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Economic Comment

Inflation is not giving up

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Our forecast of January CPI (2.7% y/y) is clearly above market expectations (according to Bloomberg and a survey by Parkiet daily it is 2.4% y/y). We guess that majority of analysts have underestimated the impact of new taxes and charges, including their influence on food prices. We also assumed that core inflation rose somewhat after the December dip caused mainly by transport services prices. January inflation readings from other European countries are mostly coming way above expectations. Later in the year we still expect inflation to stabilise around the NBP target partially caused by high statistical base effects from 2020. However, risks for the CPI path seem to be skewed upwards, given possible disruptions on the food market and supply limitations in the initial phase of demand recovery when epidemic restrictions will be eased.

On Monday, 15 February, Polish CPI data will be out. January readings do not get a flash release by GUS, so we know less than usual before the full report. This also means that January prints in Poland are also the only ones that come after the preliminary data for Eurozone and the readings from Czechia and Hungary. One thing the markets are focusing on at the start of 2021 is tracking signs of global reflation, so we considered it worthwhile to describe in more detail what the Polish publication may bring.

Forecasts

Market consensus (based on Parkiet daily newspaper, gathered in late January) is 2.4% y/y – equal to the December reading. The dispersion of forecasts was particularly high this time. Median of forecasts gathered by Bloomberg news agency is also 2.4% y/y.

The large dispersion may come not only from the usual thinking that the turn of the year is often a moment of price policy revisions by producers and sellers. There is also an unusually large number of additional factors the CPI impact of which had to be assessed (sugar tax, extra tax on alcoholic beverages in bottles up to 30cl, retail tax, electricity bill hike, power surcharge, RTV subscription hike).

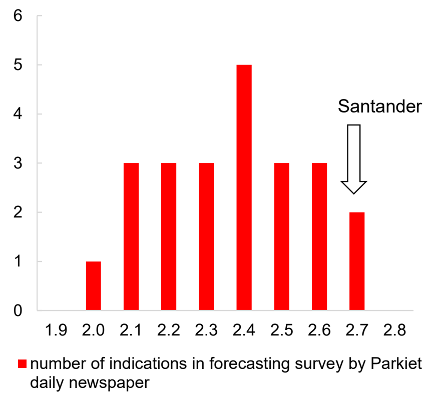
We show for comparison the dispersion of Dec'20 CPI forecasts, the previous edition of the Parkiet survey. (see: margin chart).

In our view, the impact of the sugar tax was strong enough to bend upwards the path of food price inflation which had been systematically falling since April 2020. We assumed that the whole impact of sugar tax and the extra tax on alcoholic beverages in bottles up to 30cl will show up in January CPI (based on information from the burdened companies). Taking into account the changes in electricity and gas bills we estimated that the total growth in the energy category slightly exceeded 5% y/y compared to 4.7% in December. We assessed the fuel price change in January at 3.5% m/m, which means that this component may have contributed to headline y/y CPI some 0.1pp more than in December. We also assumed that y/y core inflation partially recovered in January after a large drop in December.

Transport services and insurance significantly depressed the December inflation, the opposite of what had happened in December 2019 – what we got was a strong negative base effect that made an impression of services prices inflation finally yielding to the pandemic. However, besides the two mentioned services categories, in December there was no broad turn in the growth of services prices. What is more, in late 2020 the persistently high services prices inflation got some support from accelerating wages.

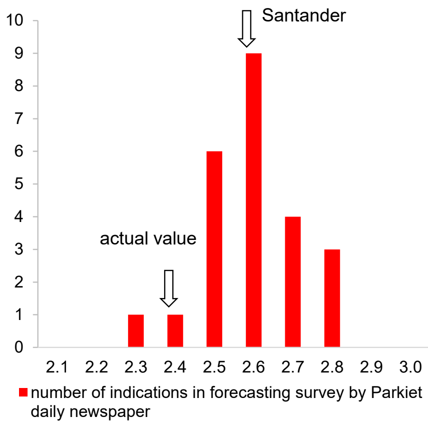
The calculations and assumptions led us to a forecast of CPI growth that is higher than the market consensus.

