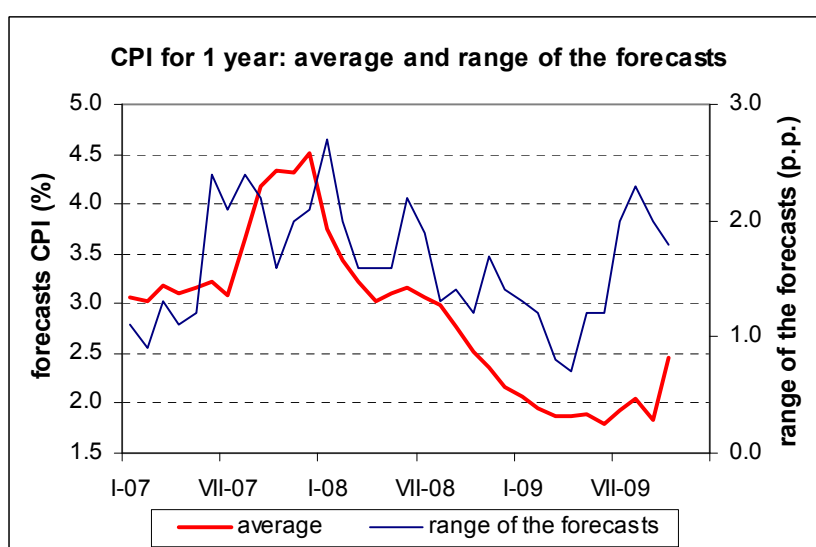


Measuring financial market inflation expectations – Results of the 126th Measurement (October 2009)

Eight domestic and one foreign analyst sent in their predictions for inflation and other indicators to the CNB's October survey. The expected inflation rate at the one-year horizon increased noticeably compared to the previous survey. This was due to a rise in indirect taxes as a result of government austerity measures. This, together with weaker domestic demand, had a negative effect on the GDP growth forecast for next year. Only three analysts expect key interest rates to be lowered at the CNB Bank Board's November meeting; the remaining six expect no change. The exchange rate forecast was shifted towards weaker levels, probably because of the actual depreciation of the koruna. Owing to planned wage cuts in the state sector and the still adverse labour market situation, nominal wage growth was also reduced.

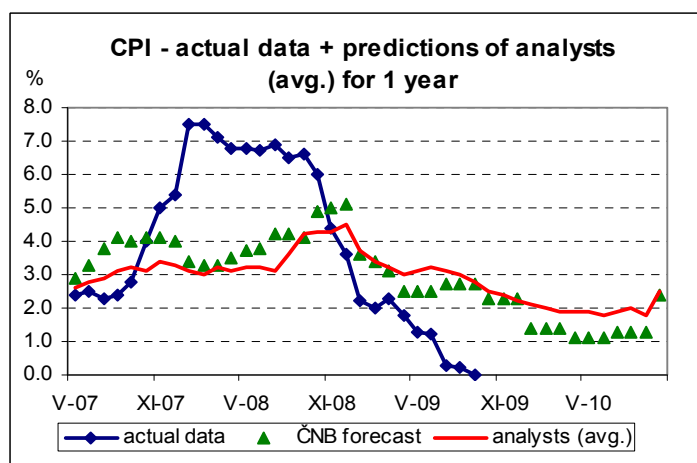
1. Inflation

X-09	annual CPI (%)	
	1 year	3 years
min.	1.5	1.8
average	2.5	2.5
max.	3.3	4.0



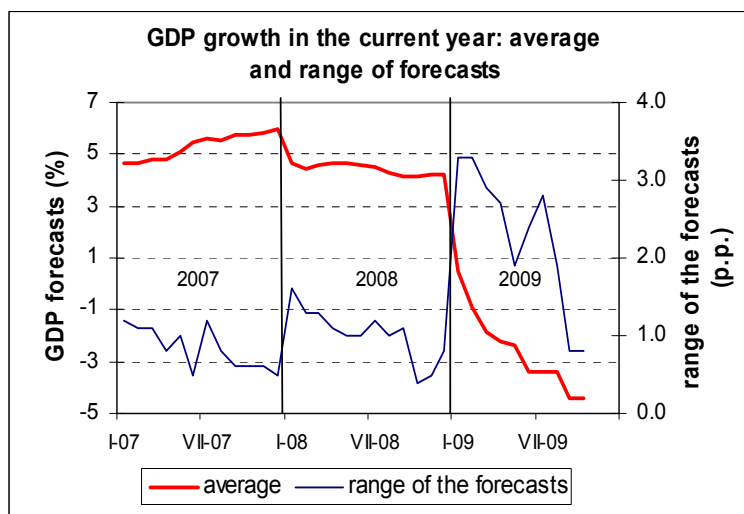
The expected increase in the price level at the one-year horizon shifted markedly upwards compared to the last survey. The average annual inflation forecast increased from 1.8% in September to 2.5% in October. The main reason was the adoption of a budgetary package for next year, which assumes an increase in value added tax and excise duties. The impact of the tax increase will thus considerably exceed the effect of the decline in some regulated prices and lower demand-pull inflation expected by many analysts. At the three-year horizon, the average inflation forecast remained unchanged at 2.5%. While the range of the one-year forecasts narrowed slightly owing to an increase in the minimum estimate, that of the three-year forecasts widened somewhat owing to a small decline in the minimum value.

