INTESA SANPAOLO

# Monthly Note

## Countries with ISP Subsidiaries

October 2017

Monthly note

Intesa Sanpaolo
International Research Network

**For 3Q, high frequency indicators signal a strengthening of the cycle in the CEE/SEE area and in Egypt. Monetary stance remains easy overall, except in CZ and UA. Further rate cuts are expected in Russia.**

High frequency indicators signal a overall continued strengthening of the economic cycle in CEE and SEE countries with ISP subsidiaries in 3Q. Economic growth appears to be broad-based, supported by both domestic and external demand. In August, retail trade was generally strong, with growth rates ranging from 4.4% in Serbia to 12.6% in Romania, supported by falling unemployment rates. In parallel, export growth was also robust in August and above the 2Q average in all CEE/SEE countries. Surveys showing, among others, PMI growing at 59.3 in Hungary and ESI close to historical highs in Slovenia and Slovakia signal expectations of a solid economic growth pattern continuing in September.

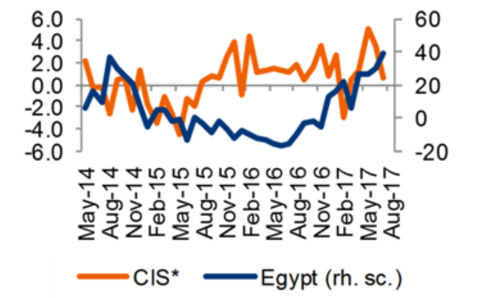
In the CIS area, in Russia, GDP growth may have eased a little in 3Q compared to the 2.5% yoy increase in 2Q. In Ukraine as well, recent releases support the view of a slowdown in 2H17, related to the trade blockade in the Donbass region. In contrast in Egypt, industrial production, which rose by 24% yoy in the first eight months of 2017, implies an acceleration of GDP growth.

Inflation rates in almost all CEE and SEE countries appear to be slightly rising, due to pressures from wage increases, which are only partially balanced out by contained energy prices and (with exceptions, such as CZ and Romania) still spare production capacity. CBs are keeping easy monetary stances overall, except in CZ where the CB has actually reversed the course of monetary policy in August by raising the reference rate by 20bps while further increases are expected in the near term. In Serbia, due to a weakening of the economy and a decline in inflation, the CB cut the policy rate by 25bps in September and again in October to 3.5% currently. In Hungary, the MNB also cut the O/N deposit rate to -0.15% in September and further reduced the cap on its 3M deposit facility. The extension of the QE programme by the ECB in the October Meeting to September 2018, *or beyond if necessary* (with the APP halved at € 30 Bn. a month since Jan. 2018) will continue to support an accomodative stance in the region.

In the CIS area, in Russia, headline inflation fell to a new low in September (+3%), leading to a new rate cut (by 25 bp) by the CBR in October, while in Ukraine, due to persisting high inflation (16.4% in September), the CB raised its policy rate at its October meeting. In addition, in Egypt, the CB made no policy changes, awaiting the start of the disinflationary process.

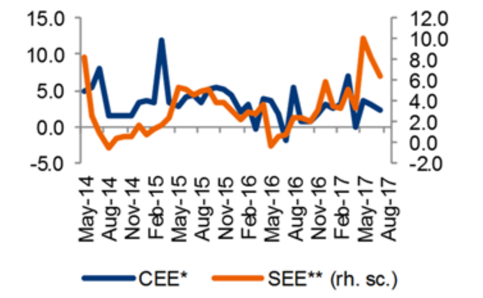
Banking aggregates generally accelerated in the CEE region, but in several SEE countries as well. Mortgages to households continued to be particularly dynamic, forcing CBs in some cases to adopt measures to prevent a debt overhang among households. Corporate loans are recovering, especially in CEE countries, where the business cycle is in a more advanced stage. NPLs/Total loans ratios are on a decreasing path in the region, but at over 10% in most SEE countries. On the funding side, banks are benefitting from a firm increase in deposit rates, in both the household and corporate sectors, and a strong liquidity cushion. Banking aggregates in Russia and in Ukraine as well remained particularly weak. In Egypt, the extraordinary increase mainly related to the accounting effect experienced in the past year regarding EGD depreciation.

**Industrial production % yoy – CIS – Egypt**




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

**Industrial production % yoy – CEE – SEE**




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

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**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 and in particular: Slovakia, Slovenia and Hungary among CEE countries; Albania, Bosnia, Croatia, Serbia and Romania among SEE countries; Russia and Ukraine among CIS countries; and Egypt among MENA countries.**

**The figures in this document have been updated as of 27th October 2017.**

# Cross Country Analysis

## CEE area

Antonio Pesce

Favourable external conditions (in the Euro area, the Eurocoin index improved further in October to 0.72) and improving internal features, namely decreasing unemployment and wage increases and withdrawal of EU structural funds, are supporting the solid economic growth on the demand side, especially in CEE, but also in SEE countries with ISP subsidiaries.

In the CEE region, in Czech Republic in August, the industrial production dynamic, albeit below the 2Q average, improved to 5.8% yoy from 3.3% yoy; in addition, retail trade accelerated in August (4.8% yoy from 4.6% in real terms). In the same month, exports grew (4.8% yoy in nominal terms) above the 2Q average. In September, the unemployment rate fell to 3.8%.

Growth of industrial production and retail sales (6.8% yoy and 4.6% yoy, respectively), above the 2Q average, and an export dynamic in double digits (10% yoy) in August mirrored the good performance of the Hungarian economy overall. In addition, in September, the manufacturing PMI grew further, to 59.3, and the ESI indicator improved to 121.9. In Slovenia as well high frequency economic indicators continued to signal a strengthening of the economic cycle. In August, industrial production rose by 8.3% yoy (from 6.5% previously). In July, exports grew at a 12.5% rate yoy, and in September, the ESI improved to 114.

Due to a contraction in the manufacturing sector (-0.6% yoy), Slovakian industrial production growth was slightly negative (-0.4%) in August, after experiencing a strong positive trend in previous months. In the same month, export growth (5.9% in nominal term) was actually higher than the 2Q average, and in September, the ESI (104.9) recorded a record high for this year. Job market conditions improved further in September and the unemployment rate decreased to 6.4%.

On the inflation side, in August in CEE countries, the rates were above the 2Q average or, as in the case of Slovenia, in line with it. The consumer price dynamic ranged from 1.4% in Slovenia to 2.7% in Czech Republic. In general, the consumer price path is still slow due to low international price dynamics and the availability of production capacity, with the only exception being Czech Republic, where the actual inflation rate rose above the CB's target (2.0%). Since the economic trend (4.4% yoy GDP growth in 2Q) is close to the potential growth rate, the Czech policy rate was increased by the CB by 20bps in July, to 0.25%, and it is projected to rise further in coming months. On the other hand, in September, the Hungarian central bank further loosened monetary conditions by lowering the overnight deposit rate by 10bps, to -0.15%. At the October meeting, the Hungarian central bank Board decided to keep the upper limit on the 3M deposit facility set in September unchanged at HUF 75Bn.

Davidia Zucchelli

In August, banking aggregates increased further in the CEE region. Lending growth accelerated in many countries, still mostly supported by the household sector. Interest rates remained low, in line with money market rates, but showed slightly different patterns in some countries.

In Czech Republic, loans growth accelerated further (7.1% yoy in August from 6.9% yoy in July). The dynamic of foreign currency-denominated loans continued to be particularly strong (25%), especially in the household sector (58.6%). In the corporate sector — where foreign currency-denominated loans account for around 30% of the total — lending growth increased significantly as well (24.7% yoy). The NPL ratio is low (4.1%) and decreasing, but new delinquencies as mortgages mature after a period of rapid growth have started to emerge, which has been highlighted by rating agencies. Deposits were also dynamic (9.4% yoy in August after 9.6% yoy in July), particularly from households (8.9%), despite low interest rates. Interest rates on lending to corporates increased in August, while the deposit rate for households decreased.

In Hungary, the recovery of the economy supported the acceleration in growth of loans to corporates (6.6%). Total loans increased to 4% (from 3.4% yoy in July), also thanks to a recovery in household loans (1.4%). Deposits accelerated as well (11.5% from 10.4% yoy in July), particularly from businesses (15.7% in August), but also from households (7.9%).

Lending growth continued to be strong in Slovakia as well (11.3% yoy in August from 10.9% in July) fuelled by economic growth and low interest rates, both in the corporate sector (by 9.6%) and especially in the household (by 13.2%) sector, driven by a rise in mortgages. Deposits also grew (4.7% yoy from 3.6% yoy in July), particularly among households (5.7%), despite the increasing competition from other savings products. In the corporate sector, they rose by 3.4% yoy.

In Slovenia, the outstanding amount of corporate loans strengthened by 4.2% yoy. Total loans showed a slight acceleration (5.5% yoy from 4.2% yoy as of July), thanks also to a further increase in household loans (6.8% yoy). NPLs amounted to 5.8% of total loans at the end of 2016, but, according to the European Banking Authority's broader definition of NPLs (which also includes some restructured loans), the ratio was higher (but still on a declining path) at 11.5%. As far as deposits are concerned (+6.3% yoy in August in the private sector), corporate deposits accelerated strongly (9.4% from 6% yoy in July) while deposits from households increased by 5.3% yoy (5.4% yoy in the previous month).

## SEE area

Antonio Pesce

Among SEE countries as well, the latest high frequency data confirmed a consolidation of the economic cycle. In Croatia, industrial production accelerated to 3.2% yoy in August, with growth remaining above the 2Q average (2.5%). In the same month, the retail trade dynamic was still strong (6.4% yoy in real terms) and exports jumped to 11.3% yoy. The unemployment rate, albeit still high, declined further in September, to 10,8%.

In Romania, economic cycle indicators —ie, industrial production (9.8% yoy), exports (10.7% yoy) and retail trade (12.6% yoy)— were strong in August and the unemployment rate remained at its lowest level (4.2%) of the last years. In September, the ESI was still close to the record high for this year, albeit slightly lower than in August.

