Monday, March 15, 2010

KBC Banking & Insurance

Central European Weekly

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Czech Republic

Czech economic growth fell by “only” 4.1% last year

Poland

Zloty waits important domestic macro readings

The Week Ahead

The Polish inflation and IP figures take the lead

Overview

	Last	Change 1W	Outlook 1W ahead	Outlook 1M ahead
EUR/CZK	25.50	-0.54%	↘	↘
EUR/PLN	3.892	0.49%	↘	↘
EUR/HUF	265.8	-0.18%	↘	↘
3M PRIBOR	1.45	0.02	→	→
3M WIBOR	4.12	-0.02	→	→
3M BUBOR	5.72	-0.03	↘	↘
10Y CZK	4.01	0.02	↗	↗
10Y PLN	5.78	-0.18	↗	↗
10Y HUF	7.01	-0.07	→	→
3M EURIBOR	0.58	-0.37	→	↗
10Y EMU	3.20	0.04	↗	↗

Last values from Friday 15:30 CET

Is The Czech Koruna Set for a Strong Appreciation?

Last week, it was the koruna, among CE currencies, which was encouraged by two highly positive data releases and finally outperformed the regional peers. Firstly, the GDP revision showed that, owing to exports, the Czech economy was growing for the second consecutive quarter at the end of the year. In addition, January’s figures indicate a surprisingly strong current account surplus. Thus the economy is recovering, while continuing to improve its external balance. This is an perfect combination for the koruna.

Furthermore, foreign trade (stagnating imports, recovering exports) is not the only reason for the external balance improvements; transfers from EU Structural Funds are also starting to rise to a reasonable degree, although these have played just a very limited role in recent years. However, January’s contribution was CZK 6 bn. Moreover, the situation will continue to improve in the future. Applications for the use of Structural Funds totalling CZK 789 bn (21% of GDP) have been filed in the Czech Republic at the moment, with projects totalling CZK 311 bn (9% GDP) already approved. Much of this money will flow to the Czech Republic within the next three years, and may significantly improve the external balance. While the money will be converted through the central bank, rather than directly through the market, it should have an indirect positive effect on the Czech currency. The reason is that the central bank will probably not wish to increase its forex reserves at such a fast rate, and therefore the bank itself will want to sell some of the euros on the market. However, even if the bank accumulates all of the euros and decides to print money instead of them, the strong monetary expansion could make the Czech National Bank raise rates more rapidly in the future. This would not be favourable for the koruna too.

By and large, the future of the koruna looks promising, unless public finances affect it, as investors and rating agencies are eagerly waiting to see how a new government will tackle the troublesome public finances after May’s parliamentary elections.

Czech Republic

Macro review

On the quarter-on-quarter basis, the Czech economy has been growing for two consecutive quarters, by 0.6% in Q3 and 0.7% in Q4. We view the new GDP figure for the last quarter positively, given the Statistical Office's earlier pessimistic forecast, which was, at first glance, inconsistent with the better figures from certain sectors of the economy. Thus the economy fared better in late 2009 than eurozone countries, where quarter-on-quarter GDP growth was only 0.1%.

The full-year decline (-4.1%) is not that surprising, particularly if it was primarily due to inventories and investment in machinery and means of transport. With demand falling, the business sector significantly reduced its investment activities, hand in hand with the increasingly idle production capacities. Full-year household consumption stagnated, but the second half of the year already saw a clear decline, due to rising unemployment and stagnating wages. The public sector, by contrast, significantly stepped up its consumption expenditure during the recession, and this will, in the end, certainly affect last year's deficit of public budgets, which probably exceeded 6% of GDP. On the supply side, the economy was being curbed by industry, which was affected by the drop in foreign demand in particular. Thus the only growing sectors were agriculture and partly construction.

For this year, we believe that the trend of falling investment and household consumption will persist. As far as investment is concerned, we expect that the public sector may partly counterbalance the drop in private investment activities, notably owing to resources from the EF. Household consumption will continue to be at the mercy of the negative labour market developments. On the other hand, foreign trade and replenishments of inventories may have a positive effect on GDP this year. Overall, however, we cannot expect any strong recovery; more likely, we will see slow and fragile growth, dependent on the divergences of the German economy. Hence we have left the forecast for this year at 1.5%.

Fixed income

The Czech yield curve steepened last week, when yields went up by 1.5 bps at the short end and almost 4 bps at the long end. Both the calming of the situation surrounding the Greek debt problems and the rise in the domestic stock market, after the release of reasonable statistical figures, contributed to that price fall. The short end of the curve showed increased volatility; a greater rise in the short end was prevented by the stagnation of consumer prices, indicating that the CNB would not hasten to raise rates. At the end of the week, CNB Deputy Governor Singer denied rumours that the central bank might continue to cut rates, despite February's year-on-year inflation being lower than the CNB's expectation. A greater rise in yields at the long end of the curve is consistent with the developments in eurozone markets.
The main statistics of this week will be January's retail sales, released on Wednesday. A decline is being anticipated, and this should encourage demand for bonds; however, statistics surprised on the upside last week, and thus we cannot completely rule out a similar scenario this time either.
Nonetheless, the main event of the week will be Wednesday's auction of government bonds for CZK 7 bn, due in 2015. The issue coupon will be determined during the week, prior to the auction. The demand for domestic bonds, after the Ministry of Finance announced that some of its bonds would be denominated in euros, is improving, and therefore this issue should also be easily subscribed.

