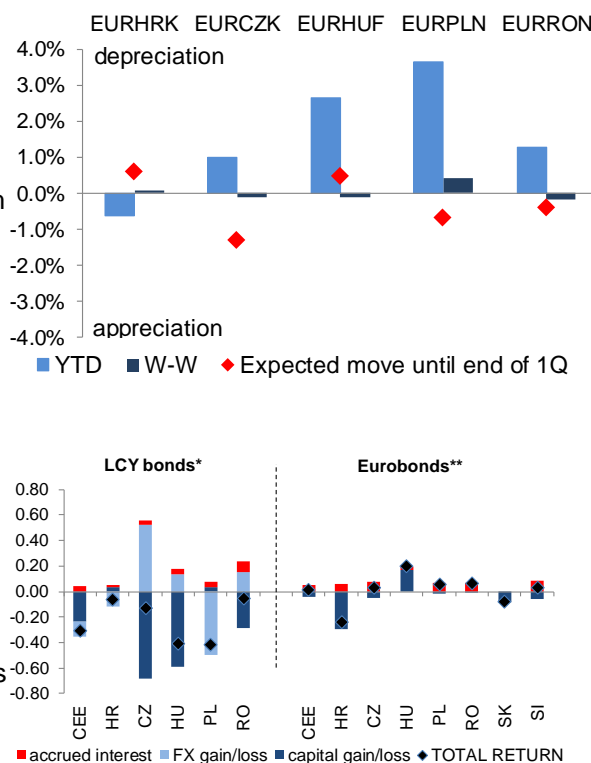


CEE Market Insights

Market outlook

In Hungary and the Czech Republic, markets have started to believe in more aggressive monetary tightening, after upbeat inflation readings were released, which propped up local currencies. The Polish zloty was the most exposed to the ongoing strength of the US dollar, as inflation does not underpin monetary tightening there. However, there is little domestic reason to believe that the PLN will fall further from current levels. For Hungary, as we think that the MNB will start tightening later or less aggressively than the market currently assumes, we believe that levels below 320 for the EURHUF are a bit too low. As for the Czech Republic, however, we stick to our view that the relatively high interest rate differential should give a boost to the koruna.

Increased interest rate expectations drove yields up in the Czech Republic and in Hungary too last week. In Romania, yields went up to a lesser extent, but auction results show markets still in some uncertainty. The budget for this year was passed at a planned deficit of 2.76% of GDP, assuming a 5.5% real GDP increase, which seems extremely optimistic. We maintain our view that yields should increase from current levels in Romania. As for Hungary, we slightly cut our 10Y yield forecast, however, as German Bund yields remain pretty low.



Looking ahead this week:

Monday	Tuesday	Wednesday	Thursday	Friday
	SK: Unemployment PL: Wages	PL: Industry, PPI	PL: Retail Sales SI: PPI	HR, RS: CPI

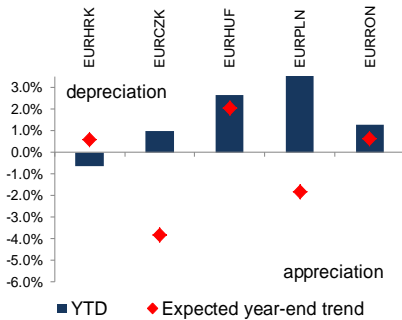
From the few indicators that are going to be released this week, probably the most interesting to watch will be January industrial output and retail sales for Poland and January CPI data for Croatia and Serbia, which are due on Friday. Poland's monthly data will give us a more precise estimate as to how the largest CEE economy was performing in 1Q19. Regarding inflation, we expect slightly lower readings for Croatia (0.7% in January vs. 0.8% in December), while inflation likely increased in Serbia, driven by higher vegetable prices and an increase of the excise tax on cigarettes. This week, we should have more clarity on the design of the banking levy in Romania, which has been strongly criticized by the central bank (and the ECB), due to its adverse impact on the economy and its financial sector, narrowing the room for maneuver and efficiency of monetary policy.

In case you missed it last week...

- CZ: Flash [GDP growth in 4Q18](#) and [January inflation](#) surprised on upside
- CZ: Brexit woes weigh on koruna appreciation; we expect [slower appreciation of koruna this year](#)
- HU: [GDP growth accelerated to 5% in 4Q18](#), [core inflation increased above 3% in January](#), S&P upgraded Hungary's sovereign rating to BBB with stable outlook
- SK: [GDP growth ends the year on a weaker footing than anticipated](#)
- RO: [4Q18 GDP growth in line with expectations](#); we lowered our forecast to 3.1% for 2019 and 2.7% for 2020
- RO: [Inflation is to stay inside the CB's target band throughout 2019](#)
- PL: [Polish economy expanded 4.9% y/y in 4Q18](#) but headline [inflation further eased to 0.9% in January](#)

