Poland: CPI falls from its peak but core inflation continues to rise

CPI inflation in Poland has passed its peak and fell to 16.1% year-on-year in March vs 18.4% in February. While the March reading was revised down, core inflation rose to around 12.3% YoY. The first phase of disinflation will be robust, but over time it will become increasingly difficult for inflation to moderate further

Food and drink was 24% more expensive in March than a year ago

Disinflation on the back of normalising energy prices

The Central Statistical Office of Poland revised the preliminary March inflation estimate to 16.1% year-on-year (flash at 16.2%). Annual inflation declined from 18.4% YoY in February. In March, inflation of goods prices declined to 17.1% YoY (from 20.2% in February), while services prices remained stable at 13.3% YoY. Services price growth has remained stable in recent months due to the upward pressure of other costs (including energy) and wages against downside pressure coming from weak demand.

The final data confirm that the decline of yearly CPI inflation in March was mainly linked to energy-related factors. The annual rate of increase in gasoline prices nosedived to 0.2% from 30.8% YoY in February amid a high reference base from March 2022, when prices at the pump soared following Russia's invasion of Ukraine. The annual inflation of house energy prices also decreased (26.0% YoY vs. 31.1% YoY respectively). At the same time, upward pressure on food prices persists. Food and non-alcoholic beverages were 24.0% more expensive in March than a year ago, and the annual rate of increase remained exactly the same as in February. Vegetables became more expensive by 7% month-on-month.

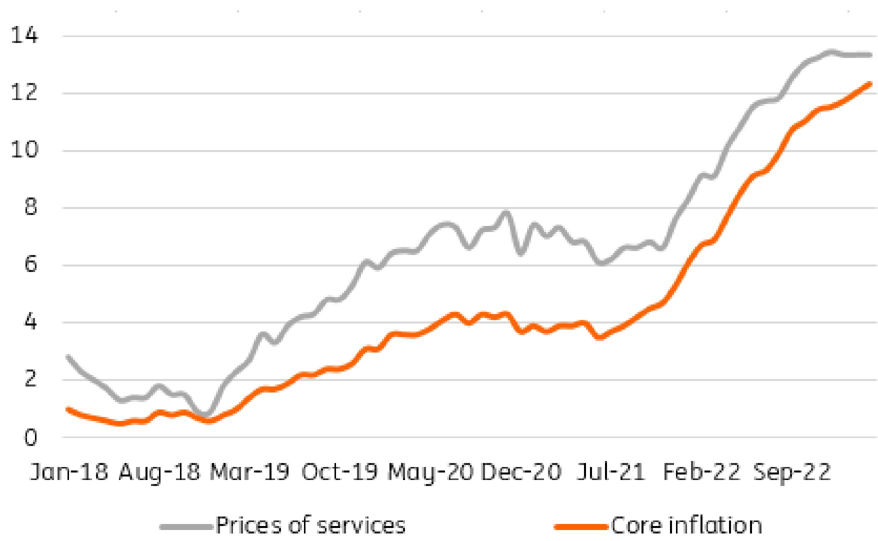
Persistent core inflation suggests targets will be missed

Our estimates show that core inflation excluding food and energy prices rose to 12.3% YoY in March, up from 12.0% YoY in February, which is in line with our earlier forecast. Strong increases in the prices of clothing and footwear (5.0%MoM) and home furnishings (1.4%MoM) are noteworthy.

The disinflation process has begun, but the further rise in core inflation suggests that it will not be a quick and easy process. In the first phase, it will be supported by a decline in the annual dynamics of fuel and energy prices, aided, among other things, by the high reference base. However, further price declines towards the National Bank of Poland (NBP) target of 2.5% YoY will become increasingly difficult. The process of passing higher costs on to retail prices continues, despite signs of a clear deterioration in consumer demand. Even two-quarters of consumption contraction was not enough to tame core CPI.

Core inflation increased further in March

Consumer prices, % YoY



Source: GUS.

No room for NBP rate cuts this year, but hikes are also unlikely

Amid the deepening economic downturn, the Monetary Policy Council (MPC) will not raise interest rates further, but today's inflation data clearly confirm that it is definitely premature to discuss interest rate cuts. Council members have gone quiet on the topic of possible rate cuts before the end of 2023, which is a positive change in the central bank's communication. Although the market is still betting on rate cuts at the end of 2023, our view is that they will remain unchanged until the end of the year, and we expect the first cuts in the third or fourth quarter of 2024.

Within the Central European region, Poland and Hungary are now the outliers with a persistent rise in core inflation, with core inflation in the Czech Republic already falling.

High inflation expectations can also be seen in the financial markets; today the yield curves are inverted (IRS or 10-year bond yields are lower than 2-year bond yields), which means that the financial markets expect economies to slow down and inflation to fall. However, in the case of Poland, the yield curve is inverted to the smallest extent (least negative slope), which we interpret as a lower belief in a sustained decline in inflation in Poland than is the case in the Czech Republic or even Hungary.

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