

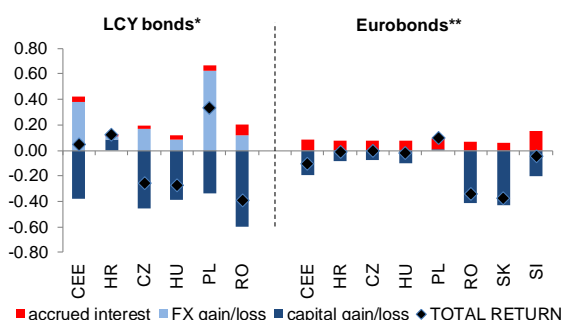
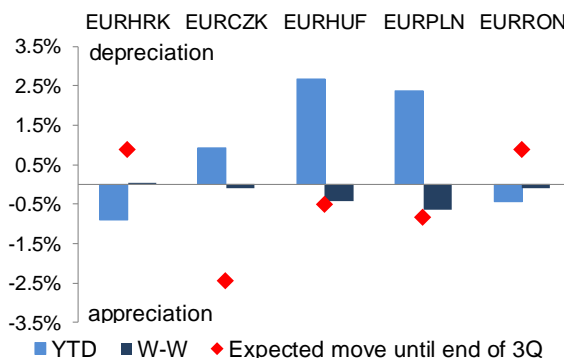


CEE Market Insights

Market outlook

At the end of last week, CEE currencies lost almost all of the gains recorded against the euro in the first half of the week. This may have been due to the market rumors that this Thursday should be D Day, when the ECB will announce the end-date of QE (December). The somewhat weaker Czech koruna is creating worries for some MPC members of the Czech National Bank, who stressed that, if the koruna stays at a weaker level, it may affect the next inflation projection, implying a need to deliver a rate hike earlier than planned. We still see a rate hike in November as the most likely scenario, but the probability of an earlier hike (i.e. in August) has recently climbed above 40%.

Yields went up across Europe last week (including Germany), in anticipation of the announcement of more details on the QE exit by the ECB after its meeting at the press conference this Thursday. Hungarian 10Y yields are close to 3.2% and Polish 10Y are above 3.3%. Croatia and Slovakia made a smart move and went to international markets at the beginning of last week with long-dated papers, which enjoyed hefty demand. The Romanian 30Y Eurobond deal (USD 1.2bn) is still running, but given that it is denominated in USD, it should be less affected by the ECB announcement.



Looking ahead this week:

Monday	Tuesday	Wednesday	Thursday	Friday
SK: Industry RO: Trade Balance, Wages CZ: CPI	RO: Industry, CPI RS: CPI	RO: Current Account SK: Wages PL: Trade Balance	SK, PL: CPI	HR: CPI

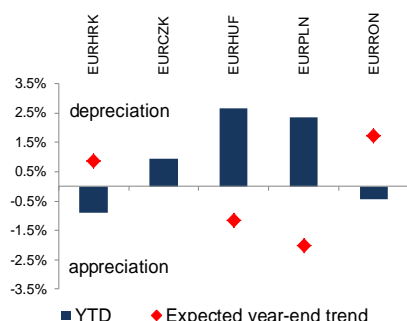
This week will be mainly about May inflation readings and the ECB meeting, at which many market participants expect more details on the QE exit. That is probably the reason why few CEE countries hurried up to tap international markets with long-dated papers last week. Poland has already published its flash estimate for May at 1.7% and we do not expect any revision. In Romania, inflation should stay at 5.2%, which we consider the peak level for this year. In the second half, we expect inflation to ease towards 3.7% (by year-end). In the Czech Republic, inflation is to move back above the target, to 2.1%, from April's 1.9%. Besides the strong wage growth and still relatively weak koruna, inflation is another reason why the probability of an earlier hike (in 3Q) has increased. Inflation rates should go up in Croatia and Serbia, but 1.6% inflation (in both countries) is seen as a normalization rather than anything alarming. On the political front, it will be interesting to follow the situation in the Czech Republic, where new PM Babis will try to finalize the talks with the other parties and form a new government, which should ask for a vote of confidence later this month. The coalition talks in Slovenia do not seem to be an easy task and may require more time.

