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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

Global economic growth was solid in the third quarter of 2018, but slightly lower than in the previous quarter. Leading indicator data are also pointing to a gradual, broad-based slowdown in the short term. The global economy remains marked by the escalation of trade tensions between the United States and China, although the recent period showed signs of a halt to further trade restrictions. At the same time, concerns are being raised about the ability of emerging market economies (EMEs) to adapt to gradual monetary policy normalisation in advanced economies and to the consequent tightening of financial conditions. Recent market volatility in certain EMEs, particularly Argentina and Turkey, indicated potential repercussions that could result in a sudden and substantial repricing of risks in global financial markets.

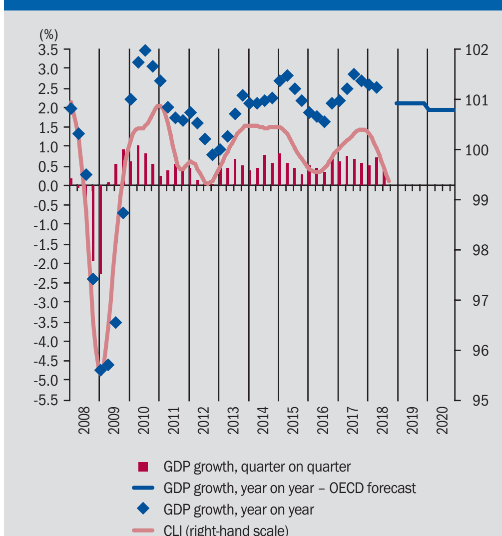
Looking at advanced economies in the third quarter, economic growth in the United States was lower than its level in the previous quarter, but remained robust, with the country benefiting from favourable labour market trends and strong fiscal expansion. The slowdown was attributable to net exports, which had a negative impact on GDP growth owing to an acceleration of import growth (probably caused by firms stocking up ahead of the introduction of further trade barriers against China). The US economy's growth was also, though, dampened by investment demand. Growth was supported by private consumption and a sharp rise in inventories. When the effects of the fiscal stimulus have faded, US economic growth is expected to be decelerating for an extended period owing to the tightening of monetary policy. Euro area GDP growth also eased in the third quarter, as net exports, reflecting weaker export performance, had a significant dampening effect. There was also slower growth in both investment and consumer demand, and only inventory growth had an appreciable positive impact on overall economic growth. The euro area's performance in the third quarter was affected by a decline in automotive industry production, related to the transition to new emission standards. Going forward, euro area GDP growth is expected to be driven by domestic demand, in particular household consumption growth resulting from accomodative monetary policy; at the same time, favourable financnial conditions are expected to support investment demand. After its strong growth in the second quarter, economic activity in Japan contracted in third quarter as a result of one-off factors. Adverse weather conditions and natural catastrophes during the summer led to a decline in investment activity, as well as in export performance. There was also, however, a slight drop in private consumption. Short-term indicator data imply that the Japanese economy has returned to a growth path in the last quarter. In the next period, despite the effects of accommodative monetary policy, Japan's economic growth is expected to be kept moderate by declining spare capacity and the fading of the fiscal stimulus. The United Kingdom's economic growth, supported by household consumption and in particular an acceleration of exports, had a positive impact on global economic growth in the third quarter. With imports stagnating, net exports also contributed positively to UK growth. After falling in each of the previous two quarters, fixed investment increased; at the same time, however, inventories fell sharply. Looking ahead, UK economic growth is expected to remain subdued, owing to weak private consumption growth that is reflective of muted real wage growth. There is also high uncertainty surrounding business investment and net exports, whose impact may be moderated amid declining foreign demand.

As regards emerging market economies, China's GDP growth slowed in the third quarter, possibly due to the repercussions of its trade war with the United States as well as to the process of gradual deleveraging. In year-on-year terms, China's economy grew more slowly than at any time since the financial crisis. Nevertheless, China's GDP growth in the first three quarters of 2018 was at or above the official target, which suggests that the growth target for the year as a whole will be met. The Chinese economy is expected to lose further momemtum in coming years owing to structural changes in the economy. It is assumed, however, that domestic policy will continue to support economic growth similarly to how it has been doing recently, by

reducing reserve requirement ratios in order to increase market liquidity. In India, too, GDP growth moderated in the third quarter, as private consumption growth eased and the farm sector's performance weakened. Nevertheless, the economy's overall growth remained robust, ensuring that India retains its place as the world's fastest growing major economy, ahead of China. In the period ahead, India's GDP growth should be boosted by business investment and exports, as these will benefit from such structural reforms as the new law on insolvency and bankruptcy, the smoother application of the tax on goods and services, and bank recapitalisations. Russia's economic growth also slowed in the third quarter, according to preliminary data. This result indicates a softening of activity growth in retail trade and manufacturing, as well as declining activity in agriculture and construction. The Russian economy's gradual recovery is expected to continue, supported by domestic demand in an environment of increasing disposable income and credit growth. The economy should also benefit from planned fiscal and structural reforms, as well as from government consumption, which is rising as a result of higher oil revenues. An EME that contributed positively to global economic growth in the third quarter was Brazil. Its GDP growth was higher compared with the previous quarter, when growth was dampened by the impact of a truckers' strike. The increase in GDP was the highest since the first quarter of 2017 and was supported by investment recovery and by government consumption. Private consumption also picked up, after remaining flat in the previous quarter. On the other hand, net trade had a negative impact, as import growth far exceeded export growth. Improving labour market conditions, credit growth, and continuing government consumption growth are expected to further bolster Brazil's economic recovery.

Economic activity growth across the OECD area fell to 0.5 % in the third quarter of 2018, down from 0.7 % in the previous quarter. In year-on-year terms, growth moderated from 2.5% in the second quarter to 2.4 % in the third quarter. The Composite Leading Indicator for the OECD area[1] fell in the third quarter after also falling in the previous quarter, and its downward trend continued in October; this implies a global economic slowdown in the short term. Further signs of a global slowdown are provided by the Global Composite Purchasing Managers' Index (PMI), whose level in October was below its average for the third quarter of 2018.

Chart 1 GDP growth and the CLI for the OECD area



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

Global consumer price inflation was relatively stable in the third quarter of 2018. In the OECD area, the inflation rate edged up from 2.8% in June to 2.9% in September. The increase was attributable to food prices and to core inflation, which in the same period increased from 2.0% to 2.3%. On the other hand, the energy component had a dampening effect on OECD headline inflation, as the falling rate of growth in energy commodity prices quickly passed through to energy prices. In October, OECD headline inflation continued rising, up to 3.1%; in this case, however, the increase was caused by a pick-up in energy price inflation. Core inflation remained unchanged and food inflation eased.

1 The CLIs for OECD countries are published on a monthly basis, and the most recent, published in December 2018, are for the period up to October 2018.

2 Commodities

The average commodity price index was slightly lower in the third quarter 2018 than in the second quarter, owing mainly to a decline in the average price of non-energy commodities. By contrast, energy commodity prices increased slightly.

Looking at energy commodities, the average price of a barrel of Brent crude oil remained relatively stable in the third quarter. From July to mid-August the oil price had a largely downward trend, as the United States' imposition of tariffs on imports from China may have indicated a reduction in global demand. The oil price was also under downward pressure from OPEC's decisions to loosen production quotas. From mid-August until the end of September, oil prices followed a strong upward trend, mainly caused by continuing tightness in the global market. The price surge stemmed partly from political tensions in Venezuela as well as from impending US sanctions on Iran, which forced oil traders to find alternatives to Iranian oil even before the sanctions came into force in November. In addition, markets were concerned about whether OPEC, OPEC's allies, and the United States would be able to meet market shortfalls. In October and November, oil prices plunged due to rising US output as well as the exempting of certain countries from the reimposition of sanctions on Iran, which improved market supply outlooks.

