

July 29 | 2019

## Weekly | 2018 | Week 30

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## | CALENDAR

DAY	DATE	TIME (CET)*	MARKET	RELEASE	CONSENSUS**
Monday	29-Jul-19	9:00	SPA	(Preliminary) HICP, Jul'19, y/y	0.6%
Tuesday	30-Jul-19	7:30	FRA	1st estimate GDP, 2Q19, q/q	0.3%
	30-Jul-19	14:00	GER	(Preliminary) HICP, Jul'19, y/y	1.3%
Wednesday	31-Jul-19	8:45	FRA	(Preliminary) HICP, Jul'19, y/y	1.2%
	31-Jul-19	9:00	SPA	1st estimate GDP, 2Q19, q/q	0.6%
	31-Jul-19	11:00	EMU	(Preliminary) Core/Headline HICP, Jul'19, y/y	1%/1.1%
	31-Jul-19	11:00	EMU	1st estimate GDP, 2Q19, q/q	0.2%
	31-Jul-19	8:45	ITA	(Preliminary) HICP, Jul'19, y/y	0.5%
	31-Jul-19	12:00	ITA	1st estimate GDP, 2Q19, q/q	-0.1%
Thursday	1-Aug-19	9:30	CZ	Manufacturing PMI, Jul'19	45.4
	1-Aug-19	10:00	EMU	(Final) Manufacturing PMI, Jul'19	46.4
	1-Aug-19	13:00	CZ	CNB rate-setting meeting, 2W repo	2.0%
	1-Aug-19	14:00	CZ	Budget balance, Jul'19	N/A
Friday	2-Aug-19	11:00	EMU	Retail sales, Jun'19, y/y	1.3%

\* LOCAL TIME IS CET

\*\* (REUTERS/ BLOOMBERG) POLL

## | AUGUST 2019 AUCTIONS

NAME	DATE OF AUCTION	DATE OF ISSUE	MATURES ON	AMOUNT OFFERED*	COUPON
CZGB 2015-2023**	28-Aug-19	30-Aug-19	25-Oct-23	CZK 3 bn. max	0.45%
CZGB 2015-2026**	28-Aug-19	30-Aug-19	26-Jun-26	CZK 3 bn. max	1.00%

\* 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.

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

## | THOUGHT OF THE WEEK

“JIMMY, YOU KNOW WHAT LIFE IS? IT IS THE S\*\*\*T THAT HAPPENS WHEN WAITING FOR THINGS THAT NEVER COME”.

## WEEK AHEAD

**Very busy week ahead of us, both here and in Eurozone.**

The biggest event in Eurozone is obviously the **release of the first estimates of 2Q19 GDP growth for 3 large Eurozone countries** (Spain, France and Italy) **and for the Eurozone as a whole**. Expectations are...well, as expected 😊 Italy is to have remained in a small contraction both q/q and y/y, France up 0.3% q/q and Spain up double that much. Altogether, Eurozone should see growth of about 0.2% q/q, although I suspect it will come at 0.3-0.4% q/q as Germany will surprise on the upside due to the boost from inventories (recall that the inventories subtracted 0.6 pp from the quarterly growth in 4Q18-1Q19).

There will also be **retail sales data and inflation data for Eurozone** (for June and July, respectively), but story will have remained unchanged: weak growth of retail sales and thus non-existent demand inflation.

As regards Czech Republic, there is a **rate-setting meeting of CNB**. There now appears to be zero appetite for further tightening, as evidenced by comments of otherwise hawkish Board member Michl ↗ last week. **Manufacturing PMI** will be shown to have remained deeply below 50 but not much can be read into this, seeing that the recent sub-50 readings failed to predict the actual production with any accuracy.

## WEEK BEHIND

■ Czech business confidence continues to worsen everywhere but in construction ▶

■ Eurozone leading indicators confirm no urgency for ECB to ease ▶

■ ...but ECB hints at fresh stimulus nonetheless ▶

■ Germany IFO shows deterioration of expectations in services ▶

## | FX

**EURCZK continued to trade sideways,...**

...with pretty much no movement whatsoever. 0.05 CZK that EURCZK moved up by last week isn't worth commenting on.

## | FI

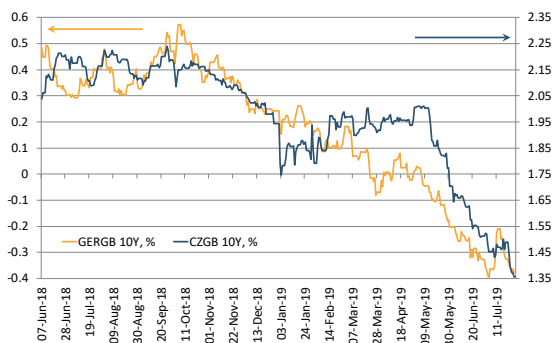
**Czech long yields fell to lowest since October 2017,...**

...with 10Y yield falling below 1.4% and hitting 1.35% at the end of last week. This was in response to (1) "it's been enough" statement from otherwise hawkish CNB Board member Michl and (2) ECB's hints at fresh stimulus this Fall.

