

Contributors

Juan Manuel Herrera

Director

+52.55.2299.6675 (Mexico)

juanmanuel.herrera@scotiabank.com

BoE Keeps Options Open, but Looks Set to Hold Steady

- **The Bank of England (BoE) matched expectations by keeping its policy rate steady at 3.75%, in a 7 hold vs 2 hike vote split, remaining on standby amid upside inflation risks against ongoing demand weakness.**
- **If recent conditions in energy markets remain in place, with prices well off their highs but still above pre-conflict levels, the BoE would likely stand pat for the remainder of the year, although it stands ready to act if prices jump again or if data show clear second-round effects of higher energy prices. Our latest pre-peace deal forecast of two BoE hikes this year is at risk of revision.**
- **With the BoE's communications generally meeting expectations in terms of the vote split, guidance, and the comments provided by policymakers, U.K. yields came off their intraday highs to practically close at the same levels as at the market open. Markets are pricing in about ~30bps in hikes by year-end, unchanged from yesterday's close.**

As widely expected, the Bank of England (BoE) kept its policy rate steady at 3.75%, remaining on standby in the face of upside inflation risks against ongoing demand weakness. Officials were split 7–2 in today's decision, with hawks Pill (chief economist) and Greene (external member) preferring a 25bps rate increase compared to the 8–1 decision in late-April when only Pill voted for a hike.

Developments in global energy markets remain the leading driver of expectations for near-term BoE policy settings. The sharp decline in energy prices in recent days due to the U.S.-Iran peace deal (pending full agreement after negotiations) has significantly reduced upside inflation risks. If energy prices were to hold around current levels (\$75–80/bbl for Brent oil)—or possibly head lower if a deal is finalized and energy flows resume quickly—the BoE would simply stand pat for the balance of the year. This is in contrast to our latest forecast of two 25bps rate hikes (in 3Q and Q4'26) that incorporated a higher energy price outlook, and is thus subject to revision.

Despite the relief in global energy prices and clearer signs of domestic economic weakness, the BoE is unlikely to return to an easing path this year as officials will still have to observe the impact of higher petrol costs and utility bills on an economy where inflation has been very stubborn in its convergence to target. In May data released yesterday, CPI excluding housing, utilities, and fuels (a 'supercore' measure) inflation came in at 3.2% y/y, sitting around or slightly above the 3% level practically every month since January 2025.

Regulated home energy bills also respond to with a lag to 'live' developments in global oil and gas prices due to the regulator's pricing mechanism. This means that Britons that saw a 7% q/q drop in their electricity and gas bill in the April–June quarter (mainly thanks to government subsidies) will face a 13% q/q increase in the July–September quarter that responds to high pre-peace deal energy prices. Possible second-round effects around inflation and wage expectations from this rise in household bills and higher petrol prices will have to be monitored by the BoE over a few months before they gain confidence around the direction for the policy rate.

The peace deal may have brought some prices relief in commodity markets but there's no certainty that this ceasefire will hold nor do we know how quickly energy flows could resume through the Strait of Hormuz. In any case, it should take several months to return to pre-conflict exports/production levels and a geopolitical premium will likely remain in place, keeping prices higher versus late-February conditions.

It would be far too early for the BoE to change its tune in response to recent developments, so it unsurprisingly "stands ready to act as necessary to ensure that CPI inflation remains on track to meet the 2% target in the medium term"—as it did in the late

June 18, 2026

-April rate announcement. Nonetheless, the BoE outlined the would-be impact on its inflation forecasts (which were just updated in the April Monetary Policy Report) from incorporating energy prices as of June 15th. According to the statement, “inflation was now expected to be a little under 3% in Q3-26 and pick up to a little over 3¼% in Q4,” thus about half a percentage point lower than the 3.6/3.7% for Q4-26 that the bank penciled in under its A and B scenarios in the April MPR.

The two voters in favour of a hike and Mann’s comments that either scenario—one with rapid resolution and a rebound in activity while energy prices remain high, or one with “sporadic continuance” of the conflict with higher energy prices—would warrant an “activist hike” suggests that she will join Greene and Pill’s hike votes at the September decision. The overall tone of officials was one of keeping their options open, and Gov Bailey highlighted that the higher energy prices of the past few months will still have an inflationary impact. While the BoE did not hike, it is certainly not considering a rate cut. For now, it is also benefitting from the run up in borrowing rates over the past few months that have acted as somewhat as a stand-in to actual policy rate hikes in terms of delivering more restrictive financial conditions.

