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Financial Market Report CEE

Volume 2 · November 2008

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

ZEW, the Centre for European Economic Research, Mannheim, and Erste Group Bank AG, Vienna, carry out a monthly survey for Central and Eastern Europe, Austria, as well as the Eurozone asking financial market experts for their assessments and expectations with regard to economic and financial market data. The results of the present survey, conducted between September 25 and October 13, 2008, are published in the November 2008 issue of the "Financial Market Report CEE". In this month's survey 61 financial market experts participated.

Economic expectations for CEE diminish in the maelstrom of the financial crisis

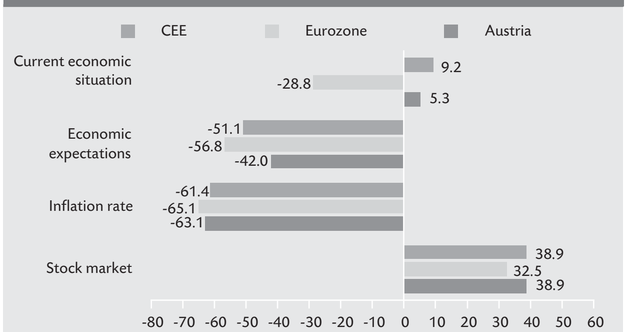
The intensified crisis of confidence in the financial systems and the concerns about possible implications for the real economies have a negative impact on the economic expectations for the CEE-region. The CEE sentiment indicator drops by 20.5 points to currently minus 51.1 points. The questioned financial market experts perceive higher downside risks for the economic growth in the CEE-region, however, the resolved governments' financial rescue plans as well as the relative high stability of the CEE domestic financial systems should restore normality to markets and sentiments. The current economic situation is evaluated by 81.4 percent of the analysts as acceptable and the balance declines to 9.2 points.

Economic outlook for CEE countries, Austria and the Eurozone

The ZEW-Erste Group Bank Sentiment Indicator CEE that shows the balance of positive and negative assessments of the economic outlook within the next six months, deteriorates by 20.5 points in the current survey and now stands at minus 51.1 points. The indicator for Austria notices the slightest loss dropping by 5.5 points to minus 42.0 points. The balance for the Eurozonestill shows one of the lowest values within the analysed economies (minus 56.8 points).

The current economic situation in Central and Eastern Europe is regarded as "acceptable" by 81.4 percent of the financial experts. 13.9 percent of the analysts characterise the situation as "good" and only 4.7 percent as "bad". Accordingly, mainly a shift of the evaluation on the present economic circumstances from "good" to "neutral" takes place for all analysed countries and the CEE-region as a whole in October. The assessment of the current economic situation in Austria has changed least, decreasing marginally by 4.0 points to 5.3 points. In line with the results of the previous months, the present state of the business activity in the Eurozone is viewed increasingly critically. The corresponding balance declines to minus 28.8 points.

Indicators for CEE, Austria and the Eurozone (balances)



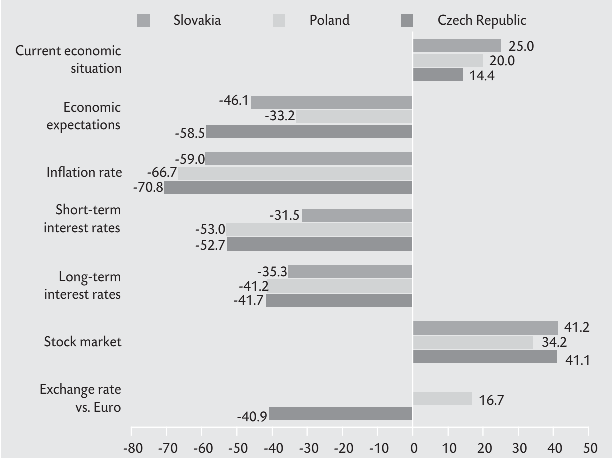
Balance of positive and negative assessment category chosen by respondents of the Financial Market Survey CEE
Source: ZEW

For the next six months the experts anticipate a further mitigation of the inflationary pressure in the CEE-region. The respective indicator drops by 2.3 points reaching minus 61.4 points. Nearly 70 percent of the survey participants expect further decreases of the inflation rates in the region. According to the financial market analysts, upside inflationary risks in the Eurozone have recently decreased further. The respective balance falls 20.0 points, now standing at minus 65.1 points.

