

FINANCIAL MARKET INFLATION EXPECTATIONS - JUNE

Financial Market Department
Operations Analyses Division

2019

Thirteen domestic and three foreign analysts took part in the CNB's June survey. The results of the survey show that the average inflation forecast shifted slightly upwards amid higher expected nominal wage growth. The expected inflation rate rose to the 2% inflation target at the three-year horizon, exceeding it slightly at the one-year horizon. The economic growth outlook remains unchanged and the majority of respondents do not expect the CNB's monetary policy to be tightened further over the next 12 months. In this context and in the context of market developments, the forecasts for both swap and interbank reference rates decreased. The expected path of the koruna exchange rate moved to a weaker level at the one-year horizon. According to the analysts, the koruna is thus expected to stand close to the level reached as of the cut-off date of this survey in June 2020.

DOMESTIC ANALYSTS	I.	II.	III.	IV.	V.	VI.	VII.	VIII.	IX.	X.	XI.	XII.
J. Polanský, Česká spořitelna	+	+	+	+	+	+						
David Marek, Deloitte Czech Republic	+	+	+	+	+	+						
Viktor Zeisel, Marek Dřimal, Komerční banka	+	+	+	+	+	+						
Patrik Rožumberský, Unicredit Global Research	+	+	+	+	+	+						
Helena Horská, Eliška Jelínková Raiffeisenbank	+	+	+	+	+	+						
Petr Dufek, ČSOB	+	+	+		+	+						
Petr Sklenář, J&T Banka	+	+	+	+	+	+						
Radomír Jáč, Generali Investments CEE	+	+	+	+	+	+						
Jaromír Šindel, Citi	+	+	+	+	+	+						
Martin Janíčko, Kamil Kovář, Moody's Analytics	+	+	+	+	+	+						
Jan Kudláček, Tomáš Lébl, AXA	+	+	+	+	+	+						
Jakub Seidler, ING	+	+	+	+	+	+						
Lukáš Kovanda, Czech Fund	+	+	+	+	+	+						
Michal Šoltés, RoklenFin	+	+				+	+					
FOREIGN ANALYSTS												
Timon Dreyer, Kevin Daly, Goldman Sachs	+	+	+	+	+	+						
Shivaan Tandon, The Economist Intelligence Unit	+	+	+	+	+	+						
Jose A. Cerveira, JP Morgan	+	+		+		+						

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

Prague, 21 June 2019

FORECAST FOR Y/Y CPI GROWTH (%)

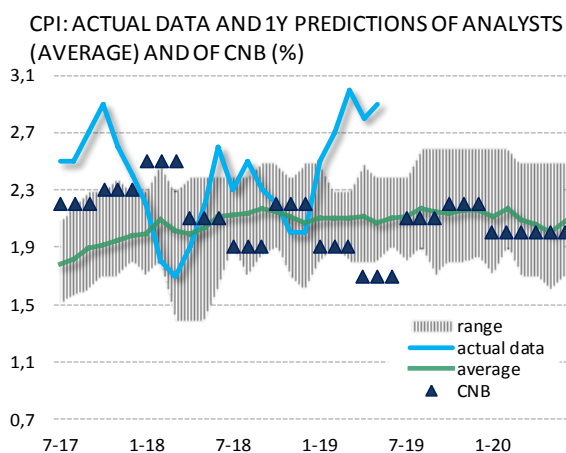
June 2019	CPI	
	1Y	3Y
minimum	1,7	1,5
average	2,1	2,0
maximum	2,5	2,3

