

Financial Market Inflation Expectations

6/2021



Czech National Bank — Financial Market Inflation Expectations — 6/2021

CNB CZECH
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I. SUMMARY

Thirteen domestic and three foreign analysts sent in their contributions to the June survey of financial market inflation expectations. The data received reveal that the average inflation forecast was unchanged and remains close to the CNB's 2% target at both the one-year and three-year horizon. The economic growth estimate for 2021 is slightly more optimistic, while the outlook for 2022 was revised downwards. Favourable pandemic and economic developments, combined with the hawkish tone of CNB Board members' communication, resulted in an increase in the expected path of future key interest rates. At the same time, the forecast for the koruna's exchange rate was adjusted to the current market level. The wage growth rate recorded a marginal shift downwards this year, while the outlook for 2022 is slightly more optimistic.

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, 23 June 2021

II. INFLATION

FORECAST FOR Y/Y CPI GROWTH

(%)

June 2021	CPI	
	1Y	3Y
minimum	1.8	2.0
average	2.2	2.1
maximum	2.7	2.5

1Y AND 3Y FORECAST FOR CPI GROWTH

(%)

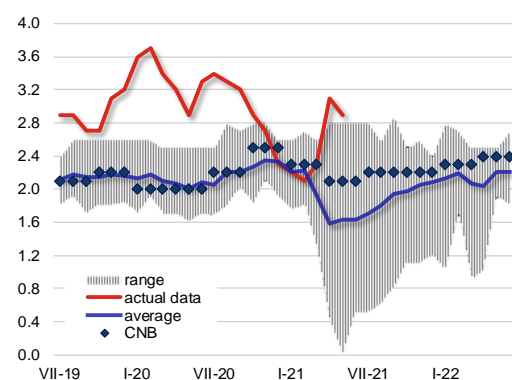
Date of Prediction	ANALYSTS		CNB (%)
	1Y	3Y	1Y
VI.20	1.6	1.9	2Q: 2.1
VII.20	1.7	2.0	
VIII.20	1.8	2.0	3Q: 2.2
X.20	2.0	2.0	
XII.20	2.1	2.0	4Q: 2.2
III.21	2.1	2.0	1Q: 2.3
V.21	2.2	2.1	
VI.21	2.2	2.1	2Q: 2.4

The CZSO announced that consumer prices had increased by 0.2% month on month in May, up by 2.9% year on year, i.e. 0.2 percentage point less than in April. The slower annual inflation was due mainly to a deepening decline in food prices, while car, fuel and services prices acted in the opposite direction. Despite slower annual CPI growth, the average forecast in our survey remains unchanged at both the one-year and three-year horizon. It remains at 2.2% at the one-year horizon, and the three-year forecast stays at 2.1% (the same as in May), thus remaining anchored just above the CNB's inflation target. The range of the individual one-year and three-year estimates widened due mainly to an increase in the maximum value.

Although the slowdown in inflation in May was surprising for many analysts, some of them are expecting inflation to grow further above the upper boundary of the CNB's tolerance band. This will be due to several factors, one being a strong labour market. It is also largely related to persisting high household demand. By contrast, disruptions to supply chains and higher prices of materials, services and energy will foster higher prices on the supply side. However, some analysts admit that a decrease in food prices may prevent inflation from rising further and, instead, will cause it to gradually slow towards the 2% target. The tightening of the CNB's monetary policy is also expected to contribute to this.

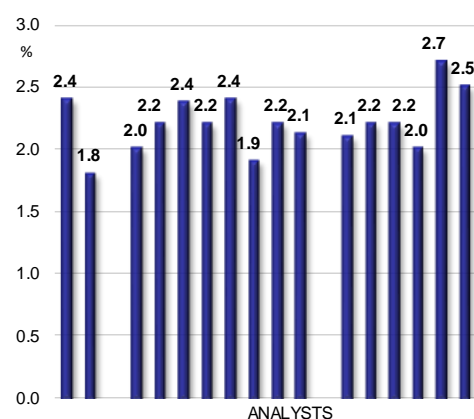
CONSUMER PRICE INDEX

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

(%)

June 2021	end of year	
	current	current + 1Y
minimum	2.5	2.3
average	3.6	4.3
maximum	5.3	5.5

