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BOE Raises Rates by a Half-Point as Push Begins for Bigger Moves

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(Bloomberg) -- The Bank of England delivered a second consecutive half-point interest-rate hike in its battle to bring down inflation, as three officials pushed for the institution to join its global peers in moving at an even quicker pace.

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The move to 2.25% was backed by five of the nine-member Monetary Policy Committee, including Governor Andrew Bailey, while one voted for a smaller move. It was the seventh increase in a row, with officials voting to tighten policy at every meeting since December.

The MPC lowered its forecast for peak inflation from more than 13% to less than 11% and suggested a deep recession may be averted as a result of new Prime Minister Liz Truss's energy relief plan. Details of that plan, as well as tax cuts and other measures, are due to be unveiled Friday, and the MPC noted that the aid will support demand, with implications for inflation.

The committee said it would "respond forcefully as necessary" if price pressures look more persistent, reinforcing the view that tightening is far from done. That, coupled with the push for a three-quarter point move from some officials, may set the stage for a bigger hike later this year.

The yield on 10-year gilts jumped more than 10 basis points to the highest since 2011 after the announcement, while traders largely stuck to bets rates will get close to 5% next year.

The pound, which initially eased as the BOE held off from following the Federal Reserve with a bigger move, later recovered some lost ground as was up 0.4% to \$1.1311 as of 12:58 p.m. London time.

The 50-basis-point increase in rates was predicted by most economists, although markets saw around a 60% chance of more.

The BOE had been under mounting pressure to keep up with the blistering pace set by other central banks around the world to protect sterling, which has slumped to its lowest level since 1985 as rapidly rising US rates draw capital.

While the BOE cut its October peak inflation number, it still expects the measure to stay above 10% for a few months after that high point. The government's energy price freeze will also "limit the reduction" in household spending forecast in August, it said, a hint that the deep recession predicted last month may be less severe than expected.

The BOE will update its forecasts in more detail in November, when it will full assess the government's fiscal plans. It said Thursday that the However, the prospect of stronger consumer demand is "likely to add to inflationary pressures in the medium term," the committee said.

Officials also projected a technical recession in the second and third quarters of 2022, as the economy takes a hit from the extra bank holiday for the funeral of Queen Elizabeth II.

Vote Split

Against a backdrop of more persistent price pressures and signs of a tight labor market, Dave Ramsden, Catherine Mann and Jonathan Haskel pushed for a 75 basis-point hike, arguing that incoming fiscal support will also add to demand.

Swati Dhingra, voting at her first meeting, was the lone voice calling for a quarter-point rise, citing concerns that activity was weakening and the risk of second-round inflation effects falling.

Collectively, about 90 central bank have raised interest rates this year, and half of them have hiked by at least 75 basis points in one shot, including the Swiss National Bank earlier Thursday. On Wednesday, the Federal Reserve announced a third consecutive 75 basis-point increase, while Sweden's Riksbank moved by a full point.

The BOE's task of calibrating policy has been made harder by huge fiscal expansion announced by new Prime Minister Truss.

On Friday, Chancellor Kwasi Kwarteng is expected to outline tax cuts and subsidies for households and firms facing soaring energy bills in a package worth more than £200 billion over the next two years. The BOE said that would knock around 2.5 percentage points off inflation in the fourth quarter, and more than 5 points in the early months of 2023.

BOE policy makers also unanimously endorsed plans to start reducing the mammoth government bond holdings built up since the financial crisis over a decade ago. Active sales, the first carried out by a major central bank, will start on Oct. 3, and be in the region of £10 billion a quarter. Adding the impact of expiring gilts, it expects its total stock, which still amount to almost £850 billion, to decline to around £758 billion in the first year.

The Monetary Policy Committee reiterated that there is a high bar for amending the plan and said it did not intend to vote on the reduction at every meeting.

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