

Measuring financial market inflation expectations – results of the 36th measurement (April 2002)

The April measurement of inflation expectations reveals no major changes in the analysts' opinions on future inflation in the Czech Republic or on the expected trend in the monitored financial market indicators. Inflation expectations remain favourable, and the koruna's ongoing appreciation trend has further shifted the expected CZK/EUR exchange rate and modestly decreased the estimates for the 1W PRIBOR at the one-month horizon. Most of the analysts, however, are not predicting a further reduction in rates. A moderate tightening of monetary policy at the close of the year is seen as the most likely scenario.

1. Inflation

IV-02	annual CPI (%)	
	1 year	3 years
min.	3,0	2,5
average	3,5	3,2
max.	4,2	4,0

The average estimate of annual consumer price inflation at the one-year horizon remained at 3.5% for the third consecutive month. The average estimate for the three-year horizon fell from 3.3% to 3.2%. No rise in inflation pressures is expected in the near future. The growth rate of the annual CPI should decrease until the middle of the year, then a gradual rise can be expected. The analysts also expect a gradual halt in the downward trend in industrial producer

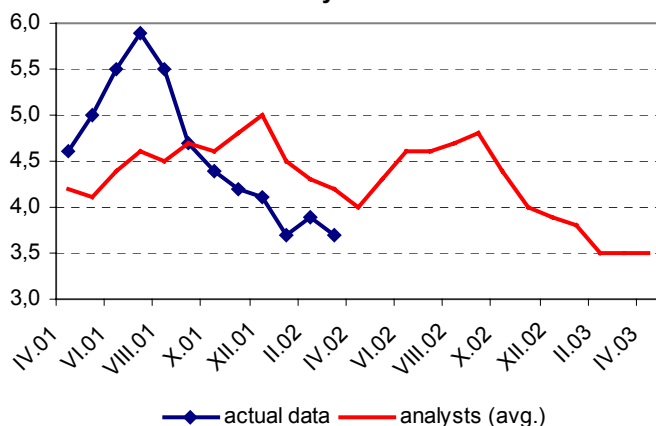
prices, which have up to now been affected by low oil prices, falling world demand (associated with the cooling of the global economy) and the strengthening koruna. The expected recovery will feed through into the Czech economy. Although the March figures from the USA gave rise to a change in expectations regarding the development of the world economy, the analysts expect the signs of stronger global economic growth and higher prices of raw materials to be offset in large part by the strong domestic currency. The expectation therefore persists that the CNB will tighten monetary policy moderately at the close of this year

As with the overall prediction, there were no major changes in the average estimates within the two groups of analysts surveyed. The domestic analysts expect average annual CPI inflation of 3.4% in April 2003, whereas the average estimate of the foreign analysts is 3.7%. The expectations for the three-year horizon are similar: the average forecast of the domestic analysts remains at 3.2% and that of the foreign analysts at 3.4%. For the one-year horizon, the range of the predictions remains higher within the group of foreign analysts (3.0%–4.2%, compared with 3.2%–3.5% for the domestic analysts). For the three-year horizon, however, the range of the domestic analysts' estimates widened considerably in this measurement (foreign: 2.9%–4.0%; domestic: 2.5%–3.7%).

The main inflation factors and risks:

- Expansionary fiscal policy.
- Growth in prices of raw materials, most notably crude oil

CPI - actual data + predictions of analysts (avg.) for 1 year



Prediction for Month of prediction	annual CPI	
	1 Y %	3 Y %
IV-01	4,0	3,4
VI-01	4,6	3,8
IX-01	4,8	3,6
XII-01	3,9	3,6
I-02	3,8	3,4
III-02	3,5	3,3
IV-02	3,5	3,2

2. Interest rates

IV-02	1W PRIBOR (%)		12M PRIBOR (%)		12M/1W spread (%)		5Y IRS (%)		CR 6,55/11 yield	
	1 month	1 year	1 month	1 year	1 month	1 year	1 month	1 year	1 month	1 year
min.	4,2	3,9	4,3	4,0			5,3	5,3	5,4	5,4
average	4,2	4,6	4,4	4,9	0,2	0,2	5,3	5,7	5,5	5,9
max.	4,3	5,0	4,6	5,3			5,4	6,0	5,6	6,4

The expected interest rate levels remained broadly the same in the April measurement as in March. The signs of economic recovery in the USA suggest the possibility of an earlier and more considerable tightening of monetary policy by the Fed than previously expected. Also, the market no longer expects a reduction in rates from the ECB; on the contrary, an increase can be expected in Q4.

