

July 22 | 2019

Weekly | 2018 | Week 29

| MARTIN LOBOTKA, (+420) 777 027 165, MLobotka@42fs.com, Research@42fs.com

| CALENDAR

| DAY | DATE | TIME (CET)* | MARKET | RELEASE | CONSENSUS** |
|-----------|-----------|-------------|--------|--|----------------|
| Tuesday | 23-Jul-19 | 16:00 | EMU | (Final) Consumer confidence, Jul19 | -7.2 |
| Wednesday | 24-Jul-19 | 9:00 | CZ | Consumer & Business Confidence, Jul19 | N/A |
| | 24-Jul-19 | 10:00 | CZ | Industrial PPI, Oct18, y/y | 3.3% |
| Wednesday | 17-Jul-19 | 11:00 | EMU | (Flash) Manufacturing / Service PMI, Jul18 | 47.6/53.3 |
| Thursday | 25-Jul-19 | 10:00 | GER | Ifo Business Climate, Jul19 | 97.0 |
| | 25-Jul-19 | 13:45 | EMU | ECB Refi/Marginal lending/Deposit Rate | 0%/0.25%/-0.4% |

* LOCAL TIME IS CET

** (REUTERS/ BLOOMBERG) POLL

| JULY 2019 AUCTIONS

| NAME | DATE OF AUCTION | DATE OF ISSUE | MATURES ON | AMOUNT OFFERED* | COUPON |
|--------------------|-----------------|---------------|------------|-----------------|--------|
| CZGB 2015-2027** | 10-Jul-19 | 12-Jul-19 | 10-Feb-27 | CZK 3 bn. max | 0.25% |
| CZGB 2017-2033** | 10-Jul-19 | 12-Jul-19 | 13-Oct-33 | CZK 4 bn. max | 2.00% |
| CZEUGB 2019-2021** | 17-Jul-19 | 19-Jul-19 | 20-Aug-21 | EUR 165 mn. Max | 0.00% |
| CZGB 2017-2033** | 24-Jul-19 | 26-Jul-19 | 13-Oct-33 | CZK 4 bn. max | 2.00% |
| CZGB 2007-2057** | 24-Jul-19 | 26-Jul-19 | 26-Nov-57 | CZK 1 bn. max | 4.85% |

* 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.

*** TO BE DETERMINED ACCORDING TO THE ACTUAL MARKET SITUATION.

| THOUGHT OF THE WEEK

“LAST THREE YEARS IN UK IS WHAT HAPPENS WHEN WHAT WOULDN'T CUT IT AS A TWITTER POLL IS ASKED IN A REFERENDUM”.

WEEK AHEAD

ECB & soft indicators on the events calendar this week.

No.1 event is obviously the meeting of ECB. Last meeting in June was very dovish: ECB put the possibility of renewed asset purchases back on the table, as did the possibility of further lowering of (already negative) deposit rate. The data since alst meeting showed stabilization of the economy at weak growth levels, so while I expect the meeting to be dovish in general, it will be a] less so than the previous one and will b] not bring any changes to the actual policy.

As regards soft indicators, there's German IFO and Czech consumer/ business confidence. More interesting of these are measurements of the business sentiment (IFO, Czech business confidence): after 9% y/y contraction of new orders in German industry in May, I am curious about what did this mean for sentiment in July.

WEEK BEHIND

- Czech producers' prices still on divergent paths ▶
- Czech current account surplus still pro CZK despite worsening in last 1 ½ years ▶
- Eurozone inflation still very low ▶

| FX

EURCZK continued to trade sideways,

...having fallen just 0.05 CZK towards the end of last week.

