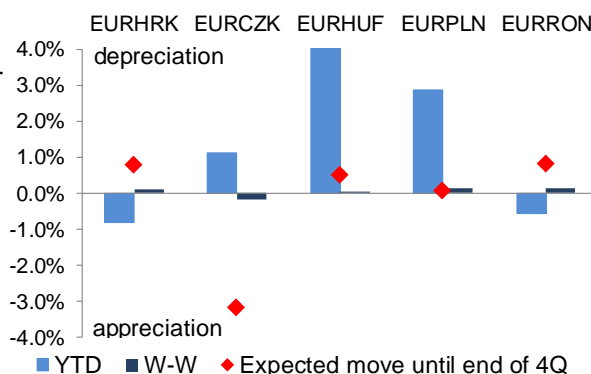


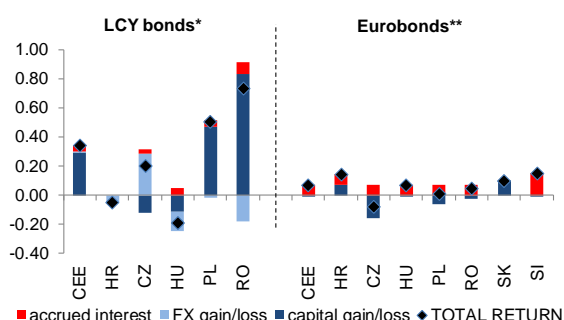
CEE Market Insights

Market outlook

The Czech koruna has finally got stronger, but it is still far from the level where the central bank would like to see it, according to its forecasts. That is why discussion on further rate hikes will remain on the table this Thursday. We expect the hike to be delivered in February unless the Czech koruna rapidly appreciates below 25 EURCZK. The Hungarian forint slightly eased last week, as the central bank is expected to remain dovish at its Tuesday MPC meeting.



Romanian and Polish 5Y LCY bonds continued their excellent performance last week, with yields falling to their lowest level since April. It is quite interesting that Hungary has not followed the trend of falling yields which we could observe in other CEE and southern euro area countries. The appreciation of the CZK helped to improve the performance of Czech bonds measured in the euro, while performance of Hungarian 5Y LCY bonds suffered additionally from the weaker forint.



Looking ahead this week:

Monday	Tuesday	Wednesday	Thursday	Friday
CZ: PPI	HU: Target Rate PL: Wages SK: Current Account	SK: Unemployment PL: Industry, PPI	CZ: Target Rate HR: Unemployment RS, HU: Current Account SK, SI: PPI	HU: Trade Balance PL: Retail, Unemployment

MPC meetings will be held in Hungary and the Czech Republic on Tuesday and Thursday, respectively. We do not expect any changes in rates in Hungary this week. On top of the rate decision, the new inflation forecast will be released and should not differ too much from the old forecast published in September. The markets expect some communication regarding the central bank's plan on the normalization of its monetary policy, such as a gradual reduction of outstanding FX swaps, which would lead to an increase in money market rates. We expect any communication to be very cautious and primarily to promote preparedness to act if needed. In the Czech Republic, given that the CZK is still weaker than expected, the debate on a rate hike will certainly continue at Thursday's MPC meeting, as was indicated by MPC member Vojtech Benda last week. We expect that a majority of MPC members (including the governor) will opt to wait with the rate hike until February in order to see a rebound of inflation and CZK development. A no-confidence vote against the government is scheduled in Romania for Thursday. We do not expect the vote to be successful and the government will likely be backed by smaller parties. This week, we should see the first set of monthly data for November for Poland. This will allow us to run our nowcast model, which currently points to 4.8% y/y growth in 4Q18.

In case you missed it last week...

