

Financial Market Inflation Expectations

—— 2/2021

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I. SUMMARY

All eighteen respondents addressed, i.e. fifteen domestic and three foreign analysts, took part in the CNB's February survey. The data received reveal that while the analysts' view on GDP growth (both this year and the next) remains unchanged, the one-year inflation forecast increased moderately. The three-year inflation forecast remains anchored at the CNB's 2% inflation target. The outlook for key interest rates has changed significantly, with most of the respondents now expecting at least one increase in the 2W repo rate by 25 basis points over the next 12 months. The appreciation of the koruna on the foreign exchange market was naturally reflected in the exchange rate forecasts at both the one-month and one-year horizons. The respondents expect higher growth in nominal wages this year, while the forecast for next year has been revised downwards.

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, 22 February 2021

II. INFLATION

FORECAST FOR Y/Y CPI GROWTH

(%)

February 2021	CPI	
	1Y	3Y
minimum	1.7	1.4
average	2.2	2.0
maximum	2.7	2.3

1Y AND 3Y FORECAST FOR CPI GROWTH

(%)

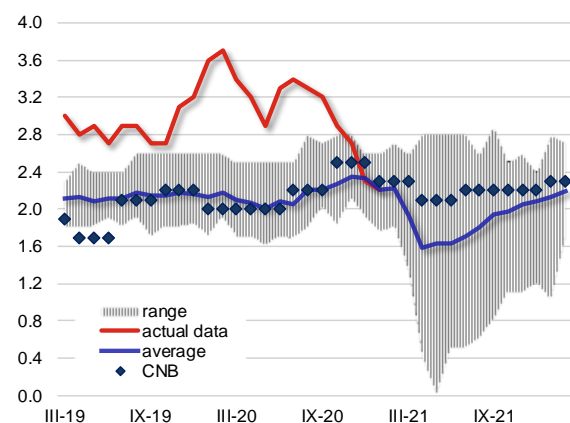
Date of Prediction	ANALYSTS		CNB (%)
	1Y	3Y	1Y
II.20	2.2	2.0	1Q: 2.3
V.20	1.6	1.9	2Q: 2.1
VII.20	1.7	2.0	
VIII.20	1.8	2.0	3Q: 2.2
X.20	2.0	2.0	
XII.20	2.1	2.0	4Q: 2.2
I.21	2.1	2.0	
II.21	2.2	2.0	1Q: 2.3

Inflation slowed further in the Czech Republic. According to the CZSO, annual CPI inflation reached 2.2% in January, which is 0.1 pp less than in December 2020. In month-on-month terms, the consumer price level increased by 1.3%. This was due in large part to prices in the food and non-alcoholic beverages category, where there was a noticeable increase in prices of vegetables, especially potatoes. Prices of alcoholic beverages and tobacco also played a significant role. Most of the analysts had been expecting a sharper slowdown in price growth. Therefore, such a high rate of inflation came as a considerable surprise to them and to the market. In this context, the average one-year inflation forecast increased by 0.1 pp to 2.2%. However, the three-year forecast remains stable at the CNB's 2% inflation target. The range of the one-year estimates narrowed in both monitored years, owing mainly to an increase in the minimum value, while a bigger change was recorded for the one-year forecasts.

Inflation is also expected to slow in the months ahead. However, given the January data, the question is whether, and to what extent, it will fall below 2%. The latest statistics tend to reduce the probability of a drop in inflation below the target. According to some of the analysts' calculations, core inflation went up, but it might slow in the months ahead on account of persisting restrictive measures and the easing of labour market tightness. The stronger koruna on the foreign exchange market could also act in the same direction. However, if the pandemic is staved off soon and we see a robust economic recovery, there may not be any major slowdown in core and headline inflation at all. Consumer prices will also be pushed up by higher oil prices and higher excise duties.