The short-term and long-term domestic rates expected at the one-month horizon correspond to the current market situation. The continuing robust appreciation of the koruna led to speculation on the market of a further reduction of the CNB repo rate. This was reflected in a shift in the expected 1W and 12M PRIBOR rates at the one-month horizon (4.2% and 4.4% respectively). However, the analysts do not consider a rate reduction very likely.

The predictions for short-term rates at the one-year horizon reflect the expectation of a moderate tightening of CNB monetary policy at the close of the year – a 0.25% increase in the 2W repo rate.

The predictions for long-term koruna rates and yields at one year derive from expected developments in the eurozone.

The average predictions in the two groups of analysts differ only very slightly, and virtually only at the one-year horizon, where the foreign analysts expect rates to be around 0.1% higher on average than the domestic analysts.

The analysts' opinions on the appropriate 2W repo rate setting were slightly lower than in the previous measurement, this time ranging between 4.0% and 5.0% (compared with 4.0% and 5.5% in March). The average of the responses is 4.33% (4.43% in March). The average for the group of domestic analysts is 4.25% (4.29% in March) and that for the foreign analysts is 4.44% (4.63% in March).

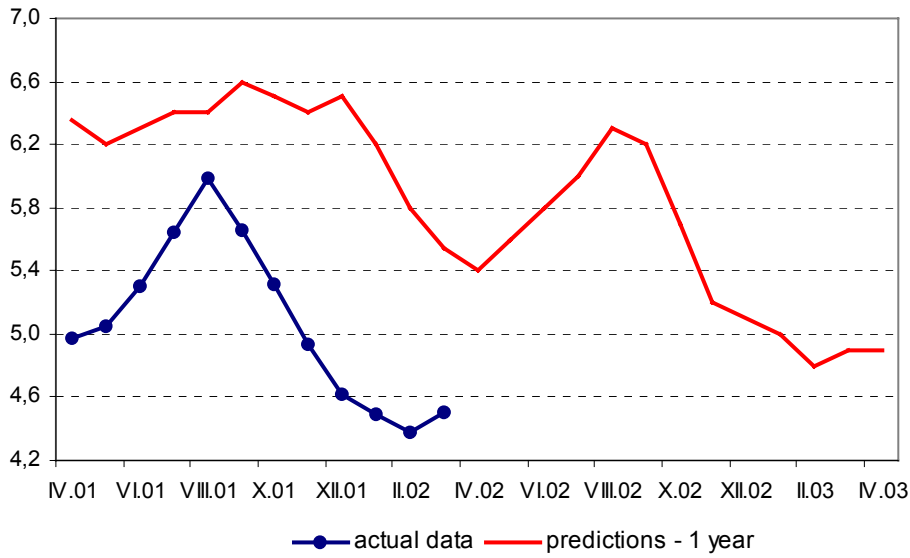
Prediction for Month of prediction	1W PRIBOR		12M PRIBOR		12M/1W spread		5Y IRS		CR 6,55/11 yield	
	1 M	1 Y	1 M	1 Y	1 M	1 Y	1 M	1 Y	1 M	1 Y
	%		%		%		%		%	
IV-01	5,0	5,2	5,0	5,4	0,0	0,2	5,8	6,2		
VI-01	5,0	5,5	5,2	5,8	0,2	0,3	6,2	6,7	6,8	7,2
IX-01	5,4	5,9	5,8	6,2	0,4	0,3	6,4	6,7	6,7	7,0
XII-01	4,7	4,9	4,7	5,1	0,0	0,2	5,3	5,6	5,6	5,8
I-02	4,6	4,8	4,5	5,0	-0,2	0,1	5,1	5,7	5,3	5,8
III-02	4,3	4,6	4,5	4,9	0,2	0,2	5,3	5,7	5,5	5,9
IV-02	4,2	4,6	4,4	4,9	0,2	0,2	5,3	5,7	5,5	5,9

expected yield of CR 6,40/10

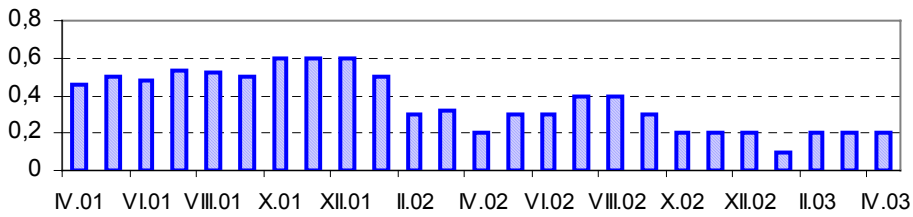
Actual values of indicators on the day of deadline for forecasts

	1T PRIBOR	12M PRIBOR	spread 12M/1T	5R IRS	výnos CR 6,55/11	analysts - avg. 2W repo rate
9.4.2002	4,28	4,44	0,16	5,25	5,45	4,33

12M PRIBOR - analysts' predictions for 1 year (avg.) and actual data (avg.)



