UniCredit Bank

Weekly

N . o . t . e . s

English translation by an external party

HIGHLIGHTS OF THE WEEK

11/2016

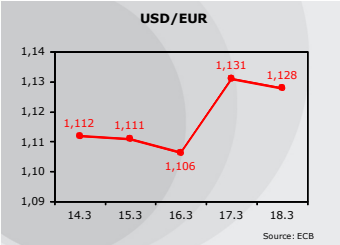
> Chart of the Week: Slovakia imports more chocolate than it exports; the balance got worse in the last 3 years in particular

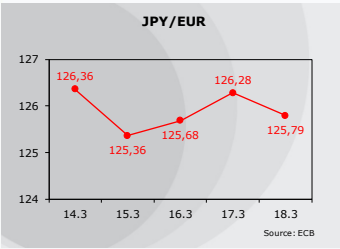
> Deflation moderated in February...

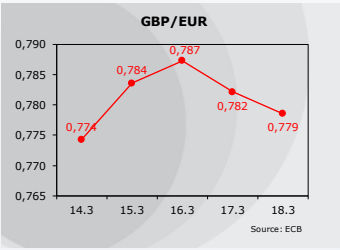
> ... prices in the eurozone resumed their yoy decline in February

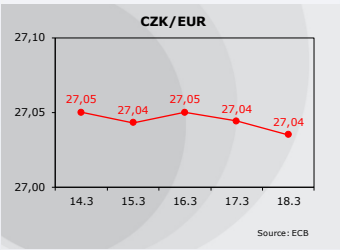
> Unemployment keeps falling, the one-digit level is within reach

WEEK ON THE MARKETS









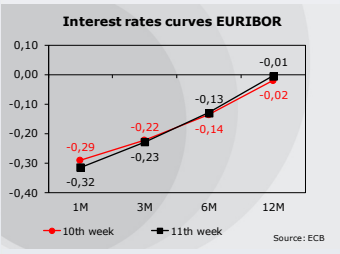
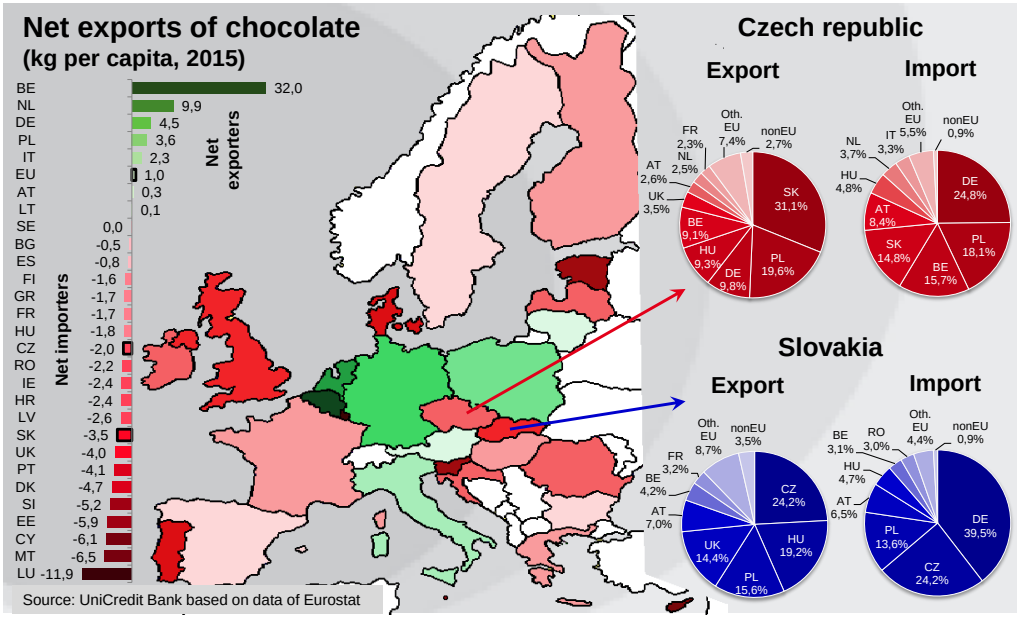