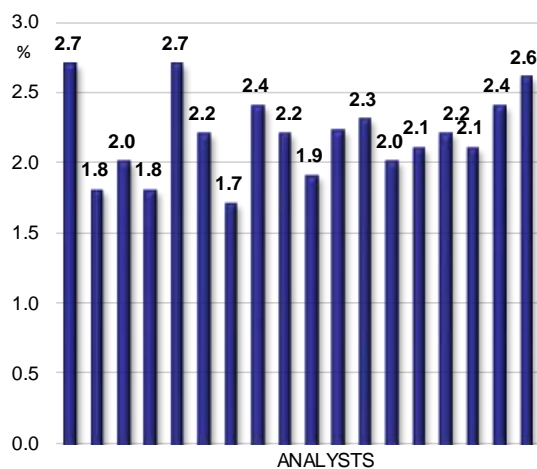
CONSUMER PRICE INDEX

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

(%)

February 2021	end of year	
	current	current + 1Y
minimum	2.0	3.5
average	3.4	4.6
maximum	6.7	6.3

FORECAST FOR GDP GROWTH

(%)

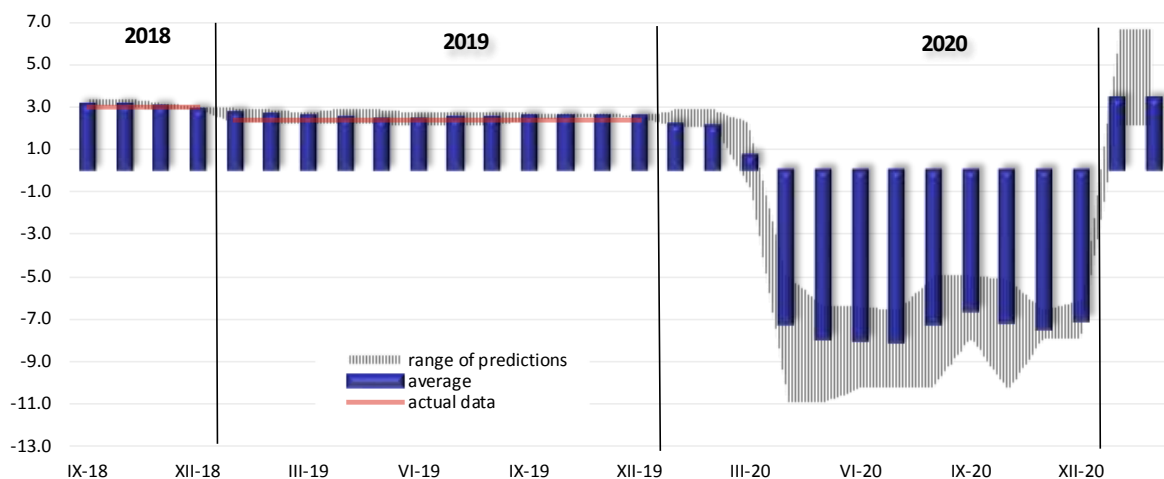
Date of Prediction	end of year	
	current	current+1Y
II.20	2.1	2.3
V.20	-7.9	5.8
VII.20	-8.0	5.6
VIII.20	-7.2	5.0
X.20	-7.1	4.3
XII.20	-7.0	3.5
I.21	3.4	4.6
II.21	3.4	4.6

According to the CZSO's preliminary figures, the Czech economy grew by 0.3% quarter on quarter in 2020 Q4. The year-on-year decline remains at the previous level (-5.0%). This came as a very positive surprise for the analysts (and the market), who had expected a quarter-on-quarter decline due to the strict restrictive measures in place. Czech GDP fell by 5.6% in 2020 as a whole, while in our December survey the analysts had been expecting a decline of 7%. Although the latest figures for GDP were much better than expected, the average estimate for economic growth in the Czech Republic for 2021 and 2022 was unchanged from the January survey. Czech GDP is thus expected to rise year on year by 3.4% in 2021 and pick up to 4.6% in 2022. The range of the individual forecasts for 2021 stayed the same, while that for next year narrowed considerably, due mainly to a rise in the minimum value, but also to a fall in the maximum value.

According to the analysts, the outlook for 2021 Q1 is not very optimistic, as the economy remains significantly paralysed by government measures. Although their impact is not as drastic as in spring 2020, a full reopening of the economy is still nowhere in sight. Domestic demand in particular will remain very weak. External demand might fare appreciably better, as some believe the economic situation in Germany, for example, to be relatively favourable given the current conditions, and Germany is one of the Czech Republic's major trading partners. Growth in future quarters will depend critically on vaccination progress. The greater the proportion of the population protected by the vaccine, the sooner the economy can be reopened. However, it is argued that at the current rate of vaccination we are more likely to see a return to normal in the second half of this year. After the lifting of restrictive measures, businesses are expected to open and restart operations. An improvement in household and business sentiment is also expected, which will subsequently be reflected in final consumption and investment. External demand is also expected to recover, with the recent reduction in income tax also having a positive effect. This should also be gradually joined by the effects of the drawdown of funds from the EU, both from traditional EU funds and from the recently approved European recovery fund.

