NÁRODNÁ BANKA SLOVENSKA
EUROSYSTÉM

Report on the International Economy

September 2018

Published by:

Address:
Národná banka Slovenska
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Discussed by the NBS Bank Board on 25 September 2018.

The cut-off date for this quarterly report was 13 September 2018.

ISSN 1339-9616 (online)

Contents

Abbreviations

CPI	consumer price index
EA	euro area
ECB	European Central Bank
EC	European Commission
EMEs	emerging market economies
EONIA	euro overnight index average
ESA 2010	European System of Accounts 2010
ESI	Economic Sentiment Indicator (European Commission)
EU	European Union
EUR	euro
EURIBOR	euro interbank offered rate
Eurostat	statistical office of the European Union
FDI	foreign direct investment
GDP	gross domestic product
GNDI	gross national disposable income
GNI	gross national income
HICP	Harmonised Index of Consumer Prices
IMF	International Monetary Fund
MFI	monetary financial institutions
MF SR	Ministry of Finance of the Slovak Republic
MMF	money market fund
MTF	NBS's Medium-Term Forecast (published on a quarterly basis)
NACE	Statistical Classification of Economic Activities in the European Community (Rev. 2)
NARKS	National Association of Real Estate Offices of Slovakia
NBS	Národná banka Slovenska
NEER	nominal effective exchange rate
NFC	non-financial corporation
NPISHs	non-profit institutions serving households
OECD	Organisation for Economic Co-operation and Development
p.a.	per annum
p.p.	percentage point
PMI	Purchasing Managers' Index
REER	real effective exchange rate
SASS	Slovenská asociácia správcovských spoločností – Slovak Association of Asset Management Companies
SME	small and medium-sized enterprise
SO SR	Statistical Office of the Slovak Republic
ULC	unit labour costs
ÚPSVR	Ústredie práce, sociálnych vecí a rodiny – Central Office of Labour, Social Affairs and Family
ÚRSO	Úrad pre reguláciu sieťových odvetví – Regulatory Office for Network Industries
USD	US dollar
VAT	value-added tax

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

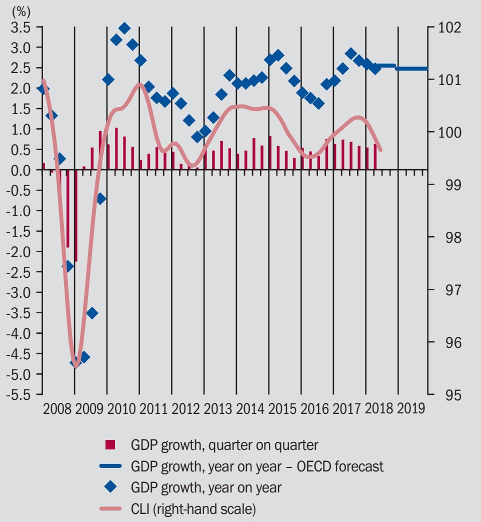
The global economy maintained solid growth in the second quarter of 2018. Some major world economies are expected to have reached the peak of the business cycle; at the same time, economic growth is becoming less synchronised. Developments in emerging market economies have been reflecting rising oil prices, higher interest rates in the United States, and mounting tensions in global trade. US protectionism and rising trading barriers are among the largest downside risks to the global economic growth outlook.

Looking at advanced economies, the United States made a strong positive contribution to global GDP growth in the second quarter of 2018. Domestic demand supported by robust private consumption growth and by still positive investment trends, and the acceleration of exports ahead of China's introduction of retaliatory import tariffs, helped ensure the highest level of global growth since the third quarter of 2014. Although the US economy was thus benefiting from a strong labour market and favourable sentiment, it benefited most of all from the fiscal stimulus. The procyclical easing of fiscal policy entails, however, a significant risk to the economy and in the short term could increase the current account deficit in the balance of payments, potentially reinforcing protectionist tendencies. The Japanese economy, after contracting in the first quarter, began expanding again in the second quarter. Private consumption may have been buoyed by labour market tightening, but possibly also by a temporary factor in the form of the early payment of summer bonuses. A pick-up in investment demand was consistent with strong data on machinery orders during the period under review and likely reflected the upward impact of labour shortages on firms' investment in labour-saving equipment. Export growth fell again, but imports accelerated, owing partly to rising prices of vehicle fuel. Net exports therefore had a negative impact on Japan's GDP growth; at the same time, since the Japanese economy is strongly export-oriented, global trade barriers, and in particular the possibility of the United States imposing import tariffs on cars, represent the main downside risk to its growth outlook. After a sluggish first quarter, the United Kingdom's economic growth accelerated in the second quarter of 2018, back up to the levels seen in the second half of 2017. Warm weather was one cause of the economy's improvement, as the construction sector regained ground it lost in the first quarter due to a hard winter, and therefore supported investment demand. Household consumption growth also increased moderately. At the same time, the country's economic activity increased despite a decline in manufacturing output. Exports slumped, owing mainly to declines in car and aircraft exports, while imports fell far more moderately; as a result, net trade made a significantly negative contribution to GDP growth. UK economic growth is expected to remain moderate amid the high uncertainty about the outcome of the Brexit negotiations. The euro area's economic growth in the second quarter remained the same as in the previous quarter, therefore still lower than last year's growth rates. Domestic demand growth was also unchanged from the first quarter, as the impact of a lower increase in household consumption was offset by higher increases in government consumption and in fixed investment spending. The pick-up in export performance was accompanied by stronger growth in imports, and so net trade had a negative impact on economic growth. Developments in the first two quarters, as well as leading indicator data, imply that the euro area growth for 2018 will be lower compared with the previous year.

