Central & Eastern European Strategy

3rd quarter 2016

Roller-coaster ride in Q3

- Limited economic effects from Brexit on CEE
- Brexit with limited impact on CEE assets
- More cautious outlook for CEE bond markets
- Liquidity supporting equities

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Central & Eastern European Strategy

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Explanation:
e … estimate (current year)
f … forecast
p … preliminary figures
n.v. … no value

Abbreviations

Currencies and Countries

ALL	Albanian lek
BAM	Bosnian marka
BGN	Bulgarian lev
BYR	Belarusian roubel
CZK	Czech koruna
HUF	Hungarian forint
HRK	Croatian kuna
PLN	Polish zloty
RON	Romanian leu
RSD	Serbian dinar
RUB	Russian rouble
TRY	Turkish lira
UAH	Ukrainian hryvnia

Economic abbreviations

%-chg	Percentage change (not in percentage points)
avg	average
bp	basis points
C/A	Current Account
CPI	Consumer Price Index
ECB	European Central Bank
FCY	Foreign Currency
FDI	Foreign Direct Investments
FX	Foreign Exchange
FY	Full year
GB	Government bond
GDP	Gross Domestic Product
HCPI	Harmonized Consumer Price Index
LCY	Local Currency
mmav	month moving average
mom	month on month
MP	Monetary policy
MPC	Monetary policy council
O/N	overnight rate
pp	percentage points
PMI	Purchasing Manager Index
PPI	Producer Price Index
QE	Quantitativ easing
qoq	quarter on quarter
qtd	quarter to date
REPO	Repurchase agreement
T/B	Trade Balance
ULC	Unit Labour Costs
UST	US Treasury bond
YC	yield curve
yoy	year on year
ytd	year-to-date

Sovereign Bond markets

CZGB	Czech local currency government bonds
HGB	Hungarian local currency government bonds
POLGB	Polish local currency government bonds
ROMGB	Romanian local currency government bonds
TURKGB	Turkish local currency government bonds

Stock Exchange Indices

ATX	Austrian stock index
BET	Romanian stock index
BIST National 100	Turkish stock index
BUX	Hungarian stock index
CROBEX10	Croatian stock index
PX	Czech stock index
MICEX	Russian stock index
WIG 20	Polish stock index

Fixed income indices

EMBIG	JP Morgan Emerging Markets Bond Index Global
CEMBI	JP Morgan Corporate Emerging Markets Bond Index

Equity related

DY	Dividend yield
EBIT	Earnings before interest and taxes
EBITDA	earnings before interest, taxes, depreciation, and amortization
EBT	earnings before taxes
EPS	earnings per share
EG	Earnings growth
LTG	Long term (earnings) growth
NIBD	Net interest bearing debt
P/B	Price book ratio
P/E ratio	Price earnings ratio
RoE	Return on equity
ROCE	Return on capital employed
RS	Recommendation suspended
UR	Under Revision

Euro area (EA)	*Austria, Belgium, Cyprus, Estonia, Finland, France, Germany, Greece, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Portugal, Slovenia, Slovakia, Spain*
CE	*Central European countries – Poland, Hungary, Czech Republic, Slovakia, Slovenia*
SEE	*South East European countries – Albania, Bosnia and Herzegovina, Bulgaria, Croatia, Kosovo, Romania, Serbia*
EE	*Eastern Europe (Russia, Ukraine, Belarus)*
CEE	*Central and Eastern Europe (CE + SEE + EE)*

Please note the risk notifications and explanations at the end of this document

More political than economic impact from Brexit

- **Brexit likely to only have limited impact in CE and SEE over medium term**
- **Low interest rates continue**
- **Russia and Ukraine leaving recession**

The unexpected result of the British referendum on exiting the EU surprised many companies and capital market participants. The EU member states in Central and Eastern Europe will especially feel the effects of Great Britain leaving the EU. Depending on the future relationship between the UK and EU, which will be negotiated over the next two years, we see the following: The decline in exports from the UK will have a direct negative impact on growth, and the lower economic output in the euro area (1.5 instead of 1.7% GDP expansion in 2017) will have an indirect impact. On the other hand, starting in 2019, the UK will drop out of the EU budget as a net payer or make lower contributions when it only participates in the European Economic Area. Over the medium term, this will negatively influence Poland, Hungary, and Romania as larger net recipients of transfer payments. We may also see a decline in investment activity as a result of the uncertain situation. In line with our projection for the euro area, we have therefore lowered our growth projections for Poland, the Czech Republic, and peers by around 0.2 percentage points for 2017. Domestic demand remains the key driver of growth in CE and SEE. The still declining prices in many countries combined with relatively high wage growth and increasing employment are pushing private consumption on a broad basis. As consumer prices are likely to remain at historic lows for longer than originally expected, the purchasing power of households should prove to be the determining factor in consumer spending in the coming quarters.

Since the beginning of the year in Russia and Ukraine signs have been pointing to a bottoming out of the recession with recovery tendencies in the second half of the year. The climbing commodities prices and rouble exchange rate have contributed to this. We are raising our 2016 GDP projection for Russia from -2.0 to -0.5%. Consumer price inflation of just over 7% in both countries as recently published is well below the high double-digit rates posted in 2015. This provides leeway for the Russian and Ukrainian central banks to cut interest rates further in the coming quarters.

Impact on currencies

The political uncertainty has impacted the development of currencies in the past months. The Polish zloty and the Romanian leu are the most prominent "victims" that are tending weaker despite the fundamental economic data. PLN and HUF are likely to react to the Brexit with the most volatility. The RUB is likely to have exhausted its potential with the newly expected USD appreciation and should consolidate until the end of the year.

Impact on the bond and equity markets

The largely completed bond market correction in CE/SEE with a noticeably wider yield spread versus German EUR government bonds offers sufficient risk buffer for the second half of 2016. For this reason, we are set to buy on a number of CEE bond markets. This is also true for Russian government bonds in the long term. The effects of the Brexit are also apparent on the stock markets in CE and SEE, so we expect a volatile sidewards trend in Q3. By contrast, we have a buy recommendation for Russia and Turkey. We take a cautious view of Poland due to unfavourable policy developments.

Financial analyst: Peter Brezinschek, RBI Vienna

CEE: Market strategy[1]

	Eurobonds		LCY Bonds		FX
	EUR	USD	2y	10y	–
BG	B (H)	–	–	–	–
HR	S (H)	S (H)	–	–	H (H)
CZ	H (H)	H (H)	H (H)	H (H)	H (H)
HU	B (H)	B (H)	H (H)[2)]	B (B)	H (H)
PL	S (S)	S (S)	H (H)	H (H)	H (H)
RO	S (H)	S (H)	H (H)	H (H)	H (H)
RU	H (H)	H (H)	B (H)	B(H)	H (H)
RS	–	B (B)	–	–	H (H)
MK	H (H)	–	–	–	–
KZ	–	H (H)			
TR	B (H)	H (H)	B (H)	B (H)	H (H)
UA	–	H (H)	–	–	S (S)
BY	–	H (H)	–	–	S (S)

[1] **LCY bonds:** *based on absolute performance in LCY*
Eurobonds: *based on expected spread change*
FX *vs. EUR*
Recommendation horizon: **end 3rd quarter 2016**
For recommendation history please see page 62
B: Buy; H: Hold; S: Sell
2) HU: 3y, not 2y tenor
Source: RBI/Raiffeisen RESEARCH

Recommendations[1] – stock markets

Indices	
Buy	BIST National, PX, MICEX
Hold	BET, BUX, CROBEX 10, ATX
Sell	WIG 30

Equities

Andritz
Current share price: EUR 41.0
Target price: EUR 53.0
Polytec
Current share price: EUR 7.10
Target price: EUR 9.50
Vienna Insurance Group
Current share price: EUR 16.92
Target price: EUR 22.20
Ciech
Current share price: PLN 55.00
Target price: PLN 85.00
InterRAO
Current share price: RUB 2.28
Target price: RUB 2.94

Recommendations[1] – debt markets

Corporate bonds		curr.[2]
Buy	Severstal 5.9% due 2022	320bp

[1] *horizon:* **end 3rd quarter 2016**
[2] *z-spreads (bp)*
Source: RBI/Raiffeisen RESEARCH

Real GDP (% yoy)

Countries	2014	2015	2016e	*Consensus*	2017f	*Consensus*
Poland	3.3	3.6	3.5	*3.4*	3.8	*3.5*
Hungary	3.7	2.9	2.2	*2.0*	2.7	*2.7*
Czech Rep.	1.9	4.3	2.3	*2.5*	2.7	*2.7*
Slovakia	2.5	3.6	3.5	*3.2*	3.3	*3.3*
Slovenia	3.0	2.9	2.2	*2.1*	2.1	*2.2*
CE	**3.0**	**3.6**	**3.0**	*3.0*	**3.3**	*3.2*
Croatia	-0.4	1.6	1.5	*1.8*	1.5	*1.9*
Bulgaria	1.5	3.0	2.5	*2.6*	3.0	*2.8*
Romania	3.0	3.8	4.0	*4.1*	3.6	*3.4*
Serbia	-1.8	0.5	2.5	*2.1*	3.0	*2.5*
Bosnia a. H.	1.1	2.8	3.0	*3.1*	3.5	*3.1*
Albania	2.0	2.6	3.5	*3.2*	4.0	*3.6*
Kosovo	0.9	3.0	3.0	*3.4*	3.5	*4.1*
SEE	**1.6**	**2.9**	**3.2**	3.2	**3.2**	3.0
Russia	0.7	-3.7	-0.5	*-0.9*	1.0	*1.2*
Ukraine	-6.6	-9.9	1.5	*1.1*	2.0	*2.4*
Belarus	1.7	-3.9	-2.0	*-2.1*	1.0	*1.5*
EE	**0.3**	**-4.1**	**-0.4**	*-0.8*	**1.1**	*1.3*
Turkey	2.9	4.0	3.5	*3.5*	3.5	*3.5*
Austria	**0.4**	**0.9**	**1.4**	*1.4*	**1.3**	*1.5*
Germany	1.6	1.4	1.8	1.7	1.7	1.5
Euro area	**0.9**	**1.7**	**1.6**	*1.6*	**1.5**	*1.6*
USA	**2.4**	**2.4**	**2.5**	1.9	**2.4**	2.3

Source: national sources, RBI/Raiffeisen RESEARCH

Consumer prices (avg, % yoy)

Countries	2014	2015	2016e	2017f
Poland	0.0	-0.9	-0.4	1.7
Hungary	-0.2	0.0	0.4	2.2
Czech Rep.	0.4	0.3	0.7	1.7
Slovakia	-0.1	-0.3	-0.1	2.2
Slovenia	0.2	-0.5	0.2	0.9
CE	**0.1**	**-0.5**	**0.0**	**1.8**
Croatia	-0.2	-0.5	-1.0	1.5
Bulgaria	-1.4	-0.1	0.3	1.6
Romania	1.1	-0.6	-1.2	2.3
Serbia	2.9	1.4	1.2	2.5
Bosnia a. H.	-0.9	-1.0	0.0	1.5
Albania	1.6	1.8	1.5	2.2
Kosovo	0.4	-0.5	1.0	2.0
SEE	**0.7**	**-0.2**	**-0.5**	**2.1**
Russia	7.8	15.6	7.5	7.2
Ukraine	12.1	48.7	15.5	12.0
Belarus	18.1	13.5	16.0	13.5
EE	**8.4**	**17.5**	**8.3**	**7.7**
Turkey	8.9	7.7	7.3	7.6
Austria	**1.5**	**0.8**	**1.2**	**2.2**
Germany	0.8	0.1	0.7	2.7
Euro area	**0.4**	**0.0**	**0.3**	**1.5**
USA	**1.6**	**0.1**	**1.4**	**2.7**

Source: national sources, RBI/Raiffeisen RESEARCH

Current account balance (% of GDP)

Countries	2014	2015	2016e	2017f
Poland	-2.0	-0.2	-0.9	-1.2
Hungary	3.9	4.4	4.5	4.1
Czech Rep.	0.2	0.9	1.4	1.0
Slovakia	0.1	-1.3	-0.9	-0.7
Slovenia	7.0	6.5	5.5	4.8
CE	**-0.2**	**1.0**	**0.7**	**0.3**
Croatia	0.9	5.2	2.0	2.2
Bulgaria	1.2	1.1	1.1	0.4
Romania	-0.5	-1.1	-2.8	-3.3
Serbia	-6.0	-4.6	-4.3	-4.5
Bosnia a. H.	-7.5	-5.6	-7.0	-7.6
Albania	-12.9	-13.6	-13.5	-14.3
Kosovo	-7.8	-9.4	-7.5	-7.8
SEE	**-1.5**	**-1.0**	**-2.4**	**-2.8**
Russia	3.2	5.0	4.0	4.5
Ukraine	-3.5	-0.1	-3.3	-3.4
Belarus	-6.8	-3.8	-5.7	-5.4
EE	**2.5**	**4.4**	**3.2**	**3.7**
Turkey	-5.4	-4.5	-5.0	-5.0
Austria	**1.9**	**2.6**	**2.5**	**2.2**
Germany	7.3	8.5	7.5	7.5
Euro area	**2.4**	**3.2**	**3.0**	**2.9**
USA	**-2.2**	**-2.6**	**-3.2**	**-3.5**

Source: national sources, RBI/Raiffeisen RESEARCH

General budget balance (% of GDP)

Countries	2014	2015	2016e	2017f
Poland	-3.3	-2.6	-2.9	-3.4
Hungary	-2.5	-2.0	-2.2	-2.7
Czech Rep.	-1.9	-0.4	-0.3	-0.2
Slovakia	-2.7	-3.0	-2.1	-1.3
Slovenia	-4.9	-2.9	-2.7	-2.5
CE	**-2.9**	**-2.1**	**-2.2**	**-2.4**
Croatia	-5.5	-3.2	-3.0	-2.9
Bulgaria	-3.6	-2.9	-2.5	-2.0
Romania	-0.9	-0.7	-3.0	-3.2
Serbia	-6.6	-3.7	-3.7	-3.0
Bosnia a. H.	-2.1	-2.5	-2.0	-1.0
Albania	-5.1	-4.0	-2.5	-1.5
Kosovo	-2.6	-2.2	-2.3	-2.5
SEE	**-2.8**	**-2.0**	**-2.9**	**-2.8**
Russia	-1.0	-3.6	-4.4	-3.3
Ukraine	-4.9	-2.3	-3.5	-3.0
Belarus	1.0	1.8	0.5	0.0
EE	**-1.2**	**-3.3**	**-4.2**	**-3.2**
Turkey	-1.3	-1.2	-2.0	-1.5
Austria	**-2.7**	**-1.2**	**-1.9**	**-1.8**
Germany	0.3	0.7	0.5	0.5
Euro area	**-2.6**	**-2.1**	**-1.7**	**-1.2**
USA	**-2.8**	**-2.4**	**-2.9**	**-2.9**

Source: national sources, RBI/Raiffeisen RESEARCH

Public debt (% of GDP)

Countries	2014	2015	2016e	2017f
Poland	50.5	51.3	52.1	52.6
Hungary	76.2	75.5	74.9	74.5
Czech Rep.	42.7	41.1	40.3	39.1
Slovakia	53.9	52.9	52.8	52.1
Slovenia	80.8	83.5	81.9	81.2
CE	**54.2**	**54.2**	**54.3**	**54.2**
Croatia	86.5	86.7	87.2	87.6
Bulgaria	26.9	26.3	29.5	30.0
Romania	39.8	38.4	39.2	39.9
Serbia	68.8	74.7	78.5	81.3
Bosnia a. H.	42.2	42.4	46.0	45.0
Albania	71.6	72.2	70.5	67.8
Kosovo	10.6	13.0	13.5	13.8
SEE	**48.5**	**48.5**	**50.0**	**50.6**
Russia	11.5	12.7	13.5	14.0
Ukraine	52.9	72.6	79.3	78.9
Belarus	34.1	48.5	49.9	46.4
EE	**14.7**	**17.5**	**18.6**	**19.0**
Turkey	35.0	34.0	32.0	33.0
Austria	**84.3**	**86.2**	**85.3**	**84.0**
Germany	74.7	71.2	68.5	65.6
Euro area	**92.0**	**90.7**	**90.5**	**89.0**
USA	**103.2**	**101.9**	**104.5**	**104.1**

Source: national sources, RBI/Raiffeisen RESEARCH

Gross foreign debt (% of GDP)

Countries	2014	2015	2016e	2017f
Poland	71.1	70.1	74.2	73.9
Hungary	113.9	105.7	98.5	87.2
Czech Rep.	66.6	70.7	74.6	78.1
Slovakia	89.7	86.1	84.9	83.1
Slovenia	124.1	114.8	110.0	104.1
CE	**71.5**	**70.4**	**72.0**	**71.0**
Croatia	108.5	103.7	99.1	98.5
Bulgaria	93.1	77.2	76.6	74.8
Romania	63.1	56.7	53.3	52.7
Serbia	78.6	81.6	80.6	78.3
Bosnia a. H.	51.8	54.2	55.5	55.7
Albania	69.2	72.6	71.1	68.2
Kosovo	31.2	33.0	33.2	34.4
SEE	**74.7**	**68.8**	**66.1**	**64.9**
Russia	29.5	39.3	38.0	31.9
Ukraine	95.2	131.5	140.0	140.4
Belarus	52.6	70.2	75.6	70.4
EE	**34.2**	**46.1**	**45.8**	**39.7**
Turkey	50.3	55.4	55.1	52.3
Austria	**n.v.**	**n.v.**	**n.v.**	**n.v.**
Germany	n.v.	n.v.	n.v.	n.v.
Euro area	**120.3**	**120.1**	**n.v.**	**n.v.**
USA	**n.v.**	**n.v.**	**n.v.**	**n.v.**

Source: national sources, RBI/Raiffeisen RESEARCH

Exchange rate EUR/LCY (avg)

Countries	2014	2015	2016e	2017f
Poland	4.19	4.18	4.38	4.29
Hungary	309	310	315	309
Czech Rep.	27.5	27.3	27.0	26.4
Slovakia	euro	euro	euro	euro
Slovenia	euro	euro	euro	euro
Croatia	7.63	7.61	7.56	7.57
Bulgaria	1.96	1.96	1.96	1.96
Romania	4.44	4.45	4.50	4.47
Serbia	117	121	123	124
Bosnia a. H.	1.96	1.96	1.96	1.96
Albania	140	140	138	138
Kosovo	euro	euro	euro	euro
Russia	51.0	68.0	74.6	66.7
Ukraine	15.9	24.3	28.9	29.7
Belarus	13597	17706	22845	23129
Turkey	2.90	3.02	3.20	3.02
Austria	**euro**	**euro**	**euro**	**euro**
Germany	euro	euro	euro	euro
Euro area	**euro**	**euro**	**euro**	**euro**
USA	**1.33**	**1.11**	**1.10**	**1.01**

Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Ratings[1]

Countries	S&P	Moody's	Fitch
Poland	BBB+	A2	A-
Hungary	BB+	Ba1	BBB-
Czech Rep.	AA-	A1	A+
Slovakia	A+	A2	A+
Slovenia	A	Baa3	BBB+
Croatia	BB	Ba2	BB
Bulgaria	BB+	Baa2	BBB-
Romania	BBB-	Baa3	BBB-
Serbia	BB-	B1	BB-
Bosnia a. H.	B	B3	NR
Albania	B+	B1	NR
Kosovo	NR	NR	NR
Russia	BB+	Ba1	BBB-
Ukraine	B-	Caa3	CCC
Belarus	B-	Caa1	B-
Turkey	BB+	Baa3	BBB-
Austria	**AA+**	**Aa1**	**AA+**
Germany	AAA	Aaa	AAA
USA	AA+	Aaa	AAA

[1] *for FCY, long-term debt; NR ... not rated*

Source: Bloomberg, RBI/Raiffeisen RESEARCH

Please note the risk notifications and explanations at the end of this document

Exchange rate forecast

Countries	28-Jun[1]	Sep-16	Dec-16	Jun-17
vs EUR				
Poland	4.44	4.40	4.35	4.30
Hungary	317.58	315.0	315.0	310.0
Czech R.	27.12	27.0	27.0	25.9
Croatia	7.52	7.55	7.60	7.50
Romania	4.53	4.50	4.50	4.50
Serbia	123.79	123.0	124.0	123.0
Albania	137.24	138.5	137.5	138.5
vs USD				
Russia	64.7	65.0	67.0	65.0
Ukraine	24.89	27.00	29.00	29.00
Belarus	20050	21000	22500	22900
Turkey	2.90	2.90	2.95	2.95
EUR/USD	1.11	1.10	1.05	0.99

[1] 5:00 p.m. (CEST)
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Key interest rate forecast

Countries	28-Jun[1]	Sep-16	Dec-16	Jun-17
Poland	1.50	1.50	1.50	1.50
Hungary	0.90	0.90	0.90	0.90
Czech R.	0.05	0.05	0.05	0.05
Romania	1.75	1.75	1.75	1.75
Russia	10.50	10.00	9.50	9.00
Turkey	7.50	7.50	7.50	6.50
Euro area	0.00	0.00	0.00	0.00
USA	0.50	0.50	0.75	1.00

[1] 5:00 p.m. (CEST)
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

3m money market rate forecast

Countries	28-Jun[1]	Sep-16	Dec-16	Jun-17
Poland	1.71	1.65	1.65	1.65
Hungary	1.01	1.05	1.05	1.05
Czech R.	0.29	0.30	0.30	0.30
Croatia	0.80	0.90	0.90	0.90
Romania	0.82	1.20	1.30	1.80
Russia	11.00	10.80	10.30	9.80
Turkey	9.73	10.50	10.00	9.00
Euro area	-0.28	-0.30	-0.30	-0.25
USA	0.63	0.60	0.85	1.10

[1] 5:00 p.m. (CEST)
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

2y LCY yield forecast

Countries	28-Jun[1]	Sep-16	Dec-16	Jun-17
Poland	1.68	1.8	1.9	2.1
Hungary*	1.91	1.8	1.9	2.2
Czech R.	-0.08	-0.3	-0.4	0.0
Croatia	1.91	1.9	1.9	2.0
Romania*	1.95	2.0	2.2	2.5
Russia	9.44	9.2	8.8	8.6
Turkey	8.56	8.9	8.8	8.0
Austria	-0.52	-0.6	-0.5	-0.4
Germany	-0.65	-0.6	-0.5	-0.5
USA	0.61	0.8	1.1	1.3

[1] 5:00 p.m. (CEST); * 3y LCY yields
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

10y LCY yield forecast

Countries	28-Jun[1]	Sep-16	Dec-16	Jun-17
Poland	3.02	3.0	3.2	3.5
Hungary	3.27	3.0	3.1	3.6
Czech R.	0.49	0.4	0.5	0.7
Croatia	3.68	3.9	3.9	3.9
Romania	3.55	3.6	3.8	4.1
Russia	8.49	8.6	8.8	8.5
Turkey	9.20	9.0	8.9	8.5
Austria	0.11	0.4	0.6	1.0
Germany	-0.12	0.0	0.3	0.7
USA	1.46	1.8	2.1	2.6

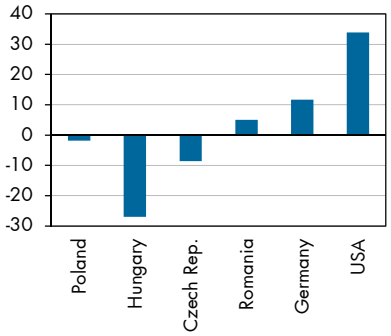
[1] 5:00 p.m. (CEST)
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Spreads 10y LCY bonds over Bund

Countries	28-Jun[1]	Sep-16	Dec-16	Jun-17
Poland	314	300	290	280
Hungary	339	300	280	290
Czech R.	60	40	20	0
Croatia	380	390	360	320
Romania	367	360	350	340
Russia	861	860	850	780
Turkey	932	900	860	780
Austria	22	40	30	30
USA	158	180	180	190

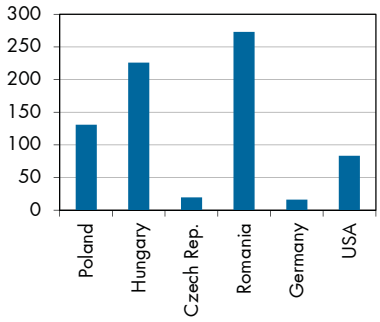
[1] 5:00 p.m. (CEST); all values in bp
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Expected 10y LCY yield change



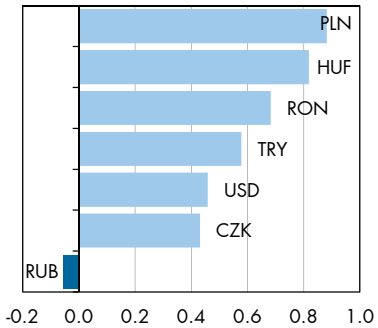
bp-change of 10y gov. bond yield in next 3 months
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Yield curve slope



bp-spread between 10y and 3m maturity
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

LCY changes vs EUR (% qoq)[1]



[1] forecasts for 30 Jun-2016 in comparison to 29 Mar-2016
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Stock market indicators

	Earnings growth		Price/earnings ratio	
	16e	17f	16e	17f
ATX	-7.7%	19.0%	11.6	9.7
WIG 30	397.7%	2.9%	12.0	11.6
BUX	n.v.	16.1%	12.1	10.4
PX	9.7%	5.2%	10.7	10.2
MICEX	0.2%	12.9%	6.8	6.1
BET*	25.6%	44.0%	10.9	7.5
CROBEX10	-58.5%	-1.5%	13.1	13.3
BIST Nat. 100	8.9%	18.1%	9.1	7.7

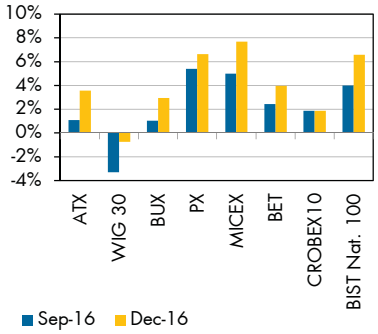
* Romania (BET) excl. Fondul Proprietatea
Source: Thomson Reuters, IBES, Bloomberg, RBI/Raiffeisen RESEARCH

Stock market forecasts

	Index estimates			
	28-Jun[1]	Sep-16	Dec-16	Jun-17
ATX	2,028	2,050	2,100	1,950
WIG 30	1,954	1,890	1,940	1,870
BUX	26,227	26,500	27,000	25,500
PX	806	850	860	810
MICEX	1,857	1,950	2,000	2,030
BET	6,444	6,600	6,700	6,300
CROBEX10	972	990	990	940
BIST Nat. 100	76,929	80,000	82,000	76,000

[1] 11:59 p.m. (CEST)
in local currency
Source: Bloomberg, RBI/Raiffeisen RESEARCH

Expected index performance



Source: RBI/Raiffeisen RESEARCH

Q2 sideways compared with the benchmark

- **Equities overweighting brought only limited success**
- **Eurobonds positioning with gains**
- **Losses from higher currency volatility**

Sum of last quarter[1]

RBI portfolio (in EUR)	-1.52%
Benchmark (in EUR)	-1.49%
RBI outperformance (in EUR)	-0.04 pp
by weighting of equities vs bonds	0.00 pp
regional equity weightings	-0.02 pp
weighting of EB vs LCY bonds	0.06 pp
country weightings of LCY bonds	-0.08 pp
country weightings of EB EUR	0.00 pp
country weightings of EB USD	0.00 pp
joint effects / duration	0.00 pp

1 29 March 2016 - 28 June 2016
EB...Eurobonds
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Period 1: 29 Mar 2016 - 27 Apr 2016

RBI portfolio (in EUR)	1.36%
Benchmark (in EUR)	1.20%
RBI outperformance (in EUR)	0.16 pp
by weighting of equities vs bonds	0.13 pp
regional equity weightings	0.03 pp
weighting of EB vs LCY bonds	0.04 pp
country weightings of LCY bonds	-0.04 pp
country weightings of EB EUR	0.00 pp
country weightings of EB USD	0.00 pp
joint effects / duration	0.00 pp

EB...Eurobonds
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Period 2: 27 Apr 2016 - 31 May 2016

RBI portfolio (in EUR)	-2.36%
Benchmark (in EUR)	-2.26%
RBI outperformance (in EUR)	-0.10 pp
by weighting of equities vs bonds	-0.13 pp
regional equity weightings	0.02 pp
weighting of EB vs LCY bonds	0.02 pp
country weightings of LCY bonds	0.00 pp
country weightings of EB EUR	0.00 pp
country weightings of EB USD	0.00 pp
joint effects / duration	0.00 pp

EB...Eurobonds
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Period 3: 31 May 2016 - 28 Jun 2016

RBI portfolio (in EUR)	-0.49%
Benchmark (in EUR)	-0.40%
RBI outperformance (in EUR)	-0.10 pp
by weighting of equities vs bonds	0.00 pp
regional equity weightings	-0.06 pp
weighting of EB vs LCY bonds	0.00 pp
country weightings of LCY bonds	-0.04 pp
country weightings of EB EUR	0.00 pp
country weightings of EB USD	0.00 pp
joint effects / duration	0.00 pp

EB...Eurobonds
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

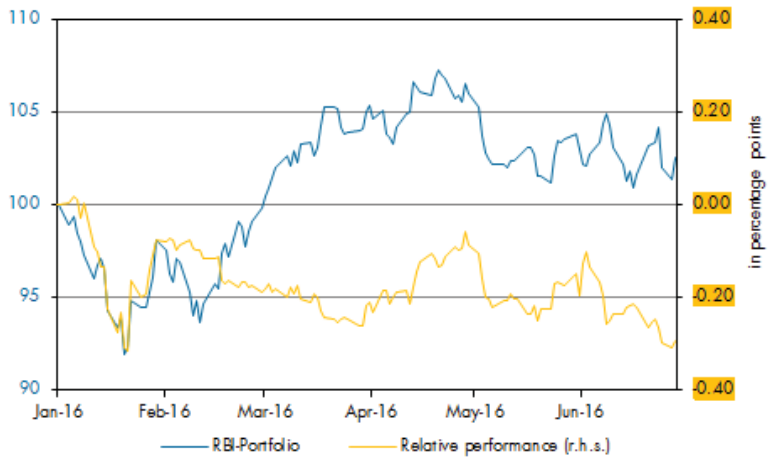
Expecting slightly higher risk-adjusted yields, we overweighted the equities segment by 3 percentage points (pp) versus bonds in the first two periods. However, this positioning only brought outperformance in the first period. Due to risk factors, in particular political uncertainty (Turkey) and the high volatility of the oil price, we closed out this weighting in the third period.

In the **equity portfolio**, we preferred Hungary throughout all periods in addition to Turkey (period 1) and the Czech Republic (period 3) because Hungary promised the greatest risk-adjusted yields due to its solid economy and prospects for interest rate cuts. These positions were financed through the more volatile markets of Poland and Russia. Overall, the segment underperformed by 2 basis points (bp) versus the benchmark.

In the **bonds segment**, the overweighting of Eurobonds in EUR versus local-currency bonds that has been in place since Q1 was maintained in all three periods. We are now closing these positions with an outperformance of 6bp. This was neutralised by the positions in local-currency bonds (-8bp), especially due to the currency losses from the underweighting of Russia.
Overall, the positive and negative effects of the individual segments virtually offset each other. All in all, the CEE portfolio is closing this quarter 4bp below the benchmark.

Financial analyst: Stefan Theußl, RBI Vienna

Performance 2016



Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

CEE portfolio

	2013	2014	2015	ytd
Benchmark	-2.54%	-8.11%	2.42%	2.83%
Portfolio	-2.41%	-8.23%	1.78%	2.53%
Relative Performance	0.12pp	-0.12pp	-0.64pp	-0.30pp

Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Hot summer expected on the stock markets

- **Volatility expected to remain high on the equity market after Brexit referendum**
- **US Fed again postpones further interest rate hikes**
- **Bonds showing diminishing risk buffers**

The **asset allocation strategy in our CEE portfolio** is currently being dominated by four topics: Brexit, the monetary policies of the ECB and the US Fed, political risks, and the oil price.

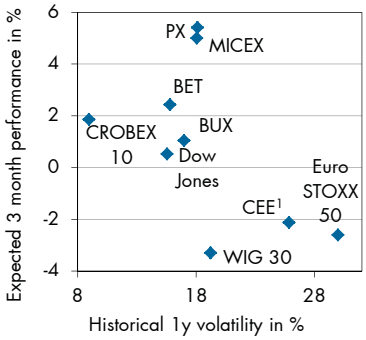
On the one hand, we are not only seeing an extremely loose **monetary policy** from the ECB but also a high level of caution by the US Fed. Now additionally, with the Britons' decision to leave the EU, the probability of a further rate hike in the next quarter decreased. All in all **the support for riskier assets such as stocks** is still given in our view. Nevertheless uncertainty caused by the Brexit referendum weighs on the markets.

On the other hand, the low interest rate environment in the euro area also affects CEE local currency bonds in the sense that their premiums over German government bonds look attractive. The danger is that risk buffers already reached the lower limit because of this hunt for returns. Hence, further price gains are limited. Politically induced risk factors (including the Russia/Ukraine conflict, franc loan conversions in Poland, new elections in Croatia, etc.) **could therefore from a euro-investor's perspective push volatility back up over the short term.**

All in all, we propose a **neutral weighting between equities and bonds in Q3.** We project that the key leading equity indices will be between 1% and 5.4% higher in local currencies (except for Poland) while we expect stagnating or slightly lower yields on ten-year government bonds. Currencies in CEE could also profit from the wait-and-see stance of the Fed and the latest developments of the oil price, showing signs of stability. The latter is also a potential source for temporary setbacks because of the high susceptibility to volatility.

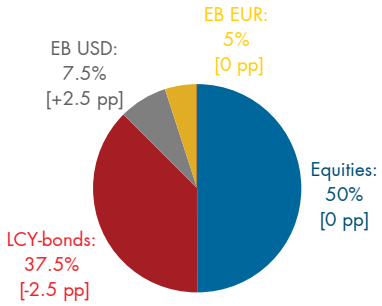
Financial analyst: Stefan Theußl, RBI Vienna

Risk-return (%)



Local currency
1 MSCI EM Eastern Europe in euro
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

CEE portfolio weightings Q3 2016



LCY…local currency, EB … Eurobonds
[-] , [+] = Over-/underweight versus benchmark
[0] = No over/-underweight versus benchmark
Source: RBI/Raiffeisen RESEARCH

Historical volatility & performance (%)

	Equities[1]						Bonds					
	Volatility[2]		Performance ytd		Performance 5y[3]		Volatility[2]		Performance ytd		Performance 5y[3]	
Countries	EUR	LCY	EUR	LCY	EUR	LCY	EUR	LCY	EUR	LCY	EUR	LCY
Czech Republic	21.5	21.4	-10.3	-10.0	-11.5	-9.6	1.1	1.1	-0.1	0.2	3.3	5.5
Hungary	25.6	23.5	5.9	6.5	-4.6	-1.3	6.0	2.7	2.6	3.1	5.5	9.1
Poland	26.5	20.7	-9.7	-6.6	-10.0	-8.2	10.6	3.0	-1.9	1.5	4.3	6.5
Romania	16.4	16.2	-4.0	-3.8	4.8	6.3	2.3	0.1	-0.1	0.1	1.1	2.6
Russia	25.4	17.9	13.7	4.9	-9.2	-1.4	16.4	3.4	20.9	8.9	-4.1	7.5
Turkey	26.9	21.7	6.8	8.1	-1.8	4.4	12.4	6.1	9.9	11.2	2.2	8.7
Croatia	6.4	6.5	1.0	-0.6	-6.8	-6.5	3.7	4.2	4.1	2.4	6.3	6.7
CEE	19.9	-	2.8	-			5.0	-	1.2	-		

[1] MSCI indices
[2] Three months volatility annualised
[3] Five-year annual return
LCY…local currency
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Major differences in the performance of CEE bonds

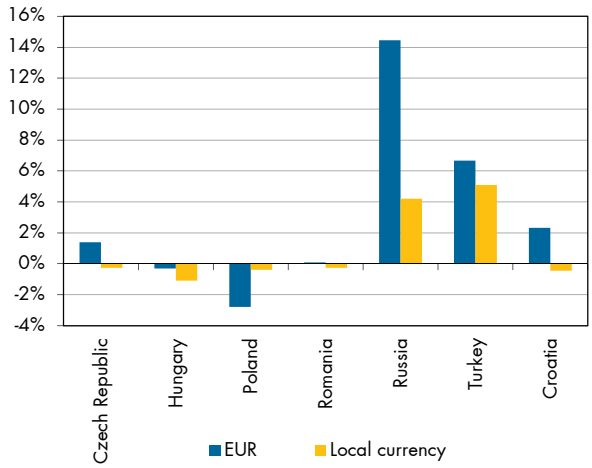
- **Yields expected to move sideways over the summer**
- **CEE currencies stable versus the EUR**
- **Russian government bonds overweighted versus Polish and Romanian ones**

Portfolio weightings: bonds*

	Portfolio	Benchmark	Difference
EB USD	15.0%	10.0%	5.0%
EB EUR	10.0%	10.0%	0.0%
LCY	75.0%	80.0%	-5.0%
Czech Republic	20.0%	20.0%	0.0%
Hungary	20.0%	20.0%	0.0%
Poland	44.0%	45.0%	-1.0%
Romania	4.0%	5.0%	-1.0%
Russia	7.0%	5.0%	2.0%
Turkey	5.0%	5.0%	0.0%
Croatia	0.0%	0.0%	0.0%

** Share in percentage points*
Source: RBI/Raiffeisen RESEARCH

Historical relative performance*



** since 3 months, local currency bonds versus portfolio bond benchmark*
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

The last quarter was dominated by rising yields and weaker currencies in CEE. The most important **global factors** were the pricing-in of interest rate hikes in the US in the middle of May and the outcome of the Brexit referendum. There were also country-specific factors such as the decisions on conversion of CHF loans in Poland. Russia was one of the few countries to see lower yields and a stronger rouble versus the euro, mainly due to the stabilizing oil price and the expectation of falling interest rates. Over the summer, **we expect stable exchange rates versus the euro and largely steady yields in CEE**. The Brexit aftermath could make Eurobonds look more favourable than local currency bonds (-5pp) in the short term. Hence, we overweight USD Eurobonds by 5pp.