EUR/CZK technical picture

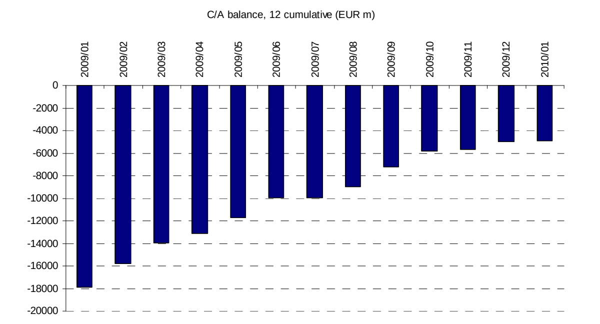
(25.4300) Below triangle, but pattern at apex (see graph).
1st support area at 25.4320/ .4110 (monthly envelope bottom/ current year low?), ahead of 25.3800 (Nov low), where pause favored.
If wrong, next levels 25.2900 (weekly Bollinger bottom), ahead of 24.9750 (Sep low): tough on 1st attempts.
Resistance area at 25.7400/ .7600 (breakdown hourly/ daily): ideal area to stay below to keep current mood on CZK.
Failure to cap would see next levels at 25.9770 (weekly Bollinger midline), ahead of 26.0330/ .0500 (falling Weekly Moving Average/ Feb 25 high), where pause favored.

DAILY CHARTS:

Poland

Currency

The Polish currency slightly lost ground last week. However, its changes were small, the currency pair EUR/PLN started at 3.87 and closed the week at 3.882. At the beginning worries that Greek problems could spread to other countries had a negative impact on the global sentiment and eased also the Polish currency. On Friday, the zloty corrected part of its losses after investors' risk appetite improved, even if Polish trade balance and current account marked a higher deficit than the market expected. Although the country's current-account deficit narrowed in January after the trade deficit was lower than in December, it surprisingly totalled EUR 710 m, while analysts expected the deficit just above EUR 0.5 bn. Indeed the gradually recovering economies of Poland's main trading partners and low statistical base in exports overlapped with rebuilding imports allowed to get better results than in 2009, however, markets expected better results.

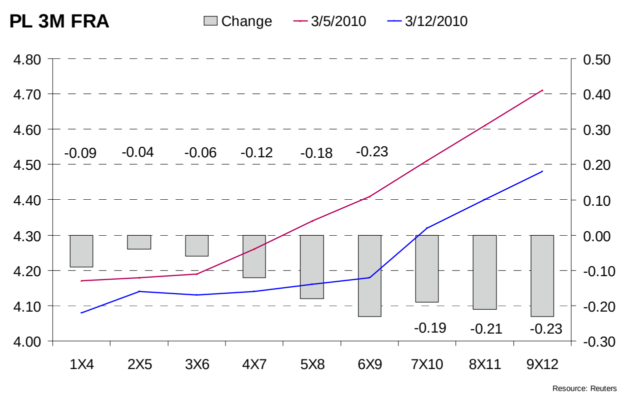


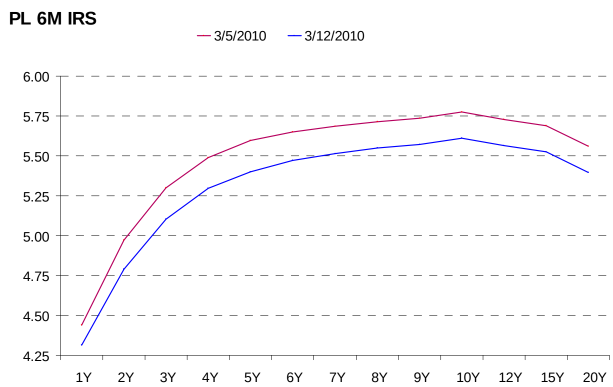
This week, there will be more important statistics released. The February inflation should show lower readings, the same improvement may confirm PPI on Wednesday. On the other hand industrial production should turn into positive territory. Therefore we expect that better fundamentals may help the Polish currency to close the week below the EUR/PLN 3.89 level.

EUR/PLN technical picture

(3.8900): Scored new reaction low off 4.9300.
1st support area 3.8570/ .8500 (current new reaction low off 4.9300/ 1st target of long term daily Double Top off 4.2250: see graph), where pause favored.
If wrong, next Support would come in at 3.8272 (monthly envelope bottom): tough on 1st attempts.
1st Resistance comes in at 3.9161 (falling weekly Short Term Moving Average): ideal area to stay below to keep current mood on Zloty.
Failure to cap would see next levels at 3.9560/ .9713 (breakdown hourly/ daily), where pause favored.