FX and bond market stable in CEE

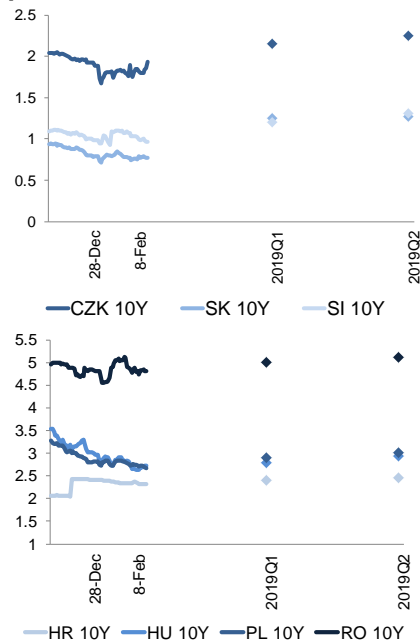
YTD change on FX market



On global markets:

This week, central bank events could provide important news for the EURUSD. ECB Chief Economist Peter Praet is scheduled to make two speeches, possibly providing insights on the ECB's assessment of the economic slowdown. The economic slowdown in the euro zone in the second half of 2018 was significantly stronger than originally expected and lowered the starting position for 2019. On the other side of the Atlantic, the Fed chairman will give his testimony on the economy and monetary policy to the US Congress. The most important macro indicators will be February PMIs for the Eurozone and large member countries.

10Y government bond yields, percent



Source: Erste Group Research, Bloomberg.

CEE currencies:

In Hungary and the Czech Republic, where core inflation either reached or even exceeded 3% according to last week's data, markets have started to believe in more aggressive monetary tightening, which propped up local currencies. On the other hand, the Polish zloty fell last week; inflation is still below 1 percent there, which does not support any tightening. Thus, the zloty was the most exposed to the ongoing strength of the US dollar. However, low inflation is not a surprise in Poland, and thus there is little domestic reason to believe that the PLN will fall further from current levels. The Serbian dinar also appreciated a bit last week, but we expect the NBS to tame any pressures, should they arise from any direction. Thus, the EURRSD could stay between 118.0 and 118.5 in the coming months. For Hungary, as we think that the MNB will start tightening later or less aggressively than the market currently assumes, we believe that levels below 320 for the EURHUF are a bit too low, so some forint depreciation could come. As for the Czech Republic, however, we stick to our view that the relatively high interest rate differential should give a boost to the koruna and the EURCZK should continuously fall in the coming months.

CEE rates and yields:

Despite the fact that Bund yields went down towards the end of last week, in most cases, we saw yield increases in CEE w/w. Of the 10Y yields that went up, we saw them rising to an extent of 6-12bp. This is mostly attributable to increased interest rate expectations (mainly in the Czech Republic and in Hungary), courtesy of relatively high inflation readings. In Romania, yields went up to a lesser extent. Bond auction results show markets still in some uncertainty in Romania. A 336-day T-bill auction saw the rejection of all bids put up for a planned amount of RON 400mn, while the 5Y RON auction went well, as RON 320mn was sold at an average accepted yield of 4.29%, with a bid-to-cover of almost 2.3. The budget for this year was passed at a planned deficit of 2.76% of GDP, assuming a 5.5% real GDP increase, which seems extremely optimistic. We maintain our view that yields should increase from current levels in Romania. As for Hungary, we slightly cut our 10Y yield forecast, however, as German Bund yields remain pretty low.

Calendar

Time	Country	Indicator	Period	Survey	Erste Est.	Prev.	Pre Comment
18-Feb							
No releases scheduled							
19-Feb							
	SK	Unemployment Rate	Jan			5.04%	
10:00	PL	Wages (y/y)	Jan	6.70%	5.8%	6.1%	After moving in sideways trend in 2H18, we expect wage growth to ease.
20-Feb							
10:00	PL	Industrial Production (y/y)	Jan	3.8%	3.90%	2.8%	Positive calendar effect (+1 working day) should support industrial performance. New orders up in December, which is positive for industrial output.
10:00	PL	PPI (y/y)	Jan	2.1%	1.90%	2.2%	Price pressure to ease in January.
21-Feb							
10:00	PL	Retail Sales (y/y)	Jan	5.5%	6.50%	4.7%	Increase of local consumer sentiment index (BWUK) observed in January compared to December, which should support retail sales.
10:30	SI	PPI (y/y)	Jan			1.4%	
22-Feb							
11:00	HR	CPI (y/y)	Jan		0.7%	0.8%	Inflation expected to remain in tight band in January.
11:00	HR	CPI (m/m)	Jan			-0.8%	
12:00	RS	CPI (y/y)	Jan		2.20%	2%	Regular annual adjustment of excise tax on cigarettes and double-digit growth in vegetable prices were main drivers of slightly higher CPI in January. CPI expected to remain in lower part of targeted band throughout 2019.
12:00	RS	CPI (m/m)	Jan		1%	0.1%	