CHART OF THE WEEK



Source: UniCredit Bank based on data of Eurostat

Easter is approaching. In our territory, Easter symbols include Easter eggs as well as various chocolate imitations of Easter eggs. Therefore, the current *Chart of the Week* focuses on the statistics focusing on chocolate. According to data of the Statistical Office of the SR, an average Slovak consumes 5.1 kg of chocolate a year. Although its consumption is very slowly increasing, it is still only about half compared to the largest chocolate consumers in the world, which include Switzerland, Germany, and Great Britain. Chocolate consumption is mainly the privilege of developed countries – Europe accounts for around one half of the global chocolate consumption, and North America for another fourth. Therefore, it is no surprise that it is Europe and North America - USA, Germany, Switzerland, and Belgium are home to major chocolate producers. The main ingredient of chocolate - cocoa, however, comes primarily from Africa (around ¾ of global production), and African countries, led by Côte d'Ivoire and Ghana, are the largest world cocoa producers.

Although, in absolute terms, chocolate consumption in Slovakia is still lagging behind the global chocolate powers, spending of Slovak people on chocolate is not by far negligible compared to their income. According to the most recent available data by Eurostat (although somewhat older data from 2005), the Slovaks spend on chocolate 0.7% of their total expenses, ranking first in the EU, and they are followed by the Czech Republic and Latvia (0.5%). An average European spends on chocolate "only" 0.2% of his total expenses. Therefore, we can say that the Slovaks really like chocolate and they are willing to spend on it quite a large portion of their income. With increasing household income, we can see an increase in chocolate consumption as well as an increased popularity of foreign chocolates among the Slovaks. In the first

half of the last decade, Slovakia was a chocolate exporter only, it imports 3.5 kg more of chocolate per capita than it exports at present. The balance of foreign trade in chocolate started to get worse rapidly mainly after 2012 (when Slovakia imported and exported chocolate in an approximately identical volume). At the same time, export of chocolate from Slovakia is not dropping - just the opposite, it is rising slightly. The balance of foreign trade in chocolate deteriorated solely to the higher import of chocolate. A considerable increase in import of chocolate may be seen also in our Western neighbour – the Czech Republic. However, the Czech chocolate producers manage to increase export of chocolate as well, keeping the chocolate trade deficit in the Czech Republic relatively stable for several years, with the Czechs importing 2 kg more of chocolate a year than they export.

Both the Slovaks and Czechs import chocolate mainly from Germany, with both countries reporting also quite a portion of mutual imports, or chocolates from Poland. The Czechs are also quite fond of Belgian chocolate.

The top net chocolate exporter per capita from among the EU countries is clearly Belgium, exporting as much as 32 kg of chocolate per capita a year on a net basis. Relatively strong exports can be found also in the Netherlands, Germany, and Poland. It is these countries that are responsible for the EU exporting more chocolate than it imports on average – by 1 kg more per capita a year on average. At the same time, most EU countries are increasingly importing more chocolate than they export.

(lk)

ECONOMIC CALENDAR

Week	Indicator	Period	Market Consensus	UniCredit Bank Estimate	Reality
11.	Consumer prices (March 14)	February	-0.5% yoy	0.0% mom -0.5% yoy	0.1% mom -0.4% yoy
	Harmonised index of consumer prices (March 17)	February	-0.5% yoy	0.0% mom -0.5% yoy	0.1% mom -0.3% yoy
	Unemployment (March 15-20)	February	-	10.32%	10.09%
12.	Producer prices (March 24)	February	-	-3.9% yoy	-
13.	State budget (April 1)	March	-	-1 000 mil. EUR	-

Source: Bloomberg, Reuters, NBS, SOSR, UPSVaR, MinFin SR, UniCredit Bank Slovakia

ECONOMY

COSNUMER PRICES

Prices rising slightly in February, yoy deflation moderates

According to surveys of the Statistical Office of the SR, prices in Slovakia went up by 0.1% mom in February, with the dynamics of their yoy decline moderating from -0.6% to -0.4%. Deflation in Slovakia is relatively moderate, driven solely by supply-side factors. Such form of deflation is not harmful to the economy; just the opposite, it supports household consumption, when the falling energy and food prices increase the available resources of households for other expenses.

On a mom basis, prices in February were pulled higher mainly by the seasonal increase in the prices of food as well as the demand-pull inflation recovering really cautiously over the recent months. The yoy deflation was moderated also to the base effect in prices of fuels.

