

Czech Republic: Hawkish message delivered today

The Czech National Bank (CNB) delivered a hawkish message today. The new forecast projects 3-4 hikes this year, and further tightening via a stronger koruna. The hawkish message was delivered despite a relatively conservative GDP projection, seeing 2.2% growth this year



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New forecast expects 3-4 rate hikes this year

As we expected, the new CNB forecast continues to pencil in rates increases this year. Still, the new forecast is even more upbeat in terms of monetary tightening needed, as it shows a little more than 3 hikes this year (Pribor at 1.16% by 4Q21) and stronger CZK (EUR/CZK at 25.40 by 4Q21, which is an equivalent of 2 implicit hikes via FX compared to the current level of koruna). Clearly the hawkish FX and rates forecasts are based on a fairly conservative GDP forecast of 2.2% for 2021.

Conservative GDP forecast for 2021

The new CNB forecast was relatively close to the 4Q21 flash GDP figure (-5% YoY vs -5.4% in the CNB forecast) and as such it has not lost its relevance. Still, the 2021 CNB GDP outlook is relatively

conservative in our view, revised upwards to 2.2% only (from 1.7% in the November quarterly inflation report, which is below the market consensus of around 3% and our forecast of around 3.5%). The YoY GDP dynamics imply only a mild QoQ recovery in 2Q of 0.7% QoQ, and 1.2% QoQ in both quarters in 2H21. This suggests a clear potential to surprise on the upside if the epidemic situation improves.

New CNB forecast

Change in the CNB forecast

	new f'cast		old f'cast	
	2020	2021	2020	2021
GDP (% yoy, avg)	-5.8	2.2	-7.2	1.7
Inflation (% yoy, avg)	3.2	2.0	3.2	2.3
Inflation (% yoy, eop 4Q avg)	2.6	2.2	2.9	2.2
3M Pribor (% eop 4Q avg)	0.4	1.16	0.3	1.05
EUR/CZK (eop 4Q avg)	26.7	25.4	27.2	26.3

Source: CNB, ING

Note: avg = average, eop=end of period

Source: CNB, ING

Inflation sometimes below the 2% target this year

CPI outlook was revised downwards for this year from 2.3% to 2.0% and the CNB sees average CPI in 1Q and 3Q below the 2% target. In January and February, the CNB forecasts CPI at 1.7%. We note that despite the strong monetary tightening via higher rates and stronger CZK, the CNB CPI forecast for 2022 remains close to the target. This clearly implies significant pro-inflationary pressures that the CNB models identifies. As such, even if CPI surprises on the downside in some months this year, this should not derail the overall trend of the monetary policy normalisation – if the Covid situation allows – and the need to hike interest rates.

We expect two hikes in 2H21

We continue to expect two hikes in 2H21, most likely November and/or December. We can also envisage one 50bp hike if CNB decides to start rates normalisation. In our view, more tightening of the monetary conditions will be delivered via the FX-channel (vs rates) as hawkish CNB might push EUR/CZK closer to 25.00 this year.