Weekly | 2018 | Week 45

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| CALENDAR

DAY	DATE	TIME (CET)*	MARKET	RELEASE	CONSENSUS**	42FS
Tuesday	13-Nov-18	8:00	GER	(Final) HICP, Oct'18, y/y	2.4%	N/A
	13-Nov-18	10:00	CZ	Current account, Sep'18, CZK bn.	-1.4	N/A
Wednesday	14-Nov-18	8:00	GER	(1st est.) GDP 3Q18, q/q (SA)	-0.1%	N/A
	14-Nov-18	9:00	CZ	(1st est.) GDP 3Q18, q/q (SA)	0.6%	0.4%
	14-Nov-18	11:00	EMU	Industrial production, Sep'18, y/y (WDA)	0.3%	N/A
	14-Nov-18	11:00	EMU	(2nd est.) GDP 3Q18, q/q (SA)	0.2%	N/A
Thursday	15-Nov-18	11:00	EMU	Trade Balance, Aug'18, EUR bn. (SA)	16.30	N/A
Friday	16-Nov-18	9:00	CZ	Import Prices, Sep'18, y/y	N/A	N/A
	16-Nov-18	9:00	CZ	Industrial PPI, Oct'18, y/y	3.4%	3.4%
	16-Nov-18	11:00	EMU	(Final) HICP, Sep'18, y/y	2.2%	N/A

* LOCAL TIME IS CET
** (REUTERS/ BLOOMBERG) POLL

| NOVEMBER 2018 AUCTIONS

NAME	DATE OF AUCTION	DATE OF ISSUE	MATURES ON	AMOUNT OFFERED*	COUPON
CZGB 2018-2029**	21-Nov-18	23-Nov-18	23-Jul-29	CZK 3 bn. max	2.75%
CZGB 2017-2033**	21-Nov-18	23-Nov-18	13-Oct-33	CZK 2 bn. max	2.00%

* 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

"GOLDMAN INVOLVED IN 1MDB??? REALLY??? ↗ REMINDS ME OF THIS ↗ "

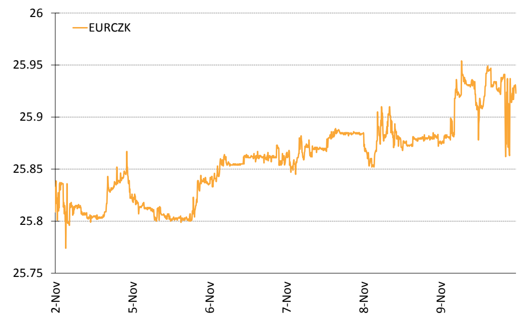
WEEK AHEAD

GDP data in the forefront, both here and in Germany.

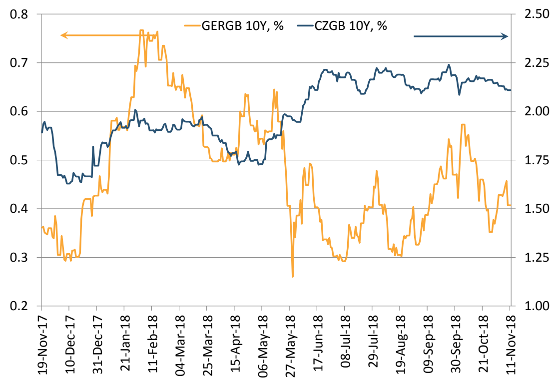
Czech GDP is expected to have grown 0.6% q/q in 3Q18. I am bit more pessimistic than that, especially in light of weak industry and retail sales' growth in 3Q18. I also think fixed investments did poorly in 3Q18 as uncertainty set in. **Import prices for September** shouldn't show much of a currency-related effects, the average EURCZK rate in September having been the same as in August.

In **Eurozone**, German 3Q18 GDP data are No.1 release. The forecast is for outright decline of 0.1% q/q, which, I feel, wouldn't be surprising considering the quarterly decline in industry ▶ and in retail sales ↗.

