ECONOMIC RESEARCH

The NewsLine

August 4, 2016

} MACROECONOMICS | FINANCIAL MARKETS | ECONOMIC POLICY | SECTORS

UK

BoE delivers comprehensive bundle of measures

Katharina Utermöhl
Phone +49.69.24431-3790
katharina.utermoehl@allianz.com
Allianz SE
https://www.allianz.com/economic-research/en

Allianz Research
https://twitter.com/AllianzResearch

The Bank of England (BoE) has launched a sweeping bundle of monetary policy measures to cushion the negative impact of the Brexit decision on the UK economy.

As expected, the BoE lowered its base rate from 0.5% to a new all-time low of 0.25%. In addition, it expanded its asset purchase program by GBP 70bn and announced that it would now also be buying corporate bonds. To cushion the negative effects of low interest rates on the banks, the Funding for Lending Scheme has been reactivated. All told, the measures will swell the BoE's balance sheet by up to GBP 170bn.

The markets welcomed the scale and breadth of the package. The interest rate cut, the first in more than seven years, had been fully priced in by the markets, not least because the prospect had already been raised at the last monetary policy meeting three weeks ago. By contrast, the expansion of the QE program exceeded market expectations. The BoE announced that it would not only be buying government bonds to the tune of GBP 60bn but also GBP 10bn worth of UK corporate bonds.

The scale of the package shows that the BoE expects Brexit to have a very negative impact on the UK economy. The bank slashed its growth forecasts and now expects GDP growth in 2017 of only 0.8% (previously 2.3%). By contrast, given the expected rise in import prices, the inflation forecast for 2017 was lifted from 1.5% to 1.9%. Although hard data are not yet available, a host of leading indicators on business and consumer sentiment have been pointing of late to a marked slowdown in the economy. Particularly worrying is the slide in sentiment in the services sector, which accounts for almost 80% of economic output. The purchasing managers' index for the services sector tumbled to 47.4 points in July, the lowest reading since the crisis year 2009.

The BoE is not biding its time with a cautious policy dosage to stabilize the UK economy, but has opted to confront a possible hard landing head on. Moreover, BoE Governor Mark Carney stressed that the bank was ready to take further measures should the economy develop even worse than currently expected. While these statements doubtless help to curb the mounting uncertainty in economic expectations, their impact on the real economy will be limited. It would also be advisable for the BoE to remain on hold in the coming months to allow today's measures to feed through and be better placed to gauge the consequences for the UK economy. The UK's departure from the EU is likely to be a drawn-out process marked by elevated economic uncertainty. The BoE would do well not to exhaust its arsenal right at the beginning of the journey but to keep some powder dry.

These assessments are, as always, subject to the disclaimer provided below.

ABOUT ALLIANZ

Together with its customers and sales partners, Allianz is one of the strongest financial communities. About 85 million private and corporate customers insured by Allianz rely on its knowledge, global reach, capital strength and solidity to help them make the most of financial opportunities and to avoid and safeguard themselves against risks. In 2015, around 142,000 employees in over 70 countries achieved total revenues of 125.2 billion euros and an operating profit of 10.7 billion euros. Benefits for our customers reached 107.4 billion euros.
This business success with insurance, asset management and assistance services is based increasingly on customer demand for crisis-proof financial solutions for an aging society and the challenges of climate change. Transparency and integrity are key components of sustainable corporate governance at Allianz SE.

CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

The statements contained herein may include prospects, statements of future expectations and other forward-looking statements that are based on management's current views and assumptions and involve known and unknown risks and uncertainties. Actual results, performance or events may differ materially from those expressed or implied in such forward-looking statements.
Such deviations may arise due to, without limitation, (i) changes of the general economic conditions and competitive situation, particularly in the Allianz Group's core business and core markets, (ii) performance of financial markets (particularly market volatility, liquidity and credit events), (iii) frequency and severity of insured loss events, including from natural catastrophes, and the development of loss expenses, (iv) mortality and morbidity levels and trends, (v) persistency levels, (vi) particularly in the banking business, the extent of credit defaults, (vii) interest rate levels, (viii) currency exchange rates including the euro/US-dollar exchange rate, (ix) changes in laws and regulations, including tax regulations, (x) the impact of acquisitions, including related integration issues, and reorganization measures, and (xi) general competitive factors, in each case on a local, regional, national and/or global basis. Many of these factors may be more likely to occur, or more pronounced, as a result of terrorist activities and their consequences.

NO DUTY TO UPDATE

The company assumes no obligation to update any information or forward-looking statement contained herein, save for any information required to be disclosed by law.