Russian government bonds denoted in rouble are **overweighted in the portfolio by 2pp** because we expect a stable EUR/RUB at around 71.5 and due to the high interest rates of about 8.5% at present, which should more than offset the slight yield increases. This is being financed with an underweighting of **Polish and Romanian government bonds (-1pp each).** As of late the Polish zloty has come under some pressure, which makes a slight recovery probable in the next weeks. However, uncertainty due to political problems remains high. In Romania, a decrease of excess liquidity should lead to a marginal increase in yields.

Financial analyst: Nina Neubauer-Kukić, CIIA;,RBI Vienna

Expected bond market performance (%)

	3m		6m		9m		12m	
Countries	**EUR**	**LCY**	**EUR**	**LCY**	**EUR**	**LCY**	**EUR**	**LCY**
Czech Republic	1.4	0.9	0.6	0.2	-0.1	-0.5	3.2	-1.2
Hungary	3.0	2.4	2.9	2.2	3.3	1.1	1.2	-1.0
Poland	0.7	0.1	0.8	-1.0	1.7	-1.2	0.6	-2.2
Romania	0.8	0.3	0.5	0.0	2.0	0.4	0.6	0.0
Russia	0.3	0.9	2.6	1.7	8.7	5.7	17.9	7.7
Turkey	3.9	3.0	10.0	6.1	14.6	10.3	23.7	13.3

Not annualised; 10y treasury bond, LCY…local currency
Source: RBI/Raiffeisen RESEARCH

Outlook mixed

- **Czech Republic has greatest recovery potential**
- **Russia hardly affected by the Brexit aftermath**
- **Politically induced uncertainty hurting Polish equity market**

After the turbulence ahead of and after the Brexit referendum, volatility should remain high short term before markets may return to calmer waters. However, several factors argue for more stability already in the third quarter: the very expansive monetary policy especially of the ECB (and its willingness to provide further measures), the good development of the economies in CE and SE, and the recent recovery of the oil price.

According to our projections, the **Russian and Czech equity markets** offer the **best potential** for higher price levels. With the highest risk-adjusted yields on the basis of our performance expectations for the next 3 months and the recently observed volatility (5%/17.9% and 5.4%/21.4%, respectively), these markets are also the most attractive for euro-investors taking our FX projections into account (RUB, CZK expected to be stable or slightly stronger). Russia is profiting from the higher oil price than at the beginning of the year, and we think the country's economy could bottom out this year. The Czech equity market is attractively valued after the latest correction. Hence, we overweight both markets by 1 percentage point (pp) each.

By contrast, we expect **below-average** performance from the **markets in Poland and Hungary**. In the case of the former, we feel that the prospects for price gains are limited by a range of risk factors (political uncertainty, conversion of the CHF loans, etc.). The latter is running out of steam and showed comparatively higher volatility last quarter, which makes us cautious. For this reason, we are underweighting both by 1pp each.

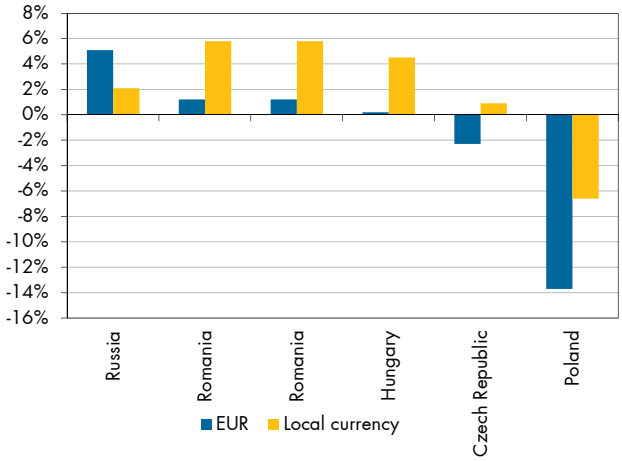
Financial analyst: Stefan Theußl, RBI Vienna

Portfolio weightings: stocks*

	Portfolio	Benchmark	Difference
Czech Republic	9.0%	8.0%	1.0%
Hungary	6.0%	7.0%	-1.0%
Poland	24.0%	25.0%	-1.0%
Russia	36.0%	35.0%	1.0%
Turkey	25.0%	25.0%	0.0%
Croatia	0.0%	0.0%	0.0%
Romania	0.0%	0.0%	0.0%

** Share in percentage points*
Source: RBI/Raiffeisen RESEARCH

Historical relative performance*



** to MSCI CEE, since 3 months*
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Expected stock market performance (%)

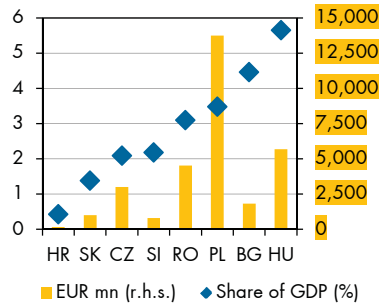
	3m		6m		9m		12m	
Countries	**EUR**	**LCY**	**EUR**	**LCY**	**EUR**	**LCY**	**EUR**	**LCY**
Czech Republic	5.9	5.4	7.1	6.6	3.4	2.9	5.2	0.4
Hungary	1.9	1.0	3.8	2.9	3.5	1.0	-0.4	-2.8
Poland	-2.4	-3.3	1.3	-0.7	0.9	-2.3	-1.2	-4.3
Romania	3.1	2.4	4.7	4.0	2.7	0.9	-1.6	-2.2
Russia	4.9	5.0	9.4	7.7	12.6	8.8	21.4	9.3
Croatia	1.4	1.9	0.7	1.9	-2.3	-1.2	-3.1	-3.3
Turkey	5.3	4.0	11.0	6.6	7.3	2.7	9.2	-1.2

Not annualised, LCY…local currency
Source: RBI/Raiffeisen RESEARCH

Focus on: Brexit spillovers to CEE economies

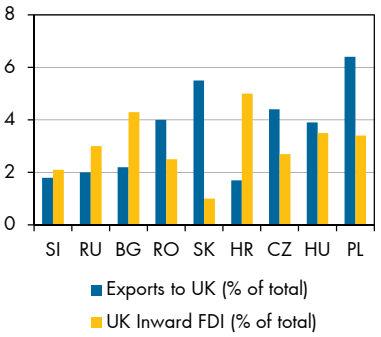
- **Brexit spillovers with more down- than upside in the real economy, investments may suffer going forward**
- **Economic downsides (trade, FDI, investments, remittances) mostly in well integrated and export-oriented CE economies**
- **EU enlargement will remain an uphill battle – watch out for political volatility and EU (enlargement) frustration**
- **Accommodative monetary policy (Fed, ECB) for longer to spill over to CE and possibly SEE markets**

Net EU transfers to CEE (2014)



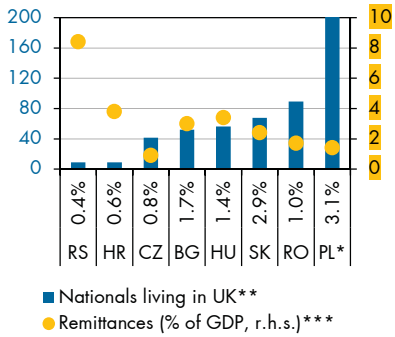
Source: Bundeszentrale für politische Bildung, European Commission, RBI/Raiffeisen RESEARCH

CEE: UK-gearing major economies*



** Latest available data 2014 or 2015*
Source: national sources, RBI/Raiffeisen RESEARCH

Nationals in UK & remittances (2014)



** Scale capped some 700,000-800,000 Polish citizens living in the UK*
*** Total (in thousands) and % working population domestically (above country abbreviations)*
**** Total remittances, share of UK may vary among individual countries*
Source: national sources, World Bank, RBI/Raiffeisen RESEARCH

With regards to Brexit spillovers to CEE we see more down- than upside. However, **overall hitches are likely to be moderate** and one has to differentiate between markets and the real economy. Supplementary market volatility – driven by political news and risk perception – could be in the cards in H2 2016. However, more accommodative monetary policy for longer globally (ECB, Fed) as well as modest economic shortcomings should not be too negative for sentiment either. That said **spillovers from ECB QE could regain importance for CEE assets.** However, there are also medium-term effects, mostly with negative implications, that should not be talked down. For **CE countries UK is a key trading partner** (in most cases accumulating trade surpluses). Secondly, UK remains a noticeable FDI partner of some CE/SEE economies, where some activities could be also affected. Moreover, CE countries are most exposed to the broader European economic and investment cycle. Therefore, **in CE and selected SEE economies we see GDP downsides of some 0.1-0.3%**, i.e. at least of a similar magnitude like in the German or overall European economy. Moreover, there is a risk that future (joint) EU funding for CE/SEE, a key target area of EU funds, may suffer going forward. However, further UK access to the EU Common Market is likely to require sizeable contributions to the EU budget beyond the 2014-2020 budgeting period (e.g. at least 50% of current UK EU funding), limiting downsides for the EU budget. A Brexit may also change CEE-UK (outward) migration and remittances flows. However, based on past crisis experience we do not expect huge backward migration to CEE. It seems more likely that we will see more intra-EU migration in Western Europe (i.e. out from UK into other Western EU countries). Moreover, UK will have to accept some "grandfathering" for EU residents that flowed in pre-Brexit. With regards to lower remittances (due to weak UK economy and weaker GBP) Poland, Hungary and Slovakia do look most exposed.

With regards to politics we see four Brexit-related trends. Firstly, EU enlargement is unlikely to be a fast selling item. EU accession talks of EU candidates from SEE are unlikely to be closed until 2020 (not to speak about unpopular talks with Turkey). Secondly, the **EU focus on neighbouring countries** (like Ukraine) **may suffer** going forward. Thirdly, the **Brexit-process may also impact on the EU stance towards Russia**. From a medium-term perspective it seems more likely that sanctions could be relaxed more easily without UK. Moreover, EU countries could be inclined to get rid of this topic, while being burdened with Brexit negotiations. Fourthly, **markets are likely to focus on (potential) anti-EU rhetoric in the political sphere** – be it in member or candidate countries. In this context limited progress in EU talks may also support anti-EU rhetoric (possibly coupled with pro-Russian rhetoric like in case of Serbia). With regards to broader European and country specific transmission channels we see CE countries most exposed to Brexit-related uncertainties. Nevertheless, overall effects should be moderate due to solid fundamentals and limited macro-financial imbalances in CE. Brexit-related political implications definitely reach out well beyond CE as outlined previously.

Financial analyst: Gunter Deuber, RBI Vienna

Weaker dynamics in CE offset by robust SEE and stabilising Russia

- **With Russia recession fading, CEE region turned to a positive growth rate after four negative quarters**
- **Still robust growth in CE/SEE expected around 3% yoy, small negative Brexit effect in 2017**
- **We strongly upgraded our Russia growth outlook for this year from -2.0% to -0.5% yoy**
- **Inflation rates were subdued in CEE in early 2016 in line with European developments**

In Q1, **quarterly GDP growth in Hungary and Poland unexpectedly contracted** while remaining resilient in the Czech Republic and Slovenia. The lower yearly growth rate slightly dampens our strong growth outlook for CE, but for now we still (wish to) see this as a temporary setback. Net exports turned negative in both Hungary and Poland on strong import growth. Domestic demand fell in both countries on weaker public spending and investment while private household demand held up well. In SEE, the **booming domestic economy in Romania and a resurgent Serbia** should be highlighted. In Romania, domestic demand went through the roof increasing by almost 10% yoy. Obviously, this points to growing economic imbalances. Finally, in Turkey, GDP continued to grow strongly by 4.8% yoy or 0.8% qoq on minimum wage hikes and looser fiscal and monetary policies.

While 2016 growth is not expected to be much affected by Brexit, slower economic growth in the UK and prolonged political uncertainty in the EU could lead to less buoyant export and investment growth in CE countries in 2017 than initially anticipated. We therefore **decided to slightly trim our GDP outlook for the CE region**.

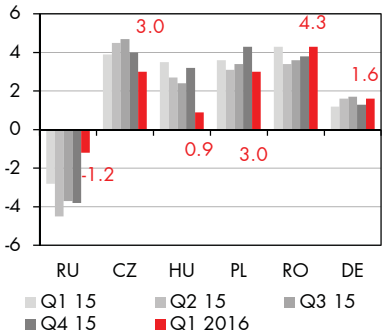
Further to the east, Russia performed much better than initially expected, as the first quarter only showed negative growth of 1.2% yoy. The Russian economy proved to be more resilient to the oil and rouble weakness at the beginning of the year. In Ukraine, the first quarter disappointed after two quarters with positive growth. **We strongly upgraded our Russia growth outlook for this year from -2.0% to -0.5% yoy**, moving from the very low of the consensus to the top. In our base scenario, we see oil prices between USD 45–50/bbl in H2 2016, with moderate upside potential in 2017. With regard to European economic sanctions against Russia, we stick to a status-quo scenario for 2016. European policymakers are set to prolong sectoral sanctions by an additional six months in H2 2016. However, we would not overrate the negative impact of sanctions on the current macroeconomic picture for Russia. Meanwhile, Russia prolonged the EU food import ban by 1.5 years, which is bad for consumers, but creates opportunities for local producers in this area (moderate positive growth effect).

Inflation rates remained subdued in the CEE region in early 2016. In CE, the yearly inflation rate amounts to -0.6% yoy, even lower than the euro area figure of -0.1% in May 2016. In SEE, the yearly inflation rate fell to -2.4% yoy at last count on the back of tax cuts in Romania. Finally, in EE and Turkey, disinflation set in after the devaluation induced high rates in 2015.

In CE, we now expect prices to stagnate this year. In SEE, Romania and Croatia are dragging the country average into negative territory. Ukraine is the outlier, where we increased the inflation forecast to 15.5% (despite a current low of 7.5% in May). For Turkey and Russia, we reduced the 2016 forecast to 7–8%. With the negative drag from energy prices fading in the second half of 2016, we expect 2017 inflation rates to rise substantially in CE/SEE, returning to a range between 1% and slightly above 2%. In the high inflation countries, we expect disinflation to continue, but at a more moderate pace.

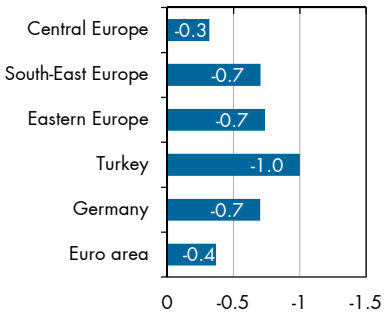
Financial analyst: Andreas Schwabe, CFA, RBI Vienna

CEE GDP growth (% yoy)



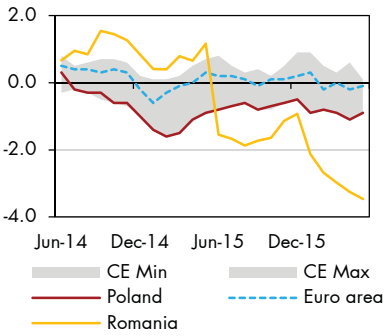
Source: Bloomberg, RBI/Raiffeisen RESEARCH

Change in CPI forecasts for 2016



Source: RBI/Raiffeisen RESEARCH

Recent CPI trend (% yoy)

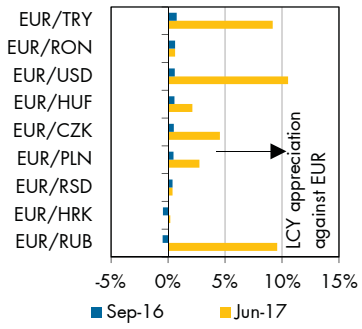


Source: Bloomberg, RBI/Raiffeisen RESEARCH

Focus on: Brexit weighing on CE currencies

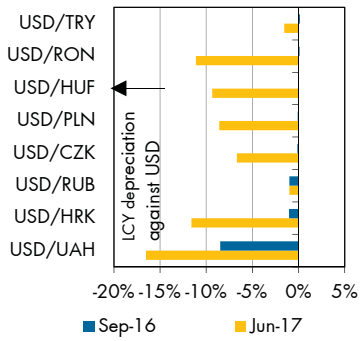
- **Brexit vote burdening CE currencies, PLN remaining CEE risk proxy**
- **CEE FX potential in Q3 limited against both USD and EUR due to political uncertainty**
- **Potential for CE currencies on a 12 month horizon in case of market stabilisation**
- **For 12 months RUB and TRY seen as strongest buys against euro on back of stronger USD**

Projections LCY vs EUR



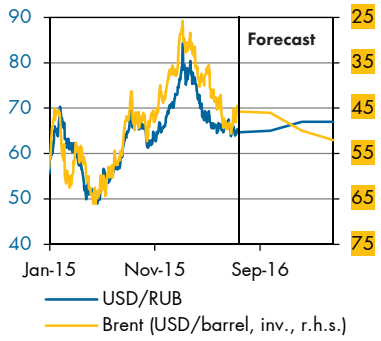
Source: Bloomberg, RBI/Raiffeisen RESEARCH

Projections LCY vs USD



Source: Bloomberg, RBI/Raiffeisen RESEARCH

High RUB/oil correlation



Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Until the Brexit vote caused market jitters at the end of the second quarter the environment for CEE FX rates proved to be more stable than we had originally estimated. Then again, the Polish zloty and the Turkish lira were showing expected depreciation against both the EUR and USD, largely driven by political developments. That said, especially **our call to sell PLN against EUR for Q2 worked out as planned.** Then again, the Russian rouble saw continued strengthening in line with the improving oil prices throughout Q2. Our projection of at least a short-term oil price setback did not materialise, **thus contradicting our call for a RUB setback** during the second quarter. Somewhat more surprising was the development of the Ukrainian hryvnia in this time span, as it was not only showing the expected sideways movement given changes in the government but even saw appreciation against both EUR and USD on hopes for a continuation of the IMF programme and more stable politics going forward.

For the third quarter of 2016, we maintain our cautious view especially with the Brexit decision causing elevated risk aversion and project only some stabilisation potential for CE/SEE currencies versus the euro. We refrain from any buy recommendation given the associated political and economic uncertainties from Brexit with CE currencies most exposed to these risks. That said **our projections for all CE/SEE currencies are neutral towards the euro for Q3.** For **the Russian rouble**, we also expect only a **sideways movement against the euro** supported by both stability in the oil price as well as the expectation of only moderate interest rate cuts. UAH and BYR are projected to return towards their overall depreciation tendencies, thus leaving them with sell recommendations against EUR.

Given our expectation of only sideways movement in the USD against the euro for the third quarter of 2016, the CEE exchange rates are projected to only tread water against the USD as well. **That said we are neutral for all CEE currencies** (excluding UAH and BYR were we have a sell recommendation) **against the USD for the third quarter.**

At a **one-year horizon (until June 2017)**, we would expect to see some calming in Brexit uncertainty and thus some stabilisation in the CE exchange rates. Here, PLN (political stabilisation in the conflict with the EU, more clarity on FX loan conversion and benign economic conditions) **and CZK** (with the expectation of an end to the FX regime in H1 2017 and thus appreciation potential for CZK) **get a buy recommendation against the euro**. Nevertheless, for the 12 month time horizon we would also point at increasing risk with regards to expected normalisation in inflation development, especially given the Brexit uncertainties and possible prolonged accommodative policy by central banks in response. Thus the risk for continuation of the Czech FX regime into H2 2017 could in our view increase, endangering our 12 month CZK call. Given the fairly strong EUR/USD view towards parity at a twelve-month horizon, **the Russian rouble and the Turkish lira get the strongest buy recommendations against the euro**. Accordingly, all CE/SEE exchange rates have a sell recommendation at a twelve-month time horizon against the USD, with a neutral view for RUB and TRY.

Financial analyst: Wolfgang Ernst, RBI Vienna

Mainly high-yielders seem attractive as post-Brexit trades

- **CEE local debt markets weathered Brexit woes quite well recouping initial losses**
- **Flight-to-quality spread widening led to higher risk premiums providing cushion in upcoming volatility period**
- **Whilst room for further gains is limited, we remain mildly bullish on Hungary, especially versus Poland and Romania**
- **Buy recommendation for OFZs & TURKGBs additionally supported by dovish post-Brexit global central bank outlook**

Since our last CEE Debt Market Strategy, **10y OFZ bonds outperformed** their regional equivalents (24/03 to 20/06). The absolute performance was driven by FX gains versus EUR to a greater extent (see chart). The ongoing oil price stability and hardening expectations of a dovish US rate hiking cycle created a favourable global backdrop for high-yielding EMs. The Brexit outcome even added support in form of a more dovish global central bank outlook. On the local scene, the rising likelihood of resumed rate cuts (CBR finally restarted rate cuts in June) was the major driver. Given the considerable year-to-date performance (10y delivered around 16%, half-and-half driven by FX and price component), room for further gains might be limited at our end-September horizon. However, due to our **favourable expectations for EUR/RUB** and the continuation of gradual rate cuts, we see room for a further bull steepening of the inverted yield curve. Nevertheless, the attractiveness for local investors is limited since bonds are trading significantly below money market rates, so we expect that the normalisation of the yield curve shape will be a long time coming. Nevertheless, non-resident yield hunters could develop an appetite for short-dated OFZs. Overall, **we maintain our Buy recommendation for OFZs** that we introduced in our last CEE Debt Market Strategy at the end of May (5% in gains in 10y segment since then).

Our speculative Buy recommendation for 10y TURKGBs as of the end of May has played out also fairly well as the market recouped the initial losses after the Brexit vote. Barring the favourable overall EM backdrop, the continuation of MP easing/simplification should **keep demand for lira bonds alive**. The Turkish central bank cut the upper boundary of its interest rate corridor for the fourth straight month in June by another 50bp. The current 7.25–9.00% o/n corridor surrounds the 7.50% key rate asymmetrically, so we expect a further cut in the o/n lending rate by some 100bp in the months to come. The TCMB is expected to walk the talk and further simplify its MP toolkit and finally return to a single rate. The weighted average costs of funding currently stand at around 8.30% – reflecting monetary conditions better than the 7.50% base rate – and should fall further. **We maintain our Buy recommendation for Turkish bonds** against the backdrop of ongoing MP support (both globally and locally), further disinflation, and easing external event risks.

By contrast, the major risk to our broadly constructive view on CE/SEE debt markets at the end-September horizon is another sell-off in core euro area (EA) yields. This could be triggered by a possible overreaction to reaccelerating EA inflation growth in early H2 2016, but the **current post-Brexit flight-to-quality mode** decreased the likelihood of such a scenario at least in the short term. There is still a significant risk buffer in place (see chart), serving as a potential cushion in case of external shocks. At the same time, **room for CE local debt markets to extend the recent post-Brexit relief rally is limited** in our view. Nevertheless, we continue to favour back-end HGBs outright, but also versus Poland and Romania as a relative play given the politics-related worsening of the credit profiles of the latter two compared with Hungary.

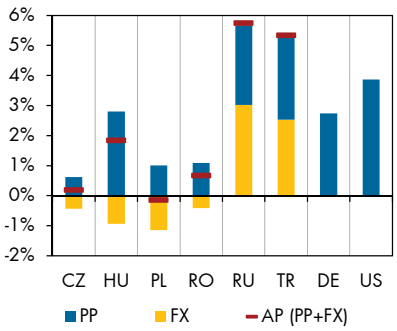
Financial analyst: Stephan Imre, RBI Vienna

Market strategy (until Sep-16)*

	LCY Bonds		FX
	2y	10y	–
CZ	H (H)	H (H)	H (H)
HU	H (H)**	B (B)	H (H)
PL	H (H)	H (H)	H (H)
RO	H (H)	H (H)	H (H)
RU	B (H)	B(H)	H (H)
TR	B (H)	B (H)	H (H)

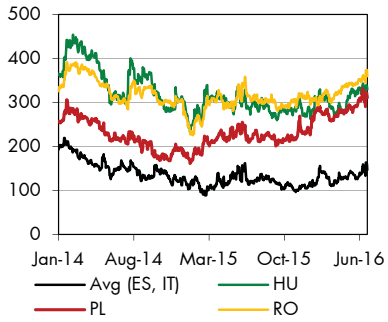
**LCY bonds: based on absolute performance in LCY*
***HU: 3y, not 2y tenor; previous recomm. (as of 30 May-2016 in our CEE Debt Market Strategy) in brackets;* **FX** *vs. EUR; B: Buy; H: Hold; S: Sell*
Source: RBI/Raiffeisen RESEARCH

Historical performance 10y LCY bond*



**between 30-May-16 and 28-Jun-16*
FX: currency performance (chg LCY/EUR)
PP: bond performance (price chg + carry)
AP: absolute performance (PP + FX)
DE and US: Only price performance (PP)
Source: Bloomberg, RBI/Raiffeisen RESEARCH

10y spread over Bunds (bp)

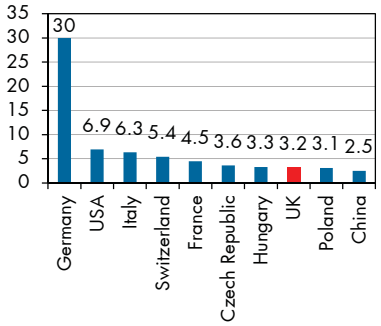


ES 5y high: 633; 5y low: 89
PL 5y high: 442; 5y low: 161
HU 5y high: 879; 5y low: 233
RO 5y high: 591; 5y low: 226
Source: Bloomberg, RBI/Raiffeisen RESEARCH

Economy slowly picking up speed

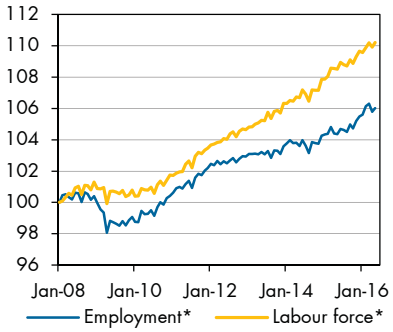
- **Improving economic dynamics in the first quarter of 2016**
- **Brexit with only minor implications for business cycle dynamics**
- **Private consumption benefiting from tax reform**
- **Domestic demand still primary driver**

Exports*: Not overly exposed to the UK



** share (%, 2015) of total Austrian goods exports*
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Labour force continues growing



** indexed, seasonally adjusted, Jan. 08 = 100*
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

The **growth of the economy accelerated** at the beginning of the year. While real GDP expanded by 0.3% qoq on average in 2015, it advanced by 0.5% qoq in the first quarter of this year. After a long period of stagnation, private consumption also showed signs of life for the first time again with growth of 0.3% qoq, likely thanks to the tax reform that took effect on 1 January 2016. The positive trend in equipment investment that has been observed for a number of quarters now persisted at the beginning of the year. As imports continued to grow at a higher pace than exports, foreign trade again made a negative contribution to quarterly GDP growth in Q1. This means that business cycle dynamics in the first three months of this year were again **driven by domestic demand**.

As for every other euro area economy, the **UK´s vote to leave the EU** constitutes a challenge also for Austria. Having said that, economic activity is not expected to face a material deterioration as a result of last week´s vote, despite the fact that exports to the UK should suffer noticeably. This is because Austria´s external sector is less exposed to the UK than in most other euro area countries (merely 8th most important trading partner in terms of goods exports), although this comes at a time when goods exports to the UK were growing considerably faster than overall goods exports (2015 UK exports: 6.0% yoy, total: 2.7% yoy). Thus, while exports to the UK should face a setback, the overall **effect on business cycle dynamics should be rather limited**. Apart from the direct implications, Austria could also be affected via reduced investment activity due to a period of prolonged and intensifying political uncertainty. However, while we assume political uncertainty to be there for some time, we do not expect an escalation and similar referenda in other countries in our current base case scenario. All in all, we do not see a reason for adjusting our real GDP forecast for 2016 (+1.4% yoy) due to the Brexit vote and opt only for a marginally more cautious stance concerning next year´s forecast (downward revision from 1.4% yoy to 1.3% yoy). This holds all the more true as our business cycle outlook has been rather cautious already prior to the Brexit vote.

Key economic figures and forecasts

	2014	2015	2016e	2017f
Real GDP (% yoy)	0.4	0.9	1.4	1.3
Trade balance (goods and services, EUR bn)	12.4	14.7	14.4	13.6
Current account balance (% of GDP)	1.9	2.6	2.5	2.2
General budget balance (% of GDP)	-2.7	-1.2	-1.9	-1.8
Public debt (% of GDP)	84.3	86.2	85.3	84.0
Unemployment rate (avg, %, EU definition)	5.6	5.7	6.2	6.4
Employment (% yoy)	0.6	0.9	1.3	1.2
Consumer prices (avg, % yoy)	1.5	0.8	1.2	2.2
Real wages (% yoy)	0.9	1.3	0.4	-0.4
Unit labour costs (% yoy)	2.3	1.4	1.5	1.7

Source: Statistics Austria, Thomson Reuters, RBI/Raiffeisen RESEARCH

Domestic demand is likely to play a key role in the expected continuation of the economic recovery also in the coming quarters. In addition to government transfer payments to asylum seekers, the reduction in income tax brought by the tax reform that went into force at the beginning of the year is still the main argument for the noticeably higher growth rates (% yoy) expected for real **private consumption** in 2016 and 2017. Gross fixed capital formation was impacted in recent years by astonishingly weak construction investment on the one hand and by an uptick in equipment investment that began in the first half of 2015 on the other hand. The recovery of gross fixed capital formation that is expected for 2016 and 2017 is projected to be fuelled in large parts by equipment investment. But construction investment should finally also support gross fixed capital formation for the first time since 2012 this year. By contrast, **foreign trade** is not expected to make any contribution to GDP growth in 2016 or 2017. This is because only moderately increasing exports (UK as a burden) should be offset by more rapid import growth mirroring solid domestic demand.

There is still good news and bad news on the **labour market.** The level of employment grew by an average of 1.5% yoy in the first five months of the year, accelerating slightly compared to the average of 2015 (0.9% yoy). The number of vacant positions is also at a high level. At the same time, seasonally adjusted unemployment is still on the rise. This means that the increase in employment is not sufficient to offset the growth of the labour force. This is likely to change little over the entire forecast horizon, which means that unemployment will probably increase further.

Inflation (HICP) came down from 1.4% yoy in January to 0.6% yoy in May. The inflation difference to the euro area as a whole has also narrowed, but is still elevated at 0.7 percentage points. Inflation (% yoy) is likely to increase noticeably in the second half of the year, largely due to the development of the oil price. But even when this effect (which will be felt in the entire euro area) is excluded, the underlying inflationary pressure is likely to remain higher in Austria than in the currency union.

Financial analyst: Matthias Reith, RBI Vienna

GDP: Value added by sector

Change (% yoy, in real terms)	2014	2015	2016e	2017f
Agriculture & forestry	4.1	-6.7	0.0	0.0
Prod. of goods/mining	1.1	1.2	1.8	1.9
Energy/water supply	2.6	2.2	1.5	1.3
Construction	-2.0	0.0	1.0	1.4
Wholesale and retail trade	-0.5	1.7	2.2	2.3
Transportation	-1.1	-0.7	0.2	1.3
Accom. & restaurant trade	0.6	0.6	1.7	1.8
Information and communication	-2.7	-1.7	0.0	0.8
Credit and insurance	-1.5	-0.2	0.3	0.5
Property & business services	2.8	2.4	2.2	2.3
Other economic services	1.2	-1.3	1.0	2.0
Public sector	-0.2	0.4	0.9	1.0
Healthcare, social services	-0.2	1.9	2.2	1.8
Other services	0.4	1.3	1.5	1.4
Gross domestic product	0.4	0.9	1.4	1.3

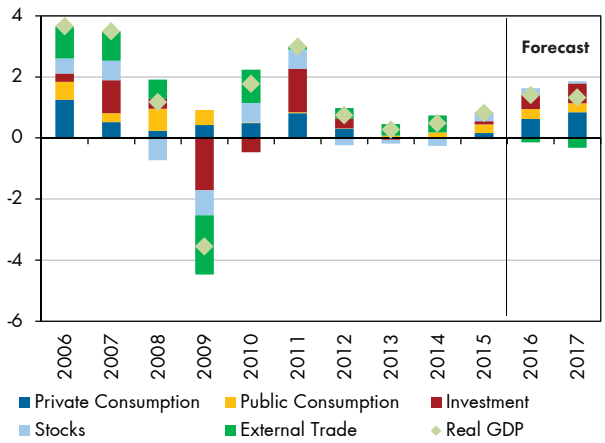
Source: Statistics Austria, RBI/Raiffeisen RESEARCH

GDP: Expenditure composition

Change (% yoy, in real terms)	2014	2015	2016e	2017f
Private consumption	0.0	0.4	1.2	1.6
Public consumption	0.8	1.4	1.6	1.5
Gross fixed capital formation	-0.2	0.5	2.1	2.9
Equipment	1.3	2.8	3.3	4.5
Construction	-1.0	-1.2	1.2	1.6
Exports	2.1	1.7	2.8	2.5
Imports	1.3	1.7	3.3	3.4
Gross domestic product	0.4	0.9	1.4	1.3

Source: Statistics Austria, Thomson Reuters, RBI/Raiffeisen RESEARCH

Contributions* to real GDP growth (yoy)

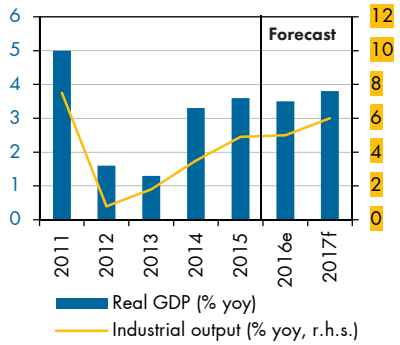


** in percentage points*
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Private consumption as the main growth driver

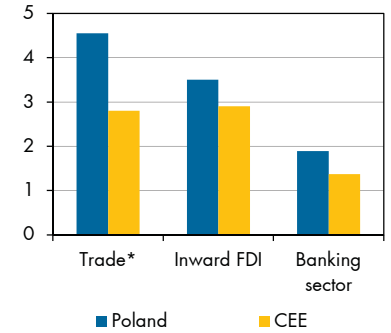
- **Fiscal stimulus to support private consumption**
- **Stubborn but harmless deflation keeping the MPC in wait-and-see mode**
- **PLN remaining susceptible for weakening, despite some stabilisation potential**
- **We maintain "Hold POLGBs" due to significant risk premiums**

Real GDP (% yoy)



Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

PL: UK-gearing (% of total)**



** export and import share*
*** 2014 or 2015 data*
Source: national sources, BIS, RBI/Raiffeisen RESEARCH

Economic outlook

Political change has shifted uncertainty regarding taxes and the overall internal economic environment. This strengthened the negative impact from the pause in EU funds absorption and caused fixed capital formation to decline by almost 2% yoy in Q1. Thus, the role of private consumption as the driver of GDP growth even increased. Private consumption is still benefitting from the strongly improving labour market (with unemployment already close to its historical low), low fuel and energy costs, and improving consumer sentiment which is already close to historical highs.

