

## Weekly | 2018 | Week 35

MARTIN LOBOTKA, (+420) 777 027 165, [MLobotka@42fs.com](mailto:MLobotka@42fs.com), [Research@42fs.com](mailto:Research@42fs.com)

## CALENDAR

DAY	DATE	TIME (CET)*	MARKET	RELEASE	CONSENSUS**	42FS
Monday	3-Sep-18	9:30	CZ	Manufacturing PMI, Aug'18	55.1	N/A
	3-Sep-18	10:00	EMU	(Final) Manufacturing PMI, Aug'18	54.6	N/A
Tuesday	4-Sep-18	9:00	CZ	Average Real Monthly Wage, 2Q18, y/y	6.0%	5.7%
Wednesday	5-Sep-18	9:00	CZ	Retail sales, Jul'18, y/y	5.7%	4.9%
	5-Sep-18	10:00	EMU	(Final) Services PMI, Aug'18	54.4	N/A
	5-Sep-18	11:00	EMU	Retail Sales, Jul'18, y/y	1.3%	N/A
Thursday	6-Sep-18	8:00	GER	Factory Orders, Jul'18, y/y (WDA)	1.9%	N/A
	6-Sep-18	9:00	CZ	Industrial production, Jul'18, y/y	7.8%	6.8%
	6-Sep-18	9:00	CZ	Trade Balance, Jul'18, CZK bn.	-5.0	2.0
Friday	7-Sep-18	8:00	GER	Industrial production, Jul'18, y/y (WDA)	2.5%	N/A
	7-Sep-18	8:45	FRA	Industrial production, Jul'18, y/y (WDA)	0.9%	N/A
	7-Sep-18	9:00	SPA	Industrial production, Jul'18, y/y (WDA)	1.6%	N/A
	7-Sep-18	11:00	EMU	(Final) GDP 2Q18, q/q (SA)	0.4%	N/A

\* LOCAL TIME IS CET

\*\* (REUTERS/ BLOOMBERG) POLL

## SEPTEMBER 2018 AUCTIONS

NAME	DATE OF AUCTION	DATE OF ISSUE	MATURES ON	AMOUNT OFFERED*	COUPON
CZGB 2007-2022**	5-Sep-18	7-Sep-18	12-Sep-22	CZK 3 bn. max	4.70%
CZGB 2018-2029**	5-Sep-18	7-Sep-18	23-Jul-29	CZK 5 bn. max	2.75%
SPP 800	13-Sep-18	14-Sep-18	14-Dec-18	CZK 0-5 bn.	N/A
SPP 801	20-Sep-18	21-Sep-18	21-Dec-18	CZK 0-5 bn.	N/A
CZGB 2018-2021**	19-Sep-18	21-Sep-18	23-Feb-21	CZK 3 bn. max	0.75%
CZGB 2014-2025**	19-Sep-18	21-Sep-18	17-Sep-25	CZK 3 bn. max	2.40%

\* FOR T-BILLS, THIS IS MAXIMUM AMOUNT PER PRIMARY DEALER.

\*\* MINFIN CAN CHANGE THE ISSUE AT THE LATEST AT THE DAY OF THE AUCTION ANNOUNCEMENT FOR ONE WITH SIMILAR MATURITY.

## THOUGHT OF THE WEEK

"I'M CONVINCED THAT IN HELL, THE ONLY INSTRUMENT YOU CAN TRADE IS EUR/SEK".

## WEEK AHEAD

Whole array of July monthly data will be released here.

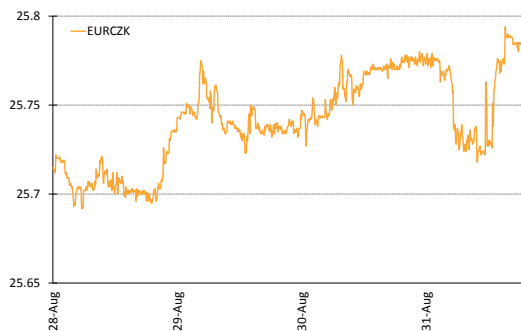
Czech retail sales and industrial production will both be affected by one more working day in July 2018 as against July 2017, and I think there should be a negative monthly growth reported for the production as a correction to surprisingly strong May and June growth numbers. Average real wage should show about 8% y/y nominal growth in 2Q18, again mostly due to rising wages in the public sector.