Expectations that global demand growth would be dented by the US-China trade war were also reflected in non-energy commodity prices, specifically in falling average metal prices. Meanwhile, the PMI-indicated slowdown in the global manufacturing industry put downward pressure on prices of zinc, copper, aluminium and nickel. The drop in aluminium prices was further amplified by growth in aluminium exports from China, as well as by hopes for the lifting of US sanctions against Russian producers. Copper prices continued responding to receding fears that workers would go on strike at the worlds largest copper mine in Chile. In October, after their declines in the previous quarter, metal prices rebounded somewhat on news that incoming US tariffs on Chinese imports would be imposed at a rate of only 10%, not 25% as had originally been expected. The metals that recorded the largest prices rises in this period were copper and zinc, partly also because the reduction in their stocks was indicative of continuing demand. The trade tensions between the US and China also had an impact on food commodity prices. Soybean prices in particular illustrate how trade disputes can affect prices. After the United States introduced restrictions on Chinese imports in July, China responded with retaliatory measures that included the imposition of tariffs on China's soybean imports from the United States. As a result, there was a sharp drop in prices of soybeans, which account for a significant share of US agricultural exports. Other food commodities that fell sharply in price during the period under review included cocoa, coffee, maize, sugar and pigmeat. By contrast, beef and wheat prices increased. In October, food commodity prices largely stabilised and, with the exceptions of cocoa, all of the above-mentioned food commodities began to increase in price.

3 The United States

In the United States, the annualised rate of GDP growth slowed to 3.5% in the third quarter of 2018, from 4.2% in the previous quarter. US GDP growth nevertheless remained robust, owing mainly to the impact of the fiscal stimulus. The year-on-year growth rate increased slightly, from 2.9% in the second quarter to 3.0% in the third.

The continuation of strong economic growth in the period under review was mostly underpinned by private consumption growth, which remained elevated but slightly lower than its level in the previous quarter. The main contributor to this consumption growth remained household expenditure on non-durable goods. The fiscal stimulus continued to have a positive impact on government spending and investments, particularly at the federal level in the area of national defence. On the other hand, investment demand growth moderated, with fixed investment increasing at its weakest pace for almost three years. A relatively large slowdown in non-residential investment growth, and a pronounced decline in residential investment may have stemmed from the gradual tightening of financial conditions. Net exports had a negative impact on GDP growth, as a slump in exports was accompanied by stronger import growth; this may have been stimulated by the frontloading of imports from China in order to avoid future tariffs on them. The negative impact of net exports was largely compensated for by changes in inventories, whose positive contribution to GDP growth was more than two percentage points. This situation of strong imports coupled with rising inventories was in contrast to the previous quarter, when strong exports reduced inventories. The fiscal stimulus was the cause of the US economy's robust expansion in the third quarter, as it was in the previous quarter. After its positive effects have faded, however, and with the impact of rising interest rates, economic activity growth may stall next year.

International trade tensions continued to escalate in the third quarter. During July and August, the US Administration imposed import tariffs on more than 1,000 Chinese products worth USD 50 billion in total.[2] In September, the US proceeded with its most extensive round of tariffs so far, levying duties on USD 200 billion worth of Chinese goods[3] (Box 1).

Consumer price inflation in the United States stopped accelerating in the third quarter of 2018, after following an upward trend from the beginning of the year. In July the headline inflation rate was still just below 3% (2.9%), but it slowed significantly in the next months; the most pronounced drop was in September, when the rate fell to 2.3%. The energy component was the primary cause of this disinflationary trend, with energy prices responding relatively quickly to changes in energy commodity prices. Core inflation items also, however, had a downward impact on headline inflation. After reaching an almost ten-year high of 2.4% in July, core inflation moderated in subsequent months, down to 2.2% in September. This drop stemmed mainly from decreasing prices of clothing and footwear (possibly reflecting the impact of dollar appreciation on import prices) as well as from a lower rate of increase in prices of healthcare goods and services. Food price inflation remained stable throughout the third quarter so had a minimal impact on headline inflation movements during this period. In October, food inflation eased and core inflation fell to 2.1%. Even so, headline inflation rose to 2.5% in October under upward pressure from energy inflation, which almost doubled. The elevated inflation rate in recent months testified to increasing price pressure in the economy and led to a further tightening of monetary policy.

At its 31 July to 1 August meeting, the US Federal Open Market Committee (FOMC) decided to leave the target range for the federal funds rate unchanged at 1.75% to 2.00%. At its meeting in September, however, in view of realised and expected labour market developments and inflation, the Committee decided to raise the target range to 2.00% to 2.25%. The Committee made no further change to the policy rate when it met in November.

2 US tariffs on USD 34 billion and USD 16 billion of Chinese imports entered into force on 6 July 2018 and 23 August 2018 respectively.

3 On 24 September 2018 the US imposed 10% tariffs on USD 200 billion worth of Chinese imports, stating that the tariff rate would be raised to 25% from 1 January 2019.

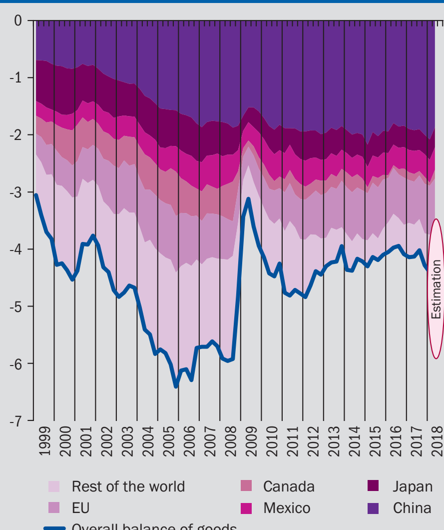
Box 1

THE TRUMP TARIFFS – A SUCCESS?

The United States has had a large trade deficit in recent decades, and although this deficit shrank after the financial crisis, the United States still has one of the highest current account deficits among advanced economies (Chart A). Looking at the bilateral trade deficits of the United States, the one with China has increased the most in the last 15 years, but those with many other countries have also been negative for a long time. According to the US Administration, the high bilateral deficits result from unfair business practices by the United States' trading partners, and it was for this reason that the Trump administration announced in 2017 its intention to reduce them.

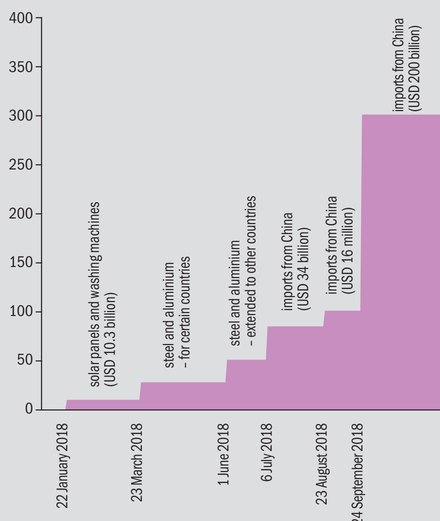
The first measure aimed at protecting domestic industry was introduced in January 2018: import tariffs on solar panels and washing machines (Chart B). The measure had a relatively low volume (around USD 10 billion per year) and affect only a tiny share of total US imports (around 0.4%). This measure was the United States' response to the Chinese government's subsidisation of Chinese exporters, which had been detrimental to US firms. In March 2018 the US Administration imposed tariffs of 25% on imports of steel and 10% on imports of aluminium, justifying the move on grounds of national security. Some trading partners were exempted from the tariff temporarily (until 1 May 2018), including Canada, Mexico, the EU, Australia, South Korea, Brazil and Argentina. The only one of those countries for which the exemption was made indefinite before that deadline was South Korea, after it agreed to a revision of the United States-Korea Free Trade Agreement. Agreements were later also reached with Argentina, Brazil and Australia, granting them an indefinite exemption from the tariff in exchange for quotas on their exports of steel to the United States, which had been swelling US steel inventories. Canada, Mexico and the EU were given additional time to negotiate permanent exemptions from the tariffs, but with no deal being reached by the deadline, the tariffs were imposed on these countries with effect from 1 June 2018. These tariffs concerned US imports worth around USD 40 billion, again only a small share of to-

Chart A US balance of goods with selected countries (percentage of GDP)



Sources: Macrobond and NBS calculations.

