

Financial Market Inflation Expectations

1/2021



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Czech National Bank — Financial Market Inflation Expectations — 1/2021

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I. SUMMARY

Fourteen domestic and three foreign analysts sent in their contributions to the first survey of financial market inflation expectations in 2021. Compared to the last survey, the analysts' opinion on inflation remains unchanged, with inflation expected to slightly exceed the CNB's 2% inflation target at the one-year horizon and to be on target at the three-year horizon. Conversely, estimated economic growth in 2021 was slightly revised to a somewhat lower level on average than expected in the December survey. The economic recovery is expected to pick up further in 2022 which, in the analysts' view, implies a slightly higher level of the CNB's key interest rates in 2021 H2. The forecasts for PRIBOR and IRS rates and the expected growth of nominal wages also shifted slightly upwards. A slight correction of the expected koruna exchange rate towards stronger levels reflects not only foreign exchange market developments over the last month, but also (similar to some other indicators) hopes that the pandemic will soon subside and then economic growth will restart again.

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

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

Prague, 25 January 2021

II. INFLATION

FORECAST FOR Y/Y CPI GROWTH

(%)

January 2021	CPI	
	1Y	3Y
minimum	1.0	1.3
average	2.1	2.0
maximum	2.8	2.3

1Y AND 3Y FORECAST FOR CPI GROWTH

(%)

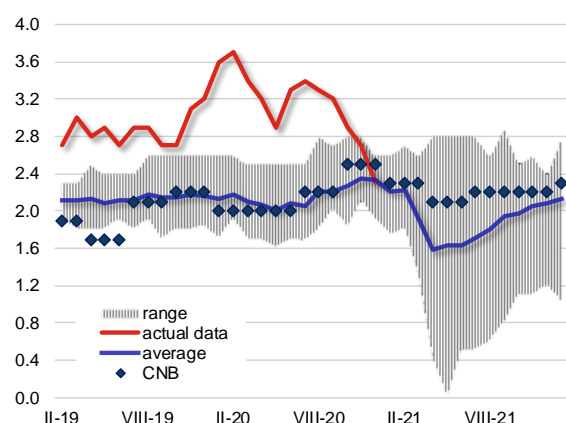
Date of Prediction	ANALYSTS		CNB (%)
	1Y	3Y	1Y
I.20	2.2	2.0	
II.20	2.2	2.0	1Q: 2.3
V.20	1.6	1.9	2Q: 2.1
VII.20	1.7	2.0	
VIII.20	1.8	2.0	3Q: 2.2
X.20	2.0	2.0	
XII.20	2.1	2.0	4Q: 2.2
I.21	2.1	2.0	

Inflation slowed again in the Czech Republic. The CZSO announced that the annual growth rate of the CPI increased by a mere 2.3% in December, i.e. 0.4 pp less than in November, its lowest increase since December 2018. This was mostly attributable to prices of food and non-alcoholic beverages. Although the rate was surprisingly low, it had virtually no impact on the average one-year and three-year forecasts by the analysts who participated in the January survey. The analysts thus still expect consumer price inflation to be 0.1 pp above the CNB's 2% inflation target at the start of next year and on target two years later. The range of individual one-year estimates widened due to an increase in the maximum value and a decline in the minimum value. By contrast, the spread narrowed somewhat for three-year forecasts due to a slightly larger decline in the minimum value.

The analysts believe that consumer price inflation will decline further at the start of this year, due mainly to weakened aggregate demand and the unwinding of higher prices in early 2020 (base effects). With many firms currently closed or operating at very limited capacity due to the ongoing pandemic, it is highly unlikely that price lists will be updated as is traditionally the case at the start of the year. The annual inflation rate is thus expected to converge to the 2% target from above and, according to some estimates, may even drop below this level. Nonetheless, an economic recovery is still expected in the second half of the year, which will intensify inflation pressures and thus shift consumer price inflation upwards again. However, their faster growth will be prevented by the CNB's rising interest rates.

