Economics | Central Banks

German Inflation Plunges to 2% as ECB Prepares to Cut Rates

- Consumer-price growth eased from 2.6% in July; est. 2.2%
- Officials caution that inflation may quicken in months ahead

A customer hands over Euro banknotes for groceries at a market in Hamburg, Germany. *Photographer: Maria Feck/Bloomberg*

By Jana Randow
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German inflation slowed to the European Central Bank's target in August – supporting the case for another cut in interest rates next month.

The 2% reading – the lowest since 2021 – was down from 2.6% in July and less than all but one economist surveyed by Bloomberg had estimated. A report earlier Thursday showed that price pressures also eased significantly in Spain, reaching a one-year low.

The disinflation trend is expected to play out in the euro zone's other two biggest economies – France and Italy – when numbers are published Friday. There'll also be figures for the bloc itself, where analysts see a retreat to 2.2% and a nowcast from Bloomberg Economics predicts a return to the 2% target.

With price gains moderating in line with ECB projections, wage pressures easing and economic momentum faltering, officials in Frankfurt led by President Christine Lagarde have warmed to a September rate cut. That would be the second reduction after an initial step in June began unwinding the spate of hikes enacted to tame record inflation.

> **What Bloomberg Economics Says...**
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> "The sharper-than-expected drop in German headline inflation to the 2% target will likely add some support in favor of a rate cut by the ECB when it next meets on Sept. 12. Still, with core inflation in the monetary union's largest economy likely hovering above 3% and services inflation north of 4%, we expect the Governing Council to maintain a gradual, quarterly pace of cuts for now."
>
> –Maeva Cousin, economist. Click here for full REACT

Policymakers, though, have also cautioned that there may be setbacks in the months ahead, stressing that their fight isn't yet won. Underlying price growth remains strong, and increases in services costs in particular are still a big concern.

"Today's drop in German inflation is the result of lower energy prices and favorable base effects as well as lower prices for goods," Carsten Brzeski, ING's global head of macro, said in an emailed note. Even so, "it's too early to give the all-clear on inflation both in Germany and the entire euro zone."

The ECB hasn't yet secured the return to the 2% goal, Chief Economist Philip Lane warned last week, saying monetary policy must remain restrictive for now. He did, though, say on Thursday that wage gains – a key factor steering consumer prices – are set to slow sharply in the next two years.

While one more quarter-point cut in the deposit rate next month – to 3.5% – won't challenge that objective, the debate in the Governing Council about subsequent steps may soon become more heated.

Already now, some differences in opinion are starting to emerge. While Portugal's Mario Centeno – one of the ECB's most outspoken policy doves – considers next month's decision to cut borrowing costs is an "easy" one, Austria's Robert Holzmann – an arch hawk – reckons such a move isn't a "foregone conclusion."

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Officials could yet be swayed. Data due before their decision in two weeks include a broad gauge of wage pressures and updated economic projections that will reveal when inflation can be expected to hit 2%.

In Germany, Bloomberg Economics' nowcast points to a reading of that level again in September, taking the latest data into account. It predicted 1.9% for August.
– With assistance from Kristian Siedenburg and Joel Rinneby

(Updates with Lane comment in seventh paragraph.)