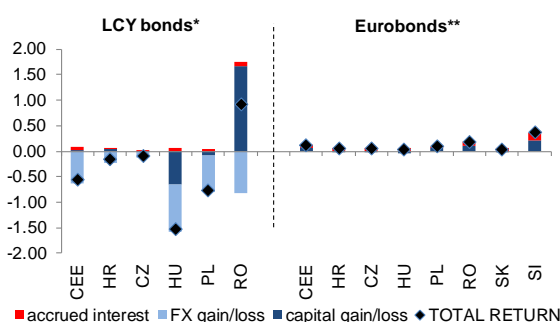
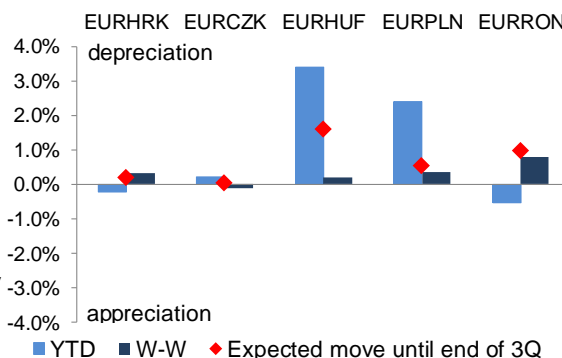


# CEE Market Insights

## Market outlook

The Turkish situation took its toll on CEE FX markets towards the end of last week, after the somewhat uneventful days earlier last week. If international sentiment, which is currently poisoned by the Turkish woes, worsens further, CEE currencies could also decline to the extent seen towards the end of last week. Fundamentally speaking, however, CEE currencies are not very mispriced at the moment. In the absence of any further deterioration in international sentiment, the Czech koruna should actually appreciate, while the Romanian leu should moderately decline, but external news seem more important for short-term developments at the moment.

In Romania, the possibility of a no-change scenario increased after the NBR kept rates unchanged last week and the inflation print came in below expectations. We think that there is now a lower chance that the NBR will hike than not this year. As for the Czech Republic, with core inflation admittedly being above the expectations of the central bank in July, we see the chances of the CNB delivering another rate hike at the next monetary meeting in late September as increasingly likely. In Hungary, rates-markets are again climbing up, while 10Y government bond yields also increased. Although Hungary seems to be sticking to a rather loose monetary policy, the MNB said earlier that it does not see loose policy to be maintained at current levels in the relevant 5-8 quarter horizon, while Hungary's current and capital account position is also very strong and one of the best in the region.



## Looking ahead this week:

Monday	Tuesday	Wednesday	Thursday	Friday
<b>RO:</b> Current Account Balance <b>PL:</b> Trade Balance <b>RS:</b> CPI	<b>CZ, RO, HU, SK, PL:</b> GDP <b>SK, PL:</b> CPI		<b>RS:</b> Current Account Balance <b>CZ:</b> PPI	<b>SK:</b> Unemployment Rate <b>PL:</b> Wages <b>HR:</b> CPI

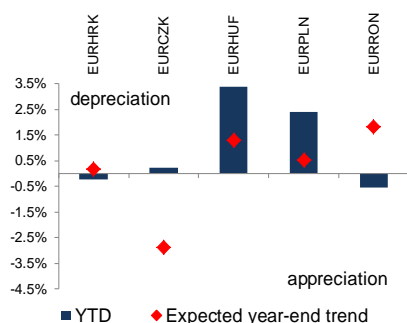
The week ahead is packed with important releases. Tuesday will bring 2Q18 GDP releases, which could show a rather healthy expansion of growth everywhere, mostly driven by domestic consumption, albeit external trade data (especially released last week in Hungary and in Slovakia) could indicate supportive power from the export side too. We see growth ranging between 5.0% in 2Q18 in Poland, to 2.5% in the Czech Republic, with Romania at 3.8%, Slovakia at 4.0%, and Hungary at 4.1%. The Czech figure might seem low at first, but its mainly due to the very high base (in 2Q17, q/q growth was as high as 2.3%). We will see Polish, Slovak, Serbian and Croatian inflation too for June, which should be close to previous readings in July.

