

FINANCIAL MARKET INFLATION EXPECTATIONS - DECEMBER

Financial Market Department
Operations Analyses Division

2014

Eleven domestic and two foreign analysts sent in their contributions to the final survey of 2014. The results indicate that, according to the analysts, consumer prices will rise more slowly at the one-year horizon, whereas inflation expectations remain anchored at the CNB's inflation target at the three-year horizon. Although the GDP growth estimate for 2014 also remained unchanged, the outlook for 2015 is more pessimistic than in the previous survey. None of the respondents expects key rates to increase next year. The forecasts for swap rates continue to track the downward tendencies in IRS rates in the market. The expected date of the exit from the exchange rate commitment was again shifted to the more distant future, in one case to 2017. At the same time, the analysts believe that the improvement in the labour market is opening up more space for nominal wage growth than they expected in November.

DOMESTIC ANALYSTS	I.	II.	III.	IV.	V.	VI.	VII.	VIII.	IX.	X.	XI.	XII.
David Navrátil, Česká spořitelna	+	+	+	+		+	+	+	+	+		
David Marek, Deloitte Czech Republic	+	+	+	+	+	+		+	+	+	+	+
Jan Vejmělek, Komerční banka	+	+	+	+	+	+	+	+	+	+	+	+
Pavel Sobíšek, Unicredit Global Research	+	+	+	+	+	+	+	+	+	+	+	+
Michal Brožka, Helena Horská, Raiffeisenbank	+	+	+	+	+	+	+	+	+	+	+	+
Petr Dufek, ČSOB	+	+	+	+	+	+	+	+	+	+	+	+
Petr Sklenář, J&T Banka	+	+	+	+	+	+	+	+	+	+	+	+
Radomír Jáč, Generali PPF	+	+	+	+			+	+	+	+	+	+
Jaromír Šindel, Citi	+			+	+			+	+			+
Tomáš Holinka, Moody's Analytics	+	+	+	+	+	+	+	+	+	+	+	+
Jan Kudláček, AXA	+	+	+	+	+	+	+	+	+	+	+	+
Jakub Seidler, ING								+	+	+	+	+
FOREIGN ANALYSTS												
Magdalena Polan, Goldman Sachs	+	+		+	+		+			+		
Alex Nice, The Economist Intelligence Unit	+	+		+	+		+	+				+
Nicolaie Alexandru, JP Morgan		+	+	+	+	+	+	+	+	+	+	+

We would like to thank everyone who contributed to this survey of financial market inflation expectations.

Prague, 16 December 2014

FORECAST FOR Y/Y CPI GROWTH (%)

December	CPI	
	1Y	3Y
2014		
minimum	0.9	1.3
average	1.5	2.0
maximum	1.9	2.3

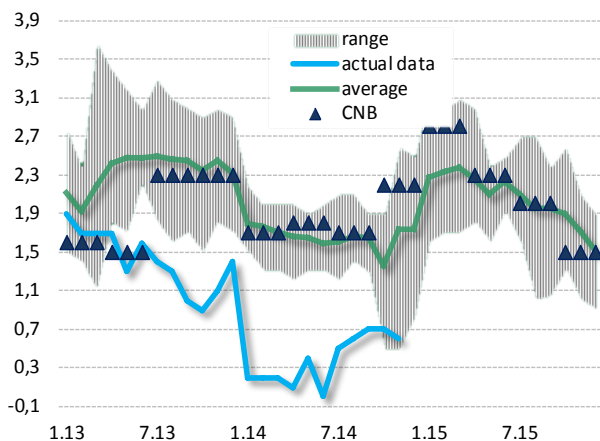
1Y AND 3Y FORECAST FOR CPI GROWTH (%)

Date of Prediction	ANALYSTS		CNB (%)
	1Y	3Y	1Y
12.13	1.7	2.1	3Q: 1,7
2.14	2.3	2.1	4Q: 2,2
4.14	2.3	2.1	1Q: 2,8
6.14	2.2	2.0	
8.14	2.0	2.1	2Q: 2,3
10.14	1.9	2.0	3Q: 2,0
11.14	1.7	2.0	
12.14	1.5	2.0	4Q: 1,5

