Italian inflation continued to decelerate in August

The August inflation release provides comforting signals of a broad-based deceleration in inflation, including the core measure. The trend looks set to continue until year-end, at a pace which will be affected by residual base effects. We stand by our 6.4% forecast for 2023 HICP inflation

Goods and services both decelerate

The preliminary estimate by the Italian National Institute of Statistics (Istat) of August consumer prices confirms that inflation is on a solid decelerating path. The headline measure was down to 5.5% (from 5.9% in July), broadly in line with expectations, driven by the non-regulated energy component, recreational services, fresh food, transport services and durable goods, only partly compensated by housing services and regulated energy goods. The statistical carryover for 2023 headline inflation now stands at 5.7%.

Both goods and service inflation decelerated to 6.4% and 3.6%, respectively, and food inflation, at 9.6% in August, fell below double digits for the first time since July 2022.

Core inflation falls

Core inflation, which strips out energy and fresh food, and is a key indicator in the eyes of the European Central Bank, also sent encouraging signals, falling to 4.8% from 5.2% in July, confirming the deceleration pace seen since June. This reflects the deceleration in services, not yet impacted by the recent acceleration in hourly wages (at 3.2% year-on-year in June)

Further declines in inflation expected...

As the pace of the decline in headline inflation is still being set by the energy component, we should be aware that substantial base effects have yet to play out as a decelerating factor over the autumn. Indicators such as import prices and producer prices continue to point to softer headline inflation ahead. Import prices contracted by 9.8% in June and producer price inflation, at -5.5% YoY in June, has been in negative territory since April. The latter is still driven by the energy component (-26.2% YoY in June), however stripping out energy and construction, the PPI inflation read in June of 2% confirms a clear declining trend.

...but the pace will depend on a combination of factors

If the pricing pipeline is sending encouraging signals, other indicators coming from August business surveys deserve attention. For the first time since September 2022, the manufacturers' pricing intentions balance rose in August from the previous month and increased in services for the second consecutive month. The only area where the deceleration in price increase intentions remains in place is the retail sector. This is a warning signal that the current pace of inflation deceleration, particularly at the core level, cannot be taken for granted.

The wage cost variable will likely have a say in the process. Here, indications are mixed. If some more wage concessions look likely over the next few months as a consequence of past inflation surprises, labour market tightness might loosen a bit. July labour market data, also released earlier today, offer some tentative evidence of this. For the first time over the last eight months, employment declined from the previous month and the unemployment rate edged up to 7.6% (from 7.4% in June). The Italian labour market is possibly finally responding to cyclical developments.

After today's inflation release, we confirm our forecast for average HICP inflation for 2023 at 6.4% YoY.

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