

United Kingdom

Inflation hits two-year high as companies pass higher costs on to consumers

- **Inflation jumps to 1.0% in September, its highest since November 2014**
- **Survey evidence suggests rise is due to firms passing higher costs on to customers**
- **Costs are growing at fastest rate for five years due in part to weak sterling**
- **Extent of cost increase indicates inflation has further to rise**

UK inflation has risen to its highest for almost two years in a sign that the weak pound is feeding through to increased consumer prices.

Consumer prices rose 1.0% on a year ago in September, according to the Office for National Statistics, the rate of inflation leaping from 0.6% in August to its highest since November 2014.

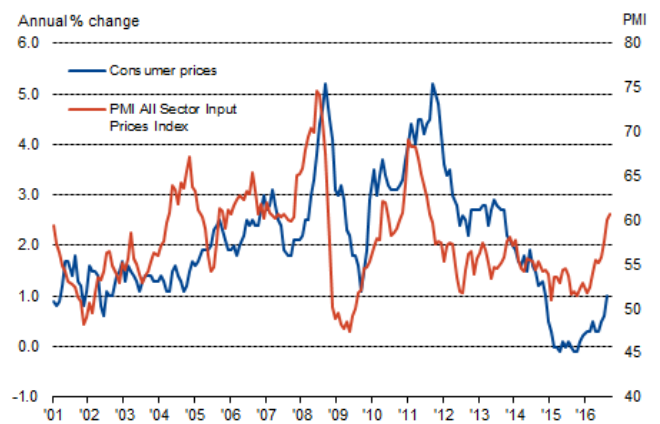
While the ONS found no direct evidence that the pound's fall had fed through to higher inflation, the link is clear from business surveys. IHS Markit PMI surveys found companies' costs to have risen at the fastest rate for just over five years in September (see attached chart), with many firms blaming higher import costs resulting from the steep drop in the value of the pound, especially against the US dollar and euro. Higher fuel costs, linked to the firming of global oil prices, were also widely reported. The September surveys also found average prices charged for goods and services to have risen at the steepest rate since January 2014.

The historical relationship between the PMI survey data on companies' costs and headline inflation indicates that consumer prices have further to rise as firms seek to pass higher costs on to customers in coming months. The Bank of England's 2% target could therefore be breached within months, though much depends on the exchange rate and the extent to which costs continue to rise, as well as the degree to which firms may choose to soak up higher costs via lower profit margins.

The rise in inflation has been anticipated by policymakers at the Bank of England, who have also stated that they will 'look through' any short-term rise due to the pound's weakness. However, the build-up of

inflationary pressures suggests that policymakers may be less willing to loosen policy further in coming months, choosing instead to wait until the inflation outlook becomes more certain.

UK inflation and companies' costs



Source: IHS Markit, Office for National Statistics.

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