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## **MONETARY AFFAIRS:**

**Preview: BoE To Keep Rates Unchanged in June,  
With a “Hawkish Hold” and Dissenters**

**by**

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**12 June 2026**

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### Preview: BoE To Keep Rates Unchanged in June, With a “Hawkish Hold” and Dissenters

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#### Executive Summary

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- ✦ **Expected Decision:** *In line with consensus, we expect the Bank of England (BoE) to hold Bank Rate at 3.75% in June.* Governor Bailey supported keeping rates at 3.75% in April and has indicated that higher market rates allow policymakers more time to evaluate whether the Iran war will require further monetary tightening. Regarding its *balance sheet policy*, in September 2025, the BoE cut gilt holdings by £70bn over the next year (down from £100bn), reducing the stock to £488bn. The plan includes £21bn of active sales, up from £13bn, with fewer maturities expected; only 20% will be long-dated gilts, versus a third previously. Regarding *forward guidance*, we expect the BoE to reiterate that decisions are taken meeting by meeting. We expect an 8-1 split as we assume Huw Pill will reiterate his vote for a hike also in June, but could be 7-2 if Meghan Greene joins him. Thinner majorities for a hold may materialise if other hawkish dissenters emerge (such as Katherine L. Mann).
- ✦ **Policy Discussion:** *The BoE faces a difficult trade-off between containing energy-driven inflation risks and supporting a fragile economy.* Governor Andrew Bailey reaffirmed the Bank's commitment to its 2% inflation target, despite expecting inflation to rise from 2.8% in April towards 4% by the end of 2026. Markets nonetheless assign a roughly 90% probability to rates remaining unchanged in June, although one or two rate hikes are still priced in by year-end.

The case for an immediate rate increase has weakened as energy market pressures have eased. Spot oil prices have fallen, natural gas prices remain relatively contained, and inflation expectations have stayed anchored. Headline inflation is now expected to peak at around 3.7%, while wage growth, hiring intentions, and labour market conditions have all softened, reducing concerns about persistent second-round inflation effects.

However, policymakers remain cautious. A prolonged disruption to energy flows through the Strait of Hormuz could reignite inflationary pressures, prompting further tightening later in the year. This has fuelled a growing debate within the Monetary Policy Committee, with Megan Greene warning that a rate hike may still become necessary, while the Organisation for Economic Co-operation and Development expects rates to remain on hold before eventual cuts in 2027. Meanwhile, ongoing quantitative tightening continues to withdraw liquidity from the financial system, adding to monetary restraint even without additional rate increases.

#### Key Assumptions and Judgements In Scenarios from April MPR

	Scenario A	Scenario B	Scenario C
Energy prices	Energy prices for oil and gas follow the market futures curves over the scenario period.	Energy prices follow the market futures curves for six months and then follow the average of the futures curves and a constant spot price at six months for the remainder of the scenario period.	Energy prices rise sharply-to a level in the upper tail of option-implied distributions- and remain elevated for a prolonged period.
Second-round effects from new energy shock	No second-round effects from the new energy shock due to weaker worker bargaining and firm pricing power stemming from weaker demand, driven by less consumption smoothing than in other scenarios.	Modest additional second-round effects, consistent with some wage effects from the scale of the energy shock.	Stronger and more persistent additional second-round effects, relative to the other scenarios stemming from greater effect of the energy shock to inflation expectations and wages and prices.

Source: Bank of England

## Analysis

✦ **EXPECTED DECISION:** *On June 18, in line with consensus, we expect the Bank of England (BoE) to hold its Bank Rate at 3.75%.* The BoE is firmly in wait-and-see mode, as stagflation risks—slow growth, rising unemployment, and persistent inflation—complicate policy choices. Governor Bailey voted with the majority to keep interest rates unchanged at 3.75% in April. More recently, he indicated that higher market interest rates have given policymakers additional time to assess whether the inflationary impact of the Iran

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war will require further monetary tightening. We expect an 8-1 split as we assume Huw Pill will reiterate his vote for a hike also in June, but could be 7-2 if Meghan Greene joins him. Thinner majorities for a hold may materialise if other hawkish dissenters emerge (such as Katherine L. Mann).

In terms of *forward guidance*, the Bank will remain evidence-based, and data dependent, with decisions made meeting-by-meeting. The MPC will continue to monitor closely the risks of inflation persistence and will decide the appropriate degree of monetary policy restrictiveness at each meeting.