Sources: Bloomberg, Reuters

Capital market forecasts

Government bond yields					
	current	2019Q1	2019Q2	2019Q3	2019Q4
Croatia 10Y	2.32	2.40	2.45	2.50	2.60
spread (bps)	222	206	197	191	189
Czech Rep. 10Y	1.93	2.15	2.24	2.29	2.34
spread (bps)	183	181	176	170	163
Hungary 10Y	2.73	2.77	2.93	3.10	3.21
spread (bps)	263	243	245	251	250
Poland 10Y	2.68	2.90	3.00	3.10	3.20
spread (bps)	258	256	252	251	249
Romania10Y	4.81	5.00	5.10	5.10	5.20
spread (bps)	470	466	462	451	449
Slovakia 10Y	0.77	1.25	1.27	1.30	1.55
spread (bps)	67	91	79	71	84
Slovenia 10Y	0.97	1.20	1.30	1.40	1.50
spread (bps)	87	86	82	81	79
Serbia 5Y	3.64	3.60	3.60	3.65	3.70
DE10Y (BBG)*	0.10	0.34	0.48	0.59	0.71

3M Money Market Rate					
	current	2019Q1	2019Q2	2019Q3	2019Q4
Croatia	0.49	0.50	0.55	0.55	0.60
Czech Republic	2.01	2.01	2.01	2.18	2.19
Hungary	0.15	0.19	0.35	0.70	0.85
Poland	1.72	1.73	1.73	1.73	1.73
Romania	3.17	2.80	2.80	2.80	2.80
Serbia	2.99	3.07	3.07	3.07	3.07
Eurozone	-0.31	-0.30	-0.30	-0.30	-

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	25.70	25.45	25.30	25.10	24.80
forwards		25.73	25.73	25.73	25.73
EURHUF	318.1	320.0	322.0	325.0	325.0
forwards		321.2	321.2	321.3	321.3
EURPLN	4.33	4.30	4.28	4.26	4.25
forwards		4.33	4.33	4.33	4.33
EURRON	4.74	4.72	4.73	4.75	4.77
forwards		4.74	4.74	4.74	4.74
EURRSD	118.2	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	-