In case you missed it last week...

- Croatia, Slovakia and Romania tapped international market with long-dated bonds
- As expected, Polish and Serbian central banks left rates unchanged
- 1Q GDP growth in Slovakia and Hungary confirmed; investments contributed strongly
- Wage growth surprised on upside in Czechia (+8.6% y/y in 1Q); MPC members call for hikes
- Largest coalition party in Slovak government announced EUR 200mn spending package

FX and bond market stable in CEE

YTD change on FX market



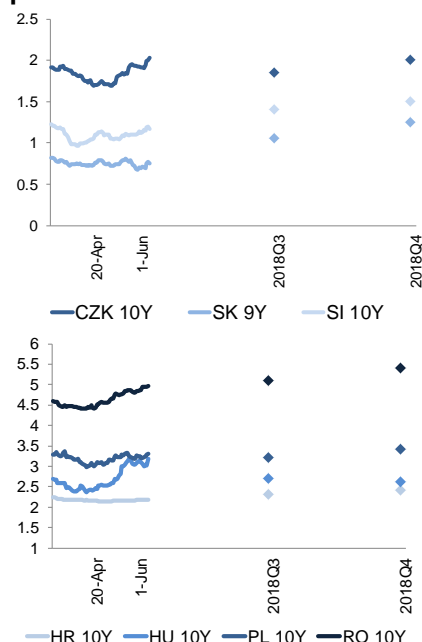
On global markets:

This week is set to be eventful and could trigger higher EURUSD volatility. Both monetary policy-setting bodies of the US Federal Reserve and the ECB will meet. For the US, an interest rate hike is all but certain, but a new survey of board members and reserve bank presidents concerning the interest rate outlook has introduced some uncertainty. The ECB should decide on the fate of the asset purchase program after September next week and might give the markets new guidance on its future course. In addition, inflation and retail sales figures for the US are scheduled.

CEE currencies:

The volatility of CEE currencies could increase this week, given the many uncertainties related to the ECB's decision on the QE exit and the FED's new interest rate outlook. A higher global interest rate environment could put some downward pressure on CEE currencies, with the Czech National Bank potentially the first to react and deliver its rate hike earlier than planned (i.e. in August). The HUF, as the CEE currency with the lowest implied interest rates in the region, could face a temporary sell-off.

10Y government bond yields, percent



Source: Erste Group Research, Bloomberg.

CEE rates and yields:

The week before the crucial ECB meeting, at which the bank is expected to announce more details on the QE exit, several CEE countries used the window of opportunity and tapped the international debt market with the offer of long-dated hard currency bonds. Croatia issued a 10Y Eurobond denominated in EUR in a volume of EUR 750mn at mid-swap +190bp. The paper was well-demanded (the order book was EUR 2.7bn) and the final pricing went well below the initial guidance (mid-swap +220bp). The proceeds are intended to finance the redemption of a Eurobond maturing in July. Slovakia raised EUR 1.5bn last week via the offer of new 10Y and 50Y benchmarks (the longest paper at this moment in CEE) priced at mid-swap +10bp and +80bp, respectively. These papers were also highly in demand and the combined order book went to EUR 5bn. Romania's Ministry of Finance, which had to face dented demand for RON papers and thus higher yields on the domestic market, initiated a switch transaction on the USD-denominated Eurobonds maturing in 2022. Debt managers are also planning a new 30-year USD bond, taking advantage of the flat USD yield curve.

