

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 market experts about their assessment and expectations with regard to economic and financial market data. The results of the present survey conducted between 2 and 27 August 2007 are published in this issue of the "Financial Market Report CEE", September 2007. 70 financial market experts participated in this month's survey.

## Experts expect no change of the business cycle development in the CEE countries

Within the next six months, the financial market experts participating in the survey carried out by the ZEW, the Centre for European Economic Research, Mannheim, which is supported by Erste Bank der oesterreichischen Sparkassen, Vienna, expect no change of the economic development for the Cen-

tral and Eastern European Countries. The survey participants assess the current economic situation for this region as good. For Austria, negative economic expectations predominate, whereas the economic situation is assessed as positive on balance.

### Economic Outlook for CEE countries, Austria and the Eurozone

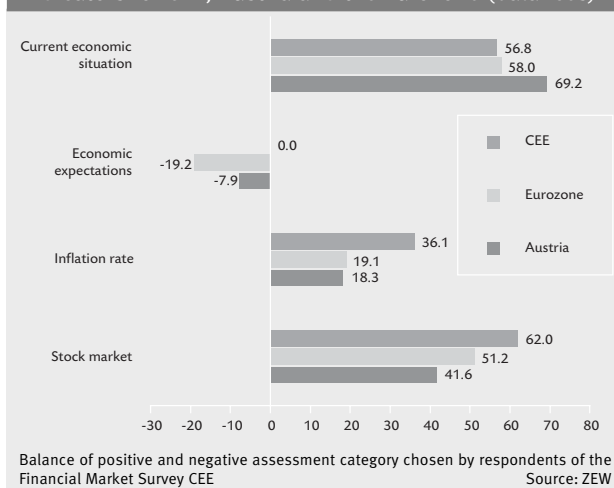
In the August survey, the ZEW-Erste Bank Sentiment Indicator CEE that gives the balance of positive and negative assessments for the economic development within the next six months, has dropped once again (-8.8 points) and now has a value of 0 points. The share of experts with optimistic expectations with regard to the economic development over the next six months balances the share of those who forecast a worsening. However, the majority of experts, 70.8 percent, does not expect a change. For Austria, the balance for the economic expectations has declined again (-0.6 points). This development can be attributed to the fact that the share of experts forecasting an improving economic development has decreased more strongly than the share expecting a worsening. Both categories lost in favour of the percentage of experts that expect no change at all. The economic expectations for the Eurozone have also worsened, the balance declined by 4.9 points.

The majority of survey participants assesses the current economic situation in Austria as „good“, whereas the balance has decreased by 6.4 points in favour of the share of experts evaluating the state of the economy as normal. Compared to this assessment, the balance for the current economic situation in CEE countries has decreased by 2.8 points. The balance that displays the assessment of the survey participants with regard to the economic situation of the Eurozone has been affected by the largest decline of 14.7 points.

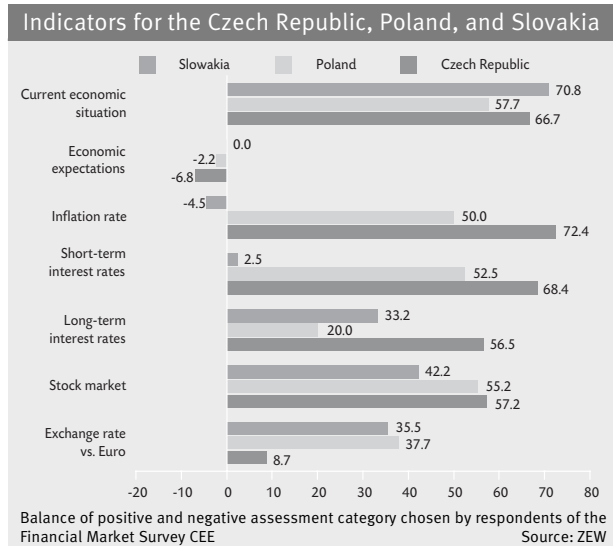
The inflation expectations of financial market experts have considerably declined for Austria and the Eurozone,

whereas the balance for the CEE countries is almost unchanged. The financial market experts give a uniform picture for the stock market development. For all three regions, the survey participants expect an increase of the stock market indices over the next six months. However, the balances have developed in different directions compared to the July survey. The balance for the Euro Stoxx 50 has increased, while the balances for the NTX and the ATX have decreased. But the share of experts forecasting a rise of the respective stock market index still outweighs the share expecting a decrease of the index to a considerable amount.

