

April 16 | 2018

Weekly | 2018 | Week 15

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| CALENDAR

DAY	DATE	TIME (CET)*	MARKET	RELEASE	CONSENSUS**	42FS
Tuesday	17-Apr	10:00	ITA	(Final) Headline HICP, Mar'18	1.1%	N/A
Wednesday	18-Apr	9:00	CZ	PPI, Mar'18, y/y	-0.4%	-0.5%
	18-Apr	9:00	CZ	Export / Import Prices, Feb'18, y/y	N/A	N/A
	18-Apr	11:00	EMU	(Final) Headline HICP, Mar'18	1.4%	N/A
Thursday	19-Apr	10:00	EMU	Current Account, Feb'18, EUR bn.	N/A	N/A
Friday	20-Apr	16:00	EMU	(Flash) Consumer Confidence, Apr'18	-0.1	N/A

* LOCAL TIME IS CET

** (REUTERS/ BLOOMBERG) POLL

| APRIL 2018 AUCTIONS

NAME	DATE OF AUCTION	DATE OF ISSUE	MATURES ON	AMOUNT OFFERED*	COUPON
SPP 788	5-Apr	6-Apr	5-Oct-18	CZK 0-5 bn.	N/A
CZGB 2007-2022**	11-Apr	13-Apr	12-Sep-22	CZK 4 bn. max	4.70%
CZGB 2015-2026**	11-Apr	13-Apr	26-Jun-26	CZK 4 bn. max	1.00%
CZGB 2017-2033**	11-Apr	13-Apr	10-Feb-27	CZK 4 bn. max	0.25%
SPP 789	12-Apr	13-Apr	13-Jul-18	CZK 0-5 bn.	N/A
SPP 786	19-Apr	20-Apr	19-Oct-18	CZK 0-5 bn.	N/A
CZGB 2018-2021**	25-Apr	27-Apr	23-Feb-21	CZK 4 bn. max	0.75%
CZGB 2018-2029**	25-Apr	27-Apr	23-Jul-29	CZK 4 bn. max	2.75%
CZGB 2017-2033**	25-Apr	27-Apr	13-Oct-33	CZK 4 bn. max	2.00%
SPP 791	26-Apr	27-Apr	27-Jul-18	CZK 0-5 bn.	N/A

* FOR T-BILLS, THIS IS MAXIMUM AMOUNT PER PRIMARY DEALER.

** MINFIN CAN CHANGE THE ISSUE AT THE LATEST AT THE DAY OF THE AUCTION ANNOUNCEMENT FOR ONE WITH SIMILAR MATURITY.

| THOUGHT OF THE WEEK

"MUST BE ONE HELL OF A TRUSTFUL UNION ↗."

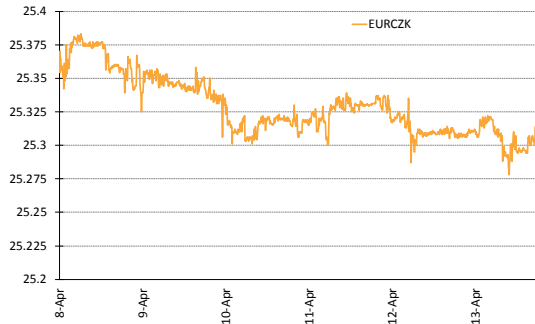
WEEK AHEAD

Nothing of importance in the Czech Republic. One might say politics is going to be the only interesting thing to watch (will ANO form the government with Social Democrats?) but that will certainly have zero impact on markets.