Chart B Overview of import tariffs imposed by the United States on trading partners (USD billions)



Source: PIIE.

tal US imports. The US Administration imposed further tariffs in July and August 2018, on more than 1,000 Chinese products; the tariffs in July affected USD 34 billion worth of goods, and those in August, USD 16 billion worth. In justifying the move, the US side claimed China was engaging in unfair business practices related to technology transfer, intellectual property, and innovation. In mid-September the US made its most extensive attempt yet to curb China's acquisition of dominant market positions, when it imposed a 10% tariff on USD 200 billion worth of Chinese imports (and said it would be increased to 25% from 1 January 2019). With these measures, the total amount of imports affected by the 2018 US tariff rounds was around USD 300 billion, or approximately 12% of total imports into the United States.[4]

Trading partners have responded to the US tariffs by taking retaliatory measures. Canada, China, the EU, Mexico and Turkey reacted to the US steel and aluminium duties by imposing tariffs on their imports of US steel and aluminium, but also on imports of US agricultural and food products and US consumer goods. China responded promptly to the US measures in July and August by imposing like-for-like import tariffs,[5] and in September it levied import duties on a further USD 60 billion worth of US merchandise. The retaliatory measures that US trading partners had taken by mid-December 2018 affected around 8% of total US exports.[1]

Besides the measures it has already adopted, the United States has said it may take further steps to improve its bilateral deficits. In March 2018 the US launched an investigation into whether imports of vehicles and vehicle parts represent a threat to national security. A tariff of 25% on such imports was under consideration but has not as yet been imposed. Such measures would hit Canada and Mexico hardest, owing to integrated supply chains and these countries' heavy dependence on the US market. This area of trade is expected to be regulated by the new United States–Mexico–Canada Agreement (USMCA), which is set to replace the North American Free Trade Agreement (NAFTA). The deal should, among other things, boost domestic production of cars and lorries and introduce updated protection measures for intellectual property. Under the USMCA, cars and lorries qualify for zero tariffs if at least 75% of their components are manufactured in the United States, Mexico or Canada. This measure would therefore provide an incentive to make cars in North America. Leaders of the three countries signed the USMCA at the end of November, while attending a G20 summit in Buenos Aires. The agreement still needs to be ratified by lawmakers in each of the countries before it enters into force. There remains the possibility of tariffs (or quotas) being levied on vehicles and vehicle parts made in other trading partners (for example, the EU, Japan, South Korea), and this, from a longer-term perspective, given the automotive industry's strong integration into global value changes, represents a significant risk to global trade and economic activity.

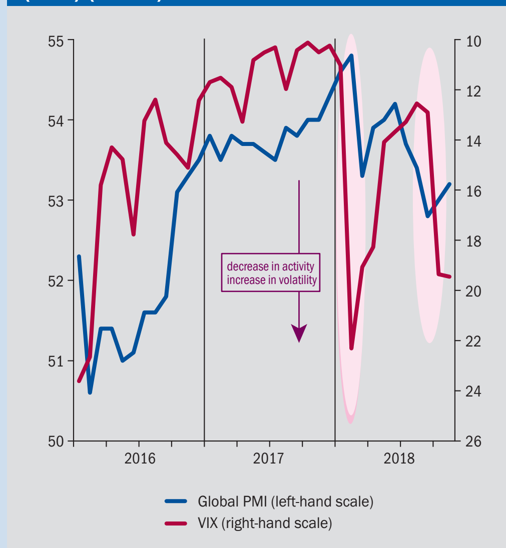
During bilateral talks held at the end of the G20 summit in Argentina, US and Chinese leaders agreed to a moratorium on new trade barriers. Back in July 2018, US President Donald Trump had indicated his readiness to impose duties on all imports from China[6] and repeated his threat just a few days before the summit; after the meeting, however, the President announced that the recently introduced 10% tariff on USD 200 billion worth of Chinese imports would not be raised to 25% from 1 January 2019 as originally planned. According to a statement issued by the US Administration on 1 December, China agreed to purchase from the United States a still to be specified amount of agricultural, energy, industrial and other products in order to reduce the trade imbalance between the two countries. Both sides also pledged to immediately begin negotiations on structural changes with respect to forced technology transfer, intellectual property protection, non-tariff barriers, cyber intrusions and cyber theft, services, and agriculture. Both sides agreed to endeavour to have this transaction completed within the next 90 days. If the parties are unable to reach an agreement by the end of this period of time, the 10% tariffs will be raised to 25%.

It would clearly be premature at this stage to assess how the import tariffs will affect the US

4 Peterson Institute for International Economics (PIIE).
5 Since these measures had a sizeable impact on US farmers (especially soybean exporters), the US Administration announced it would compensate farmers with direct payments.
6 This would extend import tariffs to USD 267 billion worth of Chinese capital and consumer goods that have not been affected by the previous tariff rounds (including, for example, mobile phones, laptop computers, and clothing).

trade deficit. The measures adopted in the first quarter of 2018 were only minor and did not have a significant impact on trade in goods. In the second quarter, however, when the US imposed tariffs on steel and aluminium, there was a marked decrease in US balance of goods deficit with all the countries or trade groupings referred to in this evaluation. The geographical breakdown of US foreign trade for the third quarter of 2018 is not yet available; nevertheless, the aggregate national accounts data indicate that the most extensive round of US tariffs against China, imposed in September, and the announced further restrictions on imports into the United States have resulted in substantial frontloading by firms and in strong import growth[7] (Chart A). This, together with a slump in exports, has significantly increased the US balance of goods deficit, to 4.5% of GDP. The aim of the US Administration in taking these measures was to reduce the trade deficit, but so far it has not achieved that. As for their impact on the global economy, it has not so far been significant, since the US Administration is supporting the domestic economy through fiscal stimulus and China is also deploying various political tools to bolster growth. On the other hand, the imposition of trade barriers has, to a large degree, been reflected in rising stock market volatility and in declining global indicators of economic activity (Chart C), which may have negative repercussion on the world economy via the activity of global investors.

Chart C Trends in global economic activity (Global PMI) and stock market volatility (VIX) (index)



Source: Macrobond.

7 *US imports at constant prices increased in the third quarter of 2018 by more than 10% on an annualised basis.*

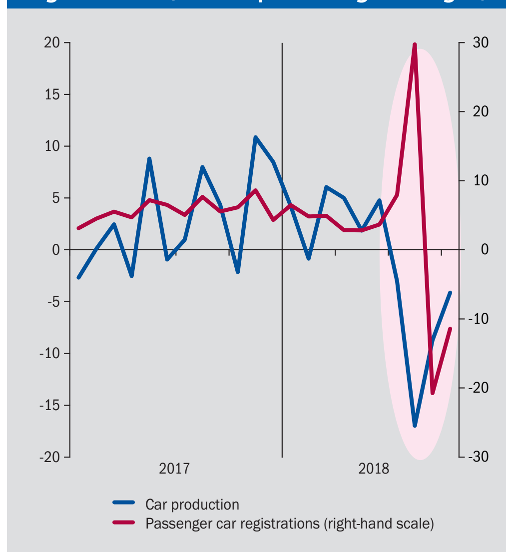
4 The euro area

Euro area economic activity growth moderated notably in the second quarter of 2018. GDP growth decreased to 0.2%, quarter on quarter, after growth of 0.4% in the previous two quarters. Looking at the larger national economies within the euro area, GDP fell, quarter on quarter, in Germany and Italy, by 0.2% and 0.1% respectively (after increasing in the previous quarter by 0.5% and 0.2%). In the Netherlands, activity growth slowed (by 0.5 percentage point, to 0.2%), while in Spain it remained unchanged (0.6%). France was the sole major economy whose GDP growth accelerated in the third quarter (by 0.2 percentage point, to 0.4%). In year-on-year terms, euro area GDP growth reflected its quarter-on-quarter slowdown, moderating by 0.6 percentage point to 1.6%.

All components apart from changes in inventories contributed to the slowdown in euro area economic growth. Net exports had the largest dampening effect, since although import growth slowed slightly, exports contracted by 0.1% (after increasing by 1.0% in the previous quarter). Both consumer demand and investment demand continued to grow, albeit more slowly compared with the previous quarter. Private consumption growth moderated for a second successive quarter, to 0.1% (after a rate of 0.2% in the second quarter). Government consumption growth also stalled. The growth rate for investment demand eased quite substantially (to 0.2%, from 1.5% in the second quarter), perhaps related to firms' postponing investment decisions amid rising tensions, particularly in relation to global trade. Changes in inventories provided the largest positive contribution. Euro area economic growth in the third quarter reflected the impact of a dip in car industry production, related to the transition to new emission standards. This is expected to have weighed on export performance as well as, to some extent, consumption.