After the cut of the main refinancing rate by the ECB fewer experts expect further reductions. The balance for the short-term interest rates in the Eurozone rises slightly by 3.9 points. Nonetheless, 63.4 percent of the financial experts anticipate a further downward change of the ECB key interest rate within the next six months. Despite the turmoil on the international financial markets the expectations of the experts concerning the development of the stock indices in the CEE countries have changed insignificantly. In line with the results of the previous months, a large majority of the survey participants predict – at current price levels – rising share prices in the region. The respective balance for the CEE index (NTX) drops slightly by 4.9 to 38.9 points. The balance for the Austrian index (ATX) stands at 38.9 points after a moderate decrease by 1.1 points.

Czech Republic, Poland and Slovakia: further lessening of the inflation risks expected

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

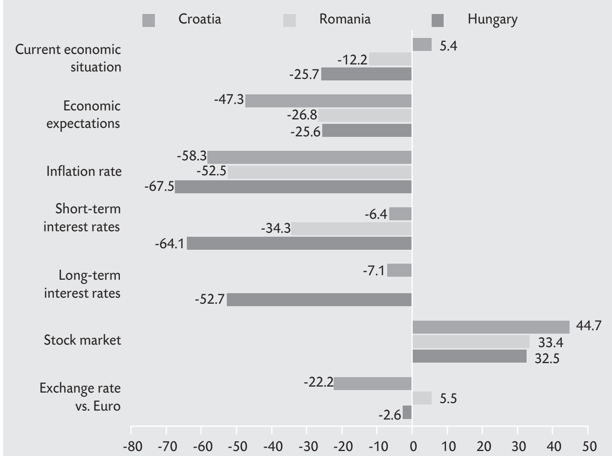
In the October survey the analysts are more cautious in their assessment of the current economic conditions in the Czech Republic, Poland and Slovakia as well. While most experts regard the business situation in the three countries as “good” in September, a shift of the evaluation from “good” to “neutral” takes place this month. Though the corresponding indicators decline by more than 30.0 points in October, they remain positive. The Czech balance now stands at 14.4 points. The Polish and Slovak economies are rated with 20.0 and 25.0 points respectively. In the current survey the experts increasingly anticipate a slowdown of the economic growth in the three countries. The balance capturing the economic expectations for the Czech Republic drops by 16.7 points to currently minus 58.8 points, which is the lowest value among all analysed countries. From the participants’ view, the future perspectives for Poland and Slovakia worsen by 9.4 and 18.8 points, reaching minus 33.2 and minus 46.1 points.

For the coming six months the overwhelming majority of the analysts anticipate a moderation of the inflation pressure within the three states. In line with this, the financial experts spot a clear tendency towards falling interest rates in the short- as well as in the long-run, as contractive monetary policy does no longer seem to be necessary.Notwithstanding the uncertainty on the global stock markets, the analysts’ view on the equity indices in the Czech Republic, Poland and Slovakia remains nearly as optimistic as in the previous month. The corresponding balances show only marginal changes between 2.1 and 4.3 points, now standing at 41.1 points, 34.2 points and 41.2 points respectively.

With regard to the expected exchange rates versus the Euro, the financial experts’ assessments of the Czech currency are most striking. The share of the analysts anticipating a depreciation of the Koruna increased markedly by 24.9 percentage points, leading to a decline of the balance to currently minus 40.9 points.