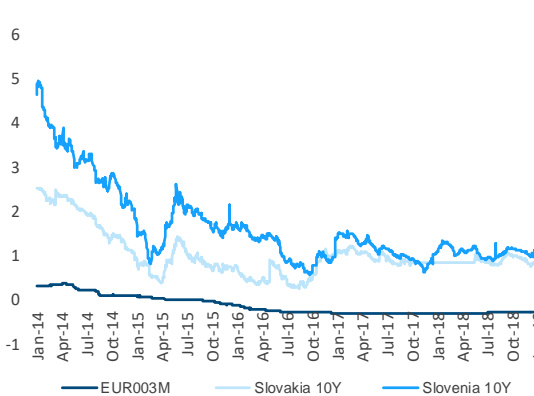
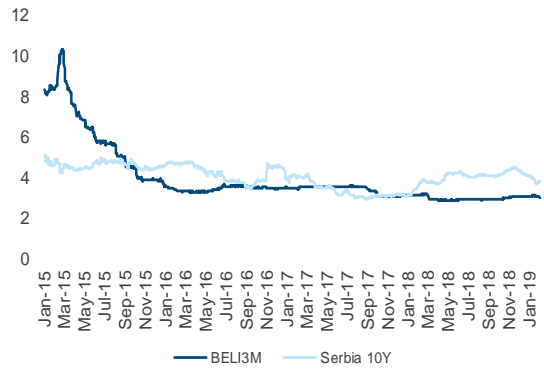
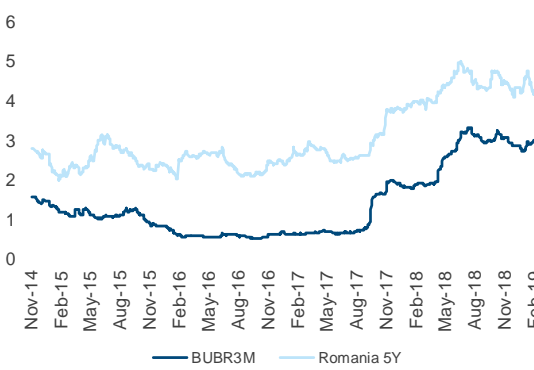
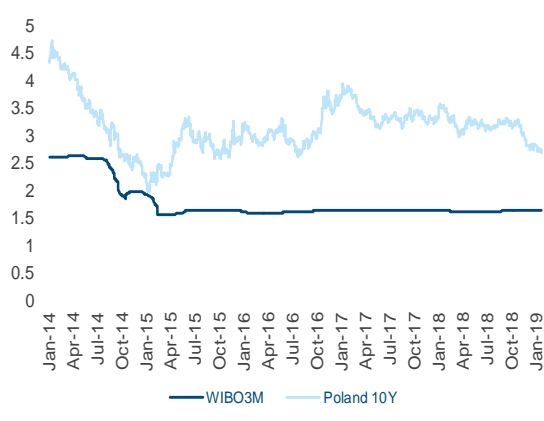
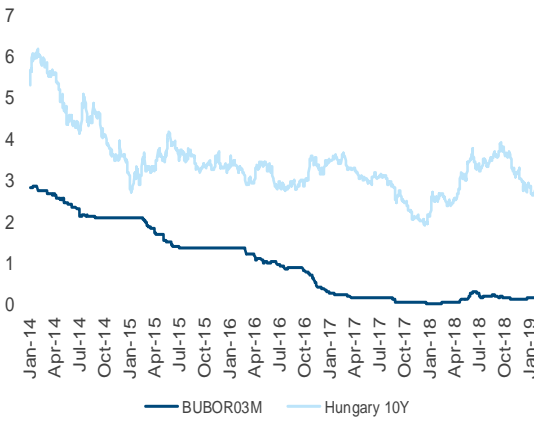
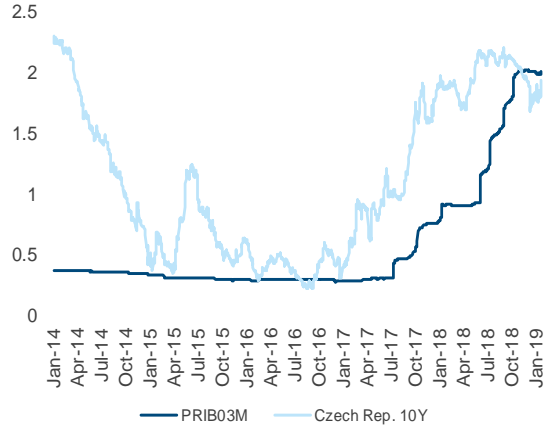
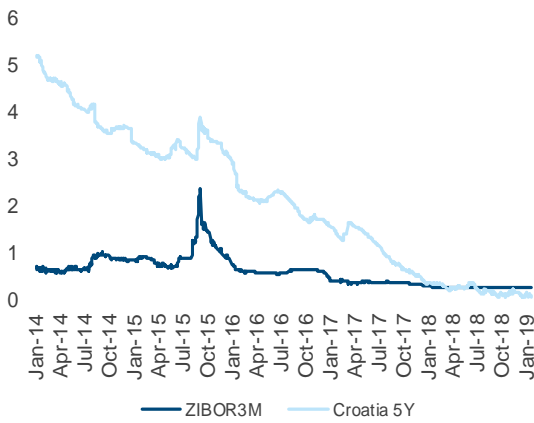
Macro forecasts

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	2.8	2.5	2.8	Czech Republic	2.4	2.2	2.3	2.0	Czech Republic	2.4	2.4	2.5	3.0
Hungary	4.1	4.8	3.6	2.9	Hungary	2.4	2.8	2.7	3.1	Hungary	4.2	3.7	3.8	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	4.1	3.1	2.7	Romania	1.3	4.6	3.2	2.8	Romania	4.9	4.2	3.8	4.0
Serbia	2.0	4.2	3.3	2.9	Serbia	3.1	2.0	2.1	2.3	Serbia	14.1	12.3	11.5	10.5
Slovakia	3.2	4.1	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	1.7	1.6	1.5	Slovenia	6.6	5.5	4.9	4.7
CEE8 average	4.7	4.3	3.4	3.1	CEE8 average	1.9	2.4	2.3	2.4	CEE8 average	6.2	5.3	5.2	5.3

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	34.7	33.2	32.1	31.4	Czech Republic	1.1	0.6	0.5	0.6	Czech Republic	1.5	1.5	1.1	0.9
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	35.1	34.7	35.5	36.2	Romania	-3.2	-4.6	-4.9	-4.8	Romania	-2.9	-2.9	-3.0	-2.5
Serbia	57.9	53.7	51.5	49.4	Serbia	-5.2	-5.2	-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	65.9	62.7	Slovenia	7.2	7.6	7.4	6.7	Slovenia	0.0	0.0	0.50	0.3
CEE8 average	50.2	48.8	48.0	46.9	CEE8 average	0.2	-0.5	-0.7	-0.6	CEE8 average	-1.1	-0.6	-1.1	-1.1

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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18 February 2019

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