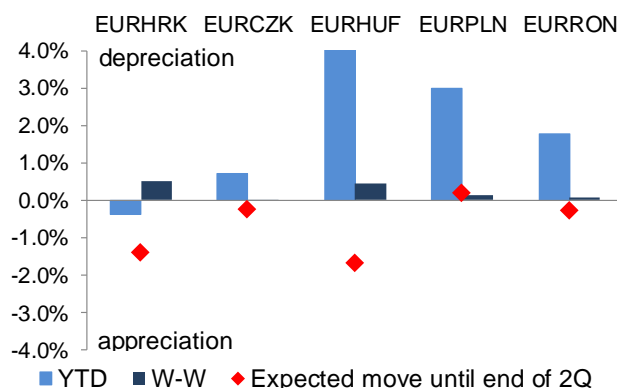


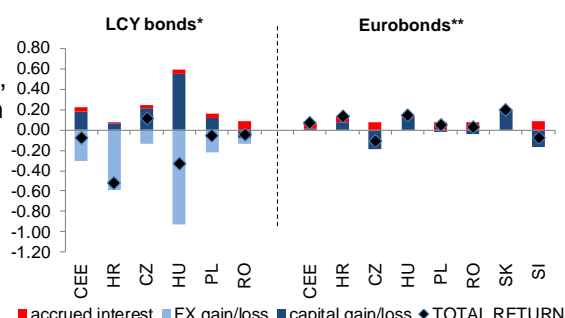
CEE Market Insights

Market outlook

While the HUF fell the most in the region last week, we think that the Hungarian central bank will not be worried much as long as long-term yields do not increase substantially, which does not seem to be the case yet. The dovishness of the central bank could mean that the forint could continue to be subject to higher volatility. In Croatia, the kuna seems somewhat weak, while usual seasonal flows at this time of the year would suggest otherwise. Still, any appreciation pressure on the kuna could continue to be tamed by the central bank, in line with comments from central banker Vujcic.



Lower Bund yields helped CEE yields to go mostly lower last week. Czech and Hungarian yield spreads even declined, likely due to worsening trade war prospects globally. Polish yields showed some uptick during the week, however, after the relatively strong GDP data release. Even more importantly, the governor signaled that he sees unchanged rates until the end of his term – which is only coming in three years. In Romania, tight liquidity control is deemed very effective by the governor. This reaffirms our view that no increase in the policy rate will come this year.



Looking ahead this week:

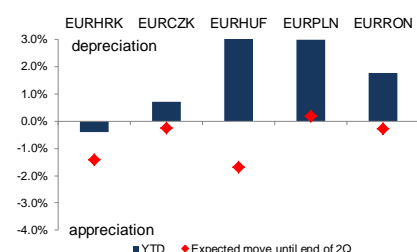
Monday	Tuesday	Wednesday	Thursday	Friday
CZ: PPI	PL: Wages SI: PPI	PL: Industry, PPI	PL: Retail	RS: Wages

This week, the release calendar is relatively empty. Except for PPI data, there will be just April's industrial output, retail sales and wage growth for Poland. This data will be very important, as it will provide us the first opportunity to get now-cast output for GDP in 2Q19 based on April numbers. At this moment, we expect the Polish economy to sustain strong growth 2Q. Last week's better than expected GDP flash estimates will lead to some upward revision of the full-year forecast. We have put our 3.1% forecast for the Romanian economy under review (a new forecast will be published within a week), while we see some upward risks for Hungary's forecast, which is likely to be updated with the detailed GDP data (due in June). Over the weekend, European elections take place. They could provide some valuable insights on new trends in domestic political preferences. However, due to low turnouts, these preferences (level-wise) should not be taken as fully representative.

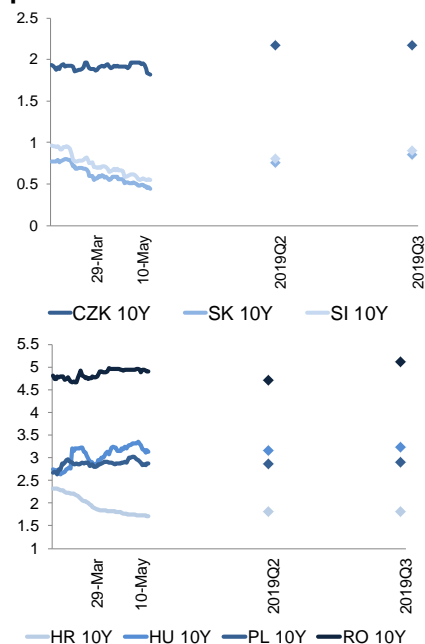
In case you missed it last week...

