BoE faces 'tough balancing act' as UK growth forecasts upgraded

Kept rates on hold

@LAURADEWIW LAURA DEW 02 FEBRUARY 2017

The Bank of England's Monetary Policy Committee (MPC) has voted unanimously to hold interest rates at 0.25% today, while UK growth expectations for 2017 have been upgraded to 2% from 1.4% on the government's fiscal stimulus plans and "firmer global momentum".

Sterling fell 0.6% to $1.2590 following the announcement as the Bank seemed in no rush to raise interest rates, despite raising its forecasts for UK economic growth for the next few years in response to developments at home and abroad.

Growth expectations were increased to 2% in 2017, from 1.5% to 1.6% for 2018 and from 1.6% to 1.7% in 2019.

The minutes of the meeting on 1-2 February said: "The upgraded outlook over the forecast period reflects the fiscal stimulus announced in the Chancellor's Autumn Statement, firmer momentum in global activity, higher global equity prices and more supportive credit conditions, particularly for households."

At the meeting, members voted unanimously for rates to be held at 0.25% and quantitative easing to remain at £435bn.

Meanwhile, the Bank's projections for inflation remain largely unchanged, with the CPI measure expected to overshoot the 2% target for a prolonged period and peak at 2.8% in the first half of 2018.

In the Bank's *Inflation Report,* the appreciation of sterling since the last forecast was noted as reducing upward pressure on inflation but other factors, such as the rising oil price and wage growth, have mitigated this.

Inflation hits 29-month high of 1.6% in December

The Committee also reiterated it would act against very high inflation: "There are limits to the extent that above-target inflation can be tolerated. The continuing suitability of the current policy stance depends on the trade-off between above-target inflation and slack in the economy."

The MPC's minutes added: "For some members, the risks around the trade-off embodied in the central projection meant they had moved a little closer to those limits."

However, members believe the risks are still finely balanced with the *Inflation Report* saying: "A sharper pickup in wage growth could raise domestic inflationary pressure in the medium term, but if wage growth remains subdued, inflation could fall below the 2% target once the upward impetus from import prices washes out. Overall, however, the risks around the projection are judged to be balanced."

Rates were cut last August from 0.5% to 0.25% in the wake of the EU referendum result with governor Mark Carney (*pictured*) hinting at the time that they could fall further.

BOE's Carney: Brexit no longer UK's biggest financial risk

Ben Brettell, senior economist at Hargreaves Lansdown, said the Bank now faces a tough job in the coming months as it seeks to balance a surprisingly resilient economy, higher inflation and the difficult-to-quantify risks posed by Brexit.

"Unsurprisingly interest rates were left on hold, but the minutes noted that some MPC members were getting a little closer to the limits of their tolerance for higher inflation. This could mean we see the first interest rate rise in more than a decade at some point this year, particularly if wage growth turns out stronger than expected.

"However, I still feel this is improbable. The most likely scenario is that higher inflation and weaker pay growth will squeeze household budgets, meaning consumer spending is likely to slow in real terms.

"The Bank is unlikely to take the risk of raising borrowing costs in this environment. If it does happen, I would expect rates to remain at their previous low of 0.5% for some significant time afterwards."

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