In Serbia, the industrial production trend improved in August (to 7.3% from 4.2%) and remained higher than the 2Q average. Retail trade also accelerated in the same month (4.4% yoy from 4.1%), as did exports (almost 15% in nominal terms from 10.3%). The export dynamic remained very strong in August in Albania and Bosnia as well (12% yoy and 20.4% yoy, respectively).

In September, inflation rates in Croatia and Romania were higher than in 2Q, while in Albania and Bosnia (August data), they remained broadly in line with the 2Q respective averages. In Serbia, the consumer price dynamic, although increasing to 3.2% in September from 2.5% previously, was still below the 2Q average (3.7%).

At the most recent Boards meetings, all the central banks of SEE countries with ISP subsidiaries confirmed their easing monetary policies or loosened monetary policy conditions further, as the National Bank of Serbia did by cutting the policy rate by 25bps, to 3.5%. In Romania, in October, the National Bank decided to keep the monetary policy rate unchanged at 1.75%, but narrowed the interest rates corridor on the NBR's standing facilities to +/-1.25% (from +/-1.5%). The short-term interest rate increased then to 1.6% from 0.6% three months ago. Exchange rates vs the euro were roughly stable in the last months, and CDS spreads fell further in the region.

Davidia Zucchelli

Regarding banking aggregates, in August, lending showed signs of improvement in SEE countries as well (with Albania and Croatia the only exceptions), even though this was to a lesser extent than in CEE countries. Despite low interest rates, deposits accelerated in every country in a context, however, of modest investment alternatives. As in CEE countries, the dynamics of the banking interest rates for new business showed a different pattern among countries and between corporates and households.

In **Albania**, loans declined further (-0.15% yoy in August from -0.8% yoy in July) because of a decrease in the corporate sector (-2.2% yoy), which accounts for 70% of loans to the private sector, while loans continued to show dynamic growth in the household sector (4.5%). Loans in foreign currency experienced a strong decrease again (-6.1% yoy), particularly in the corporate sector (-7.6% yoy), where they account for 57% of total loans. In the household sector, the reduction was lower (-1.3%). NPLs remained quite high (15.3% as of July). Deposits were roughly stable overall (-0.04% yoy) in August; household deposits fell, however (-2.1%), while deposits from businesses increased again substantially (11.5%).

In **Bosnia**, loans continued to follow an increasing path (7.2% in August from 6.8% yoy in July) both in the corporate (7.6% yoy) and the household (6.7% yoy, particularly consumer loans) sectors. Deposits continued to increase as well (8.3% from 8.9% yoy in July). In **Croatia**, loans shrank further as a stock, by 0.2% (from a fall of 0.5% yoy in July), but transaction data estimated by the CB showed positive signs (9% mom growth in May). Lending stocks decreased by 0.2%, both in the corporate and the household sectors Deposits continued to grow (2.2% from 1.7% yoy in July), particularly from businesses (8.4%), while households remained broadly stable (0.4%).

In **Romania**, loans increased in August (6.4% from 5.1% yoy in July), particularly in the household sector (7.7% yoy), but loans to corporates accelerated significantly (5.0% yoy), supported by the strong cyclical phase. Deposits continued to perform well (11.6% from 10.7% in July).

In **Serbia**, loans grew by 2.7% yoy in August (from 2.5% yoy in July), particularly in local currency (+11% yoy); loans denominated in foreign currency (67% of total loans) declined by 2.4%. Total loans were driven by loans to households, although decelerating (9.9% yoy), while loans to corporates declined (-2.4% yoy). Deposits continued to perform extremely well (15.4% from corporates and 2.4% from households). Deposits in foreign currency accounted for 72% of the total (49% in the household sector and 81% in the corporate sector).

## CIS and MENA areas

Giancarlo Frigoli

In **Russia**, the latest data suggest that GDP growth may have eased a little in Q3 compared to the 2.5% yoy increase recorded in Q2. The performance of the industrial sector was a bit disappointing. Following the 0.9% yoy gain seen in September (slowing from +1.5% in August partly due to working day effects, as there was one less working day this year), industrial output rose by an average 1.2% yoy in the quarter, down from 3.8% yoy in Q2. More positive news came from the agricultural sector, where production increased by 8.5% yoy in September and by 3.4% yoy in Q3. More importantly, retail sales rose by 3.1% yoy in September and by 2.1% yoy in Q3. Consumers are benefitting from higher wages and a further fall in inflation, as the headline index dropped to a post-Soviet low of 3.0% yoy in September from 3.3% in August. Construction, which rose a modest 0.1% yoy in Q3, continued to underperform other sectors. With both headline and core inflation well below target in September (at 3% and 2.8%, respectively), the CBR cut its main policy further in October (by 25 pb to 8.25%) following the 50 bp cut in September. Ms Nabiullina, the CBR Governor, said in recent public statements that she saw the key rate at 6.5-7.0% in 2019.

In **Ukraine**, 3Q data releases confirmed that construction, which rose by 23.8% in September and by 24.6% in 3Q, together with retail sales (up 8.2% yoy in September and by 8.2% yoy in the July-September period of this year) are the main engines of growth amid a scenario of still-weak industrial production (-0.4% in Q3) and a slight decline in agricultural output. The trade blockade with the Donbass region is weighing on electricity generation and steel output, due to shortages in the supply of coal. Agricultural output was down by 0.7% from January to September compared to last year's levels mainly reflecting smaller crops of cereals, sugar beet and sunflowers. These numbers support the view of a contained deceleration in the pace of GDP expansion in the second half of this year, leading to an expectation for a mild slowdown in real GDP growth this year (to 2%). Inflation accelerated to 16.4% in September, its highest level since March 2016, on the back of tariff increases and price hikes on alcoholic beverages and tobacco. To contain inflationary pressures, the central bank raised its policy rate by 100bps (to 13.5%) at its end-October meeting.

The latest round of talks between Ukraine and the IMF on a new tranche of a USD 17.5Bn loan have made little progress. The IMF approved the loan for Ukraine in 2015. Under the relevant memorandum, the funds could be released in instalments provided the government was making progress on agreed economic and anti-corruption reforms. Ukraine received the most recent tranche worth USD 1Bn in April 2017 (for a total of USD 8.4Bn distributed). The government has so far been reluctant to stick to its own resolution to increase the price of natural gas for private consumers by 17.6% as of 1 October. According to the press, talks could now be frozen until April 2018, and resume at the end of the heating season. At that time, the government might be ready to raise tariffs.

In Egypt, headline CPI inflation slowed slightly to 31.6% yoy in September from 31.9 yoy in August. At the same time, the annual rate of core CPI declined to 33.3% in September from 34.9% in August. Inflation is likely to see a significant fall next year, as the effects of the November 2016 currency devaluation cease. The ECB set the inflation target at 13% (+/-3%) in 4Q18 and to single-digit rates thereafter.

Industrial production rose by 23.8% in August and by 24% in the first eight months of this calendar year. Tourism, manufacturing, natural gas and trade all recorded strong gains in the period. Construction and electricity generation however fell. Activity numbers sustain our view of an acceleration in GDP in the 2017 calendar year and in the 2018 fiscal year, which started last July. We see GDP to rise by 4.5% in calendar 2017 and by 4.6% in 2018. The IMF in its October's release of the WEO report projected Egypt 's GDP growth in 2018 at 4.5%.

Davidia Zucchelli

In Russia, bank lending decreased again in August, (-1.3% yoy from 0.1%) because of a new significant decrease in the corporate sector (-3.7% from -1.7% at June), which accounts for around 75% of loans to the private sector. In contrast, household lending experienced an acceleration to 6.7% yoy (from 5.8% yoy in June). In July, deposits increased by 3.6% yoy (from 4.8% in June). In line with official rates, interest rates on new loans to businesses declined to 10.44% (from 10.68%), but the interest rate on deposits from households continued to follow a more unclear trend, increasing to 6.07% (from 5.7%). The interest rate spread remained much higher in the household sector (14.2pp vs 16pp) than in the corporate sector (2.8pp vs 3.3pp) in July vs December 2016.

Lending in Ukraine saw a further decrease in August (-3.6% from -1.6% yoy in July). Loans to corporates decreased by -4.1% (the share of private sector loans is over 80%). Household loans showed a more contained decrease (by -1.5%). Deposits increased by 5.9% (with respect to 7.7% yoy in July) both from corporates (8.4% from 10.4% in July) and households (4.7% from 6.3%). NPLs remained the Sword of Damocles. The NPL ratio, calculated according to the new accounting rules, increased to well over 50%. Coverage is significant (77.3%), but the "NPL net of provisions to capital" ratio was 96.3% at June.

In Egypt in June, loans and deposits grew strongly (nominally by 37% and 43%, respectively), due to the accounting effect of the local currency depreciation (net of that effect, performances are estimated at 3.7% and 14.9%, respectively). The fx effect was stronger in the corporate sector, where loans in foreign currency accounted for almost 41% of total loans, while in the household sector, they accounted for just 3% of the total. Deposits increased, both from corporates (31%) and households (47%). The LTD ratio remained very low (37% and decreasing from 39.2% in December 2016). In line with official rates, lending interest rates on new business increased to 18.5% in July (from 18% in June) and deposit interest rates rose to 12.4% (from 11.2% in June).

# Country-Specific Analysis

## Albania

### Real Economy

Kledi Gjordeni

The analysis of available data indicates that economic activity in Albania continued to grow in the second and third quarters, driven by both domestic and external demand, while inflation declined in August and September. The rise in employment, the improvement of financing conditions, and the improvement in confidence in production sectors have supported the expansion of consumption and private investment.

The latest GDP data from 2Q17 show growth of 4.06%, which is higher than the previous CB forecast of 3.9%. During 2Q17, the unemployment rate decreased by 1.6% yoy, to 13.9 %. In September 2017, exports of goods amounted to ALL 24Bn, an increase of 16.8% yoy and 30.3% compared to the previous month. In parallel, imports of goods amounted to ALL 53Bn, an increase of 10.5% yoy and 7.6% vs August 2017. The trade deficit in September was ALL 29Bn, higher by 5.7% compared to September 2016, but lower by 5.9% compared to August 2017. During 9M17, exports of goods were up by 13.3% yoy and imports by 6.8% yoy.

