

GBP Macro Report

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UK Macro views

1. Repeating the past pattern of BoE forecast errors points to an upside inflation risk, owing to underestimating the UK's supply-side weakness.
2. Fiscal sustainability concerns amplify bond market volatility, particularly at the long-end and during data-driven periods. Disappointing economic data, coming from weak supply-side performance, and fiscal fatigue simultaneously raise questions about fiscal capacity and inflation persistence. In these episodes, yield curve steepening and risk premium episodes should be expected. These tilt the BoE hawkish.
3. The authorities can mitigate yield curve steepening through active debt management, now a bigger feature of the UK policy mix, reducing the average maturity of new issuance. A second policy option to contain steepening is that HMT prioritises restraint in public spending and tax rises that face lower implementation risk (eg re-profiling fixed investment plans). Back-loading fiscal adjustment has the opposite effect.

GBP Market developments I

GBP OIS and GBPUSD

cumulative change

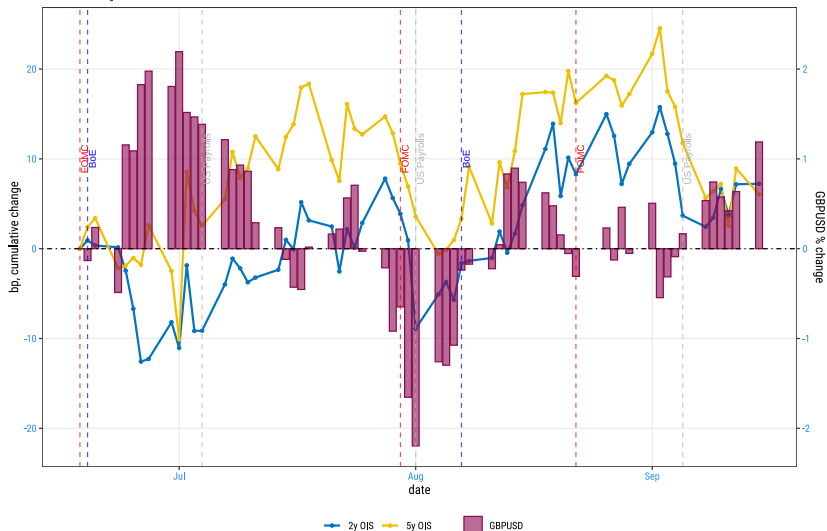


Figure 1: OIS and Sterling

GBP Market developments II

Gilt yields and UK Equity prices

cumulative change

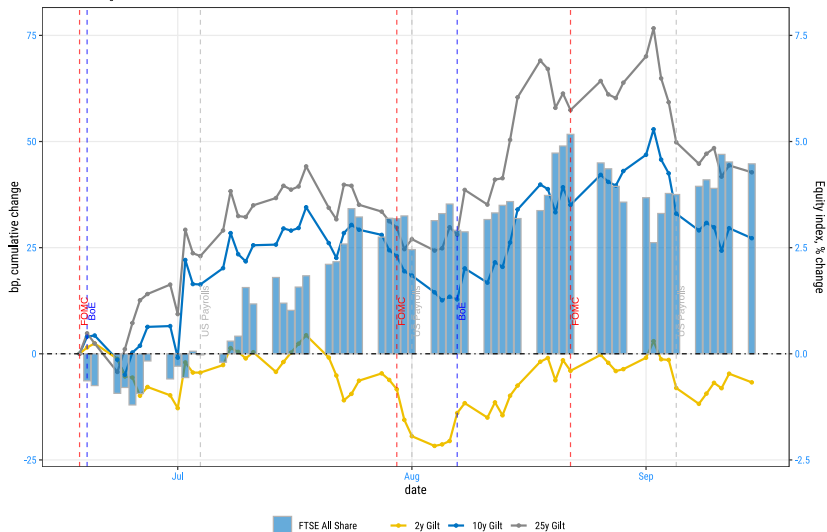


Figure 2: Gilts and Equities

Evolving macro forecasts

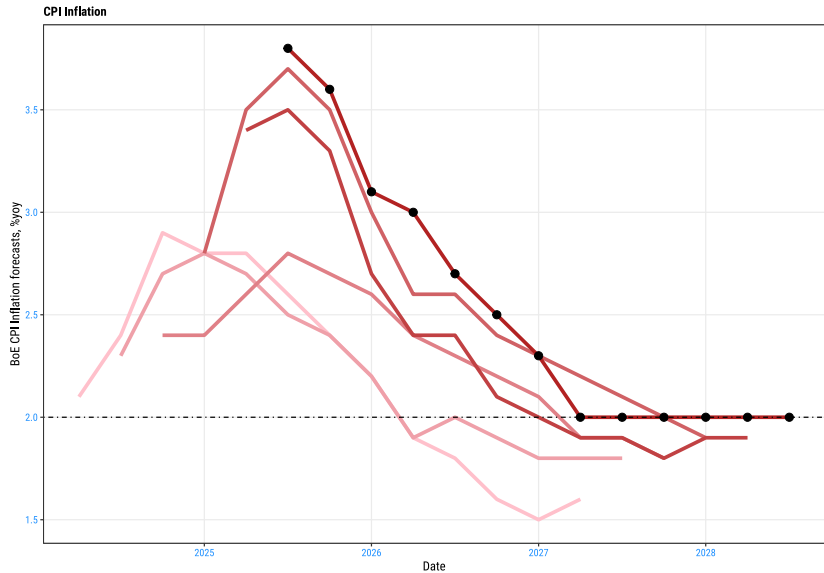
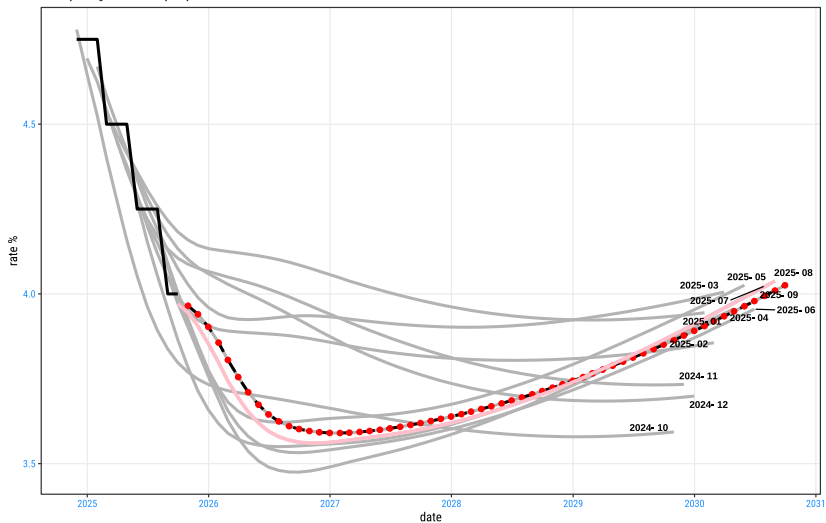


Figure 3: Successive BoE Inflation Forecasts

Successive OIS curves tilting hawkish

GBP OIS Curves: The past 12 months

monthly averages of end-of-day daily data



Source: Bank of England data

Figure 4: Successive OIS Curves

A test of fiscal fatigue?