Apart from strong fundamentals, private consumption should be additionally boosted by a looser fiscal policy with a new bonus for children being introduced in April. We estimate its value at almost 2% of private consumption. Due to the still low savings rate, the majority of new funds might rather be spent than saved by households. This might even boost private consumption growth to 5% at the turn of the year. With additional support from public spending and a modest upward trend in investment activity, **GDP growth should gather strength and come close to 4% yoy in H2**. It must be stressed, however, that this optimistic scenario is currently at risk due to an increasingly challenging global environment (Brexit, potential fallout on the European economic cycle). That said there is a risk that lower investment activity and a rising propensity to save (at the expense of lower private consumption) will dampen the prospects for the Polish economy compared to our pre-Brexit take.

Despite the still strong internal demand and closed output gap, deflation is still stubborn. Oil prices remain the key issue and will determine if the currently expected scenario of CPI returning to positive values in Q4 this year will materialise. As there are no visible signs of any negative impact from deflation on the economy, **the MPC is sticking to its wait and see bias**, and we expect this stance

Key economic figures and forecasts

	2011	2012	2013	2014	2015	2016e	2017f
Nominal GDP (EUR bn)	380.2	389.4	394.8	410.7	427.9	426.0	460.0
Real GDP (% yoy)	5.0	1.6	1.3	3.3	3.6	3.5	3.8
Industrial output (% yoy)	7.5	0.8	1.8	3.5	4.9	5.0	6.0
Unemployment rate (avg, %)	12.4	12.8	13.5	12.3	10.5	9.1	8.6
Nominal industrial wages (% yoy)	5.0	3.4	2.9	3.7	3.5	4.5	4.5
Producer prices (avg, % yoy)	7.6	3.3	-1.3	-1.5	-1.7	0.8	2.0
Consumer prices (avg, % yoy)	4.3	3.7	0.9	0.0	-0.9	-0.4	1.7
Consumer prices (eop, % yoy)	4.6	2.4	0.7	-1.0	-0.5	1.5	1.8
General budget balance (% of GDP)	-4.9	-3.7	-4.0	-3.3	-2.6	-2.9	-3.4
Public debt (% of GDP)	54.8	54.4	55.7	50.5	51.3	52.1	52.6
Current account balance (% of GDP)	-5.1	-3.5	-1.3	-2.0	-0.2	-0.9	-1.2
Official FX reserves (EUR bn)	75.4	82.6	77.1	83.0	87.4	92.0	85.0
Gross foreign debt (% of GDP)	65.8	71.4	70.4	71.1	70.1	74.2	73.9
EUR/PLN (avg)	4.1	4.2	4.2	4.2	4.2	4.4	4.3
USD/PLN (avg)	3.0	3.3	3.2	3.2	3.8	4.0	4.2

Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

to continue **for the next 12 months**. Although Poland has the largest UK gearing among the CE economies we do not expect that the potential fallout will be sufficient to change the monetary policy stance.

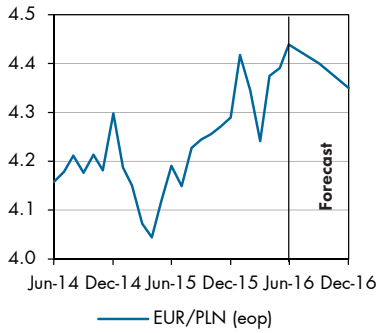
Financial market outlook

Quarrels with the EU, the unresolved FX loan conversion, and the Brexit decision have weighed negatively on the zloty during the second quarter, driving the zloty down to levels around 4.45–4.50 against the euro. Comparing the zloty movement in the second quarter with its peers makes the underperformance of the PLN during this period obvious. Then again, with the mentioned negative implications already priced into the zloty and the overall benign economic conditions expected to prevail in Poland, we see some moderate room for improvement once these political uncertainties abate in the coming months. Then again, investors should be aware of **continued elevated volatility in the zloty,** not only due to the aforementioned uncertainty that should especially weigh on the PLN in the near term but also given that the PLN remains a currency susceptible to external risk developments and a CEE risk proxy.

In the run-up to the Brexit referendum, Polish bonds lost more ground in comparison with regional peers. The 10y yield spread over lower-rated Hungarian equivalents almost vanished again in mid-June since market participants regarded zloty assets as relatively more exposed to Brexit risks (also due to technical reasons in the form of more liquid market conditions). However, following the Brexit vote, the market managed to recoup losses and pricing on Poland's LCY debt market is now refocusing on local factors. Indeed, Poland is facing a negative rating drift mainly due to local political risks. A lot will depend on the **final version of the FX loan conversion scheme** to be presented in the next few months and the developments in terms of the EU dispute regarding the Polish rule of law etc. However, we continue to note that a certain risk premium is still in place in Poland. This becomes all the more visible when compared with the abnormally low levels that we saw in early 2015 following the ECB QE euphoria rally. Hence, these widened spreads should be regarded as a normalisation process vis-á-vis core debt markets. Looking ahead, **we maintain our Hold recommendation for Polish bonds for our end-September horizon**, even with some potential for moderate gains in the cards given the stable base rate outlook and our FX strategists' expectations of a moderate PLN recovery versus the EUR in the same investment horizon.

Financial analysts: Marta Petka-Zagajewska, Raiffeisen Polbank, Warsaw
Stephan Imre, RBI Vienna

Exchange rate development



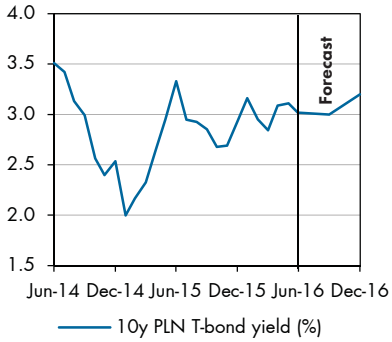
EUR/PLN: 5y high 4.56, 5y low 3.93
Source: Bloomberg, RBI/Raiffeisen RESEARCH

Exchange rate forecasts

	28-Jun[1]	Sep-16	Dec-16	Mar-17	Jun-17
EUR/PLN	4.44	4.40	4.35	4.30	4.30
Cons.		*4.35*	*4.33*	*4.28*	*4.29*
USD/PLN	4.02	4.00	4.14	4.17	4.34
Cons.		*3.91*	*3.91*	*3.94*	*3.96*

[1] 5:00 p.m. (CEST)
Source: Bloomberg, RBI/Raiffeisen RESEARCH

PLN yield development (%)



10y PLN T-bond yield: 5y high 6.11, 5y low 2.00
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Interest rate forecasts (%)

	28-Jun[1]	Sep-16	Dec-16	Mar-17	Jun-17
Key rate	1.50	1.50	1.50	1.50	1.50
Consensus		*1.35*	*1.30*	*1.25*	*1.40*
1 month[2]	1.65	1.55	1.55	1.55	1.55
3 month[2]	1.71	1.65	1.65	1.65	1.65
Consensus		*1.70*	*1.71*	*1.72*	*1.76*
6 month[2]	1.79	1.75	1.75	1.75	1.75
12 month[2]	1.81	1.80	1.80	1.80	1.80

[1] 5:00 p.m. (CEST) [2] Offered rate
Source: Bloomberg, RBI/Raiffeisen RESEARCH

Yield forecasts (%)

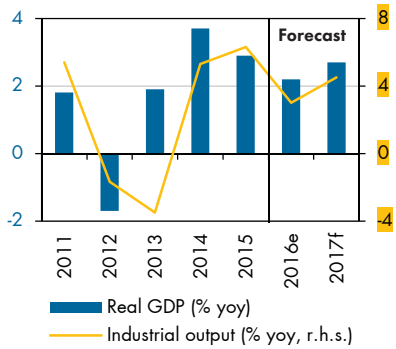
	28-Jun[1]	Sep-16	Dec-16	Mar-17	Jun-17
2y T-bond[2]	1.68	1.8	1.9	2.0	2.1
Consensus		*1.5*	*1.6*	*1.6*	*1.8*
10y T-bond[2]	3.02	3.0	3.2	3.3	3.5
Consensus		*3.1*	*3.1*	*3.2*	*3.3*

[1] 5:00 p.m. (CEST) [2] Bid yield
Source: Bloomberg, RBI/Raiffeisen RESEARCH

Watch out for fast wage increases

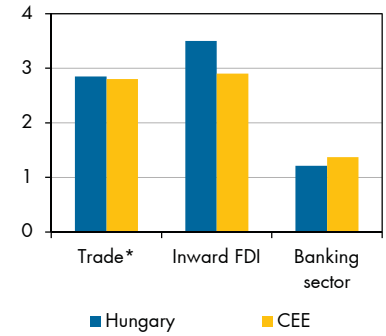
- **Q1 growth surprised on the downside driven by one-off items**
- **Strong household consumption remains the main growth driver**
- **Wage increase may accelerate further – might become a concern soon**
- **Key rate bottoms out at 0.9% – and should stay there for a long period of time**

Real GDP (% yoy)



Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

HU: UK-gearing (% of total)**



** export and import share*
*** 2014 or 2015 data*
Source: national sources, BIS, RBI/Raiffeisen RESEARCH

Economic outlook

The economy slowed in Q1, with GDP growth coming in at a mere 0.9% yoy. The weak performance was explained by the drastic contraction of construction industry output (this was driven by the base effect – high EU fund absorption in Q1 2015 and poor utilisation of EU funds in Q1 2016) and the waning of growth in the automobile industry. As these items are definitely temporary, the outlook is still okay and **we expect rebounding growth rates in the coming quarters and keep our 2.2% GDP forecast unchanged for 2016**. One should not be too concerned about the near-term growth prospects, especially because of the steadily rising household demand. The financial situation of households is improving mainly thanks to labour market developments. Employment indicators are at their peaks, not only since the crisis but also in pre-crisis comparison, and the **unemployment rate is at a record low of 6%**. This is being helped by the rising migration outflow (approximately 400,000 Hungarians are working abroad) and ongoing public work schemes (which employ 200,000 persons). At the same time, demand for labour is rising. Given the weaknesses of the labour supply, this translates into labour shortages and rising wages. The government is also moving forward with long-term salary increase programmes in the public sector (for example, health sector employees are being offered a 60% wage increase in the next three years). There is certainly sufficient room for such measures in the public budget as the cumulated budget deficit is close to zero after the first five months thanks to increasing tax receipts. Other fiscal measures are targeting at increasing public infrastructure developments in order to stimulate economic growth and to bring GDP growth to 2.7% in 2017. However, Brexit-related downsides may challenge the medium-term outlook, mostly via a shallower European economic recovery cycle. As export-oriented economy Hungary is fairly exposed to the European cycle and some sectors, like car manufacturing or pharmaceuticals, which may suffer within our post-Brexit scenario.

Key economic figures and forecasts

	2011	2012	2013	2014	2015	2016e	2017f
Nominal GDP (EUR bn)	100.7	99.0	101.3	104.2	108.8	111.6	120.4
Real GDP (% yoy)	1.8	-1.7	1.9	3.7	2.9	2.2	2.7
Industrial output (% yoy)	5.4	-1.7	-3.5	5.3	6.3	3.0	4.5
Unemployment rate (avg, %)	11.0	10.9	10.3	7.9	7.0	6.2	5.7
Nominal industrial wages (% yoy)	6.2	-0.7	4.4	4.0	5.3	7.5	8.0
Producer prices (avg, % yoy)	4.3	4.3	0.7	-0.4	-0.7	-1.0	3.0
Consumer prices (avg, % yoy)	3.9	5.7	1.7	-0.2	0.0	0.4	2.2
Consumer prices (eop, % yoy)	4.1	5.0	0.4	-0.9	0.9	1.6	2.0
General budget balance (% of GDP)	4.2	-2.1	-2.3	-2.5	-2.0	-2.2	-2.7
Public debt (% of GDP)	81.0	78.3	76.8	76.2	75.5	74.9	74.5
Current account balance (% of GDP)	0.7	1.9	4.1	3.9	4.4	4.5	4.1
Official FX reserves (EUR bn)	37.6	33.9	33.8	34.7	30.5	26.0	24.0
Gross foreign debt (% of GDP)	134.5	128.5	117.6	113.9	105.7	98.5	87.2
EUR/HUF (avg)	279.4	289.2	296.8	308.7	309.9	314.8	308.8
USD/HUF (avg)	201.2	225.1	223.6	232.8	279.4	286.2	305.7

Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Financial market outlook

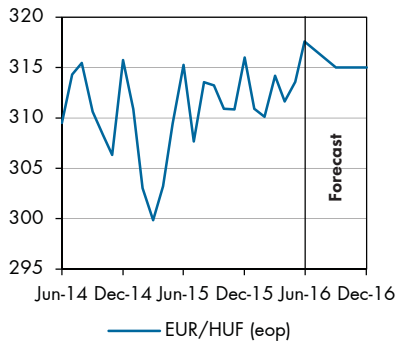
The National Bank of Hungary (MNB) launched a new rate cutting cycle in March. The key rate was lowered three times (by 15bp each) and bottomed out at 0.9%. With the last cut, Hungarian rate-setters said that the inflation outlook and the cyclical position of the real economy point to leaving the base rate unchanged for an extended period of time. Of course, it does not specify how long the benchmark rate is to remain on hold, but we expect the **current rate to stay in place well into 2018**. Furthermore, in case of a need for further stimulus, the MNB can still push the rate corridor even lower, or it can reduce the amount of money the banks can park in 3m deposit as excess liquidity. For the effectiveness of both, the interbank money market would need to improve further. That is why the MNB took steps in the past few months towards creating an active BUBOR market. Overall, for the foreseeable future, we see scope for only modest fine-tuning actions as mentioned above.

The end of the rate cutting cycle contributed to terminating the previous bullish positioning on the HGB market. While Fitch Ratings eventually upgraded Hungary to investment grade, the government's recent twist towards fiscal loosening will likely cause the other two major rating agencies to hold off. While this alone would signal a further rise in yields on the HGB market, the ECB's asset purchases (which are tightening the market for attractively yielding bonds not only in the euro area but also in the emerging markets) should keep **steady demand for HUF assets** in place and continue luring non-residents to HGBs again after a prolonged period of net outflows. As the reaction to the Brexit vote showed – HGBs recouped the initial losses in post-Brexit trading completely – the market seems quite resilient to external shocks. Overall, **we maintain our mildly bullish view on HGBs** due to the attractive yield pickup against the backdrop of a still favourable credit story (if not overdone) despite the recent fiscal relaxation.

As a result of the upgrade and the end of monetary easing, the HUF appreciated somewhat against the EUR, so much so that EUR/HUF just touched the lower edge of the well-known 310–315 trading range for the first time in April, but then quickly returned to the upper end. In the short-term especially the Brexit vote has potential to keep HUF at the weaker end of its trading range. So all in all, **the exchange rate remained within the range, and we do not see any reason why it should move away significantly** from there in the short run. Some market participants may pay special attention to the fact that the MNB is already much more tolerant of HUF appreciation, but since May's rate decision they have not had a chance to see whether the hypothetical floor at 308 remains in place or not. In this context, we see no big changes ahead in the trend that indicates stability around recent levels for the coming months.

Financial analysts: Zoltán Török, Gergely Pálffy, Raiffeisen Bank Zrt., Budapest

Exchange rate development



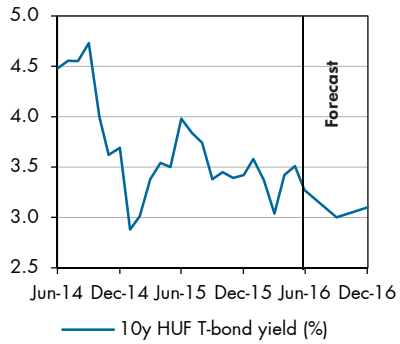
EUR/HUF: 5y high 321.02, 5y low 262.04
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Exchange rate forecasts

	28-Jun[1]	Sep-16	Dec-16	Mar-17	Jun-17
EUR/HUF	317.58	315	315	310	310
Cons.		*315.0*	*317.0*	*313.5*	*313.0*
USD/HUF	287.39	286	300	301	313
Cons.		*281.0*	*282.0*	*284.0*	*285.5*

[1] 5:00 p.m. (CEST)
Source: Bloomberg, RBI/Raiffeisen RESEARCH

HUF yield development (%)



10y HUF T-bond yield: 5y high 10.83, 5y low 2.82
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Interest rate forecasts (%)

	28-Jun[1]	Sep-16	Dec-16	Mar-17	Jun-17
Key rate	0.90	0.90	0.90	0.90	0.90
Consensus		*0.85*	*0.80*	*0.80*	*0.90*
1 month[2]	1.01	1.05	1.05	1.10	1.05
3 month[2]	1.01	1.05	1.05	1.10	1.05
Consensus		*1.12*	*0.94*	*1.17*	*1.23*
6 month[2]	0.96	1.10	1.10	1.10	1.10
12 month[2]	0.96	1.10	1.10	1.10	1.10

[1] 5:00 p.m. (CEST) [2] Offered rate
Source: Bloomberg, RBI/Raiffeisen RESEARCH

Yield forecasts (%)

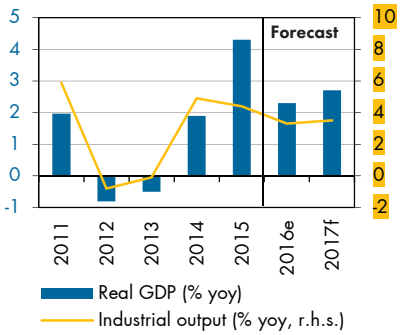
	28-Jun[1]	Sep-16	Dec-16	Mar-17	Jun-17
3y T-bond[2]	1.91	1.8	1.9	1.9	2.2
Consensus		*n.v.*	*n.v.*	*n.v.*	*n.v.*
10y T-bond[2]	3.27	3.0	3.1	3.3	3.6
Consensus		*3.29*	*3.27*	*3.44*	*3.61*

[1] 5:00 p.m. (CEST) [2] Bid yield
Source: Bloomberg, RBI/Raiffeisen RESEARCH

Household consumption compensates drop in public investments

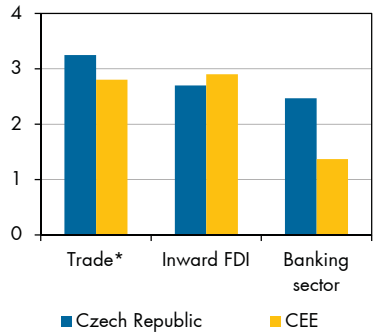
- **Unemployment is lowest in Europe and already below its natural level**
- **Continuing energy outages negatively weigh on industrial production**
- **Very favourable external balance argues for stronger CZK, FX floor vivid until mid-2017**
- **CZK government debt will stay well supported**

Real GDP (% yoy)



Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

CZ: UK-gearing (% of total)**



** export and import share*
*** 2014 or 2015 data*
Source: national sources, BIS, RBI/Raiffeisen RESEARCH

Economic outlook

After exceptionally strong economic growth in 2015 the Czech economy decelerated to 3% in the first quarter 2016, mainly due to lower public investments. Strong household consumption partially compensated for the decline in public investments. The unemployment rate is currently at the lowest level in Europe (4.1%) and the share of unemployed people between15-64y declined to the lowest level since 2009. Firms already complain about a lack of qualified job applicants, which pressures employers to raise wages. Solid wage growth was visible already in Q1 2016 when average nominal wage accelerated above 4% yoy. We expect wage growth to be above 4% yoy (on average) this year.

Faster drawings from the old EU funds programme helped the Czech Republic boost its GDP to 4.3% last year but this year drawing from the new EU funds programme will begin only gradually. Therefore we **expect the Czech economy to decelerate towards 2.3% yoy**. Household consumption will be the key driver of economic growth as higher wages, slowly raising inflation and still high consumer confidence should further boost consumer spending. Private investments have potential for positive surprise if current (almost) stagnating labour productivity revives and helps to attract more investors. According to latest business cycle surveys firms expect increase in investments but mostly into newer facilities rather than an expansion of production. Energy outages still negatively weigh on industrial production. External environment remains very favourable for the Czech economy with both current account and trade balance reaching for record high surpluses. Faster wage growth and the currently raising oil prices should wake up currently low inflation (0.1% in May). **Inflation will probably reach the 2% inflation target at the beginning 2017**. However, Brexit-related risks to the European recovery (possibly also the reflation outlook) may challenge our rather upbeat (pre-Brexit) assessment of the Czech economic outlook.

Financial analysts: *Daniela Milučká, Raiffeisenbank a.s., Prague*

Key economic figures and forecasts

	2011	2012	2013	2014	2015	2016e	2017f
Nominal GDP (EUR bn)	163.5	160.8	156.9	154.7	163.9	170.9	182.7
Real GDP (% yoy)	2.0	-0.8	-0.5	1.9	4.3	2.3	2.7
Industrial output (% yoy)	5.9	-0.8	-0.1	4.9	4.4	3.3	3.5
Unemployment rate (avg, %)	6.7	6.8	7.7	7.7	6.5	5.6	5.4
Nominal industrial wages (% yoy)	3.5	3.2	1.0	2.9	3.0	4.1	4.0
Producer prices (avg, % yoy)	5.6	2.1	0.8	-0.8	-3.2	-3.2	2.2
Consumer prices (avg, % yoy)	1.9	3.3	1.4	0.4	0.3	0.7	1.7
Consumer prices (eop, % yoy)	2.4	2.4	1.4	0.1	0.1	1.8	1.7
General budget balance (% of GDP)	-2.9	-3.9	-1.3	-1.9	-0.4	-0.3	-0.2
Public debt (% of GDP)	41.0	44.7	45.1	42.7	41.1	40.3	39.1
Current account balance (% of GDP)	-2.1	-1.6	-0.5	0.2	0.9	1.4	1.0
Official FX reserves (EUR bn)	31.0	34.0	40.8	45.0	59.4	83.6	104.1
Gross foreign debt (% of GDP)	54.8	60.2	63.5	66.6	70.7	74.6	78.1
EUR/CZK (avg)	24.6	25.1	26.0	27.5	27.3	27.0	26.4
USD/CZK (avg)	17.7	19.6	19.6	20.8	24.6	24.6	26.1

Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Financial market outlook

The Czech National Bank (CNB) continues intervening on the FX market keeping the EUR/CZK floor at 27.0. As the economy has been growing solidly, foreign capital inflows continued. Therefore the CNB has continued intervening on the FX market, increasing FX reserves to above EUR 65 bn from below EUR 50 bn one year ago. We expect that at the beginning of next year the level of FX reserves will rise to above EUR 80 bn i.e. around 50% of the GDP.

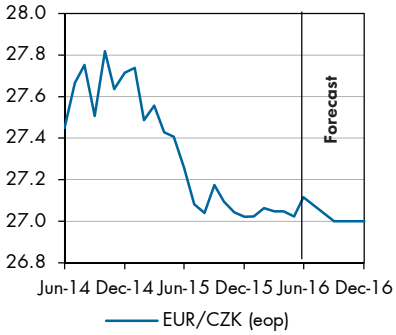
As widely expected CNB board member and former Prime Minister Jiri Rusnok was named the new CNB governor. We do not think that the change within the CNB board will have a significant implication for the support of the current FX commitment. The key variable for the CNB is the inflation outlook. Despite the increased Brexit-related risks to our call, we continue to think, that at the beginning of 2017 the inflation rate will increase towards the 2% target. We also stick to our baseline scenario that the CNB might finally decide to let the CZK appreciate below EUR/CZK 27.0 around mid-2017. But the risks currently are skewed somewhat towards even further postponement of FX regime abandoning due also to a prolongation of the accommodative ECB policy after the Brexit decision. However, we do not expect a new explicit floor, but in case of strong appreciation the CNB will very likely continue intervening. As the market will be distorted by the precedent/continuing CNB interventions the CZK might in fact shortly depreciate to weaker levels above EUR/CZK 27.0. Above all we would **therefore warn of a significant rise of EUR/CZK volatility by that time**.

In case the speculative pressure on CZK is too strong (above EUR 5 bn intervention needs per month), the CNB might decide to cut the deposit interest rate into negative territory for a short period of time. As mentioned also by CNB board members, for that case the negative deposit rate would be applied probably only to new foreign capital inflows. Therefore, although the negative interest rates are not a part of our base case scenario, the probability **of an introduction of a selective deposit rate might be close to 50 %**.

The budget deficit in 2015 was only 0.4% of the GDP and for this year we could see a similar outcome. Given the very low government bond yield levels, the position of the Czech Ministry of Finance remains very favourable. Czech government bond yields were relatively stable over the last quarter. Due to the speculation on the future CZK strengthening CZGB's are being supported from abroad. The share of holdings of the CZGBs by non-residents on total outstanding amounts has increased to above 22% up from 14% a year ago. Until H1 2017 we think this trend will prevail and the CZGB yield spread over German benchmarks will stay low, especially as the Czech market should maintain its regional save haven status due to Brexit-related uncertainty.

Financial analysts: *Michal Brozka, Raiffeisenbank a.s., Prague*

Exchange rate development



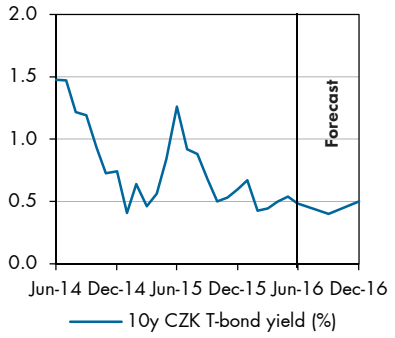
EUR/CZK: 5y high 28.35, 5y low 24.08
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Exchange rate forecasts

	28-Jun[1]	Sep-16	Dec-16	Mar-17	Jun-17
EUR/CZK	27.12	27.00	27.00	27.00	25.90
Cons.		*27.00*	*27.00*	*27.00*	*27.00*
USD/CZK	24.54	24.55	25.71	26.21	26.16
Cons.		*24.25*	*24.50*	*24.56*	*24.97*

[1] *5:00 p.m. (CEST)*
Source: Bloomberg, RBI/Raiffeisen RESEARCH

CZK yield development (%)



10y CZK T-bond yield: 5y high 4.45, 5y low 0.36
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Interest rate forecasts (%)

	28-Jun[1]	Sep-16	Dec-16	Mar-17	Jun-17
Key rate	0.05	0.05	0.05	0.05	0.05
Consensus		*0.05*	*0.10*	*0.05*	*0.10*
1 month[2]	0.20	0.22	0.22	0.20	0.20
3 month[2]	0.29	0.30	0.30	0.30	0.30
Consensus		*0.27*	*0.26*	*0.26*	*0.27*
6 month[2]	0.36	0.40	0.40	0.45	0.50
12 month[2]	0.45	0.50	0.53	0.55	0.60

[1] *5:00 p.m. (CEST)* [2] *Offered rate*
Source: Bloomberg, RBI/Raiffeisen RESEARCH

Yield forecasts (%)

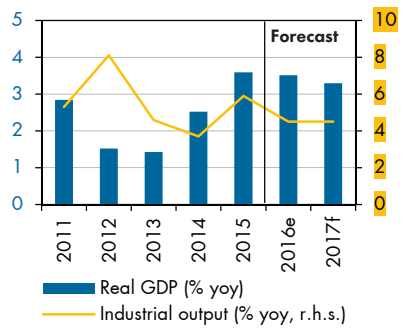
	28-Jun[1]	Sep-16	Dec-16	Mar-17	Jun-17
2y T-bond	-0.08	-0.3	-0.4	-0.4	0.0
Consensus		*-0.1*	*-0.2*	*-0.2*	*0.0*
10y T-bond	0.49	0.4	0.5	0.6	0.7
Consensus		*0.5*	*0.6*	*0.8*	*0.9*

[1] *5:00 p.m. (CEST)*
Source: Bloomberg, RBI/Raiffeisen RESEARCH

Strong economy

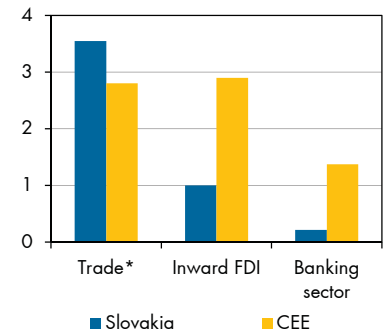
- **New government (again) has optimistic budget plan**
- **Acceleration of household demand**
- **Economy is closing negative output gap**
- **ECB bond purchases keeping Slovak yields steady**

Real GDP (% yoy)



Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

SK: UK-gearing (% of total)**



** export and import share*
*** 2014 or 2015 data*
Source: national sources, BIS, RBI/Raiffeisen RESEARCH

Political and economic outlook

The newly elected coalition government consists of four parties: the dominant party SMER, the partially transformed ex-nationalist SNS party, the Hungarian Most-Híd party, and SIET, which was considered the leader of the right parties shortly before the election but which suffered the biggest losses compared with the opinion polls. The government manifesto has nice ideas and targets, but we are a bit sceptical with regards to its implementation. The government plans to decrease the corporate tax rate to 21% from 22% and to continue fighting tax evasion. They plan to introduce far-reaching reforms in the education and health-care systems. The first draft should be finished by the end of 2016.

In Q1 2016, real GDP went up by 3.4% yoy and by 0.8% qoq. Due to sluggish foreign demand, exports and imports were mostly stable compared with last year. The growth of the Slovak economy was fuelled mainly by household demand (2.5% yoy) and government spending (3.1% yoy). As expected, investment growth has rapidly slowed from previous double-digit values to 1.5% yoy due to missing EU funds. Construction output fell noticeably in monthly terms back to the level observed in 2014. Despite the favourable financial conditions, household are still reluctant to spend money and the savings rate of households is continuously increasing to historical highs. Nevertheless, **we expect a further acceleration of household demand in the next quarters and forecast 3.5% yoy real GDP growth for 2016.**

Economic growth is having a very positive effect on the labour market. In Q1 2016, employment according to the local method rose at the fastest rate since 2008 (2.9% yoy). Nominal wages increased by 3.3% yoy and 3.8% in real terms in the same period. However, the statistics on tax and social contribution revenues suggest much faster wage growth (around 5%), which is more in line with the high deposit growth. Unemployment decreased to 10.4%, and we are

Key economic figures and forecasts*

	2011	2012	2013	2014	2015	2016e	2017f
Nominal GDP (EUR bn)	70.4	72.4	73.8	75.6	78.1	80.7	84.2
Real GDP (% yoy)	2.8	1.5	1.4	2.5	3.6	3.5	3.3
Industrial output (% yoy)	5.3	8.1	4.6	3.7	5.9	4.5	4.5
Unemployment rate (avg, %)	13.4	13.9	14.2	13.2	11.5	9.2	8.3
Nominal industrial wages (% yoy)	3.6	4.0	3.6	5.1	2.9	4.0	4.5
Producer prices (avg, % yoy)	2.6	3.9	-0.1	-3.5	-4.2	-2.0	2.0
Consumer prices (avg, % yoy)	3.9	3.6	1.4	-0.1	-0.3	-0.1	2.2
Consumer prices (eop, % yoy)	4.4	3.2	0.4	-0.1	-0.5	0.9	2.5
General budget balance (% of GDP)	-4.1	-4.3	-2.7	-2.7	-3.0	-2.1	-1.3
Public debt (% of GDP)	43.3	52.4	55.0	53.9	52.9	52.8	52.1
Current account balance (% of GDP)	-5.0	0.9	2.0	0.1	-1.3	-0.9	-0.7
Gross foreign debt (% of GDP)	78.5	75.8	81.9	89.7	86.1	84.9	83.1

** euro area entry on 1 January 2009*
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

already below the structural unemployment level (around 12%). Therefore, the problem with skill-mismatch on the labour market will be more pronounced in the next quarters.

Consumer inflation stood at -0.8% yoy in May, having been in negative territory for more than 28 months now. This is still being driven by lower energy prices, lower VAT (the VAT rate went down from 20% to 10% for a limited number of food items in January 2016), and a decrease in the price of some fruits and vegetables. Core inflation (ECB method, i.e. headline ex food, alcohol, tobacco, and energy) is continuously picking up and is now at +1%. This development along with strong wage growth in certain sectors suggests that the Slovak economy is closing a negative output gap. We **expect core inflation to increase over the rest of the year**. Since gas prices are expected to fall in July 2016 (regulated energy price change lags oil price development), the headline inflation will be in negative territory until September 2016. As in well-integrated and export-oriented CE peers the outlook for the Slovak economy is likely to experience some modest headwinds in the current post-Brexit setting.

Financial market outlook

The newly elected government plans to reach a balanced budget in 2019, but we are bit sceptical about the feasibility of this goal. It is possible to reach it, but the lack of external pressure (weak pressure from EU institutions and low yields due to the QE programme) and internal pressure (desire to utilise low bond yields to finance large investment projects) is running against it.

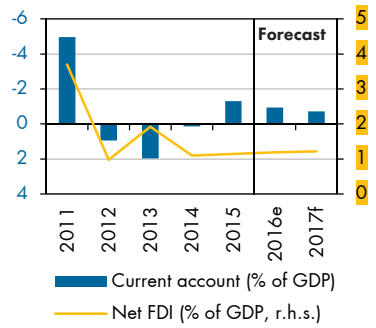
Public debt should decrease to below 50% of GDP in 2018, but only if the government sticks to its deficit reduction plan. This value would be comfortably below the threshold defined in constitutional debt cap law.

The ECB is continuing its public sector purchase programme (PSPP) through the National Bank of Slovakia. As of 31 May, the ECB owned EUR 6.8 bn in Slovak bonds. This represents around 19% of the total outstanding debt (bonds and T-bills). Since the NBS is not able to buy as many Slovak bonds as desired, it also has to buy more and more EU, EIB, and EFSF bonds.

Therefore, **we see no room for spread increases** (vs. German bonds) in the near future. The spread of ten-year Slovak government bonds vs. German bond remains very low (around 30bp) and does not reflect a difference in the rating between these two countries. However, the most recent Brexit-related fallout on markets has shown that some liquidity premia is definitely warranted for Slovak government bonds, as the market has dried up (or was virtually non-existent) in the Brexit aftermath.

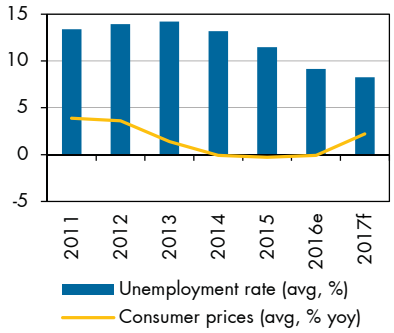
Financial analyst: Juraj Valachy (+421 2 5919 2033), Tatra banka, a.s., Bratislava

Current account and FDI inflows



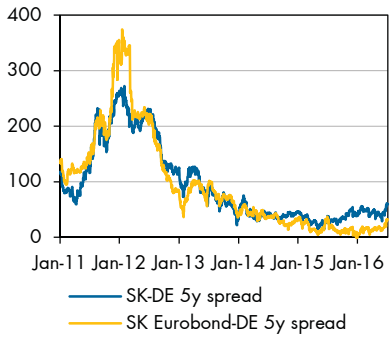
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Inflation outlook



Source: Bloomberg, RBI/Raiffeisen RESEARCH

Slovakia vs. German 5y Bund*

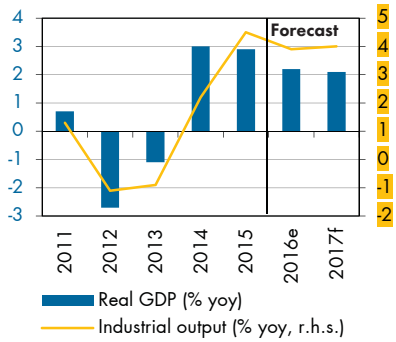


** spread in basis points*
Source: Bloomberg, RBI/Raiffeisen RESEARCH

S&P upgrades rating

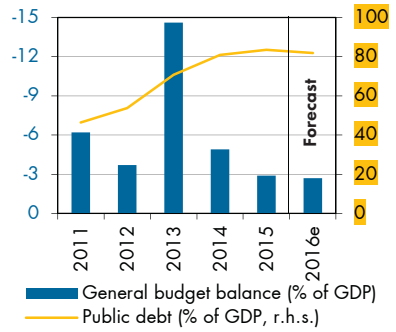
- **Economy gets good start to 2016 as export growth continues**
- **Inflation still depressed by energy prices, to recover in H2**
- **Rating agency S&P hikes rating from A- to A on fiscal improvements and recovery**
- **Government debt in a downward trend with deficit below the 3% threshold**

Real GDP (% yoy)



Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Budget balance and public debt



Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Overall, the Slovenian economy is doing well. After economic growth of 3.0% and 2.9% over the past two years, the first quarter result in 2016 was encouraging as well. In comparison with the first quarter of 2015, GDP expanded by 2.5%, and by 0.5% in comparison with the previous quarter. Interestingly, after rather balanced growth in 2015 (by equal thirds: household demand, gross investment, and net exports), the growth in Q1 was driven much more by net exports while domestic demand was substantially weaker. Exports are thus still the backbone of the Slovenian recovery, growing by over 5% yoy in Q1. Given the positive export dynamics, the trade and current account balance is improving and surpassed a 12-month rolling sum of USD 3 bn.