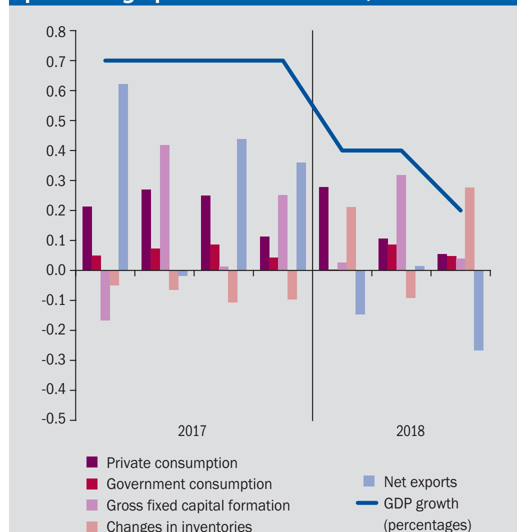
Consumer spending growth decelerated despite still being supported by low interest rates. The continuing upward trend of the saving ratio indicated by developments in the second quarter may have been related to weaker growth in private consumption.[8] The third quarter also saw a pronounced slowdown in annual employment growth (to 0.2%, from 0.4% and 0.5% in the previous two quarters), which may likewise have dampened consumer spending growth. Another

Chart 3 Car production and passenger car registrations (annual percentage changes)



Sources: Macrobond and NBS calculations.

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



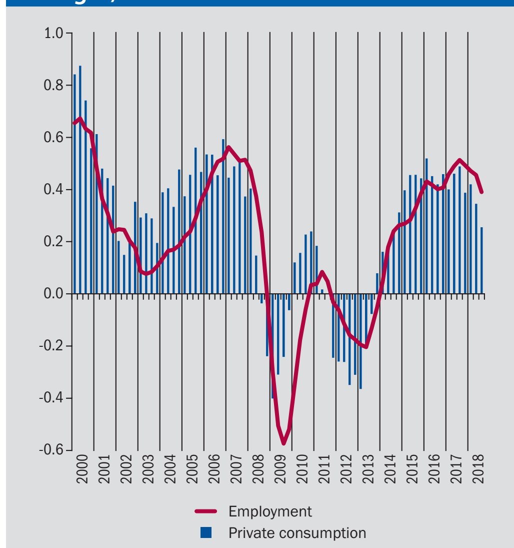
Sources: Macrobond and NBS calculations.

8 *Saving ratio data for the third quarter were not available by the cut-off date for this report.*

factor, however, which probably contributed to lower private consumption growth in the third quarter was a drop in car sales (resulting from production bottlenecks). According to survey results, households' intentions to make major purchases did not change significantly through October, but they fell noticeably in November. Their level, however, continues to imply scope for an increase in consumer spending growth.

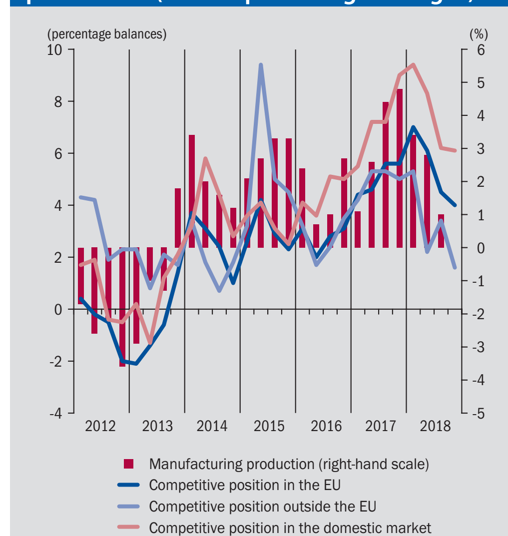
Industrial firms' assessments of their competitive position continued to deteriorate in the fourth quarter and did so in respect of all markets. Their most favourable assessments concerned com-

Chart 4 Private consumption and employment (quarter-on-quarter percentage changes)



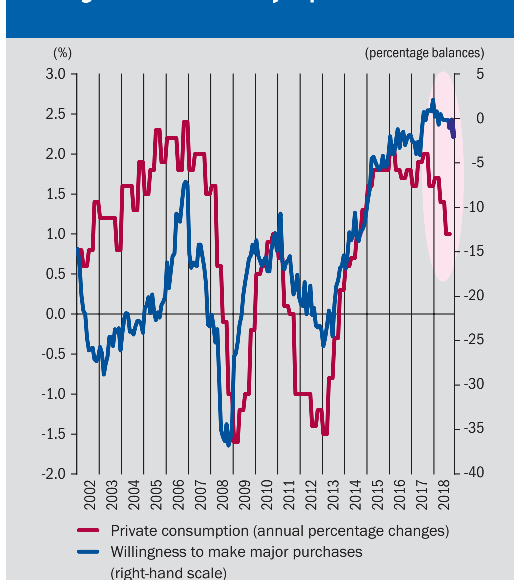
Source: Macrobond.
Note: Calculated from moving averages for four quarters.

Chart 6 Industrial competitiveness (percentage balances) and manufacturing production (annual percentage changes)



Sources: European Commission, Eurostat and NBS calculations.

Chart 5 Private consumption and consumers' willingness to make major purchases



Source: Macrobond.

Chart 7 Export expectations in industry (percentage balances) and manufacturing production (annual percentage changes)

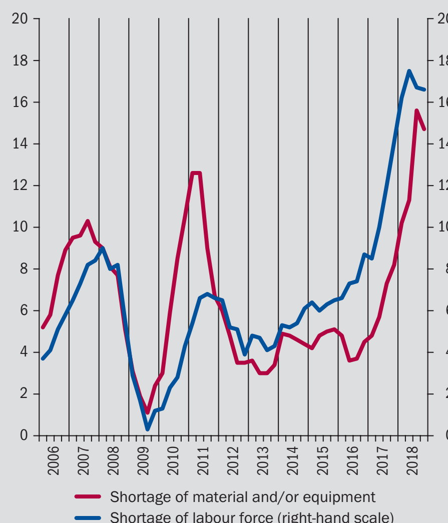
Sources: European Commission, Eurostat and NBS calculations.

petitiveness in domestic markets, while competitiveness in extra-EU markets was seen in the least favourable terms, probably owing to persisting trade tensions and protectionism risks. As well as having a less positive view of their competitive position, firms also dialled down their export expectations, which implies that export activity's contribution to euro area economic growth will be lower in the next period.

Industrial firms' most recent assessments of the factors limiting their production also point to a moderate cooling of economic activity. Survey results for the fourth quarter, as for the previous quarter, showed an increase in the percentage of respondents reporting 'financial constraints' as a factor limiting production. This may have been related to the ECB's announced intention to end its asset purchase programme. The importance of 'insufficient demand' increased moderately, but this factor nevertheless remains at historically low levels and is not expected to weigh significantly on economic growth. As for production factors – 'shortage of material and/or equipment' and 'shortage of labour force' – there was a slight drop in the share of respondents that felt these were limiting production; this implies an easing in labour market tightening as well as less pressure to increase investment in equipment. At the same time, however, the importance of these production factors remains at historically elevated levels that point to persisting demand for labour and continuing growth in investment demand.

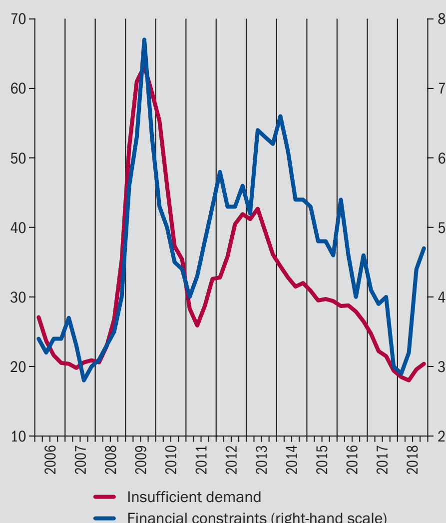
The unemployment rate edged down by 0.1 percentage point in the third quarter, to 8.1% – its lowest level for ten years – and it remained at that level in October. Expectations for future employment had a downward trend in all sec-

Chart 9 Factors limiting production in industry (percentages)



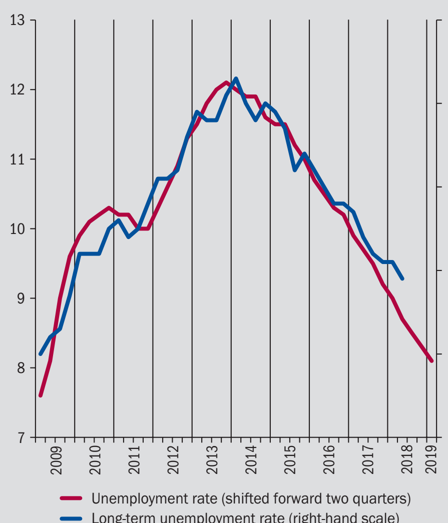
Source: Macrobond.