## In case you missed it last week...

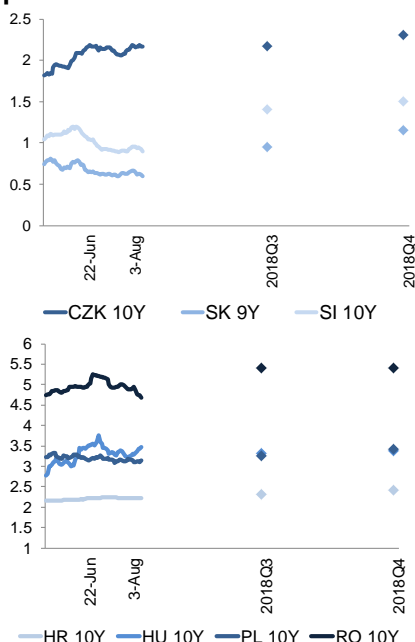
- **SI:** Fitch kept rating of Slovenia unchanged at 'A-' with stable outlook
- **RS:** NBS kept policy rate unchanged at 3.0%, as expected
- **SK:** Ministry of Labor proposed 8.3% minimum wage hike, from EUR 480 to EUR 520, from January 2019
- **SI:** Marjan Sarec was nominated as PM-designate to lead minority government
- **HU:** Vice-Governor Nagy said Hungary should get upgrade from 'BBB-'; S&P is to decide this Friday

## FX and bond market stable in CEE

### YTD change on FX market



### 10Y government bond yields, percent



Source: Erste Group Research, Bloomberg.

### On global markets:

Last Thursday and Friday were all about Turkish developments, which had a notable negative spillover effect on global markets too. After the lira fell by an eye-popping 11-12% vs. the US dollar in just one and a half days, President Erdogan suggested on Friday afternoon that an 'effective response to the West' would be to exchange dollars and gold held 'under the pillow' into Turkish liras, while he also stressed that the country 'will not surrender to economic hitmen'. After the words of Erdogan and US President Trump's tweet that he will increase tariffs further on Turkish steel and aluminum products, the currency took a further beating, meaning another roughly 9-10% decline in just a matter of hours. In the meantime, the ECB gave out a warning that some banks in the Euro Area might be exposed if Turkey's position worsens further, although also saying that the situation is not yet critical. As the premier seems to be sticking to the notion that Turkey should not change its economic policy, it is difficult to see what could stop the ongoing deterioration, although the extent of decline in the lira is very extreme and (in normal circumstances) would call for a correction.

### CEE currencies:

Currencies in the region were rather stable, or even appreciating, at the beginning of the week, with the exception of the Romanian leu, which gave up some of the gains from previous weeks after the NBR decided not to hike the policy rate. Later last week, however, the developments of the Turkish lira took their toll on CEE markets too. As CEE fundamentals are not comparable to those of Turkey, the market contagion effect was modest. If international sentiment, which is currently poisoned by the Turkish woes, worsens further, CEE currencies could also decline slightly. Fundamentally speaking, CEE currencies are not very mispriced at the moment. Thus, in the absence of any further deterioration in global sentiment, the Czech koruna should actually appreciate, while the Romanian leu should moderately decline. Still, at present, international factors seem more important for short-term FX moves.

### CEE rates and yields:

Rate developments in the Czech Republic and Romania were going in the opposite direction last week, as expectations for further hikes are still strong for the Czech case, while in Romania, the possibility of a no-change scenario increased after the NBR kept rates unchanged and the inflation print came in below expectations at 4.6% y/y for July. As for the latter, we think that there is now a lower chance that the NBR will hike than not this year. As for the Czech case, with core inflation admittedly being above the expectations of the central bank in July (the data was also released last week), we see the chances of the CNB delivering another rate hike at the next monetary meeting in late September as increasingly likely. Further rate developments are strongly dependent on the koruna as well. If the CZK fails to appreciate after another rate hike, then an additional hike by the end of the year will become increasingly likely as well. As for yields, Hungarian bonds were mostly sold last week, as evidenced by a near-20bp increase of the 10Y yield. 3X6 FRA and 2Y swap markets also started climbing higher recently. Although Hungary seems to be sticking to a rather loose monetary policy, the MNB said earlier that it does not see loose policy to be maintained at current levels in the relevant 5-8 quarter horizon, while Hungary's current and capital account position is also very strong and one of the best in the region.

