

Czechia Watch: CNB did not change rates, but there were more votes for a hike

The CNB did not surprise with its decision and, as expected, decided to keep rates stable for the seventh time in a row. However, what was surprising was the ratio of votes, with three bank board members raising their hand for a 25bp hike.

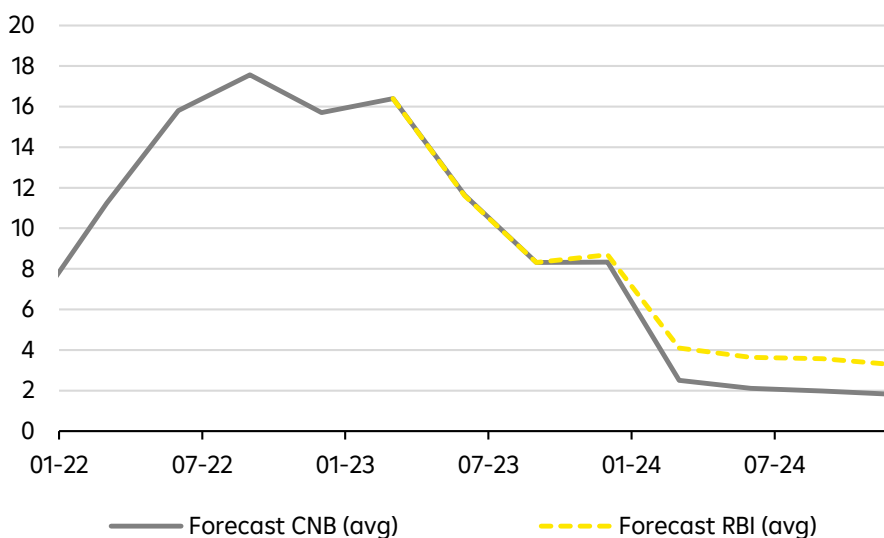


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The number of votes for the hike unexpectedly increased

Speculation about a possible hike at the May meeting proved partly justified, with **rate stability voted through by the smallest possible majority of 4 votes**. At the previous meeting, only one of the seven members voted for a hike, six for the stability. On the basis of comments made in the previous weeks, we can guess that at least one of the two newcomers to the bank board (Kubíček and Procházka – second meeting for them), in addition to board member Holub, raised their hand in favour of a rate hike. However, in the past, deputy governors Zamrazilová and Frait have also spoken in favour of a possible hike. The answer to this uncertainty will be revealed only next week by the minutes from the meeting. **The likely reason for the more hawkish stance is loose fiscal policy together with uncertain wage development.**

This year's inflation forecast has shifted towards ours, but we expect higher inflation next year
CPI yoy, in %



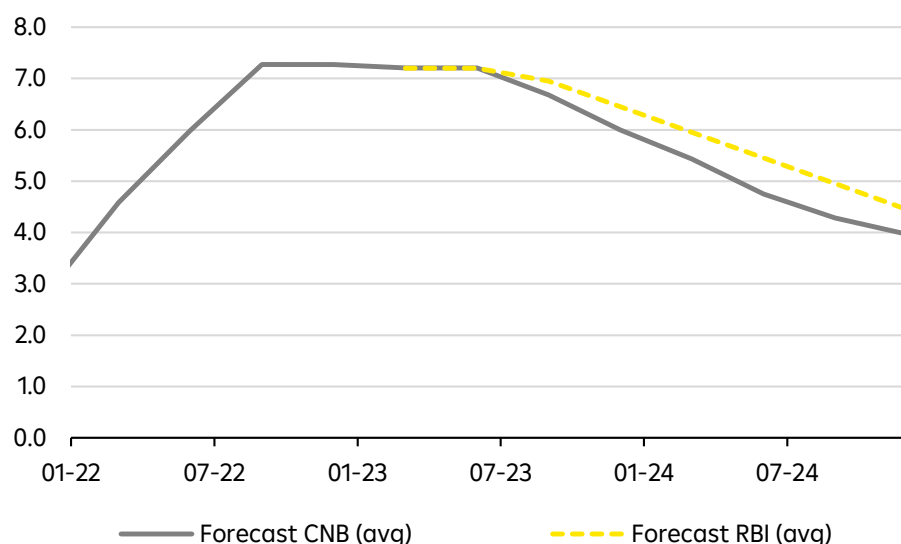
Source: CNB, Macrobond, Raiffeisen Research/RBI