EURCZK CONTINUES TO MOVE HIGHER DESPITE CNB STANCE



BOND MARKETS CALM



WEEK BEHIND

CZ: industry confirms German flu is here ▶

Czech retail weakest in 5 years as car sales plummet ▶

Czech inflation still predominantly due to housing ▶

GER: industry soft, but stabilized ▶

EMU: retail sales very weak ▶

| FX

EURCZK continued to move higher.

Not large moves, by any measure, but steady drift upward it is. Despite the CNB's expectation that interest rate differential will push it lower…

| FI

Nothing eventful in the bond markets, here or in Germany.

10Y Bunds remained close to 40 bps., 10Y Czech govies around 2.1%.

| CZECH ECONOMY

Czech industry slowed down further in September, confirming it is being impacted by the German softness.

Not that it was not to be expected: in September, Czech manufacturing PMI fell to lowest (53.9) since December 2016, so it was just a matter of time before it shows up in the actual numbers. The m/m growth of 1.1% looks nice, but it still wasn't enough for the industry to see positive quarterly growth in 3Q18 as against 2Q18. In other words, industry was likely a drag on 3Q18 q/q GDP growth.

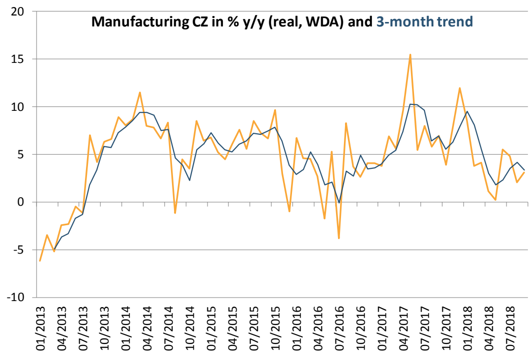
The annual growth of 2.5% was weaker than what PMI suggested, but this seems partially driven by one-offs. See, there was a temporary interruption at chemical plants resulting in 15% y/y decline in production of chemicals, and there is also 15% y/y decline in car production. This latter decline is almost certainly due to production of some models having been halted pending the issuance of new homologations under new emission tests (World harmonized Light vehicle Test Procedure, or WLTP) introduced by EU in the wake of dieselgate. So, both of these factors are reversible.

Against this relatively optimistic view of the future goes the continuing weakness of soft indicators, especially PMI: manufacturing PMI worsened further in October, reaching lowest level (52.5), since November 2016. It is thus weaker than what it was at the end of 3rd quarter of this year and does not bode well for 4Q18 growth.

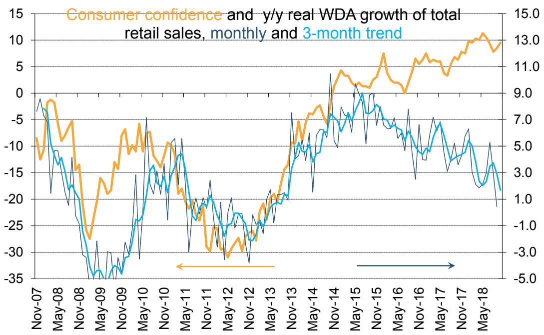
Czech retail sales show weakness due to dieselgate as well, but there'd be slowdown even without this.

Adjusted for seasonal effects and for working days, total retail sales, incl. cars, grew just 0.4% y/y, the **weakest growth since mid-2013**. Even without this, though, the slowdown as against last year is evident, if not as pronounced: core retail sales, i.e. sales without food, fuel and cars, grew only 5.4%

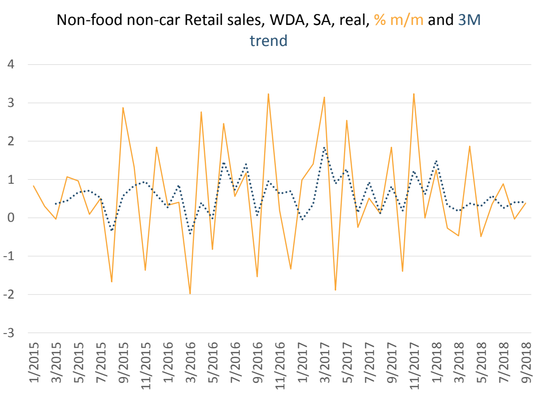
CZECH INDUSTRY WEAKENING AS GERMAN ONE IS.



