

Czech inflation up slightly, to 2.7% YoY in February

Inflation accelerated further, from 2.5% YoY in January to 2.7% in February. This was mainly due to food prices. Inflation should continue to grow over the next two months, but then should slow. For the whole year, we expect a level of 2.5% on average. The next CNB hike seems likely in May.



Source: Shutterstock

Food prices the main factor behind CPI growth in February

February CPI increased by 2.7% YoY and by 0.2% MoM. The main factor behind the acceleration was food prices, which increased by 0.7% MoM. Due to a base effect, their YoY dynamics accelerated from -0.2% YoY in January to 1.3% YoY in February. Food prices alone saw YoY CPI growth 0.3ppt higher than in January. On the other hand, fuel prices fell by 1.5% in February, but should start to grow again in March.

2.7% YoY

February CPI growth

Above the central bank estimate of 2.4%

Higher than expected

Housing costs are growing, but will slowdown

The surprising increase to 2.5% in January inflation was concentrated mainly in housing prices, with notable rises in electricity, gas, rent and heat prices. Housing items have grown only moderately in February. Still, the housing category is the most important factor behind the annual CPI growth this year, contributing 1.4ppt in February. This growth is also driven by imputed rent, which is part of the CPI computed by the Czech Statistical Office, but not in the Eurostat's Harmonized Index of Consumer Prices (HICP).

However, imputed rent will gradually slow as we expect housing prices do decelerate significantly this year due to the CNB's macroprudential measures. CPI excluding imputed rent was just 2.3 % YoY in February.

Structure of inflation in the Czech economy

| | February 2019 | | | | January 2019 | | Change in YoY Cont (ppt) |
|----------------------------------|---------------|------------|---------|------------|---------------|-------------|--------------------------|
| | YoY (%) | Cont (ppt) | MoM (%) | Cont (ppt) | YoY(t-1) (%) | Cont. (ppt) | |
| Total | 2.7 | 2.7 | 0.2 | 0.2 | 2.5 | 2.5 | 0.2 |
| Food and non-alcoholic beverages | 1.3 | 0.2 | 0.7 | 0.1 | -0.2 | 0.0 | 0.3 |
| Alcoholic beverages, tobacco | 3.2 | 0.3 | -1.2 | -0.1 | 3.2 | 0.3 | 0.0 |
| Clothing and footwear | -1.2 | 0.0 | -1.3 | -0.1 | -0.7 | 0.0 | 0.0 |
| Housing, water, energy, fuel | 5.4 | 1.4 | 0.4 | 0.1 | 4.9 | 1.3 | 0.1 |
| Furnishings, households equip. | 1.4 | 0.1 | 0.7 | 0.0 | 1.1 | 0.1 | 0.0 |
| Health | 3.5 | 0.1 | 0.2 | 0.0 | 3.6 | 0.1 | 0.0 |
| Transport | 0.1 | 0.0 | -0.3 | 0.0 | 0.8 | 0.1 | -0.1 |
| Post and telecommunication | -1.3 | 0.0 | -0.2 | 0.0 | -1.0 | 0.0 | 0.0 |
| Recreation and culture | 2.2 | 0.2 | 1.6 | 0.1 | 1.9 | 0.2 | 0.0 |
| Education | 2.2 | 0.0 | 0.1 | 0.0 | 2.2 | 0.0 | 0.0 |
| Restaurants and hotels | 3.8 | 0.2 | 0.3 | 0.0 | 3.8 | 0.2 | 0.0 |
| Miscellaneous goods and services | 4.2 | 0.3 | 0.2 | 0.0 | 4.7 | 0.3 | 0.0 |

Items contributing to CPI slowdown

Items contribution to CPI acceleration

Source: Czech Statistical Office, ING

Gradual slowdown expected after a few months

While inflation will accelerate further over the next two months (though it should remain within the CNB tolerance band), from May it should start to slow to close to 2%. Therefore we do not think the CNB will be under pressure to deliver any imminent hike in March, with current inflation a "lost battle". More relevant for the central bank is inflation over the monetary policy horizon. Based on our estimate, this is just above 2%.

Two hikes this year, the first most likely in May

All in all, we still expect the CNB to deliver two hikes this year. The Czech economy is in relatively good shape although the global outlook continues to deteriorate. But despite inflation (at 2.7%

YoY) being above CNB expectations (2.4%), we prefer the May meeting for the first hike, as there will be a new forecast available. There is only one month between the end-of-March meeting and the beginning-of-May meeting, which should motivate the CNB board to keep to a “wait-and-see” approach at the end of March.