

CNB Preview: Rates on hold this Thursday, hikes to come in 2H18

The CNB will stay on hold on Thursday. Expect the continuation of the modestly dovish bias as CPI undershot the CNB forecast



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No change on Thursday is widely expected

The CNB meeting this Thursday should provide little surprise, as this is the first one since August last year where the consensus is crystal clear. The CNB will stay on hold, as suggested by its February forecast and the dovish rhetoric of CNB Board members. The latest developments in GDP growth, wages and CZK path are in line with the February CNB forecast; only CPI inflation declined more than expected.

0.75

2-week repo rate

should not change this Thursday

CPI below the target mainly due to lower food prices

CPI is now below the target, reaching 1.8% YoY in February vs 2.2% forecasted by the CNB. But this was related mainly to lower growth in food prices and the high base effects from the last year, when prices accelerated due in part to some oneoffs (electronic sales registration in restaurants). As such, compared to the inflation peak in October (2.9% YoY), contributions of food prices to YoY CPI growth declined from 1.4ppt to 0.4ppt in February and restaurants prices contribution fell by 0.2ppt.

The CNB wants to avoid CZK strengtning to tight monetary conditions via rates

The below-target inflation is convenient for the CNB, as it enables it to communicate its dovish stance more credibly. The CNB wants to sound dovish now to avoid CZK strength driven by hike expectations, as tightening of monetary conditions via FX would leave limited room for interest rate tightening. A higher interest rate is the preferred option for CNB to further escape with rates from the zero-bound.

Hikes to come again in the second half of the year

We thus expect the CNB to remain dovish on Thursday, mentioning anti-inflationary risks to the forecast given the lower inflation. The current CNB dovish stance should limit CZK strength for now, enabling the CNB to hike again in 2H18 (two hikes are our baseline now). We also don't exclude a June meeting hike provided EUR/CZK remains flat, thus significantly weaker than the CNB's projected level of 24.90 EUR/CZK (for 2Q18), in turn allowing the CNB to tighten via rates. Still, the August meeting seems more likely for a rate hike as it provides a new set of CNB forecasts.