

Czech Republic: Headline inflation accelerated further in January

January inflation accelerated due to a sharp increase in regulated prices. Core inflation slowed down but still remained high, reflecting the persistence of previous demand pressures



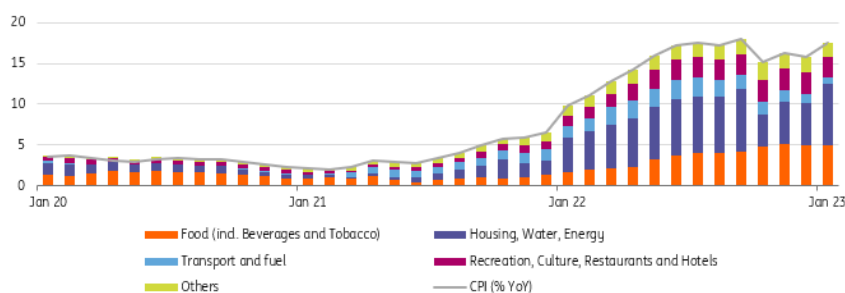
17.5% January inflation (YoY%)

Higher than expected

Increasing regulated prices push inflation higher

Czech headline inflation accelerated in January from 15.8% to 17.5% year-on-year in January (more or less in line with our estimate of 17.6%, above the market consensus at 17.1%). The main contribution to the acceleration of inflation came from administered prices, which increased by 30% month-on-month in January and added 4.6pp to the MoM increase of CPI. As expected, the biggest shock came from a considerable price increase in 'housing, water, electricity, gas and other fuels' (electricity prices for households jumped by 139.8% MoM). Core inflation added 0.8pp.

Contributions to year-on-year inflation (pp)

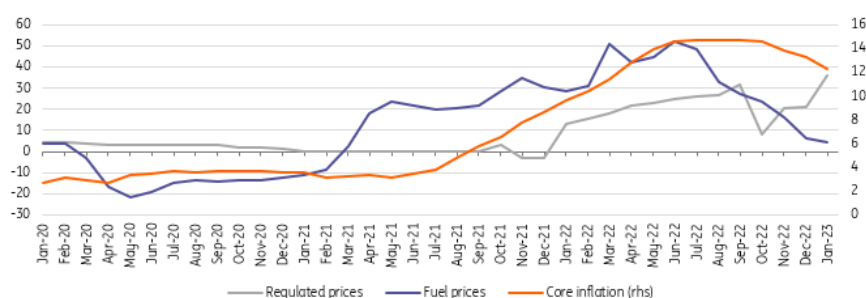


Source: Czech Statistical Office

Core inflation slowed down but still strong

The acceleration of headline inflation mainly due to the hefty increase in regulated prices is surely impressive. For the Czech Central Bank, however, what is more important is the development of core inflation. Although core inflation slowed down in February by 1pp to 12.3% YoY, this still-strong growth shows the persistence of previous demand pressures on inflation in the Czech economy, despite the moderation of real consumer spending in the second half of 2022. The CNB board can be satisfied that owner-occupied housing is slowing, as a consequence of the previous hefty tightening of monetary policy.

Regulated prices, core inflation, fuel prices (%YoY)



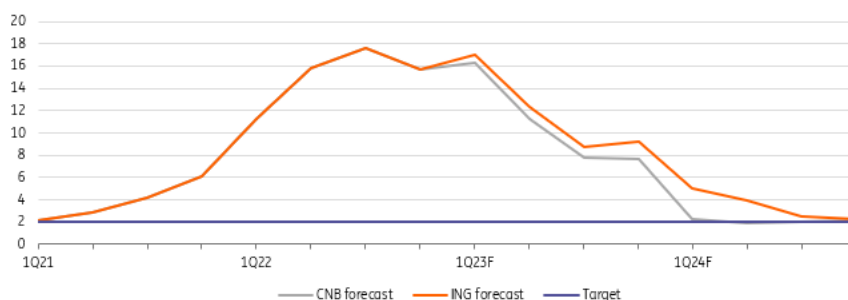
Source: CNB

Inflation likely to moderate to single digits in 2H23

At 17.5% YoY, we suppose this could be the likely peak of headline inflation this year. However, there is still a risk that some re-pricing was done later in January. Therefore, it may not be fully reflected in the January CPI report but could contribute to a still-hefty headline inflation figure in February, above 17% YoY. The risk for stubbornly high inflation in coming months stems from the uncertainty regarding the near-term development of fuel prices. The first February surveys signal that fuel prices could be edging up again.

We expect headline inflation will likely start to moderate in the second quarter, towards 9.2% YoY by the end-2023. The CNB forecast is more optimistic, at 7.6% YoY by end-2023, then falling swiftly close to the inflation target during the first quarter of next year.

CPI forecast (%YoY)



Source: CNB, ING

CNB board unlikely to hurry with rate cuts this year

In our view, the CNB board will be unlikely to hurry with rate cuts this year. The winter CNB forecast suggests a reduction in interest rates as of the second quarter. However, it seems more likely that the bank board would prefer to keep interest rates at current levels of 7% for a longer period until inflation falls below nominal rates. Therefore, only 'cosmetic' reductions of interest rates or a wait-and-see approach seem more likely. We see the first possible debate about rate cutting in August when a symbolic 25bp could be delivered.