

The NewsLine

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EUROZONE

Inflation busy going nowhere – no matter

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Even if the ECB's inflation target has not yet been met, we see a return to a healthy price environment in the eurozone: services prices are showing signs of normalization, wage growth is creeping up and inflation expectations among consumers continue to rise. The ECB can be content with this picture, especially as fundamentally the buoyant economy points to a further pickup in inflation.

According to today's flash estimate for September, eurozone inflation remained mired at 1.5%. At 1.3% on a year earlier, core inflation (stripping out energy and unprocessed food) was also unchanged compared with August. We are forecasting similar figures for the coming months. Given a base effect largely caused by energy prices, the headline inflation rate will probably dip to 1.2% temporarily at the turn of the year. As things stand, inflation rates "below but close to 2%" are unlikely to be reached until towards the middle of next year – provided the euro does not climb substantially further (our estimates show that a sustained 5% rise in the external value of the euro lowers the eurozone inflation rate by around a quarter of a percentage point).

At the moment it is striking that services inflation at 1.5% is markedly higher than for industrial goods ex energy at 0.5%. In our view this shows that in the global economy price-dampening forces are still at work. By contrast, in the services sector, which is influenced more by domestic economic factors, the trend in prices is returning to normal. Wage growth is also showing signs of perking up. In the second quarter compensation per employee was up 1.6% on a year earlier (the nadir stood at 1% in Q2 2016). Furthermore, the results of the EU Commission survey published yesterday show consumer inflation

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expectations climbing back to the elevated level seen early in the year although current inflation is now lower than at the start of the year.

In our opinion, this all suggests a return to a healthy price environment in the eurozone. The ECB can by all means be content with this even if its target has not yet quite been reached. We see no grounds for concern about its reputation, but the ECB needs to act in a forward-looking manner as the buoyant eurozone economy in particular points fundamentally to an ongoing pickup in inflation.

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