Coming on the heels of yesterday’s hawkish surprise by the Federal Reserve, U.K. markets were likely trading cautiously into today’s announcement with 2yr gilt yields rising close to 5bps in the hour prior to the decision; U.K. wages and employment data published earlier today was also stronger than expected. With the BoE’s communications generally meeting expectations in terms of the vote split, guidance, and the comments provided by policymakers, U.K. yields came off their highs to practically close at the same levels as at the market open; 2s closed 4bps higher and 10s closed flat. At writing, markets are pricing in a total of ~30bps in BoE hikes by end-2026 (peaking at 40bps in April/June 2027), unchanged from yesterday’s local close but down about 5bps from the pre-statement peak. The GBP is in the bottom half of the G10 currency leaderboard against the USD, falling by 0.5% (similarly to the JPY’s decline) to the 1.32 mark.

This report has been prepared by Scotiabank Economics as a resource for the clients of Scotiabank. Opinions, estimates and projections contained herein are our own as of the date hereof and are subject to change without notice. The information and opinions contained herein have been compiled or arrived at from sources believed reliable but no representation or warranty, express or implied, is made as to their accuracy or completeness. Neither Scotiabank nor any of its officers, directors, partners, employees or affiliates accepts any liability whatsoever for any direct or consequential loss arising from any use of this report or its contents.

These reports are provided to you for informational purposes only. This report is not, and is not constructed as, an offer to sell or solicitation of any offer to buy any financial instrument, nor shall this report be construed as an opinion as to whether you should enter into any swap or trading strategy involving a swap or any other transaction. The information contained in this report is not intended to be, and does not constitute, a recommendation of a swap or trading strategy involving a swap within the meaning of U.S. Commodity Futures Trading Commission Regulation 23.434 and Appendix A thereto. This material is not intended to be individually tailored to your needs or characteristics and should not be viewed as a “call to action” or suggestion that you enter into a swap or trading strategy involving a swap or any other transaction. Scotiabank may engage in transactions in a manner inconsistent with the views discussed this report and may have positions, or be in the process of acquiring or disposing of positions, referred to in this report.

Scotiabank, its affiliates and any of their respective officers, directors and employees may from time to time take positions in currencies, act as managers, co-managers or underwriters of a public offering or act as principals or agents, deal in, own or act as market makers or advisors, brokers or commercial and/or investment bankers in relation to securities or related derivatives. As a result of these actions, Scotiabank may receive remuneration. All Scotiabank products and services are subject to the terms of applicable agreements and local regulations. Officers, directors and employees of Scotiabank and its affiliates may serve as directors of corporations.

Any securities discussed in this report may not be suitable for all investors. Scotiabank recommends that investors independently evaluate any issuer and security discussed in this report, and consult with any advisors they deem necessary prior to making any investment.

This report and all information, opinions and conclusions contained in it are protected by copyright. This information may not be reproduced without the prior express written consent of Scotiabank.

™ Trademark of The Bank of Nova Scotia. Used under license, where applicable.

Scotiabank, together with “Global Banking and Markets”, is a marketing name for the global corporate and investment banking and capital markets businesses of The Bank of Nova Scotia and certain of its affiliates in the countries where they operate, including: Scotiabank Europe plc; Scotiabank (Ireland) Designated Activity Company; Scotiabank Inverlat S.A., Institución de Banca Múltiple, Grupo Financiero Scotiabank Inverlat, Scotia Inverlat Casa de Bolsa, S.A. de C.V., Grupo Financiero Scotiabank Inverlat, Scotia Inverlat Derivados S.A. de C.V. – all members of the Scotiabank group and authorized users of the Scotiabank mark. The Bank of Nova Scotia is incorporated in Canada with limited liability and is authorised and regulated by the Office of the Superintendent of Financial Institutions Canada. The Bank of Nova Scotia is authorized by the UK Prudential Regulation Authority and is subject to regulation by the UK Financial Conduct Authority and limited regulation by the UK Prudential Regulation Authority. Details about the extent of The Bank of Nova Scotia's regulation by the UK Prudential Regulation Authority are available from us on request. Scotiabank Europe plc is authorized by the UK Prudential Regulation Authority and regulated by the UK Financial Conduct Authority and the UK Prudential Regulation Authority.

Scotiabank Inverlat, S.A., Scotia Inverlat Casa de Bolsa, S.A. de C.V., Grupo Financiero Scotiabank Inverlat, and Scotia Inverlat Derivados, S.A. de C.V., are each authorized and regulated by the Mexican financial authorities.

Not all products and services are offered in all jurisdictions. Services described are available in jurisdictions where permitted by law.