FORECAST FOR GDP GROWTH

(%)

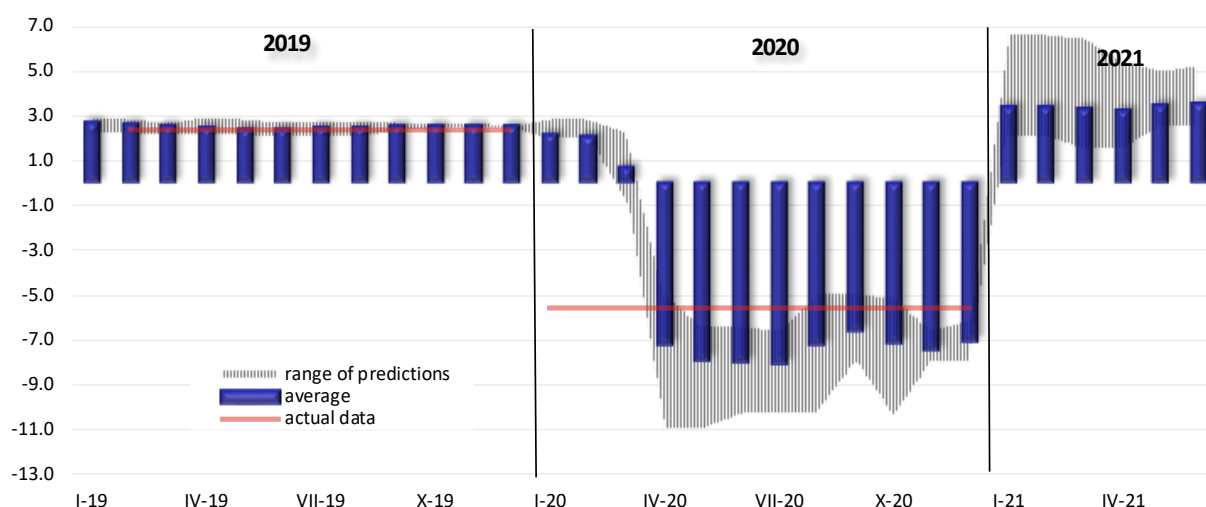
Date of Prediction	end of year	
	current	current+1Y
VI.20	-7.9	5.6
VII.20	-8.0	5.6
VIII.20	-7.2	5.0
X.20	-7.1	4.3
XII.20	-7.0	3.5
III.21	3.3	4.4
V.21	3.5	4.5
VI.21	3.6	4.3

Compared to the previous survey, analysts are now slightly more optimistic about domestic economic growth this year. They expect the annual GDP growth rate to reach 3.6%, up by 0.1 percentage point from May. Conversely, economic growth is expected to be slower next year at 4.3%, as against 4.5% in the previous survey. The range of the individual estimates widened. This was due to an increase in the maximum value for 2021 estimates, while in the case of next year's forecasts it was due to a larger decline in the minimum value.

The analysts generally expect the domestic economy to rebound gradually from 2021 Q2. They assume that household consumption will increase significantly as restrictions are lifted and shops and services reopen. This will be fostered not only by savings generated by consumers during lockdown but also by a tax change. The conditions on the labour market are also essential for consumer appetite, where there has been no dramatic increase in unemployment or fall in wages, despite a very unfavourable pandemic situation. Moreover, the high growth rates of household consumption will also stem from base effects in 2021. Government consumption is also expected to foster growth (perhaps not to the same extent as before), reflecting the upcoming parliamentary elections. According to the analysts, fiscal consolidation will occur only after the elections. Investment activity is expected to increase as the economy recovers; it was favourable already in 2021 Q1 and will be boosted by financial resources from EU funds. External demand is also likely to strengthen as the global economy recovers, but the growth rate of imports might exceed the growth rate of exports this year due to increased consumption and investment activity. However, this should change in the years ahead and net exports are expected to again be one of the components of Czech GDP which will foster growth. Nevertheless, the above scenario is fraught by uncertainty, which stems from a potential deterioration of the pandemic situation and the related restrictive measures.

