

# Financial Market Inflation Expectations

8/2021



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## I. SUMMARY

Twelve domestic and three foreign analysts sent in their contributions to the CNB's August survey, which was affected by the summer holidays. The results of the survey show that due to the latest economic developments, the analysts expect higher inflation at the one-year horizon even though the estimate for GDP growth was lowered for this year. By contrast, the outlook for economic growth for next year was increased. The three-year inflation forecast remains just above the CNB's 2% inflation target. The analysts believe overall that the economic conditions require greater monetary policy tightening and therefore expect interest rates to grow faster than they were predicting in the previous survey. In addition to the appreciation of the koruna from mid-June to mid-July, the change in the forecast for the exchange rate also reflects the expectation of tighter CNB monetary policy settings. The tight labour market and an increase in wages in the public sector will lead to faster nominal wage growth this year and the next.

<b>DOMESTIC ANALYSTS</b>	<b>I.</b>	<b>II.</b>	<b>III.</b>	<b>IV.</b>	<b>V.</b>	<b>VI.</b>	<b>VII.</b>	<b>VIII.</b>	<b>IX.</b>	<b>X.</b>	<b>XI.</b>	<b>XII.</b>
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 Jách, 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	+	+	+	+	+	+	+	+				
<b>FOREIGN ANALYSTS</b>												
Timon Dreyer, Kevin Daly, Goldman Sachs	+	+	+	+	+	+	+	+				
Alessandro Cugnasca, 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, 25 August 2021

## II. INFLATION

### FORECAST FOR Y/Y CPI GROWTH

(%)

August 2021	CPI	
	1Y	3Y
minimum	1.9	2.0
average	2.4	2.1
maximum	2.7	2.4

### 1Y AND 3Y FORECAST FOR CPI GROWTH

(%)

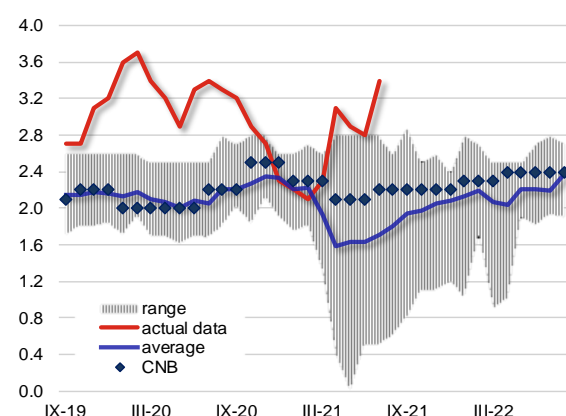
Date of Prediction	ANALYSTS		CNB (%)
	1Y	3Y	1Y
VIII.20	1.8	2.0	3Q: 2.2
X.20	2.0	2.0	
XII.20	2.1	2.0	4Q: 2.2
III.21	2.1	2.0	1Q: 2.3
V.21	2.2	2.1	
VI.21	2.2	2.1	2Q: 2.4
VII.21	2.2	2.1	3Q: 2.4
VIII.21	2.4	2.1	

Monthly CPI inflation in the Czech Republic picked up to 1.0% in July, which was due mainly to an increase in prices of package holidays. Inflation picked up by 0.6 percentage point to 3.4% year on year. According to the CZSO, this was largely due to higher transport prices. Fuel prices rose substantially compared to last July, with car prices also going up. alcoholic beverages, tobacco and housing also largely contributed to annual inflation. The analysts' average forecast – up by 0.2 percentage point to 2.4% at the one-year horizon – was also in response to the surprisingly large increase in inflation in July, which moved well beyond the tolerance band. By contrast, the three-year forecast is unchanged from the previous survey, remaining just above the CNB's 2% inflation target, i.e. at 2.1%. The range of the individual forecast narrowed owing to a decline in the maximum values at both the one-year and three-year horizons.

The analysts continue to see the strong labour market as the main inflationary factor as the unemployment rate remains very low despite the pandemic. The low unemployment rate creates favourable conditions for strong household demand. This is accompanied by the rapid growth in prices of food, materials and energy, most notably oil and – depending on oil prices – fuel prices. Price growth is also visible in services and the accelerating inflation is probably also due largely to shortfalls in firms' subcontracting chains. The analysts admit that the annual growth rate of the CPI may climb to 4% in the months ahead, with some estimates well above this level. This notwithstanding, the pace of inflation is expected to weaken gradually next year as the CNB's tightening of monetary policy starts to have an effect, the current one-off pandemic-related factors gradually subside and the effect of a stronger koruna exchange rate is reflected in import prices.