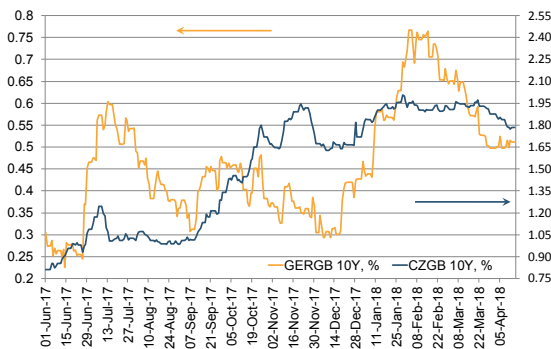
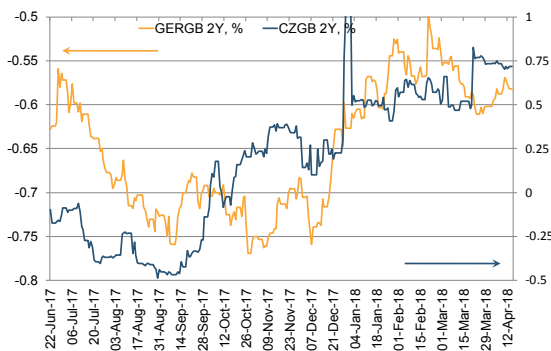
In Eurozone, flash consumer confidence is important. It is the only indicator that hasn't worsened yet – if it does (stability is forecast) it would be final confirmation that growth dynamics is on the downward trajectory.

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EURCZK DRIFTED LOWER LAST WEEK...



TOTAL CALM IN THE BOND MARKETS



WEEK BEHIND

- ▶ Czech inflation fell further in March, but...
- ▶ Current account in stable surplus
- ▶ Fed's increasingly confident in its hawkish stance
- ▶ Eurozone industry very weak in February

| FX

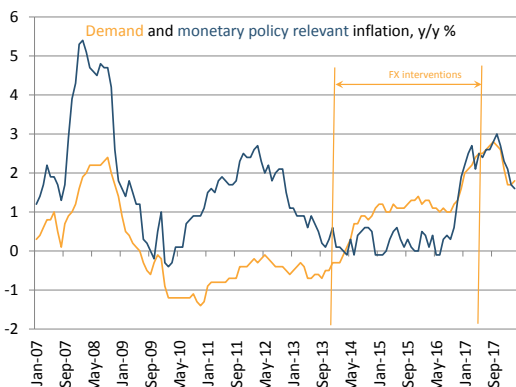
EURCZK drifted lower towards 25.30.

| FI

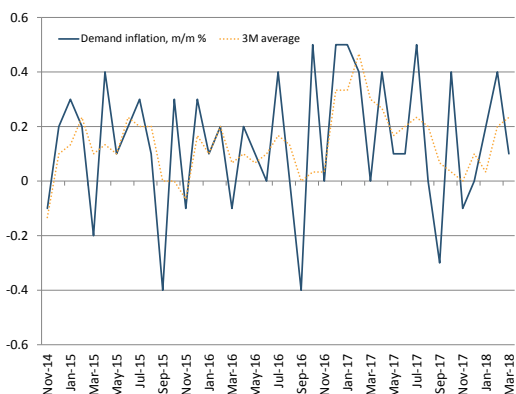
German / Czech yields' movements were tiny last week, just like the week before.

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CZECH MPRI FELL, BUT DEMAND INFLATION...

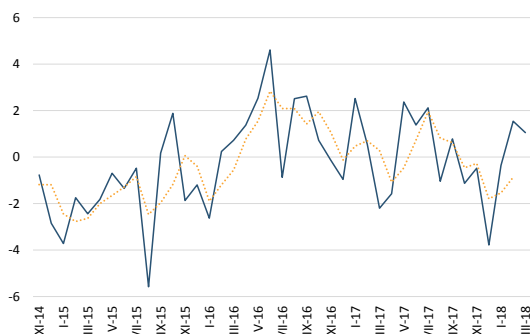


...SHOWS SIGNS OF REBOUNDING.



TOGETHER WITH STABILIZED FOOD PRICES, CZECH MPRI SHOULD SLOWLY RETURN TO 2% THIS YEAR.

