

Inflation drivers in the euro area

JVI Webinar: Monetary policy challenges inside and outside the euro area



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Deputy Governor

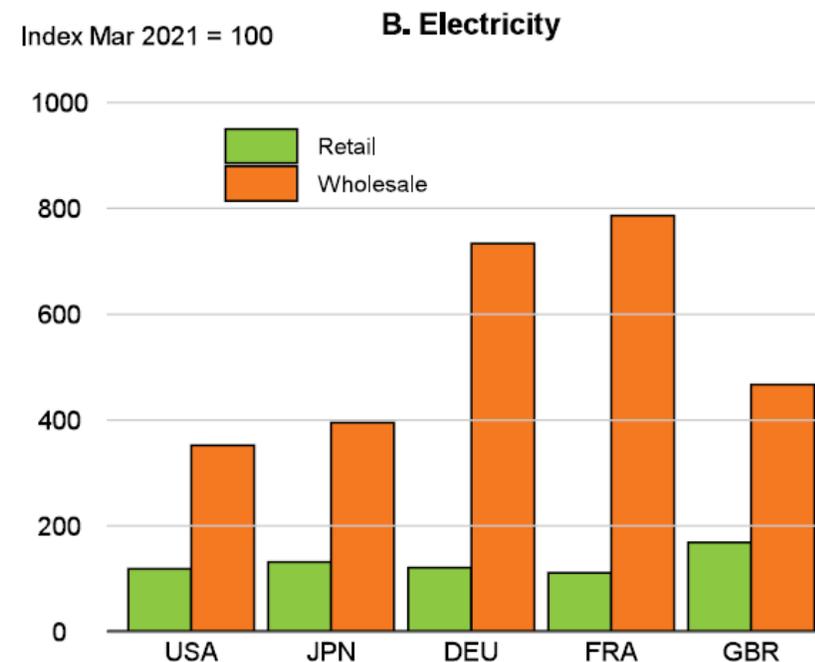
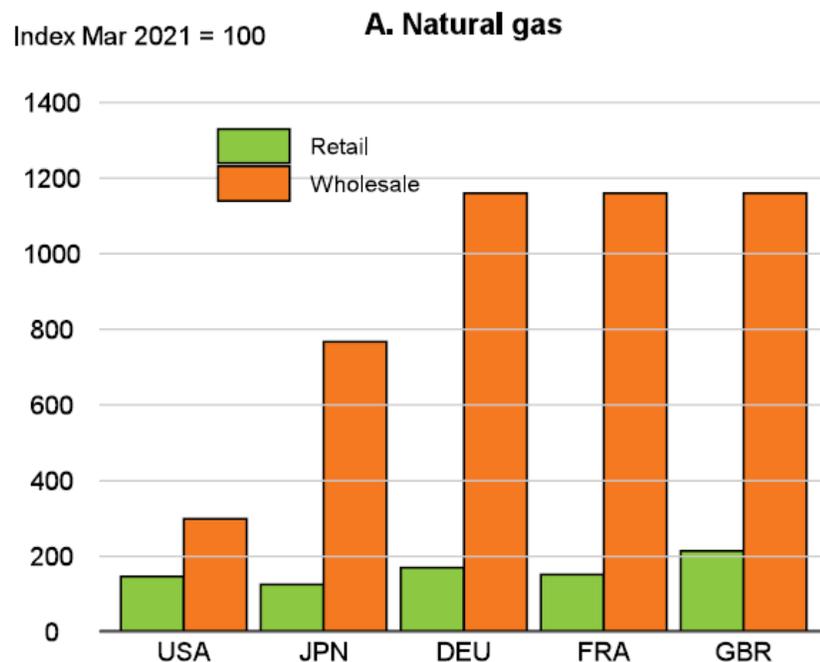


December 2022

Summary

- Inflation has become a global phenomenon
- Large supply shocks (bottlenecks, more recently energy and food price surge)
- Demand supported by fiscal measures and forced savings
- Monetary policy nightmare: series of big supply shocks, threats to inflationary expectations and CB credibility
- Key indicators to watch: labor market trends, fiscal policy and energy security

Global surge in energy prices

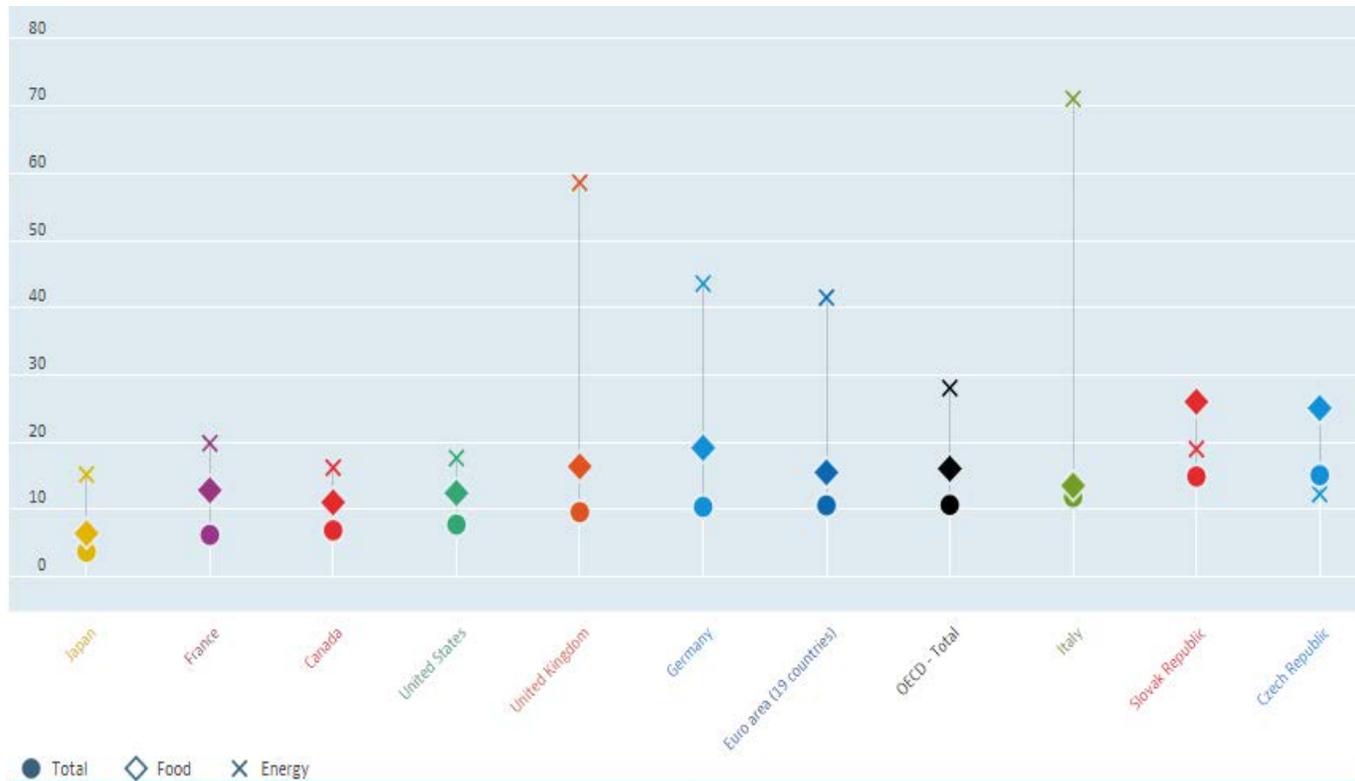


Note: Data refer to September for retail prices (August for the United States) and wholesale prices. Retail price changes based on the personal consumption expenditures deflator in the United States, harmonised consumer prices in Germany, France and the United Kingdom, and national consumer prices in Japan. Natural gas wholesale prices correspond to the Henry Hub Natural Gas spot price for the United States, to Liquefied Natural Gas price in Asia for Japan, to the Dutch Title Transfer Utility (TTF) for Germany, France and the United Kingdom. Wholesale electricity prices data come from each domestic electricity market.

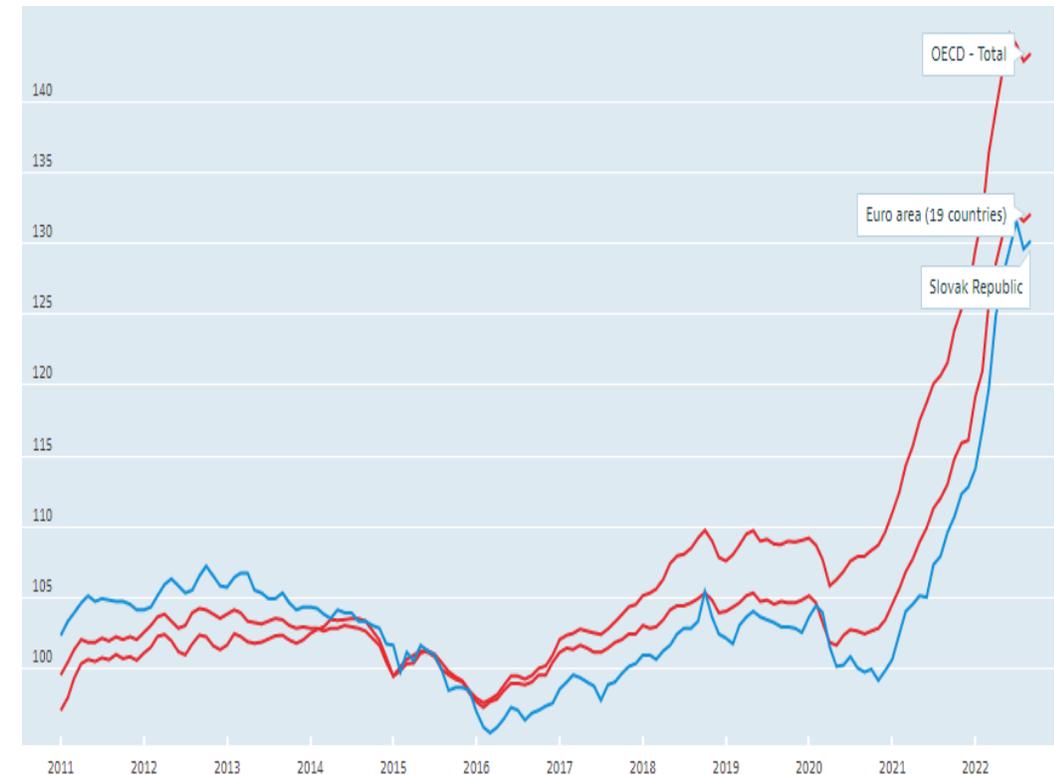
Source: Refinitiv; U.S. Bureau of Economic Analysis; Statistics Japan; Eurostat; U.S. Energy Information Administration; Japanese Power; and OECD calculations.

