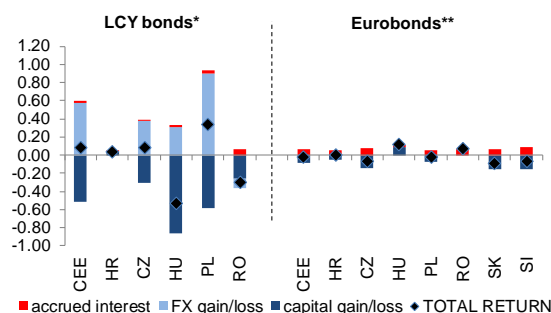
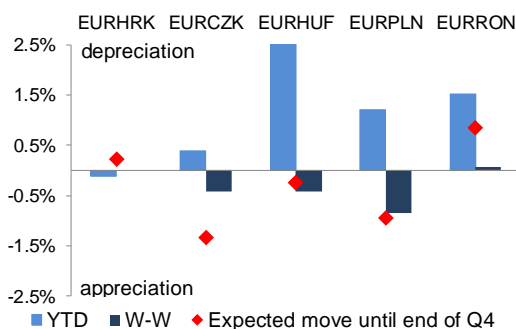


# CEE Market Insights

## Market outlook

The ECB decision will undoubtedly be a major factor for CEE FXFI markets this week, while developments around Brexit could also complicate the picture. Although we expect that a 10bp cut in the deposit rate will be delivered and monthly purchases of EUR 40bn worth of bonds could come from the ECB, markets are likely expecting somewhat more radical moves and thus there is a risk for a hawkish surprise. In this case, the US dollar may fall against the euro, which is usually positive for CEE currencies, but could also increase market uncertainty in general. In this case, however, government bond yields will likely not be able to avoid an increase.

This time, it was an improvement in the global market mood that caused CEE yields to increase and this also brought temporary relief to CEE currencies. The fact that spreads over German Bunds also grew is likely due to the fact that investors started eyeing stocks and should not have anything to do with local fundamentals. Croatian bonds continued to avoid the trend and delivered further yield declines. As we have noted, we cut our Croatian 10Y yield forecast due to this resilience. In Serbia, while the central bank again had to resort to interventions on the market to keep the RSD from appreciating, we do not think that a rate cut could come this week.



## Looking ahead this week:

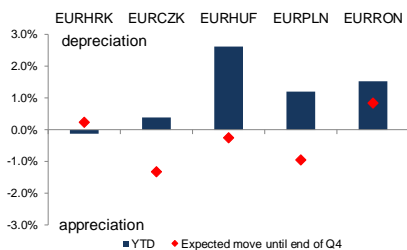
Monday	Tuesday	Wednesday	Thursday	Friday
RO: Trade Balance, Wages SI: Trade Balance	SK, SI: Industry CZ, HU: CPI HR: PPI	PL: Target Rate RO: CPI	RS: Target Rate, CPI RO: Industry SK: Wages	RO: Current Account SK: CPI PL: CPI, Trade Balance

This week, inflation rate and industrial output data will be in focus in CEE, as well as MPC meetings in Poland and Serbia. In the Czech Republic, Hungary and Romania, we expect headline CPI to ease marginally in August, as was the case in Poland, where we await confirmation of the flash reading. In Serbia, the inflation rate should remain stable, close to the lower bound of the inflation target. Given the limited inflationary pressure, the Serbian central bank is likely to keep the policy rate unchanged at 2.5% after delivering two cuts. Stability of rates is also the baseline scenario in Poland. Even if the MPC gets to discuss rate hike motions, as was the case at the last meeting, we believe that a majority to pass such a motion is unlikely to form. Industrial production output in July recovered in the Czech Republic, Croatia, Hungary and Poland so far. This week, we will see the industry figure for Slovenia, which is expected to grow, albeit at a slower pace compared to the previous month, while in Romania a further contraction is the most likely scenario.

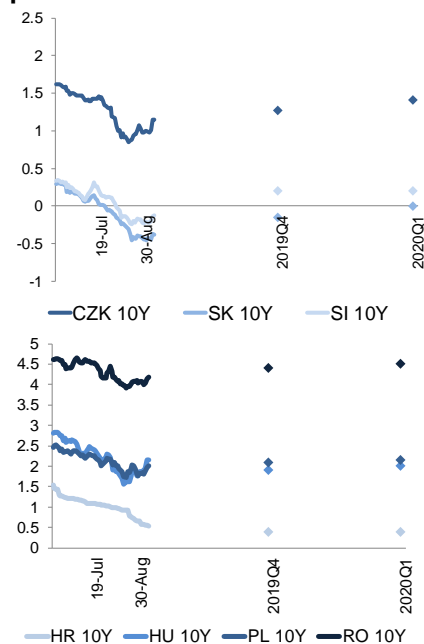
## In case you missed it last week...

