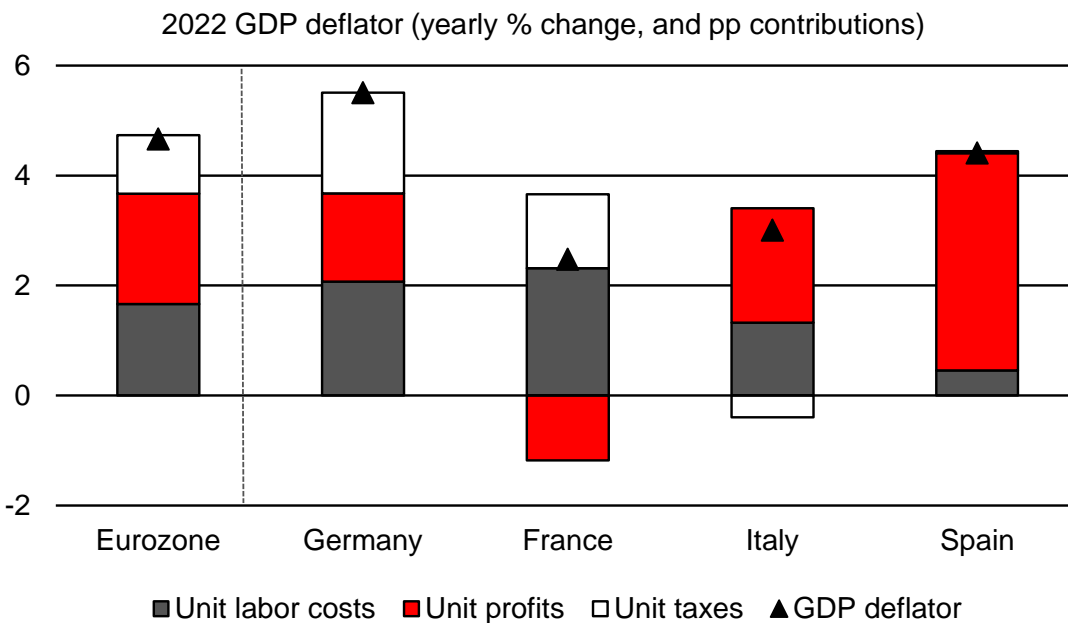


## Eurozone: profit margins have been at least as important as wages in driving inflation



Source: Eurostat, UniCredit Research.

Note: Data on France refers to the average over the 1Q22-3Q22 period.

- Our *Chart of the Week* illustrates how the growth of the GDP deflator – which measures the “price” of gross domestic product per unit of output and is a gauge of domestic price pressure – accelerated last year at the eurozone level and across the largest economies of the bloc. We break down the deflator into its main determinants – namely labor costs; firms’ profitability, as measured by the gross operating surplus (the national-account equivalent of EBITDA); and taxes on production and imports, less subsidies – all divided by real GDP. In the eurozone, the contribution of unit profits (a proxy for profit margins) to the growth rate of the GDP deflator slightly exceeded that of unit labor costs and was higher than its average over the last two decades. Quarterly data indicate that its contribution significantly increased in the second half of last year.
- Our chart also shows that the contribution of unit profits to the growth of the GDP deflator varied significantly from country to country, with Spain and France representing extreme situations in this regard. In Spain, unit profits accounted for almost all the growth of the GDP deflator as solid labor productivity growth largely offset upward pressure from labor costs. In contrast, France experienced a contraction in unit-profit growth, which dampened the increase in the growth rate of the GDP deflator, partly offsetting a strong pick-up in the growth of unit labor costs. The situation was more balanced in Germany and Italy. In Italy, the solid contribution of unit profits largely reflects a significant acceleration in their growth in 4Q22. Of course, our analysis is based on aggregate data, which disguises a lot of variation at the sector level.
- This evidence suggests that the ECB should broaden its inflation narrative from its recent focus on labor costs to include the drivers of corporate profitability, which has been surprisingly strong in the last couple of years despite a massive increase in the price of imported inputs. This would provide a more comprehensive picture of the current drivers of underlying price pressure in the eurozone, although this is unlikely to have any meaningful

implications for monetary policy (See our [Sunday Wrap](#), 5 March). Going forward, profit margins are likely to ease as demand growth slows, while unit labor cost growth may remain high for longer as wages rise to partly compensate workers for past and current high inflation.

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