

# **Regional analysis**

# **Inflation**

## **Inflation – Two Sides Of The Same Coin**

**Authors:**

Andrej Knez, Chief Markets Analyst

Ivan Odrčić, Lead Financial Markets Analyst

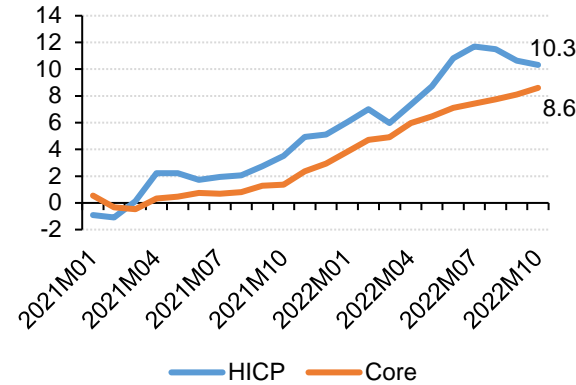
# Highlights – Inflation

Annual inflation rate in October gained pace across the region, bar Slovenia, where it mildly slowed, and averaged around 15%. At the same time, core inflation rate (as treated by Bloomberg Adria, see note below the graphs on the right) averaged around 13% (data for Bosnia unavailable), hence slowly but surely creeping to headline rate. The key highlight remains that apparently there is still enough domestic demand to allow for further price increases, especially in case of core categories.

On a country specific level, annual HICP inflation rate in **Croatia** returned to a record-level of 12.7%, last seen in this year's July and after stagnating in the previous two months at 12.6%. Considering the significance in the overall index, the annual growth of consumer prices was primarily influenced by the increase in prices in the categories of Food and non-alcoholic beverages by +19.4% (+4.2 percentage points in total price growth), followed by Housing, water, electricity, gas and other fuels by +16.4% (+2.0 pp, considering the higher prices of gas and electricity for households) and Restaurants and hotels by +18.1% (+1.9 pp, which is largely the result of an extremely good tourist season, i.e. stronger foreign demand). Compared to September, prices increased by 1.0%, with the single strongest contribution coming from a 6.9% increase in the prices of Clothing and footwear, which is usually affected by the seasonal factor, i.e. the arrival of new collections after the summer period. The stagnation of Transport prices on a monthly level and the annual slowdown of growth for the fourth month in a row suggest a gradual but evident departure from the extreme pressure of energy costs, under which consumers are burdened. On the other hand, the monthly increase in the prices of Food and non-alcoholic beverages by 1.1% cancelled out the positive effects regarding the stabilization of global prices of agricultural products, which spilled over into the monthly drop in the prices of food and non-alcoholic beverages during September, and thus significantly nullified the influence of state aid measures (primarily in the form of freezing the prices of certain food items). The core inflation rate remained the same in September, i.e. it stood at +11.7% yoy and it was slightly short of a record-high level of 11.8% yoy seen in this year's August.