Chart 8 Factors limiting production in industry (percentages)



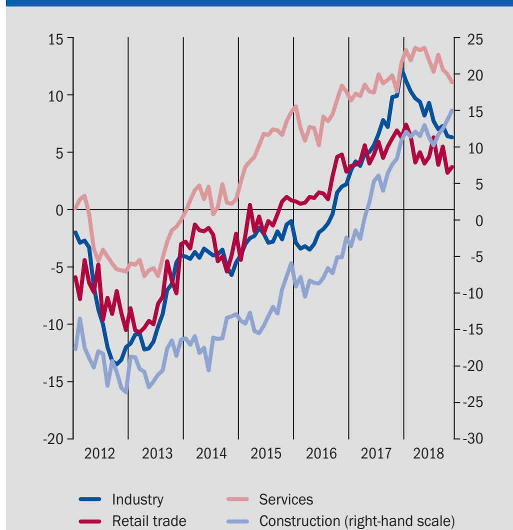
Source: Macrobond.

Chart 10 Unemployment and long-term unemployment rates (percentages)



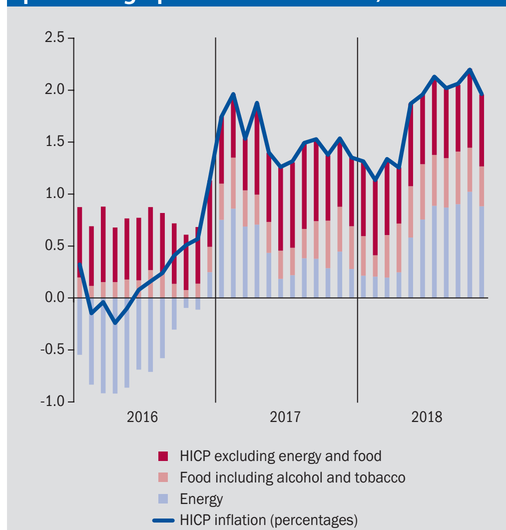
Source: Macrobond.

Chart 11 Employment expectations by sector (percentage balances)



Source: Macrobond.

Chart 12 HICP inflation and selected components (annual percentage changes; percentage point contributions)



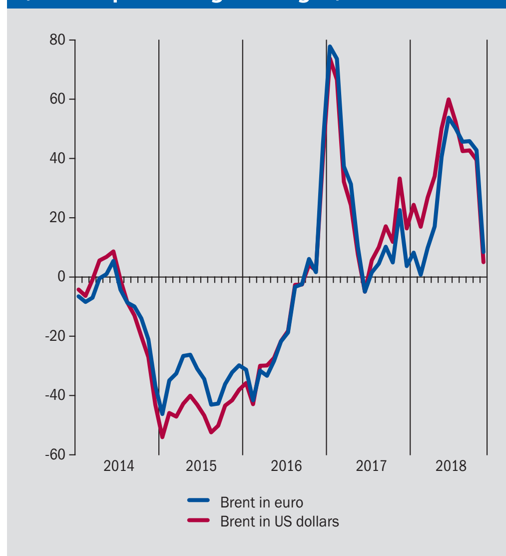
Source: Macrobond.

tors other than construction. This situation may reflect, on the one hand, the impact of labour shortages, and, on the other hand, the weakening of economic activity growth supply and lower need for production capacity utilisation. In the construction sector, by contrast, employment expectations continued to increase, indicating the continuation of relatively strong demand for construction investment.

Euro area annual HICP inflation continued to accelerate moderately in the third quarter of 2018, supported by increasing energy inflation. Other components, with the exception of services prices, had a slightly negative impact. The headline rate was 0.1 percentage point higher in September than in June, at 2.1%. Core inflation (HICP excluding energy and food) remained unchanged during the same period, at 0.9%. In October, headline inflation increased further, to 2.2%, owing not only to higher energy prices but also to the fact that core inflation increased by 0.2 percentage point (to 1.1). November saw core inflation edge back down (to 1,0%), and with both energy and food inflation also declining, headline inflation fell to 2.0%.

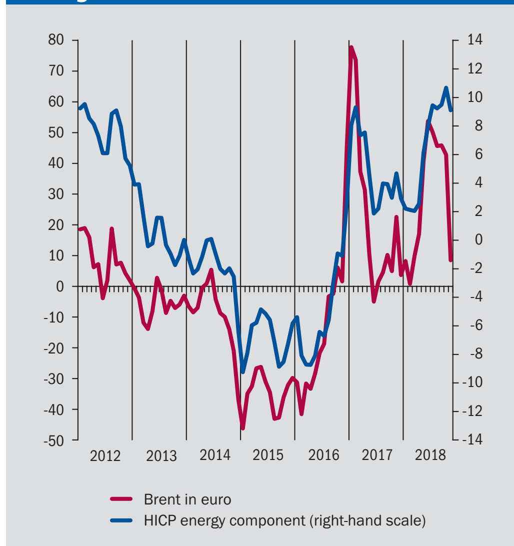
The gradual rise in oil prices in the second quarter of 2018, together with the base effect of their decline in June 2017, resulted in oil inflation rising sharply in June. From the second half of August, oil prices began rising to levels

Chart 13 Oil prices in euro and US dollars (annual percentage changes)



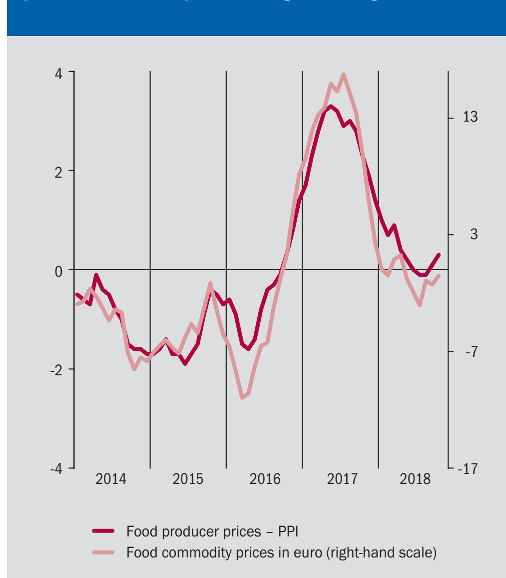
Sources: Macrobond and NBS calculations.

Chart 14 Oil prices in euro and the HICP energy component (annual percentage changes)



Sources: Macrobond and NBS calculations.

Chart 15 Food commodity and producer prices (annual percentage changes)

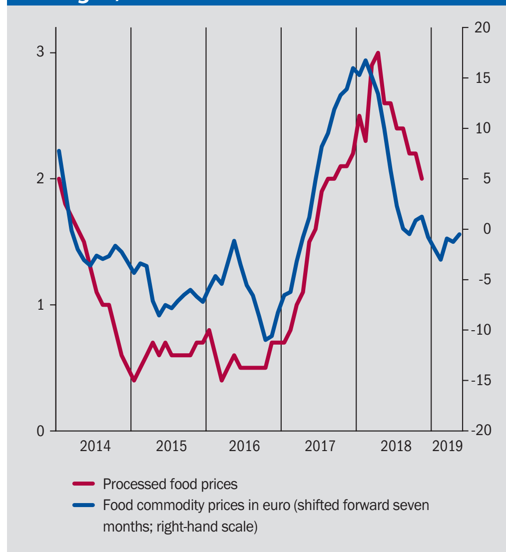


Source: Macrobond.

in excess of USD 80 per barrel, so the annual rate of increase in oil prices remained elevated in the third quarter, at between 45% and 50%. This increase passed through to consumer energy prices and contributed to an acceleration of headline inflation. In early October, however, oil prices began to fall quite sharply, and in November they declined to below USD 60 per barrel. Their annual rate of increase therefore slowed markedly (from over 40% to less than 9%); however, the impact of this slowdown on consumer prices has so far been only slight and is expected to become more pronounced only in subsequent months.

Annual food inflation stood at 2.6% in September 2018, 0.1 percentage lower than in June. This reflected a slowdown in processed food inflation, whose impact was only partly offset by an increase in unprocessed food inflation. From October, however, unprocessed food inflation also began to moderate, largely owing to lower rates of change in fruit and vegetable prices. Thus, total food inflation slowed to 2.0% in November. The moderation of food inflation reflected the pass-through of European food commodity prices, whose annual rate of decline became more negative in July and then gradually less negative in subsequent months. The pass-through to food producer prices was almost immediate. Commodity price trends have been passing through to processed food prices with a lag and without yet fully transmitting their past decline.