Hungary, Romania and Croatia: economic expectations worsen, but no mood of crisis

Indicators for Croatia, Hungary, and Romania



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

The balances indicating the experts’ assessment of the current economic situation in Hungary, Romania and Croatia decline in October by 23.7 points, 35.1 points and 26.4 points respectively. However, a clear majority of the respondents still regard the momentous conditions in the three countries as normal and the corresponding balance for Croatia even remains slightly positive.

The analysts’ growing concerns about the future economic development in the three countries are reflected in the declining balances. In particular with regard to the prospects for Croatia the analysts are more doubtful, as the respective indicator drops by 34.8 to minus 47.3 points. This is the largest decrease in this category. Having been the only ones to exhibit positive values in the previous months, the economic expectations for Hungary worsen by 25.7 to minus 25.6 points. Nonetheless, more than half of the participants (55.8 percent) still anticipate an improvement of the economic conditions or an unchanged business cycle. As a consequence, Hungary remains the country featuring the brightest future perspectives among all analysed countries. It is closely followed by Romania (minus 26.8 points).

In analogy to the results of the previous months, the financial experts predominantly forecast declining inflation rates for the three countries against the background of decreasing commodity prices worldwide.

Correspondingly, a clear majority of the analysts expect falling interest rates. In the case of Croatia the participants predominantly expect no adjustment.

Despite the current turmoil on the financial markets worldwide, the respondents remain optimistic concerning the anticipated share prices in the three countries. The balances which show the stock market expectations for Hungary, Romania and Croatia close at high positive levels, namely 32.5 points, 33.4 points and 44.7 points.

Special question: Financial market turmoil

During the last weeks the landscape of world finance changed dramatically. The uncertainty on the capital markets further increased, leading to sharp reductions in the values of equities and tighter liquidity. More and more financial institutions, such as the world's largest insurance company AIG, the German Hypo Real Estate and the Benelux bank Fortis, were caught in the maelstrom of the credit crisis and had to be saved by extensive governmental rescue packages.

The new dimension of the credit crisis brought many bankers, politicians and economists to call for public aid and increased regulation on the financial markets. Many governments worldwide decided already financial rescue plans and further steps to overcome the financial crisis are intensively discussed.

Against this background we asked the financial market experts within this month's issue of the special question to evaluate different potential measures to cope with the credit crisis. The majority of the respondents (83 percent) regard the governmental rescue packages as "good" or "very good" solutions against the liquidity and confidence crunch within the banking sector.

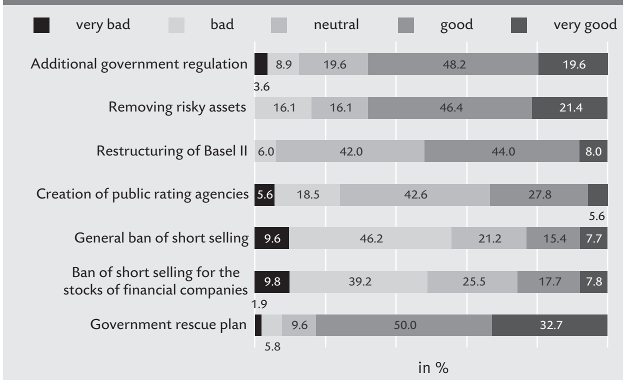
According to most participants, additional government regulation of the financial sector is needed for stabilising the financial markets, too. 68 percent of the experts questioned in the survey spot a positive impact of this measure.

Still, the financial experts predominantly disapprove of generally banning short-selling. Short-selling is often demanded in the media at present, as this practise may precipitate a slide in share values putting companies that are affected by the credit crisis under further pressure. 23 percent of the analysts assent to this view. The majority of the respondents (56 percent), however, take the view that short-selling is rather the symptom than the cause of the financial turmoil. This holds for the interdiction of the short-selling for stocks of financial companies only, too. Although, the acceptance among the analysts is slightly higher here.

A slight majority of the experts, namely 52 percent, recommend a restructuring of the Basel II international banking regulatory framework, which has been applied in the European Union since January 1, 2007. The rules on capital are often criticised by economists for having a procyclical effect. Aas banks must back their credits with more equity when they face greater risks and this may require them to lend less during a recession or a credit crunch, which could aggravate the downturn..

