

May 06 | 2019

Weekly | 2018 | Week 18

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CALENDAR

DAY	DATE	TIME (CET)*	MARKET	RELEASE	CONSENSUS**
Monday	6-May-19	10:00	EMU	(Final) Services PMI, Apr'19	52.5
	6-May-19	11:00	EMU	Retail sales, Mar'19, y/y	1.6%
Tuesday	7-May-19	8:00	GER	Industrial orders, Mar'19, y/y (WDA)	-5.4%
	7-May-19	9:00	CZ	Retail sales, Mar'19, y/y	1.9%
Wednesday	8-May-19	8:00	GER	Industrial production, Mar'19, y/y	-2.7%
Thursday	9-May-19	9:00	CZ	Industrial production, Mar'19, y/y	0.8%
	9-May-19	9:00	SPA	Industrial production, Mar'19, y/y	-1.0%
Friday	10-May-19	8:45	FRA	Industrial production, Mar'19, y/y	0.0%
	10-May-19	9:00	CZ	Unemployment, Apr'19	2.8%
	10-May-19	10:00	ITA	Industrial production, Mar'19, y/y	-0.9%

* LOCAL TIME IS CET

** (REUTERS/ BLOOMBERG) POLL

MAY 2019 AUCTIONS

NAME	DATE OF AUCTION	DATE OF ISSUE	MATURES ON	AMOUNT OFFERED*	COUPON
CZGB 2015-2027**	15-May-19	17-May-19	10-Feb-27	CZK 3 bn. max	0.25%
CZGB 2017-2033**	15-May-19	17-May-19	13-Oct-33	CZK 3 bn. max	2.00%
CZGB 2007-2057**	15-May-19	17-May-19	26-Nov-57	CZK 0.5 bn. max	4.85%
CZGB 2015-2026**	29-May-19	31-May-19	26-Jun-26	CZK 3 bn. max	1.00%
CZGB 2018-2029**	29-May-19	31-May-19	23-Jul-29	CZK 3 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.

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

THOUGHT OF THE WEEK

“NOT WATCHING GAME OF THRONES IS NEW “I DON’T WEAR WATCHES”.

WEEK AHEAD

An array of monthly CZ data from the end of 1Q19, and the Eurozone industry: that is what is up for release this week.

Both Czech retail sales and industrial production are expected to have slowed down at the end of 1Q19, the former perhaps a bit surprisingly so given the state of the labor market and sky-high confidence, the latter quite rationally so, considering the weakness evident in Germany.

In Eurozone, **retail sales and industry production for March** will be released, but don't hold your breath: the former will be too weak to be any source for inflation any time soon, and hence it will be of zero interest to ECB, and the latter will show another annual contraction. What with the manufacturing PMI deep below 50, right...?

WEEK BEHIND

Czech manufacturing weakest in over 7 years...

...but CNB continues to tighten nonetheless.

EMU GDP growth surprised on the upside in 1Q19,...

...but Eurozone sentiment worsened further at the start of 2Q

Eurozone core inflation up, but likely only due to Easter

EURCZK UNCHANGED DESPITE CNB'S HIKE,...



| FX

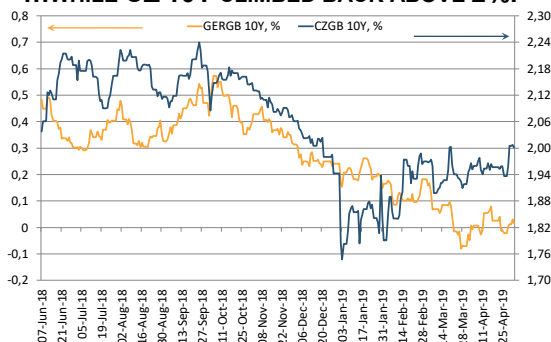
EURCZK fell slightly before the CNB meeting...

...but returned to 25.70 by the end of last week. So much for interest rate differential effect that CNB keeps invoking.

| FI

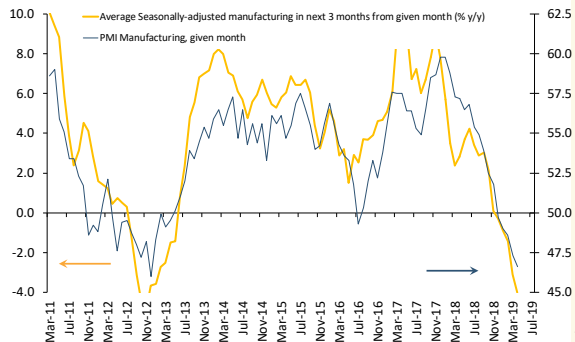
Czech 10Y yields climbed back above 2%,...

...WHILE CZ 10Y CLIMBED BACK ABOVE 2%.



...in the run-up to the CNB's meeting. German yields remained essentially unchanged, and thus only slightly above zero.

