NÁRODNÁ BANKA SLOVENSKA
EUROSYSTÉM

Report on the International Economy

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Abbreviations

CPI	Consumer Price Index
EA	euro area
ECB	European Central Bank
EC	European Commission
EIA	Energy Information Administration
EMU	Economic and Monetary Union
EONIA	euro overnight index average
ESA 95	European System of National Accounts 1995
EU	European Union
Eurostat	Statistical Office of the European Communities
FDI	foreign direct investment
Fed	Federal Reserve System
EMU	Economic and Monetary Union
EURIBOR	euro interbank offered rate
FNM	Fond národného majetku – National Property Fund
GDP	gross domestic product
GNDI	gross national disposable income
GNI	gross national income
HICP	Harmonised Index of Consumer Prices
IMF	International Monetary Fund
IPI	industrial production index
IRF	initial rate fixation
MFI	monetary financial institutions
MF SR	Ministry of Finance of the Slovak Republic
MMF	money market fund
NARKS	National Association of Real Estate Offices of Slovakia
NBS	Národná banka Slovenska
NEER	nominal effective exchange rate
NPISHs	Non-profit Institutions serving households
OIF	open-end investment fund
p.a.	per annum
p.p.	percentage points
qoq	quarter-on-quarter
PPI	Producer Price Index
REER	real effective exchange rate
SASS	Slovenská asociácia správcovských spoločností – Slovak Association of Asset Management Companies
SO SR	Statistical Office of the Slovak Republic
SR	Slovenská republika – Slovak Republic
ULC	unit labour costs
VAT	value-added tax
yoy	year-on-year

Symbols used in the tables
. – Data are not yet available.
- – Data do not exist / data are not applicable.
(p) – Preliminary data

1 The global economy

Global economic growth slowed moderately in the fourth quarter of 2016, as stable growth across advanced economies was accompanied by weaker growth in certain emerging economies. Despite its slowdown in the last quarter, global economic activity accelerated over the whole of the second half of 2016. Current indicators show that this trend was maintained at the beginning of 2017. Looking ahead, the world economy will be affected by the new US administration's fiscal stimulus policies, by the normalisation of US monetary policy and its implications for emerging economies, and by the resetting of future relations between the United Kingdom and the European Union. Other factors that will shape the direction of the world economy include the impact of commodity prices on global exporters and the ongoing rebalancing of the Chinese economy.

The UK economy maintained surprisingly solid growth after the country voted in June 2016 to leave the EU. Its growth rate at the end of the year was the highest among advanced economies, and was driven mainly by continuing stable growth in private consumption and a pick-up in export performance. In the medium term, however, the UK's GDP growth is expected to slow owing to depreciation of the pound sterling and its downward impact on real income and private consumption, as well as to a weakening of investment. The euro area economy maintained the same pace of growth in the fourth quarter of 2016 as in the previous quarter, reflecting growth in private and government consumption, as well as increasing investment demand. On the other hand, net trade made a negative contribution as the acceleration in export growth was accompanied by stronger growth in imports. Going forward, domestic demand is expected to continue benefiting from the ECB's accommodative monetary policy, while export activity should be boosted by the pick-up in global trade and by the lagged impact of past euro exchange rate depreciation. In the United States, economic growth slowed in the fourth quarter as the upturn in export growth observed in the third quarter was not maintained. This slowdown weighed on global economic growth. The upward impact of improving labour market conditions on wage growth, as well as rising trends in property prices and share prices, are expected to buoy real disposable income and consumption in the period ahead. Investment demand is expected to be boosted by higher oil prices. Japan's economy maintained its decelerating trend in the fourth quarter of 2016. Its growth was based almost entirely on net trade, with consumption and investment making only marginal contributions. The figures were also affected, however, by the adoption of a new methodology for national accounts and the resulting revisions of historical data. Fiscal and monetary policy stimuli are expected to continuing having a positive impact on the Japanese economy.

In China, economic growth slowed towards the end of the year but remained relatively strong. Its growth was driven mainly by increases in private investment and consumption. GDP growth in China is projected to follow a gradual downward path in coming years, depending on what steps the government takes to rebalance the economy. India's economic growth was moderately more subdued in the fourth quarter. It may have been negatively affected by the withdrawal of the highest-denomination banknotes from circulation and the adverse impact of that measure on consumption. Overall, however, India's GDP growth remained robust, thanks to wage increases in the agricultural and public sectors and to government expenditure. As a result of structural reforms, particularly in the area of goods and services taxation, investment is expected to increase gradually. The Brazilian economy, weakened by high unemployment and low levels of business and consumer confidence, contracted further in the fourth quarter than in the previous quarter. According to available indicators, however, the recession is expected to ease, as domestic demand is boosted by improved financial and business conditions. In addition, a more marked fall in the inflation rate put downward pressure on inflation expectations, bringing them into line with the central bank's target. The Russian economy improved in the last quarter of 2016 and is gradually emerging from a deep recession. Nevertheless, several indicators are sending mixed signals about the economy. While industrial production rallied on the back of rising oil prices and appreciation of the rouble, the continuing decline in retail trade indicates weak consumer demand. Uncertainty about the future is persisting in the context of a fiscal policy that may weigh on the Russian economy and since a combination of structural reforms and insufficient fixed investment is undermining the economy's supply capacity.

GDP growth in the OECD area slowed in the fourth quarter of 2016 to 0.4%, quarter on quarter, from 0.5% in the previous quarter. The year-on-year growth rate remained unchanged, at 1.7%. Although global economic growth moderated slightly at the end of 2016, the Composite Leading Indicator (CLI) for the OECD area[1] points to a gradual recovery. The CLI maintained its upward trend in the fourth quarter of 2016 and at the beginning of 2017.

Global activity growth is expected to accelerate slightly in the period ahead. The US economy

Chart 1 GDP growth and the CLI for the OECD area

Source: OECD.
Note: CLI – Composite Leading Indicator.

is expected to benefit from accommodative financial conditions, favourable labour market developments, high confidence levels, and fiscal stimulus policies. At the same time, however, investment and economic growth in the United Kingdom may be adversely affected in the medium term by the uncertainty surrounding the country's future trade relations with the EU. Japan's economic growth is likely to remain subdued despite the impact of monetary and fiscal stimuli. As regards economic activity trends across emerging economies, they are expected to be heterogeneous. China's GDP growth will continue to moderate, while India and the countries emerging from deep recession are envisaged to support global growth.

The upturn in the annual inflation rate for energy commodities quickly passed through to global inflation. Energy prices began increasing in the fourth quarter of 2016 for the first time in more than two years and contributed significantly to the acceleration in consumer prices. Food inflation gradually emerged from negative territory, but did not yet show any substantial response to the stronger increase in food commodity prices. Annual inflation in the OECD area climbed to 1.8% in December 2016, up from 1.2% in September. Core inflation did not contribute to the increase in the headline rate, since despite falling earlier in the fourth quarter, it ended the year back at its September level (1.8%). Consumer price inflation increased further in January 2017, to 2.3%, reflecting the acceleration in energy inflation. At the same time, inflation excluding energy and food also increased (to 1.9%) and so, to a lesser extent, did food inflation.