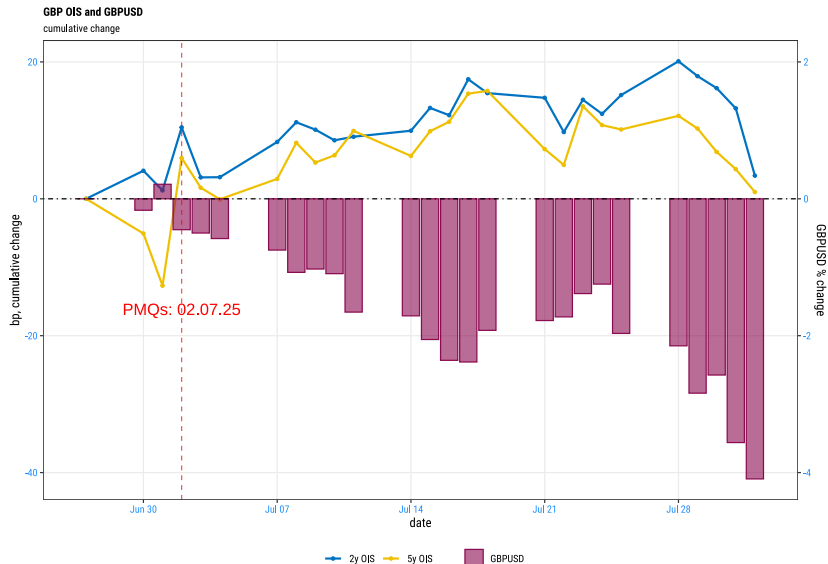


Figure 5: Fiscal fatigue and risk premium in OIS and Sterling

International spillovers in bond markets

Estimated Structural Shocks in International Bond Markets

Structural shocks from 4-country VAR with change-in-volatility identification

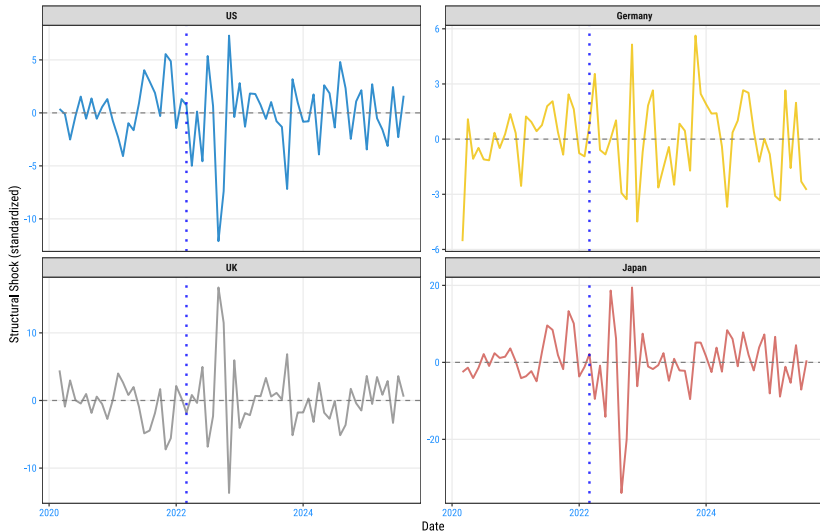


Figure 6: International spillovers

MPC Voting: increased disagreement

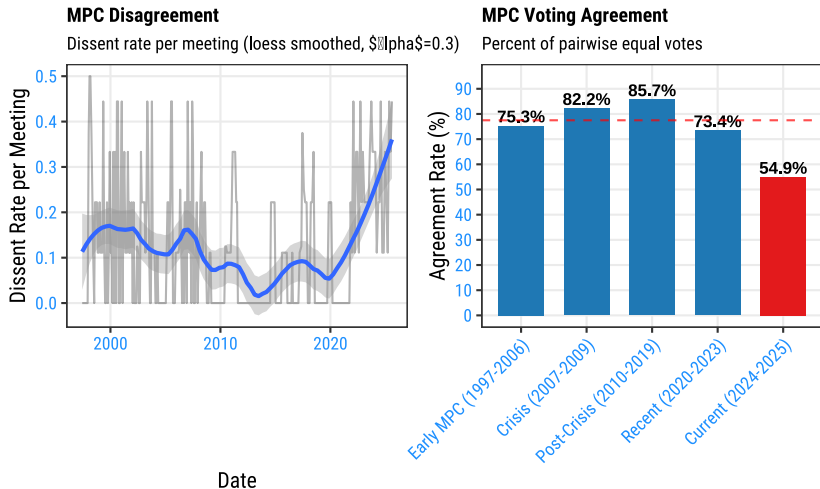


Figure 7: A weaker Consensus in MPC rate decisions

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