In Eurozone, most important are the German industrial data – orders and production. The former fell 4% in June, so some rebound is in order. Eurozone July retail sales will be reported to have remained very weak, further strengthening the case for ECB's long period of inactivity.

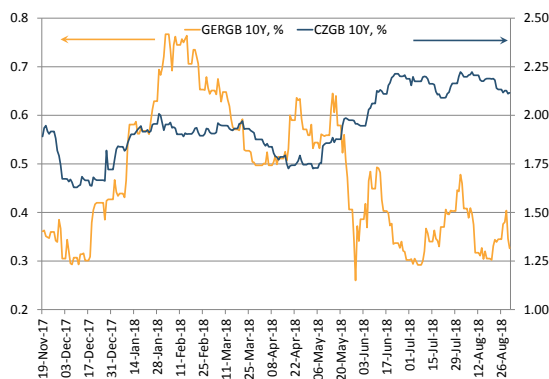
WEEK BEHIND

- CZ: 2Q18 GDP growth revised up ▶
- GER: IFO index improves, but this unlikely to be the beginning of the trend... ▶
- EMU: Consumer confidence slips to lowest this year ▶
- EMU: Unemployment rate stays at 8.2% ▶ while core inflation remains at 1% ▶

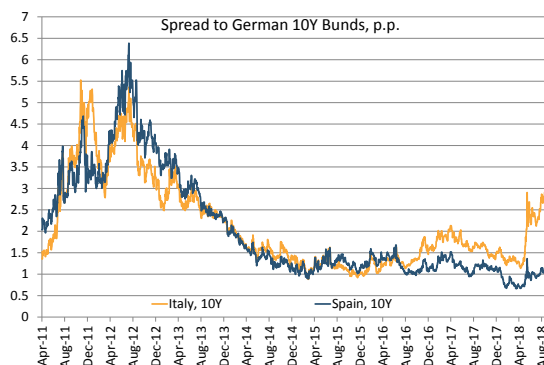
EURCZK IN A TIGHT RANGE CENTERED ON 25.75



GERMAN BUND YIELDS FELL IN THE 2ND HALF OF THE WEEK...



...AS ITALY GOT UNDER SELLING PRESSURE AGAIN.



FX

CZK remained in a tight range centered at 25.750.

FI

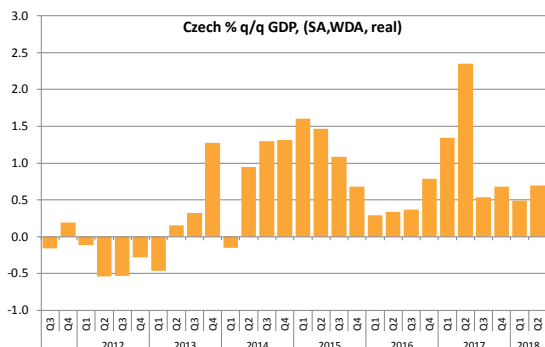
Up and down in Germany.

German 10Y yields first rose towards 40 bps. as surprisingly strong IFO reading came in and as trade fears eased with USA and Mexico reaching an agreement on NAFTA revision.

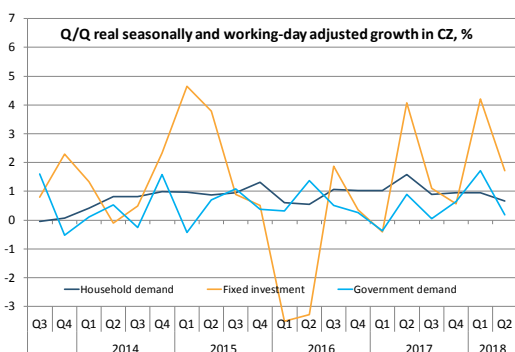
Thereafter, in the second half of the week and against the backdrop of low August Eurozone inflation, the renewed sell-off in Italy led to return of German yields back down to 30 bps. This also led to the widening of GER-ITA 10Y spread to widest in almost 5 years (290 bps.). If this keeps going on, let alone escalates, ECB's gonna have a hard time really pulling the plug on asset purchases come December.