In September 2017, the annual rate of consumer prices was 1.6 % vs 1.8% a year ago. The decline in inflation reflected a slowdown in food prices, especially unprocessed food, whereas other groups did not show notable volatility. CB projections for average inflation in 2017 have been revised slightly downward, from 2.2% to 2.1%

### Financial Markets

Expected economic and price developments support the current monetary policy stance. The monetary policy rate is expected to remain unchanged in the short term, at 1.25%. The CB deems that the intensity of the monetary stimulus will not diminish before 2Q18. In any case, the normalisation of monetary policy should be prudent, with the aim of guaranteeing price stability in the medium term and supporting the stability of economic growth. Foreign investment, an improved trade balance, and higher revenues from tourism continue to influence the exchange rate. In September, the Lek appreciated further by 2.81% yoy against the euro.

### Banking Sector

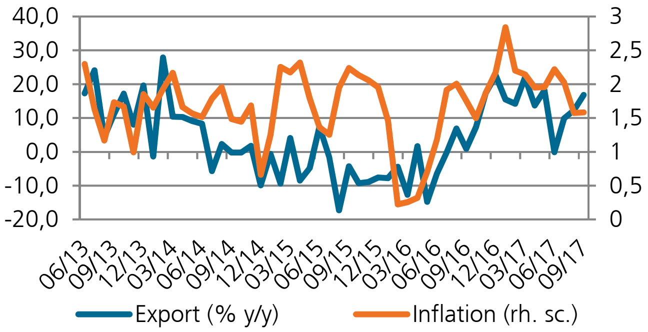
As a result of the measures taken to reduce the level of non-performing loans, their ratio to total loans fell to 15.14% in August, the lowest level since 2011. The non-performing loans ratio has been decreasing for almost all the banks in the system, and reflects not only the regulatory requirement for writing them off, but also the repayment of loans by the private sector. In August 2017, total loans yoy to the private sector decreased slightly, by 0.15%. Household loans increased by 4.50%, while corporate loans decreased by 2.15%. On the deposit side, the last data from August 2017 show a slight increase in total deposit of 0.15%. Household deposits shrank by 2.19%, while corporate deposits expanded by 14.4% yoy.

**Last economic indicators**

| % | Last value | 2Q17 | 1Q17 |
|---|---|---|---|
| Industrial production, wda yoy | n.a. | n.a. | n.a. |
| Export of goods, nominal yoy | 12.1 (Aug) | 10.5 | 15.7 |
| Unemployment rate | n.a. | 13.9 | 14.2 |
| Inflation rate, average yoy | 1.6 (Aug) | 2.0 | 2.4 |
| Loans (priv sector, yoy, eop) | -0.2 (Aug) | -1.7 | -0.1 |
| Deposits (priv sector, yoy, eop) | 0.0 (Aug) | 1.3 | 1.5 |

Source: INSTAT, Central Bank of Albania

**Export and inflation**




Source: INSTAT

## Bosnia and Herzegovina

### Real Economy

Ivana Jovi□

Following 2.8% yoy growth in 1Q17, 2Q GDP data surprised, with lower-than-expected 1.7% yoy growth. Details reveal that slowdown in growth was triggered by 7.8% and 1.1% yoy lower GVA in agriculture and construction, respectively, and is partly explained by bad weather conditions, but by lower public investment as well. Although supportive of growth, both manufacturing (+3.1% yoy) and trade, accommodation and transportation (+4.4% yoy) registered slowdowns in growth compared to the previous quarter (+4.4% and +5.4% yoy, respectively). Even though the slowdown in 2Q reinforces the potential for downside risks to our current 3.0% growth estimate, we currently maintain it, as 3Q high frequency data reflects supportive trends. Specifically, July-August data indicate strong 6.1% yoy growth in industrial production, supported by as much as 23% higher exports and 5.0% stronger retail trade volume.

The inflation rate inched up to 1.0% yoy in August (from 0.9% in July), and strengthened further to 1.5% yoy in September, with the nine-month average still at 1.1% yoy growth. September's 0.5% mom growth was mainly fuelled by seasonally higher prices of clothing (5.1% mom), food products (0.7% mom), energy (0.5% mom) and transport (0.4% mom).

### Banking Sector

Ana Lokin

Loan growth continued to accelerate (July +6.8% yoy, August +7.2% yoy), mostly as a result of strengthening of corporate demand. Loans to non-financial corporations rose by 7.1% yoy in July and by 7.7% yoy in August. Household loan growth also accelerated, but more moderately, from 6.5% yoy in July to 6.8% yoy in August. Breaking down household loans by purpose shows that the strongest rise, as previously was the case, was observed to be in consumer loans (July +8.5% yoy, August +8.6% yoy); housing loans did show some signs of recovery as well (July +0.9% yoy, August +1.6% yoy).

Deposit growth remained robust (July+ 8.9% yoy, August +8.3% yoy), in line with positive real sector developments and credit growth. The rise in household deposits decelerated somewhat (July +7.8% yoy, August +7.3% yoy), as did the growth of deposits of non-financial corporations (July +11.7% yoy, August +10.6% yoy).

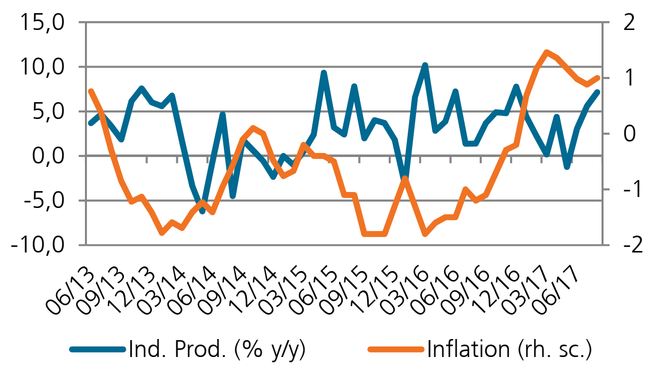
Loan quality continued to improve. Thus, at the end of 2Q, the total NPL ratio amounted to 11.1%, down by 0.4 pp qoq. The share of loans to non-financial corporations declined by 0.5 pp qoq, to 13.9%, and loans to households fell by 0.3 pp qoq, to 8.0%, where the share in consumer loans slipped by 0.2 pp qoq, to 6.9%. In line with a more moderate profit rise in 2Q (1Q17 +29.9% yoy, 1H17 +25.8% yoy), ROAA and ROAE weakened in 2Q17, to 1.7% and 12.1% (1Q17: 2.0% and 13.6%), respectively. The capital adequacy ratio increased slightly: at the end of 2Q17, it stood at 15.9%, up by 0.2 pp qoq.

**Latest economic indicators**

| % | Last value | 2Q17 | 1Q17 |
|---|---|---|---|
| Industrial production, wda yoy | 7.1 (Aug) | 2.1 | 2.2 |
| Export of goods, nominal yoy | 20.4 (Aug) | 13.7 | 17.4 |
| Retail trade, real, wda yoy | 5.9 (Aug) | 5.6 | 5.9 |
| Inflation rate, average yoy | 1.0 (Aug) | 1.2 | 1.1 |
| Loans (priv sector, yoy, eop) | 7.2 (Aug) | 6.2 | 4.8 |
| Deposits (priv sector, yoy, eop) | 8.3 (Aug) | 9.1 | 8.4 |

Source: BHAS, CBBH

**Industrial production and inflation**




Source: Labour and employment agency

# Croatia

## Real Economy

Ivana Jovi□
Ivan Odr□i□

After the slowdown in July, to 2.5% yoy, growth in industrial production recovered to 3.2% in August, due to a 3.4% increase in manufacturing (o/w food production rose by 10.0%), while real retail trade turnover accelerated to 6.4% yoy (5.9% in July), supported by an excellent tourist season (6.1% yoy arrivals) and rising wages (5.0% yoy real net wages). Fuelled by strong foreign demand, export of goods posted double-digit growth rates in both July (11.3%) and August (12.3% yoy). Investment activity continued to be driven by private investment, as the construction work index suggests 5.6% yoy growth in building construction and a 2.5% yoy decline in civil engineering work. A private-investment-based recovery has also confirmed by fiscal data which indicate a strong 23% yoy decline in gross fixed capital formation by the government in 1H17.

Inflation accelerated to 1.4% yoy in September (1.0% in August), owing to a strong increase in food prices while lower electricity prices based on a decrease in VAT were partially offset in September by a hike in surcharges for renewable energy sources, thus resulting in an average 3Q17 annual inflation rate of 1.1%.

## Financial Markets

Ana Lokin

The money market was calm in September, with the liquidity surplus at HRK 14Bn. Average 3M Zibor decreased by 1 bps mom, to 0.59%. The market remained lethargic in October, without any movements rates. Foreign currency inflows started to subside in September as the tourist season ended, which put depreciation pressures on the kuna. The average EUR/HRK rate rose to 7.45, +0.7% mom. In October, the kuna continued to weaken, albeit slowly, with the fx rate expanding to 7.51. The 10Y government bond yield continued on a declining trend in September, falling by 20 bps mom on average, to 2.6%, supported by S&P's rating outlook upgrade.

