

Eurozone inflation drops further ahead of trade turmoil

Inflation ticked down from 2.3 to 2.2% in March. This was not just on lower energy prices, but also a pronounced decline in services inflation. Even though the latter is in part driven by a late Easter, the decline is a dovish sign for the ECB ahead of possible trade upsets to the inflation outlook



Shoppers in Berlin

While inflationary risks remain prominent for the moment, recent months have shown quite benign developments in core inflation. While core had stuck stubbornly at 2.7% for months, it has now fallen from 2.6 in February to 2.4% in March. This is mainly on the back of weaker services inflation, which dropped from 4% in December to 3.4% in March.

Weak services inflation is in part due to an Easter effect as the holiday falls late this year. That usually results in softer services inflation in March and a bounce back in April. Then again, businesses in the service sector have seen selling price expectations soften and indicated weakness in business activity in recent months, so a return to a lower inflation trend seems in the making regardless of short-term Easter effects.

Uncertainty around the short-term outlook for inflation remains very high. US tariffs could result in

deflationary pressures on the eurozone market as they depress exports and therefore growth. Besides that, it also results in more supply in the eurozone market as the US increases barriers to access. Retaliatory measures from the European Commission will likely have an upward effect on eurozone inflation, though, as they are essentially a domestic tax that gets introduced and will be paid for by consumers to some extent.

Last year at the March press conference, ECB president Lagarde said, “*we will know a little more in April and a lot more in June*”, opening the door to the first rate cut of the cutting cycle. This year, she’ll know an awful lot more in April, as much more will be known about US tariffs imposed on European products and about the retaliation that the European Commission is preparing at the April ECB meeting. That will be key in determining where rates are headed. But all things being equal, today’s inflation print was soft enough to justify another rate cut to get the policy rate more firmly in neutral territory.

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