



Press conference of the CNB Bank Board

7th Situation Report on Economic and Monetary Developments

3 November 2016

The monetary policy decision and the stance of the CNB

- At the close of the meeting the Board decided unanimously to leave interest rates unchanged. The two-week repo rate remains at 0.05%, the discount rate at 0.05% and the Lombard rate at 0.25%.
- The Board also decided to continue using the exchange rate as an additional instrument for easing the monetary conditions and confirmed the CNB's commitment to intervene unlimitedly on the FX market if needed to weaken the koruna so that the exchange rate of the koruna against the euro is kept close to CZK 27.
- The Board repeated that the exchange rate commitment is one-sided. This means the CNB will not allow the koruna to appreciate to levels it would no longer be possible to interpret as “close to CZK 27/EUR”. The CNB prevents such appreciation by means of automatic and potentially unlimited interventions, i.e. by selling koruna and buying foreign currency. If the exchange rate departs from CZK 27/EUR on the weaker side, the CNB allows the koruna exchange rate to move according to supply and demand on the FX market.

Reasons for the decision in the context of the new forecast (i)

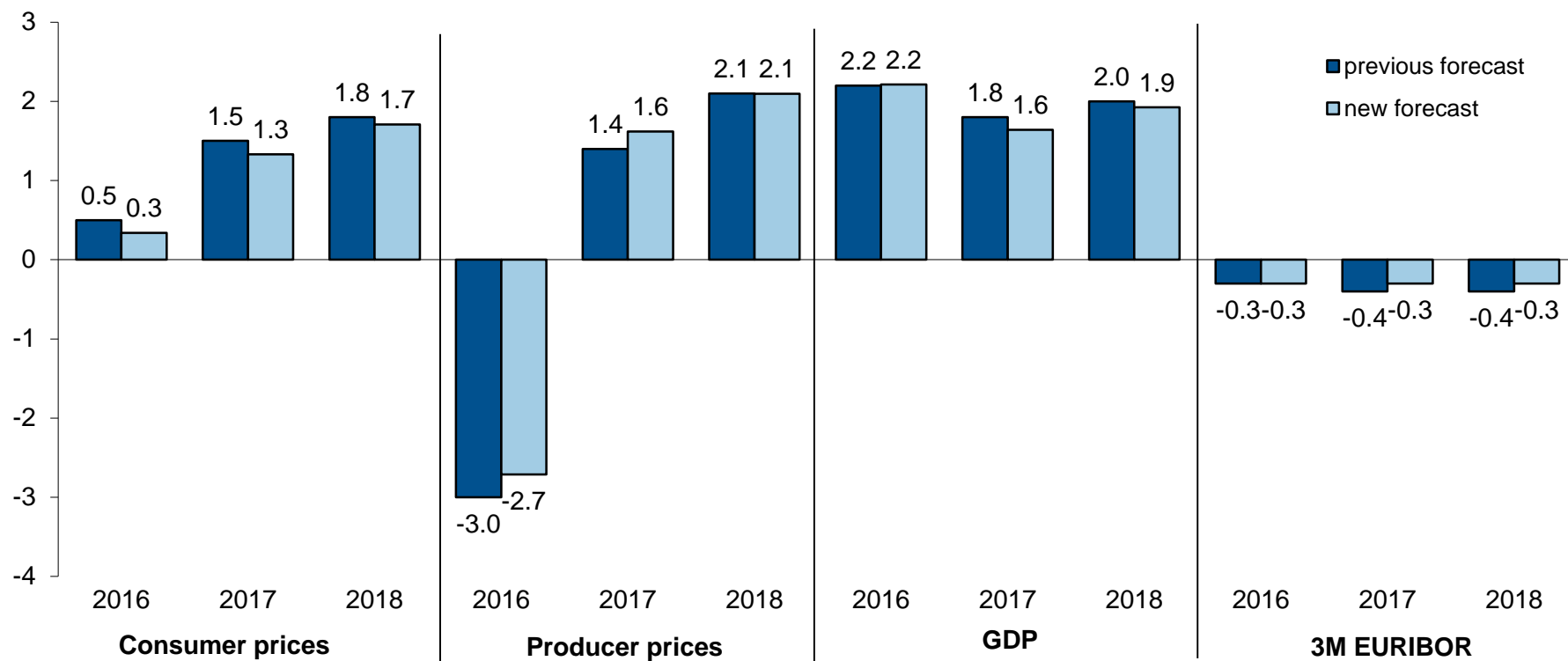
- The forecast assumes that market interest rates will be flat at their current very low level and the exchange rate will be used as a monetary policy instrument until mid-2017. Consistent with the forecast is an increase in market interest rates thereafter.
- Inflation is starting to rise, but it is still well below the CNB's target of 2%. According to the forecast, inflation will increase further and slightly exceed the 2% target at the monetary policy horizon. During 2018, it will return to the target from above.
- According to the forecast, sustainable fulfilment of the target, which is a condition for a return to conventional monetary policy, will occur from mid-2017 onwards.