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

(%)

June 2021	2W repo rate		12M PRIBOR		5Y IRS		10Y IRS	
	1M	1Y	1M	1Y	1M	1Y	1M	1Y
minimum	0.25	0.50	0.75	0.85	1.51	1.80	1.70	1.90
average	0.42	1.16	0.84	1.66	1.77	2.11	1.85	2.21
maximum	0.50	1.50	0.98	2.00	1.90	2.50	1.95	2.55

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
VI.20	0.20	0.14	0.41	0.41	0.55	0.67	0.76	0.92
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
III.21	0.25	0.64	0.56	1.00	1.44	1.71	1.70	1.95
V.21	0.27	0.88	0.67	1.31	1.70	1.95	1.84	2.07
VI.21	0.42	1.16	0.84	1.66	1.77	2.11	1.85	2.21

ACTUAL INDICATOR VALUES AS OF FORECAST DEADLINE

(%)

	2W repo rate	12M PRIBOR	5Y IRS	10Y IRS
15.6.	0.25	0.73	1.65	1.64

The analysts' view of the CNB's meeting in June shifted considerably due to the bank's communication. While only one respondent had expected key interest rates to increase in May, eleven of them were now expecting an increase. The remaining five respondents expected the CNB to tighten its monetary policy later. According to the analysts, the CNB Bank Board sent a clear signal that it does not want to tolerate high inflation and that it is preparing itself and the market for an interest rate increase, which is forecast to occur around the middle of the year. However, it was clear that the decision to increase interest rates would not be unanimous. Oldřich Dědek had already clearly voiced his reservations and cautious approach and Aleš Michl's statements were perceived in a similar way.

A pronounced shift to higher expected key interest rates can also be seen at the one-year horizon. While in the May survey most of the analysts (specifically five) expected the 2W repo rate to be set at 1.00%, eight respondents are now expecting it to increase to 1.25%, and two are even expecting it to increase to 1.50%. In their forecasts, the analysts take into account not only the CNB's hawkish communication but also the surprisingly strong growth in core inflation and especially progress in vaccination, which reduces uncertainty about the strength of the economic recovery. They believe that the CNB forecast is likely to prove too pessimistic and will have to be revised upwards. The arrival of an autumn wave of the pandemic is naturally the main risk and may put a spanner in the works of economic prospects.

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

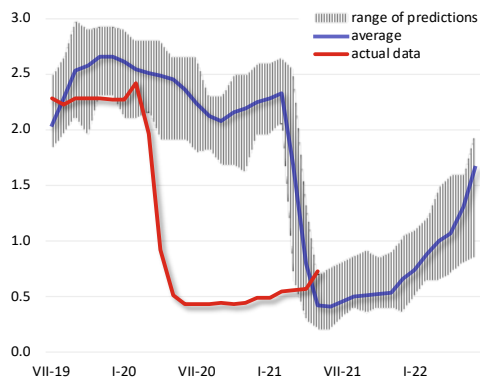
(%)

2W repo rate level in 1Y (%)	0.05	0.25	0.50	0.75	1	1.25	1.5
number of analysts - current survey	0	0	2	0	3	8	3
-previous survey	0	0	3	4	5	3	0

Optimism regarding the economic recovery and the prospect of higher key interest rates were also reflected in interbank market reference rates and swap rates, or their forecasts, which increased by 1–35 basis points. Due to faster growth in shorter maturity, the difference between 5Y IRS and 10Y IRS decreased again slightly, and the expected slope of the swap curve has thus flattened in this area.

