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Monthly note

Intesa Sanpaolo
International Research
Network

High frequency indicators confirm overall a robust economic cycle in 1Q but with a few signs of moderation. Inflation weakens, still supporting easy monetary stances (except in RO). The CB of Egypt cuts policy rates.

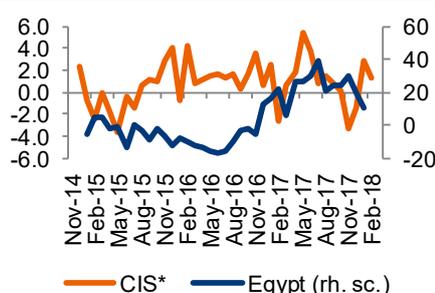
Most recent high frequency indicators and surveys confirm an overall robust economic cycle in CEE and SEE countries in the early months of 2018 but with a few signs of moderation. In February, industrial production recorded a solid performance (+5.3%), slightly below the average recorded in 4Q17 (6.9%). In the same month, on the demand side, retail sales were generally strong, thanks to falling unemployment and rising wages, but exports contracted as in the case of CEE countries (except in Slovakia and Slovenia) or decelerated as in the case of SEE countries (except Albania and Serbia), after a buoyant 4Q17. Forward-looking indicators – such as PMIs and ESIs – remained close to their historical highs in March, with levels however slightly below the peaks registered in previous months.

Over the last couple of months, inflation pressures have remained subdued in almost all CEE/SEE countries, thus still supporting easy monetary stances in the region, with a few exceptions. A slowdown in the development of inflation in Czech Republic, after recent peaks, is quite likely to soften the central bank’s tightening cycle, resulting in one more hike instead of the two currently seen in the remainder of this year. On the contrary, in Romania, with the jump in March of the inflation rate to 5.0%, well above the upper bound of the target range, the central bank is expected to continue along a tightening cycle. In the SEE region, due to unexpectedly low inflation rates, the NBS cut again the policy rate in April. A further cut cannot be ruled out.

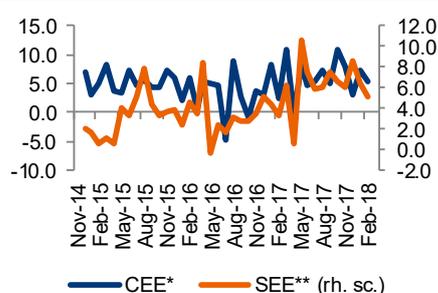
In the CIS region, according to preliminary estimates, GDP rose by 1.1% yoy in 1Q18, compared to 0.9% yoy in 4Q17 in Russia, but the growth outlook is being clouded by the new US sanctions and the related (but then partially reversed) sell-offs in the Russian financial markets earlier this month which weakened the rouble to above 60 against the USD despite the parallel jump in the oil price. In Ukraine, the recent data point to a slowdown in the annual pace of growth in 1Q18 compared to the 2.2% recorded in 4Q17. Annual inflation accelerated to 2.4% in March in Russia, but remained well below the 4% CBR target. In Ukraine, inflation fell to 13.2% in March, but a slower-than-expected deflationary process likely prevents the CB from re-starting an easing cycle. In the MENA region, economic growth prospects have improved in Egypt, with real GDP growth accelerating to 5.3% 4Q17 and recording a similar pace in the 1Q18. In March, the central bank further cut the policy rates as inflation (at 13.3% last month) moved close to the target.

Banking aggregates accelerated in many CESEE countries. However, while household loans were overall dynamic (in particular, in Slovakia and CZ), corporate loans showed a more volatile pattern in CEE/SEE countries and continued to contract in Albania, Croatia and Serbia. NPLs/total loans ratios continued to decline overall to around 5% in CEE countries (except Poland, at 9.6%) and 10% in several SEE countries (13.4% in Albania). On the funding side, the most recent data still show significant increases of deposits from both households and corporates, accompanied, after many years of negative changes, by a rebound in foreign liabilities in several cases. Lending growth accelerated in Russia and Ukraine, but was still weak (negative in real terms) in Egypt.

Industrial production % yoy – CIS – Egypt



Industrial production % yoy – CEE – SEE



Sources: National Statistics Offices; note * weighted average on Russia and Ukraine data

Sources: National Statistics Offices; note * weighted average on Slovakia, Slovenia Hungary, Czech Rep. and Poland data; ** weighted average on Bosnia, Croatia, Romania and Serbia data

[See the final page for important information.](#)

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ALBANIA



Albania

ROMANIA



Romania

SLOVAKIA AND CZECH REPUBLIC



VUB BANKA

BOSNIA AND HERZEGOVINA



Bosna i Hercegovina

RUSSIAN FEDERATION



BANCA INTESA

SLOVENIA



INTESA SANPAOLO BANK

CROATIA



PRIVREDNA BANKA ZAGREB

SERBIA

BANCA INTESA
Beograd

HUNGARY



CIB BANK

EGYPT



ALEXBANK

بنك الإسكندرية

UKRAINE



PRAVEX-BANK

This note has been coordinated by Gianluca Salsecci. The names of the authors are reported in the single sections.

The note considers the countries with Intesa Sanpaolo Subsidiaries: Slovakia, Slovenia, Hungary and Czech Republic among the CEE countries, with the addition however of Poland where ISP is present with a Branch, Albania, Bosnia, Croatia, Serbia and Romania among SEE countries; Russia and Ukraine among CIS countries; Egypt among MENA countries.

The figures in this document have been updated as of 27th April 2018.

Cross Country Analysis

CEE area

After a strong 4Q17, the latest high frequency economic indicators continue to show a sustained dynamic of economic activity in the **CEE region** in the early months of 2018, with a few sign of moderation.

Antonio Pesce

In **Czech Republic**, in the first two months of this year, industrial production grew by 4.2% yoy on average, below the 4Q average (5.1%) but still a good pace. In the same period, exports decelerated to 1.8% yoy in nominal term (from 6.2% in 4Q), though with a downward shift caused by the February contraction (-0.3%). In March, the Economic Sentiment Indicator (ESI) nevertheless remained close to the record high.

High frequency indicators still signal a robust economic dynamic in **Hungary**. In February, industrial production growth decelerated to 4.1% yoy, but was still above the 4Q average; in the same month, exports contracted, however, by 0.2% yoy, but this was after a strong performance in January (almost 5.0%). Even though the PMI edged down last month, it stayed near its historical high and above the threshold of 50.

In **Slovakia**, industrial production growth softened to 1.1% yoy in February; however, the ESI rebounded to 103 in March from January's 18-month low (100.7). This was driven by a rise in the Industrial Confidence component of the index. Exports remained continued to record a strong performance in February (4.9% yoy), as did retail sales (5.0%). In **Slovenia**, economic conditions remained solid in the first months of this year, as highlighted by the strong performance in both industrial production (7.2% yoy) and exports (12.5%) in February, even though their trends were below the 4Q averages.

In **Poland**, in March, industrial production rose by double digits (11.4% yoy), well above the 4Q average; in February, the real retail trade dynamic strengthened further (7.9%), but exports remained on a negative trend (-0.4% yoy in nominal term) for the second consecutive month. The ESI fell to 110 in March from the February peak (112).

Over the past couple of months, even given the strong economic dynamic, **Inflation** weakened in the region – except in Slovakia – ranging from 1.3% in Poland to 2.0% in Hungary in March. The drop was driven mainly by weaker food and fuel price increases. Based on the feeble inflation path, the **monetary policy** in CEE countries is expected to remain easy. In Czech Republic – where inflation had been rising in previous months – the central bank is likely to retreat from the expected tightening, with one more hike instead of two likely in the remainder of this year. This month, the Hungarian central bank has maintained the loose monetary conditions and the Board has decided to maintain the policy rate unchanged at 0.9%. It has confirmed the HUF75bn upper limit on three-month deposits. Moreover, in March, the Council set the amount of liquidity to be crowded out for 2Q18 at least at HUF400-600bn. The monetary authority will continue mortgage bond purchases and interest rate swap facilities in the 5Y and 10Y maturities as programmes.

Exchange rates vs the euro have been in general quite stable over the last few months. CDS spreads increased slightly in the area, except in Poland, where they decreased somewhat instead.

In the **CEE region**, banking aggregates continued to show positive changes, although decelerating as of February. Lending growth was supported particularly by households in Slovakia, Slovenia and Czech Republic, and in the corporate sector, especially in Hungary. Interest rates remained low, in line with money market rates.

Davidia Zucchelli

In **Czech Republic**, loan growth decelerated slightly (6.2% yoy in February from 6.5% yoy in December), supported particularly by the household sector (7.8% yoy, as in the previous five months). The NPL ratio remained very low (4%) and on a stable path. Deposits were also

dynamic (+6.5% yoy in February, after +7.6% yoy in 2017), increasing at the same speed in the household and the corporate sectors (6.6% and 6.4%, respectively) despite low interest rates.

In **Hungary**, loans confirmed a strong recovery as of February (+4.7% yoy), supported by corporates (9.8% yoy), while the outstanding amount of loans to households declined slightly (-0.6 yoy). We would note, however, that demand for loans has also been increasing across a whole spectrum of products and segments in the last several months, as highlighted by the central bank. Deposits accelerated to +13.7% (from +11.8% yoy in January), particularly from businesses (+21.1% in February), but also from households (+7.3%).

In **Poland**, loans showed a stable increase of around 3% yoy as of December, a similar performance to that recorded in November, particularly in the corporate sector (+6.1% yoy in 2017), while the household sector recorded a lower increase (by 2.8% yoy in 2017). Central authorities put in place several measures to reduce risks, but the forced conversion of loans denominated in foreign currency no longer appears to be on the agenda. Impairment loans – as defined by the NBP – decreased from 10.5% of total loans in 2016 to 9.2% at end-2017. Regarding deposits (up by 4.1% in 2017), households showed an increase of 4.2% yoy and corporates a fall of 3.8% yoy (from +6.1% yoy in October). Foreign liabilities continued to decline (-11.7% yoy as of February from -13% in 2017).

