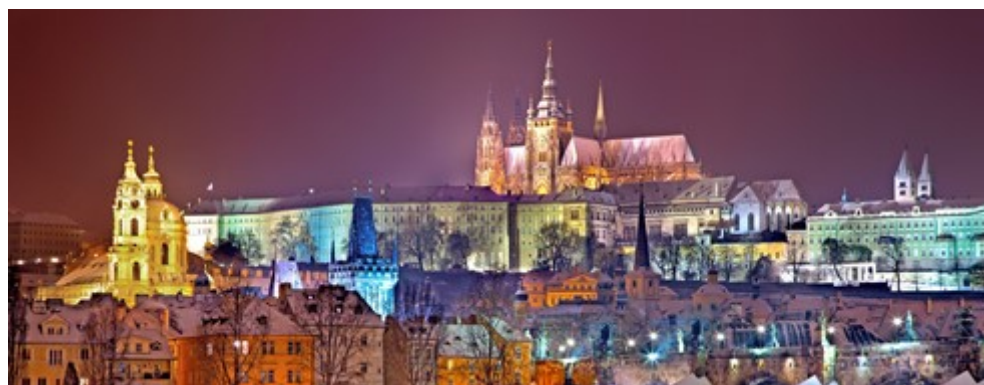


Czechia Watch: Inflation decline before another increase

In December, inflation decreased to 15.8% vs. expected 16.2% in line with latest downside surprises in many European economies. However, in January, a renewed increase of the inflation rate is likely due to traditional repricing coupled with reshuffling in fiscal measures.



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Main drivers of the December inflation print

In December, consumer **prices remained flat** compared to November. Prior to that, prices grew by 1.2% after declining by 1.4% in October. The perceived volatility in monthly CPI data in 4Q22 is driven primarily by fiscal measures designed to shield consumers from high energy prices. The subdued month-on-month development in December resulted in a **decline of the year-on-year inflation rate from 16.2% to 15.8%**, more than we expected (16.1%). Market consensus reached 16.2% with a relatively wide range stretching from 15.8% to 16.7%. **The full-year average year-on-year CPI figure reached 15.1% in 2022, broadly aligned with our forecast of 14.9%.**

Contributions to monthly and yearly inflation (in percentage points)

	mom	yoy
Food and non-alcoholic beverages	0.1	4.5
Alcoholic beverages, tobacco	-0.1	0.5
Clothing and footwear	0.0	0.7
Housing, water, energy and fuel	0.1	4.5
Furnishing, household equipment	0.0	0.7
Health	0.0	0.3
Transport	-0.3	1.0
Post and telecommunication	0.0	0.1
Recreation and culture	0.1	1.1
Education	0.0	0.1
Restaurants and hotels	0.1	1.5
Miscellaneous goods and services	0.0	0.8
Total	0.0	15.8

Source: CZSO

Despite the lower than expected headline number, we do not view the December inflation result as particularly surprising, with most of the **main CPI items not deviating much from expectations** either in terms of direction or magnitude. Prices in **transport** declined by 10.5% month-on-month thanks to cheaper prices at gas stations. **Food prices** were pro-inflationary but less so than suggested by preliminary weekly data, explaining most of the deviation in our forecast. **Energy prices** were more subdued with natural gas prices up by 2.0% compared to last month and electricity prices by 1.2%. In November,

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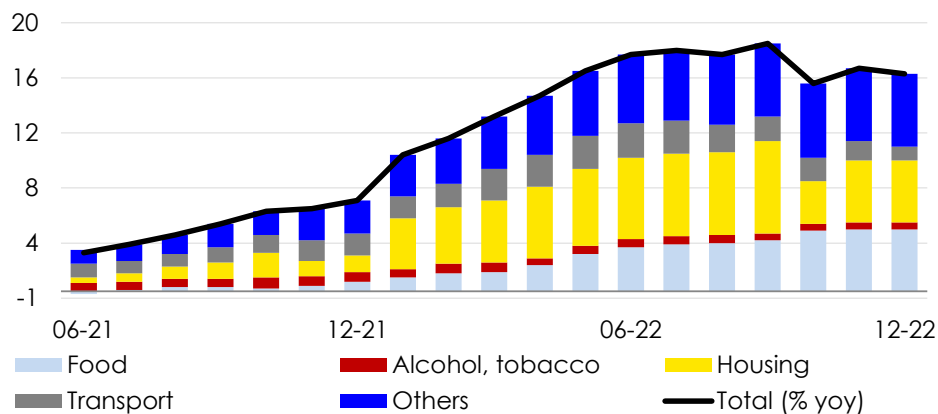
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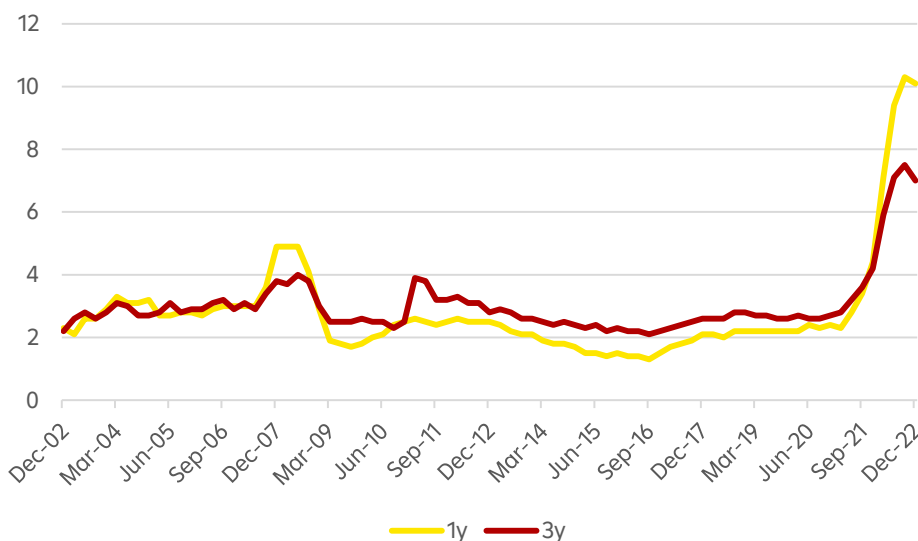
the move was larger at 14.1% for natural gas and 3.9% for electricity. Once again, the price statistics was significantly influenced by fiscal measures to reduce the impact of high energy prices. The Czech statistical office calculates **hypothetical inflation without the fiscal impact**: inflation would stand at 19.3% year-on-year versus the reported 15.8 %. Still, even the hypothetical number with much higher inflation would constitute a slowdown since in November it stood at 19.8%. Importantly, these hypothetical inflation figures include the effect of the previous waiver on VAT which, statistically, pushes inflation up.