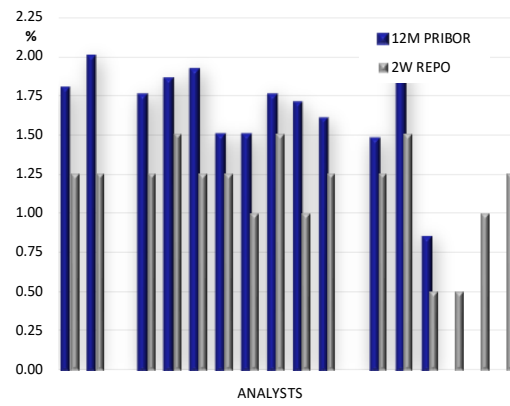
12M PRIBOR AT 1Y

ACTUAL DATA, AVERAGE AND RANGE OF PREDICTIONS



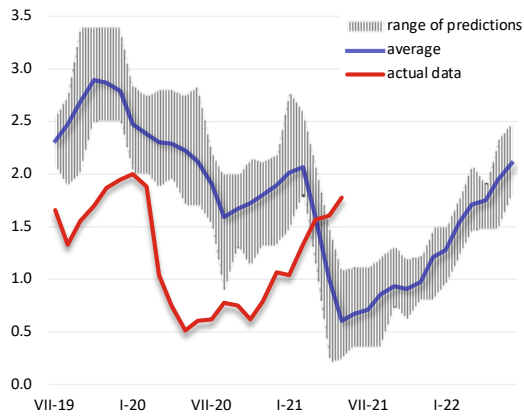
2W REPO AND 12M PRIBOR AT 1Y

PREDICTIONS OF INDIVIDUAL ANALYSTS



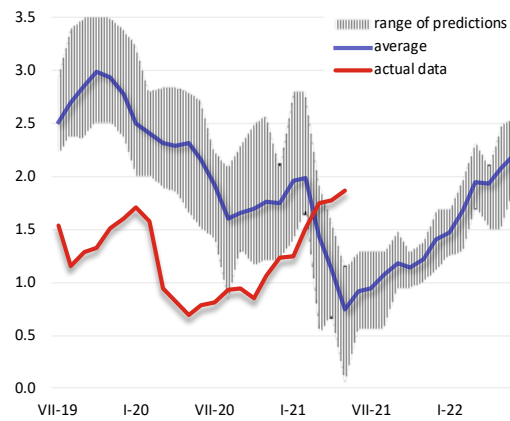
5Y IRS AT 1Y

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
VI.20	26.67	26.01
VII.20	26.64	25.93
VIII.20	26.17	25.76
X.20	27.11	25.88
XII.20	26.33	25.63
III.21	26.01	25.32
V.21	25.55	25.19
VI.21	25.36	24.88

EXCHANGE RATE FORECAST

June 2021	EUR/CZK	
	1M	1Y
minimum	25.20	24.20
average	25.36	24.88
maximum	25.50	25.38

ACTUAL EUR/CZK AS OF FORECAST DEADLINE

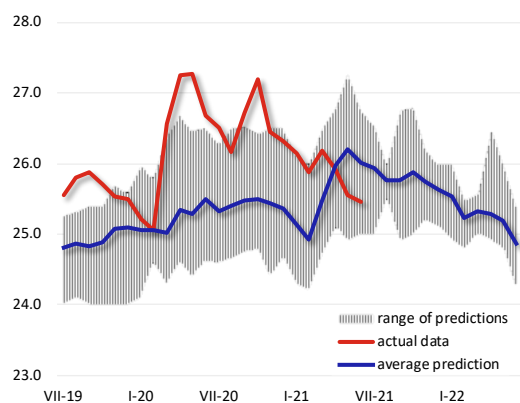
15.6.	25.45
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Although the koruna exchange rate appreciated only slightly on the foreign exchange market (up by around 4 hellers), its one-month forecast shifted from CZK 25.55 to the euro to CZK 24.36 to the euro. The one-year forecast changed to a similar extent, standing currently at CZK 24.88 to the euro.

Despite an expected increase in the CNB's interest rates, the analysts do not expect a more pronounced appreciation of the koruna at the one-month horizon. They believe that the tightening of the CNB's monetary policy is already incorporated in the current level of the koruna's exchange rate. The analysts are still expecting a gradual appreciation trend in the second half of this year and in the first half of next year, which is based mainly on the interest rate differential between the Czech Republic and the euro area and the convergence of the Czech economy to Western European countries. The stronger levels should also be fostered by generally better market sentiment associated with a global fading out of the pandemic. However, if the CNB were to suggest that it would increase its key rates more slowly than expected by the market due to pandemic-related uncertainty, there could be a temporary weakening of the koruna's exchange rate on the foreign exchange market.

