

## German headline inflation continues gradual downward trend in April

After energy price inflation, it is now food price inflation that has started to drop as a result of base effects, pushing down German headline inflation. Core inflation, however, still doesn't show any sign of retreating



To paraphrase Meghan Trainor's song: it's all about that base. German headline inflation continued its downward trend, coming in at 7.2% year-on-year in April (from 7.4% YoY in March), but what looks like a broader disinflationary process is still only disinflation on the back of base effects. Yes, headline inflation has now dropped from its winter peak of 8.8% to 7.2% YoY and the HICP measure came in at 7.6% YoY, from an 11.6% peak in October last year. But the sharp drop in headline inflation is mainly the result of negative base effects from energy prices and in April for the first time also food prices. Underlying inflationary pressures, however, remain high and given that the month-on-month change in headline inflation was still above historical averages for April, there is no reason to cheer.

### Food price inflation finally starts to come down

Today's drop in headline inflation will support the view of those who always advocated that the

inflation surge in the whole eurozone was mainly a long but transitory energy price shock. If you believe this argument, today's drop in headline inflation is the start of a longer disinflationary trend. As much as we sympathised with this view one or two years ago, inflation has, in the meantime, also become a demand-side issue, which has spread across the entire economy. The pass-through of higher input prices, though cooling in recent months, is still in full swing. Widening profit margins and wage increases are also fuelling underlying inflationary pressure, not only in Germany but in the entire eurozone.

## Headline inflation to come down further but core will remain high

Available German regional components suggest that core inflation remains high. While energy price inflation continued to come down and food price inflation for the first time started to slow down, most other components showed broadly unchanged inflation rates. At the same time, selling price expectations in the manufacturing sector have almost dropped back to their historical averages but selling price expectations in services remain high. All of this suggests that the pass-through of inflationary pressure is gradually slowing down but is far from over.

Looking ahead, let's not forget that inflation data in Germany and many other European countries this year will be surrounded by more statistical noise than usual, making it harder for the European Central Bank to take this data at face value. Government intervention and interference, whether that's temporary or permanent or has taken place this year or last, will blur the picture. In Germany, for example, the Bundesbank estimated that energy price caps and cheap public transportation tickets will lower average German inflation by 1.5 percentage points this year. And there is more. Negative base effects from last year's energy relief package for the summer months should automatically push up headline inflation between June and August.

Beyond that statistical noise, the German and European inflation outlook is highly affected by two opposing drivers. Lower-than-expected energy prices due to the warm winter weather are likely to push down headline inflation faster than recent forecasts suggest. On the other hand, recent wage settlements and still decent pipeline pressure in services are likely to keep core inflation high. We continue to expect that German headline inflation will average at around 6% this year.

## 25bp rate hike most likely at next week's ECB meeting

For the ECB, today's data had something for everyone. Positive and negative surprises on growth and rather erratic inflation data can be used by both doves and hawks. As a result, an already heated debate on whether to hike rates by 25bp or 50bp will become even more heated. We still think that next week's Bank Lending Survey results will tilt the balance in one of the two directions. Given the growing divide within the ECB, a rate hike of 25bp would still be a typical European compromise. However, today's fireworks of very opposing data points have not made the ECB's life any easier.

## Author

### Carsten Brzeski

Global Head of Macro

[carsten.brzeski@ing.de](mailto:carsten.brzeski@ing.de)

## 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>.