CEE: Inflation slowed down in [Czechia](#), [Croatia](#) and [Slovakia](#) and accelerated in [Romania](#) and [Serbia](#) in April
CZ: [Favorable economic development continues](#)
PL: [Polish economy sustained solid growth in 1Q19](#)
RO: [Romanian economy expanded 5% y/y in 1Q19](#); we have put our full-year forecast under review
SK: [Flash GDP points to a mild acceleration in 1Q19 from lukewarm 4Q18](#)
HU: [Hungarian economy posted 5.3% y/y growth in 1Q19](#); we see upside risks to our full-year forecast
PL: MPC kept rates unchanged, [stability of rates is expected at least for 2019](#)
RO: [Central bank opts for tight liquidity control instead of raising key interest rates](#)
RS: We increased our year-end inflation forecast to 2.5%, from 2.1%

YTD change on FX market



10Y government bond yields, percent



Source: Erste Group Research, Bloomberg.

On global markets:

Next week, the most important macro data for the EURUSD will come from the Eurozone. PMIs for the month of May will be released and will give markets an important update on the status of the economy of the Eurozone as a whole, as well as from large member countries.

CEE currencies:

The forint again proved to be the most vulnerable in the CEE region to negative international news, as last week brought an almost one percent weakening against the EUR. As long as the weakening in the forint is not severe and long-term government bond yields do not reflect the fact that the market is pricing in a substantially larger inflation premium quickly, the central bank is unlikely to act. We think that the forint could remain subject to volatility in the coming weeks. Other currencies in the region only marginally weakened last week, or remained little changed, amid the deteriorating international sentiment (due to trade wars). The Croatian kuna seems relatively weak, as, despite the approaching holiday season, the HRK does not show the usual appreciation pattern. Appreciation of the HRK could be further burdened by comments from central banker Vujcic that, although he sees appreciation pressure on the kuna, he still sees the exchange rate as flat going forward. Interesting comments came from the NBS in Serbia as well, as they made it clear that they do not prefer to see much lower levels in the EURRSD going forward, as they do not want such moves to create disinflationary pressure. This reinforces our view that the dinar could remain stable against the euro.

CEE rates and yields:

CEE bond markets were affected by developments of German Bunds last week, as the latter declined by 5bp on the 10Y tenor w/w. Still, Czech and Hungarian yields fell much more than Bund yields in the region. The narrowing of the spread in these countries is a bit at odds with the good GDP data released last week (especially for Hungary, which posted 5.3% y/y real GDP growth for 1Q19, while the Czech figure was at 2.5%), but could perhaps be better understood against the backdrop of the deteriorating international sentiment. This latter element was likely driven by the worsening of global trade war prospects, which is especially problematic for Czechia and Hungary, which are heavily exposed to the international auto sector. For Hungary, the bond market does not seem to be pricing in increasingly higher inflation for the time being, despite evident signs of economic overheating and a still rather dovish central bank. Poland also showed interesting developments, as the 10Y yield went up by 10bp (to 2.9%) after the publication of the 1Q19 GDP estimate, which came as a positive surprise (at 4.6%) compared to market expectations. Currently, the 10Y is at 2.85-2.90%, which is roughly in line with our forecast for the end of 2Q19. Additionally, Governor Glapinski said that he would see unchanged rates until the end of his term, which will come in three years – a rather strong commitment, while core inflation is at the highest level since 2012. As for Romania, the central bank kept rates unchanged at 2.5%, while reiterating that strong liquidity control will be kept in place and added that this measure could be equivalent to a 75bp hike in the policy rate. This comment reaffirms our view for an unchanged base rate this year in Romania, despite the fact that the NBR is expecting inflation to stay above the target even at the end of this year.

Calendar

Time	Country	Indicator	Period	Survey	Erste Est.	Prev.	Pre Comment
20-May							
9:00	CZ	PPI (y/y)	Apr	4.0%	3.9%	3.8%	Increasing labor costs and higher oil prices are main proinflationary factors behind producer price inflation.
21-May							
10:00	PL	Wages (y/y)	Apr	6.50%	6.2%	5.7%	Wage growth should sustain solid growth.
10:30	SI	PPI (y/y)	Apr			1.1%	
22-May							
10:00	PL	Industrial Production (y/y)	Apr	8.7%	4.0%	5.6%	We expect somewhat weaker performance of industry.
10:00	PL	PPI (y/y)	Apr	2.6%	2.4%	2.5%	Price pressure should remain limited.
23-May							
10:00	PL	Retail Sales (y/y)	Apr	9.6%	6.5%	3.1%	Easter effect should shift retail sales up.
24-May							
12:00	RS	Wages (y/y)	Mar			6.9%	