Looking ahead, global inflation is projected to moderate. In the near term, prices of oil and other commodities should contribute positively to the headline rate. In the medium term, a gradual reduction in spare capacity at the global level may support inflation. Given the relative stability in oil futures prices, energy prices are not expected to have a significant impact on global growth.

1 *The CLIs for OECD countries are published on a monthly basis, and the most recent, published in March 2017, are for the period up to January 2017.*

2 Commodities

The quarter-on-quarter increase in the commodity price index was higher in the fourth quarter of 2016 than in the third quarter. Energy commodity prices accounted for most of that acceleration, and non-energy commodity prices also made a positive contribution. Overall in 2016, the commodity price index increased by 26%, including increases of 44% in the oil component, 34% in metals, and 7% in agricultural commodities.

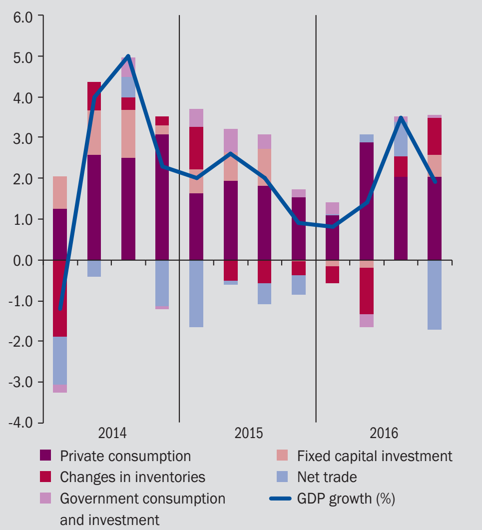
Oil prices increased more than the prices of any other energy commodities in the fourth quarter of 2016, with the average price of a barrel of Brent crude oil rising to USD 50, around USD 4 higher than in the previous quarter. The oil price climbed at the end of November when OPEC decided to cut oil production, and was further boosted in December when Russia and other non-OPEC producers also committed themselves to cutting production. As for demand-side effects on the oil price, the International Energy Agency (IEA) projects that oil demand growth will diminish in 2017 due to the slowdown of economic growth in China and India, which together account for around one-quarter of total global demand. Looking at other energy commodities, natural gas prices climbed at the end of 2016 as a result of cold weather. Coal prices maintained their strong upward trend, reflecting the softening of supply caused by industrial rebalancing in China and reduced coal production in Australia. The rate of increase in the non-energy commodity price was higher in the fourth quarter owing mainly to metal prices. Marked increases in prices of iron ore and copper reflected demand from the Chinese construction sector, and were also partly a reaction to the US presidential election results and to infrastructure spending plans announced by the incoming US administration. The agricultural commodities price index fell again in the fourth quarter of 2016 and thus had a negative impact on the overall commodity price index. The agricultural commodity prices that fell the most were the prices of pork, cocoa and rice. The upward trend in the overall commodity price index continued in January, reflecting positive contributions from both the energy and non-energy components.

3 The United States

In the United States, the annualised rate of economic growth moderated in the fourth quarter of 2016 in line with expectations, falling to 1.9% (from 3.5% in the previous quarter). Nevertheless, the growth rate for the second half of the year was higher than that for the first six months, and leading indicators point to a further acceleration of growth at the beginning of 2017. The year-on-year GDP growth rate increased from 1.7% in the third quarter to 1.9% in the fourth quarter.

The slowdown in the annual pace of the US economy's growth in the last quarter of 2016 reflected the base effect of higher than usual export growth in the third quarter (caused by a spike in soya exports to China[2]). As the impact of this one-off factor faded and as import growth increased, net trade made a significantly negative contribution to overall GDP growth in the fourth quarter. Its downward impact was partly offset by the positive contribution of inventories. Private consumption growth remained unchanged from the previous quarter and, together with growth in real disposable income, the continuation of favourable labour market trends, and the prospect of income tax reductions, will support activity growth going forward. Investment demand picked up in the fourth quarter after falling or stagnating in the previous four quarters. Its growth was driven entirely by residential investment, which in contrast to the previous quarter recorded growth acceleration. As for non-residential investment, its growth rate remained largely unchanged, with investment in equipment increasing for the first time in over a year and structural investment declining. Government consumption and investment increased only slightly in the fourth quarter and therefore had no more than a marginal impact on US GDP growth. In the short term, the US economy is expected to be supported by fiscal stimuli, while in the medium term its growth may be inhibited by the implementation of protectionist policies.

Chart 2 Annualised GDP growth and its composition (percentages; percentage point contributions)

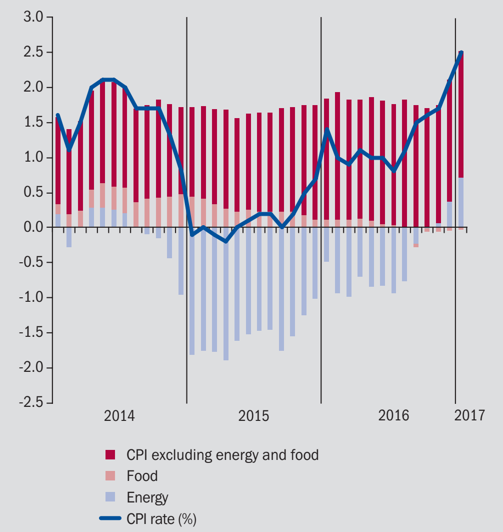


Source: Bureau of Economic Analysis.

Upward price pressures in the United States gained momentum in the fourth quarter, with annual consumer price inflation climbing from 1.5% in September 2016 to 2.1% in December. Energy inflation turned positive for the first time in two years, reflecting the rapid pass-through of increases in energy commodity prices. Energy price movements were also the main accelerator of the headline inflation rates, given that food inflation remained slightly negative and core inflation slowed somewhat. Energy inflation picked up significantly in December and even more rapidly in January. Its January rate was twice as high as the December rate, reaching a five-year high of 2.5% year on year. Inflation excluding energy also contributed positively to the headline rate in December and January, after showing a downward trend in previous months. In December this component rebounded to 2.2% – the rate recorded in September – and in January it edged up further, to 2.3%. Food inflation remained slightly negative. Looking ahead, consumer price inflation may be pushed further upward by wage growth acceleration and the impact of significant fiscal stimuli.

2 *US exporters met the demand resulting from poor harvests in South America.*

Chart 3 Annual consumer price inflation and its composition (percentages; percentage point contributions)



Sources: Bureau of Labor Statistics and NBS calculations.