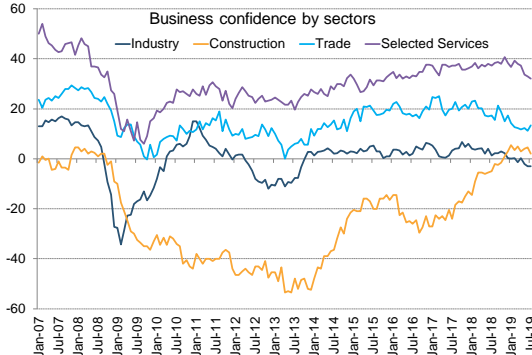
**NO MOVEMENT WHATSOEVER ON EURCZK LAST WEEK**



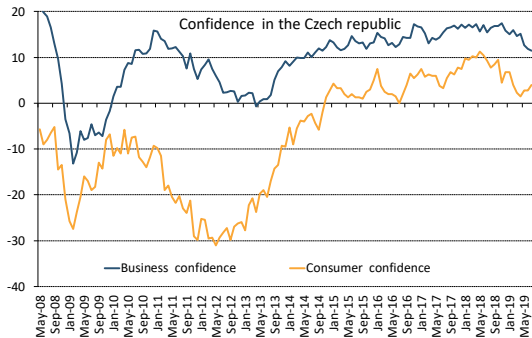
**CZECH 10 YIELDS FELL FURTHER IN THE RUN-UP TO THE CNB MEETING.**



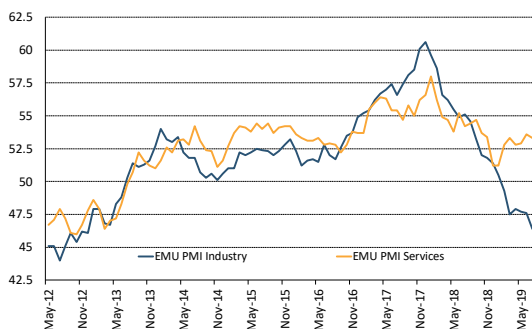
**CONFIDENCE CONTINUES TO DRIFT LOWER IN MOST SECTORS**



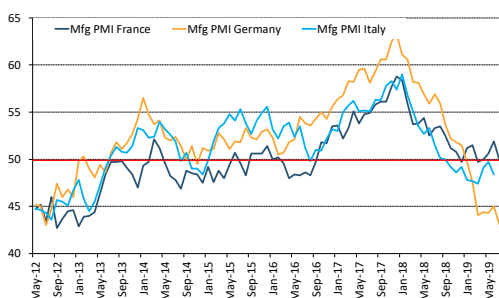
**HOUSEHOLD CONFIDENCE IS IMPROVING**



**EMU SERVICE SECTOR REMAINS IMMUNE TO WEAKNESS IN MANUFACTURING,...**



**...WHICH, IN TURN, IS MAINLY DUE TO GERMANY, AS SEEN IN PMI OR...**



**CZECH ECONOMY**

**Construction remains the only sector where optimism continues to reign,...**

...at least judging by the July confidence data from the Czech statistical office. Data showed that all three main sectors outside construction (that is, industry, trade, services) saw confidence worsened year-to-date, and for services and industry there was worsening in the month of July as well.

While confidence in construction is close to an all-time-high, reflecting the construction boom that's been going on for some time now, one in industry is lowest since September 2013, in services since October 2015. Hence, although there is no evidence of large-scale worsening of the optimism, there is one of gradual drift towards pessimism in almost all sectors. This is indicative of weakening of the economic dynamics, not of impending recession.

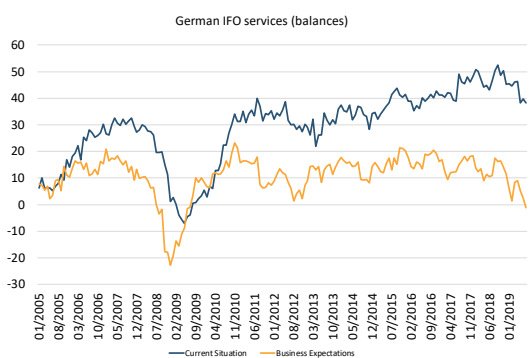
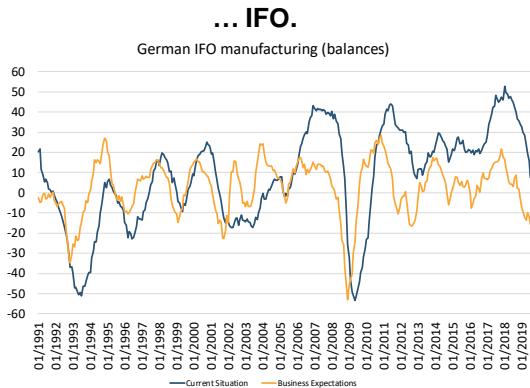
For households, and slightly surprisingly so, confidence improved for the third month in a row. Having been worsening for 12 consecutive months since May 2018, confidence rose from April's low of 1.5 pts. to 4 pts in July. This is still much lower than May 2018 high of 11.3 pts., but is comfortably higher than long-term average. Households thus don't show any pessimism and can be relied upon to provide growth driver for the remainder of the year.

