

Falling UK core inflation another headache for the Bank of England

We doubt the latest unexpected fall in core inflation will stop the Bank of England raising rates in August, but it makes the prospect of additional tightening later this year look even more unlikely



We don't believe a strong first half of the year is likely to change the course of Bank of England rate cuts in 2024

At 1.9%, UK core inflation has unexpectedly fallen below target for the first time since March 2017. Reading through the details, it seems that clothing prices played a key role. Prices do tend to fall at this time of the year, but the latest 2.2% decline in clothing costs in June was much steeper than usual. One possible explanation is that retailers are being forced to bring forward discounts as consumers continue to take a cautious approach to spending. If that is the case, then we may see core inflation nudge back up to 2% next time if July's discounts are consequently less steep.

Either way, there's no escaping the fact that core inflation continues to slip as the effect of the sterling's post-Brexit plunge fades. We doubt this will bat too many eyelids at the Bank of England at the next meeting, and we still expect the committee to raise rates in August. After all, policymakers are more focussed on wage growth, which despite a slight slowdown in momentum, has been performing better this year.

However, if core inflation were to continue falling faster than the Bank expects, then we think this would make a second rate hike in 2018 even more unlikely. Once the central bank has hiked rates in August, we think heightened Brexit uncertainty could make it very

complicated for policymakers to raise rates again before May 2019.

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