Lending growth continued to be strong in **Slovakia** as well (9.6% in January, as in December 2017), fuelled by economic growth and low interest rates, both in the corporate sector (by 5.2%) and especially in the household sector (by 13.6%), driven by a rise in mortgages. Deposits also grew (6.2% yoy from 5.2% yoy in December) from both households (4.3%) and corporates (9.5%, up from 6.7% yoy as of December). Foreign liabilities decreased by 1.9% yoy in January.

In **Slovenia**, the recovery of total loans has been confirmed, although at a slightly slower pace (+2.8% yoy from +3.2% in December 2017), driven by retail lending (+6.2%), while loans to corporates decreased by 0.6% yoy in February. NPLs amounted to 6.0% of total loans as of December. Regarding deposits (+7.0% yoy in February in the private sector), the corporate sector remained dynamic (10.9% from 12.7% yoy in January) while deposits from households increased at a lower rate (by 5.7% yoy from 5.3% in the previous month).

SEE area

Most recent high frequency data have confirmed, overall, the consolidation of the economic cycle among **SEE** countries as well.

In **Croatia**, industrial production growth rose to 3.3% in February while in the same month retail trade remained on a positive trend (1.2%). The dynamic for exports was positive too, though with a decelerating profile. The export dynamic remained very strong and in double digits in **Albania** and in **Bosnia** as well (the former at 14.2% yoy in March and the latter at 10.9% yoy in February).

In **Romania**, industrial production (5.8% yoy), exports (7.6% yoy) and retail trade (4.9% yoy) remained strong in February, though below the 4Q averages. In March, the ESI was still very high, albeit lower than the last year's record high. In **Serbia**, following the impressive growth in January (10.6% yoy), industrial production decelerated to 3.3% in February, bringing the average growth in the two months to 7.0%; moreover, in January and February, exports grew at double digits (21.6% yoy and 13.8% yoy, respectively).

In March, **inflation** pressures remained subdued, with the exception of Romania, where inflation climbed to a five-year high of 5.0% (well above the upper bound of the central bank's corridor target of 1.5-3.5%). Rising wages and price pressures suggest that the economy could overheat. So, we expect the Romanian central bank to maintain a tightening stance. At their last board meetings, all the other central banks of SEE countries with ISP subsidiaries confirmed their easing **monetary policies**. Due to the unexpectedly low inflation, the Serbian National Bank

Board cut the policy rate further, however, to 3% at its April meeting and further cuts cannot be ruled out. **Exchange rates** in the region were roughly stable vs the euro in the past months, with some appreciation in Albania, due to the good performance of exports. CDS spreads increased slightly in the area.

Regarding **banking aggregates**, in February, they decelerated slightly from previous performances in **SEE countries**. The corporate sector remained fragile in Albania, Croatia and Serbia. Despite low interest rates, deposits increased in every country, but at a lower rate.

Davidia Zucchelli

In **Albania**, loans remained unchanged (+0.9% yoy in February), but lending activity still decreased by 1.4% yoy (from -0.9% yoy in January) to corporates while accelerating slightly to +6% yoy in February from 5.7% in January to households (with long-term credit demand dominating). Despite the write-offs, NPLs increased again at a rate of 13.7% of total loans from 13.2% in December. Loans in foreign currency continued to decrease (-2.8% yoy) in the corporate sector (-3.9% yoy), where they account for 56% of total loans. In the household sector, they remained stable (+0.4%). Deposits decreased slightly in the private sector (-0.9% yoy) in February; household deposits fell (-1.9%) while deposits from businesses increased (by 5.6%). Foreign liabilities increased by 3.9%, following an improving trend, as seen in some other CESEE countries.

In **Bosnia**, banking aggregates continued their positive trend, with loans increasing by 7.6% yoy in February and deposits by 8.6% yoy (by 15.7% yoy for corporates and by 6% yoy for households). In **Croatia**, loans increased slightly, by 0.7% yoy, in February (from -0.01% yoy in 2017). Corporate loans remained fragile (-1.1% yoy), but appeared to be improving, while household loans accelerated by 2% yoy. Deposits continued to grow (3.2% from 2.2% yoy in January), particularly from businesses, at 8.6%, and by 1.6% yoy from households.

In **Romania**, loans increased in February (6.2% yoy from 6.8% yoy in January), particularly in the household sector, at 8.4% yoy, while loans to corporates confirmed a 3.8% yoy increase, as recorded in the previous month. NPLs continued to decrease (to 6.4% of total loans). Deposits performed well (12.7% from 12.4% in January). In **Serbia**, loans grew by 2.5% yoy in January (from 2.8% yoy in January). Total loans were driven by loans to households (7.5% yoy from 7.9% yoy), driven by easing credit standards for new loans, while loans to corporates declined (-1.4% yoy). Loans in foreign currency increased by +1% yoy. Deposits continued to perform well (3.4% yoy, 1.4% from corporates and 7.5% from households). Deposits in foreign currency accounted for 71% of the total (85% in the household sector and 45% in the corporate sector).

CIS and MENA areas

In **Russia**, most of the activity figures for March were disappointing. Industrial production growth slowed to 1.0% yoy from 1.5% yoy in February, while construction output collapsed (-9.7%). The industrial growth figures suffered from distortions related to working-day effects: there were two fewer working days in March this year than in March 2017. Net of this effect, industrial production rose by 2% yoy. In sectors in which activity strengthened, the improvement was small. Growth in agricultural output ticked up to 2.7% yoy from 2.6% yoy, while retail sales growth edged up only a little (+2% vs +1.8%). According to preliminary estimates by the Russian Ministry of Economic Development, GDP rose by 1.1% yoy in 1Q18 compared to 0.9% yoy in 4Q17. The Russian GDP growth outlook has recently been negatively affected by new US sanctions and the sell-off in Russian financial markets earlier this month. But, local markets have recovered much of their lost ground and most of the tightening that did occur during the sell-off has reversed. For now, we are sticking with our GDP growth forecast for this year of 1.8%.

Giancarlo Frigoli

Annual inflation rose to 2.4% in March from 2.2% in February, but it remained well below the CBR's 4% targets. The ruble came under downward pressure in April, after the announcement of new sanctions, depreciating by over 9% against the USD (RUB/USD at 63 at the end of April)

In this context, the Russian Central bank at its last meeting on 27th April took a pause in its easing cycle, but we expect that it will cut further the policy rate during this year.

In **Ukraine**, both headline and core inflation slowed in annual terms in March, to 13.2% (vs 14% in February) and 9.4% (vs 9.6% in February), respectively. The slowdown mainly reflected the fall in prices for fuel and oil products. Due to the slower-than-expected deflationary process, the central bank has so far abstained from starting an easing cycle.

Industrial production in February 2018 grew by 2.0% yoy; in January, this figure was +3.6%. Economic growth in the first two months of this year vs the two months in the prior year stood at 2.8%, including 6.5% in the manufacturing industry and 1% in mining and quarrying, while a decline of 6.1% was recorded in the supply of electricity, gas, steam and air conditioning. Again, in February, agricultural output fell by 0.3% yoy, as a delayed spring negatively affected wheat yields, while construction activity rose by 0.7%, rebounding from the 1% fall recorded in January. These numbers point to a slowdown in annual growth in 1Q18 compared to the 2.2% recorded in 4Q17.

In **Egypt**, the central bank cut its policy rates again in March (overnight lending rate down by 100bps, to 17.75%). The move followed the continuation of the disinflation process (annual inflation slowed to 13.3% in March from 14.4% in February, and from its peak at 33% in July last year; again in March, core inflation fell to 11.6% from 11.9% in February) and the stability of the currency, with the EGP/USD rate hovering around 17.5. New interest rate cuts are expected over the remainder of the year, as inflation is closing on the central bank's target at a faster than previously forecast pace. Meanwhile, economic growth prospects have improved, with real GDP growth accelerating to 5.3% in October-December (2Q of FY18) and, according to preliminary estimates by the finance minister, confirming this pace in 3Q of FY18 (January-March 2018). GDP growth in the current fiscal year could be slightly higher than the 5.2% forecast by both the ISP Research Department and the IMF.

In **Russia**, bank lending accelerated again in January (5.9% yoy from 5.2%) due to a recent significant rise in the household sector (+13.9% yoy from 12.7% yoy). Corporate lending, which accounts for around 74% of loans to the private sector, showed a recovery (3.3% from -0.7% in November), supported by SMEs, though credit demand from large corporates remained weak. In more detail, loans denominated in foreign currency declined by 14.1% yoy in the corporate sector. In January, deposits increased by 6.5% yoy (from 8.1% in 2017). In line with official rates, interest rates on new loans to businesses declined to 9.1% (from 9.4%), but the interest rate on deposits from households continued to follow a more unclear trend, increasing to 5.5% (from 5.3%).

Davidia Zucchelli

Lending in **Ukraine** showed a further increase in January (5.9% from 5.2% yoy in December 2017). Loans to corporates increased by 5% (the share of corporate loans to the private sector is over 80%), while household loans increased again (by 9.4% yoy, after +6.6% yoy in 2017). Deposits increased by 13.1% in January (vs 12.1% yoy in 2017), both from corporates (14.7% in January from 13.7%) and households (12.3% from 11.4%). NPLs remained unsustainably high (over 54.5% of total loans). The spread remained significant, at 1.7pp vs 2.2pp in December 2017.

In **Egypt**, in December, with the accounting effect of the local currency depreciation on annual changes of the banking aggregates having ended in November, loans and deposits grew by 7.1% and 23.8%, respectively. Nevertheless, in real terms, net of inflation, changes remained negative in lending and around 10% in deposits. Deposits increased, both from corporates (2.7%) and households (29.9%). The LTD ratio remained very low (34%, decreasing month on month from 39.2% in December 2016). Lending interest rates on new business decreased to 19.7% in February (from 19.9% in January) and deposit interest rates rose to 13.5% (from 13.4% in January).

Country-Specific Analysis

Albania

Real Economy

In the second half of 2017, GDP grew at a slower pace than in the first half (3.5%), down from the 3.9% average growth rate registered in the first half of 2017. From the supply side, economic growth in 2017 continued to be especially supported by the activity in the services sector, with some deceleration in the construction and industrial sector. From the demand side, economic growth in 2017 was supported mostly by expansion in private consumption at 2.9%, with some slowdown in investments and a negative contribution from net foreign trade. In March 2018, exports increased by 14.2% yoy and 13.3% mom, while imports increased by 2.6% yoy and 20 % mom.