Indicators for CEE, Austria and the Eurozone (balances)



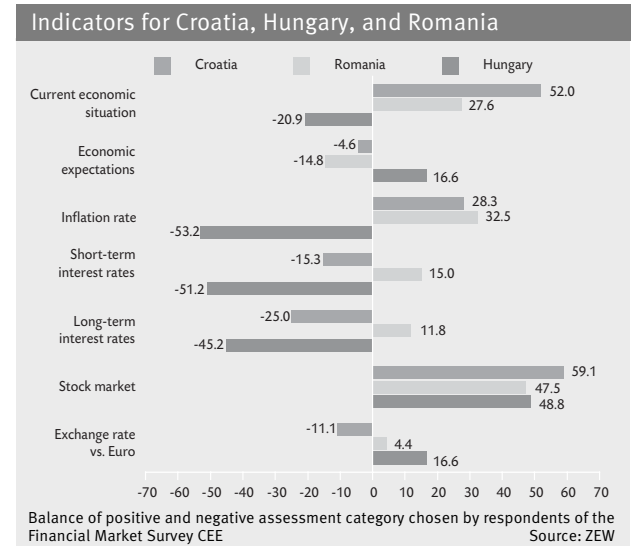
## Czech Republic, Poland, and Slovakia: Expectations for further development have worsened



The financial market experts assess the current economic situation in the Czech Republic, Poland and Slovakia as „good“. These evaluations come from a clear majority of experts. However, the economic expectations have worsened compared to last month's survey, especially for Slovakia where the balance decreased by 15.4 points. But still 81.8 percent of the respondents forecast that the good situation of the Slovakian economy will not change over the next six months. For the two other economies, the change of the balance is not as dramatic with -3 points for the Czech Republic and -2.1 points for Poland. Once again, the majority of experts does not expect a change in business cycle development over the next half year. With the decreasing optimism for the economic development, the inflation expectations of experts have decreased too for Slovakia. In August, the experts forecast a decreasing inflation rate on balance. For the other two economies, rising inflation expectations predominate.

The balances for the expected interest rate development draw the following picture: For Slovakia, the majority of experts anticipates unchanged interest rates. In contrast to this, the respondents expect the long-term interest rates to increase; the balance is clearly positive with 33.2 points. For Poland, the balance indicates higher short-term and long-term interest rates in six months where the expectations for the rise are more pronounced at the long end of the term structure. For the Czech Republic, the difference between the balances for the short-term and long-term interest rates is not as strongly marked. The experts' expectations with regard to the stock market development are clearly positive. The balance for the PX 50 has gained 11 points compared to the July survey and is now higher than the balance for the WIG index which has gained 2.2 points. Again, the experts' forecast for the development of the SAX changed in the opposite direction, but the share of experts projecting the stock market index to rise still outweighs the share of experts with pessimistic expectations.

## Croatia, Hungary, and Romania: Optimism for economic development in the next six months has decreased



Hungary, Romania and Croatia show the lowest balances for the assessment of the current economic situation. This is especially true for Hungary which is the only country with a negative balance matching the negative economic situation. Even though the experts anticipate the Hungarian economy to improve over the next six months, the balance for economic expectations has decreased compared to the July survey. For Romania and Croatia, the survey participants expect a worsening of the economic development. Inflation expectations for Romania have picked up again; the balance has increased by 15.1 points compared to the previous month's survey. Also, the inflation expectations for Croatia are on the upside but lower than last month. Only for Hungary, the experts project a lower inflation rate in six months on balance (-53.2 points) and with a broad majority of 68.1 percent.