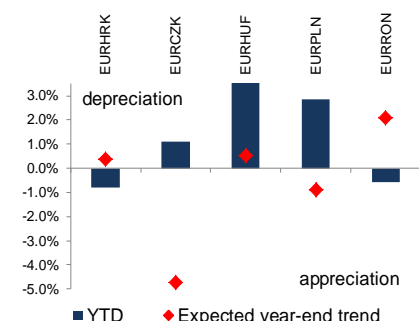
CEE: check out our newly issued publication [What's up in CEE, focused on outlook for 2019](#)

CEE: inflation numbers fell sharply in November, mainly due to lower fuel prices

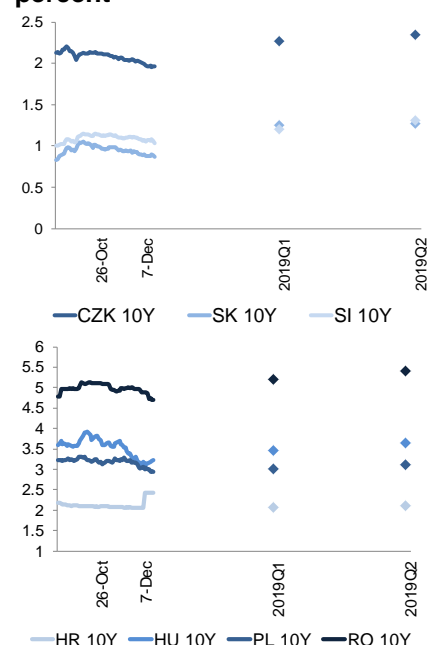
PL,SK,RO : inflation should rebound in January due to hikes in energy prices and excise taxes

RO: we have changed our interest rate outlook – key rate to remain stable throughout 2019

YTD change on FX market



10Y government bond yields, percent



Source: Erste Group Research, Bloomberg.

FX and bond market stable in CEE

On global markets:

This week's main event for the EURUSD will, without question, be the FOMC meeting in the US. An interest rate hike is widely expected. The market focus will be on the guidance for the future path of the US key interest rate.

CEE currencies:

The Czech koruna has finally slightly appreciated, but it is definitely still far from the central bank's expected level. While the central bank will very likely pause in its hiking cycle at its MPC meeting held this Thursday, the discussion on the further need for tightening will continue, with the most likely outcome being that the bank will see where inflation and the CZK are in January and hike afterwards if needed. The recent drop in inflation seems temporary and the central bank expects inflation to return to above the inflation target at the beginning of next year. We see the Czech koruna as the best-performing currency in 1Q19, appreciating towards 25 EURCZK in 1Q19.

CEE rates and yields:

Lower inflation readings for November left a mark on yield development last week. 10Y yields went further down in Poland (-10bp w/w) and Romania (-20bp w/w) last week. In Romania, we have changed our call for the interest rate outlook for next year. Given that inflation is likely to stay within the central bank's target range and core inflation has slightly eased, we do not expect any rate hike throughout next year. Romania's 10Y yields dropped below 4.7%, a level last seen in May. We still expect yields to climb back above 5% in the coming months, as the government will struggle to keep the budget under control. The budget proposal being discussed in the parliament is based on forecasted 5.5% GDP growth while the recent forecasts point much slower growth (3.4-3.6%). Slower growth will unmask the structural deficit built up in recent last years and make consolidation much harder and politically costly. And this will happen at a time when the ruling government has lost the majority in the parliament and has to rely on the support of smaller parties.