Kledi Gjordeni

Inflation remains below the target of the Bank of Albania, reflecting little pressures on rising wages and production costs, and benefitting from appreciation of the exchange rate. It was pushed up mainly by food and non-alcoholic beverages. In March 2018, consumer prices rose by 2.0 % yoy. A year earlier, the annual rate was 2.1%.

Financial Markets

The Bank of Albania believes that its current stance on monetary policy remains adequate and it will remain accommodative in the medium term to ensure stable convergence of inflation to target. Interbank market interest rates continued to be close to the policy rate.

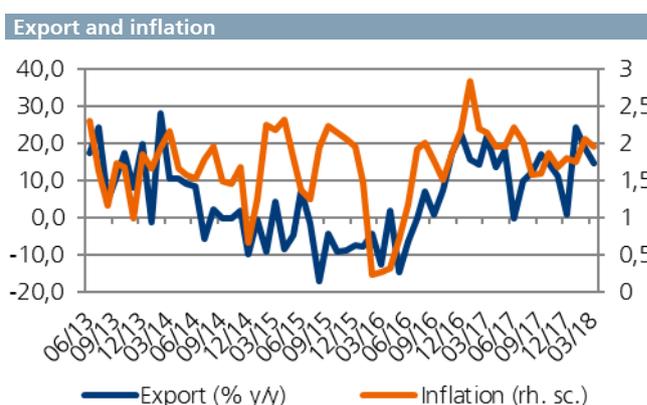
Regarding the foreign exchange market, the local currency (LEK) appreciated more than 3% yoy against the EUR. Following the Memorandum of Cooperation signed between the Bank of Albania, the Ministry of Finance and Economy, and the Albanian Financial Supervision Authority, the CB has started a de-euroisation campaign to promote the use of the national currency in economic and financial transactions and to reduce risks to financial stability.

Banking Sector

In February 2018, total deposits decreased by 0.86 yoy. Household deposits shrank by 1.9%, whereas corporate deposits continued to contribute positively at 5.64 %. Credit to the private sector continues to be supported largely by the expansion of credit in LEK (+5.1% yoy in February); credit in foreign currency decreased by 2.83%. Moderate credit growth (overall +0.9% yoy) reflects the simultaneous effect of sluggish demand and tightened conditions from the supply side. NPLs fell to 13.7% from 18.3% at the end of 2016. In addition to write-offs, other factors, including loan restructuring and loan settlements, were the main contributors to the fall. Liquidity in the banking sector remains ample.

Last macroeconomic indicators			
%	Last value 4Q 2017 3Q 2017		
Industrial production, wda yoy	n.a.	n.a.	n.a.
Export of goods, nominal yoy	14.2 (Mar)	8.7	13.2
Unemployment rate	n.a.	13.4	13.6
Inflation rate, average yoy	2.0 (Mar)	1.8	1.7
Loans (priv sector, yoy, eop)	0.9 (Feb)	0.5	0.7
Deposits (priv sector, yoy, eop)	-0.9 (Feb)	-1.3	0.2

Source: INSTAT, Central Bank of Albania



Bosnia and Herzegovina

Real Economy

Real GDP growth in 4Q17 amounted to 3.0% yoy (0.8% qoq), driven mainly by strong growth in wholesale/retail trade (8.4% yoy) and manufacturing (7.5% y/y), which contributed to roughly 40% of gross valued added, while agriculture's contribution declined by 8.4% yoy. Overall, in line with our expectations, the economy expanded by 3.0% yoy in 2017, as manufacturing and trade/transportation and accommodation services expanded by 6.1% and 6.8% yoy, respectively, thus growing at a stronger pace than in 2016 (5.4% and 4.2%, respectively). In contrast to those performances, agriculture's contribution declined, to 4.4% growth yoy compared to a 7.6% yoy increase in 2016.

Ivana Jović

High frequency data indicate favourable economic developments over the first two months of 2018, as industrial production expanded by 5.8% yoy, supported by 6.2% growth in mining and quarrying, 5.3% growth in manufacturing, and 7.9% growth in electricity production. Over the same period, goods exports increased by 17.7% yoy, while retail trade volume expanded by a strong 10.8% yoy. In line with the data, we maintain our current forecast of 3.1% growth in 2018, although increasing uncertainty related to October's election process threatens to paralyse the country, as reforms to election laws are a prerequisite to later successful government formation.

Banking Sector

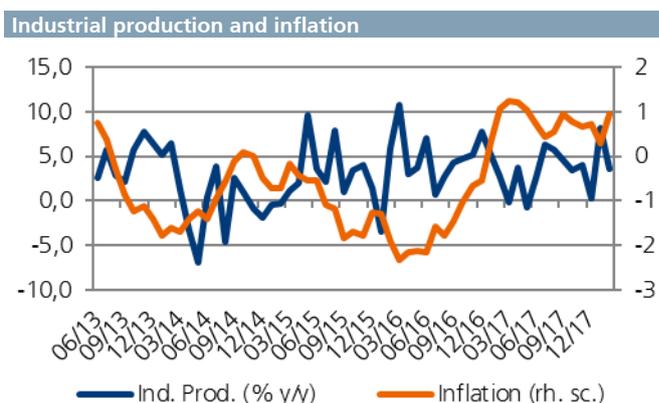
The steady pace of growth in credit demand was maintained in February, when private sector loans saw a 7.6% yoy increase, the same rate as in the previous month. Growth in loans to non-financial corporations sped up slightly, to +8.2% yoy, while loans to households decelerated somewhat, to 7.0% yoy. Breaking down household loans by purpose reveals that the rise in dominant consumer loans moderated to +8.1% yoy while housing loans continued to recover, posting a 5.0% yoy increase. However, the rise in credit card loans slowed to 1.6% yoy. Deposit growth weakened a bit in February, but remained robust at 8.7% yoy, mostly due to the notably lower growth of deposits of non-financial corporations (15.7% yoy vs 19.5% in the previous month). Household deposits growth rose to +6.0% yoy, as a result of a stronger rise in funds on transaction accounts (14.2% yoy), while the increase in sight deposits remained solid, at +10.8% yoy, and time deposits continued to shrink (-0.3% yoy).

Ana Lokin

The NPL ratio continued to improve during 4Q17, declining by 0.7pp qoq, to 10.0%. The shares in loans to non-financial corporations slid by 1.2pp qoq, to 12.3%, and in loans to households by 0.2pp qoq, to 7.5%.

Latest macroeconomic indicators			
%	Last value	4Q 2017	3Q 2017
Industrial production, wda yoy	3.6 (Feb)	2.5	5.7
Export of goods, nominal yoy	10.9 (Feb)	15.7	22.9
Retail trade, real, wda yoy	4.2 (Feb)	4.4	4.2
Inflation rate, average yoy	0.9 (Feb)	0.7	0.6
Loans (priv sector, yoy, eop)	7.6 (Feb)	7.3	7.3
Deposits (priv sector, yoy, eop)	8.6 (Feb)	9.0	8.9

Source: BHAS, CBBH



Croatia

Real Economy

As in other EU countries, the beginning of the year was relatively unstable. Industrial production underperformed, showing low 1.5% yoy growth. A 5.5% decline in energy production overshadowed a 2.9% increase in manufacturing. Along the same lines, exports declined by 1.6% yoy over the first two months of the year, though imports increased by 9.7% yoy, supported by good domestic demand. Real retail trade over the observed period increased by 3.6% yoy, in part due to strong 39.5% growth in car sales. Overall, we see 1Q growth mainly reflecting strong personal consumption and tourism in line with early Eastern holidays. Inflation in 1Q18 continued on the path recorded in 2017, showing 1.0% yoy growth.

On 23 March, S&P upgraded its long-term rating in local and foreign currency to BB+ (from BB), with a Stable outlook. Fitch upgraded its rating in January. We expect that Moody's will follow, based on the April Notification, according to which the government recorded a surplus of 0.8% over GDP, with the public debt ratio declining to 78% in 2017 (vs a 0.9% deficit and an 80.6% debt ratio in 2016).

Financial Markets

The liquidity surplus exceeded HRK29bn in March, but the average 3M Zibor fell by slightly (-1bps mom, to 0.49%), as demand remains thin. January's FX intervention seems to have stabilised the market. Thus, the EUR/HRK rate continued to fluctuate mildly in March, with the average remaining constant mom at 7.44. The spread between the 10Y kuna government bond and the Bund recorded an increase in March of 30bps mom, but due to a decline in the benchmark yield, the average 10Y kuna government bond yield rose by 15bps mom, to 2.2%. In April, markets have calmed, with interest rates and yield showing small fluctuations. The kuna has risen slightly in value vs the euro.

Banking Sector

In February, private sector loans finally resumed growth, recording an increase of 0.7% yoy, owing to 2.0% yoy growth in household loan. Loans to non-financial corporations slipped by 1.1% yoy, however. As previously was the case, transaction data showed that private sector demand is heating up, where cumulative growth of banks' claims on the private sector rose to 3.8% yoy, with corporates at +3.1% yoy and households at +4.4% yoy. The breakdown of household loans by purpose shows that housing loans, in spite of unfavourable regulatory changes affecting citizens' credit eligibility, grew by a 1.5% yoy, mostly due to a revival in demand for euro indexed loans. At the same time, cash non-purpose loans accelerated to 6.6% yoy. Other types of loans continued on a downward trend (overdrafts at -5.4%, credit card at -2.9%, other purposes at -1.9% yoy). The rise in deposits increased to 3.2% yoy in February, as corporate deposits showed continued robust dynamics (+8.6% yoy) while growth in household deposits rose by +1.6% yoy (FX-adjusted at 0.8% yoy) due to a sharp 3.5% mom increase in funds in kuna transaction accounts.