The financial market experts forecast the short- and long-term interest rates to develop in the same direction for each of the three countries. For Hungary, they expect both short-term and long-term interest rates to decrease. The experts also project decreasing interest rates for Croatia, however, the balances are not as pronounced as for Hungary. Only for Romania, the participants' expectations for rising interest rates in the long-term and short-term still predominate. With regard to the stock market development, the financial market experts are optimistic on balance and there are no pronounced differences between the balances for the stock market indices of Hungary and Romania. The positive balance for the CROBEX is even higher. However, the balances have all decreased compared to the previous month's survey. Concerning exchange rate expectations, survey participants expect the Kuna to depreciate on balance, whereas the expectations for the other two currencies point to an appreciation with regard to the Euro. Here, we see large swings of the balances compared to the previous month's survey; the balances for the Croatian and Hungarian currency had the opposite sign.

## Special Question: Expectations Formation Concerning Macroeconomic Development

In this month’s special question, the financial market experts were asked to assess how strongly certain indicators influence their expectations formation with regard to the macroeconomic development within six months. For each variable, the experts were given the choice between a low, middle or strong impact (see Figure 4a, b and c respectively).

A majority of financial market experts, 53.85 percent each, indicates that industrial production and the economic situation in the EU have a strong impact on their expectations formation with regard to the macroeconomic development. The results show that these indicators are the most important for evaluating the economic development of an economy. The US economy with its vast demand for imported goods is often seen as fuelling the world economy, but clearly, the CEE states are more dependent on the economic situation in the EU. This view is displayed in the participants’ answers. For the influence of the US economy, the assessment of the financial mar-

ket experts is more or less evenly spread across the categories. Also, financial market experts judge monetary policy decisions of central banks as being an important influence on expectations formation with a share of 92 percent opting for a strong or medium influence. Whereas the monetary transmission mechanism starts at short-term interest rates, the usefulness of the whole spectrum of interest rates is analysed time and again in predicting the economic development in the academic literature. Only very few participants (2.04 percent) see the term structure as a strong variable in shaping their expectations, 48.98 percent answered “middle” and “low” respectively. Also, the experts rate the stock market development as a not especially important factor in forming their expectations; approximately 81 percent of the respondents say it has only medium or low importance.

Exports also belong to the group of indicators influencing macroeconomic expectations formation in a strong way. Many of the participants (45.31 percent) consider exports as a strong influence on their expectations formation. The strong influence of the EU economy on the CEE countries is also confirmed when looking at the importance of the exchange rate for influencing expectations formation. While the medium category received the highest share of answers for the exchange rate versus the Euro (53.3 percent), 45 percent of experts rate the influence of the exchange rate versus the Dollar as low.

The remaining indicators – incoming orders, retail sales, the unemployment rate, capacity utilisation, the oil price and consumer sentiment – prove that they are important indicators for assessing the future macroeconomic development. However, the experts see all of them having average importance in forming economic expectations. Except for capacity utilisation, the answers are biased in direction of higher importance. For the unemployment rate, the categories of low and strong influence on expectations formation are equally occupied (25.4 percent).

Figure 4a: Percentage of experts assessing the influence of the variable on expectations formation as strong.

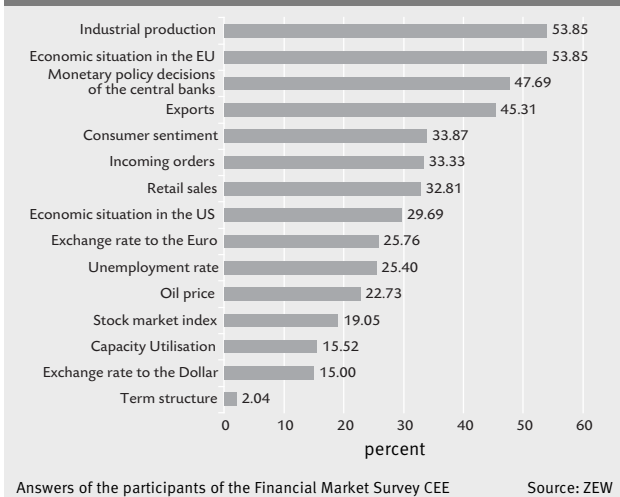


Figure 4b: Percentage of experts assessing the influence of the variable on expectations formation as medium.

