

Czech National Bank Minutes: Inflationary risks emerge

The Czech National Bank board assessed the risks and uncertainties in the outlook as moderately inflationary. We consider another 50bp cut at the next meeting as the most likely option for now, but the pace of monetary easing is expected to slow down thereafter



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Inflation outlook assessed as moderately inflationary

At its last meeting, the CNB board lowered the policy rate by 50bp to 5.25% with all seven members voting in favour. The CNB Minutes provide more detail on the decision and the outlook. The bank board assessed the risks and uncertainties in the outlook as moderately inflationary, with the main concerns listed below.

- Slow unwinding of elevated inflation expectations.
- Strong wage demands in a tight labour market.
- Persistence in high price growth of services.
- The weaker exchange rate of the koruna.
- Acceleration of money creation resulting from a pickup in credit activity.

Meanwhile, a deterioration in global economic activity and a weaker performance of the German economy was mentioned as a downside risk to the inflation outlook.

Structure of inflation will be watched

The discussion focused on the structure of inflation, in particular the difference between the subdued price dynamics in goods and upbeat price growth in the service sector. Deputy Governor Eva Zamrazilova sees prices in the service sector as a clear upside risk to the inflation outlook. Board member Jan Kubicek agreed, asking whether this is due to reverberations from the previous inflationary episode or an independent inflationary hotspot, with price developments in services also representing an inflationary risk for him.

On the other hand, Tomas Holub sees this as part of extinguishing the inflationary fire. The price dynamics in services prices have to be monitored but do not constitute a reason for not continuing the monetary easing process. Jan Frait agreed with his standpoint, with both board members considering a 75bp cut. Karina Kubelkova sees the number and intensity of upside inflation risks as decreasing compared to the previous forecast.

Monetary easing to carry on

Another point of discussion was the real natural interest rate. Overall, the issue of the equilibrium rate is not a major issue right now and will become relevant when rates get closer to the equilibrium rate estimates. The evolution of foreign equilibrium rates is perceived as particularly important, especially the European Central Bank's approach.

Based on the Minutes, we consider another 50bp cut at the next meeting as the most likely scenario for now. However, the pace of monetary easing is expected to slow down thereafter with reviving household spending and continued nominal wage growth contributing to price pressures. Inflation data for April is out on Monday, with our expectations at 2.4% year-on-year and 0.2% month-on-month.

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