The Bank of England’s latest forecasts show inflation staying above the 2% target, despite rising UK rate expectations. Prices should get a further boost from the looser fiscal policy announced in the Budget. But, as ever, all those forecasts hinge on a smooth Brexit.

Warming up. The MPC didn’t raise rates last week, but it wants you to know that rate hikes will be on the horizon if we get a Brexit deal. Talk of greater momentum in UK household spending, a strong labour market and above target inflation are signs that the Bank of England’s assessment is shifting. It even pointed to a margin of excess demand that it expects to build as supply remains constrained. You might have expected markets to jump at such a clear warning, but the muted reaction indicates they remain much more focussed on just how likely a deal is to emerge at all, rather than what happens next.

Red box. Last week's Budget was the first to be held on a Monday for 56 years. Back in 1962, the Conservative government ran a 2% deficit, public spending was 38% of GDP. Sound familiar? Following a big upgrade to official fiscal forecasts, Chancellor Hammond announced a £100bn fiscal loosening, injecting £80bn into the NHS, raising Income Tax thresholds and making Universal Credit more generous. Hence national income accounts for around 38% of public services. The deficit, meanwhile, was cut to just 1.2% of GDP in 2018-19, but is forecast to remain stubbornly around 1% of GDP thereafter. The Chancellor is betting on continued steady growth, record employment and a smooth Brexit transition.

Under Steer. Consumer credit growth in the UK softened last month, up by 7.7% – a 3yr low, driven by a sharp decrease in new borrowing for car finance in September, a month traditionally strong owing to new registrations. The figures add to concerns on the motor industry amid new testing requirements impacting supply and distorting the market, waning appetite for diesel cars and worsening consumer confidence. Net credit card, personal loans and overdrafts, however, remained steady.

Two's company. Following the slowdown in EZ manufacturing, the UK's makers also reported a sizable drop in activity in October. The Manufacturing PMI fell from a revised 53.6 in September to 51.1, a 2¼ year low. New orders from both domestic and foreign customers were to blame, with fingers pointed at both Brexit and wider global trade tensions. Neither will be resolved soon. However, the Construction PMI hit 53.2, up from September's 52.1 and the 2nd highest for 16 months.

Bid up. Another solid jobs report from the US – 250k positions were added during October, probably slightly overstating the underlying strength owing to a weak prior month (Hurricane Florence), but undoubtedly robust. And it kept the unemployment rate at 3.7%, the lowest level since December 1969. Meanwhile wage growth continues to creep up,

rising 3.1%y/y during October. Slowly, but surely, the US labour force is reclaiming a little more bargaining power.

A bumpy ride. After a blockbuster growth performance in 2017, the Euro area has slowed for much of 2018. The flash reading for Q3 GDP shows a measly 0.2% increase q-o-q (vs an unimpressive 0.4% in Q2). Anecdotal evidence from business and household confidence indicator suggests possible cutbacks in spending. Mounting trade tensions, financial market turmoil could be to blame. And some one-off factors, too – think the German car industry's struggle with tougher emission standards. Despite this, the ECB looks poised to wind down quantitative easing by year-end**.**

Mixed Bag. October Eurozone inflation rose to 2.2% y-o-y, its highest rate since December 2012. The spike in inflation is attributable to the rally in oil prices as energy prices increased by 10.6% y-o-y. Core inflation, however, registered a muted 1.1% rise. Although the headline figure is above the target rate, policy makers don't foresee an early rate hike. Recent weaker data suggests the 'vigorous pick-up' in inflation hinted by President Draghi may have to wait particularly if the steady improvement in the labour market comes to an end.

Disappointing. The latest Chinese manufacturing and non-manufacturing PMI surveys surprised on the downside in October, signalling further weakness in early Q4. The headline manufacturing index dipped to 50.2 in October (50.8 in September), with weakness widespread. Notably, export orders dropped last month as rising concerns of a potential US/China trade war took their toll. In a similar vein, there was little to cheer in the latest monthly services report. This explains the Chinese authorities' latest tax cutting package, aimed at shoring up confidence in the economy.

Share this:

- Twitter
- Facebook
- LinkedIn
- Email