

UK inflation surprises higher again as peak draws closer

UK inflation is set to peak at 8.5% or slightly above in April, and is unlikely to fall below 7% at all this year if petrol prices stabilise around current levels. This undoubtedly makes life difficult for the Bank of England, but policymakers are increasingly shifting focus to the deteriorating growth backdrop. We expect one or perhaps two more rate hikes



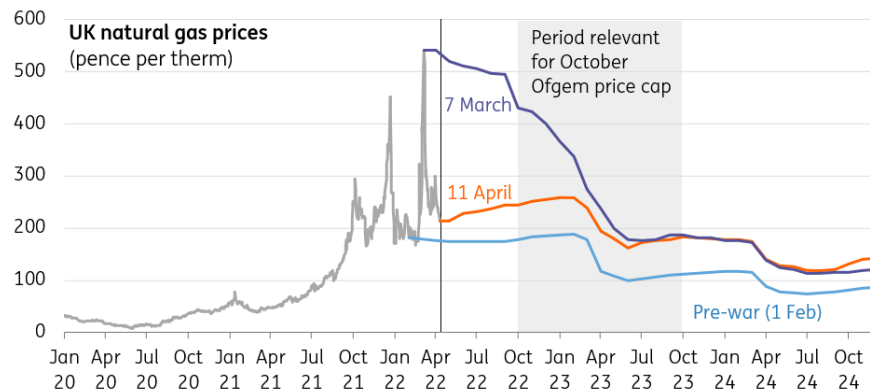
Unsurprisingly, the main source of the acceleration in inflation is fuel prices

Another month, another upside surprise to UK inflation. Headline CPI is now at 7%, up from 6.2% and a few percentage points higher than consensus (and indeed our own forecasts). Unsurprisingly, the main source of the acceleration is fuel prices which increased by almost 10% on the month. But there are large month-on-month price rises in a range of categories, including furniture – a legacy of supply chain disruption – and hospitality.

It still looks like April will mark the peak, and today's upside surprise means we should probably expect that to be around 8.5% or perhaps even slightly higher. That's when the 54% rise in the household energy cap will show through, as well as another slight increase in fuel prices. Based on

current futures prices, we're expecting another 30% increase in the energy cap in October, net of a £200 rebate from the government. That estimate has come down since early March as gas futures have slipped back, and for now suggests we'll avoid a second peak in inflation in the autumn.

Gas prices have fallen back since early March



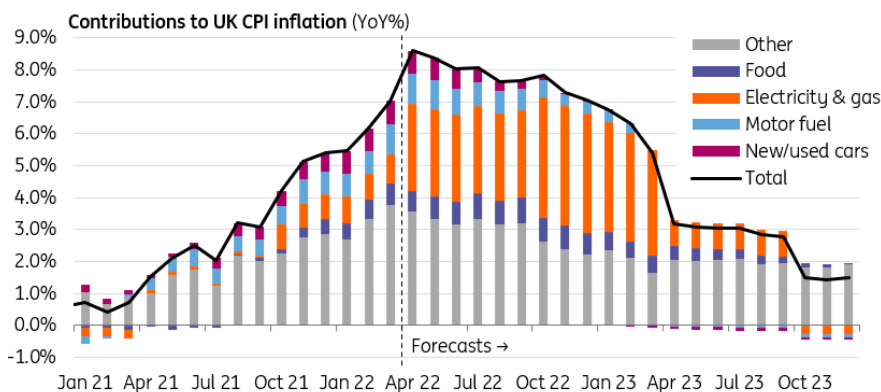
Source: Macrobond, ING

As a result, our best guess is that there will be a very slow decline in headline inflation beyond April, probably not dipping below 7% at all this year if petrol prices stabilise around current levels.

Remember that various durable goods prices began to increase most noticeably from the spring of last year, in response to various supply issues. To generate even higher inflation readings from here, we'd need to see monthly price rises in excess of those we saw last year. That's undoubtedly possible, given the pressure on commodity prices (in effect adding another layer to last year's disruption). And indeed our forecasts already include some further pressure on food prices given higher input costs.

But we are nevertheless likely to see some downward pressure on the headline rate from some goods categories, most notably used car prices. Vehicle inflation has been contributing 0.7pp to the overall headline rate, though price rises appear to have stalled over the past few months.

UK inflation unlikely to fall below 7% this year



Source: Macrobond, ING

While the Bank of England has been resolutely focused on preventing a sustained period of

inflation over the next couple of years, the committee is gradually placing greater emphasis on the associated growth slowdown. After one or perhaps two more frontloaded rate hikes, we expect the committee to press pause on its tightening cycle through the second half of the year.

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