UK Inflation Surprises Again, Limiting Bank of England's Scope for Rate Cuts

Inflation in the UK climbed more than expected in July, further restricting the Bank of England's room to support a sluggish economy with lower borrowing costs.

Figures from the Office for National Statistics (ONS) showed consumer prices rising 3.8% in the year to July, up from 3.6% in June and slightly above economists' forecasts of 3.7%. On a monthly basis, prices edged up 0.1%. The increase marked the fourth consecutive month in which inflation overshot market expectations.

The data lands just two weeks after a contentious decision by the Bank of England to cut interest rates. Governor Andrew Bailey was the decisive vote in favour of the reduction, going against the recommendation of Chief Economist Clare Lombardelli and Deputy Governor for Monetary Policy.

Airfares and Services Drive Increase

The ONS attributed much of July's price rise to higher airfares, reflecting resilient consumer demand for travel. Food prices—often a politically sensitive measure—rose 0.4% on the month and were 4.9% higher than a year earlier.

Even excluding volatile food and energy prices, the so-called core Consumer Price Index (CPI) still climbed 0.2% month-on-month and 3.8% annually, both above predictions. Service-sector inflation accelerated to 5.0% from 4.7% in June, underscoring persistent cost pressures in the domestic economy.

Market Reaction and Policy Outlook

The stronger-than-expected inflation figures cast doubt on the central bank's ability to continue easing policy in the near term.

"With core inflation heading higher, beating market expectations, this brings further into question the Bank of England's ability to ease interest rates in the near term," said Marcus Jennings, bond strategist at asset manager Schroders.

Analysts suggest the data will increase pressure on the Bank to proceed cautiously, balancing the need to revive economic growth against the risk of reigniting price pressures.