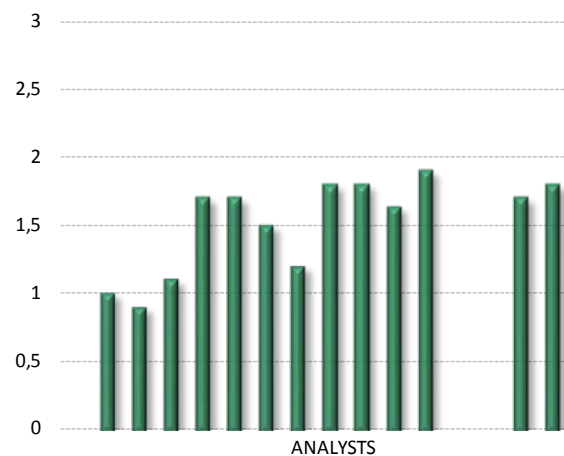
According to the CZSO, annual CPI inflation rose by 0.6% in November, 0.1 pp less than in October. The analysts' average forecast at the one-year horizon also shifted downwards by 0.2 pp in the December survey, to 1.5%. The analysts' forecast at the three-year horizon was again unchanged, remaining at the CNB's 2% inflation target. The range of the extreme forecasts narrowed again at the one-year horizon due a larger decline in the maximum value, but widened at the three-year horizon due a decline in the minimum value.

The main factors that will affect consumer prices in the months ahead include oil prices in world markets. Their decrease will exert downward pressure on inflation in the Czech Republic. According to some of the analysts, the probability of deflation increased again. In this respect they are considering whether the central bank should respond if inflation turns temporarily negative due to falling oil prices, i.e. a cost shock.

CPI: ACTUAL DATA AND 1Y PREDICTIONS OF ANALYSTS (AVERAGE) AND OF CNB (%)



CPI AT 1Y: PREDICTIONS OF INDIVIDUAL ANALYSTS



FORECAST FOR GDP GROWTH (%)

December 2014	end of year	
	current	current+1Y
minimum	2.2	2.0
average	2.4	2.3
maximum	2.6	2.6

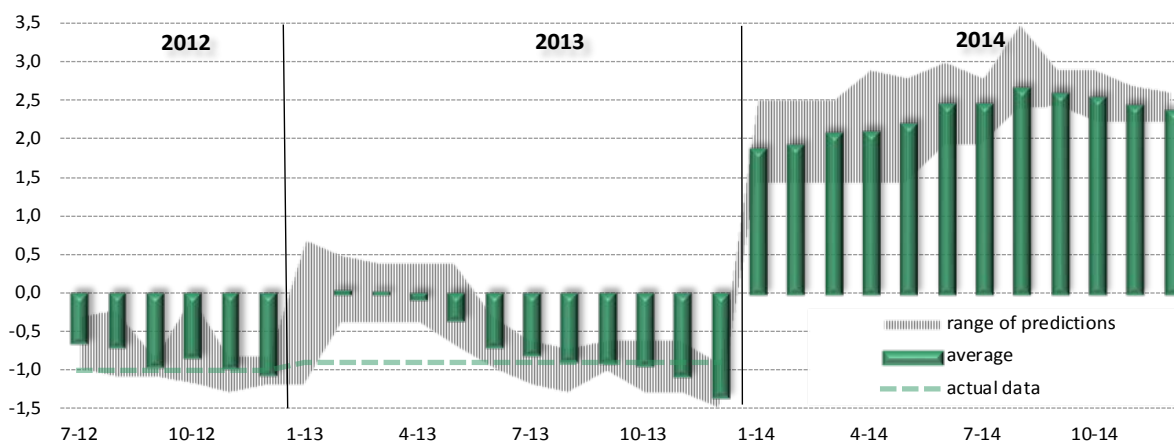
FORECAST FOR GDP GROWTH (%)

Date of Prediction	end of year	
	current	current+1Y
12.13	-1.3	1.9
2.14	1.9	2.5
4.14	2.1	2.5
6.14	2.5	2.7
8.14	2.7	2.8
10.14	2.5	2.5
11.14	2.4	2.4
12.14	2.4	2.3

The CZSO revised its estimate for annual growth of the domestic economy in 2014 Q3 from 2.3% to 2.4%. The analysts' view of GDP growth this year was unchanged at 2.4%, whereas the forecast for next year decreased by 0.1 pp to 2.3%. This is the first time since 2011 that the forecast for next year has been below the estimate for the current year. The range of the extreme forecasts narrowed slightly at both monitored horizons due to a decline in the maximum values.