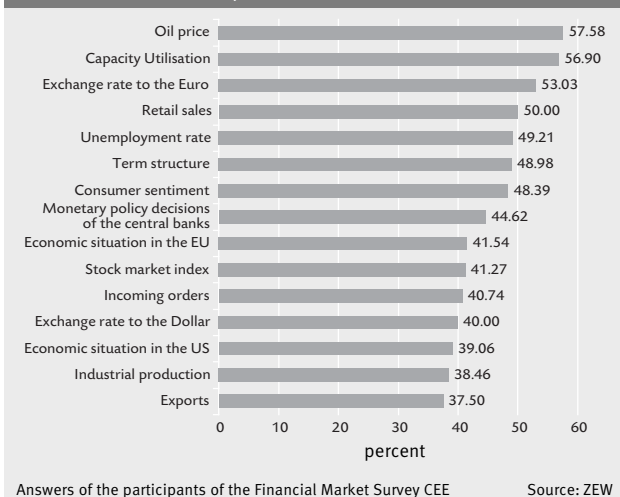
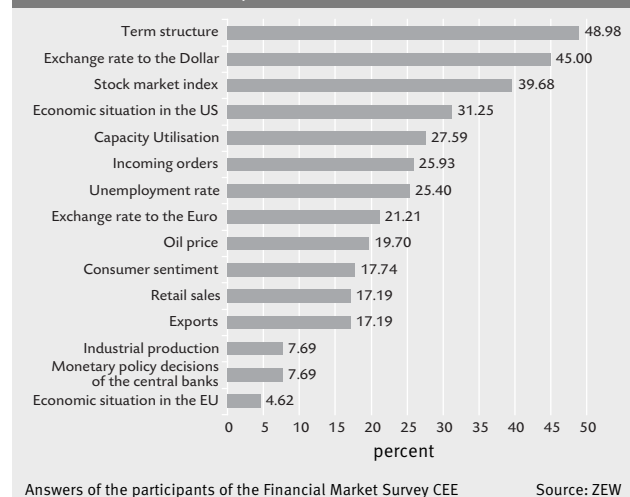


Figure 4c: Percentage of experts assessing the influence of the variable on expectations formation as low.