## Banking Sector

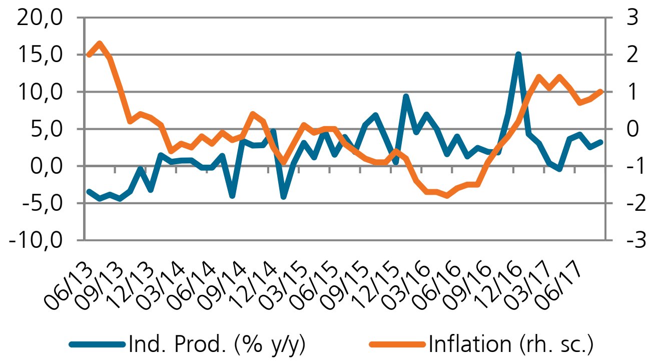
Private sector demand rose, as transaction data show, according to which the claims in the private sector rose by 2.8% yoy in August, which resulted in a moderation of the pace of loan decreases (-0.2% yoy). In August, corporate loans edged down by 0.2% yoy, the same as seen for household loans. The breakdown by purpose shows that investment and other corporate loans are recovering, while in the retail segment, 'cash' and 'other purpose loans' continue on a positive trend. Deposit growth remains around 2% yoy (August +2.2% yoy), where rise in corporate deposits stays strong (+8.4% yoy). Although the outflow of euro time deposits ceased in July-August, thanks to inflows from tourism, household deposits recorded a modest 0.4% yoy increase, affected by adverse fx rate movements. The NPL decline resumed in 2Q17, with the ratio dropping by 0.8 pp qoq, to 13.2%, as a result of high amount of sold claims, as a result of which the corporate NPL ratio declined by 1.5 pp qoq, to a still-high 27.1%, and the household ratio fell by 1.0 pp qoq, to 9.1%.

**Latest economic indicators**

| % | Last value | 2Q17 | 1Q17 |
|---|---|---|---|
| Industrial production, wda yoy | 3.2 (Aug) | 2.5 | 2.4 |
| Export of goods, nominal yoy | 11.3 (Jul) | 7.6 | 22.6 |
| Retail trade, real, wda yoy | 6.4 (Aug) | 4.8 | 5.2 |
| ESI (index) | 116.4 (Sep) | 115.8 | 119.0 |
| Inflation rate, average yoy | 1.4 (Sep) | 1.1 | 1.1 |
| Loans (priv sector, yoy, eop) | -0.2 (Aug) | -1.3 | -2.3 |
| Deposits (priv sector, yoy, eop) | 2.2 (Aug) | 1.9 | 2.8 |

Source: CBS, EC, CNB

**Industrial production and inflation**




Source: EC

## Czech Republic

### Real Economy

Zdenko Štefanides

The Czech economy continues to boom even though high frequency activity data have recently posted some deceleration following the torrid 2Q pace. Although volatile, the data confirm the underlying pace of GDP growth at close to 4%. Crucially, the Czech economy now features widespread inflationary pressures. Consumer price inflation picked up to 2.7% yoy in September from 2.5% in the previous month, while house price growth rose to 13.2% yoy, the fastest pace of growth in Europe (2Q data). And, with the unemployment rate holding at 2.9%, the lowest level in the EU, average nominal wage growth for the overall economy accelerated to 7.6% yoy in 2Q, from an already strong 5.3% pace recorded in the previous quarter.

On the political font, the Czech Republic held parliamentary elections on 20-21 October. The results refer to a striking victory for the populist movement, ANO, headed up by former Finance Minister Andrej Babis. Despite its dominance, with nearly 30% of votes and 78 seats in the 200-seat lower house of parliament, it will be challenging for ANO to form a coalition government because of the very fragmented parliament (with a record nine parties represented) as well as controversy surrounding its leader (Mr Babis has been accused of EU subsidy fraud). In any case, we do not expect political developments to have a significant impact on economic performance. ANO was a junior coalition partner in the outgoing government and judging by its fiscally responsible track record it is unlikely to shift economic policy in a material way.

### Financial Markets

Amid a booming economy and rising inflation, the CNB remains in hawkish mode and the potential for rate hikes remains: it is only a question of when and by how much rather than if. After lifting rates in August, the CNB was close to raising rates again in September. The CNB board, however, voted four to three in favor of taking a pause to wait to see the new quarterly Inflation forecast, due for approval at the upcoming meeting on 2 November. We expect the repo rate to be raised by 25 bps at that time, but do not exclude even a 50 bps hike. Further hikes in 2018 seem likely, and probably at a steeper rate than foreseen previously. The CZK remains under appreciation pressure, gaining 1.9% vs the euro in the past month alone. At its current level of 25.6 vs the euro, the koruna is thus 5.2% stronger vs the CZK 27.0 cap abandoned in April.

### Banking Sector

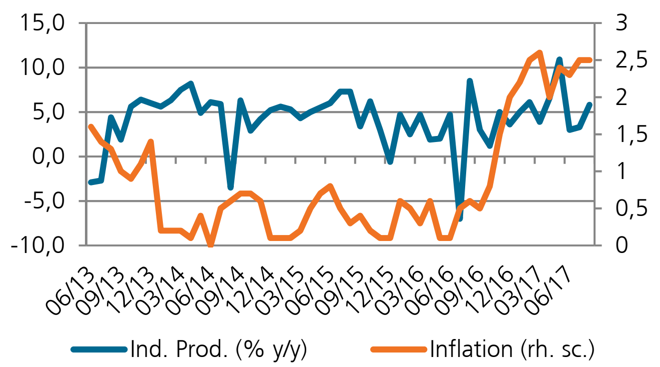
A fast-growing credit market is the key factor fueling a property market boom. The central bank is thus trying to slow things down by tightening credit conditions. It has said that banks should start to comply with bank recommendations and gradually tighten lending standards. Hitherto, though, there has not been a visible moderation in the pace of growth of credit itself. The stock of mortgage loans grew at a rate of 10.3 % yoy in August, a similar pace to those recorded in the previous three months. The broader category of housing loans (including building societies) and overall household loans also maintained their previous growth dynamics, at 9.5% and 8.2%, respectively.

**Latest economic indicators**

| % | Last value | 2Q17 | 1Q17 |
|---|---|---|---|
| Industrial production, wda yoy | 5.8 (Aug) | 6.8 | 5.0 |
| Export of goods, nominal yoy | 4.8 (Aug) | 4.6 | 7.4 |
| ECB refi rate | 0.2 (24th Oct) | 0.0 | 0.0 |
| ESI (index) | 108.4 (Sep) | 106.9 | 106.5 |
| Inflation rate, average yoy | 2.7 (Sep) | 2.2 | 2.4 |
| Loans (priv sector, yoy, eop) | 7.1 (Aug) | 7.3 | 6.7 |
| Deposits (priv sector, yoy, eop) | 9.4 (Aug) | 9.6 | 10.2 |

Source: CBS, EC, CNB

**Industrial production and inflation**




Source: EC

# Egypt

## Real Economy

Samer Halim

Preliminary data point to a GDP growth rate of 4.2% in FY16/17 compared to 4.3% in FY15/16, when 4Q FY16/17 grew at 5% compared to 4.5% in the same period of the previous year. Suez Canal revenues increased by 3.4% in the January- September 2017 period, to USD 4.3Bn, due to the improvement in international trade volumes and incentives offered by the Suez Canal Authority to customers. Tourism revenues also jumped by 211.8%, to USD 5.3Bn, during the first nine months of 2017 compared to USD 1.7Bn in the same period a year earlier, mainly due to the rise in tourist numbers and their spending. Furthermore, Egypt's trade deficit declined by 37%, to USD 20.1Bn, during the period between January and August 2017, due to the rise in the country's non-petroleum exports by 11%, to USD 15Bn, and the decline in imports from USD 45.5Bn to USD 35.1Bn in the same period. Finally, Prime Minister Sherif Ismail stated that Egypt's giant new offshore Zohr gas field in the Mediterranean is set to produce 500m cubic feet per day by the end of 2017, adding that imports should decline significantly once the field starts producing.

## Financial Markets

The rate of urban CPI inflation eased for the second consecutive month in September 2017, when the headline rate fell to 31.59% (yoy) and 1% (mom) from 31.92% (yoy) and 1.13% (mom) in August 2017. The Monetary Policy Committee (MPC) decided at its meeting on 28 September to leave the overnight deposit, overnight lending, and the discount rates unchanged at 18.75%, 19.75%, and 19.25%, respectively. However, the CBE did decide to raise the Reserve Requirement Ratio (RRR) of banks from 10% to 14% in a bid to curb inflation. The EGP remained relatively stable against the USD in September, at EGP 17.66 compared to EGP 17.76 rate recorded in August. Net International Reserves rose by 1.1%, to USD 36.53Bn in September 2017, covering 7.8 months of imports, compared to USD 36.14Bn in August 2017.

## Banking Sector

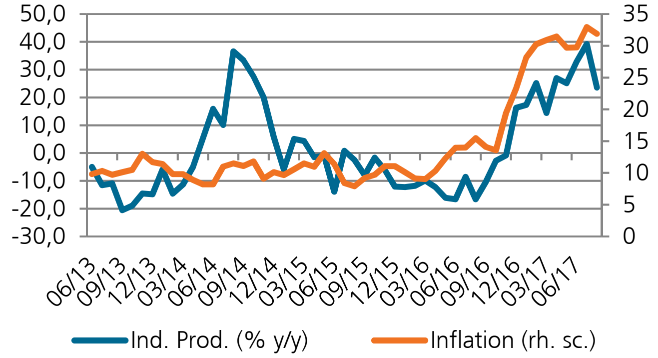
Total deposits from the private sector recorded an annual increase of 43%, reaching EGP 2.4Tn by the end of June 2017 on the back of the 114% rise in the value of foreign currency deposits (27.1% of total private deposits) following the sharp depreciation of the exchange rate after the floating of the Egyptian pound in November 2016. In parallel, total loans to the private sector also rose significantly, by 37%, to EGP 906.7Bn. This increase can also be attributed to the strong increase (by 78%) in the value foreign currency loans (31.6% of total private loans), following the depreciation of the Egyptian pound.

