



World Economic Situation and Prospects

Weekly Highlight

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Inflation in the euro area

Headline inflation in the euro area reached a post recession peak close to 3 per cent in the latter part of 2011, but has been on a downward trend ever since, registering 1.1 per cent year over year in September 2013. Core inflation (abstracting from energy, food, alcohol and tobacco) has remained far lower, hovering around 1.5 per cent throughout 2012, but decelerating nearly continuously in 2013, reaching 1.0 per cent in September.

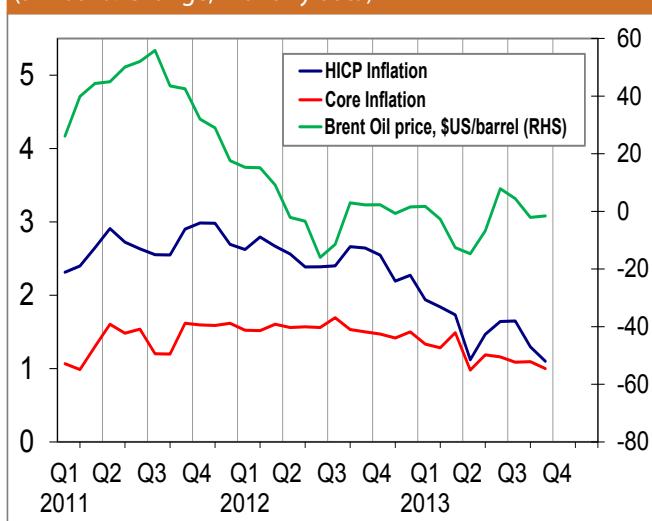
The movements of energy prices explain much of this pattern of divergence, as they generated a significant wedge between headline and core inflation in 2011-2012, but the two have narrowed since (see figure 1). The size of this wedge does not follow exactly the current movements in oil prices, because the growth rates are calculated as year over year, which can lead to so-called base effects. In the cur-

rent context, while oil prices have trended upwards since July, the year over year growth rates decreased, because oil prices were relatively high in the same period one year ago. The inflation contribution from food prices can have a similar impact. Other temporary factors, such as increases in indirect taxes and administered prices have had impacts at the country levels, explaining some of the variance in headline inflation rates across countries in the region. This explains why measures of core inflation are more useful in assessing underlying inflation trends.

In the euro area, despite the recent exiting from recession and generally positive short-term indicators and survey data, core inflation at 1 per cent and trending downwards, means that the region remains perilously close to deflation.

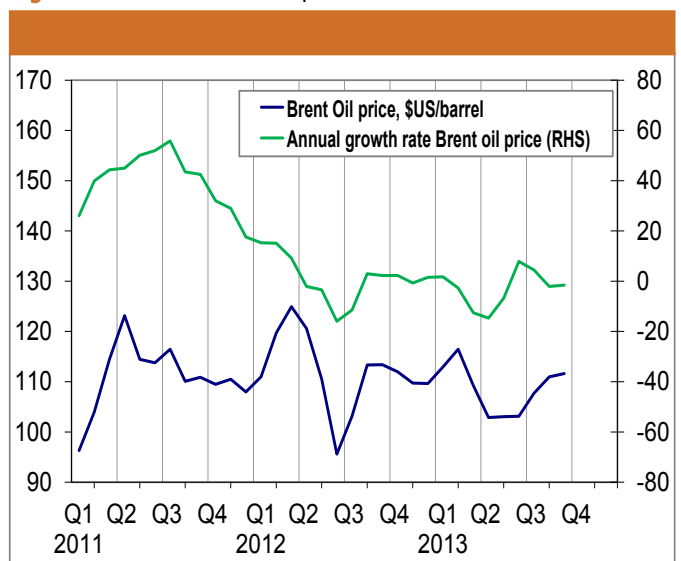
Figure 1: Inflation in the Euro Area

(annual % change, monthly data)



Source: OECD, Main Economic Indicators

Figure 2: Base effects from oil price movements



Source: OECD, Main Economic Indicators