Germany: No inflation

Inflation came in at 0.0% YoY in August, reflecting the VAT cut and low energy prices.

Based on the inflation outcomes in several regional states, German inflation came in at 0.0% year-on-year in August, from -0.1% YoY in July. The harmonised index, relevant for ECB policy making, dropped to -0.1% YoY, from 0.0% in July.

The regional data paint a picture of diverging inflationary trends in the German economy. The negative base effect from low energy prices is keeping headline inflation low but there is more: the VAT cut of July is most visible in prices for food and clothing, while at the same time inflation for services has remained almost stable. The fact that the increase in hotel prices is still very much in line with the trend seen prior to the VAT cut suggests that lower taxes are also used to support businesses and are not necessarily entirely passed on to consumers.

There had been speculation as to whether the current crisis would be deflationary or inflationary. While rising unemployment and very little pricing power for companies argue in favour of deflationary trends, monetary and fiscal stimulus eventually argue in favour of more inflationary pressure. Today's German inflation data suggest that for the time being the deflationary threat is clearly more pressing than any inflationary one.

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