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

<b>Current economic situation</b>	<b>good</b>		<b>acceptable (normal)</b>		<b>bad</b>		<b>balance</b>									
Austria	69.2	(-6.4)	30.8	(+6.4)	0.0	(+/-0.0)	69.2	(-6.4)								
Croatia	54.0	(-5.3)	44.0	(+3.3)	2.0	(+2.0)	52.0	(-7.3)								
Czech Republic	66.7	(+1.8)	33.3	(-1.8)	0.0	(+/-0.0)	66.7	(+1.8)								
Hungary	8.3	(-2.0)	62.5	(-1.3)	29.2	(+3.3)	-20.9	(-5.3)								
Poland	64.4	(-2.9)	28.9	(-2.0)	6.7	(+4.9)	57.7	(-7.8)								
Romania	42.5	(-5.5)	42.6	(+0.6)	14.9	(+4.9)	27.6	(-10.4)								
Slovakia	72.9	(-3.0)	25.0	(+2.8)	2.1	(+0.2)	70.8	(-3.2)								
CEE	58.8	(-2.6)	39.2	(+2.4)	2.0	(+0.2)	56.8	(-2.8)								
Eurozone	58.0	(-14.7)	42.0	(+14.7)	0.0	(+/-0.0)	58.0	(-14.7)								
<b>Economic expectations</b>	<b>improve</b>		<b>no change</b>		<b>worsen</b>		<b>balance</b>									
Austria	7.9	(-4.3)	76.3	(+8.0)	15.8	(-3.7)	-7.9	(-0.6)								
Croatia	13.6	(-6.0)	68.2	(+1.5)	18.2	(+4.5)	-4.6	(-10.5)								
Czech Republic	8.8	(-4.1)	75.6	(+5.2)	15.6	(-1.1)	-6.8	(-3.0)								
Hungary	43.7	(-4.5)	29.2	(+3.3)	27.1	(+1.2)	16.6	(-5.7)								
Poland	20.0	(+3.7)	57.8	(-9.5)	22.2	(+5.8)	-2.2	(-2.1)								
Romania	19.2	(-6.8)	46.8	(-7.2)	34.0	(+14.0)	-14.8	(-20.8)								
Slovakia	9.1	(-15.9)	81.8	(+16.4)	9.1	(-0.5)	0.0	(-15.4)								
CEE	14.6	(-4.7)	70.8	(+0.6)	14.6	(+4.1)	0.0	(-8.8)								
Eurozone	8.5	(-4.0)	63.8	(+3.1)	27.7	(+0.9)	-19.2	(-4.9)								
<b>Inflation rate</b>	<b>increase</b>		<b>no change</b>		<b>decrease</b>		<b>balance</b>									
Austria	23.6	(-10.6)	71.1	(+12.6)	5.3	(-2.0)	18.3	(-8.6)								
Croatia	34.8	(-6.9)	58.7	(+8.7)	6.5	(-1.8)	28.3	(-5.1)								
Czech Republic	74.5	(+0.5)	23.4	(+3.0)	2.1	(-3.5)	72.4	(+4.0)								
Hungary	14.9	(-4.8)	17.0	(+6.3)	68.1	(-1.5)	-53.2	(-3.3)								
Poland	59.1	(+0.6)	31.8	(-4.0)	9.1	(+3.4)	50.0	(-2.8)								
Romania	46.5	(+3.0)	39.5	(+9.1)	14.0	(-12.1)	32.5	(+15.1)								
Slovakia	11.1	(-14.4)	73.3	(+16.4)	15.6	(-2.0)	-4.5	(-12.4)								
CEE	42.5	(+0.5)	51.1	(-0.9)	6.4	(+0.4)	36.1	(+0.1)								
Eurozone	25.5	(-15.2)	68.1	(+18.1)	6.4	(-2.9)	19.1	(-12.3)								
<b>Short-term interest rates</b>	<b>increase</b>		<b>no change</b>		<b>decrease</b>		<b>balance</b>									
	[abs.]	[rel.]	[abs.]	[rel.]	[abs.]	[rel.]	[abs.]	[rel.]								
Croatia	10.3	(-22.2)	10.9	(-18.9)	64.1	(+21.6)	45.9	(+5.4)	25.6	(+0.6)	43.2	(+13.5)	-15.3	(-22.8)	-32.3	(-32.4)
Czech Republic	70.8	(-8.0)	26.3	(-16.5)	26.8	(+7.7)	39.5	(+8.5)	2.4	(+0.3)	34.2	(+8.0)	68.4	(-8.3)	-7.9	(-24.5)
Hungary	20.9	(+7.2)	10.0	(-2.7)	7.0	(-4.8)	17.5	(+4.7)	72.1	(-2.4)	72.5	(-2.0)	-51.2	(+9.6)	-62.5	(-0.7)
Poland	62.5	(-3.5)	34.3	(+0.2)	10.0	(+7.9)	51.4	(-0.9)	10.0	(+7.9)	14.3	(+0.7)	52.5	(-11.4)	20.0	(-0.5)
Romania	37.5	(+8.6)	43.3	(+13.3)	40.0	(+17.8)	18.9	(-11.1)	22.5	(-26.4)	37.8	(-2.2)	15.0	(+35.0)	5.5	(+15.5)