Energy and food prices

Consumer inflation in October 2022 (%)



Producer inflation

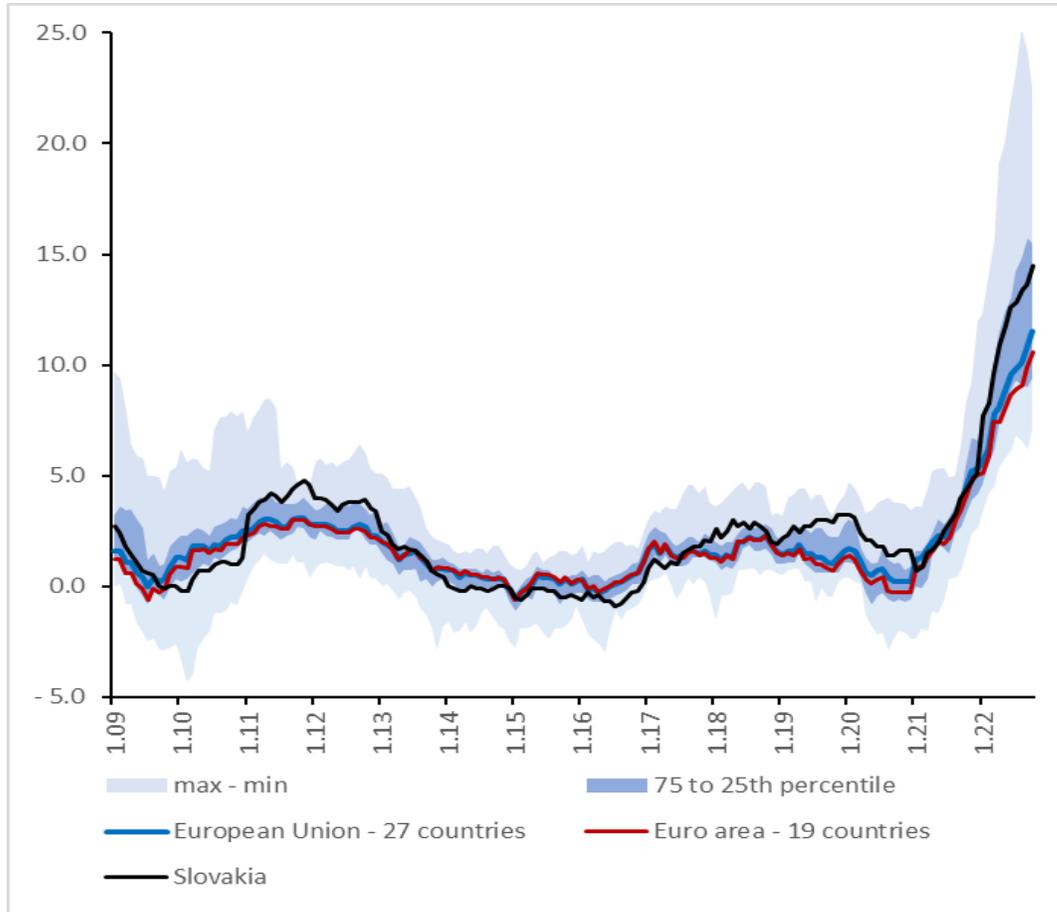


Note: Latest data for October 2022

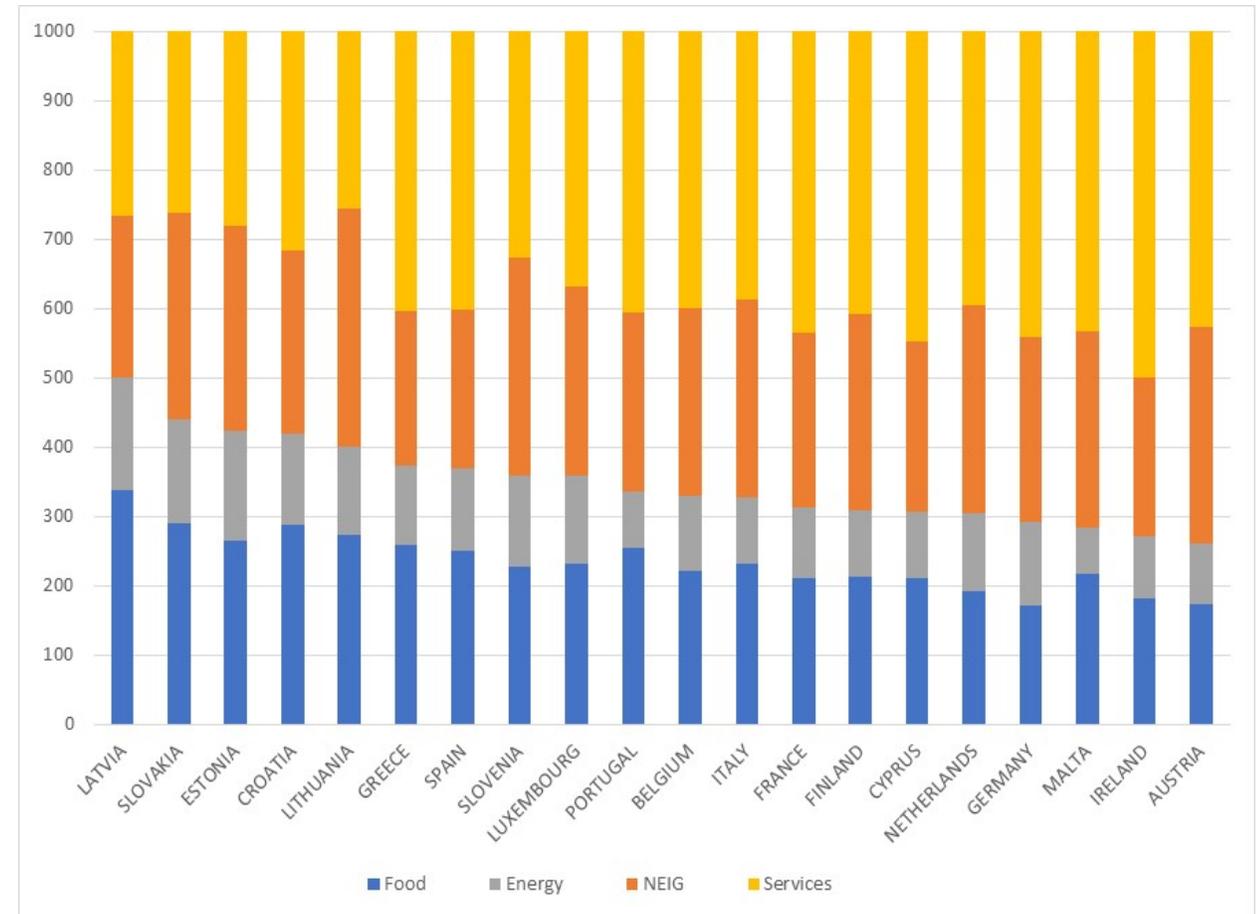
Source: OECD

Substantial differences in the EA

Headline inflation (%)



Consumer basket (weights)



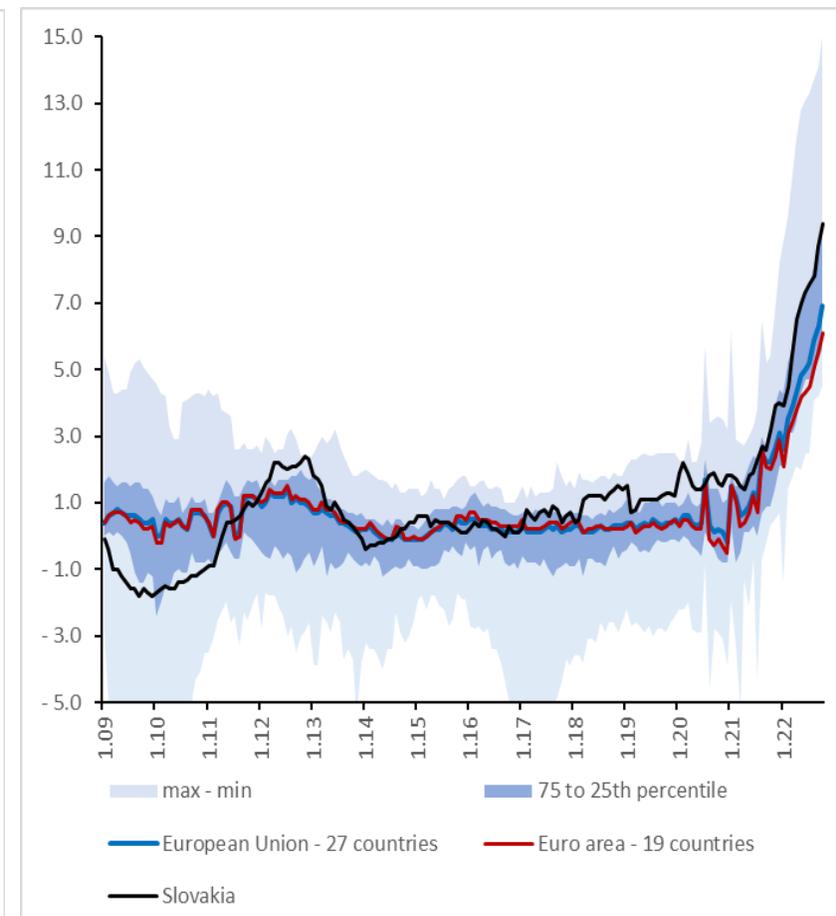
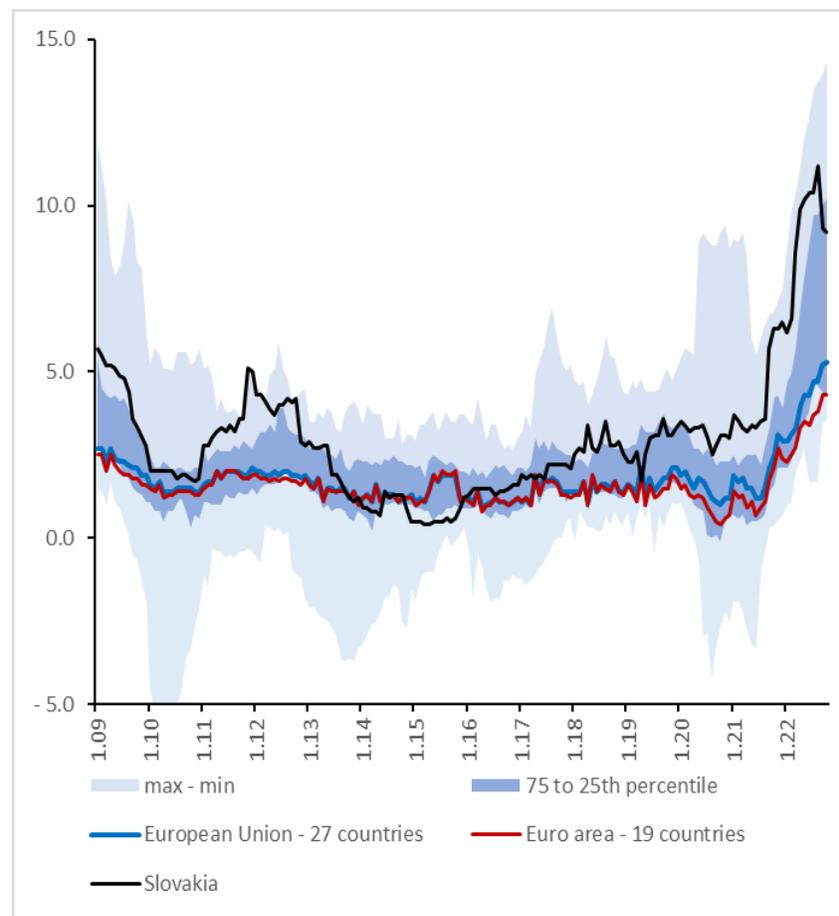
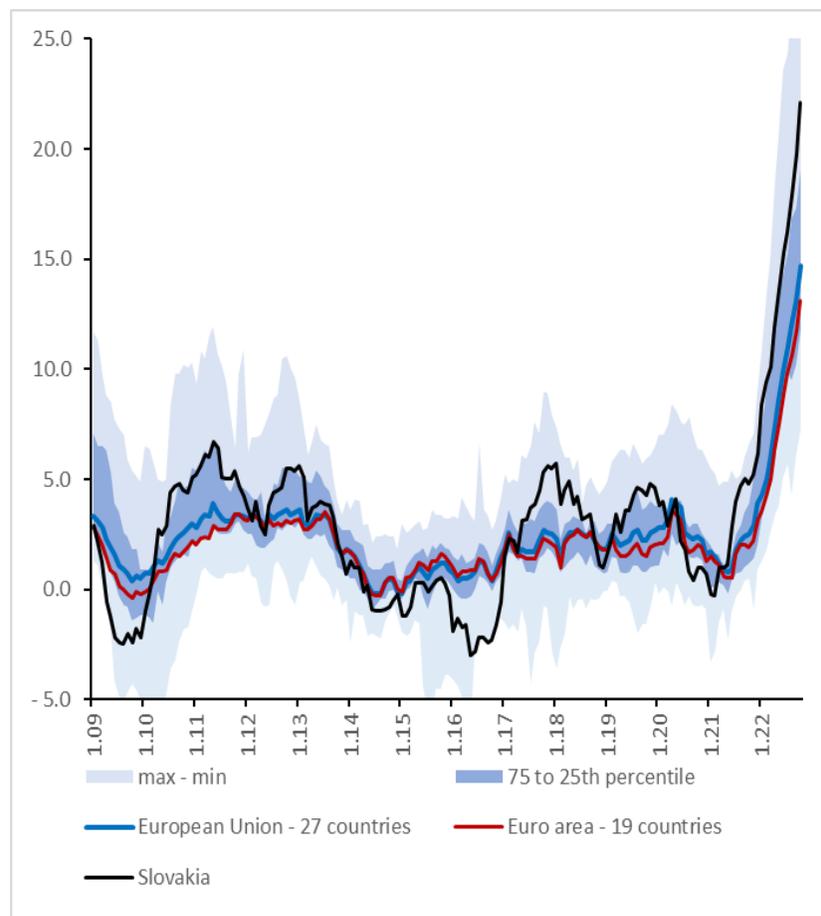
Source: Eurostat

