Euro zone inflation hit new high amid near certain recession

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The escalation of the euro zone inflation rate to 9.1 percent in August, amid forecasts that it will soon hit double digits, makes it a near certainty that the European Central Bank (ECB) will impose a significant interest rate hike when it meets next week.

The inflation spike, which was marginally higher than anticipated, and the moves by the ECB to lift interest rates, take place in conditions where the European economy is heading for a recession, if not already in one.

It has been battered by rising energy and electricity prices, a product of the escalating NATO proxy war against Russia in Ukraine. But one of the significant features of the latest data is that inflationary pressures are spreading more broadly.

The so-called core inflation rate, which strips out volatile energy and food prices, rose to 4.3 percent, up from 4 percent in July.

Reporting on the European inflation, the *New York Times* noted that in Estonia it had reached 25 percent, with nine countries registering double-digit levels, including Lithuania and Latvia where it is over 20 percent. This is an indication that processes at work in the extremities of the euro zone economy could soon reach the heart.

Responding to the inflation data, German central bank president Joachim Nagel said inflation was "becoming an enormous burden for more and more people." But this "concern" for the mass of the population was wheeled out to provide the rationale for a tightening of monetary policy which will only accelerate the recessionary trends while doing nothing to bring down prices.

"We need a strong interest rate hike in September. And further interest rate hikes can be expected in coming months," he said.

In a speech in Berlin on Tuesday, he ruled out any relaxation of the interest rate hikes because of their impact on the economy declaring: "We should not delay further hikes for fear of a possible recession."

The aim of this tightening, in line with the class war agenda agreed to by central bankers at their Jackson Hole meeting last month, is to contract the economy in order to batter down workers' wage demands to compensate for the highest inflation in four decades.

Jack Allen-Reynolds, an economist at Capital Economics, told the *Financial Times* (FT) that inflation was set to hit a headline rate of 10 percent by the end of the year.

"With ECB policy rates a long way below appropriate levels [they are close to zero], it is clear that the bank will raise interest rates by a larger-than-normal increment next week. A 75 basis point hike looks increasingly likely," he said.

In an article on the European economy this week, headlined "Europe is heading for recession. The only question is how bad it will be," the *Economist* said "every single warning light is flashing red."

According to the article, amid all the confusion about the effects of the COVID-19 pandemic, the impact of the drought across much of the continent and the future of gas supplies there was broad agreement on one thing: recession is coming.

It would be led by Germany, Italy, and central and eastern Europe. According to analysts at JP Morgan Chase, there will be a 2 percent contraction for the overall euro zone in the fourth quarter. Growth rates for France and Germany will be -2.5 percent, Italy -3 percent. It said Italian industry appeared to be in "free fall."

Italy could also spark a financial crisis as a result of ECB monetary tightening because of the high levels of government debt. ECB officials are fearful that if the yield on Italian government bonds rises too sharply in relation to German debt this could lead to a crisis of the euro zone currency system as took place in 2012.

At its last meeting in July, the ECB put in place a mechanism to try and prevent this; but despite assurances by the central bank's president Christine Lagarde, there is no guarantee it will work.

If Italian industry is in "free fall," the situation in Germany is no better.

Earlier this week it was reported that some German companies are halting production because of rising gas and energy costs. Economy minister Robert Halbeck said industry had worked to cut gas consumption and switch to alternatives.

But some companies had stopped production altogether, a situation he described as "alarming."

"It's not good news, because it can mean that the industries in question aren't just being restructured but are experiencing a rupture—a structural rupture, one that is happening under enormous pressure," he said.

The crisis is hitting middle-sized industrial companies, the so-called Mittelstand, which form a crucial component of the German economy.

According to a poll published on Wednesday by DMB, a lobby group for the Mittelstand, reported by the FT, 73 percent of companies were experiencing "severe strain" with 10 percent saying that in the next six months their "existence is under threat."

Commenting on the results, DMB head Mark Tenbieg said: "Trust in the economic competence of the government is disappearing and small- and medium-sized enterprises feel they have been left alone by the authorities."

The recessionary trends are not confined to Europe. The US economy has contracted for each of the past two quarters and there are moves by major companies, including Ford, to cut their labour force.

One indicator of the state of the global economy is the fall in oil prices. They have been in steady decline over the past three months, falling by 8 percent in the first two days of this week. The price of Brent crude, the main international benchmark, dropped by 12 percent in August.

Evercore ISIO analyst Stephen Richardson told the *Wall Street Journal*: "The oil market is going from recession fears to recession acceptance."

Edward Moya, senior market analyst at the trading firm Oanda told the *Journal*: "Energy traders anticipate a brutal period for global growth.

"China factory activity remains depressed and another eurozone record-high inflation reading has raised the prospects of much more aggressive European Central Bank tightening that could trigger a severe recession."