Looking for one more hike in the Czech Republic

A November rate hike by the Czech National Bank looks like a done deal

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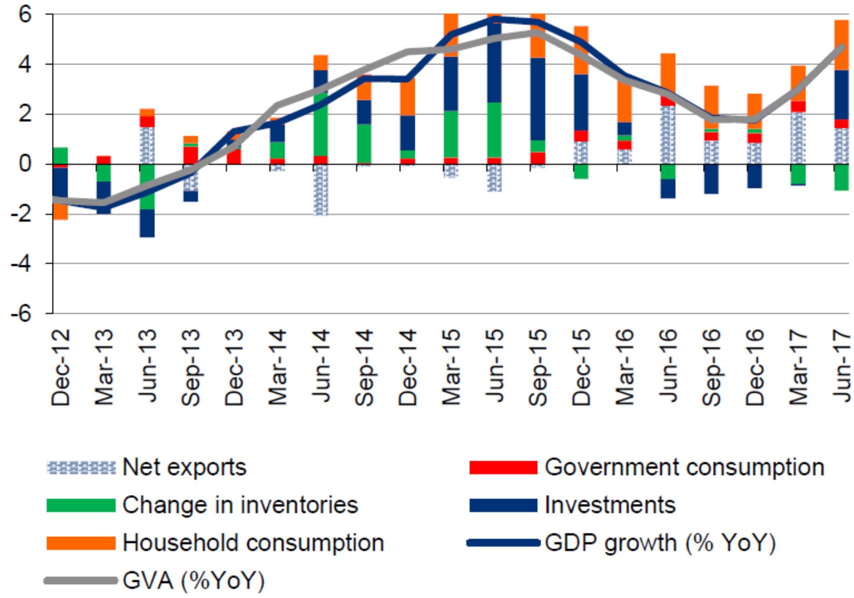
Give the lack of strength in the Czech koruna and sound domestic economic data, we believe a 25 basis point rate hike at the November meeting is a done deal. Recent comments by Governor Rusnok appear to confirm late Autumn as when we can expect a rise, with the publication of the CNB Inflation Report.

- 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. Moreover, the post-interventions 'over-boughtness' in CZK limiting koruna appreciation and the favourable economic growth generate clear pro-inflationary risk.
- Economic performance soared in 2Q17 as GDP growth reached 4.7% YoY, well above the initial market estimate of 2.9% and the CNB forecast of 3.6%. Stronger dynamics were driven by renewed investment activity and accelerating consumption by households (4.4% YoY, vs 3.5% in the CNB forecast) and foreign demand.
- Wage dynamics are picking up. Average real wage growth reached 5.3% in 2Q17, beating

market and CNB expectations (Figures 3 and 4). In all, the economic backdrop remains favourable, demanding tighter monetary conditions. As such, the CNB will deliver another hike this year, in our view.

Czech GDP structure



Source: CZSO, ING Bank

On the other hand, the CNB is unlikely to see a need for an imminent hike (ie, in September). This was confirmed by Governor Rusnok yesterday, pointing to his preference to see another CNB staff forecast before the next policy rate decision. The favourable 2Q17 GDP growth is partially an 'optical effect, driven by a working day adjustment (65 in 2Q16 vs 61 in 2Q17). Indeed, real non-seasonally adjusted GDP growth in 2Q17 reached 3.4% YoY (Figure 5), vs 4.7% adjusted.

Also, July credit statistics confirmed a significant deceleration in new housing loans, which reached its lowest level since January 2016 (Figure 6). This drop went beyond typical holiday seasonality and might be related to new CNB macro-prudential measures. As such, we believe that the CNB will decide to tighten monetary policy more gradually, in order to have enough time to evaluate its policy decisions, influencing the real economy with some lag. Thus, we see a hike in September as less likely and expect further tightening only at the November meeting, when new CNB staff projections become available.