DAILY CHARTS:





CE Weekly Preview

WED 9:00	CZ Retail Sales (change in %)		
	Jan-10	Dec-09	Jan-09
Sales	**-2.5**	-1.9	-3.5

CZ: Retail Sales Continue to Fall

January’s retail sales data is likely to bear out the continuing trend of falling sales, which has persisted for fifteen consecutive months. Lower car sales and one less business day in the month suggest another decline. Nevertheless, the main reason is poor consumer demand, with consumers reducing their spending on household equipment, due to their worsened financial situation and concern about the future development of that situation. The wait for more attractive prices in shops is also relevant, but this is immeasurable. For this year as a whole, we anticipate a further decline in retail sales, within 1%. An improvement is unlikely to occur until 2011, when the recovery of the Czech economy might encourage the labour market.

Calendar

	Date	Time	Indicator	Period	Forecast		Consensus		Previous	
					m/m	y/y	m/m	y/y	m/m	y/y
CZ	15.3.2010	09:00	PPI (%)	02/2010	0.1	-1.6	0.1	-1.6	0.5	-1.5
PL	**15.3.2010**	**14:00**	**CPI (%)**	**02/2010**			**0.4**	**3.0**	**0.5**	**3.6**
CZ	16.3.2010	09:00	Retail sales (%)	01/2010		-2.5		-2.7		-1.9
PL	16.3.2010	14:00	Wages (%)	02/2010			1.5	3.2	-11.5	0.5
PL	16.3.2010	15:00	Budget balance (PLN M)	02/2010					-4 841.5	
HU	17.3.2010	09:00	Industrial output (%)	01/2010 *F					8.8	5.7
CZ	**17.3.2010**	**12:00**	**CZ bond auction 3.40%/2015 (CZK B)**	**03/2010**			**7**			
PL	**17.3.2010**	**14:00**	**Industrial output (%)**	**02/2010**			**3.2**	**9.4**	**-5.4**	**8.5**
PL	17.3.2010	14:00	PPI (%)	02/2010			0.3	-2.1	0.3	0.2
HU	19.3.2010	09:00	Wages (%, ytd.)	01/2010						0.0

m/m - monthly change; y/y - yearly change; s.a. - seasonally adjusted; n.s.a. - non-seasonally adjusted; P - preliminary; F - final
EMU, USA, UK, JPY - figures seasonally adjusted, if not stated otherwise; Central Europe - figures seasonally non-adjusted, if not stated otherwise
Government Bond Auction: period = auction settlement date; m/m = total bids; y/y = supply

Our forecast

Official interest rates (end of the period)

		Current	Jun-10	Sep-10	Dec-10	Mar-11	Last change	
Czech Rep.	2W repo rate	*1.00*	1.00	1.00	1.25	1.50	-25 bps	16/12/2009
Hungary	2W deposite r.	*5.75*	5.50	6.00	6.00	6.00	-25 bps	2/23/2010
Poland	2W inter. rate	*3.50*	3.50	3.75	4.00	4.00	-25 bps	6/25/2009

*Short-term interest rates 3M *IBOR (end of the period)*

		Current	Jun-10	Sep-10	Dec-10	Mar-11
Czech Rep.	PRIBOR	*1.45*	1.55	1.65	1.80	2.05
Hungary	BUBOR	*5.72*	5.50	6.00	6.00	6.00
Poland	WIBOR	*4.12*	4.60	4.70	4.80	4.80

Long-term interest rates 10Y IRS (end of the period)

	Current	Jun-10	Sep-10	Dec-10	Mar-11
Czech Rep.	*3.48*	3.50	3.70	3.85	4.02
Hungary	*6.71*	7.75	8.00	7.50	7.25
Poland	*5.63*	5.50	5.70	5.80	5.90

Exchange rates (end of the period)

		Current	Jun-10	Sep-10	Dec-10	Mar-11
Czech Rep.	EUR/CZK	*25.5*	25.8	24.8	23.8	25.5
Hungary	EUR/HUF	*266*	280	275	270	265
Poland	EUR/PLN	*3.89*	3.85	3.60	3.90	3.30

GDP (y/y)

	Q3 2009	Q1 2010	Q2 2010	Q3 2010	Q4 2010
Czech Rep.	*-4.5*	1.4	1.7	1.5	1.4
Hungary	*-5.3*	-1.5	0.5	1.0	2.0

Inflation (CPI y/y, end of the period)

	Dec-09	Jun-10	Sep-10	Dec-10	Jan-11
Czech Rep.	*1.0*	1.1	2.1	2.2	2.0
Hungary	*5.5*	3.5	3.5	3.5	3.5

Current Account as % of GDP

	2009	2010
Czech Rep.	-0.8	-1.0
Hungary	-1.0	-0.5

Public finance balance as % of GDP (in ESA95 standards)

	2009	2010
Czech Rep.	-6.5	-5.5
Hungary	-3.9	-5.5

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