World consumer food prices (FAO), m/m a 3-month average, %



CZECH ECONOMY

Czech inflation fell further in March, though monthly data show rebound in demand inflation dynamics.

Czech monetary-policy relevant inflation (MPRI) fell further to 1.6%, lowest since November 2016. This brought the inflation 0.6 pp below the February 2018 forecast of the CNB and thus now presents strong anti-inflationary risk. The deviation from the expectation was primarily ($\approx 2/3$) due to the lower food prices (surprise to me that CNB didn't expect this considering that world food prices have decelerated notably in the past few months) but core inflation was also lower than what CNB expected. More importantly, this was so even though CZK stopped strengthening in the 1Q18.

CNB remains cautiously optimistic, though, claiming that the "overall fundamental inflation pressures remain strong". Although one could wonder why the strong (and, since this is repeated ad nauseam by CNB, clearly persistent) inflation pressures have caused inflation to heavily undershoot CNB forecast, there is some fundament for the optimism. The monthly dynamics of the demand inflation quickened, lifting its annual change from 1.7% in February to 1.8% in March. Stabilization of the world food prices also implies that there shouldn't be further downside here.

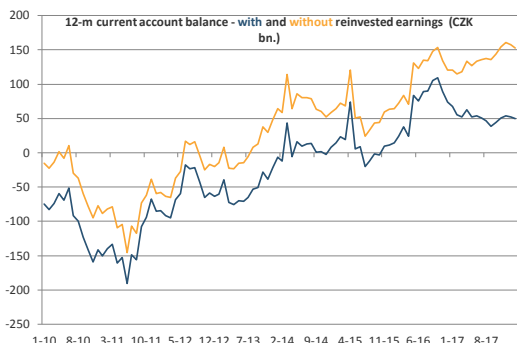
From now on, the inflation will slowly rise back to 2%, but a] it will happen without CZK strengthening (proving CNB wrong in its expectation that ever-strengthening CZK is needed to contain inflation) and b] only slowly. CNB should thus not change the rates this year, if inflation is the only thing it cares about. But if non-inflation concerns prevail ("let us normalize policy while we can"), then it easily might. And will.

Current account still in a surplus (50 bn. in February), showing two things.

First, that although fundamentally CZK would have

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CURRENT ACCOUNT STABLE AROUND CZK 50 BN.



a reason to strengthen, the current account surplus is still dwarfed by the amount of speculative money still in the CZK. In other words, despite the evolution of EURCZK over last 12 months, the missing counterparty problem persists. And I think we're only waiting for the trigger.

Second, the growth of aggregate demand reduced the surplus visibly in 1H17 (12-month surplus halved) but hasn't done anything in the 2H17. The stability of current account surplus since then thus confirms that household demand really slowed in 2H17. And it looks like it didn't quicken in 1Q18 either.

EUROZONE ECONOMY & FED

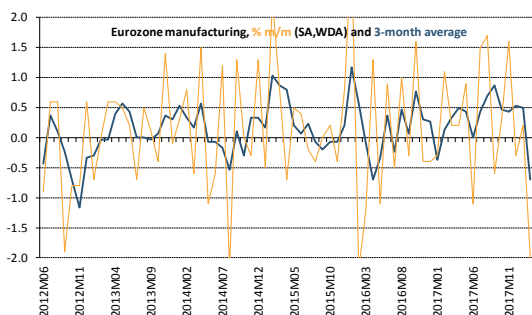
FED's minutes from its March 20-21 meeting showed its increased confidence in growth and inflation outlook.

All FOMC members said that the outlook beyond the 1Q18 improved in recent months, for both growth and inflation, and while there were some who pointed the risks ("prospect of retaliatory trade actions by other countries", "implications of higher planned budget deficits for fiscal sustainability and real interest rates"), FOMC concurred that the outlook for two more hikes is realistic this year. And, in a shift in a more hawkish direction, "number of participants indicated that the stronger outlook for economic activity, along with their increased confidence that inflation would return to 2 percent over the medium term, implied that the appropriate path for the federal funds rate over the next few years would likely be slightly steeper than they had previously expected".