Turning to emerging market economies, India maintained robust economic growth in the second quarter of 2018. Its year-on-year growth rate of 8% was the highest for two years and strengthened the country's position as the fastest-growing large economy. Private consumption was the main driver of growth, but exports, too, accelerated significantly, albeit with imports increasing by a similar margin. Growth in both government consumption and fixed investment spending slowed, but remained at robust levels. Going forward, India's activity growth may be dampened by the downward impact of higher oil prices on domestic demand and by the tightening of monetary policy in response to rising inflation. China's economic growth in the second quarter was stronger than in the first quarter in quarter-on-quarter terms, but lower year on year. This may have reflected China's efforts to rein in its lending boom at a time of mounting trade tensions with the United States, which may weigh on the Chinese economic growth in the second half of the year. The decline in sentiment resulting from the trade situation had a negative impact on the real estate market. Chinese activity growth is expected to continue moderating, owing to regulatory tightening of the financial sector and to the softening of external demand. The Russian economy continued its recovery in the second quarter of 2018, which, given the unimpressive results in Russian manufacturing industry, may be imputed to rising oil prices, low unemployment and wage growth. On the production side, the economy was supported by Russia's hosting of the football World Cup, which boosted activity in services related to accommodation, transport and food services. Favourable labour market trends, rising commodity prices, and increasing oil production are also expected to have had a positive impact on Russian activity growth. The next quarter may see Russian growth affected by US sanctions targeting foreign aid, defence and security goods, which took effect at the end of August. The heightened geopolitical risks and possibility of further economic sanctions remain key risks to the outlook for Russia's economy. Brazil's economic growth remained largely unchanged in the second quarter. Although it increased slightly, GDP growth would have been higher still but for the negative impact of widespread truckers' strikes in May and June. This caused investment to drop, while at the same time exports registered their largest fall since the end of 2014. Imports also fell, but to a far lesser extent, and therefore net trade had a negative impact on GDP growth. The main drivers of growth were therefore government spending and household consumption. The lagged effects of the strikes, as well as political instability, could shape the course of the Brazilian economy in the near term.

Economic activity growth across the OECD area edged up in the second quarter of 2018, to 0.6% quarter on quarter (from 0.5% in the previous period). In year-on-year terms, growth moderated from 2.6% in the first quarter to 2.5% in the second quarter. The Composite Leading Indicator for the OECD area[1] fell slightly in the second quarter of 2018 and continued its downward path in July, which may imply a global economic slowdown in the near term. The Global Composite Purchasing Managers' Index is also presaging a slight easing of global activity growth, as its average value for July and August was lower than its average for the second quarter of 2018.

Chart 1 GDP growth and the CLI for the OECD area



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

Looking ahead, global economic trends will be affected by the US Administration's imposition of further import tariffs. Tariffs on steel and aluminium imports from Canada, Mexico and the European Union took effect at the beginning of June 2018.[2] During July and August, the US Administration imposed further import tariffs on more than 1,000 Chinese products worth USD 50 billion in total.[3] In response to this approach, trading partners of the United States are adopting retaliatory measures and filing complaints with the World Trade Organisation, and so the risk of a trade war is increasing. The measures so far taken by United States are not likely to have had a significant impact on the global economy. Further import tariffs under consideration, including tariffs on USD 200 billion worth of Chinese products and on USD 208 billion worth of imports of cars and car parts from all trading partners could, however, have a greater impact on the world economy, given the wider extent

1 *The CLIs for OECD countries are published on a monthly basis, and the most recent, published in September 2018, are for the period up to July 2018.*
2 *The United States imposed tariffs on other countries back in March, allowing exemptions for those that met its trade demands: South Korea, which agreed to revise the United States-Korea Free Trade Agreement; and Argentina, Brazil and Australia, which accepted quotas on their exports of steel to the United States (a cause of elevated US inventories).*
3 *Tariffs on USD 34 billion and USD 16 billion worth of imports took effect, respectively, on 6 July 2018 and 23 August 2018.*

of the automotive market and its integration into global value chains.

Global consumer price inflation rose significantly in the second quarter of 2018. In the OECD area, consumer price inflation rose from 2.3% in March to 2.8% in June, with the sharp acceleration caused entirely by a near doubling of energy price inflation. At the same time, food price inflation increased only marginally and core inflation remained unchanged, at 2.0%. In July, OECD inflation continued to rise, edging up to 2.9%. Energy prices again accelerated, but inflation excluding food and energy also increased this month, to 2.1%, and put the greater upward pressure on the headline rate.

2 Commodities

The average commodity price index was higher in the second quarter of 2018 than in the first quarter. With non-energy commodity prices rising only slightly, the overall increase was largely attributable to energy commodity prices.

Looking at energy commodities, the average price of a barrel of Brent crude oil climbed by around USD 7, quarter on quarter, to USD 74. Until mid-May, the oil price's upward trend was based on strong growth in demand, continuing production restraint by members of the Organization of Petroleum Exporting Countries (OPEC), falling global inventories, and rising geopolitical tensions. When, in mid-May, the United States withdrew from the Iran nuclear deal, oil prices surged to a three-and-a-half year high of USD 80 amid the prospect of the United States imposing sanctions on Iran and of a resulting drop in oil exports from that country. Oil prices corrected in the latter part of the month, and in June they were affected by expectations of supply increases after the meeting of OPEC members and Russia held in that month. Although the meeting resulted in an agreement to hike production, markets continued to reflect supply shortage concerns stemming from expectations of reduced Iranian supplies and from output disruptions in Canada. As a result, oil prices returned back to the USD 80 level.

As for the non-energy commodity price index in the second quarter, the impact of a quarter-on-quarter increase in food commodity prices was cancelled out by a decline in metal prices. Food commodity prices were driven up mainly by a rise in cocoa prices resulting from dry weather in Africa, which accounts for two-thirds of global cocoa production. Wheat prices increased owing mainly to a drop in Russian production, also caused by dry weather. Downward pressure on food commodity prices came largely from coffee prices, as good coffee bean harvests resulted in oversupply. Sugar prices dropped sharply as global inventories reached record levels amid diminishing demand and rapidly increasing production. A decline in wholesale pork prices was caused partly by a decline in US exports of the commodity to countries (China and Mexico) that have imposed retaliatory tariffs on the United States, and partly, in Europe, by cheap pork production in certain EU countries. The fall in metal prices was caused largely by expectations that the US-China trade tensions will curb demand, and it may also have reflected a slowdown in the global metal processing industry. The iron ore price in particular fell as a result of elevated stocks in China, and the zinc price also decreased. On the other hand, the average price of aluminium increased after the US imposed sanctions on the Russian producer Rusal. Nickel prices also rose amid speculation that sanctions would be placed on other Russian producers.

3 The United States

In the United States, the annualised rate of GDP growth surged from 2.2% in the first quarter of 2018 to 4.2% in the second quarter. The year-on-year growth rate also increased, from 2.6% to 2.9%.

The marked acceleration in US economic activity during the period under review was driven mainly by private consumption, which picked up strongly after a relatively subdued start to the year. In particular, spending on durable goods increased sharply, as plans to increase tariffs on car imports may well have stimulated spending on these products. Furthermore, households began increasing expenditure on non-durable goods, especially clothing and footwear. Private consumption growth was also supported, however, by spending on food and accommodation services. Another positive contributor to domestic demand was fixed investment growth, which remained robust despite being lower in the second quarter than in the first quarter (owing to weaker growth in non-residential investment). Residential investment fell again, but far more moderately. The strength of private consumption and investment was in line with the impact expected from the tax reform introduced by the US Administration at the start of the year. Furthermore, the fiscal stimulus had a positive impact on government consumption and investment, in particular at the federal level in the area of national defence. The US economy received a significant boost from exports in the period under review; their surge, however, was based on a one-off effect, with soybean and corn exports increasing as a result of efforts to avoid China's impending import tariffs on these products. Since imports fell slightly in the second quarter, net trade made a strongly positive contribution to GDP growth. By contrast, changes in inventories had a sizeable negative impact on US activity growth. The fiscal stimulus strongly supported the US economy in the first half of 2018, but looking ahead, when the stimulus's positive effects have faded and monetary policy is tightened, the economy's expansion may ease significantly next year.