The US Federal Open Market Committee (FOMC) decided at its meeting in November 2016 to leave the target range for the federal funds rate unchanged at 0.25% to 0.50%. The Committee judged that the case for an increase in the federal funds rate had continued to strengthen but decided to wait for some further evidence of continued progress toward its objectives. In view of realised and expected labour market conditions and inflation, the Committee decided in December 2016 to raise the target range for the federal funds rate to 0.50% to 0.75%. The Committee decided at its January/February 2017 meeting to maintain the target range at its December level. According to the FOMC, the stance of monetary policy remains accommodative, thereby supporting further improvement in labour market conditions and a return to 2 per cent inflation.

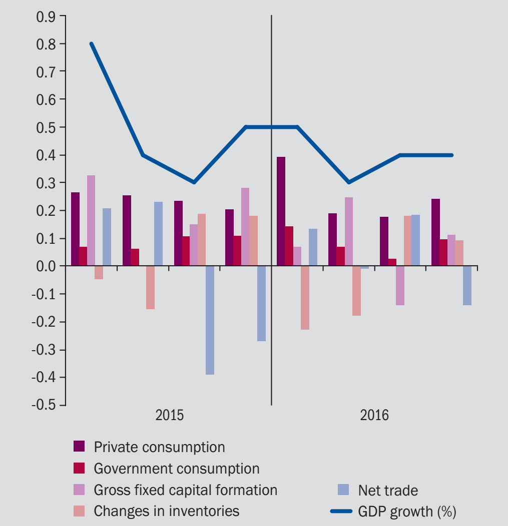
4 The euro area

The euro area economy grew, quarter on quarter, at the same pace in the fourth quarter of 2016 as in the previous quarter[3]. Looking at the larger economies within the euro area, growth accelerated in Germany (from 0.1% to 0.4%) and France (from 0.2% to 0.4%), remained at the same relatively high level in Spain (at 0.7%), and moderated in Italy (from 0.3% to 0.2%) and the Netherlands (from 0.8% to 0.5%). In year-on-year terms, euro area GDP growth edged down in the fourth quarter, to 1.7%, 0.1 percentage point lower compared with the previous quarter.

Domestic demand continued to be the main driver of economic expansion. Private consumption made the largest positive contribution, with its growth rate increasing moderately in the fourth quarter (by 0.1 percentage point, to 0.4%). Thus the upward trend in consumer demand was extended to almost three years. Public consumption growth accelerated (from 0.1% to 0.4%) and therefore also had a positive impact on economic growth. So too did gross fixed capital formation, which after declining by 0.7% in the third quarter, increased by 0.6% in the fourth quarter. Looking at short-term indicators in the fourth quarter, it appears that output growth in sectors concerned with fixed investment (construction, capital goods production) remained relatively solid and may imply further strengthening of investment demand. The impact of changes in inventories on activity growth in the fourth quarter was also positive, albeit less so compared with the previous quarter. In contrast to its positive impact in the third quarter, net trade contributed negatively to GDP growth since import growth (2.0%) was notably higher than export growth (1.5%). Nevertheless, exports recorded their highest growth since the fourth quarter of 2014.

After increasing for three consecutive quarters, the saving ratio fell in the third quarter of 2016. Although the decline was only slight, it may indicate a certain response to the significant reduction in interest rates. The conditions are thus being created for private consumption to continue growing in 2017. Its growth may, however, be curbed to some extent by the upward path of headline inflation and consequent impact on gross disposable income growth. This may also temper consumer confidence, which in February declined after increasing in the previous five months. On the other hand, the continuing improvement in labour market conditions is expected to support consumer demand.

Chart 5 Quarterly GDP growth and its composition (percentages; percentage point contributions)



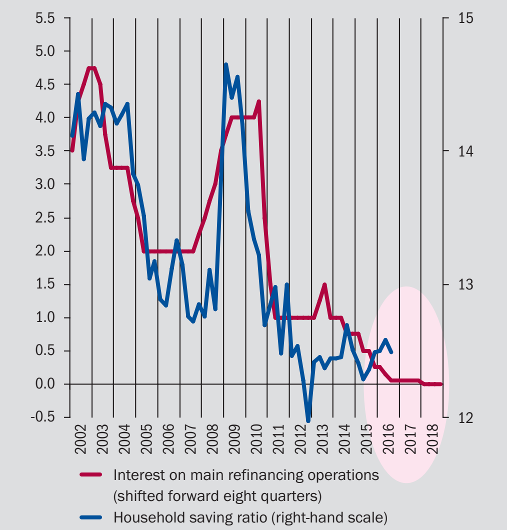
Sources: Macrobond and NBS calculations.

Chart 4 GDP growth (constant prices; percentages)

Source: Macrobond.

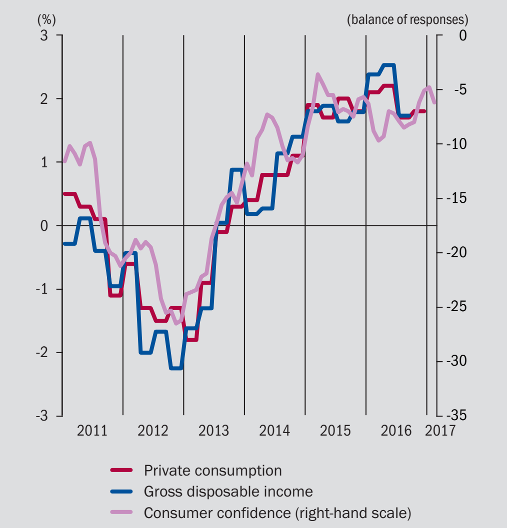
3 Real GDP growth in the third quarter was revised up from 0.3% to 0.4%.

Chart 6 Monetary policy rates and the household saving ratio (percentages)



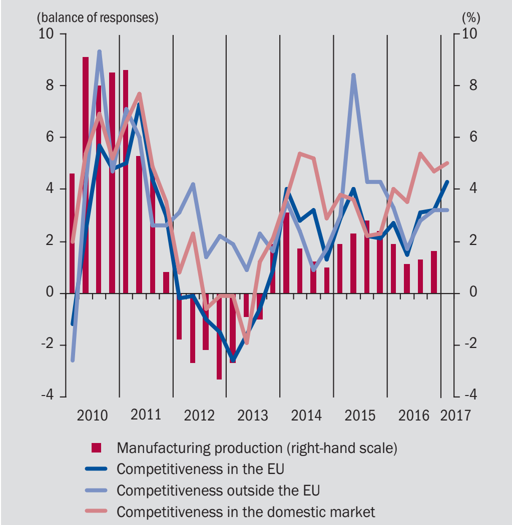
Source: Macrobond.