What drives inflation in Slovakia?

Food inflation (%)

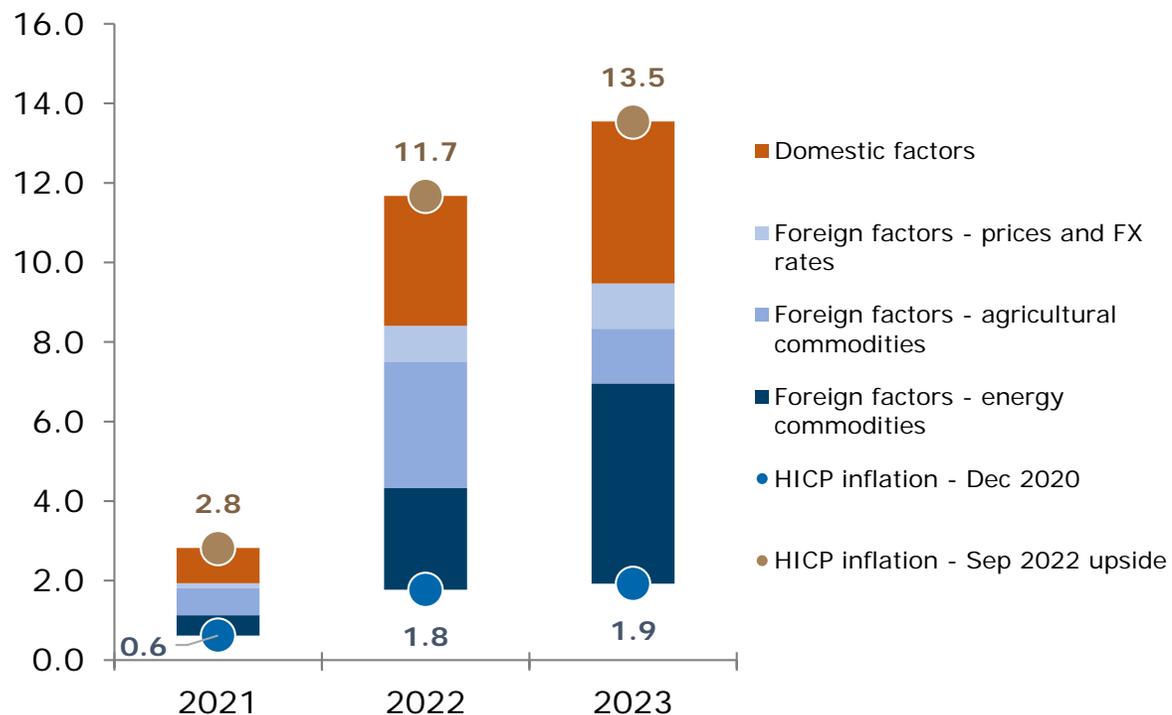
Services inflation (%)

NEIG inflation (%)

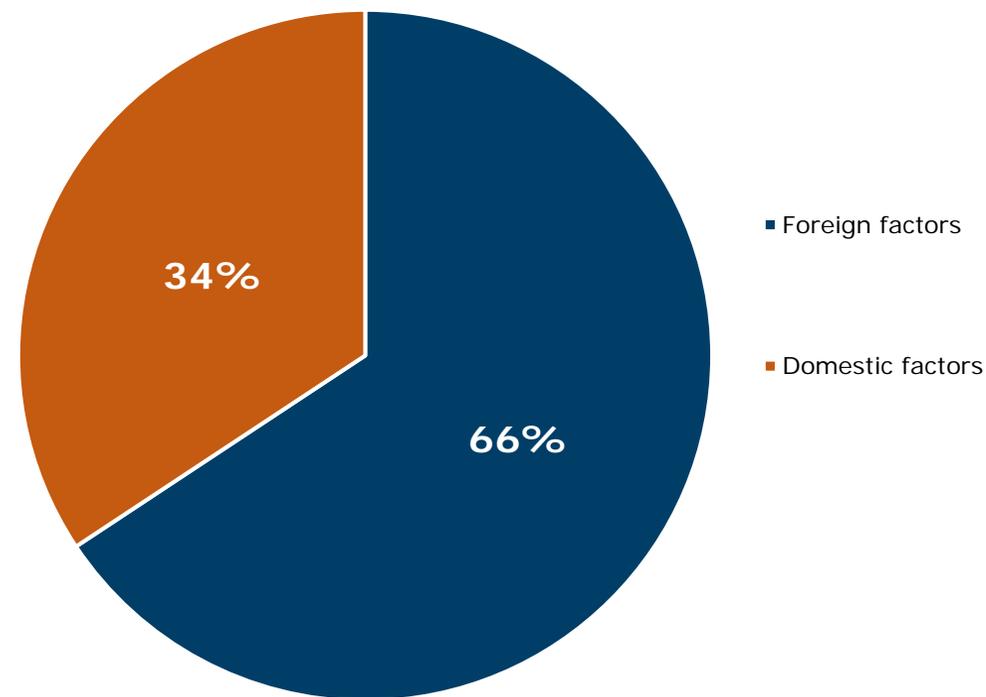


Inflation decomposition (1)

Comparison 2020:P4Q vs 2022:P3Q upside



Cumulated revision decomposition over 21-22

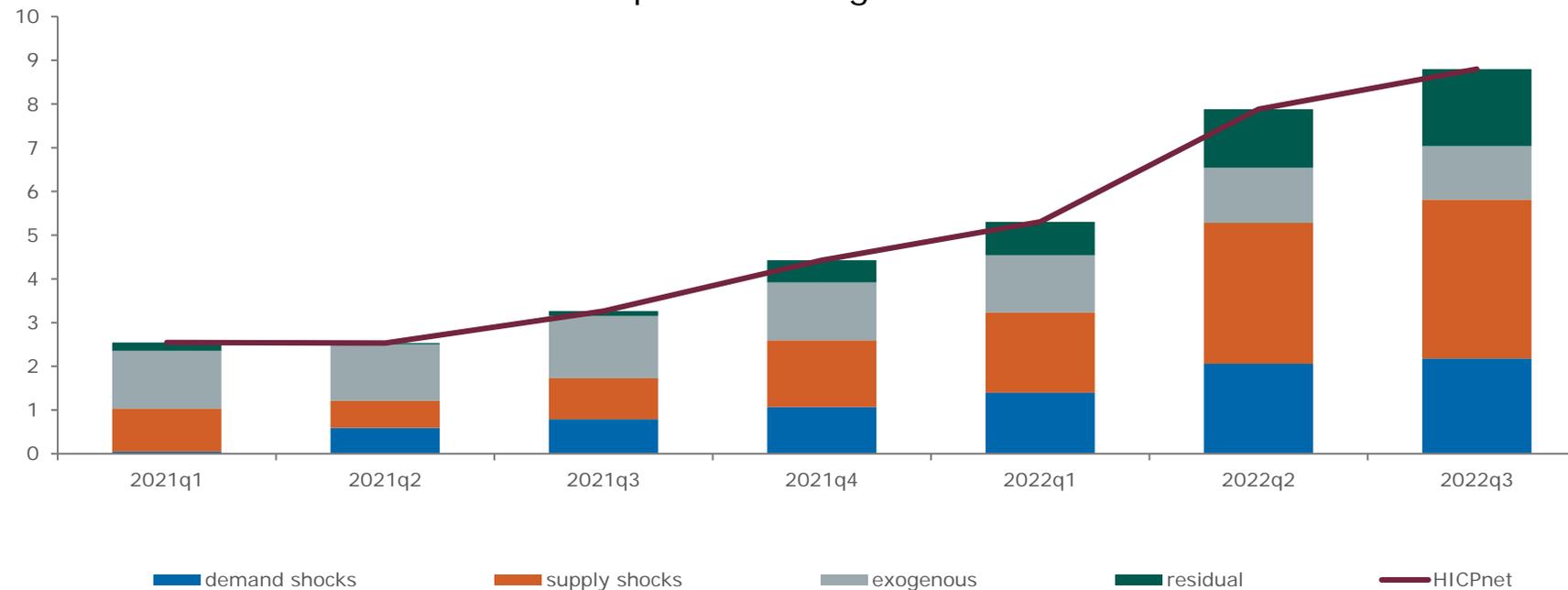


Source: Eurostat

Inflation decomposition (2)

- Supply shocks dominate, their contribution is still increasing
- Positive demand shocks since 2021 – post COVID rebound in HH consumption