Calendar

Time	Country	Indicator	Period	Survey	Erste Est.	Prev.	Pre Comment
11-Jun							
	SK	Industrial Production (y/y)	Apr		6.0%	-2.3%	<i>Industrial production likely to have picked up somewhat, aided by last year's very low base, despite lower number of working days this year.</i>
8:00	RO	Trade Balance	Apr			-1056.7	
8:00	RO	Wages (y/y)	Apr			15.5%	
9:00	CZ	CPI (y/y)	May	2.1%		1.9%	
9:00	CZ	CPI (m/m)	May	0.3%		0.3%	
12-Jun							
8:00	RO	Industrial Production (y/y)	Apr		7.8%	4.1%	<i>Possible acceleration of industrial production based on higher new orders in manufacturing.</i>
8:00	RO	CPI (y/y)	May	5.4%	5.2%	5.22%	<i>Annual inflation at multi-year highs at present, mainly due to factors outside NBR control.</i>
8:00	RO	CPI (m/m)	May		0.3%	0.54%	<i>Higher fuel price was key pro-inflationary factor in May.</i>
12:00	RS	CPI (y/y)	May		1.6%	1.1%	<i>Base effect gradually fading out.</i>
12:00	RS	CPI (m/m)	May			0.4%	
13-Jun							
	RO	Current Account Balance	Apr			-967	
9:00	SK	Wages (y/y)	Apr			4.4%	
14:00	PL	Trade Balance	Apr	-51		-317	
14-Jun							
9:00	SK	CPI (y/y)	May		2.8%	2.9%	<i>Inflationary pressures thought to have eased slightly in May.</i>
9:00	SK	CPI (m/m)	May		0.1%	0.6%	<i>Small monthly change in consumer price index expected.</i>
10:00	PL	CPI (y/y)	May F			1.7%	<i>Flash expected to be confirmed</i>
10:00	PL	CPI (m/m)	May F			0.1%	
15-Jun							
11:00	HR	CPI (y/y)	May		1.6%	1.3%	<i>Inflation expected to remain in narrow band in May.</i>
11:00	HR	CPI (m/m)	May			0.7%	

Sources: Bloomberg, Reuters

Capital market forecasts

Government bond yields					
	current	2018Q3	2018Q4	2019Q1	2019Q2
Croatia 10Y	2.17	2.30	2.40	2.50	2.50
spread (bps)	174	154	148	145	136
Czech Rep. 10Y	2.03	1.85	2.00	2.08	2.15
spread (bps)	160	109	108	103	101
Hungary 10Y	3.18	2.70	2.60	2.70	2.70
spread (bps)	275	194	168	165	156
Poland 10Y	3.31	3.20	3.40	3.50	3.50
spread (bps)	288	244	248	245	236
Romania10Y	5.16	5.10	5.40	5.40	5.60
spread (bps)	473	434	448	435	446
Slovakia 9Y	0.76	1.05	1.25	1.45	n.a.
spread (bps)	33	29	33	40	n.a.
Slovenia 10Y	1.17	1.40	1.50	1.60	1.70
spread (bps)	73	64	58	55	56
Serbia 5Y	3.81	4.00	4.00	4.20	4.20
DE10Y (BBG)*	0.43	0.76	0.92	1.05	1.14

3M Money Market Rate					
	current	2018Q3	2018Q4	2019Q1	2019Q2
Croatia	0.49	0.50	0.50	0.60	0.70
Czech Republic	0.92	0.97	1.11	1.19	1.34
Hungary	0.12	0.08	0.05	0.05	0.10
Poland	1.70	1.73	1.73	1.73	1.73
Romania	2.89	2.70	2.75	2.80	2.80
Serbia	2.88	3.00	3.00	3.00	3.25
Eurozone	-0.32	-0.30	-0.30	-0.30	-0.10

FX					
	current	2018Q3	2018Q4	2019Q1	2019Q2
EURHRK	7.38	7.45	7.50	7.45	7.30
forwards		7.38	7.38	7.38	7.38
EURCZK	25.77	25.14	24.96	24.78	24.65
forwards		25.80	25.80	25.80	25.80
EURHUF	319.6	317.0	315.0	315.0	315.0
forwards		322.8	322.8	322.8	322.8
EURPLN	4.28	4.24	4.21	4.19	4.19
forwards		4.28	4.28	4.28	4.28
EURRON	4.66	4.70	4.73	4.74	4.75
forwards		4.66	4.66	4.66	4.66
EURRSD	118.1	118.0	118.0	118.5	118.5
forwards		-	-	-	-
EURUSD	1.18	1.14	1.13	1.16	1.16

