Arlingclose Economic and Interest Rate Forecast – June 2024

The Bank of England appears to be on the verge of loosening monetary policy, after a group on the Monetary Policy Committee (MPC) saw the last no change decision as finely balanced. However, the news about wage growth, core and services inflation has been on the stronger side, so a plethora of rates cuts in 2024 remains unlikely, as Bank Rate remains restrictive to bear down on inflationary pressure.

In June, the MPC continued its dovish tilt. Two members voted for a rate cut, but it appeared that some of the remaining seven were close to joining them.

UK GDP growth stagnated in a rain-affected April, but other data suggests that, while not strong, growth rebounded in May. However, activity appears to be ebbing somewhat after the more robust activity growth in quarter 1.

While wage growth remained strong, buoyed by significant increases in minimum wage, labour market data for April suggested that the market was loosening, with employment and vacancies down, and unemployment up. Anecdotal evidence has suggested lower pay growth for some time, and we expect the weaker labour market situation to hasten that outcome.

On the other hand, consumer sentiment has improved and is feeding into spending – May's retail sales data indicated robust underlying demand despite the weather-related volatility. Stronger demand in quarter 1 therefore raises some upside risks to our view.

Inflation rates will move lower over the next 12 months. The near-term path is less certain due to recent developments in commodity and energy markets, but we expect higher interest rates to dampen activity and this in turn to dampen inflation through the supply chain. There are upside risks from geo-political issues and stronger domestic activity. With continued policymaker fear around the persistence of underlying inflationary pressure, particularly services inflation, we believe Bank Rate will initially reduce slowly.

We expect that the continuation of restrictive monetary policy will bear down on activity and will require substantial loosening in 2025 to boost activity and inflation.

Global bond yields will remain volatile and investors' positioning for the timing of US monetary loosening will continue to influence movements in gilt yields. Moreover, there is a heightened risk of fiscal policy, credit events and/or geo-political events causing substantial volatility in yields.

The graph below shows the Arlingclose central case along with market implied and downside risks for Official Bank of England Base Rate.