Consumer price inflation in the United States accelerated substantially in the second quarter of 2018, and at the end of the period it was close to 3%. By April, the headline inflation rate was already under upward pressure from high energy inflation that reflected petrol prices. The overall rate jumped even further in May, however, when the annual rate of increase in petrol prices exceeded 20%, and it rose again in June owing to the same factor. Energy prices were therefore the main cause of the rise in consumer price inflation in the second quarter, from a rate of 2.4% in March to 2.9% in June (its highest level for more than six years). Inflation excluding energy and food, i.e. core inflation, also contributed to that increase, as it rose over the same period from 2.1% to 2.3%. Its acceleration may have been caused by continuing tightening of the labour market and by increasing wage growth. Components that put upward pressure on core inflation included new vehicle prices, whose rate of decrease moderated, and prices of healthcare goods and services, which accelerated. Tariffs imposed on imports of washing machines at the beginning of the year gradually began passing through to the year-on-year change in household appliance prices, which started increasing after more than five years of decline. This suggests that the tariffs subsequently placed on steel and aluminium could gradually push up core inflation by raising producers' input costs. Food prices remained relatively stable in the second quarter and so did not have a significant impact on the inflation path. In July, headline inflation stayed put at 2.9%, as the impacts of a marginal increase in energy inflation and an increase in core inflation (to 2.4%) were offset by a drop in food inflation. The strong increase in headline inflation over recent months attests to rising price pressures in the economy and implies further tightening of monetary policy.

The US Federal Open Market Committee (FOMC) decided at its meeting in May 2018 to leave the target range for the federal funds rate unchanged, at 1.50% to 1.75%. At its meeting in June, however, in view of realised and expected labour market developments and inflation, the Committee decided to raise the target range to 1.75% to 2.00%. At its 31 July to 1 August meeting, the Committee made no further change to the policy rate. According to the FOMC press release issued after that meeting, the stance of monetary policy remains accommodative, thereby supporting strong labour market conditions and a sustained return to 2% inflation.

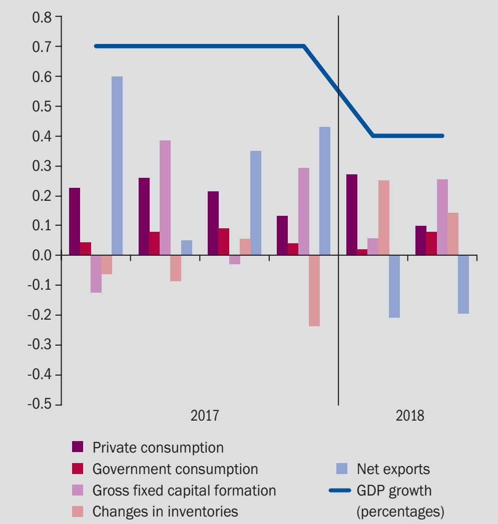
4 The euro area

Euro area GDP increased by 0.4%, quarter on quarter, in the second quarter of 2018, the same rate as in the previous quarter. Looking at the larger national economies within the euro area, GDP growth increased by 0.1 percentage point in both Germany (to 0.5%) and the Netherlands (0.7 %), and fell by 0.1 percentage point in both Spain (0.6%) and Italy (0.2%), while remaining unchanged in France (0.2%). In year-on-year terms, euro area growth moderated from 2.4% to 2.1%.

Economic growth in the second quarter, as in the first quarter, was driven by domestic demand, with investment demand accounting for much of that contribution. Gross fixed capital formation growth accelerated to 1.2%, from 0.3% in the first quarter, owing mainly to increases in machinery and equipment investment and, to a lesser extent, in construction sector investment. Private consumption continued to rise, but more moderately compared with the first quarter (down by 0.3 percentage point, to 0.2%). By contrast, government consumption growth increased, and changes in inventories also had a positive impact on headline growth, albeit more moderate than their impact in the previous quarter. Net trade contributed negatively to GDP growth, as it did in the first quarter; since the acceleration in export growth (from -0.7% to 0.6%) was lower than the acceleration in import growth (from -0.3% to 1.1%).

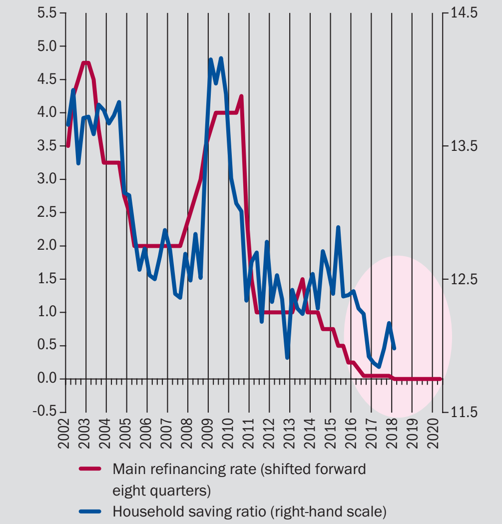
Consumer demand continued to be supported by low interest rates, as well as by the favourable labour market situation. After its upward trend in 2017, the saving ratio dropped to a relatively low level in the first quarter of 2018. Nevertheless, according to survey results, households' intentions to make major purchases did not change significantly during the second quarter, after weakening in the first quarter. The moderation of consumer demand growth at a time of improving labour market conditions may to some extent reflect the impact of rising vehicle fuel prices (caused by oil price increases). The next period is expected to see consumer demand remain stimulated by the labour market recovery, as well as by signs of a pick-up in wage growth. On the other hand, the pass-through of persisting high oil prices to vehicle fuel prices and to energy prices as a whole may reduce household disposable income and partly dampen consumer demand.