Ivana Jović

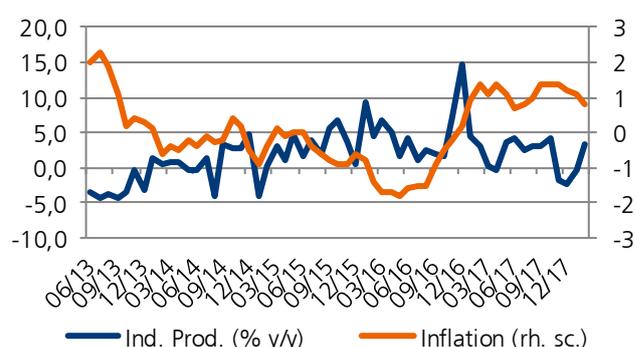
Ivan Odrčić

Ana Lokin

Latest economic indicators			
%	Last value	4Q 2017	3Q 2017
Industrial production, wda yoy	3.3 (Feb)	0.0	2.9
Export of goods, nominal yoy	3.2 (Jan)	8.8	11.7
Retail trade, real, wda yoy	1.2 (Feb)	3.3	5.6
ESI (index)	114.8 (Mar)	115.5	113.7
Inflation rate, average yoy	1.1 (Mar)	1.3	1.1
Loans (priv. sector, yoy, eop)	0.7 (Feb)	-0.1	0.3
Deposits (priv. sector, yoy, eop)	3.2 (Feb)	2.4	3.1

Source: CBS, EC, CNB

Industrial production and inflation



Source: EC

Czech Republic

Real Economy

Industrial activity has moderated as 2018 has progressed. Production in particular has slowed to just over 4.0% yoy in the first two months, from nearly 8.0% growth in 4Q17. Moderation of industrial growth was matched by trade flows, which in February dropped from year-earlier levels. We consider this moderation to be temporary and look for a recovery along the lines experienced in the Eurozone.

Zdenko Štefanides

Construction activity, in contrast, accelerated. Output rose by more than 20% yoy in the first two months of 2018 compared to 5.5% growth in the preceding 12 months. Particularly fast growing were new dwellings, up 26% yoy. Fast growth was also seen in retail sales, up 7.8% yoy in the first two months of 2018, confirming that domestic demand, particularly household consumption, is now the key growth driver of the Czech economy.

Meanwhile, inflation continued to edge lower, to 1.7% yoy by March from 1.8% in February and a 2.9% peak in October 2017. The deceleration in consumer price growth is due primarily to tighter monetary conditions (higher rates and a stronger koruna) which softened the pro-inflationary impact of fast-growing household demand and tight labour market, exemplified by continuing strong growth of wages (8.0% yoy in 4Q17).

Financial Markets

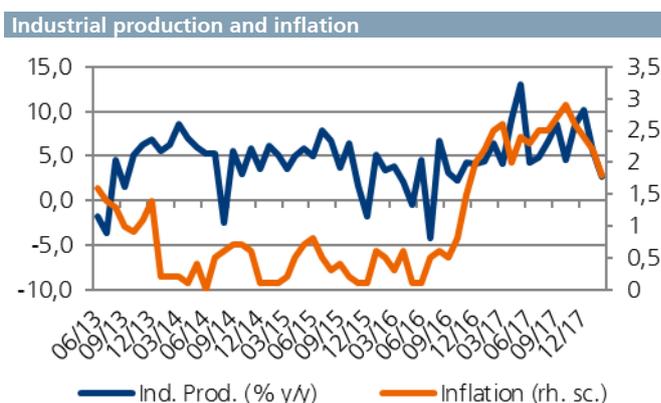
While the fundamental case for higher rates in Czech Republic driven by booming domestic demand remains in place, the pressure on the CNB to rise rates in the nearest months has eased, particularly as inflation has subsided. The koruna, however, has moved sideways in recent weeks and months. At 25.4 vs the euro, the koruna has basically stopped appreciating as 2018 has progressed. Also, at current levels, the koruna is somewhat weaker than assumed in the last CNB forecast. Thus, instead of two hikes over the remainder of this year, we now pencil in just one, likely occurring towards the end of the year.

Banking Sector

The Czech banking sector continues to grow strongly, along with the booming economy. Yet, growth of loans has moderated somewhat, in line with expectations, as gradually increasing interest rates and tighter regulations in the mortgage market have started to have an effect. Thus, in February, overall loan volumes were up 6.2% yoy compared to 6.7% growth in 2017 as a whole. Regarding the deposit market, volumes continue to benefit from the strong saving culture and growing household incomes. In February, deposit volumes were up 6.5% yoy compared to 5.8% yoy in the same period last year.

Latest economic indicators			
%	Last value	4Q 2017	3Q 2017
Industrial production, wda yoy	2.7 (Feb)	7.7	6.6
Export of goods, nominal yoy	-0.3 (Feb)	6.2	4.8
ECB refi rate	0.8 (20th Apr)	0.5	0.2
ESI (index)	109.9 (Mar)	108.4	108.4
Inflation rate, average yoy	1.7 (Mar)	2.6	2.6
Loans (priv sector, yoy, eop)	6.2 (Feb)	6.5	6.5
Deposits (priv sector, yoy, eop)	6.5 (Feb)	7.6	8.9

Source: CBS, EC, CNB



Source: EC

Egypt

Real Economy

The IMF raised its forecast for Egypt’s growth to 5.2% in 2017/18 from 4.8% earlier in its “World Economic Outlook, April 2018” report. The Egyptian government also announced that it was targeting GDP growth of 5.8% in 2018/19, up from 5.2% in the current fiscal year, and lowering the budget deficit and public debt to 8.4% and 91% of GDP compared to 9.8% and 97%, respectively. The balance of payments recorded a USD5.6bn surplus in 1H17/18, with the current account experiencing a sharp contraction of 64% in its deficit. Foreign reserves rose to USD42.6bn at the end of March 2018, compared to USD42.5bn in February 2018.

Samer Halim

Annual headline inflation dropped to its lowest level since May 2016, to 13.3% yoy in March 2018 compared to 14.3% in February. The Reuters news agency reported that Egypt aims to cut subsidies on fuel and electricity by about 26% and 47%, respectively, in 2018/19. But, the central bank’s inflation target of 13% by the end of 2018 still appears reachable.

Financial Markets

In its meeting held on 29 March, the Monetary Policy Committee cut the overnight deposit and the lending rates by 100 bps each, to 16.75% and 17.75%, respectively. State-owned banks announced that they would stop issuing their 17% yield savings certificates after the decision.

The EGP exchange rate has been stable against the USD, reaching EGP 17.7. This stability is expected to continue in 2018, based on two opposing forces: the positive influence of the last sharp EGP depreciation on the current account and foreign investments, and the negative impacts of the inflation differential with trade partners. Egypt raised EUR2bn in a dual-tranche euro-denominated bond sale, attracting an overall EUR7.5bn in orders, which reflects the confidence of international investors in the Egyptian economy.

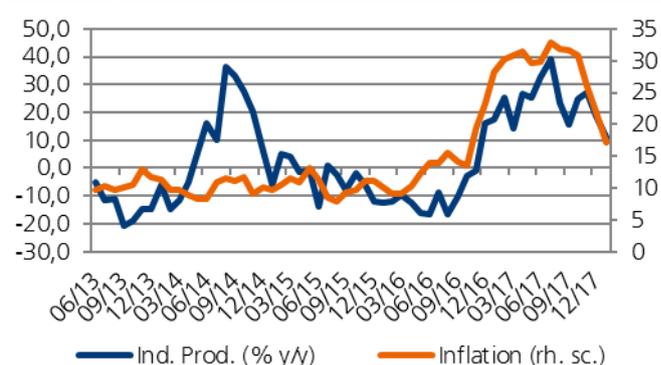
Banking Sector

Total bank loans to the private sector reached EGP918bn in December 2017, up 7.1% yoy, while private sector deposits reached EGP 2.7Tn, up 23.8% yoy, impacted by high interest rates. Total loans to the corporate sector accounted for 72% of total private loans, while household deposits accounted for 82% of total private deposits. In December 2017 compared to September 2017, the capital adequacy ratio improved to 15.2% compared to 14.7% and non-performing loans/total loans declined to 4.9% compared to 5.3%. On the other hand, the loans/deposits ratio declined to 44.2% compared to 45% based on the same time comparative.

Latest economic indicators			
%	Last value 4Q 2017 3Q 2017		
Industrial production, wda yoy	11.1 (Jan)	23.5	26.1
Nom exports yoy	7.0 (Jan)	21.6	13.7
Retail sales yoy	n.a.	n.a.	n.a.
Inflation rate yoy	13.3 (Mar)	26.2	32.1
CB reference rate	17.75 (Apr)	18.8	18.8
Loans (priv sector, yoy, eop)	7.1 (Dec)	7.1	33.4
Deposits (priv sector, yoy, eop)	23.8 (Dec)	23.8	45.3

Source: Ministry of Industry & Foreign Trade, Central Bank of Egypt, HSBC

Industrial production and inflation



Source: Ministry of Planning, CAPMAS

Hungary

Real Economy

Industrial production and exports remained in positive territory in February, which turned out to be a weak month in most of CEE. Industry grew by 4.1%, close to the average of last year. PMIs and other forward-looking indicators were down slightly in February and March compared to multi-year peaks in January. However, the most recent figures are still close to the highest levels recorded since the end of the global economic crisis and the latest downturns do not represent a significant slowdown, in our view, just the opposite, supporting ongoing expectation of robust growth for 2018. Nevertheless, growth rates may be slightly weaker this year compared to the 4.4% yoy recorded in 4Q17, which was boosted by market-based services which provided the strongest support to Q4 growth. EU funds remain a strong driver of growth amid accommodative fiscal and monetary policy. Wage growth has remained in double digits. Headline inflation posted a lower-than-expected figure in March (2.0%), similar the performance recorded in the first two months of the year (even after a below 2% result was seen in February). The downward trend is unlikely to continue, despite rising wages having a limited impact on the headline figure so far and even though the rise in core inflation stopped slightly below 3%. External and internal balances look set to remain in good shape, though the fiscal balance improvement of the preceding years appears to have ceased this year.

