

UK core inflation rises, but how long will it last?

We expect core CPI to fall back towards the 2% target over the next few months, although this is unlikely to stop the Bank of England hiking in May



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2.7% UK core inflation
(YoY%)

The Bank of England has put markets on guard for another near-term rate hike, in no-small-part because policymakers expect underlying inflationary pressures to build – and at face value, the latest UK data backs them up.

Core inflation rose more than expected to 2.7%, as recreation prices fell considerably less rapidly than would be seasonally expected at the start of the year. Some of this is reportedly down to entrance fees at zoos and gardens, but given that much of the recreation category (things like computers and TVs) is fairly sterling-sensitive, we wouldn't expect this resilience to last. That's because the sharp fall in the pound after the Brexit vote has now more-or-less fed through to

consumer prices and the rate of pass-through is starting to ease. The recent sterling strength will only accelerate this process.

This should see core inflation slow fairly noticeably over coming months, potentially hitting the 2% target over the summer. In principle, this will take some pressure off the Bank of England to raise rates again, although policymakers are more heavily focused on wage growth. The news here has been more positive of late and suggests that pay may be starting to respond to skills shortages and a tighter jobs market. It's still early days (the latest pick-up comes off a low base), but we doubt the data over the next two-three months will change the minds of many policymakers about the direction of travel for wage growth.

For this reason, we've pencilled in a rate hike at the May meeting, although this is still contingent on the Brexit progress – chiefly an announcement on the transition period, as well as some further clarity on the government's preferred future trade model.

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