This development is underpinned by positive industrial production growth of 7.5% yoy in April and almost 6% over the last 12 months, while retail sales are still much lower at around 1.5% yoy. **We keep our economic growth forecast for this year at 2.2%**, which is a bit better than the latest forecast by the Slovenian National Bank of 1.9% yoy. The slowdown in comparison with last year is mainly a weakness of public investment as this year's EU funds are lower than in 2015. For next year, the central bank is more upbeat than we are with an outlook of 2.5% versus our unchanged 2.1% yoy.

Price developments are still in negative territory, with headline CPI at -0.4% yoy in May and amounting to -0.6% yoy over the last 12 months. As in other economies, inflation is still being suppressed by lower energy prices as core inflation without energy and unprocessed food is one percentage point higher at 0.6% yoy. With a stabilisation of energy prices, **we still see the inflation rate climbing to around 1% yoy by the end of this year** and further in 2017.

On a positive note, S&P upgraded the sovereign rating from A- to A given the private sector recovery, the consolidation of government finances to below the 3% of GDP threshold, and the adoption of a fiscal rule to achieve a structurally balanced budget by 2020. Thus, S&P expects the debt to GDP ratio to fall towards 75% by 2019 (from the current 82%).

Financial analysts: Andreas Schwabe, CFA; Elena Romanova, RBI Vienna

Key economic figures and forecasts*

	2011	2012	2013	2014	2015	2016e	2017f
Nominal GDP (EUR bn)	36.9	36.0	35.9	37.3	38.6	39.7	41.3
Real GDP (% yoy)	0.7	-2.7	-1.1	3.0	2.9	2.2	2.1
Industrial output (% yoy)	1.3	-1.1	-0.9	2.2	4.5	3.9	4.0
Unemployment rate (avg, %)	8.2	8.9	10.1	9.7	9.1	8.5	8.2
Nominal industrial wages (% yoy)	2.7	3.7	0.5	0.5	1.5	2.0	1.0
Producer prices (avg, % yoy)	3.8	1.0	0.3	-0.7	0.6	1.5	1.0
Consumer prices (avg, % yoy)	1.8	2.6	1.8	0.2	-0.5	0.2	0.9
Consumer prices (eop, % yoy)	2.1	2.7	0.7	0.2	-0.5	1.1	1.0
General budget balance (% of GDP)	-6.2	-3.7	-14.6	-4.9	-2.9	-2.7	-2.5
Public debt (% of GDP)	46.4	53.7	70.8	80.8	83.5	81.9	81.2
Current account balance (% of GDP)	0.2	2.6	5.6	7.0	6.5	5.5	4.8
Gross foreign debt (% of GDP)	112.7	118.9	115.9	124.1	114.8	110.0	104.1

** euro area entry on 1 January 2007*
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Changing growth pattern – more sustainable?

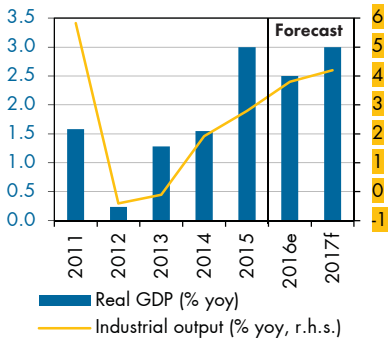
- **Private consumption currently driving economic growth**
- **Tight public and private investments expected in H2**
- **Improved situation on the labour market**
- **Lasting decline in lending to businesses**

In line with the positive growth environment in CEE, GDP in Bulgaria grew by 3.0% yoy in real terms, repeating the result in 2015. Otherwise, not only external demand but also much stronger domestic demand have been GDP drivers. Based on rapidly growing average salaries (8.3% yoy) and low interest rates on deposits (average 0.7% p.a.), household consumption soared, supporting GDP growth by 2pp, while gross fixed capital formation contributed 1.4pp in Q1. Accordingly, the net export contribution narrowed to 0.7pp (5.1pp in Q1 2015). The new-fangled private consumption-driven growth model is anticipated to continue further in Q3 and Q4, following the ongoing common pattern for the CEE region. In fact, it could be seen as a result of the ECB's QE policy, which in addition will push inflation into positive territory in H2 (0% as of April). Against the backdrop of flourishing private consumption, **exports and investments are expected to become more sluggish** than in 2015. In this respect, weaker EU funding in 2016 due to the new EU programme transition period will limit public investment, and the state budget will not be able to compensate for this to any great extent. Otherwise, narrowing year-on-year lending to businesses since end-2014 in the declining interest environment (average 5.5% p.a.) along with double-digit increases in corporate deposits since November 2015 are clear evidence of insufficient investment opportunities for enterprises. The survey of the National Statistical Institute estimated a 4.2% yoy decrease in private investment in the industry in 2016.

The political conditions (fuelled by the **presidential elections in autumn**) are not expected to hinder the economic trends despite sluggish structural reforms and some potential friction in the ruling coalition. The external political environment, however, will remain a source of potential social and economic instability (military conflicts, refugee influx, etc.).

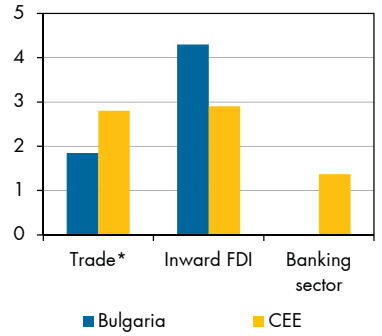
Financial analyst: Emil S. Kalchev, Raiffeisenbank (Bulgaria) EAD, Sofia

Real GDP (% yoy)



Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

BG: UK-gearing (% of total)**



** export and import share*
*** 2014 or 2015 data*
Source: national sources, BIS, RBI/Raiffeisen RESEARCH

Key economic figures and forecasts

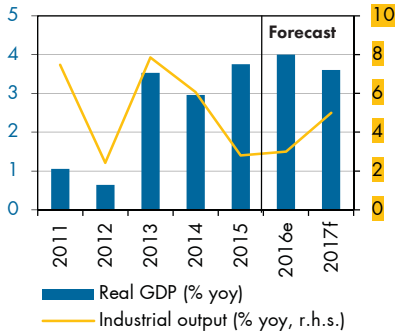
	2011	2012	2013	2014	2015	2016e	2017f
Nominal GDP (EUR bn)	41.0	41.7	41.9	42.7	44.2	45.7	48.1
Real GDP (% yoy)	1.6	0.2	1.3	1.5	3.0	2.5	3.0
Industrial output (% yoy)	5.8	-0.4	-0.1	1.9	2.8	3.8	4.2
Unemployment rate (avg, %)	11.3	12.3	12.9	11.4	9.2	8.4	8.0
Nominal industrial wages (% yoy)	9.6	12.7	0.7	1.5	9.1	10.0	8.2
Producer prices (avg, % yoy)	9.4	4.2	-1.4	-1.2	-1.9	0.4	1.0
Consumer prices (avg, % yoy)	4.2	3.0	0.9	-1.4	-0.1	0.3	1.6
Consumer prices (eop, % yoy)	2.8	4.2	-1.6	-0.9	-0.4	0.8	2.3
General budget balance (% of GDP)	-2.0	-0.4	-1.8	-3.6	-2.9	-2.5	-2.0
Public debt (% of GDP)	15.5	17.6	18.1	26.9	26.3	29.5	30.0
Current account balance (% of GDP)	1.0	-0.2	1.9	1.2	1.1	1.1	0.4
Official FX reserves (EUR bn)	13.3	15.6	14.4	16.6	20.4	23.5	21.2
Gross foreign debt (% of GDP)	88.6	90.5	88.1	93.1	77.2	76.6	74.8
EUR/BGN (avg)	1.96	1.96	1.96	1.96	1.96	1.96	1.96
USD/BGN (avg)	1.41	1.52	1.47	1.47	1.76	1.78	1.94

Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

GDP driven by rapidly growing consumption

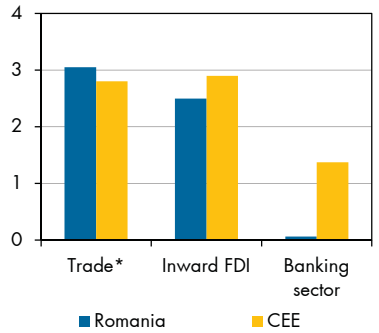
- **Solid, domestically driven GDP growth, but macroeconomic imbalances on the rise**
- **Underlying inflationary pressures still contained, but likely to strengthen**
- **Decreasing liquidity surplus and increasing inflation rate to result in higher ROBOR rates**
- **RON yields to gradually increase due to domestic and external factors**

Real GDP (% yoy)



Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

RO: UK-gearing (% of total)**



** export and import share*
*** 2014 or 2015 data*
Source: national sources, BIS, RBI/Raiffeisen RESEARCH

Economic outlook

Economic growth remained solid in early 2016 as real GDP advanced by 1.6% qoq and 4.3% yoy in Q1, beating our and market analysts' projections. As expected, the GDP advance was once again driven by domestic demand as private consumption posted an impressive 10% yoy increase while gross fixed capital formation also went up by 7% yoy. For the **rest of 2016, we expect strong GDP dynamics** driven by consumption and investment. Private consumption should advance further thanks to fiscal expansion (successive VAT rate cuts and increase in public sector wages). Moreover, investments should continue to improve due to the low level of interest rates, but also due to some fiscal incentives that are in place. Furthermore, even though exports of goods and services decelerated in 2015, we expect an uptick in 2016 as a result of improvement in foreign demand. The rapid economic growth **should be accompanied by an enlargement of the external imbalances** as the increase in domestic demand is likely to result in a faster increase in imports of goods and services compared with exports. Politics should remain in the limelight in the following period. In the first round of local elections held in June 2016, the Social Democratic Party (PSD) received more votes (by around 7 percentage points) than its main competitor (the National Liberal Party – PNL) and could become the front runner in the parliamentary elections in November/December. In order to win the elections, the PSD would probably try to strengthen its cooperation with its former allies (UNPR – National Union for Romania's Progress and ALDE – Alliance of Liberals and Democrats for Europe). According to recent comments by the leader of the PSD, they do not intend to submit a no-confidence-vote against the technocratic government in the near term as it might result in early elections. However, such an initiative cannot be ruled out entirely. The **elections imply risks of additional fiscal stimulus**, which might put more pressure on the public budget deficit.

Key economic figures and forecasts

	2011	2012	2013	2014	2015	2016e	2017f
Nominal GDP (EUR bn)	133.3	133.5	144.3	150.2	160.3	168.9	182.3
Real GDP (% yoy)	1.1	0.6	3.5	3.0	3.8	4.0	3.6
Industrial output (% yoy)	7.5	2.4	7.9	6.1	2.8	3.0	5.0
Unemployment rate (avg, %)	7.2	6.8	7.1	6.8	6.8	6.5	6.5
Nominal industrial wages (% yoy)	6.7	4.6	4.2	7.4	6.8	7.0	5.4
Producer prices (avg, % yoy)	7.1	5.4	2.1	-0.1	-2.2	-1.6	1.9
Consumer prices (avg, % yoy)	5.8	3.3	4.0	1.1	-0.6	-1.2	2.3
Consumer prices (eop, % yoy)	3.1	5.0	1.6	0.8	-0.9	0.5	2.8
General budget balance (% of GDP)	-5.4	-3.7	-2.1	-0.9	-0.7	-3.0	-3.2
Public debt (% of GDP)	34.2	37.4	38.0	39.8	38.4	39.2	39.9
Current account balance (% of GDP)	-4.9	-4.8	-1.1	-0.5	-1.1	-2.8	-3.3
Official FX reserves (EUR bn)	37.1	35.4	35.4	35.7	35.6	36.4	37.6
Gross foreign debt (% of GDP)	75.0	75.5	68.0	63.1	56.7	53.3	52.7
EUR/RON (avg)	4.24	4.46	4.42	4.44	4.45	4.50	4.47
USD/RON (avg)	3.05	3.47	3.33	3.35	4.01	4.09	4.43

Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

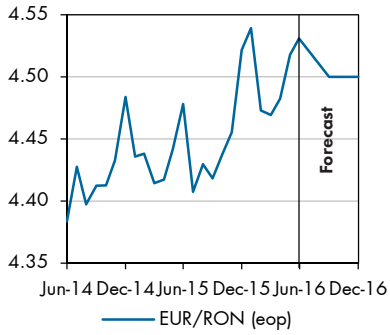
The annual inflation rate remained deeply in negative territory (-3.5% yoy in May 2016) due to the successive VAT rate cuts in June 2015 and in January 2016. Moreover, underlying inflationary pressures remained contained during the past months, resulting in an inflation rate below our expectations. This and a lower path for administrated prices prompted us **to revise our annual inflation rate forecast for the end of 2016 downwards to 0.5% yoy** from the previous 1.5% yoy. Also, the Central Bank's rhetoric has changed during the last weeks compared with the beginning of the year, becoming less hawkish. We **expect the National Bank of Romania (NBR) to maintain the key interest rate unchanged at 1.75%** until the second half of 2017, but the monetary policy stance should start to tighten earlier through an increase in money market rates (ROBOR).

Financial market outlook

During Q2, ROBOR rates continued to trade at very low levels significantly below the key interest rate. The excess liquidity in the money market decreased for some months after the peak in January. We expect ROBOR rates to start to move upward in the coming months as a result of a decline in excess liquidity in the money market. However, they should continue to trade below the key interest rate until March 2017. At the same time, **yields for short-dated Romanian government securities should continue to benefit from the excess liquidity conditions**, but then should also begin to move up towards the end of the year. On the other hand, yields for longer-dated Romanian T-bonds are likely to be more sensitive to developments on the domestic market – enlargement of macroeconomic imbalances and increased noise on the political scene due to the parliamentary elections – resulting in higher yields towards the end of 2016 and early 2017. We do not see any near-term risks for RON related to (purely) UK-driven portfolio outflows due to the outcome of the British EU referendum. Any negative implications may arise from broader European economic fallout and overall risk selling on markets.

Financial analyst: Silvia Maria Rosca, Raiffeisen BANK S.A., Bucharest

Exchange rate development



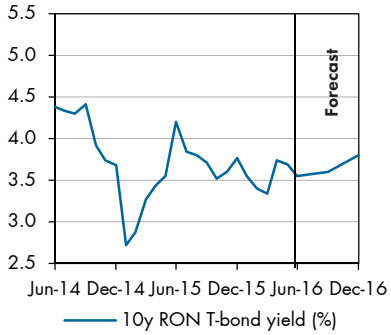
EUR/RON: 5y high 4.64, 5y low 4.19
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Exchange rate forecasts

	28-Jun[1]	Sep-16	Dec-16	Mar-17	Jun-17
EUR/RON	4.53	4.50	4.50	4.45	4.50
Cons.		*4.50*	*4.50*	*4.45*	*4.46*
USD/RON	4.10	4.09	4.29	4.32	4.55
Cons.		*4.12*	*4.09*	*4.11*	*4.15*

[1] 5:00 p.m. (CEST)
Source: Bloomberg, RBI/Raiffeisen RESEARCH

RON yield development (%)



10y RON T-bond yield: 5y high 7.9, 5y low 2.66
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Interest rate forecasts (%)

	28-Jun[1]	Sep-16	Dec-16	Mar-17	Jun-17
Key rate	1.75	1.75	1.75	1.75	1.75
Consensus		*1.75*	*1.80*	*1.85*	*1.95*
1 month[2]	0.65	1.00	1.10	1.60	1.70
3 month[2]	0.82	1.20	1.30	1.60	1.80
Consensus		*0.72*	*0.95*	*1.18*	*2.05*
6 month[2]	1.07	1.30	1.40	1.70	1.80
12 month[2]	1.21	1.50	1.50	1.80	1.90

[1] 5:00 p.m. (CEST) [2] Offered rate
Source: Bloomberg, RBI/Raiffeisen RESEARCH

Yield forecasts (%)

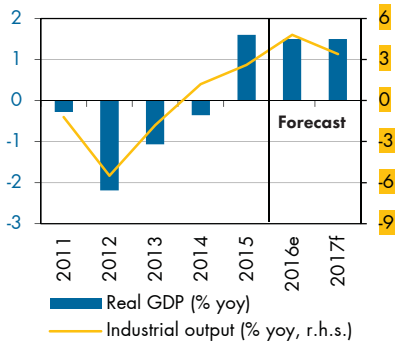
	28-Jun[1]	Sep-16	Dec-16	Mar-17	Jun-17
3y T-bond[2]	1.95	2.0	2.2	2.4	2.5
Consensus		*n.v.*	*n.v.*	*n.v.*	*n.v.*
10y T-bond[2]	3.55	3.6	3.8	3.9	4.1
Consensus		*n.v.*	*n.v.*	*n.v.*	*n.v.*

[1] 5:00 p.m. (CEST) [2] Bid yield
Source: Bloomberg, RBI/Raiffeisen RESEARCH

In the shadow of politics

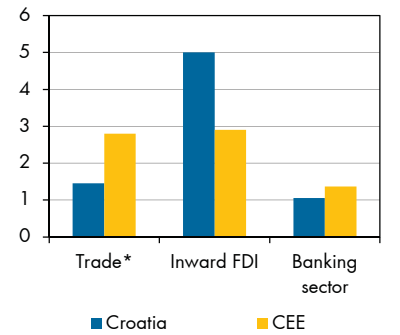
- **Rising political uncertainty – threat to the rating and mid-term perspective**
- **Recovery gained momentum**
- **Delay of Eurobond issuance**
- **HRK stability above all**

Real GDP (% yoy)



Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

HR: UK-gearing (% of total)**



** export and import share*
*** 2014 or 2015 data*
Source: national sources, BIS, RBI/Raiffeisen RESEARCH

Economic outlook

The recovery that started in 2015 has continued since the beginning of the year and has been largely driven by domestic demand. Household consumption continues to be supported by falling prices, the stabilisation of the labour market, and a good tourist season. Positive movements are also visible in EU fund absorption, which spurred investment activity. **We do not see any significant direct impact on the Croatian economy due to the Brexit.** Over the next three years the British American Tobacco (BAT) has planned to invest EUR 30 mn in order to increase the production capacity, thus a minor impact could be less investments going forward. The related increase in import growth has offset the continuous acceleration of exports, thus stressing the requirement to strengthen the country's competitive position (based on quality) and to reduce the high dependency on imports. Encouraging indicators at the beginning of the second quarter, positive expectations regarding the strong tourist season, and the economic environment of Croatia's main export partners suggest that this year's GDP growth could be even higher than initially expected. Still, political vulnerabilities that have been present since the end of May are casting a shadow on these positive developments, thus pointing to mid-term risks. Disagreements between the parties in power ended with a no confidence vote against Prime Minister Oreskovic which passed the Parliament and thus bringing down the Government. **New elections (probably in September) could bring about an even more complicated political situation** since the outcome is not likely to bring a clear winner. Under such circumstances, the much awaited implementation of reforms would definitely have to be postponed and the mid-term growth prospects would be depressed. In the short term, political uncertainty should restrain public expenditure growth and the economic recovery should continue to have a positive effect on revenues, thus keeping the budget deficit at around 3% of GDP. Recent fiscal developments confirmed our stance that even without the government doing anything, fiscal adjust-

Key economic figures and forecasts

	2011	2012	2013	2014	2015	2016e	2017f
Nominal GDP (EUR bn)	44.7	44.0	43.5	43.0	43.9	44.9	46.2
Real GDP (% yoy)	-0.3	-2.2	-1.1	-0.4	1.6	1.5	1.5
Industrial output (% yoy)	-1.2	-5.5	-1.8	1.2	2.6	4.8	3.4
Unemployment rate (avg, %)	13.7	15.9	17.4	17.3	16.3	15.9	15.5
Nominal industrial wages (% yoy)	1.3	1.9	1.7	1.5	-4.1	2.0	1.5
Producer prices (avg, % yoy)	6.4	7.0	0.5	-2.7	-3.9	-3.9	2.0
Consumer prices (avg, % yoy)	2.3	3.4	2.2	-0.2	-0.5	-1.0	1.5
Consumer prices (eop, % yoy)	2.1	4.7	0.3	-0.5	-0.6	0.5	1.6
General budget balance (% of GDP)	-7.8	-5.3	-5.3	-5.5	-3.2	-3.0	-2.9
Public debt (% of GDP)	63.7	70.7	80.8	86.5	86.7	87.2	87.6
Current account balance (% of GDP)	-0.7	0.0	1.0	0.9	5.2	2.0	2.2
Official FX reserves (EUR bn)	11.2	11.2	12.9	12.7	13.8	13.5	13.0
Gross foreign debt (% of GDP)	103.7	103.0	105.7	108.5	103.7	99.1	98.5
EUR/HRK (avg)	7.43	7.52	7.58	7.63	7.61	7.56	7.57
USD/HRK (avg)	5.35	5.85	5.71	5.76	6.86	6.87	7.50

Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

ment is happening due to the structure of expenditures. Still, Croatia definitely needs a stable government with a focus on reforms and private sector needs to achieve sustainable fiscal metrics. Meanwhile, external vulnerability should continue to decrease slowly. The still high level of indebtedness is constraining the sources of growth and also implies that the process of deleveraging should continue, while the growth in exports of goods and services with a better inflow of EU funds should support the current account.

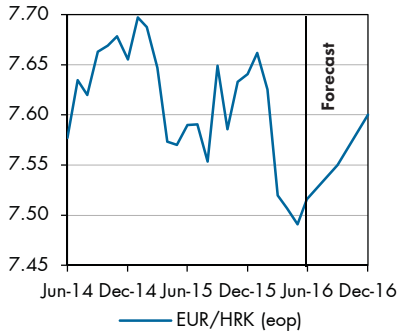
Financial market outlook

The strengthening of the HRK against the EUR that had persisted over the past months was stopped at the end of May when political troubles started to dominate the scene. Although being rather shallow and thus subject to speculative positioning by some market players, the FX market has remained calm with EUR/HRK hovering around 7.50. Besides the political uncertainty, the EUR/HRK rate (which has temporarily moved above 7.50) might partially be attributed to the profit taking and market positioning ahead of the upcoming EUR-linked maturities of sovereign liabilities (credit lines). Still, we are going to see a stronger HRK in the summer months. The **HRK is supported by the seasonal inflow of tourism-related FCY receipts** and the possible (but temporary) withdrawal of HRK liquidity due to the tourist season and announced sovereign HRK bond issue. The latter could be generous as the **Ministry of Finance was forced to delay the Eurobond issuance** that was planned in May due to the political uncertainty. Besides the pure HRK bond in the amount of 3.5 bn, the summer is also bringing the EUR T-bill maturity of 1.25 bn, which we expect to be rolled over. Although being depressed by an ample liquidity surplus, short-term and long-term yields are widely exposed to the increased risk of a further rating cut if the political turmoil continues. Refinancing needs in 2016 will definitely be met as the local market is flush with a liquidity surplus, and market players (especially large institutional investors such as pension funds) are able to meet a possible increase in the government bond supply. Nevertheless, an average of 20% of the refinancing needs over the years to come may not be met solely on the local market.

Towards the end of summer, the kuna could see slight depreciation. An upward EUR/HRK trend is expected towards the end of the year. However, we are confident that the CNB will remain consistent in its policy of preserving the stability of the domestic currency given the still high degree of euroisation, that is, the currency risk for all segments of the economy. At the same time, the **CNB will continue to pursue an accommodative monetary policy** by preserving high levels of liquidity in the financial system in order to ease domestic financing conditions. The key issue thus remains the transfer of surplus liquidity into the real sector, which should generate growth and new employment. For the time being, at least in Croatia, the process remains partly limited due to high indebtedness in all sectors (exceeding 200% of GDP).

Financial analyst: Z. Živković Matijević, Raiffeisenbank Austria d.d., Zagreb

Exchange rate development



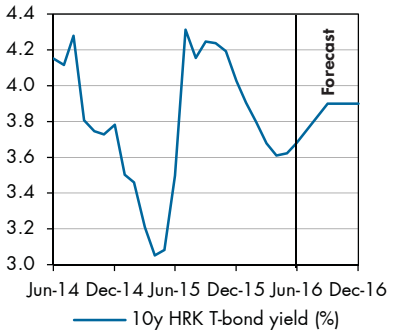
EUR/HRK: 5y high 7.72, 5y low 7.36
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Exchange rate forecasts

	28-Jun[1]	Sep-16	Dec-16	Mar-17	Jun-17
EUR/HRK	7.52	7.55	7.60	7.60	7.50
Cons.		*7.54*	*7.55*	*7.56*	*7.57*
USD/HRK	6.80	6.86	7.24	7.38	7.58
Cons.		*6.73*	*6.80*	*6.82*	*6.85*

[1] 5:00 p.m. (CEST)
Source: Bloomberg, RBI/Raiffeisen RESEARCH

HRK yield development (%)



10y HRK T-bond yield: 5y high 7.47, 5y low 3.01
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Interest rate forecasts (%)

	28-Jun[1]	Sep-16	Dec-16	Mar-17	Jun-17
1 month[2]	0.61	0.60	0.50	0.50	0.50
3 month[2]	0.80	0.90	0.90	0.90	0.90
6 month[2]	0.98	1.15	1.10	1.10	1.10
12 month[2]	1.30	1.55	1.50	1.50	1.50

[1] 5:00 p.m. (CEST) [2] Offered rate
Source: Bloomberg, RBI/Raiffeisen RESEARCH

Yield forecasts (%)

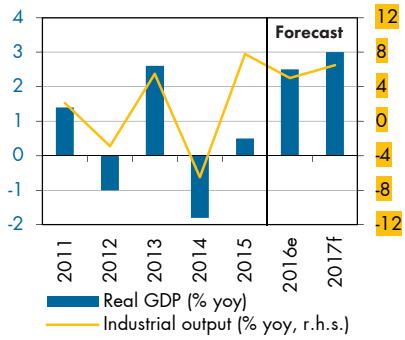
	28-Jun[1]	Sep-16	Dec-16	Mar-17	Jun-17
2y T-bond	1.91	1.9	1.9	2.0	2.0
		n.v.	n.v.	n.v.	n.v.
10y T-bond	3.68	3.9	3.9	3.9	3.9
Consensus		*n.v.*	*n.v.*	*n.v.*	*n.v.*

[1] 5:00 p.m. (CEST)
Source: Bloomberg, RBI/Raiffeisen RESEARCH

The market is nervous amid halted reforms

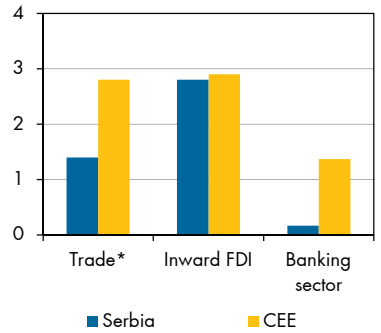
- **IMF wraps up fifth review**
- **Delayed reforms influencing cautious monetary policy...**
- **... and money market rates/yield fluctuations and EUR/RSD weakening**
- **IMF raising GDP growth prospects**

Real GDP (% yoy)



Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

RS: UK-gearing (% of total)**



** export and import share*
*** 2014 or 2015 data*
Source: national sources, BIS, RBI/Raiffeisen RESEARCH

The hesitant government formation during the fifth International Monetary Fund (IMF) review under the EUR 1.2 bn standby arrangement and the visit of the president of the People's Republic of China to the country is making the market a bit nervous. Though EUR/RSD depreciation is still fairly moderate, the growth in the 1w repo rate after it has been perpetually sliding down from early 2015 might be a signal that investors will be demanding higher risk premiums due to the almost halted public sector reforms. Early jitters are evident on the debt market as the public debt management agency (PDA) is only meeting the lower yield demands while the investors demanding higher premiums are left out. The PDA feels comfortable as it has refinanced 61.7% of the outstanding portfolio, the narrowing of the budget deficit has caused public debt to decline, and the **good performance of the economy** is feeding the flow of tax revenues. The National Bank of Serbia (NBS) will remain cautious as inflation (May: 0.7% yoy) should start to gradually grow to 1.8% yoy (our new forecast) on the back of the oil and agricultural prices recovery in conjunction with the expected state regulated prices hike. Though the outgoing cabinet ministers confirm the IMF's satisfaction concerning the reorganisation plans of the key SOEs, investors would like to see more action. Thus, **further reform delays might cause fluctuations on the FX market**, supporting a flat key rate, moderate FX interventions, and fairly moderate upward corrections of the money market rate.

Leading indicators point to robust economic performance, prompting the EU, IMF, and the National Bank of Serbia to upgrade the GDP projections for 2016 to the 2%–2.5% range. A positive contribution to the strengthening of the economy is also expected from the steel producer Zelezara Smederevo (sold to the Chinese HIBIS group). We stick to our 2.5% GDP forecast, with the growth being a function of the exports and FDI-led investments, though also of the gradual recovery in private spending.

Financial analyst: Ljiljana Grubic, Raiffeisenbank a.d., Belgrade

Key economic figures and forecasts

	2011	2012	2013	2014	2015	2016e	2017f
Nominal GDP (EUR bn)	33.4	31.7	34.3	33.1	33.3	34.9	37.4
Real GDP (% yoy)	1.4	-1.0	2.6	-1.8	0.5	2.5	3.0
Industrial output (% yoy)	2.1	-2.9	5.5	-6.5	7.8	5.0	6.5
Unemployment rate (avg, %)	23.0	23.9	22.1	20.1	17.9	20.0	22.0
Nominal industrial wages (% yoy)	5.0	1.5	1.5	4.0	2.9	4.0	4.0
Producer prices (avg, % yoy)	14.2	5.6	3.6	1.3	2.0	3.0	3.5
Consumer prices (avg, % yoy)	11.3	7.8	7.8	2.9	1.4	1.2	2.5
Consumer prices (eop, % yoy)	7.0	12.2	2.2	1.7	2.5	1.8	2.8
General budget balance (% of GDP)	-4.8	-6.8	-5.5	-6.6	-3.7	-3.7	-3.0
Public debt (% of GDP)	44.2	55.9	58.8	68.8	74.7	78.5	81.3
Current account balance (% of GDP)	-8.6	-11.5	-6.1	-6.0	-4.6	-4.3	-4.5
Official FX reserves (EUR bn)	12.0	10.9	11.2	10.0	10.4	10.0	10.8
Gross foreign debt (% of GDP)	72.2	81.1	75.4	78.6	81.6	80.6	78.3
EUR/RSD (avg)	102.0	113.0	113.1	117.3	120.7	123.3	123.6
USD/RSD (avg)	73.3	88.0	85.2	88.5	108.8	112.1	122.4

Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

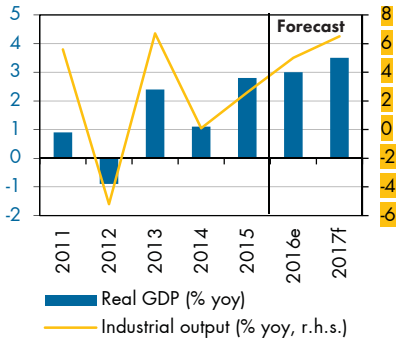
Economic recovery ongoing

- **Agreement reached with the IMF worth EUR 550 mn**
- **Industry, exports, and retail sales continued to advance in 2016**
- **Inflation print still very low – positive territory should be reached in H2 2016**
- **Labour market remains the weakest link in the economy**

Economic figures in H1 2016 were mostly in the shadow of the political developments. After BiH formally submitted an application to join the European Union on 15 February 2016, the political focus has turned to the negotiations with the IMF on the new economic programme. Finally, the agreement (Extended Fund Facility – EFF) worth EUR 550 mn was reached with the first tranche expected to be allocated in Q3 2016. The focus of the economic programme will be: improvement of the business environment, fiscal consolidation, and financial sector stability. The **new agreement with the IMF is expected to ensure fiscal stability** in the next three years, which is one of the key milestones for our positive economic assessments in the period from 2016 to 2018. The available macroeconomic indicators already started to shape our positive scenario. In the first four months of 2016, industrial production went up 4.4% yoy, exports of goods gained 1.4% yoy, and retail sales expanded by 7.4% yoy. We have much reason to believe that the BiH economy will continue to strengthen in the course of the year, driven by positive momentum in most of the GDP categories but with exports and gross investments likely at the forefront of economic growth. On a negative note, inflation is still very low (-1.4% yoy in January–April 2016), but we expect that the CPI rate will snap back into positive territory in H2 2016. Despite the anticipated decline in the years to come, the unemployment rate will remain at a high level of 26.0% (ILO methodology). Tackling the difficult labour market conditions should be a political focus in the years to come (and is also highlighted in the IMF economic programme) as it represents the weakest link in the BiH economic landscape. For the mid-term period of 3y in our base case scenario, we believe that the **BiH economy will see continuous and slightly accelerating economic recovery**, with the peak of economic growth likely being reached in 2018 (real GDP growth of 4.0% yoy).

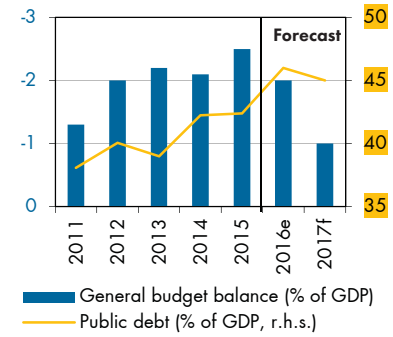
Financial analyst: Srebrenko Fatušić, Raiffeisen Bank d.d., Sarajevo

Real GDP (% yoy)



Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Budget balance and public debt



Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Key economic figures and forecasts

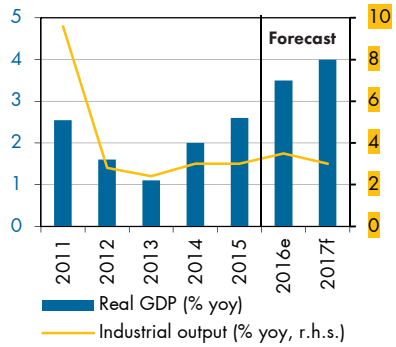
	2011	2012	2013	2014	2015	2016e	2017f
Nominal GDP (EUR bn)	13.4	13.4	13.7	14.0	14.4	15.0	15.8
Real GDP (% yoy)	0.9	-0.9	2.4	1.1	2.8	3.0	3.5
Industrial output (% yoy)	5.6	-5.2	6.7	0.1	2.6	5.0	6.5
Unemployment rate (avg, %)	27.6	28.0	27.5	27.5	27.7	26.0	25.0
Nominal industrial wages (% yoy)	6.8	2.2	-0.5	0.3	0.0	3.0	5.0
Producer prices (avg, % yoy)	3.8	1.3	-2.2	-0.2	0.6	1.5	2.5
Consumer prices (avg, % yoy)	3.7	2.1	-0.1	-0.9	-1.0	0.0	1.5
Consumer prices (eop, % yoy)	3.1	1.8	-1.2	0.0	-1.3	1.0	2.0
General budget balance (% of GDP)	-1.3	-2.0	-2.2	-2.1	-2.5	-2.0	-1.0
Public debt (% of GDP)	38.1	40.0	39.0	42.2	42.4	46.0	45.0
Current account balance (% of GDP)	-9.6	-9.1	-5.3	-7.5	-5.6	-7.0	-7.6
Official FX reserves (EUR bn)	3.3	3.3	3.6	4.0	4.4	4.5	4.7
Gross foreign debt (% of GDP)	48.9	52.2	52.2	51.8	54.2	55.5	55.7
EUR/BAM (avg)	1.96	1.96	1.96	1.96	1.96	1.96	1.96
USD/BAM (avg)	1.41	1.52	1.47	1.47	1.76	1.78	1.94

Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Thriller with the judiciary system reform

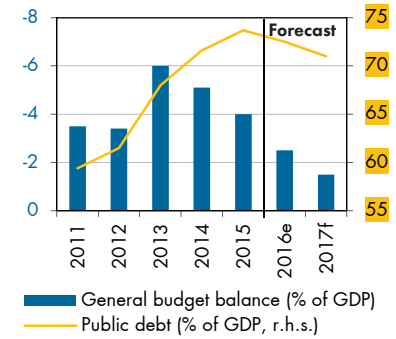
- **Eased monetary policy to continue throughout 2016**
- **FDI in large energy investment projects**
- **Public debt to GDP decreased as public finances improved**
- **Judiciary system reform approval unsure due to lack of political will**

Real GDP (% yoy)



Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Budget balance and public debt



Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

An expected recovery of the construction sector through an increase in FDI, the good performance of the tourism sector, and an increase in domestic electric power production enabled GDP to grow by 2.6% in 2015. The expectations are for an increase of about 3–3.5% in 2016, but this rate is still below potential. Economic growth will be supported by continued FDI and a moderate recovery of domestic demand. The annual inflation rate came in at 0.7% in May, but remains far from the target of 3.0% set by the Bank of Albania. A gradual increase in the inflation rate is expected in the second half of the year. The monetary policy is expected to be expansionary at least during 2016. The base rate is at 1.25% after the latest cut in early May, and further monetary stimulus can be expected during 2016. The eased monetary policy reflected in lower loan rates (average of 6.0% in April 2016, down from 7.7% in December 2015) and the legal framework to resolve the high level of NPL in the banking system that is being discussed in the parliamentary commissions is expected to provide a better lending perspective for the second part of the year.