Sandor Jobbagy

Financial Markets

The NBH maintained loose monetary policy in March and April, leaving the 3M policy rate on hold at 0.90%, similar to in the preceding months and over all of 2017. The focus remained on the O/N depo rate (also unchanged at -0.15%) with the administrative decrease of the 3M depo stock (ending at HUF 75bn at the end of last year). Further rate cuts are unlikely this year, but monetary easing is ongoing, as the NBH has started a new swap programme and mortgage bond purchases of significant scale have taken place since January 2018. This reflects the central bank's commitment to drive longer yields down, in addition to supporting ongoing low BUBOR rates well below the 0.90% base rate level, essentially close to 0%. Recently, both the forint and bond yields have remained stable, even shortly before and after the parliamentary election in April.

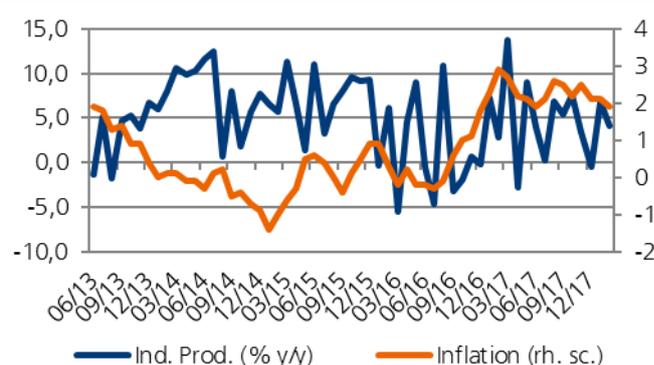
Banking Sector

The strengthening of domestic consumer confidence and demand continued to support the loan market at the beginning of 2018. Following several years of contraction, bank loan stock had already shown strong growth in 2017, and growth continued at the beginning of 2018. The dynamics of new lending were somewhat weaker in February, but this should be temporary. Some loan segments (including mortgages and personal loans) are showing especially dynamic pick-ups. Asset quality continues to improve, with NPLs at close to 6%. The sector has continued to experience high liquidity and a strong capital position.

Latest economic indicators			
%	Last value	4Q 2017	3Q 2017
Ind production yoy	4.1 (Feb)	3.5	4.2
Nom exports yoy	-0.2 (Feb)	7.0	6.9
ESI (index)	120.6 (Mar)	120.8	121.9
Retail sales yoy	4.7 (Dec)	5.8	4.8
Inflation rate yoy	2.0 (Mar)	2.3	2.4
CB reference rate	0.9 (20th Apr)	0.9	0.9
Loans (priv sector, yoy, eop)	4.7 (Feb)	6.0	4.6
Deposits (priv sector, yoy, eop)	13.7 (Feb)	10.8	13.5

Source: CSO, NBH, Bloomberg

Industrial production and inflation



Source: CSO

Poland

Real Economy

In Poland, the rise of forward-looking sentiment indicators came to a halt in March, but these remained close to their highest levels since the end of the global crisis, similar to the end of 2017. The EU Economic Sentiment Indicator has not dropped below the 110 level in any months of 1Q18, thus still reflecting expectations of strong future growth. Industrial production slowed down somewhat towards year-end (3.5% yoy in December 2017), and despite some recent improvement, it has so far in 2018 failed to show a lasting and durable recovery. External balances showed some deterioration in terms of trade while the current account balance was close to zero. Fiscal policy remained in check, as shown by the annual deficit. Domestic demand and rising wages have had a limited impact on inflation so far this year. GDP growth surged to 5.1% yoy in 4Q17, delivering the strongest quarter of 2017, following a 4.9% performance in the third quarter of the year. Economic growth was supported by relatively strong private consumption. Industrial performance also improved. Investments, however, struggled to rise despite the low 2016 base. Judicial reforms and conflicts with the EU have so far not had an adverse impact on overall GDP growth and the outlook. Headline CPI dropped to 1.3% in March (down from 2.1% in December), making the 2017 full-year average 2.0%. Core inflation remained below 1% in 1Q18, as it did in most of 2017.

Sandor Jobbagy

Financial Markets

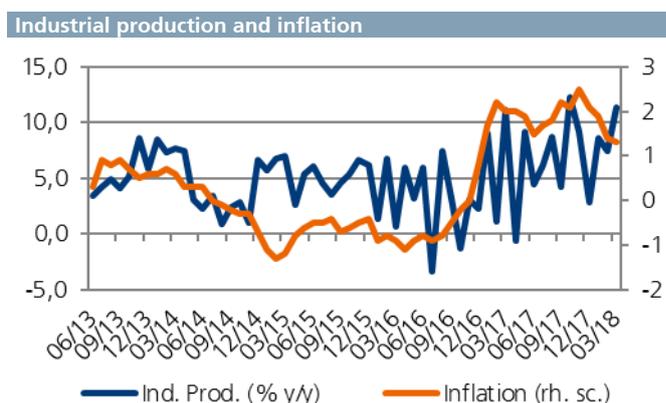
The NBP left its policy rate unchanged (1.50%) in 1Q18, similar to the whole of 2017. The latest monetary decisions were backed by the moderate rise of domestic price levels in addition to favourable external conditions - in particular, the loose policy of the ECB. At the same time, the central bank appears to be concerned about food price growth (which is markedly higher than in the preceding quarters of 2017) and accelerating wage growth. Expectations of the beginning of a tightening cycle at the end of 2018 have faded, especially given the recent low readings of CPI. Partly in connection with monetary expectations, the zloty depreciated in February and March, but the latest levels essentially match those seen during the last month of 2017. The range of 4.15-20 vs the euro has been characteristic of the majority of the period since the beginning of 2018.

Banking Sector

Loan stocks to the private sector showed persistent rises throughout 2017, though at a somewhat moderated pace in September and October. The yoy dynamic was close to 4%, which so far has not been reached in 2018. Lending activity showed some slowdown to both households and the corporate sector. Deposit volumes have continued to increase, despite relatively low (though not decreasing) interest rates. The quality of the banking sector's entire loan portfolio remained solid, with low (and slightly further decreasing) average NPL ratios.

Latest economic indicators			
%	Last value	4Q 2017	3Q 2017
Ind production yoy	11.4 (Mar)	8.1	6.4
Nom exports yoy	-6.2 (Dec)	4.3	8.4
ESI (index)	110.0 (Mar)	106.7	105.4
Retail sales yoy	4.8 (May)		
Inflation rate yoy	1.3 (Mar)	2.2	1.9
CB reference rate	1.5 (20th Apr)	1.5	1.5
Loans (priv sector, yoy, eop)	3.2 (Dec)	3.2	4.2
Deposits (priv sector, yoy, eop)	4.1 (Dec)	4.1	4.9

Source: CSO, NBH, Bloomberg



Romania

Real Economy

March inflation continued to rise to 4.95% yoy (February 2018 at 4.72% yoy), reaching the highest level since mid-2013. Unemployment dipped below 4% for the first time since 2008, with February 2018 data printing 3.9%. The second reading of GDP showed that growth was an outstanding 6.9% in 2017. Industrial production slowed, however, in February for the second month in a row, to 6.7% yoy (from 8.7% in January 2018).

One of the main growth drivers last year was the increase in public budget expenses, reported at above 14%. This pace is regarded as unsustainable, supporting market expectations of decelerating GDP growth in 2018 and onwards.

Financial Markets

Romania recorded the highest inflation print in the entire EU in March 2018, which was a hot topic within the domestic public. At its last rate-setting meeting, the central bank paused, leaving the policy rate unchanged at 2.25%, pointing to the monthly inflation dynamic (trending lower) and the relatively high interest rates on the Romanian leu compared to developed economies and geographic peers. Notwithstanding this, the tightening cycle is likely to continue further in 2018.

The foreign exchange market remained generally stable, albeit at historically high levels (around 4.66 vs the Euro) and amid a widening foreign trade deficit. The central bank's excess liquidity sterilisation operations relieved some of the upward pressure on the euro vs the leu, and brought short-term money market rates closer to the policy rate.

Banking Sector

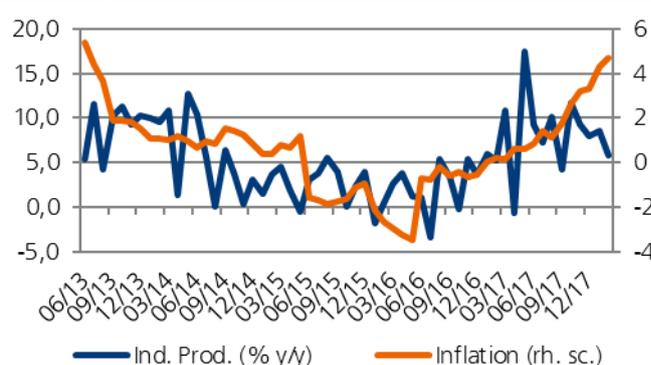
Local currency private sector credit continues to increase, per February data (+15.75% yoy and +0.40% mom). Household sector (+21.42% yoy) is more than double that of corporate sector (+9.38% yoy). Meanwhile, FX credit continues to contract (-6.95% yoy), with the household sector again being the main driver. Deposit dynamics are also in double-digit territory (+12.87% yoy), with local currency deposits (12.43% yoy) being outpaced by foreign currency deposits (13.37% yoy). A sectorial view points to a preference of the household sector for safety, as FX deposits (+13.17% yoy) have outpaced local currency deposits (+8.76% yoy), while, the corporate sector is more sensitive to returns, as local currency deposits (+17.19% yoy) are leading and FX deposits are close behind (+13.84% yoy).

Interest rate dynamics bode well for the banking sector, as loan demand is pushing new credit interest rates higher (at 6.63% in February 2018, up by 95bps from February 2017). Excess liquidity acted as a break on new deposit interest rates (1.11% in February 2018, up 54bps from February 2017).