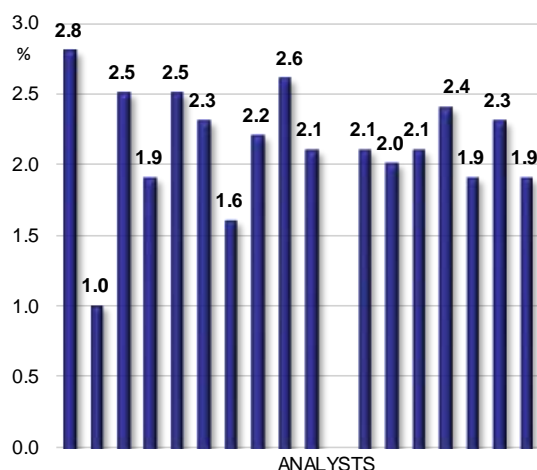
CONSUMER PRICE INDEX

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



CONSUMER PRICE INDEX AT 1Y

PREDICTIONS OF INDIVIDUAL ANALYSTS (%)



III. GROSS DOMESTIC PRODUCT

FORECAST FOR GDP GROWTH

(%)

January 2021	end of year	
	current	current + 1Y
minimum	2.0	1.6
average	3.4	4.6
maximum	6.7	6.8

FORECAST FOR GDP GROWTH

(%)

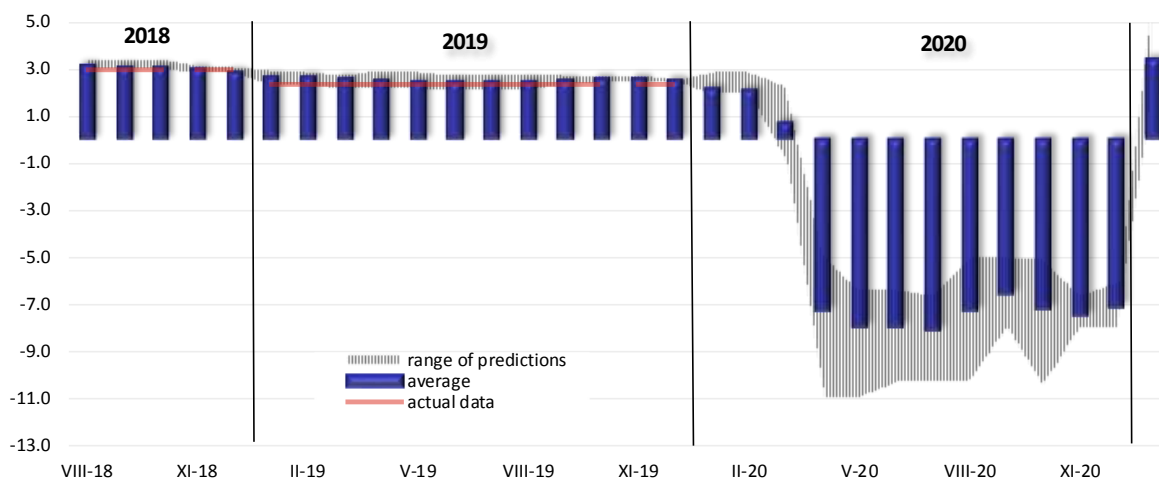
Date of Prediction	end of year	
	current	current+1Y
I.20	2.2	2.3
II.20	2.1	2.3
V.20	-7.9	5.8
VII.20	-8.0	5.6
VIII.20	-7.2	5.0
X.20	-7.1	4.3
XII.20	-7.0	3.5
I.21	3.4	4.6

The revision of GDP growth data brought no change in 2020 Q3, and the Czech economy thus recorded an annual decline of 5.0% and increased quarter-on-quarter by 6.9%. However, in our survey the analysts' average economic growth forecast for 2021 worsened slightly, down by 0.1 pp to 3.4%. The economic recovery is expected to accelerate to 4.6% in 2022. The spread of the individual estimates for 2021 widened somewhat due to a moderate increase in the maximum value.

The analysts expect the economy to recover this year after last year's very adverse economic developments from a historical perspective. However, at least in Q1, the economy is not expected to recover fully, due to the restrictive socially-distancing measures. The situation in the quarters ahead will essentially depend on the course of vaccination, which the analysts expect will not likely be made available to the general public until 2021 Q2. If the vaccination process is fast and runs smoothly, growth this year might be higher than expected by the analysts in the baseline scenario. The positive fiscal impulse arising from the abolishment of the super-gross wage and a reduction in income tax will also enhance growth considerably, which will have a positive impact on household consumption. Investment activity might be boosted in 2021 by the recovery plan and the start of a new programme period for budgetary funds. The global economy is also expected to restart gradually, which would have a positive effect on the Czech economy through a recovery in external demand.