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

(%)

February 2021	2W repo rate		12M PRIBOR		5Y IRS		10Y IRS	
	1M	1Y	1M	1Y	1M	1Y	1M	1Y
minimum	0.25	0.25	0.40	0.65	0.91	1.21	1.15	1.28
average	0.25	0.56	0.53	0.89	1.26	1.53	1.44	1.68
maximum	0.25	1.00	0.60	1.23	1.60	1.80	1.80	2.00

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
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
II.21	0.25	0.56	0.53	0.89	1.26	1.53	1.44	1.68

ACTUAL INDICATOR VALUES AS OF FORECAST DEADLINE

(%)

	2W repo rate	12M PRIBOR	5Y IRS	10Y IRS
15.2.	0.25	0.55	1.38	1.54

All the respondents are still expecting key interest rates to remain unchanged at the March Bank Board meeting and the 2W repo rate to stay at 0.25%. By contrast, there has been a significant shift in opinion at the one-year horizon. While in January a small majority of respondents still believed that key interest rates would remain stable over the next 12 months, the vast majority, i.e. 16 of the 18 respondents, is now expecting them to increase. Four of the analysts are expecting the 2W repo rate to increase by 50 bps to 0.75%, and one of them is even projecting an increase of 75 bps to 1.00%. Only two respondents are now expecting the CNB's key rates to be left unchanged at the one-year horizon. According to the analysts, the better-than-expected economic growth in 2020 Q4 and the surprisingly high January inflation rate clearly increases the probability of a faster tightening of the CNB's monetary policy. Nonetheless, the pandemic-related risks remain very high and the CNB will probably stay cautious with regard to increasing key interest rates. Moreover, part of the tightening of the monetary conditions will be delivered by their exchange rate component through a stronger koruna. For this reason, the first increase in key interest rates is not expected until 2021 Q4 or the start of 2022. However, if the vaccination drive gains momentum, a large part of the population are soon vaccinated, and it becomes clear in the summer that the pandemic-related risks are considerably lower and inflation pressures are increasing as the economy recovers, the CNB Bank Board could go ahead with its first rate increase in August.

PRIBOR interbank reference rates have shifted upwards from the previous survey in line with the projected increase in key interest rates, as has the analysts' average forecast. The estimated 12M PRIBOR is 3 bps higher at the one-month horizon and 15 bps higher at the one-year horizon. The rise in market swap rates has been more pronounced and their forecasts have thus shifted upwards more markedly (by 21–25 bps).

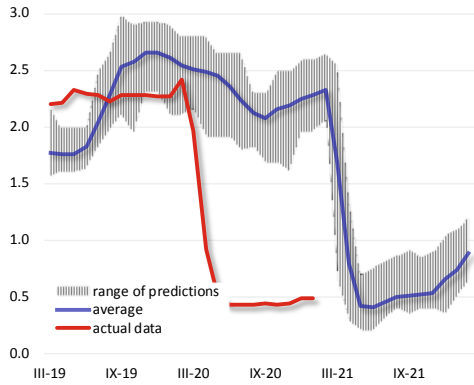
ANALYSTS' FORECAST – 2W REPO RATE LEVEL IN 1Y

(%)

2W repo rate level in 1Y (%)	0.05	0.25	0.50	0.75	1	1.25
number of analysts - current survey	0	2	11	4	1	0
-previous survey	0	9	7	1	0	0

