ECONOMIC RESEARCH

The NewsLine

January 18, 2016

} MACROECONOMICS | FINANCIAL MARKETS | ECONOMIC POLICY | SECTORS

EUROZONE

Oil price slide signals no need for further ECB action

Dr. Michael Heise
Phone +49.89.3800-16143
michael.heise@allianz.com
Allianz SE
https://www.allianz.com/economic-research/en

Allianz Research
https://twitter.com/AllianzResearch

Although eurozone inflation rates are set to remain mired near zero in the coming months, further ECB loosening is not warranted. The economic upswing in the eurozone is no longer so weak that further measures are called for. An inflation indicator we have calculated also shows no need for further ECB loosening, but argues more for thoughts to focus on exit earlier than currently expected.

The recent slide in the oil price has more or less wiped out the base effect of the end-2014 oil price drop. Eurozone inflation rates now no longer look set to pick up by the middle of this year but will remain mired at the current low level (December 0.2% y-o-y). We have revised our forecast for average eurozone inflation in 2016 down to 0.6% (for 2017 we are forecasting 1.6%).

This rests on the assumption that the oil price slide will come to an end and that prices will pick up again moderately to around USD 45 a barrel by year-end. The euro-dollar exchange rate is likely to average USD 1.09 per EUR in 2016 (marginally below last year's average). For an increase in "home-made" inflation a pickup in wage growth is so far missing, but this is likely to be merely a matter of time as the improvement on the labor market is now making substantial headway. The unemployment rate in the eurozone has fallen from its peak of 12.1% in the spring of 2013 to 10.5% of late and will probably dip slightly below the 10% mark at the end of 2016.

The current concerns about the global economy, tied mostly to the decline in the oil price, are in our view overdone. Not least thanks to the slide in the oil price, we expect the eurozone to achieve decent economic growth of almost 2%

both this year and next. With national fiscal policy no longer tightening the belt as sharply as during the crisis, there is a risk that monetary and fiscal policy combined will give more of a boost than necessary to the upswing now under way. Even if the ECB clearly misses its price norm in 2016 for the fourth year in a row, this is not a sign of dangerous deflation but is attributable to the necessary adjustment processes in the eurozone and the ongoing slide in commodity prices. The ECB should therefore not signal its willingness to take yet further action, thus obliging itself to act at a later stage.

For a while now we have calculated an inflation indicator comprising components which the ECB deems relevant: the rate of change in the harmonized consumer price index year-on-year in percent, the annualized rate of change in a three-month average based on the seasonally adjusted consumer price index compared with the previous three-month average in percent, and long-term market-based inflation expectations based on the five-year, five-year forward inflation swap rate.

The readings of this aggregated (weighted) inflation indicator fell from around 1.8% in early 2013 to a low of -0.3% in January 2015. The indicator currently stands at 0.5%. Based on our inflation forecasts up to the end of 2017, it would climb to just over 1% by the middle of this year and to slightly over 1.5% by year-end (more or less back in line with the ECB's objective of "below but close to 2%"). This pattern currently signals no need for action by the ECB. We expect monetary policy to remain unchanged going into next year – with regard to both the unconventional measures as well as key rates. However, the indicator readings suggest that deliberations about gradually leaving the intensified crisis mode in place since December might already emerge in the second half of 2016.

These assessments are, as always, subject to the disclaimer provided below.

ABOUT ALLIANZ

Together with its customers and sales partners, Allianz is one of the strongest financial communities. About 85 million private and corporate customers insured by Allianz rely on its knowledge, global reach, capital strength and solidity to help them make the most of financial opportunities and to avoid and safeguard themselves against risks. In 2014, around 147,000 employees in over 70 countries achieved total revenues of 122.3 billion euros and an operating profit of 10.4 billion euros. Benefits for our customers reached 104.6 billion euros.
This business success with insurance, asset management and assistance services is based increasingly on customer demand for crisis-proof financial solutions for an aging society and the challenges of climate change. Transparency and integrity are key components of sustainable corporate governance at Allianz SE.

CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

The statements contained herein may include prospects, statements of future expectations and other forward-looking statements that are based on management's current views and assumptions and involve known and unknown risks and uncertainties. Actual results, performance or events may differ materially from those expressed or implied in such forward-looking statements.
Such deviations may arise due to, without limitation, (i) changes of the general economic conditions and competitive situation, particularly in the Allianz Group's core business and core markets, (ii) performance of financial markets (particularly market volatility, liquidity and credit events), (iii) frequency and severity of insured loss events, including from natural catastrophes, and the development of loss expenses, (iv) mortality and morbidity levels and trends, (v) persistency levels, (vi) particularly in the banking business, the extent of credit defaults, (vii) interest rate levels, (viii) currency exchange rates including the euro/US-dollar exchange rate, (ix) changes in laws and regulations, including tax regulations, (x) the impact of acquisitions, including related integration issues, and reorganization measures, and (xi) general competitive factors, in each case on a local, regional, national and/or global basis. Many of these factors may be more likely to occur, or more pronounced, as a result of terrorist activities and their consequences.

NO DUTY TO UPDATE

The company assumes no obligation to update any information or forward-looking statement contained herein, save for any information required to be disclosed by law.