

## Eurozone sentiment rises further ahead of ECB meeting

As the ESI reaches the highest level in a decade, healthy growth and weak inflation problem continue to baffle the ECB



The August survey indicators all point to some modest improvements compared to July, but the main message is that the economy maintains a healthy cruising speed. Economic growth in the Eurozone seems to be stable at around 2% year-on-year for the moment, well above trend growth.

The Economic Sentiment Indicator showed improvements in both services and industry, showing the current economic strength is widespread. Production and employment expectations both improved in the industry sector, but a drop off in employment expectations in services shows there could be some levelling off regarding job market recovery in the months ahead.

The key takeaway for monetary policy is inflation expectations did not show an uptick. The current weak inflation environment is likely to have continued in August as we expect the inflation rate to have ticked up marginally to 1.4% and core inflation to have remained stable at 1.2%. In fact, it is unlikely that inflation will increase much above 1.5% for the rest of the year and the ESI inflation expectations confirm that.

Consumer inflation expectations decreased marginally from 11.7 to 11.6 in August, and industrial selling price expectations were stable but below the March reading. In the service sector, selling price expectations improved marginally, but they are also still below levels seen earlier in the year.

The difficult situation of healthy growth and weak inflation continues to trouble the ECB ahead of next week's governing council meeting. Although we do expect at least a game plan from the ECB next week and probably a tasking of the relevant committees to investigate tapering options, ongoing weakness in inflation expectations will not make Draghi's life easier.

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