

August 27 | 2018

Weekly | 2018 | Week 34

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CALENDAR

DAY	DATE	TIME (CET)*	MARKET	RELEASE	CONSENSUS**	42FS
Monday	27-Aug-18	10:00	GER	IFO Business Climate, Aug'18	101.8	N/A
Wednesday	29-Aug-18	8:45	FRA	(2nd estimate) GDP, 2Q18, q/q	0.2%	N/A
Thursday	30-Aug-18	9:00	SPA	(Preliminary) HICP, Aug'18, y/y	2.3%	N/A
	30-Aug-18	11:00	EMU	(Final) Consumer confidence, Aug'18	-1.9	N/A
	30-Aug-18	14:00	GER	(Preliminary) HICP, Aug'18, y/y	2.1%	N/A
Friday	31-Aug-18	8:45	FRA	(Preliminary) HICP, Aug'18, y/y	2.5%	N/A
	31-Aug-18	9:00	CZ	(2nd estimate) GDP, 2Q18, q/q	0.5%	N/A
	31-Aug-18	9:00	SPA	Retail sales, Jul'18, m/m	N/A	N/A
	31-Aug-18	11:00	EMU	Unemployment rate, Jul'18,	8.2%	N/A
	31-Aug-18	11:00	EMU	(Preliminary) Core /Headline HICP, Aug'18, y/y	2.1% / 1.1%	N/A
	31-Aug-18	11:00	ITA	(Preliminary) HICP, Aug'18, y/y	1.7%	N/A
	31-Aug-18	12:00	ITA	(2nd estimate) GDP, 2Q18, q/q	0.2%	N/A

* LOCAL TIME IS CET

** (REUTERS/ BLOOMBERG) POLL

AUGUST 2018 AUCTIONS

NAME	DATE OF AUCTION	DATE OF ISSUE	MATURES ON	AMOUNT OFFERED*	COUPON
CZGB 2011-2023**	8-Aug	10-Aug	18-Apr-23	CZK 4 bn. max	VAR
CZGB 2014-2025**	8-Aug	10-Aug	17-Sep-25	CZK 4 bn. max	2.40%
SPP 799	9-Aug	10-Aug	9-Nov-18	CZK 0-5 bn.	N/A
CZGB 2014-2027**	22-Aug	24-Aug	19-Nov-27	CZK 4 bn. max	VAR
CZGB 2018-2029**	22-Aug	24-Aug	23-Jul-29	CZK 4 bn. max	2.75%

* 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

"MAGA=MY ATTORNEY GOT ARRESTED".

WEEK AHEAD

2nd estimate of Czech 2Q18 GDP growth will reveal the structure of the growth.

According to the terse statement accompanying the release of the first estimate two weeks back, everything contributed to the growth. If so, nothing must have contributed much...Of analytical interest is the growth of household demand. I think it will be shown to have been much slower than in previous 6 quarters when it averaged almost 1% q/q (for reasons, read here [↗](#)).

In Eurozone, most important is the **preliminary inflation for August**, though the core and headline are forecast to have remained unchanged on July. Meaning, especially in case of core inflation, stubbornly low. Structure of **Italian 2Q18 GDP** will hardly shock anybody, the expansion having been moribund for years now. Finally, **August German IFO** will probably confirm that industry is not in for a better 2H18 than how it performed in the 1H18.

WEEK BEHIND

CZ: consumer confidence still high, but lowest this year ▶

GER: 2Q18 GDP surprise due to inventories ▶

EMU: PMI hints at 0.3-0.4% quarterly growth ▶

| FX

CZK remained in a tight range of 25.700-25.750 throughout last week.

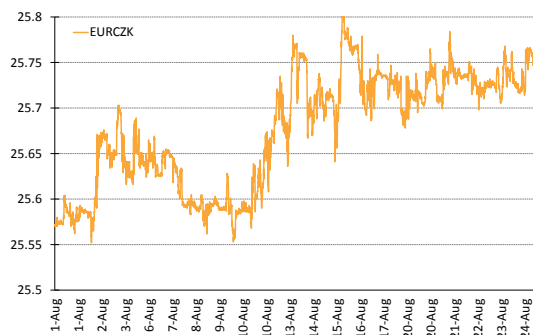
There was nothing to move it anywhere.

| FI

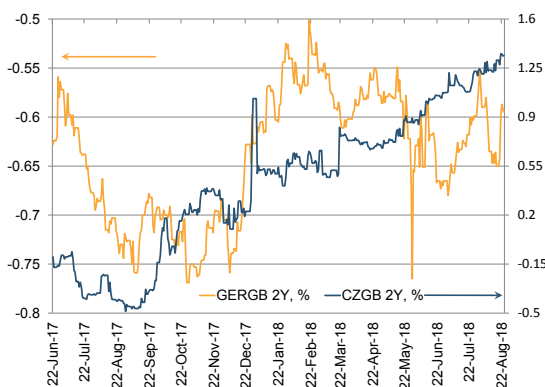
Not much happening in the bond markets either.

