

## Czech Republic: Central bank to stay on hold after front-loading cuts

We expect the Czech National Bank to stay on hold next Wednesday. The bank already delivered a larger cut vs the CNB's staff recommendation in May, particularly considering the falling interest rate trajectory in the second half of the year. This means that rates might stay unchanged next week, and potentially at future meetings as well



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The CNB will not publish new forecasts next Wednesday. It will only assess how the latest economic developments correspond to the May forecast. No significant deviation from the May forecast is apparent so far, which would suggest that the Czech economy is not tracking the CNB's adverse scenario and, as such, no more monetary easing is needed.

Indeed, 1Q20 GDP of -3.3% quarter-on-quarter (-2.0% YoY) was in line with the forecast, though the structure of growth differed, as the CNB expected a less intense fall in investments (-11.4% vs -5.4%) YoY and a more severe fall in foreign trade (-2.4% vs -5.8% YoY).

CPI decelerated at a slower pace and ended above the CNB's forecast in May (2.9% vs. 2.6%). Core inflation even accelerated from 2.7% to 3.3% in May due to a decline in taxes. These taxes are excluded from the CNB core inflation measure.

**0.25%** 2-week repo rate  
most likely unchanged next week

Wage growth of 5% YoY in 1Q20 was above the CNB forecast of 4.2%. Private sector wages in particular grew more than the central bank expected (5% vs 3.8%).

The Czech koruna has recently appreciated against the euro to below 26.7, stronger than the CNB's 2Q average forecast of 27.2. However, the average EUR/CZK in 2Q was at 27.1 up until now, so the deviation from the CNB forecast is negligible.

The CNB reduced its countercyclical capital buffer further from 1% to 0.5% yesterday. As such, these measures should not be a part of next week's meeting.

The CNB surprised at the last two meetings by delivering stronger-than-expected cuts. But this time an on-hold decision seems the most likely outcome. The latest CNB communications from Vojtech Benda, Marek Mora and Governor Jiri Rusnok all suggested that rates might stay on hold for some time, supporting no change next week.

The expected on-hold CNB decision should have a muted impact on the CZK as the market is pricing in a low probability of a cut and the latest CNB interest rate forecast also points to flat rates for the rest of the year.

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