Latest economic indicators			
%	Last value	4Q 2017	3Q 2017
Ind production yoy	5.8 (Feb)	9.6	7.3
Nom exports yoy	7.6 (Feb)	8.8	8.4
ESI (index)	101.4 (Mar)	103.8	104.5
Retail sales yoy	4.9 (Feb)	12.9	13.4
Inflation rate yoy	5.0 (Mar)	3.1	1.4
CB reference rate	2.2 (20th Apr)	1.8	1.8
Loans (priv sector, yoy, eop)	6.1 (Feb)	5.6	7.3
Deposits (priv sector, yoy, eop)	12.7 (Feb)	10.4	10.8

Source: National Statistical Institute, NBR

Industrial production and inflation



Source: NBR

Russia

Real Economy

In March, GDP grew by 0.7% yoy (in comparison with 1.4% yoy and 1.3% yoy in January and February, respectively). The slowdown in GDP growth is associated with a decline in construction industry, which amounted to -9.7% yoy after near zero growth in January-February. According to official preliminary estimates, real GDP rose by 1.1% yoy in 1Q18. Industrial production grew by 1.9% in 1Q18 in annual terms. The main contributor to industrial production growth in 1Q18 was the production of electric and heat energy and gas supply (which saw an increase of 1.3% yoy). Oil production decreased by 1.5% yoy, due to the fulfillment of the terms of the OPEC+ agreement, while natural gas production increased by 4.4%, which can be explained by increased domestic and external demand due to cold weather. Consumer demand continues to grow steadily. The Consumer Sentiment index has reached its highest levels for the entire history of observation (104.7 and 104.0 in February and March, respectively). One of the factors supporting consumer optimism is the accelerated growth of wages in January-February.

Irina Lekareva

In March, inflation accelerated in annual terms for the first time after eight months of continuous decline. Annual inflation in March was 2.4%. However, it is expected that in the coming months, annual inflation may decrease again to a range of 2.1-2.2%.

Financial Markets

On 23 March, the Bank of Russia cut the key rate by 25bps, to 7.25%, but at its last meeting on 27 April it took a pause in its easing cycle. The CBR is expected to continue to cut the key rate and complete the transition to a neutral monetary policy in 2018.

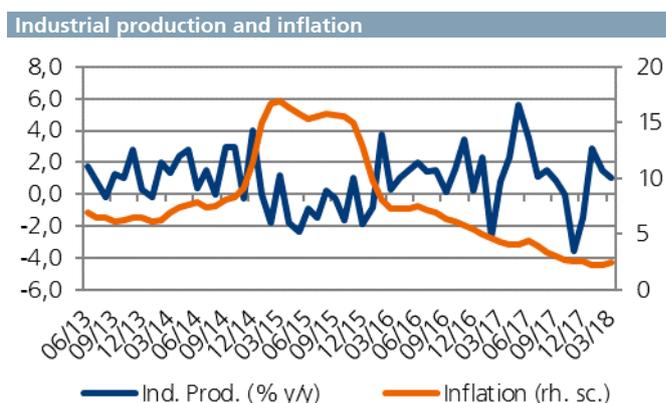
Following the announcement of new set of US sanctions on 6 April 2018, the rouble weakened against the US dollar (by over 9% to 63 RUB : 1 USD at end April). According to the Central Bank this decline is to be regarded as temporary and is not expected to affect GDP growth. Support to the exchange rate should come from the oil prices. Since the beginning of April, the quotation of the Ural quality increased by more than 13%, to \$ 72.3 per barrel (as of 23 April).

Banking Sector

In 1Q18, Russian banks recorded a profit of RUB352bn vs RUB339bn in 1Q17. In January, the total assets of the banking sector increased by 4.6% yoy and loans rose by 5.9%. Loans increased both in the corporate and the retail sectors (+3.3% and 13.9%, respectively). In contrast, loans denominated in FC decreased by 14% yoy as of January, particularly in the corporate sector (-14%), reducing the share of loans in FC to 20.2% of total loans (27.2% in the corporate sector). In January, corporate deposits grew by 7.2% yoy, to RUB16.7tn, while household deposits grew by 6.1% yoy, to RUB25.4tn.

Latest economic indicators			
%	Last value	4Q 2017	3Q 2017
Ind production yoy	1.0 (Mar)	-1.7	1.2
Nom exports yoy	31.3 (Feb)	24.5	18.7
Retail sales yoy	2.0 (Mar)	3.0	2.1
Inflation rate yoy	2.4 (Mar)	2.6	3.4
CB reference rate	7.25 (30th Mar)	7.8	8.5
Loans (priv sector, yoy, eop)	5.9 (Jan)	5.2	1.4
Deposits (priv sector, yoy, eop)	6.5 (Jan)	8.1	4.4

Source: State Statistics Federal Service, Central Bank of Russia



Source: State Statistics Federal Service

Serbia

Real Economy

Based on National Bank of Serbia (NBS) projections, real GDP grew by around 3.8% yoy in 1Q18. Exports of goods recorded double-digit growth of 14% yoy in the first two months of the year, supported by very good results in manufacturing, as 22 out of 23 industry branches registered positive growth, while FDI increased by 17.7% yoy, amounting to EUR401mn.

Inflation amounted to 1.4% yoy in March 2018, which was below the bottom end of the target tolerance range (3.0% ±1.5pp). The drop in yoy inflation was mainly a result of the high base effect (one-off increase last year in petroleum and food prices), as well as lower-than-expected prices of vegetables and firewood, due to a mild winter. Core inflation amounted to 0.8% yoy, its lowest level since inflation has been measured by the consumer price index, indicating weak inflationary pressures.

Financial Markets

Monetary policy easing continued in April 2018, when the key policy rate was cut for the second month in a row by 0.25pp, to 3.0%, its lowest level in the inflation targeting regime. Additionally, the interest rate corridor was narrowed from ±1.5 to ±1.25 pp, meaning that the deposit facility rate remained unchanged at 1.75% while the lending facility rate was cut by 50bps, to 4.25%. The NBS is likely to keep the policy rate flat in the coming period in order to maintain its room for manoeuvre in case of stronger external shocks amid stronger Fed tightening and ECB tapering, although the possibility of a further rate cuts should not be excluded in an environment of persistently low inflation and a strong dinar.

During the first three months of 2018, the dinar appreciated against the euro by 0.1% and against the dollar by 3.1%, while the NBS bought EUR 580mn and sold EUR 180mn on the FX market so as to avoid excessive volatility of the exchange rate. According to Bloomberg, the dinar is the second strongest currency in the world, showing the best performance over the past 12 months. The dinar will continue to be under appreciation pressures in the coming months, mainly due to strong export and capital inflows, fiscal outperformance and increased foreign investment in dinar bonds.

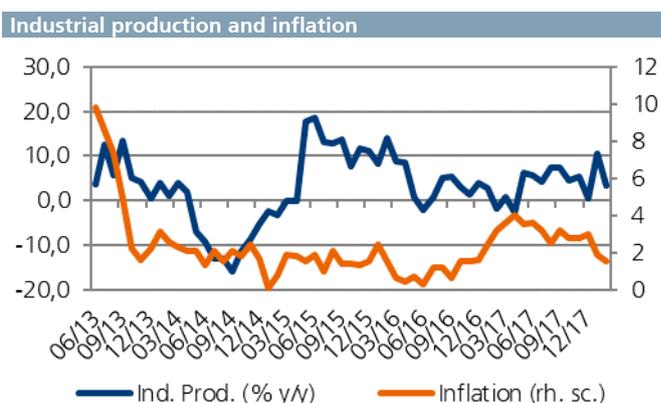
Banking Sector

The banking sector in Serbia recorded a profit of half a billion euros ca. in 2017, which is the best result in the past 10 years. This good result was accomplished despite the decrease in interest rates. In February 2018, interest rates on new dinar loans stood at 5.1% for corporates and 10.6% for households, recording a fall of 9.8pp since the monetary policy easing started five years ago. The share of NPLs has recorded a significant drop of 12.7pp since the adoption of the NPL Resolution Strategy, amounting to 9.6% in February 2018, which is its lowest level in the last nine years.

Latest economic indicators			
%	Last value	4Q 2017	3Q 2017
Ind production yoy	3.3 (Feb)	3.5	6.3
Nom exports yoy	13.8 (Feb)	7.9	12.7
Retail sales yoy	2.0 (Feb)	2.3	3.7
Inflation rate yoy	1.4 (Mar)	2.9	3.0
CB reference rate, eop	3.0 (20th Apr)	3.5	3.8
Loans (priv sector, yoy, eop)	2.5 (Feb)	2.1	0.8
Deposits (priv sector, yoy, eop)	3.4 (Feb)	3.1	5.1

Source: Statistical Office, National Bank of Serbia

Marija Savic



Source: Statistical Office, National Bank of Serbia

Slovakia

Real Economy

The latest round of data has not changed our positive outlook for economic development in Slovakia for 2018 and 2019. Clearly, activity data posted a slight deceleration of overall industrial production, but the automotive sector has posted the first signs of expected recovery in both production and new orders, which should be represent key pillars of an acceleration in the domestic economy. Retail sales and construction output posted solid yoy growth. Our positive outlook is supported by the latest round of confidence surveys. The overall index of economic sentiment calculated as a three-month moving average showed a very decent result. This was mainly due to improved confidence in industry. Tight conditions in the labour market persist, supporting wage and consumption growth, but also pointing to signs of increasing inflationary pressures.

Andrej Arady

In April, Eurostat released its annual report on public fiscal statistics. In headline terms, Slovakia posted decent progress on the fiscal front, with the deficit narrowing from 2.2% of GDP in 2016 to 1.0% of GDP in 2017. This was primarily due to positive economic developments and an improving labour market. However, the deficit was still higher than the Euro Area average. Indeed, the consolidation effort was not hugely ambitious. Net of interest payments, Slovakia posted a primary surplus for the first time in its history, but the vast majority of European countries still posted even higher surpluses in this phase in the economic cycle. The debt/GDP ratio decreased to 50.9%, however, which is well below the European average.

Financial Markets

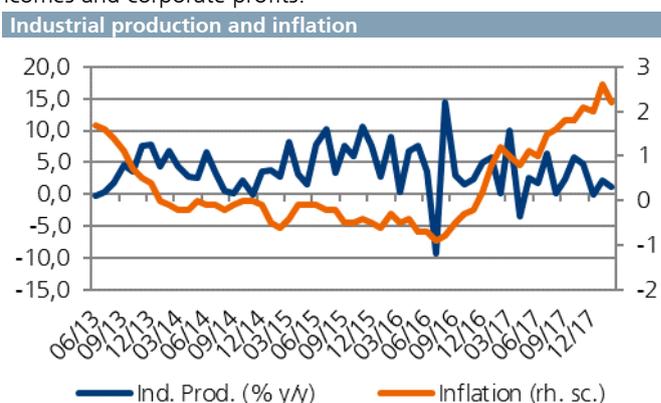
Demand for Slovak government bonds remains high. In April, Slovakia sold nearly EUR200mn in bonds maturing in 2031 and 2047 at average yields of 1.24% and 1.78%, respectively. The bond market in the Eurozone continues to be steered by ECB purchases, thus undervaluing bond yields. So far, the ECB has been very cautious in offering any commentary that could be construed as bearish. Yields on Slovak benchmark 10Y bonds increased over the past month only slightly, by 9bps, to 0.97% on 23 April, resulting in a spread vs the German Bund remaining below 40bps. As we appear to be approaching the end of QE, yields should start to rise and realign to their fair values.