Short end of the CZGB curve continued to drift higher as weak CZK makes another hike this year guaranteed, while long end fell few bps to 2.13%.

EURCZK ALMOST MOTIONLESS BETWEEN 25.7-25.75

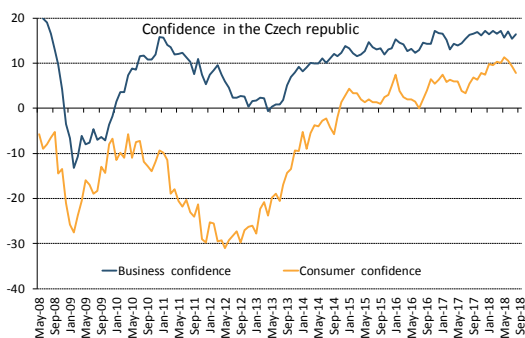


SHORT END CONTINUES TO DRIFT HIGHER AS WEAK CZK MAKES HIKE LIKELY



CZECH ECONOMY

CONSUMERS AT THEIR MOST PESSIMISTIC THIS YEAR, THOUGH STILL VERY OPTIMISTIC HISTORICALLY

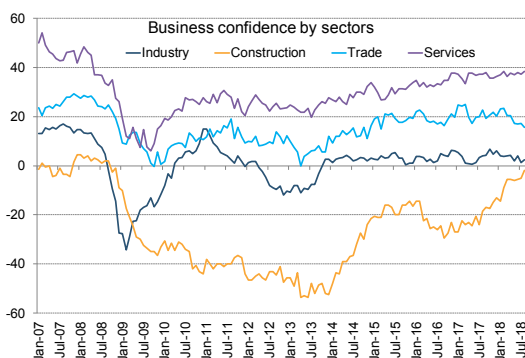


Consumer confidence worsened to lowest this year – but still remains high historically.

Having registered all-time high in June (10.6 pts.), consumer confidence fell to 7.8 pts. in August, the lowest recorded level since December 2017 (7.5 pts.).

The decline was, according to the Czech Statistical Office, due to the fact that the consumers became more worried about the worsening of the situation in next twelve months. And, a bit paradoxically, they also became more worried about higher prices down the road. In other words, they are afraid of economic slowdown causing the slide in CZK. Not entirely irrational expectation, if you ask me, with expansion now too long and with billions of euros worth of speculative money still here.

CONFIDENCE IN CONSTRUCTION HIGHEST SINCE CRISIS

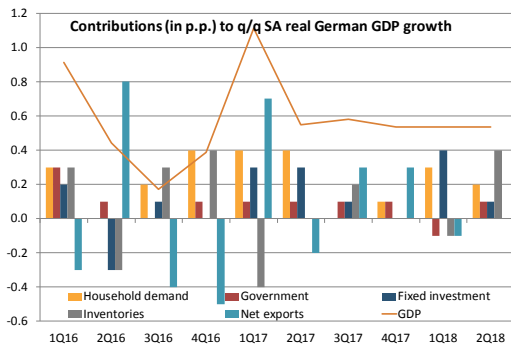


The evolution of the consumer confidence thus confirms my view that household demand has already seen its best in this cycle. And that demand will grow more slowly in the next 4 quarters than in previous four quarters.

As regards businesses, companies remained as optimistic on average in August as they were in July. Under the surface, though, there are some interesting movements. **Confidence** in services remained unchanged whereas the one **in trade** fell further, having reached **the lowest (15.6 pts.) since March 2015**. This is clearly the reflection of trade war fears. On the other hand, **confidence in construction sector rose to highest since November 2008**, reflection of booming real estate sector and pick-up in government investments (the latter to be seen this Friday when GDP structure is released)

EUROZONE ECONOMY

GERMAN 2Q18 GDP GROWTH SURPRISE DUE TO INVENTORIES' BUILD-UP



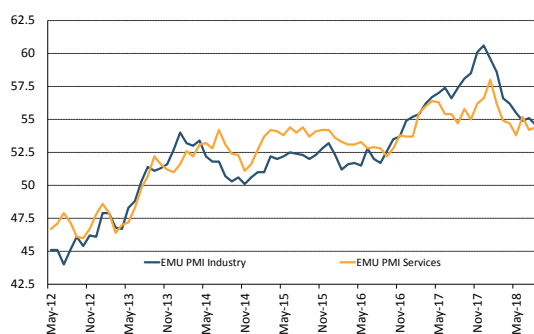
German 2Q18 GDP growth may have surprised on the upside, but it was very likely just one-off.