Key Interest Rate					
	current	2018Q3	2018Q4	2019Q1	2019Q2
Croatia	0.30	0.30	0.30	0.30	0.30
Czech Republic	0.75	0.75	1.00	1.00	1.25
Hungary	0.90	0.90	0.90	0.90	0.90
Poland	1.50	1.50	1.50	1.50	1.50
Romania	2.50	2.75	2.75	2.75	2.75
Serbia	3.00	3.00	3.00	3.00	3.25
Eurozone	0.00	0.00	0.00	0.00	0.00

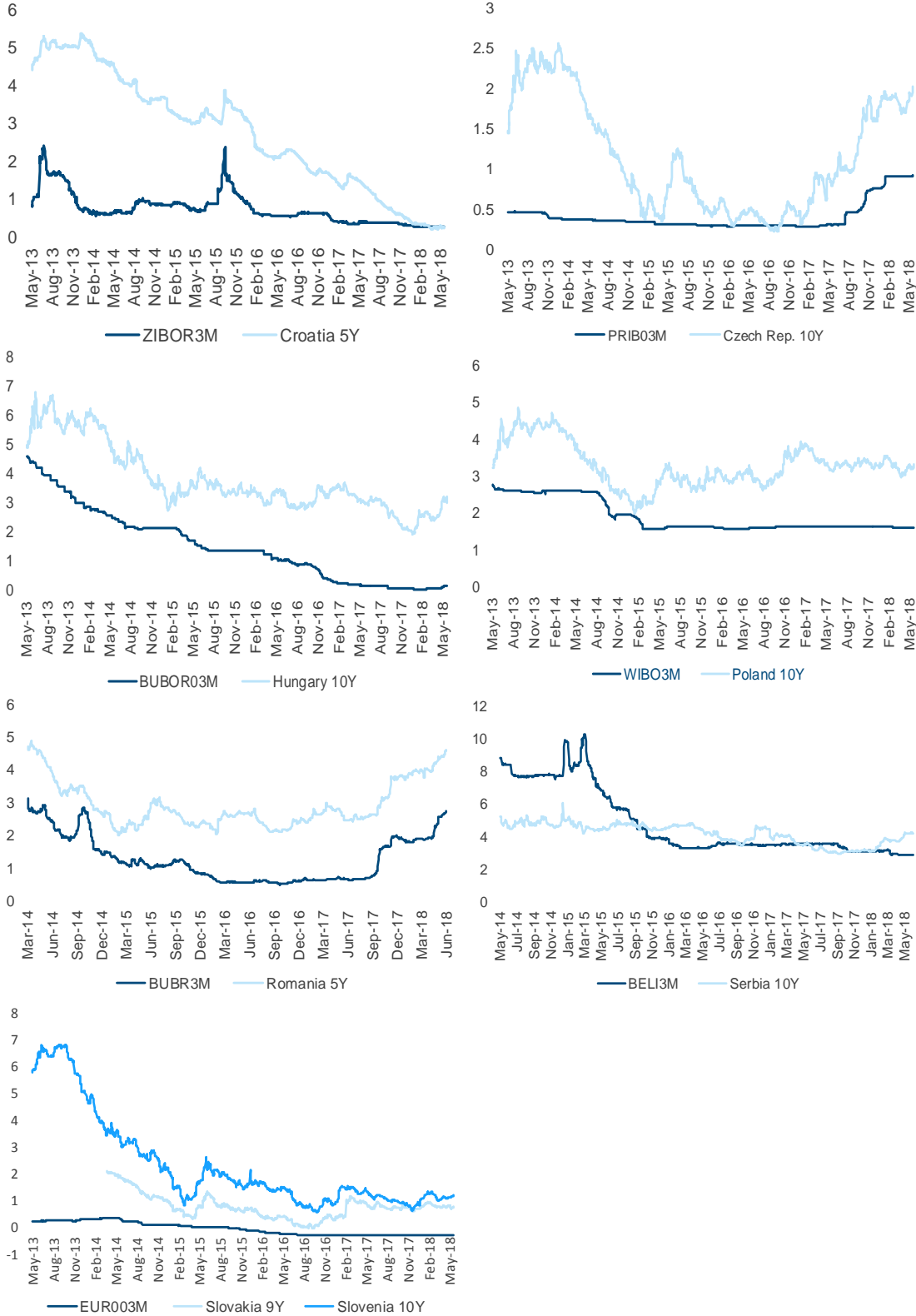
Macro forecasts

Real GDP growth (%)					Average inflation (%)					Unemployment (%)				
	2016	2017	2018f	2019f		2016	2017	2018f	2019f		2016	2017	2018f	2019f
Croatia	3.5	2.9	2.8	2.7	Croatia	-1.1	1.1	1.5	2.0	Croatia	13.1	11.3	10.1	9.2
Czech Republic	2.5	4.6	3.6	3.1	Czech Republic	0.7	2.5	2.1	2.0	Czech Republic	3.6	2.9	2.3	2.5
Hungary	2.2	4.0	4.0	3.5	Hungary	0.4	2.4	2.6	3.5	Hungary	5.1	4.2	3.9	3.9
Poland	2.9	4.6	4.2	3.3	Poland	-0.6	2.0	1.7	2.2	Poland	8.9	7.2	6.5	6.7
Romania	4.8	6.9	4.1	3.0	Romania	-1.5	1.3	4.6	2.8	Romania	5.9	4.9	4.9	5.0
Serbia	2.8	1.9	3.5	3.2	Serbia	1.6	3.0	1.8	3.2	Serbia	15.3	13.2	11.6	11.1
Slovakia	3.3	3.4	3.9	4.2	Slovakia	-0.5	1.3	2.4	2.3	Slovakia	9.6	8.1	7.2	6.6
Slovenia	3.1	5.0	4.5	3.7	Slovenia	-0.1	1.4	2.0	2.0	Slovenia	8.0	6.6	5.9	5.4
CEE8 average	3.1	4.7	4.0	3.3	CEE8 average	-0.4	1.9	2.4	2.4	CEE8 average	7.6	6.2	5.6	5.6