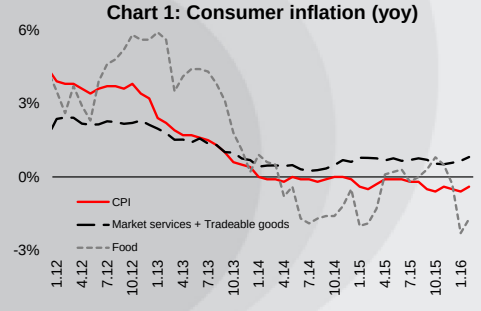
The demand-pull inflation measured by the index of prices of tradable goods (excl. fuels) and market services (excl. imputed rent) – calculation of UniCredit Bank is starting to show very carefully the first signs of recovery. It was confirmed also by February, when it increased by 0.1% mom, with the dynamics of its yoy growth accelerating for three months in a row from 0.7% to 0.8%. The demand-pull inflation accelerated in February mainly due to tradable goods, where the price growth accelerated from 0.1% to 0.4% yoy. The yoy growth of prices of market services did not change compared to January (remaining at 1.7%).

In February, prices of food rose by 0.3% mom, in particular due to the traditional seasonal increase in the prices of seasonal food - fruit and vegetables. However,

mainly in the case of vegetables, the seasonal hike in prices was slower than usual, with the dynamics of the yoy growth of food prices moderating from -2.3% to -1.7% compared to January.

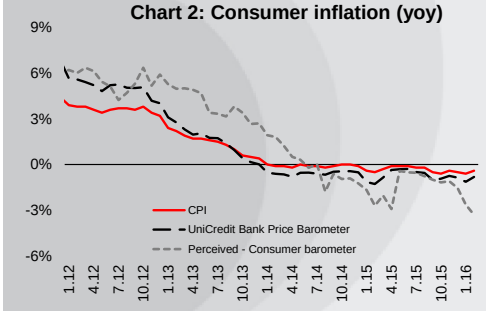
World market oil prices started to recover in February, with the average Brent oil prices in EUR rising by 2.7% mom. Due to the traditional time lag between the oil prices and prices of fuels in Slovakia, prices at Slovak petrol stations were still slightly falling in February – being lower by -1.9% on average compared to January. Due to lower last year's comparison basis, in the aftermath of the sharp decline in petrol and diesel prices in February, the dynamics of the yoy decline in prices moderated from about 13% to 10%. However, fuels were still reducing the overall yoy inflation by 0.2 pp.

Chart 1: Consumer inflation (yoy)



Source: SO SR, UniCredit Bank

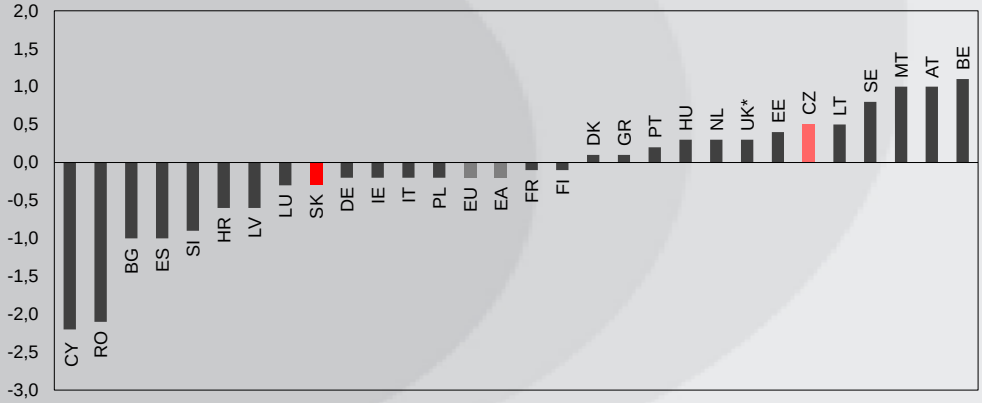
Chart 2: Consumer inflation (yoy)



Source: UniCredit Bank. SO SR

The UniCredit Bank Price Barometer (i.e. the perceived inflation measured through frequently bought goods and services) went up by 0.2% mom in February, with its decline moderating from -1.1% to -0.8% compared to the same period a year ago. Even despite a moderate deceleration of the yoy deflation in February (as well as deceleration of the yoy decline in frequently bought goods and services), the perception of price decline by consumers reached a new historical low of -3.3% yoy according to the consumer barometer of the Statistical Office (calculated from the balance of answers). On the contrary, inflation expectations have gone in the opposite direction. Reporting an all-time low in January, a moderate correction could be seen in February – however, consumers still expect a -1.5% price decline in the next 12 months (probably also owing to the reduced VAT rate on selected food).