May 06 | 2019

CZECH PMI FALLS TO LOWEST SINCE END OF 2012**CZECH ECONOMY**

Czech manufacturing began the 2nd quarter in an even weaker condition that it ended the 1Q19 in.

See, April PMI deteriorated to the lowest (46.6) since the end of 2012 in what was the 10th decline in a row. While the actual output declined, it did so only marginally, but, and more ominously, the new orders fell again, and at roughly the March rate, i.e. at the rate unseen since 2012. This does not bode well for the coming months in terms of actual production.

Of course, there was a net decrease in employment. Of course the optimism regarding the future remained low (though somewhat higher than in March). And of course the current levels of PMI imply a contraction of industry (of about 4% y/y) around the middle of the year. And it is also little surprise that output inflation eased. But did any of this matter...

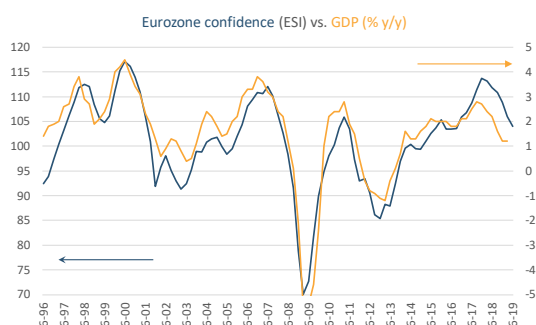
...to CNB? No way.

CNB raised the interest rates for the 8th time in this cycle, bringing the repo to 2%. There was new quarterly forecast released and at least five central bankers hinted they'd vote for the hike in the run-up to the meeting, so the result of Thursday's vote wasn't surprising.

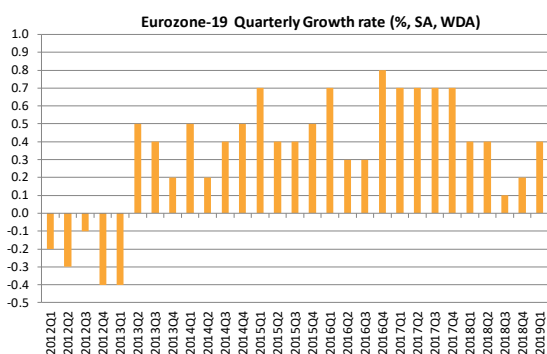
And neither was the new forecast. It again expects CZK to strengthen – and the strengthening is, wait for it, again supposed to be due to interest rate differential (which proved of very little potency in moving EURCZK lower in last 18 months) and due to the real convergence (which also wasn't much of a pusher). The poor track record of these two factors in recent years matters little: EURCZK is forecast at 24.7 this time next year. To which I say: it will not be anywhere near that level.

As before in this tightening cycle, CNB basically used the higher inflation that is due to food prices, regulated prices and housing (i.e. to segments taming the price increases of which via repo hikes is either inefficient or inane) to normalize the policy

SENTIMENT IN EUROZONE WORSENEO FURTHER IN APRIL



EUROZONE GDP GROWTH SURPRISED ON THE UPSIDE IN 1Q19,...



further so that it has cushion when – not if – the economy slows. Though with weaker data coming in from industry and the structure of the inflation, it should’ve stayed put.

Bottom line: in 6 months, I wouldn’t be surprised if the discussion were about whether the rates shouldn’t actually go *down*.

| EUROZONE ECONOMY

| Sentiment in Eurozone worsened further in April.

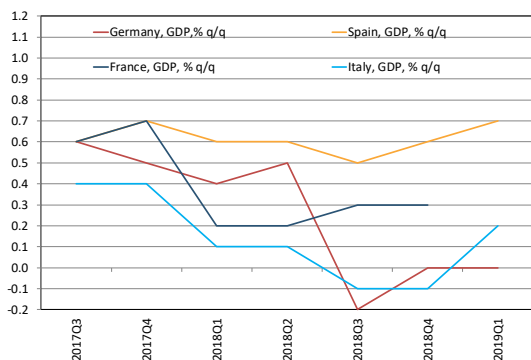
Economic sentiment indicator (ESI) fell to 103.7 pts. at the beginning of 2Q19, the lowest since August 2016, but still comfortable above the long-term (1985-2019) average of 100.9 pts. That said, April level was markedly lower than the 1Q19 average of 105.6 pts. and thus indicative of weaker GDP growth than 1.2% y/y seen in 1Q19. The worsening of ESI in April was due to further decline in sentiment in industry (to lowest since October 2013) and lower confidence in the construction, while consumer confidence remained at the level seen in previous 6 months.

The GDP growth that is consistent with this level of ESI is about 1% y/y, hardly something to justify expectation, embedded in CNB’s latest forecast, that ECB would start tightening in 2020.

| And that holds even though GDP q/q growth surprised on the upside in 1Q19.

