

## Czech economy slows, and expected to slow down further

Czech economy slowed down to 1.8% in 4Q19, but domestic demand remained surprisingly strong. But given the rising uncertainty amid Covid-19 outbreak, we expect growth to dip below 2% this year but the market pricing of almost four rate cuts are a bit too aggressive and premature in our view



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### Surprisingly strong domestic demand

4Q19 GDP growth for the Czech Republic was revised slightly upwards to 1.8% YoY and 0.3% QoQ, i.e. 0.1 percentage point above the flash estimate published two weeks ago.

Surprisingly, domestic demand came in above expectations as households consumption accelerated to 3.2%, and fixed investments to 3.6% YoY after somewhat weaker previous quarters. Inventories contributed also very positively so total investments growth reached 8% YoY. On the other hand, foreign demand disappointed, mainly goods exports fell by 2.2%YoY in 4Q19 after average growth of around 2% in previous quarters.

These are the weakest numbers since 1Q13.

As such, net exports contributed to growth by negative 2.2 ppt in 4Q19 as a result of weaker

forging demand of 2019 related to trade-wars, Brexit uncertainty and troubles in the automotive segment, mainly in Germany.

Still, despite better than expected domestic demand of the Czech economy, 4Q19 figures provide just limited guidance to this year's development given Covid19 outbreak, which is the main interest of the market right now.

**1.8% YoY** Czech GDP growth in 4Q19

2.4% for the whole 2019

Lower than expected

## Outlook remains unclear, but growth to be below 2%

We expect the Czech economy to grow by 1.9% this year, which belonged to more negative estimates while market consensus was slightly above 2% before Covid-19 panic intensified at the end of February.

But given the recent market turmoil and slowdown in the global economy, it is becoming clear that the Czech economy is likely to decelerate below 2% this year. OECD revised global economy growth downwards by 0.5 ppt and eurozone growth by 0.3 ppt this year.

As such, risks for Czech economy growth are also tilted to the downside, though figures will be gradually adjusted based on developments in the coronavirus outbreak and its damages to the global economy.

### Rate cuts expected by the market not likely

Markets are starting to expect rapid central banks reaction to support global economic growth, which has pushed the market to price in four rate cuts from the Czech central bank until the end of the year. However, we do not see such aggressive move as realistic given the specifics of CZK after the FX floor regime and its lack of sensitivity to interest-rate differentials abroad and the Bank's focus on inflation targeting.

*If the situation worsens further, some insurance rate cuts are imaginable in 2H20 but almost four cuts seem to be too aggressive and premature in our view.*

Even with global central banks delivering rate cuts, the Czech central bank does not need to follow in such an aggressive way as the koruna will not be appreciating as strongly due to monetary easing abroad. This was also the case in 2019 during Fed/ECB easing.

If the situation worsens further, some insurance rate cuts are imaginable in 2H20 but almost four cuts seem to be too aggressive and premature in our view.

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