German inflation continues to slow

Lower energy prices and less of the usual seasonal impact from the Easter break pushed down German headline inflation in April

Source: Shutterstock

The just-released flash estimate of German inflation for April brought some relief for the European Central Bank as headline inflation came in at 2.1% year-on-year, down from 2.2% YoY in March. However, at second glance, the increase in core inflation, to 2.9% YoY from 2.6% the previous month, suggests that the inflation threat has still not disappeared for good. The European inflation measure dropped to 2.2% YoY from 2.3% in March.

The available regional state data suggests that falling prices for energy were the main driver behind slowing headline inflation. At the same time, services inflation accelerated. It's probably more a sign of weak economic activity; the usual seasonal 'Easter bunny' effect hardly registered in the data. Normally, when the Easter break shifts from one month to the other, headline inflation moves on the back of base effects. This year, these base effects didn’t even show in subcomponents like leisure or hotel prices.

Looking ahead, the current two most important macro themes will also have implications for headline inflation: trade tensions and fiscal stimulus. While the current phase of trade tensions and high uncertainty will insert more disinflationary pressures via lower energy prices, a stronger euro and possible dumping of European or Chinese products, fiscal stimulus will rather add to inflationary pressures over the longer term. Investments in infrastructure, a sector which, until recently, already suffered from the lack of skilled workers and high material costs, are likely to bring back some inflation.

For the ECB, today's growth and inflation reports clearly pave the way for some additional, though very gradual and measured, rate cuts, without giving any reasons for panic.

Author

Carsten Brzeski
Global Head of Macro
carsten.brzeski@ing.de