

Irish consumer prices (January)

Thursday, 11 February 2010

As expected, the annual rate of decline in the consumer price index continued to ease in January. Having peaked at -6.6% in October last year, the year-on-year rate of decrease dropped back to -5.7% in November and then -5.0% in December, and now the latest CPI figures, released this morning, show prices down 3.9% in the year in the opening month of 2010, a trend that is likely to continue as the year goes on. On a monthly basis, prices were 0.6% lower than in December, but the decrease was well down on the 1.7% drop posted in January 2009. Meanwhile, the HICP index was down 0.7% in the month, giving a year-on-year rate of change of -2.4% as against -2.6% in December.

The main factors contributing to the monthly CPI change in January were decreases in clothing and footwear and household durable goods due to the traditional Winter sales. However, there were increases in petrol and diesel prices as well as in the cost of medical insurance and dental and optical services.

Movements in oil prices and mortgage interest rates have been important contributory factors to the short-run volatility in inflation. Oil prices have been characterised by strong volatility in recent years, with the euro price of oil 32.8% lower in 2009 than the previous year. Energy costs and interest rates will again be key drivers of the movement in the consumer price index this year.

During 2009, a squeeze on disposable incomes, a large jump in the savings rate and a substantial decline in employment, led to a sharp contraction in nominal spending. Retailers, aided by lower prices for UK imports due to the sharp depreciation of sterling, responded by lowering prices to stimulate demand. Retailers sought to lower prices from producers and wholesalers, resulting in a further subsiding of supply chain inflationary pressures. The intensified competitive pressures were quite apparent in the food retail sector even when allowance is made for international food commodity trends. As consumers became more price conscious and inclined to alter their shopping habits, the more established retailers introduced more aggressive price reductions to stem market share losses to discount retailers. Further discounting is likely in the first half of this year.

Recent data show that price pressures for the Eurozone as a whole remain fairly subdued, with little indication that there will be an inflation problem any time soon. Quite simply, the huge level of spare capacity is likely to weigh on underlying Eurozone/Irish inflation in the short-term. And a sharp drop in wage growth in response to earlier increases in unemployment will exacerbate this effect. Admittedly, a significant fall in the euro might work in the opposite direction. But this would nowhere near offset the fundamental downward pressure on domestic prices.

The bottom line is that while overall prices are likely to be lower on average again in 2010 than in 2009, Ireland's rate of deflation is set to ease considerably this year. Following an average fall in prices of 4.5% in 2009, we are looking for a much more modest fall of less than 1.0% in 2010.

	All Items Index (Dec 2006=100)	% Change Month	% Change Year	HICP Index (2005=100)	% Change Month	% Change Year
2009 January	104.1	-1.7	-0.1	107.6	-0.8	1.1
2009 November	101.1	0	-5.7	106.2	-0.1	-2.8
2009 December	100.6	-0.5	-5.0	105.7	-0.5	-2.6
2010 January	100.0	-0.6	-3.9	105.0	-0.7	-2.4

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