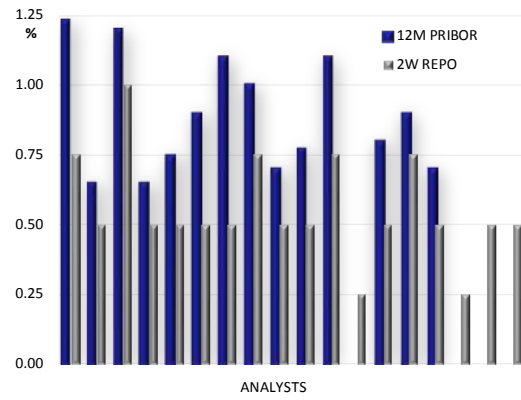
12M PRIBOR AT 1Y

ACTUAL DATA, AVERAGE AND RANGE OF PREDICTIONS



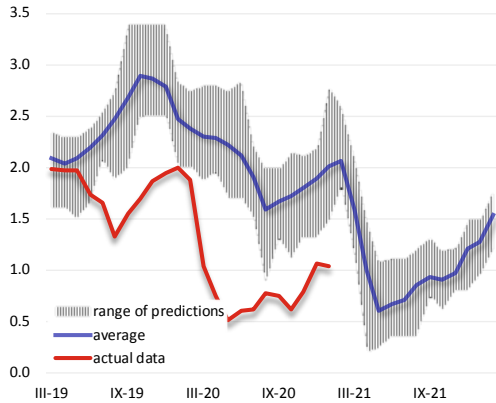
2W REPO AND 12M PRIBOR AT 1Y

PREDICTIONS OF INDIVIDUAL ANALYSTS



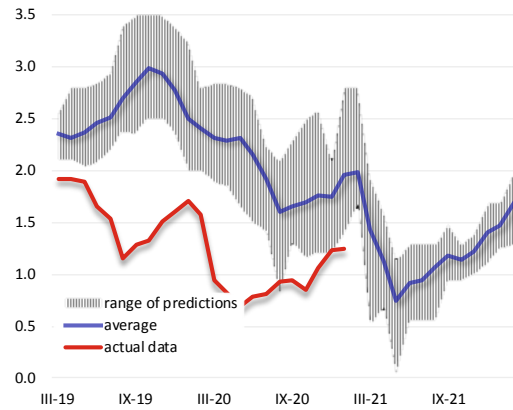
5Y IRS AT 1Y

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
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
II.21	25.78	25.23

EXCHANGE RATE FORECAST

February 2021	EUR/CZK	
	1M	1Y
minimum	25.50	24.80
average	25.78	25.23
maximum	25.90	25.50

ACTUAL EUR/CZK AS OF FORECAST DEADLINE

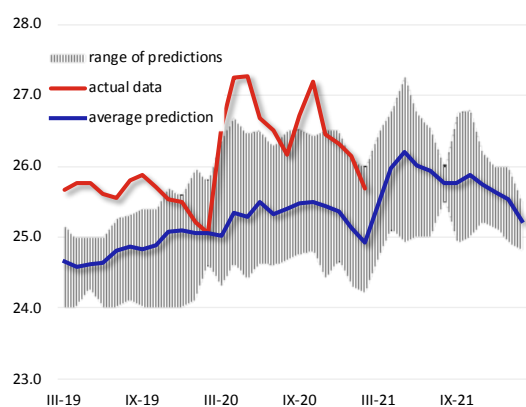
15.2.	25.68
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The koruna is continuing to strengthen. Since mid-January, it has appreciated from CZK 26.16 to CZK 25.68 against the euro. This was essentially driven by fundamentals, i.e. GDP at the end of last year, higher-than-expected inflation at the start of 2021 and related expectations of an earlier start to the normalisation of CNB monetary policy. The change in the exchange rate on the foreign exchange market was accordingly reflected in the forecasts in our survey. However, the analysts expect the koruna to correct slightly by mid-March this year to about CZK 25.8 to the euro from its current level at the closing date of the survey (mid-February).

The one-year forecast for the koruna exchange rate has also shifted to a stronger level. An improvement in the pandemic situation and market sentiment, a faster-than-originally-expected tightening of the CNB's monetary policy, higher external demand for Czech products and services and renewed convergence of the Czech economy to Western European countries should cause the koruna to appreciate for the rest of 2021 and at the start of 2022. The analysts thus estimate that the koruna exchange rate will be close to CZK 25.23 to the euro in mid-February 2022. However, the future course of the coronavirus pandemic presents a major risk to this scenario. The analysts expect the pandemic might recede due to a combination of warmer weather and vaccination progress. Nonetheless, the overall situation is currently not favourable at all, and there is little cause for optimism yet.

