

Czech inflation at 2% target again in December

Inflation stagnated in December at 2% as slightly higher food prices were offset by weaker fuel prices amid a recent decline in oil prices. For the whole of 2018, average inflation reached 2.1%



Source: Shutterstock

Fuel prices declined while food prices increased in December

A 1.2% acceleration in December food prices was offset by a 3.6% fall in fuel prices, as oil prices declined in the past three months. The slowdown in prices also came from alcoholic beverages, while price increases continued in housing (due to higher rents), heating, hot water and electricity (see the table). For the whole year, average inflation reached 2.1%, which is the highest figure in a decade.

Structure of inflation in the Czech economy

	YoY (%)	Cont (ppt)	MoM (%)	Cont (ppt)	YoY(t-1) (%)	Cont (ppt)
Total	2	2.0	0.1	0.1	2.0	2.0
Food and non-alcoholic beverages	-0.6	-0.1	1.2	0.2	-1.2	-0.2
Alcoholic beverages, tobacco	2.8	0.3	-0.6	-0.1	3.2	0.3
Clothing and footwear	-1.5	-0.1	-1.2	0.0	-1.4	-0.1
Housing, water, energy, fuel	4	1.0	0.2	0.1	3.9	1.0
Furnishings, households equip.	1.8	0.1	0.1	0.0	1.6	0.1
Health	3.4	0.1	-0.2	0.0	3.4	0.1
Transport	1.6	0.2	-1	-0.1	2.9	0.3
Post and telecommunication	-0.8	0.0	-0.3	0.0	-0.8	0.0
Recreation and culture	0.8	0.1	0.2	0.0	0.4	0.0
Education	2.3	0.0	0.1	0.0	2.2	0.0
Restaurants and hotels	3.8	0.2	0.3	0.0	3.8	0.2
Miscellaneous goods and services	4.1	0.3	-0.2	0.0	4.0	0.3

Source: CZSO, ING Bank

Inflation should increase in months ahead

Inflationary pressures will continue to grow further this year due to a tight labour market and solid wage growth. It should be accompanied by a rise in energy prices, especially electricity and gas for households, and food prices as a result of the poor harvest last year. The combination of these factors should lead to a gradual acceleration of inflation to 2.5% at the turn of the first and second quarters, followed by a gradual return to 2%. For the whole year, average inflation might reach the same level as in 2018. Without the recent fall in oil prices, inflation prospects for this year would be significantly higher, around 2.6%.

2.1%

Average inflation in 2018

the highest figure in last decade

February hike is likely despite CPI on target

From the point of view of the Czech National Bank, however, it is essential that this year's core inflation (now around 2.5%) continues to accelerate as this measure is more important for the setting of monetary policy. Note that services prices accelerated further in December to 3.4% from 3.3% in November. Due to the prospects for core inflation growth, we still see a further increase in rates at the CNB's February monetary policy meeting as very likely, although the CNB's new forecast will revise Czech GDP growth and inflation slightly downwards.

The CNB is still hike prone central bank

Still, further tightening of monetary policy this year will depend not only on inflation or the development of the koruna exchange rate but also on the global environment. However, members of the CNB Board are generally supporters of interest rate normalisation, and if foreign developments make it even slightly possible, they will continue to raise rates this year. As such, the chances of at least two hikes are still high in our view, despite the market's growing pessimism.

