PM Datanote: U.K. Consumer Prices, November

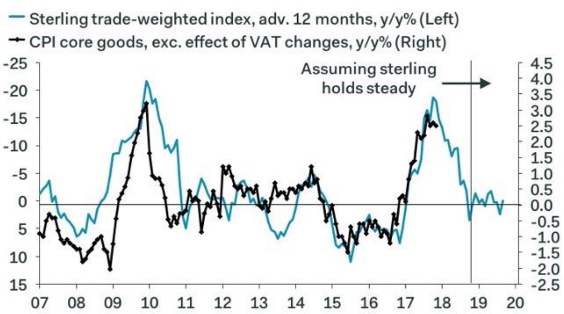
In one line: November’s rate should represent the peak.

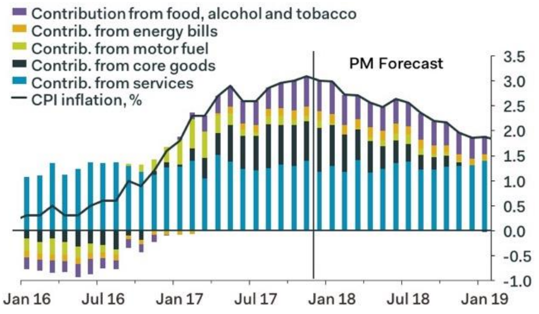
CPI inflation increased to 3.1% in November from 3.0% in October, above the consensus, 3.0%. Core inflation, however, held steady at 2.7%, matching the consensus.

The rise in inflation in November—to its highest level since March 2012—was driven by a 0.06 percentage point increase in the contribution to the headline rate from airline fares inflation. The usual sharp month-to-month fall in plane ticket prices in November depressed the index by much less than in November 2016, because the weight of airline fares in the CPI has declined to 5%, from 8% last year. In addition, food inflation edged up to 4.1%, from 4.0%, as supermarkets continued to respond to the recent 6% year-over-year increase in food producer prices. Consumers also were hit in November by a further wave of price rises by retailers in response to sterling’s depreciation. Retailers, however, already had begun to raise prices following sterling’s depreciation last November, so core goods inflation actually ticked down to 2.5%, from 2.6% in October.

November’s CPI inflation rate is one-tenth above the MPC’s *Inflation Report* forecast and it will compel the Governor to write an Open Letter to the Chancellor explaining why inflation is more than 1% adrift from the 2% target. November’s inflation rate, however, should represent the peak. We expect CPI inflation to fall back to 3.0% in December, as food inflation moderates temporarily and airfares inflation slumps. Then in early 2018, CPI inflation will fall sharply as the anniversary of last year’s huge sterling-related increases in core goods prices is reached. So provided the recent pickup in oil prices doesn’t gather momentum, we expect CPI inflation to return to the 2% target by the end of 2018, enabling the MPC to wait around 12 months before raising interest rates again.

The first chart shows that past movements in sterling indicate that core goods inflation probably has peaked and will fall sharply in 2018. The second chart shows that a decline in core goods’ contribution to the headline rate to zero by the end of 2018 should be enough to bring CPI inflation back to its target within the next 12 months.





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