GDP GROWTH AT END OF CURRENT YEAR

AVERAGE AND RANGE OF PREDICTIONS



IV. INTEREST RATES – 2W REPO, PRIBOR, IRS

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

(%)

January 2021	2W repo rate		12M PRIBOR		5Y IRS		10Y IRS	
	1M	1Y	1M	1Y	1M	1Y	1M	1Y
minimum	0.25	0.25	0.48	0.50	0.85	0.95	0.90	1.25
average	0.25	0.38	0.50	0.74	1.02	1.28	1.20	1.47
maximum	0.25	0.75	0.51	1.11	1.15	1.50	1.32	1.70

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
I.20	2.01	2.07	2.28	2.27	1.99	2.02	1.75	1.96
II.20	2.25	2.15	2.47	2.32	2.00	2.06	1.72	1.98
V.20	0.19	0.16	0.41	0.42	0.44	0.60	0.56	0.74
VII.20	0.24	0.18	0.43	0.45	0.56	0.71	0.76	0.94
VIII.20	0.25	0.27	0.43	0.50	0.69	0.85	0.88	1.07
X.20	0.24	0.24	0.42	0.52	0.60	0.90	0.85	1.15
XII.20	0.25	0.35	0.46	0.65	0.92	1.20	1.13	1.40
I.21	0.25	0.38	0.50	0.74	1.02	1.28	1.20	1.47

ACTUAL INDICATOR VALUES AS OF FORECAST DEADLINE

(%)

	2W repo rate	12M PRIBOR	5Y IRS	10Y IRS
15.1.	0.25	0.49	0.99	1.23

All the respondents again expect the Bank Board to leave key interest rates unchanged at its next meeting in February and the 2W repo rate to remain at 0.25%. The prevailing view is that the key interest rates will also remain unchanged at the current level at the one-year horizon. The Czech economy is in a double-dip recession, the vaccination rollout will be relatively slow and therefore the majority of respondents believe that it will not be necessary to tighten the CNB's monetary policy in 2021. Nevertheless, the remaining almost half of the respondents expect that the key rates will be increased this year. Seven respondents expect them to rise by 25 bps and one by as much as 50 bps. They believe that the economic recovery will start in 2021 H2 which, along with tax changes, should lead to growth in demand and, consequently, inflation pressures. The CNB will then have to respond by tightening its monetary conditions.

ANALYSTS' FORECAST – 2W REPO RATE LEVEL IN 1Y

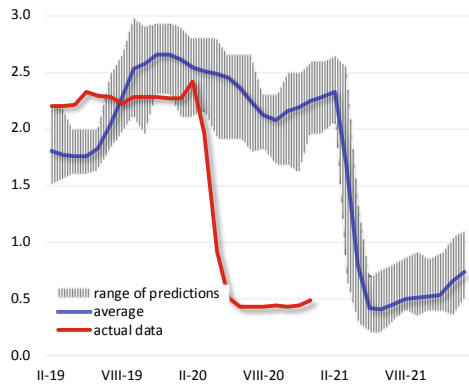
(%)

2W repo rate level in 1Y (%)	0.05	0.25	0.50	0.75	1	1.25
number of analysts - current survey	0	9	7	1	0	0
-previous survey	0	11	5	1	0	0

Given the strengthening expectations of growth in key interest rates at the one-year horizon, the outlooks for the PRIBOR interbank reference rates were revised upwards, up by 4 bps for the one-month maturity and 8 bps for the 12-month maturity. Similarly, forecasts for swap rates – probably taking into account improved sentiment on the global markets – were also revised upwards, up by 7–10 bps.