Chart 3: Harmonised index of consumer prices (02/16, YoY)



*01/2016

Source: UniCredit Bank based on data of Eurostat

In the harmonised Eurostat methodology, prices in Slovakia grew by 0.1% mom in February, with the dynamics of their yoy decline moderating from -0.6% to -0.3%. On average, consumer prices increased by 0.2% mom on average in the eurozone countries, however, due to the base effect, inflation in the eurozone returned to slightly negative figures after four months, with the prices being lower by -0.2% on average compared to last year's February. Recovery of inflation in the eurozone (and Europe) is still prevented by cheap oil. Cheap oil was the main reason for price decline also in February, when prices of fuels were falling by as much as -10.7% yoy on average in the eurozone, reducing inflation of the eurozone by as much as a one half of a percentage point, and the decline in prices of heating oil accounted for

another two tenths of the inflation's reduction, with gas accounting for one tenth of the same.

Yoy decline in prices also in the eurozone

February saw a slight deceleration in the growth of core inflation (i.e. inflation adjusted for the change in food and energy prices), which is still subdued mainly by the secondary effects of cheap energy. Nevertheless, core inflation is safely reporting positive figures, ranging quite narrowly from 0.8% to 1.0% in recent months. A yoy decline in core prices is reported by a single eurozone country, namely Cyprus. On the contrary, the dynamics of the yoy growth of core prices in Slovakia accelerated slightly from 0.8% to 0.9% in February, reaching its peak in 2.5 years.

The number of eurozone countries with deflation has more than doubled in February – from 6 to 11 (although Greece got out from moderate deflation, however, a moderate yoy price decline was reported again by Germany, Ireland, Italy, France, Luxembourg, and Finland) - the fastest price decline was reported again by Cyprus (by as much as -2.2%), Spain (-1.0%), and Slovenia (-0.9%). Out of the 9 EU countries that are not yet members of the euro area, nearly one half of them (four) reported a yoy price decline, with the highest decline being reported by Romania (by as much as -2.1%) and Croatia (by -0.6%). On the contrary, the fastest price growth was reported by Belgium (1.1%), Austria (1.0%), and Malta (1.0%); as for the non-eurozone EU countries, by Sweden (by 0.8%).

OUTLOOK

There is still no stronger inflation driver and this situation should persist also for most of 2016. Low prices of oil and other energy commodities, besides the direct impact through prices of fuels and regulated energy prices, decelerate also the recovery of demand-pull inflation. Return of food prices to the positive is hindered also by tax alterations (reduction of VAT on selected food). However, the current moderate recovery of world market oil prices could slightly accelerate also the gradual wearing off of the effect of low oil prices. In the second half of the year, inflation should be getting close to zero again and we might finally (after three years) see a slightly positive inflation at the end of the year. (lk)

UNEMPLOYMENT

Unemployment is approaching 10%

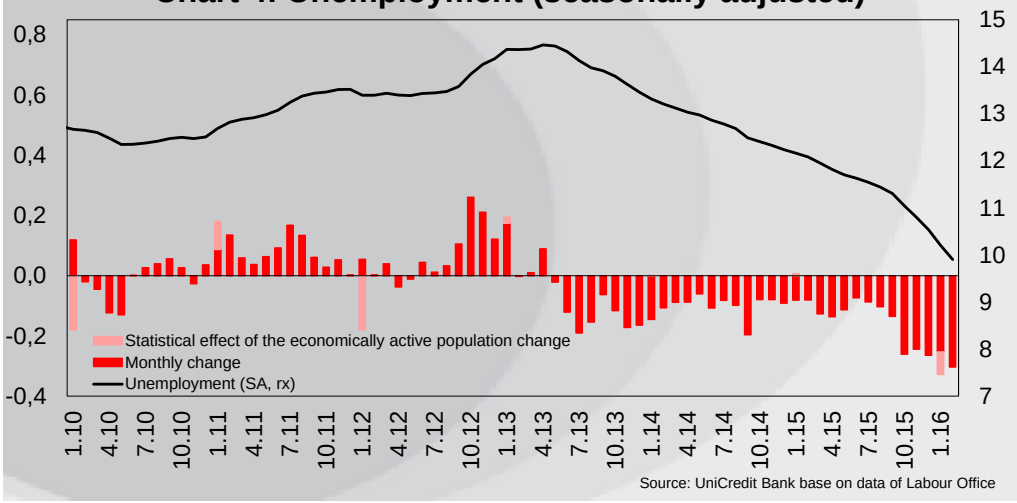
The labour market maintains its positive trend; in February, unemployment in Slovakia was fast approaching 10% - according to the methodology of the Central Office of Labour, Social Affairs, and Family, (disposable) unemployment went down by -0.30 pp to 10.09%. In February, the seasonally adjusted unemployment (calculation of UniCredit Bank) went down by another -0.30 pp to 9.90, reporting one-digit levels for the first time since February 2009. Unemployment was lower by 2.23 pp, i.e. by more than 58 thousand unemployed, compared to the same period a year ago.

