Italian inflation accelerates further in September, and there's more to come

For once, it was food and leisure rather than energy driving up inflation, but this could be temporary as past wholesale gas price increases will soon drive the energy component up again

According to preliminary Istat data, in September the Italian headline inflation rate accelerated further to 8.9% (from 8.4% in August) and the harmonised headline measure reached 9.5% (from 9.1% in August).

Food and recreation services driving the acceleration

The data breakdown shows evidence of a change in the pattern of how inflation was generated. In September, the main driver of the acceleration was the food component (both fresh and non-fresh food accelerated in double-digit territory) and recreation and hotels and restaurant services, the latter possibly indicating some inertia in the tourism-related reopening effect. Energy goods, which benefited from a favourable base effect, acted instead as a minor drag. The core inflation measure accelerated further to 5% (from 4.4% in August), signalling that the pass-through of past energy price pressures is still in place.

But energy inflation could soon accelerate again

In our view, the September release will not mark the peak in the ongoing inflationary wave. The energy "tax shields" recently confirmed by the government are still in place, but provide only partial protection, and the energy component looks set to provide a renewed push soon. Arera, the Italian energy regulator, announced yesterday that, even taking into account the impact of the last government support package, the price of electricity for protected clients (those who have not opted for the free market) will have to increase by 59% starting October on the back of recent developments in wholesale gas prices. Protected gas prices are also expected to increase substantially but their impact will show up in inflation data only in November, due to a change in the computation method. This means that in both October and November, the energy component will likely fail to benefit from favourable base effects.

Recessionary and PPI pressures contrasting forces over the next few months

To be sure, as the economy will be entering recessionary territory in 4Q22, businesses will likely find it more difficult to pass through price pressures, but the acceleration in producer price inflation to 40% YoY in August (from 35.5% in July) suggests that price inertia might be stronger than hoped for. What seems less likely now is the activation of substantial second-round wage effects. August employment data, also released earlier today, signalled a second consecutive contraction in employment. A fully-fledged recession would make things worse, likely shifting the priorities towards protecting employment rather than getting higher salaries.

All in all, with September data now in the bag, we expect headline inflation to increase further (and possibly peak) over 4Q22, with the harmonised measure flirting with the 10% level, and pushing the 2022 average to 8%. A slow normalisation over the winter would very likely see 2023 average HICP inflation in the 5.5% area.

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