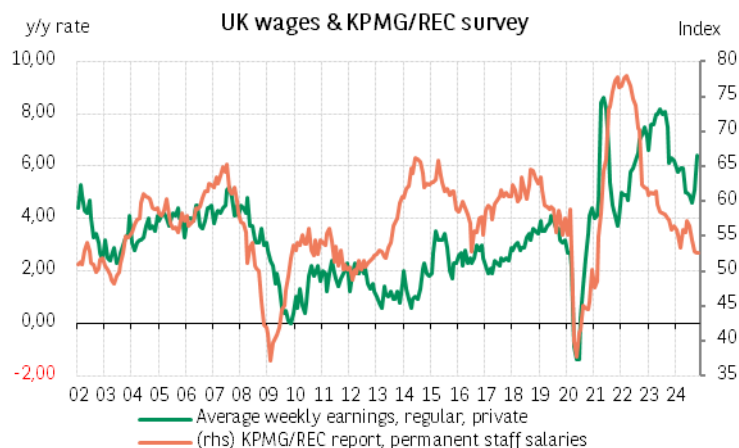


EcoBrief

Bank of England: no change, but more fears about economic activity

While the Bank of England's (BoE) decision to keep its key rates unchanged at 4.75% on December 19th was in line with market expectations, the vote by three MPC members in favour of a 25 basis point cut was less so. This week, which has had a wealth of economic indicators in the UK, will certainly have shifted the lines, between rising inflation in November and heightened fears that an overly restrictive monetary policy could derail the economic recovery. Indeed, the BoE has revised its growth forecast for Q4 downwards, from 0.3% to 0.0%.



Sources: ONS, KPMG/REC

Bond yields have risen sharply this week in response to inflation figures and especially wage figures, which rose by more than 6% year-on-year this autumn. The markets are now anticipating two rate cuts in 2025, a similar scenario to the US Federal Reserve, according to the latest FOMC projections (dot plots).

We do not believe that the markets are anticipating enough rate cuts in 2025. Although the UK economy is facing significant wage pressures, economic activity is significantly less dynamic than in the US (and will remain so in 2025), mainly because of the multiple brakes on consumption (which we describe in detail in our latest EcoPerspectives¹), which will only be fuelled by persistently high interest rates. Furthermore, some leading indicators point to wage disinflation in the future (*see chart*), which is more in line with the signs of a more significant deterioration in the labour market.

Between an ECB whose rate cuts will, admittedly, be gradual but steady, and a US Federal Reserve that is now more hawkish, the BoE will be in an intermediate position in 2025, with four rate cuts expected in 2025 according to our forecasts, at a rate of one cut per quarter. With our estimate of a neutral rate of around 2.75%, the BoE still has room for manoeuvre to lower rates while also maintaining the restrictive monetary policy needed in order to bring inflation back towards the 2% target on a lasting basis.

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¹ [United Kingdom | Recovery expected, but the road to monetary normalisation will be long](#)

