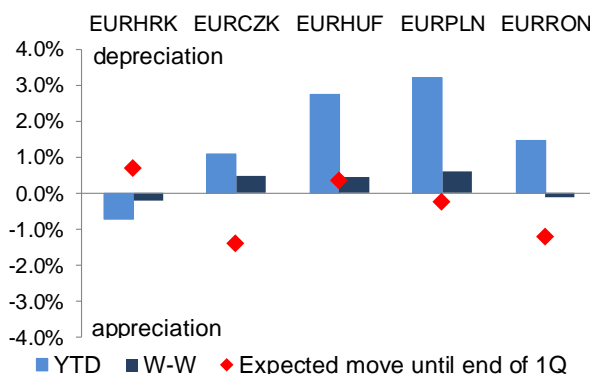




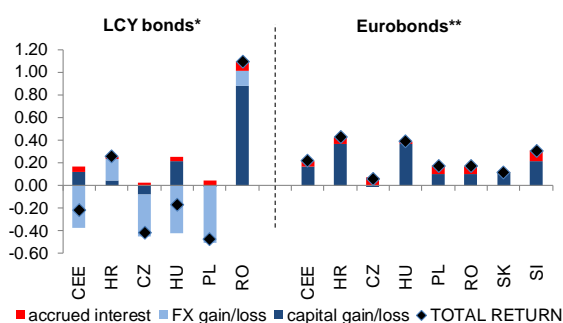
CEE Market Insights

Market outlook

Most currencies weakened last week in CEE – a notable exception was the Romanian leu, as it enjoyed some relief, given that the government seems to be backpedaling from its extremely controversial measures to some extent, and the NBR also likely present on the market, on behalf of the MinFin. In the meantime, the US dollar also firmed against the euro, which could have had a negative impact on CEE currencies as well.



Yields fell marginally in the region (1-3bp w/w), apart from the Czech Republic. Yields are being kept at bay also by a strong decline in Bund yields, courtesy of the new forecasts of the European Commission. Yield declines in Romania and the very strong buying interest for short-term government papers at the auction last week. However, for markets to calm down on the longer run, policymakers would need to come forth with more exact plans on how they want to amend the controversial measures in Romania.



Looking ahead this week:

Monday	Tuesday	Wednesday	Thursday	Friday
SK: Industry, Wages RO: Trade Balance, Wages SI: Industry	HU: CPI	RO: Current Account, Industry, CPI CZ: CPI PL: Trade Balance	RS: Current Account RO, HU, SK, PL: GDP 4Q	CZ: GDP 4Q SK, PL: CPI

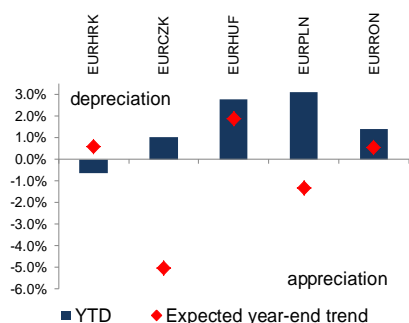
Five CEE countries will publish their flash estimates of GDP growth for 4Q18 this week. While we expect the growth to exceed 4% in Hungary, Poland, Slovakia and Romania (4.3%, 4.7%, 4.1% and 4.5%, respectively), in Czech Republic we should see only very benign growth at about 2.4%. Weaker external environment and more dovish interest rate outlook in the Euro Area led us to forecast one hike less in Czech Republic in 2020 and assume less aggressive koruna appreciation in 2019 compared to our previous forecast. In case of hard Brexit, we would expect depreciation of koruna well above 26 EURCZK with later correction to current levels by the year-end. Besides GDP flash estimates several CEE countries will publish inflation for January. We expect inflation to edge up (0.2-0.3pp) to 2.2% in Czech Republic and Slovakia, slightly decline (-0.2pp) in Hungary to 2.5% and remain flat at 3.3% in Romania. Discussion on Romania's budget will continue this week, including potential redesign or postponement of banking levy which have had an adverse effect on Romanian markets. Finally, S&P is scheduled to review Hungary's rating on Friday, which currently stands at 'BBB-' with a positive outlook. There is a chance for an upgrade already now, but such a step is more likely in August, in our view.