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

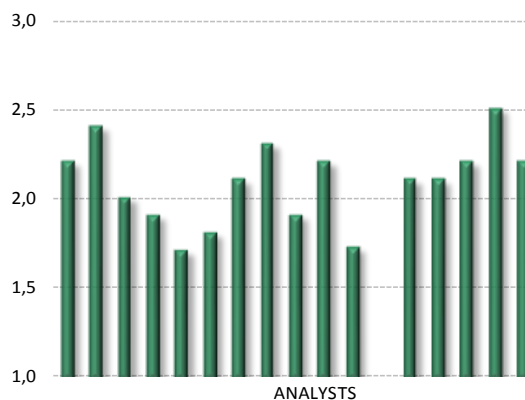
Date of Prediction	ANALYSTS		CNB (%)
	1Y	3Y	1Y
6.18	2,1	2,0	2Q: 1,7
9.18	2,1	2,0	3Q: 2,1
11.18	2,2	2,0	
12.18	2,2	2,0	4Q: 2,2
2.19	2,2	2,0	1Q: 2,0
4.19	2,1	2,0	
5.19	2,0	1,9	2Q: 2,0
6.19	2,1	2,0	

According to the CZSO, the consumer price index accelerated again in May, increasing by 2.9% year on year, 0.1 pp more than in April. This was due mainly to a rise in food prices (potatoes in particular) and housing-related costs. The analysts' average forecast in this survey also went up by 0.1 pp in both horizons monitored. The one-year forecast thus shifted to 2.1% and the three-year forecast returned to the CNB's 2% inflation target. The range of maximum values and three-year individual estimates narrowed due to a rise in the minimum values.

Although higher inflation in May came as a bit of a surprise to the analysts and they might have adjusted their estimates accordingly, they still expect the price level to decline slowly and gradually to the 2% inflation target. The slowdown in inflation is expected to be attributable to higher CNB key interest rates and base effects for fuel prices and core inflation. However, this will be moderated by growth in administered prices and, according to some analysts, higher food prices reflecting last year's weaker harvest. By contrast, there is a view expecting a downward correction of food prices.



CPI AT 1Y: PREDICTIONS OF INDIVIDUAL ANALYSTS



FORECAST FOR GDP GROWTH (%)

June 2019	end of year	
	current	current+1Y
minimum	2,0	2,0
average	2,4	2,4
maximum	2,8	2,9

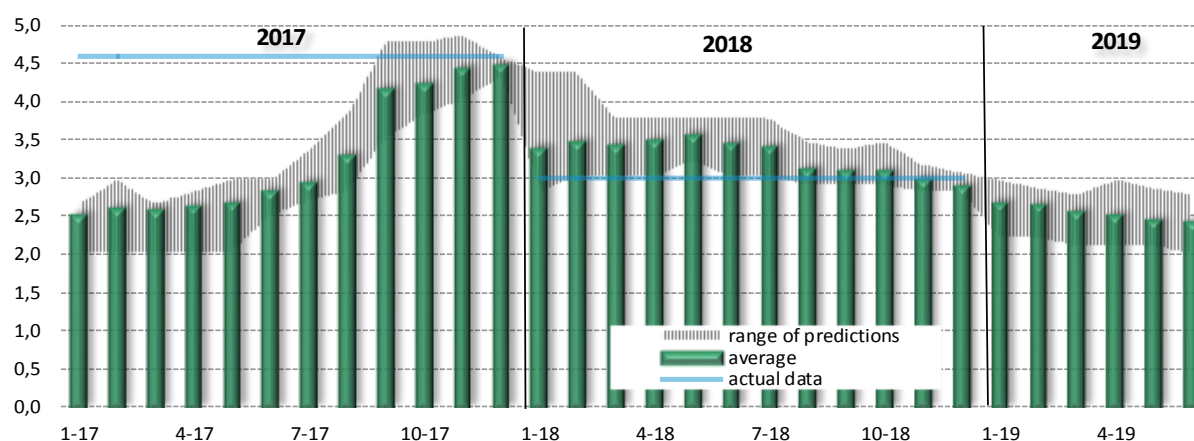
FORECAST FOR GDP GROWTH (%)

Date of Prediction	end of year	
	current	current+1Y
6.18	3,4	3,0
9.18	3,1	2,9
11.18	3,0	2,9
12.18	2,9	2,8
2.19	2,6	2,6
4.19	2,5	2,5
5.19	2,4	2,4
6.19	2,4	2,4

The CZSO increased annual GDP growth for 2019 Q1 by 0.1 pp. According to the revised estimate, the Czech economy grew by 2.6% in the first three months of 2019. The biggest contributors to gross value added were manufacturing and, from the demand perspective, mainly household consumption. However, this information did not affect the analysts' forecasts, which remain at 2.4% on average for this year and the next. The range of the forecasts for 2019 remains the same due to an equal decrease in both extreme values, while that of the forecasts for 2020 narrowed due mainly to an increase in the minimum value.