Chart 7 Private consumption, gross disposable income and consumer confidence (annual percentage changes; balance of responses)



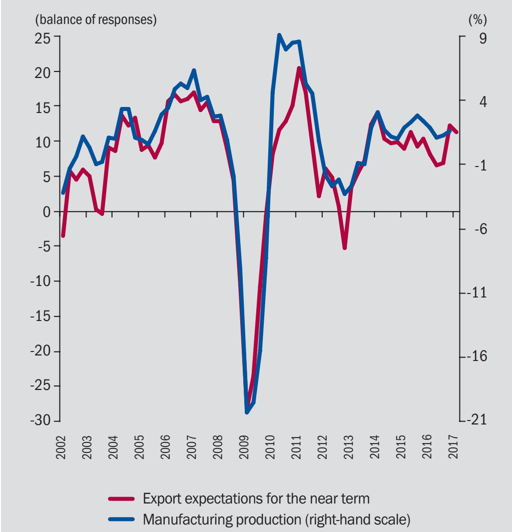
Source: Macrobond.
Note: The year-on-year rate of change in private consumption and gross disposable income in each month of each quarter is approximated by the rate of change for the quarter as a whole.

Chart 8 Competitiveness in industry (balance of responses) and manufacturing production (annual percentage changes)



Sources: European Commission, Eurostat and NBS calculations.

Chart 9 Export expectations in industry (balance of responses) and manufacturing production (annual percentage changes)

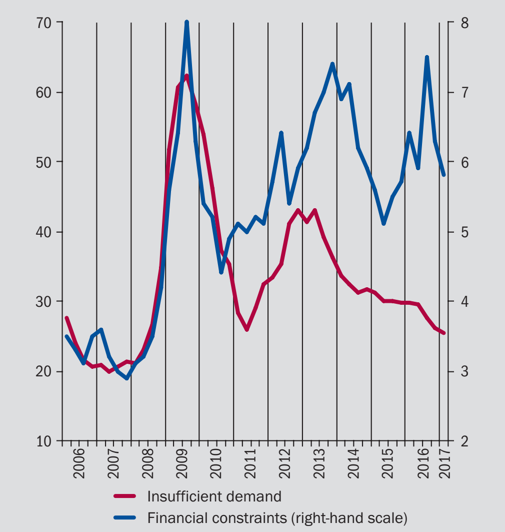


Sources: European Commission, Eurostat and NBS calculations.

Manufacturing production growth was higher in the fourth quarter than in the third quarter, consistent with the relatively high export growth. This acceleration was in line with previous surveys that showed improvements in firms' assessment of their competitiveness and in their export expectations. In the first quarter of 2017, firms remained quite strongly positive in their assessments of how they are positioned to compete, particularly in EU markets. Although export expectations fell slightly they remained favourable and indicative of continuing export growth.

Turning to firms' assessments of what factors are limiting their production, survey results for the first quarter of 2017 showed a further decline in the impact of "insufficient demand", which indicates that the economy is continuing to recover. Concerns about "financial constraints", which increased sharply in the third quarter of 2016 (probably in response to the UK's vote to leave the EU) and eased in the fourth quarter, moderated further in the first quarter thanks to the continuing favourable impact of accommodative monetary policy on financing conditions. The extent to which "shortage of labour force" is seen as a constraint on production remained largely unchanged, at a level approaching the historical highs of the pre-crisis period and pointing to strengthening of the labour market. As for "shortage of material and/or equipment", its impact rose for a third successive quarter and, taken in conjunction with brighter assessments of capacity utilisation, may indicate an increasing need for new investment and therefore investment demand growth.

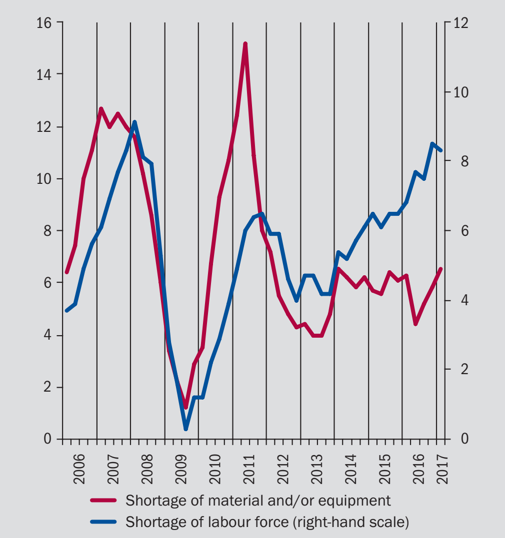
Chart 10 Factors limiting production in industry (percentages)



Source: Macrobond.

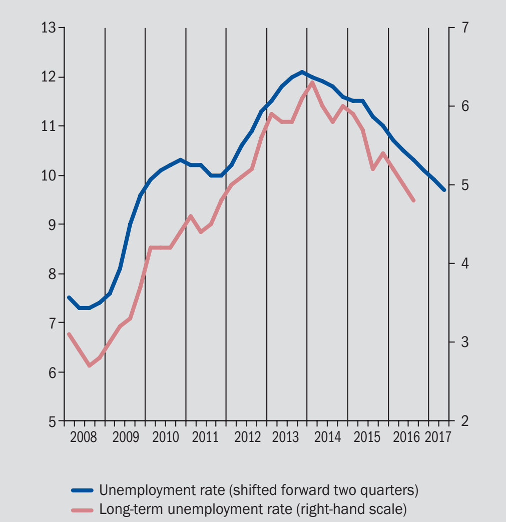
The upturn in labour market conditions continued in the fourth quarter of 2016, with unemployment falling from 9.9% in September to 9.6% in December. The rate remained unchanged in January 2017. The gradual decline in the jobless rate included a further decline in the long-term unemployment rate. Employment expectations continued to pick up in almost all sectors in the first two months of 2017, with the most notable improvements recorded in industry and retail trade. The construction sector saw employment expectations fall in January and then increase in February to exceed their end-2016 level. In the services sector, too, expectations rose in February after falling in January, but in this case they did not surpass the December level.

Chart 11 Factors limiting production in industry (percentages)



Source: Macrobond.

Chart 12 Unemployment rate and long-term unemployment rate (percentages)



Source: Eurostat.

Chart 13 Employment expectations by sector (balance of responses)

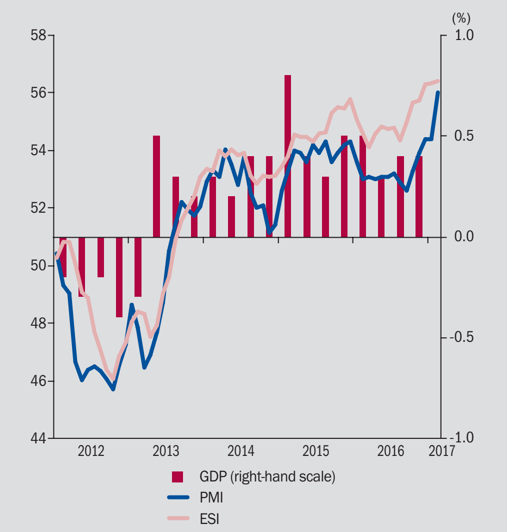
Source: European Commission.