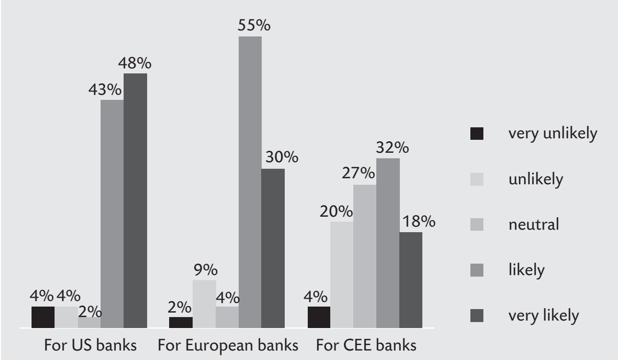
Additionally, we asked the analysts to evaluate whether public or independent rating agencies are appropriate and needed. The current ones are sometimes accused of being jointly responsible for the extent of the credit crisis having passed judgements on mortgage-backed securities. At the moment the reproach circulates that rating agencies have not evaluated these financial products critically enough, being in a customer relationship with the institutions they rate. However, the majority of the financial experts share the view that these accusations are not or only partly justified, considering the creation of public rating agencies to be a very bad, bad or neutral method to overcome the financial turmoil.

Figure A: How do you evaluate the following measures to overcome the financial crisis?



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

Figure B: Do you expect any further concentration in the banking sector as a result from the new dimension of the financial crisis?



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

Still, 34 percent of the respondents are in favour of public rating agencies. Finally, we wanted to find out, whether removing risky assets from the financial markets, as practised in the US, is an effective solution to the credit crunch targeting at the stabilisation of the banking system. Most experts (67 percent) clearly support this policy regarding it to be good or even very good in this context.

Within the second part of this month's special question we lay the focus upon the consequences for the banking sector in America, Europe and the CEE resulting from the current turmoil. Is further concentration to be expected?

With regard to US and European banks, overwhelming majorities of 91 and 85 percent respectively, share this view. The proportion of the respondents describing the probability of further concentration with very likely (48 percent) is highly pronounced in the case of the US American financial system, whereas, according to the experts, mergers between banks in Europe are rather likely (55 percent).

As to the CEE-region, half of the financial analysts anticipate an increased concentration in the banking sector as a result of the credit crisis. Nonetheless, a significant share of the participants, namely 24 percent, expects no adjustments.

Mariela Borell, Oliver Herrmann

ZEW-Financial Market Survey: October 2008

Current economic situation	good		acceptable (normal)		bad		balance	
Austria	15.8	(-0.5)	73.7	(-3.0)	10.5	(+3.5)	5.3	(-4.0)
Croatia	10.8	(-23.4)	83.8	(+20.4)	5.4	(+3.0)	5.4	(-26.4)
Czech Republic	21.5	(-25.5)	71.4	(+20.4)	7.1	(+5.1)	14.4	(-30.6)
Hungary	6.9	(-15.1)	60.5	(+6.5)	32.6	(+8.6)	-25.7	(-23.7)
Poland	30.0	(-25.3)	60.0	(+17.4)	10.0	(+7.9)	20.0	(-33.2)
Romania	12.2	(-23.2)	63.4	(+11.3)	24.4	(+11.9)	-12.2	(-35.1)
Slovakia	30.0	(-37.4)	65.0	(+36.7)	5.0	(+0.7)	25.0	(-38.1)
CEE	13.9	(-24.1)	81.4	(+21.4)	4.7	(+2.7)	9.2	(-26.8)
Eurozone	4.5	(-3.5)	62.2	(-9.8)	33.3	(+13.3)	-28.8	(-16.8)