Chart 16 Food commodity prices and processed food prices (annual percentage changes)

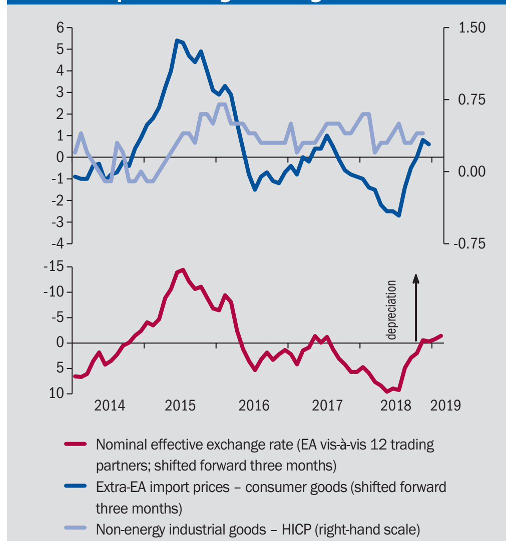


Source: Macrobond.

Hence processed food prices can be expected to come under downward pressure in coming months.

Core inflation was a relatively subdued 0.9% in September, unchanged from its level in June. The services component was the same in September as in June, at 1.3%, though it increased by 0.1 percentage point in July before coming back down. Non-energy industrial goods inflation also accelerated in July and then moderated in the next two months, down to 0.3% in September (just below the June level of 0.4%). In October, HICP inflation excluding energy and food increased to 1.1%, owing to rises in non-energy industrial goods inflation (caused mainly by increases in clothing and footwear prices) as well as in services inflation (package tour prices). In November, services inflation slowed, and so did core inflation (to 1.0%). This slowdown was probably attributable to previous months' higher rates of increase in volatile components of services inflation (specifically package tour prices).[9] The annual growth rate of the ECB's indicator of negotiated wages eased slightly in the third quarter, yet still implies that wage growth will have a positive impact on both core inflation, via services inflation. At the same time, recent trends in the euro's exchange rate – weakening year-on-year appreciation, or slight depreciation – had an upward impact on the rate of change in import prices for consumer goods. Their declining trend, dating back to June 2017, began to moderate from May 2018 and came to an end in July. These import prices increased moderately in subsequent months. Hence import prices may have been putting some upward pressure on non-energy industrial goods inflation.

Chart 18 Non-energy industrial goods prices and the nominal exchange rate (annual percentage changes)

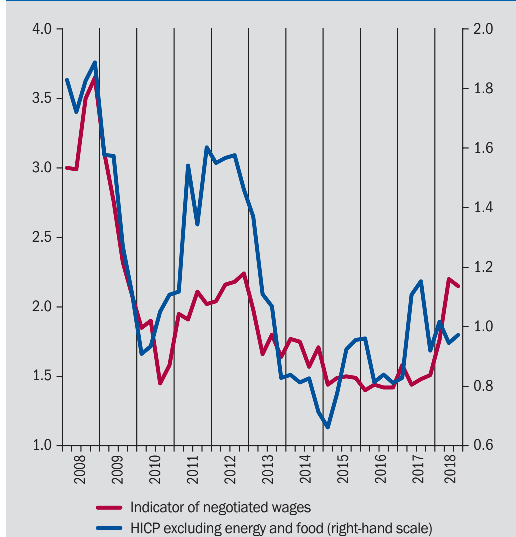


Source: Macrobond.
Note: Positive values for the exchange rate denote depreciation of the euro.

Selling price expectations have shown considerable volatility in recent months, but their broad trend has been moderately upward. The ECB Survey of Professional Forecasters (SPF) shows a slight increase of 0.1 percentage point in inflation expectations for one and two years ahead respectively. Therefore, the inflation expectations have in the past two years increased by 0.5 and 0.4 percentage point respectively.

At its monetary policy meetings between June and December 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%

Chart 17 Negotiated wages indicator and core inflation (annual percentage changes)



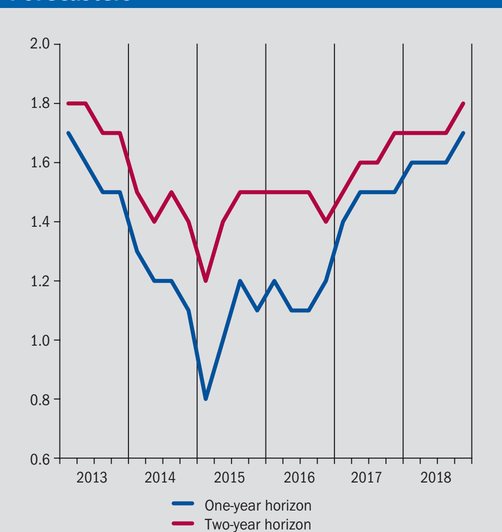
Source: Macrobond.

9 *Further details on the composition of HICP inflation, are due to be released after the cut-off date for this report.*

Chart 19 Price expectations in industry, services and retail trade (percentage balances)

Source: Macrobond.

Chart 20 Expectations for HICP inflation according to the ECB's Survey of Professional Forecasters



Source: Macrobond.

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 ECB continued to make net purchases under the asset purchase programme (APP) at the monthly pace of €30 billion until the end of September 2018 (the purchases had been set at that pace since January 2018). From October to December 2018, the monthly pace of the net purchases was reduced to €15 billion. At its meeting in December, the Governing Council decided to end net purchases under the APP in December 2018, and at the same time to enhance its forward guidance on reinvestment. Accordingly, the Governing Council intends to continue reinvesting, in full, the principal payments from maturing securities purchased under the APP for an extended period of time past the date when it starts raising the key ECB interest rates, and in any case for as long as necessary to maintain favourable liquidity conditions and an ample degree of monetary accommodation. The ECB also published the Governing Council's decision on the technical parameters of the reinvestments.

Box 2

ESTER (EURO SHORT-TERM RATE)[10]

Benchmark interest rates play an important role in the economy and, even more so, in the financial and banking system. They are used as benchmarks in contracts linked to floating interest rates, in the valuation of balance sheet items in accounting, and in derivatives markets. Benchmark rates are a means for central banks to monitor the implementation and transmission mechanism of monetary policy. One of the most widely used overnight benchmarks is EONIA (euro overnight index average).

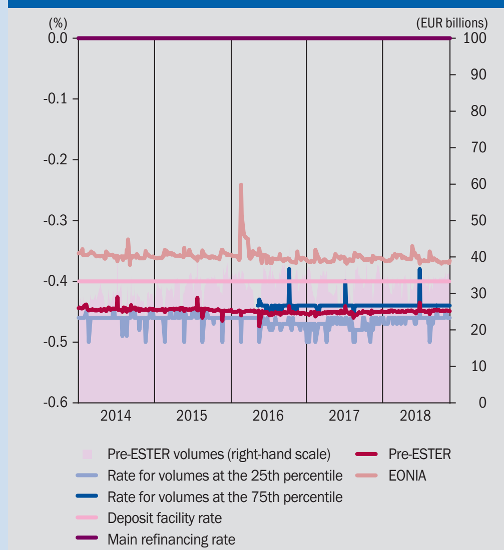
In September 2017 the European Central Bank (ECB) decided to develop a new, more comprehensive euro short-term rate (ESTER) based on daily information relating to money market transactions.[11] The information will be obtained from the ECB's money market statistical reporting (MMSR)[12] dataset, based on data from a pool of 52 of the euro area's largest monetary financial institutions (MFIs). These reporting agents are listed in the ECB's Statistical Data Warehouse[13] and at present comprise 50 banks.

