

Czech Republic: The CNB delivered dovish hike as expected

The Czech National Bank delivered a 25bp hike as broadly expected by the market. While the CNB staff forecast still shows one more hike for 2019, Gov Rusnok clearly signalled no more hikes this year as a base case. Any further hike this year is only likely if there is a significant improvement in foreign developments. This does not seem very likely at this point



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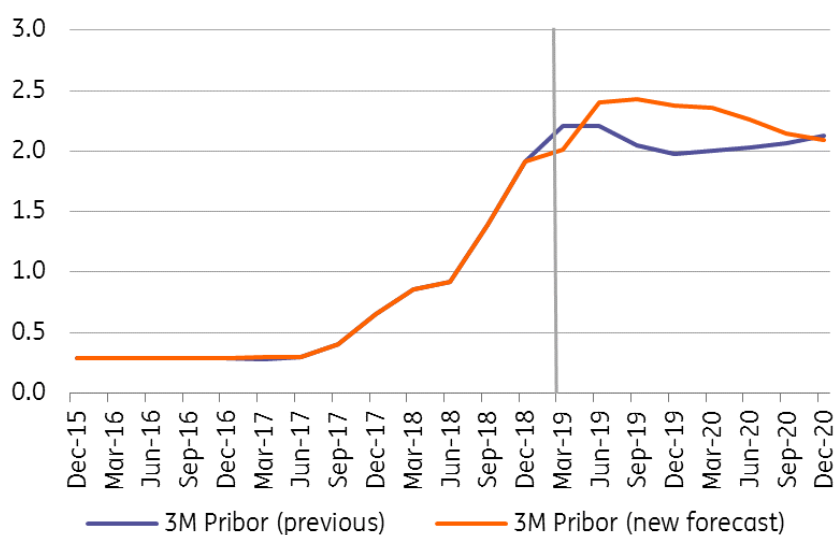
Here are some bullet points summarizing our view on today's CNB press conference:

- While the CNB delivered a unanimous hike today and 2-week repo get to 2%, the forward guidance points to the approaching end of the tightening cycle.
- Although the new CNB staff macroeconomic forecast indicates a possible rate hike this year (as 3M Pribor reaches 2.42% in 3Q19), **Governor Rusnok was clear that he expected stability of interest rates this year. As such, the CNB will stay on hold for some time, in**

our view. Any further hike this year is only likely if there is a significant improvement in foreign developments. This does not seem very likely at this point.

- We observe a non-negligible change in the CNB reaction function as the CNB staff forecast (for interest rates) now matters less and the expert judgement of the board members matters more. This is a significant shift from the 2016-2018 state of affairs.
- **GDP growth was revised downwards in the new forecast for this year and next** from 2.9% and 3% to 2.5% and 2.7%, respectively. On the other hand, average inflation was revised upwards from 2.2% and 2.0% to 2.6% and 2.1%, respectively. The CNB, as well as analysts, expects inflation to gradually slow from May onwards.
- **Koruna's exchange rate was revised towards weaker values in the new forecast**, and the CNB expects EUR/CZK 24.94 in 4Q19, while in the previous forecast it anticipated EUR/CZK 24.5 at the end of this year.
- **With the CNB likely reaching the end of the tightening cycle, the main factor holding the overbought CZK together (hawkish CNB) has now vanished.** Coupled with the slowing Czech economy and the maturing global economic cycle, we now see CZK upside as exhausted and look for a permanent trend in EUR/CZK higher, mainly from 2H19 onwards.

The CNB's 3M Pribor rate (%)



Source: CNB, ING