Slovakia	17.1	(-2.1)	15.8	(+3.9)	68.3	(+6.6)	50.0	(-11.9)	14.6	(-4.5)	34.2	(+8.0)	2.5	(+2.4)	-18.4	(-4.1)
Eurozone	52.1	(-6.9)			37.5	(+3.6)			10.4	(+3.3)			41.7	(-10.2)		
<b>Long-term interest rates</b>	<b>increase</b>		<b>no change</b>		<b>decrease</b>		<b>balance</b>									
	[abs.]	[rel.]	[abs.]	[rel.]	[abs.]	[rel.]	[abs.]	[rel.]								
Croatia	11.1	(-28.9)	6.1	(-30.3)	52.8	(+9.9)	39.4	(+6.1)	36.1	(+19.0)	54.5	(+24.2)	-25.0	(-47.9)	-48.4	(-54.5)
Czech Republic	61.6	(-3.5)	22.2	(-18.4)	33.3	(+10.0)	50.0	(+14.9)	5.1	(-6.5)	27.8	(+3.5)	56.5	(+3.0)	-5.6	(-21.9)
Hungary	16.7	(+1.8)	10.5	(-5.0)	21.4	(+0.1)	21.1	(+12.2)	61.9	(-1.9)	68.4	(-7.2)	-45.2	(+3.7)	-57.9	(+2.2)
Poland	40.0	(-4.2)	22.2	(-4.6)	40.0	(-6.5)	41.7	(-24.2)	20.0	(+10.7)	36.1	(+28.8)	20.0	(-14.9)	-13.9	(-33.4)
Romania	35.3	(+1.0)	41.2	(+11.8)	41.2	(+12.3)	23.5	(-3.0)	23.5	(-13.3)	35.3	(-8.8)	11.8	(+14.3)	5.9	(+20.6)
Slovakia	43.5	(+16.0)	11.1	(-5.6)	46.2	(-13.8)	58.3	(-5.6)	10.3	(-2.2)	30.6	(+11.2)	33.2	(+18.2)	-19.5	(-16.8)
Germany	47.6	(+4.4)			50.0	(+10.8)			2.4	(-15.2)			45.2	(+19.6)		
<b>Stock market indices</b>	<b>increase</b>		<b>no change</b>		<b>decrease</b>		<b>balance</b>									
EURO STOXX 50	60.5	(+5.4)	30.2	(-2.5)	9.3	(-2.9)	51.2	(+8.3)								
ATX (Austria)	55.5	(-5.9)	30.6	(+5.6)	13.9	(+0.3)	41.6	(-7.6)								
NTX (CEE)	69.1	(-4.3)	23.8	(+5.4)	7.1	(-1.1)	62.0	(-3.2)								
CROBEX (Croatia)	68.2	(-6.7)	22.7	(+3.9)	9.1	(+2.8)	59.1	(-9.5)								
PX 50 (Czech Rep.)	64.3	(+6.6)	28.6	(-2.2)	7.1	(-4.4)	57.2	(+11.0)								
BUX (Hungary)	63.4	(-4.5)	22.0	(+5.0)	14.6	(-0.5)	48.8	(-4.0)								
WIG (Poland)	71.0	(+3.7)	13.2	(-5.2)	15.8	(+1.5)	55.2	(+2.2)								
BET (Romania)	62.5	(-2.8)	22.5	(+0.8)	15.0	(+2.0)	47.5	(-4.8)								
SAX (Slovakia)	52.7	(-6.8)	36.8	(+5.8)	10.5	(+1.0)	42.2	(-7.8)								
SBI 20 (Slovenia)	48.5	(-1.5)	42.9	(+5.4)	8.6	(-3.9)	39.9	(+2.4)								
<b>Exchange rates (vs. Euro)</b>	<b>appreciate</b>		<b>no change</b>		<b>depreciate</b>		<b>balance</b>									
Kuna (Croatia)	20.0	(-14.7)	48.9	(+14.2)	31.1	(+0.5)	-11.1	(-15.2)								
Koruna (Czech Rep.)	32.6	(-10.8)	43.5	(+5.8)	23.9	(+5.0)	8.7	(-15.8)								
Forint (Hungary)	35.4	(+16.9)	45.8	(-11.6)	18.8	(-5.3)	16.6	(+22.2)								
Zloty (Poland)	55.5	(-1.9)	26.7	(-6.6)	17.8	(+8.5)	37.7	(-10.4)								
Lei (Romania)	40.0	(-3.4)	24.4	(-12.6)	35.6	(+16.0)	4.4	(-19.4)								
Koruna (Slovakia)	42.2	(-8.8)	51.1	(+8.2)	6.7	(+0.6)	35.5	(-9.4)								
US-Dollar	34.0	(+5.5)	21.3	(-9.1)	44.7	(+3.6)	-10.7	(+1.9)								

Note: 70 Financial experts participated in the August survey which was conducted during the period 08/02/07-08/27/07. 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 July in parentheses). Balances refer to the differences between positive and negative assessments.