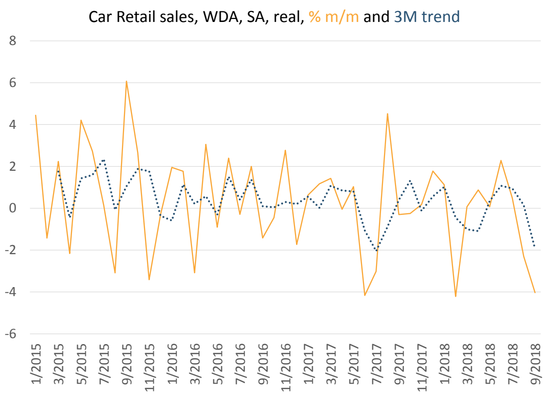
RETAIL SALES IN WEAKEST GROWTH SINCE MID-2013



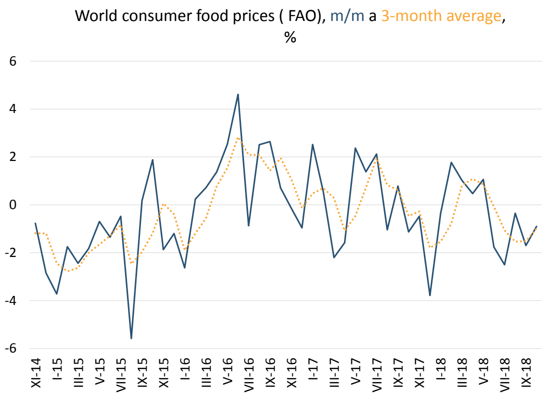
...DUE TO SLOWDOWN IN CORE SALES, BUT, MAINLY, DUE TO...



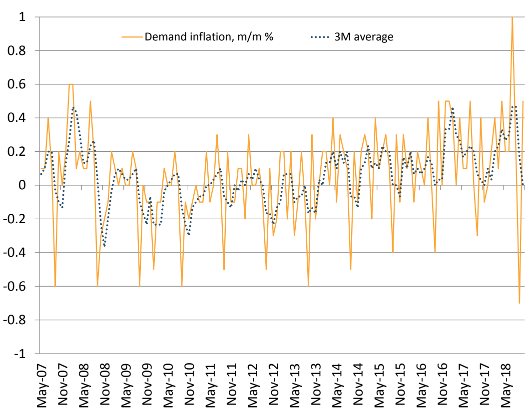
…Fall in Car sales.



Czech inflation slows in October as (global) food prices decelerate



Demand inflation didn't change in August-October.



y/y, one of the weakest growth rate seen in last two years, and well below 9% annual growth seen this time last year.
That retail lost momentum is seen in monthly numbers as well: whereas in 2017 the rolling quarterly growth was 2.5-3.5%, this year's one is 1%. In other words, we shall soon see annual growth of core retail sales slowing to 4% y/y (unless, of course, monthly dynamics picks up).

The difference in September between growth of the core sales and growth of the total sales was due to car sales which plunged 4.1% y/y (-4% m/m) in September (WDA, SA, real). This was primarily due to numerous models of cars not being offered for sale pending the issuance of new EU emissions certificates.

Czech inflation is still primarily due to housing. Without the growth in that segment, inflation would be well below the 2% CNB target.

