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Economic Comment

Astonishing rise of inflation

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Flash CPI inflation reading for December showed a much higher-than-expected outcome: 3.4% y/y instead of 2.8% market consensus and our 3.0% forecast. We estimate that core inflation ex food and energy surged from 2.6% y/y to 3.2% - the highest in more than 17 years. After such high December, CPI is in fact certain to be well above 4% y/y in 1Q2020 and may remain substantially above 3% for the better part of the year. The monetary policy has just become much more interesting.

Flash CPI inflation reading for December showed a much higher-than-expected outcome: 3.4% y/y instead of 2.8% market consensus and our 3.0% forecast. Inflation is now the strongest in seven years. Based on the limited information given by GUS in the flash release we estimate that core inflation ex food and energy surged from 2.6% y/y to 3.2% - the highest in more than 17 years.

Food inflation also proved quite strong: 1.2% m/m instead of 0.7% we assumed based on price developments on the wholesale markets; the previous tie food prices rose so much in December was in 2016 and before that – in 1999. Our base scenario is a gradual decline of food price growth this year, but we see a growing risk this will not happen. It is getting more difficult to assume that in 2020 food supply would come back to normal and food prices calm down: weather is still unusual and poses a risk of crop losses also this year, there are further reports of ASF and new ones about avian flu.

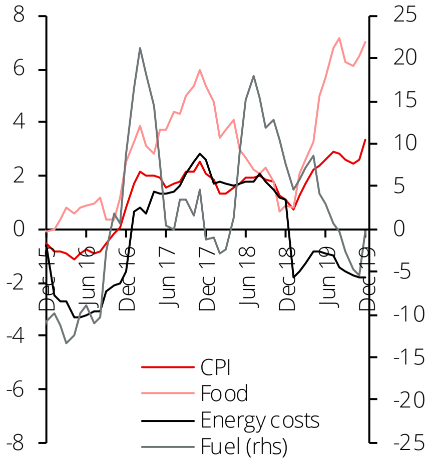
Fuel prices rose by 2.1% m/m in December, which moved their y/y growth from -5.4% to -0.2%. The reported rebound was slightly smaller than we estimated. While this category is a significant factor contributing to the rise of y/y CPI inflation vs November, it is not responsible for the big surprise with the December flash reading.

After such high December, CPI is in fact certain to be well above 4% y/y in 1Q2020 and may remain substantially above 3% for the better part of the year. Please mind that we have energy tariff hike upcoming in 1Q and the different timing of introduction of the hike by energy providers (due to different decision dates by the regulator) will cause that CPI growth will hang above 4% y/y longer than we had assumed. What is important, the potential compensation to households from the government will not mitigate the impact of electricity price tariffs on CPI. We also do not know if the approved hikes will be the last ones this year – it cannot be excluded that another wave comes in the middle of the year.

On the flip side, the economy started slowing and wage pressure is easing, which should ease the inflationary impulse somehow later in 2020. A question is arising, however, if the quicker than expected rise of inflation can lead to further rise of inflation expectations and as a consequence to a rebound of wage pressure. Consumer inflation expectations rose substantially already in late 2019, climbing to the highest level in seven years.

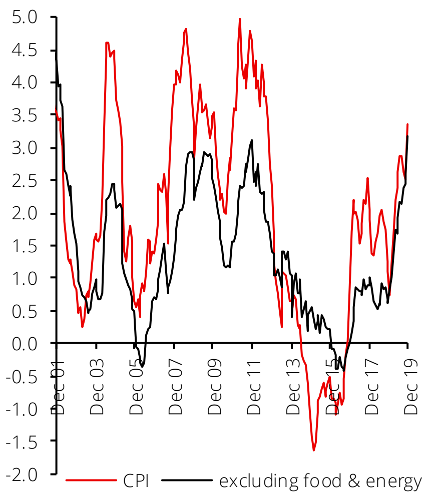
The monetary policy has just become much more interesting. We do not rule out that rate hike motions will be back on the agenda soon, although we do not think they will gather majority support anytime soon. Today, the January MPC meeting starts. The interest rate market was pricing a rate cut in Poland few weeks ago, now such conviction may disappear.

CPI inflation and selected components, %y/y



Source: GUS, Santander

CPI and core inflation, %y/y



Source: GUS, NBP, Santander

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