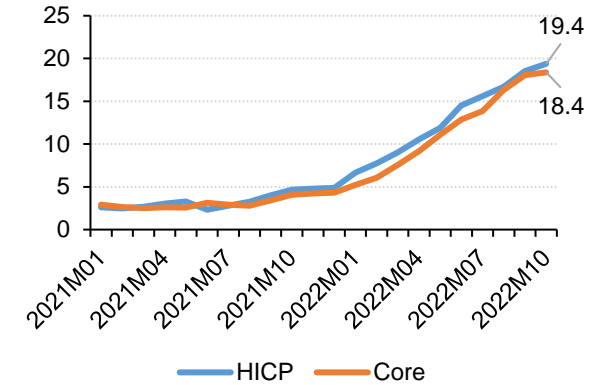
**SI HICP and Core HICP, yoy % ch.**

Source: Eurostat



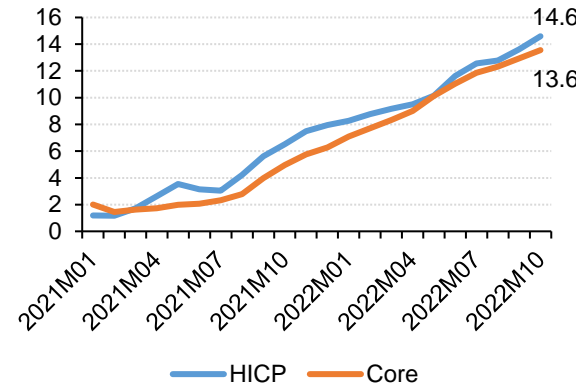
**MK HICP and Core HICP, yoy % ch.**

Source: Eurostat



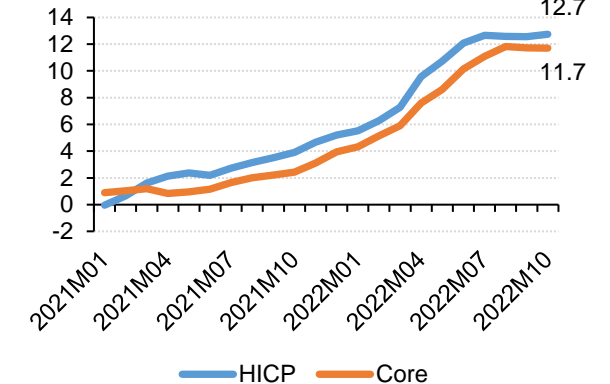
**RS HICP and Core HICP, yoy % ch.**

Source: Eurostat



**HR HICP and Core HICP, yoy % ch.**

Source: Eurostat



To track core CPI trends, Bloomberg Adria uses Eurostat's standard as follows: total HICP inflation minus energy prices (because they are more or less highly volatile in our environment and subject to administrative regulation) and seasonal food prices.

# Highlights – Inflation

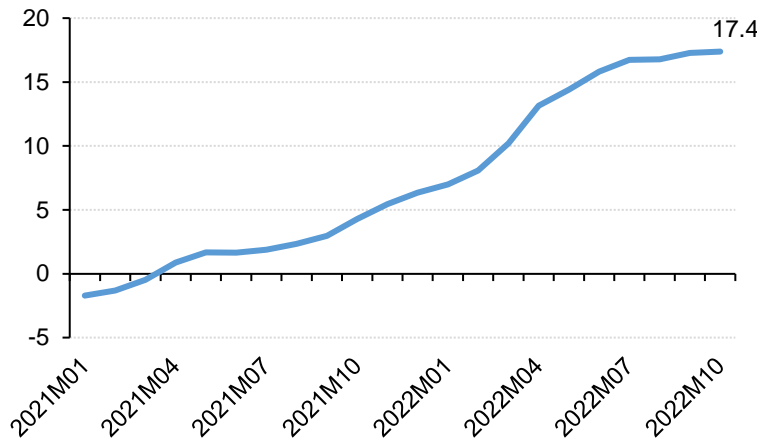
The annual inflation rate in **Bosnia and Herzegovina** accelerated to a record-level of 17.4% in October 2022 (vs. 17.3% yoy in September). The strongest contribution to the overall increase in prices at the annual level came from the 27.3% higher food prices, which is in line with the lack of more important state aid measures for the population, especially considering the globally stabilizing situation regarding food prices. If we look at the monthly level, where consumer prices increased by 2.1% (the highest since the this year’s April), the strongest increase was recorded in the category Housing, water, electricity, gas and other energy products (+8.3%) or more precisely, a 10.5% increase in electricity, gas and other energy sources, which is not surprising given the increase in gas prices for many households during October. The costs of food and energy alone will continue to be the main drivers of overall price growth for consumers in the coming period, all the more so since further increases in gas and electricity prices for households are expected from the New Year.

In **Serbia**, inflation accelerated its pace for the fifteenth month in a row, reaching an almost record level of 14.6% yoy (the previous highest value of 14.7% was recorded in April 2008), being up from September’s 13.6% yoy value. Dominant contributors to headline increase were rising Food and non-alcoholic beverages and Housing, water, electricity, gas and other fuels prices (+23.0% and +17.2% yoy, respectively). Government of Serbia will also try to contribute to calming the rise in prices (the other subject being NBS, with its key policy rate hikes), specifically energy costs for households, by introducing discounts on electricity bills (starting with October, for the bills coming in November), where each household will see subsidies to electricity bills if they reduce energy usage. Households also benefit from the fact that a slightly milder winter has been announced in the entire region, so the overall effects of the specific measure should be even greater. The core inflation rate, meanwhile, sped to +13.6% yoy, i.e. slightly short of a record, 13.7% increase seen in June 2008.

**Slovenia’s** case is unlike rest of the region, as the inflationary pressures softened for the third month in a row, amounting to 10.3% yoy, largely on the back of softer Transport prices increase vs a month before (+10.4% vs +15.8% in September). More precise, significantly softer growth in the prices of automotive fuels (+13.1% vs +27.3% in September), given the higher base last year, with the further slowdown of fuel prices expected for November, as the Government regulated prices of fuels outside the motorways and expressways areas. As regards core inflation rate, it accelerated to +8.6% yoy (previous high, of 8.7%, was last seen in August 2002).

HICP inflation in **North Macedonia** sped to a record-high of 19.4% yoy (the largest rate in the region), mainly due to stronger growth of vegetables (+22.2% vs +12.6% in September) and lack of government aids for high prices. Aside from the NBRNM’s (National Bank of the Republic of North Macedonia) attempts to tackle high inflation with its rate hiking programme, additional support will come from recently IMF-approved two year arrangement under the Precautionary and Liquidity Line (PLL) in the amount of SDR 406.87 mln (about € 530mln). Core inflation rate, at the same time, reached a record level of 18.4% yoy.

