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ERSTE BANK

Financial Market Report CEE

Volume 2 · July 2007

International Finance Market Data: Assessments and Expectations
ZEW Economic Sentiment Indicator for Central and Eastern Europe, Supported by Erste Bank

ZEW, the Centre for European Economic Research, Mannheim, and Erste Bank der oesterreichischen Sparkassen, Vienna, carry out a monthly survey for Central and Eastern Europe, Austria, and the Eurozone asking financial experts about their assessment and expectations with regard to economic and financial market data. The results of the present survey conducted between 6 and 25 June 2007 are published in this edition of the "Financial Market Report CEE", Volume 2. 78 financial market experts participated in this month's survey.

Good economic situation for CEE countries will continue

The survey of financial market experts carried of by the ZEW (Centre for Centre for European Economic Research), Mannheim, with support from the Erste Bank der oesterreichischen Sparkassen AG, Vienna, shows that the current economic situation in the countries of Central and Eastern Europe is assessed as good. The expectations for the following six months are optimistic as well. For Austria, the experts rate the situation and outlook very similar.

Economic Outlook for CEE countries, Austria and the Eurozone

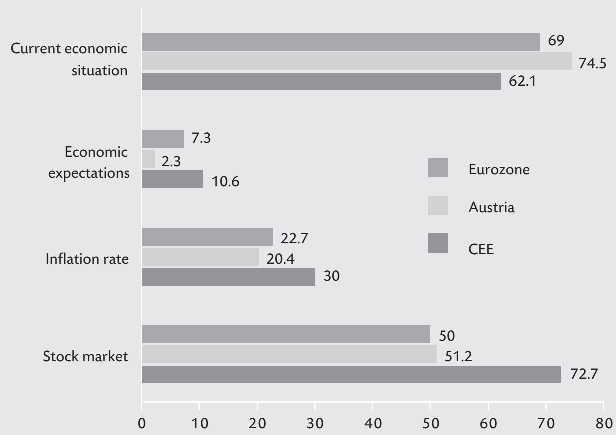
The ZEW-Erste Bank Sentiment Indicator for Central and Eastern Europe (CEE) has decreased by 7.7 points and now stands at a level of 10.6 points. The indicator is calculated as the balance between positive and negative assessments of the economic outlook for the Central and Eastern European countries. The major part of the financial experts projects no change in the economic development in the next six months (78.6 percent). 16 percent of the respondents assume that the situation will improve; that are 9 percent less than in the previous month. 5.4 percent of the experts, 1.3 percent less than in the May survey, expect a worsening of the economic situation in the next six months. The experts assess the current situation for the CEE countries as mostly good (balance: 62.1 points).

For Austria, the financial market experts assess the situation as superior compared to the countries in Central and Eastern Europe (balance: 74.5 points). This is consistent with the good business cycle situation in Austria. The outlook is rather neutral, 89.1 percent of the respondents do not expect a change within the next six months. With a balance of 7.3 points, the outlook for the Eurozone is even less optimistic than that of the CEE countries, but better compared to the last month's survey (+3.7 points). However, the experts judge the current situation to be better than in the CEE countries (balance: 69 points).

Inflation expectations for the CEE region as a whole have increased; the balance now reaches a level of 30 points. For Austria, there are still expectations for an increasing inflation rate in the next six months; the balance is 20.4 points compared to 24 points last month. For the Eurozone as a whole, expectations of rising inflation also outweigh that of decreasing inflation by 22.7 points.

The optimism of the financial experts concerning the stock market development is still marked, even if lower on balance compared to last month's survey. For all indices, the proportion of experts expecting an increase outweighs the proportion expecting a decrease. E.g., for the ATX, the balance is 51.2 points. This is 14.6 points lower than in the May survey. The optimism for the Euro Stoxx 50 has also declined by 12 points. For the NTX, the stock market index of the CEE countries, the balance is almost as high as last month (72.7 points).