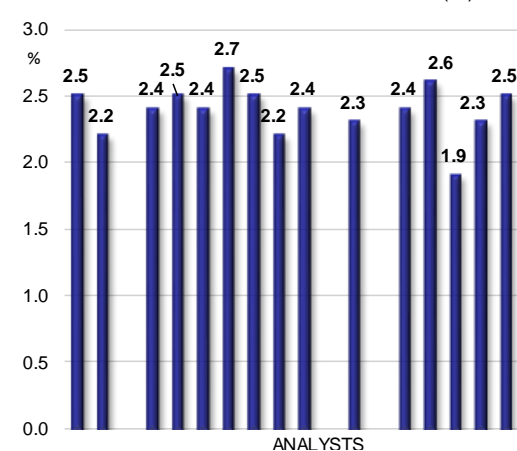
### CONSUMER PRICE INDEX

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

(%)

August 2021	end of year	
	current	current + 1Y
minimum	2.8	3.4
average	3.4	4.7
maximum	4.2	6.9

#### FORECAST FOR GDP GROWTH

(%)

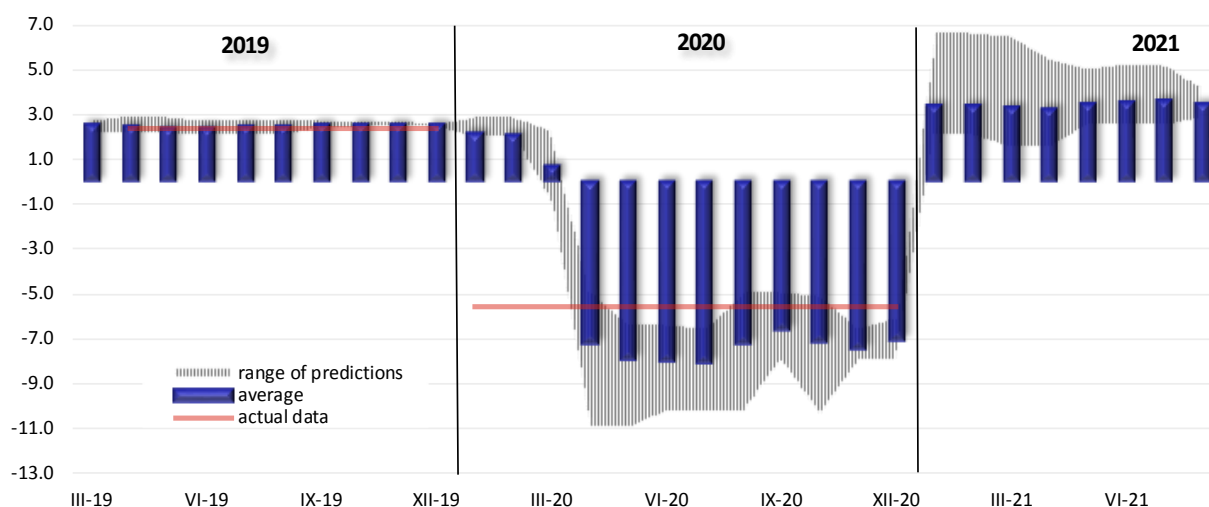
Date of Prediction	end of year	
	current	current+1Y
V.III.20	-7.2	5.0
X.20	-7.1	4.3
XII.20	-7.0	3.5
III.21	3.3	4.4
V.21	3.5	4.5
VI.21	3.6	4.3
VII.21	3.6	4.5
VIII.21	3.4	4.7

At the end of July, the CZSO published a flash estimate for Czech GDP growth in 2021 Q2, which lagged behind estimates. GDP grew by a mere 0.6% quarter on quarter, which represents annual growth of 7.8%, whereas quarterly growth around 2% had been expected, given the anti-epidemic measures in 2021 Q1 and the recovery in domestic and external demand in 2021 Q2. The cause of such low economic growth will be published along with a more accurate estimate. However, worse-than-expected growth in 2021 Q2 is naturally reflected in the analysts' forecast for this year, which was lowered by 0.2 percentage point to 3.4%. By contrast, the outlook for next year increased by the same amount to 4.7%. The range of the individual estimates for this year narrowed due to a decrease in the maximum value and an increase in the minimum value, while the outlooks for next year narrowed due to a greater increase in the minimum value.