According to the analysts, the economy is expected to maintain solid performance. Its growth will continue to be driven mainly by household consumption, which is based on the tight labour market and related high wage growth. Nevertheless, even households are taming the strong buying appetite observed in previous years and are creating precautionary savings. Conversely, the foreign trade balance is under pressure from weaker external demand (particularly, a slowdown in the automotive industry may have a negative impact on the Czech Republic) and strengthening imports stemming from robust domestic demand. However, some respondents believe that the situation in the euro area might improve in the second half of this year. This notwithstanding, the impacts of the planned exit of the United Kingdom from the EU and of the still unclear protectionist measures in foreign trade remain a major unknown.

GDP GROWTH IN CURRENT YEAR: AVERAGE AND RANGE OF PREDICTIONS



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
6.18	0,81	1,40	1,22	1,83	1,86	2,19	2,05	2,46
9.18	1,45	2,16	1,89	2,53	2,34	2,68	2,40	2,86
11.18	1,75	2,29	2,20	2,66	2,59	2,87	2,63	2,94
12.18	1,75	2,30	2,20	2,65	2,43	2,79	2,42	2,78
2.19	1,81	2,22	2,25	2,54	1,99	2,38	1,96	2,41
4.19	1,87	2,17	2,27	2,48	2,03	2,28	1,97	2,29
5.19	2,00	2,14	2,32	2,45	2,03	2,22	1,98	2,32
6.19	2,00	2,08	2,35	2,35	1,90	2,12	1,81	2,16

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

June 2019	2W repo rate		12M PRIBOR		5Y IRS		10Y IRS	
	1M	1Y	1M	1Y	1M	1Y	1M	1Y
minimum	2,00	1,50	2,25	1,90	1,60	1,70	1,50	1,50
average	2,00	2,08	2,35	2,35	1,90	2,12	1,81	2,16
maximum	2,00	2,25	2,78	2,65	2,30	2,85	2,10	2,73

ACTUAL INDICATOR VALUES AS OF FORECAST DEADLINE (%)

	2W repo rate	12M PRIBOR	5Y IRS	10Y IRS
14.6.	2,00	2,29	1,68	1,63

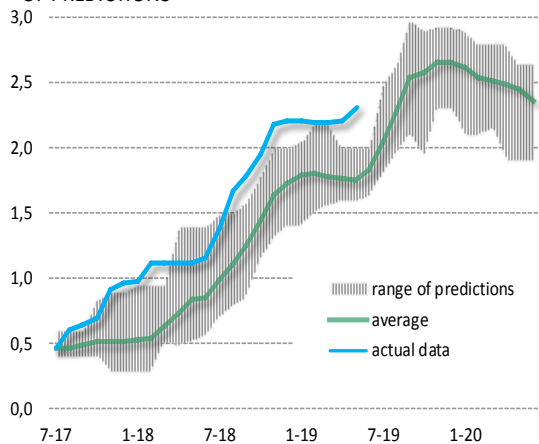
As last month, none of the respondents expected the 2W repo rate to change at the CNB Board meeting in June. It is thus expected to remain at the current level (2%) at least until the start of August. But the outlook for the period ahead has been corrected. While most analysts in the previous survey expected the CNB to increase the 2W repo rate one more time by 25 bps over the next 12 months, the view that the key interest rate will remain at the current level until June 2020 prevails slightly at the moment. This is naturally due to the concern that further monetary policy tightening might put an excessive burden on domestic economic growth. Moreover, there is again a risk that Brexit-related uncertainty will intensify in the second half of the year, which will not create ideal conditions for increasing key interest rates.

