

# Economic snapshot

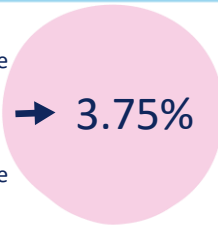
by David Fenton, TSB's Chief Economist



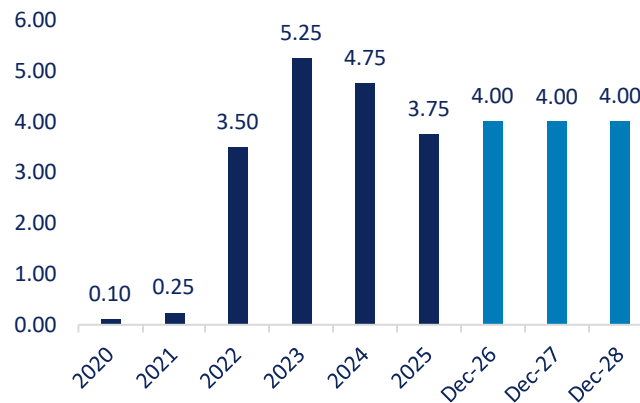
The BoE left the UK policy rate on hold at 3.75% in June, as expected. The central bank said it would keep a close eye on events in the Middle East, and their ongoing effect on the economy. Governor Bailey said that the Iran/US deal was “encouraging” but added there would need to be an assessment of how much damage has been done to the infrastructure for supplying energy. The BoE reiterated its forward guidance on rates, saying it “stands ready to act as necessary”. Market expectations for Bank Rate have moderated in recent weeks, though one hike is still fully priced in by end-2026.

## Interest rates

- Bank Rate was left unchanged at 3.75% in June. The 7-2 vote was in line with market expectations, though Catherine Mann intimated she was closer to a hike than the rest of the majority. Governor Bailey said that the risks to interest rates are on the upside. He added he would respond “promptly” to any signs of stronger second-round effects on inflation.
- Markets have one quarter-point rate hike fully priced in for 2026 (see chart), with rates then settling at 4.00% for an extended period.



## Market implied outlook for Bank Rate (year end)



## Housing market

- House prices fell for a third consecutive month in May, according to the Halifax index. However, the decline was negligible, and the year-on-year growth rate ticked up to 0.5%. Moneyfacts said there had been some “significant cuts” to mortgage rates and expressed hope that the deal between the US and Iran would make borrowers “feel more positive” about the mortgage market.
- The mortgage market in 2026 is closely tracking 2025, with gross lending of £93 bn over the year-to-April (£92 bn last year). Mortgage approvals remain resilient (65.9k in April).



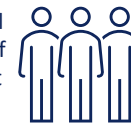
## Prices and inflation

- CPI inflation was unchanged at 2.8% in May, but lower than market expectations (3.0%) and the BoE's most recent forecast (3.2%). The main upward impetus to inflation came from transport, with the ONS highlighting a large increase in air fares – though this may have had more to do with the timing of Easter, and the school holidays, than underlying inflationary pressures. The main downward impetus came from food price inflation.
- The BoE said CPI inflation was now expected to be a little under 3% in Q3 2026, and a little over 3¼% in Q4. This was below the path expected in the BoE's April forecast.



## Jobs and earnings

- Just as the pass-through from higher energy prices to inflation has so far been less forceful than the BoE might have feared, the impact of geopolitical uncertainty on the labour market has been less severe. Payrolls are still on a downward trajectory, but the trend remains gradual, and the unemployment rate fell in April to 4.9%. Wage growth was broadly unchanged in April, and remains higher than inflation, so purchasing power is holding up relatively well.
- The BoE noted that its contacts expected one-year-ahead wage growth of 3.4%, which had been stable since before the start of the conflict.



## Economic activity

- The UK made a stronger start to 2026 than the BoE had expected. GDP increased by 0.6% in Q1. The BoE said that this apparent strength was at odds with business surveys, however, which had remained subdued. The BoE reckons that *underlying* GDP growth had been a round 0.2% in Q1 – and would remain at around that pace in Q2. Even so, the BoE noted that there was little evidence that the conflict had led to a “rapid deterioration” in the growth outlook.
- 0.2% is below estimates of the UK's trend growth rate. The BoE is monitoring the extent to which emerging economic slack is restraining inflation persistence.