Calendar

Time	Country	Indicator	Period	Survey	Erste Est.	Prev.	Pre Comment
17-Dec							
9:00	CZ	PPI (y/y)	Nov	3.7%	3.5%	3.9%	Decline in oil prices will affect development of PPI inflation, which should gradually slow down in November and December
18-Dec							
10:00	PL	Wages (y/y)	Nov	7.2%	6.5%	7.6%	Stabilization of wage growth is observed
14:00	HU	Target Rate	Dec 18	0.9%	0.9%	0.9%	
14:30	SK	Current Account Balance	Oct			110.79	
19-Dec							
	SK	Unemployment Rate	Nov		5.2%	5.23%	Favourable development on the labour is expected to have continued in November.
10:00	PL	Industrial Production (y/y)	Nov	4.3%	1.5%	7.4%	Dropping sentiment to impact performance of industry
10:00	PL	PPI (y/y)	Nov	3.1%	3.0%	3.2%	Price pressure to stay around recently observed levels
20-Dec							
	HR	Unemployment Rate	Nov			9.1%	
	RS	Current Account Balance	Oct			-212.5	
8:30	HU	Current Account Balance	3Q		180	772.4	
9:00	SK	PPI (y/y)	Nov		7.0%	7.2%	Producer prices are likely to mark another brisk increase, albeit the inflationary pressures from energy prices (lower oil prices) have eased a bit recently.
10:30	SI	PPI (y/y)	Nov			1.9%	
13:00	CZ	Target Rate	Dec 20	1.75%	1.75%	1.75%	We expect CNB to keep interest rates unchanged; in our view, CNB could wait until beginning of next year to assess economic situation and decide about timing of next rate move
21-Dec							
9:00	HU	Trade Balance	Oct F			293	
10:00	PL	Retail Sales (y/y)	Nov	7.9%	7.0%	9.7%	Retail sales to maintain solid growth, but stabilization can be observed
10:00	PL	Unemployment Rate	Nov	5.8%	5.7%	5.7%	Unemployment rate to remain low

Sources: Bloomberg, Reuters

Capital market forecasts

Government bond yields					
	current	2019Q1	2019Q2	2019Q3	2019Q4
Croatia 10Y	2.43	2.05	2.10	2.20	2.30
spread (bps)	217	149	142	141	141
Czech Rep. 10Y	1.96	2.26	2.34	2.43	2.51
spread (bps)	170	170	166	164	162
Hungary 10Y	3.21	3.45	3.63	3.75	3.81
spread (bps)	296	289	295	296	292
Poland 10Y	2.94	3.00	3.10	3.15	3.20
spread (bps)	268	244	242	236	231
Romania 10Y	4.70	5.20	5.40	5.40	5.40
spread (bps)	444	464	472	461	451
Slovakia 10Y	0.87	1.25	1.27	1.30	1.55
spread (bps)	61	69	59	51	66
Slovenia 10Y	1.03	1.20	1.30	1.40	1.50
spread (bps)	77	64	62	61	61
Serbia 5Y	3.35	3.65	3.70	3.70	3.80
DE10Y (BBG)*	0.26	0.56	0.68	0.79	0.89

3M Money Market Rate					
	current	2019Q1	2019Q2	2019Q3	2019Q4
Croatia	0.49	0.50	0.55	0.55	0.60
Czech Republic	2.02	1.92	1.97	2.11	2.19
Hungary	0.13	0.45	0.55	0.75	0.85
Poland	1.72	1.73	1.73	1.73	1.73
Romania	3.04	3.30	3.30	3.30	3.30
Serbia	3.05	3.05	3.05	3.10	3.10
Eurozone	-0.31	-0.30	-0.30	-0.10	-

FX					
	current	2019Q1	2019Q2	2019Q3	2019Q4
EURHRK	7.39	7.45	7.30	7.42	7.45
forwards		7.39	7.39	7.39	7.39
EURCZK	25.79	25.00	24.70	24.60	24.50
forwards		25.82	25.82	25.82	25.82
EURHUF	323.8	325.0	325.0	325.0	325.0
forwards		327.0	327.0	327.0	327.0
EURPLN	4.30	4.30	4.28	4.26	4.25
forwards		4.30	4.30	4.30	4.30
EURRON	4.66	4.69	4.70	4.75	4.77
forwards		4.66	4.66	4.66	4.66
EURRSD	118.4	118.5	118.5	118.5	119.0
forwards		-	-	-	-
EURUSD	1.13	1.11	1.12	1.14	-