Chart 15 Eurocoin indicator and quarterly euro area GDP growth

Sources: Centre for Economic Policy Research/Bank of Italy and Eurostat.

Leading indicators for the euro area are relatively favourable and point to a moderate acceleration in economic growth. After remaining unchanged in January, the composite Purchasing Managers' Index (PMI) increased quite sharply in February to reach its highest level in almost six years. The European Commission's Economic Sentiment Indicator (ESI) increased for a sixth successive month, to stand higher than at any time since March 2011. The further improvement of the Eurocoin indicator is also signalling an increase in activity growth.

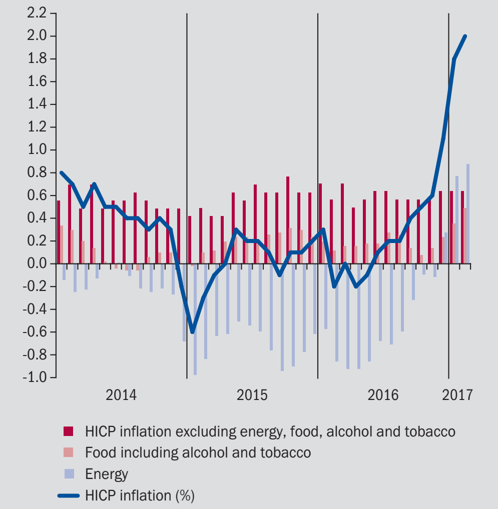
Chart 14 Leading indicators and quarterly euro area GDP growth



Sources: Macrobond, Eurostat, Bloomberg and NBS calculations.

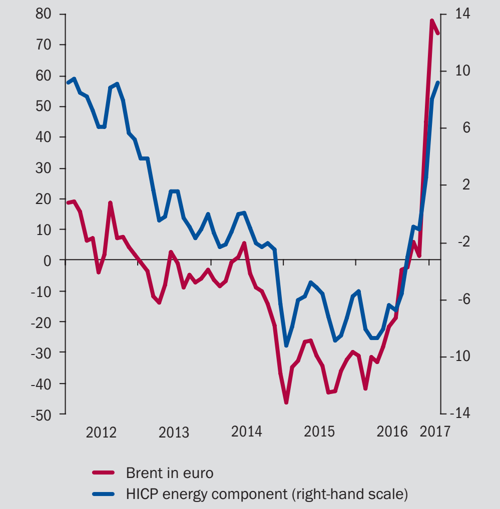
Euro area annual HICP inflation accelerated gradually in the fourth quarter of 2016 on the back of rising energy and food inflation. Headline inflation increased from 0.4% in September to 1.1% in December. At the same time, however, inflation excluding food and energy remained subdued, with its rate in December at 0.9%, only 0.1 percentage point higher compared with September. The annual rate of change in energy and food prices increased appreciably further in January and February, thus contributing to the increase in the headline rate, which reached 2.0% in February. Inflation excluding energy and food remained unchanged during this period. Cost-push pressures therefore continue to be the main factor in price movements, while inflation in demand-sensitive items remains subdued.

Chart 16 Annual HICP inflation rate and the contributions of selected components (percentages; percentage point contributions)



Sources: Macrobond and NBS calculations.

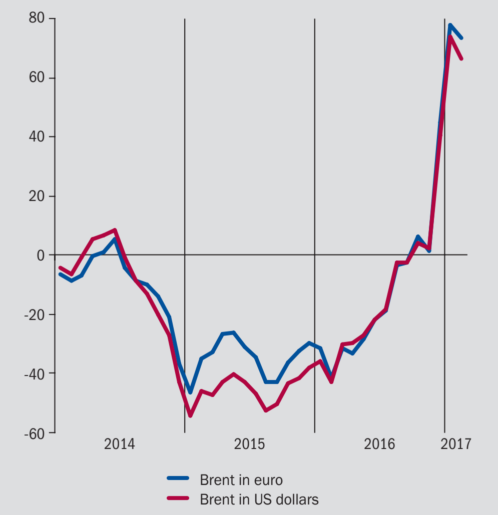
Chart 18 Oil prices in euro and the HICP energy component (annual percentage changes)



Sources: Macrobond and NBS calculations.

Energy prices continued to track the year-on-year change in the average global price of crude oil, which, in euro terms, went from a negative figure in September 2016 to an increase of almost 80% in January 2017. Annual energy inflation reflected not only the gradual increase in oil prices in the fourth quarter of 2016 (except in November) and the first two months of 2017, but also a significant base effect. Whereas in January and February 2016 the average oil price was just above USD 30 per barrel, at the beginning of 2017 it was slightly higher than USD 55 per barrel. This movement was reflected in consumer energy prices, as their annual rate of change turned positive in December 2016 and accelerated significantly in the next two months, to over 9%.

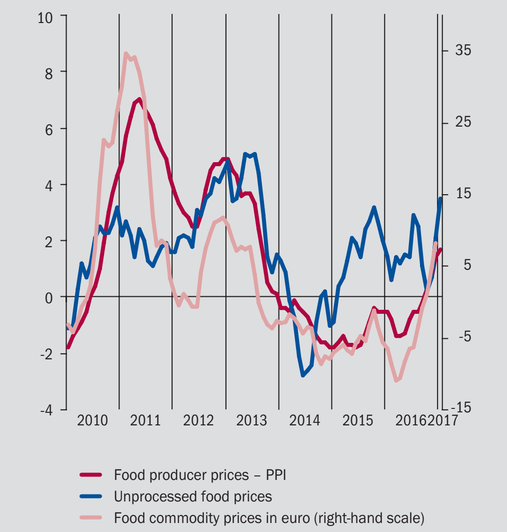
Chart 17 Oil prices in euro and US dollars (annual percentage changes)



Sources: Macrobond and NBS calculations.

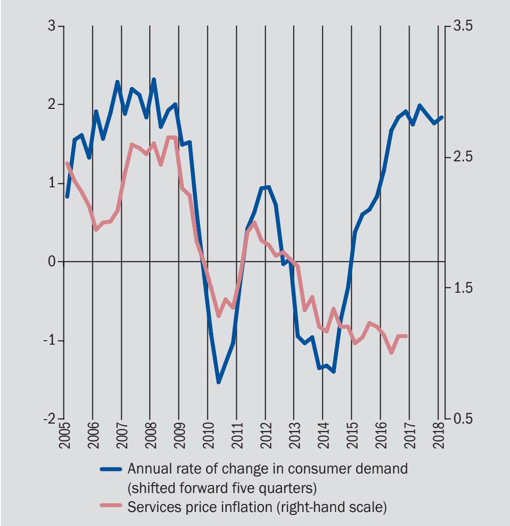
The recovery of the food commodity market continued and gradually had an upward impact on food producer price inflation, which turned positive in October and accelerated to 1.7% in January (1.9 percentage points higher than its September level). A marked increase in commodity prices at the turn of the year quickly passed through to unprocessed food inflation, which rose from 1.1% in September to 2.1% in December and then accelerated to more than 5% in January and February. The increases in commodity prices and food producer prices were reflected to some extent, with a lag, in processed food prices. Their annual rate of change accelerated moderately from 0.5% in September to 0.7% in December and 0.9% in February. At the same time, commodity price movements are pointing to a further increase in processed food inflation.

