpparibas
+44 (0)20 7338 4834



Thomas Grounds
Research
Thomas.Grounds@realestate.bnpparibas
+44 (0)20 7318 4676



UK ECONOMIC UPDATE

The Bank of England's Monetary Policy Committee (MPC) voted by 7-2 to keep rates on hold at 0.5%, with no change in asset purchases and corporate bond holdings at GBP435bn and GBP10bn respectively. This was largely down to the weak second estimate of Q1 2018 GDP growth, which came in at 0.1%, below consensus of 0.3%. A slowdown had been expected, given snow disruption in late February and early March. The largest sector, the services sector, increased by 0.3% overall in the first quarter, production output was estimated to have increased by 0.6% while construction output was estimated to have decreased by 2.7%. This is the weakest growth for the construction sector since Q2 2012.

The next GDP release on 29 June will feature the large annual revisions exercise the Office of National Statistics is undertaking, so there is a higher chance of changes to the underlying GDP growth then. As of now however, official data on UK's GDP growth suggests it was a very weak first quarter.

The MPC meeting minutes reveal members

are keen to see how the data unfolds over the coming months to discern whether the softness points to a change in the underlying growth.

Little change to BoE's forecasts

Given the weakness of GDP growth in Q1, 0.3ppts weaker than expected in the February Inflation Report, the BoE's growth outlook remains relatively unchanged. The MPC strongly believe that the Q1 growth figure will eventually be revised up to 0.3% q-o-q with some bounce back expected in the near term.

The GDP growth forecast for 2018 has been revised down from 1.8% to 1.4%, but that is entirely a result of the weak Q1 GDP figure.

Over the medium term, the inflation forecast is also relatively unchanged. As a result there is little change in the Bank's view, only the tone is slightly softer.

Despite the MPC emphasising that growth does not need to be that strong for policy to tighten it is beginning to look as though the window for 2018 rate rises may

have closed. After leaving interest rates unchanged at the May meeting, policy makers are left with just seven meetings before the UK's official departure date at which they could potentially push rates higher.

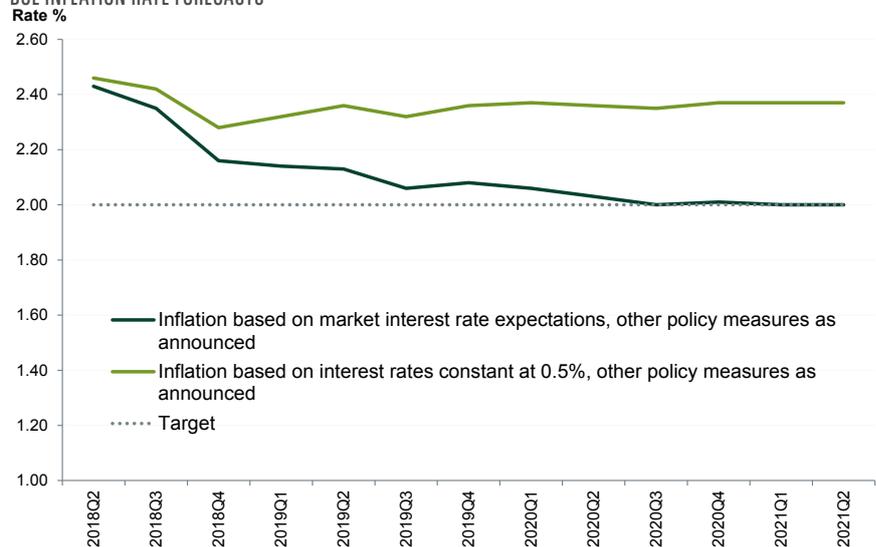
We are also five months away from a critical juncture for Brexit negotiations. The EU's chief negotiator has said negotiations must be complete before the end of October to give the 27 EU countries time to sign off the deal.

By autumn, inflation could be close to target and although the transition agreement has gone fairly smoothly this could change - resulting in potential political volatility later this year, which warrant rates to remain on hold at least until the end of this year.

On the upside, if the labour market strengthens further, a rate rise in August or later in 2018 is a distinct possibility. Markets are currently placing a 50% chance of the August rate rise taking place.

“The bullish outlook for inflation provides the case for the MPC's prospective further rate increases. The MPC forecasts if interest rates stay at 0.5% inflation would overshoot the 2% target.”

BOE INFLATION RATE FORECASTS



Source: Bank of England