Although the analysts expect the Czech economic recovery this year to be driven by domestic and foreign demand, the latest data published have reined in the expectations regarding its intensity. At the same time, the analysts admit that it would come as no surprise if a refined estimate led to a more significant upward revision. Domestic demand is expected to be driven mainly by a strong labour market, rapid wage growth and household consumption, while a recovery in external demand will foster Czech exports and also boost firms' investment activity. An inflow of funds from the EU is also expected to have a pro-growth effect. However, these estimates are based on the assumption that the pandemic situation will not worsen to the extent that large-scale closures will have to take place. Although this is unlikely, nothing can be ruled out based on previous experience, and the resulting economic performance would naturally be lower.

#### 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

(%)

August 2021	2W repo rate		12M PRIBOR		5Y IRS		10Y IRS	
	1M	1Y	1M	1Y	1M	1Y	1M	1Y
<b>minimum</b>	0.75	1.25	1.25	1.50	1.96	2.15	1.70	1.90
<b>average</b>	1.00	1.80	1.36	2.14	2.12	2.34	1.98	2.31
<b>maximum</b>	1.25	2.25	1.50	2.35	2.27	2.60	2.20	2.70

### 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
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
VII.21	0.67	1.39	1.14	1.85	1.88	2.15	1.86	2.19
VIII.21	1.00	1.80	1.36	2.14	2.12	2.34	1.98	2.31

### ACTUAL INDICATOR VALUES AS OF FORECAST DEADLINE

(%)

	2W repo rate	12M PRIBOR	5Y IRS	10Y IRS
<b>15.8.</b>	0.75	1.34	2.14	1.95

Most of the respondents (11 of 15) estimate that the CNB Bank Board will again increase the 2W repo rate by 25 basis points to 1.00% at its regular meeting in September 2021. Two analysts expect it to increase by 50 basis points to 1.25%, while two respondents expect it to remain at the current level. The one-year forecast was also revised significantly upwards, with most respondents (6 of 15) expecting the 2W repo rate to rise to 1.75% in the next 12 months. Five respondents expect it to increase to 2.00% and one to as much as 2.25%. The need for higher rates is based not only on macroeconomic data, i.e. mainly the surprising pace of inflation, but is also confirmed by the CNB itself through the hawkish tone of Board members' communication. Some of the analysts believe that concerns about increasing inflation expectations will strengthen the Bank Board's willingness to tighten monetary policy. The key rates might thus be raised at each CNB monetary policy meeting until the end of the year, and the increase may be by as much as 50 basis points at the upcoming meetings. This is despite weaker data on GDP growth in 2021 Q2. However, there is still a risk that any worsening of the pandemic situation will entirely reshape this scenario.

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

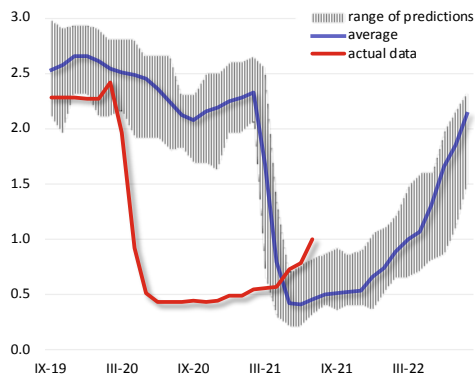
(%)

2W repo rate level in 1Y (%)	0.5	0.75	1.00	1.25	1.5	1.75	2	2.25
<b>number of analysts - current survey</b>	0	0	0	1	2	6	5	1
<b>-previous survey</b>	0	1	1	5	6	3	0	0

The assumption of a faster tightening of the CNB's key interest rates and a rise in current market interest rates is unavoidably reflected in the analysts' forecasts, which rose again. The average forecasts for the PRIBOR interbank reference rates increased by 22–29 basis points and the forecasts for IRS rates by 12–23 basis points.