**BH CPI, yoy % ch.**  
Source: BHAS



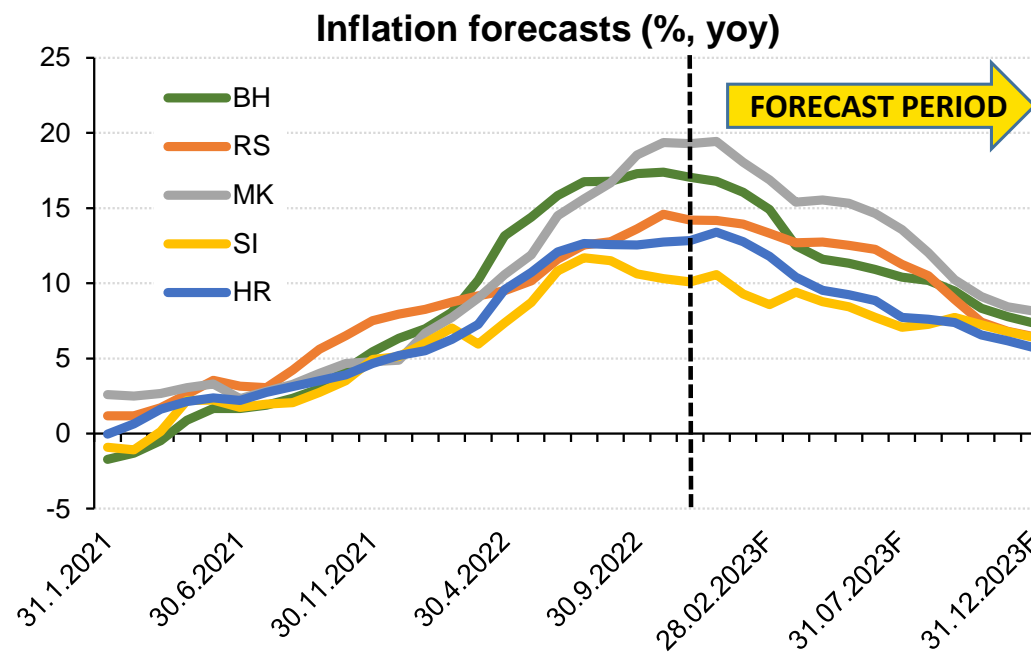
As regards inflation outlook, we see a turning point in 4Q2022-1Q2023, with the serious slowdown in inflationary pressures happening in the second part of 2023, driven by base effect, monetary policy rate hikes influence, food and energy prices softening (even though this year Governments across the region subsidised costs for end-users and those subsidies are expected to fade as soon as Spring 2023) and dampened demand (as full blown overall economic activity around the globe makes an impact). One serious unknown for the next year, however, remains geopolitical uncertainty, which can significantly alter actual inflation outcome in the year ahead and beyond.

All told, we see **Adria region annual inflation rate averages in range of 8-13% in 2023**, with Slovenia and Croatia at the lower end of distribution, while North Macedonia runs at the top of the projected area. Also important – we see the targeted **2% mark for inflation rates reaching only somewhere in 2025**.

**We see interest rates on the money market going further up**, with the private sector interest rates following suit. These are **the key arguments** behind our view:

- 1) **ECB** – we see the **Eurozone’s monetary authority hiking the rates by additional 75bps**, with the hiking cycle likely to end in 1H 2023. The reason for further policy tightening lies in the need to contain the mid-term inflation expectations, with the CPI inflation expected to fall within the medium target of below 2% only in 2025.
- 2) **NBS** – we see **Serbian central bank hiking rates by an extra 100bps over course of next six months** with inflation to peak only during 4Q22-1Q23 and ongoing spillovers from the headline inflation onto the core categories. The ECB’s policy tightening will also generate some transmission into the local financial system given the magnitude of the euroization in Serbian economy.
- 3) **NBRNM** – we see **NBRNM hiking rates by an additional 100bps in the next six months** amid an ongoing fight against persistently high inflation and need to safeguard the stability of the EUR/MKD dirty float regime.

FORECASTS			
Averages (%)	2022	2023	2024
Croatia	10.7	8.6	4.1
Slovenia	9.2	7.9	4.1
B-H	14.2	10.9	5.3
Serbia	11.6	10.7	4.9
N. Macedonia	14.1	13.1	5.3



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## **Bloomberg Adria Team Analytics**

**Andrej Knez, Chief Markets Analyst**  
andrej.knez@bloombergadria.com

**Ivan Odrdic, Lead Financial Markets Analyst**  
ivan.odrcic@bloombergadria.com

**Ratko Guduric, Senior Markets Analyst**  
ratko.guduric@bloombergadria.com

**Jelena Zindovic, Senior Corporate Finance Analyst**  
jelena.zindovic@bloombergadria.com

**Matteo Mosnja, Corporate Finance Analyst**  
matteo.mosnja@bloombergadria.com

**Ilija Nestic, Corporate Finance Analyst**  
ilija.nestic@bloombergadria.com

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