According to the analysts, the main risks to future economic growth in the Czech Republic include weaker economic growth in export markets, i.e. in Germany and other key European countries in particular. A slide of the EMU into recession, which would be accompanied by deflation, or a hard landing of the Chinese economy could have a major negative impact on Czech GDP. The analysts see other risks in geopolitical developments and potential economic sanctions against Russia or a reduction in gas supplies from Russia.¹

GDP GROWTH IN CURRENT YEAR: AVERAGE AND RANGE OF PREDICTIONS



¹ The currency crisis in Russia erupted in full after the cut-off date of this survey.

FORECAST FOR 2W REPO, 12M PRIBOR AND 5Y AND 10Y IRS (%)

Date of Prediction	2W repo rate		12M PRIBOR		5Y IRS		10Y IRS	
	1M	1Y	1M	1Y	1M	1Y	1M	1Y
12.13	0.05	0.05	0.60	0.73	1.21	1.71	2.02	2.44
2.14	0.05	0.14	0.56	0.73	1.17	1.61	1.96	2.46
4.14	0.05	0.12	0.57	0.80	1.20	1.74	1.90	2.41
6.14	0.05	0.12	0.53	0.70	0.83	1.43	1.52	2.08
8.14	0.05	0.05	0.51	0.60	0.74	1.11	1.33	1.75
10.14	0.05	0.05	0.51	0.60	0.62	0.98	1.13	1.60
11.14	0.05	0.05	0.51	0.59	0.57	0.92	1.03	1.51
12.14	0.05	0.05	0.51	0.59	0.53	0.86	0.96	1.36

FORECASTS: MINIMUM, AVERAGE AND MAXIMUM 2W REPO, 12M PRIBOR, 5Y AND 10Y IRS (%)

December 2014	2W repo rate		12M PRIBOR		5Y IRS		10Y IRS	
	1M	1Y	1M	1Y	1M	1Y	1M	1Y
minimum	0.05	0.05	0.50	0.50	0.25	0.70	0.90	1.15
average	0.05	0.05	0.51	0.59	0.53	0.86	0.96	1.36
maximum	0.05	0.05	0.55	0.75	0.60	1.00	1.10	1.60

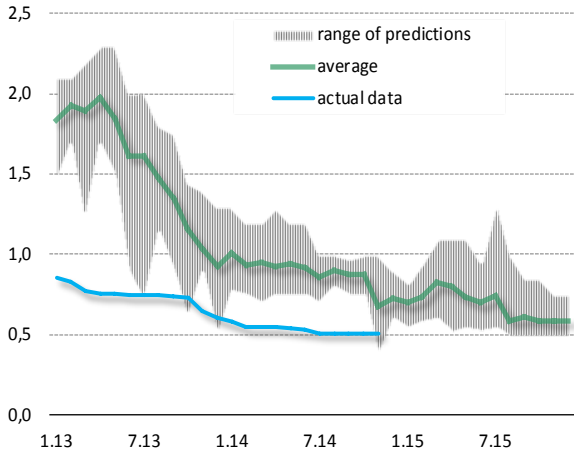
ACTUAL INDICATOR VALUES AS OF FORECAST DEADLINE (%)