Indicators for the CEE, Eurozone and Austria (balances)

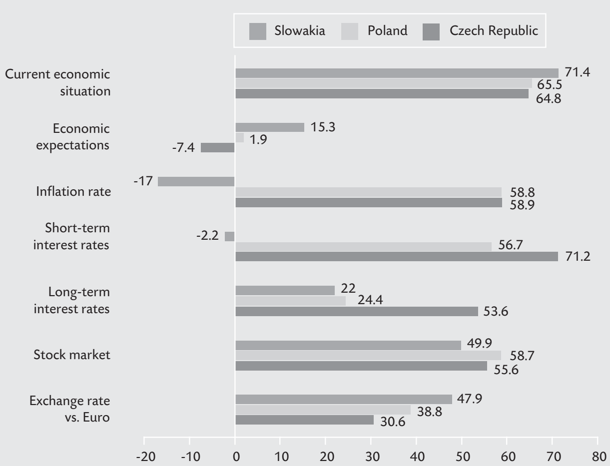


Balance of positive and negative assessment category chosen by respondents of the Financial Market Survey CEE

Source: ZEW

Czech Republic, Poland, and Slovakia: Very good economic situation, mixed expectations

Indicators for the Czech Republic, Poland, and Slovakia



Balance of positive and negative assessment category chosen by respondents of the Financial Market Survey CEE Source: ZEW

The financial experts assess the current economic situation in the Czech Republic, Poland, and Slovakia as especially good. The balance of answers opting for “good” versus “bad” is above 60 points for all three countries. For Slovakia, 21.1 percent of the respondents even expect a further improvement of the economy, 73.1 percent do not expect a change and 5.8 percent regard a worsening as likely. Opposite to this assessment, the outlook for the Czech Republic is not as good. Here, a majority of experts does not expect a change, and the respondents expecting a worse economic situation outweigh the optimistic ones (balance: -7.4 points). For Poland, the economic outlook is almost balanced (1.9 points), and again the majority does not expect a change (68.5 percent).

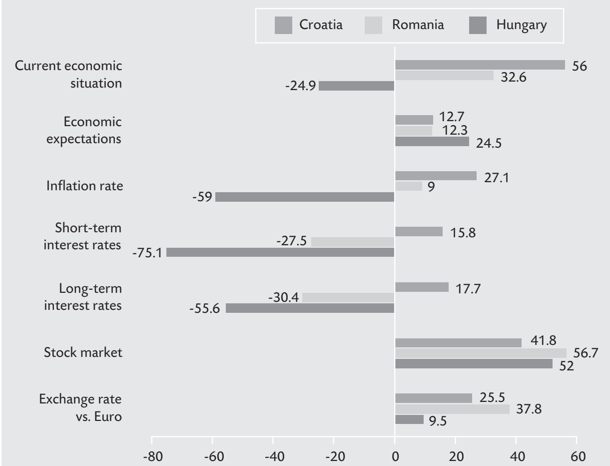
Consistent with the expectations of rising inflation rates in the Czech Republic and Poland, the financial market experts expect rising short-term interest rates. In Slovakia, the experts do not expect decreasing short-term rates any longer. The balance of short-term interest rate expectations is almost neutral (-2.2 points) with a majority of respondents forecasting no change at all (57.8 percent). The expectations for long-term interest rates are more similar than for short-term rates. Here, the experts expect rising rates, especially for the Czech Republic and, to a lesser extend for both, Poland and Slovakia.

The stock market development can be expected to be sound for the next six months. The financial experts forecast increasing indices, all balances are positive. However, the optimism is not as pronounced as last month as all balances show lower values; -8.4 points for the PX50 (Czech Republic), -11.5 points for the WIG (Poland), and -11.5 points for the SAX (Slovakia). For all three countries, the majority of respondents still expects the indices to increase.

The participants forecast an appreciation of the country-specific currencies versus the Euro. The highest balance is deduced for the Slovak Koruna (47.9 points) followed by the Zloty (38.8 points) and the Czech Koruna (30.6 points) for this sample of countries.

