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**FLASH REPORT**

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# BoE: 'Finely Balanced' Cut with 'Careful' Guidance Points to September Hold

- **The Bank of England kicked off its easing cycle today with a 25bps policy rate cut to 5.00% in a 5–4 vote split with hawkish tinges. That Gov Bailey and Chief Economist Pill were in opposite camps, cut vs hold, also suggests today's was a relatively low conviction cut.**
- **The BoE saying that they "have to be careful not to cut interest rates too much or too quickly" materially dampens odds of another cut at the September decision. We expect cuts to resume in November, with a 25bps move then matched in December.**
- **The BoE highlighted in its MPR a narrower measure of services inflation that should guide markets in gauging policy success in the two CPI prints before the September announcement.**

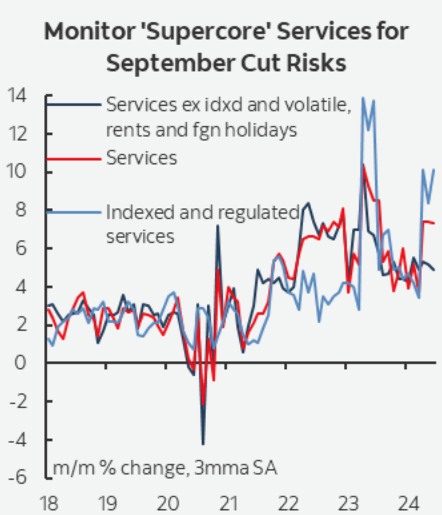
The Bank of England kicked off its easing cycle today with a 25bps policy rate cut to 5.00%. The move was in line with the bias of markets and economists going into the decision, but with 'only' 15bps priced in and practically all analysts calling it 'too close to call' it really looked like anyone's guess for what the Bank would decide today. We were marginally in favour of a rate hold today followed by a cut in September. Instead, we will probably see the inverse, with a cut today and a hold at the next meeting, as guided by the relatively hawkish tone of today's communications. We maintain our expectation for two more 25bps cuts in 2024, both of these in the fourth quarter.

How did the BoE manage to deliver a hawkish hold decision? First, the MPR right away states that "this decision was finely balanced. The risks of higher inflation remain. We need to make sure inflation stays low. So we have to be careful not to cut interest rates too much or too quickly." This is a very strong signal that the BoE is not yet eyeing another move in September. The onus is on incoming data and the BoE is starting from zero and sticking to its strict meeting-by-meeting approach; Bailey completely dodged when asked about this at the presser, sticking to data dependency. Unchanged guidance on policy having to "remain restrictive for sufficiently long" means that the cutting cycle will be slow in its early days.

Second, the vote breakdown of 5–4 suggests that Gov Bailey had to act as a tiebreaker, aligning with the camp where, for some, "the decision was finely balanced". Maybe he preferred the opportunity of the once-a-quarter post-decision press conference and release of the Monetary Policy Report (MPR) to explain in greater detail why they've begun an easing chapter. It may not have been a high conviction move for Bailey, as reflected by his neutral tone in the presser. Maybe they're going the way of the ECB, which looks on track to roll out its first three cuts on the occasion of its quarterly forecasts review. The BoE's next MPR release is in November.

Third, and finally, we thought that, were the BoE to cut rates today, it would have been a 6–3 cut-hold split. Most notably, we saw Chief Economist Pill and Gov Bailey voting together. That the former, whom one would think is the authority on the state of the economy and whether policy is too restrictive, did not think the time is right sends an important signal about the BoE's next steps. For us, a solid reason for delaying a first would-be cut was the chance to monitor two more CPI and jobs/wages releases between now and September. Pill probably wants greater confidence before voting for cuts. The minutes note that the four members preferring to hold would do so "until there was stronger evidence that these upside pressures [second-round effects, more entrenched underlying domestic inflationary pressures, etc.] would not materialize."

**Chart 1**



Sources: Bank of England, Scotiabank FICC/Economics.

The BoE's forecast revisions did not surprise but, at the margin, support the view of the 'holds' given the higher near-term inflation and GDP growth path. Notably, the BoE now sees services inflation at 5.5% in September 2024, compared to the 4.7% it had penciled in for this month back in the May MPR. While this mostly reflects the fact that, for instance, June inflation overshot the May MPR's projection by 0.6ppts (actual 5.7% vs forecast of 5.1%), it is still a risk that the likes of Pill weighed in favour of a rate hold. At year-end, services inflation is seen at a still very high 5.3% which looks like a tough environment in which to continue cuts.

However, the BoE's MPR (and Bailey in his presser) highlight a more benign trend observed in a narrower measure of services inflation (chart 1) that excludes volatile or indexed components, among others. This should become the guide for markets in gauging policy success in the two CPI prints before the September announcement. If the seasonally-adjusted 3-month moving average pace of prices growth in (call it) 'supercore' services remains around 5%, then the BoE will have a clear reason to hold in September.

Market reaction (14.15UK/9.15ET)

- As is often the case, US data releases soon after the release of the BoE's statement and near the end of Bailey's presser makes it trickier to read the market's clean interpretation of the BoE's communications. Still, when markets were pricing in 15bps in cuts for today's decision and in fact we got 25bps, then GBP rates markets had to simply adjust to this. On the other hand, it would seem that the hawkish tone of today's decision limited further gains. For example, only about 6/7bps were added to implied cumulative cuts by December 2024.
- Markets are now pricing in an additional 38bps in cuts by year-end, which combined with today's action totals 63bps. This is roughly split across one full 25bps cut by the November MPR/presser decision and toss-up odds that the BoE cuts again at its final gathering of 2024. A notable reaction to today's decision was that markets went from about 10bps of easing implied between today's and September's meeting to now only showing about 5/6bps. Put another way, September cut odds went from 40% pre-August cut to 20–25% with the one 25bps cut in the bag.
- Gilts are the clear outperformer in global rates markets today. The yield on UK 2yr debt has fallen 9–10bps on the day, with about half that done in 10s and a third of that in 30s. This is a classic bull steepening response to a rate cut. It is important to highlight, however, that UK 2s were already solidly bid 4/5bps before the BoE's decision and in fact struggled to make up more ground on the statement and Bailey's presser. It was the miss in US unit labour costs and jobless claims data that gave them another push.
- The rally in US rates on the data triggered broad FX gains vs the USD to bring the GBP back from its depths as it sat little changed post-BoE around 1.277. At writing, the GBP is chopping around the 1.28 level to track a 0.5% loss that makes it the worst-performing major on the day, though this damage was done prior to the bank's decision (in anticipation, of course). Against the EUR, the GBP is only down about 0.1% from its pre-decision levels.
- All in all, in isolation of broad market moves, UK rates and currency markets are relatively unscathed to at most incorporating today's underpriced rate cut.