- HR: [Industrial production](#) growth accelerated in July.
- CZ: Growth of [industrial output](#) and retail sales surprised to the upside.
- HU: Solid performance of the [industry](#) and [retail sales](#) in July.
- SK: Net exports and fixed investment dragged down [growth to 2.0% y/y in 2Q](#), while [retail sales](#) slump again.
- RO: Investments supported the [GDP growth](#) in 2Q19, while [retail sales](#) in July landed at four-month high.
- RS: GDP release revealed an [unchanged growth profile](#), with robust domestic demand activity.
- RS: [Moody's upgraded Serbian outlook](#) to positive and affirmed rating at Ba3

**YTD change on FX market**



**10Y government bond yields, percent**



Source: Erste Group Research, Bloomberg.

**On global markets:**

This week, the ECB Council meeting will decide on further measures to stimulate the economy. As there have hardly been any hints from the ECB, the uncertainty over the outcome is high. The gloomy outlook for the economy has pushed market expectations up, so a risk of a disappointment exists, which would also trigger a reaction by the EURUSD. In addition, further events regarding Brexit will shape markets this week.

**CEE currencies:**

Currencies in the region got temporary relief after global investor sentiment turned more positive last week. Trade war fears, the situation in Hong Kong and concerns around Brexit have all eased, giving way to some FX appreciation. It is uncertain how local currencies will fare going forward, however. This week, all eyes are on the ECB meeting, and there is a widespread expectation for something noteworthy to happen. We expect that a 10bp cut in the deposit rate will be delivered and monthly purchases of EUR 40bn worth of bonds could come from the ECB. Markets might expect something more radical, however. Therefore, there is a risk for a hawkish surprise. In such a case, the US dollar is likely to weaken against the euro, which could prove beneficial for CEE currencies. On the other hand, such a surprise could increase market uncertainty and reduce the carry favoring CEE FX. After the recent weakening of the Hungarian forint, we increased our forecast for the EURHUF and now expect it to hover between 325 and 335 vs. the range of 320-330 that we envisaged earlier. Besides global jitters, fears of high inflation are also abating, which could reinforce the MNB such that its strongly dovish bias could be maintained. This is not positive for the forint, however.

**CEE rates and yields:**

Yields increased considerably last week, amid the improving market mood and a likely rotation into stocks by investors. Spreads above German Bunds also increased in most CEE countries. A major outlier from this development is Croatia, where 10Y yields continued to slowly decline. We have therefore cut our 10Y HRK yield forecast. Also important to note is the increase in short-term rates in Romania, Poland and the Czech Republic in the last two weeks, indicating a lower probability of the monetary easing assumed by the markets. The only country where this is less visible is Hungary, where rates have already been very close to zero for a longer time already. As for Serbia, the central bank needed to again intervene on the RSD market to prevent the currency from appreciating (this time buying a total of EUR 80mn on the FX market). After the two rate cuts carried out earlier this summer, the pressure on the currency market has abated in Serbia, and only started to intensify in the very recent past. Thus, we do not expect the central bank to ease its policy this week.

