

Erste Bank, Vienna, and ZEW, the Centre for European Economic Research, Mannheim, have for the first time carried out a financial market survey for Central and Eastern Europe, Austria, and the Eurozone. Detailed results of the first survey conducted between 8 and 21 May 2007 are published in this edition of "Financial Market Report CEE", Volume 1. 88 financial market experts participated in this month's survey. The Financial Market Report CEE will be published on a monthly basis.

## Results of the first survey: Strong economic situation in CEE states

The first Financial Market Report CEE presents the results of the ZEW-Erste Bank survey conducted in May. It offers insight into the assessment of the current economic situation, and expectations for Central and Eastern Europe, the Eurozone and Austria for the next six months concerning the general economic situation, interest rates, exchange rates and stock market indices. The indicators reflect the difference between the percentage of analysts who are optimistic and the percentage of analysts who are pessimistic.

The possible outcome of the balance lies between -100 and +100 points. Positive values of the balance indicate that the number of participants expecting a rise in the respective

variable outweigh the number of participants with negative expectations.

In general, the survey reveals a positive assessment of the economic situation in CEE, the Eurozone and Austria. Currently the economic situation in CEE is considered "good" by 61.9 percent of the participants and by 0 percent as "bad". 38.1 percent evaluate it as normal. Thus, the balance of positive and negative expectations for this indicator is 61.9 points.

The indicators for the current economic situation for the Eurozone and Austria are 65.5 and 68.6 points. Compared to the test phase of the survey in April, the changes are almost negligible, between plus and minus one point.

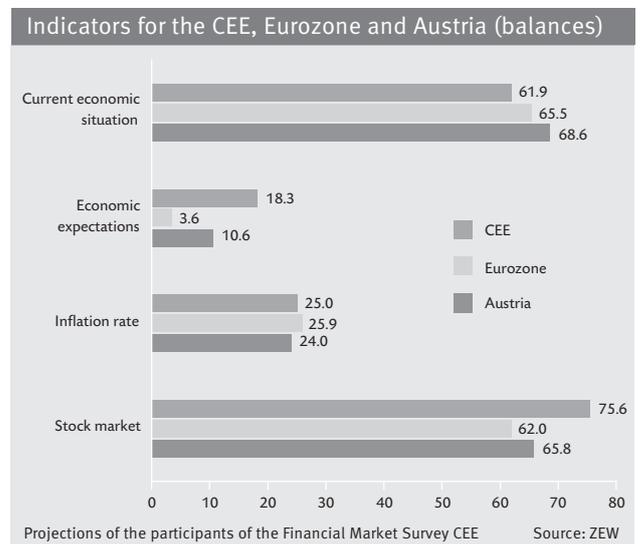
### A slightly positive outlook for the Eurozone, a better one for the CEE states

Economic expectations are not quite as optimistic as the current situation, but still positive. Though the vast majority of experts does not expect a change of the economic situation, the indicator for the Eurozone is only 3.6 points. The outlook for the CEE states and Austria is clearly better, with 18.3 and 10.6 points respectively. The indicator for the Eurozone dropped 7.3 points compared to the test phase of the survey, whereas the indicator for the CEE states lost 5.6 points and the indicator for Austria remained unchanged.

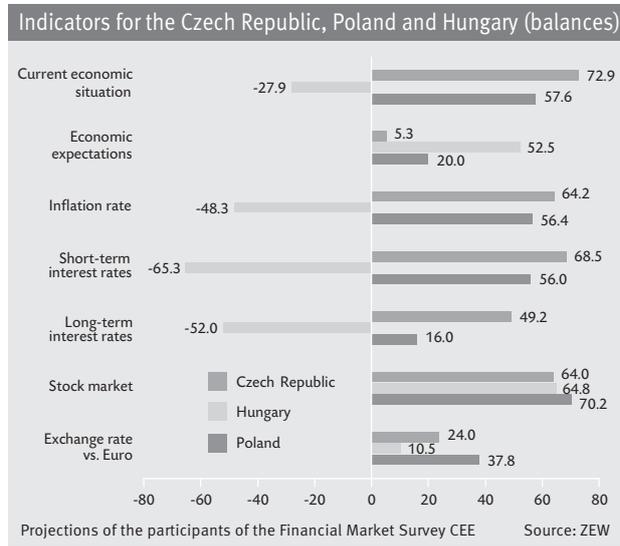
Most of the experts forecast increasing inflation rates for the upcoming six months for CEE, Eurozone and Austria. The indicators here increased by double digits compared to the test phase in April and lie now between 24 and 26 points. Furthermore a clear majority of 86 percent expect increasing short-term interest rates in the Eurozone and 50 percent forecast a growth in the long-term rates in Germany. These two rates are used as benchmarks for the expected development of the interest rates in the CEE countries.