In case you missed it last week...

- CEE: [Special Report - CEE automotive sector changing horses](#)
- CZ: [CNB](#), [NBR](#), [NBP](#) and [NBS](#) all kept policy rates unchanged, as expected
- HU: [Industrial output surprised on the upside](#) and [retail sales proved somewhat lower than expected in Dec](#)
- CZ: [Industrial production declined slightly](#)
- SI: Fitch left the sovereign rating unchanged on Friday at 'A-' with a stable outlook

FX and bond market stable in CEE

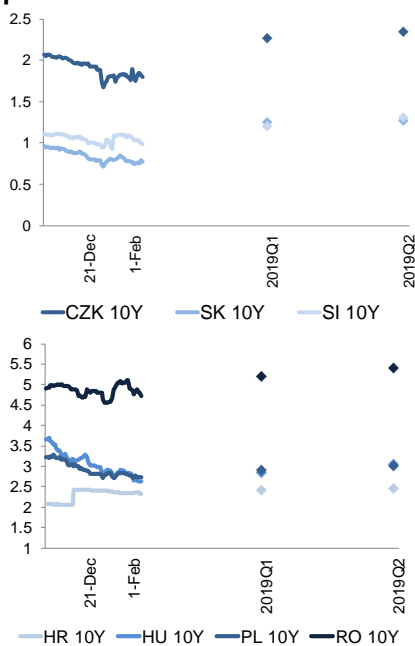
YTD change on FX market



On global markets:

The downward revision of GDP forecasts by the European Commission has also left its mark on the bond market. Now that the expected lower growth is close to potential, investors fear that this will have a dampening effect on inflation in the medium term. ECB President Draghi stressed at the monetary policy meeting in January that a weaker growth dynamic close to or below potential growth could mean that it takes longer for inflation to approach the ECB target. Since both the US Fed and ECB have made it unusually clear that they will wait and closely monitor the data situation before taking any further decisions, the financial markets are sensitive to revisions of economic forecasts.

10Y government bond yields, percent



Source: Erste Group Research, Bloomberg.

CEE currencies:

Most currencies weakened last week in CEE – a notable exception was the Romanian leu, as it enjoyed some relief, given that the government seems to be backpedaling from its extremely controversial measures to some extent, including the intention to cut the so-called “greed tax”. However, the NBR was also likely present on the market, as the governor said that it cannot deny news either that they were on the market, or the news that they did intervene on behalf of the MinFin. The HUF likely also weakened as markets gave up somewhat on high hopes that the MNB will start tightening soon, while the decline of the PLN might have to do with Governor Glapinski’s comments that the NBP might not hike for the next two years (or even until 2022). On the other hand, the CNB in Croatia needed to intervene on the HRK market, buying a total of EUR 450mn at an average rate of 7.41686. Kuna buying interest, however, can likely be explained by the recent government bond swap operation, where EUR 500mn of the total EUR 1.5bn maturity was replaced with a combination of a 10Y pure kuna issue and a 3Y FX-linked issue. In the meantime, the US dollar also firmed against the euro, which could have had a negative impact on CEE currencies as well. Current exchange rate levels in CEE are not very far off from our forecasts. Appreciation from current levels does not seem to likely at either of them, while for the CZK, where we have appreciation penciled in, we are expecting the koruna to appreciate to a lesser extent than the central bank envisages.

CEE rates and yields:

Yields fell marginally in the region (1-3bp w/w), apart from the Czech Republic. Yields are being kept at bay also by a strong decline in Bund yields, courtesy of the new forecasts of the European Commission. Yield declines in Romania and the very strong buying interest for short-term government papers at the auction last week, with around RON 1.3bn demand for RON 300mn worth of papers (as a result, the issued amount was doubled) indicates the relief of market participants. However, for markets to calm down on the longer run, policymakers would need to come forth with more exact plans on how they want to amend the controversial measures in Romania. Current yield levels indicate some downward risks to our yield forecasts in some CEE countries.