**Latest economic indicators**

| % | Last value | 2Q17 | 1Q17 |
|---|---|---|---|
| Industrial production, wda yoy | 23.6 (Aug) | 28.3 | 19.0 |
| Nom exports yoy | 9.5 (Jul) | 4.8 | 20.8 |
| Retail sales yoy | n.a. | n.a. | n.a. |
| Inflation rate yoy | 31.6 (Sep) | 30.3 | 29.8 |
| CB reference rate | 18.8 (24th Oct) | 16.8 | 14.8 |
| Loans (priv sector, yoy, eop) | 37.0 (Jun) | 37.0 | 39.1 |
| Deposits (priv sector, yoy, eop) | 43.3 (Jun) | 43.3 | 40.6 |

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

**Industrial production and inflation**




Source: Ministry of Planning, CAPMAS

# Hungary

Sandor Jobbagy

## Real Economy

GDP growth slowed to 3.2% yoy in 2Q17, following a 4.2% (upwardly revised) result in the first quarter of the year. The growth was below expectations, despite the ongoing surge of investments. In addition to EU-funded projects, investment dynamics are becoming more broad-based. While private investments are still weaker, investments in construction, machinery and equipment rose in 2Q17. On the production side, the primary contributors to economic growth were market services. Growth in the industrial and agricultural sectors fell behind the performance of the first three months of the year. We would note that the automotive industry recorded a relatively weaker performance, while all sectors accounting for a more significant weight within the processing industry showed growth. The dynamic rise of sentiment indicators continued in 2Q17, suggesting average annual growth rate above that seen in 2Q17. Fiscal policy also provided more support to growth than in 2016.

Headline CPI was 2.5% in September, close to the average level of 1H17. At the same time, core inflation continued to move higher (2.9%), approaching the NBH's headline target. Domestic demand also appears to be getting stronger, primarily due to higher wages. Inflation is expected to continue to fluctuate in a range of 2-3% over the rest of the year. Industrial production reported a strong performance in August (6.8% yoy). External and internal balances remained strong amid volatile monthly export performances.

## Financial Markets

The NBH left the policy rate unchanged (0.90%) both in September and October, while cutting the O/N depo rate to -0.15% at the September meeting. The official statement highlighted downward risks in inflation (despite rising wages and higher core inflation) and the forint's earlier appreciation. The end-Q4 target for the 3M depo was cut to HUF 75Bn and no further changes are planned for 2018. The market adjustment is ongoing; short-dated T-bill rates are in negative territory and money market rates are close to or below zero. The long end of the yield curve also showed some downward shift. The forint returned to near the EUR 1/HUF 310 level.

## Banking Sector

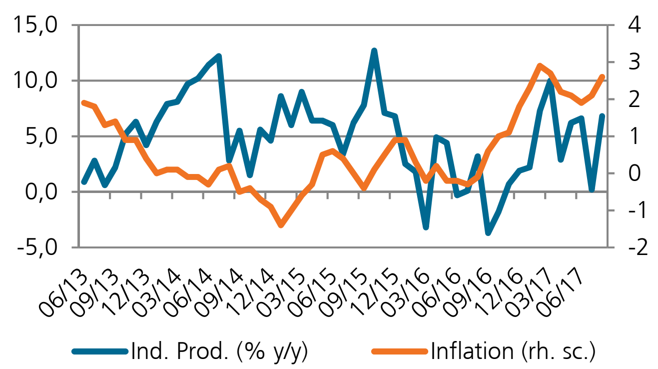
Loan stocks to the private sector showed persistent rises from May to August, with the yoy dynamics approaching 4%. Lending continued to households, and also revived in the corporate sector. Deposit volumes have continued to increase, despite the low interest rates. Real economic development lent support to the demand side of the loan market; credit conditions continued to ease. Household demand for housing and personal loans remained relatively strong. The quality of the banking sector's entire loan portfolio continued to improve, with NPLs below 7% at the end of 1H17.

**Latest economic indicators**

| % | Last value | 2Q17 | 1Q17 |
|---|---|---|---|
| Ind production yoy | 6.8 (Aug) | 5.2 | 6.5 |
| Nom exports yoy | 10.0 (Aug) | 7.5 | 12.8 |
| ESI (index) | 121.9 (Sep) | 118.6 | 115.7 |
| Retail sales yoy | 4.6 (Aug) | 4.3 | 3.3 |
| Inflation rate yoy | 2.5 (Sep) | 2.1 | 2.6 |
| CB reference rate | 0.9 (24th Oct) | 0.9 | 0.9 |
| Loans (priv sector, yoy, eop) | 4.0 (Aug) | 2.3 | 0.1 |
| Deposits (priv sector, yoy, eop) | 11.5 (Aug) | 11.3 | 9.6 |

Source: CSO, NBH, Bloomberg

**Industrial production and inflation**




Source: CSO

## Romania

### Real Economy

Sebastian Maneran

The role that fiscal policies play in the Romanian economy is a key focus for the mainstream media as of late. Specifically, the strength of the fiscal stimulus, executed via wage and pension hikes and lower taxes, raises concerns that assumed obligations in the state budget will leave gaps that will need to be filled. In order to close those gaps, the economic rhetoric regarding the public agenda is focusing on different forms of tax hikes.

Not only is the market focused on the validity of the 3% budget deficit target this year, but whether inflation will remain in check as well. September inflation was 1.77% yoy (vs 1.15% yoy in the previous month) mainly on the back of higher excise taxes, slight depreciation of the EUR/RON FX rate, and increasing energy costs in international markets. Retail sales are growing at a double-digit rate (+12.6% yoy in August), as entitlement policies and public pensions and wage increases reverberate into the real economy.

### Financial Markets

Given that external liquidity conditions should remain abundantly available into the end of 2017, and based on carefully managed expectations that interest rates would not move higher, the local central bank looked likely to remain quiet for most of the year. However, once the domestic focus switched consistently to tax increases, based on an inflation rate rate recorded in September not seen since late 2013, in order to keep inflation expectations anchored, the central bank was forced to act. The policy rate corridor was narrowed to 125 bps around the 1.75% policy rate (from 150 bps). The central bank's reaction, and rising inflation expectations, have led the market to start pricing in further policy tightning and even interest rate hikes as early as 2018. Given the conservative approach of monetary policy in Romania, and the results achieved so far, it is unlikely there will be interest rate hikes in 2018, in our view.

The yield curve has shifted higher on the back of the above-mentioned inflation expectations, and the EUR/RON fx spot rate has come down slightly, with the RON being supported by higher interest rates.

### Banking Sector

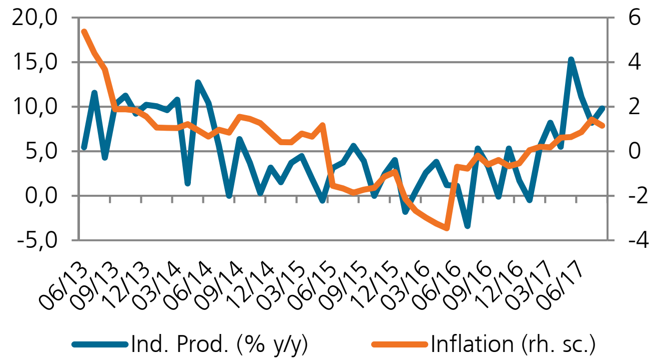
Wage increases in the public sector have been supporting new domestic deposits, which reached a new record (new deposits at RON 269M) at the end of August 2017 while mortgage loans pushed total new loans to a record at the end of August as well, of RON 119M. Hence, the banking industry stood out again as local credit markets showed signs of good health (low financing costs, a downward trending NPL rate, etc). However, upward trending sovereign financing costs and the push to digital are challenges for the Romanian banking sector that are compounded due to an increase in regulations and fiscal policy uncertainty.

**Latest economic indicators**

| % | Last value | 2Q17 | 1Q17 |
|---|---|---|---|
| Ind production yoy | 9.8 (Aug) | 10.6 | 4.4 |
| Nom exports yoy | 10.7 (Aug) | 7.8 | 10.0 |
| ESI (index) | 104.9 (Sep) | 105.4 | 105.4 |
| Retail sales yoy | 12.6 (Aug) | 8.3 | 7.2 |
| Inflation rate yoy | 1.8 (Sep) | 0.7 | 0.1 |
| CB reference rate | 1.8 (24th Oct) | 1.8 | 1.8 |
| Loans (priv sector, yoy, eop) | 6.4 (Aug) | 3.8 | 2.7 |
| Deposits (priv sector, yoy, eop) | 11.6 (Aug) | 8.9 | 11.2 |

Source: National Statistical Institute, NBR

**Industrial production and inflation**




Source: NBR

## Russia

### Real Economy

Anna Mokina

According to the Ministry of Economic Development, GDP growth increased to 2.3% yoy in August compared to 1.8% yoy in July. The main drivers of the August growth acceleration were agriculture and industry. Industrial output growth accelerated by 0.4 pps, to 1.5% yoy in August, due to a recovery in manufacturing industries, but the rate slowed slightly, to 0.9%, in September. August statistics confirmed a positive trend in consumer demand in recent months. The main factor behind has been the growth in real wages.

In August, consumer prices rose by 3.3% yoy and monthly deflation reached a historical record of 0.5%. Inflation for non-food goods is slowing down and the growth of prices for services has stabilised at about 4%. The growth of prices for food products also appears to be decreasing due to seasonal factors. In September, annual inflation slowed to 3% (the lowest figure since the early 1990s) and consumer prices fell by 0.1% mom (vs -0.5% mom in August). Core inflation, taking into account temporary volatile factors, amounted to 2.8%.

### Financial Markets

The Central Bank of Russia lowered its main policy rate both in September (by 50 pb) and in October (by a less aggressive 25 pb). The official rate now stands at 8.25%. Strong deflation was the key factor behind such moves by the CBR which in its communiqué as of 27th October left open the option of further rate reduction. We expect the CBR will cut further interest rates at its forthcoming policy meetings.

Tough rhetoric from the FOMC meeting and news about the beginning of normalisation of the US interest rates contributed to a significant weakening of the dollar against global currencies. The events in Catalonia however added at the end to some weakening of the euro. In the last 3 months, the RUB strengthened slightly, by ~2.9% against the USD, due to global trends. A rise in the oil price and local fx selling supported the ruble, enabling it to stay below RUB 58/USD 1.