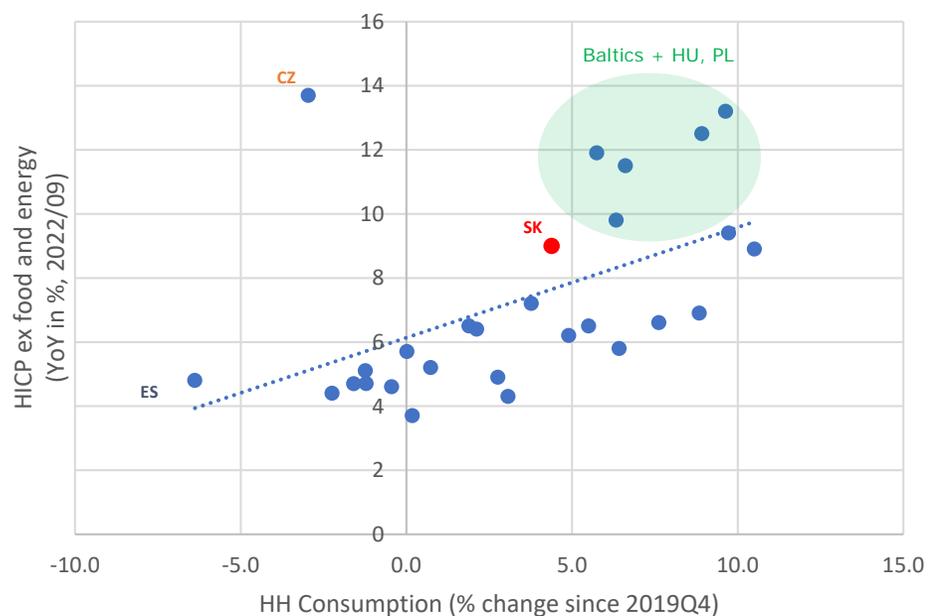
HICP net inflation (excluding food, energy and administered prices, seasonally adjusted, %)
Decomposition using BVAR model



Source: Eurostat, NBS calculations

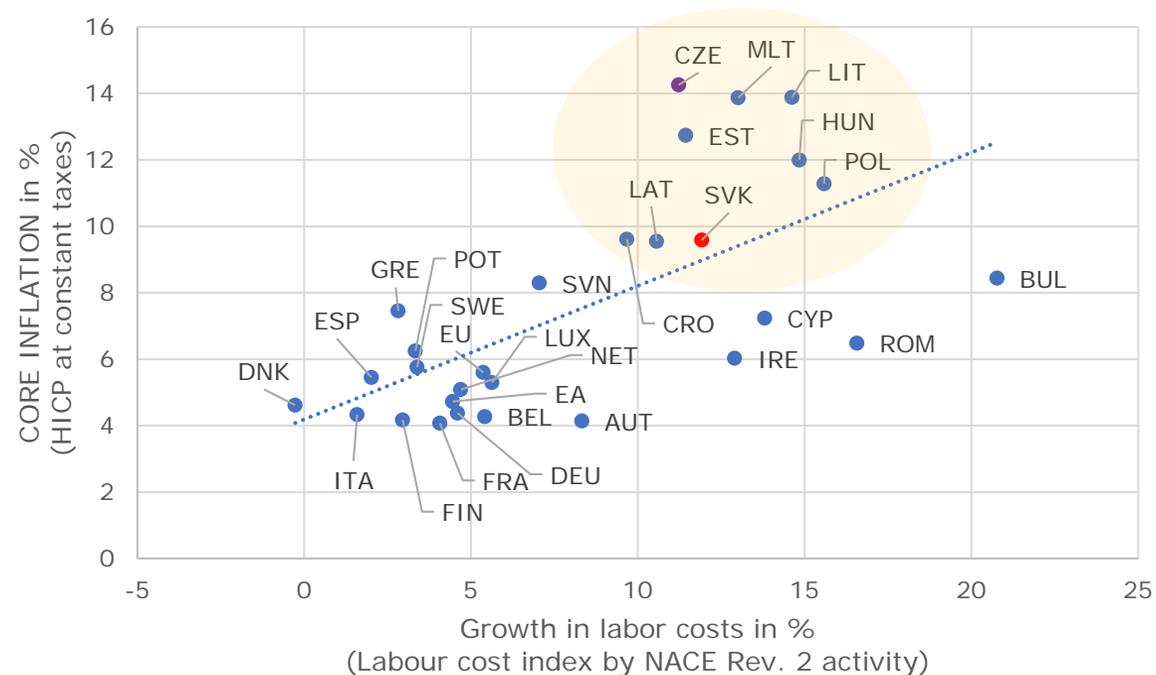
Role of domestic factors

Inflation pressure from households consumption
EU countries



Source: Eurostat, NBS calculations

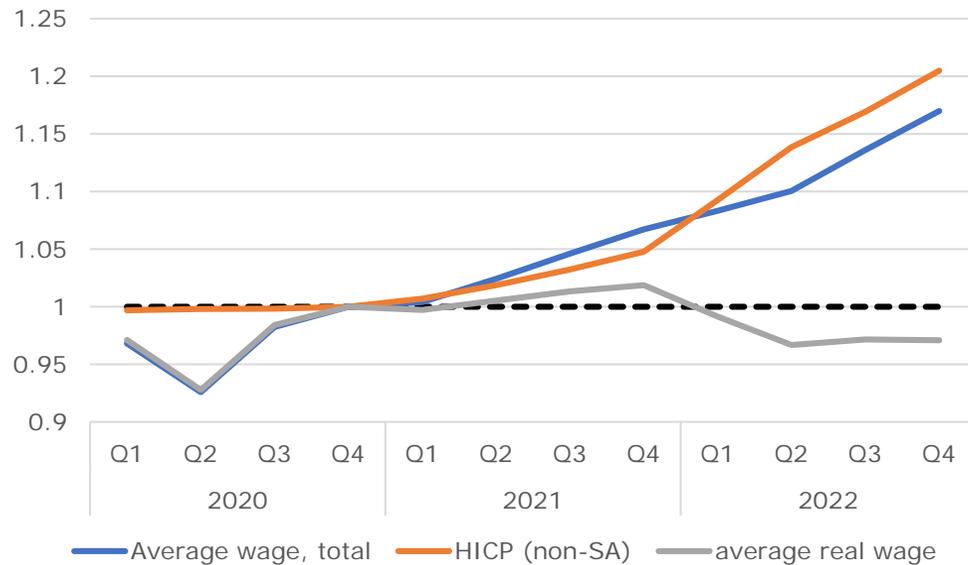
Core inflation vs growth in labor costs
2022:Q2 relative to 2021:Q1



Source: Eurostat, NBS calculations

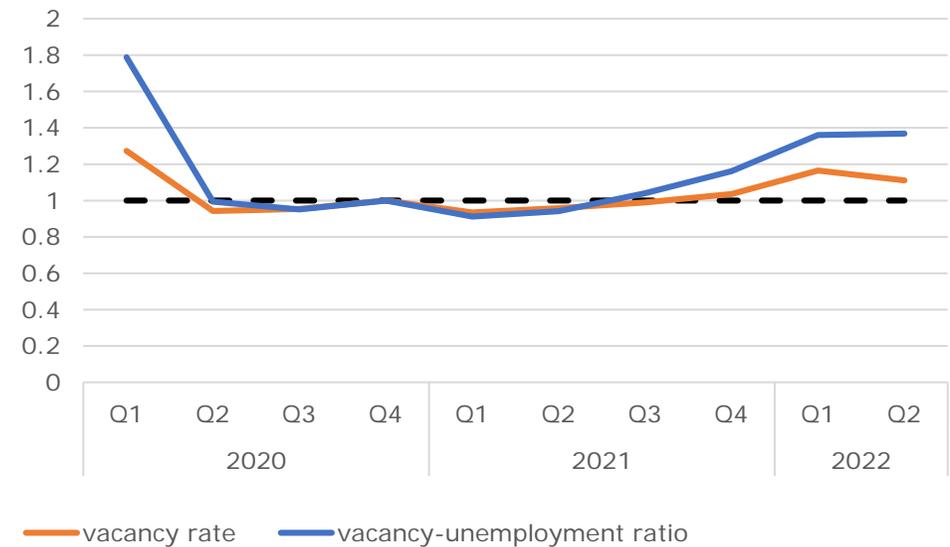
Labor market dynamics

Wage development
(indexed as of 2020:Q4)



Drop in real wages is still limited

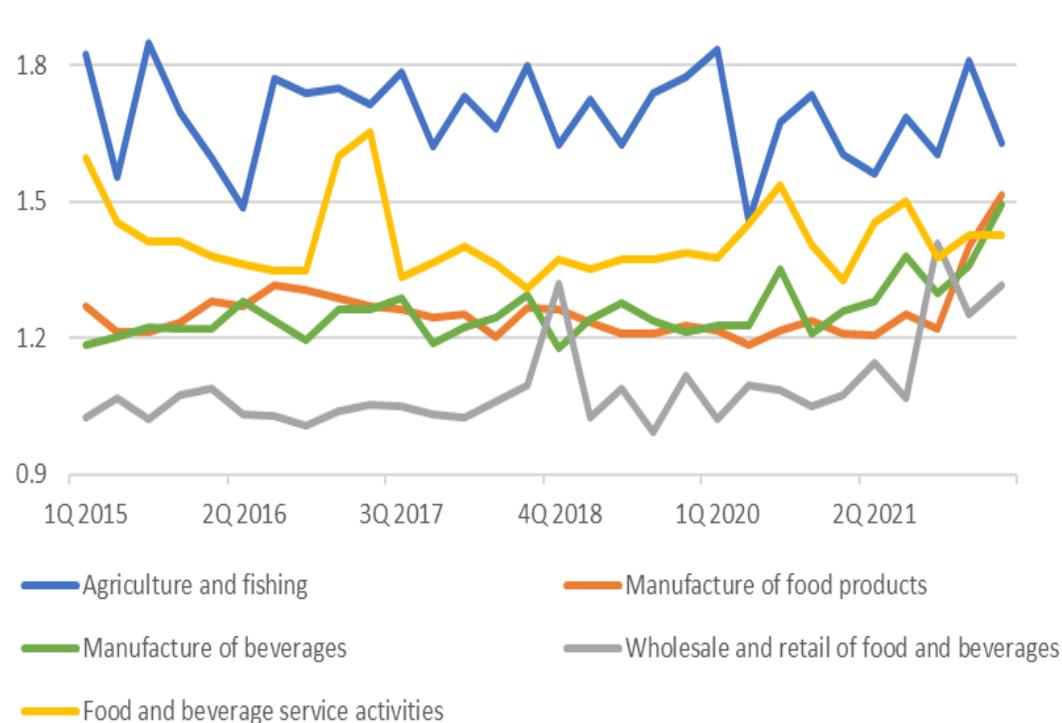
Labor market measures
(indexed as of 2020:Q4)