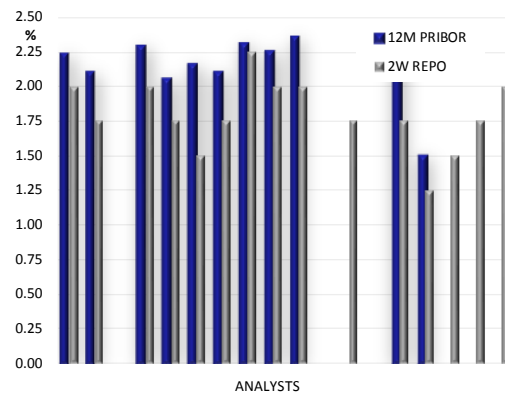
**12M PRIBOR AT 1Y**

ACTUAL DATA, AVERAGE AND RANGE OF PREDICTIONS



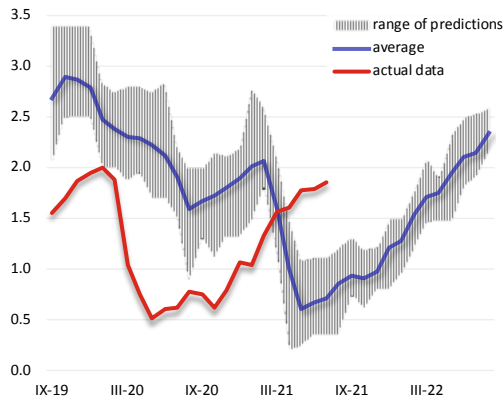
**2W REPO AND 12M PRIBOR AT 1Y**

PREDICTIONS OF INDIVIDUAL ANALYSTS



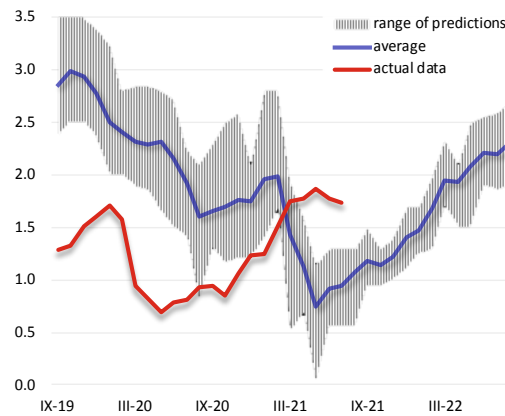
**5Y IRS AT 1Y**

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
V.III.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
VII.21	25.46	24.93
VIII.21	25.37	24.82

### EXCHANGE RATE FORECAST

August 2021	EUR/CZK	
	1M	1Y
minimum	25.20	24.00
average	25.37	24.82
maximum	25.50	25.20

### ACTUAL EUR/CZK AS OF FORECAST DEADLINE

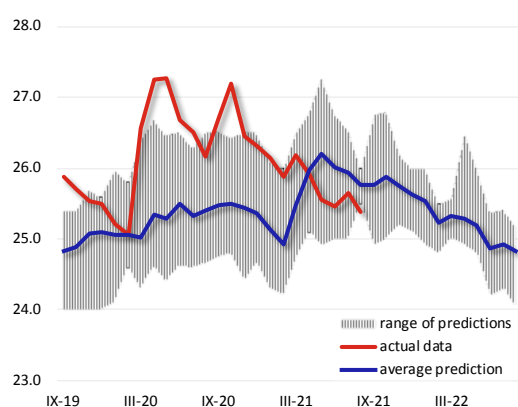
15.8.	25.39
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The koruna's exchange rate appreciated against the euro by around 20 hellers to CZK 25.39 compared to the previous survey. As usual, this was also reflected in the analysts' updated forecasts, which shifted to stronger levels at the two monitored horizons. On average, the koruna is thus expected to be around CZK 25.37 to the euro in mid-September and gradually appreciate to CZK 24.82 to the euro by August 2022.

In addition to a change in initial conditions, the shift of the forecasts to stronger levels is due to an assumption of an even faster rise in key interest rates than expected last month. The scenario of gradual appreciation of the koruna's exchange rate based on the continuing convergence of the Czech economy towards Western European countries remains the main predetermining aspect of a future long-term trend. A growing interest rate differential, especially when compared with the interest rate settings in the euro area, will add to this. Last but not least, the koruna may also appreciate due to an improvement in global sentiment if the pandemic starts to fade. On the other hand, any worsening of the pandemic situation, in the Czech Republic or abroad, will exert downward pressures on the koruna's exchange rate.