### Banking Sector

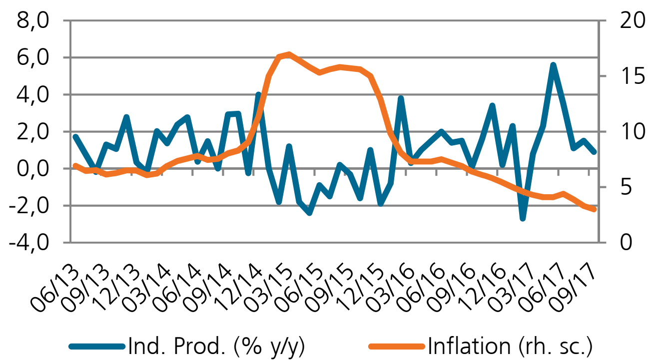
Lending to the private sector decreased by 1.3% in July, mostly due to a decrease in loans denominated in foreign currency (-16.7%), while loans in local currency grew by 4.8%. Loans to households in local currency increased by 7.6%, with weaker growth of 3.4% seen in the corporate sector. The volume of deposits from the private sector grew by 3.6% yoy, which demostrates the continuing saving pattern of the population and business. Deposits grew as well in local currency, by 11.5%, but decreased by 10.8% in foreign currency. The deposits growth rates were almost of equal size in local currency for households (+11.7%) and corporates (+11.1%).

**Latest economic indicators**

| % | Last value | 2Q17 | 1Q17 |
|---|---|---|---|
| Ind production yoy | 0.9 (Sep) | 3.8 | 0.1 |
| Nom exports yoy | 10.2 (Jul) | 23.5 | 36.9 |
| Retail sales yoy | 1.9 (Aug) | 1.0 | -1.6 |
| Inflation rate yoy | 3.0 (Sep) | 4.2 | 4.6 |
| CB reference rate | 8.25 (27th Oct) | 9.0 | 9.8 |
| Loans (priv sector, yoy, eop) | -1.3 (Jul) | 0.1 | -3.1 |
| Deposits (priv sector, yoy, eop) | 3.6 (Jul) | 4.8 | 3.4 |

Source: State Statistics Federal Service, Central Bank of Russia

**Industrial production and inflation**




Source: State Statistics Federal Service

# Serbia

## Real Economy

Marija Savi

Following weak weather-affected growth of 1.2% yoy in the first half of the year, recent indicators suggest an acceleration in economic activity in 2H17. Industrial production has been growing steadily (4.2% yoy growth in July and 7.3% yoy in August), exports finally are showing faster growth than imports (14.7% yoy vs 12.9% yoy in August), and retail sales edged up after a weak start of the quarter.

Inflation grew to 3.2% in September 2017, after falling to 2.5% in August, due to a high base effect. When compared to the previous month, consumer prices increased marginally by 0.1%, mainly due to seasonal price hikes for fresh vegetables and firewood. Core inflation, which excludes volatile items including energy, food, alcohol and tobacco, remained low, at 1.5%, confirming low inflationary pressures. The central bank expects inflation to remain within the target tolerance band of 3.0%±1.5 pp in the period ahead. Inflation growth will be slowed by the high base from the prices of petroleum products and, as of early 2018, by the dropout from the yoy calculation of this year's one-off price hikes for certain products and services.

## Financial Markets

In October 2017, the NBS cut the key policy rate by 0.25 bps for the second month in a row to a new historical low of 3.5%. Monetary policy easing was supported by persistently low inflationary pressures, weaker-than-expected GDP growth in 1H17, and a relatively strong dinar. By lowering the key policy rate, the National Bank of Serbia is providing additional support to credit activity and economic growth.

The dinar has appreciated against the euro by 3.7% since the beginning of the year while the NBS has sold EUR 345M and bought EUR 1,125M on the fx market in order to mitigate excessive daily volatility of the exchange rate. The appreciation is a result of improved export performance, higher remittances, strong inflow of FDIs, and greater investor interest in Serbian local currency bonds backed by JP Morgan's trading list as well as stronger fx-linked bank assets.

## Banking Sector

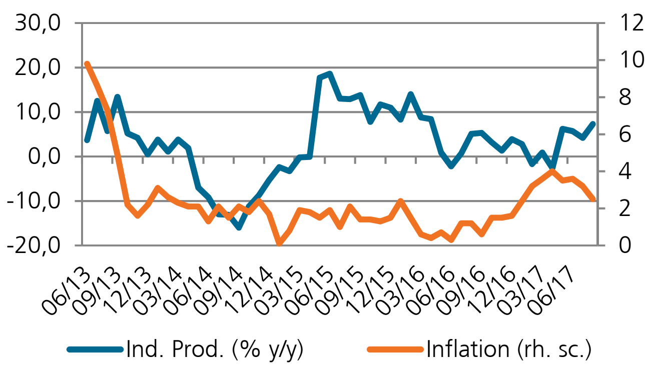
Loans to the private sector increased by 2.7% yoy in August 2017, driven by strong growth in lending to households (9.8% yoy) and a further recovery in corporate loans (-2.4% yoy). The yoy drop in corporate loans was driven by the NPL write-off effect. Owing to considerable NBS monetary policy easing, low global money market rates, and increased interbank competition, the RSD lending rates almost halved in comparison to 2013, when the fall in interest rates was initiated, while EUR and EUR-indexed lending rates are more than two times lower.

**Latest economic indicators**

| % | Last value | 2Q17 | 1Q17 |
|---|---|---|---|
| Ind production yoy | 7.3 (Aug) | 3.1 | 0.7 |
| Nom exports yoy | 14.7 (Aug) | 13.2 | 12.8 |
| Retail sales yoy | 4.4 (Aug) | 3.5 | 3.6 |
| Inflation rate yoy | 3.2 (Sep) | 3.7 | 3.1 |
| CB reference rate, eop | 3.5 (24th Oct) | 4.0 | 4.0 |
| Loans (priv sector, yoy, eop) | 2.7 (Aug) | 2.2 | 4.5 |
| Deposits (priv sector, yoy, eop) | 6.6 (Aug) | 7.4 | 12.0 |

Source: Statistical Office, National Bank of Serbia

**Industrial production and inflation**




Source: Statistical Office, National Bank of Serbia

# Slovakia

## Real Economy

Andrej Arady

Domestic activity remained solid in all sectors except automotive as 3Q unfolded. Growth in construction in the first two months of 3Q bounced to 8.7% yoy from -0.1% yoy in 2Q based on a booming housing market. Retail sales meanwhile increased by nearly 6% yoy in the July-August period. Consumption is being supported by ongoing progress on the labour market, with the registered unemployment rate down to a new all-time low of 6.4% in September. A tightening labour market already began to translate into an acceleration in wage growth of close to 5% yoy in 2Q. In the first two months of 3Q, industrial production posted 4.4% yoy growth, up from 1.7% yoy in 2Q, of which only 1.3% related to car production. The key driver of growth is now metals production. Nevertheless, a slowdown in the automotive sector is most likely only temporary, caused by preparation for the new generation of car models.

The outlook remains encouraging. Economic sentiment calculated as a three-month moving average in September picked up considerably. Over the past three months, confidence has improved in all reported sectors. The gain was especially strong for households, where confidence increased to the highest level in a decade. Taking into consideration the latest available data, our full-year forecast of 3.4% yoy growth of GDP in 2017 appears to be realistic.

Price-wise, domestic inflation picked up further, to 1.6% yoy in September, a tenth above the Euro area average. The most recent growth was driven primarily by the food component. We continue to expect that consumer price inflation will pick up further in the next year, moving close to 2%. Producer prices rose even more significantly, moving from 0.7% yoy in July to 2.1% in August. However, property prices have shown the highest rise, at around 7% yoy in 2Q.

## Financial Markets

Spreads on Slovak government bonds vs German bunds remained stable over the past weeks at around 40bps. Along with the normalisation of monetary policy, we continue to expect not only rising rates on government bonds, but also widening spreads vs German bunds, back to above 60 bps.

## Banking Sector

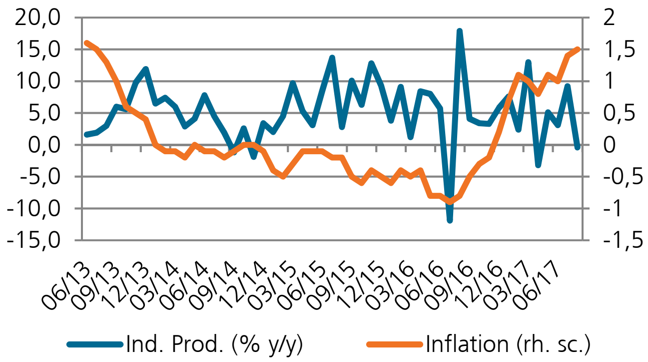
With regard to loan volume, the Slovak banking sector continues to grow at an encouraging double-digit year-on-year pace. However, growth has slipped somewhat from the recent peak in 2Q. In August, loan growth rose to 11.3% yoy from 10.9% yoy in the previous month, but was still down from the recent peak of 12.4% in May. The deceleration from the peak is based on performance in both household and corporate sectors. New regulatory measures tightening the credit conditions should gradually further moderate growth of household debt in the future. Nevertheless, a booming labour market should continue to support high growth.

**Latest economic indicators**

| % | Last value | 2Q17 | 1Q17 |
|---|---|---|---|
| Ind production, wda yoy | -0.4 (Aug) | 1.7 | 7.7 |
| Nom exports, yoy | 5.9 (Aug) | 2.1 | 11.4 |
| ESI (index) | 104.8 (Sep) | 102.3 | 104.6 |
| Retail sales, yoy | 6.8 (Aug) | 7.5 | 5.5 |
| Inflation rate, yoy | 1.6 (Sep) | 1.0 | 0.9 |
| ECB refi rate | 0.0 (24th Oct) | 0.0 | 0.0 |
| Loans (priv sector, yoy, eop) | 11.3 (Aug) | 12.0 | 11.4 |
| Deposits (priv sector, yoy, eop) | 4.7 (Aug) | 4.0 | 4.7 |

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

**Industrial production and inflation**




Source: Statistical Office of Slovak Republic

# Slovenia

## Real Economy

Ivana Jovi

High frequency data for 3Q17 indicate continued positive trends in the Slovenian economy, as industrial production in the July-August period increased by 7.4% yoy, supported by 12.5% higher merchandise exports and 8.5% yoy higher retail trade volume turnover. The value of new construction showed 8.7% and 7.6% yoy growth in July and August, respectively, thus posting a 15.5% yoy increase over the first eight months of this year, but it is still struggling at a 40% lower level than in 2010. With regard to the labour market, employment growth remains high (+3.6% yoy in July) and unemployment decreased by 14.9% yoy, to 80,990, in September. In this context, average net earnings in the first seven months of 2017 increased by 2.3% yoy in nominal terms and by 0.8% yoy in real terms. On the external front, four-quarter current account surplus reached 5.4% of GDP in 2Q17, reflecting a higher surplus in merchandise and services and a slightly narrowing deficit in the primary and secondary income accounts. Following sharp increase at the beginning of the year, inflation pressures moderated and the rate stabilised at 1.4% in September while 12-month average price growth was 1.2%.

