Germany: The Easter Bunny strikes back

The small uptick in headline inflation offers support for ECB hawks. But only at first glance

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Based on the results of eight regional states, German headline inflation increased for the first time since November last year, coming in at 1.6% year-on-year in March, up from 1.4% YoY in February. According to the harmonised European definition (HICP), the measure more relevant for ECB policy making, headline inflation accelerated to 1.5% YoY, from 1.2% in February.

At first glance, stronger German inflation data looks like a welcome argument for ECB hawks as it seems to confirm their view that prices are finally accelerating. However, on second glance German inflation data is actually providing further evidence that even in the cyclically most advanced economy of the Eurozone, a wage-price-spiral is hardly noticeable.

> *Once again, it's the Easter bunny effects blurring the German inflation picture*

In fact, today's increase in headline inflation was mainly driven by higher food prices and prices for leisure activities and holiday package deals. Core inflation measures, where available, were still lower than January. As the Easter vacation break this year started in March and not in April as last year, this seasonal effect is the main driver behind the stronger annual data. Once again, it's the Easter bunny effects blurring the German inflation picture.

All of this means that the current economic controversies on whether or not the Phillips curve is broken and whether higher wages still lead to higher inflation will not be solved anytime soon. For the ECB this means that even though there seems to be a consensus that QE should end, there is still disagreement on the timing and nitty-gritty details of tapering, as indicated by several speeches of the most prominent and influential ECB members since the March meeting.

Earlier this week, Jens Weidmann's speech in Vienna received quite some market attention, even though an end to QE before 2018 draws to a close and a first rate hike in mid-2019 did not sound like a big surprise to us. The more interesting question is whether Weidmann talked in his capacity as leader of the ECB hawks or in an attempt to be presidential, reflecting the broad consensus view of the entire Governing Council.

While the latter would be broadly in line with our own ECB scenario, the former would keep the option open for a more dovish outcome, e.g. an extension of QE at a very low level until March 2019, which would consequently postpone a first rate hike towards the second half of 2019.

The Easter bunny came early enough this year to push up German inflation; it must have come too early for the ECB as the release of the March meeting minutes was postponed to 12 April - an indication that the ECB wants to have a quiet Easter break, without new QE tapering speculations.

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