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# Economic Comment

## Service prices go up

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In February, CPI rose to 1.2% y/y, in line with expectations and despite a downward revision of January reading to 0.7% from 0.9%. According to our estimates, the change in inflation basket weights generated some upside pressure on inflation in early 2019 so the revision of the January figure was not caused by this factor. We estimate that core inflation rose less than we have expected so far – to c0.7-0.8% y/y in January and 1.0-1.1% y/y in February – with the striking acceleration of services' prices (2.3% y/y in February vs 1.8% y/y in January and 0.9% y/y in December). Today's data do not change our outlook for inflation – we expect core CPI to climb to 2.5% y/y and headline CPI to slightly above 2.0% y/y at the year end.

**In January**, inflation rose by 0.7% y/y vs 0.9% y/y from the preliminary reading. The downside revision was caused not by the changes in the CPI basket weights, but by revisions of prices inside the categories. In particular, there is no sign of the rise of clothing prices we expected upon seeing the retail sales data (with the deflator in the category rising a lot). The decrease of inflation vs December (1.1% y/y) was mainly the effect of falling electricity prices (-7.3% y/y) and fuel prices (-2.0% y/y), while core inflation most likely rose a bit, to 0.7-0.8% y/y from 0.6% in December.

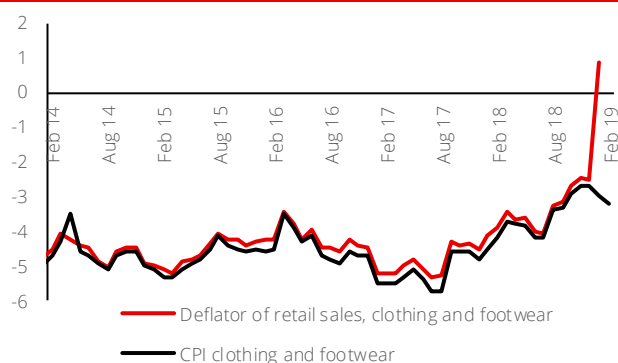
**In February**, inflation rose to 1.2% y/y due to a rise of prices by as much as 0.4% m/m, which means that this was the strongest February for CPI since 2012. The main factor pushing inflation up in February was food, going up by 0.9% m/m, with sugar, vegetables, fruits and flour as the strongest contributors. In our view, core inflation moved to c1.0-1.1% y/y.

Rise of core inflation in y/y terms is the result of a **rebound in services prices** that increased by 2.3% y/y in February vs 0.9% y/y in December 2018. It is worth to notice that the price rise was broad-based: apart from base effect in financial services that pushed this category up, telecommunications rose 2.8% since December, tourism added 2.9% since December, waste collection added 7.1% since December, transportation (1.7% y/y in February), hairdressing and cosmetics services added 1.6% since December, and transport prices rose by 1.7% y/y (here we operate on annual scale due to strong seasonality).

We expect services prices to fuel rise of the **core inflation** this year that could near **2.5% y/y in late 2019** while the headline **CPI might break 2% y/y**.

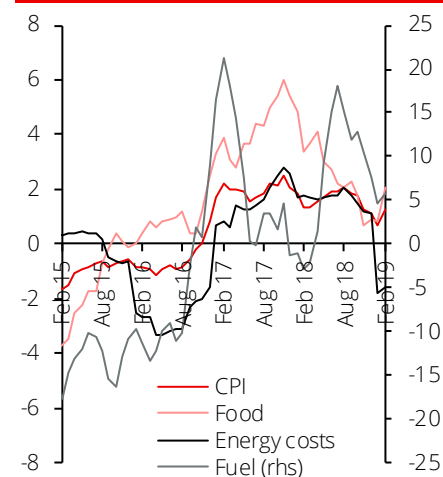
In **the new inflation basket**, we saw some noticeable changes after only marginal corrections introduced in 2015-2018. Higher weights were applied for transport (+1.6pp), food (+0.5pp) and hotels/restaurants (+0.5pp) while lower for housing (-1.2pp) and telecommunications (-0.7pp). According to our estimates, new weights generated slight upside pressure on CPI in early 2019 but later in the year should work towards lower CPI. However, the impact on the inflation path should not exceed 0.1pp in any month.

### CPI's clothing and footwear prices vs corresponding retail sales deflator, % y/y



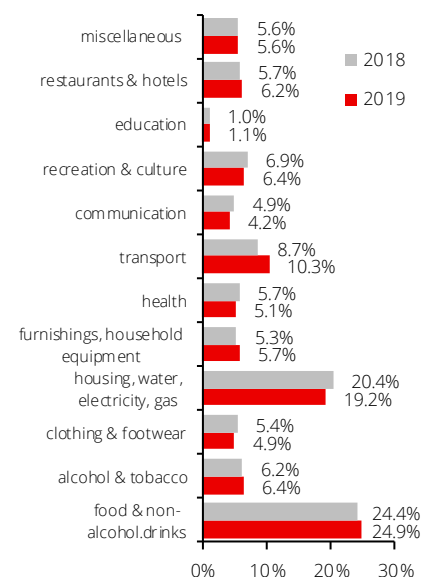
Source: GUS, Santander Bank Polska

### Inflation and main components, % y/y



Source: GUS, Santander Bank Polska

### Inflation basket



Source: GUS, Santander Bank Polska

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