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EUROZONE INFLATION STUCK AT AROUND 1%

Berenberg Macro Flash

Eurozone inflation, September, in %, yoy

	Headline	Core
Actual:	0.8	1.0
Previous (Aug):	1.0	0.9
Consensus:	0.9	1.0
Berenberg:	0.9	1.0

Tough luck for the ECB: Almost every time Eurostat has published inflation data so far this year, the result has been disappointing for the ECB. Eurostat's second reading for headline inflation today shows a drop from 1% yoy in August to 0.83% in September (see Chart 1). This is even a little lower than the first estimate of 0.85%. Eurostat confirmed its earlier estimate of core inflation at 1% yoy after 0.9% in August. Both measures of inflation are a far cry of the ECB's target of "below, but close to, 2%".

Policy package impact: The jury is out as to whether the comprehensive policy package which the ECB Governing Council adopted with a "clear majority" in September will bring inflation closer to target. Some fading of trade tensions, an orderly resolution to the Brexit saga and more fiscal easing could have a bigger impact on the real economy and on underlying inflation than the recent ECB actions. Amid mostly favourable disinflationary pressures resulting from the supply side (demographics, globalisation and technology), the ECB could probably interpret its target more flexibly and settle with a longer horizon over which to bring inflation back to target.

Underlying price pressures building? The first reading of September inflation had already shown a rise in service price inflation from 1.3% yoy in August to 1.5% in September. Service prices are among the better gauges of domestically generated price pressures (see Chart 2). The second reading today adds more colour to that: price pressures for those items of the price basket that are closely linked to domestic demand and the labour market (recreation and personal care, housing costs etc.) keep edging up (see Chart 3). These gains were offset by softer price increases – or bigger price drops in the case of energy for example – across the other components of the price basket (durables goods, communication etc.). While underlying price pressures seem to be building, they do so at a glacial pace. The pace may even slow down in response to lower GDP growth.

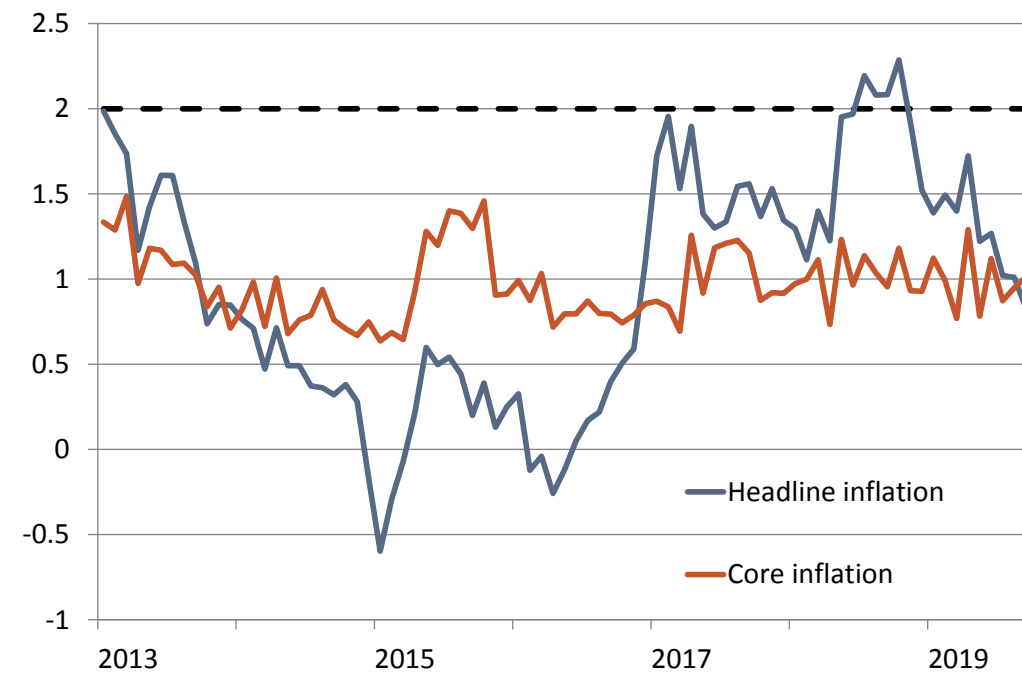
Positive for households: So far, private consumption has been the most important pillar keeping Eurozone growth above the waterline. Healthy employment growth, stable consumer confidence and real income gains support private consumption. While inflation around 1% yoy causes a headache for the ECB, it contributes to healthy gains in real wages of more than 1% yoy amid



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nominal wage growth just above 2%. Some fiscal measures to raise disposable income and purchasing power also help to contain the downside risks to private consumption.