Labor market stays strong

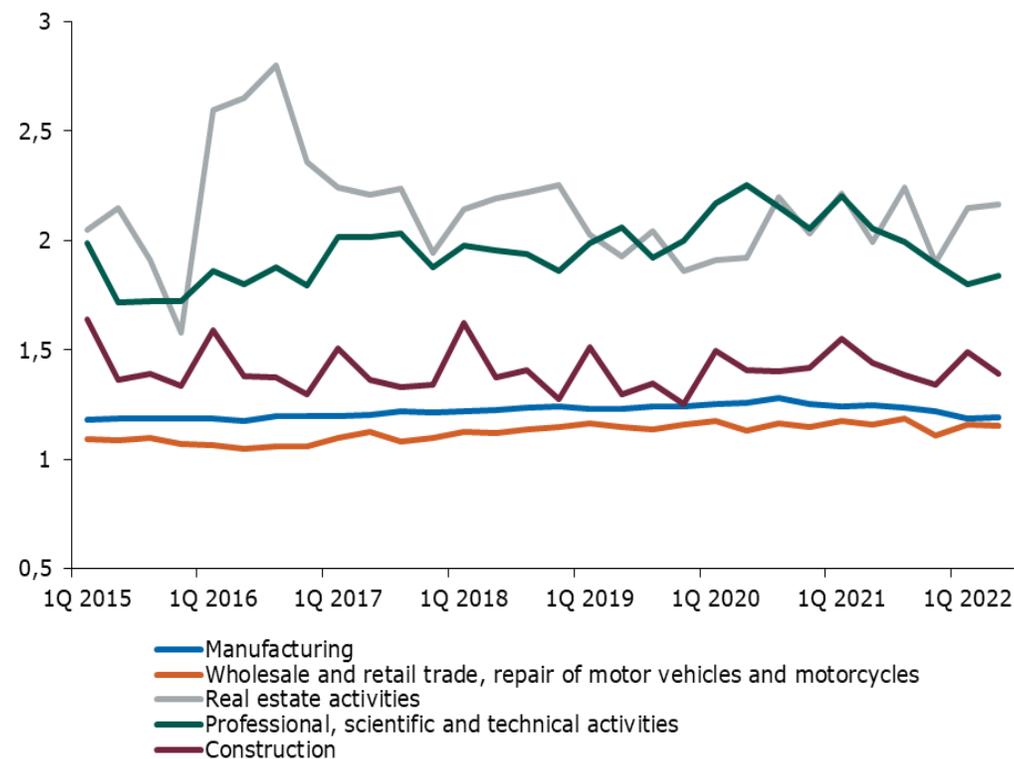
Markups higher in the food sector

Mark-ups in food production chain



Source: SO SR, NBS

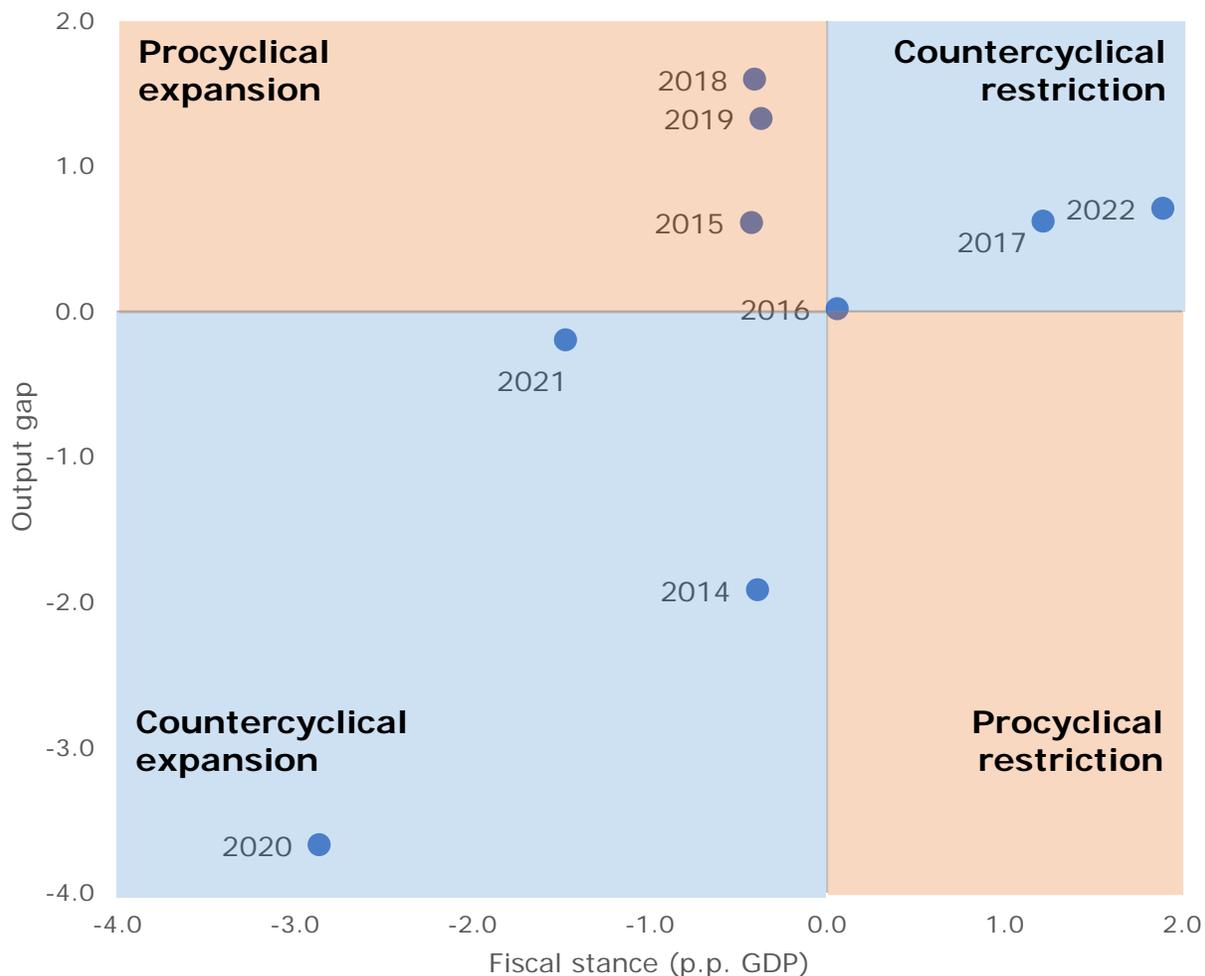
Average sectoral markup – selected sectors



Source: SO SR, NBS

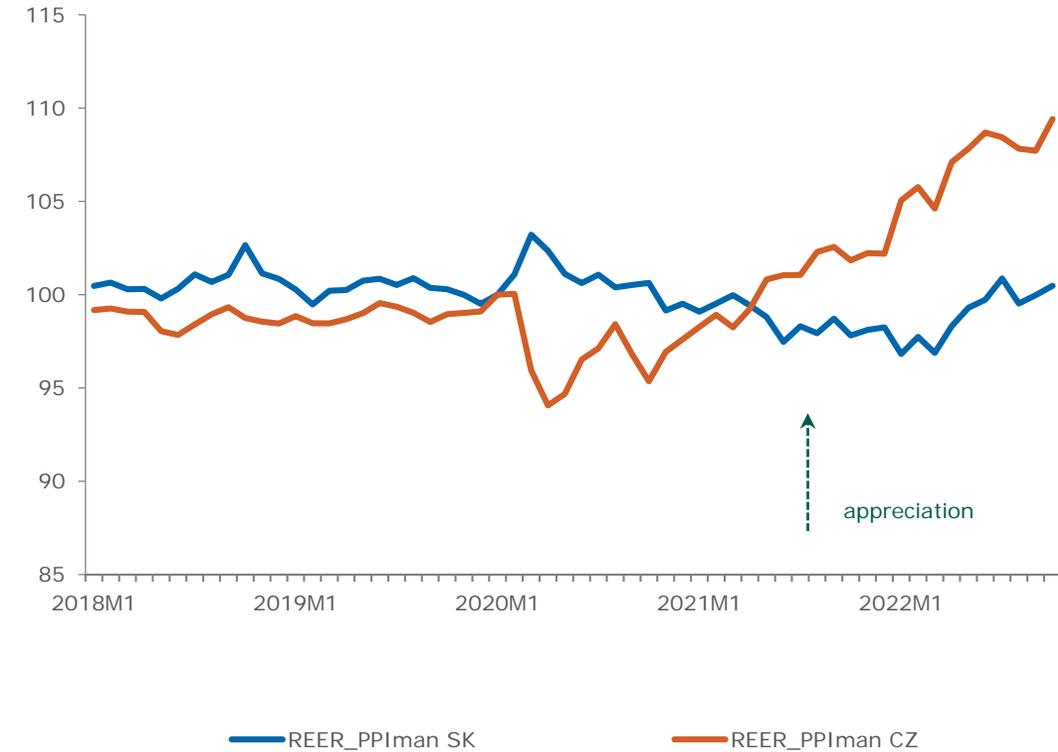
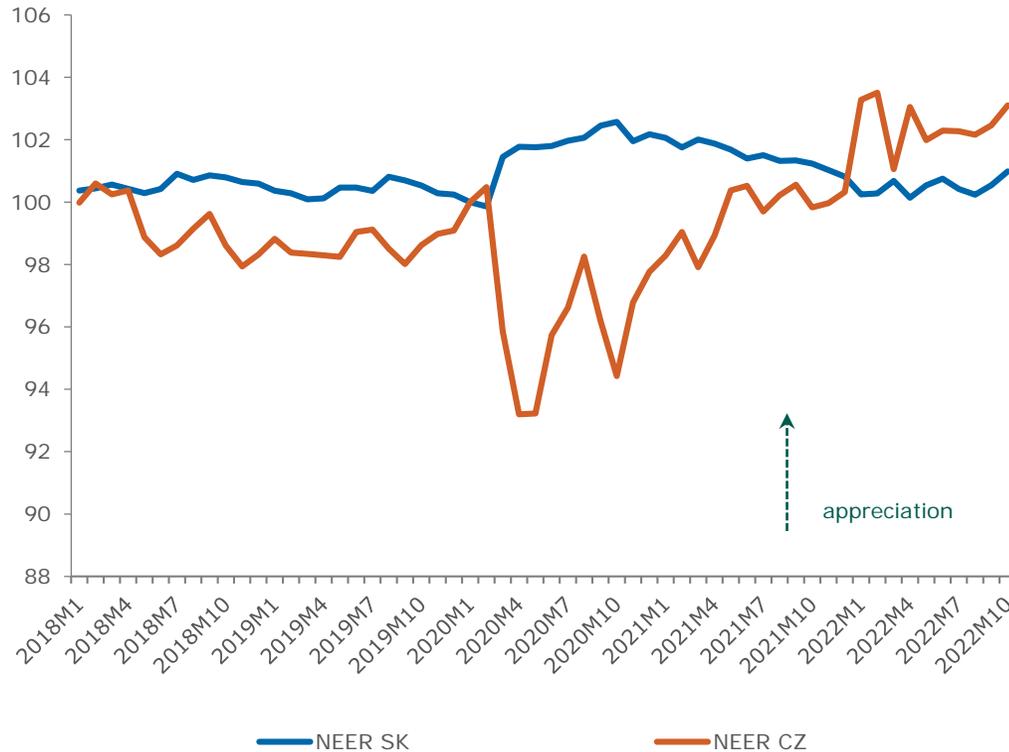
The role of fiscal policy

Fiscal stance and Output gap



- In recent years (from 2014) there are several periods of expansionary fiscal policy, both in bad times (countercyclical) and good times (pro-cyclical)
- Few periods of fiscal consolidation
 - in 2017 due to revenue windfalls and savings on current expenditure
 - In 2022 due to elimination of COVID measures
- Fiscal expansion, when the economy is above potential (pro-cyclical), can lead to inflation pressures
- Fiscal restraint can reduce the cost and time-frame of bringing inflation to its target

Effective exchange rates



Source: ECB and NBS calculations

- Base indices, 2020M1=100
- Similar NEER volatility in calm economic situation – standard deviations CZ 0.7 vs. SK 0.2 (2018-2019)
- In crisis - Czech NEER more volatile than Slovak NEER – standard deviations CZ 2.8 vs. SK 0.7 (since 2020)