The MMSR reporting banks broken down by country of establishment:

Germany	14	Netherlands	4
France	12	Ireland	1
Italy	6	Sweden	1
Spain	5	Greece	1
Belgium	5	Austria	1

ESTER[14] will take into account not only interbank transactions, but also transactions with other entities (money market funds, insurers, other financial corporations) from the unsecured market segment, and it will reflect the wholesale borrowing costs of euro area banks. ESTER will be based exclusively on daily data and will be published for each TARGET2 business day. ESTER will be published every morning and take into account only the data received by the submission deadline of 07:00 CET the same morning (the rate will be published no later than 09:00 CET). ESTER is calculated using overnight unsecured fixed rate deposit transactions over €1 million, and it is calculated as a volume-weighted trimmed mean in the following way: by ordering the transactions from the lowest rate to the highest rate; aggregating the transactions occurring at each rate level; removing the top and bottom 25% in volume terms; and calculating the mean of the remaining 50% of the volume-weighted distribution of rates. By filtering out transactions conducted at outlying rates, such trimming underlines the principal trend. In the event that the number of reporting banks falls below 20, or five banks account for 75% or more of total transaction volumes, the data will be deemed insufficient to calculate the rate in the standard way. This will trigger a short-term contingency procedure, under which ESTER will be calculated using the rate from the previous TARGET2 business day. Among the information published together with ESTER will be the number of banks whose data was used in the calculation for the given day.

Chart A EONIA and pre-ESTER



Source: ECB.

10 Source: https://www.ecb.europa.eu/press/pr/date/2017/html/ecb.pr170921.en.html

11 Since July 2016 the ECB has been collecting this information in accordance with Regulation ECB/2014/48 (Regulation (EU) No 1333/2014).

12 List of MMSR reporting banks: https://www.ecb.europa.eu/stats/financial_markets_and_interest_rates/money_market/html/index.en.html

13 MFIs meeting the criteria laid down in Regulation ECB/2014/48.

14 Source: https://www.ecb.europa.eu/paym/initiatives/interest_rate_benchmarks/shared/pdf/ecb.ESTER_methodology_and_policies.en.pdf

The ECB will publish ESTER from October 2019. In order to ensure that financial market participants have sufficient time to adjust processes and procedures for the transition to ESTER, the ECB began in summer 2018 to publish the pre-ESTER,[15] a data series calculated using the same methods as those defined for ESTER. Pre-ESTER differs in that it is based on time-lagged daily data reported by banks (currently numbering between 30 and 35) for each reserve maintenance period. In other words, pre-ESTER is based on data that include all revisions in terms of cancellations, corrections and amendments submitted by reporting agents by the time of calculating the rate.

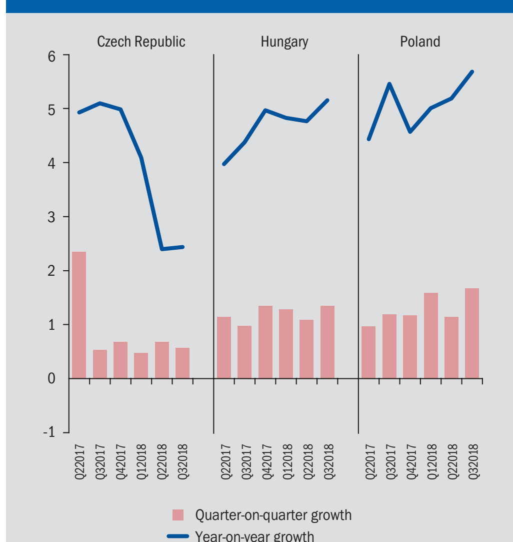
In September 2018 the Working Group on Euro Risk-Free Rates – established by the ECB, the Belgian FSMA,[16] ESMA,[17] and the European Commission – recommended ESTER as the alternative euro risk-free rate that will replace EONIA in January 2020.[18]

15 Source: https://www.ecb.europa.eu/paym/initiatives/interest_rate_benchmarks/shared/pdf/ecb.Pre-ESTER.en.pdf
16 FSMA – Financial Sevices and Markets Authority.
17 ESMA – European Securities and Markets Authority.
18 Source: https://www.ecb.europa.eu/press/key/date/2018/html/ecb.sp180925.en.html

5 The Czech Republic, Hungary and Poland

In both Hungary and Poland, annual GDP growth accelerated in the third quarter of 2018, while in the Czech Republic it remained unchanged, at 2.4%. Hungary's GDP growth was 0.4 percentage point higher in the third quarter than in the second, at 5.2%, and Poland's was 0.4% higher, at 5.7%.

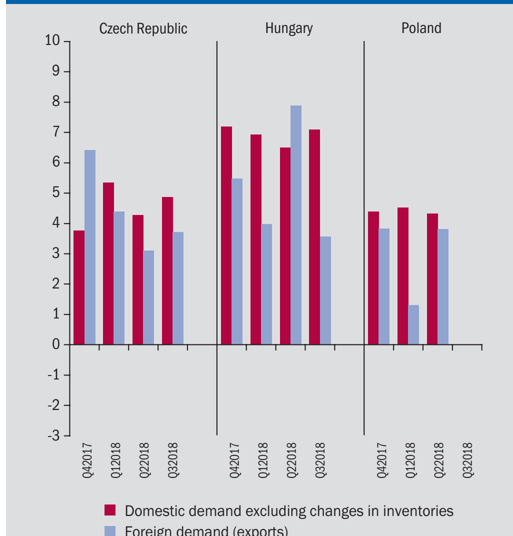
Chart 21 GDP (percentage changes)



Source: Eurostat.

As for quarter-on-quarter GDP growth in the countries under review, Hungary and Poland both recorded an increase in growth compared with the previous quarter. In Hungary, the rate rose by 0.2 percentage point, to 1.3%, and in Poland by 0.6 percentage point, to 1.7%. By contrast, Czech economic growth edged down by 0.1 percentage point, to 0.6%. The activity slowdown in the Czech Republic was caused largely by net exports, which after contributing positively to GDP in the previous quarter had a sizeable dampening effect in the third quarter. Investment demand growth also decelerated. Compared with the previous quarter, both private and public domestic consumption made a larger positive contribution. Czech GDP growth was also supported by changes in inventories, which in the previous quarter dampened overall growth. In Hungary, the slight acceleration of economic growth was driven mainly by investment growth, which was higher compared with the previous quarter. At the same time, the rate of decrease in inventories moderated. The contributions of household consumption and government consumption remained unchanged. Net exports had a significant dampening effect on GDP growth, owing to a pronounced drop in exports. In Poland, the increase in economic growth[19] was underpinned by growth in investment demand and inventories. Consumer demand growth was similar in both the private and public sectors. Net exports had a moderating impact on GDP growth.

Chart 22 Contributions to quarterly GDP growth (percentage points)



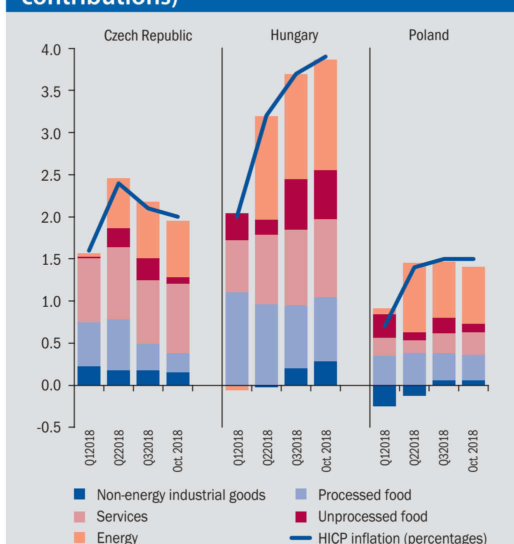
Sources: Eurostat and NBS calculations.

Comparing its levels in June and September 2018, annual consumer price inflation increased in Hungary (by 0.5 percentage point, to 3.7%) and in Poland (by 0.1 percentage point, to 1.5%), but slowed in the Czech Republic (by 0.3 percentage point, to 2.1%). The easing of Czech consumer price inflation reflected mainly prices of processed food and, to a lesser extent, services. Non-energy industrial goods inflation remained the same. Both energy inflation and unprocessed food inflation accelerated. In October, Czech headline inflation slowed slightly further, due mainly to prices of processed and unprocessed

19 The text is based on data published by the Polish Statistical Office.

food. In Hungary, the only components that did not contribute to the rise in headline inflation were processed food inflation, which slowed, and energy inflation, which remained broadly unchanged. In October, Hungary's consumer price inflation again accelerated slightly, pushed up mainly by the non-energy industrial goods and energy components. Compared with Hungary, Poland recorded a more modest increase in headline inflation over the third quarter. The upward pressure came largely from non-energy industrial goods prices, whose annual rate of change went from negative to positive, and from unprocessed food inflation, which accelerated. Services inflation also increased moderately, while other headline inflation components recorded a lower rate of increase. In October, Poland's headline inflation was unchanged from September.