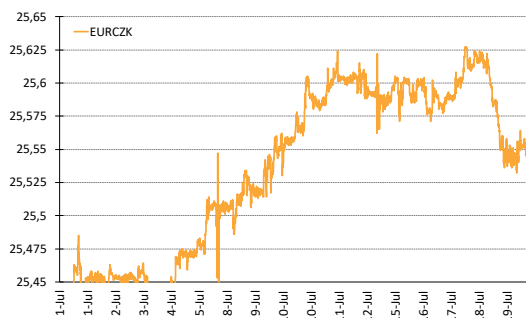
| FI

Last week, German 10Y bonds recouped some losses from the week before.

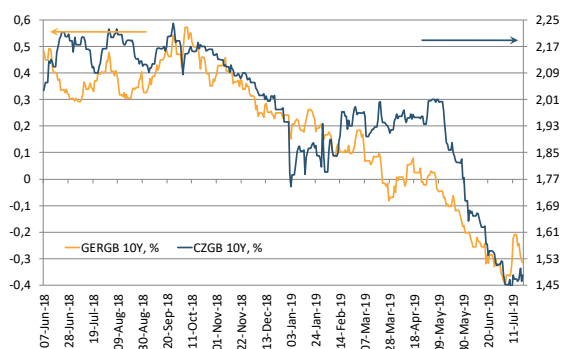
As we wrote last week, the fairly large increase (+20 bps.) we saw two weeks ago was caused by the increase of US Treasury yields, which, in turn, was caused by positive surprise in US CPI inflation (2.1%\$ vs. expectation of 2%). Last week, yields (of not only German but other countries' bonds as well) fell (i.e., prices rose).

I couldn't figure out why: final inflation wasn't different from the preliminary one and news from Bloomberg ↗ that ECB was studying potential change of inflation goal to a symmetrical one about 2% (from current "below, but close to, 2%") should push yields up by making further easing less likely.

CZK TRADED SIDeways LAST WEEK,

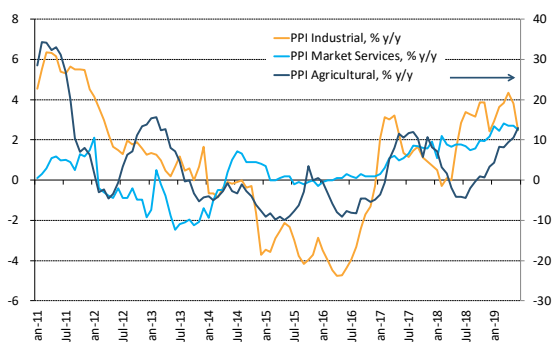


GERMAN YIELDS FELL AMID RUMORS ECB MAY CHANGE INFLATION TARGET

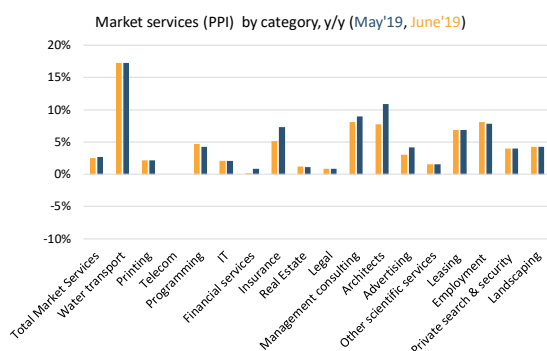


CZECH ECONOMY

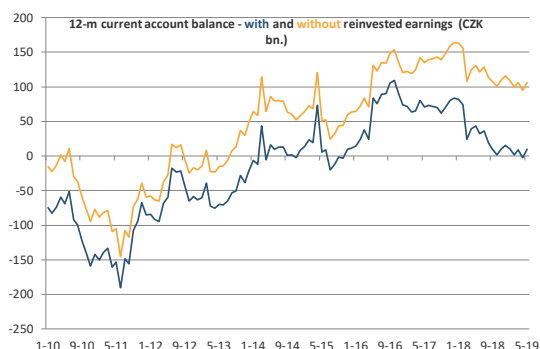
PRODUCER PRICES ON DIVERGENT PATHS.