Key Interest Rate					
	current	2019Q1	2019Q2	2019Q3	2019Q4
Croatia	0.30	0.30	0.30	0.30	0.30
Czech Republic	1.75	1.75	1.75	2.00	2.00
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	2.50	2.50	2.50	2.50
Serbia	3.00	3.00	3.00	3.00	3.25
Eurozone	0.00	0.00	0.00	0.00	-

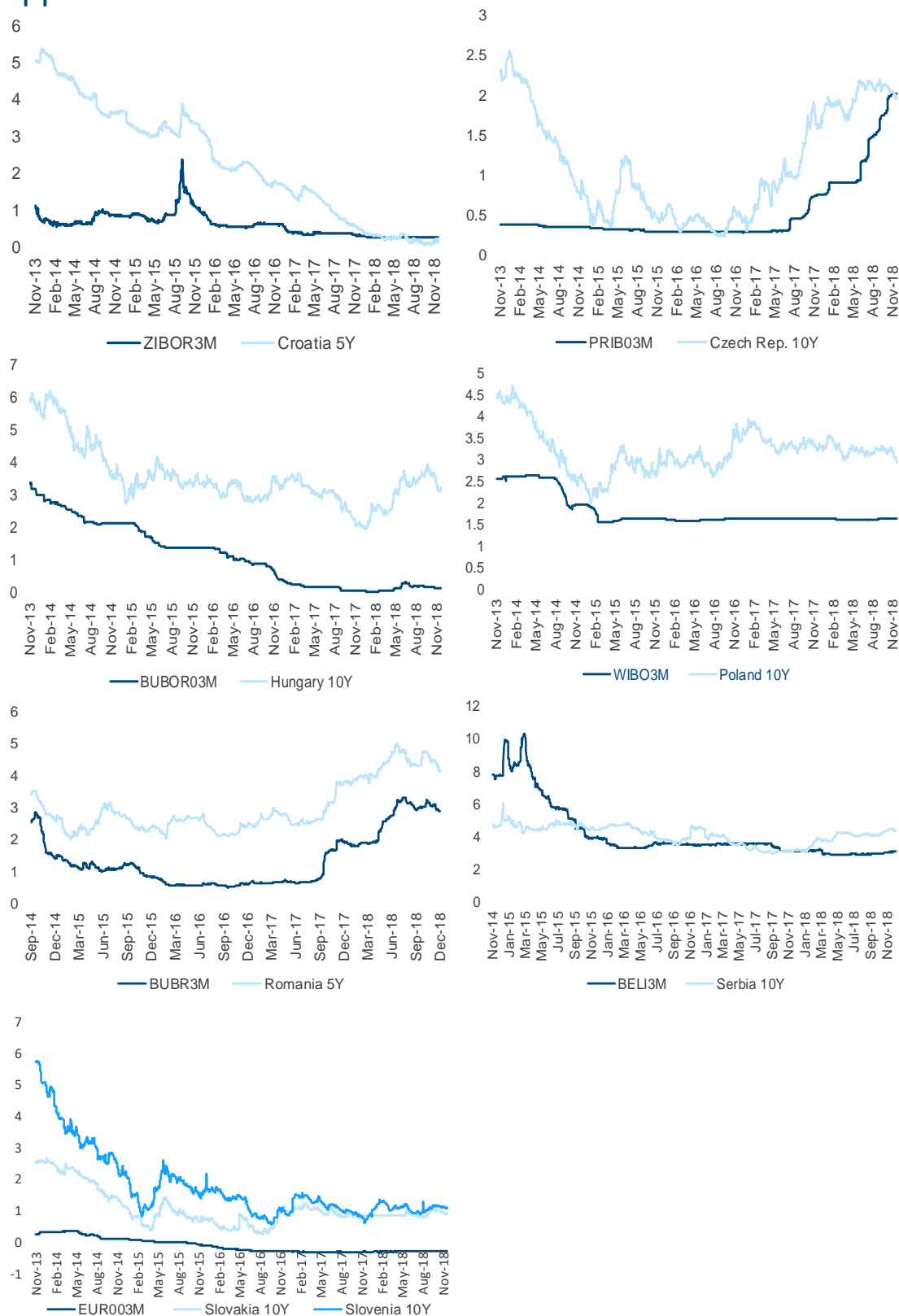
Macro forecasts

Real GDP growth (%)					Average inflation (%)					Unemployment (%)				
2017	2018f	2019f	2020f		2017	2018f	2019f	2020f		2017	2018f	2019f	2020f	
Croatia	2.9	2.8	2.6	2.5	Croatia	1.1	1.6	1.4	1.6	Croatia	11.3	8.8	7.8	7.3
Czech Republic	4.5	3.0	3.0	2.9	Czech Republic	2.4	2.2	2.1	1.9	Czech Republic	2.4	2.3	2.6	3.1
Hungary	4.1	4.6	3.6	2.8	Hungary	2.4	2.9	3.0	3.1	Hungary	4.2	3.7	3.9	3.9
Poland	4.8	5.1	3.8	3.3	Poland	2.0	1.7	2.4	2.5	Poland	7.2	6.2	6.2	6.3
Romania	7.3	4.3	3.4	3.9	Romania	1.3	4.6	3.2	3.1	Romania	4.9	4.6	4.8	5.0
Serbia	1.9	4.3	3.5	3.1	Serbia	3.0	2.0	2.3	2.7	Serbia	13.2	12.7	11.7	10.2
Slovakia	3.2	4.3	4.3	3.6	Slovakia	1.3	2.6	2.5	2.5	Slovakia	8.1	6.7	6.2	5.7
Slovenia	4.9	4.4	3.6	3.3	Slovenia	1.4	1.8	2.1	2.2	Slovenia	6.6	5.5	4.9	4.7
CEE8 average	4.8	4.4	3.6	3.3	CEE8 average	1.9	2.4	2.5	2.5	CEE8 average	6.2	5.4	5.4	5.4