German Statistical Office released the structural data for 2Q18 GDP growth last week. While reaffirming the 0.5% q/q growth from the preliminary estimate, the structure, hitherto unknown, made it clear that the growth of this magnitude is unlikely to be repeated in 2H18, and that the growth in 3Q18 will very likely be weaker than what, say, PMI calls for. Other components of the demand contributed moderately: households added 0.2 pp, fixed investments 0.1 pp. In other words, there was nothing inflationary in the data.

Last week, recall, I thought government demand was behind slightly faster-than-forecast growth. It wasn't. The truth is that the upside surprise was due to inventories, contribution of which to the quarterly growth was highest (0.4 pp) since the last quarter of 2016.

Which, it is clear, is hardly sustainable: build-up of inventories in 2Q18 looks like result of production going on while demand slowed, likely global one and on escalation of the trade war. And, as such, it will be reversed in 2H18, likely already in 3Q18. Hence my expectation that 3Q18 growth will be slower than in 1H18 and what leading indicators suggest, i.e. 0.3% q/q.

PMI STABILIZED AT LEVELS CONSISTENT WITH 0.3-0.4% Q/Q GROWTH



Eurozone PMI stabilized in 3Q18, suggesting 0.3-0.4% q/q expansion of the output.

Services PMI rose to a two-month high in August, but 54.4 pts. seen in August was just 0.2 pts. higher than in July.

Manufacturing, on the other hand, saw another worsening (to a 21-month low of 54.6), though 54.6 was just half a point lower than in July, i.e. nothing ground-shaking either.

Put together, given the much higher weight of services in the overall index, the composite PMI

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edged higher to 54.3, 0.1 pts higher than in July. These are levels consistent with about 0.4% quarterly expansion growth in the third quarter.

The most important takeaway is that weak performance of the industry will continue: new exports rose at the weakest in 2 years, hiring was weakest in 17 months, backlogs were weakest in three years. With trade war US President embarked on showing no signs of de-escalation, industry is hardly going to do better in the 2nd half of the year than how it fared in the first one.

In sum: as long as services don't follow suit, the overall growth may keep its current dynamics, though will not accelerate. But, the risks are clearly to the downside, the trade war, Brexit or just the plain fact that this expansion is now very mature being the main reasons. Growth deceleration to 1% in next 4 quarters is what I expect.

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MARKETS ‡

MM / IRS		3M PRIBOR	6M PRIBOR	2Y	5Y	7Y	10Y	
%	Actual	1.480	1.580	2.025	2.215	2.243	2.275	
	-1M	1.190	1.280	1.845	2.085	2.084	2.120	
	-3M	0.900	0.990	1.400	1.790	1.876	1.955	
	-6M	0.910	0.990	1.290	1.675	1.785	1.910	
ASW spread*		2Y	3Y	4Y	5Y	7Y	10Y	
bps.	Actual	-0.687	-0.784	-0.668	-0.503	-0.244	-0.142	
	-1M	-0.727	-0.805	-0.684	-0.550	-0.218	-0.009	
	-3M	-0.536	-0.614	-0.498	-0.371	-0.182	0.026	
	-6M	-0.719	-0.715	-0.646	-0.632	-0.541	-0.015	
CZGB**		2Y	3Y	4Y	5Y	7Y	10Y	
%	Actual	1.338	1.338	1.508	1.712	1.999	2.133	
	-1M	1.118	1.165	1.364	1.535	1.866	2.111	
	-3M	0.864	0.975	1.210	1.419	1.694	1.981	
	-6M	0.571	0.746	0.923	1.043	1.244	1.895	
FX		EURCZK	EURPLN	EURHUF	EURRON	EURTRY	EURUSD	
	Actual	25.753	4.278	323.72	4.635	6.997	1.163	
	-1M	25.696	4.303	326.18	4.630	5.712	1.169	
	-3M	25.783	4.310	319.26	4.629	5.524	1.172	
	-6M	25.364	4.173	313.14	4.653	4.659	1.230	

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

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