## Financial Markets

Ana Lokin

3M Euribor remained unchanged at -0.33% in the August-September period, while the average 10Y government bond yield marked a downward path, decreasing by 13 bps mom in August and by an additional 5 bps mom in September, remaining a tad above 1%. In line with global trends, 5Y CDS remained on a positive trend, falling by 5 bps on average in August and by 7 bps mom in September, to 61 bps. It is now close to levels last seen in 4Q10.

## Banking Sector

Loan growth rate accelerated to +5.5 yoy in August (July +4.2% yoy) mainly due to a notably faster rise in corporate loans. Growth of loans to non-financial corporations rose to +4.2% yoy (July: +2.0% yoy), mostly owing to base effects (corporate loans started to rise mom from October of last year), whereas loans to households, supported by rising employment and strong consumer confidence, increased by 6.8% yoy (July: +6.6% yoy). The breakdown of household loans by purpose shows that the rise in consumer loans remained robust at 12.8% yoy (July: +12.3% yoy). Housing loans recorded a 4.8% yoy increase (July: +4.7% yoy), while other loans rose to 6.1% yoy (July: +5.5% yoy).

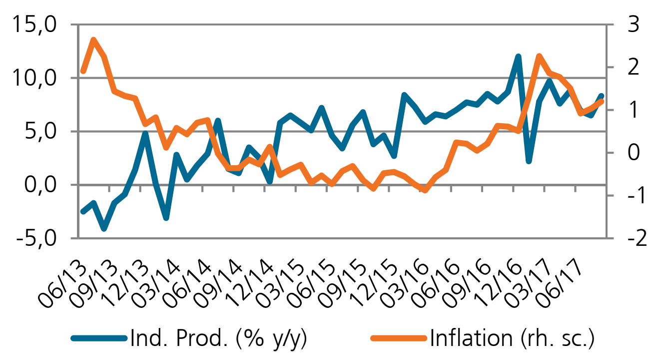
The rise in deposits strengthened to +6.3% yoy in August (July: +5.6% yoy), mostly due to a sharper increase in corporate deposits (+9.4% vs +6.0% yoy in July), particularly term deposits, which jumped by 20.2% yoy (sight: +5.8% yoy). The pace of growth in household deposits continued to fluctuate around 5% (August: +5.3% yoy), whereas term deposits, pressured by low and continuously declining interest rates (0.2% in August, -10 bps yoy), resumed their negative trend (-15.7% yoy in August, but sight deposits marked a steep rise (+18.0% yoy).

**Latest economic indicators**

| % | Last value | 2Q17 | 1Q17 |
|---|---|---|---|
| Ind production, wda yoy | 8.3 (Aug) | 7.8 | 6.6 |
| Nom exports yoy | 12.5 (Jul) | 10.7 | 12.4 |
| ESI (index) | 114.1 (Sep) | 112.9 | 112.9 |
| Consumer confidence Indic. | -4.0 (Aug) | -4.7 | -6.0 |
| Inflation rate yoy | 1.4 (Sep) | 1.4 | 1.8 |
| ECB refi rate | 0.0 (24th Oct) | 0.0 | 0.0 |
| Loans (priv sector, yoy, eop) | 5.5 (Aug) | 3.4 | 1.6 |
| Deposits (priv sector, yoy, eop) | 6.3 (Aug) | 6.1 | 7.2 |

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

**Industrial production and inflation**




Source: Statistical Office of the Republic of Slovenia

# Ukraine

## Real Economy

Giancarlo Frigoli

The recently released data showing the GDP breakdown in Q2 reflected that capital investment accelerated to 23.7% yoy and house purchases increased by 6.9% yoy (from 2.8% yoy in 1Q). At the same time, foreign trade negatively affected GDP in 2Q. Suspension of trade with the government non-controlled area has caused exports to drop more significantly (-2.1% yoy in 2Q from -0.4% yoy in 1Q). Natural gas supplies as well as higher domestic demand contributed to an acceleration in import growth (to 4.6% yoy in 2Q from +2.9% yoy in 1Q). Gross value added (GVA) increased for construction (to 28.8% yoy) and trade (to 3.8 yoy). In the production sector, despite the difficulties in the metals and mining industry and the energy sector, output of other industries increased markedly, especially for the machinery industry. Growth in manufacturing accelerated to 4.2% yoy. 3Q data releases provided a picture similar to that seen in 2Q: domestic demand remained strong (in particular construction and retail trade), industrial production posted a new decline while net trade negatively affected growth, following strong demand for imported goods (+9% from July to August).

## Financial Markets

In recent months, primarily reflecting faster-than-expected growth in raw food and tobacco prices following the unfavourable weather conditions in spring 2017, inflation (16.4% yoy in September) came in above the NBU's forecasts. However, inflation is expected to trend downwards in the final months of 2017, primarily reflecting last year's high base. Even excluding tariff hikes, annual inflation is now forecast by the Ukrainian authorities to end 2017 at around 12%, well above the 8+/-2% target range announced by the CB in its July Inflation Report. The need to return inflation to the target prompted the NBU to hike its main policy rate by 100 bp (to 13.50%) at its end October meeting. The hryvnia has shown some weakness in recent weeks, though the rate has been little changed from the end-2016 close, due to demand factors. The Monetary Authority has sold foreign currency to smooth fluctuations.

## Banking Sector

Davidia Zucchelli

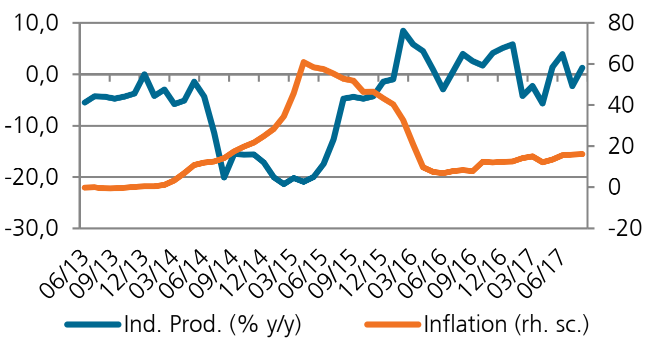
Banks recorded a decrease in lending again in August, interrupting the slight improvements highlighted in the previous months. Nominal loans decreased by 3.6% yoy in August (from -1.6% in June) in both the corporate (-4.1% yoy) and household (-1.5%) sectors. Net of the exchange rate effect, loans recorded a decline of 5.7%. In contrast, deposits experienced a nominal increase (5.9% yoy in August, but +3.4% net of the exchange rate) supported by a slight improvement in the unemployment rate, particularly in local currency (+12% yoy). NPLs remained the Sword of Damocles. The NPL ratio increased to 57.5% (as of June). Coverage is significant (77.3%), but the "NPL net of provisions to capital" ratio was 96.3% at June. ROA and ROE referring to the first eight months of 2017 were positive (0.4% and 3.5%, respectively), but new significant provisions are expected in December, with a likely negative effect on profitability. Because of the crisis, many banks have been closed or have merged: licenced banks declined from 96 in December 2016 to 88 in August, but banks with 100% foreign capital remained stable at 17. According to the CB, by the end of 2017, the number of banks will likely decline further, to 75-80.

**Latest economic indicators**

| | Last value | 2Q17 | 1Q17 |
|---|---|---|---|
| Ind production yoy | -0.4 (Sept) | -0.1 | -0.2 |
| Nom exports yoy | 21.1 (Aug) | 25.6 | 38.4 |
| PMI manufacturing | n.a. | n.a. | n.a. |
| Retail sales | 8.2 (Sep) | 8.6 | 3.3 |
| Inflation rate yoy | 16.4 (Sep) | 13.8 | 14.0 |
| CB reference rate | 13.5 (26th Oct) | 12.5 | 14.0 |
| Loans (priv sector, yoy, eop) | -3.6 (Aug) | -1.4 | -5.0 |
| Deposits (priv sector, yoy, eop) | 5.9 (Aug) | 7.8 | 5.6 |