Croatia, Hungary, and Romania: Improvement of economic situation expected

Indicators for Croatia, Hungary, and Romania



Balance of positive and negative assessment category chosen by respondents of the Financial Market Survey CEE Source: ZEW

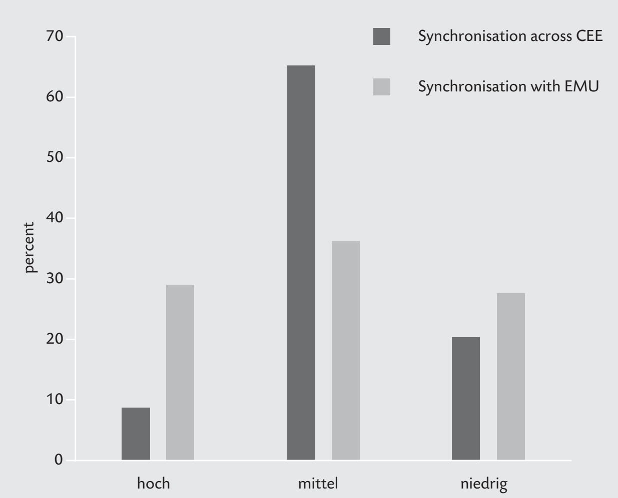
For Croatia, Hungary, and Romania, the expectations of the financial experts are overall optimistic. On balance, the experts project improving economic conditions for Croatia (12.7 points), for Hungary (24.5 points) and for Romania (12.3 points). While the change of the balance for Croatia and Romania is not large (-5.6 points and -0.4 points), the balance for Hungary has lost 28 points. The share of respondents that expect the Hungarian economy to improve in the following six months has decreased by 10.2 points, and the share of experts that expect a worsening has increased by 17.8 points. In addition to that, the experts assess the economic situation in Hungary on balance as “bad” (-24.9 points).

Financial experts expect the Hungarian inflation rate to decrease. Consistent with this view, the expectations for lower short- and long-term interest rate prevail on balance. The category of decreasing rates also has the highest occupation for both time horizons. For Croatia, all three balances – inflation rates, short- and long-term interest rates – are positive; the respondents forecast increasing inflation rates and, therefore, project interest rates to rise on balance as well. For Romania, the expectations of the financial experts for the development of inflation and interest rates differ. The experts project increasing inflation on balance (9.0 points), but forecast short- and long-term interest rates to fall.

As for all other countries, the experts are optimistic with regard to stock market developments for the three countries. Accordingly, the balances are positive. Again, experts forecast the currencies to appreciate against the Euro. The highest value in this respect shows the Romanian Lei with a balance of 37.8 points, whose value has increased by 13.3 points compared to the previous month. A similar development is expected for the Croatian Kuna, the balance amounts to 25.5 points. The expert’s expectations with regard to the Hungarian Forint have not changed on balance (9.5 points), but both categories of an appreciating or a depreciating currency have gained weight to almost the same extent (4.2 and 5.2 points).

Special Question: Which countries lead the business cycle within the CEE region and synchronisation of business cycles across CEE countries and with the Eurozone

Synchronisation of business cycles across CEE and of the CEE countries with the Eurozone



Answers of the participants of the Financial Market Survey CEE Source: ZEW

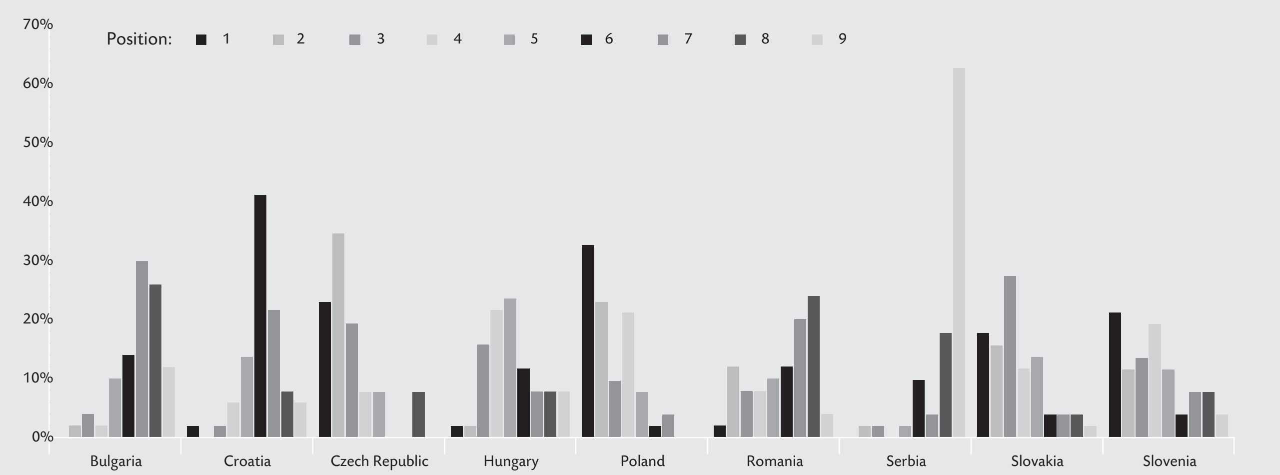
The economic convergence of the states that joined the EU in 2004 and will, at some point in time, all take part in the European Monetary Union (EMU), is being debated in the academic literature, especially on optimum currency areas. Economic theory as well as empirical studies state that the countries forming the union should demonstrate a high level of convergence. In addition to that, a single monetary policy is easier to conduct if the synchronisation of business cycles is sufficiently high across countries. In this case, the common interest rate does not lead to diverging effects that depend on the state of the regional economies. This month's special question takes a look at the synchronisation of CEE countries' business cycles within the CEE region and with the EMU. This is particularly interesting for the CEE countries that already joined the EU.

