The countdown for the energy cap hike has begun. Amidst rising price pressures consumers are adjusting their behaviour, borrowing more, while businesses are easing up on hiring. But the impending strain will outlast winter, making government support even more urgent. Elsewhere, things don’t look any better. The Eurozone continues to grapple with soaring inflation while growth momentum remains lukewarm in China.

Cutting back. At the beginning of August 76% of the people in the UK who reported increasing cost of living listed higher fuel prices as one of the factors – an increase of 8ppts over January. And 44% have reported cutting down on non-essential travel in their vehicle – an increase of 17ppts over January. This change in behaviour is noticeable in the fuel consumption. Automotive fuel prices peaked at 48% above the previous year in July, with consumers reducing their fuel demanded per transaction by 16% over the same period. The winter will show how heating demand will change amidst the cost-of-living crisis.

Long-lasting. The hit to UK household living standards will extend beyond the coming winter. Resolution Foundation projects the typical energy bill will swell to £3,760 in 2022/23 and to £6,600 in 2023/24 from £1,500 in 2021/22. Meanwhile, non-pensioners household real disposable income is projected to fall by 10% between 2021/22 and 2023/24 without any government support. While losses will be similar across the income distribution, their implications will be disparate. About 4 million households on pre-payment meters will be unable to smooth payments across the year and will need to find an extra £700/month in Jan-Feb. Plus not everyone receives the same pay rise. Government support is becoming increasingly critical for tempering these losses, but the cost to maintain the same level of support announced in May has jumped by £18bn.

More of the same. Bank of England’s July data on money and banking statistics shows that UK households continued to reduce their pace of savings and borrow more to maintain their current level of consumption amid surging inflation. Net consumer credit rose by £1.4bn in July, above its 2015-19 average while households’ liquid assets increased £4.6bn, below the 2018-19 average. But one area that continues to maintain its resilience despite the headwinds is the housing market, activity held broadly steady in July, despite the eye-watering rise in mortgage rates. The question remains, how much longer?

Fearful firms. Focus on the UK cost-of-living crisis shines brightest on its effect on households. Fair play, given analysis from the Joseph Rowntree Foundation showing some single adults may be paying an impossible 120% of their income on energy in 2023/24. Yet don’t overlook businesses, for it’s firms where the strains are most evident already. Small business sales fell 10% in July, the steepest drop since Lockdown 1.0. The number of UK start-ups has declined 8% recently, and online vacancies have slipped slightly. With wholesale gas prices rising 30% in the week to 28th August, many small and not-so-small businesses face a bleak winter.

Sticky. The Bank of England can’t do much about price rises that come from international gas markets, but it is trying to prevent those rises from spreading across the economy. That job just got harder, according to its own survey of decision makers in UK firms. CFOs report rising costs and upward pressure on wages. So far nothing new. But last month they also estimated that inflation would be around for a lot longer, with CPI about 8% next year and still up at 4% in 3 years’ time. 4% might seem low given today’s rates, but the MPC won’t want to see a forecast of twice its target. This news should add further pressure for a 50bps rate rise on 15th September.

Whammy! Eurozone inflation climbed to a record high of 9.1% in August, up from 8.9% in July, adding to mounting challenges facing households and businesses in the single currency area. Energy costs leapt 38% over the past year. Food & drink prices were 10.5% higher. More importantly for European Central Bank policymakers, weighing whether to implement an outsized interest rate rise later this week, core goods and services inflation rose 0.3ppts to 4.3% despite warnings that companies have yet to fully pass-on the recent rise in production costs to consumers. Another 50bps or possibly even 75bps hike looks increasingly likely.

Healthy rise. The US added another solid dose of jobs last month with payrolls expanding by 315k. For all the talk of a slowing US economy, the pace of job creation has changed little since the spring. The unemployment rate rose from 3.4% to 3.7%. But it was of the healthy variety, attributed to more folk coming back into the labour force. The participation rate of prime-age workers (those aged 25-54) is within a whisker of its pre-Covid level. Yearly wage growth remained unchanged at 5.2%, but the monthly figures point to some reduced momentum. If the Fed had been asked to describe a labour market report that pointed to a ‘soft-landing’ amidst rising rates, last month’s labour market report would fit the bill.

Heat & power cuts. China’s manufacturing sector contracted in August driven by droughts, and power shortages amid heatwaves. The Caixin Manufacturing PMI fell to 49.5 in August, from 50.4 in July as output was dragged by new Covid-19 restrictions coupled with softening demand. Output, new orders, and new export orders all fell in August – below 50 for the latter two, for the first time since May. This was also echoed by China’s official manufacturing PMI, which remained in contraction territory – 49.4 in August vs. 49.0 in July. Similarly, the official composite PMI, fell to 51.7 from 52.5 in July. Overall, the world’s second largest economy is struggling to sustain momentum as risks grow due to a darkening outlook with high inflation and the war in Ukraine hitting external demand.

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