

Eurozone unemployment continues to tick up as inflation turns negative

While unemployment remains massively suppressed by short-time work schemes, inflation is dropping. One-off factors played a role but declining services inflation confirms once more that this crisis is indeed deflationary



Slowly but surely the effects of the historic economic shock caused by Covid-19 are finding their way to unemployment and inflation. Massive stimulus has successfully suppressed the usual passthrough of the downturn to the labour market, but nevertheless unemployment is creeping up. The increase in July was again marginal - from 7.8 to 7.9% - meaning that the total increase in the crisis so far has been just 0.7%. According to our estimates, unemployment would be around 10% at the moment if short-time work schemes weren't in place, meaning that the schemes are a key factor in keeping the unemployment rate this low for the time being.

The inflation rate plummeted in August from 0.4 to -0.2%. The biggest swing in the rate was caused by a reversal in rising industrial goods prices last month, which was a one-off factor due to a change in the start of the sales season in some large eurozone economies. These countries - including France and Italy - postponed the start of the sales to give retailers a breather coming out of the lockdown period. Now that sales have started in some of these economies, prices in goods

have gone into reverse. But there is a more structural element visible in services inflation, which has been dropping since May. The decline from 0.9 to 0.7% in August indicates that lower core inflation is not just noise but that the weak economy is starting to have more of an effect on price growth.

As short-time work schemes are being extended at the moment, it is likely that the unemployment rate will continue to creep up at a very subdued pace for quite some time. This provides a comfortable cushion against income declines and negative second round effects on the economy but still, the direction of unemployment is up. For the European Central Bank, which meets later in the month, these numbers are more a confirmation of what they already know: this crisis is deflationary despite some of the novel elements to it.

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