

Eurozone inflation slides back to 2%

Inflation falls on oil price drop, but the decline in core inflation back to 1% will add to discussion about the ECB's path to normalising rates



Source: Shutterstock

The slight drop in inflation was mainly due to the fall in energy prices.

The drop in the oil price was much larger than the slide in inflation suggests, mainly caused by logistical problems that hindered supply in Germany and Netherlands for example, but also by higher taxes. The logistical issues are likely to fade out, which suggests that the inflation rate will continue to fall modestly over the coming months.

More problematic is the decline in core inflation, which was below analyst expectations. The weak core inflation is in part due to concerns about a cooling economy, which have made businesses hesitant to price through higher input prices such as increased wages.

Softer headline inflation for the beginning of 2019 is largely expected, but the degree to which inflation will drop will be key for the ECB to determine when to hike. For now, the ECB maintains its forward guidance of a rate hike after the summer of next year, but if economic conditions continue to show sluggishness, the question is if that will be maintained.

With downside risks likely to remain a key factor for the Eurozone and already some

moderation in the labour market, it could be that the expected core inflation improvements are delayed further, which would make the forward guidance harder to maintain.

Author

Bert Colijn

Chief Economist, Netherlands

bert.colijn@ing.com

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