	2W repo rate	12M PRIBOR	5Y IRS	10Y IRS
12.12.	0.05	0.51	0.55	0.95

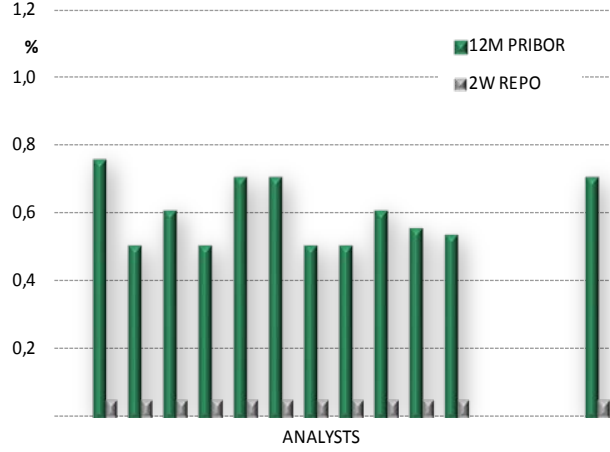
The view of the path of key interest rates in the coming 12 months remained unchanged in December, so none of the respondents expects the 2W repo rate to increase. Both the one-month and one-year forecasts for the 12M reference PRIBOR rate remained at their November level.

The IRS forecasts tracked the decline in corresponding market rates, going down by 4–15 bp. The largest shift was observed for the one-year 10Y IRS forecast. According to the analysts, the level of IRS rates will continue to be determined largely by external factors such as global economic developments and the related response of central banks.

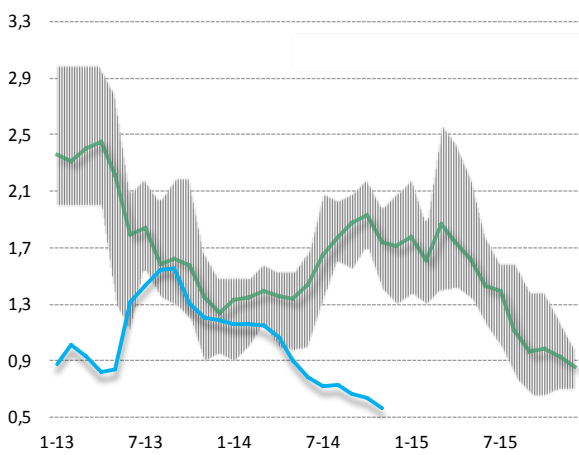
12M PRIBOR AT 1Y : ACTUAL DATA, AVERAGE AND RANGE OF PREDICTIONS



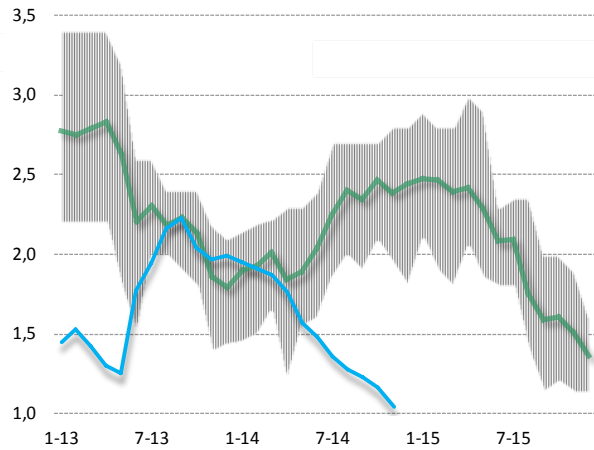
2W REPO AND 12M PRIBOR: 1Y PREDICTIONS OF INDIVIDUAL ANALYSTS



5Y IRS AT 1Y: AVERAGE AND RANGE OF PREDICTIONS



10Y IRS AT 1Y: AVERAGE AND RANGE OF PREDICTIONS



1M AND 1Y EXCHANGE RATE FORECAST

Date of Prediction	EUR/CZK	
	1M	1Y
12.13	27.45	26.94
2.14	27.42	26.95
4.14	27.40	26.96
6.14	27.41	26.98
8.14	27.73	27.33
10.14	27.48	27.26
11.14	27.54	27.27
12.14	27.60	27.34

EXCHANGE RATE FORECAST

December 2014	EUR/CZK	
	1M	1Y
minimum	27.40	27.00
average	27.60	27.34
maximum	27.80	27.92