Economic expectations	improve		no change		worsen		balance	
Austria	10.6	(+8.1)	36.8	(-21.7)	52.6	(+13.6)	-42.0	(-5.5)
Croatia	8.3	(-1.7)	36.1	(-31.4)	55.6	(+33.1)	-47.3	(-34.8)
Czech Republic	4.9	(+2.9)	31.7	(-22.5)	63.4	(+19.6)	-58.5	(-16.7)
Hungary	18.6	(-3.9)	37.2	(-17.9)	44.2	(+21.8)	-25.6	(-25.7)
Poland	20.6	(+14.0)	25.6	(-37.4)	53.8	(+23.4)	-33.2	(-9.4)
Romania	17.1	(+4.3)	39.0	(-16.3)	43.9	(+12.0)	-26.8	(-7.7)
Slovakia	7.7	(+7.7)	38.5	(-34.2)	53.8	(+26.5)	-46.1	(-18.8)
CEE	8.9	(+4.8)	31.1	(-30.1)	60.0	(+25.3)	-51.1	(-20.5)
Eurozone	9.1	(+3.1)	25.0	(-1.0)	65.9	(-2.1)	-56.8	(+5.2)

Inflation rate	increase		no change		decrease		balance	
Austria	5.3	(-1.7)	26.3	(-13.2)	68.4	(+14.9)	-63.1	(-16.6)
Croatia	13.9	(+11.4)	13.9	(-3.6)	72.2	(-7.8)	-58.3	(+19.2)
Czech Republic	2.4	(-3.6)	24.4	(+4.4)	73.2	(-0.8)	-70.8	(-2.8)
Hungary	4.6	(-1.4)	23.3	(+9.3)	72.1	(-7.9)	-67.5	(+6.5)
Poland	5.1	(-5.5)	23.1	(+1.8)	71.8	(+3.7)	-66.7	(-9.2)
Romania	10.0	(-0.4)	27.5	(+12.9)	62.5	(-12.5)	-52.5	(+12.1)
Slovakia	5.1	(-6.0)	30.8	(-4.8)	64.1	(+10.8)	-59.0	(-16.8)
CEE	6.8	(-1.4)	25.0	(+0.5)	68.2	(+0.9)	-61.4	(-2.3)
Eurozone	7.0	(-2.8)	20.9	(-14.4)	72.1	(+17.2)	-65.1	(-20.0)

Short-term interest rates	increase				no change				decrease				balance			
	[abs.]		[rel.]		[abs.]		[rel.]		[abs.]		[rel.]		[abs.]		[rel.]	
Croatia	22.6	(+9.4)	33.3	(+10.5)	48.4	(-20.0)	56.7	(-17.6)	29.0	(+10.6)	10.0	(+7.1)	-6.4	(-1.2)	23.3	(+3.4)
Czech Republic	10.5	(+1.2)	24.4	(-13.1)	26.3	(-38.8)	45.9	(+3.4)	63.2	(+37.6)	29.7	(+9.7)	-52.7	(-36.4)	-5.3	(-22.8)
Hungary	12.8	(+6.2)	23.7	(+1.0)	10.3	(-20.1)	42.1	(+10.3)	76.9	(+13.9)	34.2	(-11.3)	-64.1	(-7.7)	-10.5	(+12.3)
Poland	8.8	(-0.5)	32.3	(-10.2)	29.4	(-38.0)	55.9	(+10.9)	61.8	(+38.5)	11.8	(-0.7)	-53.0	(-39.0)	20.5	(-9.5)
Romania	11.4	(-0.2)	33.3	(+11.3)	42.9	(+1.0)	36.4	(+2.3)	45.7	(-0.8)	30.3	(-13.6)	-34.3	(+0.6)	3.0	(+24.9)
Slovakia	17.1	(-21.3)	18.8	(-6.9)	34.3	(-4.2)	65.6	(+9.2)	48.6	(+25.5)	15.6	(-2.3)	-31.5	(-46.8)	3.2	(-4.6)
Eurozone	9.8	(+7.7)			26.8	(-11.5)			63.4	(+3.8)			-53.6	(+3.9)		

