

Eurozone | Negative inflation in February and moderation in core, worse than expected

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Greater drop in energy prices and strong moderation in core inflation

Although we have yet to learn the final data, Eurostat's flash estimate was below our expectations, as the national data anticipated late last week, noting that inflation fell by 0.5pp to -0.2% YoY in January (BBVA Research and consensus: 0% YoY). A greater fall in energy prices (-8% YoY from -5.4% YoY in January) and lower unprocessed food prices (0.3% YoY after 1.4% YoY January) partly explain the 0.3pp reduction in headline inflation, but the negative surprise came from a greater moderation in services inflation (1% YoY from 1.2% YoY) and, in particular, non-energy industrial goods (0.3% YoY after 0.7% YoY), which explain the remaining 0.2pp of the falling prices and send core inflation to 0.8% YoY from 1% YoY in January (Figure 1).

Negative inflation rates could continue until summer

The evolution of oil prices will continue to be the main determinant of the behaviour of inflation in the coming months, so we now expect the drop in inflation to intensify again in March (by about 0.3pp) and to continue throughout the second quarter (when we expect oil prices to reach the minimum), and to only gently pick up after the summer to slightly positive rates later this year (about 0.5% YoY).

Regarding core inflation, our models suggest that it could moderate slightly in the short term, while remaining relatively stable for the remainder of the year at rates somewhat below 1% YoY. Today's data may reflect a greater slowing down in domestic demand, on which increasing uncertainty, both global and domestic, could be weighing, but they may also reflect higher second-round effects than ly expected, especially in the prices of non-energy industrial goods. February confidence surveys suggest that companies are passing on the decreasing prices of raw materials to consumers in the eurozone as a whole.

Figure 1

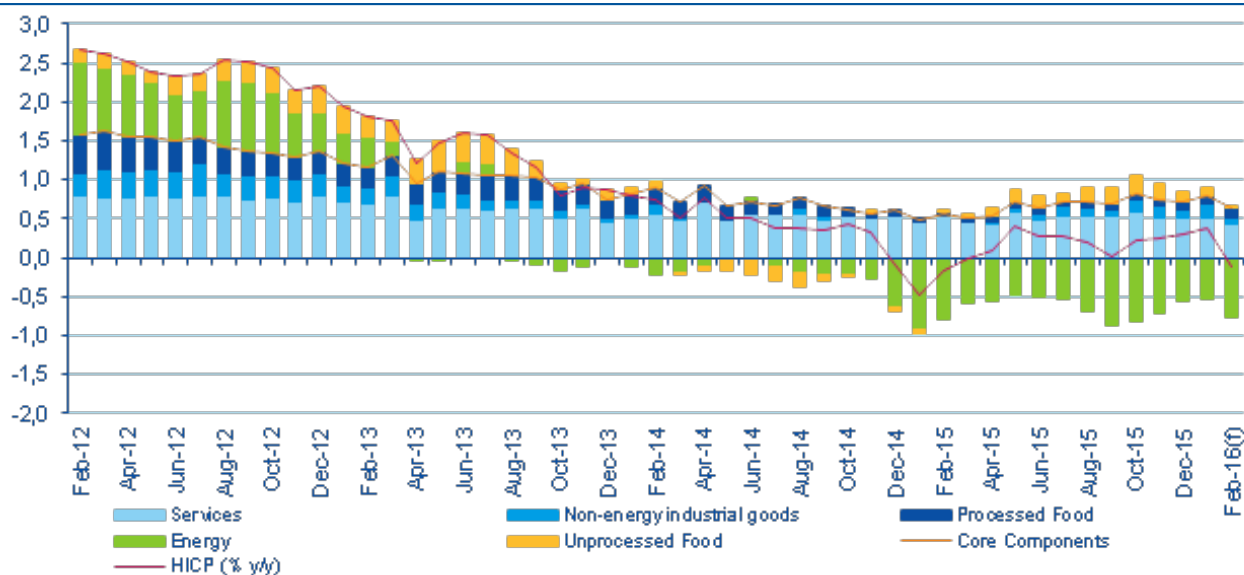
Eurozone. HCPI inflation (% YoY)

	Observed		February 2016	
	Decembre 2015	January 2016	Flash Estimate	BBVA Research
HCPI	0,2	0,3	-0,2	0,0
Energy	-5,8	-5,4	-8,0	-7,8
Fresh Food	2,0	1,4	0,3	0,7
HCPI excluding energy and food	0,9	1,0	0,7	0,9
Core excluding Fresh Food and Energy	0,9	1,0	0,8	0,9
Services	1,1	1,2	1,0	1,1
Non-Energy Industrial Goods	0,5	0,7	0,3	0,7
Processed Food	0,7	0,8	0,9	0,7

Source: Eurostat and BBVA Research

Figure 2

Eurozone. Annual HICP inflation rate. Contribution by component



Source: Eurostat and BBVA Research

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