Calendar

Time	Country	Indicator	Period	Survey	Erste Est.	Prev.	Pre Comment
11-Feb							
	SK	Industrial Production (y/y)	Dec		0.04	3.7%	Industrial production growth is expected at decent pace, albeit with some likely impact of seasonal winter breaks
8:00	RO	Trade Balance	Dec		-1.8	-1567.4	Imports of consumer goods are rising fast, fueling Romania's external imbalance
8:00	RO	Wages (y/y)	Dec		15.6%	13.31%	Strong wage growth in public sector and rather prudent approach of private companies when increasing wages of their workers
9:00	SK	Wages (y/y)	Dec			3.2%	
10:30	SI	Industrial Production (y/y)	Dec		2.0%	2.5%	Slowdown of growth after strong 1H18; reflecting weaker demand from key trading partners
12-Feb							
9:00	HU	CPI (y/y)	Jan	2.80%	2.5%	2.7%	Mixed developments in different price categories; however, headline rate could have mainly been dominated by further drop of fuel prices
9:00	HU	CPI (m/m)	Jan	0.30%		-0.3%	
13-Feb							
	RO	Current Account Balance	Dec			-8730	
8:00	RO	Industrial Production (y/y)	Dec		1.8%	5.2%	Headwinds from Eurozone economy are affecting local manufacturing sector
8:00	RO	CPI (y/y)	Jan	3.30%	3.3%	3.27%	Inflation inside NBR's target in January
8:00	RO	CPI (m/m)	Jan	1.00%	0.8%	0.16%	Higher excise taxes for energy, car fuel and tobacco and weaker leu were key pro-inflationary factors in January
9:00	CZ	CPI (y/y)	Jan	2.10%	2.2%	2%	Increase in wage costs of firms, solid domestic demand and weak koruna remain most important pro-inflationary factors also at beginning of this year
9:00	CZ	CPI (m/m)	Jan	0.70%	0.8%	0.1%	In m/m terms, inflation will be driven by higher prices of food, energy and by seasonal factor associated with increase in prices of package holidays
14:00	PL	Trade Balance	Dec		-1111	-229	
14-Feb							
	RS	Current Account Balance	Dec		-505	-200.9	Slump in exports in December leading to widening of C/A deficit; FY18 C/A deficit expected at 5.4% of GDP
8:00	RO	GDP (y/y)	4Q A	4.50%	4.5%	4.35%	Real GDP is growing at annual rates below those from 2017
9:00	HU	GDP (y/y)	4Q P	4.60%	4.4%	4.9%	Some slowdown might have taken place following outstanding performance seen in 3Q18; consumption growth might have been somewhat lower, while industry seems to have proved more resilient to
9:00	SK	GDP (y/y)	4Q P		4.1%	4.6%	We expect GDP growth to have slowed down to 4.1% y/y, with domestic demand remaining its key driver as net exports remained rather lukewarm
10:00	PL	GDP (y/y)	4Q P	4.80%	4.7%	5.1%	We expect economy to slowdown in last quarter of 2018, due to weakening of private consumption
15-Feb							
9:00	CZ	GDP (y/y)	4Q A	2.40%	2.4%	2.4%	Although slowdown in y/y GDP growth has been affected by weaker growth in Euro Area, we also see it as soft landing from overheated phase of business cycle closer to its potential growth
9:00	SK	CPI (y/y)	Jan		2.2%	1.9%	Consumer price growth is likely to have inched up, driven by regulated energy prices, food and service prices
9:00	SK	CPI (m/m)	Jan		1.1%	-0.1%	Significant contribution to monthly increase of consumer prices should be due to higher regulated prices
10:00	PL	CPI (y/y)	Jan	1.00%	0.7%	1.1%	Inflation is expected to further ease, given freeze of energy prices and oil prices decrease