Banking Sector

The most recent data regarding the banking sector aligned with previous trends. Growth of loan volumes remains very strong (9.4% yoy in February), although it appears to be gradually decelerating from the stellar pace recorded in 2017. Despite the recent deceleration, the regulator still appears to be concerned about fast growing indebtedness, thus intensifying its work on further restrictive measures. The next regular report on financial stability, which will be published next month, will likely shed more light on this issue. In contrast, growth of deposits is gradually accelerating, on trend, supported by rising household incomes and corporate profits.

Latest economic indicators			
%	Last value	4Q 2017	3Q 2017
Ind production, wda yoy	1.1 (Feb)	3.5	3.0
Nom exports, yoy	4.9 (Feb)	7.1	7.6
ESI (index)	103.0 (Mar)	103.3	104.8
Retail sales, yoy	5.0 (Feb)	5.7	5.5
Inflation rate, yoy	2.5 (Mar)	2.0	1.6
ECB refi rate	0.0 (20th Apr)	0.0	0.0
Loans (priv sector, yoy, eop)	9.4 (Feb)	9.6	10.7
Deposits (priv sector, yoy, eop)	5.1 (Feb)	5.2	4.3

Source: Statistical Office of the Slovak Republic, National Bank of Slovak Republic



Source: Statistical Office of Slovak Republic

Slovenia

Real Economy

In the first two months of the year, the economy continued to outperform, as industrial production advanced by 9.5% yoy (manufacturing by 10.2% yoy), supported by a strong performance by exports. Goods exports posted a double-digit growth rate in the January-February period (+11.7% yoy). However, personal consumption moderated, as retail volume in January-February declined by 0.8% yoy, amid 4.3% lower sales of fuel and 5.8% lower sales of food products, but also reflecting an extremely high base (in the corresponding period last year, growth was 12.5% yoy). The 1Q18 headline inflation rate remained moderate, averaging around 1.5% yoy: the growth rate of prices of services (+2.2%) outpaced those for goods (+1.2%).

Ivana Jovič
Ivan Odrlič

As expected, the April EDP notification confirmed a 0.03% of GDP general government surplus and a 73.6% debt/GDP ratio in 2017, marking a significant improvement compared to the previous year's 1.9% of GDP deficit and debt level of 78.6%.

Financial Markets

Average 3M Euribor in March remained at -0.33%. The spread between the Slovenian 10Y government bond and the Bund rose by 10bps mom, to 60bps in February, and remained at the same level in March. Thus, the average 10Y government bond yield in March followed the trend of the benchmark yield and amounted to 1.2%. The average 5Y CDS spread barely moved mom in March and stood at 53bps. In April, the yield was down to 1.1%, as the spread retreated to 50bps, whereas the CDS spread rose somewhat, towards 58bps.

Ana Lokin

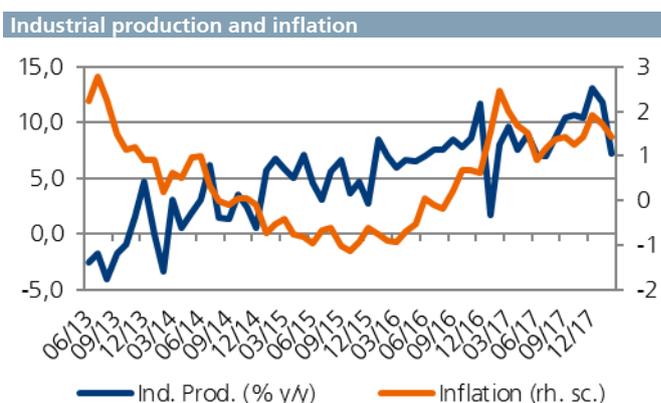
Banking Sector

The private sector loan increase moderated to +2.8% yoy in February, as corporate lending remained volatile. Hence, loans to non-financial corporations were down by 0.6% yoy. Loans to households continued their steady pace of growth and marked a 6.2% yoy rise. Breaking down the household portfolio by purpose shows that the rises in housing and consumer loans softened to 4.1% and 11.6% yoy, respectively, whereas other loans accelerated to 6.3% yoy. Private sector deposit growth remained strong in February, at +7.0% yoy, as growth of corporate deposits moderated to +10.9% yoy while household deposits growth rose to +5.7% yoy. An increase in overnight and redeemable at notice deposits slowed slightly, to 13.1% yoy, whereas growth in term deposits continued to narrow (-5.9% yoy).

Banks continued to focus on active resolution of problem loans. Thus, at the end of 4Q17, the share of non-performing claims stood at 3.7%, down by 0.7pp qoq. The share in corporate portfolios fell by 0.4pp qoq, to 5.3%, and in the household portfolio by 0.1pp, to 3.0%. The broader NPE ratio (EBA definition) saw a 1.1pp qoq decline, to 6.0%.

Latest economic indicators			
%	Last value 4Q 2017 3Q 2017		
Ind production, wda yoy	7.2 (Feb)	11.4	8.7
Nom exports yoy	12.5 (Jan)	15.4	14.5
ESI (index)	113.3 (Mar)	117.2	113.1
Consumer Confidence Indices	0.8 (Mar)	0.2	-4.6
Inflation rate yoy	1.5 (Mar)	1.5	1.3
ECB refi rate	0.0 (20th Apr)	0.0	0.0
Loans (priv sector, yoy, eop)	2.8 (Feb)	3.2	5.9
Deposits (priv sector, yoy, eop)	7.0 (Feb)	7.0	7.5

Source: Statistical Office of the Republic of Slovenia, National Bank of Slovenia



Source: Statistical Office of the Republic of Slovenia

Ukraine

Real Economy

In its bi-annual WEO released in mid-April, the IMF confirmed its forecast for Ukraine's GDP growth in 2018 at 3.2% while it reviewed downwards the forecast for 2019, to 3.3% from 4%. The National Bank of Ukraine forecasts that Ukraine's GDP will accelerate in 2018 to 3.4% from 2.5% in 2017 and then slow to 2.9% in 2019-20. The ISP research department sees GDP growth at 3.2% both this year and in 2019. The average annual inflation forecast in 2018 was reviewed downwards by 1pp, to 11%, and in 2019, the IMF expects 8% average inflation in Ukraine. The consumer price growth forecast for late 2018 was revised downwards by 2 pp, to 9%. By the end of 2019, the IMF expects inflation in Ukraine to be around 6.5%. The ISP research department is less optimistic on inflation and projects annual rates of 10% at end-2018 and 8.5% at end-2019.

Giancarlo Frigoli

Financial Markets

Ukraine's central bank kept the main interest rate on hold at 17% at its April meeting, pausing after a series of rate increases. After four hikes of the key policy rate, the monetary authority said that current monetary conditions are sufficiently tight to bring inflation back to its mid-term targets, confirmed at 8.9% for end-2018 and 5.8% for end-2019. However, the central bank warned that all its expectations hinged on Ukraine sticking with the IMF's USD17.5bn programme. Ukraine has received USD8.4bn so far from the IMF, but additional payments have been delayed, as the government is back-tracking on reforms ahead of presidential and parliamentary elections that will take place in 2019 at the latest.

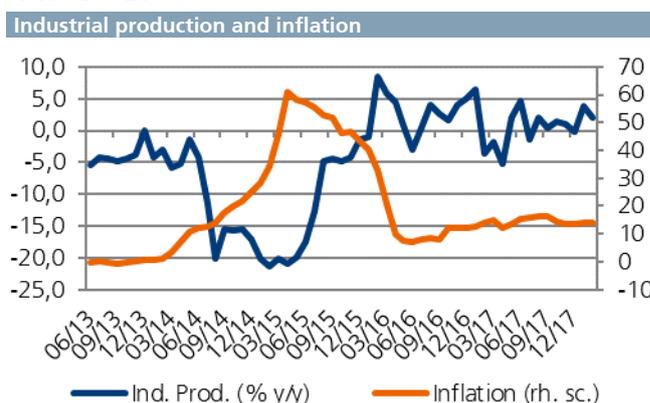
Banking Sector

Loans showed a strong dynamic as of January (+5.8% yoy), accelerating from December (+0.9%), in nominal terms. The recovery in lending has been particularly strong among households (+9.4% yoy in January from 6.6% in 2017), driven by consumer loans. Nevertheless, their share in total loans to the private sector remained modest, lower than 20%. Corporate loans showed a recovery (+5% yoy as of January from -0.4% in 2017) supported by loans in local currency, while loans denominated in foreign currency continued to decrease, by 1.1% as of January (although improving from -11% in 2017).

Davidia Zucchelli

NPLs remained at an unsustainable level (over 54% of total loans). The percentage of these loans, excluding those related to state- and Russian-owned banks, was 28.4%. Deposits increased by 13.1% (with respect to 12.1% yoy in 2017) both from corporates (14.7% in January from 13.7%) and households (12.3% from 11.4%). The LTD ratio increased slightly, to 129.4% (from 123% as of end-2017), a still-too-high level. Foreign liabilities continued to decline (-20.9% yoy as of January from -23.5% in 2017). Due to significant provisioning, the banking sector booked losses of UAH24.4bn in 2017. The losses were mostly generated by four banks. The number of loss-making banks decreased from 33 in 2016 to 18 in 2017.