Source: ECB and NBS calculations

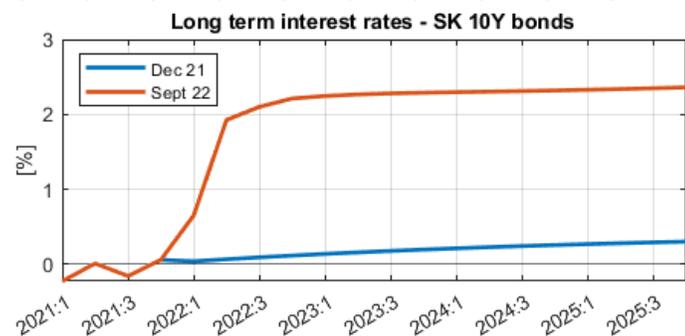
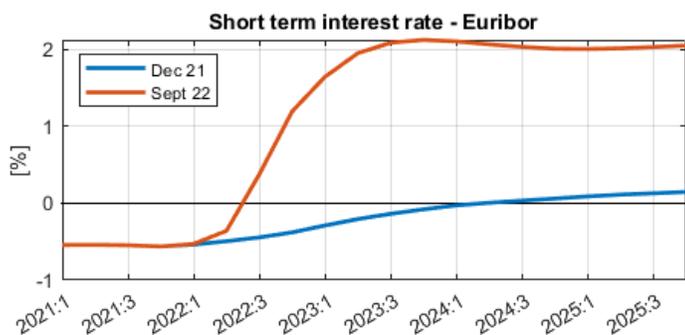
- The REERs provide a similar picture – volatility determined by the NEERs
- PPI-manufacturing based REER standard deviations – CZ 0.4 vs. SK 0.6 (2018-2019)
- In crisis - larger standard deviations in the Czech Republic – CZ 4.5 vs. SK 1.5 (since 2020)

Monetary policy response

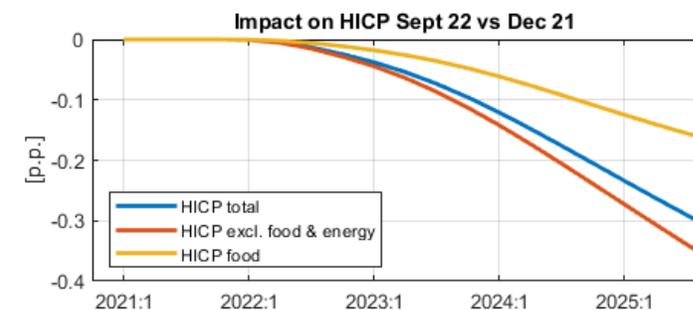
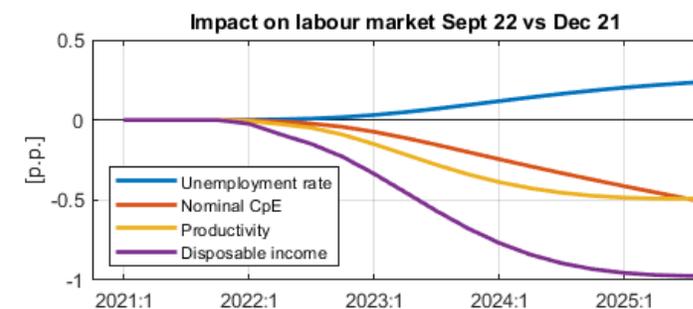
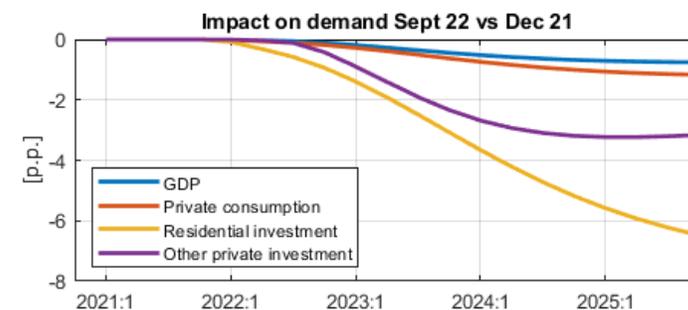
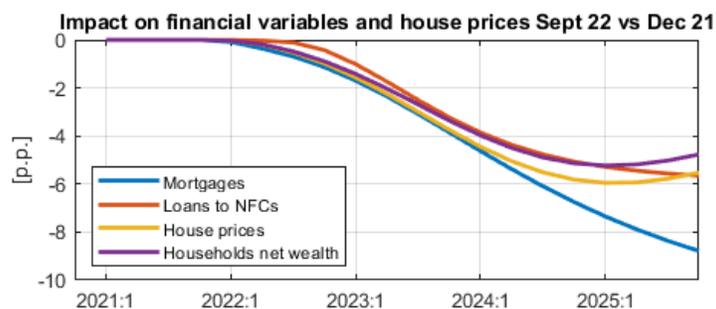
Model-based impacts of actual monetary policy tightening:

- a) a negative impact on further lending → subdued demand through both consumption and investments channel accompanied by a correction in house prices
- b) *only a limited impact on HICP inflation suppression,*
- c) the effects of today's tightening could emerge gradually over a longer time horizon

An increase of Euribor and 10Y SK bonds since Dec 21



Source: ECB



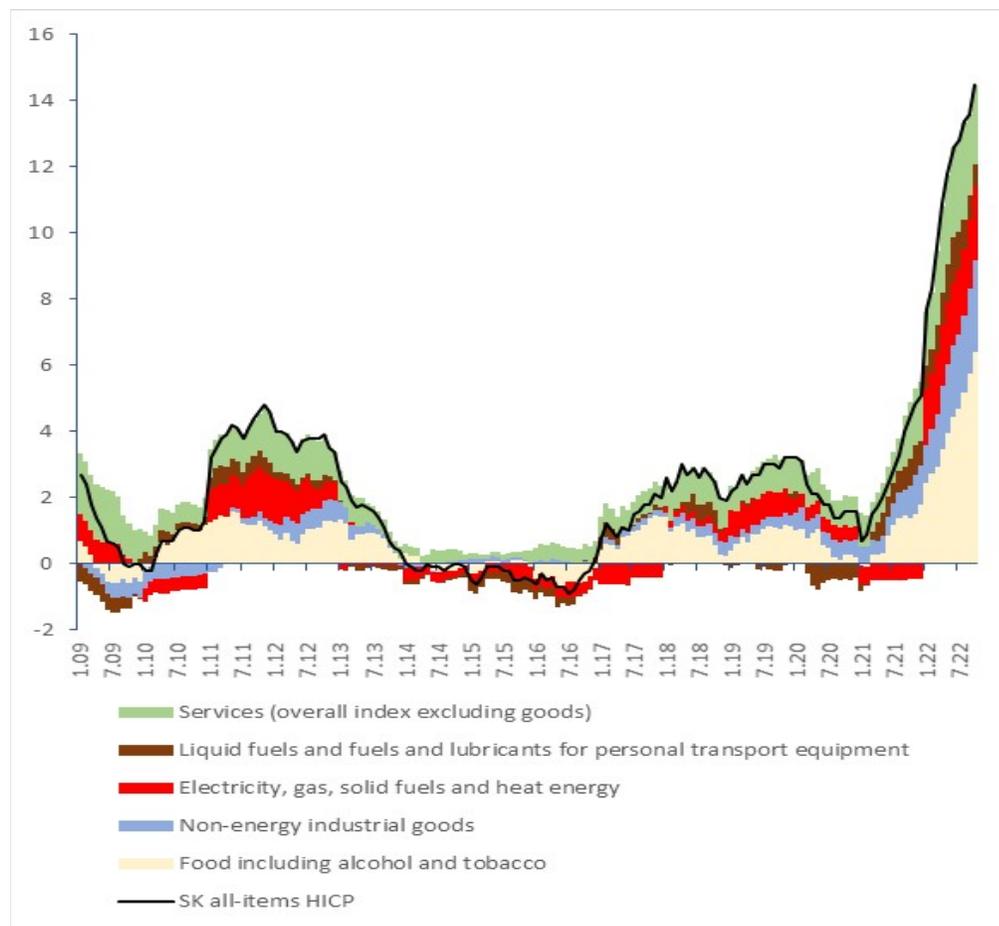
Source: NBS. Model responses as deviations from baseline level.

Background slides

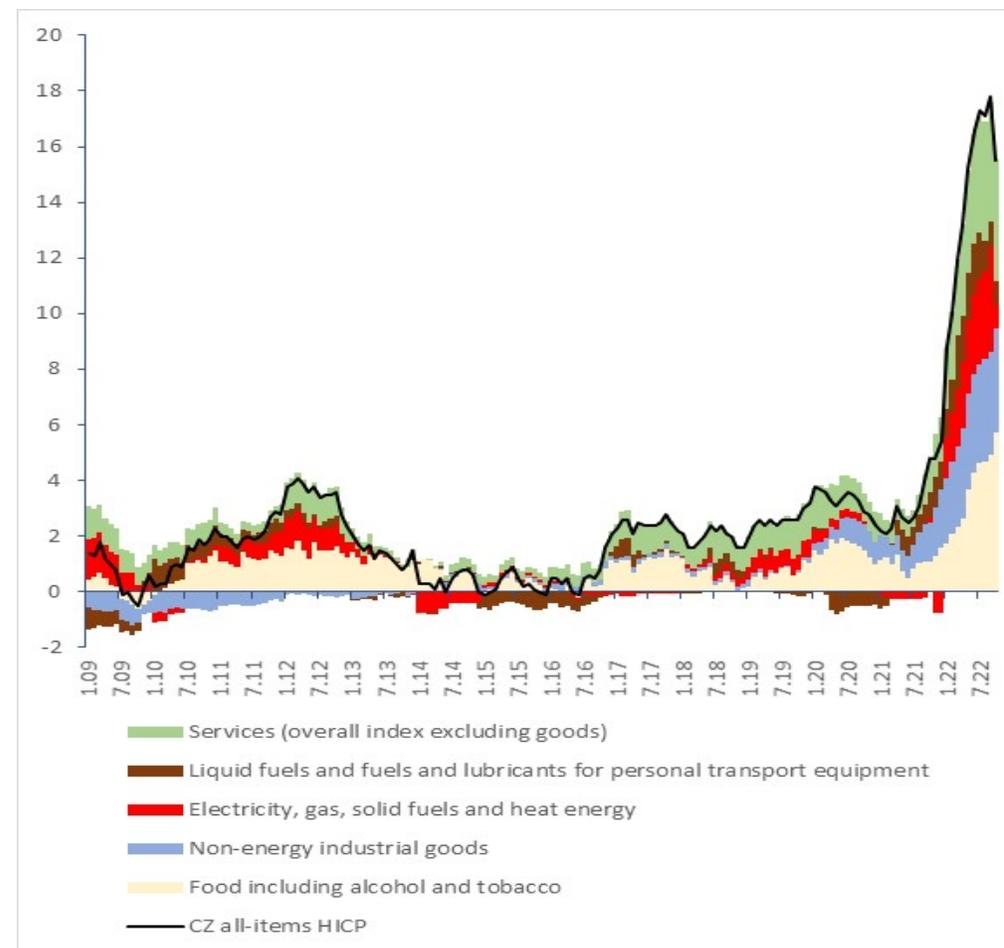


Comparison with Czechia

Headline inflation and main components – SK (% p.p.)