Forecast distribution for Jan21 CPI, % y/y



Source: Parkiet, Santander

Forecast distribution for Dec20 CPI, % y/y



Source: Parkiet, Santander

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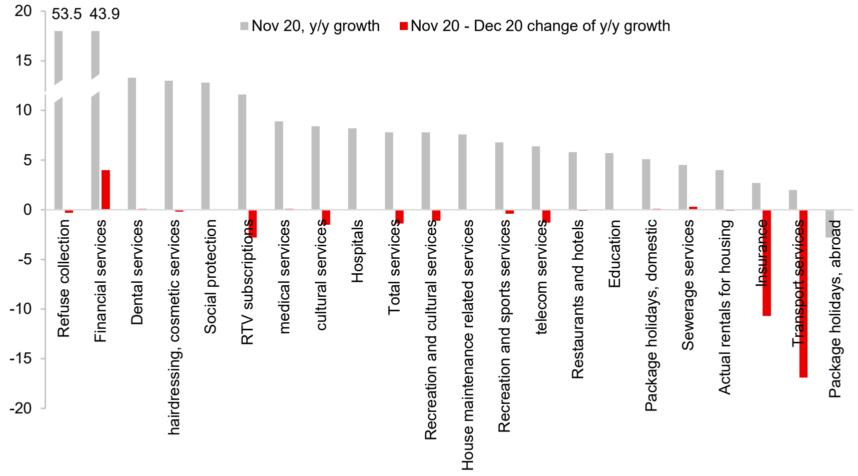
Services prices inflation in y/y terms and its change in Dec'20 in percentage points, CPI data for Poland



Source: GUS, Santander

Inflation environment

We know, that in the neighbourhood of Poland, there was a significant rise in inflation in January – In Eurozone and in particular in Germany. The January move pulled many European countries and Eurozone as a whole from the negative inflation territory. The Eurozone inflation instead of the expected 0.6% y/y increased to 0.9% y/y from -0.3% y/y in the month before. The German HICP grew to 1.6% y/y vs expectations of just 0.5%y/y and a previous reading of -0.7%y/y.

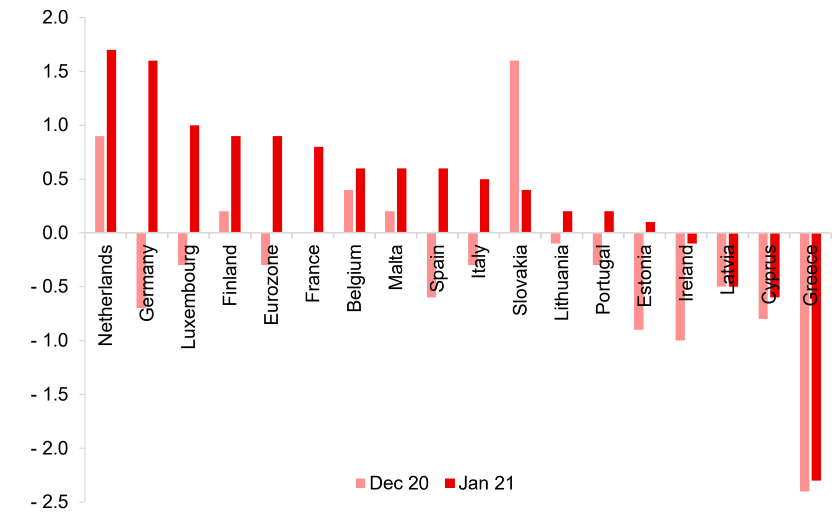
The scarce preliminary data imply that the move higher was a result of the core elements of the inflation basket: industrial goods (excluding energy) and services. In many countries, the energy prices also significantly beat up the overall consumer prices growth, however the food prices component had neutral and often even negative influence on the change of inflation between December and January (excluding Germany, where it added to total HICP).

Forecast median for Jan'21 inflation according to Bloomberg and actual value

HICP,%r/r	Actual Dec'20	Forecast Jan'21	Actual Jan'21
Eurozone	-0.3	0.6	0.9
Germany	-0.7	0.5	1.6
Germany CPI	-0.3	0.7	1.0
France	0.0	0.5	0.8
Spain	-0.6	-0.6	0.6
Italy	-0.3	0.2	0.5
Norway CPI	1.4	1.8	2.5

Source: Bloomberg, Santander

HICP inflation in EU countries, for which flash estimates for Jan'21 were released