In other words, strongly pro-dollar minutes. And despite the increasing tensions in Syria, dollar fell towards 1.24 against euro. Go figure.

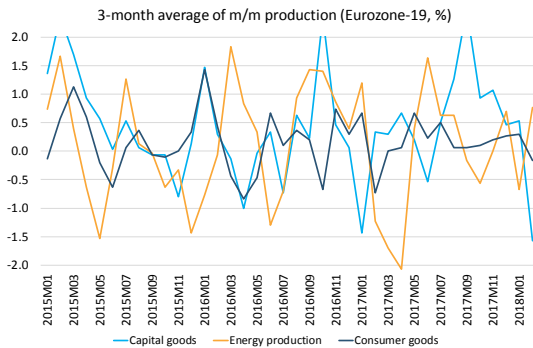
As the German industrial data released the week before suggested, Eurozone industrial production was weak in February and reinforced my view that GDP growth in 1Q18 was slower than 4Q17.

EUROZONE MANUFACTURING FALLS STRONGLY IN FEBRUARY, THE REASON BEING...



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...FALL OF PRODUCTION OF CAPITAL GOODS.



Industrial production fell 0.8% m/m after the contraction of 0.6% in January, almost guaranteeing that its growth in 1Q18 will be slower than in 4Q17. More importantly – and more pessimistically – the decline was due to manufacturing, Manufacturing fell 2% m/m, fastest decline since last February (but that contraction, of 2.2% m/m, came after strong January 2017 growth of 3.1%). After slow growth this last January (+0.2% m/m), manufacturing at best stagnated in 1Q18, a far cry from the expansion of approx. 1.5% in the final quarter of last year. Looking at the structure, the decline was led by decline in the production of capital goods. And, as the difference between industrial production growth and growth of manufacturing suggests, the energy production rebounded (due to weather).

Although I certainly wouldn't worry too much about impending recession (leading indicators are very high by historical standards), **the hard data confirm what the worsening of leading indicators suggested: that the economic growth momentum has peaked.**

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MARKETS ‡

MM / IRS		3M PRIBOR	6M PRIBOR	2Y	5Y	7Y	10Y	
%	Actual	0.709	0.969	1.268	1.635	1.721	1.825	
	-1M	0.709	0.969	1.295	1.690	1.787	1.895	
	-3M	0.709	0.969	1.310	1.610	1.689	1.805	
	-6M	0.709	0.969	1.020	1.350	1.479	1.615	
ASW spread*		2Y	3Y	4Y	5Y	7Y	10Y	
bps.	Actual	-0.534	-0.634	-0.542	-0.415	-0.169	0.013	
	-1M	-0.806	-0.697	-0.747	-0.621	-0.502	0.065	
	-3M	-0.787	-0.802	-0.661	-0.732	-0.523	0.033	
	-6M	-0.842	-0.776	-0.869	-0.832	-0.749	-0.160	
CZGB**		2Y	3Y	4Y	5Y	7Y	10Y	
%	Actual	0.734	0.798	1.008	1.220	1.552	1.838	
	-1M	0.489	0.779	0.859	1.069	1.285	1.960	
	-3M	0.523	0.652	0.888	0.878	1.166	1.838	
	-6M	0.178	0.385	0.394	0.518	0.730	1.455	
FX		EURCZK	EURPLN	EURHUF	EURRON	EURTRY	EURUSD	
	Actual	25.364	4.199	312.09	4.662	4.970	1.228	
	-1M	25.389	4.188	312.83	4.661	4.708	1.240	
	-3M	25.540	4.153	308.44	4.631	4.495	1.203	
	-6M	25.888	4.311	312.20	4.577	4.241	1.173	

‡ As of Sunday night
 * Spreads to generic bonds
 ** Generic bond

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