## Calendar

Time	Country	Indicator	Period	Survey	Erste Est.	Prev.	Pre Comment
<b>13-Aug</b>							
	RO	Current Account Balance	Jun		-1	-3018	Pressure from widening trade balance on goods segment and limited increase in surplus of services could be counterbalanced by higher inflows of EU subsidies
12:00	RS	CPI (y/y)	Jul		2.5%	2.3%	We expect that CPI will continue to gradually move towards mid of target band, supported by stronger demand, wage pressure and seasonal effects
12:00	RS	CPI (m/m)	Jul			0.4%	
14:00	PL	Trade Balance	Jun	-78		98	
<b>14-Aug</b>							
8:00	RO	GDP (q/q)	2Q A	1.5%	1.2%	0.1%	Rebound in economic growth in q/q terms in 2Q18 after series of one-offs that affected economic activity in 1Q18
8:00	RO	GDP (y/y)	2Q A	4.2%	3.8%	4.0%	Slower economic growth compared with corresponding quarter from 2017
9:00	CZ	GDP (q/q)	2Q A	0.8%	0.7%	0.5%	Development of real economic activity remained solid in 2Q, due to both domestic and foreign demand
9:00	CZ	GDP (y/y)	2Q A	2.8%	2.5%	4.2%	We expect GDP growth in y/y terms to slow down in 2Q; besides higher rates and stronger koruna, this development is affected by strong growth in 2Q17
9:00	HU	GDP (q/q)	2Q P	0.8%	0.0%	1.2%	
9:00	HU	GDP (y/y)	2Q P	4.0%	4.1%	4.4%	2Q18 GDP figures could have been driven by rising internal demand
9:00	SK	CPI (y/y)	Jul	2.7%		2.8%	
9:00	SK	CPI (m/m)	Jul	-0.1%		0.1%	
9:00	SK	GDP (y/y)	2Q P	3.7%	3.6%	3.6%	We expect flash estimate to be confirmed, with growth driven mostly by household consumption and investment
10:00	PL	CPI (y/y)	Jul F		2.0%	2.0%	We expect flash to be confirmed at 2.0% y/y
10:00	PL	CPI (m/m)	Jul F			-0.1%	
10:00	PL	GDP (y/y)	2Q P	5.0%	5.0%	5.2%	Strong retail sales, robust industrial production and construction output growth in 2Q18 show strong growth dynamics
<b>16-Aug</b>							
	RS	Current Account Balance	Jun			52.8	
9:00	CZ	PPI (y/y)	Jul	3.1%	3.2%	2.9%	Increase in labor costs and higher oil prices affected PPI inflation in July, in our view
<b>17-Aug</b>							
	SK	Unemployment Rate	Jul			5.4%	
10:00	PL	Wages (y/y)	Jul	7.6%	7.2%	7.5%	We expect wages to sustain solid growth
11:00	HR	CPI (y/y)	Jul			2.4%	
11:00	HR	CPI (m/m)	Jul				

Sources: Bloomberg, Reuters

## Capital market forecasts

Government bond yields					
	current	2018Q3	2018Q4	2019Q1	2019Q2
<b>Croatia 10Y</b>	2.22	2.30	2.40	2.50	2.50
spread (bps)	189	180	175	166	154
<b>Czech Rep. 10Y</b>	2.17	2.17	2.30	2.32	2.37
spread (bps)	183	167	165	148	141
<b>Hungary 10Y</b>	3.46	3.31	3.36	3.40	3.49
spread (bps)	312	281	271	256	253
<b>Poland 10Y</b>	3.13	3.25	3.40	3.50	3.50
spread (bps)	280	275	275	266	254
<b>Romania10Y</b>	4.69	5.40	5.40	5.40	5.80
spread (bps)	435	490	475	456	484
<b>Slovakia 9Y</b>	0.60	0.95	1.15	1.30	n.a.
spread (bps)	26	45	50	46	n.a.
<b>Slovenia 10Y</b>	0.90	1.40	1.50	1.60	1.70
spread (bps)	56	90	85	76	74
<b>Serbia 5Y</b>	3.68	3.80	3.80	3.85	3.85
<b>DE10Y (BBG)*</b>	<b>0.34</b>	<b>0.50</b>	<b>0.65</b>	<b>0.84</b>	<b>0.96</b>