**EUROZONE ECONOMY**

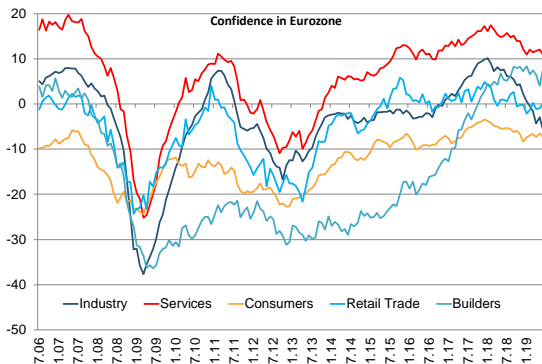
**Eurozone leading indicators showed that there is no need to wave the big dovish flag at the ECB.**

True, PMI in manufacturing edged lower in July, hitting, according to preliminary data released last week, 46.4 pts., the lowest since December 2012. But service PMI has been edging higher since the end of the previous year, being now (in July 2019) 2.1 pts. higher than in December 2018 (51.2 vs. 53.3 pts.). This, at the minimum, shows that the

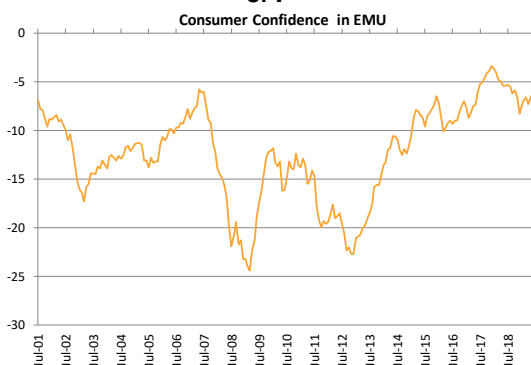
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**SAME PICTURE OF ISOLATED WEAKNESS EMERGES IN EC CONFIDENCE DATA**



**CONSUMER CONFIDENCE CONTINUES TO HOLD UP.**



weakness in Eurozone is concentrated in industry alone and isn't spreading. Moreover, if you recall from our previous weeklies, industry weakness is concentrated in Germany: Spanish or French industries continue to grow y/y, Italian one is in small decline. There have thus been no spill-overs from industry to services.

**...except maybe in Germany where the overall IFO index fell to 95.7 pts., lowest since December 2012. The biggest drag came from manufacturing, naturally, with current assessment of the situation in that sector being the lowest since December 2012 and the expectations at their gloomiest since November of that year, but services also took a hit. Current situation assessment remained upbeat, but expectations worsened. And worsening it was: July's -1.1 pts. is the lowest reading since 2009. Although this doesn't look good for the future on the surface, my view is that the expectations component in services reflects the gloomy situation in industry and the expectation that, at some point, services will be hit as well. But must they be, really? I say it would have already happened were it supposed to.**

And, at any rate, remember that this just concerns Germany, not the whole of Eurozone,

**June Eurozone EC-measured consumer/business confidence confirmed that the Eurozone weak spot is isolated and it is industry.**

Confidence in industry took another dive in July (to lowest since September 2013) while confidence in all other sectors held up well. Needless to say, **consumer confidence** held up as well. Although, as noted many times before here, this has little bearing on actual consumer demand so it can – should, really – be somewhat discounted when forming the opinion about the future consumer demand in the Eurozone.

**All this nonetheless, ECB meeting paved the way for fresh stimulus down the road,**

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maybe even as early as in September.

**First**, ECB confirmed that work has begun on how to implement further easing of the policy *if* it is deemed necessary: Draghi said that Governing council has “*tasked the relevant Eurosystem Committees with examining options, including ways to reinforce our forward guidance on policy rates, mitigating measures, such as the design of a tiered system for reserve remuneration, and options for the size and composition of potential new net asset purchases.*”

**Second**, that “*if*” pretty much means “*when*” was reinforced by the ECB’s assessment that, although wages and employment gains allegedly continue to “*underpin the resilience of the economy*”, the economic environment is one of “*muted inflationary pressures and declining inflation expectations*”. In other words, growth is not producing inflation.

**Third**, Draghi stressed that ECB’s goal is symmetrical (i.e., too low inflation is as much of a concern as too high an inflation), and that “*if the medium-term inflation outlook continues to fall short of our aim, the Governing Council is determined to act.*”

Combined with Draghi having made it very clear that falling inflation expectations is something ECB doesn’t like and will work to prevent, this pretty much guarantees that ECB will do something soon: “*We see a considerable mass of expected inflation moving to lower levels of inflation and that’s exactly what we are seeing: 1.6% is the inflation rate that we see in 2021 in our projections. That’s something about which the Governing Council said today in the introductory statement: we don’t like it.*”

Although Draghi said there is no unanimity on the Governing Council regarding what to do, he said “*most people*” on the GC converged on the outlook, at the same time, what to do about it. In other words, Germans don’t like restarting the QE, but we have majority to do it.

Bottom Line: it now looks increasingly likely that September will bring an easing package. Like it or not.

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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

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