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

**Industrial production and inflation**




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] | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | 2Q17 | 1Q17 | 2016 | Last | mth | 2Q17 | Last | mth | 2Q17 | Last | mth | 2Q17 | 2016 | 2Q17 | 1Q17 | 2016 | 2Q17 | 1Q17 |
| CEE | | | | | | | | | | | | | | | | | | |
| Czech Rep. | 4.7 | 3.0 | 2.4 | 5.8 | Aug | 6.8 | 4.8 | Aug | 4.6 | 2.7 | Sep | 2.2 | 0.7 | | | | | |
| Hungary | 3.2 | 4.2 | 2.0 | 6.8 | Aug | 5.2 | 10.0 | Aug | 7.5 | 2.5 | Sep | 2.1 | 0.4 | | 14 | -5938 | 1750 | 953 |
| Slovakia | 3.3 | 3.1 | 3.3 | -0.4 | Aug | 1.7 | 5.9 | Aug | 2.1 | 1.6 | Sep | 1.0 | -0.5 | n.s. | n.s. | n.s. | | 190 |
| Slovenia | 4.4 | 5.1 | 3.1 | 8.3 | Aug | 7.8 | 12.5 | Jul | 10.7 | 1.4 | Sep | 1.4 | -0.1 | n.s. | n.s. | n.s. | 768 | 571 |
| SEE | | | | | | | | | | | | | | | | | | |
| Albania | 4.1 | 3.9 | 3.5 | n.a. | n.a. | n.a. | 12.1 | Aug | 10.5 | 1.6 | Aug | 2.0 | 1.3 | -76 | 9 | 47 | -231 | -179 |
| Bosnia H. | 1.7 | 2.8 | 3.1 | 7.1 | Aug | 2.1 | 20.4 | Aug | 13.7 | 1.0 | Aug | 1.2 | -1.1 | 115 | -148 | 473 | -242 | -165 |
| Croatia | 2.8 | 2.5 | 3.0 | 3.2 | Aug | 2.5 | 11.3 | Jul | 7.6 | 1.4 | Sep | 1.1 | -1.1 | -2044 | 2558 | -193 | 144 | -1542 |
| Romania | 5.9 | 5.6 | 4.8 | 9.8 | Aug | 10.6 | 10.7 | Aug | 7.8 | 1.8 | Sep | 0.7 | -1.5 | | 699 | -350 | | -3248 |
| Serbia | 1.3 | 1.0 | 2.8 | 7.3 | Aug | 3.1 | 14.7 | Aug | 13.2 | 3.2 | Sep | 3.7 | 1.1 | -183 | -549 | -52 | -287 | -624 |
| CIS MENA | | | | | | | | | | | | | | | | | | |
| Russia | 2.5 | 0.5 | -0.2 | 0.9 | Sep | 3.8 | 10.2 | Jul | 23.5 | 3.0 | Sep | 4.2 | 7.1 | 12910 | 12732 | -1356 | | 23283 |
| Ukraine | 2.3 | 2.5 | 2.3 | -0.4 | Sep | -0.1 | 21.1 | Aug | 25.6 | 16.4 | Sep | 13.8 | 14.9 | 2344 | -440 | -466 | -394 | -866 |
| Egypt | 4.9 | 4.3 | 3.8 | 23.6 | Aug | 28.3 | 9.5 | Jul | 4.8 | 31.6 | Sep | 30.3 | 13.7 | 2779 | 4261 | 7820 | -2396 | -3529 |
| *m.i. E.A.* | *2.1* | *1.7* | *1.8* | *3.8* | *Aug* | *2.7* | *6.8* | *Aug* | *5.4* | *1.5* | *Sep* | *1.5* | *0.2* | | | | | |

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

## Markets and Ratings

| | S/T rates[1] | | L/T rates[2] | | Foreign exchanges[3] | | | Stock markets | | CDS spread (bp) | | Rating |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | 18/10 | chg bp 3M | 18/10 | chg bp 3M | 18/10 | 3M chg% | 1Y chg% | 3M chg% | 1Y chg% | 18/10 | 18/07 | S&P |
| CEE | | | | | | Vs Euro | | | | | | |
| Czech Rep. | 0.5 | 0.2 | 1.5 | 0.5 | 25.7 | -1.4 | -4.8 | 4.5 | 15.1 | 36.5 | 37.5 | AA- |
| Hungary | 0.0 | -0.1 | 2.6 | -0.5 | 308.2 | 0.5 | 0.5 | 8.9 | 34.7 | 88.0 | 101.0 | BBB- |
| Slovakia | -0.3 | 0.0 | 0.8 | -0.2 | Euro | Euro | Euro | -6.2 | -1.3 | 38.8 | 38.8 | A+ |
| Slovenia | -0.3 | 0.0 | 0.9 | -0.4 | Euro | Euro | Euro | 1.2 | 11.3 | 62.0 | 72.3 | A+ |
| SEE | | | | | | | | | | | | |
| Albania | 1.2 | 0.0 | n.a. | n.a. | 133.6 | 0.8 | -2.3 | n.a. | n.a. | n.a. | n.a. | |
| Bosnia H. | n.a. | n.a. | n.a. | n.a. | 1.96 | Board | Board | n.a. | n.a. | n.a. | n.a. | |
| Croatia | 0.6 | 0.0 | 2.5 | -0.3 | 7.5 | 1.3 | 0.0 | 0.6 | -6.5 | 104.6 | 154.4 | BB |
| Romania | 1.6 | 1.0 | 4.3 | 0.4 | 4.6 | 0.6 | 1.7 | -1.9 | 17.7 | 90.6 | 94.5 | BBB- |
| Serbia | 3.5 | -0.5 | n.a. | n.a. | 119.0 | -1.3 | -3.4 | 3.0 | 19.1 | 129.3 | 149.0 | BB- |
| CIS MENA | | | | | | Vs USD | | | | | | |
| Russia | 8.6 | -0.6 | 7.5 | -0.3 | 57.3 | -2.9 | -9.2 | 9.6 | 6.9 | 122.5 | 153.8 | BB+ |
| Ukraine | 16.1 | 0.0 | 9.7 | 0.0 | 26.4 | 2.0 | 3.0 | -18.2 | -8.9 | 588.5 | 611.1 | B- |
| Egypt | 18.8 | -1.5 | 15.6 | -3.1 | 17.6 | -1.7 | 98.7 | -11.8 | 38.6 | 345.8 | 393.6 | B- |
| *m.i.A.E.* | *-0.3* | *0.0* | *0.4* | *-0.1* | *1.2* | *1.7* | *7.4* | *2.4* | *13.2* | *5.1* | *6.0* | |

Source: Datastream, Reuters;[1] The data for Albania refers to january, for Egypt refers to september, for Czech Republic refers to september; [2]For Ukraine, the long-term rate refers to a government issue in dollars; [3] The (-) 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 | 2016 | Last | mth | 2016 | Last | mth | 2016 | Last | Mth | 2016 | Last | mth | 2016 | S[4] | Last | mth | 2016 | S[4] | Last | mth | 2016 |
| CEE | | | | | | | | | | | | | | | | | | | | | | | |
| Czech Rep. | 7.1 | Aug | 6.7 | 4.1 | Aug | 4.8 | 94.3 | Jun | 38.4 | 9.4 | Aug | 5.8 | 2.04 | Aug | 1.86 | C | 0.32 | Aug | 0.91 | H | 76.5 | Aug | 76.6 |
| Hungary | 4.0 | Aug | -1.9 | 6.6 | Jun | 9.0 | 7.4 | Aug | -7.0 | 11.5 | Aug | 6.3 | 2.61 | Aug | 3.12 | C | 0.3 | Aug | 0.54 | H | 83.8 | Aug | 83.8 |
| Slovakia | 11.3 | Aug | 10.3 | 4.2 | Aug | 4.7 | -3.3 | Aug | 0.8 | 4.7 | Aug | 4.6 | 1.84 | Jul | 1.97 | C[2] | 0.23 | Jul | 0.41 | H[2] | 98.5 | Aug | 94.9 |
| Slovenia | 5.5 | Aug | -2.7 | 7.3 | Jul | 8.5 | -12.9 | Aug | -17.9 | 6.3 | Aug | 7.2 | 2.38 | Aug | 2.81 | C[2] | 0.11 | Aug | 0.23 | H[2] | 80.7 | Aug | 81.0 |
| SEE | | | | | | | | | | | | | | | | | | | | | | | |
| Albania | -0.2 | Aug | 0.2 | 15.3 | Jul | 18.3 | -15.7 | Aug | -13.2 | 0.0 | Aug | 2.7 | 9.24 | Aug | 7.01 | PS | 0.56 | Aug | 0.78 | PS | 53.6 | Aug | 52.3 |
| Bosnia H. | 7.2 | Aug | 3.4 | 11.1 | Jun | 11.8 | 15.2 | Aug | -5.3 | 8.3 | Aug | 7.4 | 3.73 | Aug | 4.62 | C | 0.42 | Aug | 0.55 | H | 110.3 | Aug | 110.1 |
| Croatia | -0.2 | Aug | -4.3 | 13.2 | Jun | 13.8 | -22.0 | Aug | -26.6 | 2.2 | Aug | 2.8 | 7.07 | Aug | 7.03 | PS | 0.68 | Aug | 0.85 | PS | 79.2 | Aug | 80.5 |
| Romania | 6.4 | Aug | 0.6 | 8.3 | Jun | 9.6 | -14.7 | Aug | -21.8 | 11.6 | Aug | 8.5 | 5.39 | Aug | 4.93 | PS | 0.51 | Aug | 0.61 | PS | 83.0 | Aug | 83.0 |
| Serbia | 2.7 | Aug | 2.4 | 15.2 | Jul | 17.0 | 6.6 | Aug | -9.1 | 6.6 | Aug | 11.5 | 9.1 | Aug | 8.45 | PS | 2.98 | Aug | 2.94 | PS | 104.7 | Aug | 102.3 |
| CIS MENA | | | | | | | | | | | | | | | | | | | | | | | |
| Russia | -1.3 | Jul | -4.2 | 9.8 | Aug | 9.4 | -12.5 | Oct | na | 3.6 | Jul | -3.9 | 10.44 | Jul | 11.83 | C | 6.07 | Jul | 6.5 | H | 105.5 | Jul | 107.7 |
| Ukraine | -3.6 | Aug | 2.0 | 57.7 | Jun | 30.5 | -21.6 | Jun | -8.0 | 5.9 | Aug | 9.1 | 15.43 | Aug | 17.25 | PS | 8.65 | Aug | 9.99 | PS | 128.7 | Aug | 136.8 |
| Egypt | 37.0 | Jun | 42.8 | 5.7 | Mar | 5.8 | 123.6 | Jun | 256.6 | 43.3 | Jun | 41.4 | 18.5 | Jul | 16.3 | C | 12.4 | Jul | 10.3 | H | 37.5 | Jun | 39.2 |
| *m.i. E. A.* | *1.5* | *Jul* | *0.9* | *n.a.* | *n.a.* | *n.a.* | *n.a.* | *n.a.* | *n.a.* | *1.6* | *Jul* | *3.3* | *1.2* | *May* | *1.4* | *C* | *0.4* | *May* | *0.4* | *H* | *82.2* | *Jul* | *81.8* |

Source: Central Banks, IMF, Moody's ;[1]monthly average; [2]lending rate on current account overdraft; on deposits up to 1 year
[4]Sector C=Corporates, H=Household, PS=Private Sector.

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