The decline in unemployment is still largely due to the increasing domestic economy, which is able to generate new jobs. The number of job seekers in labour offices who were placed on the labour market went up at the end of the previous year, keeping close to its post-crisis peaks also in February, with as many as 18 thousand unemployed finding a new job. The increased demand for new employees persists. It is confirmed also by the statistics of vacant positions – their number grew to 34 thousand already, which represents a yoy growth by 22.5 thousand. At the same time, the relatively high number of vacant positions indicates that the decline in unemployment could continue also in the next months. On the other hand, a suitable workforce on the labour market is depleting quite fast; in some regions, employers can often not find adequate candidates at labour offices for their vacancies, due to an inadequate structure of the unemployed - a high portion of low-skilled long-term unemployed with no working habits or strong regional disparities. Slovak companies are increasingly employing employees from abroad; the number of foreigners working in Slovakia grew by more than 5 thousand (or by almost 30%) on a yoy basis in February, with their number increasing by more than one thousand in the last month. However, there is still around 26-27 thousand of foreigners working in Slovakia, i.e. about 1% of the employed, and Slovakia continues to "export" considerably more workforce than it "imports". If there are no major structural changes in the near term which would increase the employability of the long-term unemployed, we can expect that the growth of employment in Slovakia will be less and less visible in the

unemployment figures, being increasingly subsidised by import of workforce from abroad.

However, the disposable unemployment declined in February also due to administrative factors, in particular due to the higher number of the unemployed in municipal jobs. In February, nearly 20 thousand of the unemployed were allocated to smaller municipal and voluntary services. The increase in their number helped reduce the disposable unemployment by 0.08 pp in February compared to January, and by as much as 0.27 pp compared to last year's February. Municipal jobs thus accounted for around one fourth of the mom and one tenth of the yoy decline in unemployment.

Chart 4: Unemployment (seasonally adjusted)



Source: UniCredit Bank base on data of Labour Office

After adjustment for traditional season, unemployment was falling also in February in all Slovak regions, with the strongest decline being reported by the regions of Košice and Banská Bystrica and the slowest decline being reported by the region of Bratislava. In terms of districts, unemployment showed a marginal increase (after adjustment for the season) only in 3 out of 79 districts compared to the previous month – Vranov nad Topľou, Banská Bystrica, and Levice. In the remaining 76 districts, unemployment was falling in February, with the strongest decline being reported by the districts of Poltár, Rožňava, Trebišov, Medzilaborce, and Stropkov. Unemployment higher than 15% was reported only by 18 out of 79 Slovak districts in January (1 less than in January), with 5 of them reporting unemployment higher than 20% - Rimavská Sobota (27.2%), Kežmarok (22.3%), Rožňava (21.0%), Revúca (20.6%), and Poltár (20.1%). The lowest unemployment rate is still reported by the vicinity of the capital – districts of Bratislava (from 4.4% to 5.3%), Galanta (4.6%), Trnava (5.3%), Senec (5.4%), Pezinok (5.5%) and Malacky (5.7%), followed by some districts in the area of Považie – Piešťany (5.0%), Púchov (5.1%), as well as the Martin district (5.7%). Unemployment below 10% was reported in February by more than one half of Slovak districts - as much as 45 out of 79 Slovak districts (1 more than in January), with unemployment falling below 7% in 21 Slovak districts.

