

## Czech: Central bank on hold amid global uncertainty

We expect the Czech National Bank to stay on hold on Thursday as the uncertain outlook for the global economy outweighs the weaker-than-expected Czech koruna and high core inflation. We see scope for two CNB hikes this year but the global economic outlook must improve first



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### More challenging global economy outlook

External headwinds appear to be driving the CNB's increasingly cautious bias, with the global environment still unclear. After soft real-data from the eurozone and Germany in the second half of last year (to some extent attributable to one off factors), this year's indicators have failed to bring any comfort to the central bank. German and China manufacturing PMIs have fallen below the 50-point threshold, signalling a contraction. Czech leading indicators have moved in a similar direction, with the January PMI hitting a six-year low and falling to 49.

## More cautious approach to monetary policy

Arguments supporting a more cautious approach to monetary tightening persist, as suggested by new board member and former CNB Chief Economist Tomas Holub two weeks ago. He suggested that while the softer currency argues for further rate hikes, the worsening global outlook, together with anti-inflationary oil prices, argue against such a move.

**1.75%** 2-week repo rate  
most likely unchanged on Thursday

## New forecast with weaker growth and inflation

The new CNB staff forecast should see downward revisions to GDP for 2019 and 2020, to below 3% from 3.3% in November. A tight labour market and solid wage growth suggest the new inflation report will forecast further inflationary pressures this year in terms of core inflation.

## CPI at 2% target due to supply factors

The recent deceleration in Czech CPI to 2% was mainly due to food and fuel prices. Importantly, December core inflation, as defined by the CNB, accelerated further to 2.6% year-on-year, as did prices of services (3.4%), up 3% YoY for the whole of 2018. Core inflation growth should remain strong this year, though headline inflation will be revised downwards from 2.6% towards 2.1% due to oil price developments.

## Thursday on hold, hikes to come later this year if global outlook improves

With an uncertain global environment and headline CPI on target, the CNB should stay on hold this week (though further implicit tightening is likely in the new forecast). We see scope for two CNB hikes this year but an improvement in the global economic outlook is now a necessary condition for further CNB tightening.