

## CNB Review: On hold as expected

The Czech National Bank stayed on hold. Despite the domestic economy remaining solid and warranting hikes, it is the external uncertainty that currently matters more for the CNB. The staff forecast still shows highly unrealistic CZK appreciation. Assuming the global environment stabilizes, we still see it as likely for the CNB to hike twice this year



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### Slightly weaker GDP growth for this year and next

The CNB forecasts delivered a weaker GDP outlook for this year from 3.3% in November for 2019 and 2020 to 2.9% and 3.0% respectively. As such, the downward revision was smaller than expected, as the latest MinFin forecast pencils in 2.5% and 2.4% growth this year and next. This is closer to our call. Due to the fall in oil prices, CPI was revised lower from a 2019-average of 2.6% to 2.2%. But still, this is a quite solid figure given the fact that the forecast pencils in 5% CZK appreciation vs EUR this year - to EUR/CZK 24.52 in 4Q19. As such, inflationary pressures are mounting within the CNB's model quite strongly.

## The CNB model expects again strong CZK appreciation

The new CNB forecast is indicating again around five-and-a-half “implied” hikes this year via the mix of FX and rates channels. As was the case previously, the bulk of tightening is expected via FX. This is quite a surprising assumption given the fact that CZK sensitivity towards interest rates is muted, as seen in previous quarters. As such, the forecast itself is hawkish, delivering a strong need to tighten monetary policy further. However, in reality the upcoming CNB rate decisions will be heavily dependent on the global outlook. Hence, looking at the implicit number of hikes is less informative now.

# 1.75

## 2-week repo rate

on hold as expected due to global uncertainty

As expected

## Further hikes will be a function of the global outlook

As Governor Rusnok mentioned, the domestic economy is still developing well, which motivates the CNB board to continue in rates normalisation towards its neutral level (2.5-3.0%), but global uncertainty is high and thus warrants cautiousness.

The main take-away is that the CNB model has become less reliable and doesn't reflect the CZK overboughtness and its potentially muted appreciation ahead. This should mean meaningful monetary tightening via rates needed in quarters ahead (as the FX on its own won't do the job), but only if global economic outlook improves. If this is the case (our base line currently), two more hikes are still on the table this year, in our view.