## Calendar

Time	Country	Indicator	Period	Survey	Erste Est.	Prev.	Pre Comment
<b>9-Sep</b>							
8:00	RO	Trade Balance	Jul		-120.0%	-1130.9	Both exports and imports smaller in y/y terms in June.
8:00	RO	Wages (y/y)	Jul		15.4%	15.47%	Solid wage growth in public sector.
9:00	CZ	Unemployment	Aug	2.7%		2.7%	
10:30	SI	Trade Balance	Jul			0.13	
<b>10-Sep</b>							
9:00	SK	Industrial Production (y/y)	Jul			-3%	Industrial production in July was likely affected by planned summer breaks at some major industrial plants (esp. in the car sector).
9:00	CZ	CPI (y/y)	Aug	2.8%	2.7%	2.9%	CPI inflation still remains close to upper bound of tolerance band around inflation target. Sound labor market and positive development in foreign demand still most important proinflationary factors.
9:00	CZ	CPI (m/m)	Aug	0.0%	-0.1%	0.4%	We expect slight decrease in overall price level, mainly due to small correction in food prices.
9:00	HU	CPI (y/y)	Aug	3.3%		3.3%	
10:30	SI	Industrial Production (y/y)	Jul			1.1%	
11:00	HR	PPI (y/y)	Aug			0.3%	
<b>9-Sep</b>							
	PL	Target Rate	Sep	1.5%	1.5%	1.5%	
8:00	RO	CPI (y/y)	Aug	3.9%	3.9%	4.12%	Minor decrease of annual inflation rate in August.
8:00	RO	CPI (m/m)	Aug		0.1%	-0.2%	Rising tobacco price and lower pressure on food price at m/m level.
<b>9-Sep</b>							
8:00	RO	Industrial Production (y/y)	Jul		-2.7%	-4.1%	Weak external demand for local manufacturing.
9:00	SK	Wages (y/y)	Jul			-3.6%	
12:00	RS	CPI (y/y)	Aug		1.6%	1.6%	
12:00	RS	CPI (m/m)	Aug			-0.2%	
12:00	RS	Target Rate	Sep			2.5%	
<b>9-Sep</b>							
	RO	Current Account Balance (π	Jul			-5135	
9:00	SK	CPI (y/y)	Aug	2.7%		2.9%	Consumer prices are likely to have retained their pace in August.
10:00	PL	CPI (y/y)	Aug F	2.8%		2.8%	Flash estimate to be confirmed.
14:00	PL	Current Account Balance (π	Jul;	-179.00		21.00	
14:00	PL	Trade Balance	Jul	-56.00		-77	

Sources: Bloomberg, Reuters

## Capital market forecasts

Government bond yields					
	current	2019Q4	2020Q1	2020Q2	2020Q3
<b>Croatia 10Y</b>	0.53	0.40	0.40	0.40	0.40
spread (bps)	114	80	80	80	80
<b>Czech Rep. 10Y</b>	1.14	1.27	1.41	1.51	1.58
spread (bps)	175	167	181	191	198
<b>Hungary 10Y</b>	2.15	1.90	2.00	2.11	2.25
spread (bps)	276	230	240	251	265
<b>Poland 10Y</b>	2.00	2.10	2.15	2.20	2.20
spread (bps)	261	250	255	260	260
<b>Romania10Y</b>	4.17	4.40	4.50	4.50	4.60
spread (bps)	478	480	490	490	500
<b>Slovakia 10Y</b>	-0.38	-0.25	-0.10	-0.05	0.00
spread (bps)	23	15	30	35	40
<b>Slovenia 10Y</b>	-0.12	0.20	0.20	0.20	0.30
spread (bps)	49	60	60	60	70
<b>Serbia 5Y</b>	2.70	3.00	2.90	2.70	2.70
<b>DE10Y</b>	-0.61	-0.40	-0.40	-0.40	-0.40

FX					
	current	2019Q4	2020Q1	2020Q2	2020Q3
<b>EURHRK</b>	7.40	7.42	7.42	7.38	7.40
forwards		7.40	7.40	7.40	7.40
<b>EURCZK</b>	25.84	25.50	25.34	25.04	24.86
forwards		26.01	26.13	26.27	26.40
<b>EURHUF</b>	330.3	329.0	328.0	328.0	328.0
forwards		331.0	331.5	332.0	332.8
<b>EURPLN</b>	4.34	4.30	4.31	4.30	4.29
forwards		4.37	4.39	4.42	4.44
<b>EURRON</b>	4.73	4.77	4.79	4.82	4.85
forwards		4.78	4.82	4.87	4.91
<b>EURRSD</b>	117.5	118.0	118.0	117.8	117.8
forwards		-	-	-	-
<b>EURUSD</b>	1.10	1.10	1.12	1.15	1.15

3M Money Market Rate						Key Interest Rate					
	current	2019Q4	2020Q1	2020Q2	2020Q3		current	2019Q4	2020Q1	2020Q2	2020Q3
<b>Croatia</b>	0.48	0.50	0.50	0.50	0.50	<b>Croatia</b>	0.30	0.30	0.30	0.30	0.30
<b>Czech Republic</b>	2.14	2.16	2.22	2.36	2.35	<b>Czech Republic</b>	2.00	2.00	2.00	2.25	2.25
<b>Hungary</b>	0.24	0.26	0.28	0.29	0.30	<b>Hungary</b>	0.90	0.90	0.90	0.90	0.90
<b>Poland</b>	1.72	1.72	1.72	1.72	1.72	<b>Poland</b>	1.50	1.50	1.50	1.50	1.50
<b>Romania</b>	3.04	3.00	2.90	2.90	3.20	<b>Romania</b>	2.50	2.50	2.50	2.50	2.50
<b>Serbia</b>	1.99	2.48	2.47	2.48	2.52	<b>Serbia</b>	2.50	2.50	2.50	2.50	2.50
<b>Eurozone</b>	-0.44	-0.50	-0.50	-0.50	-0.50	<b>Eurozone</b>	0.00	0.00	0.00	0.00	0.00