Latest economic indicators	Last value		
	4Q 2017	3Q 2017	2017
Ind production yoy	2 (Feb)	0.8	0.4
Nom exports yoy	17.7 (Feb)	20.2	21.4
PMI manufacturing	n.a.	n.a.	n.a.
Retail sales	5.6 (Feb)	9.0	8.2
Inflation rate yoy	13.2 (Mar)	14.0	16.2
CB reference rate	17.0 (20th Apr)	14.5	12.5
Loans (priv sector, yoy, eop)	5.8 (Jan)	0.9	-2.4
Deposits (priv sector, yoy, eop)	13.1 (Jan)	12.1	7.9



Source: State Statistics Service of Ukraine, National Bank of Ukraine

Source: State Statistics Service of Ukraine

Country Data: Economy, Markets and Banks - the economic cycle

Economy																		
	GDP chg yoy			Ind. Prod ¹ . chg.yoy			Export nom. ch yoy			Inflation chg yoy			FX reserves chg (mln €) ²			CA bal. (mln €) ³		
	4Q17	3Q17	2016	Last	mth	4Q17	Last	mth	4Q17	Last	mth	4Q17	2016	4Q17	3Q17	2016	4Q17	3Q17
CEE																		
Czech Rep.	5.1	5.1	2.6	2.7	Feb	7.7	-0.3	Feb	6.2	1.7	Mar	2.6	0.7					
Hungary	4.4	3.9	2.2	4.1	Feb	3.5	-0.2	Feb	7.0	2.0	Mar	2.3	0.4	1174	-1235	-5938	197	784
Poland	5.1	4.9	2.8	11.4	Mar	8.1	-0.4	Jan	4.3	1.3	Mar	2.2	-0.6					
Slovakia	3.5	3.4	3.3	1.1	Feb	3.5	4.9	Feb	7.1	2.5	Mar	2.0	-0.5	n.s.	n.s.	n.s.		
Slovenia	6.0	4.5	3.1	7.2	Feb	11.4	12.5	Jan	15.4	1.5	Mar	1.5	-0.2	n.s.	n.s.	n.s.	532	871
SEE																		
Albania	3.4	3.6	3.5	n.a.	n.a.	n.a.	14.2	Mar	8.7	2.0	Mar	1.8	1.3	215	38	47	-295	-133
Bosnia H.	3.0	3.0	3.1	3.6	Feb	2.5	10.9	Feb	15.7	0.9	Feb	0.7	-1.6	182	376	473	-281	-112
Croatia	2.0	3.3	3.2	3.3	Feb	0.0	3.2	Jan	8.8	1.1	Mar	1.3	-1.1	752	926	-193	-674	3881
Romania	7.0	8.6	4.8	5.8	Feb	9.6	7.6	Feb	8.8	5.0	Mar	3.1	-1.5	-347		-350	-6295	-5017
Serbia	2.5	2.2	2.8	3.3	Feb	3.5	13.8	Feb	7.9	1.4	Mar	2.9	1.1	-744	787	-52	-678	-384
CIS MENA																		
Russia	0.9	1.8	-0.2	1.0	Mar	-1.7	31.3	Feb	24.5	2.4	Mar	2.6	7.1	5157	7677	-1356		-2509
Ukraine	2.2	2.4	2.4	2.0	Feb	0.8	17.7	Feb	20.2	13.2	Mar	14.0	14.9	747	1037	-466	-891	-1074
Egypt	5.3	5.2	3.8	11.1	Jan	24.6	7.0	Jan	21.6	13.3	Mar	26.2	13.7	485	5230	7820	-1785	-1605
m.i. E. A.	2.7	2.5	1.8	2.9	Feb	4.2	3.0	Feb	6.1	1.3	Mar	1.4	0.2					

Source: Datastream, Reuters; ¹Wda data for Slovakia, Slovenia; Bosnia, Croatia, Egypt; ²USD for Russia, Egypt, Ukraine, Romania; ³USD for Russia, Egypt, Ukraine

Markets and Ratings															
	S/T rates ¹			L/T rates ²			Foreign exchanges ³			Stock markets		CDS spread (bp)		Rating	
	18/04	chg bp	3M	18/04	chg bp	3M	18/04	3M chg%	1Y chg%	3M chg%	1Y chg%	18/04	18/01	Moody's	
CEE															
Vs Euro															
Czech Rep.	0.9		0.2	1.6		-0.2	25.3		-0.2	-5.4	0.9	16.6	33.7	33.1	A1
Hungary	0.0		0.0	2.4		0.4	310.4		0.7	-0.8	-2.3	19.2	77.8	77.3	Baa3
Poland	1.7		0.0	3.1		-0.2	4.2		0.0	-1.7	-9.3	3.0	41.5	45.1	A2
Slovakia	-0.3		0.0	0.8		0.0	Euro		Euro	Euro	-1.4	10.3	40.2	36.8	A2
Slovenia	-0.3		0.0	1.1		0.1	Euro		Euro	Euro	0.8	7.6	52.3	51.0	Baa1
SEE															
Albania	1.2		0.0	n.a.		n.a.	129.3		-3.4	-4.4	n.a.	n.a.	n.a.	n.a.	B1
Bosnia H.	n.a.		n.a.	n.a.		n.a.	1.96		Board	Board	n.a.	n.a.	n.a.	n.a.	B3
Croatia	0.5		0.0	2.2		0.0	7.4		-0.2	-0.1	-4.6	-8.0	94.8	90.9	Ba2
Romania	2.0		0.2	4.4		0.1	4.7		0.1	3.0	6.7	8.5	79.0	77.5	Baa3
Serbia	3.0		-0.5	n.a.		n.a.	118.2		-0.2	-4.4	-2.6	7.2	119.5	118.6	Ba3
CIS MENA															
Vs USD															
Russia	7.3		-0.5	7.4		0.0	61.1		8.0	8.7	-3.2	18.8	124.6	104.3	Ba1
Ukraine	17.8		0.6	14.5		0.0	26.2		-9.2	-2.5	2.6	-12.2	363.4	360.5	Caa2
Egypt	18.0		-1.2	14.7		-0.6	17.7		0.1	-2.4	6.9	6.8	255.9	340.3	B3
m.i.A.E.	-0.3		0.0	0.5		0.0	1.2		1.1	15.7	-5.1	-0.4	5.2	5.1	

Source: Datastream, Reuters; ¹The data for Albania refers to January, for Egypt refers to March, for Czech Republic refers to March; ²For Ukraine, the long-term rate refers to a government issue in dollars; ³The (-) sign indicates appreciation.

Aggregates and bank rates for the private sector																							
	Loans Chg yoy %			NPL/Loans %			Foreign Liab. Chg yoy %			Deposits Chg yoy %			Loans rate ¹ -NewB* %		DepositsRate ¹ -NewB* %		Loans/Dep %						
	Last	Mth	2017	Last	mth	2016	Last	mth	2017	Last	Mth	2017	Last	mth	2017	S ⁴	Last	mth	2017				
CEE																							
Czech Rep.	6.2	Feb	6.5	3.7	Feb	4.8	21.0	Feb	69.6	6.5	Feb	7.6	2.43	Feb	2.33	C	0.87	Feb	0.66	H	75.4	Feb	75.8
Hungary	4.7	Feb	6.0	6.0	Sep	9.0	10.1	Feb	12.2	13.7	Feb	10.8	2.22	Feb	2.50	C	0.27	Feb	0.24	H	78.9	Feb	80.1
Poland	3.2	Feb	3.2	9.2	Dec ⁵	10.5	-11.7	Feb	-13.0	4.1	Dec	4.1	3.64	Feb	3.66	C	1.65	Feb	1.65	H	98.0	Dec	98.0
Slovakia	9.4	Feb	9.6	4.1	Feb	4.7	-10.2	Feb	-6.0	5.1	Feb	5.2	2.06	Feb	1.97	C ²	0.07	Feb	0.07	H ²	100.2	Feb	98.8
Slovenia	2.8	Feb	3.2	6.0	Dec	8.5	-14.5	Feb	-13.4	7.0	Feb	7.0	2.38	Feb	2.41	C ²	0.15	Feb	0.14	H ²	78.1	Feb	78.3
SEE																							
Albania	0.9	Feb	0.5	13.7	Feb	18.3	3.9	Feb	0.0	-0.9	Feb	-1.3	8.52	Feb	7.26	PS	0.8	Feb	n.a.	PS	53.6	Feb	53.3
Bosnia H.	7.6	Feb	7.3	10.0	Dec	11.8	5.0	Feb	4.6	8.6	Feb	9.0	3.98	Feb	3.51	C	0.29	Feb	0.23	H	108.4	Feb	108.4
Croatia	0.7	Feb	-0.1	11.4	Dec	13.8	-12.0	Feb	-17.8	3.2	Feb	2.4	6.75	Feb	3.74	PS	0.67	Feb	0.97	PS	79.4	Feb	78.6
Romania	6.1	Feb	5.6	6.4	Dec	9.6	-6.0	Feb	-9.1	12.7	Feb	10.4	6.63	Feb	4.93	PS	1.11	Feb	0.80	PS	76.6	Jan	76.7
Serbia	2.5	Feb	2.1	9.6	Feb	17.0	26.2	Feb	14.4	3.4	Feb	3.1	9.0	Feb	4.75	PS	2.84	Feb	3.03	PS	102.7	Feb	101.3
CIS MENA																							
Russia	5.9	Jan	5.2	10.4	Jan	9.4	-16.4	Jan	-17.5	6.5	Jan	8.1	9.14	Jan	9.43	C	5.53	Jan	5.27	H	106.9	Jan	104.8
Ukraine	5.8	Jan	0.9	54.5	Dec	30.5	-20.9	Jan	-23.5	13.1	Jan	12.1	16.94	Jan	15.54	PS	9.83	Jan	13.37	PS	129.4	Jan	123.0
Egypt	7.1	Dec	7.1	4.9	Dec	5.8	1.1	Dec	1.1	23.8	Dec	23.8	19.7	Feb	19.8	C	13.5	Feb	13.6	H	33.9	Dec	33.9
m.i. E. A.	2.1	Feb	1.0	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	16.7	Feb	n.a.	1.20	Feb	n.a.	C	0.36	Feb	0.4	H	82.2	Feb	81.5

Source: Central Banks, IMF, Moody's; ¹monthly average; ²lending rate on current account overdraft; on deposits up to 1 year

³Sector C=Corporates, H=Household, PS=Private Sector. ⁵impairment loans as defined by the CB.

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