Long-term interest rates	increase				no change				decrease				balance			
	[abs.]		[rel.]		[abs.]		[rel.]		[abs.]		[rel.]		[abs.]		[rel.]	
Croatia	17.9	(+7.4)	25.9	(+9.2)	57.1	(+9.7)	55.6	(+11.2)	25.0	(-17.1)	18.5	(-20.4)	-7.1	(+24.5)	7.4	(+29.6)
Czech Republic	11.1	(-25.2)	17.6	(-18.1)	36.1	(+8.8)	55.9	(+15.4)	52.8	(+16.4)	26.5	(+2.7)	-41.7	(-41.6)	-8.9	(-20.8)
Hungary	10.5	(+8.4)	21.7	(+21.7)	26.3	(+6.7)	29.7	(+4.7)	63.2	(-15.1)	48.6	(-26.4)	-52.7	(+23.5)	-26.9	(+48.1)
Poland	14.7	(+7.9)	21.2	(+11.6)	29.4	(-2.4)	45.5	(+12.2)	55.9	(-5.5)	33.3	(-23.8)	-41.2	(+13.4)	-12.1	(+35.4)
Slovakia	5.9	(-1.4)	12.2	(+9.7)	52.9	(-10.5)	63.6	(-8.9)	41.2	(+11.9)	24.2	(-0.8)	-35.3	(-13.3)	-12	(+10.5)
Germany	17.5	(+6.6)			37.5	(-19.0)			45.0	(+12.4)			-27.5	(-5.8)		

Stock market indices	increase		no change		decrease		balance	
EURO STOXX 50	55.0	(-1.2)	22.5	(-6.7)	22.5	(+7.9)	32.5	(-9.1)
ATX (Austria)	61.1	(+3.6)	16.7	(-8.3)	22.2	(+4.7)	38.9	(-1.1)
NTX (CEE)	61.1	(+0.2)	16.7	(-5.3)	22.2	(+5.1)	38.9	(-4.9)
CROBEX (Croatia)	57.9	(-8.8)	28.9	(+6.7)	13.2	(+2.1)	44.7	(-10.9)
PX 50 (Czech Rep.)	59.0	(-0.1)	23.1	(-1.9)	17.9	(+2.0)	41.1	(-2.1)
BUX (Hungary)	57.5	(-10.6)	17.5	(+0.5)	25.0	(+10.1)	32.5	(-20.7)
WIG (Poland)	57.1	(-1.9)	20.0	(-0.5)	22.9	(+2.4)	34.2	(-4.3)
BET (Romania)	52.8	(-3.0)	27.8	(-0.1)	19.4	(+3.1)	33.4	(-6.1)
SAX (Slovakia)	55.9	(-0.6)	29.4	(+3.8)	14.7	(-3.2)	41.2	(+2.6)
SBI 20 (Slovenia)	49.9	(-10.6)	31.3	(+5.0)	18.8	(+5.6)	31.1	(-16.2)

Exchange rates (vs. Euro)	appreciate		no change		depreciate		balance	
Kuna (Croatia)	16.7	(-16.6)	44.4	(+8.5)	38.9	(+8.1)	-22.2	(-24.7)
Koruna (Czech Rep.)	12.9	(+1.8)	33.3	(-26.7)	53.8	(+24.9)	-40.9	(-23.1)
Forint (Hungary)	31.6	(+3.3)	34.2	(-22.3)	34.2	(+19.0)	-2.6	(-15.7)
Zloty (Poland)	38.9	(-0.6)	38.9	(+15.6)	22.2	(-15.0)	16.7	(+14.4)
Lei (Romania)	33.3	(+11.4)	38.9	(-9.9)	27.8	(-1.5)	5.5	(+12.9)
US-Dollar	51.2	(+6.3)	17.1	(-11.5)	31.7	(+5.2)	19.5	(+1.1)

Note: 61 Financial experts participated in the October survey which was conducted during the period 09/25/08-10/13/08. 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 September in parentheses). Balances refer to the differences between positive and negative assessments.

I M P R I N T

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