OUTLOOK

Growing economy should be able to generate new jobs also in the next months. We expect that unemployment continues to fall gradually, and its decline in the spring months will be made stronger also by the gradual commencement of seasonal jobs. According to the labour offices' methodology, disposable unemployment should reach the magical limit of 10% in March. (lk)

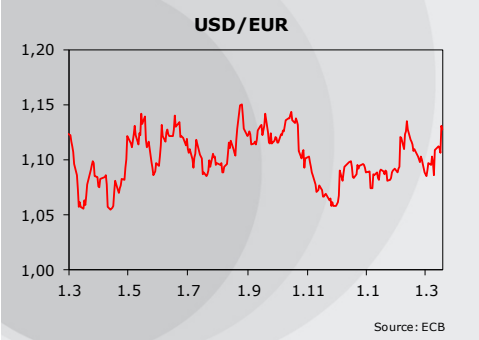
ECONOMIC OUTLOOK

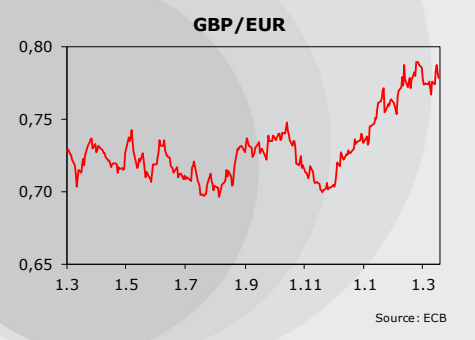
Slovakia	2011	2012	2013	2014	2015E	2016F	2017F
Real GDP growth	**2,8**	**1,5**	**1,4**	**2,5**	**3,6**	**3,2**	**3,2**
GDP per capita	13 052	13 398	13 643	13 947	14 287	14 860	15 383
Household consumption	**-0,6**	**-0,4**	**-0,8**	**2,4**	**2,4**	**2,9**	**2,6**
Government consumption	-1,7	-2,6	2,2	5,9	3,4	1,7	0,0
Gross investments	7,6	-14,0	1,5	2,6	13,1	-0,2	10,8
Exports	12,0	9,3	6,2	3,6	7,0	6,1	5,1
Imports	9,6	2,5	5,1	4,3	8,2	5,1	6,1
Industrial Production	**6,9**	**13,4**	**5,3**	**3,7**	**7,0**	**5,5**	**6,5**
Construction	-1,7	-12,5	-5,3	-4,2	16,3	2,7	6,5
Retail Sales	-2,8	-1,0	0,1	3,6	1,7	2,3	2,5
CPI (average)	**3,9**	**3,6**	**1,4**	**-0,1**	**-0,3**	**-0,3**	**1,4**
CPI (Dec.)	4,4	3,2	0,4	-0,1	-0,5	0,5	1,6
Real Estate inflation	-3,0	-1,1	-0,9	-0,8	0,3	2,3	2,5
Average Wage level	786	805	824	858	883	911	941
Nominal Wage growth	**2,2**	**2,4**	**2,4**	**4,1**	**2,9**	**3,1**	**3,4**
Real Wage growth	-1,6	-1,2	1,0	4,2	3,2	3,3	2,0
Employment growth (LFS)	1,5	-1,0	0,0	1,5	2,6	1,0	1,3
Unemployment (average, LFS)	**13,5**	**14,0**	**14,2**	**13,2**	**11,5**	**10,6**	**9,4**
Fiscal deficit (% of GDP)	-4,1	-4,2	-2,7	-2,8	-2,7	-2,0	-1,0
Public Debt (% of GDP)	43,3	51,9	54,6	53,5	53,0	52,7	51,4
Foreign Direct investment (EURbn)	2,8	3,2	-0,3	0,2	0,7	2,5	3,5
ECB Refi rate (%, Dec.)	**1,00**	**0,75**	**0,25**	**0,05**	**0,05**	**0,00**	**0,00**
3M EURIBOR (%, Dec.)	1,2	0,2	0,3	0,1	-0,1	-0,3	-0,3
3Y SK gov't bonds(%,Dec.)	2,7	0,3	0,7	-0,1	-0,6	0,0	1,5
10Y SK gov't bonds(%,Dec.)	5,2	3,9	2,7	1,2	0,7	1,0	2,0