In terms of *balance sheet policy*, the BoE agreed to cut its government bond holdings by £70 billion (from £100 billion) over the next year, bringing the total to £488 billion. The plan includes £21bn of active bond sales, up from £13bn last year, with fewer maturities expected. Only 20% of sales will be long-dated gilts, down from a third previously.

✦ **POLICY DISCUSSION:** *The BoE faces a difficult trade-off between containing energy-driven inflation risks and supporting a fragile economy, leaving policymakers debating not only when rates might be cut but also whether further tightening may still be necessary.* In his annual testimony before the House of Lords Economic Affairs Committee, Bank of England Governor Andrew Bailey reaffirmed the Bank's commitment to its 2% inflation target, rejecting suggestions that it should be raised to 3%. Although UK inflation fell to 2.8% in April, the BoE still expects it to rise towards 4% by the end of 2026 under its baseline scenario. Nevertheless, investors assign roughly a 90% probability to rates remaining unchanged in June, while pricing in one or potentially two rate hikes by year-end.

The case for an immediate rate increase has weakened compared with April. At the height of concerns over the Iran conflict, policymakers appeared increasingly worried about the inflationary consequences of higher energy prices. Since then, however, spot oil prices have fallen significantly, natural gas prices have remained relatively contained, and current energy market conditions lie between the Bank's April stress scenarios, neither of which policymakers viewed as automatically warranting tighter policy. Falling natural gas futures also suggest that July's 12% increase in household energy bills could be followed by an 8% decline in October, limiting the extent of the inflation shock.

Domestic inflation indicators have likewise become more reassuring. One-year-ahead inflation expectations have eased, while longer-term expectations remain broadly stable, suggesting firms do not expect the latest energy shock to trigger persistent inflation. Headline inflation is now expected to peak at around 3.7% in September before stabilising near 3.5%, remaining below the Bank's informal 4% threshold. Moreover, evidence of second-round effects remains limited. Wage growth has slowed markedly from the elevated levels seen in 2023, corporate surveys show little change in wage expectations, and recent inflation data has been relatively benign despite modest increases in firms' output price expectations.

The labour market is also showing signs of cooling. Firms continue to reduce headcount, hiring difficulties have fallen sharply from their 2022 peaks, and expected wage growth has declined to a post-2022 low of 3.4%. Together with weak employment data and a fragile economic backdrop, these developments strengthen the case for the BoE to maintain rates at current levels for the time being.

However, policymakers remain cautious about declaring victory over inflation. A prolonged disruption of energy flows through the Strait of Hormuz could push oil and, more importantly for the UK, natural gas prices substantially higher. Such a scenario could reignite inflationary pressures and increase the risk of second-round effects through wages, pricing behaviour, and inflation expectations. Consequently, while a

June rate hike appears unlikely, a move later in the summer cannot be ruled out if energy markets deteriorate further.

This uncertainty has produced an increasingly visible debate within the Monetary Policy Committee. MPC member Megan Greene has argued that the case for a rate hike is strengthening, warning that waiting until inflation pressures are fully reflected in official data could leave the Bank behind the curve. In contrast, the OECD expects the BoE to keep rates unchanged through the remainder of the year before delivering a modest rate cut in 2027, arguing that existing monetary restraint is already slowing demand sufficiently. Page | 4

Complicating the policy outlook further is the Bank's ongoing quantitative tightening programme. Bailey noted that banking reserves have fallen to approximately £640 billion from a peak of around £980 billion, indicating that liquidity is already being withdrawn from the financial system. As a result, financial conditions continue to tighten even without additional rate increases.

- ✦ **MACROECONOMIC ANALYSIS:** *Higher energy costs and supply disruptions linked to the closure of the Strait of Hormuz are expected to weigh on growth and inflation, reinforcing expectations of further Bank of England tightening later this year.* UK GDP grew by 0.6% q-o-q in Q1 2026, matching expectations and accelerating from 0.2% in the previous quarter, driven primarily by broad-based strength in the services sector. While the data suggest the economy entered Q2 on a relatively strong footing, economists caution that it largely reflects pre-war conditions, with business confidence, hiring, and investment sentiment weakening since the outbreak of the US-Iran conflict.

Inflation fell from 3.3% in March to 2.8% in April, helped by lower household energy bills following an Ofgem price-cap reduction and slower increases in regulated service prices. However, inflation is expected to rise again as higher energy costs feed through to consumers, with the July increase in the Ofgem price cap and rising food prices likely to push inflation higher. Unlike the 2022 energy shock, weaker consumer demand and a softening labour market should limit second-round effects on wages and prices, reducing the risk of a prolonged inflation surge.