The government remains committed to fiscal consolidation and the reduction of public debt to below 60% of GDP by 2019, which is expected to start in 2016. Public debt dropped from an estimated 72.2% at the end of 2015 to 69.3% of GDP in Q1 2016. The consolidation strategy is based on broadening the tax base, improving revenue compliance and administration, and implementing structural reforms.

In order to open the negotiation phase with the EU on the integration agenda, it is imperative for the parliament to approve the judiciary system reform. Despite the increased pressure from the EU and the USA to get the proposed reform approved, the negotiations between the parliamentary parties are becoming a political thriller as the lack of political will is evident.

Financial analyst: Valbona Gjeka, Raiffeisen Bank Sh.a., Tirana

Key economic figures and forecasts

	2011	2012	2013	2014	2015	2016e	2017f
Nominal GDP (EUR bn)	9.3	9.6	9.7	10.0	10.3	11.1	11.9
Real GDP (% yoy)	2.6	1.6	1.1	2.0	2.6	3.5	4.0
Industrial output (% yoy)	9.6	2.8	2.4	3.0	3.0	3.5	3.0
Unemployment rate (avg, %)	14.0	13.3	17.0	18.0	17.7	16.5	15.0
Nominal industrial wages (% yoy)	8.0	8.0	8.0	8.0	8.0	3.0	1.9
Producer prices (avg, % yoy)	2.6	1.1	-0.4	-0.5	1.0	2.0	2.0
Consumer prices (avg, % yoy)	3.5	2.0	1.9	1.6	1.8	1.5	2.2
Consumer prices (eop, % yoy)	1.7	2.4	1.9	0.7	1.9	2.0	2.5
General budget balance (% of GDP)	-3.5	-3.4	-6.0	-5.1	-4.0	-2.5	-1.5
Public debt (% of GDP)	59.4	61.5	68.0	71.6	72.2	70.5	67.8
Current account balance (% of GDP)	-11.9	-9.4	-10.5	-12.9	-13.6	-13.5	-14.3
Official FX reserves (EUR bn)	1.9	2.0	2.0	2.2	2.9	2.8	2.8
Gross foreign debt (% of GDP)	53.5	57.4	65.5	69.2	72.6	71.1	68.2
EUR/ALL (avg)	140.4	139.0	140.3	140.0	139.7	138.0	138.3
USD/ALL (avg)	100.9	108.2	105.7	105.5	126.0	125.5	136.9

Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Russia supports tight policies and reforms with a new loan

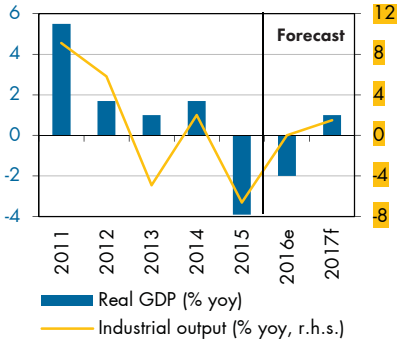
- **Economy in recession amidst low domestic demand and poor external trade results**
- **Russia backed EDB supports economic readjustment with a USD 2 bn loan**
- **FX reserves are at a stable but low level due to high foreign debt repayments**
- **Inflation on a downward trend in spite of weak and volatile Belarusian rouble**

In March, Belarus and the Eurasian Development Bank (EDB) agreed on a new ten-year USD 2 bn loan to come in tranches until the end of 2018. The loan is set to support a programme of reforms and austerity policies, including limits on the money supply, a deficit-free budget, a -2% GDP net increase in lending under government programmes, phased hikes in utility prices, and constraints on wage increases. The country's foreign trade contracted by a quarter in 2015, but was generally well balanced. Contraction moderated this year, while a slight trade deficit (USD 0.17 bn) returned. Despite the positive trade correction, high repayments on foreign public debt (USD 3.3 bn due in 2016) put the BYR under pressure. The **BYR** lost 36% of its value in 2015 and another 14% ytd. We **adjusted our forecast towards lower depreciation** due to restrictive policies and new external funding. FX reserves stand stable at USD 4 bn backed by FX borrowings in the local and external markets. In spite of the weak local currency, the regulator is restraining inflation at 12–13% yoy amid a reduced BYR money supply, but also due to a decline in external prices. CPI is not to exceed 15% in 2016.

Following moderate 1–2% growth during the previous three years, the Belarusian economy slid into recession in 2015 (GDP shrank by 3.9%). The decline in economic activity continues this year. Lower household incomes (7% decrease) and the unfavourable external environment (downturn in Russia; low prices and demand for potash fertilisers) continue to suppress economic growth. Industrial output decreased by 1.9% yoy in Jan–May while investment was hit especially hard by the downturn (over 21% drop). **We do not expect the economy to resume growth until the end of the year, anticipating a mild GDP contraction by 2%.** The share of non-performing assets in the banking sector doubled this year to 12.3%, which could pose a risk of a reversal to the preliminary accommodative policies by the national bank.

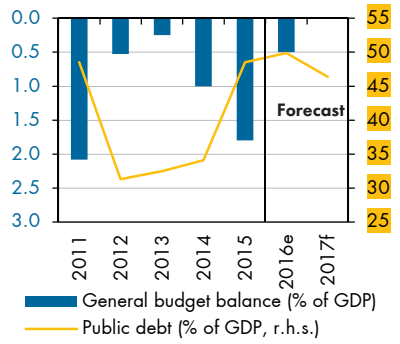
Financial analyst: Natalya Chernogorova, Priorbank Open Joint-Stock Company, Minsk

Real GDP (% yoy)



Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Budget balance and public debt



Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Key economic figures and forecasts

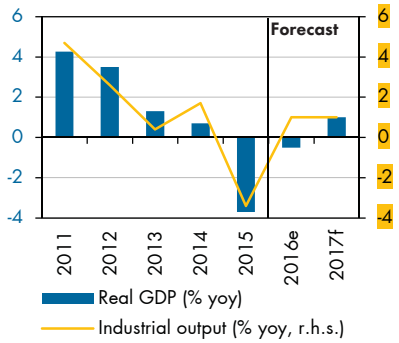
	2011	2012	2013	2014	2015	2016e	2017f
Nominal GDP (EUR bn)	41.2	49.4	54.9	57.2	49.1	43.3	49.2
Real GDP (% yoy)	5.5	1.7	1.0	1.7	-3.9	-2.0	1.0
Industrial output (% yoy)	9.1	5.8	-4.9	2.0	-6.6	0.0	1.5
Unemployment rate (avg, %)	0.6	0.5	0.5	0.5	1.0	1.5	2.0
Nominal industrial wages (% yoy)	59.2	93.8	35.2	20.1	7.6	8.0	10.0
Producer prices (avg, % yoy)	71.4	76.0	13.6	12.8	16.8	14.5	12.5
Consumer prices (avg, % yoy)	53.2	59.2	18.3	18.1	13.5	16.0	13.5
Consumer prices (eop, % yoy)	108.7	21.8	16.5	16.2	12.0	15.0	13.0
General budget balance (% of GDP)	2.1	0.5	0.2	1.0	1.8	0.5	0.0
Public debt (% of GDP)	48.5	31.3	32.5	34.1	48.5	49.9	46.4
Current account balance (% of GDP)	-8.9	-2.9	-10.0	-6.8	-3.8	-5.7	-5.4
Official FX reserves (EUR bn)	6.1	6.1	4.8	4.2	3.8	2.7	2.8
Gross foreign debt (% of GDP)	63.7	51.9	51.8	52.6	70.2	75.6	70.4
EUR/BYR (avg)	7,220	10,747	11,834	13,597	17,706	22,845	23,129
USD/BYR (avg)	5,218	8,360	8,906	10,250	15,964	20,768	22,900

Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Green shoots start to emerge

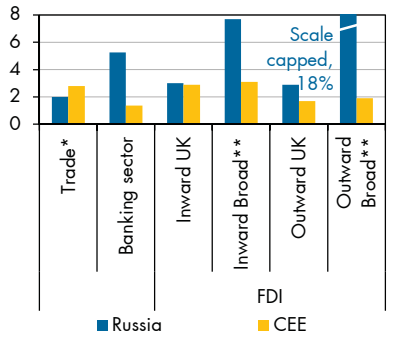
- **GDP growth outlook revised upward to -0.5% due to positive input from net exports**
- **CBR restarts an easing cycle in June but will remain careful with further cuts**
- **USD/RUB risks balanced; neither deep depreciation nor appreciation expected**
- **OFZ pricing is likely to further tighten – we maintain our constructive view on RUB bonds**

Real GDP (% yoy)



Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

UK: UK-gearing (% of total)**



** export and import share*
*** 2014 or 2015 data*
Source: national sources, BIS, RBI/Raiffeisen RESEARCH

Economic outlook

The economy seems to be in better shape than we expected at the beginning of 2016. Except for construction where the decline has resumed (-5.9% yoy in April vs. -1.4% yoy in March), all other economic indicators showed improvement or stabilisation. While internal demand (investments and consumption) continues to deteriorate, net exports – supported by RUB depreciation – remain the key driver of the recovery. RUB weakening resulted in lower demand for imported goods with a partial shift to local products and in an impressive improvement in the profitability of exports. Under such circumstances, industrial production started to recover quite quickly after a moderate decline in 2015. We anticipate that a recovery on the back of RUB depreciation would not start until H2 2016. Thus, we **have revised our GDP growth forecast from -2% to -0.5% yoy in 2016** with a positive contribution from net exports (+2% of GDP). Benefiting from some import substitution and higher exports, industrial production is set to grow this year. On the other hand, a weak RUB exchange rate (affecting purchasing power and the costs of imported equipment) will continue to discourage internal demand and we do not see any reasons to revise our forecast for investments and consumption this year (-4% yoy and -3% yoy, respectively). As the current moderate recovery of the domestic economy reflects by and large a natural bounce back following a substantial setback in 2014/2015 we do not see our more constructive economic outlook to be challenged due to the expected modest Brexit-related slowdown of the European economy. Meanwhile, recent CPI developments were better than expected, mainly due to a much lower pass-through from the FX weakening in early 2016. As of mid-June, it even fell below 7.3% yoy. Along with **better inflation expectations, a fairly stable FX rate, and slower growth of nominal wages**, this allowed the CBR to cut the key rate by 50bp to 10.5% in June. However, given persisting inflation risks arising from the inertia of inflation expectations and the fiscal situation (uncertainty regarding wage and pension growth, lack of a mid-term strategy

Key economic figures and forecasts

	2011	2012	2013	2014	2015	2016e	2017f
Nominal GDP (EUR bn)	1,460.4	1,677.1	1,678.8	1,526.1	1,182.4	1,126.5	1,336.5
Real GDP (% yoy)	4.3	3.5	1.3	0.7	-3.7	-0.5	1.0
Industrial output (% yoy)	4.7	2.6	0.4	1.7	-3.4	1.0	1.0
Unemployment rate (avg, %)	6.5	5.5	5.5	5.1	5.6	6.0	6.0
Average gross wages (% yoy)	11.5	13.9	11.9	9.1	4.4	4.0	6.0
Producer prices (avg, % yoy)	12.0	5.1	3.7	5.9	13.0	9.0	7.5
Consumer prices (avg, % yoy)	8.5	5.1	6.8	7.8	15.6	7.5	7.2
Consumer prices (eop, % yoy)	6.1	6.6	6.5	11.4	12.9	7.3	6.8
General budget balance (% of GDP)	1.6	0.4	-1.0	-1.0	-3.6	-4.4	-3.3
Public debt (% of GDP)	9.8	10.5	11.3	11.5	12.7	13.5	14.0
Current account balance (% of GDP)	4.8	3.3	1.5	3.2	5.0	4.0	4.5
Official FX reserves (EUR bn)	384.1	407.8	369.8	318.5	339.1	352.4	372.5
Gross foreign debt (% of GDP)	26.5	29.5	32.7	29.5	39.3	38.0	31.9
EUR/RUB (avg)	40.9	39.9	42.3	51.0	68.0	74.6	66.7
USD/RUB (avg)	29.4	31.1	31.9	38.6	61.3	67.8	66.0

Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

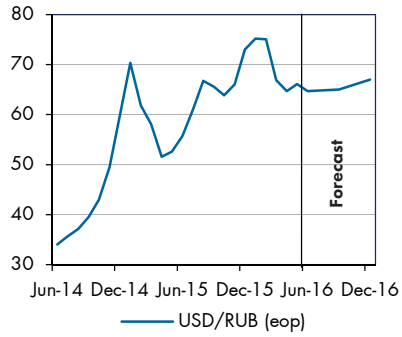
on fiscal consolidation, etc.), we **expect the CBR to be careful with further easing this year** and the next 50bp cut will not be possible until autumn.

Financial market outlook

In Q2, the RUB was supported by the good performance of oil prices (which passed USD 50/bbl Brent) despite fruitless OPEC negotiations on the back of decreasing production of shale oil and crude oil inventories declining in the US. Brexit decision meanwhile had only very limited impact on RUB. The main factor that will likely have a significant influence on FX in the summer is the shrinking of the current account balance month-on-month and year-on-year, even with oil at USD 50–52 per barrel of Brent, due to dividend payments and a recovery in imports. Dividends are estimated to total USD 13bn, a significant part of which will be converted into FX. Increasing rouble liquidity in the banking system that the CBR is not going to actively absorb at least in the coming months is not supportive for the RUB, either. From a technical point of view, the RUB exchange rate is close to the 300-day moving average (RUB/USD 66), which we consider a strong support. A deep dive below this seems unlikely at least in the short term. In Q2, yields on 10y OFZs dropped below YTM 8.5%, which is 50bp lower than in March 2016 and the minimum since mid-2014 despite the fact that the key rate is 300bp higher now (10y OFZs completely recouped intial losses triggered by the Brexit vote). We think that the **current OFZ yield curve looks too tight** and implies 1) aggressive rate cuts in the near future (at least 200bp) and 2) a drop of the RUONIA down to the deposit rate due to a growing excess of RUB liquidity as a result of the budget deficit being financed by the reserve fund. The CBR does not share such a view and intends to keep a cautious approach and cut the key rate gradually. We explain such skewed OFZ pricing by low issuance of new OFZs and weak credit activity on the local market. Large state-owned banks already enjoying excess rouble liquidity are the key OFZ buyers. We also saw strong demand from foreign accounts after the release of surprisingly weak US payrolls (which means no USD key rate hike at least in the near term). We do not expect the MinFin to increase borrowings on the local market. For non-residents, OFZs remain attractive as yields over the expected long-term CPI look still competitive with other local EM debt, especially as the global central bank outlook became more dovish following the Brexit vote. With 10y yields already below our year-end targets, the normalisation of the still inverted yield curve should be driven mainly by the front-end of the curve in the longer run, which is a function of the pace of rate cuts (which we expect to be only gradual). Overall, we **maintain our mildly bullish stance towards the RUB government bond market** given the attractive yield-pick-up compared with CE/SEE paper and the relatively stable rouble outlook out to 3 months.

Financial analysts: Anton Pletenev, Denis Poryvay, AO Raiffeisenbank, Moscow

Exchange rate development



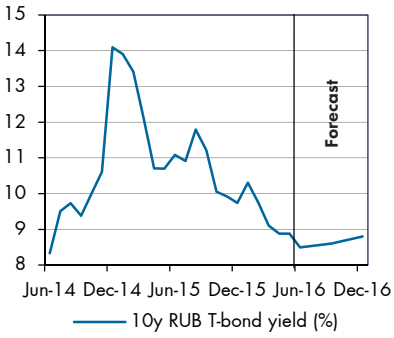
USD/RUB: 5y high 84.24, 5y low 27.51
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Exchange rate forecasts

	28-Jun[1]	Sep-16	Dec-16	Mar-17	Jun-17
EUR/RUB	71.46	71.5	70.4	69.0	64.4
Cons.		*74.9*	*75.0*	*74.4*	*72.9*
USD/RUB	64.67	65.0	67.0	67.0	65.0
Cons.		*66.2*	*67.0*	*66.0*	*66.0*

[1] 5:00 p.m. (CEST)
Source: Bloomberg, RBI/Raiffeisen RESEARCH

RUB yield development (%)



10y RUB T-bond yield: 5y high 16.24, 5y low 6.44
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Interest rate forecasts (%)

	28-Jun[1]	Sep-16	Dec-16	Mar-17	Jun-17
Key rate	10.50	10.00	9.50	9.00	9.00
Consensus		*9.8*	*9.3*	*8.7*	*8.1*
1 month[2]	10.76	10.30	9.80	9.30	9.30
3 month[2]	11.00	10.80	10.30	9.80	9.80
6 month[2]		n.v.	n.v.	n.v.	n.v.
12 month[2]	11.08	11.40	10.90	10.40	10.40

[1] 5:00 p.m. (CEST) [2] Offered rate
Source: Bloomberg, RBI/Raiffeisen RESEARCH

Yield forecasts (%)

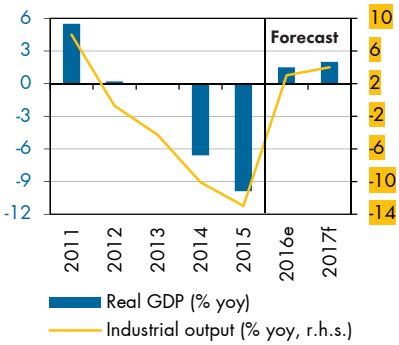
	28-Jun[1]	Sep-16	Dec-16	Mar-17	Jun-17
2y T-bond[2]	9.44	9.20	8.80	8.50	8.60
Consensus		*n.v.*	*n.v.*	*n.v.*	*n.v.*
10y T-bond[2]	8.49	8.60	8.80	8.50	8.50
Consensus		*n.v.*	*n.v.*	*n.v.*	*n.v.*

[1] 5:00 p.m. (CEST) [2] Bid yield
Source: Bloomberg, RBI/Raiffeisen RESEARCH

From political crisis to slow recovery

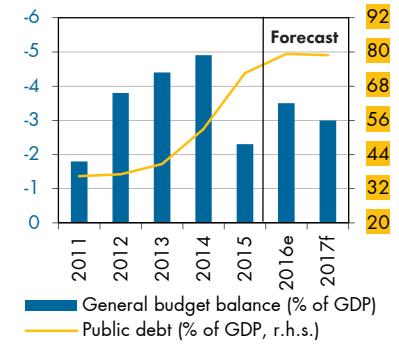
- **Resolved political crisis opens another small window for reforms, IMF money expected by summer**
- **Return to weak growth in 2016; inflation much lower than in 2015; rise in H2 from current low expected**
- **Central bank is loosening monetary policy and gradually removing FX restrictions**
- **Exchange rate much more comfortable, but devaluation risks could rise in autumn**

Real GDP (% yoy)



Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Budget balance and public debt



Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Political outlook

After two months of uncertainty, the political crisis in Ukraine ended in April. An ally of President Poroshenko, Volodymyr Groysman (speaker of the parliament), was installed as prime minister and almost the entire government was replaced. Groysman's team has demonstrated their intent to move forward with reforms so far, albeit under obvious external pressure. An advantage of the new political setup is a better relationship between the new government and presidential administration. On the other hand, the coalition supporting the new cabinet barely exceeds the required majority of 226 votes. Thus, the government is rather weak in this respect, which may present a serious obstacle to fundamental reforms. However, it should be mentioned that the coalition has so far demonstrated a good ability to organise support from other groups in parliament. One of the recent examples is amendments to the constitution regarding justice, which passed with 335 votes in parliament.

Meanwhile, Minsk-II is stuck and the military situation in Donbas is still not quiet. There has been no progress in the implementation of Minsk-II in the first half of the year.

Economic outlook

According to preliminary estimates, Ukraine's economy returned to positive modest growth of 0.1% yoy in Q1 2016. However, GDP shrank by 0.7% qoq in seasonally adjusted terms after two consecutive quarters of growth. This still rather disappointing result is a reflection of the two-month political crisis, lack of external financing, volatility on the FX market, and unfavourable global price dynamics. However, most of these issues have improved in the meantime or most likely will be solved in the nearest future. Thus, in our view, the dynamics in the next quarters should improve and **we still maintain our forecast of 1.5% yoy GDP**

Key economic figures and forecasts

	2011	2012	2013	2014	2015	2016e	2017f
Nominal GDP (EUR bn)	116.9	135.2	135.3	99.9	81.4	79.9	88.2
Real GDP (% yoy)	5.5	0.2	0.0	-6.6	-9.9	1.5	2.0
Industrial output (% yoy)	8.0	-0.7	-4.3	-10.1	-13.0	3.0	4.0
Unemployment rate (avg, %)	8.7	8.2	7.8	9.7	9.5	9.0	9.0
Nominal industrial wages (% yoy)	20.9	14.8	7.9	6.0	20.5	14.6	15.0
Producer prices (avg, % yoy)	19.0	3.6	-0.1	17.1	36.0	13.9	10.1
Consumer prices (avg, % yoy)	8.0	0.6	-0.2	12.1	48.7	15.5	12.0
Consumer prices (eop, % yoy)	4.6	-0.2	0.5	24.9	43.3	14.0	9.0
General budget balance (% of GDP)	-1.8	-3.8	-4.4	-4.9	-2.3	-3.5	-3.0
Public debt (% of GDP)	36.4	37.1	40.7	52.9	72.6	79.3	78.9
Current account balance (% of GDP)	-6.3	-8.2	-9.2	-3.5	-0.1	-3.3	-3.4
Official FX reserves (EUR bn)	24.5	18.6	14.8	6.2	12.2	16.2	19.2
Gross foreign debt (% of GDP)	77.6	76.5	79.3	95.2	131.5	140.0	140.4
EUR/UAH (avg)	11.1	10.4	10.8	15.9	24.3	28.9	29.7
USD/UAH (avg)	8.0	8.1	8.2	12.0	22.0	26.3	29.4

Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

growth in 2016. Inflation dropped sharply in February to May 2016, coming in at 7.5% in May, due to the base effect and the growth in the domestic food supply (as a result of the trade restrictions with Russia). Nevertheless**, we expect that the inflation rate could snap back to as much as 14% yoy by the end of 2016 from its current low** due to tariff increases and possible UAH devaluation later this year.

Finally, Ukraine hosted an IMF mission from 10 –18 May to continue discussions on the second review under the Extended Fund Facility (EFF) programme. The mission reached a staff level agreement with authorities on the steps needed to complete the second EFF programme review. The IMF noted significant progress in restoring macroeconomic stability. However, the implementation of structural and institutional reforms is critically important. Moreover, the fight against corruption remains one of the major indicators for international partners that Ukraine is still on the path of reform. In order to finally get the IMF Executive Board's approval (consideration is expected in July), authorities have to "boost their efforts to entrench fiscal and financial stability, decisively enhance transparency and rule of law, and reform the large and inefficient state-owned enterprise sector". On a positive note, international donors welcomed the constitutional changes in the area of justice mentioned above, and on 3 June, the US signed a third USD 1 bn loan guarantee agreement with Ukraine (even before the finalisation of the second IMF programme review). **We think that Ukraine will see a positive decision by the IMF** in summer. Nevertheless, rumours have it that the next IMF tranche may be cut from USD 1.7 bn to USD 1 bn to increase the subsequent ones.

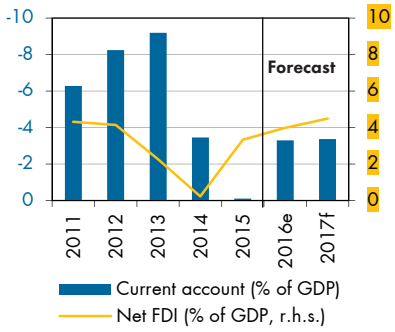
Financial market outlook

The hryvnia has been strengthening slowly against the backdrop of declining political tensions and seasonal issues. Despite the fact that the National Bank of Ukraine was the net FCY buyer in April to May, FX reserves remained at a level of USD 13.5 bn in May, which is still low.

Taking into account the recent UAH strengthening and slowing inflationary dynamics, the National Bank of Ukraine has relaxed some FX market restrictions and eased monetary policy. During April to June, the regulator decreased the key policy rate by 5.5pp to 16.5%, decreased mandatory FX sales from 75% to 65%, increased daily limits for permitted FX purchases and UAH cash withdrawal, lowered bureaucracy for FX transactions (decreased number of documents needed), and slightly improved conditions for foreign investors (funds in FCY, which were transferred under investment purposes, are no longer required to be converted into UAH). Moreover, the regulator decided to allow the repatriation of dividends accrued to foreign investors for 2014–2015, but with some limitations on the volume. Despite these steps, the **central bank will continue to prevent excessive UAH volatility** via administrative measures, thus limiting depreciation potential that we continue to expect going forward.

Financial analysts: Sergii Drobot, Raiffeisen Bank Aval Public Joint Stock Company, Kiev
Andreas Schwabe, CFA, RBI Vienna

Current account and FDI inflows



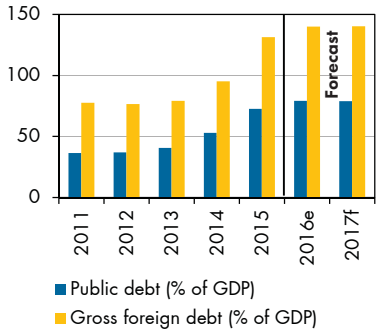
Source: State Statistics Committee of Ukraine, RBI/Raiffeisen RESEARCH

Exchange rate forecasts

	28-Jun[1]	Sep-16	Dec-16	Mar-17	Jun-17
EUR/ UAH	27.50	29.70	30.45	29.87	28.71
Cons.		*28.76*	*29.10*	*29.64*	*30.18*
USD/ UAH	24.89	27.00	29.00	29.00	29.00
Cons.		*27.00*	*27.00*	*29.00*	*27.29*

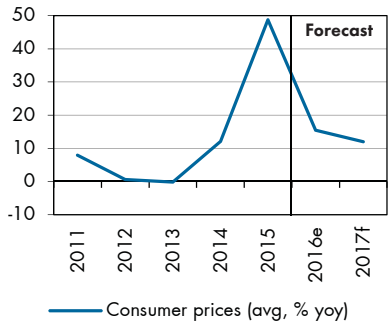
[1] *5:00 p.m. (CEST)*
Source: Bloomberg, RBI/Raiffeisen RESEARCH

Public and external debt



Source: State Statistics Committee of Ukraine, RBI/Raiffeisen RESEARCH

Inflation outlook

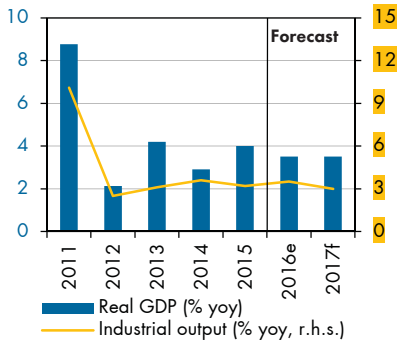


Source: State Statistics Committee of Ukraine, RBI/Raiffeisen RESEARCH

Booming economy on the Bosporus

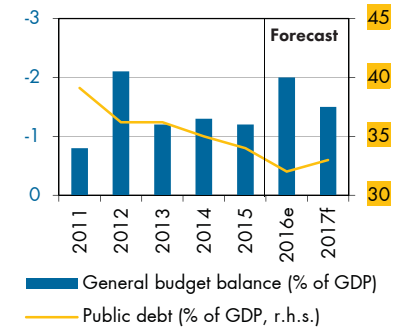
- **Strong domestic demand propelling growth in Q1, we are upping GDP forecast**
- **Falling inflation and still moderate credit growth allow monetary loosening**
- **TRY has been under pressure due to deteriorating trade balance,...**
- **...but we remain on Buy mainly due to slow Fed and stable FX prospects**

Real GDP (% yoy)



Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Budget balance and public debt



Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Economic outlook

Based on strong domestic demand, the economy steamed ahead both in 2015 (GDP 4% yoy) and in the first quarter of this year (GDP 4.6% yoy; 0.8% qoq). Private household consumption rose by a staggering 6.9% yoy in Q1 while government consumption increased by 10% yoy. On the contrary, investments and exports were much less drivers of growth as the first stagnated and the second rose by 2.4% yoy. With resurging imports, net exports negatively contributed to GDP growth. Strong domestic demand has been fuelled by public wage hikes, a minimum wage increase by 30%, and additional demand created by Syrian refugees. The strong performance **allowed us to adjust our GDP forecast for 2016 from 3.0% to 3.5% yoy**. Some see even dangers of overheating in the medium term.

A falling inflation trend since the beginning of 2016 has also been supportive for growth. The CPI rate came down from 8.8% at the end of 2015 to 6.6% yoy in May. Lower inflation allowed the central bank to effectively loosen monetary policy by reducing the upper ceiling of the interest rate corridor and the average funding rate. Strong growth and somewhat looser monetary and fiscal policies have yet not translated into a surge in bank lending growth, which has fallen towards 10% from 20–25% yoy a year ago. In 2015, the current account deficit reached a five year low of **only USD 32 bn or 4.5% of GDP**. However, we **expect a higher current account deficit in 2016** than in 2015 due to higher energy prices, stronger import demand, and restricted revenues from tourism.

On the grounds of a resilient economy, the rating agency S&P in May revised its rating outlook from "negative" to "stable", at the same time affirming the upper non-investment grade rating of "BB+". Finally, with President Tayyip Erdogan further increasing his grip on Turkish politics, there is the looming danger of an even higher personalisation in decision making, which may negatively affect the quality of economic policies going forward.

Financial analyst: Andreas Schwabe, CFA, RBI Vienna

Key economic figures and forecasts

	2011	2012	2013	2014	2015	2016e	2017f
Nominal GDP (EUR bn)	555.2	612.2	618.8	602.5	647.1	676.8	794.5
Real GDP (% yoy)	8.8	2.1	4.2	2.9	4.0	3.5	3.5
Industrial output (% yoy)	10.1	2.5	3.1	3.6	3.2	3.5	3.0
Unemployment rate (avg, %)	9.1	8.4	9.0	9.9	10.3	10.0	10.0
Nominal industrial wages (% yoy)	8.0	6.0	6.0	n.v.	n.v.	n.v.	n.v.
Producer prices (avg, % yoy)	11.1	6.1	4.5	10.2	6.0	6.0	6.0
Consumer prices (avg, % yoy)	6.5	8.9	7.5	8.9	7.7	7.3	7.6
Consumer prices (eop, % yoy)	10.5	6.1	7.4	8.2	8.8	7.2	7.4
General budget balance (% of GDP)	-0.8	-2.1	-1.2	-1.3	-1.2	-2.0	-1.5
Public debt (% of GDP)	39.1	36.2	36.2	35.0	34.0	32.0	33.0
Current account balance (% of GDP)	-9.6	-6.1	-7.7	-5.4	-4.5	-5.0	-5.0
Official FX reserves (EUR bn)	68.0	90.4	95.1	105.2	101.7	104.8	117.6
Gross foreign debt (% of GDP)	39.3	43.1	47.3	50.3	55.4	55.1	52.3
EUR/TRY (avg)	2.34	2.31	2.53	2.90	3.02	3.20	3.02
USD/TRY (avg)	1.68	1.80	1.91	2.19	2.73	2.91	2.99

Source: Thomson Reuters, wiiw, RBI/Raiffeisen RESEARCH

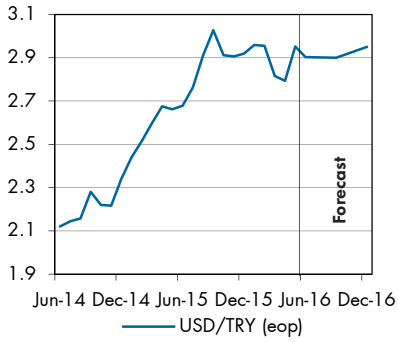
Financial market outlook

Security concerns and political uncertainty might weigh on the risk-sensitive lira. Investor fears about economic stagnation after Binali Yildirim became the new AKP leader and prime minister and half of the members of the cabinet have been replaced could be soothed as deputy prime minister Mehmet Simsek, a guarantor for investor confidence, retained his position. The market fears an extension of President Erdogan's power. He already signed a bill to lift the immunity of parliamentary members from prosecution, a constitutional change that could end with the removal of some pro-Kurdish opposition deputies from parliament. Moreover, the government wants to present a draft law introducing a presidential system to parliament by the end of the year. Snap elections are not planned. Ongoing security concerns due to bomb attacks and also disagreements between Turkey and the European Union and the crumbled relations with Russia are contributing to a declining number of foreign visitors and are accordingly leading to **further pressure on the TRY** due to diminishing capital flows. Tourism fell by 34.7% yoy in May (the biggest drop since 1994). The decline does not bode well for the tourism high season. The number of Russian visitors fell by 91.8%, the number of Germans by more than a third.

The further postponement of monetary policy tightening in the US in conjunction with receding global growth concerns were the main external drivers providing Turkish lira bonds some relief in April/May. Following the subsequent correction on the TURKGB market during May, we put Turkish bonds on Buy highlighting the speculative character of this call. For the time being, our recommendation dated 27 April 2016 has played out well, mainly driven by the favourable price performance amidst a fairly stable TRY versus EUR. At the same time, the normalisation of the yield curve shape – the slope turned positive end-March – continued. What definitely pulled some non-resident flows into the local currency debt market was the slow but continuing normalisation process of Turkish monetary policy under the new governor Cetinkaya against the backdrop of falling CPI inflation. For the time being, the Turkish central bank (TCMB) is about to symmetrise the o/n interest corridor that surrounds the 7.50% base rate. That being said, the TCMB already diminished the upper band whilst leaving all other rates constant. As a consequence, the weighted average costs of funding fell gradually over the past three months. Since **we see some room left for TURKGB gains (also helped by our expectations for TRY vs. EUR)**, we maintain our speculative Buy recommendation, which is additionally supported by the Brexit-induced dovish shift in the global central bank outlook. (International) political uncertainty, however, remains in place and poses a considerable risk to our call.