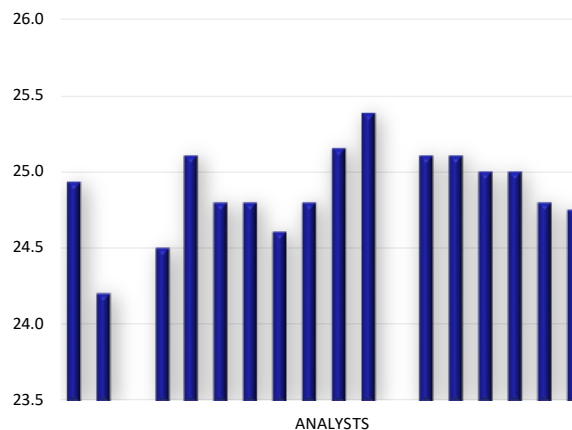
EUR/CZK

ACTUAL DATA, 1Y PREDICTIONS AND THEIR RANGE



EUR/CZK AT 1Y

PREDICTIONS OF INDIVIDUAL ANALYSTS



VI. NOMINAL WAGES

FORECAST FOR NOMINAL WAGE GROWTH

(%)

June 2021	year end	
	current	current+1Y
minimum	2.20	2.50
average	3.73	4.40
maximum	6.40	5.30

FORECAST FOR NOMINAL WAGE GROWTH

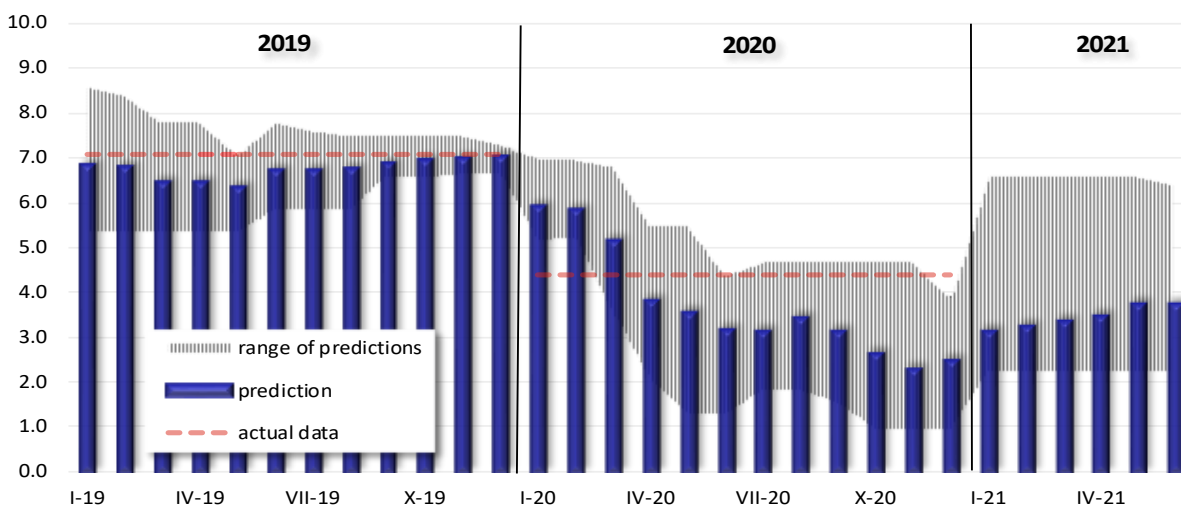
(%)

Date of Prediction	year end	
	current	current+1Y
VI.20	3.2	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
III.21	3.4	4.4
V.21	3.8	4.3
VI.21	3.7	4.4

Despite all the negative impacts of the pandemic, the situation on the labour market is not bad at all. Thanks to strong external demand and especially extensive government support programmes, unemployment and wage growth did not deteriorate as much as they could have in a similar crisis environment. According to the analysts, this can also be observed in the demand for labour, which did not decline significantly and continued to exceed the number of vacancies. Moreover, excess demand for new workers is expected to increase further now that the recovery has started. As the economy recovers, unemployment may thus decline from the second half of the year, which will strengthen the position of employees in wage negotiations. This, combined with inflation above the 2% target, creates conditions for relatively fast wage growth, while maintaining an acceptable pace in real terms. However, wage growth is lagging behind unemployment and will not become apparent until next year. Although the analysts have again corrected their forecasts for 2021 downwards by 0.1 percentage point on average to 3.7%, the outlook for next year has already been shifted upwards by 0.1 percentage point to 4.4%.

NOMINAL WAGE GROWTH

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



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