

United Kingdom

Inflation hits two-year high amid rising producer costs

- Official data show consumer prices up 1.2% on a year ago in November
- Rising producer costs likely to feed through to further price hikes in coming months
- Consumer spending to come under pressure

UK inflation rose more than expected in November, with further upward pressure likely to appear in coming months.

Consumer prices rose 1.2% on a year ago, according to the Office for National Statistics, up from 0.9% in October and its highest rate of increase since October 2014.

The upturn comes at a time when producers are facing sharply higher costs, linked to the weaker pound and rising global commodity prices (notably oil), and consumers have shown little appetite to rein-in their spending. The combination of rising costs and resilient consumer demand appear to have led to price rises, especially for clothing.

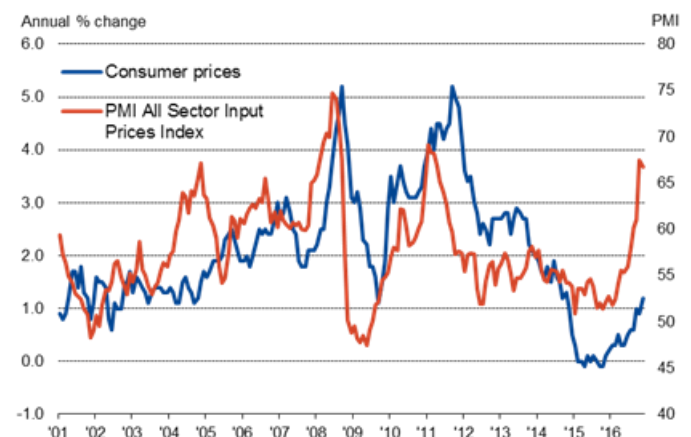
Further upward pressure on prices seems inevitable as rising costs feed through to the high street. Purchasing managers at UK factories report that costs are increasing at the fastest rate for over five years, and one of the highest rates seen in the 20-year history of PMI data collection. The majority of firms have at least partly blamed higher import costs resulting from the pound's depreciation, though many have also noted the increase in global prices for oil and other commodities such as metals and oil-based chemicals, which have shown signs of picking up further in recent weeks. The IHS Materials Price Index (MPI), which tracks global prices for a wide variety of commodities, rose another 1.7% in the first week of December.

The worry is that, as prices continue to rise, consumer spending is likely to be squeezed. [A survey of 1,500 UK households in November](#) found the outlook for personal finances over the coming year to have been the gloomiest for three years, the darker mood stemming mainly from fears of spending power being eroded by rising prices. The survey's gauge of expected inflation in the coming year rose to its highest since October 2014.

At the moment, evidence suggests that spending amid higher prices is being supported by households eating into their savings, but this is clearly unsustainable. The risk is that waning consumer demand will slow the economy.

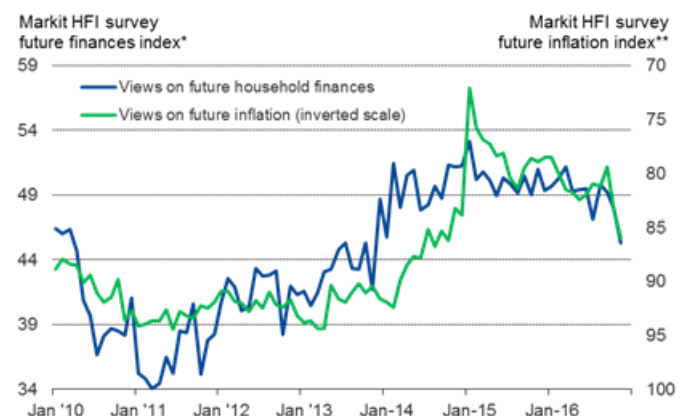
This leaves the Bank of England with a juggling act of supporting the economy as the country rides through Brexit related uncertainty while preventing inflation from spiking higher. The central bank is expecting inflation to rise to nearly 3% in 2018 but will most likely keep interest rates on hold at their historic low this month.

Inflation and producer prices



Source: IHS Markit, Office for National Statistics.

Households' expectations about finances and inflation



Based on monthly survey of 1500 households. Seasonally adjusted index, 50 = no change
 * "How do you think your household's financial situation will have changed 12 months from now?"
 ** "how do you think prices generally for goods and services that you buy will have changed 12 months from now?"

Source: IHS Markit.

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