
All eyes on services price inflation

- ◆ Key inflation rates were unchanged in June
- ◆ Stagnant services price disinflation is a concern for the BoE
- ◆ European elections highlight fiscal challenges & policy redirection

UK CPI inflation holds steady at 2% and the labour market is loosening

Headline CPI inflation was 2.0% in June y-o-y, unchanged from May but in line with the Bank of England's target rate. The core rate – that excludes energy and food – and services inflation were both also unchanged at 3.5% and 5.7%, respectively. While there was some evidence of temporary 'event' driven pressures in hotel prices, services price inflation remained broad based and price momentum has been rising.

This perhaps stands to reason against a backdrop of still high wage growth at 5.7% 3m/yr in May and historically low unemployment rate 4.4%. However, the labour market has shown signs of gradual loosening, vacancies are 32% below their May 2022 peak and the number of people employed is 23% higher than its August 2022 trough.

For the Bank of England, pay growth is just about on track to meet their forecast of 5.1% 3m/yr in Q2 but the lack of further downward progress in services price inflation – their most important single indicator - will be cause for concern. We now see the BoE's first rate cut in November.

Consumers point to a more subdued summer for economic activity

UK GDP expanded 0.4% m-o-m in May, in part flattered by a warm weather bounce following a soggy April (when GDP growth was 0%). Nonetheless, on a 3m/3m basis the UK economy grew 0.9% and is on track to record decent second quarter growth. For June, while PMI activity indices pointed to slowing momentum, output remained in expansionary territory at 52.3. And, retail sales – that makes up about 5% of total GDP - fell -1.2% m-o-m in June, however, that follows strong growth in May (2.9%).

GfK consumer confidence then started the third quarter on a less benign note, rising just 1pt in July to -13. Falling inflation and robust wage growth is helping to support a recovery in real incomes; however, households seem to be more cautious. Confidence in own personal financial situation for the year ahead declined for a second consecutive month to +3 and the saving index rose to +27, near its recent highs. The lack of translation from higher real disposable income into consumption perhaps reflects still high interest rates and an element of cost of living scarring.

Post election fiscal direction

The UK general election passed with little fuss despite the Labour Party's landslide victory. In France, the snap parliamentary election ended in gridlock with no party winning an outright majority. However, even before the latest political twists and turns, Europe faced a tough fiscal consolidation challenge.

Disclosure appendix

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