Chart 2 Euro area GDP and its components (quarter-on-quarter percentage changes; percentage point contributions)



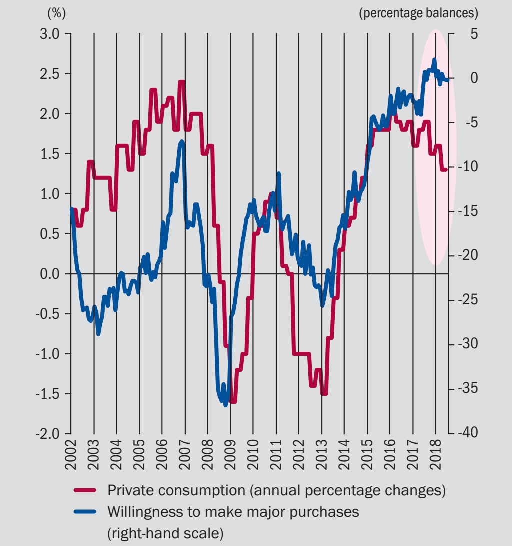
Sources: Macrobond and NBS calculations.

Chart 3 Monetary policy rates and the household saving ratio (percentages)



Source: Macrobond.

Chart 4 Private consumption and consumers' willingness to make major purchases



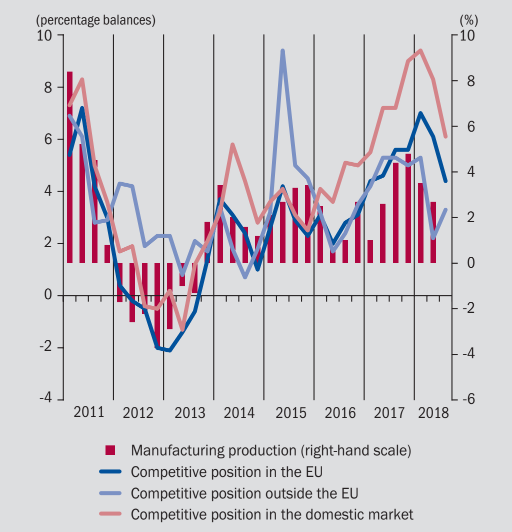
Source: Macrobond.

Chart 6 Export expectations in industry (percentage balances) and manufacturing production (annual percentage changes)

Sources: European Commission, Eurostat and NBS calculations.

Industrial firms' assessments of their competitive positions in domestic and EU markets deteriorated for a second successive quarter in the third quarter of 2018, but still remained at relatively favourable levels. These assessments probably imply that this year's economic growth will be lower than last year's. As for assessments of competitiveness in extra-EU markets, they improved slightly in the third quarter after worsening markedly in the previous period, with the change likely a result of the easing of trade tensions between the United States and the EU at the end of July. The weakening of competitive positions was reflected in a decline in export expectations, and also presages lower industrial production growth.

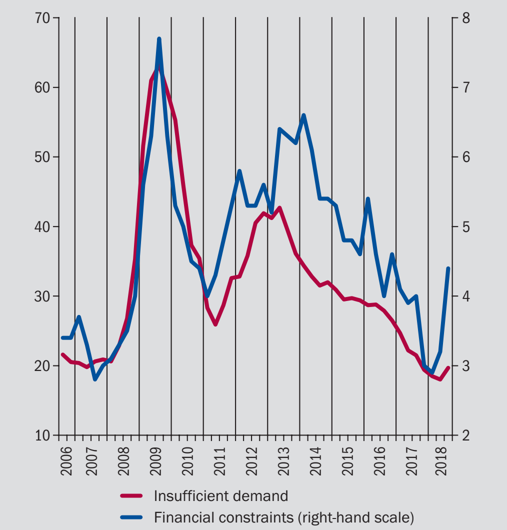
Chart 5 Industrial competitiveness (percentage balances) and manufacturing production (annual percentage changes)



Sources: European Commission, Eurostat and NBS calculations.

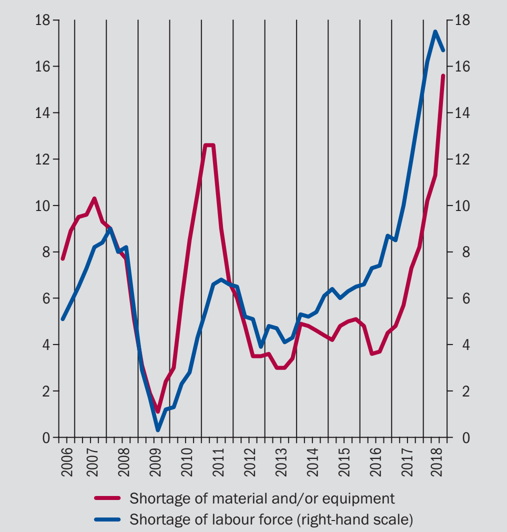
Like other indicators, industrial firms' latest assessments of the factors limiting their production imply a slowdown in economic growth. Survey results for the third quarter show that the percentage of respondents reporting 'insufficient demand' as a factor limiting production increased, moderately, for the first time in six quarters, and that the importance of 'financial constraints' rose sharply. Nevertheless, concerns about insufficient demand remained exceptionally low and favourable for economic activity growth. There was a slight decrease in the share of respondents reporting 'shortage of labour force' as a concern, but this indicator stayed very high, reflecting an employment situation that remains positive. By contrast, the importance of 'shortage of material and/or equipment' continued to increase, implying that plant will have to be renewed and that investment demand will continue rising.

Chart 7 Factors limiting production in industry (percentages)



Source: Macrobond.

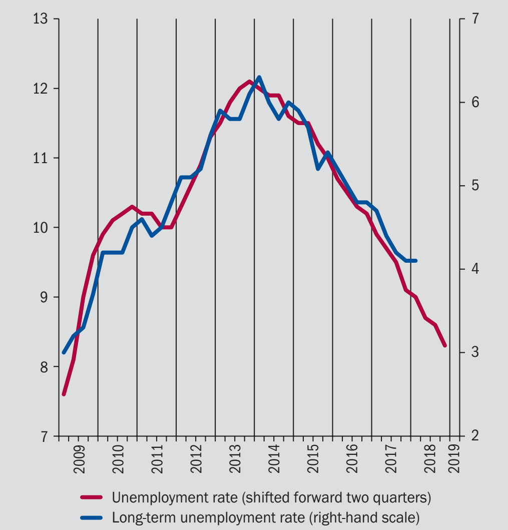
Chart 8 Factors limiting production in industry (percentages)



Source: Macrobond.

Labour market conditions maintained their favourable trend in the second quarter. The unemployment rate stood at 8.2% in June, 0.3 percentage point lower compared with March, and stayed at that level in July. Expectations for future employment also remain relatively high but are gradually moderating, in particular in industry and, to a lesser extent, retail trade. The decline in these expectations may be related in part to labour supply shortages, as well as to the uncertainty associated with rising protectionism and the deterioration in industrial firms' assessments of their competitiveness and in their export expectations. On the other hand, future employment expectations in the services and construction sectors are relatively stable, since after falling slightly in

Chart 9 Unemployment and long-term unemployment rates (percentages)



Source: Macrobond.