First the financial experts evaluate the synchronisation of business cycles across the CEE countries. The participants rather opt for a lower congruence of the cyclical development in the CEE region. 65.2 percent of them consider business cycle synchronisation in CEE to be of an intermediate level, 20.3 percent evaluate the synchronisation to be at a rather low level, and 8.7 percent at a high level. Asked for their evaluation of the correlation between the EMU and CEE business cycles, the answers are not that clear cut: 36.2 percent of the financial experts perceive this business cycle synchronisation to be of an intermediate degree, 29 percent answered that EMU and CEE countries are highly synchronised, and 27.5 percent responded that synchronisation is rather low. It is noteworthy that the experts consider the correlation among CEE countries considerably higher than between CEE countries and the EMU.

In the second part of the special question, the experts were asked to rank the CEE countries according to their lead in the region's business cycles. Evaluating the rankings country by country, Poland and Slovenia lead the CEE business cycle. For both countries, the first position is most strongly occupied compared to the other possible categories. This result seems most intuitive as Poland is the largest economy of the region and Slovenia has the highest per capita income (both measured in Purchasing Power Parities). Poland and Slovenia are followed (in this order) by the Czech Republic, the Slovak Republic, Hungary, Croatia, Bulgaria, Rumania and Serbia. Only the fact that the experts assign a higher impact on the business cycle of the region to Croatia than to the new EU member states, Rumania and Bulgaria, is somewhat surprising.

If the ranking is not performed according to the highest category occupied for each country individually, but the hierarchy is built according to the highest entry across all Central and Eastern European countries, the picture still is similar. Poland is the country which was named first place most often (32.1 percent), with Slovenia and the Czech Republic are also ranking high on the list (20.2 percent and 22.6 percent). Serbia again takes the last place; Hungary, Croatia and Bulgaria are again in the mid-field.

Business cycle leadership within the CEE region



Answers of the participants of the Financial Market Survey CEE Source: ZEW

ZEW-Financial Market Survey: June 2007

Current economic situation	good		acceptable (normal)		bad		balance	
Austria	74.5	(+5.9)	25.5	(-5.9)	0.0	(+/-0.0)	74.5	(+5.9)
Croatia	56.0	(+10.8)	44.0	(-10.8)	0.0	(+/-0.0)	56.0	(+10.8)
Czech Republic	68.5	(-6.1)	27.8	(+4.1)	3.7	(+2.0)	64.8	(-8.1)
Hungary	3.4	(+1.8)	68.3	(-0.6)	28.3	(-1.2)	-24.9	(+3.0)
Poland	67.3	(+8.0)	30.9	(-8.1)	1.8	(+0.1)	65.5	(+7.9)
Romania	46.1	(+6.4)	40.4	(-11.3)	13.5	(+4.9)	32.6	(+1.5)
Slovakia	73.2	(+4.4)	25.0	(-2.9)	1.8	(-1.5)	71.4	(+5.9)
CEE	63.8	(+1.9)	34.5	(-3.6)	1.7	(+1.7)	62.1	(+0.2)
Eurozone	69.0	(+3.5)	31.0	(-3.5)	0.0	(+/-0.0)	69.0	(+3.5)

