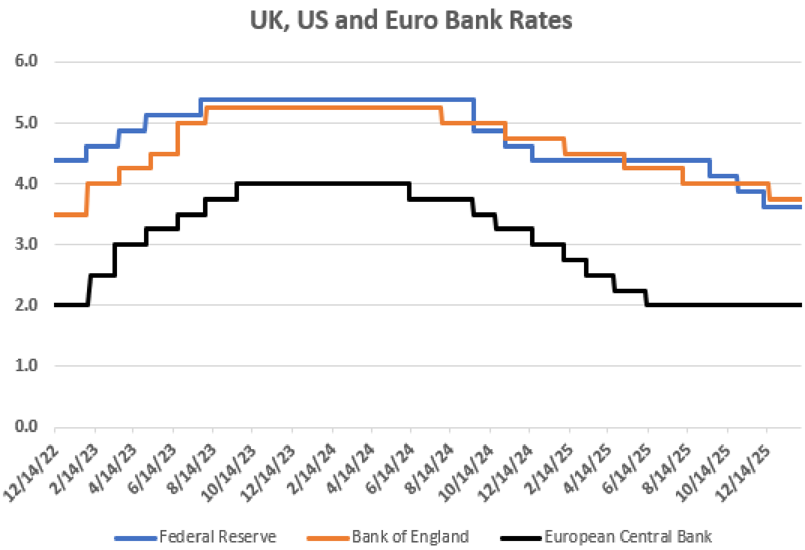
Bank of England holds Bank Rate at 3.75%

On Thursday, the Bank of England held Bank Rate at 3.75%, as had been widely expected.

Date published: 06.02.2026



To nobody's great surprise, the Bank of England followed the European Central Bank's decision (also today) and the Fed's decision of last week to leave interest rates on hold.

However, as in November and December, the Bank's decision was the closest possible: 5-4. The markets had not anticipated such a tight vote and, in response, upped the chances to evens that the next meeting, on 19 March, will deliver a rate cut.

According to the minutes of the meeting, three of those voting for the status quo believed "a more prolonged period of policy restriction was likely to be warranted to mitigate the remaining risks that inflation could settle above the target" whereas the other two (including Andrew Bailey) "judged that the weight of evidence was [not] yet sufficient to warrant reducing Bank Rate at this meeting".

The minutes and accompanying Monetary Policy Report show the Bank projecting that "CPI inflation is expected to fall back to around the target from April, owing to developments in energy prices including from Budget 2025", a lower projection than in the previous Monetary Policy Report, published before the Autumn 2025 Budget. The Bank says that the risk from greater inflation persistence has continued to fade, while some downward risks to

inflation from weaker demand and a loosening labour market are unabated. The central projection for CPI inflation in twelve months' time (Q1 2027) is now 1.7%, against 2.2% in November.

Inflation is not expected to return to 2% until 2029. The Bank also cut its growth forecast for 2026 from 1.2% to 0.9% and shaved 0.1% of 2027, taking the projection down to 1.5%. While the 2027 figure is in line with the OBR's, at the time of the Autumn 2025 Budget the OBR projected 1.4% growth for 2026.

The Bank's stance today is that "Bank Rate is likely to be reduced further' whereas in November its view was a more cautious "Bank Rate is likely to continue on a gradual downward path". In both instances this was qualified with the warning that "judgements around further policy easing will become a closer call'. Market projections before the meeting were that the rate would be 3.25% in a year's time (and then start gradually rising).

Comment

The gilts market pushed up prices on short-dated bonds in response to the Bank's dovish decision, but longer-dated bonds dropped. The latter move was seen as a sign of concern about the current unsettled state of the government.

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