Chart 23 HICP inflation and its components (annual percentages; percentage point contributions)

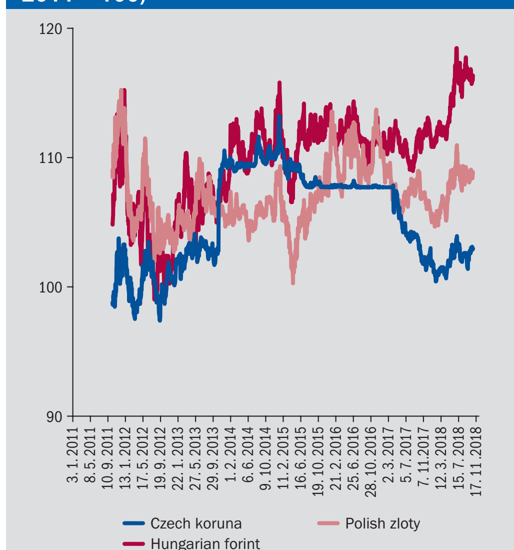


Sources: Eurostat and NBS calculations.

The currencies of all three countries were trading stronger against the euro at the end of the third quarter than at the end of the second quarter: the Czech koruna had appreciated by 1.11%, the Hungarian forint by 1.64%, and the Polish zloty by 2.19%.

After their depreciation trend in the second quarter of 2018, the exchange rates of the reviewed currencies strengthened at the beginning of the third quarter as sentiment improved and tensions receded in financial markets. Investment risk remained affected by market expectations about the monetary policy stances of the world's major central banks, as well as by the threat of trade war escalation following the introduction of new protectionist measures in the world trade system and by continuing tightness in the global oil market (with oil inventories falling in the United States and sanctions being imposed on Iran). At the end of the quarter, the exchange rates of emerging market economies were additionally affected by financial market turbulence in two EMEs: Turkey and Argentina. Meanwhile, the currencies of central and eastern European countries were largely resistant to the pressures buffeting the currencies of other EMEs, thanks to favourable trends in their domestic economies (relatively strong economic growth supported mainly by domestic consumption as well as by investment).

Chart 24 Exchange rate indices of national currencies vis-à-vis the euro (index: 3 January 2011 = 100)

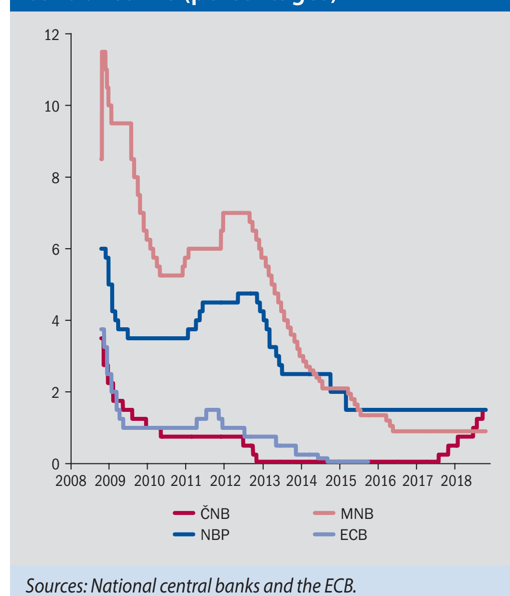


Sources: Eurostat and NBS calculations.
Note: A fall in value denotes appreciation.

The Czech central bank was the only one of the three countries' central banks that adjusted its monetary policy rates in the third quarter of 2018. Česká národní banka (ČNB) increased its base interest rate (the two-week repo rate) by 25 basis points on two occasions: first to 1.25% with effect from 3 August 2018, and then to 1.50% with effect from 27 September 2018. The

lombard rate was also raised by 25 basis points in both August and September, taking it to 2.50%, and the discount rate was raised by 20 and 25 basis points, up to 0.50%. According to the central bank, this gradual raising of interest rates is consistent with the ČNB's current macroeconomic forecast and supports the normalisation of monetary policy conditions at a time when the Czech economy is performing favourably and when the labour market is tightening and creating inflationary pressures. In November, ČNB increased the base rate again, to 1.75%, after discussing the new macroeconomic forecast. In Hungary, the **Magyar Nemzeti Bank** (MNB) left its key interest rates unchanged in the third 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%. According to the central bank, keeping the base rate unchanged and maintaining an accommodative monetary policy stance continued to be necessary in order to achieve the inflation target in a sustainable manner. At its September meeting, the MNB's Monetary Council approved a future strategic framework for the setting of unconventional policy instruments, as well as a programme to support SME lending, entitled the Funding for Growth Scheme Fix, which should replace the Market-Based Lending Scheme from April 2019. As part of its future strategy for the setting of unconventional monetary policy instruments, the Monetary Council decided that the three-month deposit facility would be phased out by the end of 2018 and that the remuneration rate for required reserves and preferential deposits would remain equal to the base rate. The Monetary Council also decided to phase out the monetary policy IRS tenders and the mortgage bond purchase programme by the end of 2018. In Poland, **Narodowy Bank Polski** (NBP) left its monetary policy rates unchanged in the third quarter of 2018 (the reference rate has been at 1.5% since 5 March 2015). In the central bank's view, based on incoming information and forecasts, the outlook for the Polish economy is favourable despite an expected slowdown in GDP growth in coming years, and inflation should remain close to target over the forecast 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 25 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	October 2018	3.7	(=)	3.7	(-0.2)	3.7	(-0.2)	-	-
OECD	November 2018	3.6	(=)	3.7	(=)	3.5	(-0.2)	3.5	-
EC[1)]	November 2018	3.9	(=)	4.0	(-0.2)	3.8	(-0.3)	3.8	-
ECB[2)]	December 2018	-	-	3.8	(-0.1)	3.5	(-0.2)	3.6	(-0.1)

Table 2 United States

	Release	2017		2018		2019		2020	
IMF	October 2018	2.2	(-0.1)	2.9	(=)	2.5	(-0.2)	-	-
OECD	November 2018	2.2	(=)	2.9	(=)	2.7	(=)	2.1	-
EC	November 2018	2.2	(-0.1)	2.9	(=)	2.6	(-0.1)	1.9	-
Federal Reserve	September 2018	2.2	(-0.1)	3.1	(0.25)	2.55	(0.15)	1.95	(0.05)

Table 3 Euro area

	Release	2017		2018		2019		2020	
IMF	October 2018	2.4	(=)	2	(-0.2)	1.9	(=)	-	-
OECD	November 2018	2.5	(=)	1.9	(-0.1)	1.8	(-0.1)	1.6	-
EC	November 2018	2.4	(=)	2.1	(=)	1.9	(-0.1)	1.7	-
ECB	December 2018	-	-	1.9	(-0.1)	1.7	(-0.1)	1.7	(=)

Table 4 Czech Republic

	Release	2017		2018		2019		2020	
IMF	October 2018	4.3	(=)	3.1	(-0.4)	3.0	(=)	-	-
OECD	November 2018	4.5	(-0.1)	3	(-0.8)	2.7	(-0.5)	2.6	-
EC	November 2018	4.3	(=)	3.0	(=)	2.9	(=)	2.6	-
ČNB	November 2018	4.5	(=)	3.1	(-0.1)	3.3	(=)	3.3	(-0.1)

Table 5 Hungary

	Release	2017		2018		2019		2020	
IMF	October 2018	4.0	(=)	4.0	(0.2)	3.3	(0.3)	-	-
OECD	November 2018	4.4	(0.4)	4.6	(0.2)	3.9	(0.3)	3.3	-
EC	November 2018	4.1	(0.1)	4.3	(0.3)	3.4	(0.2)	2.6	-
MNB	September 2018	4.0	(=)	4.4	(=)	3.5	(=)	3	(0.2)

Table 6 Poland

	Release	2017		2018		2019		2020	
IMF	October 2018	4.6	(=)	4.4	(0.3)	3.5	(=)	-	-
OECD	November 2018	4.8	(0.2)	5.2	(0.6)	4	(0.2)	3.3	-
EC	November 2018	4.8	(0.2)	4.8	(0.2)	3.7	(=)	3.3	-
NBP	November 2018	4.6	(=)	4.8	(0.2)	3.6	(-0.2)	3.4	(-0.1)

1) Global economic growth excluding the EU.
2) Global economic growth excluding the euro area.
Note: Data in brackets denote the percentage point change from the previous projection.