ACTUAL EUR/CZK AS OF FORECAST DEADLINE

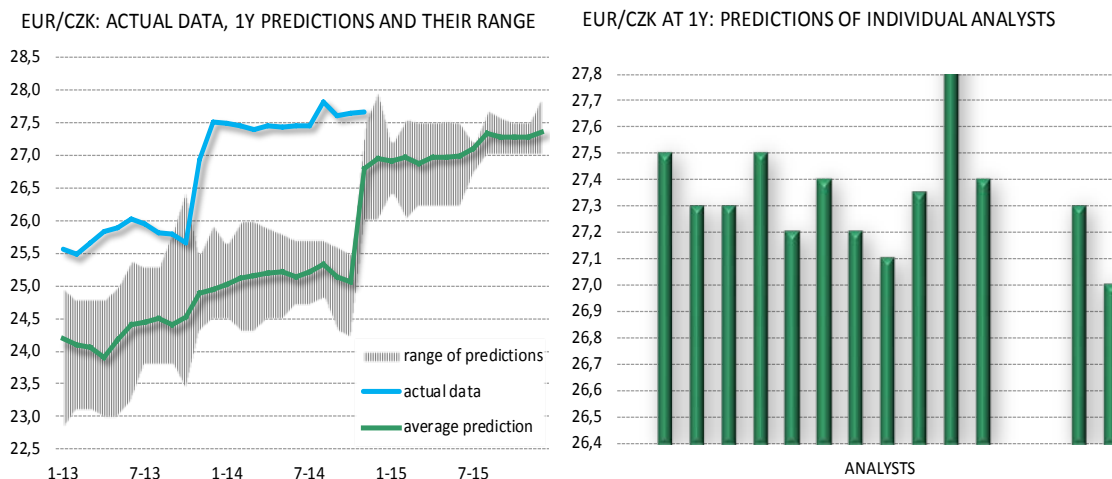
12.12.	27.59
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The koruna appreciated slightly against the euro compared to the previous survey (from CZK 27.65 to CZK 27.59). This change was not reflected in the analysts' forecasts this time. On the contrary, they shifted to slightly weaker levels. According to the analysts, the koruna is expected to remain close to CZK 27.60 to the euro until mid-January 2015 and gradually appreciate to CZK 27.34 during 2015. If the European and, subsequently, Czech economy slides into recession, the koruna's exchange rate could depreciate to weaker levels.

EXPECTED EXIT FROM EXCHANGE RATE COMMITMENT

Expected exit	Number of analysts	
	October survey	November survey
1Q 2016	4	3
2Q 2016	3	2
3Q 2016	1	4
4Q 2016	2	2
2016 (Q nespecifikováno)	1	0
1Q 2017	0	1

The date of the expected exit from the current exchange rate commitment is being gradually postponed. Most respondents believe now that the CNB will exit from its exchange rate commitment in 2016 Q3 (see the table above). For the first time in a long time, the opinion was expressed that the exit might not occur until 2017 Q1.



FORECAST FOR NOMINAL WAGE GROWTH (%)

December 2014	year end	
	current	current+1Y
minimum	2.5	2.9
average	2.8	3.3
maximum	3.1	3.8

FORECAST FOR NOMINAL WAGE GROWTH (%)

Date of Prediction	year end	
	current	current+1Y
12.13	0.8	2.3
2.14	2.1	2.8
4.14	2.2	3.1
6.14	2.4	2.9
8.14	2.5	3.0
10.14	2.6	3.1
11.14	2.8	3.1
12.14	2.8	3.3

The average nominal wage growth forecast for 2014 remained at the November level of 2.8%, while that for 2015 increased by 0.2 pp to 3.3% despite expected slower GDP growth.

The analysts who made a distinction between the forecast for wage growth in the business sector and that in the non-business sector estimate that wages in the business sector will grow by 2.9% in 2014 and by 3.5% in 2015, while wages in the non-business sector will rise by 2.6% in 2014 and by 3.6% in 2015.

WAGE GROWTH - END OF CURRENT YEAR: AVERAGE AND RANGE OF PREDICTIONS (%)