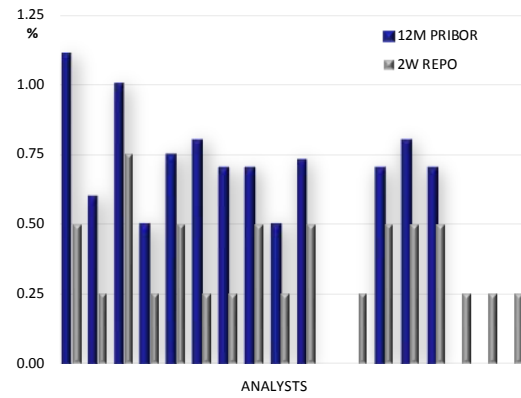
12M PRIBOR AT 1Y

ACTUAL DATA, AVERAGE AND RANGE OF PREDICTIONS



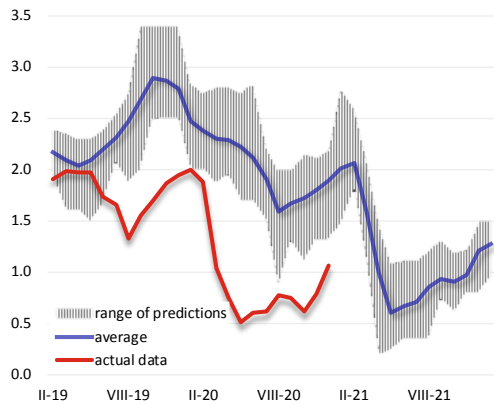
2W REPO AND 12M PRIBOR AT 1Y

PREDICTIONS OF INDIVIDUAL ANALYSTS



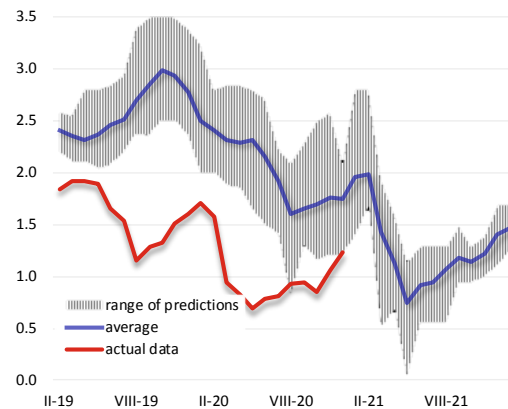
5Y IRS AT 1Y

AVERAGE AND RANGE OF PREDICTIONS



10Y IRS AT 1Y

AVERAGE AND RANGE OF PREDICTIONS



V. EXCHANGE RATE

1M AND 1Y EXCHANGE RATE FORECAST

Date of Prediction	EUR/CZK	
	1M	1Y
I.20	25.26	25.14
II.20	25.05	24.93
V.20	27.28	26.20
VII.20	26.64	25.93
VIII.20	26.17	25.76
X.20	27.11	25.88
XII.20	26.33	25.63
I.21	26.13	25.53

EXCHANGE RATE FORECAST

January 2021	EUR/CZK	
	1M	1Y
minimum	26.00	24.90
average	26.13	25.53
maximum	26.35	26.00

ACTUAL EUR/CZK AS OF FORECAST DEADLINE

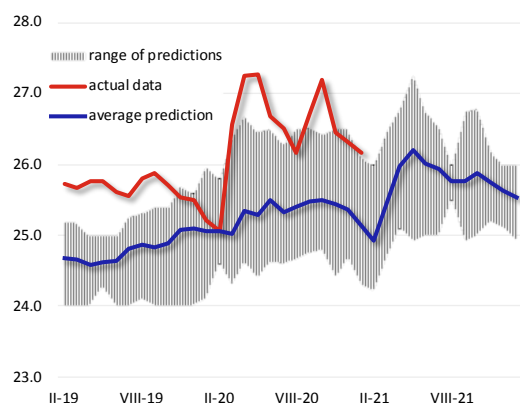
15.1.	26.16
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The koruna's exchange rate appreciated against the euro from CZK 26.36 to CZK 26.16 compared to the December survey. The analysts believe that this shift is due on the one hand to improved global sentiment, fostered by ongoing vaccination and the results of the US election. On the other hand, in their view it might be due to gradually strengthening expectations of growth in the CNB's interest rates. However, adverse domestic developments in the pandemic are preventing the koruna from appreciating further.

The analysts predict a slightly stronger koruna (CZK 26.13 to the euro) at the very short, i.e. one-month horizon. A gradual appreciation trend is expected to follow during the course of 2021, due to several factors. One factor is an improvement in the pandemic situation (both in the Czech Republic and abroad). This is not only expected to improve investor confidence in regional currencies, but also to pave the way to a stable economic recovery. The related inflation pressures, intensified by tax changes, will further lead at least to expectations of growth in key interest rates, which also fosters a stronger koruna. Last but not least, there is still the traditional convergence scenario, according to which the Czech Republic's gradual convergence to more advanced Western European countries will result in appreciation of the domestic currency. The analysts expect the koruna's exchange rate to be close to CZK 25.53 to the euro in January 2022, up by 10 hellers compared to the previous survey. In addition to the uncertain pandemic situation, the worsening of public finances is also considered a risk. A mere weakening of the already very fragile investor confidence in public debt quality and sustainability might cause the koruna's exchange rate to depreciate and deviate from the baseline scenario.

