

## Eurozone inflation stable as the outlook on prices gets increasingly muddled

Eurozone headline inflation remains stable at 2.4%. With higher energy prices and improving domestic demand, questions about the direction of inflation become louder. Still, we think the economic environment is benign enough for a rate cut in June and expect the ECB to be data-dependent after that



A supermarket in Barcelona

Eurozone core inflation dropped in April from 2.9 to 2.7%, with services inflation moderating the most. The headline number was flat because food inflation accelerated from 2.6 to 2.8%, and energy prices dropped less quickly, from -1.8 to -0.6 % compared to April last year. This was more or less in line with expectations, although core inflation did come in slightly higher than expected.

Yesterday's German inflation data sparked concerns about 'stickiness' as it ticked back up, according to the European definition. Those worries exist for quite a few countries; think of Spain, which also saw inflation tick up again, and France, which is set to see energy inflation rise sharply again in the coming months. Other countries actually saw rapid declines in April.

With [GDP growth faster than expected](#) today, domestic demand is showing signs of recovery in the eurozone, which could make inflation more stubborn. Then again, a weak business survey for April

showed that services inflation is expected to continue to moderate in the coming months. Overall, a more muddled picture on inflation is emerging as we get closer to the target of 2%.

The European Central Bank is data-dependent. Yes, they mention it a lot, but for the coming rate decisions, they really will be. Today's inflation data is a warning that the ECB will likely be careful with rate cuts and may take its time in normalising rates. With an economy showing signs of picking up and unemployment at record lows, the ECB can afford to do so. Still, the eurozone is not the US and demand doesn't bring as much risk to the ECB as it does to the Fed despite today's encouraging 1Q GDP release. We still expect a first cut in June, but the Bank will remain extremely cautious.

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