Sources: Bloomberg, Reuters

Capital market forecasts

Government bond yields					
	current	2019Q1	2019Q2	2019Q3	2019Q4
Croatia 10Y	2.33	2.40	2.45	2.50	2.60
spread (bps)	224	198	186	182	180
Czech Rep. 10Y	1.80	2.15	2.24	2.29	2.34
spread (bps)	170	173	165	161	154
Hungary 10Y	2.63	2.84	3.03	3.28	3.32
spread (bps)	253	242	244	260	252
Poland 10Y	2.71	2.90	3.00	3.10	3.20
spread (bps)	262	248	241	242	240
Romania10Y	4.74	5.20	5.40	5.40	5.40
spread (bps)	465	478	481	472	460
Slovakia 10Y	0.77	1.25	1.27	1.30	1.55
spread (bps)	67	83	68	62	75
Slovenia 10Y	0.98	1.20	1.30	1.40	1.50
spread (bps)	89	78	71	72	70
Serbia 5Y	3.54	3.60	3.60	3.65	3.70
DE10Y (BBG)*	0.09	0.42	0.59	0.68	0.80

3M Money Market Rate					
	current	2019Q1	2019Q2	2019Q3	2019Q4
Croatia	0.49	0.50	0.55	0.55	0.60
Czech Republic	1.99	2.01	2.01	2.18	2.19
Hungary	0.15	0.19	0.40	0.70	0.85
Poland	1.72	1.73	1.73	1.73	1.73
Romania	3.10	3.30	3.30	3.30	3.30
Serbia	3.03	3.07	3.07	3.07	3.07
Eurozone	-0.31	-0.30	-0.30	-0.10	-

FX					
	current	2019Q1	2019Q2	2019Q3	2019Q4
EURHRK	7.41	7.45	7.30	7.42	7.45
forwards		7.41	7.41	7.41	7.41
EURCZK	25.82	25.45	25.30	25.10	24.80
forwards		25.84	25.85	25.85	25.85
EURHUF	319.2	320.0	322.0	325.0	325.0
forwards		322.4	322.4	322.4	322.4
EURPLN	4.31	4.30	4.28	4.26	4.25
forwards		4.31	4.31	4.31	4.31
EURRON	4.75	4.69	4.70	4.75	4.77
forwards		4.75	4.75	4.75	4.75
EURRSD	118.3	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	3.00
Eurozone	0.00	0.00	0.00	0.00	-