Financial analysts: Martin Stelzeneder, CEFA, Stephan Imre, RBI Vienna

Exchange rate development



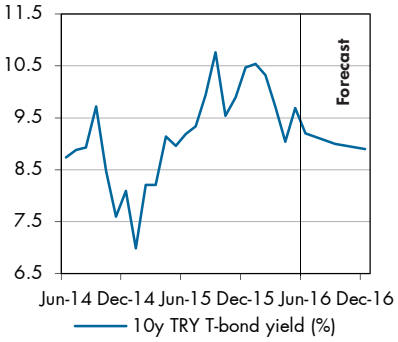
USD/TRY: 5y high 3.06, 5y low 1.61
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Exchange rate forecasts

	28-Jun[1]	Sep-16	Dec-16	Mar-17	Jun-17
EUR/TRY	3.21	3.19	3.10	3.09	2.92
Cons.		*3.30*	*3.21*	*3.19*	*3.07*
USD/TRY	2.90	2.90	2.95	3.00	2.95
Cons.		*3.00*	*3.06*	*3.10*	*3.10*

[1] 5:00 p.m. (CEST)
Source: Bloomberg, RBI/Raiffeisen RESEARCH

TRY yield development (%)



10y TRY T-bond yield: 5y high 11.08, 5y low 6.02
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Interest rate forecasts (%)

	28-Jun[1]	Sep-17	Dec-16	Mar-17	Jun-17
Key rate	7.50	7.50	7.50	7.00	6.50
Consensus		*7.75*	*7.75*	*7.75*	*7.80*
1 month[2]	9.60	10.50	10.00	9.50	9.00
3 month[2]	9.73	10.50	10.00	9.50	9.00
Consensus		*10.26*	*9.93*	*10.00*	*10.15*
6 month[2]	9.84	10.60	10.10	9.60	9.10
12 month[2]	9.94	10.70	10.20	9.70	9.20

[1] 5:00 p.m. (CEST) [2] Offered rate
Source: Bloomberg, RBI/Raiffeisen RESEARCH

Yield forecasts (%)

	28-Jun[1]	Sep-17	Dec-16	Mar-17	Jun-17
2y T-bond[2]	8.56	8.9	8.8	8.3	8.0
Consensus		*9.4*	*9.9*	*10.5*	*10.7*
10y T-bond[2]	9.20	9.0	8.9	8.6	8.5
Consensus		*9.7*	*10.1*	*10.9*	*11.1*

[1] 5:00 p.m. (CEST) [2] Bid yield
Source: Bloomberg, RBI/Raiffeisen RESEARCH

A colder outlook for summer ahead

- **Positive returns on CEE Eurobonds have been largely facilitated by slower Fed policy action**
- **Q3 likely to be more difficult for CEE due to tight valuations and Brexit fuelling greater uncertainty**
- **Rating upgrade story for Hungary and Slovenia may continue while Croatia and Romania face negative pressures**
- **In EUR we opt for Turkey, Hungary, and in USD for Serbia, also trading Romania for Turkey**

EMBIG USD index & spreads*

	28-Jun		Spread value, bp		
	Index	Spread, bp	qoq*	5y min	5y max
PL (A-)	610	149	16	71	361
LT (A-)	174	147	10	81	493
KZ (BBB)	190	352	-50	195	617
RO (BBB-)	152	229	28	141	528
TR* (BBB-)	742	316	16	170	411
HU (BB+)	305	245	27	162	726
RU (BB+)	1066	262	-32	155	702
HR (BB)	154	328	30	224	657
RS (BB-)	230	307	-23	217	724
BY (B-)	165	520	-9	466	1747
UA (B-)	648	749	-87	467	4281
Europe*	1126	317	-8	20	485
Africa	903	554	3	239	714
Asia	634	253	10	153	335
Mid East	489	574	29	328	602
Latam	647	537	-26	297	719
Global	**736**	**425**	**-5**	**244**	**532**
Inv.grade	**562**	**273**	**8**	**146**	**337**
BB	**720**	**340**	**-20**	**188**	**500**
B	**1127**	**570**	**-7**	**377**	**1099**

** S&P ratings, TR - Turkey Fitch rating, Europe - CEE, Q/Q - quarter-on-quarter (latest = cut-off date), 5y - 5-year minimum and maximum*
Source: Thomson-Reuters, RBI/Raiffeisen RESEARCH

CEE ratings direction

	rating *	Direction **
CE:		
CZ	AA-/A1/A+	⇔
SK	A+/A2/A+	⇔
PL	BBB+/A2/A-	⇔⇩
LT	A-/A3/A-	⇔
LV	A-/A3/A-	⇔
SI	A/Baa3/BBB+	⇧
HU	BB+/Ba1/BBB-	⇧
SEE:		
RO	BBB-/Baa3/BBB-	⇔⇩
BG	BB+/Baa2/BBB-	⇔
TR*	BB+u/Baa3/BBB-	⇔
HR	BB/Ba2/BB	⇩
RS	BB-/B1/BB-	⇔⇧
AL	B+/B1/n.r.	⇔
BH	B/B3/n.r.	⇔
EE:		
KZ	BBB-/Baa3/BBB	⇔
RU	BB+/Ba1/BBB-	⇔
BY	B-/Caa1/B-	⇔
UA	B-/Caa3/CCC	⇔⇩

*⇔ no change, ⇧ upgrade possible, ⇩ downgrade possible; * rating - S&P/Moody's/Fitch, Turkey S&P unsolicited rating; ** the likelihood of rating change in 3 to 12 months; Source: Rating agencies, RBI/ Raiffeisen RESEARCH*

Market trends

In the outgoing quarter, positive returns on CEE Eurobonds have been largely facilitated by slower Fed policy action which created positive backlash momentum on the emerging markets, leading to the compression of yields across the entire spectrum. **At the same time Brexit vote in UK brought only limited spread widening in CEE.** In the CEE market space, higher beta sovereigns were leading the market trend with the largest price gains coming primarily from EE (ex-CIS) markets. On the contrary, nearly all CE sovereigns delivered only smallish gains in Q2 due to their already tight spreads compared with EM peers. At the same time, CE still benefited from relative spread tightening vs. EU peripherals with average outperformance reaching about 30bp (or 18bp excluding Hungary). On the rating front, our anticipations were perfectly fulfilled with Hungary finally returning to investment grade after Fitch raised the HU sovereign from BB+ to BBB- with a stable outlook. Also, in June, both Slovenia and Serbia received a one notch upgrade from S&P and Fitch, which came on the back of strengthened public finances in both cases. Meanwhile, Poland became the only disappointment in CE after Fitch lowered its outlook to negative. In EE, Moody's downgraded the Kazakh FCY rating from Baa2 to Baa3 with a negative outlook while the agency positively affirmed Russia's rating at Ba1, removing the negative credit watch. **As the average rating score for CE firmed in line with our expectations, we see some risk to it emerging from Poland while there are good signs of the outlook stabilising for EE.** In SEE, we find Croatia's politics weakening its credit profile while fiscal risks increase in Romania ahead of the elections, which potentially could lead to a negative outlook change as well. In CE, we expect the rating upgrade story for Hungary and Slovenia to continue while Poland is subject to the risk of a one-notch downgrade in the next six months.

Primary markets

Overall CEE Q2 sovereign issuance went down to USD 9 bn equivalent compared with USD 12 bn in Q1. Poland, Turkey, and Slovenia were among the top three CEE issuers. Currency-wise, the majority of CEE opted for EUR denominated paper, which accounted for 62% of overall placements. Perhaps the most surprising placement was Russia's sovereign that was structured more like a domestic USD bond, with both custody and settlement assigned to National Settlement Depository instead of Euroclear after USA and EU recommended their banks and investors not to deal in Russia's issue. **We expect similar activity in Q3 with more placements likely in August or even September as post-Brexit uncertainty might limit July's activity.**

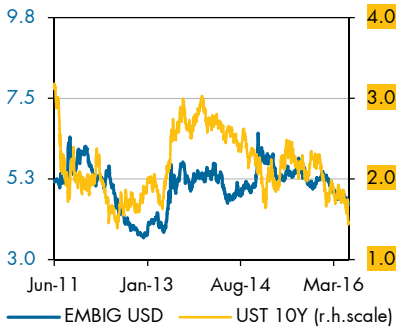
Outlook and strategy

Although the post Brexit vote uncertainty can manifest itself through lower market liquidity and higher risk aversion we do not anticipate larger reactions on CEE marketplace. In a nutshell, we believe that since the world central banks, including Fed and ECB, are likely to provide all support necessary for maintaining global finan-

cial system stability the low yield environment is likely to remain for longer time and would stimulate more hunt for yield in coming months. This, in turn, should preclude CEE Eurobonds from losing excessively in the risk spin-off scenario due to their relatively lower risk profile except EE. However, the approaching quarter is likely to be more difficult for CEE mainly due to prior market complacency about Fed policy tail risk leading to the accumulation of "valuation excesses" and still unclear future following the Brexit vote. In particular, the Fed's policy direction remains unchanged despite the expected delay of tightening, while ECB's extremely loose policy may not be enough to prevent negative spillovers from the Fed. In this situation, we expect higher volatility to return as investors may take a bearish turn on the back of post-Brexit uncertainty and mainly priced-in delay of Fed tightening. This, in turn, implies a relatively negative outlook for CEE. The second caveat could be overly optimistic CEE valuations that are not always supported by fundamental improvements. Another problem may be too tight CEE valuations vs. EU peripherals since the average spread between the two regions has tightened close to zero since the start of 2016, with CEE spreads only marginally bouncing back from their historical lows. As a result, we see no fundamental story to prove the need for a further spread reduction while the only reason for more tightening could be internal problems in the EU periphery itself. In this regard, **we find very little value in most of CEE as measured against EU peripherals** while on absolute scale CEE Eurobond yields remain close to historical lows, too. Speaking of country recommendations, we find very few directional trade opportunities in CEE. We believe that nearly all of CEE will be negatively affected in the USD segment, with slightly more stability expected for Serbia thanks to a positive fiscal turnaround and for Russia due to a possible easing of some sanctions at the end of 2016 or in early 2017. **In the EUR segment, we opt for Turkey due to surprisingly smooth economic performance and for Hungary and Serbia on the back of positive re-rating stories likely continuing.** At the same time, we recommend a tactical reduction of Croatian Eurobonds due to the political crisis negatively affecting the reform implementation agenda. In terms of relative value, we opt for going long on Turkey vs. short on Romania ahead of the autumn elections in Romania.

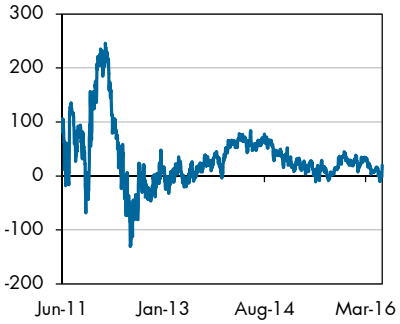
Financial analyst: Gintaras Shlizhyus, RBI Vienna

CEE EMBIG vs. UST 10y yields, %*



** JPM EMBI Global index family*
Source: Thomson Reuters, Bloomberg, RBI/Raiffeisen RESEARCH

CE/SEE vs. EUP spread*



** spread in basis points between CE/SEE and EU Peripheral (EUP) average 5y (duration adjusted) yields, CE/SEE - Czech, Hungary, Latvia, Lithuania, Poland, Romania EUR Eurobonds, EUP - Italy + Spain average 5y yields*
Source: Bloomberg, RBI/Raiffeisen RESEARCH

Benchmark Eurobond forecast and performance

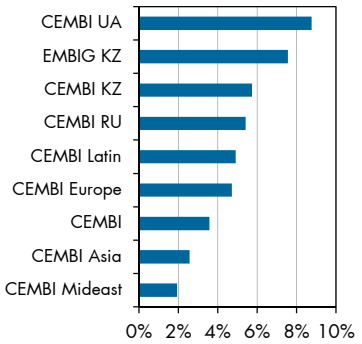
				Spread		Range			Spread	Range			Spread	Range		
Issue		Rating	Dur.	28-Jun	Sep-16	min.	max.	Perf. (%)	Dec-16	min.	max.	Perf. (%)	Mar-17	min.	max.	Perf. (%)
PL 3% due 23	USD	BBB+	6.0	**130**	**135**	131	142	-0.3	**136**	132	143	-1.1	**144**	140	151	-7.0
PL 4.5% due 22	EUR	BBB+	5.0	**88**	**90**	89	92	-0.1	**67**	67	69	0.5	**71**	70	73	0.3
LT 6.625% due 22	USD	A-	4.7	**163**	**150**	141	157	0.6	**151**	141	158	0.0	**157**	148	165	-4.6
LT 4.85% due 18	EUR	A-	1.6	**52**	**45**	40	54	0.1	**45**	40	54	0.0	**49**	44	58	0.0
TR 3.25% due 23	USD*	BBB-	6.0	**241**	**235**	231	255	0.3	**208**	204	228	1.2	**198**	194	218	-3.6
TR 5.125% due 20	EUR*	BBB-	3.6	**254**	**230**	213	245	0.9	**214**	197	229	1.2	**215**	199	231	1.2
RO 4.375% due 23	USD	BBB-	6.1	**187**	**190**	189	202	-0.2	**206**	204	217	-1.9	**218**	216	229	-8.2
RO 4.875% due 19	EUR	BBB-	3.1	**110**	**110**	107	120	0.0	**114**	110	123	-0.3	**122**	118	131	-0.5
BG 2% due 22	EUR	BB+	5.4	**210**	**200**	193	207	0.5	**183**	176	190	1.2	**198**	191	205	0.4
RU 4.5% due 22	USD	BB+	5.1	**229**	**220**	213	223	0.5	**237**	231	240	-1.0	**255**	248	258	-6.5
HU 5.375% due 23	USD	BB+	5.6	**220**	**195**	178	204	1.4	**197**	180	206	0.5	**200**	183	209	-4.6
HU 3.875% due 20	EUR	BB+	3.4	**98**	**90**	85	93	0.3	**82**	77	85	0.3	**85**	80	88	0.2
HR 5.5% due 23	USD	BB	5.6	**310**	**350**	336	378	-2.3	**372**	357	400	-4.2	**399**	385	427	-10.8
HR 3.875% due 22	EUR	BB	5.3	**388**	**400**	391	443	-0.6	**400**	392	443	-1.2	**421**	413	464	-2.3
RS 7.25% due 21	USD	BB-	4.4	**324**	**290**	278	302	1.5	**309**	297	321	0.3	**313**	301	325	-3.3
BY 8.95% due 18	USD	B-	1.4	**546**	**580**	556	592	-0.5	**580**	556	592	-0.6	**634**	610	646	-2.2
UA 7.75% due 27	USD	B-	7.1	**730**	**770**	756	784	-2.9	**777**	763	791	-4.2	**762**	747	776	-9.5

** USD bond spreads to UST notes, EUR bond spreads to German Bunds, Perf. as cumulative return of gross prices up to forecast horizon, countries sorted by S&P rating, Turkey - Fitch rating*
Source: Bloomberg, S&P, Fitch, RBI/Raiffeisen RESEARCH

Carry still attractive amid no imminent Fed tightening

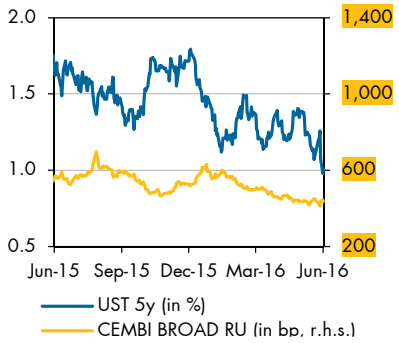
- **Solid carry and supporting oil price trajectory**
- **Spread tightening potential backed by technicals**
- **Fed dovishness back after Brexit vote**
- **Own shorter duration in export-oriented sectors**

Q2 2016 qtd returns



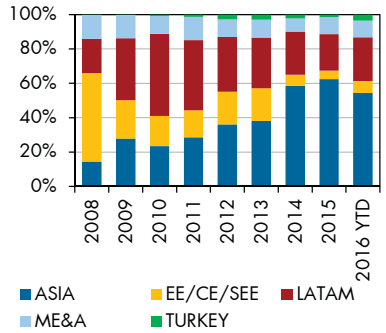
**data are for Broad Series*
5y average annual return in %: CEMBI Broad Mideast: 5.7, CEMBI Broad Asia: 6.2, CEMBI Broad: 5.1, CEMBI Broad Europe: 6.4,CEMBI Broad Latin: 3.3, CEMBI Broad RU: 7.3, CEMBI Broad KZ: 0.8, EMBIG KZ: 6.1, CEMBI Broad UA: 0.0
Source: JP Morgan, RBI/Raiffeisen RESEARCH

UST vs. CEMBI RU Index



UST: 5y high: 1.85 %, 5y low: 0.54 %
CEMBI BROAD RU: 5y high: 1,207bp; 5y low: 315bp
Source: Bloomberg, JP Morgan, RBI/Raiffeisen RESEARCH

EM corporate issuance (%)



Source: Bond Radar, RBI/Raiffeisen RESEARCH

We count on the solid carry, supporting oil price trajectory, and decent technical and fundamental pictures that will back valuations in the last two quarters of 2016. That said, we think that EE credits will remain well-bid thanks to the recurring dovishness of the Fed's monetary policy as the return to the hiking cycle will be likely postponed until December 2016.

Our oil analyst forecasts average Brent prices of 46 and 50 in Q3 and Q4 2016, respectively, compared with 48 now. In the event of any oil-induced consolidation in Q3 2016, we maintain our view that purchasing on lows may represent a good buying opportunity utilising transitory price weakness in the EE corporate credit space.

We argue that the spread tightening potential has still not been fully exploited and that a solid carry and spread pick-up to DM credits provides some mitigating power against rising risk-free rates. Today, Russian credits are trading about 190bp wide of this credit cycle's lows from back in 2011. Despite a different macro-backdrop and quite a progressed credit cycle today, we still believe that some tightening potential is in the cards going forward.

Oil price correlations remain in the driver's seat. The 90-day rolling correlation of the CEMBI Broad Russia Index spreads and the oil price sank to -0.98 against the 7y average of -0.67 while the 60-day rolling correlation stands at -0.96 versus the 7y average of -0.61. With that said, the oil price dependence of Russian spreads will remain the market-shaping factor more than anything else for now.

Despite the fact, that the Brexit vote result might have removed some tailwind from the Fed's tightening ambitions, we may witness a Fed rate hike in December 2016, which will eventually put a drag on valuations due to the likely upward shifts of the US Treasury curve. However, the postponement of Fed hikes to December will support valuations in Q3 2016. Furthermore, our economists forecast a 0.5% drop in Russian GDP this year. With that said, we recommend avoiding sectors with dominant exposure to the domestic recessionary environment with the exception of single credits representing strong outright mispricing stories. We have recently issued a buy call on VimpelCom 7.5043% due 2022, as it traded cheap against the universe of its index constituents and represented a high beta play at attractive spread levels. All in all, we recommend concentrating on the stronger credit stories in export-oriented sectors.

The oil and gas sector remains supported by the positive oil price trajectory. We stick to our view that the ongoing positive oil price momentum remains crucial for valuations. We are maintaining our buy call on Gazprom 8.625% due 2034. We suggest that the likelihood of a higher tax burden for hydrocarbon producers in the current year has been largely diminished. This is, in our view, due to the recovering oil prices and privatisation plans announced by the Russian government. Tax hikes are not off the table yet, however, more likely materialising in 2017 or beyond. To recap, the latest proposal of the Ministry of Finance envisages an increase in mineral extraction tax by lowering the base rate of USD 15/bbl, reflecting the lower production costs due to the weaker rouble. Such a dramatic increase in the tax burden levied on hydrocarbon producers would result in as much as a 20% impact or

more on EBITDA, which would result in negative drag on investment outlays. With that said, our house view is rather a compromise solution of about 5–10% average negative effect on EBITDA delayed to 2017 or beyond.

Technical situation remains favourable. Despite a slight pick-up in issuance activity, the technical situation remains supportive. Looking at the constituents list of the Russian sub-segment of the JPMorgan CEMBI Broad Index, we note that market capitalisation dropped by 27% yoy, adding a certain scarcity element to Russian credits, itself the largest stakeholder in the CEE credit remit.

New Russian issuance still remains rather contained due to the combination of imposed sanctions, elevated funding costs, and the deleveraging focus of a number of corporates. Although new corporate issuance in Russia picked up from an equivalent of USD 3.7 bn in the whole of 2015 (0 in the first 6m of 2015) to an equivalent of USD 4.3 bn ytd, it still lags behind the pre-crisis levels (first 6m of 2014: an equivalent of USD 9.9 bn). From where we stand now, we expect no progress on the sanctions front until the end of 2016, with the gradual phasing out of sanctions subject only to more progress being made on the Minsk II front. That said, we expect only a gradual and continuously hesitant pick-up in issuance towards the end of 2016 as the spread compression on the secondary market reduces funding costs and makes Eurobond markets more attractive.

Primary market activity picked up in the whole CEE corporate space in yearly comparison. The irresolute start to 2016 marked by sparse issuance was reversed in Q2. Total EM corporate issuance dropped from an equivalent of USD 172 bn in the first six months of 2015 to an equivalent of USD 113 bn in the same period of this year, a 34% decline. Looking at primarily market activity in the CEE corporate space, the picture was completely different.

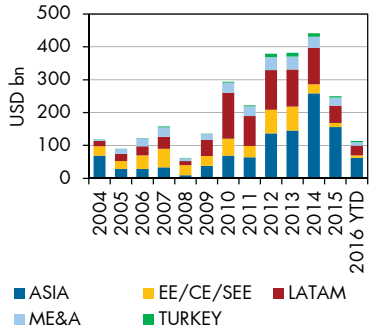
CEE corporates issued an equivalent of USD 8.0 bn in bonds in the first six months of 2016 compared with an equivalent of USD 4.9 bn in the respective period of 2015, for a 62% increase yoy. Taking a look at the regional composition, EE credits were leading the pack with a 62% share, ahead of CE at 30% and SEE at 0% of the total.

Turning to performance, EE credits remained well-bid in Q2 2016 and outperformed their direct EM peers by a wide margin. The EM credit index delivered 3.6% while the three best-performing markets were Kazakh quasi-sovereigns (EMBIG KZ, 7.6%), Kazakh non-quasi-sovereigns (CEMBI KZ, 5.7%), and Russia (5.4%) ahead of LatAm (4.9%), Asia (2.6%), and MidEast (1.9 %).

The relatively solid performance of Kazakh credits can be ascribed to the stabilisation of the USD/KZT exchange rate after the introduction of free float back in August 2015. To recap, the tenge strengthened by about 13% against the dollar since its lows registered in January 2016. Looking at our covered universe in Kazakhstan, we have one outstanding buy recommendation on Halyk Bank's 2021 bond. Furthermore, we ascribe the relatively good performance of Russian credits in Q2 2016 to the generally supportive oil price environment and the dovish tone of the Fed's monetary policy. To recap, the oil price surged by almost 23% in the quarter-to-date and the US Treasury yield curve shifted downward by 32, 22, and 16bp in the 10y, 5y, and 3y segments, respectively. Looking at the basic performance breakdown, 75% of the yield drop in Russia was explained by spread compression as the spreads tightened by 65bp and yields dropped by 87bp. A similar pattern was seen in Kazakhstan, where spreads compressed by 36bp and yields dropped by 54bp. Turning to Ukraine, we note that the investible universe covered by the respective sub-index contained only one bond in June, namely MHP 8.25% due 2020, representing a drop from two bonds after the April rebalancing.

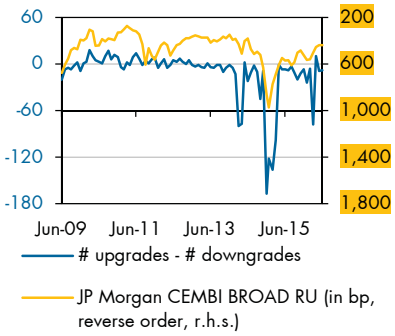
Financial analyst: Martin Kutny, CFA; RBI Vienna

EM corporate issuance



Source: Bond Radar, Bloomberg, RBI/Raiffeisen RESEARCH

Rating drift in Russia



CEMBI BROAD: 5y high: 571bp; 5y low: 296bp
Source: Bloomberg, JP Morgan, RBI/Raiffeisen RESEARCH

Selected EE Eurobonds

Issuer	ISIN	Maturity	Yield in %
Alfa Bank	XS0544362972	25/09/2017	2.3
Evraz	XS0618905219	27/04/2018	4.6
Gazprom	XS0708813810	23/01/2021	4.1
Sberbank	XS0799357354	28/06/2019	2.9
Vimpel-Com	XS0587031096	02/02/2021	5.1

Source: Bloomberg, RBI/Raiffeisen RESEARCH

Restrained development expected

- **No boost from earnings development**
- **Valuations moderate**
- **"Hold" recommendation for the third quarter**

Value matrix*

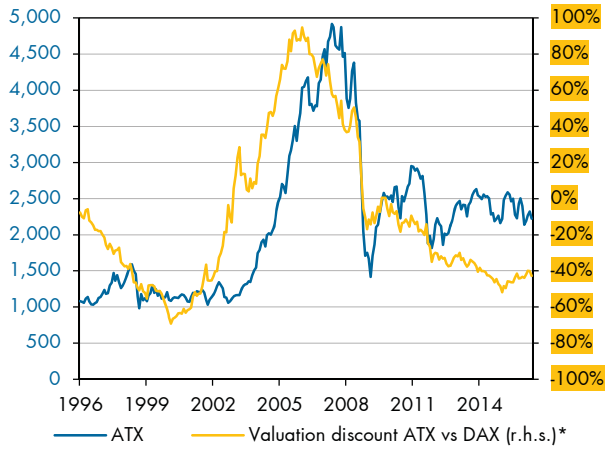
Domestic business activity		2	(2)
Exports	OECD – excl. Eastern Europe	2	(2)
	Eastern Europe	2	(2)
	Asia	3	(3)
Company earnings		3	(3)
Key sectors		2	(2)
Valuation – P/E-ratio		2	(2)
Interest rates / yields		1	(1)
Exchange rates		2	(2)
Foreign equity markets		2	(2)
European liquidity		1	(1)
Technical outlook		3	(2)

1 (4) denotes highly positive (negative) influence on the market. All factors are weighted equally.
** expected trend for the next 3 to 6 months*
Previous assessment in parentheses
Source: RBI/Raiffeisen RESEARCH, Raiffeisen Centrobank

The **development of the Austrian equity market** during the last period under review was all in all rather **restrained**. Even though the ATX had more or less tended to move sideways for some time, it clearly lost ground over the course of the British EU referendum. The Austrian leading index was gravely affected by the fact that a large weighting within the index is attributed to the financial sector. Anyway, it became clear again that in times of increased risk aversion the decoupling from international stock markets is hardly possible.

We feel that the **economic conditions** are **solid** and stable. The euro area economy will recover further this year. Activity in Austria in the first quarter was higher than the same period of the previous year. Domestic demand was an important support factor. For now, it seems that the moderate economic recovery will continue. At least as far as can be read from the available leading indicators. On this basis, we expect GDP growth of 1.4% in 2016, which would not reach our projected aggregate growth rate for the euro area (1.6%). In Eastern Europe, it is again the CE countries that are showing the most satisfactory economic development. We expect no positive dynamics in Russia. Even though the latest data brought positive surprises, we still expect the economy to contract (-0.5%) in 2016.

ATX shows valuation discount



** cyclically adjusted price/earnings ratio based on rolling 10 year trailing index earnings*
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

The **influence of the ECB** and its policies will continue to be important for the Austrian equity market. In any case, we see no **direct driver in the addition of corporate bonds to the securities purchasing programme**. In fact, this is being viewed with increasing criticism on the capital markets because of the lack of effects on the economy and inflation so far. In general, however, the ECB's policy will ensure that yields in the fixed-income segment will not rise to any great extent, preserving the relative attractiveness of the equities segment. The absolute **valuations** are also still **not expensive**. We calculate a P/E ratio of 11.6 for the ATX companies based on our estimated adjusted earnings for 2016. This means that the valuation discount versus most of the Western European equity markets will re-

Sector structure of the ATX

Sector	Company	Weight
Financials	BUWOG, CA Immobilien, conwert, Erste Group, Immofinanz, Raiffeisen Bank International, Uniqa, Vienna Insurance Group	46.5%
Industrials	Andritz, Österreichische Post, Wienerberger, Zumtobel	19.0%
Energy	OMV, SBO	15.0%
Basic materials	Lenzing, RHI, voestalpine	13.5%
Telecom	Telekom Austria	2.3%
Utilities	Verbund	2.8%
IT	AT&S	0.9%

Source: RBI/Raiffeisen RESEARCH, Raiffeisen Centrobank, Vienna Stock Exchange

main. The valuation of the ATX is also in good company with the most important indices in Central Europe (such as the BUX and WIG 30).

We are conservative on **earnings development** for this year. The most recent figures published during the reporting period were solid in general. In terms of the heavyweights, Erste Group again delivered better-than-expected results. OMV and Andritz more or less met the expectations with their earnings. The outlooks for the most important ATX companies are unchanged for the most part. However, the outlook for Erste Group may prove to be rather cautious. OMV and Wienerberger saw no cause to make changes, and Andritz sees decreasing revenue but improved profitability. The influence of a Brexit is only significant for a few Austrian companies due to their exposure (for example, Wienerberger or Zumtobel). Indirect effects could however also come into play in the medium- to long-term through the risk of reduced budgets for EU funds and weaker FX currencies could impact CEE-exposed names. Protracted lower interest rates could affect financial companies on further shrinking reinvestment yields. All in all, we expect profits to decline, on an aggregated level, by up to 10% year-over-year.

Summary: The commotion surrounding the referendum in UK will most likely not calm down too quickly. Therefore, the political risk remains an essential factor for European capital markets. Apart from that, we see the external influences to be less distinctive this time. We currently consider the ECB's actions to be a supportive factor. However, in our opinion, because of this, especially the relative appeal over the fixed income segment remains. In terms of economic development, we also expect no immediate boost. It is indeed true that the economic recovery in Austria, and within the euro area, is making progress, however one should continue to not expect any big jumps in this regard. In fundamental terms, we continue to see no sufficient momentum, which could trigger positive effects on the development of stock prices. In contrast, valuations however, remain moderate. All in all, the prevailing influence factors suggest a rather restrained development of the **ATX** during the **third quarter** and we therefore assign a **"hold" recommendation** to it.

Financial analyst: Johannes Mattner, CFA, RBI Vienna

Fair value of ATX[1] – June 2017

	Bond yields (10y)		
EY-BY[2]	**0.75%**	**1.00%**	**1.25%**
10.00%	1,940	1,896	1,854
9.75%	1,986	1,940	1,896
9.50%	2,035	1,986	1,940
9.25%	2,086	2,035	1,986
9.00%	2,139	2,086	2,035
8.75%	2,196	2,139	2,086
8.50%	2,255	2,196	2,139
8.25%	2,318	2,255	2,196
8.00%	2,384	2,318	2,255
7.75%	2,454	2,384	2,318
7.50%	2,528	2,454	2,384
7.25%	2,607	2,528	2,454
7.00%	2,691	2,607	2,528
6.75%	2,781	2,691	2,607

[1] based on the expected earnings for 2016/2017 (i.e. 208.6 index points)
[2] earnings yield less bond yield
Source: RBI/Raiffeisen RESEARCH, Raiffeisen Centrobank

Earnings yield* less bond yield

** earnings yield = E/P; based on 12-month forward earnings*
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH, Raiffeisen Centrobank

Valuation and forecasts

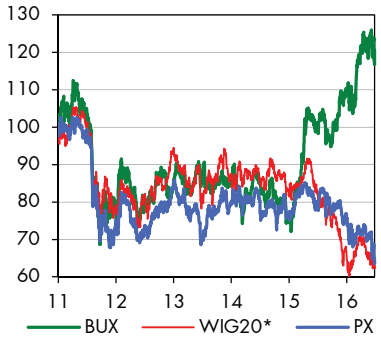
	28-Jun[1]	Sep-16	Dec-16	Mar-17	Jun-17
12-months forward earnings	209.3	183.6	192.0	200.3	208.6
Bond yield forecast	0.26	0.40	0.60	0.75	1.00
Earnings yield less bond yield (EY-BY)	**10.06**	**8.50**	**8.50**	**9.00**	**9.75**
ATX-forecast based on EY-BY		2063	2110	2054	1940
ATX-forecast	**2,028.0**	**2,050**	**2,100**	**2,000**	**1,950**
Expected price change		1.1%	3.6%	-1.4%	-3.8%
Range		1,800-2,250	1,800-2,250	1,800-2,250	1,800-2,250
P/E based on 12-month forward earnings	9.7	11.2	10.9	10.0	9.3

[1] 11:59 p.m. (CEST); Source: RBI/Raiffeisen RESEARCH, Raiffeisen Centrobank

Expansive monetary policy providing support

- **Moderate valuation of many CEE indices**
- **Political uncertainty regarding Brexit could have negative impact**
- **Oil price recovery providing support**
- **Still no normalisation of political relations with Russia**

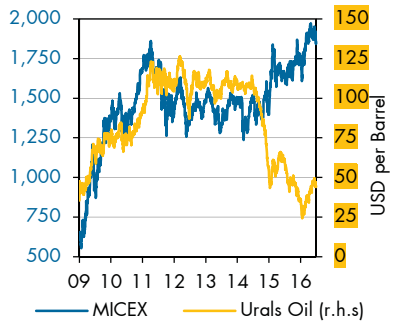
CE core equity indices



In local currency
** due to the short data history of the WIG 30 index we still use the WIG 20 for this chart*
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

The CEE equity markets again developed differently in the second quarter of 2016. While the indices in Russia, Hungary, and Croatia were all stable, the other leading indices from Poland, the Czech Republic, Turkey, and Romania suffered above-average losses. In addition to home-brewed problems (such as in Poland), speculations about an interest rate hike in the US, and lacklustre economic data from China and Japan, uncertainty ahead of the referendum on Britain exiting the EU and the result of this referendum caused poorer price development. In light of the roughly two-year transitional and negotiation period, the short-term economic effects will be negligible, and the increase in the oil price and the still ultra-loose monetary policy of most central banks should provide sufficient support for the equity markets. The political uncertainty surrounding the potential for further exit referendums, which could cause greater jitters depending on the final terms of the exit given the coming parliamentary elections in 2017 (Germany, France, the Netherlands), is a more substantial factor, however. Therefore, we are expecting stable conditions in the third quarter thanks to the high liquidity and solid economic growth that we are projecting, but are cautious at a one-year horizon.

MICEX vs oil price



Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

With the recession petering out, the Russian economy is now recovering slowly from its low. While the economy can not be expected to provide any real support to the **Russian equity market**, the gradual exit from the valley of tears was enough on its own to improve sentiment and to allow the leading MICEX index to reach new record highs in Q2 in combination with the climbing oil price. The black gold will still be the most important driver in the coming quarter due to the recent strong correlation with Russian equities. After the marked uptrend since the lows in January (+81%), a break in the coming weeks with a setback for Russian energy stocks would come as no surprise, but the general direction of oil for the next 24 months should be positive overall. In valuation terms, the companies in the MICEX are 47% cheaper than the rest of the emerging markets with an aggregate P/E ratio of 6.8 on an index basis, and are therefore rather attractive. Eliminating the generally lower-valued energy sector, this represents a valuation discount of roughly 34%. In terms of the Western sanctions against Russia, on the other hand, no agreement about easing or gradual lifting is likely before the beginning of 2017. The prospects for further interest rate cuts and the sustainable appreciation of the rouble (which is especially relevant for foreign investors) are sources of support. The Rus-

Value matrix stock markets

	PL		HU		CZ		RU		RO		HR		TR	
Politics	4	(4)	2	(2)	2	(2)	3	(3)	4	(3)	4	(3)	4	(3)
Interest rate trends	2	(2)	2	(1)	2	(1)	2	(3)	2	(2)	2	(2)	3	(4)
Earnings outlook	3	(2)	2	(2)	3	(2)	3	(3)	1	(2)	4	(4)	2	(2)
Key sectors	4	(4)	2	(2)	2	(3)	2	(2)	3	(2)	2	(2)	2	(2)
Valuation (P/E)	2	(2)	2	(2)	2	(2)	1	(1)	2	(1)	3	(3)	2	(1)
Liquidity	2	(1)	3	(3)	3	(3)	2	(1)	3	(3)	4	(4)	1	(1)
Technicals	3	(1)	1	(1)	3	(2)	2	(3)	2	(2)	3	(1)	2	(1)

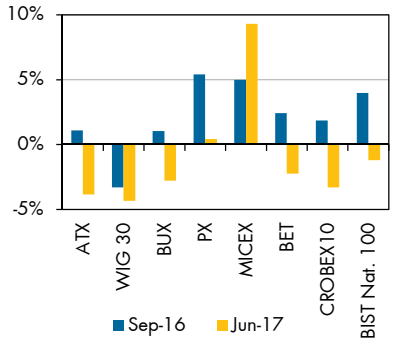
1 (4) denotes highly positive (negative) influence on the market. All factors are weighted equally. Assessment refers to a 3-month period. Figures in brackets reflect our former assessment.
Source: RBI/Raiffeisen RESEARCHSource: RBI/Raiffeisen RESEARCH

sian equity market should experience the latter above all through the pricing out of economic risks and a further increase in the price of oil. **Buy**.

The **Polish** equity index **WIG 30** suffered disproportionate losses compared with its local peers in the second quarter of 2016. However, this is not attributable to the very solid economic environment in Poland (2016 GDP growth estimated at 3.5% for 2016), but rather to the ongoing political uncertainty. Beginning with the coming restructuring of the CHF loans (the basic elements of the "CHF Fix" programme were already presented in June), this also includes additional taxes (for example on banks and insurance companies, retailers, etc.) and worries about the independence of various institutions. The fact that new discussions about a reform of the private pension funds could begin in the second half of the year is another exacerbating factor. No details have yet been released, but the goal may be a merger of the twelve private funds into a single state-run pension fund. In light of the statement that the current equities-based approach is not "efficient", we do not expect a reform that is friendly for the equity market. Despite the quite solid fundamental conditions, we must take the political risk into account, and consequently we opt for a cautious position, both for the coming quarter and over a one-year horizon. **Sell**.