Reasons for the decision in the context of the new forecast (ii)

- A need to maintain expansionary monetary conditions at least to the current extent persists.
- The Bank Board states again that the CNB will not discontinue the use of the exchange rate as a monetary policy instrument before 2017 Q2.
- The Bank Board still considers it likely that the commitment will be discontinued in mid-2017.

The external environment (i)

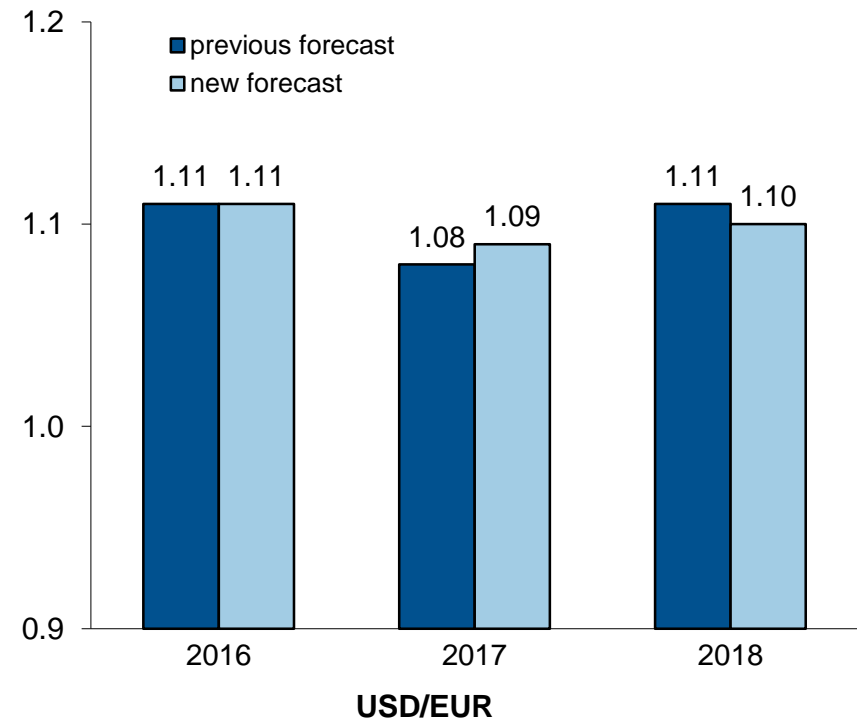
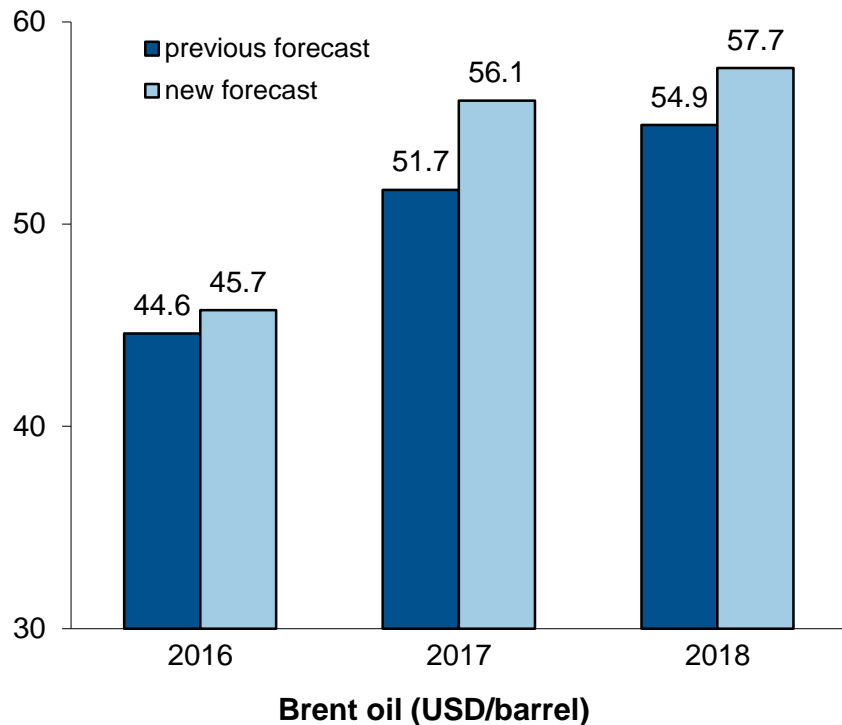
Comparison between the assumptions of the new and previous forecasts for the effective euro area*