## Macro forecasts

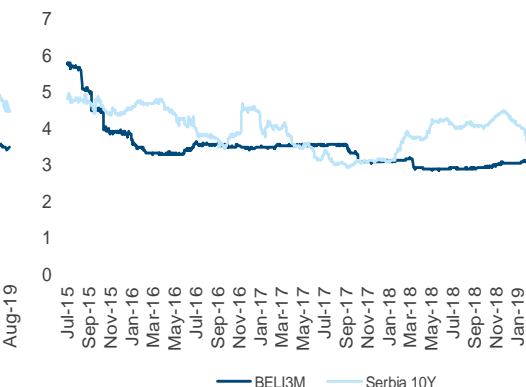
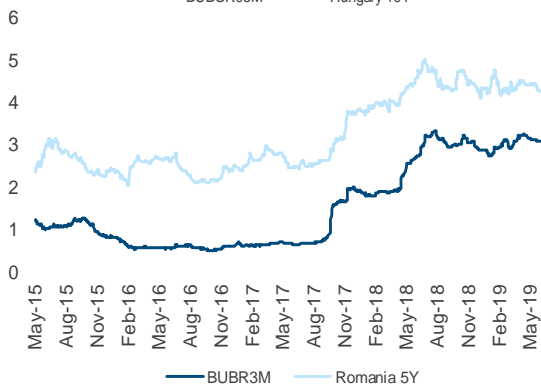
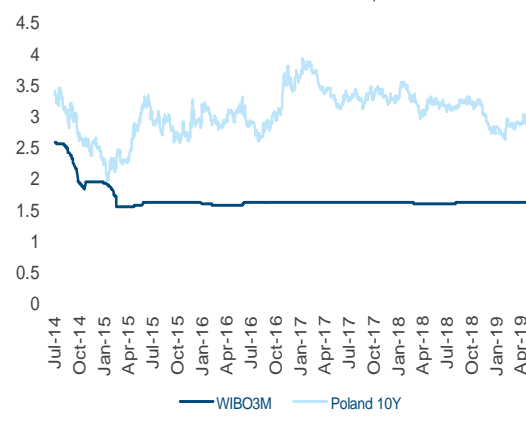
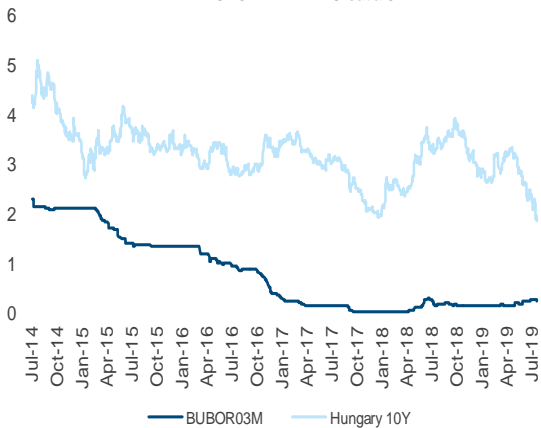
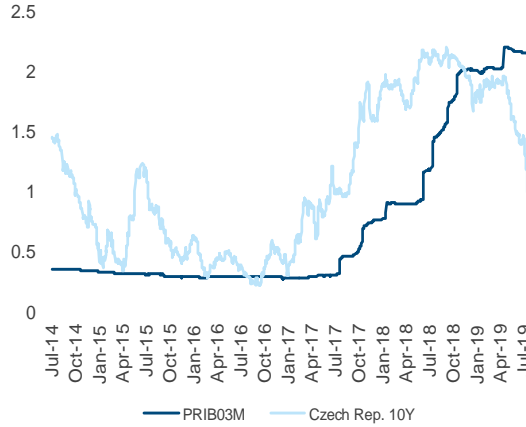
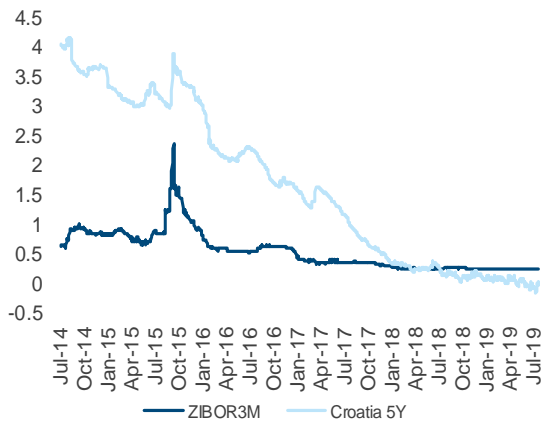
Real GDP growth (%)					Average inflation (%)					Unemployment (%)				
	2017	2018	2019f	2020f		2017	2018	2019f	2020f		2017	2018	2019f	2020f
Croatia	2.9	2.6	3.2	2.5	Croatia	1.1	1.5	1.0	1.3	Croatia	11.3	8.4	7.4	6.4
Czech Republic	4.5	2.9	2.6	2.8	Czech Republic	2.5	2.1	2.6	2.2	Czech Republic	2.9	2.3	3.0	3.3
Hungary	4.1	4.9	4.6	3.3	Hungary	2.4	2.8	3.3	3.3	Hungary	4.2	3.7	3.4	3.4
Poland	4.8	5.1	4.3	3.6	Poland	2.0	1.6	2.4	2.7	Poland	7.3	6.1	6.0	6.4
Romania	7.0	4.1	4.5	3.8	Romania	1.3	4.6	3.9	3.3	Romania	4.9	4.2	3.8	4.0
Serbia	2.0	4.3	3.3	3.5	Serbia	3.2	2.0	2.1	1.8	Serbia	13.5	12.7	10.6	9.8
Slovakia	3.2	4.1	2.5	2.3	Slovakia	1.3	2.5	2.6	2.3	Slovakia	8.1	6.5	5.8	5.9
Slovenia	4.9	4.5	3.2	3.1	Slovenia	1.4	1.7	1.5	1.9	Slovenia	6.6	5.1	4.2	3.7
<b>CEE8 average</b>	<b>4.7</b>	<b>4.4</b>	<b>3.8</b>	<b>3.3</b>	<b>CEE8 average</b>	<b>1.9</b>	<b>2.4</b>	<b>2.7</b>	<b>2.6</b>	<b>CEE8 average</b>	<b>6.3</b>	<b>5.2</b>	<b>5.0</b>	<b>5.2</b>