The unemployment rate rose unexpectedly to 5.0% in the three months to March from 4.9%, while job vacancies fell to a five-year low of 705K, signalling a weakening labour market. Payroll employment declined by 100,000 in April, with lower-paid sectors such as hospitality and retail experiencing some of the sharpest reductions in hiring and employment. The data suggest the first effects of the Iran war and rising business costs are beginning to weigh on recruitment, prompting firms to scale back hiring plans. Wage growth slowed to 3.4%, remaining only marginally above inflation, which is likely to keep consumer spending subdued even as labour market conditions soften. While weaker employment and wage growth would normally support monetary easing, persistent inflation risks may keep interest rates higher for longer.

- ✦ **MARKET IMPLICATIONS:** *Longer Gilt rates always in focus.* UK 10Y gilt yields remains to their highest level since May 21, as inflation concerns deepened amid escalating Middle East tensions. *in the fixed-income space*, as of June 10 and since the last meeting on April 30: *i) the 2y Gilt yield* edged down by 9 bps to 4.37% (+64 bps y-t-d); *and ii) the 10y Gilt yield* was down by 7 bps to around 4.95% (+41 bps y-t-d). *In the currency space*, the GBP/USD exchange rate edged higher towards 1.3385, but gains remain constrained by strengthening expectations that US interest rates will stay elevated for longer. although sterling has found some support, expectations of higher-for-longer US rates continue to favour the dollar, potentially limiting further upside in GBP/USD unless incoming UK data or BoE communications become more hawkish. As of June 10, *GBP/USD* decreased by 1.7% from the last meeting in April to 1.34 (-0.7% y-t-d). *GBP/EUR* fell by 0.1% since the April meeting to around 1.16 (+0.9% y-t-d). *In the equity space*, on Thursday, FTSE 100 rose 0.6%, supported by gains in financial stocks, including HSBC, Standard Chartered and Prudential, as Hong Kong-exposed firms rebounded after recent losses linked to China's tighter cross-border investment rules. However, broader gains were capped by ongoing Middle East tensions and growing investor concerns over rising AI-related corporate spending. Since the last meeting in April, as of June 10, the FTSE 100 decreased by 1.9% to 10,254,81 (+3.1% y-t-d).

✦ **APPENDIX (MACRO ASSESSMENT): UK economic growth was underpinned by higher investment, household consumption, and government spending.** In Q1, the economy advanced by 0.6% q-o-q (c: 0.6%; p: 0.2%) marking the strongest growth since Q1 2025. Household expenditure and government consumption rose by 0.6% (p: 0.1% in Q4) and by 0.4% (p: 0.1% in Q4) respectively. Gross fixed capital formation shrank by 0.6% (p: -0.1% in Q4). Business investment increased by 0.7% q-o-q (p: -2.9%). There was a decrease in net trade, with imports increasing by 0.6% (p: 0.6%) and rises by less by 0.1% (p: -0.3%). The British economy expanded 1.1% y-o-y (c: 0.8%; p: 1.0%) in Q1. The British economy expanded by 0.3% m-o-m in March (c: -0.2%; p: 0.4%).

*Leading business indicators signalled the first contraction in business activity in over a year.* Retail sales volumes were unchanged (c: 1.3%; p: 1.4%) in April. When looking at business confidence, in April, the S&P Global/CIPS Flash UK Composite PMI fell to 49.7 (c: 48.5; p: 52.6). Services PMI declined to 49.3 (p: 52.7). Manufacturing PMI was up to 53.9 (p: 53.7).

*The data pointed to a softening labour market as higher costs and uncertainty weighed on hiring.* In March, unemployment rate edged up to 5.0% (c: 4.9%; p: 4.9%). Total average weekly earnings, including bonuses, increased by 4.1% y-o-y (c: 3.8%; p: 3.9%) in the three months leading up to March. Average wages rose in real terms, with an annual change of 3.4% excluding bonuses. The number of job vacancies declined to 705K in March (p: 712K).

*Headline inflation reading marked marking the lowest since March last year.* In April, CPI inflation slowed to 2.8% y-o-y (c: 3.0%; p: 3.3%). Core inflation edged eased to 2.5% y-o-y (c: 2.6%; p: 3.1%). The slowdown was driven by lower housing and household services inflation following the introduction of an energy price cap, alongside softer increases in transport, food, health, and recreation costs. Monthly consumer prices rose 0.7%, matching the pace recorded in March.



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