

November 26 | 2018

Weekly | 2018 | Week 47

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CALENDAR

DAY	DATE	TIME (CET)*	MARKET	RELEASE	CONSENSUS*	42FS
Monday	26-Nov-18	9:00	CZ	Business/Consumer Confidence, Nov18	N/A	N/A
	26-Nov-18	10:00	GER	IFO Business Climate, Nov18	102.3	N/A
Thursday	29-Nov-18	8:45	FRA	(2nd est.) GDP 3Q18, q/q (SA)	0.4%	N/A
	29-Nov-18	9:00	SPA	Retail sales, Oct'18, y/y	N/A	N/A
	29-Nov-18	9:00	SPA	(Preliminary) HICP, Nov18, y/y	2.0%	N/A
	29-Nov-18	11:00	EMU	(Final) Consumer confidence, Nov18,	-3.9	N/A
	29-Nov-18	14:00	GER	(Preliminary) HICP, Nov18, y/y	2.3%	N/A
Friday	30-Nov-18	8:00	GER	Retail sales, Oct'18, y/y	1.6%	N/A
	30-Nov-18	8:45	FRA	(Preliminary) HICP, Nov18, y/y	2.3%	N/A
	30-Nov-18	9:00	CZ	(2nd est.) GDP 3Q18, q/q (SA)	0.4%	0.3%
	30-Nov-18	11:00	EMU	(Preliminary) HICP, Nov18, y/y	2.0%	N/A
	30-Nov-18	11:00	ITA	(Preliminary) HICP, Nov18, y/y	1.60%	N/A
	30-Nov-18	12:00	ITA	(2nd est.) GDP 3Q18, q/q (SA)	0.0%	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

“EACH WEEK, I CONTINUE TO BE AMAZED WHAT'D NEVER OCCURRED TO ME WOULD BE A PROBLEM AFTER BREXIT: GIBRALTAR, REALLY?”

WEEK AHEAD

Lots of data releases, especially in the 2nd half of this week.

Here, the structure of the 3Q18 GDP growth will be released. In view of German structure released last week (see below), it is likely that the slowdown vs. previous quarters was due do net exports (manufacturing).

In Eurozone, there will be updates to GDP data for France and Italy, but there will not be any significant divergences from the first estimates. In Italy, structure will be released but it is hardly something that'd make the stagnation from the 3rd quarter more palatable.

More importantly, there will be **preliminary November inflation data for Eurozone**. With core likely to have stayed around 1% and growth momentum weakening further, the case for ECB's prolonging the QE is getting stronger. But, I think, not sufficiently so to make ECB change the course.

WEEK BEHIND

German 3Q18 GDP growth dragged down by exports ▶

Eurozone PMI continued to worsen mid-way through 4Q18 ▶

| FX

EURCZK moved slightly lower.

0.1 CZK, to be exact. Although this technically is strengthening of CZK, the EURCZK is still far, far away from what CNB forecast, as recently as half a year ago, it would be this time of the year.

| FI

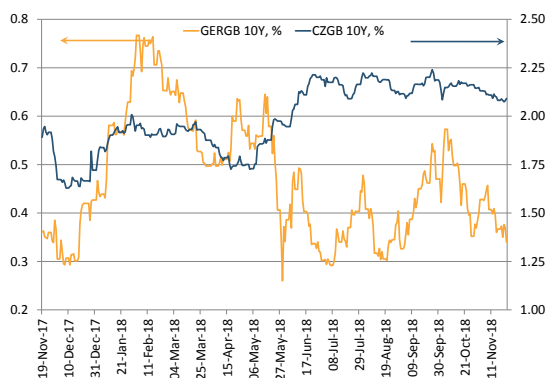
German yields continued to drift lower.

10Y German Bunds slid to below 35 bps., lowest level since early September, and did so amid worries that weak German growth data might force ECB to reverse its early summer decision to discontinue QE this December.

EURCZK FALLS TO 25.90



BOND YIELDS CONTINUE TO MOVE LOWER



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| CZECH ECONOMY

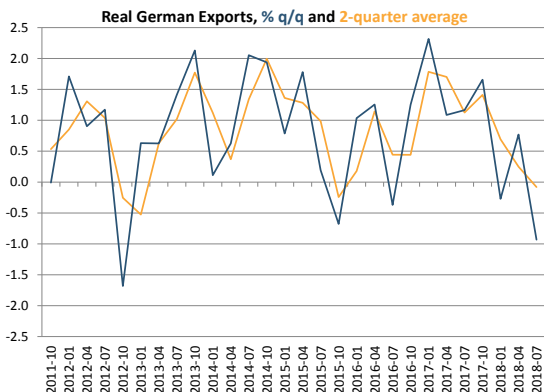
2 new people were officially appointed to CNB Board by President Zeman.

