

## UK inflation surprise boosts chances of Bank of England pause

We're still tempted to say the Bank of England will hike rates tomorrow, and some of the downside surprise in services inflation is down to volatile travel categories. But it's a close call, and both wage and inflation data suggest the end of the current tightening cycle is very close to its conclusion



Bank of England officials have been laying the ground for a pause over recent weeks, and that should be aided by further falls in services inflation over the coming months

Thursday's Bank of England meeting just got a lot more interesting.

August's inflation data has come in well below expectations, and core CPI now sits at 6.2%, down from 6.9%. Both we and the consensus had expected this to dip just a tenth of a percentage point. More importantly, services inflation – which we know is one of the key metrics for the BoE – fell from 7.4% to 6.8%. That's comfortably below the Bank's most recent forecast of 7.2% for August.

Admittedly, these numbers do deserve a bit of caution. The majority of that fall in services inflation can be put down to airfares and package holidays. Both of these saw prices fall in level terms, which is highly unusual for August. These moves don't tell us a huge deal about “persistence” in inflation, in the same way that July's surprise pick-up in services inflation was down to an unusual spike in social rents. The Bank of England will probably treat both July's increase and August's fall

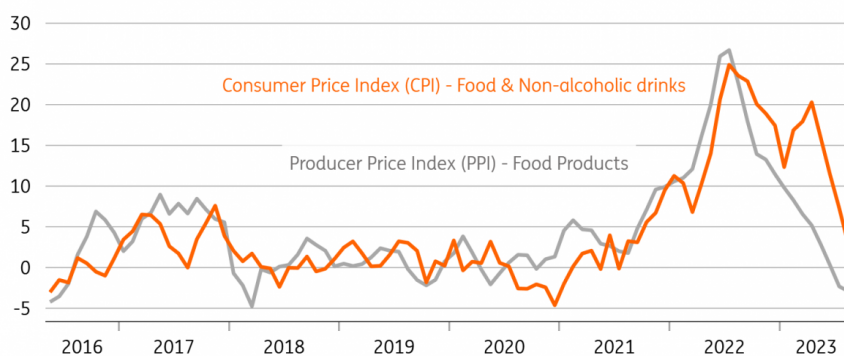
in services CPI with a light pinch of salt given the volatility we're seeing.

That said, we are clearly seeing disinflation across a range of categories, particularly for goods. Household goods and vehicles, both major contributors to core inflation during the supply chain issues, have seen inflation rates collapse over recent months. Food inflation, though less relevant to BoE decision-making, is also coming down quickly. The recent falls in the level of producer prices suggest food inflation will end the year below 10% from 13.6% now.

## UK food inflation is falling quickly, inline with producer prices

### UK food inflation: CPI vs producer prices

Three month annualised change, seasonally-adjusted by ING



Source: Macrobond, ING calculations

All of this makes tomorrow's BoE meeting a much closer call. We'd already been flagging the risk that the Bank could opt to pause this week while still keeping the door open to another hike in November, and that scenario has now become more realistic. Today's downside miss on services inflation followed some slightly dovish news on wage growth last week, where there were hints that this may finally be starting to ease – or is at least reaching a peak. That same report also showed that the jobs market is cooling noticeably.

It's a very close call, but we're still tempted to say the Bank will follow through with a hike tomorrow. But we could get a couple more members voting for a pause, and either way a rate hike tomorrow – if it comes – is likely to be the last.

BoE officials have very clearly been laying the ground for a pause over recent weeks, and that should be aided by further falls in services inflation over the coming months. Lower gas prices are taking a lot of the pressure off service-sector businesses to raise prices. We suspect services inflation will end the year below 6% and fall further through the first half of next year. Rate cuts could begin around the middle of 2024.

### Author

#### James Smith

Developed Markets Economist, UK

[james.smith@ing.com](mailto:james.smith@ing.com)

## Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies)*. The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit [www.ing.com](http://www.ing.com).