Chart 19 Food prices: commodity, producer and consumer prices (annual percentage changes)



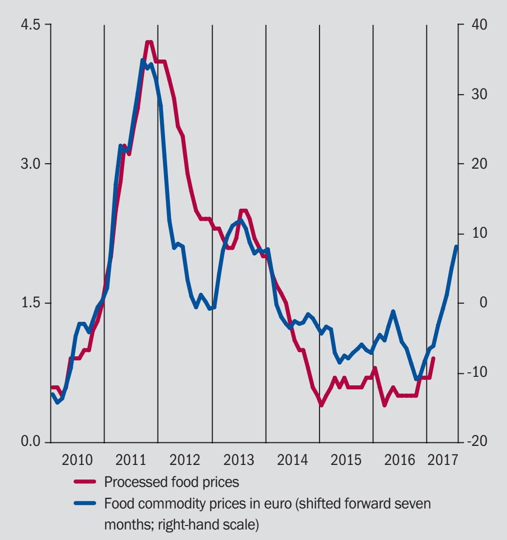
Sources: Macrobond, ECB and NBS calculations.

Chart 21 Consumer demand and services price inflation (annual percentage changes)



Source: Macrobond.

Chart 20 Food commodity prices and processed food prices (annual percentage changes)



Source: Macrobond.

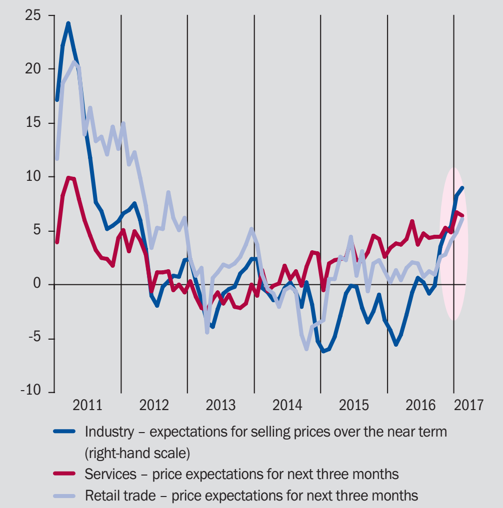
Chart 22 Non-energy industrial goods prices and the nominal exchange rate (annual percentage changes)

Source: Macrobond.
Note: Positive values for the exchange rate denote depreciation of the euro.

In an environment of strong competition, prices of demand-sensitive items in the consumption basket remained subdued. Despite relatively strong growth in consumer demand, services inflation stayed muted. While the rate did accelerate slightly in the fourth quarter (by 0.2 percentage point, to 1.3%), it was broadly unchanged in the first two months of 2017. Services inflation could come under upward pressure from second-round effects of rising energy and food prices, as well as from indicators of continuing consumption growth. Non-energy industrial goods inflation remained unchanged from August to December, at 0.3%, before accelerating in January (to 0.5%) and then slowing in February (to 0.2%). Although the nominal exchange rate's gradually moderating year-on-year appreciation, or slight depreciation, to some extent stemmed the annual rate of decline in import prices of consumer goods, it did not yet have an impact on prices of non-energy industrial goods. Inflation in market components of the consumption basket is probably being contained by strong competition and by efforts to gain or maintain market share.

Price expectations continued to increase across almost all sectors in the first two months of 2017. Their highest rise was again in industry, where the increase in cost factors gradually had an impact. This was related to the annual rate of inflation in industry import prices, which gradually became less negative and then turned positive in December. A result of that movement was upward pressure on producer prices in industry as a whole and in manufacturing in particular.

Chart 23 Price expectations in industry, services and retail trade (balance of responses)



Sources: European Commission and Eurostat.

Chart 24 Price expectations in industry (balance of responses) and producer prices (annual percentage changes)

Sources: European Commission, Eurostat and Macrobond.

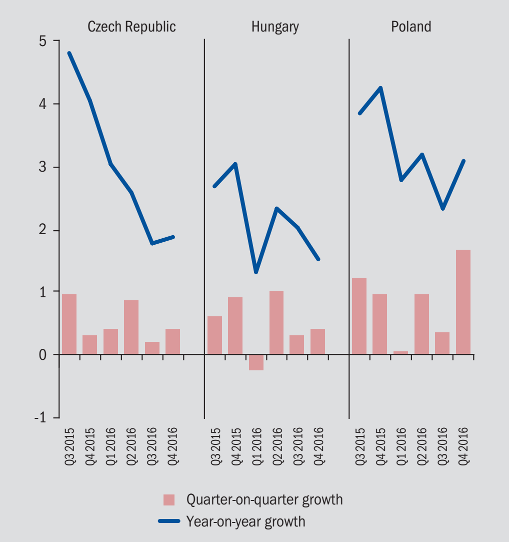
At its meetings from December 2016 to March 2017, the ECB's Governing Council decided to leave the interest rates on the main refinancing operations, the marginal lending facility and the deposit facility unchanged at 0.00%, 0.25% and -0.40% respectively. The Council said it continued to expect the key ECB interest rates to remain at present or lower levels for an extended period of time, and well past the horizon of its net asset purchases.

At its meetings in September and October 2016, the Council confirmed that monthly purchases of €80 billion under the expanded asset purchase programme (APP) were intended to run until the end of March 2017, or beyond, if necessary, and in any case until the Council saw a sustained adjustment in the path of inflation consistent with its inflation aim. At its December meeting, the Council decided that it would continue its purchases under the APP at a monthly pace of €80 billion until the end of March 2017 and that from April 2017 the net asset purchases were intended to continue at a monthly pace of €60 billion until the end of December 2017, or beyond, if necessary, and in any case until the Council saw a sustained adjustment in the path of inflation consistent with its inflation aim. In addition, the Council confirmed that if, in the meantime, the outlook became less favourable, or if financial conditions became inconsistent with further progress towards a sustained adjustment of the path of inflation, it intended to increase the programme in terms of size and/or duration. The Council also confirmed that the net purchases would be made alongside reinvestments of the principal payments from maturing securities purchased under the APP. To ensure the continued smooth implementation of the Eurosystem's asset purchases, the Council also decided to adjust the parameters of the APP as of 2 January 2017 as follows: first, the maturity range of the public sector purchase programme would be broadened by decreasing the minimum remaining maturity for eligible securities from two years to one year; second, purchases of securities under the APP with a yield to maturity below the interest rate on the ECB's deposit facility would be permitted to the extent necessary. At its meetings in January and March, the Council confirmed that purchases under the APP and reinvestments would continue to be made at the pace stipulated in the December meeting.