Inflation structure broadly unchanged



pp contributions to yoy% headline inflation
Source: Macrobond, Raiffeisen Research

Inflation expectations eased slightly, but remain elevated



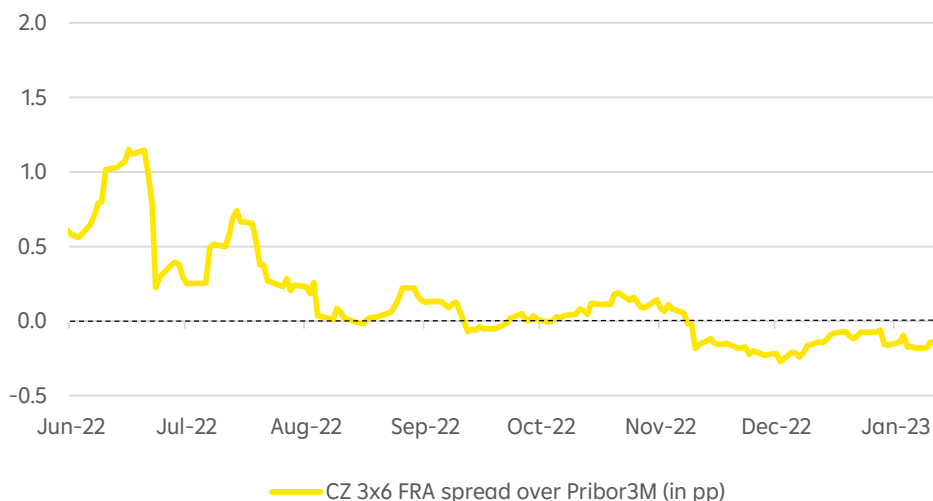
Inflation expectations among NFC, 1 and 3 years ahead
Source: CNB, Raiffeisen Research

Monetary policy implications

The December inflation figure is good news for CNB, precisely for its strategy of rate stability. Data show that demand-driven inflation is easing. The development of household spending and earnings within the sectoral accounts of the CZSO shows that consumers’ willingness to spend has decreased. Firms were so far successful in passing higher costs onto customers, documented by the increasing profit rate, but the room to continue doing so is getting narrower.

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No bets on rate hikes in coming months



Source: Bloomberg, Raiffeisen Research

Demand conditions suggest further inflation easing

Going forward we expect **continuing easing of underlying inflation** on the back of deteriorating purchasing power of households, but also lower external cost pressures depicted, for example, in the latest PMIs for the eurozone. That being said, we **expect inflation to decline be slowly and gradually** due to still elevated inflation expectations, low unemployment rate and second-round effects from previous supply shocks (notably energy). More so, January will likely bring a renewed increase of the year-on-year inflation rate due to traditional repricing of goods and services this time coupled with reshuffling in fiscal measures — the energy tariff being replaced by price caps. January inflation is crucial in setting the level of the year-on-year CPI for the remainder of the year. **For the whole year 2023, we expect average inflation close to 9% with risks skewed to the upside.**

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Symbol	Date	Recommendation	Company
CZ	30.12.2022	Under Revision	Czech Republic
CZ	07.06.2022	Under Revision	Czech Republic

History of long term recommendations			
Symbol	Date	Recommendation	Company
CZ	30.12.2022	Not rated	Czech Republic
CZ	07.06.2022	Not rated	Czech Republic

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and activities) and B (ancillary services) of Annex I of Directive 2014/65/EU of the European Parliament and of the Council (“special services”) have been provided in the past 12 months (column B).

	Column A	Column B
Investment recommendation	Basis: All recommendations for all financial instruments (last 12 months)	Basis: Recommendations for financial instruments of all issuers, for which special services were rendered in the last 12 months
Buy recommendations	62.2%	60.9%
Hold recommendations	22.8%	23.1%
Sell recommendations	15.0%	16.0%

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	Column A	Column B
Investment recommendation	Basis: All recommendations for all financial instruments (last 3 months)	Basis: Recommendations for financial instruments of all issuers, for which special services were rendered in the last 3 months
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