The outlook for the stock market indices is significantly positive, with 75.6 points for the CEE states as measured in

the NTX CEE, 62.0 points for the Euro Stoxx 50, and 65.8 points for Austria's ATX.



## Strong current economic situation in the Czech Republic and Poland, but not in Hungary



Financial market experts regard the current economic situation in Poland and the Czech Republic as very satisfying, the balances reaching 58 and 73 points. Concerning Hungary, the economic situation is considered as weak (-28 points). There have been only slight changes compared to the test phase of the survey, between plus 3.8 and minus 1.1 points.

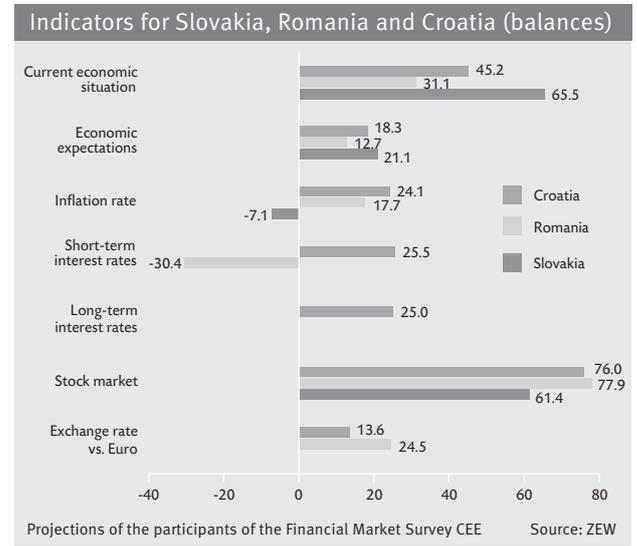
With regard to the economic expectations, the experts questioned in May are quite optimistic, especially when asked about Hungary (52.5 points) and Poland (20.0 points). Since 67 percent of financial market experts expect no change in the economic situation in the Czech Republic, the indicator reached only 5.3 points. When looking at last month's test survey, the balance rose a remarkable 25.2 points for Hungary, rose 4.1 points for Poland, and it dropped 10.1 points for the Czech Republic.

Almost 68 percent of survey participants forecast an increasing inflation rate in the Czech Republic. The corresponding indicator is at 64.2 points; this is the highest value within the analysed CEE states. In Poland financial market experts expect increasing rates (56.4 points) as well. In contrast, 66 percent of the experts predict an inflation decline in Hungary, and the balance reaches the lowest value of all CEE countries (-48.3 points).

The majority of the experts surveyed expect decreasing short-term and long-term interest rates in Hungary (-65 and -52 points), whereas they expect the interest rates to rise in Poland (56 and 16 points) and the Czech Republic (68 and 49 points).

When asked about the stock markets, the experts responded once again very positively. Indicators are between 64 and 70 points, with the Polish stock market considered to have the best chances for further positive development. The financial market experts predict the value of the local currencies to rise (measured against the Euro), especially the Zloty (38 points) and the Koruna (24 points), and to a lesser extent the Forint (10 points).

## Robust economies and a positive outlook for Slovakia and Croatia; interest rate cuts expected in Romania



According to the experts surveyed, all three countries seem to be enjoying a strong current economic situation, above all Slovakia with 65.5 points, even though the indicator dropped by 13.6 points compared to last month's test run. Croatia scores a strong 45.2 points and Romania reaches 31.1 points. Economic expectations are also on the positive side, with 21.1 points for Slovakia, 18.3 points for Croatia, and 12.7 points for Romania.