Prediction for Month of prediction	annual CPI		CNB 1 Y %
	1 Y %	3 Y %	
X-08	2.5	2.5	4Q: 2,0
XI-08	2.2	2.5	
II-09	2.0	2.4	1Q: 1,4
IV-09	1.9	2.4	
VII-09	1.9	2.6	2Q: 1,1
VIII-09	2.0	2.7	
IX-09	1.8	2.5	3Q: 1,6
X-09	2.5	2.5	4Q: 2,4



2. Gross domestic product

X-09	GDP growth in	
	current year	next year
min	-4.8	0.8
average	-4.4	1.6
max	-4.0	2.5



Prediction for Month of prediction	GDP growth in	
	current year	next year
	%	
X-08	4.2	3.2
XI-08	4.2	2.4
II-09	-0.9	1.8
IV-09	-2.2	1.2
VII-09	-3.4	1.3
VIII-09	-3.4	1.6
IX-09	-4.4	1.9
X-09	-4.4	1.6

The forecast for this year's GDP decline remained unchanged compared to the previous survey. Domestic economic output is thus expected to decrease by 4.4% year on year in 2009. However, the outlook for next year is more pessimistic than in September. According to the current results, the Czech economy will grow by only 1.6% in 2010.

A further rise in unemployment and very low wage growth are expected to have an adverse effect on household consumption in 2010. In the analysts' opinion, economic growth in 2010 will also be slowed to a large extent by the government's austerity measures. Investment activity will not be strong either, because of low production capacity utilisation and low demand (weak orders of capital goods). One of the major risks to GDP growth is the evolution of inventories, which have recently been very volatile. The economic recovery could also be negatively affected by a too strong appreciation of the koruna (with an adverse impact on exports) or a slower recovery of the European or German economy.

3. Interest rates

X-09	2W repo rate (%)		12M PRIBOR (%)		5Y IRS (%)		10Y IRS (%)	
	1 month	1 year	1 month	1 year	1 month	1 year	1 month	1 year
min.	1.00	1.00	2.25	2.25	3.10	3.50	3.55	3.85
average	1.17	1.58	2.38	2.67	3.33	3.80	3.78	4.32
max.	1.25	2.50	2.50	3.40	3.50	4.45	4.50	4.90

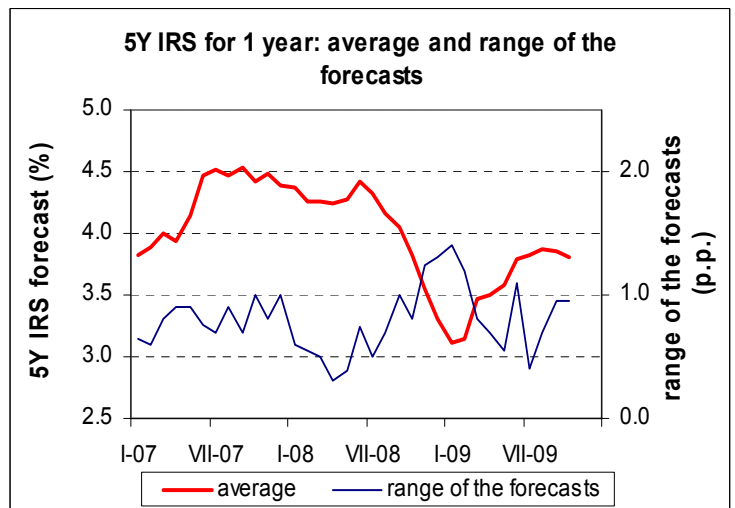
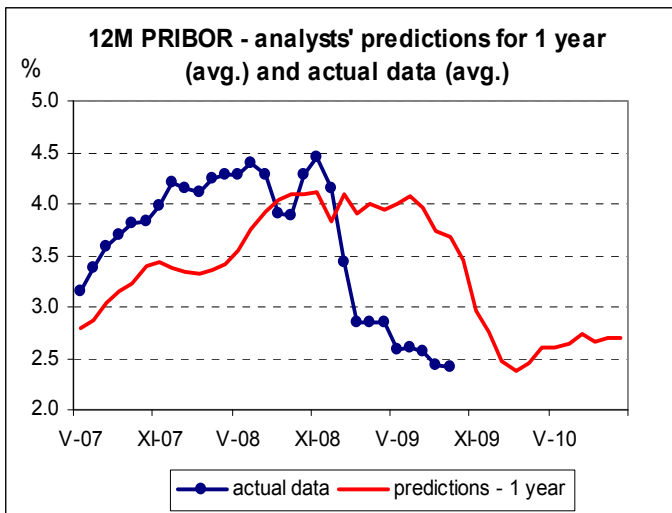
The forecasts for key interest rates and IRS yields decreased slightly compared to September at both the one-month and one-year horizons. The only exception was the ten-year IRS yield at the one-year horizon, which increased slightly. The biggest downward shifts were recorded for the 2W repo rate at the one-year horizon and the 5Y IRS at the one-month horizon. Six of the nine respondents expect the CNB Bank Board to leave key interest rates unchanged at its November meeting. The remaining three expect a rate reduction of 25 basis points. A return to monetary policy tightening is expected in the second half of next year.