The leading **Czech** index **PX** was hit hard with a loss of around 10% in the second quarter. This makes for a total loss of around 15.7% since the beginning of

Expected index performance



Source: RBI/Raiffeisen RESEARCH

Indices in performance comparison

	2007	2008	2009	2010	2011	2012	2013	2014	2015	28-Jun-16[1]
ATX	1.1%	-61.2%	42.5%	16.4%	-34.9%	26.9%	6.1%	-15.2%	11.0%	-15.4%
BUX	5.6%	-53.3%	73.4%	0.5%	-20.4%	7.1%	2.2%	-10.4%	43.8%	9.6%
WIG 20[2]	5.2%	-48.2%	33.5%	14.9%	-21.9%	20.4%	-7.0%	-3.5%	-19.7%	-5.8%
PX	14.2%	-52.7%	30.2%	9.6%	-25.6%	14.0%	-4.8%	-4.3%	1.0%	-15.7%
MICEX	11.5%	-67.2%	121.1%	23.2%	-16.9%	5.2%	2.0%	-7.1%	26.1%	5.4%
BET	22.1%	-70.5%	61.7%	12.3%	-17.7%	18.7%	26.1%	9.1%	-1.1%	-8.0%
CROBEX	63.2%	-67.1%	16.4%	5.3%	-17.6%	0.0%	3.1%	-3.1%	-2.8%	-1.6%
BIST Nat. 100	42.0%	-51.6%	96.6%	24.9%	-22.3%	52.6%	-13.3%	26.4%	-16.3%	7.3%
CECE Composite Index	10.5%	-53.7%	40.5%	15.7%	-29.1%	25.7%	-9.6%	-6.0%	-12.4%	-10.3%
DAX	22.3%	-40.4%	23.8%	16.1%	-14.7%	29.1%	25.5%	2.7%	9.6%	-12.1%
Euro Stoxx 50	6.8%	-44.4%	21.1%	-5.8%	-17.1%	13.8%	17.9%	1.2%	3.8%	-15.6%
S&P 500	3.5%	-38.5%	23.5%	12.8%	0.0%	13.4%	29.6%	11.4%	-0.7%	-0.4%
MSCI World	2.8%	-40.1%	22.8%	7.8%	-7.6%	13.1%	26.3%	7.7%	0.2%	-4.9%

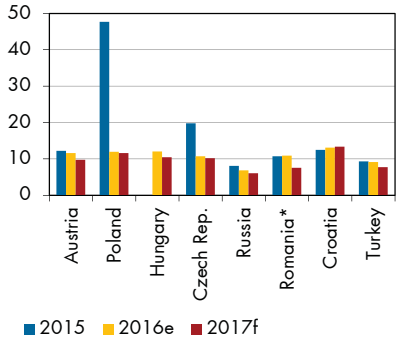
In local currency
[1] 11:59 p.m. (CEST)
[2] Due to the short data history of the WIG 30 index we still use the WIG 20
Source: Bloomberg, Thomson Reuters, RBI/Raiffeisen RESEARCH

Stock market indicators

	Long-term earnings growth	Earnings growth			Price/earnings ratio			Dividend yield
		15	16e	17f	15	16e	17f	16e
ATX	4.3%	71.0%	-7.7%	19.0%	12.2	11.6	9.7	3.2%
WIG 30	2.9%	-56.5%	397.7%	2.9%	47.7	12.0	11.6	4.0%
BUX	3.7%	n.v.	n.v.	16.1%	n.v.	12.1	10.4	2.9%
PX	3.6%	n.v.	9.7%	5.2%	19.8	10.7	10.2	6.2%
MICEX	3.2%	17.2%	0.2%	12.9%	8.1	6.8	6.1	5.2%
BET*	5.1%	-43.1%	25.6%	44.0%	10.7	10.9	7.5	5.3%
CROBEX10	1.9%	224.8%	-58.5%	-1.5%	12.5	13.1	13.3	2.8%
BIST Nat. 100	4.8%	-10.3%	8.9%	18.1%	9.3	9.1	7.7	3.1%

** Romania (BET) excl. Fondul Proprietatea*
Source: Thomson Reuters, IBES, Bloomberg, RBI/Raiffeisen RESEARCH

P/E ratios in comparison

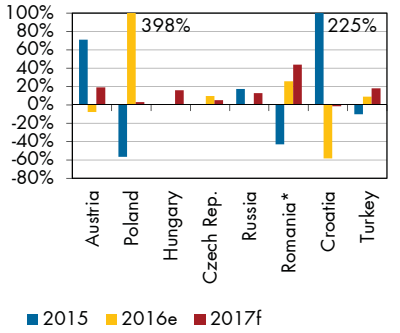


** Romania (BET) excl. Fondul Proprietatea*
Source: Thomson Reuters, IBES, Bloomberg, RBI/Raiffeisen RESEARCH

the year. The banking and insurance sector, which makes up around 50% of the PX, was again the source of the majority of the substantial losses. However, we also expect that the financials in the PX have bottomed out. There are strong arguments for the Czech market from a fundamental perspective at present. Year-on-year economic growth of 3.0% in the first quarter combined with the lowest unemployment rate (April/seasonally adjusted) of all EU states in the amount of 4.1% speak for themselves. The announcement by the Czech central bank that it will be supporting the CZK/EUR exchange rate at around 27 until about the middle of 2017, instead of early 2017 – as stated before, should also provide additional support. The anticipated aggregate earnings increase for the index in 2016 now amounts to 9.7%. This translates to an expected P/E ratio of 10.7 for 2016, which is moderate by historical standards. In line with the solid economic prospects (2016e GDP: 2.3%), we therefore expect good performance by the Czech PX index. **Buy**.

The **Hungarian** stock index **BUX** was unable to sidestep the effects of the increased risk aversion (Brexit), but was still rather stable in Q2. In addition to the solid development of the economy (expected GDP growth: 2.2% and 2017: 2.7%), the Hungarian equity market also profited from the latest interest rate cuts (most recently by 15bp) to 0.9%. After Fitch raised its rating for Hungary to investment grade in May, we now see greater potential for Moody's following suit during one of its next reviews (8 July or 18 November) due to the very solid economic data. The aggregated 2016e P/E ratio based on the consensus estimates is currently 12.1, which we feel is moderate. **Hold**.

Earnings growth



** Romania (BET) excl. Fondul Proprietatea*
Source: Thomson Reuters, IBES, Bloomberg, RBI/Raiffeisen RESEARCH

The increasing political risk (bombings, Erdogan's authoritarian leadership style, doubts about the independence of the central bank) and speculations about interest rate hikes by the Fed caused investors to sell off Turkish equities in Q2. A total of USD 798 mn was withdrawn from the Istanbul exchange in the five weeks from the beginning of May to the end of June. Even though the tourism industry is suffering in particular from a lack of Russian guests (-79% in annual comparison), the economic outlook is still providing a solid foundation for the future development of the **Turkish BIST National 100**. Economic growth (2016e: 3.5%) should be boosted by private consumption, which should profit from the 30% minimum wage increase. Therefore, we see the corporate earnings projections (2016e: +8.9%; 2017f: +18.1%) as being on solid footing. After the latest price declines,

Index estimates

	28-Jun[1]	Sep-16	Dec-16	Mar-17	Jun-17	Recommendation
ATX	2,028	2,050	2,100	2,000	1,950	**HOLD**
Performance		1.1%	3.6%	-1.4%	-3.8%	
Range		1,800-2,250	1,800-2,350	1,750-2,200	1,700-2,150	
WIG 30	1,954	1,890	1,940	1,910	1,870	**SELL**
Performance		-3.3%	-0.7%	-2.3%	-4.3%	
Range		1,700-2,200	1,750-2,150	1,700-2,100	1,650-2,050	
BUX	26,227	26,500	27,000	26,500	25,500	**HOLD**
Performance		1.0%	2.9%	1.0%	-2.8%	
Range		23,500-29,000	23,500-29,500	23,000-29,000	22,500-28,000	
PX	806	850	860	830	810	**BUY**
Performance		5.4%	6.6%	2.9%	0.4%	
Range		700-900	710-1,000	670-970	650-950	

In local currency
[1] 11:59 p.m. (CEST)
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

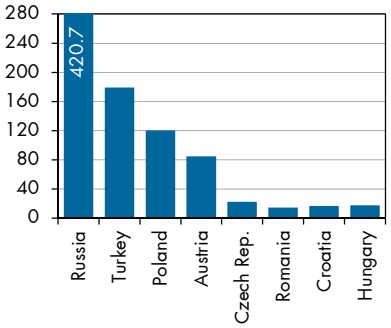
we see the companies in the BIST National 100 as having very attractive valuations again at a P/E ratio of 9.1. **Buy**.

The leading **Romanian** index **BET** posted a loss of 4.4% in the second quarter. The controversial mortgage loan law that went into force in May could cause property values to fall by between 5% and 10% according to estimates of the local central bank. The continued loose fiscal policy (including a VAT reduction and minimum wage hike by 19%) is also fuelling fears of a possible rating downgrade, which would of course also negatively impact Romanian equities. Economic conditions in Romania are currently much better than the equity market would lead one to believe. The Romanian exchange barometer should also profit from one of the highest rates of GDP growth in all of Europe – we expect a plus of 4% for 2016. However, we are cautious one quarter out, especially as not only a possible rating downgrade but also uncertainty ahead of the coming parliamentary elections (scheduled for November 2016) could put the equity markets under further pressure. **Hold**.

The **Croatian** equity market index **CROBEX 10** has been almost unchanged since the beginning of the year with a loss of 1.8%. The still excessive public debt is hampering sorely needed structural reforms and government investments. But reforms are still a way off. Because Croatia's government is history just five months after being sworn in. Observers are now expecting new elections in September. Part of the funds to pay off the debts is to be raised through privatisation. In this, however, the Croatian privatisation agency (CERP) suffered a setback. It was unable to sell its close to 30% share in the hotel chain Suncani Hvar on the Zagreb Stock Exchange (ZSE). The average daily trading volume on the ZSE, which is plagued by low turnover anyway, fell by 8.9% in annual comparison in the first quarter. In light of our projected aggregate 2016e P/E ratio of 13.1 on an index basis and an average earnings contraction of 58.5% for the companies in the CROBEX10 (caused among other things by the basis effect from the above-average profit of Adris Grupa in connection with the sale of its tobacco division), we see little potential for improvement in the Croatian leading index at a one-year horizon, also considering the political turmoil. **Hold**.

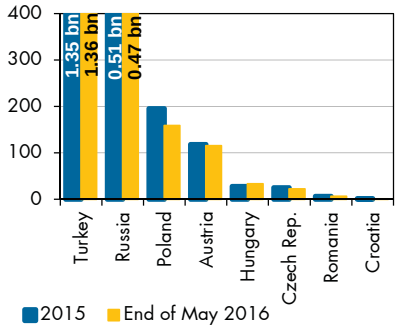
Financial analysts: Aaron Alber, Andreas Schiller, Christoph Vahs; RBI Vienna

Market capitalisation overview



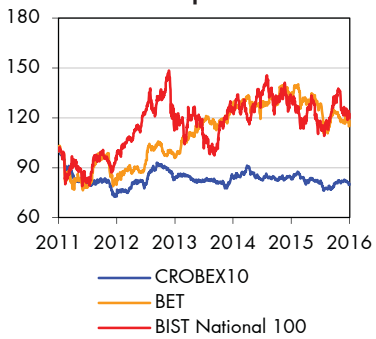
In EUR bn; end of May 2016
Source: FESE, WFE, ZSE, RBI/Raiffeisen RESEARCH

Avg. daily turnover (EUR mn)



Source: FESE, WFE, ZSE, RBI/Raiffeisen RESEARCH

SEE indices in comparison



Source: Bloomberg, RBI/Raiffeisen RESEARCH

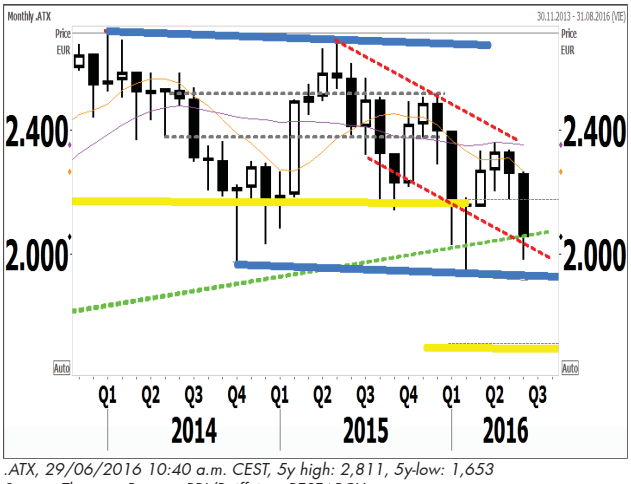
Index estimates

	28-Jun[1]	Sep-16	Dec-16	Mar-17	Jun-17	Recommendation
MICEX	1,857	1,950	2,000	2,020	2,030	**BUY**
Performance		5.0%	7.7%	8.8%	9.3%	
Range		1,650-2,100	1,800-2,200	1,850-2,250	1,850-2,250	
BET	6,444	6,600	6,700	6,500	6,300	**HOLD**
Performance		2.4%	4.0%	0.9%	-2.2%	
Range		5,500-8,000	5,500-8,100	5,000-7,500	5,000-7,500	
CROBEX10	972	990	990	960	940	**HOLD**
Performance		1.9%	1.9%	-1.2%	-3.3%	
Range		880-1100	880-1100	850-1100	850-1100	
BIST Nat. 100	76,929	80,000	82,000	79,000	76,000	**BUY**
Performance		4.0%	6.6%	2.7%	-1.2%	
Range		67,000-85,000	75,000-87,000	72,000-85,000	70,000-82,000	

In local currency
[1] 11:59 p.m. (CEST)
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Stock Markets: Mixed Picture

ATX



.ATX, 29/06/2016 10:40 a.m. CEST, 5y high: 2,811, 5y-low: 1,653
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

ATX

Last: 2,056 **NEUTRAL**

The ATX just has hit its neutral range's lower band at 1,980 (blue lines, since 05/11/2013) and thus puts the upward-trend which is in effect since April 2009 into question. As long as bearish confirmation at 1,910 (-> 1,707 – 1,500) is lacking , it might as well perform a bullish reversal with 2,100 (-> 2,170 – 2,230 – 2,300).

Position:

Buy	2,100	-> 2,230 – 2,300
Sell	1,910	-> 1,707 – 1,500

BIST National 100

.XU100, 29/06/2016 11:00 a.m. CEST, 5y high: 93,179, 5y-low: 49,622
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

BIST National 100

Last: 76,778 **NEUTRAL**

The Triangle within range 73,150 – 90,720 (blue lines) provides support by its lower band. Thus the chance on a bullish signal at 77,810 and even 80,200 (-> 85,000 – 86,870) still is there. Else, a sell-signal would get triggered at 73,150 (-> 69,200 – 68,230).

Position:

Buy	77,810	-> 80,200 – 85,000
Sell	73.150	-> 69,200 – 68,230

BUX

.BUX, 29/06/2016, 11:15 a.m. (CEST), 5y high 27,397, 5y low 14,930
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

BUX

Last: 26,316 **~BULLISH**

Since April a pattern per se to be neutral to be rated, a so-called "Diamond" (grey lines), is being formed. For a buy-signal it would have to cross 26,600, the Diamond's center line, first and both 27,480, the pattern's high, and 27,930 (-> 28,690 – 29,450) subsequently, while 25,505 (-> 24,150 – 23,270) would have to hold firm.

Position:

Buy	26,600	-> 27,480 – 27,930
Stop	25,050	

CROBEX 10

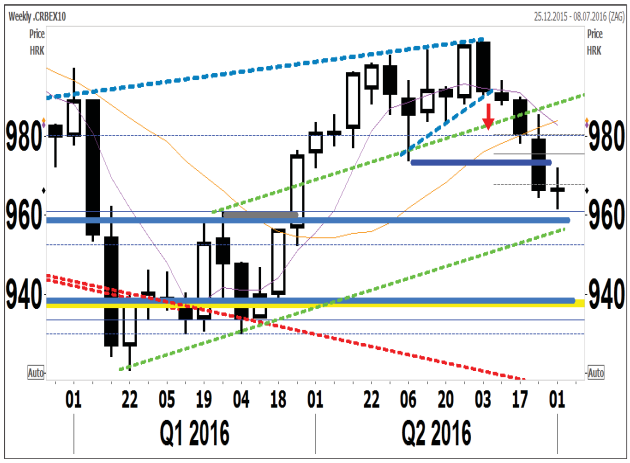
Last: 966 **~BEARISH**

The major support 955 almost has been hit. In case it does not hold firm the current retracement would continue towards 935 - 920 which seems being expectable. Should instead the support 955 prove firm, a rebound to about 980 would be due.

Position:

Short -> 935
Stop 973

CROBEX



.CROBEX10, 29/06/2016 10:30 a.m. CEST, 5y high: 1,210, 5y-low: 879
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

MICEX

Last: 1,873 **NEUTRAL**

The current congestion in between 1,825 – 1,980 has begun to form on 21.04.2016. A first bullish signal would be the crossing of 1,925, while a first bearish one would be a drop through 1,820 that could stretch towards 1,770 and even 1,700 again.

Position:

Buy 1,925 -> 1,980 – 2,100
Sell 1,820 -> 1,770 – 1,700

MICEX

.MCX, 29/06/2016 11:35 a.m. CEST, 5y high: 1,970, 5y-low: 1,237
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

WIG 30

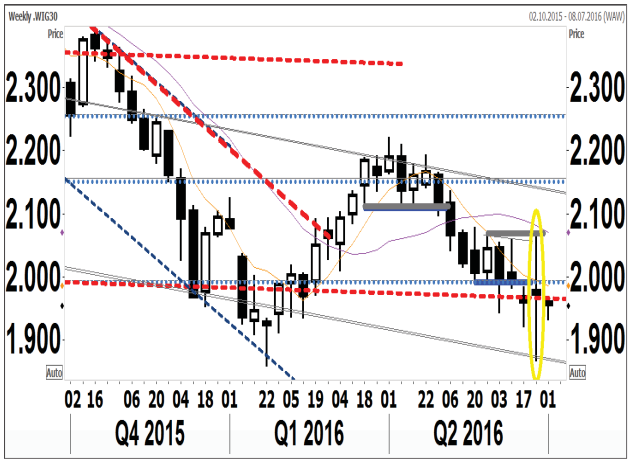
Last: 1,954 **NEUTRAL**

The current congestion, in effect since 21/01/2016, might become a Double-Bottom with 2,222 (-> 2,400), yet a first bullish signal at the 50%-level of last week's Rickshaw Man Doji would be required, e.g. a move past 2,000 (-> 2,044 – 2,133). Else, 1,1850 (-> 1,760 – 1,620) cannot be excluded.

Position:

Buy 2,000 -> 2,044 – 2,133
Sell 1,900 -> 1,850 – 1,760

WIG 30



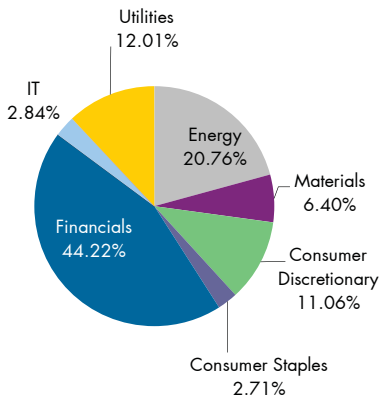
.WIG30, 29/06/2016 11:45 a.m. CEST, 5y high: 2,775, 5y-low: 1,879
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Financial analyst: Robert Schittler, RBI Vienna

Sector weightings in comparison

Sector weightings Poland, WIG 30

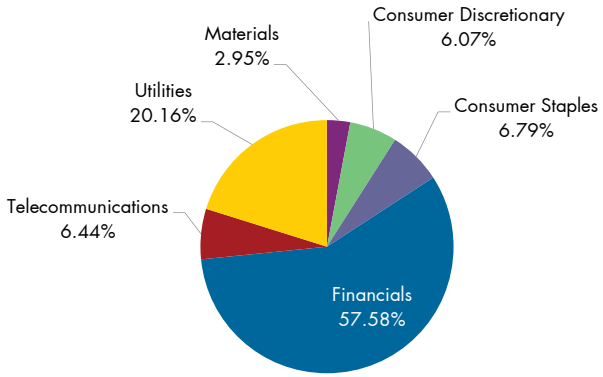
Dom. market cap.: EUR 120.5 bn (Source: FESE; 31-May 2016)



Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Sector weightings Czech Republic, PX

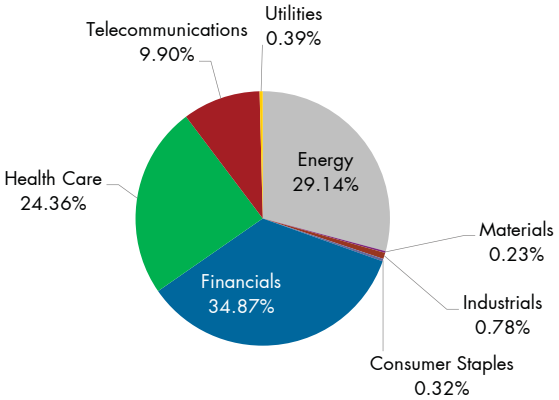
Dom. market cap.: EUR 22.5 bn (Source: FESE; 31-May 2016)



Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Sector weightings Hungary, BUX

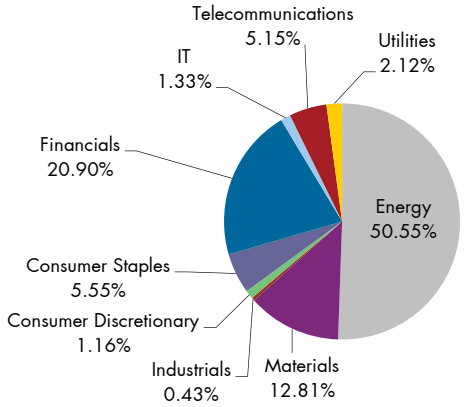
Dom. market cap.: EUR 17.5 bn (Source: FESE; 31-May 2016)



Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Sector weightings Russia, MICEX

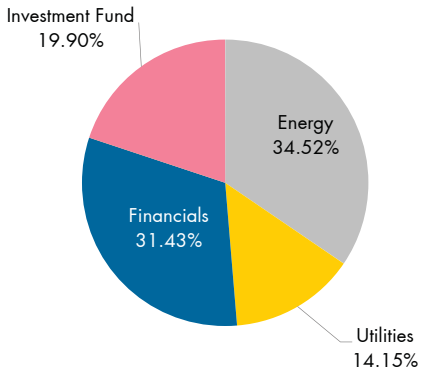
Dom. market cap.: EUR 420.7 bn (Source: WFE; 31-May 2016)



Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Sector weightings Romania, BET

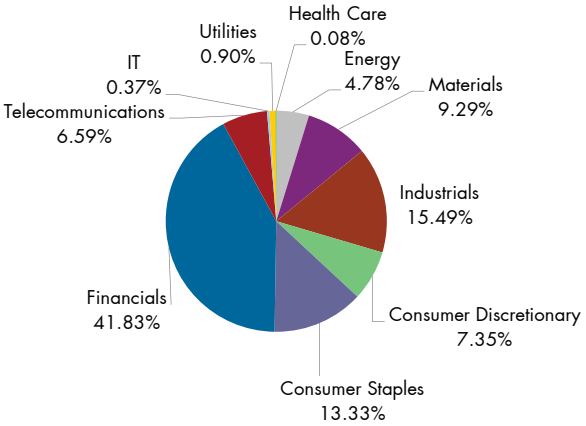
Dom. market cap.: EUR 14.6 bn (Source: FESE; 31-May 2016)



Source: Bloomberg, RBI/Raiffeisen RESEARCH

Sector weightings Turkey, BIST National 100

Dom. market cap.: EUR 179.2 bn (Source: FESE; 31-May 2016)



Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Solid Q2 earnings expected, but Brexit vote triggers uncertainties

- **Brexit vote might increase NIM pressure and FX volatility, but could also have a positive effect on loan growth in the short-term**
- **Poland: still unresolved CHF issue to keep volatility high, Q2 16 results of PL banks might show slightly better P&L quality**
- **Q2 should be characterised by further NIM pressure, but low cost of risk**

After the Brexit vote we see banks in our universe potentially affected via three channels (excluding a general weakening of economic momentum and an increase in equity risk premia). These include (1) a period of protracted low interest rates in the euro area causing further pressure on net interest margins, (2) enhanced FX volatility with potential appreciation risk of CHF impacting FX mortgage lenders and (3) a potential renegotiation of the 2014-2020 EU budget leading to a cut of EU funds with CEE countries having the highest exposure. However uncertainty in this respect might also lead to a short term increase of the take-up rate with positive effects on loan growth.

As we outlined previously, regulatory uncertainty in Poland has been dominating this years stocks performance the Q2 16. In fact, the President's Office presented an updated solution in early June, however, apart from having strong links to the January draft, the lack of details will keep the CHF saga dominating the screens during Q3 16. There was some progress on the M&A front (Alior agreed to buy BPH excl. CHF) and given the latest rumours we could expect more news-flow to come over the summer. The potential change of the BFG law and the discussions around pension funds could come into the spotlight later in Q3.

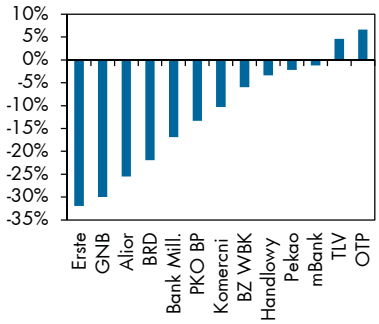
Q2 16 might show only modest earnings improvement compared to the relatively weak Q1 16. Despite one more month of bank tax payments (it was introduced in February) we forecast flattish to slightly growing NII and a recovery of F&CI. Banks are expected to maintain solid cost control and risk provisioning should remain at quite healthy levels. Given the recent performance we would keep Alior Bank and BZ WBK as our favourite names but would overall stay cautious in Poland.

With regard to Erste Group we reckon with further NIM pressure that will only partly be offset by sound loan growth in the Czech Republic, Slovakia and Austria, but still assume that the FY bottom line will be supported by low risk costs. Trading at a 2 year low price/book multiples should provide a reasonable entry level for the stock in the medium term given the improved capitalization and risk profile of the bank. At OTP Q1 figures demonstrated headwinds for core earnings due to intensifying NIM pressure, but a very favourable risk cost environment and finally improving loan dynamics should enable OTP to remain on track towards its 2017 ROE target of >15%.

Romanian banks will start to book provisions for the walkaway law in earnest as part of their Q2 results. While the actual losses are still probably modest, the Central Bank will push for pre-emptive action – but the market should be aware of this. We believe that the BRD share has been more than sufficiently penalised ytd due to this law, hence we expect an outperformance and would prefer it over its main peers due to the significant discount.

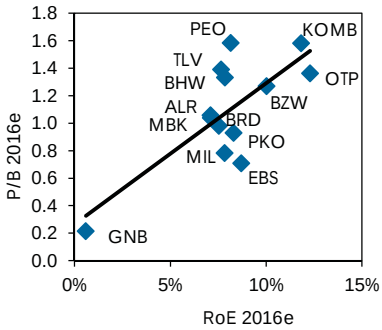
Financial analysts: Jovan Sikimic, Stefan Maxian, CFA

YTD stocks performance (in %)



ytd, incl. 28 June
Source: Bloomberg

P/B - RoE 2016e regression

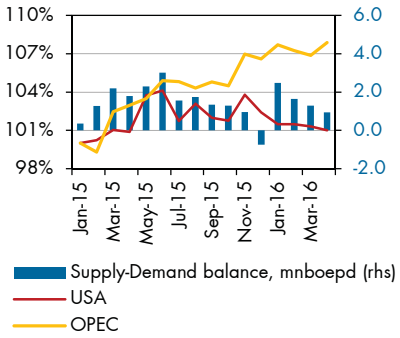


Source: Raiffeisen Centrobank estimates

Oil & gas: Improving supply-demand balance not yet sustainable

- **Price of Brent oil to hover around USD 50/bbl**
- **Downstream players still facing a healthy environment**
- **We favour MOL and PKN and remain bearish on SBO**

USA/OPEC production growth

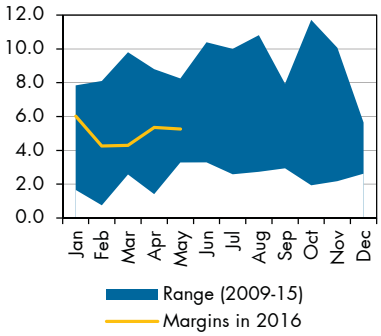


Source: IEA Oil market report

The recent recovery of the oil price (Brent +90% since the year-low level of USD 25.8/bbl) was driven by an improved supply-demand balance. Global oversupply of crude oil decreased from 1.7 mn boepd in 2015 to cca. 1.0 mn boepd in April, according to the International Energy Agency (IEA). This improvement, however, was mainly driven by production outages in Canada (wildfires) and Nigeria/Libya (security issues), which we believe provided only temporary support to the oil price (Canadian output is already coming gradually back).

US producers were the most affected by the depressed level of the oil price. However, the decline of US production YTD (-470 kboepd) was more than offset by additional barrels produced by Iran since the lifting of economic sanctions (+560 kboepd since Jan-16). Therefore, we believe that a sustainable recovery of the oil price should start only when the impact of heavy under-investments in E&P becomes visible. According to Bloomberg consensus, oil majors are projected to cut their 2015-17 annual upstream capex by cca. 30% on average in comparison with 2014 spending. Lower spending to replace oil reserves could translate into a future decline of crude output from currently producing oil fields and thus be supportive for the oil price.

NWE refining margins, USD/bbl



Source: Thomson Reuters

We reckon that in an environment of USD 50/bbl for Brent the downstream players could still face healthy levels of refining and petchem margins. Moreover, the CEE refiners continue to benefit from (i) a wider Brent-Ural spread due to higher availability of crude oil and (ii) healthy growth of motor fuel consumption in the CE markets. Petchem producers are also taking advantage of robust regional demand as well as lack of spare petchem capacities in Europe.

In the current environment we would favour integrated players with strong exposure to downstream (including petchem and retail). In our universe we believe that MOL and PKN have an optimal exposure to benefit from the current market conditions. At the same time, we stay bearish on SBO as we expect global drilling activity to remain weak due to currently frozen investments in E&P.

Financial analyst: Oleg Galbur

Andritz: Attractively valued global player

- **Current share price: EUR 41.0**
- **Target price: EUR 53.0**
- **Market capitalisation: EUR 4,193 mn**

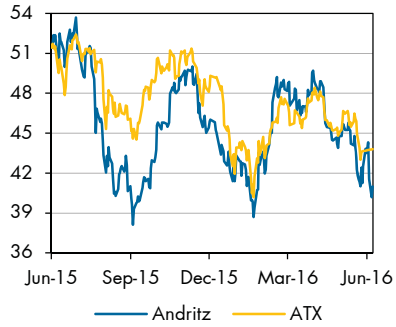
Andritz delivered a good start into the business year 2016, reaping the benefits from a strong order backlog in Pulp&Paper that more than compensated for a weakening metals business as automotive sentiment has deteriorated over the course of the past year. Despite slower sales, EBITA increased by 11% to EUR 107 mn in the seasonally weak first quarter, with profitability on EBITA rather strong at 6.5%. Management expects similar trends for the full year: Sales should decrease slightly, while profitability is to remain at solid levels. Hence, and backed by Q1 results having been in line, we confirmed our FY 16e estimates.

Andritz has negligible exposure to the UK, which accounts for around 1% of revenues, and boasts a diversified global order backlog. Nevertheless, we still decided to eliminate one rather large order for equipping a tidal lagoon project off the Welsh coast worth EUR 250 mn. Earlier this year, we would still have expected it to be booked in 2016, but the current political turmoil and the outstanding decision on its subsidies made us cut our mid-term forecast by around EUR 20 mn, which, however, should be covered by recent acquisitions. We have therefore left our overall forecast fairly unchanged.

We believe that with the current sentiment, Andritz's low exposure to European markets (only 32% of order backlog, 39% of order intake and 37% of sales in Q1 16) adds to the attractiveness in terms of valuation. Andritz trades below its five-year average multiples across the board, while offering stable to increasing earnings as profitability gains should outpace top line weakness. Also, we believe that the dividend payout is about to increase, supporting yields above the 3% mark. So, albeit accounting for an even slower hydropower momentum and having discounted cautious automotive forecasts some time ago already, we believe that Andritz is an attractive investment at our new target price of EUR 53.

Financial Analyst: Teresa Schinwald

Andritz vs. ATX



Andritz: 5y high: 57.5, 5y low: 27.7
ATX: 5y high: 2,811, 5y low: 1,653
Source: Bloomberg

Income statement & balance sheet (IFRS)

in EUR mn	2015	2016e	2017f	2018f
Income statement				
Consolidated sales	6,377	5,962	5,914	5,796
EBITDA	535	533	543	538
EBIT	369	387	395	391
EBT	376	388	404	405
Net profit b.m.	270	280	289	289
Net profit a.m.	268	276	285	285
Balance sheet				
Total assets	5,778	5,754	5,875	5,969
Shareholders' equity	1,198	1,300	1,436	1,561
Goodwill	529	529	529	529
NIBD	-903	-1,099	-1,247	-1,392

Source: Andritz, Raiffeisen Centrobank estimates

Key ratios

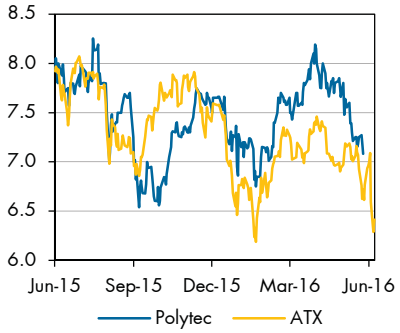
	2015	2016e	2017f	2018f
EPS	2.60	2.70	2.79	2.79
P/E ratio	17.3	15.2	14.7	14.7
Operating CF per share	2.13	5.98	4.29	4.33
Price cash flow	21.2	6.9	9.6	9.5
Book value per share	11.71	12.70	14.03	15.26
Price book value	3.8	3.2	2.9	2.7
Dividend yield	3.0%	3.6%	3.8%	3.9%
ROE	24.1%	22.1%	20.8%	19.0%
ROCE	17.3%	18.1%	17.8%	16.5%
EV/EBITDA	8.0	7.6	7.2	6.9

Source: Andritz, Raiffeisen Centrobank estimates

Polytec: Still in the fast lane

- **Current share price: EUR 7.10**
- **Target price: EUR 9.50**
- **Market capitalisation: EUR 157 mn**

Polytec vs. ATX



Polytec: 5y high: 8.54, 5y low: 5.00
ATX: 5y high: 2,811, 5y low: 1,653
Source: Bloomberg

Polytec is a manufacturer of high-performance plastics components with particular focus on the European car and truck industries. The group produces injection-moulded components and fibre-reinforced plastics parts at 25 plants. It offers the entire value-added chain from development, design and tool manufacturing to production and subsequent processes such as varnishing.

We rate Polytec a "BUY" because the company firstly profits from internal measures as well as acquisitions and secondly capitalises on positive demand trends in Europe. The group's series of good quarterly results warrants particular mention. In the recent past, above all the results for FY 2015 but also for Q1 16 were compelling across the board. We anticipate the solid organic growth to continue this year. As a result of economies of scale in combination with internal efficiency-improvement measures and the turnaround at the Ebensee plant, the group should be able to post increasing results and rising profitability. While Volkswagen group is the most important customer accounting for almost 30% of sales, the results of Polytec underpin the management's statements that "Dieselgate" does not have negative impact on the business performance so far. In addition, Polytec may benefit from the lower oil prices – at least to an extent. We are therefore optimistic that Polytec should generate attractive sales and earnings growth in 2016. Polytec's UK exposure primarily stems from the business with Jaguar/LandRover, which accounts for ca. 8% of sales. While the implications of the Brexit remain to be seen, we assume that luxury OEMs should be more resilient than mass market OEMs. The share displays a low valuation in a peer group comparison and boasts a dividend yield of some 4%.

As regards end-customer markets we can observe a positive picture. The European car market continued its growth path in 2016. After growing 9% in 2015, EU registration figures increased by 10% from January to May. The European truck market gives reason to be optimistic as well: truck registrations (> 16 t) have risen by about 18% ytd.

Financial analyst: Markus Remis, CEFA

Income statement & balance sheet (IFRS)

in EUR mn	2015	2016e	2017f	2018f
Income statement				
Consolidated sales	626	646	672	690
EBITDA	60	62	66	67
EBIT	37	38	39	38
EBT	32	32	33	33
Net profit b.m.	24	24	25	24
Net profit a.m.	24	23	24	24
Balance sheet				
Total assets	485	530	548	561
Shareholders' equity	157	173	191	207
Goodwill	19	19	19	19
NIBD	99	125	123	118

Source: Polytec, Raiffeisen Centrobank estimates

Key ratios

	2015	2016e	2017f	2018f
EPS	1.08	1.05	1.09	1.07
P/E ratio	7.1	6.7	6.5	6.6
Operating CF per share	2.33	1.89	1.89	2.13
Price cash flow	3.3	3.8	3.8	3.3
Book value per share	7.13	7.89	8.67	9.40
Price book value	1.1	0.9	0.8	0.8
Dividend yield	3.9%	4.2%	4.9%	4.9%
ROE	16.0%	14.0%	13.1%	11.9%
ROCE	9.0%	7.9%	7.6%	7.2%
EV/EBITDA	4.6	4.6	4.3	4.2

Source: Polytec, Raiffeisen Centrobank estimates

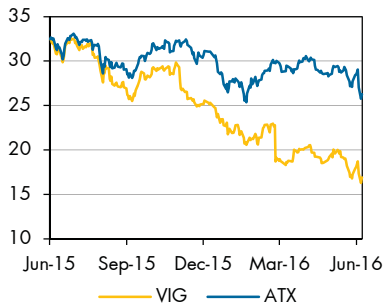
Vienna Insurance Group: Rebound potential

- **Current share price: EUR 16.92**
- **Target price: EUR 22.20**
- **Market capitalisation: EUR 2,171 mn**

While lower yields for a longer period clearly exert a negative impact on the insurance industry, the share performance of approx. -60% since April 2015 implies that the market has already discounted this environment to a large extent. The assumption of a 10/20bp lower total portfolio yield should impact profit before tax by ca. EUR 25 mn/EUR 50 mn based on our calculations.