**CZECH ECONOMY**

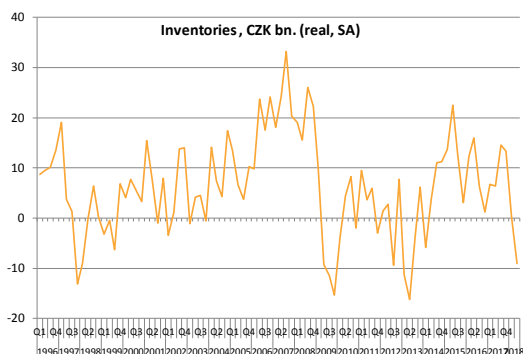
**GROWTH REVISED UP TO 0.7% Q/Q**



**AGGREGATE DEMAND SLOWED IN 2Q18,...**



**...BUT THE FALL OF INVENTORIES IS GOOD NEWS FOR 2H18.**



**2<sup>nd</sup> estimate of GDP growth was revised up, bringing it closer to what Hungary and Poland growth was in 2Q18.**

Up from first estimate of 0.5% q/q, the second estimate has the Czech growth at 0.7% q/q in 2Q18, slightly below the ≈ 1% quarterly growth of Poland, Hungary in the same quarter. Annual growth slowed from 4.1% in 1Q18 to 2.4% y/y in 2Q18 and, based on the growth in the first half, the economy appears to have definitely settled into the annualized growth rate of 2.5%.

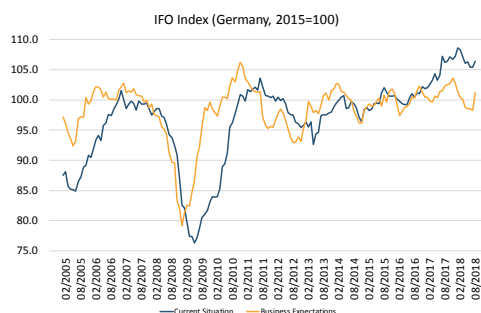
**Structure wasn't too surprising. Household demand growth slowed to 0.7% q/q, the slowest rate of growth in two years, likely the reflection of full labor market, rock-bottom savings rate, increased inflation (=lower real wage growth). Growth of fixed investments slowed as well, but remained at very respectable at 1.7% q/q, still among the fastest rates of growth in last four years and above the average rate of growth (1.1% q/q) in that period. However, with monetary policy getting tighter and profitability of firms compromised by wage growth, this is likely to slow down further.**

Slower growth of aggregate demand resulted in less imports and hence **positive contribution of next exports to quarterly growth** – exports added 0.6 pp, imports another 0.2 pp to the growth.

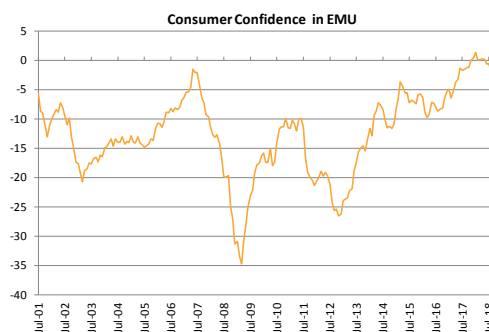
**The most positive piece of news in the Friday released were inventories. See, they fell 9 bn., most in five years, but this suggests that the rebuild of them in 2H18 will turn them into growth support. It will not be anything large, but should provide some boost going forward.**

All in all, despite the slightly quicker growth in 2Q18 than originally estimated, **the economy has clearly settled into the 2.5% annualized growth rate.** That is somewhat under the potential output growth, i.e. the inflationary implications of 2Q18 release aren't anything important. That said, with