I already covered what these guys are likely to stand for elsewhere ↗ so I won't repeat myself here.

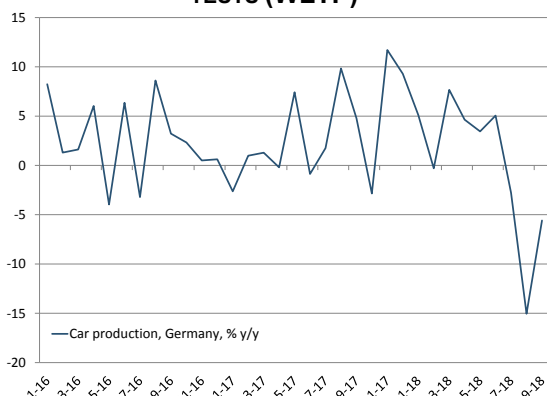
In other developments, although CNB recommended that banks tighten screws on mortgages, not much seems to have happened ↗ in October: despite mortgages having become pricier, the total volume of mortgages rose to CZK 24.28 bn., i.e. highest since November 2016. Furthermore, CNB does not seem to be much closer to new regulatory powers it wants ↗ that would permit it to *order* banks, as opposed to *recommend* to them, to lend less (currently, CNB only has "recommendations" in its toolkit that banks can choose to ignore, though they usually don't).

Recall that in June CNB recommended to banks ↗↗ to lend only to those meeting Debt-to-Income and Debt-Service-to-Income limits. If banks choose to ignore these (October might suggest that, but it also reflects deals that began in September and were only consummated in October, so one cannot be sure), house prices can go higher still. And thus the housing component of consumer inflation – the primary driver of inflation, currently contributing 0.9 pp to 2.1% overall inflation – will not fall easily.

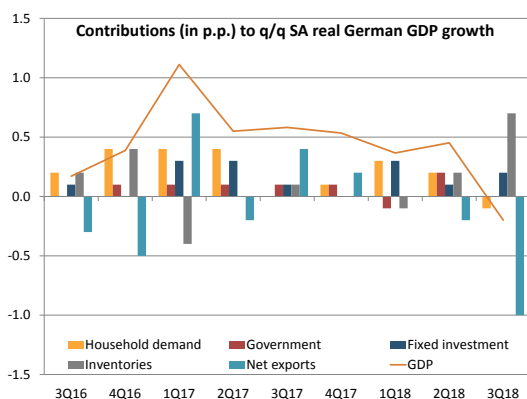
GERMAN 3Q18 GDP CONTRACTION DUE TO EXPORTS,...



...AND IN PART DUE TO NEW CAR EMISSIONS TESTS (WLTP)



HOUSEHOLD DEMAND IN FIRST Q/Q CONTRACTIONS SINCE 1Q15.



EUROZONE ECONOMY

It were German exports which dragged the German growth down in 3Q18, but household demand weakened as well.

As was suspected – and as was suggested by the previous releases of the German Statistical office – exports were the No.1 reason behind the 0.2% q/q contraction of the German economy in 3Q18. This was thus the first q/q contraction since 1Q15 (-0.1% q/q) and the largest one since 1Q13 (-0.3% q/q).

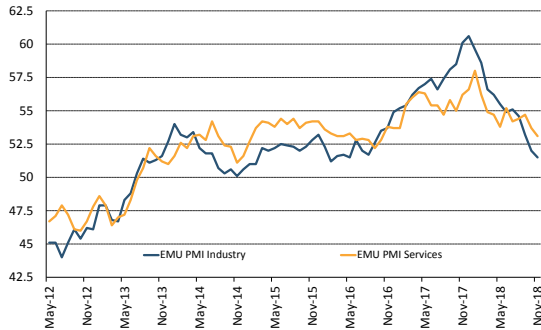
Exports contracted 0.9% q/q, their worst quarterly performance since 4Q12, very likely reflection, at least in part, of lower car production. Although simmering trade war between US and China may have taken a toll, car production was likely to have been, to some extent I cannot measure, influenced by the halt of production of some models that did not make homologations according to new standard (WLTP or Worldwide Harmonized Light Vehicle Test Procedure) on time. That this was the case is seen in precipitous decline in the annual growth of car production: it fell from +5% y/y in June to -15% in August (and -6% y/y in September). This tests-induced slowdown will be reversed in time.

That said, there are other signs of the weakness that extend beyond this.

