

A close call as to when the CNB will hike

We think a 25 basis point rate rise by the Czech National Bank, either this week or in November, is a done deal



Source: Shutterstock

The CNB meets on Wednesday

Given the lack of strength in the Czech koruna (CZK) and sound domestic economic data, we believe a 25bps hike either this week or in November meeting is a done deal. We see a 60% probability of a hike in a November vs 40% of a hike on Wednesday. This is not necessarily for fundamental reasons, but rather due to the publication of the Czech National Bank Inflation Report and a new set of forecasts at the November meeting.

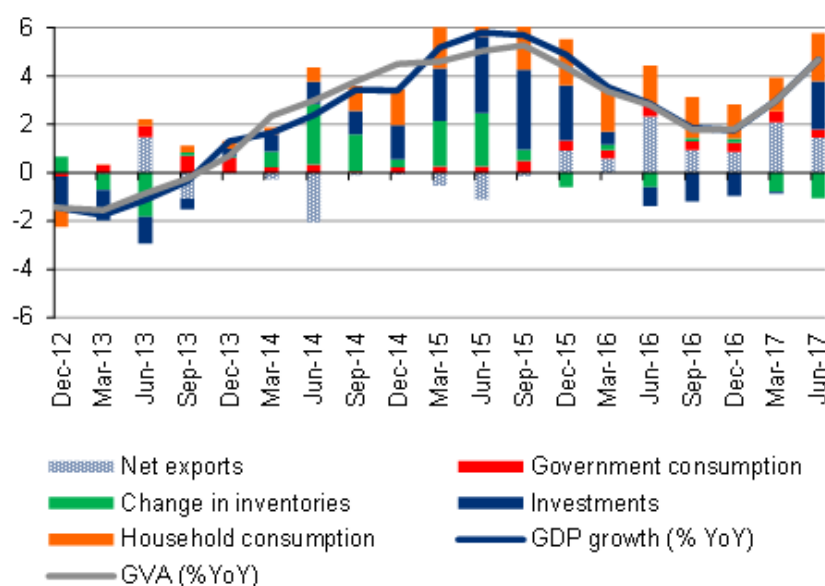
Inflation and economic performance

Czech CPI inflation hit 2.5% in July and should remain safely in the upper tolerance band of the CNB over the monetary policy horizon. The CZK has been over-bought since intervention by the CNB, therefore limiting koruna appreciation. That, and favourable economic growth, generate clear pro-inflationary risks.

Economic performance soared in 2Q17 as GDP reached 4.7 YoY, a figure well above the initial market estimate of 2.9% or the CNB forecast of 3.6%. Stronger dynamics were driven by renewed investment activity, but also accelerating consumption of households (4.4% YoY vs 3.5 in the CNB'S

forecast) and foreign demand.

Czech GDP structure (ppt)



Source: CZSO

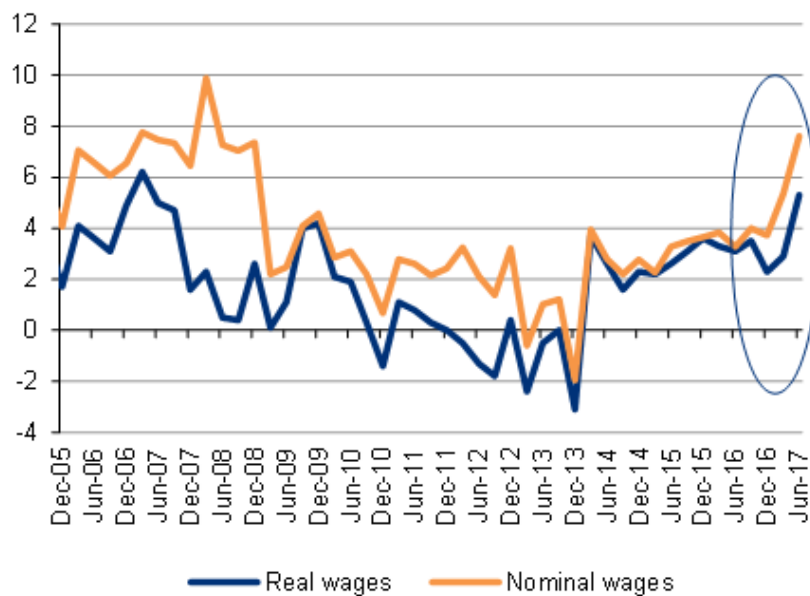
Significant wage growth

Wage dynamics are picking up. The average real wage growth reached 5.3% in 2Q17 beating expectations of the market and the CNB, see below. The economic story remains favourable, which demands tighter monetary conditions. As such, the CNB will deliver another hike this year.

Yet, the CNB may not see a need for an imminent hike this Wednesday. This was confirmed by Governor Rusnok, pointing at his news conference to see another CNB staff forecast before the next rate decision. The favourable Q2 GDP is partially an “optical effect” driven by working day adjustment (65 in 2Q16 vs 61 in 2Q17). Real not-seasonally adjusted GDP growth in 2Q17 reached 3.4% YoY, vs 4.7% adjusted. Also, the July credit statistics confirmed a deceleration in new housing loans, which got to the lowest level since January 2016. This fall went beyond the typical holiday seasonality and might be related to new CNB macro-prudential measures.

Czech wage dynamics

Percentage, year-on-year



Source: CZSO

A close call

We believe the CNB will wait until November but will pre-signal the hike this week, although it's a close call.