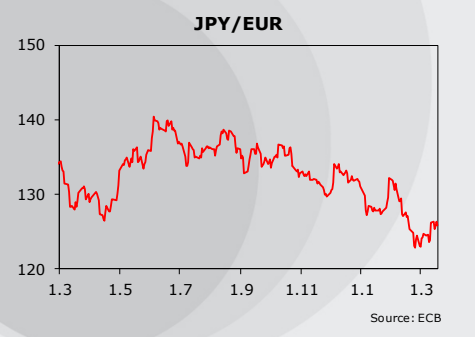
Abroad	2011	2012	2013	2014	2015	2016F	2017F
Eurozone GDP	**1,5**	**-0,6**	**-0,4**	**0,9**	**1,5**	**1,7**	**1,6**
German GDP	**3,1**	**0,9**	**0,5**	**1,6**	**1,7**	**1,8**	**1,4**
Czech R GDP	1,7	-1,0	-0,9	2,0	4,3	2,2	3,0
USA GDP	1,7	2,8	1,9	2,4	2,4	2,2	2,4
Eurozone Inflation	2,7	2,5	1,3	0,4	0	0,4	1,4
EUR/USD (average)	**1,39**	**1,28**	**1,33**	**1,33**	**1,11**	**1,08**	**1,16**
EUR/USD (Dec)	1,32	1,31	1,37	1,21	1,09	1,12	1,18
EUR/CZK (Dec)	25,8	25,1	27,5	27,7	27,0	27,0	26,5
EUR/HUF (Dec)	304,2	285,8	300,2	315,5	314,0	320,0	325,0
EUR/PLN (Dec)	4,5	4,1	4,2	4,3	4,3	4,2	4,2

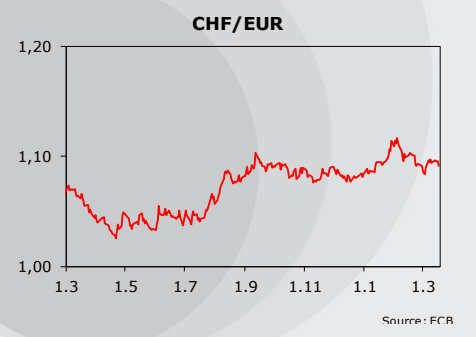
Source: NBS. SOSR. ÚPSVaR. MinFin SR. Eurostat. ECB
Forecasts: UniCredit Bank Slovakia – Slovakia. Eurozone. USA (EURIBOR. USDLIBOR. Brent. USD/EUR); UniCredit Group (CEE Economic Research. CIB) – Eurozone. USA