5 The Czech Republic, Hungary and Poland

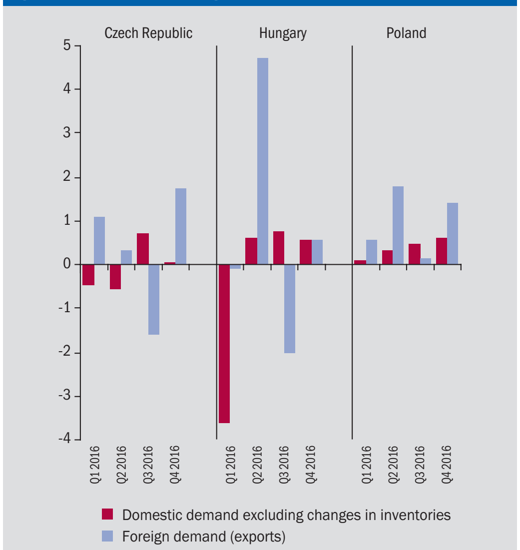
In the Czech Republic, annual GDP growth was 0.1 percentage point higher in the fourth quarter of 2016 than in the third quarter, at 1.9%, and in Poland it accelerated by an even faster, 0.8 percentage point, to 3.1%. Hungary's economic growth slowed by 0.5 percentage point, to 1.5%.

Chart 25 GDP growth (percentages)



Source: Eurostat.

Chart 26 Contributions to quarterly GDP growth (percentage points)



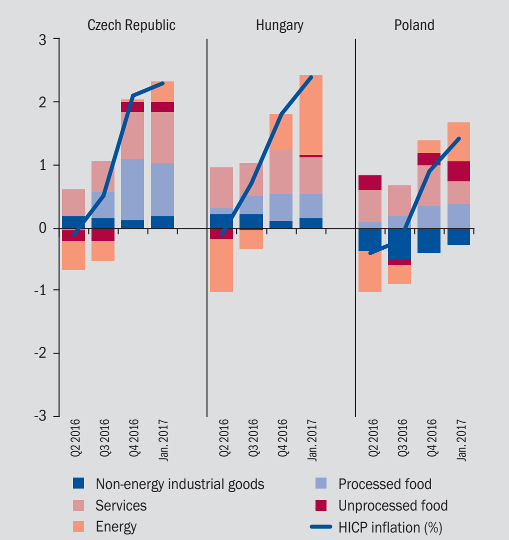
Sources: Eurostat and NBS calculations.

In quarter-on-quarter terms, economic growth in all three countries was stronger in the fourth quarter than in the previous quarter. In the Czech Republic it accelerated by 0.2 percentage point, to 0.4%, in Hungary by 0.1 percentage point, to 0.4%, and in Poland by 1.3 percentage point, to 1.7%. The Czech Republic's GDP growth was supported by household final consumption (albeit to a lesser extent compared with the third quarter) and in particular by net trade, as export growth significantly exceeded import growth. The negative contributions of investment demand and changes in inventories were both more pronounced compared with the previous quarter, while the negative impact of government consumption remained the same. In Hungary, net trade was the main driver of the economy's modest expansion, as export growth turned notably positive while imports recorded only a more moderate decline. Household consumption also had a positive impact, even greater than in the previous quarter. Investment and changes in inventories both weighed on GDP growth. Poland's economic growth was supported by household consumption and government consumption, as well as by changes in inventories and net trade (export growth exceeded import growth). Investment demand made the only negative contribution, albeit more moderate compared with the previous quarter.

Annual consumer price inflation in all three countries was higher in December 2016 than in September. In the **Czech Republic** it accelerated by 1.6 percentage point, to 2.1%, in Hungary by 1.1 percentage point, to 1.8%, and in Poland by 1.1 percentage point, to 0.9%. The acceleration in Czech headline inflation was supported by nearly all components, but in particular by increases in processed food prices and in services prices. Unprocessed food inflation also had a positive impact and energy inflation turned positive for the first time in three years. Non-energy industrial goods inflation slowed slightly. In January, the Czech inflation increased again, owing mainly to the further acceleration in services inflation and energy inflation. In **Hungary,** too, annual consumer price inflation was significantly higher in December than in September. The increase was accounted for mainly by energy inflation – which was markedly positive after a long period in negative territory – and services inflation, and to a lesser extent by the processed food component. Non-energy industrial goods inflation slowed, and therefore its positive contribution to the headline rate was lower compared with September. The non-processed food component had a neutral impact in December, as in September. In January, Hungary's consumer price inflation rate accelerated again, due largely to the continuing substantial increase in energy prices. In **Poland,** the annual consumer price inflation rate increased in December after declining in previous quarters. Services inflation exerted the largest upward pressure, followed by food inflation and energy inflation. As in the other countries, the energy component returned to growth after a prolonged negative trajectory. Non-energy industrial goods inflation again made a negative contribution, albeit more moderate since its annual rate of change was less negative compared with September. In January, Poland's headline inflation rate continued to increase, with the energy component making the largest contribution to its acceleration.

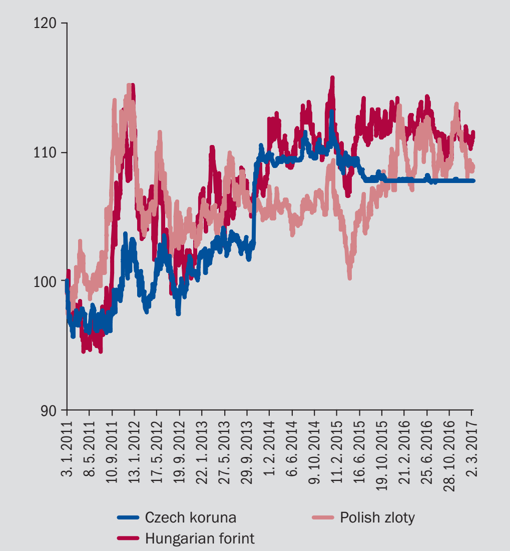
The Czech koruna's exchange rate vis-à-vis the euro at the end of 2016 stood unchanged from its level at the end of September 2016, while both the Hungarian forint and Polish zloty had depreciated, by 0.54% and 2.73% respectively. It remains the case that the koruna is constrained to follow a largely strengthening trajectory, since the Czech central bank is still committed to using foreign exchange interventions to maintain accommodative monetary policy conditions. The movements of the forint and zloty during the fourth quarter reflected financial market sentiment, which was influenced in particular by the situation in the oil market, by expectations of changes in the monetary policy stances of major central banks, and by non-economic events (such as the US presidential election).

Chart 27 HICP inflation and its composition (percentages; percentage point contributions)



Sources: Eurostat and NBS calculations.