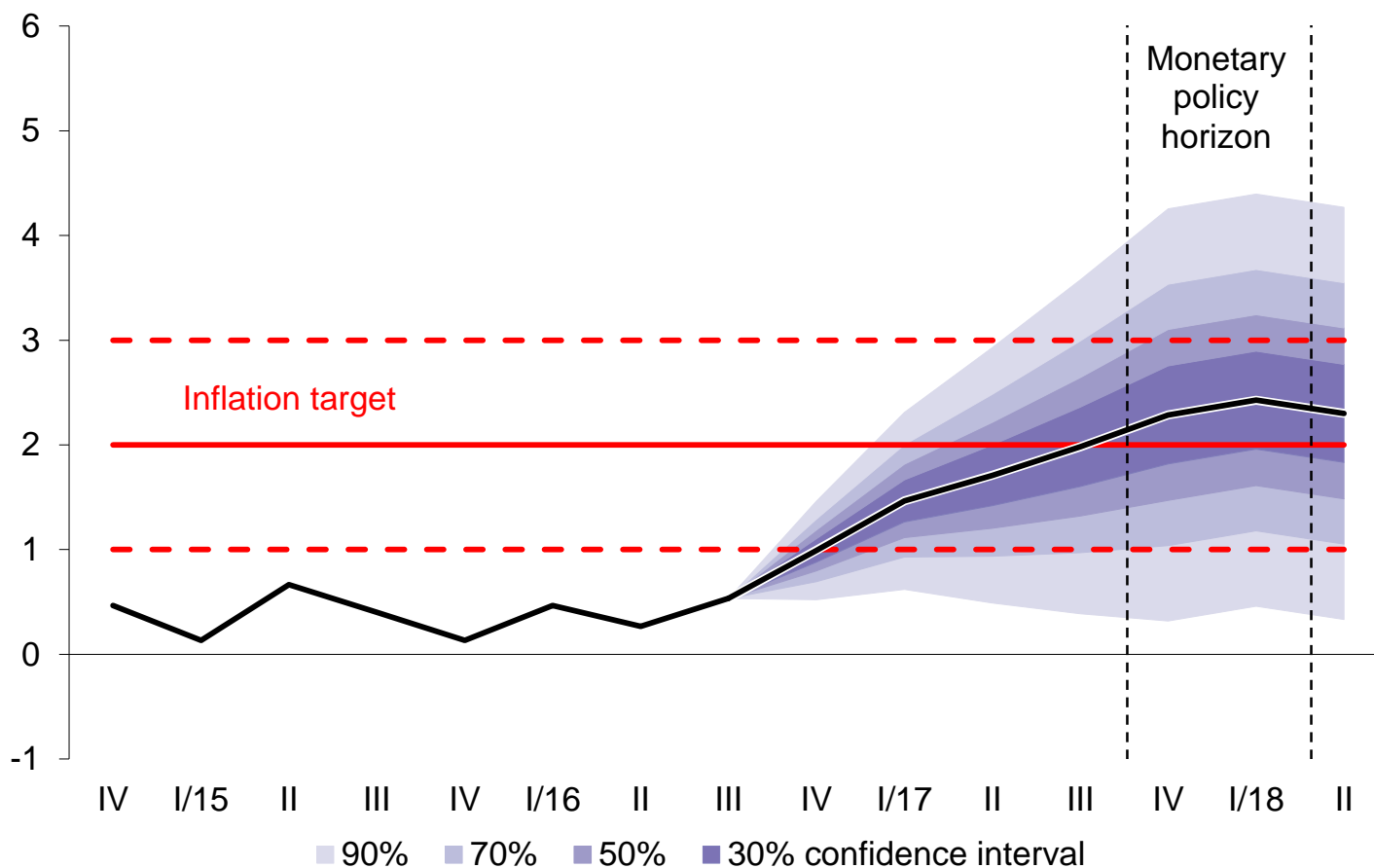
* Effective euro area means that individual countries of the euro area are weighted by their share in Czech exports

