

Europe Flash

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Economic Analysis

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EZ final January inflation revised upwards

Inflation remained stable at 0.8% in January, in line with our initial forecasts

- **The preliminary estimate for headline inflation has been revised upwards by 0.1pp to 0.8% YoY in January and core inflation by 0.1pp to 1% YoY**

Eurostat has revised upwards its preliminary estimate for eurozone inflation in January by 0.1pp, such that it remained stable at 0.8% YoY, which is in line with our initial forecast (BBVA Research: 0.8% YoY), but still below consensus (0.9% YoY). This weakness was due to the fact that the lower energy prices (-1.2% YoY) and the more limited inflation of fresh foods (1.3% YoY after 1.5% YoY) were offset by the 0.1pp increase in core inflation, in line with our forecasts (Table 2). As we anticipated after the change in methodology for calculation of price seasonality in the services sector in Germany, the uptick in inflation of the latter (1.2% YoY after 1.0% YoY) was the principal cause for the increase in core inflation, while the rise in non-energy industrial goods prices and processed foods remained relatively stable (0.2% YoY, 2% YoY, respectively) (Chart 1). Finally, note that part of this price stability is also due to the change in the weightings of components, which puts more emphasis on services and foods, to the detriment of energy and non-energy industrial goods. By country, there was also a slight increase in the weightings of Germany and France at the expense of Italy and Spain.

- **By country, inflation stabilised overall, although with significant differences by component**

As noted above, the higher inflation in the services component throughout the eurozone reflects the strong increase in Germany (+0.4pp to 1.4%), marking a return to the levels seen last year after the disappearance of the transitory effects of seasonality on the prices of these products. Also, in Germany there was also an increase in inflation in non-energy industrial goods (+0.4pp to 0.9% YoY), while the increase in processed food prices was much more moderate (+0.1pp to 3.5%). As a result, core inflation in Germany rose by 0.3pp to 1.5% YoY. This was offset by the fall in energy prices, such that headline inflation remained unchanged at 1.2% YoY.

In France, both core and headline inflation remained stable at 0.8% YoY in January. In this case, the increase in inflation in the services component (+0.3% to 1.7% YoY) was offset by a steep fall in non-energy industrial goods prices (-0.8% YoY after -0.1%), while the moderation in the rise in energy prices (+0.3% YoY down from 1.1%) was offset by the stronger growth in fresh food prices (1.3% YoY, up from 1%).

Inflation in Italy, and more particularly Spain, were below the eurozone average at 0.6% YoY and 0.3% YoY respectively. The principal difference in the performance of these two countries with regards to Germany and France was the performance of services, which have remained relatively stable in Italy (around 1% YoY after decelerating from 1.5% in the middle of 2013) and fell again in Spain (-0.2% YoY), as a reflection of the weakness of domestic demand in these economies. As a result, core inflation remained at 1.0% YoY in Italy, while in Spain it slowed slightly to 0.1% YoY.

- Inflation will moderate slightly in 1Q14**

Our forecasts still assume that inflation will decline slightly in the next two months (at around 0.6% YoY), partly due to another fall in energy prices, but also due to the moderation in core inflation, particularly in March as a reflection of the change in the calendar effect of the Easter holidays. Inflation should continue to tick up in the second quarter by around 0.3pp to 0.9% YoY and will remain relatively stable until the last quarter of the year, when inflation might return to levels above 1% YoY.

The weak but positive rates of growth that we expect in the coming months imply that it is unlikely that disinflation will continue. We consider that a scenario of low and stable rates of inflation around 0.9% YoY is more likely while the recovery in domestic demand consolidates, as observed since 2Q13 excluding the impact of higher taxes on prices.

Table 1
Eurozone. Annual changes (HICP, %)

	% YoY		% MoM	
	December2013	January2014	December2013	January2014
HICP	0.8	0.8	0.3	-1.1
Energy	0.0	-1.2	0.6	0.0
Unprocessed food	1.5	1.3	1.3	0.6
Excluding energy and unprocessed food	0.9	1.0	0.2	-1.4
Services	1.0	1.2	0.6	-0.4
Non-energy industrial goods	0.3	0.2	-0.3	-3.8
Processed food	2.0	2.0	0.0	0.3

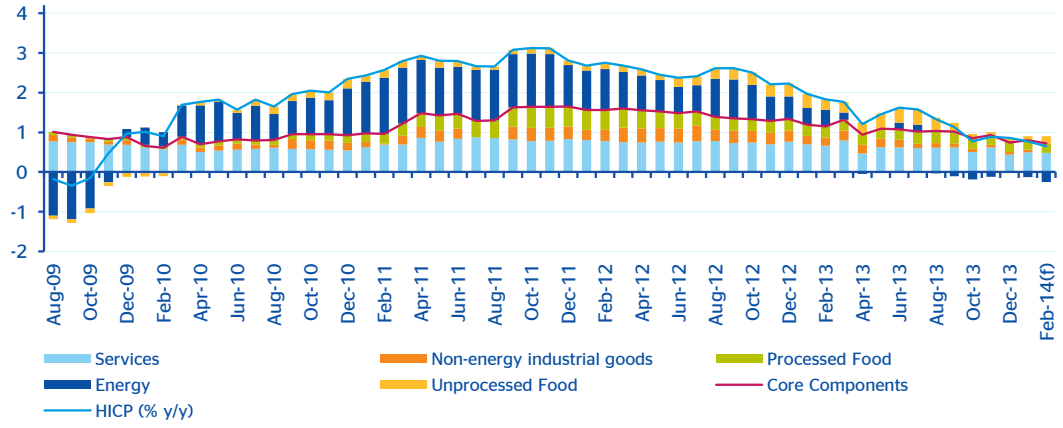
Source: Eurostat and BBVA Research

Table 2
Annual inflation rate (HICP, % YoY): forecast errors

January 2014	Weight %	Forecast %	Observed %	Confidence interval forecast (*)
Headline	100.0	0.8	0.8	(0.6 ; 0.9)
Energy	10.80	-1.6	-1.2	(-2.0 ; -1.1)
Unprocessed food	7.48	1.4	1.3	(0.8 ; 2.0)
Excluding energy and unprocessed food	81.73	1.0	1.0	(0.9 ; 1.2)
Services	42.81	1.4	1.2	(1.3 ; 1.5)
Non-energy industrial goods	26.67	0.5	0.2	(0.3 ; 0.7)
Processed food	12.25	1.9	2.0	(1.8 ; 2.1)

(*) 80% confidence.
Source: Eurostat and BBVA Research

Chart 1
Eurozone. Annual HICP inflation rate. Contribution by component



Source: Eurostat and BBVA Research

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