

Is the first CNB rate hike closer than we think?

Friday's inflation data poses an upside risk but the market remains unfazed. The CNB could easily find itself in a situation where inflation stays above 3% for a longer period, and neither the central bank nor the markets are prepared for it. The discussion could quickly change from whether we will see another CNB rate cut to when we will see the first rate hike

Czech National Bank building in Prague



Are markets underestimating the upside inflation risk?

On Friday, the Czech Republic's inflation for June will be released, which is a key number for the Czech National Bank and for the markets. Looking at the surveys reminds me of the situation before the May number, when I posted a similar comment. The consensus expects a year-on-year rise from 2.4% to 2.9%, which aligns with [our economists'](#) forecast. However, the most common estimate is actually 2.8%, with a few lower projections and 3.0% marking the upper bound.

Looking at the numbers in detail, it seems to me that 2.9% seems more like the minimum we could see, and the risk is clearly to the upside here, [just like in May](#). June 2024 was an exceptional month when disinflation peaked, creating this base effect for the YoY number. I suspect last year's

month-on-month figure may be sending misleadingly soft signals. Historically, June MoM readings have been notably higher than the 0.2% currently reflected in the surveys for this June.

More recently, both fuel and food surveys point to upward pressure. Moreover, fuel may actually lead some estimates to understate inflation, since the sharpest price acceleration in fuel prices took place in the last week of June, potentially missing the cutoff for some forecasts. On top of that, there is a pattern of acceleration in imputed rents. The only downside I see is the announced cut in household energy prices by CEZ, the biggest provider in the country. However, the impact of such cuts has recently tended to be less pronounced than estimates have suggested.

CNB ready for higher inflation in June but not for a longer period

Overall, it seems to me that the range is more like 2.9-3.2% for June inflation. And based on the CNB's communications, I think there is an internal expectation for higher inflation as well. The general assumption is that June should be this year's peak, which is our economists' forecast for now as well. However, the risks are building in our view. We have mentioned multiple times in our reports the increasing weight of imputed rents and food prices, where the fundamentals are clearly pointing up. Most recently, David Havrlant, our Czech economist, showed in the last CNB preview that [core inflation may easily head into the 3-4% range](#) in the coming months due to imputed rents and the housing market.

The June number may be a bigger shock for the markets than for the central bank. Medium-term though, I believe the CNB is not prepared for inflation, including the core rate, to remain above 3% for an extended period. If the upside risks materialise, we're likely to see a full hawkish pivot at the August meeting, once the July data is in and the forecast points to persistently higher inflation.

The market will face more hawkishness

However, markets will have more food for thought, with the CNB minutes from the June meeting also due to be released on Friday. Governor Ales Michl confirmed during the last press conference that the hawkish change in the statement's language was intentional, which I think will also be visible in the minutes. So we'll likely hear discussions around ending the cutting cycle, with some board members supporting the view that 3.50% is already the neutral rate. Given the strengthening economy, they may see no need for further cuts, fuelling hawkish sentiment regardless of the June inflation print.

Although the market saw some hawkish repricing in June, I still believe the curve is pricing in about 15-18bp of cuts. It's not yet pricing in the possibility of a complete stop to CNB rate cuts, or the prospect of a hike being the next move. Therefore, I believe there is more room for repricing, and I am not a fan of many trade ideas from others to receive rates here, although the levels are attractive. On the contrary, it is only a matter of time before the market realises that this time is different, and the CNB will have to demonstrate its hawkish resolve.

This is why the Czech koruna has been our favourite currency for some time now, and we believe there is room for another rally. In the [CNB preview](#) three weeks ago, I mentioned 24.500 EUR/CZK as the first stop, which is probably the story for the summer, with further gains later on. The rates market is more complicated since the market needs to see a real turnaround in CNB

communication to start thinking about rate hikes in the future. Friday's inflation data may be the first real test, but markets will likely need more time before reassessing their CNB outlook. That said, I still favour the payer side of the curve.

Author

Frantisek Taborsky

EMEA FX & FI Strategist

frantisek.taborsky@ing.com

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies)*. The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit www.ing.com.