Financial market experts expect rising inflation rates in Croatia (24.1 points) and Romania (17.7 points), where strong wage and credit growth are leading to overheating and inflationary pressures. But the experts say that this should not be the case in Slovakia (-7.1 points). The current statistic in Slovakia shows that in the first four months of 2007 prices went up by 2.8%, while in the same period last year they increased by 4.4%.

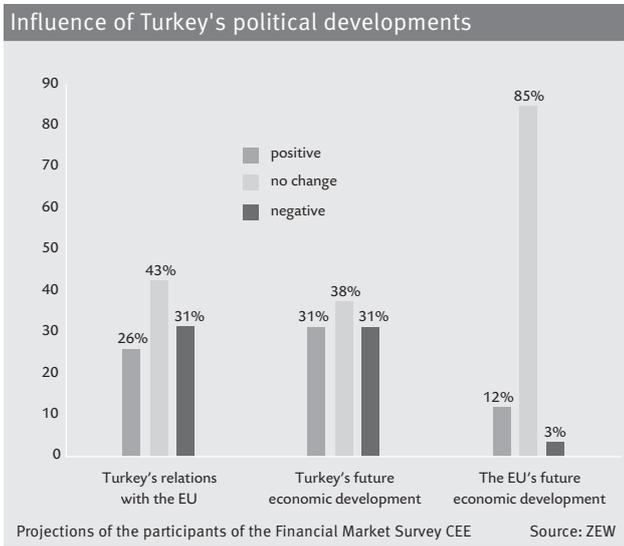
Financial market experts expect short-term interest rates to decrease in Romania (-30 points) and expect short- and long-term interest rates to increase in Croatia (26 and 25 points).

The outlook for the three countries' stock markets is overwhelmingly positive, with 61.4 points for Slovakia, 77.9 for Romania and 76.0 for Croatia. Additionally we analysed the indicator for Slovenia's SBI 20. It gained 23.6 points in comparison with the test phase of the survey. This is in line with the outstanding SBI 20 return of the past 52 weeks of 86 percent.

Last but not least, and in accordance with the countries' robust economies, the Croatian Kuna (14 points) and the Romanian Lei (25 points) are also expected to gain over the Euro.

Especially concerning the Romanian Lei, one of the currencies with the best performance in 2006 due to the high interest from foreign investors, the experts expect further appreciation. There were still many investors, which were unable to invest in Romania before the EU entry, but following the entry they will be able to do so.

## Special Question: What influence will the recent political developments in Turkey have on Turkey's relations with the EU, Turkey's future economic development compared to the EU



Each month the financial experts answer a special question. In May they were asked about their expectations concerning the influence of the recent political developments in Turkey on Turkey's relations with the EU, Turkey's future economic development and the EU's future economic development.

The government crisis in Turkey began with the nomination of Foreign Minister Abdullah Gül as presidential candidate by Prime Minister Tayyip Erdogan. Both are members of the Justice and Development Party (AKP), which is at times accused of having Islamist tendencies. At the heart of the conflict is a fear that the ruling party would misuse its control of both the Parliament and the presidency to erode the secular foundation of modern Turkey. The secularist opposition boycotted the vote in Parliament and took the issue to the Constitutional Court, which declared the vote for Gül invalid. In response, parliament endorsed the AKP's call for early elections. In a statement seen as a warning that it might intervene, the military reaffirmed its willingness to act as the "absolute defender of secularism".

