

CNB Preview: 50bp cut likely this Thursday

We expect the Czech National Bank to cut interest rates by a further 50 basis points this Thursday, though recent communication from the central bank was not specific about the intensity of further rate reductions, so a surprise might emerge. Quantitative easing will be mentioned again, but only as a financial stability tool



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A 50bp cut this Thursday is likely

Given the current extraordinary developments in both domestic and global economies related to the spread of Covid-19, the CNB is likely to continue the path of monetary easing. Indication of a further lowering of rates was less straightforward in the recent communication by CNB representatives, but it was broadly indicated that a reduction of rates is likely, though there were no specifics about the scale of the cut. However, we expect a further 50bp cut this Thursday.

QE not in the pipeline for now

Finance Minister Schillerova indicated at the end of March the CNB's intention to start QE, but the

CNB downplayed this option and highlighted its need for financial stability purposes only. Despite that, the MinFin repeated the scope for potential Czech government bond buying by the CNB later during April, but recent communications steered clear even after the act on CNB buying was approved in Parliament and the CNB could possibly embark on broad bond-buying (though this legal change applies only until the end of 2021). Board member Tomas Holub mentioned to Reuters in mid-April that QE might be an option only if rates are at zero, and the economy is heading into a protracted recession with strong deflationary pressures. We are not yet there for now, in his opinion.

New CNB forecasts will be introduced

Although the government has started easing some of the restrictions, it took longer than the expected the end of March. Therefore Czech GDP revisions are gradually moving downwards and the range of consensus GDP estimates is fairly wide – from -5% to -10% year on year in 2020. The CNB will introduce its new set of forecasts, but is very likely to accompany them with various outlook scenarios. The CNB's baseline for 2020 might indicate a recession of around 6-7%, in our view.

The potential for other tools to be delivered during the May meeting is likely to be limited. The CNB reduced its countercyclical capital buffer further to 1% and additional lowering might come later this year, but unlikely this week. EUR/CZK should continue its grind lower, to back below the 27.00 level, as further CNB rate cuts are largely priced in while the central bank is unlikely to embark on QE.

The CNB rate decision to be released later

The press release on the Bank Board's decision on key interest rates will be published at 2:30 pm on Thursday and the regular press conference following the monetary policy meeting will start at 3:45 pm. This is the new setup introduced by the CNB starting with the May rate meeting.