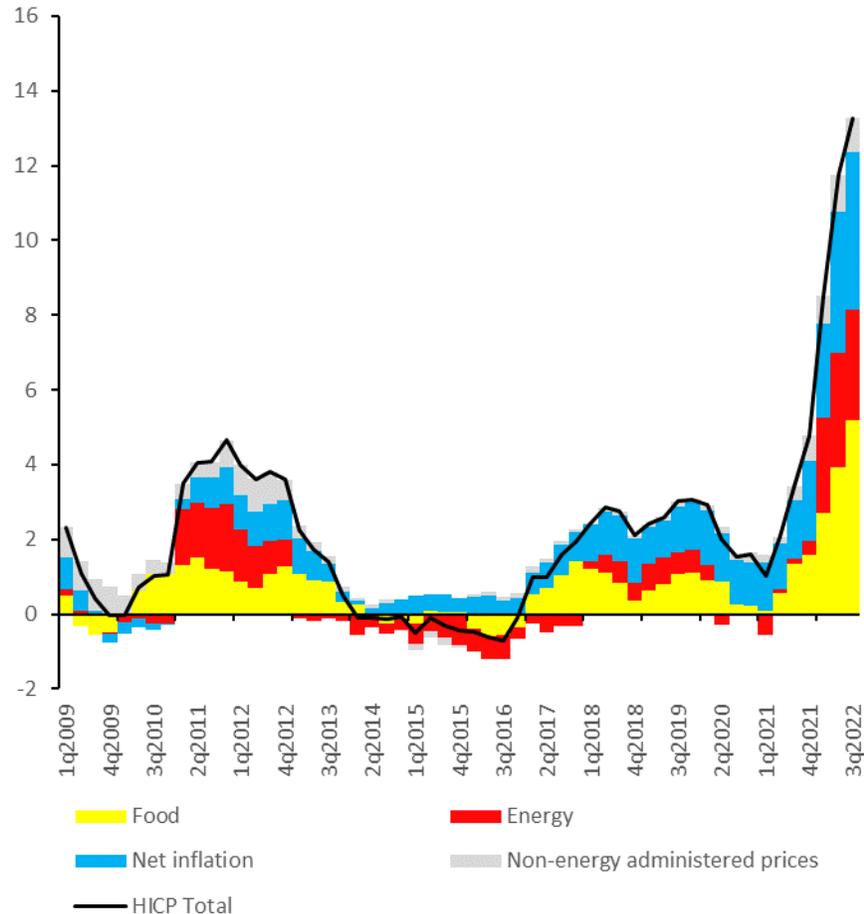
Headline inflation and main components – CZ (% p.p.)



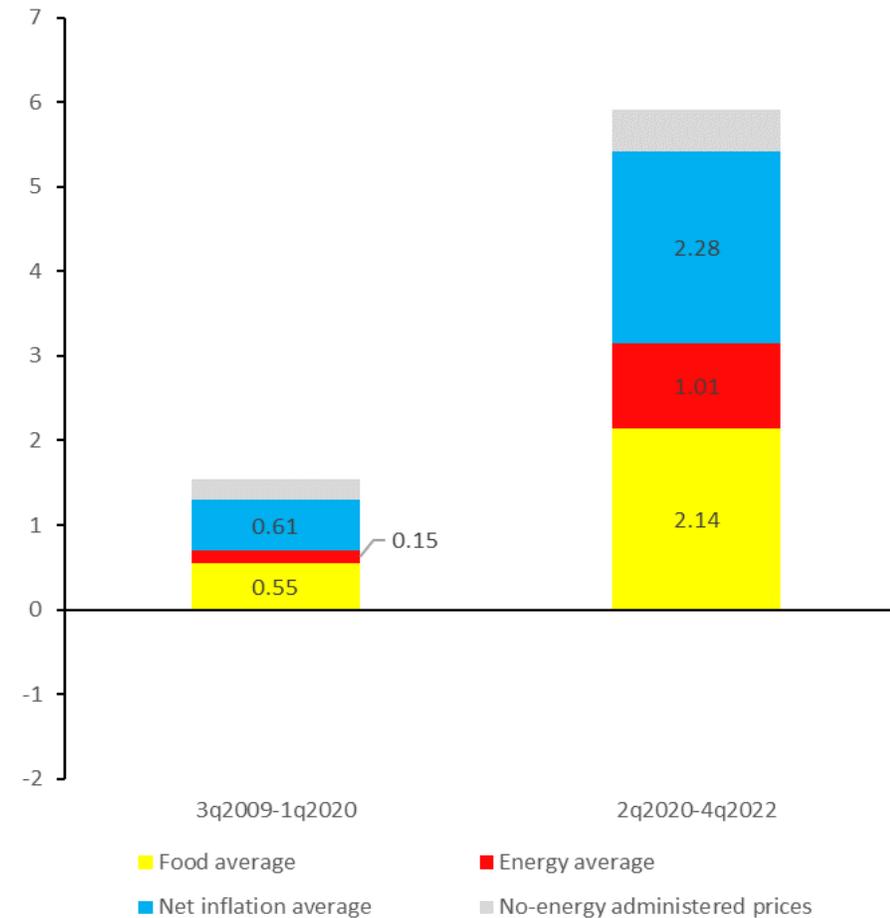
Inflation decomposition in detail

Main contribution comes recently from food prices and net inflation

Headline inflation and main components (% p.p.)



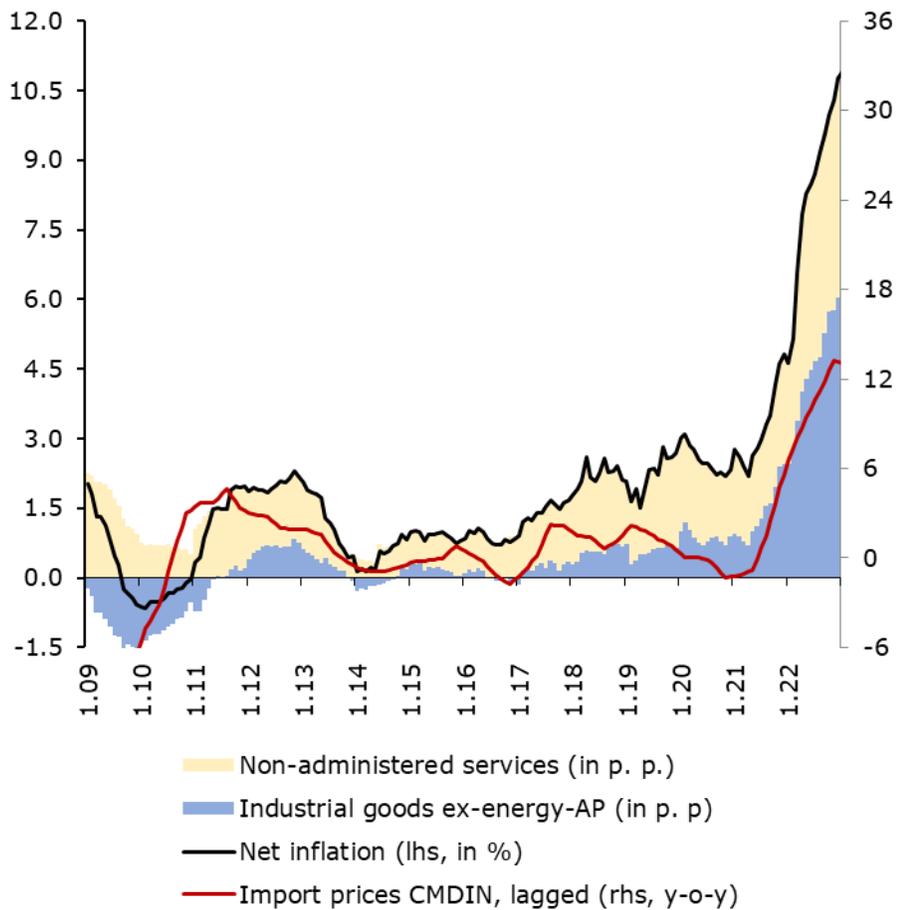
Contributions of main components (in p.p.)



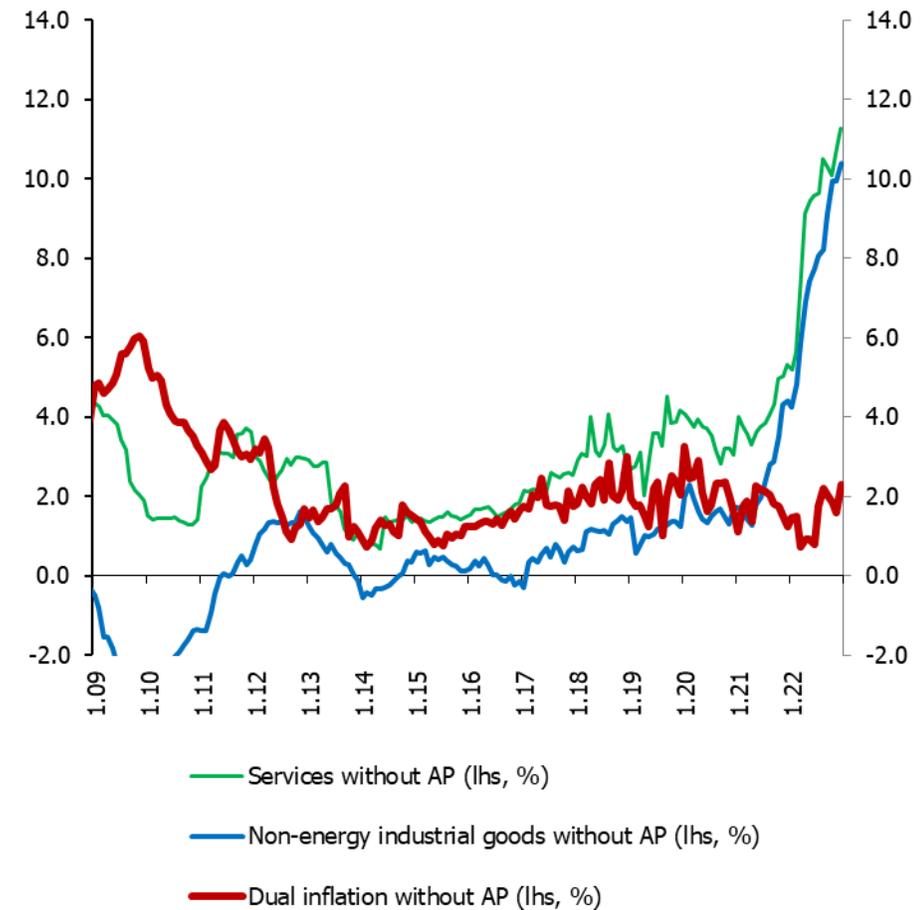
High contribution from Net inflation in last 2 years

