

Czech inflation beats forecasts with a 2.2% rise

CPI accelerated to 2.2% in May after 1.9% in April. While this was mainly due to the effect of higher food and fuel prices, prices of services also accelerated by 2.8%. Inflationary pressures tied to strong wage growth and a weaker Czech koruna favour a rate hike at the end of June



Source: Shutterstock

Fuel prices pushed up prices in May

May's inflation accelerated to 2.2% from 1.9% in April, beating both the market estimate (2.0%) and the central bank forecast (1.9%). In month-on-month terms, prices rose by 0.5%. Higher prices compared to April were mainly due to higher fuel costs, which increased by 4.2% MoM and reached the highest level since mid-2015, while food prices picked up by 1% after falling in the past three months.

2.2% YoY May inflation

back above the 2% target after three months

Higher than expected

Food prices main driver of weaker CPI in 1Q18

Weaker inflation in previous months was caused by the combined effect of a stronger koruna, weaker decline in food prices and a high base. Prices began to accelerate strongly at the turn of 2016/2017 as food and restaurant prices increased following the introduction of the online sales registration. Indeed, food prices were growing by 6.4% YoY in 4Q17 and decelerated to 2.6% YoY in 2018 on average. This means that the contribution of food to YoY CPI growth declined by 0.7ppt this year compared with 4Q17.

Prices of services are accelerating

For monetary policy, prices of services are more important, however, as they better reflect the economic situation and demand-driven inflationary pressures. These increased by 2.8% YoY in May, and accelerated further compared with April. As such, YoY prices of services reached the highest level since the end of last year. Core inflation, by the Czech National Bank's definition increased from 1.8% to 1.9% in May while simple core inflation remained at 2% YoY.

Structure of the inflation in the Czech Republic

	YoY (%)	Cont (ppt)	MoM (%)	Cont (ppt)	YoY (t-1) (%)	Cont (ppt)
Total	2.2	2.2	0.5	0.5	1.9	1.9
Food and non-alcoholic beverages	2.4	0.4	1	0.2	1.8	0.3
Alcoholic beverages, tobacco	3.6	0.3	0.4	0.0	3.8	0.4
Clothing and footwear	-1.4	-0.1	-0.5	0.0	-0.8	0.0
Housing, water, energy, fuel	2.5	0.6	0.3	0.1	2.5	0.6
Furnishings, households equip.	1.5	0.1	0.3	0.0	1.1	0.1
Health	3.9	0.1	0.7	0.0	3.8	0.1
Transport	2.9	0.3	1.2	0.1	1.5	0.2
Post and telecommunication	-2.2	-0.1	-0.2	0.0	-2.2	-0.1
Recreation and culture	0.5	0.0	-0.2	0.0	0.8	0.1
Education	1.5	0.0	0	0.0	1.5	0.0
Restaurants and hotels	3.6	0.2	0.5	0.0	3.5	0.2
Miscellaneous goods and services	2.5	0.2	0.3	0.0	1.9	0.1

Source: CZSO, ING Bank

Higher CPI increases likelihood of June hike

Taking into account current oil prices and the weak CZK, inflation should remain above 2% in the coming months. Still, inflationary pressures should strengthen thanks to favourable developments in the labour market and rising wages. If the koruna remains at current levels and oil prices do not start to decline significantly, inflation will most likely flirt with 3% in 1Q19. This is a reason why the CNB should not postpone further tightening of monetary policy. The koruna is now considerably weaker than expected by the CNB in its latest forecast (25.1 EUR/CZK in early June), which requires monetary tightening via rates. Therefore we believe a hike will come at the next monetary policy

meeting at the end of the June, and today's inflation data further increase the likelihood of this.

[Read about solid wage growth in Czech Republic](#)