Public debt (% of GDP)					C/A (%GDP)					Budget Balance (%GDP)				
2017	2018f	2019f	2020f		2017	2018f	2019f	2020f		2017	2018f	2019f	2020f	
Croatia	77.5	73.9	70.7	68.2	Croatia	4.0	2.8	2.2	1.1	Croatia	0.8	0.2	0.0	-0.5
Czech Republic	34.6	32.6	30.8	28.9	Czech Republic	1.1	0.7	0.6	0.4	Czech Republic	1.5	0.3	0.4	0.3
Hungary	73.3	72.4	69.9	67.4	Hungary	3.2	1.4	0.8	1.8	Hungary	-2.2	-2.3	-2.0	-2.0
Poland	50.6	50.1	50.5	49.7	Poland	0.2	-0.4	-0.5	-0.7	Poland	-1.7	-0.9	-1.4	-1.5
Romania	35.0	35.2	35.8	35.8	Romania	-3.2	-3.8	-4.1	-4.0	Romania	-2.9	-3.3	-3.0	-2.5
Serbia	61.3	54.5	52.0	49.6	Serbia	-5.3	-4.8	-4.6	-4.2	Serbia	1.2	0.9	-0.5	-0.5
Slovakia	50.9	48.9	47.6	45.9	Slovakia	-2.0	-1.3	-0.7	0.4	Slovakia	-0.8	-0.8	-0.7	-0.4
Slovenia	72.4	67.8	65.5	61.9	Slovenia	7.2	7.6	7.4	6.8	Slovenia	0.0	0.0	0.50	0.3
CEE8 average	50.3	48.9	48.1	46.7	CEE8 average	0.2	-0.4	-0.5	-0.5	CEE8 average	-1.1	-1.1	-1.2	-1.2

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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17 December 2018

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