Chart 10 Employment expectations by sector (percentage balances)

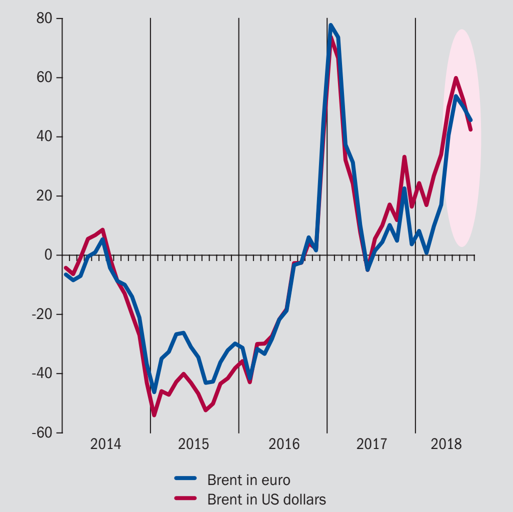
Source: Macrobond.

July, compared with June, they increased again in August.

Euro area annual HICP inflation increased gradually during the second quarter, reflecting relatively strong rises in energy price inflation and food inflation (the latter more moderate than the former). The headline inflation rate was 2.0% in June, 0.7 percentage point higher than in March. On the other hand, core inflation (inflation excluding energy and food) fell by 0.1 percentage point over the same period, to 0.9%. The impact of the services component was partly offset by an increase in the non-energy industrial goods component. In July, headline inflation increased slightly (to 2.1%), supported by a further acceleration of energy inflation, as well as by a rise in core inflation (to 1.1%). In August, the headline rate edged down to 2.0%, owing mainly to an easing of core inflation (to 1.0%) and partly to a marginal decline in the energy inflation.

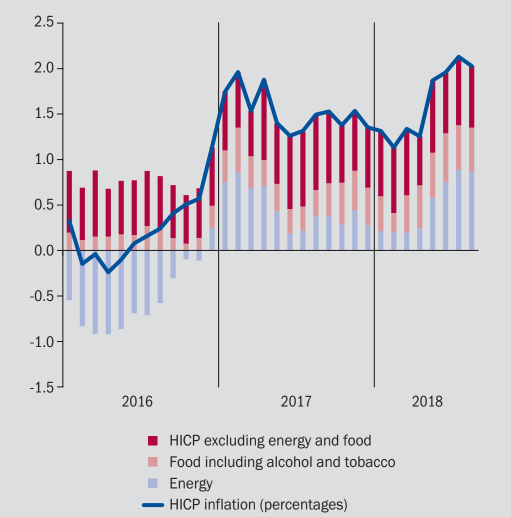
Looking at consumer energy prices during the second quarter, their annual rate of change mirrored that of global oil prices, which surged from the beginning of the quarter and peaked in June, in euro terms, at more than 50%. Oil price inflation moderated only slightly in the next two months. The acceleration in euro-denominated oil prices reflected not only commodity price trends, but also the gradual easing of the euro's year-on-year appreciation against the US dollar, which fell from 16% at the end of March, to just 4% at end-June and to around 2% at end-August. As a result, energy price inflation gradually accelerated from 2.0% in March to 8.0% in June. It continued rising in July (9.5%), before slowing marginally in August.

Chart 12 Oil prices in euro and US dollars (annual percentage changes)



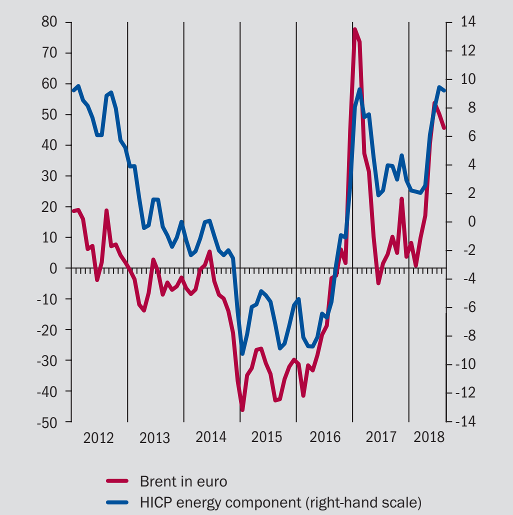
Sources: Macrobond and NBS calculations.

Chart 11 HICP inflation and selected components (annual percentage changes; percentage point contributions)



Source: Macrobond.

Chart 13 Oil prices in euro and the HICP energy component (annual percentage changes)

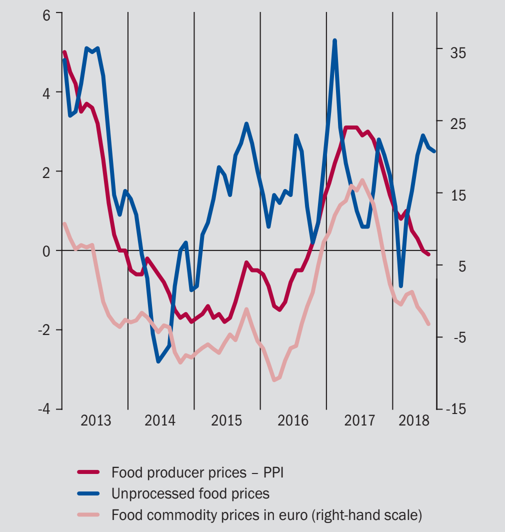


Sources: Macrobond and NBS calculations.

Consumer food price inflation increased from 2.1% in March to 2.7% in June, before moderating to 2.5% in July and staying at that level in August. Overall food inflation reflected opposite trends in unprocessed food prices and processed food prices. On the one hand, unprocessed food inflation increased quite strongly (from 0.8% in March to 2.9% in June), owing mainly to higher rates of increase in vegetable and fruit prices. On the other hand, processed food inflation fell slightly (from 2.9% in March to 2.6% in June), as a result of the slowdown in food commodity inflation recorded in the previous period. In July and August, both processed and unprocessed food inflation moderated. As for food commodity inflation, its annual rate of change rose in April, before resuming its downward trend in the next two months. From May, it moved into negative territory. It is therefore expected that food commodity prices will continue to have a negative impact on food producer prices and processed food prices in the next period.

