

## Germany: Inflation shock

The surge in German headline inflation could pose a new communication challenge for the ECB



### Watch out, the inflation monster is back

Based on inflation outcomes of several regional states, German inflation in January came in at 1.0% year-on-year, from -0.3% in December. The harmonised index, relevant for European Central Bank policymaking surged to 1.6%, also remained unchanged at -0.7% YoY.

This was the largest monthly increase in a long time.

### More to come

Before anyone gets too scared, this surge is mainly the result of the reversal of last year's VAT reduction, higher energy prices and the new carbon tax.

On the back of the VAT cut reversal, core inflation has also increased. Judging from the available regional data to around 1.5% YoY. With the VAT increase, it is hard to disentangle the negative impact from the latest lockdown measures and the positive impact from a higher VAT on prices.

---

*Looking ahead, today's inflation number is just the beginning of a*

## *period of significantly higher headline inflation in Germany*

---

Interestingly, the prices for clothing increased sharper than justified by higher VAT, probably another result of the lockdown comparing fictive prices of closed retailers with winter sale prices from last year.

Looking ahead, today's inflation number is just the beginning of a period of significantly higher headline inflation in Germany. The full impact of higher energy prices compared with last year will show in the coming months. Also, the full base effect from the VAT cut reversal will only be reflected in inflation numbers after the summer. Together with price mark ups in some sectors once the economy starts to reopen again, headline inflation in Germany could be pushed above 2% after the summer.

## **A new communication challenge for the ECB?**

However, before getting too nervous about inflation, we highlight that the economy will not reach its pre-crisis level before early-2022, unemployment and insolvencies are bound to increase and a further euro appreciation will be rather deflationary, putting a lid on any inflationary pressure. Nevertheless, these inflation developments could easily present a new communication challenge for the ECB.

Recent comments on possible yield curve control, warnings against premature tightening of monetary and fiscal policies as well as more emphasis on symmetry and hence the possibility of inflation overshooting are just a few tools the ECB could use to preserve what seems to be the ECB's latest treasure: favourable financing conditions.

### **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 [www.ing.com](http://www.ing.com).