Instead of 0.3% q/q that was the analysts’ consensus, the preliminary release has GDP growth at 0.4% q/q in 1Q19 (1.2% y/y). This was the consequence of Italy’s surprisingly strong (for Italy standard, that is) return to black. Whereas analysts were forecasting slight contraction of the Italian economy (-0.1% q/q, just like in each quarter in the 2nd half of last year), Italy grew 0.2% q/q instead. Spain also reaccelerated to 0.7% q/q, rate of quarterly growth unseen since the end of 2017. France grew 0.3% q/q, just like in 3Q and 4Q18.

...OWING TO, PREDOMINANTLY, ITALY.

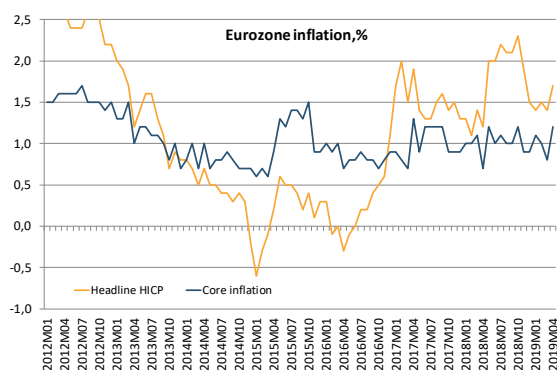


Structural data were not available yet for the entire Eurozone. What is available are data from France and the statement from the Italian statistical office Istat.

As for latter, Istat said net exports were positive contributor to quarterly **Italian growth** and that domestic demand (including inventories) was a negative one. From this, it looks like the positive contribution of net exports was primarily driven by decline in imports. Hardly something to inspire optimism for the future.

For **France**, Insee (French Statistical office) said the domestic demand accelerated slightly, contributing 0.3 pp to q/q growth as against 0.2 pp in 4Q18m and that it grew in both components (household consumption +0.4% q/q, fixed investments +0.3% q/q). The drag on growth came from net exports, reflection of strong growth in imports (0.9% q/q) and no growth in exports (0.1% q/q) – but in the case of the latter, this was actually pretty good, considering that in 4Q18 exports grew 2.2% q/q.

EUROZONE CORE INFLATION UP, BUT THIS IS IN ALL LIKELIHOOD JUST EASTER EFFECT



Eurozone core inflation rose to 1.3% in April.

This is the highest rate since April 2017, and it was driven by jump in service prices.

Services accelerated from 1.1% y/y in March 2019, which was their slowest growth since April 2018 (1%), to 1.9% y/y which is the fastest growth since May 2018 (1.9%).

Hence, it does appear somehow related to Easter and its changing timing in different years. See, same thing happened in 2017 when services rose 1% y/y in March but 1.9% y/y in April. I'd hazard a guess this is somehow related to prices of travel tickets and accommodation (hotels) and other such items, items that have a tendency to rise around Easter.

Thus, what I am almost 100% certain of is that March inflation is not the beginning of sudden acceleration of core inflation. No, May will see core inflation return to around 1.1-1.2%.

May 06 | 2019

MARKETS ‡

MM / IRS		3M PRIBOR	6M PRIBOR	2Y	5Y	7Y	10Y	
%	Actual	2,050	2,090	2,230	2,090	2,025	2,018	
	-1M	2,020	2,060	2,105	1,940	1,870	1,880	
	-3M	1,990	2,060	2,053	1,785	1,708	1,720	
	-6M	1,960	2,030	2,390	2,565	2,550	2,525	
ASW spread*		2Y	3Y	4Y	5Y	7Y	10Y	
bps.	Actual	-0,474	-0,537	-0,475	-0,336	-0,154	-0,017	
	-1M	-0,294	-0,340	-0,264	-0,188	-0,026	0,086	
	-3M	-0,245	-0,247	-0,237	-0,205	-0,026	0,071	
	-6M	-0,877	-0,827	-0,817	-0,725	-0,499	-0,394	
CZGB**		2Y	3Y	4Y	5Y	7Y	10Y	
%	Actual	1,756	1,643	1,660	1,754	1,871	2,001	
	-1M	1,811	1,720	1,731	1,752	1,844	1,966	
	-3M	1,808	1,698	1,626	1,580	1,682	1,791	
	-6M	1,513	1,658	1,718	1,840	2,051	2,131	
FX		EURCZK	EURPLN	EURHUF	EURRON	EURTRY	EURUSD	
	Actual	25,705	4,279	322,99	4,756	6,682	1,119	
	-1M	25,700	4,289	319,82	4,755	6,321	1,123	
	-3M	25,717	4,290	317,55	4,754	5,971	1,146	
	-6M	25,808	4,309	321,70	4,659	6,187	1,139	

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

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