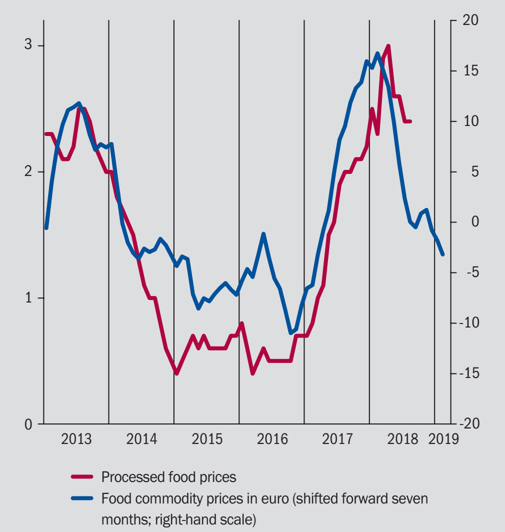
Core inflation (headline HICP inflation excluding energy and food) did not change significantly during the second quarter, despite the increased volatility resulting from calendar effects (the different timing of Easter). Core inflation stood at 0.9% in June, 0.1 percentage point lower than in March, while services inflation was 1.3% in June, 0.2 percentage below its March level. The negative impact of the services component was partly offset by the non-energy industrial goods inflation, which increased to 0.4% (by 0.2 percentage point). In August, core inflation was 1.0%, slightly higher compared with June. As the year-on-year appreciation of the nominal effective exchange

Chart 14 Food prices: commodity, producer and consumer prices (annual percentage changes)



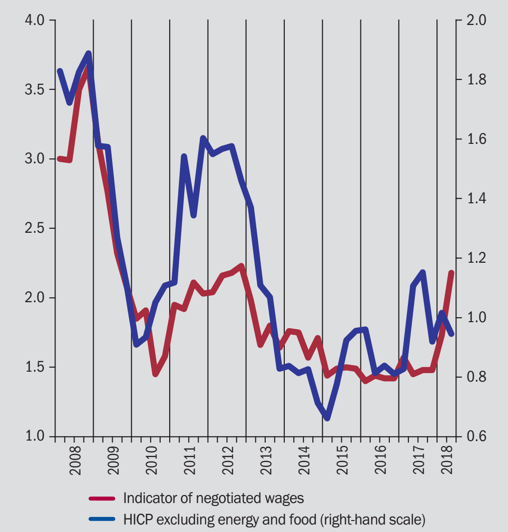
Source: Macrobond.

Chart 15 Food commodity prices and processed food prices (annual percentage changes)



Source: Macrobond.

Chart 16 Negotiated wages indicator and core inflation (annual percentage changes)

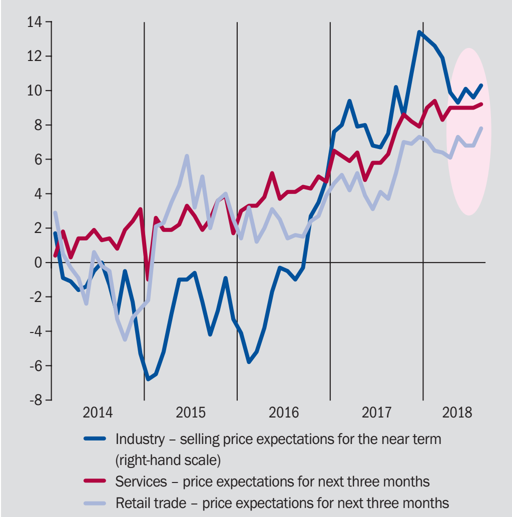


Source: Macrobond.

Chart 17 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.

Chart 18 Price expectations in industry, services and retail trade (percentage balances)



Source: Macrobond.

rate was diminishing, it gradually supported the easing of the annual rate of decrease in import prices for consumer goods. Thus exchange rate developments may in coming months, via import prices, put upward pressure on non-energy industrial goods inflation. Signs of moderately accelerating wage growth amid labour market tightening may also support demand-sensitive inflation. The annual growth rate of the ECB's indicator of negotiated wages increased in the first two quarters, from around 1.5% to more than 2%.

Selling price expectations remain on a broadly upward trend. In July and August they increased moderately in both the services and retail trade sectors. In industry, they fell significantly between January and May, before stabilising, and even rising marginally, in subsequent months. Selling price expectations are likely reflecting a gradual rise in input costs, related both to commodity price trends and to a labour market situation that includes signs of accelerating wage growth. Compared with the ECB Survey of Professional Forecasters (SPF) for the second quarter of 2018, the SPF for the third quarter shows underlying inflation expectations to be unchanged.

Chart 19 Expectations for HICP inflation according to the ECB's Survey of Professional Forecasters

Source: Macrobond.

At its monetary policy meetings between March and September 2018, 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

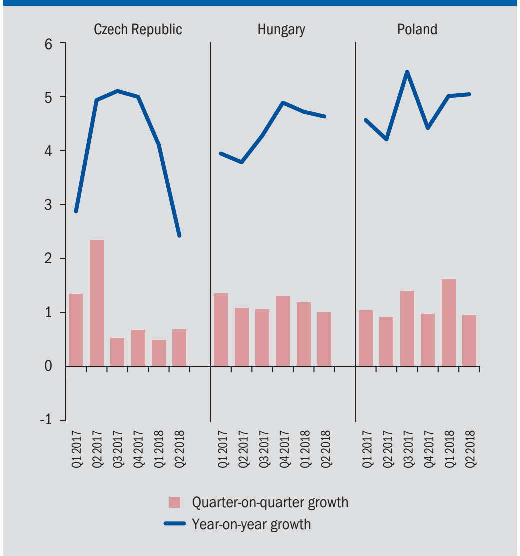
0.00%, 0.25% and -0.40% respectively. The Governing Council expects that rates will remain at their present levels at least through the summer of 2019, and in any case for as long as necessary to ensure the continued sustained convergence of inflation to levels that are below, but close to, 2% over the medium term.

Regarding non-standard monetary policy measures, the Governing Council said that net purchases under the asset purchase programme (APP), set at a monthly pace of €30 billion since January 2018, would continue at their current pace until the end of September 2018. After September 2018, the pace of the net asset purchases will be reduced to €15 billion until the end of December 2018. Subject to incoming data confirming the medium-term inflation outlook, the net purchases will then be ended. At the same time, the Governing Council intends to maintain its policy of reinvesting the principal payments from maturing securities purchased under the APP for an extended period of time after the end of the net asset purchases, and in any case for as long as necessary to maintain favourable liquidity conditions and an ample degree of monetary accommodation.

