

# UK economy

## Inflation moves back up to 2.7%

- **CPI rises from 2.4% to 2.7% in May**
- **RPI rise from 2.9% to 3.1%. CPIH\* up from 2.2% to 2.5%**
- **Upturn in inflation signals ongoing squeeze on consumer spending power, capping economic growth**

UK inflation rose more than expected in May, acting as a reminder that the ongoing erosion of spending power from rising prices will continue to act as a brake on economic recovery.

Consumer price inflation rose from 2.4% in April to 2.7% in May, according to the Office for National Statistics, returning to the rate seen throughout much of the past year with the exception of April's temporary lull. Economists were expecting a rise to 2.6%.

The rate was driven up by air fares, motor fuel, clothing and footwear, though lower food prices helped moderate the rate of increase.

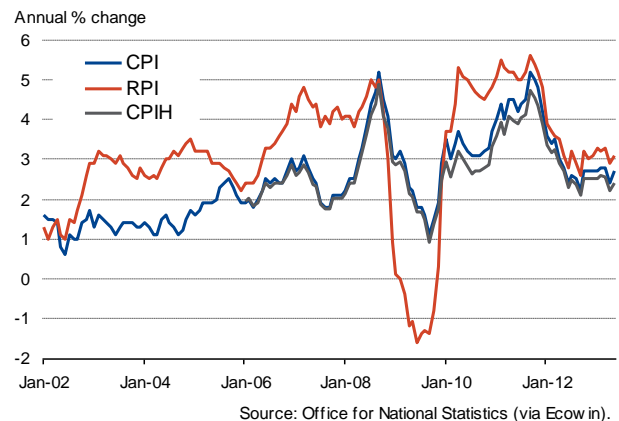
Importantly, inflation continues to run well above pay growth, which was just 0.9% per annum in the three months to April (or 1.3% if bonuses are included), up only marginally on the 0.8% record low seen in March. Back last September, real incomes had been falling at a rate of just 0.3%. That rate of decline has now accelerated to 1.8%.

Real pay has been falling continually since late 2009, which has been one of the factors causing the economic recovery to have been disappointingly weak. However, other factors have helped offset some of the income squeeze from inflation in recent months. Households' financial worries are now at their lowest since the start of 2010, according to Markit's monthly study of 1,500 households in June, with sentiment having been buoyed by people being busier at work, rising house prices and the better economic news flow in the media.

Economic growth appears to have picked up in the second quarter. The business surveys and the monthly official data available so far point to an acceleration of GDP growth from 0.3% in the first quarter to perhaps

0.5%. The worry is that with stubbornly high inflation continuing to erode consumers' purchasing power, this may be as good as it gets. Pay growth needs to outstrip inflation before we see a robust, sustainable and broad-based economic upturn.

### Consumer prices



### Real pay growth



\* CPIH is the new measure of consumer price inflation including owner occupiers' housing costs, which account for around 12% of the total 'basket'.

## Chris Williamson

### Chief Economist

Markit

Tel: +44 207 260 2329

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

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