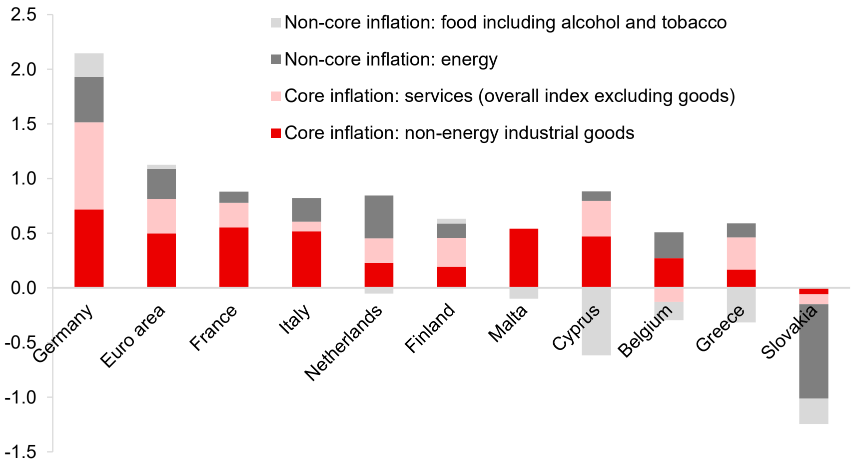


Source: Eurostat, Santander

January inflation readings, both those published by the Eurostat for the Eurozone countries as well as the upcoming reading in Poland, are based on the old set of inflation basket weights, hence the move is not a result of the basket components reweighting process.

What happened to the inflation in the close neighbourhood of Poland? In Germany there was a huge shock, however in Slovakia, which back in December had the highest inflation in the Eurozone, in January there was the largest decrease of inflation among the member countries which reported flash estimates. Lithuania's inflation moved higher but just a bit.

Breakdown of the change of y/y HICP inflation between Dec'20 and Jan'21, in percentage points



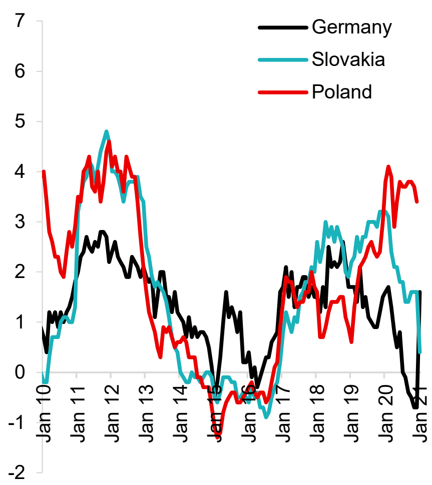
Source: Eurostat, Santander

One can wonder whether in Poland in January the inflation will move in a similar fashion to Germany or rather to Slovakia fashion (two readings on the opposite sides of the inflation change spectrum). In both cases there is a rationale for expecting some sort of correlation to Polish CPI (geographical and cultural proximity, trade linkages).

In 2020 there was, however, a total decorrelation of CPI paths of those countries inflations with the Polish one. The higher correlation persists still with the inflations of Hungary and Czechia – those two countries will get their CPIs published on Friday 12 February which is one working day before the Polish reading on Monday 15 February.

At least in the case of Germany, the upside jump of inflation has resulted from the reversal of the temporary anti-crisis cut in the main VAT rate to 16% from 19%. In Poland the noticeably higher inflation path in 2020 was a function of increases in administered prices, while the taxes impacting consumer prices were not lowered. The administered prices are being increased in 2021 as well, while other taxes and fees impacting CPI are being hiked. As a result, the factors which strongly upbeat the German inflation might help the Polish inflation stay at the elevated level, preventing the negative base effects from occurring.

HICP inflation, % y/y



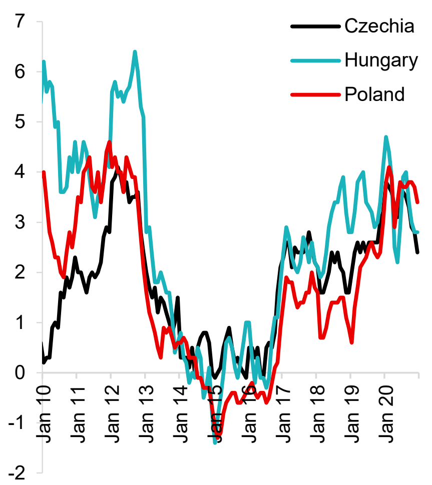
Source: Eurostat, Santander

Conclusions for January

We do not expect Poland to witness such a strong spike in CPI as numerous euro zone countries. However, our forecast prepared at the end of January proved to be the highest on the market. We guess that it is because our estimates of new items (taxes and hikes in administered prices) were higher and we assumed a partial rebound in services prices after the December decline. Thus, maybe CPI did not jump as much as in the euro zone, but in our view it was not as stable as assumed by the consensus.

Later in the year we expect inflation to stabilise around the NBP target with a temporary increase to about 3% in April-May, followed by a decline, partially caused by high statistical base effects from 2020 and the still muted internal demand. However, risks for the CPI path seem to be skewed upwards, given possible disruptions on the food market and supply limitations in the initial phase of demand recovery when epidemic restrictions will be eased.

HICP inflation, % y/y



Source: Eurostat, Santander

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