Soaring inflation cast a shadow over business sentiment. Fresh PMIs released last week reinforce the view that UK economy is flatlining as growing uncertainty about the rising cost of living eats into consumer spending intentions. The squeeze on households’ real incomes is pushing up wage demands with rail workers on strike last week. On the pandemic front UK is experiencing another surge in infection rates.

Sustained. We didn’t need telling, but inflationary pressures remain pronounced. Prices rose 9.1% y/y in May, quicker than the 9% pace in April. The culprits are a familiar bunch. Food prices were up almost 9% on a year ago, while gas prices are almost double. But there were some tentative hints at waning momentum in price pressures. Core prices rose 0.5% between May and April, that’s less than in previous months. And some of the goods prices that had seen outsized gains, e.g., used cars and computers, are starting to retreat. It’s help to policymakers on the lookout for evidence that inflation will eventually slide back to a normal level. But it’s scant consolation to those experiencing a profound impact on their cost of living, with more to come.

Slowdown on the Horizon. UK flash composite PMI was stuck at the same level in June as May’s 15–month low reading of 53.1. Growth continued to wane especially sharply in the manufacturing sector as output edged lower to 51.2, a 16-month low, from 51.6, while the sectors PMI fell from 54.6 to a 23-month low of 53.4. Britain’s economy is showing substantive signs of stalling as high inflation takes a massive hit on new orders. Further, swathes of businesses are being pushed to pass higher costs on to clients and push up pay for workers. The tailwind from the reopening of the economy has faded, having been overcome by headwinds of soaring prices, supply delays, and labour shortages.

Going down for now. Hardly surprising news that UK retail sales have remained on a downward trend in May given the squeeze on households’ disposable income and huge surge in prices. Volumes fell 0.5% from previous month –and were 4.7% lower than a year ago – plus previous month’s solid gain was revised down to 0.4% from 1.4%. The 1.6% fall in food sales was the main driver suggesting that households are spending less in supermarkets as the cost-of-living crisis intensify. Petrol sales volumes rose by 1.1%, demonstrating that households have much less to spend on other goods and services. To add to the saga, consumer mood is grim, with the GfK consumer confidence index falling to a new record low of -41 in June from -40 in May. But with Mr Sunak grants in Q3 there is some hope on the horizon for a rebound in sales.

Onward and upward. If in February 2020 you bought a property – you made the right choice. Since the beginning of the pandemic average property prices increased by 22%, making it the most financially successful period for the homeowners since March 2004. You did particularly good if you bought a detached house (+26%), and even better if you bought a detached house in Scotland (+34%). The slowest growth during this period was in London flats (+7.8%). The question is how the property market will react as cost-of-living crisis and higher borrowing costs bite.

Sunshine and showers. The sun continues to shine on the UK jobs market, with online vacancies up 5% in mid-June, to 123% pre-pandemic levels. But while the jobs thermometer rises, dark clouds loom on the horizon. A net 6% of firms reported declining turnover. Yet the recent balmy weather has encouraged outdoor pursuits, with park visits up 13%. Indeed, only two places see more visits than they did pre-covid, parks (158%) and grocery & pharmacy (109%). Everyone seems to be enjoying nature and stocking up on hay fever tablets. The barometer’s a worry though, as pressure and prices rise in the wholesale gas market.

Outside in. Different central banks around the world are, largely, raising interest rates at different speeds, ranging from the US Federal Reserve’s most recent change of 0.75% to the European Central Bank’s position of expecting to start raising rates at its next meeting. In the UK, the Bank of England is charting a middle way, so far moving by 0.25% each meeting. So, what should it do in response to the faster moves from the Fed? One Monetary Policy Committee (MPC) member, Catherine Mann, thinks it should go faster, sooner. Mann highlights the risk that sterling may fall in value if rates in the UK don’t keep up with those in the US. And a weaker exchange rate would likely mean more imported inflation, especially for food and energy, which is not what the economy needs right now. If this view gains support, expect more MPC members to join Mann in voting for 0.5% rises in future.

It’s not what you think. As Brexit becomes 6 years old, economists start to quantify the effects of the decision to leave with EU. Following the post-referendum period in 2016, new analysis from Resolution Foundation shows that prices went up and wages went down as depreciation of the pound weighted on import prices. And uncertainty caused business sentiment to stagnate. With the implementation of the TCA, 18 months ago, the immediate effects have not been quite as expected. UK exports to the EU are not shrinking relative to the rest of the world. What is most concerning though is that Brexit is affecting UK's trade competitiveness –as measured by total trade as a share of GDP – across both EU and not-EU markets. This will lead to widespread productivity and real income shocks. While the full effects will take years to be felt, UK's economic structure is not going to fundamentally change but it will drive big changes for some sectors.

Faltering. The inevitable is happening. Composite PMI slid to a 16-month low of 51.9 in the Eurozone (vs. 54.8 in May) while US print eased to 51.2 (vs. 53.6 in May). And it's not just the domestic demand weakening. PMI eased notably for the month of June due to the rising cost of living and falling confidence. New export orders contracted at the steepest pace since June'20 in the US. In terms of the headwinds, there are no signs of supply issues, related to the war in Ukraine and business disruption in China, abating, though these might be partially offset by the dampening effect of shrinking margins.

Building a solution. Easing the energy cost burden is a pressing priority for policymakers. And that's putting it mildly. So, it's encouraging that global energy investment is set to rise 8% in 2022, according to the International Energy Agency. Most encouragingly, three quarters is coming from clean energy. Having grown 2% per annum in the five years following the Paris Agreement in 2015, it's been climbing 12% since 2020. Good, but more is needed to meet international climate goals. And a separate concern is cost pressures. They're eating up half of the 8% rise in 2022. And even areas that have sustained price declines over the past decade have flipped –solar panels and wind turbine costs are up by between 10 and 20% since 2020!

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