Chart 1: Headline and core inflation (yoy, in %)

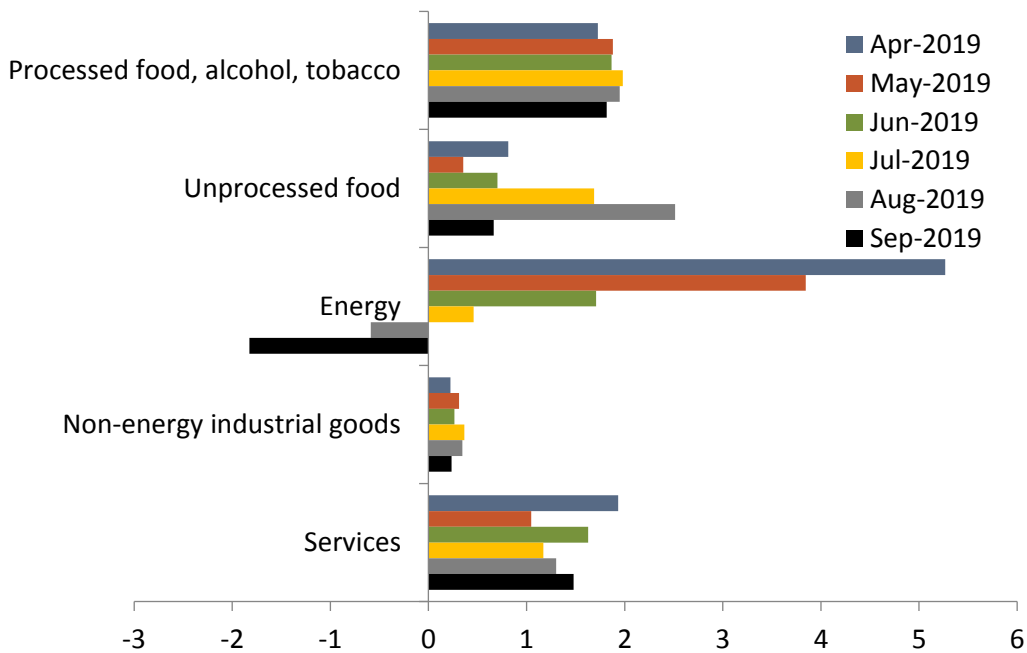


Sources: Eurostat, Berenberg calculations



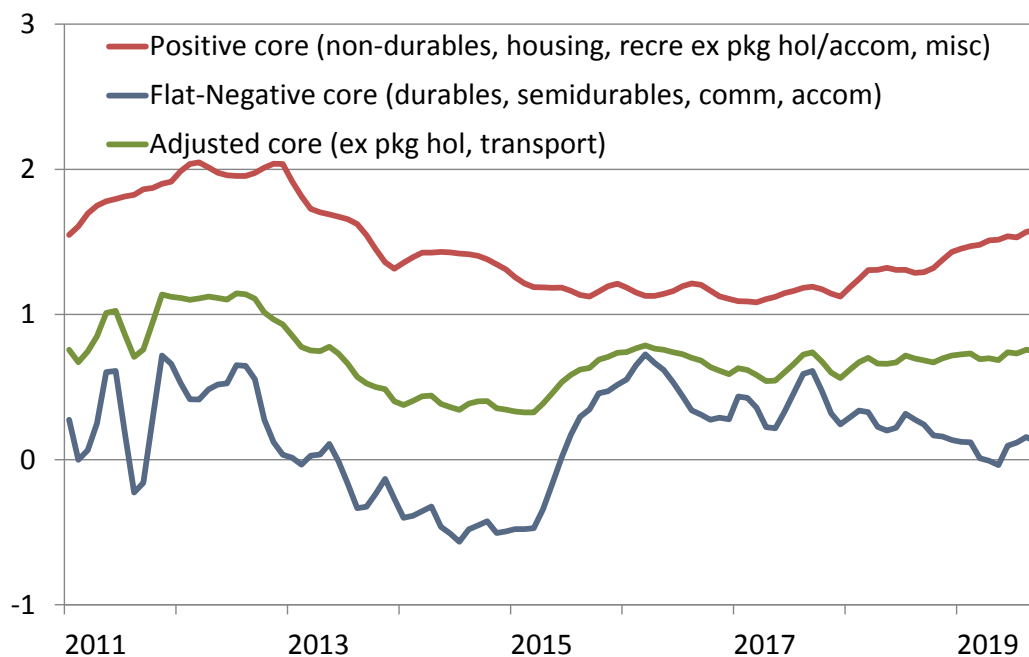
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Chart 2: Inflation by component (yoy, in %)



Source: Eurostat

Chart 3: Softer versus stronger basket



Yoy change in %. Adjusted core: core consumer price index ex package holidays and transport services. Stronger basket: non-durables, housing services, recreation and personal care (ex package holidays and accommodation); and miscellaneous services. Softer basket: durables and semi-durables, communication and accommodation services. Source: Eurostat, Berenberg



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