Public debt (% of GDP)					C/A (%GDP)					Budget Balance (%GDP)				
	2017	2018	2019f	2020f		2017	2018	2019f	2020f		2017	2018	2019f	2020f
Croatia	77.8	74.6	71.2	68.9	Croatia	3.7	2.6	1.4	-0.1	Croatia	0.8	0.2	0.0	-0.5
Czech Republic	34.6	32.7	31.0	30.1	Czech Republic	1.7	0.3	0.4	0.5	Czech Republic	1.6	0.9	0.6	0.3
Hungary	73.4	70.8	68.2	66.4	Hungary	2.8	0.5	-0.1	0.7	Hungary	-2.2	-2.2	-1.8	-1.4
Poland	50.6	48.9	48.0	46.5	Poland	0.2	-0.7	-0.5	-0.7	Poland	-1.5	-0.4	-1.5	-0.8
Romania	35.2	35.0	34.5	36.0	Romania	-3.2	-4.5	-4.8	-5.2	Romania	-2.7	-3.0	-3.0	-4.0
Serbia	59.3	53.6	51.3	49.2	Serbia	-5.2	-5.2	-6.3	-6.0	Serbia	1.1	0.6	-0.5	-0.5
Slovakia	50.9	48.9	48.1	47.0	Slovakia	-2.0	-2.5	-2.3	-1.6	Slovakia	-0.8	-0.7	-0.7	-0.4
Slovenia	74.1	70.1	66.5	63.0	Slovenia	7.2	7.0	6.4	5.7	Slovenia	0.0	0.0	0.70	0.8
<b>CEE8 average</b>	<b>50.3</b>	<b>48.4</b>	<b>46.9</b>	<b>45.8</b>	<b>CEE8 average</b>	<b>0.2</b>	<b>-0.9</b>	<b>-1.0</b>	<b>-1.1</b>	<b>CEE8 average</b>	<b>-1.0</b>	<b>-0.7</b>	<b>-1.2</b>	<b>-1.1</b>

Note: \*Information on past performance is not a reliable indicator for future performance. Forecasts are not a reliable indicator for future performance.

## Appendix



Note: \*Information on past performance is not a reliable indicator for future performance. Forecasts are not a reliable indicator for future performance.

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