Economic expectations	improve		no change		worsen		balance	
Austria	6.6	(-10.4)	89.1	(+12.5)	4.3	(-2.1)	2.3	(-8.3)
Croatia	17.0	(-8.0)	78.7	(+10.4)	4.3	(-2.4)	12.7	(-5.6)
Czech Republic	7.4	(-11.9)	77.8	(+11.1)	14.8	(+0.8)	-7.4	(-12.7)
Hungary	49.1	(-10.2)	26.3	(-7.6)	24.6	(+17.8)	24.5	(-28.0)
Poland	16.7	(-12.4)	68.5	(+6.7)	14.8	(+5.7)	1.9	(-18.1)
Romania	32.7	(+3.6)	46.9	(-7.6)	20.4	(+4.0)	12.3	(-0.4)
Slovakia	21.1	(-7.0)	73.1	(+8.2)	5.8	(-1.2)	15.3	(-5.8)
CEE	16.0	(-9.0)	78.6	(+10.3)	5.4	(-1.3)	10.6	(-7.7)
Eurozone	18.2	(+4.1)	70.9	(-4.5)	10.9	(+0.4)	7.3	(+3.7)

Inflation rate	increase		no change		decrease		balance	
Austria	29.5	(+1.2)	61.4	(-6.0)	9.1	(+4.8)	20.4	(-3.6)
Croatia	39.6	(+1.7)	47.9	(-0.4)	12.5	(-1.3)	27.1	(+3.0)
Czech Republic	62.8	(-5.0)	33.3	(+4.7)	3.9	(+0.3)	58.9	(-5.3)
Hungary	17.8	(+/-0.0)	5.4	(-10.7)	76.8	(+10.7)	-59.0	(-10.7)
Poland	64.7	(+4.7)	29.4	(-7.0)	5.9	(+2.3)	58.8	(+2.4)
Romania	36.3	(-1.0)	36.4	(-6.7)	27.3	(+7.7)	9.0	(-8.7)
Slovakia	15.1	(-2.4)	52.8	(-5.1)	32.1	(+7.5)	-17.0	(-9.9)
CEE	40.0	(+0.7)	50.0	(+3.6)	10.0	(-4.3)	30.0	(+5.0)
Eurozone	34.0	(+1.2)	54.7	(-5.6)	11.3	(+4.4)	22.7	(-3.2)

Short-term interest rates	increase				no change				decrease				balance			
	[abs.]		[rel.]		[abs.]		[rel.]		[abs.]		[rel.]		[abs.]		[rel.]	
Croatia	34.2	(-5.0)	25.0	(-1.1)	47.4	(+0.3)	47.2	(+8.1)	18.4	(+4.7)	27.8	(-7.0)	15.8	(-9.7)	-2.8	(+5.9)
Czech Republic	75.6	(+5.1)	23.8	(-6.6)	20.0	(-7.5)	50.0	(+6.5)	4.4	(+2.4)	26.2	(+0.1)	71.2	(+2.7)	-2.4	(-6.7)
Hungary	6.2	(-5.4)	10.9	(+3.2)	12.5	(+1.0)	13.0	(+3.4)	81.3	(+4.4)	76.1	(-6.6)	-75.1	(-9.8)	-65.2	(+9.8)
Poland	68.1	(+10.1)	28.9	(+14.0)	11.4	(+9.4)	57.9	(-10.2)	11.4	(+9.4)	13.2	(-3.8)	56.7	(+0.7)	15.7	(+17.8)
Romania	17.5	(+0.1)	20.5	(+3.8)	37.5	(+2.7)	20.5	(-0.3)	45.0	(-2.8)	59.0	(-3.5)	-27.5	(+2.9)	-38.5	(+7.3)
Slovakia	20.0	(+7.8)	9.0	(+4.9)	57.8	(+8.8)	45.5	(+18.4)	22.2	(-16.6)	45.5	(-23.3)	-2.2	(+24.4)	-36.5	(+28.2)
Eurozone	81.1	(-4.4)			13.2	(-1.3)			5.7	(+5.7)			75.4	(-10.1)		

