



Weekly Bulletin – 16th April 2007

UK, US and eurozone interest rates all drifted upwards again last week on market concerns that, in the UK and eurozone, short term rates may not necessarily peak after just one more rate hike. The US had been trading on the basis that short term rates would start to fall before the year end, a prospect that now looks increasingly in doubt. There had been some hope that EUR interest rates might stage a small rally if President Trichet failed to use the magic words ‘extreme vigilance’ at the press conference following their meeting last week. He did not do so, thus making any chance of another rate hike before June unlikely. However, with economic data and survey releases within the eurozone remaining strong, all the market is really expecting is a delay in the inevitable.

The UK sees a range of economic data being released this week which is likely to determine whether a rate hike next month is a certainty and is likely to influence its current fears of the 5.50% level not being sufficiently high to satisfy the MPC that it will curb inflationary pressures from rising above 2.00% on a longer term view.

First up, today, will be the latest set of producer price input and output indices. As noted a couple of weeks ago, with the growing concern that manufacturers and retailers are being able to make price increases stick, this data is likely to grow in importance. The output prices are expected to remain at 0.3% on the month and 2.2% year on year. If they come out at higher levels, the market might console itself that that the BCC survey last week offered some evidence that manufacturers’ price expectations are on the wane, albeit from very high levels.

Tomorrow sees the actual inflation figures for March being released. The CPI measure is expected to rise 0.2% which should keep the year-on-year measure at a static 2.8%. There should be some influence in this month’s figures of lower electricity pricing, but this may be offset by the higher petrol prices that were seen during the month. Most economists are also expecting a further rise in both household goods and services inflation. However, inflation, across almost all sectors, should start to fall next month and decline back to the MPC’s 2.00% target level in time for the summer holidays.

Wednesday sees the production of the latest labour market figures. Average earnings are expected to remain steady at 4.2%, or perhaps move a pip higher, hardly a level to have caused Mervyn King so much anguish in the latter half of last year. Having been used, successfully but with no eventual justification, as an excuse for at least one pre-emptive rate increase, the MPC will now, no doubt, drop its significance to that of an also-ran. This, at least, will confirm their reputation for being utterly inconsistent.

Thursday sees the release of the latest retail sales figures. These are expected to be fairly buoyant based on CBI and BRC’s surveys, although hardly likely to match up to February’s quite extraordinary result. The median forecast is for a rise of about 0.5% which would leave the year-on-year figure at a lower, but still very healthy, 4.7%. However, there is recent evidence, in the furniture industry in particular, that like for like sales have fallen off a cliff in the past month, not an element that will affect this set of figures but, if maintained, should have a pronounced effect in future months.

If the variety of domestic economic data is not enough to provide the market with plenty to analyse, it will also have to absorb the release of the minutes of the MPC’s meeting earlier this month. It is strongly suspected that this will show a three-way split with the arch dove, David Blanchflower, continuing to vote for a cut in rates and with the two latest recruits, Messrs Besley and Sentance, renewing their demand for a rate hike. They may have been joined by one or two others, but we suspect that the Bank of England’s cabal on the committee will have shown solidarity in voting for a ‘no change’ decision, thus reverting to the norm of leaving themselves in a position to coincide rate changing decisions with the publication of the Inflation Report. However, we do expect the language and concerns contained within the MPC minutes to produce a situation where a rate hike next month will come as a surprise to absolutely nobody.

This is likely to be a pretty edgy week in the UK market and it will probably take a pleasant surprise from one of the economic releases to head off a continued drift to yet higher levels.

JCD Rathbone