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New forecast assumes higher growth but also higher inflation

The new CNB's spring forecast shifts **GDP growth expectations** significantly towards our estimate. The CNB previously forecasted a 0.3% decline this year, but now expects 0.5 % growth (our estimate = +0.9%). **In the case of inflation**, there has been a slight upward shift in the context of this year, from 10.8% to 11.2% (our est. = 11.3%), but we see the main uncertainty in the CNB's outlook for next year, with the central bank expecting inflation to average at 2.1% (our est. = 3.7%). The **forecast in relation to interest rates** has undergone an expected adjustment, where the projection does not foresee further hikes, but instead a lowering of interest rates in Q3'23. However, Governor Michl tempered these expectations at the press conference, calling market expectations (a cut at the turn of Q3 and Q4'23 at the time of the press conference) premature. **For the koruna**, the CNB expects a gradual depreciation from current levels, with the exchange rate expected to be around 24.0 EUR/CZK by the end of the year. The forecast sees further depreciation beyond 24.50 EUR/CZK in 2024.

New forecast opens room for cuts, but Governor Michl hinted at a slower pace 3M interbank rate, in %



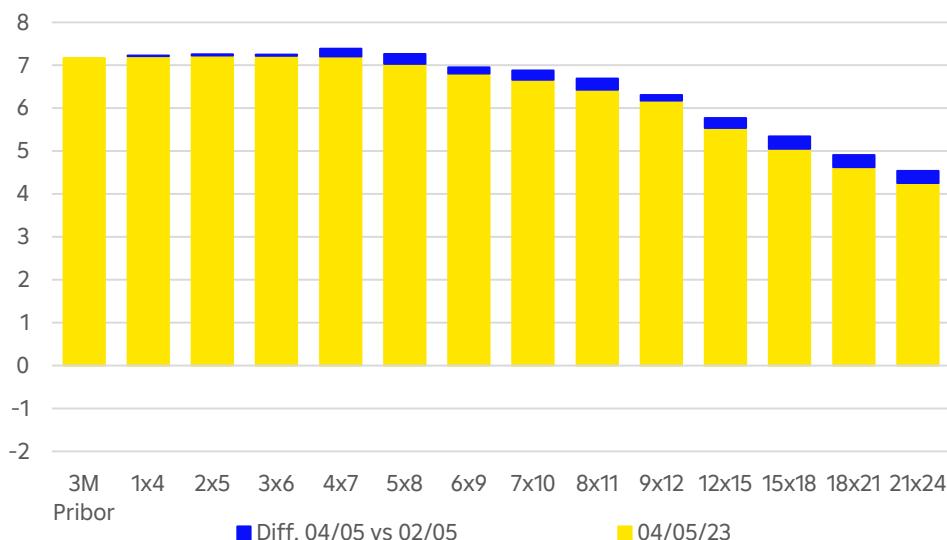
Source: CNB, Macrobond, Raiffeisen Research/RBI

After the press conference, the market lowered its expectations for the pace of this year's cuts

As a result, the meeting on Wednesday did not bring an immediate change, but **the growing number of votes for a rate hike caught the market by surprise**. This was immediately reflected in the development of the koruna, which appreciated slightly to 23.50 EUR/CZK after the vote ratio was mentioned at the press conference. **There was also a shift in market expectations regarding the level of rates by the end of this year**. Before yesterday's meeting, the market had expected rates to fall by 60 basis points by the end of 2023. Now it is expected that rates will fall by only 40bps, and the market is not completely ruling out a hike in the next few months.

Market expectations moved higher after the press conference

FRA curve, in %



Source: Bloomberg, Raiffeisen Research/RBI

We expect rate stability in June, but a hike cannot be ruled out

Compared to our forecast, which assumes cuts from Q3'23 to 6.00% by the end of this year, the current developments represent a significant risk in the direction of a longer-taking stability, and **we are therefore putting our forecast under the revision**. The CNB's decision at the June meeting will depend significantly on the Q1'23 wage data (published on June 5) and also government's approach to state budget consolidation. Currently, we see rate stability as a more likely option. However, if wage growth surprises to the upside significantly and the government does not present clearer outlines for reducing the government deficit, **a 25bps rate June hike by the CNB is possible**.

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CZ	07.06.2022	Not rated	Czech Republic

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