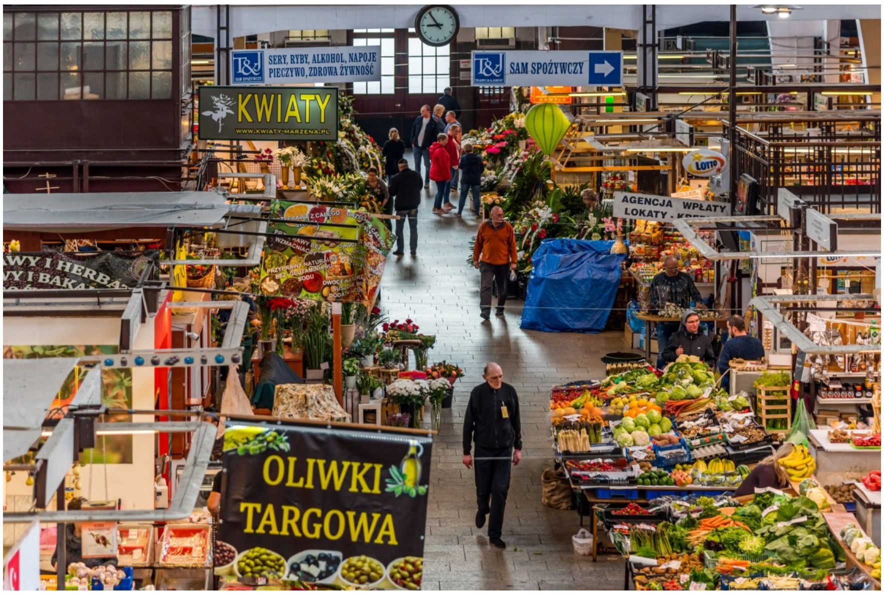
The end of 2022 saw inflation fall in Poland, but the peak is still ahead

December CPI inflation was confirmed at 16.6% YoY. It moderated on the monthly decline in energy prices. The core inflation is trending upwards and the peak in headline CPI inflation is still ahead. In 2023, we expect disinflation alongside global trends, but elevated core inflation will leave no room for the National Bank of Poland's rate cuts this year



December flash CPI confirmed

The preliminary estimate of December inflation was confirmed at 16.6% year-on-year, up from 17.5% YoY in November, although monthly growth was slightly revised down to 0.1% from 0.2% month-on-month. Growth of goods prices eased to 17.6% YoY from 18.8% a month earlier, while services price inflation rose to 13.4% YoY from 13.2%. Cheaper fuel prices than in November were accompanied by a strong reduction in heating prices (-10.8% YoY). This mainly stemmed from a sharp decline in coal for heating purposes, which was linked, among other things, to the intervention purchase of coal on foreign markets and its distribution at subsidised prices. Food prices continue to rise robustly. In December last year, foodstuffs were on average 22.1% more expensive than a year earlier. The monthly growth of clothing and footwear is also noteworthy as it went against the typical seasonal pattern. Despite the marked decline in the headline inflation rate, core inflation continues on an upward trend, rising to 11.6% YoY (our estimate) from 11.4% YoY in November. The increase in month-on-month core inflation in December slowed slightly, but is still very high by historical standards.

The peak of inflation is still ahead of us, possibly February 2023. While the jump in petrol prices at the beginning of the year, when VAT on fuel rose from 8% to 23%, was avoided, thanks to the pricing policy of a major player in the fuel market, we are still facing increases in energy prices for households in January linked to higher indirect tax rates. More importantly, the beginning of the year is also traditionally the time for companies to update their price lists, so some of the inflationary pressures observed in previous months will be reflected in price rises in early 2023. Signals from the economy show that in some sectors, the barrier of weak demand is insufficient to prevent large price increases. Enterprises still need to adjust prices to higher costs, eg wholesale electricity and gas prices grew at triple-digit levels. Examples from recent weeks include increases in train fares. In our view, the peak CPI will be around 20% YoY.

Disinflation expected in 2023, but core inflation will remain elevated

This year will be marked by disinflation, from around 20% YoY to around 10% in December. But in our opinion, there will be no conditions for interest rate cuts this year due to stubbornly high core inflation. Companies continue to face the consequences of the energy crisis (including increased distribution rates for electricity and gas, as well as more expensive energy in new contracts for wholesale users), forcing them to pass on higher costs to the prices of their products. At the same time, high wage pressures persist in sectors benefiting from high energy prices (mining, energy). Indexation processes (high indexation of pensions, 20% rise in minimum wage, and price indexation in intercompany contracts) will limit the rate of inflation decline.

In our assessment, the attention of the central banks in the coming quarters should focus on core inflation, so as not to succumb to the illusion of falling price pressures associated with a reversal of the trend in energy markets. Core prices (other than food and energy) will be a better gauge of underlying price developments in the economy.

We maintain our view that the problem is the persistence of core inflation. Poland, with its election cycle and the overhang of high energy prices, is exposed to the risk of slow disinflation and the persistence of elevated inflation when the economy rebounds. There will be no conditions for interest rate cuts in Poland this year. However, the decline in headline CPI should dominate global markets. But the bond markets are behaving (pricing in rate cuts just after the last rate hike) as if they are ignoring the fact that the pandemic and war have permanently altered (raised) inflation and neutral rates globally.

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