

Instant Reaction

EcoAlert

Inflation in the Czech Republic accelerated again



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Consumer price index (July 2021)

	Current	KB forecast	Consensus
Consumer prices			
Consumer prices (% mom)	1.0	0.6	0.5
Consumer prices (% yoy)	3.4	2.9	2.9

Source: Bloomberg, CZSO, Economic & Strategy Research, Komerční banka

The month-on-month rise in consumer prices was twice as fast as expected in July. The year-on-year inflation rate reached 3.4%, which is 0.4pp above the CNB forecast, and is heading for 4%. Above all, the prices of services are rising. Concerns about rising inflation expectations will lead the CNB to further raise interest rates. Uncertainty about price developments in the near term remains elevated.

Consumer prices in the Czech Republic increased 1.0% in July compared to June, beating all estimates. On average, analysts expected an increase of 0.5% mom, while our estimate was 0.6%. Year-on-year inflation increased to 3.4% from the previous 2.8%. An acceleration to 2.9% yoy was expected while the CNB forecast projected 3.0% yoy.

Month-on-month inflation was mainly driven by higher prices of packaged holidays, which is largely a seasonal phenomenon. But other services probably became more expensive, as well. The overall rise in services was 1.9% mom, while prices of goods rose 0.4% mom. Contrary to expectations, food prices also rose, while we estimated a slight decline here. Energy prices were also higher, and thus housing costs also rose. On the other hand, the further rise in fuel prices did not surprise. Here, prices increased another 3% in July.

Price changes in the consumer basket ...

	mom	yoy
Total	1.0%	3.4%
Food and non-alcoholic beverages	0.4%	0.8%
Alcoholic beverages, tobacco	-0.2%	6.1%
Clothing and footwear	-0.1%	6.0%
Housing, water, energy, fuel	0.9%	2.5%
Furnishings, household equipment	1.0%	2.9%
Health	0.2%	3.1%
Transport	1.3%	8.2%
Post and telecommunications	-0.2%	-0.7%
Recreation and culture	5.5%	2.0%
Education	0.0%	2.8%
Restaurants and hotels	1.1%	4.0%
Miscellaneous goods and services	0.3%	3.0%

Source: CZSO, Economic & Strategy Research, Komerční banka

... and their contribution to overall inflation

Contribution to inflation in p.p.	mom	yoy
Total	1.0%	3.4%
Food and non-alcoholic beverages	0.0	0.1
Alcoholic beverages, tobacco	0.0	0.6
Clothing and footwear	0.0	0.2
Housing, water, energy, fuel	0.2	0.6
Furnishings, household equipment	0.0	0.2
Health	0.0	0.1
Transport	0.2	0.9
Post and telecommunications	0.0	0.0
Recreation and culture	0.5	0.2
Education	0.0	0.0
Restaurants and hotels	0.1	0.3
Miscellaneous goods and services	0.0	0.2

Source: CZSO, Economic & Strategy Research, Komerční banka

Prices in transport remain the main driver of year-on-year inflation. Without them, the annual inflation rate would not be 3.4% but just 2.5%. Other main drivers of inflation are the

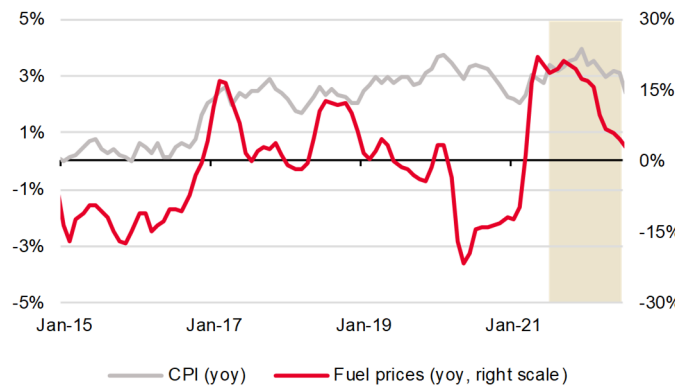
prices of cigarettes and alcohol, which contributed to the year-on-year rise in prices by 0.6pp, but gradually also housing costs, with rental prices rising 2.8% and electricity prices 7.6% yoy. We are also observing an increase in prices in the services sector, which is related to the adjustment after the pandemic. Year-on-year, prices of goods rose 2.9%, while prices of services rose 3.9%.

Importantly, core inflation, which does not include items not affected by monetary policy, is still not slowing down. On the contrary, according to our estimate, core inflation accelerated to 3.9% yoy in July from the previous 3.5%.

In our forecast, we assumed inflation would start to weaken from August, and even so, at the end of the year, its year-on-year rate would be 3.5%. However, the uncertainty of price developments after the pandemic is still considerable. In any case, the acceleration in inflation in July was above estimates, and if the following development of consumer prices were as we foresaw, inflation would reach 4% yoy at the end of this year. **However, if inflation does not slow down in the coming months, as we expect, it may be realistically close to 5% yoy at the end of 2021.**

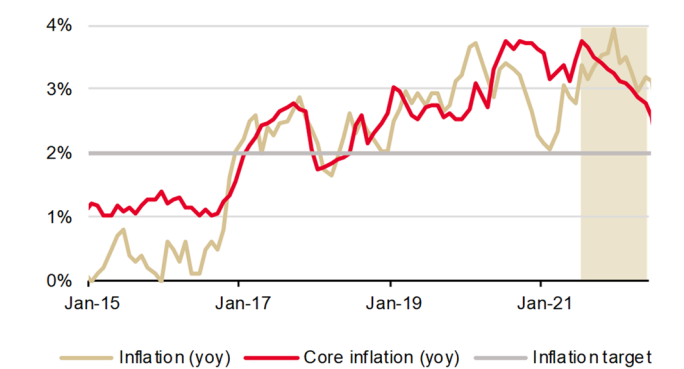
Although monetary policy can do nothing with the current rate of inflation, fears of rising inflation expectations are likely to increase the willingness to raise interest rates. The financial market is currently speculating about this. At the next meeting in September, we expect a further increase in the CNB's interest rates by 25 basis points, and again we can count on a discussion of an even faster increase. The real risk is thus an increase in the main repo rate at the following CNB meetings by 50 point steps.

Fuel prices keeps inflation higher



Source: CZSO, Economic & Strategy Research, Komerční banka

Core inflation has not slowed yet



Source: CZSO, Economic & Strategy Research, Komerční banka

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