3M Money Market Rate					
	current	2018Q3	2018Q4	2019Q1	2019Q2
<b>Croatia</b>	0.50	0.50	0.50	0.60	0.70
<b>Czech Republic</b>	1.46	1.34	1.36	1.44	1.59
<b>Hungary</b>	0.17	0.30	0.35	0.45	0.55
<b>Poland</b>	1.70	1.73	1.73	1.73	1.73
<b>Romania</b>	3.30	3.25	3.00	3.10	3.40
<b>Serbia</b>	2.90	3.00	3.00	3.00	3.25
<b>Eurozone</b>	-0.32	-0.30	-0.30	-0.30	-0.30

FX					
	current	2018Q3	2018Q4	2019Q1	2019Q2
<b>EURHRK</b>	7.43	7.45	7.50	7.45	7.30
forwards		7.43	7.43	7.43	7.43
<b>EURCZK</b>	25.61	25.60	25.20	24.85	24.70
forwards		25.64	25.64	25.64	25.64
<b>EURHUF</b>	322.7	326.0	325.0	325.0	325.0
forwards		325.9	325.9	325.9	326.0
<b>EURPLN</b>	4.29	4.30	4.30	4.30	4.30
forwards		4.29	4.29	4.29	4.29
<b>EURRON</b>	4.66	4.70	4.73	4.74	4.75
forwards		4.66	4.66	4.66	4.66
<b>EURRSD</b>	118.0	118.0	118.0	118.5	118.5
forwards		-	-	-	-
<b>EURUSD</b>	1.15	1.14	1.13	1.15	1.16

Key Interest Rate					
	current	2018Q3	2018Q4	2019Q1	2019Q2
<b>Croatia</b>	0.30	0.30	0.30	0.30	0.30
<b>Czech Republic</b>	1.25	1.25	1.50	1.50	1.75
<b>Hungary</b>	0.90	0.90	0.90	0.90	0.90
<b>Poland</b>	1.50	1.50	1.50	1.50	1.50
<b>Romania</b>	2.50	2.75	2.75	2.75	3.00
<b>Serbia</b>	3.00	3.00	3.00	3.00	3.25
<b>Eurozone</b>	0.00	0.00	0.00	0.00	0.00