Public debt (% of GDP)					C/A (%GDP)					Budget Balance (%GDP)				
	2016	2017	2018f	2019f		2016	2017	2018f	2019f		2016	2017	2018f	2019f
Croatia	80.2	77.5	74.1	70.9	Croatia	2.6	3.9	2.6	1.7	Croatia	-0.9	0.8	0.0	-0.5
Czech Republic	36.8	33.9	31.9	30.4	Czech Republic	1.1	1.3	0.6	0.5	Czech Republic	0.7	0.6	0.2	0.2
Hungary	76.0	73.6	72.5	71.1	Hungary	6.0	2.9	2.1	1.9	Hungary	-1.7	-2.0	-2.5	-2.5
Poland	54.2	50.6	50.2	49.7	Poland	-0.3	0.3	-0.3	-0.9	Poland	-2.4	-1.5	-2.3	-2.2
Romania	37.4	35.0	34.8	36.4	Romania	-2.1	-3.4	-4.0	-4.4	Romania	-3.0	-2.9	-3.4	-2.9
Serbia	71.9	61.3	58.7	55.6	Serbia	-4.2	-4.7	-5.3	-6.6	Serbia	-1.3	1.2	-0.5	-0.5
Slovakia	51.8	50.9	49.7	47.2	Slovakia	-1.5	-2.1	-1.0	-0.4	Slovakia	-2.2	-1.0	-1.0	-0.6
Slovenia	78.3	71.9	69.3	65.7	Slovenia	5.2	6.4	6.4	5.7	Slovenia	-1.8	0.0	0.2	0.5
CEE8 average	53.5	50.2	49.0	48.0	CEE8 average	0.4	0.2	-0.3	-0.7	CEE8 average	-1.8	-1.2	-1.8	-1.6

Note: *Information on past performance is not a reliable indicator for future performance. Forecasts are not a reliable indicator for future performance.

Appendix



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11 June 2018

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