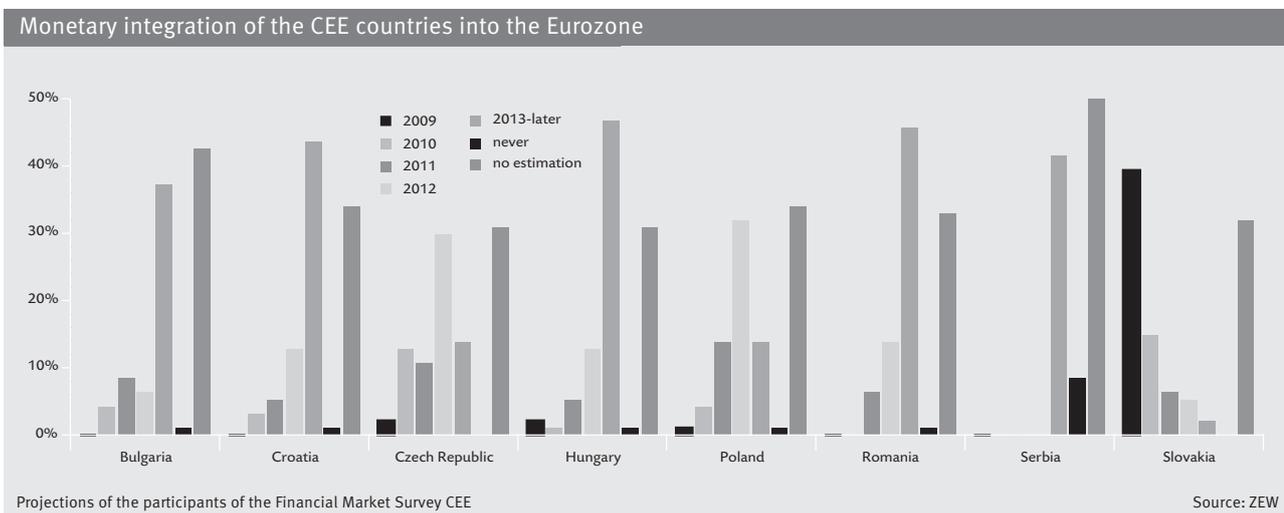
The reactions of the financial markets, various institutions and governments on these developments were heterogeneous. The political turmoil has caused weaknesses in equity and bond markets, and it has resulted in a lower value of the Turkish lira. After the ruling issued by the Constitutional Court of Turkey, the European Commission welcomed the announcement of holding new parliamentary elections soon in order to ensure political stability and democratic development in Turkey.

The expectations of the European Commission are mostly in line with the results of the survey. The majority of financial market experts currently see no reason to change their view on Turkey's relations with the EU. However, 31 percent of the survey participants expect the political developments to have a negative influence on these relations, 26 percent expect a positive influence.

The experts' view concerning the impact of the early parliamentary and presidential elections on Turkey's future development is quite balanced. An equal share of 31 percent each of financial market experts, expect a negative and a positive influence, whereas 38 percent expect no change after the government crisis.

Most participants (85 percent) feel sure that the EU's future economic development will remain unaffected by the current political situation in the Turkey. Nearly 12 percent expect that Turkey is more likely to converge politically and economically with the EU, with more benefits for the Union, only 3.4 percent expect a negative influence.

In the test phase of the survey conducted in April the financial experts were asked about their expectations concerning the year of the monetary integration of selected CEE countries. The earliest possible date was the year 2009. The results made Slovakia (after Malta and Cypress) the country that is expected to be the first to adopt the Euro in 2009, and the Czech Republic and Poland the most probable candidates for 2012. Hungary, Romania and Bulgaria are not expected to join the Eurozone before 2013.