The external environment (ii)

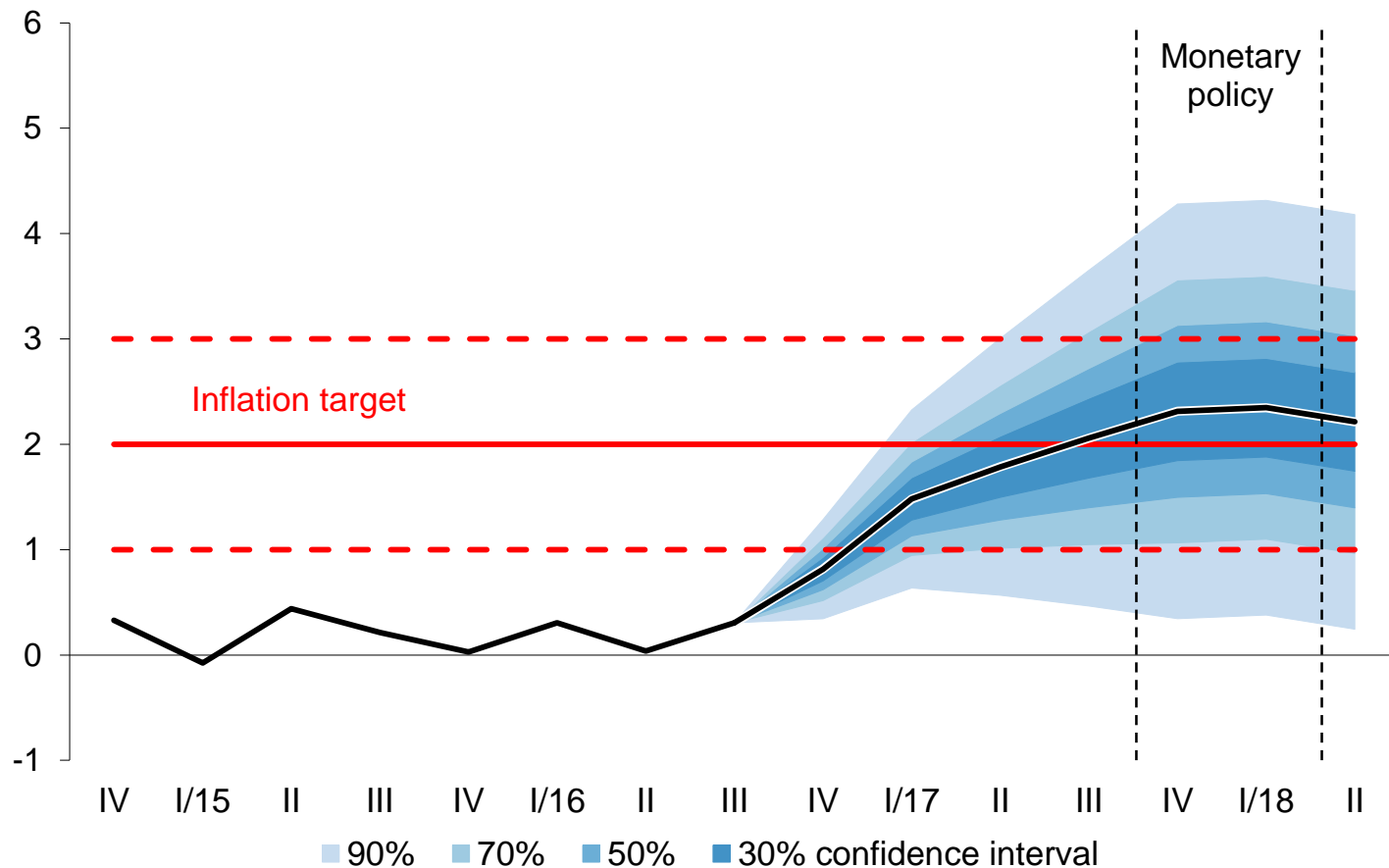
Comparison between the assumptions of the new and previous forecasts