5 The Czech Republic, Hungary and Poland

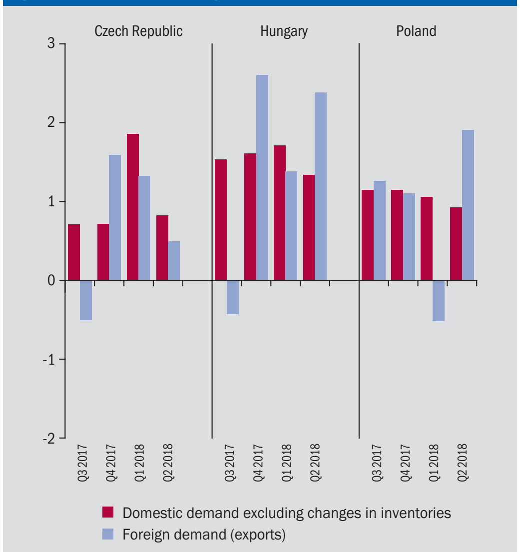
In the Czech Republic, annual GDP growth was 1.7 percentage points lower in the second quarter of 2018 than in the first quarter, at 2.4%, and in Hungary it was 0.1 percentage point lower, at 4.6%. In Poland the rate remained unchanged.

Chart 20 GDP (percentage changes)



Source: Eurostat.

Chart 21 Contributions to quarterly GDP growth (percentage points)

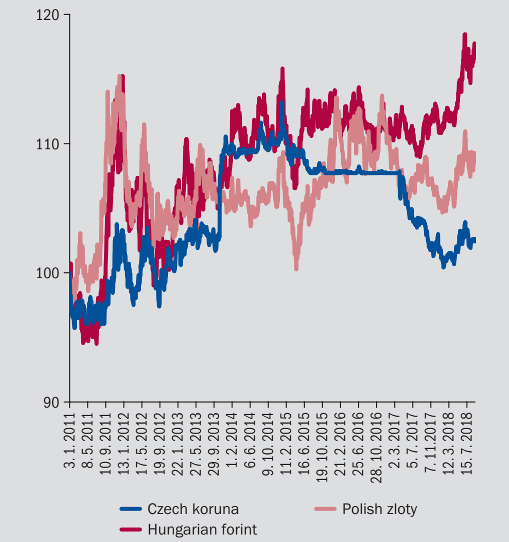


Sources: Eurostat and NBS calculations.

As for quarter-on-quarter GDP growth in the countries under review, only the Czech Republic recorded an increase in the second quarter; its growth rate of 0.7% was 0.2 percentage point higher compared with the previous quarter. GDP growth eased to 1.0% in both Hungary (down by 0.2 percentage point) and Poland (by 0.6 percentage point). In the Czech Republic, the acceleration of economic growth was driven by net exports, whose positive impact followed a negative contribution in the previous quarter. Government final consumption remained flat. The other components (household consumption, investment and changes in inventories) also contributed positively, but to a lesser extent than they did in the first quarter. In Hungary, the slowdown in GDP growth stemmed from a softening of investment demand and from a greater decline in inventories. The positive impact of private consumption remained unchanged. Government consumption's contribution turned from negative in the first quarter to neutral, and net trade's contribution turned from negative to positive. In Poland, the slowdown in economic growth was attributable mainly to a more pronounced decline in inventories and to a softening of investment growth. Net exports had a significantly positive impact on GDP growth, with export growth substantially exceeding import growth. The contributions of both private consumption and government consumption were moderately positive.

Annual consumer price inflation in all three reviewed countries was higher in June 2018 than in March 2018, with the Czech Republic recording an increase of 0.8 percentage point, to 2.4%, Hungary 1.2 percentage point, to 3.2%, and Poland 0.7 percentage point, to 1.4%. In **the Czech Republic**, the acceleration was caused mainly by energy prices, and to a lesser extent by prices of food (both processed and unprocessed) and services. Non-energy industrial goods inflation remained broadly unchanged. In July 2018, Czech consumer price inflation fell slightly compared with June, owing mainly to the impact of the food component, in particular unprocessed food prices. In **Hungary**, energy prices and, to a lesser extent, services prices accounted for most of the increase in headline inflation in the second quarter. By contrast, both processed food inflation and unprocessed food inflation decelerated, while non-energy industrial goods inflation remained flat. In July 2018, Hungarian headline inflation increased further, again owing mainly to the contribution of energy prices. There was also upward pressure, albeit less, from non-energy industrial goods inflation. In **Poland,** as in the other countries, the increase in consumer price inflation in the second quarter was driven mainly by energy prices. The non-energy industrial goods component continued to have a negative impact, but more moderate compared with March. Unprocessed food inflation eased significantly, and services inflation fell more moderately. In July, Poland's headline inflation was unchanged from its level in June.

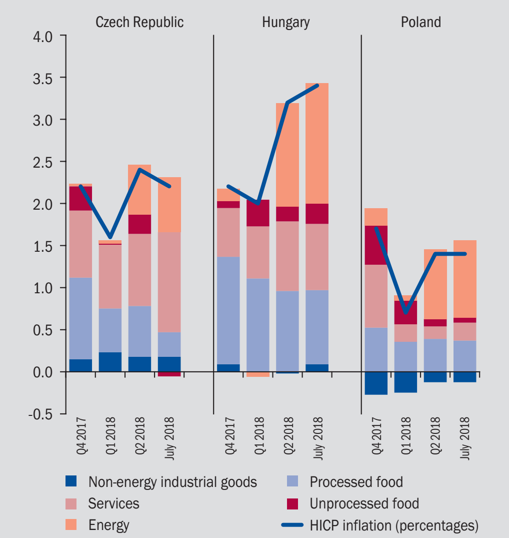
Chart 23 Exchange rate indices of national currencies vis-à-vis the euro (index: 3 January 2011 = 100)



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

The currencies of all three countries were trading weaker against the euro at the end of the second quarter than at the end of the first quarter: the Czech koruna had depreciated by 2.34%, the Hungarian forint by 5.65%, and the Polish zloty by 3.86%.

Chart 22 HICP inflation and its components (annual percentages; percentage point contributions)

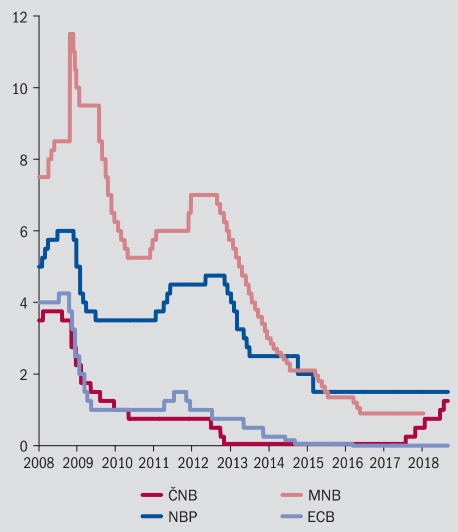


Sources: Eurostat and NBS calculations.