The monetary-policy relevant inflation (MPRI) slowed to 2.1% y/y in October (vs. 2.2% in September), mainly due to slower growth of food prices. More important than this (due to very dry summer likely just) transitory effect (and one that reflects global food price deceleration over last few months) is the fact that **accommodation still accounts for over 40% of the inflation**. In other words, were the prices in this segment (which primarily include rents, gas and electricity prices) stable y/y, we'd be looking at MPRI of 1.2%. Or, put differently, what CNB has been this year reacting to via increases of the repo rate is nothing else but real estate prices and oil prices. Whether that is how monetary policy should be conducted, more so when signs are becoming clearer and more numerous that economic growth is cooling, is left for the reader to assess.

The **demand inflation re-accelerated to 2.3% y/y** (September: 2.1%), the monthly rebound of 0.5% m/m coming after deep drop (-0.7% m/m) in September. The growth of demand inflation in last three months, a much more stable indicator, was zero...

| EUROZONE ECONOMY

Retail sales' growth was almost non-existent in September, further undermining the "inflation is on its way to target" narrative of ECB.

Retail sales growth was mere 0.8% y/y (adjusted for different number of working days and real) in September, meaning the Eurozone retail sales contracted (-0.3%) in 3Q18 as against 2Q18. The weakness was especially pronounced in Germany and Spain where retail sales fell about 1% in 3Q18, and Italy was weak as well (-0.3% q/q). Retail sales only grew in France (+1% q/q), hardly enough for the whole of Eurozone to remain in black.

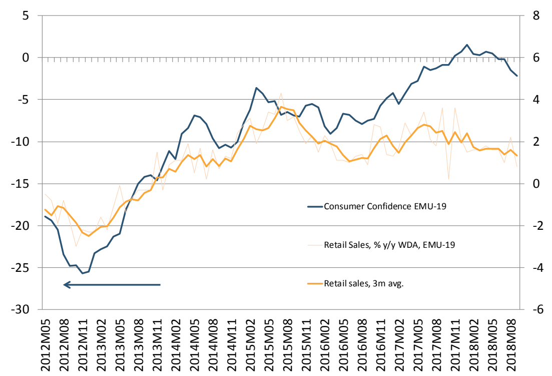
So, as written last week, this might be the time for ECB to reconsider the end of QE, if you ask me. Not that I think it will.

German industry remains in a soft spot, but data suggest situation has already stabilized.

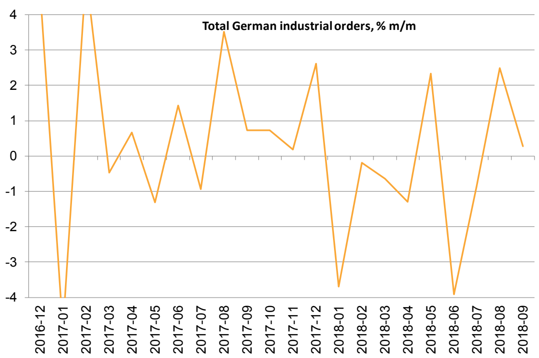
Industry posted a second monthly gain in September: after upwardly revised August's growth of 0.1% (from previous reported -0.3%), September saw gain of 0.2% m/m. Weak, but positive growth. There was first growth (0.9% m/m) after three months in capital goods production but otherwise nothing spectacular in the structural data. Industry was thus down about 1% q/q in 3Q18.