PRICES OF MARKET SERVICES CONTINUE TO REFLECT TIGHT LABOR MARKET, CONSTRUCTION BOOM



CURRENT ACCOUNT CLEARLY WORSENERD IN LAST 6 QUARTERS, REMAINS PRO-CZK NONETHELESS



Czech producer prices continue to show divergent paths.

Prices of industrial producers rose 2.5% y/y, much weaker than 3.8% y/y seen in May and weakest annual growth rate since December. This was due to the first monthly decline since December, reflecting lower coke and mineral fuel prices.

Prices of agricultural producers, on the contrary, rose at the highest annual rate (12.9%) since February 2013, reflecting continuing rises of crop production (+18%) and of animal products (+8%). This is in line with predictions and evolution of global food prices which grew by almost 7% in the first half of this year. The contribution of food prices to inflation, already responsible for ¼ of the total inflation, will thus probably increase further in the 2H19.

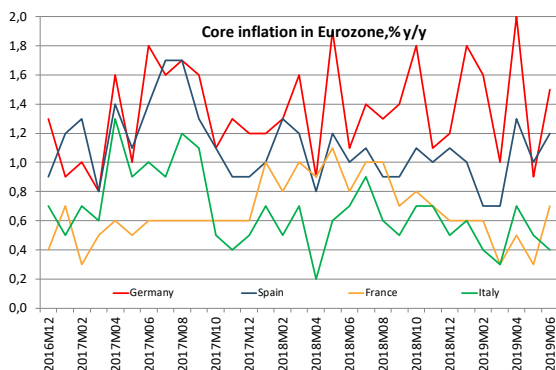
As regards **market services**, the growth of their prices eased to slowest (2.5% y/y) since February. Structure shows strong growth of prices in water transport as well as in architecture, employment and leasing. This reflects boom in construction, tight labor market and willingness on the part of consumers / firms to get into debt amid booming economy.

Annual current account surplus remains stuck to zero,...

...but the one that is most relevant for FX, i.e. current account without reinvested earnings, is firmly in black at around CZK 100 bn. There is clear worsening visible over last 6 quarters, primarily reflecting strong imports (i.e., strong aggregate demand).

That said, current account still points at stronger CZK. The problem is that the degree to which CZK remains overbought is so large that it trumps it.

CORE INFLATION BELOW ECB TARGET IN ALL BIG ECONOMIES



EUROZONE ECONOMY

Final inflation confirmed what we already knew.

That is, that there are no inflationary pressures anywhere in the Eurozone. Despite what Draghi said half a year ago.

Headline inflation was 1.3% in June whereas core inflation was 1.1%, in both cases far away from the ECB's target and no clear path there. Looking at the individual countries, one can see that not even full employment for three years is a guarantee of rising inflation: see Germany.

Looking forward, there is nothing why one should expect the inflationary picture to change – industry remains weak, labor market improves slowly (0.8 pp. per annum in the unemployment rate) and risks are abundant (China / US, Brexit, Italy). While not in favor of a cut, these factors certainly do not support a hike.