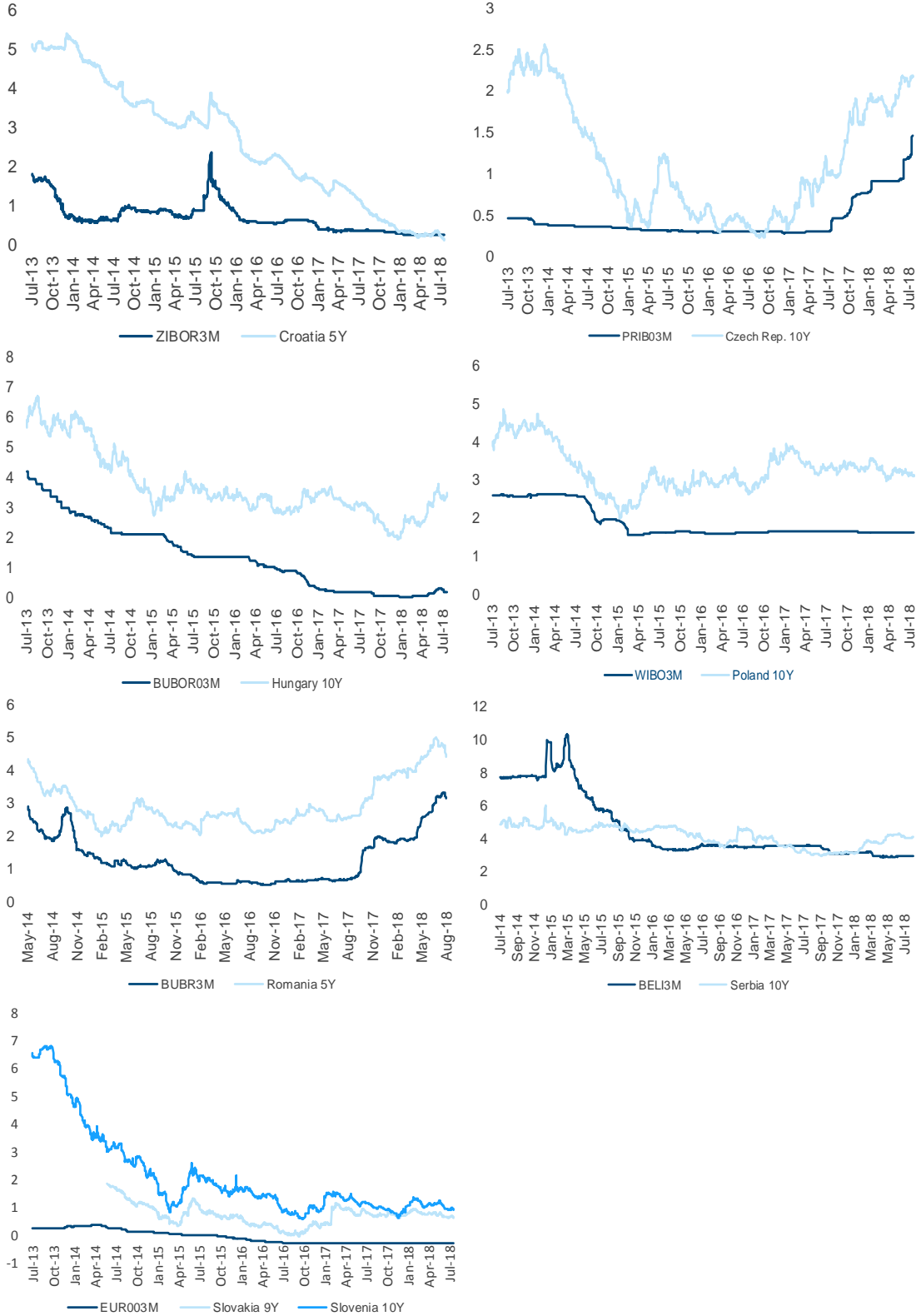
## Macro forecasts

Real GDP growth (%)	2016	2017	2018f	2019f	Average inflation (%)	2016	2017	2018f	2019f	Unemployment (%)	2016	2017	2018f	2019f
Croatia	3.5	2.9	2.8	2.7	Croatia	-1.1	1.1	1.7	1.8	Croatia	13.1	11.3	9.6	8.7
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	3.3	Hungary	0.4	2.4	2.6	3.5	Hungary	5.1	4.2	3.9	3.9
Poland	2.9	4.6	4.6	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	3.4	Romania	-1.5	1.3	4.7	3.3	Romania	5.9	4.9	4.6	4.8
Serbia	2.8	1.9	3.5	3.2	Serbia	1.6	3.0	2.1	3.4	Serbia	15.3	13.2	11.6	11.1
Slovakia	3.3	3.4	3.9	4.2	Slovakia	-0.5	1.3	2.5	2.5	Slovakia	9.6	8.1	6.9	6.4
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
<b>CEE8 average</b>	<b>3.1</b>	<b>4.7</b>	<b>4.1</b>	<b>3.3</b>	<b>CEE8 average</b>	<b>-0.4</b>	<b>1.9</b>	<b>2.4</b>	<b>2.5</b>	<b>CEE8 average</b>	<b>7.6</b>	<b>6.2</b>	<b>5.5</b>	<b>5.6</b>

Public debt (% of GDP)	2016	2017	2018f	2019f	C/A (%GDP)	2016	2017	2018f	2019f	Budget Balance (%GDP)	2016	2017	2018f	2019f
Croatia	80.6	78.0	74.4	71.4	Croatia	2.6	3.9	2.5	1.8	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	70.9	Hungary	6.0	2.9	2.1	2.0	Hungary	-1.7	-2.0	-2.2	-2.3
Poland	54.2	50.6	50.2	49.7	Poland	-0.3	0.3	-0.3	-0.9	Poland	-2.4	-1.7	-2.3	-2.2
Romania	37.1	35.0	35.2	35.8	Romania	-2.1	-3.3	-3.9	-4.0	Romania	-3.0	-2.9	-3.4	-2.9
Serbia	71.9	61.3	58.0	54.8	Serbia	-4.2	-4.7	-5.3	-6.6	Serbia	-1.3	1.2	0.0	-0.5
Slovakia	51.8	50.9	49.6	47.9	Slovakia	-1.5	-2.1	-1.2	-0.5	Slovakia	-2.2	-1.0	-1.0	-1.3
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
<b>CEE8 average</b>	<b>53.5</b>	<b>50.2</b>	<b>49.1</b>	<b>47.9</b>	<b>CEE8 average</b>	<b>0.4</b>	<b>0.2</b>	<b>-0.3</b>	<b>-0.7</b>	<b>CEE8 average</b>	<b>-1.8</b>	<b>-1.2</b>	<b>-1.7</b>	<b>-1.6</b>

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

## Appendix



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

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