New orders, however, seem to imply that, if production doesn't get any better, it will not get worse. New orders rose 0.3% m/m in September, after 2.5% revised increase in August. So, although the orders are still almost 1 % lower than what they were one year ago, they are up almost 3% since the end of July. Whether this is normal volatility (which orders data do display) or beginning of the recovery remains to be seen. While worsening of

EUROZONE RETAIL SALES CONTINUED TO WEAKEN AT THE END OF 3Q

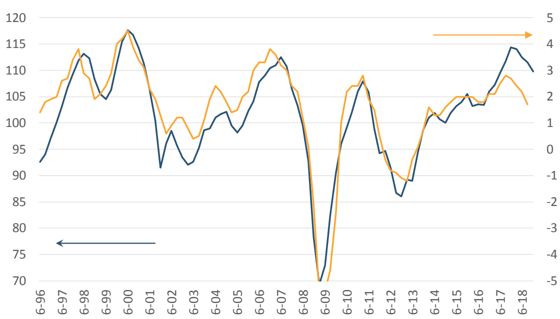


GERMAN ORDERS UP FOR THE 2ND MONTH



EUROPEAN SENTIMENT INDICATOR QUALITATIVELY IN LINE WITH WEAKER GDP

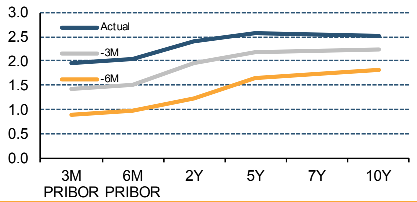
Eurozone confidence (ESI) vs. GDP (% y/y)



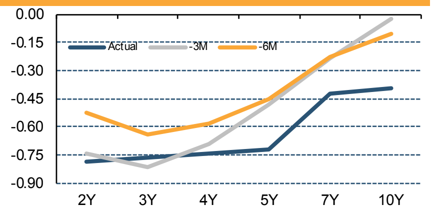
the PMI in October or continuing deterioration of EC European Sentiment Indicators (ESI) might lead one to believe the weakness is not over yet, relative stability of IFO says it may be. We shall see in the following months, but whatever the situation turns out to be, it is unlikely that inflation will start converging to ECB target soon.

| Markets ‡

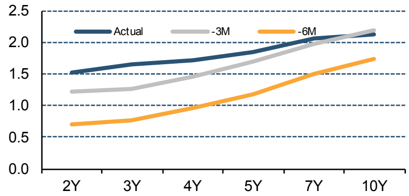
MM / IRS		3M PRIBOR	6M PRIBOR	2Y	5Y	7Y	10Y
%	Actual	1.960	2.030	2.393	2.565	2.542	2.525
	-1M	1.730	1.800	2.275	2.505	2.518	2.530
	-3M	1.420	1.510	1.955	2.180	2.203	2.225
	-6M	0.900	0.990	1.240	1.635	1.725	1.830



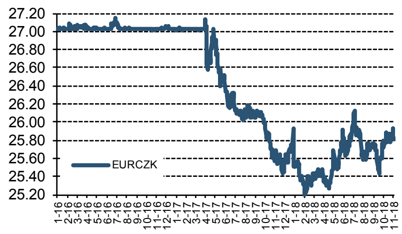
ASW spread*		2Y	3Y	4Y	5Y	7Y	10Y
bps.	Actual	-0.790	-0.763	-0.744	-0.725	-0.425	-0.394
	-1M	-0.781	-0.860	-0.816	-0.751	-0.531	-0.445
	-3M	-0.747	-0.815	-0.695	-0.482	-0.236	-0.027
	-6M	-0.529	-0.644	-0.584	-0.452	-0.227	-0.104



CZGB**		2Y	3Y	4Y	5Y	7Y	10Y
%	Actual	1.513	1.658	1.718	1.840	2.051	2.131
	-1M	1.494	1.549	1.656	1.754	1.987	2.085
	-3M	1.208	1.258	1.446	1.698	1.967	2.198
	-6M	0.711	0.773	0.960	1.183	1.498	1.726



FX		EURCZK	EURPLN	EURHUF	EURRON	EURTRY	EURUSD
	Actual	25.808	4.309	321.70	4.659	6.187	1.139
	-1M	25.723	4.302	322.91	4.667	6.945	1.148
	-3M	25.615	4.262	320.21	4.618	5.882	1.157
	-6M	25.501	4.266	313.92	4.666	5.055	1.199



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

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