After a first quarter in which they displayed volatility, though not as a clear trend, the exchange rates of the reviewed currencies followed a marked depreciation course in the second quarter of 2018. This weakening against the euro stemmed mainly from investor aversion to financial market risk and the resulting increase in investor focus on dollar assets. Investment risk was affected by market expectations about the monetary policy stances of the world's major central banks (with divergence appearing between the Federal Reserve, which in June continued its monetary policy tightening by raising its key rate, and the ECB, which maintained monetary policy accommodation, albeit to a lessening extent), as well as by the risk that the escalation in protectionist measures within the world trading system could morph into a trade war, and by the geopolitical repercussions of Italy's election result. A subsequent factor that also affected exchange rates of emerging market currencies was the financial market turbulence in Turkey. The Czech central bank, at its monetary policy meeting in July and then again in August, even evaluated the koruna's weaker level as providing scope for monetary policy tightening via the interest rate component.

The Czech central bank was the only one of the three countries' central banks that adjusted its monetary policy rates in the second quarter of 2018. **Česká národní banka** (ČNB) decided to increase its base interest rate (the two-week repo rate) by 25 basis points, to 1.00%, with effect from 28 June 2018. At the same time, it increased the lombard rate, by 50 basis points, to 2.00% and kept the discount rate unchanged at 0.05%. In the February 2018 edition of its macroeconomic forecast (entitled the *Inflation Report*), ČNB resumed the publication of forecasts for the koruna-euro exchange rate. According to ČNB, the exchange rate outlook does not constitute a commitment by the central bank; it is merely a variable that is conditional on the assumptions adopted for the macroeconomic forecast. In the reasoning of its rate changes in June, ČNB stated that the koruna's weaker exchange rate was creating room to tighten monetary conditions in their interest rate component, thereby making it possible to take a further step towards the normalisation of monetary policy and also supporting the achievement of the financial stability objective. The central bank raised its key rates again in August, after discussing the latest macroeconomic forecast. In Hungary, the **Magyar Nemzeti Bank** (MNB) left its key interest rates unchanged in the second quarter of 2018, with the base rate, overnight collateralised lending rate and one-week collateralised lending rate all standing at 0.90%, and the overnight deposit rate in negative territory at -0.15%. In explaining its stance, the MNB Monetary Council reiterated that leaving interest rates unchanged and maintaining accommodative monetary conditions for an extended period of time (using also non-standard monetary instruments) was necessary in order for inflation to sustainably meet its target from mid-2019. The MNB maintained the cap on the use of its three-month deposit facility at HUF 75 billion in the second quarter. In addition, the MNB's Monetary Council set the average amount of liquidity to be crowded out for the second quarter at HUF 400-600 billion. The MNB continued implementing the following unconventional monetary policy measures: (i) unconditional interest rate swap facilities with five-year and ten-year maturities (with the maximum allotted amount set at HUF 600 billion for the first half of 2018); and (ii) a targeted programme for the purchase of mortgage bonds with a maturity of three years or more. **Narodowy Bank Polski** (NBP) left its monetary policy rates unchanged in the second quarter of 2018 (the reference rate has remained at 1.5% since 5 March 2015). In the central bank's judgement, taking current information into account, inflation will remain close to the inflation target over the projection period. As a result, according to the NBP, the current level of interest rates is conducive to keeping the Polish economy on a sustainable growth path and maintaining macroeconomic stability.

Chart 24 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	2017		2018		2019		2020	
IMF	July 2018	3.7	(-0.1)	3.9	(=)	3.9	(=)	-	-
OECD	May 2018	3.7	(=)	3.8	(-0.1)	3.9	(=)	-	-
EC[1)]	July 2018	3.9	(=)	4.2	(=)	4.1	(-0.1)	-	-
ECB[2)]	September 2018	3.8	(=)	3.9	(-0.1)	3.7	(-0.2)	3.7	(=)

Table 2 United States

	Release	2017		2018		2019		2020	
IMF	July 2018	2.3	(=)	2.9	(=)	2.7	(=)	-	-
OECD	May 2018	2.3	(=)	2.9	(=)	2.8	(=)	-	-
EC	May 2018	2.3	(0.1)	2.9	(0.6)	2.7	(0.6)	-	-
Federal Reserve	June 2018	2.3	(=)	2.85	(0.05)	2.4	(=)	1.9	(-0.05)

Table 3 Euro area

	Release	2017		2018		2019		2020	
IMF	July 2018	2.4	(0.1)	2.2	(-0.2)	1.9	(-0.1)	-	-
OECD	May 2018	2.6	(0.1)	2.2	(-0.1)	2.1	(=)	-	-
EC	July 2018	2.4	(=)	2.1	(-0.2)	2.0	(=)	-	-
ECB	September 2018	2.5	(=)	2.0	(-0.1)	1.8	(-0.1)	1.7	(=)

Table 4 Czech Republic

	Release	2017		2018		2019		2020	
IMF	April 2018	4.3	(0.8)	3.5	(0.9)	3.0	-	-	-
OECD	May 2018	4.6	(0.3)	3.8	(0.3)	3.2	(=)	-	-
EC	July 2018	4.3	(-0.1)	3.0	(-0.4)	2.9	(-0.2)	-	-
ČNB	May 2018	4.6	(-0.1)	3.2	(-0.7)	3.3	(-0.1)	3.4	-

Table 5 Hungary

	Release	2017		2018		2019		2020	
IMF	April 2018	4.0	(0.8)	3.8	(0.4)	3.0	-	-	-
OECD	May 2018	4.0	(0.1)	4.4	(0.8)	3.6	(0.8)	-	-
EC	July 2018	4.0	(=)	4.0	(=)	3.2	(=)	-	-
MNB	June 2018	4.0	(=)	4.4	(0.2)	3.5	(0.2)	2.8	(0.1)

Table 6 Poland

	Release	2017		2018		2019		2020	
IMF	April 2018	4.6	(0.8)	4.1	(0.8)	3.5	-	-	-
OECD	May 2018	4.6	(0.3)	4.6	(1.1)	3.8	(0.6)	-	-
EC	July 2018	4.6	(=)	4.6	(0.3)	3.7	(=)	-	-
NBP	July 2018	4.6	(=)	4.6	(0.4)	3.8	(=)	3.5	(-0.1)

1) Global economic growth excluding the EU.
2) Global economic growth excluding the euro area.
Notes: Data in brackets denote the percentage point change from the previous projection.
The IMF projections of July 2018 cover only large economies.
The European Commission's forecast of July 2018 covers only EU countries.