ANALYSTS FORECAST - 2W REPO RATE LEVEL IN 1Y (%)

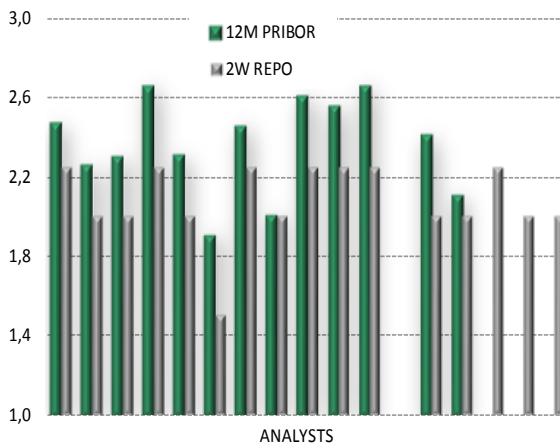
2W repo rate level in 1Y (%)	1,50	1,75	2,00	2,25	2,50
number of analysts - current survey	1	0	8	7	0
-previous survey	1	0	4	11	0

The forecast for interbank rates (12M PRIBOR) and IRS declined except for the one-month forecast for the 12M PRIBOR. It thus reflects a decrease in corresponding market rates and the perspective of expected stability of key interest rates (unlike the expected tightening suggested in the May survey).

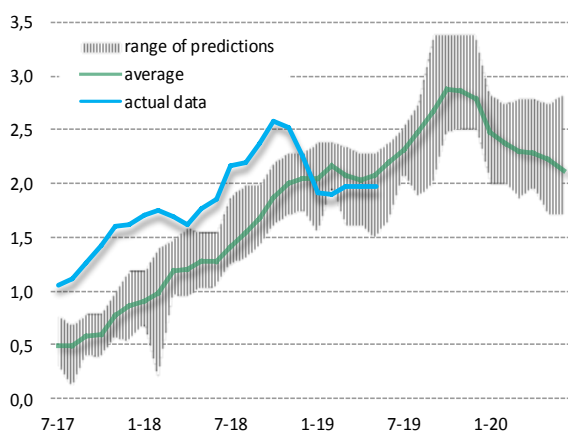
12M PRIBOR AT 1Y : ACTUAL DATA, AVERAGE AND RANGE OF PREDICTIONS



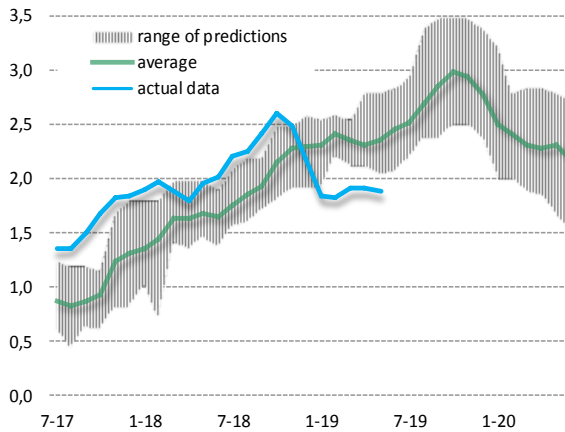
2W REPO AND 12M PRIBOR: 1Y PREDICTIONS OF INDIVIDUAL ANALYSTS



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
6.18	25,51	24,64
9.18	25,53	24,82
11.18	25,86	25,07
12.18	25,78	25,09
2.19	25,63	25,07
4.19	25,61	25,34
5.19	25,68	25,28
6.19	25,65	25,49

EXCHANGE RATE FORECAST

June 2019	EUR/CZK	
	1M	1Y
minimum	25,55	24,63
average	25,65	25,49
maximum	25,80	26,50