Sources: Bloomberg, Reuters

Capital market forecasts

Government bond yields					
	current	2019Q2	2019Q3	2019Q4	2020Q1
Croatia 10Y	1.72	1.80	1.80	1.80	1.90
spread (bps)	182	165	158	152	154
Czech Rep. 10Y	1.82	2.17	2.17	2.33	2.44
spread (bps)	192	202	195	205	208
Hungary 10Y	3.14	3.14	3.23	3.40	3.46
spread (bps)	324	299	301	312	310
Poland 10Y	2.88	2.85	2.90	3.00	3.10
spread (bps)	298	270	268	272	274
Romania10Y	4.90	4.70	5.10	5.20	5.40
spread (bps)	501	455	488	492	504
Slovakia 10Y	0.44	0.75	0.85	0.85	0.95
spread (bps)	55	60	63	57	59
Slovenia 10Y	0.54	0.80	0.90	0.90	1.00
spread (bps)	65	65	68	62	64
Serbia 5Y	3.91	3.96	3.90	3.93	3.95
DE10Y (BBG)*	-0.11	0.15	0.22	0.28	0.36

3M Money Market Rate					
	current	2019Q2	2019Q3	2019Q4	2020Q1
Croatia	0.47	0.50	0.50	0.50	0.50
Czech Republic	2.20	2.18	2.18	2.18	2.24
Hungary	0.16	0.22	0.30	0.45	0.60
Poland	1.72	1.72	1.72	1.72	1.72
Romania	3.28	3.20	3.70	3.60	3.50
Serbia	2.96	2.96	2.98	2.98	2.99
Eurozone	-0.31	-0.30	-0.30	-0.30	-

FX					
	current	2019Q2	2019Q3	2019Q4	2020Q1
EURHRK	7.43	7.32	7.42	7.45	7.42
forwards		7.43	7.43	7.43	7.43
EURCZK	25.75	25.65	25.51	25.31	25.03
forwards		25.77	25.77	25.77	25.77
EURHUF	325.6	319.0	320.0	322.0	322.0
forwards		328.8	328.8	328.8	328.9
EURPLN	4.31	4.31	4.32	4.29	4.29
forwards		4.31	4.31	4.31	4.31
EURRON	4.76	4.75	4.75	4.77	4.79
forwards		4.76	4.76	4.76	4.76
EURRSD	118.0	117.9	118.0	118.3	118.1
forwards		-	-	-	-
EURUSD	1.12	1.15	1.18	1.18	-

Key Interest Rate					
	current	2019Q2	2019Q3	2019Q4	2020Q1
Croatia	0.30	0.30	0.30	0.30	0.30
Czech Republic	2.00	2.00	2.00	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	-