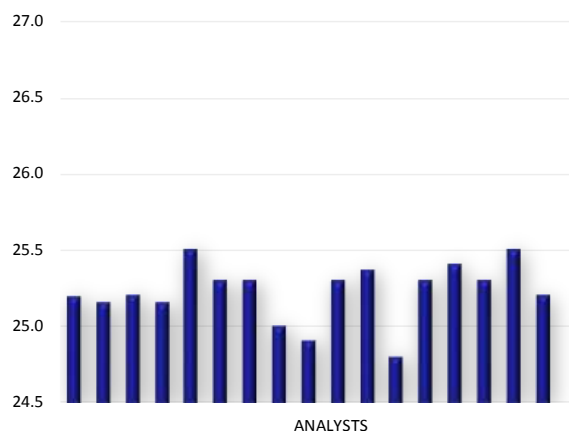
EUR/CZK

ACTUAL DATA, 1Y PREDICTIONS AND THEIR RANGE



EUR/CZK AT 1Y

PREDICTIONS OF INDIVIDUAL ANALYSTS



VI. NOMINAL WAGES

FORECAST FOR NOMINAL WAGE GROWTH

(%)

February 2021	year end	
	current	current+1Y
minimum	2.20	2.50
average	3.27	4.24
maximum	6.60	5.50

FORECAST FOR NOMINAL WAGE GROWTH

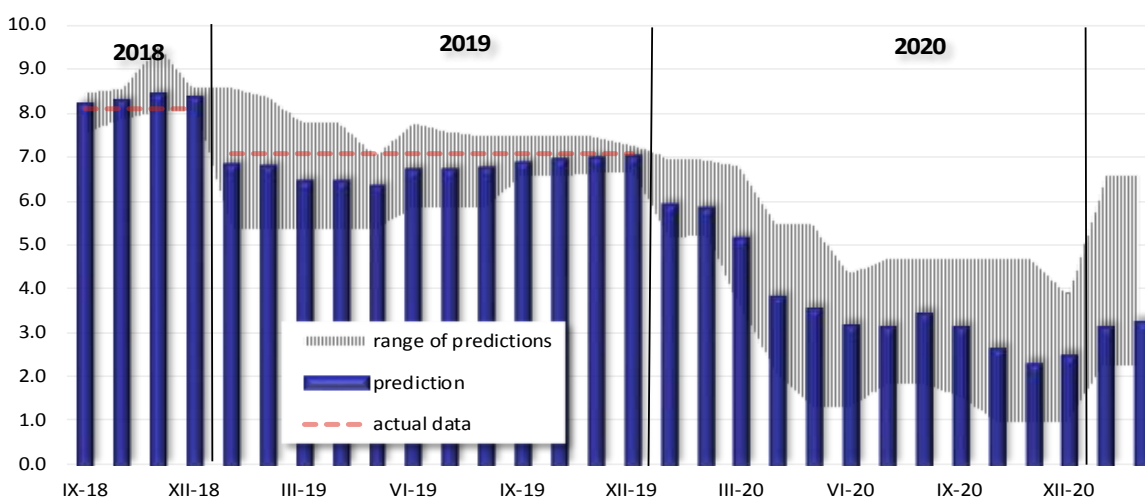
(%)

Date of Prediction	year end	
	current	current+1Y
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
II.21	3.3	4.2

It was only a matter of time before the effects of the strict restrictive measures aimed at mitigating the spread of the coronavirus also manifested themselves on the labour market. The CZSO announced that the general unemployment rate under the ILO definition¹ in the population aged 15–64 rose by 1.0 pp year on year to 3.1% in 2020 Q4. The seasonally adjusted general unemployment rate was 3.2% in December, up by 1.2 pp year on year. According to the Czech Labour Office, the share of unemployed persons registered with them rose in January by 0.3 pp to 4.3%, compared to 3.1% in January 2020. Although the statistics show steady deterioration, taking into account the conditions of the current global crisis they are not yet entirely bad (thanks in part to government support programmes). Indeed, according to Eurostat's latest available data, the Czech Republic has the lowest unemployment rate in the EU. However, the labour market reacts to the current economic situation with a significant lag, so we can still expect to see a rise in unemployment. The unemployment rate is naturally a key factor in nominal wage growth. The opinions on wage growth in 2021 are slightly more optimistic than in the last survey, with the forecast increasing by 0.1 pp to 3.3%. By contrast, the outlook for next year has been revised downwards. Wage growth is thus expected to pick up to 4.2% on average, 0.2 pp lower than expected a month ago.

NOMINAL WAGE GROWTH

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



¹ International Labour Organization.

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