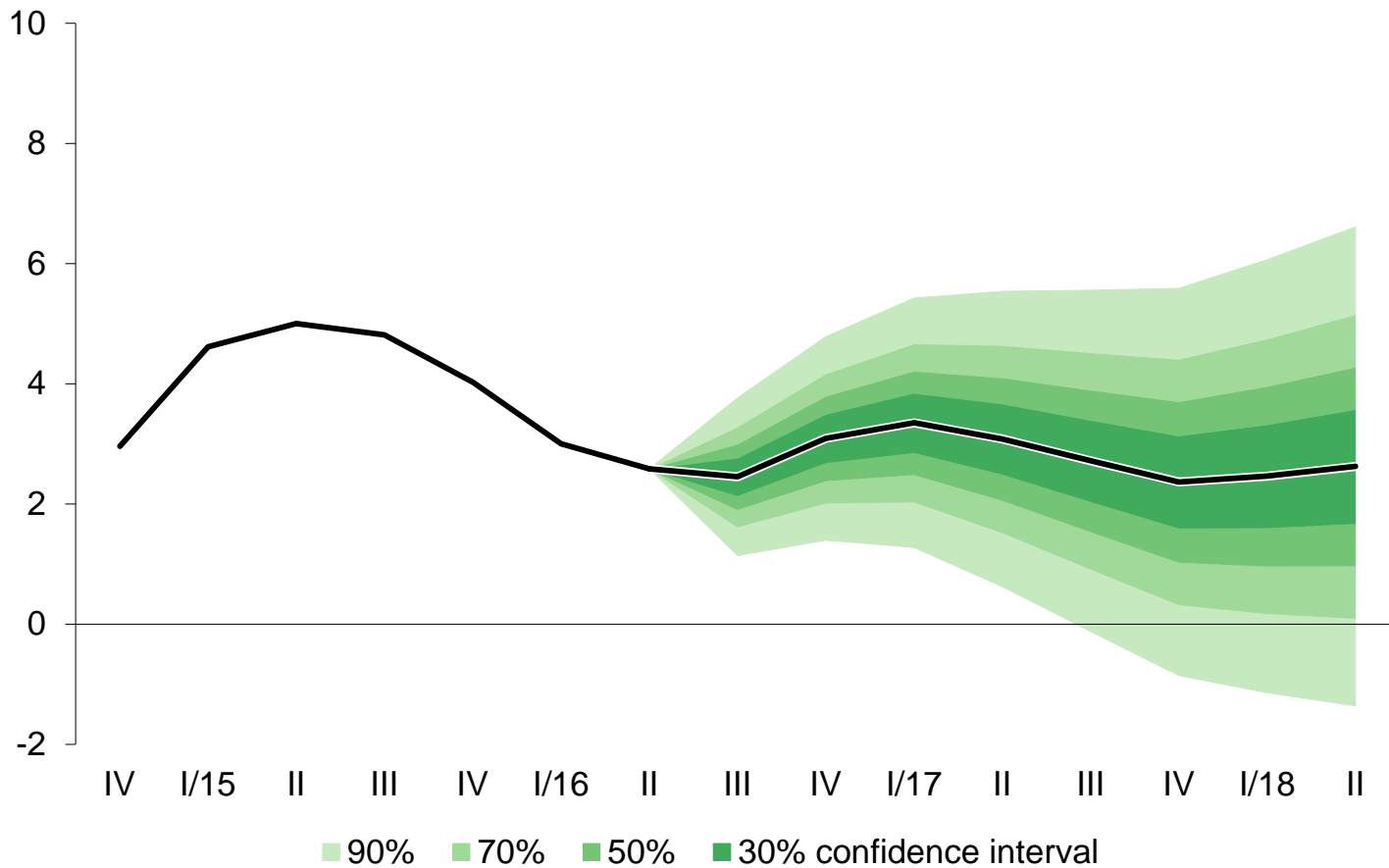
The forecast for headline inflation



