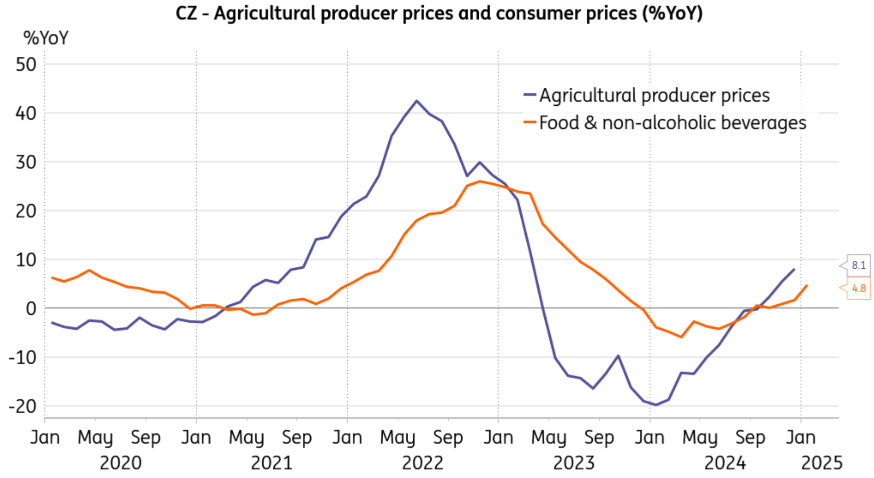
Food prices drive Czech inflation

The Czech Statistical Office confirmed the headline inflation rate at 2.8% in January. Price acceleration in the food segment was the main driver of consumer prices. Monetary easing is set to continue but will be done cautiously as the terminal rate approaches

Food and housing drive inflation

Czech consumer prices added 2.8% year-on-year in January, coming in 0.2ppt softer than at year-end. Consumer prices rose by 1.3% month-on-month, mainly driven by higher prices in the food, alcoholic beverages, and tobacco sections. This appears to have compensated for the Christmas discounts in the food segment that tempered inflation in December. Nevertheless, pro-inflationary pressures are accumulating in the food sector, with agricultural producer prices increasing by 8.1% at the year-end.

Potent pricing in agriculture will hit consumer prices



Source: CZSO, Macrobond

In annual terms, consumer inflation was strongly impacted by food and housing prices. Food prices rose by almost 5% YoY in January, while housing price dynamics slowed down to 1.3%. Prices of goods added 1.7% YoY, and services prices gained 4.7% from the preceding year. The imputed rent growth picked up to 2.9% YoY in January from 1.7% previously, mainly due to increasing prices of new properties. Our estimate of the annual core inflation rate is 2.6% though there is some downside risk associated with the impact of tax adjustments.

Rate cuts to continue until the terminal rate is reached

Stronger core inflation and accumulated cost pressures in the food segment will lead to a cautious approach to further policy rate reductions despite some relief from softer annual dynamics in the service sector. Still, the price growth of services would have to slow down to some 3.5%, by the CZSO definition, to be consistent with a 2% inflation target.

We expect the Czech National Bank board to carry on with rate cuts, although at meetings when new forecasts are issued, with the next cut in May and the final one in August, bringing the base rate to a 3.25% landing zone. We see the headline inflation picking up to 2.7% this year and crossing the 3% upper bound of the tolerance band around the 2% target in the middle and towards the end of the year. The whole-year average is thus above this year's CNB inflation outlook of 2.4%, mainly due to stronger food price dynamics, in our view. Both the ING and the CNB forecast see the core rate remaining stable at 2.5% for this year.

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