Dual inflation remains stable

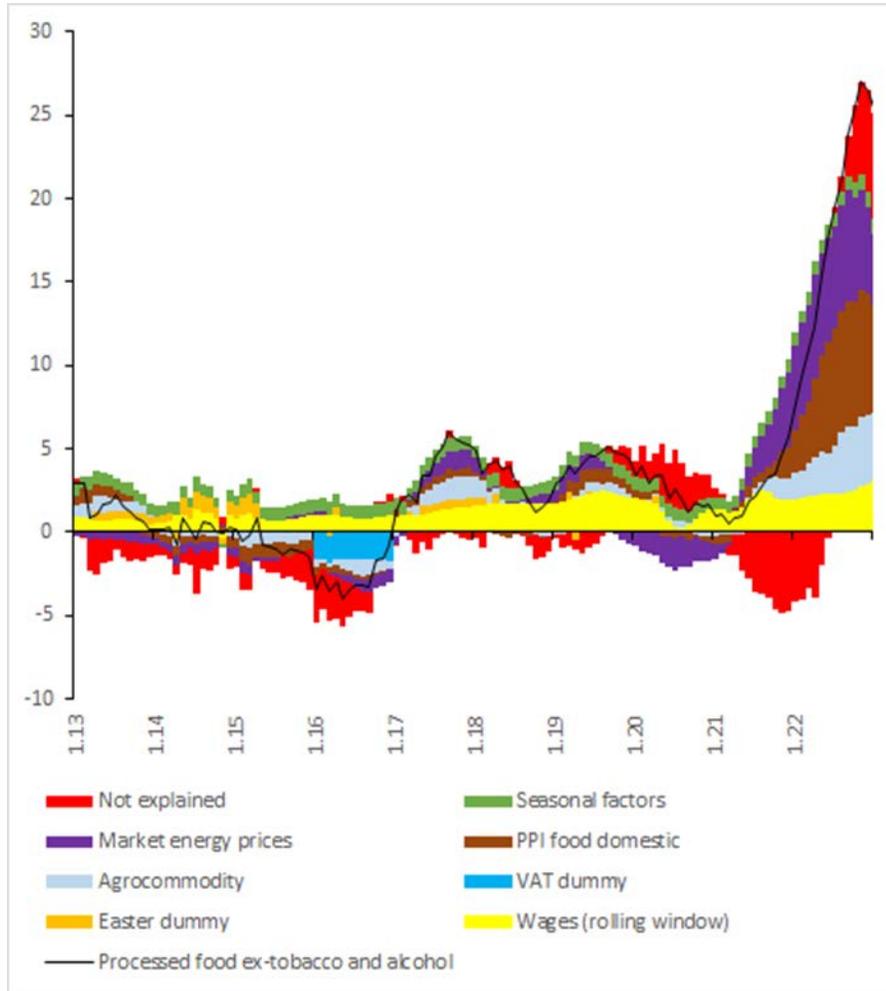
Net inflation breakdown (% p.p.)



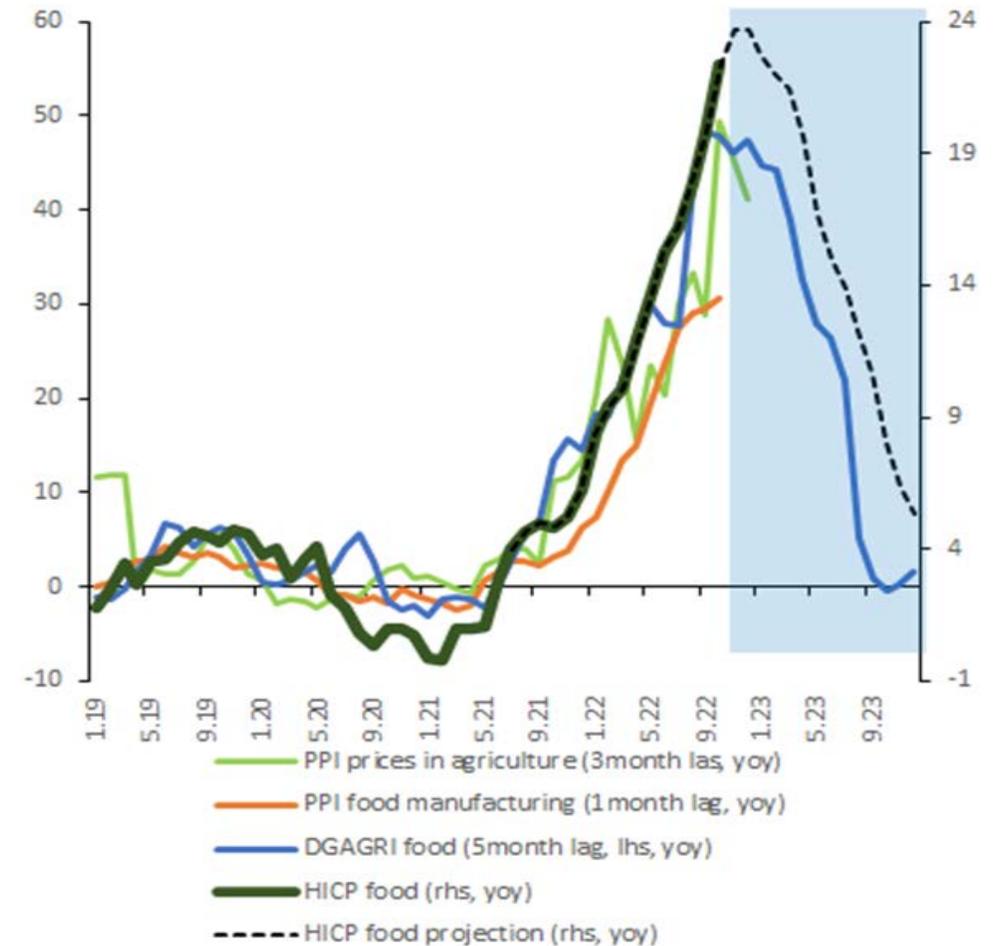
Goods vs services inflation (in %)



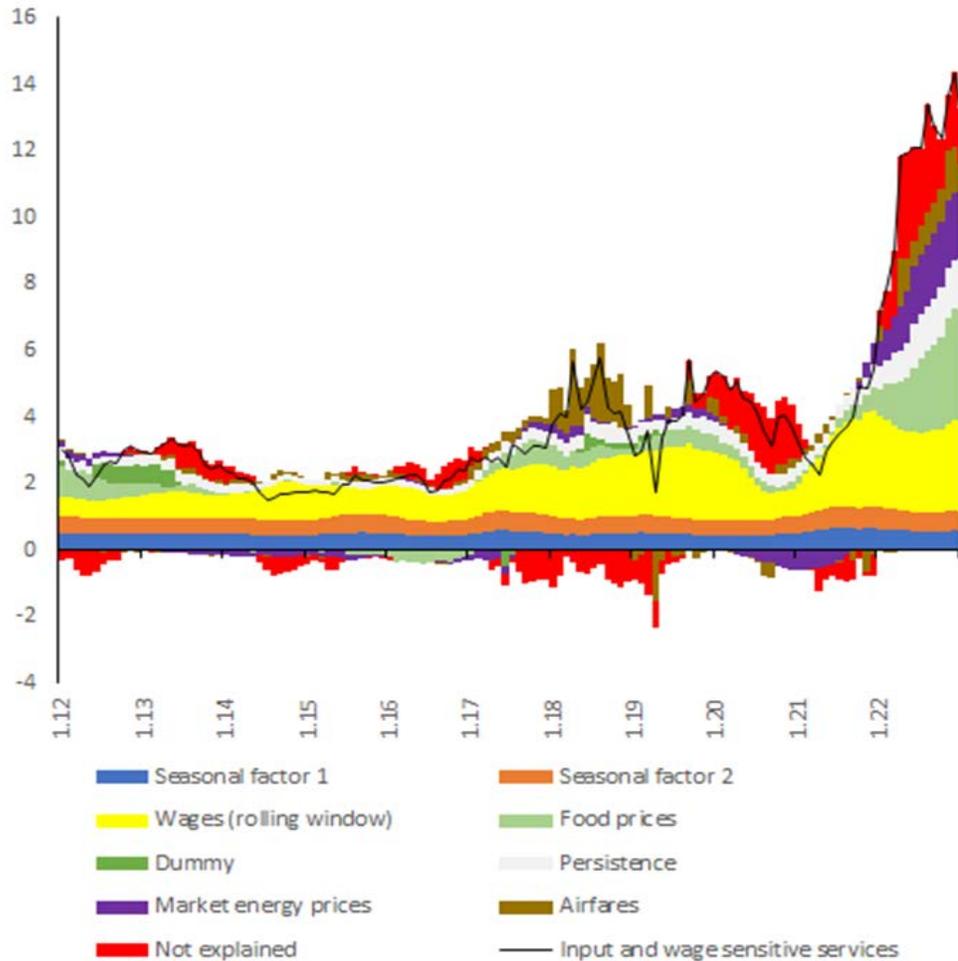
Food inflation breakdown (% p.p.)



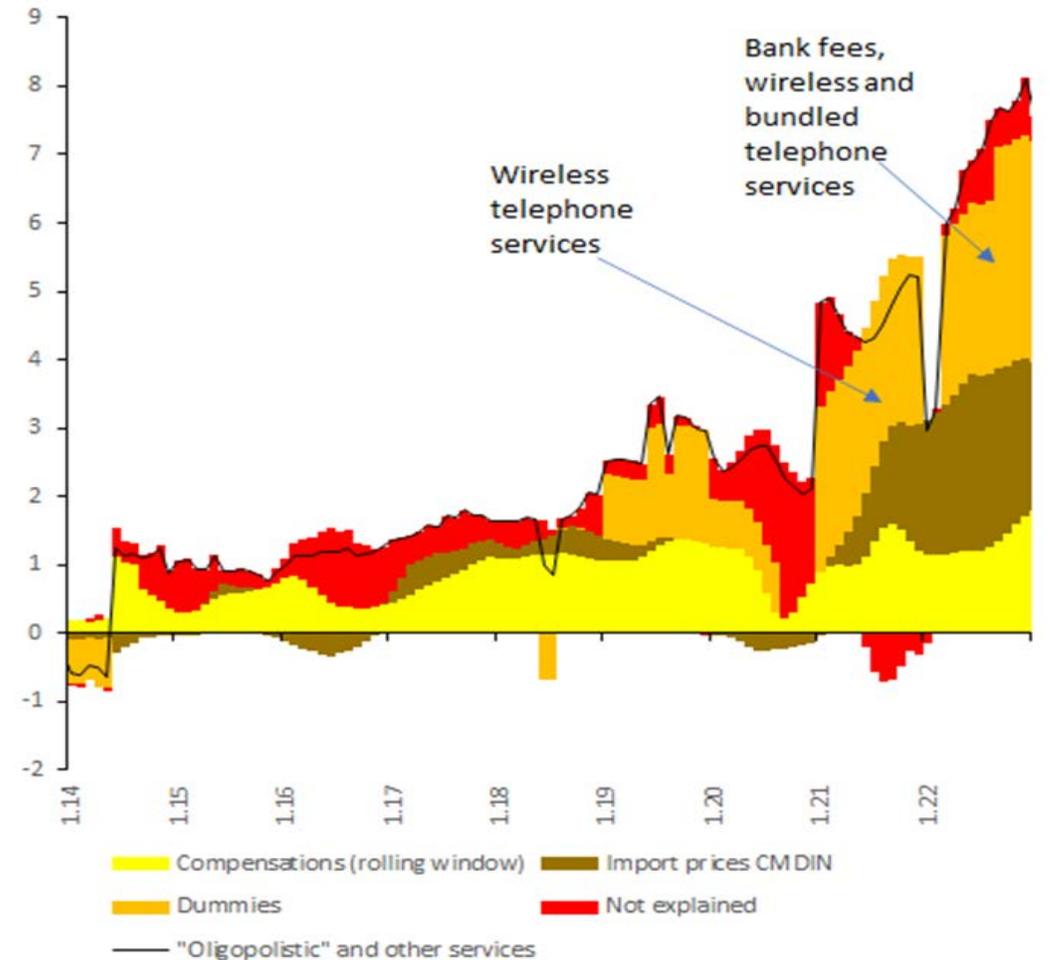
Food production chain prices (in %)



Net services (ex-AP) - cost sensitive (% , p.p.)



Net services (ex-AP) - "oligopolistic" (in % , p.p.)



NEIG inflation affected mainly by higher import prices and domestic energy costs

NEIG inflation (% p.p.)