According to the analysts, a slower monetary policy tightening could be fostered by a runaway appreciation of the koruna or a slower recovery of the domestic economy. By contrast, a faster rise in interest rates might result from a brisker recovery in the EMU or globally accelerating inflation as a consequence of a wrong exit strategy from the quantitative easing.

Prediction for Month of prediction	2W repo rate		12M PRIBOR		5Y IRS		10Y IRS	
	1 M	1 Y	1 M	1 Y	1 M	1 Y	1 M	1 Y
	%		%		%		%	
X-08	3.22	2.89	3.91	3.46	3.25	3.83	3.71	4.16
XI-08	2.53	2.06	4.19	2.96	3.17	3.55	3.41	4.03
II-09	1.69	1.48	2.52	2.38	2.86	3.15	3.33	3.63
IV-09	1.64	1.77	2.79	2.59	3.26	3.49	3.77	4.06
VII-09	1.36	1.69	2.53	2.73	3.40	3.83	3.87	4.48
VIII-09	1.25	1.86	2.39	2.66	3.44	3.88	3.85	4.43
IX-09	1.25	1.69	2.39	2.69	3.44	3.86	3.81	4.29
X-09	1.17	1.58	2.38	2.67	3.33	3.80	3.78	4.32

Actual indicator values as of forecast deadline

	2W repo rate	12M PRIBOR	5Y IRS	10Y IRS
15.10.	1.25%	2.42%	3.52%	3.89%

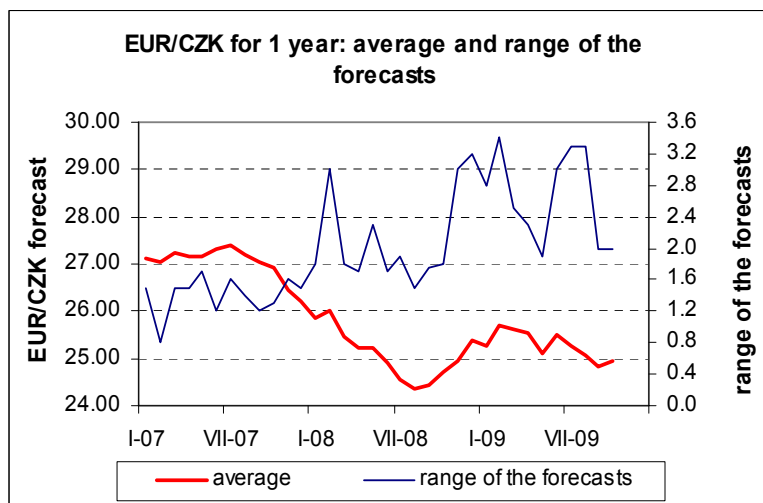


4. The exchange rate

X-09	EUR/CZK	
	1 month	1 year
min.	25.40	24.00
average	25.82	24.96
max.	26.30	26.00