Chart 28 Exchange rate indices of national currencies vis-à-vis the euro (index: 3 January 2011 = 100)

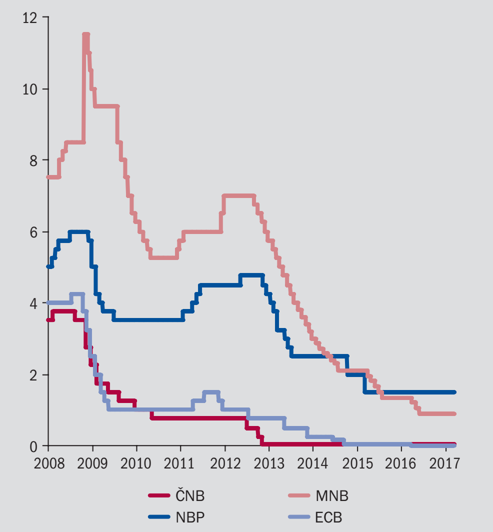


Sources: Eurostat and NBS calculations.
Note: A fall in value denotes appreciation.

The koruna's exchange was held above CZK 27.0 per euro thanks to the Czech central bank's significant interventions on the foreign exchange market. Appreciation pressure on the koruna stemmed from the fact that the time (mid-2017) is approaching when the central bank expects to discontinue its commitment to use the exchange rate as a monetary policy instrument, as well as from favourable inflation figures for the Czech economy.

As regards monetary policy settings in the three countries in the fourth quarter of 2016, **Česká národní banka** (ČNB) kept its base rate unchanged at 0.05% (zero lower bound). In the statements issued after its monetary policy meetings in the fourth quarter, the ČNB Bank Board confirmed its commitment to using the exchange rate as an additional instrument for easing monetary policy until mid-2017 (its interventions on the foreign exchange market during the third quarter amounted to €7.742 billion). At its December meeting the Board discussed whether to introduce negative interest rates as a tool for supporting the exchange rate commitment and a smooth exit from the commitment, but in the end decided that such a measure was inconsistent with discontinuation of the exchange rate commitment and that it should occur at a time of expected tightening of monetary conditions. According to the Board's statement after its February meeting, conditions for sustainable fulfilment of the 2% inflation target – the precondition for returning to a conventional monetary policy regime – are expected to be met from around mid-2017 and also after the return to a conventional monetary policy. The Board also confirmed that it stood ready to use its instruments to mitigate potential excessive exchange rate fluctuations. In Hungary, the **Magyar Nemzeti Bank** (MNB) did not alter either its base rate or overnight deposit rate in the fourth quarter of 2016, leaving them at 0.9% and -0.05% respectively (the deposit rate has been at that level since 23 March 2016). In October and November, however, the MNB Monetary Council cut the overnight collateralised lending rate by a cumulative 25 basis points, to 0.9% (thus narrowing the policy rate corridor), and the one-week collateralised lending rate by a cumulative 15 basis points, to 0.9%. The Council set a limit on the use of the MNB's three-month deposit facility from October, and said it considered the limit to be an integral part of its monetary policy instruments. At its October meeting, the Council decided to lower the required reserve ratio for banks from 2% to 1%, effective from 1 December 2016. According to the Council, maintaining the current monetary policy settings over the policy horizon is consistent with the medium-term achievement of the inflation target and a corresponding degree of support for the economy. The Council also confirmed its readiness to ease monetary conditions further, using non-standard instruments if necessary. In Poland, **Narodowy Bank Polski** (NBP) left its monetary-policy settings unchanged in the fourth quarter of 2016 (keeping the reference rate at 1.5%). According to the NBP's Monetary Policy Council, the inflation rate was becoming gradually less negative owing to the dissipating effects of the earlier sharp fall in global commodity prices, and also to the acceleration of wage growth in Poland. The Council also said the current level of interest rates was conducive to keeping the Polish economy on a sustainable growth path and to maintaining macroeconomic equilibrium.

Chart 29 Key interest rates of national central banks (percentages)



Sources: National central banks and the ECB.

SUMMARY OF GDP GROWTH PROJECTIONS OF SELECTED INSTITUTIONS

Table 1 Global economy

	Release	2016		2017		2018		2019	
IMF	January 2017	3.1	(=)	3.4	(=)	3.6	(=)	-	-
OECD	March 2017	3.0	(0.1)	3.3	(=)	3.6	(=)	-	-
EC	February 2017	3.0	(=)	3.4	(=)	3.6	(0.1)	-	-
ECB[1)]	March 2017	3.1	(0.1)	3.5	(=)	3.8	(0.1)	3.8	(=)

Table 2 United States

	Release	2016		2017		2018		2019	
IMF	January 2017	1.6	(=)	2.3	(0.1)	2.5	(0.4)	-	-
OECD	March 2017	1.6	(0.1)	2.4	(0.1)	2.8	(-0.2)	-	-
EC	February 2017	1.6	(=)	2.3	(0.2)	2.2	(0.3)	-	-
Federal Reserve	December 2016	1.85	(0.05)	2.1	(0.05)	2.0	(0.05)	1.9	(0.05)

Table 3 Euro area

	Release	2016		2017		2018		2019	
IMF	January 2017	1.7	(=)	1.6	(0.1)	1.6	(=)	-	-
OECD	March 2017	1.7	(=)	1.6	(=)	1.6	(-0.1)	-	-
EC	February 2017	1.7	(=)	1.6	(0.1)	1.8	(0.1)	-	-
ECB	March 2017	1.7	(=)	1.8	(0.1)	1.7	(0.1)	1.6	(=)

Table 4 Czech Republic

	Release	2016		2017		2018		2019	
IMF	October 2016	2.5	(=)	2.7	(0.3)	2.4	-	-	-
OECD	November 2016	2.4	(=)	2.5	(-0.1)	2.6	-	-	-
EC	February 2017	2.4	(0.2)	2.6	(=)	2.7	(=)	-	-
ČNB	February 2017	2.4	(-0.4)	2.8	(-0.1)	2.8	(-0.1)	-	-

Table 5 Hungary

	Release	2016		2017		2018		2019	
IMF	October 2016	2.0	(-0.3)	2.5	(=)	2.4	-	-	-
OECD	November 2016	1.7	(0.1)	2.5	(-0.6)	2.2	-	-	-
EC	February 2017	1.9	(-0.2)	3.5	(0.9)	3.2	(0.4)	-	-
MNB	December 2016	2.8	(=)	3.6	(0.6)	3.7	-	-	-

Table 6 Poland

	Release	2016		2017		2018		2019	
IMF	October 2016	3.1	(-0.5)	3.4	(-0.2)	3.3	-	-	-
OECD	November 2016	2.6	(-0.4)	3.2	(-0.3)	3.1	-	-	-
EC	February 2017	2.8	(-0.3)	3.2	(-0.2)	3.1	(-0.1)	-	-
NBP	March 2016	2.8	(-0.2)	3.7	(0.1)	3.3	(=)	3.2	-

1) Global economic growth excluding the euro area.
Notes: Data in brackets denote the percentage point change from the previous projection.
The IMF projections of January 2017 and the OECD projections of March 2017 cover only large economies.