Long-term interest rates	increase				no change				decrease				balance			
	[abs.]		[rel.]		[abs.]		[rel.]		[abs.]		[rel.]		[abs.]		[rel.]	
Croatia	35.3	(-4.3)	25.7	(+4.5)	47.1	(+1.3)	42.9	(+0.3)	17.6	(+3.0)	31.4	(-4.8)	17.7	(-7.3)	-5.7	(+9.3)
Czech Republic	63.4	(+6.7)	30.0	(+2.3)	26.8	(-9.0)	55.0	(+1.8)	9.8	(+2.3)	15.0	(-4.1)	53.6	(+4.4)	15	(+6.4)
Hungary	13.3	(+1.3)	13.3	(+4.8)	17.8	(-6.2)	8.9	(+0.4)	68.9	(+4.9)	77.8	(-5.2)	-55.6	(-3.6)	-64.5	(+10.0)
Poland	43.9	(+11.9)	27.5	(+14.7)	36.6	(-15.4)	50.0	(+1.1)	19.5	(+3.5)	22.5	(-15.8)	24.4	(+8.4)	5	(+30.5)
Romania	15.1	(-1.5)	14.7	(+6.4)	39.4	(-1.1)	47.1	(+8.2)	45.5	(+2.6)	38.2	(-14.6)	-30.4	(-4.1)	-23.5	(+21.0)
Slovakia	41.5	(+3.5)	16.7	(+10.2)	39.0	(-11.0)	59.5	(-1.4)	19.5	(+7.5)	23.8	(-8.8)	22.0	(-4.0)	-7.1	(+19.0)
Germany	47.8	(-2.2)			37.0	(-3.7)			15.2	(+5.9)			32.6	(-8.1)		

Stock market indices	increase		no change		decrease		balance	
EURO STOXX 50	62.5	(-5.5)	25.0	(-1.0)	12.5	(+6.5)	50.0	(-12.0)
ATX (Austria)	63.7	(-8.1)	23.8	(+1.6)	12.5	(+6.5)	51.2	(-14.6)
NTX (CEE)	75.0	(-5.0)	22.7	(+7.1)	2.3	(-2.1)	72.7	(-2.9)
CROBEX (Croatia)	58.1	(-17.9)	25.6	(+1.6)	16.3	(+16.3)	41.8	(-34.2)
PX 50 (Czech Rep.)	57.8	(-12.2)	40.0	(+16.0)	2.2	(-3.8)	55.6	(-8.4)
BUX (Hungary)	58.0	(-14.6)	36.0	(+16.4)	6.0	(-1.8)	52.0	(-12.8)
WIG (Poland)	65.2	(-11.4)	28.3	(+11.3)	6.5	(+0.1)	58.7	(-11.5)
BET (Romania)	68.1	(-14.2)	20.5	(+7.2)	11.4	(+7.0)	56.7	(-21.2)
SAX (Slovakia)	54.7	(-13.5)	40.5	(+15.5)	4.8	(-2.0)	49.9	(-11.5)
SBI 20 (Slovenia)	48.7	(-37.4)	38.5	(+24.6)	12.8	(+12.8)	35.9	(-50.2)

Exchange rates (vs. Euro)	appreciate		no change		depreciate		balance	
Kuna (Croatia)	40.4	(+3.1)	44.7	(+5.7)	14.9	(-8.8)	25.5	(+11.9)
Koruna (Czech Rep.)	44.9	(+7.9)	40.8	(-9.2)	14.3	(+1.3)	30.6	(+6.6)
Forint (Hungary)	34.0	(+4.2)	41.5	(-9.4)	24.5	(+5.2)	9.5	(-1.0)
Zloty (Poland)	55.1	(+6.0)	28.6	(-11.0)	16.3	(+5.0)	38.8	(+1.0)
Lei (Romania)	57.8	(+14.4)	22.2	(-15.5)	20.0	(+1.1)	37.8	(+13.3)
Koruna (Slovakia)	52.2	(+6.6)	43.5	(+1.4)	4.3	(-8.0)	47.9	(+14.6)
US-Dollar	32.1	(-1.8)	26.4	(+8.5)	41.5	(-6.7)	-9.4	(+4.9)

Note: 78 Financial experts participated in the June survey which was conducted during the period 06/06/07-06/25/07. Analysts were asked about their expectations for the next 6 months. Numbers displayed are percentages (month-over-month percentage point changes compared to the survey in May in parentheses). Balances refer to the differences between positive and negative assessments.

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