Q1 16 numbers fully matched RCB and consensus market expectations and are reassuring, in our view, that VIG is on track to reach its FY 16e guidance of PBT in the amount of EUR 345-400 mn, which was reiterated upon the Q1 16 results release. In the set of Q1 16 results we also positively highlight strong other comprehensive income driven by unrealised gains and losses from financial instruments available for sale of EUR 109 mn, lifting BVPS to EUR 37.9 vs. EUR 36.5 in Q4 15. Capitalisation looks robust as the company indicated a Solvency II ratio in excess of 200% applying a partial internal model. The share fell below its tangible book value in March (EUR 20.2 in FY 15, EUR 21.7 as of Q1 16 before going ex-dividend of DPS 15 in the amount of EUR 0.60 in May). VIG shares trade at an about 10% discount on P/E ratio 2016e and 2017f. PBV of 0.5x compares to 0.7x of the European insurance peer group. While above mentioned yield erosion poses a downside risk to our forecasts and still weighs on the sentiment towards insurance stocks our positive stance is also underpinned by the following developments: 1) The MoU between the Republic of Austria and HETA creditors to settle the restructuring of the HETA debt instruments could lead to a write-up of HETA bonds. 2) The management stated in the recent conference call that VIG should face only a very small negative impact from April frost damages in Austria given its limited exposure to crop insurance. 3) Citing company statements we point to restructuring potential as the company refers to opportunities in fields like bundling of services and processes. 4) CEE P&C insurance market dynamics started to pick up in FY 15 which broadly lasted into Q1 16, following robust macro trends.

VIG vs. ATX



VIG: 5y high: 32.91, 5y low: 16.21
ATX: 5y high: 2,811, 5y low: 1,653
Source: Bloomberg

Income statement & balance sheet (IFRS)

in EUR mn	2015	2016e	2017f	2018f
Income statement				
Gross written premiums	9,020	8,942	8,963	9,134
Net earned premiums	8,181	8,123	8,100	8,239
Net investment income	1,000	882	815	802
Insurence benefits net	-6,749	-6,589	-6,523	-6,615
Profit before tax	172	394	420	433
Net profit a.m.	314	285	305	314
Balance sheet				
Total assets	45,148	45,260	46,184	47,186
Shareholders' equity	5,058	5,251	5,277	5,350
Intangible assets	2,080	2,094	2,108	2,123
Investments	30,709	30,741	31,547	32,388

Source: VIG, Raiffeisen Centrobank estimates

Key ratios

	2015	2016e	2017f	2018f
Cost ratio net group	-22.6%	-23.3%	-23.2%	-23.0%
Benefit ratio net group	-82.5%	-81.1%	-80.5%	-80.3%
Combined Ratio	-97.3%	-97.0%	-96.5%	-96.0%
DPS	0.60	0.70	0.80	0.85
Dividend yield	2.4%	4.1%	4.7%	5.0%
EPS adj.	2.45	2.23	2.38	2.46
P/E ratio adj.	10.3	7.7	7.2	6.9
Book value per share	36.5	37.9	37.9	38.4
Price book value	0.7	0.5	0.4	0.4
ROE	6.6%	6.0%	6.3%	6.4%

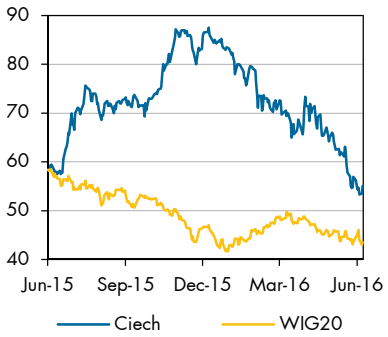
Source: VIG, Raiffeisen Centrobank estimates

Financial analyst: Bernd Maurer, CIIA

Ciech: Attractive multiples, soda ash market still strong

- **Current share price: PLN 55.00**
- **Target price: PLN 85.00**
- **Market capitalisation: EUR 653 mn**

Ciech vs. WIG 20



Ciech 5y high: 87.49; 5y low: 10.83
WIG20: 5y high: 2820.08, 5y low: 1674.57
Source: Bloomberg

Ciech has been a beneficiary of the recent macro trends including the weaker EUR vs. the USD (lower risk of soda ash imports to Europe and higher margins on spot sales of the Romanian subsidiary) coupled with growing demand for soda ash. Lower prices of raw materials are still supportive in 2016 and we expect a moderate growth of input costs to take hold only in the upcoming years. Ciech is attractively priced based on P/E and EV/EBITDA multiples even considering the risk of Turkish soda supply, that may be launched in the second half of 2017. We see the impact of competitors' capacities as priced in at current levels. Also, we would like to stress that Ciech's key clients are located in Northern Europe and that they are supplied by factories in Germany and Poland, where the market impact should be lower compared to the Black Sea basin (Ciech's Romanian subsidiary).

The pricing of soda ash contracts for 2016 was stable with a record-high year expected in the soda business. Q1 16 brought EBITDA of over PLN 200 mn and there are chances for even better quarterly results later this year considering that the full impact of capacity increase will be visible starting from Q2 16e, while the silicates contract with Solvay should support figures in the second half of 2016 and afterwards. Owing to the weak euro and the absence of new capacities in Europe we do not expect that foreign soda will significantly harm European producers in 2016-2017. Following the peak in the capex programme in 2015-2016 (higher capacities of soda ash, energy efficiency, environmentally induced capex, organic segment development), we expect stronger cash flow generation starting from 2017.

Brexit referendum is not likely to have a meaningful direct impact on Ciech's sales (UK exposure at 1% of revenues in 2015). Indirectly, Ciech may suffer from the weaker macro environment, but on the other hand it should benefit from the weaker PLN and the stronger USD.

Financial analyst: Dominik Niszcz, CFA

Income statement & balance sheet (IFRS)

in PLN mn	2015	2016e	2017f	2018f
Income statement				
Consolidated sales	3,273	3,441	3,489	3,467
EBITDA	716	861	849	794
EBIT	498	604	579	523
EBT	277	529	503	458
Net profit b.m.	346	423	413	375
Net profit a.m.	343	423	413	375
Balance sheet				
Total assets	3,910	3,904	4,055	4,010
Shareholders' equity	1,337	1,499	1,742	1,952
Goodwill	62	62	62	62
NIBD	1,341	1,278	1,087	857

Source: Ciech, Raiffeisen Centrobank estimates

Key ratios

	2015	2016e	2017f	2018f
EPS	6.64	8.03	7.83	7.12
P/E ratio	13.2	6.8	7.0	7.7
Operating CF per share	8.74	12.82	12.89	12.23
Price cash flow	7.3	4.3	4.3	4.5
Book value per share	25.38	28.44	33.05	37.05
Price book value	3.4	1.9	1.7	1.5
Dividend yield	3.3%	5.8%	5.7%	5.2%
ROE	29.3%	31.3%	25.5%	20.3%
ROCE	20.5%	17.2%	15.9%	14.2%
EV/EBITDA	8.2	4.8	4.7	4.7

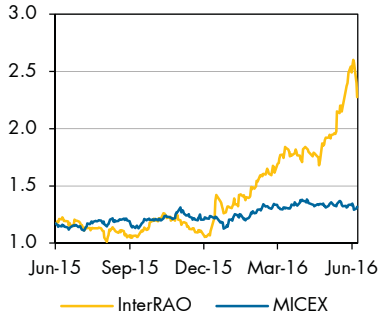
Source: Ciech, Raiffeisen Centrobank estimates

InterRAO: Selling a non-core asset as a stock trigger

- **Current share price: RUB 2.28**
- **Target price: RUB 2.94**
- **Market capitalisation: EUR 3,316 mn**

In May, the company announced that it had reached an agreement with En+ for the sale of a 40% stake in Irkutskenergo for a total cash consideration of RUB 70 bn. We treat the valuation as extremely generous (+85% to the market price prior to the announcement) and therefore consider this deal as a significant positive driver for InterRAO. The transaction value is RUB 70 bn, with the largest portion to be received in Q2 2016f and the rest in several instalments before May 31, 2018. We currently model that the first payment amounts to 70% of the total deal value. The company generates a significant cash inflow (~40% of the market cap of InterRAO before the announcement of the deal) for a non-core asset that many investors did not fully reflect in their valuation of the fair value of the company. However, the company has no real intention to pay generous dividends. Commenting on the potential use of the proceeds of the deal, management stated that a special dividend/switching to interim dividend payments should not be expected as highly probable. At the same time, the company believes that these funds could allow it to better shape itself to pursue its strategy and to target some M&A deals (e.g. in the electricity supply sector).

InterRAO vs. MICEX



InterRAO: 5y high: 4.04, 5y low: 0.65
MICEX: 5y high: 1,914, 5y low: 1,237
Source: Bloomberg

As we treat the comments of the management as quite a strict indication that investors should wait for FY 16e dividends to see the impact of the deal on dividends, we highlight that the value of the deal is significantly above the book value of the stake, which is ~RUB 8 bn under IFRS and ~RUB 16 bn under RAS. This means that the company would reflect the difference (after taxation) on its P&L, and a higher bottom line should lead to more dividends. Nonetheless, since we expect to see InterRAO FCF-positive and ND-negative still in FY 2016f we believe that the company could at least increase its payout as there should be plenty of cash on the balance sheet. We believe that the main risk at the moment is that the funds received could be used for value destructive M&A deals and investors may not see the company sharing the value it generates from the transaction with them.

Financial analyst: Fedor Kornachev

Income statement & balance sheet (IFRS)

in RUB mn	2015	2016e	2017f	2018f
Income statement				
Consolidated sales	805,344	846,327	898,227	939,458
EBITDA	48,438	75,503	82,231	85,891
EBIT	25,460	52,040	58,550	62,658
EBT	26,865	87,179	67,428	76,517
Net profit b.m.	23,936	69,743	53,942	61,214
Net profit a.m.	22,715	67,815	51,190	58,091
Balance sheet				
Total assets	563,239	605,715	619,837	662,509
Shareholders' equity	362,663	428,617	462,854	508,148
NIBD	10,489	-61,040	-110,867	-171,248

Source: InterRAO, Raiffeisen Centrobank estimates

Key ratios

	2015	2016e	2017f	2018f
EPS	0.22	0.65	0.49	0.56
P/E ratio	5.1	3.5	4.6	4.1
Operating CF per share	0.64	1.06	0.85	0.91
Price cash flow	1.7	2.1	2.7	2.5
Book value per share	3.47	4.11	4.43	4.87
Price book value	0.3	0.6	0.5	0.5
Dividend yield	1.6%	7.1%	5.4%	6.1%
ROE	6.4%	17.1%	11.5%	12.0%
ROCE	7.4%	16.3%	11.8%	12.4%
EV/EBITDA	2.1	2.3	1.5	0.7

Source: InterRAO, Raiffeisen Centrobank estimates

Risk notifications and explanations

Warnings

- Figures on performance refer to the past. Past performance is not a reliable indicator for future results and the development of a financial instrument, a financial index or a securities service. This is particularly true in cases when the financial instrument, financial index or securities service has been offered for less than 12 months. In particular, this very short comparison period is not a reliable indicator for future results.
- Performance of a financial instrument, a financial index or a securities service is reduced by commissions, fees and other charges, which depend on the individual circumstances of the investor.
- The return on an investment in a financial instrument, a financial or securities service can rise or fall due to exchange rate fluctuations.
- Forecasts of future performance are based purely on estimates and assumptions. Actual future performance may deviate from the forecast. Consequently, forecasts are not a reliable indicator for future results and the development of a financial instrument, a financial index or a securities service.

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Investment recommendation	Basis: All recommendations for all financial instruments	Basis: Recommendations for financial instruments of all issuers, for which investment banking services were rendered in the last 12 months
Buy recommendations	42.4	59.4
Hold recommendations	29.6	3.1
Sell recommendations	28.0	37.5

Detailed information on recommendations concerning financial instruments or issuers disseminated during a period of 12 month prior to this publication (acc. to Art. 4 (1) h) Commission Delegated Regulation (EU) 2016/958 of 9.3.2016) is available under: https://raiffeisenresearch.com/web/rbi-research-portal/recommendation_history

Corporate Credits

Recommendations history for 12 months

GAZPROM	Start of coverage	17.04.2008
	Date of recommendation	Recommendation
GAZPRU 4.950% due 2022	16/10/2015	Sell
GAZPRU 8.265% due 2034	10/02/2016	Buy
GAZPRU 8.265% due 2034	28/04/2016	Buy

VimpelCom	Start of coverage	28.01.2009
	Date of recommendation	Recommendation
VIP 9.125% due 2018	10/08/2015	Buy
VIP 9.5043% due 2022	28/04/2016	Buy

Bonds

Financial instruments/Company	Date of the first publication
Eurobonds	01/01/2001
LCY bonds	01/01/1997

Recommendations history: Local currency government bonds (I: no change)*

	CZ				HU				PL				RO				RU				TR			
Date of change	2y	5y	10y	CZK	2y	5y	10y	HUF	2y	5y	10y	PLN	2y	5y	10y	RON	2y	5y	10y	RUB	2y	5y	10y	TRY
24/06/2015	Hold	Hold	Buy	Hold	Hold	Hold	Sell	Hold	Hold	Hold	Sell	Hold	Hold	Hold	Sell	Hold	Buy	Buy	Buy	Hold	Sell	Sell	Sell	Sell
06/08/2015	I	I	Hold	I	I	Sell	I	I	I	Sell	I	I	I	Sell	I	I	Hold	Hold	Hold	I	Hold	I	I	Hold
03/09/2015	I	I	I	I	I	I	I	I	I	I	I	I	I	I	I	I	I	I	I	Buy	I	I	I	Buy
22/09/2015	I	I	I	I	I	I	I	I	I	I	I	I	I	I	I	I	I	I	I	I	Sell	I	I	I
04/11/2015	I	I	I	I	Buy	Buy	Buy	I	I	Hold	Hold	I	I	Hold	Hold	I	I	I	I	Hold	Hold	Hold	Hold	Hold
17/12/2015	I	I	I	I	I	I	I	Buy	Buy	Buy	I	I	Buy	Buy	Buy	Buy	Buy	Buy	I	Buy	I	I	I	I
25/01/2016	I	–	Buy	I	Hold	–	I	Hold	I	–	I	I	Hold	–	Hold	I	–	–	–	–	I	–	I	I
11/02/2016	I	–	I	I	I	–	I	I	I	–	I	I	I	–	I	I	Hold	–	Hold	I	I	–	I	I
23/02/2016	I	–	I	I	I	–	I	I	Hold	–	I	I	I	–	I	Hold	I	–	I	I	I	–	I	Buy
24/03/2016	I	–	Hold	I	I	–	I	I	I	–	I	Sell	I	–	I	I	I	–	I	Sell	Sell	–	Sell	Sell
26/04/2016	I	–	I	I	I	–	I	I	I	–	I	Hold	I	–	I	I	I	–	I	I	Hold	–	Hold	I
31/05/2016	I	–	I	I	I	–	I	I	I	–	I	I	I	–	I	I	Buy	–	Buy	Hold	Buy	–	Buy	Hold
20/06/2016	I	–	I	I	I	–	I	I	I	–	I	I	I	–	I	I	I	–	I	I	I	–	I	I

** recommendations based on absolute expected performance in LCY; FX vs EUR; 5y segment not covered anymore; Source: RBI/Raiffeisen RESEARCH*

Recommendations history: Sovereign Eurobonds (I: no change)*

	BG		HR		CZ		HU		KZ		LT		PL		RO	
Date of change	EUR	USD	EUR	USD	EUR	USD	EUR	USD	EUR	USD	EUR	USD	EUR	USD	EUR	USD
24/06/2015	Hold	–	Hold	Hold	Hold	Hold	Hold	Hold	–	–	Hold	Hold	Buy	Hold	Hold	Hold
06/08/2015	I	–	Sell	Sell	I	I	I	I	–	Buy	Buy	I	Hold	I	I	I
03/09/2015	I	–	I	I	I	I	I	I	–	I	Hold	I	I	I	I	I
22/09/2015	I	–	I	I	I	I	Buy	Buy	–	I	I	I	Buy	I	Buy	Buy
04/11/2015	I	–	I	I	I	I	I	I	–	Hold	Buy	I	I	Buy	I	I
03/12/2015	I	–	I	I	I	I	I	I	–	Buy	I	I	I	I	I	I
17/12/2015	I	–	I	I	I	I	I	I	–	I	Hold	I	I	I	I	I
25/01/2016	I	–	Hold	Hold	I	I	Hold	Hold	–	Hold	I	I	I	I	Hold	Hold
23/02/2016	I	–	I	I	I	I	Buy	Buy	–	Buy	I	I	I	I	I	I
17/03/2016	I	–	I	I	I	I	I	I	–	I	I	I	I	I	I	I
24/03/2016	I	–	I	I	I	I	Hold	Hold	–	I	I	I	I	I	I	I
29/03/2016	Buy	–	I	I	I	I	I	I	–	I	Buy	I	I	Hold	I	I
20/04/2016	I	–	I	I	I	I	I	I	–	I	I	I	I	I	I	I
26/04/2016	Hold	–	I	I	I	I	I	I	–	Hold	Hold	I	Sell	Sell	I	I
13/05/2016	I	–	I	I	I	I	I	I	–	I	I	I	I	I	I	I
20/06/2016	Buy	–	Sell	Sell	I	I	Buy	Buy	–	I	I	I	I	I	Sell	Sell

** recommendations based on absolute expected performance, i.e. expected spread change; Source: RBI/Raiffeisen RESEARCH*

Recommendations history: Sovereign Eurobonds (I: no change)*

	RU		RS		SK		SI		TR		UA		BY		MK	
Date of change	EUR	USD	EUR	USD	EUR	USD	EUR	USD	EUR	USD	EUR	USD	EUR	USD	EUR	USD
24/06/2015	Hold	Hold	–	Sell	Hold	–	Buy	–	Buy	Hold	Hold	Hold	-	Buy	Buy	–
06/08/2015	I	I	–	I	I	–	Hold	–	Hold	I	Sell	Sell	-	Sell	Hold	–
03/09/2015	I	I	–	I	I	–	I	–	I	I	Hold	Hold	-	I	I	–
22/09/2015	I	I	–	I	I	–	I	–	Sell	Sell	I	I	-	I	I	–
04/11/2015	Buy	Buy	–	I	I	–	I	–	Hold	Hold	–	I	-	Hold	I	–
03/12/2015	Hold	Hold	–	I	I	–	I	–	I	I	–	Sell	-	I	I	–
17/12/2015	I	I	–	I	I	–	I	–	Buy	Hold	–	I	-	I	I	–
25/01/2016	Buy	Buy	–	I	I	–	Buy	–	I	Buy	–	I	-	I	Buy	–
23/02/2016	I	I	–	Hold	I	–	I	–	I	I	–	I	-	I	I	–
17/03/2016	Hold	Hold	–	I	I	–	I	–	I	I	–	I	-	I	I	–
24/03/2016	I	I	–	I	I	–	I	–	I	I	–	I	-	I	I	–
29/03/2016	I	I	–	I	I	–	I	–	I	I	–	Hold	-	I	I	–
20/04/2016	I	I	–	I	I	–	I	–	I	I	–	I	-	I	Hold	–
26/04/2016	I	I	–	Buy	I	–	I	–	I	I	–	I	-	I	I	–
13/05/2016	I	I	–	I	I	–	I	Buy	Hold	Hold	–	I	-	I	I	–
20/06/2016	I	I	–	I	I	–	I	–	Buy	I	–	I	-	I	I	–

** recommendations based on absolute expected performance, i.e. expected spread change, under revision; Source: RBI/Raiffeisen RESEARCH*

Equities

Recommendations history (I: no change)

Date	MICEX	WIG 30	PX	BUX	BET	CROBEX 10	BIST 100	ATX
2015/06/24	Buy	Hold	Buy	Buy	Buy	Hold	Hold	Buy
2015/08/28	I	I	I	I	I	I	I	Buy
2015/09/04	I	I	I	I	I	I	I	Buy
2015/09/18	Buy	Hold	Buy	Buy	Buy	Buy	Hold	Buy
2015/10/23	I	I	I	I	I	I	I	Hold
2015/12/04	I	I	I	I	I	I	I	Hold
2015/12/16	Buy	Buy	Buy	Buy	Buy	Hold	Buy	Buy
2016/01/29	I	I	I	I	I	I	I	Buy
2016/02/15	I	I	Buy	Buy	Buy	I	I	I
2016/02/26	I	I	I	I	I	I	I	Buy
2016/03/11	I	I	I	I	I	I	I	Hold
2016/03/29	Hold	Hold	Buy	Buy	Buy	Hold	Buy	I
2016/05/27	I	I	I	I	I	I	I	Hold
2016/06/28	Buy	Sell	Buy	Hold	Hold	Hold	Buy	Hold

Equities

Financial instruments/Company	Date of the first publication
MICEX	21/12/2009
WIG 30	08/12/2014
PX	01/06/1994
BUX	01/06/1994
BET	19/12/2006
CROBEX 10	31/07/2009
BIST 100	25/06/2012
ATX	01/04/1993

Equities

Andritz: 5y high: EUR 57.49, 5y low: EUR 27.41

Recommendation history

01/02/2002 (Initiation date)	Rating	Target Price	Prev. day's close	Upside
04/04/2016	Buy	56.00	46.70	19.9%
06/11/2015	Buy	55.00	45.80	20.1%
08/10/2015	Buy	54.00	41.70	29.5%
31/07/2015	Buy	60.00	49.19	22.0%
05/03/2015	Buy	60.00	51.74	16.0%

Polytec: 5y high: EUR 8,541, 5y low: EUR 4,998

Recommendation history

10/08/2007 (Initiation date)	Rating	Target Price	Prev. day's close	Upside
06/04/2016	Buy	9.50	7.58	25.3%
09/11/2015	Buy	9.00	7.31	23.1%
07/05/2015	Buy	10.00	8.35	19.8%

MOL: 5y high: HUF 21,450 , 5y low: HUF 10,710

Recommendation history

01/02/2002 (Initiation date)	Rating	Target Price	Prev. day's close	Upside
01/06/2016	Buy	18,200	15,500	17.4%
19/05/2016	Hold	18,200	16,100	13.0%
29/03/2016	Reduce	15,500	15,850	-2.2%
10/02/2016	Hold	14,000	13,710	2.1%
10/11/2015	Hold	15,000	13,400	11.9%
09/10/2015	Buy	15,000	13,190	13.7%
30/09/2015	Buy	15,000	12,160	23.4%
09/09/2015	Hold	15,000	13,335	12.5%
13/08/2015	Buy	17,600	14,275	23.3%
19/05/2015	Buy	17,500	14,650	19.5%

Ciech: 5y high: PLN 87.49, 5y low: PLN 10.83

Recommendation history

13/11/2007 (Initiation date)	Rating	Target Price	Prev. day's close	Upside
15/03/2016	Buy	85.00	70.26	21.0%
13/10/2015	Buy	83.00	71.60	15.9%
25/08/2015	Buy	79.00	68.60	15.2%
28/05/2015	Buy	65.00	55.98	16.1%

PKN: 5y high: PLN 85.25, 5y low: PLN 32.02

Recommendation history

01/02/2002 (Initiation date)	Rating	Target Price	Prev. day's close	Upside
12/05/2016	Buy	78.00	67.56	15.5%
04/04/2016	Hold	75.00	72.51	3.4%
21/01/2016	Buy	75.50	64.33	17.4%
28/10/2015	Hold	72.00	64.88	11.0%
09/10/2015	Hold	75.00	64.50	16.3%
06/10/2015	Hold	75.00	68.00	10.3%
03/08/2015	Hold	80.00	76.14	5.1%
07/05/2015	Reduce	61.00	66.00	-7.6%

Equities

SBO: 5y high: EUR 95.98, 5y low: EUR 42.005

Recommendation history

01/02/2002 (Initiation date)	Rating	Target Price	Prev. day's close	Upside
05/04/2016	Reduce	47.50	51.70	-8.1%
10/02/2016	Reduce	43.50	45.65	-4.7%
16/12/2015	Reduce	45.00	48.50	-7.2%
09/10/2015	Sell	45.00	58.41	-23.0%
31/08/2015	Reduce	45.00	48.98	-8.1%
23/07/2015	Reduce	48.00	52.00	-7.7%
01/07/2015	Reduce	54.00	54.23	-0.4%
03/06/2015	Reduce	56.00	61.89	-9.5%

Erste Group: 5y high: EUR 37.2, 5y low: EUR 10.645

Recommendation history

01/02/2002 (Initiation date)	Rating	Target Price	Prev. day's close	Upside
12/05/2016	Buy	28.00	23.45	19.4%
05/04/2016	Buy	29.00	24.66	17.6%
18/02/2016	Buy	30.00	25.59	17.2%
07/10/2015	Buy	30.00	25.97	15.5%
17/08/2015	Hold	30.00	28.42	5.6%
17/06/2015	Hold	27.00	25.20	7.1%

OTP: 5y high: HUF 7,380, 5y low: HUF 2,798

Recommendation history

01/02/2002 (Initiation date)	Rating	Target Price	Prev. day's close	Upside
19/05/2016	Hold	7,000.00	6,800.00	2.9%
07/04/2016	Hold	7,000.00	6,890.00	1.6%
23/02/2016	Hold	6,700.00	6,115.00	9.6%
17/06/2015	Hold	5,900.00	5,421.00	8.8%

BZ WBK: 5y high: PLN 422, 5y low: PLN 210

Recommendation history

07/03/2005 (Initiation date)	Rating	Target Price	Prev. day's close	Upside
07/04/2016	Buy	343.00	297.80	15.2%
04/12/2015	Buy	328.00	259.20	26.5%
17/06/2015	Buy	392.00	332.00	18.1%

Alior Bank: 5y high: PLN 99.8, 5y low: PLN 48.23

Recommendation history

23/10/2013 (Initiation date)	Rating	Target Price	Prev. day's close	Upside
07/04/2016	Buy	86.00	69.60	23.6%
25/02/2016	Buy	76.00	61.26	24.1%
04/12/2015	Buy	77.00	65.80	17.0%
17/06/2015	Hold	92.80	87.20	6.4%

BRD-GSG: 5y high: RON 14.48, 5y low: RON 7.125

Recommendation history

06/11/2003 (Initiation date)	Rating	Target Price	Prev. day's close	Upside
07/04/2016	Buy	12.05	10.16	18.6%
23/10/2015	Buy	12.70	10.86	16.9%
17/06/2015	Buy	11.90	10.13	17.5%
14/01/2015	Buy	11.10	9.06	22.5%
21/08/2014	Hold	10.10	8.80	14.8%

Equities

Vienna Insurance Group: 5y high: EUR 42.81, 5y low: EUR 16.795

Recommendation history

06/12/2007 (Initiation date)	Rating	Target Price	Prev. day's close	Upside
25/05/2016	Buy	22.20	19.16	15.9%
22/03/2016	Buy	22.00	18.79	17.1%
26/11/2015	Hold	30.00	26.88	11.6%
27/08/2015	Buy	35.00	28.68	22.1%
27/05/2015	Buy	39.00	34.99	11.5%

Adris: 5y high: HRK 424.7, 5y low: HRK 200

Recommendation history

21/01/2005 (Initiation date)	Rating	Target Price	Prev. day's close	Upside
15/04/2016	Buy	514.00	393.34	30.7%
28/09/2015	Buy	413.00	338.74	21.9%
23/07/2014	Hold	337.00	283.44	18.9%

OMV: 5y high: EUR 39.69, 5y low: EUR 20.07

Recommendation history

01.02.2002 (Initiation date)	Rating	Target Price	Prev. day's close	Upside
15.03.2016	Reduce	23.00	25.05	-8.2%
10.02.2016	Reduce	21.50	22.49	-4.4%
09.10.2015	Hold	25.50	24.59	3.7%
08.10.2015	Hold	25.50	24.37	4.6%
25.08.2015	Buy	25.00	21.16	18.2%
18.08.2015	Hold	25.00	24.04	4.0%
29.05.2015	Hold	27.00	25.77	4.8%

Equities

Wienerberger: 5y high: EUR 17.825, 5y low: EUR 5.532

Recommendation history

01/02/2002 (Initiation date)	Rating	Target Price	Prev. day's close	Upside
04/05/2016	Hold	18.00	16.95	6.2%
04/03/2016	Hold	18.00	16.45	9.4%
13/11/2015	Hold	16.50	14.20	16.2%
21/08/2015	Hold	18.50	16.65	11.1%
20/05/2015	Hold	15.50	15.23	1.8%

Zumtobel: 5y high: EUR 29.89, 5y low: EUR 7.383

Recommendation history

20/09/2006 (Initiation date)	Rating	Target Price	Prev. day's close	Upside
28/04/2016	Hold	13.00	11.79	10.3%
15/04/2016	Hold	12.50	14.85	-15.8%
02/03/2016	Hold	18.50	16.15	14.6%
11/12/2015	Buy	26.50	23.01	15.2%
09/09/2015	Buy	28.00	22.00	27.3%
25/06/2015	Buy	29.50	25.22	17.0%

InterRAO: 5y high: RUB 4.05, 5y low: RUB 0.652

Recommendation history

12.02.2013 (Initiation date)	Rating	Target Price	Prev. day's close	Upside
18.05.2016	Buy	2.94000	1.85200	58.7%
15.02.2016	Buy	1.92000	1.39950	37.2%
08.06.2015	Buy	1.90000	1.15200	64.9%

Coverage universe recommendation overview

Empty	buy	hold	reduce	sell	suspended	UR
Universe	47	59	10	1	11	2
Universe %	36%	45%	8%	1%	8%	2%
Investment banking services	19	26	3	0	3	0
Investment banking services %	37%	51%	6%	0%	6%	0%

Source: Raiffeisen Centrobank, rounding differences may occur

Technical analysis and asset allocation

Financial instruments/Company	Date of the first publication
ATX	15/04/1995
BELEX 15	01/10/1996
BUX	01/10/1996
CROBEX	18/11/2009
MICEX	02/09/2013
PX	15/03/2002
WIG 30	01/10/1996

Technical analysis: Historical recommendations

Date	ATX	BUX	BIST 100	CROBEX 10	MICEX	WIG 30
11/06/2015	NEUTRAL	NEUTRAL	BULLISH	BULLISH	NEUTRAL	BULLISH
25/06/2015	BULLISH	BULLISH	NEUTRAL	BULLISH	BULLISH	NEUTRAL
02/07/2015	BULLISH	BULLISH	NEUTRAL	NEUTRAL	BEARISH	BULLISH
09/07/2015	NEUTRAL	BULLISH	NEUTRAL	NEUTRAL	NEUTRAL	NEUTRAL
16/07/2015	BULLISH	BULLISH	NEUTRAL	BULLISH	BULLISH	BULLISH
22/07/2015	BULLISH	BULLISH	NEUTRAL	BULLISH	NEUTRAL	BEARISH
30/07/2015	NEUTRAL	BULLISH	BULLISH	BULLISH	NEUTRAL	BEARISH
06/08/2015	NEUTRAL	BULLISH	BULLISH	BULLISH	BULLISH	NEUTRAL
11/08/2015	NEUTRAL	NEUTRAL	BULLISH	BULLISH	BULLISH	NEUTRAL
20/08/2015	BEARISH	BEARISH	BEARISH	NEUTRAL	BEARISH	NEUTRAL
26/08/2015	NEUTRAL	BEARISH	NEUTRAL	BEARISH	NEUTRAL	NEUTRAL
03/09/2015	BEARISH	BULLISH	BEARISH	BULLISH	NEUTRAL	BULLISH
10/09/2015	NEUTRAL	BEARISH	BEARISH	BEARISH	NEUTRAL	BULLISH
16/09/2015	BULLISH	NEUTRAL	BULLISH	BEARISH	BULLISH	NEUTRAL
24/09/2015	BEARISH	BEARISH	BEARISH	BEARISH	BEARISH	BEARISH
01/10/2015	BEARISH	BULLISH	BEARISH	BEARISH	BULLISH	BEARISH

Technical analysis: Historical recommendations

Date	ATX	BUX	BIST 100	CROBEX 10	MICEX	WIG 30
08/10/2015	BULLISH	NEUTRAL	BEARISH	BEARISH	BULLISH	BULLISH
14/10/2015	NEUTRAL	NEUTRAL	BULLISH	BEARISH	BULLISH	NEUTRAL
22/10/2015	BULLISH	BULLISH	BULLISH	BULLISH	BULLISH	BULLISH
20/10/2015	BULLISH	BULLISH	BULLISH	NEUTRAL	BULLISH	BULLISH
05/11/2015	BULLISH	BULLISH	BULLISH	BEARISH	BULLISH	BEARISH
12/11/2015	BULLISH	BULLISH	BULLISH	BEARISH	BULLISH	NEUTRAL
18/11/2015	BULLISH	BULLISH	BULLISH	NEUTRAL	BULLISH	NEUTRAL
26/11/2015	BULLISH	BULLISH	BULLISH	NEUTRAL	BULLISH	NEUTRAL
03/12/2015	BULLISH	NEUTRAL	BULLISH	NEUTRAL	NEUTRAL	NEUTRAL
09/12/2015	BEARISH	BULLISH	BEARISH	NEUTRAL	NEUTRAL	BEARISH
14/12/2015	BULLISH	BULLISH	NEUTRAL	NEUTRAL	BULLISH	BULLISH
30/03/2016	BULLISH	BULLISH	BULLISH	BULLISH	BULLISH	BULLISH
29/06/2016	BEARISH	BULLISH	NEUTRAL	BEARISH	NEUTRAL	NEUTRAL

Bullish: Buy, Bearish = Sell

CEE portfolio weightings

	Jul 15	Aug 15	Sep 15	Oct 15	Nov 15	Dec 15	Jan 16	Feb 16	Mar 16	Apr 16	May 16	Jun 16	Jul 16
Stocks	↔	↑	↔	↑	↑	↔	↑	↔	↔	↑	↑	↔	↔
Czech Rep	↑	↑	↑	↑	↑	↑	↑	↑	↑	↔	↔	↑	↑
Hungary	↑	↑	↑	↑	↑	↑	↑	↑	↑	↑	↑	↑	↓
Poland	↓	↓	↓	↔	↓	↓	↓	↓	↓	↓	↓	↓	↓
Russia	↑	↑	↑	↑	↑	↔	↑	↔	↔	↓	↔	↓	↑
Turkey	↓	↓	↓	↓	↓	↓	↓	↔	↔	↑	↔	↔	↔
Croatia	↔	↔	↔	↔	↔	↔	↔	↔	↔	↔	↔	↔	↔
Romania	↔	↔	↔	↔	↔	↑	↑	↔	↔	↔	↔	↔	↔
Bonds	↔	↓	↔	↓	↓	↔	↓	↔	↔	↓	↓	↔	↔
EB USD	↔	↔	↔	↔	↔	↔	↔	↔	↔	↔	↔	↔	↑
EB EUR	↔	↔	↔	↔	↔	↔	↔	↑	↑	↑	↑	↑	↔
LCY	↔	↔	↔	↔	↔	↔	↔	↓	↓	↓	↓	↓	↓
Czech Rep	↔	↔	↔	↔	↔	↔	↔	↔	↔	↑	↑	↔	↔
Hungary	↓	↓	↔	↑	↑	↑	↑	↑	↑	↔	↔	↑	↔
Poland	↔	↔	↔	↑	↑	↑	↔	↓	↓	↔	↓	↔	↓
Romania	↔	↔	↔	↔	↔	↔	↑	↑	↑	↑	↔	↔	↓
Russia	↑	↑	↔	↔	↔	↔	↑	↔	↔	↓	↔	↓	↑
Turkey	↔	↔	↔	↓	↓	↓	↓	↔	↔	↔	↔	↔	↔
Croatia	↔	↔	↔	↔	↔	↔	↔	↔	↔	↔	↔	↔	↔

Date of the first publication 01/01/2006

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VIG	3		

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