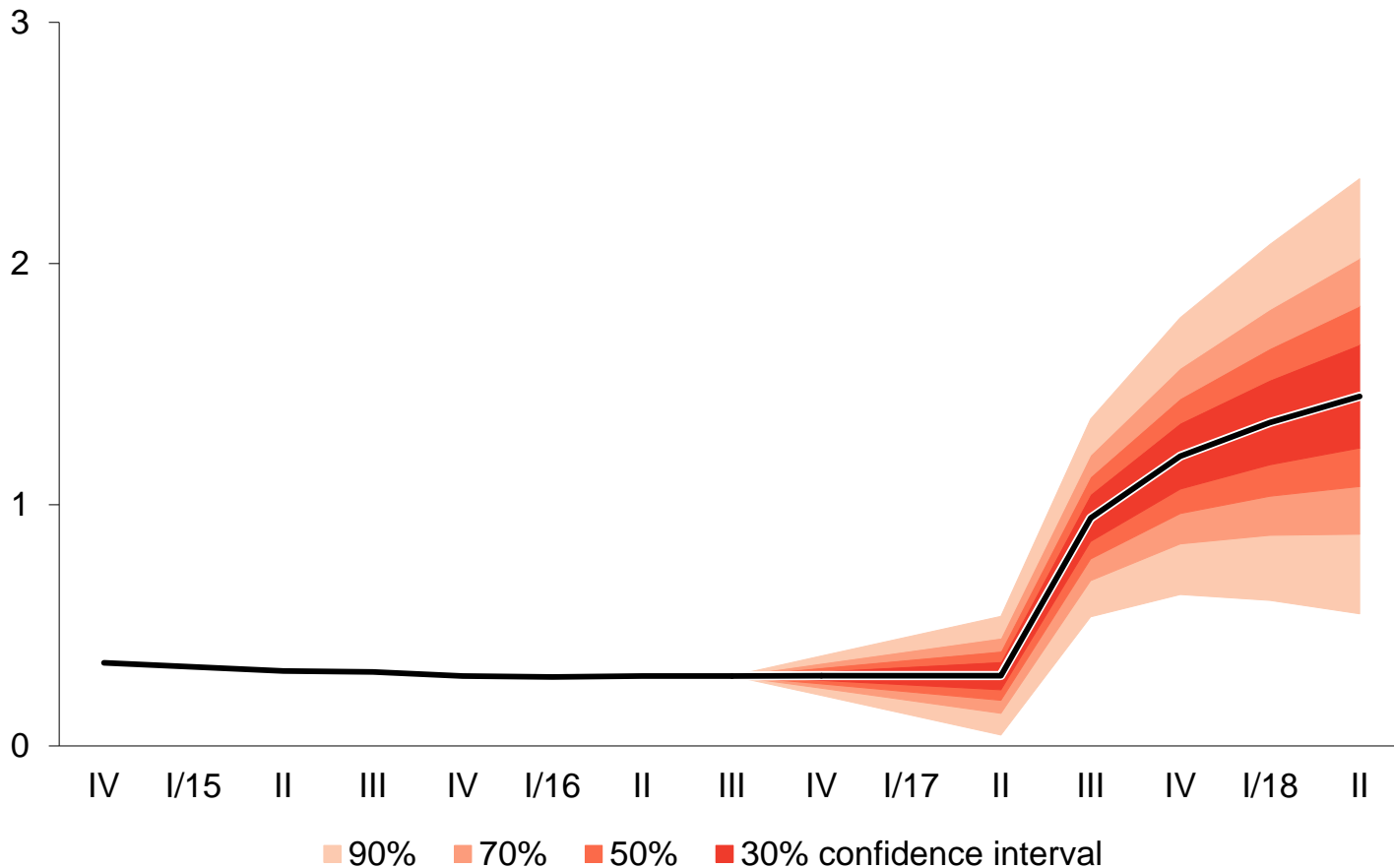
The forecast for monetary policy-relevant inflation