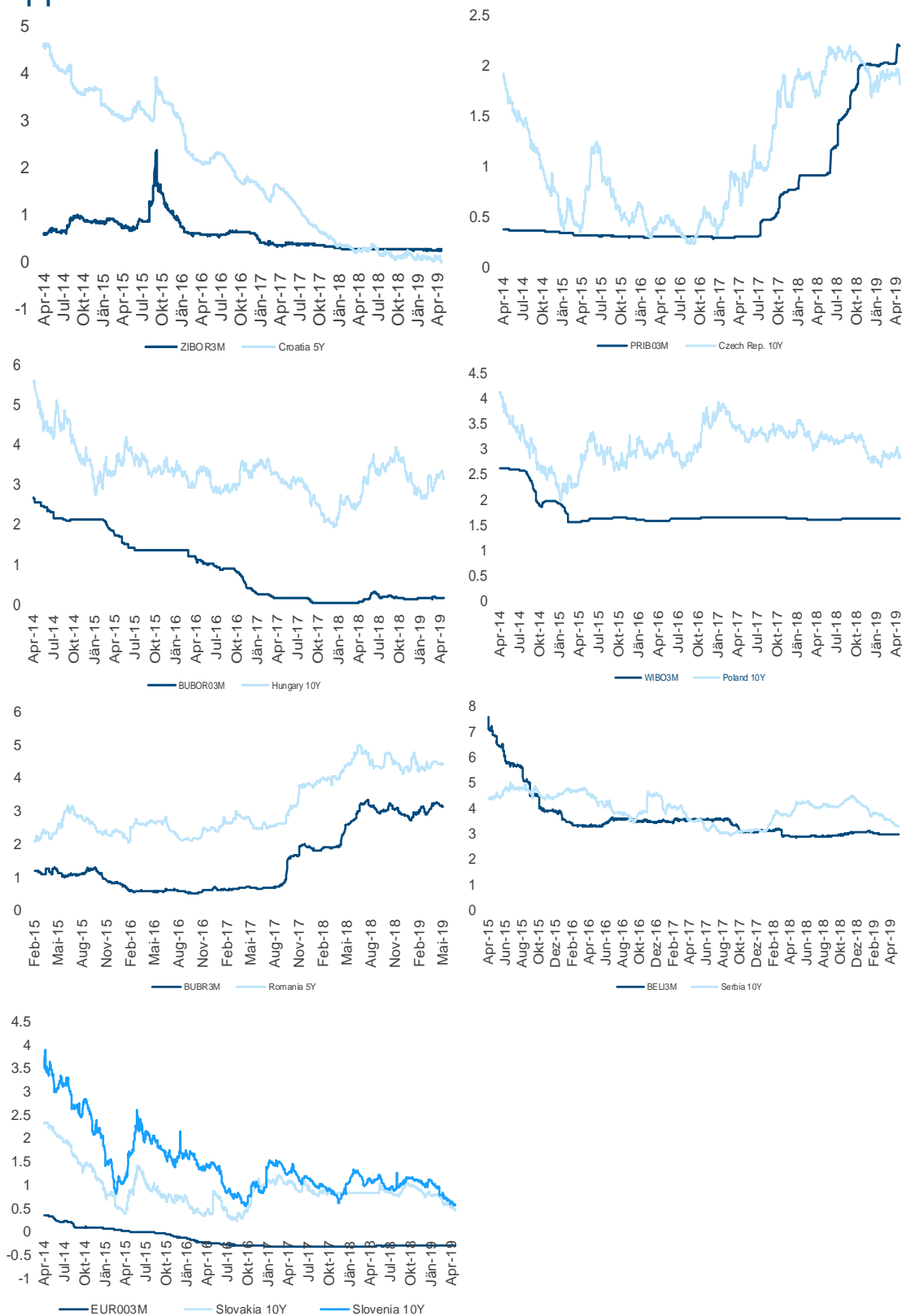
Macro forecasts

Real GDP growth (%)					Average inflation (%)					Unemployment (%)				
2017	2018f	2019f	2020f		2017	2018f	2019f	2020f		2017	2018f	2019f	2020f	
Croatia	2.9	2.6	2.3	2.3	Croatia	1.1	1.5	1.0	1.2	Croatia	11.3	8.4	7.4	6.4
Czech Republic	4.5	3.0	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	4.9	3.8	2.9	Hungary	2.4	2.8	3.1	2.9	Hungary	4.2	3.7	3.6	3.5
Poland	4.8	5.1	4.2	3.4	Poland	2.0	1.6	2.2	2.4	Poland	7.2	6.1	6.3	6.4
Romania	7.0	4.1	3.1	3.7	Romania	1.3	4.6	3.6	3.1	Romania	4.9	4.2	3.8	4.0
Serbia	2.0	4.3	3.0	3.3	Serbia	3.0	2.0	2.5	1.8	Serbia	13.5	12.7	12.2	11.7
Slovakia	3.2	4.1	3.4	3.6	Slovakia	1.3	2.5	2.5	2.5	Slovakia	8.1	6.5	6.3	5.8
Slovenia	4.9	4.5	3.2	3.1	Slovenia	1.4	1.7	1.3	1.5	Slovenia	6.6	5.1	4.2	3.7
CEE8 average	4.7	4.4	3.5	3.3	CEE8 average	1.9	2.4	2.5	2.4	CEE8 average	6.2	5.3	5.2	5.2

Public debt (% of GDP)					C/A (%GDP)					Budget Balance (%GDP)				
2017	2018f	2019f	2020f		2017	2018f	2019f	2020f		2017	2018f	2019f	2020f	
Croatia	77.8	74.1	71.4	69.3	Croatia	3.7	2.6	1.4	0.5	Croatia	0.9	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	73.4	70.8	68.4	66.6	Hungary	2.8	0.5	-0.1	0.7	Hungary	-2.2	-2.2	-1.8	-1.8
Poland	50.6	48.9	50.1	49.3	Poland	0.2	-0.4	-0.5	-0.7	Poland	-1.4	-0.4	-1.9	-2.6
Romania	35.2	35.0	35.1	35.3	Romania	-3.2	-4.5	-4.9	-5.3	Romania	-2.7	-3.0	-3.0	-2.5
Serbia	63.3	53.8	51.4	49.4	Serbia	-5.2	-5.2	-5.5	-5.2	Serbia	1.1	0.6	-0.5	-0.5
Slovakia	50.9	48.9	47.8	46.1	Slovakia	-2.0	-2.5	-2.4	-1.2	Slovakia	-0.8	-0.7	-0.7	-0.4
Slovenia	72.4	67.0	63.8	60.8	Slovenia	7.2	7.3	6.5	5.8	Slovenia	0.0	0.0	0.50	0.3
CEE8 average	50.4	48.3	47.9	46.9	CEE8 average	0.1	-0.7	-1.0	-1.0	CEE8 average	-0.9	-0.6	-1.3	-1.5

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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20 May 2019

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