12M/1W spread (predictions for 1 year)



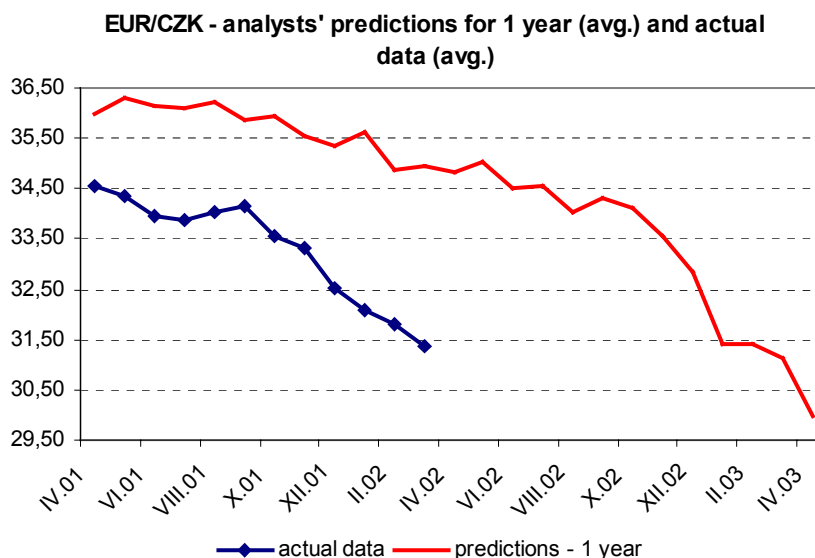
3. Exchange rate

IV-02	EUR/CZK	
	1 month	1 year
min.	29,50	28,00
average	30,49	29,98
max.	31,00	31,50

Prediction for Month of prediction	exchange rate	
	1 month	1 year
IV-01	34,60	34,82
VI-01	34,02	34,52
IX-01	34,05	34,32
XII-01	32,94	32,85
I-02	32,23	31,42
III-02	31,62	31,15
IV-02	30,49	29,98

With the domestic currency continuing to appreciate, the expected CZK/EUR exchange rate is shifting further. The average expectations at the one-month horizon are again around the level current at the time the predictions were dispatched

(the fixing on 9 April was 30.220). For the one-year horizon, the average prediction is CZK 29.98/EUR. At the one-month horizon the estimates of the two groups analysts differ by 60 hellers (domestic: CZK 30.73/EUR on average; foreign: CZK 30.13/EUR on average). At the one-year horizon the difference is greater, reaching 84 hellers (domestic: CZK 30.32EUR on average; foreign: CZK 29.48 on average). The range of the estimates at the one-year horizon remains traditionally much greater in the group of foreign analysts, standing at CZK 3.50 in the April measurement. In the group of domestic analysts, the range remains narrow at CZK 1.30.



The strong appreciation of the koruna over the last month was bolstered by positive macroeconomic figures (GDP for 2001 Q4, the balance of payments for 2001 Q4 and the February trade surplus) indicating that the Czech economy coped with the weaker external demand and strong koruna in this period. In addition to inflow of foreign direct investment and the prospect of early accession of the Czech Republic to the EU, however, the analysts attribute the rapid appreciation to market speculation on the conversion of at least part of the proceeds of privatisation on the market. They feel that currently the CNB's interventions can slow the appreciation only in the short term. The only thing that can change this is the conversion of the state's incomes from the sale of Transgas and the distribution companies – by convincing traders of the validity of the agreement between the CNB and the Government. With the implementation of this agreement, the central bank's interventions should be more effective and slow the appreciation of the koruna to an acceptable level.

The verbal and direct interventions of the CNB are counteracting the appreciation of the koruna. Also strengthening are concerns about the tougher export environment. The excessively strong koruna, combined with the weaker external demand, could have devastating effects on some Czech exporters. The export figures over the months ahead will be of key importance to the analysts. The problems in the eurozone could pass through fully into the domestic macroeconomic data in Q2. A temporary depreciation of the koruna can also be expected in connection with the June elections. In the medium term, the state of public finances remains the biggest risk factor for the koruna.