**ZEW-Financial Market Survey: June 2007**

Current economic situation	good		acceptable (normal)		bad		balance									
Austria	68.6	(-0.8)	31.4	(+0.8)	0.0	(+/-0.0)	68.6	(-0.8)								
Croatia	45.2	(-2.4)	54.8	(+4.0)	0.0	(-1.6)	45.2	(-0.8)								
Czech Republic	74.6	(+0.8)	23.7	(-2.5)	1.7	(+1.7)	72.9	(-0.9)								
Hungary	1.6	(-5.9)	68.9	(+10.7)	29.5	(-4.8)	-27.9	(-1.1)								
Poland	59.3	(-0.7)	39.0	(+5.2)	1.7	(-4.5)	57.6	(+3.8)								
Romania	39.7	(-7.0)	51.7	(+11.7)	8.6	(-4.7)	31.1	(-2.3)								
Slovakia	68.8	(-11.8)	27.9	(+10.0)	3.3	(+1.8)	65.5	(-13.6)								
CEE	61.9	(-0.8)	38.1	(+2.3)	0.0	(-1.5)	61.9	(+0.7)								
Eurozone	65.5	(+1.3)	34.5	(-1.3)	0.0	(+/-0.0)	65.5	(+1.3)								
Economic expectations	improve		no change		worsen		balance									
Austria	17.0	(+4.2)	76.6	(-8.5)	6.4	(+4.3)	10.6	(-0.1)								
Croatia	25.0	(-2.8)	68.3	(-0.6)	6.7	(+3.4)	18.3	(-6.2)								
Czech Republic	19.3	(-5.3)	66.7	(+0.5)	14.0	(+4.8)	5.3	(-10.1)								
Hungary	59.3	(+12.3)	33.9	(+0.6)	6.8	(-12.9)	52.5	(+25.2)								
Poland	29.1	(+3.7)	61.8	(-3.3)	9.1	(-0.4)	20.0	(+4.1)								
Romania	29.1	(-5.3)	54.5	(+3.7)	16.4	(+1.6)	12.7	(-6.9)								
Slovakia	28.1	(-12.8)	64.9	(+13.4)	7.0	(-0.6)	21.1	(-12.2)								
CEE	25.0	(-1.9)	68.3	(-1.8)	6.7	(+3.7)	18.3	(-5.6)								
Eurozone	14.1	(-6.2)	75.4	(+5.1)	10.5	(+1.1)	3.6	(-7.3)								
Inflation rate	increase		no change		decrease		balance									
Austria	28.3	(+7.0)	67.4	(+1.4)	4.3	(-8.4)	24.0	(+15.4)								
Croatia	37.9	(+8.1)	48.3	(+6.2)	13.8	(-14.3)	24.1	(+22.4)								
Czech Republic	67.8	(+26.5)	28.6	(-12.7)	3.6	(-13.8)	64.2	(+40.3)								
Hungary	17.8	(-16.0)	16.1	(-2.4)	66.1	(+18.4)	-48.3	(-34.4)								
Poland	60.0	(+23.9)	36.4	(-4.6)	3.6	(-19.3)	56.4	(+43.2)								
Romania	37.3	(+6.4)	43.1	(+8.6)	19.6	(-15.0)	17.7	(+21.4)								
Slovakia	17.5	(-7.9)	57.9	(+16.6)	24.6	(-8.7)	-7.1	(+0.8)								
CEE	39.3	(+15.5)	46.4	(-9.2)	14.3	(-6.3)	25.0	(+21.8)								
Eurozone	32.8	(+6.2)	60.3	(-0.6)	6.9	(-5.6)	25.9	(+11.8)								
Short-term interest rates	increase		no change		decrease		balance									
	[abs.]	[rel.]	[abs.]	[rel.]	[abs.]	[rel.]	[abs.]	[rel.]								
Croatia	39.2	(+10.1)	26.1	(+3.2)	47.1	(-7.1)	39.1	(-0.5)	13.7	(-3.0)	34.8	(-2.7)	25.5	(+13.1)	-8.7	(+5.9)
Czech Republic	70.5	(+5.7)	30.4	(+6.3)	27.5	(-5.8)	43.5	(+2.8)	2.0	(-2.7)	26.1	(-9.1)	68.5	(+5.6)	4.3	(+15.4)
Hungary	11.6	(-7.4)	7.7	(-2.9)	11.5	(+4.6)	9.6	(-7.9)	76.9	(+0.1)	82.7	(+10.8)	-65.3	(-10.2)	-75.0	(-13.7)
Poland	58.0	(+1.4)	14.9	(-6.6)	2.0	(-1.8)	68.1	(+17.1)	2.0	(-9.1)	17.0	(-10.5)	56.0	(+3.2)	-2.1	(+3.9)
Romania	17.4	(-5.0)	16.7	(-5.7)	34.8	(+0.1)	20.8	(+6.5)	47.8	(+2.8)	62.5	(-0.8)	-30.4	(-9.9)	-45.8	(-4.9)