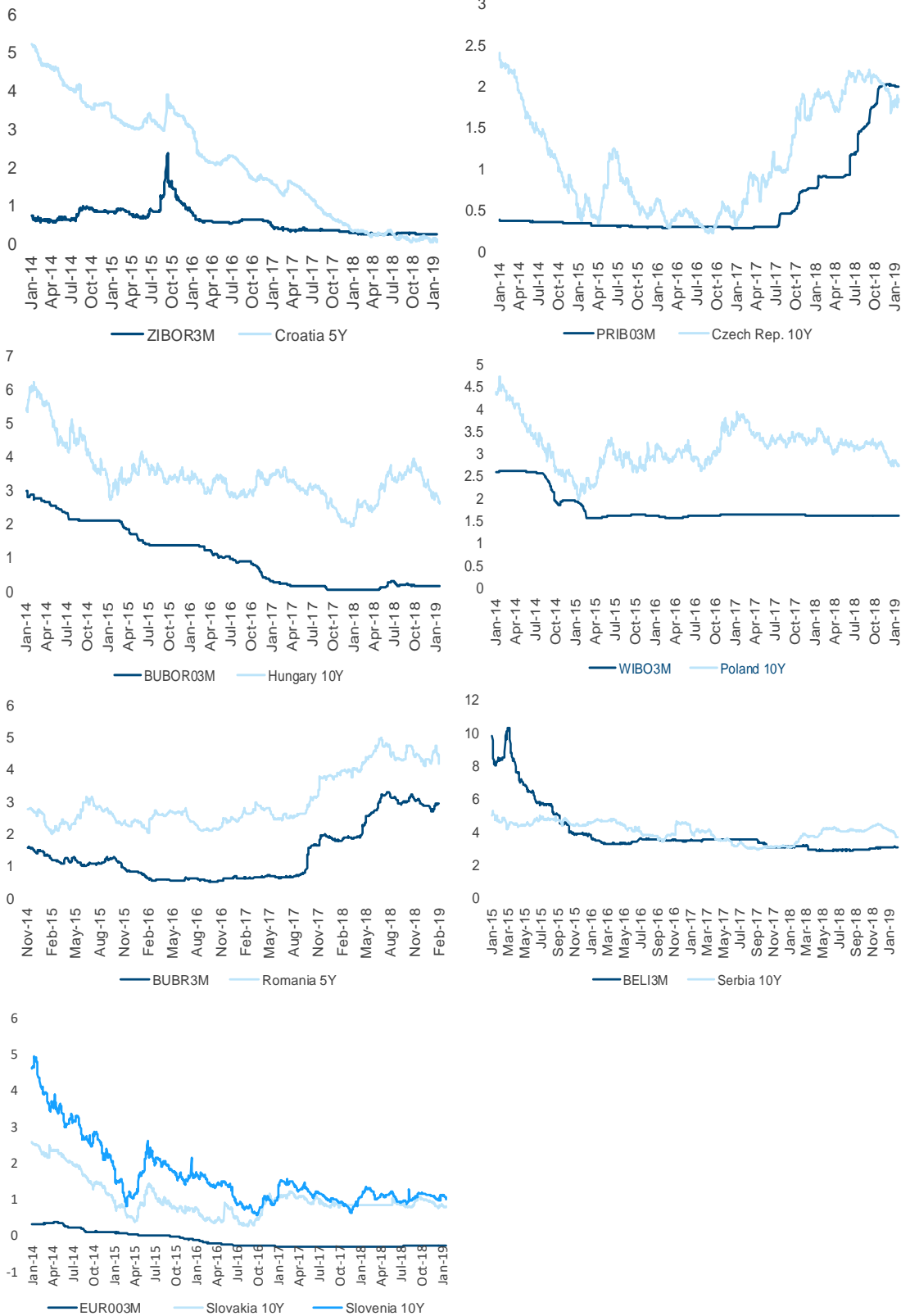
Macro forecasts

Real GDP growth (%)	2017	2018f	2019f	2020f	Average inflation (%)	2017	2018f	2019f	2020f	Unemployment (%)	2017	2018f	2019f	2020f
Croatia	2.9	2.8	2.6	2.5	Croatia	1.1	1.5	1.0	1.5	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	2.9	Hungary	2.4	2.8	2.6	3.1	Hungary	4.2	3.7	3.9	3.9
Poland	4.8	5.1	3.8	3.3	Poland	2.0	1.6	1.9	2.5	Poland	7.2	6.1	6.3	6.4
Romania	7.0	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	2.0	4.2	3.3	2.9	Serbia	3.1	2.0	2.4	2.8	Serbia	14.1	13.0	12.0	10.4
Slovakia	3.2	4.2	3.4	3.6	Slovakia	1.3	2.5	2.5	2.5	Slovakia	8.1	6.7	6.3	5.8
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	4.7	4.4	3.5	3.3	CEE8 average	1.9	2.4	2.2	2.5	CEE8 average	6.2	5.4	5.4	5.4

Public debt (% of GDP)	2017	2018f	2019f	2020f	C/A (%GDP)	2017	2018f	2019f	2020f	Budget Balance (%GDP)	2017	2018f	2019f	2020f
Croatia	77.5	73.9	71.1	68.6	Croatia	4.0	2.8	2.4	1.3	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	71.8	69.0	67.0	Hungary	3.2	1.4	0.8	1.8	Hungary	-2.2	-2.0	-1.8	-1.8
Poland	50.6	49.9	49.8	48.7	Poland	0.2	-0.4	-0.5	-0.7	Poland	-1.7	-0.4	-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	57.9	53.7	51.3	49.0	Serbia	-5.2	-5.3	-5.2	-4.9	Serbia	1.1	0.9	-0.5	-0.5
Slovakia	50.9	49.0	48.2	46.5	Slovakia	-2.0	-1.5	-0.9	0.2	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	50.2	48.8	47.8	46.3	CEE8 average	0.2	-0.4	-0.6	-0.5	CEE8 average	-1.1	-0.9	-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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11 February 2019

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