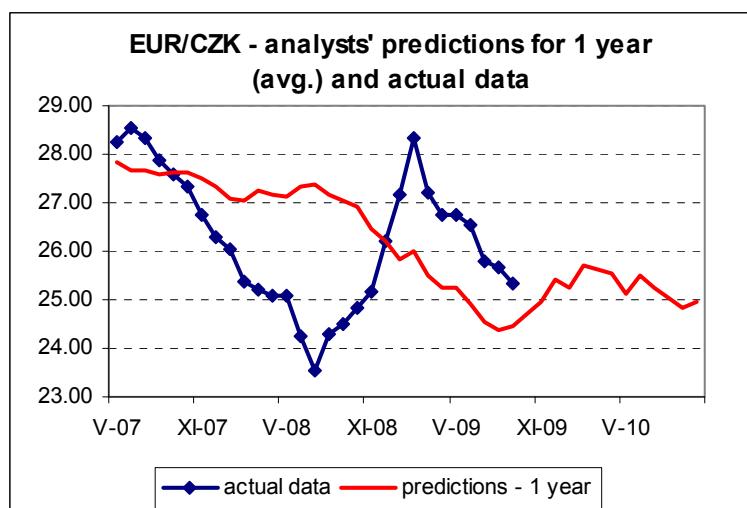
Actual exchange rate

15.10.	25.35
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The consensus forecast for the exchange rate was shifted towards weaker levels at both the one-month and one-year horizons compared with the September survey, with the one-month forecast showing the larger decline. The main reason will probably be the weakening of the actual exchange rate by about 50 hellers. Many analysts had predicted such a correction but had already reduced its expected magnitude in the previous survey because of the trade surplus and strengthening confidence among foreign investors. In the analysts' opinion, however, the depreciation should not last long and the koruna should gradually return to an appreciation trend.

Prediction for Month of prediction	exchange rate EUR/CZK	
	1 month	1 year
X-08	24.90	24.72
XI-08	25.50	24.96
II-09	28.64	25.71
IV-09	27.12	25.52
VII-09	26.32	25.25
VIII-09	26.07	25.05
IX-09	25.48	24.84
X-09	25.82	24.96

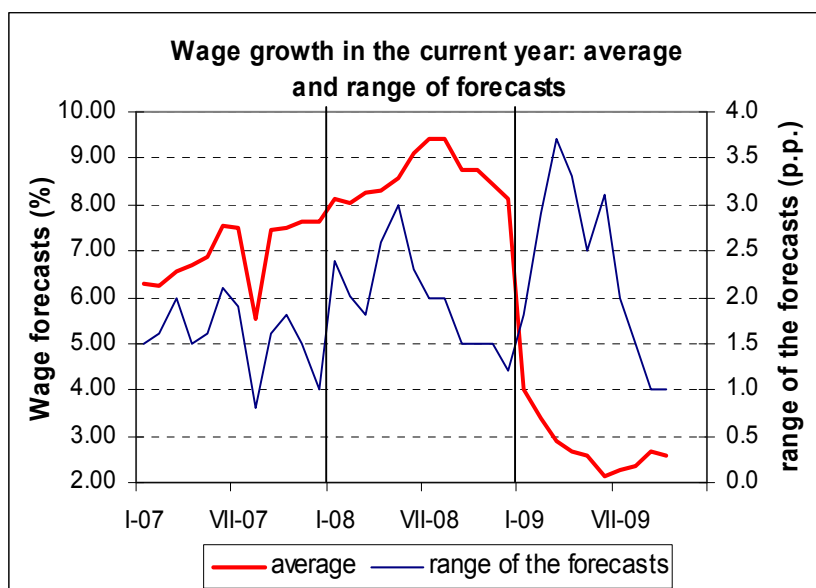


The risks of the forecast are becoming balanced as the koruna depreciates. Domestic political developments, particularly the results of the parliamentary elections next year, are now regarded as the main depreciation risk. There is no guarantee that the new elections will produce a sufficiently strong government able to rely comfortably on majority support in parliament. By contrast, the exchange rate could appreciate immediately if foreign investors again show sudden interest in the koruna. According to some estimates, only one-fifth to one-third of the original investment volumes have returned to the Czech Republic following the dramatic sell-offs.

5. Wages

X-09	Wage growth in	
	current year	next year
min	2.0	0.2
average	2.6	1.9
max	3.0	3.5

Prediction for Month of prediction	wage growth in	
	current year	next year
	%	
X-08	8.8	6.7
XI-08	8.4	6.1
II-09	3.4	4.2
IV-09	2.7	3.8
VII-09	2.3	3.3
VIII-09	2.4	3.4
IX-09	2.7	2.7
X-09	2.6	1.9



The average forecasts for wage growth decreased compared to the previous month. For this year the change was only negligible (0.1 p.p.), but a more pronounced decline (of 0.8 p.p., due largely to planned wage cuts in the state sector) is expected next year. According to the analysts, the labour market situation will remain very complicated and a large excess of job applicants over vacancies will slow nominal wage growth even further. This is consistent with the worse outlook for economic growth next year. The forecast for wage growth in the business sector was completely unchanged (2.4% in 2009 and 4.3% in 2010), whereas in the non-business sector a much worse trend is expected owing to the government's austerity measures (+2.1% in 2009 and -3.1% in 2010).

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