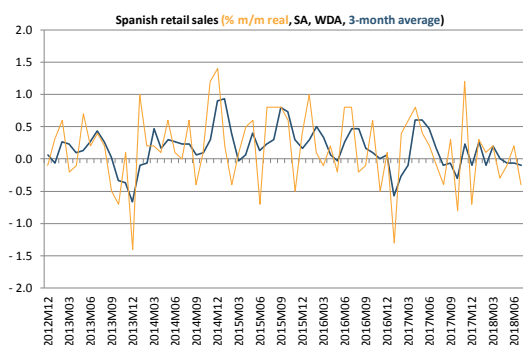
**GERMAN IFO IMPROVES ON IMPROVEMENT OF EXPECTATIONS**



**CONSUMER CONFIDENCE WORSENS IN AUGUST**



**SPANISH RETAIL SALES SUGGEST EURO AREA RETAIL REMAINED WEAK MIDWAY THROUGH 3Q18**



real estate prices off the chart and CZK weaker, CNB is likely to tighten again this year.

**EUROZONE ECONOMY**

**German IFO improved for the first time since January while European consumers grew less optimistic.**

**IFO index, having worsened previously to lowest in a year, rebounded in August, especially in its expectations' component.** The jump of 3 points from July's 98.2 pushed the expectations to highest since January, and also took the overall index up one point from July's 105.4 pts. **The improvement in expectations was due to relative calm in US-EU trade relations after Juncker's visit to Washington.** This, I am afraid, though, was just a reprieve – with elections in US and Trump in need of stirring up its base, we're certainly in for more foreign trade-related bellicosity from US president. Weak German PMI and the fall in June industrial orders suggest industry soft patch shall continue for some time still.

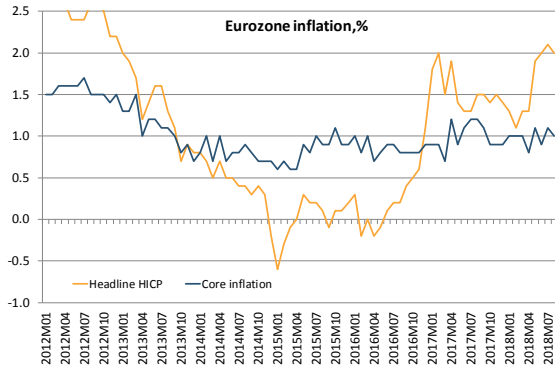
In August, less optimism was seen among Euro area consumers. Their **confidence slipped to lowest in a year in August**, and although it remained still very high by historical standards, it's clear it's been trending downward continuously this year.

This makes quickening of retail sales growth, anemic in last months, unlikely: the first glimpse at August data, from Spain, seems to confirm that. **Spanish retail sales fell 0.4% m/m in July, falling in the quarter of July-June-May, and making for the negative annual growth of 0.4% y/y.** Nothing there to scare the ECB...

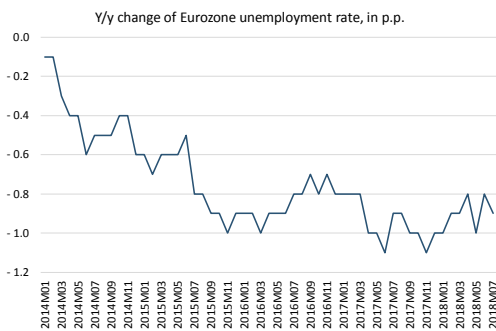
**....as there is nothing in the recent unemployment and inflation data.**

**August preliminary core inflation** returned to 1% from July's 1.1%, i.e. close to where it's been in last five years on average, while headline inflation returned to 2% from July's 2.1%. The biggest