July 22 | 2019

MARKETS ‡

| MM / IRS | | 3M PRIBOR | 6M PRIBOR | 2Y | 5Y | 7Y | 10Y | |
|-------------|--------|-----------|-----------|--------|--------|--------|--------|--|
| % | Actual | 2.160 | 2.220 | 1.968 | 1.673 | 1.585 | 1.563 | |
| | -1M | 2.170 | 2.220 | 1.930 | 1.685 | 1.620 | 1.620 | |
| | -3M | 2.020 | 2.070 | 2.120 | 1.965 | 1.893 | 1.893 | |
| | -6M | 2.010 | 2.070 | 2.180 | 1.980 | 1.915 | 1.920 | |
| ASW spread* | | 2Y | 3Y | 4Y | 5Y | 7Y | 10Y | |
| bps. | Actual | -0.430 | -0.421 | -0.274 | -0.224 | -0.088 | -0.073 | |
| | -1M | -0.287 | -0.241 | -0.189 | -0.196 | -0.150 | -0.067 | |
| | -3M | -0.392 | -0.419 | -0.343 | -0.263 | -0.067 | 0.064 | |
| | -6M | -0.405 | -0.382 | -0.270 | -0.224 | -0.127 | -0.044 | |
| CZGB** | | 2Y | 3Y | 4Y | 5Y | 7Y | 10Y | |
| % | Actual | 1.538 | 1.422 | 1.471 | 1.449 | 1.497 | 1.490 | |
| | -1M | 1.643 | 1.564 | 1.551 | 1.489 | 1.470 | 1.553 | |
| | -3M | 1.728 | 1.659 | 1.677 | 1.702 | 1.826 | 1.957 | |
| | -6M | 1.775 | 1.728 | 1.768 | 1.756 | 1.788 | 1.876 | |
| FX | | EURCZK | EURPLN | EURHUF | EURRON | EURTRY | EURUSD | |
| | Actual | 25.531 | 4.250 | 325.02 | 4.727 | 6.349 | 1.122 | |
| | -1M | 25.607 | 4.254 | 324.06 | 4.725 | 6.623 | 1.137 | |
| | -3M | 25.699 | 4.282 | 320.10 | 4.758 | 6.541 | 1.125 | |
| | -6M | 25.582 | 4.286 | 317.53 | 4.711 | 6.055 | 1.137 | |

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

CONTACTS

MARTIN LOBOTKA, ANALYST (+420) 777 027 165, MLobotka@42fs.com

RESEARCH Research@42fs.com

AVAILABLE AT THOMSON REUTERS EIKON MESSENGER

PREVIOUS ISSUES OF WEEKLY AND OTHER REPORTS ARE AVAILABLE [HERE](#) ↗

July 22 | 2019

| DISCLAIMER

This publication has been prepared by 42 Financial Services Czech Republic (hereafter referred to as '42 Financial Services' only). This report is for information purposes only.

Publications in the United Kingdom are available only to investment professionals, not private customers, as defined by the rules of the Financial Services Authority. Individuals who do not have professional experience in matters relating to investments should not rely on it.

The information contained herein has been obtained from public sources believed by 42 Financial Services to be reliable, but which may not have been independently justified. No guarantees, representations or warranties are made as to its accuracy, completeness or suitability for any purpose.

This material is not intended as an offer or solicitation for the purchase or sale of any financial instrument or any other action and will not form the basis or a part of any contract.

Neither 42 Financial Services nor any of its affiliates, its respective directors, officers or employers accepts any liability whatsoever (in negligence or otherwise) for any loss howsoever arising from any use of this document or its contents or otherwise arising in connection therewith. Any opinion, estimate or projection expressed in this publication reflects the current judgment of the author(s) on the date of this report. They do not necessarily reflect the opinions of 42 Financial Services and are subject to change without notice. 42 Financial Services has no obligation to update, modify or amend this report or to otherwise notify a reader thereof in the event that any matter stated herein, or any opinion, projection, forecast or estimate set forth herein, changes or subsequently becomes inaccurate.

The past performance of financial instruments is not indicative of future results. No assurance can be given that any financial instrument or issuer described herein would yield favorable investment results.

42 Financial Services, its affiliates, principals or employees may have a long or short position or may transact in the financial instrument(s) referred to herein or may trade in such financial instruments with other customers on a principal basis. 42 Financial Services may act as a market maker in the financial instruments or companies discussed herein and may also perform or seek to perform investment banking services for those companies. 42 Financial Services may act upon or use the information or conclusion contained in this report before it is distributed to other persons.

This report is subject to the copyright of 42 Financial Services. No part of this publication may be copied or redistributed to persons or firms other than the authorized recipient without the prior written consent of 42 Financial Services.

By accepting this report, a recipient hereof agrees to be bound by the foregoing limitations.

Copyright: 42 Financial Services Czech Republic, 2019.

All rights reserved.