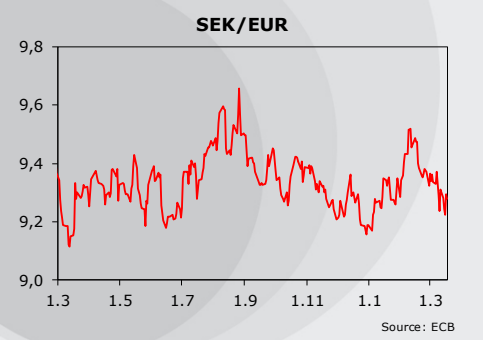
FOREIGN EXCHANGE

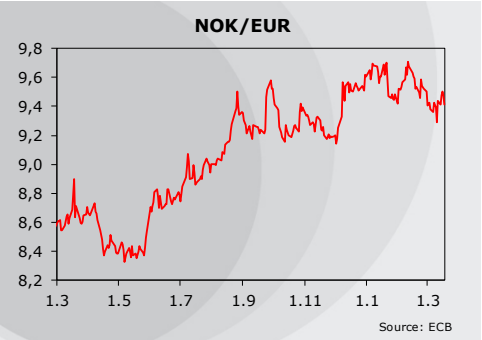


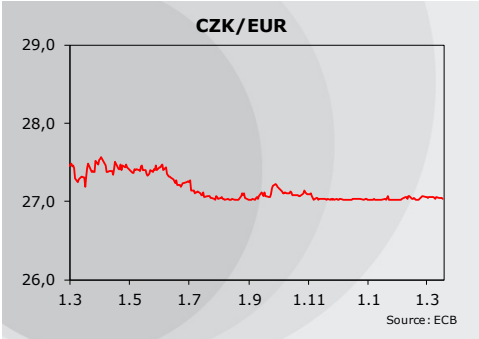


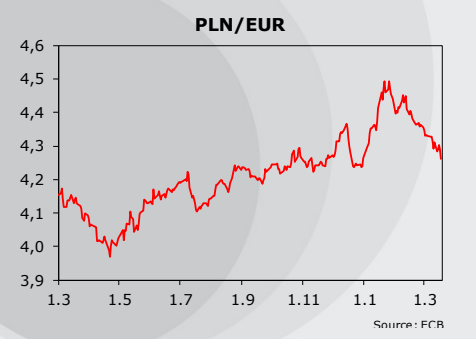


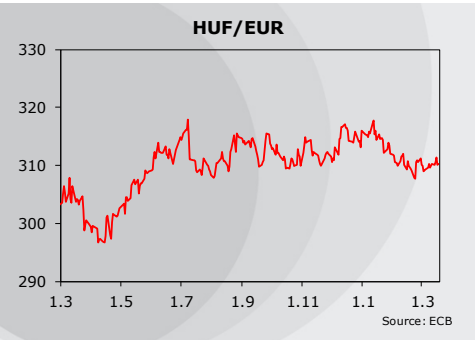


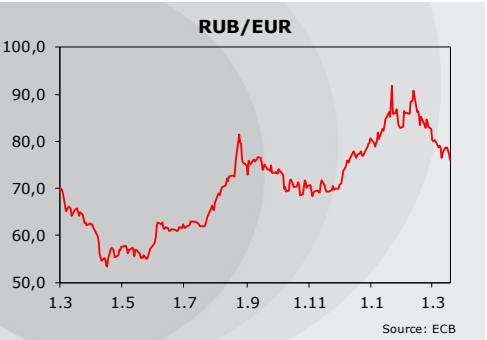












MONEY MARKET

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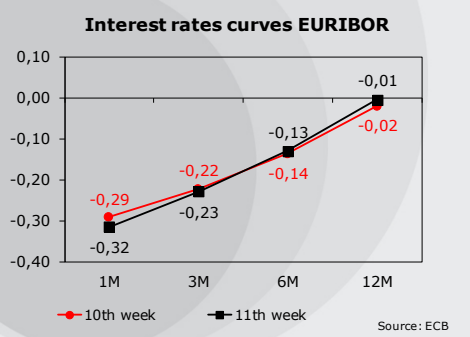
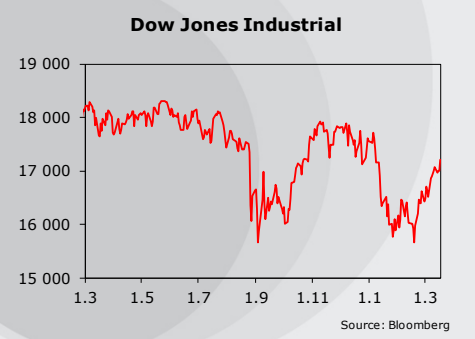
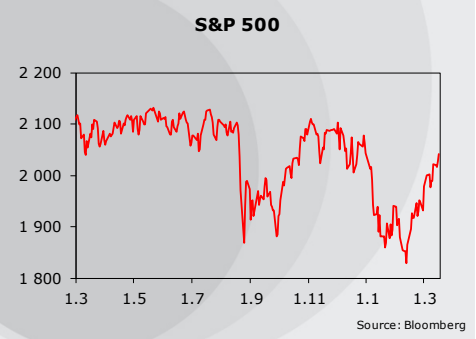
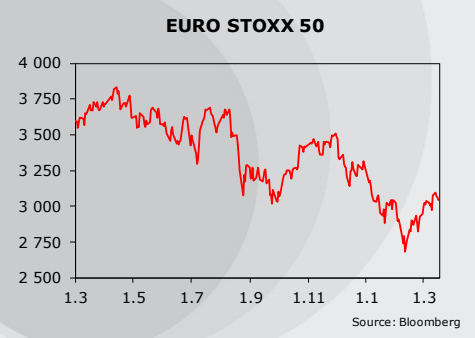
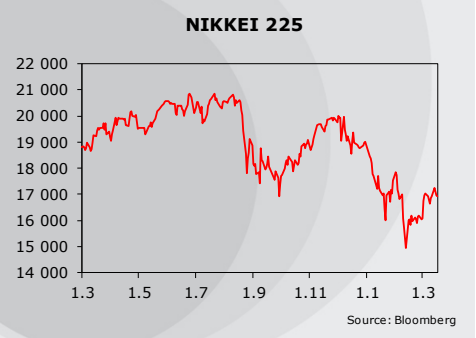


EQUITY









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