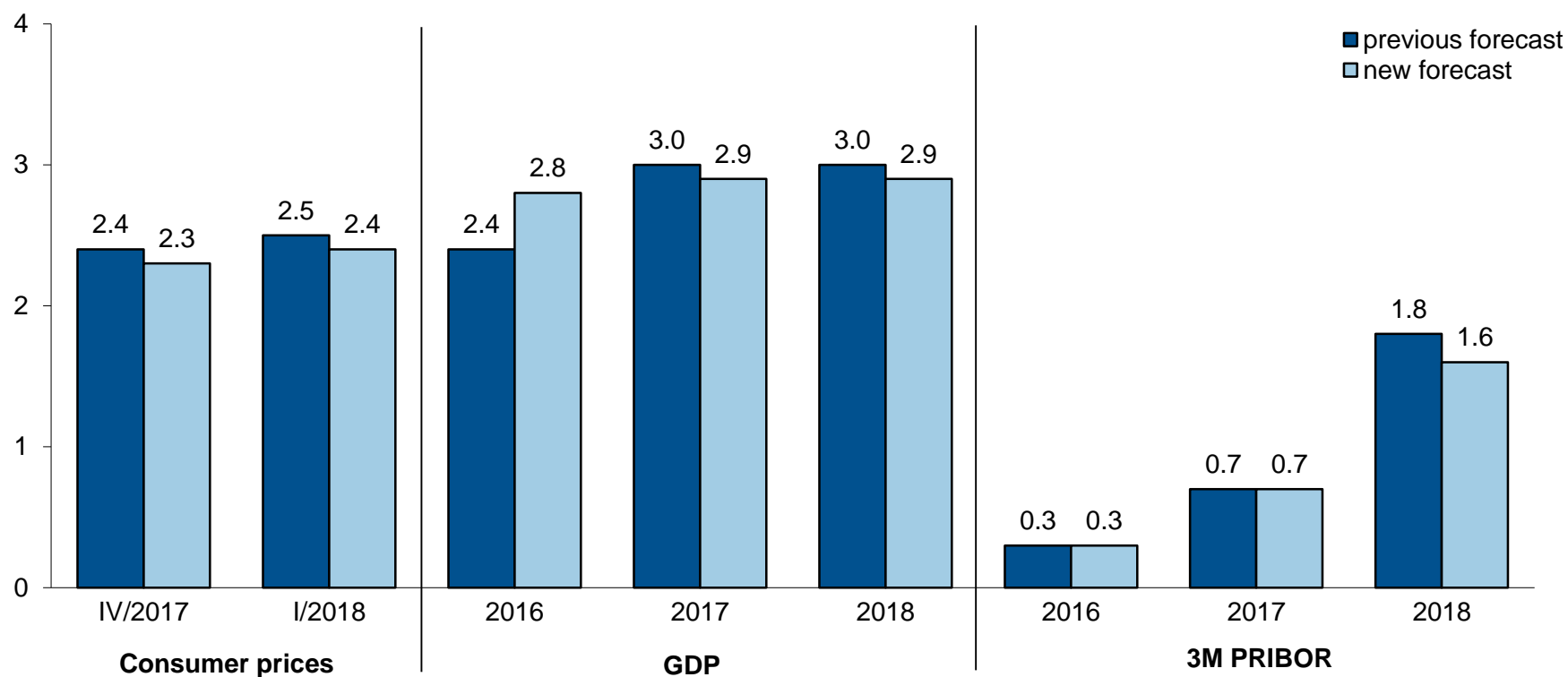
The forecast for GDP



The forecast for interest rates (3M PRIBOR)



Comparison with the previous forecast



Risks to the forecast

The Bank Board assessed the risks to the forecast as being balanced.

Uncertainties:

- the speed of return to growth in government and corporate investment
- the effect of the election cycle on discretionary government expenditure
- the impacts of the outcome of the UK referendum on external demand
- the future settings of the monetary conditions of the major central banks

Summary

- The Bank Board decided to leave interest rates unchanged and to continue using the exchange rate as an additional instrument for easing the monetary conditions.
- A need to maintain expansionary monetary conditions at least to the current extent persists. The Bank Board assessed the risks to the new forecast as being balanced.
- The CNB will not discontinue the use of the exchange rate as a monetary policy instrument before 2017 Q2.
- The Bank Board still considers it likely that the exchange rate commitment will be discontinued in mid-2017.



Thank you for your attention

More information about the forecast can be found at

http://www.cnb.cz/en/monetary_policy/forecast/

and in Inflation Report IV/2016. The summary of the Report (together with the table of key macroeconomic indicators) will be published on 4 November 2016. The whole Report will be published on 11 November 2016.