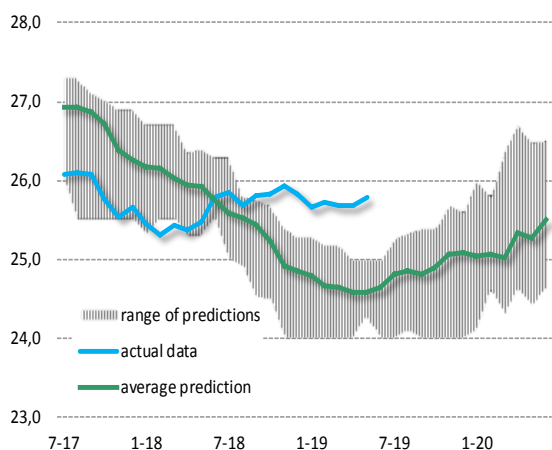
ACTUAL EUR/CZK AS OF FORECAST DEADLINE

14.6.	25,54
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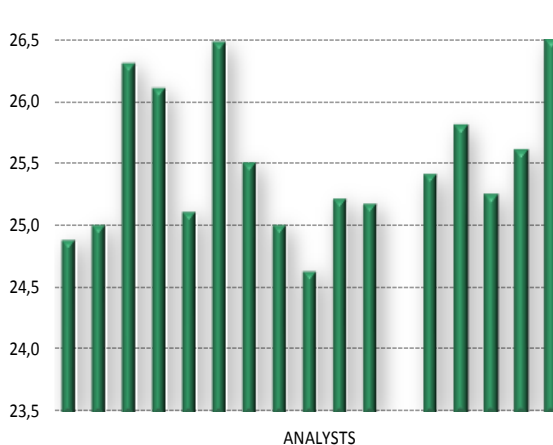
The one-month forecast for the koruna exchange rate against the euro was almost unchanged from the previous survey, remaining at CZK 25.65 CZK to the euro. Conversely, the koruna exchange rate is now expected to remain virtually flat at the one-year horizon (compared to the situation as of the deadline for submitting forecasts), with CZK 25.49 to the euro being the weakest one-year forecast since August 2017.

The analysts still perceive relatively great sensitivity of the koruna exchange rate to sentiment on foreign markets. In this context, they believe that as long as a high degree of uncertainty prevails in the global economy, the koruna will remain weak compared to its long-term equilibrium. The main causes of the undervalued koruna currently include uncertainties stemming from intensifying protectionist measures in foreign trade and the threat of “hard” Brexit, which, given the latest political developments in the United Kingdom, seems to be more likely. Moreover, as the prospect of further monetary policy tightening becomes less likely, the rate of the expected koruna appreciation decreases. However, if these risks do not materialise, the analysts admit that the koruna exchange rate might return to the long-term scenario of gradual appreciation.

EUR/CZK: ACTUAL DATA, 1Y PREDICTIONS AND THEIR RANGE



EUR/CZK AT 1Y: PREDICTIONS OF INDIVIDUAL ANALYSTS



FORECAST FOR NOMINAL WAGE GROWTH (%)

June 2019	year end	
	current	current+1Y
minimum	5,8	4,0
average	6,7	5,1
maximum	7,8	7,6

FORECAST FOR NOMINAL WAGE GROWTH (%)

Date of Prediction	year end	
	current	current+1Y
6.18	7,8	5,6
9.18	8,2	6,3
11.18	8,4	6,5
12.18	8,3	6,7
2.19	6,8	5,3
4.19	6,4	4,9
5.19	6,3	4,8
6.19	6,7	5,1

The labour market continues to show signs of overheating; according to labour offices, the share of unemployed persons decreased to 2.6% in May and the number of unemployed persons is the lowest since 1997. According to the CZSO, the gross monthly nominal wage grew by 7.4% in 2019 Q1. Given the rise in consumer prices of 2.7%, this represents a real increase of 4.6%. These facts probably led the analysts to revise upwards the average forecast for nominal wages, by 0.4 pp to 6.7% and 0.3pp to 5.1% for 2019 and 2020 respectively. Despite the fast wage growth in the public sector and the acute labour shortages in some sectors, which are hard to reduce by hiring foreign workers due to tight restrictions and which create strong upward pressures on prices of labour, the wage growth rate is expected to slow gradually in line with a slowing rate of economic growth. Moreover, new graduates might at least temporarily ease the excess demand for labour in summer months.

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

