

Snap | 29 July 2022

Eurozone inflation reaches new highs, driven by supply

Food and core inflation continue to trend higher while the gas crisis is keeping energy inflation elevated. Supply, rather than demand, remains the main driving force behind rising inflation. Don't rule out another 50 basis point hike from the ECB in September



Another ugly inflation reading for July. Both supply-side problems causing high inflation and the second-round effects resulting from this show no imminent sign of relief. Energy inflation was only slightly down at 39.7% as gas supply concerns are keeping prices elevated. The market prices for natural gas reached new peaks this month, translating into high consumer prices once again.

Food inflation also continues to trend up as higher transport costs, shortages and uncertainty around Ukrainian supply have pushed up producer prices which are still being priced through to the consumer. With market prices trending lower for food commodities, some relief could be seen over the course of the second half though.

Core inflation is also still on an upward trend and at 4% is well above the European Central Bank's target. While a smaller percentage of businesses have indicated that they are increasing prices at this point, we do expect the core rate to continue its upward trend in the months to come

as input costs for businesses remain elevated in a large number of sectors, which is putting pressure on margins. Goods inflation increased from 4.3 to 4.5% and services inflation from 3.4 to 3.7% in July, which shows that businesses are still passing higher costs onto the consumer.

Even though GDP growth was still slightly positive in the second quarter, demand is already cooling significantly at this point. This confirms our view that despite rising core inflation, very little of this is demand-driven. High input costs are therefore likely to be the main driver behind the rapidly rising consumer prices with some service sectors like tourism perhaps being the exception.

Ultimately, this makes the impact of the ECB's rate hike on current inflation very limited, although it does add to a further cooling of demand in the eurozone. With a recession looming and inflation reaching new highs, the question is how the ECB will respond to an economy which is already cooling down. Don't rule out the ECB front-loading hikes, so 50 basis points in September is definitely still on the table.

Author

Bert Colijn

Chief Economist, Netherlands

bert.colijn@ing.com

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies).* The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit <http://www.ing.com>.