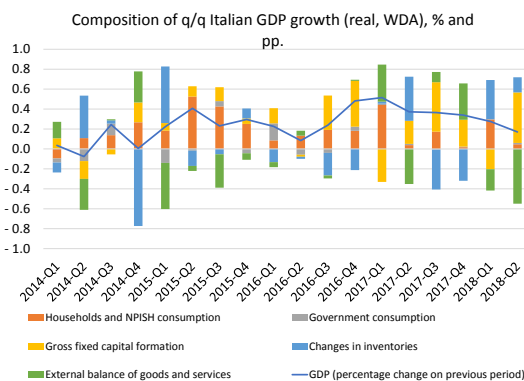
**CORE INFLATION REMAINED SUBDUED IN EUROZONE IN AUGUST AND...**



**...RATE OF UNEMPLOYMENT IMPROVEMENT SUGGEST THIS WILL THE CASE IN THE FORESEEABLE FUTURE AS WELL.**



**ITALIAN, FRENCH GDP CONFIRMED WEAK IN 2Q18**



annual contributor to the recent rise of headline is still the energy prices (+9.2% y/y in August vs. July 9.5%). As far as core inflation is concerned, it is still the same message: no threat of deflation, but no threat of demand pressures either.

And the evolution of the unemployment rate doesn't suggest any of this will change in next year or so: unemployment rate (8.2% in July, just like in May and June) will at this rate of improvement (-0.9 pp/year) take three year to get to the NAIRU, and even once it gets to that level there is no guarantee that wage growth accelerates immediately thereafter, a necessary condition for core inflation acceleration. I mean, look at Germany or US where labor market's been tight for years now, with little inflation pressures evident.

**French and Italian GDP growth rate were confirmed at 0.2% q/q in 2Q18.**

For France, 2Q18 was thus as weak as 1Q18, for Italy it was 0.1 pp weaker.

**Structure-wise, no surprises in France** as this was already 2nd estimate and France is in habit of releasing structural data right away (i.e., in the 1<sup>st</sup> one): household demand fell 0.1% q/q, fixed investments rose 0.8% q/q, making the total contribution of domestic demand to quarterly growth identical to that in the 1Q18: 0.2 pp. Net exports were a drag due to strong rebound of imports (+1% q/q).

**Italian growth** also doesn't show a) it should quicken soon and b) any inflationary signs. The biggest contributor were fixed investments (+0.5% q/q) while contribution of household demand was zero.

Put together, nothing that should worry ECB. Ehm, inflation-wise, I meant. Italian bond market is another story...





MARKETS ‡

MM / IRS		3M PRIBOR	6M PRIBOR	2Y	5Y	7Y	10Y	
%	Actual	1.490	1.600	2.045	2.218	2.246	2.290	
	-1M	1.220	1.300	1.875	2.155	2.170	2.205	
	-3M	0.910	0.990	1.330	1.680	1.765	1.860	
	-6M	0.910	0.990	1.300	1.700	1.795	1.920	
ASW spread*		2Y	3Y	4Y	5Y	7Y	10Y	
bps.	Actual	-0.726	-0.814	-0.700	-0.527	-0.274	-0.174	
	-1M	-0.636	-0.733	-0.630	-0.437	-0.209	-0.005	
	-3M	-0.467	-0.535	-0.416	-0.292	-0.076	0.091	
	-6M	-0.795	-0.702	-0.680	-0.646	-0.507	0.010	
CZGB**		2Y	3Y	4Y	5Y	7Y	10Y	
%	Actual	1.319	1.320	1.483	1.691	1.972	2.116	
	-1M	1.239	1.285	1.477	1.718	1.961	2.200	
	-3M	0.863	0.957	1.188	1.388	1.689	1.951	
	-6M	0.505	0.783	0.935	1.054	1.288	1.930	
FX		EURCZK	EURPLN	EURHUF	EURRON	EURTRY	EURUSD	
	Actual	25.774	4.302	326.60	4.635	7.614	1.161	
	-1M	25.578	4.276	320.74	4.622	5.746	1.169	
	-3M	25.826	4.316	319.67	4.662	5.297	1.169	
	-6M	25.410	4.176	313.87	4.657	4.633	1.219	

‡ As of Sunday night  
 \* Spreads to generic bonds  
 \*\* Generic bond

CONTACTS

MARTIN LOBOTKA, ANALYST

(+420) 777 027 165, [MLobotka@42fs.com](mailto:MLobotka@42fs.com)

RESEARCH

[Research@42fs.com](mailto:Research@42fs.com)

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