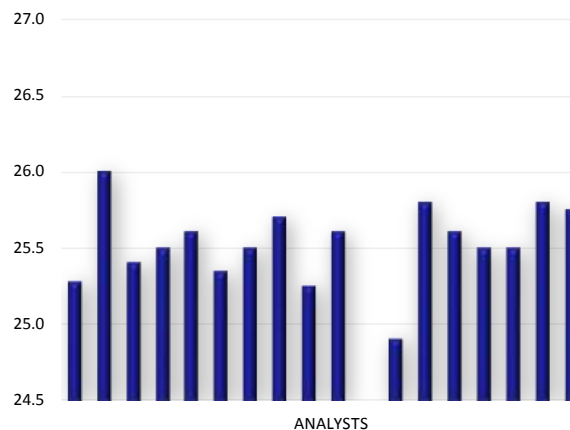
EUR/CZK

ACTUAL DATA, 1Y PREDICTIONS AND THEIR RANGE



EUR/CZK AT 1Y

PREDICTIONS OF INDIVIDUAL ANALYSTS



VI. NOMINAL WAGES

FORECAST FOR NOMINAL WAGE GROWTH

(%)

January 2021	year end	
	current	current+1Y
minimum	2.20	2.50
average	3.16	4.36
maximum	6.60	6.80

FORECAST FOR NOMINAL WAGE GROWTH

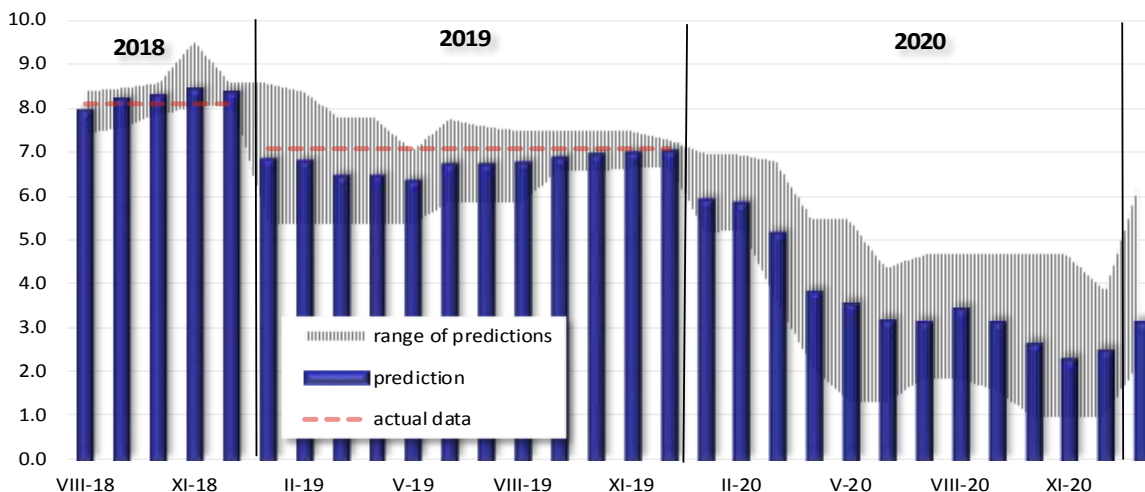
(%)

Date of Prediction	year end	
	current	current+1Y
I.20	5.9	4.9
II.20	5.8	4.9
V.20	3.5	2.8
VII.20	3.1	2.9
VIII.20	3.5	3.2
X.20	2.7	2.9
XII.20	2.5	2.9
I.21	3.2	4.4

Despite the significantly adverse economic conditions, unemployment on the labour market has been increasing only very slowly, due mainly to extensive government support programmes. According to the latest available data, in November 2020 the proportion of unemployed people aged 15–64 as a percentage of the economically active population remained unchanged from October at 2.9%. This, along with the expected economic recovery, may have prompted the analysts to increase the forecast for nominal wage growth. The analysts currently expect wages to rise on average by 3.2% in 2021, up by 0.3 pp compared to the December survey. The outlook for 2022 is even more optimistic, with wage growth rate expected to pick up to 4.4%.

NOMINAL WAGE GROWTH

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



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