

# United Kingdom

## Inflation hits Bank of England target for first time in over four years

- **Consumer prices rise 2.0% in December**
- **Falling inflation takes rate-hike pressure off the Bank of England and raises prospect of return to real wages growth in 2014**

Inflation has hit the Bank of England's 2.0% target for the first time since November 2009, suggesting that the UK economy is enjoying a period of strong growth and falling inflation.

Consumer price inflation was 2.0% in December, down from 2.1% in November, according to the Office for National Statistics, having fallen sharply since hitting a peak of 2.9% in June.

Some renewed upward pressure on inflation may come through in early 2014 due to rising energy bills. But it seems likely that widespread discounting on the high street, low global commodity prices and sterling's strength (the 6% appreciation in the trade weighted exchange rate reduces the cost of imports) should help keep inflation close to, if not below, the 2.0% target for some time to come.

The fall in inflation is good news in two respects. First, the easing is a welcome relief to the Bank of England and helps keep the spectre of higher interest rates at bay. Low inflation allows monetary policy to remain loose in the face of faster than expected economic growth and plummeting unemployment.

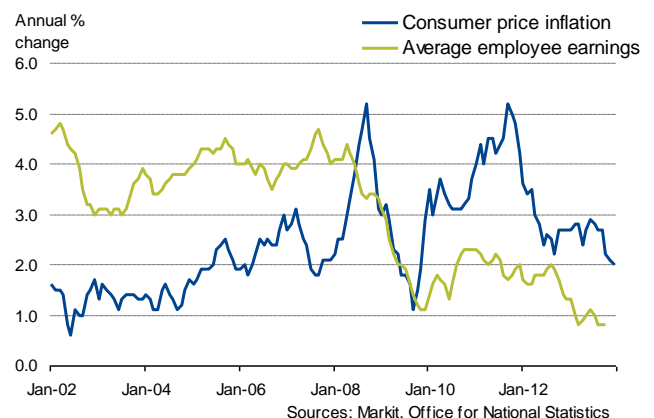
Talk of higher rates has increased in recent weeks because the Bank of England has been wrong-footed by the strength of the economy. Having estimated that unemployment would not fall below 7% until late-2014, it now looks likely that this threshold for higher interest rates to be considered could be breached imminently. However, even if the jobless threshold is crossed, as long as inflation remains under control (at least hovering around the 2.0% target), the Bank can reasonably argue that there is no need to tighten policy.

Second, lower inflation brings closer the prospect of real wages growth. Wages have fallen in real terms by 7.9% since the start of 2009, but with inflation down sharply and pay pressures showing some signs of life. Although real wages continue to fall at an annual rate

of 1.1%, a return to real wages growth is becoming a distinct possibility for 2014. Recruitment consultancies reported the largest rise in starting salaries since 2007 in December, fuelled by surging demand for staff and rising skill shortages.

Wage growth will help ensure a more robust and sustainable economic upturn, as it means the proceeds of the recovery filter through to workers as well as shareholders.

### Inflation and wages



### Real wages growth



### Chris Williamson

Chief Economist

Markit

Tel: +44 207 260 2329

Email: [chris.williamson@markit.com](mailto:chris.williamson@markit.com)

[Click here](#) for more PMI and economic commentary.

For further information, please visit [www.markit.com](http://www.markit.com)