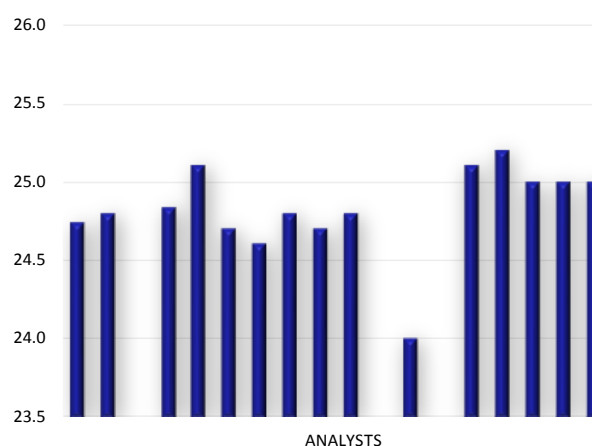
### EUR/CZK

#### ACTUAL DATA, 1Y PREDICTIONS AND THEIR RANGE



### EUR/CZK AT 1Y

#### PREDICTIONS OF INDIVIDUAL ANALYSTS



## VI. NOMINAL WAGES

### FORECAST FOR NOMINAL WAGE GROWTH

(%)

August 2021	year end	
	current	current+1Y
minimum	3.2	3.0
average	4.0	4.6
maximum	5.0	5.3

### FORECAST FOR NOMINAL WAGE GROWTH

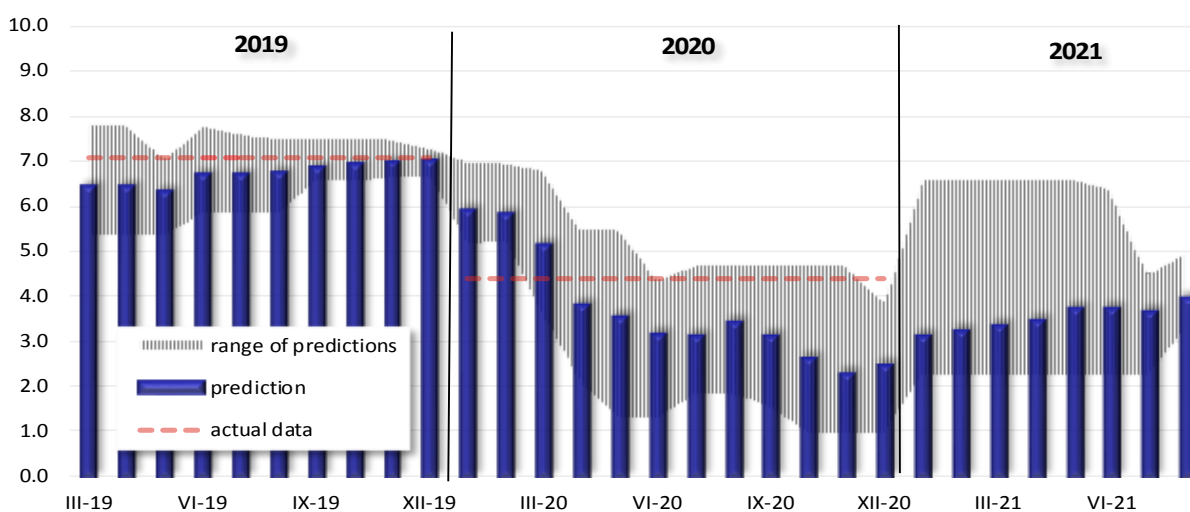
(%)

Date of Prediction	year end	
	current	current+1Y
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
VII.21	3.7	4.5
VIII.21	4.0	4.6

The labour market conditions remain very favourable for employees. The general unemployment rate according to the Labour Force Survey, i.e. the share of unemployed persons to economically active persons aged 15–64, dropped to 2.9% in June and the annual increase is virtually negligible despite the pandemic crisis. Although there is usually a decline in recruitment in July due to the holidays, according to the Czech Labour Office the share of unemployed persons remained unchanged at 3.7% in the first month of the holidays. This is even slightly less than in July 2020 and is one of the lowest levels in the EU. Some industries which incurred considerable economic losses in the past months, such as restaurants, services and transport, are almost fully up and running again in some regions. By contrast, the situation is worse from an employer's perspective; firms are looking for new employees and a shortage of high-quality applicants is often mentioned as an issue. This negative effect will be dampened only slightly by the termination of government support programmes, which artificially maintained unemployment at low levels. Therefore, unemployment is not expected to grow significantly in the years ahead, rather the opposite. This, combined with inflation currently above the CNB's tolerance band, paves the way for higher wage growth. The analysts' forecast for this year was thus increased by 0.3 percentage point to 4.0%, with the public sector being again the main driver, due mainly to the payment of special bonuses in health care. Wage growth is expected to pick up to 4.6% next year, 0.1 percentage point more than in the July survey.

### NOMINAL WAGE GROWTH

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



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