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INDEPENDENT FINANCIAL PLANNING
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August Inflation Numbers

The Consumer Price Index (CPI) for August showed prices rising 0.6% over the month, whereas prices were up by half as much between July 2016 and August 2016.

The consensus had been for a 2.8% annual rate, so the rise to that much nearer 3% surprised the markets and took inflation back to its May peak. The CPI/RPI gap remained at 1.0%, with the RPI (Retail Price Index) annual rate now standing at 3.9% (up 0.3% on July's annual figure). Over the month alone, the RPI was up 0.7%.

The Office of National Statistic's (ONS) favoured CPIH index rose only 0.1% to 2.7% for the year, a smaller move that reflects the different weightings and constituents of that index against the more familiar CPI. (In case you don't know, CPIH index is a new additional measure of consumer price inflation which includes a measure of occupiers' housing costs).

The ONS puts the inflation increase down to a variety of factors:

Clothing and footwear

This category provided the largest upward movement, with average prices rising by 2.4% between July and August 2017 compared with 1.0% between the same two months a year ago. Prices of clothing and footwear usually rise between July and August as Autumn ranges start to enter the shops following the Summer sales season. The rise was larger this year than in 2016 and may have been influenced by the proportion of items on sale, which fell by more between July and August this year than between the same two months a year ago. Annual inflation in the category is now 4.6% at the start of the year it was zero.

Recreational and culture

There was a smaller upward effect from a range of goods and services in this category, where prices rose by 0.1% on the month compared with a fall of 0.3% between July and August last year. The most notable, but small, upward pressures came from data processing equipment and package holidays. In both cases, prices rose by more between July and August this year than between the same two months a year ago.

Restaurants and hotels

The upward effect in this category came from accommodation services – mainly overnight hotel accommodation – where prices fell by less between July and August this year than between the same two months a year ago.

Transport

Overall this category supplied a small upward contribution to the headline rate, but this change concealed two larger, partially offsetting movements, from road fuels and air fares. Motor fuels had a large upward effect on the change in the rate between July and August, with prices rising between the two months this year compared with a fall a year ago. For example, petrol prices rose by 1.8 pence per litre this year but fell by 1.8 pence per litre a year ago. This is a reversal from recent months, where prices have generally fallen compared with rises in the equivalent month a year ago. The change probably reflects the weakening of sterling against the dollar.

As usual, air fares rose between July and August, but the rise of 10.9% was smaller than the 14.4% recorded between the same two months a year ago. As a result, this category was responsible for the largest, partially offsetting, downward contribution to the headline rate.

Core CPI inflation (CPI excluding energy, food, alcohol and tobacco) mirrored the CPI change, with an increase of 0.3% to 2.7%. Of the twelve index components, the lowest category for inflation was recreation and culture, with an annual increase of 1.8%, while the highest was clothing and footwear at 4.6%. Goods inflation rose 0.4% to 3.1%, while services inflation increased by 0.1% to 2.7%.

Producer price inflation (PPI) reversed its previous pattern of falls. The input PPI figure rose from 6.2% in the year to July 2017 to 7.6% in the year to August 2017, still marking a 12.3% fall from its January 2017 peak. Output price (aka factory gate price) inflation rose 0.2% to 3.4%.

COMMENT

The jump in inflation gave a boost to sterling, with the pound rising to nearly €1.11 and $1.326 as markets anticipated that the Bank of England's first increase in interest rates had moved nearer. The Bank's Monetary Policy Committee met recently and no action to increase interest rates was taken. The Bank of England continues its "look through the blip" mantra but has now clearly signaled that UK interest rates will rise. The first rate hike is expected in December. Mark Carney is between a rock and a hard place, clearly a need to meet the Bank of England's inflationary target, yet with Brexit negotiations reaching a critical point, the prospects for the UK Economy could best be described as on a knife edge. Is this an appropriate time for rates to be increased? Time will tell.

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