Slovakia	12.2	(-4.7)	4.1	(-8.6)	49.0	(+13.4)	27.1	(+5.3)	38.8	(+10.8)	68.8	(+3.3)	-26.6	(+4.0)	-64.7	(-11.9)
Eurozone	85.5	(+10.5)			14.5	(-9.0)			0.0	(-1.8)			85.5	(+12.0)		
Long-term interest rates	increase		no change		decrease		balance									
	[abs.]	[rel.]	[abs.]	[rel.]	[abs.]	[rel.]	[abs.]	[rel.]								
Croatia	39.6	(-7.1)	21.2	(-9.7)	45.8	(+16.9)	42.6	(+11.6)	14.6	(-9.8)	36.2	(-1.9)	25.0	(+2.7)	-15	(-7.8)
Czech Republic	56.7	(-7.3)	27.7	(-10.8)	35.8	(+11.8)	53.2	(+10.9)	7.5	(-4.5)	19.1	(-0.1)	49.2	(-2.8)	8.6	(-10.7)
Hungary	12.0	(+1.3)	8.5	(-0.6)	24.0	(+6.1)	8.5	(-6.0)	64.0	(-7.4)	83.0	(+6.6)	-52.0	(+8.7)	-74.5	(-7.2)
Poland	32.0	(-4.0)	12.8	(-4.2)	52.0	(+18.0)	48.9	(+4.2)	16.0	(-14.0)	38.3	(+/-0.0)	16.0	(+10.0)	-25.5	(-4.2)
Romania	16.6	(-11.6)	8.3	(-11.2)	40.5	(+20.0)	38.9	(+19.5)	42.9	(-8.4)	52.8	(-8.3)	-26.3	(-3.2)	-44.5	(-2.9)
Slovakia	38.0	(+2.3)	6.5	(-6.9)	50.0	(+14.3)	60.9	(+20.5)	12.0	(-16.6)	32.6	(-13.6)	26.0	(+18.9)	-26.1	(+6.7)
Germany	50.0	(-7.8)			40.7	(+11.0)			9.3	(-3.2)			40.7	(-4.6)		
Stock market indices	increase		no change		decrease		balance									
EURO STOXX 50	68.0	(+1.3)			26.0	(+3.2)			6.0	(-4.5)			62.0	(+5.8)		
ATX (Austria)	71.8	(+15.6)			22.2	(-11.1)			6.0	(-4.5)			65.8	(+20.1)		
NTX (CEE)	80.0	(+2.2)			15.6	(+0.8)			4.4	(-3.0)			75.6	(+5.2)		
CROBEX (Croatia)	76.0	(-4.4)			24.0	(+12.2)			0.0	(-7.8)			76.0	(+3.4)		
PX 50 (Czech Rep.)	70.0	(-3.7)			24.0	(+6.5)			6.0	(-2.8)			64.0	(-0.9)		
BUX (Hungary)	72.6	(-1.1)			19.6	(+0.3)			7.8	(+0.8)			64.8	(-1.9)		
WIG (Poland)	76.6	(+3.4)			17.0	(-0.9)			6.4	(-2.5)			70.2	(+5.9)		
BET (Romania)	82.3	(+8.2)			13.3	(-5.2)			4.4	(-3.0)			77.9	(+11.2)		
SAX (Slovakia)	68.2	(-0.9)			25.0	(+3.2)			6.8	(-2.3)			61.4	(+1.4)		
SBI 20 (Slovenia)	86.1	(+13.6)			13.9	(-3.6)			0.0	(-10.0)			86.1	(+23.6)		
Exchange rates (vs. Euro)	appreciate		no change		depreciate		balance									
Kuna (Croatia)	37.3	(-13.6)			39.0	(-3.1)			23.7	(+16.7)			13.6	(-30.3)		
Koruna (Czech Rep.)	37.0	(-8.3)			50.0	(+6.2)			13.0	(+2.1)			24.0	(-10.4)		
Forint (Hungary)	29.8	(-3.5)			50.9	(+13.0)			19.3	(-9.5)			10.5	(+6.0)		
Zloty (Poland)	49.1	(-8.7)			39.6	(+11.5)			11.3	(-2.8)			37.8	(-5.9)		
Lei (Romania)	43.4	(-9.2)			37.7	(+7.2)			18.9	(+2.0)			24.5	(-11.2)		
Koruna (Slovakia)	45.6	(-6.0)			42.1	(+5.0)			12.3	(+1.0)			33.3	(-7.0)		
US-Dollar	33.9	(+15.7)			17.9	(-3.3)			48.2	(-12.4)			-14.3	(+28.1)		

Note: 88 Financial experts participated in the May survey which was conducted during the period 05/08/07-05/21/07. Analysts were asked about their expectations for the next 6 months. Numbers displayed are percentages (month-over-month percentage point changes compared to the test phase in April in parentheses). Balances refer to the differences between positive and negative assessments.