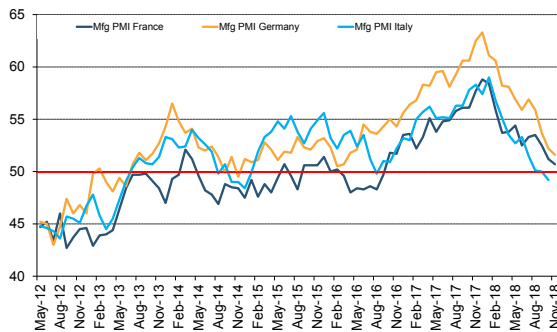
Household demand contributed negatively to q/q growth rate for the first time since 1Q15, and most since 4Q13. With unemployment at or close all-time low, this was certainly unexpected. On the other hand, but also surprisingly, fixed investments continued to grow at about 0.8% q/q rate. That this growth didn't stop or at least falter points at trade war fears having so far had little impact on actual fixed investments decisions. So far.

To sum, while disappointing at the level of the headline number, the structure of the 3Q18 German GDP growth offers some hope that 4Q18 will be better. Though, true, growth rates of 2017 – above 0.5% q/q – will remain unattainable.

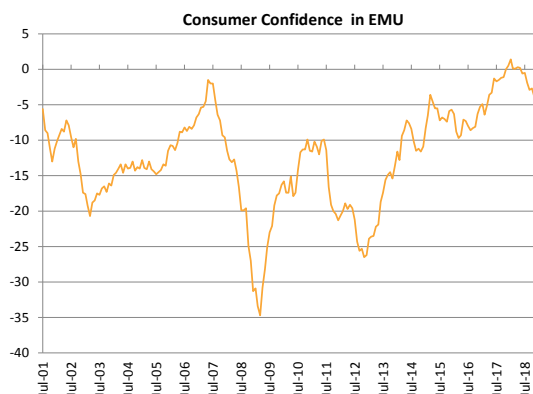
PMI CONTINUES TO WORSEN MID-WAY THROUGH 4Q18,...



...ESPECIALLY IN MANUFACTURING.



CONSUMER CONFIDENCE LOWEST SINCE APRIL 2017



This was confirmed by flash November PMI data.

German manufacturing didn't seem to have regained firm footing in November, its PMI having fallen further to 51.6, the lowest since March 2016 (50.7). French industry also fell (50.7) so this looks like wider problem than with just German carmakers due to WLTP (although manufacturers, according to the PMI compiler – Markit - did blame “sluggish car sales especially” for weakness in the overall PMI).

With Italy likely below 50 (Italy releases only final PMI, so no data there yet), as was the case in October, **the Euro-area manufacturing PMI fell to 51.5, the 2½ year low.** And it does not look like this is going to improve soon: **orders fell for the second month in a row.**

Service sector is in better shape but it too did see better times: there was another worsening of the service index in November, to its lowest (53.1) in little over two years. Expectations regarding the future growth were at 4 year low, not a good omen for the coming quarters. And neither is the slowest growth of new orders in 2 years.

Combine this with **worsening of the consumer confidence** – flash November data, released last week showed it fell to -4 pts., lowest since April 2017 – and it is hard to see why economic growth should quicken any time soon. And how ECB can reasonably continue to say that all is fine and that, as ECB minutes released last week said, data “continue[d] to support confidence that the sustained convergence of inflation to the Governing Council’s aim would proceed and be maintained even after a gradual winding-down of net asset purchases.”

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MARKETS ‡

MM / IRS		3M PRIBOR	6M PRIBOR	2Y	5Y	7Y	10Y	
%	Actual	2.010	2.080	2.345	2.438	2.419	2.405	
	-1M	1.770	1.860	2.375	2.603	2.604	2.608	
	-3M	1.480	1.580	2.020	2.213	2.241	2.270	
	-6M	0.900	0.990	1.390	1.790	1.876	1.955	
ASW spread*		2Y	3Y	4Y	5Y	7Y	10Y	
bps.	Actual	-0.750	-0.748	-0.711	-0.586	-0.421	-0.314	
	-1M	-0.823	-0.834	-0.821	-0.753	-0.533	-0.452	
	-3M	-0.683	-0.783	-0.671	-0.501	-0.238	-0.130	
	-6M	-0.481	-0.595	-0.478	-0.357	-0.167	0.031	
CZGB**		2Y	3Y	4Y	5Y	7Y	10Y	
%	Actual	1.595	1.659	1.716	1.852	1.998	2.091	
	-1M	1.552	1.662	1.742	1.850	2.071	2.156	
	-3M	1.337	1.336	1.502	1.712	2.003	2.140	
	-6M	0.909	0.987	1.228	1.433	1.709	1.986	
FX		EURCZK	EURPLN	EURHUF	EURRON	EURTRY	EURUSD	
	Actual	25.915	4.291	322.38	4.660	5.995	1.133	
	-1M	25.783	4.296	323.22	4.665	6.589	1.147	
	-3M	25.747	4.290	324.50	4.634	7.071	1.154	
	-6M	25.786	4.303	318.43	4.627	5.355	1.170	

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

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